How does Corporate Social Responsibility affect Financial Performance?

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Abstract:
The objective of the paper is to determine the impact of corporate social responsibility (CSR) on financial performance and moderate role of enterprise size. Quantitative method is used in the study with research samples of 389 garment and textile enterprises in Vietnam. The results show that CSR has positive effects on financial performance on these enterprises. In addition, the firm sizes as a moderating role in this relationship, the bigger the business, the better the relationship between CSR and financial performance. However, for smaller businesses, this relationship opposite effect. The implementation of CSR reduces the financial performance. Research results show that CSR has a positive impact on financial performance, then creates motivation for enterprises to implement CSR voluntarily. However, small businesses should have a long-term strategic plan to implement CSR part by part in order to ensure the survival of the business.

Keywords: Corporate social responsibility, financial performance, moderating of size

1. Introduction

Corporate Social Responsibility (CSR) has been studied for a long time in most economic sectors. In recent times, CSR seems to have become popular and is considered to be an important matter for businesses around the world (Mirsha and Saura, 2010). Because the benefits brought by CSR are quite clear: Reduce staff turnover rate, increase customer satisfaction (Galbreath, 2009), improve reputation, motivate employees, increase capital access (Hansen, 2004), increase market share, performance (Epstein and Roy, 2001), etc. Research on the relationship between CSR and financial performance has attracted the attention of many scholars, according to the National University of Hong Kong (2015), articles on CSR most appear on management journals, there have been about 310 CSR articles on the Journal of Business Ethics since 1982, 90% of which were published after the year 2000. According to the Academy of Management Journal (AMJ) (2016), from 1958 to 2015, AMJ published 87 articles on this subject.

However, studies on the impact of CSR on financial performance are questionable. A large number of studies have shown a positive relationship between CSR and financial performance (Elliott et al., 2013; Lys et al., 2014). Some others have suggested a negative one between CSR and financial performance (Wagner, 2005; Lopez et al., 2007). And there are a few studies that provide a neutral/mixed or non-statistically meaning relationship between CSR and financial performance (McWilliams and Siegel, 2000; Makni et al., 2009). Thus, there are different and non-uni-ted viewpoints on the relationship between CSR and financial performance. What causes the difference between these results? And in what case is CSR important to financial performance? In this study, we examine the moderate role of firm size in the relationship between CSR and financial performance to better explain the impact of CSR on financial performance. The paper includes (i) literature overview, (ii) theoretical backgrounds, (iii) hypotheses and research models, (iv) research methods, (v) research results and (vi) discussion and recommendations.

2. Literature review

CSR has existed for a long time in the world. In the 1790s, there was a boycott by consumers to sugar product harvested by slaves in the United Kingdom. Within a few years, more than 300,000 Britons boycotted this sugar product. In addition, nearly 400,000 petitions with signatures were sent to the Parliament requesting for an end to the slave trade, etc. Hence, awareness of CSR has long been around the world, has undergone a period of development and has become increasingly comprehensive and meaningful. However, official CSR studies began in the 1950s (Bowen, 1953).

Over a long time from 1950 to 1999, the perception of researchers and enterprises on CSR became more and more comprehensive. In previous decades, CSR had just been understood as activities against abuses on human rights, slave trade and the use of forced labors (slaves). Later, CSR was considered in a broader range, which was activities with more social and environmental responsibility. Because businesses operated for profit in society, they also affected society and the environment. In this stage, awareness of CSR began to shape its impact on business profitability, and this relationship is still being studied and debated today. The period from 2000 up to present, CSR research has focused on smaller and specialized topics in this field, rather than the conceptualization studies.

