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ESG narrative and ESG performance :Talk or Walking the talk?

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Abstract: The subject, text and object constitute the basic logical framework of narratology, the subject of the ESG narrative is listed companies, the text is ESG reports, corporate governance, and environment and society-related content in annual reports, and the object is stakeholders. This paper selects China's A-share listed companies in 2018 ~ 2022 as the initial sample and represents the ESG narrative by selecting the ESG-related word frequency weights in the annual report of the enterprise in that year. The multiple regression model of ESG "consistency between words and deeds" is constructed by taking the ESG rating scores of CSI in the same year as the ESG performance of the enterprise. It is found that, firstly, there is indeed a "discrepancy between words and deeds" between corporate ESG narratives and corporate ESG performance, and corporations have a stronger tendency to exaggerate their CSR. Second, board size is positively related to corporate ESG "misrepresentation", and firm size has a particularly significant effect on the social dimension of corporate ESG performance.The above findings have some implications for our regulators: First, we should pay more attention to the social dimension of corporate ESG narratives, as listed companies often exaggerate their social responsibilities to improve their ESG performance. Second, more quantitative indicators should be used to evaluate the social dimension.
Keywords: ESG Narrative, ESG Performance,ESG "inconsistent"

Introduction

ESG, which stands for Environment, Social, and Governance, is a comprehensive non-financial performance assessment framework for measuring the environmental, social, and governance performance of companies.

Mieke Bal, a renowned Dutch contemporary narratologist, in his book Narratology: An Introduction to Narrative Theory, proposes a "theory of narrative texts", which is known as "narratology" (Bal M, 2009)[1], he argues that "the theory of narrative texts" is the most important element of corporate performance assessment in the world. According to Bal M, 2009, narrative practice consists of three basic components: who tells the story (the narrator), what is the story (the text), and who listens to the story (the receiver). The narrator is the core of narrative practice. The narrator is the subject of narrative practice, the text is the object on which narrative practice is based, i.e., the content, framework, and material, and the receiver is the object of narrative practice, and this "trinity" constitutes the basic logical framework of narratology[2].(Zhengfu Shen,2023)

ESG narrative, is often mistakenly thought to be equivalent to ESG disclosure. However, there are some conceptual and purposeful differences between ESG narrative and ESG disclosure. ESG narrative refers to how a company tells the story of its ESG strategy and performance, and ESG narrative is more of a process. In contrast, ESG disclosure refers to how a company discloses information about its ESG performance to the public, and ESG disclosure is more of an outcome. As British novelist W. Somerset Maugham said, "The process is more important than the result," and ESG narratives deserve more attention.

Currently, the main vehicle for China's ESG narrative is in ESG reports, corporate governance, and environmental and social responsibility chapters in annual reports. As of 2024, 953 listed companies in China have already disclosed their 2023 corporate ESG reports to the public, a 74% [2]increase from 2023. This represents 18% of the total number of A-share listed companies (5,198).[3] However, for a long time, the "decoupling phenomenon" of CSR has been common, which means that the commitments made by enterprises at the social level have not been fulfilled in practice [3].

Whether a listed company talks or walking the talk affects the listed company's market capitalization[4][5][6][7], but also tarnishes its corporate image[8][9][10][11].

Literature Review

1.Research about consistency of ESG performance and narrative

Papers examining ESG narratives alone focus on ESG narrative tone.Albitar K et al. (2023), in examining the relationship between corporate governance, and ESG narrative tone, found that more independent directors would lead to a less optimistic language (positive tone) and a more pessimistic language (negative tone) in the CSR report[12].

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[2] Source: Calculated based on data published on cninfo.com.cn.

[3] Source: Flush Finance (10jqka.com.cn)

