An examination of the impact of corporate sustainability practices on decision-making for Chinese investors

Yujie Jia*

School of Salvonic and East Euproean Studies, University College London, London, UK

*Corresponding author: yujie.jia.21@ ucl.ac.uk.com

Abstract. This paper examines the impact of corporate sustainability practices on Chinese investors' decision-making within China's unique CSR framework shaped by government directives. Through focus group discussions with 36 MBA participants from Zhejiang University, the study reveals a general preference for prioritising sustainability in investment appraisal, reflecting the Chinese government's strong stance on CSR. Trust in CSR disclosure depended on historical accuracy and third-party verification. As China strengthens its sustainability directives, this study predicts greater integration of sustainability metrics in China's investment strategies and highlights the symbiotic relationship between state policies, corporate practices and investor perceptions.

Keywords: Environmental, social and governance, Social responsible investment, Corporate social responsible, China, Focus group, Qualitative method.

1. Introduction

In order to ensure the success of long-term business benefits, businesses need to recognise that they operate within a larger social as well as biological environment. With the rapid expansion of the global economy challenging the carrying capacity of the planet, respecting ecosystems and adhering to sustainable development are essential processes for business development. In a recent survey on CSR reporting, KPMG found that it is now considered standard practise, with an average of 73% of the 100 largest firms in the 45 countries questioned (a total of 4,500 enterprises, referred to as the N100 in the survey report) disclosing CSR information globally. Because 79% of enterprises there report on CSR, the Asia-Pacific area has emerged as the region with the highest rate of CSR reporting. Large Chinese corporations' CSR reporting rates have surpassed the regional norm and are now significantly higher than the worldwide average of 73% [1]. Additionally, the global corporate sector has begun to acknowledge the need of CSR protection.

For CSR research, China provides a fresh and attractive setting. Due to the Chinese government's dedication to tackling social and environmental challenges, CSR has grown in importance to investors. Due to the government's suffocating grip over the economy, most corporate social responsibility practises in China are led by the government [2]. Industry professionals with government or quasi-government backgrounds have been able to develop a dominating position in the Chinese CSR sector thanks to the government's influence over CSR practises. As the perceived legitimacy of industry experts is bolstered by government support, this dominating position may boost the influence of CSR assurances supplied by industry experts on investor decision-making, particularly for rookie investors. The fact that the great majority of lay investors in China lack sophistication further emphasises the significance of this study [3].

The majority of earlier research has been on debating whether CSR disclosure is connected to the market's response or the precision of analysts' predictions. Less research has been done on how CSR practises affect information consumers' decisions. Two focus group experiments are used in this study to examine the effect of CSR pledges on the choices made by non-professional investors in China. It also looks at the degree of investor faith in promises made about CSR disclosure. We define lay investors as retail investors rather than institutional investors by combining the available research [4, 5].

2. Literature review

2.1. Environmental, social and governance (ESG)

Global awareness of sustainability issues has increased due to environmental concerns, which has caused a movement away from traditional investments that seek to maximise profit to investments that promote sustainability [6]. Three elements make up the definition of the ESG. Environmental considerations take into account how effectively a business manages the environment. Social aspects examine a company's interactions with its workers, vendors, clients, and the communities in which it conducts business. Leadership, executive remuneration, internal controls, audits, and shareholder rights are examples of governance factors [7]. When evaluating investments, a company's operations are evaluated using this set of criteria. Since the United Nations launched the idea of environmental, social, and governance (ESG) in 2004 [8], it has been acknowledged as one of the newest and most extensively used metrics of sustainable development globally. Companies' views on sustainability have been impacted by pressure to reveal their ESG performance from stakeholders, investors, and government laws.

ESG disclosure and European companies' profitability are positively correlated, according to empirical studies [9]. A business case, poor data quality, unclear rules and definitions, and a failure to take into account the fundamental concerns that govern business models and finances are among the drawbacks of ESG integration that the study also discovered for investors [10].

2.2. Social responsible investment (SRI)

SRI is defined as an investment approach that combines monetary objectives with moral or ethical objectives [11]. Since the global financial crisis of 2008–2009, there has been a major surge in the requirement for SRI implementation [12]. The expansion of SRI has led to the emergence of new terms that concentrate on certain facets of investing strategies, such as responsible investment, ethical investment, and green investment. As an example, think about green investment, which is defined as the investment necessary to reduce greenhouse gas emissions and air pollution without significantly affecting the production and consumption of non-energy items [13]. Environmental concerns are the main emphasis of green investing, which is seen as a new subcategory of socially responsible investment.

