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Does Firm Political Risk Affect the Relationship between Corporate Social Responsibility and Firm Value?

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Abstract: This paper investigates whether firm-level (idiosyncratic) political risk (PR) affects the relationship between corporate social responsibility (CSR) and firm value using a sample of 16,518 firm-year observations which correspond to 2055 unique firms belonging to the Russell 3000 Index over the sample period 2010–2020. Our main findings are as follows: First, firm-level PR does not affect firm value. Second, CSR is positively related to firm value, which is mainly driven by the social component of CSR. Finally, PR has no effect on the CSR–firm value relationship, regardless of the PR type. Our evidence suggests that firm-level PR is not priced in the financial market and as such it does not affect the CSR–firm value relationship. This is consistent with portfolio theory which suggests that only systematic risk is priced.

Keywords: firm-level political risk; corporate social responsibility; firm value; systematic political risk

1. Introduction

During the last two decades, the concept of corporate social responsibility (CSR) is gradually gaining importance among corporations, investors, and policymakers. This increased attention is due, among other things, to factors related to corporate behaviors (e.g., corporate scandals, 2000 dot-com bubble, 2008 financial crisis) and investor preferences regarding social, environmental, and governance (ESG) issues. The signing of the US climate law, the Inflation Reduction Act, by U.S. President Joe Biden on 16 August 2022 is a good example of this increased attention from regulators [1]. The new climate law allocates $370 billion (e.g., tax credits and tax credit bonuses) to decarbonization efforts and is expected to enable the U.S. to cut its emissions by 40% by 2030 relative to 2005 levels [1]. The signing in 2006 of the UN Principle for Responsible Investment (PRI) and its evolution is another good example of this increased attention from investors. CSR has therefore become an important issue for firms and the subject of an intense debate among academics, practitioners, and policymakers.

The CSR literature provides mixed views regarding the theoretical underpinning and financial implications of CSR. Three theoretical arguments most cited are shareholder theory, agency theory, and stakeholder theory. The shareholder theory suggests that managers should maximize shareholders' wealth and consider CSR to be an additional cost that reduces profits [2]. Agency theory suggests that managers could implement CSR actions opportunistically to extract personal benefits at the expense of other stakeholders, including shareholders [3–5]. The stakeholder theory suggests that managers should maximize stakeholders' welfare and consider CSR to be an investment that increases profits [6–9].

Much of the CSR literature focuses on the relationship between CSR and firm value or financial performance [10,11]. However, the evidence is mixed. Several studies find a positive relation [12–17], whereas other studies do not find any relation [18–20] between CSR and firm value or financial performance. Other studies find a nonlinear relationship or provide an alternative explanation to CSR, e.g., CSR signals private information about future performance [21,22]. Despite the mixed evidence, several studies show various channels through which CSR can enhance firm value, including increased future revenue growth [11], lower cost of capital, higher institutional ownership and analyst coverage [23], increased transparency [24], better access to finance [25], and lower risk [26].

The mixed evidence regarding the financial implications of CSR led to an important research stream in the CSR literature focusing on the roles of variables moderating or conditioning this relationship [27–30]. That is, CSR can affect firm value only under certain conditions. For example, ref. [27] showed that CSR and firm value are positively related only for firms with higher customer awareness. Ref. [28] found that the impact of CSR varies with the level of influential institutional ownership and depends upon economic conditions (e.g., 2008–2009 financial crisis). Ref. [31] found that large shareholder ownership lowers the relation between CSR and firm value in Korea. The authors of [32] reported similar findings in Turkey. In [33], the authors found that CSR activities had a positive effect on returns only during the 2008–2009 financial crisis. More recently, some studies have shown that political risk (PR) could affect the CSR–firm value relationship [34,35]. Ref. [35] found that politically connected firms overinvest in CSR to obtain political legitimacy and access to governmental resources. Our paper contributes to this research stream by examining whether *firm-specific* PR moderates the CSR–firm value relationship.

Politicians and regulatory bodies frequently shift their policies, causing a high degree of PR. The overall uncertainty attributed to the political system can hamper value creation because it creates difficulties for firms regarding funding, planning, and maximizing the outcomes of their activities. For instance, ref. [36] found that PR depresses firm investment. PR can increase the cost of capital [37], return volatility [38], analyst forecast error [39], bid–ask spread [40], stock price crash risk [41], earnings management [42], and corporate risk-taking [43]; it can also reduce stock prices [44], merger-and-acquisition (M&A) deals [45], and IPO activity [46]. Moreover, ref. [47] found a negative relation between politically connected firms and analysts' stock recommendations. Nevertheless, some firms and industries have proven to be more resilient than others in preserving their value during periods of high PR. For instance, ref. [48] showed that high PR has a negative valuation effect in only 33% of Fama–French 30 industries while investment has decreased in 90% of them. On the other hand, 3% of Fama–French 30 industries had higher valuation and 64% of the industries were not affected. This narrow impact on market value is quite surprising [48]. Previous literature focused on the effects of aggregate levels of PR (instead of firm-level PR) on a variety of corporate decisions and asset pricing e.g., [44,49]. However, our understanding of the potential effects of firm-level PR is still limited.

This paper examines whether firm-specific PR moderates the CSR–firm value relationship. Our paper is related to the work of [33] and [34]. Ref. [33] showed that CSR activities had a positive effect on returns only during the 2008–2009 financial crisis. Ref. [34] found that there is a positive association between CSR and firm value only when aggregate (systematic) PR is high. These findings suggest that CSR engagement is not relevant during "normal" and more "steady-state" times. In other words, CSR activities can add value to firms only under certain circumstances (e.g., severe PR).

Based on the stakeholder theory, we argue that CSR activities can preserve firm value when firm-specific PR is high. Strong CSR engagement should allow firms to produce and maintain high levels of social capital (e.g., trust and reputation) that can be used to sustain their competitive advantage during times of severe PR [33,34]. In the same line of reasoning, PR can negatively affect the quality of public information, leading to high demand for additional firm-level information [8,32]. The disclosure of CSR-related information can reduce information asymmetry between the firm and its stakeholders

(including shareholders) and ultimately offset the negative consequences of information ambiguity and opacity during periods of severe PR [39,40]. Managers can avoid altering their risk-management strategies during periods of high PR because CSR can reduce the cost of capital [50,51] and risk [52].

Our paper is closely related to the work of [34] which examines the impact of aggregate (systematic) PR on the CSR–firm value relationship. Our analysis differs from theirs in two ways. First, ref. [34] uses the index from [49] as a proxy for aggregate (systematic) PR, while our tests rely on firm-specific measures of PR developed by [53]. Ref. [53] applies text-searching techniques to construct a new measure of firm-specific PR which differs from existing measures in several aspects. For instance, the proposed PR measure indicates the share of firm quarterly earnings conferences devoted to PR. It reflects the perception of managers and participants in the conference calls. Moreover, most of the variation in the measure is at the firm level. For instance, "*only a very small number of firms involved with power generation will be affected by new regulations governing the emissions of mercury from coal furnaces across state lines or changing rules about the compensation for providing spare generation capacity in Ohio*" [53] (p. 5). Second, we also examine the eight different channels (components) of firm-specific PR, stemming from economic, environment, health, institutions, tax, technology, trade, and security issues, as some channels may have stronger, weaker, or neutral effects on the CSR–firm value relationship.

