

The Mediating Role of Corporate Image on the Relationship between Corporate Social Responsibility and Firm Performance: An Empirical Study

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Abstract

This study attempted to investigate the effects of corporate social responsibility on firm performance. It also tried to identify the mediating role of corporate image on the relationship between corporate social responsibility and firm performance. This research collected data on latent constructs through a questionnaire administered survey of managers across a spectrum of industries in Bangladesh. The proposed model has been empirically tested by using SmartPLS 2.0 software. Empirical results, based on a sample of 125 firms, suggest that corporate social responsibility can improve corporate image by establishing good controls and monitoring and thereby improve overall firm performance. The results of this study also suggest that executives should not dismiss corporate social responsibility and also need to take into account the mediating role of corporate image. A more comprehensive model can be developed considering some other context specific variables. This study also highlights the implications of the model.

Keywords: Corporate Social Responsibility, Corporate Image, Firm Performance

Introduction

Corporate social responsibility (CSR) has gained significant attention from both academics and professionals in recent years. This attention derives mainly from the realization of the potential strategic value of pursuing CSR practices in the firm (McWilliams et al., 2006). For instance, firms can possibly achieve a positive image and/or better relationship with essential groups such as customers through CSR practices. Both internal and external stakeholders are emphasizing on the potential and actual benefits of CSR implementation and practices. The globalization of firms is also encouraging the spread of CSR practices in

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various organizations. Values that managers use to guide their decision making process are critical for insight into CSR practices of a firm (Agle et al., 1999). In addition, personal and organizational characteristics are also related to varying perceptions in ways that would help to clearly and precisely express the conditions of CSR practices.

According to the literature, company reputation or image, customer satisfaction, and firm performance are highly significant in the scholarly study (Homburg et al., 2005). Image is a general trait of a firm and reflects the extent to which a firm is perceived as good or bad (Roberts and Dowling, 2002). Precisely, corporate image refers to the impressions of a particular company held by the public (Johnson and Zinkhan, 1990). Image or reputation is important because it demonstrates how a particular firm compares to its competitors considering the stakeholder impressions of the firm's disposition to behave in a certain manner (Clark and Montgomery, 1998). Corporate image can affect the ability to raise prices with consumers and can create mobility barriers within the industry (Peloza, 2006). CSR practices are expected to signal to stakeholders a positive impression of corporate behaviour, thereby increasing image. A significant number of academic research investigates the relationship between corporate social responsibility (CSR) and firm performance; however, the findings are indecisive (Chen and Wang, 2011; Jacobs et al., 2010; Mahoney and Roberts, 2007). Though results are mixed, the trend seems to suggest a positive relationship between CSR and firm-performance. To date, a few studies have investigated that relationship further to see the potential effects of mediating variables. This is also in accordance with the work of Galbreath and Shum (2012) as they argue that different intervening variables have not been fully investigated to see the effects of mediating variables on that link. CSR and corporate image have gained much attention in different research areas; however, in isolation. Less focus has given to investigate the underlying process of performance improvement through their collective effect. Hence, one of the objectives of this study is to investigate the mediating role of corporate image on the link between corporate social responsibility (CSR) and firm performance.

Objectives of the Study

Many previous studies have indicated that CSR practices are growing in developing countries as a result of pressures from external stakeholder groups (Belal, 2001; Kamal and Deegan, 2013). Kamal and Deegan

(2013), in this regard, argue that the more an organisation faces legitimacy crisis the more it undertakes CSR initiatives. Hence, the primary objective of this study is to investigate the role of corporate social responsibility on firm performance. To comply with the primary objective, this study stresses upon following specific objectives:

1. To investigate the role of corporate social responsibility (CSR) on corporate image and on firm performance.
2. To examine the mediating role of corporate image on the link between CSR and firm performance.

Justification for the Study

This study attempts to contribute to the existing CSR literature in three ways. First, this study provides an opportunity to see the relationship among CSR, corporate image and firm performance from a developing country context, such as Bangladesh, as most of the CSR studies considered those links from developed country perspectives. Second, Research on CSR has not kept pace in that the vast majority of studies examine those links and ended up with inconclusive findings. CSR is found to have a positive effect firm's overall performance in association with a fully mediated variable like corporate image. Finally, the findings are important for policymakers and executives in developing countries who are considering the adoption of CSR for improving their firm image as well as performance.

