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The Effect of Islamic Social Reporting on Firm Value (Case Study on Islamic Banks In Indonesia)

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Abstract

This study aims to determine the effect of islamic social reporting against firm value. The development of ISR includes five themes, they are social, labor, enviroment, corporate governance and service/ product. This study identified 43 disclosure index items of ISR main theme. Data analysis using multiple linier regression. The data used is secondary data obtained form annual reports of islamic banks registered on Bank Umum Syariah by taking a sample of 12 islamis banks. The result indicate that islamic social reporting simultaneously influences firm value. Partially only 3 indicators that have effect on firm value, they are social influence of 0,07977; labor influence of 0,11304; and environment influence of 0,15579.

Keywords: islamic social reporting, social, labor, environment, corporate governance, service and product, and firm value.

1. Introduction

The Islamic Banking sector has been accused of being indirectly involved in facilitating the transfer of funds to terrorist organizations (de Goede, 2003; Pollard and Samers, 2007). To counter these perceptions the Islamic banking sector is required to portray itself as an ethical and socially responsible financing option, and has sought to strengthen reporting practices to demonstrate transparency in its operations (Khan, 2010). Sharia banks are required to comply with the rules and regulations set out for the conventional banking sector that meet the requirements of the sharia known as ISR. ISR is an extension of social reporting that helps companies make decisions to fulfill their obligations to others and to creators and includes not only the expectations of the wider community regarding the company's role in the economy but also on a spiritual and religious perspective. In particular, the ISR index emphasizes social justice regarding the rights of minorities, employees and the environment (Haniffa, 2002).

Branco and Rodrigues (2008: 683) explain that managers should disclose CSR information that meets the needs of various stakeholders. Failure to do so can result in withdrawal of support and adversely affect the company's reputation / value socially. So that it can reduce the economic benefits for the organization. Failure to meet the demands of various stakeholders can lead to withdrawal of support as well as bad perceptions that arise on the organization's reputation and economic sustainability. This implies that the perceptions of many stakeholders contribute to the creation of a company's reputation, which in turn can generate economic benefits. The reputation and value of the company will show a positive trend when the company is involved in CSR activities and is disclosed

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in the annual report. These companies are considered to have good value corporate values and intangible assets which can be translated positively in many ways such as stimulating customers, fostering investment interest, attracting the best talent, motivating employees, generating job satisfaction, generating more positive and accepting media coverage. increased value of financial analysts (Brammers and Pavelin, 2004: 705).

In line with this, the ACCA (2007) web-based survey of 244 respondents consisting of representatives from companies, academia, government and international agencies reported that thirty percent of respondents stated that CSR reporting is very important while 50 percent stated that it is somewhat important in building a company's reputation. Only a small proportion of respondents (20 percent) stated that the reporting had no impact on their view of the company's reputation. Previous empirical studies highlighted that CSR reporting has become an increasingly important part of how stakeholders assess a company's reputation. In line with this, Bebbington et al (2008: 373) argue that failure to manage CSR wisely will affect the company's reputation. This suggests that CSR disclosure is a tool by which management can influence the perceptions of various stakeholders. With respect to organizations governed by the principles of Islamic moral law (sharia), it is hoped that the stakeholders have certain expectations of the behavioral practices of these organizations.

There are two things that must be considered in disclosing ISR from an Islamic perspective, namely: accountability, social justice and ownership. Western concepts of accountability are usually limited to organizational stakeholders. Accountability refers to the processes that an organization goes through, thus making a commitment to balance the needs of stakeholders in its decision making. This concept is limited to the human world when imagined from a Western perspective. However, from an Islamic point of view this concept is broader. In Islam, accountability is first and foremost to Allah SWT. Briefly capturing the concept of accountability in Islam. Allah has provided mankind with resources and blessings, too many to count. Humans are expected to use this blessing to serve Allah, and on the Day of Judgment, each person must give an account of how he uses it. This awareness should encourage the actions of every Muslim in all aspects of life, be it personal or business, thus it can be said that accountability to Allah implies accountability to society (Othman, Thani and Ghani, 2009).

