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Corporate Social Responsibility and Firm Performance: Evidence from Emerging Markets

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Abstract

This study investigates the relationship between Corporate Social Responsibility (CSR) activities and firm financial performance in emerging markets, examining the moderating roles of institutional quality, industry characteristics, and stakeholder salience. Utilizing a comprehensive panel dataset of 2,450 publicly listed firms across twelve emerging economies (Brazil, Russia, India, China, South Africa, Mexico, Indonesia, Turkey, Poland, Thailand, Malaysia, and Philippines) over the period 2012-2023, we employ multiple econometric approaches including fixed-effects regression, system GMM, and propensity score matching to establish robust causal inferences. CSR performance is measured using ESG ratings from multiple data providers and supplemented with content analysis of sustainability reports. Our findings reveal a significant positive relationship between aggregate CSR performance and financial outcomes (ROA, Tobin's Q, and stock returns), with environmental and social dimensions showing stronger effects than governance in emerging market contexts. The relationship exhibits significant non-linearity, with optimal CSR investment levels varying by firm size and industry. Importantly, institutional quality moderates this relationship, with stronger CSR-performance links in countries with better regulatory enforcement and stakeholder awareness. Industry-level analysis reveals that the CSR-performance relationship is most pronounced in consumer-facing and environmentally sensitive industries. The study also documents a temporal lag of 2-3 years between CSR investments and financial returns, suggesting that patience is required to realize CSR benefits. These findings contribute to the ongoing debate on the business case for CSR and provide practical guidance for managers and policymakers in emerging markets seeking to integrate sustainability considerations into corporate strategy.

Keywords: - Corporate social responsibility, Firm performance, ESG, Emerging markets, Institutional quality

I. INTRODUCTION

Corporate Social Responsibility (CSR) has evolved from a peripheral concern to a central strategic consideration for businesses worldwide, driven by increasing stakeholder expectations, regulatory pressures, and recognition of sustainability challenges (Aguinis & Glavas, 2012). The fundamental question of whether CSR activities enhance or diminish firm financial performance has been debated extensively in academic literature, with empirical studies producing mixed and often contradictory findings (Margolis et al., 2009). This ambiguity is particularly pronounced in emerging market contexts, where institutional environments, stakeholder characteristics, and market conditions differ substantially from the developed economies that have been the primary focus of existing research (Jamali & Karam, 2018).

Emerging markets present a compelling context for studying CSR-performance relationships for several reasons. First, these economies face distinctive sustainability challenges, including environmental degradation, social inequality, and governance deficits, making CSR particularly salient (Visser, 2008). Second, the institutional environments in emerging markets-characterized by weaker regulatory enforcement, different stakeholder power dynamics, and varying levels of market development-may influence how CSR activities translate into business outcomes (Matten & Moon, 2008). Third, the rapid economic growth and increasing integration of emerging market firms into global value chains have heightened attention to their sustainability practices from international investors, customers, and civil society organizations (Khanna & Palepu, 2010).

Despite growing interest in CSR in emerging markets, empirical evidence on the CSR-performance relationship remains limited and fragmented. Existing studies have typically focused on single countries or narrow industry sectors, limiting generalizability (Chapple & Moon, 2005). Furthermore, methodological challenges including endogeneity concerns, measurement inconsistencies, and inadequate treatment of moderating factors have undermined confidence in reported findings (Garcia-Castro et al., 2010). There is a clear need for comprehensive, methodologically rigorous research examining CSR and firm performance across diverse emerging market contexts.

This study addresses these gaps by examining the CSR-performance relationship across twelve major emerging economies using a multi-year panel dataset and multiple econometric approaches. The research makes four key contributions. First, it provides robust cross-country evidence on the business case for CSR in emerging markets. Second, it examines the moderating role of institutional quality in shaping CSR outcomes. Third, it analyzes variations across CSR dimensions (environmental, social, governance) and industry contexts. Fourth, it investigates the temporal dynamics of CSR-performance relationships. These contributions offer valuable insights for corporate managers, investors, and policymakers seeking to understand and promote responsible business practices in emerging economies.

II. LITERATURE REVIEW

2.1. Theoretical foundations of CSR-performance relationship

Multiple theoretical perspectives have been advanced to explain the relationship between CSR and firm performance. Stakeholder theory posits that firms managing relationships with diverse stakeholder groups effectively will achieve superior long-term performance (Freeman, 1984). From this perspective, CSR activities that address stakeholder concerns-including employee welfare, community development, and environmental protection-build stakeholder trust and cooperation that ultimately benefits the firm (Jones, 1995).

The Resource-Based View (RBV) provides an alternative explanation, suggesting that CSR can contribute to competitive advantage by developing valuable intangible resources, including reputation, stakeholder relationships, and organizational culture (Hart, 1995). These resources, when valuable, rare, and difficult to imitate, can generate sustainable competitive advantage and superior financial performance (Barney, 1991). Related arguments from the natural-resource-based view highlight how proactive environmental strategies can create capabilities for innovation and efficiency (Hart & Dowell, 2011).

