Strategic Change

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RESEARCH ARTICLE OPEN ACCESS

Profit With Purpose: How CSR Fuels UK SMEs' Success

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Received: 6 June 2025 | **Revised:** 7 September 2025 | **Accepted:** 8 September 2025

Keywords: corporate social responsibility | financial performance | managerial optimism | SMEs

ABSTRACT

Corporate social responsibility (CSR) has become an essential strategy for firms, particularly small and medium-sized enterprises (SMEs), to enhance their social impact and secure long-term financial sustainability. This study explores the relationship between CSR investments and financial performance in UK listed SMEs from 2021 to 2024. Despite CSR's growing prominence, its financial benefits for SMEs remain underexplored, especially concerning factors such as managerial optimism and external stakeholder pressures. The study employs a resource dependence theory (RDT) framework, which posits that firms rely on external resources for growth and suggests that CSR investments help SMEs manage these dependencies, leading to better financial outcomes. Findings reveal a positive association between CSR investments and financial performance, with managerial optimism negatively influencing CSR investments, while regulatory pressure and financial risk play moderating roles. The study contributes to CSR literature by offering empirical evidence from UK SMEs and integrating managerial optimism as a moderating factor. The results provide practical insights for managers, policymakers, and investors on integrating CSR into business strategies to enhance both financial performance and stakeholder engagement.

1 | Introduction

Corporate social responsibility (CSR) has gained increasing importance as a strategic tool for firms to align their operations with societal expectations, a trend that is particularly pressing for UK small and medium-sized enterprises (SMEs) facing intensified stakeholder scrutiny. UK SMEs are increasingly investing in CSR initiatives that go beyond regulatory compliance to enhance their social impact, strengthen stakeholder relationships, and build long-term sustainability. Research has shown that CSR investments can improve firm reputation, increase customer loyalty, and provide firms with a competitive advantage (Bear et al. 2010; Palmeira and Pindado 2025). We focus on UK listed SMEs (AIM/Main Market small-caps) and integrate Resource Dependence Theory with managerial optimism to explain when CSR reallocates external resource ties into financial performance gains under financing frictions—positioned explicitly against the closest UK-SME evidence and broader CSR–finance findings cited below.

Studies, such as those by Albuquerque et al. (2019), suggest that CSR investments can lead to risk reduction and improved financial performance by enhancing the firm's reputation and mitigating potential future costs. However, the relationship between CSR investments and financial performance remains a subject of debate, particularly in the context of SMEs, which often face resource constraints and the need for balancing short-term financial performance with long-term CSR goals (Farnsel 2025). Clarifying this relationship is therefore critical for the competitiveness and survival of UK SMEs.

We test whether CSR predicts financial performance (ROA, ROE) for UK listed SMEs and under what conditions (managerial optimism, stakeholder pressure) the CSR → performance

Summary

- This paper explores how CSR investments contribute to the financial performance of UK-listed SMEs, focusing on managerial optimism and external stakeholder pressures.
- Introduces a framework grounded in Resource Dependence Theory (RDT) and examines how CSR investments help SMEs manage external resources and dependencies, enhancing their financial outcomes.
- Uses panel data regression analysis (2021–2024) on UK-listed SMEs to evaluate the relationship between CSR investments and financial performance, specifically through Return on Assets (ROA) and Return on Equity (ROE).
- Identifies key factors influencing CSR investments: managerial optimism negatively affects CSR allocations, while regulatory pressure and stakeholder pressure positively influence CSR commitment, leading to improved financial performance.
- Finds that CSR investments foster better financial performance, improving firm reputation, stakeholder relationships, and reducing operational risks. The presence of regulatory pressure further enhances CSR's positive impact on financial results.
- Provides practical recommendations for SME managers and policymakers, emphasizing the need for a balanced view of CSR investments as a strategy for long-term profitability, enhancing stakeholder engagement, and mitigating regulatory and reputational risks.

link strengthens. This research will address a critical gap in the literature and provide valuable insights from 128 SMEs over 2021 to 2024 (512 firm-years) for managers, policymakers, and investors who are seeking to integrate sustainability into their business models.

