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DOES PRIMARY STAKEHOLDER MANAGEMENT POSITIVELY AFFECT THE BOTTOM LINE? SOME EVIDENCE FROM AUSTRALIA

by

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Abstract

The premise behind stakeholder theory is that firms are comprised of interdependent relationships ('primary stakeholders') and that firms have a responsibility to manage these relationships strategically in order to meet corporate objectives. Failure to retain the participation of a primary stakeholder group will result in the failure of that corporate system. To test the theory, this research studies the relationship between management of primary stakeholders and firm performance in a sample of Australia firms. The results suggest that some primary stakeholder groups, but not all, positively affect firm performance. More specifically, corporate governance and employee management were significantly and positively associated with performance. On the other hand, environmental performance and social impact, while significant, had a negative association with performance. The study, to a degree, confirms stakeholder theory. However, rather than offering equal attention to all primary stakeholders, the implications of this research suggest that firms might favour those stakeholder groups that can most positively affect their performance.

Keywords

Stakeholder theory, primary stakeholders, stakeholder management, internal stakeholders, external stakeholders, firm performance

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INTRODUCTION

According to Porter (1980, 1985), corporate strategy has, as a major underlying premise, a focus on obtaining a competitive advantage. By obtaining a competitive advantage a firm can positively affect its performance (Porter, 1991). For any management team, the issue of positively affecting firm performance is of fundamental strategic concern.

Over the years, there has been no shortage of prescribed strategies for how firms can positively affect their performance. For example, a popular strategy built upon industrial organization (IO) economics is the competitive forces approach, where a firm seeks to defend itself against five industry forces (consumers, suppliers, direct competitors, substitutes and potential entrants) and, where possible, tries to influence them in its favour (Porter, 1980, 1985). The key objective of this strategy approach is for the firm to limit competition so as to be in a better position to seize and keep as much profit for itself as possible. Strategies based on building core competencies, on the other hand, are aimed at helping a firm create a unique position in the market—one that cannot be easily duplicated—thereby offering the potential to generate and protect superior returns (Prahalad and Hamel, 1990). A market orientation strategy suggests that in order to positively affect performance, a firm needs to gain keen knowledge about its market, turn that knowledge into a customer value proposition that is superior to its competitors while at the same time continuously adapting to market changes (Kohli and Jaworski, 1990; Narver and Slater, 1990).

Another strategy, perhaps one that is gaining renewed attention in light of an ever-growing interest in corporate social responsibility and corporate citizenship, is stakeholder management

(Freeman, 1984). The premise behind stakeholder management is that firms are comprised of interdependent relationships ('primary stakeholders') and that firms have a responsibility to manage these relationships strategically in order to meet corporate objectives (Freeman, 1984; Clarkson, 1995; Donaldson and Preston, 1995; Post et al., 2002; Crane and Livesey, 2003; Bourne and Walker, 2005; Zsolnai, 2006). As with any strategic management approach, corporate managers, faced with difficult decisions with respect to scarce resource allocation, must ask if stakeholder management has the potential of generating an advantage that positively affects the bottom line. Such is an important practical question for management teams—and for researchers, an important empirical question.

The objective of this paper is to examine what impact, if any, primary stakeholder management has on firm performance. More specifically, we seek to:

1. Describe how primary stakeholder management might positively affect a firm's bottom line.
2. Empirically test the relationship between primary stakeholder management and firm performance.
3. Offer practical insights for managers interested in understanding if there is strategic value to be gained from a primary stakeholder management approach.

To proceed, we first explore the theoretical background of primary stakeholder management and propose hypotheses. Next, the methodology and results are discussed. Following the results, we discuss the findings and offer limitations. Finally, implications and a conclusion are offered.

