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Does size matter? Corporate social responsibility and firm performance in the restaurant industry☆

Hyewon Youn[a,*], Nan Hua[b], Seoki Lee[c]

[a] LCB Hospitality Management, Sookmyung Women's University, Republic of Korea
[b] Rosen College of Hospitality Management, University of Central Florida, United States
[c] School of Hospitality Management, The Pennsylvania State University, United States

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ABSTRACT

Despite an increasing number of hospitality studies on the link between corporate social responsibility (CSR) and corporate financial performance (CFP), the literature has predominantly focused on the CSR–CFP relation without considering moderating factors. Consequently, the current study introduces firm size as a potential moderator on the CSR–CFP relationship. Performing a two-way fixed-effects model by firm and year with Newey-West standard errors, this study finds that firm size moderates the effect of positive CSR on CFP while it does not moderate the effect of negative CSR on CFP in the U.S. restaurant context.

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1. Introduction

In general, corporate social responsibility (CSR) can be defined as the corporate actions that go beyond the firm's legal and contractual obligations and support the societal good (McWilliams and Siegel, 2001). The topic of CSR has received increasing attention from both researchers and practitioners over past a few decades and CSR practices have become mainstream business activities (Kitzmueller and Shimshack, 2012). In 2011, nearly 60% of Fortune 500 companies published corporate accountability reports and more than one-third of large U.S. companies have voluntarily implemented external certifications for social and environmental standards (Kitzmueller and Shimshack, 2012; Lys et al., 2013).

With the increasing amount of money and attention that companies are giving to CSR initiatives (DiGuili and Kostovetsky, 2014), it has become imperative to empirically investigate the impact of CSR on firm performance. Over the years, many studies have explored the relationship between CSR and corporate financial performance (CFP) to test whether companies do well by doing good (Kitzmueller and Shimshack, 2012). Previous CSR–CFP studies have been conducted under diverse geographical contexts; however, the findings are still inconclusive (Choi et al., 2010). For example, Margolis et al. (2007) conducted a comprehensive meta-analysis of 192 relationships from 167 studies previously published and found a modest positive average correlation between CSR and CFP. Peloza (2009) also reviewed 128 studies that examined the CSR–CFP relationship and reported that 59% found a positive relationship, 27% a mixed or neutral relationship, and 14% a negative relationship. Based on a review of 21 empirical studies, Pava and Krausz (1996) concluded that socially responsible firms either outperformed or performed at least as well as other firms. This finding was also confirmed by their experiment as they found that socially responsible firms showed significant improvement over non-socially responsible firms on several performance measures.

In addition to the inconclusive results from the previous literature, it was suggested that moderating effects should be considered when studying the relationship between CSR and CFP (e.g., Aguinis and Glavas, 2012; Fombrun and Shanley, 1990) to shed light on the mixed findings on the CSR–CFP link. In particular, several studies have discussed firm size as a potential moderating factor at the organizational level (e.g., Aguinis and Glavas, 2012; Graves and Waddock, 1994; Ocasio, 2011; Van de Ven, 1986). Consequently, the current study is conducted to test the moderating effect of firm size on the relationship between CSR and CFP in the restaurant context, making unique contributions to the literature from both testing context and content perspectives.

Specifically, this study first proposes that larger restaurant firms' CSR and positive CSR initiatives would have positive impacts on CFP based on the efficiency argument of firm size stemming from the economies of scale literature (Miller, 1978) and the franchising characteristic in the restaurant industry (Brickly and Dark, 1987).

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* Corresponding author.
E-mail addresses: hyewonyoun@sookmyung.ac.kr (H. Youn), Nan.Hua@ucf.edu (N. Hua), leeseoki@psu.edu (S. Lee).

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Second, this study hypothesizes an insignificant moderation effect of firm size on the relationship between negative CSR initiatives and CFP that may support weak form market efficiency. Findings of this study generally support the proposed hypotheses.

Since no study has investigated whether the impact of CSR on restaurants' CFP depends on restaurant size, findings of this study will assist restaurant companies in incorporating CSR strategies into their operations more efficiently and utilizing CSR activities as a means of enhancing their overall business performance. Moreover, this study will add to the hospitality CSR literature on the relationship between CSR and CFP by providing the first piece of comprehensive empirical evidence for the moderating effect of firm size. And lastly, taking its cue from Kang et al. (2010) and Kim and Kim (2014), this study further categorizes overall CSR into positive CSR (PCSR) and negative CSR (NCSR) to examine the differential marginal effects of PCSR and NCSR on CFP conditional on restaurant firm size.

The rest of this paper is organized as follows. Section 2 lays out the theoretical background and develops study hypotheses regarding the moderating effect of firm size on the relationship between CSR and CFP. Section 3 presents the data and method employed in this study and Section 4 displays the results. Section 5 discusses implications for managers and further research.

2. Literature review

2.1. Corporate social responsibility and firm performance

Over the years, the concept of corporate citizen has gained much popularity, with multiple stakeholders, such as customers, employees, regulators, local communities, and shareholders, sharing intricate interdependent relationships (Donaldson and Preston, 1995; Jones, 1995). As a result, stakeholder theory was proposed by Freeman (1984), with a normative perspective suggesting that stakeholders have legitimate interests in the firm (Agle et al., 1999) and an instrumental perspective contending that the firms that engage in stakeholder management should outperform those that fail to do so (Harrison et al., 2010). This proposition thus offers a theoretical foundation to investigate CSR activities—managerial decisions drive CSR activities, which affect stakeholders and firm financial performance at the same time.

