# Disclosure of Corporate Social Responsibility and Financial Performance in Islamic Banks

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*Abstract:* - The objective of this research is to evaluate the impact of Corporate Social Responsibility (CSR) disclosure on financial outcomes (ROA) for the years 2016 to 2018. The moderating variables are company size and age. The sample used for the study comprised data from Islamic banks in Indonesia between 2016 and 2018. The analysis method utilized is structural equation modeling (SEM), with CSR as the independent variable and ROA as the dependent variable. The research also included business size and firm age as moderating factors. The findings of the study indicate that the company's age and corporate social responsibility have significant impacts on profitability.

*Key-Words:* CSR, ROA, Firm Size, Firm Age, Islamic Banks.

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# 1 Introduction

The Corporate Social Responsibility (CSR) program is an obligation of a company that is not only responsible for consumers, shareholders, or employees but also responsible for the environment. According to the European Commission (EU) (2001), the concept of CSR encompasses enterprises incorporating social and environmental issues into their business operations as well as voluntary contacts with their stakeholders.

In Indonesia, based on Limited Liability Company Law No. 40 of 2007 concerning Limited Liability Companies, it notes that the company is responsible for natural resources in social and environmental terms, although this clause focuses more on companies engaged in natural resources. Meanwhile, there are no clear and comprehensive norms for the banking industry because banks have little operational impact on the natural resource environment. However, banks must pay attention to the prevailing laws and regulations when providing credit to companies that control natural resources.

In addition to the needs of shareholders, banks are expected to concentrate on other environmental interests, such as society, workers, regulators, and even the media. This has culminated in the rise and growing exposure to the banking effect of social risks. The response of management to global competition involves quality improvements and risk management measures, system and process reorganization, and better transparency. To resolve dynamic and evolving social risks and to meet the requirements of globalization, CSR is an excellent mechanism to overcome this challenge as an institution of trust.

CSR disclosure is in the form of a report containing all business activities related to CSR. It is generally referred to as sustainable reporting when making a report. Certain criteria may be followed by banks as a guide. Though companies in Indonesia are already prominent and widely practiced, there are no standard regulations that standardize CSR disclosure rules, but Global Reporting Initiatives (GRI) are the most used, [1].

The indicators used in social success disclosure are made up of 91 indicators. These indicators include economic, environmental, and social indicators that are included in the guidelines of the Global Reporting Initiative / GRI G4. The introduction of CSR in a bank is also carried out because the bank requires the credibility of the society that the company focuses not just on operations but also on the world around which the bank is situated. This could be accomplished by expressing thanks to the community for having a beneficial impact on the community's excellent image and faith in the future survival of a better organization.

Banking and other financial institutions are particularly dynamic because changes in a country's economy influence its financial institutions. The growth of financial institutions in Indonesia, both conventional and Islamic financial institutions, has developed very well. Fundamentally, Islamic banks operate similarly to conventional banks, acting as mediators between those with surplus cash (through fundraising operations) and individuals in need (by financing activities). To ensure that the goods supplied by traditional banks, both the products of raising funds (funding) and the products of financing (financing) can essentially also be supported by Islamic banks. One distinction between conventional banks and Islamic banks is that Islamic banks do not use an interest system, but rather a profit-sharing system, which is a fund management system in an Islamic economy in which profit-sharing estimates are based on an agreement between the bank and the customers who invest their funds.

Research on CSR disclosure of banking financial results in Indonesia is very adequate, but relevant to Islamic banking the inclusion of moderate firm size and firm age variables is very limited. The purpose of this study is to assess the influence of CSR disclosure on financial outcomes (ROA) from 2016 to 2018. Corporation size and age are moderating variables.

# 2 Literature Review

CSR is a prominent idea in corporate reporting. Every company has a CSR policy that results in full annual reporting on its activities. CSR in Sharia Banks is also important, CSR practices that are consistent with Islamic ethical standards for clients to recognize and advocate Islamic Banks, [2].

