THE IMPACT OF MANAGERIAL DISCRETION ON CORPORATE SOCIAL RESPONSIBILITY AND FIRM PERFORMANCE

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Abstract

Managerial discretion, although an important element of strategic decision-making in corporate social responsibility (CSR), has not yet received due attention from researchers. Prior studies have focused on the impact of overall CSR spending on firm performance, showing mixed results. This study can be considered unique as it analyses total and sector-specific CSR expenditures undertaken by firms. Using panel data analysis, we examine the role of managerial discretion in strategic CSR decisions and their impact on firm performance. Building on extant literature, we hypothesize that managerial discretion, demonstrated in spending beyond the legally mandated CSR budget and sector-specific CSR decisions, will positively impact firm value (Tobin's Q) and free cash flow. Our analysis of five years of data on 340 large listed firms confirms these hypotheses, showing a positive impact of managerial discretion on both firm value and free cash flow. Also, from a governance perspective, board independence influences free cash flow. While previous studies have suggested mixed or limited effects of CSR on firm performance, our findings suggest that managerial discretion significantly enhances firm performance through strategic CSR decisions. To our knowledge, this is the first attempt to investigate the specific effects of managerial discretion on firm performance.

Keywords: Managerial Discretion, Corporate Social Responsibility, Corporate Governance, Board Independence, Free Cashflow, Firm Performance

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1. INTRODUCTION

In recent years, corporate social responsibility (CSR) has become a central component of many firms' business strategies (Matten & Moon, 2020). Traditionally, CSR involves utilizing profits for societal good in areas aligned with shareholder interests. But today, management researchers as well as practitioners acknowledge that CSR can have significant strategic relevance (strategic CSR), which suggests that CSR spending leads to both social impact and at the same time positive outcomes for the corporation involved (Latapí Agudelo et al., 2019; Tata & Matten, 2016; Vishwanathan et al., 2020). This move towards strategic CSR signifies a critical balance between social responsibility and firm performance.

As in every other corporate function, managers play a central role in the CSR function as they identify relevant sectors for CSR engagement that align with strategic goals, develop programs that deliver shared value (Porter & Kramer, 2011), and decide on the allocation of resources for CSR (Talan & Sharma, 2019). In prioritizing investments with dual outcomes — social value and return on investment — managers ensure the long-term sustainability of CSR efforts. Although recent research has recognized the influence of CSR spending on various aspects of firm performance including financial outcomes, brand reputation, and employee behaviour (Albinger & Freeman, 2000; Barko et al., 2022; Borghesi et al., 2014; Breuer et al., 2018; Menon & Kahn, 2003; De Silva & De Silva, 2021; Low & Siegel, 2020), the impact of managerial discretion in CSR decisions remains underexplored and lacking empirical evidence. Previous studies have also produced inconclusive results concerning the relationship between CSR spending and financial performance (Gillan et al., 2021; Panwar et al., 2022). Given this background, the central research question of this study is:

RQ: Does managerial discretion in CSR decision-making impact firm performance, specifically in terms of financial outcomes?

We attempt to address this research gap by exploring the influence of managerial discretion on firm performance, considering both overall and sector-specific CSR spending.

The rest of the paper is structured as follows. The theoretical framework is presented in Section 2. This is followed by a presentation of the research design and qualitative analysis of previous studies in Section 3 and a description and discussion of the results in Section 4. The conclusion is outlined in Section 5.

