



**university of
 groningen**

**faculty of economics
 and business**

Master Thesis

Does CSR create firm value? - A Comparison of moderating effects of country and industry characteristics

By

Christian Erich Oskar Flachsland

Supervisor: Dr. H. Gonenc

Co-Assessor: Prof. Dr. B. Scholtens

Submitted for the degree of

MSc International Financial Management

Double Degree with Uppsala University

Faculty of Economics and Business

Rijksuniversiteit Groningen

Uppsala Universitet

chflachsl@gmail.com



**rijksuniversiteit
 groningen**



**UPPSALA
 UNIVERSITET**

Abstract

This study aims to demonstrate how different country and industry-level variables affect the value-creating abilities of CSR initiatives. It contributes to the growing body of literature about CSR as it directly compares the moderating effects of the quality of country-level institutions with the moderating effects of the respective industry sector. The study amongst 3,670 firms in a sample period from 2006-2014 shows that CSR initiatives have a superior value-creating ability in environments with weak capital markets and country governance standards. Firms in controversial industry sectors have a superior ability to create value through CSR because they display a higher potential for reputational gains through CSR due to the nature of their business. The results of the study suggest a supremacy of country-level determinants over industry-level determinants of the CSR-firm value relationship.

Key words

Corporate social responsibility, Firm value, Market-supporting institutions, Capital markets, country governance standards, controversial industries

Abstract

1. Introduction

2. Literature review and hypotheses development

2.1 Literature review

2.2 Hypotheses development

2.2.1 The effects of CSR initiatives on a firm

2.2.2 Country-effects on value-creating effects of CSR

2.2.2.1 The value-creating effect of CSR in different institutional environments

2.2.2.2 The effect of capital market development on the value-creation of CSR

2.2.2.3 The effect of corporate governance development on the value-creation of CSR

2.2.2.4 Conceptual model

2.2.3 Industry-effects on value-creating effects of CSR: A closer look at controversial industries

2.2.3.1 A stakeholder-theory approach to industry-level differences in CSR

2.2.3.2 Industry-characteristic differences in the value-creating effect of CSR

2.2.3.3 Conceptual model

3. Methodology, Data and Sample

3.1 Variable Measurements

3.1.1 CSR initiatives

3.1.2 Firm value

3.1.3 Quality of market-supporting institutions

3.1.4 Quality of capital markets

3.1.5 Quality of corporate governance standards

3.1.6 Controversial industries/ conventional industries

3.1.7 Control Variables

3.2 Data and Sample

4. Results

4.1 Descriptive statistic and correlations

4.1.1 Descriptive statistics

4.1.2 Correlations and multicollinearity

4.2 Regression results

4.3 Robustness tests

5. Conclusion

References

Appendix A: Robustness Test using Industry-adjusted Tobin's Q

Appendix B: Robustness Test using Industry-adjusted Tobin's Q

Appendix C: Correlation-Matrix

1. Introduction

CSR engagement of firms is continuously growing amongst virtually all industry sectors and countries and therefore continues to gain attention in the academic literature (Cai et al., 2012). Despite this increasing focus on CSR in the literature, scholars fail to arrive at a clear consensus about the effectiveness of CSR for firm's financial well-being and their meaning to firms' stakeholder (Cai et al, 2012). This study aims to contribute to this academic debate by presenting further evidence of the effect of CSR on firm value and the mediation of this effect by several country and industry-level characteristics. The concept of CSR generally defines the extent to which a firm considers its stakeholder's needs in its corporate actions. Jo et al. (2011) add an important aspect to this definition, as they further define CSR actions as any interactions of the firm with its stakeholders that goes beyond any legal requirements the firm is subject to. CSR is therefore characterized by the voluntary character of the actions. In general, CSR can be seen as a stretch of companies thrive towards good corporate governance in order to secure sustainability through a higher degrees of transparency, philanthropy and accountability. The crucial question for firms now is the effectiveness of these actions on their financial well-being. While the effect of CSR on firm performance has been shown to be positive time and again (Griffin & Mahon, 1997; Margolis & Walsh, 2003; Beurden & Gössling, 2008), the evidence of CSR effects on firm value continue to be mixed (El Ghouli et al., 2016). While some studies show positive effects of CSR initiatives on firm value (Luo & Bhattacharya, 2006; Servaes & Tamayo, 2013; Jo & Harjoto, 2011), other scholars oppose these findings with contradictory evidence (Dillenburger et al., 2003; Orlitzky et al., 2003; Tencati et al., 2004) and show negative effects of CSR on firm value. These mixed findings root from fundamentally different attitudes towards firm's responsibilities in the interaction with their environment. Proponents of the value-creating effect of CSR refer to the work of Carroll (1979), who introduced the concept of the social contract and thereby highlighted a firm's responsibility to take actions in order to compensate its environments for its corporate actions and thereby be aware of rights and privileges that apply to all members of the society. This view is opposed by researchers following the shareholder-approach put forward by Friedman (1962, 1970). He states, that all use of firm resources towards CSR-initiatives is a waste of shareholder resources as these resources could also be deployed to positive NPV-projects in order to maximize shareholder value. Jensen & Meckling (1976) follow a

similar logic as they simply view CSR as the inevitable outcome of agency conflicts between shareholders and a firm's management. Corporate Executives will engage in CSR solely in order to pursue their own benefits and increase their personal reputation. One main driving force of this academic dissent is the appliance of different research methodologies and data sources by academics. Differences in the measurement of CSR and the data sources of these measures, different performance and value indicators and different sample periods and research designs continuously lead to diverging outcomes (Cai et al., 2012). This study will provide further evidence in this field.

Several recent studies (Meyer et al., 2009; Cai et al., 2012; El Ghoul et al., 2016) highlight the major importance of country-level differences for the effect of CSR initiatives on firm value. El Ghoul et al. (2016) shows, that firms can create value through CSR initiatives in weak institutional environments. In this context, CSR can be used as a tool to overcome these weak environments by interactions with the firm's environment. Meyer et al. (2009) show, that different levels of investor protection mediate the relationship between CSR and firm value. Better investor-protection regimes will encourage shareholders to positively evaluate CSR initiatives since they believe that managerial entrenchment practices are limited in these context. The crucial determinant of cross-country differences in the relationship of CSR initiatives and firm value is the presence of institutional voids in different countries (El Ghoul et al., 2016). These institutional voids can take the form of insufficient capital markets, weak institutions and all other deficient country-level determinants of firm success. The value-creating or value-destroying effect of CSR initiatives is shown to be highly dependent on the quality of country-level institutions (Lev et al., 2010). The investigation of cross-country differences gains importance in a globalizing world, as lawmakers seek to understand how they can create an environment where firms will invest in CSR because it creates firm value and the society can enjoy the beneficial effects of these initiatives. Corporate executives, on the other hand, try to understand how they can strategically use CSR initiatives to overcome flawed institutions in their host countries. In a rapidly changing world (increasing globalization developments, destabilized political regimes), it is of crucial importance for practitioners to understand how CSR affects firm value differently in different institutional environments. Public pressures and unexpected natural disasters (e.g. Fukushima) can change the economic circumstances for the efficiency of CSR rapidly. After the nuclear catastrophe in Fukushima in 2011, the german government quickly reacted to public pressures

and initiated an exit from nuclear power generation within the country. This event highlighted the importance of not only country-level effects, but also industry-level effects on CSR initiative's effects on firm value. The public opinion towards nuclear energy companies changed rapidly and created a different societal environment for these companies. Firms that operate in controversial industry sectors are generally shown to have different characteristics for value-creation or destruction through CSR. A study by Wilson & West (1981) states, that controversial industries have a special need for CSR to compensate for the nature of their business activities since they are perceived with reactions of outrage and disgust due to moral foundations within a society. These industries include gambling, alcohol, tobacco, military goods and, due to the effects of climate change, also fossil fuel and nuclear firms in our days. Scholars have a lively debate about the effectiveness of CSR in those industries. Proponents argue that firms in controversial industry sectors need CSR as a strategic tool to overcome their bad reputation in the society (Frynas, 2005; Banerjee & Bonnefous, 2011; Cai et al., 2012). While accepting this strategic relevance of CSR for controversial firms, opponents argue that controversial industries should not be allowed to undertake CSR initiatives because they will use them to disguise and hide the true consequences of their products and business activities (Palazzo & Richter, 2005). Even the World Health Organization (WHO) calls for government interventions in controversial firm's attempts to raise the social acceptance of their business. Byrne (2010) further states, that firms in controversial industry sectors should not be allowed to undertake CSR initiatives because their business ideas contradict with each society's fundamental goals of health and morality. There is consequently mixed evidence towards the effects of CSR on value in those industries. Yoon et al. (2006) and Sweeney & Coughlan (2008) show positive effects of CSR on firm value in those industries, whereas Cai et al. (2012) present conflicting evidence and a value-destructive effect of CSR. This study will outline the possible explanations for these phenomena in detail in the literature section and present further evidence on the topic through its research outcomes. It aims to contribute to the literature by closing the gap between industry and country level determinants of CSR and bring these fields together.

It can be concluded, that institutional voids and reputational voids can therefore be motives for firms to carry out CSR initiatives as CSR seems to be suitable tool to overcome these voids. Considering the mentioned arguments, the questions about a potential supremacy of cross-country or cross-industry factors arises as my research question:

Is the ability to overcome institutional voids or the ability to overcome reputational voids a more important determinant of the value affecting ability of CSR initiatives?

The answer to this research question is highly important for lawmakers and managers in order to optimize their attitudes towards CSR and focus on the most important factors for their individual business. This study aims to answer the posed research question by analyzing 22,034 firm-year observations during a sample period from 2006-2014. OLS regressions are conducted in order to determine the moderating effects of country-level factors (quality of market-supporting institutions, quality of capital markets and quality of country-level governance standards) and industry-level factors (being a part of the ‘controversial’ industry-sector) on the relationship of CSR and firm value. I find a consistent positive correlation of CSR and firm value and therefore confirm the stakeholder theory approach to CSR in line with numerous other studies (Luo & Bhattacharya, 2006; Servaes & Tamayo, 2013; Jo & Harjoto, 2011). The quality of capital markets and country governance standards is further found to have a negative effect on the value-creating potential of CSR initiatives. It can be derived that environments with institutional voids are superior to environments with well-developed institutions in their ability to enable firms to create value gains through CSR. I further observe a positive relationship between a firm’s classification as ‘controversial’ and the CSR-value relationship. This suggests, that these firms can create more value through CSR due to the occurrence of reputational voids in this industry. These voids enlarge the potential of value-creation through CSR. I further find a positive association of CSR and firms in controversial industries which highlights these industry’s superior need for CSR. When all the mentioned moderating factors are linked in one model, I observe a supremacy of country-level moderators over the industry-level moderator. However, they are both found to be significant moderators of the CSR-value relationship.

The next chapter will provide a review of relevant literature and the development of my hypothesis. Chapter three will then proceed with a description of the methodology and will forego the presentation of my results. The last chapter will provide a conclusion of the conducted research.

2. Literature review and hypotheses development

The following literature review will first define the concept of CSR, briefly show the historical development of this definition and then elaborate on the effect of CSR initiatives on the firm and a firm's motivations for CSR. Academic references will then assist in the development of hypotheses.

2.1 Literature review

The role of CSR in the economy has long been subject of fierce academic debates. CSR was first mentioned in academic literature by Bowen in 1950, as he defined it as lines of philanthropic actions in according with societal values (Bowen, 1950). This initial philanthropic approach was however quickly neglected by numerous scholars (Fredrick, 1960; Davis, 1960), and replaced with the shareholder theory. Proponents of the shareholder theory argue, that CSR is a waste of valuable firm resources that could otherwise be deployed into a value-creating context (Friedman, 1962, 1970). Contrasting to that, Carroll first introduced the concept of firm responsibilities towards the society in 1979, and thereby initiated the stakeholder perspective on CSR (Carroll, 1979). He states, that a firm's responsibilities encompass economic, legal, ethical, discretionary and philanthropic components. Building on that, Donaldson (Donaldson, 1982; Donaldson and Dunfee, 1999) developed the concept of the social contract to elucidate the importance of firm actions aimed at societal goals. He elaborates on a tacit contract between firm and society, which grants firms certain rights for certain responsibilities. In reaction to the developments in the academic literature, Freeman introduces his explicit concept of stakeholder theory in 1984. He first defines a firm's stakeholder as 'any group or individual who can affect or is affected by the achievement of an organization's purpose' (Freeman, 1984). He then further argues, that it is in a company's strategic interest to respect the interests of all its stakeholders. As an extension to the traditional stakeholder theory, instrumental stakeholder theory emerged in the literature (Berman, 1998). It states, that CSR can assist firms in gaining stakeholder support and provide them with valuable resources. Deriving from these argumentations, one can define CSR as a 'political economy', including all rights and responsibilities that a society consciously or unconsciously assigns to the private industry. Due to several global economic developments, CSR has continued to receive a lot of attention in the worlds of practitioners

and academics in recent years. As the liberalisation of markets increases, a declining importance of the regulatory approach can be observed (Van der Steen, 2015). The emergence of global giants in the business world and along with that, a consolidation of market share can further be observed. These phenomena merge in the development of ‘global embedded firms’ and global value chains (Aguinis & Glavas, 2013). As the concept of CSR was intangible in its first academic appearances, the growth of global businesses led to attempts to employ a more comprehensive view towards CSR. Responsible business activities, and their display through CSR, have developed to powerful instruments of corporate action in our days. The vast majority of scholars views them as very influential and potential value-creating tools for firms, and thereby closely links CSR and firm performance (Porter & Kramer 2006, 2011; Lev et al., 2010). CSR can consequently be defined as a firm’s participation in social initiatives to interact with a firm’s environment and take responsibility for its impact on this environment.

There are several potential reasons why firms engage in CSR. The maximization of stakeholder value is one potential motive, firms can thereby use CSR initiatives as a strategic tool to increase interest-alignment with its stakeholders and thereby eliminate potential sources of conflict between the firms and its environment. This motive is challenged by Baumol and Blackman (1991), who point out that firms can’t undertake these stakeholder value maximizing initiatives in a competitive environment, because CSR initiatives are so resource-intensive that their execution can threaten a firm’s survival in a competitive environment. Another motive for CSR could be the thrive for personal benefits (e.g. reputation building) by managers at the expense of shareholder value. This potential entrenchment effect was first introduced by Friedman (1970). He argued, that managers could view CSR initiatives as a personal tool to derive personal benefits from corporate resources and therefore misappropriate shareholder property. Consequently one can conclude, that more firm engagement in CSR initiatives will result in more severe agency problems. Fabrizi et al. (2014) support this view as they show that higher corporate governance will lead to more CSR initiatives in an effort by the management to extract personal benefits. They further find that managerial incentives to optimize shareholder value lead to less CSR initiatives. Cespa and Cestone (2007) further show, that managers use CSR as a tool to gain and maintain stakeholder support in order to avoid their own replacement and protect their job. Efficient

corporate governance therefore needs to lower corporate cash holdings and thereby reduce the potential of managerial entrenchment through CSR. Firms can further try to reduce information asymmetries about their business operations and send signals about their trustworthiness and moral conformity of their operations to their stakeholders (Bandsuch et al., 2008). Firms in ‘sin’-industries (e.g. tobacco, gambling, military) can use CSR as a tool to cover up their unethical behavior, this motive is called ‘window-dressing’ and I will discuss it in detail in chapter 2.2.3.2. The most intuitive reason to invest in CSR is societal pressure towards ethical behavior. This pressure can be exercised formal (by law), quasi-formal (by lobbyist) or informal (by the civil society). Strong civil societies are characterized by a high level of social capital in the society. Strong social capital implies strong norms and values that enhance collective responses to external influences (Woolcock, 2001). Stakeholders in these strong social environments expect firms to engage in socially responsible, societal welfare increasing activities, even if the firm can’t derive any benefits from them and has to bear substantial costs (Benabou & Tirole, 2010).

