



Contents lists available at ScienceDirect

European Management Journal

journal homepage: www.elsevier.com/locate/emj

The impact of corporate social performance on the cost of debt and access to debt financing for listed European non-financial firms

Fabio La Rosa ^a, Giovanni Liberatore ^{b,*}, Francesco Mazzi ^b, Simone Terzani ^c

^a Kore University of Enna, Faculty of Economics and Law, Cittadella Universitaria, 94100 Enna, Italy

^b The University of Florence, Economics and Management School, Accounting and Finance Division, Via delle Pandette 9, Building D6, 50127 Florence, Italy

^c University of Perugia, Department of Economics, Via A. Pascoli 20, 06123 Perugia, Italy

ARTICLE INFO

Article history:

Received 23 November 2016

Received in revised form

21 September 2017

Accepted 27 September 2017

Available online xxx

Keywords:

Non-financial performance
Corporate social responsibility
Social performance
Debt cost
Debt financing access

ABSTRACT

This study addresses the controversial issue of how non-financial performance affects the cost of debt capital and access to it. The relationship between corporate social performance and two measures of debt cost (accounting-based and market-based) and the measure of debt access are analysed by means of a multi-theoretical framework combining economics with social theories. By observing a sample of listed European non-financial firms over an 8-year period from 2005 to 2012, we find a negative relationship between corporate social performance and interest rate. Consistent with this result, we find a positive relationship between corporate social performance and debt rating. Thus, corporate social performance has a positive role in reducing the cost of debt capital. Moreover, firms with better corporate social performance are more attractive to lenders in terms of leverage allowance. Overall, our findings provide deeper insight into the reasons why companies should improve their corporate social performance.

© 2017 Published by Elsevier Ltd.

1. Introduction

The accounting literature suggests that companies that consistently make detailed, timely, and informative disclosures obtain numerous market benefits, for example, lower cost of debt capital (COD) (Mazumdar & Sengupta, 2005; Verrecchia, 1983). If the negative relationship between financial disclosure and COD (i.e. the higher disclosure is, the lower is the COD) seems to be clear, the effects of non-financial disclosure are not so univocal because the content of any specific information can differently influence appraisal of risk (Sengupta, 1998). Among all non-financial information, that on corporate social responsibility (CSR) is certainly interesting (Dhaliwal, Li, Tsang, & Yang, 2011), because of its increased demand from stakeholders and the current trend toward CSR (Arvidsson, 2011). In particular, the cost of capital can reflect CSR risks and benefits (Weber, 2008). For example, firms might benefit from lower interest rates (Goss & Roberts, 2011) and higher access to debt capital through CSR (Cheng, Ioannou, & Serafeim, 2014). Following a combined approach aimed at integrating

economic theories (agency cost of debt and voluntary disclosure) with social theories (reputation and stakeholder), we expect companies receive financial benefits by acting responsibly.

This study enters the debate from a unique perspective by examining the impact of a ready-to-use corporate social performance (CSP) index, which is the Datastream/ASSET4, on both the COD and access to debt financing.¹ The use of a commonly available source of information allows us to analyse the link between a flow of information produced by a third party (i.e. Thomson Reuters Datastream) and used by the market, and the cost of debt of a firm. We use two proxies of cost of debt, namely, the interest rate and debt rating (hereafter, 'rating') and a measure of debt access ('leverage'). We analyse this relationship through a sample of European firms listed in the 17 countries which are included in the Standard and Poor's (S&P) Europe 350, from 2005 to 2012. Our results show a negative relationship between interest rate and CSP. Likewise, there is a positive relationship between the rating and CSP. In addition, we find CSP positively impacts debt capital access. Moreover, since during the 2008 global financial crisis companies faced the difficulties of both higher interest rates and credit constraints, we aim to investigate how the credit crisis affected the

* Corresponding author.

E-mail addresses: fabio.larosa@unikore.it (F. La Rosa), giovanni.liberatore@unifi.it (G. Liberatore), francesco.mazzi@unifi.it (F. Mazzi), simone.terzani@unipg.it (S. Terzani).

¹ In this work, we use CSP and social performance interchangeably.

association between CSP and both COD and debt capital access. Our analysis confirms prior results (Hoepner, Oikonomou, Scholtens, & Schröder, 2016), which find no evidence of the link between CSP and COD during the financial crisis years. The results obtained from multivariate analysis are robust to different models' specifications and sensitivity tests.

This study makes three contributions to the existing literature. First, it examines the impact of social performance on the cost of debt, adding new empirical evidence in a research field that has controversial results. Second, this study considers a cross-country European sample, which has rarely been undertaken in the literature to date (Girerd-Potin, Jimenez-Garcès, & Louvet, 2014; Menz, 2010; Perrini, 2005). Third, the study provides evidence of the impact of social performance on the cost of debt when considering a time horizon that includes the ongoing financial crisis.

The remainder of this paper is organised as follows. Section 2 reviews the relevant literature and develops the hypotheses. Section 3 discusses the research methodology. Section 4 presents our findings and Section 5 draws conclusions and implications.

2. Literature review and hypotheses development

2.1. Firms' disclosure and cost of debt

Prior studies argue that by providing more informative disclosures, firms increase demand for their debt and equity issues and thereby lower their cost of capital (Fishman & Hagerty, 1989; Verrecchia, 1983). Empirical evidence is consistent with the view that voluntary public disclosure reduces information asymmetry and facilitates a firm's access to lower-cost external financing. More informative disclosures are found to result in a more effective allocation of capital overall due to reduced information asymmetry, decreased bid–ask spreads, increased stock liquidity, a lower average cost of both equity and debt capital and, consequently, better investment decisions (Healy, Hutton, & Palepu, 1999; Sengupta, 1998).

