

**THE EFFECT OF CORPORATE SOCIAL RESPONSIBILITY ON
FINANCIAL PERFORMANCE OF 100 TOP SMALL AND MEDIUM
ENTERPRISES IN KENYA**

SHARON WANGARI SIMON

D61/79483/2012

**A RESEARCH PROJECT SUBMITTED IN PARTIAL FULFILLMENT OF
THE REQUIREMENTS FOR THE AWARD OF MASTER OF BUSINESS
ADMINISTRATION, SCHOOL OF BUSINESS, UNIVERSITY OF NAIROBI**

OCTOBER 2014

DECLARATION

I, the undersigned, declare that this is my original work and has not been presented in any other institution for any other award prior to this declaration.

Signature:..... Date:.....

Sharon Wangari Simon

D61/79483/2012

This research project has been submitted for examination with my approval as a university supervisor.

Signature:.....Date:.....

Mr. Cyrus Iraya,

Lecturer Department of Finance and Accounting

ACKNOWLEDGEMENTS

I wish to acknowledge Almighty God for the divine life and compassion in seeing me through all the achievements in my academic life. I wish to express my appreciation to my supervisor, Mr. Cyrus Iyara for whom I am most indebted for his insightful guidance and helpful comments that assisted in a long way in nurturing small idea to evolve to this end.

I also wish to thank my colleagues and friends for their comments and criticism which were also useful in one way or the other in the course of this project. The contribution and encouragements made by my family members especially for their caring support. Finally, I would like to appreciate all those who made this research project a success and will always be grateful to them.

DEDICATION

This research Project is dedicated to my husband Mr. Patrick Kioko, my children Daniel Tamale and Samuel Kioko. Special feeling of gratitude to my loving parents Simon Wambua and Elizabeth M. Simon, my brothers Vincent Mututu and Victor Mavua whose words of encouragement and push for tenacity ring in my ears.

ABSTRACT

Corporate Social Responsibility (CSR) is gaining momentum in Kenya as organisations are recognizing the vital role it plays on firms' performance. This is so mostly with the large corporations who are using it as a corporate positioning tool and have continued to enjoy high profits from positive market perception due to CSR. Whereas CSR is taken to have positive effect on financial performance, those opposed to it argue that CSR involves the undertaking of a set of actions which are potentially cost increasing. Whereas studies on effect of CSR on financial performance are intensive, the findings have been contradicting, concentrating on large firms and leaving SMEs out. This study sought to determine the effect of CSR on financial performance of small and medium sized enterprises in Kenya using the top 100 SMEs. The study used descriptive survey research design with data being obtained from secondary sources which were the published financial statements, Chairman's Statement and notes to the financial statements for five years period from 2009 to 2013. The data obtained was analyzed using SPSS version 21 with multiple regressions being used to show the relationship between dependent and independent variables. The significance of the results was determined using Z tests, ANOVA and coefficient of correlation and determination. The study found CSR has significant positive effect on financial performance of small and medium sized enterprises in Kenya. The study also found that size of SME has significant effect on profitability where bigger SMEs have better financial performance than small ones. SME industry was also found to affect financial performance with SMEs in service industry having highest financial performance followed by trading and manufacturing being least profitable as measured by return on assets. The study recommends for more investment in CSR as a way of boosting SMEs profitability.

TABLE OF CONTENTS

DECLARATION.....	ii
ACKNOWLEDGEMENTS	iii
DEDICATION.....	iv
ABSTRACT.....	v
LIST OF CHARTS AND FIGURES.....	viii
LIST OF TABLES	ix
LIST OF ABBREVIATION.....	x
CHAPTER ONE	1
INTRODUCTION.....	1
1.1. Background of Study	1
1.1.1. Corporate Social Responsibility	2
1.1.2. Financial Performance	4
1.1.3. Corporate Social Responsibility and Financial Performance	5
1.1.4. Small and Medium Enterprises in Kenya	7
1.2. Research Problem	9
1.3. Research Objective	11
1.4. Value of the Study	11
CHAPTER TWO	13
LITERATURE REVIEW	13
2.1 Introduction.....	13
2.2 Theoretical Framework.....	13
2.2.1 Agency Theory.....	14
2.2.2 Good Management Theory	15
2.2.3 Slack Resources Theory.....	16
2.3 Determinants of SMEs Financial Performance.....	16
2.3.1 Corporate Social Responsibility	16
2.3.2 Size.....	17
2.3.3 Industry	17
2.4 Empirical Review.....	18
2.4.1 International Evidence	18
2.4.2 Local Evidence.....	20
2.5 Summary of Literature Review.....	21
CHAPTER THREE	23
RESEARCH METHODOLOGY	23

3.1	Introduction.....	23
3.2	Research Design.....	23
3.3	Population	23
3.4	Data Collection Techniques.....	24
3.4.1	Data Validity and Reliability	24
3.5	Data Analysis Techniques.....	25
3.5.1	Analytical Model	25
3.6.2	Test of Significance	26
	CHAPTER FOUR.....	27
	DATA ANALYSIS AND INTERPRETATIONS.....	27
4.1	Introduction.....	27
4.2	Descriptive Statistics.....	27
4.2.1	Response Rate.....	27
4.2.2	Industry of Small and Medium Sized Enterprises	27
4.2.3	Small and Medium Sized Enterprises Engagement in CSR Activities.....	28
4.2.4	Forms of Small and Medium Sized Enterprises CSR Activities	29
4.2.5	Amount Spent on CSR.....	30
4.2.6	SMEs Industry and CSR activities.....	31
4.2.7	SMEs Profitability	32
4.3	Correlation Analysis	33
4.4	Regression Analysis.....	34
4.4.1	Model Summary	34
4.4.2	Model Analysis of Variance.....	34
4.4.3	Model Analysis of Variance.....	35
4.5	Discussion and Interpretation of the findings	35
	CHAPTER FIVE	38
	SUMMARY, CONCLUSIONS AND RECOMMENDATIONS	38
5.1	Introduction.....	38
5.2	Summary.....	38
5.3	Conclusions.....	40
5.4	Policy Recommendations	41
5.5	Limitations of the study	42
5.6	Suggestions for further study	43
	REFERENCES.....	45
	APPENDICES.....	49
	APPENDIX I: 2013 TOP 100 SMES.....	49

LIST OF CHARTS AND FIGURES

Figure 4.1: Industry of SMEs.....	28
Figure 4.2: SMEs engagement in CSR	29
Figure 4.3: CSR Activities.....	30
Figure 4.4: Amount spent on CSR.....	30
Figure 4.5: Average amount spent on CSR per industry	31
Figure 4.6: Top 100 SMEs profitability.....	32

LIST OF TABLES

Table 4.1: CSR and SMEs Industry	31
Table 4.2: Correlation Analysis on Independent Variables and Profitability	33
Table 4.3: Overall Model Summary	34
Table 4.4: Overall Model ANOVA	34
Table 4.5: Overall Model Coefficients	35

LIST OF ABBREVIATION

CSR	Corporate Social Responsibility
GDP	Gross Domestic Product
GOK	Government of Kenya
ROA	Return on Assets
ROE	Return on Equity
SME	Small and Medium Sized Enterprises
SPSS	Statistical Package for Social Sciences

CHAPTER ONE

INTRODUCTION

1.1 Background of Study

Engagement in corporate social responsibility (CSR) implies extra cost for the company, the first objective of management is profit maximization; companies need more certainties about the increase in value that the introduction of CSR brings (Ghelli, 2013). Friedman (1970) argues that there is one and only one social responsibility of business, which is to use its resources and engage in activities designed to increase its profits so long as it stays within the rules of the game, which means to, engage in open and free competition without deception or fraud. Reich (2007) contends that, as a result of high competition in the market, instead of engaging in CSR projects, which harm themselves, corporations need to concentrate on activities that have positive effects and gains. If the aim of business is to maximize profits, what are the motives that lead organizations to engage in social projects yet they are not profit generating?

This might be explained by the view that CSR projects provide sustainability for organizations long term profits; therefore it could be a tool for profit maximization. In the literature, it is argued that organizations engage in CSR projects for commercial benefits to increase the value of the organizations for society and government (Sachs, Maurer, Ruhli, and Hoffmann, 2006). CSR projects help organization differentiate

themselves from other companies (Morsing and Schultz, 2006), which could have a positive effect on stakeholders (Jamali and Mirshak, 2007).

The global importance in CSR is on the rise. Beyond gaining economic profit, more and more organizations respect social issues related to the surroundings where they operate. Environmental protection and human rights, customer relationship management, developing the local environment and community, supporting suppliers and increasing supplier diversity, improving education and improving healthcare conditions in developing countries are among most addressed social issues. Proponents of CSR claim that organizations need to respect interest and contribute to social benefits of society while sustaining operating activities. In contrast, opponents claim that, organizations do not necessarily need to consider the interest of wider society, since the existence of organizations already provides opportunities for society; organizations need to focus on their main activities in order to maximize profit (Zengin, 2010). This is also depicted by Isaksson and Steimle (2009) who view CSR as the company's commitment to behave socially and environmentally responsible while striving for its economic goals. Hence, CSR actions ought to be correlated with the financial performance and outcomes of firms (Theofanis, 2010).

1.1.1. Corporate Social Responsibility

Corporate Social Responsibility (CSR) refers to the firm's considerations of, and response to, issues beyond the narrow economic, technical, and legal requirements of the firm to accomplish social benefits along with the traditional economic gains which the firm seeks (Davis, 1973). CSR is also viewed as the continuing commitment by business to behave ethically and contribute to economic development while improving

the quality of life of the workforce and their families as well as of the local community and society at large (World Business Council for Sustainable Development, 1999). There is also a disagreement on the components of CSR among those that view CSR as an ethical attitude and those who argue that it is a firm's strategy (Wan-Jan, 2006). Stainer (2006) states that CSR concept is to show that ethical principles, from wherever derived, can improve reasoning and harmonize decisions, especially in complex situations and thus enhance performance (Theofanis, 2010).

