

The Mediating Role Of Corporate Social Responsibility On The Relationship Between Corporate Governance And Financial Performance Of Indian Banks

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Previous studies on the relationship between corporate social responsibility (CSR) and economic achievement have yielded results that are inconsistent. As a result, there has been a growing need for studies to explore mediators and moderators to better explain these varied findings. The relationship between corporate governance (CG) and financial performance (FP) is analysed in this study, with a focus on the mediating effect of CSR outcomes. Based on a sample of 26 banks listed on the Bombay Stock Exchange (BSE) in India, covering a ten-year period from 2014 to 2023 and consisting of 255 observations, our research demonstrates that CSR mediates the relationship between corporate governance and financial performance. The financial data were sourced from the Prowess database, while the CSR and corporate governance data were obtained through content analysis of the banks' annual reports. The outcomes demonstrate that CSR plays a critical role in enhancing profitability, efficiency, and market valuation, with CG directly influencing only market valuation (Tobin's Q). These findings contribute to the CSR literature by shedding light on the mediating role of CSR outcomes, helping to explain the previously inconsistent results in studies examining CSR and financial performance.

Keywords: Corporate governance, corporate social responsibility, financial performance, mediation, banks.

1. Introduction

The Indian banking sector has a rich history spanning around 200 years and has experienced significant changes since gaining independence. The oldest bank in the country is the State Bank of India. In the Indian banking industry, the Reserve Bank of India (RBI) is the highest regulating body. The liberalization, privatization, globalization, and introduction of

information technology have caused significant disruption in the Indian banking sector. The recent fraud in banks in India is an example of failure of corporate governance.

Corporate Governance (CG) and sustainability are emerging fields of study because they are crucial in managing organizational affairs given the increasing complexity of stakeholder demands, particularly concerning new phenomena such as COVID-19 [1]. CG refers to the principles, procedures, standards of conduct, and systems that promote accountability and proper conduct of business affairs for the benefit of stakeholders [2]. Risk and formal decision-making are two areas where governance is effective for organizational sustainability [3]. However, CG varies across countries and firms due to the cultural, economic, and social environment [4].

Consumers now expect organisations to pursue values that are sustainable for the economy and society. In this regard, CSR is essential, as it refers to the actions that organizations undertake to address these values [5].

As you may know, sustainable development is an essential problem that concerns many nations and the entire world economy. This type of growth is dangerous to the environment and socio-economic development since it is uncontrolled [6]. Effective CG, coupled with ethical practices, helps firms build trust, improve financial performance (FP), and enhance corporate image [7]. The association between CG and FP has been shown to be mediated by CSR in emerging markets like Indonesia [3].

Even though prior literature has focused on the connection between CG or CSR and FP [8], [9], [10], [11], the mediating role of CSR in the CG and FP relationship has not been studied extensively, especially regarding Indian banking industry. Banking is crucial for developing a nation's economy, and the managers of the banks have to be responsible for protecting the environment. This research study intends to provide an answer to this interesting research question of how CSR activities affect the CG-FP connection regarding the Indian banking industry.

Given are the research objectives: to measure banks' financial performance in relation to CSR; to analyze the mediating effect of CSR in this relationship; and to evaluate the relationship between CG and bank performance. Additionally, research aims to offer empirical evidence through robust methodology, on the significance of CSR in enhancing bank performance and to explore the implications for improving governance frameworks.

The results of analysis on 26 listed banking companies for a period of ten years show that CSR mediates the positive impact of CG on financial performance, with CSR playing a crucial role in driving profitability, efficiency, and market valuation, while CG directly influences only market valuation (Tobin's Q).

The remainder of the paper is structured as follows: Section 2 delineates the pertinent literature review, Section 3 delineates the methodology, Section 4 examines the results and discussion, Section 5 delineates the conclusions, and Section 6 addresses limitations and future "research.

2. Literature review and hypothesis development

(a) **Theories:** Several financial performance theories explain the relationship between CG, CSR, and financial performance. In Table 1 each theory, its postulation, and how it perceives CG and CSR are given.

