

The spillovers of corporate misbehavior

ABSTRACT

Corporate scandals do not occur in isolation; the negative repercussions often extend beyond the offending firm, affecting innocent peers within the same industry. Our study demonstrates that when a firm's peers are involved in ESG-related scandals, the fallout can significantly diminish the valuation and financial performance of the firm, despite its lack of misconduct. Using firm-level data from 42 countries, we find that an average-magnitude scandal within an industry leads to a 1.95% equity value loss for unaffected firms in the following year. This decline is primarily driven by rising operational costs, suggesting that scandals disrupt supply chains and inflate costs across the industry. Additionally, firms impacted by their peers' scandals adopt more conservative strategies, increasing cash holdings and curtailing ESG investments. However, smaller firms and those with robust cash reserves exhibit greater resilience to these negative spillover effects.

Keywords: Corporate misbehavior, Corporate Social Responsibility, Spillover effect, Corporate reputation

JEL Classification: M10, M14, M21

1. Introduction

Financial contagion is a well-established phenomenon, demonstrating how market crashes and economic shocks seldom remain confined to their points of origin. When a crisis strikes, the ripple effects often cascade through industries, impacting firms with no direct exposure to the original shock. Prior research has extensively documented how financial linkages and supply chain dependencies can amplify these shocks, transferring financial distress from troubled firms to their peers (Allen & Gale, 2000). However, while much of the literature has focused on the transmission of financial risks and operational disruptions, there is growing evidence that reputational damage can also spread through industry networks, creating a new and underexplored channel of risk propagation.

The concept of peer effects in corporate finance has traditionally centered on the transmission of knowledge, strategies, and best practices across firms. Earlier research demonstrates that firms often learn from their industry peers, adopting successful practices and enhancing their competitiveness (Fresard, 2012; Bustamante and Fresard, 2021). This positive spillover effect highlights how knowledge transfer and strategic imitation can contribute to firm growth and resilience. However, less attention has been paid to the darker side of peer effects – specifically, how negative externalities such as reputational damage can also spread through industry networks. When a firm's peers engage in unethical behavior or become embroiled in scandals, the taint can extend to otherwise compliant firms, eroding their market value and financial performance.

One striking example of this phenomenon occurred during the Volkswagen emissions scandal in 2015. While Volkswagen bore the brunt of legal and financial penalties, peer firms within the automotive industry, including BMW and Daimler, also experienced negative stock market reactions, despite their lack of involvement in the scandal (Bouzzine and Lueg, 2020). This suggests that investors often reassess entire industries when scandals arise, leading to widespread declines in valuation. Such spillovers are not merely transient market reactions but can reflect deeper shifts in investor sentiment and operational realities, as industry participants face higher scrutiny, regulatory pressures, and potentially disrupted supply chains (Dyck et al., 2010).

The economic rationale behind these spillover effects is multifaceted. First, reputational damage can alter consumer behavior, reducing demand not only for the offending firm's products but also for those of its competitors (Gao et al., 2021). Second, scandals may disrupt supply chains and partnerships, as suppliers and distributors adjust their strategies to mitigate risk exposure (Hoberg and Phillips, 2010). These factors combine to create an environment in which even firms with sound governance and ethical practices suffer financial losses due to the actions of their peers. This is especially pronounced when scandals lead to calls for increased scrutiny from regulators, raising compliance costs for similar firms (Dyck et al., 2024).

Our study contributes to the literature by providing empirical evidence that scandals related to environmental, social, and governance (ESG) issues have far-reaching consequences for firms with no direct involvement in the misconduct. Using firm-level data from 42 countries, we introduce a novel measure of industry-level scandal exposure and analyze its impact on peer firms' valuation and financial performance. Our findings reveal that an ESG scandal of average magnitude within an industry results in a 1.95% loss in equity value for non-offending firms over the following year. This valuation drop is not merely a short-term market reaction but is accompanied by tangible financial consequences, including reduced profitability and increased operational costs.

Moreover, we document significant changes in the strategic behavior of firms impacted by their peers' scandals. Firms tend to adopt conservative financial strategies, such as increasing cash holdings and cutting back ESG investments. This shift suggests that firms perceive a heightened risk environment following industry scandals and respond by building financial buffers and reducing discretionary spending. Interestingly, we find that the severity of these effects varies with firm characteristics – smaller firms and those with stronger cash positions exhibit greater resilience, highlighting the importance of financial flexibility in navigating reputational crises.

Our findings reveal that the financial performance decline of firms affected by their peers' ESG scandals is primarily driven by increased operational costs rather than reduced sales. This distinction is critical to understanding the underlying mechanisms of reputational spillovers and their economic consequences. When an ESG scandal emerges within an industry, the immediate assumption might be that all firms in the sector would experience reduced sales due to diminished consumer trust (Newell and Goldsmith, 2001). However, our analysis suggests a more nuanced dynamic. While sales volumes remain relatively stable, peer firms face escalating costs related to compliance, operational adjustments, and risk management (Nunes and Park, 2016; Nunes et al., 2020; Singh and Hong, 2020; Fu et al., 2024). These dynamics could disrupt the normal flow of goods throughout the supply chain (Singh and Hong, 2020), ultimately affecting financial performance on the demand side (Zsidisin et al., 2016). These incremental costs are not merely incidental but represent a significant financial burden that directly impacts profitability and valuation.

In the sections that follow, we outline our empirical strategy, present our findings, and discuss the broader implications of our research. By shedding light on the spillover effects of ESG scandals, we contribute to a deeper understanding of how reputational risks propagate through industry networks, influencing firm behavior and market outcomes even in the absence of direct misconduct.

2. Hypothesis Development

The literature documents that corporate scandals undermine the value of competitor firms (Cole et al., 2021). For example, Bouzzine and Lueg (2020) report that Volkswagen's diesel emissions scandal provoked a significant decrease in the stock prices of industry peers, and that this response was more pronounced than the fall in the price of Volkswagen shares itself. An and Xu (2021) investigate whether the Harvey Weinstein harassment scandal affected the firm value of companies within the entertainment industry and find that peer firms exhibited an average daily loss of 1.5% in stock price during the event window. This contagion effect is also documented by Lins et al. (2024) in a study covering the same scandal. Focusing on the automobile industry, Liu and Varki (2021) investigate the spillover effect of product recalls on competitors and report a negative influence on the market value of peer firms. A possible explanation for this behavior is given by signaling theory, as the leak of corporate misconduct could reveal the underlying risks of its environment (Zou et al., 2015). Since, according to mimetic isomorphism (DiMaggio and Powell, 1983), peer firms tend to adopt similar practices, this extends to corporate irresponsibility (Dorfleitner et al., 2022). Hence, we expect a negative relation between misconducts and competitors' equity value.

The literature on corporate scandals also reports that the negative influence of misconduct further reverberates into fundamentals, undermining firms' profitability (Aoudi et al., 2018; Cole et al., 2021) through two main channels. First, a decrease in sales, as customers may avoid the unethical firm due to moral concerns (Nardella et al., 2023), compliance risks (Fu et al., 2024), or a decline in credibility (Newell and Goldsmith, 2001), leading to reduced market participation (Cumming et al., 2015). The second channel is an increase in costs, as a bulk of studies report that corporate irresponsibility harms the supply chain (Nunes and Park, 2016; Nunes, 2018; Nunes et al., 2020; Iborra and Riera, 2022). Since our focus is on peer firms, we argue that sales dynamics is not the most auspicious channel to explain the deterioration in competitors' financial performance. It is more likely that peer firms would benefit from the decrease in market participation of unethical firms, as documented by Zeume (2017). On the other hand, as suppliers are negatively affected by scandals, this practice could have harmful consequences for the supply chain, bringing instability to the regular flow of goods and services (Singh and Hong, 2020) and ultimately increasing industry costs. Consequently, we argue that the negative influence of corporate misconduct on peer firms' profitability is more plausibly explained by increased costs rather than decreased sales. Accordingly, we hypothesize that:

H1: Firms experience a deterioration in financial performance when their industry peers are involved in ESG-related scandals, primarily due to increased operational costs rather than weakened sales.

As misbehavior brings negative outcomes for peer firms, it is plausible to expect that competitors would act to mitigate the harmful consequences of rivals' practices. In this context, Aoudi et al. (2018) report that ESG practices act as insurance against the negative effects of corporate social responsibility, which could be understood as an effort to reestablish a firm's reputation (Perks et al., 2013; Karmani et al., 2024). This behavior is consistent with the evidence from Ferrés and Marcet (2021), who document that firms tend to increase their investments in corporate social responsibility after being involved in misconduct. The authors also find that this effort is associated with lower fines and a less pronounced decrease in sales. Consequently, we expect a positive relationship between misconduct and the ESG practices of non-offending firms.

