Journal for Social Science Archives

Online ISSN: 3006-3310
Print ISSN: 3006-3302
Volume 3, Number 2, 2025, Pages 142 – 157
Journal Home Page
https://jssarchives.com/index.php/Journal/about

Role of Corporate Governance Internal Mechanism and CSR on Enhancing Firm Performance: Evidence from Pakistan

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ARTICLE INFO

Article History:

Received:	*March*	*02, 2025*
Revised:	*April*	*11, 2025*
Accepted:	*April*	*14, 2025*
Available Online:	*April*	*16, 2025*

Keywords:

Corporate social responsibility, transformational leadership, corporate governance, firm performance and environmental strategy

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OPEN ACCESS

ABSTRACT

The corporate business faces escalating social and competitive challenges in today's worldwide economy. Literature has revealed the existence of several internal disciplining mechanisms of corporate governance that are hypothesized as factors influencing firm performance. This paper reviews the theoretical and practical research on internal mechanisms of corporate governance, especially dividend payouts, CSR, environmental strategy, transformational leadership and firm performance. The main purpose of this study is to evaluate the role of leadership and environmental strategy in CSR and firm performance. Data were collected from managers of Pakistani financial analysis businesses. The ultimate sample size was 100, and data was collected through a questionnaire. This study found empirical evidence that favors an internal mechanism and CSR affecting firm performance, transformational leadership, and environmental strategy serve as a mediator among firm performance and CSR. Moreover, this research keen analysis on the previous studies related to CSR in emerging economies. Firms, policymakers, and practitioners may make efforts to enhance their CSR practices. Overall, we draw the conclusion that socially responsible corporate enterprise endeavors have a higher chance of success in Pakistan.

Introduction

In today's competitive market, organizations must prioritize social responsibility, firm performance and corporate governance to gain advantage (Rodriguez-Fernandez, 2016; Ali, 2023). Corporate social responsibility (CSR) t has become a prevalent issue for firms to maintain their operations in the global market, with worries regarding global warming, environmental preservation, and social welfare serving as a mediator among CSR and firm performance (Shih, 2024). This is done to gain consumer brand recognition and positive feedback.

While scholars have studied the impact of CSR on firm performance (El-Menawy et al., 2024; Phillips et al., 2019), it is unclear how CSR activities might drive future development and progress in enterprise operations. Moreover, focusing solely on earnings, sales, or corporate expansion may not always help organizations (Staniškienė and Stankevičiūtė, 2018; Phillips et al., 2019; Zhu et al., 2024). On the other hand, promoting and executing altruistic CSR thinking that prioritizes customer advantages, social welfare, or environmental preservation can enhance a company's sustainability and performance (Shih, 2024).

Corporate social responsibility (CSR), which is integrating social, economic and environmental concerns in corporate operations and stakeholder relations (Ling, 2019; Tziner & Persoff, 2024). CSR refers to the legal obligations of corporations to society and the environment, and the consideration of sustainable development and public policy (Kuo et al., 2024; Liu et al., 2021). A clear environmental strategy is likely to influence CSR-effectiveness when it comes to firm performance and stakeholder engagement. Research and practice show a growing link between corporate social responsibility (CSR) and environmental strategy (Jamil et al., 2022; Channa et al., 2021; Salman et al., 2024).

A sound environmental strategy is a moderator that amplifies the benefits of CSR by relating company actions to larger environmental challenges such as climate change, resource preservation, and pollution abatement. When firms take proactive initiatives towards environmentalism, they subsequently lend life to their CSR strategy.

Recent CSR research has focused on the role of leadership in selecting and executing organizational practices (Xue et al., 2024, Jnaneswar & Ranjit, 2020). Leadership's impact on firm performance and CSR is still not well understood (Niazi,2023; Nureen et al., 2023; Khan et al., 2018). However, transformational leadership has a huge impact on the efficacy of CSR activities (Niazi, 2023; Khan et al., 2018). Furthermore, transformational leadership affects the link among CSR and performance of the firm by fostering open communication and ensuring that CSR activities are perceived as authentic and beneficial by both internal and external stakeholders.