## 2.1 Corporate Social Responsibility and Return on Asset

CSR has a positive influence on ROA, implying that enterprises with significant capital market power have superior CSR performance, which indicates that companies that are successful and have high growth aspirations have many resources to commit to charitable initiatives and to affirm their presence for stakeholders, [3], [4].

According the findings of one of the previous studies, variable control of the firm size and age revealed a significant and positive association between CSR disclosure and ROE and ROA-evaluated financial efficiency, [5]. The findings revealed that the bank's CSR operations improved and that its disclosure contributed to the bank's increased economic efficiency. Other studies found that there was an impact of firm size on profitability as measured by ROA, [3], [6]. CSR in Malaysian public companies and found that company size in terms of ROA and ROE has a significant positive relationship with company output as one of the control variables, [7]. Furthermore, in terms of ROA and ROE, a firm age has been found to have a substantial negative relationship with the results of the company. In accordance with one of the previous studies, they discovered a substantial positive association between ROA and ROE in the control variable of company size and a significant negative relationship between ROA and ROE in the control variable of firm age, [8].

It is identified a substantial association between the amount of CSR and financial success in Tunisia, [9]. The findings indicate that Tunisian-registered banks that are good performers are more accountable and have an opportunity to market their CSR. While the relationship between firm size and firm age is negligible, the larger and older firms have a positive impact on financial performance (profitability), which encourages a rise in the adoption of better CSR practices, [10].

The studies revealed that CSR influenced ROA but had no effect on Tobin's Q. Meanwhile, firm age might mitigate the impact of CSR on ROA and Tobin's Q. In the meanwhile, the size of the Commissioners' Board and the organization did not affect the link between CSR, ROA, and Tobin's Q. Other researchers who did CSR studies on ROA and Tobin's Q discovered that ROA was impacted by corporate era, [3]. On the other hand, studied the impact of CSR on financial performance as measured by ROA and Tobin's Q, [6]. Their research found that earnings control, firm size, and leverage all have an impact on ROA. However, it was revealed that the firm's age had no influence on ROA.

## 2.2 Firm Size dan CSR

The size of the firm is one of the most utilized factors in literature to support the release of CSR. The Agency's theory and credibility support several statements concerning the link between CSR actions and disclosure. Firm size is used to assess the political expenses that increase with corporate size and risk level. Firm size is a business entity measurement that indicates the magnitude and scope of its operations, [11].

More precisely, the larger companies had higher CSR efficiency, [6]. Other studies shows a significant relationship between firm size and CSR, that large bank sizes have good CSR, [12], [13]. However, another research discovered that more exposure (firm size) did not result in more CSR disclosure in annual and online reports in Tunisia, [9]. Overall, it doesn't seem like the measure is exerting any pressure on banks to make CSR concerns part of their reporting procedures. These findings highlight the necessity of considering the relevant CSR values in industrial banking (for small and large banks).

## 2.3 Firm Age dan CSR

Younger companies are expected to provide more thorough disclosures to demonstrate their adherence to the standards. The financial performance of both new and established businesses has drawn substantial interest from academics in a variety of fields, including economics, organizational studies, and finance, [14].

It is indicated that banks that have been registered in Tunisia for a long time prefer to legitimize their company through increased CSR to demonstrate ethical knowledge, older banks are more conscious of CSR problems, [8]. In line with previous research regarding the establishment of a firm age as a control variable that affects CSR financial efficiency, [5], [10].

## 2.4 Research Hypothesis

Based on the results of the previous studies above, we make the following research hypothesis as follows.

H1: CSR affects the ROA.
H2: The impact of CSR on ROA can be moderated by firm size.
H3: The impact of CSR on ROA can be moderated by firm age.

# 3 Research Method

## 3.1 Research Sample

This investigation utilizes a quantitative research technique, with secondary data serving as the major source of information. Researchers obtained Sharia Bank data which revealed CSR activities in the annual report or the sustainability report for 2016-2018. The annual reports of each bank and the official website of the Indonesia Stock Exchange are the sources of the data used in this study.

