Journal of Business Ethics (2007) 70:165–174
DOI 10.1007/s10551-006-9103-8
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Corporate Social Responsibility and Socially Responsible Investing: A Global Perspective

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ABSTRACT. This research examines the relationship between corporate social responsibility (CSR) and company stock valuation across three regions of the world. After a brief introduction, the article gives an overview of the evolving definition of CSR as well as a discussion of the ways in which this construct has been operationalized. Presentation of the potential impact of corporate social performance on firm financial performance follows, including investor characteristics, the rationale behind their choices, and their influence on the marketplace for securities worldwide. The unique method used to select socially responsible investments is then provided that also includes a description of the quantitative techniques employed in the analyses. Results are offered subsequently, and the close describes implications for global enterprises as socially responsible investments.

KEY WORDS: Corporate social responsibility, global investments

> The obligation to work for social betterment is the essence of the notion of corporate social responsibility. (Frederick, 1994, p. 151)

Contentious debate over the modern relevance of corporate social responsibility was spawned by the economist Milton Friedman (1970), who argued that public companies possess only minimal ethical obligations (e.g., to operate within the societal ethical frame, to avoid deception and fraud) beyond maximizing profits and obeying the law. However, this position has few adherents, especially among the scholarly community interested in practical ethics, moral maturity, and/or the intersection between business and society. For example, business ethicists often discuss the essential role of multiple interests in the decision calculus of effective executives (Carroll, 1999). Additionally, researchers in other fields have studied the positive impact of moral reasoning on the performance of managers and employees who have boundary-spanning occupations (Goolsby and Hunt, 1992).

Given the importance of social consciousness and actions to a firm's success, authors such as Brigham, Gapenski, and Ehrhardt (1999, p. 3) ask the question: "How do we balance social concerns against the need to create value for our shareholders?" For-profit companies now recognize the benefits of principled behavior but may fail to understand the potential costs. For instance, activities deemed acceptable or appropriate by one constituency may be viewed as undesirable or immoral by another (Robin and Reidenbach, 1987). Furthermore, business leaders who pay too much attention on philanthropy or social issues may neglect the primary reason for their existence (Murphy, 1994). In order to avoid such potential problems, organizations need to develop a clear understanding of this multidimensional construct.

Operational definitions of *corporate social responsibility* (CSR) vary widely by epoch and author, with the three-dimensional model of Carroll (1979) as an exemplar. At its core is the deep-seated belief that "business organizations have societal obligations which transcend economic functions of producing and distributing scarce goods and services and generating a satisfactory level of profits for their shareholders" (Epstein, 1989, p. 585). A major implication for managers is that they must be constantly in tune with the dynamic nature of the needs and desires of the public that explicitly or implicitly influence their accomplishments (L'Etang, 1995). Thus, the myriad ways in which these different groups react to ownership opportunities are due, in part, to the economic, legal, ethical, and

discretionary/philanthropic actions of firms within the public domain (Carroll, 1998).

The purpose of this paper is to examine the relationship between corporate social responsibility and company stock valuation across three regions of the world. The next section provides an overview of the evolving definition of CSR, along with a discussion of the ways in which this construct has been utilized in practice. Presentation of the potential relationship between corporate social responsibility and financial performance follows, emphasizing characteristics of such investors, the rationale behind their choices, and their impact upon the marketplace for securities worldwide. The method employed in the selection of a socially responsible investment is then provided that also includes a description of the quantitative techniques used in the analysis. The results are offered subsequently, and the conclusion discusses implications for socially responsible investing.

Corporate social responsibility theory and practice

Modern theoretical discussions of corporate social responsibility occurred during the latter half of the twentieth century as a result of growing attention to the impact of business activity on the larger society (see Carroll, 1999 for a more expansive account). For example, a rebirth of interest in chronicling the social responsibilities of business and its leadership occurred in the 1950s that included activities aimed at meeting important societal goals. The radical political agendas and reform movements of the 1960s caused an escalation of vigilance, which led by the 1970s to public demands for businesses to broaden their focus to previously ignored social issues. The 1980s saw an attempt to organize CSR activities into categories that considered the impact of such organizational actions on internal and external constituencies of firms.

