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The Relationship of Corporate Governance and Profitability with Corporate Social Responsibility Disclosure in Pakistan

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Abstract
The objective of this research study is to investigate the impact of corporate governance attributes and profitability on corporate social responsibility disclosure (CSRD) among listed non-financial firms in Pakistan. The current study gathered data from the published annual reports of the 66 non-financial firms listed on the Pakistan Stock Exchange (PSX) from 2013 to 2016. The study employed a fixed effect model or a random effect model for data analysis, along with some pre-requisite diagnostic tests. The results of the study demonstrate the following outcomes: First, the board size, managerial ownership, and return on assets are positively linked with corporate social responsibility disclosure; second, return on equity shows a significant negative relationship with corporate social responsibility disclosure. Importantly, this study suggests that corporate governance attributes and firm profitability are the most significant components in improving corporate social responsibility disclosure. The research study has some important implications for academicians, auditors, and policymakers in improving corporate social responsibility reporting disclosure.

Key Words: *Corporate Governance, Profitability,* Socially Accountable, *Managerial Ownership, Policymakers*.

Introduction

Corporate social responsibility (CSR) is an authorized term for the link and association between businesses and society (Khan et al., 2018). The concept of CSR was introduced by Sheldon (1924). The aim of introducing this concept was to create inclusive awareness about the negative impact of a corporation's operations on both environmental and social issues (Mousa et al. 2018). Corporate Social Responsibility Disclosure (CSRD) adheres to the corporation's obligation to provide information to various stakeholder groups and individuals. The main purpose of CSR is not only profit maximization but also includes the responsibility of the company toward its multiple stakeholders, like its investors, customers, community, employees, and environment (Gill, 2008; Ofori and Hinson, 2007; Platonova et al., 2018). CSR activities have originated in numerous areas, such as environmental welfare, public support, product promotion, advertisement, and fair employee treatment (Cherian et al., 2019; Mulyadi and Anwar, 2012; Reverte, 2009). The corporation's benefits are highly dependent on the excellence of its CSR communication (Chaudhri, 2016). Corporations direct many kinds of CSR activities, which are under discussion as to whether they are just used for brand image and status or whether they have an authentic impact on business performance (Birkey et al., 2016; Chernev and Blair, 2015; Saleem et al., 2022). Several studies have revealed that by investing in social welfare activities, a corporation can achieve an advantage over its competitors. Corporations with CSR activities also get more profit and attract more stakeholders (Ansong, 2017; Lambertini and Tampieri, 2015). Corporations can improve their market image through CSR activities, which increase consumer loyalty, purchase intentions among consumers and stakeholders, and other potential benefits such as tax breaks, free publicity, and attractiveness as an employer (Aguinis and Glavas, 2013; Cheema and Javed, 2017; Crane et al., 2019; Zara et al., 2022).

In the financial statements of numerous significant organizations around the world during the past few decades, several corporate accounting scams have been discovered. These frauds will eventually cause corporate meltdowns (Aygun et al., 2014; Glaum et al., 2004). For instance, high-profile cases and scandals include those involving the Taj Company, the Crescent Bank fraud case, the Mehran bank scandal, and the scandal surrounding the privatization of the Pakistan Telecommunication Company Limited (PTCL) in Pakistan. Other examples include the failures of Enron, Xerox, and WorldCom in the United States; Parmalat in Italy; Flowtex in Germany; AIH in Australia; and Royal Ahold in the Netherlands (Abid and Ahmed, 2014; Javeed and Yaqub, 2015). Investor losses amounted to hundreds of millions of dollars as a result of these incidents, which eventually undermined investors' confidence in the fairness of the financial markets. The absence of corporate governance norms and procedures is the primary cause of many business scams.

