EFFECT OF CORPORATE SOCIAL RESPONSIBILITY ON THE FINANCIAL PERFORMANCE OF LARGE MANUFACTURING COMPANIES IN KENYA

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DECLARATION

This research project is my original work and has not been submitted for examination in any other university

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This research project has been submitted for examination with my approval as the University Supervisor.

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DEDICATION

I dedicate this research project to all who have directly and indirectly contributed to my academic journey.

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Am thankful to the Lord Almighty for granting me health and mental capability to complete my course work and undertake this research paper

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ABSTRACT

A firm exists to pursue the interest of stakeholders. Society is a key stakeholder for any firm, and hence, its interests, needs, and viewpoints must be considered. The role of CSR, therefore, is to attain profitability in a manner that uplifts and protects societies as well as conserving the environment. The purpose of the research was to examine the effect of corporate social responsibility on the financial performance of large manufacturing companies in Kenya. The research had ROA as the dependent variable and CSR, efficiency and capital intensity as the independent variables. The study used a descriptive and a cross-sectional study design and targeted large manufacturing companies operating in Kenya. The research used secondary data. Descriptive statistics and inferential statistics were the mode of statistics. The results showed that an insignificant positive relationship between ROA and CSR whereas there is an insignificant positive relationship ROA and efficiency. The findings also found out that capital intensity had an insignificant negative relationship with ROA

CHAPTER ONE

INTRODUCTION

1.1 Background of the Study

The concept of corporate social responsibility (CSR) has attracted interest from scholars and practitioners for close to a century. In the early 1920s, scholars advocated for companies to adopt CSR as a basis of improving performance. The great depression and the Second World War dealt a blow to CSR as companies struggled with reduced revenues and major costs cuts. It was not until the early 1950s that business firms begun to embrace CSR. According to Bowen (1953), CSR refers to the policies, decisions, and lines of actions that a business entity embraces to create value for society (Bowen, 1953). Davis (1960) opined that CSR is a business entity decisions and actions geared towards an objective partially beyond its direct economic and technical interest (Davis, 1960).

Benabou and Tirole (2010) argue that the concept of CSR emanates from the stakeholder view of a firm (Benabou & Tirole, 2010). A firm exists to pursue the interest of stakeholders. Society is a key stakeholder for any firm, and hence, its interests, needs, and viewpoints must be considered. Given that owners of a firm designate their power to management teams, the latter have a responsibility of managing relations with all stakeholders. Sundaram and Inkpe (2004) argued that it was unrealistic to expect managers to ponder and factor the interests and concerns of all stakeholders in the firms they manage (Sundaram & Inkpen, 2004). Brickley, Smith and Zimmerman (2002), however, argue that creating wealth for the shareholders involves allocating resources to all processes and activities that affect value creation in a firm. CSR adds value to an organization and should, therefore, be pursued to the point where costs related to CSR do not exceed benefits gained (Brickley, Smith, & Zimmerman, 2002).

Research on CSR majorly focuses on its direct and indirect benefits to a business entity. According to McGuire, Schneeweis, and Naroff (1988) Milton Friedman was one of the early scholars against the concept of CSR arguing it goes against the core reason of profit making. Mcguire, Schneeweis, and Naroff (1988) argued that

investing in CSR positively impacted on its reputation (McGuire, Schneeweis, & Naroff, 1988). Kallio and Nordberg (2006) poised that the concept of CSR was not only naïve but a distraction to the profit making objective of any business firm (Kallio & Nordberg, 2006). Empirical studies on CSR reveal that it enhances corporate image and boosts revenues and profitability in the long run (Ponnu & Okoth, 2009). Caroll and Shabana (2011) found out that embracing CSR enabled firms to gain reputational capital and acceptance by the society (Carroll & Shabana, 2011).

The studies on the positive impact of CSR on firm's brand and long term performance has resulted to an increase in business entities embracing the practice. The current global business environment is characterized by informed stakeholders with ease of access to information relating business entities. Maintaining a reputation of ethics and CSR endears a firm to its customers leading to better financial performance. Investors are increasingly pressuring management teams to disclose their CSR activities in their financial reports (Hooghiemstra, 2000). Some business entities have also opted to include CSR in their firm strategy. Orliziky, Schmidt, and Rynes (2003) argue that incorporating CSR in the overall firm strategy ensures better alignment with an organization's processes leading to improved performance (Orlitzky, Schmidt, & Rynes, 2003).

In order to empirically test and define the association between corporate social responsibility and financial performance of large manufacturing firms in Kenya, a conceptual framework was adopted. The framework was premised on the reviewed literature on CSR. The predictor variable was the CSR expenditure while the single outcome variable is the firm performance of large manufacturing firms.

1.1.1 Corporate Social Responsibility

Hopkins (2004) defines CSR as a process of handling the interests of stakeholders in a business entity in acceptable manner as defined by a civilized society. The aim of CSR, according to Hopkins (2004) is to improve the quality of life for members of society and at the same time increasing a firm's profitability (Hopkins, 2004). Buchholz (1991) opined that CSR is a management technique that creates a balance among a firm's commercial, communal and ecological responsibilities with a view of meeting stakeholder expectations (Buchholz, 1991). Tan-Mullins (2014) argued that

firms which adopted CSR sought to not only attain but surpass the expectations of their stakeholders. In defining CSR, Tan-Mullins (2014) posits that business entities should not only focus on maximizing their profits but should contribute to the welfare of societies as well as protect the environment in which they operate (Tan-Mullins, 2014).

The role of CSR, therefore, is to attain profitability in a manner that uplifts and protects societies as well as conserving the environment. By embracing CSR on a strategic level, firms not only avoid unnecessary and costly fines but enhance their image and perception among stakeholders. Unlike corporate social performance that is practicable and measurable, CSR is difficult to quantify and measure. Abbott and Monsen (1979) recommended three broad measurement models of CSR. The three models are content analysis, social accounting, and reputation index (Abbott & Monsen, 1979). Cochran and Woods (1984) suggested reputational index and content analysis as additional models to measure CSR. The content analysis model measures CSR by evaluating the quantitative and qualitative CSR practices. Reputational index measures CSR by rating and ranking business entities based on an objective analysis of their social performance (Cochran & Wood, 1984).

