

## 1. Introduction

Corporate Social Responsibility (CSR) has globally been recognized as one of the core concepts in corporate management since 1980s, when cross-border businesses were accelerated in economic and financial liberalization. CSR relates to broad business activities and processes, however, expected gains from CSR are, in general, uncertain and ambiguous to get consensus. Further, business organizations bear significant costs for CSR practices in a short run, even if responsible behavior in the society is the central issue for corporations to tackle in a long-term viewpoint. Strategic responses of business organizations to their stakeholders vary from firm to firm, or industry to industry, so corporate social performance is not uniform but multi-dimensional.

Therefore, in this study, we apply the stakeholder management approach to CSP, focusing on the role of investors as a driver of CSR. The purpose of this study is to investigate the relationship between corporate ownership and CSP of Japanese business firms in the late 2000s, when the ownership structure had changed significantly. Foreign investors became major players in the stock market, while cross-shareholdings among business corporations and financial intermediaries were resolved gradually. In addition, some domestic institutional investors began to voice against management of their investees in the prolonged stagnant economy. Thus, in these changing surroundings, Japanese firms began to review their attitudes for shareholders as well as their relationship with other stakeholders.

This study sheds lights on influences of foreign investors to CSP aspects of Japanese firms, comparing with those of domestic relationship investors or corporate investors in the late 2000s. The features of this study are as follows. First, we try to explicitly separate foreign investors' preference bias to high CSP firms from their influence on CSP of investee companies. Second, we use CSP comprehensive index and five dimensional indices of stakeholders' perspective, both of which we originally calculated based on questionnaire results of CSR Database of Toyo Keizai Inc.

The rest of the paper will proceed as follows: Section 2 surveys background and preceding studies. Section 3 presents research objective and introduces hypotheses to examine. Section 4 explains our data and estimation method, and Section 5 reports

empirical results and basic observations. Finally, in Section 6 we introduce implications for CSR practices of Japanese firms in international perspective and the role of different investor groups, and give discussion points for future research development. Our empirical results suggest that foreign investors might have played a key role as CSR driver and have influenced stakeholder management of Japanese firms in the late 2000s.

## **2. Ownership Structure and Investors' Behavior in Japan**

### **2.1. Definition of CSR and Stakeholders**

Though the discussions on the definition of the concept of CSR have a long and wide-ranging history, there has been no strong consensus on it yet.

The concept of CSR has long been discussed in business and society field of academia (Carroll 1979; Wood, 2000; Windsor 2006; McWilliams, Siegel and Wright, 2006). On the other hand, many empirical studies have been conducted on relationship between corporate social performance (CSP) and corporate financial performance (CFP) since 1970s (Cochran and Wood, 1984; McGuire, Sundgren and Schneeweis, 1988; Waddock and Graves, 1997; McGuire and Siegel, 2000 and 2001). The definitions of CSR range from the narrow aspects of stakeholder management to the broad aspect of social issue management.

The definition of CSR is still embryonic and ambiguous in both academic analyses and business practices, but *researchers are moving beyond just defining and identifying CSR activities to strategic role of CSR in organizations* (McWilliam et al. 2006, p.2). Many researchers have been interested in financial aspect of CSR and incentives for responsible activities of business in society. Some researches apply governance framework on CSR practices and analyze relationship between CSR activities and financial performance.

Empirical research on relations between CFP and CSP in governance framework gives business organization practical implication for *how firms' roles in society take place in the interaction with their stakeholders* (de Graaf and Stoelhorst, 2009, p.5).

Thus, *the comprehensiveness of CSP becomes problematic in assessing the relationship between CSP and CFP, because some aspects of CSP might aid financial performance whereas other aspects of CSP might hurt it* (Cox and Schneider, 2010, p.255). In the

meantime, disaggregating the dimensions of CSP in relationship management with stakeholders may develop sustainable sources of competitive advantage (Hillman and Keim, 2001)

Various models for stakeholder behavior are proposed to explain the relationship between CSP and CFP. With observations and theoretical discussion, consumers might be expected to be a driver of CSR, *supporting pro-social corporate products and punishing corporations that fail social responsibility* (Smith, 2008). Schuler and Cording(2006) theoretically examine the role of information intensity and moral values in linking CSP with consumers' purchase behavior.

