RELATIONSHIP BETWEEN CORPORATE SOCIAL RESPONSIBILITY PRACTICES AND FINANCIAL PERFORMANCE OF FIRMS QUOTED IN THE NAIROBI SECURITIES EXCHANGE (NSE)

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ABSTRACT

The main goal of businesses is to maximize profit and increase the shareholder's value. In 2000, a movement defining broader corporate responsibilities for, the environment, local communities, working conditions and ethical practices has gathered momentum. This new driving force is known as corporate social responsibility (CSR). There has been significant interest and debate on the impact that a firm's investments in corporate social responsibility (CSR) practices and initiatives have on its market value. This project was concerned with assessing the relationship between CSR and a firm's performance. While the CSR activities may be consistent with the firm value maximization, the researcher investigates whether the incremental spending on CSR has an effect in the corporate financial earnings of the firm and its investment standing in the public domain. The research critically evaluated the argument that managers should maximize the present value of their firm's cash flow in making strategic choices favouring the shareholders. Alternatively, they could abandon wealth, maximizing the interests of the firm's shareholders for the good of other stakeholders. In effect, the proposed research study investigated whether the activities addressing the plight of other stakeholders would improve, have no impact or affect the company's corporate performance. The study targeted all the 47 listed firms in the Nairobi Security Exchange (NSE). Structured questionnaires and a secondary data collection sheet were issued to the head of the firm and acted as the unit of observation. This study adopted a descriptive research survey design; the collected data was examined descriptively in terms of means and standard deviations and also inferential where Pearson's correlation and multiple linear regression were used to examine the relationship between the dependent and the independent variable. The data was presented using both tables, charts, graphs and statistical commentary. The study established that corporate social responsibilities practices significantly affected the financial performance of the listed firms although this relationship was not moderated by government policies. All the formulated hypotheses were rejected ($p<0.05$). The study recommended that corporate communication managers and public relations managers of the listed firms should improve more on CSR strategy and reporting frameworks to greatly enhance financial performance. The policy makers of the respective listed firms in Kenya should give more weight on CSR strategy and reporting when designing policies to improve CSR practices for improved financial performance. The practitioners like external and internal auditors of the listed firms at the NSE should critically audit the CSR strategies and reporting frameworks of these firms to greatly drive their financial performance.

INTRODUCTION

Corporate Social Responsibility Reporting (CSR reporting) helps to convey information about businesses' CSR initiatives to stakeholders and society. It also reflects their vision, values and personalities. Through CSR reports, stakeholders assess a company's reputation. Therefore, CSR reporting has become a mechanism for promoting business values. According to Craib and PwC (2010), it has "become critical to a company's credibility, transparency, and endurance." If CSR reporting is of high quality, stakeholders are provided with reliable and relevant CSR information that helps to close the information gap between the companies and stakeholders (The Institute of Chartered Accountants, 2004). Therefore, quality CSR reporting increases a company's reputation and strengthens its competitiveness. Thus, the concept of Corporate Social Responsibility has gained a substantive focus on the global economy. The emphasis on the need for more socially responsible firms has moved from being the preserve of the developed economies to being the concern of also the emerging and the developing nations thanks to globalization. Over nearly two decades, the relationship between organizations and society has been subject to much debate, often of a critical nature.

The nature of CSR is, therefore, a highly topical area for business. The majority of organizations around the world are taking steps to demonstrate and enhance their CSR credentials, including committing to sustainable development. Public interest in these issues is great but is mixed with widespread scepticism about the sincerity of corporate engagement with social and environmental programmes. To capture the compliance with the times, Companies have shifted from the capitalist notion of doing business. Few trends could so thoroughly undermine the very foundations of our free society as the acceptance by corporate officials of a social responsibility other than to make as much money for their stockholders as possible (Friedman, 1962).