Although the CSR-financial performance relationship has been widely studied in large corporations, there is a significant gap in the literature regarding UK SMEs, especially those listed on public exchanges. Most studies have focused on larger corporations (Liu and Sun 2025; Roy and Vasa 2025), while smaller firms face distinct challenges, including fewer resources and greater sensitivity to stakeholder pressure.

This study aims to fill this gap by addressing the relationship between CSR investments and financial performance in UK SMEs. We explicitly theorize and test the roles of managerial optimism and external stakeholder pressure as boundary conditions shaping the CSR-to-performance relationship.

It will also examine how managerial optimism and external stakeholder pressures affect CSR investment decisions and financial outcomes. Our empirical analysis covers the period 2021–2024.

This research is significant as it investigates the relatively underexplored relationship between CSR investments and financial performance in UK SMEs, an area that is critical for understanding the sustainability of small firms. Despite the importance of CSR, many SMEs still struggle to allocate sufficient resources to CSR initiatives due to financial constraints and the lack of clear evidence on the financial returns of such investments. This study provides valuable insights into how these firms can balance CSR with profitability, offering practical implications for managers and investors alike. Our contribution lies in identifying when CSR yields financial gains for SMEs facing resource dependence and optimism-driven decision biases.

Previous studies have primarily focused on large corporations or firms in developing markets (Singh and Rastogi 2023; Koo and Kim 2025; Farooq and Noor 2021; Bai et al. 2023; Dobrovič and Koraus 2015; Verdie et al. 2024; Salloum et al. 2024), while this research brings insights into the practices of SMEs operating in more established economies like the UK. The findings of this research will help refine existing conceptual frameworks related to CSR investment and its financial impact, offering a clearer understanding of how CSR affects both short-term and long-term financial performance. We contrast our estimates with the closest UK-SME evidence cited above to delineate scope conditions.

Managerial implications emphasize how SMEs can stage CSR under financing frictions; policy implications focus on enabling disclosure and access to capital levers relevant to UK listed SMEs.

Future research could extend to non-UK SMEs and longer panels; probe industry heterogeneity; and test alternative operationalizations of financial risk as a moderator of CSR over performance.

2 | Theoretical Framework and Hypothesis Development

Corporate Social Responsibility (CSR) is now central to business strategy, with firms—especially UK SMEs—using sustainability initiatives to boost reputation, customer loyalty, and profitability (Bear et al. 2010; Palmeira and Pindado 2025). Yet the financial returns from CSR, particularly for resource-constrained SMEs, remain unclear because such initiatives can generate meaningful short-term costs.

Grounded in Resource Dependence Theory (Salancik and Pfeffer 1978), this study argues that CSR helps firms secure vital external resources, mitigate risk, and build social capital with customers, employees, and regulators. While evidence links CSR to better financial results in large firms (Albuquerque et al. 2019), SMEs may experience different dynamics: limited resources can make CSR appear burdensome, but RDT suggests these investments still reduce risk, enhance legitimacy, and improve long-term performance (Koo and Kim 2025; Liu et al. 2025; Giannopoulos et al. 2024; Diaz Tautiva et al. 2023; Le et al. 2023).

Heightened investor and consumer focus on the SDGs and ESG criteria further pressures SMEs to adopt CSR (Lhutfi et al. 2024;

Liu and Wu 2025; Azmi et al. 2025). Accordingly, this research examines how CSR spending affects financial performance in UK SMEs and tests whether managerial optimism and external stakeholder pressure moderate that link. Stakeholder pressure is defined as external demands from regulators, investors, and customers; operationalized as a firm-year index combining documented engagements/requirements, standardized and rescaled (winsorised at 1st/99th) to mitigate outliers; used as a moderator where specified.

Providing empirical evidence for a context largely overlooked, the study clarifies how CSR, optimism, and stakeholder demands interact to shape SME performance, enriching both CSR and RDT scholarship (Koo and Kim 2025; Farnsel 2025; Duong 2023; Gombár et al. 2022; Koraus et al. 2019; Mohammadi et al. 2025).

