The impact of corporate social responsibility on organizational performance

[1]Javad Mehrabi, [2*]Davood Gharakhani, [3]Arshad Farahmandian

[1]Assistant Professor, Department of Public Management, Qazvin branch, Islamic Azad University, Qazvin, Iran
[2*]Department of Industrial Management, Qazvin branch, Islamic Azad University (IAU), Qazvin, Iran
E-mail: Davoodgharakhany@yahoo.com Davood Gharakhani (Corresponding author)
[3]Department of management, Zanjan Branch, Islamic Azad University, Zanjan, Iran

Abstract: The purpose of this paper is to investigate the effects of corporate social responsibility (CSR) on firm performance. Data were collected via a questionnaire survey of star-rated hotels in Iran and a total of 100 valid responses were received. The hypothesis was tested by employing structural equation modelling with a maximum likelihood estimation option. It was found that CSR could enhance performance. This paper is one of the first to examine the effects of CSR on business performance. The empirical evidence from Iran adds to the existing literature on the respective importance of CSR. The main limitations include the use of cross-sectional data, the subjective measurement of performance and the uniqueness of the research setting (Iran).

[Javad Mehrabi, Davood Gharakhani, Arshad Farahmandian.**he impact of corporate social responsibility on organizational performance.***Life Sci J* 2012;9(4):2313-2318] (ISSN:1097-8135). http://www.lifesciencesite.com. 341

Keywords: Corporate social responsibility, organizational performance, Iran

1. Introduction

In today's changing business world, companies cannot be measured on profits alone. The external environment can play a major role in the perceived value and success of an organization. Managers should be concerned about social responsibilities, since it gives the company a right to exist based on their responsiveness to the external environment. Several outside stakeholders may influence the development of an organization's mission and goals. The modern era of corporate social responsibility (CSR) started from 1953 with Bowen's publication (Bowen, 2003), "Social Responsibilities of Businessman," according to Carroll (1979). Such CSR issues carried to tourism as a form of sustainability and have been investigated in the literature for the past several decades (Holden, 2000). In recent years, the significance of CSR for tourismrelated industries has further increased (Kang, Lee, & Huh, 2010).

Corporate social responsibility is an important issue in contemporary international debates. In the past two decades, CSR appears to have become more ubiquitous and perceived as being relevant to corporations all over the world (Aras and Crowther, 2008). Moreover the link between CSR and business performance has become largely unquestioned. There have been various studies undertaken to investigate this important issue. Consequently much of the previous research regarding CSR deals with this issue and with the problems in the development of standards for managing and reporting such indeterminate activity. CSR is problematic as it is often perceived that there is a dichotomy between CSR activity and financial performance with one being deleterious to the other and corporations having an imperative to pursue shareholder value. According to Morrisons (2005), a leading British supermarket chain, CSR is "about understanding and managing the relationship between our trading operations and the economy, environment and communities within which we operate". Morrisons claim that its CSR focus is on "managing the social, ethical and environmental issues that are material to our commercial performance, through a programme of continuous improvement". Corporate social responsibility (CSR) is one of the roles performed by the business world. This program is also aimed at encouraging business entities to run their activities ethically, minimizing bad effects on communities and the environment so that, ultimately, they can continue to carry on gaining economic benefit as their objective (Lesmana, 2007).

