RELATIONSHIP BETWEEN CORPORATE SOCIAL RESPONSIBILITY AND FINANCIAL PERFORMANCE OF COMMERCIAL BANKS IN KENYA

GRACE AWUOR OGOLLA

D61/76226/2009

A RESEARCH PROJECT REPORT SUBMITTED IN PARTIAL FULFILLMENT OF THE REQUIREMENT FOR THE AWARD OF THE DEGREE OF MASTER OF BUSINESS ADMINISTRATION, SCHOOL OF BUSINESS, UNIVERSITY OF NAIROBI

OCTOBER, 2013

DECLARATION

This research report is my own original work and it has not been submitted anywhere for any award of a degree or diploma. Where other sources of information have been used, they have been acknowledged.

Signature: ………………… Date…………………..

Name: Ogolla Grace Awuor

Reg. No.D61/76226/2009

This proposal has been presented with my approval as the university supervisor.

Signed ……………….. Date …………………

Dr. Fredrick Ogilo

Department of Finance and Accounting,

Lecturer, School of Business, University Of Nairobi.

Signed ……………….. Date …………………

Dr. Josiah Aduda

Chairman, Department of Finance and Accounting.

School of Business, University Of Nairobi

DEDICATION

I dedicate this project to my wonderful Husband, Son and Parents who believed in the pursuit of academic excellence. I also would like to thank my friends for their support and encouragement; I could not have completed this project without their assistance, tolerance and enthusiasm.

ACKNOWLEDGEMENT

First and foremost, I would like to thank God the Almighty father who gave me the strength to carry out this research work. Secondly I would like to thank my supervisor Dr Fredrick Ogilo for the guidance he gave me throughout this research project. This project could not have been completed on time without his help and support. He was always there even when the end seemed so far. He ensured a well researched paper was finalized.

I wish to thank my Husband Pastor Patrick Maurice Onyango for his encouragement, Patience and prayers during my studies. To my beloved son Kish Onyango who was also patience during my studies.

ABSTRACT

The main objective of the study was to determine whether there exist a relationship between corporate social responsibility and financial performance of commercial banks licensed by central bank of Kenya. Corporate social responsibility and financial performance in the banking system have been neglected in many studies conducted in developing counties hence the study sought to plug that gap. The study adopted casual design. The population of the study comprised of all the 41 commercial banks licensed by central bank of Kenya that were in operational between Jan 2007 and Dec 2011.Secondary data was obtained from the audited financial reports of the central bank of Kenya for the period from 2007 to 2011. A multiple regression model was adopted to determine the relationship between the two variables. Corporate social responsibility score was obtained using content analysis of reports of the banks on various components of corporate social responsibility as reported in their audited financial reports. One major finding of the study was that there is a strong relationship between the independent variables corporate social responsibility and the dependent variable financial performance. In conclusion Commercial banks should enhance efficiency in the banking services so as to improve financial performance as there was a significant relationship between the two variables. It was recommended that the commercial banks should invest more in corporate social responsibility to improve on company performance. Suggestions that in the years to come and given the availability of a wider pool of data the same could be under taken over a longer time span to assess whether there are any major difference in the findings when data is taken over a longer time of ten or more years.

TABLE OF CONTENTS

LIST OF ABBREVIATIONS

ANOVA Analysis of Variance

CBK Central Bank of Kenya

CFP Corporate Financial Performance

CSP Corporate Social Performance

CSR Corporate Social Responsibility

FP Financial Performance

NASI Nairobi Securities Exchange All Share Index

NSE Nairobi Securities Exchange

NYSE New York Securities Exchange

ROA Return on Assets

SPSS Statistical Package for Social Science

SRI Social Responsible Investment

CHAPTER ONE: INTRODUCTION

1.1 Background of the study

The concept of corporate social responsibility means that organizations have moral, ethical, and philanthropic responsibilities in addition to their responsibilities to earn a fair return for investors and comply with the law. A traditional view of the corporation suggests that its primary, if not sole, responsibility is to its owners, or stockholders. However, CSR requires organizations to adopt a broader view of its responsibilities that includes not only stockholders, but many other constituencies as well, including employees, suppliers, customers, the local community, local, state, and federal governments, environmental groups, and other special interest groups. Corporate social responsibility is related to, but not identical with, business ethics. While CSR encompasses the economic, legal, ethical, and discretionary responsibilities of organizations, business ethics usually focuses on the moral judgments and behavior of individuals and groups within organizations. Thus, the study of business ethics may be regarded as a component of the larger study of corporate social responsibility (Carroll and Buchholtz, 2003).

Stakeholder theory was developed by Freeman (1984) incorporating corporate accountability to a broad range of stakeholders. Wheeler et al, (2002) argued that stakeholder theory derived from a combination of the sociological and organizational disciplines. Stakeholder theory is less of a formal unified theory and more of a broad research tradition, incorporating philosophy, ethics, political theory, economics, law and organizational science. Freeman (1984) defines Stakeholder theory as “any group or individual who can affect or is affected by the achievement of the organization’s objectives” Stakeholder theorists suggest that managers in organizations have a network of relationships to serve – this include the suppliers, employees and business partners.

Kenya’s financial system comprises commercial banks, of which some are partly or wholly owned by foreign financial institutions. According to CBK, foreign banks comprise about a quarter of all banks in the country, with 11 foreign banks out of 44 commercial banks in 2007. The foreign banks account for about 40% of commercial banks’ core capital. There are five foreign banks that are fully foreign incorporated. These fully foreign owned banks accounted for 9.2% of the core capital of the banking.

