

---

## **How Corporate Social Responsibility Affects Accounting Performance: A Cross-Country Analysis**

---

*Submitted 20/06/20, 1<sup>st</sup> revision 14/07/20, 2<sup>nd</sup> revision 27/07/20, accepted 30/09/20*

Agus Munandar<sup>1</sup>, Akhmad Syakhroza<sup>2</sup>, Dwi Martani<sup>2</sup>, Dodik Siswanto<sup>2</sup>

**Abstract:**

**Purpose:** *The aim of this study is to examine the impact of corporate social responsibility (CSR) on the accounting performance (AP). This study extend the previous literature in terms of country coverage which employing Zakat as a proxy for CSR.*

**Design/Methodology/Approach:** *Our sample for this study is 709 firms from companies in Kuwait, Saudi Arabia, and Malaysia. We predict that highly corporate social responsibility exhibits high level of return on equity (ROE), and return on assets (ROA).*

**Findings:** *We find that firms with strong incentives for corporate social responsibility are more likely to increase their ROE and ROA. This suggest that corporate social responsibility is important platform in increasing its corporate performance.*

**Practical implications:** *Based on this study, effectiveness of implementation of CSR program benefits the society, in turn, leads the company to enhance the level of CFP.*

**Originality/Value:** *This paper uses some companies in some countries in a cross country analysis. Research results in one country often overlooks institutional and cultural factors such as corporate governance, local government regulations, and the relationship between shareholders and management.*

**Keywords:** *Cross country, Corporate Social Responsibility, corporate financial performance.*

**JEL Codes:** *M4, M41, N30.*

**Paper Type:** *Research Paper.*

---

<sup>1</sup>Accounting Department, Faculty of Economics and Business, Universitas Indonesia, E-mail: [agos.munandar@gmail.com](mailto:agos.munandar@gmail.com);

<sup>2</sup>Academic Lecturer and Researcher, Faculty of Economics and Business, Universitas Indonesia.

## **1. Introduction**

Most previous studies discussed the the impact of CSR on financial performance on a single country. Griffin and Mahon (1997) found that CSR related positively and significantly to corporate financial performance using a chemical industry sample. Kao, Yeh, Wang, and Fung (2018) also conducted research on the relationship between CSR and financial performance for the State-Owned Enterprises (SOEs) and non-SOEs in China and shows a more positive impact for non-SOEs. Likewise, Yan, Chou, Chang, and Darcy (2017) also showed a positive relationship between CSR and financial performance for a sample of companies listed on the Taiwan stock exchange.

A previous paper has a different result such as Brammer and Millington (2008) which explains that companies in the United Kingdom (UK), companies that are socially performing does not produce optimal finance performance. Likewise, Berman, Wicks, Kotha, and Jones (1999) also explained that CSR does not have a significant effect on the return of company assets (return on assets). This finding is also supported by Griffin and Mahon (1997) who show the results of CSR that are not related to assets or equity funds.

Differences in the results of various studies regarding the impact of CSR on company's financial performance due to differences in the theory of the association is supported in the research of Chen and Lin (2015). Based on stakeholder theory and value enhancement, CSR payment creates a positive appreciation thereby increasing the concern of stakeholders such as employees, consumers, investors, shareholders, and social institutions. This argument is based on the explanation of Brammer and Millington (2008) when explaining the relationship between CSR and financial performance. Stakeholder awareness creates stakeholder contributions to the company through the purchase of productive products, investments or labor. To that end, Lev, Petrovits, and Radhakrishnan (2010) explained that the positive appreciation created a good relationship between the company and its stakeholders so that it had an impact on improving the company's financial performance.

As for agency theory, the payment of CSR is seen as additional agency costs caused by conflicts of interest between shareholders and managers or the board of directors. This argument is based on the explanation of Brown, Helland, and Smith (2006) when describing the relationship between CSR and corporate financial performance. In addition, the payment of CSR is an activity that reduces company revenue thereby reducing the company's financial performance. For this reason, the payment of CSR has a negative effect on the company's financial performance.

