



# A stakeholder resource-based view of corporate social irresponsibility: Evidence from China

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## ABSTRACT

Following the stakeholder resource-based view (SRBV), we conceptualize the value relevance of corporate social irresponsibility (CSI) based on the stakeholders' bargaining power and interests in the well-being of the firm, and classify the stakeholders into *residual claimants* (i.e., customers, shareholders) and *fixed claimants* (i.e., employees, environment). Using curated detailed news data of 816 CSI episodes and 56,503 Chinese government daily publications from June 2006 to July 2012, we find that CSI episodes alienating residual claimant stakeholders lead to greater shareholder value destruction. Drawing from the stakeholder salience, we find that CSI episodes alienating high legitimacy claims of shareholders and customers, high urgency claims of employees, and powerful claims of customers result in a more pronounced underperformance. Although there are potentially overlapping boundaries between fixed and residual claimants under special circumstances, the findings provide implications for firms making strategic decisions involving multiple stakeholders.

## 1. Introduction

In the last two decades, the world has witnessed large-scale corporate actions that are deemed as socially irresponsible. From Enron's and WorldCom's accounting fraud to Foxconn's suicides and Sanlu's melamine contamination in milk products, these pervasive corporate irresponsible behaviors have brought adverse impacts to our society. While the literature has focused primarily on corporate social responsibility (CSR), recent emerging studies point out that corporate social irresponsibility (CSI) brings different perspectives in terms of the context, media attention, and its value relevance (e.g., Doh et al., 2010; Hawn, 2020; Lange and Washburn, 2012; Nardella, Brammer and Surdu, 2020; Pearce and Manz, 2011; Price and Sun, 2017; Putrevu et al., 2012; Zylidopoulos et al., 2012).

The literature defines corporate social responsibility (CSR) as corporate responsibilities that have a positive impact on the environment, society and its associated stakeholders, beyond the firms' interests in making profits (Carroll, 1979; McWilliams and Siegel, 2001; Zylidopoulos et al., 2012). While it is natural to consider CSI as the opposite of CSR, recent studies point out that CSI is not necessarily the opposite side of the coin of CSR, as context and incentives differ (e.g., Jones, Bowd &

Tench, 2009; Lange & Washburn, 2012; Muller & Kraussl, 2011; Pearce & Manz, 2011; Price & Sun, 2017). We follow Strike et al. (2006) to define corporate social irresponsibility (CSI) as corporate actions that adversely affect identifiable stakeholders' legitimate claims. Based on the stakeholder theory and the stakeholder resource-based view (Barney, 2018; Freeman et al., 2020), we also argue that CSI is not the exact opposite of CSR because CSI is more relevant to the maintenance of sustainable stakeholder relationships, while CSR is more relevant to the building of such relationships. Compared to CSR, companies have no incentive to publicize CSI which is usually discovered by third parties such as the government, regulators, and news media instead of actively promoted by the firm. Therefore, the government and the news media play significant roles in the value relevance of CSI. The difference between CSR and CSI has considerable implications for the timing and terminology of CSI. In terms of timing, CSR research typically observes when an act of CSR was *commenced*, while CSI research only observes when it was *discovered*. To accurately reflect this inability of researchers to observe the commencement of CSI, we use the term "episode" instead of "act" to imply the uncertain commencement time. Therefore, our study contributes to the CSI literature by examining the impact of CSI episodes observed by the public and the news media on the firms' stock

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returns.

Studies on the relationship between CSI and corporate financial performance to date mostly focus on the developed markets (Kölbel et al., 2017; Kruger, 2015; Oikonomou et al., 2014; Price and Sun, 2017). Little is known about episodes of CSI and their potential shareholder value destruction in emerging markets. CSI episodes have occurred extensively in China over the last decade, such as the melamine contamination of milk and other high-profile food safety incidents. Similarly, China is considered to have relatively weak investor protection (Chen et al., 2013; La Porta et al., 1997) and the Chinese central government holds relatively high legal authority over corporations and financial markets (Brunnermeier et al., 2018; Claessens et al., 2000; Tian and Estrin, 2008). These settings allow us to examine the stakeholder salience because the Chinese central government's concerns represent the legitimacy of stakeholder claims while the severity and source reach of the news media represent the urgency and power of stakeholder claims. Furthermore, Stevens et al. (2016) argue that news media reporting on Chinese firms has become important in recent years and is intensified through global distribution. Hence, based on the social media news, they acknowledge the importance of media news since "social license granted by actors in civil society is a social contract, rather than the legal one" (Stevens et al., 2016, p.951). This social (informal) contract or claim established from the news media is crucial for firms to maintain their legitimacy to operate (Henisz et al., 2014). While extant literature examines the impact of CSI, measured by CSR concerns, on firms' performance (e.g., Strike et al., 2006; Price and Sun, 2017), our study makes an empirical contribution by examining the stock value relevance of CSI episodes that are identified by the news media and the central government concerns.

In considering the value relevance of CSI, we follow the stakeholder resource-based view (SRBV hereafter) that "the generation of firm profits requires that stakeholders, besides shareholders, hold *residual claims* on firm profits" (Barney, 2018: p. 3306). In other words, a stakeholder who controls and provides access to resources that create the most value in a bundle of co-specialized resources for the firm holds higher "economic bargaining power" and hence is considered a *residual claimant* as opposed to a *fixed claimant*. Drawing from SRBV, we argue that the shareholder value destruction effect of CSI is stronger when it destroys the relationships between the firm and its residual claimant stakeholders compared to the fixed claimant stakeholders because the former provides access to resources that are vital to a firm's economic profits. Based on the SRBV, we also argue that the value relevance of CSI depends on the stakeholders' interest in the well-being of the firm.

Furthermore, the nature of fixed and residual claims is likely to vary based on the stakeholder salience. Mitchell et al. (1997) define stakeholder groups who have the *legitimate moral* or *presumed* (implicit) claims based on the attributes of stakeholder salience: legitimacy, urgency and power. Equivalent to Mitchell et al.'s (1997) typology for stakeholder salience, we also examine the value relevance of CSI that destroys the relationship with key stakeholders who i) hold high legitimacy within our socially constructed system of laws, norms and values; ii) are considered as urgent and time-sensitive to the firm; or iii) have the power to alter the firms' CSI activities or to force the firm to follow the stakeholders' desire (objectives).

Answering recent calls for further conceptual development in the stakeholder theory and the resource-based view (Dmytriiev et al., 2021; Freeman et al., 2021), our study makes a theoretical contribution by conceptualizing the value relevance of CSI drawing from the SRBV, which is based on the resource-based view, and the stakeholder salience, which is based on the stakeholder theory. This conceptual contribution is important since extant literature (e.g., Agle et al., 1999; Brower and Rowe, 2017) mostly applied the SRBV and the stakeholder salience to CSR but not to CSI. Considering that the stakeholders' negative attributions are stronger toward CSI than their positive attributions toward CSR (Lange and Washburn, 2012), and maintaining sustainable stakeholder relationships is the key to firms' competitive advantage, the

concepts of stakeholder resource-based view and stakeholder salience are even more pertinent to examine the value relevance of the CSI.

## 2. Hypotheses development

Literature on CSI is growing. Based on the resource-based view, Strike et al. (2006) find that internationally diversified firms act socially responsibly in order to create value but also destroy their value when they act irresponsibly. They argue that CSI worsens identifiable social stakeholders' welfare, which eventually negatively affects the firms' valuable resources. Lenz et al. (2017) illustrate CSR and CSI interactions by drawing upon the instrumental stakeholder theory, and argue that different domains of CSR have differential value implications and that CSI negatively affects CSR's positive impact on firm value. Price and Sun (2017) examine the value relevance of CSR and CSI by using a moderating high-low matrix, and suggest that CSI incidents have stronger influence and longer lasting impact on market value than CSR.

More recent studies examine CSI separately from CSR. Based on the stakeholder agency theory (Hill and Jones, 1992), Jain and Zaman (2020) demonstrate that the board structure significantly affects firms' CSI. Drawing from the attribution theory, Lange and Washburn (2012) and Antonetti and Maklan (2016) argue that observers tend to react more negatively to CSI because social irresponsibility has a greater capacity to attract the observers' attention. Based on attribution and expectancy violations theories, Nardella, Brammer and Surdu (2020) investigate the impact of CSI attributions on changes in organizational reputation and demonstrate stakeholder assessments from CSI according to their prior perceptions of organizational behavior. Shea and Hawn (2019) show that social perceptions of firms' friendliness (warmth) and competence influence the value relevance of CSI. Hawn (2020) finds that the media coverage of firms' CSI plays a more significant role than CSR in the probability of success and the duration of cross-border acquisitions. Kölbel et al. (2017) utilize the agenda setting theory as a complement to stakeholder theory and employ RepRisk data to analyze the relationship between CSI and bondholders' credit risk. They find that the source reach and the severity of media coverage on firms' CSI indeed increase firms' credit risk. However, the extant literature has not yet integrated the thinking of various types of stakeholders which can make the case for comprehensive understanding of the implications of firms' CSI profile. We argue that different domains of CSI, such as environmental episodes and corporate government episodes, only impact the concerned and relevant crucial types of stakeholders and the impact itself is also different. To the best of our knowledge, our study is the first to empirically investigate the shareholder value effect of CSI by utilizing the framework of stakeholder resource-based view (SRBV) and the stakeholder salience (see a comparison of closely related studies in Table 1). The detailed hypotheses development processes are discussed below.

