The Impact of ESG Factors on Financial Performance in BRICS

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ABSTRACT

During the past decades the concepts such as corporate social responsibility, sustainability, and extra-financial factors – namely environmental, social, and governance of companies (ESG), have evolved gradually. There has been an ongoing emphasis on the environment friendly acts, social activities, and governance practices of firms to extend corporations' activities from simply maximizing shareholder wealth to fulfilling the various stakeholder expectations.

Stakeholder theory provided the basis for this thesis. We examined the association between corporate financial performance and corporate social responsibility performance measured by ESG scores, in a handful of emerging economies labelled the BRICS. The total panel data was composed of 1420 observations of 292 companies over the period of 2014 to 2018.

The empirical results indicate that under current market condition, companies located in BRICS countries are able to earn more profit through enhancing their ESG performance. For our case study, it seems that governance practices are not contributing to the financial performance of companies as much as the social and environmental practices are.

Keywords: ESG, CSR, stakeholder theory, financial performance, ROA

ÖZ

Geçtiğimiz yıllarda kurumsal sosyal sorumluluk, sürdürülebilirlik ve şirket dışı çevresel, sosyal ve yönetişim (ÇSY) gibi finansal olmayan faktörler ve bunlara bağlı olan kavramlar kademeli olarak gelişti. Kurumların faaliyetlerini genişletmek için firmaların çevre dostu davranışları, sosyal aktiviteleri ve yönetişim uygulamalarına, hissedar refahını maksimize etmekten, çeşitli paydaş beklentilerini yerine getirmeye kadar devam eden bir vurgu yapılmıştır.

Paydaş teorisi bu tez için temel kuramı sağlamıştır. Kurumsal finansal performans ile ÇSY seviyesiyle ölçülen kurumsal sosyal sorumluluk performansı arasındaki ilişkiyi, BRICS olarak adlandırılan bir kaç gelişen ekonomide inceledik. Toplam panel verileri 2014 ve 2018 yılları arasında 292 özel ve kamu şirketinin 1420 gözleminden oluşmuştur.

Ampirik sonuçlara göre mevcut piyasa koşullarında BRICS ülkelerinde bulunan şirketlerin ÇSY performanslarını artırarak daha fazla kar elde edebildiklerini göstermektedir. Bu çalışmamızda, yönetişim uygulamalarının, şirketlerin sosyal ve çevresel uygulamalardaki kadar finansal performanslarına katkıda bulunmadığı görülmektedir.

Anahtar kelimeler: ÇSY, KSS, paydaş teorisi, finansal performans, aktif karlılık

This thesis is wholeheartedly dedicated to my beloved parents.

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LIST OF ABBREVIATIONS

BRICS	Brazil, Russia, India, China, South Africa
CFP	Corporate Financial Performance
CSR	Corporate Social Responsibility
ESG	Environmental, Social, and governance
OLS	Ordinary Least Square
ROA	Return On Assets

Chapter 1

INTRODUCTION

Numerous studies have shown the adverse impact of life today, how unequal working conditions and wealth are dispersed around the world, and also how corruption in various levels is a large part of the society. As the public is being more informed and mindful of this social affliction, the need to address these issues -mostly by corporations and governments- has increased. This has led to the enforcement of rules, regulations, and initiatives concerning sustainability to be able to monitor and address these concerns.

Therefore, in the last decade, there has been an ongoing emphasis on the environment friendly acts, social activities, and governance practices of firms to extend corporations' activities from simply maximizing shareholder wealth to fulfilling the various stakeholder expectations (Gillan, 2010).

The traditional view of business was that the corporations exist to maximize the profit of shareholders (Friedman, 1970). Under this mindset, any contribution to the "social objectives" in general was considered as spending the "shareholders' money" and reducing their profit and was professionally unacceptable. However, in response to this view, the stakeholder approach to strategy came into view in the mid-1980s. This alternate argument claimed that corporations should take into account a wide range of groups who can affect or are affected by the corporation or in a single word, its "stakeholders" (Freeman, 1984). Later on, Freeman proposed that managing stakeholders' needs appropriately could sustain value creation for shareholders. Currently, the view in which Freeman created for stakeholder is the prevailing view of business in the academic literature (Taneja, Taneja, & Gupta, 2011).

A significant area of interests for theorists of social responsibility has been the definition of legitimate stakeholders. Jones (1995) believed the development of stakeholder and its contributing features has provided a basis for the advocates of Corporate Social Responsibility (referred to as CSR hereafter) who theorize that better CSR could lead to making stronger relationships with different stakeholders (employees, consumers, local communities, environmental activists and concerned citizens among many others) and it is necessary if a company wants a sustainable profit making and long-term success.

There have been various definitions of corporate social responsibility since early 20th century. Fitch (1976) defined corporate social responsibility as the serious attempt to solve problems caused wholly or in part by the corporations. CSR refers to strategies corporations or firms which conduct their business in a way that is ethical, society friendly and beneficial to the community in terms of development (Ismail, 2009). Beyond legal requirements, CSR is part of a company's management activities for the well-being of society (Yoon, Lee, & Byun, 2018).

While studying CSR, using standard and comparable CSR information is crucial. Yet still clearly defining CSR concept is not easy, as a result some disagreements can be seen regarding the definition. In a primary study of CSR, Carroll (1979) posited a model to enable companies to test investing in CSR based on the ethical, economic, and legal scopes (environmental issues were considered a part of the economic and legal scope). After that, phrases like sustainability, corporate responsibility, corporate governance, socio-environmental governance, and environmental, social and governance (ESG) became commonly in use as synonymous with CSR.

The idea of ESG was firstly represented in a report prepared by the United Nations Principles of Responsible Investment, in which speaks favorably of considering ESG scores by investors as a central ingredient while making decisions for investing. In practice, management consulting firms and investors widely use ESG scores as a major index to understand a firm’s overall CSR performance. According to a study of Kocmanová & Šimberová (2014) ESG scores are made of attributes that we are able to measure them, are easy to compare, trustable, operational, trackable, significant, and expressive. These qualities together make the indicators more beneficial and valuable.

ESG basically is a measure for evaluating a company’s environmental, social, and corporate governance actions and merges the implementation of these actions. A company’s *environmental performance* points out its attempts in lowering resource expenditure and emissions. A company’s *social performance* shows how much the company respects employment quality, human rights, product responsibility, and bond with community. At last, a company’s *corporate governance performance* shows the managers responsibilities and rights.

Using ESG scores as a major index for evaluating CSR, this study explains the association between CSR and corporate financial performance (referred to as CFP hereafter) considering stakeholder theory as a foundation of analysis, in a handful of emerging economies labelled the BRICS. The term BRIC was first created by O’Neill in 2001, who is a British economist with the idea that, as of 2040 the economies of West would be left behind by Brazil, Russia, India and China (South Africa was added later) (O’Neill, 2012). The population of BRICS countries was over 3.1 billion people in 2015, about 41% of the world population. Also, members except South Africa, are in the top 10 list of the world population. As of 2018, these five countries have totally nominal GDP of US$18.6 trillion, about 23.2% of the gross world product, combined GDP (PPP) of around US$40.55 trillion (32% of World's GDP PPP) and an estimated US$4.46 trillion in combined foreign reserves according to IMF (IMF, 2017).

In this thesis the role that ESG plays in leading BRICS firms is explored. The total panel data was composed of 1420 observations of 292 companies over the period of 2014 to 2018 from two databases; Thomson Reuters Eikon (As of 2019 known as REFINITIV) to get the ESG ratings for our sample companies, and DataStream for financial variables about the company profile such as Return on Assets (ROA), company size, and financial leverage. There has been no question about the trustworthiness of these two databases neither among corporate information users nor scholars, as Cheng et al. (2014) argue.

