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ELABORATING THE RELATIONSHIP BETWEEN CSR AND FINANCIAL PERFORMANCE: A REVIEW STUDY

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ABSTRACT: -
The paper describes the relationship between CSR and financial performance. Purpose of this paper is to sum up the measures used to proxies these constructs. For this purpose a storyline review of related articles is done and relevant measures have been summarized. In the extensive literature CSR is measured by using following methods content analysis, reputational indices by rating agencies and questionnaire methods. The measures used for financial performance are accounting based measures (i.e., Return on assets, Return on sales, Return on equity and Return on capital employed), market based measures (i.e., stock returns and market value of company) and common indicators (i.e., Tobins' Q and market value added). Each of measures discussed above having their own pros and cones.

KEYWORDS: *CSR, Financial performance and measures.*

INTRODUCTION :

A company has some responsibilities for the society in which a company is operating (i.e., called corporate social responsibility). It is also known as business responsibility, corporate citizenship or relationship for community. In every sense social responsibility means that the business organization has entered into a social agreement, this agreement bound the business organization in a relation that at the time of decision making the organization has to think about the society. The history of CSR is almost as long as that of companies. CSR is growing over the years. Earlier the concept is that a business enterprise has some responsibilities towards society besides generating only revenue. The modern approach of CSR is different; nowadays it focuses on larger corporate practices rather than on the decision-making. Businesses have a large numbers of responsibilities including the whole society, except the shareholders. According to the financial theory the only objective of a business is shareholder's wealth maximization. Except the shareholders, many other stakeholders have an impact on business organization, these stakeholders often motivated by non-monetary benefits such as impact of the company on the society and environment. CSR practices varies from company to company and these differences depend on some company specific factors like company's size, area of operation, culture of the firm, demand of the stakeholders, and how previously the company is in engaging CSR. Some companies focuses on a single aspect of CSR, which is regarded as the most significant for them or where they have the maximum impact. On the other side some companies aims to integrate CSR in all aspects of their operations. Both the management and employees have to follow the principles if they want the successful implementation of the CSR.

PRINCIPLES OF CSR

Principles of CSR includes is a mixture of ideas such as corporate governance, business ethics, and sustainable development.

1. The business has to follow the ethical business practices and have to assess the moral effects of their work from product development to distribution. An ethical business organization will have to look beyond its own ethical practices.
2. The business has to work with accordance to the sustainable development. Sustainable development means to use the resources of the society without compromising the need of the future generation.
3. All businesses must act in accordance with legislation that prevents the environment pollution which includes water, air, and soil pollution. Corporations have to take permission from government or from any other regulatory authority in order to be capable to pollute up to a certain limit. They must also make provision for cleaning up. Except the national rules for the environment pollution businesses must also compliance global environmental concerns.
4. Businesses have to maintain some relationship with the local communities that live around the business. As the business recruit staff from the local society and use the resources of that particular society this is the responsibility of the businesses to assist local community in a number of ways e.g. supporting education programs and health awareness initiatives.
5. A socially responsible business has to review their supplier's practices. It is the responsibility of the business that suppliers also comply with the responsible business. It is clearly mentioned that if any supplier want to continue trading with them he has to engage in social activities.
6. Socially responsible investment avoids investment in the companies that engage in the production of alcohol and tobacco etc. and seeking investment in companies engaged in social justice and environment sustainability. (Investopedia)

CSR IN INDIA

Concept of Corporate Social Responsibility in India now shifts towards meeting the social issue from just making profits. Companies Act, 2013 Sec. 135(1) describes the provisions of the CSR and the companies covered under the criteria. The companies having Net worth more than Rs. 500cr. or Turnover more than 1000cr. rupees or Net Profit more than 5cr. rupees during any financial year shall be covered within the CSR provisions. "Companies" word used in the section also includes the foreign companies having branch or project offices in India. The prescribed CSR Expenditure for the company covered under the criteria discussed above is 2% of the amount of the net profit for the last 3 financial years. The CSR Policy identifies that companies can invest in activities like, promotion of gender equality, donations for hospital facilities, sponsoring sporting events, protection of national heritage, Contribution in the National Relief Fund, and Slum area development.