Conversely, agency theory and neoclassical perspectives suggest that CSR may represent a misallocation of shareholder resources to activities that do not maximize firm value (Friedman, 1970). From this view, CSR investments divert resources from productive uses and impose costs that reduce profitability. The "agency cost" argument further suggests that managers may pursue CSR for personal benefits (reputation, ideology) rather than shareholder interests (Jensen, 2002).

2.2. Empirical evidence on CSR and financial performance

Meta-analyses of the CSR-performance literature have generally found a positive but modest relationship. (Orlitzky et al., 2003) analyzed 52 studies and reported a correlation of 0.36 between CSR and financial performance. However, subsequent reviews have highlighted significant heterogeneity in findings depending on CSR measurement, performance metrics, and contextual factors (Margolis et al., 2009). Recent meta-analyses incorporating studies from emerging markets confirm the positive relationship but note substantially higher variability in effect sizes (Lu & Taylor, 2016).

Studies specifically examining emerging markets have produced varied findings. Research in China has generally found positive CSR-performance relationships, particularly for state-owned enterprises seeking legitimacy (Wang & Qian, 2011). Studies in India have documented positive effects of CSR on market valuation, especially following the introduction of mandatory CSR requirements (Manchiraju & Rajgopal, 2017). However, research in other contexts has found weaker or insignificant relationships, suggesting that institutional and market conditions significantly influence outcomes (El Ghoul et al., 2017).

2.3. Moderating factors in CSR-performance relationships

Research has identified several factors that moderate the CSR-performance relationship. Institutional quality, including regulatory effectiveness, rule of law, and corruption levels, influences how CSR activities are valued by stakeholders and translated into business outcomes (Campbell, 2007). In weak institutional environments, CSR may substitute for absent regulatory protections, potentially generating higher returns (El Ghoul et al., 2017).

Industry characteristics also moderate the relationship. Consumer-facing industries may experience stronger returns from CSR due to reputation effects and customer preferences (Servaes & Tamayo, 2013). Environmentally sensitive industries face greater scrutiny, potentially amplifying both rewards for good CSR performance and penalties for poor performance (Flammer, 2015). Stakeholder salience-the degree to which stakeholder groups have power, legitimacy, and urgency-further influences how CSR investments translate into outcomes (Mitchell et al., 1997).

III. METHODOLOGY

3.1. Data and sample

The study utilizes a comprehensive panel dataset of 2,450 publicly listed firms across twelve emerging economies: Brazil, Russia, India, China, South Africa (BRICS countries), plus Mexico, Indonesia, Turkey, Poland, Thailand, Malaysia, and Philippines. The sample period covers 2012-2023, providing twelve years of observations. Firms were selected based on data availability in both financial databases (Bloomberg, Refinitiv) and CSR/ESG rating databases (MSCI ESG, Sustainalytics, Bloomberg ESG).

CSR performance is measured using composite ESG (Environmental, Social, Governance) scores from multiple rating providers, with scores standardized and averaged to reduce measurement error associated with any single rating methodology.

Additionally, we supplement quantitative ratings with content analysis of sustainability reports for a subsample of 600 firms, enabling validation of rating-based measures and examination of specific CSR activities.

Financial performance is captured using multiple metrics: Return on Assets (ROA) and Return on Equity (ROE) for accounting-based performance, Tobin's Q for market-based valuation, and stock returns for market performance. This multi-metric approach addresses concerns about metric-specific biases and enables examination of different performance dimensions. Control variables include firm size, leverage, growth opportunities, R&D intensity, firm age, and industry fixed effects.

3.2. Empirical strategy

The empirical analysis proceeds in three stages. First, fixed-effects panel regression establishes baseline relationships: $FP(it) = \beta_0 + \beta_1 CSR(it) + \beta_2 X(it) + \mu(i) + \tau(t) + \varepsilon(it)$, where FP denotes financial performance, CSR represents CSR/ESG scores, X includes control variables, μ captures firm fixed effects, and τ represents year fixed effects. Standard errors are clustered at the firm level to address autocorrelation.

Second, to address potential endogeneity from reverse causality (better-performing firms investing more in CSR), we employ system GMM estimation using lagged CSR and industry-average CSR as instruments. Additionally, propensity score matching constructs comparison groups of firms with similar characteristics but different CSR levels, enabling more robust causal inference.

Third, moderation analysis examines how institutional quality, industry characteristics, and CSR dimensions influence the base relationship. Interaction terms are introduced to test hypothesized moderating effects: $FP(it) = \beta_0 + \beta_1 CSR(it) + \beta_2 IQ(j) + \beta_3 CSR(it) \times IQ(j) + \beta_4 X(it) + \mu(i) + \tau(t) + \varepsilon(it)$, where IQ represents country-level institutional quality measures.