CSR is an important issue in the contemporary international debate. In the past two decades, CSR has become increasingly popular and is considered being connected to all corporations around the world (Aras and Crowther,
Various results have been given by previous studies on the benefits and impacts of CSR. The benefits brought by CSR can be categorized as business benefits (corporate benefits) and social benefits. Or they could be classified into monetary and non-monetary benefits (Weber, 2008). Monetary benefits included direct financial effects such as revenue increase and costs reduction. Also, there were benefits that did not directly lead to cash flow but are still measured by monetary terms such as reducing risk, increasing brand value, etc. (Gerpott and Thomas, 2004; Naderer, 2005). Non-monetary benefits were those not directly measured by currency but still affected the business’s competitiveness and financial performance. These benefits could be quantitatively measured by customers’ repeated purchase rate, employee turnover rate, and so on. They could be qualitatively measured by access to capital, employees’ satisfaction, and so on. To measure these non-monetary benefits, Weber (2008) has launched the KPI system. However, assessing the impact of CSR on corporate benefits under the KPI can only be done for a specific CSR project and at a typical enterprise for a long time. Therefore, we do not approach CSR benefits in this way.

CSR has drawn special attention from academics for more than 20 years. There have been a lot of articles trying to figure out whether CSR activities bring benefits to financial operations. Most of the early research on this subject found a negative relationship and supported shareholder theory and organizational theory. Friedman (1970) argued that maximizing profit was the only responsibility of businesses. Furthermore, Jensen and Meckling (1976) thought that the core motivation behind managers’ CSR actions was to create a positive impression on the media.

On the other hand, the majority of the latest research supported the theory of stakeholders and argued that the benefits of CSR were long-term ones. CSR created intangible assets such as customer loyalty, reputation, and so on. (Hillmand and Keim, 2001). Mirsha and Saura (2010), analyzed the relationship between CSR and financial performance in Indian companies, the results showed that CSR and its aspects both had positive effects on financial performance and non-financial performance of these companies. Rexhepi et al. (2013), argued that CSR activities were mandatory for companies to meet the society and customer expectations and to maintain their market share. A comprehensive analysis of 52 studies by Orlitzky et al. (2003) confirmed the positive relationship between CSR and financial performance. Hasan et al. (2018) analyzed the relationship between CSR and financial performance through intermediary variables - working productivity in manufacturing firms in the United States. As a result, CSR had a positive effect on financial efficiency through the intermediate variable - productivity.

However, there have been studies that found a two-way mixed relationship or even did not identify any connection between CSR and FP. (McWilliams and Siegel, 2001; Lioui and Sharma, 2012). Aras et al. (2010) found no relationship between CSR and financial performance in developing countries.

Because of these mixed results, a number of studies attempted to identify CSR’s affecting mechanism on a business’s financial performance. According to Jayachandran et al. (2013), the explanation for these mixed results was that most studies apply a synthetic CSR index, while each parameter needed to be separately tested. Moreover, some studies suggested that corporations’ CSR actions should be consistent with consumers’ support (Bhattacharya and Sen, 2004) and in line with key business objectives (Porter and Kramer, 2006). Some studies explored the relationship between enterprise size and CSR. However, these studies produced quite vague results. Udaysankar (2008) found a U-shaped relationship between CSR involvement and enterprise size. Small size and big size businesses have similar motivation to carry out CSR activities. Midsize businesses are the least motivated. Another study conducted by Perrini et al. (2007) found that there was a tendency of larger firms to perform more CSR activities than that of small and medium ones. Aras et al. (2010) found a statistically significant relationship between enterprise size and CSR activities, but there was no relationship between CSR and financial performance.

Previous studies have examined the role of business size in the level of CSR implementation. Very few studies examine the moderate role of enterprise size to explain the impact mechanism of CSR on financial performance. In this study, we examine the moderate role of enterprise size in the relationship between CSR and financial performance. The context of the study is the Vietnamese garment and textile enterprises. These enterprises are mainly engaged in processing orders from international buyers such as USA, Europe and Japan. These markets give very strict requirement on CSR. CSR can be considered as a “laissez-passé” for Vietnamese enterprises to reach the world market.
3. Theoretical background and research hypothesis