REVIEW OF LITERATURE

This study divided previous literature into two sections as;

Section 2.1: Positive relationship between corporate social responsibility (CSR) and financial performance (FP). This positive relation means that investments or expenditure on CSR activities increase the profitability of the firm. Amount spent on social activities enhance the publicity of the companies and broaden the market for that company. On the other side it also include that those firm earn more profits invest more in the social activities. So the positive relation include both directions that CSR increase profitability and good profitability leads to investment in social actions.

Section 2.2: Negative and neutral relationship between corporate social responsibility (CSR) and financial performance (FP). This negative relation means that money spent on the social activities does not leads to better financial performance. It indicates that the money spent leads to extra cost burden on the firm and increase the gross margin finally decrease the total profits of the company. So, negative relation means that the social responsibility does not leads to achieve the good financial performance. The neutral relation means that that direction of the relation is not statistically significant and doesn't indicating any relation.

SECTION 2.1
POSITIVE RELATION BETWEEN CSR AND FP

Fernandez (2016) investigated the relationship between Corporate Social Responsibility (CSR) and Financial Performance (FP) in Spanish listed companies. This study covered 107 companies listed on the Madrid Stock Exchange in the year 2009. For six multivariate regression models, the dependent variable was FP represented by ROA (Return on Assets), ROE (Return on equity) and Tobin's Q. Independent variable CSR was represented by the Global Reporting Initiative (GRI) index. LNASSET (company size by taking the natural logarithm of the assets) were used as control variable. The conclusion demonstrated positive relationships in both directions, that the social is profitable and that the profitable is social. Singh (2014) investigated the impact of CSR disclosure on the financial performance of firms in the UK. Financial performance was measured as return on assets (ROA), Tobin's Q, and total shareholder returns (TSR). He measures CSR disclosure using content analysis of CSR keywords on the annual reports of the firms ranging from 2008 till 2012. The sample composed of 34 firms of crude petroleum, 32 of mining metal and 38 of pharmaceutical industry. The regression model includes various control variables viz., the size of the firm, the age of firm, financial leverage and specific year-effect. Results showed that CSR affects the FP of firms in short-term negatively and earns a positive return on the FP in the long-term scenario. Servaes & Tamayo (2013) studied the relation between CSR and firms value. To measure CSR, the KLD Stats database was used and for performance, Tobin's q (i.e. market value of the firm) was used as Dependent Variable. Profitability measures: return on assets, return on sales, and return on equity were used. In addition, size and value were the control variables. The sample consists of all firms in the S&P 500 Index and the Domini 400 Social Index for the period 1991–2000.The results of regression analysis showed that corporate social responsibility (CSR) and firm value were positively associated with firms with high customer consciousness, as peroxide by advertising expenditures. Uadiale & Fagbemi (2012) empirically examined the extent to which corporate social responsibility contributes to financial performance in the context of Nigeria. The study examined the impact of CSR activities on financial performance measured with Return on Equity (ROE) and Return on Assets (ROA). The research design for the CSR disclosure was the content analysis. A sample size of 40 listed companies on the Nigerian Stock Exchange was randomly selected and annual reports for CSR disclosure & financial performance is collected for the year ended 2007. The results showed that CSR has a positive and significant impact on financial performance. Wang & Bansal (2012) studied that CSR activities help create business value develop strategic resources, and ensure against risks, but also cost money, distract the managers, and aggravate relationships between principals and agents. They tested the relationship by surveying the CEOs and presidents, also studying the signature Web sites of 149 new ventures, after identifying the valid contact information for CEOs or presidents, they measured CSR disclosure by examining the number of times that CSR keywords appeared on the web page of each firm. Measure of the financial performance was a nine-item, seven-point scale. Industry, places of origin, market scope, firm size and firm age were used as control variables. They conclude that a long-term orientation positively moderated the relationship between CSR activities and financial performance also magnifies the value of the benefits that accrue from CSR activities. Baird, Geylani & Roberts (2012) examined the link between corporate social performance (CSP) and corporate financial performance (CFP). They tested that to what extent firm value (i.e., stock price) was associated with an indicator of CSP (i.e., DS400). A panel data set was assembled using secondary data from three market information providers; Value Line Inc., S&P, and KLD Research & Analytics Inc. The intrinsic value of a firm's common stock price for years 2001 through 2008 was used as financial performance. Three control variables were included in the model: firm size, operating profitability, and the use of debt in the capital structure. Random coefficient model and ordinary least square method was used for analysis and results showed a measurable and statistically significant relationship between social and financial performance. Bolanle, Adebiyi & Muyideen (2012) examined the relationship between corporate social responsibility and profitability in the Nigerian banking industry. Annual reports formed the secondary source of data collection for the period of 2001-2010.