Companies in Kenya pursue CSR by a way of improving the staff welfare, implementing community development programmes such as building schools, dispensaries, drilling bore holes, funding sporting activities, the establishment of scholarship funds for needy children rehabilitation and maintenance of roundabouts within Central Business District among others. These corporations are under moral obligation to act in fair, transparent and accountable manner. Corporate Social Responsibility among Kenyan firms is a marketing strategy where businesses ensure that their products or services are visible and in the process rebrand in such a way to reposition them in the market. Most business firms in Kenya will engage in CSR only if such initiatives give them a competitive advantage in marketing their products. They undertake CSR to reduce pressure from trade unions, environmental organisations, consumer watch groups and positioning themselves as market leaders in their respective fields (Wafula, 2012).

Measuring CSR has been a subject of discussion with Waddock and Graves (1997) pointing out the problem of measuring CSR and also the unclear relationship between CSR and financial performance. Wood (2010) measured CSR by using social reports,

environmental reports, annual reports of social or environmental disclosures and ethical practices adopted by the companies. Mahoney and Roberts (2007) calculated a composite measure of CSR, based on community relations, diversity, employee relations, environment, international, product safety, and other ratings. Soana (2009) pointed out that social performance is best measured by five different methods: content analysis, surveys carried out using questionnaires, reputational measures, unidimensional indicators and ethical ratings. While these measures adopted may be good measures of CSR, their ratings are subjective and hard to measure. For this study, CSR will be determined quantitatively by the total amount spent per annum on CSR.

1.1.2. Financial Performance

Firm performance is measured either from the accounting or market view. McGuire *et al.*, (1988) pointed out the problems that may occur, using accounting based measures and market based measures. Accounting measures are susceptible to differential accounting procedures and managerial manipulation and market-based measures, due to investor's evaluation, may not be sufficient. The advantage of market-based measures is that they can estimate the value (or the cost) of companies adopting certain strategies to be socially responsible, conditional on the existing information (Goukasian and Whitney, 2008). Measurement of firms' financial performance can be based on: profitability, liquidity, solvency, financial efficiency and repayment capacity (Fiori *et al.*, 2009).

The most popular measures of corporate financial performance are return on assets (ROA) and return on equity (ROE) (Griffin and Mahon, 1997). ROA represents the profitability of the firm with respect to the total set of resources, or assets, under its

control (Hull and Rothenberg, 2008). In this study, financial performance will be measured by return on assets based on the fact that it shows the firms' ability to utilise its assets in generating wealth for shareholders.

1.1.3. Corporate Social Responsibility and Financial Performance

The linkage between's CSR and financial performance has remained unclear with literature showing contradiction information. Literature available can be grouped into three; those which find positive relationship, suggesting that CSR improves firms' value, those which found negative relationship, adopting the idea that firm must use its resources only to maximize its profits and otherwise it will have adverse results, and those which found neutral relationship. CSR may also be linked with subsequent financial performance as to find out the degree financial performance is improved, also it can be linked with past firm performance to explore if firms with high financial performance take on CSR actions (Theofanis, 2010).

Based on this interrelationship that financial performance and CSR determines the magnitude of each other; Waddock and Graves (1997) based on the theories of "slack resources" and "good management" proved that better financial performance results in improved CRS and improved CSR led to improved financial performance. This presents a serious conflict among researchers on whether CSR is independent or dependent variable evaluating the relationship between CSR and financial performance. Moskowitz (1972) suggested that the high listed companies in terms of CSR reported higher than average stock returns while Bird *et al.*, (2007), concluded that firms who engaged in CSR activities will be rewarded in the market place but market seem to evaluate more negatively firms which do not include CSR strategy in

their business. Nelling and Webb (2009), using ROA and annual stock return as dependent variables, found positive and significant relationship with CSR score.

The relationship between CSR and corporate performance has been found to be both negative and positive as pointed out previously. Feldman *et al.*, (1997) revealed that an improvement in environmental management system and future environmental performance will increase shareholder wealth by five percent. On contrast, negative relationship was proved in the study of Wood and Jones (2005). Brammer *et al.*, (2006) found that the overall CSR measure has significant but negative effect on stock returns. Evaluating each social performance indicator, they found that the measure of employee performance has significant and negative effect on stock returns, community measure has positive but not significant effect and environment measure has negative and no significance too. In addition, Vance (1975) found a negative correlation between rankings of social responsibility and stock market performance. Wood and Jones (2005), finds that negative impact on abnormal stock returns after the announcement of CSR actions in indicating that market does not recognize CSR efforts.

Firm performance and CSR are affected by several factors. Waddock and Graves (1997) indicates that firm size (total sales, total assets and number of employees), risk (long-term debt to total assets ratio) and industry affects the relationship between firm performance and CSR. Size plays an important role because; small companies cannot adopt CSR activities in the same extent as large ones. Brammer *et al.*, (2006) indicate that market capitalisation and risks facing the company as having significant impact on firm's attitude against CSR because of savings, costs and market. The kind of industry

and its characteristics may create problems in exploring CSR actions (Waddock & Graves, 1997).

1.1.4. Small and Medium Enterprises in Kenya

Small and medium-sized enterprises (SMEs) are classified differently in various countries. Firms which employ less than five full-time workers are referred to as micro enterprises. Those employing between 5 and 49 workers are called small scale enterprises and those with 50-99 full-time employees are medium enterprises (GoK, 2005). In Kenya, the SMEs play an important role in employment and wealth creation, income distribution, accumulation of technological capabilities and spreading the available resources. According to the Economic Survey (GoK, 2012), the SME sector contributed 79.8% of new jobs created in the year 2011 with 89.7% of new jobs created in 2013 being created by the small and micro enterprises sector (GoK, 2013).

The SMEs sector is very volatile and experience a high degree of business closure and shrinkage, as a result the government has been making numerous efforts to assist the development of the SME sector. The high SMEs mortality rate implies that SMEs are limited in their ability to create long-term sustainable employment and may also be responsible for the greatest number of job and wealth losses. Despite the many challenges and difficulties of the SMEs, the sector has great potential for increased employment creation. Some studies carried out indicate that most SMEs fail due to lack of appropriate financing and financial services (Ochanda, 2014).

Kenya is a low income country faced with major development challenges, the economy is dominated by Small and Medium Enterprises (SMEs) and firms lack sufficient resources to implement CSR programs, the profits earned barely allows them to adopt voluntary social responsibility. CSR projects have been left for big companies who have the financial muscle or donors who have their own conditions for disbursing funds. The big companies have continued to make substantial profits due to their strategic approach to CSR which they use as a means of promoting their products and services. Indeed these firms' activities are recognised as legitimate and consistent with the expected social norms (Wafula, 2012).

CSR adoption by SMEs can affect the long-term competitiveness of the firms. Three categories of CSR actions with a high impact on competitiveness have been identified as ethical production management, environmental considerations and customer value creation (Tantalo, Caroli, and Vanevenhoven, 2012). Adoption of CSR can stimulate the innovation of SMEs, by implementing stakeholder engagement and local networking. Positive outcome of local networking and co-operation amongst stakeholders enables SME to fully deploy its synergies, and scope economies applied not only to productive aims (Battaglia, Bianchi, Frey and Iraldo, 2010).

Being socially responsible can help SMEs to succeed, increase profit and overall performance. However, for SMEs to be acknowledged as socially responsible, they need not to focus only on business ethics and urban affairs but also on environmental affairs. Environmental sustainability and growth have been the focus of attention in recent years, although, in the past years, most organizational policies on SMEs focus on growth at the expense of environmental quality, these policies were premised on the

expectation that gains in material well-being would far exceed losses incurred in environmental degradation. Realistically, SMEs may simply be contented to survive as long as they are making decent living. Hence, there is little need to engage in environmental sustainability (Olusanya, Suleiman and Oyebo, 2012). Lawal and Sulaimon (2007) note that SMEs are only motivated to adopt environmental management policies by legislations and chain pressures, the former is unlikely to be readily accepted by resource constrain of SMEs and the latter in any way just transfers the large firms agenda into the smaller firms without accounting for the complex and heterogeneous nature of this sub-sector. To cope with the issue of environmental management, SMEs need not only to develop specific activities and strategic responses at organizational level but also facilitate the evolution of managerial values and beliefs toward higher level of environmental management; in addition, there is need for governments backing of environmental management by assisting SMEs that are involved in environmental sustainability (Olusanya *et al.*, 2012).

1.2 Research Problem

Corporate Social Responsibility is deliberate action where organisations adopt strategies aligning their operations to the interest of stakeholders. However, pursuing Corporate Social Responsibility is a voluntary decision for business even though society pressures have influenced many firms to integrate social and environmental concerns in their strategic plans (Nelling and Webb,2009). Whereas CSR is taken to have positive effect on financial performance, those opposed to it argue that CSR involves the undertaking of a set of actions which are potentially cost increasing (such as higher attention to workers conditions within the firm and in subcontracting companies, adoption of more environmentally, and costly productive processes). These

sources of additional reputational costs need to be compensated by some potential benefits to be economically sustainable. However, studies focused their attention on big firms, leaving SMEs outside the whole picture (Ghelli, 2013).

In Kenya, CSR is gaining momentum as organisations recognise the important role it plays in business performance. This is so mostly on the large corporations who are using it as a corporate positioning tool and have continued to enjoy high profits from positive market perception due to CSR. In pursuing CSR, companies have also benefitted from operational efficiency through the reduction of waste with policies requiring organisation to protect their environment by using eco-friendly systems for example, 'going green' that ensures paper usage is drastically reduced as the use of electronic mail is the modern trend of communication. Corporate disclosures of performance in social and environmental areas have helped businesses build a good reputation based on recognition of their efforts by stakeholders. It is also important to use CSR as a means of meeting stakeholder's demands, since this allows the business to explore profitable opportunities with the support of stakeholders (Wafula, 2012).

