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Corporate Social Responsibility and Financial Performance in Developing Economies: The Nigerian Experience

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Abstract

Corporate social responsibility (CSR) has the potential to make positive contributions to the development of society and businesses. Organisations are beginning to see the benefits from setting up strategic CSR agendas. The increasing attention to CSR is based on its capability to influence firms' performance. The CSR movement is spreading over the world and in recent years a large number of methods and frameworks have been developed, the majority being developed in the West. This study focuses on developing economies and on Nigeria specifically. Using a sample of forty audited financial statements of quoted companies in Nigeria, this study examines the impact of CSR activities on financial performance measured with Return on Equity (ROE) and Return on Assets (ROA). The results show that CSR has a positive and significant relationship with the financial performance measures. These results reinforce the accumulating body of empirical support for the positive impact of CSR on financial performance.

Keywords: Corporate Social Responsibility, Financial Performance, Developing Economies-Nigeria

1. Introduction

The social impact of corporations is becoming a very important issue in business administration (Fiori *et al.* 2007). The performance of business organizations is affected by their strategies and operations in market and non-market environments. Hence, there is a debate on the extent to which company directors and managers should consider social and environmental factors in making decisions. In essence, Corporate Social Responsibility (CSR) may be described as an approach to decision making which encompasses both (social and environmental) factors. It can therefore be inferred that CSR is a deliberate inclusion of public interest into corporate decision making, and the honoring of a triple bottom line which are People, Planet and Profit. (Harpreet 2009). CSR has been defined in various ways. Majority of these definitions integrate the three dimensions: economic, environmental and social aspects into the definition, what is usually called the triple bottom line. The triple bottom line is considering that companies do no only have one objective, profitability, but that they also have objectives of adding environmental and social value to society (Mirfazli 2008).

CSR has been defined as a "concept whereby companies integrate social and environmental concerns in their business operations and in their interaction with their stakeholders on a voluntary basis" (Green Paper Promoting a European Framework for Corporate Social Responsibility 2001). Helg (2007) also defines CSR as the set of standards to which a company subscribes in order to make its impact on society.

A wide variety of definitions of firm performance have also been proposed in the literature. Both accounting and market definitions have been used to study the relationship between corporate social responsibility and firm performance (Orlitzky *et al.* 2003). However, since most social responsibility scholars seek to understand the ways that socially responsible corporate activities can create or destroy shareholder wealth, market definitions of firm performance seem likely to be more appropriate than accounting definitions of firm performance in this context (Margolis & Walsh 2001).

The history of formalized CSR in Nigeria can be traced back to the CSR practices in the oil and gas multinationals. The CSR activities in this sector are mainly focused on remedying the effects of their extraction activities on the local communities. The companies provide pipe-borne waters, hospitals and schools. Many times, these initiatives are ad hoc and not always sustained (Amaeshi *et al.* 2006). The development of CSR in Nigeria has a somewhat different development phase. While CSR as a concept in the West was developed as early as in the 1950´s the concept of CSR is a relatively new phenomena in

Nigeria. Contrary to the West, the main influencing factors driving the CSR agenda in Nigeria have been foreign. Multinational companies operating in Nigeria together with foreign governments and international NGOs have been the primary drivers (Helg 2007).

The Nigerian government has through its National Economic Empowerment and Development Strategy (NEEDS) set the context by defining the private sector role by stating that "*the private sector will be expected to become more proactive in creating productive jobs, enhancing productivity, and improving the quality of life. It is also expected to be socially responsible, by investing in the corporate and social development of Nigeria…*" (Nigerian National Planning Commission 2004).

Little research exists on the CSR and financial performance in Nigeria apart from some research studies on multinational companies operating in Nigeria. This paper seeks to contribute to the existing body of work in this area by examining the extent to which corporate social responsibility contributes to financial performance of Nigerian listed firms. The rest of the paper is structured as follows: the next section reviews the existing work on corporate social responsibility and firm performance. Section three provides a brief description of the data employed for the empirical analysis and specifies the estimation models. Section four presents the analysis of data and interpretation of results. The final section summarizes the findings and draws out some policy implications.