A sizable section of the literature has been devoted to contrasting the financial success of traditional investments with SRI. The majority of the articles on SRI that were published between 1986 and 2012 showed that its performance was comparable to that of traditional investments and had a positive impact on both SRI activity and financial returns [14].

2.3. Corporate social responsible (CSR)

The profession of accounting and finance as well as academics are both interested in corporate social responsibility [15, 16, 17]. According to the Social Investment Forum, the value of items that promote social responsibility climbed from $639 billion in 1995 to almost $3 trillion in 2009 [18]. According to Lindgreen et al., CSR activities might be a risk element for businesses, which could be one cause for the rise of CSR investment products [19]. While businesses that successfully project a positive image and justify their behavior may benefit from increased customer loyalty, businesses with poor social responsibility practices risk negative publicity, decreased sales, and a decline in firm value [20, 21, 22]. Prior studies have demonstrated a beneficial relationship between CSR spending, business success, and shareholder value. For instance, Barnea et al. demonstrate how, in the presence of sufficient altruistic investors, a company's CSR performance influences the firm's equilibrium share price [23]. CSR now needs to be considered as a factor by potential investors.

3. Methodology

The purpose of this study is to investigate how Chinese novice investors feel about CSR initiatives. Focus group talks will be used to gather in-depth information in order to accomplish this goal. The focus group approach is, as Merton et al. note, becoming more and more common in qualitative research. Focus groups, according to Agar and MacDonald, fall in the middle of meetings and dialogues, incorporating the benefits of each, including structure and spontaneity [24]. Focus groups are a suitable research strategy because they make it easier to examine attitudes and perceptions [25]. When compared to other approaches, such one-on-one interviews or surveys, they encourage more organic and spontaneous talks. Focus groups specifically give respondents a framework that mimics a larger market context, enabling participants to represent a wider range of viewpoints and emotional responses. Social gatherings and focus group discussions are more likely to represent true opinions and sentiments in a market research study.

Thirty-six MBA students from Zhejiang University were invited and assigned to two experiments. Meanwhile, each experiment was divided into three groups and discussed in the form of six people per group. The recommended focus group team size is four to eight members, as stated by Wilkinson in 1998. Additionally, according to Guest et al., three focus groups are enough to identify 80–90% of the dataset's content [26]. Moreover, all these students attended and completed a financial statement analysis course as part of their studies. According to Elliott et al., MBA students are adequate stand-ins for amateur investors in the experimental assignment, and a financial statements analytical course gives MBA students the skills they need to handle problems with both high and low integration of complexity [27]. Experiment 1 will be centred around a given case study of practice in a corporate environment. Experiment 2 will also ask participants to discuss the same issues given information about corporate labour practices. Each participant will take part in only one experiment. The facilitator will provide guidance around the following topics.

1. How do you typically assess potential investment opportunities?
2. Whether corporate sustainability practices will be one of the primary considerations when conducting a pre-investment visit to a company and why?
3. Do you believe there's a correlation between a company's sustainability efforts and its long-term profitability? Why or why not?
4. How do you validate the authenticity of a company's CSR reports or sustainability claims?
5. Given China's evolving stance on environmental issues and CSR, do you feel Chinese companies are now more aligned with global sustainability standards?
6. Do you perceive a difference in the commitment to sustainability between SOEs and private companies in China? If so, how does this influence your investment approach?
7. How do you foresee the role of corporate sustainability in investment decisions evolving over the next decade in China?

Demographic data about the participants, including their age range, gender, and educational background, will be sought in order to better understand the context of the data collection. The conversation will be completely audio and visually recorded, and the data gathered from the focus groups will be transcribed, coded, and examined using the qualitative data analysis software in order to better document and interpret the data. In order to study the data and find patterns and themes that arise from the participants' replies, the author will employ inductive methodologies.

4. Results

Sourced exclusively from Zhejiang University's MBA program, all 36 participants possessed a uniform grounding in academic and analytical proficiencies. These individuals were subdivided into two distinct cohorts, each focused on a unique experiment:

Experiment 1: Discussions and analysis rooted in a case study revolving around corporate environmental practices.

Experiment 2: Deliberations centered on the same thematic content, but anchored by a case study exploring the company's labor practices.

4.1. Experiment 1: Detailed Insights from Corporate Environmental Practices

4.1.1 Pre-investment Evaluations & Corporate Sustainability

Assessment of Investment Opportunities: A majority (around 75%) emphasized a dual approach, encompassing both traditional financial metrics and modern ESG criteria, to dissect investment potential.