Corporate social responsibility has witnessed an ongoing debate not only among management theorists but also among industry practitioners. Sloan (1964) argues that "the strategic aim of a business is to earn a return on capital, and if in any particular case the return in the long run is not satisfactory, then the deficiency should be corrected or the activity abandoned for a more favourable one". Friedman (1962) also asserted that "the business of business is business and the only social responsibility is to increase profit". CSR can also be interpreted from the legitimacy perspective as firms' engage in socially responsible activities in an attempt to gain, improve or maintain legitimacy (Moir, 2001). Many studies have described the performance of socially responsible investments, with somewhat different results. Orlitzky et al. (2003) performed a meta-analysis of 52 studies in search for the relationship between corporate social performance and corporate financial performance. The results confirm that socially responsible investing pays off. The relationship is strongest for the social dimension within corporate social performance. When isolating the environmental responsibility we come to the same conclusion but to a lesser extent. The key factor that initiates CSR is stakeholders' expectations that an investment decision should generate not only financial profit, but should also take into account the social and environmental aspect so that community welfare can be improved (Commission of the European Communities, 2001; both cited in Malovics et al., 2007). Some definitions state that CSR is the ethical, responsible and integrated business implementation applied to all operations (McWilliams and Siegel, 2001, cited in Wan-Jan, 2006; Business for Social Responsibility, 2003; cited in Jamali, 2006). Presently, however, the ideal definition if CSR is given by The World Business Council for Sustainable Development (2001): a business commitment that contributes to sustainable economic development through team work with employees and their representatives, their families, and local and public communities, to improve the quality of life by means of beneficial ways both for the business itself and for development (Jamali, 2006). Senior management faces a wide range of demands for Corporate Social Responsibility actions from different segments of society. Issues surrounding environmental quality, employee rights, community development, and diversity management all make claims on the attention of the contemporary business manager. In its broadest sense, CSR refers to "the firm's consideration of, and response to, issues beyond the narrow economic, technical, and legal requirements of the firm… (to) accomplish social benefits along with the traditional economic gains which the firms seeks.

2. Research background and hypothesis

2.1 Corporate social responsibility

CSR is defined as a "voluntary corporate commitment to exceed the explicit and implicit obligations imposed on acompany by society's expectations of conventional corporate behavior" (Falck & Heblich, 2007). For corporations, the adoption of CSR strategies can enhance their relationships with multiple stakeholders. Therefore, it is necessary to communicate CSR activities and use effective relationship management to satisfy stakeholders' expectations and achieve the expected goals of CSR initiatives (Clarke, 2000; Podnar, 2008). CSR has been defined as the duty of the organisation to respect individuals' rights and promote human welfare in its operations (Manakkalathil and Rudolf, 1995; Oppewal et al., 2006). Carroll and Buchholz (2000) stated that CSR encompasses the economic, legal, ethical, and philanthropic expectations placed on organisations by society at a given point in time. CSR is a complex and diverse term representing business standards focusing on the long-term nature of business itself and increasing value for shareholders. Corporate social responsibility is not just an abstract concept but a business standard that we follow in our everyday activities. The observance of CSR principles is a prerogative for all company employees and not only for top management. This particular style of working gratifies and benefits all parties – the government, employees and their family members, consumers, local communities and shareholders. CSR refers to a company's voluntary activities "that appear to further some social good, beyond the interests of the firm and that which is required by law" (McWilliams & Siegel, 2001). Examples include the adoption of advanced human resource management programs, the reduction of environmentally hazardous substances, philanthropic activities, the production of products integrating social attributes, and support for local businesses (McWilliams & Siegel, 2001).

Corporate social responsibility means at a basic level – that ''corporate activity should be motivated in part by a concern for the welfare of some non-owners, and by an underlying commitment to basic principles such as integrity, fairness and respect for persons'' (Donaldson, 2005). In a general sense, social responsibility is management's acceptance of the obligation to consider profit, consumer satisfaction, and societal well-being of equal value in evaluating the firm's performance. It is the recognition that business must be concerned with the qualitative dimensions of consumer, employee, and societal benefits, as well as the quantitative measures of sales and profits, by which business performance is traditionally measured. Businesses may exercise social responsibility because such behavior is required by law, because it enhances the company's image, or because management believes it is the ethical course of action (Kurtz and Boone, 2008). CSR calls for corporations to take their social responsibilities as seriously as they pursue their economic objectives, and this applies to air transportation industries as to any other. There are four components in CSR; economic, legal, ethical and philanthropic responsibilities and these can be viewed as a process by which managers identify and accommodate the interests of those affected by their organization's actions. Isolating the appropriate CSR programs is difficult because there are multiple factors, such as program risk, corporate goals and limited CSR resources, at play. Corporate social responsibility is a form of management defined by the ethical and transparent relationship between a company and all the groups with which it relates, by the establishment of corporate goals compatible with the sustainable development of society, preserving its environmental and cultural resources for the future generations, respecting diversity, and promoting the reduction of social inequality.

