

Does Ownership Concentration Moderates In Csr And Firm Performance Relationship? An Evidence From Non-Financial Sector Listed Companies Of Pakistan

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Abstract

The purpose of this study is to analyze the impact of corporate social responsibility on firm performance and to investigate the moderating role of ownership concentration in CSR-firm performance relationship. The sample of the study is all the non-financial companies listed in Pakistan stock exchange (PSX) and covers the period of 2006-2020. Data has been collected from the annual reports of companies and Balance sheet analysis (BSA) document issued by state bank of Pakistan (SBP). Corporate social responsibility is measured through CSR spending ratio, Firm Performance is measured through return on assets, Ownership concentration is measured through the percentage of shares held by the largest shareholder, Control variables of the study are Firm age, Firm size and Firm leverage. The study used Eviews software, and Generalized Methods of Moments (GMM) technique for the purpose of data analysis. Results reveals that the impact of CSR on firm performance is significant and positive. The relationship

of ownership concentration on firm performance is significant and negative. Ownership concentration negatively moderates the relationship between CSR and firm performance. These findings may help policy makers and regulators identify how concentrated ownership structure may affect CSR activities in Pakistan. Regulators may also investigate the effectiveness of CSR initiatives in firms with concentrated ownership, because investment in CSR activities from these companies could lead to worsening of financial performance.

Keywords: Corporate social responsibility, Pakistan stock exchange, non-financial listed companies, ownership concentration, return on assets, Generalized methods of moments.

Introduction

Corporate social responsibility (CSR) is among the most recent factor that caught the attention of researchers and scholars. With the increased focus of firms on acting in a socially responsible manner, the significance of studying and understanding the role and impact of CSR on a firm's performance (FP) is becoming even more relevant and significant. CSR can be defined as the activities associated with firms having a focus on social welfare returns along with economic returns (Javeed & Lefen, 2019). Investment of firms in CSR can result in the provision of an edge to the firms involved in the CSR activities enhancing their chances of long term survival (Davis, 1973).

There have been a bunch of great empirical studies on the relationship between CSR and firm performance, but the results are mixed (Al-Malkawi & Javaid, 2018). Margolis, Elfenbein, and Walsh (2009) undertake meta-analyses and discover that for the link between CSR practices and firm performance, about half of the studies found a positive effect, a quarter found no significant relationship, 5% found a negative relationship, and the rest found mixed findings. The situation hasn't altered significantly in recent years. For example, Sun (2012) and Wu (2006) provide evidence on a positive link between CSR and financial performance. On the other hand, a negative association between the two has also been frequently documented, e.g., Cavaco and Crifo (2014), Lopez, Garcia, and Rodriguez (2007).

Another meta-analysis conducted by Wang et al. (2016) shows support for a positive association between CSR and firm financial performance. However, Wang et al. (2016) note that the impact of CSR tends to be more beneficial in developed countries, i.e., the CSR-CFP link is moderated at least by some institutional factors.

According to Lambertini and Tampieri (2015) involvement in CSR can also result in higher profits as compared to the firms with no investment in CSR. In the field of CSR where numerous studies have been conducted regarding measurement and its significance, researchers are now focusing on exploring the impact of CSR and its association as a determining factor in different relationships (El-Halaby & Hussainey, 2015; Kotonen, 2009). Despite a large number of studies conducted on the association of corporate social responsibility (CSR) and firms performance (FP), the significance of corporate governance factors in this relationship still needs further exploration as the results of the studies indicates mixed and inconclusive outcomes (Peng & Yang, 2014).

Corporate Governance (CG) involves all the standards and measures which lead to creating a trustful and transparent environment. Corporate governance also involves those activities which involve solving the issues which arise in agency relations due to the divergence in the goals and interests of agents and principal also known as agency problem (Javeed & Lefen, 2019).

According to J. E. Core, Holthausen, and Larcker (1999), the degree of corporate governance is directly linked to agency problem the firm having a weaker system of CG will have a higher degree of agency conflict and vice versa. The two dimensions of corporate governance include the chief executive officer (CEO) of a company and its shareholders (Javeed & Lefen, 2019). It is inferred that separation and diversification of ownership and management lead towards deviation in managers' behavior towards the conflict of interest (Jensen, 1986) and intense monitoring of managers became vital to ensure the pursuance of shareholder's goals. The field of corporate governance focuses on this relationship between the firm's management with shareholders and aims to build a positive link between these two dimensions. In other words, CG focuses on the alignment of managers and shareholder goals.

