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The Influence of Good Corporate Governance and Corporate Social Responsibility on Firm Value: Evidence from Indonesia

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Abstract

The company goal is to maximize the shareholders' prosperity, not just to maximize profit. The fact is that the company not only has economic responsibility but also social responsibility to the community and its environment. The purpose of this study was to analyze the effect of good corporate governance (GCG) and corporate social responsibility (CSR) on the firm value. The research sample of 15 companies was taken using purposive sampling from companies listed in the LQ-45 on the Indonesia Stock Exchange for the period of 2014-2017. This study uses panel data regression analysis with Random Effect model method. GCG is a representation of managerial ownership, institutional ownership, independent commissioner, and audit committee. The results of this study indicate that there is a significant influence between GCG and CSR on firm value simultaneously. Partially, independent Commissioners and CSR each have an influence on the firm value, but there is an anomaly.

Keywords: GCG; CSR; Firm value; LQ-45.

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1. Introduction

The company is established with a clear goal, which is to maximize the value of the company. The company's goal is to maximize the shareholders' prosperity, not just to maximize profit. Short-term oriented companies only prioritize maximum profits, without regard to social responsibility and ignoring risks. The fact that cannot be ignored is CSR which is currently no longer an option, but has become a fasionable management concept (Türker, 2015).

To realize the company's goals requires a new awareness, that the company not only has economic responsibility (especially to shareholders) but also has social responsibility to the community and its environment. With an awareness of the social environment of this community, the concept of corporate social responsibility (CSR) emerged. Exploitively exploiting natural resources so far threatens the sustainability of raw material resources and energy (Iwuji *et al.*, 2016), and triggers social disharmony with the environment community and increasingly severe labor conflicts. Therefore, it can be said that CSR plays an important role in sustainable development (Behringer and Szegedi, 2016).

Research on corporate social responsibility towards corporate value is mostly done in Indonesia and in other countries. A survey released by the National Consumers League and Fleishman Hillard International Comunication shows that two-thirds of consumers will prefer to buy company products that they are socially responsible for, especially companies that treat their employees well (Iwu-Egwuonwu, 2010). So that it can be understood that corporate social responsibility plays an important role in increasing company value (Jo and Harjoto, 2011; Kang *et al.*, 2015) and become a determining factor for consumer choice (Modak *et al.*, 2014). However, CSR activities are not able to maximize the value of the company, instead causing a significant reduction in stock prices when imposing CSR through regulation (Manchiraju and Rajgopal, 2015)

CSR activities are carried out only possible if the company implements good corporate governance / GCG (Cahyandito and Pau, 2017). With good governance, trust will be obtained from investors, customers and the wider community (Sarah, 2017). Long-term goals are expected to increase the value of the company.

In the process of maximizing the value of the company there will be differences in interests between shareholders and managers. These differences have led rise a theory known as the agency conflict (Panda and Leepsa, 2017). This conflict often raises c osts which are called agency costs, such as changes in share ownership structure between management and stockholders.

Shareholders have an interest in supervising management performance as a function of good corporate governance (GCG), while, there is also independent supervision which is the duty of the independent board of directors to prevent agency problems or to align between managers and shareholders.

The supervisory process for management performance can also be carried out by a board of directors who, in addition to being responsible for monitoring, is also responsible for the management of the company's resources and operations. Supervision can also be carried out by the audit committee to ensure transparency and accountability of

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the financial management report. Those parties which are able to reduce management actions that can be detrimental as a form of GCG implementation.

Based on this background, the purpose of this study was to analyze the influence of good corporate governance and corporate social responsibility on the firm value that included in the LQ-45 on the Indonesia Stock Exchange in the period of 2014-2017.

