The Association Between Corporate Social Performance and Corporate Financial Performance: Evidence From Kuwait

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The literature on the association between corporate social performance (CSP) and corporate financial performance (CFP) fails to provide conclusive evidence regarding the nature of this relationship. Some studies found a positive while others reported a negative or neutral (no) relationship. The purpose of the present study is to expand earlier research on this relationship in the context of Kuwaiti corporations. To achieve this objective, a sample of Kuwaiti corporations is selected, representing all economic sectors, sizes and ages over a period of two years: 2018 and 2019. A disclosure index of CSP disclosure is developed, to measure corporate social performance. The results of the two regression models reveal that both ROA and ROE as measures of CFP are positively and significantly associated with CSP, while control variables (size and age) are not statistically significant at any acceptable level. These results suggest that corporate management should treat investing in social activities as a core business strategy that would pave a way for a higher financial performance and thus, maximize its stockholder's wealth.

Keywords: corporate social performance (CSP), corporate financial performance (CFP), Return on Assets (ROA), Return on Equity (ROE), content analysis, Kuwait stock exchange (KSE)

INTRODUCTION

Traditionally, a firm aims to make profit to maximize its value, and thus maximizing its shareholders' wealth. However, achieving this objective should not cause negative side effects for other stakeholders and society as a whole (Galant and Cadez, 2017). The research results in the area of corporate responsibility confirmed this view and concluded that corporations have a responsibility to various stakeholder groups other than shareholders. That is, a firm is expected not only to fulfill its economic responsibility, but also its social and environmental responsibilities.

The incentives of a firm's fulfilling its corporate social responsibility (CSR) are not only due to social and environmental pressure, but also based on more practical reasons associated with firm performance. As

argued by Baranett and Sulomon (2012), the better a firm manages its relationships with its stakeholders, the more successful it will be over time. Porter and Kramer (2006) have stated a similar argument; corporate social responsibility should be seen as one of the core business strategies in a firm, implying that the firm could benefit from its social investment. Weber (2008) identified five potential benefits of CSR for a company of being socially responsible: (1) the positive effects on a company's image and reputation; (2) a positive effect on employees' motivation, retention and recruitment; (3) cost savings; (4) increased revenue from higher sales and market share; and (5) a reduction of CSR-related risk.

The potential impact of corporate social activities on corporate performance motivated academics and practitioners to investigate the relationship between corporate social performance (CSP) and corporate financial performance (CFP). Literature in this area fails to provide conclusive evidence regarding the nature of this relationship. Some of the previous research results revealed a positive relationship; others documented negative or even no relationship.

The purpose of the present study is to expand earlier research on the relationship between CSP and CFP in the context of Kuwaiti corporations.

LITERATURE REVIEW

Previous research regarding the association between CSP and CFP have shown mixed results. The research results do not provide conclusive evidence on the nature of this relationship. Some results have shown a positive relationship while others reported a negative or neutral (no) relationship. There is no clear-cut conclusion as to whether there is any correlation, or lack thereof.

The first group of research, representing the majority, documented a positive relationship between CSR and CFP. Hou (2018) examines this relationship in Taiwan's firms. The study indicates that socially responsible firms can achieve financial results superior to those of firms that do not pursue CSR initiatives. Maqbool and Zameer (2018) employed a panel data set of 28 Indian commercial banks for 10 years, to verify the impact of CSR on both profitability and market returns in the Indian context. Size, risk, capital intensity and age were incorporated as control variables. The results show that CSR positively impacts profitability and stock returns. It is clearly indicated by the findings that CSR, as a valuable and rare resource, can be exploited to create a competitive advantage for the firm. Similarly, Wang (2011) empirically explored the impact of fulfilling CSR on stock performance. The main finding reveals that fulfilling CSR has a significantly positive impact on stock performance. The implication suggests that a firm could serve as a good corporate citizen, while in the meantime pursuing the growth of stockholder's wealth.