Despite their emerge and spread in the globalizing economy, CSR initiatives are however still viewed critically by some academics who follow Henderson’s argumentation, that CSR’s adoption would result in reduced competition, less economic freedom and thereby undermine the market economy (Henderson, 2001). He makes this point especially in the context of developing economies, as he argues that CSR is likely to hold back economic development there. In his point of view, this negative effect of CSR occurs due to the suppression of employment opportunities within developing countries. World Bank statistics further support his critical view of CSR as they show, that increases in CSR (manifested in higher scores of the national corporate responsibility index) go along with rising labor costs per worker (World Bank Group, 2015). Advocates and opponents of CSR continue to have fierce debate and thereby highlight the importance of more research in that area (Japhet et al., 2015; Martínez-Ferrero et al., 2016; Baden & Harwood, 2013).

2.2 Hypotheses development

2.2.1 The effects of CSR initiatives on a firm

Drawing on transaction cost theory and stakeholder theory (Hill, 1990; Williamson, 1989; Freeman, 1984), CSR can be seen as a potential tool to overcome transaction costs associated with a firm's relationship to its stakeholders. These costs have their origin in transaction problems in a firm's interaction with its stakeholders and the embedded exchange operations. They can manifest in ex-ante transaction costs (e.g. initiation costs, negotiation costs, contracting costs) and ex-post transaction costs (e.g. control costs, enforcement costs) (Coase, 1937; Williamson, 1985). Instrumental stakeholder theory further states, that CSR can be an efficient tool for firms to obtain critical resources. The business benefits arising from CSR range from the mentioned access to valuable resources (mainly human resources), to beneficial effects in the fields of risk management and brand differentiation up to potential effects of reduced scrutiny by regulatory authorities (Bhattacharya et al., 2008; Kytte & Singh, 2005; Paluszek, 2005; Griffin & Vivari, 2009). According to the resource-based view, resources are firms ultimate sources of competitive advantages (Wernerfelt, 1984). By reducing transaction costs and granting firms access to valuable resources, CSR can consequently enhance the value-creation in an organization (Foss & Foss, 2005). By its definition, CSR has positive effects on the social/ environmental performance of an organization. This positive effect on social and environmental performance is shown to translate into positive effects towards an organization's financial performance (Orlitzky et al., 2003). Therefore, in accordance with numerous academic studies (Luo & Bhattacharya, 2006; Servaes & Tamayo, 2013; Jo & Harjoto, 2011), I draw the following hypothesis:

H_{1,1}: "Corporate Social Responsibility initiatives have a positive effect on firm value"

2.2.2 Country-effects on value-creating effects of CSR

CSR initiatives are a managerial tool for firms to reduce transaction costs that are associated with difficulties in firm's exchange processes with its environment (El Ghouli et al., 2016). This transaction costs pose significant risks and costs to firms as they drive down a firm's economic efficiency and the economic value of an exchange process. Scholars suggest, that

country-level differences have a substantial impact on the magnitude of these transaction costs (Akerlof, 1970; Williamson 1985). Countries develop intermediaries to these exchange processes, these institutions have the responsibility to resolve conflicts in the exchange processes, reduce information asymmetries and consequently drive down transaction costs. Meyer et al. (2009) emphasizes the role of institutions for effective working markets and points out substantial differences amongst countries. While developed economies have a high degree of institutionalization in their economy and are characterized by efficient markets, developing economies frequently lack institutions (Meyer et al., 2009). Firms in developing markets therefore face high transaction costs in developing countries, they for instance face problems in raising capital due to information asymmetries caused by the absence of information intermediaries (e.g. analysts) in capital markets. A lack of intermediaries may further cause excessive government interventions in firm's business operations and lead to problems in firm's investment decisions due to a unpredictability of government actions. These excessive interventions can further harm fair competition in markets (Kuppuswamy et al., 2014). Weak legal conditions can further result in product market failures because customers lack the opportunity to take legal actions if products are of bad quality (Khanna & Palepu, 1977). Environments that lack efficient market intermediaries or institutions therefore pose risks to firms and urge firms to develop strategies in attempts to overcome these market imperfections.

These strategies mainly consist of market-based approaches. Hutchcroft & Rocamora (2003) find, that firms can overcome these domestic institutional voids by international expansion strategies and geographic diversification. Karna et al. (2013) suggest the creation of domestic business environments through geographical clusters as a strategic option for multinational firms. Strategic alliances between local and foreign partners can also help to overcome a weak institutional environment and ease access to capital markets (Oxley, 1999). The internalisation of intermediary responsibilities (in capital and output markets) in large business federation and strategic alliances is viewed as the most efficient market-based tool to overcome bad institutional quality (El Ghouli, 2016). These solutions however bear costs and risks for firms since unrelated business diversification is found to cause inefficiencies in decision-making and poor markets for corporate control (La Porta et al., 1998; La Porta et al., 1999). Furthermore, business group members are harder to monitor than unaffiliated organizations (La Porta et al., 1998). While market-based approaches to institutional voids come with the

mentioned costs, non-market approaches like CSR initiatives can present alternative tools for firms.

2.2.2.1 The value-creating effect of CSR in different institutional environments

The resource-based view defines firms as unique bundles of resources (Williamson, 1985). This particular resource combination is however affected by transaction costs that can harm a firm's acquisition of new resources (Garleanu & Pedersen, 2013). Because of the importance of resources in the creation of competitive advantages, lower transaction costs and better access to resources can generate firm value (Foss & Foss, 2005). CSR initiatives can ease the access to resources by creating a tight network with resource-supplying stakeholders. CSR initiatives can take over the responsibilities of lacking market intermediaries and thereby drive transaction costs down. Providers of capital view CSR investing firms as highly transparent and low in short-termed opportunism (Donaldson, 1999). The access to external funding can therefore be facilitated by CSR initiatives that drive down information asymmetries and subsequently overall agency costs. CSR can lead to long lasting, benevolent relationships with firm stakeholders and this decreases firm's risk vulnerability and compliance expenditures (Godfrey, 2005). Less investment risks will create firm value because it allows firms to undertake value-creating investments easier (El Ghouli et al., 2016). CSR investments can further result in increased customer trust and loyalty and assist in the generation of a higher product demand. Contract costs can be significantly reduced because CSR initiatives signal a firm's commitment to act in accordance with stakeholder claims and can subsequently lead to mutual commitments through trade credits (Lev et al., 2010). I conclude, that CSR initiatives ease access to scarce resources and therefore reduce firm's transaction costs. The ability to invest in CSR can therefore pose a strategic competitive advantage for firms that operate in weak institutional environments where access to social and capital resources is more difficult. The creation of internal markets framed by strategic alliances is shown to have a higher value-creating effect in countries with weak market-supporting institutions (Ricart et al., 2004). The same effect comes into play for CSR initiatives' value-enhancing effect in weak institutional environments. This proposition is consistent with research conducted by Rodriguez et al. (2006), that shows that cross-country differences in institutional quality have an effect on the effectiveness of CSR initiatives. CSR

initiatives should therefore be of higher strategic importance and create more value for firms in weak institutional environments. It can further be assumed that developing countries with institutional voids contain fewer organizations with the ability to invest in CSR, which drives up the strategic advantage of CSR.

Consequently I hypothesize, that

H_{2.1}: “The quality of a country’s market-supporting institutions moderates the relationship between CSR initiatives and firm value”

2.2.2.2 The effect of capital market development on the value-creation of CSR

Enhanced value-creation through CSR in weak institutional environments is caused by CSR initiatives’ higher ability to contribute to firm value in weaker developed capital markets. In this context, it seems logical to isolate the effect of capital market developments and further investigate its moderating effect on the relationship between CSR initiatives and firm value. A recent study shows, that capital market development is the biggest driving force in the quality of a country’s market-supporting institutions (El Ghouli et al., 2016). Information asymmetries and agency costs can lead to inefficient capital markets. These inefficient capital markets constrain firm’s access to external sources of financing and constrict their scope of strategic actions (Kim et al., 2012). CSR initiatives are effective to overcome this effect since they increase stakeholders’ perception of a firm’s transparency and a low level of managerial opportunism (El Ghouli et al., 2016). The quality of capital markets will therefore substantially impact a firm’s ability to access external firms of financing and the potential value-creating effect of CSR in this context will be higher in environments with higher information asymmetries and agency costs. I hypothesize, that

H_{2.2}: “The quality of a country’s capital markets moderates the relationship between CSR initiatives and firm value”

2.2.2.3 The effect of corporate governance development on the value-creation of CSR

Another source for cross-country differences in the value-creating effect of CSR initiatives is a country’s corporate governance level. As Mc Gee (2008) points out, corporate governance standards differ amongst countries and their effect on CSR effectiveness is therefore country-specific. By applying the same logic as in 2.2.2.2, it can be derived that countries

with a weaker corporate governance system provide more opportunities for CSR initiatives to contribute to firm value. The value-creating potential of CSR is suggested to increase along with a decrease in the quality of a country's corporate governance standards. Eldar (2014) further argues, that a focus on CSR conflicts with firm's thrive to maximize shareholder value. Shareholder theory points out the management's responsibility to maximize shareholder wealth by investing in positive NPV projects. Since CSR initiatives are very capital intense, they impede with the goal of shareholder value maximization. Due to higher corporate governance standards, managers can therefore also be discouraged to undertake CSR initiatives because corporate governance standards hinder them from endangering the goal of shareholder maximization. A higher level of corporate governance can therefore decrease the value-creating effect on CSR initiatives because the ability of CSR initiatives to fill the gap of a flawed environment is weaker in the presence of strong corporate governance standards. I hypothesise, that

H_{2,3}: "The quality of a country's corporate governance standards moderates the relationship between CSR initiatives and firm value"

2.2.2.4 Conceptual model

The hypotheses of the preceding chapter are illustrated in this conceptual model.

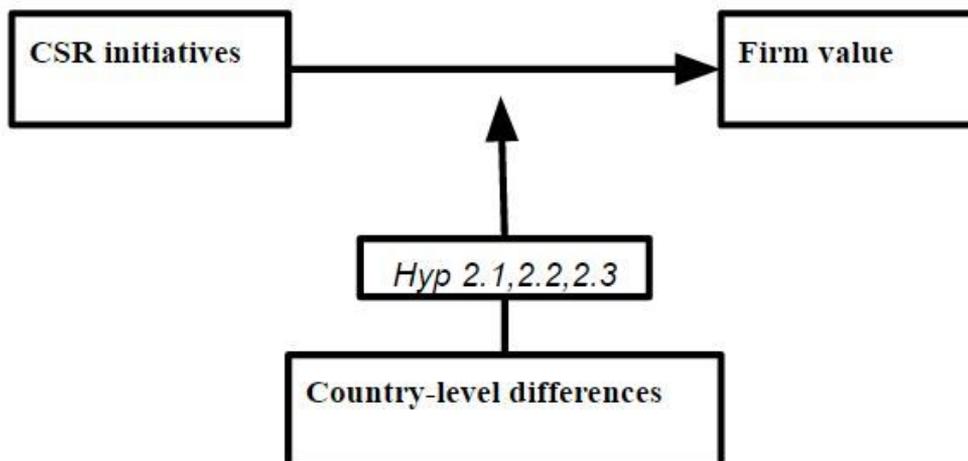


Figure 1: Conceptual model chapter 2.2.2

2.2.3 Industry-effects on value-creating effects of CSR: A closer look at controversial industries

Sturdivant and Ginter (1977) were the first scholars who pointed out the importance of industry-level differences when studying the effects of CSR-initiatives. Their view was further supported by Cottrill (1990), who states that a lack of inclusion of industry-level variables in CSR-related research will lead to clearly defective research outcomes and subsequently flawed conclusions. Subsequent research consequently took industry-level differences into account and arrived at different conclusions.

Whereas Balabanis et al. (1998) and Cowen et al. (1987) did not find any differences amongst industries when it comes to CSR, the majority of scholars arrived at different conclusions.

Waddock and Graves (1997) conducted a cross-industry study amongst 469 US-firms and found considerable differences amongst industries in terms of CSR disclosure. The effects of industry-level differences on CSR in a sample of 369 US-firms were even found to be so high, that Simpson and Kohers (2002) saw themselves forced to recommend fellow researchers to just stick to single-industry research in the future. Their view was further supported by Moore, who stated that ‘Comparing the social performance of an oil company, where environmental and employee safety issues are likely to be paramount, with a high street retailer in effect makes no sense’ (Moore, 2001). Following this logic, Acquier and Aggeri (2001) found, that CSR-initiatives in particular industries are always directed at the stakeholder group with the biggest importance for that industry. Hamid supported these findings in 2004, as he examined the CSR-reports of 48 US-firms and found a focus of reported CSR-initiatives on the stakeholder, that the individual firm considers most important. This research suggests, that industry-level differences in CSR can be explained by applying stakeholder theory.

2.2.3.1 A stakeholder-theory approach to industry-level differences in CSR

Stakeholder theory was first introduced by Freeman (1984), who defines stakeholders as all individuals or groups who affect or are affected by an organization’s thrive to achieve its strategic goals.

Since this definition applies to practically everyone, it was subsequently heavily criticized by numerous scholars (Patton, 1989; Preston & Sapienza, 1990). Clarkson (1995) therefore splits Freeman's broad group of stakeholders up into a primary and secondary component. He defines primary stakeholders as those, whose direct participation is unconditionally required for an organization in order to be able to achieve its goals. Consequently, secondary stakeholder's participation is not essential for an organization to achieve its goals. They engage in transactions with organizations in a framework of reciprocal transactions, but the transaction volume and their relevance are not critical for the organization's economic survival. Clarkson (1995) further suggests, that these primary and secondary stakeholder definitions vary by industry. He exemplarily mentioned customers as primary stakeholders for the telecommunications and retail sectors, but the environment as primary stakeholder for the automobile and fossil fuel sectors. Goyal et al. (2013) have shown, that organizational financial performance is affected by the balance of all stakeholder groups' interests in an organization's strategy. As a challenge to the widely popular opinion that firms should primarily focus on their shareholder's interests, stakeholder theory highlights the importance of a balanced treatment of the claims of all stakeholders, including shareholders. Scholars argue, that merely all organizations have a big, integrated group of stakeholders and they have the obligation and bear the responsibility to treat all of them in a well-balanced fashion.