2. Literature Review

The concept of Corporate Social Responsibility (CSR) in its present form originated in 1950's when Bowen wrote on "The Social Responsibilities of a Businessman" (Carroll 1999). Since then the notion of CSR has come to dominate the society-business interface and many theories and approaches have been proposed. With respect to CSR and firm's financial performance, the literature consists of three principal strands: (i) the existence of a positive correlation between CSR and financial results (ii) the lack of correlation between CSR and financial results; and (iii) the existence of a negative correlation between CSR and financial results.

Some proponents of the first strand (Soloman & Hansen 1985; Pava & Krausz 1996; Preston & O'Bannon 1997; Griffin & Mahon 1997) find that investment in Corporate Social Responsibility have a big return in terms of image and overall, financial result; the related benefits, in fact are bigger than the related costs. Literature reveals the existence of many positive externalities that are linked to CSR in its bid to respond to stakeholders' requirements. Clarkson (1995) and Waddock & Graves (1997) believe that satisfying the interest of stakeholders (shareholders, employees, suppliers, community, environment and so on) and being accountable to them may actually have a positive impact on all firm dimensions, particularly financial performance. Positive reputations have often been linked to positive financial returns. Roberts & Dowling (2002); Fombrun *et al*. (2000); Porter & Van Der Linde (1995) and Spicer (1978), posit that CSR initiatives can lead to reputation advantage as improvements in invested trust, new market opportunities and positive reactions of capital market would enhance organisation's financial performance.

The idea of the second group of theorists is that there is no relationship between corporate social responsibility and corporate financial performance (McWilliams & Siegel 2000; Ullmann 1985; Aupperle *et al*. 1985; Waddock *et al.* 1997). Waddock *et al.* (1997) explain that a neutral relation may suggest that many variables in the relation between social and financial performance make the connection coincidental. McWilliams *et al.* (2000) find that the firms supplying corporate social responsibility products to their own customers have a different demand curve compared to those with no corporate social responsibility. Ullmann (1985) underlines that no clear tendency can be recorded between connections on social information, social performance and economic results. The main reason for this appears to be the theory's inadequacy, inappropriate keyword definitions and lack of empirical materials. It was observed that important aspects are not just social performance and economic but also "information" about social performance and that only a few studies have analyzed this three-dimensional relation.

Other studies highlight the impossibility of defining the sign of the existing relation between corporate social responsibility and performance, both in the short term-on the basis of Abnormal return measure and market actions-and in the long term (Aupperle *et al.*1985).

Finally, the idea of that negative relationship exists between CSR and financial performance is focused on empirical studies and contributions that refer to managerial opportunism hypotheses. Preston *et al.* (1997) point out that manager can reduce investments in corporate social responsibility in order to increase short term profitability (and, in this way, their personal compensation). This point seems to be really interesting, due to the fact that other authors (Barnea & Rubin 2006) suggest the existence of an opposite trend linked to the same phenomena (Managerial opportunism). Waddock *et al.* (1997) assumed that companies with responsible behavior may have a competitive disadvantage, since they have unnecessary costs. These cost, fall directly on the bottom line and would necessarily reduce shareholders profits and wealth. Both short term analyses based on measuring abnormal returns (Wright & Ferris 1997), Market measures and long term studies (Vance 1975) have negative relationship between performance and corporate social responsibility.

Empirical studies of the relationship between CSR and financial performance comprise essentially two types. The first uses the event study methodology to assess the short-run financial impact (abnormal returns) when firms engage in either socially responsible or irresponsible acts (Wright *et al.* 1997; Posnikoff 1997; McWilliams *et al.* (1997). The second type of study examines the relationship between some measure of corporate social performance (CSP) and measures of long term financial performance, by using accounting or financial measures of profitability (Cochran & Wood 1984; Aupperle *et al*. 1985; Waddock *et al*. 1997). The relationship between corporate social responsibility and corporate financial performance has been studied intensively with mixed results. In a survey of 95 empirical studies conducted between 1972-2001, Margolis *et al*. (2001), report that: "When treated as an independent variable, corporate social performance is found to have a positive relationship to financial performance in 42 studies (53%), no relationship in 19 studies (24%), a negative relationship in 4 studies (5%), and a mixed relationship in 15 studies (19%)." In general, when the empirical literature assesses the link between social responsibility and financial performance the conclusion is that the evidence is mixed.

