

# Corporate Social Responsibility and Profitability in the Banking Sector: The Case of Selected Private Banks in Ethiopia

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## ABSTRACT

In this article, we explore the relationship between corporate social responsibility and profitability with particular reference to Ethiopian financial industry. In line with this, the paper investigated the practice of corporate social responsibility and its impact on profitability in two private banks in Ethiopia. The study used two sampling phases. The first one is to sample out the two banks among the sixteen private banks operated in the country and the second phase is to select number of respondents within the selected banks. According to National Bank of Ethiopia, (NBE, 2020) annual report among the sixteen private commercial banks operated in the country, six of them were operated in the industry for more than 20 years and two banks namely Dashen and United banks were randomly selected for the study. The study used questionnaires as an instrument for data collection and the Cronbach alpha test was used to test the reliability of the instrument. Correlation analysis was carried out to identify the nature of strength and direction of the relationship between the independent variables (philanthropic, ethical, legal and economic responsibilities) and the dependent variables (profitability), regression analysis was also employed to determine the degree in which the dependent variable can be predicated or explained from the independent variables. The finding reveals that ethical, philanthropic, legal and economic responsibilities of CSR dimension have a positive and significant impact on profitability of the banks. Furthermore, the overall finding of the study suggested that CSR practice of banks has a significant impact on the level of their profitability. The study recommends that banks should improve their efforts exerted towards their CSR practice in order to enhance their profitability.

**Keywords--** Banks, CSR, Philanthropic Responsibility, Ethical Responsibility, Legal Responsibility, Economic Responsibility, Profitability

## I. INTRODUCTION

Recently corporate social responsibility (CSR hereafter) is developing as a significant feature of business philosophy which emphasized on responsibility towards all stakeholders (shareholders, employees, creditors, suppliers, government, and community) rather than only on maximization of profit for shareholders. Islam (2012) stated that the concept of business has changed from profit making activities to social welfare

activities where businesses are not only responsible to its shareholders but also to all of its stakeholders. Mc Williams and Siegel (2001) defined CSR as efforts of an organization towards achieving commercial success while adopting ways that appreciates and facilitates communities, societies, people and environment at large. Similarly, the European commission (2001) describe CSR as a concept whereby companies integrate voluntary, social and environmental concerns in their business operations and in their interaction with other interested parties.

As the issue of sustainable development grows significantly, CSR becomes an element that addresses these issues. Since financial institutions particularly bank's play a crucial role in financing the economic and developmental activities of the world, their contribution towards sustainable development is undeniable. Studies conducted by Belás et al. (2014; 2015) and Chochořáková et al.(2015) prevailed that implementation of CSR in banks have economic, social and environmental features. When seeing the economic aspect of CSR, the main focus is on the financial or economic performance of banks which is the main objectives of their establishment. Workplace rules and regulations, philanthropic activities and protection of human rights are included in the social aspect of CSR. The environmental aspect of CSR includes bank's policy towards the protection of the environment and the degree of financing socially responsible projects.

The price and quality of a product are no longer the main competitive advantages; it is ethical view and social practices that are considered the key factors which can stimulate customer response (Bussey, 2006 as cited in Chang, 2017). Studies show that customers are willing to reject a firm with no social responsibility by switching to another firm that practice CSR (Webb, Mohr, & Harris, 2008). This switching behaviour might affect the firm's revenue and reputation negatively (Brunk, 2010). In this regard, Banks need to be socially responsible to be able to build their "reputational capital", thereby enabling them to attract high quality employees, negotiate better contracts, expand their customer base, attract investors and win public trust and confidence (Achua, 2012).

Existing studies show that CSR impacts the financial performance of firms (Lins et al., 2017), their

market value (Ding et al., 2016; Ferrell et al., 2016), and their financial risk (Kim et al., 2014). Some authors have tried to empirically assess the relationship between CSR and banks' profitability. They tend to show a positive link between CSR and bank profitability indicators such as return on assets or return on equity. (Nizam et al., 2019; Wu and Shen, 2013; Shen et al., 2016; Wu et al., 2017). However, (Berger and Humphrey, 1997) argued that using ratios to assess the performance of banks has some limitations. Indeed, the univariate nature of ratio analysis may be problematic when analysing complex multidimensional organizations, such as banks, which produce multiple outputs using multiple inputs, so to avoid the shortcomings of ratio analysis, efficiency frontier techniques were used by most studies focusing on bank performance.

