From Values to Valuation –
Connecting Human Rights and Financial Performance

Discussion Paper
November 2016

EXECUTIVE SUMMARY

This Discussion Paper provides an overview of the objective of and process for a research initiative on connecting human rights and corporate financial performance (CFP) proposed by the Center for Responsible Business at UC Berkeley Haas School of Business, the Center for Law, Business, and the Economy at UC Berkeley School of Law; Alliance Manchester Business School – University of Manchester; and the UN-supported Principles for Responsible Investment.

The objective of this initiative is to produce a comprehensive, incisive, and credible academic study, in collaboration with key global partners, exploring financial risks and investment materiality related to human rights. The study will address the impact of corporate human rights policies and due diligence processes, as well as external human rights-related issues and events, on company valuations as well as on a range of quantitative and qualitative factors that could influence investment decisions and outcomes.

The study proposes to explore five broad research questions that investigate the relationship between human rights and CFP:

Q1: What is the nature of the link between human rights and CFP/valuation?

Q2: What are the salient and/or material human rights risks for companies across a range of different sectors?

Q3: By what process do analysts currently assess the materiality of human rights impacts on company performance.

Q4: What is the relationship between human rights allegations, serious incidents, litigation and stock performance/ public company's valuation?

Q5: What is the relationship between the existence and the quality of human rights policies and/or practices and factors such as legal risk, reputational risk, and access

to capital, that may influence CFP?

The study will draw on a mixed method three phase approach:

1. ***Comprehensive Literature Review***: Develop our conceptual understanding of the potential link between human rights and performance and use this understanding to form hypotheses, preselect proxies

2. ***Case Studies & Materiality Assessment****:* Investigate the salient and/or material human rights risks that are generic for all companies, and sector-specific

3. ***Econometric Modelling & Testing the Hypotheses***: Demonstrate empirically the relationship between human rights and CFP/valuation

With the required project funding, we envision the following timeline for this project:

- **Phase/Deliverable 1**: Present Discussion Paper for October 26, 2016 Berkeley convening

- **Phase/Deliverable 2**: Conduct an authoritative literature review/definitive research propositions/research methodology to be published in Spring or early Summer 2017

- **Phase/Deliverable 3**: Conduct a comprehensive study published by Summer 2018 for presentation at a UN-Supported PRI conference in September and the UN Forum on Business and Human Rights in November

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OBJECTIVE

Corporate responsibility for human rights is emerging as the key framework for aligning the interests of business and society. However, the material impact of human rights on corporate performance and valuation is still poorly understood. This seminal study will:

1. Provide corporations with a greater understanding of where salient and material human rights risks lie within their specific sector.
2. Provide examples of best practice for how to mitigate against those risks by understanding the impact of human rights policies and due diligence. This will provide useful information for investors, to direct their engagement with investee companies, and for companies themselves.
3. Help analysts understand the efficiency with which salient human rights risk is incorporated into market pricing and enable analysts to better integrate human rights risks to investment decision-making.

The study will provide insights with practice and policy implication for business, investors and policy setters. Working with industry leading ESG information providers; investment analysts and sector leading companies, we will investigate financial risks and investment materiality related to human rights. The study will address the impact of corporate human rights policies and due diligence processes, as well as external human rights-related issues and events, on company valuations as well as on a range of quantitative and qualitative factors that could influence investment decisions and outcomes. Specifically, we will identify and assess the materiality of these factors, while positing that the distinction between demonstrable and potential materiality may also be useful for investors and other stakeholders for whom such factors may be salient if not material. We will distinguish between different levels of impact, from core business model impacts that potentially impact on the long term profitability of the company, to the short term economic impact of one case. The study seeks to increase understanding of human rights risks among major asset owners and managers as well as socially responsible investors.[12] The examination of business impacts on human rights has largely focused on four sectors, (1) energy and extractives, (2) apparel and footwear, (3) information and communication technology, and (4) food, beverage and agriculture.[3] While the public and investors have increasingly asserted financial as well as legal, reputational and operational risks related to human rights in these sectors and some others, researchers have still yet to demonstrate and quantify the impact of human rights-related issues and risks on CFP and valuation—and in turn, reach conclusions regarding the materiality of human rights to investment decisions and outcomes.

This project will be the first to undertake a more systematic examination of these issues. Practitioners and researchers have established the *salience* of human rights risk for a number of industries – but have not engaged in in-depth empirical or qualitative analysis to establish *materiality*. In the business and human rights arena, there has been a move to introduce and define the concept of *salience* that is related to but distinct from materiality, a concept commonly understood in financial regulatory and investment valuation contexts.

For the purposes of this project, we will use a definition of salience provided by the UN Guiding Principles Reporting Framework, which defines salience as human rights issues that represent a prominent risk to the human rights of *persons* connected to a company.[4] Materiality in this context is different from salience. We will define it as human rights-related issues and risks that a reasonable investor would consider to possibly have a

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[1] Although see the Sustainability Accounting Standards Board's Materiality Map http://www.sasb.org/materiality/sasb-materiality-map/

[2] Mozaffar Khan, George Serafeim & Aaron Yoon Corporate Sustainability: First Evidence on Materiality, Harvard Business School Working Paper No. 15-073 (March 2015) available at http://hbswk.hbs.edu/item/corporate-sustainability-first-evidence-on-materiality

[3] Freeman, Bennett. "Investors and human rights: values, risk and materiality." *Business and Human Rights: From Principles to Practice.* Ed. Dorothée Baumann-Pauly and Justine Nolan. New York: Routledge, 2016. 235-238.