1.1.2 Financial Performance

Organizational performance in general is a key metric in evaluating the progress of an organization in achieving its desired vision. Kaplan and Norton (1992) define performance as an indicator on the utilization of a firm's assets and resources to achieve envisioned objectives in an efficient and effective manner. Stakeholders ascertain performance as positive if it meets or exceeds their expectations (Kaplan & Norton, 1992). Financial performance is one of the subset of organization performance that ascertains the progress of achieving a firm's financial objectives. Scholes and Johnson (2002) observed that decision making by stakeholders is informed by both financial and nonfinancial performance (Scholes & Johnson, 2002). Richard, Devinney, Yip, and Johnson (2009) further points out that determining performance is a critical management function as it attracts external competencies for an organization with desirable attributes (Richard, Devinney, Yip, & Johnson, 2009). Combining both internal and external capabilities and competencies enable firms to distinguish themselves in the market. Richard et.al (2009) also advocated for the use

of a combined model which includes both financial and on financial indicators to assess organizational performance.

Murerwa (2015) defined financial performance as a biased measurement of how management employs assigned primary to generate a firm's revenues over a period of time. By determining the financial performance of an organization, stakeholders make informed decisions on its financial health (Murerwa, 2015). Lebans and Euske (2006) argued that financial performance is a key measure of success in all business entities. Investors rely on financial performance information to ascertain an organization's overall financial health over a period time (Lebans & Euske, 2006). Financial performance information also allows for comparison of firms in similar industries or comparison of industries. The process of assessing financial performance is always on going and relies on financial statements which are organized and prepared in logical and consistent manner as outlined by accounting regulations and procedures.

The main financial statements used to assess performance include; statement of cash flow, statement of financial position and income statement. The notes to financial statements are also a critical part of the information contained in the financial reports. Lebans and Euske (2006) revealed that information relayed by financial statements does not fully reveal the financial operations of a firm. Relying on financial statements, however, offered users an opportunity to determine a firm's profitability and its financial stability in the long run and short run (Striteska & Spickova, 2012). According to Murerwa (2015) the process of analysing financial statements entails examining four perspectives which include; financial structure analysis, working capital analysis, profitability, and activity analysis.

1.1.3 Linking CSR and Financial Performance

Brammer and Millington (2006) observed that embracing CSR created direct financial benefits to organizations owing to improved brand reputation which improved their sales. Hooghimestra (2000) argued that embracing CSR could increase the ability of an entity to attract capital owing to its reputation. In making investment decisions, some investors evaluate a firm's reputation in CSR. Such investors will withhold investments for firms that fail to give back or pollute the environment despite the

attractiveness of the opportunity. However, socially responsible investors will be willing to fund firms that embrace CSR despite their challenges.

According to Nguyen (2018) embracing CSR will ultimately lead to improved financial performance owing to efficient use of resources in order to ensure funding is availed for CSR activities. Brickley, Smith, and Zimmerman (2002) observed that embracing CSR ultimately led to improved sales as customers were attracted to firms that gave back to the community. The recent awareness campaigns on the destruction of the environment as well as the climate change effects have created new opportunities for companies involved in CSR. By investing in activities that mitigate and correct the negative effects to the environment, companies have found a new marketing strategy to appeal to the masses. Carroll and Shabana (2011) observed that entities which embraced CSR activities that reversed the negative effects of environmental destruction not only appealed to customers but also government agencies. The favourable appeal to both customers and government agencies ultimately lead to improved financial performance.

1.1.4 Manufacturing Companies in Kenya

Kenya's manufacturing sector has largely stagnated over the last five decades. A report by the Kenya Association of Manufacturers (KAM) noted that the country's reliance on agriculture and the service sectors has led to deindustrialization. The report highlights the major sectors as textile and apparel, food and beverage, edible oils, paper and board, automotive, metal and allied, pharmaceutical and medical equipment, leather products and footwear, timber, wood and furniture, energy, electrical and electronics, chemical and allied and the building, construction and mining. The contribution of the manufacturing sector to Kenya's Gross Domestic Product (GDP) was 8.4% which was reduction from 9.2% recorded in 2016. Informed by the dwindling returns in the manufacturing sector, the Kenyan government has made strides to revamp the operations and process that support the sector. The inclusion of the manufacturing sector in the government's Big Four Agenda highlights the commitment to revival of the sector (Kenya Association of Manufacturers, 2019).

According to the KAM 2018 report a majority of the manufacturing companies in Kentya have experienced turbulent times with some facing a threat of going under as operations have become unsustainable. The players in the sector have highlighted a number of problems which have stagnated their growth. Poor taxation policies have been consistently identified as a major hindrance to growth in the manufacturing sector. The Kenyan government is often quick to target companies in the manufacturing sector as quick option to raise revenue. The repercussions have not only affected the local market but the export market as well. By imposing higher taxes, the price of goods manufactured in Kenya is higher than the competition making them unattractive. The poor planning by government in handling the manufacturing sector is further evidenced by the high cost of industrial inputs, power, and labour. The higher costs of productions create inefficiencies and ineffectiveness which ultimately make the manufactured products more expensive.

Informed by the new policy towards supporting the manufacturing sector, the Kenyan government is implementing processes in support of the same. According to a report published by the Ministry of Industry, Trade and Co-operatives, the government has committed to providing manufacturers with cheap and reliable power to run their operations. Protection laws are being implemented to ensure that local manufacturers are shielded from established firms seeking to exploit the Kenyan market. The report also points out that the increased war on counterfeits would serve to strengthen the manufacturing industry. Despite the problems faced, large manufacturing firms have not only survived in the market but have also embraced CSR policies and activities that have positively influenced the welfare of Kenyans.

