VALUE CREATION THROUGH STAKEHOLDER MANAGEMENT: THREE ESSAYS ASSESSING THE EFFECTS OF COMPETITIVE STRATEGIES, ENVIRONMENTAL PERFORMANCE FEEDBACK, AND (INTER)NATIONAL GOVERNANCE INSTITUTIONS

by

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Value Creation Through Stakeholder Management: Three Essays Assessing the Effects of Competitive Strategies, Environmental Performance Feedback, and (Inter)national Governance Institutions

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ABSTRACT

This dissertation is composed of three related yet independent studies, with a consistent theme on stakeholder management and value creation of organizations. Using the instrumental stakeholder theory lens, in Essay 1, I examine how generic competitive strategies influence the link between stakeholder management (SM) and firm financial performance. I develop a framework that highlights the synergistic effects of a differentiation strategy on SM, but also the trade-offs between a cost leadership strategy and SM in their consequences for financial performance. I further propose that for firms pursuing a low cost competitive advantage, secondary SM intensifies the trade-offs between SM and financial performance when compared with primary SM, whereas both primary and secondary SM are likely to improve financial performance for differentiators. Drawing from behavioral theory studies, Essay 2 of my dissertation examines how negative/positive performance feedback (i.e., the negative/positive attainment discrepancy between firms' actual performance and aspirations) with respect to firms' environmental performance can serve as a determinant of firms' subsequent social orientation. I found a U-shaped relationship between negative environmental performance feedback and corporate social performance. I also found an inverted U-shaped relationship between positive environmental performance feedback and firms' social orientation. The results suggest that when firms have extremely poor environmental performance far below aspiration levels, they are more motivated to perform better in addressing social issues, mainly due to legitimacy concerns. On the contrary, as firms' environmental performance is well above aspirations, their motivation to improve social performance will be decreased significantly, partly because their legitimacy is already

secured by the satisfactory environmental performance. Essay 3 examines the relationship between private voluntary governance institutions (via the compliance with the UN Global Compact) and corporate social responsibility (CSR), as well as how public governance (via the quality of national institutions) will condition this relationship. In particular, I argue that the positive impact of the UN Global Compact (UNGC) on CSR is likely to wear off over time. I further propose that national institutions moderate the UNGC-CSR relationship, such that the inverted U-shape between the UNGC and CSR is steeper when national institutions are stronger. The findings in this dissertation have implications for research on stakeholder management and value creation of organizations, CSR, behavioral theory and (inter)national governance institutions.

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INTRODUCTION

Early works in the management field have stressed addressing the needs and interests of broader stakeholder groups rather than merely of stockholders, suggesting that corporate strategic decision-making should take into account the interests of shareholders, employees, customers, suppliers, and the broader community (Andrews, 1980; Freeman and Reed, 1983). However, the role of managing stakeholders for gaining competitive advantage and the centrality of good stakeholder relationships as a key strategic resource have been under-emphasized until recently (Freeman, 2010; Barney, 2018).

Driven by an urge to understand whether doing good (stakeholder orientation or stakeholder management) also leads to doing well (firm financial performance), a large body of work has focused on understanding the ***consequences*** of stakeholder orientation. Building on an instrumental stakeholder perspective, substantial work argued that stakeholder orientation leads to superior performance (Jones, 1995; Barnett, 2007; Agle et al., 2008). Some of the theorized economic benefits accruing from stakeholder orientation are the ability to attract and retain employees (Greening and Turban, 2000; Backhaus, Stone and Heiner, 2002), customer satisfaction and increased demand for products (Luo and Bhattacharya, 2006), ability to attract investors (Johnson and Greening, 1999), availability of critical resources (Wang, Choi and Li, 2008) and risk reduction through reputation capital (Godfrey, 2005). On the other hand, others have argued that there are significant trade-offs between stakeholder orientation and financial performance. Friedman's (1970) simple argument that firms that engage in more socially responsible activities, will incur more costs and hence will have a lower financial performance seems to stand the test of time (Vogel, 2007). Empirical

evidence from hundreds of studies on the relationship between a firm's stakeholder orientation and its financial performance has produced mixed and inconclusive findings (Orlitzky, Schmidt and Rynes, 2003; Margolis, Elfenbein and Walsh, 2009). In **Essay 1** of my dissertation, I test and theorize on the effect of an important boundary condition that the literature has surprisingly underemphasized, namely, a firm's generic competitive strategies. I theorize the critical impact of generic competitive strategies on how stakeholder management (SM) affects financial performance and further based on whether it is focused on primary or secondary stakeholders.

Compared to the body of work examining the consequences of stakeholder orientation, only a few studies have begun to examine the ***antecedents*** of stakeholder orientation. A better understanding of the antecedents is important given the substantial heterogeneity in the stakeholder orientation of firms witnessed in the real world, both across industries as well as within industries. Some of the key factors identified by extant work explaining the differences in stakeholder orientation across firms include stakeholder pressures (Brammer and Millington, 2008), national culture (Lenssen et al., 2007), nation-level institutions (Ioannou and Serafeim, 2012), corporate governance (Johnson and Greening, 1999; Jo and Harjoto, 2012), integrative complexity of top management teams and decentralization of decision making (Wong, Ormiston and Tetlock, 2011), or board reputation (Mallin and Michelon, 2011). In **Essay 2** and **Essay 3** of my dissertation respectively, I propose and test two important antecedents of stakeholder orientation ignored by prior work, namely, environmental performance feedback and the interplay between transnational and national institutional influences.

Research Gaps, Motivation, and Research Questions

Essay 1. Instrumental stakeholder theory posits that adherence to stakeholder orientation can be synergistic with the achievement of conventional corporate performance objectives (Donaldson and Preston, 1995). Effective stakeholder management, ranging from workplace diversity and employee relations to product quality, community development and natural environment, is likely to generate competitive advantages (Richard, 2000; Hart and Ahuja, 1996; Russo and Fouts, 1997; Hillman and Keim, 2001; Ruf, Muralidhar, Brown, Janney and Paul, 2001; Luo and Bhattacharya, 2006; Choi and Wang, 2009). Taking good care of stakeholders' demands and interests allows firms to win trust and support from stakeholders, and strengthen the firms' cooperation with different stakeholders, which in turn contributes to better financial performance. However, extant work in strategy has not still explicitly considered the potential downside (i.e., costs) of stakeholder management, failing to explain clearly whether and under what conditions the benefits of developing and maintaining stakeholder relations may outweigh or be offset by the costs (Jones, Harrison and Felps, 2018). In particular, our understanding of how a firm's competitive strategies influence the link between stakeholder management and firm financial performance is still quite limited (Berman, Wicks, Kotha and Jones, 1999; Sharma and Starik, 2002). This is surprising because the very discipline of strategic management is built on the foundation that firm competitive advantages generated by their competitive strategies primarily explain the differences in firms' financial performance.

Based on the assumption that good stakeholder relations do not always lead to improved firm performance, in Essay 1, I examine the joint effects of stakeholder strategy

and generic competitive strategies (Porter, 1980, 1985) on firm financial performance. One key premise is that stakeholder and competitive strategies do not work separately, but rather jointly, to drive firm performance (Freeman, 1984; Baron, 2003; Coda, 2012; Zollo et al., 2018). Using the instrumental stakeholder theory lens, I examine how generic competitive strategies influence the link between stakeholder management (SM) and firm financial performance. I develop a framework that highlights the synergistic effects of a differentiation strategy on SM, but also the trade-offs between a cost leadership strategy and SM in their consequences for financial performance. I test the theoretical mechanism further by distinguishing between primary and secondary stakeholders, who differ in their degree of firm specificity and instrumentality. I propose that for firms pursuing a low cost competitive advantage, secondary SM intensifies the trade-offs between SM and financial performance when compared with primary SM, whereas both primary and secondary SM are likely to improve financial performance for differentiators.

Essay 2. Corporate social responsibility (CSR) involves corporate activities and practices oriented to address both social and environmental issues raised by stakeholders, in order to create the broader social welfare. Although social and environmental responsibility are closely related, they are quite different. Nevertheless, prior studies usually combine environmental and social orientation of firms under the general rubric of CSR, neglecting the differences between them (Bansal, Gao and Qureshi, 2014). Because of its significant reliance on technology and innovation, environmental orientation requires more long-term expenses and costs involved in scientific pursuit and technological input. To some extent, it tends to be more difficult or 'technical' for firms to pursue environmental practices than

addressing social issues, such as philanthropic donations, supporting community development, and maintaining employee relations, etc. There is not much work that separates firms' stakeholder orientation into social and environmental dimensions, or empirically examines why firms respond differently to stakeholder demands. The determinants of the heterogeneity in stakeholder orientation among firms in different situations and the motivation for firms to engage in stakeholder management are under-explored. To advance stakeholder management research, we need to understand not only the outcomes of stakeholder orientation but also why firms pursue stakeholder management in the first place. Based on assumptions of the behavioral theory of the firm (BTOF), the heterogeneity in stakeholder orientation among firms may result from the different evaluation and interpretation of performance attainment discrepancy relative to the firms' aspirations (or goals). As firms assess their goal achievement relative to the reference point, they adjust their subsequent orientations and actions (Cyert and March, 1963; Levinthal and March, 1981).

Essay 2 of my dissertation examines how negative/positive performance feedback (i.e., the negative/positive attainment discrepancy between firms' actual performance and aspirations) with respect to firms' environmental performance can serve as a determinant of firms' subsequent social orientation. This research is motivated by the recent calls for the need to distinguish between corporate environmental and social practices in the CSR literature, as firms' investment in environmental issues tend to be more technical than dealing with social issues. To understand how and why environmental performance feedback (below or above aspirations) may impact firms' subsequent social orientation, I offer a behavioral theory explanation for the heterogeneity in organizations' interpretation and responsiveness to

failed and achieved environmental performance goals. In particular, I propose a U-shaped relationship between negative environmental performance feedback and corporate social performance. I also predict an inverted U-shaped relationship between positive environmental performance feedback and firms' social orientation. That is, when firms have extremely poor environmental performance far below aspiration levels, they are more motivated to perform better in addressing social issues, mainly due to legitimacy concerns. On the contrary, as firms' environmental performance is well above aspirations, their motivation to improve social performance will be decreased significantly, partly because their legitimacy is already secured by the satisfactory environmental performance.

Essay 3. On the one hand, country-level characteristics, such as national institutional arrangements and the quality of state governance, shape firms' CSR-related practices, the content of CSR programs involving multi-stakeholder management, and engagement to address ESG (Environmental, Social, and Governance) related issues (Maignan and Ralston, 2002; Campbell, 2007; Matten and Moon, 2008; Ioannou and Serafeim, 2012). On the other hand, the growth of international private governance institutions such as the UN Global Compact (UNGC), which is also called global corporate codes, private business codes, or civil regulations, is increasingly assumed to shape firms' CSR efforts and stakeholder performance through enhanced reputation and stakeholder support (Cetindamar, 2007; Ortas et al., 2015). Private governance institutions constitute a critical component of global business regulations whose legitimacy and enforcement are not rooted in public authority, which is also known as the governance and regulatory institutions of international business that occur through private, voluntary, non-state business codes (Vogel, 2008, 2010). Although

the UNGC is the world's largest and most widely adopted voluntary codes, conclusions about its efficacy in shaping corporate responsible practices remain elusive. Moreover, there is limited empirical evidence on dynamic effects of the UNGC adoption over the long run, and we know little about how the UNGC is interrelated to state-based institutions to shape firms' CSR practices.

Essay 3 of my dissertation investigates the differences in CSR performance among firms, particularly among those who are participants in international voluntary codes (i.e., the UN Global Compact). No prior work has systematically examined the independent and joint influences of international and national institutions on firms' CSR. Further, existing studies have not yet compared the global impact of the UNGC among firms from different regulatory contexts, based on a comprehensive, longitudinal dataset using an international sample. Particularly, few insights have been provided regarding firms from emerging markets or from countries with weak governance institutions. The lack of systematic, empirical evidence with respect to the link between the UNGC, national institutions, and their implications for corporate stakeholder performance in different situations motivates this study to provide a fresh perspective on the dynamic impact of the UNGC on global firms over time, how well it works, and under what conditions it plays a significant role in shaping firms' CSR. In Essay 3, I argue that the positive impact of the UN Global Compact (UNGC) on CSR is likely to wear off over time. I further propose that global voluntary governance codes (i.e., the UNGC) will interact with national governance institutions to shape firms' stakeholder orientation. Specifically, national institutions positively moderate the non-linear (inverse U-shape) relationship between the UNGC adoption and CSR, such that at both sides of the inverted

U-shape, the effect of the UNGC adoption on CSR is enhanced as national institutional quality increases.

Empirical Setting and Data Sources

The empirical evidence for my dissertation comes from a comprehensive sample of listed companies across all industries from both developed and emerging markets that have available ESG information, which is identified from Thomson Reuters Eikon database and then merged with other data sources. In **Essay 1**, the empirical analysis is based on a panel dataset of S&P 500 firms over a fifteen year period (2005 to 2019). In **Essay 2**, my hypotheses testing is based on panel data analyses on a global sample of 6,659 listed firms across all industries from 72 countries from 2004 to 2019. In **Essay 3**, the main analyses rely on a multi-industry panel data sample of 5,813 listed firms from 62 countries during 2004-2019. Overall, in my dissertation, I utilize a comprehensive sample covering over fifteen/sixteen years, which is one of the longest duration datasets among the stakeholder management studies. Further, few empirical research on stakeholder management has used a dataset of more than 60 countries.

Thomson Reuters Eikon database is one of the most comprehensive secondary data sources for Environmental, Social and Governance (ESG) information used by previous research on stakeholder management/orientation. Eikon tracks more than 400 ESG metrics to assess and compare a company's ESG commitment and effectiveness across ten major themes (such as emissions, environmental innovation, workforce, product responsibilities, human rights and so on) based on the companies' own ESG disclosure and other data sources such as NGO websites, stock exchange filings, and news sources etc. Thomson Reuters ESG scores

and assessment items cover a comprehensive set of stakeholder categories like employee relations, customer satisfaction, partnerships with suppliers, interaction with local communities, and concerns for the natural environment, etc. I also draw accounting and financial information from Thomson Reuters Eikon, complemented by Compustat Global and Compustat North America reports, such as firm size, firm age, slack, financial leverage, R&D intensity, advertising intensity, and industry competition. Data on firms' adherence to the UNGC program is from the United Nations Global Compact Initiative (UNGCI) reports. Corporate social irresponsibility (CSI), corporate violations of the UNGC principles, and negative CSR events are retrieved from the RepRisk databases. Country institution and governance quality variables are drawn from the World Bank's datasets on Worldwide Governance Indicators (WGI). Country competitiveness variables are taken from the Global Competitiveness Index provided by World Economic Forum. Variables, measures, and estimation approaches are described in the Methodology section, and empirical findings are presented and interpreted in the Results and Discussion sections, of each paper.

Contributions

The three papers are essentially interrelated and have implications for both theory and practice. The **first paper** enhances the understanding of whether and under what conditions good stakeholder relations (aiming to create value for all stakeholders) will help firms improve financial performance (i.e., value appropriated by shareholders), by analyzing the interplay between stakeholder and competitive strategies. I theorize the critical influence of generic competitive strategies on how stakeholder management (SM) impacts financial performance and further based on whether it is focused on primary or secondary stakeholders.

Put together, the theory highlights not only 'when SM pays', but also 'when SM may *not* pay'. This paper extends prior works on the interaction between stakeholder and competitive strategies (e.g., Berman et al. 1999) by examining not only when the interaction effects are positive but also when they are negative, and further by disentangling the distinct performance effects of primary and secondary SM. This study thus adds to the literature on the 'contingencies' of the SM-performance link (e.g., Garcia-Castro and Francoeur, 2016) by examining the contingent role of competitive strategies and their differential effects on primary and secondary SM. While SM may create overall value for stakeholders, understanding when it may have negative financial consequences is also important, as CEOs and the top management teams are primarily held accountable for a firm's financial performance. Empirically, this study offers rigorous, large sample evidence using fifteen-year longitudinal data and addresses the multiple sources of endogeneity that afflict many stakeholder studies (Barnett and Salomon, 2012; Liu et al., 2021).

Drawing on the behavioral theory of the firm (BTOF), the **second paper** highlights some important drivers of stakeholder engagement and the heterogeneity in firms' stakeholder orientation. First, I offer a behavioral explanation for why and how firms are motivated to change or improve future social performance in response to negative/positive environmental performance feedback. Integrating behavioral theory and CSR research, this study goes beyond examining whether external institutional or stakeholder pressures drive firms' stakeholder orientation to examine how firms' environmental performance against aspiration levels can serve as an internal motivation for improving future social performance. Second, this paper contributes to CSR literature by advancing the theory on discrimination

between social and environmental responsibility. My empirical analyses not only show a distinction, but also a potential trade-off, between firms' engagement with social and environmental practices. Third, I extend behavioral research by examining how larger discrepancies in performance goals will affect firms' interpretation and responses to feedback about environmental performance beyond economic concerns. Empirically, this research demonstrates that environmental performance far below/above aspirations (i.e., larger discrepancies) will trigger firms to change their search behaviors significantly in terms of future social orientation, compared to smaller discrepancies.

Through analyses of the international participants of the UN Global Compact (UNGC), the **third paper** offers insights about how global voluntary governance codes will interact with national governance institutions to constrain or foster firms' CSR and hence stakeholder value creation. This paper contributes to literatures on international business (IB), CSR, and institutional theory in several ways. First, this study not only enhances our understanding of institutional drivers of firm behavior by resolving the contradictory propositions on the effectiveness of the UNGC, but also goes beyond testing institutional drivers of corporate conduct to examine the interplay between national governance institutions and private business regulations like the UNGC. It contributes by providing nuanced theoretical mechanisms of the diminishing returns to the adoption of voluntary initiatives. This study builds on and advances the institutional theory by studying the interdependence of national and transnational governance institutions, as well as their relative efficacy in facilitating corporate responsible behaviors. Second, this study contributes to the IB literature by highlighting that private governance (the UNGC) can differentially

complement the effects of national institutions in different situations, which might lead to the regulatory heterogeneity across global markets. Empirically, this research is among the first few studies that provide rigorous empirical evidence through an international sample of over sixteen years and by addressing various endogeneity issues associated with the UNGC-CSR link.

Taken together, my dissertation will shed light on whether, when, how, and why stakeholder management strategies matter to firms' value creation, by studying the antecedents, consequences, contingencies and heterogeneity of stakeholder orientation. The different value creation potential of stakeholder-based and business strategies bundles influences firms' sustainable competitive advantage and long-term success, as well as firms' legitimacy and credibility in the eyes of various stakeholders domestically and internationally. Accordingly, such firm-stakeholder interactions affect firms' subsequent motivation for managing relationships with multiple stakeholders, which in turn may sustain a virtuous circle among firms, their stakeholders and the society.

ESSAY #1: WHEN DOES IT (NOT) PAY TO BE GOOD? INTERPLAY BETWEEN STAKEHOLDER AND COMPETITIVE STRATEGIES

ABSTRACT

Using the instrumental stakeholder theory lens, I examine how generic competitive strategies influence the link between stakeholder management (SM) and firm financial performance. I develop a framework that highlights the synergistic effects of a differentiation strategy on SM, but also the trade-offs between a cost leadership strategy and SM in their consequences for financial performance. I test the theoretical mechanism further by distinguishing between primary and secondary stakeholders, who differ in their degree of firm specificity and instrumentality. I propose that for firms pursuing a low cost competitive advantage, secondary SM intensifies the trade-offs between SM and financial performance when compared with primary SM, whereas both primary and secondary SM are likely to improve financial performance for differentiators. Empirical analyses using a panel dataset of S&P 500 firms over a fifteen year period (2005 to 2019) and a series of robustness tests support my predictions. The findings highlight important boundary conditions for SM's impact on firms' financial performance and highlight not only 'when SM pays' but also 'when SM may *not* pay'.

Keywords: competitive strategies; financial performance; stakeholder management; primary and secondary stakeholders

When Does it (not) Pay to be Good? Interplay between Stakeholder and Competitive Strategies

INTRODUCTION

> "The fall from favour of Danone's purpose-driven chief. Ousting of Emmanuel Faber underlines the challenge of pursuing profits and ESG goals".
>
> - Financial Times, March 16 2021

The past decade with its unprecedented challenges has brought into sharp focus the tension between achieving social and financial ends for businesses (Financial Times, 2021; Lynn, 2021). Adam Smith's observation that "the candidates for fortune too frequently abandon the paths of virtue; for unhappily, the road which leads to the one, and that which leads to the other, lie some times in very opposite directions" (Smith, 1776/1976: 63) rings true to this day. There is a renewed scholarly interest to move beyond "inductive moral empiricism" and a futile search for "universally applicable findings" (Lynn, 2021: 521-523; Margolis & Walsh, 2003; Wang, Dou, & Jia, 2016) and examine contingencies to better understand 'when does it (not) pay to be good'. The recent ouster of Danone CEO Emmanuel Faber (Financial Times, 2021) highlights the need and urgency for research that underlines the potential trade-offs (Vogel, 2005).

Stakeholder theory has been quite valuable in providing a theoretical basis for this inquiry (see reviews by Laplume, Sonpar & Litz, 2008; Parmar, Freeman, Harrison, Wicks, Purnell & de Colle, 2010; Wang, Gibson & Zander, 2020). Within stakeholder theory, an instrumental variation[1] (Jones, 1995; Donaldson & Preston, 1995; Jensen, 2002) has identified a number of boundary conditions for stakeholder management[2] (hereafter SM) to be associated with higher financial performance and shareholder value (Russo & Fouts, 1997;

Sharma & Starik, 2002; Wang & Choi, 2013; Dixon-Fowler, Slater, Johnson, Ellstrand, & Romi, 2013; Garcia-Castro & Francoeur, 2016; Kim, Kim, & Qian, 2018). Within this stream, there is a growing interest in understanding how the competitive strategies pursued by firms influence the financial consequences of SM (Zollo, Minoja, & Coda, 2018; Barney, 2018). Berman, Wicks, Kotha and Jones (1999) is one of the earliest studies to explore the interaction effects of competitive strategies and SM using data from 81 US firms. Asking whether stakeholder commitment is intrinsic or instrumental, their study reports evidence for some significant interaction effects between different types of strategies and stakeholder relationships. More recent work (Zollo et al., 2018; Barney, 2018) has theorized why certain combinations of competitive, growth and SM strategies have the potential for creating higher financial value, though these arguments have not been empirically tested yet. This paper adds to this line of enquiry by theorizing and testing how a firm's generic competitive strategies – low cost and differentiation - influence the financial value addition potential of SM. My goal is to examine not only when the interaction effects between competitive strategies and SM is likely to be positive, but also when they could be negative. In addition, building on research that highlights stakeholder heterogeneity (Hillman & Keim, 2001; Garcia-Castro & Francoeur, 2016), I explore how such heterogeneity influences the interaction between SM and competitive strategies. Specifically, I address the questions - (a) when is SM likely to be synergistic with competitive strategy and when is it likely to involve trade-offs or negative synergies (b) how do these effects differ between primary and secondary stakeholders - and provide rigorous empirical evidence for these effects.

Building on instrumental stakeholder theory (Donaldson & Preston, 1995; Jones,

1995), I theorize that there are indeed trade-offs between SM and a firm's financial performance when firms pursue competitive advantages based on a low cost strategy, whereas SM offers synergies and strengthens financial performance when firms pursue a differentiation strategy. SM involves higher costs (Garcia-Castro & Francoeur, 2016; Jones et al., 2018) and the inherent logic of a low cost-based competitive advantage (translated into low prices) makes it difficult to pass them on to the customers. Hence, a simultaneous pursuit of SM and a cost-based competitive advantage is likely to weaken financial performance. On the other hand, a differentiation advantage, with its focus on fulfilling the unique needs of customers, brand building and eliciting a higher willingness to pay from customers (and a premium pricing strategy), has a synergistic effect on SM and improves financial performance. Further, I disaggregate SM into two components – based on its focus on primary and secondary stakeholders, who differ in their degree of instrumentality for financial value addition (Jones, 1995; Clarkson, 1995; Garcia-Castro & Francoeur, 2016)[3]. I propose that secondary SM intensifies the trade-offs between SM and financial performance when compared with primary SM for firms with cost-based competitive advantage. However, firms with a differentiation advantage are able to derive synergistic benefits from both primary and secondary SM as they are able to recover the higher costs of secondary SM through their ability to command premium prices.

I test the predictions using a longitudinal panel dataset of S&P 500 firms from 2005 to 2019 (fifteen years)[4] with 5,032 firm-year observations. The findings indicate that SM combined with a differentiation advantage boosts financial performance both directly and in the case of primary and secondary SM. For cost leaders, I do not find evidence for a direct

negative effect of SM on financial performance. However, I find that a combination of secondary SM and cost-based competitive advantage negatively affects financial performance, whereas primary SM has a positive effect. This finding indicates that, for cost leaders, the negative effect of secondary SM could be cancelling the positive effect of primary SM, thereby resulting in an overall insignificant effect. I perform several robustness checks, as well as Heckman-2SLS models that combine two-stage Heckman selection method with the two-stage least squares instrumental variable (2SLS IV) models (Liu, Shao, De Sisto & Li, 2021), to corroborate my results.

This paper makes important theoretical and empirical contributions to the stakeholder literature with instrumental focus. I theorize the critical influence of generic competitive strategies on how stakeholder management impacts financial performance and further based on whether it is focused on primary or secondary stakeholders. Put together, the theory highlights not only 'when SM pays', but also 'when SM may *not* pay'. I extend prior work on the interaction between stakeholder and competitive strategies (e.g., Berman et al. 1999) by examining not only when the interaction effects are positive but also when they are negative, and further by disentangling the distinct performance effects of primary and secondary SM. This study thus adds to the literature on the 'contingencies' of the SM-performance link (e.g., Garcia-Castro & Francoeur, 2016) by examining the contingent role of competitive strategies and their differential effects on primary and secondary SM. While SM may create overall value for stakeholders, understanding when it may have negative financial consequences is also important, as CEOs and the top management teams are primarily held accountable for a firm's financial performance[5]. Empirically, this study offers rigorous, large sample evidence

using fifteen-year longitudinal data and addresses the multiple sources of endogeneity that afflict many stakeholder studies (Barnett & Salomon, 2012; Liu et al., 2021).

In the next section, I describe the theory and develop the hypotheses. I then describe my data and methods and report the empirical findings. I conclude by discussing the results and by highlighting the key implications and limitations of this research.

THEORY AND HYPOTHESES

Strategy and Stakeholder Management

Quest for sources of sustainable competitive advantage and performance variance among organizations defines the field of strategic management (Rumelt et al., 1991). This search for the determinants of sustainable superior performance has generated a large body of research over the years that emphasizes the importance of generic competitive strategies and valuable resources, routines and capabilities (Porter, 1980, 1985; Miller, 1988; Barney, 1991; Spanos & Lioukas, 2001; Rivard, Raymond, & Verreault, 2006). Developing and sustaining a distinct competitive advantage stemming from low cost or differentiation results in superior rents and financial performance (Dess & Davis, 1984). Such competitive advantages are generated and sustained by valuable and inimitable resources and capabilities (known as resource-based view), which also serve as sources of growth for firms (Penrose, 1959; Barney, 1991).

Though the stakeholder concept has its origins earlier (Rhenman & Stymne, 1965; Carroll, 1979; Markley & Harman, 1982), Freeman (1984) is arguably the first to fully articulate a stakeholder theory and its relevance to strategic management. Despite the original strategic focus, a section of stakeholder research subsequently has argued for stakeholders to be viewed as ends in themselves and not as means to an end (Goodpaster, 1991; Laplume et

al., 2008; Weitzner & Deutsch, 2019). An instrumental approach (Jones, 1995; Donaldson & Preston, 1995) forms the foundation for most strategy research given the field's core focus on achieving superior firm performance (Barney, 2018; Jones et al., 2018; Bridoux & Stoelhorst, 2016; Freeman, Harrison, Wicks, Parmar, & De Colle, 2010; Harrison, Bosse, & Phillips, 2010). Effective stakeholder management (SM), which refers to "management practices that reflect awareness of and response to the legitimate concerns of the multiple constituencies of the corporation" (Post, Preston, & Sauter-Sachs, 2002: 20), is likely to generate competitive advantages and hence superior financial performance (Richard, 2000; Hart & Ahuja, 1996; Russo & Fouts, 1997; Hillman & Keim, 2001; Porter & Kramer, 2006; Luo & Bhattacharya, 2006; Choi & Wang, 2009; Harrison et al., 2010).

Prior research has suggested a number of pathways by which SM generates value for all stakeholders, including shareholders (Hillman & Keim, 2001; Laplume et al., 2008). Good stakeholder relationships are a valuable resource that can help firms achieve and sustain a performance advantage (Choi & Wang, 2009) and enhance a firm's capacity to generate shareholder wealth over time (Post et al., 2002). By avoiding opportunistic relationships and building trust with stakeholders (Heugens, Van Den Bosch & Van Riel, 2002), a firm is able to gain stakeholder loyalty, positive reciprocation and key information and knowledge held by stakeholders (Harrison et al., 2010; Jones et al., 2018). Improved stakeholder relations also help firms reduce firm risks and transaction costs (Ortiz-de-Mandojana & Bansal, 2016; Post et al., 2002; Jones et al., 2018). Among the stakeholders, primary stakeholders (such as employees, suppliers, customers and shareholders), characterized by more firm-specific relationships, are likely to generate more value and are associated with superior financial

performance when compared to more widely defined stakeholder groups (i.e., secondary stakeholders) (Hillman & Keim, 2001; Garcia-Castro & Francoeur, 2016). For multinational firms, stakeholder-based strategies are likely to mitigate the liabilities of distance and foreignness when expanding internationally (Marano, Tashman, & Kostova, 2017). Put together, this body of work has been able to highlight the critical role of stakeholders in the various stages of the value creation process and the likelihood of SM to be associated with an improved financial performance, though the empirical evidence on this link has been mixed (Laplume et al., 2008).

