



The impact of market orientation and corporate social responsibility on firm performance

Evidence from China

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Abstract

Purpose – The purpose of this paper is to investigate the joint effects of market orientation (MO) and corporate social responsibility (CSR) on firm performance.

Design/methodology/approach – Data were collected via a questionnaire survey of star-rated hotels in China and a total of 143 valid responses were received. The hypotheses were tested by employing structural equation modelling with a maximum likelihood estimation option.

Findings – It was found that although both MO and CSR could enhance performance, once the effects of CSR are accounted for, the direct effects of MO on performance diminish considerably to almost non-existent. Although this result may be due to the fact that the research is conducted in China, a country where CSR might be crucially important to performance given the country's socialist legacy, it nonetheless provides strong evidence that MO's impact on organizational performance is mediated by CSR.

Research limitations/implications – The main limitations include the use of cross-sectional data, the subjective measurement of performance and the uniqueness of the research setting (China). The findings provide an additional important insight into the processes by which a market oriented culture is transformed into superior organizational performance.

Originality/value – This paper is one of the first to examine the joint effects of MO and CSR on business performance. The empirical evidence from China adds to the existing literature on the respective importance of MO and CSR.

Keywords Market orientation, Corporate social responsibility, China, Business performance

Paper type Research paper

Introduction

As a central tenet of the modern marketing sciences, market orientation (MO) has been heralded by academics and practitioners for decades (see e.g. Felton, 1959; Kotler, 1984; Levitt, 1960; Webster, 1988). Although there is a growing body of empirical evidence to support the proposition that MO has positive impact on business performance (Narver and Slater, 1990), several researchers have reported non-significant or even negative effects for this association (see Kirca *et al.*, 2005).

Previous attempts to reconcile the disparity in the current research findings were made by either examining the moderating effects of environmental factors such as market turbulence and competition intensity (Slater and Narver, 1994; Greenley, 1995; Diamantopoulos and Hart, 1993), or identifying the mediators (Han *et al.*, 1998; Sandvik and Sandvik, 2003). Research findings using the former approach are so far non-conclusive (Gotteland and Boule, 2006). For instance, while Greenley (1995) and Harris (2001) found that a positive MO and business performance relationship exists only at low level of market turbulence, Diamantopoulos and Hart (1993) showed that the relationship exists at high level of market turbulence instead. In contrast, research on the mediators has generated more consistent results. For example, innovation has been consistently identified as a key mediator by several studies (Han *et al.*, 1998; Agarwal



et al., 2003; Kirca *et al.*, 2005). As only a handful research on the mediators has been conducted, however, our understanding on how MO can be transformed into superior organizational performance remains very limited (Sandvik and Sandvik, 2003).

In light of the above knowledge void, in this paper, we propose a new mediator, namely, corporate social responsibility (CSR) (see Figure 1). The choice of CSR as a mediator for further investigation was based on two interrelated facts. Firstly, like studies on MO-performance relationships, there is a growing body of management literature testifying the positive impacts of CSR on performance (see e.g. Maignan *et al.*, 1999; Luo and Homburg, 2007). Despite the fact that MO and CSR are both now generally recognized as important determinants of business performance, few studies have accounted for their joint effects on performance. Consequently, issues such as to what extent CSR may help market-oriented companies to achieve better business performance remains unclear. Secondly, tentative evidence in regards to the mediating role of CSR in MO-performance is given by a prior study (Maignan *et al.*, 1999) which shows that a firm's MO has positive effects on the level of CSR it displays. As the focus of Maignan and colleague's study (1999) is on the antecedents of CSR, they did not fully investigate how the presence of CSR affects the MO's impact on business performance and whether CSR is a link between MO and performance, which will be the subject of the current study.

Background and hypotheses

In one of the seminal papers on MO, Kohli and Jaworski (1990) used the term "market orientation" to mean the implementation of the marketing concept. More formally, they took an information-processing perspective and defined MO as "the organization-wide generation of market intelligence pertaining to current and future customer needs, dissemination of the intelligence across the departments, and organization-wide responsiveness to market intelligence". In contrast, Narver and Slater (1990) took a cultural perspective and defined MO as "the organizational culture that most effectively and efficiently creates the necessary behavior for the creation of superior value for buyers and, thus, continuous superior performance for the business." They posited that the content of an MO included three behavioral components – customer orientation, competitor orientation, and interfunctional coordination – and two decision criteria – long-term focus and profitability. Notwithstanding these differences in philosophical stance, Cadogan and Diamantopoulos (1995) demonstrated that the two definitions overlap considerably and can be integrated into a broader aggregate definition.