Cash holdings are another source of protection against the negative outcomes of scandals. For example, Thakur and Kannadhasan (2019) and Tran (2020) document that firms with higher cash holdings tend to be less affected by misconduct, as they have more liquidity to cover legal penalties and greater financial flexibility to navigate a more turbulent future (Dorfleitner et al., 2022; Banerjee et al., 2022; Dorfleitner and Kreuzer, 2024). Accordingly, we predict a positive influence of scandals on future cash holdings of peer firms. Regarding capital expenditures (Capex), previous studies report that misconduct increases the cost of capital (Banerjee et al., 2022) and limits funding sources (Cumming et al., 2015; An and Xu, 2021), which could potentially affect a firm's ability to invest in long-term projects. Based on this precautionary approach, we forecast that misconduct is negatively associated with future Capex of peer firms. For these reasons, our second hypothesis is as follows:

H2: Firms adopt a more precautionary financial approach—characterized by increased cash holdings, reduced capital expenditures, and increased ESG investments—following ESG-related scandals involving their industry peers.

3. Data and Methodology

3.1 Sample definition

The primary source of our data is the LSEG database, formerly Refinitiv, which is widely used in the study of corporate misconduct due to its comprehensive ESG Controversies Scores (Dorfleitner et al., 2022; Komath et al., 2023; Dorfleitner and Kreuzer, 2024). Our global dataset covers 110,890 firm-year observations for 5,980 different companies, excluding financial firms, located in 42 countries over the period from 2002 to 2023. From this sample, we exclude firms without ESG Controversies Scores data, resulting in the loss of 49,565 firm-year observations. Since our focus is on “ethical” firms, we apply an additional filter to retain only firms without controversies in a given

year. This screening eliminates another 11,060 firm-year observations. The final sample consists of 50,265 firm-year observations for 5,970 non-financial firms from 42 countries.

Table 1 presents the sample composition by country. As expected, U.S. firms dominate the sample, representing 27.12% of the firm-year observations, followed by Japan (12.07%), Hong Kong (6.22%), and the U.K. (5.08%). Given the diverse socio-economic backgrounds of the sampled countries and the geographical dispersion of firms, it is unlikely that our estimates are biased by regional idiosyncrasies. However, the higher representation of developed countries raises the question of whether the results are driven by these economies, as institutional quality plays an important role in corporate misconduct (Groening and Kanuri, 2013; Zeume, 2017; Banerjee et al., 2022; Dorfleitner et al., 2022; Kathan et al., 2025). In the robustness section, we examine this possibility and find no support for this alternative explanation. The next subsection describes how we measure our central dependent variable.

(Table 1)

3.2 Scandal magnitude measures

We use the ESG Controversies Score as our primary measure of the magnitude of corporate scandals within an industry. This score, provided by LSEG, is based on 23 ESG-related scandal topics, with recent controversies reflected in the latest complete period (LSEG, 2023). It considers the number of scandals involving a firm during a fiscal year, based on well-established media sources such as Bloomberg and the Wall Street Journal. If a firm is involved in a scandal that affects multiple topics, the different affected topics are accounted for, increasing the severity of the scandal in the score. Consequently, the gravity of the scandal is captured not only by media coverage intensity but also by the extent of ESG topic violations. Given that large firms plausibly attract more media attention, the firm's market capitalization is considered in the score's composition. Companies with no scandals in a given year receive a score of 100, which diminishes to as low as 0 depending on the gravity of the scandal. Only firms with a score of 100 in a given year are retained in the final screening described in the previous subsection.

Since our focus is on the spillover effects of corporate misconduct on competitor firms, we develop a measure to capture the magnitude of scandals within an industry in each country, as expressed in Equation (1):

$$Scandal\ Magnitude_{i,j,t} = 100 - \frac{\sum Controversies\ Score_{s,i,j,t}}{N_{i,j,t}} \quad (1)$$

where $Controversies\ Score_{s,i,j,t}$ is the ESG Controversies Score from LSEG for firm “s” in industry “i”, country “j” and year “t”. $N_{i,j,t}$ is the number of firms in industry “i”, country “j” and year “t”. The re-scaling aims to provide a more intuitive interpretation of the severity of scandals, where higher values represent more severe events. Since this continuous variable considers the number of firms with controversies within an industry, it allows us to compute the severity of the scandal in terms of ubiquity, an essential aspect when examining contagion effects. The following example illustrates this intuition. Suppose that a set of four firms in the same country-industry exhibits the ESG Controversies Score of 60 (Firm A), 40 (Firm B), 100 (Firm C) and 50 (Firm D). In this case, the Scandal Magnitude is 37.5 ($100 - \frac{60+40+100+50}{4}$). We calculate this measure using both scandal and no-scandal firm-year observations but retain only the latter in our final sample, as previously mentioned.

To illustrate which industries are more severely affected by corporate misbehavior, Panel A of Table 2 reports the mean Scandal Magnitude across industries, with the top 10 highlighted in italics. The automobile sector is the most affected by scandals. As expected, industries related to extractive activities (e.g., oil and mining) also appear in the upper part of the ranking, along with some less intuitive sectors such as media and leisure services. In Panel B, we present the mean Scandal Magnitude for each country. The fact that most of the countries in the top 10 list are developed economies with high levels of institutional pressure aligns with previous studies documenting that societies with high moral standards are more likely to monitor corporate behavior, facilitating the detection of corporate misconduct (Nardella et al., 2020; Banerjee et al., 2022; Dorfleitner et al., 2022; Dorfleitner and Kreuzer, 2024). This evidence also supports the observation that countries with low institutional quality occupy the bottom part of the ranking.

(Table 2)

In an alternative design, we replace the *Scandal Magnitude* $_{i,j,t}$ by the share of scandal firms (i.e., ESG Controversies Score < 100) in a given country-industry as our central variable. We find that the results remain consistent, as detailed further in the paper. Figure 1 presents the mean Scandal Magnitude during our sample period (solid line, left axis) alongside the mean share of scandal firms in a given country-industry (dashed line, left axis) and the absolute number of scandals per year (columns, right axis).

(Figure 1)

The figure indicates that the magnitude of scandals within industries showed a decreasing trend until 2021 but began rising again in the last couple of years. This decreasing trend contrasts with the increase in the absolute number of scandals. However, the rise in the number of scandals can be explained by the expansion of the LSEG database over time. In relative terms (i.e., the share of scandal firms represented by the dashed line), the number of scandals per industry is decreasing. This pattern suggests that using our measure of scandal magnitude is more consistent than relying solely on the absolute number of scandals to investigate corporate misbehavior.

We now address the peculiar increase in all measures of corporate scandals during the last two years of our sample period. This behavior can be explained by the fact that LSEG counts recent controversies in the latest closed fiscal year (LSEG, 2023). For example, if the last fiscal year available for a firm is 2022 and controversies arise in 2023, these controversies are included in the 2022 score. Once the fiscal year for 2023 is completed, the corresponding controversies are then assigned to that year. This procedure leads to a concentration of scandals in recent years, justifying the spike in their number. To address this, in the robustness section we run the main analysis excluding observations from the last couple of years and find that the results remain unchanged.

3.3 Empirical model

We employ the following model for our baseline tests:

$$Y_{s,i,j,t} = \alpha_0 + \alpha_1 \text{Scandal Magnitude}_{s,i,j,t-1} + \sum \alpha_2 \text{Controls}_{t-1} + \text{Industry Dummies} + \text{Country Dummies} + \text{Year Dummies} + \varepsilon_{s,t} \quad (2)$$

where $Y_{s,i,j,t}$ represents a series of variables related to financial performance, namely: Market Capitalization, Tobin's Q, Return on Equity, Operating Profit and Sales Growth of firm "s" of industry "i" in country "j" and year "t". We employ a series of firm-level control variables aiming to reduce endogeneity. These variables are the following. Size, as larger firms are more likely to attract media attention related to firms' misbehavior (e.g. Drempetic et al., 2020). Leverage, as firms more dependent on external capital tend to constrain unethical behavior since scandals can limit access to financial markets (e.g., Dorfleitner et al, 2022). Return of Asset, given that firms with poor recent financial performance are more inclined to abandon ethical behaviors (e.g., Campbell, 2007). Number of analysts, since enhanced scrutiny tend to reduce corporate misconduct (e.g., Aouadi and Marsat, 2018). Finally, Selling, General and Administrative Expenses (SG&A) since scandal-prone firms

often invest more in advertising and marketing campaigns to reinforce their reputation (e.g., Perks et al., 2013). A detailed definition of these variables is available in Appendix A, Table A.1, while the correlation among these variables is presented in Table A.2 of the same appendix. Notably, the highest VIF among the control variables is 1.91, indicating that our estimates are not biased by multicollinearity. All variables are winsorized at the 2% and 98% levels to control for outlier effects. In the model, we include Industry and Country Dummies because corporate scandals vary across industries and are sensitive to institutional quality (e.g., Dorfleitner et al., 2022; Tan et al., 2024), as suggested by the results reported in Table 2.¹

3.4 Summary statistics

In Table 3, we present the summary statistics of the key variables after winsorization. Corporate scandals are not a dominant behavior within industries, as more than half of the Scandal Magnitude observations exhibit a null value. At the country level, however, misbehavior is more common and dominates the distribution. The sample is also dominated by profitable firms with growing sales, which are more commonly funded by own capital. Finally, it is worth noting that the main variables exhibit moderate dispersion, suggesting that our findings are not driven by outliers.

