

Corporate Actions as Moral Issues

Elisabeth Kempf Oliver Spalt

Harvard Business School, CEPR, & NBER

University of Mannheim & ECGI

June 2024

Introduction

- Exploding interest in investing along environmental, social, and governance **(ESG) criteria**
 - Frequently motivated via investors' **nonpecuniary preferences** (e.g., Pastor, Stambaugh, Taylor (JFE 2021))

$$\text{Investor } i\text{'s utility} = -e^{-\overbrace{A_i \tilde{W}_i}^{\text{Financial}} \underbrace{-b_i' X_i}_{\text{Nonpecuniary}}}$$

Introduction

- Exploding interest in investing along environmental, social, and governance **(ESG) criteria**
 - Frequently motivated via investors' **nonpecuniary preferences** (e.g., Pastor, Stambaugh, Taylor (JFE 2021))

$$\text{Investor } i\text{'s utility} = -e^{-\underbrace{A_i}_{\text{Financial}} \tilde{W}_i - \underbrace{b_i' X_i}_{\text{Nonpecuniary}}}$$

- Surveys reveal moral or ethical concerns as an important motivation for ESG investing (e.g., Giglio et al. (2023), Kruger et al. (2020))

Introduction

- Exploding interest in investing along environmental, social, and governance **(ESG) criteria**
 - Frequently motivated via investors' **nonpecuniary preferences** (e.g., Pastor, Stambaugh, Taylor (JFE 2021))

$$\text{Investor } i\text{'s utility} = -e^{-\overbrace{A_i}^{\text{Financial}} \tilde{W}_i - \overbrace{b_i' X_i}^{\text{Nonpecuniary}}}$$

- Surveys reveal moral or ethical concerns as an important motivation for ESG investing (e.g., Giglio et al. (2023), Kruger et al. (2020))
- Open questions:
 - ① Which firm attributes generate nonpecuniary utility?
 - ② How do those concerns rank relative to financial motives?
 - ③ Heterogeneity in nonpecuniary preferences?

- **This project:** Study **nonpecuniary preferences** of a representative sample of 3,000 Americans over **a broad range of corporate actions** frequently studied in corporate finance

- **This project:** Study **nonpecuniary preferences** of a representative sample of 3,000 Americans over **a broad range of corporate actions** frequently studied in corporate finance
- Main findings:
 - ① Concerns about **treatment of workers** and **high CEO pay** rank highest, with surprisingly *little heterogeneity* across participants
 - Higher than concerns about workforce diversity and clean energy usage

- **This project:** Study **nonpecuniary preferences** of a representative sample of 3,000 Americans over **a broad range of corporate actions** frequently studied in corporate finance
- Main findings:
 - ① Concerns about **treatment of workers** and **high CEO pay** rank highest, with surprisingly *little heterogeneity* across participants
 - Higher than concerns about workforce diversity and clean energy usage
 - ② Participants trade off moral concerns against monetary costs
 - For a \$100 increase in personal cost, the share of respondents in favor of moral actions decreases by 3.3 ppt

- **This project:** Study **nonpecuniary preferences** of a representative sample of 3,000 Americans over **a broad range of corporate actions** frequently studied in corporate finance
- Main findings:
 - ① Concerns about **treatment of workers** and **high CEO pay** rank highest, with surprisingly *little heterogeneity* across participants
 - Higher than concerns about workforce diversity and clean energy usage
 - ② Participants trade off moral concerns against monetary costs
 - For a \$100 increase in personal cost, the share of respondents in favor of moral actions decreases by 3.3 ppt
 - ③ **Shareholders report a greater willingness to pay** for morally desirable corporate actions than customers or employees

Survey

- Survey among **3,000 participants** representative of the adult U.S. population in terms of gender, age, race, and ethnicity
- Conducted in June 2023 via Qualtrics
- Standard set of socio-demographic variables
- Asked about moral perceptions of 11 corporate actions, whose order is randomized
- Framed as **legal and positive NPV** decisions by hypothetical supermarket chain “XYZCorp”
- **Randomly assigned stakeholder** treatment group (customer, employee, or shareholder)

- S1 (Layoffs): “Lay off employees.”
- S2 (Outsourcing): “Outsource parts of its operations in the United States to a foreign country with lower wages.”
- S3 (Taxes): “Reduce the taxes it pays in the United States by having more of its profits taxed in low-tax countries.”
- S4 (Incentive Pay): “Decrease base salaries (which are not linked to an employee’s performance) and increase bonuses (which are linked to an employee’s performance) for the firms’ employees.”
- S5 (Wage Reduction): “Reduce workers’ salaries at a recently acquired firm.”
- S6 (Diversity): “Not introduce a new hiring system to increase the gender and racial diversity of its workforce.”

