



How does corporate social responsibility contribute to firm financial performance? The mediating role of competitive advantage, reputation, and customer satisfaction



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ABSTRACT

Direct relationship between corporate social responsibility (CSR) and firm performance has been examined by many scholars, but this direct test seems to be spurious and imprecise. This is because many factors indirectly influence this relation. Therefore, this study considers sustainable competitive advantage, reputation, and customer satisfaction as three probable mediators in the relationship between CSR and firm performance. The findings from 205 Iranian manufacturing and consumer product firms reveal that the link between CSR and firm performance is a fully mediated relationship. The positive effect of CSR on firm performance is due to the positive effect CSR has on competitive advantage, reputation, and customer satisfaction. The final findings show that only reputation and competitive advantage mediate the relationship between CSR and firm performance. Taken together, these findings suggest a role for CSR in indirectly promoting firm performance through enhancing reputation and competitive advantage while improving the level of customer satisfaction.

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1. Introduction

Recognition of the direct relationship between CSR and firm performance has garnered much interest among authors recently. The findings are rather inconclusive and misleading (Margolis & Walsh, 2003; Mishra & Suar, 2010; Vogel, 2005). This is because, while a positive association between CSR and firm performance has been a dominant theme in many articles, universally, (e.g. Abu Bakar & Ameer, 2011; Oeyono, Samy, & Bampton, 2011; Orlitzky, Schmidt, & Rynes, 2003; Roshayani, Faizah, Suaini, Mustaffa, & Tay, 2009; Van Beurden & Gössling, 2008), others suggested a negative or no correlation (e.g. ACCA, 2009; Aupperle, Carroll, & Hatfield, 1985; Crisóstomo, Freire, & Vasconcellos, 2011; Malcolm, Khadijah, & Ahmad Marzuki, 2007).

Some scholars (e.g. Alafi & Hasonah, 2012; Galbreath & Shum, 2012; Griffin & Mahon, 1997; Margolis & Walsh, 2003; Rowley & Berman, 2000; Wood & Jones, 1995) questioned the applied approach taken by the majority of studies which have examined the direct relationship between CSR and firm performance. They claim that positive, negative or neutral results

obtained by examining the direct relationship between CSR and firm performance cannot be 100% reliable, as this link may be affected by some other intervening factors which many studies have omitted.

Finally, it can be concluded that the relationship between CSR and firm performance is more complicated than the results of many previous studies indicate. Accordingly, this study attempts to extend previous researches on the relationship between CSR and firm performance. In doing so, a new question that will be asked in this study is: 'Are competitive advantage, reputation, and customer satisfaction mediators in the relationship between CSR and firm performance?' In undertaking this study, and in addition to verifying some predicted CSR benefits such as customer satisfaction, reputation, and competitive advantage, the relationship between CSR and firm performance, which is more complex than most studies showed, will be tested.

Previous studies in different environmental management domains have predicted that customer satisfaction, reputation, and competitive advantage are three outcomes of CSR (e.g. Mulki & Jaramillo, 2011; Salmons, Perez, & Bosque, 2009; Walsh & Beatty, 2007). Firm performance is also positively affected by these three interdependent variables (Li, Ragu-Nathan, Ragu-Nathan, & Subba Rao, 2006; Matzler & Hinterhuber, 1998; Mulki & Jaramillo, 2011; Yamin, Gunasekaran, & Mavondo, 1999). Evidence has revealed that high levels of customer satisfaction have two main consequences for a firm including reputation

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and competitive advantage (Anderson & Sullivan, 1993; Matzler & Hinterhuber, 1998; Walsh, Dinnie, & Wiedmann, 2006). Therefore, customer satisfaction, reputation, and competitive advantage should be included together in studies on the relationship between CSR and firm performance.

Some authors attempted to identify the role of these variables as the main intervening variables in the relationship between CSR and firm performance (e.g. Alafi & Hasoneh, 2012; Galbreath & Shum, 2012; Luo & Bhattacharya, 2006; Margolis, Elfenbein, & Walsh, 2008; Margolis & Walsh, 2003; Rowley & Berman, 2000; Ullmann, 1985). For example, Luo and Bhattacharya (2006) and Alafi and Hasoneh (2012) examined only the role of customer satisfaction as a mediator in this relationship. Later Galbreath and Shum (2012) expanded Luo and Bhattacharya's (2006) and Alafi and Hasoneh's (2012) works by adding reputation as another mediator.

This study argues that the relationship between CSR and firm performance is more complex than previous researches have revealed. Therefore, sustainable competitive advantage which has been omitted as the final outcome of customer satisfaction and reputation (Awang & Jusoff, 2009) is assumed to be another effective mediator in this relationship. Accordingly, this study tests and develops a more complex relationship between CSR and firm performance by including three mediators (customer satisfaction, reputation, and sustainable competitive advantage) as three predicted benefits of CSR. Mediating these three variables directs future researches away from an indefensible direct relationship between CSR and firm performance.

It is worth noting that most studies on CSR and firm performance have been done in developed countries based on European and US data. Therefore, a sample from Iran as a developing country could be helpful in demonstrating CSR outcomes in a worldwide context. This is important as CSR has never been adequately addressed in Iranian businesses in practical terms and in the academic environment in theoretical terms (Chapardar & Khanlari, 2011). Moreover, evidence shows that expectation of CSR level among Iranian firm's stakeholders is higher than the actual level of CSR practiced by firms (Salehi & Azary, 2009). Therefore, sufficient ground exists for such studies in Iran which is mainly outside the scope of international researches and is underutilized as a selected sample in the area of CSR (Chapardar & Khanlari, 2011; Nejati & Ghasemi, 2012).