Chapter 2

LITERATURE REVIEW

2.1 Stakeholder Theory

A key to understanding our general surrounding is theorization (Weick, 1995). Since theories present more prominent scholarly thoroughness and understand the intricacy of the empirical world based on clarifications and predictions, a good comprehension of theories in scholarly work is required (Bacharach, 1989). Beside organizing the knowledge, theory 'explains the values which shape knowledge' (Suddaby, 2014).

In CSR literature, theory can give us logical frameworks to make a complicated reality simpler and impart a valuable understanding of socially responsible and irresponsible actions (Unerman & Chapman, 2014). As a matter of fact, it will help scholars to see the triggers of social changes at various levels of analysis (Aguilera, Rupp, Williams, & Ganapathi, 2007). These being said, this section leads to the theory that link ESG and performance. In such manner, Stakeholder theory is introduced, to help clarify the task in defining a strategic orientation, such as with ESG.

Freeman (1984) characterizes a company as an organizational entity through which various participants achieve several goals (Donaldson & Preston, 1995). He brings up the word stakeholder as "any group or individual who can affect or is affected by the achievement of an organization's objectives" (Freeman 1984: 46). In creating this definition, Freeman (1984) took the position that firms produce externalities that impact both internal and external parties (Sarkis, Gonzalez-Torre, & Adenso-Diaz, 2010).

Stakeholders frequently raise pressures on firms to strengthen the positive impacts of the externalities and lessen the negative ones. As a 'going concern', a phrase John R. Commons (1936) made popular, based on stakeholder theory, the established corporation basically consists of three main groups—External stakeholders, Internal stakeholders, and Shareholders/Shareowners. External stakeholders comprise participants such as Communities; Competitors; Customers; Governments; Political Groups; Suppliers; and Trade Associations. Internal stakeholders involve participants such as Companies; Employees; 'Financiers' or 'Investors'; and Parent Company. And the third group of stakeholders is 'Shareholders/ Shareowners'.

This group differs from the terms' Investors' and 'Financiers' by pointing out just those individuals, institutions, or entities that own shares of common or ordinary stock in the firm in question (CFA Institute, 2008). 'Investors' and 'Financiers', correspondingly, refer to all individuals or institutions who seek opportunities for investment in shares and other securities of the firm being referred to. Theories mentioned above supports strategic ESG, as it is assumed that a firm's valuation can be affected materially by ESG risk factors.

2.2 Corporate Responsibility

The idea of responsibility is no longer a new concept in business literature; it is a matter that has been discussed for decades. The significance of responsibility and responsible acts has grown enormously in recent years. Niskala (2014) argues that in this changing world, technological developments have enhanced many methods in various businesses and industries. Subsequently, these developments had an impact on the process and the dimensions in which firms associate with their surrounding like society, personnel, and environment. For instance, the primary components and the scope of environmental obligations were not similar to what they are today; a great deal is greater understanding and consciousness of elements such as global warming.

Initially, recognizing the involvement of responsibility is essential, and the ways it has an impact on the businesses. There have usually been contradictory opinions regarding the significance and role responsible for making actions closer on the road to the more responsible and sustainable operation. A question that might arise in this regard is why any firm should behave responsibly, and how?

The concept of CSR is the most practiced concept in the corporate responsibility topic. CSR is often integrated within the sustainability subject. Although these two terms convey and describe dissimilar matters, they often are considered as synonyms. One of the critical aspects that differs between them is that CSR considers the company's current actions on a strategic stage, however, sustainability usually is viewed as a broader idea of how a firm is aware of its acts in the long term.

Moreover, the idea of environmental, social, and governance pictures both responsibility and sustainability. ESG was evolved from the investors' vision, who wanted the phrase to define these factors from a standpoint closer to their incentives. An impressive coverage in ESG is that it also takes into consideration the governance factor of the organization's responsible acts more profoundly. Later on, these factors will be introduced and described for the study in order to be clear in the sense of what will be examined later.

2.3 Corporate Social Responsibility

CSR is considered to be the most conventional concept concerning responsibility associated topics. The idea emerged when the need to determine the effect of businesses on societies was realized. The primary viewpoint was focused on risk management and used only to specify likely negative impacts to avoid inflicting them to society. Eventually, these views were modified into a more dynamic way, by deriving the advantages and positive effects that businesses are expected to deliver to society and thereby obtain profit (Carroll & Shabana, 2010).

CSR observes if the firm behaves responsibly. Many distinctive CSR concepts exist that make it tough to find a specific independent definition since the concept is very comprehensive. Therefore, there are several definitions for CSR despite the uncertainties in the approach that this term should be defined.

The idea of CSR goes back to the ’50s when Bowen (1953) introduced factors involving social responsibilities on a corporation in one of his books. It provided the foundation for future scholars. CSR in the ’60s and ’70s was mostly concentrated on the social elements and addressed necessary social moves and the actual meaning of social responsibility for business and society, which financial performance was not included, as firms weren’t seeking any returns (Carroll & Shabana, 2010).

During the past years, there have been developments in the definition of CSR; meanwhile, many subsidiary terms and theories were added to define its other components, like performance (Carroll, 1999). Carroll’s contributions in CSR are considered to be conclusive by many scholars. However, the implications of definition are various. Dahlsrud (2008) argues that having multiple definitions can twist productive discussions.

Five main dimensions of CSR that are most distinguished and which most definitions are being used consistently were found by Dahlsrud (2008) in his study of analyzing different CSR definitions. The dimensions include social dimension, economic dimension, environmental dimension, stakeholder dimension, and voluntariness dimension, which were found in a study of content analysis of different definitions stated in the literature. Carroll and Shaban (2010) followed that to reach a precise definition; also, four classes of CSR was viewed as these classes suggest a motive for each scope of CSR. They consist of economic, legal, ethical, and discretionary/philanthropic practices that business must work through (Carroll, 1979).

Vogel (2005) emphasizes on the new trend of CSR activities which could generally be recognized as the relationship between CFP and responsibility. In the philanthropic view, the link between profitability and CSR initiatives were minimal. Most CSR actions were raised from doing good for the society and was far from CFP goals (Kurucz, Colbert, & Wheeler, 2008). Along the way, the view completely shifted to generate profit from CSR, and firms became able to see how much they accomplished (Du, Bhattacharya, & Sen, 2010).

2.3.1 CSR and ESG

According to Kurcuz et al. (2008), there is a similarity between case for ESG and CSR which can be categorized into four parts including (1) reducing cost and risk, (2) toning up both legitimacy as well as credibility (3) generation win-win circumstances by creating synergistic value with stakeholders (4) to built competitive advantages.

These points of views can build not only a business case for CSR, but also it can be used for creating the ESG case (Carroll and Shabana 2010). Based on this view, both cost as well as risk reduction point of view could hypothesize that ESG could provide a base for a firm to recognize tax advantage or ignore sever regulation that could decrease its cost.

Apart from this, ESG activities could provide a base for its stakeholders by lowering the risk of resistance. Second authority, as well as reputation point of view, could keep the ESG activities and help a company for reinforcing its authority and reputation by representing competing desires of its stakeholders as well as operating profitability. As a result, a firm has opportunity to perceive as a part of its community; also, its function would be authorized. Third, better competitiveness point of view could argue that, a company has a chance to recover their reputational positioning, recover their ESG performance as well as profitability, create more desirable communication with its stakeholders, generate worker loyalty, decrease their turnover, get better attention of workers talent, generate buyers loyalty by better competitiveness arguments. Fourth, synergistic value creation may show opportunities for a company to hold that ESG and provide a base for it to complete the desires of its stakeholders as well as pursuing its profit targets.