1.1.1 Corporate Social Responsibility

Corporate social responsibility is defined as a perceptual representation of a company’s past action and future prospects that describe the firms overall appeal to all of its key constituents when compared with other leading rivals. A growing body of research argues that good corporate social responsibility have strategic value for the firms that possess them. According to Walker (2010), a corporate social responsibility can lead to several strategic benefits such as lowering the firms cost; enabling firms to charge premium prices; attracting applicants, investors and customers; increasing profitability and creating competitive barriers. A positive reputation increases the likelihood that stakeholders will contract with a given firm. More reputable firms can charge a premium, which will in turn attract investors. A positive corporate social responsibility will attract employees and promote lower turnover, improve customer attitude, lower client’s perceived risk, increased the propensity to joint venture and create higher credibility.

Kibera (1996) says the concept of social responsibility of business is concerned with the obligation that business has in helping to promote the welfare of the society.

He says that business has been experiencing pressure from the society to be socially responsible. He gives two reasons for the increased pressure as: firstly the society has more become more enlighten and more educated thus more aware of its problems, rights and the role business can play in social welfare. Secondly, the society's problems have become more alarming to the level where the society is impatient and feels that something must be done. Therefore more than ever before businesses are expected to play a role in combating these problems.

In Kenya, the companies engage in a number of long terms corporate social responsibility projects. These include the long term rehabilitation and capacity-building programme for the Mama Ngina Children's Home and other homes, Scholarships fund to enable bright children from underprivileged families to acquire quality education, donating money to charities towards proper diagnosis, long term treatment, care and counseling of mental illness sufferers in Kenya, donation to the Kenya Red Cross Society towards the emergency relief fund regarding the recent civil unrest, involvement in environmental conservation activities through distribution of tress seedling the society for planting, sporting and other charitable activities. However, not all listed companies are involved in CSR; some do very little if any. It is important to understand what drives companies which are engaged in CSR and how it affects CFP.

Corporate social responsibility measure lacks concreteness thus quantitative assessment is extremely difficult.CSR is a concept with many dimensions, which do not behave similarly in all industries and therefore have their own characteristic. There are CSR disclosure which consist of analysis of the annual report, letter to the shareholders and other corporate disclosure.

Social measures are analyzed on how companies influence the customers, employees, community, environment and minority groups. Corporate Social Responsibility reflects an approach to internal decision making, the presence or absence of which may not easily be determined by external observers. There are many ways of measuring the CSR of a company.

1.1.2 Measurements of Corporate Social Responsibility

Content analysis and reputation index are two generally accepted methods of measuring CSR (Cochran and Wood, 1984). Each has its strengths and weaknesses, and can by no means be considered fully adequate measure of CSR. Great care must be exercised and adjustment may be required when these measures are used for comparing social responsibilities of firms in the same industry or from different sectors.

Content analysis measures, either qualitatively or quantitatively, the extent of the reporting of particular variables in a broad array of firm publications, which usually include annual report, sustainability report, and corporate websites. The variables under analysis represent CSR activities, and the evaluation of these variables is fairly mechanical and objective. The same evaluation can be applied easily on a large sample of firms. However, the choice of these variables can be subjective and the interpretation of them shows no true indication of what the firms are actually doing.

Reputation index rates firms based on the foundation of one or more dimensions of social performance as perceived by knowledgeable observers. The same criteria apply consistently to each firm. However, the resulting ranking is highly subjective as it may vary significantly from observer to observer.

Past studies have utilized a variety of sources to assess corporate social responsibility of firms. Carmelo Reverte (2008) used CSR disclosure ratings from the Observatory on corporate social responsibility in his research in explaining CSR disclosure practices of Spanish listed firms. Other measures which appear in CSR related academic papers include Fortune reputation survey, Domini 400 Social Index, and Dow Jones Sustainability Group Index. One problem with these metrics is that they do not cover enough firms to provide a reliable measure (Simpson and Kohers, 2002). Scholtens (2008) as well as other researchers built their own appropriate CSR measures in their research framework. This results in a major contribution to why there exist inconsistencies among many CSR empirical findings

1.1.3 Corporate Social Responsibility and Financial Performance

The relationship between corporate social responsibility and financial performance has been a debate topic of scholars for a half century (Simpson and Kohers, 2002). The empirical study result on the CSR and CFP link have never been in agreement, as some studies determine negative correlation, some determine positive correlation, while others determined no correlation at all. The viewpoint for positive correlation between CSR and CFP suggests that as a company's explicit cost are opposite of the hidden cost of stakeholders, therefore, this viewpoints proposed from the perspective of avoiding cost to major stakeholders and considering their satisfaction (Cornell and Shapiro,1987). In addition, this theory further infers that commitment to CSR would result in increased cost to competitiveness and decrease the hidden cost of stakeholders.

This argument is meaningful and reasonable, as good relationship with employees, suppliers and customers are necessary for the survival of the company.

Bowman and Haire (1975) pointed out that some shareholders regard CSR as a symbolic management skill, namely, CSR is a symbol of reputation, and the company reputation will be improved by actions to support the community, resulting influence on sale. Therefore, when a company increases its cost by improving CSR in order to increase competitive advantages, such CSR activities can enhance company reputation, thus in the long run CFP can be improved, by sacrificing the short term CFP.The viewpoint for negative correlation between CSR and CFP suggests that the fulfillment of CSR will bring competitive disadvantages to the company. When carrying out CSR activities, increased cost will result in little gain if measured in economic interest. When neglecting some stakeholders, such as employees or the environment, result in a lower CSR for the enterprise, the CFP may be improved, Hence Aupperle et al., (1985) indicated that this theory was based on the assumption of negative correlation between CSR and CFP.