THEORETICAL BACKGROUND AND HYPOTHESES

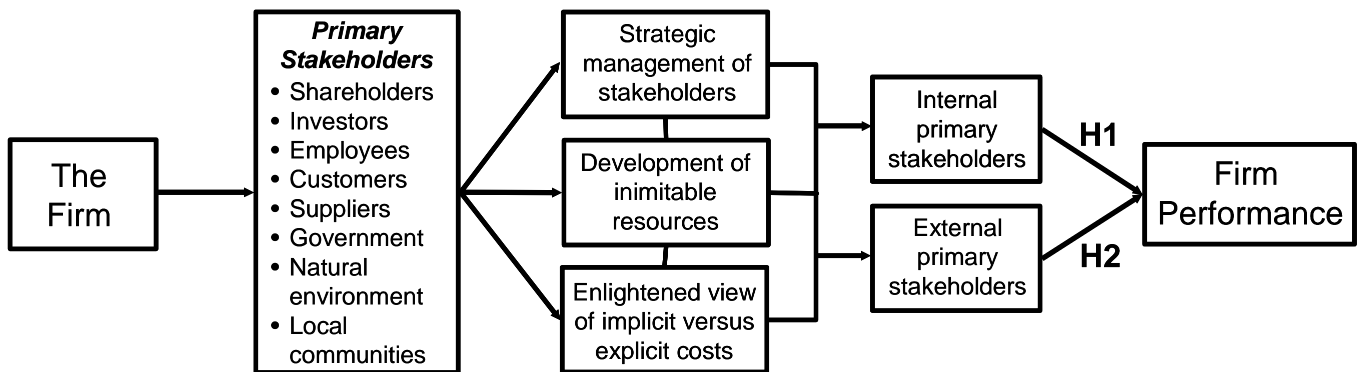
A good deal of attention has been focused on the responsibilities of business in society. Carroll (1979), in a defining article, suggested that firms have four responsibilities: 1) economic; 2) legal; 3) ethical; and 4) discretionary (e.g., philanthropy). While Carroll's (1979) work described *what* a firm's responsibilities might be, Freeman's (1984) landmark book helped to more accurately describe to *whom* the firm is responsible. Picking up on this theme, stakeholder theory gained prominence in the 1990s—and continues today—as a focused area of study within the management literature. Essentially, stakeholder theory is based on the proposition that firms are comprised of interdependent relationships ("primary stakeholders") and that firms have a responsibility to manage these relationships strategically in order to meet corporate objectives (Freeman, 1984; Hill and Jones, 1992; Harrison and St. John, 1994; Clarkson, 1995; Donaldson and Preston, 1995; Jones, 1995; Mitchell et al., 1997; Jawahar and McLaughlin, 2001; Post et al., 2002; Crane and Livesey, 2003). However, consensus on an exact definition of primary stakeholders has yet to be achieved (Mitchell et al., 1997; Beaver, 1999; Jawahar and McLaughlin, 2001; Lépineux, 2005).

For purposes of this paper, we adopt Clarkson's (1994, p. 5) definition of primary stakeholders as those stakeholders who "bear some form of risk as a result of having invested some form of capital, human or financial, something of value, in a firm". Primary stakeholders include those groups that are important to the firm as an ongoing concern. Clarkson (1995) and Starik (1995) suggest primary stakeholders include groups such as shareholders, investors, customers, employees, suppliers, governments who provide infrastructures and whose laws and regulations must be obeyed, the natural environment and the communities in which a firm operates. Although not all community 'residents' can be considered investors, customers, suppliers or employees, they provide an infrastructure base for the firm and in turn are directly impacted by tax revenues and natural environment protection (or degradation).

According to Clarkson's (1995) and Starik's (1995) conceptualisation of primary stakeholders, we can discern that there is an 'internal' and an 'external' perspective. That is, primary stakeholders can be conceptualised as consisting of both internal and external constituents, which corroborates other scholars who likewise suggest that firms have obligations and strategic considerations for both internal and external stakeholders (Kanter, 1999; Porter et al., 2002; Post et al., 2002; Gago and Antolín, 2004). More specifically, from the 'internal' perspective, firms engage with and have responsibilities to primary stakeholders such as employees and shareholders. On the other hand, 'external' primary stakeholders include constituents such as customers, communities, suppliers, government entities and the natural environment. Such a perspective suggests that, in theory, firms seeking advantages from a primary stakeholder management orientation are faced with the task of strategically addressing multiple constituents, one where balancing a variety of interests and needs is important in terms of affecting firm performance. Figure 1 presents the theoretical model.

