

Green economy: Islamic social reporting for companies

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Abstract

Purpose - The purpose of this study is to examine the impact of Islamic social reporting on firm value.

Method - This research uses quantitative methods. The sample in this study is 13 sharia companies registered in the Jakarta Islamic Index for 2016-2020. Data analysis using multiple linear regression. Islamic social reporting as an independent variable, while the firm value is measured using Tobin's Q as the dependent variable, and firm size as a control variable.

Result - The empirical results in this study found that Islamic social reporting has a positive and significant effect on firm value.

Implication - Sharia companies listed in the Jakarta Islamic Index are expected to focus on Islamic principles in carrying out activities including in social aspects to increase company value as part of the company's strategy.

Originality - This study combines the ISR disclosure index from several previous researchers to measure ISR disclosure in Islamic companies.

Keywords: Islamic social reporting; firm value; firm size; performance



Introduction

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In order to ensure future global economic growth and prosperity, the G20 plays a strategic role. The government needs to recognize the interrelated relationship between economic growth, environmental sustainability, and social progress (Harto et al., 2022). This relationship is often known as the "green economy." The need for a systematic approach to legislation, planning, investing, and action plans for reducing inequality, community engagement, ecological responsibility, and wealth creation is one of the key challenges in industrial growth and development.

Corporate governance that guarantees a corporation is sustainable, accountable, and responsible to society is the result of the industry development and advancement (Pogge & Sengupta, 2015). These developments lead us to some important questions about the industry's view of sustainability as well as social responsibility (Singh et al., 2018). Because sustainability is closely related to corporate social and environmental responsibility initiatives, it is important for companies to pay attention to the value, events, reactions, and needs of investors to maximize firm value so that social responsibility disclosure can be a strategy for companies (Setiawan et al., 2019).

Corporate Social Responsibility (CSR) is a social accountability report that must be disclosed by the firm in its annual report as stipulated in Law Number 40 of 2007. In current history, CSR is no more a form of corporate responsibility for the ecosystem, community, and social concerns; it is only a means of evading reporting duties (Bose et al., 2018). For example, the Indonesian government requires companies to set aside a maximum of 2% of their net profit for social activities. Companies can state that they have performed their CSR obligations but are directly unable to handle issues related to them (Hussain et al., 2021).

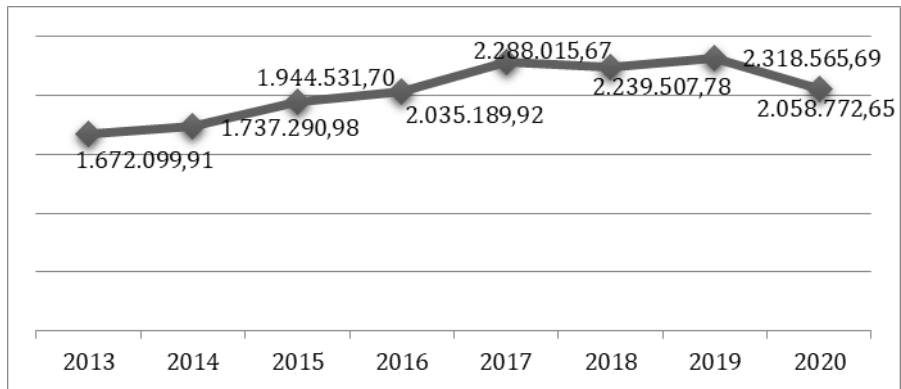
Sharia principles and the Muslim population are business opportunities that have prospects, as evidenced by the existence of Islamic capitalization worldwide including in Indonesia. The demographics of Indonesia are mostly

Muslims whose lives are influenced by Islamic values derived from Islamic law (Wahyudi & Puspita, 2022). The disclosure of Sharia-compliant information can attract Indonesians, who are majority Muslims, to become investors in Sharia-compliant companies.

The disclosure of important and essential information about the company's activities in conformity with Islamic principles is one way to satisfy the needs of investors. Islamic Social Reporting (ISR) is a kind of corporate social responsibility reporting based on Sharia principles to fulfill its responsibilities as *khalifatul-ardh fil ardh* to Allah and Muslims in general (Setyani et al., 2022). As a proof that their investing operations conform to Islamic precepts, Muslim investors want ISR disclosure.