Our findings show that firms with strong CSR engagement perform better during times of high PR as well as during "normal" and more "steady-state" times. However, we find that PR has a neutral impact on the CSR–firm value relationship. This neutral effect holds when we examine the eight category-specific indexes of PR provided by [53], when we partition our sample based on nine industries (communications, consumer discretionary, consumer staples, energy, health care, industrials, materials, real estate, and technology), and when we decompose CSR activities into three subcategories (Environment, Social, and Governance). It appears that some firms in each industry cope better with high PR while others are unable to preserve their value, so that on average the effect of PR is neutral. Furthermore, being idiosyncratic in nature, firm-level PR may be fully diversifiable, and only PR at the aggregate level is priced. This may explain why we find a neutral impact of PR while prior literature shows significant valuation effects based on systematic PR.

The remainder of this paper is structured as follows: Section 2 summarizes the literature on the impact of PR and CSR on firm value, and discusses the theoretical arguments behind our hypotheses. Section 3 describes our research design and variable construction. Section 4 presents the findings and Section 5 discusses these findings and their implications. Section 6 concludes the paper.

2. Review of Literature and Hypotheses Development

Our research is related to two important strands of the literature. The first literature strand examines the effects of PR on firm's decisions and outcomes. The second literature strand examines the impact of CSR on firm value. The first and second parts of this section discuss these two streams, respectively. The last part of this section discusses the potential moderating role of PR in the CSR–firm value relationship.

2.1. The Valuation Effects of PR

Numerous studies in the literature examine the relationship between PR and corporate investment [36]; M&A activities [45]; cost of external financing [54,55]; stock price volatility [44]; debt maturity and leverage [56]; IPO activities [46]; accounting conservatism [57]; earnings management [42]; analyst forecast errors [39]; and analysts' stock recommendations [47]. In general, two channels through which PR can affect firm value are proposed. The first channel focuses largely on the real option theory which predicts that high levels of PR will increase the value of the option to delay a firm's investments until the uncertainty starts to subside [36,45]. The option to wait should be stronger for more irreversible investments and weaker for investments that are most costly (or difficult) to delay [36,45].

Consistent with these predictions, ref. [36] found that the decrease in corporate investment during times of high PR is stronger for firms with more irreversible investments. The research found in [45] has shown that PR has a more pronounced impact on M&A deals in industries with high concentration or low merger activity, where competition is weak and M&A activity can be postponed more easily.

Moving away from the real option channel, a growing number of studies rely on the information channel to explain the detrimental effects of PR. As suggested by [55], a firm's production, hiring, financing, and investment activities transmit valuable information to different market participants. During high-PR periods, a slowdown in these activities may decrease the amount of information that market participants receive from the firm. This could lead to severe agency problems between stakeholders and managers, resulting in distortions in allocative efficiency [48]. High PR could also have a detrimental effect on financial analysts' role in transmitting firm-level information to market participants. In this respect, ref. [39] has shown that the accuracy of analysts' forecasts is lower when PR is high. In the same line of reasoning, when PR increases market participants' uncertainty with respect to firms' prospects, this could have a negative impact on managers' learning capacities.

The managerial learning hypothesis predicts that managers can learn new information from a firm's stock prices and use this information when making investment decisions [58–60]. We argue that informed investors' trades can impound information into stock prices that is new to managers, i.e., managers do not have such information. For example, managers can learn new information from policymakers, institutional investors, customers, and financial analysts about the future state of the economy, the demand for a firm's products, and the competition with other firms [61]. The learning process should allow managers to add new information to their own information and make value-maximizing investment decisions [61]. If PR impacts managerial learning negatively, high levels of PR may distort the fundamental role of markets in guiding managers to make efficient investment decisions (high revelatory efficiency) [55]. Consistent with these predictions, ref. [55] shows that the sensitivity of investment to a given firm's cost of capital decreases when PR is high. In the same line of reasoning, ref. [48] also found that investment–price sensitivity is low during times of high PR. The above arguments lead to the following hypothesis:

Hypothesis 1: *There is a negative relationship between PR and firm value.*

A less-explored channel in the PR literature is the managerial risk-taking incentives. We argue that managers' risk-taking behavior can play an important role in investment decisions. In this respect, adequate risk-management strategies during high-PR periods can help firms avoid "negative" uncertainty while making use of "positive" uncertainty [43,62,63]. We argue that managers who are unable to differentiate between "negative" and "positive" uncertainty will reduce investment expenditures and take a defensive position. Such typical risk-avoiding behavior should not allow managers to support high-risk and high-yield investment opportunities [43,62,63]. In this respect, ref. [62] has shown that when firms cannot fully insure against PR, they have incentives to reduce capital stock. On the other hand, if firms can identify the potential opportunities of future PR uncertainty, they should be able to support higher risk associated with higher-yield investment projects and ultimately preserve value creation during times of high PR [43,63]. This leads to the following hypothesis:

Hypothesis 2: *Well-designed risk-taking incentives under high PR can preserve firm value.*

2.2. The Valuation Effects of CSR

The CSR literature provides mixed views regarding the theoretical underpinning, definition, measurement, integration and implementation, and financial implications of

CSR. CSR literature provides at least three theoretical arguments underpinning CSR: shareholder theory, agency theory and stakeholder theory. The shareholder theory suggests that managers should maximize shareholders' wealth and consider CSR to be an additional cost that reduces profits and consequently firm value [2]. Agency theory suggests that managers could act opportunistically to extract personal benefits at the expense of other stakeholders, including shareholders. In this case, managers implement CSR actions to build their personal reputation as good/proactive citizens, i.e., career concerns, e.g., to easily find a job elsewhere if fired or justify poor financial performance by the firm's engagement in CSR actions [3–5]. The stakeholder theory suggests that managers should maximize stakeholders' welfare and consider CSR as an investment that increases profits and consequently firm value [6,7,9]. Furthermore, the stakeholder theory provides two CSR versions: normative CSR and instrumental or strategic CSR [8]. Normative CSR is grounded in ethical and moral values (i.e., CSR actions are the right things to do based on ethical or moral values irrespective of their financial implications). Instrumental or strategic CSR suggests that a firm implements CSR for strategic reasons, e.g., as a response to stakeholders' demands or expectations. For instance, firms could be reactive to stakeholders' demands in order to obtain resources or their support, either to continue to do business (social license to operate) or to avoid ESG risks (e.g., avoid negative media or publicity that could ultimately affect the survival of the firm).

The CSR literature also provides mixed views regarding CSR meaning (definition, form, or type) and measurement, i.e., what to include or exclude [64,65]. Ref. [66] argues that the CSR concept is largely debated among academics and practitioners, and applied differently both across countries and across firms within the same country or industry. CSR operationalization (i.e., measurement) also differs between and within academics and practitioners. The proliferation of ESG data providers and the variety of these data illustrate the difficulties associated with CSR operationalization. Another dilemma is whether one should focus on an aggregated CSR measure or the individual CSR components, which themselves have subcomponents that vary in intensity and importance over time for the same firm and across firms and industries.

An important emerging research stream in the CSR literature focuses on CSR integration and implementation into corporate identity and strategies. Ref. [65] proposes a model of CSR development and implementation including seven organizational stages articulated around three cultural phases (CSR reluctance, CSR grasp, and CSR embedment). The CSR reluctance phase includes one dismissing stage (CSR is perceived as a constraint); the CSR grasp phase includes a self-protecting stage, a compliance-seeking stage, and a capability-seeking stage; and the CSR embedment phase includes a caring stage, a strategizing stage, and a transforming stage where CSR becomes fully integrated into every aspect of the firm's activities. The support of the organizational culture or corporate identity (values, beliefs, attitudes and practices) is essential for the model in [65] to be successful. That is, CSR integration involves the integration of CSR principles into corporate identity so that the firm makes the transition to positive corporate identity where the focus is on positive outcomes, processes, and attributes, e.g., moving from harm avoidance and focusing on self-interest to openness and helping others [66,67]. Ref. [66] argues that corporate values are the cornerstone of both positive corporate identity and CSR. Applying the model of [65] to a case study, they found higher inconsistencies between real corporate values (values driving the firm's operating activity), ideal corporate values (values driving the organization), and CSR values (firm's CSR principles), which has led to a lower CSR integration into corporate identity. To achieve its full potential and be communicated efficiently to outsiders, CSR needs to be fully integrated into corporate identity [66]. This is consistent with [68] who argue that building a focused and integrated CSR as part of a firm's core strategies can lead to a sustainable competitive advantage. Ref. [69] examined the CSR structures of U.S. firms and found evidence of CSR specialization, where most firms focus on a single CSR dimension. They also find that CSR diversification had a positive impact on firm value before and during the 2008 financial crisis.