Despite the fact that, Ethiopian banking sector is believed to be growing in recent times as the number of banks escalates and branch outreach also diversified, it is important to examine the impact of CSR practice on their profitability. Therefore, the study provides an empirical evidence that examines the impact of CSR practice and its impact in the banking sector of Ethiopia by focusing on two private banks, namely Dashen bank and united bank.

## II. THEORETICAL FRAMEWORK

This section presents the theoretical framework that the study draws on. It is adopted from the Carol's CSR pyramid specifically the economic, legal, ethical and philanthropic responsibility of CSR which consists of activities towards shareholders, customers, employees, environment, society, and other stakeholders (Freeman et al., 2010). In this study, relevant components from the established models have been selected to fit the research objectives. Primary data will be used to gather information regarding the practice of CSR with respect to Carol's CSR pyramid and its impact on profitability of selected banks and regression analysis will be used to assess the relationship between CSR and profitability's of the respective banks.

### *Economic Responsibility*

Economic responsibility is the foundation of the pyramid on which all other responsibilities stand, and concerns with firm's performance in a manner consistent with maximizing earning per share as well as maintaining strong competitive position (Carroll, 1991).

### *Legal Responsibility*

Legal responsibility requires a firm to operate with compliance to the laws and regulations of a country and also meets its legal obligations in the process (Carroll, 1991).

### *Ethical Responsibility*

Ethical responsibility relates with performance of a firm in a manner consistent with expectations of societal norms and ethical norms as well as preventing

ethical norms from being compromised in order to achieve corporate goals (Carroll, 1991).

### *Philanthropic Responsibility*

Philanthropic responsibility refers to performing in a manner consistent with philanthropic and charitable expectations of society and also assists voluntarily those projects that enhance a community's quality of life (Carroll, 1991).

## III. RESEARCH QUESTIONS AND OBJECTIVES

There were an effort in this study to provide answers to the following research questions:

1. What is the dominant practice of CSR dimension in selected private banks?
2. Is there significant relationship between CSR and profitability in selected private banks?
3. Which CSR dimension has more impact on profitability?

In line with the above research questions, the following objectives were established.

- I. To identify the common dimension of CSR practice in selected banks.
- II. To assess the relationship between CSR practice and profitability in selected banks.
- III. To identify the CSR dimension which has more impact to profitability in the selected bank.

## IV. RESEARCH METHODOLOGY

The role of methodology is to carry on the research work in a scientific, and valid manner. Methodology comprises the approach, strategy, methods and procedures adopted to conduct research (Chaston and Mangles, 2003).

### *Research Design*

The research design refers to the overall strategy that is chosen to integrate the different components of the study in a coherent and logical way, thereby, ensuring it will effectively address the research problem; it constitutes the blueprint for the collection, measurement, and analysis of data. The type of research design undertaken in this study was a deductive cross-sectional survey that adopt quantitative approach.

### *Target Population and Sampling Technique*

According to NBE (2020) annual report there are sixteen private commercial banks operated in the country. For the purpose of this study six banks were identified based on their year of establishments, which operated about 20 years and above in the industry. Then Dashen and United banks were randomly selected for this study.

The target population of the study were Head office employees of Dashen bank and United banks. Population for the study were 1,532 employees, 1006 were employees of Dashen bank and the rest 526 were United bank employees.

**Sample Size Determination**

The study employed sample determination method developed by Yemane (1967) to determine a

sample size with Confidence level is 95 % and precision level is 0.05.

The formula is:

$$n = \frac{N}{1+N(e^2)}$$

Where,

N= is the population size

e = is the level of precision or sampling error

$$\begin{aligned} n &= \frac{N}{1+N(0.05^2)} \\ &= \frac{1532}{1 + 1532 (0.05)^2} \end{aligned}$$

Sample Size = 317

Hence, 208 samples were selected from Dashen bank and 109 from united bank according to their proportion to the target population.

