Internal and External CSR, differences between America and Europe

Abstract:

Purpose – The purpose of this study is to analyze the effect of Financial Performance (FP) on Corporate Social Responsibility (CSR). In particular, this study disaggregates CSR into external and internal CSR and evaluates the impact of FP on both CSR categories. Moreover, the study analyzes whether the effect of FP on CSR changes if the firm's country of origin is America or Europe.
Design/methodology approach – Using a quantitative method, the authors perform a general linear model analysis to look between differences regarding the region using Bloomberg's data, from 2014. The final sample consisted of 268 firms from USA and Canada (n = 86), Europe (n = 117), and Latin America (n = 65)
Findings – It was found that net income was the only variable of financial performance that positively affects total CSR expenditures. However, this effect is lower in USA and Canada than it is in Europe. We also found that European firms have higher internal CSR expenditures when compared with firms from USA and Canada, but the difference is not significant for external CSR expenditures, while firms in Latin America do not differ significantly from firms in Europe in their CSR expenditures.
Practical implications – This study will enlighten managers to know what the most profitable form of investment on CSR is, depending on the region where the firm is
Originality value – The value of the present work is to extant the literature about CSR, disaggregating it in external and internal and taking in count the region of the firms. The value that is generated through actions that favor any of the company's stakeholders.

Keywords: Corporate Social Responsibility (CSR), Financial Performance (FP), External CSR Expenditures, Internal CSR Expenditures.

INTRODUCTION

Corporate Social Responsibility (CSR) is a concept that has been evolving through time. This concept took recognizable shape in the 3rd decade of the 20th century. And the concept was defined as “corporations’ obligation for social betterment” (Frederick, 1994). CSR has taken an important role since multiple stakeholders took recognizable importance in the organization decisions (Carrol, 1991); organizations pay more attention to fulfill their stakeholders’ requirements regarding social, environmental and economic aspects. In a similar fashion, the triple bottom line definition of the CSR examines it in economic, social and environmental aspects (Elkington, 1998). This approach took a remarkable importance that even has important from a business perspective, actually, the World Business Council on Sustainable Development, “which comprises 150 of the world’s largest companies and which operates at the CEO level” (Wheeler, Colbert, & Freeman, 2003, p.16), employs this approach. Since the triple bottom line is considered a pragmatic proposal regarding CSR (Garriga & Melé, 2004) we have chosen to use this CSR approach in order to develop the study.

Since the economic aspect is really important for the company in order to growth or at least survive; there has been an effort in order to know whether the relation between Financial Performance (in the following FP) and CSR, if exists, is positive or negative (Reinhardt & Stavins, 2010). There are some efforts in order to identify the kind of relation between CSR and FP that are found in the literature. 3 different relations have been identified between FP and CSR: positive, negative or neutral/non-effect relations (Wood & Jones, 1995; Orlitzky, Schmidt, & Rynes, 2003; Reinhardt & Stavins, 2010). Not just the relation between CSR and FP has been studied, but even more this relation comparing different regions (Bennet, 1998; Maignan & Ralston, 2002). Other studies had looked at the relation that exists between FP and a disaggregate CSR e.g. implicit and explicit CSR (Matten and Moon, 2008).

However, little is known if the relation could change depending if the firm has external or internal CSR expenditures. Neither if this external or external expenditures are different depending on the region where companies are located. Hence, the purpose of this study is to analyze the effect of FP on CSR. In particular, this study disaggregates CSR into external and internal CSR and evaluates the impact of FP on both CSR categories. Moreover, the study analyzes whether the effect of FP on CSR changes if the firm’s country of origin is America or Europe.

At this stage in the research, external CSR expenditures will be defined as visible CSR initiatives that helps to enhance the community in which a firm is located; and internal CSR expenditures as invisible investments for the outsiders in order to enhance the firms regarding operation and work environment. This research focus on the economic variables that may explain the relation between FP and CSR, other non-economic variables were not included. However, the authors mentioned some non-economic variables that might be interesting to explore in future research.

