Improving Corporate Performance through Stakeholder-Based ESG Practices

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Abstract. In the context of escalating concerns over environmental issues and global warming, consumers and investors increasingly prioritize corporate sustainability and social responsibility. To bolster corporate image and competitiveness, many companies integrate Environmental, Social, and Governance (ESG) principles into their strategic frameworks. While existing research has established a positive link between robust ESG practices and improved financial performance—attributed to factors such as enhanced reputation, cost reduction, and effective risk management—the precise mechanisms of this relationship remain unclear. This study aims to enhance understanding by exploring how ESG considerations impact stakeholders and influence corporate performance. Empirical evidence underscores that commendable ESG performance yields favorable outcomes for all key stakeholders. Simultaneously, the research examines the reciprocal relationship where executive behavior significantly influences ESG ratings. Through this investigation, it aims to provide additional insights into the intricate interplay between ESG, stakeholders, and corporate performance, contributing to a nuanced comprehension of this crucial nexus.

Keywords: ESG, Corporate Performance, Stakeholders.

1. Introduction

Environmental, social, and governance (ESG) criteria have become increasingly important for evaluating corporate performance and sustainability. This paper analyzes the relationship between ESG and corporate performance from the perspective of key stakeholders, including employees, government, investors, consumers, and executives.

At present, studying the impact of ESG on enterprises has become a key research direction for scholars at home and abroad. Most of the studies believe that the improvement of ESG performance has a positive impact on enterprises. From the perspective of profitability, good ESG can improve the profitability of enterprises [1]. From an investment perspective, portfolios and funds composed of high ESG stocks perform well [2]. At the same time, ESG performance improves firms' investment efficiency, i.e., mitigates firms' underinvestment and discourages firms' overinvestment [3]. From the perspective of corporate reputation, good ESG performance can build a good social image and enhance corporate reputation, which can attract more investors [4]. It will get more favorable bank credit and obtain more policy support [5, 6]. It also helps improve customer loyalty and stability [7].

From the above studies, it can be found that most of the current studies on ESG and corporate performance focus on the impact of ESG on the financial value and brand image of companies. As a result, the research objects are mostly investors and corporate managers. At the same time, the analysis from the perspective of important stakeholders, such as the government and consumers, needs to be included. This paper aims to provide additional insights by examining how ESG affects stakeholders and in turn, impacts corporate performance.

Specifically, this paper discusses how employee recognition, government regulations, investor preferences, consumer values, and executive behavior relate to ESG scoring and corporate financials. Case studies on companies like Costco, BYD, and Tesla are analyzed to demonstrate these connections. The analysis provides a multi-faceted view of the ESG-performance relationship and highlights the mediating role of stakeholders. The findings contribute to the academic literature on sustainable and responsible business practices. From a practical perspective, they guide managers on implementing impactful ESG strategies.

2. Employees

This section discusses how ESG performance influences corporate financial outcomes through employees, based on Li Weian's stakeholder view, defining corporate governance as coordinating company interests across all stakeholders [8].

2.1. ESG Performance Cultivates Employee Loyalty

Analysis shows that strong ESG credentials grasp employees' hearts and minds. Excellent ESG signifies an admirable corporate culture that fundamentally increases staff's sense of belonging, identity, and emotional alignment with the company's purpose and values [9]. This leads to tangible impacts, including enhanced employee motivation, willingness to invest discretionary efforts, engagement with work, and overall job satisfaction [10].

In aggregate, these boost employee loyalty and commitment to the organization, reducing tendencies to explore alternate job openings purely for marginal financial incentives. Thus, ESG excellence directly lowers employee turnover rates, helping maintain stability in operations and cumulative skill levels across the company's human capital. Avoiding recurring churns in rehiring and retraining new workers saves substantial replacement costs while minimizing productivity disruptions during transitions [11].