Firm value is the company's performance as represented by its share price, which is determined by the demand and supply of the capital market and represents the public's opinion of the firm's success (Aras et al., 2017). One measure of a firm value is the market capitalization value of the Jakarta Islamic Index (JII) for the period 2013-2020.

Figure 1 indicates that the capitalization value of the IDX-launched Sharia stock index JII, which consists of 30 issuers, is increasing over time. Although the market capitalization value of JII has declined between 2018 and 2020, the overall value of this market capitalization indicates that Islamic enterprises in JII are performing well. One of the many elements that might affect a firm value is micro-factors, often known as "basic factors" (Harto et al., 2022). This company's core factors are factors that the company can influence. The firm's annual reports, financial statements, social responsibility reports, and corporate governance reports are analytical tools for analyzing fundamental factors. Islamic social reporting should be included in one of these reports due to the fact that ISR disclosure might be investors' consideration when making investment choices (Othman & Thani, 2010b). Consequently, the firm value is a consequence of the ISR disclosure that Sharia-compliant businesses must execute.



Source: Data by Researchers (2022)

Figure 1. Market Capitalization Jakarta Islamic Index

Earlier research showed more about the use of ISR in Islamic banks. Maali et al. (2006) and Kamla & Rammal (2013) conducted these studies to quantify the degree to which Islamic businesses practice ISR. According to Othman & Thani (2010a), the use of ISR in selected firms' annual reports is considered negligible. A solid ISR disclosure will provide a favorable signal to shareholders, which will increase the firm value. Cahya et al. (2017), Ratri & Dewi (2017), Nohong et al. (2019), Setiawan et al. (2019) and Jihadi et al. (2021) found that ISR disclosure has a positive influence on firm value. However, Ani (2017) and Wahyuni et al. (2019) concluded that there is no beneficial effect.

This issue becomes required because of the explanation of each variable and the discrepancies between some of the study outcomes discussed above. The discrepancy in outcomes is assumed to be caused by the firm size, which tends to reveal varied social responsibility, resulting in a difference in the firm value. As a result, the purpose of this research is to investigate the impact of these factors on business value. In order to maximize the company's value in sharia companies listed in the Jakarta Islamic index, there needs to be an effort for companies to minimize conflicts due to information asymmetry, especially in social aspects as part of the company's strategy. This research

will be useful for investors to determine the influence of Islamic social reporting on company value and as information that their investment activities in a company are in line with Islamic principles.

Literature Review

Principals (shareholders) require relevant and full information on the firm's overall status, yet shareholders do not have access to this information, despite the fact that it is utilized to make economic choices (Orazalin & Mahmood, 2020). Thus, there is a difference in the information that is owned and known between the agent and the principal, which is referred to as "information asymmetry." Minimizing information asymmetry requires broad disclosure of information by the firm, namely by conducting credible, relevant, and complete reporting (Esa & Ghazali, 2012).

Agency theory also posits that the presence of information asymmetry leads to fraudulent acts by the agent, which have an influence on business value and may be mitigated by transparent, accountable, responsible, and comprehensive information reporting (Zambon et al., 2019). One of the expansions of the disclosure of firm information that can minimize conflicts is social reporting. The better the firm's accountability reporting to stakeholders, the more positively the public and investors respond (Aras et al., 2017).

In addition, the good image expressed through reporting and attached to the firm will have an impact on high consumer loyalty to the firm's products so that investors are more interested in the firm, which will have an effect on improving the firm value (Høgevold et al., 2015). Thus, it can be concluded that social reporting as a firm accountability reporting is one of the fundamental factors that can increase firm value.

Islamic social reporting describes corporate social reporting from an Islamic viewpoint (ISR). According to Rahma & Bukair (2015), accountability is the connection between the person and the organization and God. ISR is the norm for reporting the social performance of Sharia-compliant enterprises,

since traditional social reporting is no longer applicable to them (Farida et al., 2022).

Conventional social reporting has limitations, therefore, it is required to develop a conceptual framework for social reporting, namely ISR based on Sharia (Haniffa & Cooke, 2005). ISR is a form of effort to account for the worship of "Muamalah" to Allah Almighty. The form of a servant's sincerity in perfecting his faith both vertically and horizontally, ISR is also a form of certainty for stakeholders in applying the principle of prudence related to the suitability and incongruity of Islamic values in business activities that will affect them in making economic decisions and religious decisions (Al-Musali & Ku Ismail, 2016).