2. LITERATURE REVIEW AND HYPOTHESES DEVELOPMENT

2.1. Conceptual framework

2.1.1. Evolution of strategic corporate social responsibility

Corporate social responsibility has evolved from a set of philanthropic obligations that go beyond legal requirements (Smith, 2001) to a strategic option with the potential to create shared value for firms and society (Heslin & Ochoa, 2008). This transition resulted in "embedded CSR" (Rasche et al., 2017), where social responsibility becomes an integral part of a company's operations, strategy, and culture. In contrast, "peripheral CSR" refers to activities separate from core business functions and serves primarily as marketing or public relations initiatives (Du et al., 2010). The progression from peripheral philanthropy to a strategic imperative (Gautier & Pache, 2015) marks a fundamental shift in how companies approach social responsibility. This transformation, pioneered by companies like The Body Shop and Patagonia, has been adopted by large corporations such as Unilever (Lawrence et al., 2019). Research suggests that cross-sector collaborations and multi-stakeholder initiatives (Matten & Moon, 2020; Maignan & Ralston, 2002; Ramesh et al., 2021; Seitanidi et al., 2014), as well as strategic CSR in specific sectors, strengthen a company's social commitment (Heslin & Ochoa, 2008).

Strategic CSR strengthens a firm's relationships with shareholders by enhancing its legitimacy among stakeholders and regulators (Deephouse et al., 2017; Durand et al., 2019; Sheth & Babiak, 2010) by meeting their expectations, including legal compliance, workplace safety, environmental stewardship, transparency, and product safety over traditional philanthropic activities (Carroll & Brown, 2018). Carroll's (2016) CSR pyramid structures these responsibilities hierarchically: economic, legal, ethical, and philanthropic, with economic viability as the base. Porter and Kramer (2011) further advanced this concept by proposing that social value creation can complement economic objectives through creating shared value.

2.1.2. Significance of managerial discretion in strategic corporate social responsibility

Given the vastness of social issues, managerial discretion gains significance in choosing and shaping various CSR practices, from sustainable resource utilization and carbon reduction to ethical employment and value creation for underserved markets (Carroll & Brown, 2018; Matten & Moon, 2020; Mason et al., 2017; Prahalad & Hart, 2002). A firm's CSR decisions often reflect managerial mindsets (Swanson, 2008), as managers may pursue CSR initiatives driven by personal values, profit objectives, stakeholder demands (Waldman & Siegel, 2008), or shared value creation (Porter & Kramer, 2011). Given that CSR would be most effective when aligned with specific industry contexts (Heslin & Ochoa, 2008), managers who decide on the overall allocation and sectoral distribution of the CSR budget could naturally be expected to seek necessary discretion in their CSR choices.

The upper echelons theory (Hambrick & Mason, 1984) highlights the influence of chief executive officer values on CSR decisions, with transformational leadership positively linked to corporate social performance (Waldman et al., 2006). Middle management also plays a key role in implementing CSR (Wooldridge et al., 2008), with managerial perceptions of stakeholder expectations shaping CSR strategies (Crilly et al., 2012). CSR is a collaborative effort involving managers, employees, civil society, and consumers (Acquier et al., 2011). Despite its importance, research on managerial discretion in CSR remains limited (Soltani et al., 2015). This study explores managerial discretion in CSR expenditure and sector choices focusing on spending beyond mandatory levels as a measure of strategic commitment.

2.1.3. Corporate social responsibility and firm performance

The relationship between CSR and firm performance continues to generate mixed outcomes in academic literature. Gillan et al. (2021) documented mixed findings across studies, with some demonstrating positive correlations while others yielded inconclusive results. A meta-analysis by Wang et al. (2016) confirmed a positive relationship between CSR and financial performance, noting stronger effects in developed economies. Research by Borghesi et al. (2014) found that companies with superior operating performance and free cash flow achieved higher environmental, social, and governance (ESG) scores, a correlation further supported by research by Gao and Zhang (2015) and Ferrell et al. (2016), which highlight the importance of ESG ratings for corporate success.

Chang et al. (2019) documented larger value increases for firms with higher ESG ratings, complementing the findings of Edmans (2011) and Lins et al. (2017), who link CSR initiatives to performance outcomes including value creation, improved operating efficiency, and higher profits, particularly during periods of declining corporate trust. Cornett et al. (2016) identified positive correlations between ESG scores and return on equity in the banking sector. Bolton and Kacperczyk (2020) found that firms adhering to ESG/CSR principles benefit from reduced capital costs, enhancing profitability. Firms that implement robust sustainability practices achieve higher performance with lower risk profiles (Eccles et al., 2014). Sustainability investments also enhance employee satisfaction, potentially improving productivity and profitability (Edmans, 2011). Banerjee et al. (2020) found that innovative companies that effectively reduce resource waste benefit the most from environmental responsibility, especially in high-emission, market-competitive industries with strong institutional structures.

