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Influence of Corporate Social Responsibility (CSR) Expenditure on Financial Performance: Empirical Evidence from the United Kingdom

by

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Abstract

Aims: CSR is considered one of the major elements that imapcts the financial performance, and it significantly helps organisations to maintain their stability and overall performance. Therefore, the aim of the current study was to assess the role of CSR in the financial performance of firms in the UK.

Method: The current study is based on a secondary quantitative research method, as a researcher has derived information from six different banks in the UK, covering the period of 2017 to 2021. For data analysis, descriptive, correlation, Hausman, and GLS random effects were used through using Stata software.

Findings: Findings from correlation analysis showed that there is a positive correlation between dependent variables (ROE, ROA), and independent variables (total assets, D/E, and CSR expenditure). Moreover, findings from the GLS model showed that all variables have a significant and positive influence on ROA, and ROE, except for the D/E ratio.

Future implications: Findings in the current research would be helpful for the researcher and policymakers in conducting studies relevant to the research topic. Moreover, researchers in future studies can also considered other control variable and mixed method for a detailed analysis.

Keywords: *Corporate Social Responsibility (CSR), financial performance, Return on Assets (ROA), Return on Equity (ROE), Assets, UK banks*

Introduction

The corporate social responsibility is one of the major aspects in the firms' performance. Corporate social responsibility is a major part as it allows for maintaining the corporate environment. CSR strategies are aimed at building a healthy corporate culture, maintaining legal and ethical standards, and being environmentally friendly. CSR can be most effectively integrated into a firm's strategic plan in a manner that will contribute to the creation of a sustainable business model that can enhance the firm's status and performance (Bag & Omrane, 2022). CSR expenditure is an example that indicates that a firm is willing and able to fulfill its obligations in an ethical manner as well as the environment and the society. It also can enhance the company's corporate culture, as well as increase the firm's overall performance to prove that it meets society's requirements. Another advantage of CSR implementation is also beneficial to firms in that it would help create competitive edges, increase the value of stocks, and foster good relations with stakeholders (Lopatta et al., 2017). This research is particularly focused at establishing the relationship between the level of compliance with CSR standards and the firms' financial performance. In particular, this study seeks to advance the hypothesis of CSR value and its consequences by examining CSR cost and various financial indicators such as ROA and ROE. Therefore, CSR not only promotes the business's ethical standards but also ensures that the business is legally on the right track and works towards ensuring that its strategies conform to the law. This is important for corporations to retain their sociopolitical license to operate as well as to build stakeholders' trust (NGUYEN & NGUYEN, 2021). Every business entity has the ability to control risks, improve public image and become more sustainable if they embrace CSR. Besides the ethical consideration, CSR can have a very meaningful impact on a firm's financial performance. Employing CSR initiatives has been found to lead to effective risk management, improved productivity, and ultimately enhanced profitability. These benefits emphasise CSR as a business investment that can bring significant value (Pham et al. , 2021):

- To evaluate the role and significance of corporate social responsibility in UK firms.
- To empirically analyse the influence of CSR financial performance of firms in the UK
- To examine other variables affecting business organisations's financial success in the UK.

Literature Review

CSR has been widely studied by academic researchers and business professionals due to its potential impact on firm performance and the creation of stakeholder value. This literature review focuses on the relationship between CSR and financial performance, the theoretical background of CSR, and the insights from the prior literature. This makes it easier to explain the relationship between CSR and financial performance with so many theories in place. Schalteger et al. (2019) argue further that Stakeholder Theory holds corporate organisations responsible to stakeholders, like employees, customers, suppliers, and society in general, and has a greater likelihood of doing well. This theory supports that CSR activities help build positive relations between the organisation and its stakeholders in improving organisational business performance. According to Battisti et al., (2022), the Resource-Based View has been found to identify that CSR can possibly be one of the ways through which a firm can gain a competitive advantage. Kamasak, 2017 also confirms that, indeed, CSR can help firms generate both physical and non-physical assets and competencies that give a company an upper hand, competitive edge and expertise within the business venture over other similar firms. For instance, future customers or investors may have a decision to patronise a particular firm because it is socially responsible or firms that do incorporate sustainability in their operations will avoid extra costs due to the efficiency of the operations. According to Gulluscio (2023), Legitimacy Theory suggests that CSR initiatives help companies regain and maintain public approval by aligning with the social domain. Such alignment can help legitimise a firm and minimise the probability of penalties or negative reactions from regulatory authorities or the public, thus contributing to financial performance.