2.4 Environmental, Social, and Governance

According to Carroll and Shabana (2010) the terms environmental, social as well as governance is a popular name, explicitly used by a group of investors to be aware of the worthy elements in CSR correlated functionalities. ESG considers the similar principals of both social as well as environmental operations. Apart from this, it reviews the governing functions of the firm. This demonstrates the firm's measurement, which explains the management process in various responsibilities. The governance features can assign the influence of the functions to the stakeholders. According to Lamberton (2005), additional consideration of the ESG concept could be mention as extra validation. Actions are mainly defined according to an accurate revision of sustainability. ESG mainly concentrates on the influence to establish sustainable function by accounting for accumulating benefits. Recognizing sustainable development is the purpose that firms use to demonstrate their financial functions (Weber, 2014).

Mooji (2017) examined the organizations, which measure ESG functions. The reason for this was to realize the most beneficial method for investors to assess firms' performance by ranking as well as rewards. On the other hand, the firms are baffling, because the extra amount of differentiation in rating convolutes the firm by confusing the profits came from the result. A preferable way for reaching ESG goals is to match with the firm's investors in values that are important and assess those goals that the firm wants to achieve.

Soyka and Bateman (2012) believe that generally, corporate sustainability is important, but the confront that are visible in the firms is to assess these matters with standardized indicators. Firms are tracking these functions in various ways with challengeable precession. The indicators have to be organized to get better information about the sustainable function and the measurable dimension. Especially, moving through the development requires the issues to be argued accountability and measure the present details in a precise way to be more profitable for the firm. Apart from this, issues moving towards ESG mainly observe from a risk mitigation viewpoint rather than creating the value point of view. This encourages most indicators to make risks and decrease the negative impacts. ESG indicators are set up to share priorities that influence the important features of the case sustainability in different ways, including costs, benefits, as well as buyer's relations. The measurement is different in various firms. As a result, many indicators used additional others in ESG disclosure (Soyka & Bateman, 2012).

2.4.1 ESG Defined

ESG is not only a constriction but also a construct, which explains three main areas including environmental, social as well as governance, that has a responsibility to measure the firm's aptitude to deliver sustainability. ESG is used widely, regularly with ethical implications, and is usually stated in the term socially responsible investment (SRI). ESG is considered nor financial, neither tangible element that use to assess a firm. Although ESG is broadly mentioned in different academic areas, the definition is not acceptable in the academic area (IFM, 2011). Present studies on ESG describes it as: strategic needs (Porter & Kramer, 2006), Social Responsible Investment (SRI) (SIF, 2007), Behavior (CFA Institute, 2008), Issues (IFM, 2011), Intangible measures (Bloomberg, 2009), Sustainability (Stewart & Brimble, 2009), Corporate Social Responsibility (CSR) (Harmon, Fairfield, & Behson, 2009),Factors, Investment methodologies.

All categorizations of ESG may be the most interesting part in representing ESG. However, a study on sustainability explains it as a development that meets present needs without compromising the ability of future generations to meet their needs". Although the description is broadly mentioned, it still is unclear. As a result, this classification of ESG makes the explanation of it difficult and shows that there is a need for a convincing definition. The lack of a clear definition of ESG confuses scholars and boosts the chance of gaining baffling impacts among ESG dimensions

(Mănescu, 2011). It also makes a reliable measurement of ESG more difficult (Marrewijk, 2009); as a result, lack of accepted definition university also boosts the possibility for inappropriate analysis (McWilliams & Siegel, 2000). These reasons could provide a base for a clear definition of the environmental, social, and governance.

ESG could be defined as procedures that is connected with an organization's relationship with the environmental surroundings, and it interacts with person organisms, and also the corporate system of both controls as well as actions including laws, customs, rules, to manage all the relationship in one organization and also to get other stakeholders' attention. ESG involved in a company's strategic planning could be various, especially for those who can link ESG elements to a company's future predictions. These firms could strongly evolve a competitive advantage, specifically when if others became unsuccessful in understanding the similar risks related to those elements (CFA, 2008). Stakeholder's strategy involves all vigorous engagement with a company's management on ESG activity, processes that can strongly decrease the risk and increase long-term value creation. This kind of approach provides a base for a strategic orientation, which allows differentiation, and improves the ESG performance.

2.4.1.1 ESG Performance

ESG Performance (ESGP) is explained as the success of EGS tasks deliberated against recognized standards of accurateness, completeness, the term cost, as well as speed. ESGP includes sub-constructs, governance performance (GP), environmental performance (EP), as well as social performance (SP).

2.5 Financial Performance

Financial performance (FP) could be described as a quantitative result of placing money in activities that are used for limiting probable negative impacts on business. Apart from this, it relates to sophisticated actions of a firm that ends to greater outcome in the firms. In order to measure CFP, a company has to face various ideas related to the choice of measurement. One aspect is to consider that the market measurement is the right ones (Alexander & Buchholz, 1978). At the same time other aspect believes accounting measurement are the better ones (Cochran and Wood (1984) ; Waddock and Graves(1997)) and some mention that both market and accounting measurement should be used together (McGuire, Sundgren, & Schneeweis, 1988).

Hillman and Keim (2001) suggest that scholars are discussing these measurements to assess CFP peculiarly, and their hypothetical meaning is diverse. In the past, they used accounting measurement to have a better plan for future profitability. They expected the investment to return from fairness securities of the firm while the market measurement was used to compare the market value of the firm's profit stability (Tayeh, Al-Jarrah, & Tarhini, 2015). As a result, this study considers an accounting measurement as Return on Asset (ROA). According to Prastowo (2002) this concept uses for an efficient firm measurement in creating income by using its property.

2.5.1 ESG and Accounting Measures of Financial Performance

After all, a study on the connection between both financial and social scopes has seemed to be questionable (Griffin & Mahon (1997); Roman, Hayibor, & Agle (1999)). Researchers on this subject are trying to find the impact of ESG elements on CFP (Surroca et al., (2010); Lourenço & Brancoc (2013)). Waddock and Graves (1997) suggested that it is probable to find a positive linkage between CSR as well as company financial performance, also the negative linkage between them, and finally, there are no linkages. A positive linkage arises while a company has acceptable CSR and is able to recruit talented personnel (Greening & Turban, 2000). A negative linkage could come about if focusing on CSR is somehow devastating the value. The reason for such thing is, when spending resources on these kinds of activities, the increased revenue is not gained. Apart from this, these activities and behaviors cause difficulties for directors to reach the company's desirable potential.

As a result, there is no visible linkage between CSR as well as financial performance that the positive or negative impact, which net off may be the result. In addition, there is no prove that shows the value-creating potential of CSR differs in companies so for such a reason the benefits go beyond the costs, or because its insignificance with unimportant effects on costs as well as revenues compared to other elements that seem to have more effect on business activity. For instance, in the research of Halbritter & Dorfleitner (2015), the ESG portfolios did not demonstrate important return dissimilarities between firms attribute both in high as well as low ESG. Although researches are concentrating on community revelations definition that is smaller, different researches have examined if environmental disclosers are worthy for shareholders. This is possibly amazing as community disclosures when stakeholders could have more concern about it and especially current employees who will be influenced by subjects such as variety and employee safety. The early study concentrated on if there is an existed contemporary linkage between social reporting as well as financial performance using, but they have no ability to discover any affiliation (Abbott & Monsen, 2017) (Also see: (Belkaoui & Karpik, 1989); (Freedman & Jaggi, 1988)). There are various expectations believing that good environmental performance companies were positively connected with profitability (Bragdon &

Marlin, 1972). There is a possibility that shows the linkage between social disclosures as well as profitability has changed. Apart from this social responsibility in firms, practices have steadily considered improper among stakeholders.

