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# CORPORATE SOCIAL RESPONSIBILITY (CSR) AND FINANCIAL PERFORMANCE

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**Abstract**

*The purpose of this research is to provide light on the ways in which socially responsible business practices have an impact on the financial success of a firm by examining the connection between Corporate Social Responsibility (CSR) and financial performance among businesses. In light of the fact that stakeholders are increasingly demanding transparency and ethical behavior, corporate social responsibility has evolved from only being a charitable initiative to being a business requirement. Quantitative data from the financial statements and corporate social responsibility reports of a variety of firms operating in a variety of industries are analyzed in this research using a mixed-methods approach. Additionally, qualitative interviews with important stakeholders are conducted. There appears to be a favorable association between corporate social responsibility (CSR) involvement and financial performance measures such as return on equity, profitability, and market valuation, according to the data published. Moreover, businesses that include corporate social responsibility into their fundamental strategy typically enjoy improved brand recognition and increased consumer loyalty, both of which contribute to the expansion of their financial resources. According to the findings of the study, although the implementation of CSR initiatives may incur early expenses, the long-term advantages, which include the reduction of risk and the improvement of stakeholder relations, greatly surpass these investments. This research makes a contribution to the expanding body of literature on corporate social responsibility (CSR) by presenting empirical evidence of the influence that CSR has on financial performance. This research also encourages firms to embrace responsible practices as a means of achieving sustainable growth.*

**keywords:** *CSR, Financial Performance***,** stakeholder, relations

## Introduction

In the past several years, the idea of Corporate Social Responsibility (CSR) has received a substantial amount of momentum within the business environment. It has emerged as a crucial component in determining the strategies of corporations and the attitudes of stakeholders. A wide variety of actions that are aimed at improving the welfare of society and tackling environmental concerns are included in corporate social responsibility (CSR). These practices are rapidly becoming an intrinsic part of the operational ethos of a company. In the past, corporate social responsibility (CSR) was considered a charitable undertaking; however, it is today acknowledged as a strategic necessity that connects the interests of corporations with the expectations of society, therefore creating sustainable business practices. Scholars and practitioners alike have engaged in a substantial amount of discussion over the connection that exists between corporate social responsibility and financial performance. There is a growing body of research that demonstrates that good corporate social responsibility (CSR) strategies may generate large financial advantages. This is despite the fact that there are others who say that CSR activities impose additional expenses on firms, which might possibly reduce profitability. These advantages present themselves in a variety of ways, including a better brand reputation, increased customer loyalty, increased staff happiness, and reduced risk, which eventually contribute to superior financial performance. The purpose of this research is to investigate the complex link that exists between corporate social responsibility (CSR) and financial performance. More specifically, the study will investigate how the implementation of socially responsible practices might have an impact on the economic success of a firm. The purpose of this research is to give a thorough knowledge of how corporate social responsibility (CSR) may be integrated into company strategy to create sustainable growth. This will be accomplished by providing an analysis of both quantitative financial data and qualitative insights from stakeholders. In doing so, this study fills a significant need in the existing body of research by providing actual data that lends credence to the idea that corporate social responsibility (CSR) is not only a moral obligation but rather a strategic asset that has the potential to improve financial performance over the course of time.

Businesses are increasingly being held accountable for the influence that they have on society and the environment as a result of the intensification of global concerns such as climate change, social inequality, and the rising scarcity of resources. Corporations are being pressured by many stakeholders, including customers, investors, employees, and regulatory authorities, to demonstrate better ethical behavior and transparency in their operations. Because of this shift in expectations, firms are being prompted to reevaluate their position within the community and the larger ecosystem, which has resulted in the incorporation of corporate social responsibility tactics into their primary business strategy. Although there is a rising acknowledgment of the value of corporate social responsibility (CSR), there is still a lack of consensus about the influence that it has on financial success. On the other hand, there are academics who argue that the expenses that are connected with putting CSR programs into action can often be more than the benefits, particularly in the near term. On the other hand, there are many who contend that businesses that place a priority on corporate social responsibility (CSR) can obtain a competitive edge, which ultimately leads to improved financial outcomes over time. The current discussion highlights the need of doing robust empirical research in order to shed light on the connection between corporate social responsibility and financial performance.