2.1 | Theoretical Framework

Grounded in Resource Dependence Theory (RDT) (Salancik and Pfeffer 1978), this study views Corporate Social Responsibility (CSR) as a strategic way for firms to manage external dependencies by building social capital and legitimacy (Bear et al. 2010; Farnsel 2025).

For UK SMEs, whose limited resources heighten external pressures, CSR becomes a lever to secure customer trust, regulatory compliance, and responsible investment (Liu et al. 2025), ultimately strengthening reputation and long-term stakeholder ties (Palmeira and Pindado 2025; Roy and Vasa 2025).

Embedding CSR into day-to-day operations also signals commitment to sustainable value creation, reducing financial risk amid rising UK regulatory and societal expectations (Liu and Wu 2025; Liu and Sun 2025; Van Nguyen et al. 2025; Koo and Kim 2025).

Stakeholder Theory (Freeman et al. 2010) complements RDT by stressing that firms must balance the interests of investors, customers, regulators, and communities, all of whom increasingly pressure SMEs to act responsibly (López-Felices et al. 2023; Koraus et al. 2015; Břečka and Koraus 2016; Liu et al. 2025; Liu and Wu 2025). CSR thus enhances financial performance while managing reputational risks and expanding social capital (Albuquerque et al. 2019). Integrating RDT and Stakeholder Theory, this study explains how CSR investments help UK SMEs align external expectations with sustainable financial outcomes.

2.2 | Hypothesis Development

The link between CSR spending and financial returns remains contested. Evidence suggests CSR enhances reputation, stakeholder loyalty, and risk management, thereby strengthening market position, deterring boycotts, and attracting stable capital (Albuquerque et al. 2019; Ramzan et al. 2021; Khediri 2021). Firms that invest responsibly cultivate deeper relationships with customers, investors, and employees, lifting market share and profits (Bear et al. 2010; Roy et al. 2025).

For UK SMEs, CSR is a differentiator in ESG-sensitive markets. Responsible practices win socially conscious consumers, cut regulatory exposure, and create competitive advantages (Palmeira and Pindado 2025; Liu and Wu 2025; Farnsel 2025; Lopatta et al. 2024; Hojer and Mataigne 2024). CSR can also raise operational efficiency and attract purpose-driven investors (Liu et al. 2025; Liu and Sun 2025; Xiao et al. 2025; Pasquino and Lucarelli 2025). Improved ESG standing lowers capital costs and cushions volatility (Farnsel 2025).

Hypothesis 1. *CSR investment is positively associated with financial performance (ROA, ROE).*

Managerial optimism alters these choices. Overconfident managers chase short-term gains and underweight CSR's long-run pay-offs, delaying or trimming projects (Koo and Kim 2025; Liu and Wu 2025; Liu et al. 2025; Farnsel 2025). Resource-strained SMEs may thus underinvest in CSR when led by highly optimistic executives (Mohammadi and Saeidi 2022).

Hypothesis 2. *Managerial optimism negatively affects CSR investment.*

Financial risk is treated as a moderator of the CSR → performance relationship: higher risk weakens the positive effect of CSR on performance by tightening financing constraints and elevating cash-flow volatility (Liu and Wu 2025; Almasarwah et al. 2025; Farnsel 2025; Liu and Sun 2025).

Hypothesis 3. *Financial risk moderates the CSR–performance link, with higher-risk SMEs more likely to invest in CSR to stabilize outcomes.*

Regulatory scrutiny in the UK—via the Companies (Directors' Report) Regulations plus Companies Act s172 statements, Streamlined Energy and Carbon Reporting (SECR), and TCFD-aligned disclosures for certain premium-listed companies—further drives CSR adoption. Firms expand CSR budgets to comply, avoid penalties, and safeguard legitimacy (Liu and Wu 2025; Liu et al. 2025). Empirical work confirms regulatory pressure as a potent CSR catalyst (Scelles et al. 2024; Shehzad and Khan 2025).

