

# To Investigate the Relationship between CSR of Companies and Their Market Valuation (Equity Valuation): Northern India

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**Abstract – Corporate Social Responsibility (CSR) has been widely studied in the past with little success on direct impact on firm's valuation. The following research investigates the relationship between CSR of companies and their market value a case study of 20 large size companies in Northern India that are listed in National Securities Exchange (NSE). The research uses secondary data for primary analysis and applies MS Excel to analyze data. The data was collected from annual company reports and NSE website for the past 5 years. The research used CSR spending and market cap to investigate the relationship in CSR of companies and market value. The research found that CSR spending and stock valuation is positively related. The concluded that firm valuation can be increased by increasing CSR activities. The research recommends that all companies should adopt a CSR in order to increase the company market value.**

**Keywords: Corporate Social Responsibility (CSR), Stakeholders, Firm Valuation, Market Value**

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## 1.1 INTRODUCTION

### 1.1.1 Corporate Social Responsibilities

Corporate Social Responsibility (CSR) activities have increased in the last decade as a result of social change and government intervention. Corporate social responsibilities refers to organization approach that is self-regulatory and that contributes to all stakeholders sustainable development (Garriga & Melé, 2013). Corporate social responsibility is also known as corporate conscience, corporate citizenship, or responsible business. Organization stakeholders' are people who have interests in the organization and whose organization's operations affect them directly or indirectly (O'Connor & Meister, 2008). Businesses nowadays, are integrating environmental and social concerns in their interactions and operations to enhance equity to stakeholders while pursuing organizational goals. Organizations are also actively engaging on social responsibilities activities to take part in solving community problems. Corporate social responsibility is today a standard business practice and organizations have to take a social stand to enhance their overall reputation.

### 1.1.2 CSR and Firm Performance

Corporate social responsibility practices have both short term and long term benefits to firm performance.

The business stakeholders feel attracted and committed and support firms that are socially responsible. Firms performance depend on the firm's relationship with all stakeholders to enables normal operations enhancing profit making (Perera Aldama, Awad Amar, & Winicki Trostianki, 2009). CSR shapes how outsiders perceive the business that can impact brand recognition and business reputation. CSR can also increase sales and customer loyalty that better the firm financial performance (Hinson & Ndhlovu, 2011). Therefore, firms' performance can be increased by increasing corporate social responsibility activities or implementing an appropriate sustainability strategy that equals all stakeholders.

### 1.1.3 The Companies Act, 2013, India

In India, the government enacted The Company Act of 2013 that set standards for corporate social responsibility. The Company Act, 2013 Section 135, requires that every business that has a net worth of RS 500 Crore or a turnover of more than Rs 1000 crores or makes an annual net profits of Rs 5 crore to contribute at least 2% of the average net profits for three preceding financial years for corporate social responsibility activities (Khandelwal & Bakshi, 2014). The turnover, net profits, and net worth are to be calculated according to terms stipulated in Section 198 of the Company Act 2013. Companies need to form a corporate social responsibility committee that

consist three or more directors who are to formulate and make recommendations to organizations CSR policy. The Indian firms are therefore required to adopt CSR as part of their business operations to avoid government sanctions.

#### 1.1.4 Aims and Objectives

The following research paper aims to investigate the relationship between the CSR activities of companies and their market valuation a case study of 20 large-size Northern Indian firms. The research will use both primary and secondary data to investigate and conclude the relationship that exist between social responsible activities and equity valuation. The information of this report will be used to recommend business CSR approach to increase market valuation.

1. To assess the role of CSR in influencing firm performance
2. To assess the impact of CSR in market valuation of Northern India region Firms.

## 1.2 LITERATURE REVIEW

### 2.2.1 Importance of CSR in Contemporary Firms

In one of the latest studies by Ghosh, (2015), stated that an organization with good corporate citizenship fosters long-term loyal relationship with customers. He found that customers were willing to pay high and premium prices for goods or services offered by a business that engages in CSR. Customers become promotional mechanism through word of mouth. He also found that consumers “punishes” firms that they believe behave socially irresponsible by boycotting products and encouraging others not to buy from the firm (Groza, Pronschinske, & Walker, 2011).

