International Journal of Economics, Business and Management Research

Vol. 7, No.08; 2023

ISSN: 2456-7760

Corporate Social Responsibilities and Firm Values: Evidence from Indonesia

Khristina Yunita[1], Mustaruddin Saleh[2], Wendy[3]

[1]Fakultas Ekonomi dan Bisnis Universitas Tanjungpura
Jalan Prof. Dr. Hadari Nawawi, Pontianak 78124, Indonesia

[2]Fakultas Ekonomi dan Bisnis Universitas Tanjungpura
Jalan Prof. Dr. Hadari Nawawi, Pontianak 78124, Indonesia

[3]Fakultas Ekonomi dan Bisnis Universitas Tanjungpura
Jalan Prof. Dr. Hadari Nawawi, Pontianak 78124, Indonesia

doi: 10.51505/IJEBMR.2023.7816 URL: https://doi.org/10.51505/IJEBMR.2023.7816

Received: July 19, 2023 Accepted: July 25, 2023 Online Published: Aug 29, 2023

Abstract

This study examines the effect of corporate social responsibilities (CSR) on the financial sector firms' value in Indonesia. Furthermore, this research also tries to prove the differences in CSR expenditures between firms that are politically connected and those that are not connected. There are five sub-sectors in the Financial sector: banking, insurance, financing, others, and securities. The final sample size is 437 firm annual reports from 2014 to 2021. The results show that CSR influences firm value positively and significantly. Another interesting finding is the significant difference in CSR expenditure between politically and non-politically connected firms.

Keywords: corporate social responsibilities, firm values, political connection, Indonesia

1. Introduction

CSR is an obligation for all firms in Indonesia and is regulated by Law No. 40 of 2007. All the firms in Indonesia have to obey this obligation and make the budget for CSR implementation. CSR is always an exciting issue, mainly when associated with political aspects. The misuse of CSR funds for the benefit of political parties and presidential campaigns in 2014 and 2019 became a hot issue. Coupled with a statement from the chairman of PPATK in Kontan media in 2013, which stated that there were indications of misused CSR funds by BUMN for the benefit of certain political parties, the banking sector was considered a CSR contributor prone to fraud.

CSR is a firm's commitment to improving community welfare through sound business practices and contributing some of the firm's resources. Firms in Indonesia are required to carry out CSR programs. Laws and government regulations regulate this program. The funds firms allocate for CSR vary from 2% to 2.5%, up to 3% of the firm's annual profits. The main objective of CSR is to align a firm's social and environmental activities with its business goals and values. In contrast, the benefits of CSR include:

Vol. 7, No.08; 2023

ISSN: 2456-7760

Increasing the reputation and good image of the firm,

- Obtaining a good perception of a responsible firm from stakeholders,
- Providing convenience in building good relations and establishing cooperation with various parties, and
- Reducing the possibility of a crisis that the firm will experience.

CSR is also considered capable of influencing firm value due to good stakeholder perceptions. CSR is considered capable of increasing the value of the firm due to a reduction in conflict with stakeholders. The firms that implement CSR have better long-term performance; even though these firms may incur some initial costs arising from their involvement in CSR, they still earn higher sales and profits due to the reputational effect of involvement in the engagements or programs, as well as long-term cost reduction and social improvement (Poddi & Vergalli, 2008). Nevertheless, CSR harms stock prices if management receives personal benefits from adopting it. In contrast, a positive effect showed that CSR policies are adopted to improve stakeholder relations (Krüger, 2015).

Over the last few years, CSR has become the focus of attention for researchers and stakeholders. CSR content is now more diverse and rich. CSR can include donations, fundraising, environmental protection, and others (Xiao et al., 2020). Public firms implement CSR because they believe it can strategically grow corporate value and spread risk. On the other hand, investment in CSR can also reduce firm value due to increased costs and a shift in the focus of operational objectives (Wang & Bansal, 2012).

