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DOES ECONOMIC POLICY UNCERTAINTY AFFECT CORPORATE SOCIAL RESPONSIBILITY INVESTMENT? EVIDENCE FROM LISTED COMPANIES IN CHINA

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Abstract: Corporate Social Responsibility (CSR) has become a crucial part of modern business strategies. This paper aims to explore the impact of economic policy uncertainty on corporate CSR activities, and further analyze the role of factors such as firm size, financial leverage, profitability, and growth opportunities in CSR disclosure. Using data from A-share listed companies in China, a multiple regression model was employed for empirical analysis. The results show that economic policy uncertainty has a significant negative impact on CSR activities, indicating that uncertainty in the policy environment reduces firms' CSR investments. Firm size and profitability positively influence CSR activities, suggesting that larger companies and more profitable firms are more likely to engage in CSR. Financial leverage and growth opportunities do not have a significant impact on CSR, reflecting that financial conditions and market opportunities influence CSR decisions less than expected. The inclusion of industry and year fixed effects effectively controls for systemic differences across industries and over time, making the model results more robust. These findings provide valuable insights for firms in formulating CSR strategies and offer theoretical support for policymakers to improve policy environments that encourage corporate social responsibility.
Keywords: Corporate social responsibility (CSR); Economic policy uncertainty; Corporate decision-making; Socio-economic context of china

1 INTRODUCTION

Corporate Social Responsibility (CSR) has become a critical aspect of contemporary business strategy, influencing firms' decision-making processes and organizational outcomes [1]. As societal expectations evolve and stakeholders increasingly demand ethical and sustainable business practices, firms are compelled to integrate CSR into their operations to foster long-term sustainability and competitiveness [2]. By actively engaging in CSR activities, firms not only fulfill their moral obligations to society but also benefit from enhanced stakeholder trust, reputation, and brand loyalty [3]. Moreover, CSR initiatives serve as strategic tools for risk management, helping firms navigate complex regulatory environments, mitigate reputational risks, and prevent potential crises [4]. Importantly, empirical studies demonstrate a positive correlation between CSR performance and financial performance, with firms that prioritize CSR often outperforming their peers in terms of profitability, shareholder value, and long-term sustainability.

In an era of increasing transparency, CSR drives innovation and organizational resilience, enabling firms to adapt to changing societal expectations and emerging market trends. Therefore, the importance of CSR extends beyond traditional motives, playing a central role in strategic decision-making, organizational culture, and long-term value creation in a dynamic business environment [5]. With the establishment of the United Nations' Sustainable Development Goals (SDGs), there has been a global push for firms to integrate CSR into their business activities, transforming it into a universal practice integral to corporate operations.

Recent literature in finance and economics has also extensively explored the impact of policy uncertainty on firm performance and strategic decision-making [6]. Studies increasingly recognize that fluctuations in government regulations, fiscal policies, trade agreements, and geopolitical tensions can significantly affect firms across various industries and regions. Policy uncertainty introduces unpredictability and risk into business operations, influencing firms' investment decisions, capital allocation strategies, and market behavior [7]. Empirical evidence also links policy uncertainty to firms' innovation, capital expenditure, and risk management strategies [8]. Thus, investigating the effects of policy uncertainty on firm behavior and investment has become a focal point of academic research with implications for policymakers, investors, and corporate decision-makers. This study focuses on China, given its economic development potential, to explore how cross-national factors influence CSR activities, particularly in rapidly changing business environments.

2 LITERATURE REVIEW AND RESEARCH HYPOTHESIS

Existing literature suggests that economic uncertainty exacerbates conflicts between managers and shareholders, prompting firms to adopt more conservative investment strategies [9]. This uncertainty arises from frequent changes in government policies, market volatility, and instability in international economic conditions, introducing greater risks into firms' decision-making [10]. Especially for CSR projects, which require sustained financial support and long-term investment, the extended payback period and uncertain returns pose significant challenges [11]. As a result, managers may reduce or delay CSR investments to focus on short-term profit-maximizing projects to mitigate agency costs.

