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Corporate Social Responsibility and Financial Performance: Does size Matter? Evidence from Kenyan Listed Firms

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Abstract

The principal objective of this empirical investigation was to probe whether size matters in moderating the relationship between corporate social responsibility and financial performance using cross-sectional dataset drawn from 61 firms listed at the Nairobi Securities Exchange for the period 2016 to 2020. Corporate social responsibility composite score was generated by aggregating the five indicators, namely: community, environmental customer, employee, investor and supplier dimensions. The size of the firm was operationalized using sales turnover while financial performance was measured by price to book value ratio. The estimation technique employed to tests the research hypothesis was regression analysis and the findings were presented in form of tables and figures. The estimation results revealed that the relationship between corporate social responsibility and financial performance varied with the size of the firm as the hypothesized linkage strengthened as firms became larger. From the findings, synergistic moderation was confirmed. The findings also validate the tenets of legitimacy theory.

Keywords: corporate social responsibility, firm size, financial performance, legitimacy theory

Introduction

The influence of corporate social responsibility (CSR) on financial performance (FP) has gained noteworthy traction in the corporate world recently. Owing to diverse and growing stakeholder demands; many firms have integrated corporate social responsibility (CSR) as one of their core corporate strategies in a quest to not only differentiate themselves from the rest, but to also ameliorate their overall FP in a competitive business environment. To date, there is no consensus, both theoretically and empirically as to whether CSR has significant influence on firm performance due to divergence in findings (Maqbool & Zameer, 2018). Whereas a plethora of theoretical literature predicts a positive association between CSR and firm performance, the skeptics of CSR practices nonetheless suggest that it is a costly undertaking with adverse implications on FP (Bhuyan, Lodh & Pereira, 2017). Despite these overriding standpoints, the relationship between CSR and FP remains unclear and unsolved.

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Owing to multidimensionality of CSR as a concept, there is no unanimity on the standard definition of the variable thus making it difficult to measure. However, CSR is delineated as obligations, schemes, programs and policies that have been extensively employed in a multiplicity of corporate contexts, and the cultural, political, economic and social associations they encompass to the larger society(s) in which their business operations are grounded (Deng & Long, 2019). Arguments in favour of CSR schemes is pegged on its key benefits such as greater revenues and market share; reinforcing the capacity to attract and retain talented workforce; strengthening firm's image, reputation and brand enhancement; attracting valuable investors, reducing costs and finally augmenting the FP (Chakroun, Salhi & Jarbaui, 2019).

As a moderator, firm size is an assortment or capacity of probable production ability an organization enjoys and the organization's service plurality that can concomitantly be provided to several customers (Mansaray & Brima). Generally, large firms tend to outperform small firms since they enjoy greater production capacity, easier access to credit facilities, broader pools of talented and qualified workforce, unmatched economies of scale, complex internal systems to deal with corporate issues and higher bargaining power over suppliers (Hou, 2018). Firm size is usually measured using a set of indicators such as asset base, number of employees, sales turnover and market capitalization. However, empirical literature suggest that vast of the metrics used to proxy size are highly correlated and there is no theoretical and empirical consensus on the most ideal metric of these variable (Yang, Bento & Akber, 2019; Oh & Park, 2015).

Financial performance is an objective measurement of outcomes of company's strategies, operations and policies in monetary terms (Choi, Kwak & Choe, 2017). Particularly, FP is important since it points out the organization's aggregate financial safety over a precise period of time and offers an essential yardstick for evaluating industry and sectorial success outlook via benchmarking (Hou, 2018). Outstanding FP attracts new investors and also inspires the current stockholders to acquire extra investments provided they are profitable (Bhuyan, *et al.*, 2017). Moreover, FP offers guidance on future investment decisions with respect to matters relating to managerial control, assets acquisitions and business development (D'Amato & Falivena, 2019).The FP indicators can be decomposed into two: accounting based metrics (return on assets/equity, net profit margin etc) as well as market based measures such as Tobin Q, market to book ratio, price earnings ratio among others.