FIGURE 1

Theoretical model



Hypotheses

According to Clarkson (1995), primary stakeholders exert considerable influence on a firm. If one, or all, of these 'internal' or 'external' stakeholders "becomes dissatisfied and withdraws from

the corporate system, in whole or in part, the corporation will be seriously damaged or unable to continue as a going concern" (Clarkson, 1995, p. 106). Thus, "the corporation's survival and continuing success depend upon the ability of its managers to create sufficient wealth, value, or satisfaction for those who belong to each [primary] stakeholder group, so that each group continues as a part of the corporation's stakeholder system. Failure to retain the participation of a primary stakeholder group will result in the failure of that corporate system" (Clarkson, 1995, p. 107). In this sense, a firm may be best viewed as a complex, interdependent set of primary stakeholders. However, effectively managing primary stakeholders can result in much more than their on-going participation with the firm; it can lead to the development of 'resources' that are inimitable, therefore offering protection against the erosion of any financial benefits that these resources might generate. The foundation for this view comes directly from the field of strategic management and specifically resource-based theory.

Resource-based theory (Dierickx and Cool, 1989; Barney, 1991; Amit and Schoemaker, 1993) posits that firms who wish to gain an advantage over their competitors need to develop resources that are causally ambiguous, socially complex, difficult to imitate and that pass through critical time-dependent stages. One way to create such resources is through effective interactions with primary stakeholders. For example, firms who are able to engage primary stakeholders beyond market transactions—which can be imitated by competitors—to develop long-term *relationships* create socially complex, time-dependent resources based on reputation and trust; reputation and trust can enhance the value of relationships, which is not so easily imitated by competitors (Fombrun and Shanley, 1990; Barney, 1991; Barney and Hansen, 1994).

According to Barney (1991), developing socially complex, time-dependent and inimitable resources, such as primary stakeholders, can lead to competitive advantage and be a source of

superior performance. Similarly, Jones (1995) argues that firms who develop relationships with primary stakeholders based on mutual trust and cooperation are in a better position to gain an advantage over firms that do not. The reason being is that developing trust and cooperation between primary stakeholders takes time, which in turn leads to mutually beneficial value exchanges. Such exchanges are beneficial to primary stakeholders in that they receive value in excess of the effort required to engage in the exchanges; to the firm, they gain advantages that lead to improved performance (Jones, 1995; Prahalad, 1997).

Lastly, stakeholder theory also recognises that firms have explicit costs (e.g., payments to bondholders) and implicit costs (e.g., environmental costs, human resource costs). Stakeholder theory predicts that if firms try to lower their implicit costs by acting socially irresponsible (e.g., not investing in pollution control systems, treating employees poorly) they will actually incur higher explicit costs, which can result in a competitive disadvantage. Reflecting this logic, Alexander and Buchholz (1982) argue that demonstrating high levels of responsibility towards primary stakeholders is an indicator of superior management skill, which leads to lower explicit costs. Additionally, the actual costs of primary stakeholder management versus the benefits may be minimal. For example, enlightened employee management policies may have a relatively low cost, but the gains in productivity, morale and retention can yield substantial performance advantages over less responsible firms (Moskowitz, 1972; Huselid, 1995; Khatri, 2000; Cruz Déniz-Déniz and De Saá-Pérez, 2003).