Additionally, corporate governance internal mechanisms, such as dividend payout policies, play a critical role in shaping firm performance by the managers to maximize the wealth of shareholders (Waheed, 2021). According to Nissim and Ziv (2001), a company's dividend payment refers to the amount of earnings distributed to shareholders. Dividend payouts are important for both shareholders and investors as they signify current and future organizational success (Farrukh et al., 2017; Bossman et al., 2022). This study has concentrated on only dividend payout as the corporate governance’s internal mechanism and its influence on the firm's performance.

The research discussed above have a significant constraint in examining how business performance affects CSR practices. Further study is needed to discover the association among CSR, environmental strategy, transformational leadership and corporate governance (dividend payout). A little research on the impact of CSR on a firm's performance, particularly considering the moderating role of environmental strategy and transformational leadership.

With the lens of agency theory this research presents a framework to assess the influence of CSR, and dividend payout on firm performance. This study utilized a path model analysis with a structural equation model (SEM). The research area's CSR challenges stem from a lack of awareness among corporate, public, and government stakeholders on their roles, rights, and duties in Pakistan. However, there is still a need to raise knowledge of CSR's advantages among corporations, corporate businesses, and stakeholders. In Pakistan, corporations view CSR as a liability rather than a source of long-term benefits for themselves, the public, and the environment due to inadequate implementation and research.

Consequently, there is a strong need to examine this critical issue and understand the CSR, dividend payout and firms performance in the selected study area. The role CSR on firm performance, especially moderating role of environmental strategy and transformational leadership has not been thoroughly explored, and CSR efforts are not achieving the desired outcomes. This motivated the researcher to study the impacts of firm CSR and dividend payout on the firm performance, while focusing on the environmental strategy and transformational leadership moderating role in the Pakistan corporate firms.

Examining the effects of dividend payments and corporate social responsibility (CSR) as corporate governance tools on business performance is the aim of this study. The study also investigates the moderating effects of transformational leadership and environmental strategy, looking at how these elements affect the connection between CSR and firm performance. The following important research questions are the focus of this study: (1) How does the distribution of dividends, as part of corporate governance, affect the firm's performance? (2) What impact does CSR have on firm performance? (3) How does environmental strategy affect the link between corporate social responsibility (CSR) and a firm’s performance? (4) How does transformational leadership affect the link between corporate social responsibility (CSR) and a firm’s performance?

Literature Review

Internal mechanism

Internal corporate governance mechanisms refer to the structures and processes established within an organization to ensure accountability, align managerial interests with those of shareholders, and enhance overall corporate performance (Ying et al., 2021; Denis, 2003). Dividend payout serves as a key internal corporate governance mechanism aimed at mitigating agency conflicts between managers and shareholders. By distributing a portion of earnings to shareholders, firms reduce the discretionary funds available to managers, thereby limiting the potential for inefficient or self-serving investment decisions (Farinha, 2003).

Regular and transparent dividend payments signal managerial discipline and financial stability, reinforcing investor confidence and aligning managerial behavior with shareholder interests. In this way, dividend policy functions not only as a financial decision but also as a governance tool that fosters accountability and curbs managerial opportunism. A well-structured dividend policy, therefore, plays a pivotal role in strengthening internal governance by promoting responsible financial management and enhancing firm value over the long term.

Dividend Payouts and the Firm Performance

By distributing profits to shareholders, dividend payouts reduce the discretionary funds available to managers, thereby curbing the potential for inefficient or self-interested investment behavior (Easterbrook, 1984; DeAngelo et al., 2006). Kumar (2003) posits that dividends act as a reward for shareholders, maintaining investor trust and signaling financial health.

Several empirical studies support the view that dividend policy contributes positively to firm performance. Thafani and Abdullah (2015), revealed that dividend payment ratios and business performance were significantly positively correlated in a panel analysis of industrial companies listed on the Colombo Stock Exchange, indicating that higher dividends attract shareholder investment and enhance firm value. Similarly, Alwi (2009), analyzing Indonesian firms, demonstrated that during periods of high agency costs, firms used dividends to signal effective governance, thereby improving performance. This is consistent with the findings of Jensen (1986) and Gugler (2003), who argue that dividends reduce agency costs and align the interests of majority and minority shareholders.