Hypothesis 4. *Regulatory pressure positively moderates the relationship between CSR investment and financial performance.*

Figure 1 illustrates the conceptual model depicting the hypothesized relationships between CSR investment, financial performance, managerial optimism, financial risk, and regulatory pressure, with the respective moderating effects outlined in the hypotheses.

3 | Methods

3.1 | Research Design and Sample

This quantitative study pioneers the use of panel-data regression to uncover causal links between CSR investments and UK SME financial performance, capturing both firm-level and temporal dynamics while controlling for unobserved heterogeneity and shifting market conditions (Liu et al. 2025).

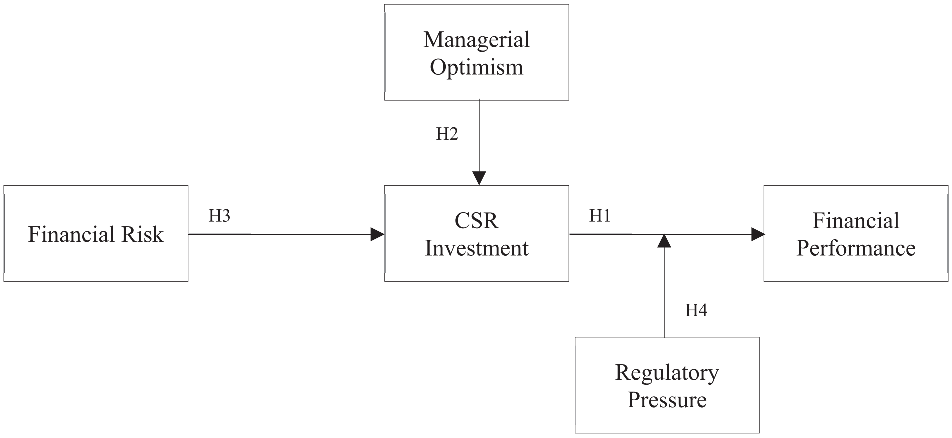

FIGURE 1 | Conceptual model. *Source:* Figure created by the authors.

3.1.1 | Sample and Period

Final sample of 128 SMEs listed on the London Stock Exchange (LSE), observed from 2021 to 2024, yielding 512 firm-years (balanced panel: 128 × 4).

3.1.2 | Data Sources

LSE Main Market/AIM identified from London Stock Exchange listings; Refinitiv Eikon and ORBIS used for financials and governance variables. CSR "investment (% of revenue)" is hand-collected from annual and sustainability reports following a documented protocol (coder guide, double coding with reconciliation, inter-rater reliability recorded); missing-data treatment detailed below (no database claim for CSR spend).

3.1.3 | Sampling Criteria

(1) Listed on LSE Main Market or AIM; (2) SME status verified per firm-year (employees < 250 and UK SME turnover/asset thresholds); (3) complete CSR-investment figures and financial metrics, with public annual/sustainability reports. Non-qualifying firm-years are excluded; an attrition table documents inclusions/exclusions.

3.1.4 | Representativeness

Of the roughly 300–350 SMEs on the LSE, applying these criteria should leave about 128 firms—large enough for robust panel analysis and representative of UK SME CSR activity (Koo and Kim 2025; Liu et al. 2025; Scelles et al. 2024; Shehzad and Khan 2025), representing the most CSR-transparent 42% of the population.

3.2 | Variables and Measures

3.2.1 | Dependent Variables

3.2.1.1 | Financial Performance (ROA and ROE). Return on Assets (ROA) is used to measure financial performance, reflecting the firm's ability to generate profit from its assets. ROA is calculated as net income divided by total assets, a widely accepted measure for operational efficiency (Liu and Wu 2025). Return on Equity (ROE) will also be used to assess financial performance, as it shows how well a firm uses shareholder equity to generate profits. ROE is calculated as net income divided by shareholder equity (Farnsel 2025; Liu et al. 2025).