We have discussed that stakeholder theory suggests that firms may best be viewed as a set of interdependent, ‘internal’ and ‘external’ primary stakeholders including shareholders, customers, employees, suppliers, governments, the communities in which they operate and the natural environment. Extrapolating from Freeman (1984), Clarkson (1995) and Lépineux (2005), among others, one can deduce that the strategic management of primary stakeholders is an important factor for positively affecting firm performance. Additionally, the relationships that result from

effectively managing primary stakeholders can lead to socially complex and inimitable resources, resources that underlie competitive advantage (Barney, 1991; Jones, 1995). Therefore, we offer the following propositions:

> Hypothesis 1: 'Internal' primary stakeholder management is positively associated with firm performance.
>
> Hypothesis 2: 'External' primary stakeholder management is positively associated with firm performance.

METHODOLOGY

Operationalising Primary Stakeholder Management

Since 2000, the firm Reputation Measurement ('RepuTex') has been collecting data on socially responsible practices of Australia's top 100 firms (as measured by revenue) including banks, insurance companies, mining companies, car makers, energy companies, telcos, retailers and food manufacturers. The specific focus is on how effectively these Australian firms are responsive to and managing their stakeholders. The RepuTex categories include: 1) corporate governance; 2) employee management; 3) environmental performance; and 4) social impact. Corporate governance includes factors such as the ability to demonstrate ethical practices and governance mechanisms that foster transparency and open accountability to shareholders. For employee management, factors such as employment policies designed to nurture and retain employees and health and safety practices are included. For environmental performance, factors such as environmentally sound production techniques, evidence of sustainability practices and reduction in emissions and waste are included. For social impact, the degree to which firms positively impact society (e.g., philanthropy, safe products) is assessed. Ideally, we would like to have broader measures of primary stakeholder management; however, following Clarkson

(1995) and Starik (1995), we assert that the RepuTex categories, while not perfectly matched, serve as an adequate proxy for measuring primary stakeholder management in the Australian sample used in this study. Furthermore, the RepuTex categories are well suited to explore 'internal' primary stakeholders (corporate governance and employee management) and 'external' primary stakeholders (environmental performance and social impact), making the data applicable for testing our hypotheses.

Operationalising Firm Performance and Control Variables

Firm performance was measured using two accounting measures and one market-based measure. Return on assets (ROA) and return on equity (ROE) were chosen as they are common accounting measures used by the investment community to assess firm performance and are among the most widely used variables to measure firm performance in empirical research (Capon et al., 1996; Davis et al., 2000). However, in addition to traditional accounting measures of performance, Market Value-Added (MVA) was also included as it is a measure that captures relative success of firms in maximising shareholder value through the efficient allocation and management of scarce resources (Stern Stewart, 1996). MVA is defined as market value (number of shares outstanding x share price) - capital (debt and equity) employed in the firm. Thus, we captured relevant indicators of performance in that both traditional internal accounting measures as well as measures of market-based performance were analysed.

With respect to control variables, several measures were included. First, size is relevant as it is a variable that has been suggested to affect firm performance (Ullman, 1985). As a proxy of firm size, total assets and total sales were used. Second, differences among industries have long been acknowledged and discussed by scholars (Bain, 1959; Caves, 1972; Porter, 1980, 1991; Stoelhorst and van Raaij, 2004). In particular to this study, depending on its characteristics, an industry may or may not experience difficulties in effectively managing primary stakeholders;

thus, controlling for industry takes such differences into account. To do so, dummy industry variables were used. Third, some scholars surmise that 'slack resources' (e.g., profits) might determine the extent to which corporate executives invest in managing strategic dimensions of the firm's ability to compete, such as primary stakeholders (McGuire et al., 1988, 1990). To control for the effects of slack resources, net profit was used. Finally, based on accepted financial theory (Curley and Bear, 1979), the returns of a firm are influenced by the degree of their 'risk' as an investment compared with the returns of that of the overall market. To control for risk, beta values were used as they are a common measure of the sensitivity of a firm's share price in the context of overall fluctuations in a share market's composite average (Curley and Bear, 1979).

