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Corporate social responsibility and systematic risk of restaurant firms: The moderating role of geographical diversification

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HIGHLIGHTS

- This study examines the effect of CSR on a restaurant firm's risk.
- This study examines the moderating role of a restaurant firm's geographical diversification.
- Geographical diversification significantly moderates the relationship between CSR and risk.

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ABSTRACT

Despite growing attention to corporate social responsibility (CSR) in the tourism literature, the relationship between CSR activities and systematic risk, one of the critical components in evaluating shareholder value, has been a topic of scarce examination. Further, the moderating role of geographical diversification on the link between CSR and systematic risk in the restaurant context has not been studied. Therefore, the current study explores these issues in the restaurant context based on the organizational theory and stakeholder theory. In addition, this study dichotomizes CSR activities into two dimensions, socially responsible activities (i.e., positive CSR) and socially irresponsible activities (i.e., negative CSR), to examine the separate effects of the two dimensions. A two-way fixed-effects model that effectively accounts for unobserved effects in a panel data set has been employed to test the proposed hypotheses.

1. Introduction

Abiding interests and concerns for corporate social responsibility (CSR) have become critical components of success in the contemporary corporate world. Major corporations confront significant pressures from stakeholders, including consumers, employees, communities, suppliers, and financiers, to demonstrate their commitment to CSR (Brammer, Pavelin, & Porter, 2006; Melé, 2008). The restaurant industry, which is considered a critical part of the tourism product and is becoming a key part of tourism marketing (Sparks, Bowen, & Klag, 2003), has received increasing attention from the public and corporations, which, in turn, puts intense pressure on restaurant firms to expend resources toward implementing and promoting CSR initiatives (McCool & McCool, 2010; Schubert, Kandampully, Solnet, & Kralj, 2010).

Along with the steady growth of the restaurant industry and stakeholders' heightened attention toward CSR issues, restaurant firms in the United States have vigorously implemented socially responsible business practices. For example, Dunkin' Donuts launched "DD Green," a green building certification program designed to help franchisees build sustainable and energy-efficient restaurants (Cronin, 2014), while Panera Bread pledged to stop using artificial ingredients in its food by the end of 2016 to provide better meals to its community (Orman, 2014). However, CSR initiatives often require substantial financial resources from firms, including, for example, purchasing environmentally-friendly equipment, implementing high quality standards for products, and initiating safety programs. Moreover, despite massive investment in CSR activities, the benefits are often long-term, while the costs involved are usually short-term (Branco & Rodrigues, 2006).

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Thus, researchers have continually attempted to provide tourism and hospitality managers with some answers about the effects of CSR activities on firm performance and value (Inoue & Lee, 2011; Kang, Lee, & Huh, 2010; Kim & Kim, 2014; Lee, Seo, & Sharma, 2013; Lee, Singal, & Kang, 2013; Park & Lee, 2009).

Despite these efforts, the tourism and hospitality literature has not yet reached a definitive conclusion on whether the effect of CSR on corporate financial performance (CFP) is positive, negative, curvilinear, or even insignificant. Most tourism and hospitality scholars have primarily utilized accounting performance (i.e., ROA and ROE) and market performance (i.e., Tobin's q and stock returns) as a proxy for CFP (e.g., Casado-Díaz, Nicolau, Ruiz & Ricardo, 2014; Inoue & Lee, 2011; Kang et al., 2010; Lee, Singal, et al., 2013; Lee, Seo, et al., 2013; Nicolau, 2008; Park & Lee, 2009). However, this approach may provide an incomplete understanding of the relationship between CSR and CFP because CFP is reflected not only in accounting and market performance measures, but also by other measures, such as various business risks. Thus, further investigation is needed to examine the financial implications of CSR in terms of different performance measures for the tourism and hospitality industry. Risk can be defined as the degree to which a firm is vulnerable to internal or external factors that impact its stock value (Sharpe, 1964). For example, a firm's strategies that accompany a heavy investment may lead to intense fluctuation in stock price. However, the relationship between CSR and risk has been largely neglected by tourism and hospitality researchers. Kim and Kim (2014) conducted what is considered a pioneering study on CSR and its influence on risk in the restaurant industry. Their study revealed that socially irresponsible activities (denoted as CSR-strengthening in their study) reduce shareholder value by increasing systematic risk, while socially responsible activities (denoted as CSR-concerning in their study) do not have an impact on systematic risk for restaurant firms. Following the lead set by Kim and Kim's study, the current study attempts to make further contributions to the tourism and hospitality CSR literature in terms of risk context.

