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THE IMPACT OF CORPORATE SOCIAL RESPONSIBILITY ON MARKET VALUE OF QUOTED CONGLOMERATES IN NIGERIA

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Abstract

This paper uses a multiple regression model to investigate whether three Corporate Social Responsibility (CRS) variables – Community Social Responsibility, Human Resource Management and charitable contribution have significant impact on quoted conglomerates' market value as measured by Tobin's Equity Q. Firm size was factored in as an extraneous variable. The regression results reveal an insignificant relationship between community social responsibility, Human resource management and market value. However, a negative impact has been documented in relation to charitable contribution, while firm size has been found to play a significant role in the CSR-market value relationship. The study recommends that businesses carry out social responsibilities reflective of their corporate size and capability and also stresses on need for further research on corporate social responsibility in other sectors of the economy.

Introduction

In any socially responsible society, companies cannot ignore the environment and major coalition members with which they interact. There is therefore a perceived social contract between organizations and society. This presumed social contract gives firms a platform for determining their social constituencies, what these constituencies expect of their respective corporate inhabitants and how to initiate corporate social objectives to meet these expectations.

Corporate social responsibility is thus concerned with treating the stakeholders of a firm ethically or in a responsible manner (Hopkins, 2004). Stakeholders exist both within a firm and outside. Even the natural environment is a stakeholder (Carrol and Buccholz, 1999).

The field of CSR has grown exponentially in the last decade. In today's competitive environment, CSR represents a high profile notion that has strategic importance to many companies (Xueming and Bhattacharya, 2006). A firm cannot healthily operate while neglecting its environment. This has thus entrenched CSR as a corporate dictate (Oba, 2008).

A recent phenomenon is the introduction of legislations/codes of conduct to ensure that businesses undertake social activities. These include codes of conduct and standards like the Global Reporting Initiative (GRI), Global Sullivan Principles (1999), Global Compact (20020, AA1000/AA1000S of 1999, ISO 26000 and the social network standards. These have been initiated after much demands by civil rights and environmental activist groups.

The CSR issue is a growing concern in corporate Nigeria today. Several qualitative empirical studies exist in this light (See Ite, 2004, 2005; wheeler et al, 2002; Christian, 2004, and Obalola, 2008). However, quantitative studies supporting the existence of a link between CSR and financial performance are relatively scanty.

The question then arises: what impact do CSR practices have on the financial states of Nigerian firms?. In other words, do Nigerian firms that incorporate CSR into their operations reap economic benefits or is CSR just a philanthropic cost?

The debate on CSR began in the early 20th century, as concerns about large corporations and their power came to the fore (Heal and Nair, 2005). With the emphasis on globalization, the great beneficiaries seemed to be the global corporations (Garcia, 2002). In such a globalized set up and in a democratic ethos, companies cannot ignore the societies in any for the social spheres where they interact. This is because the accumulation of capital is only possible due to the existence of these societies, which constitute their markets and especially because their activities have a tridimensional impact (economic, environmental and social) on societies and their habitat (De Regil, 2003).

An examination of the relationship between CSR and market value is important to the extent that while businesses open to the interests of group in the society, they must certainly seek profits first and see maximization of shareholder's return as prime. In other words, the major/primary responsibility of business is to use its resources and engage in activities designed to increase its profits so long as it stays within the rules of the game without deception or fraud (Friedman, 1970). This study is necessary most especially at this era when CSR is becoming a growing initiative both in the corporate and public domain of the Nigerian system (Oba, 2008). The study utilises three (3) CSR proxies as independent variables to assess the values of quoted conglomerates. These are community social responsibility, human resource management, and charitable contributions. Firm size is also factored into the equation as an extraneous variable. At the other end, Tobin's equity Q, a proxy for market value is employed as the dependent variable.

The study addresses this research question what is the individual and consolidated effect of community CSR, Human Resource Management and Charitable contributions on market value of conglomerates and to what extent can the market value of these firms be predicted using these variables?

Accordingly, a null hypothesis has been advanced in response to this question – CSR proxies (community CSR, Human Resource Management and charitable contributions) have no significant impact on market value of quoted conglomerates in Nigeria.

The remainder of the paper is organized as follows:- Section two summarizes some of the theoretical arguments on the relationship and impact of CSR on the value of firms. Section three outlines the research design of the study. Section four presents and discusses the results of the study. Section five offers concluding remarks and recommendations.