Data Collection

To collect the data on stakeholder management, RepuTex uses a variety of independent research teams such as academics experts, NGOs (non government organisations) and other non profit organisations and foundations that have a particular interest in how effectively and responsibly Australian firms meet stakeholder obligations. Criteria are developed by using a consultative approach with community groups, academics, government agencies and interested third parties relative to the market. Each assessor then rates a given company's performance against these criteria on a point system, utilising both high and low scores. Although research teams assign high and low scores, all scores are indexed to a common demarcation point (in our sample, the ratings were indexed to a 100 point system). Once the results are compiled and validated by RepuTex, they are then published and made available to the public. We used these publicly available scores as data points for measuring primary stakeholder management in the sample. All financial and market data (for the performance and control variables) were drawn from the FinAnalysis database.

We note that the RepuTex index does, of course, rely on the judgement of its assessors. However, it was chosen for this study for four key reasons: 1) each firm in the index is rated on how well it addresses multiple primary stakeholders, which is consistent with stakeholder theory; 2) each stakeholder category is assessed by independent researchers who are not affiliated with any of the rated firms; 3) firms are rated with an objective set of screening criteria, which is applied consistently across all companies; and 4) by using the RepuTex index, we created a multidimensional measurement which is important, as unidimensional (or aggregated) methods may mask the individual dimensions of primary stakeholder groups that could be equally important and relevant (cf. Lyndenberg et al., 1986; Wolfe and Aupperle, 1991).

Analysis

To analyse primary stakeholder management, scores were used from the year 2000. We chose the year 2000, as this is one of the few years that RepuTex has made available, to the public, the full and complete range of results from each assessor. However, because the RepuTex data for the year 2000 contained several private firms and missing data on some categories, the number of firms had to be revised from 100 to 38. The main reason for this adjustment was that a broad range of performance data needed to be captured from the FinAnalysis database, which offers financial data only on public firms. While the small sample size was beyond our control, we believe it serves as a good basis for exploratory research of primary stakeholder management in Australia.

To build the models for analysis, current year (2000) primary stakeholder management scores were included as independent variables, total sales and total assets (firm size) for the current year (2000) were included as control variables and net profit (slack resources), firm risk (beta value) and dummy industry variables (all for the year 2000) were also included as control variables. Subsequent year performance (2001) included three measurements (ROA, ROE,

MVA), which were used as the dependent variables. By using subsequent year performance, the 'lagged' effect of the primary stakeholder management efforts of firms was accounted for. We believe a lagged model between the independent and dependent variables is justified as primary stakeholder management is not expected to have an immediate effect on firm performance (Agle et al., 1999) and due to the data collecting procedure of the RepuTex index (RepuTex measures are not logged as specific timed behaviour during the reporting year). To test the relationship between primary stakeholder management and firm performance, we merged the RepuTex data with the FinAnalysis data for each of the 38 companies and used regression analysis to analyse the results. Table 1 provides descriptive statistics and correlations.

Means, Standard Deviations and Correlations

Variable	Definition	Mean	SD	1	2	3	4	5	6	7	8	9	10	11	12
1. ROA '01	Return on assets for 2001	4.83	3.61	1.00											
2. ROE '01	Return on equity for 2001	12.53	9.49	0.723**	1.00										
3. MVA '01	Market Value-Added for 2001	7370673.50 M$	11848988.79 M$	0.310*	0.505**	1.00									
4. TS '00	Total sales for 2000	8627545.80 M$	7776553.79 M$	-0.055	0.219	0.401*	1.00								
5. NP '00	Net profit for 2000	713256.71 M$	9606627.83 M$	-0.023	0.361*	0.728**	0.709**	1.00							
6. TA '00	Total assets for 2000	42209826 M$	78699807.23 M$	-0.435**	0.090	0.386**	0.512**	0.742**	1.00						
7. IND '00	Industry for 2000	42.38	19.66	-0.034	0.362*	0.015	0.058	0.152	0.317*	1.00					
8. Risk	Beta value for 2000	0.96	0.38	-0.405**	-0.366*	-0.033	0.210	0.263	0.423**	-0.187	1.00				
9. CG '00	Corporate governance for 2000	60.54	7.56	0.287*	0.161	-0.082	-0.077	-0.216	-0.203	0.289*	-0.411**	1.00			
10. EM '00	Employee management for 2000	72.29	7.90	0.346**	0.449**	0.356**	-0.015	-0.186	-0.069	-0.069	-0.270	0.156	1.00		
11. ENP '00	Environmental performance for 2000	33.32	5.06	0.147	0.004	-0.300*	0.178	0.055	-0.200	-0.054	-0.284*	-0.074	0.223	1.00	
12. SI '00	Social impact for 2000	45.17	6.68	-0.263*	-0.337**	-0.470**	0.261	-0.379**	0.136	-0.242	0.011	-0.037	-0.107	-0.090	1.00