**Data Source and Collection Techniques**

The study employed primary data to get reliable and relevant information. A structured self-administered questionnaire, with a five-point Likert scale ranging from 'strongly disagree' (1) to 'strongly agree' (5) were used to gather the data. The constructs in the questionnaire were developed from the literature review. The questionnaire were adopted from different journals and modified to address the specific research objective of this study.

**Data Analysis and Presentation Method**

Using SPSS version 20, descriptive analysis was employed and Correlation analysis was carried out to identify the nature of strength and direction of the relationship between the independent variables (philanthropic, ethical, legal and economic responsibilities) and the dependent variables (profitability), regression analysis was also employed to determine the degree in which the dependent variable can be predicated or explained from the independent variables Before this, the model was tested for classical linear regression model assumptions such as heteroscedasticity, autocorrelations, multicollinearity,

normality and linearity assumptions and the model satisfy the classical linear regression model assumptions. Besides, reliability test was performed; i.e., Cronbach alpha coefficients were computed for each of the variables being assessed by the instrument. Cronbach Alpha Coefficients for each of the construct of CSR of this study were 0.785 for Philanthropic responsibility, 0.894 for Ethical responsibility, 0.897 for Legal responsibility, 0.810 for Economic responsibility and 0.833 for profitability. According to Pallant (2010), a Cronbach alpha value of at least 0.7 can be regarded as an acceptable level of reliability. Therefore, each coefficient was statistically significant and very satisfactory compared to normal standards of reliability.

**Result**

Descriptive, correlation and multiple linear regression were employed to identify the extent and degree of relationship between the dependent variable (profitability) and the independent variables (dimensions of CSR).

**Descriptive Result and Interpretation**

The discussion attempts to accomplish the objectives of the study, and answer the research questions. The survey was conducted with 317 respondents representing 100 percent of the sample size.

**Philanthropic Responsibility**

	N	Mean	Std. Deviation
The bank provides support for national pride and government campaigns.	317	3.56	.694
The bank provides support for the art culture science and sport.	317	3.68	.682
The bank makes contributions and donations to charitable bodies and community.	317	3.53	.673
Managers and employees of the bank participate in charitable activities of their local communities.	317	3.78	.823
The bank responds to natural and human made disasters	317	3.56	.820
Valid N (list wise)	317		

Source: survey results and own computations

The above table shows the mean and standard deviation scores of philanthropic responsibilities under taken by selected private banks. Managers and employees of the bank who participated in charitable activities of their local communities has a higher mean score of 3.78 with standard deviation of 0.823, followed by activities associated with providing support for the art, culture, science & sport has a mean score of 3.68

with standard deviation of 0.682. Banks response to natural and human made disasters has a mean score of 3.56 with standard deviations of 0.820. Likewise, banks support for the national pride and government campaign has a mean score of 3.56 and standard deviations of 0.694. The lowest mean of 3.53 and standard deviations of 0.673 is scored by banks activity towards making donation and contribution to charitable bodies.

**Ethical Responsibility**

	N	Mean	Std. Deviation
The bank has well developed ethical principle and communicated to its employees.	317	3.73	.962
The bank operates in a manner consistent with expectations of societal and ethical norms.	317	3.74	.890
The bank has good corporate governance.	317	3.64	.848
The bank motivates its employees through recognition, appreciation and reward.	317	3.93	.939
The bank works towards improving working conditions to its employees.	317	3.38	.995
The bank facilitates various training for its employees to improve their capacity.	317	3.70	.776
The bank gives due care for the health and safety of its employees	317	3.68	.791
Valid N (list wise)	317		

Source: survey results and own computations

The above table shows the mean and standard deviation score of banks activity related with ethical responsibility. Hence a higher mean of 3.93 is scored by activities undertaken by the banks to motivate their employees through recognition, appreciation and reward

with standard deviations of 0.939 and the lowest mean is 3.38 which is scored by activities under taken by the banks towards improving working conditions to their employees with standard deviations of 0.995.

