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RESEARCH ARTICLE

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Corporate social responsibility engagement and firm performance in Asia Pacific: The role of enterprise risk management

Tahira Naseem[1] | Faisal Shahzad[1] | Ghazanfar Ali Asim[1] | Ijaz Ur Rehman[2] | Faisal Nawaz[1]

[1] Department of Management Sciences, COMSATS University Islamabad, Islamabad, Pakistan

[2] College of Business Administration, Al Falah University, Dubai, United Arab Emirates (UAE)

Correspondence
Faisal Shahzad, Department of Management Sciences, COMSATS University Islamabad, Attock Campus, Islamabad, Pakistan.
Email: faisalnoorshah85@gmail.com

Abstract

We examine a channel through which corporate social responsibly affects firm performance. More specifically, we modeled the mediating role of enterprise risk management between corporate social responsibility and firm performance. We use the weighted average of environmental, social, and governance scores (as a proxy of corporate social responsibility) extracted from DataStream of Thomson Reuters-ASSET4. Drawing on the stakeholder theory and using a large sample of 1021 Asia Pacific firms throughout 2006–2016, we show that corporate social responsibly is positively associated with firm performance. Our results suggest that corporate social responsibly is linked to enterprise risk management. However, the effect of corporate social responsibly on firm performance is both direct and indirect. We provide evidence that enterprise risk management partially mediates the relationship between corporate social responsibility and firm performance. We account for the issue of endogeneity and use alternative measures of firm performance for a robustness check. The findings offer important implications of socially responsible business processes through leveraging on the significance of enterprise risk management.

KEYWORDS

corporate social responsibility, enterprise risk management, firm performance

1 | INTRODUCTION

Does corporate social responsibility (CSR) increase the financial performance? Although some studies serve as confirmatory evidence (Alafi & Hasoneh, 2012; Cegarra-Navarro, Reverte, & Eduardo, 2015; Famiyeh, 2017; Galbreath & Shum, 2012; Shen & Chang, 2008), other studies have yielded negative (Cordeiro & Sarkis, 1997; Crisóstomo, De Souza Freire, & De Vasconcellos, 2011; Manchiraju & Rajgopal, 2017; Vance, 1975; Wright & Ferris, 1997) or neutral results (Dobbs, Van Staden, Dobbs, & Van Staden, 2016; McWilliams & Siegel, 2000; Nollet, Filis, & Mitrokostas, 2016). These findings (Galbreath & Shum, 2012; Wood, 2010) imply that there is no conclusive evidence to support a clear and direct relationship between CSR and financial performance. In general, these inconsistencies in results are owing to variation in conceptual determinants of CSR (Brammer & Millington, 2008) methodologies used, different contexts (for instance, country differences), and the measurements and variables (McWilliam & Siegel, 2000; Ullmann, 1985; Wang, Dou, & Jia, 2016). Nevertheless, there could also be other reasons for these inconsistent empirical results.

The stakeholder theory of the firm posits that to fulfill the demands of various stakeholders, firms must adjust their strategies in any given market. Hence, taking under careful consideration, the priorities of stakeholders is an essential yet necessary step in designing operations that strike a right balance between business growth and social progress. Barnea and Rubin (2010) suggest that firms adopting CSR principles assume that by operating ethically and responsibly for the good of the society at large has a greater chance of success. These firms can potentially provide investors with more reliable and transparent financial

information through constrained earnings management, and it is for this reason that solid reputation and market share can be increased (Jo & Harjoto, 2011). Particularly concerning managing risks, research (Arora & Dharwadkar, 2011) has shown that firms rarely possess similar investment risk profiles, that is, business risks arising from environmental and social issues sustain higher operating costs and increase investors' risks. Hence, risk management is a fundamental concern in the current dynamic global environment, especially when such a risk is associated with CSR.

Ingham and Havard (2017) proposed that strategic decisions taken by a manager of a firm are expected to be consistent with CSR policies. For instance, the literature argues that improvement in CSR policies is strongly linked to the strategic decisions taken in the context of risk management (Cheng, Ioannou, & Serafeim, 2012; Dhaliwal, Radhakrishnan, Tsang, & Yang, 2012; Zhang, Gao, & Morse, 2015). The seminal study of Zhang et al. (2015) implies that CSR performance is most likely associated to the firm's performance via strategic decisions driven by CSR policies to manage risk, and such decisions have either good or bad outcomes. Keeping this argument in context, it can be implied that the reason for inconsistency in findings is due to the lack of enough empirical investigation to further explore the channels via which CSR can positively influence firm's financial performance (Harjoto & Laksmana, 2018).

Our interest is to examine the role of enterprise risk management (ERM) in the relationship between CSR and firm performance using a sample of 12 Asia Pacific Markets. The contribution of the study is summarized as follows: Previous studies have explored the kinds of strategic choices that CSR might influence. For example, Cheng et al. (2012) find evidence to suggest that CSR is linked to risk level, whereas Boatright (2011) and Godfrey, Merrill, and Hansen (2009) documented that firm's engagement in CSR activities serves as a controlling mechanism that ensures safeguarding of interests of all the stakeholders. These empirical studies suggest that active engagement of companies in CSR activities makes them consider the interests of all stakeholders thereby supporting ERM,[1] the process that also takes into account risks associated with all stakeholders. These studies, however, do not test if these types of actions synchronously affect firms' financial performance. We follow the line of inquiry of Cheng et al. (2012), Boatright (2011), and Godfrey et al. (2009). However, we modeled the mediated relationship of ERM to empirically test whether or not the relationship between CSR and financial performance is indirect?