In addition to exploring the risk implications of CSR activities, this study proposes a potential moderator into the model. Rowley and Berman (2000) argued that it is important to consider moderating variables for more nuanced explanations of the CSR-CFP relationship. Several studies demonstrated that moderators play a key role in explicitly examining the CSR-CFP link in the tourism and hospitality context. For example, Lee, Singal, et al. (2013) investigated the moderating effect of economic conditions on the relationship between CSR and CFP in the restaurant industry in the United States, while Lee, Seo, et al. (2013) examined oil prices as a moderator for the airline industry in the United States. However, further explorations of potential and interesting moderators are necessary to enhance the tourism and hospitality CSR literature, especially because it is still a novel element of the risk context in the restaurant industry. Of the many potentially important moderators, such as consumer perception, restaurant types (e.g., fast food and full-service), and slack resources, the present study attempts to better explain the effect of CSR on restaurant firms' risk by introducing geographical diversification as a moderator.

Geographical diversification can be defined as the expansion of a firm's operations into multiple locations (Lu & Beamish, 2004). Firms are increasingly diversifying the geographical scope of their businesses for the sake of achieving competitive advantages (Lu & Beamish, 2004), and many restaurant firms have implemented geographical diversification (Park & Jang, 2012). When a firm geographically diversifies its operations, the tendency is to expose a business to more diverse regions and people, creating conditions that make it possible to enhance consumer and market awareness of the company's activities and operations (Lu & Beamish, 2004). This increased awareness may influence the effect of the company's other strategies, such as CSR activities, on its financial performance.

Therefore, building upon the organizational learning theory (Zahra, Ireland, & Hitt, 2000) and stakeholder theory (Freeman, 1984), the current study proposes that the heightened level of consumer awareness of a restaurant firm derived from the implementation of geographical diversification helps that firm to increase the magnitude of the effect of CSR on firm risk. Following Kang et al. (2010), the current study categorizes CSR into two dimensions: positive CSR (i.e., socially responsible activities) and negative CSR (i.e., socially irresponsible activities). Given the extremely limited body of literature on CSR and firm risk in the tourism and hospitality context, this study contributes not only to the existing CSR literature, but also to the tourism and hospitality literature, by providing insights to guide strategic decision-making for CSR activities.

The study proceeds as follows: First, the literature review section outlines the conceptual background and develops hypotheses. The methodology section describes the data and econometrics techniques used to test the proposed hypotheses. The final two sections present empirical results and conclude the study with discussions, limitations, and suggestions for future research.

2. Literature review

2.1. CSR and systematic risk

The publication of “Social Responsibility of the Businessman” by Howard R. Bowen and Johnson, (1953) represents the genesis of the modern period of literature on CSR (Carroll, 1999). Numerous scholars have since attempted to develop an explicit and robust definition of CSR. According to a content analysis of existing CSR definitions conducted by Dahlsrud (2008, p. 7), CSR is “[a] concept whereby companies integrate social and environmental concerns in their business operations and in their interaction with their stakeholders on a voluntary basis,” as defined by Commission of European Communities in 2001. This definition has been widely accepted in the academic and business context.

Alongside increasing interest in, and attention to, CSR activities from the general economy and public, the tourism and hospitality industry also started implementing CSR initiatives. For example, the American Hotel and Motel Association's Code of Operating Practices in 1972 clarified socially responsible business operations that focused mostly on guests and ethical business behaviors. In addition, the International Hotel and Restaurant Association (IHRA) organized a global council in 2003 to provide a guideline for business practices on CSR activities. Clarkson (1995) contended that the multidimensionality of CSR is more evaluable within a framework involving various stakeholders' interests that closely align with the stakeholder theory proposed by Freeman (1984). Based on the notion put forth by Clarkson (1995) and Freeman (1984) on the stakeholder framework, many subsequent studies have measured the dimension of CSR activities with the Kinder, Lydenburg, Domoni (KLD) data that represent a firm's attention to stakeholder issues, including five categories of CSR activities: (1) employee relations; (2) product quality; (3) community relations; (4) environmental issues; and (5) diversity issues.

In addition to the multidimensionality issue, it should be noted that a firm can simultaneously engage in socially responsible and irresponsible activities. Also, the fact that a firm participates in more socially responsible initiatives does not necessarily mean that it engages in fewer socially irresponsible initiatives (Tang, Qian, Chen, & Shen, 2015). For instance, while firms may initiate environmentally-friendly and proactive activities, they may commit willful violations of employee health and safety standards.