Based on the affirmative viewpoint and the constructed social impact hypothesis (Cornell & Shapiro, 1987), solid social performance leads to more substantial financial outcomes. This social performance enhances the firm's business reputation, reduces commercial risks, and gains support from the authorities. This support from the authorities can attract investment, satisfy the expectations of various stakeholders, and ultimately improve firm performance. The social impact hypothesis concludes that there is a positive relationship between CSR and financial performance.

Existing theoretical research has yet to lead to the same consensus about the effect of CSR on firm value or financial performance (Buchanan et al., 2018). Referring to conflict resolution theory, high CSR activity can generate high corporate value by reducing conflicts of interest between managers and non-investment stakeholders, increasing the firm's reputation and profitability. However, from the point of view of investment theory, this CSR practice is expensive, so it can raise concerns about over-investment, especially if the firm is experiencing a financial crisis (Buchanan et al., 2018).

The empirical research shows the different effects of CSR on firm value. Some studies show a positive effect, while others show negative CSR results on firm value. The existence of different aspects of CSR activities, such as community-related CSR versus products or legal versus normative CSR, has various implications for corporate value (Bird et al., 2007; Jo & Harjoto, 2011). CSR can influence firm performance through institutional arrangements, namely the transitional economy. This arrangement creates channels for CSR so that it can influence firm performance. This channel is called a political network (Lin et al., 2015).

Even though the research results are different, we can say that CSR can influence the firm's value. Effective CSR practices can help build a firm's trust and reputation, improving financial performance. Transparent and positive CSR reporting can also affect the perceptions of investors and the public toward the firm, which can affect its value. CSR can help strengthen a firm's relationship with key stakeholders such as employees, customers, suppliers, and local communities. By taking into account the interests of these stakeholders, the firm can obtain more significant support and minimize the risk of conflicts that can harm the firm's value. In connection with the explanation above, the hypothesis proposed in this study is that CSR positively influences the firm's value.

2. Method

This study uses the annual reports of firms in the financial sector on the Indonesia Stock Exchange. The financial sector comprises five subsectors: banks, financial institutions, insurance, investment funds, and other finance. The sample criterion is an annual report that can be accessed from 2014 to 2021 and has information about the amount of CSR expenditure in rupiah. The number of annual reports observed is 437. We collect the information by visiting the websites of financial sector firms listed on the Indonesia Stock Exchange. We used two methods to collect the data. First, we used quantitative data from the financial data presented in the annual report; second, we did the content analysis to find information about the political connections carried out by the board of commissioners or board of directors in the sample firms. The financial data collected includes financial ratios and information regarding the backgrounds of the board of directors and the board of Commissioners. This study uses the following variables.

Firm Value (FV)

The dependent variable in this study is firm value. We defined firm value as a reflection of firm performance and proxied it with stock prices. The firm's value reflects the public's assessment of the firm's performance. Firm Value is proxied by Tobin's Q. Tobin's Q is a statistical picture that functions as a proxy for firm value from an investor's perspective. For calculating Tobin's Q, we use the market value of the firm's assets and the replacement value of the firm's assets as the modification firm value formula (Chung & Pruitt, 1994) as follows:

$$Q = \frac{MVS + D}{TA}$$

Where:

MVS (market value of all outstanding shares) is the market value of the shares obtained by multiplying the number of outstanding shares by the share price (Outstanding Shares * Stock Price).

D (Debt) is the market value of debt, where this value can be calculated using the following equation:

$$D = (AVCL - AVCA) + AVLTD$$

AVCL = Accounting Value of the firm's Current Liabilities

Current Liabilities = Short Term Debt + Taxes Payable

AVLTD = Accounting value of the firm's Long Term Debt

AVCA = Accounting value of the firm's Current Assets

Current Assets = Cash + Account Receivable + Inventories

TA = Firm's assets.