Deakin and Hobbs (2007) present a model of CSR as a set of mechanisms for aligning corporate behavior with the interests of society in reducing externalities and promoting a sustainable corporate sector, including voluntary action beyond compliance with the aim of enhancing competitiveness. The financial perspective of this model is concerned with managerial incentives to align CSR strategies in the financial market and to promote shareholder engagement on internal issues related to employment and safety. To devote corporate resources to constituencies such as employees, customers, suppliers, and local communities can help to create shareholder value (Brickley et al., 2003). In the context, long-term institutional investors such as pension funds and insurance companies are expected to play a crucial role as a key driver of CSR.

## **2.2. Long-term Investors and CSP in Preceding Studies**

Institutionalization of investment is a recent trend commonly observed in the developed economies. On the relationship between institutional shareholding and CSP, abundant empirical studies have presented since 1990s, following a pioneer work by Cochran and Wood (1984). Many of the results suggest positive relation between institutional shareholdings and CSP (Waddock and Graves, 1997; Johnson and Greening, 1999; Hillman and Keim, 2001).

Investment time horizon and aim differ among types of institutional investors. Social investors generally have long-term perspective, though the aim of investment is various. They includes value-based investors who act in accordance with deeply held ethical view, value-seeking investors who use social and environmental data to enhance

portfolio performance, value-enhancing investors who use shareholder activism techniques to enhance investment value focusing primarily on corporate governance, and investors targeting some specific concerns (Kurtz, 2008). Socially responsible investment (SRI) movement in the USA in the 1970s and the 1980s were religious value-based and social-political value-based. Recent global institutional investors who concern with CSP seem to be value-seeking or value-enhanced rather than value-based.

Decision making of long-term institutional investors such as pension funds is actually subject to regulatory constraints and they are also under pressure from their customers. Pension funds in the UK were requested to disclose their policy for social responsible investment by the 2000 revision of Pension Funds Act within their formal Statement of Investment Principles. Under the regulation, SRI has been broadly spread among the institutional investors in the UK, and CSR influenced decision making of pension investors in the European region. On the other hand, pension funds and mutual funds have been confronted with increasing demand for financial gain from their customers in the demographic aging society. Association between CSP and CFP is gaining growing interest in long-term asset management in the developed countries.

Cox et al. (2004) investigated the pattern of institutional shareholding and its relationship with socially responsible behavior by large UK companies in 2001-2002. Their results suggest that shareholding by long-term institutional investors or pension funds is positively related to CSP. With the same data set, Cox et al. (2008) examined the relationship between multidimensional CSP and pension ownership, and found that the UK pension funds prefer employee-aspects of CSP. Cox and Schneider (2010) compared preference of CSP of the US domiciled and the UK domiciled pension plans in the UK stock market. They found that the UK pension plans have a positive relationship with workplace practice or environment, while the US pension plans stress CFP. These results imply that regulatory framework of institutional investment is a determinant in driving CSR activities.

Neubaum and Zahra (2006) throw light on the influence of shareholders' activism and coordination on executives' support of CSP. They found that active behavior of institutional investors had positive association with CSP, using Fortune 500 firm-data of 1995 and 2000. Their results suggest that the long-term shareholdings may foster relational exchange between shareholders and corporate executives on enhancing CSP.

Based on organizational architecture of corporations, they imply coordination among stakeholders reduces conflicts with executives and might enhance corporate value.

### **2.3. Foreign Ownership and Domestic Investors in Japan**

Conventionally, the stock ownership of Japanese companies is characterized as insider holdings or cross-holdings among corporations based on long-term business relationship. This feature of ownership structure has changed since the Bubble Economy Burst in the late 1980s. In contrast to declining of cross-shareholding, institutional investors and foreign investors has emerged as major shareholders of the Japanese firms since the 1990s, when globalization of business and financial liberalization advanced in step with world-wide growth of capital flow and cross-border diversification of portfolio investments.

Table 1 shows the stock ownership at market value during the period from 1985 to 2010, whose data source is stock ownership survey by Tokyo Stock Exchange. Stockholding by foreigners (foreign domiciled) was 4.7% in 1990, rose to 18.8% in 2000, and peaked at 28% in 2006. Domestic corporate shareholding reduced from 60.2% to 49.9% during the period between 2000-2010. Among shares owned by domestic corporations, shareholding by trust banks, consisting with investment trust accounts and pension fund accounts, kept around 18%, while shareholding by commercial banks, insurance companies and business companies, reduced from 42.8% to 31.7%. Thus, relationship investment by corporations and financial institutions except trust banks might be still large part of ownership of Japanese listed companies even at the end of 2000s. Shareholding by individuals, which include various types of direct holdings by individual investors, was about 20% through the 2000s.