### 2.1. Value relevance of CSI for residual and fixed claimants

The resource-based view (RBV) focuses on firms' ability to profit from having resources and social networks that create sustained competitive advantages (Barney, 1986, 1991; Barney, 2001; Barney et al., 2011; Helfat and Peteraf, 2003; McWilliams and Siegel, 2001, 2011; Rumelt, 1984; Wernerfelt, 1984)<sup>1</sup>. The literature has recognized that RBV explains how CSR can generate sustained competitive advantages for firms (e.g. McWilliams and Siegel, 2001; Orlitzky et al., 2011; Siegel and Vitaliano, 2007; Zygliopoulos et al., 2012). Considering the importance of stakeholders in firms' ability to obtain sustainable and cooperative advantage (Freeman et al., 2020), the SRBV is a timely extension to the RBV as it recognizes that "the generation of firm profits requires that stakeholders, besides shareholders, hold residual claims on the firms' profits" (Barney, 2018, p.3306). Based on the SRBV and the stakeholder theory, we consider CSI as a firm's wrongdoing that destroys its competitive advantage since CSI adversely affects the

**Table 1**  
Related empirical studies on CSI and corporate financial performance.

	Strike et al. (2006)	Price and Sun (2017)	Lenz et al. (2017)	Kölbel et al. (2017)	Walker et al. (2019)
Focusing on CSI	✓	✓	✓	✓	✓
Examining CSI across different domains	X	X	✓	X	X
Examining CSI characteristics	X	X	X	✓	X
Examining fixed versus residual claimants	X	X	X	X	X
Examining shareholder return	X	X	X	X	X
Research objective	Investigates whether international diversification of large US firms relates to CSR	Investigates the impact of CSR and CSI on firm performance	Investigates the role of CSI contextual factors on the link between CSR and firm value	Investigates the relationship between CSI and firm risk	Investigates the impact of CSI on firm performance in coordinated market economies (CMEs) and liberal market economies (LMEs)
Theoretical framework for CSI	Organizational complexity theory	Instrumental Stakeholder theory	Instrumental stakeholder theory	Instrumental Stakeholder theory, agenda setting theory	Institutional theory
Sample period (Region)	222 firms between 1993 and 2003 (US)	562 firms between 2000 and 2010 (US)	3041 firms between 1991 and 2009 (US)	539 firms between 2008 and 2013 (38 countries)	8608 firm-year between 2009 and 2013 (16 countries)
Model/method	GLS regression analyses	OLS regressions and VAR	Linear mixed with Gaussian copulas	OLS regressions	OLS regressions
Measures of CSI	KLD database	KLD database	KLD database	RepRisk database	Sustainalytics database
Summary of main results	Firms can act socially responsible and socially irresponsible at the same time, and CSI is caused by increased complexity of international diversification.	CSI provides a longer enduring effect than CSR and firms engaging little CSR and CSI perform better than firms engaging highly of both.	CSR is financially devalued when CSI occurs. CSI moderates the positive relation between other domain CSR and firm value.	Firms receiving higher CSI media coverage leads to higher financial risk.	CSI in LMEs is higher than CMEs and CSI adversely affects firm performance in LMEs but not CME. Corporations mirror their institutional environment.
	Sun & Ding (2020)	Zaman et al. (2020)	Hawn (2021)	Harjoto et al. (2021)	This study
Focusing on CSI	✓	✓	✓	✓	✓
Examining CSI across different domains	X	X	X	X	✓
Examining CSI characteristics	X	X	X	✓	✓
Examining fixed versus residual claimants	X	X	X	X	✓
Examining shareholder return	X	✓	X	✓	✓
Research objective	Investigates the impact of CSI on firm value under external (environmental dynamism and competition intensity) and internal (firm capability).	Investigates the impact of monetary penalties from CSI on firm stock price crash risk	Investigates the role of media coverage in firms' CSR and CSI on cross-border acquisitions in BRICS countries.	Investigates the impact of CSI on firms' stock abnormal returns.	Investigates the impact of CSI on shareholder value in China across four different stakeholder groups (domains): shareholders, consumers, environment and employees
Theoretical framework for CSI	Instrumental stakeholder theory	Conflict Resolution hypothesis	Media coverage hypothesis	Institutional theory and Reputational risk	Stakeholder perspective of resource-based view (SRBV) and the stakeholder salience
Sample period (Region)	516 firms between 1996 and 2015 (US)	411 firms between 2003 and 2015 (US)	2588 firms between 1990 and 2011 (BRICS)	7368 firms between 2007 and 2017 (41 countries)	149 A-shares firms between 2006 and 2012 with 816 CSI episodes (China)
Model/method	Vector autoregressive with exogenous variables (VARX)	Autoregressive distributed lag (ARDL)	Match-pair and OLS regressions	Portfolio approach	Portfolio approach
Measures of CSI	KLD database	Asset4 database	RepRisk database	RepRisk database	RepRisk database
Summary of main results	Negative impact of CSI on firm value is longer and stronger for firms in high dynamism and more competitive markets and for firms with low capability.	Monetary penalties (CSI) are negatively related to the crash risk. Investors perceive monetary penalties from CSI as the end of uncertainty about firm's future performance.	Firms with CSI are less likely to complete cross-border deals and takes longer to complete than firms with no such coverage or with media coverage of CSR.	CSI media coverage significantly affects firms' reputational capital, measured by a significantly negative abnormal returns.	The adverse impact of CSI on shareholder returns is higher for the residual claimants' stakeholders. The adverse impact of CSI is significant across stakeholder salience (legitimacy, urgency and power).

maintenance of relationships between the firm and its key stakeholders who provide valuable resources to the firm.

The SRBV indicates that different stakeholders have different levels or degrees of bargaining power over economic claims of a firm's profits and these stakeholders can be categorized into two groups: fixed claimants and residual claimants. Barney (2018) indicates that the resource-based theory of profit generation must implicitly adopt a stakeholder perspective. Key stakeholders who control resources that create the most value in a bundle of co-specialized resources hold greater bargaining power over the firms' economic claims and therefore hold a residual claim instead of a fixed claim. This classification of stakeholders based on the bargaining power of firms' economic claims allows us to construct a novel stakeholder classification into fixed and residual claimants that is different from the traditional classification of fixed and residual claimants of firms' economic profits.

In examining the degree of value destruction from CSI, we argue that CSI which offended the stakeholder group(s) with higher bargaining power tends to have a more damaging impact on shareholder returns since those with higher bargaining power "can use their bargaining power to become residual claimants on the firm profits they help generate" (Barney, 2018, p.3306). Hinging on this definition of the residual claimants' bargaining power, we can go beyond the standard definition of the shareholder supremacy (which recognizes only the shareholder as the residual claimant group) and re-classify those stakeholders if they can use their bargaining power to become residual claimants.

Commencing on Barney's (2018) identification of the key stakeholder groups and with the consideration of potentially overlapping boundaries between fixed and residual claimants' stakeholders, we examine four key stakeholder groups (domains): shareholders (corporate governance), consumers (products), environment and employees. First, we identify the shareholders who provide the necessary capital to the firm. Corporate governance scandals, such as corruption, bribery, tax evasion, fraud and misleading communication will send negative signals to shareholders and other stakeholders. We argue that shareholders have the most profoundly impactful reactions to corporate governance scandals among all stakeholders since they will most likely either withdraw their investments or demand higher premiums (returns) to compensate for higher risk. As A-shares in Mainland China are mainly available for local investors and only Qualified Foreign Institutional Investors (QFII) have limited access to invest in A-shares, we argue that this unique market structure allows local shareholders to hold a relatively high bargaining power over the firms, and therefore can use their bargaining power to become residual claimants on the firm's profits. We also argue that shareholders have the highest interest in the well-being of the firm because their investment returns depend on the well-being of the firm.

