Social Responsibility and competitive success of firms in the Lisbon Metropolitan Region.

Completed Research Paper

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Abstract

Social Responsibility is considered a crucial issue to enhance a long-term competeveness in firms because it has been demonstrated the causal relationship with several strategic business variables. This paper develops a conceptual model and applies Structural Equations Modeling technique to a sample of 91 firms from the Lisbon Metropolitan Region in order to understand the link between Social Responsibility and competitive success. The model provides a simple guidance for upgrading competitive success in firms operating in Portugal. We consider this work as a starting point to develop a more accurate model for Portuguese economic reality in the near future.

Keywords: *Social Responsibility, Innovation, Performance, Competitive Success, Lisbon.*

1. Introduction

Social Responsibility (SR) in Europe is a trending area in management and both, academics and practitioners are developing new models to understand and to measure the concept and how to get competitive advantage by responsible business behavior. In the particular case of Portugal, SR could be understood as a way to overcome the economic crisis. SR has been previously empirically related with competitive success in other countries and contexts (Weber, 2008; Vilanova *et al.*, 2009; Gallardo-Vázquez and Sánchez-Hernández, 2012; Marín *et al.*, 2012; Boluta and Pitelis, 2014). In this paper the question we seek to answer is: What is the effect of SR on Portuguese business competitive success? To explore this question we start by reviewing SR evolution and the existing research in Portugal. In next sections we develop a structural equation model to analyze the causal effect of SR to other variables including competitive success because, furthermore to our knowledge, no research has explicitly examined these relationships. As a result, last section offer some remarks and complementary future lines of research.

2. Literature Review, Method and Research Hypotheses

2.1. Approaching SR in specific regional context

The literature review concerning SR is very rich. It is possible to find some important contributions from before the fifties (Barnard, 1938; Clarks, 1939). However it was after this

period during the called "modern era" of SR that a proliferation of studies around the SR appeared. According with Carroll (1999), this modern era started with the contribution of Bowen (1953), and the publication of its book "social responsibilities of the businessman". The topic sparked interest and during the following decades many studies, concerning SR, have been published.

During the sixties more profound approaches tried to define SR (Frederick, 1960; MacGuire and Walton, 1963). On the seventies a boom of definitions and approaches to SR occurred. At this time many references to "corporate social performance" begun to emerge and the term SR gains greater projection (Johnson, 1971; Eells and Walton, 1974; Sethi, 1975; Preston and Post, 1975; Carroll, 1977; 1979). In the eighties, the focus is no longer the tentative definition of SR but the deepening of alternative themes in particular required on business ethics and stakeholder management, SR and profitability, responsibility, responsiveness and social issues (Jones, 1980; Tuzzolino and Armandi, 1981; Dalton and Cosier, 1982; Strand, 1983; Drucker, 1984; Cochran and Wood, 1984; Aupperle *et al.,* 1985; Epstein, 1987). In the nineties, other alternative themes were developed (such as corporate citizenship) but come few additional inputs to the definition of SR. In 1991 Carroll revisited its four-part SR definition (Carroll, 1991) and proposed that the discretionary component of SR is called philanthropic and suggests that the four components are introduced into a pyramid, the base of which is economic responsibility. According to Carroll, the socially responsible company makes profits, obey the law, ethics is behaves as a corporate citizen through charitable activities. Between 2000 and 2005 appeared a set of national and international organizations dedicated to ethics and SR. And, mechanisms of institutionalization of ethics and SR began to develop. Arise ethics codes, training in ethics, directors and managers responsible for SR, audits in ethics and SR and develop the reports of sustainability.

Also from the nineties until today arise inputs to determine what needs to be considered to assess corporate social performance. Nowadays firms are encouraged to work actively for SR because not only it is a business opportunity for them in today's world, but in many cases it is a reflection of the expectations of their customers, employees, society, and other stakeholders (MarkHerbert and Von Schantz, 2007). Recently, the European Commission has put forward a simpler definition of SR as "the responsibility of enterprises for their impacts on society" (EU, 2011: 7) and outlines what a business should do to meet that responsibility. In this European framework, we share with Van der Heijden *et al.* (2010:1787) the conceptualization of the internal process of SR "as an organizational sense-making process that involves creating and sharing a unique meaning of Corporate Social Responsibility".