The mediating role of ERM between CSR and firm performance stems from the internal control mechanism within an organization. CSR performance is highly correlated to the policies an organization initiates to increase ERM (Chen et al., 2012; Dhaliwal et al., 2012; Zhang et al., 2015). Our study banks on shareholder theory to investigate the association between ERM, CSR, and financial performance, specifically, on notion that firm secures the trust of investors via achieving high levels of CSR, which in turn positively influence the firm's financial stature via increased capital inflow from investors (Donaldson & Preston, 1995; Freeman, 1984; Harjoto et al., 2015; Hart, 1995). In this context, ERM is viewed as one of such actions by (Harjoto & Laksmana, 2018), influencing the financial performance of a firm due to its high synchronicity with CSR.

The findings of the study may assist management in understanding the implications of CSR policies and adoption of ERM system for firm performance. The active engagement of a firm in CSR activities enables its managers to view risks about all the stakeholders—investing and noninvesting—holistically rather than individually. The Committee of Sponsoring Organizations–ERM (COSO-ERM) Integrated Framework (2004) also suggests that while developing objectives and making strategy, a firm should use resources effectively and efficiently within an acceptable level of risk thereby increasing firm profitability and market returns. Therefore, the ERM process not only reduces risk but also enhances firm performance by the efficient use of CSR that could be beneficial to firms.

On the basis of Baron and Kenny (1986), we employ a technique to gauge the influence CSR has on firm performance. We construct a panel dataset using a sample of 1,021 Asia Pacific companies from 2006 to 2016. We show that CSR engagement of the firm increases financial performance of a firm and that ERM plays an important role of mediation between CSR engagement of the firm and performance. We measure ERM with the proxy of ERM index[2] (ERMI) of (Gordon, Loeb, & Tseng, 2009). According to the COSO, the index is based on four objectives of ERM. This index was developed to measure how efficiently a firm's ERM system works and whether the firm achieves its objectives concerning operations, reporting, strategy, and compliance.

The remainder of the paper is organized in the following way. In Section 2, we discuss the conceptual framework based on the developed hypotheses. Section 3 describes the methodology and builds the econometric model. Afterward, we present our results in Section 4. Finally, we conclude and discuss practical implications.

2 | LITERATURE REVIEW AND HYPOTHESES DEVELOPMENT

2.1 | CSR and firm performance

The agency theory (Jensen & Meckling, 1976) propounds that the managers of a firm act as agents of their principals, namely, the shareholders, and have to act on their behalf taking measures that aim at maximizing their wealth. Thus, in the light of agency theory, the single most important stakeholder group of a firm that should be taken care of by the managers is the shareholders. On the contrary, however, Donaldson and Preston (1995) drawing on the

[1]"ERM provides a framework for corporates to balance downside risks and to exploit the opportunities (upside risks) holistically. Overall, it supports the achievement of organizational objectives by focusing on the interrelatedness of risks" (Agarwall & Ansel, 2016).

[2]ERM index consists of four objectives: (1) Strategy refers to a firm's ability to present itself in front of competitors in the marketplace. (2) Operations refer to a firm's input–output relation in a firm's operations (Banker, Datar, & Kaplan, 1989). If a firm has more output than input, it means it is performing better and has higher operating efficiency. (3) Reporting refers to the concept of reporting reliability, and it represents the involvement of a firm in illegal earning practices. (4) Compliance describes a firm's ability to follow the rules and regulations that results in lowering the firm's risk and improve its performance (OKeefe, King, & Gaver, 1994).

normative aspect (the other two being descriptive/empirical and instrumental) of the stakeholder theory (Freeman, 1984) suggest that a firm has multiple stakeholders—persons or groups having legitimate interests in various aspects of corporate activity—all of whom should be given due consideration while the managers of a firm are intending to take any action. The instrumental aspect of the stakeholder theory aims at examining the links between the stakeholder management practices and the attainment of corporate performance goals. We, therefore, posit that CSR activities affect the whole range of a firm's stakeholder groups, which in turn affect the firm's bottom line outcomes such as profitability.

A number of academicians are of the view that not all individual activities constituting the broad spectrum of CSR always result into enhanced financial performance under all circumstances (Brammer & Millington, 2008). However, broadly speaking, extant empirical findings mostly offer support to the notion that greater involvement in CSR results into improvement of firms' financial performance (Fombrun, Gardberg, & Barnett, 2000; Lin, Yang, & Liou, 2009). It would be apt to conclude that comprehensive involvement in CSR activities entails firms to bear costs; however, the benefits in terms of amelioration in financial performance usually outweigh such costs.

Stakeholder theory provides a foundation for studying the interrelationship of firms and human society (Freeman, 1984). From the standpoint of this theory, being an integral part of the society, firms are to a certain extent responsible for enhancing its well-being (Donaldson & Preston, 1995). Therefore, besides mere shareholders, firms should try catering to the interests of other stakeholders as well. Thus, adopting an all-encompassing approach toward addressing the interests of a whole range of stakeholders is of prime importance.

In consonance with stakeholder theory, striking a balance between the needs and interests of multiple stakeholders on the part of firms is very important because these different stakeholders—investors, shareholders, employees, communities, suppliers, governmental bodies, and the natural environment—provide tangible and intangible resources essential to survival and success of firms (Brower & Mahajan, 2013; Chatterji, 2014, p. 92). The resources are in the form of funds by shareholders and equity investors; revenues, loyalty, and advocacy by customers; skills and effort by employees; raw material, parts, components, and knowledge by suppliers; location and infrastructure by communities; and ecosystem facilities by the natural environment. Stakeholders might fully or partially cease to provide the resources to firms owing to their inability to respond to the varied needs of multiple stakeholders appropriately. This could ultimately threaten the long-term survival and existence of the firms (Ahn & Park, 2018). A firm's survival and success could be ensured only if its managers are able and committed to creating wealth, satisfaction, or value for all of its stakeholders (Clarkson, 1995). CSR encompasses activities that can partially create wealth, value, or satisfaction for multiple stakeholders of the firm. Hence, in line with stakeholder theory, one of the ways a firm can address different needs of its stakeholders and garner their sustained support is by exhibiting its involvement in CSR activities.