2.2. Costco Example

For example, Costco's pioneering governance model acting upon strong ESG principles has achieved tremendous employee loyalty and industry-leading retention. A Bloomberg report revealed Costco pays an average hourly wage of $20.89, much higher than comparable retail rivals Walmart ($12.67) or Target ($8.18). Additionally, 88% of Costco employees have company health insurance, an exceptionally high figure for the retail sector.

Consequently, over 90% of Costco workers stay beyond a year, whereas Walmart sees 44% annual turnover. Multiple research studies suggest replacing an employee costs 1.5 times their salary on average, with additional ramp-up delays before new hires are fully cross-trained and integrated into operations. Managers often take even longer to regain productivity. Such expenses and disruptions can be substantially avoided through progressive ESG-aligned retention schemes [12].

2.3. Stimulating Engagement & Efficiency

Furthermore, salaries and benefits only partially impact efficiency. Additional aspects like inspiration, enthusiasm, and satisfaction with the broader work environment also play a key role in activating peak employee performance [13]. Companies hardwiring ESG principles like Costco into their DNA can utilize effective performance evaluation protocols, fair promotion channels, non-hierarchical policies, and inclusive cultures to motivate employees intrinsically.

For instance, nearly all Costco senior executives are homegrown from early store-level entry points, setting an example for ambitious younger staff to aspire towards through dedicated efforts. Moreover, corporate privileges like parking spaces are allocated purely based on tenure, not hierarchy. Shop floor employees are treated with equal respect as office staff. Such structural measures subliminally yet unambiguously signal to employees that their unique contributions are cherished, promoting deeper self-drive. Protecting employees from undue stress also unlocks fuller application of their skills [14].

Ultimately, companies excelling on ESG dimensions are best positioned to stimulate peak workplace productivity by aligning wider organizational systems to crowd in intrinsic motivation and meaningfully engage human talents beyond purely transactional levers. This analysis shows that companies exhibiting solid ESG foundations towards employees reap manifold dividends – lower turnover, recruiting, and training costs coupled with higher engagement, satisfaction, effort, and productivity gains – collectively enhancing corporate performance.

3. Government

Governments play an increasingly interventionist role in balancing broader environmental, societal and governance externalities against narrow corporate profit motives [15]. Well-designed regulations and incentives promoting responsible corporate conduct can provide win-win benefits for both corporations and communities. On the other hand, non-compliance can impose heavy financial and reputational costs for corporations.

China's "Parallel Management Measures for the Average Fuel Consumption of Passenger Vehicle Enterprises and the Credits of New Energy Vehicles" (namely the double-integral policy) for the automobile industry (enacted in 2017) aims to address environmental externalities by mandating ever-tighter fleet efficiency and electric vehicle share standards for manufacturers. The so-called double-integral is the CAFC (Corporate Average Fuel Consumption) integral, NEV (New Energy Vehicle) integral, or fuel consumption integral and new energy integral for short. Companies generate credits based on how much they over or under-comply with the annually advancing standards. Over-compliant green leaders like BYD and Tesla can sell their excess credits to others. Under-compliant stragglers must purchase credits from others to cover their deficits over time [16].

3.1. Calculation Formulas

$$\text{CAFC integral} = (\text{up to the standard value} - \text{actual value}) \times \text{annual total production/import} \tag{1}$$

$$\text{NEV integral} = \text{pure electric vehicle integral} + \text{plug} - \text{in hybrid vehicle integral} + \text{fuel cell vehicle integral} \tag{2}$$

Both CAFC integral and NEV integral have standard value and actual value. If the actual value is greater than the standard value, the corporate can get positive integrals. On the contrary, the corporate will get negative integrals. To be simplify, the more environmentally friendly, the more positive integrals corporate will get. It should be noted that in addition to the calculation methods mentioned above, many factors affect the double integration, such as the quality of the equipment and the power consumption of 100 kilometers, etc., all of which will affect the final integral obtained by the enterprise in the form of "coefficient", which will not be listed here.