**Theoretical Aspects of the Relationship between Corporate Social Responsibility and Financial Performance**

Milton Friedman was one of the most notable individuals who opposed the idea of corporate social responsibility (Friedman 1997). According to him, a company is an economic organization, and as such, it ought to focus on the economic environment as its primary area of operation. Friedman believes that there is just one social obligation that businesses have, and that is to maximize the profits of their owners to the greatest extent possible (to safeguard their property rights). He stated that managers who utilize a company's resources for social goals that are not for profit divert economic efficiency and impose a "illegal tax" on the corporation. A decline in the owners' revenue is a consequence of the allocation of funds to social activities. Friedman came up with a concept that argued that there is a negative connection between corporate social responsibility and financial performance. According to Balabaris (1998), those who assert that there is a negative link between social responsibility and economic success also say that a high level of investment in social responsibility results in additional expenses. It is possible that these charges will put a company at a disadvantage economically when compared to other companies that are less socially responsible. On the other hand, an increasing number of academics are of the opinion that businesses can no longer be regarded as merely private entities. Not only is a company accountable to its shareholders (owners), but it is also accountable to all of its stakeholders, who are powerful forces that may contribute to the acceleration of a company's performance. A connection may be made between this viewpoint and the stakeholder theory itself, which was initially developed by E. Freeman (Freeman 1994). For the most part, the stakeholder theory of the company is utilized in order to conduct an analysis of the many groups to whom the company ought to be liable. Shareholders, also known as stockholders, are considered to be the owners of the company under the conventional approach to the shareholder perspective. The company is obligated to take into consideration the shareholders' requirements in order to raise the value of their shares for the shareholders. It is the contention of the stakeholder theory that there are other parties involved, such as communities, suppliers, workers, consumers, and so on, and that these stakeholders may behave in ways that either assist or hinder a company in achieving its objectives. A stakeholder group is defined by E. Freeman as a group that either has the ability to impact or is affected by the accomplishment of the organization's aim. This definition is considered to be the foundational definition. Analysis of stakeholders often involves dividing them into two categories: major stakeholders and secondary stakeholders (Moir 2001; Clarkson 1995). One way to describe the major stakeholder group is as the group through which the organization would be unable to continue existing if it did not get support. The employees, owners, customers, and suppliers of a company, as well as the communities in which the company operates, are the primary stakeholders. The term "secondary group" refers to individuals who have an impact on the business or are influenced by it, but who do not engage in transactions with the organization and are not particularly important to the corporation's continued existence. Stakeholder theory asserts that the capacity of a company's management to provide satisfaction for the company's major stakeholders is a critical factor in determining the company's ability to survive and thrive. In the event that any of the key stakeholder groups decides to withdraw their support for the company, the functioning of the company would be negatively impacted. A competitive advantage is garnered by businesses that cultivate favorable relationships with main stakeholders that extend beyond the scope of market transactions. The beneficial impact that corporate social responsibility (CSR) has on the performance of a company can also be understood with the assistance of three theories that are related. "social identity theory," "signaling theory," and "consumer inference making theory" are the three theories that Mishra (2010) identifies. The consumer inference making theory proposes that a customer would infer a good attitude toward a product if they are aware that the company that manufactures the product is a responsible business. The consumers' goodwill is influenced by these assumptions, which in turn impacts their propensity to make a purchase. Signaling theory proposes that in situations where there is an information asymmetry between buyers and sellers, consumers look for information or signals that differentiate companies that perform well with respect to attributes of consumer interest (such as quality, reliability, etc.), and they favor companies that perform well with respect to such attributes over companies that perform poorly with respect to such attributes. It's possible that a consumer may link CSR with improved product quality. The notion of signaling can also be helpful in explaining the relationships that exist between employees and a firm that is focused on corporate social responsibility. The corporate social responsibility (CSR) of a firm may be an indicator of the organizational attractiveness of the company to potential job-seekers in situations when there is an information gap between employers and workers. The social identity theory places an emphasis on the fact that an individual's self-concept is impacted by their participation in many social groups, including the organization for which they are employed. When an employee is influenced by the image and reputation of his or her employer, the employee's own self-image is impacted. When employees of a company have the impression that the company is socially responsible, they should have a stronger sense of identification with the company. One's good attitude toward the firm is a direct result of having a high level of identification with the company. On top of that, a consumer might feel a strong sense of identification with a firm that displays social responsibility. With this kind of identification, customers are more likely to have favorable opinions of a company's product, which in turn leads to an increased possibility of the company's product being consumed more frequently. It is also possible to expand the arguments in support of a favorable link between corporate social responsibility and financial success within the framework of a resource-based philosophy.