Some other studies suggest that CSR is not related to CFP at all, Ullmann (1985) pointed out that there is no reason to anticipate the existence of any relationship between CSR and CFP, an the two. On the other hand, the issue of CSR measurement may also cover the link between CSR and CSP would disappear with introduction of more accurate variables, such as the research and development strength, into the economic model. Socially responsible investment SRI combines investors' financial objective with their concerns about social, environmental or ethical consequences taken into account in the selection, retention and realization of investments both positive and negative, within the context of rigorous financial analysis.

By controlling the impact of its activities on stakeholders, it targets threefold economic, social and environmental performance through which it contributes to the overall objective of sustainable development. That is why socially responsible companies are also called sustainable companies; the performance of socially responsible companies is a key element in their performance.

1.1.4 Financial Performance Measure

Two widely recognized accounting ratios are employed as proxies for financial performance in the banking sector. Return on asset measures how much profit the bank assets can generate. This ratio is free from the effects of bias that can result from differences in capital structure amongst banks. Return on equity measures how much profit the bank can generate from shareholder investment. It is best use to compare companies in the same industry. Annual share price return is also employed to provide a non-accounting measure of bank performance. It reflects the overall market evaluation of each bank in a year.

1.1.5 Commercial Banks in Kenya

In Kenya, the Banking Sector is composed of the Central Bank of Kenya, as the regulatory authority and the regulated; Commercial Banks, Non-Bank Financial Institution and Forex Bureaus. As at 31st December 2009 the banking sector comprised 45 institutions, 43of which were commercial banks and 2 mortgage finance companies are licensed and regulated under the banking Act, Cap 488 and Prudential Regulations issued there under. Forex Exchange Bureaus are licensed and regulated under the Central Bank of Kenya (CBK) Act, Cap 491. Out of the45 commercial banking institutions, 33 were locally owned and 12 were foreign owned.

The locally owned financial institutions comprise 3 banks with significant government shareholding,28 privately owned commercial banks and 2 mortgages finance companies (MFC).Of the 42 private banking institutions in the sector,71% are locally owned and the remaining 29% are foreign owned. Performance of the banking sector was rated strong as institutions achieved satisfactory conditions and improve operations results despite high market completion as each of these institutions scramble for a significant market share. New products have been introduced in the market as a result of rising completion. The system remained well capitalized. Shareholders’ funds, deposits and assets increased by 35.2%, 27.7% and 31.9% respectively (CBK, 2009).

1.2 Research Problem

Corporate social responsibility aims at lowering firms cost; enabling firms to charge premium prices; attracting applicant, investors and customers; increasing profitability and creating competitive barriers. However as seen in studies of (Kibera,1996) says the concept of social responsibility of business is concerned with the obligation that business has been experiencing pressure from the society to be socially responsible. Davis (1975) argues that modern business is intimately integrated with the rest of society. It is not some self-enclosed world, like a small study group. Rather, business activities have profound ramifications throughout society, and their influence on peoples’ lives is hard to escape. Therefore, corporations have responsibilities that go beyond making money because of their great social and economic power.

According to stakeholder’s theory it argues that, apart from making profit and obeying the law, a company should attempt to alleviate or solve social problems since there are those who believe in providing for society’s discretionary expectations. This theory maintains that corporations should consider the effects of their actions upon the customers, suppliers, general public, employees, and others who have a stake or interest in the corporation. According to social contract theory, Gray et al. (1966) argues that a society is a series of social contacts between members of society and society itself. He states that the business does not act in a responsible manner because of it is in its commercial Interest, but because it is part of how society implicitly expect business to operate.

Several studies have been conducted both locally and internationally on the relationship between corporate social responsibility and financial performance. Roshima (2002) did a study on the relationship between corporate social responsibility disclosure and corporate governance characteristics in Malaysian public listed companies with the objective of finding the relationship between corporate governance and the extent of corporate social responsibility. He noted that government ownership and audit committee are positively and significantly correlated with the level of corporate social responsibility. Auka (2006) did a study on factors influencing the practice of CSR of financial institutions in Kenya with objective of finding out the factors that influence the practice of CSR of financing institutions in Kenya and the benefits that arise as a result of financial institutions engaging in the social activities. In his study he noted that the factors that have great influence on the extent of the practice of CSR in the financial institutions is corporate image, moral obligations and solving societal problems and the most important benefit of CSR in the financial institution is to improve corporate image.

Kweyu (1993) studied managerial attitudes towards CSR among banks and found profitability to be the most dominant objective in implementing CSR in banks.

Most studies, though, both locally and internationally have focused on the other sectors listed at the NSE. Corporate social responsibility in the banking sector has rarely been studied and there are inconsistent prior results and limited research on the banking systems of developing countries about factors influencing corporate social responsibility and financial performance of banks in developing countries. Furthermore, CSR relationships have been partly neglected in many studies conducted in developing countries. The study intended to plug that gap. The study sought to answer the following questions; what is the relationship between corporate social responsibility and financial performance in the banking sector of the banks licensed at the central bank? What other factors that may influence a firm's financial performance?

1.3 Objective of the study

To establish whether there exists a relationship between corporate social responsibility and financial performance of commercial banks in Kenya.

