Strategic Leadership in Corporate Social Responsibility

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This paper

- By selecting a credible CSR mission statement, the first mover can lead the industry to a Pareto optimal “social” equilibrium
- Examples of how coordination helps:
  - Reduce marginal cost of clean energy technology adoption
  - Avoid consumers associating industry with bad labor conditions
  - Avoid supply chain breakdowns (?)
    - Here also see a stakeholder theory by Magill, Quinzii, and Rochet (2015), in which firms internalize the risks to consumers, workers

Implementation

- Intuitively, with strategic complimentarities, multiple equilibria seem to be likely. If they can be ranked, coordination could help move to a more optimal one?
- The paper suggests a two-stage implementation where in the first stage the leading firm commits to a θ ("mission statement") and in the second stage players pick the strategic variables
- **Is this the most compelling way how firms can implement CSR in a product market equilibrium?**
  - Why not just meet in an industry group and set the standards?
  - Antitrust concerns: "The loftiest of purported motivations do not excuse anti-competitive collusion among rivals"
  - Unlikely to be enforced but greyzones possible

Consistent with some empirical evidence

- The paper suggests an industry equilibrium
- Difficult to document "strategic leadership" empirically but some evidence supports it
  - Cao, Liang, and Zhan (2020): The passage of a close-call CSR proposal and its implementation are followed by the adoption of similar CSR practices by peer firms
  - My work with Guoman She: E&S disclosure in firms' press releases and conference calls with equity analysts is correlated among peer firms and such within-industry correlation increases after one peer's environmental lawsuits (and leads changes in ESG rankings)

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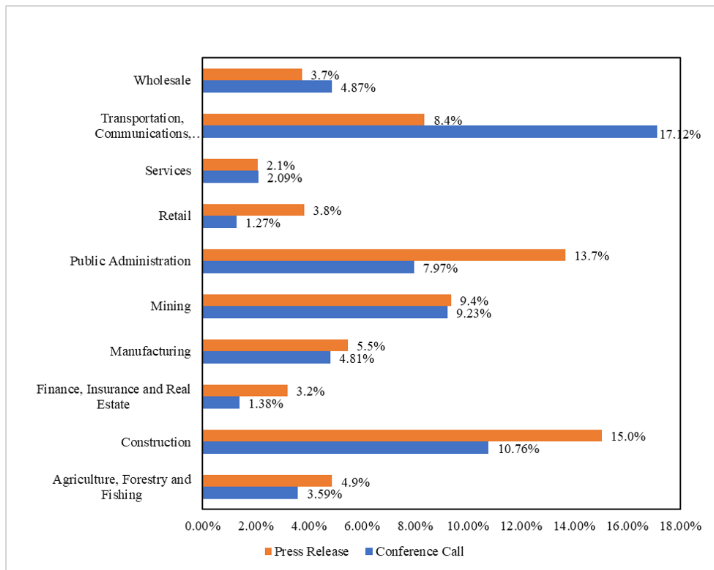

Observing a credible θ

- But is the two-stage game with a mission statement the most compelling depiction of reality (incl. examples in the paper)?
  - Mission statements often seem to be quite high-level
    - "to accelerate the world's transition to sustainable energy"
    - "to empower every person and every organization on the planet to achieve more"
    - "to bring the best user experience to its customers through its innovative hardware, software, and services"
  - They might not be specific enough for rivals to infer firms' commitment to the wage-setting policies or investment in supply chain resilience
  - Also, might not be irreversible ("don't be evil")
- Is it realistic that rivals do not consider θ to be cheap talk (greenwashing)?

Noisy θ

- Most likely, rivals only observe a noisy signal about θ through disclosure, advertising, positioning in the product markets, etc
- This then has all the cheap talk implications
  - Is that consistent with the model in the paper?
- **How to make the commitment to "strategic leadership" credible?**

Principle-agent solution

- Mission statements could be accompanied by observable CEO contracts that could provide a credible signal about firm's θ
  - Xiong and Jiang (2022): executive contract disclosure changes rival firms' incentives to invest
- Increasing reliance on ESG-based metrics / strategic goals in executive compensation
  - Ma (2019): 45% of CEOs receive cash incentive plans which include non-financial performance metrics, e.g., *"18 strategic goals in the following categories: (i) service excellence; (ii) safety and risk management; (iii) value pricing; (iv) profitable growth; (v) resource utilization; (vi) new energy environment; and (vii) employee engagement"*
  - Glass Lewis: In 2021, 1/4 of US firms included a environmental or social metric as part of their executive incentive plans

Examples

- Some examples from such metrics in exec contracts in 2020 (Incentive Lab):

Increasing Production From Direct And Purchased Renewable Energy In The Smelting Operation
Controllable Erosion and Sediment Rate
Utility Resilience Reliability and Climate Change
Utility Renewable Portfolio Standards
Net Megawatts Change
Greenhouse gas management
Year-on Year improvement in total GHG emissions intensity
Agency Reportable Environmental Event Rate (AREER)
Reducing Carbon Emissions In The Refining Operations
Peoples Gas Leaks
Aqua Wastewater Compliance
Launch Catalogue of Emissions-Reducing Technologies
Reduce C02 Emissions
Environmental Leadership: Drinking Water Quality
Carbon Neutrality
Roll out Climate Change policy in 1Q and complete TCFD reporting in 3Q

Other assumptions

- Two firms with homogenous technologies
  - Magill, Quinzii, and Rochet (2015) consider that asymmetry between multiples firms breaks stakeholder strategy
- Both care about the same strategic variables $f(t_i)$ and there's no information asymmetry
  - Follower firms might ignore their private information, leading to information cascades (Grenadier, 1999)
- This $f(t_i)$ relates to a "good" non-monetary component of the objective function
  - What if firms are stuck in a "good" equilibrium and $f(t_i)$ coordination leads to a worse societal one, as e.g. perceived by a median voter?
  - Can rivals' profit-driven motives sometimes police from corporate owners' idiosyncratic preference for $f(t_i)$?