In a cross-sectional research, Waddock and Graves (1997) found that there is a linkage between social as well as financial performance, by using three accounting variables such as return on equity (ROA), return on sales (ROS) finally return on assets (ROA), for the purpose of measurement. Researchers recognized that one year covered CSR has important clarifying control on ROA, less control on ROS, and no control for ROE. Study found that lagged accounting variables have control of the next CSR figures.

According to Stevens (1984), companies that are showing the high level of environmental damage mitigation cost has the capability to experience less return than those with lower costs. There is a possibility that CSR grounds decreases when better performance applies to it. As a result, a company could have a good financial position to use in CSR-related activities. Companies may make intended disclosures for limiting the information indiscretion that exists between both internal and external stakeholders.

An extra subject is to limit the causal relationship. Companies boost spending on CSR while expecting superior monetary performance in the future; preceding results neglected an important variable, specifically the confidential data that directors have about the how firm is going to perform in future (Lys, Naughton, & Wang, 2015).

Al-Tuwaijri, Christensen, and Hughes (2004) inspected the linkage between both environmental and economic performance in a cross-sectional parallel equations approach, estimation of the connection can be harshly partial if the endogen is not usable for, explanation of the findings in preceding assessments of the linkage between the mentioned variables. According to Ullmann (1985), this provides a base for them to detain the impact of all variables on the management strategy. Al-Tuwaijri et al. (2004) recognize that there is a positive connection among three variables. This positive correlation improves operation performance for US companies in both computers as well as the electronics segment in a long-term period (Al-Tuwaijria, Christensen, & Hughes, 2004).

According to Hart (1995) natural resources-based theory, starting innovative technologies is beneficiary for companies. Hart believed that as various developments in environmental behavior were rigid necessities more than voluntary; they raised companies cost. However, revenues increased supplementary, it last about two years for investors to make their payments for such activities.

The proper environmental performance results in better ROA (Russo & Fouts, 1997), and an appropriate environmental performance enhances revenues, profitability, as well as market share. The reason for such a thing is boosted product demand and customer loyalty. Xie et al. (2019) in a very recent study evaluated the efficiency of corporations and researched its nonlinear relationship with ESG disclosure in which they found a nonnegative relationship. Also, Taylor et al. (2018) found that the value of companies can moderately increase by disclosing CSR information. Through such findings, not only the positive effect of CSR on environmental initiatives is clear, but also its contribution to generating value can be seen.

Brogi & Lagasio (2019) found that profitability in banks is linked with a significant and positive relationship with ESG and environmental awareness. Similarly, Yu and her colleagues (2018) found that as companies disclose ESG data more, their evaluation measures, such as Tobin's Q, is better. Furthermore, many studies propose that companies which more asset, liquidity, greater R&D, less insider holdings, and better past financial performance tends to easier report ESG issues. All are supporting that ESG reporting will lead to better financial returns (Weber, Diaz, & Schwegler, 2014), (Fatemi, Glaum, & Kaiser, 2018).

Similarly, Zhao, et al. (2018) found that good ESG performance can indeed improve financial performance, which has significant meanings for investors, company management, decision-makers, and industry regulators. Yoon, Lee, & Byun (2018) found the effect of CSR practices positive and significant on a firm's market, verifying a positive CSR-valuation relationship in emerging markets, which provides substantial policy and welfare implications in markets where governments play a major role in promoting CSR. Cheng, Ioannou, & Serafeim (2014) found better CSR performance leads to lower capital constraints.

In Qiu, Shaukat, and Tharyan (2016) research, data development analysis has been used to estimate corporate effectiveness, and consider the nonlinear connection between corporate effectiveness. Although many scholars believe that, this matter may be connected to probable measuring in environmental performance, they were somehow unable to find any linkage between both environmental disclosures as well as profitability in UK companies. They recognized that those companies making social disclosures have a tendency for better market values. In addition, they show more interest to anticipate future cash flows. Raise in compulsory reporting expected to unfavorably affect profitability by growing costs since companies' behavior reasonably reported (Qiu, Shaukat, & Tharyan, 2016).

Disclosure rule explains which superior companies should work harder to sign their benefit, and frail performing companies will be put under pressure to improve their standards. Ioannou and Serafeim (2016) suggest that improvement in expositing novel policies boosts company valuations. This well boost invention costs and therefore reduces profitability (Patten, 2002). Sikka (2010) suggests in an article related to companies' motivations for involving in society responsible behavior there is an existence of an obvious contradiction between the policies documents those companies stating their purpose to perform in a socially responsible way with regard to their participation in ignoring tax is observed as 'organized hypocrisy'.

Sikka (2010) believed that various firms have no tendency to observe the money, which is paid, the taxes as a community responsibility, but it is examined as a serious cost. Researcher argues that CSR declaration forms an exterior effort to keep the company from a breakup, which may occur from any uncertain performance that includes in it. As a result, companies are trying to boost their position based on community responsibility as protection; therefore, any tax transgressions that consider as being public has fewer reputational damage. As a result, firms could perform strongly on CSR grounds as well as sustainability disclosures to 'Greenwash' over those areas where behavior is less.

Lanis & Richardson (2012) papered a negative connection between both CSR disclosure levels and effectual tax rates even as Hoi, et al. (2013) discover that when companies are socially responsible have extra tendency to connect in tax covering actions and are insistently evading taxes after having a proper control on the effect of further elements. According to Kim and Venkatachalam (2011) when firms involved in activities such as gambling, alcohol production business demonstrates superior disclosure performance than the same one in other sectors.

There is a linkage between higher levels of social responsibility with superior integrity in more traditional accounting measurement, including a low number of possibilities in making use of optional accretion to control earning as well as to operate activities and decreased the base for rigid study (Kim, Kang, & Mattila, 2012). By viewing the evasion of the corporate tax as a feature of the company's communal act, it is significant to find out the effect on its financial performance. Even though the proof on this subject is more questionable, the consensus shows a little linkage between tax avoidance as well as stock market performance (Brooks, Godfrey, Hillenbrand, & Money, 2016). Those companies that pay the least manufacturing attuned tax rates facing additional stock market risk (Guenther, Matsunaga, & Williams, 2016).

2.5.2 Corporate Social Performance and Financial Risk

The stakeholder's theory gives proper support that explained the positive linkage between both CSP along with financial risk. The improvement in CSP will help to value development to persist lessening the risks (Clarkson, 1995). In a study Godfrey (2005) suggests that CSP have the capability to create a convinced 'moral capital'. This helps the firm's reputation as long as the company discovers itself in the middle of disagreements. This provides a base for the firm has a superior chance for keeping its honesty and conserve its rational prosperity with the stakeholders (Godfrey, 2005).

Orlitzky and Benjamin (2001) used risk performance metrics and to measure the fiscal effect on CSP with no extra attempt to recognize if this effect was related to boosts proceeds, less weakness risk, or both. Meta-analysis in the study shows an important mean true score connection, which is negative between both CSP as well as the risk. In addition, it implies that the connection is more powerful for the market-based measurement or risk against accounting-based measurement.