Empirical literature suggests that the effect of CSR and performance vary with the size of the firm. As suggested by Chakroun *et al.* (2019), bigger companies can effortlessly sustain amplified CSR expenditures due to superior levels of resources (slack resources) at their disposal and this has higher influence on FP. On the contrary, CSR has marginal influence on FP for smaller companies owing to resource constrains since they dedicate vast of their corporate resources to improving performance in their business operations via auxiliary customary activities (Deng & Long, 2019). Moreover, Yang *et al.* (2019) suggest that for bigger companies, CSR activities have greater positive influence on FP on the basis of the efficiency argument of firm size stemming from benefits resulting from the economies of scale. Conversely, smaller companies rarely enjoy the benefits of economies of scale and thus CSR schemes have minimal effect on FP (Mansaray & Brima).

Research Problem

Based on the existing empirical investigations, it is evident that the linkage between CSR obligations and firm performance is ambiguous and inconclusive. This is largely attributed to divergence in the reported empirical findings ranging from positive, neutral and negative association between CSR and FP. Nag and Bhattacharyya (2016) reckon that this incongruence is a as a result of choice of variables, sampling variations, disparity is the study timeframe, type of metrics used to operationalize the study variables, misspecification of estimation models and selection of control variables. Efforts to reconcile these mixed findings have note borne any fruits and this has led to proliferation of a plethora empirical investigations across many disciplines.

There is notable disparity in FP among the firms listed at the NSE. Some firms are reporting better FP compared to their counterparts and it is therefore essential to probe whether these variations are linked to CSR and also whether the strength and direction of CSR-FP relationship vary with firm size. With the intention of disentangling the nexus between CSR and financial performance, instead of widely cited direct linkage between CSR and financial performance, this empirical investigation explores the potential influence of the as a moderator which aids in understanding better the reasons behind this linkage and to clarify the current divergent findings that have emerged in the empirical literature.

Furthermore, there are notable differences with respect to CSR-FP relationship outcomes between developed and developing markets (Maqbool & Zameer, 2018). Specifically, the regulatory, political,

economic and cultural environments are critical contextual factors that shape the CSR–FP relationship. Unlike developed markets, many developing markets have weak institutions, economic and political environments and this is one of the key sources of mixed findings in the vast of prior empirical studies. Likewise, the absence of universally accepted delineation of CSR, size and FP has made it impossible to effectively measure these variables thus contributing to inconclusive and divergent empirical outcomes (Yang *et al.*, 2019). Finally, the bidirectional relationship between CSR and FP is another area of concern since there is no empirical clarity whether CSR leads to better FP or it is FP that leads to better CSR endeavors. This study therefore seeks to address these gaps by investigating the relationship between CSR, size and FP within the context of the listed firms at the Nairobi Securities Exchange.

Research Objective

The objective of this study is to examine the moderating role of firm size on the relationship between corporate social responsibility and financial performance of the firms listed at the Nairobi Securities Exchange.

Theoretical Literature

Ostensibly, there are several frameworks and theoretical perspectives that have been widely employed in justifying and linking CSR, size and FP. These theories include: legitimacy, resource based view and stakeholder theories. However, a compelling argument as to whether size matters in CSR-FP relationship is largely anchored by legitimacy theory which was propagated by Davis (1973). Legitimacy is a widespread acuity that firms' actions are appropriate within socially constructed system of norms, beliefs and values. Specifically, legitimacy theory envisages existence of an implied social contract between the society and organization, and the support from the society is vital for growth and survival organization. To gain social validation, corporate actions must be construed to be within the desired societal limits and norms since it bestows legitimacy to businesses operations (Hou, 2018).