Table 1: Theory and How it Perceives CG and CSR

Theory	How CG is perceived	How CSR is perceived
<p>Agency Theory [31]: The main focus of Agency theory is on the relationship between the Principal (shareholders) and Agents (Management). The theory assumes that agents might not act in the best interests of principals and could pursue self-interest leading to conflicts.</p>	<p>According to this perspective, corporate governance serves as a tool for monitoring as well as controlling managerial conduct to make sure that decisions are made with the best interests of shareholders in consideration.</p>	<p>This theory often regards CSR with skepticism. If CSR programs fail to optimize shareholder value, they may be perceived as a misallocation of resources.</p>
<p>Stakeholder Theory [29] emphasizes the interconnectedness of a firm with its customers, suppliers, employees, investors, and communities, promoting the importance of providing benefits for all stakeholders.</p>	<p>Prioritizing ethical issues and the interests of stakeholders in decision-making, CG should take into consideration the interests of all stakeholders, not just shareholders.</p>	<p>CSR is essential to the stakeholder theory because companies have accountability for the wider social and environmental effects of their operations.</p>
<p>Stewardship theory [30] assumes that managers, as stewards of the company, are inherently motivated to act in the best interests of the organization, including shareholders and other stakeholders. Managers” are viewed as trustworthy and capable of managing corporate resources responsibly.</p>	<p>Managers should be given the power and autonomy to make choices that are advantageous to the business and its stakeholders, according to CG.</p>	<p>CSR is seen as a natural extension of stewardship, where managers take a long-term view of corporate social responsibility, acting in the best interest of society and future generations.</p>
<p>Resource-based view Theory Postulated by Jay Barney, 1991, emphasizes that a firm’s competitive advantage comes from its</p>	<p>RBV sees governance mechanisms as critical resources that can enhance a firm’s ability to manage its assets efficiently</p>	<p>CSR is viewed as an intangible resource that can enhance a firm’s reputation, stakeholder trust, and customer loyalty.</p>

internal resources and capabilities rather than external market conditions.		
Signaling Theory Postulated by Michael spence explains how the ‘signaler’ conveys information to ‘receiver’ in a context where there is information asymmetry.	Strong CG conveys to stakeholders and investors the legitimacy, transparency, and moral behavior of a company.	CSR activities represent a variety of stakeholders, including investors, customers, and employees, a company's commitment to sustainability, social responsibility, and ethical, and business practices.

Strong CG mechanisms can mitigate agency conflicts between management and shareholders, stakeholder interests are aligned with the company’s objectives leading to improved financial performance. CSR initiatives can also align management interests with shareholders’ interests, and enhance stakeholder satisfaction.

(b) The banking system in India

India's banking system is highly structured, consisting of regional rural banks (RRBs), public sector banks (PSBs), cooperative banks, private sector banks, as well as foreign banks. RBI is the central bank responsible for supervising, regulating, and controlling the Indian banking system. The RBI issues guidelines on various banking activities, conducts on-site inspections and off-site surveillance, manages monetary policy through tools including the reverse repo rate, Cash Reserve Ratio (CRR), and the repo rate, provides deposit insurance to depositors in case of bank failures, and mandates prudential norms. Small Finance Banks (SFBs) and Payments Banks in India are also fully controlled and regulated by the RBI. Both these types of banks are bound by rules, regulations, and monitoring by RBI as is the case with all other banks in India. LODR, Basel III Norms, Companies Act of 2013, RBI Act of 1934, Banking Regulation Act of 1949, and SEBI Act are a few of the significant laws and regulations for banks in India. The RBI Act of 1934, the Banking Regulation Act of 1949, the Companies Act of 2013, the SEBI Act, LODR, and the Basel III Norms are examples of frameworks. These frameworks assist in providing checks and balances so that the banks act in a responsible manner, which is also legal and transparent hence promoting financial stability and social wellbeing.

The Basel Committee on Banking Supervision (BCBS) is an international committee that was established in 1974 to create rules for banking supervision. The governors of the G10 central banks founded BCBS. It creates guidelines and standards for supervisors, such as the Basel Accords, which establish global benchmarks for market liquidity risk, stress testing, and bank capital sufficiency. Although not directly controlling Indian banks, the BCBS's standards significantly influence India's banking regulations, with the RBI adopting these standards and implementing them being a member of the BCBS. Basel Committee on Banking Supervision revised the corporate governance guidelines in 2015 [12].