Deviation from a previous own paper is that this paper uses companies in some countries in a cross country analysis. Research results in one country often overlook institutional and cultural factors such as corporate governance, local government regulations, and the relationship between shareholders and management (Enomoto, 2018). For this reason, cross-country studies are very appropriate and useful for

comparing the impact of institutional and cultural factors on accounting information (financial performance). Cross-country research provides answers to questions about the crucial factors that distinguish the practice of CSR in each country. For this reason, this study analyzes the impact of CSR on financial performance in a cross-country context.

This research focuses on cross-country analysis. Previous research has examined the relationship between CSR and financial performance of companies in one country (individual country). Javaid and Al-Malkawi (2018) have focused on analyzing companies in Saudi Arabia. Samad, Said, Kamarulzaman, and Mahshar (2015) conducted an analysis only for companies in Malaysia. As for Reskino (2016) and Menne, Winata, and Hossain (2016) have analyzed only for the banking sector in Indonesia. Research on the relationship between CSR and financial performance is also conducted in one country such as Griffin and Mahon, (1997) which focuses on companies in the United States, Chen and Lin (2015) and Lin, Hung, Chou, and Lai (2019) researches focus on companies in Taiwan.

## **2. Literature Review and Legislative Background**

### **2.1 Stakeholder Theory**

Stakeholder theory stated that companies must create value for all stakeholders such as employee, customer, shareholder, etc. This interconnection triggers positive support from all stakeholders, in turn, affects to the company's economy and its future (Clarkson, 2011). The company stakeholders define as entities that can influence or determined by the company. The stakeholders are of two types primary and secondary. Primary stakeholders such as shareholders, customers, employees, are very important for the survival of the company. On the other hand, secondary stakeholders consisting of government, media, competition, regulators, political groups, are not important for the core company.

Based on theoretical considerations, this implies that company should not only get high profit but also build harmonious relationships with all stakeholders. The success of a company depends on the level of harmony between the company and its stakeholders (Russo and Perrini, 2010). If the company has a good interest with their interests, the company requires high finance (Barnett, Jermier, and Lafferty, 2006). Market constituents such as employees, customers, suppliers and creditors can directly influence companies through their economic choices. Both non-market constituents such as the public, the media, nongovernmental organizations (NGOs) also indirectly influence companies through information, and perceptions that are formed (Henriques and Sadorsky, 1999). Involvement, corporate actions in social fields such as CSR affect company performance (Clarkson, 2011).

Finally, companies complicate CSR, including CSR as a role played by companies in society in legal, ethical, social and economic matters. This activity must include

community expectations. Basically, the company's operations must be in accordance with the rules of society such as adjusting the law and adjusting to ethical habits.

## **2.2 CSR and Financial Performance**

A large body of a previous paper examines the relationship between CSR and financial performance. Unfortunately, discussions about financial performance and Zakat as a measurement of CSR paid less attention. Financial performance is a main objective of management in carrying out the company. In recent years, management should consider tripple bottom line such as profit, planet, and people. Some companies consider CSR as linked to financial performance. This argument is consistent with the signaling theory and the theory of value improvement. On the other hand, some companies argue that the expenditure of CSR decreases the company's financial performance as a logic of agency theory that considers the expenditure of CSR as costs (Chen and Lin, 2015; Lin *et al.*, 2019)

A large number of studies have investigated the relationship between spending on funds for social care (CSR) and financial performance. Yan *et al.* (2017) focused on companies listed in the Taiwan stock exchange and showed a positive relationship between spending CSR and financial performance. In the context of Zakat as a measure of compay CSR, Javaid and Al-Malkawi, (2018) used Zakat as CSR indicators when conducted investigation relationship between CSR and financial performance.

This study focuses on 107 non-financial companies listed in the Saudi Arabian stock market for the period 2004-2013 and the results indicated that relationship between CSR and financial performance is significantly positive. Reskino (2016) research in Islamic banking in Indonesia found that CSR and financial performance had a significant positive relationship. In contrast, Samad *et al.*, (2015) also investigated the relationship between CSR and financial performance using companies in Malaysia and found that relationship between CSR and financial performance is significantly negative.