Costs of SM and the Contingent Effect of Competitive Strategies

Recent SM research has underlined its costs and the specific 'contexts' (Jones et al., 2018: 380) and 'contingencies' (Garcia-Castro & Francoeur, 2016: 410; Lynn, 2021) when the costs of SM could outweigh the benefits. Highlighting a 'sunny-side bias' displayed by the field (Jones et al., 2018: 372), this work stresses the need to pay more attention to the costs of developing stakeholder relationships along with their benefits (Barnett & Salomon, 2006; Harrison & Bosse, 2013; Garcia-Castro & Francoeur, 2016). Some key contingencies and boundary conditions identified by prior research include geographic and institutional context (Wang & Qian, 2011; Marano et al., 2017; Gupta, Crilly & Greckhamer, 2020), industry factors (Russo & Fouts, 1997; Baird, Geylani & Roberts, 2012; Garcia-Castro & Francoeur, 2016), firm innovation (Hull & Rothenberg, 2008; Garcia-Castro & Francoeur, 2016), type of stakeholder relationships (Barnett, 2007; Bridoux & Stoelhorst, 2014; Jones, Felps & Bigley, 2007; Jones et al., 2018) and stakeholder synergies (Tantalo & Priem, 2016).

The generic competitive strategies pursued by a firm constitute one such important

contingency determining SM's effect on financial performance (Berman et al., 1999; Zollo et al., 2018)[6]. Competitive strategies pursued by different firms can be captured parsimoniously by the two generic strategy categories: differentiation and cost leadership (Porter, 1980, 1985). A differentiation strategy involves creating a competitive advantage by providing unique and distinctive products or services for customers, thus creating demand inelasticity and a higher willingness to pay; whereas a cost leadership strategy aims to achieve the lowest cost position in the industry through cost efficiencies and create an advantage for customers through low prices (Miller, 1988; Brandenburger & Stuart, 1996). Given that the value creation and capture process is distinct for different competitive strategies, the financial consequences of high stakeholder management would be different for firms pursuing different competitive strategies.

Berman et al. (1999) was one of the first studies to present empirical evidence on these arguments even though the focus of this study was on testing the instrumental versus normative models of stakeholder orientation. Using data from 81 US firms, this study reports some significant interaction effects between various stakeholder relationships and competitive strategies without delving into possible trade-offs. In a recent conceptual paper, Zollo et al. (2018) identify bundles of competitive, growth and stakeholder strategies that are likely to create higher value for all stakeholders. Specifically, they argue that a combination of integrated stakeholder strategy with differentiation advantage and arms-length stakeholder strategy with low cost advantage creates higher value. In another conceptual paper, Barney (2018) underlines the critical link between all stakeholders by arguing that without nonshareholder stakeholders providing the resources needed to generate economic profits,

there will be no superior rents for shareholders.

This paper seeks to integrate this prior work on the joint effects of competitive and stakeholder strategies with a focus on both positive as well as negative synergies and provide rigorous empirical evidence for these effects. Specifically, I examine when competitive strategy is likely to have a synergistic effect with SM to improve financial performance (as in the case of differentiation strategy) and when it is likely to result in trade-offs thereby undermining financial performance (as in the case of cost leadership strategy). I also add further nuance by distinguishing these effects between primary and secondary stakeholders. While prior work has highlighted the heterogeneity between primary and secondary stakeholders (Clarkson, 1995; Hillman & Keim, 2001; Garcia-Castro & Francoeur, 2016), few studies examine how the financial consequences of competitive strategies vary between different types of stakeholders.

Synergistic Effects of a Differentiation Strategy and Stakeholder Management

Synergy is the ability of two or more activities or entities to generate greater value together than apart (Goold & Campbell, 1998). I expect at least three types of synergies between SM and a differentiation strategy (each enhancing the other), which will strengthen the positive association between SM and financial performance for firms with a differentiation advantage. First, in addition to the existing sources of differentiation advantage for a firm such as unique industrial design, technology, innovation, identifying and serving the unique needs of customers etc., SM serves as an additional lever of differentiation. A differentiation strategy typically leads to higher costs compared to an average player in the industry, but still yields superior margins due to higher product prices the customer is willing to pay (think Whole

Foods). Using the same underlying logic, firms pursuing a differentiation advantage are likely to derive a higher customer value from SM so that any additional costs of SM may be more than offset through premium pricing (Zollo et al., 2018). Take for example, The Body Shop, a well-known beauty products company. The main source of differentiation for The Body Shop traditionally valued by its customers is that its products are manufactured using skin-friendly, natural ingredients, but the company's stakeholder-oriented policies and its decision to only source cruelty-free, fair trade raw materials further enhances its differentiation advantage and premium pricing ability (www.thebodyshop.com). Due to innate logic and the ability to recover higher costs through premium pricing, a differentiation strategy enables SM and vice versa.

Secondly, stakeholder management strengthens the various sources of advantage for a firm pursuing a differentiation strategy and its ability to implement it. A firm's ability to generate a differentiation advantage relies on critical resources provided by stakeholders (Barney, 2018). SM leads to a 'close relationship capability' with stakeholders, which in turn leads to reciprocation, commitment and support by stakeholders for effective implementation of the differentiation strategy (Jones et al., 2018; p.373; Harrison et al, 2010). As Wang and Qian (2011; p.1175) point out, "stakeholders will respond more positively when they are aware of such activities, so firms with more visibility, such as those advertising heavily …have the most to gain". Strong and trustworthy relations with employees and suppliers may prompt them to willingly share knowledge and bring in innovations that strengthen the differentiation advantage (Heugens et al., 2002; Choi & Wang, 2009; Harrison et al., 2010). For example, Steinway & Sons is committed to making craft pianos (as opposed

to mass-produced ones) aimed at satisfying the needs of virtuoso piano performers. It nurtures long-term relationships with the virtuoso pianists and artists who provide advice and feedback for the firm to improve its technology and quality. This helps the firm to develop its unique capability and identity as an innovative, craft piano maker, which forms a virtuous cycle and serves as the heart of its differentiation advantage (Cattani, Dunbar, & Shapira, 2017).

Finally, the likelihood of stakeholder synergies and complementarities is higher when firms pursue a differentiation advantage (Tantalo & Priem, 2016; Garcia-Castro & Francoeur, 2016). Firms are motivated to 'manage for stakeholders' (Harrison et al., 2010: 60) in the presence of stakeholder synergies – when a strategic action can create value for multiple stakeholders simultaneously, thereby satisfying different stakeholder groups without trade-offs (Tantalo & Priem, 2016; Garcia-Castro & Francoeur, 2016). For example, caring for employees could lead to more motivated workforce, which in turn would give rise to better designed and higher quality products thus generating a higher perceived value in the minds of the customers. A similar value creation logic could motivate firms to invest in supplier capabilities, which could help improve the quality of inputs and raw materials and ultimately product quality and customer satisfaction that can result in higher product prices, superior financial performance and better returns to shareholders. British-Dutch multinational Unilever's philosophy of environmental protection and sustainable development appeals to environmentally sensitive stakeholders, which in turn helps the company win new customers, brand loyalty and community support. Further, innovations resulting from stakeholder management will facilitate product differentiation, which together provide new sources of

value creation and strengthen firm performance (Vishwanathan, van Oosterhout, Heugens, Duran & Van Essen, 2020). For all these reasons, I expect the joint effects of a differentiation strategy and stakeholder management to be synergistic and positive on firm performance.

> ***Hypothesis 1:*** *A differentiation-based competitive advantage has a positive influence on the relationship between stakeholder management and firm financial performance.*

Trade-offs between Cost Leadership Strategy and Stakeholder Management

Trade-offs exist when there are negative synergies between two or more activities or entities. I posit that negative synergies exist between a cost leadership strategy and SM such that their joint effect is likely to be negative on firm financial performance. The first and foremost reason for this stems from the very foundational logic, upon which a low-cost competitive advantage is built. A cost leadership strategy enables the firm to charge very low prices and still enjoy superior profits due to its lower costs compared to the rest of the industry (think McDonald's). The core value proposition for customers in the case of low-cost strategy is a low price, which necessitates achieving the lowest cost position in the industry (Porter, 1985). While pursuing this strategy, firms need to be the absolute cost leaders and those that do not have the lowest cost position are vulnerable to price competition (Brandenburger & Stuart, 1996). Therefore, "cost leadership strategy does not, by definition, allow for recovery of stakeholder integration efforts through increasing price levels" (Zollo et al., 2018: 1763). When a firm pursues SM and a low cost strategy simultaneously, most of the value created by the firm accrues to non-shareholder stakeholders including customers (who get a low price) leaving less for shareholders as captured by financial performance measures (Coff, 1999; Garcia-Castro & Aguilera, 2015).

I now outline a number of trade-offs between SM and cost leadership strategy, which together underscore my core argument that a simultaneous pursuit of the two is likely to negatively impact financial performance. The pursuit of a cost leadership strategy leads to more constraints on SM than a differentiation strategy in that it allows only those practices to be deployed, which improve productivity and lower costs. But the costs of many SM activities are not offset by productivity gains. "If investing in stakeholders had no attached costs to the firm, then all firms would do so" (Garcia-Castro & Francoeur, 2016: 409; Harrison et al., 2010). Such costs involve direct economic resources as well as indirect ones such as the time required to interact with and prioritize stakeholders (Bettinazzi & Zollo, 2017). Such constraints may at best lead to arms-length relationship with stakeholders (Zollo et al., 2018). On the other hand, developing a close relationship capability requires continuous and significant investments in integrating various stakeholder interests into strategic decisions, which runs counter to the goal of achieving a low cost position. For example, cost-focused firms are less likely to adopt industry-leading practices for environmental protection, employee compensation or payments to suppliers as it may increase costs and jeopardize their core value proposition to their customers.

It is hard for firms to balance between high stakeholder investments and the goal of achieving cost leadership because the pursuit of one weakens the other, thereby affecting the overall firm performance. These potential conflicts between the goals of maximizing SM and achieving a low cost advantage lead to the conclusion that their simultaneous pursuit is negatively associated with financial performance.

Hypothesis 2*: A low-cost based competitive advantage has a negative influence on the relationship between stakeholder management and firm financial performance.*

Distinguishing the Effects of Primary and Secondary Stakeholder Management

The heterogeneity among stakeholders in terms of their salience or degree of instrumentality has been highlighted in multiple ways – internal and external stakeholders (Freeman, 1984; Hawn & Ioannou, 2016), primary and secondary stakeholders (Clarkson, 1995), and stakeholders' capacity for power, legitimacy and urgency (Mitchell, Agle & Wood, 1997). While it is not easy to delineate "the boundaries of legitimate stakeholders…nor (determine) the weights to be attached to the interests of each stakeholder…" (Bird, Hall, Momente & Reggiani, 2007: 190), Jones (1995) and Clarkson (1995) provide the rationale for distinguishing primary and secondary stakeholders based on contract and transaction cost theories. Primary stakeholders are those "without whose continuing participation the corporation cannot survive as a going concern" (Clarkson, 1995) and are contractually more bound to the firm (Jones, 1995). SM studies have typically considered shareholders, employees, customers and suppliers as primary and examined the financial performance consequences of SM using primary stakeholders (for example, Hillman & Keim, 2001; Coombs & Gilley, 2005; Choi & Wang, 2009; Bridoux & Steolhorst, 2014; Garcia-Castro & Francoeur, 2016; Barney, 2018). On the other hand, firms have weak contractual obligations with secondary stakeholders (Jones, 1995) and their transactional engagements are also not very deep (Clarkson, 1995). From an instrumental stakeholder point of view, they consist of a wider group of stakeholders who are not primary (Hillman & Keim, 2001). Primary stakeholders serve more of an 'enlightened self-interest' when compared to secondary stakeholders (Jones et al., 2007: 145). Resources and capabilities that are more firm-specific are likely to create more financial value (Coff, 1999; Barney, 2018) and primary stakeholders

can be considered to be more firm-specific than other stakeholders (Garcia-Castro & Francoeur, 2016). There is considerable empirical evidence in support of this view that investments related to primary stakeholders as against secondary stakeholders lead to increased financial performance (Berman et al., 1999; Hillman & Keim, 2001; Garcia-Castro & Francoeur, 2016).

I further decompose SM into primary and secondary SM and examine their consequences depending on the generic competitive strategies pursued by a firm. I have argued earlier that SM, in general, has negative performance implications for firms pursuing a cost leadership strategy, due to its inherent logic of low-price driven competition and due to the presence of trade-offs between the two. Extending this logic, a secondary SM is likely to hurt cost leaders even more than a primary SM approach. This is because firms' practices and activities seeking to address secondary stakeholder issues may not carry immediate instrumental benefits and cost the cost leaders even more, thereby magnifying the potential trade-offs. For example, activities such as support for community development, protection of human rights and the environment, result in additional costs, which cannot be passed on to the customers by cost leaders due to their competitive logic of low price advantage.

Firms respond to pressures from their most salient stakeholders (Mitchell et al., 1997). Cost leader firms are under greater pressures from investors and financiers to reduce additional costs particularly arising from investments in secondary stakeholders such as addressing social issues. On the other hand, investing in primary stakeholders such as employees, suppliers and customers may result in some economic benefits that may include higher productivity, lower procurement costs and higher sales, which may offset some of the

costs and reduce the negative impact on financial performance for low-cost strategy firms. Firms also tend to prioritize the needs and expectations of stakeholders on which they depend for critical resources and survival (Ashforth & Gibbs, 1990). Thus, firms that pursue a low-cost strategy are more inclined to invest in and benefit from the primary stakeholders as compared to secondary stakeholders.

Now consider firms pursuing a differentiation advantage, which results in a higher willingness to pay on the part of their customers and premium prices for their products. For such firms too, secondary SM may not result in direct or immediate economic benefits through higher productivity as in the case of primary SM. In fact, secondary SM may lead to a net increase in costs. However, a differentiation strategy's underlying principle of premium pricing ability allows it to recover the higher costs of secondary SM. In addition, the stakeholder synergies and complementarities associated with a differentiation strategy – activities that concurrently create value for multiple stakeholders – arise mostly from secondary SM. For example, a firm's community and environmental investments will likely generate positive spillovers in attracting and retaining better manpower and in improving customer brand perception. Investing in secondary SM enhances a firm's 'close relationship capability' with both primary and secondary stakeholders (Jones et al., 2018; p.373). Lastly, it is possible for differentiators to leverage the investments in secondary SM as additional factors for differentiation and thereby command higher prices or acquire a larger customer share (consider for example, firms making social investments such as Unilever and Patagonia). In other words, both primary and secondary SM are likely to improve financial performance for differentiators.

Hypothesis 3a: *For firms pursuing a differentiation advantage, both primary and secondary stakeholder management are likely to be positively related to firm financial performance.*

Hypothesis 3b*: For firms pursuing a low cost advantage, secondary stakeholder management is likely to be more negatively related to firm financial performance when compared to primary stakeholder management.*

METHODS

Data and Sample

Smaller sample sizes and inadequate longitudinal panel data are two of the core concerns associated with most of the extant empirical studies on the relationship between investing in stakeholders and financial performance (Laplume et al., 2008). Data disclosure by companies on environmental, social and governance (ESG) parameters has improved over the last ten years thanks to initiatives such as Global Reporting Initiative and due to the efforts of Global Sustainability Standards Board (Sustainability Reporting Guidelines, 2013). Investment recommendations by analysts have begun to consider not only financial performance data but also a company's track record in ESG dimensions, which is giving a further boost to sustainability reporting by firms. Thanks to these trends, the timing is now right to examine empirical evidence using longitudinal panel data on the direct as well as moderating effects of the link between stakeholder management (SM) and financial performance.

I use data from Thomson Reuters Eikon database, one of the most comprehensive secondary data sources for ESG data currently available. Eikon tracks more than 400 ESG metrics to measure and report a company's relative ESG commitment across ten major themes (such as emissions, environmental product innovation, human rights and so on) based

on data sources including company reports, filings to stock exchanges, NGO websites, news reports etc. Thomson Reuters ESG scores enhance and replace ASSET4 ESG Ratings, often used by prior studies to measure SM performance. Even though Thomson Reuters claims to cover over 8,000 companies, availability of longitudinal data for more than five years is limited to only large firms. Hence I choose S&P 500 firms (as of financial year 2019) as my sample and put together data on ESG and other financial variables for fifteen years (financial years 2005 to 2019). Firm attributes and financial variables have been collated from Compustat database after matching company codes.[7] Due to missing data for some of the measures, the final dataset consists of 5,032 firm-year observations for models with market value (Tobin's Q) and 5,037 firm-year observations for models with ROA over a fifteen-year period.

Variables and Measures

Dependent variable: Firm financial performance. I choose the most commonly used market-based financial measure of firm performance for listed firms, namely, Tobin's Q. In line with prior studies (e.g., Gompers, Ishii, & Metrick, 2003), I measure Tobin's Q as the ratio of market value of assets to book value of assets.[8] Accounting-based performance measures such as ROA have their limitations, as they capture historical performance and are liable for accounting adjustments by managers from time to time. On the other hand, market-based measures such as Tobin's Q are likely to weigh in and capture all available information on the company (Hillman & Keim, 2001; Wang & Choi, 2013). Market value as captured by Tobin's Q is more likely to incorporate the information value of social practices and stakeholder management of a firm. Due to its wide usage, I also use ROA as an

alternative measure of firm financial performance, measured as net income divided by total assets (Berman et al., 1999; Choi & Wang, 2009).

Independent variables: The independent variables measure firms' stakeholder management and generic competitive strategies namely cost leadership and differentiation.

Stakeholder management. Following previous SM studies (Berman et al., 1999; Hillman & Keim, 2001; Coombs & Gilley, 2005; Choi & Wang, 2009; Laplume, Walker, Zhang, & Yu, 2021), I examine firms' SM performance and operationalize it based on "firm behavior rather than beliefs" (Hillman & Keim, 2001: 130). The overall SM performance of a company is reflected in the environmental, social and governance (ESG) parameters and includes the effects on a comprehensive set of stakeholders such as employees, customers, suppliers, community etc. "The most popular operationalization of SM is a multifaceted measure…which includes (metrics such as)…community relations, workplace diversity, labor relations, environmental impact and product safety" (Laplume et al., 2008: 1167). Though it is debatable whether the natural environment should be considered as a stakeholder (Phillips, Freeman, & Wicks, 2003), I included the environmental (E) dimensions following prior works on SM (e.g., Berman et al., 1999; Hillman & Keim, 2001; Laplume et al., 2021). The E score reflects the management practices promoting eco-efficiency technology and environmental innovation which in turn have an impact on all other stakeholders. I also prefer a broader operationalization of SM as my theorization requires splitting it further into primary and secondary SM. To account for all the factors and practices that determine the SM related behavior of a company, I rely on the overall ESG scores calculated by Thomson Reuters Eikon database to measure SM. Thomson Reuters uses a comprehensive set of 178

comparable measures collected from the company's reports and other data sources for its ESG scoring (Thomson Reuters ESG Scores, 2018). The overall ESG scores take a value ranging between 0 and 100, where a higher ESG score for a firm implies a greater level of SM (Hillman & Keim, 2001).

I create two separate variables to distinguish between primary and secondary SM, based on the ten areas of SM performance available in Thomson Reuters Eikon database. The *primary SM* variable includes four areas that capture activities related to key stakeholders that have direct and formal contractual relationships with the firm: work force (employee relations), product responsibility (customers), management and shareholders. The management dimension differs from the shareholder dimension, as the latter involves corporate practices for merely one stakeholder group - the investors. The management dimension, on the other hand, reflects the degree by which the managers act in the interest of all stakeholders (including shareholders, employees, customers, and suppliers etc).

The *secondary SM* is comprised of six broader stakeholder areas that represent activities that are not directly related to transactions with the contractual or primary stakeholders: resource use, emissions, environmental innovation, human rights, community, and CSR practices. The community dimension measures the company's commitment towards good citizenship and protecting public interests whereas the CSR dimension measures its practices to communicate and integrate economic, social and environmental impacts into day-to-day decision-making. I provide descriptions of all the ten individual metrics that make up primary and secondary SM in the Appendix C. I scaled the SM variables (divided by 100) to avoid small coefficients.

Low cost advantage. In line with prior studies, I measure a firm's cost leadership strategy through its degree of cost advantage as reflected in cost efficiency (e.g., Berman et al., 1999). Specifically, I measure cost efficiency as the ratio of the total operating expenses directly related to cost of goods sold and services provided, to net sales. I subtract this ratio from 1 to measure the degree of low cost advantage of the company.

Differentiation advantage. A differentiation strategy aims to create brand equity and a higher willingness to pay by the customer. This involves a relatively higher level of spend on selling, advertising and administrative expenses. As operationalized by prior studies, I measure the differentiation advantage of a company using a ratio of selling, general and administrative expenses to net sales (e.g., Berman et al., 1999; Wang & Qian, 2011).

I use industry-adjusted competitive strategy variables for all my estimations computed by subtracting from the firm values the average value of all firms with the same two-digit SIC code, excluding the focal firm. To mitigate the impact of outliers, I winsorize the moderator variables at the 1% level. My results are also robust to winsorizing at the 2% level and to trimming at the 1% and 2% levels.

Control variables. I first control for key firm-level variables, which are likely to have an impact on a firm's performance. *Firm size*, measured as the natural logarithm of the net sales of a firm in each year, is used to account for the size of resources and scale effects on firm performance. The *age* of each firm since its listing, in years, is used as a measure of its experience. The financial leverage of a firm has an effect on its performance, which I control using a firm's *debt ratio,* measured by the ratio of long-term debt to total assets. To control for the level of *industry competition*, I use the Herfindahl Index of concentration (Spanos,

Zaralis, & Lioukas, 2004), calculated by summing the squared market shares of firms in each industry each year. I define industry using the two-digit Standard Industrial Classification (SIC) codes and use firms' sales to compute market shares. The Herfindahl index measures industry concentration, thus higher values indicate lower industry competition. I control for firm fixed effects to account for all time-invariant firm-level omitted variables.[9] Finally, I include year dummies in all the models to account for time effects.

Model Specification and Data Analysis

I estimate the models using fixed effects panel regression procedures. A Hausman test rejects the hypothesis of random effects in my data, so I focus on fixed effects estimates for my results (Hausman, 1978; Greene, 1997). The panel design offers some important advantages. First, since it includes both cross-sectional and time series data, it increases the available degrees of freedom so as to improve estimation efficiency. Second, panel estimation procedures allow us to control for unobserved heterogeneity (the possibility that estimated results are due to unobserved factors or omitted variables), and thereby reduce the possibility of biased parameter estimates and spurious results (Greene, 1997). Third, as panel data measures the variables of interest over a period of time, lagged effects can be observed to help rule out reverse causality.

In all my regression models, I use heteroscedasticity-consistent robust standard errors clustered by firm. I lag all independent variables and control variables by one year as the effect of strategies on firm performance is reflected over a period of time and also to address the possibility of reverse causality. In estimating the effects of SM on firm financial performance, I acknowledge the potential problem of endogeneity. As a robustness check, I

adopt the Heckman-2SLS approach that combines a two-stage Heckman selection model to overcome sample selection bias (Heckman, 1979) and a two-stage least squares instrumental variable (2SLS IV) model (Wooldridge, 2010) to address the concerns associated with endogeneity, reverse causality and unobserved heterogeneity. To further check the robustness of my results, I re-run the models using alternative specifications and alternative measures of the key variables.

RESULTS

I check the data for normality of the residuals, heteroscedasticity and existence of collinearity, if any. Multicollinearity is not found to be an issue and the VIF values are within the accepted levels. Table 1.1 reports the descriptive statistics and Pearson correlations for all the variables. The average Tobin's Q is relatively high at 2.33, given that my sample consists of S&P 500 firms. Adequate variance across firms is observed for the measures for competitive strategies and stakeholder management. The mean age of the sample firm is over twenty-seven years and the mean debt ratio, about 0.24. The average net sales of a firm in the sample stands at USD 8,201 million. The pairwise correlations between all the variables are along expected lines.

Insert Tables 1.1 and 1.2 about here

The panel regression results for the effect of the main explanatory and control variables on Tobin's Q are provided in models 1 to 4 of Table 1.2. Model 1 is the baseline model with all independent and control variables. Hypothesis 1 predicts that differentiation advantage and SM have synergistic effects on firm performance. Hypothesis 1 is tested by adding the interaction term – differentiation advantage × SM – to model 1 (results in model 2). The coefficient of the interaction term in model 2 is positive and statistically significant ($\beta = 4.50$, $p<.001$),

supporting my hypothesis 1 that a differentiation advantage and SM reinforce each other to strengthen firm performance. Hypothesis 2 states that there is a partial trade-off between cost leadership and SM in the prediction of firm performance. I test hypothesis 2 by introducing an interaction term – low cost advantage × SM – in model 3, in addition to the baseline and control variables. I do not find support for hypothesis 2 as the coefficient of the interaction term is found to be statistically insignificant (β= 0.45, $p>.10$). The results of model 3 indicate that the positive association between SM and firm financial performance is not weakened for cost leaders. I obtain similar results from the models using ROA as an alternative measure of the dependent variable, in which the interaction term between differentiation advantage and SM is positive and significant (β=0.18, $p<.05$), and the interaction term between cost advantage and SM is not statistically significant (β=0.01, $p>.10$). The null result of hypothesis 2 points to a possibility that the effects of primary and secondary SM for cost leaders could run in opposite directions, thus leading to an overall insignificant effect.

Insert Table 1.3 about here

Table 1.3 presents the results of analyses testing the distinct effects of primary and secondary SM on Tobin's Q (in models 1 and 2) and ROA (in models 3 and 4). As reported in model 1 in Table 1.3, the interaction term between primary SM and differentiation advantage (β=3.10, $p<.05$) is positive and significant, whereas the interaction term between secondary SM and differentiation advantage (β=1.58, $p>.01$) is positive yet insignificant. A Chow test shows that the difference between the two interaction terms is not statistically significant ($p>.10$). It suggests that both primary and secondary SM help boost financial performance for differentiators, supporting hypothesis 3a. In model 2 of Table 1.3, the coefficient for the

interaction term between primary SM and cost advantage (β=4.00, p<.01) is positive and significant, whereas the interaction between secondary SM and cost advantage (β=-2.83, p<.05) is negative and significant. Only secondary SM has a negative effect on financial performance for cost leaders. A Chow test shows that the difference between the two interaction terms is statistically significant (p<.01). Therefore, it confirms that secondary SM hurts firm financial performance for cost leaders more than primary SM, which supports the predictions of hypothesis 3b. These results further suggest that hypothesis 2 on the tradeoffs between SM and low cost strategy is not valid across all stakeholders. I address the implications of the heterogeneous (opposite) effects of primary and secondary SM for cost leaders in the discussion section.

Robustness Checks

I conduct several supplementary analyses to test the sensitivity of my results. Specifically, I rerun the main analysis using Heckman-2SLS models, alternative specifications and alternative measures of the key variables.

Addressing endogeneity. I employ Heckman-2SLS models to address sample selection and endogeneity concerns while examining the relationship between SM and firm performance (Liu et al., 2021). I first estimate the Heckman's first-stage model and then perform instrumental variable regressions for the second-stage Heckman model. In the first-stage Heckman model, I use Probit analysis where the dependent variable is a dummy indicator for whether or not a firm engages in SM in a given year (*SMDUM*), thereby estimating the probability of engaging in SM in the full sample of firms. I then compute the Inverse Mills Ratio (*IMR*) to control for the potential sample selection bias in the

second-stage regression. To predict the probability of a firm pursuing SM, I regress the dummy variable of SM on a set of firm attributes that may affect the probability of investing in stakeholders: firm age, firm size, industry competition, the number of analysts following, and industry [10] and year fixed effects. My choice of variables for this model was guided by data availability and my objective to maximize the number of observations. I use the number of analysts following the focal firm as the exclusion restriction variable, since at least one variable in the Heckman first stage should not be included in the second stage (Certo, Busenbark, Woo, & Semadeni, 2016). SM and sustainability activities of a firm are positively related to the number of financial analysts following it (Harjoto & Jo, 2011), thus making the latter a suitable exclusion restriction.

In the two-stage least squares instrumental variable (2SLS IV) regressions, I select the instruments from the following exogenous variables and the lagged variables of them (Kennedy, 2008): board gender diversity score assessing the percentage of female on the board (*Board Gender Diversity Percent Score*), executive gender diversity score assessing the percentage of female executive members (*Executive Members Gender Diversity Percent Score*), the proportion of firms in an industry that received corporate responsibility (CR) awards per year (*Industry-Year CR Awards*), and the cumulative number of years that a firm had been an active member of the UN Global Compact program (*Years as UNGC Signatory*). I derive the data for all the instruments from the Thomson Reuters Eikon database. A valid instrument must satisfy two criteria (Wooldridge, 2012) - be uncorrelated with the error term (exogeneity criterion) and be correlated with the concerned endogenous variable (relevance criterion). Previous studies demonstrate that presence of female and minority directors on the

board (Cornett, Erhemjamts, & Tehranian, 2016) and the proportion of firms in an industry that are known for responsible practices (Cuypers, Koh, & Wang, 2016) are effective instruments for SM. Research also suggests that the UNGC membership is correlated with SM (Schembera, 2018), but does not have a direct influence on a firm's financial performance. The number and final choice of the instruments for each estimation model was guided by post-analysis diagnostics that ensure the validity of the instruments (Cameron & Trivedi, 2005; Baum, Schaffer, & Stillman, 2007). I perform and report detailed diagnostics on the validity and relevance of the instruments.