[Table 1 about here]

Since the early 2000s, governance by institutional shareholders has gradually been recognized among domestic long-term institutional investors. In 2001, Pension Fund Association (PFA) began to disclose their policy for voting as shareholders and they

actually began to execute voting rights on stocks of its in-house portfolio management. On the other hand, fund managers of pension funds have increasingly been exposed to strong pressures from their customers to demand high performance in the rapidly demographic aging society.

In general, institutional investors often have behavioral bias under pressures from their customers or regulatory authority, and their behavior also might be biased due to incentive system of organization they belong to (Scharfstein and Stein, 1990; Sias, 2004; Hansen and Hill, 1991). Suto and Toshino (2005) examined behavioral biases of fund managers of Japanese institutional investors based on the 2003 survey data. According to their results, fund managers reveal short-term or myopic bias, herding, and self-marketing to improve appearance of portfolio performance, under strong pressures from their customers to demand short-term and high financial performance. It is also suggested that in relationship between sponsor companies of pension funds and fund management companies or Keiretsu financial group, fund managers could conspicuously be weak to the pressures from customers.

These biases of long-term investors would contradict to their role as monitors for corporate value, in other words, they would hurt corporate governance mechanism of shareholders. Japanese institutional investors in the early 2000s at least were remarkably sensitive to their customers' expectation and reputation and their behavior was biased.<sup>1</sup>

## **2.4. Preference of Foreign Investors**

Given the growing cross-border portfolio investment, many researchers have concerned with behavior of foreign investors and examined their preference. According to previous studies, foreign investors are inclined to invest more in large and esteemed firms, less in poorly governed firms. Thus, they generally have home-country bias in selecting investee companies due to information asymmetry relative to local investors (Choe, Koh, and Stulz, 2005; Leuz et al., 2009).

---

<sup>1</sup> Suto, Menkhoff, L. and Beckmann (2005) compare the results of the same form of surveys in Japan, Germany and the U.S. Their finding is that Japanese fund managers reveal more strongly biased behavior than both German and the U.S. fund managers in terms of short-time bias and herding.

As to the US investors, they reveal strong preference on disclosure and transparency, avoiding insider system, peculiar relationship, weakness of stockholder protection (Kang and Stulz, 1997; Kho, Starks and Warnock, 2006; Aggarwal, Klapper and Wysocki, 2005; Leuz et al.2009). Institutional investors generally prefer firms with low transaction costs or high liquidity in the market (Gompers and Metric, 2001). In the context, foreign investors might prefer large-scale, with global popularity, and high credit-ranked firms in the Japanese stock market.

In response to globalization of shareholdings and transactions in the stock market in the 2000s, corporate governance to shareholders' value maximization began to be recognized slowly. In 2006, Tokyo Stock Exchange started to require listed companies to disclose Corporate Governance Report. In 2007, Financial Instruments and Exchange Act passed and became effective in April 2008. A company, which is required to submit Annual Securities Reports to Ministry of Finance, also has to submit Internal Control Reports simultaneously. On the side of corporate sector, large and international companies have strengthened investors' relation (IR) and most of them have voluntarily issued CSR reports.

However, from global viewpoint, disclosure and transparency of Japanese firms are still significantly insufficient even at the end of the 2000s (OECD, 2010; ACGN 2008). Further, Japanese pension funds should be more concerned with nonfinancial disclosure to improve long-term performance (OECD, 2010). Using data of the Japanese firms in 1991-2008, Miyajima and Nitta (2011) examined relationship and causality between shareholding and features of governance related variable, and found that membership structure of board of directors for shareholders' interest is a determinant of foreign ownership. The results suggest that foreign investors gave premium for the firms with more independent directors in the board. Thus, foreign investors not only had home country bias and preferred good corporate governance in investing in the Japanese stocks, but also influenced on improvement of corporate performance of investee companies.

## 2.5. SRI Market in Japan

Traditional Japanese corporations are distinguished by ethical self-disciplines or CSR policy in succession.<sup>2</sup> Some key concepts of CSR such as quality of products, social contributions and securing employment in the community are rather familiar to traditional Japanese corporate management in order to survive for a long time. Nevertheless, SRI market in Japan is extremely small in comparison with the scale of the economy in Japan.<sup>3</sup> Based on 2009 estimation, 90% of SRI is investment trust funds for individuals, so that only 10% is due to long-term institutional investment. Japanese institutional investors are still very skeptical about SRI in terms of investment policy and performance.<sup>4</sup> Their concern is financial performance rather than social performance under strong pressure to demand high investment performance. Further, investment funds for individuals have been biased toward environmental aspect of CSR. Long-term institutional investors such as pension funds have been reluctant to implement investment strategy based on CSP.