Nevertheless, managers are bounded by their professional obligations to balance the needs and desires of firm stakeholders to strive for a high level of financial performance, because different stakeholders may possess distinct views of CSR activities' effects on the financial wellbeing of the firm after all (e.g., Friedman, 1970; Poitras, 1994). For example, large charitable financial commitment may be welcomed by customers and local communities but deemed improper by shareholders as misappropriation of limited resources (Friedman, 1970). On the other hand, shareholders may tolerate socially irresponsible activities, such as environmental pollution, as the resultant downside financial cost tends to be smaller than taking the action of correction (e.g., Poitras, 1994). Among the various stakeholders, shareholders are increasingly concerned about CSR and its impact on firm performance (Porter and Kramer, 2006).

Extensive empirical studies have been conducted to investigate the link between CSR and CFP, covering diverse geographical contexts such as Spain (Garay and Font, 2012; Rodriguez and Armas-Cruz, 2007), Greece (Karagiorgos, 2010), Libya (Bayoud et al., 2012), Korea (Choi et al., 2010) and Canada (Mahoney and Roberts, 2007), to name a few. Two distinct schools of theoretical arguments have emerged as a result and offered mixed empirical evidence. On the one hand, a firm's expenditure in socially responsible activities can be seen as business investment (Gatti et al., 2012); consequently, CSR expenditures should positively influence CFP through improved firm reputation and relationship with external stakeholders (Orlitzky et al., 2003). Majority of previous studies have supported the positive CSR–CFP relationship (e.g., Gatti et al., 2012; Orlitzky et al., 2003). On the other hand, CSR expenditures can behave as pure cost burdens for firms and fail to maximize shareholder wealth (e.g., Lee et al., 2009; Makni et al., 2009); therefore, along this line of reasoning, prior literature has also reported a negative relationship between CSR and CFP (e.g., Brammer et al., 2006).

From these prior studies, though, has frequently emerged a theoretical argument—firm size moderates the relationship between CSR and CFP. For example, using publicly held Canadian firms, Makni et al. (2009) assessed the effects of a firm's aggregate CSR and individual dimensions of CSR (community and society, corporate governance, customers, employees, environment, human rights) on three measures of CFP (ROA, ROE, and market returns), respectively. They found empirical evidence in support of significantly negative relationships between the aggregate CSR and the market return measure of CFP and between the environmental dimension of CSR and all three measures of CFP. Makni et al. (2009) then argued that the impact of environmental initiatives on firm performance may depend on firm size in that smaller firms may not benefit from CSR initiatives as much as larger firms. However, they did not perform an empirical analysis on such a potential moderating effect of firm size, leaving an empirical void. It is also worth noting that, due to a large number of potentially intervening variables between social and financial performance that are difficult to control, some argue that it is impossible to determine the nature of CSR–CFP relationship (Fombrun and Shanley, 1990).

In the hospitality and tourism context, researchers have followed the same two distinct schools of theoretical arguments in the mainstream to study the CSR–CFP relationship, namely, the business investment (e.g., Orlitzky et al., 2003) and cost burden (e.g., Makni et al., 2009) arguments, yielding mixed results that support both positive and negative relationships between CSR and CFP. For example, following from the argument that CSR expenditures behave as business investment (e.g., Orlitzky et al., 2003), high CSR involvement should improve operation efficiency by increasing sales and reducing costs (e.g., Brammer and Millington, 2006). As a result, researchers found a positive relationship between CSR and CFP for hotel companies (Lee and Park, 2009), a positive impact of positive CSR on firm value for hotels and restaurant firms (Kang et al., 2010), a U-shaped relationship between CSR and ROE for restaurant firms (Park and Lee, 2009), significant positive effects of overall CSR and positive CSR on stock returns (Kim and Kim, 2014), and a positive impact of judicious investment by family firms in CSR on their future financial performance (Singal, 2014). On the other hand, cost burden (e.g., Makni et al., 2009) arguments contend a negative relationship between CSR and CFP. Following these arguments, researchers found that negative CSR hurt firm value (Kim and Kim, 2014) and CSR dimensions exert differential effects on firm performance across the four industry sectors of airline, casino, hotel, and restaurant companies (Inoue and Lee, 2011). In addition, researchers have started to notice that moderating variables could play a potential role in the relationship between CSR and CFP. For example, because consumer discretionary expenditures, which are highly sensitive to economy status, exert significant influence on service industries such as restaurants and airlines (e.g., Singal, 2014), economic conditions (Lee et al., 2013a) and oil prices (Lee et al., 2013b) could moderate the relationship between CSR and CFP.

Overall, previous CSR–CFP studies on hospitality and tourism firms have used different methodologies and measures of CSR and CFP and found a positive, negative, or no relationship between CSR and firm performance. Since a firm's financial performance is the ultimate measure for the success or failure of any CSR initiatives

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