Between the mid-1980s and the turn of the century, the term *stakeholder* became part of the language used by scholars to delineate any constituency or person who can affect or is affected by the goal-oriented actions of an organization (Freeman, 1984). The addition of this concept to the CSR literature eventually moved the focus away from an examination of independent entities interacting and influencing one another to an investigation of business and society as interwoven in a complex web of dependency and expectation (Nasi et al., 1997; Wood, 1991). This perspective culminated in the seminal work of Frederick (1998), who posits a naturological/biological model of the corporation and its community that directs their mutually supporting and competing relationships (also see Hill and Cassill, 2004).

The practical implications of CSR have received much attention. Research suggests that corporate social responsibility represents a differentiating factor that may be used successfully by firms to distinguish themselves within their industries (Drumwright, 1994). Proponents of this position believe that investors interested in using their decisions to effect social change are substantial in size and buying power. These ''buyers'' are likely to frame their evaluations of alternative products or stock offerings within the context of the parent companies' alignment with their beliefs and values (Kelley and Elm, 2003). Such findings are consistent across a number of countries that represent different cultural dictates, aspirations, and consequences for actions (Maignan, 2001).

The primary way in which businesses are assessed by potential investors is through perceived corporate social performance (CSP). This indicator measures the ability of firms to meet or exceed the expectations of various stakeholder groups on important social issues (Wood, 1991). Thus, companies that provide socially responsible products, engage in cause-related marketing, or donate to non-business entities may engender CSR associations that enhance their overall product or brand evaluations (Becker-Olson et al., 2006; Dacin and Brown, 1997; Machan, 2004; Smith and Alcorn, 1991). While some scholars question the reporting reliability of CSP information in the United States and Europe (see Laufer, 2003), the preponderance of evidence triangulates around the belief that CSR is an important form of investment by the corporation.

Socially responsible investing

The linkage between corporate social responsibility and firm financial performance has received considerable research attention (see Margolis and Walsh,

2001; Orlitzky et al., 2003), especially in the area of socially responsible investing (SRI). One particularly relevant definition of this construct was advanced by the UK Investment Forum, which describes SRI as ''investments enabling investors to combine financial objectives with their social values'' (Munoz-Torres et al., 2004, p. 200). These individuals are said to ''mix money with morality'' in their decision-making (Diltz, 1995), and they tend to be younger, better educated, and more concerned about causes such as the environment and labor relations than their less socially conscious counterparts (Rosen et al., 1991). Nonetheless, their objective remains to receive a fair return while simultaneously accomplishing CSR goals.

As Krumsick (2003, p. 583) notes, ''socially responsible investing ... is more wide-spread than ever, in the U.S. as well as Europe and Asia.'' SRI appears to have its origins in the 1940s when unions and government agencies avoided investments with companies perceived to engage in unfair labor practices (Martin, 1986). This focus on values-based investing experienced rapid expansion during 1970s because of major social upheavals including the Vietnam War, urban strife, environmental degradation, and Apartheid (Spencer, 2001). By the 1990s the emphasis shifted to human rights violations and global labor standards, particularly in the apparel, shoe, and toy industries (Rivoli, 2003). The most recent set of concerns involves corporate governance, where investors evaluate firms according to their responsiveness to a variety of important stakeholders (Moir, 2001).

Socially responsible investing has grown to where one out of every eight dollars placed in the hands of professional money managers in the United States is dedicated to such investment opportunities (Laufer, 2003). Most of these stock portfolios are subject to a variety of social screens described as inclusionary or exclusionary, which are designed to target companies that meet or fail to meet certain criteria (Spencer, 2001). Examples abound but common criteria exclude firms associated with tobacco, gambling, weapons, and alcohol. Additionally, companies with positive records in their dealings with minorities, women, and their communities often are included. While scholars debate the ability of these screens to operate as intended (see Martin, 1986), the result has been an excess of 1.5 trillion dollars in over 175 mutual funds that include (but not necessarily limited to) SRI options (Stone, 2001).