Building on the initial research by, *inter alia*, Kohli and Jaworski (1990) and Narver and Slater (1990), significant progress has been made in the conceptualization and measurement of MO and also in evaluating its impact upon organizational performance (Deshpande *et al.*, 1993; Kohli *et al.*, 1993; Subramanian and Gopalakrishna, 2001; Kirca

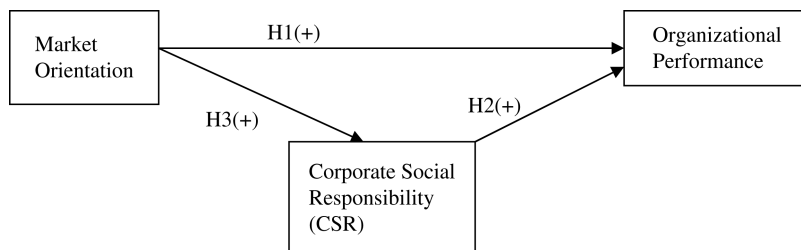


Figure 1.
Conceptual framework

et al., 2005). In the main, studies on the impacts of MO have demonstrated a significant and positive relationship between MO and organizational performance (see Narver and Slater, 1990; Jaworski and Kohli, 1993; Deshpande *et al.*, 1993; Kirca *et al.*, 2005) although a number of studies, mainly in non-US contexts, have suggested that the relationship could be context specific (see for example, Diamantopoulos and Hart, 1993; Greenley, 1995; Harris, 2001). As our study is conducted in China and most of the previous studies conducted in this setting have found a positive relationship between MO and organizational performance (Liu *et al.*, 2003; Sin *et al.*, 2003), we hypothesize that:

H1. MO has a direct impact on organizational performance.

As a broad concept, CSR has been given a variety of meanings. Along with the term of CSR, other terms such as corporate social responsiveness, corporate social performance, corporate citizenship and stakeholder management have also been extensively used (see Maignan *et al.*, 1999; Standwick and Standwick, 1998; Turban and Greening, 1996; Waddock and Graves, 1997; Shropshire and Hillman, 2007). Despite the existence of a variety of definitions, a review of literature suggests that the classification framework made by Carroll (1979) has received a wide acceptance. According to Carroll (1979), CSR is a multi-dimensional construct, consisting of four types of responsibilities: economic, legal, ethical and discretionary.

Economic responsibilities include the obligations for businesses to maintain economic wealth and to meet consumption needs. Legal responsibilities imply that businesses must fulfill their economic mission within the framework of legal requirements. Ethical responsibilities require that businesses abide by the moral rules defining appropriate behaviors in society. Discretionary responsibilities are tantamount to philanthropic responsibilities and reflect society's desire to see businesses contributing to its development.

Although earlier research on the CSR and business performance link have reported a negative relationship (e.g. Vance, 1975) or no relationship (e.g. Aupperle *et al.*, 1985), more recent studies on the linkage have provided more consistent empirical evidence showing a positive relationship between those two constructs (Russo and Fouts, 1997; Waddock and Graves, 1997; Maignan *et al.*, 1999; Luo and Bhattacharya, 2006). The discrepancy between the earlier and more recent studies might result from the fact that business environments are in a state of flux and the current business environments are becoming more favorable towards businesses that place an emphasis on CSR. For instance, a recent survey (Smith, 1996) found that 88 per cent of consumers in the study are more likely to buy from a company that is socially responsible. It is also reported that CSR has positive effects in helping companies to attract more talented and committed employees (Maignan *et al.*, 1999). To be consistent with recent empirical evidence demonstrating a positive impact of CSR on organizational performance (Maignan *et al.*, 1999), we hypothesize that:

H2. CSR has a positive impact on organizational performance.