In this study, an ISR disclosure index designed by Haniffa & Cooke (2002) is used, which adds one theme to the ISR disclosure index designed by Othman & Thani (2010), namely corporate governance. Thus, there are 48 disclosure items of Islamic Social Reporting which are divided into six themes, namely 1) Financial and Investment, 2) Goods and Services, 3) Personnel, 4) Society, 5) Environment, and 6) Corporate Governance.

The primary objective of a company is to increase shareholders' wealth (Nohong et al., 2019). Information and statistics pertinent to the firm value are crucial for investors to know what level of welfare the investor will get (Pogge & Sengupta, 2015). To achieve optimal corporate value requires the continuity of goals and harmony of interests between management and shareholders (Wahyudi & Puspita, 2022). This is consistent with the emphasis of agency theory on determining contracts between management and shareholders in the most efficient manner (Ibrahim & Muthohar, 2019). Efforts to increase firm value are always disrupted due to information asymmetry and agency conflicts. Thus, financial statements that provide full, relevant, and necessary information for shareholders may become a media manager to account for their performance in order to offer shareholders with signals to evaluate the firm's performance (Wahyuni et al., 2019).

The Tobin-Q ratio is used to determine the firm value in this research. Tobin-Q is one of the ratios that can provide the best information. This is because the Tobin-Q ratio can reflect the firm's assets, reflect market sentiment, as well as reflect an intellectual model or intangible assets whose value is very significant in the firm compared to the tangible assets owned by the firm (Nohong et al., 2019).

A company's objective is to maximize shareholder wealth through dividends and raise the firm value as shown by the stock price. Stockholders will be more successful as the stock price rises. This occurs if investors react favorably to the company's shares and do so in a manner that raises the stock price (Kte'pi, 2012). Therefore, in order to maximize firm value and actualize a business that is going concerned, it is crucial for firms to pay attention to the value, events, and reactions as well as the demands of investors (Rizfani & Lubis, 2019).

Hypothesis Development

The disclosure of ISR may assist businesses in maximizing the value. The higher the stock price, the more prosperous the shareholders. This happens if there is a positive response by investors and gives a good reaction to the company's shares so that the stock price increases. When formulating policies, it's critical for the company to take a variety of social and environmental concerns into account that might subsequently have an influence on growing firm value if it wants to constantly maximize firm value (Farooq & de Villiers, 2019). Because the company's prospects are viewed favorably, the ISR disclosure might send a good message to investors. The stock price will be affected by this encouraging indicator, which will raise the firm value.

The aforementioned claim is confirmed by the findings of studies by Cahya et al. (2017), Ratri & Dewi (2017), Nohong et al. (2019), Setiawan et al. (2019) and Jihadi et al., (2021), which demonstrate that ISR disclosure increases business value. Ani (2017) and Wahyuni et al.'s (2019) research show that ISR disclosure has no effect on the value of a business.

ISR disclosure increases a firm value, according to research by Cahya et al. (2017), Ratri & Dewi (2017), Setiawan et al. (2019), and Jihadi et al. (2021). Another study by Nohong et al. (2019) demonstrates that ISR disclosure significantly and favorably affects business value. Despite the fact that Ani (2017) and Wahyuni et al. (2019) demonstrate that ISR disclosure has no impact on business value, and based on the foregoing description, the following is the study's hypothesis:

H: Islamic Social Reporting has a positive impact on the firm value.

Research Methods

Associative research is the methodology employed in this study. The population is companies that went public and were registered with JII for the years 2016 to 2020. Thirty issuers are registered with JII. The 30 issuers are the Sharia stocks with the largest trading volume on the Indonesia Stock Exchange (IDX). Companies as samples of this study were chosen using a purposive sampling strategy. The standards used by researchers for their samples are listed in table 1.

The company's annual report, which met the criteria, served as the secondary source of data for this study. A complete examination (content analysis) of the annual reports of each Sharia firm registered with JII was conducted using the websites of each firm and www.idx.co.id in order to gather the necessary ISR data.

ISR was used as both a dependent and independent variable in this study. Othman & Thani (2010) created an index to measure this variable. The ISR disclosure item index consists of 48 disclosure items, which are broadly divided into 6 themes: finance and investment, products and services, employees, community, environment, and corporate governance. The ISR index is measured using a checklist with a score of 1 if the company reveals the item, and a score of 0 if it does not.