Numerous studies have been done on CSR in Kenya but have mainly been in the context of big firms where compelling evidence that CSR can be used as a strategic tool to enhance the competitiveness. Okwoma (2012) studied the effect of corporate social responsibility on the financial performance of commercial banks in Kenya where CSR was observed to have positive effect on profitability for large and medium banks with a negative insignificant effect on small banks. Mwangi (2011) did a study on relationship between CSR and financial performance of companies quoted at NSE. The results of the analysis showed that there was an upward trend in performance of listed firms on the NSE as well as upward trend in the amount of money investment in

CSR programs. Mwangi and Jerotich (2013) studied the relationship between corporate social responsibility practices and financial performance of firms in the manufacturing, construction and allied sector of the Nairobi Securities Exchange. The study found an insignificant positive relationship between corporate social responsibility practice and financial performance.

None of these studies have examined CSR from a SMEs point of view irrespective of the fact that size of a firm has been found to be an important determinant of effect of CSR on financial performance in addition to conflicting findings by previous studies. This study therefore sought to bridge this gap by determining the effect on CSR on financial performance of SMEs. It was to answer the question, what is the effect of CSR on financial performance of small and medium sized enterprises in Kenya?

1.3 Research Objective

To determine the effect of corporate social responsibility on financial performance of small and medium enterprises in Kenya

1.4 Value of the Study

The study is of importance to SME managers, the government, policy formulators, researchers and academicians. The management of firms charged with the responsibility of deploying capital with an objective of maximizing shareholders wealth. This study is of significant benefit to them by providing information on how CSR affects financial performance of their firms.

The study on SMEs is very important to the government and policy makers in Kenya due to the contribution of SME to the Kenyan economy in both terms of employment

and GDP. Policy makers will be enlightened to make policies relating to CSR and ascertain the appropriate guidelines to be put in place for governing SMEs. The research has also added value to the business community especially SME entrepreneurs who have or are in the process of setting up their business. This has allowed them to practice corporate social responsibilities as it improves its financial performance. The study has also added value to the academic community. This is because the study has shed more light in the CSR activities on the Kenyan SMEs sector and its impact on the financial performance as well as for those who want to undertake further research on CSR.

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

The chapter focuses on theoretical and empirical literature. It contains theories and literature review on studies that have been done on past on CSR and financial performance. The chapter begins with theoretical framework which consists of theories related to CSR and its relation to financial performance and ends with a chapter summary.

2.2 Theoretical Framework

Numerous studies have attempted to explore the nature of relationship between firm's profitability and its social performance. Different researchers conducted different studies with different methodologies in attempt to prove that CSR has an impact on financial performance of a firm and others empirical studies. In spite of all these studies, there is still lack of consensus among the results of different researchers on the nature of relationship between corporate social responsibility and corporate financial performance. The study was guided by theories which presents set of arguments that require further research which include agency theory, good management theory slack resources theory.

2.2.1 Agency Theory

The theory was proposed by Jensen and Meckling (1976). The theory recognizes a corporation as merely a nexus of contractual arrangements between managers and shareholders. Thus, managers are assumed to be agents of shareholders who are likely to pursue corporate actions that advance their own personal interests at the expense of shareholders' value. Each party (organization or agent as a stakeholder) plays different roles for other parties. Organizations are bound together by the contracts each agent has and play a crucial role on contract between the parties. These links between organizations and agents mean that every organization has responsibility to other agents and organizations. Organizations balance the benefits of each party by using managerial tools and actions such as CSR, and communicate their actions through annual reports and websites.

Sunder (1997) proposition of set of contracts, CSR is viewed as actions taken by organization for creating value to agents contracting with organizations. This goes beyond economic value adding activities; to include the social value adding process. This theory directs organizations to be socially responsible since they are social agents contracting with other agents, as a part of chain; their aim goes beyond profit-maximization.

The theory assumes that organization constructs the business environment and agents are the members of social society. Therefore, each individual either voluntarily or involuntarily plays the role of an agent. The theory implies that CSR is not a voluntary undertaking and affects financial performance. From the theory, the role of

organizations is seen as to honour a “set of contracts” among employees, customers, managers, shareholders, suppliers, auditors among others.

2.2.2 Good Management Theory

The theory was proposed by Waddock and Graves (1997) and predicts that CSR and financial performance are generally positively related across a wide variety of industry and study contexts. According to this theory, the satisfaction of various stakeholder groups is instrumental for organizational financial performance. The theory argues that the implicit and explicit negotiation and contracting processes entailed by reciprocal, bilateral stakeholder–management relationships serve as monitoring and enforcement mechanisms that prevent managers from diverting attention from broad organizational financial goals (Jones, 1995).

The theory implies that investment in CSR leads to increased financial performance since by addressing and balancing the claims of multiple stakeholders; managers can increase the efficiency of their organization’s adaptation to external demands. High corporate performance is viewed not only as coming from the separate satisfaction of bilateral relationships but also from the simultaneous coordination and prioritization of multilateral stakeholder interests. These strategic and tactical steps may be necessary to reduce the likelihood of the organization’s becoming stuck in a high-density network (Hill and Jones, 1992).

2.2.3 Slack Resources Theory

The theory suggests a positive relationship between CSR and financial performance just like good management theory. However, the theory proposes a different temporal ordering, that CSR is directly associated with subsequent financial performance. High levels of CSR may provide the slack resources necessary to engage in corporate social responsibility and responsiveness (Waddock & Graves, 1997). CSR often represents an area of relatively high managerial discretion, the initiation or cancellation of voluntary social and environmental policies may, to a large extent, depend on the availability of excess funds (McGuire *et al.*, 1988). The theory implies bidirectional causality between corporate social performance and financial performance. Hence, CSR leads to high financial performance and also high performance leads to more investment in CSR

2.3 Determinants of SMEs Financial Performance

Each company differs on how it implements CSR; if it implements the differences depend on such factors as the specific company's size, the particular industry involved and CSR activities the company is engaging in.

2.3.1 Corporate Social Responsibility

CSR is aimed at maximizing shareholder value measured by profitability. CSR activities are also viewed as strategic goal of achieving competitive advantages, which would produce long-term profits. In this case, CSR is used to achieve competitive advantage by investing in philanthropic activities, identifying strategic social and ethical resources and capabilities and through disruptive innovation, a means of attending to the bottom of economic pyramid. CSR is also viewed from marketing

perspective in which, it is the process of formulating and implementing marketing activities that are characterized by an offer from the firm to contribute a specified amount to a designated cause when customers engage in a revenue-providing exchanges that satisfy organizational and individual objectives (Okwoma, 2012). This implies the role of CSR s a determinant of firms' profitability.

2.3.2 Size

The size of the company is an important determinant of firm profitability since big companies have wider visibility and also enjoys economies of scale. Studies report how smaller firms tend to invest less in CSR than bigger companies since bigger companies have greater visibility they engage in more and better social initiatives than smaller firms with lower visibility. Bigger firms have more resources that can be invested in CSR activities and attract more attention from different stakeholders whose needs are of primary importance (Waddock & Graves, 1997). For this reason, studies suggest taking of the firm size into account when studying relationship between CSR and performance.

2.3.3 Industry

Industry factors like competition, regulation and nature of the industry customers highly influences firms' financial performance. In addition firms that come from different industries have to deal with different external context, with distinct environmental, social and financial concerns, as well as different stakeholders' needs. When making a study across different industries there are some industry-specific effects that are masked and covered by the overall research and hence incorporation of industry as a determinant in a multi-industry research tends to confound the relationship between CSR and financial performance. It is important to understand that

in a single industry both the external and internal pressures experienced by different firms are expected to be the same (Ghelli, 2013).

2.4 Empirical Review

Based on previous studies, the relationship between CSR and financial performance could be positive, negative, or neutral. Empirical literature shows that the effect of CSR on financial performance is both positive and negative with other studies not being conclusive.

2.4.1 International Evidence

Theofanis (2010) studied corporate social responsibility and financial performance on Greek companies. Analysis of CSR as the independent variables was done using content analysis of sustainability reports in generating a compound score of company's CSR level. The study found a positive and significant relationship between stock returns and CSR. The model was found to be statistically significant and results showing that a company which adopts CSR strategy could be evaluated positively by the market and its stakeholders. This result concluded that a company which adopts CSR strategy and practices may obtain higher stock values due to the fact that stakeholders (shareholders) evaluate positively these activities. Study recommendations are that managers to implement CSR actions in a greater extent to enhance firm market efficiency and use of accounting measures and content analysis to measure financial performance and CSR respectively.

Marc, Frank, Schmidt and Rynes (2003) studied corporate social and financial Performance. The study used the following constructs to measure CSR; CSR

disclosures; CSR reputation ratings; social audits, CSR processes, and observable outcomes; and managerial CSR principles and values. The results of the meta-analysis showed that there is a positive association between CSR and corporate financial performance across industries studied. This meta-analysis also found that the relationship between CSR and financial performance tends to be bidirectional and simultaneous, with reputation appearing to be an important mediator of the relationship.

Leonardo, Stefania and Damiano (2007) studied corporate social responsibility and corporate performance using evidence from a panel of US listed companies. The study finds that CSR is meant to redirect the focus of corporate activity from the maximization of shareholders to that of stakeholders interests and observe in fact that workers in CSR firms produce total sales per employee but a smaller portion of earning goes to shareholders through returns on equity. The “penalty” that social responsibility imposes on shareholders was found to be compensated by increased earnings through return on assets. The study also found negative consequences arising when a CSR stance is abandoned.