Kim and Kim (2014) examined whether CSR enhances value for shareholders. Specifically, they tested the effect of CSR on two different types of equity-holder risks (systematic and unsystematic risks). The findings suggested that social responsibility was found to enhance shareholder value by increasing Tobin's Q, while firms having minimal CSR reduced shareholder value by increasing the risk. Peters and Mullen (2009) found that the effects of corporate social responsibility could be accumulated and reinforced positively in the long run, thus leading to a better firm performance. Simpson and Kohers (2002) have found similar results. Their research results support the hypothesis that the link between social and financial performance is positive.

Using content analysis, Gamerschlag, et al. (2011) analyzed 130 listed German companies' CSR disclosures to investigate the determinants of these voluntary disclosure activities. The results show that, consistent with the political cost theory, German companies' disclosures of all CSR issues are affected by their visibility, shareholder structure, and relationship with their US stakeholders. In addition, higher profitability is associated with more environmental disclosures. Finally, size and industry membership affect the amount of CSR disclosure. Palaniappan and Srinivasa (2016) identified the relationship between corporate governance disclosure practices and firms performance with respect to profitability. The study implied positive and significant impact with the corporate governance disclosure and firms performance of manufacturing firms in India.

Varenova, et al. (2013) attempted to find a link between the CSP and CFP by exploring the perception of executives of the FTSE All-Share companies. The purpose was to investigate the insights of corporate executives on both the issues of the social responsibilities of business and the link between CSR and financial performance. Among other results, the findings indicated that socially responsible businesses employ CSR in pursuit of their commercial interests and consider it to be their competitive advantage. Moreover, the business seems to have integrated CSR into all its operations and activities and considers it as a necessity rather than luxury, which suggests that CSR and financial performance are in synergy. Similar results have been documented by other studies (e.g., Simpson & Kohers, 2002; Al-Tuwaijri, et al., 2004; Burnett & Hansen, 2008; Karagiorgos, T., 2010; Rodgers et al. (2013); Erhemjamts & Venkateswaran (2013) and Chen et. al (2015).

Although most of literature on CSR and CFP relationship documented positive relationship, yet some research took another opinion and empirically documented a negative relationship. This is based on the possible impact a company's social activities might have on its costs and expenses, that is, social responsibility incurs costs and deteriorates profitability. As mentioned by Galand and Cadez (2017), CSR is costly since being socially responsible incurs additional expenses, such as investments in pollution reduction, employee benefits packages, donations and sponsorships to the community, etc. The conventional view maintains that these expenses will deteriorate profitability and lead to a 'competitive disadvantage' (Alexander & Buchholz, 1978). Empirical evidence supports this view and found a negative relationship between the CSR and CFP. Elouidani and Zoubir (2015) analyzed the influence of CSR on the financial performance. Using a sample of 20 firms listed on the stock exchange of Casablanca between 2007 and 2010, they found a negative and significant impact of the CSR on financial performance. The negative influence is important in large companies, which means it is a mediating factor. Baird et al. (2012), and Peng & Yang (2014) have documented similar results.

The debate regarding CSR and CFP has led to a third possibility, CSR works independently, that is the relationship is neutral or no relationship. Both variables are mutually exclusive and the relation is only by chance, or there are so many interposing variables between CSR and financial performance that relationship hardly exists (Maqbool and Zameer, 2018). Empirically, McWilliams and Siegel (2000) investigated the relationship between CSR and financial performance in the sample size of 524 for a period of 6 years. The result showed upwardly biased estimates of the financial impact of CSR, but when the model was properly specified, by incorporating R&D, the result showed neutral effect of CSR on financial performance. Kraft and Hage (1990) related community service with different organizational characteristics in the sample of 82 companies. The results highlighted that community service has no effect on profit goals, low price niche, multiplicity of outputs, and workflow continuity. Similarly, Griffin and Mahon (1997) examined the relationship between CSR and corporate financial performance, while measuring CSR employs both perceptual based data (KLD Index and Fortune reputation Survey) and performance-based data (TRI data base and corporate philanthropy). The result showed that Fortune and KLD indices very closely track one another, whereas TRI and corporate philanthropy shows neutral relationship. Miron, D. and Petrache, A. (2012) examined the linkage between CSP and CFP in multinational companies operating in Romania. The study revealed that improved financial performance does not necessarily lead to better CSP, and improving CSP does not necessarily lead to better CFP. A neutral relationship has been documented by Sun et al. (2010), and Soana (2011).