Second, due to the abundant manufactured products with competitive prices in China, consumers hold relatively high economic bargaining power which makes it harder for Chinese companies to replace (substitute) their consumers once these consumers discover that the products have become unsafe or carry a great deal of risk (Clarke and Boersma, 2017; Jiang et al., 2009). The monopsony markets where suppliers rely heavily on their few large corporate customers (e.g., Apple, Amazon, Alibaba, etc.) make the consumers hold a relatively high economic bargaining power over the firms, and they can use their bargaining power to become residual claimants on the firm profits they helped generate. These large corporate customers also have a high interest in the wellbeing of their own firms since their own reputations also highly depend on the well-being of these suppliers. Non-corporate customers also have a high interest in the longevity of the firm since their ability to continue to consume the products depends on the well-being of the firm. Therefore, consumers are most likely to hold a relatively high level of residual claims.

Third, the environment cannot be assigned to one specific stakeholder group, and therefore it represents a variety of stakeholder groups

(community, natural resources, non-governmental organizations or NGOs, etc.). Research studies have also shown that this group of stakeholders holds less bargaining power due to a lack of uniformity for environmental regulations and community protections by local governments in China, such that it provides greater bargaining power towards the firm (e.g., Yang et al., 2018). More importantly, environment has less interest in the well-being of the firm since the environment may prefer the firm to cease its operations if it pollutes the environment. Thus, we consider this group of stakeholders (environment) to hold significantly lower residual claims over the firms' economic profits than the shareholders and the consumers, and we consider the environment to lean towards the fixed claimants group.

Finally, there is an abundant supply of labor (employees) in China. As the redundant workers caused by the privatisation reform of state-owned enterprises in the mid-1990s and the millions of migrant workers coming from the countryside, China hasn't had issues with the supply of cheap labor. The absence of an incentive pay for these lower-level workers makes the employee group have less interest in the well-being of the firm due to high voluntary employee turnover since their main objective is to search for a better job (Cheng et al., 2019). Unlike shareholders, consumers, and the environment, social norms and shared values toward employees in China also make this group of stakeholders hold the least bargaining power over the firm due to the abundant supply of labor and a relatively weak labor union (Fu, 2017; Périsset, 2017). Cheng et al. (2019, p.84) indicate that labor unions in China "lack independence and do not play a critical role in wage bargaining". Therefore, employees are less likely to be able to use their bargaining power to become residual claimants. Thus, based on the lowest bargaining power of the employees over the firms, we consider the employees also to lean towards fixed claimants.

Consistent with the SRBV argument that residual claimants hold more bargaining power and have a higher interest for the well-being of the firms, and therefore have greater economic claims over firms' profits and value creation than fixed claimants, we hypothesize based on the above reasoning as follows:

**Hypothesis 1:** *CSI that affects stakeholders with high bargaining power and interest in the firms' well-being has greater adverse effects on shareholder returns.*

## 2.2. Value relevance of CSI based on stakeholder salience

Mitchell et al. (1997) define stakeholder salience as the degree to which the firm prioritizes competing stakeholder claims. They explain that the stakeholder claims could be in a form of economic claims but also a moral or presumed claim. More specifically, Mitchell et al. (1997) urge that in examining the broad view of stakeholder salience, we need to identify the stakeholders with the moral (presumed) claim because stakeholders with this claim can also influence the firms' license to operate, survival, and competitive advantage. Mitchell et al. (1997, p.854) argue that in determining "who and what really counts," the firm must pay attention to all three of these categories: "the stakeholders' power to influence the firm, the legitimacy of the stakeholders' relationship with the firm and the urgency of the stakeholders' claim".

When CSI offends stakeholders who hold a high legitimacy, they can take away the firms' legitimacy (legal rights, moral rights, moral interests, etc.) to operate. Stakeholders with high urgency could bring serious adverse media attention to the firm. When CSI offends stakeholders who hold a high power, they could potentially use their power to adversely influence resources (Pfeffer and Salancik, 1978) and increase transaction costs (Williamson, 1979) to bring about the firms' outcomes that they desire. Thus, CSI that adversely affects these three stakeholder salience categories is expected to have adverse effects on firms' shareholder returns.

We apply Mitchell et al.'s (1997) typology of the stakeholder salience to explain the value relevance of CSI through operationalizing the stakeholders' legitimacy, urgency and power in China. First, we argue

that in the context of CSI, the legitimacy of a claim on a firm depends on the firm's "legal title, legal right, moral right, at-risk status, or moral interest" (Agle et al., 1999, p.508; Mitchell et al., 1997, p.862). Based on social norms, the Chinese government holds relatively high legal authority over corporations. The government represents the stakeholder group who holds a high *legitimacy claim*. We identify the government concern as our measure of the *stakeholder legitimacy claim*. The Chinese government holds the legitimacy power to take away the firm's legal right to operate. Therefore, when the firm's CSI is identified by the government, the firm faces the risk of losing its legal right to operate. Hence, CSI published by the Chinese government daily publications brings an adverse impact on the firm's stock prices.

Second, the urgency of the stakeholder salience calls for immediate (pressing) attention by the firm. In the context of CSI, urgency represents the time-sensitive issues that require immediate (timely) attention by the firm. While extant literature has argued that the urgency is "irksome but not dangerous" (Mitchell et al., 1997, p.875), recent studies have shown that the stakeholder urgency from the negative news media of CSI undermines the firms' social legitimacy (as opposed to legal legitimacy) to operate (Harjoto et al., 2021; Hawn, 2021; Kölbel et al., 2017). Increasing public negative sentiments on the news media coverage of CSI over time can become increasingly harsh if the firm does not address the issue immediately. The stakeholders' dissatisfactions further fuel the news media to strengthen their interpretive frame which influences the stakeholders' attributions to increase the blame on the firm for its irresponsible actions (Lange and Washburn, 2012) in such that the firms can lose their social license to operate as indicated in the Iron Law of corporate social responsibility (Davis, 1967). The media coverage elevates the urgency into the social legitimacy to operate and intensifies the value relevance of CSI (Kölbel et al., 2017) such that the urgency is no longer just "mosquitoes buzzing the managers' ears".

Third, the power represents the stakeholder power to influence the firm's behavior. In the media agenda setting literature, the firm's ability to manage stakeholder opinions is one of the critical elements in managing social complexity. As we are living in the digital news media, the spread of negative news from CSI (once it is covered by the prominent news media outside of China) elevates the stakeholder power to influence the firm's economic profit. When the firm is unable to manage the stakeholder opinions, then the firm's CSI episode becomes a media feeding frenzy or a news scandal (e.g., the news of melamine contamination in milk products was eventually covered by multiple prominent news media) as a manifestation of the media agenda setting effect (Tang and Tang, 2016). During a media feeding frenzy, stakeholders are gaining more power to influence the firm's behavior because prominent news media with a powerful reach and wide audiences (e.g., the New York Times, the Guardian, the Economist, etc.) allow stakeholders to instantly gain support from stakeholder groups across different regions and countries around the globe. We hereby argue that higher source reach (media prominence) allows the stakeholders to gain power due to increasing public support from other stakeholder groups to demand the firm to change its irresponsible behavior.

Based on Mitchell et al.'s (1997) typology of stakeholder salience (i.e., legitimacy, urgency and power), we hypothesize that CSI has a stronger value relevance to the firm's shareholders when CSI action violates the stakeholders with high legitimacy, urgency and power in China. We form our second hypothesis as following:

**H2a:** *CSI that affects stakeholders with high legitimacy has stronger adverse effects on shareholder returns.*

**H2b:** *CSI that affects stakeholders with high urgency has stronger adverse effects on shareholder returns.*

**H2c:** *CSI that affects stakeholders with high power has stronger adverse effects on shareholder returns.*

### 3. Data and sample selection

To measure CSI, we obtained a one-time only access to RepRisk's

firm-level data which differs from the RepRisk's Index data since it provides curated detailed data based on daily scanning (radar) of negative media coverage on environmental, social and governance (ESG) risks.<sup>1</sup> RepRisk records media coverage in 20 different languages for more than 80,000 listed and unlisted companies, and it is managed, checked, and verified by highly-trained analyst team members – the scope of coverage is hardly curatable by a single researcher. The RepRisk database has been used by a number of researchers who have found the dataset to be robust and rigorously constructed (Breitinger and Bonardi, 2017; Kölbel et al., 2017).

The RepRisk news data is derived from the news information provided by independent third parties, including international and local media, government sites, NGOs, newsletters, social media and blogs. Once companies are exposed to negative and controversial news, RepRisk records the report date, company information, news source name, issue type, and rates the severity and the source reach (i.e. prominence) of the news source. Severity indicates the strength and type of episode or accusation, and its extent and consequences for the environment or people. RepRisk uses a score of "1", "2", and "3" to represent low, medium and high severity, respectively. The source reach rating is a measure of the influence of the source. The higher the rating, the more influential the source is considered to be with the public and decision-makers. RepRisk uses a score of "1", "2", and "3" to indicate that the news is reported by local media (or national NGO), national-level media (or major NGO), and international source (or top source), respectively. If multiple sources report the same news on the same day, only the source with the highest reach is recorded.