Literature Review and Hypotheses Development

Corporate Social Responsibility and Corporate Image

According to Carroll (1979) CSR refers to the social responsibility of business which encompasses the economic, legal, ethical, and discretionary (philanthropic) expectations that society has on organizations. This definition has become fairly widely accepted (Mohr et al., 2001) and emphasizes four principle types of responsibilities; economic, legal, ethical and philanthropic (Matten and Crane, 2005). Corporate image is a shared view of an organisation perceived by its stakeholders and it is considered to be an important factor for organisational legitimacy (Patten, 1991; Dowling, 1986). Organisations use several strategies to improve their image and the CSR engagement is one of the major ways to develop such image (Galbreath, 2010b; Vilanova et al., 2009).

The legitimacy perspective reports that firms persistently try to legitimate their activities through social and environmental friendly behaviours. The term, legitimacy theory, derives from 'social contract' that offers a firm a 'license to operate' within the society. Deegan's (2009) legitimacy theory attempts to explain corporate legitimate behaviour to satisfy stakeholders. A number of earlier studies (Patten, 1991; Roberts, 1992; Govindan et al., 2014) have investigated the nature of CSR activities where legitimacy pressure was found to be as an important factor for CSR practices. It has been argued that organisations accept social and environmental compliance to gain legitimacy which has been linked with better corporate image.

The existing literature shows strong relationship between corporate social responsibility and corporate image (McGuire et al., 1988). According to Fryxell and Wang (1994), image is an investment. It has been argued that reputation is a strategic asset in order to gain competitive advantage (Srivastava et al., 1997). Fomburn (1996) and many other scholars argue that CSR activities, such as, environmental friendly business operations, community engagement, human rights policies promote a positive image of the firm (Sweetin et al., 2013). If the broader stakeholders group find any irresponsible firm behaviour it can affect image which ultimately threatens firm's existence. Realising these facts, organisations are increasingly showing their commitment to offer environmental friendly products and services. Therefore, it is important for an organisation and its management to build strong corporate image and CSR is a mechanism which helps to establish that image (Arendt and Brettel, 2010). Thus, we postulate:

H1: corporate social responsibility has positive impact on corporate image

Corporate Image and Firm Performance

Corporate image is described as an organisation's strategy to create a desired identity (Gray and Balmer, 1998; Roberts and Dowling, 2002). CSR scholars argue that organisations and their managers create an organisation's image through various social and environmental friendly operations that satisfy the stakeholders (Bebbington et al., 2008; Carmeli and Cohen, 2001; Fomburn, 1996). It has been argued that corporate image is a symbol of corporate identity which helps to achieve organisational objectives. Prior literature suggests that corporate image plays a vital role in improving firm performance through acquiring more

customers (Fomburn and Shanley, 1990; McGuire et al., 1988). A growing number of academic studies empirically tested the impact of corporate image on firm performance and found a positive relationships (Hammond and Slocum, 1996; Roberts and Dowling, 2002). These findings suggest that image works as a signal by which a firm selects its strategies to satisfy stakeholders. In addition, Brammer and Millington (2005) note that the external causes, such as, good corporate strategy, management quality, efficient use of resources help to maintain corporate reputation and enhance performance. Porter and Kramer (2007) argue that through CSR, firms establish their image that ensures competitive advantage and provide financial returns from the market. Good image of a firm helps to reduce associated costs of a firm as employees prefer to work in a reputed firm at a lower salary (Roberts and Dowling, 2002). On the basis of above discussion, the following hypothesis is proposed,

H2: *There is a positive relationship between corporate image and firm performance*

Corporate Social Responsibility (CSR) and Firm Performance

Scholars broadly argue that organisations can benefit from CSR practices through gaining more customers (Gallardo-Vázquez and Sanchez-Hernandez, 2014). Firms that satisfy their stakeholders are able to achieve competitive advantage. Firms can benefit from CSR enhanced reputation when they face major crisis (Janney and Gove, 2011). Carroll (1979) suggests four types of responsibility related to CSR such as economic, legal, ethical, and discretionary responsibility. Birch (2002) argues that all firms are not likewise in practicing CSR. The economic responsibility of a firm is to make profit through job creation and providing better quality products and services. The safer workplace and ensuring human rights for the employees lead better output in the production that increase firm performance (Dawkins and Lewis, 2003; Saleh et al., 2011). Russo and Fouts (1997) argue that those firms who follow environmental laws and regulations as part of their legal responsibility can improve their environmental as well as firm performance. Moreover, as part of CSR practice, firms provide quality products and invest in community development activities which has implications for long term firm performance (Waddock and Graves, 1997; Mahoney and Roberts, 2007). In addition, being a responsible employer by providing training and employment facilities a firm may also reduce