2. Literature and hypotheses development

2.1. Corporate social responsibility (CSR)

Over the last few decades, researchers have paid considerable attention to CSR. Therefore, it has become a prominent concept in management literature (de Bakker, Groenewegen, & den Hond, 2005; Dobers, 2009; Nejati & Ghasemi, 2012). In addition to theoretical aspects, companies have also become more active in engaging CSR in practice (Dahlsrud, 2008; McWilliams, Siegel, & Wright, 2006). The driving force behind this is an upsurge in environmentally sensitive consumers who are demanding sustainable and more environmentally friendly products and services (Gauthier, 2005; Van Beurden & Gössling, 2008).

Despite the large body of literature on CSR, there is still no unified and precise definition (Scherer & Palazzo, 2007; Wood, 2010). Thus, CSR does not mean the same thing to everybody (Van Marrewijk, 2003). Wood (2010) contends that this is because CSR is difficult to conceptualize. Talaei and Nejati (2008) also claimed that the lack of clear conceptual boundaries has led to these diverse definitions. In light of these claims, some authors (e.g. Lozano, 2008; Orlitzky, Siegel, & Waldman, 2011; Van Beurden & Gössling, 2008) believe that the lack of a clear definition makes it difficult to conduct empirical studies on CSR.

Despite the lack of a clear definition, all contending definitions of CSR agree on one thing, which is that firms must meet the expectations of society when planning their environmental management strategies

(Gossling & Vocht, 2007). According to Van Beurden and Gössling (2008) CSR answers the uncertainties that business corporations have to cope with in terms of the social context of the dynamic, global, and technological business arena that we witness today. In a well-known definition of CSR by Carroll (1979), CSR is the social responsibility of a business which includes the economic, legal, ethical, and discretionary expectations that society has of organizations at a given point in time.

Carroll's (1979) definition is the clearest conceptualization of CSR because, in addition to identifying the firm's obligations toward society, it systematically differentiates the firms' responsibilities from mere profit making and from the social responsibilities of governments (Chen, Chang, & Lin, 2012; Lozano, 2008; Wood, 2010). Proof of the strength of this claim is the variety of scholars who have used this definition in their studies (e.g. Galbreath, 2008; Galbreath & Shum, 2012; Sheth & Babiak, 2010; Shum & Yam, 2011).

This study considers the economic and ethical dimensions of CSR as presented by Carroll (1979). It is also argued by Turker (2009) that while economic responsibility should be distinguished from other responsibilities, they should be considered together in addressing CSR because financial interests are the fundamental reason for establishing a business, and corporate ethical behaviors, which are something beyond mere financial issues, are the main factor influencing an organization's survival (Nejati & Ghasemi, 2012).

2.2. CSR and firm performance

In the history of development economics, CSR has been thought of as a key factor in attaining economic goals and wealth generation (Garriga & Mele, 2004). Therefore, many studies attempted to find a global link between CSR and firm performance (e.g. Alafi & Hasoneh, 2012; Galbreath & Shum, 2012; Lin, Yang, & Liou, 2009; Luo & Bhattacharya, 2006; Margolis et al., 2008; Orlitzky et al., 2003; Rettab, Brik, & Mellahi, 2009; Shen & Chang, 2008; Van Beurden & Gössling, 2008). For example, empirical findings by some (e.g. Alafi & Hasoneh, 2012; Galbreath & Shum, 2012; Luo & Bhattacharya, 2006; Margolis et al., 2008; Shen & Chang, 2008) researchers showed a positive association between CSR and firm performance. Orlitzky et al.'s (2003) findings further support the idea presented by Garriga and Mele (2004). Their study, which involved a review of all 52 earlier surveys about the correlation between CSR and company performance, showed that more socially responsible companies had stronger economic results. Later, survey data was adopted from 280 companies in UAE by Rettab et al. (2009) to examine the connection between CSR operations and company performance; the outcome indicated that CSR has a positive association with all three determinants of company performance: monetary performance, personnel commitment, and corporate integrity. The impact of CSR on firm performance among 1000 Taiwanese cases was also examined and a positive association between CSR and monetary performance was identified (Lin et al., 2009). Galbreath (2008) also found strong positive links between CSR and organizational benefits among Australian firms. Consistent with previous studies, after examining 34 previous studies on CSR and firm performance linkage by Van Beurden and Gössling (2008), it was found that 68% of studies demonstrated a positive association. Lastly, the positive and strong relevance of CSR and firm performance was clearly supported by Alafi and Hasoneh's (2012) findings which had been done based on Housing Banks in Jordan.

Review of the available literature reveals that the majority of studies cited use developed European or US samples (Galbreath & Shum, 2012). Despite (1) the lack of study on CSR and firm performance in developing countries, especially in an Iranian context; (2) being underutilized as a selected sample in international researches (Chapardar & Khanlari, 2011; Nejati & Ghasemi, 2012); and (3) the existence of a negative gap between actual and expected level of CSR among Iranian firms (Salehi & Azary, 2009), we predict that similar results to that of Western countries will be found in Iran, a developing Asian country. It is worth

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