
The Influence of Corporate Social Responsibility and Corporate Governance on Banking Financial Performance

Submitted 20/04/19, 1st revision 07/05/19, 2nd revision 17/06/19, accepted 11/07/19

Maryam Mangantar¹

Abstract:

Purpose: This study aims to analyze the influence of corporate governance, corporate social responsibility on the financial performance of the banking sector as it is listed in the Indonesian Stock Exchange.

Design/Methodology/Approach: This explanatory research uses secondary data in the form of Annual Corporate Financial Reports. Sample was selected by census techniques with a length of observation of 5 years from 2012 to 2016. The data analysis technique uses multiple regression models.

Findings: The results of the study show that corporate social responsibility does not have any significant effect on financial performance as measured by the Return on Assets (ROA). Corporate governance does not have any significant effect on financial performance. Another finding is that social responsibility and governance have a positive direction with financial performance.

Practical Implications: The good corporate governance and social responsibility will improve the banking's financial performance. The success of the company in improving its financial performance is inseparable from the application of good corporate governance.

Originality/Value: The study implies a recommendation for the banking sector in Indonesia which is needed to improve the corporate governance and then the financial performance. Banking sector companies must pay attention and increase social responsibility because it can improve the company's financial performance.

Keywords: Corporate social responsibility, good corporate governance, company financial performance, banking sector.

JEL Code: G21, G3

Paper Type: Research article.

¹Corresponding author: Sam Ratulangi University, Faculty of Economics and Business, Management Department, Indonesia, marjam.mangantar@gmail.com

1. Introduction

The purpose of the establishment of a company is to achieve maximum profit, to prosper the owner or shareholders of the company and also to maximize company's value. Economic developments in Indonesia are increasingly fast influencing the business world, especially in the financial sector. Companies that are engaged in financial services are increasingly perceived by the community in connection with efforts to improve the quality of financial services. Banking is one part of the financial services sector that acts as an intermediary between parties in need and those who have excess funds. Banks are business entities that collect public funds in the form of deposits, and channel to the public in order to improve the lives of the general public (Law No.7 of 1992).

Banks as other forms of limited company are formed with the aim of maximizing shareholder prosperity or maximizing the value of the company and not just maximizing profit. Banking companies as business entities that collect funds for the public, especially those listed in the Indonesian Stock Exchange, are carrying out their company activities represented by management (agents) appointed by the shareholders (principals). Agencies must use their expertise, wisdom and fairness in running the company and must prioritize the interests of shareholders. In fact, company management tends to ignore the interests of shareholders for their own sake which has a negative impact on company performance. Shareholders have an interest so that the funds invested in the company can be used professionally in order to provide maximum profit. Management has other interests in the investment fund. The intended conflict of interest is conflict agency or agency problem. The Century Bank case that occurred in 2008 or the City Bank of Indonesia case in 2011 indicated a weak implementation of corporate governance in financial sector companies in which there are banking companies in Indonesia.

Corporate supervision in the financial sector is intended to make Indonesia to have a sound and fundamentally sound financial system. This financial sector also needs to be monitored in order to protect the interests of consumers and the public (financial services authority), efforts to supervise companies in the financial sector can be realized with the implementation of good corporate governance. Investment decision making and decisions based on consideration of the company's fundamental factors are no longer relevant at this time. Along with the development of the business, it also requires good accountability, information and communication while companies are required to provide social responsibility to the community (Corporate Social Responsibility) as an effort to position themselves in the eyes of investors.

In general, this study aims to analyze the influence of Corporate Governance (CG) and Corporate Social Responsibility (CSR) on financial performance, but specifically this study aims to analyze the influence of Corporate Governance and bank activities in order to apply the principle of social responsibility to the community towards increasing corporate value. Research on the value of the

company is important because the sustainability of the business of a company or institution engaged in the banking sector always requires a high level of performance so that it can guarantee high corporate value. The result study of Jamali *et al.* (2015) showed that corporate governance and social responsibility didn't have effect on financial performance, while CG has a significant positive effect on the value of companies in manufacturing companies listed in the Indonesian Stock Exchange (Kumalasari and Pratikto, 2018).