Much of the CSR literature strives to establish a business case for CSR [10,11]. As such, the large body of CSR literature focuses on the financial implications of CSR. However, this literature is characterized by the absence of consensus regarding the relationship between CSR and firm value or financial performance. The evidence is mixed. Numerous studies have reported a positive relation between CSR and firm value or financial performance [12–17]. Other studies have not found any relation between CSR and firm value or financial performance [18–20]. In addition, ref. [22] found an inverted U-shaped relationship between CSR and firm value in mainland China and Hong Kong. Ref. [21] provides an alternative explanation to the positive relation between CSR and firm value. They showed that CSR signals private information about future performance. In other words, high-CSR firms are those expecting higher future performance.

In sum, the CSR–firm value relationship has been extensively examined in the literature with no conclusive results. Nonetheless, several studies report evidence of various channels through which CSR can enhance firm value, including increased future revenue growth [11], lower cost of capital, higher institutional ownership and analyst coverage [23], increased transparency [24], better access to finance [25], and lower risk [26]. Ref. [11] found that philanthropy increases future revenue growth through attracting and retaining customers (i.e., increased name and brand recognition). Ref. [25] found that CSR leads to better access to finance because of lower agency costs (better engagement with stakeholders) and increased transparency (lower informational asymmetry).

Under the stakeholder theory, CSR engagement is viewed as a way to resolve conflicts among stakeholders and run the firm to the mutual advantage of its stakeholders, including the firm's shareholders [34,70,71]. A higher protection of stakeholders' interests could help firms build forms of social capital such as legitimacy, reputation, and trust [34]. As a result, stakeholders (e.g., employees, customers, suppliers, and communities) should perceive the firm as an attractive partner [71]. Firms should, then, profit from more motivated employees and loyal customers [34,71]. Suppliers may also engage in lowering firms' costs, increasing quality, and investing in strategic and innovative relationships with the firm. In the same line of reasoning, financial partners can also reciprocate CSR engagement and lower the cost of capital [50,51]. Under the stakeholder theory, CSR activities can also serve as a powerful mechanism that reduces firm risk and agency costs [34,70,71]. The above arguments lead to the following hypothesis:

Hypothesis 3: *There is a positive relationship between CSR and firm value.*

2.3. The Moderating Role of Firm-Level PR

The mixed evidence regarding the signs and direction of a relationship between CSR and firm value or financial performance has led to an important research stream in the CSR literature focusing on the roles of variables moderating or conditioning this relationship. A growing number of studies suggest that the focus on the direct relationship between CSR and firm value can lead to spurious and imprecise findings because many influential factors can indirectly affect the potential CSR–firm value relationship [27–30]. For instance, ref. [27] has shown that CSR and firm value are positively related only for firms with higher customer awareness. In [28], the research has shown that the CSR–firm value relationship is affected by influential institutional ownership and economic conditions (e.g., 2008 financial crisis). The authors of [31] found that large shareholder ownership lowers the relation between CSR and firm value in Korea. They concluded that ownership structure moderates the CSR–firm value relationship. Ref. [32] reports similar findings in Turkey. Ref. [33] found that CSR activities have a positive effect on returns only during the 2008–2009 financial crisis. The findings of ref. [29] suggest that the CSR–firm value relationship is moderated by firm size and age. In [34], the authors also found that the CSR–firm value relationship is moderated by PR. This new line of research suggests that CSR is value-relevant only under certain conditions. Our paper contributes to this research stream by examining whether firm-specific PR moderates the CSR–firm value relationship.

We argue that CSR activities can decrease the value of the option to delay a firm's investment. During times of high PR, loyal customers may maintain their demand and even accept paying higher prices. As a result, uncertainty related to project revenues should be less severe for firms with strong CSR engagement. At the same time, suppliers may also support the firm and act as a buffer against potential changes in a firm's costs by maintaining such costs at low levels and engaging in innovative relationships with the firm. This will reduce the uncertainty related to project costs and ultimately reduce the option to delay a firm's investments. In addition, ref. [34] argues that firms with strong CSR engagement should be able to obtain financial resources at more favorable terms when PR is high because of greater stakeholder support, enhanced firm reputation, and trust. Lower financing constraints should also decrease the incentive to delay a firm's projects and offset the negative consequences linked to PR.

CSR engagement can reduce information asymmetry between managers and firms' stakeholders [39,72], and signal a higher quality of firms' future prospects [73–75]. We expect these effects to be stronger when PR is high. The research in [39] documents the fact that good CSR practices moderate analyst forecast error when PR is high. Ref. [61] argues that managers can learn from informed stakeholders and adjust their CSR practices accordingly. This could enhance their ability to make value-maximizing investment decisions and offset the negative impacts of high PR. The above arguments lead to the following hypothesis:

Hypothesis 4: *Firms with high CSR have higher values when PR is high.*

3. Data and Empirical Methodology

Our initial sample includes all the constituents of the Russell 3000 Index which is composed of 3000 large U.S. companies, as measured by market capitalization. The Russell 3000 Index represent 98% of the investable U.S. equity market. The list of constituents of the Russell 3000 Index between 2010 and 2020 is obtained from Bloomberg. To construct our final sample of firms, we start by removing financial and utility firms from the list of constituents of the Russell 3000 Index due to their different balance sheet structures and the government support they may receive. Then, we require that the remaining sample of firms have data in these three databases: Refinitiv ESG database for CSR data, Refinitiv DataStream for accounting data, and the PR data from [53]. Since PR data is measured on a quarterly basis, we use the data of the last quarter as a proxy for the yearly PR of a firm. Our final sample includes 16,518 firm-year observations which correspond to 2055 unique firms over the sample period 2010–2020.

Ref. [53] developed a firm-level measure of PR that captures firm-level exposure to PR. It is constructed using information produced by decision makers within the firm rather than information produced outside the firm. More specifically, ref. [53] used a training library of political text and a training library of non-political text to identify two-word combinations (bigrams) that are often used in political texts [53]. Afterward, "[they] *count the number of instances in which these bigrams are used in a conference call in conjunction with synonyms for "risk" or "uncertainty" and divide by the total length of the call.*" [53] (pp. 2136–2137) The result represents the share of the conversation related to PR [53]. We standardize this measure so that the distribution has zero mean and a standard deviation of one:

$$ZPRISK_{it} = \frac{PRISK_{it} - \overline{PRISK}}{SD_{PRISK}}, \tag{1}$$

where PRISK is the measure of [53]. ZPRISK is the standardized measure of PR, $\overline{PRISK}$ is the average of PR in the sample, and SD_{PRISK} is its sample standard deviation. For robustness, PRISK is only divided by SD_{PRISK} and used as a second standardized measure of PR.