However, well-governed firms often use dividend policy strategically to balance shareholder expectations with long-term performance goals. When managed appropriately, dividend payouts serve as a credible governance mechanism that can enhance firm value and performance. Based on this theoretical and empirical foundation, subsequent proposition is proposed:

Hypothesis 1: A relationship exists between dividend payout and firm performance

Firm performance and CSR

Corporate social responsibility in India, has historically lagged behind Western applies (KPMG, 2005). However, economic, the entry of multinational corporations, increasing consumer expectations the case for CSR in the region (PiC, 2004). In India, CSR has traditionally focused on community development, with historical roots in philanthropic contributions by business communities during the 19th century, particularly among Gujarati and Parsi traders.

Despite this legacy, India ranks low globally in public expectations for CSR (International, 2001), partly due to a perceived weak linkage between CSR and firm performance. Barriers to CSR adoption by top management, lack of internal consensus, and challenges in measuring impact (Krishna, 1992). Institutional constraints such as unclear policies, poor governance, and inadequate infrastructure further hinder CSR initiatives. Nevertheless, there is a growing public sentiment that firms should go beyond profit-making to engage in broader societal responsibilities (Kumar, 2001).

Contemporary frameworks suggest a strategic view of CSR, where socially responsible actions contribute to firm competitiveness. Schaltegger et al. (2019); Kumar et al., (2023) and Li et al. (2020) argue that effective CSR enhances a firm's financial performance, market value, and strategic positioning. Williams (2001) posits an optimal level of CSR that maximizes both profit and stakeholder satisfaction, although individual leadership traits may also influence CSR engagement. CEOs, as key decision-makers, often shape CSR strategy and integrate social values into corporate priorities, reinforcing CSR's role as a strategic management function.

Empirical studies suggest that CSR can positively impact firm performance by strengthening stakeholder relationships and enhancing reputation (Margolis & Walsh, 2003; Waddock & Graves, 1997). This instrumental perspective views CSR as a strategic tool aligned with economic goals. According to previous studies, a hypothesis is occur such as:

Hypothesis 2: An association is exists between CSR and firm performance

Environmental strategy

Recently, increasing global pressure has led to the adoption and enforcement of stricter environmental regulations worldwide. Anticipating evolving policies and growing societal and market expectations, firms are increasingly engaging in proactive environmental strategies. The rise in demand for environmentally friendly products, services, and production processes has emphasized the strategic importance of sustainable practices for long-term competitiveness and survival.

While earlier research on environmental proactivity yielded mixed results (Christmann, 2000), several studies have linked strong environmental strategies to improved financial outcomes. instance, Mishra (2010) examined the influence of CSR on Indian manufacturing firms using a survey-based approach and Pearson correlation analysis. The study found that integrating environmental responsibility into corporate strategy contributed to firm performance, reinforcing the value of CSR in emerging economies.

Environmental strategies, when effectively implemented, not only improve operational efficiency and compliance but also enhance the association among CSR initiatives and firm's performance by strengthening stakeholder trust and market positioning. Based on this rationale, the following hypothesis is proposed:

Hypothesis 3: Environmental strategy acts as a moderator between CSR and firm performance

Transformational Leadership

Transformational leadership is widely recognized as one of the most effective and proactive forms of leadership, wherein leaders engage deeply with their followers to inspire performance beyond routine expectations. (Podsakoff et al., 1990), through a comprehensive review of seven key conceptualizations of transformational leadership, identified core behavioral dimensions such as articulating a compelling vision, fostering collective goals, challenging conventional thinking, addressing individual needs, establishing high performance expectations, and serving as a moral role model.

Within the strategic management literature, increasing scholarly attention has been directed toward the role of top executives in shaping organizational strategy and influencing firm outcomes. Rooted in the foundational insights of Child (1972), the upper echelons theory asserts that organizational outcomes, including performance, are significantly shaped by the values, experiences, and cognitive frameworks of senior leaders. This theoretical lens emphasizes the strategic influence of leadership in decision-making processes and corporate behavior, including CSR engagement.