2. Literature Review

2.1. Firm Value

Corporate actions are often carried out such as going public, mergers, acquisition, even when the closure of a business requires an assessment of the company's assets. Firm value measurement generally uses the company's stock price, as in research (Jallo *et al.*, 2017; Mulyono *et al.*, 2018; Pandelaki and Farida, 2017) which reflects the higher share price means the higher the value of the company. However, there is also a measure of corporate value is market price to book value (PBV) conducted by Dagilienė (2013), Hadiwijaya *et al.* (2016), Hafez (2016), as well as the industry-adjusted Tobin's Q method (Almaqoushi and Powell, 2017; Gherghina and Vintila, 2016), and approximate Tobin's Q (Chan and Li, 2008; Fahlenbrach and Stulz, 2009; Kurniasari *et al.*, 2017; Ruiz-Mallorquí and Santana-Martín, 2011; Vania and Supatmi, 2014).

Research conducted byHaryono and Iskandar (2015), Ruiz-Mallorquí and Santana-Martín (2011) used Tobin's Q and PBV to measure company value. Tobin's Q is the equity market value plus long-term debt then divided by total assets (Hatem, 2015). Market to book value ratio that reflects the company's value in the Hafez (2016) is the ratio between the current stock market and book value.

2.2. Agency Theory

Agency theory is based on contractual relations amongs members within existing companies, principals and agents as the main actors (Daly, 2015). Shareholders entrust managers the authority to make decisions. Managers are as the decision maker sometimes have interests for themselves and ignore the interests of shareholders. This deviates from company goals. Agency theory, can explain how the parties involved in the company will behave, because basically between agents and principals have different interests which can lead to conflict.

The existence of agency problems raises agency costs (Jensen and Meckling, 1976). These costs include monitoring costs, bounding costs, and the cost of losses due to a decrease in the level of utility (the residual loss). This agency theory is the basis of the corporate governance concept. Corporate governance aims to reduce agency costs due to information asymmetric (Juniarti, 2013). How sure investors are to invest, it depends on how the corporate governance is implemented to gain profits. Hence investors have an interest in controlling managers (Shleifer and Vishny, 1997).

2.3. Good Corporate Governance (GCG)

Corporate governance is a set of methods, rules, structures and processes of managed company activities (Khan, 2011) to achieve a balance between the interests of the organization and stakeholders (Jaimes-Valdez *et al.*, 2017). Khan (2011), in his review said that for long-term corporate governance will increase value for shareholders and companies. There is no single definition of corporate governance.

Corporate governance consists of institutional ownership variables, independent directors, and audit committee (Willim, 2015). Research (Juniarti, 2013) GCG variable is a proxy of ownership structure, board of directors and audit committee. Unlike GCG in banks, Bank of Indonesia sets the main principles in GCG that are related to transparency, accountability, responsibility, independence and fairness (Hadiwijaya *et al.*, 2016). Research conducted by Ilyas and Rafiq (2012), used a measure of governance in the banking sector consisting of discipline, social awareness, accountability, fairness and responsibility. The global financial crisis is one example of failure in corporate governance (Kumar, 2013). The research conducted by Vania and Supatmi (2014) presented that corporate governance as a board diversity measured by five variables, namely women in board, competence in the economy and business, age, external director and citizenship. In Indonesia, the owner is generally as management as well. Likewise the director is also a commissioner, so the monitoring and control function is not independent (Hidayat and Utama, 2015)

Managerial ownership is also widely used as a proxy in corporate governance variable as in research by Chen (2006), as well as institutional ownership (Charfeddine and Elmarzougui, 2010; Sahut and Gharbi, 2010; Thanatawee, 2014). The measurement of managerial ownership is the number of shares owned by the company manager compared to the number of shares outstanding. Similarly, institutional ownership as investors is the number of shares held by the institution against the total number of shares outstanding. Currently institutional investors have an important role, which has changed dramatically from passive investors to being active in monitoring (Charfeddine and Elmarzougui, 2010). Institutional shareholders are usually in the form of entities such as banking, insurance, retire funds and mutual funds. Institutional investors have the capability to analyze financial statements directly compared to individual investors.