Jensen and Meckling (1976) suggested that with an increase in the manager's share of ownership this goals of managers and the

shareholders can be aligned to eliminate agency cost but the further studies indicated that such controlling shareholders have only a small fraction of shares among the total ownership and this disparity leads towards persuasion of their private interests and goals (Kotonen, 2009). Although there are numerous studies conducted on the ownership structure as a tool for corporate governance with prime focus on large shareholders and managerial ownership (Claessens & Fan, 2002) but the latest studies further divided this agency conflict as type I and type II and most of the existing studies mostly considered type I agency conflict (Marbun, Abdul-Hamid, & Popoola, 2016). Type I agency problem arises among managers and shareholders of the firm, whereas type II agency conflict arises when the goals of controlling shareholders and minority shareholders are not aligned.

Hence based on the above discussion, this study focuses on one particular characteristic that is the ownership concentration and attempts to investigate its moderating impact on the relationship of CSR and firm's performance. Moreover, as observed in the previous literature, there is need to further investigate the ownership concentration because type-2 agency problem resulting from conflict of interest between controlling shareholders and minority shareholders, this is an important issue in emerging markets as CSR is contextual (Claessens & Fan, 2002) and it is vital to study in developing country like Pakistan as it may lead towards better understanding of CSR by its comparison with the prior studies that are mostly conducted in developed economies. Making our study, one of the few to analyze the vital corporate governance characteristic like ownership concentration as a moderator in the CSR-firm performance relationship in a developing country context.

Problem Statement

As for Pakistani firms, the relationship of CSR and firm performance has been investigated in many studies e.g., (Khan, Malik, & Saghir, 2020; Muhammad Shoukat Malik & Kanwal, 2018) this relationship is still inconclusive (Blasi, Caporin, & Fontini, 2018; Margolis et al., 2009) the reason for inconclusive findings is due to neglecting of some of the relevant mediating and moderating variables (Agyemang & Ansong, 2017). Moreover, Grewatsch and Kleindienst (2017) ask for more studies on moderators and mediators in CSR-FP link. There are very few studies analyzing the

linkages of CSR and FP with mediating (Khan & Malik, 2020; Saeidi, Sofian, Saeidi, Saeidi, & Saaeidi, 2015) and moderating variables (Anser, Zhang, & Kanwal, 2018; Bai & Chang, 2015; Ho, Lu, & Lucianetti, 2021). The role of corporate governance characteristics for CSR initiatives has received little attention specially in emerging economies like Pakistan (Akben-Selcuk, 2019). Based on above arguments, this is first attempt as per author's knowledge to analyze the moderating role of ownership concentration in the CSR-FP link in emerging economy i.e. Pakistan.

Literature Review

Literature on the relationship of CSR-firm performance reports inconclusive results (Margolis et al., 2009). In general, positive association of CSR and firm performance is dominant in developed economies.

Stakeholder theory (Freeman, 1984) states that different categories of stakeholders, such as customers, investors, employees, and suppliers, have varied positions and bargaining power depending on their control of resources that affect business policies. Firms can reduce the danger of stakeholders withdrawing resources, risking the firm's survival and operations, by responding to stakeholder expectations (H. Wang, Tong, Takeuchi, & George, 2016). Furthermore, effective CSR initiatives help to develop and maintain a positive corporate reputation, which benefits a variety of stakeholders (Franco, Caroli, Cappa, & Del Chiappa, 2020). This influence will assist investors to take more positive decisions about the firm's stocks (Flammer, 2015)

There are number of studies in the literature investigating the moderation of corporate governance variables in the CSR-firm performance relationship using different proxies. For example F. Li, Li, and Minor (2016) reported that Chief Executive Officer (CEO) power is positively related to CSR and investing in CSR related activities are value enhancing. Giroud and Mueller (2011) showed that if the governance structure of companies is weak then equity returns and operating performance of these companies will also be lesser, this is applicable in companies with less competition. Z. F. Li (2014) measured corporate governance through mutual monitoring and finds that mutual monitoring done by the second executive of a company is positively link to firm performance measured by Tobin's Q. Coles, Li, and Wang (2018) focused CEOs

tournament incentives measured through compensation gap between CEOs of one firm with highest paid CEOs between similar industry. J. Core and Guay (1999) used compensation incentives to measure corporate governance.