3.1. Stakeholder theory

Stakeholder theory combines with CSR to explain the effect of CSR on financial performance (Marom, 2006). Both the two concepts, CSR and stakeholder theory, are recognized as important aspects of corporate governance. This trend can be seen as a natural progression in parallel with industries’ development and businesses activities are increasingly concerned with democracy and environmental protection. Stakeholder theorists have studied the relationship between stakeholder management and its impact on financial performance (Berman et al., 1999; Mirsha and Suar, 2010). Despite their different views, all of these studies deal with the same problem: The business’s ethical behavior to its stakeholders affects its wealth. The difference between studies is the study design, the social viewpoint, the environment, the definition of measurement and the source of data, the period of time (Griffin and Mahon, 1997). Thompson et al. (1995) explained that stakeholders are groups in relation to an organization. According to Clarkson (1995), stakeholders are people or groups that have ownership or interest in the company's activities. The relevant groups are Employees, local communities, suppliers, customers, society, government, etc. Stakeholders are of two types: primary and secondary stakeholders (Clarkson, 1995). The key stakeholders are: "One side without its continuous participation, the business cannot survive," and the secondary stakeholders are: ”Those who have influence or are affected by the business, but they are not involved in business transactions and not necessary for the survival of the business “(Clarkson, 1995, p. 106).

3.2. Theory of Slack Resources

To explain the relationship between CSR and financial performance, Fauzi and Idris (2009) used the theory of Slack Resources. This theory is developed on the view that an enterprise can carry out its activities based on the resources owned by the business. Slack resource should be prioritized for planned activities. According to Waddock and Grave (1997), as corporate’s financial performance improves, available resources will easily allow the company to implement CSR such as social and community relations with employees, etc. Some corporate’s CSR activities based on their resources have brought competitive advantage to the company through image, reputation, market share and long-term cost savings (Miles and Covin, 2000).

3.3. Good Management Theory

Good management theory is used by Waddock and Grave (1997) in explaining the linkage CSR -financial efficiency. According to good management theory, firms should strive to satisfy their stakeholders without assuming financial condition. When doing so, businesses will have a good image and reputation. From the viewpoint on resources, CSR’s attributes are one of the enterprise’s intangible assets and CSR is one component contributing to the competitiveness of the business (Barney, 1991). Basically, the theory encourages managers of businesses to continuously look for better ways to improve their competitive advantage and finally improve the company's financial performance. According to Miles and Covin (2000), CSR is a good way to meet the needs of stakeholders and can be a distinct advantage to enhance competitiveness.

3.4. The relationship between CSR and financial performance

Implementing CSR will increase the corporate’s ability in accessing capital, improve its image and reputation (Galbreath, 2009). CSR helps businesses maintain relationships with customers, increase customer loyalty, and make employees satisfied with higher engagement (Saeidi et al., 2015). CSR improves the corporate’s financial performance (Mirsha and Suar, 2010; Hasan et al., 2018). A small number of studies suggest that implementing CSR increases the business’s expenses and reduces profits. This means that the business changes from maximizing shareholder’s profit value to developing the benefit of a broader set of stakeholders. In today's competitive environment, businesses operate not only for profit but also for their social, environmental impact and other stakeholders. It not, it is really difficult to survive and develop sustainably; for example, Formosa (2017) has harmed the environment and had to suffer a hefty consequence for such actions. Therefore, we propose the following hypothesis:

H1: CSR has a direct and positive impact on financial performance

3.5. Moderator role of enterprise size

The relationship between CSR and financial performance has been much discussed, but the result of this relationship is still unclear. As most studies have shown positive relationships (Mirsha and Suar, 2010). Besides, a comparatively small proportion of studies have shown a negative or mixed/neutral relationship or no statistically significant relationship between CSR and financial performance. So what governs this result? Some researchers argue that it is due to the impact of research contexts such as developed and developing economies (Aras et al., 2010). Others argue
that it is due to the regulation of external investment and product differentiation (Lee and Jung, 2016). There are quite a few companies interested in business size when assessing the impact of CSR on financial performance. Business size is often separately studied in previous research in terms of the effect on CSR or financial performance or on both as an independent variable. Perrini et al. (2007) found that the tendency of large enterprises to implement CSR was greater than that of small and medium enterprises. Udayasankar (2008) argues that very small and large enterprises implement CSR more than medium-sized ones. According to stakeholder theory and good management theory, CSR implementation will bring about good financial performance for enterprises. Therefore, we propose the following hypothesis:

\[ H2: \text{The enterprise size plays a regulating role in the relationship between CSR and financial performance} \]