Corporate Social Responsibility (CSR) has been widely studied with much of the study concentrating on business-society relationships and dynamics in the developed economies of Europe and North America (Egri and Ralston 2008). CSR performances in both developed and developing economies are not at par due to inherent structural disparities such as weak enforcement of regulations, corruption and lack of awareness of the basic rights of the various stakeholders (Ibrahim & Hamid, 2019). Due to a limited capacity of regulators, compliance with even basic legislation cannot be taken for granted in many cases (Fox, 2004). The political system of many developing countries is furthermore shaped by a low salience of NGOs (Logsdon, Thomas & Van Buren, 2006), while ethical consumerism is often not an established phenomenon either (Newell & Muro, 2006). In a study by Ibrahim & Hamid (2019) on the impact of CSR on financial performance of listed Non-Financial Services Companies in Nigeria, acknowledged that CSR has been embraced by organizations. However, the study states that there have been contradicting findings on how CSR relates to financial performance some indicating a negative association while others indicating a positive relationship.

In Kenya, the relationship between corporate social responsibility and a firm's financial performance has been studied. The studies show that CSR have been adopted by a number of firms however on the relationship they have with company performance, the results remain inconclusive. For example, a study by Nkaiwatei (2011) on the relationship between social accounting practice and profitability in the oil industry in Kenya, found that financial performance was one of the factors that determine CSR practice in the oil industry. Mutuku (2005) established that there is no relationship between CSR and financial performance.

Despite numerous studies being analysed the relationship between CSR and firm performance in recent decades globally and even here in Kenya, the findings are not entirely conclusive. This has kept the scholars interested in deepening their understanding of this relationship. One of the reasons for this can be explained by inadequate of even lack of consensus stems from the existence of different conceptualizations of CSR and firm performance, as well as different measurement methodologies and different models used to analyse the relationship between both variables.

Statement of the problem

Every company have a primary key objective of increasing or maximizing profits. However, it is believed that companies have more than that one role and that they exist for more than just economic goals (Khamah, 2014). These beliefs have resulted in most companies engaging in CSR activities here in the country. Gichana (2004) focused on CSR practices by companies listed at NSE. His findings revealed that a majority of Kenyan companies are increasingly adopting social responsibility in their strategic thought process and most recognized the practice (Social responsibility) as one of their core values. In addition, Okiro, Kinyua and Omolo (2014) in a study indicated that CSR expenses are being accepted by managers much the same way as operational expenses. This raises some complexity in issues as to whether firms that practice CSR perform better or worse compared to those that do not. The need to implement CSR has been widely recognized by developed as well as developing economies. In Kenya, the Companies Act require firms to carry out activities in a socially responsible manner. However, Kenyan firms still lack little evidence of awareness of CSR even though 43 percent of the companies reported some extent on social performance and 26 per cent promised to implement CSR activities in the future (Mwangi & Jerotich, 2013).

Most of the studies suggest a positive relationship between both variables, but on the other hand there are also many studies that suggest that this relationship is either inexistence or it is negative. For example, Mutuku, (2005) found no evidence to indicate a relationship between CSR and financial performance. This was in support of a study done by McWilliams and Siegel, (2001) who found the same and argued that CSR is only a way to attain differentiation and does not directly affect profit rate. In contrary, Nkaiwatei (2011) on the relationship between social accounting practice and profitability in the oil industry in Kenya, found that financial performance was positively related to CSR practice in the OIL industry.

One of the reasons for this lack of consensus stems from the existence of different conceptualizations of CSR and business performance, as well as different measurement methodologies and different models used to analyse the relationship between both variables. A knowledge gap, therefore, existed which studies the impact of CSR on Corporate financial performance which this study would liked to address.

Objectives of the Study

i. To determine the relationship between CSR Strategy & reporting and financial performance of firms listed in the NSE.
ii. To determine the relationship between Stakeholders engagement and financial performance of firms listed in the NSE.

LITERATURE REVIEW

Theoretical Literature

There are various theories trying to figure out the company responsibilities to the society. They are divided in to two groups, that is, those that suggest a positive relationship between CSR and corporate financial performance and those that depict a negative relationship.

Shareholder Theory

The stakeholder theory will be used to illustrate how CSR improves financial performance in firms. According to the model, stakeholders are concerned about enhancing their value. According to the shareholder theory, the goal of companies is to maximize shareholders' wealth. Following Milton Friedman (1970), the sole responsibility of companies is to "make as much money as possible while conforming to the basic rules of the society, both those embody in law, and those embody in ethical custom." As a company is deemed to be a vehicle for creating wealth for those who risk capital (Greenwood, 2001), maximizing profit is necessary for its survival. As managers have agency relationships with shareholders, they have a fiduciary duty to maximize profit (Friedman, 1970). Consequently, they should only undertake projects that have favourable financial value.