(Table 3)

4. Empirical results

4.1 Peers' firm values

In our first empirical exercise, we analyze whether corporate misconduct affects competitors' firm value. In this regard, we employ Market Capitalization and Tobin's Q as dependent variables in separate models. Following related literature (Edmans, 2011; Aouadi and Marsat, 2018; Komath et al., 2023), these are defined, respectively, as the natural logarithm of Market Capitalization and the ratio between Market Value and Book Equity. Table 4 presents the results for the baseline model. We also add an alternative framing that excludes control variables to provide a sensitivity analysis to investigate whether our central findings are biased by model specification.

(Table 4)

¹ In the baseline model, we estimate the parameters with clustered standard errors at the individual level. In an unreported test, we use industry-level clustering and find that the results remain consistent.

The estimates from the baseline models (3) and (7) indicate that corporate misconduct is associated with a future decrease in peers' firm value, as the coefficients of the Scandal Magnitude are highly significant (t-statistics of -5.34 and -9.02, respectively). This relationship is also economically meaningful, as an average scandal produces a 1.95% decrease in competitors' Market Capitalization in the following year.² This influence is of a similar magnitude to the findings of Dyck et al. (2024), who estimate that corporate fraud destroys 1.60% of equity value annually.

In models (4) and (8), we estimate the parameters using firm fixed effects to control for invariant idiosyncratic factors omitted in the baseline model that could potentially affect the results. The coefficients of the central variable remain significant under this approach (t-statistics of -8.63 and -5.25, respectively). In general, the control variables exhibit the expected relationship with Market Capitalization, as larger, less indebted, and more profitable firms display higher market values. Finally, the estimates of the univariate models (i.e., without control variables) in columns (1), (2), (5) and (6) indicate that the negative influence of scandals on peer firms' value that we document is not driven by model specification.

These results suggest a spillover effect of corporate scandals toward socially responsible firms at both the industry level. Previous studies focusing on specific events have already documented the contagion effect of corporate scandals (Ivaschenko, 2004; An and Xu, 2021; Lins et al., 2024). Our findings add to this literature by demonstrating that this effect is ubiquitous, given the extensive geographical coverage and breadth of misconduct captured by our dataset. The spillover effect could be attributed to reputational loss from stakeholders' perspectives, driven by fears that competitors may also engage in unethical practices (Nunes and Park, 2016; Liu and Varki, 2021), possibly due to mimetic isomorphism (DiMaggio and Powel, 1983; Dorfleitner et al, 2022). If this is the case, it would be plausible to expect that the negative influence of peer scandals is not limited to firm value but also reverberates in firms' fundamentals. The next subsection explores this perspective.

4.2 Peers' financial performance

To investigate the influence of scandals on the performance of competitor firms, we employ ROA, Operating Profit, and Sales Growth as the dependent variables in our baseline model. Evidently, when using ROA as the dependent variable, we omit the homonymous lagged parameter of the baseline

² Since the Scandal Magnitude distribution contains several observations equal to zero, we cannot use the mean value from the descriptive statistics as a proxy for an average scandal. Instead, we must exclude the null values (i.e., no-scandal observations) and then calculate the average of the remaining observations. By doing so, the mean Scandal Magnitude is 0.107. We then multiply this value by 0.183 to obtain the economic significance of 1.95%

model. For all dependent variables, we expect a negative relationship with lagged scandals. The results are presented in Table 5.

(Table 5)

In the case of ROA and Operating Profit, there is a negative influence of scandals within the industry (t-stat of -2.72 and -3.92, respectively), which is also observable in the alternative specification that accounts for firm fixed effects (Models (4) and (8)). This suggests that corporate misbehavior brings negative economic outcomes for peer firms, undermining their financial performance. However, this effect does not appear to provoke a decrease in sales. For all models employing this dependent variable, the Scandals coefficient is significant only in one (Model (12)) and only at a moderate level of 10%. Finally, we observe that all the results are observable in the models without control variables, what indicates that the pattern here reported are not driven by model specification.

The literature on corporate scandals well establishes that firm misconduct undermines financial performance (Cumming et al., 2015; Price and Sun, 2017; Aouadi and Marsat, 2018; Cole et al., 2021; Tan et al., 2024). Our results extend these findings by demonstrating that corporate misbehavior also negatively affects the profitability of competitor firms. In the next subsection, we explore whether the results so far are driven by the way we define our central variable.

4.3 Alternative specification: share of scandal firms

The continuous variable Scandal Magnitude that we introduce offers the advantage of exploring the influence of corporate misconducts of varying magnitudes and natures in more comprehensive contexts, addressing the generalization issue present in previous studies that focus on specific events. However, a plausible concern when proposing new measures is whether the results are driven by the way the variable is defined. Additionally, this approach limits comparisons with similar studies. To address these concerns, we employ an alternative definition for our central independent variable. Specifically, we examine the spillover effect of scandals using the proportion of firms with misconducts within an industry in each country and year, consistent with previous studies that use the number of scandals as the central variable (Nardella et al., 2020; Dorfleitner et al., 2022; Dorfleitner and Kreuzer, 2024). Table 6 presents the results.

(Table 6)

Overall, the results align with the patterns previously documented. The proportion of scandal firms is negatively related to firm value dynamics. For financial performance measures, the negative effect of corporate scandals on peer firms is more pronounced for operational margins but remains significant at 5% level when using ROA as the dependent variable. Additionally, the lack of a significant impact on competitors' sales persists when using this alternative specification. The fact that Operational Profit is the most affected financial performance variable, while Sales Growth remains unaffected by scandals, suggests that increases in costs and/or expenses are the channel through which firm performance is impacted. This possibility is examined in greater depth in the next subsection.

4.4 Do corporate scandals affect costs and expenses of peer firms?

Since competitors' sales are not affected by corporate scandals, the explanation for why their operational margin decreases lies in the increase of costs and/or expenses. The positive influence of scandals on these variables is plausible. First, in the case of costs, the literature reports that suppliers are especially affected by negative corporate events (Iborra and Riera, 2023; Nunes, 2018; Xie et al., 2023), which could undermine their operational performance, influencing their supply of goods and services and leading to supply chain contamination (Nunes, 2018; Xie et al., 2023; Yang and Zou, 2025). Regarding expenses (i.e., SG&A), previous studies document that firms tend to increase their investments in marketing and sales after a corporate scandal to reestablish their reputation (Perks et al., 2013; Karmani et al., 2024). In this case, it is rational to expect that peer firms, given the contagion effect documented, could also increase their SG&A expenses as a precaution against reputational loss. Finally, there is evidence that scandal firms tend to increase ESG-related investments after scandals (Ferrés and Marcet, 2021), either as an expectation of more scrutiny from stakeholders and regulators (Dorfleitner et al., 2022) or as an effort to recover their reputation (Karmani et al., 2024). This could potentially affect both costs and expenses of peer firms. To address this, we employ COGS (Cost of Goods and Services) and SG&A, in both cases scaled by Sales, as our dependent variables in two specifications of our baseline model. The estimates are presented in Table 7. Evidently, when using SG&A as the dependent variable, we omit the homonymous lagged parameter of the baseline model.

(Table 7)

We find a positive influence of scandals on COGS, observable in both random-effects (Models 1 and 3) and individual fixed-effects (Models 2 and 4) estimations, and for both specifications of our

central variable. In all cases, this relationship is significant at the 1% level. However, we do not find that corporate misbehavior significantly affects SG&A expenses of peer firms. These results suggest that the escalation in costs is the channel through which competitors' performance is undermined, which is in line with the literature documenting that corporate misconducts have a spillover effect on the supply chain (Nunes, 2018; Yang and Jiang, 2024; Yang and Zou, 2025) and in accordance with H1. The literature on the contagion effect of scandals on supply chain argues that the fall in firm value of providers is provoked by an expectation of lower future cash flows due to a higher uncertainty of the future demand (Nunes et al., 2020) and to the need to realign their operation as a response to the new scenario (Nunes and Park, 2016). This response could plausibly affect the regular flow of goods and services throughout the supply chain in different dimensions (e.g. price, quality, offer), ultimately affecting the financial performance of customers (Zsidisin et al., 2016; Singh and Hong, 2020).

The fact that we do not find that SG&A are affected by peer scandals indicate that the increase in marketing and sales expenses as an effort to reinforce firms' reputation after a scandal (Perks et al., 2013; Karmani et al., 2024) is not observed when the misconduct affects competitors.

4.5 Scandals and peers' investment decisions

Since scandals seem to bring negative outcomes for competitors, in this subsection we investigate whether corporate misbehavior influences the investment decisions of peer firms as a response to the consequences brought by these events. In this regard, we focus on three dimensions of corporate investments: ESG practices (i.e., investment in intangibles), cash holdings (i.e., short-term investments), and Capex (i.e., long-term investments). Motivated by the literature reporting that ESG scores (Price and Sun, 2017; Aouadi and Marsat, 2018; Ferrés and Marcet, 2021) and cash holdings (Tran, 2020; Banerjee et al., 2022) attenuate the effect of corporate misconduct, we expect a positive relation between these variables and lagged scandals, which would indicate that competitors aim to mitigate the effect of misbehaviors through these channels. In the case of Capex, we expect a negative relation, since corporate scandals tend to increase the cost of capital (Karpoff et al., 2005; Cumming et al., 2015; Banerjee et al., 2022), eventually affecting the capacity of firms to conduct long-term investments (Martinez-Conesa et al., 2017). In this regard, we employ ESG Score growth, cash and cash equivalents (scaled by total assets), and Capex (scaled by total assets) as our dependent variables in the baseline model.³ Table 8 presents the results.