There are three essential dimensions of legitimacy: moral and pragmatic facets. Firms consistently legitimize their business activities by embracing CSR in order to solicit support from the society and organizations may benefit via improved FP. Moreover, Maqbool and Zameer (2018) argue that firm size is a precursor of corporate legitimacy. Essentially, big companies especially the publicly owned are prone to increased public scrutiny by numerous stakeholders as they are highly visible socially and similarly more

susceptible to unpleasant reactions from diverse stakeholder groups (Masaray & Brima, 2017). As a result of increased legitimacy requirements, large organizations aggressively participate in CSR schemes unlike small organizations so as to enhance their corporate image hence consequently improving their FP (Choi *et al.*, 2018).

Empirical Literature

There is lack of convergence in empirical literature with respect to the linkage between CSR and financial performance. Mixed findings have been reported in the prior empirical investigations ranging from positive, neutral as well as negative relationship. An empirical study undertaken by Cui, Liang and Lu (2013) probed the linkage between CSR obligation and sales performance while employing firm size as the moderator. The study made use of cross-sectional dataset obtained from a sample of 630 CEOs' of Chine private firms. To measure the variables, CSR obligations index was constructed using diverse environmental, social, product, employee, supplier and investor dimensions. Firm size was represented by number of staff while the sales growth was employed to proxy sales performance. Using ordinary least square (OLS) estimation method, the findings established that size moderated CSR-FP linkage since the previous negative association became increasingly positive for bigger companies thus confirming the moderating effects. Consistent findings are reported by Pablo, Benito and Juan (2019) who investigated the moderating effect of firm size on the association between CSR schemes and economic performance with the aid of a dataset drawn from a sample of 279 Spanish firms while applying the partial least square (PLS)-structural equation model (SEM) as the key estimation technique.

In contrast, divergent findings are reported by Devie, Liman, Tarigan and Jie (2018) who while using PLS estimation technique examined the probable influence of CSR and FP in Indonesian using age, leverage and size as moderators. The cross-sectional dataset was gathered from a sample of 40 quoted companies with years of observation ranging from 2008-2016. To operational the study variables, Tobin Q, EPS, NPM and ROE were employed as the proxies of FP whereas CSR was represented by KLD index. Moreover, ratio of the net value of fixed assets to gross value of fixed assets, liabilities divided by assets, asset base were utilized to measure age, leverage and size respectively. The findings established that varying the levels of age, leverage and size had insignificant effect on the strength of CSR-FP linkage. Similar findings are confirmed by Isa and Jamilumadaki (2017) who applied cross-sectional data drawn from 15 firms for the

period 2005-2014. The study assessed the nexus between CSR disclosure and FP of listed consumer goods firms in Nigeria while using size and leverage as the moderators.

To investigate whether CSR-FP linkage differ with size, Youn, Hua and Lee (2015) using a two-way fixed effect estimator carried out an empirical study while employing unbalanced panel data comprising of a sample of 262 companies for the fiscal period 1992 to 2011. Tobin Q, aggregate revenue and KLD index were utilized as the metrics for measuring FP, size and CSR respectively. The outcome suggested that CSR-FP linkage become stronger due to increase in firm size hence validating synergistic moderation influence. The findings of this study mirror those of Nag and Bhattacharyya (2016) who probed CSR based on social, customers, employee and environmental dimensions its relation to FP using both market (PER) and accounting (ROA) indicators of FP among 30 listed Indian firms.

Conceptual Framework

The empirical investigation examined the moderating effect of firm size on the relationship between CSR and FP. Theoretically, CSR-FP relationship usually vary with the size of the firm. The conceptual model is presented in Figure 2.1.

