



Understanding corporate philanthropy in the hospitality industry



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ABSTRACT

This study makes a unique contribution to the corporate social responsibility literature, both from a theoretical perspective and corporate philanthropy (CP) perspective that has been under-researched so far. Specifically, it extends the investigation of the motives of CP to the hospitality industry in the emerging country of Taiwan and is the first examination of the determinants of CP in the hospitality industry based on the value enhancement (VE) and agency cost (AC) theories. Previous studies found that either AC or VE determinants, not both, play a major role in making philanthropy decisions. This study reveals new and interesting findings using the data from 13 publicly traded hospitality companies in Taiwan collected between 1996 and 2011. Panel regression test results show that both VE determinants (labor intensity and profitability) and AC determinants (board size and the ratio of independent directors to total directors) were found to be significant factors in explaining the discretionary behavior of CP in the hospitality industry. Furthermore, the lagged philanthropy-to-sale ratio was also significantly related to CP decisions in the hospitality industry in Taiwan, suggesting that the behavior of CP in the Taiwanese hospitality industry is persistent. The possible explanation is that changing philanthropy pattern may lead to market-adverse expectations and reactions and damage the reputation of companies.

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1. Introduction

Corporate philanthropy (CP) is the discretionary act of corporations donating a portion of their profits or resources to nonprofit organizations. An interesting question is why corporations give to charity. Fry et al. (1982), Amato and Amato (2012), and Du et al. (2013) stated that empirical questions about CP were limited to surveys of corporate executives, making it difficult to distinguish what corporations actually do from what their executives claim that these corporations do. As Fry et al. (1982) noted, although the rationale for CP could be altruism, CP data offer little insight into the altruistic motive of CP if CP is motivated primarily by profit-related considerations.

Academic studies have examined the reasons for corporations' philanthropic contributions. Several studies (Brown et al., 2006; Fry et al., 1982; Navarro, 1988) have focused on the profit-maximizing or self-motivated managerial perquisite motives instead of on altruism. The profit motivation argument is examined here based

on value enhancement theory and the argument of self-motivated managerial perquisite is explained by the agency cost theory.

Value enhancement theory postulates that CP creates value for shareholders. Brown et al. (2006) argued that CP may be regarded as a form of moral capital investment, which could enhance a firm's image and reputation among its stakeholders. This positive image increases firm value by promoting customer loyalty (Lev et al., 2010), motivating employees (Greening and Turban, 2000; Navarro, 1988), inducing preferential treatment from regulators or policymakers (Brown et al., 2006), or providing insurance-like protection against risk (Godfrey, 2005). In this regard, value enhancement theory of CP could be considered a specific form of stakeholder theory, that is, a model of analysis, which addresses the relationship between both moral and value objectives of a firm and its stakeholders (Roberts, 1992).

Agency cost theory proposes that managerial insiders who participate in CP may increase their own utility through CP while shareholders incur expenses. CP may provide managerial insiders with philanthropy-related benefits and offer an opportunity to support their own pet charities to enhance their personal reputation (Brown et al., 2006). Managerial insiders thus may have the incentive to pursue their own interests through CP. As the cost of philanthropy has exceeded its financial contributions, CP represents an agency cost because it satisfies the managerial insiders'

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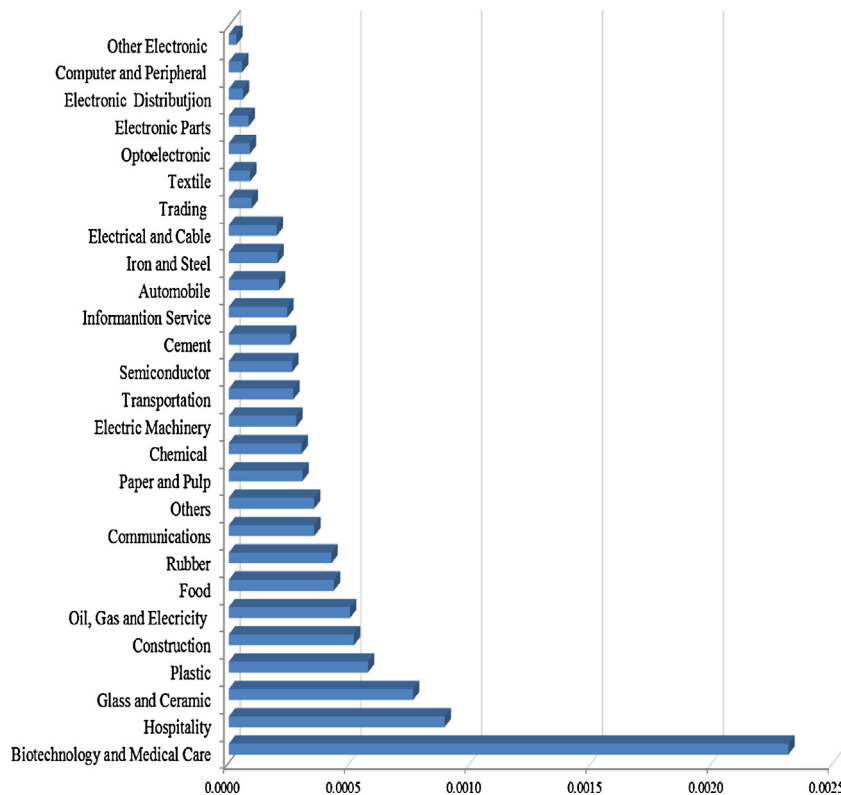