In Freeman's (1984) view, a firm can raise its bottom line to a higher level if it acts in a socially responsible manner by adopting a balanced approach to addressing varying needs of all of its stakeholders. Several empirical studies (Jones, 1995; Shahzad, Rehman, Nawaz, & Nawab, 2018) reveal that a firm's response to meeting the stakeholders' needs through active engagement in CSR activities is linked with the better financial performance of the firm. The relationship between CSR and financial performance manifests itself in several ways.

First, healthy relationships are established between a firm and its stakeholders due to the firm's commitment to engagement in CSR activities (Godfrey, 2005). Consequently, these relationships give rise to exchanges that are beyond ordinary transactions and create bilateral value (Schnietz & Epstein, 2005). These exchanges further lead to a better financial performance by creating relational assets and moral capital for all the stakeholders (Wang et al., 2016). The relational assets and moral capital serve as socially intricate and nonmaterial resources, which are inimitable for the competitors. These resources, therefore, provide a firm with a competitive advantage in the form of enhanced financial performance (Barney, 1991; Godfrey et al., 2009).

Second, some specific benefits accrue to the firms' employing engagement in CSR to manage their stakeholders. These benefits include decreased employee turnover and enhanced employee commitment (Santos, 2011), improved customer loyalty, increased customer satisfaction (Saeidi et al., 2015), and improved repute (Chatzoglou, Chatzoudes, Amarantou, & Aggelidis, 2017; Tencati, Perrini, & Pogutz, 2004), which are the specific benefits. Consequently, firms experience improvement in their bottom line outcomes. The improvement in the bottom line leads to a reduction in transaction costs and an increase in financial performance (Manchiraju & Rajgopal, 2017; Sprinkle & Maines, 2010).

Third, firms actively involved in CSR activities mostly maintain operational standards that are over and above those legally required (Carroll, 1979) thereby avoiding costs of meeting stringent regulations (Hart, 1995). Fourth, adoption of socially responsible practices may also help firms avoid the costs and negative consequences of unforeseen accidents (Bansal & Roth, 2000). Ultimately, the financial performance of firms ameliorates, because such reduction in risk enables them to raise funds through debt and equity at a lower cost (Dhaliwal, Li, Tsang, & Yang, 2014; El Ghoul, Guedhami, Kwok, & Mishra, 2011; Goss & Roberts, 2011).

Several academicians are of the view that not all individual activities constituting the broad spectrum of CSR always result in enhanced financial performance under all circumstances (Brammer & Millington, 2008). However, extant empirical findings mostly offer support to the notion that greater involvement in CSR results into improvement of firms' financial performance (Fombrun et al., 2000; Lin et al., 2009). It would be apt to conclude that extensive involvement in CSR activities entails firms to bear costs; however, the benefits in terms of amelioration in financial performance usually outweigh such costs. Therefore, we hypothesize as follows:

H1. *CSR has a positive relationship with financial performance.*

2.2 | CSR, ERM, and firm performance

Prior literature on the impact of CSR on firm performance offers mixed evidence (Cordeiro & Sarkis, 1997; Lin et al., 2009; Manchiraju & Rajgopal, 2017; Reverte et al., 2016; Wu & Shen, 2013). However, no significant attention has been paid toward exploring the channels through which CSR impacts firm performance with a few exceptions including (e.g., Anser, Zhang, & Kanwal, 2018; Harjoto & Laksmana, 2018; Hasan, Kobeissi, Liu, & Wang, 2018). Hasan et al. (2018) suggested that productivity acts as a channel through which CSR activities affect firm performance. On the other hand, Harjoto and Laxmana (2018) revealed that corporate risk-taking mediates the effect of CSR on firm performance.

It would, thus, be appropriate to explore some other channels through which CSR influences firm value/performance. In this study, however, we confine our focus to analyzing the ERM process as a channel that allows CSR to influence firm performance. Stakeholder theory posits that firm managers, while making decisions, must take into consideration the interests of all the stakeholders. Hence, in line with the stakeholder theory, a firm's engagement in CSR activities serves as a controlling mechanism that ensures the safeguarding of interests of all the stakeholders. Some empirical studies suggest that active engagement of companies in CSR activities makes them consider the interests of all stakeholders thereby supporting ERM process that also takes into account risks associated with all the stakeholders (Boatright, 2011; Godfrey et al., 2009). Prior studies have shown that better CSR performance reduces the risk level of a firm (Chen, Hung, & Lee, 2018; Cheng et al., 2012; Dhaliwal et al., 2012; Zhang et al., 2015). In this study, we employ an ERM index comprising four components, namely, strategy, operational efficiency, reporting quality, and compliance, to gauge the effectiveness of the ERM process in firms. Extant literature offers evidence regarding the influence of CSR separately on each of the stated components of ERM index.[3]

Overall, the preceding discussion asserts that CSR enables firms to develop ERM. Past research has also shown that ERM enhances firm performance (Florio & Leoni, 2017; Hoyt & Liebenberg, 2011; Mohammed & Knapkova, 2016). Recently, academicians and practitioners have started paying increasing attention to examining the impact of overall risk on firm performance. In the past, however, the silo-based approach was used to analyze and manage risks. Nevertheless, this approach led to suboptimal outcomes owing to managing one risk at a time while overlooking the interrelatedness of risks (Grace et al., 2015; Hoyt & Liebenberg, 2011; Power, 2009). Therefore, over the last two decades or so, a new trend has emerged for risk management that is adopting holistic approach to manage a firm's risk. This approach is referred to as ERM that manages risks coherently rather than managing them separately as individual risks (Bromiley, McShane, Nair, & Rustambekov, 2015). Therefore, ERM process enables a firm to better understand the collective risk in all business activities, provides better deployment of resources, and increases capital efficiency and return on equity (ROE) by identifying and managing not only the downside risks (the negative ones—threats) but also the upside risks (the positive ones—business opportunities; Callahan & Soileau, 2017).