Li et al. (2022) revealed in their study that corporate practices help to create brand awareness and information about the business which means that the good business corporate practices come along with an effective environment. The author further elaborated that brand equity allows the business to add value to their operations in such a way that it helps them to maintain an effective relationship between the business people. Menezes (2019) also explains in their study that business success comes with business growth which means that the stock value increases with the practices of the business. The author further added in their study that the stock price and stock volatility comes along with each other which means that they are firmly dependent on the involvement of the management team in the business. In a similar ground, Sekhon & Kathuria (2019) addressed that the positive impact of business practices goes relatively on the financial returns because that enables to make a reliable difference to the overall existence of the business. The author provided reliable information about the business growth and the positive connection with the good practices because that allows for maintaining an effective ground of the operations in the business. Wu et al. (2020) relatively explain in their study that the sustainability comes along with the stock returns and the progress of the returns goes along with the process of operations are being carried by the management team. The author provided an explanation that a positive relationship can be seen between the operations of the business and the returns of the business. ABIDIN (2021) also provided a relative detail on the overall business analyses by stating that good business practices come with the process of how business is carried along.

It means that business reliability comes with the intention of clear business grounds and the right tool of entering in the business. Rani & Mann (2018) stated in their study that the business practices and the business value is created through the environment of the business because that helps in making a good image of the business. The author further added that the brand equity is mainly dependent on the way business operations are carried forward because that allows to maintain a reliability of clear operations and stock returns. Memon et al. (2019) firmly argued that good corporate practice allows getting good business return because that focuses on getting a good stock pricing. The author further elaborated that the high stock price would allow to get connected with the brand value by providing a clear understanding on the progress of the business. Pucheta-Martínez & Gallego-Álvarez (2021) clearly explains that the business image and the business determination go along with each other by providing a strategic understanding about the good practices. The author further elaborated the concept by explaining that the CSR strategies are meant to make the business environment good which has the only purpose to ensure that the business determination results as a good return.

Manokaran et al. (2018) provided further information on CSR practices by explaining that CSR allows connecting with business practices and stock prices because that is the major motive of business performance. It has been clearly expressed by the author in the study that the activities of the business goes with the right strategies because that helps in bringing the right value of the business. Yadav & Sinha (2021) provided information in their study that CSR promotes the business practices which empower the customer traffic as well as company profit increases with time. The author further added that the CSR activity allows to be connected with the employee engagement which helps in maintaining the customer retention and loyalty which helps in maintaining the revenue and the high business return.

Based on a literature review, this study proposes the following hypotheses to determine the interaction between CSR expenditure and the performance of the firm. The emphasis is on understanding how CSR expenditure, CSR assets, and the debt-to-equity ratio affect the financial performance of UK firms by using ROE and ROA ratios.

CSR spending is hypothesised to affect the financial performance of a firm in the context of the study. It posits that CSR projects such as the provision of stakes to support community advancement, environmental conservation, and employee satisfaction should and will improve the image of the firm and efficiency hence better financial returns Wang & Sarkis, (2017). The following are the hypotheses on CSR spending:

- H1a CSR expenditure has a significant influence on ROE of the UK's firms
- H0a CSR expenditure has no significant influence on ROE of the UK's firms
- H1b CSR expenditure has a significant influence on ROA of the UK's firms
- H0b CSR expenditure has no significant influence on ROA of the UK's firms

The total assets of a firm have been identified as having a significant relationship with the financial performance of a firm. The test refers to a higher asset base as indicating better operational capacity and possible revenue-earning capacity. The following are the hypotheses that explain how assets affect financial performance:

- H1c Assets have a significant influence on ROE of the UK's firms
- H0c Assets have no significant influence on ROE of the UK's firms
- H1d Assets have a significant influence on ROA of the UK's firms
- H0d Assets has no significant influence on ROA of the UK's firms

Debt to equity ratio is an indicator of financial leverage and shows the extent of borrowing that a firm undertakes against the shareholders' funds Orlu et al., (2022). The following hypotheses are used to evaluate how this ratio affects financial performance