(c) Regulations regarding corporate governance

Key Corporate Governance Requirements for Banks:

- Board of Directors: It must consist of a mixture of executive as well as non-executive directors and be independent.
- Board Committees: The Stakeholder Relations Committee, Nomination and Remuneration Committee, Audit Committee, and Risk Management Committee are all required.
- Audit Committee: Consists of non-executive directors and is in charge of monitoring internal controls, financial reporting, and legal and regulatory compliance.
- Risk Management Committee: oversees the bank's risk management program and ensures that risks are appropriately identified, evaluated, and mitigated.

Corporate Governance Guidelines by RBI:

- Fit and Proper Criteria: Banks must have a process for determining the 'fit and proper' status of directors.
- Disclosure Requirements: Banks must disclose information related to their corporate governance practices in their annual reports.

SEBI Listing Obligations and Disclosure Requirements (LODR):

- Applicability: Regulations apply to listed banks covering various aspects of corporate governance.
- Disclosure and Transparency: Disclosure of relevant insight to the public and shareholders in a timely and correct approach is a requirement for listed banks.

Companies Act, 2013:

- Applicability: Mandates various corporate governance practices such as board diversity, director responsibilities, and CSR.
- CSR Mandate: Banks that satisfy specific requirements have to invest in CSR initiatives at least 2% of their average net earnings and have to declare the specifics in their annual reports.

Public Sector Banks (PSBs) Specific Guidelines:

- Government Role: The government holds a significant ownership stake, and the appointment of directors often involves government nominations.
- Board of Directors: The board structure includes representatives from the government, RBI, and professional directors.

Private Sector Banks:

- Ownership and Management: Private banks have more flexibility in board appointments and management structures.
- Additional Oversight: RBI may impose additional governance requirements on private sector banks.

Basel III Guidelines:

- Risk Management: Basel III guidelines emphasize the need for strong corporate governance practices to manage risks effectively.

(d) Corporate social responsibility regulations

As regards CSR, different types of banks have different obligations. Banks incorporated as companies under the Companies Act – mostly private banks- have to follow the mandatory provisions of CSR under the Companies Act and public sector banks have freedom to comply

with RBI circulars. Nevertheless, RBI has not mandated any specific instructions to the banks about the implementation of these CSR initiatives. Circulars are only advisory.

RBI issued a circular dated 21st December 2005 on Donations by banks.

- Allows voluntary contributions from all Scheduled Commercial Banks, including PSBs, up to 1% of their previous year's profit.
- Limits donations to Rs. 5.00 lakhs for loss-making banks.

The RBI issued recommendations on December 20, 2007, outlining the part banks should play in CSR, non-financial reporting, and sustainable development.

- Advises banks to implement sustainable development plans with Board approval and publish non-financial reports every year.
- Encourages banks to stay updated on developments and adjust their strategies accordingly.

Under the Companies Act:

The introduction of Section 135 of the Companies Act, 2013, which requires CSR activities for businesses, including banks registered under the Companies Act, has increased the profile of CSR in Indian banks. Banks with a net value of at least Rs 500 crores, a turnover of ₹1,000 crores, or a net profit of Rs 5 crores in a given financial year are required to dedicate at least two percent of their average net earnings over the preceding three financial years to CSR projects.

Banks typically focus on education, healthcare, rural development, financial inclusion, environmental sustainability, skill development, and promoting gender equality through their CSR activities. Monitoring and reporting are required, and many banks use their CSR funds to enhance financial inclusion by promoting digital literacy, opening bank accounts in rural areas, and offering micro-loans to underserved sections of the population.

(e) Corporate Social Responsibility and financial performance

Numerous studies have examined at the relationship between CSR and financial performance, and most of them have found it to be beneficial. Several empirical investigations have established that CSR undertakings enhance organizational performance regarding ROA, ROE and Tobin's Q [13], [14]. Moreover, research indicates that there is a reciprocal relationship between CSR and financial performance, with profitability having an impact on CSR disclosure [14]. This research establishes a moderate positive relationship between CSR and financial performance using factor analysis and multivariate regression analysis.

(f) Corporate Governance and Corporate Social Responsibility

There has been a growing understanding of the connection between CG and CSR as two mutually dependent concepts. CG involves the management of CSR policies and the two concepts are designed to accommodate both the corporate objectives and the stakeholders' needs [15]. Research shows that good CG is a prerequisite for the development of sound CSR initiatives [16]. Both have similar goals such as the main goal of CSR is to promote CSR while the purpose of anti-corruption is to prevent corruption in business [15], [16]. In developing countries, there is increasing recognition of the relationship between CG and CSR, transcending a compliance CG to voluntary CSR benchmarks [16]. While some people have

suggested that CSR is a part of CG, others try to reverse this situation [17]. According to the previous studies, it was found that there is a mutual relationship between CG and CSR, where higher CG is associated with higher CSR [16], [18]. Recent legal reforms in India have created a research interest in the effect of CG attributes on CSR disclosures with some attributes such as chairman-CEO duality and female board representation exerting considerable influence on CSR expenditures [19].

