EFFECT OF CORPORATE SOCIAL RESPONSIBILITY ON FINANCIAL PERFORMANCE OF FIRMS LISTED IN NAIROBI STOCK EXCHANGE.

MAINA ALICE MUTHONI

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DEDAN KIMATHI UNIVERSITY OF TECHNOLOGY

A Thesis Submitted to the School of Business Management and Economics in Partial Fulfillment for the Award of Degree of Masters of Business Administration of Dedan Kimathi University of Technology

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DECLARATION

This research project is my original work and has not been presented for award of a degree in any other university.

Maina Alice Muthoni

B211/1592/2011

Signature…………………………….. **Date………………………………………**

This research project has been submitted for examination with our approval as University supervisors.

Signature…………………………….. **Date………………………………………**

Dr. George K. Riro

Finance & Accounting Department

Dedan Kimathi University of Technology.

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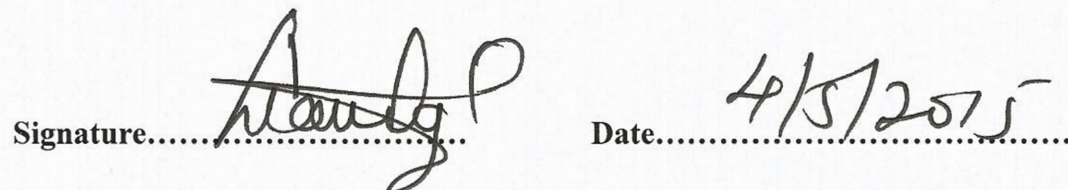

Signature…………………………….. **Date………………………………………**

Dr. David N. Kiragu

Finance & Accounting Department

Dedan Kimathi University of Technology.

DEDICATION

My dedication goes to my loving husband Charles, our children Maggie and Kevin for their support and encouragement. May it inspire them to pursue education to the highest level.

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I would like to acknowledge the Almighty God for his blessings and strength in the undertaking of my study. I humbly appreciate the University for enabling me to further my studies. I would like to extend my gratitude to my lecturers for their continued support in the course of my study. I also appreciate the assistance given to me by my supervisors Dr.Riro and Dr.Kiragu for the support and my fellow colleagues at the institution. May God bless you.

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LIST OF ABBREVIATIONS AND ACRONYMS

CSP - Corporate Social Performance

CSR – Corporate Social Responsibility

FP – Financial Performance

ROK – Republic of Kenya

NSE – Nairobi Stock Exchange

ROA - Return on Assets

ROE - Return on Equity

SPSS – Statistical Package for Social Science

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ABSTRACT

Corporate social responsibility (CSR) has emerged as an important aspect in the global business community and has become a mainstream activity. The purpose of this study was to assess the effect corporate social responsibility has on a financial performance of a firm. The main objective of the study was to assess the effects of CSR on financial performance of firms in Kenya. The specific objective of the study was to assess the effects of CSR on profitability, Liquidity and efficiency of firms in Kenya. The theories guiding the study were stakeholders theory, slack resources theory and Virtous Circle theory. These theories are relevant to this study because they address the various angles from which corporate social responsibility could affect financial performance. Employing a descriptive survey research design, the study targeted public companies which had established foundations within their corporate social responsibility policy. Using Purposive sampling the study selected six companies and used all of them to enable the researcher control the variables "size" and "industry" of the company which have been shown to intervene in the relationship between CSR and Financial performance. Annual financial reports were used to get particulars about a company's CSR spending and the resulting financial performance in terms of returns. Descriptive and inferential statistics was employed in data analysis. Descriptive statistics involved frequency distributions and means. Bivariate linear regression model was used to establish the relationship between CSR and profitability. The study found that there was no significant relationship between CSR and liquidity of firms in any of the six participating firms. The findings also showed that there was no relationship between CSR and firm efficiency in majority participating firms. The researcher concluded that corporate social responsibilities in Kenyan firms with foundations have more effect on profitability than liquidity and efficiency. The researcher recommended that firms with foundations should focus on investing their CSR funds to solve problems that have a widespread effect.

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CHAPTER ONE

INTRODUCTION

1.1 Background to the study

Corporate social responsibility (CSR) is an important management tool today. Corporate social responsibility has emerged as a significant theme in the global business community and has become a mainstream activity. The European Commission defines CSR as a concept whereby companies decide voluntarily to contribute to a better society and a cleaner environment (Simms 2002). Adams and Zutshi (2004) define it as the integration of business operations and values whereby the interest of all stakeholders including customers, employees, investors and the environment are reflected in an organization's actions and policies. The Three Concentric Approach encompasses CSR as a model with three specific levels: The first circle involves financial performance, in particular, growth and productivity. The second circle focuses on these financial items and awareness of the society a firm interacts with. The final circle involves the care and improvement of the environment that a firm operates in (Carroll 1991).

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The perception of CSR as a means of enhancing both social and financial performance is known in the literature as the business case for CSR. The business case is not a new approach to CSR as for many years the management literature maintained that managers could help their companies to discover win-win opportunities that improve their social and environmental performance while simultaneously increasing profits (Hart, 1995). Even in early CSR initiatives, there was always the premise that by adopting CSR

practices firms would enhance the social environment in which they operated and that such efforts would be in their long-term financial interest (Carroll & Shabana, 2010).

Of late, a new concept called corporate social performance has gained recognition. Wood (1991) defines Corporate social performance (CSP) as the extent to which a company is successfully able to implement the interests of its stakeholders, in the economic, social and environmental domain in its business operations, and the extent to which a company is successfully able to implement actions aimed at guaranteeing the continued existence at least at an equal level, of the company, society and the environment at large.

In the past, governments have relied on legislation and regulation to deliver social and environmental objectives in the business sector. According to Carroll and Shabana (2010) CSR is treated as a private institutional alternative to government regulation, and the choice between these two options depends on their relative costs and benefits. Government has the power to enforce regulation. But government regulation isn't perfect, and it can even end up reducing public welfare because of its cost or inefficiency (Simms 2002). The government also may lack the resources and competence to design and administer appropriate regulations, particularly for complex industries requiring much specialized knowledge. Simms (2002) opined that industry groups might find ways to influence regulation to the point where it is ineffective or even ends up benefiting the industry at the expense of the general population.