3.2. Rules for Double Integrals

The rules for using the CAFC integral and NEV integral are almost different. There are three key facts it must notice related directly to the following analysis:

(1) Only CAFC-positive integrals can be carried over and transferred.

(2) Only NEV positive integrals can be sold.

(2) Negative integral should be offset by positive integral.

3.3. Impact on Corporate

Suppose a corporation has outstanding performance, producing more high-efficiency new energy vehicles and less highly polluting fuel cars. In that case, the corporation will have more CAFC-positive integrals and NEV-positive integrals. By selling NEV-positive integrals, the corporation can earn great profit. A case in point is BYD. Among the companies meeting the average fuel consumption standard for passenger cars in FY2021, BYD ranks first, with a total of 3,551,754 positive integrals. At the same time, the positive integral of NEV, which can be traded, has 1655615 points. According to the annual report of credits released by the Ministry of Industry and Information Technology, the average price of NEV integral in 2021 is 2,088 yuan/points, which means that if

BYD sells all its positive integrals, it will get 3.456 billion yuan, which can be included in the 2022 financial report. Secondly, the corporation can carry over this year's remaining CAFC positive integrals. However, only some of the CAFC-positive integrals can be carried over to next year. The remaining CAFC positive integrals times the carry-over rate this year equals the integrals corporate have at the beginning of next year.

3.4. Corporate with Inferior Performance in ESG

Corporations will get more negative impacts if they produce cars with high fuel consumption. The high-fuel consumption product cannot be sold before the negative integrals are returned to zero. Therefore, the corporation need to use positive integrals to offset the negative integrals. Suppose the company does not have enough positive integrals to offset the negative ones. In that case, there are two ways to get more positive integrals: (1) Purchase NEV positive integrals from other companies, increasing the expense. (2) Transfer CAFC-positive integrals from its related companies.

Suppose the corporation does not want to change the negative integral to zero. In that case, it should submit the product adjustment plan and set the deadline for compliance so that the expected positive integrals generated in the current year can offset the negative integrals that have not been offset. Making a product adjustment plan means corporations need to produce more new energy vehicles and reduce the production of highly polluting cars or improve technology, which will increase manufacturing expenses and manage expenses. In this case, the corporation must compare the expense between purchasing integrals and making a product adjustment plan to decide.

Such empirical evidence supports the notion that companies that incorporate strong ESG considerations related to employee welfare and ethical behavior towards their internal stakeholders are rewarded with more committed, loyal, and productive workforces. These collectively translate into significantly lower employee turnover and recruiting costs while unlocking greater productivity, efficiency, innovation, and financial performance.

4. Investor Preferences for ESG

In capital markets, an increasing number of investors prefer to invest in ESG-related programs. According to the 2021 Global Consumer Survey from Accenture, 98% of Chinese interviewees recognize that the value of environmental protection and sustainable development impacts purchasing decisions, while only 43% will pay more for sustainability. The main driver for profit-seeking investors to favor ESG investments gradually is that they provide better returns than conventional options.

The core difference between ESG and normal investment programs is that the former entails greater corporate attention to the environment, social issues, and governance [17]. McKinsey’s research shows that high ESG-scoring companies had above-average returns and lower risk over several years [18]. On the one hand, adopting ESG best practices requires dedicated funding so costs may increase in the short-term. Conversely, it leads to positive outcomes like improved reputation, operational efficiency, proactive regulation compliance, and risk mitigation that enhance long-term value.

For instance, the Exxon Valdez oil spill exemplified the severe environmental and financial consequences of prioritizing immediate savings over responsible conduct. The accident cost Exxon over $7 billion in clean-up expenses, settlements, and lost revenues. Investors suffered from an initial share price drop of 6.2%, amounting to $8 billion in market capitalization losses that took years to recover. Such cases highlight that while ESG investments may mean sacrificing some profits initially, they avoid larger losses from incidents through risk reduction. Thereby, investors and companies stand to gain consistent returns in the long term rather than the temporary benefits of cutting corners.

