AN ANALYTICAL STUDY OF CORPORATE SOCIAL RESPONSIBILITY AND FINANCIAL PERFORMANCE IN BANKING SECTOR OF SRILANKA

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ABSTRACT

Corporate Social Responsibility (CSR) reporting has become an increasing trend in the corporate world. It is a relatively new concept but has become a major research topic in the accounting profession. In recent years, few notions have so fully captured the corporate imagination as that of corporate social responsibility (CSR), defined broadly as a company's status and activities with respect to its perceived societal or, at least, stakeholder obligations. While CSR is by no means a new idea, more companies than ever before are backing CSR initiatives such as corporate philanthropy, cause-related marketing, minority support programs, and socially responsible employment and manufacturing practicesand they are doing so with real financial and marketing muscle.The motivations behind why companies make voluntary CSR disclosures are unclear. This paper aims to analytically explore the relationship between Corporate Social Responsibility and financial performance among the ten selected banks in Sri Lankan. CSR is measured by using of "Nila Unit" andfinancial performance is measured using two financial ratios namely; Return on Equity and Return on Assets. For the measurement of "Nila Unit" it was used 77 Key words with relates to corporate social Responsibility. This is carried out to see to what extent CSR activities are affected on each banks financial performance over seven years of time.The results indicates that there is a significant positive relationship between Corporate Social Responsibility and Financial Performance.

Keywords：Corporate Social Responsibility, Return on Equity, Return on Assets

INTRODUCTION

Corporate social responsibility (CSR) has received increased attention from business, the media, and researchers. Empirical studies have examined the relation between CSR and corporate financial performance (CFP), and while the results are mixed, overall the research has found a positive but weak correlation (David P. Baron, Maretno A. Harjoto, and Hoje Jo,2009). Becoming socially responsible for a firm and to improve the corporate performance can be associated with a sequence of bottom-line benefits. Nonetheless in numerous cases, it seems that the time frame of the costs and benefits can be out of alignment the costs are immediate, and the benefits are not often realized quarterly. Nevertheless, many benefits can be recognized as communally responsible firms have enhanced brand image and reputation, consumer's attraction, increase its reputation within the business community by having increased ability to attract capital and trading partners.

Certain studies have been carried out by the researcher Fauzi (2008) in the Indonesian society on social responsibility and the related responsiveness. He has focused on the corporate social responsibility disclosures in plenty of firms by the help of annual report but has not touched managerial perception that is considered as an important approach in the literature.

A large number of major corporations all around the world are adopting corporate social responsibility reporting. In 2002 KPMG produced a report showing that 45 percent of the

250 largest companies worldwide report corporate social responsibility. This was an upsurge from 35 percent in 1999 (Simms, 2002).As per Friedman (1970), he has mentioned that each firm is different to each other when implementing the corporate social responsibility and its activities. The differences are depending on some unique factors such as the size of the specific firm, the involved industry, the firm's business culture, stakeholder demands, and so on.For successful implementation of such activities to enhance the social wellbeing, it is crucial that the corporate social responsibility principles are playing a major role of the firm values and strategic planning.

This paper is aimed to analyze the relationship between Corporate social responsibility and financial performance in selected commercial banks of Sri Lanka. The concept of corporate social responsibility indeed, takes on different meanings depending on the firm or group that uses it.The corporate social responsibility catches a place in the outline of intellectual forums and academic discussions. It should ensure the fact that, whether the corporate social responsibility is sufficiently spoken in the regular processes of corporate bodies, or in Sri Lanka what is the current assessing level of it etc.In the drives of the firms in the banking sector in several countries, is to gather the gains towards the competitiveness to grab the market and to sustain in it. Therefore the responsibility must be based on their corporate objectives as an initial step. Strategies are formed according to the appraisal and requirement of the firm to perk up their performances. The agility or the aptitude of the firm to answer the circumstances presented by the economic doubts can be comprised by their corporate strategies (Roger, 2002).

