

SESSION 3: ESG, CSR AND SUSTAINABILITY

DOES IT MAKE A DIFFERENCE WHEN INTERNALIZED? EXPLORING DIFFERENT CSR APPROACHES PREDICTING FIRM COMPETITIVENESS

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Abstract

Drawing upon signaling and organizational commitment theories, this study clusters unobtrusive corporate social responsibility (CSR) behaviors from the commitment and compliance dimensions to different CSR approaches, and examine how these approaches predict firm competitiveness using secondary data from Chinese public companies. It contributes to the CSR literature by providing empirical evidence that internalized CSR contributes to increasing firm competitiveness. It also contributes to the literature on firm competitiveness by identifying three aspects of core competence — financial, technological and dynamic capabilities — and their corresponding correlations with firm competitiveness, thus integrating both the resource-based view (RBV) and the dynamic capability perspective. The negative correlation discovered between dynamic capability and firm competitiveness challenges the views of the literature and indicates the existence of additional facets and potential boundaries of dynamic capability in the context of strongly collective cultures, such as China.

1. INTRODUCTION

Yvon Chouinard, the founder of outdoor apparel maker Patagonia chose to transfer the ownership of his \$3 billion company, and its profits of \$100 million per year, to a non-profit organization rather than selling it or listing it publicly. Mr. Chouinard considered the earth to be “our only shareholder”, and instead of extracting value from nature and transforming it into wealth for investors, he determined that the wealth created by Patagonia would be used to protect the earth, the source of all wealth. His actions open a new chapter for corporate social responsibility (CSR) and issue a call for truly internalized CSR, instead of mere rhetoric about making the world a better place.

However, key questions do arise: How should CSR activities be internalized? Why do firms need to internalize them? How can one determine if a firm is internalizing CSR? Will internalized CSR make any difference in terms of driving firm competitiveness? Drawing from tenets of signaling theory and organizational commitment theory in behavior science, the study uses unobtrusive measures to cluster different CSR approaches from the CSR compliance and commitment dimensions and examine how the various approaches predict firms’ competitiveness differently.

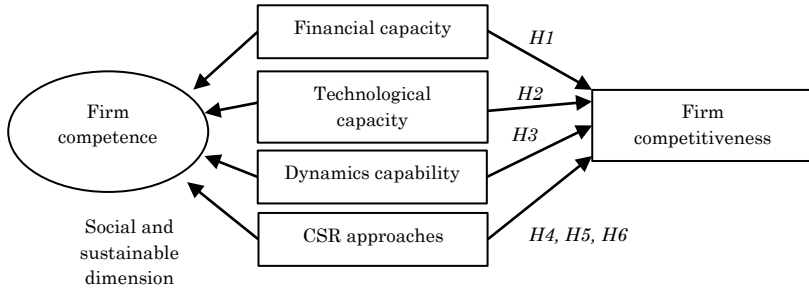
2. OVERALL FRAMEWORK AND HYPOTHESES

Integrating both the resource-based view (RBV) (Barney, 1991) and dynamic capability theory, three core aspects of core competence are identified, namely financial capacity (Li et al., 2020), technological capacity (McDonald & Eisenhardt, 2020) and dynamic capability (Mousavi et al., 2018, 2019). CSR approaches, which add a social and sustainable dimension to firms’ competence, can also influence firms’ competitiveness. Hence, the research framework outlined in Figure 1 is proposed below and the first three of six hypotheses are put forward.

H1: Financial capacity is positively related to firm competitiveness.

H2: Technological capacity is positively related to firm competitiveness.

H3: Dynamics capability is positively related to firm competitiveness.

Figure 1. Main research framework

Drawing from signaling theory (Connelly et al., 2011; Spence, 2002) and commitment theory (Meyer & Allen, 1984, 1997), CSR behaviors, such as the adoption of the Global Reporting Initiative (GRI) guidelines, the employment of Big 4 auditors and CSR violations and penalties, operate as different types of signals sent by firms. They are driven by the various immediate and strategic objectives of corporations, implying different levels of commitment to CSR activities. Adopting the GRI guidelines and hiring Big 4 is associated with strong CSR commitments while a CSR penalty in response to a violation clearly signals the effectiveness of CSR enforcement and the compliance level. The interaction of commitment and compliance dimensions categorizes CSR approaches into 4 types as shown in Figure 2 below.

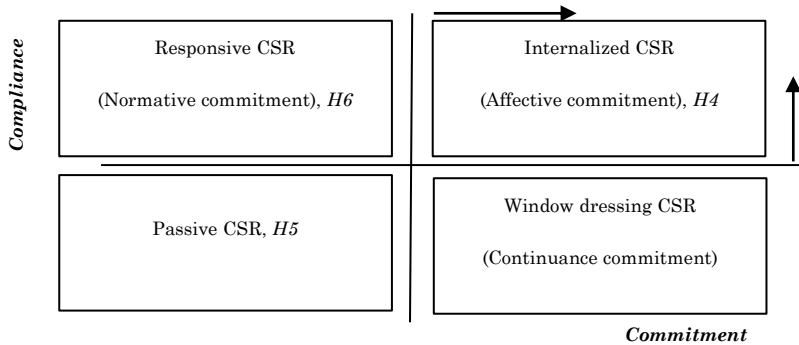
An internalized CSR approach arises from affective commitments when corporations believe in CSR and see real “value” in adopting CSR actions, hence contributing to firm competitiveness. “Continuance commitment” brings a “window-dressing” CSR approach as a “corrective plan” when a CSR violation is witnessed, which imposes extra costs on the firm and attempts to disguise its opportunistic behavior. Consequently, the competitiveness of such firms is unlikely to be perceived in the same manner as that of corporations adopting an internalized CSR approach. Another category of firms is those who choose CSR activities out of normative commitments, that is, because they feel they ought to, in a purely responsive rather than an active way. Hence, they will tend to do “just enough”, and it is very unlikely that this approach will have any significant positive impacts on a firm competitive advantage. Finally, a company that shows no commitment or compliance with CSR activities is what Moon et al. (2011) referred to as a “stupid” company (p. 54) adopting a passive CSR approach. In the long run, the competitiveness of such a firm would definitely be harmed. Given the four different approaches and their varying impacts on firm-level competitiveness, the next set of hypotheses is put forward:

H4: An internalized CSR approach maximizes firms’ competitiveness.

H5: A passive CSR approach is negatively related to firms’ competitiveness.

H6: A responsive CSR approach is unlikely to have significant positive effects on firms’ competitiveness.

Figure 2. Framework for CSR approaches



3. VARIABLES, DATA AND METHODOLOGY

Firm competitiveness. Market share is used as a direct measure of firm competitiveness.

Financial capacity. Financial capacity is measured by both the return on assets (ROA) and the asset turnover rate from resource generation capability and resource utilization efficiency dimensions.

Technological capacity. In this research, patent data are used to provide quantitative indicators of technological capacity (Tong et al., 2014). Also, the number of approved (and, therefore, high-quality) patents is used to indicate innovation quality (Tong et al., 2014).

Dynamic capability. In view that management team dynamics are a crucial indicator of a firm’s dynamic capability (Teece 2007, 2012) and teams that have more diverse in educational qualifications will be able to access to broader cognitive frames which contribute to the sensing stage of dynamic capabilities (Hambrick et al., 1996), the education dynamics of the management team is used to measure dynamics capability from both diversity of subjects (Dahlin et al., 2005; Hutzschenreuter & Horstkotte, 2013) and diversity of education levels dimensions. The Blau Index is adopted to calculate both educational diversity scores (field and level of education).

Control variables. The study includes a number of control variables for firm size (*LSIZE*), firm age (*AGE*), ownership type (*OWN*) and

industrial type (*INDUS*) in the model based on the theoretical and empirical research.

The analysis relies mainly on the following two data sources: 1) the Chinese Research Data Services (CNRDS); 2) the China Stock Market and Accounting Research database (<http://www.gtarsc.com>). To explore how different CSR approaches predict firm competitiveness differently, a four-step analytical process is followed:

Step 1: Apply principal factor analysis and k-means cluster analysis to cluster the CSR approaches.

Step 2: Construct independent variables through principal factor analysis again.

Step 3: Use a fixed effects linear regression (FEM) to test the overall modeling effect and the hypotheses.

Step 4: Conduct robustness tests.

4. RESULTS

The results of principal factor analysis employing four dummy variables *compliance1_Dummy* (violation status), *compliance2_Dummy* (penalty status), *Dis_GRI* (whether adopts GRI regulations), *Big 4* (whether employs Big 4 auditors) justifies k-mean clustering, and successfully clusters the firm-year observations into four different CSR approaches, namely passive CSR cases, responsive CSR cases, internalized CSR cases, and window-dressing CSR cases.

Principal factor analysis for dimension reduction using the six major variables *ROA*, *AT*, *Patents received*, *Patents applied*, *Education dynamics* and *Education level dynamics* indicates suitability for factor analysis and dimension reduction. Accordingly, the three variables of *financial capacity*, *technological capacity* and *dynamics capability* for the base model regression are generated.

The regression results support *H1*, *H2*, *H4*, *H5*, and *H6*. Dynamics capability is significant for market share, but with a negative correlation, which conflicts with *H3*. The robustness test is conducted by replacing the control variable *LSIZE* with *Total Asset* and *Total Revenue* respectively. Results indicate good robustness of the study.

5. DISCUSSIONS AND LIMITATION

This analysis successfully clusters CSR behaviors into different CSR approaches, draws tenets from behavioral science, boosts cross-disciplinary studies and contributes to the study of CSR by providing valuable empirical support for the importance of internalizing a CSR approach in shaping firms' competitiveness (Porter & Kramer, 2006, 2011). The research also contributes to the analysis of core competencies by identifying three dimensions — technological capacity, financial

capacity and dynamic capability — from the RBV and dynamic capability theory, and by determining their correlation with firm competitiveness. The negative correlation between dynamic capability and firm competitiveness in a Chinese organizational context implies that there are other facets and conditions of dynamic capabilities that are worthy of further examination.

Despite the contributions of this study, some limitations must be acknowledged. The mechanism by which CSR activities at the firm level are internalized requires further exploration. In addition, a fixed effects model is applied to focus on exploring impacts at the cluster level. In the future, a study using a dynamic model to explore the mechanism and longitudinal impacts at the firm level is essential. In addition, it would be interesting to investigate how changes in the CSR approach of one firm across different years influence its competitiveness. Finally, although the findings indicate that dynamic capability may have a negative impact on firm competitiveness, particularly in the Chinese context, a range of theoretical questions await clarification.

6. CONCLUSION

“To give is not to lose, to give is to win”. To give out of a genuine commitment and effort, based on an internalized CSR approach, allows firms to win the trust and support of stakeholders on behalf of our biggest stakeholder, “our planet”, with which the growth of the business is right at the door. It is likely that this is the strongest wisdom underlying Patagonia’s CSR approach.

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