Furthermore, Dhanesh, (2014) noted that CSR enhanced collaborative work environment. They found that employees whose demands were considered were committed and loyal to the organization. The organizations are also able to attract and retain highly talented employees in the industry that improves organizational performance. They concluded that in competitive industries, employees’ satisfaction is only achieved by incorporating their interests and perceptions into their work that in turn improves constancy and commitment in the organization.

On the other hand, Garriga & Melé, (2013) defined CSR as a continuous commitment by an organization to behave ethically when contributing to economic development while improving workforce, their families and local community quality of life that impact organization perception, operations and performance. They argue organization integration of environmental, social, and economic considerations approach creates long term benefits to the business. Garriga & Melé, (2013) concludes that engaging business shareholders and other stakeholders efficiently manages potential

risks building credibility and trustworthiness in the society that a business operates in. However, Du, Bhattacharya, & Sen, (2010) assessed that financial capabilities were the major beneficiaries of CSR rating. They found that company’s cost of equity was cheaper for companies that had higher CSR ratings. These findings were supported by Arevalo & Aravind, (2017) where they found that the relationship was stronger in stakeholder oriented countries. Thus, the studies imply that CSR is an important component of firms thereby allows organizations to integrate environmental and social aspects in enhancing equity to stakeholders and performance of the organization.

### 1.2.2 Factors affecting Firm Valuation

Lee & Yeo, (2016), avers that firm’s value is highly dependent on profitability. A highly profitable firm is more valuable than a less profitable business. They found that a firm with a competitive advantage was able to attain market and customer concentration that increased its profitability. Market and customer concentration enabled firms to consistently maintain profitability that increased firm’s value (Chandra & Ro, 2008).

Furthermore, Hail, (2013) defined firm valuation as the economic measure that reflects the market value of a company. Firm’s value is used to determine how well a firm is operating and the returns that shareholders get in return. Roll, Schwartz, & Subrahmanyam, (2009) on the other side defined firm valuation as the net worth of value that a shareholder is willing to give or receive in exchange of the shares owned. Similarly Li, Chen, & French, (2012) found that businesses value was negatively correlated to risk. The higher the business risk the lower the value of the business share. Investors were not willing to invest in high risky business that decreased the business share demand decreasing the it’s valuation (Yu & Zhao, 2015) .

However, according to Gaio & Raposo, (2011) firms’ value was highly affected to growth prospect. A firm that was likely to grow in the future had high value compared to stagnating businesses. They found that business earning tract was used by investors to add value to their shares in a firm. They also found that companies with industry and growth prospects had a higher value.

Lastly, Zheng, Liu, & George, (2010) research found that organizations that had CSR were able to easily acquire financing compared to other organizations. The organizations enjoyed high credit rating that enhanced their ability to get finances. Bancel & Mittoo, (2014) on the other hand, found that firms with CSR had lower cost of acquiring capital. The firms were therefore able to acquire capital that increased the firm’s value. Competitive advantage returns that shareholders, business risk, and high credit rating are

some of the main factors that were identified with respect to CSR in affecting firm valuation.

### **1.2.3 CSR report of companies in Delhi NCR region**

CSR in Delhi NCR region, companies have closely linked their strategies with principles of CSR that enhance sustainable development (Jain & Winner, 2016). CSR activities are looked as priority and many companies have scaled up their CSR operations. The Company Act of 2013 requires all companies to spend 2% of their net profits on CSR. According to Jain & Winner, (2016), only 18% of the top companies in Delhi NCR complied with 2% spending on CSR in 2014. In 2016, the CSR spending increased to 95% from 66% in 2015 financial year. Education and health care dot the largest share of the CSR spending (Vartiak, 2016). Environment sustainability is the third spent CSR practice by companies in Delhi NCR with more than 115 companies undertake more than 473 CSR projects in Delhi NCR (KPMG International, 2015). Therefore, all companies in Delhi NCR region report their CSR spending and have an increasing trend to meet the statutory law enacted in 2013.