The population used in this research is Islamic Financial Institutions, where the Islamic Bank that has been included in the listing is getting more attention from the public. While the sample selection in this study was determined using the purposive sampling technique, namely the sampling technique based on certain criteria, namely as follows:

- Sharia banks registered with the Financial Services Authority for the 2016-2018 period.
- Sharia banks publish financial reports or annual reports for the 2016-2018 period either through the IDX website or on the websites of each Islamic bank.
- Islamic bank financial reports presented during the study period using the form of Rupiah (Rp).
- Sharia banks that carry out CSR disclosures in their annual reports (Annual Report) consecutively during the 2016-2018 period.

The content analysis approach was used in this study to investigate CSR. By assigning a score to the annual report of the social disclosure measurement carried out by observing the presence or absence of an information item listed in the annual report, the evaluation of the content analysis process is also conducted with a nominal score. If the information item is not in the financial report, it is given a score of 0, and if the specified information item is in the annual report, it is given a score of 1. Then, to obtain the overall score for each business in each year, the cumulative score of all indicators is added up. To achieve the overall value provided in the annual report based on the 2015 GRI guidelines, the disclosure of corporate social aspects is presented.

This ease of funding will influence the company's value and be good information for investors, a large company size that continues to expand will define potential profit levels (Eko, 2014). In this research, the size is determined from the company's average number of assets during the 2016-2018 sample year.

## 3.2 Analysis Tool

The data logged (Ln) when entering data in the Structural Equation Modeling (SEM) software is used to produce total asset data as research variables. This size variable is viewed in logarithmic form due to its large magnitude and distribution relative to other variables.

Firm size = Total Company Assets

The length of time a company has been listed on the Indonesian Stock Exchange is known as the firm age. The age of a company is also a measure of its ability to compete and thrive for a very long period. The firm age is determined based on the difference between the year of study and the year of registration or the year of IPO (first issue) on the IDX. In Islamic banks, the firm age has been registered since the business became Sharia Commercial Bank (BUS). In this analysis, firm age was measured using the following:

Age = year to n – the first year recorded as a Sharia Commercial Bank (BUS).

ROA is a form of profitability ratio that is intended to measure the ability of the company to invest in the business activities of the company to generate profits using its assets. Investment decisions within the company will be reflected on the asset side of the company and therefore the term ROA is often equivalent to Return on Investment. Using the following formula, ROA can be calculated:

ROA = Net Profit Before Tax / Total Asset

With the use of data processing tools like Smart PLS 3.0, the regression analysis is carried out using SEM. Regression analysis is the process of determining how the dependent variable (bound) is affected by one or more independent variables to estimate and project the population average or average value of the dependent variable based on the known value of the independent variable. The research model used in this study is presented in Figure 1 as follows:

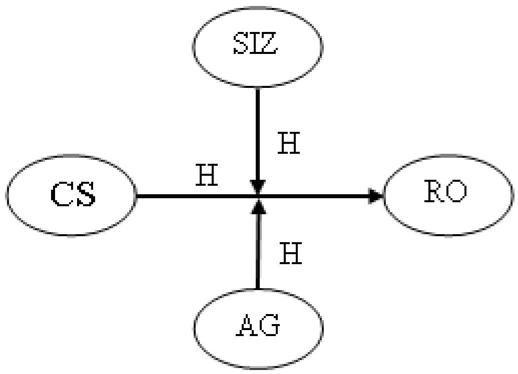


Fig. 1: Research Model

# 4 Results and Discussion

## 4.1 Result

The data collected from the source is then processed by descriptive statistical data processing, which is used to describe the data, to find a general conclusion from the data being processed. Descriptive statistics have been collected. The mean, lowest, maximum, and standard deviation numbers provided the researcher with a visualization.