In contrast, research attention on ESG narratives has focused more on ESG disclosure[13]. Despite a large and important literature on ESG performance and ESG disclosure, there is still a deficiency in studying the relationship between them[14]. The literature on the relationship between ESG performance and disclosure is very sparse. From the field of CSR, the most recent work on this topic focuses on the phenomenon of green washing[15] and the consistency or inconsistency of companies in this regard[16]. The consistency of ESG narratives and ESG performance then extends to the study of "cohort effects" and "green washing".
X X He et al.(2024)argue that just as there is "inconsistent" behavior in enterprises, "inconsistent" corporate ESG also exists and has a diffusion effect.The triggering mechanism of ESG "misbehavior" is influenced by internal capabilities and the external environment. In large-scale firms, excess compensation reinforces the diffusion benefit of ESG "words over deeds"; in industries with low market concentration, the diffusion effect of ESG "words over deeds" does not exist, while the diffusion effect of "deeds over deeds" is significant, and in industries with high market concentration, the diffusion effect of ESG "words over deeds" is significant. In industries with low market concentration, the diffusion effect of ESG "words over deeds" does not exist, while the diffusion effect of "deeds over words" exists significantly, while in industries with high market concentration, the diffusion effect of ESG "words over deeds" exists significantly[17].Yue Wu (2020) argues that with the growing popularity of corporate social responsibility (CSR), critics point out that companies tend to focus on prominent CSR activities while neglecting the unobservant, using CSR as a marketing headline. Companies emphasizing the observable over the unobservant are often referred to as "green washing".[15]
The debate on whether it is possible for firms to do well by doing good in either ESG performance or disclosure is still ongoing.They find that the consistency of ESG and its three separate dimensions negatively affects the corporate stock price crash risk. ESG consistency contributes to lower stock price crash risk through the mechanisms of alleviating agency problems and increasing information transparency.（Huang J et al.,2024）[18].

2.Theories and hypotheses

There are three common types of "inconsistencies" between corporate ESG disclosure and performance: first, misleading the public by misrepresenting or exaggerating a company's actual ESG activities.For example, a BP spokesperson claimed that the company would invest $8 billion in renewable energy technologies between 2005 and 2015, while Greenpeace said that, in fact, 93% of BP's investment fund in 2008 was spent on fossil fuels, and only 1.3% was spent on solar energy technologies; secondly, the use of impression management tactics in disclosure activities to present a company's image to the outside world by means of symbolic and superficial work, such as by reporting on "positive energy events" or presenting an empty picture of a company. Second, they use impression management strategies in their disclosure activities to present a positive public image through symbolic and superficial efforts, such as reporting on "positive events" or making empty promises to build up ESG reports; and third, they are selective in their disclosure activities, choosing to disclose only beneficial or relatively harmless ESG information, and shying away from negative information[19].
According to the theory of management motivation, the emergence of ESG narrative and ESG performance divergence can be distinguished into two scenarios: one is unintentional. the lack of ESG professionals, the lack of ESG disclosure system and standards leads to the lack of basis for narrative behavior and other difficulties, which greatly increases the subjective arbitrariness of managers in the implementation of ESG information disclosure. Second, it is premeditated. From the individual level, Lin wanfa et al. (2022) take agency theory as a starting point, pointing out that management will obfuscate through a large amount of descriptive information in order to realize personal interests such as reputation protection and position stability[20].
From the perspective of stakeholder theory, ESG disclosure is the result of conflicts and games among corporate stakeholders, and the governance effect of institutional investors on corporations is closely related to their motivations [21], and the conflict between management and institutional investors with inconsistent interest objectives may further exacerbate the extent of ESG "inconsistency in words and deeds". "Institutional theory.
From the perspective of institutional theory, institutional pressures drive firms to adopt new strategies to adapt to the competitive environment[22]. The cost of change and adaptive capacity of different firms bring new pressures on management to cope with the changes in the competitive landscape, which increases the likelihood of management's "misbehavior" due to conflict of interest issues.Based on the above analysis, this paper proposes the following hypotheses:

H1: There is "inconsistent" behavior between corporate ESG narratives and corporate ESG performance.

Suttipun M (2021) found that there is a positive correlation between the size of the board of directors and corporate ESG using a sample of Thai-listed companies from 2015 to 2019[23].Chebbi K and Ammer M A (2022) examined the relationship between board composition (size, independence, and gender diversity) and ESG disclosure and the impact of corporate governance reforms on ESG disclosure using a sample of Saudi-listed companies. The results confirm that board size and its level of independence have a positive and significant effect on ESG disclosure[24].Thirumagal P G et al. (2023) studied the moderating effect of board independence and board size between women directors and ESG using five years data of from 28 companies for the period 2017-2021, which was analyzed through Eviews software, using multiple regression analysis find the moderating effect. Board independence, board size, and company size have significant effects on ESG, environmental, social, and governance factors[25].Based on the above analysis, this paper proposes the following hypotheses:

H2: There is a positive correlation between board size and corporate ESG "inconsistent".

Research design

1.Sample selection and data source

In this paper, China's A-share listed companies are selected as the initial sample from 2018 ~ 2022, the financial data are obtained from CSMAR database, various annual reports are collected from Juchao Information Network (CNN), and the samples are screened in the following ways: ① excluding samples that have been treated by special treatment such as ST or ＊ ST during the sample period; ② excluding listed companies in the financial category; ③ excluding companies that have appeared for only one year; and ④ eliminating the companies with missing and abnormal data (iv) Remove companies with missing data and anomalies. Finally, 11125 annual observations of companies are obtained.