Another proxy in corporate governance is the existence of an independent commissioner. It is the number of independent commissioners to the total board of commissioners owned by the company. Research (Indriawati and Sari, 2017) examined the effect of independent commissioners on voluntary disclosure. The audit committee also has an important role in creating GCG because it is able to monitor the process of financial statements (Almaqoushi and

Powell, 2017). Research related to the audit committee with the value of the company has also been carried out by Alqatamin (2018), Chan and Li (2008).

2.4. Corporate Social Responsibility (CSR)

CSR in Indonesia is a mandate that must be implemented, but the reality is not yet fully implemented by the company. CSR awareness is only owned by companies that are committed to building a better quality of life together for all stakeholders and the environment. According to Behringer and Szegedi (2016) companies must offer the creation of a balance amongs economic interests, environmental needs and social expectations by conducting CSR as a business model to integrate the spirit of sustainable development.

Research (Singh *et al.*, 2011) used 6 dimensions of CSR based on the international CSR index such as the Dow Jones corporate sustainability index and the FTSE4 Good index in evaluating the impact of CSR on stock market value. These dimensions are CSR practices that focus on community investment, workplace quality, CSR and reporting strategies, stakeholder agreements, environmental performance and supply chains. Many studies have been conducted to examine how the influence of CSR on corporate value. The results vary between studies. Some proved that the relationship is positive, partly negative, and others proved neutral (Hafez, 2016). Hafez (2016) research proves that there is no significant influence between CSR on company value. However, there is a significant influence between CSR on the company's financial performance. The CSR index is used based on the principles of CSR in the OECD which consists of 9 questionnaires with scores ranging from 0 to 10 for each question.

The effect of social disclosure of company activities on company value (Dagilienė, 2013) means additional costs. Companies that report low social responsibility, actually have high corporate value as measured by market to book value.

3. Research Method

This research was conducted using a descriptive quantitative approach, where the population is companies listed in the LQ-45 index on the Indonesia Stock Exchange. The stocks included in this LQ45 index are those that have the largest market capitalization and a high level of trading liquidity. Purposive sampling is used to determine the sample and selected as many as 15 companies. Observation period from 2014-2017.

The analysis technique used is the panel data regression model, with the dependent variable (Y) is the market price to book value ratio (PBV) as the company's value (Hafez, 2016). PBV is the ratio of market price per share to book value per share. While the independent variable used in this study is GCG which is represented by four variables, namely managerial ownership / MO (X1), institutional ownership / IO (X2), independent commissioner / IC (X3), and Audit committee / AC (X4). Another variable to see its effect on the value of the company is CSR as X5. The panel regression model is as follows;

$$Y_{it} = \alpha + \beta_1 X_{1it} + \beta_2 X_{2it} + \beta_3 X_{3it} + \beta_4 X_{4it} + \beta_5 X_{5it} + e_{it} \qquad (1)$$

Where:

- Y_{it} is the dependent variable (PBV)
- X_{it} represents independend variables
- i is entity (company)
- t is time (year)
- α is constant/intercept
- β is the coefficient for the independent variable
- e_{it} is the error term

Either managerial ownership (MO) or institutional ownership (IO) is a ratio of the number of each ownership to the total number of shares outstanding. Independent commissioners (IC) are the ratio between the numbers of IC to the number of commissioners. The Audit Committee (AC) is the number of members of the company's audit committee.

For the measurement of CSR performance in this study, the content analysis method is used by looking at whether there is a report / information on social activities carried out by the company. It is given a score of 1 if there are reports, and 0 if there are no reports. There are 79 items of CSR disclosure guidelines issued by the Global Reporting Initiative (Gunawan, 2009) which are divided into 6 indicators, namely economic indicators, environmental and social performance (employment, human rights, society and product responsibility).

In panel data analysis, classical assumptions were tested, namely multicollinearity test and heteroscedasticity test. To estimate the data panel model is used ordinary least square (common effect), fixed effec model (FEM) and random effect model (REM). For selecting the best estimation model (Akbar *et al.*, 2011) conducted a chow test, Haussman test, and Breusch-Pagan Lagrange Multiplier test.