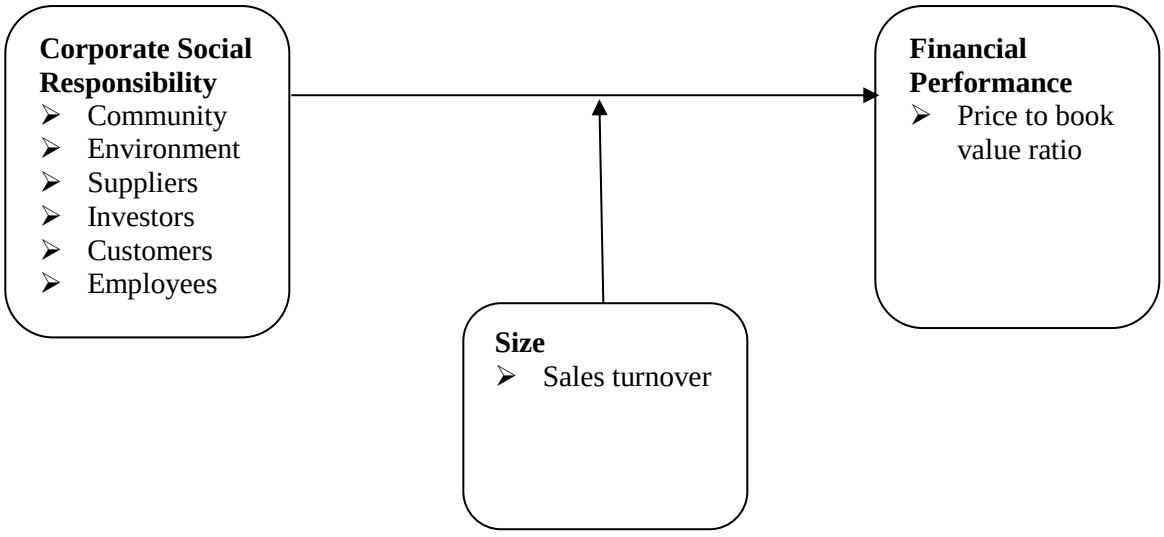

Figure 2.1: Conceptual Model

Research Hypothesis

H_{01}: There is no significant moderating effect of firm size on the relationship between corporate social responsibility and financial performance of firms listed at the Nairobi Securities Exchange.

Methodology

The empirical analysis is based on a set of three variables, namely: CSR, size and FP. Empirical data on CSR was gathered using primary sources while data on size and FP was obtained from secondary sources. The study adopted descriptive cross-sectional census survey of 61 firms listed at the NSE. Theoretically, there are several coinciding reasons for employing moderators (interactions) in empirical studies (Andersson, Cuervo-Cazurra & Nielsen, 2014). Stipulating moderation improves understandings of economic/social associations by giving circumstances under which such associations applies, are stronger or weaker. Therefore, moderation prolongs well-known associations to settings that the previous empirical studies overlooked. More importantly, inclusion of interactions must be theoretically be justified. The moderator (size) is grounded on legitimacy theory. To test the moderation effects; the study used process macro (model 1) which gives simultaneously comprehensive output hierarchical regression analysis, simple slope analysis as well as Johnson-Neyman procedure. These methods are vital in validating interaction effects.

The analysis of the empirical data was executed using descriptive (mean, standard deviation, minimum and maximum values) and inferential statistics. Before carrying out inferential statistics, only multicollinearity test was performed to evaluate whether the explanatory variables were highly correlated since the study utilized cross-sectional data. Pooled ordinary least squares method (OLS) was applied to test the relationship among the study variables owing to its statistical and computation proficiency. For estimation purposes, a general linear model employed is as indicated below:

$$FP = \beta_0 + \beta_1 CSR + \beta_2 FS + \beta_3 CSR*FS + \zeta$$

*Where: **FP** = financial performance; $\boldsymbol{\beta_0}$ = Constant; $\boldsymbol{\beta_1}, \boldsymbol{\beta_2}, \boldsymbol{\beta_3}$ = coefficients; CSR = corporate social responsibility; FS = firm size; **CSR*FS** = interaction term given by the product of CSR and size; $\boldsymbol{\zeta}$= error term.*

Descriptive Statistics, Diagnostic Test and Correlation Analysis

Table 1: Descriptive Statistics

Variable	N	Mean	SD	Min	Max
CSR	50	4.21	0.60	2	5
FS	50	22.44	1.85	18	26.76
FP	50	0.97	0.99	-3.63	3.07

The composite score for CSR (M = 4.21, SD = 0.60) was reasonably high implying that the participants agreed that their organizations had adopted CSR obligations in their corporate activities. The mean score for firm size was 22.44 with standard deviation of 1.85 suggesting negligible disparities in the revenues generated by firms. The average score for FP was 0.97 with a standard deviation of 0.99 indicating high disparity in terms of price to book value ratio among the listed firms.