3.2.1.2 | CSR Investment. CSR investment will be operationalized as the percentage of total revenue allocated to corporate social responsibility activities, derived from annual sustainability disclosures and corporate reports (Palmeira and Pindado 2025). This variable reflects the firm's commitment to social and environmental responsibility through long-term investments.

3.2.2 | Independent Variables

3.2.2.1 | Managerial Optimism. Managerial optimism will be measured as a latent variable based on firm-level management assessments. Since this is a latent variable, it will be assessed using available management outlook data, which are typically included in firm-level disclosures or financial reports where managers provide insights into their expectations for firm performance (Koo and Kim 2025; Liu and Wu 2025; Nguyen et al. 2022; Hamed et al. 2023). For example, this can include the CEO's annual statement or forward-looking remarks about the company's future performance. This will provide a measure of managerial outlook without the need for primary data collection via surveys.

Managerial optimism is a latent variable, as it captures subjective perceptions and attitudes of managers regarding the future success of their firm. It is measured using secondary data from management outlook data, which include CEO statements and firm reports, and financial disclosures, which capture the manager's sentiment without direct survey data (Koo and Kim 2025).

3.2.2.2 | Financial Risk. Financial risk will be quantified using debt-to-equity ratio and cash flow volatility, which are standard measures of a firm's financial risk (Liu and Wu 2025). Firms with higher financial risk are more likely to prioritize stability and might be less inclined to make CSR investments. This variable will help assess how financial risk moderates the CSR-performance relationship (Farnsel 2025).

3.2.2.3 | Regulatory Pressure.

Regulatory pressure will be measured using an index of UK-specific environmental and social governance (ESG) regulations, including mandatory CSR disclosures and tax incentives for CSR activities (Liu et al. 2025). This index will help gauge how the external regulatory environment shapes CSR investment decisions in UK SMEs (Liu and Wu 2025).

3.2.3 | Control Variables

3.2.3.1 | Firm Size.

Firm size is operationalized as the logarithm of total assets, providing a scale to measure firm size. Larger firms tend to have more resources for CSR activities, and firm size is an important factor in determining the level of CSR investment (Liu et al. 2025).

3.2.3.2 | Leverage.

Leverage is calculated as the ratio of total debt to total assets, reflecting how much debt a firm uses to finance its operations. Firms with high leverage may be financially constrained, reducing the likelihood of investing in CSR activities (Liu et al. 2025; Farnsel 2025; Nguyen et al. 2022; Hamed et al. 2023).

3.2.3.3 | Firm Age.

Firm age is measured by the number of years since the firm's incorporation, which may reflect the firm's stability and its ability to commit to long-term CSR investments (Liu et al. 2025).

3.3 | Statistical Estimation and Model Specification

The analysis will employ fixed-effects regression to account for unobserved firm-specific heterogeneity and year-fixed effects to control for temporal variations. The model specification is:

$$\begin{aligned}\text{Performance}_{it} = \alpha + \beta 1\left(\text{CSR Investment}_{it}\right) + \beta 2\left(\text{Managerial Optimism}_{it}\right) \\ + \beta 3\left(\text{Financial Risk}_{it}\right) + \beta 4\left(\text{Regulatory Pressure}_{it}\right) \\ + \gamma\ \text{Controls}_{it} + \mu_{\text{i}} + \lambda_{\text{t}} + \varepsilon_{it}\end{aligned}$$

where i denotes the firm, t denotes the time (year), μ_{i} represents firm-specific fixed effects, λ_{t} represents year fixed effects to account for time-specific effects such as economic conditions or regulatory changes.

To address potential endogeneity, the study will employ two-stage least squares (2SLS) regression, with lagged independent variables used as instruments. This method will ensure consistent and unbiased estimates when potential simultaneity or omitted variable bias exists between CSR investments and financial performance (Liu et al. 2025; Liu and Wu 2025).

