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THE EFFECT OF CORPORATE SOCIAL RESPONSIBILITY ON NON-FINANCIAL PERFORMANCE IN SABAH OIL PALM INDUSTRY

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DISERTATION SUBMITTED IN FULFILLMENT FOR THE DEGREE OF MASTER OF BUSINESS ADMINISTRATION

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DECLARATION

I hereby declare that the material in this dissertation is my own except for quotations, excerpts, equations, summaries and references, which have been duly acknowledged.

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ABSTRACT

THE EFFECT OF CORPORATE SOCIAL RESPONSIBILITY ON NON-FINANCIAL PERFORMANCE IN SABAH OIL PALM INDUSTRY

The aim of this study is to determine whether CSR initiatives toward six different stakeholder groups contribute positively toward firm's non-financial performance in Sabah oil palm industry. The six groups of stakeholder are employees, investors, customers, suppliers, communities and natural environment. There are 54 participants in this study. Questionnaire survey form was used to collect the data related to the degree of implementation on CSR initiatives. The findings show that the implementation of CSR initiatives in Sabah oil palm industry is at a moderate level. The mean scores of CSR initiatives toward the various stakeholders are: employees' development (mean = 3.48), employees' welfare (mean = 3.29), investors (mean = 3.35), customers (mean = 3.55), suppliers' ethical practices (mean = 3.50), suppliers' pricing practices (mean = 3.79), communities protection (mean = 3.00), communities development (mean = 3.63) and environment (mean = 3.27). The results also reveal that only CSR initiatives toward investors ($\beta = .494$, $p < 0.00$) and communities' development ($\beta = .388$, $p < 0.00$) contribute positively toward firm's non-financial performance in Sabah oil palm industry. Therefore, this study suggests that there is a need to increase awareness among oil palm estate managers on the roles and importance of CSR issues in order to increase firm's non-financial performance.

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ABSTRAK

Tujuan kajian ini ialah untuk menentukan sama ada inisiatif-inisiatif CSR ke arah enam kumpulan pemegang saham menyumbang secara positif ke arah prestasi bukan kewangan dalam industry kelapa sawit di Sabah. Enam kumpulan pemegang saham ialah pekerja, pelabur, pelanggan, pembekal, komuniti dan alam sekitar. Terdapat 54 peserta dalam kajian ini. Borang soal selidik digunakan untuk mengumpul data berkaitan dengan darjah pelaksanaan inisiatif-inisiatif CSR. Penemuan menunjukkan bahawa pelaksanaan inisiatif-inisiatif CSR dalam industry kelapa sawit di Sabah berada di tahap sederhana. Skor min inisiatif-inisiatif CSR ke arah pelbagai pemegang saham adalah pembangunan pekerja (min = 3.48), kebajikan pekerja (min = 3.29), pelabur (min = 3.35), pelanggan (min = 3.55), amalan beretika pembekal (min = 3.50), amalan penentuan harga pembekal (min = 3.79), perlindungan komuniti (min = 3.00), pembangunan komuniti (min = 3.63) dan alam sekitar (min = 3.27). Keputusan juga mendedahkan bahawa inisiatif CSR ke arah pelabur ($\beta = .494$, $p < 0.00$) dan pembangunan komuniti ($\beta = .388$, $p < 0.00$) menyumbang secara positif ke arah prestasi bukan kewangan dalam industri kelapa sawit di Sabah. Oleh itu, kajian ini menandakan terdapat satu keperluan untuk meningkatkan kesedaran antara pengurus-pengurus kebun kelapa sawit berkaitan peranan-peranan dan kepentingan isu-isu CSR supaya dapat meningkatkan prestasi bukan kewangan.