Given the SR importance, and to examine the extent to which business practice actually is a reflection of what is accepted in theory, we focus on a specific research project that was designed for firms in a Regional Community in Spain, the Autonomus Community of Extremadura, to measure their orientation towards CSR with respect to other management's strategic variables (Gallardo-Vázquez and Sánchez-Hernández, 2012, 2013, 2014). It is understood that without measurement instruments it is impossible to situate firms in the space of the various actions that comprise socially responsible behaviour. While various studies in the literature have defined measurement scales considering specific aspects or dimensions of SR, one can find none that provides a satisfactory measure of the degree of a firm's orientation to SR in its entire extent. Neither are there any scales that can explain the causal relationships of SR with other important corporate strategic variables at a regional level. With this purpose we have considered necessary to test whether the previous scale defined for

Extremadura is able to cover the different dimensions of SR e social, economic, and environmental at a specific regional level, different from the first study, to deal with the variety of situations that a firm might have to address to gain a label of being socially responsible. The Lisbon metropolitan region has been the object of study in this work.

2.2. The study contextualization

In Portugal, in recent years, SR has gained increasing importance. With reference to the European Commission Green Paper published in 2001, appeared in Portugal a number of organizations/associations in order to promote new management philosophies grounded in concepts that emerge from the Social Responsibility and Sustainable Development. Organizations, such as, Group Discussion and Support for Corporate Citizenship (GRACE), CSR Europe and ERS Portugal, BCSD Portugal, Portuguese Association for Business Ethics (APEE), have been active in the development and implementation of these new themes in organizational context. Initially, social responsibility was adopted by large companies and multinationals, but currently it is assumed as a strategy that allows improved competitiveness also in small and medium businesses, and according with Kastenholz *et al.* (2004) a growing number of companies are adopting codes of conduct is higher, seeking environmental certification and/or pursue social goals.

Studies from Rego *et al.* (2003) revealed important data concerning the adoption of social responsibility by Portuguese companies. They concluded that a considerer number of Portuguese companies have a code of conduct and that most of the managers of companies without codes of conduct considered important to have this code and spread it within their organization. Abreu and Crowther (2005) have analyzed SR in Portugal empirically. Their findings show the relationship between SR activity and corporate image and performance and also, the existence of cultural differences in SR conceptualization. The authors highlight the importance of more research in this area, in Portugal and in the newly expanded European Community. Other authors (Dias-Sardinha and Reijnders, 2005; KPMG, 2006; Branco and Rodrigues, 2006, 2008) confirmed this increasingly importance of SR in Portuguese industry, in particular, in what concern the environmental dimension. Specifically, studies in car manufacturing shown that SR contributes not only to better corporate financial performance by lowering costs and increasing productivity but also indirectly to better corporate financial performance by increasing consumer car purchasing satisfaction (Loureiro *et al.*, 2012).

2.3. Causal relationships

Measuring SR performance remains a challenging task (Morimoto *et al.*, 2005). In the fact, SR performance is a social construct and some physical property where not available and results depend how SR is measured. Ullmann (1985) proposed two categories of SR measures: social disclosure (embracing voluntary corporate social reporting and mandatory pollution reporting) and social performance which might preferably use a reputational index or some other form of third party ranking/rating system. Though, Ullmann (1985) admitted that often social disclosure is utilized as a surrogate for actual SR performance. SR means that companies perform accountability to their stakeholders by incorporating social and environmental concerns in their business operations (Tanimoto and Suzuki, 2005).

Nevertheless, firms will necessarily have to take into account cultural differences when defining their SR policies and communicating to stakeholders in different countries (Bird and Smucker, 2007). Some studies suggest that a vast majority of corporate social

programs are primarily intended to create good relations and a positive publicity, and to boost employees' moral (Porter and Kramer, 2002) but also refers that, very often they have nothing to do with the strategy of the firm (Gallego-Álvarez, *et al.* 2011).

In a local perspective, investments made in social responsibility contribute to enhance the demand for the products sold by the company, given the goodwill produced by the firm to be seen as a responsible company (Mackey *et al.* 2007; Mainardes *et al.* 2011). At this respect, Gallego-Álvarez *et al.* (2011) affirm that, in the future, only those firms following sustainability as a goal will achieve a competitive advantage. Related to competitiveness, Waddock and Graves (1997) revealed a positive relationship between firms social performance and its financial performance and Orlitzky *et al.* (2003) suggested a positive link between social and financial performance.

Additionally, today enterprises are starting to integrate social entrepreneurship into their core activities in order to develop socially innovative products and services (Schwab, 2008). According to Asongu (2007), innovation is a strong argument for SR. Larsen and Peck (2001, p.17) claimed that "innovative companies are thinking and acting in terms of a triple-bottom-line ethic, which goes well beyond the drive to maximize shareholder value by incorporating environmental quality and social justice considerations into their business decisions". Mac Gregor and Fontrodona (2008) have explored the fit between SR and innovation in a study which involved 60 SMEs throughout Europe concluding that SR implementation and innovation can be configured to form a virtuous circle. More specifically, Borger and Kruglianskas (2006) demonstrated that there were strong relationships between the implementation of CSR strategy and effective environmental and innovative performance, aspect also supported by Chang (2011). Hockerts and Morsing (2008) have studied SR in the innovation process and later, Werther and Chandler (2010) have considered innovation as strategically important for SR.