Since 15 years, there have been various attempts to talk about this subject with numerous studies mainly focuses on the connection between both CSP and financial risk. Better CSP for managing the risk helps both lawful and regularity action that taking in opposition to companies (Godfrey, Merrill, & Hansen, 2009). Sharfman and Fernando (2008) concentrated on company environmental act and demonstrated that it can direct to a reduction cost of capital throughout diverse ways such as a reduction in systematic risk. The authors confirm the preceding results for an ample board data example by both conservative and problematic risk metrics. study discovered that the negative risk increasing impact of other social as well as environmental disagreement becomes more powerful during the higher market instability. Luo and Bhattacharya (2009) balanced the mentioned examination by focusing on the impact of CSP on individual company risk and discover a negative relationship involving the two notions.

In contrast, Bassen et al. (2006), Cheng et al. (2014) found positive associations between best ESG practices and the risk profile of a company. It is worthy to the point that the mentioned study examines the linkage between CSP along with risk by means of applying equity markets as the applicable monetary laboratory. Apart from this, there is proof for examining other assets. Corporate connections of companies with better environmental as well as CSP potency contains superior credit ratings, and as a result, it inferiors yield when the precise opposite is right for companies with more environmental concerns. All the results are reliable through the novel work of Goss (2009). Researcher explained that CSP is considering being determinative of fiscal distress. Finally, the opposite CSP- risk affiliation have an equal position in the real estate market (Eichholtz, Kok, & Yonder, 2012). They recognize that the real estate venture that explains a superior share of 'green' properties have lower market betas.

2.6 BRICS

O'Neill (2001) believed that BRIC would get beyond the economics of the west by the help of countries such as India, Brazil, Russia, and China by 2040. The total GDP of the mentioned countries quadrupled from 2000 to 2010, rising from US$3 trillion to US$12 trillion. O'Neill (2012) believed that BRICS have a better opportunity for efficiency growth than in developed countries. We can say that countries with younger labor have a greater potential to produce GDP growth. Nonetheless, the pressure is increasing for fewer conventional improvement. This development is visible in the capital market of countries such as Africa and Brazil.

As previously mentioned, ESG features have an influence on not only the risk profile but also on the financial returns of firms (see: (Orlitzky & Benjamin, 2001); (Bassen, Meyer, & Schlange, 2006); (Hong & Kacperczyk, 2009); (Cheng et al., 2014)). Various studies are focusing on the impact of ESG on the business risk for economic development (Richardson & Welker, 2001); (Dhaliwal, Li, Tsang, & Yang, 2011). Lockett et al. (2006) suggest that 89% of hypothetical articles are categorized as non-normative, while the balance of CSR in developing countries is consistently on debate.

There are various numbers of articles on the role of business in improvement which are used for vital point of view (Blowfield & Frynas, 2005). According to Raynard and

Forstater (2002), it is obvious that in developing nations, responsible management is distinguished by assistances of local imperative that basis to the society. Those directors who have responsibilities for firms that are situated in these regions are experiencing an immense challenge; they are facing global standards of the international markets while meeting authorized infrastructure failure. Various economics are at various level of development with changeable complexity in both civil and society, that is why firms are at a different level of corporate maturity.

Chapter 3

METHODOLOGY, HYPOTHESES, AND DATA

3.1 Introduction

This study uses ESG scores as a major index for evaluating Corporate Social Responsibility performance and explains the relationship between CSR and corporate financial performance based on stakeholder theory arguments in a handful of emerging economies labelled the BRICS – an acronym denoting Brazil, Russia, India, China, and South Africa.

There is inconsistency in the findings of previous studies, which makes this topic worthy of taking on additional research since more assessments with various methods could add to the total subject of study. We have measured CSR performance by ESG score provided by Thomson Reuters Eikon and financial performance by ROA (see Dowell, Hart, & Yeung (2000); Maurya & Pajuste (2005); Cheng, Ioannou, & Serafeim (2014)). Following the literature reported in chapter two, the hypotheses of this thesis which we want to address are given below:

H1. Overall ESG performance has a statistically significant impact on the financial performance of firms in BRICS countries.

Assuming the disaggregation of the ESG performance proxy, hypotheses H1a, H1b, and H1c are proposed as constituents of H1:

- H1a. Environmental performance has a statistically significant impact on the financial performance of firms in BRICS countries.
- H1b. Social performance has a statistically significant impact on the financial performance of firms in BRICS countries.
- H1c. Corporate governance performance has a statistically significant impact on the financial performance of firms in BRICS countries.

For a study to be examined, we can use three main research methods: quantitative, qualitative, and mixed-method (Venkatesh, Brown, & Bala, 2013). The quantitative method and nonexperimental design are suitable for our research.

Quantitative method is mostly used by the researchers when the aim is to evaluate the relation among numeric variables against recognized theories (Dinsmore, 2014). This study attempts to specify if there is a relationship between CSR performance and CFP. The purpose of this thesis is to test statistical data and not to explore a human variable, which states a quantitative method instead of qualitative (Marshall & Rossman, 2014). According to literature, if the association between ROA and ESG scores are positive, it will validate stakeholder theory. If relation results were negative, the relationship cannot validate stakeholder theory (Aguilera, Rupp, Williams, & Ganapathi, 2007) (Unerman & Chapman, 2014).

As we choose the quantitative method, we have two primary pathways: experimental and nonexperimental (Dinsmore, 2014). As we do not collect descriptive statistics (minimum, maximum, and mean values…), performing an experiment is not going to be employable for this study. Nonexperimental methods are consisting of correlation studies (Qi-Yi et al., 2013).

3.2 Data and Variables

For collecting the data, we considered the list of companies from emerging countries, the BRICS in particular, comprising Brazil, Russia, India, China, and South Africa. After this filter, because of missing data for small companies, we selected our companies based on their market capital, and we chose the ones greater than 1 billion USD. The total panel data contained 1420 observations from 292 companies for five years, over the period of 2014 to 2018.

We collected data from two databases. We are first using Thomson Reuters Eikon which composed the independent variables of the Eq (1), as described in the methodology section, about the company's performance in three pillars of environmental, social and governance, or the overall ESG scores. Also, we collected our variables about the company profile from DataStream, for the dependent variable and control variables. There has been no question about the trustworthiness of these two databases, neither among corporate information users nor scholars, as Cheng et al. (2014) argue.

Thomson Reuters ESG Scores measure companies' ESG performance based on reported data in the public domain across 3 pillars and 10 different ESG topics. Thomson Reuters captures and calculates over 400 company-level ESG measures, of which they have carefully selected a subset of the 178 most relevant and comparable data points to power the overall company assessment and scoring process. The underlying measures are based on considerations around materiality, data availability, and industry relevance. The three ESG pillars are: a) the environmental performance score, b) social performance score, and c) corporate governance performance score (REFINITIV, 2018).

We used four independent variables for our empirical model: Overall ESG score, Environmental pillar score, Social pillar score, and governance pillar score. For our dependent variable at the company level, we used Return on Assets (ROA) which was mostly used in the finance literature (Dowell et al., 2000); (Maurya & Pajuste, 2005); (Cheng et al., 2014). We also added control variables, size (total assets) and debt-to-equity ratio, to be accounted in our results for a more comprehensive number of factors.

We considered companies in BRICS from Thomson Reuters Eikon database. Despite the fact that the data for ESG indexes are available from 2001, for the companies in BRICS, it dates back to 2007. Due to missing values of companies for emerging countries in the database, for the purposes of the sample of this work, we decided to use the period of 2014-2018.