Margolis and Walsh (2007) attempted to relate corporate social responsibility and corporate social performance. In the relation between CSP and CFP, the authors defined CSP in two ways: as a multidimensional construct that is either constructed by examining

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companies' efforts of living up to multiple responsibilities, or by looking at a company's principles, processes, practices and outcomes or as a function of how stakeholders are treated by a company. Efforts have been made to discriminate between the concepts of CSR and CSP, however in literature these concepts are often used interchangeably

Corporate financial performance (CFP) refers to the financial outcomes of business operations. Corporate performance refers to the outcomes of management processes in relation to the goals that were set (Simms, 2002). It is the ability of the organization to use its resources efficiently and effective in order to reach those goals. Corporate performance can be divided into two categories: operational performance and financial performance. Operational performance contains measurements like market share, marketing effectiveness and product quality. Financial performance can be split up, once more, into market-based performance and accounting based performance. The first referring to, for example, earnings per share and stock prices, the latter includes return on assets and return on equity (Fauzi *et. al.*,, 2010).

Organizations require implementing partners for their CSR programs since the activities are often not within the company's core competence. Many organizations such as the Kenya Commercial Bank (KCB), Safaricom and the East African Breweries have formed foundations to help them implement their respective CSR programs. Not all organizations may have the resources to set up foundations and in any case, successful CSR programs essentially have to have community implementing partners (Infotrack, 2012).

Nyangongo (2012) studied the CSR practice and its role in the profitabi1ity of selected organizations namely Barclays Bank, National Bank, Kenya Commercial Bank, British

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American Tobacco and African Wildlife Foundation. Findings from the study indicated that CSR was a major contributor to the profitability of organizations through enhanced image and reputation. Further the quality performance was vital in improving reputation with customers. The research also found out that these organizations had strategic partners in their CSR agenda. However, the greatest impediments to CSR practices were finances and poor public perception.

Rutto (2003) investigated the influence of corporate social responsibility reporting on the financial performance of listed companies at Nairobi securities exchange. The findings showed that the impact of the influence of CSR reporting on companies listed in the NSE had differential effects on factors of financial performance. It was associated with increased customer motivation, increased sales, employee morale, enhancing organization's reputation and reduced crisis incidences among others. The findings further provide some evidence of the possibility that CSR reporting among the limited companies represent attempts by companies to improve their corporate image and to be seen as responsible corporate citizens.

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Kirwa (2013) investigated the effects of corporate social responsibility on the performance of firms operating within the financial sector. Postbank which is the only pure savings bank in the country was selected for purpose of the study. Findings indicated that CSR activities have a higher effect on the performance of the bank as performance focused on image, profitability, customer satisfaction, employee satisfaction, costs and risk profile of the organization. Given that the market place has become competitive and players in the industry compete for customers with an intention

of increasing the deposits level, the findings indicated that CSR may be considered a differentiation strategy by the bank.

1.2 Statement of the problem

Kenyan Companies have taken to CSR with gusto in the recent past improving staff welfare and work environment, embracing transparency and accountability in their business transactions, self-regulation and implementing community development programs. However, it is the community component that is highly visible to most people and gives companies the much sought after enviable public image. Companies have been involved in various activities in sports, environment, health, education and training, the needy in society and even national leadership and governance.

The effect of CSR initiatives is of interest to managers and scholars alike. However, here in Kenya, little empirical data exists on the impact of CSR on financial performance. None of the reviewed studies incorporated the aspect of philanthropic oriented foundations and as such a knowledge gap exists which this study sought to fill by evaluating the effect of corporate social responsibility on financial performance of firms with philanthropic oriented foundations in Kenya.

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1.3 Purpose of the study

The purpose of this study was to assess the effect of corporate social responsibility on financial performance of firms with philanthropic oriented foundations in Kenya.

1.4 Specific Objectives of the study

The study was guided by the following specific objectives:

(i) To determine the effect of CSR on profitability of firms in Kenya.

(ii) To assess the effect of CSR on liquidity of firms in Kenya.

(iii) To evaluate the influence of CSR on efficiency of firms in Kenya.

1.5 Research questions

(i) What is the effect of CSR on profitability of firms in Kenya?

(ii) What is the effect of CSR on liquidity of firms in Kenya?

(iii) What is the influence of CSR on efficiency of firms in Kenya?

1.6 Justification of the study

Research suggests that CSR can produce positive outcomes for a company; however, there is little understanding of this relationship in the Kenyan Corporate world. Economic development and improved standards of living can come about through well implemented CSR initiatives. It is important to understand the effect CSR has on the financial performance of an institution so as to improve a company's capacity.

1.7 Significance of the study

The findings of this study will be of invaluable importance to the management of various companies about the benefits or lack thereof that CSR has to their business in regard to financial performance. The findings can also assist the government through the ministry of trade on the incentives it can give to companies to enable them implement CSR initiatives that are both beneficial to the community and the community itself. Researchers and scholars can use the findings generated by this study in their works.

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1.8 Scope of the study

The study was carried out in the context of Kenyan companies listed in the Nairobi stock exchange. The study was interested in those companies that have philanthropic oriented foundations as part of their CSR strategy or policy. The study sought to establish the impact of activities involved in CSR have on the financial performance of the company in terms of revenue and profit/loss margin.

1.9 Limitations of the study

In carrying out the research the researcher encountered the following limitations: Since the study relied on secondary data, the study was limited to the information made public by the participating companies. To avoid this limitation interfering with the purpose of this study, the researcher used information that public companies are expected to report by law such as return on equity and return on assets. The study was also limited to the three weeks in which the data collection and analysis took place; to mitigate this, the researcher hired the services of a research assistant to assist in data management.

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1.10 Assumptions of the study

The researcher made the following assumptions:

i. That the returns made public by the companies are truthful

ii. That no other factors apart from the ones identified affect the relationship under investigation

1.11 Definition of terms

Corporate social responsibility: In this study, CSR refers to activities of foundations owned by companies whose function is mainly giving back to the community (Carroll and Shabana ,2010).

Efficiency refers to ratio between the input to run a business operation and the output gained from the business. (Becchetti and Trovato ,2011).

Financial performance: Return on sales/investment. (Fauzi *et. al.,*, 2010).

Foundation: A non-governmental entity that is established as a nonprofit corporation or a charitable trust, with a principal purpose of making grants to unrelated organizations, institutions, or individuals for scientific, educational, cultural, religious, or other charitable purposes (Cho, Lee & Pfeiffer, 2012).

Liquidity refers to ability to convert an asset to cash quickly (Zygmunt ,2010).

