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Joint Impact of Financial Performance and Corporate Social Responsibility on Firm Value: Does Legitimacy Matter?

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Abstract: The purpose of this study is to examine the effect of the interaction of financial performance and corporate social responsibility disclosure on firm value. The research model was constructed from the theory of legitimacy and used a purposive sampling method. The companies in the sample were non-financial companies listed on the Indonesian Stock Exchange for the period 2017-2019 that disclose annual and sustainable development reports respectively. Analysis of data by moderate regression analysis. The results of this study indicated that neither financial performance nor corporate social responsibility had a significant effect on firm value. On the other hand, the interaction between financial performance and disclosure of corporate social responsibility had a significant positive effect on firm value. Furthermore, the implications of the research both theoretically and practically have been discussed.

Keywords: corporate social responsibility, financial performance, firm value.

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INTRODUCTION

Facing the rapidly changing realities and huge global risks as well as maintaining a credible organizational image, all business entities strive to always maintain a balance between financial benefits for the organization, community welfare, and environmental sustainability (Ting & Yin, 2018; Lu et al., 2019; Barauskaite & Streimikiene, 2021). Many companies are concerned with gaining legitimacy by integrating the expectations of their stakeholders into a comprehensive corporate strategy. The above phenomenon has also been confirmed by companies in Indonesia, since the enactment of the Financial Services Authority Regulation No. 51/POJK.03/2017 Regarding the Implementation of Sustainable Finance for Financial Service Institutions, Issuers, and Public Companies, it is noted that issuers are increasingly aligning business strategies with corporate social responsibility programs (Budi, 2021).

Research themes related to the phenomena and realities above often relate to financial performance and corporate social responsibility. However, despite numerous studies on the relationship between financial performance, corporate social responsibility, and firm value, the findings have been inconsistent and still inconclusive (Ting & Yin, 2018; Deswanto & Siregar, 2018; Barauskaite & Streimikiene, 2021; Grassmann, 2021). Likewise, research results in the context of the Indonesian stock market confirm various results, including for example Erdianty & Bintoro (2015) which state that financial performance is not a direct predictor of firm value. The same thing is expressed by Deswanto & Siregar (2018) who state that financial performance does not affect the value of the company either directly or through the disclosure of corporate environmental responsibility. However, this contrasts with the findings of Jihadi et al (2021); Lukman & Tanuwijaya (2021) which confirm financial performance as a firm predictor of value.

Literature review explains the heterogeneity of the relationship between financial performance, corporate social responsibility, and firm value, among others, have been presented by several researchers, both implicitly and explicitly, including Malik (2015); Grewatsch & Kleindienst (2017); Brooks & Oikonomou (2018) which provides a review of research that explores moderators in the pattern of relationships in the above study. The moderator's role in question is in corporate social responsibility. In the context of the above thought, Ting & Yin (2018); Nardella et al. (2022) reveal that the increase in financial performance is revealed to be more real when the company contributes limited resources to activities that are closely related to the interests of stakeholders.

Concerning firm value, the financial performance achieved by a business entity is not sufficient to predict or affect firm value. This is in line with the statement of Ting & Yin (2018) which explains that the meaning of achieving financial performance will be strengthened by the extent to which this performance is reflected in the form of corporate social responsibility that has an impact on stakeholders. The perspective above indicates that stakeholders want and even demand an entity or company to carry out its business which is oriented towards prosocial actions and protecting the environment. Disclosure or social and environmental investment by a business entity then has an impact on the public legitimacy of a company (Nielsen & Thomsen, 2018). Corporate legitimacy will be formed when an entity's actions are highly desirable, appropriate, or appropriate in some socially constructed system of norms, values, beliefs, and definitions Deephouse et al. (2017). The important point is that to gain legitimacy, an entity must be able to align its behavior with the expectations of its stakeholders. These actions will have an impact on ensuring the viability of a company (Camilleri, 2015).

Studies related to CSR concerning firm value have been widely studied in the fields of accounting, finance, and management. The main benefit related to CSR is that it has a positive effect on firm value, both in the short and long term. Another benefit is as an important strategic tool to maximize shareholder value and company value by protecting the interests of other stakeholders (Malik, 2015).

