

CHAPTER ONE: INTRODUCTION

1.1. Background of the Study

The competitive environment within the business landscape has been rapidly increasing due to the increasing globalization and also due to the fact that it has become easier and convenient for the competitors to reproduce the innovations developed by the firms. Accomplishing and sustaining competitive advantage for a longer period of time has become a tough challenge for the performance of business enterprises (Kumar et al., 2011). Similarly attracting consumers has also become a challenging task whereas corporate social responsibility (CSR) has become a way forward with which firms can impact the customers incidentally (Lee, Oh & Kim, 2013). Moreover, quality, price and the other vital factors that consumers contemplate before buying from the brand, CSR performance of the company has also been regarded as a substantial factor that, individuals commence making a purchase decision (Desai & Waller, 2010). A supple resourcefulness by a firm which is focused towards the important stakeholders chiefly the consumers and the investors are referred to as CSR (Mpekansambo, 2013). The CSR undertakings carried out by the firms have a constructive and a substantial impact on the society particularly in the case of international organisations who have the prerequisite resources to bring transformation in the society with the benefit of their social welfare work.

Due to the positive image of the brand that is conveyed due to their social activities, the consumers tend to attract to the firms that actively participate in such activities. According to Manzini & Vezzoli (2003) customer make purchases of the products and services from brands that have emphasized the issue related to sustainable, social and economic development or have operated for the sector that needed assistance. There are various ways through which firms can contribute in CSR activities. Some of the commonly used ways of fulfilling their social obligations by the firm are participation in environmental efforts considering how critical it has become to take care of the environment (Scherer & Palazzo, 2011), participating in philanthropy activities like donating money for a cause and local community programs is another way through which firms can strengthen their CSR performance (Carroll & Shabana, 2010). CSR has recently

has also evolved in Pakistan and the local Pakistani firms are now actively participating in CSR activities.

On the other hand, CSR has played a significant role in evaluating the future worth of the firms in terms of their competence, effectiveness, and even subsistence (Saguy, 2016); hence those companies that have implemented CSR activities are more appealing and attractive for the investors and stakeholders. More prominently, the evidence in reference to the responsible behaviour of the firms is approved by their financial information; hence offering more value for the firms in a broader standpoint (García-de-Madariaga & Rodríguez-de-Rivera-Cremades, 2010). This proposes that the actions undertaken by businesses can produce a positive reaction from the investors, as firms that have undertaken CSR actions have the greater probability of showing higher returns subsequent to the socially responsible activities (Cheng, Ioannou & Serafeim, 2014). However, some studies have related socially responsible actions with that of distress risk, while representing a negative association between the two concepts.

According to the study conducted by Bénabou & Tirole (2010), companies have frequently incorporated CSR activities, chiefly as a risk management strategy, as these activities can help firms in augmenting their reputation, which eventually protects these firms from social, regulatory, and political sanctions. This suggests that lack of CSR orientation will finally result in negative sanctions, and this would result in the loss of brand image and reputation while increasing the media and political pressure on the companies in terms of possible consequences and penalties (Jo & Harjoto, 2011). However, CSR activities and positive commitment in them results in the cohort of several benefits ranging from financial to social, and these benefits ultimately permit the businesses to compensate the costs related with it.

The study conducted by Saeidi et al. (2015) suggested that the life cycle of the company has played a role of mediator in reference to CSR and financial distress. In particular, it is obvious from the cases of companies that their access to resources is more likely to progress with the passage of time across the life cycle stages, which leads to the estimation that there exists a relationship between CSR and financial distress across the life cycle stages (Torugsa, O'Donohue & Hecker, 2012). The fundamental purpose for it can be argued to be the relationship between the CSR activities and financial distress, and the vigorous nature in reference to the economic rudiments and their variations; for instance, the cash flows, asset turnover, solvency-related risks and even retained earnings, and even the opportunities that

would be obtainable to the companies during their life cycle (Ducassy, 2013). This has even been established that the negative relationship between the financial distress and the positive CSR activities is magnified due to the progression of firms in their life cycle. Therefore, the main of this study has been to identify whether corporate social responsibility and financial distress are inter related or not as well as the effect of life cycle on the relationship between corporate social responsibility and financial distress.

1.2. Corporate Social Responsibility Practices in Pakistan

In Pakistan, the role of corporate sector is much prominent and remains indebted to various economic considerations (Iqbal et al, 2012). CSR has been one of the most negated issues in Pakistan with a total lack of understanding of the concept. Initial data indicated that only a handful companies are actively pursuing the CSR approach whereas the majority either doesn't know of this concept or isn't aware of its benefits in the long run for the society and country (Sharif & Rashid, 2014). Numerous companies in Pakistan have also been engaged in incorporating CSR initiatives. For instance, Pakistan State Oil has been focused on the main areas such as healthcare, community development, disaster relief and environment (Arifeen, 2017). On the other hand, MCB Bank has also incorporated CSR for ensuring that the interest of its stakeholders has been safeguarded by the notion of principles and codes of good governance (Arifeen, 2017). There was in fact a study conducted using the data to show CSR activity in Pakistan for RBI (Responsible Business Initiative) that presented the indifference of the business sector.