1.4 Value of the study

The study will be of value to the banking industry in Kenya as it will enable the bank managers and financial analyst to make more informed decisions in order to protect their stock returns against financial crises. The study will be of great value to the body of corporate financial management discipline and will form the basis of further research by identifying the gap that arises from this study, Further, the study will create forum for further discussions and debate on firm financial performance related issues among financial consultants and financiers thus by adding to the body of knowledge that already exist.

To the theory, the study will be useful to scholars and academic researchers understand more of the information on relationship between corporate social responsibility and financial performance of commercial banks hence adding more information to the existing of pool of knowledge. It will also be used as a basis for further research.

The Central bank of Kenya will also use the findings of this study to enhance their regulatory authority over Commercial banks in that they will be able to develop more informed and comprehensive regulatory frame work that are to be followed or implemented by the commercial banks to mitigate the effects of financial crisis in future and to the scholars and academic researchers it will add more to the existing pool of knowledge and a basis for further research.

CHAPTER TWO: LITERATURE REVIEW

2.1 Introduction

This chapter reviewed various theories that provided explanations to the relationship between corporate social responsibility and the financial performance. The theories discussed are stakeholder's theory and social contract theory. It further examines the previous empirical research done in this area of study, followed by the explanations of variables in the analysis model before the concluding remarks.

2.2 Theoretical Review

Various theoretical frameworks have been researched on the relationship between corporate social responsibility and financial performance of a firm and had an effect on the financial performance of such firms.

2.2.1 Stakeholders Theory

Stakeholder theory states that the purpose of a business is to create as much value as possible for stakeholders. In order to succeed and be sustainable over time, executives must keep the interests of customers, suppliers, employees, communities and shareholders aligned and going in the same direction. Johnson (1971) in his definition of CSR, conceives a socially responsible firm as being one that balances a multiplicity of interests, such that while striving for larger profits for its stockholders, it also takes into account, employees, suppliers, dealers, local communities and the nation. This definition draws from stakeholder theory as developed by Freeman (1984).

According to Freeman (1984), the firm can be described as a series of connections of stakeholders that the managers of the firm attempt to manage. Stakeholder, according to Bruno & Nichols (1990: 171) is a term which denotes any identifiable group or individual who can affect or be affected by Organizational performance in terms of its products, policies, and work processes. Davis (1975) argues that modern business is intimately integrated with the rest of society. It is not some self-enclosed world, like a small study group. Rather, business activities have profound ramifications throughout society, and their influence on peoples' lives is hard to escape. Therefore, corporations have responsibilities that go beyond making money because of their great social and economic power. Stakeholders are typically analyzed into primary and secondary stakeholders.

Clarkson (1995) defines a primary stakeholder group as "one without whose continuing participation the corporation cannot survive as a going concern" - with the primary group including "shareholders and investors, employees, customers and suppliers, together with what is defined as the public stakeholder group; the governments and communities that provide infrastructures and markets, whose laws and regulations must be obeyed, and to whom taxes and obligations may be due". The secondary groups are defined as "those who influence or affect, or are influenced or affected by the corporation, but they are not engaged in transactions with the 15 corporation and are not essential for its survival". Mitchell et al. (1997) developed a model of stakeholder identification and salience based on stakeholders possessing one or more of the attributes of power, legitimacy and urgency. Thus, it is anticipated that firms would pay most attention to those legitimate stakeholder groups who have power and urgency.

In practice this might mean that firms with problems over employee retention would attend to employee issues and those in consumer markets would have regard to matters that affect reputation. Stakeholder groups may also become more or less urgent; so environmental groups and issues became more urgent to oil firms following the Exxon Valdez oil spill (Patten, 1992). The stakeholder theory surfaced the question central to this research, which is whether organizations can be socially responsible and have good performance (profitable) while still satisfying investors and shareholders by providing acceptable levels of return on those investments.

2.2.2 Social Contracts Theory

Social contract theory, nearly as old as philosophy itself, states that a person' moral or political obligations are dependent upon a contract or agreement among them to form the society in which they live. Gray et al. (1996) describe society as "a series of social contracts between members of society and society itself". In the context of CSR, an alternative possibility is not that business might act in a responsible manner because it is in its commercial interest, but because it is part of how society implicitly expects business to operate. Donaldson and Dunfee (1999) developed integrated social contracts theory as a way for managers to take decisions in an ethical context. They differentiate between macro social contracts and micro social contracts. Thus a macro social contract in the context of communities, for example, would be an expectation that business provides some support to its local community and the specific form of involvement would be the Micro social contract. Hence companies who adopt a view of social contracts would describe their involvement as part of societal expectation however, whilst this could explain the initial motivation, it might not explain the totality of their involvement.

2.3 Determinants of Corporate Social Responsibility

The literature has identified the following factors to be key determinants of corporate social responsibility, efficiency, capital intensity and CSR score as the independent variables. Return on Equity It measures a firm's efficiency by generating profits from every income of net assets (assets minus liabilities), and shows how well a company uses investment to generate earnings growth.ROE is equal to a fiscal year's net income (after preferred stock dividends but before common stock dividends) divided by total equity (excluding preferred shares), expressed as a percentage. It measures the rate of return on ownership interest (shareholders' equity) of common stock owners.

Capital intensity is shown by how profitable a company is and this is arrived at by the Return on Assets. It is given by the ratio between net income and total assets. This ratio tells us, what the company can do with what it has this show the earnings they derive from the assets they control. It is a useful number for comparing competing companies in the same industry. The number will vary widely across different industries. Return on assets gives an indication of the capital intensity of a company, which will depend on the industrial sector. Companies that require large initial investments will generally have lower returns on assets. This parameter is widely used in the literature.