As can be observed, there have been discrepancies in previous literature. Although the majority documented positive relationship, others revealed negation or no relationship. McWilliams et al (2006) explained these conflicting results to be a consequence of "inconsistency in defining CSR, inconsistency in defining firm performance, inconsistency in samples, imprecision and inconsistency in research design, misspecification of models, changes over time, or some more fundamental variances in the samples that are being analyzed." Moreover, the existing research has been conducted in different countries with different cultures and using different methods and over different periods of time. To the knowledge of the authors, no similar research has been conducted in the Gulf Region generally, and in Kuwait specifically. The present study extends earlier research on the relationship between CSP and CFP, by investigating the nature of this relationship in the context of Kuwait.

RESEARCH OBJECTIVE AND QUESTIONS

Research Objectives

The main objective of the present research is to extend previous research by investigating the nature of the relationship between CSP disclosure and CFP in the context of Kuwaiti corporations. Specifically, the purpose is to investigate the nature of this relationship, whether there is a positive, negative, or no relationship in the context of Kuwaiti corporations. For the purpose of measuring corporate performance, two accounting-based measures are used: Return on Assets (ROA), and Return on Equity (ROE).

Research Question

Based on the research objective, this study intends to answer the following questions:
- Is there a relationship between CSP and CFP as measured by ROA?
- Is there a relationship between CSP and CFP as measured by ROE?
- Is there a significant difference regarding CSP among different company size?
- Is there a significant difference regarding CSP among different company age?

RESEARCH METHODOLOGY

To achieve the research objective and to answer these questions, data were collected from the relevant source of information issued and released by a sample of Kuwaiti corporations listed on the Kuwaiti Stock Exchange (KSE). This section presents the research methodology including, sample size, the disclosure index, the source documents from which data has been collected, content analysis technique used for data collection, and finally the research hypotheses.

Sample

For the purpose of this research, a sample of Kuwaiti companies listed on the Kuwait Stock exchange (KSE) were selected. All the companies of the major economic sectors listed on the KSE's website for year 2018 and 2019 constituted the initial sample. These sectors include financial institutions, financial service, real estate, and manufacturing/industrial sector. At the time of accessing the website of the KSE (www.boursakuwait.org.kw), these sectors consisted of 147 companies representing more than 85% of the total companies listed on the KSE. We accessed the companies' websites to find out the available issued information. The search aimed at getting a complete annual report and or CSR report or any similar reports. For a company to be included in the sample it must have a complete annual and a CSR report issued either separately or within the annual report. After doing this search, the final sample consists of 71 observations representing about 25% of total population. The sample is quite representative due to the fact that it belongs to the different economic sectors, and represents different company size in each sector. The economic sectors not included in the analysis are: consumer services (16 companies), health care (4 companies), and telecommunication (5 companies)

Research Variables

The Dependent Variable (CFP)

There is no real consensus as to which indicator should be used in measuring corporate financial performance (CFP). In the area of CSR's studies, three categories of measuring CFP are commonly used. The first category is based on accounting measures, such as ROA, ROE (e.g., Ehsan and Kaleen, 2012). The second is market-based measures such as stock return and market value of a company (e.g., Hou, T. C., 2018, Karagiorgos, 2010). The third used a combination of both accounting and market-based measures, such as Tobin's Q (e.g., Maqbool and Zamer, 2018; Elouidani and Zoubir, 2015).

Each category has positive and negative traits. Accounting-based measures are available for all companies and reasonably comparable. However, they may be biased due to the varying age and assets structure across industries. On the other hand, market-based measures reflect changes in CSR faster than

accounting-based measures. However, they incorporate systematic market characteristics (non-firm-specific). As such, there has been a tendency to use more than one measure of CFP.