Ghelli (2013) studied corporate social responsibility and financial performance using fortune 500 data. The study found that in the manufacturing sector the relationship between CSR and performance was positive significant in both directions, while in the retail trade industry the relationship was in some cases even negative and never significant. The study concluded that depending on the sector in which the analysis is conducted the results will be different. The manufacturing and retail trade industries are two different sectors: the way in which the businesses are run, the differences in

the environment and context in which they operate, and the different needs that the stakeholders have, could explain the difference in the results.

2.4.2 Local Evidence

Wafula (2012) examined corporate social responsibility from a Kenyan firms' perspective. The study analysed the activities of the selected companies in Kenya to help in understanding the impact of CSR on their performance. The study found that many organisations are recording both tangible and intangible benefits as a result of incorporating social responsibilities in their business strategies. The perception that CSR is a voluntary activity is gradually changing as institutions work hard to achieve sustainable growth and development through social programs. The study concluded that the assumption that organisations will always act on the interest of the wider society to bring social change is misplaced because these entities are formed primarily to look after the interest of their owners; CSR is used as a tool for advancing organisation's objectives not necessarily related to social responsibility.

Okwoma (2012) studied the effect of corporate social responsibility on the financial performance of commercial banks in Kenya. This study used a longitudinal research design and covered the year 2007 to 2011 both years inclusive. Financial performance was measured by use of accounting ratios that included ROA, ROE and data obtained from supervisory reports compiled by central bank of Kenya. CSR was measured using financial spending on CSR activities. The study found that CSR had a positive and significant effect on ROA and ROE. The study further found that CSR contributed significantly to the financial performance of large and medium size commercial banks but did not have any significant effect on the ROA of small commercial banks.

Mwangi and Jerotich (2013) studied the relationship between corporate social responsibility practices and financial performance of firms in the manufacturing, construction and allied sector of the Nairobi Securities Exchange. The study used regression analysis to establish the relationship between financial performance and CSR practice of firms listed in the Manufacturing, Construction and allied Sector of the NSE. Efficiency and capital intensity of the firms were also included as control variables in the model. The study found is that there was a strong relationship between the independent variables (CSR practice, efficiency and capital intensity) used in the model and the dependent variable (ROA). Whereas CSR score was found to have a positive relationship (correlation coefficient of 0.7407) with financial performance this was not significant.

2.5 Summary of Literature Review

Based on the literature review, the relationship between CSR and financial performance could be positive, negative, or neutral. An effort to meet stakeholders' expectation, every company should try to improve corporate social performance from time to time and, at the same time, the economic/financial should also be improved according literature reviewed. However, question regarding which one between corporate social performance and financial performance come first has emerged. In addition, empirical literature shows that the effect of CSR on corporate performance is both positive and negative with other studies not being conclusive.

There is an extensive debate concerning the legitimacy and value of being a socially responsible business. There are different views of the role of a firm in society and

disagreement as to whether wealth maximization should be the sole goal of a corporation. Most studies have identified certain benefits for a business being socially responsible, but most of these benefits are still hard to quantify and measure. A number of theories have been reviewed explaining the reasons why corporate should undertake CSR which include Agency theory, Slack resource theory and good management theory. Under the agency theory, CSR is seen as an honour of the contract between corporate and parties. Slack resource theory argues that a company should have a good financial position to contribute to the corporate social performance. Conducting the CSR needs some fund resulting from the success of financial performance. According to this theory, financial performance comes first. Good management theory holds that social performance comes first. Based on the theory, a company perceived by its stakeholders as having a good reputation will ease the company to get a good financial performance. However, researchers have focused their attention on big firms, leaving SMEs outside the whole picture.

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

The chapter contains the research methodology facets and procedures followed in the execution of the research work which entails: the research design, target population, data collection and data analysis procedures. The study sought to determine the effect of CSR and financial performance of SMEs in Kenya.

3.2 Research Design

Descriptive designs explain phenomena as they exist and are often used to obtain information on the characteristics of a particular problem or issue while correlation studies establish relationships between various variables. Research design is a roadmap of how one goes about answering the research questions. A descriptive research design determines and reports the way things are. A descriptive research design is used when data are collected to describe persons, organizations, settings or phenomena. The design also has enough provision for protection of bias and maximized reliability (Mugenda & Mugenda, 2003).

3.3 Population

Population refers to an entire group of individuals, events or objects having common observable characteristics in which the results will be generalized in the target population (Mugenda & Mugenda, 2003). The study population was year 2013 top 100 SMEs in Kenya (See appendix I). According to Kenya's Top 100 Survey, an initiative

of KPMG and Kenya Business Daily owned by the Nation Media Group, the Survey seeks to identify Kenya's fastest growing medium sized companies in order to showcase business excellence and highlight some of the country's most successful entrepreneurship stories (Business Daily, 2014). Top 100 companies rank ahead of their peers in terms of revenue growth, profit growth, returns to shareholders and cash generation/liquidity and continuously have succeeded in growing its market position in the industries in which it operates over time, and this growth has translated into both returns for its shareholders and a fairly sound financial position. A census survey was carried out.

3.4 Data Collection Techniques

Data was collected from secondary data sources which were obtained from annual financial statements. The study covered a period of five years from 2009 to 2013. CSR information was obtained from Published financial Statements, Chairman's and statement notes to the financial Statement.

3.4.1 Data Validity and Reliability

Mugenda & Mugenda (2003) asserted that, the accuracy of data to be collected largely depended on data collection instruments in terms of validity and reliability. Validity refers to the degree to which results obtained from the analysis of the data actually represents the phenomenon under study. Validity and reliability was maintained by obtaining all the information required from secondary data sources which were published. Reliability on the other hand refers to a measure of the degree to which instruments yield consistent results (Mugenda & Mugenda, 2003).

3.5 Data Analysis Techniques

Data collected 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 to determine the score for SMEs CSR. The study employed regression analysis as the main statistical method to analyse the data.

3.5.1 Analytical Model

The study employed multiple regression analysis as the main statistical method to analyse the data. Data analysis was done using SPSS version 21 where financial performance was the dependent variable and CSR as the independent variable as shown in equation:

$$ROA = \alpha + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + e_t$$

ROA = Financial Performance as measured by Return on Assets

$$ROA = \frac{\text{Net profits}}{\text{Total Assets}}$$

α = Constant amount (what the company earns with zero amount spent on CSR activities. The amount can vary depending on the company size and industry)

X1 = CSR as measured by total amount spent on CSR per year as a percentage of assets

X2 = Size as measured by the turnover as a percentage of assets

X3 = Industry type as measured by dummy variables where;

1. Manufacturing,
2. Trading and

3. Service

$\beta_1, \beta_2, \beta_3$ = Coefficients of the various independent variables

e_t = Error term

3.6.2 Test of Significance

Analysis was done using SPSS version 21 and the coefficient of determination (R^2), Pearson coefficient of correlation (R), z-values, t-values and F-values determined and used in making statistical inference. The coefficient of correlation showed the nature of the relationship between the independent and depend variables.

CHAPTER FOUR

DATA ANALYSIS AND INTERPRETATIONS

4.1 Introduction

This chapter contains the findings and results of the application of the variables using techniques mentioned in chapter three. Specifically, the data analysis was in line with the objective of the study which was to determine the effect of corporate social responsibility on financial performance of small and medium enterprises in Kenya.

4.2 Descriptive Statistics

4.2.1 Response Rate

The information relating to 100% of the studied SMES was obtained implying 100% response rate. This could be attributed to the fact that the study used secondary data and hence did not require investment of respondents' time. In addition, the information was obtained from collection of the financial statements presented by top 100 SMEs and hence removing from the researcher the hustle of visiting specific firms.

4.2.2 Industry of Small and Medium Sized Enterprises

The study started by gathering background information from secondary sources relating to the specific SME. This was considered vital in enabling the researcher to make conclusions relating to firm or industry specific factors affecting profitability of small and medium enterprises.

Out of the 100 studied firms, 47% were in service industry, 33% in trading and 20% in manufacturing. The results of the findings are presented in figure 4.1 below. Waddock and Graves (1997) found that the industry in which a firm operates affects the relationship between firm performance and CSR and industry characteristics may create problems in exploring CSR actions.

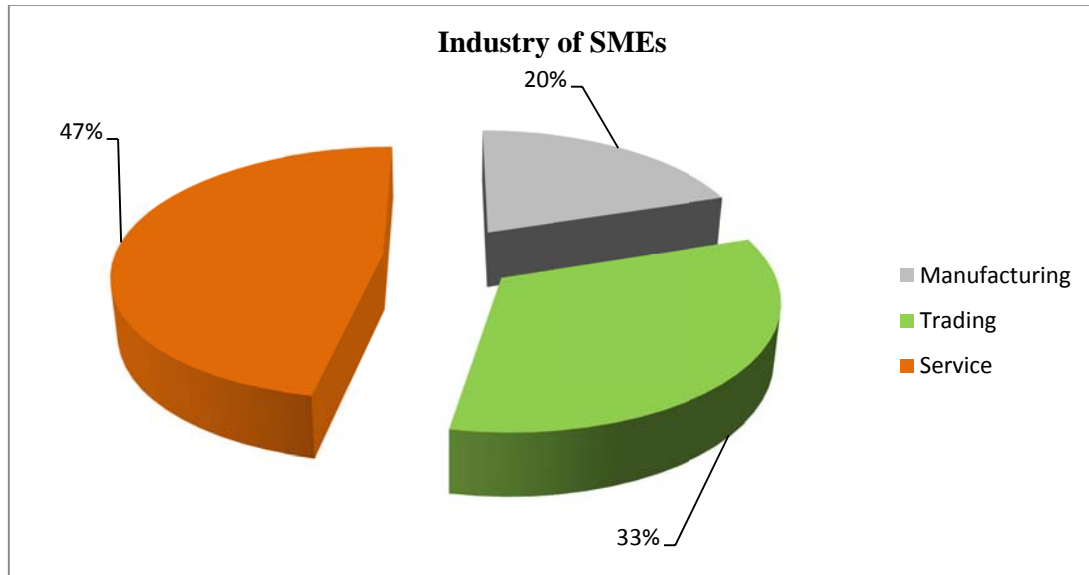


Figure 4.1: Industry of SMEs

Source: Study Data

4.2.3 Small and Medium Sized Enterprises Engagement in CSR Activities

The analysis involved carrying out content analysis on the disclosures on the financial statements and amount spent on corporate social responsibility. Figure 4.2 below shows that 93% of the SMEs at least were involved in CSR for the five periods with 7% of the SMEs not seen to be involved in CSR at all for the period or the same was never disclosed.