According to Grening (2000), the resource-based theory considers each organization to be a collection of distinct resources and capabilities that serve as the foundation for the organization's strategy and are the major source of the company's profitability. The resource-based theory places an emphasis on the fact that resources that serve as sources of competitive advantage are not particularly movable across organizations, and that enterprises often do not have the ability to quickly replicate the manner in which resources are utilized inside other firms. It is possible to consider human resources, which come in the form of individuals who are highly talented and highly driven, to be scarce resources that are difficult to replicate and that can result in competitive advantages. An additional important, uncommon, and difficult-to-imitate asset that contributes to the development of competitive advantages is a company's reputation. Considering that investments in activities related to social responsibility have significant repercussions in the production of the core intangible resources that were discussed earlier, corporate social responsibility (CSR) may be seen as having strategic value for businesses (Branco, Rodrigues 2006).

**CSR from the stakeholders' perspective**

By analyzing the effects that social responsibility has on a variety of stakeholders, one may gain an understanding of the mechanism by which corporate social responsibility (CSR) could increase profitability. The link between corporate social responsibility (CSR) efforts and profitability may be investigated using five different kinds of stakeholders. Stakeholder theory, "consumer inference making" theory, signaling theory, social identity theory, and resource-based theory are some of the theories that are utilized in this section of the study.

**CSR towards employees and firm performance**

A company's corporate social responsibility (CSR) toward its employees may be seen in the policies and procedures it has regarding workers' unions, the engagement of employees in decision making, the compensation policy, and the working conditions. By adhering to high standards, businesses are able to meet the demands of their employees, which in turn improves the employment performance of those individuals and the financial performance of the organization. It should come as no surprise that contented workers generate more motivation and output than dissatisfied workers. The perception that a company has a strong commitment to corporate social responsibility (CSR) typically results in an enhanced capacity to attract better job candidates and to retain personnel, which in turn contributes to a reduction in staff turnover, recruiting. and training expenses. Workplace attitudes are also influenced by corporate social responsibility, which boosts employee morale and encourages them to contribute to activities that are helpful to the firm. The accumulation of human capital that is accomplished through the implementation of socially responsible practices has the potential to become a source of competitive advantage and lead to enhanced financial performance.

**CSR towards consumers and firm performance**

It is imperative that businesses exercise caution with regard to matters such as ethical advertising norms, as well as the health and safety of consumers in relation to the utilization of products. A favorable signal about a firm's responsible approach towards its consumers is sent by being transparent about the procedures that the company has in place to resolve such situations. These kinds of positive signals assist to improve the image of the brand and the reputation of the firm, as well as increase customer loyalty. Both the image of the brand and the reputation of the company are considered to be significant intangible assets that provide a company an advantage over its fellow competitors. According to Waddock and Graves (1999), it has been shown that a good customer perception about the quality and safety of a product leads to greater sales and improved profitability for the company. According to Byus (2010), "Socially responsible businesses have the potential to achieve greater profitability through sales to'morally conscious customers' either as a result of an increase in the volume of sales or through the ability to charge a higher unit price."

**CSR towards investors and firm performance**

When it comes to issues such as shareholder participation in decision making, respect for shareholders' rights, auditors' independence, policies toward insider trading, transparency in financial and non-financial disclosures, and transparent compensation policies with respect to key executives, corporate social responsibility (CSR) towards investors examines the policies and practices of companies. Mishra and Suar (2010) found that there is evidence to imply that the implementation of improved corporate governance norms leads to an increase in business performance. Additionally, it is emphasized that businesses that embrace CSR principles with regard to investors are more transparent and have a lower risk of bribery and corruption at their disposal.