LITERATURE REVIEW

Relation between FP-CSR

Studying the relation between FP-CSR is nothing new, actually, this relation has been a debate for decades, when studies show different conclusions regarding this relation (Hull & Rothenberg, 2008; Rowley & Berman, 2000). Table 1 exemplify some efforts of studying this causation through decades

Table 1

Positive Relation	**Reference**
There is a positive relation between CSR and FP, not only that but also there is virtuous circle in this relation since CSR is related to a better FP but at the same time a better FP causes a greater CSR investment	(Waddock & Graves, 1997)
It was found that in 127 empirical studies about the relation between FP-CSR, almost half of these studies found a positive relationship between these variables. While only seven found a negative relationship.	(Margolis & Walsh, 2003)
There is not only an improvement on the company’s FP when doing CSR but also doing CSR has an insurance-like benefit when a company suffer a negative event when CSR activities are focus on society at large instead of trading partners	(Godfrey, Merrill, & Hansen, 2009)
Neutral/non-effect relation	
Using a forced-choice instrument in order to analyze the relationship between an orientation toward CSR and profitability it was found that there is no relationship between CSR and a better FP.	(Aupperle, Carroll, & Hatfield, 1985)
The relation between CSR and FP was not by itself but because of R&D intensity and advertising intensity. With their new model the authors found that there is a neutral relationship between CSR and FP.	(McWilliams & Siegel, 2000)

"There is no relationship between the two variables, as the general equilibrium principle cancels out the costs and benefits from socially responsible corporate behavior, thereby neutralizing any possible interaction"	(Ducassy, 2012)
Negative relation	
Found a negative relation when taking in count the year after when the CSR action was made.	(Vance, 1975)
Using Market Value-Added as a market-based measure for FP, and social issue participation as a measure of Corporate Social Performance (CSP), it was found a negative relationship	(Hillman & Keim, 2001)
Regarding the diversity concerns there is a negative relationship between this variable and stock returns of the firm.	(Bird, Hall, Momentè, & Reggiani, 2007)

Even though, it is shown that it is not a clear conclusion about the relation between FP-CSR, these mixed results might be explained because of the different methods to measure CSR and the different theoretical approaches even the misunderstanding of the approaches. Meta-analysis shows that indeed there is a positive and significant effect on FP depending on the firm's CSR (Wang, Dou, & Jia, 2016). It is important to mention that the relation between CSR and FP, it is best seen on the long-term instead of short term. (Nollet, Filis, & Mitrokostas, 2016). It is also particularly interesting how the causation is not clearly identified. For the purpose of this research, the authors followed the causation explained by Margolis, Elfenbein and Walsh (2009) finding that the relation between CSR and FP is that a better FP leads to a higher CSR, then the authors will focus only in studying this causation.

Internal and External CSR

Stakeholder theory serve as a theoretical lens to explain some drivers of CSR, in the case of this theory, the relations between the firm and its environment, particularly its stakeholders (Frynas & Yamahaki, 2016). Therefore, this theory is suitable for informing the relation of FP-CSR that is the purpose of this work. Stakeholder theory assumes that there are particular stakeholders that are more important to the firms and that the firms must attend their needs in order to survive and growth (Bridoux & Stoelhorst, 2014; Mitchell, Agle, & Wood, 1997). Firms need the recognition of both the internal and external stakeholders this could be achieved through CSR actions (de Sousa Filho, Wanderley, Pasa Gómez, & Farache, 2010).

On the other hand, from institutional theory lenses, internal actions are explained to be driven for conformity with legitimized structures, while external actions are driven by looking of public endorsement. However, this is conceptually similar to the distinction of internal and external audiences in the stakeholder theory. It is also similar that legitimacy is critical for a firm's survival and growth (Hawn & Ioannou, 2016).

Hence, there is a necessity of knowing how different CSR actions can impact on both internal and external stakeholders making a disaggregate CSR important. Also, there are some limitations of using just one CSR measure when looking for a relation between CSR and some measures of the firm's FP. That is why, some researchers suggest using not just one measure for CSR, even thought it would represent a higher effort of gathering data (Burke & Logsdon, 1996). Therefore, there have been some efforts looking for measures of CSR disaggregating it. The internal and external CSR has been studied in different ways, such as how a firm looks for recognition from internal and external stakeholders (Burke & Logsdon, 1996).