Social responsibility is frequently associated with enterprises that are more effectively managed [20]. Additionally, [21] and [3] demonstrated that corporate social responsibility is significantly and positively influenced by CG. Good corporate governance, then, must include making sure companies act morally and responsibly toward all stakeholders, society, and the environment.

Overall, CG and CSR are increasingly viewed as complementary aspects of responsible business practices.

(g) The mediating role of Corporate social responsibility

The relationship between CG, CSR, and financial performance has been extensively discussed in the literature to date. The outcomes show that CG affects FP both directly and indirectly through CSR. The current study also pointed out that effective CG increases the level of ethical and responsible behaviour, thus improving CSR practices [22],[3], [20]. Further, CG enhances CSR responsiveness and thus has a positive impact on financial performance [21], [23]. There is a positive correlation between the organization's sustainable and responsible social and environmental undertakings and business profitability and performance [7], [24], [25]. CSR has been found to mediate the relationship between CG and financial performance to some extent. Studies have shown that CG improves CSR, which in turn improves financial performance [17].

Further theoretically speaking the relationship among CG, CSR, and financial performance on the basis of Stakeholder theory, Resource-based view theory, and stewardship theory can be summarized:

- **Stakeholder theory** argues that well-governed companies act ethically and align business practices with stakeholder interests, promoting sustainability. Success requires balancing economic, social, and environmental values, not just focusing on profits.
- **RBV theory** views good CG as a valuable resource that supports CSR practices, leading to improved financial performance.
- **Stewardship theory** posits that the board of directors prioritizes maximizing company performance over self-interest, contributing to good governance and value creation.

In essence, these theories provide different perspectives on how CG enhances CSR and, ultimately, FP and firm value.

As indicated by the previous discussions, raising CG can maximize CSR initiatives and improve CSR results, which will ultimately raise FP. As a result, it is reasonable to offer the following hypotheses on CSR's mediating role in the relationship between CG and FP:

- H1: CG is positively associated with CSR.
- H2: CSR is positively associated with financial performance.
- H3: CSR mediates the relationship between CG and financial performance

(h) Conceptual” Model

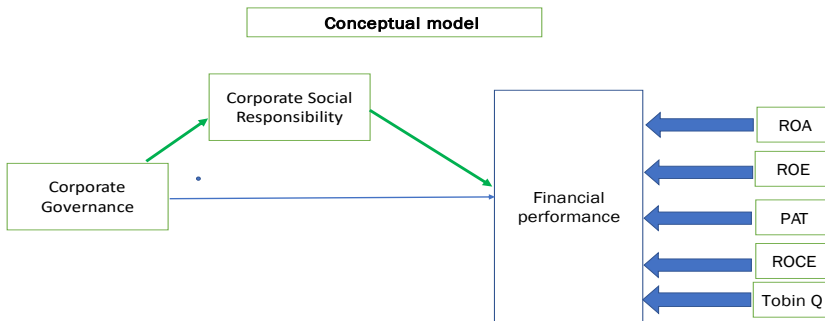


Figure 1: Proposed Conceptual model

3. Methodology

- (a) Sample:** This study used purposive sampling to determine the suitability of specific characteristics for banking sector companies listed on the BSE, companies with CG and CSR reports, and companies publishing annual financial reports on their websites or on the BSE website. Thus, in total, there are 26 banking companies in the sample.
- (b) Data and variables:** The Centre for Monitoring the Indian Economy (CMIE) maintains the Prowess database, which provides financial data to the banking organizations in the sample. The data has been collected from 2013-14 to 2022-23 for a period of 10 years. For measuring the CG – the independent variable- instead of depending on individual components of CG a comprehensive index has been prepared by extracting the data through content analysis from annual reports of the respective banks for the said period of 10years. Details are presented in Table 2 and include binary values for each component's CG suitability or otherwise.