- H1e Debt to Equity has a significant influence on ROE of the UK's firms
- H0e Debt to Equity has no significant influence on ROE of the UK's firms
- H1f Debt to Equity has a significant influence on ROA of the UK's firms
- H0f Debt to Equity has no significant influence on ROA of the UK's firms

Methodology

In research philosophy, there are two main types of philosophies namely; positivism and interpretivism. Likely, Saunders et al. (2015) in their study indicated that the philosophy of positivism is prioritised to explain numerical data/information, while interpretivism is used for textual data. However, the current research is based on statistical data and hypothesis testing; therefore, a researcher has relied on the philosophy of positivism. The justification for using the philosophy of positivism is as it assists the researcher in logical and precise findings (Alharahsheh & Pius, 2020). Additionally, it also eliminates the biases from gathered information, and overall increase the reliability and credibility of the research.

In research design, there are two ways qualitative research design and quantitative research design (Edmonds & Kennedy, 2016). In this specified research, the author has relied on the quantitative research method, as the researcher's aim is to evaluate the influence of CSR on the financial performance of UK firms. Thus, it significantly helps the researcher to ascertain the truth relevant to the research topic.

Research approach refers to the process or method used while conducting research. Although, there are two main types of approaches i.e. deductive and inductive approaches (Armat et al., 2018). The author further evaluated that the inductive approach is used for qualitative studies, while the deductive approach is used for quantitative research. Notably, the current research is based on the quantitative research method; therefore, the author has relied on a deductive approach, and it significantly helps in hypothesis development, based on the aim and objectives of the research.

The source of data in this specified research was secondary, as the aim of the researcher was to assess the influence of CSR on the financial performance of UK firms. For the purpose of this, data has been derived from annual reports of six UK banks from 2017 to 2021. Regarding variables, ROA and ROE were used as a proxy of financial performance, CSR expenditure growth % was used as an independent variable, and firm size (total assets) and D/E ratio were used as control variables. For data analysis, descriptive statistics, correlation analysis, Hausman test, and GLS random effect were used through using Stata software, to ascertain statistical information and association between variables.

Results

Descriptive Statistics

Table 1 - Descriptive Statistics

Variables	Obs	Mean	Std. Dev.	Min	Max
ROA	30	0.209943	0.255352	-0.33454	0.591548
ROE %	30	5.129007	5.471745	-9.391	13.64
Total Assets £	30	1846773	4484565	43456	25200000.00
D/E Ratio	30	1.7955	1.490125	0.09	5.4
CSR %	30	3.163333	0.958711	1.45	4.8

Descriptive statistic has been used to evaluate the characteristics of the variables involved in the current research. Referring to the above table, it can be seen that the mean value of ROA is found to be 0.209, and its standard deviation value is determined to be 0.255. It implies that the average rate of ROA is 20.9% in UK firms, and it is expected to deviate towards 25.5%. Moreover, ROE has also been considered an indicator of financial performance. It can be observed that the average ROE is found to be 5.12%, and it is expected to deviate toward 5.47%. On the other hand, the mean value of total Assets is found to be 1846773, and its standard deviation value is which 4484565 denotes that the average size of the firm (total assets) is found to be £1,846,773, and it is expected to deviate towards £4,484,565. Further, the mean value of the D/E ratio is 1.795, and its standard deviation value is 1.49 which suggested that the average D/E ratio is found to be 1.79 and it is expected to deviate towards 1.49. Lastly, the mean value of CSR is determined to be 3.16, and its standard deviation value is 0.95 which implies that average CSR expenditure is found to be 3.16%, and it is expected to deviate towards 0.95%.

Correlation Analysis

Table 2 - Correlation Analysis

	ROA	ROE	Total Assets	D/E Ratio	CSR
ROA %	1				
ROE %	0.9233*	1			

	0.000				
Total Assets £	0.2572*	0.2132*	1		
	0.007	0.0258			
D/E Ratio	0.078	0.2507	-0.1861	1	
	0.682	0.1814	0.3248		
CSR %	0.1420*	0.0779*	0.1163	0.4336*	1
	0.0454	0.0254	0.5406	0.0167	

Correlation analysis has also been used to determine the direction and level of association between variables included in the current research. From table 2, it can be seen that the coefficient value of ROA with respect to ROE is found to be 0.923 which implies that there is a positive and strong association between ROA and ROE. Additionally, the coefficient value of total assets with respect to ROA is computed to be 0.257 which denotes that there is a positive, but weak association between ROA and total assets. Similarly, there is also a positive but weak association between ROA and D/E ratio, as the coefficient value is identified as 0.078. Lastly, the coefficient value of CSR with respect to ROA is recorded as 0.1420 which demonstrated that there is a positive and weak association between ROA and CSR.