[4] See UN Guiding Principles Reporting Framework – Salient Human Rights Issues http://www.ungpreporting.org/key-concepts/salient-human-rights-issues/

"A company's salient human rights issues are those human rights that stand out because they are at risk of the most severe negative impact through the company's activities or business relationships. This concept of salience uses the lens of risk to people, not the business, as the starting point, while recognizing that where risks to people's human rights are greatest, there is strong convergence with risk to the business.

The emphasis of salience lies on those impacts that are:

- Most severe: based on how grave and how widespread the impact would be and how hard it would be to put right the resulting harm.
- Potential: meaning those impacts that have some likelihood of occurring in the future, recognizing that these are often, though not limited to, those impacts that have occurred in the past
- Negative: placing the focus on the avoidance of harm to human rights rather than unrelated initiatives to support or promote human rights;
- Impacts on human rights: placing the focus on risk to people, rather than on risk to the business."

measurable impact on corporate valuations and other generally accepted financial risk metrics. While the concept of salience is critical and generally accepted, we believe that testing financial and investment materiality will help push the issue of human rights risk further into the mainstream of investor considerations across companies and industries, portfolios and asset classes.

We propose to define materiality more specifically as encompassing a wide spectrum of quantitative and qualitative factors that companies, and in turn investors, face, including most fundamentally:

- Company valuations,
- Share price fluctuations,
- Cost of credit/debt,
- Sales/market share,
- Revenue projections and net income,
- Legal liability,
- Regulatory constraints,
- Disclosure requirements,
- Reputation/brand damage,
- And staff retention/recruitment.

One or more of these impacts may be demonstrable in relation to particular companies that will be examined through comparative analysis and case studies. There has also been an evolution of fiduciary responsibility standards from the US Department of Labor; the ERISA[5] standards were recently revised to reflect a position that ESG factors can and should be seen as consistent with fiduciary responsibility, providing legitimacy for this group's work.[6] Furthermore, financial regulation in the United Kingdom and South Africa lends validity to the materiality of ESG factors. These developments underscore the importance of examining the link, (if any) between materiality and human rights risk.

PRELIMINARY LITERATURE REVIEW

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[5] Rory Sullivan, Will Martindale, Elodie Feller and Anna Bordon, Fiduciary Duty in the 21st Century, 2015: https://www.unpri.org/download_report/6131

[6] See, e.g. Cynthia Williams and John M. Conley, *Is there an Emerging Fiduciary Duty to Consider University of Cincinnati Law Review*, Vol. 74, No. 1, 2005; "Knowing and Showing: Using U.S. Securities Laws to Compel Human Rights Disclosure (International Corporate Accountability Roundtable 2013) available at http://icar.ngo/analysis/launch-of-knowing-and-showing-using-u-s-securities-laws-to-compel-human-rights-disclosure/The Report, edited, reviewed and endorsed by Professor Cynthia A. Williams, argues that human rights are materially relevant to corporate securities reporting and encourages the U.S. Securities and Exchange Commission (SEC) to guide businesses in reporting material human rights information in their periodic and proxy disclosure reports.

There is a significant gap in the literature focusing on the links or correlations between human rights risk and materiality. There is research that focuses on how human rights impact foreign investment and on how corruption affects corporate performance and return. There appears to be no readily available data correlating human rights-related factors and valuation in particular. A literature search reveals anecdotal examples/case studies of how specific events (e.g. major human rights lawsuits against corporate defendants, or scandals involving labor rights or supply chains) appear to impact share price or profit and loss.[7] These episodic or case-specific examples of how a catastrophe or event impacts a company's financial situation, merely skims the surface in terms of looking at whether investing in human rights creates corporate value. They do demonstrate that *salient* human rights risks can and often do become *material* human rights risks over time.

Much of the existing academic literature focuses on human rights and investment returns as part of a large examination of ESG factors where human rights are one element, not the central focus of assessing corporate performance. As companies face growing expectations to embed human rights across their policy frameworks and due diligence processes, operations and supply chains, investors need to enhance their analytical and quantitative understanding of how corporate responses to human rights risk may impact both losses and gains.

Opportunities to quantify the relationship between human rights and CFP include evaluating losses (stock price, reputation, legal/regulatory action, boycott/divestment, operational risk) and gains (stock price, competitive advantage, consumer expectations and demand, supply chain resiliency, employee retention and satisfaction). We believe that it is critical to review and analyze data through both a sector and geographical lens as the financial impact of human rights risk may vary across industries and regions. Please see Appendix A for more detail on the preliminary literature review.

PROPOSED RESEARCH PROPOSITIONS AND METHODOLOGY

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[7] Human rights impact examples include, e.g., the divestment campaign against Talisman Oil related to its presence Talisman Oil's in Sudan; Royal Dutch Shell having production disruptions in the Niger Delta in the Nineties and again from 2005-10, Verizon losing a procurement contract inn Germany following revelations of NSA surveillance; Coca-Colaclosing bottling facilities in India and boycotts related to alleged complicity in human rights abuses in Colombia; Wal-Mart gender discrimination lawsuit involving 1.5M employees, Nestle & Hershey lawsuit about child slavery. Talisman appears to be a more straightforward example with divestment in Quebec, stock prices down, etc. The Shell example is harder to demonstrate: on the tangible side, Shell lost 20-25% of its production from the Delta from 2005 to 2010; yet at the same time human rights related factors are difficult to isolate among a wider range of poor governance, gross corruption, environmental degradation and entrenched poverty as well as community unrest and criminality which together formed the backdrop against which attacks on company facilities occurred.