In this research, CFP is assessed using accounting-based measures, specifically ROA and ROE and incorporates some control variables in the analysis to eliminate the possible negative aspects of using accounting-based measures on the results. Such variables include company size and company age.

The Explanatory Variable (CSP)

To achieve the research objective, a disclosure index of potential CSP disclosure is developed. Towards this, an extensive search in the relevant literature was undertaken to identify a list of items covering most of CSR aspects. Carroll (1991) contended that corporate social responsibility should be built upon a four-level pyramid. The bottom level of the pyramid was economic responsibility. Next, a firm should fulfill its legal responsibility. The third level of corporate social responsibility was ethical responsibility. On the top level of the pyramid is human responsibility, which suggested that a firm should serve as a good corporate citizen to improve overall living quality in human society.

In a recent study, Chen et al. (2015) used the 45 Global Reporting Initiative (GRI) indicators. The 45 indicators were divided into 4 groups (labor practices, human rights, society performance, and product responsibility performance). Similarly, Karagiorgos (2010) used 26 indicators derived from GRI reports, which divided in two main groups (social performance indicators and environment performance indicator). The 26 items examined by Karagiorgos (2010) are used in the present study. This list has been tested against a sample of corporate annual reports and other sources to find out whether it needs future refinement. The final list includes 25 items.

Each of the disclosure items was scored without weighting. Using un-weighted disclosure checklist in this study is based on the argument that the weighting process will reflect interests of a particular information user; hence, increasing the subjectivity in developing the disclosure indices (Marston and Shrives, 1996). Moreover, Robbins and Auston (1986) concluded that there is no significant difference between the results based on weighted and unweighted disclosure indices.

Each of the sample annual reports was carefully scrutinized against the checklist to identify the presence/absence of each item in the report. Based on this process, each of the disclosure items in the checklist was scored one if it is disclosed or zero if not. Giving that the expected disclosure (EXD) is the maximum number of CSR items that assumed to be disclosed, the disclosure score for each company is computed as follows:

- Compute the Actual Disclosure (ACD): which is equal to the summation of the actual items disclosed for each company, scored as (1).
- Calculate the Corporate Social Performance Score (***CSP score): which is a*** disclosure index for each company and computed using the following equation:

$$\textbf{\textit{CSP score = ACD/EXD}}$$

The value of any ***CSP score*** ranges from 0 to 1, and the higher the value of the score, the higher the level of CSR disclosure.

Control Variables

It has been suggested that the relationship between CSP and CFP is affected by several factors. Among these factors are firm size, type of industry, and risk (Johansson et al., 2015). In addition to these three factors, company age has been considered as an important control variable (Maqbool and Zameern, 2018). In this research, three control variables are included: company size, type of industry, and company age.

Company Size

Elouidani and Zoubir (2015) argue that company size influences its degree of commitment in the CSR. Company size has a potential impact on social credentials. Large firms have ample resources to possess and process social information, which in turn gives the firm more competitive advantages (Maqbool and

Zameern, 2018). The larger companies are more politically visible than smaller companies. Consequently, they are more exposed to political attack in the form of greater regulations. Therefore, large companies have a greater incentive to disclose more information in their annual reports than small companies, to enhance their reputation and public image, and to protect themselves against public criticisms or the threat of government intervention. Total assets used as the criteria for company's size selection in each economic sector.

Company Age

Company age might have an impact on the company's attitude toward the quantity of CSR disclosures. This is based on the argument that management problems, decisions and principles are rooted in time ((Maqbool and Zameern, 2018).) Company age is depicted by the period from the inception/establishment date to the year of analysis, year 2019.

The Research Hypotheses

As mentioned earlier, the selected sample companies cover four economic sectors, and represent the different company size and age in each sector. Given the association between CSP and CFP, and the control variables that might moderate or have an impact on this association, the following hypotheses will be tested:

H1: There is a positive correlation between the CSP and CFP.