The above viewpoint was also stated by Gordon et al. (2009) linking ERM with high firm performance. Florio and Leoni (2017) also suggested that increased market and accounting-based performance are linked to better ERM process implemented in a firm. A similar conclusion was also validated by Farrell and Gallagher (2015) linking a greater value of firms with mature ERM process. However, this association is subject to the orientation of ERM for several external factors, that is, external uncertainties, competition, diversification, corporate governance, and size of firms.

On the basis of the above discussion, we develop our second hypothesis as follows:

> **H2.** *Enterprise risk management has a mediating effect on the relationship between corporate social responsibility and firm performance.*

3 | RESEARCH METHODOLOGY

3.1 | Data collection and sample size

We employed a large sample of 1,021 companies in the Asia Pacific region from 2006 to 2016. We choose the constituents of "Asia Pacific" developed by ESG-ASSET4 and managed by Thomson Reuter. We obtained the information on the names and mnemonics of firms included in ESG-ASSET4 that we gathered from the DataStream; fundamentals data for those firms were combed from the DataStream. Therefore, we chose the firms to form each country based on environmental, social, and governance (ESG) coverage in ASSET4. Further, Sobel intermediary factor test method (Baron & Kenny, 1986) is employed to examine the direct and indirect effects of CSR on firm performance. Sample-wise distribution across countries and sectors is provided in Panels A and B of Table 1. Panel A of Table 1 presents the distribution of firms across countries. Approximately 67% of the sample originates from Australia, Hong Kong, Taiwan, and South Korea. Panel B of Table 1 shows the distribution of sample across sectors. The industrial sector represents the most significant proportion compared with other sectors of the sample.

3.2 | Variables

3.2.1 | Dependent variable: Firm performance

We used return of asset (ROA) and ROE to measure the financial performance of the firm in this study. There is a great variety of firm financial performance measures in the extant literature. The review article of Griffin and Mahon (1997) suggests that there are as many as 80 different types of measures of financial performance of the firm.

[3]CSR helps management to devise strategies that give the firm competitive edge over its competitors and enhances its operational efficiency (Bloom, Hoeffler, Keller, & Meza, 2006; Lev, Petrovits, & Radhakrishnan, 2010). Also, CSR reduces earning management and enhances FRQ (Garcia-Sanchez & Garcia-Meca, 2017; Kim, Park, & Weir, 2014). Moreover, CSR enables firms to avoid costly government fines (by improving compliance with regulations; Brown, Helland, & Smith, 2006).

TABLE 1 Sample composition

Panel A. Sample distribution across countries		
Countries	**N**	**%**
Australia	323	31.64
China	74	7.25
Hong Kong	141	13.81
India	80	7.84
Indonesia	32	3.13
Malaysia	43	4.21
New Zealand	37	3.62
Philippines	16	1.57
Singapore	33	3.23
South Korea	98	9.60
Taiwan	115	11.26
Thailand	29	2.84
Total	**1,021**	**100**
Panel B. Sample distribution across sectors		
Industry	**N**	**%**
Consumer services	50	4.90
Industrial	778	76.20
Consumer goods	37	3.62
Oil and gas	20	1.96
Basic materials	37	3.62
Health care	24	2.35
Telecom	15	1.47
Utilities	27	2.64
Technology	33	3.23
Total	**1,021**	**100**

However, the most commonly used measures of financial performance of the firms are ROE, ROA, and return on sales. Large number of studies used ROA and ROE to measure the financial performance of the firm (Berman, Wicks, Kotha, & Jones, 1999; Callahan & Soileau, 2017; McGuire, Sundgren, & Schneeweis, 1988; Saeidi et al., 2015).

3.2.2 | Independent variable: CSR

Holme and Watts (1999) define the CSR as "enduring promise by the company to perform according to rules of ethics that lead to the economic development and make improvements in the standard of living of people and society on a larger basis." According to McWilliams and Siegel (2000), CSR refers to activities that intend to promote public welfare or social goods. The CSR acts as proper measure for stakeholder management because CSR is the result of company decisions to satisfy the interests and needs of too numerous stakeholders (Harjoto et al., 2015; Wang et al., 2016). To measure CSR, we take advantage of comprehensive CSR index by combining the ESG pillars of CSR managed by Thomson Reuters-ASSET4. For each firm in our sample, ASSET4 contours several indicators of ESG. The ASSET4 element of Thomson Reuters gives the information that is used to determine the ratings related to CSR pillars. On the basis of prior literature, we assigned equal weight to each pillar (Attig, Boubakri, El Ghoul, & Guedhami, 2016; Cheng et al., 2012; Samet & Jarboui, 2017).

Within these three pillars, environmental score (61 indicators) includes resource use, emissions, and innovations. The environmental aspects of CSR score measure and reflect the impact created on nonliving and living natural systems by the firm operations that include land, water, air, and entire ecosystem. The score signifies the best management practices of the firm to circumvent the environmental risks and to exploit the environmental opportunities in the competing uses resulting in long-term shareholder value generation and expansion. The social score (63 indicators) includes a firm's commitment toward product responsibility, community, diversity, and opportunity, employment quality, health and safety, and training. The social score mainly focuses on the effectiveness of management practices in terms of creating loyalty and trust among the firm's customers, workforce, and society as a whole that in turn reflect the firm's reputation and strength, which are vital to forming its capacity to accumulate long-term value for its shareholder. The corporate governance pillar (54 indicators) includes management commitment and effectiveness toward board functions, board structure, compensation policy, vision and strategy, and shareholder rights. The governance aspects of CSR assess a firm's system and process to determine the extent to which the firm's board executives and members act with regard to best interests of the firm's long-term shareholders. In particular, the governance score reflects a firm's capability of how better firms manage, control, and steer the shareholder rights and responsibilities through incentive creation and check and balance to promote long-term shareholder value.