(Table 8)

³ The ESG data is the ESG Score informed by LSEG.

The results reveal that, contrary to our expectations, peer firms are more likely to decrease their ESG practices after an industry-level scandal (t-stat = -2.42). This suggests that firms with no misconduct do not feel compelled to improve their reputation in response to a competitor's scandal, presumably because the misbehavior in question harms the image of the offending firm rather than the industry's overall reputation. On the other hand, we observe an increase in cash holdings following these events (t-stat = 2.64), suggesting that firms adopt a more conservative approach to cash management as a precaution against potential turbulence ahead (Hugonnier et al., 2015; Thakur and Kannadhasan, 2019; Tran, 2020), considering the spillover effects of corporate scandals. Finally, we do not find a significant relationship between corporate controversies and future long-term investments of peer firms (t-stat = -0.32). A possible explanation is that the documented increase in the cost of capital for scandal-affected firms does not extend to the broader industry and, consequently, does not influence the long-term investment decisions of competitors. Taken together, the results indicate that managers of competitor firms adopt a cautious approach to short-term investment decisions in the aftermath of a scandal. Consequently, the evidence in this section partially confirms H2.

4.6 Moderator effect of firms' characteristics on scandals spillovers

In this last empirical exercise, we examine whether firms' characteristics exert a moderator effect on the scandal spillovers. Motivated by previous studies, we investigate whether ESG scores, cash holdings, and size attenuate the influence of scandals on peer firms. Aouadi and Marsat (2018) document that firms with higher ESG scores are less affected by corporate scandals, arguing that ESG practices serve as an insurance against negative corporate social responsibility news. In the case of cash holdings, Ferrés and Marcet (2021) document that corporate misconducts tend to be less harmful for firms with more short-term investments, since by holding more cash, they are less exposed to funding shortages that commonly move in tandem with scandals (Cumming et al., 2015). Finally, as large firms tend to attract more attention from traditional media and market participants (Dorfleitner et al., 2022), it is plausible to believe that they are more affected by scandals in their industries.

In this regard, we introduce in our baseline model a dummy variable that equals 1 for firms with ESG Scores (or cash holdings or size) above the median each year and 0 otherwise. The new specification is as follows:

$$\begin{aligned}
Y_{s,i,j,t} = & \alpha_0 + \alpha_1 D_{s,t-1} \cdot \text{Scandal Magnitude}_{s,i,j,t-1} + \alpha_2 (1 - D_{s,t-1}) \cdot \text{Scandal Magnitude}_{s,i,j,t-1} \\
& + \sum \alpha_3 \text{Controls}_{t-1} + \text{Industry Dummies} + \text{Country Dummies} \\
& + \text{Year Dummies} + \varepsilon_{s,t}
\end{aligned} \tag{3}$$

our focus is on coefficients α_1 and α_2 , as the contrast among them would indicate the moderator effect, if any, of the variable under scrutiny. The results are presented in Table 9. For brevity, we omit the estimates for the control variables. For the same reason, we do not include the coefficients for the alternative specification of our central variable, which is based on the proportion of scandal firms. These results are available in Appendix A.4 and are consistent with the baseline model's estimates.

(Table 9)

We start by examining the moderator effect of ESG scores. The negative influence of corporate scandal on the firm value of competitors is significant for firms with high and low scores, whereas the difference among the coefficients (-0.540 and -1.029) is statistically nonsignificant (p-value 0.15). In the case of financial performance, the influence is mixed, as the ROA of high ESG firms is less affected by peer scandals, whereas their operational profit decreases more after these events (t-stat -5.32). Based on these blurred results, we conclude that ESG score does not represent a pivotal role in reducing the spillover effect of corporate misconduct.

We now move to cash holding effects. In general, firms with more cash tend to suffer less from industry scandals since the impact of these events on firm value and profitability (i.e., ROA and operating margin) is less pronounced when compared with firms holding fewer short-term investments. This pattern is also observable in sales, as companies with more cash holdings are more likely to increase their sales after peer scandals, which suggests that, under some circumstances, scandals can partially benefit competitors (Zeume, 2017). This moderator effect also indicates that the increase in cash holdings of peer firms after these events, documented in the previous subsection, seems to be a consistent managerial decision that indeed attenuates the impact of competitor scandals on firm performance.

Finally, the results in the bottom part of Table 9 reveal that large firms are especially affected by industry scandals, since, for these companies, all financial parameters are significantly affected by these events. In contrast, in the case of small firms, only the operational profit seems to be undermined by peers' misconducts. The pivotal role of size is particularly interesting in the case of sales. Whereas competitors' scandals are linked with future decreases in sales of large firms (t-stat -4.08), these events seem to produce an increase in revenues of small companies (t-stat 2.68). Taken together, these

findings support the view that firms' visibility is an important factor in the realm of corporate misconducts, even when more visible firms are not the main actors behind the scandal.

5. Robustness checks

5.1 Filtering recent controversies

As mentioned in the methodology section, the ESG controversies score incorporates recent scandals from the last fiscal year reported. When there is a lag between the release of the fiscal year's results and the publicity of the scandal, this procedure could possibly distort the relationship examined here in more recent years. To verify if this procedure biases our results, we exclude the last two years of our dataset and run the previous empirical exercises. The main results are summarized in Table 10.

(Table 10)

The main patterns remain virtually unchanged by the exclusion of recent observations. There is a negative influence of industry scandals on firm value (i.e., Market Capitalization and Tobin's Q), as well as on ROA (t-stat -2.40) and profit margin (t-stat -4.49). Once again, the decrease in profitability seems to be attributed to the increase in costs observed after these events (t-stat 4.20). Finally, we still observe that, on average, the sales growth of competitors is not harmed by corporate misconduct.

5.2 Geographic dispersion

The literature on corporate scandals reports that institutional quality plays a central role in the visibility and outcomes of firm misconducts. In general, countries with higher press freedom (Dorfleitner et al., 2022), stronger regulatory frameworks (Tan et al., 2024), those located in more developed countries (Dorfleitner and Kreuzer, 2024), and those with higher corruption control (Banerjee et al., 2022) are more likely to monitor and punish unethical practices. Since our dataset is geographically dispersed, compressing countries with distinct institutional quality, it is plausible to conjecture whether the spillover effect documented here is found among countries with different socio-economic characteristics. To address this, we divide our sample into G7 and non-G7 countries, as more developed economies tend to display similar institutional environments. Furthermore, this design allows us to examine whether the central results are driven by outlier countries that dominate

the sample, as G7 countries account for 54.6% of our firm-year observations. Table 11 shows the estimates.

(Table 11)

The results demonstrate that the main features of the contagion effect of scandals on the industry are observable in both subgroups, as misconducts are linked with future decreases in firm value and financial performance of competitors. Even though, in light of previous studies, institutional quality can possibly influence the magnitude of the effect, our results indicate that it does not play a pivotal role in this regard.

6. Conclusion

We investigate the spillover effects of corporate scandals on peer firms with no misconduct. In this effort, we introduce a new continuous variable designed to capture the magnitude of corporate misconduct the industry level, using the ESG Controversies Score from LSEG. Based on a sample of 50,265 firm-year observations covering 5,970 non-financial firms from 42 countries, our results indicate that scandals provoke a decrease in competitors' firm value. More specifically, we document that an industry scandal of mean magnitude is associated with a decrease of 1.95% in the equity value of peer firms in the following year. We also find that the profitability of competitors is undermined after these events. Our results indicate that this deterioration is driven by the rise in Costs of Goods and Services, which significantly increase after scandals, suggesting that the supply chain is a relevant actor in the contagion effect of corporate misconduct. Moreover, we also report that competitors are more likely to increase cash holdings and to decrease ESG investments and Capex after these events. Finally, small firms and companies with more cash holdings tend to be less affected by industry scandals.

To the best of our knowledge, our study is the first to document, at a large scale, that corporate scandals bring harmful outcomes to competitors, even when peer firms do not display unethical behaviors. Consequently, our findings have important implications for policymakers and researchers interested in the consequences of corporate social irresponsibility. Our study is also of interest to managers, as we provide evidence of managerial decisions that can possibly attenuate the impact of peers' misconduct. Finally, it is worth noting that our results have limitations. The literature documents that the effects of corporate misbehavior on firm performance are complex and sensitive to country, industry, and firm-specific idiosyncrasies. Consequently, it is plausible to presume that

the spillover effect documented here varies across these dimensions. Therefore, investigating whether these factors influence this phenomenon is a promising agenda that we leave for future work.

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Table 1: Geographic dispersion of sampled firms

The table shows the number of firms per country and the representativeness of each country in terms of firm-year observations. The sample period is from 2002 to 2023.