1.12 Organization of the study

The study consists of five chapters. Chapter one consists of background of the study, statement of the problem, research objectives, research questions, significance of the study, limitations of the study, assumptions of the study and definitions of significant terms. Chapter two consists of related literature that analyses the impact of CSR activities on financial performance, theoretical framework and the conceptual framework. Chapter three explains the methodology of the study, while Chapter four presents an analysis of the findings. Chapter five presents the summary, conclusion and recommendations of the study

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CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

This chapter presents a synthesis of available literature on the relationship between corporate social responsibility and financial performance. The researcher reviews existing theories in the theoretical framework and proceeds to highlight findings and conclusions of similar studies in the empirical review. The researcher summarizes the findings and conclusions of these studies and identifies gaps to be filled by this study. A conceptual framework is also presented.

2.2 Theoretical framework

There are three different theoretical concepts of the relation between corporate social responsibilities and financial performance namely stakeholder theory, slack resources theory and the virtuous circle concept.

2.2.1 The Stakeholders theory

The stakeholder theory was proposed by Edward Freeman in 1984 in his publication entitled Strategic Management. Freeman argued that business relationships should include all those who may "affect or be affected by" a corporation (Clarkson, 1995). By identifying stakeholders, analyzing relationships with them and evaluating these relationships, firms are able to successfully operate in their public and strategic environments. The analysis and evaluation of stakeholder relationships enables firms to determine which parties deserve or require attention from management, resulting in

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optimization of relationships and preservation of corporate legitimacy (Doh & Guay, 2006). Jones (1995) put forward an operationalization of stakeholder theory that could offer instrumental value to management. In his instrumental stakeholder theory, he argues that firms that work on the basis of honest, trusting and ethical relationships will be rewarded by stakeholders in terms of positive reputation effects, making these firms suitable business partners. Applying this theory to CSR, Jones suggests that corporate responsible behavior corresponds to attempts to build honest, trusting and ethical relationships. By extension, firms that are high in CSP should benefit financially from their positive interaction with stakeholders. Paying attention to the domains of CSR improves the relations with the stakeholders that were identified, ultimately resulting in better overall performance (Waddock and Graves, 1997).

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2.2.2 The slack resources Theory

The slack resources theory postulates that the level of resources that management devotes to CSR activities is driven by the accessibility of resources not required for other purposes. This concept is perhaps best articulated in Jensen (1986) who suggested that management faced with holding cash in excess of their needs are likely to invest this free cash in a way that is at variance with maximizing the value of the firm. Slack resources theorists argue that firms with better financial performance will have resources available to invest in CSR. Since these resources, financial and other, are necessary to improve CSP, a link between the two is expected. In this line of reasoning, better CFP will result in better CSP (Waddock and Graves, 1997). In other words: all firms may want to excel in CSR but only those with sufficient resources will find themselves performing well.

2.2.3 The Virtous Circle Theory

The virtuous circle theory as the name suggests that CSR is a predictor of financial performance as well as a result of the same. Put forward by Waddock and Graves (1997) the theory suggests that companies that have slack resources at their disposal, and allocate these resources in the social domain, are expected to increase CSP. Here, an increase in financial performance is a predictor of an increase in social performance. Based on good management theory, the authors expect a similar, positive relationship in the other causal direction: CSP is a predictor of CFP. The mechanism at work is stakeholder relationships. Investments in the social domain are expected to result in improved relationships, resulting in overall better performance.

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2.3 Empirical Review

The relationship between corporate social responsibility and corporate financial performance has been studied intensively with mixed results. In a survey of 95 empirical studies conducted between 1972-2001, Margolis and Walsh (2001) reported that when treated as an independent variable, corporate social performance is found to have a positive relationship to financial performance in 42 studies (53%), no relationship in 19 studies (24%), a negative relationship in 4 studies (5%), and a mixed relationship in 15 studies (19%). Of the 51 studies carried out between 1970 and 1995, 33 found a positive relationship, 9 found a negative relationship and 9 found no relationship between CSR and financial performance (Chand 2006).

This section presents the findings and conclusions of similar studies carried out across the world. The studies are grouped into two sections: those that found a positive relationship and those that found a negative relationship.

2.3.1 Effects of CSR on Profitability.

Margolis *et. al.,* (2007) reviewed 167 studies that satisfied two conditions: CSP and CFP were measured on the firm level, and an effect size for the association between CSP and CFP was provided. The analysis resulted in finding a positive relationship between CSP and CFP. Based on their results, Margolis *et. al.,* (2007) concluded that the financial impact of CSP is, at the least, neutral. This conclusion contradicts the concerns of those theorizing about a negative relationship (e.g. Friedman, 1970). Only in 2 percent of the analyzed studies a significant negative association was detected. However, the small effect size indicates that, although CSP is not detrimental for CFP, it is not very beneficial to CFP either (Wissink, 2012).

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Spicer (1978) found a positive correlation between a firm's economic performance and its level of pollution control in the paper and pulp industry. He found that the higher the level of pollution control the greater the profitability and size of the firm and the lower the systematic and total risk. He also concluded that the benefits seen were short lived.

Anderson and Frankle (1980) used a firm's market value to measure financial performance and its relationship with CSR. A positive relationship between market value and CSR was found. This meant that investors were investing more in firms who reported CSR than those who did not. This provides some evidence of the existence of the 'ethical investors.'

Cochran and Wood (1984) examined the relationship between CSR and corporate financial performance (CFP).They found that asset age was highly correlated to levels of CSR and that there was a positive relationship between CSR and CFP when asset age was removed. This extra variable added a new element to Cochran and Wood's empirical research and it provided a possible insight into a variable that may be causing conflicting conclusions by various researchers.

Griffin and Mahon (1997) looked at the chemical industry and found that high CSR was linked to high CFP and that low amounts of CSR reporting was linked to lower CFP. Joyner and Payne (2002) also found a positive correlation between reporting CSR with performance and firm value. Joyner and Payne noted the difficulty of measuring the benefits of CSR. The authors also saw some indication of a time lag between when CSR was reported and the financial benefits seen. These findings conflict with the results of Spicer (1978) who found that the financial benefits were short lived.

O'Bannon and Preston (1997) expect a negative relationship from CFP to CSP. This is expected because managers pursue private goals, for instance benefitting from remuneration schemes, which are linked to short-term financial performance. These managers are less likely to invest in CSR because these investments will not pay off in the short-term and would endanger manager compensation. The temptation here, and the link between CFP and CSP, is cashing in by reducing CSR investments. A second reason for the negative association is that when managers are faced with poor financial performance they may want to disguise or justify this performance by means of excessive investments in CSR. Goss and Roberts (2009) reason in a similar way: managers that want to polish their reputations may do so at the expense of shareholders. Both

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management actions may explain why negative financial performance may result in improved attention to the social domain.