3.2.3 | Mediator: ERM

To measure a firm's ERM, we used the ERMI index of Gordon et al. (2009). According to the COSO, the index is based on four objectives of ERM. This index is developed to measure how efficiently a firm's ERM system works and whether or not a firm achieves its objectives relative to strategy, operations, reporting, and compliance.

$$\text{ERMI} = \sum_{k=1}^{2} \text{Strategy}K + \sum_{K=1}^{2} \text{Operation}K + \sum_{K=1}^{2} \text{Reporting}K + \sum_{K=1}^{2} \text{Compliance}K.$$

Strategy

It refers to a firm's ability to present itself in front of competitors in the marketplace. When a firm implements its strategy, the purpose is to gain an edge over its competitors in the same industry (Porter, 2008). This would lower a firm's total risk and thus enhance its performance. All firms in the same industry compete to grab more sales opportunities. Thus, an increase in sales of a firm *i* relative to the industry's average sales means firm *i* is performing better than its average competitors. By using the following formula, the success of a firm's strategy can be measured.

$$\text{Strategy}_1 = \frac{\text{Sales}i - \mu_{\text{sales}}}{\sigma_{\text{sales}}},$$

where Sales_i indicates Sales of firm i from 2006–2016, μ_{sales} represents average industry sales from 2006–2016, and σ_{sales} represents the standard deviation of sales of all firms in the same industry during the aforementioned period.

Operations

It refers to a firm's input–output relation in a firm's operations (Banker et al., 1989). If a firm has more output than input, it means it is performing better and has higher operating efficiency. Thus, the higher the operating efficiency, the lower a firm's overall risk of failure. Resultantly, it leads to an increase in firm value. Operational efficiency can be measured by dividing sales by total assets.

$$\text{Operation}_1 = \frac{\text{Sales}}{\text{Total Assets}}.$$

Another method of measuring a firm's operational efficiency is by dividing sales by the number of employees.

$$\text{Operation}_2 = \frac{\text{Sales}}{\text{Number of Employees}}.$$

Reporting

The method of measuring poor financial reporting quality is by taking the absolute value of normal accruals divided by the sum of the absolute value of normal and abnormal accruals (Johnson, Khurana, & Reynolds, 2002). Jones (1991) accruals estimation model is used to measure abnormal accruals. Normal accruals are calculated as a change in revenue and the level of property, plant, and equipment. Total assets at the start of the year will be used as the deflator in this model. The abnormal accruals will be calculated as follows:

$$\frac{TA_{it}}{A_{it-1}} = \alpha it\left[1/_{A_{it-1}}\right] + \beta 1it\left[\Delta REVit/_{A_{it-1}}\right] + \beta 2it\left[PPE_{it}/_{A_{it-1}}\right] + eit, \quad (1)$$

where TA_{it} represents the total accrual of firm i at time t; A_{it-1} shows the total assets of firm i at time $t-1$; $\Delta REVit$ shows the change in sales revenue of firm i at time $t-1$ to t; PPE_{it} indicates the property, plant, and equipment of firm i at time t; and e_{it} is the error term.

Total accruals are computed by a difference between operating cash flows and income before extraordinary items. The variable Abnormal Accruals is the error term from the regression model shown in Equation (1). The variable Normal Accruals is defined as Total Accruals minus Abnormal Accruals. Reporting is measured as follows:

$$\text{Reporting} = \frac{|\text{NormalAccruals}|}{|\text{NormalAccruals}| + |\text{AbnormalAccruals}|}.$$

Compliance

It describes a firm's ability to follow the rules and regulations that results in lowering the firm's risk and improve its performance. To measure compliance, we take the proportion of auditor's fees to net sales revenue.

$$\text{Compliance} = \frac{\text{Auditor Fees}}{\text{Net Sales}}.$$

3.2.4 | Control variables

Following the previous literature, control variables included in this study are firm size (FS), financial leverage (FL), board independence (BI), board size (BS), and sales growth (SG; Florio & Leoni, 2017; Harjoto & Laksmana, 2018; Mohammed & Knapkova, 2016; Reverte et al., 2016). Table 2 appended below describes dependent, independent, and control variables in detail.

3.3 | Econometric model

To test the pathway through which CSR expectedly affects FP, Baron and Kenny's (1986) method is used to analyze the intermediary effect. Taking the ERM as a mediator, we design the following models:

$$\begin{aligned}\text{FP}_{i,t} = {} & \alpha_0 + \alpha_1\text{CSR}_{i,t} + \alpha_2\text{FS}_{i,t} + \alpha_3\text{FL}_{i,t} + \alpha_4\text{BI}_{i,t} \\ & + \alpha_5\text{BS}_{i,t} + \alpha_6\text{SG}_{i,t} + \varepsilon_{i,t},\end{aligned} \quad (2)$$

$$\begin{aligned}\text{ERM}_{i,t} = {} & \beta_0 + \beta_1\text{CSR}_{i,t} + \beta_2\text{FS}_{i,t} + \beta_3\text{FL}_{i,t} + \beta_4\text{BI}_{i,t} \\ & + \beta_5\text{BS}_{i,t} + \beta_6\text{SG}_{i,t} + \mu_{i,t},\end{aligned} \quad (3)$$

$$\begin{aligned}\text{FP}_{i,t} = {} & \gamma_0 + \gamma_1\text{CSR}_{i,t} + \gamma_2\text{ERM}_{i,t} + \gamma_3\text{FS}_{i,t} + \gamma_4\ \text{FL}_{i,t} \\ & + \gamma_5\ \text{BI}_{i,t} + \gamma_6\text{BS}_{i,t} + \gamma_7\text{SG}_{i,t} + \sigma_{i,t},\end{aligned} \quad (4)$$

where α_1 in Equation (2) is the total effect of CSR on FP, β_1 in Equation (3) is the effect of CSR on ERM, and γ_1 in Equation (4) is the effect of intermediate variable ERM on FP. The mediation effect of ERM is an indirect effect that is the product of β_1 and γ_2. The relationship between them is the total effect = direct effect + mediator effect, that is, $\alpha_1 = \gamma_1 + \beta_1\ \gamma_2$.

