Firm Value, Financial Performance, and Corporate Social Responsibility in the Indonesian Banking Industry

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Abstract. This research aims to examine whether a company's financial performance and corporate social responsibility (CSR) reporting affect the value of the banking firms listed on the Indonesia Stock Exchange (IDX). This study uses 33 banks as a sample for three-year periods from 2016 to 2018, resulting in 99 bank-year observations. Financial performance was measured by bank financial ratios such as capital adequacy ratio (CAR), return on equity (ROE), net interest margin (NIM), net profit margin (NPM), non-performing loan (NPL), operating expense to operating revenue (BOPO), and loan to deposit ratio (LDR). Meanwhile, CSR reporting was measured by a checklist based on Global Reporting Initiatives (GRI) G4 sustainability reporting guidelines. Firm value was calculated by price to book value, a ratio that reflects the stock market's estimate of a company's present and future profits and growth prospects. Multivariate regression analysis suggests that CSR reporting does not affect firm value, while three financial ratios, namely ROE, CAR, and LDR, affect firm value. The results indicate that investors in investing their money in the banking industry do not consider the company's CSR but its financial condition. The descriptive statistic reveals that the level of CSR reporting made the Indonesian banking companies is relatively low, 26 percent on average. This research provides evidence about the amount of CSR reporting of the Indonesian banking companies that may not impact firm value. The capital market authority agency then may release some regulations to enhance CSR reporting.

Keywords: Firm value · Corporate social responsibility · Corporate social responsibility disclosures · Financial performance · Bank industry · Indonesia

1 Introduction

The firm value is the stockholder's appraisal of a business's performance. It is reflected in the stock price. The rising stock price reflects investors' confidence in the firm and their willingness to pay more for a better return [1, 2]. One way to enhance firm value is through good news from the company, such as sound financial performance and corporate social and environmental (CSR) reporting.

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CSR is a conception that integrates social and environmental responsibility into corporate process and stakeholder relationships. According to Jizi et al. [3], firms with strong financial performance but under public scrutiny generally employ sustainability disclosure. The disclosures comprise three economic, environmental, and social aspects. Under the environment aspects, a company explains the consequences of its operation on the environment, climate change, the business' performance in alleviating these consequences, and its contribution to green and sustainable growth [4]. According to Mukhtaruddin [5], CSR disclosure in the annual report enhances the firm's impression. It turns out to be one of the concerns that investors and potential investors consider when selecting whether or not to invest in a company. The investment decision is made because investors and potential investors believe that the business portrays to the public an impression that neither the company nor any of its subsidiaries solely focused on profit but is also concerned with the environment and society.

Some studies investigate whether or not CSR impacts corporate value. Although there are conflicting results, most studies confirm that CSR positively influences firms' value [6–12]. This article investigates whether CSR reporting and a bank's financial performance affect a bank's firm value. A bank is an industry that produces minimum pollution compared to other industries such as mining and manufacturing. Hence, probably the investors will consider the fundamental information such as financial ratios rather than CSR information. Some studies assert that CSR disclosures make no difference on a bank's firm value [13, 14]; even in Taiwan, CSR disclosures do not impact firm value in all industry sectors until it reaches a threshold value [15].

2 Literature Review and Hypotheses

2.1 Signaling Theory and Previous Studies

Spence [16] introduced Signaling Theory in 1973, which describes how a business communicates with users of financial information. Connelly et al. [17] assert that signaling theory is practical for understanding the behavior of two parties with asymmetry in information. The signaling hypothesis will motivate individuals with information access to convey signals to those with less information access. The transmitter of an information signal is defined as a party that possesses enough valuable information (good news) or an inadequate quantity of useful information (bad news). In contrast, the recipient of the information signal is defined as the information's user. The stock market is frequently related to signaling theory, as there will always be an information imbalance between corporations and investors [18]. However, information asymmetry may be mitigated by sending management signals to investors. The signal is an activity done by management that informs investors about management's outlook for the company's future [19]; some of the signals are CSR reporting and company financial performance.

Some studies have investigated the effect of CSR reporting and financial condition on business value in the banking sector [5, 9, 11, 13, 14, 20]. These studies, however, employ limited financial ratios such as return on asset and return on equity only. There are specific financial ratios that need to be explored in the banking industry on the association between bank financial condition and bank's business value. This study contributes to the existing literature by examining bank-specific financial ratios such as capital adequacy ratio, net interest margin, loan to deposit ratio, non-performing loan, and operating cost to operating income ratio. This study provides insight into which financial ratios, together with CSR disclosures other than ROE and ROA, would significantly explain the bank's firm value.

