

## Conference Paper

# The Development of CSR Implementation in Indonesia and Its Impact on Company's Financial and Non-financial Performance

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## Abstract

The purpose of this study is to describe the development of corporate social responsibility (CSR) implementation in Indonesian listed companies. After briefly explaining the history and legal basis of CSR implementation in Indonesia, this article tries to deeply and widely describe CSR practices in top 200 Indonesian listed companies during the period of 2014 and 2015. The CSR implementation in Indonesian listed companies was benchmarked to ISO 26000 (guidance on social responsibility) standard in order to compare the CSR practices in Indonesia with global standard. Finally, this article will end with the conclusion on the relationship between the level of CSR practice with company's performance, both financial and non-financial performance. Result indicated that beside there was an improvement, the level of CSR implementation in top 200 listed companies in Indonesia during the period of 2014 and 2015 was generally still low compared to global CSR implementation standard. Companies in finance sector were the leader in implementing CSR practice in accordance to global standard, whereas those in miscellaneous industry as well as trade, services and investment sector were the two industrial group that became the poorest in implementing CSR. This might indicate that more regulations and initiatives need to be taken by related stakeholders such as government, industry association, media, etc. to push and motivate industry to do CSR more like their peer in global context. The second finding was that the level of CSR implementation had positive and significant influence on companies' financial performance, both measured by ROE and ROA, but not companies' non-financial performance, both from the customer and employees perspective. It means that doing better CSR will give financial reward to the company. However, many efforts are still required to convince customers and employees in Indonesia to show the value of CSR to them.

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## 1. Introduction

Corporate social responsibility (CSR) management in the global context has moved fast from planning and implementation to evaluation and control phase. As a tool for CSR planning and implementation, starting from 1 November 2010, the International Standard Organization (ISO) has officially issued ISO 26000 as a guidance for organization social responsibility. Meanwhile, as a tool for CSR evaluation and control, many companies have published their CSR report, namely, sustainability reporting based on a standard issued by Global Reporting Initiative (GRI).

CSR is a concept in which a company has responsibility not only in economic sense but also in social and environmental senses. Consequently, a company must not only need to satisfy the need of its shareholder, that is, to maximize profit, but also have to address the need of its other stakeholders equally. These other stakeholders include internal stakeholders—customers, employees and suppliers—as well as external stakeholders—government, competitors, consumers advocates, environmentalist and special interest groups (Freeman, 1984: 25).

In the last 10 years, various governing bodies such as governments, financial regulators or stock exchanges across the globe had issued several regulations and made some initiatives to improve CSR practices. For example, UK government since 2006 had obligated all listed companies to report on environment, labour, social and society aspects. Likewise, Swedish government since 2007 required all Swedish Government-owned Enterprises to publish CSR report according to GRI. More recently, since 2015, the governing bodies had made compulsory for certain Taiwanese listed companies to publish company's CSR report according to the GRI Generation 4 (GRI G4). The Singaporean authority in that year also released a rule that all Singapore's listed companies had to publish CSR report using the latest G4 standard by 31 December 2015 (KPMG, 2009; CSR Asia, 2015; Ho, 2009).

Indonesia is currently the only country in South East Asia region that became the member country of G-20 (group of 20 of the world's largest economies). Many have predicted that Indonesia will play a more important role in the future. McKinsey Global Institute (2012), for example, stated that Indonesia would become the top seven economies in the world in 2030. A global accounting firm, PWC (2015), even forecasted that Indonesia will be the fifth biggest economy in 2030 and fourth in 2050. As one of the major economy players in the world, it is rationale that many expect Indonesia to play an active role in social responsibility implementation. Indonesia is also a country with many corporations operating in natural resources-related business,

such as mining, plantations, and forestry, a condition that had made the world demand Indonesian companies to do business more responsibly.

