Internationalization and ESG Performance of EMNCs: Evidence from China

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Abstract

In recent years, ESG has been a widely discussed issue in both the real business environment and academia. As a concept of the close association of CSR (corporate social responsibility), ESG is supposed to help resolve the liability of foreignness in the internationalization process, particularly for EMNCs (emerging market multinational corporations). Thus, based on institutionalization and stakeholder theory, this paper assumes that EMNCs may proactively improve their ESG performance as their extent of internationalization increases. Using the data of 767 Chinese A-share listed EMNCs and 2901 observations from the period of 2015 to 2022, this paper investigates the relationship between internationalization and ESG performance. Considering the extent of internationalization from geographical and financial dimensions, the empirical result shows a significantly positive effect of internationalization on ESG performance, which applies to any dimensions of internationalization. The result holds after the check of robustness, such as employing an alternative dependent variable. Furthermore, this effect is tested by the group of EMNCs entering developed and emerging markets. It is found that the positive effect of internationalization on ESG performance is only effective for EMNCs entering advanced markets.

1. Introduction

In recent years, ESG has been a widely discussed issue in both the real business environment and academia. As a concept of the close association of CSR (corporate social responsibility), ESG is supposed to help resolve the liability of foreignness in the internationalization process, particularly for EMNCs (emerging market multinational corporations). Internationalization is the process by which "a firm expands the sales of its goods or services across the borders of global regions and countries into different geographic locations or markets" (Hitt, Ireland, and Hoskisson, 2007). MNCs refer to multinational corporations, as the participants of internationalization. In their active internationalization process, it becomes inevitable to face the complicated global business environment, especially for EMNCs (Emerging Market Multinational Corporations) entering advanced markets. Thus, this research hopes to explore the relationship between the extent of internationalization and ESG performance for EMNCs. As a case for emerging markets, China's percentage of OFDI of GDP has been in an increasing trend since the 1980s. Therefore, this research will use cases from Chinese EMNCs.

2. Literature Review

To find the research gap, three main topics of literature need to be reviewed, including internationalization, ESG, and the relationship between these two issues.

The existing literature about internationalization is mainly about the process or framework of MNCs' internationalization (e.g. Amal et al., 2013) in qualitative studies. For quantitative studies, the mainly discussed topics include the relationship between internationalization and the financial performance of MNCs(e.g. Hsu, Chen, and Cheng, 2013). However, the research cap is that few studies mention internationalization in the context of CSR or ESG.

For ESG, the literature before is mainly about how ESG can affect other factors. For example, ESG is found to affect GDP at a macro level (e.g. Diaye, Ho, and Oueghlissi, 2022). In the long run, ESG performance positively affects GDP per capita. At a micro level, ESG is associated with firms' financial performance (e.g. Velte, 2017). Many of the research provide proof of a positive relationship between ESG and corporate financial performance. However, few studies research from the opposite side, which is the factors affecting ESG. In the elements that are considered to affect ESG performance, the element of the industry is commonly discussed, such as the difference between some sensitive industries and others (Garcia, Mendes-Da-Silva, and Orsato, 2017). There are several studies on the relationship between internationalization and CSR, such as the one from Attig et al. (2016). However, several ones employ ESG or use SMEs as their research objects.

3. Research Questions

Based on the literature review on the topics above, the research gap can be discussed. Firstly, ESG has not been discussed a lot in academia. CSR has been widely and frequently discussed in many research since it was born. As a concept created later than CSR, recent years have witnessed a rapid development of ESG all over the world. Beginning from ESG investing, nowadays most listed firms have released their ESG report to society. Thus, ESG should also be researched more in academia. Secondly, ESG has rarely been explored under the internationalization context. Although the relationship between internationalization and CSR has been mentioned in some research, that of ESG has seldom been considered. Thirdly, although cases of other countries have been discussed in either internationalization or ESG topics, those of Chinese cases are of great significance while few are discussed. Chinese EMNCs have been developing at a fast speed in recent years, conducting internationalization behaviours like making foreign sales or establishing overseas subsidiaries. Therefore, research on Chinese EMNCs can contribute to the understanding of EMNCs and their CSR behaviour. Furthermore, this impact will be considered in the difference between markets, especially developed and emerging markets. What has been discussed a lot in the existing literature and well observed in real life is that there is an unbalanced situation between developed and emerging markets, such as the perspectives of the economy, institutions and so on.

