Corporate Social Responsibility and Its Impact on Corporate Profitability: Some Evidences from Selected Private Commercial Banks in Bangladesh

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Abstract

This paper is an endeavor to investigate the linkage between Corporate Social Responsibility (CSR) and Profitability. The researcher has considered CSR as an independent variable and Return on Asset (ROA), Return on Equity (ROE) and Earning Per Share (EPS) as dependent variables. Firstly, the researcher has presented the CSR activities of different selected banks from year 2007 to 2010. Secondly, a simple regression analysis is performed to investigate the relationship between dependent and independent variables. The study found that there is a significant negative relationship between CSR and ROA. The study also found that there is no relationship among ROE, EPS and CSR.

Keywords: Corporate Social Responsibility, Return on Asset, Return on Equity, Earning Per Share

1.1. Introduction

The field of corporate social responsibility has grown exponentially in the last decade. More than half of the Fortune 1000 companies issue corporate social responsibility (CSR) reports (Tsoutsoura et al., 2004). A large number of companies are engaged in a serious effort to define and integrate CSR into all aspects of their businesses. An increasing number of shareholders, analysts, regulators, activists, labor unions, employees, community organizations, and news media are asking companies to be accountable for an ever-changing set of CSR issues. There is increasing demand for transparency and growing expectations that corporations measure, report, and continuously improve their social, environmental, and economic performances. The definition of corporate social responsibility is still debatable. According to Business for Social Responsibility (BSR), corporate social responsibility is defined as "achieving commercial success in ways that honor ethical values and respect people, communities, and the natural environment." McWilliams et al. (2001) describe CSR as "actions that appear to further some social good, beyond the interest of the firm and that which is required by law." A point worth noticing is that CSR is more than just following the law (McWilliams et al., 2001). Alternatively, according to Frooman (1997), the definition of what would exemplify CSR is the following: "An action by a firm, which the firm chooses to take, that substantially affects an identifiable social stakeholder's welfare." A socially responsible corporation should take a step forward and adopt policies and business practices that go beyond the minimum legal requirements and contribute to the welfare of its key stakeholders. CSR is viewed, then, as a comprehensive set of policies, practices, and programs that are integrated into business operations, supply chains, and decision-making processes throughout the company and usually include issues related to business ethics, community investment, environmental concerns, governance, human rights, the marketplace as well as the workplace. Each company differs in how it implements corporate social responsibility, if at all. The differences depend on such factors as the specific company's size, the particular industry involved, the firm's business culture, stakeholder's demand, and how historically progressive the companies are engaging in CSR. Some companies focus on a single area, which is regarded as the most important for them or where they have the highest impact or vulnerability—human rights, for example, or the environment—while others aim to integrate CSR in all aspects of their operations. For successful implementation, it is crucial that the CSR activities are part of the corporation's values and strategic planning, and that both management and employees are committed to them. Furthermore, it is important that the CSR strategy is aligned with the company's specific corporate objectives and core competencies.

1.2. Objectives of the Study

The main objective of the study is to analyze the CSR activities and its impact on financial performance of the selected banks operating in Bangladesh. The specific objectives are listed below:

- To identify the CSR activities performed by the selected commercial banks.
- To investigate the relationship between CSR and profitability of the selected commercial banks.

1.3. Methodology

1.3.1. Sample Selection

Total 47 banks are currently operating in Bangladesh. The researcher selected only privately commercial banks for this study purpose. Public commercial banks, foreign banks and investment banks were not taken into consideration due to their difference in operation and direct government regulation. Out of 29 commercial banks 8 banks were selected for the study which represents 27.59% of the total population. The reason behind such selection was only these 8 banks have been investing on CSR for last 4 years continuously according to Bangladesh Bank Report on CSR on July, 2011. The selected banks were Eastern Bank Limited (EBL), Bank Asia

Limited (BAL), Dutch Bangla Bank Limited (DBBL), Pubali Bank Limited (PuBL), Trust Bank Limited (TBL), NCC Bank Limited (NCCBL), South East Bank Limited (SEBL) and Brac Bank Limited(BBL).

1.3.2. Secondary Data

The researchers were collected data from Bangladesh Bank Report July 2011 on CSR performance. The ROA, ROE and EPS were collected from the annual report of the selected banks from 2007 to 2010.