1.2 Research Problem

The concept of CSR was first explicitly mentioned in the early 1930's by Berle and Means (1932) in their article on the role of firms in promoting social welfare. Berle and Means (1932) argued that CSR was an effective tool in controlling the power of large firms as it directed some of their profits to social good (Berle & Means, 1932). The traditional view of CSR was premised on the ideology that the practice was a luxury good and only established and well off manufacturing firms would engage in CSR (Spence, 2007). According to Johnson and Greening (1999), CSR refers to a

financial strategy adopted by organizations to expand their market share by engaging in activities that promote social welfare.

The modern view of CSR counters the traditional narrative as it argues that the practices are not a cost burden to organizations; rather they present an opportunity for firms to gain a competitive advantage (Johnson & Greening, 1999). Meznar and Nigh (1995) found that the spending on CSR differs depending on firm size. The study revealed that small and medium enterprises (SME) spent considerably lower amounts on CSR compared to large and established firms (Meznar & Nigh, 1995). Brammer and Millington (2006) disputed the findings by Meznar and Nigh (1995) arguing that the measures used to compare the firms were fundamentally flawed and only considered the financial spending. Brammer and Millington (2006) further argued that firms embrace and practice CSR as guided by their strategies. The CSR practices adopted is also dependent on the environment that a firm operates in and the pressing social needs (Brammer & Millington, 2006).

Khamah (2014) opines that embracing CSR is part of management's responsibility to increase shareholder wealth by spending on activities that do not directly contribute to its revenue (Khamah, 2014). Gichohi (2016) observed that most firms perceive CSR expenses as normal operational expenses raising questions as their contribution to profitability of the said firms (Gichohi, 2016). The study sought to examine if the spending on CSR has an impact on the financial performance of large manufacturing companies operating in Kenya. Large manufacturing firms possess the required financial muscle to spend on CSR. A number of large manufacturing companies in Kenya are also listed implying that they are significantly affected by stakeholder perception which ultimately influence their share price. Financial performance reports of listed companies dominate business news in media outlets contributing to a market perception of an entity's operations.

Investors in a listed company rely on financial reports to determine the projected performance over the time they intend to hold a company's share. Listed firms also have the option of raising extra capital from shareholders and other investors. The decision to increase capital for a listed company is heavily influenced by investor perceptions of its operations. Kipruto (2014) argues that positive financial performance reduces screening, monitoring costs as well as diversifying risk across

projects (Kipruto, 2014). Kim, Mauer, and Sherrman (1998) found out that listed companies could increase their probability of future success in projects by building a profile that attracted capital injection. The surety that financing capital will be sourced and availed as and when required allows listed companies to invest in long term projects, innovate, and pursue set objectives (Kim, Mauer, & Sherman, 1998).

The concept of CSR has attracted numerous local and international research. Hayek (1969) concluded that the adoption of CSR in business entities creates a diversion from management's primary role of increasing shareholder wealth (Hayek, 1969). More recently, Henderson (2011) opined that adopting CSR threatened the prosperity of countries as resources were spent on activities that did not directly contribute to the profitability of business entities (Hursh & Henderson, 2011).

The traditional view of CSR has been heavily criticized and proven by research to be fundamentally flawed. Ofori (2014) argued that CSR was a strategic tool that firms would adopt to benefit their operations in both short and long term (Ofori, 2014). In their study, Cochran and Woods (1984) concluded that a positive correlation between CSR and financial performance of the firms reviewed. The findings matched those of Waworuntu, Wantah, Rusmanto (2014) who studied the operations of firms in South Africa (Waworuntu, Wantah, & Rusmanto, 2014).

Locally, studies on the impact of CSR on financial performance of manufacturing firms are mostly unpublished thesis of graduate and undergraduate students. Naiseka (2014) found out that firms in Kenya are driven to embrace CSR by shareholders. Naiseka's study concluded that no clear link existed between CSR and financial performance (Naiseka, 2014). Wanjala (2011) conducted a study to ascertain the factors impacting adoption of CSR among Kenyan commercial banks. The study concluded that profitability was a major driver for banks that practised CSR.

Kipruto (2014) observed that CSR practices did not in any way affect the performance of commercial banks in Kenya. A majority of the local studies have focused on the banking sector and their findings cannot be generalized to other sectors. The study aimed to fill the gap by focusing on the manufacturing sector and posing the question; what are the effects of corporate social responsibility practices on the financial performance of large manufacturing firms in Kenya?

1.3 Objective of the Study

To examine the effect of corporate social responsibility on the financial performance of large manufacturing companies in Kenya.

1.4 Value of the Study

The recent changes in government policy geared to boosting the manufacturing sector in Kenya presents an opportunity for players to expand their operations. It is expected that the policy changes will lead to improved performance. The study will benefit scholars and practitioners ascertain the role of CSR in improving the financial performance of manufacturing firms in Kenya. The study intends to demonstrate the CSR practices that large manufacturing companies have adopted and how the same has affected their financial performance.

The study will also benefit the management teams of small manufacturing firms and foreign entities that have plans to set operations in Kenya. By highlighting the CSR practices that large manufacturing firms have adopted, other players in the Kenyan manufacturing sector can determine what specific practices have the most impact on their financial performance. The study will also reveal CSR practices that either have no impact or have minimal impact on financial performance.

The study will also benefit policy makers in government and private sector. The discussion on CSR expenditure and the impact on performance could provide policy makers with justification on creating policy that encourages or discourages CSR. Private sector players could use the research findings to lobby stakeholders to address legislations, policies, and practices to grow the manufacturing sector. The study will also contribute to the knowledge of CSR and academics in general.

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

The chapter discusses the theories and concepts that the background of the study. The chapter is systematically organized and highlights the theories informing the study, research variables, empirical reviews, and a summary.

2.2 Theoretical Foundation

The concept of CSR has attracted the interest of scholars and practitioners over the years. In the contributions, researchers and scholars have advanced theories and models in support of CSR which are widely published and referenced in the field of management. The essence of highlighting theories in research is to define, relate and propose related concept to explain or predict situations by demonstrating an existence or lack thereof between or among the research variables. The study will expose three theories namely; stakeholder theory, slack resource theory, and agency theory. The three theories encapsulate the research variables and offer a detailed perspective on CSR practices adopted by large manufacturing firms and their effect on the financial performance.