Based on the literature review and research gaps discussed, this paper aims to explore these research questions.

Firstly, the main research question is :

Does internationalization have a positive impact on the ESG performance of Chinese EMNCs?

Besides, some sub-questions are:

1) How do different aspects of internationalization affect the impact?

2) Does the difference in the market that EMNCs enter affect the impact?

4. Hypothesis Formulation

Figure 1 is the framework of hypotheses 1-3. In the international business area, Institutionalization Theory (Forsgren, 2017) is one of the widely used theories in the International Business (IB) area. It is believed that the environment for MNCs includes not only a business but also an institutional environment, in which legal, cognitive, or normative factors need to be considered. Stakeholder theory is another important theory used in the IB area. Since business is constructed by different relationships and their changes, managers should be responsive to all of the relationships that can create and trade values, including customers, employees, government and so on. The motives from two dimensions act as pull powers for the positive relationship between internationalization and ESG performance. Thus, based on institutionalization and stakeholder theory, this paper assumes that EMNCs may proactively improve their ESG performance as their extent of internationalization increases. The main hypothesis for this paper can be established as follows:

H1: Internationalization can positively affect ESG performance.

H2: Investment level of internationalization impacts ESG Performance positively.

H3: Geographic distributions of internationalization have positive effects on ESG performance.

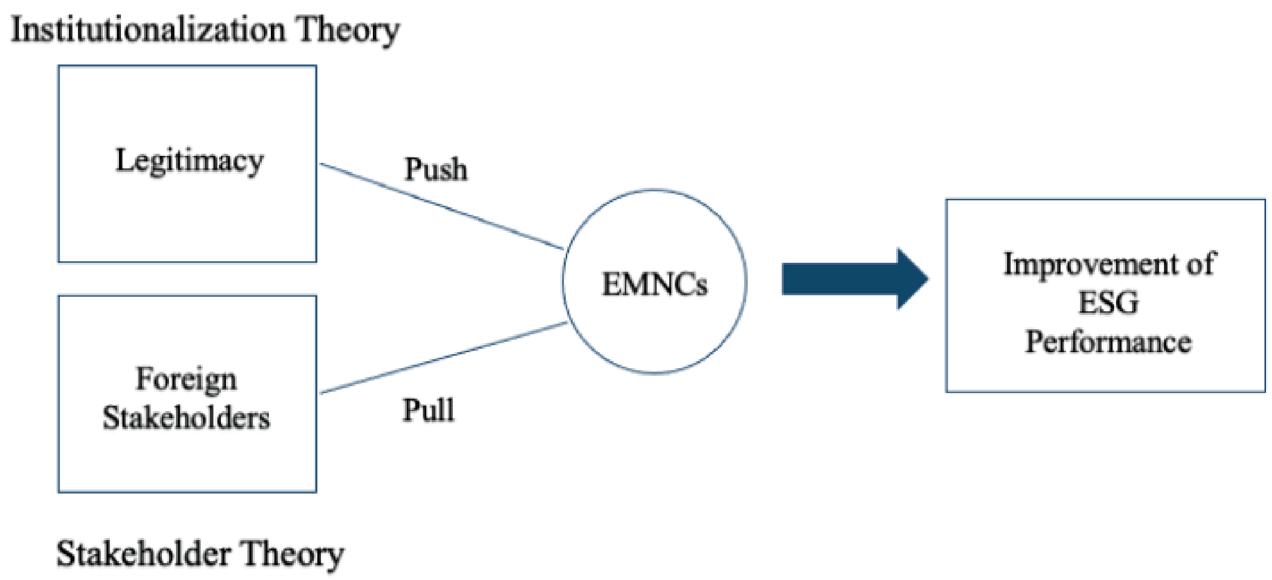

Figure 1 The Framework of Hypotheses 1-3

Besides the institutional and firm level of motives received in the overseas market, there is also organizational learning happening in the internationalization, as shown in Figure 2. Subsidiaries can transfer that new knowledge back to the headquarters in their home country. Through these paths of knowledge transfer, the consequence is that the whole MNC or EMNC gain knowledge from overseas markets, such as the popularity or significance of ESG.