3.2.1 Variables Explanation

The variables for analyzing are described as follows: Return on Assets (ROA) is the ratio of the net income of a company to the value of its asset. Using this ratio, one can measure and contrast the profitability of several firms across the same industry (Garcia, Mendes-Da-Silva, & Orsato, 2017). ROA is employed as a financial performance measure based on accounting indicators as our dependent variable in the regression model.

Next variable is environmental, social, and governance performance (ESG), which we employed as an independent variable in the regression model to investigate whether it affects the company’s financial performance. ESG Scores in Thomson Reuters database are designed as an objective, and transparent measure of a firm’s ESG performance shows how much they are committed and competent within 10 basic themes (emissions, environmental product innovation, human rights, shareholders, etc.) based on the information that company itself reports.

The debt-to-equity ratio (D/E) shows the firm’s capital structure and its attributes of riskiness. It counts as the critical measure for the performance of the firm financially. As the D/E of a firm which generates profit well stays within a sensible level, mostly it has potential to influence CFP (Zhao, et al., 2018). We employed D/E as one of the control variables in our model.

Also, another essential attribute in CFP is size. Usually, it is considered as assets or total sales (Zhao, et al., 2018). In this thesis, we obtained the Log of total assets (Log TA) as a representation of the size, another control variable in our model.

3.3 Methodology

The objective of this thesis is to investigate whether there is an association between a company’s performance in CSR, measured by ESG scores, and its financial profile within the BRICS economies. Based on the variables that we selected and employing panel data regressions, the model to be tested is presented below in Eq(1), with N = 1420 and T = 5.

$$ROA_{it} = \alpha_0 + \alpha_1 ESG_{it} + \alpha_2 DE_{it} + \alpha_3 Log\ (TA)_{it} + \varepsilon_{it} \qquad \text{Eq(1)}$$

Where ROA explains the return on assets, ESG shows the overall ESG score, DE shows the debt-to-equity ratio, and TA is total assets. ε_{it} is the error term. As alternative cases, we replaced: 1. environmental pillar score (ENV), 2. social pillar score (SOC), and 3. Corporate governance pillar score (GOV), instead of ESG in the Eq(1) separately. The aim is to investigate the significance of each of these three scores in the proposed model.

Firstly, we analyzed the correlation between the variables. Rudestam and Newton (2014) in their study suggested, when the aim is to predict a relation of two or more groups as a single group, a correlational design should be utilized. The correlational design investigates how strong are the relationships between variables (Field, 2013). The data were interpreted with a Pearson's Correlation Coefficient (r) for the value of ROA that is the dependent variable. The r can be utilized for specifying the linearity and strength connecting quantitative variables, in which r equals 1 means total positive correlation and r equals -1 means total negative correlation (Green & Salkind, 2016); (Yang, Liu, Tsoka, & Papageorgiou, 2016).

We conducted an ordinary least square analysis on our panel data. Linear regression is proper to use when the variables are normally distributed (Sainani , 2013). Hazra and Gogtay (2016), believed we should use this statistical model for decision making about the connection between the independent and dependent variables. The non-experimental design, coupled with the advanced correlational technique, linear regression, is suitable to reach a favorable outcome with respect to the characteristics of the hypotheses that we want to test.

To demonstrate the linear regression is meaningful, we carry out several unit root test on our variables. Unit root test tests whether a time series variable is non-stationary and possesses a unit root. A unit root test for the panel is called Levin-Lin-Chu (2002) (or LLC) which assumes all observations are at a class of integration, which is homogeneous. Maddala & Wu (1999) found some alternative descriptions of the unit root and used different panel unit root methods. Imp, K., Pesaran, M. H., & Shin, Y. (2001) (or IPS) came up with a similar test. However, Kaddour (2000) proposed a different hypothesis. He put being observations of panel stationary, derive of a lack of a unit root. Moreover, we used the EVIEWS version 10 software to regress the selected variables and analyze them.

The outcome of analyzing the data may or may not be in line with stakeholder theory with correlation of ESG performance, or CSR performance, to CFP. If the correlation is positive and significant, it supports the existence of a relationship between ESG performance and CFP for the firms in BRICS. If it shows negative or nonsignificant, it will not support the relationship between CSR initiatives and financial performance.

Chapter 4

EMPIRICAL RESULTS

As mentioned in the previous chapters the objective is to examine the impact of ESG scores on ROA. Before running the regression, we have shown the correlation among the variables, unit root tests, variance inflation factor test. The results of our analysis are presented below.

Table 1: Correlation Matrix Analysis

Correlation Probability	DE	LTA	GOV	SOC	ENV	ESG	ROA
DE	1.000000 -----						
LTA	0.166383* (0.0000)	1.000000 -----					
GOV	-0.015451 (0.5607)	0.002679 (0.9196)	1.000000 -----				
SOC	0.007691 (0.7721)	0.053759** (0.0428)	0.306903* (0.0000)	1.000000 -----			
ENV	0.014670 (0.5807)	0.228458* (0.0000)	0.289112* (0.0000)	0.700143* (0.0000)	1.000000 -----		
ESG	0.004285 (0.8718)	0.123462* (0.0000)	0.633723* (0.0000)	0.870697* (0.0000)	0.855391* (0.0000)	1.000000 -----	
ROA	-0.249054* (0.0000)	-0.455349* (0.0000)	-7.24E-06 (0.9998)	0.031174 (0.2404)	-0.031946 (0.2289)	-0.000972 (0.9708)	1.000000 -----

Note1: The number in the parenthesis are P-values. *Note2:* *Significant at the level of $p<0.01$; **Significant at the level of $p<0.05$

The correlation matrix for the linkage between the dependent ROA and independent factors is demonstrated in Table 1. We can see that the linkage between Overall ESG score and ROA is not significant and negative (r = -0.000972, p<0.05), likewise, Environmental pillar and ROA have a non-significant and negative relation (r =-0.025531, p< 0.05). However, the relationship between Social pillar and ROA is positive and again, not significant (r =0.036951, p< 0.05). Same as the relationship between Corporate Governance pillar and ROA (r =0.002098, p<0.05). When dealing with social sciences, low correlation of dependent variable and independent variables are relatively common, according to Lattin et al. (2011) and Garcia et. al (2017). Also, the correlation outcome for the size of the firm and its relationship with the profit shows a negative and significant (r=-0.166383, p<0.05) similar case with the D/E (r=-0.247245, p<0.05).

Other findings from our correlation matrix uncover a positive and significant linkage (r=0.166383, P<0.05) between the company size and its debt-to-equity ratio which means as the company gets larger, the financial leverage of the company is higher. In addition to that, it worth mentioning that for our sample companies, size also is positively related to the ESG scores (except corporate governance) which are in line with studies of some scholars like Deegan and Gordon (1996) and also Baron (2009). However, as we described earlier, the relationship between ESG scores and profit was not significant.

We ran a variance inflation factor test (VIF), and it shows no correlation among the predictor variables as in the result, there was no sign of multicollinearity. In the analysis that we ran all the values that we measured are far lower than the multicollinearity limit of 10. Values higher than 10 represent substantial correlation among the independent variables (Craney & Surles, 2002).