Based on stakeholder theory and value improvement theory, spending on CSR creates a positive reputation from stakeholder, in turn, raising awareness from stakeholder (Brammer and Millington, 2008b). This awareness creates a well relationship between stakeholders and company, in turn, it enhances company's financial performance (Lev *et al.*, 2010). The attention of stakeholders creates loyalty and protection of shareholders to the company (Brown *et al.*, 2006). This awareness also creates a company's operational efficiency, reduces company costs, and also increases company financial performance. For this reason, spending on CSR has a positive impact on increasing the company's financial performance. This reasoning leads to the hypotheses that CSR will have a positive effect on financial performance.

### 3. Data and Research Methodology

In this section, we introduce sample and the proxies for corporate social responsibility, and corporate financial performance. In addition, this section also provides methodology for testing hypothesis. The sample data downloaded from Thomson Reuters database that covers Kuwait, Saudi Arabia, and Malaysia. Research data is from 2007 to 2018 (11 years). The study uses a sample of institutions which publishes Zakat payment (CSR proxy). The final number of observations is 709 companies. The selection of corporate performance measures follow prior studies on corporate charity in Asia and Taiwan (Berman *et al.*, 1999; Chen and Lin, 2015; Griffin and Mahon, 1997). Accounting and financial data at the end of each year for every company is also collected from Thomson Reuters for measuring corporate performance.

The degree of corporate social responsibility is measured using Zakat. This figure measures levels of intensity of corporate charity spending. The indicator of Corporate Social Responsibility measure is as follows:

$$\text{CSR} = \text{Ln Zakat}$$

ROA (Returns on assets) and ROE (returns on equity) are commonly measures for past performance of corporates (Chen and Lin, 2015; Stapleton, Brealey, and Myers, 2006). These measurements indicate profit per dollar of assets and per dollar of equity, respectively:

$$\text{ROA} = \frac{\text{Income After Taxes}}{\text{Average of total asset at the beginning and the end of the year}} \times 100\%$$

and

$$\text{ROE} = \frac{\text{Income After Taxes}}{\text{Average of total equity at the beginning and the end of year}} \times 100\%$$

These proxies indicate corporate profitability, quality of corporate earning, and management efficiency to create profits (Athanasoglou, Brissimis, and Delis, 2005). In addition, these measurements are also appropriate to compare profitability and quality of earning across different corporates (Capon, Farley, and Hoenig, 1990)

The control variables in this paper are country (COUNTRY) and industrial specialties (INDUSTRY). It also used size which proxied by asset (ASSET) as a control variable. These control variables have been used in previous studies. In addition, this paper also used lagged corporate financial performance (Lagged / NI,t-1) as control variable. As

stated in Javaid and Al-Malkawi (2018) research company's current financial performance is influenced by previous financial performance.

This study used regression design to test research hypotheses. The model is specified as follows:

$$\text{Company Performance (CP)} = \alpha_1 + \alpha_2 \text{CSR}_{it} + \alpha_3 \text{controls}_{it} + \varepsilon_{it}$$

The paper is using panel data for 11 years since 2009. In the equation model,  $\alpha_2$  and  $\alpha_3$  addresses the paper hypotheses. In this mode,  $\alpha$  should be significant suggesting that CSR affects company performance (CP) significantly. In addition, sign of  $\alpha$  should be positive because the theory of value enhancement suggests that signs should be positive.

#### 4. Empirical Results

This section presents the summary of descriptive statistics in Table 1 for variables' characteristics of Islamic firms. Looking at the eleven-year average, the mean ten-year values for corporate social responsibility payment is 16.600 (US\$ Thousand). Data sample for this paper consist of 31 observation from financial industries and 678 from non financial industries, in turn, total sample is 709 observations.