The further above table also indicates the relationship between ROE and other variables. It can be seen that ROE has also a positive, but weak association with total assets, as the coefficient value is determined to be 0.213. Moreover, ROE has also a positive and weak association with the D/E ratio and CSR, as the coefficient value is found to be 0.250 and 0.077, respectively. Thus it implies that both ROA and ROE are positively correlated with total assets, D/E, and CSR.

Hausman Test

Table 3 - Hausman Test - ROE

	(b) fe	(B) re	(b-B) Difference	sqrt(diag(V_b-V_B)) S.E.
CSR %	0.46581	-1.7471	2.21285	1.6044
Total Assets £	0.000	0.000	0.000	.
DE Ratio	0.61517	1.62853	-1.0134	1.23755

Test: Ho: difference in coefficients not systematic

chi2(2) = (b-B)'[(V_b-V_B)^(-1)](b-B)

= 2.63

Prob>chi2 = 0.2686

Table 4 - Hausman Test - ROA

	(b) fe	(B) re	(b-B) Difference	sqrt(diag(V_b-V_B)) S.E.
CSR %	0.06501	-0.0798	0.14483	0.0769
Total Assets £	0.00	0.00	0.00	.
DE Ratio	0.07149	0.04656	0.02493	0.05934

Test: Ho: difference in coefficients not systematic

chi2(2) = (b-B)'[(V_b-V_B)^(-1)](b-B)

= 3.69

Prob>chi2 = 0.1584

The Hausman test has also been used to detect the existence of random or fixed effects. Likely, Lee and Yu (2020) in their study indicated that in the Hausman test, if the P value is found to be less than the threshold of 0.05 then the null hypothesis is rejected and the fixed effect is preferred, or vice-versa. However, referring to the above outcome, it can be seen that the P value of ROA is 0.268 > 0.05, and ROE is 0.158 > 0.05. Thus both values are found to be greater than a threshold which suggested that the null hypothesis is accepted, and the random effect is preferred use.

Random Effect GLS

Table 5 - Random Effect GLS - ROA

ROA	Coef.	Std. Err.	Z	P>|z|	[95% Conf. Int	
CSR %	**1.747	1.140	-1.53	0.012	-3.981	0.487
Total Assets £	**0.039	0.000	1.80	0.07	0.00	0.00
D/E Ratio	***1.628	0.741	2.2	0.028	0.174	3.082
_cons	**6.994	3.320	2.11	0.035	0.485	13.503

Number of Obs	30	R-Square	Within	0.0217
Number of Groups	6		Between	0.677
Prob	0.0084		Overall	0.2072

From the above table, it can be seen that the coefficient value of CSR is computed to be 1.747, and its P value is found to be 0.012 < 0.05, which implies that CSR has a positive and significant influence on ROA. Similarly, a total asset has also a positive influence on ROA, as the coefficient value is found to be 0.039, and it is significant at the 5% level. Lastly, the D/E ratio has also a positive, and significant influence on ROA, as the coefficient value is determined to be 1.628, and the P value is 0.028 < 0.05.

Further while referring to the above table, it is also noteworthy that the overall value of R-square is found to be 0.207 which suggested that overall 20.7% changes in the model are predicted due to variance in independent variables. Further, the Prob value is found to be 0.008 < 0.05 which suggested that the model is fit for analysis.

Table 6 - Random Effect GLS - ROE

ROE	Coef.	Std. Err.	Z	P>|z|	[95% Conf. Int	
CSR %	**0.079	0.054	-1.46	0.014	-0.187	0.027
Total Assets £	*0.000	0.000	1.8200	0.0690	0.000	0.000
DE Ratio	0.046	0.035	1.31	0.191	-0.023	0.116
_cons	**0.342	0.159	2.15	0.031	0.030	0.654
Number of Obs		30		R-Square	Within	0.0157
Number of Groups		6			Between	0.7854
Prob		0.0198			Overall	0.1519

Referring to table 6, it can be seen that the coefficient value of CSR is found to be 0.079, and its P value is found to be 0.014 < 0.05, which demonstrated that CSR has a positive and significant influence on ROE. Similarly, the total asset has also a positive influence on ROE, as the coefficient value is identified as 0.000, and it is significant at the 10% level. Lastly, the D/E ratio has also a positive, but an insignificant influence on ROE, as the coefficient value is determined to be 1.628, and the P value is 0.191 > 0.1.