Vance (1975) found a negative relationship between CSR and financial performance. He looked at share price and found that in building a portfolio an investor would be better off investing in companies who reported little or no CSR. He concluded that companies have more reasons to be socially responsible than only how it affects the per share value of their common stock.

Shane and Spicer (1983) also found a negative relationship between the level of social disclosures and economic returns. This is a direct contrast to Spicer's 1978 paper which found a significant positive relationship. The explanation that Shane and Spicer (1983) provided for the negative results is that investors are put off by CSR.

Riahi-Belkaoui (1992) found a negative relationship between external perceptions of a company's CSR activities and executive compensation schemes. His findings suggest that top management may be discouraged from undertaking CSR activities. This is due to the fact that the shareholders do not appreciate their profits being spent on activities they do not consider beneficial to them.

Fry and Hock looked at members of the oil industry such as Texaco and concluded that the amount of CSR did not increase or decrease the profitability of the firm. Fry and Hock put any change in financial performance down to an increase in firm size. Their concluding comments also suggest that the firm's size and public image management also determine the amount of CSR reporting undertaken. The industry a firm operates in may have a strong effect on the results that are found when examining the relationship

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between CSR and financial performance. Firm size is possibly a problematic variable that must be controlled (Fry and Hock ,1976).

Alexander and Buchholz (1978) examined the relationship between the level of CSR and stock market performance, and also stock level risk. The study did not find any significant relationship between CSR and either of these two variables. One possible explanation for this is that the market is efficient and thus any 'positive news' will change the share price instantly rather than over a period of time. If the changes to the stock price had occurred instantly, this research didn't provide any insight into whether or not CSR impacted stock market performance.

Aupperle *et. al.,* (1985) carried out a survey using a specially designed survey instrument that they created to minimize the effects of bias in their respondents' answers. To measure financial performance the researchers used both long-term and short-term return on assets. No relationship was found between the variables, CSR and financial performance, suggesting the effect CSR has on profitability is neutral and by reporting CSR profits are neither increased nor decreased (Aupperele *et. al.* 1985,).

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2.3.2 Effect Of CSR On Liquidity

The liquidity of an asset means how quickly it can be transformed into cash. When referring to company liquidity one usually means its ability to meet its current liabilities and is usually measured by different financial ratios (Lanka, 2013). According to Zygmunt (2010), The liquidity is essential for company existence. It principally has an effect on financial costs reduction or growth, changes in the sales dynamic, as well as it influences on company risk level. The decisive significance of liquidity means that it

is important for company development and at the same time is one of the fundamental endogenous factors which are responsible for company market position.

Few studies have been carried out on the effect of CSR on liquidity. Subramaniam, Samuel and Mahenthiran (2014) sought to examine the liquidity implication of voluntary Corporate Social Responsibility (CSR) reporting from the perspective of the Malaysian Capital Market. The findings that the greater the level of CSR disclosures the higher the liquidity, particularly in terms of the price impact. According to the authors, While the increased CSR disclosures convey information about nonfinancial risks, the increased in institutional ownership and their price discovery activities reduce the risk by lowering the spread. This study sought to add to the body of knowledge by assessing the effect of CSR on liquidity of firms in Kenya.

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2.3.3 Effect Of CSR On Efficiency

In a business context, operational efficiency can be defined as the ratio between the input to run a business operation and the output gained from the business. When improving operational efficiency, the output to input ratio improves (Coelli *et al.,* 2005). Inputs would typically be money (cost), people (headcount) or time/effort. Outputs would typically be money (revenue, margin, cash), new customers, customer loyalty, market differentiation, headcount productivity, innovation, quality, speed & agility, complexity or opportunities. The efficiency ratio, a ratio that typically applies to banks, in simple terms is defined as expenses as a percentage of revenue (expenses / revenue), with a few variations. A lower percentage is better since that means expenses are low and earnings are high. It relates to operating leverage, which measures the ratio between fixed costs and variable costs.

The nexus between corporate social responsibility and corporate performance is of fundamental importance to understand if the former can be a sustainable strategy in the competitive race. Becchetti and Trovato (2011) examined the relationship on a sample of firms observed in a 13-year interval by focusing on a performance indicator (productive efficiency). Findings showed that firms included in the Domini 400 index (a CSR stock market index) do not appear to be more distant from the production frontier than firms in the control sample after controlling for the heterogeneity of production structure.

In evaluating the relationship between corporate social responsibility and stock market efficiency, Becchettiy, Cicirettiz and Giovannellix (2009) found that net difference between CSR strengths and weaknesses significantly reduces both the absolute forecast error on EPS and its standard deviation after controlling for standard regressors plus year, industry, and firm/broker effects. their findings are consistent with the hypothesis that reduced transaction costs (and conflicts) with stakeholders and more transparent accounting practices implied by CSR significantly affect the bias. The CSR effect is strongly asymmetric and mainly driven by CSR weaknesses, consistent with the fact that the predicted channels of influence are mainly captured by CSR weakness scores. A crucial aspect of their findings is that CSR contributes to make financial markets efficient as unbiasedness and efficiency are (in almost all specifications) not violated in the subsample of the top 20 percent (lowest CSR weaknesses) companies, while they are in the bottom 20 percent CSR companies.

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2.4 Research Gaps

There have been a number of researchers investigating the relationship between Corporate Social responsibility and financial performance. The results have been inclusive. A number of papers found positive relationships. Margolis *et. al.,* (2007), Spicer (1978), Anderson and Frankle (1980)) while others found negative relationships (O'Bannon and Preston (1997), Goss and Roberts (2009), Vance (1975)} or no relationships (Fry and Hock (1976), Alexander and Buchholz (1978) and Aupperle *et. al.,* (1985)) between the variables at all.

A review of the of the studies suggested that the industry in which a firm operated in determined the direction of the relationship between CSR and financial performance as seen in the Spicer (1978) study. There was a significant difference in the CSR scores across the two industries. This demonstrated the importance of controlling the industry variable when researching the CSR and financial performance relationship. A significant positive relationship was found between CSR and financial performance for firms inside the production industry but not inside the service industry.

Another intervening variable that emerged in the relationship between CSR and financial performance was the role of the managers as seen in O'Bannon and Preston's study. These managers are less likely to invest in CSR because these investments will not pay off in the short-term and would endanger manager compensation.