Table 2: Unit Root Tests

Variable	IPS Test statistics (P-Values)	LLC Test statistics (P-Values)	ADF-Fisher Test statistics (P-Values)	PP-Fisher Test statistics (P-Values)
ROA	-27.9268(0.00)	-232.533(0.00)	1030.40(0.00)	1208.05(0.00)
ESG	-10.7670 (0.00)	-45.7471(0.00)	806.121(0.00)	974.637(0.00)
ENV	-7.49319(0.00)	-55.7973(0.00)	718.852(0.00)	919.534(0.00)
SOC	-5.90419(0.00)	-29.6575(0.00)	703.919(0.00)	868.601(0.00)
GOV	-13.1080(0.00)	-61.9183(0.00)	871.156(0.00)	1054.02(0.00)
TA	-6.39164(0.00)	-42.9009(0.00)	646.913(0.00)	847.764(0.00)
DE	-34.3151(0.00)	-260.088(0.00)	777.439(0.00)	976.044(0.00)

Note: Null hypothesis: There is unit root problem.

We conducted a unit root test on our variables shown in Table 2. We demonstrated the panel unit test outcome with four methods: i) IPS; ii) LLC and iii) ADF-Fisher, iv) PP-Fisher tests. IPS and ADF-Fisher obtain individual unit root processes. However, LLC considers a common unit root flow through the cross-sections. PP-Fisher differs from ADF-Fisher as it ignores any serial correlation. All of these tests assume a null hypothesis that a unit root exists. Our results indicate that the variables were stationary, the null hypothesis was rejected, and there was no need for further examination.

Lastly, we employed four distinct linear regression analyses to investigate the proposed hypotheses. The results of the effects of the independent variables that we chose on the CFP was estimated by Panel Least Square and are shown in Table 3 (the overall ESG score is the independent variable), in Table 4 (the environmental pillar score is the independent variable), in Table 5 (the social pillar score is the independent variable); and finally, in Table 6 (corporate governance pillar score is the independent variable).

Table 3: Linear regression analysis Panel OLS with ROA as dependent variable

Variable	Coefficient	t- Statistic	Prob.
C	0.448054	20.80769	0.0000
ESG	0.000210	2.278868*	0.0228
LTA	-0.017022	-18.27346	0.0000
DE	-0.005257	-7.551904	0.0000
R-squared	0.241012		
F-statistic	149.8805		

Notes:* is significant at $p<0.05$ significance level; ESG is the overall ESG score the independent variable; Control variables: LTA is Logarithm of Total Assets, and DE is Debt-to-Equity ratio.

In the next step, we ran a regression analysis on our model for the dependent variable ROA and independent Overall ESG score. From Table 3, first, we can see that Overall ESG score is statistically significant at the 5 percent significance level, and when ESG increases by 1 percent, ROA will only increase slightly by 0.0002 percent. This positive effect can be explained by reducing cost and risk while pursuing ESG activities as they help the company to enjoy tax benefits or lessen strict regulation, that results in lower cost hence higher profit. So, our findings confirm our hypothesis H1 in which we assumed ROA is associated with the overall ESG performance. This result is consistent with a previous study of Zhao, et al. (2018) on China's listed power generation companies. The relation between LTA with ROA is negative, and it is strongly significant when LTA increase by 1 percent ROA will decrease by 0.02 percent approximately. Similarly, DE has also a negative relationship with ROA. The significance level is at 1 percent, and a 1 percent increase in DE leads to a 0.005 decrease in ROA, which is not surprising as firms with higher financial leverage will maintain less profit. The value of R-squared for our regression is 0.241012, which shows that our independent variables can explain the dependent variable (ROA) by 24%. Lastly, the value of F-statistics is 149.88, which is higher than estimated F-statistics and shows that our regression is highly significant.

Table 4: Linear regression analysis Panel OLS with ROA as dependent variable

Variable	Coefficient	t- Statistic	Prob.
C	0.456157	21.29106	0.0000
ENV	0.000225	3.018479*	0.0026
LTA	-0.017414	-18.36426	0.0000
DE	-0.005232	-7.525627	0.0000
R-squared	0.243098		
F-statistic	151.5949		

Notes:* is significant at p<0.05 significance level; all the coefficients are standardized beta. ENV is the Environmental pillar score the independent variable; Control variables: LTA is Logarithm of Total Assets, and DE is Debt-to-Equity ratio.

Table 4 shows our regression analysis for dependent ROA and independent ENV. The relationship between ROA and ENV (environmental performance) is also statistically significant. The coefficient of ENV is 0.0002, that means 1 percent increase in ENV will result in 0.0002 percent increase in ROA. This proves our H1a hypothesis in which there we assumed there is an association between the environmental performance and the ROA.

Although some debate the increase in cost for being an environmentally considered firm, it is proved that in a lot of cases the path to becoming environment-friendly for businesses is actually pretty rewarding and the short-term costs will be covered by the benefits that it brings from different sources especially in the long run. The value of R-squared for our regression is 0.243098, which shows that our independent variables can explain the dependent variable (ROA) by 24%. Lastly, the value of F-statistics is 151.5949 and shows that our regression model is highly significant.

Table 5: Linear regression analysis Panel OLS with ROA as dependent variable

Variable	Coefficient	t- Statistic	Prob.
C	0.446827	20.71247	0.0000
SOC	0.000171	2.398116*	0.0166
LTA	-0.016876	-18.23630	0.0000
DE	-0.005281	-7.589243	0.0000
R-squared	0.241309		
F-statistic	150.1245		

Notes:* is significant at $p<0.05$ significance level; all the coefficients are standardized beta. SOC is the Social pillar score the independent variable; Control variables: LTA demonstrates Logarithm value of the Total Assets, and DE is Debt-to-Equity ratio

From Table 5, our regression analysis for dependent ROA and independent SOC. The relationship between ROA and SOC (social performance) is also statistically significant. The coefficient of ENV is 0.00017, that means a 1 percent increase in SOC will result in 0.00017 percent increase in ROA. This proves our H1b hypothesis in which we assumed social performance is associated with ROA, and we see that good social practice influences the firms' profit levels.

The value of R-squared for our regression is 0.2413098, which shows that our independent variables can explain the dependent variable (ROA) by 24%. Lastly, the value of F-statistics is 150.1245, which is higher than the estimated F-statistics and shows that our regression is highly significant.

Table 6: Linear regression analysis Panel OLS with ROA as dependent variable

Variable	Coefficient	t- Statistic	Prob.
C	0.453178	20.78759	0.0000
GOV	-5.29E-06	-0.069874	0.9443
LTA	-0.016758	-18.09706	0.0000
DE	-0.005284	-7.577085	0.0000
R-squared	0.238231		
F-statistic	147.6102		

Notes:* is significant at $p<0.05$ significance level; all the coefficients are standardized beta. GOV is the Governance pillar score the independent variable; Control variables: LTA is Logarithm of Total Assets, and DE is Debt-to-Equity ratio.

From Table 6, our regression analysis for dependent ROA and independent GOV. Surprisingly, the relationship between ROA and GOV (governance performance) is not statistically significant. So, we reject H1c hypothesis in which we assumed governance performance is associated with ROA. This outcome can be explained by the fact that our sample data is from emerging economies in which they usually fail in their legal infrastructure and the cultures do not support the responsible business. As a result, the managers of the companies operating in these nations are struggling to meet international standards of the global market which is not surprising since their actions are usually judged by their contributions to local norms or religious values.

The value of R-squared for our regression is 0.238231, which shows that our independent variables can explain the dependent variable (ROA) by about 24%. Lastly, the value of F-statistics is 147.6102, which is higher than estimated F-statistics and shows that our regression is highly significant.