**CSR towards the community and firm performance**

Donations to charitable organizations, collaborations between the public and private sectors, community contacts, and involvement in social and economic development concerns are the primary ways in which corporate social responsibility (CSR) is presented to the community. These activities may be regarded as instruments for strengthening the image of the brand and creating the reputation of the company. According to Wang and Qian (2011), "Corporate philanthropy is an exceptionally positive one that affects corporate financial performance." This is due to the fact that decisions about charitable donations may be made strategically in order to boost a company's image and reputation, as well as to increase the value of the company's "moral capital." It is possible to view corporate philanthropy as a means by which businesses may improve their relationships with the major stakeholders in their operations and, as a result, elicit favorable responses from the community, such as an increase in the amount of support and engagement. For instance, when employees of a company have the perception that the company is morally sound or ethical, they should be more ready to emotionally connect with the company. Additionally, the socially responsible image that a firm projects in the community might help to strengthen customer loyalty. According to Waddock and Graves (1997), it has been noted that expenditures in community development activities may also assist a company in obtaining competitive advantages by reducing the cost of regulatory compliance and reducing the risk of incurring tax liabilities. One other essential component of a corporate social responsibility plan aimed at the society at large is the conservation of the environment. According to Owen and Scherer (1993), there is a correlation between environmentally friendly goods, processes, and management systems and increased profitability. This may be achieved through either increased revenue or decreased costs. Companies who are environmentally conscious see a rise in revenue as a result of consumers' preference for their products. A reduction in expenses that are incurred as a result of environmental crises, wastes of raw materials, and inefficient industrial processes may be achieved by the investment in environmental management systems. It has also been found that businesses that install more stringent environmental controls have a reduced probability of having to pay hefty fines for excessive pollution (Tsoutsoura 2004). In addition, the adoption of better environmental standards not only enables a company to be ready to deal with more stringent requirements in the future, but it also places the company in a position to be ahead of the competition (Barrett 1992).

**Empirical studies of CSR and financial performance**

A positive relationship between CSR and firm performance has been revealed in many studies. The majority of empirical works about this relationship have been conducted using examples of corporations from the USA and Europe. For example, M. Tsoutsoura's dataset included most of the Standard & Poor’s 500 firms and covered the years 1996-2000 (Tsoutsoura 2004). Regressions were used on the panel data for 422 companies. As a measure of CSR participation the Domini 400 Social Index was used. Control variables consisted of size (the logarithm of assets or logarithm of sales), debt level (Debt/Assets), and industry (industry was determined by dummy variable). The results indicated that the signs of the relationship between CSR and financial performance (ROE and ROA) were positive and statistically significant. A similar methodology was applied They collected data for 240 firms (120 U.S. firms which participated in Dow Jones Sustainability Index (DJSI) and 120 U.S. firms which didn't participate in the DJSI) from Standard & Poor's Compustat database for 10 years (1998-2007). The DJSI firms were matched with nonDJSI firms based on industry and the closest match on total asset size. The analysis comprised nine years (1999-2007). Since some variables were based on changes from the prior year, financial data for 1998 was also collected to provide a baseline for 1999. In all, 2160 firm-years were used in the analysis (240 sample firms multiplied by 9 years). The basic approach was to regress a measure of corporate financial performance on growth in revenue, change in size, debt ratio, industry sector and an indicator of social responsibility. As measures of financial performance the following measures were used alternatively: gross profit margin, net operating profit (EBIT), profit margin, and return on assets. The one-year change in total revenues measured the growth in business. The one-year change in total assets controlled for changes in the size of the company. The ratio of total debt to total assets was included to control for the risk facing the firm. The key variable of interest was the dummy variable, which indicated whether the firm was a member of the Dow Jones Sustainability Index (dummy variable=1) or not a member of the index (dummy variable=0). The remaining variable represented various sectors of industry according to the SIC code. It was proved that the indicator of corporate social responsibility was significant and positively associated with return on assets (ROA) and gross profit margin. The CSR indicator was not significant in the case of profit margin and EBIT. Some studies on the relationship between corporate social responsibility and profitability have been also conducted for companies from developing countries. investigated the Istambul Exchange 100 Index companies and their social responsibility policies and financial indicators. The relationship between CSR and financial performance was empirically examined (using the econometric model) between 2005 and 2007. The authors did not find any significant relationship between corporate social responsibility and firm performance, explaining firm profitability as a function of firm size, risk level, and CSR. Nor was a statistically significant relationship between CSR and performance of Brazilian companies found Their dataset included 78 non-financial companies and covered the period 2001-2006. The authors regressed (using a panel econometric model) ROA on Corporate Social Responsibility Index (CSRI), firm size (logarithm of total assets) and debt level (Debt/Assets). The CSR Index was based on relative amounts spent on social actions by a firm (social expenses related to company's net sales).