In one of the seminal works on MO, Narver and Slater (1990) argued that being external oriented, as is the general implication of MO, a business would not only be sensitive to its external publics but also be anticipatory of their concerns. By taking a preemptive approach to address issues that are of customers concerns would help to make a company stand out from its competitor and to become more favorable choices as suppliers of products to customers (Narver and Slater, 1990). Therefore, in a business environment where external publics such as consumers have high expectations of

companies' CSR, arguably, market-oriented companies will be among the first to realize the importance of CSR and accordingly, implement CSR activities on route to achieve better business performance.

Before the economic reforms in the late 1970s, most Chinese enterprises were state-owned and provided extensive social programs to its employees such as free housing and medical cares. Although nowadays, many Chinese companies, especially those non-state-owned ones have shed off their welfare programs, the society at large still has high expectations of firms' social obligations. Operating under such environment, arguably, market-oriented companies in China will place great emphasis to CSR activities on route to achieve above average business performance. On the basis of the above arguments, we posit that:

H3. CSR is a key mediator in the MO-performance relationship.

Research method

Research context

To test our model, we collect data from hotel companies in China. The Chinese hotel industry provided a suitable context to test the hypotheses for the following reasons. First, the hotel sector in China is among one of the earliest sectors to open to foreign investment in the early 1980s and previous research in this context shows that the industry is moving towards a greater degree of MO. Furthermore, previous research also found that there is considerable variety across hotel groups in terms of MO and the level of CSR displayed (reference removed for review purposes), which creates the opportunity to explore the impact of these variables on organizational performance.

Data collection

To collect the data, a questionnaire together with a covering letter and a stamped return envelope was mailed to 600 hotels, randomly drawn from the *Directory of the Chinese Star-rated Hotels* (China National Tourism Administration, 1999), a Chinese tourism authority's official publication. The mail package was addressed to the hotels' managing director. Fourteen hotels could not be reached because of the incorrect addresses, resulting in an effective base of 586 hotels. With a cut-off date four weeks after the mailing, 143 completed questionnaires were received, resulting in a response rate of 24.4 per cent, a figure fairly comparable with those of both previous studies on MO (Slater and Narver, 1994; Greenley, 1995) and management research in China (Wang and Chow, 1999; Luo and Tan, 1998).

Following Armstrong and Overton (1977), non-response bias in the survey was assessed by comparing the early respondents (two weeks prior to the cut-off time) and late respondents' value on a number of key variables including MO and organizational performance. None of the differences was found to be significant, suggesting that the non-response was less likely to be a cause for concern in subsequent analysis.

Instrument development and refinement

As the differences between China's business environment and the Western economies' are well documented (Luo and Tan, 1998), to ensure the construct validity of our scales, we followed a four-stage iterative procedure, similar to the one adopted by Kohli *et al.* (1993), to refine the existing scales. The key features include expert review, focus group critique and two rounds of pretesting. The complete set of items for all the scales used in this study together with their sources is provided in the Appendix. All these scales

(except for the performance scale which is measured by seven point scales) are measured using five point Likert type scales, ranging from “not at all” to “very much”.

The MO instrument employed in the study was based on MARKOR scale developed by Kohli *et al.* (1993). As a result of the above scale refinement procedure, a number of modifications were made to the original 20 items of MARKOR to fit with the current research setting. The performance instrument is composed of three items asking the respondents to assess their companies’ results against their major competitors in terms of sales growth, return on equity (ROE) and overall performance. Our operationalization of the CSR construct is based on the scale developed by Maignan *et al.* (1999). As the original scale is composed of 29 items, which is deemed too long to use in our research setting, we decided to prune the items by first, asking a panel of ten Chinese hotel managers to comment on the relevancy of the existing conceptualization of CSR (Maignan *et al.*, 1999) in China’s business environment. All four dimensions were confirmed by the panelists as highly relevant, providing tentative evidence to the construct validity of this scale. After this procedure, we asked the same panelists to rank the relevancy of the items of the original CSR scale. For each of four components of the CSR construct, we then select one item that has the highest overall ranking to represent each component (two items received equal top ranking in the cases of ethical component and hence both were selected). As a result of the above two steps, we obtained a five-item scale for CSR.

All the measures discussed above were subjected to a purification process assessing their dimensionality, reliability and validity. Specifically, following guidelines suggested by Gerbing and Hamilton (1996), we obtained unidimensional measures using a sequential process of exploratory factor analysis (principal axis factoring with oblique rotation) and confirmatory factor analysis (maximum likelihood estimation using the covariance matrix as input in LISREL 8.72).