### **1.2.4 Empirical studies on impact of CSR on firm valuation in India**

Several studies have been undertaken to investigate the impact of CSR on firm's valuation. Yu & Zhao, (2015) examined the impact of capital market as a result of corporate sustainability. The study used the NSE equity value and sustainability reports. The study used quantitative approach to analyze and conclude research findings. They found that corporate social responsibility practices and strategies reduce firm risks promoting long term creation of value of a company. Again, Servaes & Tamayo, (2013) research found that CSR contributed to firm's shares stability. He established that Tata Consultancy Services Limited (TCS) shares were stable for three years that made the company be ranked amongst the 4<sup>th</sup> biggest and valuable IT services company in the globe. He concluded that CSR enhanced good share purchase behavior to investors that sustained the firm's finances. CSR also improved financial performance that enhanced shares confidence. On the other hand, Jo & Harjoto, (2011) examined CSR critical factors and its impact on competitiveness and corporate financial performance. The study showed that CSR has positive relationship with CFP that increased the firm financial performance. The CSR also increased company competitiveness that increased its sales and general firm's value (Ammann, Oesch, & Schmid, 2011). They concluded that CSR activities in India were driven by competency, financial health, and stakeholder's satisfaction. Lastly, Mishra & Suar, (2010) research found that CSR improved firm reputation, created positive customer behavior and improved employees'

commitment. The research showed that companies were using CSR activities to establish their identity that become the focal point in attaining competitive advantage in the industry and market. Firms with high reputation were able to attract highly qualified and talented employees, gain customer loyalty that increased the firm's valuation (Vilanova, Lozano, & Arenas, 2009).

### **1.2.5 Research Gap**

From the literature review, there is research gap in determining optimal CSR spending for firm valuation. There is no study that focused in estimating the impact of CSR spending in North Indian Companies over equity value. Furthermore, CSR impact on value of business has not been studied on the basis of equity value of the company in India. Also no study estimates the impact of CSR spending in North Indian regional companies over equity values. Lastly, there is gap in literature on the basis of the time series and are not up to date.

## **1.3 METHODOLOGY**

### **1.3.1 Study Design**

The research is a quantitative research that analyzes numeral data to determine the effect of CSR spending to firms' valuations in North Indian region. An inductive research approach helped to determine the relationship where CSR spending is the independent variable and market capitalization is the dependent variable. According to Ripinsky & Williams (2008) market cap of a company is a good indicator of its market valuation. Companies' official websites as well as the National Stock Exchange (NSE) database was referred to for the data.

### **1.3.2 Sampling Plan and Size**

The research used a sample size of 20 large sized firms that are listed in the NSE and are based in North Indian region. The 20 largest companies in North India region are selected and data collected from the National Securities Exchange (NSE) and the annual financial reports. Sample is selected based on the size of the company and availability of required data. The sources of data collection were secondary sources, whereby equity performance values were collected from NSE database and CSR spending was collected from the company websites, annual reports and newsletters. The data collected for the past five years i.e. from 2013 to 2017.

### **1.3.3 Statistical Analysis**

The focus of the study is on quantitative analysis of the data collected. Data is primarily tabulated in a table and trend based percentage analysis used as a

basic tool to assess the impact of CSR spending on equity value of the company. The MS Excel package is used to analyze statistical data and presentation graphs. The statistical tools are used for sample analysis, frequency analyses, and percentage analysis.