* p <.05; ** p <.01

TABLE 1
Descriptive statistics and correlations

RESULTS

Table 2 presents the results of the regression analysis. For ROA, the model was significant ($p < .01$) with an adjusted R^2 of 0.522. For ROE, the model was significant ($p < .01$) with an adjusted R^2 of 0.574. For MVA, the model was significant ($p < .01$) with an adjusted R^2 of 0.661. While all models were significant, the association between each primary stakeholder category and performance was mixed; this is, the results indicated both positive and negative associations.

The association of the relationship between each primary stakeholder category and firm performance is of particular interest to this study.

TABLE 2

Regression results for the performance variables

Independent Variables	ROA '01 β	ROA '01 *t*	ROE '01 β	ROE '01 *t*	MVA '01 β	MVA '01 *t*
Constant		-0.606		0.323		-0.483
CG '00 (I)	0.272	1.774*	0.107	0.739	0.017	0.133
EM '00 (I)	0.268	1.873*	0.315	2.326**	0.378	3.131***
ENP '00 (E)	-0.039	-0.264	-0.185	-1.340	-0.231	-1.876*
SI '00 (E)	-0.266	-1.859*	-0.389	-2.882***	-0.122	-1.009
Total sales '00	-0.148	-0.830	-0.064	-0.379	-0.242	-1.609
Net profits '00	1.079	4.149***	1.132	4.608***	1.393	6.353***
Total assets '00	-1.010	-4.023***	-0.620	-2.617***	-0.452	-2.134**
Industry '00	0.168	1.083	0.403	2.761***	0.095	0.728
Risk '00	-0.100	-0.601	-0.292	-1.855*	-0.131	-0.933
R^2	0.652		0.690		0.753	
Adjusted R^2	0.522		0.574		0.661	
F	5.006***		5.947***		8.140***	

I = Internal primary stakeholder; E = External primary stakeholder
* p <.10; ** p <.05; *** p <.01

Table 2 demonstrates that corporate governance, one of two internal primary stakeholder categories, was significantly ($p < .10$) and positively associated with performance, namely ROA. Employee management, the second internal primary stakeholder category, was significantly and positively associated with ROA ($p < .10$), ROE ($p < .05$) and MVA ($p < .01$). Thus, Hypothesis 1 is supported, which stated that 'internal' primary stakeholders would be positively associated with firm performance. As with Hypothesis 1, Hypothesis 2 posited that 'external' primary stakeholders would be positively associated with firm performance. However, Table 2 shows that both external primary stakeholder categories, while significant, were negatively associated with firm performance. Specifically, environmental performance was significantly ($p < .10$) and negatively associated with MVA. Similarly, social impact was significantly and negatively

associated with ROA ($p < .10$) and ROE ($p < .01$). Given the negative association of these external primary stakeholders with firm performance, Hypothesis 2 is rejected.

As for the control variables, Table 2 shows net profit was significantly ($p < .01$) and positively associated with ROA, ROE and MVA. Firm size (total assets) was significantly (at either $p < .05$ or $p < .01$) and positively associated with ROA, ROE and MVA. Industry was significantly ($p < .01$) and positively associated with ROE and risk was significantly ($p < .10$) and negatively associated with ROE. Although total sales did not have a statistical association with performance, the findings with respect to the other control variables were consistent and in the expected direction.