Table 1. Descriptive Statistics Results

| | ROA | CSR | SIZE | AGE |
|---|---|---|---|---|
| Mean | 0.359 | 0.239 | 16.168 | 2.157 |
| Median | 0.525 | 0.220 | 15.841 | 2.079 |
| Maximum | 12.400 | 0.505 | 18.404 | 3.258 |
| Minimum | -10.770 | 0.044 | 13.403 | 0.693 |
| Std. Dev. | 4.681 | 0.143 | 1.292 | 0.545 |
| Skewness | 0.074 | 0.343 | -0.031 | -0.014 |
| Kurtosis | 4.601 | 1.979 | 2.345 | 3.703 |
| Observations | 36 | 36 | 36 | 36 |

*Source: Computations from research data*

From the results of Table 1, descriptive statistics processed using PLS 3.0 show the minimum value, maximum value, average value (mean), and standard deviation of all research variables from 2016 to 2018. The dependent variable in this investigation is ROA, as shown by the data in Table 1. The mean ROA value is determined to be 0.359 based on the 36 available data. The maximum value is 12,400, namely PT. Sharia National Pension Savings Bank in 2018. The minimum value of -10,770, namely PT. Panin Dubai Syariah Bank in 2017. The standard deviation of Return on Assets is 4,681

The 36 observations in the descriptive statistics from CSR, which served as the study's independent variable, have a mean value of 0.239. The highest number, which corresponds to PT. Bank Syariah Mandiri in 2018, is 0.505. In 2016, PT. MayBank Syariah Indonesia and PT. Sharia National Pension Savings Bank both has a minimum value of 0.044. The CSR variable's standard deviation is 0.143.

The results of the Firm Size descriptive statistic which became the moderating variable in this study, the number of observations of 36 has a mean value of 16,168. The maximum value is 18,404, namely PT. Bank Syariah Mandiri in 2018. The minimum value of 13,403, namely PT. MayBank Syariah Indonesia in 2018. The standard deviation of the Firm Size variable is 1.292.

The results of the descriptive statistics from Firm Age which became the second moderating variable in this study, the number of observations of 36 has a mean value of 2.157. The maximum value is 3,258, namely PT. Bank Muamalat Indonesia in 2018. The minimum value is 0.693, namely PT. Sharia National Pension Savings Bank in 2016. The standard deviation of the Firm Age variable is 0.545.

The results of regression analysis using SmartPLS show that the R-squared value or the coefficient of determination in this study is 0.23. According to the results, CSR, the research's independent variable, may explain around 23% of the variance in the dependent variable, ROA, with the remaining 73% presumably being impacted by other independent factors that were not included in this study. The following (Figure 2) shows the results of data processing using the structural equation modeling method.

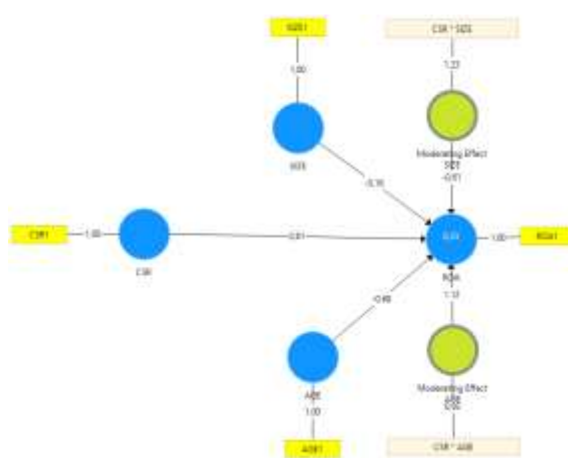

Fig. 2: Result Model Analysis

 

Table 2. Evaluation of Measurement in Research Model

| Variable | R – Square | Size Effect ($f^2$) | Goodness of Fit (GoF) |
|---|---|---|---|
| ROA | 0.23 | | 0.48 |
| CSR | | 0.053 | |
| Moderating SIZE | | 0.127 | |
| Moderating AGE | | 0.153 | |

*Source: Computations from research data*

The Size Effect ($f^2$) test measures changes in the R-square value that can be used to assess the effect of exogenous variables on endogenous variables with a material effect. In the Size Impact test, if it has a value of 0.02, this means that the predictor variable has a low influence, if it has a value of 0.15, this means that the predictor variable has a moderate effect, if it has a value of 0.35, it means that the predictor variable has a strong impact. The test results for the Size Effect show that the CSR variable has a value of 0.053 and the moderating variable SIZE has a size effect value of 0.127 which means that as a predictor variable, it has a low influence on the structural model level, while for the moderating variable AGE has a size effect value of 0.153 which means that it is a predictor variable. moderate influence at the structural model level.