Corporate Social Responsibilities (CSR)

The independent variable in this study is Corporate Social Responsibilities (CSR). CSR is defined as the firm's responsibility for the impact caused by the firm's activities on society and the environment ethically and transparently, carried out consistently for the welfare of society through sustainable development, and always trying to pay attention to stakeholders' expectations.

We calculate the CSR expenditure based on data presented by the firms in the annual or sustainability reports. We will take all the scores without considering if they have a positive or negative score. We sorted the CSR costs and then put them in a formulation adapted from (Monzur & Habib, 2017) as follows:

$$CSR_{index} = \frac{CSIR_{it} - MinCSR_{jt}}{MaxCSR_{jt} - MinCSR_{jt}}$$

Where:

CSR_{it}: the total firm spending for CSR each year in IDR.

Min_{CSRjt}: the minimum CSR spending for the same industry each year in IDR.

Max_{CSRjt}: the maximum CSR spending for the same industry each year in IDR..

Based on these two variables, we propose a research model.

$$FVal_{it} = \alpha_0 + \beta_1 CSR_{it} + \varepsilon_{it}$$

Where:

$FVal_{it}$ = Firm Value

CSR_{it} = Corporate Social Responsibilities

We also conduct tests to distinguish whether there are differences in CSR spending between politically connected and non-politically connected firms. We use the difference test to determine whether there is a difference. We use a dummy to classify the firms. For politically connected firms, we give a score of 1, while for those not politically connected, we give a score of 0.

3. Results

We run 437 annual reports after sample selection and use regression to examine the effect of CSR on firm value. We regressed the CSR index on firm value to measure the impact. After the test, we have the results as follows.

Tabel 1. The Results of CSR Testing on Firm Values

fv	Coef.	St.Err.	t-value	p-value	[95% Conf	Interval]	Sig
csrindex	86.238	19.531	4.42	0.00	47.85	124.626	***
sector: insurance base	0	.	.	.	.	.	
Others	-1.147	16.455	-0.07	.944	-33.489	31.194	
Financing	-.774	10.956	-0.07	.944	-22.309	20.76	
Banking	-.216	8.99	-0.02	.981	-17.885	17.454	
Securities	4.118	17.309	0.24	.812	-29.904	38.139	
Constant	.798	8.225	0.10	.923	-15.369	16.964	

Mean dependent var	5.303	SD dependent var	58.000
R-squared	0.046	Number of obs	437
F-test	4.130	Prob > F	0.001
Akaike crit. (AIC)	4779.530	Bayesian crit. (BIC)	4804.010

**** p<.01, ** p<.05, * p<.1*

According to Table 1, CSR can influence firm value significantly. For each sub-sector, it turns out that CSR does not impact firm value. This test intends to test the effect of CSR on firm value directly.

After we find that CSR positively and significantly influences firm value, we prove whether there are significant differences in CSR spending between politically connected and non-politically connected firms. We classify financial sector firms into two groups: politically connected and non-politically connected. We score one if the firms are in the first group and 0 if not. The test results show that there are significant differences between firms that are politically connected and not politically connected. We presented the result in the following table.

Table 2. The CSR Expenditure Differences Between Politically Connected and Not Politically Connected Firms

Description	**obs**	**Mean1**	**Mean2**	**dif**	***St Err***	***t value***	***p value***	***sig***
pc dummy - csrindex	437	.531	0.054	.477	.022	21.1	0.000	***

*** p<.01, ** p<.05, * p<.1

4. Discussion

Our test results show that CSR can influence firm value significantly and positively. The results of this study support the previous studies (Aula & Mai, 2022; Machmuddah et al., 2020; Saleh et al., 2011; Wirawan et al., 2020). Resource Dependence Theory emphasizes the importance of firm access to external resources so that firms that carry out effective and trusted CSR initiatives can build strong relationships with external stakeholders such as consumers, investors, and the community. Through the support and acceptance provided by these stakeholders, the firm can secure valuable resources, such as capital, reputation, or customer loyalty, which can ultimately increase the firm's value.