### 1.3.4 Companies Selected

List of company headquartered in Northern India and also listed in NSE were;

Sl. No.	Company Name
1	Chambal Fertilisers & Chemicals Ltd
2	Container Corporation Of India Ltd
3	Bharti Airtel Ltd
4	Dalmia Bharat Sugar & Industries Ltd
5	DLF Ltd
6	Kwality Ltd
7	Radico Khaitan Ltd
8	Globus Spirits Ltd
9	Engineers India Ltd
10	Bharat Heavy Electricals Ltd
11	Jindal Saw Ltd (Jindal)
12	Indian Oil Corporation Ltd
13	Hero MotoCorp Ltd (Hero)
14	HT Media Ltd
15	Indraprastha Gas Ltd
16	Dhampur Sugar Mills Ltd
17	TT Ltd
18	The State Trading Corporation Of India Ltd
19	Godfrey Phillips India Ltd
20	JK Tyre & Industries Ltd

Table 1: List of chosen companies

## 4.4 RESULTS

The results from 20 large-size companies in North Indian Region and listed in National Securities Exchange (NSE) show that majority of companies are spending on CSR activities.

### 4.4.1 Descriptive Analyses

The data for a few companies (TT Ltd., Jindal Saw Ltd and Dalmia Sugars) were not available. The total CSR spending of the selected companies increased from Rs 178.8 cr in 2012-13 to Rs 537.7 cr in 2016-17. The number of companies allocating funds for CSR activities increased from 30% in 2013 to 90% in 2017. Companies that did not earn profits in a financial year did not set CSR budget. For instance TT Limited and The State Trading Corporation of India Ltd did not make profits and therefore did not set out CSR budget for the year. On the other side, companies that made profits had CSR spending budget for the year. For instance, Chambal Fertilizers and Chemical Limited, Container Corporation Limited and Bharti Airtel Limited consistently allocated resources for CSR activities. The market cap increased with increase in CSR spending but the value is not constant. The graphical

presentation shows that the average market cap of NSE of the companies selected was low in 2013 which increased to the highest level in 2017.

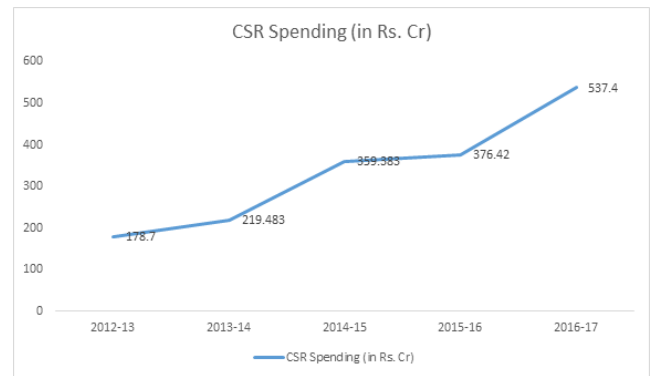


Figure 1: Cumulative CSR Spending for all selected companies (203-2017) in Rs. Cr.

Source: compiled by author

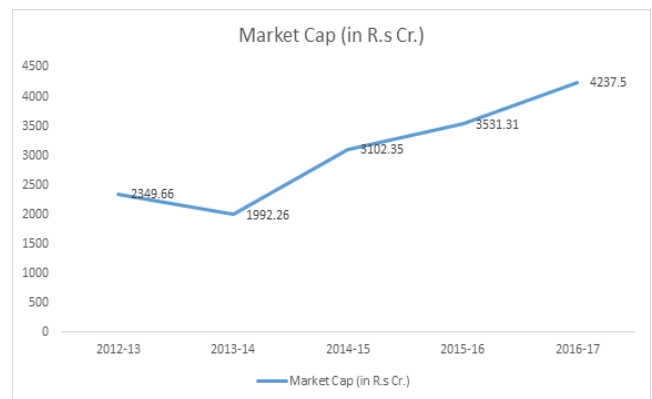


Figure 2: Cumulative Market Cap for all selected companies (203-2017) in Rs. Cr.

