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Linking social and economic responsibilities with financial performance: The role of innovation

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ABSTRACT

The research conducted in this study focuses on the role of a company's innovation culture in linking economic and social responsibilities with financial performance. Specifically, our study addresses the following two questions: Does innovation trigger the simultaneous development of both economic and social dimensions of corporate social responsibility? Does the simultaneous pursuit of economic and social responsibilities result in a higher financial performance? These questions are examined through an empirical investigation of 133 companies, belonging to the Spanish Social Environmental Agreement, using structural equation modelling validated by factor analysis. The results indicate that, although companies are using innovation outcomes to support both economic and social achievements, they are only taking advantage effectively of economic achievements to obtain a higher financial performance.

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1. Introduction

Innovation is increasingly considered to be one of the key drivers of the long-term success of a company in today's competitive environment (Bruni & Verona, 2009; García-Morales, Lloréns-Montes, & Verdú-Jover, 2008). Companies with the capacity to innovate are able to respond to environmental challenges faster and better than companies that are not able to innovate (Brown & Eisenhard, 1995). This paper points out that innovation is one way to transfer learned knowledge to offer better solutions that meet new requirements, unarticulated needs (Maranville, 1992; Powell, 1998), or existing social needs, and implementing innovative ideas and decisions.

Organizations and management researchers have also increasingly focused on the importance of corporate social responsibility (CSR) both in terms of the concept itself and the outcomes that flow from an adoption of CSR. In this context, CSR refers to situations where companies integrate social, economic and environmental concerns in their business operations and in their interaction with their stakeholders on a voluntary basis (European Commission, 2001; Perrini, 2005). Thus, embracing CSR requires that companies engage in voluntary activities that "need to be undertaken to operate in an economic, social and environmentally sustainable manner" (Foreign Affairs, Trade and Development Canada, 2015). We would also note that improvements in the processes involved in implementing CSR may also involve what has been referred to as 'social innovation' (Rexhepi, Kurtishi, & Bexheti, 2013).

Companies are engaged in a wide variety of different types of social activities, such as actions taken to address the concerns of environmental interest groups and the communities within which they operate (Perrini, 2005), actions ensuring that employees are treated fairly (Weber, 2008), or providing support for arts and cultural programs (Blakely & Aparicio, 1990). This paper analyzes two important aspects of CSR; one concerning what may be considered to relate to achieving economic objectives and the other relating to achieving social objectives. Although it seems intuitively clear that a firm pursues both economic and social objectives (Elkington, 2004) it is also clear that these are fundamentally different types of objectives that potentially require the design and implementation of very different structures for their achievement (Cegarra & Martinez, 2009). For example, while the social dimension of sustainable development deals with the impact that the organization may have on social systems in which it operates, the

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economic dimension of sustainable development refers to impacts that the organization may have on the economic conditions of its stakeholders and on economic systems at local, national, and global level (GRI, 2011).

The differences between economic and social objectives are especially important in small and medium sized enterprises (SMEs) which often have to face resource constraints in funding, technology and materials (Lewis, Massey, Ashby, Coetzer, & Harris, 2007). In this context, it may be argued that SMEs are more likely to initially address concerns that are obviously related to economic objectives and hence the adoption of social and environmental initiatives is slower (Walker & Preuss, 2008), which in turn is likely to result in tensions between them that are difficult to reconcile (Carroll & Shabana, 2010). For example, while achieving economic objectives and taking responsibility for them involves ensuring the company's own profitability, achieving social objectives may well involve donating services to community organizations, engaging in projects to aid the environment or donating money to charitable causes, namely actions that may compromise the achievement of economic objectives.

The research conducted in this study focuses on a company's capacity to innovate and examines how that capacity can result in the maintenance of an appropriate balance between economic and social objectives which we propose results in the improvement of organizational performance. In conducting this research we have addressed the following questions: Does innovation trigger the development of objectives related to both economic and social dimensions of corporate social responsibility at the same time? Does the simultaneous pursuit of economic and social objectives and recognizing the associated responsibilities result in improved financial performance?

By addressing the above questions this study seeks to clarify the difference between a company's innovation outcomes in general and its social innovations in particular. In spite of the fact that innovation has been viewed as a means of understanding the impact of CSR on organizational outcomes (Lockett, Moon, & Wayne, 2006), the existing research literature does not provide any empirical evidence, particularly in relation to SMEs, investigating the balance between economic and social objectives or how they relate to financial performance. The rest of the paper is organized as follows. First, the conceptual framework is discussed and presented in Section 2, while the methodology of the study is presented in Section 3. The results of data analysis are then presented in Section 4 with the discussion in Section 5 concluding the paper.