In order to achieve a suitable parameter estimate to sample size ratio (Bagozzi and Yi, 1988), we initially conducted the analysis by splitting the measures into two sets. In the first set, we examined only the MO scale. The second set contained all remaining scales. After eliminating several items because of cross loadings and contribution to poor model fit, we obtained excellent model fit in the two sets of items (see fit indexes for measurement models 1 and 2 in Table I).

After this, we created a partially aggregated three-item measure of MO. Specifically, we averaged across the items in the generation scale to create an observed score (GEN) for the generation latent variable. We constructed similar observed scores for the dissemination latent variable (DISS) and responsiveness latent variable (RESP). Then,

Models	χ^2 (df)	$\Delta\chi^2$ (Δ df)	<i>p</i>	RMSEA	NNFI	CFI
Measurement model 1 ^a	52 (35)		0.032	0.059	0.872	0.953
Measurement model 2	18.7 (25)		0.809	0.000	0.973	1.000
Full measurement model	48.7 (49)		0.486	0.000	0.951	1.000
Default structural model	48.7 (49)		0.486	0.000	0.951	1.000
Rival model 1 ^b	162.7 (52)	110.7 (3)	0.000	0.123	0.836	0.873
Rival model 2 ^c	107.2 (50)	57.2 (1)	0.000	0.090	0.863	0.934

Table I.
Fit measures for
measurement and
structural models

Notes: ^aMarket orientation scale only; ^bconstraining all the paths linking non-performance latent variables to zero; ^cconstraining the path between market orientation and corporate social responsibility to zero; ^dconstraining the path between corporate social responsibility and customer satisfaction to zero

we examined all scales together and the fit indexes for this full measurement model are very good (see Table I).

In Table II, we show the measurement properties of the variables and in Table III the correlations. All measures returns a composite reliability in excess of the threshold value of 0.60 recommended by Bagozzi and Yi (1988). In sum, the results of the measurement analysis process indicate that the purified scales show adequate evidence of convergent validity.

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Variable/item ^a	Mean	Standard deviation	Factor loading ^b	Variance extracted (%)	Composite reliability
<i>MO</i>					0.811
Generation	3.252	0.600	0.779	0.607	
Disseminate	3.148	0.724	0.730	0.533	
Responsive	3.380	0.603	0.786	0.618	
<i>CSR</i>					0.882
Item 1	3.810	0.798	0.780	0.608	
Item 2	3.662	1.017	0.801	0.648	
Item 3	3.690	0.818	0.877	0.770	
Item 4	3.613	0.815	0.747	0.558	
Item 5	3.225	0.829	0.670	0.498	
<i>Performance</i>					0.879
Overall	5.031	1.155	0.877	0.770	
ROE	4.669	1.192	0.841	0.707	
Sales	4.747	1.214	0.805	0.648	

Table II.
Summary statistics of
the measurement
analysis

Notes: ^aItem numbers refer to the item list in Appendix; ^ball parameter estimates are significant at the $p < 0.001$ level; MO = market orientation; CSR = corporate social responsibility

Variable	RESP	DISS	GEN	GROW	ROE	Overall	CSR5	CSR4	CSR3	CSR2	CSR1
Resp	1.00										
Diss	0.57	1.00									
GEN	0.61	0.57	1.00								
Grow	0.25	0.23	0.25	1.00							
ROE	0.26	0.24	0.26	0.68	1.00						
Overall	0.27	0.26	0.27	0.71	0.74	1.00					
CSR5	0.36	0.34	0.36	0.31	0.32	0.34	1.00				
CSR4	0.41	0.38	0.40	0.34	0.36	0.37	0.50	1.00			
CSR3	0.48	0.44	0.47	0.40	0.42	0.44	0.59	0.66	1.00		
CSR2	0.44	0.41	0.43	0.37	0.38	0.40	0.54	0.60	0.70	1.00	
CSR1	0.42	0.39	0.42	0.36	0.37	0.39	0.52	0.58	0.68	0.63	1.00