Shareholders are just one group of many different groups of stakeholders and they should not be treated substantially favorable since all stakeholders are claimants on the firm with equal rights and responsibilities (Orts & Strudler, 2002). Ruf et al. (2001) argue, that a balanced treatment of stakeholder interests will enable organizations to keep up a high level of stakeholder support for its strategic goals and actions and consequently leads to an improved financial performance. However, proponents of Habermasian discourse ethics argue that organizations have to deal with a wide spectrum of heterogeneous stakeholder interests and it is nearly impossible to keep up a balanced incorporation of all stakeholder interest in the organization's strategic goals (Rasche & Esser, 2006). Practitioners widely supported this critical view towards stakeholder theory as they emphasized the scarceness of management resources and highlighted the critical importance of an efficient allocation of these management resources to several identified key stakeholder groups (Philips, 2004). The rising level of competition across most industries in our days causes organizations to be unable to

balance all stakeholder interests equally and assign them the same importance in their corporate decision-making procedures. Several scholars have observed a trend towards a focus on a few key stakeholder groups in recent years and consider this trend to be an ongoing phenomenon (Van Offenbeek et al., 2016). A modified version of stakeholder theory and a stakeholder group ranking according to key stakeholder attributes are there used as a managerial tool in practice to ensure an efficient allocation of scarce management resources towards the most important stakeholder groups.

Mitchell et al. (1997) conducted an exploratory study to identify these key stakeholder attributes, that managerial action should focus on. They consider legitimacy, power and urgency as main drivers of managerial attention towards different groups of stakeholders. The importance of stakeholder groups is therefore determined by the individual manifestation of these three factors in each stakeholder group's interests. The urgency of stakeholder interests can further be decomposed in time sensitivity and the overall relevance of the stakeholder's interests. Driscoll & Starik (2004) stated, that the relevance of a timely handling of stakeholder claims differs amongst industries and exemplarily show that it is particularly high for the environment as a stakeholder in the fossil-fuel industry. They further show, that the importance of stakeholder's claims is substantially different across industry sectors. Legitimacy of stakeholder claims is defined by an organization's recognition of the appropriateness and desirability of these claims. Carroll (1991) suggests considerable industry-level differences amongst the legitimacy of stakeholder claims. The power of claims is defined by the very nature of the party's relationship. If the stakeholder's bargaining power is high, he can force the organization to take strategic actions that are ultimately not in the primary interest of the organization and that the organization would not have taken in the absence of this stakeholder group. Banerjee & Bonnefous (2011) conducted a study about the relative bargaining power of different stakeholder groups in the French nuclear industry and concluded, that the power of stakeholder groups differs among all stakeholders and is highly likely to further differ amongst industry-sectors. Svenfelt et al. (2011) provided further inside to the topic as they identified four key stakeholder groups for each firm. Consumers, workforce, shareholders and the social community of the organization (including the environment) are the key determinants of the relevance of stakeholder claims in their research. They conclude, that the relevance of a stakeholder's claim rises with the number of stakeholder groups he can be placed in. Consequently it must be noted, that parties can have

several different stakes in a firm and can therefore be placed in multiple categories. He further highlights, that there are industry-level differences as to the composition and size of these stakeholder groups. Since scholars have shown all the mentioned stakeholder characteristics and groups to be different amongst industries, I conclude that the volume of CSR-initiatives as a firm action directed towards stakeholders will also differ amongst industries.

While some organizations face a homogenous group of stakeholders, others face a largely heterogenous set of opposing stakeholder interests. Conflicting stakeholder claims on the firm's strategic direction and very different needs, opinions and interests about an organization's daily business therefore present a major challenge for nearly all firms. Boutin-Dufresne & Savaria (2004) argue, that a consensus or diversity of stakeholder interests that an organization faces, is largely affected by the industry-sector that the organization operates in. Organizations in different industry sector may face diverse demands towards CSR-initiatives due to a differing stakeholder environment. This stakeholder-focused approach to CSR across individual industries was supported by numerous scholars in ensuing research (Maloni & Brown, 2006; Jenkins & Yakovleva, 2006; Kashmiri et al., 2016).

Cai et al. (2011) specifically highlight the importance of CSR for particular industries. They argue, that controversial industries like alcohol, tobacco, gaming, fossil fuels, etc. have a superior need for CSR compared to other industries caused by the nature of their activities. In alignment with these findings, Rodrigo et al. (2016) find, that stakeholders of firms in controversial industries care more about CSR-initiatives than stakeholders in other industries. They claim that concerns of sustainability are the major focus for stakeholders in controversial industries. Firms in controversial industries are therefore characterized by a higher need to invest in CSR in order to overcome their reputational deficits. As Wilson & West (1981) state, the nature of business of controversial industries is viewed with feelings of disgust and outrage by the society. These perceptions root in fundamental moral norms and values within in society. As firms in the mentioned industries endanger the fundamental goal of public health in a society, the public views them as controversial industries with questionable business models. The big question in the literature now is, if these firms can become socially responsible and derive value from their engagements in CSR (Hong & Kacperczyk, 2009). As mentioned, proponents argue that controversial industries need CSR

as a strategic tool to overcome their reputational voids and become better organizations in the public opinion. They further state, that even firms in controversial industry sectors are characterized by each human's need to act in a socially responsible manner (Frynas, 2005). Opponents argue, that managers of firms in controversial industry sectors are simply imperfect and they are not aware of the waste of resources their CSR initiatives imply (Cai et al., 2012). Opponents of CSR in controversial industries continue to acknowledge the fact, that firms in these industry sectors invest more in CSR than firms in conventional industries, but they view it critically. Even the World Health Organization concluded, that firms in controversial industry sectors should be prohibited from investments in CSR since they use them to cover up the bad effects of their business activities on the society. Palazzo & Richter (2005) recognize the high level of CSR initiatives in the controversial sector and express scepticism about the value of these CSR initiatives for the society at large. Sweeney & Coughlan (2008) attribute the higher level of CSR engagement in controversial industries to a high level of public controversies about their business and therefore a heightened need to cover them up. In line with all these scholars, I hypothesize:

H_{3.1}: "The volume of CSR initiatives of firms in controversial industries is affected by their stakeholders' special emphasis on CSR, and is therefore higher than in conventional industries"

2.2.3.2 Industry-characteristic differences in the value-creating effect of CSR

Apart from having an effect on the volume of firm's CSR initiatives, literature suggests that industry-characteristics also have an effect on the value-creating effect of CSR initiatives. This mediating effect of industry-level differences on the relationship of CSR initiatives on firm value can be explained by three mutually exclusive theories. As mentioned before, controversial industries face a higher demand for CSR by their stakeholders and are therefore a good subject to identify industry-level differences. All three theories are based on Carroll's (1991) definition of CSR as a key component of efficient stakeholder management. He further defines stakeholder management as a process, by which managers align their goals and objectives with the stakeholder claims that an organization faces. His research yields three different approaches that can shape a firm's stakeholder management, namely moral, immoral and amoral stakeholder management.

Moral stakeholder management is executed by managers who accept moral boundaries in their thrive for profit. Ethics play a big role in their decision-making procedures, as they aim to make decisions in accordance to the principles of fairness, justice and law. Morally behaving managers display a high level of ethical leadership and their overall professional behavior is conform to superior levels of conduct. To develop my first hypothesis about the mediating effect of industry characteristics on the CSR-value relationship, I assume that firms in controversial industries carry out moral stakeholder management. Jensen (2002) stated, that morally behaving managers use CSR as a management tool to enhance philanthropy, transparency and strategy within a firm and to finally drive up the firm value. This view is supported by Wood (1991), who emphasizes that managers can be defined as moral actors because their room for decisions is constrained by the overall thrive to achieve firm goals in a socially responsible way. He calls this the ‘principle of managerial discretion’ (Wood, 1991). Polonsky & Jevons (2009) find, that moral managers use CSR initiatives in their strategic concept along with core competencies and business goals to be able to drive up environmental, social and firm value simultaneously. Porter (2011) regards CSR initiatives as opportunities for firms to optimize their interaction with society rather than just inevitable costs. Inside-out and outside-in linkages are key determinants in order to identify and assess these opportunities. They define a firm’s impact on its environment through their business activities (inside-out) and the environmental effects on the firm (outside-in). Firms should identify and evaluate strategic areas for CSR along their entire value-chain by assessing their inside-out effects. Where these social or environmental linkages collide with business activities, CSR initiatives have the potential to create corporate shared value (Cottrill, 1990). The development of hybrid cars is a good example, since this product is an intersection between a car manufacturers’ fundamental operations and environmental considerations since the emission levels are declining. Technological advancements or societal developments of norms and values cause the business goals of firms in controversial industries to collide with social and environmental issues more often than this is the case in conventional industries (Rodrigo et al., 2016). In line with these findings, organizations in controversial industries have a higher potential to drive up firm value through CSR. Their inside-out and outside-in linkages with the society are deeper and more frequent than the linkages of firms in

conventional industries, which gives them a higher potential for value-enhancements through CSR and therefore more strategic utility of CSR. I hypothesize, that

H_{3.2}: “The relationship of CSR-initiatives and firm value is moderated by industry-level differences in stakeholder influence and therefore stronger for firms in controversial industries compared to conventional industries”

In line with Cai et al. (2011), I call this explanation the ‘**value-enhancement hypothesis**’.

The foundation for a contradictory prediction about the relationship of CSR initiatives and firm value is provided by Carroll’s (1991) definition of immoral stakeholder management. Immoral behaving managers are characterized by their active opposition to ethical and moral norms that a society puts forward. Their decision-making procedures lack the consideration of ethical principles and they are aware of the negative public response that their actions trigger. Barnea and Rubin (2010) conducted research about the motives of immoral behaving managers to carry out CSR initiatives. They find, that private motives are the primary driving force why immoral managers engage in CSR. Immoral managers hazard the consequences of a loss in shareholder wealth due to costly CSR initiatives to ameliorate their own reputation and gain private benefits. In their analysis of the corporate investment-decisions of the Forbes 500 CEOs, Malmendier and Tate (2005) find evidence that overly confident corporate executives are likely to overinvest in CSR. They argue, that overconfident CEOs will tolerate value-destroying over investments in CSR to derive personal benefits. Further theoretical research confirms that overconfident corporate executives sometimes make irrational investment-decisions and tolerate value destroying effects and thereby act in a way that is harmful to their business (Goel & Thakor, 2008). By acting in this harmful way, they pursue private interests prioritized to business interests and thereby act in an immoral way. Stakeholder claims and societal interests are harmed by this unethical conduct of business activities. Cai et al. (2011) conclude, that immoral managers don’t undertake CSR initiatives to support their business and thereby use them as a tool in strategic management. As mentioned above, firms in controversial industries have more linkages with their direct environment than firms in conventional industries. These linkages have a negative impact on the relationship of firm and stakeholders caused by the nature of business activities in controversial industries. Literature however suggests, that corporate executives in

controversial industries don't use CSR initiatives to compensate for the negative impact of their business on its stakeholders (Malmendier & Tate, 2005; Goel & Thakor, 2008; Barnea & Rubin, 2010). Immoral managers consequently won't use CSR to enhance the transparency of their operations either, but merely use it for their own good (Carroll, 2001). Barnea and Rubin further find, that organizations publicate their positive CSR initiatives while they withhold information about negative developments in CSR. Notwithstanding frequent negative developments in a globalized business world, most firms don't respond to societal calls for a higher engagement in CSR (Jenkins, 2005). All the mentioned points can be summarized in the **window-dressing hypothesis**. In the long-run, immoral stakeholder management will be penalized by investors in the stock market and CSR initiatives will therefore have an adverse effect on firm value. Investors will finally realize corporate executives' real motives of personal benefit extraction (e.g. reputation) and penalize these intentions. Recent research suggests, that this effect is mainly present in controversial industries. Rodrigo et al. (2016) find two possible explanations for this phenomenon, the higher level of investor scrutiny in controversial industries and a higher tendency for managers to behave in an immoral way in those industries. It is suggested, that controversial or 'sin' industries attract immoral and unethically behaving managers by the nature of their activities. El Ghouli et al. (2010) support this view, they find that CSR initiatives increase the costs of equity capital in controversial industries. They conduct their study amongst numerous industry sectors, and while all other sectors displayed a value-enhancing effect of CSR initiatives, the effect of CSR initiatives on firm value was negative for the tobacco and nuclear power industry. Consequently, I hypothesize

H_{3.3}: "The relationship of CSR-initiatives and firm value is moderated by industry-level differences in manager's intentions when carrying out CSR-initiatives and therefore weaker for firms in controversial industries and positive for firms in conventional industries"

Carroll's (1991) definition of amoral stakeholder management leads to another prediction about the relationship of CSR initiatives and firm value. Amoral managers don't consider ethical norms or values in their decision-making procedures. They simply ignore potential side-effects of their business decisions on others. Characteristic for amoral managers is a missing awareness of moral principles and simply a high degree of non-sensitivity to linkage

effects with stakeholders. Amoral management is therefore neither moral nor immoral. If we now define managers as amoral, we can assume that they neither care about reputation building and personal benefits from CSR, nor about a value-enhancing effect of CSR on firm value. Lindgreen et al. (2012) suggest, that managers in controversial industries are likely to be amoral since they work for firms in this sector despite the fact, that the society views their business activities as unsavory. Their actions are simply caused by recent trends or developments in the corporate world. If the market leader in their industry sector engages in CSR, they will simply follow his actions to copy his successful behavior (Porter & Kramer, 2006). Literature further suggests, that while CSR initiatives have a positive effect on investors, the business nature of firms operating in controversial industry sectors is likely to offset this positive effect on firm's financial performances (Cai et al., 2011). Investors link firms from controversial industries and their business operations with deep levels of distrust and 'unholy spirits from the past' (Cai et al., 2011). It can be assumed, that amoral managers simply view their CSR initiatives as irrelevant to value creation and thereby follow the logic that Modigliani and Miller put forward in their irrelevance theorem (1958). This view is supported by Nelling and Webb (2009), who don't find a correlation of CSR initiatives and a firm's financial performance and the work of Baron et al. (2011), who find a horizontal social market line, suggesting that there is no relationship of CSR initiatives and firm value. All this evidence suggests that amoral managers don't seek to create firm value through CSR initiatives and can be labeled the **value-irrelevance hypothesis** (Baron et al., 2011). It can be concluded that CSR initiatives of amoral managers will not affect firm value and are therefore value-neutral. Investors will anticipate the neutral attitude of amoral managers towards social and ethical issues and their intentions behind CSR initiatives, and therefore CSR initiatives will not be reflected in firm value changes. Consequently, I hypothesize

H_{3,4}: "There is no relationship between CSR and firm value in controversial industries"

2.2.3.3 *Conceptual model*

The hypotheses of the preceding chapter are illustrated in this conceptual framework.