No	Country	# of firms	% sample	No	Country	# of firms	% sample
1	Argentina	22	0.29%	22	Japan	474	12.07%
2	Australia	251	4.47%	23	South Korea	154	2.57%
3	Austria	20	0.43%	24	Malaysia	158	1.54%
4	Belgium	36	0.69%	25	Mexico	42	0.67%
5	Brazil	103	1.77%	26	Netherlands	34	0.61%
6	Canada	256	4.97%	27	New Zealand	45	0.82%
7	Chile	32	0.64%	28	Norway	68	0.97%
8	China	257	4.46%	29	Philippines	30	0.52%
9	Czech Republic	2	0.02%	30	Poland	25	0.41%
10	Denmark	35	0.81%	31	Portugal	12	0.23%
11	Finland	47	0.85%	32	Saudi Arabia	58	0.48%
12	France	119	2.26%	33	Singapore	71	1.33%
13	Germany	127	2.14%	34	South Africa	72	1.33%
14	Greece	19	0.35%	35	Spain	50	0.98%
15	Hong Kong	338	6.22%	36	Sweden	185	2.85%
16	Hungary	4	0.08%	37	Switzerland	84	1.76%
17	India	576	3.40%	38	Thailand	114	1.32%
18	Indonesia	56	0.90%	39	Turkey	76	0.92%
19	Ireland	10	0.16%	40	United Arab Emirates	35	0.24%
20	Israel	18	0.24%	41	United Kingdom	224	5.08%
21	Italy	75	1.01%	42	United States of America	1,748	27.12%

Table 2: Mean scandal magnitude per Industry and Country

This table shows the mean scandal magnitude for each Industry (Panel A) and Country (Panel B). The sample period is from 2002 to 2023.

Panel A: Scandal Magnitude per Industry			
GICS Industry Name	Mean Scandal Magnitude	GICS Industry Name	Mean Scandal Magnitude
<i>Automobiles</i>	<i>0.140</i>	Leisure Products	0.050
<i>Technology Hardware, Storage & Peripherals</i>	<i>0.129</i>	Textiles, Apparel & Luxury Goods	0.050
<i>Interactive Media & Services</i>	<i>0.122</i>	Professional Services	0.050
<i>Aerospace & Defense</i>	<i>0.110</i>	Chemicals	0.048
<i>Communications Equipment</i>	<i>0.093</i>	Ground Transportation	0.047
<i>Oil, Gas & Consumable Fuels</i>	<i>0.086</i>	Commercial Services & Supplies	0.046
<i>Metals & Mining</i>	<i>0.084</i>	Electrical Equipment	0.046
<i>Hotels, Restaurants & Leisure</i>	<i>0.078</i>	Machinery	0.044
<i>Passenger Airlines</i>	<i>0.077</i>	Diversified Consumer Services	0.043
<i>Consumer Staples Distribution & Retail</i>	<i>0.073</i>	Personal Care Products	0.042
Health Care Equipment & Supplies	0.071	Wireless Telecommunication Services	0.040
Pharmaceuticals	0.069	Industrial Conglomerates	0.040
Entertainment	0.069	Automobile Components	0.038
Health Care Providers & Services	0.068	Marine Transportation	0.038
Food Products	0.067	Biotechnology	0.035
Broadline Retail	0.066	Specialized REITs	0.033
Media	0.066	Containers & Packaging	0.031
Diversified Telecommunication Services	0.066	Construction & Engineering	0.030
Multi-Utilities	0.063	Trading Companies & Distributors	0.029
Household Durables	0.062	Life Sciences Tools & Services	0.027
Electric Utilities	0.062	Health Care Technology	0.027
Semiconductors & Semiconductor Equipment	0.061	Gas Utilities	0.024
Specialty Retail	0.059	Construction Materials	0.022
Software	0.057	Building Products	0.022
Energy Equipment & Services	0.056	Electronic Equipment, Instruments & Components	0.022
Household Products	0.055	Water Utilities	0.021
Beverages	0.054	Real Estate Management & Development	0.019
Air Freight & Logistics	0.052	Independent Power and Renewable Electricity Producers	0.018
Tobacco	0.052	Paper & Forest Products	0.015
IT Services	0.051	Transportation Infrastructure	0.013

Panel B: Scandal Magnitude per Country

Country	Mean Scandal Magnitude	Country	Mean Scandal Magnitude
<i>Germany</i>	<i>0.150</i>	Austria	0.059
<i>Israel</i>	<i>0.146</i>	Portugal	0.055
<i>Italy</i>	<i>0.135</i>	Greece	0.055
<i>France</i>	<i>0.131</i>	Japan	0.052
<i>Ireland</i>	<i>0.126</i>	Sweden	0.052
<i>United Kingdom</i>	<i>0.125</i>	Poland	0.048
<i>United States of America</i>	<i>0.115</i>	Mexico	0.044
<i>South Korea</i>	<i>0.107</i>	New Zealand	0.040
<i>Netherlands</i>	<i>0.106</i>	Singapore	0.037
<i>South Africa</i>	<i>0.104</i>	China	0.036
Finland	0.096	Hong Kong	0.036
India	0.092	Turkey	0.028
Brazil	0.087	Chile	0.026
Denmark	0.079	Philippines	0.026
Switzerland	0.078	Malaysia	0.025
Norway	0.077	Argentina	0.022
Spain	0.071	Thailand	0.017
Australia	0.069	Czech Republic	0.011
Belgium	0.067	Indonesia	0.011
Canada	0.066	Saudi Arabia	0.010
Hungary	0.064	United Arab Emirates	0.005

Table 3: Summary statistics

This table shows the summary statistics of the key variables used in the study. Please refer to Appendix A.1 for the definition of all variables.

	N	Mean	Std Dev	P25	P50	P75
Scandals Magnitude - Industry	50,265	0.05	0.08	0.00	0.00	0.07
Scandals Magnitude - Country	50,265	0.08	0.05	0.04	0.07	0.11
Market Capitalization	50,031	21.95	1.22	21.13	21.96	22.78
Tobin's Q	50,262	3.23	3.84	1.09	1.96	3.71
Return on Equity	50,262	0.10	0.19	0.04	0.10	0.17
Return on Asset	50,265	0.05	0.07	0.02	0.04	0.08
Operating Margin	50,265	0.13	0.22	0.06	0.11	0.21
Δ Sales	49,872	0.11	0.26	-0.03	0.07	0.19
Size	50,265	22.02	1.36	21.14	22.05	22.96
Leverage	50,265	0.26	0.18	0.12	0.25	0.38
Num. of analysts	50,265	10.95	7.76	5.00	10.00	16.00
SG&A Expenses	50,265	0.24	0.25	0.09	0.17	0.31
Cash	50,265	0.10	0.10	0.03	0.07	0.14
Δ ESG Score	44,301	0.09	0.24	-0.04	0.04	0.16
Capex	50,265	5.00	4.33	1.97	3.83	6.63

Table 4: Spillover effects of corporate scandals on firm's value

This table shows the estimates for the baseline model:

$$Y_{s,i,j,t} = \alpha_0 + \alpha_1 \text{Scandal Magnitude}_{s,i,j,t-1} + \sum \alpha_2 \text{Controls}_{t-1} + \text{Industry Dummies} + \text{Country Dummies} + \text{Year Dummies} + \varepsilon_{s,t} \quad (2)$$

where the dependent variable is Market Capitalization or Tobin's Q. Scandal Magnitude is the central variable that aims to capture the intensity of corporate scandals within an industry "i" in a given year. The control variables are Size, Leverage, Return on Assets, Analyst Coverage and Selling, General and Administrative Expenses. Variable definitions are given in Appendix A.1. ***Significant at the 1%, **5%, and *10% levels.

Dependent:	Market Cap _t				Tobin's Q _t			
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
Industry Scandal Mag _{t-1}	-0.197*** (-4.79)	-0.315*** (-9.86)	-0.183*** (-5.34)	-0.249*** (-8.63)	-0.845*** (-5.35)	-0.805*** (-5.41)	-2.858*** (-9.02)	-0.767*** (-5.25)
Size _{t-1}			0.513*** (58.91)	0.409*** (62.47)			-0.943*** (-29.27)	-0.917*** (-27.73)
Leverage _{t-1}			-0.452*** (-10.87)	-0.33*** (-13.31)			2.542*** (20.76)	2.526*** (20.25)
ROA _{t-1}			2.569*** (33.07)	2.435*** (54.06)			5.913*** (26.30)	5.788*** (25.46)
Num. of Analysts _{t-1}			0.017*** (15.53)	0.013*** (21.95)			0.029*** (9.74)	0.03*** (9.62)
SG&A _{t-1}			0.447*** (12.25)	0.180*** (6.79)			0.709*** (5.38)	0.753*** (5.62)
Firm FE	N	Y	N	Y	N	Y	N	Y
Industry FE	Y	N	Y	N	Y	N	Y	N
Country FE	Y	N	Y	N	Y	N	Y	N
Year FE	Y	Y	Y	Y	Y	Y	Y	Y
N	48,393	48,393	47,974	47,974	48,596	48,596	48,171	48,171
adj. R ²	0.08	0.01	0.64	0.59	0.09	0.01	0.24	0.17