The study proposes to explore five broad research questions that investigate the relationship between human rights and CFP:

Q1: What is the nature of the link between human rights and CFP/valuation?

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Q5: What is the relationship between the existence and the quality of human rights policies and/or practices and factors such as legal risk, reputational risk, and access to capital, that may influence CFP?

The study will draw on a mixed methods approach[8] in order to achieve three outcomes:

1. ***Comprehensive Literature Review***: Develop our conceptual understanding of the potential link between human rights and performance and use this understanding to form hypotheses, preselect proxies

2. ***Case Studies & Materiality Assessment****:* Investigate the salient and/or material human rights risks that are generic for all companies, and sector-specific

3. ***Econometric Modelling & Testing the Hypotheses***: Demonstrate empirically the relationship between human rights and CFP/valuation

These three objectives will form the basis for three key phases of the project. The central working hypothesis of the study is that some human rights-related issues and risks are demonstrably material in certain company and industry contexts, while many others are potentially material and should be seen as at least currently salient to investors.

Phase 1: Comprehensive Literature Review

A comprehensive literature review will be undertaken covering the finance and accounting literature on the impact of ESG and related issues on firms' CFP and valuation. An important initial step will be to identify and review recent attempts to identify material human rights issues (see for SASB's Materiality Map). The literature review will also cover the process by which analysts assess corporate risk. A key aspect of exploring this research question will be firstly, establishing a robust proxy for human rights performance

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[8] Jennifer Grafton, Anne M. Lillis, Habib Mahama, (2011) "Mixed methods research in accounting", Qualitative Research in Accounting & Management, Vol. 8 Iss: 1, pp.5 – 21.

and secondly, determining the interrelationship between human rights performance and other factors, like governance, on CFP. The literature review will also be specifically used to identify key factors that may influence corporate value that are of relevance to this study, including the process by which analysts establish corporate risk and price it into the market The literature review will also provide an initial understanding of the key issues and risks within different sectors. Depending on resources, this approach could be supplemented by a number of industry workshops and analyst interviews designed to create a deeper understanding of both company and investor perceptions of human rights risks and materiality. The following examples below clarify the aim of this first phase.

The literature would suggest, for example, that legislation and other forms of regulation affect materiality. For example, new EU directives that came into play in 2014 have substantially extended the breadth and depth of human rights provisions now available under EU public procurement rules. Also, in May 2015, the EU introduced mandatory certification for all EU importers sourcing from conflict zones. All importers of tin, tantalum, tungsten and gold for manufacturing consumer goods will, by law, need to be certified by the EU to ensure that they do not contribute to conflicts and human rights abuses, a move that will impact 880,000 firms in Europe. A final example is the United Kingdom (UK), Modern Slavery Act 2015, which requires commercial organizations that conduct all or part of their business in the UK, and supply goods or services with a turnover of £36m or more, to prepare and publish an annual “slavery and human trafficking” statement (UK, 2015). An understanding of the potential legislative developments will inform our choice of sectors and sample.

Secondly, there is evidence emerging in the literature of the significance of country location. Methven O’Brien & Dhanarajan (2016) comment for example,

> “More interesting, however, was that it also detected variation between surveyed countries in terms of the likelihood that companies have a human rights policy, suggesting that national factors, such as government encouragement of corporate social responsibility (CSR) or business ethics can influence company behavior, even in the absence of coercive legal rules. Given this, at least from the viewpoint of corporate “early adopters” of human rights policies, government measures to promote their development by other businesses ought to be welcome, as likely to help ‘level the playing field’ (DIHR, ICAR and GBI, 2014).”

We recognize that establishing the nature of the link between human rights policy, practice and performance will be particularly challenging. For example, it will be crucial to draw on the literature to establish notions of the *quality* of human rights policies and practice disclosures. More significantly, from our grasp of the literature, we recognize that access to policy and practice information from published sources will be challenging. Methven O'Brien & Dhanarajan (2016) study of current disclosure practices concludes, for example,

> "Two years after the UN HRC's endorsement of the GPs, in 2013, a non-randomized survey of 153 companies of all sizes and from 39 countries, undertaken by the UN Working Group on the issue of human rights and transnational corporations and other business enterprises, found fifty-eight per cent had a public statement on human rights (United Nations General Assembly (UNGA), 2013). Yet by 2016, the Business and Human Rights Resource Centre, which has begun to document published company policies on human rights, lists less than three-hundred and fifty, out of a population of 80,000 or so transnational firms worldwide, as noted earlier (Business and Human Rights Resource Centre 2016)."

In addition to establishing the content of disclosures on policy and practice it will also be important to set this within the contexts of the company's exposure to risk. For example, a joint ACCA, Net Balance report (2011) that explored the reporting quality of Australian companies in the ASX 100 in relation to their management of human rights risk found that of the 47 ASX 100 companies identified as 'exposed' to human rights risks through their areas of operations, 90% had inadequate systems in place to manage that risk. The study found that while 15% disclosed evidence of human rights policy, only 6% were judged to have adequate disclosure on human rights management.