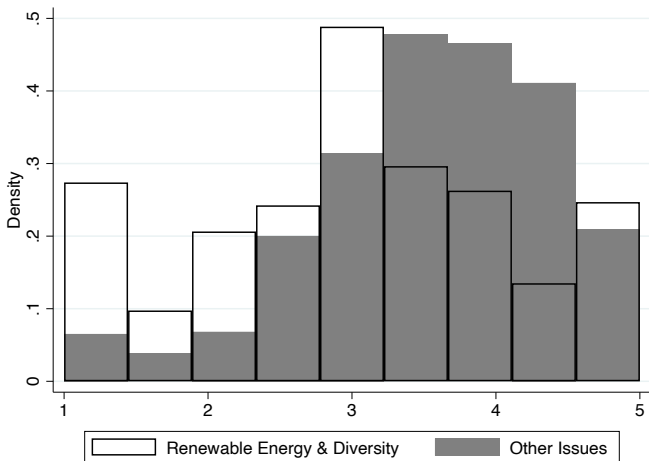
- S7 (CEO Pay): “Pay the CEO \$15 million in total compensation this year, which is 300 times the pay of the average employee at the company.”
- S8 (Renewable Energy): “Not require its suppliers to increase the share of renewable energy usage.”
- S9 (Dividends): “Keep dividend payments to shareholders unchanged while implementing a rigorous cost cutting program at the company.”
- S10 (Leverage): “Take out a loan in order to pay a dividend to its shareholders (thereby increasing the risk of bankruptcy and reducing corporate tax payments).”
- S11 (Board Independence): “Appoint the current CEO also as the Chairman of the Board, giving the CEO more power inside the company.”

Questions about moral preferences:

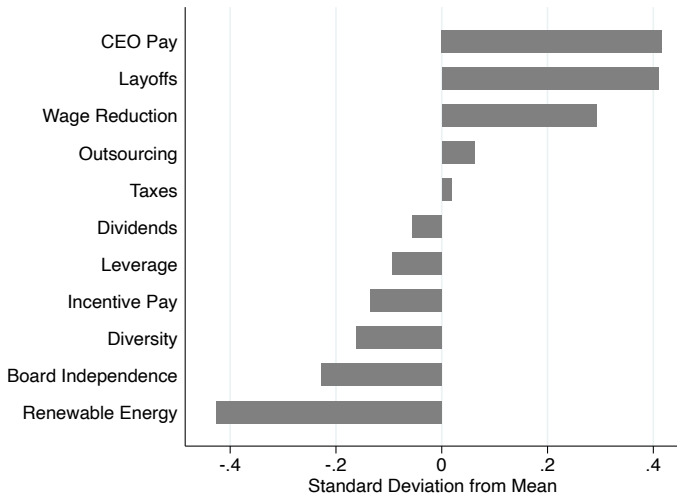
- “On a scale from 1 (strongly disagree) to 5 (strongly agree), tell us your reactions to the following statements:”
 - ① Q1: “This is purely a financial decision. When evaluating it, morals should play no role.”
 - ② Q2: “This is morally wrong.”
- Q3: “Please rate the following 11 items according to how much they represent moral issues using a scale from 1 (not a moral issue at all) to 5 (clearly a moral issue).”

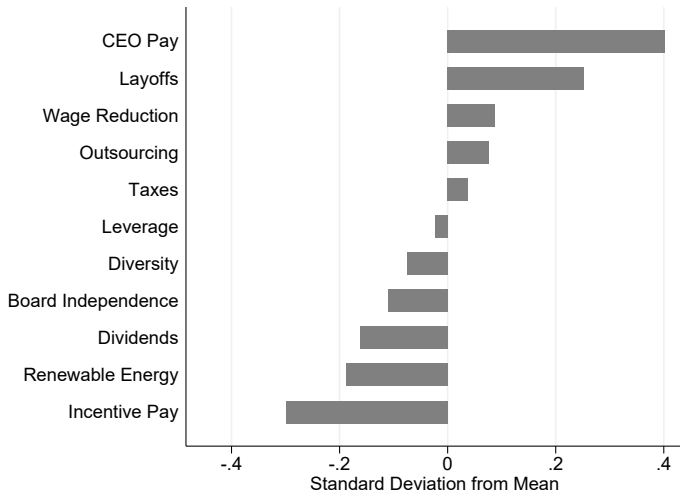
Questions about trade-offs:

- Assess whether respondents would be in favor of the company pursuing the morally more appealing action, with varying costs (\$0 vs. \$100 vs. \$500)
- Yes/no question
- Example: “If the company decided to pay all taxes domestically, prices of their products would be higher. These measures would result in you spending \$100 more this year at their shops. Would you be in favor of XYZCorp paying all taxes domestically?”