Despite prevalent positive associations, some studies report neutral or negative outcomes. Investments in CSR may not yield immediate financial returns. For example, Margolis et al. (2009) found statistically insignificant relationships between social initiatives and financial performance. Although extensive literature supports the positive impact of CSR on performance, further research is needed to identify its conditions.

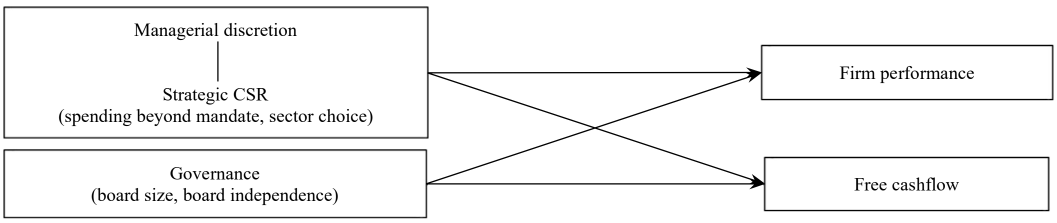
2.1.4. The role of governance in corporate social responsibility

Corporate governance has a crucial role in integrating CSR with social and environmental goals. The board of directors serves as an important mechanism for aligning CSR initiatives with organizational goals. Vinjamury (2021) demonstrates that board size and board independence significantly impacts firm performance, with larger and more independent boards providing improved governance oversight. In this context, improved governance oversight may help align CSR expenditures with the firm's corporate goals. Governance extends beyond the board structure to encompass the stakeholder engagement and accountability mechanisms needed to optimize CSR performance (Fassin, 2012).

Integrating CSR into governance frameworks can generate social and financial benefits. Orlitzky et al. (2013) found that robust governance often leads to financial outperformance through responsible decision-making practices. Johnson et al. (1999) found links between corporate governance structures and improved corporate social performance, particularly in terms of diversity and product quality. Bear et al. (2010) demonstrated a positive correlation between gender-diverse boards and CSR engagement, while Harjoto and Jo (2011) showed that board independence and institutional ownership enhanced firm value through CSR initiatives. Mallin and Michelon (2011) highlighted the positive impact of independent directors, female board members, and CSR committees on corporate social performance.

These findings underscore governance's multifaceted role in enhancing CSR outcomes. Integrating CSR into governance structures yields benefits for society and corporate performance, emphasizing the importance of board diversity, stakeholder engagement, and robust accountability mechanisms. The conceptual model in Figure 1 below provides the theoretical background discussed so far in this article.

Figure 1. Theoretical framework: The impact of managerial discretion and governance on firm performance



2.2. Development of hypotheses

Managers, as shareholder agents, prioritize CSR activities that enhance financial performance. Vishwanathan et al. (2020) distinguish between strategic and traditional CSR, arguing that strategic CSR activities positively impact firm performance through the following mechanisms: 1) firm reputation, 2) stakeholder reciprocation, 3) risk mitigation, and 4) innovation capacity. Managers typically allocate resources based on strategic effectiveness rather than legal minimums, as increased CSR allocations can signal a commitment to social responsibility and positively impact firm value. Tobin's Q, widely employed in CSR research, provides a market-based measure of firm performance (Gillan et al., 2021; Servaes & Tamayo, 2013; Vomberg et al., 2015; Edeling & Fischer, 2016). Therefore, the first hypothesis can be formulated as:

H1: Expenditures above the established corporate social responsibility budget have a positive impact on firm value (Tobin's Q).