employee turnover and improve performance. These activities have direct influence on firm's market return, sales growth and profitability, thus, enhance firm's overall performance (Orlitzky et al., 2003; Bowman, 1978). Similarly, when firm's social engagement is properly presented and fit their stakeholders' expectations that actions lead to value creation and positive impact on firm performance. Hence, it is expected that,

H3: *Corporate Social Responsibility has positive impact on firm performance.*

Corporate Image as Mediator between CSR and Firm Performance

Academic scholars have empirically investigated the relationship between CSR and firm performance; however, came up with inconclusive findings (Berman et al., 1999; Galbreath and Shum, 2012). Recent literature explores some other variables, such as, corporate reputation or image can play a vital role in the link between CSR and firm performance (Galbreath and Shum, 2012; Jamali et al., 2008). Some researchers argue that CSR has strong impact on corporate image (Carmeli and Cohen, 2001; Gray and Balmer, 1998). CSR increases corporate image by creating positive customer perceptions. Many authors report that reputation has positive impact on firm market share, and market returns in terms of assets and equity (Galbreath, 2010b; Hammond and Slocum, 1996). The evidence of prior literature shows that CSR and corporate image both have positive effect on firm performance and the underlying arguments have extensively discussed in the previous sections. Hence, it can be hypothesized that,

H4: *Corporate image mediates the relationship between CSR and firm performance*

Research Framework

Based on the above discussion, the researchers propose a conceptual framework in order to guide the present research, presented in Figure 1. The proposed model exhibits the direct role of CSR and direct as well as mediated role of corporate image on firm performance.

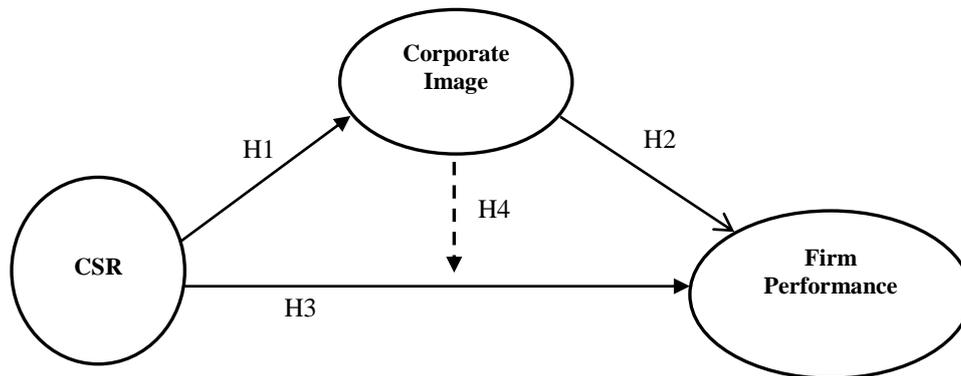


Figure 1: Proposed Research Framework

Methodology

Sample and Data Collection

Previous research predominantly used Kinder, Lydenberg and Domini (KLD) rating for CSR and related constructs, such as, corporate image measurement and KLD ratings (Nelling and Webb, 2009). A growing number of studies used content analysis for CSR measurement based on published annual reports data (Adams and Kuasirikun, 2000; Guthrie and Abeysekera, 2006) in spite of criticisms for validity and reliability of content analysis. CSR research connected to corporate image and firm performance also used secondary data sets and mainly focused on US samples (Galbreath and Shum, 2012). This study selects firms from a developing country, Bangladesh, where data sets and published annual reports, in many cases, do not exist. Therefore, a questionnaire administered survey approach has been chosen which seems appropriate in this situation (Lai et al., 2010) particularly where secondary data sets are unavailable. This study conducts a pilot survey with 25 managers and carried out an extensive literature search before preparing the final survey. Questionnaires were sent to the Managing Directors or Chief Executive Officer who has power to undertake strategic decision making for the business operations as well as CSR strategy. Initially 210 firms have been chosen using a list of companies of Bangladesh. The organisations are mainly classified as manufacturing or service oriented firm. The common

method bias and error is a challenging issue in survey method (Huse et al., 2011). Hence following the guidance of Podsakoff et al. (2003), several initiatives were taken to reduce the chance of common method bias in this research. After three rounds of follow up emails, and direct phone calls, 176 responses have been obtained and considering the logical elimination for unusable data, 125 responses found usable for this research.