2.2.1 Stakeholder Theory

The stakeholder theory highlights the relationship among a firm's stakeholders defining the processes and outcomes of the interactions as well as interests pursued. Hillman and Luce (2001) argue that the stakeholder theory ought to guide management teams to pursue the interests of all stakeholders. Embracing CSR demonstrates that a firm respects the interests of the society and the environment in which it operates. Freeman and Reed (1983) revealed that an organization has two groups of stakeholders each with unique needs and expectations. The first group of stakeholders are those affected by a firm's operations and mostly consist of communities who share a neighbourhood with a firm. The second group of stakeholders are those who provide resources to support a firm's operations.

The stakeholder theory postulates that all stakeholders impact a firm's operations depending on how management relates with them. Pederson (2004) observed that maximizing the value of each stakeholder ultimately maximizes the value of a firm. Jensen (2002) argued that firms which wish to report positive market performance must address the interest of stakeholders beyond their shareholders. The communities in which a firm operates have expectations on the responsibilities that the entity must meet or risk closure. Zingales (2000) also advocated for good relations between firms and their surrounding communities to ensure sustainable operations.

Freeman (1984) postulated that business entities have both implicit and explicit agreements with all their stakeholders and are, therefore, liable to honour the said agreements. Honouring both implicit and explicit agreements makes a firm reputable among its stakeholders. Tesler (1980) argued that firms which honour agreements have minimal litigations and enjoy cordial interactions with interested parties. The stakeholder theory, therefore, postulates that CSR positively performance, from a financial perspective. Critics of the theory argue that it challenges the shareholders' property privileges. Sternberg (1997) argued that the stakeholder theory challenges the ideology of capitalism.

2.2.2 The Slack Resource Theory

The above theory defines slack resources as free and often unexploited or underutilized resources an organization possesses and can be deployed for use if need arises. Wisink (2012) argues that the slack resource theory recommends that firms with slack resources invest the same in CSR activities to avoid wastage and at the same time improve social welfare. According to Waddock and Grave (1997) availability of slack resources implies that a company financially sound and investing in CSR would not impact negatively on its performance.

McGuire (1988) observed that analysts and practitioners had managed to convince most companies that embracing CSR was an expensive affair, hence could only be done if slack resources. McGuire (1988) recommended organizations to employ the slack resources in CSR as it enhanced their effectiveness and efficiency positively contributing to achievement of organizational goals. Buchholtz (1999) argued that

using slack resources for CSR minimized the possibility of wastage and the negative effects accruing from the same.

According to McGuire (1988) several studies point to a direct correlation between CSR and financial performance, underlining the slack theory argument. Ahmed (2014) argues that improved environmental awareness and social consciousness goes hand in hand with improved performance. Zhong (2011) argued that there was no clear evidence between slack resources and financial performance. Ahmed (2014) countered the argument by stating that use of slack resources for CSR endeared a firm to the society and ultimately improved its financial and non-financial performance. Ross (1973) criticizes the slack resource theory by arguing it leads to agency problems that could negatively affect a firm's performance.

2.2.3 Agency Theory

The above theory was first fronted by Ross in 1973 where he defined the relationship between principles and agents. Ross (1973) postulated that principles hired agents to work for them and expected the latter to make the best decisions to benefit the former. Gerrans and Murphy (2005) revealed that agents in the company include the management team while the principles were the shareholders. According to Ross (1973) the agency theory relies heavily on the assumption that the sole responsibility of management teams is to maximize shareholders' wealth. Ross (1973), therefore, postulates that embracing CSR depicts a waste of a firm's assets. Williams and Siengel (2005) argued that embracing CSR furthers other objectives as opposed to the core objective of maximizing shareholders' wealth.

Williams and Siengel (2005) also argued that embracing CSR introduced moral hazards and agency costs which negatively affected investors' returns. In making decisions on CSR management teams were likely to be subjective leading to disputes and cause unnecessary squabbles among members of the management team negatively impacting on expected performance. According to Jones (2004) agents as depicted by the agency theory possesses an in depth knowledge in the duties and responsibilities assigned by the principal. Jones (2004) further argued that there is need for principals to reasonably trust agents to meet expectations and be accorded support to achieve the same. The agency theory requires agents to uphold and respect

the trust bestowed by agents. The agency theory argues that an adverse association exists between CSR and financial performance

2.3 Determinants of Financial Performance

Mirza and Javed (2013) argued that embracing CSR does not in any way break laws or regulations stipulated in pursuing the wealth maximization. On the contrary, embracing CSR enables business entities to endear themselves to the communities in which in they operate positively impacting on their operations. Mirza and Javed (2013) argued that perceiving CSR as unnecessary expense and a waste of resources is fundamentally misguided in the current business environment. The current consumer is more informed and aware of the role of business entities to support communities and their environments. A consumer will, therefore, make a decision to purchase a product based on an entities' CSR activities. Chen (1995) identified internal and external factors influencing financial performance.

2.3.1 Corporate Social Responsibility

CSR has been proven to directly and indirectly contribute to financial performance. Tan-Mullins (2014) observed that embracing CSR affects an entity's sustainable competitive advantage, customer satisfaction, and reputation. Actively pursuing CSR creates a sustainable competitive advantage in the long run. Spence (2007) observed that linking CSR with a firm's overall strategy creates a sustainable competitive advantage. Management must, however, select the CSR activities carefully to ensure maximum impact in the long run. Sundaram and Inkpen (2004) observed that CSR directly contributed to the reputation of a firm. Reputable entities record higher sales due to their recognizable brand.

2.3.2 Size

Chen (1995) argued that company size ought to be determined by its amount of assets. Firms with a large asset base have a well-established organizational structure and culture. A large asset base enables firms gain easier access to factors of production including extra capital and human resource skills. Chen (1995) further argued that firms with a large asset base invest in technology that create market owing to superior products and cheaper production costs. Dominant firms in any market have the capability to alter prices and production volumes to achieve desired levels of

profitability. Firms with a large assets base also enjoy economies of scale as they can leverage on their size of operations to negotiate for favourable costs and higher revenues.