Table 2: Components for preparing the CG index (CGI)

Legal aspects	Board efficiency aspects
Adverse Auditor’s report	Total no of directors
Default in payments of tax	No of independent directors
Dispute in payment of tax	No of Women directors
Related party transactions disclosure	No of board meetings held
Whether shareholders’ grievance committee is formed	Attendance at the board meeting

Whether CSR committee is formed	Audit committee independence
Whether E voting information is given in the AGM notice	Audit committee meetings held
Whether company has disclosed policies to prevent sexual harassment	Busyness of Directors
	CSR committee’s independence
	CEO Duality

3.b.1. For measuring CSR – the mediating variable - also a comprehensive index has been prepared based on the 12 disclosure components given in Schedule VII of the Companies Act. Binary code is given for the existence or otherwise of the said component in the annual report of the banks. Also, a value ‘0’ is given if CSR expense is incurred less than 2%, ‘1’ is given if spent 2%, and a value ‘2’ is given if the CSR expenses incurred by the company are more than 2%. Thus, the summation of all these components is the CSR index (CSRI) utilized to find the impact of CSR on FP.

3.b.2.Measurement of FP variables – Dependent variable

Table 3: Financial Performance variables

Variables	Symbol	Units	Data Source	Literature source
Profit “after Tax	PAT	INR Million	Prowess	
Return on Assets	ROA	%	Prowess	[32], [33],[34], [35], [36], [37]
Return on Equity	ROE	%	Prowess	
Return on Capital Employed	ROCE	%	Prowess	
Tobin Q	Tobin’s Q	Times	Balance sheet analysis	[32],[34],[38], [39],[40]

Tobin’s Q is computed by the formula (Total assets + market capitalisation— book value of equity) / total” assets.

(c) Method

Causal mediation analysis is done using SAS 9.4 (proc Casualmed). In the analysis, Structural Equation Modeling (SEM) is used, which is a more comprehensive and robust method for testing mediation. SEM simultaneously assesses both the direct and indirect paths, along with other relationships in the model. SEM provides not only estimates of the indirect effect but also accounts for the relationships between all variables in the model, making it more flexible and accurate for complex models. Bootstrapping, which is often used to assess mediation (sensitivity analysis), has been shown to be more accurate in SEM since it is not predicated on the assumption of a normal distribution of the indirect effects.

4. Results and discussion

(a) Descriptive statistics

Table 4: Descriptive Statistics of Analysis Variables

Variable	N	Mean	Std Dev	Minimum	Maximum
PAT	255	4.44	12.87	-58.99	25.74
ROE	255	0.64	18.74	-76.14	28.58
ROCE	255	0.79	9.93	-45.32	18.75
ROA	255	0.31	1.35	-5.75	4.45
Tobin's Q	255	1.06	0.18	0.83	2.05
CSR	255	3.73	2.66	0.00	12.00
CG	255	14.53	5.22	0.00	25.00

- The FP measures (PAT, ROE, ROCE, ROA) show a wide range of profitability, with some firms showing significant losses (negative values) while others report strong positive returns.
- Tobin’s Q values are generally close to 1, indicating that firms’ market values are approximately equal to their asset replacement costs.
- CSR and CG practices vary widely, with some firms excelling in these areas and others scoring poorly.

(b) Mediation analysis

Table 5. Summary of Estimation of Causal Mediation Effects “of Corporate Social Responsibility Between Corporate Governance and Company Financial Performance

Obs	Causal Effect	PAT		ROE		ROCE		ROA		Tobin's Q	
		Esti mate	P> Z	Esti mate	P> Z	Esti mate	P> Z	Esti mate	P> Z	Esti mate	P> Z
1	Total Effect	0.282	<.001	0.214	0.004	0.229	0.001	0.254	<.001	0.331	<.001
2	Controlled Direct Effect (CDE)	0.075	0.267	0.018	0.754	0.011	0.839	0.061	0.348	0.239	0.010
3	Natural Direct Effect (NDE)	0.075	0.267	0.018	0.754	0.011	0.839	0.061	0.348	0.239	0.010
4	Natural Indirect Effect (NIE)	0.206	<.001	0.195	<.001	0.217	<.001	0.192	<.001	0.091	0.050

Obs	Causal Effect	PAT		ROE		ROCE		ROA		Tobin's Q	
		Estimate	P> Z	Estimate	P> Z	Estimate	P> Z	Estimate	P> Z	Estimate	P> Z
5	Percentage Mediated	73.18	0.0005	91.35	0.0045	95.02	0.0018	75.83	0.011	27.63	0.0474

Table 5 provides an overview of the causal mediation effects of CSR as a mediator between different measures of FP (Tobin's Q, Return on Capital Employed [ROCE], Return on Assets [ROA], Return on Equity [ROE], Profit After Tax [PAT], and Return on Equity [ROE]) and CG. Through CSR, the mediation analysis divides the overall impact of CG on FP into direct and indirect impacts. An examination of each part is provided below.