2.4 Empirical review

Fauzi (2009) did a research on firms listed on the New York Securities Exchange (NYSE) to determine the relationship between CSR and corporate financial performance. Using a sample of 101 companies listed at the NYSE and a regression model with financial performance as the dependent variable and CSR index as the independent variable, he found that CSR has no effect on CFP. He however found that leverage (a control variable in the model) has a moderating effect on the interaction between CFP and CSR.

Cheruiyot (2010) carried out a research to establish the relationship between corporate social responsibility and financial performance of firms listed at the Nairobi stock exchange. This was a cross sectional study of all the 47 listed companies in the NSE's main segment as at 31 December 2009. Using regression analysis he sought to establish the relationship between the CSR index and financial performance measured in terms of the Return on assets, return on equity and return on sales. His conclusion was that there was a statistically significant relationship between CSR and financial performance.

According to Margolis and Walsh (2002), one hundred twenty-two published Studies between 1971 and 2001 empirically examined the relationship between corporate Social responsibility and financial performance. The first study was published by Narver in 1971. Empirical studies of the relationship between CSR and financial performance comprise essentially two types. The first uses the event study methodology to assess the Short-run financial impact (abnormal returns) when firms engage in either socially Responsible or irresponsible acts. The results of these studies have been mixed.

Wright and Ferris (1997) discovered a negative relationship; Posnikoff (1997) reported a positive relationship, while Welch and Wazzan (1999) found no relationship between CSR and Financial performance. Other studies, discussed in McWilliams and Siegel (1997), are similarly inconsistent concerning the relationship between CSR and short run financial returns. The second type of study examines the relationship between some measures of corporate social performance (CSP) and measures of long term financial performance, by using accounting or financial measures of profitability. The studies that explore the Relationship between social responsibility and accounting-based performance measures have also produced mixed results.

2.5 Summary of literature review

Corporate Social Responsibility reports on a firm's social and environmental performance from a variety of perspectives; including community involvement, employee relations, product safety, philanthropy and the impacts of the firm on the environment. When a company is in a favorable position, it can perform its responsibility well. As long as a company is making profits, they tend to engage in CSR activities unlike when the companies are not making profits.

A responsible company is rewarded by its good reputation. Numerous studies have been conducted based on this belief but have failed to arrive at the conclusion. As a result of this studies done show positive correlations, others negative and others no correlation at all and a closer examination of these studies reveals a number of concerns around data sources, the type and variety measures used as both independent and dependent variable and control variables. From the foregoing summary it emerges that the researchers have not been conclusive as regards to the relationship between corporate social responsibility and the financial performance of firms, hence the study sort to fill this gap.

CHAPTER THREE: RESEARCH METHODOLOGY

3.1 Introduction

This chapter examined the research design, the population and the sample size used in the study. It further explained the data collection method and data analysis methods to be used in the study.

3.2 Research Design

The research adopted the casual design to determine the relationship between corporate social responsibility and financial performance of all the 41 licensed commercial banks. Mugenda (2003) explains that causal studies explore relationships between variables and this is consistent with this study which sort to establish the nature of the relationship. This research analyzed data on all the 41 licensed commercial banks within the specified period of time. This was consistence with other studies that had successfully used the causal design such as Rayn 2008 and Mwangi 2010.

3.3 Population of the study

All the 41 commercial banks licensed by the Central bank of Kenya and were operational between Jan, 1st 2007 and Dec, 31st 2011 made up the population.

3.4 Data Collection

The researcher used secondary data obtained from authorized data vendors. The data requirements included the name of all the listed commercial banks. In any study of CSR it must be recognized that communication is a central aspect of social interaction (Weber, 1990). The ability of companies to convey their intentions and actions to the societies in which they are located is recognized as being integral to the relationship between business and society.

The use of websites to disseminate company information served this purpose. Websites are a form of secondary data and have some distinct advantages over other data sources for research purposes (Gilbert, 2008).

3.6 Data Analysis technique

Data was edited, coded and classified into different components to facilitate a better and efficient analysis. CSR practice has different components and for the purpose of this study, components for environmental concerns, community involvement, employee concerns, product/customer concerns and others were used to analyze CSR practice. Content analysis was used to determine the score for CSR based on the number of sentences dedicated to each component of CSR in the company's annual report.

The Statistical Package for Social Sciences (SPSS) version 18 was used to analyze the data collected. The coefficient of determination, R squared, measure was used to test the significance of the regression model in explaining the relationship between CSR practices and CFP. R squared is a measure of goodness of fit showed the percentage variance in the dependent variable that was explained by the independent variable(s). The higher the R squared the better the model. The P-Value and the t-test were used to test the individual significance of the predictor variables that was used in the study.

The relationship was explained by the following regression model;

ROA $=\alpha o+\alpha_1$CSR + α_2EFF+ α_3CI+e

Where:

ROA= Return on Assets

CSR =Corporate Social Responsibility of firm

EFF=Efficiency

CI=Capital Intensity for firm

e= error term

α=Constant

α1- constant (coefficient) of Corporate Social Responsibility

α2- a constant (coefficient) of Efficiency

α3- a constant (coefficient) of Capital Intensity

3.6.1 Operationalization of the Variables

Financial performance represented by F was the dependent variable and was measured by Return on Assets, Which was calculated as (Net Income/Total assets. Efficiency was the independent variable and calculated as (Cost of sales/Total sales). Capital intensity was an independent variable was calculated as (Total assets/Total sales) which was used as control variables. CSR was obtained by adding the five components; community involvement, employee concerns, staff, product/customer concerns and others.