Regarding definition, the internal and external components of CSR had been defined. The foremost as aspects of CSR that are related to the internal operation of the organization and the latter as actions related to enhance firm's reputation such as philanthropy and community contributions (Brammer, Millington, & Rayton, 2007). Therefore, the authors used measures about the investment in operational sustainability for the internal CSR and measures of community spendings for the external CSR.

There had also been explored the internal and external motives of CSR and associating the internal ones with community related activities and internal with management of sustainability at the company level (Pérez-López, Moreno-Romero, & Barkemeyer, 2015). Some external motives found by Pérez-López et al. (2015) were related with reputational benefits, while internal motives were related to improvement inside the company such as employee training and improve in operational performance. these findings are in line with the indicators of internal and external CSR propose by the authors.

A recent study shows that there is a joint effect of external and internal CSR on a better market value; furthermore, it is explained that the degree to which firms focus on external or internal CSR is significantly different (Hawn & Ioannou, 2016). According to the authors, this distinction and how they interplay may be associated with firm performance, has not been fully explored.

Based on the literature mentioned above, and both, stakeholder theory and institutional theory. A general hypothesis regarding the well-known relation between FP-CSR was developed as follows:

H1: Firms with higher financial performance have a higher level of an overall CSR expenditure.

To look at the specific effect of internal and external measures of CSR, the authors proposed the following two hypotheses that arise from H1 and based on stakeholder theory and its assumptions that the firm focus more on certain specific stakeholder, hypotheses were developed as follow:

H1a: Firms with higher financial performance have higher levels of CSR external expenditure.

H1b: Firms with higher financial performance have higher levels of CSR internal expenditure.

CSR differences between America and Europe

When looking at differences between countries, institutional theory serves as a theoretical lens, since CSR is conceived trough this theory as an outcome of societal norms (Frynas & Yamahaki, 2016). It explains how firms from different countries, may have their own motives to do CSR in order to obtain legitimization of their stakeholders (Babiak & Trendafilova, 2011). Actually, differences in political, educational, and cultural systems of countries had shown to have an impact of how firms do CSR (Ioannou & Serafeim, 2012).

There are some differences in the conceptualization of CSR in Europe and America as suggested by Maignan & Ralston (2002) it is stated that the USA' companies tend to mention more explicitly their CSR actions on websites that they European counterparts. Following this, Matten and Moon (2008) found that indeed the USA tend to focus on what can be "shown", called it the explicit CSR, while European countries seem to "work in the shadows" doing an implicit CSR. However, Jackson and Apostolakou (2010) found that there are some similarities between the companies in USA and the ones in Anglo-Saxon countries. They findings suggest that what Matten and Moon is true but for the rest of Europe.

On the other hand, there have been studies that show a comparison between regions, showing that there are some similarities between the CSR between European and American firms except for Mexican firms (Welford, 2005). But other works recognized that there are differences between firms from countries such as UK and USA (Aguilera, Williams, & Conley, 2006) or even regarding the region of North America vs. Europe (Luna Sotorrío & Fernández Sánchez, 2008). However, little is known about the interaction between internal and external CSR and the region of the firm.

Since, it has been shown that USA had focused more on “visible” and Europe on non-so-visible aspects of CSR. We can expect that this trend to occur on external and internal CSR respectively. Hence, we theorize that:

H2a: Firms from the American continent have higher external CSR expenditures when compared with firms from Europe

H2b: Firms from the European continent have higher internal CSR expenditures when compared with firms from America

METHODOLOGY

Using Bloomberg’s data of firms from 2008-2015, panel data analysis was initially performed. However, the authors recognized that time was not statistically significant. Hence, another type of analysis was necessary to analyze the data. The authors perform a general linear model analysis to look between differences regarding the region using the data from 2014.

The sample consisted of 268 firms from USA and Canada (n = 86), Europe (n = 117), and Latin America (n = 65). The countries of origin are shown in Table 2. In this sample, 75% of companies reported "community spending" and 49% "investments in sustainability” (Table 3 provides descriptive statistics for region). Following Shahzad & Sharfman (2015) suggestions, the authors included those firms that do not invest their money on CSR activities in order to avoid sample-selection bias of only those who actually invest on CSR.