The main corporate development in the previous decade was the evolution of CSR along with the acceleration of corporate governance (CG) mechanisms (Awan et al., 2012). Companies with good CG attributes not only encourage ethics, transparency, and liability but also maintain profits while promoting greater disclosure practices (Bayoud et al., 2012; Lau et al., 2016; Ruangviset et al., 2014). Michelon and Parbonetti (2012) stated that profitable companies disclose more CSR information to authorize their presence, show their contribution towards society, and promote a positive impression of their performance in society. Profitable firms improve their status and seek a reputation by involving themselves in social activities (Ghazali, 2007; Saleem et al., 2020). CG codes might help in addressing key issues of corporate accountability, responsibility, corruption, and transparency (Christensen et al., 2015). The Security and Exchange Commission of Pakistan (SECP) issued the Companies CSR General Order in 2009, which is appropriate for all public corporations. According to the said order, for all organizations, it is necessary to disclose all CSR activities performed in each financial year in the directors' report to the shareholders. Corporations are encouraged but not bound to follow them, but, since 2013, the rules have been applied where appropriate to all public companies (Ehsan et al., 2018; Yu et al., 2019). In Pakistan, the Code of Corporate Governance (CCG) was introduced by the SECP in 2002. That was a major step in CG modifications in Pakistan for the establishment of a structure for better governance of corporations listed on Pakistan's Stock Exchange (PSX) (Saleem et al., 2020; Yasser et al., 2011). The SECP modified the CCG proximally in 2012, 2017, and 2019, which is used by Pakistan's stock exchanges. Although Pakistan is following the standards of CG codes and CSR guidelines issued by SECP and general rules to surpass CSR pursuit, it is still facing various scandals of outrageous wrongdoing.

The literature lacks consideration about CSR implementation when it approaches developing countries because this area of research is not fully developed and a gap exists (Ali et al., 2017; Malik & Kanwal, 2018). Pakistan is a developing country. CSR research in Pakistan has been going on for more than a decade (Yunis et al., 2017). Despite increased CSR and global awareness, several commercial scandals occur regularly in Pakistan, including the manipulation of workers' child labor. The exploitation of labor, child labor, deficient employees' advantages, an unacceptable workplace, and other corporate abuses were a couple of zones pinpointed by the global eye (Ashraf, 2018; Delaney et al., 2016; Fatima, 2017). This research study uses data from the manufacturing sector, the textile sector, as well as some other sectors to investigate the impact of CG and profitability on CSRD in Pakistan. This study is an attempt to draw attention to the understanding and perceptions related to CSRD in Pakistan. Therefore, the objective of this research study is to investigate the impact of corporate governance CG attributes and profitability on the CSR Disclosure index (municipal prosperity, well-being & training, environment & vitality, inventions & consumers, and staff) in selected non-financial firms in Pakistan.

The remaining sections of the paper are structured as follows: The literature review and methodology are presented in Sections 2 and 3, respectively. Then, Section 4 contains the empirical findings and discussion. The study's findings, suggestions, and future directions are all included in Section 5.

Literature Review

Board Size (BDS)

The most essential characteristic of CG is the board size (BDS). It signifies the size of the board of the corporation, which is denoted by the total number of members on the board (Daghsni et al., 2016; Michelon & Parbonetti, 2012; Saleem et al., 2019). Dias et al. (2017) stated in their study that CSRD is affected positively by BDS. A larger board will represent a larger assortment of investors and will also promote improved monitoring, more transparency, and improved levels of CSRD. It also fosters more self-confident stakeholder administration. Several studies have also stated a positive relationship between CSRD and BDS (Tibiletti et al., 2021; Laksmi & Kamila, 2018; Matuszak et al., 2019; Ntim & Soobaroyen, 2013; Rao & Tilt, 2016). Hassn (2014) stated that increasing the number of executives on the board, provides an occasion for members who are interested in CSRD and also increases communication levels between the corporation and the community. According to the previous literature, several authors claim that corporations' performance can be enhanced by having larger boards. Some other studies revealed BDS's negative impact on accomplishing CSR and found that BDS's disclosures have no impact on its disclosures (Kolsi, 2017; Opusunju & Ajayi, 2016; Saleem et al., 2020). Corporations have a limited number of board members, and several authors suggest that larger boards are less likely to generate any positive contribution to a corporation's performance and are most likely to cause problems, which generally dominate the potential benefits of having a larger board (Lahlou, 2018).