CHAPTER FOUR: DATA ANALYSIS AND FINDINGS

4.1 Introduction

This chapter discussed data analysis, findings, interpretations and presentation. Data for each variable was analyzed using correlation and thereafter, the regression analysis is tabulated and the findings discussed.

4.2 Descriptive Analysis

The descriptive analysis results are shown in the tables below. The ROA for each bank was computed and the results presented in Table 1 below. From this table it's evident that ROA for companies in this sector fluctuates significantly ranging from as low as – 2% to a high of 27.6%. Barclays with an average ROA of 23.4% seems to be one of the best performers over the five year period while NIC Bank with an average ROA of 5.43% has the worst performance

Table 1: Return on Assets (Net Income/Total Assets)

	Bank	**2007**	**2008**	**2009**	**2010**	**2011**	**Average**
1	DTB	0.1495	0.1650	0.1402	0.1589	0.2253	0.1678
2	Chase Bank	0.1420	0.1379	0.1863	0.2033	0.1737	0.1686
3	Barclays	0.2420	0.2762	0.2403	0.2300	0.1813	0.2340
4	Equity	0.1169	0.0858	0.0921	0.0858	0.0834	0.0928
5	NIC	0.0359	0.0785	0.0333	0.0466	0.0773	0.0543
6	I &M	0.0936	0.0793	0.0532	0.0649	0.0561	0.0694
7	KCB	0.1839	0.1209	0.2171	0.1591	0.1749	0.1712
8	Corporative	0.0490	0.0145	0.0464	0.0686	0.0696	0.0496
9	Prime Bank	0.1300	0.1520	0.0835	0.0407	0.0630	0.0939
10	Standard/Charted	0.0855	0.0591	0.1522	-0.023	0.0415	0.0629

Source: Computations from raw data obtained form CBK

4.2.1 Corporate Social Responsibility (CSR) Score

Content analysis was used to determine the score for CSR based on the number of sentences dedicated to each component of CSR in the company's annual report. The total CSR score was obtained by adding the scores for the five components of CSR. Table 3 below was a summary of these scores. From this table its apparent that KCB bank had the highest average score of 103 followed closely by Barclays bank with a score of 88. Chase bank had the lowest score of 9 followed by Prime bank with a score of 17.

Table 2: Total CSR Score

	Company	**2007**	**2008**	**2009**	**2010**	**2011**	**Average**
1	DTB	63	79	58	42	43	57
2	Chase Bank	17	9	7	5	7	9
3	Barclays	133	125	74	60	50	88
4	Equity	32	36	41	34	51	39
5	NIC	16	11	32	32	24	23
6	I &M	22	22	28	27	53	30
7	KCB	82	130	113	103	88	103
8	Corporative	65	55	52	33	17	44
9	Prime Bank	14	17	19	22	12	17
10	Standard/Charted	2551	89	45	50	64	55

Source: Computations from raw data obtained form CBK

4.3 Regression Analysis

The regression equation established was as follows:

Firm Financial performance = 0.357 + 0.001$X1$ – 0.395 $X2$ – 0.020$X3$

Both efficiency and capital intensity were inversely related with firm financial performance while CSR had a direct relationship with firm financial performance. The regression coefficients shows that αo (the value of firm financial performance when capital intensity, CSR score and efficiency were all rated zero) is equal to 0.357. The model also shows that, for every one unit increase in CSR, firm financial performance increases by 0.001 units (α1= 0.001). For every one unit decrease in efficiency, firm financial performance increases by 0.395 units (α2= -0.395) and for every one unit decrease in capital intensity, firm financial performance increases by 0.020 units (α3= -0.020). Since efficiency was computed as Cost of Sales/Total Sales then a high ratio would mean that the company is being inefficient and therefore the inverse relationship found in this study is expected and justifiable.

Using P-Values to test on the individual significance; a predictor variable is said to be linearly related with the response variable if it's P-Value < 0.05 (5% significance level). The findings in table 3 show that only efficiency has a significant linear relationship with firm financial performance. The implication of this study would be that commercial banks would have to put more emphasis on reducing the ratio of cost of sales to sales (efficiency) in order to increase financial performance.

Table 3: Regression Results

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig. (P-Value)
		B	**Std.Error**	**Beta**		
1	(Constant)	0.357	0.147		2.430	0.051
	CSR Score	0.001	0.001	0.347	1.329	0.232
	Efficiency	0.395	0.153	-0.839	-2.579	0.042
	Capital intensity	0.020	0.032	-0.220	-0632	0.551

Source: Computations from raw data obtained form CBK

4.4 Correlation Analysis

A correlation matrix was used to check on the concept of multi-collinearity, that is if there is a strong correlation between two predictor variables (correlation coefficient > 0.8). In a situation where two predictor variables have a correlation coefficient greater than 0.8, then one of them must be dropped from the model. As shown in table 4, none of the variables is strongly correlated with each other. Thus a model of three predictor variables (Capital intensity, CSR score, and efficiency) could be used in forecasting of financial performance among the commercial banks listed at the central bank of Kenya during the period 2007-2011.