Based on the results of previous studies even differences in research findings, the authors are interested in testing and re-analyzing the influence of CG on financial performance. The novelty of this research lies in testing and analyzing the influence of CG and CSR on financial performance.

2. Literature Review

2.1 The Value of the Company

Company value is an investor's perception of the company, which is often associated with stock prices. High stock prices make the value of the company also high. The main objective of the company according to the theory of market value of the firm is to maximize the value of the firm (Salvatore, 2005). Maximizing the value of the company is very important for a company, because maximizing the value of the company also means maximizing the prosperity of shareholders which is the company's main goal. Shareholder value in theory and empirical evidence can be created through the financial management decision (Mangantar *et al.*, 2019). According to Husnan (2000) the value of the company is the price that the prospective buyer is willing to pay if the company is sold. Keown (2004), states that company value is the market value of outstanding debt and equity securities.

Company value is a reflection of market value, because the value of a company can provide maximum shareholder prosperity if the company's stock price increases. In addition, company value is measured using the Tobin's q ratio. Tobin's q is one of the ratios which considered to provide the best information, because this ratio can explain various phenomena in the company's activities. Research on the value of the company has been carried out which aims to analyze the variables that influence the increase in the value of the company.

2.2 Corporate Social Responsibility

The World Business Council for Sustainable Development stresses, "*CSR is the continuing commitment by business to behave ethically and contribute to economic development while improving the quality of life of the workforce and their families, as well as of the local community and society at large....*" (WBCSD, 1998). The European Union defines CSR as "*... the concept that an enterprise is accountable for its impact on all relevant stakeholders. It is the continuing commitment by*

business to behave fairly and responsibly and contribute to economic development while improving the quality of life of the work force and their families as well as of the local community and society at large” (Green Paper, 2001).

Based on a global corporate social responsibility (CSR) standard, a comparative framework have been produced in order to evaluate corporate social performance in national level. The nine CSR standards are UN Global Compact, Global Reporting Initiatives guidelines, Ethibel Sustainable Index, Dow Jones Sustainability Index, Global 100, FTSE4Good, Accountability Rating, SA8000 and World Business Council for Sustainable Development (Giannarakis *et al.*, 2011)

Some of the results of previous studies that discussed the effect of CSR on the company's financial performance showed varied results. Kolisch (2015), Fauzi and Idris (2010), Pan *et al.* (2014) state that CSR has a significant effect on the company's financial performance, but the results of other studies state that CSR does not have a significant influence on the financial performance as in the researches of Siregar and Bukit (2017), Bratenius and Melin (2015), Islam *et al.* (2014). Therefore the first research hypothesis is as follows:

H1: Corporate Social Responsibility influences banking financial performance.

2.3 Corporate Governance

The Forum for Corporate Governance in Indonesia (FCGI) defines Good Corporate Governance as a set of rules that regulate relations between shareholders, company managers, creditors, governments, employees, and other internal and external stakeholders related to their rights and obligations or in other words a system that controls the company, with the aim of creating added value for all interested parties. One program in charge of assessing the implementation of Good Corporate Governance in Indonesia is CGPI (Corporate Governance Perception Index). CGPI is a research program and ranking of the implementation of Good Corporate Governance for companies in Indonesia. This program is designed to trigger companies to improve the quality of the application of the concept of Corporate Governance through continuous improvement by carrying out evaluations and observations (Morais Pereira and Bonito Filipe, 2018; Bratamangala, 2018).

In Bank Indonesia Letter Number 15/15 / DPNP dated April 29th 2013 concerning Guidelines for Good Corporate Governance for Commercial Banks, the elements of evaluation of banking GCG include 11 indicators as: 1) Implementation of the duties and responsibilities of the Board of Commissioners; 2) Implementation of duties and responsibilities of the Board of Directors; 3) Completeness and implementation of the duties of the Committee; 4) Handling conflicts of interest; 5) Implementation of the compliance function; 6) Implementation of the internal audit function; 7) Application of the external audit function; 8) Application of risk management including the internal control system; 9) Provision of funds to related parties and

large funds; 10) Transparency of the Bank's financial and non-financial conditions, GCG implementation reports and internal reporting; 11) Bank strategies plan.