Therefore, CSR initiatives may lead to objections from shareholders. According to Ruf et al. (1998), CSR contributions are outflows of economic resources that cannot create wealth for shareholders. From the standpoint of the shareholders, CSR contributions ruin their investment. However, shareholder theory does not prohibit CSR contributions that make value (Sweeney, 2009). In this case, the cost-benefit principle dictates a firm's CSR considerations, including grants and disclosure. Under the shareholder theory, CSR is justified if the related future income is expected to be higher than the current associated costs.

Stakeholder Theory

Freeman (1984) argues that companies' responsibilities are not limited to shareholders, but encompass their stakeholders, groups of people who can affect or be affected by the companies, such as employees, customers and financiers. As stakeholders can contribute to a company's wealth capacity (Post et al., 2002), to sustain growth, companies should prioritize stakeholders' interests (Van der Laan, 2009) and take their perspectives and activities into consideration. In this case, CSR disclosure is used as a means of displaying company accountability (Van der Laan, 2009). The underlying argument has two strands. First, stakeholders provide the resources, such as capital, labour and revenue (Sweeney, 2009). If companies act irresponsibly toward employees, customers, and society, then they risk losing these critical resources. Second, stakeholders are both potential beneficiaries and risk bearers (Post et al., 2002). They are exposed to risks associated with socially irresponsible behaviour, such as inferior quality products or exploitation of labour and the natural environment. According to the distribution justice principle (Sweeney, 2009), a firm's profit should be divided among all of the risk-takers, including stakeholders.

Metcalfe's (1998) sub-classification of stakeholders into primary and secondary has helped to define this concept clearly. Primary stakeholders are those whose participation is critical to a company's operation, e.g., customers, employees, and shareholders. Secondary stakeholders are people who affect or are affected by a company's activities, but are not engaged in company transactions, for example, the media (Metcalfe, 1998). This distinction clarifies the determinants of CSR initiatives.

Stakeholder theory can be broken into three parts: descriptive, normative, and instrumental (Donald & Preston, 1995). The first is the description of the specific characteristics of responsible companies. The second is the justification for the actions taken by the company based on the moral guidelines (Donald & Preston, 1995). The third is the connection between the stakeholder approach and the desired outcome (Donald & Preston, 1995). It examines the link between CSR performance and firm performance, contributing to the understanding of the instrumental part of this theory.

Stakeholder theory is used to explain the motivations for CSR reporting. Roberts (1992) uses the stakeholder theory to analyze the determinants of CSR disclosure using logistic regression. He examines the link between CSR disclosure and stakeholder power, and a firm's strategic posture and past economic performance, respectively. Specifically, he uses the percentage of ownership, donations to political parties and leverage ratio as proxies for stakeholder power, and the number of public affairs staff and philanthropic foundations as proxies for strategic posture. Besides, he uses stock market and accounting-based measures to test the effect of economic performance in the previous year on a firm's decision regarding CSR disclosure in the current year. As the information on the proxies for stakeholder power and firms' strategic posture is difficult to obtain from Chinese firms, this study focuses on testing the relationship between economic performance and the publication of CSR reports.

Empirical Literature

Various studies have been done to evaluate how CP relates to financial performance. Hategan and Curea-Pitorac (2017) sought to identify this relationship in Romanian listed firms. The authors conducted data analysis on firms listed in the Bucharest Stock Exchange between 2011 and 2015 and evaluated 29 companies that had made large profits for the entire period. Logistic regression was used to show how businesses use financial and non-financial indicators when making charitable contributions. Tobin's Q Ratio and Return on Equity were used to determine company performance levels. Further, Hategan and Curea-Pitorac (2017) used qualitative research by using panel data econometrics approach to identify the correlations between the variables. The findings illustrated that there is a positive correlation between CP and financial performance on Romanian listed corporations. However, they also found out that philanthropy not only increases a firm's financial position but also enhance non-financial factors such as improving public perception. The paper concluded by indicating that managers are more inclined to become philanthropic to improve their firm's performance and to increase its value. The authors encourage that further studies should be done to assess how other variables enhance the relationship between the two variables.