Yenesew (2014), however, warns against pursuing the expansion of operations owing to the challenges that arise from the same. Firms that become too big often grapple with diseconomies of scale owing to inefficient operations. Several studies have been conducted to ascertain the effects of the size on the financial performance of firms. Lee (2015) positively associated firm size with corporate financial performance. Lee (2009) also observed that smaller firms recorded higher growth rates in profits compared to bog firms. Pervan and Visic (2012) observed that the relation between profitability and firm size was evident and was either positive or negative.

2.3.3 Capital structure

According to Mirza and Javeth (2013), the decision on how to finance a company's operations ultimately affects its financial performance. Management teams have the option of sourcing more capital from shareholders, using retained earnings or using debt. The decision on the most optimal source of funds depends on various factors. Acquiring debt increases the risk of default which ultimately leads to bankruptcy arising from failure to pay current and accruing debts. If well used, debt financing is a cheaper source of funding owing to the tax benefits accruing as well as increased scrutiny due to obligations arising.

Muriu (2011) opines that use debt financing is favoured by most firms due to ease of access. According to Mwangi and Birundu (2015), there is need for management teams to be cautious in accruing debt. Objective analysis of a business entity's capacity to pay its debt in the short and long run ought to be thoroughly interrogated. In their study, Mwangi and Birundu (2015) concluded that capital structure for small and medium enterprises was not significantly linked with their financial performance. Ndiwa (2014) observed that the capital structure decisions made by management teams in sugar manufacturing firms in Kenya had negatively impacted on their financial performance.

2.3.4 Corporate Governance

Corporate governance refers to the association that exist among management teams, board of directors, investors, regulators, and other interested parties. Bairathi (2009) opined that corporate governance involves more than the management function and requires all parties interested in the operations of a firm to maintain fair, efficient, effective, and transparent supervision and oversight. The rise in number of listed companies across the globe has necessitated an increase in corporate governance scrutiny. Wanjiru (2013) observes that strong corporate governance not only protects investors but all stakeholders affected by a business entity's operations. Strong corporate governance, therefore, enables accountability as each party is held accountable for their actions or inactions. Weak corporate governance creates loopholes for entities to exploit and waste resources at the expense of investors.

Freeman (1984) observed that companies which embrace strong corporate governance have favourable and sustainable business operations. Zheka (2005) opined that corporate governance ultimately determines financial performance. Kigotho's (2014) study on the relation between attributes of corporate governance and corporate financial performance among listed firms on the NSE determined that a positive association exists. Olweny (2013) also sought to determine the influence of corporate governance on the performance of Kenyan insurance companies. Olweny concluded that there was positive correlation between firm performance and corporate governance.

2.4 Empirical Review

Yusoff, Mohamad, and Darus (2016) led a research to ascertain the influence of CSR disclosure on the financial performance of publicly listed firms in Malaysia. The study evaluated the published financial accounts of thirty publicly listed companies to ascertain the nature and depth of CSR disclosure. The researchers embraced a descriptive research design and used hypothesis to determine the impact of CSR disclosure on the financial performance of the listed firms. The study found out that there was a significant relationship between disclosing CSR practices and the corporate financial performance of listed Malaysian firms in the subsequent year. The researchers also found out that top performers in the stock market displayed a

relatively high breadth of CSR disclosure. The research study also concluded that displaying volumes CSR was inconsequential; rather it was the variety of CSR practices.

Maqbool and Zameer (2018) evaluated the link between CSR and financial performance by empirically analysing Indian banks. The study focused on twenty-eight banks listed on the Bombay Stock Exchange. The descriptive study evaluated the performance of the listed banks over a 10-year period from 2007 to 2016. The researchers incorporated risk, age, capital intensity, and size as control variables. The study concluded that CSR positively impacted on profitability and stock returns of listed banks in India. The researchers concluded that in the Indian context, it pays to be socially responsible. As part of their recommendations, Maqbool and Zameer (2018) advised that firms should not perceive CSR as an optional activity, rather management should integrate CSR with their long term business strategy (Maqbool & Zameer, 2018).

Platanova and Asutay (2018) conducted a study to determine the impact of CSR disclosure on the financial performance of the gulf region banking sector. The descriptive study evaluated the financial reports of Islamic bank in the Gulf Cooperation Council (GCC) region over a fifteen-year period from 2000-2014. The study revealed a significant positive relationship between disclosing CSR and future performance of Islamic banks. The observation underscored the importance of CSR activities in positively affecting the financial performance of GCC region Islamic banks. The study concluded that a relationship that was insignificant between individual dimensions of CSR and current financial performance was existent among the banks under review. The study recommended that Islamic banks in the GCC region ought to embed CSR in their missions and visions for improved financial performance (Platonova & Asutay, 2018).

Nguyen (2018) sought to determine the effect of corporate social responsibility disclosure on the financial performance of credit institutions in Vietnam. The study examined the financial reports of credit institutions over a six-year period from 2011 to 2016. Nguyen (2018) used content analysis as the research design while ordinary least square estimator analysed the association between the research variables. Nguyen’s study concluded that was a significant negative relationship between CSR

disclosure and financial performance of commercial banks in Vietnam. Nguyen (2018) opined that the negative relationship between CSR and financial performance could be explained by laws on CSR in Vietnam and the economic slowdown experienced at the time of the research (Nguyen, 2018).

Gangi, Mustili, and Varrone (2019) conducted a study to assess the influence of CSR knowledge on the corporate financial performance of the European banking industry. The study sought to evaluate the operations of seventy-two banks from twenty European countries over seven years from 2009 to 2015. The empirical study relied on hypothesis to determine the association between the research variables. The research findings revealed that internal knowledge of CSR led to proper implementation of the practices leading to beneficial implications for external stakeholders. The study also revealed that engaging in CSR improves the competitiveness of banks in Europe as customers perceive the bank more positively (Gangi, Mustilli, & Varrone, 2019).