In this regulation out of a total of 11 (eleven) indicators, GCG assessment in this study was carried out by looking at the three aspects used, namely the Independent Commissioner, the Board of Directors, and the Audit Committee.

Some of the results of previous studies that discussed the effect of GCG on the company's financial performance showed varied results. Mahyang *et al.* (2018), Hartutik and Budi (2016), Markonah *et al.* (2014) stated that GCG has a significant effect on the company's financial performance, but the results of other studies state that good corporate governance does not influence the company's financial performance (Siswanto *et al.*, 2017; Dewany, 2015; Sianipar & Wilson, 2019). Therefore the second research hypothesis is as follows:

H2: Good corporate governance influences banking financial performance.

3. Research Methodology

The study uses an explanatory or explanatory design, which tests or confirms the relationship or the influence between variables. This research is designed to identify cause and relationships between variables where research problems have been clearly defined. Causal design is useful for analyzing the relationships between one variable and another. The purpose of this study is to test or confirm whether there is a relationship or influence of social responsibility and corporate governance on financial performance.

This research is located in the Indonesia Stock Exchange. This location was chosen with the following consideration: First, the Indonesia Stock Exchange is the only stock exchange in Indonesia that trades the securities of all listed companies in Indonesia through the Indonesia Stock Exchange. Second, the data set available of the Indonesia Stock Exchange (IDX) is completed and easy to obtain. Third, the data set of the Indonesia Stock Exchange is accurate and accountable because it has been widely publicized through ICMD (Indonesia Capital Market Directory).

The research objects in the financial statements of banking companies are in the form of balance sheets and income statements for the period 2012 to 2016 which were published in the ICMD from 2013 to 2017. The subjects of this study are companies engaged in the financial sector of the banking sub-sector listed in the stock exchange. The population target of this study is all banking companies listed in the Indonesia Stock Exchange until 2017. Samples of companies that meet the criteria as research samples consist of companies that fall into the category of banking sub-sector companies including private and government banks, currently companies that are categorized in this sub-sector. The sampling technique in this study was purposive sampling method, namely the technique of taking samples with

certain considerations where the population that met the criteria was stated as a sample in the study.

The criteria for determining the sample are as follows: (1) companies in the banking sub-sector which are listed annually on the Indonesia Stock Exchange during 2012 to 2017; (2) companies in the banking sector that regularly present and publish financial statements in a row during 2012 to 2017; (3) companies in the banking sector that are always and consistently not included in the Indonesia Stock Exchange black list during the study period; (4) companies in the banking sector whose shares are actively traded on the Indonesia Stock Exchange during the study period; (5) companies in the banking sector that have complete data related to the variables used in this study.

Table 1. *Research Populations and Samples Criteria*

Banking companies registered on the Indonesia Stock Exchange in 2012-2017	51
Banking companies are consistently blacklisted	20
Banking companies that suffered losses	08
Bank Sample Amount	11

Source: *www.idx.co.id: data processed, 2018.*

The type of data used in this study is secondary data that has been published in the form of financial ratios data calculated from the elements in the company's Annual Financial Report in the manufacturing sector which are published at the end of each period as of December 31 every year from 2012 to 2017. The data is in the form of Balance Sheet, Loss/Profit Statement, List of shareholders, Web site of the Indonesia Stock Exchange (IDX), Capital Market Supervisory Agency (BAPEPAM), the Central Statistics Agency (BPS), Bank Indonesia and the Financial Services Authority and other sources relevant to research. The analysis technique used is a multiple linear model which states a linear relationship between two or more dependent variables. The multiple linear model in this study is as follows:

$$Y = a + b_1x_1 + b_2x_2 + e$$

Testing the hypothesis of the influence between variables we used alpha (α) level of significance as 5%. The variables described in the conceptual framework are explained as follows:

1) Social Responsibility (X1) and Social and Environmental Responsibility as the company's commitment to participate in sustainable economic development to improve the quality of life and the environment that is beneficial, both for the company itself, the local community, and the community in general (Law number 40 of 2007 concerning the NV);

2) Corporate Governance (X2), Good Corporate Governance as the principles that underlie a process and mechanism for managing a company based on laws and business ethics (Regulation of the State Minister for State-Owned Enterprises No: PER - 01 / MBU / 2011). The indicators are the size of the independent commission, the size of the board of directors and the size of the audit committee with a data ratio scale;

3) Financial Performance (Y), as measured by profitability. In the banking business (banking business profitability) is the ability of the banking business to earn profits based on the investment it does. The financial performance indicator in this study is Return on Assets (Matar and Eneizan, 2018), which is profit divided by the number of assets, with the ratio data scale.