Notes: RESP = responsiveness to market intelligence; DISS = intelligence dissemination; GEN = intelligence generation; Satis = customer satisfaction; Grow = sales growth; ROE = return on equity; Overall = overall performance; CSR (1-5)= items 1-5 of corporate social responsibility scale. All correlations are significant at the $p < 0.001$ level except for the following. The correlations for DISS-ROE and DISS-Grow are significant at the $p < 0.05$ level while the correlation for DISS-Overall is non-significant

Table III.
Correlation matrix

Construct reliability was evaluated using the procedure suggested by Fornell and Larker (1981), including examining the parameter estimates and their associated *t* values and assessing the average variance extracted for each construct (Anderson and Gerbing, 1988). Discriminant validity was assessed in a two-step process. An initial level of discriminant validity was established by calculating the shared variances between each pair of constructs and verifying that it was lower than the average variance extracted of the individual constructs (Fornell and Larker, 1981). This was the case for each average variance extracted/shared variance scenario. Next, using a procedure recommended by Anderson (1987) and Bagozzi and Phillips (1982), pairs of constructs were assessed in a series of two-factor confirmatory factor models using LISREL. Each model was run twice, once constraining the phi coefficient to unity and once freeing this parameter. A chi-difference test was then performed. In all case, the model with the free parameter was found to be superior, providing evidence of the discriminant validity of the constructs.

Analysis and results

The hypotheses were tested by employing the structural equation modelling with a maximum likelihood estimation option. In the first two hypotheses, we predict a direct effect of MO (H1) and CSR (H2) on performance. To test the hypotheses, we estimate two models with performance as the only endogenous variable for both models and MO as the exogenous variable in Model 1 and CSR as the exogenous variable in Model 2. The results show that the effects of MO (*b* = 0.40, *p* = 0.000) and CSR (*b* = 0.57, *p* = 0.000) on performance are both highly significant, hence the support for *H1* and *H2*.

H3 predicts that CSR is a mediator between MO-performance. We followed the procedure recommended by Baron and Kenny (1986) in testing the existence of mediating effects:

- the independent variable must affect the dependent variable;
- the independent variable must affect the mediators;
- the mediators must affect the dependent variable; and
- when mediators enter the model, the contribution of a previously significant independent variable must drop substantially for partial mediation and become insignificant for full mediation.

To this end, we built on Model 1 by adding CSR as a new endogenous variable. The results of this new model (Model 3) were summarized in Table IV. Overall the model achieved a very good fit as all the fit indices are considered satisfactory. More specifically, the chi-square is 39.1 with 41 degrees of freedom and significant with

Path	Loading (standardised)	Significant	Fit index
<i>H1</i> (MO-performance)	0.01	ns	$\chi^2 = 39.1$ df = 41 RMSEA = 0.000 CFI = 1.000 NNFI = 0.96
<i>H2</i> (CSR-performance)	0.56	$p < 0.001$	
<i>H3</i> (MO-CSR)	0.69	$p < 0.001$	

Table IV.
Structural model
estimation results

$p = 0.56$. The RMSEA-value is 0.000, and the NFI and CFI values are 0.96 and 1.000, respectively, both exceeding the 0.95 threshold suggested by Hu and Bentler (1999).

Supports for *H3* were found when we compare the three research models as discussed above. In specific, Model 1 provides the evidence that MO affects business performance, satisfying the first condition set out by Baron and Kenny (1986). In Model 3, the direct path from MO to CSR is found to be highly significant ($b = 0.69, p = 0.000$), thus, the second condition is met. The third condition that the mediators must affect the dependent variable is also met since CSR is found to have positive effects on performance in Model 2. Finally, although MO is a significant independent variable in Model 1, when CSR (mediator) is added to the model, the effects of MO on performance (dependent variable) ceases to be significant (see Table IV), providing strong support for the full mediation of CSR on the effects of MO on performance.

Discussion

In this study we assess the joint effects of MO and CSR on performance. We found that although both MO and CSR could enhance performance, once the effects of CSR are accounted for, the direct effects of MO on performance diminish considerable to almost non-existent. Although this result may be due to the fact that our research is conducted in China, a country where CSR might crucially be important to performance given the country's socialist legacy, it nonetheless provides a strong evidence that MO's impact on organizational performance is mediated by CSR. The identification of this chain of events adds to the growing body of literature on the mediators of the MO and organizational performance relationship (Han *et al.*, 1998; Sandvik and Sandvik, 2003) and provides an additional important insight into the processes by which a market-oriented culture is transformed into superior organizational performance.