A popular institute in Pakistan namely Pakistan Centre of Philanthropy is responsible for promoting the concept of corporate giving in the country. It watches and monitors the philanthropic practices carried out across the country that can make a positive impact upon people's daily life (Kiran, Kakakhel & Shaheen, 2015). For instance, it has been identified that Pakistan's social welfare and humanitarian services have been looking forward to achieving public support and for this the organisation has partnered with Coca-Cola Pakistan for Ramazan fundraising. (Arifeen, 2017) However, there is a visible deviation of interests between the corporate sector of Pakistan and its society (Malik & Nadeem, 2014). Social sector on the other hand has been the most neglected sector with least investment in it. Because of the changing times and the rise of the CSR approach in various developed nations, many rating agencies in

Pakistan have started rating and considering many industries of the corporate sector to measure their corporate social performance (Visser & Tolhurst, 2017). Hence, considering this, the current research has undertaken a case study of Pakistan to identify if corporate social responsibility and financial distress are interrelated or not as well as the effect of life cycle on the relationship between corporate social responsibility and financial distress.

1.3. Problem Statement

The era of globalization has urged the developed leaders to adapt to the growing approach of corporate social responsibility and its positive impact on the firm's performance that also helps to curtail the effect of financial distress to the firm (Wood, 2010). But the subject of CSR is not that developed in countries like Pakistan (Raza & Majid, 2016). Given the social and economic indicators of Pakistan that lag far behind in the ranking still the approach of CSR is yet to be accepted in Pakistani industrial and other sectors. The approach that is prevalent in Pakistani firms is that they consider investing in CSR a cut in their companies' profit without understanding the basic fact that a positive CSR approach can reduce the financial distress in the mature life cycle stage of the firm (Sharif & Rashid, 2014). There is a far knowledge gap in not applying this approach to Pakistani firms of the private sector. There are few studies conducted to explore the effects of positive CSR on reducing financial distress in which some of the studies has indicated that positive CSR reduces financial distress whereas other studies has indicated insignificant effect. Therefore, the study seeks to analyse the effects of positive CSR on reducing financial distress among the companies of Pakistan.

As described above, the corporate sectors within Pakistan are not very much inclined towards CSR. Reason behind less or no investment in CSR activities is due to lesser awareness and knowledge regarding benefits of CSR. Although CSR activities require huge investments from firms but they result is long term which can help the organisation to recover the amount. Another reason behind resistance from CSR activities is because they are time consuming and requires a lot of effort (Lindgreen, & Swaen, 2010). In addition, there are only few corporations in Pakistan that are investing in CSR while many of the corporations are avoiding investing in the CSR activities. Therefore, the study seeks to provide the effect of CSR for reducing the financial distress for the corporation in Pakistan.

However, it is essential for firms in Pakistan to invest in CSR activities because such kind of actions will enable organisations to create brand awareness, good relationship with stakeholders as well as stock holders and good relationship with societies of the customers. CSR involves investment of money and time because of which firms resist to do CSR activities. Due to this concept, many firms within Pakistan do not focus to invest in CSR activities. This has been estimated that firms think that they have to reduce their profit margin in order to invest in CSR activities.

1.4. Objectives of the Study

The main aim of the study is to analyse corporate social responsibility performance, financial distress and firm life cycle with the evidence from Pakistan. With respect to this, the objectives of this research have been formulated as under:

- To identify whether corporate social responsibility and financial distress are inter related or not.
- Effect of life cycle on the relationship between corporate social responsibility and financial distress.

1.5. Research Questions

This empirical study attempts to answer the following research questions.

1. Are corporate social responsibility and financial distress associated with each other?
2. Does the association between CSR and financial distress get affected in the firm's life cycle stage?

1.6. Rationale and Significance of the Research

This study has contributed to the literature in several important ways. First, it has provided unique empirical evidence that assessed the relationship between CSR performance and financial distress. The findings of the research have supported the view that CSR activities preserve corporate financial performance. This study then linked CSR performance with firm life cycle stages and provides evidence that the interaction between both positive CSR performance

and life cycle progression has been empirically associated with financial distress. This study extended the literature by examining the association between CSR performance and financial distress generally and by arguing that CSR activities constitute a set of risk management mechanisms and strategies that impact a whole range of stakeholders. Moreover, this study will enable the researcher to identify the issues and problems such as financial distress which are faced by the firms running within Pakistan. In addition to that, this study will also look into the impact of financial distress faced by the firms on the processes and procedures of the company.

1.7. Structure of the Study

The structure of the study has been divided into five sections. Chapter one has provided a detailed introduction that has incorporated a contextual background of the study. It has also included the foundation of the study as well as its rationale and significance. The chapter has also outlined the aims and objectives of the study as well as appropriate research questions. Chapter two has provided a review of important previously conducted studies in the form of literature review linked with whether corporate social responsibility and financial distress are inter related or not as well as the effect of life cycle on the relationship between corporate social responsibility and financial distress. This has comprised of the appraisal and valuation of the primary literature incorporated in the study in order to identify the main theoretical underpinnings related to the research area.

Chapter three has provided a research methodology a study has adopted. This has also included a description of research philosophy, research design, research approach, data collection resources, methodological issues and techniques of inspecting and analysing data. Chapter four has summarized data analysis and results of the study. Through these results the objectives and aims of the study have been attained. It has also encompassed a relevant argument of the objectives with the help of verification of previous literature. The last section of the study has incorporated a complete summary of results which have led towards the suitable recommendations and likelihood for impending research. The comprehensive conclusion of the research has also been given in this section.