Social Justice Theory is very important for moral development and learning justice in society. Allah commands to give back trust to those who are trustworthy. Some examples of Islam's emphasis on social justice are: prohibition of usury to prevent exploitation of people, imposition of Zakat to help reduce poverty in society, and recommendations for helping others through charity. In Islamic business, justice includes all transactions with employees, customers, and all members of the communities in which the business operates. Allah is the ultimate owner of everything and man has been entrusted with his resources as trust to be used according to Allah's commandments. This concept is closely related to the concept of accountability because for this entrusted resource each person must be held accountable on the Day of Resurrection. The implication of this concept for Islamic business is that the resources used must be in accordance with Allah's commandments and for the benefit of society. Thus it can be concluded that the three concepts of accountability, social justice and ownership are interrelated and interdependent. In this discussion, of course, it does not only cover ISR disclosures, but examines more deeply from a different point of view, whether the disclosure in the ISR index has an influence on firm value, so that the company can be more enthusiastic in increasing the value of a company.

2. Literature Review

Islamic Social Reporting (ISR)

ISR was first studied by Ross Haniffa in 2002. Then Rohana Othman further developed a more extensive study in 2009 in Malaysia, and until now research is still developing with a similar theme by other researchers. Haniffa (2002) reveals that there are many limitations in conventional social reporting systems, so he proposes a conceptual framework for ISR based on sharia-compliant provisions. ISR is an extension of social reporting that helps companies make decisions to fulfill their obligations to others and to creators and includes not only the expectations of the wider community regarding the company's role in the economy but also on a spiritual and religious perspective (Haniffa, 2002). At ISR, the emphasis on social justice goes beyond reporting on environmental, minority interests and employees. This deals with issues related to the welfare of society related to interests and unfair trade practices (Sulaiman, 2005) such as income distribution (known as zakat). Such concerns are in line with stakeholder theory which explains that management provides information to users to maintain company success. The sustainability and success of the company is tied to the full support of its stakeholders (Ullman, 1985). Therefore, it is important for management to evaluate, identify, and report completely social and environmental information in accordance with stakeholder requests (Mohamed Zain, 2004).

Stakeholder Theory

According to Stakeholder theory, corporate sustainability requires support from stakeholders. The stronger the stakeholders, the more companies will have to adjust. Stakeholders can influence (directly or indirectly) and become the control of assets needed by the company, so that the dominance of stakeholders is determined by the level of control they have over the assets. Therefore, when stakeholders have control over significant resources of the organization, the company is likely to react in a way that satisfies them. The government is one of the important stakeholders for the company, therefore the company will conduct and try to make disclosures based on the rules set by the government. So it is very possible that there will be differences in the disclosure of social responsibility in Islamic Banks due to differences in the existing rules in each country. While the latest research shows that the Islamic social reporting index in Indonesia is the highest in Southeast Asia (Othman, Thani and Ghani, 2009).

Islamic Bank

Islamic banking refers to a system of banking activities that is in accordance with Islamic law (Sharia) in all aspects. Among other things, Shari'ah prohibits dealing with interest and making transactions with an unknown fate (gharar), while it requires transactions to be halal (halal), and also requires Muslims to pay a religious retribution in the form of Zakat. Eliminating interest from their transactions is a basic principle on which Islamic banking is based. Based on this definition, it can be stated that for conventional banks, the main objective is profit maximization, which is in line with the Capitalist world view in which these banks are founded. This situation is not the case for Islamic banks because they are founded on the basis of the Islamic religion. Although, banks are seen as separate and legitimate entities in their own right, in reality they are run by humans.

Islamic banks are thus run by Muslims, and the ultimate goal of a true Muslim is to succeed in this world and the hereafter by pleasing Almighty Allah in all his affairs. For this reason, Islamic banks have their end goal. This is not to imply that profit is not the main objective of Islamic banks;

conversely, Islamic bank managers are expected to strive earnestly to make reasonable profits for both savers and their shareholders, but meanwhile apply Islamic principles in all their transactions (Haniffa, 2002). So unlike conventional banks, profit maximization is not the main goal of Islamic banks, as they have to incorporate profit and morality into their goals.

3. Methodology

Research Design

This research uses descriptive quantitative method by proposing several hypotheses. The descriptive method begins with analyzing the annual report data which is then tabulated to determine the effect of the independent variable on the dependent variable. The data used is secondary data by looking at the reports published by 12 Syari'ah Banks registered in the BUS.

Measurement Data

Dependent Variable

The dependent variable in this study is firm value. To project firm value, it can be seen from Tobin's Q value, which is the ratio to compare the market value of a corporate stock with total assets. Here is the mathematical formulation of Tobin's Q formula:

Tobin's Q =
Information:
Q: firm value
MVE (Market Capitalization): closing price x number of shares outstanding
DEBT (Liabilities): total company debt
TA: total assets / assets

If a ratio value is greater than 1, it means that the company's assets can be purchased at a lower price than the company itself, meaning that the market gives a higher valuation to the company (overvaluation), whereas if the Q ratio is lower than 1, it indicates that the market provides lower rating.