Table 1. Sample Criteria

No	Sample Criteria	Number of Companies
1	Companies registered in JII for the period 2016-2020	30
2	Companies that passed the review by the IDX in May and November during the period 2016-2020	(15)
3	Companies whose annual reports are available during the period 2016-2020	(2)
4	Companies that present financial statements in rupiah	13

As for identifying ISR index items, the content analysis method is utilized. The calculation of the ISR disclosure rate is as follows (Othman & Thani, 2010b):

$$ISRD = \frac{\text{Number of items disclosed}}{\text{Sum of all index items}} \times 100\% \quad (1)$$

In this study, the firm value serves as the dependent variable. Tobin's Q results are interpreted as follows: if the calculated result is between 0 and 1, it indicates that the cost of replacing the asset exceeds the stock's market value. This indicates that the market places a lower value on the firm. Moreover, a result larger than 1 implies that the market value of the stock surpasses the value of the firm's assets. This implies a good market response to the firm. The following represents a measurement of the firm value (Nohong et al., 2019):

$$FV = \frac{(\text{Closing share price} \times \text{Number of shares outstanding}) + \text{Book value of debt}}{\text{Book value of total assets}} \quad (2)$$

In this research, firm size is the control variable. Size is frequently used to explain many features of a business (Jihadi et al., 2021). In order to collect the required information, controlling and supervising agents for large corporations incurs considerable agency expenses. Consequently, the firm's level of disclosure is influenced by its size (Fuente et al., 2017). This research uses firm size to create empirical evidence that ISR has an influence on firm value irrespective of unstudied external variables. Using the total asset value, this research calculates the firm size as follows (Jihadi et al., 2021):

$$FS = \text{Natural logarithm of total assets} \quad (3)$$

As previously described, an operational definition of a variable is developed in order to measure the variables required in this instance. In this work, descriptive statistics and classical assumption tests were employed for data analysis. Descriptive statistics give an overview and description of data based on the mean, standard deviation, variance, maximum, minimum, total, range, kurtosis, and skewness (distribution density) without trying to make population-wide conclusions. In this research, the classical assumption test includes three tests: the autocorrelation test, the heteroscedasticity test, the normality test, and the Goodness of Fit Test of a Model.

The goal of the goodness-of-fit test for a statistical model is to assess whether the regression function of the sample forecasts the actual value properly, given the frequency of expectations generated from the hypothesized distribution. The test may be evaluated using the value of the coefficient of determination, the statistical value of f , and the statistical t -value. The objective of linear regression analysis is to determine whether or not there is a correlation between independent variables and dependent variables. This test also assesses the strength of the link between two or more variables and identifies the direction of the relationship between the dependent and independent variables. The following describes the regression analysis employed in this study:

$$FV = \alpha + \beta ISR + \beta FS + \varepsilon \quad (4)$$

Note:

ISR	: Islamic Social Reporting
FV	: Firm Value
FS	: Firm Size
α	: Constant
β	: Parameters to be estimated
ε	: Error

Results and Discussion

This study was conducted on Jakarta Islamic Index-listed companies. JII contains only 30 of the most liquid Sharia-compliant stocks listed on the IDX. Following the financial services authority's twice-yearly review of the Sharia securities list, the 30 Sharia stocks are reviewed. This study drew samples from companies registered with JII between 2016 and 2020 using purposive sampling. There are thirteen sampled companies that meet the criteria where these companies were observed for five consecutive years, resulting in the collection of sixty-five data. Following is a description of the data analysis employing content analysis and secondary data from independent and dependent variables processed with SPSS version 26 software.

The variables utilized in this investigation are outlined in table 2. The minimum is the smallest value in an observation series of a data group, whereas the maximum is the greatest value possible. The standard deviation is calculated by dividing the number of available data by the square root of the variance between the information value and the mean, divided by the number of accessible data. The ISR variable has a minimum value of 58.33, which belongs to PT Bumi Serpong Damai Tbk in 2020, and a maximum value of 85.42, which belongs to PT Unilever Indonesia in 2017. The standard deviation of the ISR is 6.08, while the average value is 73.65. Since the mean value exceeds the standard deviation, this indicates that the ISR variable data is reasonably correct, as it implies that the ISR variable has a small error standard. Moreover, this study indicated that the theme of investment and finance was the least prevalent throughout the observation year among JII-registered Islamic enterprises. However, the usury item is the sole item that is always declared by the firm, as shown in the form of interest income and interest expenses in the firm's financial statements. Also, zakat products were never disclosed by the company during the observation period. The most prevalent topics during the observation period were environmental and socioeconomic ones.