4. Data Analysis and Discussion

4.1. Panel Data Analysis

To estimate the model parameters using panel data, the first Chow Test is performed. This test is used to determine whether panel data regression techniques with fixed effect methods are better than the common effect method. The result is in table 1, showing cross-section chi-square is significant with P value of 0.000 which means the fixed effect method is selected.

Table-1. Chow Test Result

Effects Test	Statistic	Prob
Cross-section F	113.109244	0.0000
Cross-section Chi-Square	222.208695	0.0000

The second step is to do the Hausman Test to choose whether the fixed effect model is more suitable than the random effect model. If it receives H_0, random effect is selected. If it rejects H_0 or accepts H_a, the fixed effect model is chosen. From the results of the Hausman Test is in table 2, shows that H_0 is accepted or p value is 0.682 > 0.05. It means the method choosen is random effect.

Table-2. Haussman Test Result

Test Summary	Chi-sq Statistic	Prob
Cross-section random	3.115780	0.6821

Third, we continue with the Langrangian Multiplier (LM) test to determine whether to choose random effects or common effects. If receiving H_0 means common effect, on the contrary if it accepts H_a or reject H_0 it means random effect. LM Test results in table 3 shows that the P value in the Pagan Breunch method is 0,000 <0.05, so the best estimation method is random effects or receiving H_a.

Table-3. Lagrange Multiplier Test Result

	Test Hypothesis		
	Cross-section	Time	Both
Breusch-Pagan	69.28794	1.777186	71.06512
	(0.0000)	(0.1825)	(0.0000)

Without using the three tests above, some econometrics experts usually choose the best method as follows; if the panel data has a number of times (t) smaller than the number of individuals (i), it is recommended to use the random effect method. This study has a time (t) of 4 years, smaller than the number of individuals (companies) of 15, which means that this study use the random effect method.

4.2. Multiple Regression Analysis

In multiple regression analysis using panel data, not all classical assumption tests were carried out. If the independent variable is more than one, multicollinearity tests need to be carried out, to ensure that there is no relationship between independent variables. The multicollinearity test results are in table 4.

Table-4. Correlation Matrix Result

	MO	IO	IC	AC	CSR
MO	1.000	0.019	-0.066	-0.192	-0.100
IO	0.019	1.000	0.030	-0.170	-0.105
IC	-0.066	0.030	1.000	0.073	0.137
AC	-0.192	-0.170	0.073	1.000	0.073
CSR	-0.100	-0.105	0.137	0.073	1.000

From table 4, it can be seen that the multicollinearity test results have no correlation between independent variables where the matrix correlation value does not exceed 0.8. Another assumption that needs to be done in the regression analysis with panel data is the heteroscedasticity test, there is a table 5. There are no symptoms of heteroscedasticity in this study, as seen from the P-value of Obs*R-squared is greater than 0.05.

Table-5. Heteroscedasticity Test Result

Heteroskedasticity Test: White			
F-statistic	1.560848	Prob. F(5,54)	0.1868
Obs*R-squared	7.576411	Prob. Chi-Square(5)	0.1812
Scaled explained SS	42.51170	Prob. Chi-Square(5)	0.0000

The results of multiple regressions with random effect models are shown in table 6. The multiple determination coefficient value shown by adjusted R-squared is 0.597953 which means that the contribution of independent variables in this model is able to explain the dependent variable of 59.79 percent. Meanwhile, the remaining 40.21 percent is explained by other variables not included in this study.

