When Does CSR Build Trust? Authenticity and Trust in the Implementation of LGBT-friendly Practices in U.S. Firms

RESEARCH SUMMARY

Theory

There is ongoing interest in understanding the mechanisms linking corporate social responsibility (CSR) and firm performance. One important, though sometimes implicit, mechanism linking CSR and firm performance is trust. Scholars have argued that CSR facilitates the development of trust between firms and their stakeholders (Flammer, 2018; Lins, Servaes, & Tamayo, 2017). In this argument, when firms engage in CSR, they signal an intention to consider stakeholder interests in decision making and not act opportunistically towards stakeholders (Godfrey, 2005). Thus, by engaging in CSR, firms can generate trust with their stakeholders, making these stakeholders more willing to make the types of firm-specific resources available that will allow firms to generate economic profits (Jones, Harrison, & Felps, 2018).

However, CSR may not always signal a non-opportunistic intention. Firms engage in CSR for a variety of reasons (Aguilera, Rupp, & Ganapathi, 2007; Bansal & Roth, 2000), including to maximize shareholder wealth (Luo, Kaul, & Seo, 2018; Jia, Gao, & Julian, 2020). If engaging in CSR is consistent with shareholder wealth maximization, stakeholders will learn little regarding a firm's intentions towards its stakeholders by observing its CSR investments. This is because firms whose only objective is to maximize shareholder wealth and have no concern for stakeholder interests per se will also make CSR investments under those conditions. If stakeholders cannot reliably distinguish a firm's intentions towards its stakeholders based on its CSR, it is less likely that trust will develop between these stakeholders and that firm.

This paper investigates the conditions under which CSR is likely to act as a credible signal of authentic stakeholder orientation and thus facilitate the development of trust between firms and their stakeholders and improve firm performance. Building on Clark, Kofford, Christensen, & Barney (2020), we argue that CSR is more likely to build trust when its ex-ante expected impact on shareholder wealth is uncertain. It is argued that under these conditions is CSR more costly for firms that are concerned only with shareholder wealth maximization and thus a credible signal of a concern for stakeholders (Spence, 1973). CSR investments made under these conditions are more likely to develop trust between firms and stakeholders and are thus more likely to improve firm performance.

Research Context and Methods

We explore the relationship between CSR and firm performance in the context of human resource policies enhancing lesbian, gay, bi-sexual, and transgender (LGBT) rights in U.S. firms. We test whether firms that implemented LGBT-friendly policies before these policies were known to have a positive impact on firm performance realize an improvement in employee productivity and firm performance. We expect to find that, while those who implemented such policies before the economic benefits of doing so were clear experienced an improvement in employee productivity and firm performance, while those that implemented these policies only after being ranked did not.

We utilize a two-stage residual estimation strategy to examine the effects of the timing of DPB implementation on firm performance. In the first stage, we use an event history analysis to predict the timing of implementation for the firms in our sample. To do this, we used the Cox proportional hazards models (Cox, 1972). In the second stage of our analysis, we begin by calculating the residuals for each observation from the first stage analysis. A positive residual is indicative of implementation of DPB prior to the timing predicted in the first-stage analysis. Our theory predicts that firms with positive residuals would see greater improvement in firm performance and employee productivity. We then use an Ordinary Least Squares (OLS) regression to estimate the effect of these residuals on firm performance and employee productivity. We include industry fixed effects and control for a number of firm level factors.

Anticipated Results and Implications

While we are still in the process of collecting data, we anticipate finding that the timing of firms' implementation of domestic partner benefits affects the extent to which this form of CSR improves firm performance and employee productivity. If these results come to fruition, this paper will make an important contribution to the literature on CSR and firm performance. While most work assumes that firms develop trust with their stakeholders by engaging in CSR and that this is an important mechanism by which CSR can improve firm performance, this paper may show that there are important contingencies to this relationship.