The Goodness of Fit (GoF) test is used to verify the structural model, the Goodness of Fit (GoF) value is between 0 and 1, the low-level value 0.10, the medium-level value is 0.25, and the high-level value 0.36 are used, [15]. The measurement of the overall fit index in the research model using the goodness of fit test resulted in a value of 0.48, these results provide a conclusion that the measurement evaluation in the research model resulted in a high value. The results of the R-square test, size effect test, and goodness of fit test are as follows (Table 2).

## 4.2 Discussion

### CSR's Effects on ROA

Based on Table 3, CSR as an independent variable has a coefficient value of 0.806 in this analysis, which means that CSR has a positive effect on the ROA. The CSR variable has a P-value of 0.049 <0.05, so the CSR variable meets the significance criterion by using an alpha value of 5%. Research shows that CSR has a positive impact on the ROA. The findings of this study are consistent with the previous research, [3].

Through carrying out CSR activities, the company can be better informed by the public that the company not only focuses on operational activities but also cares about the world in which the company is based which will improve public trust in the company. The CSR activities carried out by businesses will influence the increase in company profitability.

Table 3. Path Coefficients, Effect, and Significance

| Hypothesis | Description | Original Sample | T-Statistics | P-Values | Effect and Significance |
|---|---|---|---|---|---|
| H1 | CSR -> ROA | 0.806 | 2.036 | 0.049 | Positive and significant (alpha 5%) |
| H2 | Moderating Effect SIZE -> ROA | -0.607 | 1.765 | 0.086 | Negative and significant (alpha 10%) |
| H3 | Moderating Effect AGE -> ROA | 1.119 | 2.620 | 0.013 | Positive and significant (alpha 5%) |

*Source: Computations from research data*

**The company's size moderates the effect of CSR on ROA**

Firm Size (SIZE) has a significant moderating effect on the impact of CSR on ROA. Based on the information in Table 3, the moderating variable SIZE has a P-value of 0.086 < 0.10, suggesting that it meets the requirement for significance using an alpha value of 10%. The findings of previous studies, which suggest that disclosure of CSR influences financial output with company size as the control variable, are supported by the findings of the current study, [3], [7], [8]. It will be challenging for banks with greater assets to sustain their rise in profitability, but they may be more flexible in selecting the budget for money while engaging in CSR activities.

**The company's age moderates the effect of CSR on ROA**

The influence of CSR on ROA can be moderated by the company's age (AGE). The AGE variable, which is the second moderating variable in this study, has a P-value of 0.013 < 0.05, indicating that it fulfills the significance requirement using a 5% alpha value.

Based on Table 3, it can be seen that company age will lessen the impact of CSR on ROA. The research conducted is supported by the study's findings which concludes that firm age is capable of moderating corporate social responsibility towards ROA, [3], [7], [8].

# 5 Conclusion

The Bank's CSR programs have a substantial effect on profitability as determined by ROA. Banks that carry out CSR will increase public trust in the business of the company, which will eventually increase the business of the bank. The CSR activities carried out by banks can be substantially reduced by firm size and firm age. Banks that are getting bigger and older may affect the CSR activities of companies. Banks that are growing and have a lengthy operational lifetime will be more acknowledged by the public as having a positive impact on their profitability through CSR.

The study's analysis has several limitations due to the sample selection, being limited to Islamic banks in Indonesia, and the limited research period, which ran from 2016 to 2018. It is recommended that further researchers use a sample of Islamic finance companies and use different research variables such as Net Interest Margin and Non-Performing loan.

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