We obtain CSR data from the Refinitiv ESG database which collects ESG data from a variety of sources such as annual reports, CSR reports, company websites, NGO websites,

stock exchange filings and news sources [76]. Refinitiv evaluates a firm's CSR based on three pillars: environmental, social, and corporate governance. Each pillar is given a score based on firm performance: Environment Pillar Score, Social Pillar Score and Governance Pillar Score. These scores include several categories. The environmental (E) pillar includes three categories: resource use, emissions, and innovation. The social (S) pillar includes four categories: workforce, human rights, community, and product responsibility. The governance (G) pillar includes three categories: management, shareholders, and corporate social responsibility strategy. Each category contains several ESG themes [76]. For example, the emission category includes four themes: CO_2 emissions, waste, biodiversity, and environmental management systems. The workforce category includes four themes: diversity and inclusion, career development and training, working conditions, and health and safety. The shareholders category includes two themes: shareholder rights and takeover defenses. Refinitiv also calculates an overall ESG Score as the weighted average of the underlying 10 category scores where the category weights vary per industry for the environmental and social categories, i.e., based on relative performance and materiality, as the importance of ESG factors differ across industries [76]. All ESG scores range from 0 to 100.

Our dependant variable is Tobin's Q measured as the market value of total assets divided by book value of total assets. Tobin's Q is also measured as follows: (total assets − common equity + price close ∗ common shares outstanding)/total assets. Our two main explanatory variables are CSR scores and ZPRISK. The latter is our proxy for firm-level PR. Following prior studies, we control for important firm characteristics (firm size, return on assets (ROA), leverage, cash, investment, Selling, General, and Administrative Expense (SGA), and sales growth). All variables, except CSR scores, are winsorized at the 1st and 99th percentiles to reduce the impact of outliers. Table 1 presents the variable definitions.

Table 1. Variables definitions.

Variable	Measurement
Tobin's Q	Market Value of Total Assets divided by Book Value of Total Assets = (Total Assets − Common Equity + Price Close × Common Shares Outstanding)/Total Assets
Overall CSR Score	ESG Score
E Score	Environment Pillar Score
S Score	Social Pillar Score
G Score	Governance Pillar Score
ZPRISK	Standardized Measure of Political Risk Index From [23]
Firm's Size	Natural Logarithm of Total Assets
ROA	Net Income/Total Assets
Leverage	(Long-Term Debt + Debt in Current Liabilities − Cash and Marketable Securities)/Total Assets
Cash	Cash and Short-Term Investments/Total Assets
Investment	Capex/Total Assets
Selling, General, and Administrative Expense	SGA/Total Assets
Sales Growth	Natural Logarithm of (sales at t/sales at t − 1)

To implement our empirical tests, we follow [34] and propose the following regression:

$$Q_{i,t} = \beta_0 + \beta_1\, CSR_{i,t-1} + \beta_2\, ZPRISK_{i,t-1} + \beta_3\, CSR_{i,t-1} \times ZPRISK_{i,t-1} + Controls_{i,t-1} + \varepsilon_i \qquad (2)$$

where $Q_{i,t}$ is Tobin's Q, CSR is firm social scores, and ZPRISK is PR. In our baseline specifications, we examine the impact of an overall CSR score and three CSR sub-scores related to environment (E), social (S), and governance (G) issues. To mitigate endogeneity concerns we lag CSR, PR and control variables by one period. We also include industry- and year-fixed effects. We estimate our regressions using the Ordinary Least Square (OLS) method in the software STATA 17. The reported *p*-values of the estimated coefficients

are based on the robust standard errors adjusted for clustering at the firm level. The estimated coefficients are robust to heteroscedasticity and autocorrelation of the error terms. For robustness, we also examine the impact of 8 different political topics in addition to the baseline measure of overall exposure to PR (Equation (1)). Hypothesis 1 suggests that coefficient β_2 should be negative and significant. The same coefficient should be nonsignificant under hypothesis 2. Furthermore, a positive and significant β_1 provides support for hypothesis 3. Finally, under hypothesis 4, the coefficient of the interaction between CSR and ZPRISK (β_3) should be positive and significant.

4. Results

Descriptive statistics of the sample are presented in Table 2. We report the mean, median, standard deviation, minimum, maximum, 25th percentile, and 75th percentile of the main variables used in our analysis. The dependent variable is firm value proxied by Tobin's Q. The mean (median) Tobin's Q is 2.454 (1.791). Our first key independent variable is the standardized measure of PR (overall PR) and its eight subcomponents (economic, environment, trade, institutions, health, security, tax, and technology). We use eight different channels of PR in addition to an overall measure because some specific channels of PR may have stronger, weaker, or neutral valuation effects. On average, the standardized overall measure of PR is 0 with a standard deviation of 1. The minimum value is –0.537 and the maximum value is 22.443. The overall measure of CSR has a mean (median) value of 41.089 (37.76).

Table 2. Summary statistics.

	N	Mean	Std. Dev.	p25	Median	p75	min	max
Q	16,410	2.454	1.891	1.307	1.791	2.831	0.73	11.459
CSR score	11,821	41.089	19.282	26.04	37.76	54.66	0.57	95.19
S-score	11,821	43.857	21.218	27.41	40.77	58.57	0.46	98.12
E-score	11,821	26.87	27.897	0	17.13	48.77	0	98.55
G-score	11,821	49.048	22.044	31.32	49.68	66.75	0.25	99.45
ZPRisk	16,518	0	1	–0.451	–0.275	0.067	–0.537	22.443
ZPRisk economic	16,518	0	1	–0.424	–0.272	0.033	–0.503	21.118
ZPRisk environment	16,518	0	1	–0.312	–0.216	–0.004	–0.355	57.602
ZPRisk trade	16,518	0	1	–0.182	–0.138	–0.034	–0.195	95.116
ZPRisk institutions	16,518	0	1	–0.372	–0.253	–0.011	–0.432	19.825
ZPRisk health	16,518	0	1	–0.222	–0.163	–0.036	–0.248	43.321
ZPRisk security	16,518	0	1	–0.408	–0.262	0.023	–0.48	22.936
ZPRisk tax	16,518	0	1	–0.337	–0.231	–0.009	–0.381	38.995
ZPRisk technology	16,518	0	1	–0.387	–0.26	0.012	–0.439	40.863
SIZE	16,410	14.446	1.714	13.247	14.452	15.583	10.456	18.692
ROA	16,408	0.009	0.156	–0.003	0.04	0.079	–0.762	0.293
LEVERAGE	15,849	0.067	0.363	–0.155	0.115	0.319	–0.906	0.91
CASH	16,352	0.197	0.218	0.038	0.113	0.271	0.002	0.933
INVESTMENT	16,397	0.045	0.048	0.015	0.029	0.056	0	0.269
SGA expense	16,055	0.262	0.239	0.089	0.196	0.363	0.005	1.21
SALES growth	13,959	0.07	0.23	–0.009	0.061	0.148	–0.855	0.994

Note: This Table reports the summary statistics of the sample. The dependent variable is Tobin's Q. The key independent variables are CSR overall score, three CSR sub-scores (E, S, G), an overall standardized measure of PR proposed by [53], and eight subcomponents of PR measure (economic, environment, trade, institutions, health, security, tax, and technology). All variables are defined in Table 1.

Table 3 reports the estimated results of our baseline regressions using aggregate measure of CSR (overall CSR score), firm-level measure of PR (overall ZPRISK), and disaggregated measures of CSR (E, S, and G scores). In model (1), we can observe the effect of overall CSR scores and overall ZPRISK on firm value. There is a positive and significant relationship between Tobin's Q and the overall CSR score (β_1 is 0.006 and significant at the 1% level). This result is consistent with hypothesis 3. However, there is no significant association between Tobin's Q and the overall ZPRISK, indicating a neutral impact of PR

on firm value. The coefficient β_2 is not statistically significant. This result does not support hypothesis 1 which suggests a negative relation between PR and firm value. Instead, this result provides support to hypothesis 2 which suggests that adequate risk management strategies during high-PR periods can preserve firm value. The coefficient β_3 associated with the interaction term CSR*ZPRISK informs us about whether firms with strong (weak) CSR engagement have higher (lower) values when PR is higher (lower). The result suggests that PR has no effect on the CSR–firm value relationship. Our findings indicate that CSR adds value to firms (β_1 is positive and significant) but that there are no incremental benefits linked to CSR during times of high PR (β_3 is not significant).