Further, it is also noteworthy that the overall value of R-square is found to be 0.151 which suggested that an overall 15.1% change in the model is predicted due to variance in independent variables. Moreover, the Prob value is found to be 0.0198 < 0.05, which indicates that the model is good and appropriate for analysis.

Discussion

The primary objective of the current research is to analyse the role of CSR in the UK and its influence on financial performance. For this purpose, hypotheses were framed to decipher the relationships between ROA, ROE, total assets, debt-to-equity ratio, and CSR. The results show that CSR significantly and positively affects both ROA and ROE, which is similarly captured in prior literature as playing a significant role in enhancing the sustainability of business organisations and bringing about improved financial performance (Pham et al., 2021; Bag & Omrane, 2022). This supports hypotheses H1a and H1b by indicating that expenditure on CSR positively affects both ROA and ROE. The study also established that total assets have a positive and significant effect on the ROA and ROE of banks in the UK. This agrees with prior empirical literature indicating that firm size has a positive correlation to financial performance. Among the benefits to be accrued by larger firms include high sales, economies of scale, growth, and financial resources accruable to these firms (Kallmuenzer & Peters, 2018; Lin et al., 2019). As a result, hypotheses H1c and H1d are also supported, showing that assets positively impact ROA and ROE. Lastly, findings in the current study has also revealed that the D/E ratio has a positive and significant influence on ROA. Further, literature and previous studies have also pointed out that a higher debt-to-equity ratio provides an advantage for expanding business operations, and ultimately positively contributed to financial performance (Anggraeni, & Kusumawati, 2022; Bag & Omrane, 2022). Thus, H1e is also found to be correct, and it implies that the D/E ratio has a significant influence on ROE. Further, findings in the current research can also be summarised with the help of the table below:

Table 7 - Hypothesis Testing Summary

	Hypothesis Statement	**Accepted**	**Rejected**

H1a	CSR expenditure has a significant influence on ROE of the UK's firms	✓	
H0a	CSR expenditure has no significant influence on ROE of the UK's firms		✓
H1b	CSR expenditure has a significant influence on ROA of the UK's firms	✓	
H0b	CSR expenditure has no significant influence on ROA of the UK's firms		✓
H1c	Assets has a significant influence on ROE of the UK's firms	✓	
H0c	Assets has no significant influence on ROE of the UK's firms		✓
H1d	Assets has a significant influence on ROA of the UK's firms	✓	
H0d	Assets has no significant influence on ROA of the UK's firms		✓
H1e	Debt to Equity has a significant influence on ROE of the UK's firms		✓
H0e	Debt to Equity has no significant influence on ROE of the UK's firms	✓	
H1f	Debt to Equity has a significant influence on ROA of the UK's firms	✓	
H0f	Debt to Equity has no significant influence on ROA of the UK's firms		✓

Conclusion

The main intent of the current research was to empirically analyse the role of CSR and its influence on the financial performance of the UK. For the purpose of this, six banks in the UK were selected, and for statistical analysis, descriptive, correlation, Hausman, and GLS random effects were used. Although, findings revealed that CSR, total assets, and D/E ratio has a positive and significant influence on ROA. Similarly, CSR, total assets, has also a positive and significant influence on ROE, while the D/E ratio has an insignificant influence on ROE. Similarly, findings in the previous studies are also in line with the findings in the current research. Thus, in order to increase the financial performance of the firm, it is essential to expand on CSR-related activities.

Future Implications

The current research has particularly focused on the banks in the UK, to empirically analyse the role of CSR on financial performance in the UK. Although the current research is limited to the quantitative research method, further qualitative analysis can also be carried out in future research, for in-depth analysis. Moreover, current research has also considered total assets and D/E ratio as control variables, but other variables (i.e. net profit, revenue, corporate governance, and board size) can also be considered for detailed analysis in future research.

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