REVIEW OF LITERATURE

There are plethora of research articles on the topic of corporate social responsibility and the corporate financial performance. According to Margolis and Walsh (2002), one hundred twenty two published studies between 1971 and 2001 empirically examined the relationship between corporate social responsibility and financial performance. Alternatively can see a significant increase in the interest in corporate social responsibility in last years (Young &Thyil, 2009; Park & Lee, 2009; Gulyas, 2009; McGehee, Wattanakamolchai, Perdue & Calvert (2009) and has become one of the most vital topics compared with others.

In between 1970 to 1995 ; 51 studies carried out, 33 found a positive relationship, 9 found a negative relationship and 9 found no relationship between CSR and financial performance (Chand 2006). A positive relationship between market value and CSR was found. This meant that investors were investing more in firms who reported CSR than those who did not. This provides some evidence of the existence of the 'ethical investors.' Cochran and Wood (1984) examined the relationship between CSR and corporate financial performance (CFP) by using new (at the time) statistical research tools to look at financial variables working as moderating variables.The first study to find a negative relationship between CSR and financial performance was Vance (1975). The study looked at share price and found that in building a portfolio an investor would be better off investing in companies who reported little or no CSR. His concluding comment, "companies have more reasons to be socially responsible than only how it affects the per share value of their common stock"3 summed up Vance's findings.The relationship between CSR and financial performance may be different across industries (Fry and Hock 1976). Fry and Hock loosely looked at members of the oil industry such as Texaco and concluded that the amount of CSR did not increase or decrease the profitability of the firm. Fry and Hock put any change in financial performance down to an increase in firm size. Their concluding comments also suggest that the firm's size and public image management also determine the amount of CSR reporting undertaken.

As Warhust (2001) pointed out that there are three major elements of corporate social responsibility. They are the product use, business practice and distribution of profits. The product use focuses on contribution of industrial products which help in wellbeing and quality of life of the society and its content. The business practice focuses on good corporate governance and gives high impetus for the environmental wellbeing and equity. Finally the distribution of profits focuses on equitably across different societies, in particular the host community.

Based on the Sri Lankan context average of the listed companies spend about 6.6% of their turnover on CSR related activities,including training,research and community work but in the case of relationship between CSR activities and financial performance only in employee relations and customer/supplier relations have the most significant alliance with respect to CSR and community relations and environment is not that much significant with perceived benefits of CSR.(Sheham&Jahfer 2011)

Activities related to corporate social responsibility not only increase revenue but also the initiatives can dramatically reduce operating costs. By adopting proper principles and processes it will motivates employees to reassess their firm social practices and to seek more efficient ways of operating and will get the ability to attract and retain its personnel (Turban & Greening 1997).There have been a large number of papers written to empirically examine the relationship between CSR reporting and a firm's financial performance. By 1995 there had been 51 papers looking into this relationship. However the research that has been carried out is varied in its results (Chand 2006) so it is difficult to establish whether there is a relationship between the two variables.

METHODOLOGY

Sample and data collection was mainly for ten selected banks with different size scales in the banking sector, as the sample is expected to use in this study for over 07 years of time period commencing from 2009-2015 based on bank's audited annual reports, internet sources, journals and the publications from the Central bank of Sri Lanka which based on secondary data sources.The data sources are the selected Measurement of corporate social responsibility in this study take up a disclosures scoring method based on content analysis. Items selected for enclosure were based on the relevance to the Sri Lankan context. The list of corporate social responsible keywords was generated throughout from the Hackston and Milne's (1996) by the list of corporate social responsible sentences which is also known as the "Decision Rules" used for the above mentioned content analysis by extracting particular social responsible words.

The independent variable of the study is the corporate social responsibility practices of employee relations, environment, community involvement and product along with its sub items, and the dependent variable is the corporate financial performance. Therefore this particular study will shows the relationship between corporate social responsibility activities and the financial performance in the banking industry in Sri Lanka

A content analysis was carried out on the ten selected banks annual reports which were in PDF format by searching for 77 different corporate social responsible key words and their related terms.Regarding to this, in this research Anycount 6.0 software along with the Adobe Reader and Microsoft word employed particularly to find and verify words appropriate with defined keywords.Counting words may appear be simplified of a rich and diverse describe of firms corporate social responsibility activities. Further, by applying those keywords into selected reports, the unit of measurement of each firm over five years was calculated by the following equation which was named as the Nila unit (Nila& Masanori, 2010).

$$\text{Unit of measurement} = \frac{\text{Number of CSR related words}}{\text{Total number of words in a report}} * 100$$

This paper uses a measurement in order to measure the financial performance of the selected banks by using the Return on Equity (ROE) and return on assets (ROA). which can be treated as accurate measures of the financial performance in any organization. These are the two most commonly used measures for financial performance and will therefore provide the most comparable results (Griffin and Mahon 1997).