Table 4: Predictor Variables Correlation Matrix

		Financial Performance	CSR Score	Efficiency	Capital intensity
Pearson Correlation	Financial performance	1.000			
	CSR Score	.538	1.000		
	Efficiency	-.736	-.129	1.000	
	Capital intensity	.211	-.377	-.470	1000

Source: Computations from raw data obtained form CBK

4.4.1 Goodness of Fit Test

The study further used correlation coefficient (r) to check on the magnitude and the direction of the relationship between the independent and dependent variable. Coefficient of determination (the percentage variation in the dependent variable being explained by the changes in the independent variables) and P- value were used to check on the overall significance of the model. Correlation coefficient of 0.870 indicates a strong positive correlation between the dependent and independent variables. On the other hand coefficient of determination (R2) of 0.758 shows that 75.8% of the variation in the firm performance (ROA) is explained by the changes in Capital intensity, CSR score, and efficiency, leaving only 24.2% unexplained. The regression model obtained for this study can therefore be used to forecast financial performance fairly. The adjusted R square of 63.7% also shows that the model is a fair estimate of the relationship between the variables. The P-Value of 0.028 is less than 0.05, which shows that there is a significant relationship between the dependent and independent variables used in the study.

Table 5 shows this summary

Table 5 Model Summary

Model	**R**	**R Square**	**Adjusted R Square**	**Standard E of the estimate**	**Change Statistics**				
					R Square change	**F Change**	**df 1**	**df 2**	**Sig Change(p-value)**
Dimension	.870 □	0.758	0.637	0.03846	0.758	6.256	3	6	0.028

Source: Computations from raw data obtained form CBK

4.4.2 ANOVA Test

Analysis of Variance (ANOVA) consists of calculations that provide information about levels of variability within a regression model and form a basis for tests of significance. It provides a statistic for testing the hypothesis that $\beta i \neq 0$ (there is a significant relationship between the response and predictor variables), against the null hypothesis that $\beta\ i \neq 0$ (there is no significant relationship between the response and predictor variables). Correlation exist between the response and predictor variables if P-value < 0.05. As shown in table 7, P-Value $= 0.028 < 0.05$ indicated that there is enough evidence to support the alternative hypothesis, that there is a significant linear relationship between financial performance and Capital intensity, CSR score and Efficiency.

Table 6: ANOVA

Model		Sum of Squares	df	Mean Square	f	Sig (P-Value)
1	Regression	0.028	3	0.009	6.256	0.028
	Residual	0.009	6	0.001		
	Total	0.037	9			

Source: Computations from raw data obtained form CBK

CHAPTER FIVE: SUMMARY, CONCLUSION AND RECOMMENDATIONS

5.1 Introduction

This chapter concludes the findings of the study conclusions and gives the recommendations after which it highlights the study limitations experienced in the course of the study. The chapter also highlights suggestions for further study.

5.2 Summary of findings

The study used regression analysis to establish the relationship between financial performance and CSR practice of firms listed at the central bank of Kenya. Efficiency and capital intensity of the firms were also included as control variables in the model. One major finding of the study is that there is a strong relationship between the independent variables (CSR practice, efficiency and capital intensity) used in the model and the dependent variable (ROA). As indicated in Table 4 on Predictor Variables Correlation Matrix

The correlation coefficient of 0.870 indicates a strong positive correlation between the dependent and independent variables taken together. However on the analysis of the relationship between the individual independent variables and financial performance, the results showed that only efficiency (Cost of sales/Sales) had a significant inverse relationship. This was show in table 5 of the model summary, Whereas CSR score was found to have a positive relationship with financial performance this was not significant. Capital intensity was also found to have an inverse relationship with financial performance which was not significant.

The main objective was to establish whether there exists a relationship between corporate social responsibility and financial performance of commercial banks in Kenya.

5.3 Conclusion

CSR practice is important and is practiced by commercial banks firms in the banking sector of the listed banks by central bank. Considering the findings that CSR practice does not have a significant relationship with firm performance, firms should not incur high costs on CSR with the hope of improving financial performance but rather for some other sustainability reasons. Commercial banks should enhance efficiency in the banking services so as to improve financial performance as there is a significant linear relationship between the two variables. Efficiency in the model was computed as the ratio between the cost of sales and sales therefore the firms should strive to reduce the cost of sales so as to improve their financial performance.

The CSR activities that are targeted at the community welfare are more popular and firms should engage in these activities if they are to be in line with what their competitors are doing. Involvement of the community in issues that concern them is of importance because the company is able to address relevant concerns and support from the community. Staff welfare was also found to be practiced by all banks sentences included in the audited financial reports for the period studied. Protection of the environment is also important for the banking sector. Banks should report all their CSR activities in the financial reports as these may help to improve their reputation.

5.4 Recommendations

The study recommends that if the sole motive of investment in corporate social responsibility is to improve on company performance, then this motive needs to be revised. Commercial banks seem to be investing in wrong social programs hence not leading directly to improved sales which would lead to improved profitability. Therefore need to invest in programs that improve company sales.

5.5 Suggestions for Further Research

In this study only listed commercial banks were considered. It was recommended that a similar study may be conducted in other sectors that have not been studied where such studies has not conducted. The study will however need to identify the relevant control variables given the selected for further studies.

5.6 Limitations of the study

Some of the banks did not have corporate social responsibility investment data and were therefore excluded in the analysis. To that extent therefore the results are limited to those that had data.

The findings of the study also indicate that the independent variable chosen for the study were not exhaustive and as such the study encountered a limitation in the explanatory power of the independent variable chosen for the study.

REFERENCES

Alexander, G., & Rogene, A. (1978). Corporate social responsibility and stock Market performance. *Academy of Management Journal*, 21 (3), 479-486.

Aupperle, E., Carroll, A. & Hatfield. (1985.) An empirical examination of the relationship Between corporate social responsibility and profitability. *Academy of Management Journal*, 28 (2) 446-463.