In testing Hypotheses 1 and 2, the endogenous variable (SM) is estimated based on two instruments (i.e., *Industry-Year CR Awards* and *Years as UNGC Signatory*) in the first-stage 2SLS model. In testing Hypotheses 3a and 3b, the first-stage 2SLS model estimates the endogenous variables (i.e., primary and secondary SM) based on the instruments: *Board Gender Diversity Percent Score, Executive Members Gender Diversity Percent Score, Years as UNGC Signatory,* and the lagged variable of *Years as UNGC Signatory*.[11] As I also examine the interaction effects of SM and competitive strategies, I generate the interaction terms between the instruments and the moderators in the instrumental variable estimation. Specifically, in the first stage of the 2SLS models, I regress the endogenous variable(s) on the instruments, differentiation and cost leadership advantages, the interaction terms, all the control variables, and firm and year fixed effects. In the 2SLS second-stage model, I use the fitted values obtained from the first stage regressions (instead of the endogenous variable) as a regressor (Wooldridge, 2012), to predict the effects of SM and competitive strategies on firm financial performance along with all other control variables used in the first stage.

I report all the Heckman-2SLS results in the Appendices A and B. Hypothesis 1 is tested by using the interaction term – differentiation advantage × SM – in model 5 of Appendix A, the coefficient of which is positive and statistically significant (β= 8.74, $p<.001$), supporting hypothesis 1. Similarly, I test hypothesis 2 with the interaction term – low cost advantage × SM – in model 6 of Appendix A, the coefficient of which is negative and statistically significant (β=-5.35, $p<.01$), supporting hypothesis 2. Appendix B presents the results for the 2SLS IV regression analyses testing the distinct effects of primary and secondary SM on Tobin's Q. As reported in models 5 and 6 in Appendix B, the interaction term between primary SM and differentiation advantage (β=13.39, $p<.001$), as well as the interaction term between secondary SM and differentiation advantage (β=7.57, $p<.001$), are positive and significant. On the other hand, in models 7 and 8, the coefficient for the interaction term between primary SM and cost advantage is not significant (β=2.50, $p>.10$), but the interaction between secondary SM and cost advantage (β=-2.47, $p<.10$) is negative and significant. Thus I find broad support for hypotheses 3a and 3b.

Alternative specifications and measures. I test the robustness of my findings using alternative model specifications incorporating industry fixed effects instead of firm fixed effects models. Industry dummy variables are defined based on two-digit SIC codes. I replicate the analysis reported in Tables 2 and 3 by specifying the models with industry and year fixed effects. Using alternative specifications controlling for industry fixed effects produces results that are qualitatively the same as the primary findings.

I re-estimate the main models using alternative measures for the key variables. I first create an indicator variable (instead of a continuous variable) as the measure of SM. I

measure a firm with high level of SM using a dummy variable equal to '1' if a firm's ESG score is above the industry median level in a given year, and '0' otherwise. Using the SM indicator variable, I find that the interaction of differentiation advantage and SM indicator is positive and significant (Tobin's Q: β=0.89, $p<.05$; ROA: β=0.08, $p<.001$), whereas the interaction between cost advantage and SM indicator variable is statistically insignificant (Tobin's Q: β=0.25, $p>.10$; ROA: β=0.01, $p>.10$). These results are in line with the main findings.

Following previous studies (Berman et al., 1999; Spanos et al., 2004), I use asset parsimony as alternative proxy for firms' low cost orientation, and advertising intensity as alternative measure of firms' differentiation. Asset parsimony is calculated as the ratio of total assets to total number of employees. Advertising intensity is operationalized as a ratio of advertising expenditures to net sales. Advertising expenses are a finer measure of marketing spend specifically aimed at brand building, which is a core aspect of differentiation. I do not use advertising intensity as a measure of differentiation for my main analysis as there are missing values for advertising expenditures for some firms in some years in my dataset.[12] I follow prior research (Wang & Choi, 2013) and replace the missing values of advertising intensity by zero for the robustness tests. When I re-run the models using the alternative measures of differentiation and cost advantage respectively, I obtain results which are highly consistent with the main findings.[13]

I use an alternative measure of firm performance viz., market-to-book ratio. Market-to-book ratio is calculated as the market value of a firm divided by the book value of assets (Martínez-Sola, García-Teruel, & Martínez-Solano, 2013), which is commonly used to

approximate Tobin's Q (Chung & Pruitt, 1994). Using the market-to-book ratio, I obtain results similar to the main findings reported in the paper with Tobin's Q as the dependent variable, which all corroborate the major findings. I finally run all the models using 2-year lags of the independent variables and obtain similar results. Thus, the sensitivity tests suggest that my empirical evidence is robust.

DISCUSSION AND CONCLUSION

Contributions and Implications

Stakeholder management (SM) studies have identified a number of factors that influence the positive relationship between SM and financial performance - industry factors, geographic and institutional contexts, firm attributes such as innovation, nature of stakeholder relationships etc. (Laplume et al., 2008; Wang & Qian, 2011; Wang & Choi, 2013; Harrison et al., 2010; Garcia-Castro & Francoeur, 2016; Jones et al., 2018). Despite the significant progress made by SM research, our understanding of the many trade-offs managers face while engaging in SM is still limited (Laplume at al., 2008; Wang et al., 2020; Financial Times, 2021). Extending the work on contingencies (Garcia-Castro & Francoeur, 2016), this paper highlights the role of generic competitive strategies and stakeholder heterogeneity in determining when SM is likely to be associated with higher financial performance and when it may not. The findings about the positive moderating role of differentiation strategy and the negative moderating role of cost leadership strategy on the relationship between SM and financial performance have important implications for both SM theory and practice. This study extends prior research by addressing not only the question "when does SM pay?", but also "when does SM *not* pay?", and helps account for some of the mixed and inconclusive

findings in the literature on the financial performance implications of SM (Margolis & Walsh, 2003; Laplume et al., 2008).

This article contributes to the work that seeks a more direct integration of stakeholder theory with competitive strategies (Coff, 1999; Berman et al., 1999; Jones et al., 2018; Barney, 2018; Zollo et al., 2018). While theorizing about the financial performance consequences of SM, Berman et al. (1999: 502) were one of the first to report "interdependence between strategy and stakeholder relationships". Jones et al. (2018: 372) underline the type of stakeholder strategies that are likely to generate a sustainable competitive advantage, calling it a 'communal sharing relational ethics' strategy. Barney (2018) and Zollo et al. (2018) focus on the combination of competitive strategies that are likely to align well with stakeholder strategies in creating overall value to stakeholders. Coff (1999) and to some extent Barney (2018) are among the few that conceptually highlight the trade-offs between SM and shareholder value. This study adds to this body of work - a) by examining not only when the interaction effects are positive but also when they are negative, b) by disentangling the distinct performance effects of primary and secondary SM and c) by providing more comprehensive and rigorous empirical evidence.

This study also contributes to the work underlining stakeholder heterogeneity. This study extends the core thesis that primary stakeholders may contribute more firm-specific and financially relevant resources and capabilities (Garcia-Castro & Francoeur, 2016; Hillman & Keim, 2001) to the specific context of the generic competitive strategies pursued by a firm. I find that both primary and secondary SM have a positive effect on financial performance in firms pursuing a differentiation advantage, and that in firms with a low cost advantage,

secondary SM negatively affects financial performance, whereas primary SM seems to benefit financial performance. These different, and opposite, effects of primary and secondary SM for cost leaders suggest that the stakeholder categories to focus on is an important element of stakeholder strategy for low cost firms.

This paper has important implications for practitioners by shedding additional light on the long-standing question of 'how to do good *and* do well' and by accentuating the challenges of implementing SM in practice. I add boundary conditions to the claim that the benefits of improved stakeholder relations can offset the related costs of SM (Barnett & Salomon, 2012). The findings point out that firms with a differentiation advantage have better prospects of balancing the twin goals of 'doing well' and 'doing good' when compared to firms competing purely based on low costs/prices. Due to the higher trade-offs involved with stakeholder orientation, it would be sensible for managers of low-cost focused firms to combine the strategy with some degree of differentiation. For example, though the core value proposition of firms like Zara or Southwest Airlines is a low price through a low cost advantage, they combine it with other distinctive factors valued by their customers and enjoy some differentiation. However, an important caveat to this study's findings is worth highlighting – they only reflect the *average* effects and do not rule out individual firms successfully managing this balance.

Limitations and Future Research Directions

This study has limitations, which also offer pointers for future research. First, the empirical evidence for my predictions is more indicative of an association, rather than causality. I acknowledge that I have not been able to convincingly establish causality for the

relationships under investigation and this presents more opportunities for future work.

Second, I use traditional measures of firm performance such as Tobin's Q and ROA in conformity with prior studies for evaluating the consequences of SM. However, there has been a welcome movement among investors to employ broader measures of firm performance, which include ESG parameters. Stakeholder theorists have always questioned the logic of measuring firm performance from the point of view of only one set of stakeholders, viz., shareholders (Harrison et al. 2010; Barney, 2018). Third, there is a need to capture the value creation and appropriation by multiple stakeholders and not just shareholders (Jones & Felps, 2013; Harrison & Wicks, 2013; Weitzner & Deutsch, 2019). While this task appears as "a Gordian knot", recent work in strategy has proposed new methods for untangling value creation and value appropriation by different stakeholders (Lieberman, Garcia-Castro & Balasubramanian, 2017: 1194). Although this study does not measure how value is distributed among multiple stakeholders, my finding of the heterogeneous effects of primary and secondary SM among cost leaders implies that value gains may be unevenly distributed among stakeholders. Future studies could investigate how exactly value is appropriated by different groups of stakeholders and how this would differ between firms pursuing different competitive strategies.

Conclusion

Stakeholder management research has arguably shown a 'sunny-side bias' (Jones et al., 2018: 372). The ouster of Emmanuel Faber underlines the growing difficulty of balancing profits and ESG goals and the challenges of creating value for all stakeholders. I believe that this research represents an important step in highlighting these challenges and trade-offs

associated with stakeholder management. While this study makes a beginning, more enquiry is needed to understand the specific trade-offs that arise while jointly pursuing SM and a cost leadership strategy. Are there productivity and scale benefits that some cost leaders can derive even while meeting the needs of stakeholders? For example, Southwest Airlines is able to reward its employees well but still has low per unit employee costs due to the high productivity of its employees and its processes. Secondly, is it possible that firms self-select themselves into different competitive and stakeholder strategies? For example, stakeholders may differ in their motives and may self-select to be associated with firms based on their competitive strategies (Bridoux & Stoelhorst, 2014). Similarly, highly stakeholder-focused firms may strive for differentiation advantages over time instead of focusing purely on cost efficiencies. While the focus of a single study like this article can only be limited, these questions point to a rich future research agenda at the intersection of competitive strategies and stakeholder strategies, and throw open a fertile area for theory building.

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NOTES

1. Though instrumental stakeholder theory has been distinguished from and criticized for lacking a normative or moral perspective by some (Cragg, 2002; Humber, 2002), many others stress that "the normative base serves as the critical underpinning for the theory in all its forms" (Donaldson & Preston, 1995: 85; Parmar et al., 2010).

2. Many related constructs such as stakeholder orientation, engagement and management are used in the stakeholder literature. I adopt the construct of stakeholder management for this paper, which is broader and the most widely used in the literature with an instrumental perspective (Laplume et al., 2008; Parmar et al., 2010).

3. Primary SM focuses on stakeholders who are characterized by more formal contractual relationships with the firms such as employees, customers and investors (Clarkson, 1995; Jones, 1995; Bridoux & Stoelhorst, 2014; Garcia-Castro & Francoeur, 2016). On the other hand, secondary stakeholders are less contractually bound to the firm (Jones, 1995; Garcia-Castro & Francoeur, 2016).

4. This study uses one of the longest duration panel datasets among the studies on stakeholder management.

5. Even though investors have begun to demand disclosures of Environmental, Social and Governance (ESG) parameters and evaluate companies' performance based on these metrics, shareholder-oriented financial performance measures such as Economic Value Added (EVA), Return on Assets (RoA) and Tobin's Q continue to play a predominate role in the evaluation of CEOs.

6. Zollo et al. (2018) offers some conceptual arguments; the current paper develops them in more detail and also offers empirical evidence.

7. More specifically, I use company ticker symbol to uniquely identify a publicly traded company and merge data from the two databases: Eikon and Compustat.

8. The numerator of Tobin's Q, market value of assets, is calculated as the book value of assets plus the market value of common stock minus the book value of total common equity and balance sheet deferred taxes.

9. I control for industry fixed effects as a robustness test later on.

10. Probit model allows only random effects instead of fixed effects. Results controlling for

industry or firm fixed effects in the Heckman second-stage models are similar.

11. The choice of instrument set for testing H3a (*Board Gender Diversity Percent Score, Years as UNGC Signatory* and the lagged variable of *Years as UNGC Signatory*) and H3b (*Executive Members Gender Diversity Percent Score, Years as UNGC Signatory* and the lagged variable of *Years as UNGC Signatory*) was guided by post-analysis diagnostics for the validity and relevance of the instruments.

12. The non-missing firm-year observations for advertising intensity were 2,452 when compared to about 5,000 observations for the rest of the variables.

13. I am unable to report here the full results of the robustness tests due to space constraints.

Table 1.1
Descriptive Statistics and Correlations

	Variable	Mean	SD	1	2	3	4	5	6	7	8	9	10	11
1	Tobin's Q	2.33	1.59	1										
2	ROA	0.07	0.08	0.43***	1									
3	Differentiation advantage [a]	0.01	0.13	0.18***	-0.05**	1								
4	Low cost advantage [a]	0.01	0.13	0.23***	0.60***	-0.01	1							
5	Stakeholder management	0.49	0.20	-0.09***	0.04**	-0.04**	-0.03*	1						
6	Primary SM	0.53	0.18	-0.07***	0.06***	-0.07***	-0.00	0.87***	1					
7	Secondary SM	0.42	0.26	-0.11***	0.02	-0.04**	-0.08***	0.92***	0.69***	1				
8	Firm age	27.31	22.94	-0.07***	0.04**	-0.04**	-0.03*	0.40***	0.36***	0.42***	1			
9	Firm size [b]	9.01	1.31	-0.26***	0.02	-0.25***	-0.13***	0.52***	0.43***	0.56***	0.33***	1		
10	Debt ratio	0.24	0.20	-0.01	-0.12***	-0.01	-0.06***	0.01	-0.00	0.03+	-0.01	-0.08***	1	
11	Industry competition	0.11	0.08	0.05***	0.07***	0.00	0.00	-0.08***	-0.06***	-0.10***	-0.10***	0.14***	-0.04**	1

Note: [a] Industry-adjusted. [b] Natural logarithm. + $p < 0.10$, * $p < 0.05$, ** $p < 0.01$, *** $p < 0.001$

Table 1.2
Interaction Effects of Stakeholder Management and Competitive Strategies on Firm Performance

	Tobin's Q				ROA			
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
Differentiation advantage [a]	-1.73**	-3.84***	-1.71**	-3.86***	-0.12***	-0.21***	-0.12***	-0.21***
	(0.59)	(0.83)	(0.59)	(0.84)	(0.03)	(0.04)	(0.03)	(0.04)
Low cost advantage [a]	0.93***	0.91***	0.73+	0.58	0.12***	0.12***	0.11*	0.11*
	(0.21)	(0.20)	(0.44)	(0.43)	(0.02)	(0.02)	(0.04)	(0.04)
Stakeholder management	0.38	0.32	0.37	0.31	-0.00	-0.01	-0.00	-0.01
	(0.23)	(0.23)	(0.23)	(0.22)	(0.01)	(0.01)	(0.01)	(0.01)
Firm age	0.02**	0.02**	0.02**	0.02**	0.00	0.00	0.00	0.00
	(0.01)	(0.01)	(0.01)	(0.01)	(0.00)	(0.00)	(0.00)	(0.00)
Firm size [b]	-0.52***	-0.52***	-0.52***	-0.52***	-0.01	-0.01	-0.01	-0.01
	(0.11)	(0.11)	(0.11)	(0.11)	(0.01)	(0.01)	(0.01)	(0.01)
Debt ratio	1.10**	1.10**	1.09**	1.09**	-0.01	-0.01	-0.01	-0.01
	(0.40)	(0.39)	(0.39)	(0.39)	(0.02)	(0.01)	(0.02)	(0.01)
Industry competition	1.43	1.58	1.43	1.59	0.16*	0.16*	0.16*	0.16*
	(1.01)	(0.99)	(1.01)	(0.99)	(0.07)	(0.07)	(0.07)	(0.07)
Differentiation advantage [a] × Stakeholder management		4.50***		4.59***		0.18*		0.19*
		(1.34)		(1.34)		(0.07)		(0.07)
Low cost advantage [a] × Stakeholder management			0.45	0.76			0.01	0.03
			(1.05)	(0.99)			(0.07)	(0.07)
Intercept	6.07***	6.06***	6.08***	6.08***	0.10*	0.10*	0.10*	0.10*
	(0.96)	(0.96)	(0.96)	(0.96)	(0.05)	(0.05)	(0.05)	(0.05)
Firm fixed effects	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Year fixed effects	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
F statistic	19.24***	18.39***	18.27***	17.51***	7.76***	8.19***	7.76***	8.49***
R^2	0.14	0.15	0.14	0.15	0.07	0.07	0.07	0.07
N	5032	5032	5032	5032	5037	5037	5037	5037

Note: [a] Industry-adjusted. [b] Natural logarithm. Robust standard errors are in parentheses. + $p < 0.10$, * $p < 0.05$, ** $p < 0.01$, *** $p < 0.001$

Table 1.3
Effects of Primary and Secondary Stakeholder Management

	Tobin's Q		ROA	
	(1)	(2)	(3)	(4)
Differentiation advantage [a]	-3.80***	-1.64**	-0.26***	-0.12***
	(0.87)	(0.57)	(0.05)	(0.03)
Low cost advantage [a]	0.97***	0.03	0.11***	0.09+
	(0.20)	(0.54)	(0.02)	(0.05)
Primary SM	0.46*	0.39+	-0.00	0.00
	(0.22)	(0.20)	(0.01)	(0.01)
Secondary SM	-0.01	0.06	-0.01	-0.01
	(0.17)	(0.17)	(0.01)	(0.01)
Firm age	0.03**	0.03**	0.00	0.00
	(0.01)	(0.01)	(0.00)	(0.00)
Firm size [b]	-0.49***	-0.47***	-0.01*	-0.01*
	(0.10)	(0.10)	(0.00)	(0.00)
Debt ratio	0.86*	0.87*	-0.01	-0.01
	(0.35)	(0.35)	(0.02)	(0.02)
Industry competition	1.16	1.05	0.20**	0.19**
	(0.93)	(0.92)	(0.06)	(0.06)
Differentiation advantage [a] × Primary SM	3.10*		0.29***	
	(1.47)		(0.08)	
Differentiation advantage [a] × Secondary SM	1.58		-0.03	
	(1.36)		(0.08)	
Low cost advantage [a] × Primary SM		4.00**		0.05
		(1.50)		(0.11)
Low cost advantage [a] × Secondary SM		-2.83*		-0.01
		(1.19)		(0.08)
Intercept	5.73***	5.58***	0.14***	0.14***
	(0.90)	(0.85)	(0.04)	(0.04)
Firm fixed effects	Yes	Yes	Yes	Yes
Year fixed effects	Yes	Yes	Yes	Yes
F statistic	17.59***	17.36***	8.05***	8.07***
R^2	0.16	0.16	0.08	0.08
N	4876	4876	4877	4877

Note: [a] Industry-adjusted. [b] Natural logarithm. Robust standard errors are in parentheses.
+ $p < 0.10$, * $p < 0.05$, ** $p < 0.01$, *** $p < 0.001$

APPENDIX A. 2SLS IV Regression Models on the Interaction Effects of Stakeholder Management and Competitive Strategies

	Second stage (Heckman) First stage (2SLS)			Second stage (2SLS)		
	Stakeholder Management			Tobin's Q		
	(1)	(2)	(3)	(4)	(5)	(6)
Stakeholder management				2.65*	2.35*	2.95**
				(1.07)	(1.10)	(1.05)
Differentiation advantage [a]	0.02	-0.00	0.01	-1.46**	-5.68***	-1.60**
	(0.04)	(0.07)	(0.04)	(0.51)	(1.36)	(0.50)
Low cost advantage [a]	-0.02	-0.02	-0.02	1.51***	1.48***	4.01***
	(0.02)	(0.02)	(0.05)	(0.20)	(0.20)	(0.98)
Firm age	0.03**	0.03**	0.03**	-0.01	-0.01	-0.02
	(0.01)	(0.01)	(0.01)	(0.14)	(0.14)	(0.14)
Firm size [b]	0.05***	0.05***	0.05***	-0.53***	-0.51***	-0.52***
	(0.01)	(0.01)	(0.01)	(0.10)	(0.10)	(0.09)
Debt ratio	0.01	0.01	0.01	0.95**	0.96**	1.04***
	(0.02)	(0.02)	(0.02)	(0.29)	(0.30)	(0.30)
Industry competition	0.07	0.06	0.07	0.43	0.79	0.41
	(0.06)	(0.06)	(0.06)	(0.67)	(0.67)	(0.68)
Inverse mills ratio	0.01	0.01	0.01	0.19	0.18	0.20
	(0.01)	(0.01)	(0.01)	(0.17)	(0.17)	(0.18)
Industry-year CR awards	0.13***	0.13***	0.13***			
	(0.02)	(0.02)	(0.02)			
Years as UNGC signatory (lagged) [c]	-0.01***	-0.01***	-0.01***			
	(0.00)	(0.00)	(0.00)			
Differentiation advantage [a] × Industry-year CR awards		0.06				
		(0.11)				
Differentiation advantage [a] × Years as UNGC signatory (lagged) [c]		-0.02				
		(0.01)				
Low cost advantage [a] × Industry-year CR awards			0.01			
			(0.10)			
Low cost advantage [a] × Years as UNGC signatory (lagged) [c]			-0.01*			
			(0.01)			
Differentiation advantage [a] × Stakeholder management					8.74***	
					(2.63)	
Low cost advantage [a] × Stakeholder management						-5.35**
						(2.00)
Firm fixed effects	Yes	Yes	Yes	Yes	Yes	Yes
Year fixed effects	Yes	Yes	Yes	Yes	Yes	Yes
F statistic	137.04***	125.48***	125.24***	30.53***	29.60***	27.50***
R^2	0.46	0.46	0.46	0.08	0.08	0.05
Underidentification test (LM statistic)				51.54***	54.55***	54.92***
Weak identification test (F statistic)				27.83	14.78	15.16
Overidentification test (Hansen J statistic)				Yes (0.72)	Yes (0.61)	Yes (0.98)
N	4833	4833	4833	4833	4833	4833

Note: [a] Industry-adjusted. [b] Natural logarithm. [c] Lagged by one year. Incorporating industry fixed effects (instead of firm fixed effects) produces similar results.
Robust standard errors clustered by firm are in parentheses. $^{+}$ $p < 0.10$, * $p < 0.05$, ** $p < 0.01$, *** $p < 0.001$

APPENDIX B. 2SLS IV Regression Models on the Effects of Primary and Secondary Stakeholder Management

	Second stage (Heckman) First stage (2SLS)				Second stage (2SLS)			
	PRIM_SM	SEC_SM	PRIM_SM	SEC_SM	Tobin's Q			
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
Differentiation advantage [a]	-0.03	0.11	-0.00	0.10*	-8.38***	-4.64***	-1.46**	-1.44**
	(0.06)	(0.07)	(0.04)	(0.05)	(1.70)	(1.07)	(0.52)	(0.48)
Low cost advantage [a]	-0.01	-0.02	-0.01	-0.05	1.37***	1.58***	0.17	2.66***
	(0.02)	(0.02)	(0.03)	(0.03)	(0.21)	(0.18)	(1.72)	(0.61)
Firm age	0.00	0.02	0.00	0.02	0.01	-0.03	0.02	-0.03
	(0.01)	(0.01)	(0.01)	(0.01)	(0.14)	(0.13)	(0.14)	(0.13)
Firm size [b]	0.04***	0.05***	0.04***	0.05***	-0.41***	-0.32***	-0.46***	-0.35***
	(0.01)	(0.01)	(0.01)	(0.01)	(0.08)	(0.08)	(0.09)	(0.08)
Debt ratio	0.00	-0.02	0.00	-0.02	1.10***	0.75**	0.97**	0.86**
	(0.02)	(0.02)	(0.02)	(0.02)	(0.30)	(0.27)	(0.30)	(0.27)
Industry competition	0.02	0.27**	-0.02	0.26**	0.87	0.33	0.62	-0.06
	(0.07)	(0.08)	(0.07)	(0.08)	(0.67)	(0.65)	(0.68)	(0.63)
Inverse mills ratio	-0.01	0.03*	-0.01	0.03*	0.26	0.29	0.26	0.28
	(0.01)	(0.01)	(0.01)	(0.01)	(0.18)	(0.18)	(0.18)	(0.19)
Years as UNGC signatory	0.03***	0.10***	0.03*	0.09***				
	(0.01)	(0.01)	(0.01)	(0.01)				
Years as UNGC signatory (lagged) [c]	-0.04***	-0.10***	-0.03***	-0.10***				
	(0.01)	(0.01)	(0.01)	(0.01)				
BD_Diversity	0.09***	0.04***						
	(0.01)	(0.01)						
Differentiation advantage [a] × Years as UNGC signatory	-0.13	-0.01						
	(0.08)	(0.09)						
Differentiation advantage [a] × Years as UNGC signatory (lagged) [c]	0.13	-0.00						
	(0.09)	(0.10)						
Differentiation advantage [a] × BD_Diversity	0.09	0.02						
	(0.07)	(0.08)						
EXE_Diversity			0.05***	0.03**				
			(0.01)	(0.01)				
Low cost advantage [a] × Years as UNGC signatory			0.07	0.09				
			(0.07)	(0.06)				
Low cost advantage [a] × Years as UNGC signatory (lagged) [c]			-0.10	-0.11				
			(0.08)	(0.07)				
Low cost advantage [a] × EXE_Diversity			0.02	0.07				
			(0.05)	(0.05)				
Primary SM					0.75		1.84*	
					(0.64)		(0.86)	
Secondary SM						0.39		1.14+
						(0.58)		(0.59)
Differentiation advantage [a] × Primary SM					13.39***			
					(3.12)			
Differentiation advantage [a] × Secondary SM						7.57***		
						(2.29)		
Low cost advantage [a] × Primary SM							2.50	
							(3.21)	
Low cost advantage [a] × Secondary SM								-2.47+
								(1.39)
Firm fixed effects	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Year fixed effects	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
F statistic	52.11***	113.42***	49.03***	115.70***	31.47***	32.20***	30.89***	31.30***
R^2	0.28	0.51	0.27	0.51	0.12	0.15	0.11	0.15
Underidentification test (LM statistic)					138.28***	98.36***	69.79***	102.45***
Weak identification test (F statistic)					25.66	20.53	13.15	22.12
Overidentification test (Hansen J statistic)					Yes (0.23)	Yes (0.07)	Yes (0.00)	Yes (0.00)
N	4656	4511	4659	4514	4656	4511	4659	4514

Note: [a] Industry-adjusted. [b] Natural logarithm. [c] Lagged by one year. PRIM_SM=Primary stakeholder management. SEC_SM=Secondary stakeholder management. BD_Diversity = Board Gender Diversity Percent Score. EXE_Diversity = Executive Members Gender Diversity Percent Score. Robust standard errors clustered by firm are in parentheses. + $p < 0.10$, * $p < 0.05$, ** $p < 0.01$, *** $p < 0.001$

APPENDIX C
Thomson Reuters ESG Measurement

Component of Stakeholder Management	Thomson Reuters ESG Category	Definition
Primary Stakeholder Management	Workforce	The Workforce Score measures a company's effectiveness towards job satisfaction, a healthy and safe workplace, maintaining diversity and equal opportunities, and development opportunities for its workforce.
	Product Responsibility	The Product Responsibility Score reflects a company's capacity to produce quality goods and services integrating the customer's health and safety, integrity and data privacy.
	Shareholders	The Shareholders Score measures a company's effectiveness towards equal treatment of shareholders and the use of anti-takeover devices.
	Management	The Management Score measures a company's commitment and effectiveness towards following best practice corporate governance principles.
Secondary Stakeholder Management	Resource Use	The Resource Use Score reflects a company's performance and capacity to reduce the use of materials, energy or water, and to find more eco-efficient solutions by improving supply chain management.
	Emissions	The Emission Reduction Score measures a company's commitment and effectiveness towards reducing environmental emission in the production and operational processes.
	Environmental Innovation	The Innovation Score reflects a company's capacity to reduce the environmental costs and burdens for its customers, thereby creating new market opportunities through new environmental technologies and processes or eco-designed products.
	Human Rights	The Human Rights score measures a company's effectiveness towards respecting the fundamental human rights conventions.
	Community	The Community Score measures the company's commitment towards being a good citizen, protecting public health and respecting business ethics.
	CSR Strategy	The CSR Strategy Score reflects a company's practices to communicate that it integrates the economic (financial), social and environmental dimensions into its day-to-day decision-making processes.

ESSAY #2: A BEHAVIORAL THEORY OF STAKEHOLDER MANAGEMENT: ENVIRONMENTAL PERFORMANCE FEEDBACK AND CORPORATE SOCIAL ORIENTATION

ABSTRACT

Research on corporate social responsibility (CSR) calls for the need to distinguish between corporate environmental and social practices, as firms' investments in environmental issues rely more on technological innovation and scientific pursuit than dealing with social issues. Yet, we know little about the relationship between firms' engagement in environmental and social practices in response to different stakeholder demands. To understand how and why environmental performance feedback (below or above aspirations) may impact firms' subsequent social orientation, I offer a behavioral theory explanation for the heterogeneity in organizations' interpretation and responsiveness to failed and achieved environmental performance goals. Based on panel data analyses on a global sample of 6,659 listed firms across all industries from 72 countries from 2004 to 2019, I find a U-shaped relationship between negative environmental performance feedback and corporate social performance. My findings also show an inverted U-shaped relationship between positive environmental performance feedback and firms' social orientation. Namely, when firms have extremely poor environmental performance far below aspiration levels, they are more motivated to perform better in addressing social issues, mainly due to legitimacy concerns. On the contrary, as firms' environmental performance is well above aspirations, their motivation to improve social performance will be decreased significantly, partly because their legitimacy is already secured by the satisfactory environmental performance.