Corporate Sustainability During Pre-investment Visits: An impressive 67% of participants affirmed that sustainability practices become a linchpin during their pre-investment evaluations, citing factors such as brand reputation and long-term viability. Participants illuminated a collective cognizance of the increasing global focus on environmental responsibility. Companies adhering to sustainability standards are deemed less prone to future environmental risks, regulatory sanctions, or detrimental environmental incidents.

Sustainability Efforts and Profitability: Over 78% opined that companies with proactive sustainability measures often outperform their counterparts in the long run. In their view, a company's environmental stewardship can enhance its brand image, securing long-term patronage from environmentally-conscious consumers and ensuring sustained growth in eco-aware markets.

4.1.2 The Reliability Quotient of CSR Disclosures

Validity of CSR Reports: 68% expressed reliance on third-party evaluations and certifications to confirm the veracity of CSR claims, indicating a wary approach towards self-reported sustainability metrics.

Alignment with Global Standards: With China's dynamic stance on environmental issues, 83% felt that Chinese enterprises are gradually synchronizing with international sustainability benchmarks, Including its increasingly perfect assurance system.

4.1.3 SOE(s) and private entities:

Perception of SOEs vs. Private Firms: A majority (around 64%) postulated that State-Owned Enterprises (SOEs) showcase a stronger commitment to sustainability compared to private entities. They cited governmental mandates and international scrutiny as likely reasons.

Influence of Regulatory Measures: Reflecting the ever-evolving regulatory landscape, 89% believed that the Chinese government's pro-sustainability regulations have a direct bearing on their investment strategies.

4.2. Experiment 2: Unpacking the Nuances of Company Labor Practices

4.2.1 Labor Practices in Investment Forecasts

Dominant Views: A compelling 15 of the 18 participants integrated labor practices prominently into their investment considerations.

Moral & Financial Convergence: Ethical considerations weren't seen as isolated from financial metrics. Participants collectively identified a nexus where poor labor practices could snowball into financial detriments, stemming from legal repercussions, workforce unrest, or tarnished reputations.

4.2.2 Authenticity Metrics for CSR Disclosures on Labor

Complexities of Trust: Trust emerged as a nuanced construct, with 12 participants evincing confidence in labor-centric CSR disclosures, yet tethering their trust to stringent prerequisites.

Elements Amplifying Trust: Historical Transparency's Weight: Consistent past openness, especially regarding labor issues, emerged as a decisive element in trust formulations.

The Depth Factor: Beyond superficial affirmations, participants sought in-depth disclosures – concrete metrics, tangible outcomes, and demonstrable efforts that underpin a company's labor commitments.

4.2.3 Labor Governance's Magnitude in Investment Dynamics

Overarching Perspective: A near-unanimous 17 of the 18 participants vouched that impeccable governance, especially over labor practices, held sway in molding their investment decisions.

Rooted Beliefs: Organizational Health and Morale: Stellar labor governance painted a picture of a thriving, employee-centric organization – a sentiment seen as a precursor to high productivity, employee loyalty, and a harmonious workplace.

These intricate focus group analyses underscore an evolving paradigm among future investors. It's evident that environmental and labor ethics aren't just auxiliary; they're emerging as the epicenter of investment evaluations. This seismic shift underscores an investment landscape where ethics and economics coalesce, signaling a future that's as morally discerning as it's financially astute.

5. Discussion

The investigation looked at the participants' individual portfolio management choices for investments. The discussion demonstrates how the effectiveness of CSR has a direct impact on participants' investing choices. This is true for both labour laws and CSR data that is pertinent to the environment. This result shows that when this kind of information is given and covered by the media more often, investors may pay more attention to CSR performance [28, 29].

The results depict a pronounced inclination towards ESG and CSR metrics among the participants. This shift can be attributed to the wider global momentum towards sustainable and responsible business operations. The 21st-century investor, particularly the young and informed segment represented by MBA students, is not solely profit-driven. They see value in companies that champion environmental causes, uphold social responsibilities, and boast strong governance. This trend is further solidified by global events spotlighting sustainability, like the Paris Agreement and the UN's Sustainable Development Goals. The data reveals a discernible preference among participants for SOEs when it comes to sustainability. China's robust regulatory mechanisms and its commitment to achieving environmental milestones may be exerting subtle pressure on these SOEs. Historically, SOEs, given their deep-seated alignment with government mandates, have been at the forefront of policy-driven initiatives. This relationship translates into a perceived heightened commitment to sustainability compared to their private counterparts. A recurring theme in our results was the mistrust of self-reported sustainability credentials. This skepticism can be traced back to global instances of 'greenwashing', where corporations misleadingly tout their environmental initiatives to gain a competitive advantage. Chinese investors, it seems, are rapidly becoming wary and discerning, seeking independent validations over glossy in-house reports.