This study adopted and used all measures for both independent and dependent variables from the existing literature. The questionnaire comprised three sections with each part separately evaluating organisation CSR practices, corporate image, and firm performance. All measures used 7-point Likert-type scale with the anchors “strongly disagree” rated 1 to “strongly agree” rated 7. The informants were asked to answer questions of each CSR dimensions and other related constructs.

This study adopted Deegan’s (2002) CSR conception which originally adopted from Hackston and Milne (1996). Based on the prior literature, Galbreath and Shum (2012) argue that universally accepted measurement of CSR is “neither available nor possible (p. 218)” though several authors used Carroll’s (1979) CSR conceptualisation such as economic, ethical, legal and discretionary responsibility. However, the Carroll’s (1979) conception does not directly confirm environment, energy and some other emerging factors which have been discussed in the contemporary CSR definition. The earlier studies predominantly used Fortune Most Admired companies as a measure of corporate image or reputation (Galbreath, 2010) which is mainly applicable to US contexts. However, in other developed and developing countries contexts such index does not exist. This study selects measurements for corporate image from Lai et al. (2010) and Galbreath and Shum (2012). These measures of image indicate the situations where organisations believe that customers are highly involved to build corporate image. Therefore, corporate image is assessed by four items adapted from the literature. Firm performance is measured by three items. Prior research widely used these items to measure firm’s performance (Saleh et al., 2011; Galbreath and Shum, 2012) though majority used data from annual reports.

Analysis and Results

Assessment of the Measurement Model

Figure 2 represents the results of Partial Least Square (PLS) analysis. This study used SmartPLS2.0 M3 to analyse the research model. The

measurement model of all constructs initially evaluated the adequacy of each multi-item scale. The Initial model consisted of 23 observed variables. This study measures internal consistency, reliability, convergent validity, and discriminant validity prior to testing the hypotheses. Referring to Igarria et al.'s (1995) and Hulland (1999) recommendation, this research considered 0.6 as the minimum cut-off level for each item. Following this rule, few items were eliminated. The revised model with 14 items was further tested using SmartPls2.0M3 (Ringle et al., 2005) and found all items exceeding cut-off value 0.6 (see Table 1). The results affirmed that all items are sufficient to represent their respective construct.

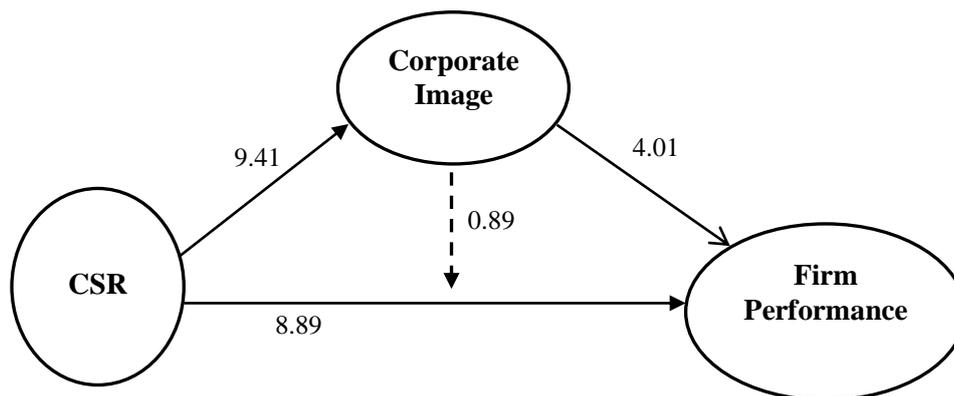


Figure2: Results of PLS analysis

To evaluate the internal consistency of the measures, Cronbach's alpha, composite scale reliability (CR) and average variance extracted (AVE) were calculated as suggested by Chin (1998) and Fornell and Larcker (1981). Table 1 represents that Cronbach's alpha for all measures exceeded the cut-off value indicating higher internal consistency. The composite reliability and average variance extracted for all measures exceeded the cut-off value (0.70 or more and 0.50 respectively), suggesting adequate reliability of the measures (see Table 1).