The data collected for this study were analyzed using regression analysis. Results showed that for every unit increase in the CSR expenditure will lead to .945 increases in the profit after tax of the company, thus the study suggests the causal relationship between the CSR and profitability of banks. Ghoul, Guedhami, Kwok & Mishra (2011) studied the effect of corporate social responsibility (CSR) on the cost of equity capital for US firms. Sample composed of 12,915 observations representing 2809 unique firms from 1992 to 2007. KLD STATS, used for CSR measure and equity premium was used as a dependent variable indicating the cost of equity. Control variables were the year and industry effects. Regression analyze showed that the coefficient on CSR was negative and statistically significant at the 1% level, suggesting that firms showing better social responsibility have a lower cost of equity capital. Bihari & Pradhan (2011) explained the corporate social responsibility (CSR) practices of major players in the Indian banking sector and to find out the impact of such practices on their performance and image. Measurement for CSR was the several published records of CSR activities. Profit after tax was taken as a performance measure. Data of major banks: OBC, Union Bank of India, Bank of Baroda, PNB, IDBI Bank, HDFC Bank, ICICI Bank & Canara Bank, from January 2001 to January 2009 was collected. The line graph shows that there was an increasing trend in the profits of the banks. Findings suggested that banks in India have increased their CSR activities, which also have a positive impact on the performance of the business, apart from improving their image and goodwill. Mishra & Suar (2010) studied CSR towards primary stakeholder's influence on the financial and the non-financial performance (NFP) of Indian firms. Data on CSR and NFP were collected from 150 senior-level Indian managers including CEOs through a questionnaire survey. Data on FP of the companies were obtained from the Prowess database of CMIE i.e. annual sales for 3 years (2004-06). Listing in stock exchanges, type of ownership, and firm size was the control variables. Findings of the study showed that stock-listed firms have better financial performance (FP) than the non-stock-listed firms, CSR was found to be associated with the increase in FP and NFP of firms. Findings suggested that responsible business practices towards primary stakeholders are profitable and beneficial to Indian firms. Bedi (2009) studied the relationship between the social and financial performance of a company and compare the dependency of corporate social expenditure on financial performance. He comparatively analyzed the expected expenditure with actual expenditure incurred on CSR. Top 37 firms were examined for the financial year 2007-08, which were rated by karmyog (NGO). Here an attempt has been made to find the dependency level of CSE on its annual profits (NPAT). Analyze by regression showed a high dependency of social expenditure on financial performance, and analysis also revealed a positive relationship between CSR and FP. Tsoutsoura (2004) studied the sign of the relationship between corporate social responsibility and financial performance. In order to measure CSR, they employ two measures; the first measure was the KLD rating data for the companies in the S& P 500 and a second measure the Domini 400 Social Index as a proxy. Financial performance was measured by accounting variables; Return on Assets (ROA), Return on Equity (ROE) and Return on Sale (ROS). Source of the data was the COMPUSTAT database and covers the S&P 500 index for the years 1996 - 2000. Risk, Size, Debt level, and Industry have been used as a control variable. The results showed a positive association between CSR and profitability.