Strategic CSR spending, recognized for its performance-enhancing characteristics, typically receives shareholder support, fostering increased trust in management. This trust may translate into greater managerial autonomy, measurable by free cash flow, which indicates the available cash flow beyond working capital and fixed asset requirements. Managers exercise discretion in CSR budget allocation, considering factors such as core business alignment, strategic advantage, cost reduction, and long-term stakeholder impact (Porter & Kramer, 2006). Carroll's (1991) CSR pyramid identifies different levels of responsibility to stakeholders, including shareholders, employees, and the environment. Firms that strategically allocate CSR funds to operationally significant sectors typically receive shareholder approval, reduce agency problems, and increase firm value. However, CSR expenditures yield varying returns: investments in human resources (healthcare, employment) may generate faster financial returns than environmental initiatives, which, although crucial for long-term sustainability, may not provide immediate financial returns. Therefore, the next hypotheses are formulated as follows:

H2a: Increased corporate social responsibility spending on human resources positively impacts free cash flow.

H2b: Increased spending on environmental causes negatively impacts free cash flow.

From a strategic perspective, board composition and independence significantly influence managerial discretion oversight, particularly regarding CSR decisions. Independent and larger boards demonstrate enhanced capacity for management monitoring, ensuring alignment between discretionary CSR decisions and broader corporate objectives (Vinjamury, 2021). Research shows that the strategic nature of CSR activities depends on their alignment with financial performance and long-term goals (Johnson et al., 1999; Harjoto & Jo, 2011). Larger boards, benefiting from diverse expertise, typically provide superior guidance for CSR expenditures that complement business objectives, improving decision-making processes and financial performance (Bear et al., 2010). This alignment promotes accountability and strategic resource allocation, significantly influencing firm value. Therefore, the third hypothesis is:

H3: Larger boards have a positive impact on firm value, as measured by Tobin's Q.

Board independence plays a crucial role in ensuring robust management oversight. Independent boards, free from potential conflicts of interest, demonstrate enhanced capacity to grant financial autonomy to managers, enabling discretionary CSR budget allocations that align with ethical and financial objectives (Mallin & Michelon, 2011). Research shows that independent boards facilitate strategic decision-making, potentially improving free cash flow and firm performance (Orlitzky et al., 2013). This study anticipates that the relationship between board independence and managerial discretion in CSR spending will reflect this positive dynamic. The fourth hypothesis is formulated as follows:

H4: Greater board independence correlates positively with free cash flow.

3. RESEARCH METHODOLOGY

For this study, we considered the top 500 companies listed on the National Stock Exchange (NSE) of India (Nifty 500 Index). It can be noted that CSR is mandatory for firms in India, which is considered an extreme form of implicit CSR (Carroll & Brown, 2018; Sharma & Singh, 2021). As per Section 135 of the Companies Act, 2013, every company has to contribute at least 2% of the average net profit earned during the three immediately preceding financial years towards social development. India has thus become the first country to make CSR a part of the law (Prasad, 2014). Due to this mandatory nature, companies report their CSR spending, including the sectors they choose to spend. We sourced this data on CSR spending along with data on operational expenditure and firm performance from publicly available sources. Following the classification provided by Awasthi et al. (2019), we excluded banks and other regulated firms from the list of top 500 companies. Prior studies (e.g., Hopt, 2013) argue that the corporate governance of banks and other financial institutions differs considerably from general corporate governance. For financial institutions, the scope of corporate governance goes beyond the shareholders (equity governance) to include debtholders, insurance policyholders and other creditors (debt governance). From the perspective of the supervision of financial institutions, debt governance is the primary governance concern. Similarly, Hopt (2021) argues that banks are unique, and so is the corporate governance of banks and other financial institutions. Hopt (2021) argues that the special governance of banks and other financial institutions is firmly embedded in bank supervisory law and regulation. As the governance structures of financial firms are impacted by supervisory law and regulation, financial companies are excluded from the analysis. The five-year data for the remaining 340 companies constitute the panel data for our analysis. A list of the main industries included in the study is included in Table A.1 (see Appendix).