**Legal Responsibility**

	N	Mean	Std. Deviation
The bank operates in compliance with NBE's directives and regulation.	317	3.85	.507
The bank discharges its activities in compliance to the rules and regulations of the country.	317	3.87	.610
The bank reports its financial statement in accordance with international reporting standard.	317	3.83	.672
The bank communicates its financial statement to the public.	317	3.84	.692
Valid N (list wise)	317		

Source: survey results and own computations

The above table shows the mean and standard deviation score of banks activity related with legal responsibility. Discharging its activities in compliance to the rules and regulation of the country scores a higher mean of 3.87 and standard deviations of 0.610. The

lowest mean is 3.83 with standard deviations of 0.672 which is scored by activities associated with reporting its financial statement with respect to international reporting standard.

**Economic Responsibility**

	N	Mean	Std. Deviation
The bank has clearly designed strategies to reduce operating cost.	317	3.69	.786
The bank continuously strives to achieve service excellence.	317	3.71	.909
The bank develops new product, redefining the existing ones and creating new channels based on customer demand.	317	3.67	.904
The bank has good risk management policy and strategy.	317	3.61	.900
Valid N (list wise)	317		

Source: survey results and own computations

According to the above table, the banks continuous effort to achieve service excellence scores the highest mean of 3.71 and standard deviations of

0.909 and the lowest is the banks risk management policy and strategy with a mean of 3.61 and standard deviation of 0.900.

**Profitability**

	N	Mean	Std. Deviation
Banks CSR practice guarantees the customer confidence level and corporate loyalty.	317	3.73	.843
Banks image brand improved by its CSR practice.	317	3.86	.836
CSR increased the market share of the bank.	317	3.71	.877
CSR practice gives a positive reputation advantage to the bank.	317	3.66	.770
Valid N (list wise)	317		

Source: survey results and own computations

The above table shows the mean and standard deviation scores of activities related with banks profitability. In this regard, improvement of banks image and brand as a result of its CSR practice score the

highest mean of 3.86 and standard deviations of 0.836. In contrary, a positive reputations advantage gained by the bank as a result of its CSR practice score the lowest mean of 3.66 and standard deviations of 0.770.

**Mean of CSR Dimension**

	N	Mean	Std. Deviation
Philanthropic Responsibility	317	3.6221	.38272
Ethical Responsibility	317	3.6863	.53837
Legal Responsibility	317	3.8478	.47723
Economic Responsibility	317	3.6703	.69481
Valid N (list wise)	317		

Source: survey results and own computations

The above table shows that the corresponding mean and standard deviation of all construct totals (total of every individual categorical construct). Consequently, legal responsibility total has a mean of 3.84, followed by ethical responsibility total has a mean of 3.68, economic

responsibility total has a mean of 3.67, and philanthropic responsibility total has a mean of 3.62. Therefore, the dominant CSR practice in selected banks is legal responsibility.

**Correlation Matrix**

	Profitability	Philanthropy	Ethical	Legal	Economic
Profitability	1				
Philanthropy	.468**	1			
Ethical	.542**	.492**	1		
Legal	.468**	.498**	.519**	1	
Economic	.494**	.443**	.635**	.519**	1

\*\*Correlation is significant at the 0.01 level (2-tailed).

N=317

Source: survey results and own computations

The above table shows the correlation between CSR dimensions (philanthropy, ethical, legal and economic responsibilities) and profitability in selected private commercial banks in Ethiopia.

The strongest relationship is between bank’s profitability and ethical responsibilities of the banks ( $r = 0.542^{**}$ ,  $p < 0.01$ ). This means that banks with well-developed ethical principle, operates in a manner consistent with expectations of societal and ethical norms and good corporate governance will results an increase in the profitability of the bank.

The relationship between bank’s profitability and economic activities of the banks is positive and significant ( $r = 0.494^{**}$ ,  $p < 0.010$ ), which means that bank’s with clearly designed strategies to reduce operating cost, well developed risk management policy and strategy, continuously develop new product and new channels will increase the profitability of the banks.