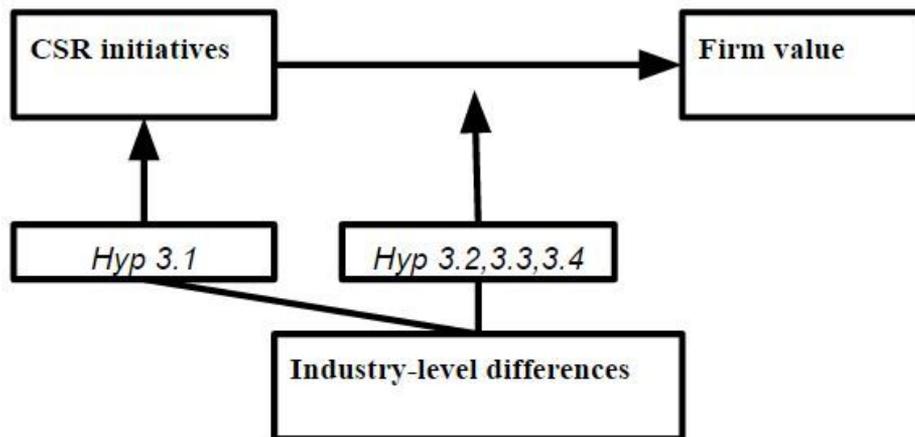


Figure 2: *Conceptual model chapter 2.2.3*

3. Methodology, Data and Sample

3.1 Variable Measurements

3.1.1 CSR initiatives

Firms undertake CSR initiatives in order to enhance their individual CSR performance. In line with Feng et al. (2014) and Cheng et al. (2014), I consequently use a firm's CSR performance as a measure for Corporate Social Responsibility. A firm's CSR performance is based on the number and volume of its CSR initiatives. This study uses the ASSET4 database as a tool to estimate a firm's CSR performance. The ASSET4 ESG database is comprised of scores of firm's social, environmental, economic and corporate governance performance. Each firm's scores in these sectors are calculated based on more than 200 objective indicators that are used as inputs. Firm's total CSR performance (CSR) is captured in the average of a firm's social (CSR_SOC) and environmental (CSR_ENV) performance scores (Luo et al., 2015). The environmental performance of a firm aims to capture a firm's effect on living and nonliving ecosystems, including land, water and air. Examples for CSR initiatives in this context are the development of ecologically friendly products or production mechanisms, the reduction of a firm's emission volume or a firm's resource consumption. Social performance scores include initiatives aimed at the generation of loyalty and trust with customers, employees and the society as a whole. Investments in human right protection, diversity programs and safety standards are examples of CSR initiatives that can enhance a firm's social performance score. The overall CSR performance (CSR) spans a possible spectrum from 0 to 100 according to the measurement in the ASSET4 database.

$$CSR = \frac{CSR_{SOC} + CSR_{ENV}}{2}$$

3.1.2 Firm value

The relationship between CSR performance and firm value is of particular interest because it represents the cumulative valuation effects of CSR initiatives on multiple levels. In line with numerous other studies (Luo & Bhattacharya, 2006; Servaes & Tamayo, 2013; Jo & Harjoto, 2011), this study uses Tobin's Q (TBQ) as a measure of firm value. Tobin's Q is defined as the quotient of a firm's market value and the total replacement value of its assets. Aligned with other studies (Malmendier & Tate, 2005; Servaes & Tamayo, 2013) I calculate Tobin's Q as follows, $TBQ = \frac{\text{book value of total assets} + \text{market value of common equity} - \text{book value of common equity}}{\text{book value of total assets}}$. As

El Ghouli et al. (2016) mention, this definition deviates from the original definition of Tobin's Q in a sense that deferred taxes are not subtracted from the numerator. Data availability concerns make this adaptation however necessary.

In order to make my results more robust, I also include industry-adjusted Tobin's Q (TBQ_ADJ) measures in my analysis. Industry-adjusted Tobin's Q measures are calculated as the difference between firm's Q and the industry median Q based on the Fama-French industry classification scheme (Cai et al., 2012). Industry-adjusted Tobin's Q measures neutralize effects of specific industries and thereby present a more robust measure for analysis (Campbell, 1996). There might be systematic variations of firm values across industries who reflect market perceptions about future growth rates in the industry or industry-specific shocks.

3.1.3 Quality of market-supporting institutions

In line with El Ghouli et al. (2016), I use various measures to approximate the quality of a country's market-supporting institutions (MSI). Stock and Credit market efficiency have to be considered as well as regulatory system, legal system and property rights. Meyer et al. (2009) states, that the integration of all these indicators in one variable yields a good proxy for the quality of a country's market-supporting institutions. Measures of stock market (SMQ) and credit market (CMQ) efficiency are developed in section 3.1.4 and illustrate whether these sources of capital are available for businesses at adequate terms of financing. To complement these measures, I rely on data from the Fraser Institute, more specifically their 'Economic Freedom of the world' report. They compute a business freedom coefficient (BF) which reflects freedom from administrative requirements and regulations, bureaucracy costs, bribes and the overall costs of tax compliance. The measure for legal system and property rights (LP) assess the quality of a country's legal system. This is judged based on the independence of judicative bodies and potential military disruptions of the legal system. The level of property rights protection is further incorporated. Each of these measures is normalized and fitted to a scale from 0 to 1. Higher values indicate a higher quality of market-supporting institutions. The average score of all these indices is used as an indicator for the quality of a country's market-supporting institutions.

$$MSI = \frac{SMQ+CMQ+BF+LP}{4}$$

3.1.4 Quality of capital markets

To investigate the effect of capital market quality in detail, I now develop detailed measures to assess the quality of capital markets. The quality of a country's capital markets can partially be estimated by using a country's stock market development index (Demirgüç-Kunt & Levine, 1996). This index is comprised of market size indicators and liquidity measures. Market Capitalization is used as a measure for a country's market size and is described by the total value of all listed shares divided by the country's GDP. Market Capitalization is of major importance for the quality of a country's capital markets since scholars predict a positive association of market size with firm's abilities to access sources of capital and diversify risks. Analysts view liquidity as an individual's ability to buy or sell securities on the markets. Liquidity can therefore be defined as the sum of all costs that occur in the process of a trade, including execution costs, search costs and time costs (to find a counterparty for the desired transaction). Due to data limitations, I proxy liquidity with total value traded divided by GDP and the turnover. Total value traded is described by the total volume of shares on the stock markets and the division of this variable by country's GDP yields a good indicator for an economy's liquidity. Turnover is defined as the division of the value of total shares traded by market capitalization. According to economic theory, a high turnover ratio implies a low level of transaction costs and higher liquidity. Turnover is a good complement to market capitalization since small, active markets are characterized by a low level of market capitalization but a high turnover ratio. It further has complementary effects with total value traded/GDP since small, liquid markets are characterized by a small level of total value traded/GDP and a high turnover.

Following the argumentation of Love (2003), I define the quality of stock markets (SMQ) as the average of the standardized measures of total market capitalization (MKT CAP), total value traded (ValTrade) and turnover (TN) and scale all these measures by the country's GDP. The standardization process is defined by a mean subtraction and division by the standard deviation.

Since the quality of country's capital markets is however not only determined by the country's stock markets, a measure of credit market quality also has to be included. In line with the definition of Fauver et al. (2003), I define credit market quality (CMQ) as the total volume of credits that banks provide to the financial sector divided by GDP.

$$SMQ = \frac{\frac{MKT\text{CAP}}{GDP} + \frac{Val\text{Trade}}{GDP} + \frac{TN}{GDP}}{3}$$

$$CMQ = \frac{\text{Total volume of bank credits provided to the public sector}}{GDP}$$

Fauver et al. (2003) states, that stock market quality and credit market quality both need to be considered for the overall quality of a country's capital markets. I consequently normalize both variables (SMQ, CMQ) and use their average as an indicator for a the quality of a country's capital markets (CAPMQ).

$$CAPMQ = \frac{SMQ + CMQ}{2}$$

3.1.5 *Quality of corporate governance standards*

Corporate standards are shown to substantially differ amongst countries (Mc Gee, 2008). The quality of a country's corporate governance standards illustrates firm's abilities to implement corporate governance standards themselves and can be quantified using publicly available World Bank data. Worldwide governance indicators are annually published by the World Bank and illustrate the quality and level of a country's corporate governance standards. I therefore define the quality of a country's corporate governance standards (CGS) as the average of these governance indicators (Eldar, 2014). The first indicator is defined as voice and accountability (VA), it indicates people's abilities to practice free speech, the freedom of expression and to actively participate and select their government and other executive and legislative bodies. Political stability and the absence of violence (PV) illustrate the probability of a coup or the destabilization of the government in an unlawful and violent manner. Government effectiveness (GE) mainly measures the quality of public services and the reliability and predictability of government actions. It further includes the level of bureaucracy the government needs to achieve its goals. Regulatory Quality (RQ) defines the government's ability to ensure a sound development of the private sector through the formulation and execution of policies and laws. The level of confidence of a society in the quality of a country's executive bodies (e.g. police), judicative bodies (e.g. courts), property rights and contract enforcement mechanisms is defined as the rule of law (RL). A country's level of corruption in the private and the public sector and the development and enforcement of anti-corruption laws is illustrated in the control of corruption (CC) indicator. The average of all these indicators provides a good proxy for the quality of a country's corporate

governance standards. The development of firm-level corporate governance standards is shown to be largely affected by this country-level measure (Eldar, 2014).

$$CGS = \frac{VA + PV + GE + RQ + RL + CC}{6}$$

3.1.6 Controversial industries/ conventional industries

I define controversial industries as industry sectors that are ‘characterized by political pressures, moral debates and social taboos’ (Cai et al., 2011). These industry sectors include industries that are perceived to be sinful, such as gambling, alcohol and tobacco. However, industry sectors with an emerging level of environmental and social debates like military, nuclear, oil and biotech firms should also be included in the cluster of controversial industries (Jo & Na, 2012). I base my classification on research by Fama & French (1997) and their 48 industry classifications. Controversial industries include alcohol firms (Fama & French group 4) with SIC-codes 2080-2085, tobacco firms (group 5) with SIC-codes 2100-2199, suppliers of military goods (group 26) with SIC-codes 3760-3769, 3795, 3480-3489 and oil firms (group 30) with SIC-codes 1300, 1310-1339, 1370-1382, 1389, 2900-2912, 2990-2999. Biotech firms (group 46) with SIC-codes 2833-2836 and cement firms (group 7) with SIC-codes 3240-3241 are further included. I further follow Hong and Kacperczyk (2009), and include gambling stocks with NAICS codes 7132, 71312, 713120, 71329, 713290, 72112, 721120. Due to recent environmental discussions I further include all firms in the coal industry with SIC-codes 1200-1299. The residual of all remaining firms consequently shapes the cluster of conventional industries. I create an industry-specific dummy (CONTROVERSIAL) variable that takes the value 0 for conventional industries and 1 for controversial industries.

3.1.7 Control Variables

Other explanatory factors need to be captured in order to isolate the desired effects as accurately as possible. Control variables are shown to drive the severity of omitted variable bias down and subsequently lead to a lower level of bias in the observed slope coefficients. The used firm-level control variables include firm size (SIZE), profitability (ROA), leverage (LEV), sales growth (SGR) and the ratio of R&D expenditures to total assets (R&D). These control variables are widely used in the literature (El Ghoul et al., 2016).

All the mentioned control variables are widely used in firm value studies and included to ensure that the effect of CSR doesn't pick up effects of other variables. Since larger firms tend to be diversified, they are subject to the diversification discount (Claessens et al., 2002). I therefore include firm size as a control variable and define it as the natural logarithm of a firm's total assets in USD (SIZE).

SIZE = natural logarithm of total assets in USD

Furthermore, more profitable firms tend to be valued higher by investors and this effect is captured by controlling for the return on assets (ROA), which is calculated as EBITDA divided by the firm's total assets.

$$ROA = \frac{EBIT(\text{earnings before interests and taxes})}{Total\ Assets}$$

Firms with higher relative levels of debt are subject to costs of financial distress and agency costs of debt, therefore I include a firm's leverage ratio as the firm's total debt divided by its total assets.

$$LEV = \frac{Total\ Debt}{Total\ Assets}$$

Expenses in Research & Development can create firm value, even though they are typically expensed but not capitalized. I therefore control for R&D expenses as the ratio of R&D expenditures to a firm's total assets. I assume that non-reporting firms do not undertake R&D activities and set their value to 0. This assumption allows me to keep a high number of observations.

$$R\&D = \frac{R\&D\ expenditures}{Total\ Assets}$$

Since Klapper & Love (2004) proved that growing firms enjoy higher valuations in the market, I include growth rates as the change in total sales to the previous year.

SGR = annual percentage change in the total sales volume

To control for the effects of capital expenditures on firm value, I include them in my analysis as the ratio of capital expenditures to total assets.

$$CAP\ EX = \frac{Capital\ Expenditures}{Total\ Assets}$$

I further include country-level control variables to further drive down the omitted variable bias. According to Griffin and Prakash (2014), firms in economically developed countries are likely to be valued higher than firms in developing countries. Therefore I include economic development (GDP) as a control variable and measure it as the natural logarithm of the country's GDP/capita ratios.

GDP = natural logarithm of GDP per capita

3.2 Data and Sample

The required data for the analysis is obtained from different sources. The initial sample consisted of all 5,823 companies that are included in the ASSET4 database in the sample period from 2006-2014. The resulting 46,584 firm-year-observations were cut because of data limitations and the final sample consists of 22,034 firm-year-observations from 3,670 firms. I exclude all observations with missing values for variables because the initial dataset resulted in an unbalanced panel. All firms in the financial industry (SIC codes 6000-6999) were excluded from the sample due to their unique regulatory background. Information about a firm's CSR performance and the financial data are obtained from the ASSET4 database of Thompson Reuters' Worldscope database. The data about the quality of stock markets and credit markets and subsequently the combination to capital market quality data was obtained from the World Financial Development Database (WFDD) published by the World Bank. Data concerning the levels of business freedom and the presence of strong legal system and property rights were obtained from the Economic Freedom of the World (EFW) database that the Fraser Institute publishes annually. The data about the level of country corporate governance standards were obtained from the Worldbank's Worldwide Governance Indicators (WGI) database. All variables were winsorized at a 1%-level in order to control for the effects of outliers.