4 | RESULTS AND DISCUSSION

Panel A of Table 3 explains the descriptive statistics of the main variables in the form of mean, minimum, maximum, and standard deviation. The mean value of CSR is 42.325, and the standard deviation is 28.528. ERMI shows the mean value of 4.568 and standard deviation of 1.109. Firm performance shows a mean value of 0.827 and standard deviation of 0.065. The mean of the firm size is 16.762 with a standard deviation of 3.581. Financial leverage shows the mean value of 0.963, which means that long-term debt financing is more than 96% of the company's assets.

Panel B of Table 3 shows the average value of each variable concerning firms of the Asia Pacific countries represented in our sample. The country factor plays a vital role in identifying the country contributing the most to CSR activities. In Panel B, we see that South Korea and

TABLE 2 Description of variables

Variable	Label	Nature of variable	Description
Independent variable			
Corporate social responsibility	CSR	Numerical	CSR = Average of environmental, social, and governance scores
Dependent variable			
Firm performance	FP	Numerical	ROA is a proxy of firm performance which is measured as a ratio of net profit after tax to total assets
		Numerical	ROE is a proxy of firm performance which is measured as a ratio of net profit after tax to capital
Mediating variable			
Enterprise risk management	ERM	Numerical	ERM index (strategy, operations, reporting, and compliance)
Control variables			
Firm size	FS	Numerical	Natural logarithm of total assets
Financial leverage	FL	Numerical	Long-term debt over total equity
Board independence	BI	Numerical	Percentage of the independent BoD members
Board size	BS	Numerical	Number of BoD members
Sales growth	SG	Numerical	$Sales_t - Sales_{t-1}/Sales_{t-1}$

India show the highest average value of CSR performance with the values of 60.345 and 59.510, respectively. These values show that South Korea and India are paying more attention toward CSR activities, and the average value of firm performance of these two countries shows that contributing more to CSR activities leads to enhancement of a firm's average performance.

The results reported in Table 4 indicate the mediating role of ERM in the relationship between CSR and firm performance. By following Baron and Kenny's (1986) method, three conditions should be fulfilled to prove the presence of mediation process: (a) in first regression, that is, Equation (2), the coefficient of the independent variable (CSR) must be statistically significant representing significant influence of CSR on FP; the dependent variable (b) in second regression, that is, Equation (3), again the coefficient of independent variable (CSR) must be statistically significant showing significant influence on the mediator (ERM); and (c) in the third regression, that is, Equation (4), the coefficient of the mediator (ERM) must be statistically significant showing significant influence on the dependent variable (FP), whereas the independent variable has less effect on the dependent variable in the third regression than in the first regression.

In column 1 of Table 4, the coefficient of CSR is positive and significant (α_1 = .01, p > 1%) as predicted. The result shows that higher CSR performance increases firm performance. These results support Hypothesis 1 and are in line with the previous studies (Galbreath & Shum, 2012; Hull & Rothenberg, 2008; Lin et al., 2009; Reverte et al., 2016). Traditional stakeholder theory posits that broadening the participation of multiple stakeholders enables the management to fulfill the following objectives: (1) Enhance the perceived legitimacy of social image of a firm; (2) enhance the active participation of the board of directors in firm's affairs; and (3) set higher performance standards for the top management.

Furthermore, column 2 indicates that the coefficient of CSR is positive and significant ($ß_1$ = .003, p>1%) and shows that CSR has a positive and significant effect on ERM. Column 3 indicates that the coefficients of CSR and ERM are positive and significant (γ_1 = .001* and γ_2 = .009***, respectively). It means that ERM partially mediates the relationship between CSR and firm performance. Overall, these results support Hypothesis 2. Furthermore, Sobel Z value is 0.003 and significant at 1% level, showing that there is a partial mediation effect of ERM. Hence, in line with the stakeholder theory, a firm's engagement in CSR activities serves as a controlling mechanism that ensures the safeguarding of interests of all the stakeholders. Some empirical studies suggest that active engagement of companies in CSR activities makes them consider the interests of all stakeholders thereby supporting ERM process that also takes into account risks associated with all the stakeholders (Boatright, 2011; Godfrey et al., 2009). Therefore, ERM process enables a firm to better understand the collective risk in all business activities, provides better deployment of resources, and increases capital efficiency and ROE by identifying and managing not only the downside risks (the negative ones—threats) but also the upside risks (the positive ones—business opportunities; Callahan & Soileau, 2017).

CSR has become standard practice for contemporary business that represents moral obligations to both stakeholders and external audience. CSR entails critical firm activities that deal with sustainability at large, beyond the firm's legal obligations. These activities are intended toward accumulating goodwill (Arendt & Brettel, 2010), heightening reputation (Brammer & Millington, 2006), increasing employee commitment (Brammer, Millington, & Rayton, 2007), and enhancing financial performance (Porter & Miles, 2013). Regardless of these holistic benefits, the possibility of what CSR entails is relative in nature, that is, how it is defined and the way it is

TABLE 3 Descriptive statistics

Panel A. Summary statistics of the sample				
Variables	**Mean**	**Std. Dev.**	**Min**	**Max**
CSR	42.325	28.528	6.255	96.33
ERM	4.568	1.109	.666	15.432
FP	.827	.065	.201	1.314
FS	16.762	3.581	4.983	25.910
FL	.963	.082	.195	2.719
BI	3.598	.702	2.639	4.488
BS	2.132	.369	0	4.331
SG	−1.832	1.456	−8.364	17.268

