

**THE EFFECTS OF CORPORATE SOCIAL RESPONSIBILITY
ON THE FINANCIAL PERFORMANCE OF LISTED
COMPANIES IN THE UK**

Submitted by Graham Paul Buckingham, to the University of Exeter as a thesis for the degree of Doctor of Philosophy in finance, October 2012.

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ABSTRACT

This thesis is an examination of the financial consequences of corporations engaging in socially responsible activities. It is motivated by the recognition that a socially responsible approach can fundamentally change the conduct and operation of business, which in turn may have a significant impact on financial outcomes both for individual companies as well as the wider economy. If social responsibility improves financial performance then managers, investors and society at large can have confidence that these activities increase prosperity as well as social welfare, making them unequivocally desirable.

Four empirical studies were undertaken of different but related financial aspects of corporate social responsibility (CSR), specifically; the determinants of social responsibility and the effect of social responsibility on profitability, market value and stock return.

In chapter two corporate social responsibility was found to be consistently and positively related to company size and certain industry characteristics, in particular companies that deal directly with the public (rather than with other companies) and companies in extractive and regulated industries were associated with a greater engagement in CSR. Although in some instances a positive link was found between return on assets and subsequent levels of corporate social responsibility the results were not consistent suggesting that higher than average profitability is not a prerequisite or consistent spur to additional social responsibility. A new methodology was also deployed, system GMM as another way of assessing the corporate social responsibility / corporate financial performance relationship; this gave broadly similar results.

Chapter three assessed the relationship between social responsibility and responsibility on profitability. There was a positive significant association with return on assets but generally insignificant results when return on sales was used as the measure of financial performance. This may indicate that social responsibility is materially associated with a better utilisation of the internal assets used by a business but that this does not extend to obtaining better margins from external customers. Alternatively it may indicate that CSR has no consistent unambiguous effect on financial results or finally that it is difficult to witness an effect by using a cross sectional approach. To more directly assess if social responsibility has an impact on financial performance a time series analysis was also carried out, no significant result was found. However given the degree of inertia in corporate social responsibility the five years of data available is unlikely to be a sufficiently long to detect any effect.

Chapter four contains a study of the effect of corporate social responsibility on market value. This uses value relevance methodology which is a relatively new approach and has the advantage of both

directly addressing the principal concern of critics of CSR, that it impairs shareholder wealth. On average corporate social responsibility was found to be associated with higher market value and by implication a better level of profit and/or lower levels of risk.

The final empirical study in chapter five examined the role of corporate social responsibility and risk as a way of parsing the result in the previous chapter and assessing whether investor cash flow or risk was the cause of enhanced market valuations. This also has the advantage of directly looking at stock returns which is a prime concern of ethical investors. Three different methodologies were used; in each case the effect noted was small and generally not significant, suggesting that social responsibility has little discernible effect on risk and hence stock return in the UK.

Overall it appears that corporate social responsibility is associated with greater market value but that no consistent unambiguous significant association between corporate social responsibility and profitability could be found using a cross sectional study. The methodologies used in the various chapters are quite different and there are also obvious differences between market value and profitability, however a more consistent result should be expected. When more extensive data sets become available a longer run time series analysis should provide additional information on the effect of corporate social responsibility on financial performance and provide a useful adjunct to this study.

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