To operationalize the CSR internal and external measures, the Bloomberg indicators “investment in operation sustainability” and “community spending” were used. As specified by Bloomberg, the first one is related with the amount of money spent by the company, in millions of dollars, on operational environmental and social compliance and other internal environmental and social initiatives, as defined by the company such as pollution prevention, recycling, employee training, safety initiatives etc.; the second one, is related with the amount of money spent by the company on community-building activities, in millions of dollars.

Also, financial performance will be defined as the profitability of the firm measured by net income, stock price, ROE, ROA. Following Waddock & Graves (1997) control variables were size and risk which was measured by number of employees and long-term debt over total assets respectively.

ANALYSIS AND RESULTS

We applied a regression models for each dependent variable ("total CSR", "community spending" and "investment in sustainability"). We used as predictors: financial performance variables ("return on asset", "return com eqy", "change in share price", "net income"), control variables ("num of employees", "lt debt to tot asset"), and dichotomic variables for region ("USA and Canada", "Latam"). Due to sample size limitations, only main effects were evaluated.

We tested for the possible presence of multicollinearity. We followed generally accepted tolerance values of variance inflation factor (VIF) up to 10 (Hair et al, 2009). Because none of the VIF values exceeded 10, we did not consider collinearity a problem.

Table 4 gives the standardized regression coefficients for the regression models. For the overall model, the results show that "net income" affects total CSR expenditures (β = 0,753, $p < 0{,}001$), also "number of employees" (β = -0,195, $p < 0{,}05$), and "USA and Canada" (β = -0,241, $p < 0{,}05$), were significant. The rest of the variables have no effects on the total CSR expenditures. H1 suggest that firms with higher financial performance have a higher level of total CSR expenditures. This prediction is partially supported.

For the model of "community spending", the results show that "net income" affects community spending (β = 0,5451, $p < 0{,}05$), but the other independent variables, including those of region, were not significant ($p > 0{,}05$). H1a holds that firms with higher financial performance have higher levels of CSR external expenditure. That prediction is partially supported.

In the regression model with "investments in sustainability" as dependent variable, "net income" (β = 0,691, $p < 0{,}001$), "number of employees" (β = -0,211, $p < 0{,}05$), and "USA and Canada" (β = -0,223, $p < 0{,}05$), were significant. The rest of the variables have no effects on investments on sustainability. H1b suggest that firms with higher financial performance have higher levels of CSR internal expenditure. That prediction is partially supported

Regarding the differences between region, these findings support H2b but fail to support H2a. We find that European firms have higher internal CSR expenditures when compared with firms from USA and Canada, but the difference is not significant for external CSR expenditures. Firms in Latin America do not differ significantly from firms in Europe in their CSR expenditures.

Table 2: Country

REGION		Frequency	REGION		Frequency
Europe	Austria	2	USA and Canada	Canada	16
	Belgium	1		USA	70
	Czech Rep.	1		Total	86
	Denmark	1	Latin America	Argentina	2
	Finland	6		Brazil	35
	France	8		Chile	5
	Germany	18		Colombia	9
	Greece	6		Mexico	11
	Hungary	2		Peru	3
	Ireland	1		Total	65
	Italy	15			
	Luxembourg	1			
	Netherlands	1			
	Poland	2			
	Portugal	3			
	Romania	1			
	Spain	20			
	Sweden	2			
	Switzerland	8			
	United Kingdom	18			
	Total	117			

Table 3: Descriptive statistics

	USA and Canada		Europe		Latin America	
	Community spending	Invest. in sustainability	Community spending	Invest. in sustainability	Community spending	Invest. in sustainability
Valid	63	31	95	62	42	39
Missing	23	55	22	55	23	26
Mean	57,53	285,69	25,15	268,75	19,15	28,34
Std. Dev.	143,977	1069,846	38,342	894,838	36,929	50,804