The Companies Act, 2013 (No. 18 of 2013) states 12 sections (see Table A.2 in Appendix for details on all 12 sections) towards which a profitable Indian firm could allocate the CSR budget. Each year firms are expected to allocate at least 2 percent of their average profits of the past three years towards any of the 12 sections. We considered the overall spending of the 340 companies towards the CSR budget for testing *H1*. We analysed how spending more than the stipulated budget affected firm performance. We hypothesized that spending more than mandated by law would signal the strategic relevance of that CSR spending for the firm. We argue that where the CSR allocation contributes to the business goals of the firm it is likely that firms spend beyond stipulations to reap the business benefits of CSR along with the intended social impact.

For testing *H2* we considered only four of the 12 sections proposed by the law and avoided sections wherein the spending could be mediated through a government agency such as contribution to military and defence, contribution to the Prime Minister's relief fund, etc. Out of the four sectors considered, three related to human development, and the fourth was related to environmental protection. We list the four sectors along with their scope as suggested by Schedule VII (see Section 135. Corporate Social Responsibility) of the Companies Act, 2013, below:

1) eradicating hunger, poverty, malnutrition, and sanitation, and making available safe drinking water (*SEC1*);

2) promoting education, including special education and employment enhancing vocation skills especially among children, women, elderly, and the differently abled and livelihood enhancement projects (*SEC2*);

3) promoting gender equality, empowering women, setting up homes and hostels for women and orphans; setting up old age homes, day-care centres, and other facilities for senior citizens and measures for reducing inequalities faced by socially and economically backward groups (*SEC3*);

4) ensuring environmental sustainability, ecological balance, protection of flora and fauna, animal welfare, agroforestry, conservation of natural resources and maintaining the quality of soil, air, and water (*SEC4*).

4. RESULTS AND DISCUSSION

A description of the variables used in the study is provided in Table 1, and their summary statistics are presented in Table 2. Our objective was to assess the impact of CSR spending beyond the mandatory amount on firm value, as measured by Tobin's Q, and to evaluate the effect of sector-wise CSR spending on free cash flow while controlling for factors such as board size and board independence.

Table 1. Description of variables

Variable	*What it represents*	*How it is measured*
TQ	Adjusted Tobin's Q	(Total assets + market capitalisation-book value of equity - deferred tax liability) / total assets.
FCF	Free cash flow	Net cash flow from operations, investing and financing activities.
Bsize	Board size	Number of directors on the board.
Ind_per	Board independence	Number of independent directors on the board / Number of directors on the board.
SEC1	CSR Section 1	Money allocated towards CSR Section 1.
SEC2	CSR Section 2	Money allocated towards CSR Section 2.
SEC3	CSR Section 3	Money allocated towards CSR Section 3.
SEC4	CSR Section 4	Money allocated towards CSR Section 4.
Spending_more	Spending above the mandated minimum	Whether the firm spent more than the mandated minimum CSR budget.
Log_assets	Logarithm of firm total assets	Natural logarithm of total assets

Source: Authors' elaboration.

Table 2. Summary statistics

Variables	*N*	*Mean*	*Median*
TQ	1580	3.6266010	2.7015616
FCF	1580	65.7910759	10.0000000
Bsize	1580	10.8822785	11.0000000
Ind_per	1580	0.4978229	0.5000000
SEC1	1580	296.1227658	0
SEC2	1580	506.1369873	75.4050000
SEC3	1580	30.3453734	0
SEC4	1580	144.5443418	0
Spending_more	1580	0.4379747	0
Log_assets	1580	10.5275827	10.4299291

Source: Authors' elaboration.

To address the potential issue of multi-collinearity among the independent variables, we conducted a correlation analysis, the results of which are presented in Table 3. The results show that the independent variables used in the analysis are not highly correlated, with the highest correlation coefficient being 0.48 between *SEC2* and *SEC4*. As an additional measure to assess the presence of multi-collinearity, we performed a variance inflation factor (VIF) analysis. The results indicate that none of the VIF values were greater than 1.72, which is within the generally accepted limits. Hence, multicollinearity does not pose a problem for the analysis.