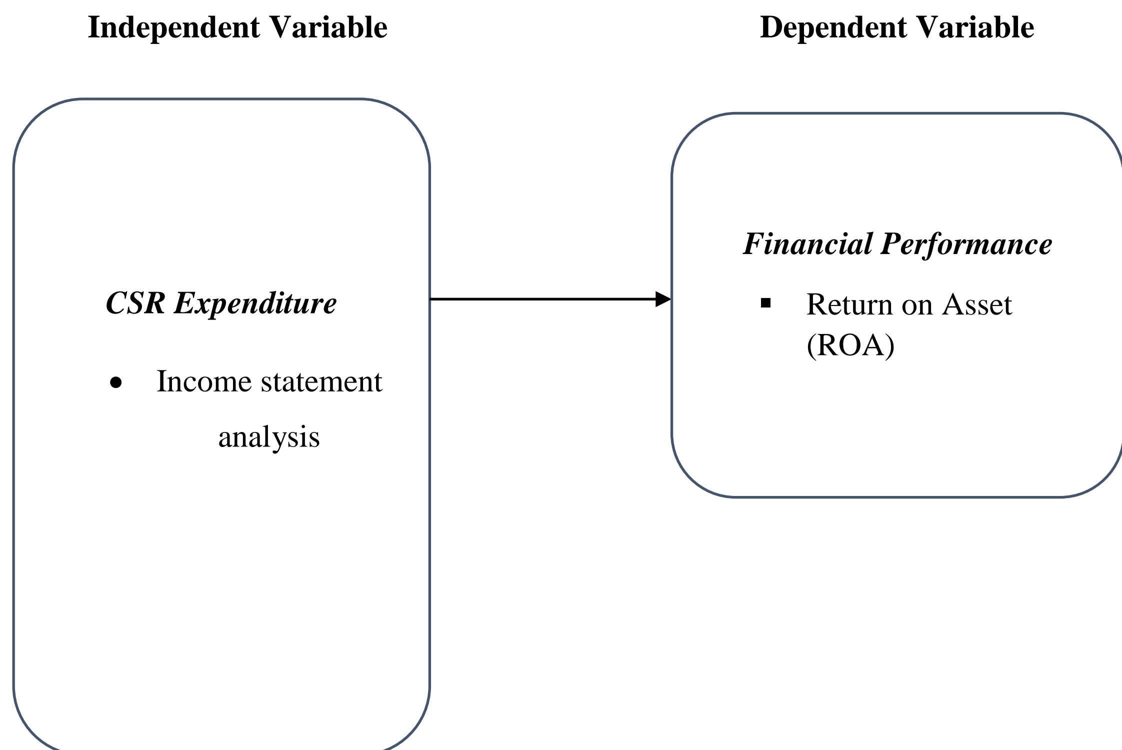
Gichohi (2016) sought to explore the impact of CSR in the performance of firms listed on the Nairobi Securities Exchange (NSE) from a financial perspective. The researcher adopted a research design that was descriptive to define the association between the research variables. Gichohi (2016) studied all the sixty-six companies listed on the NSE from 2010-2014. The researcher relied on secondary data which was sourced from financial results, company reports, and website material of the listed firms. The research concluded that a positive but insignificant correlation between CSR and financial performance of listed companies on the NSE existed. Based on the findings, Gichohi (2016) recommended that firms should only embrace CSR should not be undertaken voluntarily; rather, regulators should demand that firms allocate funds to support communal welfare projects.

Mungai (2015) conducted a local study to determine the impact of CSR on the financial performance of the manufacturing sector players in Kenya. The study targeted sixty-eight manufacturing firms operating in Kenya as of 2014. The study embraced descriptive research design with the data collected analysed using multiple regression model. Mungai (2015) concluded that CSR had little consequence on performance, from a financial perspective. The study also revealed that players in the Kenyan manufacturing sector perceived CSR as a voluntary exercise which was

embraced solely to improve the social welfare of communities around them (Mungai, 2015).

2.5 Conceptual Framework

In determining the empirical relationship between corporate social responsibility and financial performance, the study relied on a two-perspective conceptual framework. The first perspective entailed the identification of the amounts spent by manufacturing firms on their CSR function. The second perspective entailed ascertaining the impact of the CSR expenditure on financial performance of large manufacturing firms. Return on Asset (ROA) was used as the financial performance measure in this study.



2.5 Summary

Yusoff, Mohamad, and Darus (2016) study on listed firms in Malaysia demonstrated the impact of CSR disclosure on the financial performance. The observations underscored the need for firms to embrace CSR as the reputation created improved the demand for a listed company's shares. Maqbool and Zameer (2018) also found out that it pays to be socially responsible as evidenced by their study on the financial performance of listed banks in India. Platanova and Asutay (2018) study also mirrored the observation by Maqbool and Zameer (2018) as it revealed that CSR

positively influenced the future financial performance of Islamic banks. An interesting observation by Platanova and Asutay (2018) was that CSR practices did not influence current financial performance.

Nguyen (2018) observed that there was a negative relationship between CSR and financial performance. Nguyen (2018) defended his findings by stating that the observation underscored the legal guidelines hindering CSR in Vietnam as well as the difficult economic environment experienced when the study was conducted. Gichohi (2016) also found out that there was a positive, though insignificant, relationship between CSR and financial performance. Gichohi's (2016) study focused on listed firms on the NSE.

Opinion is heavily split on the impact of CSR on the performance, financially, of business entities across different sectors. From the literature reviewed, the split is evident from theories postulated to the empirical studies carries. The dynamic nature of business operations has created opportunities and threats leading to better management of resources. Proponents of CSR argue that embracing the practices ultimately improves the financial performance. Opponents of CSR argue that the practices are a waste of resources which will negatively affect a firm's financial performance in the long run.

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

The chapter highlighted the methodology adopted in carrying out the research study. The chapter details the method used to collect data required, evaluate the data and draw research findings. The chapter highlighted the research design and the target population as well as the process of data analysis. The chapter also provided a justification for the data analysis process.