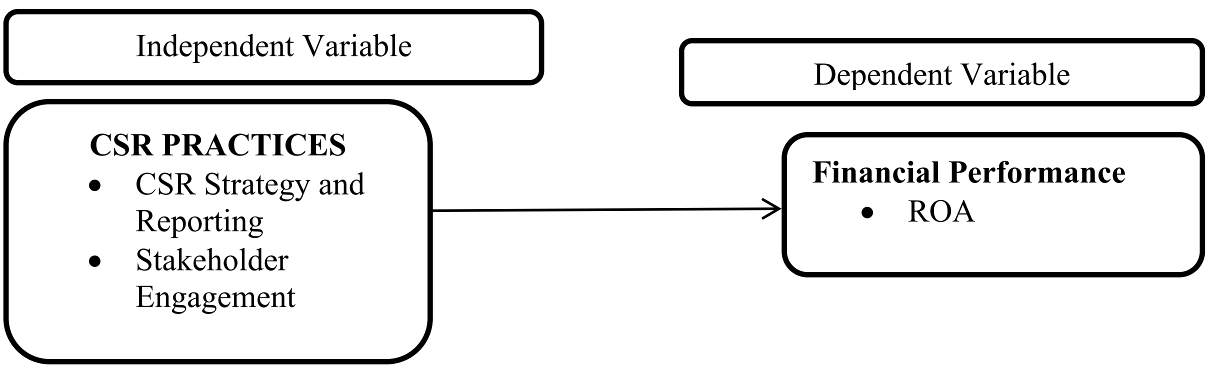
Wang et al. (2015) carried research on the relationship between CSR and financial performance in the construction industry. The paper focused on the dimension of social responsibility in philanthropy. The authors used the stakeholder theory which emphasizes on the interconnectedness of relations between enterprises and their suppliers, customers, investors, employees, and communities and other entities that may have stakes in the firm (Wang et al., 2015). Moreover, they used the transaction cost approach to show that philanthropy increases expenses. Other theories used include dependence and legitimacy models. A sample of 15 companies was used among the US, Japan, Australia, Europe, and China. The study found out that there is a curvilinear relationship between CSR and financial performance. Therefore, the authors concluded that their results would be necessary to policymakers and will push companies to conduct more charitable contributions to increase their revenues.

In Kenya, Mutuku (2013) researched the link between CSR and financial performance. The study also sought to determine the effects of firm size, industry sector, and organizational structure on social responsibility. Although the rise of privatization and liberalization have enhanced corporate growth, companies are consistently facing the challenge of understanding and responding to their social responsibilities. Additionally, firms are enduring pressure from diverse entities such as civic society, government, customers, and shareholders, to fulfil their legal obligations to resolve broader societal issues. The study used a sample size of 33 firms listed on the NSE. The key variables included employee engagement, corporate governance, customer service, community leadership, and environmental conservation. Moreover, the correlational analysis used indicated that there was no significant relationship between CSR and financial performance in construction industries by a linkage was found within the finance and investment sectors. The author concludes that companies should include social responsibility into their agendas and indicates that future studies can focus on determining whether a relationship exists between CSR and non-financial performance.

Similarly, Mwangi and Jerotich (2013) conducted a research to evaluate the relations between CSR practices and firm performance in the manufacturing and construction sector in Kenya. The key independent variables were efficiency, CSR practices, and capital intensity, while the dependent parameter was financial performance. The study utilized a correlational descriptive survey research design and the regression analysis model to establish a link between financial performance and CSR. The sample size had 14 companies that were listed with NSE by December 2011. The findings of the research indicated that there was no significant relationship between CSR and financial performance. However, a strong positive correlation was established between the dependent and independent variables when used together. Therefore, the authors recommended that companies should not incur high expenses on CSR hoping to improve their value, but instead, they should indulge in these practices for other sustainability benefits. Mwangi and Jerotich (2013) suggest that further studies should be done in different sectors and then compared to their findings.

Conceptual Framework

The independent variable is corporate social responsibility with financial performance used as the dependent variable.