Table 4: Standardized regression coefficients

	Dependent variables								
	Total CSR			Community spending			Invest. in sustainability		
	Beta	t		Beta	t		Beta	t	
(Constant)		3,006			1,334			2.985	
ROA	-0,147	-0,848		-0,053	-0,729		-0,154	-0,947	
ROE	0,048	0,278		-0,033	-0,477		0,056	0,338	
D_Px	0,072	0,825		0,013	0,185		0,084	0,981	
Net income	0,753	7,447	***	0,545	6,869	*	0,691	7,148	***
Employees	-0,195	-2,071	*	0,035	0,489		-0,211	-2,330	*
Debt ratio	-0,142	-1,703		-0,037	-0,567		-0,122	-1,524	
USA and Can.	-0,241	-2,468	*	-0,001	-0,018		-0,223	-2,334	*
Latin America	-0,077	-0,883		0,016	0,230		-0,088	-1,057	
Observations	100			183			120		
R^2	0,426			0,309			0,356		

* p < 0,05, ** p < 0,01, *** p < 0,001

CONCLUSION

First of all, it is interesting how other studies (Bird, Hall, Momentè, & Reggiani, 2007; Nollet, Filis, & Mitrokostas, 2016) had found that the relation between FP-CSR is more visible through time. However, in this study it was found that time is not a significant variable when looking for a relation between these two variables when using an economic measure for CSR, specifically CSR expenditures. Not even when disaggregating the CSR on internal and external it is shown to have a different behavior. It is also remarkable that, unlike other studies (Waddock & Graves, 1997) which found that the relation between FP-CSR is true for different indicators of firm’s financial performance. This study only found statistical support for net income.

Second, it seems that net income has a greater impact on the internal CSR (β = 0,691) than on the external CSR (β = 0,5451). However, this finding may be taken with caution since the European firms are shown to focused more on the internal CSR but also, they represent a bigger number of firms (n=117), comparing with those in USA and Canada (n=86) which focus less on the internal CSR (β = -2,334). This behavior was expected since previous literature (e.g. Maignan & Ralston, 2002) shows that European firms have a special focus on CSR regarding environmental actions.

Third, at present, with the appearance of the Sustainable Development Goals, SDG of the United Nations, a commitment that has been assumed by large companies, countries and civil society organizations, through the Global Compact, investment in them , is more oriented to diminish the negative impacts or externalities produced by the business world with research and development, governments with the creation of laws and citizenship with responsible behavior. In the case of companies, as we pointed out earlier, in Europe most of the companies invest in the 17 SDGs that are classified in five dimensions, in the dimension Planet, People and Prosperity, without being clear yet, how to participate in Peace and Partnerships'.

Finally, the number of employees seems to have a negative impact on the CSR expenditures; in other words, firms with higher numbers of employees has smaller CSR overall and internal expenditure. This might be explained because, when a firm has a huge number of employees, some investments such as training, which is part of the internal expenditures, become a big investment of resources for the firm to invest in.

IMPLICATIONS AND VALUE

The implications of this work will be to know how the internal and external CSR expenditures are related with a firm's Financial Performance depending on the region. This study will enlighten managers to know what the most profitable form of investment on CSR is, depending on the region where the firm is. An important implication for the company, is that although it is true, one tends to see the results financed as essentially monetarized; We seldom do the same with the intangible value that can be given to the company that deals in investing in favor of some of its stakeholders. Without appreciating that this can generate intangible results that are profitable in the long term for the company.

The value of the present work is to extant the literature about CSR, disaggregating it in external and internal and taking in count the region of the firms. The value that is generated through actions that favor any of the company's stakeholders, considerably returns, through materialization's and intangibles that improve the organizational quality.

LIMITATIONS AND FUTURE RESEARCH

We acknowledge some limitations on this research, such as including just economic variables in order to look for a relation of CSR and FP. While by doing this, we try to avoid some difficult to objectively measure variables, we must recognize the importance of non-economic values like reputation. The way that reputation can create value for the company has been explored (Fernández Sánchez & Luna Sotorrío, 2007). It might be interesting to include reputation in future research, since reputation is valuable not just for investors but for the general public and have an impact on share value (Raithel & Schwaiger, 2015).

On the other hand, future research might explore the relation between the firm's financial performance and the Sustainable Development Goals. Since, this perspective introduces new concepts that go beyond CSR. However, new data should be gathering to look for this relation because firms might not had incorporated this approach before 2015.

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