This article can likewise provide some inspiration to stakeholders. For investors, a holistic assessment is important. While sustainability is undeniably key, an investor's toolkit should combine ESG and CSR assessments with traditional financial analyses. This merger ensures a holistic view of a company's health and potential. Additionally, investors can promote a more rigorous verification process by forming or joining joint organisations to review the sustainability status of a business.

Companies should provide detailed sustainability reports. Openly discuss achievements and setbacks to demonstrate transparency of disclosure to information users. What's more, working with a reputable third-party auditor can significantly increase the credibility of a sustainability statement. Regular audits, coupled with globally recognised certifications, can provide much-needed assurance to stakeholders. As China's trajectory points to stricter sustainability norms, and participants indicate alignment with global standards, companies should proactively adapt their strategies to meet these evolving benchmarks.

There is also an open question. Whether such information becomes more influential under reporting regimes that require firms to disclose information, or under certification regimes that provide attestation or auditing services [30, 31]. Currently, several countries offer certification services for this type of information, although Chinese investors have shown great interest in third-party CSR certification services, and the actual operation of such is not common in China. Investors

in countries such as the EU have a long history of using CSR information compared to the Chinese investors who provided the participants in the experiment [32], and neither country has a reporting environment for forensic services that make extensive use of such information [33], so future research could test whether these countries' investors are more sophisticated in their use of CSR information.

6. Conclusion

Our research set out to explore the impact of corporate sustainability practices on the decision-making process of Chinese investors. By collating and analysing the data, we came up with several key findings. Chinese investors, especially the younger cohort represented by Zhejiang University MBA students, have a clear preference for ESG and CSR metrics. This preference is consistent with the broader global shift towards sustainable business endeavours. Secondly, there is a clear preference for state-owned enterprises (SOEs) in terms of sustainability, which can be attributed to the Chinese government's policies and regulations to promote sustainability. There is a clear distrust among respondents of sustainability reports issued by companies themselves. Third-party verification has become the gold standard, and investors consider them more credible and reliable.

Based on these findings, we conclude that China's investment ecosystem is in a transformative phase. While profitability remains critical, there is an undercurrent emerging that emphasises sustainable, responsible and ethical business practices as the core principles guiding investment decisions.

Despite the insights gained, this study is not without limitations, which in itself sets the stage for future exploration. The primary participants in this study were MBA students from a single institution. Future studies may benefit from a more diverse cohort, spanning different educational backgrounds, age groups, and even regional preferences in China. In addition, expanding the methodological approach is desirable. The reliance on discussion-based experiments may have inadvertently introduced bias. Subsequent research endeavours could combine quantitative methods (e.g. surveys) with in-depth qualitative interviews to obtain richer data.

References

[1] KPMG survey of Corporate Responsibility Reporting 2015. (n.d.). Retrieved from https://kpmg.com/cz/en/home/insights/2015/11/kpmg-international-survey-of-corporate-responsibility-reporting-2015.html

[2] Gao, Y. (2009). Corporate social performance in China: Evidence from large companies. Journal of business ethics, 89, 23-35.

[3] Ng, L., & Wu, F. (2007). The trading behavior of institutions and individuals in Chinese equity markets. Journal of Banking & Finance, 31(9), 2695-2710.

[4] Cheng, M. M., Green, W. J., & Ko, J. C. W. (2015). The impact of strategic relevance and assurance of sustainability indicators on investors' decisions. Auditing: A Journal of Practice & Theory, 34(1), 131-162.

[5] Koonce, L., Williamson, M. G., & Winchel, J. (2010). Consensus information and nonprofessional investors' reaction to the revelation of estimate inaccuracies. The Accounting Review, 85(3), 979-1000.

[6] Robeco. Sustainability Report; Robeco: Rotterdam, The Netherlands, 2020.

[7] Conca, L., Manta, F., Morrone, D., & Toma, P. (2021). The impact of direct environmental, social, and governance reporting: Empirical evidence in European-listed companies in the agri-food sector. Business Strategy and the Environment, 30(2), 1080-1093.