Keywords: environmental performance feedback, corporate social performance, stakeholder orientation, attainment discrepancy, aspirations, behavioral theory of the firm

A Behavioral Theory of Stakeholder Management: Environmental Performance Feedback and Corporate Social Orientation

INTRODUCTION

The importance of firms' stakeholder orientation and corporate social responsibility (CSR) has been increasingly emphasized by strategy and management scholarship over the last few decades (Barney, 2018; Berman, Wicks, Kotha and Jones, 1999; Hillman and Keim, 2001; Harrison, Bosse and Phillips, 2010; Barnett and Salomon, 2012). CSR involves corporate activities and practices oriented to address both social and environmental issues posed by stakeholders, in order to create social welfare. Prior studies usually put environmental and social orientation of firms under the umbrella concept of CSR, neglecting the differences between them. Recent CSR scholarship has called for the need to discriminate between corporate social and environmental practices (Bansal, Gao and Qureshi, 2014), because they are different yet closely related. While corporate social performance (CSP) includes firms' practices and policies associated with social responsiveness and societal relationships aiming to provide social benefits to stakeholders (Wood, 1991; Bansal et al., 2014), corporate environmental performance (CEP) focuses on "practices that benefit the environment (or mitigate the adverse impact of business on the environment)" (Gunningham, 2009).

Both CEP and CSP involve meeting the needs of stakeholders beyond shareholders, and require enduring commitment and investment of firms. A major difference between them lies in that CEP is grounded in technology, research and development (R&D) and environmental sciences (Bansal et al., 2014). CEP, including emission reduction or environmental product innovation, will require more technological input and scientific pursuit due to the unique attributes of the natural environment (Bansal and Knox-Hayes, 2013; Bansal et al., 2014). For example, issuing a policy of promoting workplace diversity or protecting human rights (even

though the firm may not actually implement it well as it stated) is relatively easier than establishing a lab or R&D center of environmental sciences, which aims to develop new environmental-friendly products or innovate the scientific process of dealing with wastes and reducing emissions. Thus, firms are more likely to pursue CSP (such as philanthropy, community relations, or employee relations) when they fail to do well in CEP, given the limited resources and capabilities within a certain period and also organizational legitimacy concerns.

It is noteworthy to examine corporate environmental and social orientation separately, as there is significant heterogeneity in stakeholder orientation when firms respond to concerns and issues raised by stakeholders (Bettinazzi and Zollo, 2017). In this study, I analyze the relationship between CEP and CSP, and in particular, how failed and achieved environmental performance goals impact firms' social orientation. One premise of this study is that the heterogeneity in stakeholder orientation may affect firms' differential engagement level in addressing environmental and social issues. Based on the behavioral theory of the firm (BTOF), I also assume that environmental performance relative to aspiration levels could be an important driver of firms' pursuit in CSP.

The BTOF suggests that performance attainment discrepancy, defined as the difference between firms' actual performance and their aspirations (Lant, 1992), influences organizational search behavior and future actions (Greve, 1998). According to the problemistic search argument, firm performance below aspiration levels (i.e., negative performance feedback, negative performance gap, or negative attainment discrepancy) triggers firms to find solutions to remedy the poor performance (Cyert and March, 1963; March and Simon, 1958; Lant, Milliken and Batra, 1992). The assumption of problem-driven search behavior offers a possible explanation for why firms may respond to negative feedback about performance goals in general. Similarly,

the slack-driven search argument of BTOF suggests that performance above aspirations (positive feedback), going with managers' confidence and abundant slack resources, might trigger more risk-taking behaviors subsequently. While many behavioral studies focus on the impact of financial performance relative to aspirations (or financial performance feedback) on organizational actions and behavioral changes (e.g., Greve, 2003; Chen and Miller, 2007; Iyer and Miller, 2008; Ref and Shapira, 2017), scholars have also examined the effects of other organizational goals and feedback, including feedback about firm size (Greve, 2008), market share and network status (Baum, Rowley, Shipilov and Chuang, 2005), new product introduction or development (Tyler and Caner, 2016; Eggers and Suh, 2019), innovation performance or innovation failure (Gaba and Bhattacharya, 2012; Maslach, 2016), acquisition performance (Kim, Finkelstein and Haleblian, 2015), and social performance (Wang, Jia, Xiang and Lan, 2021), etc. Extending this line of research, I examine the impact of firms' environmental performance goals and attainment discrepancy on their subsequent social performance.

To my knowledge, there is not any empirical research that has investigated the effect of environmental performance feedback on organizations' behavioral responses related to social orientation. The main purpose of this study is to develop and test a theoretical model on the effects of a firm's environmental performance relative to aspiration levels (i.e., environmental performance feedback)[1] on its future social orientation. My baseline proposition is that prior environmental performance of a firm will have asymmetrical effects on future social performance, depending on whether the former is (well) above or below the firm's aspiration levels. Empirical studies suggest that negative/positive feedback by itself is not always adequate to induce behavioral changes or increased risk-taking (Greve, 1998; Iyer and Miller, 2008; Gaba

[1] Managers make decisions by benchmarking themselves against superior performers in the industry (i.e., performance relative to social aspirations) or against their own performance history (i.e., performance relative to historical aspirations).

and Bhattacharya, 2012; Maslach, 2016), but rather the greater degree of discrepancies between firms' performance and their aspirations may trigger behavioral changes significantly (Gao, Yang and Zhang, 2021; Ref and Shapira, 2017; Ref, Feldman, Iyer and Shapira, 2021). That is, larger attainment discrepancy is likely to lead firms to change their search behavior differently, compared to smaller discrepancies. In this study, I seek to address these two unanswered research questions: 1) why and how environmental performance relative to aspiration levels influences firms' social performance; 2) why and how smaller and larger discrepancies in environmental performance differ in their effects on firms' social performance engagement.

My core argument is that when firms' environmental performance is well below/above aspirations, their motivation to improve its future social performance will change considerably compared to situations where their environmental performance is near aspirations. Specifically, I predict a U-shaped relationship between negative CEP feedback and CSP, such that firms will only turn to improve their CSP when their CEP is extremely poor (well below aspirations) in order to maintain legitimacy. Unlike financial performance goals, firms do not aspire to maximize social performance, but only aim to satisfice, due to legitimacy concerns and resource constraints within a given time. This is why they need a stronger trigger such as extremely poor environmental performance, to act as a catalyst to improve their future social orientation. I then propose an inverse U-shaped relationship between positive CEP feedback and CSP, such that firms' motivation to improve CSP will first increase with positive discrepancy in CEP (due to managerial confidence and excessive resources), and then after a certain point decrease significantly, mainly because their legitimacy is already secured by the superior environmental performance as well as due to depleted resources in environmental investments.

I test my hypotheses using panel data on a global sample of 6,659 listed firms across all

industries from 72 countries between 2004 and 2019[2], with 35,303 firm-year observations in the final dataset. Empirical analyses after accounting for heteroscedasticity, firm, industry, country and time effects, as well as a set of robustness tests, strongly support my predictions.

This study makes several contributions to the literatures on stakeholder orientation, CSR, and performance feedback. First, I offer a behavioral explanation for why and how firms are motivated to change or improve future social performance in response to negative/positive environmental performance feedback. Integrating behavioral theory and CSR research, this study goes beyond examining whether external institutional or stakeholder pressures drive firms' stakeholder orientation to examine how firms' environmental performance against aspiration levels serves as an internal motivation for improving future social performance. Second, this paper contributes to CSR literature by advancing the theory on discrimination between social and environmental responsibility. My empirical analyses not only show a distinction, but also a potential trade-off, between firms' engagement with social and environmental practices. Third, this study extends behavioral research by examining how larger discrepancies in performance goals affect firms' interpretation and responses to feedback about environmental performance beyond economic concerns, and by testing and theorizing a curvilinear relationship between environmental performance feedback and firms' subsequent responses in social responsibility. Empirically, this paper demonstrates that environmental performance far below/above aspirations (i.e., larger discrepancies) will trigger firms to change their search behavior significantly in terms of future social orientation, compared to situations with smaller environmental performance discrepancies.

I structure the rest of the article as follows. In the next section, I present the theoretical foundations of this study and develop my hypotheses. I then describe my dataset and estimation

[2] One of the longest duration and most comprehensive panel datasets among CSR studies.

methods, and present the results. I conclude by discussing the implications of my findings, limitations of this study, and suggestions for future research.

THEORY AND HYPOTHESES

Distinguishing between Environmental and Social Performance

Research has identified many determinants of a firm's CSP such as pressures by various stakeholders (Brammer and Millington, 2008), national culture and institutions (Lenssen et al., 2007; Ioannou and Serafeim, 2012), corporate governance dimensions (Johnson and Greening, 1999; Jo and Harjoto, 2012), integrative complexity of top management teams and decentralization of decision making (Wong, Ormiston and Tetlock, 2011), and board reputation (Mallin and Michelon, 2011). Firms' strategic actions are motivated by their performance against their aspirations or performance feedback (Greve, 2003; Chen and Miller, 2007; Iyer and Miller, 2008); however, we do not know whether and to what extent firms' environmental performance relative to aspiration levels plays a role in motivating firms to pursue future social orientation.

Although corporate social and environmental orientation are similar and critical components of CSR, they are different, particularly in terms of addressing different issues in response to different stakeholder expectations. Previous studies often incorporate social and environmental dimensions together under the general concept of CSR or CSP (e.g., Ioannou and Serafeim, 2012), without distinguishing between them. Recent CSR scholarship has emphasized the importance of discriminating between corporate social and environmental practices (Bansal et al., 2014), due to the uniqueness of addressing environmental issues that focuses on environmental sciences. Firms' environmental orientation, such as reducing emissions, mitigating environmental footprint and developing eco-friendly products and services, tends to require more investments in technological activities and development of innovative solutions.

Although both environmental and social causes require enduring commitment and allocation of organizational resources, research and development (R&D) and innovation initiatives typically involve longer time commitment and continuous financial resources (Flammer and Bansal, 2017; Xu et al., 2019). For example, investing in environmental labs to support innovation and development of new technology related to emission reduction will be relatively more difficult and time-consuming than a simply one-time donation to poor communities.

Because of its significant reliance on technology and innovation, environmental orientation needs more long-term expenses and costs that are less reversible. To some extent, it seems to be more difficult or 'technical' for firms to pursue environmental practices (Bansal et al., 2014) than social practices such as philanthropic donations, supporting community development and employee training, etc. For instance, a firm can cancel its employee training program or reduce the number of women/minorities in the board easily, but it cannot withdraw from an environmental R&D center immediately. The underlying assumption in this study is that firms that fail to perform well in addressing environmental issues are likely to either engage more in social performance because of the fear of legitimacy loss, or decrease in social performance due to stringent organizational resources and the fear of future failures. On the other hand, I believe that firms that are able to meet successfully their environmental performance goals may either increase their engagement with social performance due to confidence and abundant resources, or reduce their motivation to improve social performance because their legitimacy is already secured by the satisfactory environmental performance.

Performance Feedback and Firms' Search Behavior

In the behavioral theory of the firm (BTOF), organizations' actual performance relative to historical or social aspiration levels will condition strategic actions and organizational changes.

The gap between current performance and performance goals (i.e., aspiration levels) is referred to as attainment discrepancy (Lant, 1992), or performance feedback. Organizations performing below and above aspirations may respond similarly to performance feedback after they compare and evaluate actual performance with their own or peer's performance (Cyert and March, 1963; March and Shapira, 1992; Gavetti, Greve, Levinthal and Ocasio, 2012; Greve and Gaba, 2017). In response to performance feedback, below-aspiration firms are more likely to act aggressively and take more risks, because they view poor performance as a problem and thus search for new activities as a remedy. Slack search behavior driven by the presence of additional resources will trigger firms to take greater risks, which is often created by high performance (Cyert and March, 1963; Greve, 2003a, 2003b). Organizations evaluate, interpret and learn from prior performance before they initiate changes or undertake risks (March, 1988; Lant and Mezias, 1992; Lant, Milliken and Batra, 1992; Vissa, Greve and Chen, 2010).

Although behavioral research has extensively examined the effects of financial performance feedback on subsequent organizational search or strategic changes, research has increasingly considered the impact of other organizational goals vis-a-vis aspirations. For instance, new product introduction performance below aspirations drives firms to increase the number of R&D alliances (Tyler and Caner, 2016). Innovation performance goals serve as an important motivator for corporate venture capital initiatives (Gaba and Bhattacharya, 2012). Acquisition performance relative to aspirations influences subsequent acquisition behaviors (Kim, Finkelstein and Haleblian, 2015). When firms' social performance falls below aspirations, they are more likely to use visuals in CSR reports (Wang et al., 2021). Extending this line of research, I examine the asymmetric effects of firms' environmental performance above and below aspiration levels on their subsequent social orientation. Firms' pursuit in addressing social

issues and hence improvement in social performance is a form of organizational search, in response to environmental performance feedback. In particular, I focus on how environmental performance near aspirations as well as far below/above aspirations may be viewed as negative/positive feedback for catalyzing improvements in social performance in the future.

Firms seek to win trust and support from various stakeholders and gain legitimacy by conforming to socially desirable practices adopted by their peers (Donaldson and Preston, 1995; Harrison, Bosse and Phillips, 2010; DiMaggio and Powell, 1983). Stakeholders' perception and evaluation of a firm are critical to corporate image, reputation and legitimacy (Gray and Balmer, 1998; Bansal & Roth, 2000), as well as to firms' financial performance ultimately (Orlitzky et al., 2003). Taking actions to manage stakeholders' perceptions as a response to performance feedback is particularly relevant and effective in CSR areas (Wang et al., 2022). Stakeholders' perception and judgment of firms' failure or success in pursuing environmental responsibility will stimulate firms to influence the external audiences' perceptions, such as initiating changes in social performance engagement in order to affect stakeholders' legitimacy judgment. The pursuit of corporate social/environmental performance entails developing and maintaining stakeholder relationships by addressing the interests of multiple stakeholders beyond legal requirements. However, this often entails additional costs, thereby prompting firms to carefully evaluate the costs and benefits of pursuing social/environmental goals. Both the motivation to influence stakeholder perceptions and firms' consideration of gains/losses in satisfying stakeholders will shape how firms change social causes investments as a response to environmental performance feedback. Overall, I theorize and predict the relationship between environmental performance feedback and social performance, by integrating behavioral theory claims including aspirations and firms' motivation to change search behaviors, as well as cost-benefit analysis in loss versus

gain situations.

Environmental Performance Below Aspirations (Negative Feedback)

As discussed earlier, the BTOF suggests that organizations take actions or initiate changes based on evaluation and comparison of performance relative to aspiration levels (Cyert and March, 1963; March and Simon, 1958; March, 1988). Organizations tend to search for solutions to remedy poor performance in response to negative feedback about performance problems (Cyert and March, 1963; March and Simon, 1958; Lant, Milliken and Batra, 1992). Consistent with the problemistic search argument, poor performance below aspirations has been demonstrated to trigger organizational responses such as strategic change (Greve, 1998; Kacperczyk, Beckman, and Moliterno, 2015), risk taking (Bromiley, 1991), product innovation (Greve, 2003), R&D search intensity (Chen and Miller, 2007), acquisitions (Kim, Finkelstein, and Haleblian, 2015), formation of R&D alliances or non-local partnerships (Tyler and Caner, 2016; Baum et al., 2005), or entry into new markets (Lim, 2019). Similarly, the pursuit of social performance is a form of organizational search, when firms fail to achieve their environmental performance goals. However, I propose that whether negative feedback will induce firms' problemistic search is subject to the degree of discrepancy in environmental performance relative to aspirations.

CEP below aspirations (with smaller performance gap). Low performance relative to aspirations triggers more aggressive actions, because managers in a loss situation tend to initiate risky changes (Kahneman and Tversky, 1979). Nevertheless, managers shift their focus of attention and change risk preferences, depending on whether their focus is on fear or hope, and on whether their attention is attached to aspirations or survival (March and Shapira, 1992; Audia and Greve, 2006). I propose that firms' propensity to improve social performance will be reduced

when the negative gap between firms' environmental performance and aspiration levels is smaller.

Failing to perform well in environmental areas suggests a firm's lack of capability and resources to successfully address environmental issues. When faced with such a failure situation, managers' focus of attention might be on fear, rather than on hope. The uncertainty of gaining returns from alternative initiatives (such as investing in social causes) will trigger firms' risk aversion behaviors, in order to reduce the possibility of future failure (Eggers and Suh, 2019). Consistent with the threat rigidity theory (Staw, Sandelands and Dutton, 1981), poor environmental performance and the related threat to legitimacy loss will induce firms to act conservatively. Thus, the firms' motivation to initiate new search behavior, i.e., allocating additional resources to improve social performance, should be decreased when facing environmental performance failures.

In addition, different organizational goals compete for organizational resources and managerial attention. Note that firms' financial performance goals should precede social/environmental performance goals, as firms cannot pursue social/environmental responsibility without continuous financial support. A firm does not seek to maximize CSR engagement as it does for financial goals, based on both legitimacy- and resource- based logics. That is, a firm pursues CSR mainly to seek and maintain legitimacy, but its CSR commitment is confined by available financial resources. Considering the irreversible expenses and sunk costs in failed environmental projects, firms have limited resources left to be deployed for social causes which also entail higher costs.

Taken together, the fear of failure, lack of confidence, as well as shortage of organizational capabilities and resources within a given period of time, may deter firms'

subsequent risk-taking activities in improving social performance in response to negative environmental performance feedback.

CEP below aspirations (with larger performance gap). The BTOF posits that low performance relative to aspiration levels triggers problemistic search such as strategic changes or risk-taking actions, to rectify the performance problem (Kahneman and Tversky, 1979; Greve 1998; Miller and Chen 2004). I predict that this problem-driven hypothesis of BTOF will only be supported when environmental performance is well below aspirations. Namely, firms will turn to engage more in social performance only when the negative discrepancy in environmental performance is larger. First, firms' failure to perform well in environmental dimensions leaves the pursuit of social performance a perfect second choice, in order to restore or preserve the firms' legitimacy. Compared to the long-term orientation and difficulty of R&D and innovation in environmental engagement, addressing social issues such as philanthropic giving or practices of increasing employee benefits seems relatively less challenging. Moreover, the typically costly and irreversible nature of environmental innovation within a given time period may influence managers' performance goals or aspiration levels, considering the costs and benefits of taking environmental initiatives. Especially when failing to achieve environmental performance goals, firms' propensity to pursue social performance will be increased because of the comparatively quicker returns and improved legitimacy gains.

Another reason for the firms' increase in social performance in response to larger discrepancy of environmental performance is grounded in the stakeholder literature (e.g., Mitchell, Agle, and Wood, 1997). Pressures from stakeholders in social areas overall tend to be greater than in environmental domains, as there are more diverse stakeholder groups in social dimensions than in environmental spheres where firms' major target is to benefit the natural

environment. Firms are supposed to be under greater pressures to meet the demands of and create benefits for the multiple stakeholders in social areas, and hence are more motived to improve their social performance particularly when facing significant setbacks in pursuing environmental performance goals. Further, in terms of the urgency and effectiveness of addressing stakeholder issues, engaging with social causes such as promoting workplace diversity or increasing philanthropic donations can be put into effect more immediately than solving environmental issues such as developing innovative environmentally-friendly processes and products.

Moreover, poor environmental performance relative to aspirations (e.g., industry peers' CEP) will result in adverse assessments and reactions by third party agencies who are engaged with social responsibility ratings of companies. This in turn will further impede the legitimacy and trust granted by stakeholders to the inferior CEP firms. As customers and investors increasingly begin to attach high importance to environmental responsibility of firms, poor CEP relative to peers would in fact result in a competitive disadvantage and weakness. Extremely poor environmental performance relative to peers may motivate firms to terminate current actions that result in negative performance gaps, and instead take new initiatives such as improving future social performance.

Therefore, I propose that firms will decrease their engagement in social performance when the negative environmental performance discrepancy is smaller, whereas firms are more likely to improve social performance when their environmental performance falls far below aspiration levels.

> ***Hypothesis 1:*** *Negative discrepancy of environmental performance has a U-shaped relationship with subsequent social performance.*

Environmental Performance Above Aspirations (Positive Feedback)

CEP above aspirations (with smaller performance gap). The BTOF on slack search suggests that plentiful slack resources also enable firms to undertake more risky actions; managers of high-performing firms with surplus slack and successful experiences are more confident to launch strategic changes (Cyert and March, 1963; March, 1981). Increased stakeholder engagement may result from superior financial performance that goes with available slack resources (Ullmann, 1985; Waddock and Graves, 1997; Orlitzky, Schmidt and Rynes, 2003). Firms in a gain situation where slack resources are abundant are more likely to invest more in addressing stakeholder issues deemed as risky (Cyert and March, 1963; March, 1981; McGuire, Sundgren, and Schneeweis, 1988; McGuire, Schneeweis and Branch, 1990; Waddock and Graves, 1997). Similarly, a firm that is capable to succeed in addressing environmental issues tends to be more positive about engaging with social issues.

Superior environmental performance relative to aspirations also demonstrates that the environmental commitment is well fit with the firm, which exhibits more economic opportunities (Bansal et al., 2014), and hence further promotes slack resources and economic capability of the firm to implement social practices. Further, the gains in both legitimacy and successful experience in better environmental performance can positively spill over to social areas. Consistent with the slack-driven hypothesis of the BTOF, I propose that as firms' environmental performance rises above aspirations, they are more likely to increase their engagement with social performance.

CEP above aspirations (with larger performance gap). However, firms' motivation in pursuing social performance may be changed significantly when the positive discrepancy in environmental performance becomes larger, since risk aversion or risk taking is subject to both aspiration levels and managers' focus of attention. Contrary to the situation in smaller positive

discrepancy, I predict that larger discrepancy in environmental performance (well above aspirations) will lead to decreases in firms' social orientation.

According to the BTOF, firms with above-average performance also tend to act conservatively and are less motivated to take actions to change, thus superior performance above aspiration levels could lead to fewer organizational changes (Miller and Chen 2004; Gaba and Bhattacharya, 2012). In such a case where environmental performance is well above aspirations, managers may shift their focus of attention from searching new opportunities to preserving current situation. Thus, when firm's environmental performance is remarkably superior to that of their peers, they might be reluctant to change and less likely to increase investment in social practices.

Moreover, when a firm performs extremely well in environmental practices, their legitimacy and good reputation, and hence stakeholder recognition and support, are already adequately secured by the satisfactory environmental performance. The firm's motivation to positively affect stakeholder perceptions by improving social performance should be reduced accordingly. Further, successful environmental projects consume large amount of time, various organizational resources and financial expenses, which may leave little for addressing social issues additionally. The resource depletion in environmental orientation substitutes the resource use in social orientation, proposing a potential trade-off between corporate engagement in social and environmental performance. Lastly, to satisfy the shareholders, one of the primary stakeholder groups, a firm will act conservatively by reducing its engagement with social issues when it is already excellent in addressing environmental issues. Because under such an "efficiency loss" condition (Wang et al., 2022: 2384) with greater positive CEP discrepancy, the firm does not want shareholders to consider that it invests unduly in CSR, which may further

increase the loss of efficiency.

Therefore, I predict that as environmental performance rises above aspirations, a firm's propensity to improve subsequent social performance will increase, and after a certain point when the firm's environmental performance is well above aspiration level, its motivation to pursue social performance will decrease.

Hypothesis 2: *Positive discrepancy of environmental performance has an inverted U-shaped relationship with subsequent social performance.*

METHODS

Sample and Data

The empirical setting of this study is listed companies across all industries from 72 countries (including both developed and emerging markets) that have available ESG information, which is identified from Thomson Reuters Eikon database and then merged with other data sources. Thomson Reuters Eikon database is one of the most comprehensive secondary data sources for corporate Environmental, Social and Governance (ESG) information used by previous research on stakeholder management/orientation. Eikon tracks more than 400 ESG metrics to assess and compare a company's ESG commitment and effectiveness across ten major themes (such as emissions, environmental innovation, workforce, product responsibilities, human rights and so on) based on the companies' own ESG disclosure and other data sources such as NGO websites, stock exchange filings, and news sources etc. Thomson Reuters ESG scores and assessment items cover a comprehensive set of stakeholder categories like employee relations, customer satisfaction, partnerships with suppliers, interaction with local communities, and concerns for the natural environment, etc.

The final dataset of this study is drawn from several data sources. Social performance

and environmental performance variables are retrieved from the Thomson Reuters Eikon database. I also draw accounting and financial information of firms from Eikon, complemented by Compustat Global and Compustat North America reports. Country-level institutions and governance variables are drawn from the World Bank's datasets on Worldwide Governance Indicators (WGI) scores. The final dataset includes 35,303 firm-year observations for 6,659 firms headquartered in 72 countries during 2004-2019.

Variables and Measures

Dependent variable: Corporate social performance. Following previous studies (e.g., Ioannou and Serafeim, 2012; Bansal et al., 2014), I operationalize corporate social performance (CSP) using the scores evaluating firms' performance in social dimensions, including workforce, human rights, community and product responsibility[3]. I use the overall scores of social dimensions to proxy social performance. This composite measure captures firms' engagement with social issues raised by various stakeholders, such as employees, customers, suppliers and local communities and so on, in order to meet multiple societal expectations.

Explanatory variables: The key explanatory variables capture the negative and positive environmental performance feedback, that is, the levels of corporate environmental performance exceeding and falling below those of firms' industry peers. Following prior research (e.g., Ioannou and Serafeim, 2012; Bansal et al., 2014), I measure ***corporate environmental performance (CEP)*** as the composite scores of firms' practices and actions in environmental issues. The separate environmental dimensions are resource use, emissions and environmental innovation[4].

[3] I construct the variable of CSP using industry-adjusted measure, computed as a firm's CSP score minus the average CSP score of all firms in the same industry defined by 3-digit NAICS codes, excluding the focal firm.
[4] I performed additional analyses replacing the overall score of environmental performance with the single dimension score of environmental innovation, as a robustness check.

Environmental performance relative to aspirations (discrepancy in environmental performance). The attainment discrepancy of environmental performance is measured as the distance between a firm's actual environmental performance and its social aspiration levels. The social aspiration level of corporate environmental performance is set to industry average (mean) performance in the prior year[5] within the same NAICS three-digit industry in the prior year. A firm's environmental performance relative to social aspiration levels is computed as the difference between a firm's environmental performance (in period t-1) and industry mean (in period t-1)[6]. As I theorize that environmental performance rising above and falling below aspirations have different impact, I split the relative environmental performance variable into two variables based on spline functions to allow for comparing slopes above and below the aspiration levels (Marsh and Cormier, 2002; Baum et al., 2005; Chen and Miller, 2007): (1) *environmental performance below aspirations (negative discrepancy of environmental performance)* and (2) *environmental performance above aspirations (positive discrepancy of environmental performance)*.

Organizations set performance goals (or aspiration levels) using two types of reference points: historical and social aspirations (Cyert and March, 1963; Greve, 1998). Social aspirations represent performance benchmarks that are set using the performance of similar others (e.g., a firm's industry peers or competitors). Historical aspirations refer to a benchmark that is based on a firm's prior or historical performance. There are no clear benchmarks for a firm's environmental performance, vis-a-vis its financial performance. However, similar to social performance, firms' environmental performance is more likely to be driven by demands and expectations of external audiences (Wang et al., 2021). Thus, social comparisons and

[5] I also conduct robustness tests using historical aspirations, instead of social aspirations, to calculate discrepancies in environmental performance, reported later.

[6] Using the industry median, instead of the mean, value as a cutoff produces similar results.

benchmarks based on peers' environmental performance, as against its own environmental performance history, is more appropriate for serving as CEP aspirations. Unlike financial performance goals, firms do not set goals of maximizing their CEP but only to achieve a satisfactory environmental performance when compared to their industry peers. Moreover, shareholders and other stakeholders have increasingly been using social/environmental performance evaluations or ratings provided by third-party agencies such as MSCI KLD Social Index, and Thomson Reuters Eikon, which use industry-specific indicators and industry-relevant measures to assess and compare a firm's social/environmental performance to that of its peers in the industry. For all these reasons, I focus on social aspirations (i.e., performance relative to similar firms within an industry) to assess a firm's environmental performance discrepancies.

Control variables: *Firm size* is measured as the natural logarithm of net sales. *Firm age* is the natural logarithm of the years since a firm's IPO. *Organizational slack* capturing the available financial resources (unabsorbed slack) is calculated as the ratio of current assets to liabilities (e.g., Greve, 2003; Marano et al., 2017). *Leverage* (potential slack) is measured as the ratio of total debt to total equity (e.g., Bromiley, 1991). To control for *industry competition*, I use the Herfindahl–Hirschman Index (HHI) of concentration, calculated by summing the squares of the market share of each firm in the industry. A higher value of the HHI index of industry concentration indicates a lower level of industry competition. *R&D intensity* is calculated as research and development expenses divided by total sales. *Advertising intensity* is measured as the ratio of advertising expenses to total sales. Given that there are missing values of advertising and R&D expenditures for some firms in some years, I follow previous research (Wang and Choi, 2013) and use zero to replace missing data. I use return on assets (ROA) as the proxy for *corporate financial performance* (profitability). ROA is calculated as net income divided by total

assets. *National institutions* and governance quality variables are drawn from the Worldwide Governance Indicators (WGI) including six dimensions: voice and accountability, political stability and absence of violence/terrorism, governance effectiveness, regulatory quality, rule of law, and control of corruption. I use a meta-index of the six variables to capture a country's conditions in governance and institutions.