DISCUSSION AND LIMITATIONS

The primary purpose of this study was to test the theory that managing primary stakeholders is a good strategy for positively affecting the bottom line. By studying 'internal' primary stakeholders (corporate governance and employee management) and 'external' primary stakeholders (environmental performance and social impact), some degree of confirmation that primary stakeholder management does affect the bottom line was found. Namely, internal primary stakeholders did have a significant and positive association with firm performance.

With respect to corporate governance, we would expect that firms who are perceived as being transparent, accountable and ethical are in a better position to establish a status for trustworthiness with shareholders than those firms who are not. According to several scholars, trustworthiness can be a source of competitive advantage (e.g., Barney and Hansen, 1994; Jones, 1995; Prahalad, 1997). On the other hand, employees can certainly be viewed as major stakeholders of any business and a firm who offers superior treatment to this internal stakeholder group is likely to enjoy strategic benefits. Our findings suggest that managing

employees as a primary stakeholder group and that acting responsibly towards them might be a means of positively impacting firm performance.

While the findings with respect to internal primary stakeholders were positive, the external primary stakeholder categories offered different results. Environmental performance, while significant, was negatively associated with MVA. This finding appears to be contrary to primary stakeholder theory; however, good environmental performance might not necessarily lead to advantages for firms or subsequent financial benefits. For example, in many industries environmental standards (e.g., pollution emissions) are set by governments or might even be voluntary. Here, firms are required by law to comply with the standards or enforce environmentally friendly practices of their own volition, out of a "social" conscience, which requires capital outlays for new equipment, facility updates and so on. While developing and managing environmentally friendly strategies, whether required by law or of voluntary effort, may be viewed as an act of social responsiveness towards the environment and community, the expenditure of scarce resources on this effort might, in fact, negatively impact firm performance, given other investment priorities.

Social impact, while significant, negatively impacted both ROA and ROE. The finding raises two important issues. First, is giving back to the community philanthropically, for example, in the best interest of the owners of the firm? That is, does philanthropy help to maximise profits? According to Friedman (1970), philanthropy should negatively impact performance. The reason being is that any use of shareholder funds beyond the strict means of making a profit is a misuse of those funds and a drain on corporate resources. That we found a negative association between social impact and firm performance lends some evidence to those who question the use of shareholder funds beyond any activity that does not strictly relate to making money (e.g., Levitt, 1958; Friedman, 1970; Lantos, 2002; Lantos and Cooke, 2003). Second, according to Birch and

Moon (2004), businesses in Australia predominately view ‘corporate social responsibility’ as the giving of profits to various social causes and community activities. If so, one would not be surprised to find that *profit spending* would have a negative impact on performance. On the other hand, not giving back adequately to local communities might be viewed by residents as socially irresponsible. Similarly, providing poor quality or unsafe products can also be viewed by the community as socially irresponsible. Both of these factors can negatively impact a firm’s performance because of a poorer image or reputation (cf. Waddock and Boyle, 1995; Wood and Jones, 1995; Altman, 1998). We further note that in our sample, the mean scores of environmental performance and social impact (Table 1), relative to corporate governance and employee management, are much lower, lending further evidence that poor management of external primary stakeholders might be detrimental to firm performance.

As with any empirical study, ours is not without limitations. First, the sample size is a limitation. Studying only 38 firms makes generalising the results difficult; thus, the results should be treated with caution. Future research, where primary stakeholder data are available, might explore much larger sample sizes in order to improve generalisability. Where larger sample sizes are possible, future research might also examine industries separately, thereby creating data for comparative purposes. Second, this study accounted for a one-year time lag. Further research could explore longer time lags in order to investigate if the effects of internal primary stakeholder hold consistently over time and if the effects of external primary stakeholder change over time (i.e., have a positive rather than negative effect on firm performance). Lastly, the RepuTex index is not without limitations. Most importantly, the index examines only the largest 100 firms (by revenue) in Australia, thereby limiting the scope of firm size. As stakeholder management is certainly not limited to large firms (Enderle, 2004), additional studies could include a sample of small and medium sized firms in order to compare and contrast the similarities and differences in

the effects of primary stakeholder management on firm performance across a range of firm sizes.