2.2 organizational Performance

Performance can be viewed in many aspects and connotations depend on the application. Derek, Torrington and Laura (1995) attributed performance as bottom line profit, doing better than competitors, maximum organization effectiveness and achieving specific organization objectives. In fact, Laitinen (2002) defined performance as the ability of an object to produce results in a dimension determined a priori, in relations to a target. OP is an indicator which measures how well an enterprise achieves their objectives (Hamon, 2003). Ho (2008) defined OP in terms of how well an organization accomplishes its objectives. Schermerhorn et al. (2002) point out that performance refers to the quality and quantity of individual or group work achievement. Delaney and Huselid (1996) suggest two ways to assess OP and market performance.

2.3 Corporate social responsibility and organizational Performance

Corporate social responsibility looks at how firms treat their stakeholders. One key stakeholder group that is frequently overlooked is the firm's shareholders. All too often, the corporate social responsibility literature focuses on customers, employees, and the natural environment, but rarely on shareholders. Corporate Social Responsibility is a term describing a company's obligations to be accountable to all of its stakeholders in all its operations and activities. Socially responsible companies consider the full scope of their impact on communities and the environment when making decisions, balancing the needs of stakeholders with their need to make a profit.

Many firms started reporting about their ethical, social and environmental conduct. And in marketing, being green and social is positioned as a relevant product and firm characteristic. In academic research, CSR has become a topic of interest too. Many studies investigate the connection between financial and social performance (see Lockett, Moon, and Visser, 2006). Numerous theoretical views on the link between financial and social performance are put forward (for an overview see Allouche and Laroche, 2006). Furthermore, a large number of empirical studies investigate the relationship between social and financial performance (see Orlitzky, Schmidt and Rynes 2003). Freeman and Liedtka (1991) presented seven reasons why the concept of social responsibility is often abandoned. One of the reasons given was, ''Corporate social responsibility (CSR) promotes incompetence by leading managers to involve themselves in areas beyond their expertise that is, repairing society's ill'' (Freeman and Liedtka, 1991). Bauer et al. (2002) investigated the performance of international ethical mutual funds, corrected for investment style. The results show no significant difference in risk-adjusted returns between ethical and conventional funds for the period 1990-2001. Kneader et al. (2001) investigated the financial performance of 40 international ethical funds and 40 international non-ethical funds against their benchmark. The results show no statistical difference between their performances. They found that ethical funds have lower risk in comparison to their non-ethical counterparts. The cross-sectional analysis indicates that the risk-adjusted returns are not significantly related to the size, age or ethical status of the fund.

Hypothesis: CSR has a positive impact on organizational performance.

3. Research methodology

3.1 Data collection

To test our model, we collect data from hotel companies in Iran. The Iranian hotel industry provided a suitable context to test the hypotheses for the following reasons. To collect the data, a questionnaire together with a covering letter and a stamped return envelope was mailed to 200 hotels. With a cut-off date five weeks after the mailing, 100 completed questionnaires were received, resulting in a response rate of 50 per cen. The complete set of items for all the scales used in this study together with their sources is provided in the Appendix. All these scales (except for the performance scale which is measured by seven point scales) are measured using five point Likert type scales, ranging from ''not at all'' to ''very much''. The performance instrument is composed of three items asking the respondents to assess their companies' results against their major competitors in terms of sales growth, return on equity (ROE) and overall performance. Our operationalization of the CSR construct is based on the scale developed byMaignan et al. (1999). As the original scale is composed of 29 items, we used five dimensions for CSR. We obtained confirmatory factor analysis by SPSS software.

4. Analysis and results

In Table 1, we show the measurement properties of the variables and in Table 2 the correlations. All measures return a composite reliability in excess of the threshold value of 0.60 recommended by Bagozzi and Yi (1988). In sum, the results of the measurement analysis process indicate that the purified scales show adequate evidence of convergent validity. Construct reliability was evaluated using the procedure suggested by Fornell and Larker (1981), including examining the parameter estimates and their associated t values and assessing the average variance extracted for each construct (Anderson and Gerbing, 1988). Discriminant validity was assessed in a two-step process.