Theoretical Issues

Corporate Social Responsibility and Financial Performance

The concept of CSR has been very controversial. It is highly favoured by some group of people and strongly opposed by others. According to Friedman (1970), in a free society, there is one and only one social responsibility of business to use its resources and engage in activities designed to increase its profits so long as it stays within the rules of the game, which is to say, engages in open and free competition without deception or fraud.

Friedman observes that few trends could so thoroughly undermine the very foundations of our free society as the acceptance by corporate officials of a social responsibility other than to make as much money for their stockholders as possible. Freeman (1984) directly challenged Friedman's assertion contending that firms have relationships with many constituent groups and these stakeholders both affect and are affected by the actions of the firm. He defines stakeholder as any group of individuals who can affect or is affected by the achievement of the organization's objective.

Murray and Montannari (2005) further observe that the failure to supplement the moral justification for social responsibility with economic consideration may explain why many executives view social responsiveness as a strictly "unproductive cost'. Such criticism have caused managers to develop more strategic forms of social responsibility that can be shown to deliver a financial return to the firm initiatives positioned as enlightened self-interest (Peloza, 2005).

There is an emerging view over the years that CSR can contribute to the financial performance of a company. This approach which has been described as the "enlightened stakeholder approach" suggests that corporate decision makers must consider a range of social and environmental matters if they are to maximize long term financial interest (Brine et al, 2006). But while this may have been endorsed as an underlying assumption, today's researchers are demanding more hard, quantitative evidence (Phillip and Claus, 2002). Academics who had previously reviewed the literature exploring the relationship between CSR and financial performance had found the studies to be inconclusive: no link could be proved or disproved (Orlitzky et al, 2003). Some have shown a significant positive relationship (Waddock and Graves, 1997, Orlitzky et al, 2003; Tsoutsoura, 2004) and some no statistical significant relationship (Aupperle, 1985, Brine et al, 2006).

Attempts to accurately reflect the financial return from CSR are more than an academic exercise (Peloza, 2005). The increased pressure faced by managers to justify the allocation of scarce resources means that money spent on CSR activities are more closely scrutinized and are at risk of being withdrawn. This area of research remain inconclusive but however should provide quantitative evidence so that through such widened perceived value of CSR investments, firms can better justify their role in solving societal woes from a position of enlightened self-interest.

<u>Measurement issues</u>

Determining how social and financial performance are connected is further complicated by the lack of consensus of measurement methodology as it relates to CSR (Tsoutsoura, 2004).

However, past studies have used either the kinder Lydenberg Domini Database (Nelling 2006; Waddock and Graves, 1997; Alexander and Buccholz, 1978, Tsoutsoura, 2004). Others have used survey instruments (Wokutch and Mckinney, 1991; Aupperle, 1991), or the Ethical Investment Research Service (Turban and Greening, 1997). And others, subjective indicators (Brammar et al, 2005; Feldman et al, 1997, Dowell et al, 2004, Brine et al, 2006). These bases either include one indicator of CSR and exclude the other depending on the rating agency's perception of what CSR entails.

As regards the debate on financial performance measures, two (2) broad subdivisions exist. They include market based (investor returns) and accounting based (accounting returns) measures. First market based measures hinge on growth prospects and sustainability of profits (Rust et al, 2004) and are devoid of manipulation from difference in accounting procedures (Branch, 1983; Brilloff, 1972). They represent an investor's evaluation of the ability of the firm to generate future economic earnings (McGuire et al, 1988). Two common market measures employed in CSR-financial performance studies are stock returns and Tobin's Q (See Nelling, 2006; Brammer et al, 2005; Dan, 2006; Heal, 2005, Xueming and Bhattacharya, 2006).

Alternatively, accounting based indicators such as the firm's return (ROA), return on equity (ROE), capture a firm's internal efficiency in some way (Cochran and Wood, 1984) and are however subject to managers' discretionary allocation of funds to different projects and policy choices, and this reflects internal decision-making capabilities and managerial performance rather than external market responses to organizational actions.

Research Design

Sample Selection and Data Source

The population of this study is quoted conglomerates. In Nigeria, conglomerates are the focus since as at April 2007, all quoted conglomerates were multinationals. Arguably, the history of 'organized' CSR in Nigeria can be traced to practices driven by Western Multinationals. As typical of multinationals, the motivations to engage in CSR are varied response to market forces, globalization and consumer and civil society pressures,etc. (Oyejide and Soyibo, 2001; Ahunwan, 2002; and Ite, 2004). This is because the activities of these firms are visible because of their global reach and as such there is a higher incentive to protect their brands and investments through CSR by contributing positively to their host communities.