Measuring CSR has always been a difficult task as there is little consensus about which measurement instrument to apply. In many cases, subjective indicators are used. Similarly, measuring financial performance is equally difficult as there is little consensus about which measurement instrument to apply. Many researchers use market measures (Alexander & Buchholz 1978; Vance 1975), others put forth accounting measures (Waddock *et al*. 1997; Cochran *et al.* 1984) and some adopt both of these (McGuire *et al*. 1988). These two measures, which represent different perspectives of how to evaluate a firm's financial performance, have different theoretical implications (Hillman & Keim 2001) and each is subject to particular biases (McGuire *et al.* 1988). The use of different measures, needless to say, complicates the comparison of the results of different studies (Tsoutsoura 2004).

In line with previous researches (Brammer *et al*. 2006; Fiori *et al.* 2007), the study adopt the first three measures of social performance: community performance, employee performance (health and safety, training and development, equal opportunities policies, equal opportunity systems, employee relations, systems for job creation and job security) and environmental performance (policies, management systems, and reporting) social measures.

3. Methodology

The research design is content analysis which involves tracing of sentences of each component of the corporate social responsibility disclosed in annual reports of Nigeria companies in the sample. This study is based on the voluntary disclosure index constructed using the annual report of the sampled companies.

Since this study is on the impact of corporate social responsibility disclosure on company financial performance, we used a sample of Nigerian listed companies (firms that prepare corporate social responsibility reports).

The population of this research work is made up of all the companies listed on the Nigerian Stock Exchange. Each company in the population must have finished its obligation in delivering annual report of the year ended 2007. A sample size of forty (40) listed companies on the Nigerian Stock Exchange was randomly selected. The sample size excludes banks and Insurance Companies. The justification for choosing non-financial sector is due to the argument that banks and other financial institutions are not directly impacting negatively on their environment and also due to their specific core business and risk profile, they would have altered the average results (Singh and Davidson 2003).

Dependent variable of the study is financial performance which is represented by ROE (measured as a proportion of Profit after tax to issued share capital) and ROA (measured as the proportion of Profit after tax to total assets). The independent variables/parameters are community performance, environment management system and employee relations.

The regression model is represented as follows:

$$Y_{ROE} = \alpha_0 + \alpha_1 CP + \alpha_2 EMS + \alpha_3 ER$$
$$Y_{ROA} = \beta_0 + \beta_1 CP + \beta_2 EMS + \beta_3 ER$$

Where:

α_0 , β_0 = Intercept coefficient

α_1 , β_1 = Coefficient for each of the independent variables

CP = Community Performance

EMS = Environment Management System

ER = Employee Relations

4. Data Analysis and Presentation of Results

This section of the study is devoted to presenting the results of the analysis performed on the data collected to test the propositions made in the study and answer the research questions. Analyses were carried out with the aid of the Statistical Package for Social Sciences, (SPSS Version 15.0).

A Pearson correlation analysis was performed on the dependent and independent variables in order to determine the degree of relationship among them. The results are shown in Table. 1 ROE is significantly correlated to community performance and environmental management system (both at $p <$ 5% level). Similarly, ROE is also significantly correlated to system for employee relations at 10% significant level. This means that as corporate social responsibility increases organisation earnings increases.

Table 2 presents summary of regression model result. The value of R and R^2 are 0.559 and 0.313 respectively. The R value of 0.559 represents the correlation between ROE and the CSR variables. The R^2 which indicates the explanatory power of the independent variables is 0.313. This means that 31.3% of the variation in ROE is explained by the independent variables. The R^2 value as revealed by the result is quite low which means that about 69% of the variation in the dependent variable is unexplained by the model, denoting a weak relationship between the explanatory variable and ROE. The standard error of the estimate is 2.348, which explains how representative the sample is likely to be of the population.

The fitness of the model can also be explained by F-ratio (F) in Table 3. According to Andy (2000), "a good model should have a large F-ratio (greater than one at least)". The F-ratio in the model is 5.460, which is significant at $p < 0.005$. This means that there is significant evidence to infer that at least one of the explanatory variables is linearly related to ROE and the model seems to have some validity.