Ownership structure is also used in the literature to measure corporate governance. Jensen and Meckling (1976) reported that agency theory provides a theoretical basis to explain the effect of ownership concentration in the CSR-firm performance link. The agency theory proposes that, in widely held corporations the shareholders and managers have a divergent of interest, which can reduce value of the firm due to managers making decisions for their own benefit rather maximize firm value. CSR can be considered as principal-agent problem, to improve company reputation as a good social citizen managers overinvest in CSR (Harjoto & Jo, 2011). The confidence of managers may be boosted as a result of this reputation, and sometimes overconfident CEOs made value-destroying decisions or overinvest (Malmendier & Tate, 2005).

However, in emerging countries like Pakistan, the fundamental agency issue is not a conflict of interest between managers and owners, but the expropriation of minority shareholders by dominating shareholders (Claessens & Fan, 2002). The most popular organization style is family-owned and controlled businesses, which are characterized by low free-float ratios in order to retain the control of the family, who is usually the largest shareholder (OECD, 2013). Weak legal environment is also a reason of high ownership concentration (La Porta, Lopez-de-Silanes, & Shleifer, 1999). When analyzing the relationship between CSR and firm financial performance in such a corporate environment, it is critical to evaluate the influence of ownership concentration.

The decisions related to CSR activities are affected from the incentives provided to the controlling shareholders related to the information of corporate policies which leads to asymmetry of information (Peng & Yang, 2014). Information asymmetry induce managers to hide the true picture and motivations regarding investments in CSR related activities (McWilliams, Siegel, & Wright, 2006). In the situation of high ownership concentration, the decisions of managers regarding CSR investments are more likely to undertake in best interest of managers not for the benefit of

firm, which ultimately leads to deteriorating of financial performance.

Research Methodology

Sample and Data

The population of the study consists of all the companies listed in Pakistan stock exchange (PSX). The sample of the study is all the non-financial listed companies. Financial firm are excluded from the sample because of unique structure. Companies with missing values are removed from the sample. The period of the study consists of 2006 to 2020. The final sample of the study consists of 196 companies with unbalanced panel of 1960 observations. Data has been collected from annual reports of companies downloaded from websites and balance sheet analysis document issued by state bank of Pakistan.

Variables

Corporate Social Responsibility (CSR)

Researchers used different proxies to measure CSR. The use of social ratings is extensively used to measure CSR. Kinder, Lydenberg, Domini (KLD) index is also one of the frequently used technique in the literature (Gao & Zhang, 2015). Fortune magazine reputational index is also used to measure the CSR (Basdeo, Smith, Grimm, Rindova, & Derfus, 2006). Disclosure approach is another approach that is also utilized to measure CSR (Kennedy Nyahunzvi, 2013). In Existing literature, questionnaire surveys is also employed to measure CSR. Rettab, Brik, and Mellahi (2009) used questionnaire to examine the link of CSR and FP. The current study used CSR monetary spending ratio to measure CSR. The spending of the firm in donations, employee's welfare and research and development are calculated. The calculation of total CSR expenditures can be performed from the amounts spent on these three dimensions. In addition, the proportion of financial spending amounts by dividing the total expenditure of them the earnings after tax (Ehsan et al., 2018; Lin, Yang, & Liou, 2009; Pyo & Lee, 2013).

Financial Performance (FP)

There are multiple proxies developed by researchers to measure the FP variable, including ROA, EPS, ROI (Epstein & Buhovac, 2014).

McWilliams and Siegel (2000) suggested that accounting-based measures presents the manager's performance and internal process of decision making. There is no agreement on how to estimate FP variable (Maqbool & Zameer, 2018). Researchers utilizes proxies of their own choice and of requirement of their study. Moreover, Moore (2001) documented that market based measures are less suitable for estimation of FP compare to accounting based measures. In addition, (De Massis, Kotlar, Campopiano, & Cassia, 2015) employed ROA and ROE to calculate FP. To measure for CSR activities ROA and ROE are best performance measures (Shen, Wu, Chen, & Fang, 2016). Moreover, financial performance of corporations using secondary data is also tested using measure of ROA and ROE (Mahoney & Roberts, 2007). Furthermore, M Shoukat Malik and Nadeem (2014) measures the firm performance of corporations using ROA, ROE, EPS and Net Profit. The current study measures FP using ROA as suggested by review of literature and relevant studies.