Whether these funds outperform realistic financial expectations or the broader stock market remains difficult to discern. Typical research results suggest that socially responsible mutual funds achieve returns that are similar to comparable mutual funds without such restrictions (Guerard, 1997; Sauer, 1997). In one of the most rigorous and comprehensive investigations to date, Statman (2000, p. 30) examined ''the performance of socially responsible mutual funds in the 1990–1998 period'' and concluded eloquently ''that their performance gives little reason for either delight or alarm.'' However, more recent and targeted studies reveal different findings. For instance, research focused on the environmental performance of public companies and their shareholder returns found a statistically significant relationship (Dillenburg et al., 2003).

Given this discussion, corporate social responsibility is defined as the economic, legal, moral, and philanthropic actions of firms that influence the quality of life of relevant stakeholders. Each of these constituencies, both individually and collectively, forms opinions about organizations through perceptions of firms' corporate social performance, which is characterized as summary judgments about CSR activities used by investors to make purchase decisions. The purpose of this investigation is to determine whether companies that are well-represented among socially responsible investment portfolios outperform the larger market. SRI funds were chosen because they receive independent scrutiny and confirmation of corporate social performance. The managers of these portfolios evaluate corporate social performance of selected stocks for inclusion with the hope that strong CSP leads to better long-run financial performance. The next section provides additional details on how these investment options were determined and compare to broader opportunities.

Methodology and results

Selection process

Only a limited number of studies show that socially responsible corporations are valued by investors in

the long run relative to firms with no social agenda (see Hill et al., 2003; Shank et al., 2005). To extend this research stream, our inquiry expands investment options to three diverse geographic regions – the United States (i.e., North America), Asia, and Europe. Their inclusion is due to the size of their stock markets, the number of alternative SRI opportunities, and the availability of accurate long-term data. Therefore, the New York, London, and Tokyo stock exchanges were the three global financial markets utilized. Our project mirrors Shank et al. (2005), who chose publicly traded common stocks by examining the holdings of socially responsible mutual funds listed with the Social Investment Forum (SIF). This listing as well as other methods was used to ensure that portfolio companies were externally verified and qualified as SRI funds so that the Most Socially Responsible Firms (Most SRF) within each region could be identified.

To locate the Most SRF, the SIF list of socially responsible mutual funds (SRMF) was examined, but an insufficient number of global offerings were found. Therefore, a series of WWW searches for additional SRMF that had a majority of international holdings were conducted. The funds resulting from this search are listed in Table I. In cases where an investment organization offered two or more global mutual funds, only one was selected for further analysis based on its international exposure. After the SRMF were selected, the next step was to examine their holdings. Current annual reports were obtained for the funds and stock holdings were cross-referenced. Individual stocks were then selected for the three Most SRF portfolios based on the frequency with which they appeared in the SRMF holdings subject to the following restrictions:

1. Companies had to be traded in their home markets *and* offer American Depository Receipts (ADR) on a major U.S. exchange such as the NYSE or NASDAQ. This limitation was established to provide a common frame of reference for the stocks under examination. Additionally, their ADR must have at least five years of historical security prices available (10 years was preferable).
2. In order to include a diverse group of offerings, a limit of three companies per country was set for Europe and four companies per country for Asia. Europe was assigned a lower limit because it has substantially more countries with established socially responsible corporations from which to select. Further, these limits ensure a wider coverage than just British and Japanese enterprises.
3. Companies must appear in at least three separate mutual funds for Europe and at least two for Asia. The multiple-fund requirement was intended to ensure that the most socially responsible companies were selected through an implied consensus of active fund managers. This is very similar to the restriction established in earlier uses but is slightly smaller due to the paucity of international SRMF.