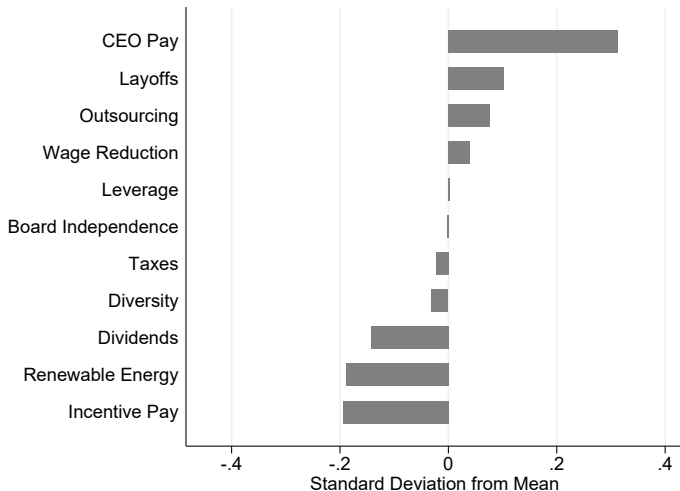


- Means: All (3.45), Renewables & Diversity (3.04), Other (3.54)





- For the average action, 26% disagree with statement that the decision is morally wrong, whereas 46% agree



- Only 10.6% strongly agree with the statement that this is a “*purely financial decision and morals should play no role*”

- These findings stand in stark contrast to (i) current focus of ESG debate and (ii) current practice in executive compensation contracts:

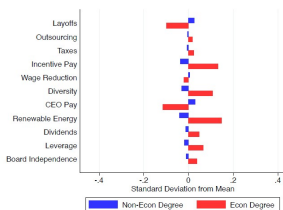
Bebchuk & Tallarita (2022): *“with respect to employees [...] most companies choose goals related to inclusion or diversity and many focus on work accidents and illness, but none incentivizes its CEO to increase salaries or benefits or to improve job security.”*

- On average moral concerns are particularly salient for:
 - **Democrats** especially diversity and renewable energy usage
 - **Older people:** especially CEO pay, outsourcing, and financial leverage
 - **Females**

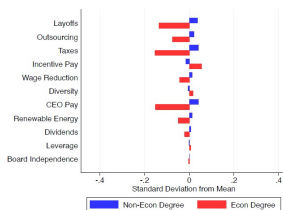
- On average moral concerns are particularly salient for:
 - **Democrats** especially diversity and renewable energy usage
 - **Older people:** especially CEO pay, outsourcing, and financial leverage
 - **Females**
- Overall, **less heterogeneity in relative rankings** than in absolute rankings

- On average moral concerns are particularly salient for:
 - **Democrats** especially diversity and renewable energy usage
 - **Older people:** especially CEO pay, outsourcing, and financial leverage
 - **Females**
- Overall, **less heterogeneity in relative rankings** than in absolute rankings
 - *All* subgroups agree that CEO pay ranks among the two most important moral issues; *none* rank renewable energy among top three

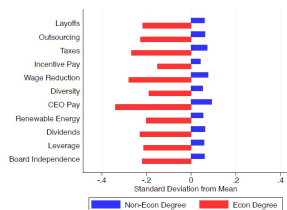
- Zooming in on **respondents with econ-related degree**:



(s) Moral Issue



(t) Morally Wrong



(u) Moral vs. Financial Issue

- **Teaching success or problem?**

Questions about trade-offs:

- Assess whether respondents would be in favor of the company pursuing the morally more appealing action, with varying costs (\$0 vs. \$100 vs. \$500)
- Yes/no question
- Example: “If the company decided to pay all taxes domestically, prices of their products would be higher. These measures would result in you spending \$100 more this year at their shops. Would you be in favor of XYZCorp paying all taxes domestically?”

	Employee (1)	Customer (2)	Shareholder (3)	All (4)
Cost ('00 \$)	-0.043*** (-19.95)	-0.040*** (-18.55)	-0.017*** (-7.66)	-0.033*** (-26.60)
Constant	0.640*** (102.02)	0.621*** (98.41)	0.646*** (104.33)	0.636*** (175.82)
R ²	0.035	0.030	0.005	0.021
N	10,985	10,951	11,051	32,987

- For every \$100 increase in personal costs, the fraction of respondents who favor the moral action decreases by 3.3 percentage points

	Employee (1)	Customer (2)	Shareholder (3)	All (4)
Cost ('00 \$)	-0.043*** (-19.95)	-0.040*** (-18.55)	-0.017*** (-7.66)	-0.033*** (-26.60)
Constant	0.640*** (102.02)	0.621*** (98.41)	0.646*** (104.33)	0.636*** (175.82)
R ²	0.035	0.030	0.005	0.021
N	10,985	10,951	11,051	32,987

- For every \$100 increase in personal costs, the fraction of respondents who favor the moral action decreases by 3.3 percentage points
- Average cost elasticity similar to Hart, Thesmar, Zingales (2023), but stakeholder variation is different

Conclusion

- First study of a representative sample of Americans' **moral views of a broad range of corporate actions**
- Main findings:
 - ① **The treatment of workers** and **pay inequality** are perceived to be significantly more of a moral issue than recently emphasized ESG issues (e.g., diversity, renewable energy usage)
 - ② **Shareholders report a greater willingness to pay** for morally desirable corporate actions than customers or employees
- Broad implications for finance researchers, instructors, and practitioners