Auka, K. (2006). Factors influencing the practice of Corporate Social Responsibility of financial Instutions in Kenya. *Unpublished MBA Project, University of Nairobi*

Barasa, M. (2008). The effect of mergers and acquisitions announcement on share prices evidence on the NSE. *Unpublished MBA Project, University of Nairobi*

Barnett, M. (2007). Stakeholder influence capacity and the variability of financial returns to corporate social responsibility, *Academy of Management Review* 32, 794-816.

Bruno, F. & Nichols, T. (1990). Stockholder and stakeholder interpretations of Business ethical role, in Hoffman, W.M. & Moore, J.M. (Eds), *Business Ethics, McGraw-Hill, New York, NY, pp. 170-5.*

Cheruiyot, K. (2010). The relationship between corporate social responsibility and financial Performance of companies listed at the Nairobi Stocks Exchange, *Unpublished MBA project*, University of Nairobi.

Cooper, D., & Schindler, P. (2003). *Business Research Methods,* Eighth Edition, Tata McGraw-Hill Publishing Company Limited

Cochran, L., & Wood, R. (1984) corporate social responsibility and financial Performance. *Academy of Management Journal*, 27 (1), 42-56.

Cornell, B., & Shapiro, A. (1987). Corporate stakeholders and corporate finance. *Financial Management, 16,5-14.*

Davis, K. (1973). The Case for and against Business Assumption of Social Responsibilities'. *Academy of Management Journal,* 16(2), 312-22

Donaldson, T., & Dunfee, T.W. (1999). *Ties That Bind*, Harvard Business school press, Boston, MA.

Fauzi, H. (2009). Corporate Social and Financial performance: Empirical evidence from American companies. *GMJ, 3, Jan – June 2009.*

Freeman, E. (1984). *Strategic Management: A stakeholder Approach.* Boston: Pitman.

Friedman, M. (1970). The Social Responsibility of Business is to Increase its Profits. *The New York Times Magazine,* 13 Sept. 1970: 32-3, 124-6

Jooh, L., Niranjan, P.,& Roh, J. J. (2010). *Relationship between Corporate Sustainability Performance and tangible Business Performance*: Evidence from oil and gas industry. ISBIT, 3, sp. Issue 3 January 2011.

Klassen, R.D. & McLaughlin, C.P. (1996). The impact of Environmental Management on Firm Performance, *Management Science, 42,* 1199-214.

Margolis, J.D. & Walsh, J.P. (2001). Misery loves companies: Rethinking social Initiatives by business. *Administrative Science Quarterly*, 48, 268-305.

Margolis, J.D. & Walsh, J.P. (2001). People and profits: The search for a link between a Company's social and financial performance, Lawrence Erlbaum Associates: Mahwah, NJ.

McWilliams, A. & Siegel, D. (2000). Corporate Social Responsibility and Financial Performance: correlation or misspecification? *Strategic Management Journal, 21(5),* 603-9.

Mitchell, R. K., Bradley R. A., & Wood, D. J. (1997). Toward a theory of Stakeholder identification and salience: Defining the principle of who and what really Counts. *Academy of Management Review* 22: 853–886.

Moir, L. (2001). *What do we mean by Corporate Social Responsibility?* Corporate Governance MCB University Press; 1, (2)16-22.

Markowitz, M. (1972) Choosing socially responsible stocks. *Business and Society Review*, 1: 71-75.

Mutuku, K. (2005).The relationship between corporate social responsibility & Financial Performance, A case of Publicly Quoted Companies in Kenya, *Unpublished MBA Thesis*, University of Nairobi.

Obusubiri, M. M. (2006). A study of Corporate Social Responsibility and Portfolio Performance at the Nairobi Stocks Exchange, *Unpublished MBA Thesis*, University of Nairobi.

Waddock, S.A. & Graves, S.B. (1997). The corporate social performance: financial performance link, *Strategic Management Journal, 18 (4),* 303-19

Wagner, M., Van, P. N., Azomahou, T., &Wehrmeyer, W. (2002).The relationship between the Environmental and economic performance of firms: an empirical analysis of the European paper industry.

Wanjala, N. (2011). Factors influencing the Practice of Corporate Social Responsibility by Commercial banks in Kenya, *Unpublished MBA Thesis,* University of Nairobi. Weber, R. P. (1990), *Basic Content Analysis,* Sage, Newbury Park, CA.

Simpson, G., & Kohers, T. (2002). The Link between Corporate Social and Financial Performance: Evidence from the banking Industry, journal of business ethics. 35 (2); 97-109

APPENDIX 1

Licensed Commercial Banks in Kenya

1. African Banking Corporation
2. Bank of Africa
3. Bank of Baroda
4. Bank of India
5. Barclays Bank of Kenya
6. CFC Bank
7. Chase bank
8. Citibank
9. Credit Bank
10. Co-operative bank of Kenya
11. Commercial Bank of Africa
12. Consolidated bank
13. Development bank
14. Diamond Trust bank
15. Dubai bank
16. Eco bank
17. Equatorial Commercial bank
18. Equity bank
19. Family bank
20. Fidelity Commercial
21. Fina bank

22. First Community Bank
23. Giro commercial bank
24. Guardian bank
25. Gulf Bank
26. Habib bank
27. Imperial Bank
28. Investment and mortgages bank
29. K-Rep bank
30. Kenya Commercial Bank
31. Middle East bank
32. National Bank of Kenya
33. NIC bank
34. Oriental Commercial bank
35. Paramount Universal Bank
36. Prime Bank
37. Stanbic bank
38. Standard Charted bank
39. Trans-National bank
40. United Bank for Africa
41. Victoria Commercial bank