Table 1: Measurement Items and Validity Assessment

| Construct | Item | Factor Loading | (CR)* | Cronbach's alpha | AVE |
|------------------|--|----------------|-------|------------------|------|
| CSR | CSR1-Compliance with environmental laws and regulations. | 0.7731 | 0.89 | 0.81 | 0.61 |
| | CSR2- Use of recycled materials | 0.7685 | | | |
| | CSR3- waste management practices | 0.8666 | | | |
| | CSR4-Reduce energy consumption | 0.8842 | | | |
| | CSR5- Occupational health and safety policies | 0.8456 | | | |
| | CSR6- Sufficient wages for the workers. | 0.7328 | | | |
| | CSR7- Policies to support local community | 0.7663 | | | |
| | CSR8- Support sponsored campaigns | 0.7122 | | | |
| Corporate Image | CI1- Customers consider as professional | 0.8033 | 0.81 | 0.72 | 0.58 |
| | CI3- Overall positive customer perception | 0.7145 | | | |
| | CI4 – Highly reputed firm | 0.8110 | | | |
| Firm Performance | FP1- Good return on equity | 0.7130 | 0.86 | 0.74 | 0.59 |
| | FP2- Positive return on assets | 0.8046 | | | |
| | FP3- CSR enhances profitability | 0.8127 | | | |

*CR= Composite reliability

Assessment of the discriminant validity of the measures was the next step to measurement validation. A construct should share more variance with its measures than with other constructs in the model (Barclay et al., 1995; Chin, 1998). The square root of the AVE should exceed the inter-correlations of the construct with the other constructs in the model (Fornell and Larcker, 1981). Table 2 represents discriminant validity of the constructs of CSR, and corporate image (CI) where the square root of the AVE exceeds the inter-correlations of the constructs with the other constructs in the model (Henseler et al., 2009). Cross loadings of the items were also inspected to find out additional support for discriminant validity (Chin, 1998). Finally, it can be concluded that the results exhibited satisfactory discriminant validity of the model.

Table 2: Discriminant Validity

| | CSR | Corporate Image | Firm Performance |
|------------------|---------------|-----------------|------------------|
| CSR | 0.718* | | |
| Corporate Image | 0.516 | 0.795 | |
| Firm Performance | 0.628 | 0.731 | 0.806 |

*Note: Bold figures on the diagonal are the square root of the AVE.

Assessment of the Structural Model

A bootstrapping procedure was used to test the statistical significance of the model as well as the hypothesized relationships (Chin, 1998; Ringle et al., 2005). The results of the structural model indicate that all but one (indirect effect between CSR and FP) proposed relationships received strong support and all of the proposed hypotheses are confirmed except one. The results exhibit a strong positive effect of CSR on corporate image ($\beta = 0.61$, $t = 9.41$, $p < 0.01$), which also support H1. Moreover, the direct effects of corporate image on FP ($\beta = 0.40$, $t = 4.01$, $p < 0.01$) are also significant and support H2. The results of the structural model, detailing the path coefficients and t-statistics are presented in Table 3. The nomological validity or explanatory power of the model can be observed through assessing R^2 values of the endogenous constructs. Based on the R^2 -value it can be inferred that the model explains 52% of the variance of the model. The generated R^2 value of firm performance is moderate, which is acceptable for an endogenous latent variable with only a few exogenous latent variables (Henseler et al., 2009).

Table 3: Structural Properties of the Constructs

| Hypothesis | Relationship | Coefficient (β) | t-value | Result |
|------------|--|-------------------------|---------|---------------|
| H1 | CSR \rightarrow Corporate Image (CI) | 0.61 | 9.41 | Supported |
| H2 | CI \rightarrow Firm Performance (FP) | 0.40 | 4.01 | Supported |
| H3 | CSR \rightarrow FP (Direct Effect) | 0.69 | 8.89 | Supported |
| H4 | CSR \rightarrow FP (With mediators) | 0.12 | 0.89 | Not-supported |
| | Endogenous Construct | Model | | |
| R^2 | CI | 0.48 | | |
| | FP | 0.52 | | |