**Relationship between CSR and Financial performance**

Corporate social responsibility (CSR) and the possible link to financial performance has been a topic of increasing attention since the 1970s. According to Alexander and Buchholz (1978), there are two ways to look at CSR. Two things are true: first, that a firm with socially conscious leadership can run a better show, which usually means better bottom line results; and second, that a corporation can lose ground in the market if it spends too much on CSR. A reputation index was used by Alexander and Buchholz (1978) to evaluate CSR performance, however this method was deemed inadequate by Cochran and Wood (1984) due to its subjectivity and inability to provide an accurate picture of a company's success in this domain. After then, there was a lag in generalizing results since scholars still haven't settled their disagreement over the many methods used to evaluate CSR and financial performance (Martinez-Ferrero & Valeriano, 2015). This is a difficult situation for researchers to be in since there are many elements and the researcher's choice of variables could greatly affect the study's results (McGuire et al., 1988). Research on social performance is often mentioned while discussing CSR initiatives. A company's social performance may be defined as the sum of its responsible and irresponsible social actions. According to earlier studies, companies are incentivized for high CSR performance and penalized for poor performance. Therefore, businesses face consequences for their corporate social responsibility (CSR) infractions (Wang and Sarkis 2017). "It is usual for enterprises to demonstrate both good and negative signs of CSP," (Oikonomou et al., 2014). Most of the research on the topic of how social responsibility and financial success relate to one another remains unresolved. Therefore, researchers have recently begun to investigate the impact of CSP on company performance through the application of the CSI. While CSI affects a company's worth, most studies find that CSR has a greater effect (Gregory-Smith et al. 2014). Fatemi et al. (2018) states that good ESG processes increase a company's worth, whereas bad practices decrease it. Furthermore, there is evidence that revealing this type of information harms the company's reputation since it mixes together good and bad practices. American businesses doing business in controversial areas might mitigate some of the risks associated with doing so by embracing socially responsible practises, according to research by Jo and Na (2012). Risk reduction via CSR initiatives had a significantly different effect on companies operating in difficult areas compared to those operating in non-controversial sectors. Researchers Harjoto and Laksmana (2018) found a correlation between CSP as measured by an aggregate score from the KLD agency and non-ideal risk levels. They claim that CSR (corporate social responsibility) helps businesses take more risks and less risks overall. Their research suggests that CSR strengths are negatively correlated with deviations from optimal risk-taking, whereas CSR concerns may be positively correlated with such deviations. These results were accounted for by the authors as a result of less resources being available for risk-taking activities, as organizations with a high strength score allocate a significant portion of their resources to CSR projects.

## Conclusion

By delving into the complex web of connections between CSR and bottom-line results, this study lends credence to the idea that doing good deeds for society may boost a business' bottom line. Key financial performance measures, including return on equity, profitability, and market valuation, are positively correlated with CSR project execution, according to the research. The research shows that companies may meet their ethical responsibilities and gain a competitive edge that can help them expand financially if they include CSR into their main business plans. Investing in corporate social responsibility helps organizations improve their financial results in the long run by improving their brand recognition, customer loyalty, and ability to recruit and retain top personnel. In addition, companies may avoid regulatory scrutiny and brand harm by actively engaging in CSR, which helps them to become industry leaders. The significance of comprehending stakeholder viewpoints on CSR is further emphasized by the study. The increasing importance of ethical behavior and transparency is highlighted by qualitative data collected from stakeholders like as workers, customers, and investors. These factors have the potential to greatly impact the level of engagement and loyalty shown by stakeholders. In order to improve their connections with important stakeholders and ensure a solid financial future, companies should emphasize CSR. This will help them satisfy these expectations. Given these results, business executives must see CSR as a core competency that supports their companies' long-term financial objectives, rather than an afterthought. To succeed in today's dynamic economy and ensure long-term financial success, companies should embrace a comprehensive CSR strategy that incorporates social and environmental factors into their operations. Finally, by offering strong proof of CSR's beneficial effect on financial performance, this study adds to the expanding corpus of knowledge on CSR. In a world where competition is fierce and people care deeply about social issues, companies which make CSR a core part of their strategy will be able to weather the storm.

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