An initiative to realize social responsibility for companies had actually been started in Indonesia from past 18 years. The Ministry of SOEs of Indonesia issued a Minister Decree No. Kep-216/M-PBUMN/1999 on 28 September 1999, followed by the enactment of Law No. 19 of Year 2003 concerning SOEs and the issuance of the SOE Ministry Regulation No. Per-05/MBU/2007 concerning SOE's partnership with small enterprises and environmental management programme. All law and regulations stated that every SOE had to allocate 4 percent of its net profit on partnership with small and medium enterprises and environmental management programmes, equally 2 percent each for partnership programme and for environmental management programmes.

In 2017, the government and the parliament of the Republic of Indonesia passed Law No. 40 of Year 2007 regarding Corporation. Article 74 of the Law said that all companies operating in and/or related to natural resources have to follow social and environmental responsibilities. Different from previous laws and regulations that were applicable specifically to SOEs, this law applied to all companies either government, private domestic or foreign-owned companies. There was also an initiative from National Center for Sustainability Reporting, a joint effort of several non-governmental organizations and professional associations started in 2005 to conduct the Indonesia Sustainability Reporting Award (ISRA) to give award to companies that had published sustainability reporting. For listed companies, the Capital Market and Financial Institutions Supervisory Board (now under Indonesian Financial Service Authority) through the issuance of the regulation No. X.K.6 of Year 2006 stated that all annual report of listed companies have to describe activities and cost related to corporate social responsibilities to societies and environment.

The objective of this research is to describe CSR in Indonesia. It described how CSR was perceived by business players in Indonesia, was implemented in Indonesia for the last two years and influenced the company's performance.

## 2. Literature Review

The idea/reason on why a company needs to manage its CSR well is generally laying on the following several theories. First is the stakeholder theory [6] that states that the previous approaches on strategic plan generally overlooked stakeholder issues and simplified environmental change issues a lot, which in fact had led to many companies

experienced many shocks. Therefore, a company needs a new management approach that is called the stakeholder approach.

Second is signalling theory, the idea that one party credible conveys some information about itself to another party. Spence (1973) stated that two parties could get around the problem of asymmetric information by having one party send a signal that would reveal some piece of relevant information to the other party. Consumers might perceive CSR as quality and public might perceive it as good signal from the company.

Third is the resource-based theory. Hart (1995), for example, argued that resources owned by a company can be used to increase competitive advantage. The experience of CSR management will become a source of competitive advantage for a company. Fourth, the legitimacy theory, as been raised by Suchman (1995), argued that a company has to act in accordance with social values and norms to keep the company live. CSR can be a tool to influence public perception on company's operations and give the company social license to operate.

The benefit of conducting CSR has been explained, among others, by the following researchers. Porter and Kramer (2006) proposed three strategic reasons of conducting CSR, that is, sustainability argument, reputation argument and license-to-operate argument. Senge et al. (2008) concluded that the benefits of CSR were (i) significant new potential revenue sources, (ii) creation of competitive edge in the customers eye, (iii) point of differentiation, (iv) opportunity to shape industry direction and to be preferred supplier and (v) brand and image enhancement.

Research on the relationship between CSR and corporate performance has attracted many researchers for years. Generally, the research intended to prove that socially responsible activities by a company led to a positive impact on the company's financial performance. However, there had been inconclusive results of the relationship between the two. For that reason, M. Orlitzky et al. (2003) conducted a meta-analysis to 52 previous studies that involved 30 years of empirical data and 33,878 samples and concluded that CSR had positive impact on corporate performance. Similar study was done by J. D. Margolis and J. P. Walsh (2003) that described that from 109 previous studies, 54 studies showed a positive and significant relationship between CSR and performance, 20 studies with various results, 28 studies said there was no significant relationship and 7 studies revealed negative relationship.

J. D. Maignan et al. (1999) tried to find the impact of CSR not only limited to financial performance, but corporate performance in a wider context. They concluded that CSR had a positive and significant influence on employee commitment, customer loyalty and business performance. Erhemjamts, Li and Venkateswaran (2013) also tried to find

the impact of CSR to broader areas, that is, to financial performance, investment policy and organizational structure and concluded that CSR had positive impact to company's performance measured by Tobin's Q and ROA.