3.3 Regression Models

The following regression models are estimated in order to test the proposed hypotheses. Model 1 tests Hypothesis _{1.1, 1.2}, Model 2 tests Hypothesis _{2.1}, Model 3 tests Hypothesis _{2.2} and Model 4 tests Hypothesis _{2.3}. Hypothesis _{3.2, 3.3, 3.4} are tested in Model 6. These models therefore include the tested factor and the interaction effect of this factor with the measure of CSR. Model 5 tests the joint effect of all country-level variables and Model 7 tests the joint effect of country and industry-level variables. All models are tested with the Ordinary Least Squares (OLS) method, which is commonly used method to test effects of CSR performance on indicators of firm's financial well-being (Nelling & Webb, 2009). To further control for potential endogeneity problems, all independent variables are lagged.

$$(1) TBQ_{i,t} = \beta_0 + \beta_1 * CSR_{i,t-1} + \beta_2 * SIZE_{i,t-1} + \beta_3 * ROA_{i,t-1} + \beta_4 * LEV_{i,t-1} + \beta_5 * SG_{i,t-1} + \beta_6 * R\&D_{i,t-1} + \beta_7 * GDP/CAPITA_{i,t-1} + \beta_8 * CAPEX_{i,t-1} + \sum Year_Dummies + \sum Industry_Dummies + \sum Country_Dummies + \varepsilon_{i,t}$$

$$(2-4,6) TBQ_{i,t} = \beta_0 + \beta_1 * CSR_{i,t-1} + (\beta_2 * MSI_{i,t-1} + \beta_3 * CSR_{i,t-1} * MSI_{i,t-1}) + (\beta_2 * CAPMQ_{i,t-1} + \beta_3 * CSR_{i,t-1} * CAPMQ_{i,t-1}) + (\beta_2 * CGS_{i,t-1} + \beta_3 * CSR_{i,t-1} * CGS_{i,t-1}) + (\beta_2 * INDUSTRY_{i,t-1} + \beta_3 * CSR_{i,t-1} * INDUSTRY_{i,t-1}) + \beta_4 * SIZE_{i,t-1} + \beta_5 * ROA_{i,t-1} + \beta_6 * LEV_{i,t-1} + \beta_7 * SG_{i,t-1} + \beta_8 * R\&D_{i,t-1} + \beta_9 * GDP/CAPITA_{i,t-1} + \beta_{10} * CAPEX_{i,t-1} + \sum Year_Dummies + (\sum Industry_Dummies) + (\sum Country_Dummies) + \varepsilon_{i,t}$$

$$(5) TBQ_{i,t} = \beta_0 + \beta_1 * CSR_{i,t-1} + \beta_2 * MSI_{i,t-1} + \beta_3 * CSR_{i,t-1} * MSI_{i,t-1} + \beta_4 * CAPMQ_{i,t-1} + \beta_5 * CSR_{i,t-1} * CAPMQ_{i,t-1} + \beta_6 * CGS_{i,t-1} + \beta_7 * CSR_{i,t-1} * CGS_{i,t-1} + \beta_8 * SIZE_{i,t-1} + \beta_9 * ROA_{i,t-1} + \beta_{10} * LEV_{i,t-1} + \beta_{11} * SG_{i,t-1} + \beta_{12} * R\&D_{i,t-1} + \beta_{14} * CAPEX_{i,t-1} + \sum Year_Dummies + \sum Industry_Dummies + \varepsilon_{i,t}$$

$$(7) TBQ_{i,t} = \beta_0 + \beta_1 * CSR_{i,t-1} + \beta_2 * MSI_{i,t-1} + \beta_3 * CSR_{i,t-1} * MSI_{i,t-1} + \beta_4 * CAPMQ_{i,t-1} + \beta_5 * CSR_{i,t-1} * CAPMQ_{i,t-1} + \beta_6 * CGS_{i,t-1} + \beta_7 * CSR_{i,t-1} * CGS_{i,t-1} + \beta_8 * INDUSTRY_{i,t-1} + \beta_9 * CSR_{i,t-1} * INDUSTRY_{i,t-1} + \beta_{10} * SIZE_{i,t-1} + \beta_{11} * ROA_{i,t-1} + \beta_{12} * LEV_{i,t-1} + \beta_{13} * SG_{i,t-1} + \beta_{14} * R\&D_{i,t-1} + \beta_{15} * GDP/CAPITA_{i,t-1} + \beta_{16} * CAPEX_{i,t-1} + \sum Year_Dummies + \varepsilon_{i,t}$$

Hypothesis _{3,1} is tested in a two-stage regression. Country/Year average of CSR and country/industry average of CSR are used as instrumental variables in the CSR equation (Gonenc & Scholtens, 2016), and Leverage and ROA in the value equation (Cai et al., 2011). These variables are considered to have an effect on the dependent variables of the respective equations, but not on the dependent variables of the other equation. Exemplary, Leverage and ROA is considered to have an effect on Tobin's Q, but not on CSR. The equations are constructed as follows:

$$(8a) TBQ_{i,t} = \beta_0 + \beta_1 * CSR_{i,t} + \beta_2 * LEV_{i,t-1} + \beta_3 * ROA_{i,t-1} + \beta_4 * R\&D_{i,t-1} + \beta_5 * CAPEX_{i,t-1} + \beta_6 * SIZE_{i,t-1} + \beta_7 * GDP/capita_{i,t-1} + \beta_8 * SG_{i,t-1} + \beta_9 * MSI_{i,t-1} + \beta_{10} * CAPMQ_{i,t-1} + \beta_{11} * CGS_{i,t-1} + \varepsilon_{i,t}$$

$$(8b) \text{ CSR}_{i,t} = \beta_0 + \beta_1 * \text{TBQ}_{i,t} + \beta_2 * \text{Year/Country-CSR}_{i,t-1} + \beta_3 * \text{Industry/Country-CSR}_{i,t-1} + \beta_4 * \text{R\&D}_{i,t-1} + \beta_5 * \text{CAPEX}_{i,t-1} + \beta_6 * \text{SIZE}_{i,t-1} + \beta_7 * \text{GDP/capita}_{i,t-1} + \beta_8 * \text{SG}_{i,t-1} + \beta_9 * \text{MSI}_{i,t-1} + \beta_{10} * \text{CAPMQ}_{i,t-1} + \beta_{11} * \text{CGS}_{i,t-1} + \varepsilon_{i,t}$$

4. Results

I first present the descriptive statistics and then proceed to the regression results.

4.1 Descriptive statistic and correlations

4.1.1 Descriptive statistics

The preceding table presents the sample descriptive statistics.

Table 1: Table of Descriptive Statistics

	Observations	Mean	Median	Standard Deviation	Min.	Max.
Tobin's Q	22,034	1.7498	1.3992	1.0485	0.2773	23.7510
CSR	22,034	52.3838	62.05	18.6043	23.49	96.59
Size	22,034	15.2370	15.2364	1.5389	9.6511	18.6167
ROA	22,034	0.09754	0.08573	0.0860	-0.5113	0.4350
Leverage	22,034	0.2560	0.2419	0.1746	0	0.8302
R&D	22,034	0.02170	0.0055	0.0366	0	0.2296
Sales Growth	22,034	1.1334	1.0787	0.3394	0.4515	4.8013
CapEx	22,034	0.0538	0.4058	0.4906	-0.0087	1146.53
ln GDP/capita	22,034	10.2705	10.5346	0.8480	6.9180	10.9840
MSI	20,614	0.5408	0.4927	0.1330	0.1007	0.9874
CAPMQ	20,614	0.4968	0.5387	0.1587	0.1892	0.9476
CGS	22,034	1.1840	1.2850	0.5616	-0.5598	1.7712

The following tables illustrate the distribution of countries and industries amongst the sample.

Table 2: Table of Descriptive Statistics by Country - Mean values of important variables

	Observations	Mean-Tobin's Q	Mean-CSR	Mean-MSI	Mean-CAPMQ	Mean-CGS
Australia	1,404	1.8328	36.0314	0.5353	0.4016	1.6027
Austria	97	1.3979	65.3680	0.4552	0.2870	1.5772
Belgium	139	1.4507	59.1812	0.4137	0.2647	1.3115
Brazil	337	1.8016	60.4297	0.1861	0.2725	0.0266
Canada	1,513	1.6893	38.0964	0.5613	0.4105	1.6181
Chile	93	1.6601	43.1366	0.4195	0.3300	1.1820
China	339	1.5713	32.5695	0.3822	0.4514	-0.5212
Columbia	26	1.4982	59.6279	0.2260	0.0752	-0.3038
Czech Republic	18	1.3321	48.4214	0.3401	0.2213	0.8909
Denmark	148	2.2934	63.2822	0.5916	0.3067	1.8066

Master Thesis - **Christian Flachsland** - *International Financial Management*

Egypt, Arab. Rep.	35	1.1969	22.8746	0.1781	0.0490	-0.5578
Finland	191	1.6371	74.5652	0.5370	0.4670	1.8307
France	646	1.5266	77.8662	0.4336	0.4949	1.2125
Germany	553	1.6078	67.8740	0.4494	0.4961	1.4785
Greece	115	1.2825	47.0811	0.3009	0.4576	0.4483
Hong Kong	696	1.7069	31.8809	0.9267	0.9883	1.4376
Hungary	15	1.0823	75.8767	0.3485	0.0931	0.6682
India	311	2.4684	61.2516	0.2866	0.1223	-0.0698
Indonesia	108	2.6066	52.4022	0.2000	0.0573	-0.3739
Ireland	86	2.0880	35.5597	0.4756	0.3072	1.4919
Israel	55	1.7553	43.9787	0.3304	0.1290	0.6018
Italy	245	1.2783	68.2104	0.3675	0.3596	0.5264
Japan	2,840	1.2734	57.6845	0.5485	0.5529	1.2453
Kazakhstan	4	1.0421	20.2450	0.3168	0.0553	-0.5125
Kuwait	6	1.3774	64.5542	0.4178	0.1436	0.0826
Luxembourg	35	1.9807	58.2996	0.5468	0.4958	1.6989
Malaysia	163	2.0780	46.2685	0.2141	0.0532	-0.1727
Mexico	117	1.9075	43.4877	0.4715	0.3698	0.3555
Morocco	7	3.0914	58.2300	0.2769	0.1253	-0.3187
Netherlands	205	1.5727	74.5270	0.5233	0.5192	1.6698
New Zealand	81	1.7412	42.9636	0.5640	0.3404	1.7860
Norway	161	1.5610	57.3283	0.5004	0.3467	1.7191
Peru	9	1.8269	24.6411	0.2546	0.0546	-0.2481
Philippines	68	2.0664	38.0416	0.2587	0.0705	-0.3705
Poland	75	1.3313	35.9043	0.3385	0.1423	0.8133
Portugal	71	1.4615	76.8126	0.4030	0.3780	0.9728
Qatar	7	2.4919	11.4934	0.4446	0.0886	0.6730
Russia	174	1.5007	50.1761	0.2627	0.0993	-0.5672
Saudi Arabia	30	1.9311	39.8875	0.4534	0.1395	-0.3166
Singapore	278	1.6775	38.1625	0.5984	0.4935	1.5138
South Korea	414	1.4409	59.9030	0.4463	0.6232	0.7606
Spain	260	1.8249	79.4912	0.4518	0.6423	0.8482
Sri Lanka	5	1.3436	66.5050	0.2308	0.0526	-0.3227
Sweden	306	1.8125	73.5517	0.5425	0.5154	1.7688
Switzerland	364	2.1897	59.7144	0.6253	0.7288	1.4798
Taiwan	525	1.6075	44.2383	0.4690	0.4893	0.9843
Thailand	82	2.2238	57.2566	0.3454	0.4997	-0.2934
Turkey	88	1.9220	54.1871	0.2863	0.2875	-0.0667
United Arab. Emirates	13	1.3789	33.7090	0.4421	0.4105	0.5590
United Kingdom	2,051	1.8173	62.7506	0.5743	0.5030	1.4106
United States	6,425	2.0259	48.1152	0.6230	0.6304	1.2485
Total	22,034	1.7498	52.3838	0.5408	0.4968	1.1840

The highest number of observations stem from the United States with 6,425 firm-year observations and the fewest number of observations come from Kazakhstan with 4 firm-year observations. Hong Kong displays the highest quality of market-supporting institutions in average over the sample period, whereas the market-supporting institutions in the Arabic

Republic of Egypt are the worst. Hong Kong also tops the list in terms of capital market quality, whereas Sri Lanka displays the worst capital market quality. Finland shows the highest levels of country-level governance indicators and the Russia holds the last places in this category. In terms of the dependent variable, Morocco displays the highest values of Tobin's Q, whereas Kazakhstan displays the lowest. The best performing country in terms of CSR is Spain, the worst is Qatar. The table below presents descriptive statistics broken down to industry sectors. It can be stated, that 15.74% of all firm-year observations meet my criterion of controversial industries. The average values further imply, that firms in controversial industries have a lower average Tobin's Q and a higher average CSR performance.

Table 3: Table of Descriptive Statistics by Industry

SIC-code	Industry	Observations	Mean - Tobin's Q	Mean - CSR
0100-0999	Agriculture, Forestry, Fishing	133	1.8695	51.6303
1000-1499	Mining	2,412	1.8036	50.3694
1500-1799	Construction	795	1.8872	54.2754
2000-3999	Manufacturing	9,840	1.7386	53.6910
4000-4999	Infrastructure	3,426	1.7261	52.6180
5000-5199	Wholesale Trade	569	1.7048	49.2811
5200-5999	Retail Trade	1,497	1.7462	50.4471
7000-8999	Services	3,362	1.7404	50.7343
Total		22,034	1.7498	52.3838
Conventional Industries		18,566	1.7580	52.1274
Controversial Industries		3,468	1.7059	53.7564

4.1.2 Correlations and multicollinearity

The correlation matrix is displayed in the appendix. No problems of multicollinearity were detected.

4.2 Regression results

The following table presents the regression results for Models (1)-(7).

Table 4: Regression results Model (1)-(7)

This table shows the results of an OLS regression of the proposed models. Tobin's Q is used as a dependent variable in all the models. Model (1) tests the overall effect of CSR on Tobin's Q in isolation. Models (2)-(4) test the respective moderating effect of the country-level variables in isolation, and Model (5) tests the joint effects of these country-level variables. Model (6) tests the moderating effect of the industry-level dummy for controversial industries. Model (7) combines all previous models and tests the joint effects of all the mentioned cross-country or cross-industry level variables and the moderating effects on the CSR value relationship. Moderating effects are tested by the inclusion of an interaction term (CSR*country/industry-level variable) in the respective models. The detailed measurement procedures of all variables are outlined in chapter 3. The inclusion of year-fixed effects and industry-fixed effects is indicated for the individual models.

Note: Statistical significance at a 10%, 5% and 1% level is indicated by the display of *, ** or ***. Standard errors are reported in brackets beneath the coefficients.