2.2 Hypotheses Development

2.2.1 Corporate Social and Environmental Reporting

The level at which a company shares information about its social and environmental activities may deliver an indicator to stockholder that the corporation is doing well in terms of CSR. The reporting shows how the company runs its daily operation in a sustainable business. Hence, corporate and social reporting encourages shareholders to place their money in the business, as evidenced by the increased share price and firm value [12, 14]. The investigation of the positive association of CSR on firm value has been confirmed by previous studies across countries, for example, in China [6], in Korea [10], in Thailand [21], and in Indonesia [8, 9, 11, 12, 22]. However, a study on Islamic banks in the Gulf Cooperation Council found that CSR negatively affects firm value [13]. This study expects that reporting activities on product responsibility, human rights, and climate change-related obstacles will increase firm value. Therefore, this study predicts this hypothesis.

H1: corporate social and environmental performance positively affects a bank's firm value.

2.2.2 Financial Performance

Naz et al. [23] define financial performance as [23]a measure of a company's financial health over a specific period. A set of financial ratios is used to assess the company's financial performance. The ratios are performed on financial statements such as the balance sheet, income statement, and cash flow statement to examine a business's operational and financial viability by considering factors such as its productivity, cash, income, and solvency. These indicators are tracked over time to look into detail if the indicators improve or worsen. Additionally, ratios are compared among firms in the same industry to determine how they compare and to gain a sense of comparative values. Ratio analysis is a critical technique in the fundamental analysis [24].

The improved corporate performance will result in a rise in the business' value. According to Ochego et al. [20], commercial banks in Kenya with a great company value embrace more excellent financial condition and effective corporate governance. Similarly, some previous studies confirm that financial performance affects corporate value [8, 11, 25–28]. Therefore, this study posits the following hypothesis.

H2: bank's financial performance positively affects the bank's business' value.

3 Research Method

3.1 Research Sampling and Data

This research scrutinizes the level of CSR disclosure among banking corporations listed on IDX from 2016 to 2018. Therefore, the study population is banking corporations listed on IDX from 2016 to 2018. The research sample is then selected on the basis of the following considerations. First, the company has CSR reporting available either in annual reports or sustainability reports. Second, the reports are available and complete during the three years of observations. Third, data related to examined variables are also available and complete during the three years. There were 45 banks listed from 2016 to 2018. Three banks had incomplete annual reports or data. Then nine banks were omitted because of outlier data. The ending sample comprised 33 banks for three years of observations, generating 99 firm-years observations. Data related to the bank's financial performance is available in the annual report. The year 2016–2018 was chosen because they were the latest data for this research.

3.2 Firm Value

Firm value was measured by the Price to Book Value (or PBV) ratio measures the current stock price relative to the book value of a firm. The price-to-book value (PBV) ratio compares the current stock price of a firm to its historical book value. PBV is also a measure to see whether a company's shares are expensive or cheap. The way to find the PBV is by dividing the stock price by the book value per share, dividing the equity value by the number of outstanding shares [29, 30].

3.3 Financial Performance

The present study utilizes seven financial ratios to assess bank financial performance. The financial ratios are Return on Equity (ROE) net interest margin (NIM), net profit margin (NPM), non-performing loan (NPL), operating cost to operating income (BOPO), capital adequacy ratio (CAR), return on equity (ROE), and loan to deposit ratio (LDR) [24, 31]. The first three ratios are included in profitability ratios. ROE is the division of net income to equity. In general, a ROE indicates that a corporation is making better use of its capital in producing earnings. [32]. NPM is a ratio that describes the bank's profit (net income) compared to the income received from its operational activities. NIM is a ratio used to analyse how much net interest income is compared to the company's productive assets. NIM is calculated by interest income (interest revenue minus interest expense) divided by the average value of the bank's productive asset. Bank's productive asset refers to "assets that generate interest (interest-bearing assets)" [31].

BOPO is the division of operating cost to operating income. The smaller the bank's BOPO, the better it manages its operational expenses. Therefore it means that the bank will make more money the more efficient it is at cutting costs [31].

The capital adequacy ratio (CAR) refers to how much capital a bank has relative to the amount of its risk-weighted assets. The CAR measures a bank's ability to cover all risks associated with its earning assets, principally loans. Under CAR, banks are required to put up capital equivalent to a certain share of their total earning assets. In order to comply with the Indonesian Central Bank Regulation [33], all Indonesian commercial banks must now have a minimum capital of 8% of total risk-weighted assets (risk-weighted assets). Banks frequently keep capital ratios over the statutory requirement to develop their loan activity. The spread between interest earned on loans and deposits will pay for itself, allowing for higher capital ratios to be maintained at minimal cost [31].