Diagnostic Tests

The most common problem that generally affects cross-sectional datasets is multicollinearity. Multicollinearity occurs when regressors are highly correlated. This often leads to spurious estimation results such as regression weights with implausible magnitudes and wrong signs as well as inflated standard errors. Variance Inflation Factor (VIF) was used to test multicollinearity and the results are presented in Table 2 below.

Table 2: Multicollinearity Test Results

Variable	VIF	Tolerance (1/VIF)
CSR	1.00	1.00
FS	1.00	1.00
Mean VIF	**1.00**	

The findings indicate that CSR and sales turnover had both VIF/tolerance values of 1.00. This confirms absence of multicollinearity since Variance Inflation Factor (VIF) is less than 10 and the tolerance value is greater than one.

Correlation Analysis

Correlation analysis measures the strength and direction of association between the variables. As indicated in Table 3, CSR was weakly and insignificantly positively correlated with firm size (r = 0.004, p < 0.05) but in contrast moderately and significantly correlated with FP (r = 0.474, p = < 0.05). Moroever, sales turnover was weakly and insignificantly correlated with FP.

Table 3: Correlation Analysis Results

Variable	CSR	FS	FP
CSR	1		
FS	0.004	1	
FP	0.474*	-0.076	1

** Implies significance of correlation at 0.05 level in a two tailed test*

Estimation Results and Discussion

To test the moderating influence of firm size on CSR-FP relationship, the null hypothesis specified below was tested.

H_{01}: The moderating influence of firm size on the linkage between corporate social responsibility and financial performance of firms listed at NSE is insignificant.

Table 4: Estimation Results (Dependent Variable: Financial Performance)

R^2	0.374				
MSE	0.648				
F(3, 46)	9.150				
Prob > F	0.000				
N	50				
Test of Highest Order Unconditional Interaction					
	ΔR^2	**F**	**df_1**	**df_2**	**p**
CSR*FS	0.144	10.551	1	46	0.002
	β	**SE**	**t**	**p**	
Constant	0.970	0.110	8.799	0.000	
CSR	0.965	0.114	8.482	0.000	
FS	-0.035	0.062	-0.561	0.578	
CSR*FS	0.262	0.081	3.248	0.002	

From Table 4, the overall interaction model was statistically significant and described sizable quantity of variance in FP {R^2 = 0.374, F (3, 46) = 9.150, p < 0.05}. This demonstrates that CSR, firm size and interaction term jointly explicated 37.4% of variance in FP. The change statistics (the test of highest order

unconditional interaction) displays variance in explanatory power by basic and the moderation/interaction model which yielded $\Delta R^2 = 0.144$, $F(1, 46) = 10.551$, $p < 0.05$. This shows that FP significantly improved by 14.4% after incorporation of the interaction term in the estimation model thus confirming the moderation effect of firm size on CSR-FP relationship.

Likewise, inspection of the individual explanatory variables indicated that CSR ($\beta = 0.965$, $t = 8.482$, $p < 0.05$) was a positive significant predictor of FP. Conversely, size insignificantly predicted FP ($\beta = -0.035$, $t = -0.561$, $p > 0.05$). However, the coefficient of the interaction between CSR and size ($\beta = 0.262$, $t = 3.248$, $p < 0.05$) was significant and positive. This validates synergistic moderation as the effect of firm size on CSR-FP relationship since the linkage became increasingly positive as size increases. As a result, this led into rejection of null hypothesis that there is no moderating influence of size on the relationship between CSR and FP.