Firms can maintain and enhance their image and reputation through CSR by investing in socially and environmentally responsible business practices. CSR helps to reduce the adverse risks associated with ethical, environmental, or political engagement violations that could damage the public's perception of the firm. In the long term, managing reputation risk can support firm value by maintaining the trust and loyalty of stakeholders. By implementing effective CSR, firms can manage and utilize external resources, reduce reputation risk, gain competitive advantage, and meet regulatory requirements. All of these contribute to increasing the firm's value in the long term, according to the perspective of Resource Dependence Theory.

We also conducted an additional test to see the differences in CSR expenditures between politically and non-politically connected firms. We use CSR expenditures from annual reports or sustainability reports. Our test results show that there are significant differences between firms that are politically connected and those that are not related to CSR expenditure. Financial sector firms with political connections incur more significant CSR expenditure than firms that do not have political connections. These results support the results of the previous research (Ananzeh et al., 2023; Huang & Zhao, 2016; Nainggolan et al., 2021).

Politically connected firms tend to incur more CSR costs because they consider several factors. Political connections provide firms access to a broader political network and establish closeness with political leaders, political parties, and related organizations. CSR is one of the media used by politically connected firms to strengthen their relationship with the ruling government. CSR can be an effective tool in influencing political stakeholders and increasing the firm's legitimacy. By building partnerships or involving political stakeholders in CSR programs, firms can gain valuable political support in facing business challenges or gaining certain competitive advantages.

Politically connected firms will gain better access to resources and business opportunities and influence existing policies and regulations. The firm will continue to strive to maintain this relationship. CSR is a tool used to maintain good relations with the government. In addition, implementing CSR is an effort to meet the government's expectations and maintain a positive image in the public eye. Politically connected firms may expect protection and support from the government or government officials in various ways, such as securing project contracts, obtaining business licenses, or avoiding legal trouble. CSR can be a tool to gain this support because CSR can strengthen relations with the government and create stronger bonds. CSR can help firms build a good image in the eyes of the public and create the trust needed to maintain relations with the government.

Active CSR implementation can benefit the firm's reputation and entity branding. In a political context, solid political connections can give firms a competitive advantage in winning public trust and support. Firms that invest more in CSR will reap positive social and environmental benefits. Politically connected firms will try to build an image as firms that are responsible and committed to the interests of the wider community. A good image will help the firm win the hearts and minds of consumers, stakeholders, and society. The general conclusion related to the implementation of CSR is that politically connected firms have a greater tendency to implement CSR as a business strategy that can provide long-term benefits.

5. Conclusion

The result shows that CSR can influence firm value significantly and positively. This research differs from previous research because the previous research excluded the financial sector, while this study used a sample of financial sector firms. The additional findings show significant differences in CSR expenditure between politically and non-politically connected firms. Financial sector firms with political connections incur more significant CSR expenditure than firms that do not have political connections.

Limitation and Recommendation

This research has limitations. The limitation is the measurement of CSR spending by the Firm. Not all firms provide complete information regarding the amount of their CSR spending. Most sample firms present their expenditure in total, not per dimension. Therefore, future research can consider CSR spending on broader dimensions.

References

Ananzeh, H., Obeid, M., Shbail, A., Al, H., & Khatib, S. F. A. (2023). Political connection , ownership concentration , and corporate social responsibility disclosure quality (CSRD): empirical evidence from Jordan. *International Journal of Disclosure and Governance*, *20*(1), 83–98. https://doi.org/10.1057/s41310-022-00167-z

Aula, R., & Mai, M. U. (2022). The Effect of Corporate Social Responsibility Disclosure on the Performance of Islamic Banks in Indonesia. *Jurnal Manajemen Bisnis*, *13*(1), 93–107. https://doi.org/10.18196/mb.v13i1.12832