In the above situation, foreign investors which have global viewpoint of CSR might have played a key role to give pressure to improve social responsible practices related ESG (Environmental, Social, and Governance) and to increase corporate social performances of the Japanese corporations.

## 3. Research Objective and Hypotheses

### 3.1. CSP Attributes

---

<sup>2</sup> The most well-known policy is the coordination of interests of three stakeholders: suppliers, buyers and community or society; Sanpou-yoshi (business should be run for three-stakeholder-benefits). Common principle of policies of major long-life companies is to establish trust based on relationship in the society as well as in transactions by self-disciplines.

<sup>3</sup> According to SIF-J estimation, market value of SRI peaked about 850 billion Japanese Yen at the end of 2007, but reduced to 579 billion JPY by the shrinking of the market. On 2007, European SRI amounted to 2.7 trillion Euro and that of the U.S. amounted to \$2.7 trillion. (Japan Social Investment Forum, *Annual Report*, 2009).

<sup>4</sup> Based on questionnaire survey for pension plans (465 from 1432 organizations; valid response rate 32.5%), only 32 respondents have already adopted SRI as of 2008 (*Study Report for SRI and PRI*, Research Institute for Policies on Pension and Aging, 2008).



Reviewing preceding studies and argument on CSR attributes, we find a consensus that different types of corporate social activities have different implications for financial performance (Cox et al., 2009, p.29). There are broad possibilities of linkage between CSP and CFP, in terms of risk management, reputation management, cost-saving, and enhancing motivation of employees. Thus, different types of investors may concern with different aspects of corporate activities. In discussing linkage between CSP and CFP, there is wide variety and ambiguity of CSP attributes although CFP are relatively clear variable.

From a viewpoint of stakeholder approach for corporate governance, corporate responsible activities can be linked to different stakeholder relations (employees, communities, customers, suppliers, the environment) and firms are required to choose appropriate architecture of internal governance and adopt strategies in the regulatory framework. With these stakeholder relationships, we define the following five attributes of corporate social performance: 1) employee relations, 2) social contributions, 3) security for organization and product safety (quality of product), 4) internal governance and risk management, and 5) environmental preservations.

The first attribute, employee relations, which includes working conditions within the organization, can contribute to enhance employee quality and motivation (Turban and Greening, 1997). Proper working hours and salary, employment of minorities, stable employment, safe circumstance, as well as enlightenment and development of abilities should be concerned.

The second attribute, social contribution, is related to firms' policy for and response to social demands. Good relationships and coordination with the community and society, where they operate, can reduce cost of conflicts, attract good human resources and enhance reputation. On the other hand, inappropriate adherence to the community might narrow business perspective and increase costs and risk of business operation.

The third attribute, firm security and product safety, is related to quality of products and sustainability of business. Therefore, it is a competitive edge of corporate management in a long-term viewpoint. The fourth attribute, internal governance and risk management, is related to the concept of quality of disclosure, compliance, internal auditing and self-disciplining. The fifth attribute, environmental preservation, is a pillar of CSR in the ongoing change of global climate, and one may think that this is the most

required responsibility for firms to fulfill. As a result, we define comprehensive or Composite CSP as integration of the above five attributes.

### **3.2. Hypotheses Development**

In light of the above discussion, we develop hypotheses to examine the relationship between the foreign ownership and CSP of the Japanese listed firms in the late 2000s, when corporate ownership structure changed rapidly. Considering simultaneous determination of CSP and the structure of shareholdings, we try to distinguish foreign investors' preference for high CSP companies from their influence on improvement of CSP of the companies they invest in. Three groups of ownership are classified based on distance from their investees; domestic corporate ownership, foreign corporate ownership, and individual ownership. Corporate ownership includes both shareholdings of business companies and financial institutions. Thus, domestic corporate ownership is rather relationship-shareholding or insider-ownership in broad. On the other hand, foreign ownership (foreign domiciled) is independent or outsider-shareholding. Foreign corporate investors might prefer established companies due to information asymmetry. Corporate investors, both domestic and foreign, are inclined to prefer large-scale and matured companies, though each reason could differ.