To further corroborate the moderation effects, simple slope analysis was applied to evaluate the conditional effects of CSR on FP at three levels of firm size; that is, when the size is small (-1.849, i.e. 1SD below the mean), average (0.000, i.e., mean) and big (1.849, i.e. 1SD above the mean). Table 5 displays the outcome of simple slope analysis.

Table 5: Empirical Results displaying conditional Effects of CSR at values of the size

FS	Effect	SE	t	p
-1.89	0.159	0.272	0.583	0.562
0.000	0.644	0.197	3.262	0.002
1.849	1.129	0.220	5.123	0.000

The estimation results presented in Table 5 confirms that when the size of the firm is small, there is insignificant association between CSR and FP ($\beta = 0.159$, $t = 0.583$, $p > 0.05$). In contrast, for medium sized firms, there is positive significant CSR-FP association ($\beta = 0.644$, $t = 3.262$, $p < 0.05$). Correspondingly, for larger firms, there is positive significant influence of CSR on FP ($\beta = 1.129$, $t = 5.123$, $p < 0.05$).

Due to challenges associated with interpretation of interaction term coefficient(s), it is imperative to assess and confirm moderation effects using interaction plots as shown in Figure 5.1. From the interaction plot, as firms grow bigger, the conditional effect of CSR on FP becomes stronger consequently showing the

synergistic interaction. This is validated by non-parallel slope adjustments.

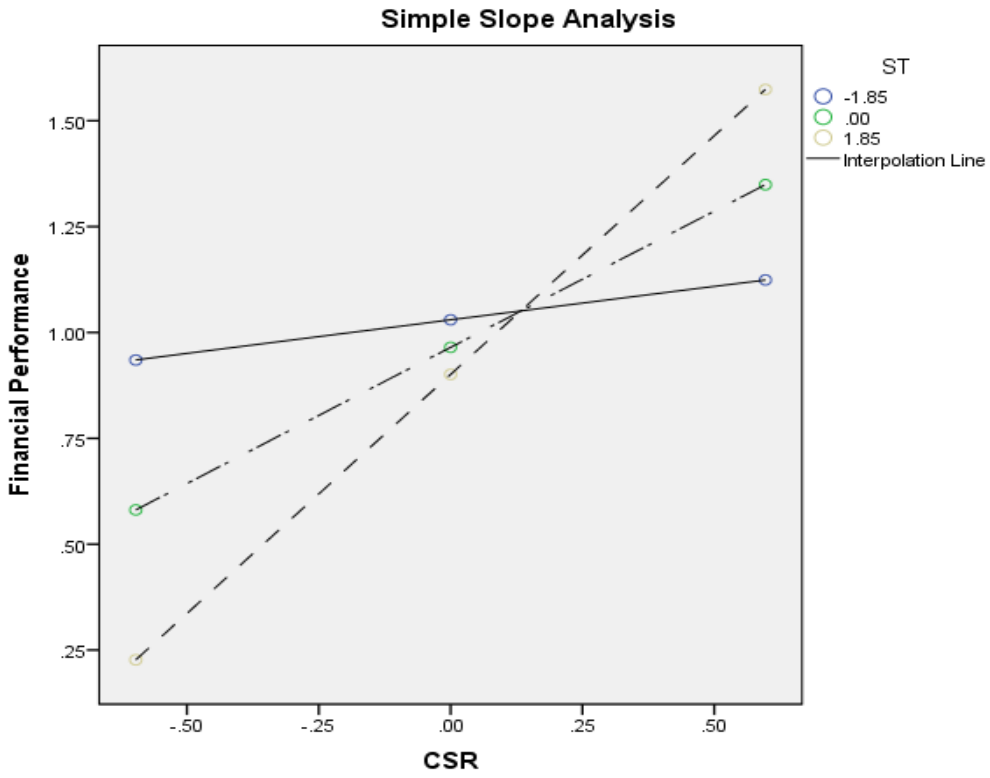

Figure 2: Interaction Plot

The final approach of verifying the moderation effect is by employing Johnson-Neyman procedure. Table 6 displays the moderator values (firm size) delineating Johnson-Neyman regions of significance. The estimation results based on this method showed that CSR-FP linkage was significant when the values of size fluctuated from -4.444 to 4.316.