1.3.3. Hypothesis

Null Hypothesis (H_1): There is no relationship between CSR and profitability.

Alternative Hypothesis (H_0): There is a significant relationship between CSR and profitability.

1.3.4. Data Analysis

Statistical Package for the Social Sciences (version 16.0) was used for data analysis. Moreover, simple regression model and Pearson's correlation matrix were mainly used to examine the impact of CSR investments. In order to test null hypothesis, t-test was also used in the study.

1.4. Modeling Approach

To measure the CSR, this research had used the CSR index calculated from the CSR disclosures provided by the annual report of firms which the criteria are classified by *Global Reporting Initiative* (GRI). This index is calculated by summing up all scores for all items of CSR by giving 1 (one) point if disclose and 0 (zero) if not disclose for each firm and then divide the summation by the number of items expected form j th firm. CSRDI calculation formula was as follow: (Haniffa et al., 2005; Wondabio, 2007).

$$CSRDIj = \frac{\sum Xij}{nj}$$

in which:

CSRDIj : Corporate Social Responsibility Disclosure Index company j

jn : total items for company j, $n \leq 7$

Xij : dummy variable; 1= if item i was disclosed; 0 = if item i was not disclosed. Thus,

$0 \leq CSRDIj \leq 1$

This research defines financial performance as accounting definition. Therefore, the financial performance indicated by ROE, EPS and ROA. To measure the firm financial performance based on the accounting definition, this research uses ROE, EPS and ROA formula, as follows:

$$ROE = \frac{NEAT}{Equity}$$

$$ROA = \frac{NEAT}{Assets}$$

$$EPS = \frac{NEAT}{\text{Number of Outstanding Shares}}$$

Where NEAT is net earnings after tax, asset is total asset, and equity is net equity of the firm stated in annual report.

1.5. Literature Review

Theoretical studies linking CSR and financial performance are few both nationally and internationally. Siegel et al. (2007) provide an excellent review, and here we highlight some of their observations. In the seminal pieces (Baron, 2001, McWilliams et al., 2001), CSR was linked to profit-maximization by modeling firms, products to contain social attributes competing for socially responsible customers. In other words, firms are responding to a demand for CSR. Other studies highlight the role of asymmetric information. In particular, in exercising CSR, firms can signal to consumers that in being good perhaps even reliable and honest, they will produce better products. Thus, CSR is a form of product differentiation, a form of advertising to establish or sustain brand loyalty (Siegel et al., 2007). The reason the relative authors choose to further study the brand-signaling role of CSR is to understand its actual mechanism. We strongly feel that prior studies, in assuming that consumers believe good firms can make better products, are failing to put all the pieces of the puzzle together. In particular, why should consumers assume good firms can make better products? In fact, this assumption is likely flawed because of two reasons. First, it may be more reasonable to assume that consumers believe efficient firms will produce better products, and that consumers should place the burden of social work on firms specialized for that purpose. Second, it may be unreasonable to assume that firms possess human characters such as goodness. The general signaling role of CSR was also studied by Goyal (2006). That study however is considerably different from the relative authors as it did not consider the brand-value of firms. Rather, Goyal (2006) investigated the signaling role of CSR when firms considering FDI are interested in favorable terms. Our study is similar to Goyal (2006) in that we also use the well-established signaling theory (Spence, 1974; Riley, 2001; Vega-Redondo, 2003; Gibbons, 1992) to perform our analysis. Barnea et al. (2005) depict that in recent years' firms have greatly increased the amount of resources allocated to activities classified as Corporate Social Responsibility (CSR). This increase in CSR expenditure may be consistent with firm value maximization if it is solely a response to changes in stakeholders,, preferences. We find that insider's ownership and leverage are negatively related to the social rating of firms, while institutional ownership is uncorrelated with it. These results support our hypothesis that affiliated shareholders induce firms to over- invest in CSR when they don't bear much of the cost associated withit.

Leonardo et al. (2007) found CSR is increasingly a core component of corporate strategy in the global economy. In recent years its importance has become even greater, primarily because of the financial scandals, investors,, losses, and reputational damage to listed companies. The paper highlights two main findings: a significant upward trend in absolute value abnormal returns, irrespective of the type of event (for example, addition or deletion from the index), and a significant negative effect on abnormal returns after exit announcements from the Domini index. The latter effect persists even after controlling for concurring financial distress shocks and stock market seasonality.