Source: compiled by author

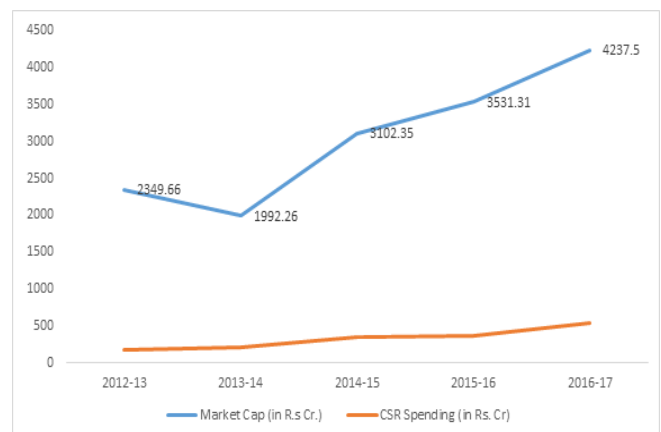


Figure 3: Comparison of Market Cap and CSR spending for all selected companies (2013-2017) in Rs. Cr.

Source: compiled by author



The amount of market cap doesn't have an immediate change as a result of change in CSR spending. From the selected companies, Bharti Airtel and Indian Oil Corp had the highest CSR spending and have the highest level of market cap. The companies have consistently increased their CSR spending in accordance with their increase in market cap. From the result of the research, CSR spending has increased in the last 5 years. Companies are reporting on CSR activities and budget allocated. The results also show that changing CSR spending does not immediately affect the firm's market cap in the security exchange market.

## 1.5 SUMMARY

From the result of the research, CSR spending has increased from 2013 to 2017. Companies are reporting on CSR activities and budget allocated. The number of firms reporting CSR activities and spending in India has increased notably in the last few years. Firms with high CSR spending have also shown the trend of consistency in NSE performance for most years. The results also show that changing CSR spending does not immediately affect the firm's market cap in the securities exchange market. The results of the research therefore, show that firm valuation can be increased by increasing firm's CSR spending of a company. CSR spending is a long term investment to firm valuation. The higher a firm's CSR spending the higher the market cap that is as a result of increased firm valuation.

## 1.6 CONCLUSIONS

From the research, there exist a relationship between CSR of companies and their market valuation. CSR activities affect the relationship between a firm and its stakeholders that largely impact its valuation. Human beings are important part of an organization and determine the success or failure of the organization. People work for organizations that impact to the surroundings. CSR ensures that all interests are considered by an organization when striving to meet its objectives. People's interests and environmental conservations are addressed through CSR that enhance sustainability of the business. Sustainability increases the organization's market value in the following ways;

CSR activities enhance customer relationship to the firm. Customers nowadays are attracted to companies that they perceive or engage ethically to both human beings and the environment. They investigate what the company is doing to enhance sustainability and make the world a better place for everybody. A good customer relationship enhances customer loyalty and promotion. Customers become loyal and committed to the company and its products (Li et al., 2012). This improves the company sales predictability and new

product adoption increasing profitability. Customers also promote the firm that they like. They encourage their families and friends to buy products from the organizations that they perceive to be engaging in sustainable business. Contrarily, customers can dislike a company and encourage families and friends to boycott their products that lead to low sales or product failure. Customers have power to determine the profitability of a company (Lai, Chiu, Yang, & Pai, 2010). Therefore, the more a company spends on CSR, it improves its perception to target audience creating good customer relationship that increases the company's customer base increasing the firm value.