	Model (1)	Model (2)	Model (3)	Model (4)	Model (5)	Model (6)	Model (7)
CSR	0.016*** [0.004]	0.019*** [0.006]	0.019*** [0.005]	0.090*** [0.010]	0.086*** [0.012]	0.015*** [0.004]	0.074*** [0.012]
SIZE	-0.657*** [0.031]	-0.645*** [0.029]	-0.691*** [0.031]	-0.225*** [0.045]	-0.268*** [0.047]	-0.676*** [0.030]	-0.259*** [0.046]
ROA	8.545*** [0.538]	9.006*** [0.560]	8.768*** [0.520]	9.197*** [0.540]	9.351*** [0.559]	9.509*** [0.584]	10.113*** [0.564]
Leverage	-2.007*** [0.309]	-1.764*** [0.314]	-1.675*** [0.296]	-1.770*** [0.299]	-1.554*** [0.305]	-1.569*** [0.292]	-1.119*** [0.288]
R&D	21.742*** [1.314]	23.111*** [1.367]	22.549*** [1.208]	19.917*** [1.288]	21.655*** [1.341]	21.401*** [1.180]	21.432*** [1.117]
Sales Growth	0.393*** [0.083]	0.398*** [0.087]	0.404*** [0.086]	0.363*** [0.081]	0.379*** [0.084]	0.392*** [0.084]	0.367*** [0.084]
CapEx	2.365*** [0.734]	2.088*** [0.746]	1.980*** [0.653]	1.912** [0.746]	1.666** [0.768]	1.799*** [0.660]	0.701 [0.658]
ln GDP/capita	0.004 [0.090]	-0.110* [0.061]	0.043 [0.097]	0.027 [0.089]	-0.091 [0.059]	0.066 [0.095]	-0.039 [0.062]
MSI		0.017 [0.498]			-1.051 [0.975]		-0.455 [1.001]
MSI*CSR		-0.005 [0.010]			0.018 [0.019]		0.007 [0.020]
CAPMQ			0.867* [0.476]		1.198 [0.902]		0.712 [0.916]
CAPMQ*CSR			-0.023* [0.009]		-0.026 [0.017]		-0.017 [0.018]
CGS				1.142*** [0.306]	1.324*** [0.311]		1.901*** [0.312]
CGS*CSR				-0.064*** [0.007]	-0.062*** [0.008]		-0.076*** [0.007]
CONTROV.						-1.081*** [0.236]	-1.162*** [0.233]
CONTROV.*CSR						0.029*** [0.004]	0.032*** [0.004]
Constant	8.295*** [1.240]	9.418*** [1.112]	8.911*** [1.282]	0.337 [1.367]	2.290* [1.263]	9.910*** [1.256]	2.559** [1.035]
Adj. R-squared	0.139	0.137	0.134	0.141	0.139	0.137	0.137
Observations	22034	20614	20614	22034	20614	22034	20614
Year	Yes						
Industry	Yes	Yes	Yes	Yes	No	No	No

As the this research uses data analysis to test the formulated hypothesis, all hypotheses will be evaluated according to their statistical significance in the dataset. The results show strong support for $H_{1,1}$, as the coefficient of CSR is found to be positive in all conducted models. This finding is line with numerous scholars, who empirically proved a value-enhancing effect

of CSR initiatives (Luo & Bhattacharya, 2006; Servaes & Tamayo, 2013; Jo & Harjoto, 2011). Many scholars find a small positive significant effect of CSR on firm value. The concept of the ‘social contract’ (Carroll, 1979) and its value-generating potential for firms is thereby confirmed. Furthermore, many of the control variables are found to be significant. The existence of country-level moderators of the CSR-value relationship is proposed in $H_{2,1}$, $H_{2,2}$ and $H_{2,3}$. All these effects are first tested in separate models, and then bundled up in a joint model to evaluate the simultaneous occurrence of these country-level moderators. Moderating-effects are tested by the inclusion of an interaction term between the independent variable and the proposed moderator in the regression models. Exemplarily, the moderating effect of market-supporting institutions is tested by the interaction effect MSI*CSR. I find small negative coefficients for the interaction effects of capital markets and CSR and governance standards and CSR, indicating that they have a negative effect on the value-creation of CSR. The effect of capital market quality is found to be statistically significant only when solely this effect is tested, and the effect of country-level governance is significant in all models. Country-level governance standards are further found to have a positive effect on Tobin’s Q in all models. Capital market quality also has a positive effect on Tobin’s Q, whereas the effect of market-supporting institutions on CSR is found to be ambiguous (negative in the joint models and positive in the individual model). The industry-dummy (CONTROV) is found to have a small positive effect on the relationship of CSR on firm value. This supports the value-enhancing hypothesis $H_{3,2}$ as the coefficient is positive, indicating a positive effect of industry-affiliation on the relationship. Controversial Industry firms are therefore found to have a higher ability to create value through CSR. Furthermore, the effect of controversial industries on firm value is negative, this indicates a systematically lower valuation of firms in controversial industries. The highest coefficient of the country-level moderators is -0.076 for the country-level governance standards in (7), the coefficient for the industry-level effect is 0.032. Whereas both coefficients have the expected sign and are statistically significant, the country-level variable therefore has a higher effect on the relationship of CSR and firm value. It can be concluded, that $H_{3,2}$ and $H_{2,3}$ can be confirmed on a statistically significant level, whereas $H_{2,2}$ can not be confirmed on a statistically significant level. $H_{2,1}$ has to be neglected because there is no identical sign of the

coefficient in all relevant models. All control variables except the logarithm of GDP/capita display statistically significant coefficients and therefore show an effect on firm value.

In order to test $H_{3,1}$, I conduct a two-stage regression model to evaluate the effect of the industry-dummy (CONTROV.) on the total volume of CSR. I find a small positive effect (0.244) of the dummy-variable for controversial industries on CSR and consequently find support for my hypothesis since this effect is significant on a 10% level. Table 5 further gives an answer to the question of reversed causality. It shows, that CSR has a significant positive effect on Tobin's Q, whereas Tobin's Q doesn't have a significant effect on CSR. The results further show the negative effect of the industry-dummy on firm value, more evidence that firms in controversial industries are valued less by investors when controlling for the firm characteristics that I introduced as control variables. It is further found, that country-level characteristics don't have a significant effect on CSR aside from country-level governance standards which have a very little significant negative effect. Capital market quality also has a negative, but highly insignificant effect on CSR. Country governance standards continue to have a positive effect on Tobin's Q.

The next table illustrates the results of the two-stage regression model.

Table 5: System of equation results Model (8)
 This table shows the results of a two-stage regression of model 8. The dependent variable in the firm value equation (8a) is industry-adjusted Tobin's Q. The dependent variable in the CSR equation (8b) is the constructed measure of CSR performance in chapter 3. The instrumental variables used in model 8a include leverage and the return on assets. Model 8b uses the average CSR performance scores by country/year and by country/industry. The inclusion of year-fixed effects is indicated for the individual models. The sample includes 22,034 observations in a period from 2006-2014.
 Note: Statistical significance at a 10%, 5% and 1% level is indicated by the display of *, ** or ***. Standard errors are reported in brackets beneath the coefficients.

	Model (8a)	Model (8b)
CSR	0.037*** [0.011]	
TBQ		0.151 [0.224]
LEV	-3.553*** [0.564]	
ROA	9.955*** [0.251]	
Country/Year CSR		0.614*** [0.025]
Country/Industry CSR		0.442* [0.226]
R&D	23.030*** [0.772]	-0.045 [0.745]
CapEx	2.529*** [0.493]	-0.087 [0.550]

	-0.756***	-0.014*
SIZE	[0.022]	[0.052]
	0.379***	0.202
Sales Growth	[0.050]	[0.211]
	-0.007	0.008
GDP/capita	[0.006]	[0.007]
	0.009	0.027
MSI	[0.020]	[0.017]
	1.051	-0.137
CAPMQ	[0.975]	[1.892]
	1.870***	-0.008*
CGS	[0.446]	[0.005]
	-0.134***	0.244*
CONTROV.	[0.001]	[0.131]
Adj. R-squared		-0.081
Observations	22034	22034
Year	Yes	Yes

4.3 Robustness tests

The results I find are robust due to the use of industry-adjusted Tobin's Q as an alternative measure of firm value. As Cai et al. (2012) put forward, the use of industry-adjusted Tobin's Q is an effective tool to prove the robustness of regressions on firm value. The Appendix provides the detailed results of these robustness tests.

5. Conclusion

As CSR is experiencing growth all around the world as a global phenomenon, lawmakers seek to create incentives for firms to invest in CSR initiatives in their countries. Differences in the quality of market-supporting institutions, capital markets and country governance standards are discussed as potential moderating factors in the CSR-value relationship, that can explain different levels of CSR from firms around the globe. Furthermore, this study introduces industry-level differences as potential factors to explain the differences in CSR across firms. The existence of reputational voids in controversial industry sectors is used as an example to investigate industry-level factors. Along with institutional voids which are characterized by a low quality of market-supporting institutions, capital markets and country governance standards, these reputational voids are found to be a key determinant of the value-creating potential of CSR. As such, they are of great importance to corporate executives since value-maximization, by nature, is a primary concern to them. This study therefore examines the research question:

Is the ability to overcome institutional voids or the ability to overcome reputational voids a more important determinant of the value affecting ability of CSR initiatives?

In order to answer this question, this study first examines the overall effect of CSR on firm value, then examines the effect of the proposed country and industry-level variables and finally links them in one model to compare their effect. Furthermore, this study conducts a two-stage regression to examine the effects of the moderators on CSR and firm value separately and take care of ‘reversed causality’ concerns.

Across all models, this study confirms the positive effects of CSR initiatives on firm value. In line with many other scholars, I find a small positive effect (Luo & Bhattacharya, 2006; Servaes & Tamayo, 2013; Jo & Harjoto, 2011). This finding supports the stakeholder theory approach and the social contract argumentation by Carroll (1979), who claims that firms bear certain responsibilities, for the purpose of this study CSR initiatives, towards their environment in order to benefit from the rights the environment grants to them. As Tobin’s Q reflects investor’s perceptions about the value of a firm, my findings suggest that investors reward firms who engage in CSR initiatives with a higher market valuation compared to identical firms, who don’t undertake CSR initiatives. This finding is good news for

lawmakers and all other members of the society as it suggests that the maximization of shareholder value goes along with socially and environmentally responsible initiatives. It challenges the widespread assumption in the society, that value-maximizing firms can't consider social and environmental issues in their corporate decision-making without forfeiting firm value.

Referring back to my initial research question, this study confirms that CSR initiatives are suitable to overcome the potentially negative impacts of institutional and reputational voids. The quality of capital markets and the quality of a country's corporate governance standards is found to be negatively affecting the relationship of CSR and firm value. CSR initiatives therefore have a higher effect on firm value in countries with a lower quality of capital markets and worse country-wide governance standards. Weak country-level institutions constitute an environment, where CSR initiatives can create higher firm value gains than in environments with strong institutions. The quality of market-supporting institutions doesn't have a clear effect on the value-creating ability of CSR initiatives, suggesting that a certain level of market-supporting institutions is necessary in order to enable a valuation and recognition of a firm's CSR initiatives, but once this threshold is reached, the quality of market-supporting institutions doesn't affect the value-creation through CSR anymore. CSR can't substitute for higher level market-supporting institutions anymore. A minimum-level of market-supporting institutions is undoubtedly needed to enable investors to consider CSR initiatives in their valuations. The effect of capital market quality is much more obvious in my results. Capital market quality consistently negatively affects the value-creation through CSR, suggesting that environments with weaker capital markets provide better opportunities for CSR initiatives to translate to firm value. This finding further suggests, that firms in countries with well-developed capital markets will take advantage of the good access to capital and increase their level of real investments instead of their CSR-level. This study consequently finds a negative effect of capital market quality on CSR. Country-level governance standards are found to have the strongest negative moderating effect on the CSR-value relationship from all the three country-level variables that are examined in this study. Interestingly, I find the reverse effect of country-level governance standards on Tobin's Q. Firms located in countries with high governance standards therefore systematically enjoy higher market valuations when controlling for important firm characteristics and the country's level of GDP/capita. Firms in

controversial industry sectors have a higher potential to create firm value through CSR due to the reputational voids in their business environment. This leads to a higher level of CSR investments in these industry sectors. When all these effects are compared, I observe the highest absolute value for the moderating effect of country governance standards, followed by the effect of controversial businesses and capital market quality. I can therefore answer my research question with the observation that while institutional and reputational voids both moderate the CSR-value relationship, the ability to overcome institutional voids is the superior determinant of value-creating abilities of CSR in different contexts.

My findings imply a lack of power for lawmakers to create incentives for CSR through a higher capital market or country governance quality. Since the overall relationship of CSR and firm value is nevertheless positive, the society needs to find other ways to incentivise managers to invest in CSR. Both the society and the firm can subsequently benefit from CSR. It is further implied, that especially firms in controversial industries benefit from investment in CSR since they can derive more value from these investments than other firms. However, due to the mentioned recommendations of the WHO, CSR initiatives of controversial firms are under high scrutiny at the moment. As the WHO recommends a high level of control and restrictions for CSR initiatives of controversial firms, I expect there to be regulatory responses in the near future. These tighter regulations might lead to higher levels of reputational voids in the near future, causing either an even higher level of value-creating ability through CSR for those firms or a value-destroying effect of CSR because it will be perceived as window-dressing. These developments seem to be a promising subject for future research.

Finally, this study is subject to several limitations. It is nearly impossible to accurately assess a firm's CSR performance. While the volume of investments in CSR can be observed, the translation of these investments into the desired positive perception of the society can't be objectively measured. These difficulties in the measurement of CSR continuously lead to conflicting research outcomes. Furthermore, the proxies for business freedom, the level of property rights and country governance standards that this study uses to construct variables are not objectively observable and the used indices are therefore subject to bias.

Acknowledgements

As this thesis marks the end of my academic career, I would like to take this opportunity to thank everybody who supported me on this long journey. Thank you to dr. Gonenc for his continuous support throughout the whole program and especially in the course of writing this thesis. You were always supportive and available for questions even on the week-ends, thank you for that!

Also thank you to all the other teachers in my program, you all broadened my horizon and thought me many interesting and useful things!

I also want to thank all my friends here in Groningen and Uppsala who made the last 18 months an amazing experience. Thank you for all the nice memories!

Thank you especially to my girlfriend who supported me throughout the program and was always there for me especially in the last stressful weeks!

Zum Schluß möchte ich noch den allerwichtigsten Leuten danken: Mama, Papa, Anne und Max. Seitdem ich Essweiler vor ein paar Jahren zum Studium verlassen habe, weiß ich umso mehr wie wichtig ein gutes Zuhause ist und wie sich echtes Heimweh anfühlt. Vielen Dank für alles!