Mackey et al. (2007) addressed the debate about whether firms should engage in socially responsible behavior by proposing a theoretical model in which the supply of and demand for socially responsible investment opportunities determine whether these activities will improve, reduce, or have no impact on a firm's market value. The theory shows that managers in publicly traded firms might fund socially responsible activities that do not maximize the present value of their firm's future cash flows yet still maximize the market value of the firm. Using a sample of non-financial Brazilian companies from 2005 to 2007, they analyze whether Corporate Social Responsibility (CSR) has an impact on firm value. Using company's Tobin's Q as a proxy for their market value, the paper finds that firms that compose the Bovespa Corporate Sustainability Index (ISE) are traded at a premium compared to the other publicly traded firms. They also indicate that the positive impact of these policies is independent of the econometric method and period analyzed. The results confirm that the benefits of corporate social responsibility policies surpass the possible costs implied by the adoption of such policies, leading corporate social responsibility to exert a positive impact on firm value. Prior empirical research has reported mixed results. McWilliams et al. (2000) provide an excellent review and we report their main observation. One stream has used event-study methods to assess the short-run impact of CSR (Clinebell et al., 1994; John et al.,1996; Posnikoff, 1997; Teoh et al., 1999; Worrell et al., 1991; Wright et al., 1997). Another stream highlighted the long-term effects of CSR (Aupperle et al., 1985; McGuire et al., 1988). McWilliams et al. (1997, 2000) have indicated how methodological issues can affect the findings and may be used to resolve some of the differences. The research studies reviewed so far have mostly highlighted on linkage of CSR with profit maximization, establishing brand loyalty to the organization, benefits of CSR, short term and long term impact of CSR. Therefore, it is clear that no in-depth study was conducted specially on the relationship between CSR investment and value of the firm as well as impact of CSR investment on value of the firm. Here, we find the gap on CSR, the most vital issue for the enterprises. Especially the service industries like banking. The present study is an attempt to mitigate such gaps on the literature of CSR, as far as possible.

1.6. Major areas of CSR Performed by the Commercial Banks in Bangladesh

- Engaged in clean water management.
- Engaged in afforestation.
- Beautifications of cities.
- Waste management.
- Natural calamities management.
- Facilitator in stab.
- Assistances for mentally or physically handicapped.
- Education of rootless children.
- Accommodation for the slum dwellers.
- Women's rights and anti-dowry practices.
- Rehabilitation of orphan/rootless children.
- Engaged in treating acid victims.
- Engaged in treating fatal diseases like cancer, cataract and leprosy.
- Providing free medical treatment to poor patients.
- Birth control products with a view to solving the population problem and to conduct camps for voluntary sterilization.
- Grants to Public Universities.
- Technical and vocational education for meritorious poor.
- Training on computer or information technology and in establishing infrastructure.
- Technical and vocational training to unskilled or semiskilled labor for export of human resources.
- Sports and provision of training at national level.
- Sanitation programs.

1.7. Analysis and Findings

Table 1. Descriptive Statistics.

Variables	Minimum	Maximum	Mean	Std. Deviation
ROA	.79	3.01	1.8672	.52285
ROE	12.06	32.25	24.2231	5.61081
EPS	4.33	237.37	45.1008	41.08387
CSR	0.140	0.86	0.4571	0.17883

From the above table, it was found that minimum ROA is 0.79 and maximum is 3.01 whereas mean is 1.8672. The average ROA is very poor for the selected banks. The minimum ROE is 12.06 and maximum is 32.25, but average is 24.2231 that indicate average ROE is high. The maximum CSR score is 0.86 and minimum is 0.14 that indicates every company discloses at least one area of CSR activities. The average CSR is 0.4571 that articulate CSR activities of selected banks are below the average.

Table 2. Correlation Matrices.