Table 3. Impact of PR on CSR-Q link.

VARIABLES	Model (1)	Model (2)	Model (3)	Model (4)	Model (5)
CSR score	0.006 ***				
	(0.000)				
S score		0.007 ***			0.006 ***
		(0.000)			(0.000)
E score			0.004 ***		0.001
			(0.000)		(0.131)
G score				−0.002 **	−0.003 ***
				(0.025)	(0.000)
sPRisk	0.005	0.011	−0.015	0.003	0.028
	(0.927)	(0.810)	(0.607)	(0.948)	(0.650)
sPRisk*CSR score	−0.001				
	(0.613)				
sPRisk*S score		−0.001			−0.001
		(0.448)			(0.296)
sPRisk*E score			−0.000		0.001
			(0.951)		(0.456)
SPRisk*G score				−0.000	−0.000
				(0.699)	(0.804)
sizew	−0.122 ***	−0.134 ***	−0.120 ***	−0.063 ***	−0.134 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
roaw	3.884 ***	3.902 ***	3.915 ***	3.964 ***	3.946 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
leveragew	1.111 ***	1.111 ***	1.105 ***	1.064 ***	1.105 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
cash_stiw	5.012 ***	4.967 ***	4.998 ***	4.995 ***	4.937 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
investmentw	1.867 ***	1.886 ***	1.844 ***	1.809 ***	1.918 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
costw	2.387 ***	2.364 ***	2.419 ***	2.484 ***	2.377 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
sales_gw	0.975 ***	0.963 ***	0.969 ***	0.909 ***	0.945 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
Constant	1.583 ***	1.734 ***	1.657 ***	0.892 ***	1.842 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
Observations	8559	8559	8559	8559	8559
R-squared	0.379	0.381	0.379	0.378	0.382
Industry FE	Yes	Yes	Yes	Yes	Yes
Year FE	Yes	Yes	Yes	Yes	Yes

Note: All models are estimated using industry- and year-fixed effects. *, **, and *** denote statistical significance at 10%, 5%, and 1%, respectively. All variables are defined in Table 1.

Models (2) and (3) in Table 3 repeat the same analysis using S-score and E-score as proxies for firm CSR engagement. The coefficient β_1 is positive and significant in both models (2) and (3) suggesting that high scores in the S and E dimensions also increase firm value. In model (2) and (3), the coefficients β_2 and β_3 are not statistically significant

suggesting again that the impact of PR on firm value and on the CSR–firm value relationship is neutral. In model (4), we use G-score to measure firm CSR engagement. The CSR–firm value association becomes negative and significant at the 5% level (β_1 is –0.002 with *p*-value of 0.025) suggesting that firms with high G-scores have lower firm values. Consistent with our previous results, the impact of PR on firm value and on the CSR–firm value relationship remains neutral when using G-score to measure firm CSR engagement. Finally, we examine the three CSR dimensions simultaneously in model (5). It seems that the positive and significant relationship between CSR and firm value is driven by the S-score. High G-score results in lower firm value. The coefficient associated with the E-score becomes insignificant. The coefficients β_2 and β_3 remain insignificant. Thus, the benefits of CSR are not dependent on whether PR is high or low. CSR engagement appears to create value primary during "normal" and more "steady-state" times. These benefits do not increase when PR is high. In all models of Table 3, the coefficients on control variables are consistent with prior literature. For instance, our findings indicate a significant and positive association between Tobin' Q and ROA, leverage, cash, investment, SGA expenses, and sales growth.

To further test the robustness of our results, we decompose PR into eight different types of PR and examine the impact of each component separately. More specifically, we examine the different topics of firm-level PR related to economic, environment, trade, institutions, health, security, tax, and technology issues. To validate their eight topic-specific measures of PR, [53] exploited firms' disclosure of the total expenditures on lobbying and the list of specific political topics these expenditures are directed toward. Using these disclosures, [23] created a map between topics discussed in conference calls and topics connected to firms' lobbying. The mapping shows that an increase of one standard deviation in risk related to a specific political topic is associated with an 11% increase in the probability that a given firm will lobby on that topic [53]. We find that PR stemming from economic (Table 4), environment (Table 5), health (Table 6), institutions (Table 7), tax (Table 8), and technology (Table 9) components have no effect on firm value and on the CSR–firm value relationship. Furthermore, we find weak evidence suggesting that the effect of PR is significant (at the 10% level) for the trade component (Table 10). Models (2) and (3) of Table 10 show that PR stemming from the topic of trade has a negative effect on firm value and a positive effect on the CSR–firm value relationship when using S and E scores. We re-estimate our regressions using security as a specific topic for PR in Table 11. The moderating effect of PR on the CSR–firm value relationship is negative and significant (at the 5% level) when using S-score to measure CSR engagement. In sum, our additional tests show that firm-level PR is not a moderator of the CSR–firm value relationship, regardless of the PR type.

Table 4. Impact of PR stemming from economic topic on CSR-Q link.

VARIABLES	Model (1)	Model (2)	Model (3)	Model (4)	Model (5)
CSR score	0.006 ***				
	(0.000)				
S score		0.007 ***			0.006 ***
		(0.000)			(0.000)
E score			0.004 ***		0.001
			(0.000)		(0.137)
G score				−0.002 **	−0.003 ***
				(0.024)	(0.000)
sPRiskT_economic	0.046	0.040	0.011	0.022	0.053
	(0.383)	(0.419)	(0.778)	(0.599)	(0.277)
sPRiskT_economic*CSR score	−0.001				
	(0.222)				
sPRiskT_economic*S score		−0.001			−0.001
		(0.231)			(0.218)

Table 4. *Cont.*

VARIABLES	Model (1)	Model (2)	Model (3)	Model (4)	Model (5)
sPRiskT_economic*E score			−0.001		0.000
			(0.547)		(0.862)
sPRiskT_economic*G score				−0.000	−0.000
				(0.508)	(0.733)
sizew	−0.122 ***	−0.134 ***	−0.120 ***	−0.063 ***	−0.134 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
roaw	3.883 ***	3.901 ***	3.916 ***	3.964 ***	3.946 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
leveragew	1.112 ***	1.112 ***	1.106 ***	1.064 ***	1.105 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
cash_stiw	5.010 ***	4.963 ***	4.997 ***	4.994 ***	4.932 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
investmentw	1.881 ***	1.900 ***	1.859 ***	1.820 ***	1.933 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
costw	2.389 ***	2.366 ***	2.422 ***	2.486 ***	2.379 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
sales_gw	0.975 ***	0.963 ***	0.968 ***	0.908 ***	0.944 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
Constant	1.586 ***	1.738 ***	1.655 ***	0.892 ***	1.844 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
Observations	8559	8559	8559	8559	8559
R-squared	0.379	0.381	0.379	0.378	0.382
Industry FE	Yes	Yes	Yes	Yes	Yes
Year FE	Yes	Yes	Yes	Yes	Yes

Note: All models are estimated with industry- and year-fixed effects. *, **, and *** denote statistical significance at 10%, 5%, and 1%, respectively. All variables are defined in Table 1.

Table 5. Impact of PR stemming from environmental topic on CSR-Q link.