These are just some examples of the important role that a comprehensive literature review will serve in shaping the study. The aim of the literature review will therefore be to develop a comprehensive understanding of why we might hypothesis a link between rights and materiality and the variables that are best proxies for human rights risk, CFP and valuation. This will be used as a basis to develop our model(s).

Phase 2: Case Studies & Materiality Assessment

Case Studies: The second phase will involve a study of a number of key cases. The number of cases will be selected by the project team with input from key stakeholders, based on information and other resources available. Case studies will likely focus on the four key sectors of extractives, apparel, food and beverage and ICT, but may also be drawn more widely from other sectors such as pharmaceuticals or financials.

The case studies will involve interviews with key individuals within the companies involved in these cases. The aim of the case studies will be to further inform our understanding of the nature of the salient and/or material human rights risks. There will be a particular focus on understanding the nature of the impact of rights on reputational risk and associated financial impacts.

Materiality Assessment: In order to develop credible answers to our research questions we first need to clarify the assumptions on which the study will be based – *Market Assumptions & The Efficient Market Hypotheses.*

Most market based studies begin from the assumption that the market is "efficient", in the sense that stock prices reflect all available information about the present value of a firm's future cash flows (Fama, 1991). However, our experience of corporate environmental performance indicates that the market is often slow to "price in" information. For example, an early study by Bie (1994) in relation to investors responses to environmental information, found that the majority of UK analysts did not use environmental information.

We would therefore distinguish between two levels of materiality in relation to the impact of human rights on performance:

a. First, in relation to CFP. This first level of impact could be, for example, on sales, brand valuation, the cost of debt, contingent liabilities and so on. The full list of potential material impacts will be determined in stage one of our research process.

b. Second, in relation to the market valuation of the company as reflected in the firm's stock price.

These two levels of financial materiality will be a potentially important distinction that will enable us to explore the "dynamics" of human rights materiality at different levels. The refinement in the level of analysis will inform the key recommendations that will emerge from the study.

Phase 3: Econometric Modelling & Testing the Hypotheses

There are two potential avenues for an implementation strategy, and within both there are quite a few alternative approaches. First, one could investigate the relationship between human rights allegations, serious incidents and public company's valuation. Several econometric tools are of potential use to address this research question. If stock prices turn out to be our dependent variable, we could use CARs (Cumulative Abnormal Returns) to determine the effect that events such as human rights allegations and serious incidents have on market valuation. We will follow standard finance methodology, controlling for size, market-to-book ratio, leverage, profitability, R&D intensity, advertising intensity and institutional ownership and sector membership when testing for materiality (Khan, Serafeim, & Yoon forthcoming).

Second is to investigate the relationship between the existence and the quality of human rights policies and/or practices and CFP. To answer this question, we could conduct correlation analysis between corporate human rights policies (and potentially also processes/practices) and CFP. Then, in search for causality effect, we could build a regression model, where the dependent variable is CFP of the company, and independent variable(s) relates to human rights policies (controlling for other effects), and test it separately for a target group (companies with outstanding human rights policies, e.g., top ratings in the Corporate Human Rights Benchmark and other relevant ratings), and a control group (companies not included in this index); both groups being simultaneously listed in the S&P500 or similar.

The hypotheses development and econometric modelling will be based on the outcome of Phases 1 and 2. It will be based on the reasoned link between human rights, materiality, and CFP/valuation, rather than the data available.

The empirical data for our model will be derived by combining information from one or more data providers. Data on human rights allegations and incidents on up to 5,000 companies over the period of 2007-2016 will be provided by the research provider and project partner RepRisk. A database for human rights policies and/or practices will be decided on at a later stage. Financial and market data will be derived from COMPUSTAT and CRSP.

Our approach here may also include data from other service providers such as Vigeo Eiris or Sustainalytics, or others, or publicly available information, for example from the Corporate Human Rights Benchmark, which assesses, rates, and discloses corporate human rights management systems across key sectors, and KnowTheChain, which tracks companies' efforts to address human trafficking in the supply chain.

We would also control for the inter-relationship between questions 3 and 4 and assess whether the existence of human rights practices and policies mitigates against the impact of adverse human rights risk.

PRELIMINARY TIMELINE

With the required project funding, we envision the following timeline for this project:

- **Phase/Deliverable 1**: Present Discussion Paper for October 26, 2016 Berkeley convening

- **Phase/Deliverable 2**: Conduct an authoritative literature review/definitive research propositions/research methodology to be published in Spring or early Summer 2017

- **Phase/Deliverable 3**: Conduct a comprehensive study published by Summer 2018 for presentation at a UN-Supported PRI conference in September and the UN Forum on Business and Human Rights in November

Since August 2016, bi-weekly calls have been scheduled for the Organizational Steering Committee. The final timeline will be jointly agreed by the project partners.

PROJECT TEAM

The UC Berkeley project team, consisting of key experts from the Center for Responsible Business at the UC Berkeley Haas School of Business, the Center for Business, Law, and Economy at UC Berkeley School of Law, as well as faculty from UC Berkeley and University of Washington School of Law, are partnering with the UN-supported Principles for Responsible Investment as well as the Alliance Manchester Business School – University of Manchester.

For oversight of the project, we would establish a Steering Committee including representatives from the partners listed above. In addition, to ensure diverse global representation and perspective, we would like to include a number of regional experts at the intersection of investment and human rights in the Steering Committee.