TABLE I

Socially Responsible Mutual Fund (SRMF) List

Fund	Website
AXA Enterprise Global	http://www.enterprisefunds.com
Calvert World Values	http://www.calvert.com
Citizens Global Equity	http://www.citizensfunds.com
Ethical Global Equity (Canada)	http://www.ethicalfunds.com
Henderson GlobalCare Growth	http://www.henderson.com/home/sri/
Kingsway SRI Asia Fund (Hong Kong)	http://www.kingswayfin.com
MMA Praxis International	http://www.mma-online.org
PAX World Values	http://www.paxworld.com
Portfolio 21	http://www.Portfolio21.com
Stewardship International (UK)	http://www.fandc.com
UBS Equity Eco-Performance (Luxemburg)	http://www.ubs.com

The methodology resulted in the selection of a 10-stock Asian portfolio and a 12-stock European portfolio for analysis. In addition to the European and Asian portfolios, we used the U.S. stock portfolio examined by Shank et al. (2005) but employed updated information that was consistent with the international Most SRF portfolios (see Table II for a complete listing of the individual equities). Security price data were sourced from Yahoo! Finance (http://finance.yahoo.com). The final data set was composed of weekly security prices from January 1, 1995 through August 8, 2005. Stock and ADR trading prices over this time period provided the basis for valuation and possible excess returns. In all

TABLE II

Socially Responsible Corporations (Most SRF)

Symbol	Company	Country	Industry
Asia			
CAJ	Cannon	Japan	Photographic Equipment
CHL	China Mobile	Hong Kong	Wireless Communications
KTC	KT	South Korea	Telecommunications Services
NTT	Nippon Telephone & Telegraph	Japan	Telecommunications Services
PKX	Posco	South Korea	Steel & Iron
SKM	SK Telecom	South Korea	Telecommunications Services
SNE	Sony	Japan	Electronic Equipment
TSM	Taiwan Semiconductor	Taiwan	Semiconductors-Integrated Circuits
TM	Toyota Motors	Japan	Automotive
UMC	United Micro Electronics	Taiwan	Semiconductors-Integrated Circuits
Europe			
BRG	BG Group	United Kingdom	Oil & Gas Pipelines
BP	British Petroleum	United Kingdom	Oil & Gas
DT	Deutsche Telekom	Germany	Telecommunications Services
EN	Ente Nazionale per l'Energia Elettrica	Italy	Utilities
PHG	Koninklijke Philips Electronics	Netherlands	Electronic Equipment
NOK	Nokia Oyj	Finland	Communication Equipment
NVO	Novo Nordisk	Denmark	Pharmaceuticals
SAP	SAP	Germany	Application Software
TEF	Telefonica	Spain	Telecommunications Services
UBS	UBS, Inc.	Switzerland	Banking
V	Vivendi Universal	France	Entertainment
VOD	Vodaphone	United Kingdom	Wireless Communications
USA			
AIG	American International Group	United States	Insurance
BAC	Bank of America	United States	Banking
CSCO	Cisco	United States	Networking/Communication Equipment
KO	Coca-Cola	United States	Beverages
FNM	Fannie Mae	United States	Credit Services
INTC	Intel	United States	Semiconductors-Integrated Circuits
JNJ	Johnson & Johnson	United States	Pharmaceuticals
MRK	Merck	United States	Pharmaceuticals
MSFT	Microsoft	United States	Application Software
PFE	Pfizer	United States	Pharmaceuticals
PG	Proctor & Gamble	United States	Consumer Goods

cases, an adjusted closing price was used whereby stock and ADR values were adjusted for dividend payouts and stock splits.

Statistical analyses

Returns for all portfolio components were calculated using the following formula:

$$R_t = [V_{t+1} - V_t + D_t]/V_t \qquad (1)$$

where R_t is the security return at time t, V_{t+1} is the security value at the end of the holding period, and D_t represents dividend payouts during the period t. Returns were calculated weekly for three different timeframes – the previous 3-years, 5-years, and 10-years ending on July 31, 2005. Each security was weighted equally within their portfolios to determine overall weekly returns. Additionally, we evaluated portfolio returns adjusting for risk using the Jensen's Portfolio Technique. This tool appraises asset portfolios based on their relative and absolute performances and provides a measure of excess returns. Risk adjusted excess returns are represented as follows:

$$E(R_i - R_f) = \alpha_i + \beta_i[E(R_m - R_f)] + \varepsilon_i \qquad (2)$$

where R_m is the period return of a market proxy and R_f is the period risk-free rate. Different market proxies were utilized to simulate average returns for each portfolio. The S&P500 was employed as a benchmark for firms in North America, representing nearly 80% of the total U.S. market capitalization. The Asian market proxy was the Nikkei 225 and the European market proxy was the FTSE 300, also representing significant market capitalization of exchanges in their regions. Comparative risk-free rates for each portfolio follow the market proxy selections. The North American rate was determined by the 3-month U.S. Treasury yield, the Asian rate by the Bank of Japan's 3-month Short Term rate, and the European rate by the Bank of England's 3-month Treasury Sterling yields. The data sets were extracted from FRED® of the St. Louis Federal Reserve Bank's as well as the Bank of Japan's and the Bank of England's Internet websites.

Results

The regression results of each of the three portfolios for the three-, five-, and ten-year time horizons are presented in Tables III–V. The significance of the intercept in each regression model (the value for Jensen's alpha) is used to measure *excess* returns for a portfolio for a particular time horizon. The returns were calculated on a weekly basis, and then annualized to show the percentage increase/decrease in the price of the stocks as a collective. If the alpha value is positive and significant, the portfolio's financial performance is superior to the overall stock market for that region on a risk-adjusted basis. If the

TABLE III

Regression results 3-year time horizon

Region	Jensen's α (Weekly %)	Excess return (Annualized %)	r^2	t	p
Asia	0.215	11.17	0.40	1.139	0.26
Europe	0.344	17.87	0.52	2.338	**0.02★**
USA	0.080	−4.14	0.80	−1.074	0.29

★Significant at $p \leq 0.05$

TABLE IV

Regression results 5-year time horizon

Region	Jensen's α (Weekly %)	Excess return (Annualized %)	r^2	t	p
Asia	0.083	4.29	0.41	0.482	0.63
Europe	0.160	8.34	0.55	1.250	0.21
USA	0.055	2.87	0.78	0.833	0.41

TABLE V

Regression results 10-year time horizon

Region	Jensen's α (Weekly %)	Excess return (Annualized %)	r^2	t	p
Asia	0.293	15.25	0.07	1.756	**0.08†**
Europe	0.257	13.39	0.49	2.749	**0.01★**
USA	0.167	8.7	0.77	3.074	**0.00★**

★Significant at $p \leq 0.05$
†Significant at $p \leq 0.10$

alpha value is negative and significant, the portfolio underperformed the regional market for that particular time period. If the alpha value is not significant, the portfolio is deemed to have performed similarly to the market after adjusting for risk.

The alphas of the three regional portfolios were first determined for the most recent 3-year period (2002–2005) to gauge their short-term financial performance. Regression results show that the 3-year excess returns are positive and statistically significant only for the European subset of socially responsible firms. The Asian portfolio is positive but not significant and the U.S. portfolio is negative but not significant at the 95% confidence level. These findings suggest that European firms did enjoy financial (stock price) performance that was superior to other European firms on a risk-adjusted basis while the Asian and U.S. firms performed similarly to their respective markets. These results also suggest possible geographic differences in how well socially responsible firms are rewarded by investors across short-term investment horizons.

The regression results for the most recent 5-year period (2000–2005) examined the intermediate-term performance of each portfolio. While none of the alphas was significantly different from zero, all three were positive. It is possible that investors were less likely to reward socially conscious firms during economic downturns like the global disruption that occurred during 2000–2002. However, the long-term investment horizon of 10-years (1995–2005) produced alpha coefficients for the U.S. and European portfolios that are significant and positive at the 95% level, revealing superior long-term financial performance by socially responsible firms. The alpha coefficient for the Asian portfolio was positive but not significant at the 95% level. However, a post-hoc examination showed significance for the Asian portfolio at a 90% confidence level.