In addition to the severity and source reach of the news to represent the urgency and power of the stakeholder salience, we also manually collect the data on government concerns from the Chinese government official website to represent the legitimacy of the stakeholder salience.<sup>2</sup> The collected data contains Chinese government daily publications, ranging from June 2005 to July 2012 and comprises a total of 56,503 articles in Chinese.<sup>3</sup> We translate all the RepRisk identified categories of issues (listed in Table 2) to Chinese and use content analysis method to investigate how the Chinese government announcements related to CSI issues. We count each Chinese translated terms among all the collected announcement data by using "1" to represent if the Chinese translated terms existed in the announcements, and using "0" to represent the opposite, then we rank the issues according to the number of counts (see Appendix A in Harjoto, Hoepner and Li (2021))<sup>4</sup>. If the number of counts is higher, it means that a particular issue is of greater concern to the Chinese government. The government concern data was chosen one year ahead of the end of sample period as we can measure how much power government announcements have in the current month in relation to the previous twelve months. We restructure the government concern index data based on the following equation. This equation is a measurement of the annualized government concern of current month compared to the

<sup>1</sup> RepRisk is an independent company that monitors companies' and projects' exposure to ESG risks. For more information, please visit <http://www.reprisk.com> and <https://www.reprisk.com/our-approach#research-approach>. The independence and objectivity of RepRisk is evident since RepRisk is the inaugural signatory of the Deep Data Delivery Standards ([www.DeepData.ai](http://www.DeepData.ai)).

<sup>2</sup> This study uses the daily number of publications, announcements and news releases published by the State Council Information Office of the People's Republic of China (SCIO) (website: <http://www.scio.gov.cn/>). The SCIO is the official government website established in January 1991. The search results comprise all the data published by SCIO, and each search result contains a headline and full article content for the announcement.

<sup>3</sup> We collected the Chinese government daily publications from January 1999 and selected June 2005 as one year ahead of the availability of RepRisk data to construct the government concern index as in equation (1). In the selected articles, around 10% of the articles are abstracts only.

<sup>4</sup> Appendix A is provided in the working paper version on the SSRN website: [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=3241981](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3241981).

**Table 2**  
CSI domains.

Domains	Issues	Impact on primary stakeholders	Impact on resource categories	Studies from the resource perspective
Corporate governance	Corruption, bribery, extortion, money laundering, executive compensation, misleading communication, corporate frauds, tax evasions, Anti-competitive practices	Shareholders (residual claimants)	Financial capital resources inputs (e.g. investors' interests and engagements)	Muttakin et al. (2018); Cuervo-Cazurra (2016)
Product	Controversial products and services Product-related health and environmental issues	Consumers (residual claimants)	Revenue generation, purchasing decision (e.g. customers' wellbeing)	Brown and Dacin (1997); Wang and Sengupta (2016)
Environment	Global pollution and climate change Local pollution Impacts on ecosystems and landscapes Overuse and wasting of resources Waste issues Animal mistreatment	Local community and/or environmental NGOs (fixed claimants)	Physical capital and natural resources inputs (e.g. firms' plant, equipment and environment)	Ramanathan (2018); Brulhart et al. (2017)
Employee relations	Forced labor Child labor Freedom of association and collect bargaining Discrimination in employment Health and safety issues Poor employment conditions	Employees (fixed claimants)	Human capital resources inputs (e.g. employees' training, skills and relationships)	Riley et al. (2017); Wang et al. (2009)

Note: This table presents the RepRisk CSI domains covered in this study. The first column shows the categories of CSI domains applied in the portfolio. The second column details the specific issues in the specific category. Drawing upon insights from resource-based theory, the third column presents the impact of CSI on key resources categories as developed in Barney (1991, 2018). All principles of the UN Global Compact are addressed.

previous 12 months. The unit-root tests indicate that equation (1) is stationary.

$$GC = \frac{12x_i}{\sum_{n=1}^{12} x_{i-n}} \quad (1)$$

When we accessed RepRisk, the news data was categorized into 27 CSI episodes. We select episodes that can be further categorized into several domains (stakeholder groups) such as environment, shareholders (corporate governance), employee relations and consumers (products).<sup>5</sup> Table 2 presents the impact of CSI domains on key resource categories that are consistent with Barney's (2018) stakeholder resource-based view.

We use all Chinese A-shares companies with news records in the RepRisk database from June 2006 to July 2012. A-shares are shares denominated in Chinese Yuan and listed on either the Shenzhen Stock Exchange or Shanghai Stock Exchange (Carpenter and Whitelaw, 2017). To avoid survival bias, we include firms that ceased to exist before July 2012. We remove American Depository Receipts (ADRs) and shares listed outside of Mainland China and Hong Kong from the sample. Our final sample consists of 149 A-shares Chinese companies that experienced 517 CSI events from June 2006 to July 2012. Table 3 provides the distribution for our sample. Panel A of Table 3 shows the number of news and CSI episodes considered in each year. Because one event can violate multiple CSI issues, we examine 517 events involving one or more Chinese firms and 816 CSI episodes. Table 3 shows that fewer news items were available in 2006. We begin the sample period in June 2006 because that is the earliest year when news data is available in the

<sup>5</sup> The types of CSI issues were selected and defined in accordance with the key international standards, such as the World Bank Group Environmental, Health, and Safety Guidelines, the IFC Performance Standards, the Equator Principles, the OECD Guidelines for Multinational Enterprises, the ILO Conventions, and more. A full list of international standards used in the RepRisk database can be found at: [www.reprisk.com/repriskscope/](http://www.reprisk.com/repriskscope/).

**Table 3**  
Sample distribution.

Panel A: Sample distribution of news and CSI episodes across years		
Year	Number of news	Number of episodes
2006	8	12
2007	52	70
2008	85	128
2009	72	127
2010	88	155
2011	128	196
2012	84	128
<b>Total</b>	<b>517</b>	<b>816</b>
Panel B: Sample Distribution of companies with CSI episodes across sectors		
Industry code	Industry categories	Company count
10	Energy	3
15	Materials	53
20	Industrials	25
25	Consumer discretionary	9
30	Consumer staples	20
35	Health care	10
40	Financials	14
45	Information technology	5
55	Utilities	9
<b>Total</b>		<b>149</b>

Note: Panel A reports the number of CSI news and relevant number of CSI episodes considered in each year of the sample period. Please note that one single news may involve several companies and hence several episodes. There are 517 news and 816 CSI episodes in the final sample. Panel B shows the sample distribution of 149 Chinese companies across the Global Industry Classification Standard (GICS) sectors.

RepRisk dataset. Panel B of Table 3 reports the sample distribution of 149 Chinese companies across various sectors. The industry classification based on the Global Industry Classification Standard (GICS) shows that the materials and industrials sectors have the highest number of

sample firms while energy and information technology sectors have the least number of firms. The sample distribution of companies with CSI episodes across sectors shows a reasonably well spread distribution.

#### 4. Methodology

##### 4.1. Calendar time portfolio approach

As the focus of this paper is specifically on the impact of CSI episodes on shareholder value, we use the *calendar time portfolio approach* originally developed by Jaffe (1974) and Mandelker (1974). Lyon et al. (1999) identify two general event study approaches for testing long-run abnormal stock returns: the traditional “per event” study framework with buy-and-hold abnormal returns for each event and the calendar-time portfolio approach that updates portfolios as new events arise.<sup>6</sup> The traditional per-event framework struggles with overlapping news and tends to experience a poorer fit of relevant asset pricing models (Fama, 1998; Mitchell and Stafford, 2000). Therefore, we use the standard calendar-time portfolio approach following Jegadeesh and Titman (1993) and Fama (1998) to detect long-run abnormal stock returns.

The approach assumes investors rebalance the portfolio on a monthly basis. Investors include firms in the portfolio if the firm experienced events in the previous month, and calculate portfolio monthly returns based on equal-weighted or value-weighted method. Then, investors employ the portfolio returns as the dependent variable in the asset pricing models to obtain alpha, which is the intercept of the model to indicate abnormal returns. This method has been widely used in extant studies, such as Fama (1998), Lyon et al. (1999), Chan (2003), Fang and Peress (2009), and Hillert et al. (2014). This process is also consistent with CSR-related studies using the calendar time portfolio approach (e.g., Deng et al., 2013; Eccles et al., 2014; Edmans, 2011; Kempf and Osthoff, 2007). The advantage of the calendar-time portfolio approach is that it can solve the potential limitations with the event-time portfolio approach such as overlapping returns (Mitchell and Stafford, 2000). The ability to integrate events that can occur on any day of the year seamlessly into calendar time is also the advantage of our approach over the standard multivariate panel regressions approach commonly applied to annual data.