RESULTS AND DISCUSSIONS

Descriptive Statistics

The corporate social responsible words for ten commercial banks range from one to seventy seven key words in the selected banks' annual reports. Table 1 gives an idea about that the Nila Unit measurement for the ten banks over seven consecutive years descriptively.

Table 01 : Descriptive Statistics

Descriptive Statistics				
		CSR	ROE	ROA
N	Valid	70	70	70
	Missing	0	0	0
Mean		1.50617	19.0724	1.9344
Std. Error of Mean		.037545	1.02233	.16927
Median		1.53600	17.9350	1.7000
Mode		1.425[a]	2.89[a]	1.23[a]
Std. Deviation		.314120	8.55346	1.41618
Variance		.099	73.162	2.006
Range		1.757	46.31	12.08
Minimum		.567	2.89	.19
Maximum		2.324	49.20	12.27
a. Multiple modes exist. The smallest value is shown				

The number of cases in the data set is 70 where it represents the ten banks during seven years time period. The data range goes from 0.5 to 2.3 in CSR, 2.89 to 49.2 in ROE and 0.19 to 12.3 in ROA. The average of the data set or the mean score is 1.51 in CSR, 19.07 in ROE and 1.93 in ROA. The amount of variability in the distribution of CSR and ROA lies the mean value without high dispersion by having 0.31 and 1.42 respectively. ROE is somewhat dispersed from the average value by 8.55 comparatively. It further means that the individual data points are different from each other.

Correlation between CSR and ROE and ROA

Correlation measures the strength and the direct relationship of the variables in this study. The Table 02 represents the Pearson correlation matrix for the identified variables of corporate social responsibility, return on equity and return on assets. There can be seen positive relationship between corporate social responsibility and return on equity and return on assets 35.2 percent and 31.5 percent respectively. The P-value is at the level of 0.003 and 0.008 respectively in return on equity and return on assets. The P-value should be less than 0.05 in order to show the significance of the variables, so as per lower P-values in both by return on equity and return on assets there can be seen a significant relationship.

Table 2 : Pearson Correlation Matrix

Pearson Correlations Matrix				
		CSR	ROE	ROA
CSR	Pearson Correlation	1	.352**	.315**
	Sig. (2-tailed)		.003	.008
	N	70	70	70
ROE	Pearson Correlation	.352**	1	.464**
	Sig. (2-tailed)	.003		.000
	N	70	70	70
ROA	Pearson Correlation	.315**	.464**	1
	Sig. (2-tailed)	.008	.000	
	N	70	70	70
**. Correlation is significant at the 0.01 level (2-tailed).				

As per the Pearson correlation matrix it shows that there is a positive relationship between the independent (CSR) and the dependent variables (ROE, ROA). Even though the relationship or the correlations among the variables are not strong they have correlated by 35.2 percent with return on equity and 31.5 percent with return on assets.

Regression analysis between CSR and ROE

Table 03 : Regression analysis between CSR and ROE

Model Summary									
Mode l	R	R Square	Adjusted R Square	Std. Error of the Estimate	Change Statistics				
					R Square Change	F Change	df1	df 2	Sig. F Change

1	.352[a]	.124	.111	8.06385	.124	9.633	1	68	.003
a. Predictors: (Constant), CSR									

ANOVA[b]						
Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	626.406	1	626.406	9.633	.003[a]
	Residual	4421.744	68	65.026		
	Total	5048.150	69			
a. Predictors: (Constant), CSR						
b. Dependent Variable: ROE						

R is the square root of R-Squared and is the correlation between the observed and predicted values of dependent variable of return on equity which at about 35.2 percent. Adjusted R-square defines that, as predictors are added to the model, each predictor will explain some of the variance in the dependent variable of return on equity simply due to chance. It has attempted to yield a more honest value to estimate the R-squared for the population. The value of R-square was 12.4 percent, while the value of Adjusted R-square was 11.11 percent.