References

- Acquier, A., & Aggeri, F. (2007). The development of a CSR industry: Legitimacy and feasibility as the two pillars of the institutionalization process (No. hal-01117319). In Den Hond, F., De Bakker, F.G.A. & Neergaard, P., ed. *Managing corporate social responsibility in action: talking, doing and measuring*. Farnham: Ashgate, 149-165.
- Aguilera, R. V., Rupp, D. E., Williams, C. A., & Ganapathi, J. (2007). Putting the S back in corporate social responsibility: A multilevel theory of social change in organizations. *Academy of management review*, 32(3), 836-863.
- Aguinis, H., & Glavas, A. (2013). Embedded versus peripheral corporate social responsibility: Psychological foundations. *Industrial and Organizational Psychology*, 6(4), 314-332.
- Akerlof, G. (1970). The market for lemons: qualitative uncertainty and market mechanism. *Quarterly Journal of Economics*, 89.
- Baden, D., & Harwood, I. A. (2013). Terminology matters: A critical exploration of corporate social responsibility terms. *Journal of Business Ethics*, 116(3), 615-627.
- Balabanis, G., Phillips, H. C., & Lyall, J. (1998). Corporate social responsibility and economic performance in the top British companies: are they linked?. *European Business Review*, 98(1), 25-44.
- Bandsuch, M., Pate, L., & Thies, J. (2008). Rebuilding Stakeholder Trust in Business: An Examination of Principle-Centered Leadership and Organizational Transparency in Corporate Governance. *Business and Society Review*, 113(1), 99-127.
- Banerjee, S. B., & Bonnefous, A. M. (2011). Stakeholder management and sustainability strategies in the French nuclear industry. *Business strategy and the environment*, 20(2), 124-140.
- Barnea, A., & Rubin, A. (2010). Corporate social responsibility as a conflict between shareholders. *Journal of business ethics*, 97(1), 71-86.
- Baron, D. P., Agus Harjoto, M., & Jo, H. (2011). The economics and politics of corporate social performance. *Business and Politics*, 13(2).

Master Thesis - **Christian Flachsland** - *International Financial Management*

Baumol, W. J., & Blackman, S. A. B. (1991). *Perfect Markets and Easy Virtue Business Ethics and the Invisible Hand*. Basil Blackwell, Oxford.

Berman, S. (1998). *Managerial opportunism and firm performance: An empirical test of instrumental stakeholder theory* (Doctoral dissertation, University of Washington).

Bénabou, R., & Tirole, J. (2010). Individual and corporate social responsibility. *Economica*, 77(305), 1-19.

Bhattacharya, C. B., Sen, S., & Korschun, D. (2008). Using corporate social responsibility to win the war for talent. *MIT Sloan management review*, 49(2).

Boutin-Dufresne, F., & Savaria, P. (2004). Corporate social responsibility and financial risk. *The Journal of investing*, 13(1), 57-66.

Bowen, H. R. (1953). *Social responsibility of the businessman*. New York: Harper and Row.

Brammer, S., & Millington, A. (2008). Does it pay to be different? An analysis of the relationship between corporate social and financial performance. *Strategic Management Journal*, 29(12), 1325-1343.

Byrne, E. F. (2010). The US military-industrial complex is circumstantially unethical. *Journal of Business Ethics*, 95(2), 153-165.

Cai, Y., Jo, H., & Pan, C. (2011). Doing well while doing bad? CSR in controversial industry sectors. *Journal of Business Ethics*, 108(4), 467-480.

Carroll, A. B. (1979). A three-dimensional conceptual model of corporate performance. *Academy of management review*, 4(4), 497-505.

Carroll, A. B. (1991). The pyramid of corporate social responsibility: Toward the moral management of organizational stakeholders. *Business horizons*, 34(4), 39-48.

Cespa, G., & Cestone, G. (2007). Corporate social responsibility and managerial entrenchment. *Journal of Economics & Management Strategy*, 16(3), 741-771.

Cheng, B., Ioannou, I., & Serafeim, G. (2011). Corporate social responsibility and access to finance. *Strategic Management Journal*, 35(1), 1-23.

Cheng, B., Ioannou, I., & Serafeim, G. (2014). Corporate social responsibility and access to finance. *Strategic Management Journal*, 35(1), 1-23.

Claessens, S., & Fan, J. P. (2002). Corporate governance in Asia: A survey. *International Review of finance*, 3(2), 71-103.

Clarkson, M. E. (1995). A stakeholder framework for analyzing and evaluating corporate social performance. *Academy of management review*, 20(1), 92-117.

Coase, R. H. (1937). The nature of the firm. *economica*, 4(16), 386-405.

Cottrill, M. T. (1990). Corporate social responsibility and the marketplace. *Journal of Business Ethics*, 9(9), 723-729.

Cowen, S. S., Ferreri, L. B., & Parker, L. D. (1987). The impact of corporate characteristics on social responsibility disclosure: A typology and frequency-based analysis. *Accounting, Organizations and society*, 12(2), 111-122.

Davis, K. (1960). Can business afford to ignore social responsibilities?. *California management review*, 2(3), 70-76.

Demirgüç-Kunt, A., & Levine, R. (1996). Stock market development and financial intermediaries: stylized facts. *The World Bank Economic Review*, 10(2), 291-321.

Dillenburg, S., Greene, T., & Erikson, O. H. (2003). Approaching socially responsible investment with a comprehensive ratings scheme: Total social impact. *Journal of Business Ethics*, 43(3), 167-177.

Driscoll, C., & Starik, M. (2004). The primordial stakeholder: Advancing the conceptual consideration of stakeholder status for the natural environment. *Journal of Business Ethics*, 49(1), 55-73.

Donaldson, T. (1982). *Corporations and morality* (pp. 36-58). Englewood Cliffs, NJ: Prentice-Hall.

Donaldson, T., & Dunfee, T. W. (1999). *Ties that bind: A social contracts approach to business ethics*. Boston: Harvard Business School Press.

Master Thesis - **Christian Flachsland** - *International Financial Management*

Eldar, O. (2014). The role of social enterprise and hybrid organizations. *Yale Law & Economics Research Paper*, (485).

El Ghoul, S., Guedhami, O., & Kim, Y. (2010). Country-level institutions, firm value, and the role of corporate social responsibility initiatives. *Journal of International Business Studies* (in press).

El Ghoul, S., Guedhami, O., Kwok, C. C., & Mishra, D. R. (2011). Does corporate social responsibility affect the cost of capital?. *Journal of Banking & Finance*, 35(9), 2388-2406.

El Ghoul, S., Guedhami, O., & Kim, Y. (2016). Country-level institutions, firm value, and the role of corporate social responsibility initiatives. *Journal of International Business Studies* (in press).

Fabrizi, M., Mallin, C., & Michelon, G. (2014). The role of CEO's personal incentives in driving corporate social responsibility. *Journal of Business Ethics*, 124(2), 311-326.

Fama, E. F., & French, K. R. (1997). Industry costs of equity. *Journal of financial economics*, 43(2), 153-193.

Fauver, L., Houston, J., & Naranjo, A. (2003). Capital market development, international integration, legal systems, and the value of corporate diversification: A cross-country analysis. *Journal of Financial and Quantitative Analysis*, 38(01), 135-158.

Feng, Z. Y., Wang, M. L., & Huang, H. W. (2015). Equity Financing and Social Responsibility: Further International Evidence. *The International Journal of Accounting*, 50(3), 247-280.

Frederick, W. C. (1960). The growing concern over business responsibility. *California Management Review*, 2(4), 54-61.

Freeman, R. E. (1984). *Stakeholder management: framework and philosophy*. Pitman: Mansfield, MA.

Friedman, M. (1962). *Capitalism and freedom: With the assistance of Rose D. Friedman*. University of Chicago Press: Chicago, IL.

Friedman, M. (1970). The social responsibility of business is to increase its profits. *New York Times Magazine*, 13(9), 122-124.

Master Thesis - **Christian Flachsland** - *International Financial Management*

Frynas, J. G. (2005). The false developmental promise of corporate social responsibility: Evidence from multinational oil companies. *International affairs*, 81(3), 581-598.

Foss, K., & Foss, N. J. (2005). Resources and transaction costs: how property rights economics furthers the resource-based view. *Strategic Management Journal*, 26(6), 541-553.

Gârleanu, N., & Pedersen, L. H. (2013). Dynamic trading with predictable returns and transaction costs. *The Journal of Finance*, 68(6), 2309-2340.

Griffin, J. J., & Mahon, J. F. (1997). The corporate social performance and corporate financial performance debate twenty-five years of incomparable research. *Business & Society*, 36(1), 5-31.

Griffin, J. J., & Vivari, B. (2009). United States of America: Internal Commitments and External Pressures. In *Global Practices of Corporate Social Responsibility* (pp. 235-250). Springer Berlin Heidelberg.

Griffin, J. J., & Prakash, A. (2014). Corporate responsibility initiatives and mechanisms. *Business & Society*, 53(4), 465-482.

Godfrey, P. C. (2005). The relationship between corporate philanthropy and shareholder wealth: A risk management perspective. *Academy of management review*, 30(4), 777-798.

Godfrey, P. C., Merrill, C. B., & Hansen, J. M. (2009). The relationship between corporate social responsibility and shareholder value: An empirical test of the risk management hypothesis. *Strategic Management Journal*, 30(4), 425-445.

Goel, A. M., & Thakor, A. V. (2008). Overconfidence, CEO selection, and corporate governance. *The Journal of Finance*, 63(6), 2737-2784.

Gonenc, H., & Scholtens, B. (2017). Environmental and Financial Performance of Fossil Fuel Firms: A Closer Inspection of their Interaction. *Ecological Economics*, 132, 307-328.

Goyal, P., Rahman, Z., & Kazmi, A. A. (2013). Corporate sustainability performance and firm performance research: literature review and future research agenda. *Management Decision*, 51(2), 361-379.

Henderson, D. (2001). The case against 'corporate social responsibility'. *Policy: A Journal of Public Policy and Ideas*, 17(2), 28.

Master Thesis - **Christian Flachsland** - *International Financial Management*

Hill, C. W. (1990). Cooperation, opportunism, and the invisible hand: Implications for transaction cost theory. *Academy of Management Review*, 15(3), 500-513.

Hill, J. (2001). Thinking about a more sustainable business—an Indicators approach. *Corporate Environmental Strategy*, 8(1), 30-38.

Hong, H., & Kacperczyk, M. (2009). The price of sin: The effects of social norms on markets. *Journal of Financial Economics*, 93(1), 15-36.

Hutchcroft, P. D., & Rocamora, J. (2003). Strong demands and weak institutions: The origins and evolution of the democratic deficit in the Philippines. *Journal of East Asian Studies*, 3(2), 259-292.

Japhet, K., Tawiah, V. K., & Benjamin, M. (2015). Debate on Mandatory Corporate Social Responsibility. *Available at SSRN 2592880*.

Jenkins, R. (2005). Globalization, corporate social responsibility and poverty. *International affairs*, 81(3), 525-540.

Jenkins, H., & Yakovleva, N. (2006). Corporate social responsibility in the mining industry: Exploring trends in social and environmental disclosure. *Journal of cleaner production*, 14(3), 271-284.

Jensen, M. C., & Meckling, W. H. (1976). Theory of the firm: Managerial behavior, agency costs and ownership structure. *Journal of financial economics*, 3(4), 305-360.

Jensen, M. C. (2002). Value maximization, stakeholder theory, and the corporate objective function. *Business ethics quarterly*, 12(02), 235-256.

Jo, H., & Harjoto, M. A. (2011). Corporate governance and firm value: The impact of corporate social responsibility. *Journal of business ethics*, 103(3), 351-383.

Jo, H., & Na, H. (2012). Does CSR reduce firm risk? Evidence from controversial industry sectors. *Journal of Business Ethics*, 110(4), 441-456.

Klapper, L. F., & Love, I. (2004). Corporate governance, investor protection, and performance in emerging markets. *Journal of corporate Finance*, 10(5), 703-728.

Master Thesis - **Christian Flachsland** - *International Financial Management*

Karna, A., Täube, F., & Sonderegger, P. (2013). Evolution of innovation networks across geographical and organizational boundaries: A study of R&D subsidiaries in the Bangalore IT cluster. *European Management Review*, 10(4), 211-226.

Kashmiri, S., Nicol, C. D., & Hsu, L. (2016). Birds of a feather: intra-industry spillover of the Target customer data breach and the shielding role of IT, marketing, and CSR. *Journal of the Academy of Marketing Science*, 1-21.

Khanna, T., & Palepu, K. (1997). Why focused strategies may be wrong for emerging markets. *Harvard business review*, 75(4), 41-48.

Kim, Y., Park, M. S., & Wier, B. (2012). Is earnings quality associated with corporate social responsibility?. *The Accounting Review*, 87(3), 761-796.

Kuppuswamy, V., Serafeim, G., & Villalonga, B. (2014). The effect of institutional factors on the value of corporate diversification. *Finance and strategy: Advances in Strategic Management*, 31, 37-68.

Kytle, B., & Singh, P. Social Responsibility Initiative Working (2005). Cambridge, MA: John F. Kennedy School of Government, Harvard University. Retrieved 2008-03-07.

La Porta, R., & Lopez-de-Silanes, F. (1998). Capital markets and legal institutions. *Beyond the Washington consensus: Institutions matter*, 73-92.

La Porta, R., Lopez-de-Silanes, F., Shleifer, A., & Vishny, R. (1999). The quality of government. *Journal of Law, Economics, and organization*, 15(1), 222-279.

Lee, D. D., & Faff, R. W. (2009). Corporate sustainability performance and idiosyncratic risk: A global perspective. *Financial Review*, 44(2), 213-237.

Lev, B., Petrovits, C., & Radhakrishnan, S. (2010). Is doing good good for you? How corporate charitable contributions enhance revenue growth. *Strategic Management Journal*, 31(2), 182-200.

Lindgreen, A., Maon, F., Reast, J., & Yani-De-Soriano, M. (2012). Guest editorial: Corporate social responsibility in controversial industry sectors. *Journal of business ethics*, 1-3.

Love, I. (2003). Financial development and financing constraints: International evidence from the structural investment model. *Review of Financial studies*, 16(3), 765-791.

Luo, X., Wang, H., Raithel, S., & Zheng, Q. (2015). Corporate social performance, analyst stock recommendations, and firm future returns. *Strategic Management Journal*, 36(1), 123-136.

Luo, X., & Bhattacharya, C. B. (2006). Corporate social responsibility, customer satisfaction, and market value. *Journal of marketing*, 70(4), 1-18.

Malmendier, U., & Tate, G. (2005). CEO overconfidence and corporate investment. *The journal of finance*, 60(6), 2661-2700.

Maloni, M. J., & Brown, M. E. (2006). Corporate social responsibility in the supply chain: an application in the food industry. *Journal of business ethics*, 68(1), 35-52.

Margolis, J. D., & Walsh, J. P. (2003). Misery loves companies: Rethinking social initiatives by business. *Administrative science quarterly*, 48(2), 268-305.