4.b.1.Total Effect

The Total Effect represents the overall impact of CG on company FP, encompassing both the direct effect and the mediated effect through CSR. Across all FP measures, the total effect is positive and highly significant, indicating that improved CG generally leads to better FP.

4.b.2.Controlled Direct Effect (CDE)

The Controlled Direct Effect isolates the direct impact of CG on FP, independent of CSR:

- The CDE estimates for all variables are insignificant ($p > .05$), except for Tobin's Q (CDE = 0.2396, $p = 0.0010$). This suggests that CG has little to no direct effect on PAT, ROE, ROCE, and ROA after accounting for CSR. However, it has a significant direct impact on Tobin's Q, indicating that some part of a company's market valuation (Tobin's Q) is influenced directly by governance, independent of CSR activities.

4.b.3.Natural Direct Effect (NDE)

Because of the same estimates, the Natural Direct Effect and the Controlled Direct Effect in this case are the same:

- The direct effects for PAT, ROE, ROCE, and ROA remain statistically insignificant ($p > .05$), implying that the role of CG in driving these FP metrics is not direct but occurs largely through CSR.
- For Tobin's Q, the direct effect is significant (0.2396, $p = 0.0010$), reinforcing the earlier observation that CG affects Tobin's Q independently of CSR.

4.b.4.Natural Indirect Effect (NIE)

The Natural Indirect Effect quantifies CSR's mediating effect, or the extent to which CSR accounts for the relationship between CG and FP. A strong mediating function of CSR in connecting CG to FP is indicated by the NIE, which is highly significant for all variables ($p < .05$). These findings suggest that a significant portion of CG's indirect effect on FP occurs through CSR.

4.b.5.Percentage Mediated

The Percentage Mediated shows the proportion of the total impact of CG on FP that is explained through CSR. These results indicate that CSR mediates the vast majority of the effect of CG on PAT, ROE, ROCE, and ROA (ranging from 73% to 95%), meaning that CSR plays an essential part in explaining the relationship between corporate governance and these financial outcomes. However, for Tobin's Q, only 27.63% of the total effect is mediated by

CSR, suggesting that factors outside CSR significantly influence the impact of CG on market valuation.

Summarising:

- More than 70% of the effect is mediated in the case of PAT, ROE, ROCE, and ROA, where CSR plays a critical mediating role in the relationship between CG and FP.
- The direct impact of CG on FP (excluding CSR) is generally insignificant for all financial metrics except for Tobin's Q, indicating that the direct relationship between CG and market valuation remains significant even after accounting for CSR.
- The relevance of socially responsible practices in obtaining better financial outcomes is highlighted by the considerable role that CSR plays in mediating the relationship between CG and FP.

(c) Mediation Analysis Results: Summary of Model Parameter Estimates

Table 6: Summary of Model Parameter Estimates: Outcome and Mediator Model

Obs	Variable	Estimate	P
1	CG-->PAT	0.07567	0.2875
2	CSR-->PAT	0.3498	<.0001
3	CG-->ROE	0.01854	0.7992
4	CSR-->ROE	0.3317	<.0001
5	CG-->ROCE	0.01139	0.8741
6	CSR-->ROCE	0.3688	<.0001
7	CG-->ROA	0.06148	0.3944
8	CSR-->ROA	0.3268	<.0001
9	CG-->Tobin's Q	0.2396	0.0010
10	CSR-->Tobin's Q	0.1550	0.0327