In particular, the reduction of the COD seems due to the activity and characteristics (e.g. forecast accuracy and dispersion) of analysts, who reduce bond yield spreads, thereby contributing to the information environment of the firm, especially when uncertainty about firm value is at its greatest (Mansi, Maxwell, & Miller, 2011). Therefore, analysts' forecasts and recommendations do affect credit ratings (Cheng & Subramanyam, 2008). Since analysts are important information intermediaries, who help market participants reduce information asymmetry between lenders and managers, the quantity and quality of the information disclosed by companies should lead to a lower COD.

For example, Nikolaev and Van Lent (2005), Sengupta (1998), and Yu (2005) find that there is a negative relationship between interest rate paid and analysts' perceptions of disclosure quality. Similarly, Francis, Khurana, and Pereira (2005) find that firms benefit from expanded disclosure by having a lower cost of both debt and equity capital, after controlling for cross-country institutional differences in legal and financial systems. Mazumdar and Sengupta (2005) confirm this inverse relationship even for private debt, that is, companies with consistently high ratings for voluntary disclosures pay lower interest on their private debt (bank loan) contracts. However, there are mixed results for low-quality corporate disclosure environments. For example, Lopes and de Alencar (2010) find a negative relationship between corporate disclosure in Brazil and cost of debt, with an association even greater than that found for cost of equity. Wang, Sewon, and Claiborne (2008) obtain no evidence that Chinese public firms benefit from extensive voluntary disclosure by having a lower COD. Likewise, Armitage and Marston (2008) obtain mixed evidence in

their UK survey that asked financial directors about disclosure and the cost of debt. Indeed, although 55% of the interviewees believed that greater transparency toward rating agencies and bankers increases the availability of debt or reduces its cost, 38% were unsure whether greater transparency would reduce the cost of debt.

It is possible to explain the mixed empirical evidence not only in terms of the informational environment but also by the nature of the disclosures. While Sengupta (1998, p. 461) focuses on 'the overall disclosure efforts of a firm over a number of years', he recognises that 'the content of any specific disclosure can cause lenders and underwriters to either increase or decrease their estimates of default risk'. Examples of specific disclosures include reporting on intellectual capital, corporate governance, or social issues. For example, Orens, Aerts, and Lybaert (2009) confirm the above-mentioned negative relationship for the case of intellectual capital, and find that firms with greater intellectual capital disclosure benefit from a lower level of information asymmetry, a lower cost of equity capital, and a lower cost of debt capital, and they exhibit higher firm value. Similarly, Ashbaugh-Skaife, Collins, and Lafond (2006), Bhojraj and Sengupta (2003), Byun (2007), and Mansi, Maxwell, and Miller (2004) find corporate governance practices to be negatively related to the cost of debt capital. While these studies find similar and consistent results, mixed evidence seems to characterise the relationship between CSR and the cost of debt. Therefore, we analyse the role of such non-financial information in explaining the cost of and access to debt capital.

2.2. CSR, cost of debt, and access to debt financing

While the relationship between financial disclosure or performance measures and the cost of debt has been analysed to a significant degree (Ahmed, Billings, Morton, & Stanford-Harris, 2002; Jiang, 2008; Reeb, Mansi, & Allee, 2001), there are few and controversial studies on the effects of non-financial, and especially social, performance on the cost of debt. Indeed, the effects of social performance or CSR have been analysed mainly on share price (Murray, Sinclair, Power, & Gray, 2006) and on the cost of equity capital (Girerd-Potin et al., 2014; Reverte, 2012; Wu, Lin, & Wu, 2014).² In particular, Girerd-Potin et al. (2014), by investigating which dimensions of social responsibility concern financial investors (and therefore, affect the cost of equity), leave open the question of which dimensions of social responsibility might impact the cost of debt. Dhaliwal et al. (2011) suggest this quite unexplored avenue of research, and point out that CSR could have a different impact on the cost of debt, as debt-holders have a payoff function which is different from that of equity-holders. Indeed, banks are financially motivated to the same extent as institutional investors, but play a more relevant economic role as delegated monitors (Allen & Santomero, 1997). However, the interest of banks in CSR issues is far from clear.

From a theoretical point of view, the theory of reputation formation in debt markets informs the relationship between social performance and COD (Diamond, 1989). The theory predicts that interest rates will decline over time as firms compile good credit histories. Indeed, there is evidence consistent with Diamond's

² The literature on the definition of CSR and CSP is inconclusive (De Bakker, Groenewegen, & Den Hond, 2005) and uses both terms to denote economic, legal, ethical, and charitable responsibilities (Windsor, 2001). Although we can consider the CSR construct a part of the broader framework of CSP (Carrol, 1979), this framework represents a way to make CSR applicable and put it into practice, that is, to measure social responsibility in terms of performance (Maron, 2006; Matten, Crane, & Chapple, 2003). Therefore, in this work, while we conceptualise CSP and CSR as synonyms, pragmatically, we consider CSP merely as a measure of CSR.

Download English Version:

<https://daneshyari.com/en/article/7423482>

Download Persian Version:

<https://daneshyari.com/article/7423482>

[Daneshyari.com](https://daneshyari.com)