Mediating Effect of Corporate Image

This study suggests corporate image as mediator between CSR and firm's performance. This conception refers that, CSR positively effects corporate image which eventually lead to better performance. This study followed the procedure proposed by Baron and Kenny (1986) to test the mediating effect. If the indirect effect of CSR on FP is significant as compared to the direct effect of CSR on FP, this will support to establish the significant role of corporate image in implementing CSR. At the outset, the relationship between CSR and firm performance is assessed. The relationship between CSR (independent variable) and FP (dependent variable) is significant ($\beta = 0.69$, $t = 8.89$, $p < 0.01$). After the inclusion of mediators the model is further assessed with all paths estimated to test

mediation effects. The results (Table 3) indicate that the significant relationship (assessed earlier without including mediators) between CSR and FP becomes insignificant ($\beta = 0.12$, $t = 0.89$, $p < 0.01$), exhibiting existence of full mediation (e.g., Baron and Kenny, 1986). Hence, the final model argues that CSR is positively associated with firm performance however, the effect is indirect. The results also demonstrate that CSR is significantly associated with corporate image which eventually fully mediate the relationship between CSR and firm performance.

Discussion and Implications

This study examines the mediating effect of corporate image on the relationship between CSR and firm performance. The empirical findings support all the hypotheses except the indirect link between CSR and firm performance. Without the existence of corporate image the link between CSR and performance is positive and significant whereas with the inclusion of mediating variable the link has become insignificant demonstrating the full mediating (e.g., Baron and Kenny, 1986) role of corporate image on the link. The result exhibits that CSR builds strong corporate image through socially responsible business operation which ultimately create a positive impression to the stakeholders as well as firm performance (Galbreath and Shum, 2012). Few studies have investigated the link between CSR and performance considering some mediating variables like customer satisfaction, employee turnover, and image. However, corporate image as a mediator has largely being ignored in prior studies. Thus, this study filled this gap by showing the importance of corporate image in improving firm performance.

This study suggests that CSR has effect on corporate image that indirectly lead to better performance. Legitimacy theory argues that failure to legitimise within the community where firms operate might risk their operation in a particular society. The results indicate that firms seek to build good corporate image in the society for their existence. The findings of this study provides empirical support of the prior studies in developing countries by Belal and Owen (2007) and Islam and Deegan (2008) who argue that CSR is a tool for legitimisation of corporate social and environmental friendly activities.

Implications

This study opens the window to clear the confusion and finds that there are some other intervening variables like corporate image which play a mediating role in the relationship between CSR and performance. CSR and corporate image is interlinked in the literature and able to provide competitive advantage for the organisations through customer satisfaction, employee satisfaction, reduce employee turnover and developing brand equity etc. (Galbreath 2010; Lai et al, 2010) that creates brand value and increase corporate image. In this regard, Jeremy and Shum (2012) assert that corporate image has positive influence on firm performance. The findings of the current study are also in line with the conceptualization of Jeremy and Shum, (2012) where they argued that corporate image helps organisation in acquiring more customers because of their interconnectivity which in turns result in achieving firm's performance. The findings suggest that managers should conceptualise and practice CSR along with other associated variables that facilitate firms' performance.

Conclusion

Despite the inconsistent findings of CSR on firm performance, there has been limited empirical evidence that investigate the mediating role of corporate image on the relationship between CSR and firm performance. Hence, this study examines the direct and mediating role of corporate image on firm performance to fill this gap in the literature. A questionnaire administered survey method has been employed to collect the data from 125 respondents from different industries. Structural Equation Modelling (SEM), with the help of SmartPLS 2.0 software has been used to validate the proposed model and to test the hypotheses. Results confirm that CSR has positive influence on firm performance which is also in line with the conception of legitimacy theory. Results also reveal that CSR has positive effect on performance via corporate image which ultimately supports the mediating role of corporate image. Hence, firms voluntarily need to undertake CSR activities to satisfy the stakeholder's social and environmental concerns which eventually helps them developing corporate image. The CSR activities of an organisation also need to legitimate their operations in the society in order to ensure long-term sustainability of the firm.

Limitations and Future Research Direction

Similar to prior academic studies, this study is also not free from limitations. Conceptualization and measurement of CSR is an issue of considerable debate and this study followed conceptualization of CSR proposed by Deegan (2002) adopted from Hackston and Milne (1996). Therefore, CSR dimensions proposed by other researchers and independent standard setters such as GRI could be taken into consideration. This study has drawn a sample from a developing country, Bangladesh and thus generalizability of the results may not be possible because of the contextual dissimilarities. Future research could be carried out in other developing or emerging countries which have similar socio-cultural context.

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