Discussion and conclusions

Summary of findings and interpretation

This global study examined corporate social responsibility through a comparison of socially responsible investments to the broader stock markets in the United States, Europe, and Asia. The ten or more firms selected for each portfolio were determined by review of the largest socially responsible mutual funds in the world. Using Jensen's Alpha, results show that only the European fund outperformed the larger equity market in the short term (i.e., 3 years). None of these statistics was significant in the medium term (i.e., 5 years); however, both the United States and European portfolios outperformed their comparison markets in the long term (i.e., 10 years). Of interest is the finding that the Asian portfolio was close to significance in this same period, suggesting possible movement in the direction of their western counterparts.

While no formal hypotheses about possible causation were posited in advance, our *post hoc* interpretation is grounded in the possible influence of national culture on socially responsible investing. Sirmon and Lane (2004, p. 309) define this construct as "deeply set values that are common to members of a nation." Further, they contend that national culture influences attitudes that are relevant to professional activities, which may be taken to include financial decision making and investing. Several diverse ways exist to characterize cultural differences, and Thomas and Au (2002) present two dimensions that distill down to vertical collectivism and horizontal individualism. The former describes a cultural paradigm that accepts inequality among members while quietly enduring differences in status for the collective. The former views the individual as an independent and autonomous agent, emphasizing equity and personal freedom.

The Asian countries represented by the most socially responsible firms are best characterized by the rubric vertical collectivism. As a consequence, their investor communities may be less likely to believe that it is appropriate to pass judgment on the motivations or actions of senior corporate executives, especially if they are considered high-ranking members of their societies. Additionally, making personal ethics or individual morality public may appear unseemly if these mores place one outside the mainstream of society. Finally, socially responsible investing that advocates for or against firms or their managers may be inappropriate if it brings unwanted attention. Of course, powerful cultural influences are subject to change, and globalization may be causing the shift in acceptability that resulted in nearly significant long-term results.

On the other hand, the United States and the European countries represented in this study are best characterized by horizontal individualism. Thus, their possible impact on socially responsible investing may be very different than Asian investors. For example, status differences may play a lesser role since western cultures are more focused on equality, producing less tolerance for indiscretions by the corporate elite. Furthermore, the emphasis on individuality and autonomy brings with it expectations of personal responsibility within societies that are comfortable demanding accountability for private actions. The finding that European investors also value socially responsible actions in the short term may stem from their long history and the large role that activism and social consciousness assume within the social fabric of nations in their region.

Taken together, these results suggest that being viewed as socially responsible by investors may impact positively the valuation of firms over the long run, providing them with the opportunity to ''do well while doing good'' (see Shank et al., 2005). However, most global enterprises are unable or unwilling to make the commitment necessary to meet or exceed the rigid standards required of the companies selected for this study. A fatalistic way for managers to approach this dilemma is to ignore corporate social responsibility in favor of egoistic opportunities that may maximize profits in the short run and appeal to more selfish investors. An alternative approach is for management to specialize or focus their CSR in ways that are consonant with their reputations or brand images. Evidence by Becker-Olson et al. (2006) corroborates this strategic thrust.

Final remarks

This study represents one of the few examinations of SRI that demonstrated the long-term positive consequences of CSR on the market value of firms (see Shank et al., 2005 for another example). The primary difference between our empirical work and others within the financial and ethics literatures is the use of composites containing firms that meet several externally-recognized ethical standards. As a result, they may appeal to and be recognized by a wider subgroup of investors with a diverse set of expectations (Hill et al., 2003). The more novel conclusion is that European investors appear to value CSR in the sort-term as well as the long-term, and Asian investors may be trending to mirror U.S. investors. If these findings remain robust under additional scrutiny, the value of CSR activities to global enterprises may continue to grow in importance.

Of course, this new way of analyzing socially responsible investing requires additional research before definitive conclusions can be attained. For instance, tracking these portfolios over time to look for possible trends and their causes as well as their historical performance relative to indigenous stock markets is a natural next step. Further, the development and testing of other portfolios that are tied to as wide a variety of cultural distinctions as possible would represent a theoretical expansion of these findings, especially if the statistical techniques utilized allowed for cross-cultural comparisons. Finally, an investigation that considers the relevance of various aspects of socially responsible corporate behavior on investment strategies and tactics within and across nation states and regional boundaries may provide useful insights.

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