This study uses the lottery method of simple random sampling to select five(5) out of the eight (8) quoted conglomerates in Nigeria. A general rule for the sample size is that the ratio should never fall below five, meaning that there should be five observations for each independent variable in the variable (see Hair et al, 1991).

Sources of data are the Nigerian Stock Exchange Fact Books for 2001 - 2006, daily official lists of the Nigerian Stock Exchange for the last day of trading in each of the years covered by the study, and the annual reports and accounts of the companies for all the years covered by the study.

Data Analysis Technique

The study utilizes multivariate technique of data analysis. A simple model has been employed to estimate the separate as well as the combined impacts of the CSR proxies on the value of quoted conglomerates in Nigeria. The model is estimated using the Ordinary Least Square (OLS).

Model Specification

The model uses a single dependent variable-market value represented by Tobin's Equity Q and three (3) explanatory variables community CSR (CCSR), human resource management (HRM) and charitable contributions (CC). A one year lag has been presumed to exist between CSR and performance. However, the use of lags have been identified as one of the major causes of multicollinearity; a condition that renders the estimates indeterminate. To mitigate this problem, we employ an econometric approach by lagging the dependent variable and factoring it as a variable in the function (Koutsoyiannis, 1977). We introduce firm size as a fifth variable (extraneous variable).

The model appears thus:

$T_Q = b_O + b_1 \, CCSR + b_2 \, HRM + b_3 \, CC + b_4 \, TQ_{-1} + b_5 \, Fs + uit$

Where T_Q = Tobin's Equity Q

CCSR = Community Corporate social responsibility

HRM = Human Resource Management

CC = Charitable contributions

TQ-1= A lag of dependent variable

FS = firm size

Uit= Random disturbance term (error term)

Estimation of Market value variable and CSR Proxies

The measurement of the variables used in this study is discussed below:

1) Market value: this is represented by Tobin's Equity Q. This is probably the most widely used valuation measure in empirical corporate finance (Drobetz, 2004). It is the ratio of market value or replacement value and calculated by market value of equity divided by value of total assets of the firm. A Tobin's Equity Q greater than one (1) indicates that the firm has done well with its investment decisions i.e. it has invested in positive net present value projects. In contrast, a value of Tobin's Q lower than one (1) indicates that the company did not earn its firm wide cost of capital with its investment project (Tobin, 1969).

2) Community Social Responsibility (CCSR):- This variable is measured as a dummy variable. It concerns every efforts of the company to develop its immediate environment via environment policies, and involvement in issues such as sports, education, social amenities and health matters. Where the company reports in its annual report on involvement in any of these, it scores 1 and where it does not report on any, it scores O.

3) Human Resource Management (HRM): This variable is likewise measured as a dummy. It covers three measures: Health and safety systems for employees, system for employee training and development, and equal opportunities policies (without discrimination against physical disability or racial/tribal differences). Where the company reports on involvement in these, it scores 1 and where it does not, it scores O.

4) Charitable contributions (CC): This variable is measured as the charitable contributions made by the firm as disclosed in the financial statements.

5) Firm size: This is measured as the sum of the total assets of the firm.

Analysis of Results

CSR and Market value - OLS Results

This subsection discusses the OLS results in relation to the impact of CSR on market value of quoted conglomerates in Nigeria. The study hypothesizes that the CSR proxies have significant impact on quoted conglomerate's market value. The regression results are presented in Tale 4.1

Table 4.1a Regression summary

Variables	Parameter estimate	Standard Error	Values (t)
CCSR	.379	.240	1.58
HRM	.239	.375	0.64
CC	-.644	.150	-4.30
TQ-1	.417	.114	3.66
FS	.637	.271	2.35

Table 4.1b Model Summary

R	R Square	Adjusted R Square	Standard Error of the estimate	Durbin Watson
.679	.454	.340	.6117	1.632

Table 4.1c Analysis of variance

	Sum of square	df	Mean square	F
Regression	7.458	5	1.49	3.987
Residual	8.979	24	.3742	
Total	16.437	29		

Table 4.1d Collinearity statistics

Variables	Tolerance	VIF
CCSR	.888	1.126
HRM	.982	1.018
CC	.313	3.196
TQ-1	.332	3.015
FS	.770	1.299

Regression results for table 4.1 A-D using SPSS on Secondary Data.

The value of R^2 in the plane explains that only 45% of the variation in Tobin's equity Q is accounted for by the regression line while the 55% unaccounted for is attributed to factors included in the disturbance variable u. A test of the overall significance of the regression shows a F* ratio of 3.987 and a theoretical F_ value of 2.62 at 5% level of significance at 5,24 degrees of freedom. Given that F*> F.0025, we accept that the regression is significant, and that the significant variables are explanatory factors of the variation in TQ.