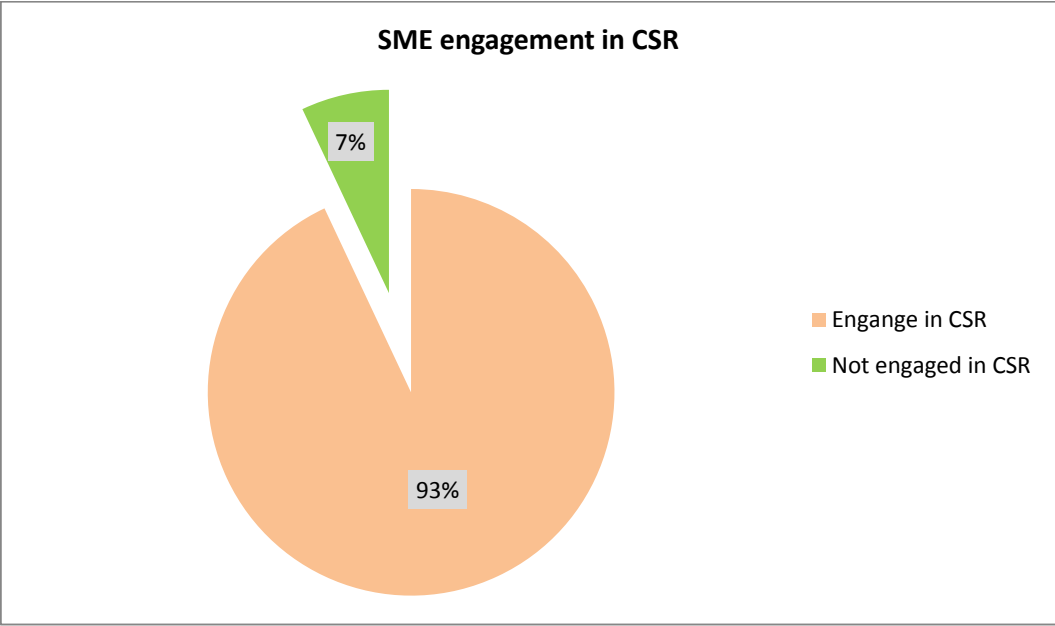


Figure 4.2: SMEs engagement in CSR

Source: Study Data

4.2.4 Forms of Small and Medium Sized Enterprises CSR Activities

This was obtained from content analysis from notes accompanying disclosures to financial statements on activities the amount spent on corporate social responsibility was applied. As shown in figure 4.3 below, ethical business was ranked to be the highest CSR activity whereby 74.2% of the SMEs disclosed carrying ethical business as the main CSR activity. Vulnerable group welfare that includes children home support was ranked second with 62.4% of the SMEs engaging in it. 46.2% of the SMEs were engaging in environmental activities including cleaning, planting trees and drainage construction and unblocking. Other CSR activities were eradication of social evils (16.1%), HIV education (22.6%), Human rights (2.2%), transport and infrastructure (9.7%) and health care provision (18.3%).

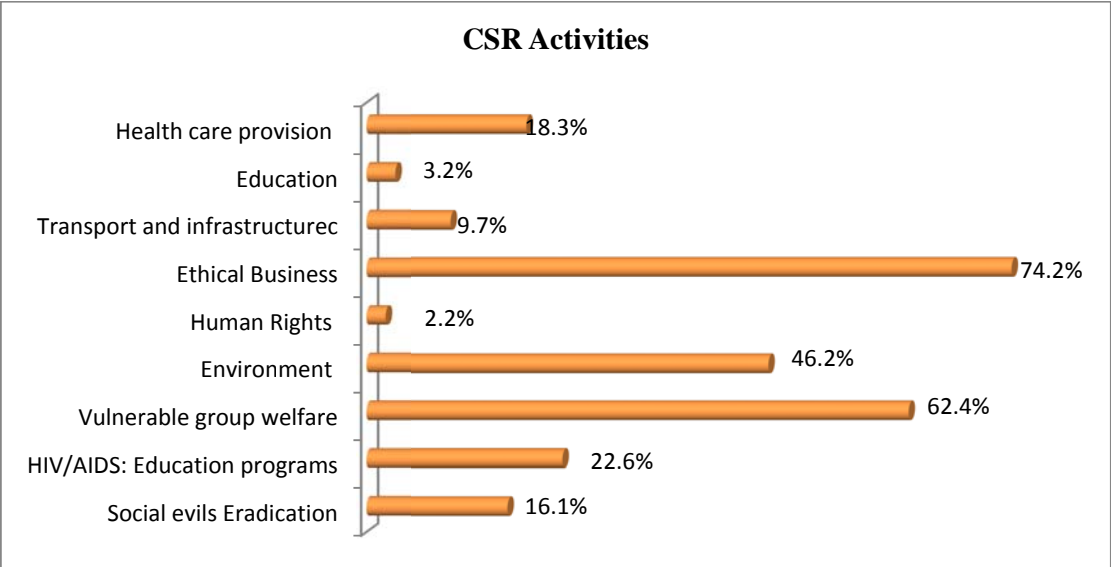
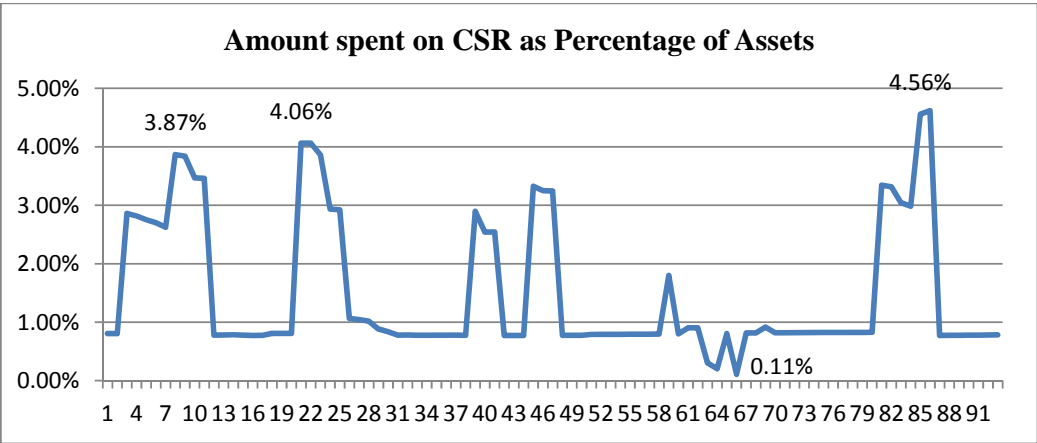


Figure 4.3: CSR Activities

Source: Study Data

4.2.5 Amount Spent on CSR

The amount spent on CSR by the SMEs was measured as a percentage of total assets. As shown in figure 4.4 below, the amount spent on CSR by the SMEs ranged between 4.56% and 0.11%.



Figure

4.4: Amount spent on CSR

Source: Study Data

4.2.6 SMEs Industry and CSR activities

As shown in figure 4.5 and table 4.1 below, manufacturing industry have the highest amount spent on CSR as a percentage of assets of 1.65%, services 1.57% while trading 1.4%.

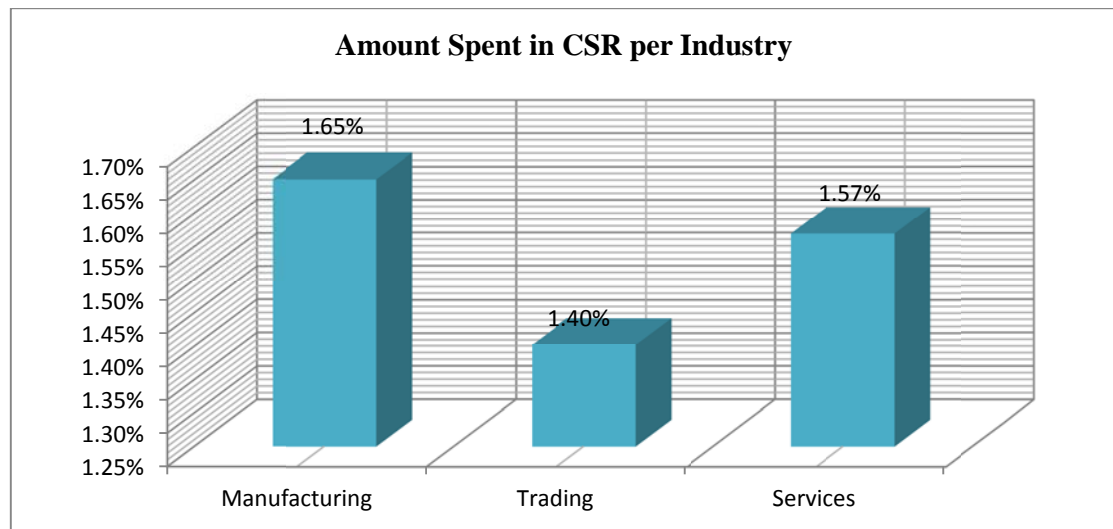


Figure 4.5: Average amount spent on CSR per industry

Source: Study Data

The high average amount spent on CSR by manufacturing firms could be attributed to the need by the manufacturing firms to create brand visibility for their products. Service firms also require more customer confidence since they sell services leading to more amounts spent on CSR.

