Corporate Social Responsibility (CSR): Impact on Equity Returns

Amit Patel
Registrar,
Ganpat University,
Mehsana, Gujarat, India
Email: registrar@ganpatuniversity.ac.in

Aashal Bhatt
Assistant Professor,
FOC (SMPIC) GLS University,
Ahmedabad, Gujarat, India
Email: aashal.bhatt@glsuniversity.ac.in

Dharmesh Gadhvi
Assistant Professor,
V M Patel College of Management Studies
Ganpat University,
Mehsana, Gujarat, India
Email:dharmesh.gadhvi@ganpatuniversity.ac.in

Abstract

In recent time, Corporate Social Responsibility (CSR) has become mandatory for many listed companies. However, it always remains a debatable issue that CSR should be mandatory or it should come from company's own wish. Corporate always thrust for the wealth maximization of their shareholder's wealth and hence expense behind CSR may result into company value decline.

On the contrary, it may give a positive impression of the company in the market and help in increasing their sales and profits. Thus, there is also a possibility that CSR actually results into shareholder's wealth creation. Here, in current study authors have tried to identify this impact of CSR on equity returns.

For the same 30 companies score for 96 CSR items was calculated and the average score was regressed with companies' equity returns for the last four years.

Key Words

CSR, Equity Returns, Wealth Maximization.

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Introduction

A core component of Corporate Strategy, in today's global economy, is Corporate Social Responsibility. The corporate social disclosure practices followed by a company are expected to increase profitability, as the societal pressures will encourage more financial transactions. Similar to the role of a citizen, an enterprise is also considered as an esteemed citizen who is judged by its actions in relation to the community of which it is a member, as well as by its economic performance.

The connecting link between good corporate citizenship and increased shareholder value has been facilitated as a result of the length of time the information has been available, the intensity of the information and the ability to conduct research not only with voluntary disclosures but also with mandatory disclosures. (Griffin, 2013)

In Accounting Literature, CSR is developed within the concept of The Triple Bottom Line referring to the financial performance of a firm by considering several aspects like profit, ROA, ROE, and EVA. (Fauzi, 2010). Extant literature is available on CSR Disclosure practices with reference to Stakeholders perspective i.e. how disclosure practices affect Employees, Customers and Corporate Reputation at large.

In parity with Abraham Maslow's Theory, which talks about basic needs first, and self-esteem at the end, it is the need of the day to keep shareholder's wealth as a priority and then to follow the stages of Carroll's Pyramid which talks about slowly and gradually following the hierarchy and reach to the top and work for Corporate Philanthropy.

However there is an argument that the potential influence of activist shareholder is higher even though they are small in number, because their voice has a significant potential to influence the opinions of other large shareholders and moreover corporate managers could consider the most audible group of shareholders in order to avoid losing legitimacy in the eyes of majority shareholders. (Prado-Lorenzo, 2012)

Instead of taking a very broad picture of taking into consideration i.e. corporate philanthropy on a priority basis, this paper makes a moderate attempt to study the impact of CSR disclosure practices on maximizing shareholder's wealth, which is at the base.

Literature Review

In addition, (Dewi, 2015) categorized financial information as good news and bad news. If the available information is a good news related to the stock issue, the market will react positively and firm's abnormal return will be higher than expected and vice-versa.

An information which attracts investors should be related to profit and stock valuation (price) since these two matters indicate a firm's performance CSRD significantly influences a firm's financial performance and value. It proves that CSRD also affects the company's image. Further company's image affects company's sales rate. As investors

positively appreciate the firm performance, it will enhance the value of the firm’s stock. (Bidhari, 2013).
On the contrary, other findings explain that the disclosure of CSR activities does not have a significant role in the firm’s financial performance. Investors also make cautious investment decisions. Both Shareholder and Stakeholder theories are normative theories of CSR dictating what a corporation’s role ought to be. According to Stakeholder theory, managers are agents of stakeholders who must ensure that the ethical rights of stakeholders are not violated and their legitimate interests are balanced while making decisions.

On the other hand, shareholder theory asserts that shareholders give capital to a company’s managers who are expected to spend corporate funds only in ways which have been authorized by the shareholders. According to Milton Friedman, “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 engages in open and free competition, without deception or fraud." (Kaushik, 2017)
However, the company should not deviate with the basic and the primary responsibility popularly called Economic Responsibility towards its shareholders. A business must be profitable to remain economically responsible to remain in business. In this way, business gives back to society by providing jobs to employees and producing goods and services to consumers.

The goal of the company at this level of the CSR Pyramid is to maximise profits for shareholders and owners. Managers, as agents of the company owners, are obliged to maximise shareholders wealth.
Although the two concepts of Shareholder theory and Stakeholder theory are clear by their definitions, shareholder theory is often misrepresented as urging companies to do anything to make profits. This is not true to the extent that this theory actually requires managers to increase profits only through legal, non-deceptive means. While Stakeholder theory is sometimes to be claimed to be not focusing on company’s profitability. Again this does not stand true as this theory ultimately aims for company’s continued existence and profitability and it must be achieved by balancing the interests of all stakeholders.

Research Methodology

Objective

To understand the impact of CSR activity on equity returns.

Content Analysis:

Using annual reports of 30 companies for the last four year, 96 different scores were calculated for the average CSR score of companies. For the matching year, adjusted equity returns were calculated and regression analysis was performed to check the impact of CSR on equity returns.

Hypothesis

Base on objective following hypothesis was developed:

H_0: There isn't any significant impact of CSR score on the equity returns of the company

Data Analysis and Interpretation

As discussed in the previous section, regression analysis was performed to check the impact of average CSR on equity returns of the company.

Table 1: Model Fit for CSR on Equity Returns

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	2273.172	1	2273.172	2.751	.100[a]
	Residual	97519.516	118	826.437		
	Total	99792.688	119			
a. Significant at 10 percent Predictors: (Constant), CSRAVG						
b. Dependent Variable: Returns						

As shown in table 1, the model was significant at the 10 percent significant level. Thus, the null hypothesis was rejected and there is a significant impact of CSR on equity returns for the company. However as shown in table 2, only 2.3 percent of the variation in equity returns was explained by variation in CSR and remaining variation wasn't predictable using CSR score.

Table2: Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.151[a]	.023	.014	28.7478099
a. Predictors: (Constant), CSRAVG				

With the result of co-efficient summary following equation was shown with the significant impact of CSRAVG (Average CSR) score on equity Returns for the companies.

Returns = 32.36 – 9.185 * CSRAVG

This result confirms the negative impact of CSR score on the company's equity returns. Thus, voluntary CSR may be difficult to achieve in Indian context.

Conclusion

This study shows an increase in CSR reporting score by on an average one unit will result in to on an average 9.185 percent decline into the stock price of the company. Hence, there is trade-off between getting good CSR score versus achieving shareholder's wealth. This conflict leads to avoidance of CSR activity by most of the corporate houses and thus it is a good step taken by the government to make it mandatory for the overall benefit of society.

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