Martínez-Ferrero, J., Banerjee, S., & García-Sánchez, I. M. (2016). Corporate social responsibility as a strategic shield against costs of earnings management practices. *Journal of Business Ethics*, 133(2), 305-324.

McGee, R. W. (2008). The Role of Stakeholders in Corporate Governance. In *Corporate Governance in Transition Economies* (pp. 35-39). Springer US.

Meyer, K. E., Estrin, S., Bhaumik, S. K., & Peng, M. W. (2009). Institutions, resources, and entry strategies in emerging economies. *Strategic management journal*, 30(1), 61-80.

Mitchell, R. K., Agle, B. R., & Wood, D. J. (1997). Toward a theory of stakeholder identification and salience: Defining the principle of who and what really counts. *Academy of management review*, 22(4), 853-886.

Modigliani, F., & Miller, M. H. (1958). The cost of capital, corporation finance and the theory of investment. *The American economic review*, 48(3), 261-297.

Moore, G. (2001). Corporate social and financial performance: An investigation in the UK supermarket industry. *Journal of Business ethics*, 34(3-4), 299-315.

Nelling, E., & Webb, E. (2009). Corporate social responsibility and financial performance: the “virtuous circle” revisited. *Review of Quantitative Finance and Accounting*, 32(2), 197-209.

Oikonomou, I., Brooks, C., & Pavelin, S. (2012). The impact of corporate social performance on financial risk and utility: A longitudinal analysis. *Financial Management*, 41(2), 483-515.

Orlitzky, M., Schmidt, F. L., & Rynes, S. L. (2003). Corporate social and financial performance: A meta-analysis. *Organization studies*, 24(3), 403-441.

Orts, E. W., & Strudler, A. (2002). The ethical and environmental limits of stakeholder theory. *Business Ethics Quarterly*, 12(02), 215-233.

Oxley, J. E. (1999). Institutional environment and the mechanisms of governance: the impact of intellectual property protection on the structure of inter-firm alliances. *Journal of Economic Behavior & Organization*, 38(3), 283-309.

Palazzo, G., & Richter, U. (2005). CSR business as usual? The case of the tobacco industry. *Journal of Business Ethics*, 61(4), 387-401.

Paluszek, J. (2005, April). Ethics and brand value: Strategic differentiation. In *PowerPoint Presentation, Business and Organizational Ethics Partnership Meeting. Markkula Centre for Applied Ethics, Santa Clara University, April 6* (Vol. 7).

Patton, M. Q. (1989). A context and boundaries for a theory-driven approach to validity. *Evaluation and Program Planning*, 12(4), 375-377.

Phillips, R. A. (2004). Some key questions about stakeholder theory. *Ivey Business Journal*.

Polonsky, M., & Jevons, C. (2009). Global branding and strategic CSR: an overview of three types of complexity. *International Marketing Review*, 26(3), 327-347.

Porter, M. E. (2011). *Competitive advantage of nations: creating and sustaining superior performance*. Simon and Schuster.

Porter, M., & Kramer, M. R. (2006). The link between competitive advantage and corporate social responsibility. *Harvard business review*, 84(12), 42-56.

Porter, M., & Kramer, M. R. (2011). Creating shared value. *Harvard business review*, 89(1/2), 62-77.

Preston, L. E., & Sapienza, H. J. (1990). Stakeholder management and corporate performance. *Journal of Behavioral Economics*, 19(4), 361-375.

Rasche, A., & Esser, D. E. (2006). From stakeholder management to stakeholder accountability. *Journal of business ethics*, 65(3), 251-267.

Ricart, J. E., Enright, M. J., Ghemawat, P., Hart, S. L., & Khanna, T. (2004). New frontiers in international strategy. *Journal of International Business Studies*, 35(3), 175-200.

Rodrigo, P., Duran, I. J., & Arenas, D. (2016). Does it really pay to be good, everywhere? A first step to understand the corporate social and financial performance link in Latin American controversial industries. *Business Ethics: A European Review*, 25(3), 286-309.

Rodriguez-Granillo, G. A., Mc Fadden, E. P., Valgimigli, M., van Mieghem, C. A., Regar, E., de Feyter, P. J., & Serruys, P. W. (2006). Coronary plaque composition of nonculprit lesions, assessed by in vivo intracoronary ultrasound radio frequency data analysis, is related to clinical presentation. *American heart journal*, 151(5), 1020-1024.

Ruf, B. M., Muralidhar, K., Brown, R. M., Janney, J. J., & Paul, K. (2001). An empirical investigation of the relationship between change in corporate social performance and financial performance: A stakeholder theory perspective. *Journal of Business ethics*, 32(2), 143-156.

Servaes, H., & Tamayo, A. (2013). The impact of corporate social responsibility on firm value: The role of customer awareness. *Management Science*, 59(5), 1045-1061.

Simpson, W. G., & Kohers, T. (2002). The link between corporate social and financial performance: Evidence from the banking industry. *Journal of business ethics*, 35(2), 97-109.

Sturdivant, F. D., & Ginter, J. L. (1977). Corporate social responsiveness: Management attitudes and economic performance. *California Management Review*, 19(3), 30-39.

Svenfelt, Å., Engström, R., & Svane, Ö. (2011). Decreasing energy use in buildings by 50% by 2050—A backcasting study using stakeholder groups. *Technological Forecasting and Social Change*, 78(5), 785-796.

Sweeney, L., & Coughlan, J. (2008). Do different industries report corporate social responsibility differently? An investigation through the lens of stakeholder theory. *Journal of Marketing Communications*, 14(2), 113-124.

Tencati, A., Perrini, F., & Pogutz, S. (2004). New tools to foster corporate socially responsible behavior. *Journal of Business Ethics*, 53(1-2), 173-190.

Van Beurden, P., & Gössling, T. (2008). The worth of values—a literature review on the relation between corporate social and financial performance. *Journal of business ethics*, 82(2), 407-424.

Van der Steen, M. (2015). Corp. Social Responsibility as global innovation. *International Management Accounting and Control lecture slides*. University of Groningen.

van Offenbeek, M. A., & Vos, J. F. (2016). An integrative framework for managing project issues across stakeholder groups. *International Journal of Project Management*, 34(1), 44-57.

Waddock, S. A., & Graves, S. B. (1997). Finding the link between stakeholder relations and quality of management. *The Journal of Investing*, 6(4), 20-24.

Wernerfelt, B. (1984). A resource-based view of the firm. *Strategic management journal*, 5(2), 171-180.

Williamson Oliver E. (1985). The Economic Institutions of Capitalism Firms Markets Relational Contracting.

Williamson, O. E. (1989). Transaction cost economics. *Handbook of industrial organization*, 1, 135-182.

Wilson, A., & West, C. (1981). The marketing of unmentionables. *Harvard Business Review*, 59(1), 91.

Wood, D. J. (1991). Corporate social performance revisited. *Academy of management review*, 16(4), 691-718.

Woolcock, M. (2001). The place of social capital in understanding social and economic outcomes. *Canadian journal of policy research*, 2(1), 11-17.

World Bank. (2015). *World Development Report 2015: Mind, Society, and Behavior*. Washington, DC: World Bank.

Yoon, Y., Gürhan-Canli, Z., & Schwarz, N. (2006). The effect of corporate social responsibility (CSR) activities on companies with bad reputations. *Journal of consumer psychology*, 16(4), 377-390.

Appendix A: Robustness Test using Industry-adjusted Tobin's Q

Table AA: Regression results Model (1)-(7)

This table shows the results of an OLS regression of the proposed models. Industry-adjusted Tobin's Q is used as a dependent variable in all the models. Model (1) tests the overall effect of CSR on Tobin's Q in isolation. Models (2)-(4) test the respective moderating effect of the country-level variables in isolation, and Model (5) tests the joint effects of these country-level variables. Model (6) tests the moderating effect of the industry-level dummy for controversial industries. Model (7) combines all previous models and tests the joint effects of all the mentioned cross-country or cross-industry level variables and the moderating effects on the CSR value relationship. Moderating effects are tested by the inclusion of an interaction term (CSR*country/industry-level variable) in the respective models. The detailed measurement procedures of all variables are outlined in chapter 3. The inclusion of year-fixed effects and industry-fixed effects is indicated for the individual models.

Note: Statistical significance at a 10%, 5% and 1% level is indicated by the display of *, ** or ***. Standard errors are reported in brackets beneath the coefficients.

	Model (1)	Model (2)	Model (3)	Model (4)	Model (5)	Model (6)	Model (7)
CSR	0.016*** [0.004]	0.018*** [0.006]	0.018*** [0.005]	0.090*** [0.010]	0.086*** [0.012]	0.016*** [0.004]	0.073*** [0.012]
SIZE	-0.655*** [0.031]	-0.644*** [0.029]	-0.669*** [0.031]	-0.225*** [0.045]	-0.268*** [0.047]	-0.654*** [0.030]	-0.237*** [0.045]
ROA	8.536*** [0.535]	8.996*** [0.557]	9.354*** [0.578]	8.757*** [0.517]	9.186*** [0.538]	9.197*** [0.554]	9.949*** [0.560]
Leverage	-2.004*** [0.308]	-1.761*** [0.314]	-1.582*** [0.295]	-1.767*** [0.298]	-1.552*** [0.304]	-1.478*** [0.291]	-1.023*** [0.286]
R&D	21.703*** [1.311]	23.072*** [1.363]	21.979*** [1.197]	19.882*** [1.284]	21.620*** [1.337]	20.834*** [1.170]	20.839*** [1.164]
Sales Growth	0.393*** [0.083]	0.398*** [0.086]	0.404*** [0.086]	0.363*** [0.081]	0.379*** [0.083]	0.394*** [0.084]	0.368*** [0.084]
CapEx	2.355*** [0.729]	2.079*** [0.742]	2.505*** [0.656]	1.903** [0.742]	1.659** [0.763]	2.320*** [0.661]	1.246* [0.660]
ln GDP/capita	0.006 [0.090]	-0.110* [0.061]	0.026 [0.096]	0.029 [0.089]	-0.091 [0.059]	0.047 [0.094]	-0.055 [0.061]
MSI		0.010 [0.497]			-1.054 [0.973]		-0.435 [0.994]
MSI*CSR		-0.004 [0.010]			0.019 [0.019]		0.007 [0.019]
CAPMQ			0.880* [0.474]		1.194 [0.900]		0.723 [0.909]
CAPMQ*CSR			-0.023* [0.009]		-0.026 [0.017]		-0.017 [0.018]
CGS				1.135*** [0.305]	1.317*** [0.310]		1.825*** [0.310]
CGS*CSR				-0.064*** [0.007]	-0.061*** [0.008]		-0.075*** [0.007]
CONTROV.						-1.513*** [0.233]	-1.588*** [0.231]
CONTROV.*CSR						0.039*** [0.004]	0.042*** [0.004]
Constant	7.108*** [1.238]	8.244*** [1.110]	7.370*** [1.280]	-0.827 [1.365]	1.142 [1.260]	8.382*** [1.256]	0.967 [1.033]
Adj. R-squared	0.139	0.137	0.133	0.141	0.138	0.136	0.137
Observations	22034	20614	20614	22034	20614	22034	20614
Year	Yes						
Industry	Yes	Yes	Yes	Yes	No	No	No

Appendix B: Robustness Test using Industry-adjusted Tobin's Q

Table AB: Regression results Model (8)

This table shows the results of a two-stage regression of model 8. The dependent variable in the firm value equation (8a) is industry-adjusted Tobin's Q. The dependent variable in the CSR equation (8b) is the constructed measure of CSR performance in chapter 3. The instrumental variables used in model 8a include leverage and the return on assets. Model 8b uses the average CSR performance scores by country/year and by country/industry. The inclusion of year-fixed effects is indicated for the individual models. The sample includes 22,034 observations in a period from 2006-2014.

*Note: Statistical significance at a 10%, 5% and 1% level is indicated by the display of *, ** or ***. Standard errors are reported in brackets beneath the coefficients.*

	Model (8a)	Model (8b)
CSR	0.063*** [0.011]	
TBQ		0.069 [0.571]
LEV	-4.830*** [0.575]	
ROA	10.197*** [0.256]	
Country/Year CSR		0.657*** [0.025]
Country/Industry CSR		0.413* [0.226]
R&D	23.922*** [0.788]	-0.014 [0.216]
CapEx	3.826*** [0.503]	-0.010 [0.182]
SIZE	-0.777*** [0.023]	-0.003* [0.053]
Sales Growth	0.396*** [0.051]	0.205 [0.210]
GDP/capita	-0.003 [0.002]	0.000 [0.000]
MSI	0.006 [0.020]	0.016 [0.017]
CAPMQ	1.158 [0.988]	-0.167 [1.902]
CGS	1.462** [0.742]	-0.005* [0.003]
CONTROV.	-0.131*** [0.001]	0.245* [0.132]
Adj. R-squared		-0.082
Observations	22034	22034
Year	Yes	Yes

Appendix C: Correlation-Matrix

Table AC: Correlation-Matrix

The following table presents the correlation matrix for dependent and independent variables. The final dataset consists of 22,034 firm-year observations from 3,770 firms over the sample period 2006-2014. All variables are winsorized at a 0.01 and 0.99 level to control for data outliers. A 1% significance level is reported as *.

	TBQ	CSR	SIZE	ROA	LEV	CAPEX	SG	RD	GDP	MSI	CAPMQ	CGS	CONTROV
TBQ	1												
CSR	-0.1167*	1											
SIZE	-0.0381*	0.3109*	1										
ROA	0.0038*	-0.0966*	0.0412*	1									
LEV	0.0565*	0.0694*	0.0268*	-0.5841*	1								
CAPEX	-0.0019	-0.0148	-0.0336*	-0.3107*	0.0126	1							
SG	0.0006	-0.0097	-0.0222*	0.0003	-0.0008	0.0011	1						
RD	0.0565*	-0.1871*	-0.1394*	-0.0108*	-0.0159*	-0.0019*	-0.0005*	1					
GDP	0.0180*	-0.0577*	-0.0010	-0.0044	-0.0015	0.0009	0.0033	0.0794*	1				
MSI	0.0019	0.0084	-0.0148*	-0.0018	-0.0016	0.0003	0.0030	-0.0117	0.0156*	1			
CAPMQ	-0.0135	0.0099	0.0426	0.0048	-0.0054	-0.0047	-0.0023	-0.0208*	0.0095	0.6869*	1		
CGS	-0.0306*	0.2794*	0.0997*	0.0327*	0.0357*	-0.0256*	-0.0281*	-0.1785*	0.0058*	0.0130*	0.0617*	1	
CONTROV	0.0217*	0.4063*	0.0582*	-0.0022	0.0218*	0.0113	0.0010	0.0532*	-0.0288*	0.0061	0.0022	0.0003	1

According to Belsey et al. (2005), the critical level of correlation is 0.7. Even though the correlation of MSI and CAPMQ comes close to this number, it doesn't exceed this critical spectrum. The premise of multicollinearity can therefore be neglected.