Table 4.1: CSR and SMEs Industry

Industry	Amount spent on CSR as Percentage of Assets	Standard Deviation
Manufacturing	1.65%	0.0117
Trading	1.40%	0.0110
Services	1.57%	0.0133

Source: Study Data

4.2.7 SMEs Profitability

As shown in figure 4.6 below, top 100 SMEs average return on assets of 3% and 34%.

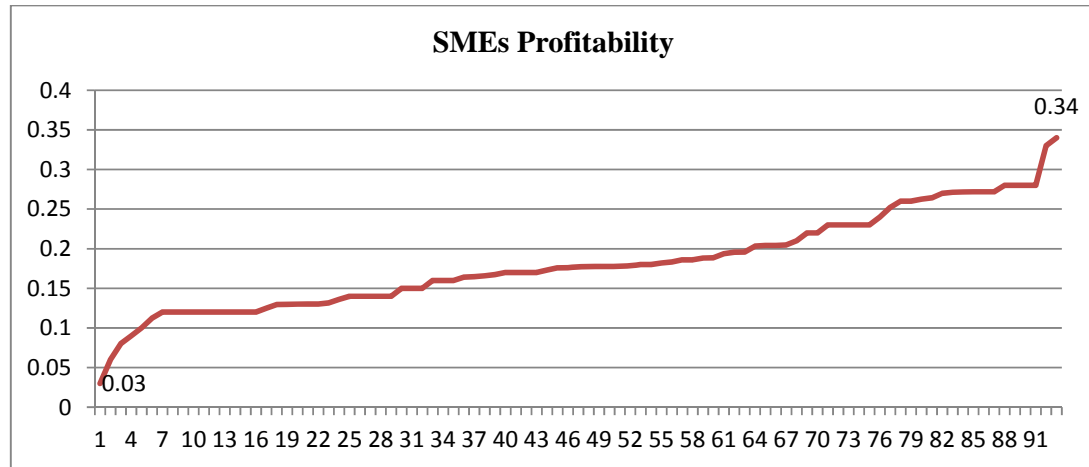


Figure 4.6: Top 100 SMEs profitability

Source: Study Data

As shown in figure 4.7 below, profitability of SMEs was observed to be high with 5% of SMEs having ROA of less than 10%, 67% with ROA between 10-20% while 28% with ROA of above 20%.

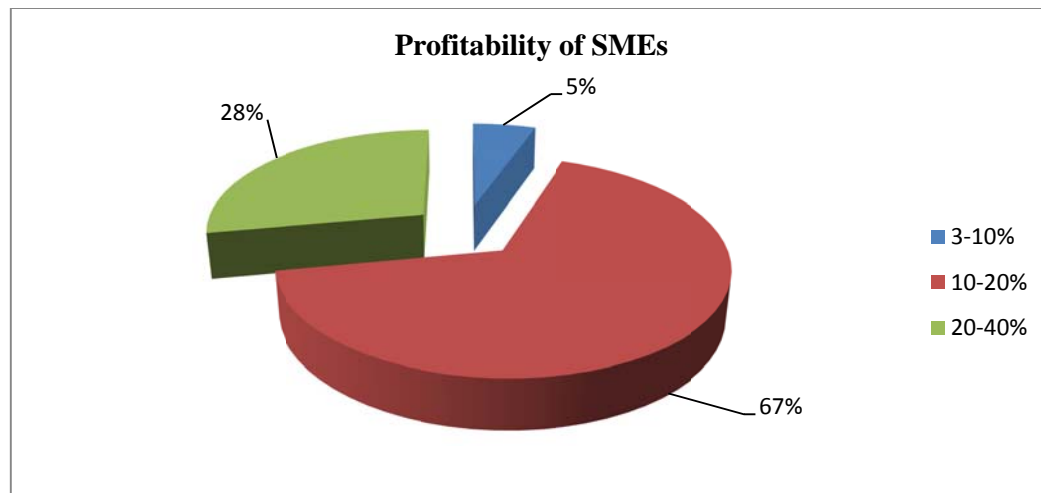


Figure 4.7: SMEs profitability

Source: Study Data

4.3 Correlation Analysis

Correlation analysis was conducted to empirically determine whether there existed a relationship between CSR, size of SMEs, industry and profitability. CSR has positive effect on profitability of top 100 SMEs in Kenya. This is shown by coefficient of correlation of 0.7407 and coefficient of determination of 0.5486. The relationship between CSR and profitability was found to be significant where the p value of 0.002 is less than 5% significant level.

Also, size of SME has positive effect on profitability as shown by coefficient of correlation of 0.4947 and coefficient of determination of 0.2447. The relationship between firm size and profitability was found to be significant as shown by p value of 0.0064 which is less than 0.05. As shown in table 4.2 below, there is positive relationship between industry and profitability as indicated by Pearson coefficient of correlation of 0.0621. The relationship between industry and profitability is significant as shown by p value of 0.005 which is less than 5%.

Table 4.2: Correlation Analysis on Independent Variables and Profitability

	Pearson Correlation	R Square	Sig. (2-tailed)	N
CSR and ROA	0.7407	0.5486	0.0020	500
Size of SME and ROA	0.49465	0.24467	0.0064	500
Industry and ROA	0.0621	0.0039	0.005	500

Source: Study Data

4.4 Regression Analysis

4.4.1 Model Summary

The relationship between CSR, SME size, industry and profitability was found to be positive as shown by coefficient of correlation of 0.86. The coefficient of determination was found to be 0.73. This implies that the model could account for 73% of the changes in profitability. The findings are detailed in table 4.3 below.

Table 4.3: Overall Model Summary

R	R Square	Adjusted R Square	Std. Error of the Estimate
0.8564	0.7335	0.7343	0.0006

Source: Study Data

4.4.2 Model Analysis of Variance

The relationship identified was found to be significant with a p value of 0.0174 which is less than 0.05 as shown in table 4.4 below. This implies that the model developed was significant and could be relied upon in making prediction.

Table 4.4: Overall Model ANOVA

	Sum of Squares	df	Mean Square	F	Sig.
Regression	0.0216	3	0.0072	1.0882	0.0174
Residual	0.3068	496	0.0034		
Total	0.3284	499			

Source: Study Data

4.4.3 Model Analysis of Variance

The coefficients of model developed are shown in table 4.5 below. All the obtained coefficients are significant for prediction at 95% confidence level as their respective p values are less than 0.05. The model developed is $Y=1.2661X_1 + 0.0918X_2 + 0.0066X_3$ where Y is financial performance as measured by return on assets, X1 is CSR, X2 is the size as measured as a percentage of sales and total assets and X3 the SMEs industry.

Table 4.5: Overall Model Coefficients

	Unstandardized Coefficients	Std. Error	Beta	t	Sig.
Constant	0.1842	0.0214		8.6012	0.0000
Industry	0.0066	0.0081	0.0850	0.8196	0.0041
CSR	1.2661	0.5293	0.2476	2.3919	0.0189
Size	0.0918	0.5298	0.0180	0.1733	0.0086

Source: Study Data

4.5 Discussion and Interpretation of the findings

The study sought to determine the effect of corporate social responsibility on financial performance of small and medium sized enterprises using top 100 SMEs. Data was collected, analyzed and interpretation based on this objective. The study found that CSR has positive and significant effect on profitability of top 100 SMEs in Kenya. This is shown by coefficient of correlation of 0.7407 and coefficient of determination of 0.5486. The findings are similar to those of Brammer *et al.*, (2006) who found CSR

has significant impact on firm's value. The findings are also similar to those of Mwangi (2011) and Mwangi & Jerotich (2013) who found that there was a strong relationship between the independent variables (CSR practice, efficiency and capital intensity) used in the model and the dependent variable (ROA). The results contradict those of Vance (1975) who found a negative correlation between rankings of social responsibility and stock market performance.

The study also found that SME size has positive effect on profitability as shown by coefficient of correlation of 0.4947. The findings are in line with those of Waddock & Graves (1997) who found that firm size (total sales, total assets and number of employees), risk (long-term debt to total assets ratio) affects the relationship between firm performance and CSR.

Further SMEs industry was found to have positive relationship between industry and profitability as indicated by Spearman coefficient of correlation of 0.0621. The results agree with those of Ghelli (2013) who found that depending on the sector in which the analysis is conducted, results on CSR and profitability will be different. Further, the study indicated that manufacturing and retail trade industries are two different sectors: the way in which the businesses are run, the differences in the environment and context in which they operate, and the different needs that the stakeholders have, could explain the difference in the results.

From regression analysis on the overall model, the coefficient of determination of 0.73 shows that the CSR, size and industry account for 73% of financial performance as measured by return on assets. The model developed was $Y=1.2661X_1 + 0.0918X_2 + 0.0066X_3$ where, Y is financial performance as measured by return on assets, X1 is CSR, X2 is the size as measured as a percentage of sales and total assets and X3 the

SMEs industry. The coefficients in the overall model on industry of 0.0066, CSR 1.2661 and size 0.0918 implies that CSR is the most important factor since every shilling investment in CSR will lead to 1.27% increase on return on assets. The industry coefficient of 0.0066 shows that an increase in code of industry; that is, move from manufacturing coded 1 to trading, coded 2 to services, coded 3 will lead to increase in financial performance of SMEs. Hence, service industry SMEs have higher financial performance as measured by ROA than trading and manufacturing. A coefficient of 0.0918 on size implies that a unit increase in turnover as a percentage of sales leads to 9% increase in financial performance.