Table 4 shows the results of the coefficients of regression model with ROE as dependent variable. The t-values for community performance, environment management system and employee relations are 2.150, 2.279 and 1.712 respectively. These values are also significant at p-values < 0.05 and 0.10. It can be deduced from the results that for each additional naira spent on community performance, environment management system and employee relations, ROE increases on the average by 30kobo, 32kobo and 24kobo respectively holding other explanatory variables constant.

A Pearson correlation analysis was performed on the variables in order to determine the degree of relationship among them. The results are shown in Table 5. ROA is positively and significantly correlated to community performance at p = 0.010. Similarly, a positive but not significant relationship exists between ROA and the other CSR variables.

Table 6 presents summary of regression model result. The R^2 value, which indicates the explanatory power of the independent variables, is 0.210. This means that 21% of the variation in ROE is explained by the independent variables. It can therefore be concluded that the R^2 value is quite low since about 79% of the variation in the dependent variable is unexplained by the model, denoting a weak relationship between the explanatory variable and EPS.

The fitness of the model can also be explained by F-ratio (F) in Table 7. The F-ratio is 3.190, which is significant at $p \leq 0.05$. This means that there is significant evidence to infer that at least one of the explanatory variables is linearly related to ROA. This confirms the existence of the relationship between ROA and community performance established in the correlation analysis above.

Table 8 shows the results of the coefficients of regression model with ROA as dependent variable. The t-values for community performance, environment management system and employee relations are 2.596, -0.285 and 1.442 respectively. Out of three CSR variables only community performance has a statistically significant impact on ROA. This means that for each additional naira spent to improve the community ROA increases on the average by 39kobo. The remaining two CSR variables do not have any statistically significant impact on ROA. However, it is worthy to note that for each additional naira spent on environment management system ROA reduces by 4k. On the other hand, for every additional naira spent on employee relations ROA increases on the average by 22kobo, holding other explanatory variables constant.

5. Conclusion

The aim of this study was to empirically examine the extent to which corporate social responsibility contributes to financial performance of Nigerian listed firms. In achieving this aim, the study obtained data on variables which were believed to have relationship with CSR and financial performance. These variables included ROE, ROA, CP, EMS and ER. This study focuses on developing economies and on Nigeria specifically. Using a sample of forty audited financial statements of quoted companies in Nigeria, this study examines the impact of CSR activities on financial performance measured with Return on Equity (ROE) and Return on Assets (ROA). The results show that CSR has a positive and significant relationship with the financial performance measures. These results reinforce the accumulating body of empirical support for the positive impact of CSR on financial performance. Based on the findings, the study recommends that corporate entities in Nigeria should invest in CSR activities in all its ramification in order to boost their image/reputation thereby increasing their returns.

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Appendices

Table 1: Correlation Matrix of ROE as a Financial Performance Measure and CSR Variables

		ROE	COMMUNITY	ENVIRO_MGT_SYS	EMPLO_RELATIONS
ROE	Pearson Correlation	1	.381(*)	.395(*)	.297(**)
	Sig. (2-tailed)		.015	.012	.063
	N		40	40	40
COMMUNITY	Pearson Correlation		1	.173	.095
	Sig. (2-tailed)			.286	.561
	N			40	40
ENVIRO_MGT_SYS	Pearson Correlation			1	.093
	Sig. (2-tailed)				.569
	N				40
EMPLO_RELATIONS	Pearson Correlation				1
	Sig. (2-tailed)				
	N				

* Correlation is significant at the 0.05 level (2-tailed).

** Correlation is significant at the 0.01 level (2-tailed).

Table 2: Summary of Regression Model Result

Model Summary				
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.559(a)	.313	.255	2.34815

a Predictors: (Constant), COMMUNITY ,ENVIRO_MGT_SYS, EMPLO_RELATIONS

b Dependent Variable: ROE

Table 3: Summary of Anova

Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	90.313	3	30.104	5.460	.003(a)
	Residual	198.498	36	5.514		
	Total	288.811	39			

a Predictors: (Constant), COMMUNITY, ENVIRO_MGT_SYS, EMPLO_RELATIONS

b Dependent Variable: ROE

Table 4: Summary of Coefficients of Regression Model

Model		Unstandardized Coefficients		Standardized Coefficients	T	Sig.
		B	Std. Error	Beta	B	Std. Error
1	(Constant)	-.161	.641		-.251	.803
	COMMUNITY	.644	.300	.303	2.150	.038(*)
	ENVIRO_MGT_SYS	1.061	.465	.321	2.279	.029(*)
	EMPLO_RELATION	.644	.376	.238	1.712	.096(**)

a Dependent Variable: ROE

*significant at 0.05 level

**significant at 0.01 level

Table 5: Correlation Matrix of ROA as a Financial Performance Measure and CSR Variables