3.2 Research Design

The research study relied on a descriptive survey design. Embracing the said research design allowed for an analysis of the impact that CSR has had on the performance of large manufacturing firms in Kenya. A descriptive design was appropriate as secondary data will be used to test relationship between the research variables. Doyle (2004) defined descriptive survey design as a model that enables researchers to ascertain the attitudes, opinions, and habits of the respondents. The study therefore, used surveys to ascertain the respondents' perceptions and understanding of CSR, and how the same contributes to their financial performance. Embracing a descriptive survey design also minimized possibilities of manipulating the population behaviour owing to the limited time allocated for conducting this study.

3.3 Population

The target population of this research was the large manufacturing companies operating in Kenya. The criteria used to determine large manufacturing firms was the revenue volumes and capital size. For purposes of the study, the large manufacturing firms to be considered had an average annual sales volume of at least USD 10 million over the past five years.

3.4 Sample Design

The essence of sampling was to ensure that the part selected for the study is a representative of the population. The study adopted a simple random sampling technique to ensure that all large manufacturing firms selected have an equal

possibility of being incorporated in the sample. The study relied on judgemental sampling owing to the limited resources in conducting the study. The use of judgemental sampling allowed the researcher to use a predefined criterion that units must satisfy so as to be selected in the research sample (Waworuntu, Wantah, & Rusmanto, 2014).

3.5 Data Collection

The study relied on secondary data to ascertain the nature of relationship between CSR and financial performance of large manufacturing firms in Kenya. The secondary data was obtained from published annual financial reports and manufacturing companies' websites. The study will also use manufacturing sector reports provided by government entities, lobby associations, and development partners. The secondary data collected captured a period of five years from 2015-2019 and focused on the balance sheet and income statement.

3.6 Validity and Reliability

Validity in research relates to the instruments used to collect research data. Hopkins (2004) defined validity as the extent to which the measuring procedure used in a study measures the theoretical concept intended. Validity of research data confirms the consistency between the theory and operationalization of procedures adopted in a study. Reliability tests and evaluates the quantitative data collected. The study ensured validity and reliability by obtaining data from reliable sources, specifically company websites and published annual reports.

3.7 Data Analysis

The data collected was analysed in various ways. Percentages were used to determine the CSR practices embraced by listed manufacturing firms. Other quantitative data were coded using SPSS (statistical packages for social sciences) to provide a detailed regression analysis. Specifically, means and standard deviation for the independent variable will be determined. The study applied ordinary least squares regression method to ascertain the influence of CSR on financial performance of large performance companies in Kenya. T-tests assessed the significance of the independent variable in determining the dependent variable.

3.7.1 Regression Equation

The analytical model embraced in this study is as follows;

$Y = f$ (CSR practices)

The empirical used in conducting the study is as follows;

$Y = \alpha + \beta_1 x_1 + \beta_2 x_2 + \beta_3 x_3 + \varepsilon$

Whereby;

Y - Represents financial performance as demonstrated by return on assets (ROA)

α – is the constant

$\beta_1, \beta_2, \beta_3, \beta_4, \beta_5$ – Represents coefficients to be determined by the model

X_1 = CSR score as determined by the financial expenditure

X_2 = Efficiency calculated by dividing cost of sales with total sales

X_3 = Capital intensity calculated by diving total assets with total sales

ε – error term

3.8 Test of Significance

The F test at 95% level of confidence will be used to ascertain if there exists a statistical significance of the whole model. The t-test at 95% will also be used to ascertain the significance of the independent variable. The study relied solely on the coefficient of determination to underscore the reliability of the regression model.

CHAPTER FOUR

DATA ANALYSIS AND INTERPRETATION

4.1 Introduction

This chapter looks at the research results and the subsequent interpretations of the analyzed data. The chapter contains descriptive statistics as well as graphical representations, correlation and the pooled regression analysis and finally interpretations of the findings.

4.2 Descriptive Statistics

This chapter contains summary statistics and graphical analysis.

4.2.1 Summary Statistics

Table 4.1 Summary Statistics

Descriptive Stats					
	N	Min	Max	Mean	Std. Dev
ROA	240	0.0142	0.9703	0.148392	0.1796303
CSR	240	1.7659	6.3754	4.151946	1.0887777
Efficiency	240	-1.5971	0.9994	0.591126	0.2915749
Capital intensity	240	-1.5971	14.6918	0.912568	1.7576874
Valid N (listwise)	240				

Author 2020

The Table above indicates that average ROA is 0.148392, which indicates that 14.84%. The average CSR over the analysed time was 4.152. The tables show that the minimum and maximum for the efficiency was -1.5971 and 0.9994 respectively while its mean was 0.5911.

The table indicates that the average capital intensity over the considered time frame was 0.9125 while its minimum and maximum was -1,5971 and 14.6918 respectively.

4.3 Correlation analysis

The researcher sought to ascertain the relationship between the study variables. For this to be determined, a correlation analysis was conducted. The relationships were determined using the Pearson's correlation coefficient.

Table 4.2: Relationship between variables

Correlations					
		ROA	CSR	Efficiency	Capital intensity
ROA	Pearson Correlation	1	0.079	0.047	-0.064
	Sig. (2-tailed)		0.221	0.473	0.321
	N	240	240	240	240
CSR	Pearson Correlation	0.079	1	0.078	-0.022
	Sig. (2-tailed)	0.221		0.231	0.737
	N	240	240	240	240
Efficiency	Pearson Correlation	0.047	0.078	1	-0.088
	Sig. (2-tailed)	0.473	0.231		0.174
	N	240	240	240	240
Capital intensity	Pearson Correlation	-0.064	-0.022	-0.088	1
	Sig. (2-tailed)	0.321	0.737	0.174	
	N	240	240	240	240

The results showed that ROA had a weak and positive correlation with CSR but showed a weak and negative correlation with capital intensity. The results also showed that ROA had weak and positive correlation with efficiency. As all the correlation values are below 0.75, hence there is no multicollinearity among the research variables.