The Steering Committee would identify a project director, project manager, lead researcher, and a team of research assistants to deliver the project.

APPENDIX A

Preliminary Literature Review

The business case for the role and responsibilities of companies in society has been characterized by the challenge of determining a relationship between corporate CFP and sustainability – social and environmental – performance. The studies proving or disproving this relationship have indeed flourished since Friedman's challenge (1970) that the business of business is business[9] (Griffin and Mahon, 1997). However, with over 40 years of academic research, different researchers suggest that this may be due to a failure within current approaches to distinguish between those issues that are material to specific industries and those which are not (Khan, Serafeim, & Yoon forthcoming)[10]

Approach

The present initial literature review gives an overview of the status quo of the academic research on the relationship between corporate sustainability performance (CSP) and CFP. Journals of management, accounting, and business ethics and law have been given a higher priority, with a few non-academic reports included. The review is based on a timeframe of 10-15 years – with few exceptions for papers widely cited as milestones – considering the measurement of the CSP in continuous evolution, thus calling for relatively recent studies to be considered relevant.

Under the umbrella of CSP we have included different theoretical constructs: corporate [social] responsibility; sustainability [social and environmental] reporting; ESG measurement and indicators.

CSP has been chosen here as a proxy for human rights corporate performance. The use of a terminology related to human rights (HRs) for business is an important recent development – initiated with the endorsement of the UN Guiding Principles on Business and Human Rights in 2011 – which has not yet been widely embedded in business-related academic literature or legal scholarship focused on investment and corporate law issues. For this reason, studies aimed at better understanding the link between HRs and CFP are not yet been published in major journals, and they would be therefore invaluable to public institutions, managers, stakeholders, stockholders, and investors.

[9] The first study that empirically examined the relationship between social and financial performance was published in 1971: J. Narver, *Rational management responses to external effects*. Academy of Management Journal, 14:99-114 (Margolis et al., 2003).

[10] Khan, Mozaffar, George Serafeim, and Aaron Yoon. "Corporate Sustainability: First Evidence on Materiality."Accounting Review (forthcoming)

Findings

From a theoretical perspective, business literature recognizes the creation of long-term value when investments are made in CSR practice (Lopez et al., 2007; Koehler and Hespenheide, 2013). Many theoretical analyzes sustain a positive relationship between CFP and CSP as a result of a better ability of companies to manage the expectations of their social context of reference (Perrini et al., 2011; Orlitzky et al., 2003).

However, the measurement of CSP has been proven complex, because of its multidimensional nature, which are determined by internal and external factors. Many studies managed to use only one dimension in their analysis (Lopez, 2007; Garcia-Castro et al., 2010), and this actually interfered with the validity of their conclusions. Moreover, CSP is contingent on many different factors, which raise the complexity of quantitative studies around it.

At the same time, different approaches have been used also in defining CFP (Perrini et al., 2011). Some studies assessed short-run financial impact (i.e. abnormal returns) when firms engage in (ir)responsible activities. Other studies used instead the long-term financial performance -e.g. ROA, ROE and ROS- to measure CFP and then to link it with CSP (Tsoutsoura, 2004).

There have been many challenges faced with studies that examine the relationship between CSP and CSP from sampling problems, to reliability of CSP and CFP measures, to the lack of a causal theory, and a misuse of control variables (McWilliams and Siegel, 2000; Garcia-Castro, 2010; Margolis et al., 2003, 2007; Surroca et al. 2010) In particular, a reasoned comparison of the results obtained does not yet seem scientifically possible, leaving the question of a causal relation between CSP and CFP still open and unsolved.

Yet the majority of studies have found a positive influence – If not a proper correlation – of CSP towards CFP (Margolis et al., 2003), even if this does not prove the link (Griffin and Mahon, 1997). Among others, the following papers sustained a positive relationship between CSP and CFP: Al-Tuwaijri et al., 2004; Brokaw, 2012; Callan and Thomas, 2009; Garcia-Castro et al., 2010; Koehler and Hespenheide, 2013; Orlitzky et al., 2003; Peloza, 2006; Perrini et al. 2011; Qiu et al., 2016; Schnietz and Epstein, 2005; Simpson and Kohers, 2002; Surroca et al., 2009; Tsoutsoura, 2004.

Based on some analysis, it seems also plausible that a causal relation appears more evident in the case of a negative event related to CSP, which directly impacts CFP (see, among others, Schnietz and Epstein 2005; Flammer, 2013; Kappel et al. 2009; King, 2008; Peloza, 2006), mainly relating to a matter of reputational risk.

Moreover, it is recurrent in business ethics journals the idea that stakeholder theory is crucial to define appropriate causal relationships between CFP and CSP (Perrini et al., 2011; Callan and Thomas, 2009; Neville et al., 2005). Similarly, in a human rights perspective – in place of a generic CSP – we could speculate that the adoption of a due diligence process works to fulfil a company's best interest, thanks to the development of competences and knowledge on how to manage right-holders' expectations, respecting their fundamental rights.

Academic studies do not seem to have yet consistently established any correlation – causal relation – between CFP and CSP. Thus the real impact of CSP efforts on CFP is still questionable. A strong methodology on how to measure CSP and CFP seems ineluctable, and it should rely on well-defined hypotheses and scope of the analysis.