4. Results

Banking business began in the Babylonian era and then continued to the days of Ancient Greece and Rome. At that time the bank's main task was only as a place to exchange money. Along with the development of world trade, the development of the banking sector is also increasingly rapid because the development of the banking world is inseparable from the development of trade. The development of trade which was originally only in the European region eventually spread to West Asia. The banks that had been known at that time on the European Continent were the Venezia Bank in 1171, followed the Bank of Genoa and the Bank of Barcelona in 1320. On the contrary, the development of banking in mainland Britain only began in the 16th century. However, because the British were actively seeking trade areas which were then colonized, the development of banks was also brought to their colonies.

The history of Indonesian banking is inseparable from the colonial era of the Dutch East Indies. At that time there were several banks that held important roles in the Dutch East Indies. Existing banks are: 1) De Javasche NV; 2) De Post Paar Bank; 3) De Algemenevolks Crediet Bank; 4) Netherlands Handles Maatscappij (NHM); 5) Nationale Handles Bank (NHB); 6) De Escompto Bank NV. In addition, there are also indigenous, Chinese, Japanese and other European Banks: 1) Bank Nasional Indonesia; 2) Abuan Saudagar Bank; 3) NV Bank Boemi; 4) The Chartered Bank of India; 5) The Yokohama Species Bank; 6) The Matsui Bank; 7) The Bank of China; 8) Batavia Bank.

In the days of independence Indonesian banking increased and developed again. Some Dutch banks were nationalized by the Indonesian government. Banks that were in the early days of Indonesian independence included: 1) Bank Negara Indonesia which was established on July 5, 1946 then became BNI in 1946; 2) Bank Rakyat Indonesia which was established on February 22, 1946. This bank is from De Algeme Volk Crediet bank or Syomin Ginko, Surakarta Bank MAI (Fair and Prosperous Airlines) in 1945 in Solo, Bank Indonesia in Palembang in 1946, Indonesian National Trade Bank in 1946 in Medan, Indonesia Banking Corporation

in 1947 in Yogyakarta, then became Amerta Bank, NV Bank Sulawesi in Manado in 1949, Kalimantan Trading Corporation in Samarinda in 1950 then merged with Bank Pacific, East Bank NV in Semarang changed its name to Bank Gemari, then merged with Bank Central Asia (BCA) in 1949.

To test the research hypothesis, the results of the testing of statistical data are presented in Table 2.

Table 2. *Testing the F test Hypothesis and t Test*

Model	F test		t	
	Constant	F	sig	sig
Social responsibility	1.238	0.298	1.306	0.197
GCG		0.134	-5.88	0.559

Source: Data processed, 2018.

From the results of the t test in Table 2, it can be seen that corporate social responsibility (X1) has a significance level of p-value of $0.197 > 0.05$, meaning that social responsibility does not have a significant effect on financial performance. Thus the results of this study reject H1 which states that social responsibility affects financial performance. The results of this study are not in line with the results of other studies. Social responsibility has a positive relationship with financial performance, meaning that the better the corporate social responsibility, the higher the company's financial performance. The results of this study are in line with the findings of Pan (2014).

The corporate governance variable (X2) has a significant level of p-value of $0.559 > 0.05$. It can be concluded that H_0 is rejected and H_a is accepted or corporate governance has no significant effect on the financial performance of the banking sector companies listed in the Indonesia Stock Exchange. Corporate governance has a positive relationship direction with financial performance where the better corporate governance will improve the company's financial performance.

Whereas from the results of the F test the results of this study found that together social responsibility (X1) and corporate governance (X2) did not have a significant effect on financial performance (Y) of the banking sector in Indonesia, characterized by a significance level of p-value 0.05. The results of this study are not in line with the findings of Dianawati *et al.* (2016) stated that social responsibility and corporate governance have a significant influence on company performance and firm value.