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LIST OF SYMBOLS

-	Negative
=	Equal to
%	Percentage
<	Less than
>	Bigger than
β	Standard coefficient beta

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CHAPTER 1

INTRODUCTION

1.0 Background

Corporate social responsibility (CSR) has been widely studied during the last decade and continues to gain widespread attention even today. Various definitions of CSR have been proposed and generally revolve around the issues of humanistic, ethical and transparency in business conduct (Marrewijk, 2003). The importance and relevance of CSR become apparent partly due to the high profile cases such as Enron which not only resulted in bankruptcy but seriously damaged the capital market and economy. The fall of a giant corporation of the size of Enron caused public outcry for a greater sense of ethics among companies and socially responsible business practice.

In Malaysia, CSR is taken seriously by the government especially when dealing with publicly owned corporations to ensure sustainability. Bursa Malaysia which is responsible for monitoring the listed companies defines CSR as integrating open and transparent business practices into business operations which are based on ethical values and respect for employees, communities and the environment (Bursa Malaysia). Sustainability is crucial especially in industries which are environmental-sensitive. In this industry, financial results alone are insufficient to measure performance. Non-financial performances need to be emphasized as well to guide sustainability. For example, in the oil palm industry which is one of the key contributors to the Malaysian economy, sustainability requires yields improvement (non-financial indicator) without land expansion (Bruce, Carmody, Shaw and Morales, 2010). Bursa Malaysia also describes sustainability as an approach used to create long term value by capturing opportunities and managing risks that emerge from economic, environmental and social development.

Most existing research show positive relationship between CSR and firm performance (e.g., Choi, Kwak and Choe, 2010; Poddi and Vergalli, 2008; Waddock

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and Graves, 1997; McGuire, Sundgren and Schneeweis, 1988).These researches focus on the traditional financial performance of the firm. However, using the non-financial performance is also important and becoming very common in today's business environment to measure a firm long-term success and sustainability.

Malaysian is one of the largest producers and exporters of palm oil. In Malaysia, Sabah has the largest oil palm plantation area covering 1.43 million hectares or 28.6% of the total oil palm plantation area in Malaysia (MPOB, 2011). The oil palm plantation in Sabah is growing and the availability of land area in Sabah together with the increasing demand for edible oils and fats in the global market provide the motivation for this study. The demand is expected to grow rapidly and thus, provide an opportunity for the Sabah palm oil industry to continue its expansion.

The increasing demand for palm oil was due to several reasons. Palm oil is categorized as a low-cost food which can be used as a tool for the sustainable development for countries with food security problems such as China and India (Bruce *et al.*, 2010). It is also being used for the bio-fuel oil since the oil palm has higher yields as compared to other vegetable oils. Asides that, the properties of oil palm which exhibit only a little taste after being processed had also become advantage for its acceptance within the market. Due to lower production price and its advantages the oil palm has gain the attention within the local market and also the international market.

The Malaysia oil palm industry has been competing vigorously in the global market over the years with other types of oil such as canola, soybean, olive and sunflower. Not only that, Malaysia also faces stiff competition with other palm oil producers' countries. Example, Indonesia as the world's second largest palm oil producer whose production cost is very low is a constant threat to the Malaysian oil palm industry (Chandran, 2004). Other important issues faced by the oil palm industry include sustainability of palm oil production and social responsibility expectation from all stakeholders.

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Even though the increasing demand for palm oil products contributes toward Malaysian economy, oil palm plantation might not be beneficial to tropical forests and natural ecosystems. Oil palm plantation companies might expand their plantation in order to increase their production without considering the environmental impact. There are various arguments that natural rainforests have been recklessly destroyed by the palm oil plantations which result in massive deforestation in Asia and destructive climate changes (Bruce *et al.*, 2010). Deforestation not only affects the environmental issue but could also threaten endangered species (Turner, Snaddon, Ewers, Fayle and Foster, 2011; Fitzherbert, Struebig, Morel, Danielsen, Bruhl, Donal and Phalan, 2008).

Oil palm plantation also faces social issues such as workers' rights and land disputes (Bruce *et al.*, 2010). It is widely documented that workers' health is not seriously taken into consideration by management of oil palm plantations. Most of today's plantation labours are being poorly paid and at high level of exposure toward hazardous chemicals. Land disputes particularly in Sarawak and Sabah are generally the consequences of palm oil plantation expansion. Thus, the study of CSR relating to the palm oil industry is of considerable importance and forms the focus of this research.