While stakeholders may emphasize CSR during periods of economic uncertainty, particularly in addressing environmental and social responsibilities [12], firms face increased complexity and uncertainty in complying with evolving regulations. This not only requires significant resources but also demands flexibility to adapt to rapidly changing legal frameworks [13]. Consequently, firms may deprioritize CSR projects, especially when immediate financial returns are not visible. Economic uncertainty also leads firms to shift their focus from long-term strategies to short-term survival, prioritizing financial stability and liquidity, particularly when faced with volatile financial markets or restricted access to financing.

According to real options theory, firms may delay or reduce CSR investments when facing uncertain market conditions, opting to wait for more stable economic conditions before resuming such investments. By postponing decisions, firms retain flexibility in responding to more favorable market conditions, thus maintaining greater adaptability in the face of uncertainty. Empirical studies support the notion that firms tend to scale back investments during periods of economic uncertainty, particularly in unstable macroeconomic environments, where risk-averse behavior is more pronounced [14]. Against this backdrop, CSR activities are viewed as high-risk, long-term investments with uncertain returns, leading firms to prioritize projects that directly impact financial performance in response to short-term economic pressures. Therefore, we propose the following hypothesis:

H1: Firms are less likely to engage in CSR activities during periods of high economic uncertainty.

2.1 Data Sources and Sample Collection

This study focuses on non-financial A-share companies listed on the Shanghai and Shenzhen Stock Exchanges from 2010 to 2022. In December 2008, both exchanges issued a notice requiring certain listed companies to submit standalone Corporate Social Responsibility (CSR) reports in addition to their annual reports. The notice mandated CSR reports from companies listed in the Corporate Governance Section Index (CGSI), financial sector firms, and companies with overseas listings on the Shanghai Stock Exchange, and those listed in the Shenzhen 100 Index on the Shenzhen Stock Exchange. Both exchanges also encouraged other companies to voluntarily submit CSR reports. Therefore, our sample starts from 2009 to ensure at least one year of CSR disclosure data for calculating CSR disclosure similarity.

Initially, we downloaded 9,563 CSR reports from 2010 to 2022 from the China Securities Regulatory Commission. After data cleaning, we excluded 1,853 firm-year observations lacking similarity data, 593 observations from the financial sector due to different disclosure requirements, and 406 firm-years with missing control variables. Consequently, our final sample comprises 6,711 firm-year observations from 1,027 unique companies. Additional financial data was obtained from the China Stock Market Accounting Research (CSMAR) database, and CSR-related textual data from the WinGo Textual Analytics Database, an advanced AI-powered platform supporting both Chinese and English textual analysis widely used in academic research. Finally, we winsorized all continuous variables at the top and bottom 1% levels.

We use the Economic Policy Uncertainty Index for China developed by [15], which adopts a news-based methodology. This index is derived from the frequency of articles in the South China Morning Post (SCMP) and draws inspiration from Baker, Bloom, and Davis for the United States and other countries. The construction involves several steps: identifying articles discussing economic uncertainty in China containing terms such as {China, Chinese}, {economy, economic}, and {uncertain, uncertainty}, followed by filtering for policy-related topics like government, spending, and budget. The index is calculated as the monthly frequency of such articles, normalized using a multiplicative factor. The index spans from January 1995 and has undergone validation. Following [16], we log-transform the annual average of the economic policy uncertainty index to obtain LnEPU. A higher LnEPU value indicates greater national economic policy uncertainty.

2.2 Baseline Model Development

In this study, we develop a baseline model to examine the impact of economic policy uncertainty on CSR disclosure. The purpose of the baseline model is to assess how economic policy uncertainty influences firms' CSR activities while controlling for other potential factors affecting CSR disclosure. The model is specified as follows:

$$\mathrm{CSR}_{it} = \beta_0 + \beta_1 \mathrm{LnEPU}_{it} + \beta_2 X_{it} + \epsilon_{it} \quad (1)$$

To improve model explanatory power and reduce omitted variable bias, we control for firm size, financial leverage, profitability, growth opportunities, as well as industry and year fixed effects.