Therefore, based on the organizational learning theory, a further hypothesis can be established:

H4: The impact of internationalization on ESG is more significant in developed markets than in emerging markets.

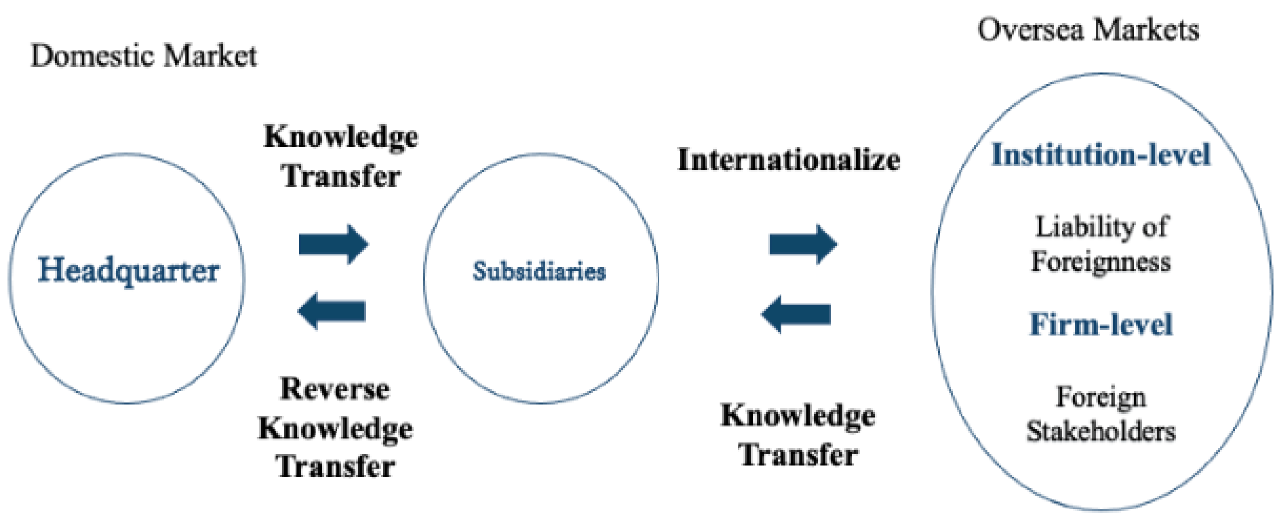

Figure 2 The Framework of Hypothesis 4

5. Methodology

Using the data of 767 Chinese A-share listed EMNCs and 2901 observations from the period of 2015 to 2022, the relationship between internationalization and ESG performance is investigated.

The baseline regression model is shown in the equation.

$$ESG_{i,t} = \beta_0 + \beta_1 Int_{i,t} + \beta Control_{i,t} + \sum Year + \sum Ind + \varepsilon_{i,t}$$

In the model, ESG performance is the dependent variable and different factors for measuring the extent of internationalization are the independent variables. The degree of internationalization is comprehensively measured in 4 indicators. Considering the geographic factors, Inter_Breadth and Inter_Depth are defined to measure the diversification of overseas subsidiaries for EMNCs. Considering the financial factors, Inter_Income is defined as the ratio of foreign income to total operating income. To comprehensively measure the degree of internationalization, Inter_Score is calculated based on the other three independent variables using the Entropy Weighting Method. β_0 is the constant and $Control_{i,t}$ are the control variables, including ROA, firm size and so on. $\sum Year + \sum Ind$ are the fixed effects of time and industry and $\varepsilon_{i,t}$ is the error term.

6. Results

Considering the extent of internationalization from geographical and financial dimensions, the empirical result shows a significantly positive effect of internationalization on ESG performance, which applies to any dimensions of internationalization. The result holds after the check of robustness, such as employing an alternative dependent variable. Furthermore, this effect is tested by the group of EMNCs entering developed and emerging markets. It is found that the positive effect of internationalization on ESG performance is only effective for EMNCs entering advanced markets. Besides, the market value is employed as a moderating variable positively acting on the impact of internationalization on ESG performance.

This research helps to fill the research gap in the international business area. Although ESG has been a popular topic these years, little research look into the factors that can affect ESG performance. Moreover, few research discuss this topic under the context of internationalization and focus on EMNCs rather than purely MNCs.

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