5. Discussion

Based on the results of the regression analysis it is proven that CSR has not any positive relationship with financial performance, as well as GCG has not any

positive relationship with financial performance. The results of this study mean that the actions of banking companies in accordance with the commitment to improve the quality of people's lives proven to improve the company's financial performance. This is not in line with the results by Hong and Hwang (2017) stating that increasing CSR activities will have a positive impact on Return on Assets. The influence of CSR on financial performance of firms in Germany and the USA have a strong empirical evidence that CSR influences firm performance and that the significance differs between Germany and the USA (Kolisch, 2015).

Social responsibility is the earnest effort of business entities to minimize negative impacts and maximize the positive impact of their operations on all economic, social and environmental stakeholders to achieve sustainable development goals. Corporate Social Responsibility disclosure reports are consistent with corporate reporting. Sustainability reporting is the company's social responsibility disclosed in the annual report. Sustainability reporting contains economic, environmental and social policies, the influence and performance of the organization and its products in the context of sustainable development. Companies that implement social responsibility transparently to the public will find it easier to achieve investment returns and produce good financial performance.

The GCG has a positive relationship with company's financial performance, where the results of this study are supported by findings from Siswanti *et al.* (2017), Markonah *et al.* (2017), Hartutik and Asmita (2016). Based on the results of CSR research does not have a significant effect on the company's financial performance. The results of this study are supported by the findings of Siregar and Bukit (2017) and Islam *et al.* (2014). The results of this study are not in line with the findings by Kolkisch (2015) and Pan (2014).

The success of the company in improving its financial performance is inseparable from the application of good corporate governance. Financial performance is reflected in Return on Assets or yields obtained from the management of company assets. The results of the study indicate that corporate governance as measured by the GCG index has no significant effect on the financial performance of banking sector companies in Indonesia. Corporate governance has a positive direction with an increase in financial performance as measured by ROA.

6. Conclusion

Corporate social responsibility does not affect financial performance in the banking sector in Indonesia. Corporate governance does not affect the financial performance of the banking sector companies in the Indonesia Stock Exchange. In any case banking sector companies need to improve corporate governance in an attempt to improve financial performance as other studies suggests. Banking sector companies must pay attention and increase social responsibility because it is a fact that can improve their financial performance as other studies suggested. The results of this

study can be used as reference material for further research relating to issues of corporate governance, social responsibility and financial performance.

References:

- Bratenius, H.L. and Melin, J.E. 2015. The Impact of CSR on Financial Performance – An event study of Abnormal stock returns of Swedish companies as a reaction to the release of the Folksam Index of Corporate Social Responsibility. Accounting, Strategy & Cont, Copenhagen Business School, Master thesis.
- Bratamanggala, R. 2018. Factors Affecting Earning Per Share: The Case of Indonesia. International Journal of Economics & Business Administration, 6(2), 92-100.
- Dewany, W.F. 2015. Analysis of the effect of GCG quality on the financial performance of Islamic banks. The Indonesia Accounting Review, Vol, 5.
- Fauzi, H., Idris, K.Md. 2010. The Relationship of CSR and Financial Performance: New Evidence from Indonesian Companies, <https://www.researchgate.net/publication/228300856>.
- Giannarakis, G., Litinas, N. and Sarianidi, N. 2011. Evaluation of corporate social Responsibility performance standards. African Journal of Business Management, 5(17).
- Hariyadi, Lastanti, S.I. and Murtanto. 2014. The effect of financial performance to corporate value with the disclosure of good corporate governance and corporate social responsibility as moderating variable. Business and Entrepreneurial Review, Vol. 13, No. 2, 113–122.
- Hartutik and Budi Asmita. 2016. The influence of good corporate governance implementation to the Financing Quality. Efficiency and Profitability of Syariah Bank In Indonesia. ISBN 978-602-17688-9-1, Proceeding 2nd Multidisciplinary Conference, November 15th, Universitas Muhammadiyah Jakarta, Indonesia.
- Husnan, S. 2000. Manajemen Keuangan: Teori dan Penerapan (Keputusan Jangka Panjang). BPFE, Yogyakarta.
- Islam, R.M., Khan, R.T., Choiudory, T. and Adnan, M.A. 2014. How earning per share (EPS) affects share price and firm value. European Journal of Business and Management, Vol. 6, No.17, 97-108.
- Jamali, H., Sutrisno, T., Subekti, I. and Prihat, A. 2012. The influence of corporate governance and Corporate social responsibility on financial performance with efficiency as mediating variable. International Journal of Business and Management Invention, 4(5), 1-10.
- Keown, A., Martin, J. 2004. Financial management: principles and Application. Pearson Prentice Hall.
- Kolisch, H. 2015. Does CSR pay? The impact of CSR on financial performance: A Comparison between Germany and the US. 5th IBA Bachelor Thesis Conference, July 2nd, Enschede, The Netherlands, University of Twente, The Faculty of Behavioural, Management and Social Sciences.
- Kumalasari, D. and Pratikto, H. 2018. Good corporate governance effects on corporate value through return on equity and return on asset of manufacturing company. KnE Social Sciences: The First International Research Conference on Economics and Business (IRCEB), 114–126, DOI: 10.18502/kss.v3i3.1878.
- Mangantar, M., Maramis, J.B. and Saerang, I.S. 2019. A review of creating shareholder value