Panel B. Average value of variables across countries								
Variables	**CSR**	**ERM**	**FP**	**FS**	**FL**	**BI**	**BS**	**SG**
Australia	34.863	4.712	0.793	13.170	.924	4.488	1.874	−1.494
China	33.205	4.459	0.816	17.799	.995	2.995	2.378	−1.790
Hong Kong	35.834	4.362	0.829	16.944	.972	3.218	2.342	1.609
India	59.510	4.588	0.857	18.745	.987	3.871	2.377	−1.675
Indonesia	51.599	4.630	0.892	23.234	.985	2.639	1.900	−1.995
Malaysia	45.020	4.500	0.827	16.152	.967	3.258	2.182	−2.160
New Zealand	37.583	4.052	0.792	14.173	.961	4.369	1.959	−2.248
Philippines	42.227	4.595	0.847	18.688	.981	3.465	2.296	−2.003
Singapore	42.262	4.437	0.820	16.091	.988	2.995	2.255	−2.558
South Korea	60.345	5.031	0.855	22.512	.990	2.890	2.144	−2.168
Taiwan	46.673	4.932	0.839	18.016	.976	2.833	2.129	−2.288
Thailand	56.392	4.648	0.849	18.235	.984	2.994	2.593	−2.074

Abbreviations: BI, board independence; BS, board size; CSR, corporate social responsibility; ERM, enterprise risk management; FL, financial leverage; FP, firm performance; FS, firm size; SG, sales growth.

TABLE 4 CSR and firm performance: Alternative measure of CSR

	ROA column (1)	**ERM column (2)**	**ROA column (3)**
CSR	.001*** (2.10)	.003*** (3.07)	.001* (1.67)
ERM			.009*** (6.67)
FS	−.004*** (−3.70)	.305*** (16.86)	−.006 (−5.99)
FL	−.199*** (−7.20)	3.517*** (7.60)	−.233*** (−8.38)
BI	−.017*** (−0.50)	.081* (0.14)	−.018*** (−0.53)
BS	.016* (3.22)	−.066* (−0.79)	.016* (3.39)
SG	.003*** (3.66)	.002 (0.12)	.003**** (3.69)
Year	Yes	Yes	Yes
Industry	Yes	Yes	Yes
N	1,731	1,731	1,731
Adj-R^2	0.1977	0.337	0.217
F	13.92	27.67	15.16
Sobel *Z* (*p* value)			0.003***

Note. *t* values are presented in parentheses. Abbreviations: BI, board independence; BS, board size; CSR, corporate social responsibility; ERM, enterprise risk management; FL, financial leverage; FS, firm size; ROA, return of asset; SG, sales growth.

*Statistical significance at the 10% level. **Statistical significance at the 5% level. ***Statistical significance at the 1% level.

TABLE 5 CSR and firm performance: Alternative measure of firm performance (ROE)

	ROE column (1)	ERM column (2)	ROE column (3)
CSR	0.014** (2.43)	0.391* (4.27)	0.010*** (1.74)
ERM			0.010*** (6.83)
FS	−0.005*** (−5.27)	0.305* (17.08)	−0.009*** (−7.54)
FL	0.074** (2.56)	3.447*** (7.50)	0.038*** (1.33)
BI	−.014*** (−0.39)	0.140* (0.24)	−0.016*** (−0.44)
BS	0.12* (2.45)	−0.063*** (−0.76)	0.013*** (2.60)
SG	0.004*** (4.05)	0.003*** (0.20)	0.004*** (4.07)
Year	Yes	Yes	Yes
Industry	Yes	Yes	Yes
N	1,750	1,750	1,750
Adj-R^2	0.161	0.345	.220
F	11.21	28.99	15.56
Sobel *Z* (*p* value)			.004 (3.621)

Note. *t* values are presented in parentheses. Abbreviations: BI, board independence; BS, board size; CSR, corporate social responsibility; ERM, enterprise risk management; FL, financial leverage; FS, firm size; ROE, return on equity; SG, sales growth.

*Statistical significance at the 10% level. **Statistical significance at the 5% level. ***Statistical significance at the 1% level.

TABLE 6 CSR and firm performance: Addressing endogeneity

	CSR column (1)	ROA column (2)
CSR		.0001* (2.85)
CSR_IND	.838*** (21.00)	
FS	4.947** (22.18)	−.0007*** (−1.22)
FL	−1.315* (−0.24)	−.179*** (−9.76)
BI	20.166*** (13.76)	−.046** (−11.05)
BS	7.857*** (7.18)	.004*** (1.14)
SG	−1.923* (−8.23)	.002*** (3.92)
Year	Yes	Yes
Industry	Yes	Yes
N	4,180	3,799
Adj-R^2	0.3478	0.2285
F	68.52	35.08

Note. *t* values are presented in parentheses. Abbreviations: BI, board independence; BS, board size; CSR, corporate social responsibility; CSR_IND, industry–year average of CSR; FL, financial leverage; FS, firm size; ROA, return of asset; SG, sales growth.

*Statistical significance at the 10% level. **Statistical significance at the 5% level. ***Statistical significance at the 1% level.

endorsed differ significantly across different firms, which primarily depends upon their philosophies, preferences, and personal values (Voegtlin & Greenwood, 2016). At this juncture, one must differentiate between better management and management following the practices more in line with socially responsible philosophy, that is, the former can be myopic concerning increasing the shareholders' wealth in short run. Thus, socially responsible corporate practices may often align with organizational values that may not be considered positive and could negatively affect firm performance in short run but can result in long-run goodwill accumulation that results in increased firm performance (Brammer & Millington, 2006).