CHAPTER FIVE

SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

5.1 Introduction

This chapter covers summary of the study, conclusion and recommendations. The summary of the study entails and outline of how the study was conducted and findings. The conclusion and recommendations of the study are based on the study findings.

5.2 Summary

The study sought to determine the effect of corporate social responsibility on financial performance of top one hundred small and medium sized enterprises in Kenya. Data was collected from secondary sources and analyzed in line with this objective. The study found that CSR has significant positive effect on profitability of top 100 SMEs in Kenya as shown by coefficient of correlation of 0.7407 and coefficient of determination of 0.5476. Size was also found to have significant positive effect on profitability as shown by coefficient of correlation of 0.4947.

The SME industry was also found to have significant effect on financial performance of SMEs as shown by positive relationship between industry and profitability as indicated by Spearman coefficient of correlation of 0.0621. Service industry firms were found to have highest financial performance followed by trading and manufacturing being least profitable as measured by return on assets. This implied that service SMEs in Kenya were more profitable which could be out of less investment in working capital and low overheads.

The relationship between CSR, SME size, industry and financial performance was found to be positive as shown by coefficient of correlation of 0.86. The relationship identified was found to be significant with a p value of 0.0174 which is less than 0.05. This relationship was obtained using multiple regression analysis where CSR, SME size and industry were independent variables while financial performance was dependent variable. Size of SMEs and industry were used as control variables.

From the top 100 studied firms, 47% were in service industry, 33% in trading and 20% in manufacturing with at least 93% of the SMEs at least were involved in CSR for the five period with 7% of the SMEs not found to be involved in CSR at all for the period or the same was never disclosed. However, the chances of engaging in CSR and not disclosing the same were less unless no resources were engaged.

Ethical business was ranked to be the highest CSR activity whereby 74.2% of the SMEs disclosed carrying ethical business as the main CSR activity. Vulnerable group welfare that includes children home support was ranked second with 62.4% of the SMEs engaging in it. 46.2% of the SMEs were engaging in environmental activities including cleaning, planting trees and drainage construction and unblocking. Other CSR activities were eradication of social evils (16.1%), HIV education (22.6%), Human rights (2.2%), transport and infrastructure (9.7%) and health care provision (18.3%).

The amount spent on CSR by the SMEs was measured as a percentage of total assets. The amount spent on CSR by the SMEs ranged between 4.56% and 0.11%. Manufacturing industry had the highest amount spent on CSR as a percentage of assets of 1.65%, services 1.57% while trading 1.4%. The high average amount spent on CSR by manufacturing firms could be attributed to the need by the manufacturing firms to

boost their profitability by creating brand visibility for their products. Top 100 SMEs average return on assets of 3% and 34%. Profitability of top 100 SMEs was observed to be high with 5% of SMEs having ROA of less than 10%, 67% with ROA between 10-20% while 28% with ROA of above 20%.

5.3 Conclusions

From the study findings, the study concludes that corporate social responsibility has significant and positive effect on financial performance of small and medium sized enterprises in Kenya. The effect is due to competitive advantage achieved by CSR activities which lead to customer goodwill and loyalty resulting to increased turnover. In addition, CSR is a marketing strategy and leads to implementation of marketing activities that are characterized by an offer from the firm to contribute a specified amount to a designated cause when customers engage in a revenue-providing exchanges that satisfy organizational and individual objectives.

The study also concludes that size of SME has significant effect on profitability where bigger SMEs have better financial performance than small ones. This is due to the fact that big companies have wider visibility and also enjoys economies of scale. In addition, smaller firms tend to invest less in CSR than bigger companies since large companies have the resources to engage in more and better social initiatives than smaller firms.

The study also concludes that SME industry has significant effect on financial performance with SMEs in service industry firms having highest financial performance followed by trading and manufacturing being least profitable as measured by return on assets. The effect is out of industry factors like competition, regulation and nature of

the industry customers highly influences firms' financial performance. In addition firms that come from different industries have to deal with different external context, with distinct environmental, social and financial concerns, as well as different stakeholders' needs.

Finally, the study concludes that CSR, size and industry of an SME account for significantly high proportion of financial performance as measured by return on assets. Therefore, the effect of CSR on financial performance also depends on the industry and the size of the firm being studied.

5.4 Policy Recommendations

Investment in corporate social responsibility has positive effect on financial performance among SMEs. The study therefore recommends that SMEs to be socially responsible so as to increase their financial performance. Sustainable performance of businesses cannot be achieved in unfavourable environment or a society full of unemployment, insecurity and other social challenges. An organization viewed not to be socially responsible will have negative perception in the market and hence reduced turnover.

The study also recommends that CSR not be viewed as a voluntary undertaking but a compulsory practice for the firms. Policies among SMEs to ensure that the firm acts in ethical and socially responsible manner to all stakeholders should be formulated and implemented. For example, to ensure that listed companies in Kenya are socially responsible, Capital Markets Authority has put guidelines and requirements for the same. Such guidelines should be implemented for SMEs.

From the study findings, size of SME has effect on profitability with bigger SMEs having higher financial performance. As a result, establishment and continued growth of small SMEs to medium and big SMEs should be encouraged. Small firms should also consider merging with big firms to increase their size and benefit from economies of scale.

To ensure this, the study recommends formulation of policies and institutions to support growth of small SMEs to large owns. Policy makers should also undertake to understand why CSR activities among SMEs is not as robust in Kenya as compared to other developed countries or other sectors and what should be done to improve CSR activities in the SME sector to maximize financial returns for economic growth.

5.5 Limitations of the study

The study only studied the top 100 SMEs in Kenya as representative of all SMEs. However, top 100 SMEs represent the cream of SMEs and may not be representative of all SMEs in Kenya and hence constituting to one of the limitations of this study. Further relying on the top end SMEs locks out the factors associated with middle and small firms hence providing results that cannot be generalized.

Secondly, in this study, CSR was measure by amount spent on CSR which may not accurately measure the level of SMEs CSR involvement. CSR does not only involve use of money and non cash CSR items may have higher impact on performance. For example, a company that presents its products in a way that seem to care about the consumers can have a higher market even though the design is just a marketing tool and not a CSR item.

Thirdly, CSR information for this study was purely obtained from secondary data with no use of primary data which may also be significant in measuring the firm's CSR level. So there could be a lot of information about SMEs CSR that was not captured in the study that needs to be incorporated in further studies.

Finally, the study used information as provided by the SMEs to the top one hundred team. This means that the data could have been distorted by the SMEs management so that the firms could be ranked highly and hence not representative of the actual performance. The reason why information is provided significantly affects the information contained in it.

5.6 Suggestions for further study

This study used the top 100 SMEs in Kenya which constitutes to the cream of SME industry but may not be representative of all SMEs in Kenya. The study suggests that another research be done on all other SMEs in Kenya in attempt to obtain a more robust relationship between CSR and financial performance of SMEs. A further study can be done to analyze all the aspects of CSR activities in the SME not only the amount spent on CSR activities.

The study also suggests similar study that takes into consideration the qualitative aspects of CSR. In fact, qualitative measures have been found to be better measures of CSR level even though hard to measure. Content analysis should be used in addition to the actual practice by the company on CSR that cannot be quantified.

The study also recommends a similar study making use of primary data to better quantify the level of SMEs CSR adoption. The SMEs to be studied should be identified at a certain point in time and data collected monthly like for five years. CSR should be

measured on monthly basis based on both qualitative and quantitative methods. The coding of the qualitative data should be coded monthly and interviews to be regularly administered to assess SMEs level of CSR. Further research is recommended on the effect of CSR top 100 SMEs but using data as obtained from the management accounts or the accounting system. The information provided should also be compared on with other sources to determine the accuracy and consistency of the same. This will lead to more accurate and reliable results.

REFERENCES

- Battaglia, M., Bianchi, L., Frey, M., & Iraldo, F., (2010). An innovative model to promote CSR among SMEs operating in industrial clusters: Evidence from an EU project. *Corporate Social Responsibility and Environmental Management Journal*, 123-175.
- Bird, R., Hall, D., Momente, F., & Reggiani, F., (2007). What Corporate Social Responsibility Activities are Valued by the Market? *Journal of Business Ethics*, 76(2), 189-206.
- Brammer, S., Brooks, C., & Pavelin, S., (2006). Corporate Social Performance and Stock Returns: UK Evidence from Disaggregate Measures. *Financial Management*, 35(3), 97-116.
- Business Daily (2014). Top 100 SMEs 2014. <http://eastafriktop100.com/top-100-companies/>. Accessed on August 8, 2014.
- Cooper R., & Schindler, P., (2003). Business Research Methods, Eighth Edition, Tata McGraw-Hill Publishing Company Limited.
- Davis, K., (1973). The Case for and against Business Assumption of Social Responsibilities. *The Academy of Management Journal*, 16(2), 312-322.
- Feldman, J., Soyka, A., & Ameer, P., (1997). Does improving a firm's environmental management system and environmental performance result in a higher stock price? *Journal of Investing*, 6(4), 87-97.
- Fiori, G., Donato, F., & Izzo, F., (2009). Corporate social responsibility and firm's performance. An analysis on Italian listed companies. Presented at the Performance Measurement Association Conference
- Friedman, M., (1970). The social responsibility of business is to increase its profits. *New York Times Magazine*
- Ghelli, C., (2013). Corporate Social Responsibility and Financial Performance: Empirical Evidence. MSc Finance & Strategic Management
- Goukasian, L., & Whitney, L., (2008). Corporate Socially Responsible Firms Perform Well! Evidence from Financial and Operating Performances. Working Paper Series
- Government of Kenya (2013). Economic Survey 2013 highlights. Ministry of devolution and planning
- Government of Kenya, (2012). Economic Survey. Nairobi Kenya: Government Printers
- Government of Kenya. (2005). Nairobi Kenya: Government Printers

