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Upfront

In Bad Times, It Pays to Be Good: *A reputation for CSR may shield companies from the public's ire.*

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Police officers prepare to carry away demonstrators at the World Trade Organization meeting in downtown Seattle on Dec. 1, 1999.

In Bad Times, It Pays to Be Good

A reputation for CSR may shield companies from the public's ire

When the Seattle World Trade Organization (WTO) meeting collapsed in 1999, many corporations' stock prices quickly followed suit. But not all fell equally. A study published in the Winter 2005 issue of *Corporate Reputation Review* showed that corporations with a reputation for social responsibility lost less market value than did corporations without such a reputation.

In the article, Karen Schnietz of Pepperdine University and Marc Epstein of Rice University measured stock prices of Fortune 500 companies in the days following the WTO talks' unraveling, which took place amidst public protests of corporate environmental and labor abuses. They then compared the stock prices of two groups: those traded in the Domini Social Index (DSI) mutual fund, which is a socially and environmentally screened index fund, and those not included in the fund, and therefore

without a reputation for corporate social responsibility (CSR).

Most striking were their findings for companies in industries notorious for environmental problems (such as energy, steel, and mining) and labor abuses (such as apparel, toys, and

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sporting goods). Among firms in these "worst-offender" industries, those that *did not* have a reputation for social responsibility saw their stock prices drop more than 3 percent, so that the average firm lost \$418 million in market capitalization. However, companies in worst-offender industries that *did* have a socially responsible reputation were buffered, experiencing only slight declines in stock prices.

Companies in other industries showed the same pattern, with stock prices plummeting only for those not having reputations for social responsibility – to the tune of 2 percent. "Apparently, the broad media coverage [of the WTO protests] prompted the public to think about corporate responsibility more widely and to question their investments across the board," said Epstein.

The study suggests that in crises

involving public welfare issues, shareholders register their discontent by selling stock in firms that do not seem socially responsible. “Some of them respond in purely financial terms, extrapolating that labor and environmental protests could trigger events that will seriously affect a company’s financial performance,” says Epstein. “Others decide it’s unethical to hold stock in a company that is not socially responsible.”

Either way, says Schnietz, “With a payoff to shareholder value in the hundreds of millions of dollars, an investment in social and environmental responsibility is clearly worth the effort.” The researchers further suggest that reducing expenditures on social or environmental issues when lean or mean times strike may not be the best strategy.

Steve Voien, an executive vice president with the PR firm Edelman who helps Fortune 10 and 500 firms develop CSR initiatives, sees what the lack of such investment can do to organizations. “A lot of the companies that I assist are in pain,” he says. “There’s no question that firms that get into big trouble over these issues – whether it’s child labor, environmental damage, or what have you – suffer huge financial consequences. If you become an ‘icon of irresponsibility’ in the public’s mind, it will cost you.”

For example, “Reports of what amounts to child slave labor on cocoa plantations in West Africa blindsided everybody, even very responsible companies,” says Voien. “That was potentially damaging to anyone who sold chocolate.”

Likewise, word of social and environmental abuses have spelled financial trouble for several other firms. The Gap and Nike experienced significant losses when it was revealed that

their overseas manufacturing facilities used child labor. Epstein also notes that “Wal-Mart is being criticized for paying low wages and importing merchandise from Asian companies that have questionable practices.”

If nothing else, getting a good CSR program in place can be good risk management. “You don’t want to be hit by the revelation of some new abuse your company is involved in, or by an activist campaign, a consumer boycott, or a resolution by activist shareholders,” he says. Epstein points out that Internet communications now allow negative press coming from even the most remote parts of the planet to travel around the world instantaneously. Similarly, electronic media give advocacy groups more muscle for mobilizing.

“You want to anticipate these issues, not be reactive,” Voien says. “More and more firms are starting to deal with CSR questions, in part because they recognize the benefits laid out in this study, but also because they have to.” —*Marguerite Rigoglioso*

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