Table 3. Correlation matrix

Variables	*TQ*	*FCF*	*Bsize*	*Ind_per*	*SEC1*	*SEC2*	*SEC3*	*SEC4*	*Spending_more*	*Log_assets*
TQ (Beta)	1	0.01313	-0.1305	0.01355	0.00702	0.00177	0.10048	0.0166	-0.02544	-0.27619
TQ (p-value)		0.602	< 0.0001	0.5906	0.7803	0.9441	< 0.0001	0.5096	0.3121	< 0.0001
FCF (Beta)		1	-0.01922	0.01976	0.01927	-0.0113	-0.0284	-0.2560	-0.03963	-0.01409
FCF (p-value)			0.4453	0.4324	0.4441	0.6527	0.2586	< 0.0001	0.1153	0.5756
Bsize (Beta)			1	-0.19913	0.15868	0.17455	0.11225	0.13497	0.1157	0.43941
Bsize (p-value)				< 0.0001	< 0.0001	< 0.0001	< 0.0001	< 0.0001	< 0.0001	< 0.0001
Ind_per (Beta)				1	-0.0222	0.05007	-0.0061	0.07432	0.02488	-0.0516
Ind_per (p-value)					0.3779	0.0466	0.8078	0.0031	0.3231	0.0403
SEC1 (Beta)					1	0.48474	0.34959	0.36367	0.03611	0.33243
SEC1 (p-value)						< 0.0001	< 0.0001	< 0.0001	0.1514	< 0.0001
SEC2 (Beta)						1	0.27016	0.48799	0.11088	0.46368
SEC2 (p-value)							< 0.0001	< 0.0001	< 0.0001	< 0.0001
SEC3 (Beta)							1	0.40124	0.06033	0.17936
SEC3 (p-value)								< 0.0001	0.0165	< 0.0001
SEC4 (Beta)								1	0.1034	0.28173
SEC4 (p-value)									< 0.0001	< 0.0001
Spending_more (Beta)									1	0.18801
Spending_more (p-value)										< 0.0001
Log_assets										1

Note: Pearson correlation coefficients, N = 1580, Prob > |r| under H_0: Rho = 0.

Source: Authors' elaboration.

The objective of the regression analysis is to examine the relationship between a dependent variable (*TQ*) and a set of independent variables (*Bsize, Ind_per, SEC1, SEC2, SEC3, SEC4, Spending_more,* and *Log_assets*).

Table 4 presents the results of the regression analysis examining the relationship between firm value (measured using Tobin's Q) and various independent variables, including the effect of CSR expenditure above the mandatory amount, CSR expenditure by sector, board size, board independence, and other control variables.

Table 4. Regression analysis using fixed effects model

Variable	*Tobin's Q (Estimate)*	*Tobin's Q Prob > |t|*	*FCF (Estimate)*	*FCF Prob > |t|*
Intercept	15.58302	< 0.0001	-1523.39	0.3679
Bsize	-0.00143	0.9585	-0.41126	0.9945
Ind_per	-0.77422	0.2255	2564.365	0.0722
SEC1	1.707E-06	0.9658	0.30654	0.0082
SEC2	0.000069	0.2097	0.495136	0.0006
SEC3	0.000287	0.2401	1.846626	0.0225
SEC4	-0.00006	0.4198	-2.71686	< 0.0001
Spending_more	0.195275	0.0862	-308.951	0.3462
Log_assets	-1.07393	< 0.0001	43.18134	0.7858

Source: Authors' elaboration.