Independent Variable

Islamic Social Reporting (ISR), is an extension of social reporting that helps companies make decisions to fulfill their obligations to others and to creators and includes not only the expectations of the wider community regarding the company's role in the economy but also on a spiritual and religious perspective. There are 43 index / disclosure items from 5 ISR reporting indicators. Each disclosure subject has a value of 1 or 0. A score of 1 will be given if the principal of the ISR disclosure is contained in company data and a value of 0 will be given otherwise. The following is an index of the data used in the ISR disclosure.

Table 1. ISR Index

No	Reporting Items
1	Usury activity
2	Gharar
3	Zakat (includes method and number of recipients)
4	Late tax / bad credit policy
5	Balance of values
6	Value added statement
7	Go green campaign
8	Halal product status
9	Product safety and quality
10	Customer complain
11	Job characteristics (including working hours and employee holidays)
12	Employee training and education
13	Career path
14	Employee engagement
15	Occupational Health and Safety
16	Work environment
17	Employee recruitment
18	The same opportunity
19	Provision of time for worship
20	Provision of a place for worship
21	Sodaqah
22	Waqf
23	Qard hasan
24	Employee donations
25	Educational scholarships
26	Employee scholarships
27	Development and coaching for youth
28	Help for the poor
29	Child health care
30	Giving social gifts
31	Sponsorship of community activities
32	Environmental conservation
33	Care for animals
34	Environmental pollution
35	Repair of public facilities
36	Making public facilities
37	Environmental management policy
38	Environmental audits
39	Sharia compliance
40	Share ownership structure
41	Organizational structure
42	Transparency of financial conditions
43	Anti-corruption policy

Source: Othman, Thani & Ghani (2009).

Hypothesis testing in this study uses multiple linear regression analysis. Tests are carried out to determine the presence or absence and how much influence between the independent variable and the dependent variable. The steps in testing the hypothesis as a whole are preceded by the Classical Assumption Test which consists of: Normality Test; Multicolonierity and Heteroscedasticity. After fulfilling the Classical Assumption Test, Multiple Linear Regression Analysis is carried out with the following results:

4. Result and Discussion

Data analysis in this study was conducted to determine the effect of independent variables on firm value. With the test results shown in the table below:

Table 2. Summary Table of Multiple Linear Regression Results

Variables	Coefficient	t value	Sig.
Constant	55,004	3,265	0,015
Products and Services	-57,732	-1,542	0,730
Labor	11,304	2,111	0,029
Social	7,977	1,938	0,037
Environment	15,579	1,090	0,049
Organizational Governance	-25,889	-0,115	0,833
R-Squared	0,679		
Adj. R-Square	0,575		

Then from the table a multiple linear regression equation is compiled with the following composition:

$$\mathbf{NP = 55{,}004 - 57{,}732\,X1 + 11{,}304\,X2 + 7{,}977\,X3 + 15{,}579\,X4 - 25{,}889\,X5 + e}$$

Information:
NP = Firm Value
X1 = Products and Services
X2 = Labor
X3 = Social
X4 = Environment
X5 = Organizational Governance

From the linear multiple regression equation above, it can be described as follows:

a. The firm value is constant at 55.004 with a positive value. This shows that if there is a situation where the variables of products and services, labor, social environment and organizational governance are equal to zero, then the firm value is 55.004.
b. The coefficient ($\beta 2$) is 11,304; shows that every time there is an increase in the labor coefficient of 1%, it will have an effect on the increase in firm value of 0.11304 provided that other variables are fixed.
c. The coefficient ($\beta 3$) is 7,977; shows that every time there is a social increase of 1%, there will be an effect on the increase in firm value of 0.07977 on condition that other variables remain.
d. The coefficient ($\beta 4$) is 15.579; shows that every time there is an increase in the environment by 1%, then it affects the increase in firm value by 0.15579 provided that other variables are fixed.

After determining the above equation, it is necessary to carry out the following tests:

1) Partial Test (t test)

Based on the summary table of the Linear Regression Test results above, it can be seen that the independent variables consisting of labor, environment and social have a significant influence on the dependent variable, while organizational governance; There is no indication that products and services have an effect on the dependent variable, which in this study is firm value.