2.Variables design

In this paper, the construction method of ESG "words and deeds" matching degree index is as follows: first, ESG_words are selected to represent the ESG narrative score in the annual report of the enterprise in the current year. Then, the ESG_scores of the company's annual report represent the ESG performance, IB is the ratio of independent directors, and BSIZE is the size of the board of directors.

Variable Type	Variable Name		Variable Symbol	Description
Independent variable	ESG Narrative	Annual report ESG related word frequency	ESG_words	See above for details
Dependent Variable	ESG Performance	CSI ESG Rating Score	ESG_scores	Equals to CSI ESG Rating Total Score
			E	CSI's score on environmental dimension
			S	CSI's score on social dimension
			G	CSI's score on corporate governance dimension
Control Variables		Independent Director Ratio	IB	Number of Independent Directors / Number of All Directors
		Board Size	BSIZE	Natural logarithm of the number of all directors

Finally, the regression model (1) is constructed and later on, the samples with residuals equal to 0 are considered as ESG "consistent" samples, and the samples with residuals less than 0 are considered as ESG "inconsistent" samples.

$$\mathrm{ESG}\_scores = \beta_0 + \beta_2 ESG\_word\mathrm{s} + IB + BSIZE \quad (1)$$

Before obtaining the ESG-related word frequencies of the annual reports of enterprises in the current year, it is necessary to construct an ESG participle dictionary for Python text analysis. First, 655 available ESG reports of listed companies in China from 2018 to 2022 were downloaded from Juchao Information Network, and these reports were pre-processed by converting text format, removing punctuation marks and numbers, and then based on the principles of high-frequency and high-relevance, ESG words were analyzed in 99999+ words among three core dimensions, namely, "environment", "society", and "governance", and the word frequencies of ESG related words were analyzed in Python. Based on the principles of high frequency and high relevance, we extracted the top 11125 ESG keywords with the highest word frequency among 99999+ words in the three core dimensions of "environment", "society" and "governance", and constructed the ESG_word with the keyword weights,and the top 300 key word with the highest frequency are shown in figure1.

Fig.1:Top 300 key word with the highest frequency

Empirical analysis

1. Descriptive Statistics Analysis

Table 2 reports the number of observations, mean, standard deviation, variance, minimum, 25% quartile, median, 75% quartile, and maximum for the main variables, totaling 11125 observations. The mean values of the variables IB, BSIZE, and ESG_words are 0.3787, 2.1259, and 0.0004, respectively; the mean value of the variable ESG_scores is 72.7582, and the mean values of the variables in the dimensions of environmental E_score, social S_score, and governance G_score are 61.8979, 75.6436 and 76.6376, implying that corporate governance and society perform significantly better than environmental performance.

Table 2 Description Statistic

		ESG_scores	E_score	S_score	G_score	IB	BSIZE	ESG_words
N	Valid	11125	11125	11125	11125	11125	11125	11124
	Missing	0	0	0	0	0	0	1
Mean		72.758214	61.897906	75.643561	76.637582	.378677	2.125854	.000372
Median		73.060000	61.530000	76.240000	78.430000	.363600	2.197200	.000095
Mode		71.7500[a]	48.1900	100.0000	80.4500	.3333	2.1972	.0000
Std. Deviation		6.2483537	8.1877226	10.0186586	8.6144970	.0586388	.2008424	.0013093
Variance		39.042	67.039	100.374	74.210	.003	.040	.000
Minimum		41.1900	31.0800	9.7700	19.6000	.1667	1.3863	.0000
Maximum		92.9300	95.1600	100.0000	97.0000	.8000	2.8904	.0473
Percentiles	25	69.255000	56.510000	70.240000	73.270000	.333300	1.945900	.000052
	50	73.060000	61.530000	76.240000	78.430000	.363600	2.197200	.000095
	75	77.055000	67.110000	82.020000	82.190000	.428600	2.197200	.000236

a. Multiple modes exist. The smallest value is shown

2. Relevance analysis

Table 3 shows the correlation coefficient analysis of the variables. The variables E_score, S_score, and G_score are significantly and positively correlated with ESG_scores at a 1% level. The variable IB is significantly and positively correlated with BSIZE at a 1% level and with ESG_words at a 5% level. The variable BSIZE is significantly and positively correlated with S_scores at the 5% level and with IB at the 1% level. The variable ESG_words is significantly and positively correlated with E_score and BSIZE at 1% level and significantly and positively correlated with IB at 5% level. The above results preliminary support hypothesis 1.