Board Independence (BDIND)

Board Independence (BDIND) is the proportion of independent executives on the board (Saleem et al., 2019). These members make the best decisions for the enhancement of corporate image in social order and the protection of investors' concerns without the influence of others (Garca-Sánchez & Martnez-Ferrero, 2018; Garca-Sánchez et al., 2022). With a more independent board, the efficiency of the board will also increase, which also guarantees the value, superiority, and significance of firms' corporate information disclosure (Eberhardt-Toth, 2017; Saleem, 2018). Further, the efficiency of independent directors in increasing the level of CSR reporting might be hampered, possibly due to a lack of knowledge and experience relative to the type of industry (Mohamed et al., 2014). Independent directors avoid risky activities that could jeopardize their reputations. Likewise, independent directors boost CSRD in private businesses, which indicates that independent executives in private businesses concentrate more on sustaining stakeholders' hassles for CSRD (Bansal et al., 2018). Many studies show that the independence of a corporation's board is positively associated with CSR practices. The more independent the board is, the more CSR practices will increase (Isa & Muhammad, 2015; Naseem et al., 2017; Rasheed et al., 2019; Saleem et al., 2019). However, several studies recruit a negative relationship between an independent board and CSR reporting (Allegrini & Greco, 2013; Rouf & Abdur, 2011). In the same vein, some studies revealed that there was no evidence of a significant association between BDIND and CSR disclosures (Liu et al., 2014; Mohamed et al., 2014; Sartawi et al., 2014).

Managerial Ownership (MO)

Managerial ownership (MO) is the entire proportion of shares detained by the administrators, the board of directors, and internal holders. MO allows managers to dominate the company and decide which plans and guidelines the company will follow because, in this case, the supervisor also acts as a shareholder (Al Amosh et al., 2021; Giannarakis, 2014; Khan et al., 2013; Liang et al., 2011). According to Antonio et al. (2017), a higher proportion of insider possession is virtuous for CSR and the financial presentation of a corporation. The Garas and ElMassah (2018) study found MO has a positive association with CSRD. The higher the level of ownership by the administration and board of directors, the higher the level of CSRD will be. Some previous studies found that MO had a substantial negative impact on CSRD and a negative association between managerial possession and CSR plans as reported. The higher share of MO is more likely to distribute voluntary information and reduce the monitoring capacity of other stakeholders (Akrout & Othman, 2013; Khan et al., 2013; Khlif et al., 2017). Likewise, some other prior studies revealed no association between MO and CSR (Agustia et al., 2018; Razak & Mustapha, 2013).

Return on Asset (ROA)

Return on Asset (ROA) is a profitability ratio technique that is expected to measure the capability of the corporation's overall resources contributed to the corporation's procedures with the intent of making profits by consuming the assets reserved. The higher the ratio, the higher the rate of return will be (Manurung et al., 2017). Manurung and Rachmat's (2019) study reveals that financial performance through ROA had a negative and significant effect on the CSRD. Corporations that are unable to achieve the level of ROA are reluctant to disclose ROA information, whereas the importance of disclosing CSR demonstrates the corporation's capability in socioeconomic and environmental matters. Large-resource companies generally do not focus on CSR or demonstrate excellence through their concern for the environment (Kuo et al., 2021; Razak et al., 2019; Saleem et al., 2022). The link between CSRD activities and ROA is advantageous. According to Dienes and Velte (2016), Matuszak & Róaska (2017), and others, CSR indices assist businesses in improving their credibility, reputation, and image with investors, which may help them cut expenses and increase profits. Some empirical investigations reveal no connection between ROA and CSR (Ben-Amar et al., 2017; Prado-Lorenzo et al., 2012).