H2: The impact of CSP on CFP is stronger for large firms.

H3: The impact of CSP on CFP is stronger for old firms.

Regression Model

According to the above hypotheses and the selection of measures of dependent and independent variables, the following two models will be analyzed:

Model 1: $ROA = \beta_0 + \beta_1 CSPscore + \beta_6 Size + \beta_7 Age + \varepsilon.$ (1)

Model 2: $ROE = \beta_0 + \beta_1 CSPscore + \beta_6 Size + \beta_7 Age + \varepsilon$ (2)

where:

ROA: Return on Asset, a dependent variable, measured as Net income/Average total assets.
ROE: Return on Equity, a dependent variable, measured as Net income/Average total equity.
CSPscore: is the index for CSP, represent the explanatory variable.
Size: a control variable, measured as natural logarithm of total assets.
Age: a control variable, measured as the period from the inception/establishment date to the year of analysis, year 2018 and 2019.

THE EMPIRICAL RESULTS

Descriptive Statistics

Summery Statistics and correlations matrix for all the dependent and independent variables used in the study sample are presented in Table 1. Panel A shows the minimum, maximum, mean and the standard deviation of each variable. The mean score of CPS amounts to 43.9% with a standard deviation of 0.129. The score shows that CSP has taken roots in Kuwait but still needs to further develop before it will be recognized as a main strategic element of the business.

It is worthwhile to notice that the value of the CPS's standard deviation is less than its mean which result in a coefficient of variation smaller than 1. This reveals that the values of all observations are not

dispersed around the mean, and thus the estimation is precise and the sample companies share the same common principle of bearing their social responsibility.

TABLE 1
DESCRIPTIVE STATISTICS AND CORRELATION MATRIX FOR THE TOTAL SAMPLE

Panel A: Descriptive Statistics

Variable	N	Min.	Max.	Mean	Std. Deviation
ROA	71	-0.169	0.246	0.0254	0.052
ROE	71	-0.229	0.230	0.055	0.093
CPS	71	0.120	0.800	0.439	0.129
SIZE	71	12.7	22.555	18.878	1.824
AGE	71	13	59	35.99	14.818

Panel B: The Correlation Matrix between all Variables

	ROA	ROE	CSP	SIZE	AGE
ROA	1	0.873**	0.440**	-0.027	0.093
ROE		1	0.427**	0.138	0.279*
CPS			1	0.163	0.196
SIZE				1	0.284*
AGE					1

** Correlation is significant at the 0.01 level (2-tailed)
* Correlation is significant at the 0.05 level (2-tailed)

Panel B shows that ROA and ROE are positively correlated with CPS at a significant level of 0.01 as expected; ROA is more highly correlated with CPS than ROE; and age and size are positively correlated at a significant level less than 0.05.

The Association Between ROA and CSP
Table 2 presents the results of the regression models using data for years 2018 and 2019. It reveals that the rate of return on assets is positively and significantly associated with CSP. The coefficient of the CSP is statistically significant for each year and for the total sample, while other controlling variables are not statistically significant at any acceptable level.

The coefficients of variation (overall adjusted R^2) for year 2018, 2019, and the two years combined are 0.196, 0.256 and 0.205 respectively.

These results reveal that the rate of return on assets as a measure of financial performance is significantly associated with CSP.

The Association Between ROE and CSP
Table 3 presents the results of the regression models using rate of return on equity as a dependent variable. The results obtained are similar to the result obtained using ROA as a measure of performance, it reveals that the rate of return on equity is positively and significantly associated with CSP. The coefficient of the CSP is statistically significant for each year and for the total sample, while other controlling variables are not statistically significant at any acceptable level.

The coefficients of variation (overall adjusted R^2) for year 2018, 2019, and the two years combined are 0.188, 0.307 and 0.222 respectively.

These results reveal that the rate of return on equity as a measure of financial performance is significantly associated with CSP.