SECTION 2.2
NEGATIVE AND NETURAL RELATION BETWEEN CSR AND FP

Usman & Amran (2015) examined the relationship between the dimensions of CSR disclosures and corporate financial performance (CFP) among Nigerian listed companies. Content analysis was conducted to extract CSR from annual reports of 68 companies (Excluding banking and insurance sectors) listed on the Nigeria Stock Exchange over the period of 2010-2012. Financial performance was measured by Return on Assets and Share Price. Log of the total asset was used to measure firm size was the control variable. Multiple regression analysis was performed and the results showed that CSR found to enhance CFP. The results also reveal a negative relationship between environmental disclosure and CFP, which indicates that disclosure of environmental impact information could be value destroying in Nigeria. (Palmer 2012) explored and tested the relationship between CSP and corporate financial performance (CFP). Unlike prior research, this study additionally tests the impact of CSP on sales and gross margin. Population involves S&P 500 firms (2001-2005), final sample includes 333 firms with the availability of data. Hypotheses involve analyzing the impact CSP has on dependent financial variables: sales (measured by total sales to total assets ratio), gross margin (measured by gross profit to total sales ratio) and ROA (measured by net income divided by total assets). Source of the financial data was the COMPUSTAT database and independent variable CSP was measured by MSCI Index. Size, risk, and industry effect were used as control variables. The relationships were tested using time series Regressions and results showed that improved CSR performance leads to an increase in gross margin and the decrease in sales. Soana (2011) examined the ways CSP can be proxies and investigated the possible relationship between CSP and CFP in the banking sector. An analysis of the relationship between corporate governance and financial performance was carried out on a sample of 31 Italian banks rated by AEI in April 2005. The ethical rating was used to establish the relationship between a company CSP and financial performance. CFP was quantified by means of accounting (Return on Average Equity, Return on Average Assets, Cost-to-Income Ratio) and market measures (Market to Book Value, Price to Book Value and Price/Earnings ratio) on 31/12/2005.Linear bi-variated correlation was then performed and results show no statistically significant relationship. Crisóstomo, Freire & Vasconcellos (2011) studied the relationship between corporate social responsibility (CSR) and firm performance, in Brazil. They use a CSR index based on relative amounts spent on social action. The CSR-CFP relationship was analyzed using financial and CSR data of 78 non-financial listed companies in the period 2001-2006. Content analysis was conducted to extract data from two different sources, one relative to CSR data and another that provided financial data i.e. Return on Assets (ROA) and Return on Equity (ROE). Control variables (size, risk, and sector) were added to the model. The results of regression analysis indicated that CSR negative correlated with firm value. Aras, Aybars & Kutlu (2010) investigated the relationship between corporate social responsibility and firm financial performance. The sample consists of the companies listed on the Istanbul Stock Exchange (ISE) 100 for the four consecutive years until 31 December 2006, thus 40 companies were selected after removing the companies. They examined the relationship between CSR and financial performance for the years of 2005, 2006 and 2007. CSR was measured by content analysis and financial performance, indicated by ROE, ROA, and ROS while size and risk were used as the control variables. Regression showed the negative relation between two constructs. Makni, Francoeur & Bellavance (2009) studied the relationship between corporate social performance (CSP) and financial performance (FP). They use two measures of CSP developed by MJRA. Return on assets (ROA) and return on equity (ROE) were used separately to measure a firm's FP and stock market return was used for robustness. Data on ROA and ROE were derived from the Stock Guide database. Market returns were obtained from the Toronto Stock Exchange (TSX) through the CFMRC database. The sample for the study was 179 companies listed on TSX in 2004 and 2005. Firm size, firm risk and industry were used as control variables. They find that the relationship between the aggregate CSP scores and the three FP measures were not statistically significant.

CONCLUSION

The previously conducted researches on linkage between CSR and financial performance give a general idea about the measurement of these constructs (i.e, CSR and financial performance). The studies included in this paper are also indicating some measures of CSR and financial performance. In the literature CSR is measured by using content analysis, reputational indices by rating agencies and questionnaire methods. The measures used for financial performance are accounting based measures (i.e., Return on assets, Return on sales, Return on equity and Return on capital employed), market based measures (i.e., stock returns and market value of company) and common indicators (i.e., Tobins' Q and market value added). Each of measures discussed above having their own pros and cones. Researchers can use these measures based on his or her convenience.

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