Individual ownership reflects decision-making of various individual investors, such as small individuals, family-owners and so on. In this study, we focus on corporate investor groups, making clear-cut preference for and influences on CSP of listed companies between domestic investors and foreign investors. We propose following hypotheses on association between CSP, in terms of comprehensive and dimensional, and ownership structure of the Japanese listed companies. Concerning dimensional CSP indices in general, foreign investors might place a higher value on each of CSP dimensions than domestic investors. Domestic corporate investors might have stronger interest in CSP-employment in Japanese insider-system of corporate management. Internal governance index might be less interesting to investors in the observed period, as internal control report was legally required for all listed corporations from 2008 and they responded to it in formal way of compliance. We examine the association of

ownership structure with Composite CSP and CSR dimensions, and the influences of changes in ownership on CSR achievement.

Hypothesis 1: *There is a positive relationship between corporate ownership and Composite CSP achievement because they prefer matured companies.*

Hypothesis 2: *The relationship between foreign ownership and Composite CSP is more positive than that between domestic corporate ownership and composite CSP.*

Hypothesis 3: *There is a positive relationship between growing foreign ownership and Composite CSP because foreign investors have influence on investee companies to improve their CSP.*

Hypothesis 4: *The relationship between growing foreign ownership and CSP is more positive than that of growing domestic ownership and CSP.*

Hypothesis 5: *The relationship between CSP dimensions and ownership structure differ in that various types of investors have various preferences for CSP practices.*

Hypothesis 6: *The relationship between CSP dimensions and change in corporate ownership structure differ in that various types of investors have various influences on CSP practices.*

## **4. Data Construction Method and Estimation**

### **4.1. Construction of CSP Indices**

We constructed our CSP indices, using the Corporate Social Responsibility Database which was provided by Toyo Keizai Inc. as a primary data source. The original database consists of three parts: (Part I) Employment, (Part II) Overall survey for CSR, and (Part III) Environment. We further subdivided the overall survey section (Part II) into three CSP attributes. They are ‘social contributions’, ‘security and product safety’, and

‘internal governance and risk management’. For each of these five CSP attributes, we constructed a CSP Index based on principal component analysis, and obtained a rating of the firms named EMP (employment), SC (social contributions), SS (security and product safety), IG (internal governance and risk management) and ENV (environment).

Among these dimensional attributes of CSP, EMP includes the ratio of female employees, the ratio of workers over 60 years old, job leaving rates, and job accident ratios. SC includes the CSR section and volunteer activities. For SS, the section to handle safeness of goods and services, apparatus for internal claims and the attainment ratio of ISO 9000s inside the firm are included. For IG, the law abidance section, it includes the CIO position and firm performance in security measures. ENV, the environmental section, includes environmental accounting and the number of ‘ECO-labels’ attached with their products.

Before conducting principal component analysis to compute five CSP dimensional indices described above, each year we first converted quantitative data such as a fraction of female employees to three or four level categorical data. Second, we make within sector adjustment since some question items have very different meanings among sectors. The seven sectors used in this study shown in Table A1 are the ones defined in Kubota and Takehara (2007) that set store on the distance between firms and final consumers. Finally, we obtained CSP dimensional index defined as first principal component.<sup>5</sup> Each index is demeaned and scaled by its standard deviation so that it approximately obeys a standard normal distribution.

The comprehensive CSP index is computed based on five dimensional indices. Let  $r(\cdot)$  denotes the function that gives a rank of the element of vector in ascending order and  $n$  denotes the number of firms in each year. Then, the comprehensive measure of CSP is defined as follows:

$$CSP = \frac{r(r(EMP) + r(SC) + r(SS) + r(IG) + r(ENV)) - 1}{n - 1} \times 6 - 3 \quad (1)$$

It is convenient for researchers if the scale of the comprehensive CSP measure is comparable to those of CSP dimensional indices. Since our CSP dimensional indices

---

<sup>5</sup> The detail of the construction of CSP dimensional indices is described in Suto and Takehara (2012).

approximately obey the standard normal distribution, equation (1) makes an adjustment by which the comprehensive measure of CSP is uniformly distributed and falls in the closed interval  $[-3,3]$ .

## **4.2. Descriptive Statistics of CSP and Firm Characteristics**

We constructed the CSP Dimensional Index Database from 2007 through 2010, which includes all the listed firms in Japan which answered to the questionnaire survey by Toyo Keizai Inc. Since Toyo Keizai Inc. sends a questionnaire sheets to the firms in the beginning of July and the firms sent back their answers by the end of September, in this study we use the most recent financial statement data and market attributed data which were available at the end of September. The primary source for financial statement data is NIKKEI NEEDS Database and that for market attributed data including market value of equity and stock return is NIKKEI Portfolio Master Database.