4. Research Methodology

4.1. The context of Vietnam’s textile and garment industry

Vietnam’s textile and garment industry is a key sector taking priority for export of Vietnamese economy. In the last 5 years, this industry has continuously had the second biggest export turnover in the country. Exports contribute about 15% to GDP. In the year 2017, the yarn industry exported 990 thousand tons with a total value of 12.62 billion USD, increasing by 23.7% in value compared to the year 2016. The garment industry export was 19.2 billion USD, an increase of 9.4% compared to the same period in 2016. The total export turnover of Vietnam’s textile and garment industry reached 31 billion USD. However, the characteristics of this industry are using much labor force (especially female workers) and quite a large amount of discharge to the environment (especially the textile and dyeing enterprises). According to the Sustainable Apparel Coalition (SAC), in order to produce a complete garment product, there are many stages such as washing, dyeing, bleaching or printing. Therefore, thousands of different chemicals are used in these activities. The production of a complete T-shirt consumes 2,495 liters of water which includes both chemicals and dyes that are flushed back to the environment and cause contamination. The use of toxic chemicals not only affects the environment but also directly affects the user if chemical residue remains on the product. Therefore, it is extremely necessary for garment and textile enterprises to implement CSR. If business activities harm the environment and people, it will cause instability for the business. The best way is for businesses to ensure that everything is in harmony with the environment and people. Therefore, CSR activities will better improve the relationship between enterprises and employees and the environment, thus improve the enterprises’ financial efficiency.

4.2. Study sample

Sample research is an important determinant of the success of a quantitative study. There are usually two ways of sample selections: random and non-random sample selection. Of which, random sampling is used more widely and results in more objective results. In this article, we randomly selected samples based on Vietnamese garment and textile enterprises named in the “Vietnam Textile and Garment Directory” issued by the Vietnam Textile and Garment Association in 2015. Emails were sent by link: https://www.surveymonkey.com/r/LRGV3GP and directly survey the textile and garment enterprises in Vietnam at conferences, workshops held by the Vietnam Textile and Garment Association. The participants were business owners, business leaders, CSR managers, school accountants, etc. who were knowledgeable about corporate’s operating strategy and CSR activities. The result after data cleaning was 389 valid questionnaires included in the analysis to test the hypothesis.

4.3. Research models

![Figure 1: a Research model](http://www.ijmsbr.com)

(Source: Research Team’s Proposal)

CSR: Voluntary actions by businesses to ensure the benefit of stakeholders such as employees, the environment, communities, suppliers, investors and customers (Mirsha and Saura, 2010). There are four ways to measure CSR: measurement based on reputation index, a measurement based on content analysis, one-way measurement of CSR and question-based survey measurement. In this study, we measure CSR based on six dimensions of CSR: staff,
environment, community, suppliers, customers, investors. Developed from research by Mirsha and Saura (2010). CSR measurement includes 39 indicators of 6 CSR aspects with a 5-point Likert scale from strongly disagree to agree strongly.

Financial performance: Result of businesses’ operating activities under the monetary measurement. Financial performance differs significantly depending on the perspective of the financial information user. Every business has many financial performance indicators to satisfy the benefits of all stakeholders such as Managers pay attention to welfare and profit because then their work is appreciated. Owners want to maximize their assets by increasing the market value of the business. Trade partners seek a stable payment of business. Employees expect a salary, bonus and work environment, etc. Thus, the research team focuses on the approach of measuring the financial performance following stakeholder theory to formulate financial performance indicators that could be used to test hypotheses. According to Santos (2012), financial performance is expressed in three aspects: profitability: ROA, ROE, ROI, ...; Growth: revenue growth, market share growth, ownership capital growth, ... and market value: TQ, PE, ... In this study, the textile and garment enterprises in Vietnam are mostly unlisted. Thus, the research team approached the measurement of financial performance in 2 aspects: Profitability and specific growth rates measured in 10 items: ROA, ROE, ROI, ROS, EVA, the growth rate of assets, growth in net sales, growth in net profit after tax, growth in equity and ownership capital growth.