In the context of CSR, transformational leaders are particularly instrumental in embedding social responsibility into the core of organizational strategy. Their ability to align employee values with broader societal goals, foster stakeholder engagement, and promote ethical practices enhances the implementation and impact of CSR initiatives. Consequently, such leaders not only influence the scope and quality of CSR efforts but also strengthen the linkage between CSR and firm performance by mobilizing organizational commitment and stakeholder trust. Based on past studies, the succeeding hypothesis is anticipated:

Hypothesis 4: Transformational leadership positively moderates the relationship between CSR and firm performance

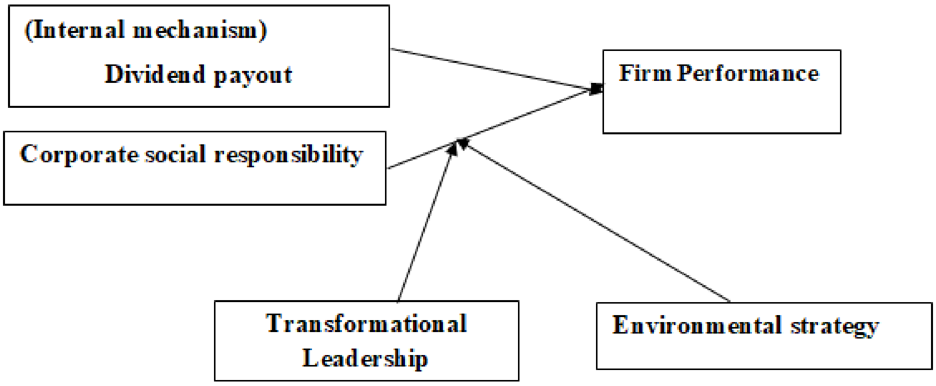

Figure 1: Framework of the study

Methodology

Sample selection

Convenience sampling is the method used for sample selection. According to Tabachnick (2001), the sample size required for a multiple regression analysis may be determined using the following formula: $N \geq 50 + 8m$, where m is the number of variables that might be predicted. The sample size for this investigation was 100.

Since there are five independent variables in the study, the sample size will be determined appropriately: 90 is equal to 50 + 8 (5). This method was also employed for sample selection by (Bibi, 2024). Data for this study came from financial analysts of Pakistani organizations that were sampled. There are 100 responders in all (mean n = 100). The foundation of this research is quantitative analysis.

Unit of Analysis

In this study, the respondents are choosing from managers in finance department of the organization.

Collection of Data

Primary data is collected through questionnaires for this study from the financial analysists of sample companies in Pakistan.

Selection of Instruments

For primary data, questionnaires are adapted by many studies. The dividend policy questions are adapted from the Richard & Edelman (1983) research, the environmental strategy and corporate social responsibility (CSR) questions are taken from the Mishra (2010) research, and the leadership questions are adapted from the Robert et al. (2005) study.

Proposed statistical test

This study employed regression analysis to explore the influence of corporate governance and CSR on performance of the firm. Additionally, SPSS is used to quantify the outcomes.

Results and Discussion

Table 1

Summary of Case Processing

		N	%
Cases	Valid	100	97.1
	Excluded[a]	3	2.9
	Total	103	100.0
Cronbach's Alpha		.969	
N of Items		5	

a. List wise deletion based on all variables in the method.

Summary of Case processing

The number of observation is 100. Moreover, it shows that data is almost 96.9% reliable.

Overall Reliability

Model summary

Table 2

ANOVA[b]

Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	5.923	2	2.962	148.350	.000[a]
	Residual	1.937	97	.020		
	Total	7.860	99			
	R	.868	R^2	0.754		

a. Predictors: (Constant), CSRt, IMt

b. Dependent Variable: FPt

Table 2 presents, that value of F is at good and data is significance. Additionally, the value of R-square is almost 74.9% which depicted that 75% deviation in firm performance is due to change in the disparity of CSR and internal mechanism of corporate governance.

Table 3

Coefficients[a]						
		Unstandardized Coefficients		Standardized Coefficients		
Model		B	Std. Error	Beta	T	Sig.
1	(Constant)	.650	.217		2.990	.003
	IMt	.336	.087	.525	3.826	.000
	CSRt	.301	.115	.356	2.591	.001

a. Dependent Variable: FPt

The result of the regression shows that corporate governance's internal mechanisms and CSR positively and significantly influenced the firm's performance.

Moderation of CSR and leadership

Table 4

Model Summary									
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Change Statistics				
					R Square Change	F Change	df1	df2	Sig. F Change
1	.851[a]	.724	.718	.14953	.724	127.257	2	97	.000
2	.868[b]	.754	.746	.14203	.030	11.521	1	96	.001

a. Predictors: (Constant), LDt, CSRt
b. Predictors: (Constant), LDt, CSRt, CSRtLDt

Two R-square values are displayed in Table 4: one is before to moderation, and the other is under its influence. Leadership acts as a moderator between CSR and business performance, as evidenced by the R-squared value of almost 72.4% before moderation and nearly 75.4% during moderation at the significant level.