For Indonesian case, J. Oeyono et al. (2011) investigated the level of CSR conducted by the top 50 corporations in Indonesia and its relationship with company's profitability and concluded that CSR level, measured based on GRI guidelines, had a positive relationship with profitability, measured by company's EBITDA and EPS. Ridho (2016) found that there was a positive and significant impact of CSR implementation on financial performance measured by both ROE and ROA in top 200 Indonesian listed companies in 2014. On the other hand, there was no significant influence of CSR on non-financial performance, both customer and employee performance, in top 200 Indonesian listed companies in 2014.

### 3. Methodology

This research used data from top 200 Indonesian listed companies in terms of revenue, both in 2014 and 2015. As independent variable is CSR implementation, while the dependent variable is company's performance. CSR implementation was measured using global standard of CSR implementation, as has been stated by ISO 26000, whereas stakeholders measurement was used to measure company's performance that include both financial and non-financial performance.

CSR implementation was measured operationally by identifying whether the top 200 Indonesian listed company had conducted CSR activities as guided by ISO 26000, which (outside organizational governance) consists of 6 core subjects and 36 issues. The first core subject is human right, which includes eight issues, that is, (1) due diligence, (2) human rights risk situations, (3) avoidance of complicity, (4) resolving grievances, (5) discrimination and vulnerable groups, (6) civil and political rights, (7) economic, social and cultural rights and (8) fundamental principles and rights at work. The second core subject labour practices consists of five issues, that is, (1) employment and employment relationships, (2) conditions of work and social protection, (3) social dialogue, (4) health and safety at work and (5) human development and training in the workplace. The third subject of the environment has four issues, that is, (1) prevention of pollution, (2) sustainable resource use, (3) climate change mitigation and adaptation, and (4) protection of the environment and restoration of natural habitats.

The fourth is fair operating practices, containing 5 issues, that is (1) anti-corruption, (2) responsible political involvement, (3) fair competition, (4) promoting social responsibility in the sphere of influence and (5) respect for property rights. The fifth core subject is consumer issues, consisting of 7 issues, that is, (1) fair marketing, factual and unbiased information and fair contractual practices, (2) protecting consumers' health and safety, (3) sustainable consumption, (4) consumer service, support, and complaint and dispute resolution, (5) consumer data protection and privacy, (6) access to essential services and (7) education and awareness. Finally, community involvement and development with seven issues, that is, (1) community involvement, (2) education and culture, (3) employment creation and skills development, (4) technology development and access, (5) wealth and income creation, (6) health and (7) social investment.

This research used secondary data, collected from annual report, CSR report and CSR information on company's website of top 200 Indonesian listed companies both in year 2014 and 2015.

Content analysis was then used to develop CSR index as measurement of CSR implementation. Content analysis was undertaken on annual report, CSR report and CSR information on website using the coding instrument based on 36 issues of ISO 26000. Score of 0 was given if the company's reports did not disclose specific information as required by a specific issue in ISO 26000. On the other hand, the score should be 1 if the company's reports provided the required information. As there are total of 36 issues in ISO 26000, therefore, if a company can satisfy all CSR implementation according to ISO 26000, its CSR index shall be 36. On the other extreme, if a company do not implement any of ISO 26000 criteria, then its CSR index shall be 0. The typical CSR index will then have range from 0 to 36. In addition, company's characteristics data such as company's size, age, industry group, share trade volume, share beta, debt to equity ratio (DER) and ownership structure was also collected.

As this research tried to measure company's performance using stakeholders' perspective, beside the traditional financial performance, that is, return on equity (ROE) and return on assets (ROA), non-financial performance measurement from customers and employees' perspective were also added. Customers' performance was measured by growth in sales [6], while employees' performance was measured by growth in the number of employees.