Measurement of financial performance: Previous studies have approached the measurement of financial performance by objective and subjective measurement. Objectively measurable data is from an available source or researcher self-calculate basing on the accounting data. Subjective measurement is taken from the business’s idea with a 5 point - Likert scale compared to its competitor (Sqyropoulou, 2013) or to the previous year (Bradley et al. 2012) and the most commonly used way is to the industry’s average over the last three years (Santos and Brito, 2012). Dollinger and Golden (1992) in their study found that subjective and objective measurements of financial performance were positively correlated. There have been a number of other studies reporting the significant correlations between subjective and objective measurements when measuring financial performance (Collins and Smith, 2006; Coombs and Gilley, 2005). In this article, the approach is the measurement of financial performance by a subjective method based on the assessment of business leaders to the sector’s average over the past three years with a 5-point Likert scale from much lower to much higher.

4.4. Analytical methods

To test hypotheses, we used SPSS 22 and Smart PLS 3.0 software to perform the following analysis: Descriptive Statistics; Cronbach Alpha reliability measurement and total variable correlation; Measurement model evaluation the by aggregate reliability, convergence value, and discriminant value; Path coefficients and T-values test through the Bootstrap technique.

5. Research results

600 questionnaires were distributed, and 536 questionnaires were collected. However, during the survey questionnaire classification and data cleaning before analysis, only 389 valid questionnaires were left for inclusion in the analysis of official data. The questionnaires empty and the "reply for fulfilling the task" were removed.

PERCENTAGE OF WORKFORCE

Figure 2: Sample size structure
This sample rate is quite similar to the "Textile and Garment Directory" issued by the Textile Association in 2015. Of which, the number of enterprises with less than 100 employees accounts for 10%; the number of enterprises with 100 to under 200 employees is 18% and the number of enterprises employing from 200 to less than 500 people is 33%. The number of enterprises with a workforce of between 500 and under 1,000 is 21%. The remaining number of enterprises with more than 1000 employees account for 19%.

Results of measuring scale reliability and total variable correlation show that 11 CSR latent variable measured observations with Cronbach Alpha's reliability of less than 0.7 and a total variable correlation coefficient of under 0.3 should be excluded from further analysis. We do not evaluate EFA because both CSR and financial performance variables are structural measurements. CSR is made up of six first-order factors, and financial performance is made up of the first 2 order factors. According to Dao Le Thanh (2018), EFA is not suitable for structural measurement.

Evaluating the measurement model by composite reliability; Convergence value and distinguished value.

Composite Reliability is measured by Cronbach Alpha, CR, and AVE.

<table>
<thead>
<tr>
<th></th>
<th>Cronbach’s Alpha</th>
<th>rho_A</th>
<th>Composite Reliability</th>
<th>Average Variance Extracted (AVE)</th>
</tr>
</thead>
<tbody>
<tr>
<td>CSR</td>
<td>0.982</td>
<td>0.982</td>
<td>0.982</td>
<td>0.666</td>
</tr>
<tr>
<td>FP</td>
<td>0.949</td>
<td>0.951</td>
<td>0.949</td>
<td>0.653</td>
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Convergence of the scale: Used to evaluate the stability of the scale. According to Fornell and Larcker (1981), the average variance extracted (AVE) must be greater than or equal to 0.5 to confirm the convergence value. The load coefficient of each observation variable is greater than or equal to 0.7 and is meaningfully indicative of the scales’ reliability. The above composite reliability table represents that the requirements on AVE are satisfactory. The outer loading of the scale is high (> 0.5) and statistically significant (Henseler et al., 2009).