Before examining the hypothesis 1 thorough 6 described in the previous section, we have to compute the percentage shares owned by domestic corporations, foreign corporations, and individuals. Japanese firms are required to disclose the brief summary of their stock ownership structure in the financial report: the number of shares owned by foreign corporations and the number of shares owned by individuals are available from these financial reports. The number of shares owned by domestic corporations in this study is defined as the sum of shares owned by financial institutions and the number of shares owned by other corporations, in which we explicitly excludes shares owned by financial products dealers, governments, and public organizations.

To investigate the behavior of the stakeholders associated with CSP, it is necessary to compute the firms' characteristics in addition to the stock ownership structure. We use the following eight variables in this study. First of all, as is pointed out in many previous studies, firm's CSP is positively related to its size. We use natural logarithm of total asset value (in million JPY),  $\ln TA$ , as a measure of size. Since the relationships between CSPs and size are not linear, in the regression analysis whose results will be reported in the latter part of this paper, we also introduce the five size dummy variables, from Size1 to Size5. Subsequent three variables are the proxy for profitability, credit risk and

growth of the firm. They are Return On Asset (ROA), Debt Ratio (DR), and Growth rate in Total Asset (GTA). As a measure of liquidity and variability of the firm, we use monthly turnover rate (Turn) and past 3 year volatility of monthly stock returns (Vol3Y), respectively. Book-to-Price Ratio (BPR) is a variable to control the difference in firm's style, i.e. value and growth. A lower book-to price ratio implies that investors expect managers to create more values thorough the operation of the firm.

Finally, we introduce a Foreign Dependency Ratio (FDR) defined as sales in foreign countries divided by total sales.

Number of firms each year and in each sector is reported in Table 2. The number of firms at minimum is 894 in 2007 and that at maximum is 975 in 2010. About 60 percent of the firms are listed in the Tokyo Stock Exchange (TSE) first section, however, about 10 percent of the firms are listed in the TSE second section and about 30 percent of the firms are listed in other exchanges except TSE. Services industry have high proportion at 37 percent of the sample firms, however, only half of them are listed in the TSE.

[Table 2 about here]

At the end of September of each year, we constructed sector portfolios or size-ranked equal-weighted portfolios, and Table 3 reports the descriptive statistics of CSP by sector (Panel A) and by firm's size (Panel B). Median and mean of CSP (comprehensive measure of CSP) is the highest in consumption goods sector. Medians of EMP (employee relations), SS (security and safeness) and IG (internal governance and risk management) are the highest in investment goods sector. On the other hand, median values of SC (social contribution) and ENV (environment preservations) are the highest in utility sector. In panel B, we can observe the pronounced positive relationship between the firm size measured by total asset and firms' CSP.

Descriptive statistics of stock ownership structure of sample firms are shown in the Table 4. There is no much difference in shares owned by domestic corporations across the sectors and across firms' size. In sharp contrast, there's a large difference in shares owned by foreign corporations. Foreign corporations tend to own large and medium sized stocks and do not invest a lot in the firms in service sectors whose CSPs are relatively low.

[Table 3 about here]

[Table 4 about here]

### **4.3. Correlation among the Variable and Regression Model**

Panel A of Table 5 reports the correlations between the CSP and ownership structure, while Panel B of Table 5 shows the correlations between the CSP and eight firm characteristic variables. In both panels, Spearman rank correlations and their corresponding probability values are shown. The results shown in this table should be examined carefully because by these results we can verify the research hypotheses we have raised.

In panel A, the correlation between comprehensive CSP and %shares owned by Japanese corporations is 0.269 and correlation between comprehensive CSP and %shares owned by foreign corporations is 0.533. Both of them are positive and significant at 1% level and this finding supports our Hypothesis 1. Since the correlation is much higher for foreign corporations, it also supports our Hypothesis 2. The correlation between comprehensive CSP and the past 5 year increase in shares owned by foreign corporations is 0.217 and significant at 1% level which supports our Hypothesis 3. Contrary to the positive correlation between CSP and increase in %shares owned by foreign corporations, correlation between CSP and increase in %shares owned by Japanese corporations is negative at -0.155. This observation does not contradict to our hypothesis 4. Finally, there exists a large dispersion in the magnitudes of the correlation between CSP dimensional indices and ownership structure variables, and this observation supports our Hypothesis 5 and 6. Overall, we can find no evidence against our Hypotheses 1 to 6 in Panel A of Table 5.