The importance of legitimacy in the form of CSR strengthens the relationship between financial performance achievement and firm value. Brooks & Oikonomou (2018) state that companies that gain legitimacy from the community can help reduce costs associated with regulations and remove the negative stigma for society. On the other hand, companies that do not get legitimacy will face obstacles in implementing their strategies, especially related to potential market control as a result of the negative stigma they face, especially related to environmental reputation. Thus, the importance of legitimacy in the form of CSR strengthens the relationship between the achievement of financial performance and firm value.

In line with this, Hahn & Kühnen (2013) reveal the potential benefits of a business entity when providing information related to corporate responsibility including increasing the reputation, transparency, and value of the product and even the brand image of a product. Even cynically, Nardella et al. (2022) state that the disclosure of corporate social responsibility is carried out to influence the perceptions and decisions of external stakeholders, especially regarding the potential profits obtained by the company in the future. This will sometimes reduce efforts to achieve the main goal, namely how and what the company should do to reduce social degradation and improve a better social environment (Aerts & Cormier, 2009).

Therefore, this research model was designed to examine the joint effect of how the achievement of financial performance is interacted with CSR in predicting its effect on firm value. This research model is built on the rationality of legitimacy theory (Guthrie & Parker, 1989; Dawkins, 2005), namely that the achievement of the company's financial performance needs public support or recognition through CSR disclosure which in turn influences firm value.

METHODS

The research data is in the form of annual reports from non-financial companies listed on the Indonesia Stock Exchange (IDX) for the 2017-2019 period. The selection of non-financial sector companies as the research sample is the presentation of the number of companies listed that are more dominant than non-financial sector companies than financial sector companies (Table 1). The independent variable of this research is financial performance, which is proxied by Return on Assets (ROA). ROA is the profitability ratio that is most highlighted because it can show the company's success in generating profits by using assets. Assets are company assets obtained from own capital or foreign capital, which are used for the company's sustainability (Lukman & Tanuwijaya, 2021). The existence of ROA helps to see the company's ability to manage the total assets of the company. The research conducted (Erdianty & Bintoro, 2015) uses a profitability ratio, namely ROA. ROA is formulated as follows (Deswanto & Siregar, 2018; Mukhtaruddin et al, 2019; Lukman & Tanuwijaya, 2021). ROA = Net Profit After Tax/Total Assets × 100%. Disclosure of Corporate Social Responsibility as a moderating variable is the disclosure of information related to corporate responsibility in the company's annual report.

CSR measurement is carried out using the CSR index. The calculation of the CSR index is carried out as follows: Make a list (checklist) of CSR disclosures. The list of items used in this research is a modified list of items from the GRI (Global Reporting Initiative); Determine the CSR index for each sample company. The formula for calculating the checklist index of corporate social responsibility disclosure is (Prena & Muliyawan, 2020; Lukman & Tanuwijaya, 2021): CSRIj = Number of items for the company/91 items CSR version of Global Reporting Initiative (GRI).

The value of the company is the market value of the company's stock that reflects the investor's assessment of each equity owned by the company. Several ways can be used to measure the market performance of a company, and one indicator that can provide the best information is Tobin's Q Ratio (Gaio & Raposo, 2011). Tobin's Q < 1 analysis indicates that the book value of the company's assets is greater than the market value of the company. Tobin's Q is formulated as follows Gaio & Raposo, 2011; Crisóstomo et al., 2011; Servaes & Tamayo, 2013; Ronald et al., 2019; Daromes et al., 2020): Tobin's Q = EMV+Debt/Total Assets, in which EMV = number of ordinary shares of the company outstanding multiplied by the closing price of the shares; Debt = Total Debt; Total Assets = Total Assets. This study uses one independent variable, one dependent variable, and one moderating variable. Therefore, this research uses moderating regression analysis. Moderated Regression Analysis (MRA) or interaction test is a special application of linear multiple regression in which the regression equation contains an interaction element (Otley, 2016)

Table 1 Summary of the Sample Observed

Sampling criteria	Number of companies
Number of non-financial companies listed on the IDX during 2017-2019	621
Number of companies that did not issue Corporate Social Responsibility during 2017-2019	(579)
Total research samples	42
Total samples processed for 3 years	126
The number of outlier data removed from the population	(87)
Total samples processed in the study	39