Descriptive statistics were then used to provide descriptive information about the CSR implementation for the years 2014 and 2015, including data phenomenon and characteristic such as minimum, maximum, mean and standard deviation. The CSR

implementation by the companies per industry group was also explained. Finally, inferential statistics using ANCOVA was employed to understand the relationship between CSR implementation and company's performance, both financial and non-financial performance for the years 2014 and 2015. In order to draw conclusion more accurately, this research used significance level of 5 percent. A  $p$ -value of less than 0.05 means that  $H_0$  is rejected and  $H_a$  is accepted.

## 4. Results and Conclusions

The CSR index calculation for top 200 listed companies in Indonesia for the years 2014 and 2015 can be summarized as the following table.

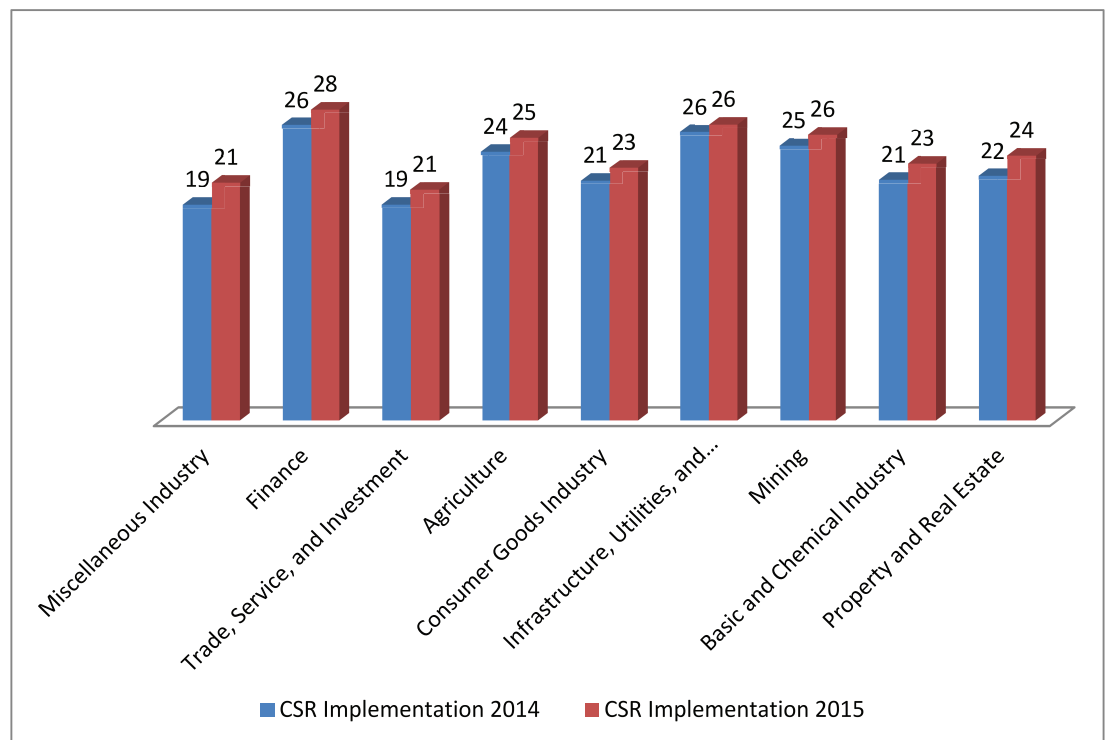
TABLE 1: CSR index calculation for top 200 listed companies in Indonesia for the years 2014 and 2015.

	Minimum	Maximum	Mean	Std. Deviation
CSR Index of 2014	6	35	22.52	6.63
CSR Index of 2015	8	35	23.58	6.29

It can be seen from Table 1 that on average, as indicated by mean value, there was a slight improvement of CSR implementation in top 200 Indonesian listed companies during the period of 2014–2015 from 22.52 to 23.58 or an increase by 2.94 percent. However, compared to global standard of CSR implementation, measured using ISO 26000 that has 36 issues as explained in previous section, even though there was improvement from 62.6 percent in 2014 to 65.5 percent in 2015, in general it could be said that the level of CSR implementation in listed companies in Indonesia was considered still low.