Next in Panel B, we confirmed the relationship between firms' characteristics and CSP indices. The correlations between comprehensive CSP measure and characteristics variables are statistically significant at 1% level in most cases. The exceptions are between CSP and debt ratio (DR) and between CSP and growth rate of assets (GTA). As

already confirmed in Table 3, there exists very strong and positive relationships between CSP indices and size (lnTA). Furthermore, CSP indices are higher in firms which are more liquid and less variable.

[Table 5 about here]

These very high correlations we just observed between CSP indices and characteristics variables raise a suspicion that those findings in Panel A which support our hypotheses 1 through 6 are illusive. To clear up this kind of doubts, we conducted regression analysis by using the characteristic variables as control variables. To check the robustness of our finding after controlling the firms' characteristics, we employed the following regression model:

$$y_j = \alpha + \beta x_j + \sum_{i=1}^7 \gamma_i CV_{i,j} + \sum_{i=2}^5 \delta_i DSize_{i,j} + \sum_{i=2}^6 \lambda_i DSector_{i,j} + \varepsilon_j. \quad (2)$$

In model (2),  $y_i$  is comprehensive CSP measure or one of five CSP dimensional indices. Independent variable  $x_j$  is one of the %shares owned by Japanese corporations, %shares owned by foreign corporations, %shares owned by individuals, %increase in shares owned by Japanese corporations, %increase in shares owned by foreign corporations, or %increase in shares owned by individuals.  $CV_{i,j}$  are the set of control variables consisting of ROA, DR, GTA, Turn, Vol3Y, BPR and FDR.  $DSize_{i,j}$  is a size dummy variable which is equal to 1 if the sample  $j$  belongs to the  $i$ -th size quintile and otherwise equal to 0.  $DSector_{i,j}$  is a sector dummy variable if the sample  $j$  belongs to the  $i$ -th sector and otherwise 0.

Before conducting the regression analysis, we excluded upper and lower 2.5 % samples as outliers. As a result, the number of firm-samples we used in the following regression analysis is 3,536.

#### 4.4. Estimation Results



Table 6 reports the regression results of different types of ownership of all sample firms on both Composite CSP and five attribute indices with a set of control variables. Concerning the association among different types of ownership in companies and Composite CSR, the results substantially support Hypothesis 1 that corporate ownership, both domestic and foreign, has a positive relationship with comprehensive corporate social performance ( $p$ -value $<0.05$ ), while individual ownership has significantly negative relationship. Estimated coefficient of CSP of foreign ownership is larger than that of domestic corporate ownership, so Hypothesis 2 is also supported. Corporate investors seemingly prefer large scale and matured companies which have had relatively high reputation in the society.

[Table 6 about here]

Table 7 indicates similar regression results of changes in ownership on Composite CSP and five attribute indices. It shows that growing foreign ownership has a positive relationship with Composite CSP so that this fact substantially supports for Hypothesis 3. With sharp contrast, we have interesting results that growing domestic ownership has a negative relationship with Composite CSP. Thus, it can be interpreted that domestic corporate investors, as a whole, are interested in non-social aspects of corporate performance. On the other hand, foreign investors are interested in social corporate performance as well as financial performance, and they contribute to the improvement of CSR practices of investee companies. According to the results, hypothesis 4 is also supported.

[Table 7 about here]

With regard to firm characteristics, Composite CSP has negative relationships with debt ratio, growth rate, stock volatility and BPR, however, ROA has no significant relationship in Table 6. High CSP companies are generally featured to be less dependent on debts, and are rather matured with lower growth, less risk, therefore relatively low market prices. Foreign dependency ratio has positive relationship with Composite CSP,

though only in the case of PANEL B it is not statistically significant.

In Table 7, debt ratio, and growth rate do not have a significantly positive relationship with CSR indices. On the other hand, both FDR and Turn are significantly positive, and volatility (Vol3Y) is significantly negative in all cases. These results suggest that firms whose business is exposed to international competition are more sensitive to corporate social performance than companies running domestic business, and that stocks of higher CSP companies have higher liquidity and less volatility in the market.