1.1 Problem Statement

Globally, the oil palm plantation is growing and affects the lives of many stakeholders. Thus, it is crucial for the industry not to focus only on the economic values but also the ethical and social impacts of their operations on employees, communities and the environment. The expectations of the public and the government may pose additional pressure for the industry. Companies are encouraged to develop and implement environmental policies and socially-friendly management practices as a sign of corporate responsibility.

Recently, CSR has become a very important indicator for the evaluation of an organization by the publics and investors. Prior to this, organizational objectives were focused on profit and shareholder wealth maximization. Thus, most prior research focused their studies on the relationship between CSR and firm

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performance and report a positive relation between the variables (e.g., Poddi and Vergalli, 2008; Waddock and Graves, 1997; McGuire *et al.*, 1988).

Recent studies by Choi *et al.* (2010) and Mishra and Suar (2010) looked at the relationship between CSR and firm performance from stakeholders' perspective. Their finding also showed positive and significant relationship between CSR toward stakeholders and firm performance. Each stakeholder has different point of view and requirement toward the CSR.

This current study further examines the relationship between CSR and firm performance from the perspectives of six stakeholder groups. However, in line with the current business emphasis on non-financial performance, this study focuses on the relationship between CSR and non-financial performance. The aim is to examine how CSR toward each stakeholder group contributes to firm non-financial performance. The information obtained from this study can be used for CSR strategy and planning to enhance the long term benefits and sustainability of the Malaysian oil palm industry.

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1.2 Objectives

These objectives of this study are:

i) To determine the extent of implementation of CSR initiatives in Sabah oil palm industry.
ii) To examine the effect of CSR toward employees on firm non-financial performance;
iii) To examine the effect of CSR toward investors on firm non-financial performance;
iv) To examine the effect of CSR toward customers on firm non-financial performance;
v) To examine the effect of CSR toward suppliers on firm non-financial performance;
vi) To examine the effect of CSR toward communities on firm non-financial performance; and

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vii) To examine the effect of CSR toward natural environment on firm non-financial performance.

1.3 Research Questions

The research questions in this study are:

1. To what extent is the level of implementation of CSR initiatives in Sabah oil palm industry?
2. Which of the stakeholder groups have positive effect on firm non-financial performance?
3. Do socially responsible business practices have an effect on firm non-financial performance?

1.4 Scope of the Study

This study intends to explore the CSR from stakeholders' perspective in affecting a firm non-financial performance. The stakeholders group consist of employees, investors, customers, suppliers, communities and natural environment. CSR are measured from each of the dimension and the dimensions that contribute toward increased non-financial performance in oil palm industry are determined.

This study was conducted in Sabah oil palm industry. Sabah was selected since it represents the largest oil palm plantation state in Malaysia. Population of this study was the estate managers who were chosen based on their ability to make decisions and judgements for their organizational operations. In other words, they possess the knowledge and the relevant experience to provide the appropriate responses to this study.

1.5 Significance of the Study

CSR conception in Malaysia is relatively at an early stage. Many studies have been conducted to investigate the relationship between CSR and firm financial performance. However, the study on CSR from the stakeholders' perspective is still lacking. Therefore, this study contributes to fill this gap and addresses the influences of CSR from different stakeholders' perspectives toward firm non-financial performance in oil palm industry in Sabah.

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The findings of this study can be used as a reference guide by the management of Sabah oil palm industry because the findings reflect the feedback from key stakeholders that affect the firm performance. Therefore, the management team can respond to them by revising or redesigning organization policies and practices to better meet the stakeholders' need. With that, the overall performance of this industry can be improved.

1.6 Organization of the Study

This study is presented in five chapters. The first chapter covers the introduction which includes the background of the study, problem statement, objectives, research question, scope of study, and significance of the study. Chapter two discusses the literature review. In this chapter, the theoretical framework and research model is presented while chapter three focuses on the research method. The results of the study are discussed in chapter four where data analysis are presented and discussed in details. Finally, chapter five concludes the study.