**Table 1. Descriptive Statistic**

Variable	Min	Mean	Max	SD	Skewness
CSR (US \$ Ribu)	0.98	16600.00	800000.00	79000.00	7.64
ROE	-0.57	0.12	1.17	0.15	0.78
ROA	-0.15	0.07	0.51	0.08	1.12
Total Aset (US \$ Milyar)	2.64	4.71	1.24	1.37	5.86
GDP	7243.46	24128.17	55495.20	10043.89	1.32
NI <sub>t-1</sub> (US \$ Milyar)	0.42	12.10	1.20	0.31	7.06

*Source: Own study.*

Based on descriptive statistics for every country such as Kuwait, Malaysia, and Saudi Arabia the average of corporate social responsibility payment in Saudi Arabia is higher than in Kuwait and Malaysia as follows (Table 2):

**Table 2. Descriptive statistics Zakat in every country (panel data n =709)**

	N	Min	Mean	Max
Kuwait	133	0.00099	0.60063	5.71359
Malaysia	81	0.00745	1.32537	17.9903
Saudi Arabia	495	0.02027	23.4181	799.851
Total	709	0.00099	16.6138	799.851

*Source: Own study.*

Table 3 presents the correlation between LnZakat, corporate financial performance, and other control variables. It reports insignificantly correlation between the variables.

This is not a problem of multicollinearity. Note that the analysis of correlation shows the positive relationship between dependent variables and independent variables. The analysis is consistent with the research hypotheses and the theory of enhancement that stated that corporate charity will improve financial performance.

**Table 3. Correlation Table**

	LnZakat	ROE	ROA	Log Total Aset	GDP	NI <sub>t-1</sub>
LnZakat	1.00					
ROE	0.20 ***	1.00				
ROA	0.24 ***	0.88 ***	1.00			
GDP	-0.37 ***	0.03	-0.00	0.10 **	1.00	
NI <sub>t-1</sub>	0.27 ***	0.60 ***	0.77***	-0.03	-0.07	1.00

Note: \*  $p < 0.10$ ; \*\*  $p < 0.05$ ; \*\*\*  $p < 0.01$ .

Source: Own study.

Table 4 provides the variance inflation factor (VIF) for measuring multicollinearity. Multicollinearity problem will affect model fit because it increases the standard errors of the coefficients for some independent variables in the model. Multicollinearity problems lead some variables statistically insignificant to seem significant. Based on the results in Table 4, the VIF value is below 10. It indicates that it supports previous inference that this model does not have multicollinearity problem.

**Table 4. Multicollinierity Test**

Variable	VIF	1/VIF
Lnzakat	2.14	0.467
Size	1.76	0.568
GDP	1.23	0.810
Industry	1.20	0.831
NI <sub>t-1</sub>	1.18	0.846
Mean VIF	1.50	

Source: Own study.

Consistent with the regression results on the main tests are the findings in Table 6 for the eleven-year average corporate social responsibility payment for both ROE and ROA. Focusing on H1 investigates the effect of corporate social responsibility payment on ROA and ROE the results strongly support H1 that corporate social responsibility payment significantly affect ROE and ROA. This main result consistent with value enhancement theory that indicates corporate charity enhances and maximise shareholders value. It also indicates, this study supports previous study such as Brown *et al.* (2006) who argued that corporate charity has positive impact on performance of corporate.

**Table 6. Regression results**

Financial Performance  $i,t = \delta_0 + \delta_1 \text{Ln Zakat } i,t + \delta_3 \text{ SIZE} + \text{GDP}_{i,t} + \delta_4 \text{ Non Financial } i,t + \delta_5 \text{ NI}_{i,t-1} + \epsilon_{i,t}$

Variable	ROE	ROA
----------	-----	-----

Ln Zakat	0.011	***	0.009	***
Size	-0.004		-0.023	***
GDP	0.000		0.000	
NI <sub>t-1</sub>	0.559	***	0.504	***
Non Financial	-0.101	***	-0.038	***
Cons	0.026		0.145	**
N	709		709	
R2 Overall	0.367		0.606	
Chi2	81.818		282.870	
P-Value	0.000		0.000	

*Note:* \*  $p < 0.10$ ; \*\*  $p < 0.05$ ; \*\*\*  $p < 0.01$ .

*Source:* Own study.

## 5. Conclusions

The study examines the impact of corporate social responsibility on corporate financial performance. The results shed light on the relationship between CSR and financial corporate performance. High payment of corporate social responsibility will increase ROE. This main finding plays an important role for corporate social responsibility management. It recommends that companies with optimal charity disbursement as average may have high financial performance. Finally, focus on corporate social responsibility substantially affect management especially directors and CEOs to pay more attention on corporate earnings.