LDR is a ratio of the total loan divided by the total deposit. LDR is the most critical statistic for assessing a bank's liquidity. In this context, loans are defined as deposits made into a conventional bank. It can be assumed that a bank with a low LDR has more liquid assets than necessary, possibly has lower earnings, and is therefore less risky than an institution with a higher LDR. However, a high LDR implies that a bank has increased its financial stress by excessive lending and signals the danger that the bank may have to sell certain loans at a loss to pay depositor claims. A high LDR number indicates decreased liquidity [24].

NPL is the percentage of the number of non-performing loans to total loans. The banking sector is also known as a risk industry due to the nature of each bank's commercial activity. Because banks are primarily intermediaries, their main risk is credit risk. The ratio of non-performing loans is used as a proxy for credit risk. Therefore, the higher the NPL, the higher the risk of a bank [24].

3.4 Corporate Social and Environmental Reporting (CSR)

The current research uses a disclosure checklist to assess CSR disclosure. The checklist was adapted from the G4 Sustainability Framework of the Global Reporting Initiative (GRI), of which the total checklist item number is 91. The present study utilizes an unweighted technique to rating CSR disclosure. Thus it considers just the existence of statements linked to disclosure rather than the quality of the given material [34]. The classification is as follows. If the object is disclosed, it gets a 1, otherwise a 0. The total number of disclosed items was then divided by the maximum achievable CSR disclosure index score (91). Therefore, the CSR disclosures of a bank company are expressed in percentage. The utilization of the GRI G4 index of disclosure in measuring the CSR reporting in this study follows previous studies [9, 12, 14, 35].

3.5 Data Analysis Technique

This study utilizes multivariate regression to test whether CSR reporting and financial performance affect a bank's firm value. The regression model is presented as follows. This study also conducts a classical assumption test before applying multivariate regression.

$$\begin{aligned} \mathrm{PBV} = \alpha + \beta 1\mathrm{ROE} + \beta 2\mathrm{NPM} + \beta 3\mathrm{BOPO} + \beta 4\mathrm{NPL} + \beta 5\mathrm{NIM} + \beta 6\mathrm{CAR} \\ + \beta 7\mathrm{LDR} + \beta 8\mathrm{CSR} + \in \end{aligned} \tag{1}$$

4 Result and Discussion

4.1 Descriptive Statistic

Table 1 portrays the descriptive statistic of variables used in the study. The lowest and highest value of PBV is 0.22 and 5.45, respectively, with a mean score is 1.65. The

Table 1. Descriptive statistics

Variables	Min	Max	Mean	SD
PBV	0.22	5.45	1.65	1.077
ROE	−38.3	32.89	8.94	7.90
NPM	−45.03	149.36	14.81	17.49
BOPO	48.80	151.19	84.59	14.97
NPL	0.01	6.37	1.73	1.14
NIM	1.53	12.00	5.36	1.82
CAR	10.52	66.43	22.34	7.43
LDR	41.99	145.26	84.26	15.53
CSR	0.08	0.44	0.26	0.08
N	99	99	99	99

Regional Development Bank of Banten achieved the maximum score of PBV in 2016. The number suggests that the bank stock price is 5.45 times higher than its book value. Bank Artha Graha International achieved the lowest score of PBV in 2018. The highest and the lowest ROE are 32.89 and −38.3, respectively, with the average score of ROE is 8.94. The bank that achieved the highest profitability is Bank Harda International in 2018. The average value of NPM, BOPO, and NIM is 14.81, 84.89, 5.36, respectively. The lowest ratio of non-performing loans is 0.01, with the average value of NPL is 1.73. The bank that has the lowest bad debt was Bank Nasional Nobu in 2016. The average value of CAR and LDR is 22.34 percent and 84.26 percent, respectively. In terms of bank performance assessment, those values are good as CAR is above 8 percent and the LDR is below 100 percent [33]. The highest capital adequacy score was achieved by Bank Ina Pradana in 2017, while Bank Woori Saudara Indonesia achieved the highest score loan per deposit in 2018.

As presented in the table, the lowest score of CSR disclosure is only 8 percent of the total CSR disclosure in the checklist. While the highest score of CSR is about 44 percent of the total disclosure in the index, the average score of the disclosure is 26 percent. It suggests that CSR reporting in the banking industry listed on IDX is low, specifically when it compares to other industries such as manufacturing, 31 percent [36]. The banking industry's low level of CSR reporting is in line with Tangngisalu [35], which states that banking firms' CSR disclosure is distinct from mining, plantation, manufacturing, and even service organizations, such as transportation service companies. The key distinction is the absence of environmental accountability; in other words, a bank is classified as a corporate entity with low pollution. However, previous studies about CSR in Indonesia conducted in the environmentally sensitive industry found that CSR reporting is relatively low compared to other countries [37–39].