2. Conceptual framework

2.1. CSR and innovation relationship

The concept of innovation has been invoked to characterize the way in which organisations are potentially able to create a path for the creation and implementation of positive changes that fuel organisational growth (Gaynor, 2002). In this context, once an innovation is implemented, it provides an organisation with benefits that have the potential of sustaining its viability in a global economy. Gaynor (2002) refers to innovation as a cultural element of an organisation that should be adopted and embraced by managers in order to communicate to employees a critical feature of the organisation's strategic direction and hence encourage employees to search for better solutions through the development and implementation of information and communication technology systems, marketing methods or processes. These ‘better solutions’ to change can be related to an innovative environment which includes employees as key actors in the identification and implementation of new opportunities that result in the more efficient utilization of resources (Gaynor, 2002).

In this paper, the authors adopt the approach proposed by Gaynor (2002) and hence adopt an approach that views innovation as the capacity to prepare the ground for promoting and pursuing better solutions (Martins & Terblanche, 2003). As Abraham and Knight (2001) noted, innovation involves making knowledge creation and innovative action a way of life evidenced by, for example, seeking to create and expand markets rather than just reacting to customer demand. Thus, at its heart, a successful innovation process can be viewed as the application of better solutions that meet new requirements, unarticulated needs, or existing market needs (Maranville, 1992; Martins & Terblanche, 2003).

It should be noted, however, that developing measures for innovation can be a tricky business. Prior research has developed measures of innovation related to its outputs and the mechanisms that cause it to occur (Leenders & Wierema, 2002). For example, some previous studies have developed measures relating to the extent to which an organization possesses an innovative culture by utilizing measures that explicitly relate to the existence of certain behaviours (e.g. Brettel & Cleven, 2011; Martín de Castro, Delgado-Verde, Navas-López, & Cruz-González, 2013), while others have suggested that measuring the outputs of innovation helps organizational employees focus in actual innovation rather than simply pay lip service to potentially innovative behaviours (e.g. Baruk, 1997; Michalisin, 2001). The present study focuses on outcome indicators which represent the realized, long-term outputs of an innovative culture, e.g. improved products and services, improvements in processes or marketing methods shaped by an innovative culture (OECD, 2005).

From the point of view of a company, social innovations are innovations that are both good for society and enhance the company's capacity to act in achieving its goals for economic development (Rexhepi et al., 2013). In this regard, Doane (2005) defines CSR as the efforts corporations make above and beyond those that arise as a result of regulations to balance the needs of stakeholders with the need to make a profit. Hopkins (1998) asserts that CSR involves interacting with the external and internal stakeholders of the firm in an ethical or in a socially responsible way. This insight corroborates the notions of Du, Bhattacharya, and Sen (2011) that, by engaging in CSR activities, companies can not only generate favourable stakeholder attitudes and better support behaviours (e.g. purchase, seeking employment, or investing in the company), but also, over the long run, build corporate image, strengthen stakeholder–company relationships, and enhance stakeholders' advocacy behaviours. Furthermore, Rasoulzadeh, Hosseinipour, Yusof, Ashikin, and Soltani (2013) think of CSR as a means of increasing operational efficiency and reducing costs, and Dahlsrud (2006) suggests that, from an economic point of view, CSR may be considered to relate to how resources for the production of goods and services are distributed within the social system.

Although some see CSR as a source of competitive advantage by enhancing corporate image and reputation (Knox & Maklan, 2004), it also can be a source of conflicts if is not properly administered (Doane, 2005). As Blakely and Aparicio (1990) point out, economic and social objectives are likely to be increasingly in conflict as organizational resources shrink and managerial support for social programs dwindles. In this regard, it is important to realize that the empirical studies of the relationship between CSR and financial performance have been inconclusive, reporting positive (e.g. Waddock & Graves, 1997; Johnson & Greening, 1999), negative (Bromiley & Markus, 1989; Davidson & Worrell, 1988), and even neutral results (McWilliams & Siegel, 2000). As McWilliams and Siegel (2000) and Surroca, Tribó, and Waddock (2010) argue, this lack of consensus might reflect model specification problems, such

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