Details of Applicants	**Principal Investigator** Dr Chen Zheng – Senior Lecturer chen.zheng@curtin.edu.au Curtin University **Co-Investigator** Dr George Shan – Associate Professor george.shan@uwa.edu.au University of Western Australia
Project Title	Sustainability engagement and stock price crash risk: Theoretical effect during the COVID-19 pandemic
Project Summary	There is no change in the project (such as research topic and methodology) used to apply AFAANZ research grant 2021-2022 round 2. Please see the below a summary of the completed project. The objective of this study is to investigate whether sustainability engagement is related to firm-specific stock price crash risk during the COVID-19 period. In this study, we employ firms' sustainability news releases during the crisis to examine its effect on the crash risk. The rationale is threefold. First, a sustainability news release draws stakeholders' attention more broadly because it coordinates their attention through agenda-setting. This release is argued to be a more effective vehicle for engaging powerful stakeholders than the other types of information channels. Second, it influences stakeholders' cognitive response to corporate sustainability engagement through framing. That is, a sustainability news release is regarded as a third-party disclosure, which is argued to be a framing mechanism that can communicate with stakeholders effectively. Third, corporate sustainability disclosures or corporate reports related to sustainability engagement during the early stage of the pandemic were simply not readily available to the market, and consequently, the market often relied on third-party media coverage to understand firms' corporate sustainability engagement. Our theoretical underpinnings are developed through the legitimacy theory and the agency theory, which provide two essentially competing arguments regarding the implications of sustainability engagement for the managerial behavior of hoarding bad news that can lead to a stock price crash. We conjecture from the legitimacy theory perspective that sustainable or responsible firms are less likely to accumulate and withhold bad news, and they thereby reduce their stock price crash risk since they often signal their legitimacy through greater transparency and more complete revelation of firm-specific information. In contrast, we argue from the agency theory perspective that, if managers disguise bad news and overinvest in sustainability activities to further their own agendas at the expense of other stakeholders, then sustainability engagement would be associated positively with crash risk.

	Our findings suggest that firms with sustainability engagement are more prone to stock price crashes during the COVID-19 pandemic. Surprisingly, the evidence in our study lends credence to the agency theory explanation per se for the positive association observed between sustainability engagement and crash risk, and is less supported by the legitimacy theory that implies sustainability engagement has a mitigating effect on crash risk. The results remain consistent with our main findings after we break down sustainability into the four types. Our results still hold after accounting for the effect of the past-year sustainability performance in our baseline model. In addition, our main findings are robust to the endogeneity checks we conduct by employing the instrumental variables (IV) approach and a dynamic panel generalized method of moments (GMM) estimation.
Funds Granted	An award of $5,800 was granted for this application by AFAANZ.
Details of Expenditures	The breakdown of research fund $5,800 consumed on this project is as follows: Due to limitations of the fund for this project we could get support of the research assistant only in terms of data collection / cleaning purposes. Research assistant name – Alinda Mondal Data collection, cleaning, and merging: RA helped us extract news from Google News to construct our sustainability media coverage (103.59 hours, $5,697.53).
Outcomes such as Working Papers	Applicants has successfully completed the project and research paper has been presented at 2022 AFAANZ Conference and submitted to an ABDC A* ranked journal - *The British Accounting Review* (rejected) and A ranked journal - *International Review of Financial Analysis* (under review). <u>Abstract:</u> Using textual analysis of the third-party disclosure of corporate sustainability news focused on the Standard and Poor’s 500 firms in the US market during 2020Q1 and 2020Q2, we find that corporate sustainability news release is positively related to firm specific stock price crash risk. This finding is surprising, but it indeed aligns with the agency theory. It indicates that the COVID-19 pandemic exacerbates the tendency of managers under increasing financial pressure to use the sustainability information release as a mechanism to mask and withhold bad news for extended periods at the expense of shareholders, which results in high stock price crash risk. Our results are robust to alternative empirical specifications, estimation methods, and tests for endogeneity. Moreover, additional evidence reveals that the agency theory dominates the legitimacy theory to explain the effect of sustainability on the stock price crash risk during the COVID-19 pandemic.

Future Intentions for this Project	The research paper is intended to be published for Journal *International Review of Financial Analysis* or other A*/A ranked journal. Also, authors aim to present it at renowned Accounting and Finance conferences internationally.
Summary of Outcomes and Benefits	The research fund has played a crucial part in completion of this project. Textual analysis for data collection is time consuming. The research fund has freed up the research team's time to concentrate on theoretical framework, hypothesis development, empirical methodology and analysis. Our study provides incremental contributions to the extant literature in several ways. First, we contribute to the sustainability theoretical underpinnings explained by pairwise competing arguments based on the legitimacy theory and the agency theory. Second, to the best of our knowledge, this is the first study to provide empirical evidence on the real-time effect of the sustainability information release in a short window on stock price crash risk, which thus fills a gap in the literature. Third, our study contributes to the line of research that examines sustainability or CSR reporting and disclosure with media coverage by using a short window.