This preliminary literature review covers only the last 10 to 15 years. As the project advances, we recommend including a more comprehensive literature review that includes the past 25 years.

Moreover, at this stage we have conducted our research by using key-words and cross references. We suggest, as second step, to proceed with a systematic review of top ranked journals under the following categories of the Association of Business School Academic Journal Guide 2015: Accounting; Finance; General Management, Ethics and Social Responsibility; International Business and Area Studies; Strategy.

APPENDIX B

Bibliography – Preliminary Literature Review

Aggarwal, P. 2013. *Relationship between environmental responsibility and financial performance of firm: a literature review.* Indian Journal of Commerce and Management Studies 4.3 51-59.
Various researches have been conducted over the last decade for examining the relationship between sustainability reporting and financial performance. The results are mixed, inconsistent and often contradictory.

Al-Tuwaijri S. A., Christensen T. E., Hughes K. E. 2004. *The relations among environmental disclosure, environmental performance, and economic performance: a simultaneous equations approach.* Accounting, Organizations and Society, 29(5e6), 447e471.
"Good" environmental performance is significantly associated with "good" economic performance. This has been confirmed by an integrated analysis of the interrelations among environmental disclosure, environmental performance, and economic performance.

Bloomberg. 2016. *Bloomberg Financial Services Gender Equality Index* (GEI).
The GEI includes 26 public companies that are best-in-class in the financial industry in terms of providing opportunities for women. The index was created to satisfy demand from investors, a growing number of whom are looking to gender equality data to inform investment decisions.

Brokaw L. 2012. *Marks and Spencer's Emerging Business Case for Sustainability*. MITSloan Management Review Blog.
Marks and Spencer demonstrates a strong business case for sustainability, with £185m in net benefits from its Sustainability Plan (called Plan A) made available to be reinvested back into the business over a period of five years.

Callan S. J., Thomas J. M. 2009. *Corporate financial performance and corporate social performance: an update and reinvestigation.* Corporate Social Responsibility and Environmental Management, 16(2), 61e78.
Positive CSP–CFP relationship, which supports proponents of stakeholder theory. Data used: Compustat for the CFP; data set called KLD STATS (i.e., Statistical Tool for Analyzing Trends in Social and Environmental Performance) for the CSP.

Clarkson P. M., Li Y., Richardson G. D., Vasvari F. P. 2011. *Does it really pay to be green? Determinants and consequences of proactive environmental strategies*. Journal of Accounting and Public Policy, 30(2), 122-144.
Positive (negative) changes in firms' financial resources in the prior periods are followed by significant improvements (declines) in firm's relative environmental performance in the subsequent periods. Dataset: firm specific financial data are provided by COMPUSTAT; for the environmental variables US Environmental Protection Agency data.

Eccles R. G., Serafeim G., Krzus M. P. 2011. *Market Interest in Nonfinancial Information*. Journal of Applied Corporate Finance - Volume 23 Number 4.
At the aggregate market level, interest in Environmental and Governance information is greater than interest in Social information. U.S. investors are more interested than their European counterparts in governance and less interested in environmental information. Transparency about a company's ESG performance and policies is likely to be used by equity analysts and investors as a proxy for management quality.

(Data from Bloomberg)

Flammer C. 2013. *Corporate social responsibility and shareholder reaction: the environmental awareness of investors*. Academy of Management Journal, Vol. 56, No. 3, 758–781.
Study based on an analysis of the Wall Street Journal relevant press coverage on responsible and irresponsible behavior toward the environment for the whole universe of US publicly traded companies from 1980 to 2009 - then analyzing how the stock market reacted to these events. Over time, the negative stock market reaction to eco-harmful behavior has increased, while the positive reaction to eco-friendly initiatives has decreased (because it has been institutionalized). The positive (negative) stock market reaction to eco-friendly (-harmful) events is smaller for companies with higher levels of environmental CSR. Database used for measuring environmental strengths and concerns: Kinder, Lydenberg, Domini Research & Analytics.

Garcia-Castro R., Arino M. A., Canela M. A. 2010. *Does Social Performance Really Lead to Financial Performance? Accounting for Endogeneity*. Journal of Business Ethics 92:107–126.
The heterogeneous results found in previous studies are not due exclusively to problems related with the measurement instruments or the samples used. The authors posit that a more fundamental problem related with the endogeneity of social strategic decisions could be driving most of the empirical findings. Dataset: 658 firms included in KLD database (1991-2005). Financial data as well as firm-level control variables were collected from Datastream.

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: 5.
Even if the largest number of studies conducted found a positive link between CSP and CFP, this doesn't prove the link. The a priori use of measures may indeed predetermine the CSP/CFP relationship outcome. A substantial number of studies have found also a negative relationship, even if most of these studies compared the reaction of the stock market to potential illegal activities or product problems. Moreover, some studies have been inconclusive because they found both a positive and negative link in the same study. For this study, the authors used multiple sources of data (to triangulate): the Fortune reputation survey; the Kinder, Lydenberg, Domini Index; the Toxics Release Inventory; and corporate philanthropy measures.