Concerning dimensional CSP, there are some interesting observations. First, in Table 6, ENV and EMP have a significantly positive relationship with both domestic and foreign corporate ownership as well, but the estimated coefficient of EMP of foreigner is much higher than that of domestic. This fact suggests that good employment policy and environment strategies are accepted to be evidences of goodness and maturity of the firms by corporate investors. Further, in Table 7, increase in a foreign ownership has significantly positive relationship with the both indices, while increase in domestic ownership has significantly negative relationship with them. That means that foreign investors might evaluate improvement of employment circumstances and environment strategies of investee companies in Japan.

Second, the similar facts are observed about Social Contribution and Security and Safeness. Thus, foreign investors seem to be more sensitive to these aspects of CSR than domestic investors, and increasing foreign ownership would have influences on improvement of social contribution and safety in business or quality of product. Third, in Table 7, increase in foreign ownership has a significantly positive relationship with IG, though domestic ownership has no significant relationship with it. It is an interesting fact in comparison with the fact that foreign ownership has no significant relationship with IG as Table 6 shows. These results suggest that foreign investors contribute to strengthen investors' self-disciplining or to improve internal governance of investees, though they might not prefer firms based on the level of IG. Fourth, ownership by individual investors has a negative relationship with all CSR Indices but increase in their ownership has a significantly positive relationship with SC and ENV, and a negative one with EMP. These results mean that individual investors might become more and more concerned with social contribution and environmental strategies of business firms.

In summary, Hypothesis 5 and Hypothesis 6 are partially supported. It is interpreted that high CSP firms are large and matured companies which are preferred by corporate investors in general, but foreign investors have influenced the improvement of every dimension of CSR practices, while domestic corporate investors are less concerned with improvement of CSR of investee companies. Individual investors also play the role of CSR driver in the aspects of social contribution and environment protection.

#### **4.5. Industry-wise Regression Results**

The association between CSP and changes in ownership could be different from industry to industry. Finally, we go on to carry out industry-wise tests on three major industry groups in our samples: consumption goods, investment goods, and services. Firms in consumption goods sector might be more sensitive to product safety and social contribution because they directly face consumers' preference and social demand, while those in investment goods sector might be more concerned about environment issues because they generally have more serious influences on circumstances than other sectors. Firms in services industry including retail and wholesale might be remarkably concerned about security and safeness. Here, we focus on influences from changes in ownership structure of each industry.

[Table 8 about here]

Table 8 shows the relationship between CSR indices and changes in ownership according to industry. With composite index in all industry, the increase in domestic corporate ownership has a significantly negative relationship, the increase in foreign ownership has a significantly positive one, and the change in individual ownership has no significant relationship. Results on CSP dimensional indices vary from industry to industry.

For all sectors, the increase in domestic corporate ownership negatively associates with SC and ENV. In contrast, the increase in foreign ownership positively associates with EMP and ENV for all sectors, and also positively associates with SC, though it is not significant for consumption goods sector. On the contrary to our assertion, the

increase in individual ownership has no relationship with all indices in consumption goods sector. However, it has a significant positive relationship with EMP, SS and ENV in investment goods sector and less significant but a positive relationship with SC and ENV in Services Sector. Among these three industries, consumption goods sector has achieved highest corporate social performance except Employee Relations, as shown in Table 3. This may be the reason why individual investors as minority cannot have a significant influence on CSP attributes of investees in the sector.

In sum, domestic corporate investors tend to be negative to evaluate CSP practices in all three sectors at all. There is a sharp contrast with foreign investors who could contribute to the improvement of EMP, ENV and SC for all sectors. It is also interesting that individual investors might contribute to promote three practices: ENV practices in investment goods sector and services sector, SS practices in investment goods sector, and SC practices in services sector. These three attributes are still remarkably weak aspects of CSP in those industries, where major owner groups are domestic corporate investors and individual investors as shown in Table 4.

## **5. Summary and Implications**

This is the first study to investigate influences of stock ownership structure on corporate social performance of Japanese business firms in the late 2000s, emphasizing the role of foreign investors in comparison with those of domestic corporate investors or individual investors. Features of our empirical analysis are two: first, constructing normalized CSP attribute indices and composite index with wide range of questionnaire survey data; second, explicitly separating foreign investors' preference bias for high CSP firms from their influence on CSP of investee companies in Japanese market.

By cross-sectional regressions of ownership structure and its changes on CSP indices controlled by firm characteristics, we found some interesting facts. First, foreign corporate ownership has more positive relationship with comprehensive social performance than that of domestic ownership. Thus, both of them have preference to large-scale and matured firms, which are relatively concerned with CSR, but foreign investors have stronger preference to CSR. Second, the increase of foreign