Beyond the bottom line: Investors favour companies that give back

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Savvy business leaders understand that when companies give back, they can attract better employees and win customers. But a new study shows they're not only doing it to impress workers and consumers: they're also doing it to boost their bottom line.

Corporate social responsibility, or CSR, is defined as actions that promote social good beyond the immediate interest of a company and its shareholders, and also beyond what is required by law. This can include things like sponsoring a new city park, launching green initiatives, setting up an employee assistance program, seconding an employee to a charitable organization, or making improvements to safety and working conditions that are far greater than what regulations demand.

New research from the UBC Sauder School of Business found that when public interest in corporate social responsibility is high, investors place a premium on companies that get involved in CSR activities. In other words, when companies do good, investors perceive greater value—even if the fundamentals aren't especially impressive.

"Back in the late '90s there was similar investor sentiment for dot-com companies. Companies changed their names to dot-com and they saw their stock prices increase," says UBC Sauder assistant professor Ira Yeung, who co-authored the study.

"Recently it was the same thing with blockchain companies: we saw companies that added blockchain to their corporate name and their stock price jumped," he says. "We wanted to look at investor sentiment—not for dot-com companies or for blockchain, but for CSR activity."

Analyzing information from the Thomson Reuters ASSET4 databases as well as thousands of corporate press releases that announced CSR initiatives, the researchers tracked the link between CSR activities and stock market performance, and found that when consumer interest in CSR is high, stock prices jump.

The researchers also noted that businesses respond to that sentimentdriven investing by upping their CSR activities—especially when they're looking for a short-term stock market boost. This is especially true for firms that are inherently difficult to value, or that have more transient investors and higher share turnover.

The findings have significant implications both for businesses and for investors. Yeung says companies that aren't involved in corporate social responsibility might want to consider the significant role CSR can play in investor sentiment. "The value of the company is not just purely the future cash flows or future profits," he explains. "Clearly investors value companies more than just future profits, and CSR activities play a role in that."

Conversely, companies that are too heavily involved in CSR activities should also be mindful that, as was the case with the dot-com bust, consumer sentiment can shift, and the premium people place on those CSR projects in theory could diminish—even though interest in CSR has been on a steady incline for years. "If they are doing CSR to boost the short-term stock price, they may want to be very careful about that," cautions Yeung.

For the same reason, investors should be careful not to overpay for companies whose stock prices are high because of CSR-driven sentiment.

"Some of these companies might be responding too much to CSR sentiment, or they might be quite overpriced relative to companies that are not doing CSR, so the future returns of these high CSR firms could be lower," explains Yeung. "They should be a little wary about investing in some of these companies, especially when investor sentiment for CSR is high."

More information: papers.ssrn.com/sol3/papers.cf …

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