VARIABLES	Model (1)	Model (2)	Model (3)	Model (4)	Model (5)
CSR score	0.006 ***				
	(0.000)				
S score		0.007 ***			0.007 ***
		(0.000)			(0.000)
E score			0.004 ***		0.001
			(0.000)		(0.151)
G score				−0.002 **	−0.003 ***
				(0.025)	(0.000)
sPRiskT_environment	0.039	0.029	0.028	0.017	0.014
	(0.477)	(0.582)	(0.447)	(0.770)	(0.820)
sPRiskT_environment*CSR score	−0.001				
	(0.458)				
sPRiskT_environment*S score		−0.001			0.000
		(0.565)			(0.879)
sPRiskT_environment*E score			−0.001		−0.001
			(0.276)		(0.289)
sPRiskT_environment*G score				−0.000	0.000
				(0.855)	(0.872)
sizew	−0.122 ***	−0.133 ***	−0.120 ***	−0.063 ***	−0.133 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
roaw	3.883 ***	3.902 ***	3.914 ***	3.964 ***	3.946 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
leveragew	1.112 ***	1.112 ***	1.106 ***	1.064 ***	1.104 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
cash_stiw	5.009 ***	4.964 ***	4.995 ***	4.992 ***	4.934 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)

Table 5. *Cont.*

VARIABLES	Model (1)	Model (2)	Model (3)	Model (4)	Model (5)
investmentw	1.883 ***	1.901 ***	1.863 ***	1.827 ***	1.938 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
costw	2.391 ***	2.367 ***	2.424 ***	2.487 ***	2.381 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
sales_gw	0.975 ***	0.964 ***	0.968 ***	0.908 ***	0.944 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
Constant	1.582 ***	1.731 ***	1.655 ***	0.892 ***	1.832 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
Observations	8559	8559	8559	8559	8559
R-squared	0.379	0.381	0.379	0.378	0.382
Industry FE	Yes	Yes	Yes	Yes	Yes
Year FE	Yes	Yes	Yes	Yes	Yes

Note: All models are estimated with industry- and year-fixed effects. *, **, and *** denote statistical significance at 10%, 5%, and 1%, respectively. All variables are defined in Table 1.

Table 6. Impact of PR stemming from health topic on the CSR-Q link.

VARIABLES	Model (1)	Model (2)	Model (3)	Model (4)	Model (5)
CSR score	0.006 ***				
	(0.000)				
S score		0.007 ***			0.006 ***
		(0.000)			(0.000)
E score			0.004 ***		0.001
			(0.000)		(0.152)
G score				−0.002 **	−0.003 ***
				(0.025)	(0.000)
sPRiskT_health	0.064	0.056	0.018	0.019	0.053
	(0.230)	(0.494)	(0.386)	(0.673)	(0.538)
sPRiskT_health*CSR score	−0.002				
	(0.200)				
sPRiskT_health*S score		−0.001			−0.001
		(0.451)			(0.611)
sPRiskT_health*E score			−0.001		−0.001
			(0.254)		(0.604)
sPRiskT_health*G score				−0.000	−0.000
				(0.750)	(0.977)
sizew	−0.122 ***	−0.133 ***	−0.119 ***	−0.063 ***	−0.133 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
roaw	3.888 ***	3.905 ***	3.918 ***	3.965 ***	3.950 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
leveragew	1.112 ***	1.113 ***	1.107 ***	1.064 ***	1.106 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
cash_stiw	5.009 ***	4.965 ***	4.997 ***	4.993 ***	4.934 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
investmentw	1.878 ***	1.898 ***	1.856 ***	1.824 ***	1.930 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
costw	2.389 ***	2.367 ***	2.422 ***	2.486 ***	2.380 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
sales_gw	0.973 ***	0.962 ***	0.967 ***	0.908 ***	0.943 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)

Table 6. *Cont.*

VARIABLES	Model (1)	Model (2)	Model (3)	Model (4)	Model (5)
Constant	1.583 ***	1.735 ***	1.653 ***	0.892 ***	1.836 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
Observations	8559	8559	8559	8559	8559
R-squared	0.379	0.381	0.379	0.378	0.382
Industry FE	Yes	Yes	Yes	Yes	Yes
Year FE	Yes	Yes	Yes	Yes	Yes

Note: All models are estimated with industry- and year-fixed effects. *, **, and *** denote statistical significance at 10%, 5%, and 1%, respectively. All variables are defined in Table 1.

Table 7. Impact of PR stemming from institutions topic on CSR-Q link.

VARIABLES	Model (1)	Model (2)	Model (3)	Model (4)	Model (5)
CSR score	0.006 ***				
	(0.000)				
S score		0.007 ***			0.006 ***
		(0.000)			(0.000)
E score			0.004 ***		0.001
			(0.000)		(0.129)
G score				−0.002 **	−0.003 ***
				(0.024)	(0.000)
sPRiskT_institutions	0.019	0.012	−0.014	0.025	0.046
	(0.668)	(0.759)	(0.592)	(0.602)	(0.370)
sPRiskT_institutions*CSR score	−0.001				
	(0.362)				
sPRiskT_institutions*S score		−0.001			−0.001
		(0.406)			(0.366)
sPRiskT_institutions*E score			−0.000		0.001
			(0.899)		(0.343)
sPRiskT_institutions*G score				−0.001	−0.001
				(0.364)	(0.350)
sizew	−0.122 ***	−0.133 ***	−0.120 ***	−0.063 ***	−0.134 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
roaw	3.885 ***	3.902 ***	3.916 ***	3.966 ***	3.947 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
leveragew	1.112 ***	1.111 ***	1.106 ***	1.065 ***	1.105 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
cash_stiw	5.012 ***	4.966 ***	4.999 ***	4.996 ***	4.935 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
investmentw	1.868 ***	1.888 ***	1.845 ***	1.809 ***	1.919 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
costw	2.388 ***	2.365 ***	2.420 ***	2.485 ***	2.379 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
sales_gw	0.974 ***	0.963 ***	0.969 ***	0.908 ***	0.945 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
Constant	1.583 ***	1.732 ***	1.654 ***	0.892 ***	1.841 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
Observations	8559	8559	8559	8559	8559
R-squared	0.379	0.381	0.379	0.378	0.382
Industry FE	Yes	Yes	Yes	Yes	Yes
Year FE	Yes	Yes	Yes	Yes	Yes

Note: All models are estimated with industry- and year-fixed effects. *, **, and *** denote statistical significance at 10%, 5%, and 1%, respectively. All variables are defined in Table 1.

Table 8. Impact of PR stemming from tax topic on CSR-Q link.

VARIABLES	Model (1)	Model (2)	Model (3)	Model (4)	Model (5)
CSR score	0.006 ***				
	(0.000)				
S score		0.007 ***			0.006 ***
		(0.000)			(0.000)
E score			0.004 ***		0.001
			(0.000)		(0.148)
G score				−0.002 **	−0.003 ***
				(0.026)	(0.000)
sPRiskT_tax	0.013	0.022	0.016	−0.015	−0.014
	(0.779)	(0.601)	(0.669)	(0.765)	(0.791)
sPRiskT_tax*CSR score	−0.000				
	(0.792)				
sPRiskT_tax*S score		−0.000			−0.000
		(0.600)			(0.839)
sPRiskT_tax*E score			−0.000		−0.001
			(0.607)		(0.633)
sPRiskT_tax*G score				0.000	0.001
				(0.648)	(0.404)
sizew	−0.122 ***	−0.133 ***	−0.120 ***	−0.063 ***	−0.133 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
roaw	3.885 ***	3.903 ***	3.915 ***	3.964 ***	3.946 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
leveragew	1.111 ***	1.111 ***	1.106 ***	1.064 ***	1.104 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
cash_stiw	5.010 ***	4.966 ***	4.997 ***	4.993 ***	4.936 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
investmentw	1.885 ***	1.905 ***	1.866 ***	1.829 ***	1.947 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
costw	2.390 ***	2.366 ***	2.423 ***	2.487 ***	2.380 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
sales_gw	0.975 ***	0.964 ***	0.969 ***	0.908 ***	0.944 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
Constant	1.579 ***	1.729 ***	1.653 ***	0.890 ***	1.827 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
Observations	8559	8559	8559	8559	8559
R-squared	0.379	0.381	0.379	0.378	0.382
Industry FE	Yes	Yes	Yes	Yes	Yes
Year FE	Yes	Yes	Yes	Yes	Yes

Note: All models are estimated with industry- and year-fixed effects. *, **, and *** denote statistical significance at 10%, 5%, and 1%, respectively. All variables are defined in Table 1.