Based on the previous arguments we believe that, within the Lisbon metropolitan area, the regional model originally developed by Gallardo-Vázquez and Sánchez-Hernández (2012) related to SR and competitive success, considering also performance and innovation, could fit in this new context. This empirical task is shown in next sections.

2.4. Method and Hypotheses

The analysis has been undertaken by using a structural equation modeling approach based in the previous work of Gallardo-Vázquez and Sánchez-Hernández (2012, 2013, 2014) in the region of Extremadura, in Spain. The multivariate technique used was Partial Least Squares (PLS), a second-generation technique primarily used to develop theories in exploratory research. PLS estimation of path models involves latent constructs indirectly measured by multiple indicators and allows the use of reflective measures, as is the case.

In the model, constructs has been hypothesized as reflective bearing in mind that this is the most used choice in social sciences. The decision to develop a reflective model implies that causality flows from the constructs to the indicators. Therefore, a change in a construct causes a change in its indicators as the indicators share a common theme and are interchangeable, enabling researchers to measure the construct by sampling a few relevant indicators underlying the domain of the construct (Coltman *et al*., 2008). The model developed to analyze SR in Portugal is shown in **Figure 1** below.
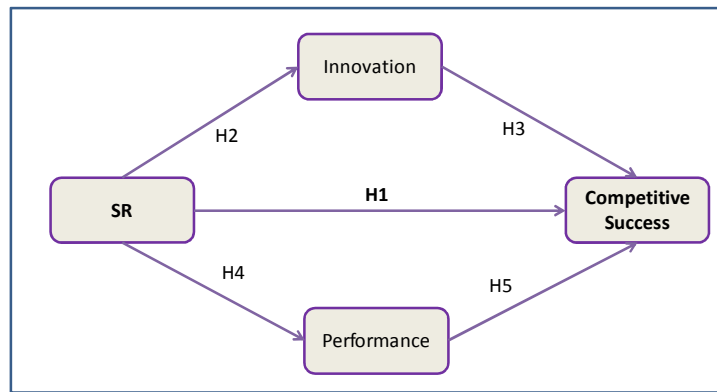
Figure 1: The conceptual model

This study aims to describe whether the firms´ orientation to SR is related to the firm's performance, innovation and competitive success. Here we present the five hypotheses to be tested:

H_1: There is a positive association between the orientation to SR and the degree of competitive success in the market.
H_2: There is a positive association between the orientation to SR and the degree of innovation.
H_3: There is a positive association between the degree of innovation and the degree of competitive success in the market.
H_4: There is a positive association between the orientation to SR and the degree of performance.
H_5: There is a positive association between the degree of performance and the degree of competitive success in the market.

To carry on the empirical analysis, the selected sample consisted of 91 firms from the Metropolitan Area of Lisbon considering that group of businesses representative of the Portuguese productive framework. Metropolitan area of Lisbon registers a higher concentration of population, have 18 municipalities and 14 cities. Nowadays, have about 3 millions inhabitants and ¼ of total Portuguese population, 30% of total Portuguese firms, 33% of total employment and contributes more than 36% to Portuguese GDP. **Table 1** presents the technical information of the study.

Table 1: Technical data sheet of the study

Technical issues	Data in the study
Universe	Managers in Portugal
Geographical scope	Metropolitan area of Lisbon (Portugal)
Date	May-June 2014
Sample	91 firms
Sample method	Convenience
Method of information collection	E-mail and phone contact
Contacted firms	500
Index of participation	10%
Analysis technique	Partial Least Squares

In order to get answers from the managers, the instrument used for data gathering was the same questionnaire previously used by Gallardo-Vázquez and Sánchez-Hernández (2012, 2013, 2014). The respondents should identify their perceptions respecting a five-point Likert scale from "1" being "not agree" to "5" being "completely agree".

3. Analysis and main results

The first step in interpreting the results is to examine measure reliability and validity. In our reflective model the SR construct drives the indicators, which have positive and high inter-correlations. Following common practice we examine first the second-order construct. Taking into account that constructs in the model have been designed as reflective, one examines the loadings, which can be interpreted in the same manner as the loadings in a principal component analysis.