In both years, none of Indonesian listed companies met the global standard of CSR implementation as the maximum score achieved by companies was only 35, or only 97 percent of global standard. On the other hand, as shown by the minimum value in Table 1, there was a listed company in Indonesia having very poor CSR implementation, that is, only 8 (22.2% of global standard) in 2015, a minor improvement from 6 (16.67%) in previous year.

As shown in Figure 1, analysis of level of CSR implementation by industrial sector reveals that finance sector continued to be the leader in CSR implementation, that is, a score of 28 (77.8%) in 2015, an increase from 26 (72.2%) in 2014. This finding is interesting as by law finance is not the sector that is mandatory to implement corporate social and environmental responsibility (CSER) as regulated by Law No. 40



**Figure 1:** CSR implementation by industrial sector in 2014 and 2015.

of Year 2007. Meanwhile, mining sector that was obliged by the law to implement CSER programme as it exploits natural resources was still below the finance sector even though there was a slight improvement of CSR implementation from 25 (69.4%) in 2014 to 26 (72.2%) in 2015. Another resources-based sector, that is, agriculture stayed even below, that is, to 25 (69.4%) in 2015, a minor increase from 24 (66.7%) in 2014. Interestingly, nonresources-based sector, that is, infrastructures, utilities and transportation showed among the top sector in implementing CSR with a score of 26 (72.2%) both in 2014 and 2015. On the other hand, both miscellaneous industry as well as trade, services and investment sector consistently became the poorest performer of CSR implementation in Indonesia with a score of 21 (58.3%) in 2015, an increase of 19 (52.8%) in 2014.

The good news is that there was a significant improvement on the number of top 200 Indonesian listed companies that published an internationally recognized CSR reporting of sustainability reporting (SR). The GRI-based SR publisher rose from 26 companies in 2014 to 38 companies in 2015. An increase of SR publication of almost 50 percent might bring a hope of an increase in CSR implementation, even though the percentage of SR publisher from top Indonesian listed companies was still low, that is, 13 and 19 percent in 2014 and 2015, respectively. As in Indonesia, the publication of SR is still voluntary, the number shows that there are 38 companies of the top 200 listed companies that



have high commitment in implementing CSR as well as reporting their CSR activities to stakeholders transparently and accountably.

Consistent with the finding that finance sector had the highest score in CSR implementation, companies from financial sector also contributed the most in publishing SR in 2015. There were 14 companies in financial sector that published SR, followed by five companies from infrastructure, utilities and transportation and from mining sector. On the other hand, only one company from miscellaneous sector published SR.

Using two years', 2014 and 2015, data panel of CSR implementation and company characteristics as independent variables and company performance, both financial and non-financial performances as dependent variables, analysed using ANCOVA shows the following relationship.

TABLE 2

	ROE	ROA	Customer	Employee
CSR Implementation 2014	Significant - positive	Significant - positive	Not significant	Not significant
CSR Implementation 2015	Significant - positive	Significant - positive	Not significant	Not significant

It can be seen from Table 2 that CSR implementation associated significantly and positively with financial performance, both ROE and ROA. This result is consistent with the previous conclusion by Ridho (2016) that CSR implementation shall have positive impact to the financial performance of Indonesian listed companies. On the other hand, there is no significant influence of CSR implementation both on customer and employee view. This indicates that the previous research by Ridho (2016) remains unchanged said that both customers and employees did not consider CSR practiced by a company as a reason to buy goods or services from a company or to work at a company.

## 5. Limitations/Future Studies

This research included only top 200 Indonesian listed companies in 2014 and 2015. Further research need to study all top Indonesian companies, including Indonesian SOEs that had not been going public. The longer time of study, for example, five years or more time series study might improve the conclusion of this research.

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