Discriminant validity: Measurement of discriminative validity helps to ensure the difference and no correlation between elements used to measure the factors. To measure discriminant value, the square root AVE of each measurement factor is greater than the latent variable correlations between that factor and others to indicate the degree of discrimination and reliability of the factors (Fornell and Larcker, 1981). Finally, the test of the factor load of each indicator gives results twice for convergence and discriminant validity (McLure, Wasko & Faraj, 2005). This has been achieved by considering the load factor of an index larger than any other of its structure (Chin, 1998; McLure, Wasko & Faraj, 2005).

<table>
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<tr>
<th></th>
<th>CSR</th>
<th>FP</th>
</tr>
</thead>
<tbody>
<tr>
<td>CSR</td>
<td>0.816</td>
<td></td>
</tr>
<tr>
<td>FP</td>
<td>0.395</td>
<td>0.808</td>
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The result of running bootstrap after running PLS is as follows:
Figure 2: Bootstrap results

It can be seen from the results of the Bootstrap running that CSR has a statistically significant positive effect on financial performance with an impact of 0.374 (P = 0.000). According to Chin et al. (1996), the effect level of 0.02; 0.15; 0.35 will indicate weak, moderate and strong influence. Therefore, CSR has had a strong impact on financial performance (0.374) in Vietnamese garment and textile enterprises. In addition, the variable of business size has an impact on the financial performance of 0.156 (P = 0.002). Finally, the authors examine the moderate role of enterprise size with the Moderating Effect Size variable. The results show that the moderator variable has a statistically significant effect at 5% and the effect level is 0.093 (P = 0.043). Based on the standardized regression coefficient, we further analyze the scale of enterprises as follows:

Figure 3: Moderator role of enterprise size

For larger enterprises, the standardized regression coefficient of the moderator variable is $\beta = 0.6$ (P = 0.000), and for smaller firms, this is $\beta = -0.4$ (P = 0.000), the result is shown in Figure 3. This means that for the larger the business,
the more CSR is implemented, the more financial performance is and for the smaller ones, the implementation of CSR makes the financial situation worse. This finding is consistent with studies by Perrini et al. (2007). The larger the enterprises are, the more engaged they are in CSR activities than the small and medium ones. Combined with the hypothesis H1 is supported, the more CSR the firms implement, the higher the financial performance is.

6. Conclusions and recommendations

In prior studies, the relationship between CSR and financial performance can be clearly established by either positive or negative impacts. But there are also studies that do not find the relationship between CSR and financial performance especially in developing economies. Aras et al. (2010) did not find a statistically significant relationship between CSR and financial performance in the developing economy, but only found a significant relationship between enterprise size and CSR. Perhaps, in economically developed countries, CSR is not fully relevant to financial performance. However, businesses still take CSR into account because of the sustainability of all business activities. Studying general enterprises in developing countries is easy to the result that there is not enough linkage to the relationship between CSR and financial performance. However, in our study, the context is Vietnamese garment and textile enterprises. These businesses mainly marketed to the US, Europe, and developed countries. Hence, CSR activities are probably better enough. Thus, in our study, we found a statistically significant positive impact of CSR on financial performance. However, the moderator role of enterprise size is very important. With greater businesses, the impact of CSR on financial performance is stronger. This means that the more the companies implement CSR, the better reputation and image they have, which leads to an increase of customer loyalty, access to capital, and an attraction of talent employees (this is crucial as high quality workforce in the garment, and textile sector are still lacking in high numbers, there are 3 universities providing training on garment and textile). In contrast, for smaller and smaller firms, the more they implement CSR, the worse their financial situation become. Because small and medium sized enterprises face many difficulties in doing business such as limiting their economic resources, human resources, understanding, etc., the implementation of CSR activities will be costly so their financial performance will be reduced. These small businesses often survive on the CSR costs that businesses do not spend. However, with a long-term development strategy, CSR is still considered as a guide for all activities of enterprises. CSR will shape businesses culture and help them grow sustainably.

References


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