The Value of Corporate Social Responsibility: Evidence from an Inflation-Driven Crisis of Trust

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I. Motivation and key findings

- What is the value of social capital to firm value?
  - Social capital: the intangible capital accumulated over time through investments in a good relationship with stakeholders.
  - When trust becomes suddenly scarce, social capital is likely to be a major driver of firm value.
- Firms with stronger social capital should be better prepared to preserve stakeholder trust.
  - We take corporate social responsibility (CSR) as a proxy of firms' social capital.
- We employ a sudden increase in inflation as exogenous variation in stakeholder trust to answer this question.
  - Survey evidence indicates that most Americans blame excessive price hikes by companies to raise profits as the leading cause of inflation.
  - This corporate greed or "greedflation" narrative was also pushed by politicians, especially Democrats.
  - Inflation and the corporate greed narrative pose significant threats to the relationship of companies with their stakeholders, and in turn affect firm cash-flows and performance.
- **We find an inflation-hedging effect of CSR on stock prices: following higher inflation, equity investors reward high-CSR firms.**

II. Data and Methodology

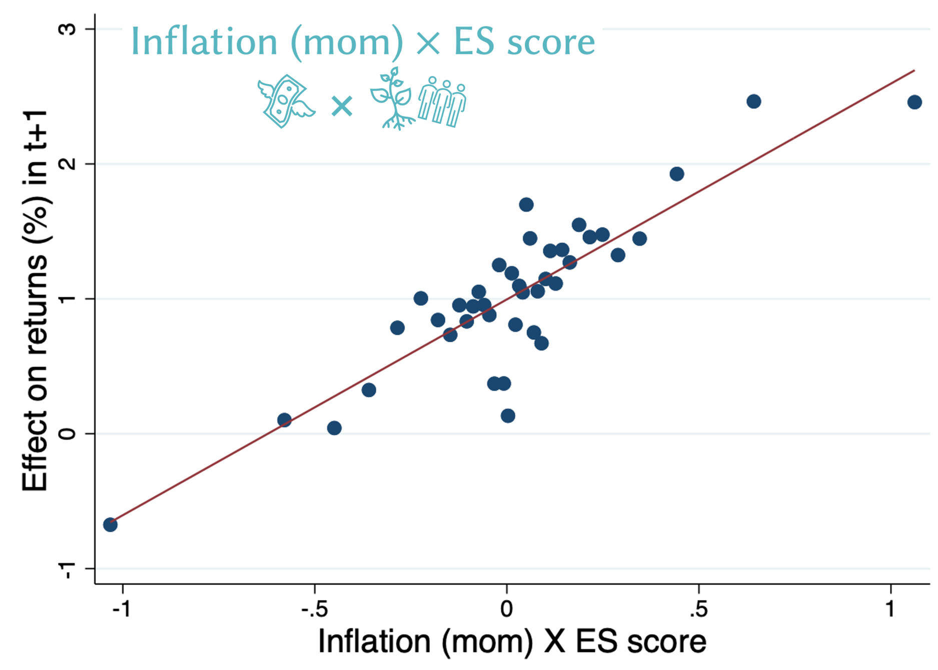
- Our main sample is non-financial and non-utility public firms in the U.S. from 2018 to 2022.
  - We compute stock returns and firm characteristics using Compustat data, and analyst forecast revisions using IBES data.
  - We proxy CSR with annual Environmental and Social (ES) scores from Refinitiv, which we standardize.
  - We take inflation rates from the U.S. Bureau of Labor Statistics.
- We run the following regression:

$$Return_{i,t+1} = \alpha + \beta_1 Inflation_t \times ESscore_{i,t} + \beta_3 ESscore_{i,t} + \gamma' \mathbf{X}_{i,t} + \delta_t + I_i + \epsilon_{i,t}$$

  - We control for lagged firm and stock characteristics (leverage, cash holdings, firm size, book-to-market, ROA, market beta and momentum).
  - We include month and industry fixed effects.
  - Standard errors are clustered at the firm level.

III. The inflation-hedging effect of CSR

- For +1 p.p. of inflation in a given month, companies with a 1 SD higher CSR level experience a stock price outperformance of 1.56*** p.p. in the month that follows, net of the effect of other firm characteristics.



- The coefficient has a positive sign in most industries, confirming the broad relevance of our findings.

IV. Drivers

- Inflation narratives and levels of trust:
  - Stronger effect among firms headquartered in Democratic states, which are more likely to be exposed to the "corporate greed" narrative.
  - Stronger effect among firms in regions where trust and fairness considerations are more important.
- Importance of stakeholders for cash flows:
  - Stronger effect in firms with higher customer awareness (advertising intensity) and sensitivity (B2C industries), as well as higher reliance on labor (R&D intensity).
- Financial analysts: forecasts of earnings and sales are more favorable for high-CSR firms.

V. Main takeaways

- **We spotlight inflation as a crisis in stakeholder trust and provide new insights into the importance of social capital for firm value.**

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