RESEARCH METHODOLOGY

This study adopted a descriptive research survey design. This research targeted all the 47 listed companies at Nairobi Security Exchange (NSE) in the main segment as at 31st December 2019. In each company, senior management staff in charge of CSR, a corporate communications or a Public relations officer acted as the unit of observation meaning they responded on behalf of the company. The study adopted a stratified sampling strategy where the population was first divided into smaller groups (strata) which were the companies. Thereafter, a simple random sampling was used to pick sample units which provided each member with an equal opportunity of being sampled. The study utilized both primary and secondary data. Primary data was collected using a structured questionnaire which captures all the dimensions of CSR and corporate financial performance. One questionnaire per company was administered through drop and pick method, email or personal administration as convenient to the respondents. The data obtained from the field was analyzed using the Statistical Package for Social Sciences (SPSS Version 25). All the questionnaires received were first coded to facilitate data entry. After data cleaning which entailed checking for errors in the entry, descriptive statistics such as mean score and standard deviation were estimated for all the quantitative variables and information presented in form of tables and graphs. Descriptive statistics were useful because they enabled the researcher to meaningfully describe the distribution of scores or measurements using few indices. Inferential data analysis was then done using Pearson correlation coefficient and regression analysis (multiple regression analysis).

Research Findings

From 47 questionnaires administered, 37 were dully filled and returned equivalent to a response rate of 78.7%. On the position Held by Respondents, 70.3% of the respondents were at the middle level position, 29.1% were at the bottom level. This means that respondents who participated in the study were drawn from middle and bottom levels which infer the diversity of the views shared by the participants on CSR practices. On gender of respondents, 54.1% of the respondents were female while 45.9% were male. On years of Operation, 86.5% of the organizations had been in operation for over 9 years, 13.5% had operated for 7-9 years. Thus, majority of the firms had operated for a long period of time implying that they had a memory of the issues revolving around CSR practices that were of major concern in the present study. On the basis of CSR Evaluation, while CSR practices were evaluated on the basis of in-house research in 56.8% of the studied firms, 43.2% of the other firms evaluated their CSR practices on the basis of the professional reports. Findings on practicing of CSR Activities showed that all the studied firms (100%) did practice CSR. This means that the firms were relevant to be used as case studies in exploring the issues of CSR practices.

CSR Strategy and Reporting

Table 1 gives the findings of descriptive statistics on CSR strategy and reporting, which was the first independent specific objective of the study.

Table 1: CSR Strategy and Reporting

	Mean	Std. Dev
The company Practices code of ethics in relation to the responsibility of its products and services	4.86	.346
The company has board - level Responsibility for CSR	4.86	.346
The company reports on community Investment in CSR reporting	4.32	.883
The company reports on environmental conservation in CSR reporting	4.86	.346
The company reports on workplace quality on CSR Reporting	4.59	.724
The company facilitate staff training programs for its Employees	4.59	.497
The company sponsor the poor through education program	4.32	.883
Average	**4.63**	**0.575**

The findings in Table 1 indicate the average score as 4.63; the value of the highest mean was 4.86 while the lowest mean was 4.32. This means that the studied firms strongly agreed on the fact that they had CSR strategy and reporting frameworks in place.

Stakeholder Engagement

The second specific objective variable of the study was stakeholder engagement. The findings on this variable as determined through descriptive statistics are as shown in Table 2.

Table 2: Stakeholder Engagement

	Mean	Std. Dev
The company have a policy or stated commitment for stakeholder engagement	4.32	.883
The company engages stakeholders concerning CSR issues on community Investment, workplace quality and environment protection	4.72	.450
The company initiates dialogue with customers, employees Community groups, shareholders/investors and NGOs.	4.59	.724
Concerns are raised during stakeholder's engagement	4.45	.730
The company formally responds to issues and Concerns raised during stakeholder engagement	4.72	.450
Average	**4.56**	**0.647**

The results in Table 2 indicate the value of the average as 4.56, with the highest value of mean of mean being 4.72 and the lowest value given as 4.32. This infers that the studied firms practiced stakeholder engagement as an aspect of their CSR activities.

Inferential Statistics Results

In order to test and make relevant inferences on the hypotheses that had been developed by the study, regression analysis was conducted. The findings were determined and summarized as shown in subsequent sections.

