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Corporate Social Responsibility and Cash Value Creation by Emphasizing the Moderating Role of Business Strategy[1]

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Research Paper

Introduction

In recent years, companies' traditional goals of maximizing stock value have been increasingly challenged by changing the concept of value and corporate social responsibility has become a major activity in the business world. This concept is defined as corporate commitments to maximize long-term economic, social and environmental well-being through firm performance, policies and resources. In fact, it is argued that the growth of companies in today's competitive business environment depends on the effective management of social responsibilities, which, while creating social and economic values, promotes the sustainable development of society. Corporate social responsibility is a multifaceted concept that reflects a company's response to the expectations and demands of a wide range of stakeholders. The purpose of corporate social responsibility is to encourage organizations to consider the interests of society, with responsibility for the impact of their activities on customers, employees, shareholders, communities and the environment. Social responsibility initiatives are increasingly important as a key element of business strategies, with the aim of protecting and consolidating the company's position among stakeholders, for long-term progressing. Research has shown that performance and value of companies, are influenced by corporate social responsibility. Due to the effect of different factors on the

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relationship between corporate social responsibility and firms value, in various studies, the moderating role of different variables in this relationship has been investigated. One of the effective variables, is business strategy because, it represents a unique and fundamental element of a company's identity. Thus, business strategy can potentially affect the relationship between corporate social responsibility, its dimensions and companies' value creation.

Methodology

In terms of purpose, the present study is an applied type, from the point of view of data collection, it is a descriptive, and, in terms of nature, it is post-event approach. It is quantitative research, because accounting and capital market information is used for calculating variables. The data related to 104 companies listed in the Tehran Stock Exchange during 2011-2019 has been analyzed. The information of 5 years is required to calculate some variables, therefore, the data required by the sample companies should be available for a period of 13 years (2007-2019). To test the research hypotheses, the multivariate linear regression model and panel data method were used as well. A combined index based on accounting variables and average decimal ranking method, is used to determine the value of the economic (return on assets, return on equity, earnings per share, tobin's Q), ethical (fairness, quality of independent auditor's opinion, discretionary accruals, accruals quality, information asymmetry), and legal (tax avoid, percentage of outside directors, disclosure quality, employers' insurance contribution, related party transactions) dimensions of corporate social responsibility. Also, by using this method, all the variables that constitute the economic, ethical and legal dimensions of corporate social responsibility are considered to determine the value of corporate social responsibility. To measure the companies' cash value creation, the indicator of cash value added has been used. The theoretical business strategy framework of Miles and Snow (1978, 2003), which classifies business strategies into three categories; prospectors, analyzers, defenders, based on composite measure to proxy for a firm’s business strategy, have been used. This composite measure strategy is constructed from the following six firm attributes: ratio of R&D expenses to sales, ratio of employees to sales, one-year percentage change in total sales, ratio of SG&A expenses to sales, standard deviation of total number of employees, and net property, plant, and equipment scaled by total assets. The ratio of R&D expenses to sales is a proxy for a firm’s propensity to search for new products, and the ratio of SG&A expenses to sales serves as a measure of a firm’s focus on marketing and sales. The ratio of employees to sales reflects a firm’s capability to produce and distribute products and services efficiently. Net PPE scaled by total assets captures a firm’s emphasis on production assets. One-year percentage change in total sales measures a firm’s historical growth or investment opportunities.

The standard deviation of total number of employees reflects a firm’s organizational stability. The average annual ratios over the past 5 years have been calculated for six variables. Then, each of the six variables rank into quintiles. For the first five variables except for net PPE scaled by total assets, have been assign a score of 5 to observations in the highest quintile, a score of 4 to the second quintile, and so on. Since prospectors exhibit lower capital intensity, the ratio of net PPE to total assets is reverse-scored and the observations in the highest (lowest) quintile are given a score of 1. Finally, for each firm-year, the sum scores of the six variables to generate strategy measure is used. This composite measure receives a maximum score of 30 and a minimum score of 6. Higher strategy score represents a firm pursuing a prospector strategy, and lower strategy score represents a firm following a defender strategy. In addition, the exact definitions of strategy -type is: defenders (6–12), analyzers (13–23), and prospectors (24–30). The effect of strategy has been investigated in two ways; strategy and of strategy -type.

Results and Discussion

The first hypothesis investigate the effect of corporate social responsibility on the companies' cash value creation. The second to fourth hypotheses investigate the effect of economic, ethical and legal dimensions of corporate social responsibility on the cash value creation. The positive coefficient of variables indicates that increasing the corporate social responsibility and the economic, ethical, legal dimensions of corporate social responsibility increases the companies’ cash value creation and the hypotheses are confirmed. The Fifth hypothesis investigate the moderating effect of business strategy on the relationship between corporate social responsibility and companies' cash value creation. The sixth to eighth hypotheses investigate the moderating effect of business strategy on the relationship between economic, ethical and legal dimensions of corporate social responsibility and cash value creation. The moderating effect of the business strategy has been studied in two ways, of strategy and strategy -type. In both methods, the moderator role of the strategy on the relationship between corporate social responsibility's dimensions, corporate social responsibility and cash value creation is positive and significant, and the hypotheses are confirmed. The results indicate that, regardless of the method of strategy calculation; strategy and strategy -type, aggressive strategy has a greater impact on the relationship between corporate social responsibility's dimensions, corporate social responsibility and companies' cash value creation.

Conclusion

Based on the statistical results, the positive effect of corporate social responsibility and its dimensions (economic, ethical, legal) on companies' cash value creation is confirmed. The results are accordance with instrumental theory which the purpose of corporate social responsibility is earning profit and acquisition economic benefits for creating the wealth of shareholders. Stakeholder and legitimacy theories support

the research findings, too. According to the stakeholder theory, the value of the firm is increased by respecting the rights of all stakeholder groups. Therefore, paying attention to the various demands of stakeholders by the management, will lead to the survival of the organization. Respecting the society's norms and the observance of laws and regulations to confirm the legitimacy by the government and general public, would lead the company to achieve its goals. Firms following a prospector’s strategy, compete each other in producing the products and finding new markets. They are always looking for innovation in product and market development. On the other hand, firm following a defender strategy, focus on a limited product market and their efforts are to increase production efficiency. Taken together, results suggest that business strategy is an important determinant of corporate social responsibility performance. The performance of defenders is similar to the strategy of cost leadership, and the performance of prospectors is similar to the strategy of differentiation. Hence, prospectors take advantage of corporate social responsibility, as their innovation-oriented strategy and, enjoy the corporate social responsibility's benefits more than any other companies. Differentiation strategy, through the creation of brand name and increasing credit and reputation of a company, creates competitive advantage. Hence, integrating corporate social responsibility and business strategies is more productive and constructive when combined with aggressive and growth strategies. In general, the presented results show that companies can gain a competitive advantage and ensure their sustainability by adhering to social commitments in accordance with resource-based and stakeholders’ theories. But choosing the appropriate business strategy matches with the conditions of industry and company, by management, is the key for the more success in this direction. Different industries have different conditions. In monopoly markets, there is no significant competition between companies that operating in the industry. The conscious choice of business strategies by management is very important for the companies' wich operating in the competitive market. In these markets, different groups of customers have different demands and desires. So, the stability and survival of the companies, depends on being able to meet the needs of different customer’s groups. The important point for the managers is that the benefits of adhering to social commitments, such as gaining economic interests, increasing the credibility and the creating innovation in the products and services, is a long - term process that managers must consider in the planning.

Keyword: Business Strategy, Corporate Social Responsibility, Value Creation.

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