Fig. 1. The average corporate philanthropy rate.

taste for “doing good” while shareholders suffer an opportunity loss (Brown et al., 2006).

However, empirical research on whether value enhancement theory or agency cost theory better explains *CP* has been mixed and inconclusive (Brown et al., 2006; Fry et al., 1982; Navarro, 1988). As Navarro (1988) and Brammer and Millington (2004) noted, empirical studies on the motives driving *CP* have been limited by the unavailability of published information or data on *CP*. Because of limited data, most previous studies on driving motives of *CP* have been conducted in developed countries, such as the UK and USA (Zhang et al., 2010). So far, no research has examined whether agency cost, value enhancement, or other determinants can more accurately explain the *CP* decision in an emerging country. Since differences between developed and emerging countries in firm characteristics, agency conflicts, and industry environment that are due to cultural, social, economic and political factors are expected (Wright et al., 2005; Young et al., 2008), it is plausible that the determinants of *CP* in an emerging country would be different from those in developed countries.

At the same time, the determinants used to explain *CP* vary across industries (Amato and Amato, 2012; Brammer and Millington, 2008; Brown et al., 2006). Further, no hospitality research has analyzed the *CP* issue. Note that while Turner et al. (2001) presented three ways in which charities in tourism in the UK are involved and the implications this may have for the industry, they did not examine the motives of charities in tourism. This paper is the first empirical research study to test and explain the rationales for *CP* in the hospitality industry, and the availability of *CP* data in Taiwan enables us to examine the issue in the context of an emerging country.

According to the data taken from Market Observation Post System (<http://newmopsov.twse.com.tw/>), the value of *CP* made by Taiwanese publicly traded companies amounted to approximately 2.797 billion NT\$ (New Taiwan dollars) in 2011. This figure represents about .282% of total annual pre-taxable profits of all publicly

traded companies in Taiwan. The total value of *CP* from hospitality companies amounted to about NT\$ 11.619 million in 2011. Among 27 industry sectors listed on the Taiwan Stock Exchange from 1996 to 2011, the hospitality industry was ranked second in terms of the ratio of the total value of *CP* to sales revenue, following the biotechnology and medical care industry (see Fig. 1). This suggests that hospitality companies in Taiwan were eager to donate a higher percentage of their sales revenue compared to other industry sectors.

Moreover, Liu et al. (2006) stated that the power of managers in Taiwanese firms is quite high. However, with a high power in the companies, managers tend to exercise significant control over the firm, and the agency problems can become problematic for shareholders. This principal–agent relationship resulting from ownership structures may have an influence on *CP* decision. Given the illustration above, it would be interesting to examine the determinants of the enthusiastic *CP* behavior of the Taiwanese hospitality publicly traded companies. Thus, this study makes a unique contribution to the corporate social responsibility (CSR) literature from both theoretical and corporate philanthropy perspectives.

The remainder of this study is organized as follows. Section 2 reviews the literature. Data and the variables are presented in Section 3. Section 4 reports methodology and empirical results. Discussion of the findings and conclusion are presented in Section 5.

2. Literature review

While researchers in the management, finance, and other fields are interested in the issue of *CP*, only a few empirical studies have examined the motives of *CP* given the limited data available. Brown et al. (2006) stated that *CP* motivated by value enhancement might boost corporate future revenue growth while philanthropic donation driven by agency cost may cause the managerial insiders to pursue their own interests. As a result, discretionary philanthropy

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