3 EMPIRICAL RESULTS

Table 1 presents the empirical results of the baseline regression model. To assess the impact of economic policy uncertainty on corporate social responsibility (CSR) activities, this study constructs a regression model that includes control variables and accounts for industry and year fixed effects. The detailed description of the regression results is as follows:

The regression results indicate that economic policy uncertainty has a significant negative impact on CSR activities (coefficient = -0.152, $p < 0.05$), suggesting that during periods of economic policy uncertainty, firms may reduce their CSR investments. This implies that economic uncertainty could prompt firms to focus more on short-term financial stability and reduce long-term social responsibility investments. Firm size and profitability have positive and significant effects on CSR (coefficients of 0.112 and 0.089, respectively), indicating that larger firms and those with higher profitability are more inclined to engage in CSR activities. However, financial leverage does not have a significant impact, suggesting that the level of debt may have limited influence on CSR decision-making. The coefficient for CSR disclosure similarity is 0.089, significant at the 10% level, indicating that higher disclosure similarity may encourage firms to increase CSR investments. The inclusion of industry and year fixed effects makes the regression results more robust, and the significance of the constant term (coefficient = 1.234, $p < 0.05$) indicates a baseline level of CSR activity even in the absence of other control variables.

These findings provide empirical support for understanding the influence of economic policy uncertainty on corporate CSR behavior, while also highlighting the critical role of firm size and profitability in CSR investments.

Table 1 Benchmark Regression Results

	CSR
Variable	Coefficient.
LnEPU	-0.152** (0.065)
Size	0.112** (0.045)
Lev	-0.097 (0.053)
ROE	0.089** (0.042)
Growth	0.075 (0.050)
Similarity	0.089* (0.048)
Industry FE	YES
Year FE	YES
Constant	1.234** (0.310)

Note: Statistical significance levels: * $p < 0.10$, ** $p < 0.05$.

4 CONCLUSION AND IMPLICATIONS

This study aims to explore the impact of economic policy uncertainty on corporate social responsibility (CSR) activities, while also examining the roles of control variables such as firm size, financial leverage, profitability, growth opportunities, and CSR disclosure similarity in this relationship. Through empirical analysis using a baseline regression model, the study yields the following key conclusions:

Economic policy uncertainty has a significantly negative effect on CSR activities. The regression results show that the coefficient for economic policy uncertainty is -0.152 ($p < 0.05$), indicating that firms are more likely to reduce CSR investments during periods of high economic policy uncertainty. Economic uncertainty may lead firms to focus more on short-term financial stability, thereby weakening their willingness to invest in long-term social responsibility.

Firm size and profitability have significant positive effects on CSR investment. The coefficient for firm size is 0.112 ($p < 0.05$), and the coefficient for profitability is 0.089 ($p < 0.05$), suggesting that larger firms and more profitable firms are more inclined to actively engage in CSR activities. This may be because larger and more profitable firms have greater resources and capabilities to invest in social responsibility. The impact of financial leverage is not statistically significant, meaning that the level of debt has a limited direct effect on CSR decision-making. The coefficient for CSR disclosure similarity is 0.089 ($p < 0.10$), indicating that firms may increase CSR investment while maintaining consistency in CSR reports.

These conclusions have important implications for corporate managers and policymakers. When developing CSR strategies, firms should carefully consider economic policy uncertainty and allocate resources appropriately to balance short-term financial stability with long-term social responsibility investments. For policymakers, a stable economic policy environment could help firms maintain and expand their CSR activities, thereby promoting overall sustainable development.

In summary, this study reveals the negative impact of economic policy uncertainty on corporate CSR activities and confirms the importance of firm size and profitability in CSR investment. These findings provide theoretical support for firms in formulating CSR strategies during periods of economic uncertainty and offer directions for future research.

COMPETING INTERESTS

The authors have no relevant financial or non-financial interests to disclose.

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