Table-6. The result of F test, adjusted R-squared and T test

Variable	Regression coefficients (B)	t-test	Signification
Constants	8.093181	0.869117	0.3886
MO	-6.528671	-0.769987	0.4447
IO	-0.090519	-0.188475	0.8512
IC	-29.65509	-8.573265	0.0000**
AC	-0.377110	-0.632806	0.5295
CSR	35.23768	1.786496	0.0796*
Adjusted R^2	=		0.597953
F-statistic	=		18.54980
Prob	=		0.000000

**significant at level of 5%
*significant at level of 10%

The F-statistic value in this model is 18,549 with P-value 0,000 < 0.05 which can be concluded that independent variables simultaneously affect significantly independent variables. The equation of the multiple regression models that is formed is as follows;

$$Y = 8{,}093 - 6{,}529\ X1 – 0{,}090\ X2 – 29{,}655\ X3 – 0{,}377\ X4 + 35{,}237\ X5$$

Partially, the independent variable that influences is X3 or independent commissionaries (IC) with a P-value of 0.000 <0.05 with a significant level of $\alpha = 5\%$. This means that the IC variable has a partial effect on the firm value. IC regression coefficient value is - 29.65509, which means that if other independent variables are constant, there is a negative influence on the firm value where each increase in IC by 1 point will reduce the firm value as many as 29.65. The influence of IC is significantly on the firm value, in line with research (Jensen and Meckling, 1976) but with the opposite direction. Jensen and Meckling (1976), explained that the existence of IC is needed to control and supervise management performance so as to create good corporate governance. Good corporate governance has a positive effect on the firm value. Conversely, the influence of IC in this study has a negative effect on firm value. In Indonesia, it becomes an anomaly case because the existence of IC in companies are alleged only as entrusted positions related to interests. So that the existence of IC in a company is burdensome instead, because the function of monitoring and controlling of management is weak. The more independent commisioners, the lower firm value because they do not encourage good corporate governance. Research (Indriawati and Sari, 2017) proves that the existence of IC in Indonesia does not influence on the information disclosure.

Another independent variable that has a partial effect on the firm value is CSR with a significance level of 10%. The P-value for CSR is 0.07 < 0.1. The value of CSR regression coefficient is 35.23768, which means that if any an increase of 1 point of CSR there will increase the firm value as many as 35.23768. The results of studies on CSR are varied. CSR and firm value have a positive relationship, if CSR activities are aligned with the company's reputation (Servaes and Tamayo, 2013). Empirical research conducted by Hafez (2016) reveals that CSR does not negatively affect the firm value, but provides a positive influence on financial performance. On the contrary (Dagilienė, 2013) found that companies with the highest PVB value were far from socially accountable.

Other independent variables such as managerial ownership, Independent ownership, and Auditor committee each have no partial effect on the value of the company because P-value is greater than $\alpha = 5\%$ or $\alpha = 10\%$. Managerial ownership (MO) has a P-value of 0.444 > 0,000, which means that there is no influence between MO and firm value. This research is in line with (Lee and Hwang, 2012) who stated that there is no positive or negative influence between managerial ownership and firm value.

Institutional ownership (IO) produces a p-value of 0.8512 which means there is no influence of IO on the firm value. Conversely, research (Charfeddine and Elmarzougui, 2010) found that there was a negative influence on the company's performance as a proxy of Tobin's Q. IO is assumed not to play a role in monitoring and controlling efficient governance activities in the company so that it does not contribute to the company's performance. In this study, although the IO does not have a significant effect, it has the same negative coefficient trend as the research by Charfeddine and Elmarzougui (2010).

The audit committee (AC) has a p-value of 0.5295 with a coefficient value of -0.387 which means that the negative influence of AC is not significant to the firm value. If the audit committee rarely holds regular meetings with the parties such as internal and external auditors, board of directors and board of commissioners, then the existence of the audit committee does not have a positive influence on the firm value.

5. Conclusion

In this study, the analysis of GCG and CSR on firm value that is proxied by PBV values uses panel data regression with random effect method. Simultaneously, the influence of GCG and CSR on firm value is significant. Partially, independent commissioners have a significant effect on the firm value, despite anomaly. The results of research on CSR are varied so far. In this study proves that CSR by companies listed on the LQ-45 Indonesia Stock Exchange has a significant effect on increasing the firm value.

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