- Griffin, J., & Mahon F., (1997). The Corporate Social Performance and Corporate Financial Performance Debate: Twenty-Five Years of Incomparable Research. *Business Society*, 36(1), 5-31.
- Hill, C., & Jones, T., (1992). Stakeholder-agency theory. *Journal of Management Studies*, 29: 131–154
- Hull, E., & Rothenberg, S., (2008). Firm performance, the interactions of corporate social performance with innovation and industry differentiation. *Strategic Management Journal*, , 29(7), 781-789.
- Isaksson, R., & Steimle, U., (2009). What does GRI-reporting tell us about corporate sustainability? *The TQM Journal*, 21(2), 168-181.
- Jamali, D., and Mirshak, R., (2007). Corporate Social Responsibility (CSR): Theory and Practice in a Developing Country Context. *Journal of Business Ethics*. , 72(3): 243–262.
- Jensen, C., Meckling, H., (1976). Theory of the firm: managerial behavior, agency costs and ownership structure. *Journal of Financial Economics*, 3(4): 305-360.
- Jones, M., (1995). Instrumental stakeholder theory: A synthesis of ethics and economics, *Academy of Management Review*, 20: 404–437.
- Leonardo, B., Stefania, G., Damiano, P., (2007). Corporate Social Responsibility and corporate performance: evidence from a panel of US listed companies. Paper presented at the XIII Tor Vergata Financial Conference.
- Mahoney, L., & Roberts W., (2007). Corporate social performance, financial performance and institutional ownership in Canadian firms. *Accounting Forum* 31(3), 233-253.
- Marc, O., Frank, L., Schmidt, S., & Rynes, L., (2003). Corporate Social and Financial Performance: A Meta-analysis. Sage Pastel Publications. London, Thousand Oaks, CA & New Delhi
- McGuire, B., Sundgren, A., & Schneeweis, T., (1988). Corporate Social Responsibility and Firm Financial Performance. *The Academy of Management Journal*. 31 (4), 854-872
- Morsing M, Schultz, M., (2006). Corporate Social Responsibility Communication: Stakeholder Information, Response and Involvement Strategies. *Business Ethics: Eur.* 15(4): 323–338
- Moskowitz, M., (1972). Choosing socially responsible stocks. *Business and Society Journal*. 1, 71-75.
- Mugenda, M., & Mugenda, G., (2003). Research methods: Quantitative and qualitative approaches. Nairobi: Acts Press.

- Mwangi, A. (2011). The relationship between corporate social responsibility and financial Performance of publicly quoted companies in Kenya. Unpublished MBA Project, University of Nairobi
- Mwangi, C., & Jerotich, J., (2013). The Relationship between Corporate Social Responsibility Practices and Financial Performance of Firms in the Manufacturing, Construction and Allied Sector of the Nairobi Securities Exchange. *International Journal of Business, Humanities and Technology*. 3, 2
- Nelling, E., & Webb, E., (2009). Corporate social responsibility and financial performance: the virtuous circle revisited. *Review of Quantitative Finance and Accounting*. 32(2), 197-209.
- Ochanda, M., (2014). Effect of financial deepening on growth of small and medium-sized enterprises in Kenya: A case of Kenya. *International Journal of Social Sciences and Entrepreneurship*, 1 (11), 191-208.
- Okwoma, D., (2012). The effect of corporate social responsibility on the financial performance of commercial banks in Kenya. MBA project, University of Nairobi
- Olusanya, S., Suleiman, A., & Oyebo, A., (2012). Corporate Social Responsibility and Effectiveness of Small and Medium Enterprises (Smes) In Nigeria. *Journal of Business and Management (IOSR-JBM)*, PP 40-47.
- Reich, R., (2007). Super capitalism: The Transformation of Business, Democracy, and Everyday Life in Pava ML (2008). Why Corporations Should Not Abandon Social Responsibility. *Journal of Business Ethics*, 83(4): 805-812.
- Sachs, S., Maurer M., Ruhli, E., & Hoffmann, R., (2006). Corporate social responsibility from a “stakeholder view” perspective: CSR implementation by a Swiss mobile telecommunication provider. *Corporate Governance Journal*, 6(4): 506-515.
- Soana, G., (2009). The relationship between corporate social performance and corporate financial performance in the banking sector”, Working Paper Series
- Stainer, L., (2006). Performance management and corporate social responsibility: the strategic connection, *Strategic Change*, 15(5), 253-264
- Sunder, S., (1997). Accounting and the Firm: A Contract Theory. *Indian Account. Rev.* 1(1): 1-19.
- Tantalo, C., Caroli, G., & Vanevenhoven, J., (2012). Corporate social responsibility and SMEs competitiveness. *International Journal of Technology and Management*. (3), 34-92
- Theofanis, K., (2010). Corporate Social Responsibility and Financial Performance: An Empirical Analysis on Greek Companies. *European Research Studies*, XIII

- Vance, C., (1975). Are socially responsible corporations good investment risks? *Management Review* 64 (8), 18-24.
- Waddock, A., & Graves, B., (1997). The corporate social performance financial performance link. *Strategic Management Journal.* , 18(4), 303-319.
- Wafula, J., (2012). *Corporate social responsibility: a perspective of Kenyan firms.* Kenyatta University, Kenya, 2,10.
- Wan-Jan, S., (2006). Defining corporate social responsibility. *Journal of Public Affairs*, 6(3-4), 176-184.
- Wood, J., & Jones, E., (2005). Stakeholder mismatching: a theoretical problem in empirical research on corporate social performance. *The International Journal of Organizational Analysis*, 3(3), 229-267.
- Wood, J., (2010). Measuring Corporate Social Performance: A Review. *International Journal of Management Reviews*, 12(1), 50-84.
- World Business Council for Sustainable Development, (1999). *Corporate Social Responsibility: Meeting Changing Expectations*” (World Business Council for Sustainable Development, Geneva).
- Zengin, Y., (2010). Corporate social responsibility in times of financial crisis. *African Journal of business Management*, pp. 382-389

APPENDICES

APPENDIX I: 2013 TOP 100 SMES

1. Lean Energy Solutions Ltd.
2. East African Canvas Co. Ltd
3. Digital City Ltd
4. Plenser Ltd
5. Allwin Agencies (K) Ltd
6. Propack Kenya Ltd
7. Vivek Investments Ltd
8. Powerpoint Systems (Ea) Ltd
9. Coninx Industries Ltd.
10. SynermedicaPharmaceuticals (Kenya) Ltd
11. Coast Industrials & Safety Supplies Ltd
12. Isolutions Associates
13. Wotech Kenya Limited
14. Avtech Systems Limited
15. Kenya Bus Service
16. Muranga Forwarders
17. Synermed Pharmaceuticals (K) Ltd
18. Tissue Kenya Ltd
19. Kenya Highland Seed Co Ltd
20. Famiar Generating Sys Ltd
21. Alexander Forbes
22. Chemicals & School Supplies Ltd.
23. Charlstone Travel Limited
24. Onfon Media Ltd
25. Elite Tools Ltd
26. Eurocon Tiles Products Ltd
27. Endeavour Africa Limited
28. Rongai Workshop & Transport Ltd
29. R & R Plastics Ltd
30. Chigwell Holdings Ltd
31. Classic Mouldings Limited
32. Pewin Cabs Limited
33. Novel Technologies Ea Ltd
34. Xtreme Adventures Ltd
35. Vintage Africa Limited
36. Punjani Electrical And Industrial Hardware Limited
37. Spry Engineering Co. Ltd
38. General Cargo Services Ltd
39. Pinnacle (K) Travel & Safaris
40. Panesars Kenya Limited
41. Specialized Aluminium Renovators Ltd.
42. Cube Movers Limited
43. Brogiibro Company Ltd

44. Total Solutions Ltd
45. Tyremasters Ltd
46. Xrx Technologies Limited
47. Sensation Ltd
48. Eureka Technical Services Ltd
49. Palbina Travel Limited
50. Waumini Insurance Brokers Ltd
51. Asl Credit Limited
52. Zaverchand Punja Limited
53. Canon Chemicals Ltd
54. Packaging Manufacturers(1976) Ltd
55. Trident Plumbers Ltd
56. Typotech
57. Kinpash Enterprises Ltd
58. Vehicle & Equipment Leasing Ltd
59. Sheffield Steel Systems
60. Complast Industries Ltd
61. Dune Packaging Limited
62. Hebatullah Brothers Limited
63. Spice World Limited
64. Museum Hill Wines Ltd
65. Yogi Plumbers Ltd
66. Vajra Drill Ltd
67. Melvn Marsh International Ltd
68. Kandiafresh Produce Suppliers Ltd
69. Fayaz Bakers Limited
70. Specicom Technologies Limited
71. Mombasa Canvas Ltd
72. Silverbirdtravel Plus Ltd
73. Iron Art
74. Radar Limited
75. Master Power Systems
76. Hardware & Welding Supplies
77. Masters Fabricators Ltd
78. Software Technologies Ltd
79. Heritage Foods Kenya Ltd
80. Africa Tea Brokers Ltd
81. Raerex (Ea) Limited
82. Travelshoppe Company Ltd
83. Oriental General Stores Ltd
84. Chuma Fabricators Ltd
85. Statprint Ltd
86. Sollatek Electronics Ltd
87. Smartbrands Ltd
88. De Ruiters East Africa Ltd
89. Kisima Drilling (Ea) Ltd
90. Care Chemists
91. Brollo Kenya Ltd
92. Canon Aluminium Fabricators Ltd
93. Satguru Travel & Tours Ltd

94. Kunal Hardware And Steel

95. Deepa Industries Limited

96. Skylark Creative Products Ltd.

97. Uneek Freight Services Ltd

98. Bbc Auto Spares Ltd

99. Lantech (Africa) Limited.

100. Polytanks Limited