Table 5: Spillover effects of corporate scandals on financial performance of competitors
This table shows the estimates for the baseline model:

$$Y_{s,i,j,t} = \alpha_0 + \alpha_1 \text{Scandal Magnitude}_{s,i,j,t-1} + \sum \alpha_2 \text{Controls}_{t-1} + \text{Industry Dummies} + \text{Country Dummies} + \text{Year Dummies} + \varepsilon_{s,t} \quad (2)$$

where the dependent variable is Return on Assets (left panel), Operational Margin (central panel) or Sales Growth (right panel). Scandal Magnitude is the central variable that aims to capture the intensity of corporate scandals within an industry “*i*” in a given year. The control variables are Size, Leverage, Return on Assets, Analyst Coverage and Selling, General and Administrative Expenses. To facilitate interpretation, the coefficients of Analyst Coverage are multiplied by 100. In the model that employs ROA as the dependent variable, we omit lagged ROA from the control variables. Variable definitions are given in Appendix A.1. ***Significant at the 1%, **5%, and *10% levels

Dependent:	ROA _t				Op. Profit _t				ΔSales _t			
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)
Industry Scandal Mag _{t-1}	-0.012*** (-3.38)	-0.010*** (-2.72)	-0.015*** (-4.50)	-0.016*** (-5.07)	-0.032*** (-4.40)	-0.028*** (-3.92)	-0.030*** (-4.20)	-0.025*** (-3.67)	-0.018 (-1.36)	0.001 (0.09)	-0.016 (-1.00)	-0.028* (-1.82)
Size _{t-1}		-0.012*** (-17.29)		-0.022*** (-30.73)		-0.004 (-1.38)		-0.017*** (-11.38)		-0.039*** (-21.81)		-0.113*** (-32.92)
Leverage _{t-1}		-0.057*** (-14.90)		-0.049*** (-18.62)		0.058*** (5.66)		0.028*** (4.93)		0.046*** (3.98)		0.082*** (6.30)
ROA _{t-1}						0.477*** (9.00)		0.388*** (37.32)		-0.280*** (-9.54)		-0.169*** (-7.17)
Num. of Analysts _{t-1}		0.065*** (7.74)		0.042*** (6.14)		0.039 (1.62)		0.059*** (4.20)		-0.12*** (-4.89)		-0.135*** (-4.24)
SG&A _{t-1}		-0.114*** (-29.23)		-0.08*** (-28.43)		-0.355*** (-7.75)		-0.273*** (-44.51)		0.191*** (13.11)		0.359*** (25.83)
Firm FE	N	N	Y	Y	N	N	Y	Y	N	N	Y	Y
Industry FE	Y	Y	N	N	Y	Y	N	N	Y	Y	N	N
Country FE	Y	Y	N	N	Y	Y	N	N	Y	Y	N	N
Year FE	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y
N	48,598	48,173	48,598	48,173	48,598	48,173	48,598	48,173	48,238	48,173	48,238	48,173
adj. R ²	0.04	0.19	0.02	0.09	0.03	0.35	0.01	0.31	0.08	0.12	0.06	0.09

Table 6: Spillover effects of corporate scandals using an alternative specification of scandal magnitude

This table shows the estimates for our baseline model employing a different specification of the scandal magnitude that uses the proportion of firms with controversies within a country-industry in a given year. The remaining variables are the same. To facilitate interpretation, the coefficients of Analyst Coverage are multiplied by 100. In the model that employs ROE as the dependent variable, we omit ROA from the control variables due to collinearity. Variable definitions are given in Appendix A.1. ***Significant at the 1%, **5%, and *10% levels.

Dependent:	Market Cap _t		Tobin's Q _t		ROA _t		Op. Profit _t		ΔSales _t	
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
Industry Scandal Share _{t-1}	-0.103*** (-6.72)	-0.058*** (-3.76)	-0.403*** (-5.71)	-0.259*** (-3.86)	-0.006*** (-3.43)	-0.003** (-2.17)	-0.013** (-3.93)	-0.010*** (-3.23)	-0.012* (-1.93)	0.007 (1.19)
Size _{t-1}		0.513*** (58.89)		-0.95*** (-24.90)		-0.012*** (-17.27)		-0.004 (-1.36)		-0.04*** (-20.97)
Leverage _{t-1}		-0.451*** (-10.85)		2.324*** (8.79)		-0.057*** (-14.9)		0.058*** (5.68)		0.051** (4.47)
ROA _{t-1}		2.571*** (33.10)		6.508*** (14.77)				0.477*** (8.97)		-0.275*** (-9.46)
Num. of Analysts _{t-1}		1.718*** (15.52)		4.764*** (10.15)		0.065*** (7.75)		0.039 (1.62)		-0.128*** (-5.15)
SG&A _{t-1}		0.447*** (12.27)		1.906*** (10.76)		-0.114*** (-29.23)		-0.355*** (-7.74)		0.19** (13.02)
Firm FE	N	N	N	N	N	N	N	N	N	N
Industry FE	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y
Country FE	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y
Year FE	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y
N	48,393	47,974	48,596	48,171	48,598	48,171	48,598	48,173	48,238	48,173
adj. R ²	0.07	0.64	0.09	0.17	0.04	0.09	0.03	0.35	0.09	0.14

Table 7: Corporate scandals and cost and expenses dynamics of competitors
This table shows the estimates for the baseline model

$$Y_{s,i,j,t} = \alpha_0 + \alpha_1 \text{Scandal Magnitude}_{s,i,j,t-1} + \sum \alpha_2 \text{Controls}_{t-1} + \text{Industry Dummies} + \text{Country Dummies} + \text{Year Dummies} + \varepsilon_{s,t} \quad (2)$$

where the dependent variable is Cost of Goods and Sales or Selling, General and Administrative Expenses. Models 2, 4, 6 and 8 use the proportion of firms with controversies within an industry as our alternative specification for Scandal Magnitudes. To facilitate interpretation, the coefficients of Analyst Coverage are multiplied by 100. In the model that employs SG&A as the dependent variable, we omit the lagged SG&A from the control variables due to collinearity. Variable definitions are given in Appendix A.1. ***Significant at the 1%, **5%, and *10% levels.

Dependent:	COGS _t				SG&A _t			
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
Industry Scandal Mag _{t-1}	0.024*** (3.95)		0.020*** (3.92)		0.000 (-0.02)		0.002 (0.43)	
Industry Scandal Share _{t-1}		0.008*** (2.94)		0.007*** (2.81)		0.003 (0.98)		0.003 (1.11)
Size _{t-1}	0.013*** (7.51)	0.013*** (7.48)	0.012*** (10.34)	0.012*** (10.28)	-0.026*** (-10.84)	-0.026*** (-10.86)	-0.007*** (-5.26)	-0.007*** (-5.27)
Leverage _{t-1}	-0.023** (-3.21)	-0.023*** (-3.22)	-0.015*** (-3.31)	-0.015** (-3.32)	-0.062*** (-6.73)	-0.062*** (-6.72)	-0.036*** (-7.49)	-0.036*** (-7.48)
ROA _{t-1}	-0.440*** (-27.77)	-0.440*** (-27.78)	-0.383*** (-47.48)	-0.384*** (-47.51)	-0.322*** (-15.93)	-0.322*** (-15.92)	-0.230*** (-27.52)	-0.229*** (-27.51)
Num. of Analysts _{t-1}	-0.038** (-2.28)	-0.038** (-2.28)	-0.019* (-1.77)	-0.019* (-1.78)	0.048*** (2.75)	0.048*** (2.76)	-0.007 (-0.63)	-0.007 (-0.62)
SG&A _{t-1}	-0.291*** (-20.71)	-0.291*** (-20.71)	-0.211*** (-44.24)	-0.211*** (-44.25)				
Firm FE	N	N	Y	Y	N	N	Y	Y
Industry FE	Y	Y	N	N	Y	Y	N	N
Country FE	Y	Y	N	N	Y	Y	N	N
Year FE	Y	Y	Y	Y	Y	Y	Y	Y
N	47,206	47,206	47,206	47,206	48,281	48,281	48,281	48,281
adj. R ²	0.41	0.41	0.40	0.40	0.18	0.18	0.22	0.22

Table 8: Scandals and competitors' corporate investments

This table shows the estimates for the baseline model that analyzes the influence of scandals on investment decisions of peer firms on ESG practices (left panel), short-term investments (middle panel) and Capex (right panel). To facilitate interpretation, the coefficients of Analyst Coverage are multiplied by 100. Variable definitions are given in Appendix A.1. ***Significant at the 1%, **5%, and *10% levels.