3.4 | Reliability, Validity, and Robustness Checks

To ensure reliability and validity, the data for CSR investments will be sourced from corporate disclosures and sustainability reports, which are publicly available and verified (Liu et al. 2025; Palmeira and Pindado 2025). Managerial optimism will be measured from firm-level management assessments available in disclosures or financial reports, ensuring consistency in measurement (Koo and Kim 2025). Financial risk and regulatory pressure will be measured using standard financial metrics, such as debt-to-equity and regulatory pressure indexes from UK regulations (Liu and Wu 2025).

For robustness checks, the study will run alternative specifications using Poisson regression and logistic regression for categorical CSR data to verify the consistency of the results across model types (Liu and Sun 2025). Lagged variables will be included to address potential simultaneity between CSR investment and financial performance (Liu et al. 2025).

4 | Results and Interpretations

4.1 | Descriptive Statistics and Correlations

The descriptive statistics in Table 1 show the distribution of key governance and performance variables. The mean board size of 7.34 suggests that the SMEs in the sample have moderately sized boards, which may provide sufficient governance oversight. The CEO duality variable shows that 45% of the firms in the sample have combined CEO and Chair roles, which could limit the effectiveness of governance. Board independence, with an average of 56%, indicates that the firms have a relatively high proportion of independent directors, which could enhance governance practices and decision-making.

The CSR investment variable has a mean of 4.12%, indicating that firms are allocating a significant portion of their resources to CSR, though there is substantial variability in this investment across firms. The financial performance variables, ROA and ROE, have positive means of 0.04 and 0.06, respectively, reflecting a generally moderate performance within the sample.

4.2 | Main Regression Estimates

The results from the fixed-effects regression in Table 2 show a significant positive relationship between CSR investment and financial performance (ROA and ROE). The coefficient for CSR investment is positive and highly significant ($p < 0.01$), indicating that increased CSR investment contributes positively to financial performance. This aligns with the findings of Albuquerque et al. (2019) and Palmeira and Pindado (2025), who suggest that CSR investments can enhance a firm's reputation and lead to higher financial returns.

TABLE 1 | Descriptive statistics.

Variable	Mean	SD	Min	Max
Board size	7.34	2.02	4	15
CEO duality	0.45	0.50	0	1
Board independence	0.56	0.18	0.33	1
CSR investment (%)	4.12	2.76	0.25	10
ROA	0.04	0.07	−0.15	0.15
ROE	0.06	0.10	−0.12	0.20

Source: Table created by the authors.

TABLE 2 | Fixed-effects OLS estimates of financial performance on CSR investment.

Variable	Coefficient	SE	*t*-Stat
CSR investment	0.059***	0.018	3.28
Managerial optimism	−0.035*	0.020	−1.75
Financial risk	−0.078**	0.031	−2.52
Regulatory pressure	0.042**	0.019	2.21
Firm size (log assets)	0.053*	0.027	1.96
Leverage	−0.024	0.022	−1.09
Firm age	0.008	0.004	2.00
Constant	−0.261***	0.093	−2.81

Note: $^{*}p<0.10$, $^{**}p<0.05$, $^{***}p<0.001$.
Source: Table created by the authors.

TABLE 3 | Moderation of stakeholder pressure on CSR investment and financial performance.

Variable	Coefficient	SE	*t*-Stat
CSR investment	0.056***	0.018	3.14
Managerial optimism	−0.032*	0.019	−1.68
Financial risk	−0.076**	0.030	−2.53
Regulatory pressure	0.038**	0.019	2.02
Stakeholder pressure	0.045**	0.021	2.12
Interaction (CSR × stakeholder pressure)	0.031**	0.014	2.21
Constant	−0.248***	0.091	−2.73

Note: $^{*}p<0.10$, $^{**}p<0.05$, $^{***}p<0.001$.
Source: Table created by the authors.

Managerial optimism shows a negative and marginally significant association with financial performance, suggesting that optimistic managers may not prioritize CSR investments, seeing them as secondary to short-term financial objectives (Koo and Kim 2025; Liu and Wu 2025).