Corporate Social Responsibility Strategy & Reporting and Financial Performance

The study sought to determine the effect of CSR strategy and reporting on financial performance. The findings were determined through linear regression analysis and summarized in Table 3.

Table 3: Corporate Social Responsibility Strategy & Reporting and Financial Performance

Model	R	R Square		Adjusted R Square	Std. Error of the Estimate	
1	.851[a]	.724		.716	.01208	
		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
(Constant)		-.176	.023		-7.512	.000
CSR Strategy and Reporting		.007	.001	.851	9.575	.000

a. Dependent Variable: ROA
b. Predictors: (Constant), CSR Strategy and Reporting

The resultant equation from Table 4.14 becomes

Y=-.176+.007X₁………………………………………………………………………….(i)

Where Y=-performance and X_1 is CSR strategy and reporting

From Table 3, the value of R square is given as 0.724, which means that 72.4% change in financial performance of firms listed in the NSE is individually explained by CSR strategy. This means that apart from CSR strategy & reporting, there are still other factors influencing financial performance of the listed firms. The results further indicate the beta coefficient of CSR strategy and reporting as 0.007 with p-value as 0.000. This finding is consistent with Wang and Qian (2011) who shared that corporate philanthropy has a positive impact on a firms' financial performance since it aids them in gaining socio-political acceptability, which in turn enables them to have positive stakeholder responses.

Stakeholders Engagement and Financial Performance

The findings of linear regression on stakeholder engagement and financial performance were determined and summarized in Table 4.

Table 4: Stakeholders Engagement and Financial Performance

Model	R	R Square		Adjusted R Square	Std. Error of the Estimate	
1	.577[a]	.333		.314	.01877	
		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
(Constant)		-.060	.026		-2.315	.027
Stakeholder Engagement		.005	.001	.577	4.179	.000

a. Dependent Variable: ROA
b. Predictors: (Constant), Stakeholder Engagement

$Y=-.060+.005X_2$……………………………………………………………………….. (ii)

Where Y=-performance and X_2 is stakeholder engagement

Table 4 shows the value of R square as 0.333, which means that 33.3% change in financial performance of the listed firms is explained by stakeholder engagement individually. Furthermore, a unit change in Stakeholder Engagement would increase financial performance of the listed firms by 0.005 units. At 5%, the p-value of stakeholder engagement (p=0.000), which means that it had significant effect on financial performance. This finding is consistent with Galant and Cadez (2017) who noted that stakeholders are interested in firms engaging in environmentally friendly activities

CONCLUSION AND RECOMMENDATIONS

Conclusion

The first objective of the study sought to determine the relationship between CSR Strategy & reporting and financial performance of firms listed in the NSE. This objective was helped in formulation of the following hypothesis; H_{01} there is no significant relationship between strategy & reporting and financial performance of firms listed in the NSE. The study rejected hypothesis H_{01} and concludes that CSR strategy and reporting is a significant factor affecting financial performance of the listed firms at the NSE.

The second objective of the study sought to determine the relationship between stakeholders' engagement and financial performance of firms listed in the NSE. This objective resulted into the following hypothesis; H_{02} there is no significant relationship between stakeholders' engagement and financial performance of firms listed in the NSE. Thus, hypothesis H_{02} was rejected and the study conclude that stakeholders engagement is a significant factor affecting financial performance of the listed firms at the NSE.

Recommendations

Based on the regression beta coefficients, CSR strategy and reporting greatly affected financial performance followed by community investment, stakeholder engagement, environmental performance and workplace quality. In view of this finding, this study makes the following recommendations:

The corporate communication managers and public relations managers of the listed firms should improve more on CSR strategy and reporting frameworks so as to greatly enhance financial performance.

The policy makers of the respective listed firms in Kenya should give more weight on CSR strategy and reporting when designing policies to improve CSR practices for improved financial performance. The policy makers at the Capital Market Authority (CMA) should formulate clear guides and regulations on CSR strategy and reporting frameworks of the listed firms at the NSE.

The practitioners like external and internal auditors of the listed firms at the NSE should critically audit the CSR strategies and reporting frameworks of these firms with the aim of greatly driving their financial performance.