## References:

- Barnett, M.L., Jermier, J.M., Lafferty, B.A. 2006. Corporate Reputation: The Definitional Landscape. *Corporate Reputation Review*, 9(1), 26-38.
- Berman, S.L., Wicks, A.C., Kotha, S., Jones, T.M. 1999. Does stakeholder orientation matter? The relationship between stakeholder management models and firm financial performance. *Academy of Management Journal*, 42(5), 488-506.
- Brammer, S., Millington, A. 2008a. Does it pay to be different? An analysis of the relationship between corporate social and financial performance. *Strategic Management Journal*, 29(12), 1324-1343.
- Brown, W.O., Helland, E., Smith, J.K. 2006. Corporate philanthropic practices. *Journal of Corporate Finance*, 12(5), 855-877.
- Capon, N., Farley, J.U., Hoenig, S. 1990. Determinants of Financial Performance: *Managemnt Science*, Vol. 36, 1143-1159.
- Chen, M.H., Lin, C.P. 2015. The impact of corporate charitable giving on hospitality firm performance: Doing well by doing good? *International Journal of Hospitality Management*, 47, 25-34.
- Clarkson, M.E. 2011. Stakeholder Framework for Analyzing and Evaluating Corporate Social Performance. *Academy of Management Review*, 20(1), 92-117.
- Enomoto, M. 2018. Cross-Country Research on Earnings Quality: A Literature Review and Future Opportunities. SSRN, 2018, March.
- Griffin, J.J., Mahon, J.F. 1997. The corporate social performance and corporate financial performance debate: Twenty-five years of incomparable research. *Business and Society*, 36(1), 5-31.

- 
- Henriques, I., Sadorsky, P. 1999. The relationship between environmental commitment and managerial perceptions of stakeholder importance. *Academy of Management Journal*, 42(1), 87-99.
- Javaid, S., Al-Malkawi, H.A.N. 2018. Corporate social responsibility and financial performance in Saudi Arabia: Evidence from Zakat contribution. *Managerial Finance*, 44(6), 648-664.
- Kao, E.H., Yeh, C.C., Wang, L.H., Fung, H.G. 2018. The relationship between CSR and performance: Evidence in China. *Pacific Basin Finance Journal*, 51, 155-170.
- Lev, B., Petrovits, C., Radhakrishnan, S. 2010. Is doing good for you? How corporate charitable contributions enhance revenue growth. *Strategic Management Journal*, 31(2), 182-200.
- Lin, L., Hung, P.H., Chou, D.W., Lai, C.W. 2019. Financial performance and corporate social responsibility: Empirical evidence from Taiwan. *Asia Pacific Management Review*, 24(1), 61-71.
- Menne, F., Winata, L., Hossain, M. 2016. The Influence of CSR Practices on Financial Performance: Evidence From Islamic Financial Institutions in Indonesia. *Journal of Modern Accounting and Auditing*, 12(2).
- Personal, M., Archive, R., Athanasoglou, P., Brissimis, S., Delis, M. 2005. MPRA Bank-specific, industry-specific and macroeconomic determinants of bank profitability. *Journal of International Financial Markets, Institutions and Money*, 18(2), 121-136.
- Reskino, R. 2016. Zakat and Islamic Corporate Social Responsibility: Does It Take Effect to the Performance of Shari'a Banking? *Shirkah: Journal of Economics and Business*, 1(2), 161.
- Russo, A., Perrini, F. 2010. Investigating stakeholder theory and social capital: CSR in large firms and SMEs. *Journal of Business Ethics*, 91(2), 207-221.
- Samad, K.A., Said, R., Kamarulzaman, M.H., Mahshar, M. 2015. Exploring the Zakat Payment and Firm's Performance of Islamic Banks in Malaysia. *The 6th International Conference on Governance, Fraud, Ethics and Social Responsibility, IConGFESR 2015*.
- Stapleton, R.C., Brealey, R., Myers, S. 2006. *Principles of Corporate Finance*. The Journal of Finance, Vol. 36.
- Yan, Y.C., Chou, L.C., Chang, T.C., Darcy, J. 2017. The Impact of Social Responsibility on Corporate Performance: Evidence from Taiwan. *Accounting and Finance Research*, 6(2), 181.