The findings of this study reflect those of Nag and Bhattacharyya (2016) who evaluated the effect CSR obligations on FP while provisioning for corporate size as a moderator using longitudinal dataset drawn from a sample of 30 firms belonging to national securities exchange (NSE) firms in India. In contrast, the findings of this study significantly contradict those of Isa and Jamilumadaki (2017) who while usining panel data from yearly reports drawn from 15 firms for the period 2006-2014 investigated the moderating role of leverage and size on the nexus between CSR and FP of quoted consumer goods companies in Nigeria.

Table 6: Conditional Effect of CSR at values of the Firm Size

FS	Effect	SE	t	p
-4.444	-0.522	0.445	-1.173	0.247
-4.006	-0.407	0.414	-0.985	0.330
-3.568	-0.292	0.383	-0.764	0.449
-3.130	-0.178	0.353	-0.504	0.617
-2.692	-0.063	0.324	-0.194	0.847
-2.254	0.052	0.296	0.177	0.861
-1.816	0.167	0.270	0.619	0.539
-1.378	0.282	0.247	1.144	0.259
-0.940	0.397	0.226	1.755	0.086
-0.771	0.441	0.219	2.013	0.050
-0.502	0.512	0.210	2.440	0.019
-0.064	0.627	0.198	3.158	0.003
0.374	0.742	0.193	3.842	0.000
0.812	0.857	0.194	4.414	0.000
1.250	0.971	0.201	4.825	0.000
1.688	1.086	0.214	5.070	0.000
2.126	1.201	0.232	5.179	0.000
2.564	1.316	0.253	5.194	0.000
3.002	1.431	0.278	5.154	0.000
3.440	1.546	0.304	5.083	0.000
3.878	1.661	0.332	4.999	0.000
4.316	1.776	0.362	4.910	0.000

Furthermore, the estimation results of this study similarly converge with those Davie *et al.* (2018) of who reported that CSR-FP linkage became stronger as companies became bigger. The results of this study also mirrors the findings reported by Cui, Liang and Lu (2013) who argued that corporate size moderated the association between CSR and FP since the previous negative association became positive as firms became bigger thus confirming moderating effects of the firm size. Finally, the upshots of the current study validate those of Pablo, Benito and Juan (2019) who while probing the moderating effect of size on the relationship between CSR and FP suggested that the bigger the company, the stronger the relationship between CSR and FP.

Conclusions and Limitations

Based on the empirical findings, it is evident that size matters in strengthening the relationship between CSR and FP. It can therefore be concluded that CSR-FP relationship vary with the size of the firm. This is

attributed to the fact that large companies posses' substantial resources compared to smaller companies and therefore being in a better position to greatly invest in CSR activities. Large companies are capable of responding better to diverse stakeholder pressures via discretionary practices such as social responsibility activities whereas small companies are often inhibited by scarce resources and therefore incapable of affording such voluntary practices since they tend to utilize resources at their disposal to ameliorate FP via more traditional avenues of competition. In addition, large firms take advantage of their core proficiencies to frame their CSR obligations which has positive implication on their FP. Similarly, large companies have better opportunity to succeed in executing notable CSR activities, since they enjoy economies of scale and therefore being in a good position to reallocate resources.

Despite of these findings, this study however has some limitations. First, this study was carried out in the context of large listed firms and the empirical findings cannot be authoritatively extrapolated to small private firms which are characterized by a unique regulatory environment. Secondly, this study largely employed cross-sectional dataset hence making it impossible to probe the temporal effects which is only possible with the longitudinal dataset. Third, the study ignored the potential influence of the mediating variables which actually explains the indirect link between CSR and FP.

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