Empirical Approach

I test the hypotheses using the high-dimensional fixed effects (HDFE) estimator with robust standard errors clustered by firm for heteroscedasticity, with the reghdfe- command in Stata/SE 15.1. The HDFE approach helps address the unobserved heterogeneity concerns (Correia, 2019). All the empirical specifications include the country-, industry-, and time-fixed effects[7] by adding year dummies for the sample period (from 2004 to 2019). I also lagged all the independent variables by one year to address the potential endogeneity issues arising from reverse causality. To compare the difference between negative and positive feedback (actual performance below or above the aspiration levels), I implement a spline specification to split environmental performance relative to aspirations into two variables, so that the two variables are entered simultaneously (Greene, 1993). The variables of negative attainment discrepancy (performance below aspiration levels) are reverse indicators, as their value is less than zero after I implement the spline functions. For ease of interpretation, I reverse-code the 'below-aspiration' variables via multiplying the variable by minus one, so their values are positive. I mean-centered all continuous variables to mitigate the concerns associated with multicollinearity or ill-conditioning between the predictor variables and their higher-order (quadratic) terms (Aiken, West and Reno,

[7] I use alternative estimation models controlling for firm and year fixed effects as a robustness test, obtaining similar results.

1991)[8].

In my hypotheses, I predict that when firms' environmental performance falls far below or rises well above their aspirations, their search behavior will change considerably, compared to situations where the discrepancy in environmental performance is near aspiration levels (below/above). Namely, I propose a curvilinear relationship between negative/positive environmental performance feedback and corporate social performance. To test the hypotheses on the effects of environmental performance relative to aspirations, I first rely on the model presenting the direct effects of above-aspiration and below-aspiration environmental performance respectively. I then introduce the quadratic term of firms' negative/positive discrepancy in environmental performance in the models, based on the models including the control and main independent variables.

RESULTS

Table 2.1 presents the descriptive statistics and correlations for the variables. The variance inflation factor (VIF) values, which are all below 3, do not indicate any problems with multicollinearity. The firms in my sample are 23.86 years old on average, and their mean social performance score is about 43.36 out of 100. Significant variations are shown across firms for the measures of profitability, slacks, discrepancies of environmental performance, and national institutions.

Insert Table 2.1 about here

Table 2.2 presents the main analyses of panel regressions for estimating the effects of environmental performance feedback on firms' subsequent social orientation. Model 1 is the baseline model with all control variables. I enter both control variables and the main explanatory

[8] I also ran the models with non-centered data, obtaining consistent results.

variables (the linear terms of environmental performance feedback) in Model 2. Models 3 and 4 add the quadratic terms of environmental performance feedback (below/above aspiration levels). Model 5 is the full model with controls, linear and quadratic terms. The coefficient of negative discrepancy of environmental performance is negative (β=-0.208, $p<0.001$) in Model 2 testing the linear effect. It suggests that poor environmental performance (the distance of environmental performance below aspiration levels) will result in decreases in subsequent social performance. The coefficient of negative discrepancy of environmental performance is also negative ($p<0.001$) in Models 3 and 4 including the direct and nonlinear effects. On the other hand, positive discrepancy of environmental performance is positively related to subsequent CSP (β=0.286, $p<0.001$) in Model 2. This indicates that firms' future social orientation increases with better environmental performance (the distance of firms' environmental performance above aspirations), which confirms the slack-driven search statement of BTOF.

Insert Table 2.2 about here

Model 3 of Table 2.2 reports the test of Hypothesis 1 by introducing the quadratic term of negative discrepancy of environmental performance. Consistent with my prediction, when firms' environmental performance is poor (below aspiration levels), their engagement in social performance will first decrease (β=-0.317, $p<0.001$) as the negative CEP discrepancy is still near aspirations, and then increase (β=0.109, $p<0.001$) significantly when their CEP is far below aspirations. This suggests a curvilinear (U-shaped) relationship between negative environmental performance feedback and firms' social orientation, supporting Hypothesis 1. That is, the problemistic search argument of the BTOF is only supported when negative attainment discrepancy is well below aspirations. Model 4 adds the quadratic term of above-aspiration

environmental performance and shows a negative coefficient (β=-0.122, p<0.001), which strongly supports Hypothesis 2. This result confirms a curvilinear (inverted U-shaped) relationship between positive environmental performance feedback and firms' subsequent social performance. That is, as firms' environmental performance improves (above aspirations), their social performance will first increase (β=0.407, p<0.001) as the positive CEP discrepancy is in the neighborhood of aspirations, and then decrease significantly (β=-0.122, p<0.001) when their CEP rises well above aspirations. Therefore, in line with my predictions, the results indicate the asymmetry in the effects of prior environmental performance relative to aspirations (above and below aspiration levels) on subsequent social orientation and CSP.

Insert Figures 2.1 and 2.2 about here

In Model 5 of Table 2.2, I present the fully specified model entering the positive and negative discrepancies of environmental performance simultaneously. I obtain consistent results with the models using the split approach for underperforming and outperforming firms (Ref and Shapira, 2017) in CEP. To further corroborate my findings, I present the nonlinear relationships graphically. Figure 2.1 illustrates the U-shaped relationship between negative environmental performance feedback and firms' social performance. In the graph presented in Figure 2.2, I show the inverted U-shaped relationship between positive environmental performance feedback and corporate social performance. Taken together, the results demonstrate that larger discrepancies between environmental performance and aspirations will trigger firms to change their search behavior significantly, compared with situations of performance discrepancies near aspiration levels (Ref and Shapira, 2017).

Validation of (Inverted) U-shaped Relationship

I follow the appropriate three-step procedures to confirm the presence of a U-shaped (an inverse U-shaped) relationship (Lind and Mehlum, 2010). The first requirement for a non-linear relationship is that the quadratic term in the regression model is significant and of the expected sign, which is validated by the results reported above. Second, the slope of the curve of the estimated relationship is sufficiently steep within each endpoint of the explanatory variable. I calculated the marginal effects of the nonlinear relationships in Hypotheses 1 and 2, using the margins- command in Stata/SE 15.1. The data range of environmental performance below/above aspirations is from 0 to 96.728. In the case of environmental performance below aspirations (in Hypothesis 1), when negative discrepancy of environmental performance=15, the slope dy/dx = -0.402 ($p<0.001$); whereas when negative discrepancy of environmental performance=90, the slope dy/dx = 0.136 ($p<0.01$). As to the case of environmental performance above aspirations (in Hypothesis 2), when positive discrepancy of environmental performance=15, the slope dy/dx = 0.457 ($p<0.001$); and when positive discrepancy of environmental performance=95, the slope dy/dx = -0.019 ($p>0.10$).

The third test for a U-shape or inverted U-shape is to check whether the extremum point (turning point) is inside the data range of the predictor. I examined the turning point of environmental performance below/above aspirations and calculated confidence intervals based on Fieller's standard errors. The tests confirm that the U-shape in Hypothesis 1 turns when negative discrepancy in environmental performance = 70.985, within the limits of the data of negative CEP feedback. Similarly, the results also show that the turning point of the inverse U-shape in Hypothesis 2 occurs when positive discrepancy in environmental performance = 91.741, which is within the data range of positive CEP feedback. These results validate the existence of a U-shaped relationship between negative discrepancy in environmental

performance and CSP, and an inverse U-shaped relationship between positive discrepancy in environmental performance and CSP, though such (inverse) U-shapes are not perfect.

Robustness Checks

I conducted a number of additional analyses to check the robustness of my main findings. First, since the theory is based on the premise that financial performance goals precede social performance goals, I regressed social performance on above-aspiration financial performance (ROA). The results support a positive link between better financial performance (above aspirations) and subsequent social performance. Also, for all my specifications concerned with the key hypotheses, there is a significantly positive association between organizational slack and subsequent social performance, which further corroborates my theoretical assumptions in line with the slack-driven search behavior of the BTOF. Second, I use industry median instead of industry mean value as cutoffs to construct the environmental performance variables below and above aspiration levels, obtaining consistent results with the key findings. Then I use respectively the 1-digit and 2-digit, rather than 3-digit, NAICS codes to define the firm's industry, before I identify the industry mean/median value of CEP and compute the measures of social aspirations. Again, I get qualitatively the same results.

Insert Table 2.3 about here

Alternative dependent variable. In addition, I use the original score of CSP, instead of the industry-adjusted CSP variable, as an alternative measure of the dependent variable. Through utilizing the original measure of social performance, I replicate the analyses in Table 2.2 and get similar results that are highly consistent with the major findings.

Alternative independent variable. I utilize the *environmental innovation* score, a

sub-dimension of the overall environmental performance score, as an alternative measure of a firm's environmental performance. As presented in Table 2.3, the results using the alternative measure of environmental performance feedback replacing with *environmental innovation* are highly consistent with the major findings reported in Table 2.2.

Insert Table 2.4 about here

Alternative estimation models and alternative aspiration measures. Last, I use other specifications incorporating firm fixed effects models, obtaining largely consistent results with the main findings. Further, I also construct different measure of environmental performance aspirations, that is, the historical aspirations. I compute firms' *environmental performance below/above historical aspirations* as the difference between firms' actual environmental performance (in period t-1) and their own prior environmental performance (in period t-2). Again, the results using alternative calculations of environmental performance aspirations are similar to the major findings. Table 2.4 presents the additional analyses using firm fixed effects models (through Models 1 to 3) and historical aspirations measures of CEP (in Models 4 to 6). Overall, the additional analyses all substantiate the robustness of the main results.

DISCUSSION AND CONCLUSION

Conclusions and Contributions

The main objective for this study is to develop and test a behavioral theory explanation for whether and how environmental performance below/above aspirations (i.e., negative/positive CEP feedback) may lead to improved social performance of firms subsequently. My theory and empirical evidence suggest that firms' different interpretation and responses to negative/positive environmental performance feedback are contingent on the degree of discrepancies in

environmental performance. My core argument is that poor environmental performance relative to aspiration level will only motivate firms to improve subsequent social performance when this negative CEP discrepancy is larger. That is, when firms have extremely poor environmental performance, they will turn to pursue social orientation as an alternative option to maintain legitimacy. Further, I propose that superior environmental performance well above aspirations may decrease firms' motivation to engage in social performance, because firms' legitimacy is already well secured by the satisfactory environmental performance, and that the resource depletion of CEP might limit the resource use for CSP. I theorized and found that larger or smaller discrepancy in environmental performance will trigger different (opposite) search behavior of firms significantly.

I find supplementary empirical evidence that confirms the differential effects between positive and negative feedback about environmental performance. My results corroborate that larger positive attainment discrepancy relative to aspirations will make firms act conservatively and hence are reluctant to change (March, 1996; Miller and Chen, 2004), as opposed to the problem-drive search argument that negative performance feedback stimulates increased behavioral change. Namely, firms with poor/superior environmental performance relative to peers will not always take actions to improve future social performance, depending on the performance discrepancy levels. The results show that extremely superior environmental performance relative to peers will prevent firms from increasing efforts to improve subsequent CSP. These findings, counter to the slack search argument of the BTOF, are consistent with conclusions of several previous studies in behavioral research that performance above aspirations (positive feedback) may provide little incentive for firms to change (Greve, 1998; 2003; Gaba and Bhattacharya, 2012).

This study makes contributions to research on the drivers of CSP and performance implications of negative/positive feedback in terms of stakeholder management. First, it contributes to literatures on CSP and stakeholder theory by offering a behavioral explanation and empirical evidence for firms' motivation to pursue CSP implying their orientation towards stakeholders in social areas. Specifically, my results demonstrate that the further a firm's environmental performance falls far below aspirations, the higher its future social performance. The CSP literature has identified different motivators for firms' engaging in social orientation (e.g., Brammer and Millington, 2008; Ioannou and Serafeim, 2012; Brower and Mahajan, 2013; Orlitzky, Louche, Gond and Chapple, 2017). However, research has yet to consider the potential role of negative/positive feedback related to environmental performance.

Second, this research represents one of the few empirical attempts to distinguish between corporate social and environmental orientation (Bansal et al., 2014) in the CSR literature. I theorize and empirically test the previously underexplored relationship between CEP and CSP, through the lens of how firms interpret and respond to environmental performance feedback differentially. I further tease out the variance of behavioral changes of firms with different degree of environmental performance gaps relative to aspirations. I find that the relationship between (positive/negative) environmental performance feedback and firms' social performance is curvilinear. This study adds to stakeholder theory and the related CSP literature by showing that organizations react to poor environmental performance relative to aspirations because of both stakeholder heterogeneity and institutional pressures (legitimacy concerns). This paper also extends the investigation of feedback-driven responses to an international context, by using a comprehensive dataset on a global sample.

Third, this study extends behavioral research to the context of stakeholder orientation by

exploring and explaining how different levels of performance discrepancies affect the way in which negative/positive environmental performance feedback is interpreted. Most prior work on behavioral theory suggests a positive link between negative feedback and subsequent organizational changes, as posited by the problemistic search thesis (Greve, 2003; Miller and Chen 2004; Baum et al., 2005; Tyler and Caner, 2016). However, my findings support that the influence of negative feedback on organizational actions and future stakeholder orientation is not always consistent with the problem-driven search predictions (McNamara and Bromiley, 1997; Greve, 1998). Under the conditions of greater failure to meet environmental performance goals, on the one hand, firms alternatively pursue CSP to gain stakeholder support and preserve legitimacy granted by various external audiences. On the other hand, the favorable situation of greater success in environmental performance decreases firms' motivation to engage in subsequent CSP, because of the seemingly trade-offs between pursuing CEP and CSP. This work highlights the importance of environmental performance feedback that promotes organizational search for improving social performance and the critical influence of larger discrepancy in environmental performance as a catalyst, when firms respond to various social/stakeholder pressures.

Drawing on the conception from behavioral theory of the firm, this study moves beyond the predominant focus on financial performance feedback through introducing feedback about environmental performance, in order to provide a deeper understanding of the antecedents of CSP. While the role of financial performance feedback is well explored in the behavioral research (e.g., Greve, 2003; Chen and Miller, 2007; Iyer and Miller, 2008; Lim, 2019), there is limited work that considers the effects of performance feedback related to stakeholder management (Nason, Bacq and Gras, 2018; Wang et al., 2021). In fact, firms have aspirations (or

goals) other than profitability, and they set goals including satisfying stakeholder interests or mitigating negative externalities of corporate deeds. This study adds to the behavioral theory literature by demonstrating that environmental performance feedback plays a role similarly to financial performance feedback in influencing firms' subsequent stakeholder (social) orientation.

Moreover, my results substantiate the sequential attention logic of meeting organizational goals (March and Simon, 1958; Greve, 2008; Tyler and Caner, 2016). In particular, I find that the negative association between smaller negative discrepancy in environmental performance and subsequent CSP seems to mirror the positive relationship between smaller positive discrepancy in environmental performance on firms' future CSP. It suggests that firms will respond to negative/positive environmental performance feedback based on, but beyond, stringent/abundant financial (resources) concerns. Thus, I argue that fulfillment of financial performance goals should precede, and also facilitate, satisfying environmental performance goals. Given that both stakeholder theory and performance feedback theory are not fully developed and systematically tested yet (Jones et al., 2018; Greve and Gaba, 2017), this article offers theoretical advancement and empirical evidence for both theories, through integrating the effects of behavioral variables and social responsibility factors on corporate strategic (re)orientations towards stakeholders.

Practical Implications

My findings have important practical implications as well. First, it provides evidence of how managers interpret environmental performance feedback as well as how and why negative/positive feedback will trigger organizational responses to initiate behavioral changes toward socially-oriented stakeholders. The extreme points of positive/negative CEP feedback for motivating firms to reduce/improve subsequent social engagement is more than one standard

deviation above the mean value of positive/negative CEP feedback in my sample. It also suggests that when firms have excessively bad environmental performance far below the industry-average level, they will interpret such failures differently and begin to initiate changes. However, when a firm's environmental performance is excellent and among the top 5% in its industry, such leading position will make the firm reluctant to change. Recognizing the significant role larger performance discrepancy can play in shaping firms' reactions to superior/poorer environmental performance, managers should make efforts to look for alternative solutions other than improving social performance, in order to mitigate the trade-offs between creating benefits for social and environmental stakeholders, or to offset the legitimacy loss and resource depletion from failed environmental orientation.

Second, the potential trade-offs between corporate environmental and social engagement demonstrated in this paper mirror the fact that it is difficult for firms to satisfy multiple stakeholders simultaneously. The crux in existing literature, and particularly in stakeholder management studies, is that we still don't know sufficiently enough about how different types of value (beyond economic dimension) is created and captured among different stakeholders (Barney, 2001; Parmar et al., 2010). For managers, a possible way out is to figure out how to create 'stakeholder synergy' (Tantalo and Priem, 2016) – a single managerial innovation or strategic action that increases different types of value for more than one stakeholder groups simultaneously while not reducing the value or benefits created for any other stakeholder group. On the other hand, to satisfy the shareholders, one of the most important primary stakeholder groups, a firm can act conservatively by investing less in addressing social issues when it already has superior environmental performance. Under the "efficiency loss" context (Wang et al., 2022: 2384) with larger positive discrepancy in environmental performance,

the firm could reduce its social performance engagement to signal to shareholders that it does not invest unduly in CSR that may increase further efficiency loss.

Lastly, the positive link between above-aspiration ROA (and also organizational slacks) and subsequent social performance validates that financial performance is still the primary goal of firms, prior to other organizational goals such as seeking stakeholder favor and reducing corporate negative impact on the society and the environment at large. Managers should recognize that a financial advantage with excess funds and abundant resources will facilitate firms to improve stakeholder engagement, leading to increased stakeholder support and trust, which in turn benefits corporate financial performance ultimately.

Limitations and Future Research

While this study represents an important step forward in examining the drivers of corporate social performance and the heterogeneity of firms' stakeholder orientation, I note several limitations in this study and see potential for future research. I use a meta-construct to measure CSP that does not capture the single components of CSP involving different stakeholder categories within the broad social areas. I encourage future research to break down the aggregated measure of CSP into separate stakeholder dimensions (Orlitzky et al., 2017), thus further accounting for the distinct influence of negative/positive feedback on corporate stakeholder performance. I also propose that CSP can be measured in different ways, especially from the perspective of stakeholders' perception and judgment of value created by firms. Future work conducting qualitative case studies to explore how stakeholders evaluate firms' CSP would be a nice extension to this study.

Further, though relying on an international sample, this study does not look at the heterogeneity between different countries, or untangle whether or which part of the national

institutions may affect CSP (Fransen, 2013) in response to environmental performance feedback. In a set of post hoc analyses, I tested the potential moderating effects of national institutions. Though I did not find significant interaction effects between national institutions and the quadratic term of negative/positive CEP feedback, I found a significant and negative interaction between national institutions and the linear term of positive CEP feedback. This result suggests that as national institutions become stronger, the positive relationship between positive CEP feedback and subsequent CSP will become weaker. Namely, for firms from countries with weak institutions, their responses to positive CEP feedback through improving CSP will be stronger. This empirical finding is consistent with some arguments of existing research (e.g., Marano et al., 2017), as companies from countries with weak institutional environment (or institutional voids) tend to face greater legitimacy challenges, which in turn push the firms to engage more in social performance. I also did not explain which aspect of strong or weak institutional arrangements the CSP-related activities could be meant to compensate for (Brown and Knudsen, 2015). Future research could disaggregate national institutions and uncover their distinct effects on specific CSP dimensions, when firms interpret and respond to different levels of environmental performance discrepancies.

Future work could also consider the potential impact of host country institutional environment on firms' CSR efforts (Rathert, 2016), or distinguish among the different types of firms, such as purely domestic firms and multinational companies. I suggest that future work could replicate and extend this research by incorporating the effects of host country institutional conditions, or the interactions of home country and host country institutions on CSP. For example, the distance between home and host countries' regulatory or political risks may be a critical driver of multinational firms' behavioral changes (Yasuda and Kotabe, 2021). While this

study is one of the few empirical work that integrates stakeholder theory and behavioral theory of the firm, I limit my discussion of firms' search behavior to CSP. I encourage future research to investigate firms' behavioral responses related to other organizational outcomes such as corporate misconducts. For instance, future research could develop a behavioral theory and empirically examine what factors involving a reference point may drive corporate irresponsible behaviors. Finally, I realize that there are other factors or contingencies that could shape firms' interpretation and responses to negative/positive feedback. Future research should consider additional contextual factors such as the characteristics of top management team (Wong, Ormiston and Tetlock, 2011), the level of differentiation in the industry (Hull and Rothenberg, 2008), or national culture (Lenssen et al., 2007), when examining the link between CEP and CSP. While this work will shed light on whether and how negative/positive feedback can be beneficial for firms' future social performance, I encourage future studies to advance behavioral theory and stakeholder research through considering other organizational outcomes in other settings (e.g., firms' responses to stakeholder attack in high-controversial industries).

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Table 2.1 Descriptive Statistics and Correlations of Variables [a]

	Variable	Mean	SD	1	2	3	4	5	6	7	8	9	10	11	12
1	Corporate social performance [b]	3.831	23.195	1											
2	Negative discrepancy of environmental performance	10.931	14.788	-0.430	1										
3	Positive discrepancy of environmental performance	10.843	16.974	0.520	-0.472	1									
4	Financial performance	0.042	0.106	0.066	-0.035	0.057	1								
5	Debt ratio	0.900	1.388	0.033	-0.025	0.036	-0.121	1							
6	Firm age	23.860	24.382	0.138	-0.110	0.148	0.035	0.021	1						
7	Firm size [c]	7.783	1.899	0.352	-0.256	0.356	0.270	0.152	0.247	1					
8	Organizational slack	1.037	1.437	-0.142	0.117	-0.126	-0.070	-0.243	-0.066	-0.364	1				
9	Industry competition	0.050	0.047	0.001	-0.006	-0.007	0.024	0.008	-0.075	-0.017	-0.011	1			
10	R&D intensity	0.389	2.943	-0.066	0.057	-0.066	-0.328	-0.055	-0.054	-0.471	0.311	0.016	1		
11	Advertising intensity	0.691	6.319	-0.069	0.065	-0.063	-0.355	-0.051	-0.049	-0.447	0.339	-0.015	0.741	1	
12	National institutions	0.213	0.825	0.067	0.021	0.018	-0.077	-0.043	0.119	-0.103	0.037	0.052	0.059	0.052	1

Note: [a] Unstandardized data. [b] Industry-adjusted. [c] Natural logarithm.

Table 2.2 Results of Main Analyses: Relationship between Environmental Performance Feedback and Corporate Social Performance [a]

	Corporate social performance				
	(1)	(2)	(3)	(4)	(5)
Financial performance	-0.039***	-0.015*	-0.016*	-0.016*	-0.016*
	(0.008)	(0.007)	(0.007)	(0.007)	(0.007)
Leverage	-0.031***	-0.019***	-0.020***	-0.019***	-0.020***
	(0.005)	(0.005)	(0.005)	(0.005)	(0.005)
Firm age	0.109***	0.067***	0.066***	0.066***	0.065***
	(0.016)	(0.010)	(0.010)	(0.010)	(0.010)
Firm size [b]	0.779***	0.444***	0.436***	0.440***	0.435***
	(0.008)	(0.008)	(0.008)	(0.008)	(0.008)
Organizational slack	0.021**	0.024***	0.023***	0.025***	0.024***
	(0.007)	(0.006)	(0.006)	(0.006)	(0.006)
Industry competition	-0.062*	-0.051+	-0.053+	-0.050+	-0.052+
	(0.029)	(0.027)	(0.027)	(0.027)	(0.027)
R&D intensity	0.160***	0.094***	0.094***	0.094***	0.094***
	(0.009)	(0.007)	(0.007)	(0.007)	(0.007)
Advertising intensity	0.134***	0.076***	0.074***	0.076***	0.074***
	(0.011)	(0.009)	(0.009)	(0.009)	(0.009)
National institutions	0.030	0.129**	0.123*	0.123*	0.120*
	(0.055)	(0.048)	(0.048)	(0.048)	(0.048)
Negative discrepancy of environmental performance		-0.208***	-0.317***	-0.191***	-0.280***
		(0.005)	(0.011)	(0.005)	(0.012)
Positive discrepancy of environmental performance		0.286***	0.268***	0.407***	0.364***
		(0.005)	(0.005)	(0.012)	(0.013)
Negative discrepancy of environmental performance - squared			0.109***		0.085***
			(0.011)		(0.011)
Positive discrepancy of environmental performance - squared				-0.122***	-0.091***
				(0.011)	(0.011)
Intercept	-0.300***	-0.170***	-0.166***	-0.169***	-0.166***
	(0.014)	(0.013)	(0.013)	(0.013)	(0.013)
Industry fixed effects	Yes	Yes	Yes	Yes	Yes
Country fixed effects	Yes	Yes	Yes	Yes	Yes
Year fixed effects	Yes	Yes	Yes	Yes	Yes
F statistic	1400.382***	2611.116***	2453.994***	2441.258***	2285.108***
R^2	0.3787	0.5158	0.5176	0.5175	0.5185
N	35303	35303	35303	35303	35303

Note: [a] All continuous variables are standardized. [b] Natural logarithm. Robust standard errors are in parentheses.
+ $p < 0.10$, * $p < 0.05$, ** $p < 0.01$, *** $p < 0.001$

Table 2.3 Results of Robustness Tests: Using Alternative Independent Variable (Environmental Innovation) [a]

	Corporate social performance				
	(1)	(2)	(3)	(4)	(5)
Financial performance	-0.038***	-0.030***	-0.030***	-0.031***	-0.030***
	(0.008)	(0.008)	(0.008)	(0.008)	(0.008)
Leverage	-0.031***	-0.030***	-0.030***	-0.030***	-0.030***
	(0.005)	(0.005)	(0.005)	(0.005)	(0.005)
Firm age	0.108***	0.097***	0.097***	0.097***	0.097***
	(0.016)	(0.015)	(0.015)	(0.015)	(0.015)
Firm size [b]	0.781***	0.710***	0.708***	0.708***	0.707***
	(0.008)	(0.008)	(0.008)	(0.008)	(0.008)
Organizational slack	0.023**	0.025***	0.024***	0.025***	0.024***
	(0.007)	(0.007)	(0.007)	(0.007)	(0.007)
Industry competition	-0.061*	-0.056+	-0.055+	-0.057*	-0.055+
	(0.029)	(0.029)	(0.029)	(0.029)	(0.029)
R&D intensity	0.161***	0.144***	0.143***	0.143***	0.143***
	(0.009)	(0.009)	(0.009)	(0.009)	(0.009)
Advertising intensity	0.135***	0.124***	0.124***	0.124***	0.124***
	(0.011)	(0.010)	(0.010)	(0.010)	(0.010)
National institutions	0.028	0.048	0.042	0.046	0.042
	(0.055)	(0.054)	(0.054)	(0.054)	(0.054)
Negative discrepancy of environmental innovation		-0.076***	-0.128***	-0.070***	-0.116***
		(0.005)	(0.012)	(0.005)	(0.013)
Positive discrepancy of environmental innovation		0.118***	0.110***	0.174***	0.153***
		(0.005)	(0.005)	(0.014)	(0.015)
Negative discrepancy of environmental innovation - squared			0.053***		0.045***
			(0.012)		(0.012)
Positive discrepancy of environmental innovation - squared				-0.056***	-0.042**
				(0.013)	(0.014)
Intercept	-0.303***	-0.273***	-0.271***	-0.272***	-0.271***
	(0.014)	(0.014)	(0.014)	(0.014)	(0.014)
Industry fixed effects	Yes	Yes	Yes	Yes	Yes
Country fixed effects	Yes	Yes	Yes	Yes	Yes
Year fixed effects	Yes	Yes	Yes	Yes	Yes
F statistic	1397.599***	1402.386***	1290.060***	1287.382***	1191.692***
R^2	0.3791	0.4035	0.4040	0.4038	0.4041
N	35238	35238	35238	35238	35238

Note: [a] All continuous variables are standardized. [b] Natural logarithm. Robust standard errors are in parentheses.
+ $p < 0.10$, * $p < 0.05$, ** $p < 0.01$, *** $p < 0.001$

Table 2.4 Results of Robustness Tests: Using Alternative Estimation Models (Firm Fixed Effects)and Alternative Aspiration Measures [a]

	Corporate social performance					
	Social Aspirations of CEP			Historical Aspirations of CEP		
	(1)	(2)	(3)	(4)	(5)	(6)
Financial performance	0.000	0.000	0.000	-0.004	-0.004	-0.004
	(0.007)	(0.007)	(0.007)	(0.008)	(0.008)	(0.007)
Debt ratio	-0.012^{+}	-0.013^{+}	-0.012^{+}	-0.010	-0.010	-0.009
	(0.007)	(0.007)	(0.007)	(0.008)	(0.008)	(0.008)
Firm age	1.508***	1.506***	1.504***	1.839***	1.841***	1.837***
	(0.071)	(0.071)	(0.072)	(0.070)	(0.070)	(0.070)
Firm size [b]	0.193***	0.191***	0.192***	0.231***	0.231***	0.226***
	(0.028)	(0.028)	(0.028)	(0.031)	(0.031)	(0.031)
Organizational slack	-0.001	-0.002	-0.001	-0.018	-0.018	-0.018
	(0.010)	(0.010)	(0.010)	(0.012)	(0.012)	(0.012)
Industry competition	-0.028	-0.028	-0.029	-0.053	-0.053	-0.053
	(0.032)	(0.032)	(0.032)	(0.035)	(0.035)	(0.035)
R&D intensity	0.016	0.015	0.016	0.015	0.015	0.015
	(0.010)	(0.010)	(0.010)	(0.012)	(0.012)	(0.012)
Advertising intensity	0.028*	0.028*	0.028*	0.034*	0.034*	0.034*
	(0.012)	(0.012)	(0.012)	(0.014)	(0.014)	(0.014)
National institutions	0.090	0.087	0.089	-0.010	-0.010	-0.013
	(0.059)	(0.059)	(0.059)	(0.056)	(0.056)	(0.056)
Negative discrepancy of environmental performance (SA)	-0.115***	-0.149***	-0.113***			
	(0.008)	(0.014)	(0.008)			
Positive discrepancy of environmental performance (SA)	0.122***	0.117***	0.137***			
	(0.009)	(0.009)	(0.017)			
Negative discrepancy of environmental performance (SA) - squared		0.035**				
		(0.013)				
Positive discrepancy of environmental performance (SA) - squared			-0.016			
			(0.015)			
Negative discrepancy of environmental performance (HA)				-0.008**	-0.015**	-0.005^{+}
				(0.003)	(0.005)	(0.003)
Positive discrepancy of environmental performance (HA)				0.033***	0.032***	0.071***
				(0.003)	(0.003)	(0.007)
Negative discrepancy of environmental performance (HA) - squared					0.008	
					(0.005)	