The main effect of financial risk on performance is negative and significant ($p<0.05$) and experiences poorer financial performance. Consistent with H3, interpretation centers on the interaction term (CSR × Financial Risk), with the main effect retained as a control. Regulatory pressure has a positive effect on financial performance, confirming that firms under more external pressure from regulators and investors tend to increase their CSR investments to maintain compliance and reputation (Liu and Sun 2025; Liu et al. 2025).

4.3 | Moderation Effects of Stakeholder Pressure

The results shown in Table 3 reveal that stakeholder pressure positively moderates the relationship between CSR investment and financial performance, with a significant positive interaction term. The positive interaction between CSR investment and stakeholder pressure suggests that when firms face increased external pressures from stakeholders, their CSR investments are more likely to improve financial performance (Freeman et al. 2010; Liu et al. 2025).

This is in line with findings from Liu et al. (2025), who demonstrated that stakeholder pressure can enhance the positive effects of CSR investments on financial performance. The moderating effect of managerial optimism remains negative, as expected, though it is less impactful when stakeholder pressure is high.

4.4 | Poisson Fixed-Effects Model for CSR Investment

Table 4's Poisson model reinforces the OLS evidence. A one-unit rise in CSR spending delivers an IRR = 1.36—that is, 36% higher odds of better ROA/ROE—while managerial optimism still shows a negative sign, confirming its dampening effect.

TABLE 4 | Poisson fixed-effects model for CSR investment.

Variable	Incidence-rate ratio (IRR)	*z*-Stat
CSR investment	1.36***	4.48
Managerial optimism	0.82*	−1.78
Financial risk	0.85**	−2.52
Regulatory pressure	1.18***	3.15
Stakeholder pressure	1.22**	2.03
Log-likelihood	−215.2	

Note: $^{*}p<0.10$, $^{**}p<0.05$, $^{***}p<0.001$.
Source: Table created by the authors.

Financial risk reduces CSR propensity (IRR = 0.85), whereas regulatory pressure (IRR = 1.18) and stakeholder pressure both raise the likelihood that CSR translates into stronger financial results (Liu and Wu 2025; Liu et al. 2025).

Data come from audited CSR and sustainability disclosures (Palmeira and Pindado 2025); optimism is proxied by management outlook statements (Koo and Kim 2025); financial risk uses debt-to-equity and cash-flow volatility (Liu and Wu 2025).

Robustness checks replicate the findings with Poisson and alternative panel specifications (Liu et al. 2025). Logistic regression is unnecessary because ROA and ROE are continuous, so linear models adequately address endogeneity and specification concerns.

5 | Discussion

The results of this study provide substantial evidence regarding the relationship between CSR investments and financial performance in UK SMEs. These findings mirror international evidence across developed and emerging markets (Bear et al. 2010; Liu et al. 2025), supporting the hypothesis that firms that invest in CSR activities are able to enhance their reputation, strengthen stakeholder relationships, and improve financial performance (Bear et al. 2010; Palmeira and Pindado 2025). Focusing on publicly listed UK SMEs—a group largely absent from prior studies—our work adds fresh evidence to this global conversation and highlights the generalizability of the CSR–performance link (Farnsel 2025; Liu et al. 2025).

Additionally, managerial optimism was found to have a negative impact on CSR investments, confirming that optimistic managers often focus on short-term financial performance at the expense of long-term CSR initiatives. This behavioral pattern, previously documented in Asian and North-American contexts (Koo and Kim 2025; Liu and Wu 2025), underscores its cross-cultural relevance. This finding is especially important for UK SMEs, where limited resources often necessitate prioritizing short-term gains over long-term investments like CSR (Koo and Kim 2025; Liu and Wu 2025).

The moderating role of financial risk further elucidates the relationship between CSR investments and financial performance. The results suggest that high financial risk firms are less likely to engage in CSR investments, primarily due to the perceived financial burden. Yet, consistent with international evidence, for firms that did invest in CSR, the long-term benefits in terms of reduced operational risks and enhanced reputation appeared to offset these risks, leading to improved financial performance (Liu and Wu 2025; Farnsel 2025). Regulatory pressure, on the other hand, positively moderated the relationship between CSR investments and financial performance, showing that firms under higher regulatory pressure are more inclined to make CSR investments to ensure compliance and mitigate potential regulatory and reputational risks (Liu and Sun 2025). Collectively, these insights position our study as an original contribution that extends, tests, and contextualizes international CSR theory within the under-explored UK SME landscape.