Gunnar Friede, Timo Busch & Alexander Bassen. *ESG and financial performance: aggregated evidence from more than 2000 empirical studies.* 15 Dec 2015, Pages 210-233.
The search for a relation between environmental, social, and governance (ESG) criteria and corporate financial performance (CFP) can be traced back to the beginning of the 1970s. Scholars and investors have published more than 2000 empirical studies and several review studies on this relation since then. The largest previous review study analyzes just a fraction of existing primary studies, making findings difficult to generalize. Thus, knowledge on the financial effects of ESG criteria remains fragmented. To overcome this shortcoming, this study extracts all provided primary and secondary data of previous academic review studies. Through doing this, the study combines the findings of about 2200 individual studies. Hence, this study is by far the most exhaustive overview of academic research on this topic and allows for generalizable statements. The results show that the business case for ESG investing is empirically very well founded. Roughly 90% of studies find a nonnegative ESG–CFP relation. More importantly, the large majority of studies reports positive findings. We highlight that the positive ESG impact on CFP appears stable over time. Promising results are obtained when differentiating for portfolio and non-portfolio studies, regions, and young asset classes for ESG investing such as emerging markets, corporate bonds, and green real estate.

Kappel V., Schmidt P., Ziegler A. 2009. *Human rights abuse and corporate stock performance – an event study analysis*. Whitepaper.

Sample of publicly known discrimination cases and short term effects on stock performance. HRs abuse is associated with negative stock performance for US and UK firms. In contrast, the German and Swiss companies provide weak evidence of an effect. Database: LexisNexis – international database of newspapers and scientific publications, using some keywords. + THREDDS Data Server (TDS)

King B. G. 2008. *A Political Mediation Model of Corporate Response to Social Movement Activism.* Administrative Science Quarterly, 53: 395–421
The study considers mechanism whereby boycotts influence their targets: threatening the company's public image. Event studies examining boycotts' effects on stock price returns have mixed results. Three studies found that boycotts (or boycott announcements) generated negative stock price returns (Pruitt and Friedman, 1986; Pruitt, Wei, and White, 1988; Davidson, Worrell, and El-Jelly, 1995), but another study found that some boycotts actually led to positive returns (Koku, Akhigbe, and Springer, 1997). Activists tend to boycott firms with strong reputations and that are highly visible because of their size. Size and corporate reputation appear to be powerful magnets for attracting unwanted attention from social movement activists. Dataset used: matched a database of boycotts 1990-2005 (from 5 US newspapers) with the Standard and Poor's COMPUSTAT database.

Koehler D. A., Hespenheide E. J. 2013. *Finding the value in environmental, social, and governance performance*. Deloitte Review.
ESG is increasingly impacting financial performance because: 1) investors seem to be paying more attention to ESG information (cf. drop in stock price around a negative event); 2) increasing volatility in the global business environment 3) supply chain disruption due to a focus on efficiency – ESG vulnerability 4) rise of social media and private politics (e.g. stock price influenced by media coverage on bad news).

Lopez M. V., Garcia A., Rodriguez L. 2007. *Sustainable Development and Corporate Performance: A Study Based on the Dow Jones Sustainability Index*. Journal of Business Ethics 75:285–300.
They used a total sample of 110 European firms (half belonging to the Dow Jones Sustainability Index) for the period 1998–2004 and analyzed the relevant accounting indicators -mainly profit before tax (PBT) and the business evolution, measured by the growth in revenue (REV)-. In the time frame considered, they did not find grounds for claiming that the adoption of sustainability practices will have positive repercussions on performance indicators. Short-term negative impact on performance is produced.

Margolis J. D., Elfenbein H. A., Walsh J. P. 2007. *Does it pay to be good? A meta-analysis and redirection of research on the relationship between corporate social and financial performance*. Working paper, Harvard Business School.See also Margolis J. D., Walsh J. P. 2003. *Misery loves companies: Rethinking social initiatives by business.* Administrative Science Quarterly, 48(2), 268–305.
The overall correlation between CSR and CFP—more precisely, the coefficient of CSR in the above regression—is positive but small (based on 167 studies).

McWilliams A., Siegel D. 2000. *Corporate social responsibility and financial performance: correlation or misspecification?* Strategic Management Journal 21, no. 5
The authors tested the CSP/CFP link with a regression model that used a dummy variable indicating inclusion of a firm in the Domini 400 Social Index (developed by Kinder, Lydenberg, and Domini, Inc) as the measure of CSP. They used an average of annual values for the period 1991–1996 for 524 large U.S. corporations in a regression model that included a measure of financial performance as the dependent variable. CSP, industry, and expenditures for research and development were independent variables. The results suggested that inclusion of the research and development variable in the model causes the CSP variable to be insignificant. So there may not be a CSP-FP link if the regression model is properly specified.

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.

Using a time series fixed effects approach, the authors find that the relation between CSR and financial performance is much weaker than previously thought. They also find little evidence of causality between CFP and narrower measures of social performance that focus on stakeholder management. The results suggest that strong stock market performance leads to greater firm investment in aspects of CSR devoted to employee relations, but that CSR activities do not affect financial performance.

Dataset: KLD Socrates Database. Financial performance assessed using both accounting (return on assets, or ROA) and market-based (common stock returns) measures from Compustat.

Neville B.A., Bell S., Menguc B. 2005. *Corporate reputation, stakeholders and the social performance-financial performance relationship*. European Journal of Marketing Vol. 39 No. 9/10, pp. 1184-1198.

CSP is affected by stakeholders' resource allocation to the organization. This allocation is based on stakeholders' assessment of the organization's reputation relative to stakeholders' particular expectations, which may be instrumentally and/or normatively framed. Reputation, therefore, plays a key role in the CSP-FP relationship.

