Private companies more likely to embrace corporate responsibility

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When companies make public declarations of social responsibility, it can be hard to tell whether they actually change practices or if they exaggerate the impact—a practice known as greenwashing.

New research by University of Michigan professors Jun Li and Andrew Wu examined the social outcomes of corporate responsibility efforts. They found:

- Private companies are more likely to follow through on corporate social responsibility declarations than public companies.
- Short-term market pressures prevent public companies from devoting the resources to corporate social responsibility efforts.
- Public companies with customer-facing brands are an exception, as this is a case when market incentives align with corporate social responsibility initiatives.

The difference between public and private companies' behavior after signing onto the United Nations Global Compact program was striking.

"There do seem to be conflicts for public companies when it comes to corporate social responsibility," said Li, assistant professor of technology and operations at the Ross School of Business. "They are constrained by shareholders and by law to maximize profits. If the CEO of Patagonia wants to buy organic cotton, he can make it happen even if it means lower margins. A public company has to justify that to shareholders."

Li and Wu developed a novel method to find a common corporate social responsibility proxy and track the outcomes. They examined the 6,420 companies that signed onto the UNGC between 2007 and 2016. It covers a broad array of responsibility goals—such as labor standards, environmental and corporate governance—and it's a unified set of standards.

They then matched those companies with reports from RepRisk, a third-party firm that screens more than 80,000 media, regulatory and commercial documents in 15 languages each day for negative events regarding company-level environmental, social and governance events.

They discovered that private companies in the study reduced their negative impacts, as reported by RepRisk, by 6.3 percent per month. There was no change for public companies, though in some cases the negative impacts increased slightly.

"If you think about corporate social responsibility, it's mostly a diversion of resources," said Wu, assistant professor of technology and operations, and finance, at the Ross School of Business. "Not only from company shareholders to other stakeholders, but also from short term to long term. But public company managers tend to focus more on the short term and are incentivized as such."

The exceptions they found among public companies were ones that own customer-facing brands. In those cases, the value of corporate social responsibility is aligned with shareholders, since consumers often punish companies for irresponsible behavior.

"We segmented where companies are in the supply chain, and when a company owns a brand that's high-profile with consumers, like household products, they have better social responsibility performance," Li said. "But with the B-to-B companies further down the chain you see the greenwashing."

More information: Jun Li. Do Firms Become More Responsible after Corporate Social Responsibility Engagement?, *SSRN Electronic Journal* (2016). DOI: 10.2139/ssrn.2853877

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