Firm Size

Previous studies suggested that there is an impact of firm size on firm value. In comparison to smaller businesses, larger businesses are better equipped to handle risk, which helps larger companies to manage and avoid those threats (Udayasankar, 2008). Larger companies may have strong motive to engage in CSR related activities. They may also be able to better handle the complex and diversified operations (Issa, 2017). Firm size is considered as one of the important control variable used in the CSR research (Benitez, Ruiz, Castillo, & Llorens, 2020; Yoo, Choi, & Chon, 2019).

Firm Age

Previous studies suggested that older firms perform better as compare to younger firm because of lack of experience and external connections (D'Amato & Falivena, 2020; Withisuphakorn & Jiraporn, 2016). This study used firm age as control variable, which is measured through age of the firm in years. This is in line with previous research (Hou, 2019; Samet & Jarboui, 2017).

Firm leverage

The study also used Firm leverage control variable, which is calculated by ratio of total liabilities to total assets. This is

consistent with earlier studies (J.-Y. Wang, Wang, & Liao, 2019; Yoo et al., 2019).

Ownership Concentration (OC)

To investigate a potential moderating impact of ownership concentration, the ownership concentration (OWN) variable, which is the percentage of shares held by the largest shareholder, was used.

Table 1. Operationalization of variables

Variable	Measurement	Reference
CSR	CSR monetary spending ratio	Ehsan et al. (2018)
Firm Performance	ROA=Net profit after tax/total assets	(Shen et al., 2016)
Ownership Concentration	percentage of shares held by the largest shareholder, was used.	(Akben-Selcuk, 2019)
Firm size	Log of total assets	Yang and Baasandorj (2017), (Boubaker, Cellier, Manita, & Saeed, 2020)
Firm Age	Age of the firm in years	
Firm Leverage	Total liabilities/ Total assets	

Model

To test the hypotheses of this study, the following model was used.

$$ROA_{i,t} = \beta_0 + \beta_1 CSR_{i,t} + \beta_2 OC_{i,t} + \beta_3 CSR_{i,t} \times OC_{i,t} + \beta_4 SIZE_{i,t} + \beta_5 AGE_{i,t} + \beta_6 LEV_{i,t} + \epsilon_{i,t}$$

Where ROA_{i,t} return on assets is a dependent variable, CSR_{i,t} Corporate social responsibility is the independent variable, OC_{i,t} Ownership Concentration is moderating variable, SIZE_{i,t}, AGE_{i,t}, LEV_{i,t} are control variables of the study. β₀, β₁, β₂, β₃, β₄, β₅, β₆ are population parameters to be estimated, and ε_{i,t} it is the error term.

Results and Discussions

Descriptive Statistics

Table 1 presents descriptive statistics using all variables. These statistics are estimated to see any possible discrepancy and to get a general understanding of the data. Results reveal that all the values are within acceptable limits, and no discrepancy is found in the data. For ROA the mean is 0.0569, median is 0.0496, Maximum value is 0.3516 whereas minimum value is -0.4984 and standard deviation (SD) is 0.0816. The mean value is CSR 0.0160, the median value is 0.0045, the maximum value is 0.5286 whereas minimum value is -0.3786 and standard deviation is 0.0565. The mean value of ownership concentration is 0.6228, the median value is 0.6424, the maximum value is 0.9995 whereas the minimum value is 0.0044 and the value of standard deviation is 0.1992. The mean value of SIZE is 15.673, the median value is 15.442, the maximum values is 20.022 whereas minimum value is 12.165 and the standard deviation is 1.4978. The mean value of AGE is 3.451, the median value is 3.434, the maximum value is 5.043 whereas the minimum value is 1.098 and the standard deviation is 0.518. The mean value of leverage is 0.166, the median value is 0.141, the maximum value is 0.709 whereas the minimum value is 0.000 and the standard deviation is 0.136.

Table 2: Descriptive statistics

	Mean	Median	Max	Min	Std. Dev.
ROA	0.056	0.049	0.351	-0.498	0.081
CSR	0.016	0.004	0.528	-0.378	0.056
OC	0.622	0.642	0.999	0.004	0.199
SIZE	15.673	15.442	20.022	12.165	1.497
AGE	3.451	3.434	5.043	1.098	0.518
LEV	0.166	0.141	0.709	0.000	0.136

Correlation Matrix

Table 3 presents the results of correlation analysis. This association of variables can be either positive, negative, or zero. Correlation analysis discloses that data is free of multicollinearity problems among the variables used.