As much as the findings of these studies are inclusive, it is worthy to note that a host of them were carried out in Europe and the Americas among giant corporations. Significant cultural, social and economic differences exist between these parts of the world and

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Kenya. Therefore, the findings of the studies from the western world cannot be wholly replicated in the Kenyan context. Not much research has been carried out on the relationship between CSR and financial performance of Kenyan Companies. There exists knowledge gap which this study intends to fill.

2.5 Conceptual Framework

A conceptual framework is proposed for the study. The framework shows how the different variables in the study interact. Robson (2011) defined a conceptual framework as a visual or written product, one that explains, either graphically or in narrative form, the main things to be studied; the key factors, concepts, or variables and the presumed relationships among them. Shields, Patricia and Rangarjan (2013) define a conceptual framework as the way ideas are organized to achieve a research project's purpose.

The CSR in this case is the input which influences the output that is; the financial performance. The conceptual framework is important in clarifying concepts and propose relationships among the concepts in a study.

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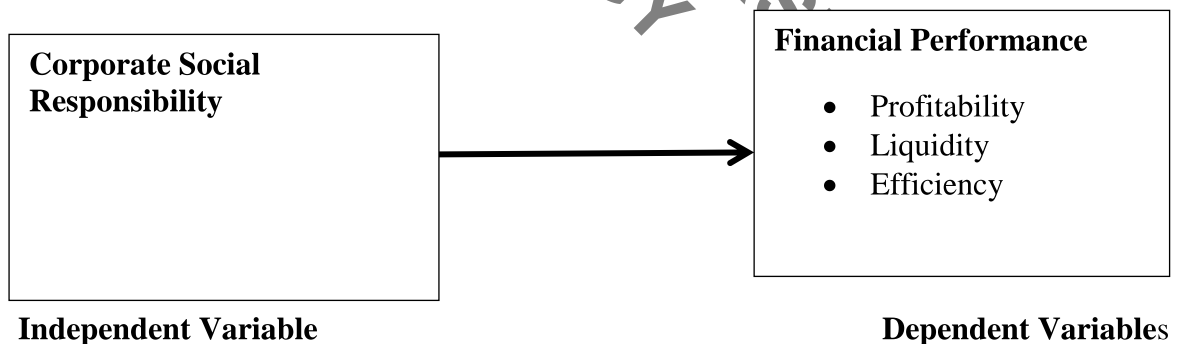

Figure 1: Conceptual framework of effects of CSR on financial performance of firms in Kenya

2.6 Operational framework

Operational framework is defined as the elements that underly how ideas work together as a whole (Shields, Patricia & Rangarjan, 2013). Operationalizing a variable means finding a measurable, quantifiable and valid index for the variable and finding a way to manipulate that variable in such a way as to have two or more levels (Jonker & Pennink, 2010). Burns (2010) adds that the process of operationalization defines fuzzy concepts and allows them to be measured, empirically and quantitatively.

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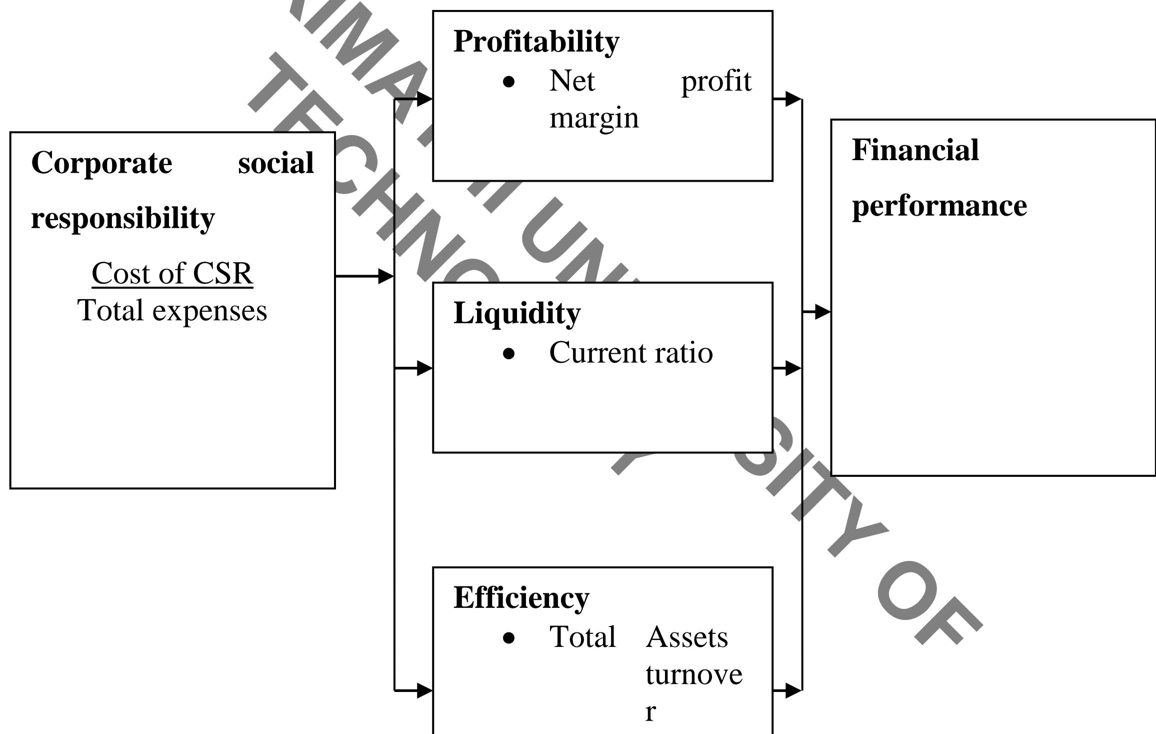

Figure 2 :Operational Framework of effects of CSR on financial performance of firms in Kenya.

The purpose of this study was to assess the effect of corporate social responsibility on the financial performance of Kenyan companies that have foundations. Literature review revealed that the relationship between these two variable can be positive, negative or none. The financial performance is as such the dependent variable in this study and since the study intends to make use of secondary data, the performance was assessed using the profit margin of at the end of the company's fiscal year. The researcher also assessed whether the observed profit or loss was an improvement or a decline from the previous fiscal years. Previous literature also outlined the importance of controlling the size and industry on financial performance and CSR which are the intervening variables in the study.

