

## RESEARCH BRIEFS

# WHAT DRIVES EXECUTIVES TO MAKE SOCIALLY RESPONSIBLE INVESTMENTS?

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### RESEARCH QUESTIONS

Corporate social responsibility (CSR) has been the focus of a significant amount of research. Specifically, scholars have looked at whether certain types of top executives are more likely to invest in CSR, and if so, what their motivations are for doing so. For example, do CEOs who invest in CSR do so to further the interests of shareholders and the firm's performance, or to enhance their own reputations? Or, are CEOs investing to further the interests of other corporate stakeholders at the expense of shareholders? What's more, scholars have asked whether these motivations are always mutually exclusive, and whether corporate governance of their firms affect CEOs' decisions regarding CSR. While scholars from a variety of disciplines have long debated these questions, the empirical evidence has been inconclusive. In particular, questions remain about the drivers of CSR and, more specifically, the role that top management plays in shaping a firm's investment in CSR and its impact on firm performance.

Fortunately, a recent study by Richard Borghesi (University of South Florida), Joel Houston (University of Florida), and Andy Naranjo (University of Florida) sheds new light on the subject by examining how the personal attributes of executives drive CSR investments. Borghesi and his colleagues suggest three reasons why top managers invest in CSR—for altruistic reasons, to further a firm's financial interests, and/or to enhance their professional reputations. In particular, this study looks at the political orientation of the CEOs—with the assumption that CEOs donating more to Democrats are more likely to invest in CSR. Borghesi and his colleagues also conjecture that CEOs facing more media exposure will be more responsive to shareholders or stakeholders. Finally, they consider whether CEOs' gender and/or level of experience influence attitudes toward CSR-related investments.

In addition to these individual-level motivations, Borghesi and his colleagues also look at

organizational-level motivations. Specifically, they address whether corporate governance constrains CEOs' actions with respect to CSR investments. They maintain that strong corporate governance implies that shareholders with more power (e.g., institutional investors) may try to dissuade CEOs from investing in CSR.

Finally, the study also considers several different firm-level characteristics that may affect a firm's CSR investments, such as firm size, age, profitability, advertising expenditures, corporate diversification, and the competitiveness of a firm's industry. For instance, more visible (high profile) firms may be more likely to invest in CSR. Likewise, firms with more organizational slack (higher profits and more cash, lower debt ratios) may invest more in CSR. And firms that are more diversified and more global and in less competitive industries may be more likely to expand their CSR programs as well.

### STUDY DESIGN AND METHODOLOGY

Study data came from a sample of 11,711 firm years from 1992 to 2006. Following prior work (e.g., David et al., 2007; Kacperczyk, 2009), Borghesi and his colleagues used Kinder, Lydenberg, Domini and Co. (KLD) data to measure corporate attentiveness to stakeholders. KLD data evaluates several different dimensions of CSR, by looking at corporations' interaction with its key stakeholders (Kacperczyk, 2009). Borghesi and his colleagues used KLD data to create various composite measures for each corporation in each year. Measures of firm-specific and industry-specific independent variables were drawn from COMPUSTAT and many of the variables looking at managerial characteristics were drawn from the ExecuComp database. For political orientation, Borghesi and his colleagues relied on Federal Election Commission databases to assess CEOs' political orientation. Lastly, media exposure was assessed by counting the number of news articles that mentioned each CEO in the Factiva database.

## KEY FINDINGS

The results showed that managerial characteristics matter in terms of understanding corporate investments in CSR. Younger CEOs, female CEOs, and CEOs who receive more media exposure are more likely to invest in CSR. Another significant finding is that CEOs who donate to both major parties are associated with higher levels of CSR, suggesting that a specific political orientation is not driving CSR investments. In terms of media exposure, CEOs who receive more media exposure are much more likely to invest in CSR—perhaps because CEOs with more media coverage feel more pressure to be responsive to stakeholders and to act on the broader interests of society.

With respect to corporate governance, firms with more institutional investors have relatively lower levels of CSR. This implies that CEOs facing more constraints from their investors are less likely to pursue CSR investments. Likewise, there was a negative relationship between the level of industry-adjusted CSR and shareholder value. Borghesi and his colleagues argue that this combined evidence suggests that CSR investments are not aligned with shareholder interests. They infer that CEOs' rationale for investing in CSR is either due to moral motivations and/or enhancement of their personal reputation. Moreover, the study found that large firms with more free cash flow and advertising expenditures have higher levels of CSR.

The results also shed some light on how firm-specific characteristics, managerial characteristics, and corporate governance affect corporate investments in specific dimensions of CSR. Most interestingly, larger and more globally diversified firms with higher levels of free cash flow are more likely to make investments in the community and diversity components of CSR. Interestingly, firms with less cash flow are less likely to invest in environmental, humanitarian, and product categories of CSR. In terms of corporate governance, firms with entrenched managers are more likely to invest in the environmental and humanitarian components of CSR, and less likely to support investments for employees. This result suggests that shareholders prefer investments in employees rather than some of the other categories of CSR. On the other hand, companies with a greater percentage of institutional investors are also less likely to invest in the employee category. Finally, in terms of political orientation, Republican CEOs were less likely to invest in the environmental category of CSR while CEOs who were identified as Democrats were less likely to invest in the product category. CEOs giving to both parties were more likely to implement

policies and programs concerning employees and humanitarian issues.

## CONCLUSION AND IMPLICATIONS

This study makes an important contribution to our understanding of how CEOs shape CSR investments. It also raises some interesting questions about why CEOs are making these investments. One of the questions that persists is, who benefits from CSR investments—shareholders, stakeholders, or the CEO? One theory is that top managers protected from short-term pressures can invest in social policies and programs that are mutually beneficial for society and the firm (Kacperczyk, 2009).

The finding that CEOs who are more entrenched are more likely to invest in environmental and humanitarian policies is consistent with this mindset. It appears that one of the constraints that firms face in terms of being able to broaden their stakeholder focus are the institutional investors who are fixated on short-term results. Consequently, the challenge for CEOs is to demonstrate the payoffs and value associated with their CSR investments to shareholders.

Another interesting question is whether CEOs' political ideologies shape CSR investments. Borghesi and his colleagues challenge extant research on this question (e.g., Chin, Hambrick, & Trevino, 2013; DiGiuli, Kostovetsky, & Leonard, 2011) that finds that liberal CEOs are much more likely to invest in CSR than their conservative counterparts. In contrast, Borghesi and his colleagues find that CEOs donating to both parties are much more likely to invest in CSR. They argue that CSR investments may augment a firm's political connections, rather than the reverse situation where political connections drive CSR investments. This interesting finding informs recent debates about whether a firm's CSR and corporate political activity substitutes and/or complements each other (e.g., den Hond, Rehbein, de Bakker, & Kooijmans-vanLankveld 2014). Either way, these are definitely issues that warrant further attention. That said, Borghesi and his colleagues did find that a CEO's political agenda shapes the *specific* types of CSR investments made by the firm.

Lastly, this study finds that managerial attributes such as gender, age, and life experience impact corporate decisions concerning CSR. Since younger CEOs and female CEOs are more likely to invest in CSR, it does raise questions about the future direction of CSR investments. As corporate leadership continues to diversify and older CEOs become replaced by younger ones, it may be that corporate interest in making CSR investments will increase in the future.

**SOURCE**

Borghesi, R., Houston, J. F., & Naranjo, A. (2014). Corporate socially responsible investments: CEO altruism, reputation, and shareholder interests. *Journal of Corporate Finance, 26*, 164-181.

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