RESULTS AND DISCUSSION

The results of the descriptive statistics in Table 2 show that the average financial return is 0.0644 and the standard deviation is 0.02972. This shows that the average value can be used as a representation of the entire data because the average value is greater than the standard deviation. Likewise, disclosure of corporate social responsibility has an average value of 0.3287 with a standard deviation of 0.12864. This shows that the average value can be used as a representation of the entire data because the average value is greater than the standard deviation. Moreover, the company's value has an average of 1.2085 with a standard deviation of 0.34401. This shows that the mean value can be used as a representation of the entire data, which is reflected in the mean value which is greater than the standard deviation.

Table 2 Descriptive Summary Statistics

Variables	N	Minimum	Maximum	Mean	Deviation
Financial Performance	39	0.03	0.19	0.0644	0.02972
Corporate Social Responsibility	39	0.14	0.69	0.3287	0.12864
Firm Value	39	0.50	2.06	1.2085	0.34401

The next test is related to the model fit test (Table 3) and Table 4, the analysis of the coefficient of determination (R2). Confirmation of the model fit test (Fit Model) has a significance value of 0.012, which is smaller than 0.05. This shows that the mode l in this equation has been well constructed (mode l fit), so it can be concluded that the theoretical framework is in line with the built mode l and that the regression mode l can be used to predict the dependent variable. Similarly, the analysis of the coefficient of determination shows that the value of Adjusted R2 is obtained at 0.249, which means that the independent variable in this study can explain the dependent variable of 24.9%. The remaining 75.1% is explained by other variables outside the model I used in this study.

Table 3 Model Testing

Model Structure	F	Sig.
1	3.518	0.012

Table 4 Coefficient of determination (R^2)

Structure Model	Adjusted R Square
1	0.249

Furthermore, Table 5 is the result of hypothesis testing and Moderated Regression Analysis, which is to test either directly or by testing moderation.

Table 5 Hypothesis testing results

Independent Variables	Dependent Variable	Standardized Beta	Significance	Confirmation
Financial Performance		0.251	0.443	Not significant
CSR	Firm Value	0.369	0.377	Not significant
Financial Performance*CSR		0.880	0.037	Significant

Financial performance is estimated at 0.251 with a firm value with a probability value of 0.443 > 0.05. Confirmation of this statistical test indicates that financial performance does not affect firm value. Thus, the hypothesis that financial performance has a positive effect on firm value is rejected. Likewise, disclosure of corporate social responsibility shows an estimated value of 0.369 with a probability level of 0.377 on firm value. As a result, the hypothesis that was constructed is also rejected. Confirmation of the test results above can be concluded that neither financial performance nor disclosure of corporate social responsibility is not a direct predictor of firm value.

The research findings are in line with the findings of Erdianty & Bintoro (2015); Rahayu & Damayanthi (2018) revealed that financial performance is not a direct predictor of firm value. The findings of this study are different from the findings of Lu & Abeysekera (2014); Deswanto & Siregar (2018); Jihadi et al. (2021); Lukman & Tanuwijaya (2021) namely that financial performance influences firm value. In line with Iatridis, 2013; Mukhtaruddin et al. (2019) explained that CSR disclosure has a positive effect on firm value.

Different results were associated with testing the interaction of financial performance, with disclosure of corporate social responsibility towards firm value. The effect of corporate social responsibility on financial performance on firm value is 0.880 with a probability value of 0.037 <0.05. This result shows that corporate social responsibility has a positive and significant influence on financial performance and on company value. Thus, the hypothesis which states that corporate social responsibility moderates the effect of financial performance on firm value is accepted.

The findings of this research confirm the arguments of Ting & Yin (2018) which states that good financial performance coupled with corporate social responsibility activities will tell many things related to the reality of the company that gives investors a good picture. In the eyes of investors, companies that perform well will be legitimized by both primary and secondary stakeholders in disclosing corporate responsibility activities. Corporate social responsibility is implemented through economic, social, and environmental performance. The better the performance is carried out; it will affect the increase in the value of the company. Investors will be interested in investing their capital in environmentally friendly companies. CSR disclosure is a consideration for investors. This finding means that the drive for better financial performance supports companies to behave responsibly in the essence of a business. This condition gives a good message to investors at large.