Secondly, CSR activities improve confidence of the company. Firms that spend on CSR to enhance sustainability improve both investors and creditors confidence. Investors are willing to invest in organizations that practice sustainability because they are perceived to have less risk. CSR activities enhance environmental and other stakeholders' relationships that reduce the risk of company failure or loss of invested funds (Wang & Zhang, 2015). Investors also perceive organizations that have CSR strategy to be long lasting compared to ones without the strategy. Companies with CSR strategy maintain their resources and work in good harmony with the environment that enhances their survival in the future. This aspect increases investors' confidence and are willing to invest in the company. This increases the company's stock demand increasing the market value of the company. On the other side, creditors favor companies that have high CSR ranking (O'Connor & Meister, 2008). They perceive them sustainable and ethical and therefore credible for financing. The companies get large and long term financing that increase the firm's capital that increases performance. Confidence therefore, enables the company to get financing from either investors or creditors boosting its operations. Adequate and available financing increase the capital value and enhance performance. Hence, CSR enhances confidence that increase the company market value through investors and creditors.

Thirdly, CSR of a company maintains employees in the organization. Employees are very valuable in an organization. Companies cannot be formed without employees as they are required to combine other factors of production to produce products. CSR protects the employees' interests and create a favorable environment for working. CSR enable a company to attract and maintain high skilled and talented employees. Maintaining talented and highly skilled employees enables the company to attain a competitive advantage in the production process (Jain & Winner, 2016). Highly skilled and experienced employees also like associating themselves with reputable organizations that incorporate their interests in the workplace. Maintaining good employees'

relationship in the company enhances collaboration that improves efficiency. Efficiency is important in minimizing resource use while maximizing output. This improves the company financial performance by increasing profitability. Skilled, talented, and experienced employees are valuable resources to any organization. They give company a competitive advantage that increases the profitability and value of the company (Dhanesh, 2014).

Lastly, the CSR of a company enhances resources sustainability. Companies that invest in CSR save resources that are useful in future usage. CSR activities save nonrenewable resources by employing renewable resources. Nonrenewable resources are resources that can get exhausted from their natural sources. These resources can be used up if they are not well managed. Companies that engage in CSR activities have sustainability policy that governs usage of nonrenewable resources to avoid exhausting. Companies need resource inputs to produce products and if resource sources are not controlled they can get used up leading to closer of the business. CSR of companies also enable conserve the environment by responsible acquisition and usage of natural resources. Companies reduce their carbon emission to reduce green gases in the atmosphere. Excessive carbon emission has impact to the environment that includes damaging of the Ozone layer and increasing global warming. Carbon emission can also cause acidic rain that harmful to living creatures and damages infrastructures. Socially responsible companies aim to reduce carbon footprint by reporting in the annual report in order to track progress. CSR of companies advocate for renewable source of energy as opposed to electricity. The companies set solar systems to replace the condensed method of electricity. Solar energy is a renewable and environmental friendly source of energy. CSR strategy aims to reduce the units of electricity that they use because it not friendly to environment. Conventionally electricity is sourced from either from thermal or hydel and lead to increased water temperature that is dangerous for living things in water. Animals and plants that live in water die when they are subjected to extremely hot water and change in their natural habitat. Companies implementing CSR strategies care for the surrounding through responsible sourcing of resources and sustainable engagement with the environment. Resource sustainability enables companies to cut operations costs, maintain raw material and enhance sustainable development (Reverte, 2012). Companies benefit from cheaper usage of renewable resources such as solar panels that only require initial cost and minimal maintenance cost compared to conventional electricity. The companies are also able to maintain raw material sources that sustain business operations. Resource sustainability also enables sustainable development. The company is able to develop at the same time developing the environment that surrounds it. Resource sustainability therefore enhances interdependence between the company and the environment for co-existence. This enables the business to pursue long

term goals and survive in the future without fear of exhausting resources or environmental hazards. Resource sustainability reduces future uncertainty that increase the firm's value.

In conclusion, CSR of companies is a key component to determining market value of a company. CSR unite all factors in an organization that increases the value of the company stock. CSR enhance competency, financial health, and stakeholders' satisfaction that have direct impact to firm valuation. Competency is increase by attracting, maintaining, and retaining highly skilled, experienced, and talented employees who enhance competitive advantage for profitability. Financial health of a company is determined by availability and adequacy of financing that is only available to reputable companies. Finally, stakeholders' satisfaction is dependent on the relationship between the company and stakeholders. The company has to incorporate all stakeholders' interests through a CSR strategy. Stakeholder satisfaction determines loyalty and confidence that have direct impact to firm valuation.

