Hello everyone

The article I chosen is entitled: Causality between CSP and financial performance: evidence from canadian firms.

It is an article written in 2008 by 3 authors and published in the journal of business ethics.

Two observations motivated the writing of this article:

The first one is : on relationship between CSP and FP, there are a few studies including Canadian firms

Second one: the introduction in 2004 of the CSID which is a database including only Canadian publicly traded firms and providing quantitative data on CSP

The aim of this article is to analyze the causal relationship between PSC and PS using the Granger causality approach.

The Granger causality approach is a statistical concept based on prediction developed in 1969 by Clive Granger.

The difference between a regression is that the regression highlights the notion of dependence between two variables, whether (wèder) or not there is causality, whereas the Granger causality allows the prediction of future values of a time serie using one variable of another old time serie

Based on the Preston and Bannon article, the 3 articles have highlighted 6 hypothesis

Social impact based on Stakeholder theory taking into account the needs of different stakeholders leads to an increase in PS

- Slack resource theory the more you have a good FP the more you have the possibility to invest in different social / socially responsible actions and conversely, the less FP we have, the less we invest into social initiatives

- The trade-offe hypothesis increasing one's CPS only brings some economic benefits and many economic costs that reduce the wealth (well) of the shareholders.

- Management opportunism hypothesis is based on the fact that managers pursue their personal interests to the detriment of the shareholders and the different stakeholders. When PS is high they reduce in CSP and when PS is not good they increase CSP to hide bad results

- Positive synergy hypothesis: is qualified to "virtuous circle"→ because having a high CSP leads to a good PS which pushes us to invest more on social aspects

- Negative synergy hypothesis is qualified to "vicious circle" → because having a high CSP leads to a degradation of PS and and so we reduce investments in social aspects

Methodology

The article focuses on 336 observations over a period between 2004-2005. The financial data come from the TSX and social CSID.

As variables we have two main: CSP which is measured by: … FP measures which is measured by ROA, ROE and market return. As control variables, the authors have chosen size, risk and industry. And they formulated the hypothesis as follow:

We have two models. The first one is to see if the financial performance granger cause the CSP in 2005 and the second model is the same but it's to see if the CSP 2004 granger cause FP 2005

Results

This table represents: The first regression between the aggregated CSP and the different FP measures

For model 1 (in blue) we see that there is no significant relationship and therefore no FP 2004 granger causes CSP → it means that is our case, using the FP in 2004 for predict CSP in a time serie isn't significant

For model 2 we see that there is a negative relationship between CSP aggregate and market return

The result demonstrate two thing:

1) the existence of an unidirectional granger causal relationship between CSP aggregate score and FP measures ;
2) and the negative reaction of the market face to a high CSP aggregate score

In the both models, the control variable don't play a significant role for the predictions

For our second regression, we will put the CSP elements (community & society, corporate governance, employees, environment, customer, and human rights) and the FP measures. Unfortunately, the authors have not yet responded to my request for quantitative data, so we don't have a regression data for both models. But the autors founded a significant relationship between employee score, environmental score, and FP measures

*Nevertheless, for the regression between employee score and FP measures

For model 2 there is a significant negative relationship between market return and employees.

Looking more closely these result, we see that the market reacts negatively when a company invest in their employee even we know that the employees play an important role in the financial performance of a company

For the regression between environmental score and FP measures

Model 1 no significant relationship the variables

but for model 2 we notice two significant negative relationships notably a granger causality between the environment score and the ROA and market return. The authors mentioned a significant negative relationship at a level of 10% between ROE and environmental score → we have 10% by dividing 0.025/0.013 = 1.92

These results correspond to the trade-off hypothesis and negative synergy hypothesis. Trade off hypothesis because of the negative impact on ROE → so a high environmental score reduces the wealth of shareholder and negative synergy hypothesis because of the negative impact on ROA & market return → so a having high environmental score leads to the degradation of FP

As a finding, the authors discovered:

-Implementing sociales aspects in a Canadian firm is too costly and the gains are too small in the short term

-The Canadian firms needs the financial support of the government to help them for this implementation of social aspects

As limitations

I found two limitations, mostly about the period chosen

-the period because the granger approach is using the predict a time serie but this period is too small,

-because the period are the small and close, the variation between variables are small → lead to a poorly prediction

-the authors don't consider the regulation because based on the industry, the regulation has a significant impact on CSP it's depend of industry.