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CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

The chapter presents research design, target population, sampling and data analysis procedures and ethical considerations

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3.2 Research Design

Research design is the procedure used by the researchers to explore the relationship between variables to form subjects into groups, administer the measures, and analyze data .Mugenda and Mugenda (2005). The study adopted a descriptive survey design. Descriptive study design is a study in which the researcher describes or presents a picture of a phenomenon under investigation (Burns, 2010). Data is collected and analyzed in order to describe the current conditions and the relationships concerning the problem. This research design is suitable because it enabled the researcher to describe the relationship between corporate social responsibility and financial performance of public companies. This method of study was used by Kariuki(2013) in studying the challenges facing Safaricom Foundation. Kirwa (2013) and Nyagongo (2013) also used descriptive survey design in similar studies.

3.3 Target Population

Target population refers to all members of a real or hypothetical set of people, events or objects to which a researcher wishes to generate results from the study (Kothari, 2004). It also defined as a group of individuals, objects or items from which samples are taken for

measurement (Kombo and Tromp,2006) The study targeted public companies which have established foundations within their corporate social responsibility policy. There were 70 Kenyan companies listed in the NSE (NSE, 2014). A total of 6 of listed companies have established foundations which operate within their CSR framework these are: Kenya Airways, Kenya commercial bank, Equity Bank, East African Breweries Limited, Safaricom Limited and Britam (CMA, 2014). Rutto (2013) also targeted public companies in the NSE in her study.

3.4 Sampling procedure

According to Mugenda and Mugenda (2003) a sample is a small group of accessible population. Sampling refers to that process of selecting a sample from a defined population with the intention that the sample accurately represents that population (Burns, 2010). Purposive sampling was employed in selecting the companies to participate in the study. Purposive sampling was employed to enable the researcher control the variables "size" and "industry" of the company which have been shown to intervene in the relationship between CSR and Financial performance. The researcher selected all the six listed companies with foundations. Camelia,Chirata&Cornelia Dascula(2011) used purposive sampling in their study corporate social responsibility reporting .This sampling procedure was also used by Kirwa (2013) and Rutto (2013).

3.5 Data Collection

Data collection is the process of gathering and measuring information on variables of interest, in an established systematic fashion that enables one to answer stated research questions, test hypotheses, and evaluate outcomes (Mugenda & Mugenda, 2012). Blaxter

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et al. (2006) Data collection is a systematic approach to gathering information from a variety of sources to get a complete and accurate picture of an area of interest.

Secondary data obtained from the companies' reports was used. The researcher used the financial statements for the six companies for the financial years 2007-2012 to assess the impact CSR has on their financial performance. The researcher was interested to learn the amount spent on CSR by a particular company as well as the profit/loss and whether the latter is an improvement or a drop. Particularly the researcher was interested in the Returns on Equity and Returns on Assets. A data summary sheet was used to collect data. Waruru(2013)used secondary data when researching corporate social responsibility in Safaricom. Ioannis Ioannou & George Serafeim(2010)used secondary data collected from companies websites.

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3.6 Data analysis

Data analytics is the science of examining raw data with the purpose of drawing conclusions about that information (Dawson, 2009). Data Analysis is the process of systematically applying statistical and/or logical techniques to describe and illustrate, condense and recap, and evaluate data (Burns, 2010). The study dealt with quantitative data financial statements of the participating companies. The researcher will employ the statistical package for social sciences (SPSS) to generate findings. Descriptive and inferential statistics was employed in data analysis. Descriptive statistics involved frequency distributions and means.

Bivariate linear regression model were used to establish the relationship between CSR and financial performance. Camelia ,Chirata&Cornelia Dascula(2011)in their study on

corporate social responsibility reporting used Pearson correlation as a measure of the strength of relationship between two variables and tested their significance. Ioannis Ioannou& George Serafeim(2010)used descriptive and inferential statistics to draw their conclusions from their study.

Model 1: CSR cost (independent variable) against Financial perfomance(dependent variable).

Financial performance will be measured using profitability ,liquidity and efficiency as variables against CSR.The linear regression model will be expressed as the following

$Y= \alpha + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3$

Where,

Y is the CSR cost of each firm which will be measured by the linear regression model.

α is the constant term

β is statistic of regression

X_1 is profitability

X_2 is liquidity

X_3 is Efficiency

3.7 Ethical considerations

Consent was sought from Dedan Kimathi University of Technology and the participating firms. The data collected was stored in a password protected computer. Only the

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researcher had access to the data. The information gathered in the study was used for study purposes.

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CHAPTER FOUR

RESEARCH FINDINGS AND DISCUSSIONS

4.1 Introduction

The chapter presents data analysis and interpretation of the findings based research findings. The data was analysed using the statistical package for social sciences (SPSS).

4.2 Descriptive Analysis

Analysis was carried out on data obtained from the companies' financial reports from 2007 to 2012.The data comprised of net profit margin, current ratio and total assets turnover. The dependent variables for the study were the net profit margin (profitability), current ratio (liquidity) and total assets turnover (efficiency), while the independent variable was CSR .The CSR was measured against the total expenses of each company.

Preliminary analysis involved descriptive statistics and correlation analysis on all the variables for the purpose of understanding the variables as well as the direction and magnitude of their relationship. Table 4.1 show that a total of 36 observations were used in the study, with net profit margin, current ratio, total assets turnover and CSR (Millions) having a mean of .461, 1.061, .933 and 51.858 respectively. Notably, the values for net profit margin, current ratio and total assets turnover have a variation less than 1 indication that these values are very close to their respective means. However, there exist a large variation of 43.942 in the CSR value, which indicate that some of the firms spent a lot of money in CSR.

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Table4. 1 :Descriptives

	N	Minimum	Maximum	Mean	Std. Deviation
Net Profit Margin	36	.0154	2.7619	.461	.597
Current Ratio	36	.12	2.21	1.061	.506
Total Assets Turnover	36	.110	2.060	.933	.619
CSR (Million)	36	.70	151.48	51.858	43.942
Valid N (listwise)	36				

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Table 4.2 has the correlation analysis output, among the dependent variables it's only the Net Profit Margin that has significance weak negative correlation (r = -.341, p. value < .05) with the independent variable. Other dependent variables insignificant correlation with the independent variable. However these findings do not differ with Riahi-Belkaoui (1992) who found a negative relationship between external perceptions of a company's CSR and profitability.

Table4.2 :Correlations coefficients of study variables

Net Profit Margin	Pearson Correlation	1
	Sig. (2-tailed)	
Current Ratio	Pearson Correlation	.177
	Sig. (2-tailed)	.303
Total Assets Turnover	Pearson Correlation	.004
	Sig. (2-tailed)	.983
CSR (Million)	Pearson Correlation	-.341*
	Sig. (2-tailed)	.042

4.3 Effect of Corporate Social Responsibility on Profitability

The model fitness of the resultant bivariate linear regression is presented in Table 4.3.This table shows that R Square value is .116 implying that 11.6% of the variation in profit explained by the variation in CSR.