This demonstrates the company's commitment to social responsibility. Moreover, the employee topic is revealed somewhat after the financial and

investment subject, as the company does not disclose if Muslim employees have the facilities and rights to do worship and other Islamic activities. Lastly, there are aspects of corporate governance that have never been reported by Sharia firms, particularly the composition, performance, and reunification of the Sharia Advisory Council. This is because Sharia businesses in JII lack a Sharia monitoring board to ensure that their operational activities adhere to Islamic principles. In 2019, PT Indofood CBP Sukses Tbk has the lowest value of the firm value variable, whereas PT Unilever Indonesia Tbk has the highest value in 2017. The average value of the firm value variable is 3.03, indicating that these companies are valued by investors at three times their book value. The firm's standard deviation from its variable value is 4.68. The firm size is the control variable in this study. In 2019, PT Matahari Department Store Tbk holds the lowest value of the firm size variable at 29.21, while PT Bumi Serpong Damai Tbk holds the highest value at 33.49. The firm size variable has a standard deviation of 1.11 and an average value of 31.51. Since the mean is larger than the standard deviation, the data for the firm size variable in this study are quite accurate, as indicated by the modest standard error.

Table 2. Descriptive Statistical Analysis Results

Variable	N	Minimum	Maximum	Mean	Std. Deviation
FS	65	29,21	33,49	31,51	1,11
ISR	65	58,33	85,42	73,65	6,08
FV	65	0,31	23,29	3,03	4,68

The objective of the classical assumption test is to ensure that the regression equation accurately estimates, is not biased, and is consistent (best linear unbiased estimator). The normality is 0.43, which represents the likelihood of significance. Consequently, it is known that all variables are normally distributed because both have a value for asymp.sig (2-tailed) larger than 0.05 or 5%. Multicollinearity demonstrates that multicollinearity does not exist among the variables in this investigation. Because the firm size

tolerance value is 0.739 and the variable's tolerance value is more than 0.10, each of the 1,353 VIF values for the firm size variable is less than 10.00. Each firm size variable and ISR has a tolerance value of 0.983 and a VIF value of 1.018, where the tolerance value exceeds 0.10 and the VIF value falls below 10.00. Therefore, it may be argued that there is no multicollinearity in this research model. The significance value of the firm size variable is 0.088, and the significance value of the ISR variable is 0.786%. Both variables are more important than 0.05, so it could be said that heteroscedasticity does not exist. The dw value is 1.852, which exceeds the du table value of 1.6621 and is less than 2.338 (4-du). Therefore, it can be stated that neither the positive nor negative autocorrelations were present in the regression data of this investigation.

Table 3 is a estimation result for the Islamic social reporting variable, firm size (control variable), and firm value. As seen in the table 3, the ISR variable has an estimated t-value of 3.270 and a significance of 0.002. This estimated t value is more than the table t value of 1.66980 ($3.270 > 1.66980$), showing that the ISR has a positive effect on the firm value, which is supported by a significance value of less than 0.05. ($0.002 < 0.05$). Thus, one may claim that ISR has a positive and large effect on the value of the company. In this regression model, the control variable, firm size, has a calculated t-value of -3,194 with a significance value of 0.002. Because the significance value is less than 0.05 ($0.002 < 0.05$), a negatively calculated t value indicates that the firm size has a significant negative effect on its value. Thus, it may be argued that the firm size has a negative effect on its value.

The F test was run to see if the variables in the regression model had a collective influence on variable Y. In the regression model, the estimated F value in table 3 is 9.324 times that of table 2.75, with a significance level of $0.000 < 0.05$. On the basis of these results, we may infer that the ISR and firm size control variables are co-responsible for the firm value. The model's corrected R-square value was calculated to be 0.206, or 20.6%, according to table 3. This indicates that the ISR variable influences the firm value by 20.6%, whereas other variables influence the firm value by 79.4%. The

hypothesis of this research is that ISR enhances the firm value. The test results for this regression model are shown in Table 3. According to the table, the coefficient value for the ISR variable is 3.270, and its significance is 0.002. This confirms the study's premise that ISR has a substantial and favorable effect on the firm value.