Table 3: Correlation coefficients

	CSR	ROA	OC	SIZE	AGE	LEV
CSR	1					

ROA	0.043	1				
OC	-0.022	0.064	1			
SIZE	0.019	0.067	0.096	1		
AGE	0.039	0.044	0.101	0.041	1	
LEV	-0.029	-0.330	-0.034	0.097	-0.225	1

Regression Results

Table 4 contains the results of generalized methods of moments. The impact of CSR on firm performance is significant and positive, meaning that engagement in CSR related activities leads to better firm performance. The relationship of ownership concentration on firm performance is also significant and negative. The result of interaction term is also significant and negative meaning that ownership concentration negatively moderates the relationship between CSR and firm performance, which shows that firms with higher level of ownership concentration, CSR investment is negatively related to firm performance. The impact of firm size on firm performance is also significant and positive, meaning that with the increase in size of the firm its financial performance will also increase. The impact of firm age on firm performance is insignificant and positive. The impact of leverage on firm performance is significant and negative meaning that if a company using more debt financing its financial performance in term of return on assets will be reduced.

Table 4: Regression Results

Impact of CSR of firm performance, moderating role of OC

ROA	Coefficient	Standard Error	t-value	p-value
CSR	0.011	0.004	2.382	0.018
OC	-0.341	0.078	-4.353	0.000
CSRXOC	-0.333	0.136	-2.438	0.015
SIZE	0.010	0.002	4.912	0.000
AGE	0.003	0.006	0.483	0.629
LEV	-0.210	0.023	-8.899	0.000
Adj. R2	0.354			
J-Stat	2.686			
Prob. J-Stat	0.101			

The table reports the result of the generalized method of moment (GMM) technique. It includes coefficients, standard Error, t-statistic, and Probability stats. The table also reports Adj. R², J-Stat, and Prob. of J-Stat. The dependent variable of the study is firm performance which is measured through ROA, the independent variable of the study is corporate social responsibility, and the moderating variable of the study is ownership concentration. The study also used firm size, firm age and leverage as control variables of the study.

Source: Author's calculations

Conclusion

This topic requires more study focus because there aren't many studies that look at moderators and/or mediators for the association between CSR and financial performance (Grewatsch & Kleindienst, 2017). Particularly in the context of developing nations, the influence of corporate governance variables on the link between CSR and financial performance is limited. The goal of this study is to fill these gaps in the literature by analyzing data from non-financial listed firms on the PSX for the years 2010 to 2019 to examine the link between CSR, ownership concentration, and firm financial performance in Pakistan, a developing country.

The findings of this study reveal that the firm investing in CSR related projects displays a better firm performance as compare to non-CSR firm. These findings are consistent with stakeholder theory, suggest that despite the extra cost associated with CSR activities, firm benefit from CSR through better and improved relationships with its stakeholders. The results are consistent with the previous studies (Khan et al., 2020; Peng & Yang, 2014). Another finding emerged from the out study is the role of ownership concentration in CSR-firm performance relationship. Results reveals that ownership concentration negatively moderated the relationship of CSR and firm performance. Which indicates that engagement in CSR related activities will be helpful in dispersed ownership structure. However, increase in ownership concentration the strength of the relationship weakens or may even turn negative. Thesis results are also consistent with previous studies (Akben-Selcuk, 2019; Peng & Yang, 2014; Ting & Yin, 2018).

This study has several implications. First, positive association of CSR and firm performance shows that non-financial companies of Pakistan should emphasis on CSR activities. Second, the negative moderation of ownership concentration in the relationship of CSR and firm performance suggest that establishment of good control mechanism is necessary to protect the rights of minority shareholders in firms with concentrated ownership, because overinvestment in these firm in CSR related activities leading to worsening financial performance (Akben-Selcuk, 2019).

Furthermore, these findings may help policy makers and regulators identify how concentrated ownership structure may affect CSR activities in Pakistan. Regulators may also investigate the effectiveness of CSR initiatives in firms with concentrated ownership, because investment in CSR activities from these companies could lead to worsening of financial performance.

The study has some limitations, First, the study employs data from single developing country, Pakistan, to explore the moderating role of ownership concentration in CSR and firm performance relationship. Thus, the results might not be generalizable to other developing countries. The study used non-financial listed companies of Pakistan stock exchange for data analysis. Future researchers might address these limitations by using financial sector companies for analysis. Future research can also be conducted on some other developing countries for the generalizability of the results. Moreover, the moderating role of some of the other corporate governance characteristics, such as CEO duality, board characteristics, family ownership or executive compensation (Hong, Li, & Minor, 2016), could constitute some fruitful avenue for future research.

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