6 | Theoretical and Managerial Implications

This study makes significant contributions to both Resource Dependence Theory (RDT) and Stakeholder Theory. RDT posits that firms rely on external stakeholders to secure essential resources, and CSR investments serve as a strategic mechanism to manage these dependencies (Salancik and Pfeffer 1978). RDT extension reconfigures external resource ties (investors, customers, regulators) under SME financing frictions, translating dependence management into ROA/ROE gains. This is particularly relevant in the UK market, where increasing regulatory requirements and societal demands for ethical business practices have made CSR a key component of business strategy (Liu et al. 2025).

Still, Stakeholder Theory (Freeman et al. 2010) is applied to explain how firms balance the interests of various stakeholders. In our setting, CSR aligns shareholder value with the growing demands of customers, investors, and regulators, consistent with Stakeholder Theory. The findings of this study show that CSR strengthens stakeholder relationships and improves financial performance in SMEs (Liu et al. 2025).

The managerial optimism findings also contribute to Agency Theory which has been applied in the context of managerial decision-making in large firms. Managerial optimism operates as a boundary condition that can attenuate the CSR over performance payoff for resource-constrained SMEs. This is consistent with Agency Theory's view of managerial discretion under constraints (Koo and Kim 2025).

From a managerial perspective, the study offers several actionable insights for UK SMEs. Managers should stage CSR under financing frictions (prioritize initiatives with near-term cash-flow benefits), align disclosures with stakeholder expectations, and avoid optimism-driven underinvestment in high-ROI CSR.

The findings indicate that CSR differentiates SMEs in ESG-sensitive markets when coupled with credible reporting and governance discipline (Liu et al. 2025). Thus, CSR should be treated as an investment with measurable performance pathways (customer retention, cost of capital, risk buffering).

Finally, investors should recognize the long-term value of CSR investments in SMEs. Investors can use CSR disclosure quality and consistency as signals of credible dependence-management; portfolios tilted to SMEs with disciplined CSR are positioned for superior risk-adjusted performance. Investors who prioritize firms with strong CSR commitments are likely to benefit from better financial returns and reduced long-term risks (Liu et al. 2025).

7 | Conclusion

The findings provide robust evidence that CSR investments are positively associated with financial performance in SMEs. The analysis confirms that CSR investments enhance a firm's reputation, foster strong stakeholder relationships, and reduce operational risks, all of which contribute to improved financial performance. These findings align with previous literature (Albuquerque et al. 2019; Bear et al. 2010), which highlight the long-term benefits of CSR investments for firms of various sizes.

Despite its contributions, this study has several limitations. First, while the sample includes UK SMEs listed on the London Stock Exchange (LSE), the findings may not be directly generalizable to non-listed SMEs or those in other regions. The study focuses on secondary data from publicly available sources, which may not capture all dimensions of CSR investment or managerial attitudes. Additionally, managerial optimism was measured using firm-level data, which may not fully reflect individual managerial perceptions across different contexts. Future studies could explore qualitative research to provide deeper insights into the personal views and attitudes of managers.

This research opens several avenues for further exploration. Future studies could expand the scope to include non-listed SMEs or SMEs in other countries, enabling cross-country comparisons of the CSR–financial performance relationship. Qualitative research could also be conducted to capture managerial perceptions and provide richer insights into the decision-making processes behind CSR investments.

Finally, it would be valuable to investigate how CSR investments interact with other strategic initiatives, such as innovation or market expansion, to create synergistic effects that drive both financial performance and CSR outcomes. Investor behavior and financial market responses to CSR investments are other potential areas of future research.

Conflicts of Interest

The authors declare no conflicts of interest.

Data Availability Statement

The data that support the findings of this study are available from the corresponding author upon reasonable request.

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