Results from the general measurement model show the final items kept for SR. It is remarkable that exclusion or inclusion of one or more indicators from the domain does not necessarily alter the content validity of the construct (Coltman *et al*., 2008). We have considered 0,60 loading value a lower limit for acceptance as modest construct reliability, that is applicable in the early stages of development of scales. That is close to the 0,7 general recommendation (Nunally, 1978). To assess discriminant validity and according to Fornell and Larcker (1981), we have calculated the average variance extracted (AVE) for all constructs getting values higher than the limit of 0,50 (0,60, 0,55 and 0,56 for Competitive Success, Innovation and Performance respectively). However the average variance extracted for SR get only a value of 0,44, that is close to 0,50 but is not really good enough to be considered a good value. Composite reiliability has been also tested, considering it a more accurate measure than Cronbach alpha value because it does not assume equal item weighting. The model shows satisfactory values for all constructs (0,70 for SR, 0,74 for Competitive Success, 0,71 for Innovation and 0,72 for Performance).

The second step of the analysis is related to the goodness-of-fit of the model in order to confirm the working hypothesis. For that purpose, PLS employs bootstrapping, a nonparametric re-sampling technique that offers both the standard error and the values of Student's *t*-statistic. Thus, to calculate the significance of the path coefficients, the test was performed with 500 subsamples using a two-tailed *t*-distribution with n-1 degrees of freedom, where n is the number of sub-samples.

Consistent with our first hypothesis, the path linking SR in to Competitive Success was positive and significant. However, as it is shown in **Table 2**, not all hypothesized relations have been verified. H_1, H_2 y H_5 are significant, but H_3 and H_4 are not. It has been verify the direct effect of SR to Competitive success, the main hypothesis of this work (H_1). There have been also verified the direct and positive effect of SR on Innovation (H_2) and the direct and positive effect of Performance on Competitive Success (H_5). However, in this empirical analysis we cannot confirm any influence of Innovation on Competitive Success (rejection of H_3) and we cannot confirm any influence of SR on Performance (rejection of H_5). Furthermore, R^2 of the dependent variables are not acceptable in all cases. PLS dies not generate a single goodness of fit metric for the entire model. The R^2 values are examined instead. In the model, the R^2 value obtained could be accepted for Innovation and Competitive Success (R^2 Innovation = 0,131; R^2 Competitive Success = 0,265) but R^2 is not acceptable for Performance (R^2 Performance = 0,012).

Table 2: Hypotheses testing with a bootstrap procedure

Hypothesis A ➜ B	Original path coefficient (β)	Mean of sub-sample path coefficient	*t*-value
H₁ SR➜ Competitive Success	0,498	0,505	8,68***
H₂ SR➜ Innovation	0,359	0,366	5,68***
H₃ Innovation ➜ Competitive Success	0,127	0,135	1,8
H₄ SR ➜ Performance	0,019	0,020	0,29
H₅ Performance➜ Competitive Success	0,188	0,186	2,88**
*p < 0.05; **p < 0.01; ***p < 0.001 (based on a Student's two-tailed test, $t_{(499)}$) $t_{(0.05;499)} = 1.96$; $t_{(0.01;499)} = 2.59$; $t_{(0.001;499)} = 3.31$			

4. Final Remarks, limitations of the study and future lines of research

In order to test the hypotheses posted in the model adapted from previous studies to the Lisbon metropolitan region, we developed the classical steps for assessing the conceptual and the structural model. The scales used in the questionnaire were not modified in order to test the same instrument in a different context, other region with different characteristics and, may be very important, a new situation of economic crisis. We acknowledge the situation studied here is different from that examined in earlier research. In addition, the small and non representative sample used has to be also recognized as important limitations.

In the analysis, individual reflective item reliability has been considered adequate considering the exploratory nature of our study, when an item has a factor loading that is greater than 0.6 on its respective construct, which implies more shared variance between the construct and its indicators than error variance. However, the first problem occurred when the average variance extracted for SR showed only a value of 0,44 because it is recommended that this value should be greater than 0,50 meaning that 50 percent or more variance of the indicators should be accounted for. At this point we can conclude that the measurement model do not satisfied the required conditions. Consequently, the structural model where three of the five hypotheses have been confirmed has to be interpreted with reserve. It is true that the main hypothesis of the model is significant confirming the direct and positive effect of SR on Competitive Success, but it has no sense to analyze the predictive power of the model acknowledging the weak results measuring the constructs involved in the path analysis carried out.

Future lines of research emerge. First the scales used in the future will be modified to suit the precise needs of the investigation and to adapt the questionnaire to specific cultural and economic context. We can consider this work and the first results obtained as a pre-test among Portuguese managers from the most dynamic business area that is Lisbon. We consider this paper a starting point to develop a SR scale for Portuguese economic reality and for Portuguese firms.

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