Dependent:	ΔESG_t		Cash_t		Capex_t	
	(1)	(2)	(3)	(4)	(5)	(6)
Industry Scandal Mag_{t-1}	-0.06*** (-5.02)	-0.029** (-2.42)	0.007* (1.82)	0.01*** (2.64)	-0.191 (-0.99)	-0.061 (-0.32)
Size $_{t-1}$		-0.013*** (-12.27)		-0.021*** (-21.83)		-0.375*** (-9.56)
Leverage $_{t-1}$		0.006 (0.98)		-0.054** (-11.45)		-0.69*** (-3.22)
ROA $_{t-1}$		-0.015 (-0.9)		0.013 (1.49)		7.537*** (18.78)
Num. of Analysts $_{t-1}$		-0.127*** (-7.91)		-0.012 (-1.19)		1.541*** (3.11)
SG&A $_{t-1}$		0.004 (0.78)		0.059*** (12.3)		0.201 (1.05)
Firm FE	N	N	N	N	N	N
Industry FE	Y	Y	Y	Y	Y	Y
Country FE	Y	Y	Y	Y	Y	Y
Year FE	Y	Y	Y	Y	Y	Y
N	44,300	44,116	48,598	48,173	48,598	48,173
adj. R ²	0.03	0.03	0.07	0.28	0.02	0.05

Table 9: Moderator effect of ESG Score, Cash holdings and Size on the spillover of corporate scandals

This table shows the estimates for the model:

$$Y_{s,i,j,t} = \alpha_0 + \alpha_1 D_{s,t-1} \cdot \text{Scandal Magnitude}_{s,i,j,t-1} + \alpha_2 (1 - D_{s,t-1}) \cdot \text{Scandal Magnitude}_{s,i,j,t-1} + \sum \alpha_3 \text{Controls}_{t-1} + \text{Industry Dummies} + \text{Country Dummies} + \text{Year Dummies} + \varepsilon_{s,t} \quad (3)$$

where the Dummy equals one (zero) when ESG Score (or Cash holdings or Size) of firm “s” is above (below) the mean in a given year. Variable definitions are given in Appendix A.1. For brevity, we omit the estimates of the control variables. ***Significant at the 1%, **5%, and *10% levels.

Dependent:	Tobin's Q _t			ROA _t			Op. Profit _t			ΔSales _t		
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)
Scandal Mag x High ESG _{t-1}	-0.540*** (-2.83)			-0.010** (-2.16)			-0.044*** (-5.32)			-0.024 (-1.53)		
Scandal Mag x Low ESG _{t-1}	-1.029*** (-3.37)			-0.017*** (-2.68)			-0.018 (-1.51)			0.040* (1.81)		
Scandal Mag x High Cash _{t-1}		-0.685*** (-2.97)			0.000 (-0.03)			-0.024** (-2.44)			0.034* (1.83)	
Scandal Mag x Low Cash _{t-1}		-0.826*** (-4.02)			-0.018*** (-5.21)			-0.04*** (-4.21)			-0.003 (-0.19)	
Scandal Mag x Large _{t-1}			-1.59*** (-8.22)			-0.013*** (-2.91)			-0.032*** (-3.71)			-0.069*** (-4.08)
Scandal Mag x Small _{t-1}			-0.171 (-0.56)			-0.007 (-1.23)			-0.035*** (-3.10)			0.056*** (2.68)
Controls	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y
Industry FE	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y
Country FE	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y
Year FE	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y
N	44,114	47,751	48,171	44,116	47,753	48,173	44,116	6,107	48,173	44,116	47,753	48,173
adj. R ²	0.24	0.24	0.18	0.17	0.19	0.19	0.33	0.35	0.35	0.13	0.14	0.13

Table 10: Spillover effects of corporate scandals excluding the last two years of our sample period

This table shows the estimates for the baseline model excluding the observations of the years 2022 and 2023 to avoid the possible bias from the concentration of events on years with less financial information available (i.e., before the release of financial reports). To facilitate interpretation, the coefficients of Analyst Coverage are multiplied by 100. Variable definitions are given in Appendix A.1. ***Significant at the 1%, **5%, and *10% levels.

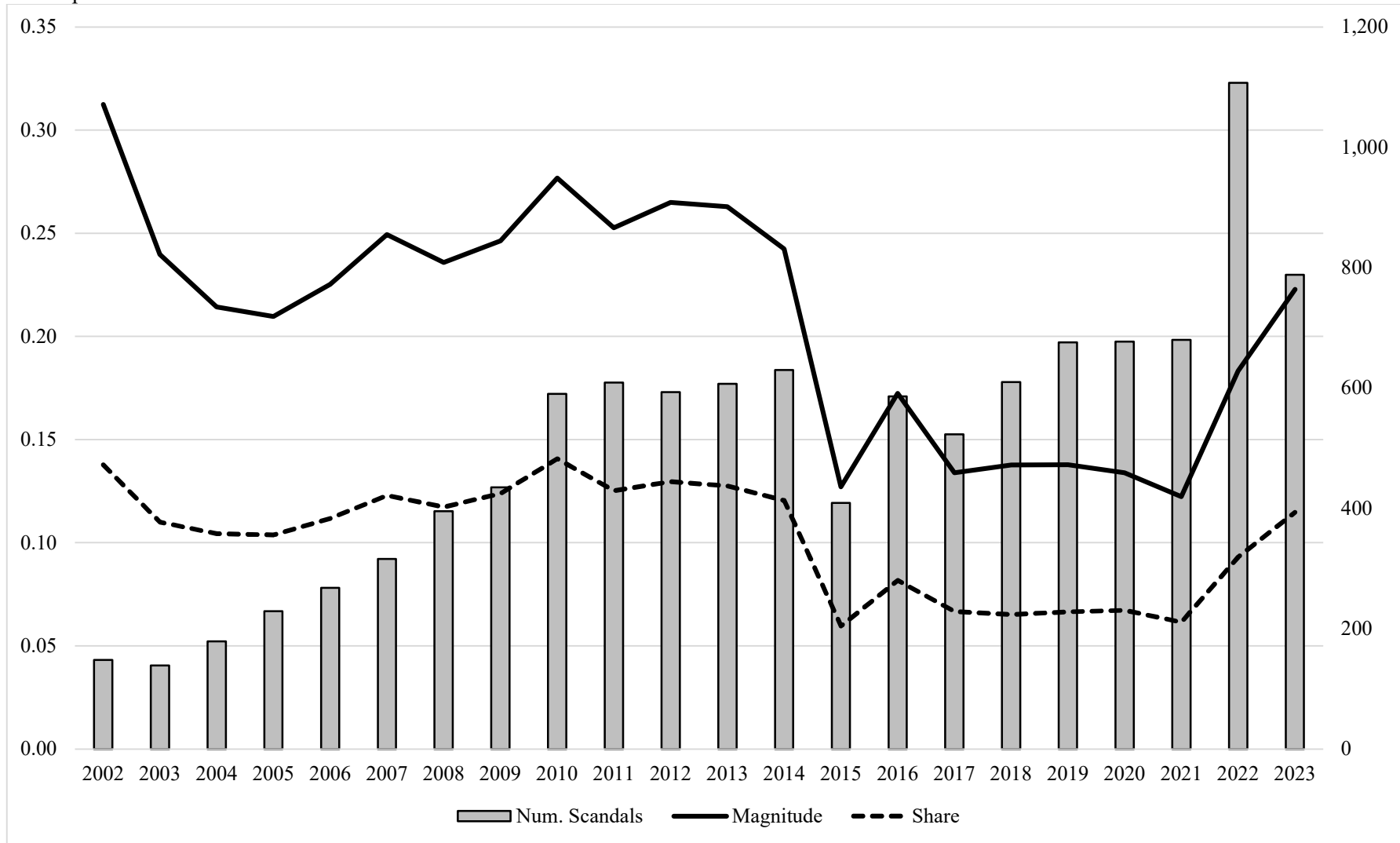
Dependent:	Market Cap _t	Tobin's Q _t	ROA _t	Op. Profit _t	ΔREV _t	COGS _t
Industry Scandal Mag _{t-1}	-0.182*** (-5.11)	-0.584*** (-3.75)	-0.009** (-2.40)	-0.030*** (-4.49)	0.015 (1.13)	0.027*** (4.20)
Size _{t-1}	0.528*** (58.18)	-0.909*** (-20.97)	0.001*** (-14.76)	-0.002 (-1.10)	-0.035*** (-17.44)	0.012*** (6.07)
Leverage _{t-1}	-0.457*** (-10.24)	2.583*** (8.74)	-0.058*** (-13.98)	0.045*** (4.88)	0.014 (1.15)	-0.021*** (-2.73)
ROA _{t-1}	2.665*** (30.51)	7.209*** (14.52)		0.478*** (20.50)	-0.187*** (-6.11)	-0.437*** (-24.89)
Num. of Analysts _{t-1}	1.54*** (13.61)	5.01*** (10.07)	0.062*** (7.03)	0.016 (0.92)	-0.132*** (-5.12)	-0.022 (-1.24)
SG&A _{t-1}	0.527*** (12.46)	2.211*** (10.19)	-0.109*** (-24.95)	-0.323*** (-16.94)	0.186*** (13.46)	-0.323*** (-20.14)
Firm FE	N	N	N	N	N	N
Industry FE	Y	Y	Y	Y	Y	Y
Country FE	Y	Y	Y	Y	Y	Y
Year FE	Y	Y	Y	Y	Y	Y
N	40,184	40,358	40,360	40,360	40,360	39,500
adj. R ²	0.63	0.24	0.17	0.32	0.16	0.43

Table 11: Spillover effects of corporate scandals among G7 and non G7 countries

This table shows the estimates for the baseline model for located in G7 and non G7 countries. G7 countries are United States, United Kingdom, Japan, Germany, France, Italy and Canada. To facilitate interpretation, the coefficients of Analyst Coverage are multiplied by 100. Variable definitions are given in Appendix A.1. ***Significant at the 1%, **5%, and *10% levels.