2) Simultaneous Testing (Test F)

This test is conducted to analyze the magnitude of influence simultaneously between the independent variables (X) on the dependent variable (Y), and to determine whether the regression model as formulated above is fit / exist or not. The f test results can be seen in the following table:

Table 3. Simultaneous Testing Results Table (Test f)

Variable	Sig.	Conclusion
Products and Services	0,005	Fit Model / Exist
Labor		
Social		
Environment		
Organizational Governance		

From the table above, it is known that the significance value is 0.005 <0.05, so it can be concluded that the regression model is fit, so simultaneously the independent variables affect firm value. Because overall this social responsibility reporting variable shows the financial performance of Islamic bank institutions, the better the reporting level, the better the financial performance of the Islamic bank. Meanwhile, the financial performance will be used by investors to find out the company's value. So that it can be concluded that the better the level of Islamic social reporting of Islamic banks will affect the increase in the value of these Islamic banks.

3) Coefficient of Determination (R2)

The coefficient of determination is intended to measure how big the equation model in this study explains the variation in the dependent variable. The results of the coefficient of determination (R2) can be seen in the summary table of the regression results listed above.

Based on the table above, it is obtained that the R-Square value is 0.575, thus indicating that 57.5% of the firm's value can be explained by the arrangement of independent variables consisting of products and services, social, labor, organizational governance and the environment. Meanwhile, 42.5% will be explained by variables outside this research model.

This study examines the effect of ISR disclosure on the company's value reputation. The results reveal a significant positive relationship between ISR disclosure on firm value. In addition, these results also highlight management proactively implementing and disclosing ISR activities that meet the needs of various stakeholders. These results contribute to the corporate value disclosure literature by providing new evidence that CSR activities and disclosure from an Islamic perspective are equally important business strategies in creating sustained superior performance for organizations. This is in line with the view that organizations need to develop a stakeholder orientation especially in an environment with increasing pressure from jurisdictions dominated by Islamic stake holders on organizations and engaging in Islamic products to increase their social responsibility from an Islamic perspective. The stakeholder orientation recognizes the importance of addressing the demands of various stakeholder groups. The disclosure of corporate ISR initiatives in annual reports is increasingly being used in communicating CSR initiatives to relevant stakeholders. This in turn strengthens stakeholder relationships and support for the organization which consequently increases firm value.

However, when examined partially, there are only 3 variables that have an influence on firm value. Meanwhile, there are two indicators that do not have a significant effect on firm value. The existence of an indicator of the ISR that has no effect on firm value is also found in research by Ali (2015) which shows that the CSR variable has no effect on firm value. This is because the large number of Islamic banks allocating funds for social responsibility is relatively low, especially in products and services as well as organizational management, whereas when compared to the company's profitability it is classified as large, so that profitability cannot prove its influence in the relationship between ISR and the value of Islamic bank companies.

Besides that, there are three variables from Islamic social reporting which are proven to have an effect on firm value because they have carried out social responsibility well. So that there are many benefits that can be provided to stakeholders, therefore it will lead to satisfaction and appreciation which has a positive impact on increasing firm value. An important dimension of corporate reporting for decision makers is social reporting. The main purpose of social reporting is to determine the impact of corporate actions on the quality of people's lives (Daykin, 2006). In this dimension, ISR reporting plays a particularly important role for Muslim decision makers.

Given the importance of ISR, it is hoped that Sharia organizations / companies can be selective in choosing management and board members in terms of specific qualifications and religious beliefs in formulating strategies and implementing ISR initiatives and disclosures. With respect to Muslim managers and board members, Islamic principles are expected to influence the behavior and decisions of stakeholders.

5. Conclusion

From the results of the calculation, several conclusions can be drawn including:
1. Islamic social reporting which consists of products and services, labor, social, environmental, and organizational governance simultaneously influences firm value.
2. Proportionally only three variables have a significant positive effect, namely labor, social and environmental variables.
3. There are two variables that do not have a significant effect on firm value if partially calculated, namely product and service variables and organizational governance.

Suggestions that can be given in this research include the following:
1. For further research, it is necessary to identify Islamic social reporting as a whole by including investment variables, press releases and the stock market.
2. Further research is suggested to enlarge the research sample, not only covering 12 Islamic banks by digging deeper into reports or annual reports published by Islamic banking companies.
3. Further research is expected to increase the variation of independent variables that can affect firm value such as, capital structure, financial performance and investment decisions.

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