Return on Equity (ROE)
Return on equity (ROE) is the ratio between net income and overall equity. The higher the ROE, the better organized the corporation's particular investments are to generate net profit the corporation's particular investments are to generate a net profit. (Manurung et al., 2017; Saleem et al., 2022). Razak et al. (2019) demonstrate the corporation's ability to manage profits to increase investor interest and show that it can greatly disclose CSR. The more CSR disclosure there is, the higher the ROE, and the more detailed information shared with shareholders and other stakeholders, the more accurate the firm's information will be deemed. According to certain studies, financial success as measured by ROE had a favorable and considerable impact on the CSRD (Bani-Khaled et al., 2021; Manurung & Rachmat, 2019; Matuszak & Roaska, 2017). According to Majeed et al.'s (2015) analysis, there was no meaningful correlation between ROE and the disclosure of CSR activity. Because ROE is a measure of short-term financial success, whereas the goal is to generate long-term profits, the disclosure of CSR activities is still less effective at promoting an improvement in ROE.

Research Study Hypothesis
The current research study used five independent variables. The three variables board size (BDS), board independence (BDIND), and managerial ownership (MO) represent corporate governance attributes, and return on assets (ROA) and return on equity (ROE) are the two proxies used to represent profitability. The study was used to investigate the impact of all these selected variables of corporate social responsibility disclosure. Therefore, the five hypotheses of the study are as follows:

H_1: There is a significant relationship between BDS and CSRD in listed non-financial firms in Pakistan.
H_2: There is a significant relationship between BDIND and CSRD in listed non-financial firms in Pakistan.
H_3: There is a significant relationship between MO and CSRD in listed non-financial firms in Pakistan.
H_4: There is a significant relationship between ROA and CSRD in listed non-financial firms in Pakistan.
H_5: There is a significant relationship between ROE and CSRD in listed non-financial firms in Pakistan.

Research Methodology

To ascertain the effect various corporate governance attributes and profitability have on corporate social responsibility disclosures, the present research study collected data on 66 non-financial companies of the KSE-100 index listed on the Pakistan Stock Exchange (PSX). Annual data for the study was gathered from the published annual reports of the companies from 2013 to 2018. The study used panel data techniques. The study excludes firms that had incomplete data during the sample period and firms that were in the process of mergers and acquisitions between 2013 and 2018. Therefore, the target population of this study only includes 66 non-financial firms. Table 1 shows the list of selected non-financial firms for analysis.

Table 1: *List of non-financial firms in the KSE-100 index*

No.	Sector	No. of Companies
1	Cement	9
2	Chemicals	8
3	Food products	4
4	Oil And Gas	10
5	Manufacturing	6
6	Textile	7
7	Sugar	1
8	Mineral Products	1
9	Information, Communication & Transport	4
10	Refined Petroleum Products	7
11	Paper, Paperboard & Products	2
12	Electrical Machinery & Apparatus	1
13	Motor Vehicles, Trailers & Auto Parts	5
14	Other Service Activities	1
	Total	66

Source: www.psx.org.pk

This study considered CSRD as the dependent variable. The reason for choosing this variable is justified by some prior studies (Aslam et al., 2018; Hermawan & Gunardi, 2019; Mousa et al., 2018). CSRD is the information disclosed voluntarily by a corporation concerning the social, ethical, and environmental effects of an organization's economic actions and its association with the corporate stakeholder through suitable channels, focusing on applicable content (Balluchi et al., 2019). A corporation can disclose its CSR undertaking in its sustainability report, a trade report associated with its financial and conservational policies. For measuring CSRD, the CSR reporting index has been used (Ehsan et al., 2018; Matuszak et al., 2019).

CSRD index=$\sum_{di} n40/nj$

A CSRD directory is settled based on 40 items. If the information about item di is revealed, di is 1, else it is 0. The total number of goods for both businesses is n, which equals 40. Following a similar methodology, five separate indices are also created: (1) the general community welfare index (11 elements), (2) the health and education index (5 items), (3) the environment and energy index (7 items), (4) the product, customer, and stakeholder index (9 items), and (5) the workforce index (8 items) (Ehsan et al., 2018). Looking at the independent variables, we consider two sets of independent variables, CG attributes, comprised of three variables: BDS, BDIND, and MO. whereas profitability measures include two variables like ROA and ROE.