Consistent with Maignan *et al.* (1999), we found that MO is a key antecedent to CSR. The finding seems to be of particular significance due to the fact that our study was conducted in China, a setting significantly different from the US where Maignan and colleagues' study was conducted. Taken together, these two studies suggest market-oriented companies are actively engaging in CSR activities. This has important managerial implications, which will be discussed in the next section.

Last but not the least, our study provides yet another evidence to a growing body of literature demonstrating the benefits of CSR to businesses (Maignan *et al.*, 1999; Luo and Bhattacharya, 2006). Most of previous research studies supporting the benefits of CSR were carried out in developed countries and ours is probably the first studies to model the impact of CSR on organizational performance in the Chinese context. As such, we believe that our study has made a useful contribution to the debate about the merits of CSR to companies in emerging markets (Quazi and O'Brien, 2000).

Managerial implications

A key message of our study to managers is that although market-oriented companies are in a good position to achieve a superior organizational performance, managers must not take it for granted that efforts to increase the MO will automatically enhance organizational performance. To ensure that happens, they must heed the needs to develop, what we coined here, the "market orientation transformation competences" which are necessary to transfer a market-oriented corporate culture into superior performance outcomes. Our study suggests one of such competences is CSR, the attainment of which will lead to not only higher level of customer satisfaction but also higher profits. Other competences may include innovation (Han *et al.*, 1998), organizational learning, new

product development (Sandvik and Sandvik, 2003) and services quality (Ngai and Ellis, 1998) as suggested by previous studies.

Limitations and future research directions

The findings, conclusions and implications of this study are bounded by a series of limitations. These limitations suggest that caution is needed in interpreting parts of the study.

The first limitation is that cross-sectional data were used in this study. Consequently, the time sequence of the relationships between MO, CSR and organizational performance cannot be determined unambiguously. The results, therefore, might not be interpreted as proof of a causal relationship, but rather as lending support for a prior causal scheme. The development of a time-series database and testing of the MO relationships with those variables in a longitudinal framework would provide more insight into probable causation. Secondly, like many previous studies including those conducted in the Chinese settings, a subjective approach was used in this study to measure organizational performance. Although a strong correlation between subjective and objective measures has been identified by previous studies (Dess and Robinson, 1984; Pearce *et al.*, 1987), to what extent this can be generalized to China has not been formally assessed. Therefore, future research might consider using objective performance measures such as stock returns (Luo and Bhattacharya, 2006) to examine the framework we developed here. Finally, as this study is conducted in China, a country with an environment that might be significantly different from those found in developed countries and in other developing countries, the generalizability of our research findings needs to be treated with caution. Further research in other countries is therefore warranted.

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Appendix. Measurement scales

Market orientation (adapted from Kohli *et al.*, 1993)

Market intelligence generation

1. We are quick to detect changes in our customers' product preference
2. We are quick to detect fundamental shifts in our industry (e.g. competition, technology, regulation)
3. We periodically review the likely effect of changes in our business environment (e.g. regulation) on customers
4. We measure customer satisfaction systematically and frequently (Narver and Slater, 1990)

Intelligence dissemination

5. We have sufficient number of interdepartmental meetings to discuss market trends and developments
6. When something important happens to a major customer or market, the whole company knows about it in a short period
7. Data on customer satisfaction are disseminated at all level in this company on a regular basis

Responsiveness to intelligence

8. We periodically review our product development efforts to ensure that they are in line with what customers want
9. If a major competitor were to launch an intensive campaign targeted at our customers, we would implement a response immediately
10. The activities of the different departments in this business unit are well co-coordinated

Corporate social responsibility (Maignan et al., 1999)

1. We continually improve the quality of our products and services
2. Our company seeks to comply with all laws regulating hiring and employees benefits
3. We are recognized as a trustworthy company
4. Our sales persons and employees are required to provide full and accurate information to all customers
5. We give active support to programs with good social causes

Organizational performance (Jaworski and Kohli, 1993)

How do you rate your company's performance in relation to your main competitors on a seven point scale

1. Our sales growth is ____
2. Our return on equity is ____
3. Our overall performance is ____

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