Table 3 Correlations

		ESG_scores	E_score	S_score	G_score	IB	BSIZE	ESG_words
ESG_score	Pearson Correlation	1	.568**	.672**	.757**	-.004	.008	-.003
	Sig. (2-tailed)		.000	.000	.000	.702	.426	.781
	N	11125	11125	11125	11125	11125	11125	11124
E_score	Pearson Correlation	.568**	1	.338**	.158**	.010	.007	-.053**
	Sig. (2-tailed)	.000		.000	.000	.290	.445	.000
	N	11125	11125	11125	11125	11125	11125	11124
S_score	Pearson Correlation	.672**	.338**	1	.151**	-.011	.021*	-.005
	Sig. (2-tailed)	.000	.000		.000	.261	.028	.617
	N	11125	11125	11125	11125	11125	11125	11124
G_score	Pearson Correlation	.757**	.158**	.151**	1	.001	-.003	.008
	Sig. (2-tailed)	.000	.000	.000		.925	.736	.419
	N	11125	11125	11125	11125	11125	11125	11124
IB	Pearson Correlation	-.004	.010	-.011	.001	1	-.536**	-.020*
	Sig. (2-tailed)	.702	.290	.261	.925		.000	.034
	N	11125	11125	11125	11125	11125	11125	11124
BSIZE	Pearson Correlation	.008	.007	.021*	-.003	-.536**	1	.031**
	Sig. (2-tailed)	.426	.445	.028	.736	.000		.001
	N	11125	11125	11125	11125	11125	11125	11124
ESG_words	Pearson Correlation	-.003	-.053**	-.005	.008	-.020*	.031**	1
	Sig. (2-tailed)	.781	.000	.617	.419	.034	.001	
	N	11124	11124	11124	11124	11124	11124	11124

**. Correlation is significant at the 0.01 level (2-tailed).

*. Correlation is significant at the 0.05 level (2-tailed).

3. Regression Analysis

The regression results for Hypothesis 1 are reported in Tables 4-6. In Table 4, the value of Adjusted R Square is 0.973, which is much greater than 0.3, which implies that the independent variables E_score, S_score, G_score, IB, BSIZE, and ESG_words selected in this paper are extremely strong in explaining ESG_scores. In Table 5, the significance values of the independent variables are less than 0.05, indicating that all the independent variables E_score, S_score, G_score, IB, BSIZE, and ESG_words have a significant effect on ESG_scores. Durbin-Watson is a statistic used to test for autocorrelation in regression analysis, if there is autocorrelation, then the residuals of the residuals of the regressions of the regressions of the regressions of the regressions of the regressions of the regressions of the regressions of the regressions of the regressions. If there is autocorrelation, then the residuals are not independently and identically distributed, which affects the validity and accuracy of the regression equation. D-W value in the range of 1.5-2.5 is acceptable, and in this paper, the D-W value is 1.791, which is acceptable.VIF (Variance Inflation Factor) is a statistic that measures the severity of multicollinearity. A statistical quantity. Generally, less than VIF less than 5 means that there is no covariance between the variables. In this paper, the VIF of all variables is less than 5, which means that there is no covariance between the variables, and the results are acceptable. In Table 6, the residuals are 4.9814, which is less than 0, meaning that there are samples that are "overstated", which verifies Hypothesis 1. At the same time, the residuals indicate that in addition to the six independent variables E_score, S_score, G_score, IB, BSIZE, and ESG_words, there must be other factors that affect the results. In addition to the six independent variables of E_score, S_score, G_score, IB, BSIZE, and ESG_words, there must be other factors affecting the performance of ESG. Since the residuals are random variables, it is a more desirable state when they are normally distributed, see Figure 2.

Table 4 Model Summary[b]

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Durbin-Watson
1	.986[a]	.973	.973	1.0276105	1.791

a. Predictors: (Constant), ESG_words, S_score, IB, G_score, E_score, BSIZE

b. Dependent Variable: ESG_score

Table 4 Model Summary[b]

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1	.986[a]	.973	.973	1.0276105	1.791

a. Predictors: (Constant), ESG_words, S_score, IB, G_score, E_score, BSIZE

b. Dependent Variable: ESG_score

Table 6 Residuals Statistics[a]