Panel A: G7 countries							Panel B: Non G7 countries					
Dependent:	Market Cap _t	Tobin's Q _t	ROA _t	Op. Profit _t	ΔREV _t	COGS _t	Market Cap _t	Tobin's Q _t	ROA _t	Op. Profit _t	ΔREV _t	COGS _t
Industry Scandal Mag _{t-1}	-0.090*	-0.553**	-0.010**	-0.025***	-0.002	0.032***	-0.193***	-0.371**	-0.011***	-0.027***	0.014	0.016**
	(-1.79)	(-2.45)	(-2.14)	(-2.6)	(-0.11)	(3.61)	(-4.49)	(-2.22)	(-2.37)	(-2.91)	(0.71)	(2.01)
Size _{t-1}	0.546***	-0.885***	-0.021***	-0.001	-0.036***	0.013***	0.486***	-1.015***	-0.014***	-0.008***	-0.043***	0.013***
	(45.27)	(-15.73)	(-20.45)	(-0.33)	(-13.18)	(5.45)	(41.08)	(-19.79)	(-16.76)	(-3.46)	(-16.42)	(5.29)
Leverage _{t-1}	-0.374***	2.887***	-0.039***	0.043***	0.029**	-0.022***	-0.574***	1.412***	-0.074***	0.085***	0.076***	-0.034***
	(-7.08)	(8.33)	(-11.00)	(4.19)	(2.11)	(-2.62)	(-8.8)	(3.74)	(-13.23)	(5.70)	(4.10)	(-2.79)
ROA _{t-1}	2.426***	6.411***		0.427***	-0.265***	-0.419***	2.536***	5.604***		0.536***	-0.328***	-0.477***
	(23.88)	(10.82)		(15.17)	(-6.98)	(-21.08)	(21.22)	(9.34)		(14.68)	(-7.18)	(-18.37)
Num. of Analysts _{t-1}	2.182***	7.899***	0.055***	0.017	-0.019	-0.023	1.284***	1.639***	0.046***	0.057***	-0.223***	-0.047**
	(14.62)	(10.24)	(5.43)	(0.68)	(-0.55)	(-0.94)	(8.63)	(3.24)	(4.52)	(2.64)	(-6.59)	(-2.03)
SG&A _{t-1}	0.536***	2.261***	-0.078***	-0.363***	0.212***	-0.315***	0.318***	1.212***	-0.096***	-0.34***	0.152***	-0.272***
	(12.04)	(9.37)	(-18.98)	(-15.60)	(10.90)	(-20.19)	(5.72)	(4.93)	(-16.92)	(-12.15)	(7.05)	(-11.95)
Firm FE	N	N	N	N	N	N	N	N	N	N	N	N
Industry FE	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y
Country FE	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y
Year FE	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y
N	26,513	26,668	26,670	26,670	26,670	26,091	22,542	22,586	22,586	22,586	22,586	22,188
adj. R ²	0.66	0.23	0.07	0.39	0.17	0.48	0.62	0.26	0.20	0.29	0.14	0.34

Figure 1: Corporate scandals over time



Note: The figure shows the evolution of the total number of corporate scandals (columns, right axis) as well as the mean scandals magnitude (solid line) and the mean proportion of scandals within a country-industry of our sample (dashed line). Please refer to Subsection 2.2 for the definition of scandals magnitude variable.

Appendix A

Table A.1: Variables definition

	Variable	Definition	Source
1	Scandals Magnitude	Summation of ESG controversies scaled by the number of controversies within a country-industry. Refer to Subsection 2.2 for a more detailed definition	Authors' own calculation
2	Market Capitalization	Natural logarithm of Market Capitalization	LSEG
3	Tobin Q	Market-to-book ratio	LSEG
4	Return on Equity	Ratio between Net Income and Equity Book Value	LSEG
5	Operating Margin	Operational profit (EBIT) scaled by Revenues	LSEG
6	Δ Sales	Arithmetic variation of annual Revenues	LSEG
7	Size	Natural logarithm of Total Assets	LSEG
8	Leverage	Ratio between Total Debt and Total Assets	LSEG
9	Return on Asset	Ratio between Net Income and Total Assets	LSEG
10	Num. of analysts	Number of analysts	LSEG
11	SG&A Expenses	Sales, General and Administrative Expenses scaled by Revenues	LSEG
12	Cash	Cash and Cash equivalents scaled by Revenues	LSEG
13	Δ ESG Score	Arithmetic variation of annual ESG Scores	LSEG
14	Capex	Capital Expenditures scaled by Revenues and multiplied by 100	LSEG

Table A.2: Key variables' correlation

	Scandals Magnitude - Industry	Market Capitalization (ln)	Tobin Q	Return on Equity	Operating Margin	ΔSales	Size	Leverage	Return on Asset	Num. of analysts	SG&A Expenses	Cash	ΔESG Score	Capex
Scandals Magnitude - Industry	1.00													
Market Capitalization (ln)	0.05	1.00												
Tobin Q	0.05	0.22	1.00											
Return on Equity	0.01	0.21	0.26	1.00										
Operating Margin	-0.07	0.17	-0.04	0.37	1.00									
ΔSales	0.03	0.04	0.14	0.09	0.04	1.00								
Size	0.00	0.71	-0.29	0.01	0.15	-0.07	1.00							
Leverage	-0.02	0.01	-0.05	-0.08	0.10	-0.04	0.28	1.00						
Return on Asset	0.00	0.23	0.21	0.75	0.53	0.11	-0.06	-0.24	1.00					
Num. of analysts	0.09	0.56	0.12	0.09	0.03	0.00	0.41	-0.02	0.10	1.00				
SG&A Expenses	0.06	-0.07	0.26	-0.23	-0.52	0.07	-0.30	-0.17	-0.29	0.00	1.00			
Cash	0.02	-0.02	0.23	-0.02	-0.22	0.08	-0.26	-0.34	0.03	0.00	0.32	1.00		
ΔESG Score	-0.02	-0.03	0.03	0.00	0.00	0.07	-0.06	-0.01	0.00	-0.04	0.01	0.01	1.00	
Capex	0.03	0.01	0.02	0.06	0.11	0.06	-0.04	0.07	0.08	0.06	-0.10	-0.13	0.01	1.00

Table A.3: Scandals proportion and competitors' corporate investments

This table shows the estimates using the proportion of scandal firms within an industry as our central variable in the baseline model that analyzes the influence of scandals on investment decisions of peer firms on ESG practices, short-term investments and Capex. To facilitate interpretation, the coefficients of Analyst Coverage are multiplied by 100. ***Significant at the 1%, **5%, and *10% levels.

Dependent:	ΔESG_t	Cash_t	Capex_t
Industry Scandal Share _{t-1}	-0.019*** (-3.38)	0.004** (2.31)	-0.013 (-0.15)
Size _{t-1}	-0.013*** (-12.09)	-0.021*** (-21.83)	-0.375*** (-9.55)
Leverage _{t-1}	0.006 (0.92)	-0.054** (-11.45)	-0.688*** (-3.22)
ROA _{t-1}	-0.015 (-0.89)	0.013 (1.48)	7.538*** (18.78)
Num. of Analysts _{t-1}	-0.125*** (-7.83)	-0.012 (-1.19)	1.542*** (3.11)
SG&A _{t-1}	0.004 (0.83)	0.059*** (12.29)	0.201 (1.05)
Firm FE	N	N	N
Industry FE	Y	Y	Y
Country FE	Y	Y	Y
Year FE	Y	Y	Y
N	44,116	48,173	48,173
adj. R ²	0.03	0.28	0.05

Table A.4: Proportion of scandal firms and the moderator effect of ESG Score, Cash holdings and Size on the spillover of corporate misbehaviors

This table shows the estimates for Equation (3) using the proportion of scandal firms within and industry our country as our central independent variable that interacts with a Dummy that equals one (zero) when ESG Score (or Cash holdings or Size) of firm “s” is above (below) the mean in a given year. For brevity, we omit the estimates of the control variables. ***Significant at the 1%, **5%, and *10% levels.

Dependent:	Tobin's Q _t			ROA _t			Op. Profit _t			ΔSales _t		
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)
Scandal Share x High ESG _{t-1}	-0.18**			-0.002			-0.016***			-0.003		
	(-2.05)			(-1.20)			(-4.37)			(-0.34)		
Scandal Share x Low ESG _{t-1}	-0.484***			-0.008***			-0.005			0.023**		
	(-3.31)			(-2.64)			(-0.83)			(2.02)		
Scandal Share x High Cash _{t-1}		-0.253**			0.002			-0.007*			0.016*	
		(-2.28)			(0.76)			(-1.65)			(1.78)	
Scandal Share x Low Cash _{t-1}		-0.35***			-0.009***			-0.017***			0.003	
		(-3.85)			(-5.09)			(-3.86)			(0.39)	
Scandal Share x Large _{t-1}			-0.72***			-0.003*			-0.01***			-0.025***
			(-8.40)			(-1.76)			(-2.77)			(-3.26)
Scandal Share x Small _{t-1}			-0.019			-0.005*			-0.015***			0.025**
			(-0.12)			(-1.74)			(-2.67)			(2.34)
Controls	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y
Industry FE	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y
Country FE	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y
Year FE	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y
N	44,114	47,751	48,171	44,116	47,753	48,173	44,116	47,753	48,173	44,116	47,753	48,173
adj. R ²	0.24	0.24	0.18	0.17	0.19	0.19	0.33	0.35	0.35	0.13	0.14	0.13