Chapter 5

CONCLUSION AND IMPLICATIONS

5.1 Conclusion

In most of the corporate finance literature, the shareholder profit maximization is a key objective, and social contributions are not considered to be beneficial. However, in the current business world, taking a broader view of corporate goals is crucial. In a more modern view, taking into account the corporations' stakeholders needs is a must although it often raises pressures on firms to strengthen the positive impacts of the externalities and lessen the negative ones (Sarkis, Ginzalez-Torre and Adenso-Diaz 2010). This brings the topic of corporate social responsibility, sustainability, and extra-financial factors – namely environmental, social, and governance of companies, to the discussion.

Vogel (2005) emphasizes on the new trend for CSR activities which are generally recognized as the relation of CFP and responsibility. In the philanthropic view, the link between profitability and CSR initiatives were minimal. Most CSR actions were raised from doing good for the society and was far from CFP goals (Kurucz, Colbert, & Wheeler, 2008). Along the way, the vision completely shifted to generate profit from CSR, and firms were capable of seeing how much they obtained (Du, Bhattacharya, & Sen, 2010).

As explained in the literature, we cannot quantify CSR; however, we can measure it using proper indexes. The one that we believed is more appropriate for this study is the ESG score. ESG tries to demonstrate a firm’s performance in environmental, social, and corporate governance actions.

We chose to study on BRICS countries since the CSR literature was limited, and the results were ambitious compared to studies on developed countries (Dobers & Halme, 2009); (Baughn, Bodie, & McIntosh, 2007). BRICS countries are essential: greater than 75% of the global income annual growth is counted for developing and emerging countries, and about 50% of this number is for the BRICS alone. Since 2008, the five BRICS have accounted for more than half of the global growth (while the developed nations for only 22 percent). Unsurprisingly, they also account for the rapid growing shares of both global trade and investment. The BRICS share of world trade is now approaching 20%, which has nearly been tripled during the last two decades. There is increasing opportunity—and necessity—for the BRICS and other emerging and developing countries to play a more active role in shaping the world economy. More robust BRICS investment and growth are likely to raise output in all countries, including in developed countries (Reddy, 2018).

However, the conditions that prevail in these countries is not flawless. National institutional settings, like incapable governments; lack of proper transparency and public governance; arbitrary enforcement of rules, regulations, and policies; and low levels of safety and labor standards, have an impact on conceiving and practicing CSR in developing nations. These differences, along with the mentioned essential characteristics of these countries, make the study on these countries worthy.

Using ESG score as a measure of CSR for the independent variable, and ROA, the variable mostly adapted for CFP in the finance literature, as a dependent variable, we studied whether there is an association between CSR and CFP of corporations located in BRICS countries. We employed the stakeholder theory as a basis for our hypotheses.

The data were collected from Thomson Reuters Eikon and DataStream for 292 companies in BRICS from 2014 through 2018. We assumed that there is a positive and statistically significant relationship between ESG scores and ROA, and we extended our hypothesis into three sub-hypotheses for each element of ESG – environmental score, social score, and governance score – for a more specific view. The Ordinary Least Square regression model was used with 1420 observations of dependent ROA and independent ESG also, we controlled our model for the company size and financial leverage for better results.

The results of this thesis indicate that with today's condition of the market, companies located in BRICS countries will be able to earn more profit through enhancing their ESG performance. Our main hypothesis for the relation between ROA and overall ESG score and our sub-hypotheses the case for environmental and social scores were confirmed. However, our last sub-hypothesis for the association between governance score and ROA was rejected. For our sample countries, it seems that governance practices are not contributing to the financial performance of companies as much as the social and environmental practices are.

The stakeholder theory of Freeman (1984) is the basis of the theoretical framework in this thesis. Stakeholder theory helped managers to realize that a framework can be applied in which not only stakeholder's interest be satisfied, but also a maximum profit can be achieved. Advocates of this theory like, Baird et al. (2012) and Dinsmore (2014), believe that providing both classes of needs could generate more significant value than by considering only one class of needs.

Considering stakeholder's theory, some might criticize that insignificancy of the correlation results in the matrix, indicates that funding ESG activities are not logical (Bazillier & Vauday, 2014). However, we can see that stakeholder's theory also suggests taking into account more than just the financial earnings (Barchiesi & La Bella, 2014). Corporations need to look for new ways to fulfill stakeholder needs as they balance the negative impact of production and operations (Rahman & Post, 2012).

By use of correlational study design as a basis, results can motivate managers to reflect the policies and procedures that are in line with ESG activities. Investing in CSR initiatives could be an option if direct proof of advantages to the company or better CFP was concluded as in this study. The results are very practical for decision-makers, like managers and investors.

The topic that we discussed was very limited regarding the academic CSR literature, especially for emerging economies, which adds an agenda for the future researchers: This study can be repeated for other emerging countries or limited to a specialized industry sector, it can be extended in terms of period if more recent data became available, it is also good to be tested with other estimation methods.

5.2 Limitations

This study is limited to the secondary data extracted from the Thomson Reuters database, which is also limited by the number of BRICS firms that file their ESG report. On the other hand, the ESG data is not available for an extended period of time.

Furthermore, it is difficult to generalize results based on existing literature since there is inconsistency among control variables as well as financial variables used to determine the CFP. As for measuring CFP, the usage of market measurements instead of ROA, the accounting measurement that we used, could be more suitable. Therefore, while we review the previous studies that either agree or disagree with our findings, we should consider other factors that may affect the results such as methodology employed, the analysis of variables, the country situation and utilizing the economic indicators in the model.

5.3 Implications

Based on the results of this study, we can confirm that the implementation of ESG activities are contributing to positive financial performance. Management must notice that stakeholders are observing their actions. They are evaluating what moral and ethical codes does the company follow to earn a profit. This case is not only valid for the stakeholders but also covers the scholars and government policymakers. So, it is quite understandable that managers should be challenged to consider which elements of ESG activities is worth investing in financially. However, ESG activities are not always pursued to gain some level of profit, instead the value that it will bring to the stakeholders and whom the company serves, as suggested by Freeman (1984) to engage in what all the stakeholders care for, not only to the interest of shareholders.

The dynamic environment of business world has always been concerned with society (Bazillier & Vauday, 2014). Throughout history, scholars like Bowen (2013) and Freeman (1984) advocated for the responsibility which leaders of businesses face morally. In the recent decades, CSR became an exciting topic as a factor of social changes for whom forming the policies. As it has been confirmed in this study that performance in CSR can impact the CFP positively, managers are suggested to invest in such activities.

Moreover, the research will provide essential verification on the necessity of reviewing the existing standards and regulations. For instance, the government should revise their regulations in terms of providing more incentives to encourage companies in carrying out ESG activities.

Corporations cannot deal with solutions alone. Capable governments cannot be substituted with functional CSR activities from corporations, as Vogel (2005) suggests. In the case of high-risk matters like human rights and corruption, companies can influence the government. Notably, less developed nations should try to shape strict rules and regulations to involve ESG activities into considerations. However, McIntosh (1998) was against strict rules as believed they could result in increasing the opportunity costs and litigation. On the other hand, Grossman (2005) argues for promoting ethical standards to allow for adaptability to these good behaviors.

What lies ahead of CSR is encouraging and full of promises. By the emergence of managerial and legal considerations, executives can adapt the best patterns and models for incorporating the CSR.

Meanwhile, they must evaluate the company’s distinctive value proposition to be aligned with their decision making regarding the CSR or particularly, ESG activities to make sustainable strategic growth. Ultimately, in doing so, indigenous corporate knowledge will increase, and executives will have a positive impact on themselves, their corporations, society at large, and the planet.

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