Following Fama (1998), we form monthly value-weighted portfolios of companies for a 74-month period from June 2006 to July 2012. In order to develop a test for the severity and the source reach of news characteristics in the portfolio construction, we track post-news monthly returns for a specific time period, which is dependent on the severity and source reach of the episodes. We apply variable holding periods of 6, 12, 18, and 24 months to our portfolios for each CSI dimension, for companies with aggregated severity score of four levels: 1, 2, 3, and higher than 3, respectively. A higher severity level of CSI episode corresponds to a longer holding period in our portfolio. For example, a CSI episode recorded with a severity score of 1 in a given month will be included in the CSI portfolio and held for 6 months. If no further episodes arise during this 6-month holding period, the company’s stock will be excluded from the portfolio once the period is completed. If a new CSI episode arises during the holding period, the holding period will be reset and a new length of holding period will be determined by the aggregated severity score. The maximum 24 months holding period is chosen based on Chan (2003) who shows that long-run returns exhibit a reversal

<sup>6</sup> As the news data reported by RepRisk may be reported with a time lag of up to 48 h from the occurrence of the actual event, this possible time lag could cause ambiguity, inaccuracy, and confounding outcomes if we use the traditional short-term event study method (e.g., Kruger, 2015; Wang et al., 2011). Hence, measuring the short-term effects of news coverage is confounded by other non-CSI events because the exact timing of the CSI event is unknown. Our approach is consistent with other studies that used RepRisk data (Breitinger and Bonardi, 2017; Kölbel et al., 2017).

around the two-year mark. Compared to short-term event studies with short event windows, we consider that 24 months holding period provides a long-term view on shareholder value. Since the news is not reported at the same time across all the companies, those included in the portfolios are not constant over the sample period. Consequently, each month, the portfolios are rebalanced. Because government announcements are less likely to be firm-specific, we add the government dummy variable into the regression equation (2) below to consider the effect of higher-level government concern.

In order to have a comparable benchmark for shareholder value performance of our sample companies, we also create a non-CSI portfolio for each CSI portfolio including all the stocks in the sample that experienced a CSI episode in the respective domain but are not in the respective CSI portfolio at the specific point in time. Simply speaking, each company is compared with itself during periods when there is news coverage and periods when there is no news coverage. Using this method, we can measure the financial returns for companies exposed to harmful CSI episodes (*CSI portfolios*) and compare them to periods when the same companies are not exposed to harmful CSI episodes (*Non-CSI portfolios*).

##### 4.2. Regression model of the shareholder value effects

The monthly portfolio excess returns are calculated and regressed using Fama and French (1993) three-factor and Carhart (1997) four-factor models. Each month, we calculate the portfolio returns based on the captured monthly returns across all securities in the sample portfolio. Since many Chinese companies are heavy exporters into global markets, national market-based models may not fully capture the market exposure beyond the domestic level. Therefore, we extend the Carhart four-factor model (Carhart extended model) to account for the market exposure at regional and global levels (Hoepner et al., 2011). The extended Carhart regression equation (2) is specified as:

$$r_{xp,t} = \alpha_p + \beta_{nat,p}r_{nat,t} + \beta_{reg,p}r_{xreg,t} + \beta_{glo,p}r_{xglo,t} + \gamma_{nat,p}SMB_{nat,t} + \delta_{nat,p}HML_{nat,t} + \lambda_{nat,p}MOM_{nat,t} + \epsilon_{p,t} \tag{2}$$

where  $r_{xp,t}$  represents the excess return of the portfolio  $p$  and the broad market over the risk-free asset return.  $\alpha_p$  denotes Jensen (1968) alpha.  $\beta_{nat,p}$ ,  $\beta_{reg,p}$ ,  $\beta_{glo,p}$  are the portfolio’s systematic exposure to the broad market portfolio at a national, regional and global level.  $r_{xnat,t}$ ,  $r_{xreg,t}$ ,  $r_{xglo,t}$  represent the market benchmark’s excess return at national, regional, and global level. The size factor  $SMB_{nat,t}$ , the value factor  $HML_{nat,t}$  and the momentum factor  $MOM_{nat,t}$  are the same as the Carhart (1997) four-factor model.  $\epsilon_{it}$  represents the error term.

To test the effect of government announcements and regulations on the impact of CSI issues on financial performance, we add the government factor into the following regression equation (3):

$$r_{xp,t} = \alpha_p + \beta_{nat,p}r_{nat,t} + \beta_{reg,p}r_{xreg,t} + \beta_{glo,p}r_{xglo,t} + \gamma_{nat,p}SMB_{nat,t} + \delta_{nat,p}HML_{nat,t} + \lambda_{nat,p}MOM_{nat,t} + \theta_{h,p}GOV_{nat,t} + \epsilon_{p,t} \tag{3}$$

where  $GOV_{nat,t}$  represents a dummy for government concern based on the issues as listed in Appendix A. For each considered CSI domain, we use “1” to represent if the government concerns of current month are higher than the average of previous 12 months on a specific issue, and use “0” to represent the opposite.

All factors are value-weighted and one month lagged. The excess market return is the market return minus the risk-free rate obtained from Datastream. We use Chinese central bank three-month bills as the national risk-free rate. We use Japan three-month interbank and three-month US Treasury Bills as proxies for the regional and global risk-free rate, respectively. For the national-level market benchmark, we construct a value-weighted market benchmark that exactly matches our

sample firms at each given point in time. This benchmark has the advantage that the performance of CSI and non-CSI portfolios have the same biases (if any) and are clean antidotes of each other. For the A-shares portfolios, no matter in which issue category, the market return is derived from the value-weighted monthly returns of all the A-shares in the sample. Compared to the characteristic-adjusted benchmark used by Daniel et al. (1997), this benchmark can conservatively control for any company- or industry-specific risks that are not captured in the model. For the regional-level market benchmark, we construct a value-weighted benchmark based on index tracked firms from 12 Asian countries including Japan, Hong Kong, Singapore, China, Indonesia, India, Malaysia, Pakistan, Philippines, Korea (South), Taiwan and Thailand. For the international-level market benchmark, we construct a value-weighted benchmark based on index tracked firms from 64 countries from the MSCI All Country World Index. The list of countries is available by request.

## 5. Empirical results

### 5.1. Value relevance of CSI for residual and fixed claimants

Table 4 shows the results of the impact of CSI episodes on risk adjusted shareholder returns by using three different asset pricing models: Fama and French (1993) three-factor model, Carhart (1997) four-factor model and Carhart extended model (Hoepner et al., 2011). Using calendar time portfolio approach, Panel A displays the results of the CSI portfolios constructed by news coverage periods. We evaluate holding periods of 6, 12, 18, and 24 months after the CSI news was recorded by RepRisk.

Based on the Carhart extended model, we find that the portfolios of firms that violated the relationship with the shareholders (corporate governance) and customers (product) have significantly negative abnormal returns (alpha) of  $-1.6\%$  ( $SE = 0.005, p = .002$ ) and  $-1.8\%$  ( $SE = 0.007, p = .011$ ), respectively. These findings indicate that both shareholders and consumers are considered as the stakeholder groups who hold residual claims and hold relatively high bargaining power over the firms. We also find that the portfolio of firms that violated the environment has a negative abnormal return ( $\alpha = -0.5\%$ ,  $SE = 0.003, p = .075$ ), which is marginally significant and the magnitude of this alpha is less than one-third of the alphas for the shareholders and consumers portfolios. This indicates that the environment represents the stakeholder group with less residual claims relative to the shareholders and consumers. Finally, we find that a portfolio of firms with CSI episodes that offend the employees does not generate a significantly lower abnormal return ( $\alpha = -0.6\%$ ,  $SE = 0.005, p = .232$ ). Therefore, this group of stakeholders (employees) hold a fixed claim.

Panel A also shows that the regional market exposures statistically significantly explain the CSI portfolios excess returns. This indicates that controlling for regional market exposures improves our regression estimations. Previous studies that examine long-run abnormal return models generally show high adjusted R-squared statistics of 0.8 or higher (e.g., Chan, 2003; Hoepner et al., 2011; Kempf & Osthoff, 2007). We find that the extended Carhart (1997) model has similar or higher adjusted R-squared statistics compared to other models, which suggest that extended market exposure does a better job in explaining excess returns. Thus, from here on, we only present the results from the extended Carhart model.

Panel B presents the results of non-CSI portfolios for no-news coverage periods. All of the abnormal returns in the non-CSI portfolios are insignificant. This indicates that the market does not punish firms that are not found to have CSI episodes.