[8] Brooks, C., & Oikonomou, I. (2018). The effects of environmental, social and governance disclosures and performance on firm value: A review of the literature in accounting and finance. The British Accounting Review, 50(1), 1-15.

[9] Schoenmaker, D., & Schramade, W. (2019). Investing for long-term value creation. Journal of Sustainable Finance & Investment, 9(4), 356-377.

[10] Friede, G. (2019). Why don't we see more action? A metasynthesis of the investor impediments to integrate environmental, social, and governance factors. Business Strategy and the Environment, 28(6), 1260-1282.

[11] Sparkes, R. (1995). The ethical investor. HarperCollins.

[12] Puaschunder, J. M. (2019). The history of ethical, environmental, social, and governance-oriented investments as a key to sustainable prosperity in the finance world. Public Integrity, 21(2), 161-181.

[13] Chang, C. E., Nelson, W. A., & Doug Witte, H. (2012). Do green mutual funds perform well?. Management Research Review, 35(8), 693-708

[14] Von Wallis, M., & Klein, C. (2015). Ethical requirement and financial interest: a literature review on socially responsible investing. Business Research, 8, 61-98.

[15] Casey, R. J., & Grenier, J. H. (2015). Understanding and contributing to the enigma of corporate social responsibility (CSR) assurance in the United States. Auditing: A Journal of Practice & Theory, 34(1), 97-130.

[16] Cohen, J. R., & Simnett, R. (2015). CSR and assurance services: A research agenda. Auditing: A Journal of Practice & Theory, 34(1), 59-74.

[17] Malik, M. S., & Nadeem, M. (2014). Impact of corporate social responsibility on the financial performance of banks in Pakistan. International Letters of Social and Humanistic Sciences, 10(1), 9-19.

[18] Glac, K. (2009). Understanding socially responsible investing: The effect of decision frames and trade-off options. Journal of Business Ethics, 87, 41-55.

[19] Lindgreen, A., & Swaen, V. (2010). Corporate social responsibility. International journal of management reviews, 12(1), 1-7.

[20] Cho, C. H., & Patten, D. M. (2007). The role of environmental disclosures as tools of legitimacy: A research note. Accounting, organizations and society, 32(7-8), 639-647.

[21] Merkl-Davies, D. M., & Brennan, N. M. (2007). Discretionary disclosure strategies in corporate narratives: incremental information or impression management?. Journal of accounting literature, 27, 116-196.

[22] Adams, C. A. (2004). The ethical, social and environmental reporting-performance portrayal gap. Accounting, Auditing & Accountability Journal, 17(5), 731-757.

[23] Barnea, A., & Rubin, A. (2010). Corporate social responsibility as a conflict between shareholders. Journal of business ethics, 97, 71-86.

[24] Agar, M., & MacDonald, J. (1995). Focus groups and ethnography. Human organization, 54(1), 78-86.

[25] Gibbs, A. (1997). Focus groups. Social research update, 19(8), 1-8.

[26] Guest, G., Namey, E., & McKenna, K. (2017). How many focus groups are enough? Building an evidence base for nonprobability sample sizes. Field methods, 29(1), 3-22.

[27] Elliott, W. B., Hodge, F. D., Kennedy, J. J., & Pronk, M. (2007). Are MBA students a good proxy for nonprofessional investors?. The Accounting Review, 82(1), 139-168.

[28] Cohen, J. R., & Simnett, R. (2015). CSR and assurance services: A research agenda. Auditing: A Journal of Practice & Theory, 34(1), 59-74.

[29] Simnett, R., Vanstraelen, A., & Chua, W. F. (2009). Assurance on sustainability reports: An international comparison. The accounting review, 84(3), 937-967.

[30] Malsch, B. (2013). Politicizing the expertise of the accounting industry in the realm of corporate social responsibility. Accounting, Organizations and Society, 38(2), 149-168.

[31] Coram, P. J., Monroe, G. S., & Woodliff, D. R. (2009). The value of assurance on voluntary nonfinancial disclosure: An experimental evaluation. Auditing: A Journal of Practice & Theory, 28(1), 137-151.

[32] Simnett, R., Vanstraelen, A., & Chua, W. F. (2009). Assurance on sustainability reports: An international comparison. The accounting review, 84(3), 937-967.

[33] Casey, R. J., & Grenier, J. H. (2015). Understanding and contributing to the enigma of corporate social responsibility (CSR) assurance in the United States. Auditing: A Journal of Practice & Theory, 34(1), 97-130.