The serial correlation test compares the empirical d* value obtained from the regression residuals with the theoretical dL and du in the Durbin Watson tables. In this equation, empirical d* is 1.632, while theoretical from the DW table for 30 observations and 5 explanatory variables at the upper and lower limits are

1.83 and 1.07 respectively. Based on the decision rule, since dL<d*<du, we conclude that the test is inconclusive.

To assess pairwise and multiple variable collinearity, the tolerance value and variance inflation factors are examined. The default tolerance value in SPSS for excluding a variable is .0001, which means that until more than 99.99 percent of variance is predicted by the other independent variables, the variable could be included in the regression equation. However, the tolerance value statistics for this equation are consistently greater than the common cut off threshold of .10 and also the variance inflation factors are consistently less than 10. These go to confirm the absence of multicollinearity in the equation.

Tabulated t values under this equation with regard to 24 degrees of freedom at 5% level of significance is 2.065. A comparison of observed t* and tabulated t shows that CCSR and HRM (to the extent of their being reported in annual reports) have no statistically significant effect on market value.

On the other hand CC (Charitable Contributions) have a significant negative impact on value with its coefficient as (-0.644). The economic implication of this sign is that the variable though significant has an inverse impact on market value. That is, the lesser the charitable contributions, the greater the market value.

This lends support to arguments of Friedman (1970) and his cohorts that philanthropic costs (Charitable contributions) have a negative impact on financial performance of a firm since the firm has less funds to invest into profitable sectors. It also lends weight to the argument that expenditures on corporate social activities is largely destructive of shareholder value (Navarro, 1988).

Firm size (denoted by total assets) has also been found significant in the market value –CSR relationship. The t-test and standard error test confirm this. This offers support to the works of Cho and Pucik 92006) and Xueming and Bhattacharya (2006) that the size of a firm influences the relationship between CSR and market value.

Conclusion and Policy Recommendations

While the impact of corporate social responsibility on market value has been analysed in several recent cross sectional time series studies in developed economies, little is known about the impact in developing economies. This study fills this gap and thus poses as a first hand empirical awareness of the financial implication of CSR practices of firms in Nigeria.

The ordinary least square (OLS) results indicate that the four variables CCSR, HRM, CC and FS) have a significant aggregate impact (at 5%) on market value of the sample firms.It also confirms the insignificance of CCSR and HRM as predictor variables of the market value of sample firms while charitable contributions was found to have a significant negative impact on value. Firm size has been confirmed to play a major role in the link between CSR and market value. This has demonstrated that the value of CSR in maximizing market value is just a western philosophy and might not be applicable to developing countries. In line with the findings and conclusion of the study, the following recommendations are proffered.

First that CSR initiatives by businesses should be reflective of their corporate size while less financially capable companies may be better off financially by avoiding CSR actions as a misalignment of CSR with internal factors could be detrimental and lead to decreased market value. This is in line with the findings of Brine et al (2006).

Second, investors while clamouring for ethical and moral responsibilities of their companies should have in mind the financial consequences of such. They should dissuade their companies from such excessive investment but only patronize minimal and strategic CSR activities in view of a healthy relationship with the environment.

Third, the government working closely with the private sector should develop initiatives in determining common standards, reporting mechanisms and the extent to which business should be responsible.

Fourth, further research attempts should be made to develop better measures of CSR as more reliable measurement of the extent to which a company has adopted CSR will allow a more accurate analysis of the effect on value. Also the study should be extended to other strata of the stock exchange and it may be useful to use a one year lag between the measurement of financial performance and the CSR measure instead of the lag of the dependent variable employed in this study. The essence is to determine whether there may be a lag associated with the implementation of social responsibility and improved financial performance (Blackburn, Doran and Shrader, 1994) and also whether better financial performance leads to increase in the level of social responsibility for an organization (Waddock and Graves, 1997).

Finally, the model used in this study cannot provide an understanding whether socially responsible firms outperform the socially reprehensible ones and precisely how much a firm should spend on CSR. This concept is exogenous to the model in this study. This issue can be answered by future empirical works that consider this proposition.

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SAMPLE COMPANIES

1. Chellarams Nigeria PLC
2. John Holt Nigeria PLC
3. PZ Cussons Nigeria PLC
4. Unilever Nigeria PLC
5. AG Leventis Nigeria PLC