Based on the preceding discussion we can conclude that both ROA and ROE as measures of Corporate financial performance are positively and significantly associated with corporate social performance. This

result is consistent with the results obtained by several previous studies, e.g., Gamerschlag, R. et al., (2011), Kim, M and Kim, Y., (2014, Palaniappan G1, Srinivasa Rao (2016), and Hou, T. C., (2018). Regarding the control variables (company size and company age) though positively correlate with CSP, they are not statistically significant at any acceptable level.

According to this result, we can accept H1, which predicts a positive correlation between CSP and CFP as measured by ROA and/or ROE and reject H2 and H3, which predict that the impact of CSP on CFP is stronger for large firms, and/or for old firms.

TABLE 2
THE ASSOCIATION BETWEEN ROA, CSP, AGE AND SIZE

	Year 2018		Year 2019		All Years	
Variable	Coeff.	t-value (Sig. level)	Coeff.	t-value (Sig. level)	Coeff.	t-value (Sig. level)
CONSTANT	6.321	0.683 (0.500)	-3.649	-0.436 (0.665)	0.084	0.014 (0.989)
CSP	0.414	2.378 (0.02)	0.511	3.344 (0.002)	0.451	4.035 (0.00)
SIZE	-0.206	-1.144 (0.262)	-0.097	-0.622 (0.538)	-0.111	-0.972 0.335
AGE	0.090	0.482 (0.633)	0.038	0.247 (0.806)	0.036	0.315 (0.754)
	$R^2 = 0.196$		$R^2 = 0.256$		$R^2 = 0.205$	

TABLE 3
THE ASSOCIATION BETWEEN ROE, CSP, AGE AND SIZE

	Year 2018		Year 2019		All Years	
Variable	Coeff.	t-value (Sig. level)	Coeff.	t-value (Sig. level)	Coeff.	t-value (Sig. level)
CONSTANT	-6.500	-0.353 (0.726)	-17.645	-1.327 (0.194)	--12.938	-1.226 (0.225)
CSP	0.316	1.803 (0.081)	0.495	3.56 (0.002)	0.385	3.478 (0.001)
SIZE	-0,018	-0.101 (0.920)	0.004	0.026 (0.979)	0.019	0.169 (0.866)
AGE	0.218	1.163 (0.254)	0.211	1.424 (0.164)	0.198	1.738 (0.087)
	$R^2 = 0.188$		$R^2 = 0.307$		$R^2 = 0.222$	

SUMMARY AND CONCLUDING REMARKS

The potential impact of corporate social activities on corporate performance motivated academics and practitioners to investigate the association between corporate social performance (CSP) and corporate financial performance (CFP). The direction of the relationship between social and financial performance of corporations has not been the subject of a consensus among authors. Also, imperial research results fail to provide conclusive evidence regarding the nature of this relationship. Some studies found a positive relationship, others reported negative, or neutral (no) relationship.

The results of the two regression models reveal that the financial performance as measured by either ROA or ROE is positively and significantly associated with CSP, while control variables (size and age of firms) are not statistically significant at any acceptable level.

The findings of this study are expected to provide useful information for management. They are important for understanding the development and implementation of corporate social practices by Kuwaiti companies. Considering the positive impact of CSR on firm's performance, CSR should not be treated as an optional activity, rather it should be integrated with long-term company strategy, that would pave the way for a higher financial performance, and thus maximize its stockholder's wealth.

As with all empirical studies, the current study is subject to limitations, and this provides an opportunity for further research streams. First limitation is that only one country is researched, thus cultural aspects cannot be generalized. Therefore, further research may be undertaken in a cross-country context. Second limitation is that, deriving the keywords for the content analysis from the GRI guidelines is not free of risk, as the guidelines might not capture all of the relevant CSR aspects, so additional research would be undertaken using other ways of collecting data related to corporate social activities. Finally, only to control variables have been included in the analysis (company size and company age), there are other variables that might influence the financial performance that would be incorporated and examined, e.g. research and development spending, dividend policies etc.

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