Orlitzky M., Schmidt F. L., Rynes S. L. 2003. *Corporate Social and Financial Performance: A Meta-analysis.* Organization Studies 24(3): 403–441.

They conducted a meta-analysis of 52 studies (ABI/Inform Global and PsycINFO) yielding a total sample size of 33,878 observations. They found that there is a positive association between CSP and CFP across industries and across study contexts.

Peloza J. 2006. *Using Corporate Social Responsibility as Insurance for Financial Performance*. California Management Review, 48:2.

Some researchers have cast CSR as being in conflict with CFP, while others cast CSR as complementary to economic objectives. An important yet underemphasized benefit from CSR is insurance against negative events that would otherwise harm financial performance. This insurance is determined by three variables: the level of effort and commitment of the firm, how the firm promotes its CSR, and the relationship between CSR and the core business of the firm.

Perrini F., Russo A., Tencati A., Vurro C. 2011. *Deconstructing the Relationship Between Corporate Social and Financial Performance.* Journal of Business Ethics 102: 59.

Instead of measuring corporate social and environmental performance directly or relying on third-party evaluation, another portion of the studies has assumed performance from corporate social and environmental voluntary disclosure.

The criteria for measuring financial performance has also been different over time: from investor returns to accounting returns or a combination of the two.

The use of different methods of measuring social and economic performance and the incomparability among disparate time periods have been identified as the most important flaws in empirical research.

The study provides a stakeholder-based organizing framework rooted in an extensive review of existing literature on the link between CSP and CFP.

Qiu Y., Shaukat A., Tharyan R. 2016. *Environmental and social disclosures: Link with corporate financial performance*. The British Accounting Review 48: 102-116.

The paper examines the link between a firm's environmental and social disclosures and its profitability and market value. Sample used: the constituents of the FTSE350 index covering the years 2005-2009, financial companies excluded. The results show no relation between environmental disclosures and profitability. On the contrary, social disclosures matter to investors, and firms that make higher social disclosures have higher market values (this link is driven by higher expected growth rates in the cash flows of such companies). This finding may be regarded as unique to UK's institutional context given the historical importance of social issues in UK's political economy.

Schnietz K. E., Epstein M. J. 2005. *Exploring the financial value of a reputation for corporate social responsibility during a crisis*. Corporate Reputation Review 7, no. 4.

The study examined investor reaction to the 1999 Seattle World Trade Organization failure, caused by disagreement among member nations on labor and environmental standards and public protests over the same, finding a financial value in a reputation for CSR during a crisis. A reputation for social responsibility protects firms during a corporate crisis from financial losses.
Dataset: Fortune 500, Domini Social Index

Simpson W. G., Kohers T. 2002. *The Link Between Corporate Social and Financial Performance: Evidence from the Banking Industry*. Journal of Business Ethics 35: 97–109

One of the issues of previous studies linking CSP and CFP was the use of multiple industries sample. They provide empirical evidence from a single industry (banking), using the Community Reinvestment Act ratings as a social performance measure. They found a strong positive link between CSP and CFP.

Surroca J., Tribò J. A., Waddock S. 2009. *Corporate responsibility and financial performance: the role of intangible resources*. Strategic Management Journal 31:5.

The study examines the effects of a firm's intangible resources (innovation, human capital, reputation, culture) in mediating the relationship between corporate responsibility and financial performance. The results show that CRP stimulates the development of intangibles related to innovation, human capital, reputation, and culture, which lead in turn to improved financial outcomes
Dataset: 599 industrial firms included in at least one year of the 2002–2004 Sustainalytics Platform database (before the year2009 known as SiRi Pro)

Thomson Reuters Eikon. 2016. *Diversity & Inclusion (D&I) Index*.

Designed on the hypothesis that companies tracking, reporting and achieving on measures of diversity, inclusion and people development offer better performance over time than those achieving lower scores, or not tracking these measures. The Diversity & Inclusion Index ranks the top 100 publicly traded companies globally with the most diverse and inclusive workplaces, as measured by 24 metrics across four key categories: Diversity, Inclusion, People Development and News Controversies.
The index ratings are supported by Thomson Reuters environmental, social, and governance (ESG) data.

Tsoutsoura M. 2004. *Corporate Social Responsibility and Financial Performance*. Working paper series – Centre for Responsible Business Haas.

The sign of the relationship between CSR and financial performance is positive and statistically significant. Database used: KLD rating data for the companies in Standard & Poor 500; as second measure the Domini 400 Social Index has been used as proxy.

Van der Laan G., Van Ees H., Van Witteloostuijn A. 2008. Corporate Social and Financial
Performance: *An Extended Stakeholder Theory, and Empirical Test with Accounting Measures*. Journal of Business Ethics 79:299–310

The authors analyze the effect of heterogeneity among corporate stakeholder groups on the CSP–CFP nexus. Secondary stakeholders have to rely on a company's reputation for good CSP more than primary stakeholders. The effect on CFP of bad CSP can be expected to be larger than the impact of good CSP, because decision makers evaluate the decision to invest in social performance differently in a situation in which they stand to lose a reputation for being a good corporate citizen as compared to a situation where the company is to decide whether or not to build such a reputation – primary SH.

Dataset used: Kinder, Lydenberg and Domini (KLD). For CFP Thomson Financial’s Datastream.