Table 9. Impact of PR stemming from technology topic on CSR-Q link.

VARIABLES	Model (1)	Model (2)	Model (3)	Model (4)	Model (5)
CSR score	0.006 ***				
	(0.000)				
S score		0.007 ***			0.007 ***
		(0.000)			(0.000)
E score			0.004 ***		0.001
			(0.000)		(0.136)
G score				−0.002 **	−0.003 ***
				(0.024)	(0.000)
sPRiskT_technology	−0.012	−0.017	−0.017	0.021	0.009
	(0.729)	(0.584)	(0.460)	(0.511)	(0.763)

Table 9. *Cont.*

VARIABLES	Model (1)	Model (2)	Model (3)	Model (4)	Model (5)
sPRiskT_technology*CSR score	0.000				
	(0.690)				
sPRiskT_technology*S score		0.000			0.000
		(0.532)			(0.681)
sPRiskT_technology*E score			0.001		0.001
			(0.251)		(0.209)
sPRiskT_technology*G score				−0.000	−0.001
				(0.501)	(0.256)
sizew	−0.122 ***	−0.133 ***	−0.120 ***	−0.063 ***	−0.133 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
roaw	3.886 ***	3.905 ***	3.917 ***	3.965 ***	3.952 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
leveragew	1.111 ***	1.112 ***	1.107 ***	1.064 ***	1.107 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
cash_stiw	5.011 ***	4.967 ***	4.996 ***	4.993 ***	4.936 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
investmentw	1.880 ***	1.896 ***	1.851 ***	1.820 ***	1.916 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
costw	2.390 ***	2.367 ***	2.423 ***	2.486 ***	2.380 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
sales_gw	0.975 ***	0.964 ***	0.970 ***	0.908 ***	0.946 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
Constant	1.578 ***	1.725 ***	1.653 ***	0.892 ***	1.834 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
Observations	8559	8559	8559	8559	8559
R-squared	0.379	0.381	0.379	0.378	0.382
Industry FE	Yes	Yes	Yes	Yes	Yes
Year FE	Yes	Yes	Yes	Yes	Yes

Note: All models are estimated with industry- and year-fixed effects. *, **, and *** denote statistical significance at 10%, 5%, and 1%, respectively. All variables are defined in Table 1.

Table 10. Impact of PR stemming from trade topic on CSR-Q link.

VARIABLES	Model (1)	Model (2)	Model (3)	Model (4)	Model (5)
CSR score	0.006 ***				
	(0.000)				
S score		0.007 ***			0.006 ***
		(0.000)			(0.000)
E score			0.004 ***		0.001
			(0.000)		(0.139)
G score				−0.002 **	−0.003 ***
				(0.026)	(0.000)
sPRiskT_trade	−0.062	−0.060 *	−0.054 *	0.035	0.009
	(0.160)	(0.073)	(0.087)	(0.499)	(0.869)
sPRiskT_trade*CSR score	0.001				
	(0.168)				
sPRiskT_trade*S score		0.001 *			0.000
		(0.052)			(0.924)
sPRiskT_trade*E score			0.001 *		0.001
			(0.061)		(0.543)
sPRiskT_trade*G score				−0.001	−0.001
				(0.339)	(0.143)
sizew	−0.122 ***	−0.133 ***	−0.120 ***	−0.063 ***	−0.133 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
roaw	3.889 ***	3.908 ***	3.921 ***	3.964 ***	3.951 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)

Table 10. *Cont.*

VARIABLES	Model (1)	Model (2)	Model (3)	Model (4)	Model (5)
leveragew	1.110 ***	1.110 ***	1.105 ***	1.064 ***	1.105 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
cash_stiw	5.013 ***	4.971 ***	5.000 ***	4.995 ***	4.942 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
investmentw	1.870 ***	1.886 ***	1.844 ***	1.820 ***	1.916 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
costw	2.385 ***	2.362 ***	2.417 ***	2.487 ***	2.377 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
sales_gw	0.975 ***	0.964 ***	0.969 ***	0.908 ***	0.945 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
Constant	1.578 ***	1.725 ***	1.656 ***	0.886 ***	1.831 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
Observations	8559	8559	8559	8559	8559
R-squared	0.379	0.381	0.379	0.378	0.382
Industry FE	Yes	Yes	Yes	Yes	Yes
Year FE	Yes	Yes	Yes	Yes	Yes

Note: All models are estimated with industry- and year-fixed effects. *, **, and *** denote statistical significance at 10%, 5%, and 1%, respectively. All variables are defined in Table 1.

Table 11. Impact of PR stemming from security topic on CSR-Q link.

VARIABLES	Model (1)	Model (2)	Model (3)	Model (4)	Model (5)
CSR score	0.006 ***				
	(0.000)				
S score		0.007 ***			0.006 ***
		(0.000)			(0.000)
E score			0.004 ***		0.001
			(0.000)		(0.137)
G score				−0.002 **	−0.003 ***
				(0.026)	(0.000)
sPRiskT_security	0.046	0.061	0.009	−0.000	0.046
	(0.255)	(0.127)	(0.743)	(0.999)	(0.249)
sPRiskT_security*CSR score	−0.001				
	(0.196)				
sPRiskT_security*S score		−0.001 *			−0.002 **
		(0.055)			(0.011)
sPRiskT_security*E score			−0.000		0.001
			(0.753)		(0.283)
sPRiskT_security*G score				0.000	0.001
				(0.905)	(0.402)
sizew	−0.122 ***	−0.134 ***	−0.120 ***	−0.063 ***	−0.134 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
roaw	3.883 ***	3.898 ***	3.916 ***	3.965 ***	3.942 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
leveragew	1.111 ***	1.110 ***	1.106 ***	1.064 ***	1.103 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
cash_stiw	5.008 ***	4.960 ***	4.996 ***	4.993 ***	4.928 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
investmentw	1.883 ***	1.901 ***	1.862 ***	1.827 ***	1.939 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
costw	2.390 ***	2.365 ***	2.423 ***	2.487 ***	2.379 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)

Table 11. *Cont.*

VARIABLES	Model (1)	Model (2)	Model (3)	Model (4)	Model (5)
sales_gw	0.974 ***	0.962 ***	0.969 ***	0.908 ***	0.944 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
Constant	1.582 ***	1.738 ***	1.654 ***	0.891 ***	1.846 ***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
Observations	8559	8559	8559	8559	8559
R-squared	0.379	0.381	0.379	0.378	0.382
Industry FE	Yes	Yes	Yes	Yes	Yes
Year FE	Yes	Yes	Yes	Yes	Yes

Note: All models are estimated with industry- and year-fixed effects. *, **, and *** denote statistical significance at 10%, 5%, and 1%, respectively. All variables are defined in Table 1.