Table 4.3 :Model summary of CSR & Profitability

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.341	.116	.090	.5695987

a. Predictors: (Constant), CSR (Million)

The ANOVA for the model is presented in Table 4.4.This table shows an F-value of 4.459 and P-value of 0.042< P=.05 The ANOVA statistics imply that the effect of CSR in profitability is significant among firms with foundations in Kenya. These research finding Agree with Margolis *et. al.,* (2007) whose analysis resulted in finding a positive relationship between CSR and profitability. However, since the study found that there was no relationship and negative relationship in some companies the findings are in agreement with Wissink (2012) who found that the small effect size indicates that, although CSP is not detrimental for CFP, it is not very beneficial to CFP either.The findings are supported by the stake holder’s theory which states that good social performance will lead to higher financial performance.

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Table 4.4: ANOVA of CSR & Profitability

	Model	Sum of Squares	df	Mean Square	F	Sig.
1	Regression	1.447	1	1.447	4.459	.042
	Residual	11.031	34	.324		
	Total	12.478	35			

a. Dependent Variable: Profitability

b. Predictors: (Constant), CSR (Million)

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The regression coefficients of the model are presented in Table 4.5. This table shows that β = -0.005 with a P-value of .042. This indicates that a unit increase in CSR will result to a .005 decrease in the net profit margin, on the other hand when the CSR value is zero the model can only predict .701 of the net profit margin. Thus the results are consistent with the virtuous circle theory, based on good management theory, the authors expect a similar, positive relationship in the other causal direction. This results are similar to Goss and Roberts (2009) who found a negative relationship where managers that want to polish their reputations may increase the money spent on CSR at the expense of shareholders. Both management actions may explain why negative financial performance may result in improved attention to the social domain. However the findings differ with those of Griffin and Mahon (1997) who looked at the chemical industry and found that high CSR was linked to high Profitability and that low amounts of CSR reporting was linked to lower CFP.

Table 4.5: Regression of Model coefficients of CSR & Profitability

	Model	Unstandardized Coefficients		Standardized Coefficients		
		B	Std. Error	Beta	t	Sig.
1	(Constant)	.701	.148		4.734	.000
	CSR (Million)	-.005	.002	-.341	-2.112	.042

a. Dependent Variable: profitability

4.4 Effect of Corporate Social Responsibility On Liquidity

The model fitness of the resultant bivariate linear regression is presented in Table 4.5.This table shows that R Square value is .058 implying that 5.8% of the variation in liquidity is explained by the variation in CSR.

Table4.6: Model Summary of CSR & Liquidity

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.241[a]	.058	.030	.49786

a. Predictors: (Constant), CSR (Million)

The ANOVA for the model is presented in Table 4.6.This table shows an F-value of 2.095 and P-value of 0.157>P=.05 The ANOVA statistics imply that the effect of CSR and liquidity are not statistically significant. Hence this model is not reliable in the prediction of liquidity among firms with foundations in Kenya. The study found that there were no significant relationship between CSR and liquidity of firms in any of the 6 participating firms. The findings are therefore in disagreement with Cho et al. (2012) found that CSR performance improves market liquidity and decreases bid-ask spreads and Cheng et al. (2013) who found that firms with better CSR performance are more

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engaged with their stakeholders, limiting the likelihood of opportunistic behavior and reduce overall contracting costs. The study therefore does not support any of the theories in the study.

Table 4.7 :ANOVA of CSR & Liquidity

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	.519	1	.519	2.095	.157
	Residual	8.427	34	.248		
	Total	8.947	35			

a. Dependent Variable: Liquidity
b. Predictors: (Constant), CSR (Million)

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The regression coefficients of the model are presented in Table 4.8.This table shows that β=-0.003 with a P-value of .157. This indicates that a unit increase in CSR will result to a .003 decrease in liquidity, on the other hand when there CSR value is zero the model can only predict 1.205 of the liquidity.

The study found that there were no significant relationship between CSR and liquidity of firms in any of the 6 participating firms. The findings are therefore in disagreement with Cho et al. (2012) found that CSR performance improves market liquidity and decreases bid-ask spreads and Cheng et al. (2013) who found that firms with better CSR performance are more engaged with their stakeholders, limiting the likelihood of opportunistic behavior and reduce overall contracting costs.

Table 4.8: Regression of model Coefficients of CSR & Liquidity

	Model	Unstandardized Coefficients		Standardized Coefficients		
		B	Std. Error	Beta	t	Sig.
1	(Constant)	1.205	.129		9.315	.000
	CSR (Million)	-.003	.002	-.241	-1.447	.157

a. Dependent Variable: Liquidity

4.5 Effects of Corporate Social Responsibility on Efficiency

The model fitness of the resultant bivariate linear regression is presented in Table 4.9.This table shows that R Square value is .023 implying that 2.3% of the variation in efficiency is explained by the variation in CSR.

Table 4.9 :Model summary of CSR & Efficiency

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.152[a]	.023	-.006	.621140

a. Predictors: (Constant), CSR (Million)

The ANOVA for the model is presented in Table 4.10.This table shows an F-value of .804 and P-value of 0.376>P=.05 The ANOVA statistics imply that the effect of CSR and efficiency are not statistically significant. Hence this model is not reliable in the prediction of efficiency among firms with foundations in Kenya.

The findings also show that there was no relationship between CSR and firm efficiency in any of the other six participating firms. The findings are therefore in disagreement with

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Nyagongo (2012) who found that CSR was a major contributor to the profitability of organizations through enhanced image and reputation. Further the quality performance was vital in improving reputation with customers. The research also found out that these organizations had strategic partners in their CSR agenda.

Table 4.10: ANOVA of CSR & Efficiency

	Model	Sum of Squares	df	Mean Square	F	Sig.
1	Regression	.310	1	.310	.804	.376
	Residual	13.118	34	.386		
	Total	13.428	35			

a. Dependent Variable: Total Assets Turnover
b. Predictors: (Constant), CSR (Million)

The regression coefficient of the model is presented in Table 4.11 .This table shows that β = -0.002 with a P-value of .376. This indicates that a unit increase in CSR will result to a .002 increase in efficiency, on the other hand when there CSR value is zero the model can only predict.821 of the efficiency. These findings are in agreement with (Becchetti and Trovato ,2011) examined the relationship on a sample of firms observed in a 13-year interval by focusing on a performance indicator and found a positive relationship between CSR and efficiency. Hence the finding are supported by the virtous circle theory which states that if more resources are put under CSR then there will be a positive effect on financial performance of firms and vice versa.