Table 4.3: Model summary

Model Summary					
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Durbin-Watson
1	.107a	0.011	-0.001	0.1797311	0.471

Author 2020

The R square value (Coefficient of determination) is 0.107 which means 10.7% of the variation in ROA was as a result of changes by the independent variables. The research findings also revealed that the standard error of estimate is 0.1780 hence showing that there is little variation and thus the correlation will be almost perfect.

The Durbin-Watson measures autocorrelation and a value towards 0 indicates a positive autocorrelation. The results show the value is 0.471 hence indicating a positive autocorrelation.

Table 4.4: Regression coefficients

Coefficients								
Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.	Collinearity Statistics	
		B	Std. Error	Beta			Tolerance	VIF
1	(Constant)	0.089	0.051		1.76	0.08		
	CSR	0.012	0.011	0.075	1.159	0.248	0.994	1.006
	Efficiency	0.022	0.04	0.036	0.545	0.586	0.986	1.014
	Capital intesity	-0.006	0.007	-0.06	- 0.916	0.361	0.992	1.008

From Table 4.5 the regression equation derived was as follows;

$Y = 0.089 + 0.012 X_1 + 0.022 X_2 - 0.006 X_3 + \varepsilon$

The regression equation found an insignificant positive relationship between ROA and CSR whereas there is an insignificant positive relationship ROA and efficiency. The findings also found out that capital intensity had an insignificant negative relationship with ROA.

4.4 Interpretation of Findings

The research found out that there is an insignificant positive connection between ROA and CSR hence an increase in CSR leads to an increase in ROA. Similarly, Maqbool and Zameer (2018) evaluated the link between CSR and financial performance by empirically analysing Indian banks and concluded that CSR positively impacted on profitability and stock returns of listed banks in India. However, Kallio and Nordberg (2006) poised that the concept of CSR was not only naïve but a distraction to the profit making objective of any business firm.

The research findings also led to the conclusion that an minor positive relationship between ROA and efficiency; thus there is an inverse relationship between the two variables. Similarly, Tan-Mullins (2014) observed that embracing CSR affects an entity's sustainable competitive advantage, customer satisfaction, and reputation. Spence (2007) also observed that linking CSR with a firm's overall strategy creates a sustainable competitive advantage.

The findings also found out that capital intensity had an insignificant negative relationship with ROA hence an increase in capital intensity would lead to a decrease in ROA. According to Waddock and Grave (1997) availability of slack resources implies that a company financially sound and investing in CSR would not impact negatively on its performance.

CHAPTER FIVE

SUMMARY OF FINDINGS, CONCLUSIONS AND RECOMMENDATIONS

5.1 Introduction

This chapter looks at the findings of the study, the conclusions as a result of the findings and the recommendations made to the study. This study also looks at the limitation of the research and makes suggestions of areas that may require further study.

5.2 Summary

The purpose of the research was to examine the effect of corporate social responsibility on the financial performance of large manufacturing companies in Kenya.

The research had return on assets as the dependent variable and CSR, efficiency and capital intensity as the independent variables. The study used a descriptive and a cross-sectional study design and targeted large manufacturing companies operating in Kenya. The study used secondary data. Descriptive statistics and inferential statistics were the mode of statistics.

The average ROA is 0.148392, which indicates that 14.84%. The average CSR over the analysed time was 4.152. The results also showed that the minimum and maximum for the efficiency was -1.5971 and 0.9994 respectively while its mean was 0.5911.

The correlation results obtained showed that ROA had a weak and positive correlation with CSR but showed a weak and negative correlation with capital intensity. The results also showed that ROA had weak and positive correlation with efficiency. As all the correlation values are below 0.75, hence there is no multicollinearity among the research variables. The R square value (Coefficient of determination) is 0.107 which means 10.7% of the variation in ROA was as a result of changes by the independent variables. The research findings also demonstrated that the standard error of estimate is 0.1780 hence showing that there is little variation and thus the correlation will be almost perfect.

The results showed that an insignificant positive relationship between ROA and CSR whereas there is an insignificant positive relationship ROA and efficiency. The findings also found out that capital intensity had an insignificant negative relationship with ROA.

5.3 Conclusions

The research found out that there is an insignificant positive relationship between ROA and CSR; hence increasing CSR expenditure led to a paltry increase in ROA. The research findings confirmed that there was an insignificant positive relationship ROA and efficiency thus there is an inverse relationship between the two variables. The findings also found out that capital intensity had an insignificant negative relationship with ROA hence an increase in capital intensity would lead to a decrease in ROA.

5.4 Recommendations

The researcher came to a conclusion that CSR has an impact on ROA among manufacturing firms in Kenya. However, the research recommends that manufacturing firm managements should be wary about CSR fluctuations as it could affect ROA. The researcher recommends that manufacturing firm management should have policies on how to reduce CSR fluctuations.

The researcher came to a conclusion that CSR score, Efficiency and Capital Intensity have an effect on ROA and the government should have policies and have strategic mechanisms to ensure GDP is growing and hence ROA of manufacturing firms will continue to grow.

The findings of the study came to a conclusion that Capital Intensity has a negative insignificant effect on ROA hence the study recommends that more research is done involving all CSR factors and their effect on ROA.

5.5 Limitations of the study

The study did not consider all CSR factors.

The research population only looked at large manufacturing firms in Kenya and did not cover the whole sector.

The research period used was only for 5 years and hence results obtained from the study only explain what has affected ROA in the study period.

Collection of data was a challenge as some of the CSR factors are not readily available to the public and it needed certain approvals and payments to acquire.

5.6 Suggestion for Further Research

The research study proposes further studies to be carried out using other CSR variables.

The study also recommends further research to include other institutions in the sector.

The research recommends that further studies to be conducted to have a longer time period so as to clearly find out what affects CSR during that time period.

The study recommends that government and private firms to provide easy access of data to enable researchers and students to increase further research without having to pay to get data.

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APPENDICES

Appendix I: Data Collection Form

	Year 2014	Year 2015	Year 2016	Year 2017	Year 2018	Average
CSR Expenditure						
Revenues						
Cost of Sales						
Total Assets						
Return on Assets (ROA)						