Our overall findings support our first hypothesis (H1) that CSI that destroys the firm's relationship with the stakeholder groups that hold high bargaining power, thus considered as the residual claimants (consumers and shareholders), brought greater adverse impact on shareholder returns than CSI that destroys the relationships with stakeholders

who holds fixed claims (environmental and employees). The empirical evidence supports Barney's (2018) stakeholder resource-based view (SRBV) that the strength of the claims of a stakeholder group depends on whether the stakeholder groups' claims are residual or fixed. First, because of the oligopsony (monopsony) market structure for Chinese companies (Clarke and Boersma, 2017; Jiang et al., 2009), CSI that offended the consumer (product-related CSI episodes) bring the most value destruction to long-term shareholder return. Second, the shareholders (investors) of the A-shares firms are not easily substituted with foreign investors and therefore they also hold a relatively higher bargaining power over the firms. Third, since the environment is associated with various stakeholder groups (community, natural resource, NGOs, local governments, etc.), environment as a stakeholder group resembles the fixed claimants. Finally, since companies hold significantly higher bargaining power over their employees, these stakeholders are considered as fixed claimants for which CSI episodes bring no impact on the shareholder returns.

### 5.2. Value relevance of CSI based on the stakeholder salience

We further examine the impact of CSI on shareholders' returns across three different typologies based on the stakeholder salience (Mitchell et al., 1997). Table 5 displays the risk-adjusted abnormal returns of the core results from Table 4 as a comparison and the results when CSI offended the stakeholder legitimacy (high government concerns), urgency (high severity) and power (high source reach). The second column of Table 5 shows that a portfolio of firms with CSI that offended the government (high legitimacy) produces significantly  $-2.3\%$  ( $SE = 0.009, p = .014$ ) and significantly  $-2.6\%$  ( $SE = 0.013, p = .046$ ) monthly abnormal returns for the shareholders and consumers group, respectively. In contrast, portfolios of stocks for firms with CSI that violated the environment and employees do not have significantly lower abnormal returns. The magnitudes of alphas for shareholders and consumers with a high legitimate concern is stronger (i.e., more negative) than the core results in Table 4. Thus, we find evidence to support H2a, which indicates CSI episodes that offended the concerns of stakeholder with higher legitimacy more adversely affect returns, especially for the shareholders and customers.

The third column of Table 5 shows that a portfolio of stocks for firms with CSI that offended the stakeholder with higher urgency (high severity) produces significantly  $-1.6\%$  ( $SE = 0.005, p = .004$ ) and significantly  $-1.9\%$  ( $SE = 0.007, p = .010$ ) monthly abnormal returns for the shareholders and consumers group, respectively. We find CSI that offended the employees is experiencing significantly  $-1.6\%$  ( $SE = 0.006, p = .014$ ) monthly abnormal returns while CSI that offended the environment is only experiencing marginally significant  $-0.5\%$  ( $SE = 0.003, p = .069$ ) abnormal negative returns. Based on the magnitudes of the alphas, we find that CSI episodes bring significantly more negative abnormal returns when CSI offended more urgent employee-related issues compared to the core results in the first column. Thus, we find evidence to support H2b which CSI violated the relationship with high stakeholder urgency adversely affects the shareholder returns, especially for the employees.

The fourth column of Table 5 shows similar results that a portfolio of firms offended the stakeholder group who holds a high power (high source reach) produces significantly  $-1.6\%$  ( $SE = 0.005, p = .003$ ) and significantly  $-2.3\%$  ( $SE = 0.008, p = .006$ ) monthly abnormal returns for the shareholders and consumers group, respectively. CSI that offended the environment experiences significantly  $-0.5\%$  ( $SE = 0.003, p = .078$ ) monthly abnormal returns but again the statistical significance and the economic magnitude of alpha is lower than shareholders and consumers groups. In contrast, the portfolio of firms with CSI that violated the employees does not have significantly lower abnormal returns. Based on the alphas, we find that CSI that violated powerful customer claims brings significantly more severe negative abnormal returns compared to the core results in the first column. Thus, we find



**Table 4**  
The domains of CSI episodes and shareholder value.

	Intercept	Market exposures			SMB	HML	MOM	Adj. R2
	$\alpha$	$\beta_{nat}$	$\beta_{reg}$	$\beta_{glo}$	$\gamma_{nat}$	$\delta_{nat}$	$\lambda_{nat}$	
<i>Panel A: CSI portfolios</i>								
<i>Residual Claim Stakeholders</i>								
<i>Shareholders (Corp. Gov)</i>								
FF 3-Factor	-0.017*** (0.005)	0.804*** (0.064)			0.177** (0.084)	0.319*** (0.104)		0.856
Carhart 4-Factor	-0.016*** (0.005)	0.802*** (0.064)			0.162** (0.075)	0.360*** (0.112)	0.084 (0.071)	0.857
Carhart extended	-0.016*** (0.005)	0.803*** (0.064)	0.003 (0.059)	0.068 (0.159)	0.166* (0.084)	0.352*** (0.109)	0.082 (0.073)	0.852
<i>Customers (Product)</i>								
FF 3-Factor	-0.020*** (0.007)	0.662*** (0.082)			0.689*** (0.152)	0.743*** (0.227)		0.688
Carhart 4-Factor	-0.019*** (0.007)	0.659*** (0.083)			0.661*** (0.144)	0.796*** (0.226)	0.137 (0.148)	0.689
Carhart extended	-0.018** (0.007)	0.658*** (0.074)	0.210** (0.095)	-0.440 (0.330)	0.659*** (0.140)	0.800*** (0.208)	0.147 (0.149)	0.695
<i>Fixed Claim Stakeholders</i>								
<i>Environment</i>								
FF 3-Factor	-0.005** (0.003)	0.969*** (0.039)			0.033 (0.068)	0.527*** (0.176)		0.900
Carhart 4-Factor	-0.005* (0.003)	0.966*** (0.038)			0.022 (0.064)	0.547*** (0.187)	0.052 (0.063)	0.899
Carhart extended	-0.005* (0.003)	0.977*** (0.042)	-0.150** (0.065)	0.089 (0.188)	0.001 (0.063)	0.547*** (0.192)	0.052 (0.069)	0.901
<i>Employees</i>								
FF 3-Factor	-0.006 (0.005)	0.926*** (0.060)			-0.057 (0.109)	0.651*** (0.161)		0.773
Carhart 4-Factor	-0.006 (0.005)	0.926*** (0.060)			-0.057 (0.106)	0.651*** (0.175)	-0.000 (0.107)	0.770
Carhart extended	-0.006 (0.005)	0.925*** (0.061)	-0.048 (0.087)	-0.189 (0.211)	-0.078 (0.107)	0.674*** (0.174)	0.009 (0.110)	0.764
	Intercept	Market exposures			SMB	HML	MOM	Adj. R2
	$\alpha$	$\beta_{nat}$	$\beta_{reg}$	$\beta_{glo}$	$\gamma_{nat}$	$\delta_{nat}$	$\lambda_{nat}$	
<i>Panel B: Non-CSI portfolios</i>								
<i>Residual claim stakeholders</i>								
<i>Shareholders (Corp. Gov)</i>								
Carhart extended	0.003 (0.002)	1.011*** (0.036)	-0.024 (0.053)	-0.226 (0.197)	0.038 (0.048)	0.033 (0.042)	-0.051 (0.044)	0.852
<i>Customers (Product)</i>								
Carhart extended	-0.001 (0.002)	1.010*** (0.020)	-0.044 (0.041)	0.237*** (0.088)	-0.027 (0.042)	-0.112 (0.082)	-0.047 (0.037)	0.695
<i>Fixed claim stakeholders</i>								
<i>Environment</i>								
Carhart extended	0.005 (0.003)	1.114*** (0.037)	0.135** (0.058)	-0.188 (0.131)	-0.012 (0.088)	-0.240*** (0.073)	-0.018 (0.094)	0.901
<i>Employees</i>								
Carhart extended	-0.001 (0.002)	1.002*** (0.025)	-0.011 (0.049)	0.182 (0.117)	-0.027 (0.061)	-0.182*** (0.058)	-0.066 (0.072)	0.764

Note: Table 4 presents the risk-adjusted performance of the Chinese A-share companies involved in negative CSI episodes. Details of different CSI episodes are described in Table 2. Panel A shows the results of CSI portfolios including companies with the different domains of CSI episodes on three versions of asset pricing models. Panel B shows the results of non-CSI portfolios on the Carhart extended model only. The non-CSI portfolios including all the stocks in the sample which are at the respective point in time not in the respective CSI portfolio. Each portfolio includes CSI episodes on all severity levels. We hold the portfolios for 6, 12, 18, and 24 months after the CSI news was recorded by RepRisk. Unless specifically noted, all portfolios in this study are value-weighted. The market return is derived from the value-weighted portfolio of all the A-shares in the sample. Column two lists monthly abnormal returns or Jensen alpha (Jensen, 1968). Column three, four and five show market risk exposure on national, regional and global level, respectively. The next three columns present the estimated coefficients of the SMB (small cap), HML (value), and MOM (momentum) investment style benchmark factors. Negative coefficients imply exposure to the respective opposite investment styles, which are large cap, growth, and contrarian, respectively. The last column shows the adjusted R squared statistics. As the sample period is from June 2006 to July 2012, the observed monthly regressions are 73. Standard errors are in parentheses. For the remaining results, coefficient covariance and standard errors are made heteroskedasticity and autocorrelation consistent based on the Newey and West (1987) method. \*, \*\*, and \*\*\* indicate significance at the 10%, 5%, and 1% levels, respectively.