4.1 | Robustness check

4.1.1 | Alternative measure of firm performance

In Table 5, we report results by employing an alternative measure of firm performance that is ROE. The results are similar to those reported

TABLE 7 Influence of CSR on firm performance

	ROA column (1)	ERM column (2)	ROA column (3)
PCSRhat	0.001*** (1.82)	0.002** (2.68)	0.001 (1.67)
ERM			.009*** (6.70)
FS	−0.003* (−3.23)	0.323*** (19.00)	−0.006* (−5.78)
FL	−.199* (−7.19)	3.525** (7.61)	−0.233*** (−8.38)
BI	−.014*** (−0.42)	0.148*** (0.25)	−0.016*** (−0.47)
BS	0.17*** (3.46)	−.038** (−0.46)	0.017* (3.58)
SG	.003*** (3.44)	0.004*** (−0.25)	0.003*** (3.52)
Year	Yes	Yes	Yes
Industry	Yes	Yes	Yes
N	1,731	1,731	1,731
Adj-R^2	.1972	.3363	.2174
F	13.88	27.57	15.14
Sobel *Z* (*p* value)			.0003 (2.492)

Note. *t* values are presented in parentheses. Abbreviations: BI, board independence; BS, board size; CSR, corporate social responsibility; ERM, enterprise risk management; FL, financial leverage; FS, firm size; ROA, return of asset; SG, sales growth; PCSRhat, predicted value of CSR.

*Statistical significance at the 10% level. **Statistical significance at the 5% level. ***Statistical significance at the 1% level.

in Table 4 in which we measure firm performance through ROA. The results in column 3 of Table 5 reveal that ERM mediates the relationship between CSR and firm performance.

4.1.2 | Endogeneity issue

We address the problem of endogeneity by using an instrumental variable technique in which an instrument is used to extract the exogenous component of CSR. Following previous studies, we use the industry–year average of CSR (CSR_IND) as an instrumental variable (Benlemlih & Bitar, 2016; Samet & Jarboui, 2017). In the first stage, we regress CSR on the instrument and all control variables. Column 1 of Table 6 reports the results of first stage regression. Next, in the second stage, we regress the firm performance (ROA) on the predicted value of CSR and all control variables. The results of column 1 of Table 6 indicate that the coefficient of CSR_IND is positive and significant. Column 2 of Table 6 reports the results of second-stage regression and reports that the influence of CSR on firm performance is still positive and significant even after capturing the issue of endogeneity.

While considering the issue of endogeneity, we reestimate Equations (2), (3), and (4) while considering the predicted value of CSR (which is derived earlier from first-stage regression) instead of CSR. The results of Table 7 also confirm the existence of partial mediation of ERM even after considering the issue of endogeneity.

5 | CONCLUSION AND IMPLICATIONS

Does a firm's engagement in CSR activities influence firm performance, and if so, how? These are the two main questions that we address in this study. To answer these questions, a sample of 1,021 companies of the Asia Pacific region for the period of 2006–2016 has been drawn. By using Baron and Kenny (1986) method, first, we examine the effect of CSR on firm performance, and afterward, we investigate the mechanism through which CSR influences firm performance.

Our results show that CSR enhances firm performance. This suggests that the involvement of a firm in socially responsible activities enables its management to enhance the perceived legitimacy of the social image of a firm and set higher performance standards for the top management. The central premise of this study is that CSR directly influences firm performance but also influences firm performance via the channel of ERM. First, CSR performance enhances ERM. Hence, in line with the stakeholder theory, a firm's engagement in CSR activities serves as a controlling mechanism that ensures the safeguarding of interests of all the stakeholders. Some empirical studies suggest that active engagement of companies in CSR activities makes them consider the interests of all stakeholders thereby supporting ERM process that also takes into account risks associated with all the stakeholders (Boatright, 2011; Godfrey et al., 2009). Later, this ERM enhances firm performance. Moreover, ERM process enables a firm to better understand the collective risk in all business activities, provides better deployment of resources, and increases capital efficiency and return on equity by identifying and managing not only the downside risks (the negative ones—threats) but also the upside risks (the positive ones—business opportunities; Callahan & Soileau, 2017).

The findings of this study have important implications. One guiding principle for corporate managers lies in the positive association between CSR and firm performance entailing efficient and effective implementation of CSR strategies to gain a competitive edge. Moreover, it should also increase R&D expenditure for the introduction of environment-friendly technology and innovative products to meet society's demand for products that are environment friendly and meet health and safety standards. Further, the adoption of CSR also sends a signal to multiple stakeholders that socially responsible firms manage

all types of risk and enhance ERM system to get higher firm performance. This study also provides help to investors in making sound investment decisions because investors are most likely inclined to invest in projects with high returns per unit of risk. Hence, this study advises investors to invest in companies that actively engage in CSR activities and have in place an effective ERM system because both contribute positively to firm performance. Our study contributes to the literature examining the mechanism through which CSR influences firm performance.

Our findings noted the importance of CSR adoption and implementation of ERM system for companies to integrate the social and environmentally responsible behavior in day-to-day business activities in order to enhance firm performance. Moreover, the active engagement of a firm in CSR activities enables its managers to view risks about all the stakeholders—investing and noninvesting—holistically rather than individually. The COSO-ERM Integrated Framework (2004) also suggests that while developing objectives and making strategy, a firm should use resources effectively and efficiently within an acceptable level of risk thereby increasing firm profitability and market returns. Therefore, the ERM process not only reduces risk but also enhances firm performance by the efficient use of resources and opportunities. The results presented here offer insights into how CSR might add value. Our study, therefore, offers practical thoughts on why CSR could be beneficial to firms. The study has a few limitations. First, the study sample was limited to the Asia Pacific; future studies shall increase the sample size to other geographical areas. Second, the present study forms an index of CSR, using ESG score. Future studies may assess the impact of each of these dimensions impact on FP.

ORCID

Faisal Shahzad https://orcid.org/0000-0001-7381-1208

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