ESG also lowers the cost of debt financing. An example is green for the E angle of ESG. Green bonds have lower interest rates than the traditional bonds. Relating to accounting, companies issuing bonds to get funds will increase the total liabilities, and at the same time, the debt ratio will increase too. Thanks to the high leverage, not only will the companies' stock be influenced, but it will also decrease the security for creditors making loans. However, green bonds have lower interest rates, affecting the company's financing performance in the early stage. The lower perceived risk makes green bonds financially attractive for investors as well. Through compliance signaling and transparency mechanisms, ESG integration signals organizations' commitment to sustainable value creation. This results in a lower cost of capital that can drive higher profitability.

5. Consumer Demand for Sustainability

According to the 2021 Global Consumer Survey from Accenture, Chinese consumers' willingness to pay more for sustainable products is relatively low at 43%. However, 98% agree that environmental values influence purchase choices. As the country transitions economically, considerations like quality, pricing, and cost-effectiveness tend to take precedence when buying goods currently. Sustainable brands need to balance purpose with consumer value delivery.

For instance, while sustainable footwear maker Allbirds is hugely popular in Western markets, its sales in China have yet to catch up with more functional brands like Lululemon [19]. However, strategies like Saturnbird's coffee pod buyback-recycling engagement program have cultivated loyal customer bases. The project allows buyers to return used capsules to earn rewards, reinforcing ecological values while incentivizing repurchases. Such initiatives aligning sustainability with quality, affordability, and consumer education are key. As market segments focused on environmental impact continue to grow, purpose-driven yet competitive brands could gain the advantage. Sustainable attributes serve to differentiate meaningfully when product performance and pricing are competitive [20].

6. The Role of Executives in ESG

Company executives play an instrumental role in ESG's vision, strategy design, and execution [21]. Firms with diverse boards and relevant experience also score higher on ESG performance. However, some leaders' personal interests may conflict with fiduciary duties towards shareholders and accountability to stakeholders [21]. Such behaviors prioritizing short-term gains over responsible growth negatively impact ESG ratings, competitiveness, and long-term success. Corporate governance aims to address this through oversight mechanisms ensuring transparency and accountability.

For example, Tesla has pioneered electric vehicles but still scores relatively poorly in governance metrics due to its CEO's uncontrolled public communications. A previous baseless tweet claiming an imminent privatization bid led to SEC lawsuits, fines, and reputational damage. By undermining leadership accountability, such incidents have decreased investor trust [21]. More broadly, executive conduct that flouts regulations risks backlash, jeopardizing ESG progress. Therefore, principled leadership aligning leader actions with stakeholder interests is vital for smooth ESG assimilation. Social media communications also require governance policies to balance transparency with responsibility [22].

7. Conclusion

In conclusion, this paper has analyzed the relationship between ESG and corporate performance from the perspective of key stakeholders - employees, government, investors, consumers, and executives. The analysis shows that strong ESG performance can lead to better financial outcomes through factors such as improved employee satisfaction and retention, access to policy incentives, attracting sustainable investments, meeting consumer values, and promoting good governance. However, ESG-performance links are complex and dependent on context. As the case studies demonstrate, consumer willingness to pay for sustainability varies across countries and requires education. Government regulations can both encourage and add compliance costs for businesses. Executives need to balance personal interests with duties to the company and its shareholders.

Overall, the findings support the business case for sustainability, with ESG strengthening stakeholder relationships and building corporate resilience. However, organizations need to adopt tailored strategies considering their unique positioning and priorities. More cross-country comparative research is also needed to generalize insights in different institutional settings. As ESG investing and business transformation gain momentum globally, this paper contributes timely insights into why sustainability pays off. It highlights the mechanisms that transmit ESG to financial materiality via stakeholders. Both researchers and executives can build on the analysis to further unravel these relationships and embed responsible values that serve both business and society.

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