Obs	Variable	Estimate	P
11	CG --> CSR	0.5903	<.0001

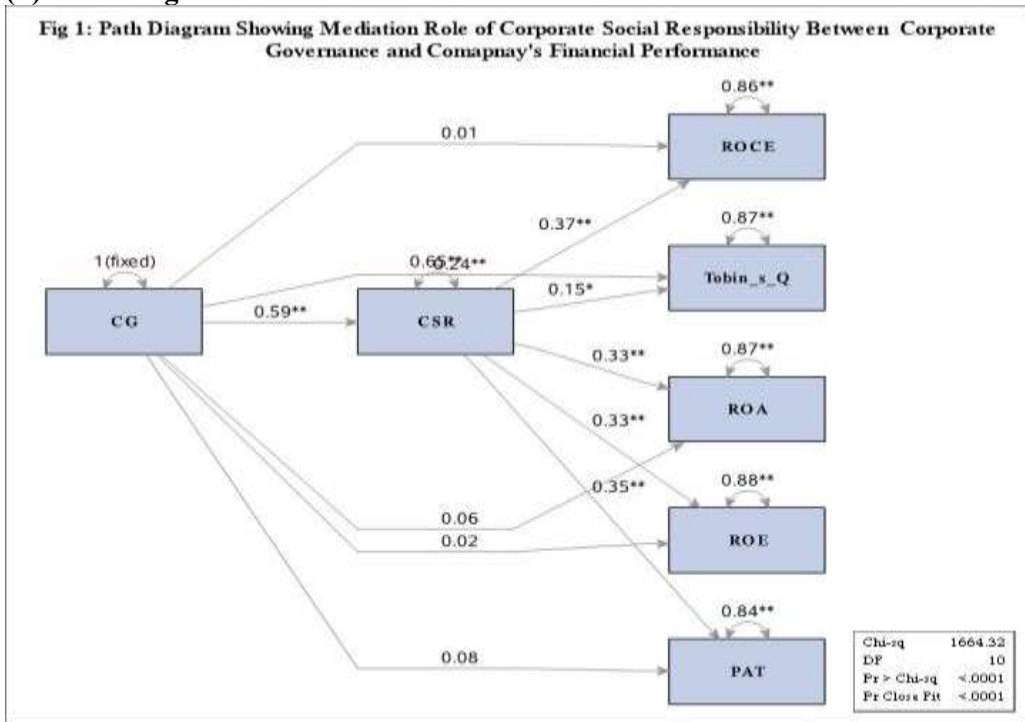
Table 6 provides the estimates and significance levels from the mediation analysis between CG, CSR, and various measures of FP. The mediation research examines both the direct as well as indirect impacts of CG on FP through CSR.

Table 6 shows that CG has no statistically significant direct impact on financial performance parameters such as PAT, ROE, ROCE, or ROA. This suggests that CG alone does not have a meaningful direct impact on profitability, as measured by PAT, CG alone does not directly affect ROE, CG alone is not a strong predictor of how efficiently a company uses its capital to generate returns and CG alone does not have a direct impact on how well a company utilizes its assets to generate returns. On the other hand, Tobin's Q, which measures market valuation in relation to asset replacement costs, is significantly positively impacted by CG. This suggests that better CG directly influences a company's market valuation, independent of CSR activities.

CSR has a strong and major impact on all FP measures (PAT, ROE, ROCE, ROA, and Tobin's Q), showing that CSR is a key driver of better financial outcomes.

CG significantly influences CSR, which, in turn, positively affects FP. Thus, much of CG's effect on FP is indirect and occurs through CSR.

(d) Path Diagram – Mediation role



4.d.1. The diagram shows that the direct effects of CG on FP indicators such as ROA, ROE, and PAT are weaker or insignificant. However, CSR mediates these relationships and has a stronger effect on FP outcomes. The strong path between CG → CSR (0.59**) and CSR → financial outcomes (e.g., CSR → ROE: 0.33**) highlights CSR's role as the primary channel through which CG enhances FP. While CG has a direct impact on Tobin's Q, its influence on other financial outcomes is largely indirect and occurs through CSR. This highlights the importance of CSR as a mechanism through which good CG enhances FP.

(e) Model Fit Statistics:

4.e.1. The bottom-right corner of the path diagram provides fit statistics for the model:

Chi-square: 1664.32

Degrees of freedom (DF): 10

p-value: < .0001, indicating a good model fit.

Pr > Close Fit: < .0001, further supporting the model's adequacy.

(f) Full Mediation vs. Partial Mediation

From the analysis and path diagram provided (with CG as the independent variable, CSR as the mediator, and various FP metrics as the dependent variables), we can identify where partial mediation and full mediation occur by looking at the significance of both the direct and indirect effects.