**Table 5**  
Abnormal returns of portfolios based on characteristics of CSI episodes.

	Core results	Legitimacy (government)		Urgency (high severity)	Power (high source reach)
	Intercept $\alpha$	Intercept $\alpha$	Intercept $\alpha$		Intercept $\alpha$
<i>Panel A: CSI portfolios</i>					
<i>Residual claim stakeholders</i>					
Shareholders (corp. gov)	−0.016*** (0.005)	−0.023** (0.009)	−0.016*** (0.005)		−0.016*** (0.005)
Customers (product)	−0.018** (0.007)	−0.026** (0.013)	−0.019*** (0.007)		−0.023*** (0.008)
<i>Fixed claim stakeholders</i>					
Environment	−0.005* (0.003)	0.001 (0.007)	−0.005* (0.003)		−0.005* (0.003)
Employees	−0.006 (0.005)	−0.004 (0.011)	−0.016** (0.006)		−0.006 (0.007)
<i>Panel B: Non-CSI portfolios</i>					
<i>Residual claim stakeholders</i>					
Shareholders (corp. gov)	0.003 (0.003)	0.006 (0.004)	0.000 (0.002)		0.001 (0.002)
Customers (product)	−0.001 (0.002)	0.002 (0.004)	−0.006 (0.004)		−0.003 (0.003)
<i>Fixed claim stakeholders</i>					
Environment	0.005 (0.003)	−0.001 (0.009)	0.002 (0.005)		0.005 (0.003)
Employees	−0.001 (0.002)	−0.000 (0.004)	0.000 (0.001)		−0.003 (0.003)

Note: The table presents the monthly regressions of abnormal returns to four news characteristics portfolio on the Carhart extended model. Only monthly abnormal returns or Jensen alpha (Jensen, 1968) are reported, more detailed results are available by request. The core results are presented in Column 2 for comparison. The next three columns show monthly abnormal returns of portfolios which consist of news with government concern, at higher severity level and source research level. Details of screening methodology can be found in the Data and Sample Selection section. Panel A shows the results of CSI portfolios including companies with the different dimensions of CSI episodes. Panel B shows the results of non-CSI portfolios including all the stocks in the sample which are at the respective point in time not in the respective CSI portfolio. Each CSI characteristics portfolio excludes CSI episodes on characteristic level of one. We hold the portfolios for 12, 18, and 24 months according to the aggregated characteristic level of 2, 3, and higher than 3, respectively. The market return is derived from the value-weighted portfolio of all the A shares in the sample. All portfolios are value-weighted. As the sample period is from June 2006 to July 2012, the observed monthly regressions are 73. Standard errors are in parentheses. Coefficient covariance and standard errors are made heteroskedasticity and autocorrelation consistent based on the Newey and West (1987) method. \*, \*\*, and \*\*\* indicate significance at the 10%, 5%, and 1% levels, respectively.

evidence to support H2c which CSI exposed by more powerful media sources adversely affects shareholder returns, especially for the customers.

Overall, we find empirical evidence to support the typology of the stakeholder salience: legitimacy, urgency and power (Mitchell et al., 1997). More importantly, the results indicate that the significant effect of CSI across fixed and residual claimants, defined from Barney (2018), still hold across different stakeholder salience. We also find that the impact of CSI on shareholder and customers returns are more negative for those with high legitimate concerns, significantly more negative for employee issues with highly urgent claims and significantly more negative for customer claims with high power. These findings bring new nuances of value relevance for CSI across stakeholder claims of varying salience.

### 5.3. Robustness tests

We conduct several robustness tests to check the consistency of our empirical results. First, we use equally-weighted portfolio returns based on the same sample companies as used in the core results. Table 6 shows robust evidence of a significant underperformance of portfolios related to CSI that offended the residual claimant group, i.e., shareholders and consumers relative to CSI that offended the fixed claimant group, i.e., environment and employees.

Second, scholars have recognized the firm's size effect on long-run abnormal stock returns (e.g., Barber and Lyon, 1997). Large companies normally have more media exposure than small companies (Strike et al., 2006; Walker, Zhang and Ni, 2008). Therefore, larger firms may dominate the returns in the CSI portfolios. Therefore, we divide the sample by using the median market capitalization as the breakpoint and exclude small companies in both the CSI portfolios and the non-CSI

portfolios. Table 6 shows that company size portfolios remain similar to the core results presented in Table 4.

Third, Reporters Without Borders' 2017 World Press Freedom Index ranks China 176th out of 180 countries. As press freedom in China is low, we are concerned that firms favored by the Chinese Communist Party (CCP) or politically connected firms would not have been targeted by negative media campaigns. Based on these concerns, we exclude news from all Chinese media agencies in the portfolio construction process. The "Exclude Chinese Media" portfolios in Table 6 produce similar results to the core results presented in Table 4, except that the environment becomes insignificant, which further confirms that the environment resembles the fixed claimants rather than the residual claimants.

Fourth, we conduct additional results based on the novelty level of the reported news. Novelty rating describes how new and thus salient the presented news on a given topic is, and whether the company, project or government has been criticized on this topic before. Novelty is assessed based on the question if a similar event has been reported previously, since investors are likely to treat new information and old information differently (Boudoukh, et al., 2013). For instance, Tetlock (2011) finds that firm's stock returns respond less to stale (i.e. less novel) news. As there are multiple sources of news reported for each event, we further examine if the results will be different if we only keep the first reported (novel) news. The results from the "Novelty of Events" portfolios are consistent with our main results.

Fifth, Lyon, Barber and Tsai (1999) identify two general event study approaches for testing long-run abnormal stock returns: the traditional "per event" study framework with buy-and-hold abnormal returns for each event, and the calendar-time portfolio approach, which updates portfolios as new events arise. We focus on the calendar-time portfolio approach in this paper and also test if using the method of 12 months

**Table 6**  
Robustness tests.

	Core results	Equal weighted	Company size	Exclude Chinese media	Novelty of Events	Buy-and-Hold 12 Months	Consumer Industry	Non-consumer Industry
	Intercept $\alpha$	Intercept $\alpha$	Intercept $\alpha$	Intercept $\alpha$	Intercept $\alpha$	Intercept $\alpha$	Intercept $\alpha$	Intercept $\alpha$
<i>Panel A: CSI portfolios</i>								
<i>Residual claim stakeholders</i>								
Shareholders (corp. gov)	-0.016*** (0.005)	-0.010** (0.004)	-0.016*** (0.005)	-0.016*** (0.005)	-0.014*** (0.004)	-0.014*** (0.004)	-0.012** (0.006)	-0.016*** (0.005)
Customers (product)	-0.018** (0.007)	-0.011* (0.007)	-0.014** (0.006)	-0.018** (0.007)	-0.017** (0.007)	-0.022*** (0.007)	-0.007* (0.004)	-0.014** (0.006)
<i>Fixed claim stakeholders</i>								
Environment	-0.005* (0.003)	-0.007** (0.003)	-0.005* (0.003)	-0.003 (0.003)	-0.005* (0.003)	-0.005* (0.003)	-0.006** (0.002)	-0.005* (0.003)
Employees	-0.006 (0.005)	-0.002 (0.005)	-0.005 (0.006)	-0.007 (0.006)	-0.008 (0.006)	-0.006 (0.005)	0.018 (0.017)	-0.006 (0.005)
<i>Panel B: Non-CSI portfolios</i>								
<i>Residual claim stakeholders</i>								
Shareholders (corp. gov)	0.003 (0.003)	0.001 (0.004)	0.002 (0.002)	-0.001 (0.003)	0.000 (0.001)	0.000 (0.002)	0.002 (0.001)	0.003 (0.002)
Customers (product)	-0.001 (0.002)	0.001 (0.003)	0.000 (0.000)	-0.002 (0.004)	-0.001 (0.001)	-0.000 (0.003)	-0.003 (0.002)	-0.001 (0.002)
<i>Fixed claim stakeholders</i>								
Environment	0.005 (0.003)	0.003 (0.005)	0.005 (0.003)	0.001 (0.002)	0.004 (0.003)	0.003 (0.003)	0.002 (0.003)	0.004 (0.003)
Employees	-0.001 (0.002)	-0.003 (0.004)	-0.001 (0.002)	-0.002 (0.003)	0.000 (0.003)	0.000 (0.003)	-0.004 (0.003)	-0.001 (0.002)