Furthermore, to conclude that CSR of companies have a linear relationship with company market valuation. I recommend that companies should implement a CSR strategy because it increases the company market value. The CSR should be an ongoing practice for companies to enhance sustainable development and increase firm value thereby benefiting all stakeholders.

However, certain limitations were assessed at the end of the study, as only secondary data was used to estimate the impact of CSR on equity values. Lack of primary data and accessibility to data was one major constraint. Furthermore, mixed method of analysis was not implemented due to lack of relevant data resources. Addressing the limitations is the aim to be focused on in the next research study.

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Table for CSR spending and total turnover of 20 chosen companies in North India

Company Name	2017 CSR spending	2017 Turnover	2016 CSR Spending	2016 Turnover	2015 CSR Spending	2015 Turnover	2014 CSR Spending	2014 Turnover	2013 CSR Spending	2013 Turnover
Chambal Fertilizers & Chemicals Ltd	9458300000	124000000	906000000	3120722	84000000.0	270585545	25400000	42617250	1220000	51608755
Container Corporation Of India Ltd	2427000000	44400000	309600000	26200000	205600000	36900000	103800000	14400000	43800000	6272092
Bharti Airtel Ltd	975590000	225000000	575000000	111000000	411000000	174000000	274000000	164000000	125000000	152000000
Dalmia Bharat Sugar & Industries Ltd	36000000	38248718	23000000	44192520	5000000	1744195	26000000	519276	13000000	480103
DLF Ltd	68500000	187000000	104000000	125000000	12820000	114000000	64100000	183000000	0.00	170000000
Kwality Ltd	34000000	197000000	1000000	113000000	240000000	83722487	150000000	18640594	0.00	6661485
Radico Khaitan Ltd	13900000	222000000	21200000	63823540	13900000	35741704	0.00	59525999	0.00	25062883
Globus Spirits Ltd	400000	2111639	4700000	269650	5000000	12897047	0.00	10106357	0.00	7628075
Engineers India Ltd	110000000	456000000	141000000	341000000	170700000	117000000	80300000	158000000	4400000	24768536
Bharat Heavy Electricals Ltd	267800000	871000000	662000000	946000000	1020600000	849000000	560300000	1240000000	2330000	811000000
Jindal Saw Ltd	68000000	1296959	64500000	3831858	52500000	68661448	0.00	128000000	0.00	18535233

Indian Oil Corporation Ltd	2139900000	1920000000	1566800000	963000000	1137900000	618000000	496300000	362000000	0.00	180000000
Hero MotoCorp Ltd (Hero)	851400000	1490000000	650000000	1270000000	237000000	1430000000	0.00	1170000000	0.00	633000000
HT Media Ltd	33000000	3150797	24500000	18351768	27300000	14881108	0.00	31688792	0.00	9155948
Indraprastha Gas Ltd	65200000	575000000	44300000	504000000	13300000	172000000	0.00	172000000	0.00	143000000
Dhampur Sugar Mills Ltd	5090000	135000000	3900000	97326885	200000	7086693	0.00	8304894	0.00	3854513
TTLtd	0.00	6898374	0.00	695619	0.00	1901304	2335248	1446324	0.00	73805
The State Trading Corporation Of India Ltd	0.00	80761742	736000	34301733	0.00	21369374	0.00	55069526	0.00	52192533
Godfrey Phillips India Ltd	49900000	169000000	47200000	215000000	49900000	90330686	0.00	17522937	0.00	5316061
JK Tyre & Industries Ltd	78752000	238000000	47240000	178000000	18500000	222000000	0.00	334000000	0.00	32285199
Total	123521780000	11140830161	7983076000	18730487519	5457700000	7269921589	5182735248	7423441049	583950000	5287343221

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