The results showed a significant positive relationship between spending more than the mandated CSR budget and firm value, as measured by Tobin's Q. Other studies in the Indian context (Panwar et al., 2022; Garg & Gupta, 2020; Laskar & Maji, 2016; Mitra, 2021) that reported a positive impact of CSR on firm value did not consider Tobin's Q as a measure of firm performance. It is important to note that the impact of mandatory CSR spending on Tobin's Q can be influenced by a number of other factors, such as the specific CSR activities being undertaken, the amount of spending etc. Also, if a firm has to spend a significant portion of its profits on CSR activities, it can reduce its profits and increase its costs, potentially affecting Tobin's Q negatively. On the other hand, mandatory CSR spending can also enhance a firm's reputation and image and could also lead to abnormal stock market returns (Arendt et al., 2010; Panwar et al., 2022). Our findings suggest that more strategic CSR budget spending, reflected in spending above the minimum required budget, can positively impact firm value (Tobin's Q). Our argument is not in any way intending to state that mindless overspending on CSR enhances firm value. We would intend to state the opposite that a strategic treatment of CSR engagement by a firm that compels it to go beyond the minimum mandated CSR budget would result in superior firm value. Therefore, managers could align CSR spending with the firm's business goals, create synergies between CSR and firm strategy, and thus increase firm value.

The results also showed a positive correlation between funds allocated to specific social welfare sectors (*SEC1*, *SEC2*, and *SEC3*) and board independence with free cash flow. This suggests that superior CSR allocation can create trust among stakeholders, reducing the agency problem. The agency problem refers to the conflict of interest between a firm's managers ("agents") and the firm's owners ("principals"). The agency problem arises because managers may put their own interests above those of the owners, which can lead to inefficiencies and misaligned incentives.

Free cash flow, on the other hand, refers to the cash that a firm has available after it has paid all of its operating and capital expenditures. A high level of free cash flow can be a positive indicator of a firm's financial health because it gives the firm the flexibility to make investments, pay dividends, or repurchase shares. The agency problem and free cash flow are related in that a high level of free cash flow can increase the potential for the agency problem. If a firm's managers have access to large amounts of free cash, they may be tempted to use it for their own benefit, such as pursuing pet projects or increasing their own salaries, rather than using it for the benefit of the firm's owners. This can lead to a misalignment of incentives between the managers and the owners and exacerbate the agency problem. However, the results of the current study indicate that managers' discretion in choosing strategically important sectors to engage in CSR reduces the agency problem, as evidenced by increased free cash flow.

In addition, active board monitoring and shareholder activism can help ensure that the interests of owners are represented and that the agency problem is addressed while providing greater autonomy for management. The positive relationship between increased board independence and free cash flow might indicate that more freedom for the management would also mean a requirement for higher monitoring and scrutiny by an independent board. Thus, the results indicate that by engaging in CSR activities aligned with business strategies, a firm can demonstrate its commitment to social responsibility, which may be viewed positively by shareholders and investors. However, the study did not find a significant relationship between free cash flow and board size.

The findings provide insights into the importance of strategic CSR spending and its impact on firm performance and free cash flow. It is important for managers to consider the sectors to which they allocate their CSR budget, as some sectors may lead to positive results while others may not. In addition, the results highlight the importance of board independence in ensuring effective resource allocation and monitoring of management decisions.

5. CONCLUSION

This study examined the relationship between a firm's strategic CSR choices and its performance. The findings indicate that spending more on CSR activities than the legally mandated budget can positively impact a firm's value, highlighting the strategic relevance of CSR spending. Additionally, money allocated to strategically chosen sectors for CSR engagement, combined with greater board independence, was positively correlated with free cash flow, suggesting that strategic CSR allocation helps gain stakeholder trust and reduce the agency problem. The results emphasize that CSR involvement should be viewed as a strategic activity, not merely a compliance obligation. Firms should identify sectors that are strategically aligned with their business operations and engage in CSR efforts that enhance firm performance. Importantly, financial allocations to CSR should be determined based on their strategic impact rather than being limited by legal mandates. Metrics that measure both social and financial impact will enable more informed decisions regarding future CSR allocations.

In this study, we analysed panel data covering 340 firms over five years. It may be noted that the study was carried out in a single-country context and would have corresponding limitations. Expanding the study to include multiple countries or regions could provide a broader understanding and validate the findings in different economic and cultural contexts. Additional research could delve deeper into the mechanisms through which CSR impacts firm performance, such as examining the role of managerial discretion and distinguishing between strategic CSR and other forms of social responsibility. Researchers could also explore the impact of CSR initiatives in sectors beyond those covered in this study. In addition, future research could focus on how CSR commitments create shared value through market reconfiguration, value chain adaptation, and ecosystem building, as suggested by Porter and Kramer (2011).