(continued)

Positive discrepancy of environmental performance (HA) - squared						-0.042***
						(0.008)
Intercept	-0.463***	-0.461***	-0.461***	-0.578***	-0.579***	-0.574***
	(0.030)	(0.030)	(0.030)	(0.030)	(0.030)	(0.031)
Firm fixed effects	Yes	Yes	Yes	Yes	Yes	Yes
Year fixed effects	Yes	Yes	Yes	Yes	Yes	Yes
F statistic	102.737***	99.054***	98.980***	85.942***	82.440***	83.885***
R^2	0.2182	0.2187	0.2183	0.1751	0.1752	0.1765
N	35303	35303	35303	35581	35581	35581

Note: [a] All continuous variables are standardized. [b] Natural logarithm. Robust standard errors are in parentheses. CEP=Corporate environmental performance. SA=Social aspirations. HA=Historical aspirations. $^{+}$ $p < 0.10$, * $p < 0.05$, ** $p < 0.01$, *** $p < 0.001$

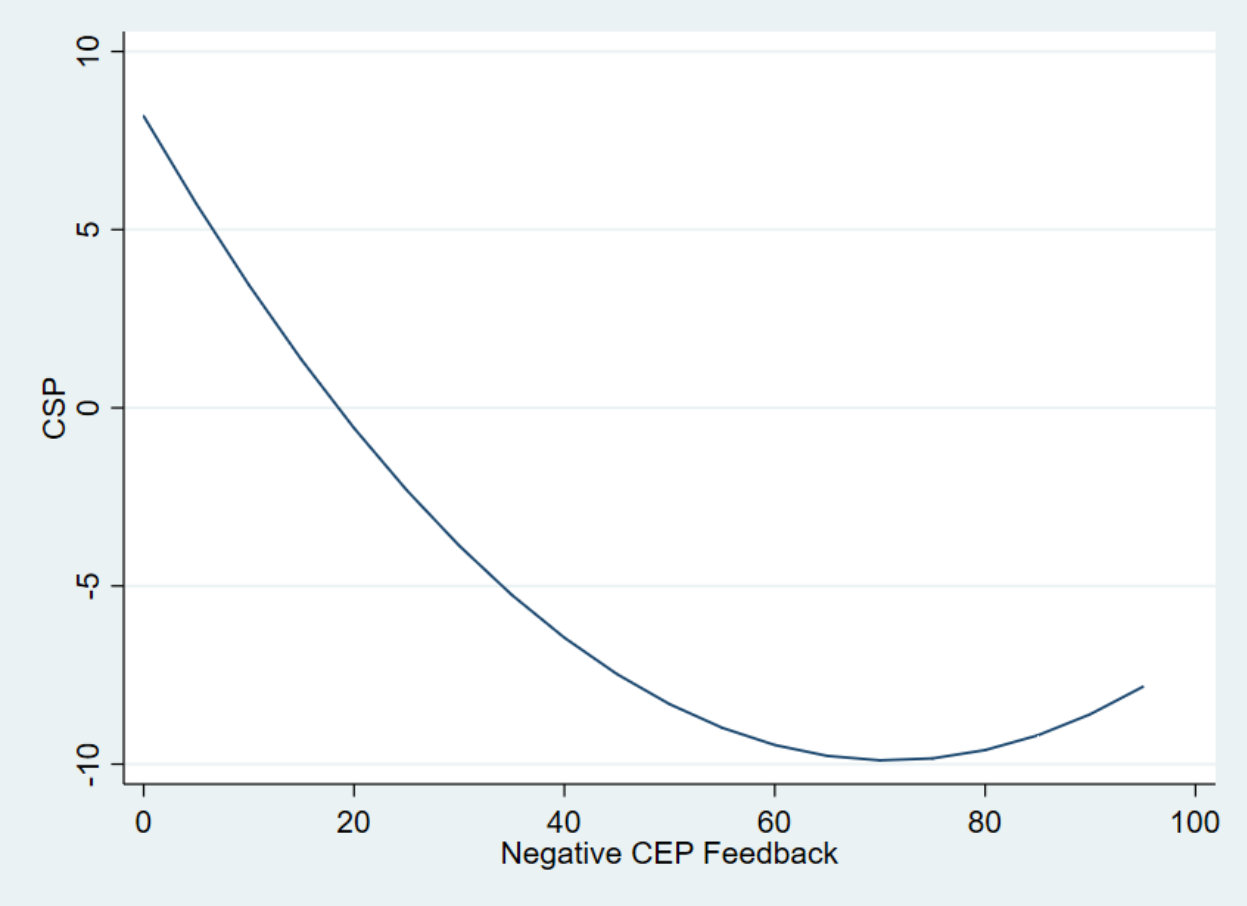

Figure 2.1 The Relationship between Negative Discrepancy of Environmental Performance and Corporate Social Performance

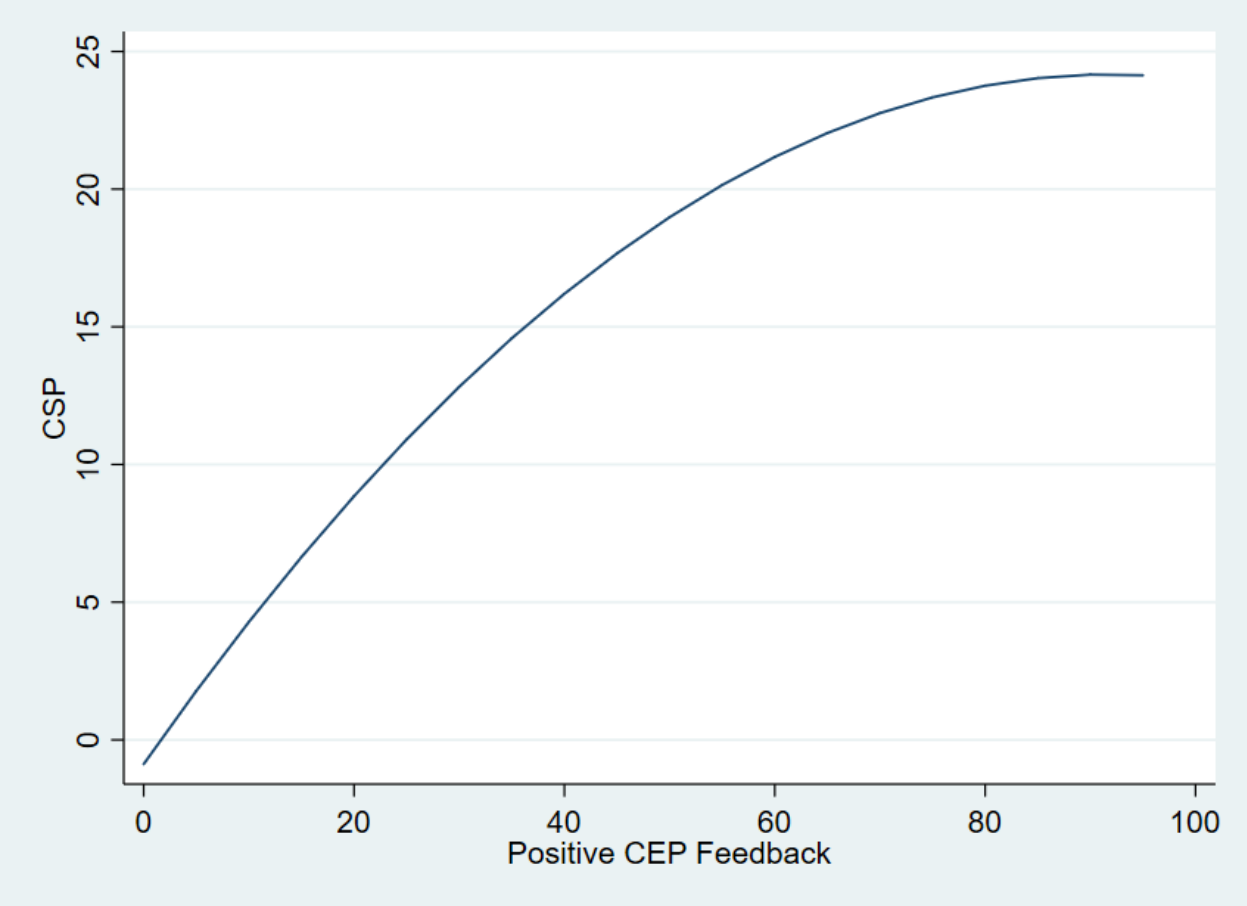

Figure 2.2 The Relationship between Positive Discrepancy of Environmental Performance and Corporate Social Performance

ESSAY #3: THE LIMITS TO VOLUNTARY GOVERNANCE INITIATIVES: THE UN GLOBAL COMPACT AND CORPORATE SOCIAL RESPONSIBILITY

ABSTRACT

Research has yet to empirically validate the limits of the United Nations Global Compact (UNGC) on corporate social responsibility (CSR). Conceptualizing the UNGC as a transnational governance and a normative institution, I develop a framework that highlights the optimal conditions for the UNGC to play an effective role in facilitating firms' socially desirable practices. I argue that the positive impact of the UNGC on CSR is likely to wear off over time. The results suggest an inverse U-shaped relationship between the level of UNGC adoption and CSR. I also find that national institutions positively moderate the UNGC-CSR link, such that the inverted U-shape is steeper when national institutions are stronger. I build on the institutional theory and theorize that national governance institutions (via the quality of national institutions) and voluntary governance institutions (via compliance with the UNGC) will jointly influence CSR. However, the UNGC adopters exhibit compliance risks of violating the UNGC principles simultaneously, as my analyses show a U-shaped relationship between the UNGC adoption and corporate violations of the UNGC principles. Empirical analyses using multi-industry panel data sample of 5,813 listed firms from 62 countries during 2004-2019 support my predictions.

Keywords: Corporate social responsibility (CSR); the UN Global Compact; national institutions; private governance; irresponsibility; compliance risks

The Limits to Voluntary Governance Initiatives: The UN Global Compact and Corporate Social Responsibility

INTRODUCTION

Research assessing cross-country differences in firms' corporate social responsibility (CSR) behavior has focused on either the role of public governance via national institutions (Ioannou & Serafeim, 2012; Young & Makhija, 2014) or the impact of private (transnational) governance institutions such as the UN Global Compact (UNGC) (Berliner & Prakash, 2014, 2015; Schembera, 2018). Though some recent studies have explored the influence of both national institutional context and private industry initiatives on firms' pro-social activities (e.g., Goerzen, Iskander, & Hofstetter, 2020), they analyze the separate or indirect effects, rather than the interactive effects, of country-level institutions and private third-party interventions. Despite the call for greater scholarly attention to the possible interaction between private and public governance on corporate strategies and performance (Aragon-Correa, Marcus, & Vogel, 2020; Knudsen, 2011; Vogel, 2008, 2010), both theoretical and empirical research that examines these joint effects is limited. The purpose of this study is to investigate two research questions: 1) What is the relationship between private voluntary governance institutions (via the compliance with the UNGC) and corporate social responsibility (CSR)? 2) How does public governance (via the quality of national institutions) condition this relationship?

In recent years, the world has increasingly recognized the importance of businesses' role in addressing social and environmental problems, in order to achieve sustainable development. This has led to a growth in non-state-based, voluntary, normative institutional initiatives such as the UN Global Compact, the Global Reporting Initiative, and the UN

Sustainable Development Goals (SDGs). Research refers to these nonstate, voluntary, private codes of conduct as private governance (or private regulation, or 'soft law'), which is distinguished from public governance based on formal rules of law and state regulations (Scherer & Palazzo, 2011; Vogel, 2008, 2010). I focus on the UNGC and conceptualize it as a private governance and a normative institution, as it is the world's largest voluntary CSR initiative and has extensive impact on firms around the globe. Global firms have increasingly accepted and participated in the UNGC, a voluntary initiative that provides standards and principles of responsible business practices. While the voluntary institutional initiatives seek to provide governance solution to public regulations and promote firms to 'do good', results on the effectiveness of private governance in changing firm behavior seem mixed and inconclusive (Berliner & Prakash, 2014, 2015; Goerzen et al., 2020; Voegtlin & Pless, 2014; Voegtlin & Scherer, 2017).

Using a sample of US listed firms, Berliner & Prakash (2015) found that the UNGC signatories undertake strategic shirking and only take symbolic, low-cost actions to improve their human rights and environmental dimensions. The UNGC has not yet demonstrated the capacity to improve participating firms' CSR efforts and performance (Berliner & Prakash, 2014; Sethi & Schepers, 2014). Based on analyses of the UNGC participants from three countries (Spain, France, and Japan), other scholars found that adopting the UNGC positively influences firms' CSR performance, which in turn positively affects corporate financial performance (Ortas, Álvarez, & Garayar, 2015). However, previous studies only examined this line of inquiry based on limited samples or within a short time frame. Despite some evidence on the effects of the UNGC, we still understand little about whether the implications

of the UNGC differ across a global context over the long run. In other words, how the efficacy of private governance (i.e., the UNGC) differs across national institutional context is under-explored and remains a puzzle. Although private governance such as the UNGC has been proposed to compensate for the shortcomings and regulatory failures of national institutions, the discussion of how voluntary regulatory pressure is integrated with state-based regulations has been mostly conceptual (e.g., Aragon-Correa et al., 2020; Vogel, 2008, 2010).

Prior work shows that good state governance and well-functioning institutions of a country will affect corporate participation and compliance level of the UNGC (Bennie et al., 2007; Knudsen, 2011). However, how firms from different institutional context differ in their engagement of realizing the UNGC values and principles still lacks both theoretical explanations and empirical tests (Doh, Husted, & Yang, 2016). The little empirical evidence on the role of state governance institutions suggests that researchers should pay more attention to the interactions of private and state regulations in driving firm behaviors and outcomes (Vogel, 2008). The lack of systematic empirical evidence regarding the link between the UNGC, national governance institutions, and firms' CSR practices in different conditions motivates me to provide a fresh perspective on the relative effectiveness of the UNGC in the presence of different levels of national institutional quality. To better understand the impact of institutional pressures on firm behavior, I build on institutional theory and develop an integrative framework to explain the combined effects of national and transnational institutional factors, namely, the interplay between national institutional quality and the UNGC in facilitating firms' socially desirable conduct.

In particular, I propose a curvilinear (inverse U-shaped) relationship between the

level of UNGC adoption and CSR. My core argument is that the positive impact of the UNGC on promoting CSR is likely to wear offer over time, with the highest CSR performance occurring at an intermediate level of the UNGC adoption. The limit to the effect of the UNGC exists mainly because of the symbolic nature of adopting the UNGC (Perez-Batres, Doh, Miller, & Pisani, 2012) which acts as a legitimacy insurance. After a certain point when firms' legitimacy is secured, firms' motivation to substantively improve CSR should be diminished. Moreover, the salience of the UNGC commitment might be reduced over a period of time, as multiple organizational goals compete for managerial attention (Ocasio, 1997) and organizational resources, leaving less to be allocated to CSR. I further propose that national institutional quality will positively moderate this curvilinear relationship, such that at both sides of the inverted U-shape, the effect of the UNGC adoption on CSR is enhanced as national institutional quality increases.

In this study, I build on the institutional configuration perspective positing that different types of institutions will jointly exert constraints and create incentives to affect individuals' actions and decision-makings (Scott, 2005; Stephan, Uhlaner, & Stride, 2015). I test my predictions based on a comprehensive sample of global firms and using a longer time period (2004 to 2019) than prior research. Thus, I examine the dynamic effect of the UNGC in a full period of time rather than viewing the UNGC adoption as a one-time single event. I constructed a unique dataset of 5,813 listed companies across all industries from 62 countries (including both emerging markets and developed markets firms) from 2004 to 2019. This study contributes to literatures on IB, CSR, and institutional theory in several ways. First, this study not only enhances our understanding of institutional drivers of firm behavior by

resolving the contradictory propositions on the effects of the UNGC and national institutions, but also goes beyond testing institutional drivers of corporate conduct to examine the interplay between national governance institutions and private business regulations like the UNGC. This paper contributes by providing nuanced theoretical mechanisms of the diminishing returns to the adoption of voluntary initiatives. This study builds on and advances the institutional theory by studying the interdependence of national and transnational governance institutions, as well as their relative efficacy in facilitating corporate responsible behaviors. Second, this study contributes to the IB literature by highlighting that private governance can differentially complement the effects of national institutions in different situations, which might lead to the regulatory heterogeneity across global markets. Empirically, this research is among the first few studies that provide rigorous empirical evidence through an international sample of over sixteen years and by addressing various endogeneity issues associated with the UNGC-CSR link. In the next section, I present the theoretical background and develop my hypotheses. I then describe my research methodology and empirical results, followed by a discussion of the contributions, limitations, future research directions, and implications of this work for research and practice.

THEORY AND HYPOTHESES

This study builds on institutional theory and adopts an institutional configuration perspective (North, 1990; Scott, 2005, 2013; Stephan et al., 2015) and CSR literatures to investigate under what conditions the UNGC will play a role in influencing firms' CSR activities. Firms are embedded within different institutional context, such that institutions enable or constrain corporate actions and decision-making concerned with CSR (Campbell, 2007; Ioannou &

Serafeim, 2012; Matten & Moon, 2008; Young & Makhija, 2014). Firm behaviors are subject to three types of institutions: (1) Formal or regulative institutions, constituting laws and regulations that are established and enforced by the state; (2) normative institutions that represent societal expectations of appropriate behavior for a particular industry, professional network, or social group (Scott, 2005, 2013); (3) cultural-cognitive institutions which are "the shared conceptions that constitute the nature of social reality and create the frames through which meaning is made" (Scott, 2013: 67). In this study, I focus the analyses on formal institutions (i.e., the national institutions) and a type of normative institutions (i.e., the UNGC). I further follow the institutional configuration perspective proposing that individuals' activities are "shaped jointly by the constraints, incentives, and resources provided by formal and informal institutions" (Stephan et al., 2015: 309). I contend that national institutions and the UNGC can have complementary effects on corporate behavior.

The Growth of Private Governance Institutions

Private governance (or private regulation) is the governance and regulatory institutions addressing corporate conduct through voluntary standards of 'responsible' business practices and non-state enforced codes of conduct (Goerzen et al., 2020; Vogel, 2008, 2010). Private governance constitutes a component of global business regulations whose legitimacy and enforcement are not rooted in public authority, thus it is also viewed as 'governance without government' (Vogel, 2010, 2008). With the purpose of fostering corporate engagement with responsible practices and sustainable development, private governance institutions and regulations are based on 'soft laws' characterized by non-legal forms of standards (Scherer & Palazzo, 2011; Vigneau, Humphreys, & Moon, 2015; Waddock, 2008). These voluntary

standards that provide guidelines and create new expectations for firms to commit to CSR activities are governance solutions to compensate for the ineffectiveness of state-based regulations, especially under the conditions where national governance institutions are weak, inadequate, or missing (Goerzen et al., 2020; Mörth, 2004; Voegtlin & Pless, 2014; Vogel, 2010). The private, non-state governance of corporate behavior (e.g., via the UNGC) seeks to institutionalize CSR involving multiple stakeholders and promote firms' engagement in socially desirable practices (Brammer, Jackson, & Matten, 2012; Waddock, 2008). The increasing business adoption of the UNGC, a type of normative institutions and the largest voluntary CSR initiative, over the last two decades has witnessed the growth of private governance of corporate behaviors and outcomes across the globe.

Implications of the UN Global Compact

As the world's largest voluntary business code and principle-based institutions, the UNGC encourages global firms to support sustainable and socially responsible practices, thereby promoting corporate responsibility and advancing social and economic development. The UNGC calls for the alignment of business operations and strategies with 10 principles in the areas of human rights, labour standards, the environment, and anti-corruption (UNGCI, 2015). Firms that adopt the UNGC are required to submit an annual report on their engagement with the 10 principles (the Communication on Progress or COP). Failing to live up to these requirements or non-communicating within the required time period leads a signatory firm to be expelled from the UNGC program.

However, as voluntary business codes, the UNGC is criticized for that its entry barrier to become signatories is low and that it does not monitor participants' actual progress

on behavioral outcomes. The credibility and ability of the UNGC to hold signatory firms more accountable and induce participants to effectively improve CSR efforts are questioned (Sethi & Schepers, 2014). There are more than 16,000 signatories to the UNGC across 156 countries, most of which are business actors (UNGCI, 2020). With the growth of business acceptance of private regulations like the UNGC, the success of the UNGC in changing firm behavior and outcomes is believed to be limited (Sethi & Schepers, 2014; Berliner & Prakash, 2014). Particularly, in the absence of clear performance standards and monitoring mechanisms, whether signatory firms that promise to commit to the UNGC principles would actually improve their outcomes on societal and environmental issues is still an unanswered question.

Given the existing critics and doubts about the efficacy of the UNGC, recent research has increasingly examined whether the UNGC plays an effective role in driving firm behavior or firm performance. For instance, membership of the UNGC could benefit corporations by influencing stakeholder perceptions, creating network opportunities, as well as gaining and maintaining good corporate image, legitimacy and reputation (Bennie, Bernhagen, & Mitchell, 2007; Cetindamar, 2007). By announcing the affiliation with the UNGC, firms signal to their investors and stakeholders that they are high-quality partners that receive endorsement by the United Nations and provide information transparency of CSR activities, which leads to a positive market reaction (Janney, Dess, & Forlani, 2009). Accordingly, corporate non-compliance with the UNGC requirements by not filing the annual COP report generates information asymmetry and non-transparency. As a result, investors and other stakeholders may raise doubts about the firms' accountability and commitment to the

values and principles of the UNGC, which generates negative stock returns (Janney et al., 2009). The commitment to the UNGC positively influences corporate market performance and creates economic values through improved multi-stakeholder management (Cetindamar, 2007; Ortas et al., 2015). Although prior studies have explored the financial performance implications of adopting the UNGC, limited research has empirically examined the influences of the UNGC on firms' CSR activities. We still do not know much about whether and how the UNGC shapes firms' changes in socially desirable behaviors or corporate outcomes on the society.

To extend our understanding of whether and how the UNGC affects firms' CSR behavior, I look at the dynamic implications of the UNGC on firms' changes in CSR practices over time, rather than viewing the UNGC adoption as one single event operationalized with a dummy indicator. Several studies have examined whether the UNGC will make firms more accountable on social and environmental issues, and generally suggested a positive association between the UNGC and CSR. Despite the fact that some firms will be delisted due to the failure to meet the UNGC requirements (Knudsen, 2011), research suggests that the UNGC signatories' CSR performance improves over time after they adopt this initiative, and that successive compliance with the UNGC principles positively affects the level of the UNGC implementation and sustainable development efforts (Berliner & Prakash, 2015; Cetindamar, 2007; Ortas et al., 2015; Schembera, 2018). In general, after committing to the UNGC principles, signatories are observed to be more responsible and more engaged in realizing the values espoused by the UNGC. Therefore, I believe that signatory firms, especially those who successively comply with the UNGC principles, not only win

continuous stakeholder support and increased confidence of investors, but also conduct more socially desirable practices as guided by the UNGC principles. I expect that the UNGC, as a form of normative institutions and a type of private governance, will play an effective role in governing corporate conduct to meet societal expectations for some time.

Diminishing Effectiveness of the UNGC Adoption on CSR

Nevertheless, I posit that this positive impact of the UNGC on promoting CSR is likely to wear off over time, such that there is an inverse U-shaped relationship between the UNGC adoption and CSR. I provide my rationales explaining the inverted U-shaped relationship by combining the legitimation and competition (of managerial attention and organizational resources) effects where the two countervailing forces gradually dominate over the other at different time points (Chang & Park, 2005; Haans, Pieters, & He, 2016). First, the UNGC adoption represents a symbolic management of CSR (Perez-Batres et al., 2012) and acts as a legitimacy insurance. Adopting the UNGC brings about benefits such as positively influencing stakeholder perceptions, creating network opportunities, as well as gaining and maintaining good corporate image, legitimacy, and reputation. However, after a certain point when firms' legitimacy is secured, their motivation to substantively improve CSR will be diminished. Second, decision makers attend more to a specific organizational goal when it becomes more salient (Ocasio, 1997). The salience of the commitment to the UNGC program tends to be decreased over a period of time, as multiple organizational goals will compete for managerial attention as well as organizational resources, thereby leaving less resources and capabilities allocated to implementing CSR.

That is, the line of the legitimation effect "takes on a concave or logarithmic shape"

(Haans et al., 2016: 1179), such that the net effect of the legitimation and competition effects is then an inverted U-shaped relationship (Chang & Park, 2005) between the UNGC adoption and CSR. Being a UNGC participant, one the one hand, offers benefits such as legitimacy and stakeholder recognition, as well as positive knowledge and capabilities spillovers, by networking with other signatory firms, sharing experiences, and learning from one another's best practices, etc. On the other hand, it also reinforces the competition of managerial attention and organizational resources, escalates costs of taking responsible actions, and even leads to potential decoupling or irresponsible practices (Perez-Batres et al., 2012; Berliner & Prakash, 2014). Namely, the nonlinear relationship between the UNGC adoption and CSR of firms exists "while the positive force increases at a decreasing rate and eventually levels off, the negative force rises quickly" (Haans et al., 2016: 1180). Therefore, firms' CSR performance will initially increase, but then after a certain point it decreases significantly with firms' adoption of the UNGC.

> ***Hypothesis 1:*** *The relationship between the level of the UNGC adoption and CSR is curvilinear (inverted U-shaped) with the highest CSR occurring at an intermediate level of the UNGC adoption.*

The Moderating Role of National Institutions

Corporate conduct varies with the differences in national institutional conditions, such that national institutions drive firms' CSR practices, the content of CSR programs, and CSR engagement (Campbell, 2007; Ioannou & Serafeim, 2012; Maignan & Ralston, 2002; Matten & Moon, 2008; Orlitzky, Louche, Gond, & Chapple, 2017). National institutional arrangements in political-economic systems and social aspects play a significant role in

shaping businesses' CSR practices and performance (Gjølberg, 2009a; Hiss, 2009; Jackson & Apostolakou, 2010). Cross-national differences in government effectiveness, as well as in enactment and enforcement of laws and regulations, are important antecedents of corporate CSR initiatives and their social and environmental impact, because enabling institutional conditions are likely to facilitate CSR or pro-social activities, known as the institutional support perspective (Aguilera, Rupp, Williams, & Ganapathi, 2007; Campbell, 2007; Maignan & Ralston, 2002; Matten & Moon, 2008; Stephan et al., 2015). While many studies focus exclusively on the separate effects of national institutions on corporate behavior, other research demonstrates that private governance institutions can substitute for the role of state-based rules and regulations where public institutions are weak (Goerzen et al., 2020; Mair & Marti 2009; Marano, Tashman, & Kostova, 2017; Stephan et al., 2015). Referred to as the institutional voids perspective in the literature, it argues that government failure or inadequate institutions may stimulate the formation of, and enhance the impact of, alternative governance institutions. However, limited work has empirically examined how public governance (via national institutions) interacts with private governance to change firm behavior. I propose an integrative view of examining the influence of national institutions and private governance simultaneously. In particular, I argue that the quality of national institutions and the degree of compliance with the UNGC will jointly affect firms' CSR activities.

Effectiveness of voluntary business codes is subject to the extent to which public and private governance institutions can reinforce one another (Vogel, 2010). The efficacy of private governance may vary with the strength of national institutions. National institutional

context also drives the cross-country differences in corporate commitment to the UNGC principles (Bennie et al., 2007; Knudsen, 2011). In the case where public governance is strong and effective, public regulations may strengthen the efficacy of the UNGC in promoting firms' CSR efforts. On the one hand, stronger national institutions will strengthen the positive association between the UNGC adoption and CSR, when the level of UNGC adoption is lower. The relevant increased costs in CSR can be mitigated by abundant resources and support provided by well-established institutional infrastructures, as well as by well-enforced laws and regulations which foster firms to act in socially responsible ways (Campbell, 2007; Maignan & Ralston, 2002; Matten & Moon, 2008; Young & Makhija, 2014). Greater institutional supports and related resources motivate the UNGC adopters to leverage such location advantages into CSR engagement. Thus, with stronger and enabling national institutions, firms are more likely to comply with the UNGC requirements (Knudsen, 2011), thereby improve CSR performance when they are in earlier stages of the UNGC adoption.