The bank’s philanthropy activities and its profitability has also positive relationship with  $r =$

$0.468^{**}$ ,  $p < 0.01$ . This reflects that an increase in philanthropic activities in society such as donation to charities, provide support for the victims of natural and human made disasters and some other similar activities will results an increase in bank’s profitability. Similarly, the bank’s legal responsibilities and its profitability has also positive relationship with  $r = 0.468^{**}$ ,  $p < 0.01$ . Therefore, all dimensions of CSR were positively correlated with the bank’s profitability.

**Regression Analysis**

Regression analysis is used to determine the degree in which the dependent variable can be predicated or explained from the independent variables. It is also used to understand by how much each independent variable (Philanthropic, Ethical, Legal and Economic) explains the dependent variable that is profitability.

The model summary below shows the statistical relationship of the dependent variable (profitability) and independent variables (CSR).

**Model Summary**

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.268 <sup>a</sup>	.072	.060	.60686
2	.650 <sup>b</sup>	.422	.407	.48195
a. Predictors: (Constant), experience, gender, education, age				
b. Predictors: (Constant), experience, gender, education, age, Ethical, Philanthropic, Legal, Economic				

Source: survey results and own computations

From the above table the demographic characteristics statistically predicted profitability of selected banks. From this finding R is equal to 0.268 which shows the presence of weak correlation between the demographic factors and dependent variable and R Square is 0.072 which indicated that demographic factors explain 7.2% of the variations on profitability of the dependent variable with unexplained factors of 92.8%.

Similarly, the 2<sup>nd</sup> model in the above table shows the independent variables of CSR statistically predicted profitability of selected banks. From this finding R is equal to 0.650 which indicates that the presence of strong correlation between the independent variables and dependent variable and R Square is 0.422 which indicates that independent variables of CSR explain 42% of the variations on profitability of the dependent variable with unexplained factors of 58%.

**ANOVA**

ANOVA <sup>a</sup>						
Model		Sum of Squares	DF	Mean Square	F	Sig.
1	Regression	8.887	4	2.222	6.033	.000 <sup>b</sup>
	Residual	114.902	312	.368		
	Total	123.789	316			
2	Regression	52.249	8	6.531	28.118	.000 <sup>c</sup>
	Residual	71.540	308	.232		
	Total	123.789	316			

a. Dependent Variable: profitability  
 b. Predictors: (Constant), experience, gender, education, age  
 c. Predictors: (Constant), experience, gender, education, age, Ethical, Philanthropic, Legal, Economic

Source: survey results and own computations

In the above table analysis of variance shows the variance of the variables which the researcher established at the F ratio ( $F(8, 308) = 28.118, p = .000$ ) is statistically significant at  $p < .05$  level of significance.

This indicates the CSR dimensions of philanthropic, ethical, legal and economic activities has statistically significant impact on the profitability of selected private commercial banks in Ethiopia.

**Effect of CSR on Profitability**

Model		Unstandardized Coefficients		Standardized Coefficient's	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	3.051	.210		14.501	.000
	gender	.228	.074	.172	3.064	.002
	age	.106	.043	.188	2.466	.014
	education	.233	.069	.189	3.366	.001
	experience	-.186	.053	-.268	-3.490	.001
2	(Constant)	-.057	.308		-.186	.852
	gender	.189	.060	.143	3.176	.002
	age	.076	.035	.134	2.184	.030
	education	.116	.056	.094	2.082	.038
	experience	-.149	.043	-.215	-3.471	.001
	Philanthropic	.258	.088	.158	2.940	.004
	Ethical	.328	.070	.282	4.672	.000
	Legal	.214	.073	.163	2.932	.004
Economic	.124	.054	.138	2.304	.022	

a. Dependent Variable: profitability

Source: survey results and own computations

The above table shows that, all of the independent variables (Philanthropic, Ethical, Legal and Economic) have a statistically significant relationship with the dependent variable (profitability) since their p-value is below the alpha level which is 0.05.