Finally, we re-estimate Equation (2) for each industry in our sample (we have nine industries: communications, consumer discretionary, consumer staples, energy, health care, industrials, materials, real estate, and technology). This allows us to better control industry effects and make sure they are not driving our findings. The results suggest that the neutral impact of PR on firm value and on the CSR–firm value relationship holds for all industries, suggesting a uniform neutral impact across industries. For the sake of brevity, we do not report these results.

5. Discussion

This paper examines whether firm-level (idiosyncratic) political risk (PR) affects the relationship between corporate social responsibility (CSR) and firm value. We developed four hypotheses. The first and second hypotheses are mutually exclusive; the first hypothesis predicts a negative relationship between PR and firm value, while the second hypothesis predicts a neutral relationship between PR and firm value. The third hypothesis suggests that CSR is positively related to firm value, whereas the fourth hypothesis suggests that PR will moderate the CSR–firm value relationship. Our main findings are as follows. First, firm-level PR does not affect firm value. Second, CSR is positively related to firm value. Finally, PR has no effect on the CSR–firm value relationship. In sum, our results provide support only to the second and third hypotheses.

Our first finding indicates that, on average, variations in firm-specific PR do not explain differences in firm value. Most studies in the literature rely on the real option channel and informational channel to explain the valuation effects of high PR. Our first finding provides support to alternative channel which is the managerial risk-taking incentives. The option-value of an investment delay can be high when PR is high [36,45]. PR can also increase managerial risk aversion. The board of directors understand that high PR coupled with managers' inherent risk aversion (loss aversion) can push firms' managers to choose the option-to-wait component of investment decisions [43,63]. This can result in suboptimal risk-taking strategies when managers choose not to support high-risk and high-yield investment opportunities [43,63]. The managerial risk-taking incentives channel assumes that PR carries not only the possibility for delayed investments but also the possibility for new potential investment opportunities created by a high-PR environment. It also assumes that managers can avoid "negative" uncertainty while making use of " positive" uncertainty during high-PR periods [43,62,63]. In this respect, boards can provide more powerful and optimal risk-taking incentives that allow managers to support adequately high-risk and high-yield investment projects in periods of severe PR. A direct managerial implication of this is that well-designed risk-taking incentives during times of high PR can help offset the negative effects of PR, if any. That is, adequate risk-management strategies during high-PR periods can preserve firm value.

Our second finding suggests a positive relationship between CSR and firm value. This is consistent with the results reported in previous studies [12–17] as well as the stakeholder theory which predicts that CSR adds value to a firm. This positive relationship between CSR

and firm value is mainly driven by the social component of CSR. However, the governance component of CSR is negatively related to firm value, whereas the environment component of CSR has no impact on firm value. Therefore, the different CSR components have different impacts on firm value. This result highlights the importance of examining the individual CSR dimensions along with the aggregate CSR and has implications for academic research, managers, investors, and policymakers. For instance, several studies [27,33,34] consider only E and S when computing their aggregate CSR measure. They argue that governance is not part of a firm's CSR remit. However, ESG data providers such as Refinitiv, Bloomberg, and S&P Global Market Intelligence as well as investors (as evidenced by the UN backed PRI) consider G as part of a firm's CSR engagement. We argue that this gap between academics and practitioners is an important issue that could be addressed in future research. In [27], the researchers argued that the link between CSR and corporate governance is unexplored and called for further work on this topic.

Our third finding suggests that firm-level PR is not a moderator of the CSR–firm value relationship, regardless of the PR type. Thus, the benefits of CSR are not affected by the level of firm-specific (idiosyncratic) exposure to PR. The authors of [34] found that CSR is positively related to firm value only when the economic policy uncertainty index (a proxy for systematic political risk) is high. In a sense, our findings complement those reported by [34]. In ref. [34], the authors show that systematic PR is priced in the financial market so that it moderates the CSR–firm value relationship. Our finding suggests that firm-level (idiosyncratic) political risk (PR) is not priced in the financial market and as such it does not affect the CSR–firm value relationship. Neither firm-specific PR in aggregate nor the individual PR components affect the relationship between CSR and firm value. It is important to note that idiosyncratic PR is only one component of the firm's overall idiosyncratic risk. Indeed, portfolio theory suggests that only systematic risk is priced. Firm-specific risk is irrelevant for investors as this could be diversified away when constructing well-diversified portfolios such as the Russell 3000 Index considered in this study.

In addition, CSR engagement appears to create value during "normal" and more "steady-state" times. There are neither additional benefits nor penalties when PR is high. This should encourage managers and increase their incentives to pursue CSR activities without worrying much about their firm-specific PR. It is important to note that this is true for firms with specific characteristics such as those included in the Russell 3000 Index, e.g., larger firms. This should also inform policymakers when developing and implementing their policies designed to promote CSR activities. For instance, policymakers could be inspired from the best CSR practices of industry CSR leaders, e.g., those included in the Russell 3000 Index, and focus their sustainability efforts (e.g., conversion to low-carbon economy, more CSR disclosure and transparency) toward medium and small firms. Policymakers could help them achieve this by providing tax incentives, better access to certain markets, or better access to financing (e.g., some forms of guaranties).

6. Conclusions

The aim of this paper is to investigate whether firm-level (idiosyncratic) political risk (PR) affects the relationship between corporate social responsibility (CSR) and firm value. Based on real option theory and informational argument (managerial risk-taking incentives), we hypothesize that firm-level PR will have a negative (neutral) impact on firm value. Based on the stakeholder theory, we hypothesize that CSR will have a positive impact on firm value. We also hypothesize that PR will moderate the CSR–firm value relationship. We test these hypotheses using a sample of 16,518 firm-year observations which correspond to 2055 unique firms belonging to the Russell 3000 Index over the sample period 2010–2020.

Our main findings are as follows. First, firm-level PR does not affect firm value suggesting that adequate risk-management strategies during high-PR periods can preserve firm value. Second, CSR is positively related to firm value which is mainly driven by the

social component of CSR. However, the governance component of CSR is negatively related to firm value, whereas the environment component of CSR has no impact on firm value. Therefore, the different CSR components have different impacts on firm value. Finally, PR has no effect on the CSR–firm value relationship, regardless of the PR type. Thus, the benefits of CSR are not affected by the level of firm-specific (idiosyncratic) exposure to PR. Our finding suggests that firm-level PR is not priced in the financial market and as such it does not affect the CSR–firm value relationship. This is consistent with portfolio theory which suggests that only systematic risk is priced.

Our work has some limitations that are left for future research. First, our sample selection criteria are restricted to firms belonging to the Russell 3000 Index. This implies that our results could not be generalized to all type of firms and across countries. Therefore, future research could examine the impact of firm-specific PR on the CSR–firm value relationship for other firms not included in such indices (e.g., small and medium firms) in developed and developing countries. For instance, ref. [35] found that politically connected Chinese firms overinvest in CSR to obtain political legitimacy and access to governmental resources. Political connection is perceived negatively by investors. Second, our findings regarding the positive impact of CSR on firm value could be affected by potential endogeneity issues, e.g., omitted factors that affect both CSR and firm value or simultaneity bias between both variables. Addressing this endogeneity issue is challenging because it requires identifying instruments correlated with CSR, but not with firm value or the use of an exogenous shock affecting CSR (e.g., regulatory change). Finally, our work could be seen as exploratory and leads to several interesting research topics. For example, future research could further examine the effects of the different firm-specific PR components (economic, environment, trade, institutions, health, security, tax, and technology) on the different sub-components of the E, S and G dimensions (e.g., diversity, community, and human rights within the S; climate risk within the E dimension; board independence within the G dimension) as some specific channels of PR may have stronger, weaker, or neutral valuation effects. It would be fruitful to also explore industry variation as stakeholders' expectations and CSR issues vary across industries.

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