Table 3. Estimation Result

Variables	Performance		
FS	-1.507	-3.194	0.002
ISR	0.282	3.270	0.002
Prob. F (Statistic)	0.000		
R	0.481		
R Square	0.231		
Adjusted R Square	0.206		

These findings indicate that a company's market value increases according to the extent to which it discloses ISR in its annual report. ISR disclosure enables investors, creditors, and other stakeholders to monitor the firm's activities to ensure social and sharia compliance, hence fostering accountability and transparency (Esa & Ghazali, 2012). This demonstrates that organizations with extensive ISR disclosures can attract investors. When Muslim investors and stakeholders receive firm information that complies with Sharia principles, they do not hesitate to invest their funds, resulting in a high demand for shares, a high stock price, and a high firm value (Abubakar, 2016).

In addition, this conclusion supports the agency theory, which suggests that the presence of information asymmetry that leads to fraud committed by management and a decline in firm value can be mitigated by the existence of transparent, accountable, responsible, and comprehensive information (Indrawaty & Wardayati, 2016). With ISR as a kind of transparent, accountable, responsible, and comprehensive information reporting in line with Sharia, information asymmetry can be reduced. This leads to a positive response from investors and stakeholders, which is good for the firm value.

This study's findings are consistent with those of prior research (Cahya et al., 2017; Ratri & Dewi, 2017; Nohong et al., 2019; Setiawan et al., 2019; and Jihadi et al., 2021). However, contrary to the findings of Ibrahim & Muthohar (2019), ISR has a negative impact on the firm value. In addition to the findings of Ani (2017) and Wahyuni et al. (2019), it revealed that ISR had no impact on the value of the company.

In addition, the regression model contains firm size control factors. The coefficient has a value of -3,194 and a significance level of 0.002 according to Table 3. This test indicates that the firm size has a negative influence on its value. This result indicates that a one-unit increase in the firm size, assuming all other parameters stay constant, would result in a 3,194 decrease in the firm value. According to this research, firm size, as measured by its total assets, is a bad signal for investors if it is extremely large.

According to Jihadi et al. (2021), the negative signal occurs due to two investor assumptions. Firstly, if a large company owns a large number of assets, the management will be free to operate existing assets, and this freedom is proportional to investors' concerns about opportunistic management actions. Second, the firm size has a negative effect on its value since investors perceive that corporations with big total assets have more retained profits than dividend payouts to shareholders. Consistent with prior research demonstrating that firm size has a negative effect on firm value, specifically the research of Jihadi et al. (2021) and a study published in the *Journal of Accounting and Economics*, the results of this study indicate that firm size has a negative impact on firm value (Idawati et al., 2021).

Conclusion

This research aims to determine the influence of Islamic social reporting (ISR) on the market value of Jakarta Islamic Index companies. This study's sample comprised up to 65 firm-year reports from 13 companies throughout a five-year observation period, 2016 to 2020. Testing of data indicates that Islamic social reporting has a significant positive impact on business values. Consequently, the study's hypothesis was validated. Thus, the expansion of

information in accordance with Sharia principles, i.e. the firm's ISR, will raise the firm value. This circumstance arises when investors and stakeholders respond positively by investing in the company, resulting in an increase in the stock price and a subsequent growth in the firm value. And based on the results of the test, the variable control of the firm size on its value reveals that the firm size has a significant negative impact on its value.

This research can be expanded by considering the following suggestions, which can be used as a guide for future research; 1) It is recommended that regulators present a Sharia supervisory board, such as in the Islamic financial and banking sector, as a party that oversees the firms' operations and regulates policies for Islamic companies in Indonesia, so that they can operate in accordance with Sharia principles; 2) The recommendation for future study is to increase the usage of research samples. Not only firms listed on the Jakarta Islamic Index, but also corporations included on the Sharia Securities List, can be used as samples (DES). Sharia companies registered with JII cannot be utilized as representatives of the whole Sharia industrial sector in Indonesia, as only two to three companies represent each industry. To be able to determine the overall situation of Sharia-compliant companies in Indonesia, it is possible to expand the research sample and develop ISR disclosure items comprehensively and appropriately, taking into account the characteristics of Sharia-compliant companies in Indonesia, or to avoid subjective interpretation of ISR items.

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