Bird, R., Hall, A. D., Momentè, F., & Reggiani, F. (2007). What Corporate Social Responsibility Activities are Valued by the Market? *Journal of Business Ethics Volume*, *76*(2), 189–206. https://doi.org/10.1007/s10551-006-9268-1

Buchanan, B., Cao, C. X., & Chen, C. (2018). Corporate social responsibility, firm value, and influential institutional ownership. *Journal of Corporate Finance*, *52*, 73–95. https://doi.org/10.1016/j.jcorpfin.2018.07.004

Cornell, B., & Shapiro, A. (1987). An Empirical Investigation of the Relationship Between Change in Corporate Social Performance and Financial Performance: A Stakeholder Theory Perspective. *Financial Management*, *16*, 5–14. http://www.jstor.org/stable/3665543

Huang, H., & Zhao, Z. (2016). The influence of political connection on corporate social responsibility——evidence from Listed private firms in China. *International Journal of Corporate Social Responsibility*, *1*(1), 1–19. https://doi.org/10.1186/s40991-016-0007-3

Jo, H., & Harjoto, M. A. (2011). Corporate Governance and Firm Value: The Impact of Corporate Social Responsibility. *Journal of Business Ethics*, *103*(3), 351–383. http://www.jstor.org/stable/41476031

Kee H. Chung, & Pruitt, S. W. (1994). A Simple Approximation of Tobin's q. *Financial Management*, *23*(3), 70–74. https://doi.org/10.2307/3665623

Krüger, P. (2015). Corporate goodness and shareholder wealth. *Journal of Financial Economics*, *115*(2), 304–329. doi: 10.1016/j.jfineco.2014.09.008

Lin, K. J., Tan, J., Zhao, L., & Karim, K. (2015). In the name of charity : Political connections and strategic corporate social responsibility in a transition economy. *Journal of Corporate Finance*, *32*, 327–346. https://doi.org/10.1016/j.jcorpfin.2014.10.007

Machmuddah, Z., Sari, D. W., & Utomo, S. D. (2020). Corporate Social Responsibility , Profitability and Firm Value : Evidence from Indonesia. *Journal of Asian Finance, Economics and Business*, *7*(9), 631–638. https://doi.org/10.13106/jafeb.2020.vol7.no9.631

Monzur, M., & Habib, A. (2017). Journal of Contemporary Accounting & Economics Corporate life cycle , organizational financial resources and. *Journal of Contemporary Accounting & Economics*, *13*(1), 20–36. https://doi.org/10.1016/j.jcae.2017.01.002

Nainggolan, Y. A., Astuti, E. D., Rahadi, R. A., & Afgani, K. F. (2021). Political Connection and Corporate Social Responsibilities: Evidence From Indonesia. *International Journal of Business and Society, 22*(2), 922–940. doi.org/10.33736/ijbs.3767.2021

Poddi, L., & Vergalli, S. (2008). *Does Corporate Social Responsibility Affect Firms' Performance?*

Saleh, M., Zulkifli, N., & Muhamad, R. (2011). Looking for evidence of the relationship between corporate social responsibility and corporate financial performance in an emerging market. *Asia-Pacific Journal of Business Administration*, *3*(2), 165–190. https://doi.org/10.1108/17574321111169849

Wang, T., & Bansal, P. (2012). Social responsibility in new ventures: profiting from a long-term orientation. *Strategic Management Journal*, *33*(10), 1135–1153. https://doi.org/10.1002/smj.1962

Wirawan, A. W., Falah, L. J., Kusumadewi, L., Adhariani, D., & Djakman, C. D. (2020). The Effect of Corporate Social Responsibility on the Firm Value with Risk Management as a Moderating Variable. *Journal of Asia-Pacific Business ISSN:*, *21*(2), 143–160. https://doi.org/10.1080/10599231.2020.1745051