- through the financial management decision. *Advances in social science, education and humanities research*, 308, 62-66, 16th International Symposium on Management, INSYMA, Atlantis Press.
- Mayang, M., Noorlailie, S. 2018. The effect of good corporate governance mechanism and corporate social responsibility on financial performance with earnings management as mediating variable. *Asian Journal of Accounting Research*, 3(1), 41-60, <https://doi.org/10.1108/AJAR-06-2018-0008>.
- Markonah, Sudiro, A., Surachman, and Rahayu, M. 2014. The effect of good corporate governance and premium growth on the performance of insurance companies, www.gatrenterprise.com/GATRJournals/index.html *J. Bank. Fin. Review*, 2(2), 1–7.
- Matar, A., Eneizan, B. 2018. Determinants of Financial Performance in the Industrial Firms: Evidence from Jordan, DOI: 10.9734/AJAEES/2018/37476.
- Morais Pereira, M.V., Candeias Bonito Filipe, A.J. 2018. Quality of Board Members' Training and Bank Financial Performance: Evidence from Portugal. *International Journal of Economics & Business Administration*, 6(3), 47-79.
- Oh, S., Hong, A. and Hwang, J. 2017. An analysis of CSR on firm financial performance in stakeholder perspectives. *Sustainability*, www.mdpi.com/journal/sustainability.
- Pan, X., Sha, J., Zhang, H. and Ke, W. 2014. Relationship between corporate social responsibility and financial performance in the mineral industry: Evidence from Chinese Mineral Firms. *Sustainability*, 4077-4101.
- Prabowo, P.A.S., Titisari, H.K. and Wijayanti, A. 2018. The effect of good corporate governance on financial performance of the company: Empirical study on manufacturing company of consumer goods sector industry listed on Indonesia stock Exchange Year 2015- 2016. *Proceedings of the 2nd International Conference on Technology, Education, and Social Science (ICTESS 2018)*.
- Sebastian, J., Karlon, A.H. 2015. The relationship between CSR and financial performance: A quantitative study examining Swedish publicly traded companies. *Economics and Financial Issues*, 7(4), 316-323.
- Siregar, N.B. and Bukit, R.B. 2017. Impact of corporate social responsibility and company size on Corporate Financial Performance with Good Corporate Governance as Moderating Variable. *Advances in Economics, Business and Management Research (AEBMR)*, 46, 241-248.
- Siswanti, I., Salim, U., Sukaharsono, G.E., Aisjah, S. 2017. The Impact of Islamic Corporate, Islamic Intellectual Capital and Islamic Financial Performance on Sustainable Business Islamic Banks. *International Journal of Economics and Financial Issues*, 7(4), 316-323.
- Tahsan, R.K., Tonmoy, T.C., Ashique, M.A. 2014. How Earning per Share (EPS) Affects Share Price and Firm Value. *European Journal of Business and Management*, Vol. 6.
- The World Business Council for Sustainable Development. 1998. *First WBCSD CSR dialogue*. The Netherlands.