Particulars	ROA	ROE	EPS	CSR
ROA Pearson Correlation	1	0.569**	-0.316	-0.342*
Sig. (2-tailed)		0.000	0.061	0.041
ROE Pearson Correlation	0.569**	1	0.168	-0.038
Sig. (2-tailed)	0.000		0.328	0.824
EPS Pearson Correlation	-0.316	0.168	1	0.328
Sig. (2-tailed)	0.061	0.328		0.05
CSR Pearson Correlation	-.342*	-0.038	0.328	1
Sig. (2-tailed)	.041	0.824	0.051	

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

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

The summary of correlation between independent and dependent variables are reported in Table 2. Table 2 presents the correlation of CSR score and independent variables that have been denoted by ROA, ROE, and EPS. Referring to the table, it was found that the correlation between CSR score and ROA is -0.342 that means there is a 34.20% negative relationship between these two variables. Looking at the companies ROE and its correlation with CSR score is -0.038 which means actually there is 3.80% negative relationship between ROE and CSR score. The correlation between CSR score and EPS is 0.328 that means there is a 32.80% positive relationship between these two variables.

1.8. Inferences from the Hypotheses

1.8.1. The Relationship Between CSR and Return on Asset.

Model Summary

Model	R	R^2	Adjusted R^2	Std. Error of the Estimate
1	0.342	0.117	.091	0.49850

Model summary shows how well the model is fitted with the variables. In the above table, R is 0.342 and R^2 is 0.117 that means only 11.70% dependent variable is explained by the independent variable. The adjusted R^2 is 0.091.

Coefficients

Variable	Unstandardized Coefficients		Standardized Coefficients	*t*-value	Sig.
	B	Std. Error	Beta		
CSR	-0.142	.067		-2.122	.041

From the above table, it is found that the standardized coefficient is. -0.342 that means there is a 34.20 % negative relationship between CSR and Return on Asset. The *t*-value is -2.122 and p-value is 0.041 which is lower than α=0.05. So, null hypothesis is rejected. It means there is significant negative relationship between ROA and CSR but the relation is weak because some other factors may affect the CSR activities.

1.8.2. The relationship between CSR and Return on Equity.

Model Summary

Model	R	R^2	Adjusted R^2	Std. Error of the Estimate
1	0.038	0.001	-0.28	5.68854

In the above table, R is 0.038 and R^2 is 0.001 that means only 0.01% dependent variable is explained by the independent variable. The adjusted R^2 is -.028. The adjusted R^2 negative means dependent variable is not explained by independent variable.

Coefficients

Variable	Unstandardized Coefficients		Standardized Coefficients	t-value	Sig.
	B	Std. Error	Beta		
CSR	-0.171	0.763	-0.038	-0.224	0.824

From the above table, it is found that the standardized coefficient is. -0.038 that means there is a 3.80 % negative relationship between CSR and Return on Equity. The t-value is -0.224 and p-value is 0.824 which is higher than $\alpha=0.05$. So, null hypothesis is accepted. It means there is no significant relationship between ROE and CSR.

1.8.3. The relationship between CSR and Earning Per Share (EPS)

Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	0.328	0.108	0.081	39.37895

From the model summary report, it is found that value of R is 0.328 and R^2 is 0.108 that means only 10.80% dependent variable is explained by the independent variable. The adjusted R^2 is 0.081.

Coefficients

Variable	Unstandardized Coefficients		Standardized Coefficients	t-value	Sig.
	B	Std. Error	Beta		
CSR	10.685	5.279	0.328	2.024	.051

From the above table, it is found that the standardized coefficient is 0.328 that means there is a 32.80 % positive relationship between CSR and EPS. The t-value is 2.024 and p-value is 0.051 which is higher than $\alpha=0.05$. So, null hypothesis is accepted. It means there is no relationship between EPS and CSR.

1.9. Concluding Remarks

Since the business institutions are the member of the society and they are making profit from the society by giving products and rendering services. So, they have to perform some social activities. This paper explores to investigate the relationship between CSR activities and profitability. The researcher conducted the research considering CSR as a qualitative factor. If the company disclose any sector of CSR activities has been scored them 1 if not 0. The researcher has considered CSR as an independent variable and ROA, ROE and EPS as dependent variables. Firstly, the researcher has presented the CSR activities of different selected banks from year 2007 to 2010. Secondly, a simple regression analysis is performed to investigate the relationship between dependent and independent variables. The result of regression analysis shows that there is a significant negative relationship between CSR and ROA. And there is no relationship among EPS, ROE and CSR.

Further research can be done by considering the CSR investment as a quantitative factor. Percentage of CSR investment as an independent variable and ROA, ROE, Sales, and company size as dependent variables.

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