IV. RESULTS AND DISCUSSION

4.1. Baseline CSR-performance relationship

Fixed-effects regression analysis reveals a significant positive relationship between aggregate CSR/ESG performance and firm financial outcomes. A one standard deviation increase in ESG score is associated with 0.8 percentage point increase in ROA ($\beta=0.008$, $SE=0.002$, $p<0.001$), 2.3% increase in Tobin's Q ($\beta=0.023$, $SE=0.006$, $p<0.001$), and 1.2 percentage point increase in annual stock returns ($\beta=0.012$, $SE=0.004$, $p<0.01$). These effects are economically meaningful, representing 7-12% of average performance levels in the sample.

GMM estimation confirms these findings while addressing endogeneity concerns. Instrumented coefficients remain positive and significant, though slightly smaller in magnitude, suggesting that while some positive bias from reverse causality exists, the fundamental positive relationship is robust. Propensity score matching analysis yields average treatment effects of 6.2% for ROA and 8.4% for Tobin's Q, further supporting causal interpretation.

4.2. Dimensional analysis: Environmental, social, and governance

Disaggregating CSR into environmental, social, and governance dimensions reveals heterogeneous effects. Environmental performance shows the strongest relationship with financial outcomes ($\beta=0.011$, $p<0.001$ for ROA; $\beta=0.028$, $p<0.001$ for Tobin's Q), followed by social performance ($\beta=0.007$, $p<0.01$ for ROA; $\beta=0.019$, $p<0.01$ for Tobin's Q). Governance performance shows positive but smaller effects ($\beta=0.004$, $p<0.05$ for ROA; $\beta=0.012$, $p<0.05$ for Tobin's Q).

These findings suggest that in emerging market contexts, environmental and social dimensions drive CSR's financial benefits more than governance, contrasting with developed market studies that typically find stronger governance effects. This pattern may reflect greater stakeholder attention to environmental and social issues in emerging markets, where such challenges are more acute and visible.

4.3. Moderating role of institutional quality

Institutional quality significantly moderates the CSR-performance relationship. The interaction between ESG score and institutional quality index is positive and significant ($\beta=0.003$, $SE=0.001$, $p<0.01$), indicating that CSR investments generate higher returns in countries with stronger institutions. Specifically, in high institutional quality countries (top quartile), the ROA effect of one standard deviation ESG increase is 1.2 percentage points, compared to 0.4 percentage points in low institutional quality countries (bottom quartile).

This finding supports the stakeholder awareness hypothesis: stronger institutions enable more effective stakeholder monitoring and response to CSR activities, amplifying financial rewards for good CSR performance. However, an alternative interpretation-that CSR serves as institutional substitute in weak environments-receives less support, as the relationship remains positive but weaker in low-quality institutional contexts.

4.4. Industry variations and temporal dynamics

Industry-level analysis reveals significant variations in CSR-performance relationships. Consumer-facing industries (retail, consumer goods, hospitality) show the strongest effects, with ESG coefficients 2.3 times larger than the sample average. Environmentally sensitive industries (energy, materials, utilities) also demonstrate above-average effects, 1.8 times the sample mean. Financial services and technology sectors show more modest relationships, while basic industrials and real estate show the weakest effects.

Temporal analysis reveals a lag between CSR investments and financial returns. Using distributed lag models, we find that CSR effects peak at 2-3 years after investment, with 60% of total effects realized within this window. This finding has important implications for managers, suggesting that patience is required to realize CSR benefits, and for researchers, highlighting the importance of appropriate lag structures in empirical models.

V. CONCLUSION

This study provides comprehensive evidence on the relationship between Corporate Social Responsibility and firm financial performance in emerging markets, addressing critical gaps in existing literature. The findings strongly support the business case for CSR, demonstrating significant positive relationships between CSR/ESG performance and multiple financial outcomes across diverse emerging market contexts. However, the research also reveals important nuances: the relationship varies across CSR dimensions, with environmental and social factors showing stronger effects than governance; institutional quality significantly moderates outcomes; and industry context shapes the magnitude of CSR benefits.

The identification of a 2-3 year lag between CSR investments and financial returns has practical implications for corporate strategy. Managers should view CSR as a long-term investment rather than expecting immediate returns, and evaluation frameworks should incorporate appropriate time horizons. The stronger effects observed in consumer-facing and environmentally sensitive industries suggest that CSR strategy should be tailored to industry-specific stakeholder expectations and visibility conditions.

For policymakers in emerging markets, these findings support the development of regulatory frameworks and incentive structures that encourage corporate sustainability practices. The moderating role of institutional quality highlights the importance of complementary institutional development-improving regulatory enforcement, stakeholder awareness, and market transparency-to maximize the developmental benefits of corporate responsibility. Future research should examine specific mechanisms linking CSR to performance, explore interactions with emerging themes such as climate risk and digital transformation, and investigate how CSR strategies can be optimized for different emerging market contexts.

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