Table 5

ANOVA[c]						
Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	5.691	2	2.846	127.257	.000[a]
	Residual	2.169	97	.022		
	Total	7.860	99			
2	Regression	5.923	3	1.974	97.880	.000[b]
	Residual	1.937	96	.020		
	Total	7.860	99			

a. Predictors: (Constant), LDt, CSRt

b. Predictors: (Constant), LDt, CSRt, CSRtLDt

c. Dependent Variable: FPt

ANOVA

Table 6

Coefficients[a]

Model-1		Unstandardized Coefficients B	Unstandardized Coefficients Std. Error	Standardized Coefficients Beta	T	Sig.
1	(Constant)	1.850	1.002		1.847	.068
	CSRt	-.351	.651	-.417	-.538	.590
	LDt	.672	.411	1.265	1.637	.104
2	(Constant)	12.202	3.195		3.818	.000
	CSRt	-2.401	.863	-2.850	-2.777	.006
	LDt	-2.381	.979	-4.489	-2.420	.016
	CSRtLDt	.622	.182	8.185	3.393	.002

a. Dependent Variable: FPt

In Table 6, Model 1, which has no moderating effects of leadership between CSR and firm performance, is displayed in Table 6. The coefficient value indicates that, at the insignificance level, leadership affects firm performance. Coefficient values in model 2 demonstrate that leadership acts as a moderator and reinforces the connection between firm performance and CSR. At the significant level, the correlation between CSR and business performance has improved by around 62.1% as a result of leadership.

Table 7

Excluded Variables[b]

Model		Beta In	t	Sig.	Partial Correlation	Collinearity Statistics Tolerance
1	CSRtLDt	8.185[a]	3.344	.001	.328	.000

a. Predictors in the Model: (Constant), LDt, CSRt

b. Dependent Variable: FPt

There is no multicollinearity issue, as this table demonstrates.
CSR and environmental strategy moderation

Table 8

Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Change Statistics: R Square Change	F Change	df1	df2	Sig. F Change
1	.847[a]	.717	.711	.15141	.717	122.930	2	97	.000
2	.868[b]	.754	.746	.14203	.037	14.235	1	96	.000

a. Predictors: (Constant), ESt, CSRt
b. Predictors: (Constant), ESt, CSRt, CSRtESt

Two R-squared values, one before and one inside the moderating effect, were shown in Table 8. At the significant level, the R-squared value is around 75.4% after moderation, compared to almost 71.7% before, indicating that environmental strategy acts as a moderator between CSR and firm performance.

Table 9

ANOVA[c]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	5.636	2	2.818	122.930	.000[a]
	Residual	2.224	97	.023		
	Total	7.860	99			
2	Regression	5.923	3	1.974	97.880	.000[b]
	Residual	1.937	96	.020		
	Total	7.860	99			

a. Predictors: (Constant), ESt, CSRt
b. Predictors: (Constant), ESt, CSRt, CSRtESt
c. Dependent Variable: FPt

ANOVA

Table 10

Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients		
		B	Std. Error	Beta	T	Sig.
1	(Constant)	.735	1.050		.701	.485
	CSRt	.430	.593	.510	.725	.470
	ESt	.166	.346	.337	.479	.633
2	(Constant)	12.201	3.194		3.819	.000
	CSRt	-2.401	.933	-2.850	-2.571	.011
	ESt	-2.381	.748	-4.845	-3.178	.001
	CSRtESt	.622	.164	8.541	3.774	.000

a. Dependent Variable: FPt

Coefficients

There are no moderating effects of environmental strategy on CSR and firm performance in Table 10, Model 1. The coefficient value indicates that the environmental strategy has a negligible impact on firm performance. The association between corporate social responsibility (CSR) and firm performance is strengthened by environmental strategy, as indicated by the coefficient values in model 2. At the significant level, there is a nearly 62.1% rise in the association between CSR and firm performance as a result of environmental strategy.

Table 11

Excluded Variables[b]

Model		**Beta In**	**t**	**Sig.**	**Partial Correlation**	**Collinearity Statistics Tolerance**
1	CSRtESt	8.541[a]	3.774	.000	.358	.000

a. Predictors in the Model: (Constant), ESt, CSRt
b. Dependent Variable: FPt

This table shows that no multicollinearity issue is occurred.