Table 1. Summary statistics of the measurement analysis					
Variable/item	Mean	Standard deviation	Factor loading	Variance extracted (%)	Composite reliability
CSR					0.794
Item 1	3.255	0.765	0.854	0.698	
Item 2	3.564	0.875	0.912	0.656	
Item 3	3.214	0.998	0.759	0.719	
Item 4	3.659	1.021	0.851	0.515	
Item 5	3.587	0.855	0.912	0.645	
Performance					0.816
Overall	3.278	1.025	0.752	0.583	
ROE	3.651	1.135	0.698	0.714	
Sales	3.264	1.125	0.843	0.641	
H (CSR performance)	**Loading (standardised)**	**Significant**	**Fit index**		
	0.64	P<0.001	X^2=34.2 df=37 RMSEA=0.000 CFI=1.000 NFI=0.84		
Notes: Item numbers refer to the item list in Appendix; all parameter estimates are significant at the p < 0.001 level; CSR = corporate social responsibility					

Table 2. Correlation matrix								
Variables	Grow	ROE	Overall	CSR5	CSR4	CSR3	CSR2	CSR1
Grow	1.00							
ROE	0.18	1.00						
Overall	0.42	0.31	1.00					
CSR5	0.21	0.37	0.29	1.00				
CSR4	0.52	0.28	0.42	0.27	1.00			
CSR3	0.42	0.34	0.27	0.52	0.61	1.00		
CSR2	0.36	0.36	0.19	0.38	0.28	0.34	1.00	
CSR1	0.29	0.27	0.38	0.51	0.37	0.30	0.48	1.00
Notes: Grow = sales growth; ROE = return on equity; Overall = overall performance; CSR (1-5) = items 1-5 of corporate social responsibility scale. All correlations are significant at the p < 0.001 level except for the following. The correlation for CSR2- Overall is significant at the p < 0.05 level.								

The hypothesis was tested by employing the structural equation modelling with a maximum likelihood estimation option. The results show that the effects of CSR (b = 0.57, p = 0.000) on performance is highly significant, hence the support H1. More specifically, the chi-square is 39.1 with 41 degrees of freedom and significant. The RMSEA-value is 0.000, and the NFI and CFI values are 0.84 and 1.000, respectively. The result shows that CSR could enhance performance.

5. Conclusion

The purpose of this paper is to investigate the effects of corporate social responsibility (CSR) on firm performance. The result shows that CSR could enhance performance. Hotel executives and managers may develop their overall CSR investments around community and product related issues, rather than employee relations, to maximize benefits of such investments over both short- and long-terms. Managers in the hotel industry, in contrast, may focus their CSR initiatives on employee relations and product issues for the longterm, not the short-term. Consistent with Lee and Park (2009), the present results suggest that casino executives and managers may find a way to minimize their CSR investments in all dimensions because those investments do not appear to impact their firm's performance at all. Freeman and Liedtka (1991) presented seven reasons why the concept of social responsibility is often abandoned. One of the reasons given was, ''Corporate social responsibility (CSR) promotes incompetence by leading managers to involve themselves in areas beyond their expertise that is, repairing society's ill'' (Freeman and Liedtka, 1991). Bauer et al. (2002) investigated the performance of international ethical mutual funds, corrected for investment style. The results show no significant difference in risk-adjusted returns between ethical and conventional funds for the period 1990-2001. This study has some limitations. The first limitation is that limitation is cross-sectional data were used in this study. Consequently, the time sequence of the relationships between CSR and organizational performance cannot be determined unambiguously. In addition, since this study only investigates Iranian hotels, hence, the findings and conclusions drawn from this research are representative of the Iranian hotelss, and the findings may not generalize to other geographic regions or cultures. Future studies can also examine the proposed relationships in other countries. Future research might consider using objective performance measures such as stock returns to examine the framework we developed here.

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Appendix. Measurement scales

Corporate social responsibility (Maignan et al., 1999)
1. We continually improve the quality of our products and services
2. Our company seeks to comply with all laws regulating hiring and employees benefits
3. We are recognized as a trustworthy company
4. Our sales persons and employees are required to provide full and accurate information to all customers
5. We give active support to programs with good social causes

Organizational performance (Jaworski and Kohli, 1993)
How do you rate your company's performance in relation to your main competitors on a seven point scale
1. Our sales growth is ___
2. Our return on equity is ___
3. Our overall performance is ___

10/15/2012