Regarding the standardized beta coefficients, the predictors of the dependent variable were ethical responsibility with a beta value of 0.282, legal responsibility with a beta value of 0.163, philanthropic responsibility with a beta value of 0.158 and economic responsibilities with a beta value of 0.138. Therefore, all the four independent variables has a positive impact on the dependent variable. Similarly, the demographic background of respondents of gender, age, education and experience have significant impact on profitability.

**V. DISCUSSION AND CONCLUSION**

The study is associated with the dimensions of CSR towards profitability in banking industry. The objective of this study is to examine the relationship between CSR practice and profitability in the banking industry, specifically in Dashen and United banks, by analysing the relationship of every construct in the theoretical framework.

The theoretical framework of the study is adopted from Carroll (1991) model of social responsibilities, particularly philanthropic, ethical, legal and economic responsibilities. In this regards the finding of the study revealed that all the four dimensions of CSR are commonly practiced in selected private banks in Ethiopia. To this end, the most performed CSR practice in selected private banks in Ethiopia is legal

responsibilities (mean = 3.84), followed by ethical responsibilities (mean =3.68), economic responsibilities (mean =3.67) and philanthropic responsibilities (mean = 3.62).

Furthermore, the legal responsibilities of CSR practice mostly associated with compliance to NBE's directives & regulations, rules and regulations of the country, preparing its financial statement according to international reporting standard and also communicating the same to the public.

Similarly, the common CSR practice with respect to the ethical responsibilities in selected private banks comprise; operating in a manner consistent with expectations of societal and ethical norms, having well developed ethical principles, having good corporate governance, motivating its employees through recognition, appreciation & reward, facilitating various capacity building training for its employees and also gives due care for the health, safety & working conditions of its employees.

CSR practice of banks related with economic responsibilities includes, having clearly designed strategies to reduce operating costs, having good risk management policy & strategies, react to customer demand by developing new product, redefining the existing ones and also creating new channels.

The last CSR practice with respect to the philanthropic responsibilities in selected private bank includes supporting national pride and government campaigns, supporting societies by providing support for the art, culture, science & sport, making donation to charitable bodies and communities and also responds to natural and human made disasters.

The second research questions of this study is to assess whether CSR and profitability in selected banks has a significant relationship or not. In this regard, the result of the study exhibits that the practice of CSR is correlated with bank's profitability. The findings show that CSR practice can explain 42% of profitability in selected private banks in Ethiopia.

The four dimensions of CSR such as, philanthropic, ethical, legal and economic responsibilities have a positive and significant relationship with profitability of banks. Philanthropic and legal responsibilities with 4% of significance level, ethical responsibility with 5% of significance level and economic responsibility with 2.2% level of significance.

The finding of the result further revealed that ethical responsibilities of CSR dimension has more impact on profitability with  $B=0.328$  followed by philanthropic responsibility with  $B=0.258$ , legal responsibility with  $B=0.214$  and economic responsibility with  $B=0.124$ .

Though all the four dimensions of CSR are commonly practiced in selected private banks in Ethiopia, the legal responsibilities of CSR dimensions is the most dominant practice in selected private banks in Ethiopia.

There is a strong positive correlation between banks CSR practices and their profitability, 42% of the variation on profitability in selected banks are explained by their CSR practice.

Specifically, all the four dimensions of CSR has a positive relationship with bank's profitability. Ethical responsibilities of the bank has the strongest relationship with bank's profitability with  $r = 0.542$ ,  $p<0.01$ , followed by the economic activities of the banks with  $r = .494^{**}$ ,  $p<0.010$ . The bank's philanthropy activities and legal responsibilities has the same relationship with bank's profitability with  $r = 0.468^{**}$ ,  $p<0.01$ .

Based on the standardized beta coefficients all the four dimensions of CSR activities has a positive impact on profitability of banks. Ethical responsibility with a beta value of 0.282 is the highest predictors of profitability of private banks in Ethiopia. Followed by philanthropic responsibility with a beta value of 0.158, legal responsibility with a beta value of 0.163 and economic responsibility with a beta value of 0.138. Therefore, based on the results of the finding the study concludes that CSR practices have a significant impact on the profitability of banks.

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