4.2 Results of Multivariate Regression

This research applies multivariate regression to test the impact of financial condition and CSR disclosure on business value. The results of the regression are depicted in Table 2. This study also assesses the classical assumption test as a prerequisite test to run the regression. The Kolmogorov Smirnov significant value reflects the result of the normality test in Table 2, which is above 0.05 (0.098). It indicates that the data in the regression model is normally distributed. Since the VIF and Tolerance are less than ten and greater than 0.1, respectively, the regression model is likewise free of multicollinearity.

As shown in Table 2, two financial performance measurements, namely ROE and CAR, positively affect firm value, significant at a 1 percent level. It indicates that a bank's profitability and capital adequacy ratio increase its firm value in the stock market. The result suggests that the bank's stock price will be higher if the ROE and CAR of the bank are also higher. In other words, the investor is more confident in investing their money in a bank with higher profitability and capital. The positive impact of ROE on a bank's firm value is consistent with previous studies [8, 11]. Meanwhile, LDR negatively impacts firm value, significant at a 5 percent level. The results indicate that if the loan to deposit ratio increases, it will reduce its firm value. It suggests that investors are careful in investing their money in bank stocks with high loan deposit ratios. Investors tend to buy shares in banks whose loans given to borrowers are smaller than the deposits received by the bank.

Table 2 also suggests that CSR does not affect the bank's firm value. The result advocates that investors in investing their money in the banking industry do not consider the company's social and environmental reporting but the company's financial condition. The finding that CSR reporting does not impact on bank's firm value is consistent with [14, 15], which found that CSR disclosure did not have any relationship with firm value. However, the finding contradicts Estiasih et al. [22] and Fadrul et al. [12], which found that CSR reporting significantly increases firm value in the manufacturing sector and mining sector, respectively. The finding contradicts the study conducted in Korea [10] and China [6]. The inconsistent finding is probably related to the difference in the industry sector that is environmentally sensitive and non-environmentally sensitive. As stated by [40], the value effect of CSR efforts is greatly influenced by the firm's relative position in the industry in which it operates. The non-significant effect of CSR on banks' firm value is probably also due to the moderate level of CSR reported by the sample banks. As presented in Table 1, the mean value of CSR reporting is about 26 percent, with the maximum value is 44 percent. The numbers are low because below 50%, with the standard deviation is also low (0.08), which means there is no variation in the CSR disclosure reported in the annual bank report. Therefore, CSR does not influence a bank's firm value.

As depicted in Table 2, NPM, NIM, BOPO, and NPL do not affect the bank's firm value. The insignificant association between NPL and the bank's firm value is not consistent with [41], which found that NPL positively influences the bank's firm value. Again, the difference in the number of sample and sample periods is probably the reason for inconsistencies. However, these financial ratios and CSR have a simultaneous effect of increasing firm value, significant at the 1 percent level. With an adjusted R^2 of 0.203, the regression model results can predict approximately 20.3 percent of the range of factors

Table 2. Result of multivariate regression test

Variables	B	t	Sig	Tolerance	VIF
Constant	1.765	1.452	0.150		
ROE	0.042	2.827	0.006***	0.616	1.623
NPM	−0.002	−0.339	0.735	0.617	1.619
BOPO	−0.003	−0.341	0.734	0.498	2.007
NPL	−0.093	−1.109	0.270	0.913	1.095
NIM	−0.006	−0.097	0.923	0.713	1.403
CAR	0.044	3.351	0.001***	0.867	1.154
LDR	−0.018	−2.599	0.011**	0.729	1.372
CSR	1.607	1.322	1.89	0.727	1.375
F Value (sig)			4.115 (0.000)***		
Adjusted R^2			0.203		
Kolmogrov Smirnov Sig			0.098		

Note: *** symbolises significant at 1%; ** symbolises significant at 5%

that influence the bank's firm value, as shown in Table 2. At the same time, the remaining 79.7 percent is comprised of aspects that were not included in the research.

5 Conclusion and Limitation

This research assesses the effect of CSR reporting and financial performance on the firm value of banks listed on IDX. Results of data analysis indicate that bank financial performance indicators, namely capital adequacy ratio and return on equity, are likely to increase firm value. Meanwhile, the loan to deposit ratio is negatively associated with the bank's firm value. CSR reporting contains corporate social activities and environmental performance data such as the organization's influence on climate change and the environment, its success in mitigating such impacts, and its commitment to sustainable and green development. The reporting does not impact the bank's firm value. The results suggest that in IDX, investors will invest their money in banks with good financial performance without paying attention to the CSR activities and CSR reporting carried out by the bank.

The research article deteriorates from boundaries that may be tackled in the subsequent work. First, in scoring the CSR disclosures, subjectivity is inevitable. So that in further research, scoring can be done by two different people to see the consistency. Second, the research results only apply to the banking sector, which may not be generalized to other sectors. Therefore, future work may examine other industries to find out the contrasts.

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