Full Mediation:

PAT (Profit After Tax):

- Direct path: CG → PAT (0.08, not significant).
- Indirect path: CG → CSR (0.59**) and CSR → PAT (0.35**).

ROA (Return on Assets):

- Direct path: CG → ROA (0.06, not significant).
- Indirect path: CG → CSR (0.59**) and CSR → ROA (0.33**).

ROE (Return on Equity):

- Direct path: CG → ROE (0.02, not significant).
- Indirect path: CG → CSR (0.59**) and CSR → ROE (0.33**).

The direct path between CG and PAT, CG and ROA, and between CG and ROE is insignificant, while the indirect path through CSR is significant in all these cases. This implies full mediation in the relationship between CG and PAT, CG and ROA, and also between CG and ROE.

Partial Mediation:

Tobin's Q (Market Valuation):

- Direct path: CG → Tobin's Q (0.15*, significant).
- Indirect path: CG → CSR (0.59**) and CSR → Tobin's Q (0.15*).

Both the direct effect and the indirect effect (through CSR) are significant. This indicates partial mediation, meaning CG affects Tobin's Q both directly and through CSR.

ROCE (Return on Capital Employed):

- Direct path: CG → ROCE (0.01, not significant).
- Indirect path: CG → CSR (0.59**) and CSR → ROCE (0.37**).

The direct effect of CG on ROCE is weak and insignificant, while the indirect effect through CSR is significant. Although the direct path is close to zero, the significant mediation suggests that partial mediation might be present, but the relationship is largely explained by the indirect path through CSR.

5. Conclusion

Therefore, the primary objective of this research is to conduct empirical research on how CG affects FP and how CSR acts as a mediator in the relationship between CG and FP for Indian banks. The goal of this research is to gain a thorough understanding of the role that CG plays in improving FP in the direction of sustainability for Indian banks. The outcomes support the hypothesis that CSR acts as a vital channel through which good CG translates into improved FP.

- **Corporate Governance and Financial Performance:** CG has a significant positive impact on **Tobin's Q** (market valuation), but its direct effects on other FP indicators like **PAT, ROE, ROCE, and ROA** are generally weak and insignificant. This suggests that CG does not directly drive overall profitability or efficiency, except in terms of market valuation.
- **Corporate Social Responsibility as a Mediator:** In order to mediate the relationship between CG and FP, CSR is essential. Through CSR, CG has significant indirect influence on FP indicators, particularly for **PAT, ROE, ROCE, and ROA**, for which CSR accounts for a significant amount of the impact (73% to 95%). This highlights that much of the value CG creates for a firm's FP is realized through its impact on CSR initiatives. The outcomes are in accordance with the findings of [17].

This outcome is consistent with stakeholder theory, which posits that CSR engagement can result in increased productivity among internal stakeholders and the preservation of positive reputation values among external stakeholders [26]. Consequently, it is likely to affect the company's primary objective, which is to optimize its financial performance.

- **CSR's Direct Impact:** All of the FP indicators are significantly, favorably, and strongly impacted by CSR. This indicates that companies with greater CSR engagement tend to perform better financially, demonstrating the importance of socially responsible practices in driving profitability, efficiency, and market valuation.
- **CG's Influence on CSR:** Corporate Governance significantly influences CSR, suggesting that well-governed companies are more likely to engage in socially responsible activities. This relationship is pivotal in explaining how CG indirectly leads to better FP through enhanced CSR practices. The research supports [27]'s claim that corporate governance signifies a company's commitment to CSR, improving its reputation, and [28] assertion that it effectively executes CSR, demonstrating the close relationship that exists between CSR and corporate governance.
- **Overall Impact:** The combination of strong CSR engagement and good governance leads to improved financial outcomes. The findings emphasize the importance of integrating

CSR into the corporate governance framework to realize financial benefits and create value for stakeholders.

This study contributes by developing an empirical model that expands the existing literature on how CG influences FP through the mediating role of CSR, offering insights into the mechanism by which CG improves FP. Owners, directors, managers, and legislators could find the contribution to be extremely interesting. These findings may have implications for stakeholders seeking to understand the relationship between financial success and broader corporate behaviors.

6. Limitations and future research

The Bombay Stock Exchange banks that are the subject of this study may not accurately represent the variety of sectors and industries. It also suggests that future studies should consider different contextual factors and consider a qualitative approach to better understand CSR and accountability.

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