Another potential area for future research could be the alignment of CSR expenditures with a firm's business objectives, particularly by examining specific sectors that are more closely aligned with a firm's strategy. Studies could also explore the key factors contributing to effective strategic CSR. Given that firms may have varying levels of expertise in both formulating and executing CSR strategies, studying how firms mature in their CSR strategy formulation and the role of external agency collaborations in implementing these strategies could provide valuable insights Where firms collaborate with external agencies to implement CSR strategies, research could focus on evaluating the selection, management, and outcomes of such collaborations. Understanding how firms can effectively design, manage, and monitor such external collaborations would contribute to strategic CSR knowledge and practice.

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APPENDIX

Table A.1. List of main industries included in the study

1. Air-conditioners & refrigerators	21. Fertilisers	41. Paper & newsprint
2. Aluminium & aluminium products	22. Gems & jewellery	42. Pesticides
3. Bakery products	23. General purpose machinery	43. Plastic films & flexible packaging
4. Beer & alcohol	24. Health services	44. Plastic furniture, floorings & miscellaneous items
5. Boilers & turbines	25. Hotels & restaurants	45. Plastic packaging goods
6. Business services & consultancy	26. Information technology-enabled services	46. Plastic tubes, pipes, fittings & sheets
7. Cement	27. Industrial machinery	47. Readymade garments
8. Cloth	28. Inorganic chemicals	48. Refractories
9. Coffee	29. Man-made filaments & fibres	49. Retail trading
10. Commercial vehicles	30. Media-broadcasting	50. Steel
11. Computer software	31. Media-print	51. Steel pipes & tubes
12. Conventional electricity	32. Miscellaneous electrical machinery	52. Storage batteries
13. Cosmetics, toiletries, soaps & detergents	33. Natural gas trading & distribution	53. Sugar
14. Cotton & blended yarn	34. Organic chemicals	54. Tobacco products
15. Diversified	35. Other automobile ancillaries	55. Two & three wheelers
16. Diversified machinery	36. Other chemical products	56. Tyres & tubes
17. Diversified manufacturing	37. Other construction materials	57. Vegetable oils & products
18. Drugs & pharmaceuticals	38. Other consumer goods	58. Wholesale trading
19. Engines	39. Other textiles	59. Wires & cables
20. Exhibition of films	40. Paints & varnishes	60. Paper & newsprint

Table A.2. Sectors specified in Section 135 of the Companies Act, 2013

Schedule	*Description*
I	Eradicating hunger, poverty & malnutrition, promoting preventive health care & sanitation & making available safe drinking water.
II	Promoting education, including special education & employment enhancing vocation skills, especially among children, women, the elderly & the differently abled & livelihood enhancement projects.
III	Promoting gender equality, empowering women, setting up homes & hostels for women & orphans, setting up old age homes, day care centres & such other facilities for senior citizens & measures for reducing inequalities faced by socially & economically backward groups.
IV	Ensuring environmental sustainability, ecological balance, protection of flora & fauna, animal welfare, agroforestry, conservation of natural resources & maintaining the quality of soil, air & water.
V	Protection of national heritage, art & culture including restoration of buildings & sites of historical importance & works of art; setting up public libraries; promotion & development of traditional arts & handicrafts.
VI	Measures for the benefit of armed forces veterans, war widows & their dependents.
VII	Training to promote rural sports, nationally recognized sports, Paralympic sports & Olympic sports.
VIII	Contribution to the Prime Minister's National Relief Fund or any other fund set up by the central government for socio-economic development & relief & welfare of the scheduled castes.
IX	The scheduled tribes, other backward classes, minorities & women.
X	Contributions or funds provided to technology incubators located within academic institutions, which are approved by the central government.
XI	Rural development projects.
XII	Slum area development.