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CHAPTER 2

LITERATURE REVIEW

2.0 Introduction

In this chapter the influence of corporate social responsibility (CSR) toward stakeholders on firm performance are reviewed. Firstly, the definition or development of each items, CSR, stakeholder theory and firm performance are reviewed. This is followed by the relationship between CSR and firm performance. Following that, the stakeholder theory and the relationship between CSR and firm performance are discussed. This includes CSR toward each of the stakeholders group in influencing the firm performance. Asides, this chapter also reviews and justifies the choice of variables.

2.1 Corporate Social Responsibility (CSR)

The concept of corporate social responsibility (CSR) has been changing over the time due to globalisation, global trends and changes of the international law. Today, various terms exist to define CSR. For example, CSR is defined as a company's sense of responsibility towards the community and environment in which it operates (Business Dictionary, 2012). Another definition of CSR is the continuing commitment by business to contribute to economic development while improving the quality of life of the workforce and their families as well as of the community and society at large (World Business Council for Sustainable Development). Most of the definitions or terms used were based on four parts conceptualization of CSR by Carroll (1979) who proposed that CSR components consist of four dimensions which were economic, legal, ethical and discretionary.

2.1.1 Economic Responsibility

According to Carroll (1979), the most social responsibility of a business is economic in nature. Organization roles were to provide goods and services needed by customers and sell it in order to gain profit. Each organization basically served as a basic unit of economic for society. Example of organizations role were to provide

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return on investment for the shareholders, creating jobs and fair pay for workers, discovering new resources, promoting technological advancement, innovation and creation of new products or services (Jamali, 2008). All the other business roles were predicted on this fundamental assumption (Carroll, 1979).

2.1.2 Legal Responsibility

The second dimension was legal responsibilities of the business. It showed on how a business had complied with the legal compliance. Society was expecting an organization not only to operate and gain profit but they were expecting the operation was within the framework of legal requirements (Carroll, 1979). Businesses had to comply with laws and regulations which had been set by the federal, state and local governments. Legal responsibilities also reflect codified ethics that they believe in fair operations according to the law which had been established (Carroll, 1991).

2.1.3 Ethical Responsibility

The third dimension was the ethical responsibilities of a business. It portrayed a business for doing the right thing as well as being moral and fair. There were activities that had not been codified into law but were expected of business by society's members (Carroll, 1979). Examples of those activities were respecting people, preventing social injury and also to avoid any of the social harm that might be the cause of the business. Ethical responsibilities had been determined by Carroll (1979) as the most difficult dimension for a business to deal with. This was caused by the weakly defined concept on the ethical responsibility which created confusion within the business context.

2.1.4 Discretionary Responsibility

The last dimension was known as discretionary responsibilities. It was based on individual judgment and choice on deciding what types of contribution they will make for giving back to society. The roles were based on voluntary business desire to involve in social roles which were not mandated, not required by law and not expected of a business in the ethical sense (Carroll, 1979). Examples of the voluntary activities might include the philanthropic contributions such as conducting

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in house programs for drug abusers, training for the unemployed or providing day-care centres for working mothers (Carroll, 1979). The philanthropic contributions not only cover for the examples, it might also involve in the donations of a company for handicap organization, helping natural disaster victims or any actions that showed their concern toward the society and environment. Jamali (2008) mentions that this type of responsibility was the most controversial since it create conflict with the economic and profit-making orientations of a business organization.

2.1.5 Pyramid of Corporate Social Responsibility

In years 1991, Carroll had revisited her previous work (Carroll, 1979) and proposed that the four groups of CSR which include economic, legal, ethical and discretionary categories might be represented in a pyramid form. The pyramid is as shown in Figure 2.1.

Figure 2.1: Carroll's Pyramid of Corporate Social Responsibility

Source: Carroll (1991)

The basic building block for the pyramid was the economic responsibilities. In order to achieve these economic responsibility businesses were expected to obey

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