IMPLICATIONS AND CONCLUSION

Over the years, a variety of business strategies have been prescribed in the literature, strategies that can be pursued by firms in order to generate a competitive advantage. Specific to this study, primary stakeholder management is argued to be a business strategy that can generate bottom line benefits for the firm. The outcomes of our research suggest three key implications.

First, a pre-eminent question is whether or not primary stakeholder management 'pays'. Based on our findings, managing primary stakeholders appears to positively affect the bottom line—to a point. Investing in internal primary stakeholders, for example, seems beneficial in that such investments may be a means to create inimitable resources that cannot be easy matched by competitors, thereby leading to a competitive advantage. On the other hand, as our study demonstrates, investing in external primary stakeholders does not necessarily guarantee financial success. Here, investments may be more transactional in nature—ones that a competitor can copy relatively easily. Additionally, investments in external primary stakeholders might come at the expense of internal primary stakeholders thereby creating a cost to the firm that is detrimental to bottom line results. Thus, our findings imply that the overall effectiveness of a primary stakeholder management approach and its practicality from a management perspective may not align perfectly with theory.

Second, and specific to the first implication, we focus on the practicality of primary stakeholder management. Essentially, the requirements of managing internal and external primary stakeholders are likely to be very different. For example, the required investments to manage employees effectively are not the same as the required investments for generating outstanding environmental performance. Thus, although a goal may be to treat all primary stakeholders equally, in practice, meeting such a goal will likely be difficult and invokes complex decision-making for managers. Our research suggests that firms might be prioritising their investments in stakeholder groups based on their respective power (Donaldson and Preston, 1995; Mitchell et al., 1997; Agle et al., 1999; Frooman, 1999; Bourne and Walker, 2005), the implication being that if investments in stakeholder groups are viewed as mutually exclusive, the group that is perceived as offering the most benefit to the bottom line will be given priority (Gioia, 1999). In this sample, internal primary stakeholders appear to be more of a priority to managers than external primary stakeholders, although, as suggested, the consequences of poorly managing external primary stakeholders might have a harmful impact on firm performance.

Third, in a closely related field, corporate social responsibility (CSR), studies have largely focused on a single dimension of CSR or combined the CSR construct into an aggregated variable in order to test its association with firm performance (e.g., Russo and Fouts, 1997; Maignan et al., 1999). While positive associations have been found between CSR and performance in most cases, little is known about how the multiple dimensions of the construct affect performance separately. Thus, aggregated measures may mask the individual dimensions

that could be equally important and relevant. Similar to the CSR construct, primary stakeholder management is a multidimensional construct (Wolfe and Aupperle, 1991; Clarkson, 1995; Starik, 1995; Post et al., 2005; Zsolnai, 2006) and was treated as such in this study. As demonstrated, the results both confirm and challenge theoretical treatments of primary stakeholder management in the literature. Such findings offer opportunity to further refine theory while at the same time offer some practical implications for managers who are faced with complex decisions in the allocation of scare resources in an increasingly competitive global marketplace.

In conclusion, a fundamental question for corporate strategists to ask is whether or not primary stakeholder management 'pays'. Through the use of a secondary database well suited for testing the association between primary stakeholder management and firm performance, what we found was that this strategic approach can positively affect the bottom line, although the effects were not entirely as predicted. While internal primary stakeholders were positively associated with performance, external primary stakeholders were negatively associated. However, normatively, we do not suggest that firms entirely neglect external for internal primary stakeholders, but rather that they closely explore the opportunity costs of prioritising one group over the other. Ultimately, while theory posits that effectively balancing and managing the demands of all primary stakeholders should lead to optimal firm performance, our study suggests that finding such a balance may not be so easy.

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