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Table 4.11:Regression of Model coefficients of CSR & Efficiency

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	.821	.161		5.087	.000
	CSR (Million)	.002	.002	.152	.897	.376

a. Dependent Variable: Efficiency

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CHAPTER FIVE

SUMMARY OF STUDY, CONCLUSIONS AND RECOMMENDATIONS

5.1 Introduction

This chapter presents a summary of the major findings from the results of the study and the conclusions made from them. It also presents the recommendations made by the researcher. This has been done in respect to the stipulated objectives in a bid to answer the research questions.

5.2 Summary of Research

The purpose of this study was to assess the effect of corporate social responsibility on financial performance of firms with philanthropic oriented foundations in Kenya. Specifically, the study aimed to establish; the effect of CSR on profitability of firms in Kenya, the effect of CSR on liquidity of firms in Kenya and the influence of CSR on efficiency of firms in Kenya. The study adopted a descriptive survey design. The study targeted public companies which have established foundations within their corporate social responsibility policy. Purposive sampling was employed in selecting six companies to participate in the study.

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Secondary data obtained from the companies' reports was used. The researcher used the financial statements for the six companies for the financial years 2007-2012 to assess the impact CSR has on their financial performance. Descriptive and inferential statistics was employed in data analysis. Descriptive statistics involved frequency distributions and

means. Bivariate linear regression model were used to establish the relationship between CSR and financial performance.

From the results, CSR has notable significant impact on net profit margin. On the other hand, CSR has mild insignificant impact on current ratio and total assets turnover. A general observation is that CSR has a negative effect on net profit margin, also has small negative insignificant effect on current ratio and lastly a small positive insignificant effect on total assets turnover.

5.3 Conclusion

5.3.1 What is the effect of CSR on profitability of firms in Kenya?

The researcher concludes that corporate social responsibilities in Kenyan firms with foundations have more effect on profitability than liquidity and efficiency. The researcher concludes that the increased profitability may be attributed to increased sales due to improved image by the public. This indicates that CSR has no significant effect on the profitability of firms in Kenya.

Financially strong companies can afford to commit monies ways that have a more long-term strategic impact, such as providing services for the community and their employees. Those allocations may be strategically linked to a better public image and improved relationships with the community in addition to an improved ability to attract more skilled employees and more customers

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5.3.2 What is the effect of CSR on liquidity of firms in Kenya?

A general observation is that CSR has a small negative insignificant effect on liquidity. The study found that there were no significant relationship between CSR and liquidity of firms in any of the 6 participating firms.

5.3.3 What is the influence of CSR on efficiency of firms in Kenya?

. A general observation is that CSR has a small positive insignificant effect on efficiency. Hence the researcher concludes that there is no significant relationship between CSR and efficiency of firms in Kenya.

5.4 Recommendations

(i)The researcher recommends that firms with foundations should focus on investing their CSR funds to solve problems that have a widespread effect. This will ensure that CSR activities touch more lives which benefit both the community as well as the firm itself. In carrying out CSR activities, the researcher recommends that all stakeholders (including customers of the firm) should be involved to enhance customer retention and thereby promote financial performance. All CSR programmes and projects should be monitored and evaluated to check whether they are achieving their intended results.

(ii)Since its evident that enhancing corporate performance does not affect liquidity, the researcher recommends that firms should have monies in terms of cash since its important for company development and at the same time is one of the fundamental endogenous factors which are responsible for company market position.

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(iii)The efficiency of the firm is not affected by the much the firms have invested in CSR hence firms should enhance the quality of performance which is vital in improving reputation with customers. . Evaluation findings can be used to inform future decisions on CSR to enhance corporate efficiency

5.5 Suggestions for further study

(i)The researcher suggests that more study should be done on the effects of CSR and firm efficiency.

(ii)The researcher also proposes a deeper study on the effects of CSR and firm liquidity.

(iii)Since the study only focused on firms with philanthropic foundations, a similar study should be carried out on all firms that are theocentric listed in the stock exchange.

(iv)Future studies should focus on getting a deeper understanding of the relationship CSR and its determinants.

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APPENDEX 1

SUMMARY SHEET DATA

	profitability	liquidity	Efficiency	CSR	Year
	Y	y	Y	X	
KQ	0.0154	0.92	2.01	16,600,000	2012
	0.0412	1.06	1.52	35,380,000	2011
	0.0288	0.87	1.34	20,350,000	2010
	0.0568	0.91	1.32	40,830,000	2009
	0.064	1.52	0.96	38,690,00	2008
	0.0697	1.39	0.94	48,290,000	2007
EABL	1.2622	1.26	48.25	700,840	2012
	2.7619	1.11	44.15	12,399,40 0	2011
	2.25	1.41	32.35	8,703,000	2010
	0.2502	2.01	1.3	86,091,850	2009
	0.2827	1.98	1.33	91,843,850	2008
	0.1593	2.21	2.06	75,288,910	2007
SAFARICOM	0.118	0.56	1.26	126,276,070	2012
	0.1388	0.64	1.189	131,589,730	2011
	0.1804	0.67	1.194	151,480,380	2010
	0.1495	0.49	1.26	105,367,600	2009
	0.2257	0.51	1.25	138,532,860	2008
	0.2531	0.77	0.84	120,104,310	2007
BRITAM	0.2145	1.51	0.56	25,194,610	2012
	0.5786	0.62	0.13	19,573,050	2011
	0.3026	0.39	0.35	27,137,840	2010
	0.2434	1.47	0.11	4,211,200	2009
	0.99	1.75	0.16	24,245,670	2008
	0.2059	1.8	0.19	25,600,500	2007
EQUITY	0.3615	1.21	0.14	1,099,700	2012
	0.4084	1.21	0.14	9,774,000	2011
	0.4054	1.23	1.14	7,555,000	2010
	1.003	1.12	0.31	71,320,000	2009
	0.8693	1.33	0.23	39,100,000	2008
	1.078	1.39	0.12	18,900,000	2007
KCB	0.277	0.75	0.12	109,810,460	2012
	0.3008	0.31	0.11	71,779,730	2011
	0.2447	0.21	0.12	40,838,710	2010
	0.1187	1.13	1.51	41,906,900	2009
	0.129	1.12	1.54	29,745,720	2008
	0.3032	0.12	0.74	24,318,780	2007

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