		COMMUNITY	ENVIRO_MGT_SYS	EMPLO_RELATIONS	ROA
COMMUNITY	Pearson Correlation	1	.179	.095	.405(*)
	Sig. (2-tailed)		.286	.561	.010
	N		40	40	40
ENVIRO_MGT_SYS	Pearson Correlation		1	.093	.045
	Sig. (2-tailed)			.569	.784
	N			40	40
EMPLO_RELATIONS	Pearson Correlation			1	.248
	Sig. (2-tailed)				.122
	N				40
ROA	Pearson Correlation				1
	Sig. (2-tailed)				
	N				

a Dependent Variable: ROA

* Correlation is significant at the 0.01 level (2-tailed).

Table 6: Summary of Regression Model Result

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.458(a)	.210	.144	22.58320

Predictors: (Constant), ENVIRO_MGT_SYS, EMPLO_RELATIONS, COMMUNITY

Source: SPSS Output.

Table 7: Summary of Anova

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	4881.202	3	1627.067	3.190	.035(a)
	Residual	18360.026	36	510.001		
	Total	23241.228	39			

Predictors: (Constant), COMMUNITY, ENVIRO_MGT_SYS, EMPLO_RELATIONS,

Dependent Variable: ROA

Table 8: Summary of Coefficients of Regression Model

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta	B	Std. Error
1	(Constant)	-.546	6.160		-.089	.930
	COMMUNITY	7.478	2.880	.392	2.596	.014(*)
	ENVIRO_MGT_SYS	-1.277	4.476	-.043	-.285	.777
	EMPLO_RELATION	5.220	3.620	.215	1.442	.158

Dependent Variable: ROA

*Significant at 0.01

Table 9: List of Nigerian Firms used in the Study

S/N	**Company**	**Industries**
1.	Hallmark Paper Products Plc	Printing and Publishing
2.	Oando	Petroleum (Marketing)
3.	PZ Cussons	Industrial/Domestic Products
4.	Dumer (Nigeria) Limited	Building Materials
5.	Costain (W.A) Plc	Construction
6.	African Petroleum (AP)	Petroleum (Marketing)
7.	Longman	Printing and Publishing
8.	Mobil Oil Nigeria Plc	Petroleum (Marketing)
9.	Conoil Plc	Petroleum (Marketing)
10.	Total Nigeria Plc	Petroleum (Marketing)
11.	Sheraton Hotel	Hotel and Tourism
12.	Dunlop Nigeria Plc	Automobiles and Tyres
13.	NAHCO	Construction
14.	Interlinked	Commercial / Services
15.	GSK	Industrial / Domestic Products
16.	Dangote	Industrial / Domestic Products
17.	Unilever	Industrial / Domestic Products
18.	Ashakecem Plc	Building Materials
19.	Thomas Wyatt	Construction

20.	Premier Paints	Chemical and Paints
21.	University Press Plc	Printing and Publishing
22.	Trans-National Express	Commercial/Services
23.	UACN Property Development	Real Estate
24.	Nampak Nigeria	Packaging
25.	SPN Packaging	Packaging
26.	Vitafoam	Industrial / Domestic
27.	John Holt	Construction
28	Briscoe (Nigeria) Plc	Automobiles / Tyres
29.	Flour Mills of Nigeria	Industrial / Domestic
30.	DN Mayer Plc	Chemical and Paints
31.	Berger Paints	Chemical and Paints
32.	Airline Service and Logistics Plc	Airlines
33.	May and Baker (M & B)	Industrial / Domestic
34.	CAP Plc	Chemical and Paints
35.	BOC Gases Plc	Chemical and Paints
36.	UAC	Industrial / Domestic
37.	AG Leventis Nigeria Ltd	Industrial / Domestic
38.	Benue Cement Company Plc	Building Material
39.	Welmeth	Building Material
40.	Julius Berger Nigeria Plc	Construction