Implication

Implications for Academics and Researchers

This study provides new avenues for research within the domains of corporate governance and corporate social responsibility (CSR).In this regard, it encourages researchers to investigate how and when certain internal governance mechanisms — including measures such as audit committees, executive pay frameworks and shareholder rights — can impact CSR performance in different industries and geographical contexts. Emphasizing the importance of examining governance structures, which have been less addressed in prior literature, also provides valuable future research implications.

Future studies might focus on the interplay between these governance systems and CSR actions, examining the relationship between those and business performance, which could provide a more nuanced understanding of the dynamics at play. This method might lead to the development of more sophisticated theoretical models that account for the complex and context-dependent character of governance and CSR linkages.

Managerial implications

Our study highlights the crucial need for the integration of strong corporate governance mechanisms with effective corporate social responsibility practices for improved firm performance. In a nutshell, managers can act as agents of change not only to improve a firm's social and environmental performance but also its financial performance by instituting ethical leadership, clear CSR targets, stakeholder engagement, and transparency. This integrated strategy will help create sustainable value for the firm, its stakeholders, and society.

This study may help up to Pakistani executives strengthen his or her understanding of CSR, particularly the stakeholder map. Furthermore, this study tackles the problem of Pakistani firms that have not formed a long-term CSR policy owing to a lack of a shown relationship to profitability (British Council et al., 2002).

By demonstrating the positive relationship between strategic CSR, governance, and firm performance, this study provides a compelling case for the adoption of CSR as a sustainable and value-creating business practice in Pakistan.

Theoretical Implications

The theoretical implications of the study significantly enhance existing corporate governance and CSR theories by exploring the relationship between governance mechanisms and CSR in the context of firm performance. These contributions provide a more holistic framework for understanding how governance structures can influence CSR practices, leading to improved firm performance.

The study urges future research to further examine these links and develop existing theoretical models to better represent the intricacies of governance, CSR, and performance outcomes in a dynamic corporate context.

By deepening our understanding of these connections, this study encourages the evolution of more comprehensive theories that better reflect the multi-dimensional nature of governance, CSR, and performance in contemporary business environments.

Recommendation

The recommendations from this study are focused on enhancing the alignment of corporate governance, CSR, and performance of the firm. By increasing corporate governance processes, incorporating CSR into core strategy, and fostering responsible business practices, organizations may achieve long-term success while benefiting society.

Policymakers, investors, and researchers also have key roles to play in fostering this alignment, ultimately contributing to more sustainable and ethically responsible business practices across industries. Some important corporate governance variables to consider include ownership concentration, percentage of outside board members (if any), insider ownership, voting coalitions, and product-market competition (Aljifri, 2007).

Future research might be conducted for individual industry categories within the manufacturing business, such as automobiles, chemicals, and so on, to identify industry-specific concerns (Mishra 2010). A research might be undertaken by expanding the sample size and concentrating on firms that have contributed to CSR and dividend policies.

Additionally, future research could expand the sample size and target companies with active CSR engagement and distinct dividend policies to examine the broader impact of these factors on firm performance.

Conclusion

This study is focused on the relationship between corporate governance, CSR, and firm performance. All the hypotheses of this study are accepted. All of the questions that the researchers had were answered in this study. The study's initial question—that internal mechanisms affect firm performance—is answered by the first hypothesis. According to this study, internal mechanisms affect the firm's performance by over 62%. The second issue is whether or not corporate social responsibility (CSR) affects firm performance. The study's findings indicate that CSR affects firm performance by about 30%. The results demonstrated that leadership functions as a mediator between CSR and firm performance at a significant level, answering the third question of whether leadership has increased the link between CSR and firm performance. According to the findings, environmental strategy moderates the relationship between corporate social responsibility and firm success at a significance level. Overall, this study adds to the existing body of knowledge already in publication by empirically confirming the linked roles of internal governance, CSR, and strategic leadership in impacting company results. This study contributes to the existing literature by empirically validating the interconnected roles of internal governance, CSR, and strategic leadership in influencing firm outcomes. It also offers practical insights for managers and policymakers aiming to improve firm performance through sustainable and responsible business practices.

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