The quantitative data analysis would be conducted by using a fixed effect model or a random effect model (REM). The data has been analyzed using STATA software. Equation 1 provides the association between CSRD and CG attributes and profitability.

$\mathrm{CRSD}_{it} = \beta_O + \beta_1 \mathrm{BDS}_{it} + \beta_2 \mathrm{BDIND}_{it} + \beta_3\, MO_{it} + \beta_4\, ROA_{it} + \beta_5\, \mathrm{ROE}_{\,it} + \varepsilon_{it}$

Where CRSD_{it} represents corporate social responsibility disclosure of the firm (i) in period (t), $\beta_\circ$ is the Intercept, $\beta_{1\text{-}5}$= Variables coefficients, Board size (BDS), Board independence (BDIND), Managerial Ownership (MO), Return On Assets (ROA), Return on Equity (ROE), and ε_{it} is an error term.

Results and Discussion

Descriptive Statistics

Descriptive statistics are a summary measure of data in terms of central tendency and dispersion. Descriptive statistics of variables under study for non-financial firms are presented below to better understand the behavior of variables in Table 2.

Table 2: *Descriptive statistics for the non-financial firms of the KSE-100 index*

Variable	Mean	Std. dev.	Min	Max	Obs
CSRD	30.607	5.7268	8.9030	43.539	351
BDS	9.2676	2.6065	5.0000	22.00	396
BDIND	1.8459	1.5828	0.0000	9.000	396
MO	-0.005	1.4648	-4.397	1.795	396
ROA	1.3149	12.616	-8.5693	0236	396
ROE	75.639	354.80	0.0002	4399	396

Unit Root Stationary Test

The unit root test has been used to determine the stationary and non-stationary nature of the data. Table 3 shows the detailed results of some variables in this study to demonstrate that either the variables are stationary or unit-root variables or not. We used the Fisher type to determine whether the data were stationary or not. The findings of the aforementioned unit-root and stationary tests show that CSRD, ROA, and ROE are stationary at the first difference, respectively.

Table 3: *Fisher Type Test*

Variables	Fisher Type Test (1st Difference)
CSRD	-4.8281***
	(0.0000)
ROA	-14.1068***
	(0.0000)
ROE	-14.8339***
	(0.0000)

Standard error in parentheses ,*** $p<0.01$, ** $p<0.05$

Hadri LM Tests

The study used the Hadri test to determine the stationary or non-stationary nature of the remaining variables. Table 4 shows the result of the Hadri LM test. The results of the aforementioned unit-root/stationary tests show that BDS and BDIND are stationary at the level, according to the decision criteria of the P-value, which is less than 0.01% level of significance by rejecting the alternative hypothesis.

Table 4: *Hadri LM Test*

Variables	Hadri LM Test (At Level)
BDS	4.7056***
	(0.0000)
BDIND	4.9206***
	(0.0000)

Standard Errors in parentheses, *** $p<0.01$, ** $p<0.05$

Hausman Test

Table 5 shows the findings of the Hausman test, which specify the criteria for the selection of the fixed effect model or the random effect model. The result of the Hausman test showed that a fixed effect model is appropriate for this study as the p-value of the test is significant or is less than 5%, respectively.

Table 5: *Hausman Test of CSRD*

Chi-Square Statistics	Prob
16.28	0.036**

Standard Errors in parentheses, *** $p<0.01$, ** $p<0.05$

Fixed Effect Model
Table 6 shows the result of the fixed effect model. The findings indicate that some variables have a significant and some variables have an insignificant association with the corporate social responsibility disclosures of selected non-financial firms.