	Minimum	Maximum	Mean	Std. Deviation	N
Predicted Value	42.029255	92.324783	72.757149	6.1625816	11124
Residual	-4.9814305	6.3497915	.0000000	1.0273333	11124
Std. Predicted Value	-4.986	3.175	.000	1.000	11124
Std. Residual	-4.848	6.179	.000	1.000	11124

a. Dependent Variable: ESG_score

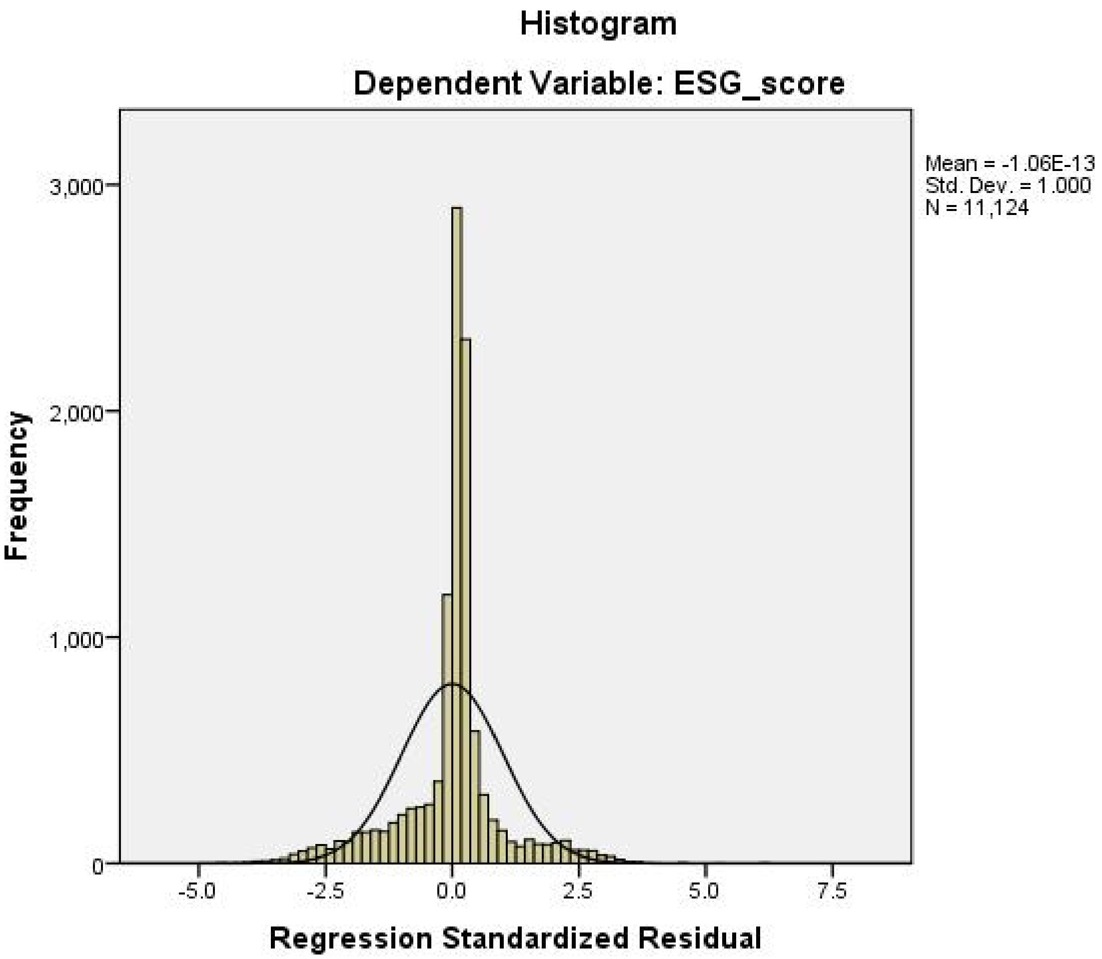

Fig2.Regression Standard Residual

Results and Discussion
Given the current behavior of listed companies' "inconsistency in words and deeds", this paper finds through the construction of multiple regression models that: first, there is indeed "inconsistency in words and deeds" between corporate ESG narratives and corporate ESG performance. According to the distribution of scores in the E, S, and G sections, corporate environmental indicators generally score lower, partly because environmental measures are more standardized than social responsibility. Therefore, rather than a strong incentive to "green washing", firms have a stronger tendency to exaggerate their CSR. Second, board size is positively associated with corporate ESG "misrepresentation", with firm size having a particularly significant impact on the social dimension of corporate ESG performance. The above findings have some implications for our regulators: First, we should pay more attention to the social dimension of corporate ESG narratives, as listed companies often exaggerate their social responsibilities to improve their ESG performance. Second, more quantitative indicators should be used to evaluate the social dimension.

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