On the other hand, however, as the level of UNGC adoption increases, stronger institutional environment may reduce the firms' efforts to pursue CSR. As discussed earlier, institutional conditions providing effective government and well-enforced laws and regulations can enable firms to participate in CSR (Gjølberg, 2009b; Maignan & Ralston, 2002; Matten & Moon, 2008; Young & Makhija, 2014). That is, developed countries with stronger institutions usually already required high levels of CSR engagement. For example, in coordinated market economies, the strong national institutions and regulatory systems drive more extensive CSR practices (Fransen, 2013). Companies from such jurisdictions will likely

find it simple to acquire or maintain the UNGC status without making too many efforts to improve their CSR performance, and thus there might be a negligible change in their CSR engagement level. Conversely, the UNGC adopters from less developed countries with weaker institutions are more likely to have to make greater CSR changes to be compliant, thereby improving their CSR performance more. Furthermore, firms from weak institutional environment may be even more motivated to pursue CSR as a legitimation strategy (Marano, Tashman, & Kostova, 2017), in order to influence the positive perceptions of international stakeholders. I argue that at medium to high levels of the UNGC adoption, the incentives for firms to improve CSR is decreased in a more enabling institutional environment with well-established institutional infrastructures, whereby the positive impact of the UNGC diminishes further.

Taken together, national institutional quality positively moderates the UNGC-CSR relationship in such a way that it enhances CSR performance at lower levels of UNGC adoption (i.e., the ascending part of the inverted-U shape curve), and it enlarges the decline in CSR performance at higher levels of UNGC adoption (i.e., the descending part of the curve). Namely, at both sides of the inverted U-shape, the effect of the UNGC adoption on CSR is enhanced by national institutional quality.

Hypothesis 2: *National institutional quality will positively moderate the inverted U-shaped relationship between the level of the UNGC adoption and CSR in such a way that the inverted U-shaped relationship will be steeper in firms from countries with high institutional quality than in firms from countries with low institutional quality.*

METHODS

Sample and Data

I test my hypotheses on a global sample of publicly listed companies across all industries from both developed and emerging countries during 2004-2019 (16 years). I identify the sample firms from Thomson Reuters Eikon database from which I draw all the CSR related variables. Thomson Reuters Eikon database is one of the most comprehensive secondary data sources for corporate Environmental, Social and Governance (ESG) information used by research on CSR. Thomson Reuters Eikon ESG scores enhance and replace the formerly ASSET4 ESG Ratings, often used by prior studies on CSR. Eikon tracks more than 400 ESG metrics to evaluate a company's ESG commitment and effectiveness across ten major themes (such as workforce, product responsibilities, resource use, environmental innovation, human rights and so on) based on companies' own disclosure and a wide range of other sources such as NGO websites, stock exchange filings, and media news sources etc. Thomson Reuters ESG scores and assessment items incorporate a comprehensive set of stakeholder dimensions like employee development, customer satisfaction, partnerships with suppliers, community investment, and environmental protection, etc.

I compile the data on the adherence to the UNGC program from the United Nations Global Compact Initiative (UNGCI) reports. The UNGCI reports record a signatory firm's country of origin and membership status information, such as when a firm starts to be an active member of the UNGC, whether a firm submits the progress report annually, and when a firm is expelled from the UNGC, etc. Accounting and financial data are also retrieved from Eikon, complemented by Compustat databases. Following previous studies (Knudsen, 2011; Tashman, Marano, & Kostova, 2019), national institutions variables are drawn from the

World Bank's datasets on the Worldwide Governance Indicators (WGI). Country competitiveness variables are obtained from the Global Competitiveness Index reports provided by the World Economic Forum.

Variables and Measures

Dependent variables: To measure *corporate social responsibility (CSR)*, I rely on the ESG metrics obtained from Thomson Reuters Eikon database, which is extensively used for CSR research. Following prior studies (e.g., Barnett & Salomon, 2012; Aouadi & Marsat, 2018), I measure CSR using the composite variable of the environmental, social and governance (ESG) scores, obtained from Refinitiv Eikon database.

Independent variable: To measure private governance via the *level of the UN Global Compact adoption*, I use the number of years that a firm has been an active UNGC member that captures a firm's successive commitment to the UNGC (Berliner & Prakash, 2015).

Moderator: *National institutions* are measured with the meta-index of World Governance Index (WGI) scores. The WGI measures the quality of state governance and institutions in six areas: *Voice and Accountability, Political Stability and Absence of Violence/Terrorism, Government Effectiveness, Regulatory Quality, Rule of Law, and Control of Corruption.* While I use a meta-index of WGI for the main analysis, I use the separate dimensions of WGI and perform additional analyses for robustness checks.

Control variables: *Firm size* is measured with natural logarithm of total assets of a firm in each year. *Firm age* is calculated as the number of years since a firm's first listing. *Firm financial performance* is measured with return on assets (ROA), which is calculated as net income divided by total assets. *Debt ratio* is measured with the ratio of long-term debt to

total assets. I measure *capital intensity* as the ratio of total assets to total sales. *R&D intensity* is measured as research and development expenses divided by total sales. *Advertising intensity* is measured as the ratio of advertising expenses to total sales. For the missing data of advertising and R&D expenditures, I follow previous research (Strike et al., 2006) and use industry averages to replace missing values. I control for other country-level factors such as *international competitiveness*, which is measured with the scores of Global Competitiveness Index (GCI). The GCI covers a broad range of sustainability dimensions, such as a country's market size, business dynamics, and macroeconomic stability etc., which may affect firms' engagement with CSR practices (Gjølberg, 2009b; Knudsen, 2011). I also control for *industry, country, and year* fixed effects in the regression models. For robustness checks, I use alternative models controlling for *firm* and *time* fixed effects.

Empirical Strategy and Data Analyses

I acknowledge that this research may suffer from potential endogeneity issues arising from different sources such as sample selection bias, reverse causality, and unobserved heterogeneity. As my analyses are restricted to firms that are the UNGC signatories, I use Heckman's (1979) two-stage selection model, to address potential self-selection bias (Shaver, 1998) and to obtain unbiased coefficients.

In the first-stage Heckman model, I use Probit analysis where the dependent variable is a dummy indicating a firm's decision to adopt the UNGC. Thus, it estimates the probability of a firm's UNGC adoption in a broader sample that includes all public firms available in Refinitiv Eikon database, covering both the UNGC signatories and non-signatories. The first-stage sample includes 65,966 firm-year observations for 6,391 firms.

The Heckman first-stage model included all the explanatory and control variables as in the main analysis. I also entered the average number of years of adopting the UNGC within a firm's same industry excluding the focal firm, i.e., *industry average level of UNGC adoption*, as the exclusion restriction, since at least one variable in the first-stage should not be introduced in the second stage (Certo, Busenbark, Woo, & Semadeni, 2016). The average level of adopting the UNGC program in an industry may impact a firm's decision to participate in the UNGC (Schembera, 2018), but do not directly influence a firm's actual activities and performance in CSR. Based on the first-stage regression model, I computed an inverse Mills ratio (IMR) which is included in all models reported in the paper. In the second stage, I included the IMR in all the specifications that use robust standard errors clustered by firm. The number of observations in the final dataset for my main analyses is then reduced to 36,886 firm-year observations for 5,813 listed firms across all industries from 62 countries during 2004-2019.

To identify under what conditions and how the UNGC is interrelated with national institutions to shape corporate conduct, I apply industry, country and year fixed effects estimator, to mitigate the concerns for unobserved time-variant heterogeneity. I lag all the independent variables by one year to address possible reverse causality and strengthen causal inferences. For robustness checks, I use random intercept multi-level models as alternative empirical specifications to test the robustness of my results. As each firm is hierarchically nested within an industry which is nested in a country, multilevel modelling helps us to account for non-independence across observations (Peterson, Arregle, & Martin, 2012) and unobserved effects on firm-level CSR. Compared to single level regressions, multilevel

models allow us to better reduce endogeneity and omitted-variable bias.

RESULTS

Table 3.1 presents the descriptive statistics and pairwise correlations of the variables used in the main analyses. Variance inflation factors (VIFs) are below 3 for all variables, raising no concern about multicollinearity. On average, the firms in my sample are about 23.65 years old since their IPO. Significant variations are shown across the sampled firms for the measures of CSR, profitability, intangible resources, national institutional quality, and the level of UNGC adoption. The number of years that the firms adopt the UNGC ranges from zero to fourteen years, with an average of about one year.

Insert Table 3.1 about here

Table 3.2 reports the results for the test of the main hypotheses. Model 1 in Table 3.2 contains the controls and main explanatory variable – *the level of UNGC adoption*. Model 2 adds the quadratic term of *the level of UNGC adoption.* Model 3 tests the effects of the moderator variable – *national institutional quality* on the UNGC-CSR relationship, by introducing the interaction terms of the UNGC and national institutions. I rely on Model 3 (the fully specified model) to interpret the linear and nonlinear effects of the UNGC adoption, as well as the interactive effects of the UNGC and institutional quality.

The positive and significant coefficients for the linear term of the UNGC variable in Model 3 of Table 3.2 ($\beta=1.688$, $p<0.001$) indicate that commitment to the UNGC is positively associated with CSR, suggesting that the UNGC seem to work well in promoting firms to 'do good'. However, the quadratic term of the UNGC adoption shows that CSR first increases but then decreases (($\beta=-0.112$, $p<0.001$) as the number of years of adopting the

UNGC increases. This result suggests a curvilinear (inverse U-shaped) relationship between the level of UNGC adoption and CSR, confirming Hypothesis 1. To better present my findings, I draw a graph of this inverse U-shaped relationship illustrated in Figure 3.1.

Insert Table 3.2 about here

Hypothesis 2 predicts that national institutional quality positively moderate the inverted U-shaped relationship between the UNGC adoption and CSR. The interaction term between the linear term of UNGC adoption and national institutions is positive and significant (β=0.248, $p<0.05$), and the second-order interaction term is negative and significant (β=-0.020, $p<0.10$). The results provide support for Hypothesis 2. To clarify the nature of the interaction effects, I plotted the results as displayed in Figure 3.2. The graph shows that the inverted U-shaped relationship is steeper in firms from countries with high institutional quality than in firms from countries with low institutional quality, further confirming Hypothesis 2.

Insert Figures 3.1 and 3.2 about here

Validity of the Inverted-U Shape Relationship

I draw on the suggestions of Lind and Mehlum (2010), to assess the validity of the U-shaped relationship between the UNGC adoption and CSR. First, I tested whether the higher-order (quadratic) term is significant and of the expected sign. As confirmed by the results I reported earlier, the squared term of the UNGC adoption indeed is significant and has a negative sign, as opposed to the direct term of the UNGC adoption with a positive sign. Second, I examined the extreme point (turning point) of the level of UNGC adoption and estimated the marginal

effects of the UNGC adoption on CSR. When the level of UNGC adoption=2, the slope dy/dx =1.294 (p=0.000); when the level of UNGC adoption =13, the slope dy/dx = -1.057 (p=0.000). These results support that the slope is indeed sufficiently steep at both ends of the data range of the UNGC adoption. Third, I tested whether the turning point of the UNGC adoption is located within its data range. I calculated the confidence intervals for the turning point based on Filler's standard errors. Results show that the turning point of the curve (extreme point of the UNGC adoption) is 7.5, and that the 95% confidence interval for the turning point [7.054, 7.995] is within the value range [0,14] of the level of UNGC adoption. The three-step tests confirmed a perfect inverted-U shape relationship between the level of UNGC adoption and CSR.

Robustness Checks

Alternative measures of key variables. I performed several additional analyses to test the robustness of my results. First, I use alternative measure of the dependent variable. In the main analysis, I use the original ESG scores to proxy CSR. For robustness checks, I rely on the industry-adjusted measures of CSR, calculated as a firm's ESG score minus the average ESG score of all firms within a same industry defined by three-digit NAICS codes, excluding the focal firm. Results using the alternative dependent variable are highly consistent with my findings reported in the main analyses. Further, I use separate scores of environmental and social dimensions to measure CSR, obtaining largely consistent results. In addition, I select the single WGI dimensions, such as *Government Effectiveness*, *Rule of Law*, and *Regulatory Quality,* as alternative measures of national institutions. I replicate the analyses reported in Table 3.2 using the single WGI indexes, obtaining similar results.

Insert Table 3.3 about here

Alternative estimation models: Multilevel modeling. Then I re-run the main analyses with alternative empirical specifications. Specifically, I test my hypotheses using random intercept multilevel modeling in which firms are nested within countries. As presented in Table 3.3, the major findings are still strongly upheld. Both the direct and quadratic terms of the level of UNGC adoption are significant and of expected sign, validating Hypothesis 1 on the curvilinear (inverted-U shape) relationship between UNGC adoption of CSR. The interaction terms between national institutional quality and both the linear and squared terms of the UNGC adoption are observed to be significant and of the right sign, supporting Hypothesis 2 on the moderating effect of national institutions on the inverse U-shaped relationship.

Post-hoc Analysis: Compliance Risks - Corporate Violation of the UNGC Principles

Research suggests that the UNGC members may experience increases in both responsible and irresponsible practices (Berliner & Prakash, 2014). This is not surprising, as previous studies have documented that firms can be responsible and irresponsible simultaneously (Mishina, Dykes, Block, & Pollock, 2010; Strike, Gao, and Bansal, 2006), given that CSR and CSI are not at the opposite ends of a continuum. CSI are negative events related to social, environmental, and corporate governance issues that are disclosed by the media or external stakeholders, including consumer complaints and boycott, forced or compulsory labor, scandals linked to corruption and bribery, violation of human rights, negative environmental or community impact etc. A socially undesirable conduct could be “any publicly disclosed firm action that, under some set of conditions, a stakeholder would deem illegal, unethical, or

socially irresponsible and take action to punish" (Barnett, 2014; p.697). A firm that is actively engaged in addressing stakeholder needs and demands on a long-term basis is also likely to receive more public attention and experience more CSI (Aouadi & Marsat, 2018). The UNGC signatories may still conduct CSI just as their non-signatory counterparts do (Berliner & Prakash, 2014), thereby 'doing good' does not necessarily offset 'doing bad' (Greenwood, 2007).

I performed post-hoc analyses that particularly investigate the UNGC signatories' CSI related to violating the UNGC principles. For instance, I focus on the CSI incidents that are deemed as violations of human rights protection, environmental responsibility, labor rights, and anti-corruption commitment, under the framework of the UNGC principles. To measure *corporate violations of the UNGC principles*, I rely on the data on the total number of incidents reflecting that a firm has violated the UNGC principles in a given year, obtained from the RepRisk database. RepRisk is one the most comprehensive secondary data sources on negative ESG issues, providing a large variety of metrics of CSI events taking place across locations of a focal firm.

Insert Table 3.4 about here

As presented in Model 3 in Table 3.4, I found a U-shaped relationship between the level of UNGC adoption and firms' violations of the UNGC principles. It suggests that with the adoption of the UNGC, corporate social irresponsibility (CSI) will first decrease (β=-0.036, $p>0.10$) within a short time period and then after a certain point, firms' CSI increases significantly (β=0.005, $p<0.01$). I also examined the marginal effects of this U-shaped relationship, drawing on the recommendations of Lind and Mehlum (2010) on the

validation of the existence of a U shape. I calculated the turning point of the effect of UNGC on CSI. The results show that the U-shape curve turns when the level of UNGC adoption = 3.6, and that the extreme point is within the data range of the UNGC adoption [1, 14].

Insert Figure 3.3 about here

The U-shaped relationship between the UNGC and CSI seems to mirror the inverted U-shaped relationship between the UNGC and CSR, which further acknowledges that the positive impact of the UNGC on promoting firms' socially desirable practices appears to diminish over time. In Figures 3.3, I graphically present the U-shaped relationship between the UNGC adoption and firms' violations of the UNGC principles. As the graph shows, the positive impact of the UNGC on reducing CSI also faces a ceiling, just like its positive effect on promoting CSR. I also expect that national institutions and the UNGC can work synergistically to reduce CSI. However, as reported in Model 3 of Table 3.4, I did not find a significant interaction effects between national institutions and the UNGC on CSI. It suggests that the UNGC does not interact with national institutions to affect CSI, but rather they work independently to influence CSI. Another finding worth noticing in Table 3.4 is that national institutional quality is negatively associated with CSI (i.e., corporate violations of UNGC principles). Given that CSI activities are disclosed by the media or external stakeholders rather than the firms per se, I cannot simply draw a conclusion that stronger national institutions discourage CSI. Instead, there are other factors arising from stronger national institutional conditions, such as greater press freedom, higher degree of globalization, and better infrastructures, that might mediate or condition the relationship between national institutions and CSI, which merits further discussions in future work.

DISCUSSION AND CONCLUSIONS

Conclusions and Contributions

Prior research has examined the individual effects of national institutions and private governance respectively on firms' social impact or changes in pro-social behavior, but empirical work on the joint effects of public and private governance is rare. Drawing on the institutional theory and CSR literatures, this study seeks to untangle the interrelationships between public and private governance by examining how national institutional conditions moderate the impact of the UNGC on corporate conduct. This study deepens our understanding of the efficacy of voluntary initiatives (i.e., the UNGC) by proposing 1) a curvilinear (inverse U-shaped) relationship between the UNGC and CSR, and 2) the positive moderating effect of national institutions on this curvilinear relationship. My findings suggest that the UNGC does play a positive role in promoting CSR, but its effect will be attenuated over time. More specifically, CSR diminishes beyond lower levels of UNGC adoption, turning negative beyond intermediate levels of the UNGC adoption. At low levels of the UNGC adoption, stronger national institutional quality will reinforce the positive relationship between the UNGC and CSR, while at high levels of the UNGC adoption, stronger national institutional quality will enlarge the declining relationship between the UNGC adoption and CSR.

This research was motivated by the elusive conclusions about the relative efficacy of voluntary CSR initiatives in shaping corporate responsible practices, as well as the under-explored impact of regulatory heterogeneity around the world across national institutional contexts. This study contributes to the institutional theory and CSR literatures by

investigating the diminishing returns to voluntary governance initiatives (i.e., the UNGC). One primary theoretical implication of this research is that I look at the dynamic effects of the adoption of UNGC over a full period of time and provide nuanced theoretical mechanisms to explain why voluntary initiatives face a ceiling (Goerzen et al., 2020). A second contribution of this study is that it adds to the research on the complementarity between public and private governance institutions, by identifying the mechanisms of how national institutions will interact with transnational private governance institutions (i.e., the UNGC) to affect corporate responsible activities, and by providing empirical evidence that supports the institutional configuration perspective (Scott, 2005; Stephan et al., 2015).

A third theoretical implication is that this study goes beyond the debate about whether private governance influences corporate behaviors to instead examine when and how the UNGC initiative may improve or worsen CSR performance (Aragon-Correa et al., 2020; Vogel, 2008, 2010). This paper offers new insights about the effectiveness of the UNGC, under what condition the UNGC plays a role, and how the UNGC works together with national institutions to facilitate/restrain positive corporate outcomes. This study contributes to the CSR literature by following the recent calls for examining international differences in firm behavior beyond a separate aspect of institutional factors (Aragon-Correa et al., 2020; Goerzen et al., 2020; Graafland & Noorderhaven, 2020; Knudsen, 2011; Vogel, 2010). I examine the interrelations of national and transnational governance institutions, as well as their combined effects on both socially desirable and undesirable practices. This wider perspective extends findings from past research that empirically investigated the institutional drivers of CSR (e.g., Ioannou & Serafeim, 2012) by highlighting the importance of joint

effects of regulative and normative institutions. This paper not only unpacks the mechanisms through which national institutions and the UNGC influence corporate behavior, but also represents the first empirical attempt to test their joint effects in different contexts. It clarifies under what conditions national institutions and the UNGC will complement one another to change corporate behavior.

Finally, this study also adds to the emerging body of work on CSI (Lange & Washburn, 2012; Mishina et al., 2010; Strike et al., 2006), by showing that the efficacy of private governance via the UNGC seems asymmetric in influencing CSR and CSI. While prior work has empirically examined the impact of publicly disclosed CSI on firm financial risks or international expansion (Kölbel et al., 2017; Hawn, 2021), research has rarely investigated the institutional influences on or (inter)national drivers of CSI. I find that the adoption of the UNGC is positively associated with CSI (i.e., corporate violations of the UNGC principles) while it is negatively related to CSR, at later stages of the UNGC adoption. This is not counterintuitive, but instead it echos previous studies suggesting that firms can be responsible and irresponsible simultaneously and that 'doing good' does not necessarily offset 'doing bad' (Greenwood, 2007; Strike et al., 2006). Nevertheless, it indicates that the efficacy of private governance via the UNGC is asymmetric in affecting CSR and CSI, as the positive association between the UNGC and CSI is reached more quickly than the negative link between the UNGC and CSR. While the UNGC is effective in stimulating firms to engage more in CSR for some time, it does not serve as a strong constraint for CSI in general.

Another fresh perspective backing by empirical evidence in my post-hoc analyses is that national institutions and the UNGC do not work jointly to influence CSI. In testing the

possible synergy between national institutions and the UNGC on CSI, I did not find a significant interaction effect on CSI. This insignificant interaction effect provides opportunities for future work to examine the underlying mechanisms by which national and transnational governance institutions will affect CSI. On first glance this result implies that the UNGC does not interact with national institutions to influence CSI, but rather they affect CSI independently. However, firms' CSI behaviors are reported by the media or external stakeholders rather than disclosed by the firms per se, thereby I cannot simply interpret that higher CSI is triggered by weaker national institutions. Instead, strong institutional conditions are oftentimes accompanied by other facilitating factors, including more press freedom, greater degree of globalization of a country, and well-established equipment and infrastructures, that may serve as mediators or contingencies between institutional contexts and firms' CSI activities. My results underscore the importance of further exploring the mechanisms by which institutional environment facilitates or impedes the diffusion of (ir)responsible business practices. My findings also suggest the need to examine further the mechanisms that drive emerging markets firms (or firms from non-enabling institutional conditions) to undertake (ir)responsible activities.

Practical Implications

This study has important implications for practice as well. First, even if the UNGC can complement national institutions to foster responsible firm behavior, it is important for policy makers and government officials to undertake effective initiatives to improve the institutional strengths and regulatory quality, in order to promote pro-social activities and positive social impact of firms. Policy makers should recognize that firms' CSR effort is subject to

institutional factors in the national political-economic system and state regulatory framework. Thus, it is critical to provide additional incentives for firms to 'do good', such as environmental taxes or other price-based policies intended to reduce environmentally harmful activities and hence promote sustainable development. Second, the nonlinear relationship between the UNGC adoption and CSR suggests that firms might strategically conform to the normative pressures arising from the UNGC principles and even decouple their CSR outcomes from the claimed CSR commitment. Managers should not only recognize the misalignment between CSR signaling (adoption of the UNGC) and CSR behavior, but also seek to improve their actual CSR performance in order to win broader stakeholder support and achieve sustainable positive societal impact.

Limitations and Future Research

This study builds on the institutional theory and CSR literatures and follows an institutional configuration perspective to test the hypotheses on a comprehensive sample of global firms from both emerging and developed countries with significant variations in national institutional quality. The heterogeneous degree of compliance with the UNGC among the sampled firms and the longitudinal panel data on firm behavior also allow me to provide robust, systematic, empirical evidence for the joint effects of public and private governance institutions on corporate outcomes. Nevertheless, I acknowledge several limitations in this study that provide opportunities for future research. First, my analysis is restricted to public companies adopting the UNGC, thus the findings may not be generalized to non-listed firms that adopt the UNGC program or other voluntary initiatives. Second, while I examine broadly the impact of national and transnational governance institutions on corporate conduct, I do

not consider precisely which single aspects of CSR are influenced by national institutional arrangements (Brown & Knudsen, 2015; Fransen, 2013), or which components of ineffective national institutions the UNGC can compensate for. Future research could examine how weak national institutions create incentives and opportunities for the substitution of alternative institutional arrangements, or how firms' single dimensions of CSR and CSI are affected by a particular part of national institutional framework.

Third, I do not distinguish among the different types of firms, such as purely domestic firms and multinational companies. Thus, I am not able to assess the differential implications of institutional configurations for domestic versus multinational firms. Related to this point, as I focus exclusively on the influence of firms' domestic governance institutions, I do not consider the potential impact of host country institutional environment on firms' CSR efforts if firms expand into a foreign country (Rathert, 2016). I suggest that future research could extend my study by exploring corporate positive and negative behaviors in the context of international expansion, as well as the impact of host country institutional settings. For example, future work could examine the links between host country institutions, firms' FDI location choices, and irresponsible practices, in order to tease out the relationship between the single dimensions of country-level institutions and firms' CSI activities. Finally, my findings demonstrate that the UNGC plays a relatively effective role in affecting firms' CSR and CSI behaviors, but I do not address how firm behaviors change or evolve specifically, with the institutionalization of the UNGC around the globe. I encourage future research to extend this study of the relative efficacy of the UNGC by examining the antecedents of compliance risks (violations of the UNGC principles) and potential decoupling

behaviors of the UNGC signatories (i.e., the discrepancy between a firm's CSR reporting and its actual CSR performance), given that the commitment to the UNGC still gives rise to decreases in CSR and increases in CSI.

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Table 3.1 Descriptive Statistics and Correlations of Variables

	Variable	Mean	SD	1	2	3	4	5	6	7	8	9	10	11
1	CSR	42.795	20.481	1										
2	Level of UNGC adoption	0.947	2.602	0.418	1									
3	National institutional quality	0.201	0.829	0.036	-0.046	1								
4	Firm size [a]	22.323	1.611	0.470	0.274	-0.090	1							
5	Debt ratio	0.967	1.493	0.036	0.018	-0.037	0.211	1						
6	Firm age	23.645	37.485	0.161	0.080	0.069	0.178	0.017	1					
7	Firm financial performance	0.053	0.078	0.060	-0.001	-0.057	-0.036	-0.152	-0.003	1				
8	International competitiveness	5.308	0.406	-0.054	-0.149	0.726	-0.032	0.002	0.047	-0.053	1			
9	R&D intensity	0.163	0.868	-0.131	-0.050	0.059	-0.277	-0.065	-0.049	-0.359	0.029	1		
10	Advertising intensity	0.256	1.741	-0.120	-0.045	0.052	-0.260	-0.057	-0.042	-0.363	0.026	0.761	1	
11	Capital intensity	3.375	5.467	-0.095	-0.072	0.043	0.030	0.107	-0.064	-0.346	0.005	0.494	0.472	1

Note: [a] Natural logarithm.