Table 6: *Fixed Effect Model*

Variables	Total CSRD
BDS	0.00748*
	(0.069)
BDIND	0.00969
	(0.220)
MO	0.01359*
	(0.080)
ROA	0.00359*
	(0.0464)
ROE	-0.00032*
	(0.051)
Constant	1.388857
	(0.000)
R-Square	0.1554
Observations	111

Standard Errors in parentheses, *** p<0.01, ** p<0.05

BDS represents the board size, which shows that there is a positive and significant association between BDS and CSRD. However, the findings of this study support the previous studies (Hassn, 2014; Laksmi & Kamila, 2018; Majeed et al., 2015; Matuszak et al., 2019). The higher the number of board members, the greater the number of investors, the increased communication level, and the improvement towards CSR activities (Velte, 2022). It also increases an organization's performance, which might deliver proficient and better decision-making capabilities (Coffie et al., 2018; Lahlou, 2018). Findings from this study show a positive and minor association between BDIND and CSRD. Likewise, the results are supported by some prior studies that suggest that having a higher number of independent executives on the board will boost the promotion of CSR activities (Aslam et al., 2018; Isa & Muhammad, 2015; Naseem et al., 2017). The results of this study also show the positive and significant link between MO and CSRD that is supported by the previous literature (Antonio et al., 2017; Garas & ElMassah, 2018). These findings imply that increasing the percentage of managerial ownership will increase the level of CSR in businesses (Pandiangan et al., 2022). The findings between ROA and CSRD show a significant positive association and are supported by the previous literature, which suggests that CSR activities may help corporations reduce costs and lead to higher profits (Mansaray et al., 2017; Matuszak & Róaska, 2017; Yusoff & Adamu, 2016). However, the output of the assessed model shows a negative and significant association between ROE and CSR that is not supported by the previous literature, which suggests that firms should increase their equity capital to achieve a certain level of CSR activities (Nguyen et al., 2021). The value of R-square (0.1554), which is 15.54%, shows how much the model is effective in this study.

Conclusion, Limitation, and Future Work

The corporate governance–social responsibility relationship has recently received an excessive amount of consideration. There has been growing awareness of the role of companies in society, and in the end, the term "CSR" has been given much attention in the financial literature. However, in Pakistan, this intention has been overlooked in previous studies, and no more work has been done on the concept of CSRD. Therefore, it is important to expand the CSRD literature by checking its effects on a firm's financial performance as well as corporate governance characteristics. This study adds to the existing body of knowledge about the impact of CG attributes and profitability on CSRD, specifically in Pakistan.

It could be stated that the scope of CG has increased the importance of CSRD (Amran et al., 2014). In this study, the CSRD shows a significant and positive association with BDS that supports the first hypothesis of this research, so the first hypothesis is accepted. Similarly, MO also indicates a significant association with CSRD, so the second hypothesis is accepted. Profitable firms improve their status and seek a reputation by involving themselves in social activities (Ghazali, 2007). Further, Michelon and Parbonetti (2012) stated that profitable companies disclose more CSR information to authorize their presence, show their contribution to society, and promote a positive impression of their performance in society. The findings of the current study show that corporate governance attributes (BDS, MO) and profitability proxies (ROA, ROE) both have a strong impact on the CSRD of non-financial firms listed in Pakistan.

This study has some limitations, which point the way forward for future efforts to add new aspects to the literature. Firstly, this research study used data from non-financial firms listed on the KSE-100 index of PSX, and future work will be done on this topic by getting data from other sources like periodicals, newspapers, and authentic websites for disclosing such information. Secondly, there is a dearth of accessible data and a small sample size for this study. It just takes firms from the non-financial sector that are listed in the KSE-100 index. This sample size should be expanded in the future to obtain the desired results. Finally, the same study will be conducted on a large data set in some other economies.

The findings of the study assist academicians in better understanding the components that will influence a firm's CSR reporting disclosure. This research study is additionally significant for practice. It can be valuable for companies to recognize the executive viewpoints that are fundamental to improving their CSR disclosure. The affiliation of the industry with CSR disclosure might require corporate managers to increase their knowledge of CSR to adapt disclosure practices pertinent to the industry to which the company belongs. The outcomes of the study can also be important for audit professionals and policymakers.

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