Corporate social responsibility is implemented through economic, social, and environmental performance. The policies of non-financial companies that are pro-social and environmental can be seen clearly in the form of processing, products produced, and distribution processes. The better the performance is carried out; it will affect the increase in the value of the company. Investors will be interested in investing their capital in environmentally friendly companies. Corporate social responsibility disclosure is a consideration for investors.

Companies that operate must provide benefits and benefits to stakeholders. The disclosure of corporate social responsibility will support the survival of the company. Investors also provide support to the company in improving the company's performance. Companies in carrying out their operational activities must provide stakeholders with benefits. Good Corporate Social Responsibility will support the survival of the company. Investor support also makes a maximum contribution to improving the company's performance. In addition, the existence of the Company Law in Indonesia and other supporting regulations applied by the government to companies to require disclosure of social and environmental responsibilities will have an impact on increasing the company's reputation. If the company does not implement, sanctions will be applied according to the provisions of the legislation. Disclosure of corporate social responsibility activities by paying attention to stakeholders will gain community legitimacy and will have a good impact on company value.

The arguments above confirm the statements of several previous researchers, for example, Nielsen & Thomsen (2018) who state that a business entity needs to disclose and invest its business in social and environmental matters. These actions will have a good impact on the emergence of a company's public legitimacy. Deephouse et al. (2017) emphasize that this legitimacy will emerge and be formed when the actions of an entity are really expected, in accordance with the socially constructed system of norms, values, and beliefs in which the entity operates.

The reason a company must present social and environmental information in its annual report is of course carried out because of legal responsibility, but also to gain community legitimacy in its social contract. Schaltegger & Burritt (2017) emphasize the disclosure of corporate social responsibility as an embodiment and shows the company's respect for the community and the environment in which they operate.

The main point is that improving the company's financial performance requires the support of community legitimacy, which is to reconcile its behavior with its broad interests. This will have an impact on the continuity of a company's operation. The legitimacy gained, in the end, will bring various benefits, including increased transparency, increased reputation, and value of the company concerned (Deegan, 2019).

CONCLUSION

Based on the descriptions that have been presented previously, this study provides at least two main findings. The first finding confirms that financial performance and corporate social responsibility have no direct effect on firm value. In other words, neither financial performance nor corporate responsibility is a direct predictor of firm value. The second finding confirms that the interaction or joint impact of financial performance and disclosure of corporate social responsibility influences firm value. Confirmation of these findings indicates that the financial performance achieved by an entity needs to be demonstrated in the disclosures and related social responsibility activities. The financial performance and social responsibility activities carried out by the company have a positive impact on the role of stakeholders, which is confirmed through positive reactions from investors. The results of this study confirm the theory of legitimacy. Baumann-Pauly et al. (2014) revealed that legitimacy provides vital support for the survival of the company as a prerequisite for resource flow and stakeholder support. Thus, legitimacy is seen as a process that shows that the company's actions are in line with the values of the community in which a company operates. In short, legitimacy theory focuses on how companies try to adhere to the values or perceptions of the community in which the company conducts its business activities (Clarkson et al., 2008; Nishitani et al., 2021). This research is expected to increase company awareness of the importance of companies being able to disclose corporate social responsibility. Disclosure of corporate social responsibility is very influential in creating investor confidence in the company. Thus, the company is increasingly controlled and the presence of a party that oversees helps improve the quality of the company's value. For regulators and the government, this study provides additional information on the disclosure of corporate social responsibility in Indonesia and builds awareness of the importance of disclosure of corporate social responsibility. This is important and builds good hopes that more and more public companies will carry out corporate social responsibility disclosure activities on the capital market in Indonesia. This study still has limitations that can be used as recommendations for further research. The scope of the research is limited to non-financial companies in the Indonesian capital market, this may not be able to describe conditions in Indonesia as a whole. Another limitation is that the sample that meets the requirements in this study is relatively small. Likewise, the financial performance proxies tested only limit the ratio of return on assets.

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