Note: Table 6 presents the monthly regressions of abnormal returns or Jensen alpha (Jensen, 1968) to all robustness test portfolios of the Chinese A-share companies on the Carhart extended model. Similar to Table 4, Panel A and B respectively show the results of CSI portfolios and non-CSI portfolios. The “equal weighted” portfolios show the monthly abnormal returns of equal-weighted portfolios while all other portfolios in this table are value-weighted. The “company size” portfolios show the monthly abnormal returns of portfolios excluding small size companies while all other portfolios include the full sample of companies. The “Exclude Chinese Media” portfolios present the monthly abnormal returns of portfolios excluding all Chinese media agencies to address the concerns about appropriateness of media coverage and press freedom in China. The “Novelty of Events” column shows monthly abnormal returns of portfolios applied stringent screening methodology which consists of news that are first time reported. The “Buy-and-hold 12 months” column presents the monthly abnormal returns of portfolios constructed by using buy and hold abnormal returns method. The last two columns show the results of the consumer industry and non-consumer industry, respectively. As the sample period is from June 2006 to July 2012, the observed monthly regressions are 73. \*, \*\*, and \*\*\* indicate significance at the 10%, 5%, and 1% levels, respectively.

buy-and-hold abnormal returns will influence the results. The additional test using this method shows that the results are largely consistent with the calendar-time portfolio approach.

Sixth, we further examine the differences among different industries. The last two columns of Table 6 compare the results of consumer (end-user consumers) industry and non-consumer (business-to-business) industry (e.g., Apple, Amazon, Alibaba, etc.), respectively. Consistent with our first hypothesis (H1), we find that the impact of CSI is stronger for business-to-business consumers (non-consumer industry) because business-to-business consumers (non-consumer) have higher bargaining power than end-user consumers (consumer industry).

In untabulated results, we split the sample into sub-sample periods based on the economy bubble theory, which can detect whether CSI episodes in China are undergoing changes. Therefore, we test the periods during the financial crisis (January 2007 to March 2009) and after the financial crisis (April 2009 to July 2012) by using the core results portfolios and we also remove the outliers from the sample by excluding companies with the 5% highest and 5% lowest number of news items.<sup>7</sup> The untabulated results are similar to our core results in Table 4.

In addition, we use two other market benchmarks for estimating the asset pricing models, namely: MSCI A IMI and CSI 300. We find less significant alphas in the CSI portfolios, however, the three benchmarks produce similar results to the core results in the portfolios relating to

shareholders and consumers. This is consistent with Kothari and Warner (1997), in that abnormal returns can differ widely when different benchmarks are used.

Finally, Hsu, Liang and Matos (2017) argue that state-owned firms have better support from government through government procurement and state funding and social roles of the state-owned enterprises (Zu & Song, 2009), therefore the state ownership can be an important factor. Following Hsu et al. (2017)’s definition on state ownership which the ultimate owner (e.g., government, state or public authority) owns more than 25% voting rights of the firm, we match our sample with the ownership data in Orbis. We find that both of the “non-state-owned” and “state-owned” portfolios with CSI episodes that destroy the relationship with shareholders and employees still significantly underperform the market benchmark.

## 6. Conclusions

### 6.1. Theoretical implications

Extant literature has recognized that the development of CSI literature is still in its nascent stage (Pisani et al., 2017). Responding to the call for conceptualizing the CSI as a separate construct from CSR (Strike et al., 2006; Pisani et al., 2017), we contribute to the stakeholder resource-based view (SRBV) by applying the SRBV to explain the value relevance of CSI in the emerging country context. We invert the definitions of “resources” from the SRBV (Barney, 1991, 2018; McWilliams and Siegel, 2011; McWilliams et al., 2006; Orlitzky et al., 2011) to

<sup>7</sup> Lins et al (2013) demarcate the time period of the financial crisis as August 2008 to March 2009, which lies within the sample period of this study.

explain the characteristics of CSI as “resource-destroying episodes”. We argue that these “resource-destroying episodes” are rarely observed because discoveries of CSI episodes are generally less frequent relative to firms’ main operations.

By applying the theoretical framework of stakeholder resource-based view (SRBV) to CSI studies, we put a particular emphasis on the importance of the stakeholder groups with fixed and residual claims according to their bargaining power over the firms’ economic claims. We integrate the stakeholder salience lens (Agle et al., 1999; Mitchell et al., 1997) on legitimacy, urgency and power to advance our understanding of how stakeholders’ moral or presumed claims can help explain the value relevance of CSI. Compared to CSR, the media coverage is crucial for identifying the severity (harshness) of the CSI episode (Kölbel et al., 2017; Tang and Tang, 2016; Tetlock, 2007). We further extend the SRBV discussions by incorporating the role of news media in influencing the stakeholder salience.

Our study also extends the recent conceptual development in the stakeholder theory of the resource-based view (Dmytryiev et al., 2021; Freeman et al., 2021) by integrating the theory of stakeholder identification and stakeholder salience (Mitchell et al., 1997) to determine “who and what really counts” based on the degree to which managers should pay attention and give priority to competing stakeholders’ claims according to the stakeholder legitimacy, urgency and power. The stakeholders’ response to the media coverage of CSI can be largely associated with the characteristics of CSI episodes.

## 6.2. Managerial implications

Our empirical findings suggest that the value relevance of CSI, measured by the shareholders’ abnormal returns, is most relevant when CSI offends stakeholders with higher bargaining power and higher stakeholder salience. Since corporate managers cannot attend to all stakeholders’ actual (explicit) and presumed (implicit) claims (Mitchell et al., 1997), our findings suggest that stakeholder groups that are considered residual claimants (shareholders and consumers) play a more significant role in explaining the shareholder value destroying impact of CSI episodes than the fixed claimants (environment and employees). The insignificant value relevance of CSI that offended employees calls for the need of Chinese government interventions with high legitimacy to protect labor rights in China. It should also motivate the Chinese government to take actions to encourage disclosure of negative issues and to improve regulatory transparency.

Corporate managers in China should also be aware that CSI episodes that offend fixed claimants’ stakeholder group (employees) can adversely affect stock returns when the news becomes more severe. The value relevance of CSI is also found when CSI offends customers with more powerful claims as the news is widely covered by prominent news media around the world. The insignificant result of source reach for CSI that offended employees brings significant concerns that shared values and social norms from the observers around the world (measured by a high media prominence or source reach) have become less sensitive to or less concerned about labor rights violations in China such that they do not significantly react negatively to the news regarding CSI that offended this group of stakeholders.

Our study provides a unique insight that there is a spectrum of non-shareholder stakeholder groups that have varying degrees of residual claims over the firms’ economic profits beyond the shareholders. This study provides managerial implications that the most severe CSI episodes in Chinese companies can be warning indicators for investors, analysts, institutions and governments; consequently, companies should avoid CSI episodes in their management and decision-making processes. The comparison results of representative stakeholders provide managerial implications for firms making strategic decisions on sustainable business practices and addressing sustainability priorities involving multiple stakeholder groups.

## 6.3. Limitations and future research

There are several limitations of our study. Due to data constraints, there are additional stakeholder groups (e.g., suppliers) excluded in the fixed and residual claimants’ comparison, and there are potentially overlapping boundaries between fixed and residual claimants under special circumstances. Our analyses are limited to investigating the domains coded by RepRisk. Future research may want to engage in additional domains and/or conduct a large-scale text-mining exercise of databases such as Factiva or Lexis Nexis. Our analyses do not examine the differences across countries due to our research focus on the Chinese context with a strong government and strong corporate customers. This raises interesting questions for further research around the impact of cultural values on determining which stakeholders have the most bargaining power to predict the strength of the relationship between CSI episodes and shareholder value in other developed and emerging countries.

## CRedit authorship contribution statement

**Maretno A. Harjoto:** Investigation, Conceptualization, Project administration, Supervision, Writing – original draft, Writing – review & editing, Validation. **Andreas G.F. Hoepner:** Investigation, Funding acquisition, Conceptualization, Writing – review & editing, Validation, Supervision, Resources, Methodology. **Qian Li:** Data curation, Formal analysis, Investigation, Methodology, Software, Validation, Writing – original draft, Writing – review & editing.

## Declaration of Competing Interest

The authors declare that they have no known competing financial interests or personal relationships that could have appeared to influence the work reported in this paper.

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