Table 3.2 The Effects of the UNGC Adoption and National Institutions on CSR

	CSR		
	(1)	(2)	(3)
Firm size [a]	5.603***	6.185***	6.155***
	(0.092)	(0.115)	(0.117)
Debt ratio	-0.231***	-0.315***	-0.311***
	(0.062)	(0.063)	(0.063)
Firm age	0.028***	0.027***	0.027***
	(0.004)	(0.004)	(0.004)
Firm financial performance	8.865***	10.208***	10.145***
	(1.197)	(1.201)	(1.201)
International competitiveness	-1.390	-1.723+	-1.674+
	(0.926)	(0.927)	(0.927)
R&D intensity	1.034***	1.067***	1.065***
	(0.131)	(0.130)	(0.130)
Advertising intensity	0.989***	0.815***	0.823***
	(0.062)	(0.065)	(0.065)
Capital intensity	-0.410***	-0.432***	-0.432***
	(0.024)	(0.024)	(0.024)
National institutional quality	1.067	0.963	0.829
	(1.107)	(1.106)	(1.114)
Inverse mills ratio (IMR)	-5.578***	-3.650***	-3.727***
	(0.191)	(0.308)	(0.312)
Level of UNGC adoption	0.116*	1.764***	1.688***
	(0.054)	(0.207)	(0.212)
Level of UNGC adoption – squared		-0.118***	-0.112***
		(0.014)	(0.014)
Level of UNGC adoption × National institutional quality			0.248*
			(0.114)
Level of UNGC adoption – squared × National institutional quality			-0.020+
			(0.011)
Intercept	-59.837***	-76.850***	-76.197***
	(5.447)	(5.788)	(5.818)
Industry fixed effects	Yes	Yes	Yes
Country fixed effects	Yes	Yes	Yes
Year fixed effects	Yes	Yes	Yes
F statistic	2248.305***	2085.649***	1810.198***
adj. R^2	0.4681	0.4688	0.4689
N	36886	36886	36886

Notes: [a] Natural logarithm. Robust standard errors are in parentheses. + $p < 0.10$, * $p < 0.05$, ** $p < 0.01$, *** $p < 0.001$

Table 3.3 Robustness Tests: Multilevel Models as Alternative Specifications

	CSR		
	(1)	(2)	(3)
Fixed effects			
Firm size [a]	5.731***	6.475***	6.450***
	(0.102)	(0.131)	(0.131)
Debt ratio	-0.164**	-0.272***	-0.269***
	(0.060)	(0.061)	(0.061)
Firm age	0.047***	0.046***	0.046***
	(0.003)	(0.003)	(0.003)
Firm financial performance	1.851	3.448**	3.446**
	(1.177)	(1.189)	(1.189)
International competitiveness	4.886***	4.289***	4.311***
	(0.644)	(0.648)	(0.648)
R&D intensity	1.057***	1.111***	1.110***
	(0.149)	(0.149)	(0.149)
Advertising intensity	0.877***	0.662***	0.669***
	(0.074)	(0.078)	(0.078)
Capital intensity	-0.410***	-0.442***	-0.442***
	(0.023)	(0.024)	(0.024)
National institutional quality	0.771+	1.104*	0.979*
	(0.442)	(0.446)	(0.449)
Inverse mills ratio (IMR)	-4.214***	-1.833***	-1.899***
	(0.220)	(0.342)	(0.343)
Level of UNGC adoption	0.915***	2.991***	2.902***
	(0.112)	(0.254)	(0.256)
Level of UNGC adoption - squared		-0.148***	-0.140***
		(0.016)	(0.016)
Level of UNGC adoption × National institutional quality			0.363**
			(0.141)
Level of UNGC adoption - squared × National institutional quality			-0.028*
			(0.012)
Constant	-99.394***	-119.791***	-119.146***
	(4.049)	(4.619)	(4.626)
Random effects			
Industry level			
σ^2 Level of UNGC adoption	-1.649	-1.552+	-1.522+
	(1.033)	(0.906)	(0.837)
σ^2 Constant	0.922***	1.014***	1.006***
	(0.264)	(0.231)	(0.233)
Country level			
σ^2 Level of UNGC adoption	0.252***	0.229***	0.221**
	(0.067)	(0.069)	(0.069)
σ^2 Constant	2.386***	2.396***	2.397***
	(0.031)	(0.031)	(0.031)
N	36886	36886	36886
Wald chi2	14906.87***	15025.89***	15033.57***
LR chi2	9203.04***	9207.35***	9212.08***

Notes: [a] Natural logarithm. Robust standard errors are in parentheses. + $p < 0.10$, * $p < 0.05$, ** $p < 0.01$, *** $p < 0.001$

Table 3.4 Post-hoc analysis: Poisson Regression Models on Corporate Violations of the UNGC Principles

	Violations of the UNGC Principles		
	(1)	(2)	(3)
Firm size [a]	0.649***	0.627***	0.626***
	(0.016)	(0.017)	(0.017)
Debt ratio	-0.025*	-0.022*	-0.022*
	(0.011)	(0.011)	(0.011)
Firm age	-0.001*	-0.001*	-0.001*
	(0.000)	(0.000)	(0.000)
Firm financial performance	0.867*	0.796*	0.796*
	(0.367)	(0.366)	(0.364)
International competitiveness	-0.160	-0.116	-0.112
	(0.193)	(0.192)	(0.193)
R&D intensity	0.226***	0.230***	0.230***
	(0.057)	(0.057)	(0.057)
Advertising intensity	0.035	0.042	0.042
	(0.032)	(0.033)	(0.033)
Capital intensity	-0.048***	-0.047***	-0.047***
	(0.007)	(0.007)	(0.007)
National institutional quality	-0.332*	-0.313+	-0.313+
	(0.168)	(0.168)	(0.171)
Inverse mills ratio (IMR)	0.110***	0.014	0.012
	(0.025)	(0.041)	(0.042)
Level of UNGC adoption	0.037***	-0.035	-0.036
	(0.007)	(0.026)	(0.027)
Level of UNGC adoption – squared		0.005**	0.005**
		(0.002)	(0.002)
Level of UNGC adoption × National institutional quality			0.005
			(0.013)
Level of UNGC adoption – squared × National institutional quality			-0.000
			(0.001)
Intercept	-12.100***	-11.547***	-11.559***
	(1.063)	(1.098)	(1.098)
Industry fixed effects	Yes	Yes	Yes
Country fixed effects	Yes	Yes	Yes
Year fixed effects	Yes	Yes	Yes
Wald chi2	2630.14***	2654.24***	2680.27***
Log pseudolikelihood	-61468.458	-61382.733	-61381.209

Notes: [a] Natural logarithm. Models are estimated on a sample of 10,374 observations for 2,628 firms. Robust standard errors are in parentheses. + $p < 0.10$, * $p < 0.05$, ** $p < 0.01$, *** $p < 0.001$

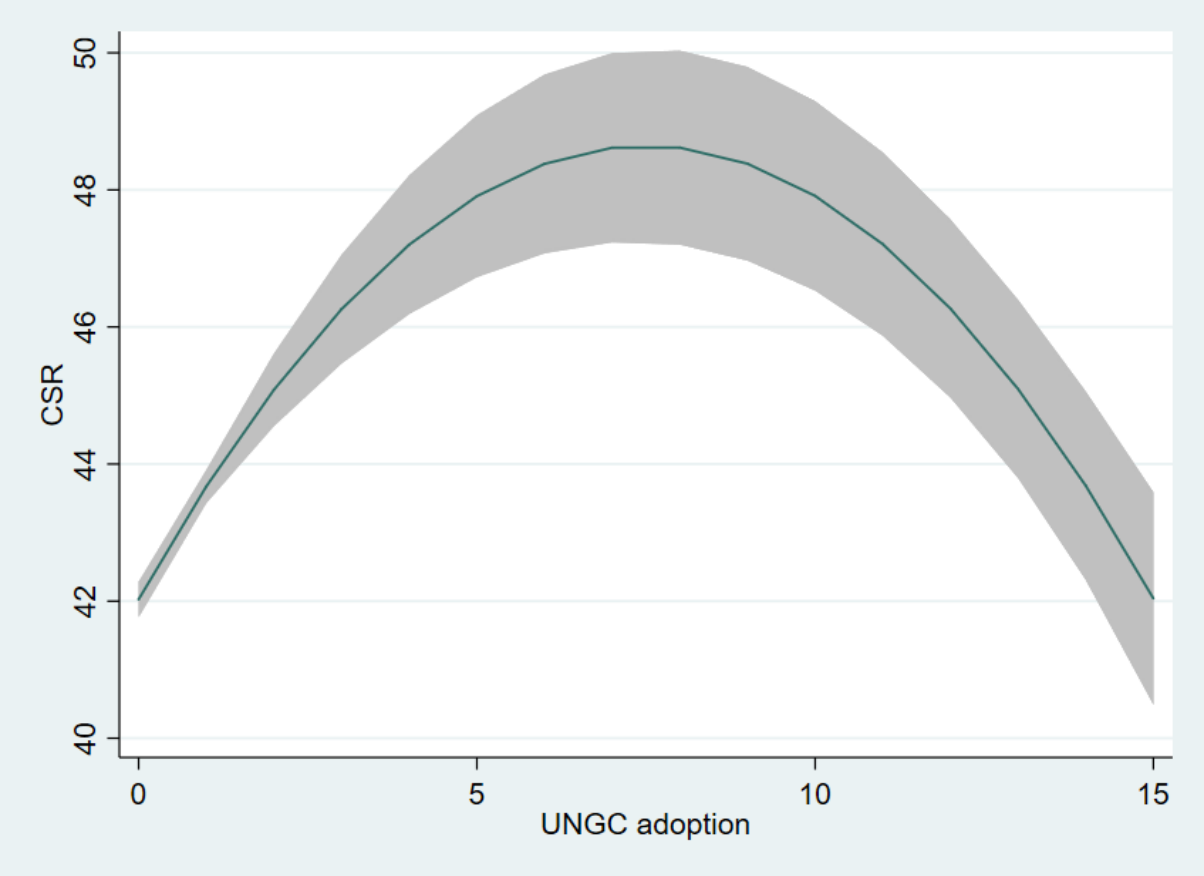

Figure 3.1 The relationship between the level of UNGC adoption and CSR

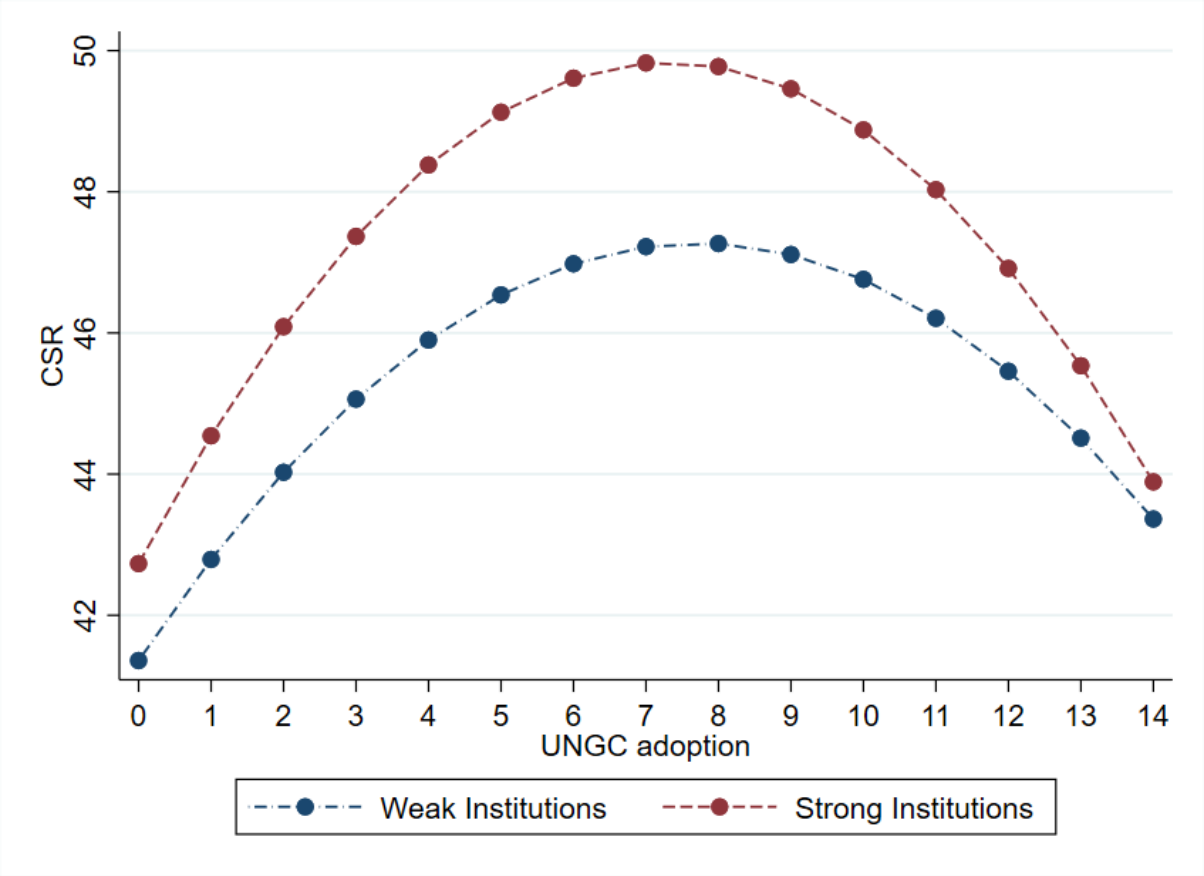

Figure 3.2 The moderating effects of national institutions on the UNGC adoption-CSR relationship

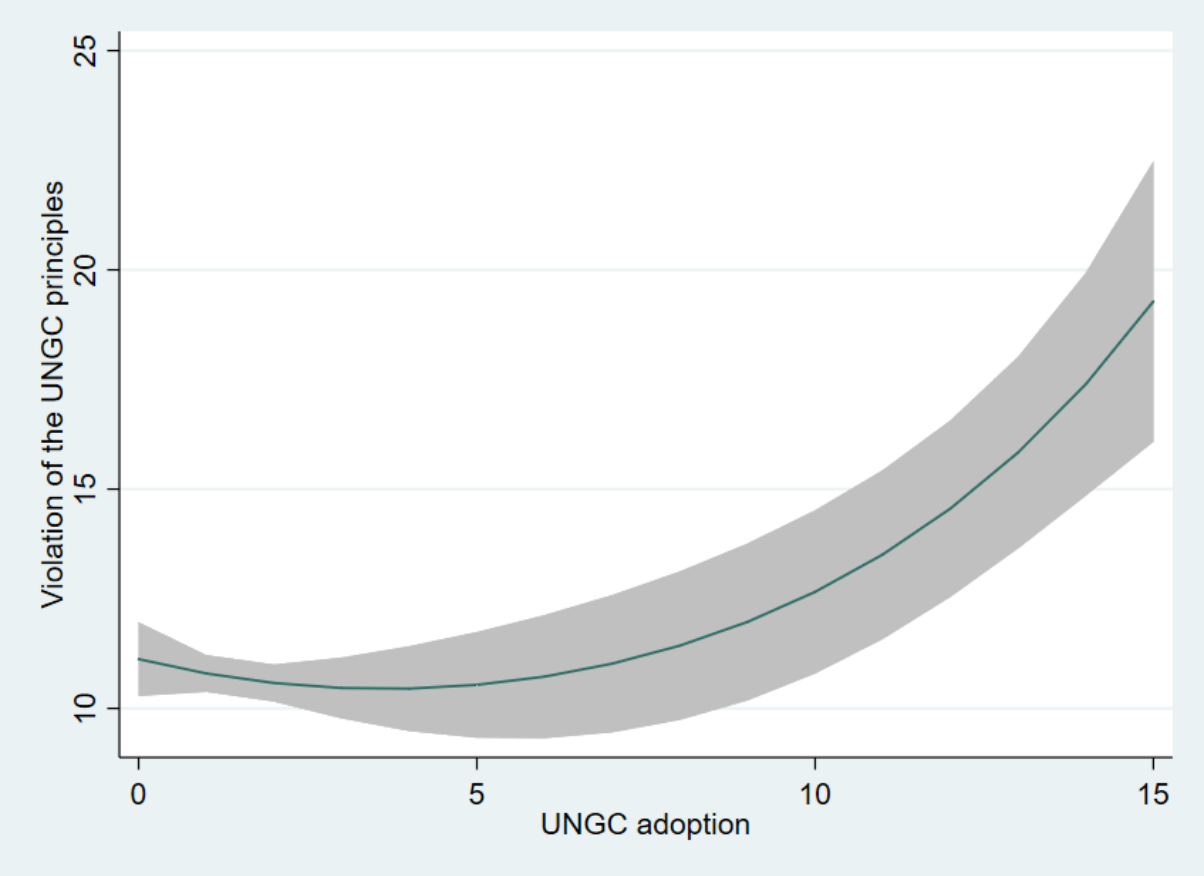

Figure 3.3 Post hoc analysis: Corporate violation of the UNGC principles

CONCLUSION

In this dissertation, I examined both the consequences (as in Essay 1) and antecedents (as in Essays 2 and 3) of stakeholder orientation of firms, as well as their implications for sustainable value creation for broader stakeholders, the firms per se, and the society at large.

Building on instrumental stakeholder theory and the research on stakeholder heterogeneity, **Essay 1** explores how such heterogeneity influences the interaction effects between stakeholder management (SM) and competitive strategies on firm financial performance. Specifically, I address two questions - 1) when is SM likely to be synergistic with competitive strategy and when is it likely to involve trade-offs or negative synergies, 2) how do these effects differ between primary and secondary stakeholders - and provide rigorous empirical evidence for these effects. I test the predictions using a longitudinal panel dataset of S&P 500 firms from 2005 to 2019 (fifteen years) with 5,032 firm-year observations in the final dataset. The findings indicate that stakeholder management (SM) combined with a differentiation advantage boosts financial performance both directly and in the case of primary and secondary SM. For cost leaders, I did not find evidence for a direct negative effect of SM on financial performance. However, I find that a combination of secondary SM and cost-based competitive advantage negatively affects financial performance, whereas primary SM has a positive effect. This finding indicates that, for cost leaders, the negative effect of secondary SM could be cancelling the positive effect of primary SM, thereby resulting in an overall insignificant effect. I performed several robustness checks, as well as Heckman-2SLS models that combine two-stage Heckman selection method with the two-stage least squares instrumental variable (2SLS IV) models, which corroborated the

major findings.

Through discriminating between corporate social and environmental practices in the corporate social responsibility (CSR) research, **Essay 2** analyzes the relationship between corporate environmental performance (CEP) and corporate social performance (CSP), and in particular, how failed and achieved environmental performance goals impact firms' subsequent social orientation. This study is based on the premise that the heterogeneity in stakeholder orientation may affect firms' differential engagement levels in addressing environmental and social issues. Building on the behavioral theory of the firm (BTOF), this study also assumes that environmental performance relative to aspiration levels could be an important driver of firms' pursuit in CSP. Specifically, this paper addresses two unanswered research questions: 1) why and how environmental performance relative to aspiration levels influences firms' social performance; 2) why and how smaller and larger discrepancies in environmental performance differ in their effects on firms' social performance engagement. I test the hypotheses using panel data on a global sample of 6,659 listed firms across all industries from 72 countries between 2004 and 2019, with 35,303 firm-year observations in the final dataset. I found that when firms' environmental performance is well below/above aspirations, their motivation to improve its future social performance will change significantly compared to situations where their environmental performance is near aspirations. Results show a U-shaped relationship between negative CEP feedback and CSP, such that firms will only turn to improve their CSP when their CEP is extremely poor (well below aspirations) in order to maintain legitimacy. The findings also suggest an inverse U-shaped relationship between positive CEP feedback and CSP, such that firms' motivation

to improve CSP will first increase with positive discrepancy in CEP (due to managerial confidence and excessive resources), and then after a certain point decrease significantly mainly because their legitimacy is already secured by the superior environmental performance as well as due to depleted resources in environmental investments.

Drawing on institutional theory and corporate social responsibility (CSR) literatures, **Essay 3** examines two research questions: 1) What is the relationship between private voluntary governance institutions (via the compliance with the UNGC) and CSR? 2) How does public governance (via the quality of national institutions) condition this relationship? I test the predictions using a unique dataset of 5,813 listed companies across all industries from 62 countries (including both emerging markets and developed markets firms) from 2004 to 2019. I found a curvilinear (inverse U-shaped) relationship between the level of UNGC adoption and CSR. The core argument of this study is that the positive impact of the UNGC on promoting CSR is likely to wear offer over time, with the highest CSR performance occurring at an intermediate level of the UNGC adoption. The limits to the effectiveness of the UNGC exist mainly because of the symbolic nature of adopting the UNGC which acts as a legitimacy insurance. After a certain point when firms' legitimacy is well secured, firms' motivation to substantively improve CSR will be decreased. Moreover, the salience of the UNGC commitment might be reduced over a period of time, as multiple organizational goals compete for managerial attention and organizational resources, leaving less to be deployed for CSR. Results further suggest that national institutional quality will positively moderate this curvilinear relationship between the UNGC adoption and CSR in such a way that it enhances CSR at lower levels of UNGC adoption (i.e., the ascending part of the inverted-U

shape curve), and it enlarges the decline in CSR at higher levels of UNGC adoption (i.e., the descending part of the curve). In the post-hoc analyses, I also found a U-shaped relationship between firms' UNGC adoption and their violations of the UNGC principles, also known as corporate social irresponsibility (CSI), which suggests the compliance risks and potential decoupling behaviors of the UNGC adopters.

Contributions and Theoretical Implications

This dissertation contributes to research on stakeholder management and value creation of organizations, corporate social responsibility (CSR) and corporate social irresponsibility (CSI), performance feedback and the behavioral theory of the firm (BTOF), as well as the efficacy of voluntary governance institutions (i.e., the UNGC) as a type of normative institutions in shaping corporate responsible practices.

1) Implications for research on stakeholder management and value creation. Despite the significant progress made by stakeholder management (SM) research, our understanding of the many trade-offs managers face while engaging in SM is still limited. Extending the work on contingencies (Garcia-Castro & Francoeur, 2016), my Essay 1 highlights the role of generic competitive strategies and stakeholder heterogeneity in determining when SM is likely to be associated with higher financial performance and when it may not. This study extends prior research by addressing not only the question "when does SM pay?", but also "when does SM *not* pay?", and helps account for some of the mixed and inconclusive findings in the literature on the financial performance implications of SM.

This research contributes to the work that seeks a more direct integration of stakeholder theory with competitive strategies (Coff, 1999; Berman et al., 1999; Jones et al.,

2018; Barney, 2018; Zollo et al., 2018). It adds to this body of work - a) by examining not only when the interaction effects are positive but also when they are negative, b) by disentangling the distinct performance effects of primary and secondary SM and c) by providing more comprehensive and rigorous empirical evidence.

This study also contributes to the work underlining stakeholder heterogeneity, as it extends the core thesis that primary stakeholders may contribute more firm-specific and financially relevant resources and capabilities (Garcia-Castro & Francoeur, 2016; Hillman & Keim, 2001) to the specific context of the generic competitive strategies pursued by a firm. I find that both primary and secondary SM have a positive effect on financial performance in firms pursuing a differentiation advantage, and that in firms with a low cost advantage, secondary SM negatively affects financial performance, whereas primary SM seems to benefit financial performance. These different, and opposite, effects of primary and secondary SM for cost leaders suggest that the stakeholder categories to focus on is an important element of stakeholder strategy for low cost firms.

Essay 1 also has important implications for practitioners by shedding additional light on the long-standing question of 'how to do good *and* do well' and by accentuating the challenges of implementing SM in practice. This research adds important boundary conditions to the claim that the benefits of improved stakeholder relations can offset the related costs of SM (Barnett & Salomon, 2012). The findings point out that firms with a differentiation advantage have better prospects of balancing the twin goals of 'doing well' and 'doing good' when compared to firms competing purely based on low costs/prices.

2) Implications for research on performance feedback, behavioral theory, and

CSR. Essay 2 makes contributions to research on the drivers of corporate social performance (CSP) and performance implications of negative/positive feedback in terms of corporate environmental performance (CEP). It adds to literatures on CSP and stakeholder theory by offering a behavioral explanation and empirical evidence for firms' motivation to pursue CSP implying their orientation towards stakeholders in social areas. It extends CSR research by examining firms' social and environmental orientation separately, as well as by theorizing and providing empirical evidence on the previously underexplored relationship between CEP and CSP, through the lens of how firms interpret and respond to environmental performance feedback differentially. It represents one of the few empirical studies that examine the relationship between corporate social and environmental orientation, as well as the potential trade-offs between them, by discriminating CSP and CEP in the CSR research.

In addition, this research generates theoretical implications for the behavioral research by investigating feedback-driven responses in the context of CSR, especially by distinguishing between the smaller and larger discrepancies in environmental performance relative to aspirations. On the one hand, under the conditions of greater failure to meet environmental performance goals, firms will alternatively pursue CSP to gain stakeholder support and preserve legitimacy granted by external audiences. On the other hand, the favorable situation of greater success in environmental performance will reduce firms' motivation to engage in CSP, due to the seemingly trade-offs between pursuing CEP and CSP. Integrating behavioral theory and CSR research, this study goes beyond examining whether external stakeholder or institutional pressures drive firms' stakeholder orientation to examine how firms' environmental performance against aspiration levels can serve as an internal

motivator for improving future social performance.

Lastly, this study advances the BTOF by examining how both larger and smaller discrepancies in performance goals will affect firms' interpretation and responses to feedback about environmental performance beyond economic concerns, by testing and theorizing a curvilinear relationship between environmental performance feedback and firms' subsequent responses. Empirically, this paper demonstrates that environmental performance far below/above aspirations (i.e., larger discrepancies) will trigger firms to change their search behaviors significantly in terms of future social orientation, compared to situations with smaller performance discrepancies.

3) Implications for research on institutional theory and efficacy of private governance institutions. Essay 3 was motivated by the elusive conclusions about the relative efficacy of voluntary governance institutions in shaping corporate responsible practices, as well as the under-explored impact of regulatory heterogeneity across national institutional contexts. This study contributes to institutional theory and CSR literatures by investigating the diminishing returns to voluntary governance initiatives (i.e., the UNGC). This research deepens our understanding of the efficacy of voluntary initiatives (i.e., the UNGC) by proposing and confirming 1) a curvilinear (inverse U-shaped) relationship between the UNGC adoption and CSR, and 2) the positive moderating effect of national institutions on this curvilinear relationship. The findings suggest that the UNGC does play a positive role in promoting CSR, but its positive effect will be attenuated over time. A primary theoretical implication of this research is that I look at the dynamic effects of the adoption of UNGC over a full period of time and provide nuanced theoretical mechanisms to explain why

voluntary initiatives will face a ceiling.

A second contribution is that it adds to the research on the complementarity between public and private governance institutions, by identifying the mechanisms of how national institutions will interact with transnational private governance institutions (i.e., the UNGC) to affect corporate responsible activities, and by providing empirical evidence that supports the institutional configuration perspective (Scott, 2005; Stephan et al., 2015) proposing that individuals' activities are "shaped jointly by the constraints, incentives, and resources provided by formal and informal institutions" (Stephan et al., 2015: 309).

A third theoretical implication is that this study goes beyond the debate about whether private governance influences corporate behaviors to instead examine when and how the UNGC initiative may improve or worsen CSR performance (Aragon-Correa et al., 2020; Vogel, 2008, 2010). This paper offers new insights about the effectiveness of the UNGC, under what condition the UNGC plays a role, and how the UNGC works together with national institutions to facilitate or impede positive corporate outcomes. This study also contributes to the CSR literature by answering the recent calls for examining international differences in firm behavior beyond a separate aspect of institutional factors (Aragon-Correa et al., 2020; Goerzen et al., 2020; Graafland & Noorderhaven, 2020; Knudsen, 2011; Vogel, 2010). It extends findings from past research that empirically investigated the institutional drivers of CSR (e.g., Ioannou & Serafeim, 2012) by highlighting the importance of joint effects of regulative and normative institutions. It also represents the first empirical attempt to test their joint effects in different contexts, using a longitudinal dataset of a comprehensive global sample.

4) Implications for research on corporate social irresponsibility (CSI). Essay 3 also adds to the emerging body of work on CSI (Lange & Washburn, 2012; Mishina et al., 2010; Strike et al., 2006), by demonstrating that the efficacy of private governance via the UNGC seems asymmetric in influencing CSR and CSI. Previous research has rarely investigated the institutional influences on, or (inter)national drivers, of CSI. I find that the adoption of the UNGC is positively associated with CSI (i.e., corporate violations of the UNGC principles) while it is negatively related to CSR, at later stages of the UNGC adoption. While the UNGC is effective in stimulating firms to engage more in CSR for some time, it does not serve as a strong constraint for CSI in general. The concurrence of the UNGC adoption and violations of the UNGC principles implies potential decoupling behaviors among the UNGC adopters.

Another fresh perspective corroborated by empirical evidence in my post-hoc analyses in Essay 3 is that, in testing the possible synergy between national institutions and the UNGC on CSI, I did not find a significant interaction effect on CSI. Nevertheless, firms' CSI behaviors are disclosed by the media or external stakeholders rather than reported by the firms per se, thereby I cannot simply interpret that higher CSI is triggered by weaker national institutions. Instead, stronger institutional conditions are usually accompanied by other facilitating factors, including more press freedom, greater degree of globalization of a country, and well-established equipment and infrastructures, that may serve as mediators or contingencies between institutional contexts and firms' CSI activities. The results underscore the importance of further exploring the mechanisms by which institutional environment facilitates or impedes the diffusion of (ir)responsible business practices. The findings also

suggest the need to examine further the mechanisms that drive emerging markets firms (or firms from non-enabling institutional conditions) to undertake (ir)responsible or illegitimate activities.

Limitations and Future Research Directions

Overall, the sample and data that I use in this dissertation is mainly secondary data on publicly listed firms. The findings in my dissertation may not be generalized to small or private firms, or in other contexts. While quantitative approach as used in my dissertation has its advantages in examining the correlations or causality between variables, it has limitations as well. To complement my existing research, I encourage future research to use other methodological and analytical approaches. For example, using the qualitative comparative analysis (QCA) to explore the complex and multiple interactions in different contexts, conducting interviews and field work to collect qualitative data, and analyzing unstructured data to generate new metrics/measures for key variables, such as the new measures of 'value', 'impact', and 'performance' in strategy and management research.

In Essay 1, I theorize and test the value creation potential of different stakeholder and competitive strategies, yet I did not examine the process of how value is distributed among different stakeholders. It is important to capture the value creation and appropriation by multiple stakeholders and not just shareholders in the strategic management process. Future studies could investigate how exactly value is appropriated by different groups of stakeholders and how this would differ between firms pursuing different business strategies.

Essay 2 extends behavioral research to the context of stakeholder orientation by exploring and explaining how different levels of performance discrepancies affect the way in

which negative/positive environmental performance feedback is interpreted. Even though this study represents an important step forward in examining the drivers of CSP and the heterogeneity of firms' stakeholder orientation, it does not look at the single components of CSP/CEP under the broad social/environmental categories. Future research could break down the aggregated measure of CSP/CEP into separate stakeholder dimensions, thus further accounting for the distinct influence of performance feedback on corporate stakeholder performance. Future research could also investigate firms' behavioral responses related to other organizational outcomes such as corporate misconducts and irresponsibility.

While Essay 3 investigates the heterogeneous degree of compliance with the UNGC among firms as well as the broad impact of national and transnational governance institutions on corporate conduct, it does not examine precisely which single aspects of CSR are influenced by which single components of institutional arrangements. Future research could examine how weak national institutions create incentives and opportunities for the substitution of alternative institutional arrangements, or how firms' single dimensions of CSR (and CSI) are affected by a particular aspect of national institutional framework. Future research could also extend this study by examining the antecedents of compliance risks (violations of the UNGC principles) and potential decoupling behaviors of the UNGC signatories (i.e., the discrepancy between a firm's CSR reporting and its actual CSR performance), given that the commitment to the UNGC still gives rise to both decreases in CSR and increases in CSI.

Concluding Remarks

There has been a substantial amount of work on how effective stakeholder management can

benefit firms' profit maximization. Yet, the potential incompatibility between stakeholder value creation and shareholder value appropriation, as well as how the trade-offs or negative synergies between them may occur, is relatively under-explored. Essay 1 of my dissertation extends past research by identifying firms' competitive strategies and stakeholder heterogeneity as important boundary conditions for the relationship between stakeholder management and firm financial performance. Thus, it provides a base for future research on the downside of stakeholder investments, suggesting that 'doing good' may *not* pay. Further, although some extant research has recognized the heterogeneity of firms' stakeholder orientation, most studies combined firms' social and environmental (and even governance) practices under the general rubric of CSR, which intends to create value for all stakeholders. Essay 2 of my dissertation provides new insights into firms' responses to stakeholders by discriminating between corporate social and environmental practices as well as by demonstrating the dynamic relationships between them. Lastly, Essay 3 of my dissertation unveils the diminishing positive effect of voluntary governance institutions (i.e., the UN Global Compact) on corporate responsible conducts. It also broadens the existing literature on stakeholder management and CSR by demonstrating firms' compliance risks and potential decoupling behaviors. Taken together, the theory and empirical findings of my dissertation advance our understanding of whether, how, why and under what conditions stakeholder management strategies will matter to firms' value creation, by examining the antecedents, consequences, contingencies and heterogeneity of stakeholder orientation. While my dissertation makes several novel contributions, more enquiry is needed to understand how organizations address the specific challenges in creating value for multiple stakeholders

simultaneously while committing to solving major societal and organizational issues.