The F-value is the Mean Square Regression (626.406) divided by the Mean Square Residual (65.026), yielding F=9.633. It provide the answer that the independent variable (CSR) is reliably predict the dependent variable (ROE). The p-value has been compared to alpha level (typically 0.05) and, arrived at a value of 0.003.Therefore it could be concluded that the CSR shows a statistically significant relationship with the dependent variable of ROE. Even though could conclude it in that manner it addresses the ability of the independent variable (CSR) to predict the dependent variable (ROE).

Regression analysis between CSR and ROA

Table 04 : Regression analysis between CSR and ROA

Model Summary									
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Change Statistics				
					R Square Change	F Change	df1	df2	Sig. F Change
1	.315[a]	.099	.086	1.35385	.099	7.500	1	68	.008
a. Predictors: (Constant), CSR									

ANOVA[b]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	13.747	1	13.747	7.500	.008[a]
	Residual	124.638	68	1.833		
	Total	138.385	69			
a. Predictors: (Constant), CSR						
b. Dependent Variable: ROA						

As per Table 04 , R is the correlation between the observed and predicted values of dependent variable of return on asset which at about 31.5 percent. Coefficient of determination or the R-Square indicates that 8.6 percent of the variance in return on assets scores that can be predicted from the variable of corporate social responsibility.

The value of R-square was 9.9 percent, while the value of Adjusted R-square is8.6 percent. It means that each additional predictor will not explain some of the variance in the dependent variable of return on assets. The F-value is the Mean Square Regression (13.747) divided by the Mean Square Residual (1.833), yielding F=7.5. It provides the answer that the independent variable (CSR) is reliably predict the dependent variable (ROA). The p-value has been compared to alpha level (typically 0.05) and, arrived at a value of 0.008.Therefore it could be concluded that the CSR shows a statistically significant relationship with the dependent variable of ROA. Even though could conclude it in that manner it addresses the ability of the independent variable (CSR) to predict the dependent variable (ROA).

CONCLUSION

The aim of this exacting study was to empirically examine the degree to which corporate social responsibility contributes to financial performance of Sri Lankan banks.Most managers identify certain benefits for a business being socially responsible, but most of these benefits are still hard to quantify and measure. This study have attempted to address the question whether corporate social performance is linked to financial performance, the dimensions of corporate social responsibility, the extent to which social reporting have impacted on banks' performance etc.

An imperative subject matter is the discrepancy of the financial performance measures and corporate social responsibility reporting measures. This paper used the two most common financial performance measures, return on assets and return on equity. A content analysis was carried out to measure a firm's corporate social responsibility disclosures based upon word counting. The list of corporate social responsible keywords was generated throughout from the Hackston and Milne's (1996) by the list of corporate social responsible sentences which is also known as the "Decision Rules" used for the above mentioned content analysis by extracting particular social responsible words. The word counting has been treated as the most popular measurement and it has been extracted to an excel sheet for the purpose of quantifying the qualitative data by converting them into a unit of measurement. The unit of measurement was selected as per the previous research on "Quantitative Relations between Corporate Social Responsibility Activity and Share Price: Introducing "Nila" Unit". Based on their content analysis of measuring corporate social responsibility using "Nila unit" of measurement it was simple to look forward in correlation and regression measurement.

Using most popular empirical methods, of content analysis the variables were tested the sign of the relationship between corporate social responsibility and financial performance. This study focuses on developing economies and on Sri Lanka specifically. Using a sample of seventy annual reports including audited financial statements of ten selected banks in Sri Lanka this study examines the impact of corporate social responsibility activities and its disclosures on financial performance measured with return on equity (ROE) and return on assets (ROA).

The results of two areas of correlation and regression analysis have provided conclusions towards such relationship. The correlation matrix is an evidence for that corporate social responsibility has a positive relationship with the financial performance measurement of return on equity with the return on assets. As per the further analysis of regression it provide the answer that there is a positive significant relationship.

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