

The Role of Firm Strategy to Intervene the Influence of Corporate Social Performance on Corporate Financial Performance

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ABSTRACT

Objective – A Corporate Social Responsibility (CSR) implementation has been implemented since over 50 years ago. All of the CSR implementation divided into two categories, namely Strategic CSR and Non-Strategic CSR. A Strategic CSR implementation should consider the firm strategy based on the CSR concept and firm strategy. Some empirical studies have tested the influence of CSR on Corporate Financial Performance. The results of those studies are still inconclusive.

Methodology/Technique – The purpose of this study is to analyze firm strategy as intervening variable between Corporate Social Performance and Corporate Financial Performance. This study used capital intensity and product differentiation to measure the firm strategy. The samples were 33 companies of LQ-45, listed in Indonesian Stock Exchange.

Findings – The results did not indicate that firm strategy intervenes the influence of Corporate Social Performance on Corporate Financial Performance, both directly and indirectly.

Novelty – The research suggests future studies to employ the other ratios representing Firm Strategy that will strengthen the literature.

Type of Paper: Empirical

Keywords: Corporate Financial Performance; Corporate Social Performance; Firm Strategy; Non-Strategic CSR; Strategic CSR.

JEL Classification: L25, M14, M41

1. Introduction

Corporate Social Responsibility (CSR) is a form of company's commitment to give short-term and long-term contributions to its environment and society in order to realize sustainable development through the configuration of the principles of social responsibility, the process of social responsiveness, policies, programs, and the results related to firm social relationship (Maignan & Ralston, 2002; Waddock & Graves, 2007). CSR has been implemented since the 1950's and keeps growing until now.

CSR implementation consists of two categories: Non-Strategic CSR and Strategic CSR. Initially, the implementation of CSR was a result of pressure from stakeholders to pay attention to the concept of sustainable development. In reality, the implementation of the CSR concept is oriented to the realization of social responsibility called non-strategic CSR. The concept is developed by considering firm strategy in a CSR

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implementation called Strategic CSR (Berman et al., 1999; Sayekti, 2015). Strategic CSR is the embodiment of CSR which not only meets the philanthropic responsibility but also becomes profitable part of the company through positive image and goodwill publication (Lantos, 2002). Strategic CSR refers to the consideration of firm strategy into the implementation of CSR (Sayekti, 2015). Firm strategy contains the vision and mission of company invested in the CSR implementation in order to attract or obtain the interest of stakeholders, such as investors and public society, to invest and consume products and services, thus increasing Corporate Financial Performance by maximizing profits.

Porter (1980) divides the measurement dimensions of firm strategy into two categories: cost leadership and product differentiation. According to Hambrick (1983), cost leadership can be measured in two ways: cost efficiency and asset persimony. Cost efficiency is the ratio of cost of goods sold to total sales and assets persimony measured by two ratios i.e. the ratio of capital intensity (total assets divided by number of employees) and capital expenditure (net capital expenditure divided by total sales). While product differentiation is measured by using selling intensity as measured by selling expense divided by total sales.

Prior studies had examined the influence of Corporate Social Performance (CSP) on Corporate Financial Performance (CFP) but still showed inconclusive results. Furthermore, Sayekti (2015) found a strategic CSR implementation in Indonesia. It can be analyzed that there was a consideration of firm strategy in a CSR implementation in Indonesia. Then, the study of Berman et al. (1999) with a different model also found firm strategy intervened the influence of stakeholder relationship on Corporate Financial Performance.

This study aims to analyze the role of Firm Strategy to intervene the influence of Corporate Social Performance (CSP) on Corporate Financial Performance (CFP) on companies listed in LQ-45 of Indonesia Stock Exchange from 2013 to 2015. This study uses CSP to reflect the stakeholder relationship in Berman's study. LQ-45 was selected because it reflected the 45 companies with the best Corporate Financial Performance in Indonesia Stock Exchange.

This study applied two theories in the hypothesis development, namely stakeholder theory and signaling theory. Stakeholder theory explains how companies get pressure from stakeholders, such as investors, governments, employees, communities, and society to implement CSR (Freeman, 1984; Donaldson & Preston, 1995; Lee, 2008; Munilla & Miles, 2005). Meanwhile, signaling theory stated by Watts and Zimmerman (1986) is used to describe the company's efforts to provide a signal to stakeholders related to the implementation of CSR disclosure by issuing CSR reports either in the form of standalone report and incorporated with annual report (Scott, 2009). Furthermore, the CSR report is expected to get a positive response from stakeholders, especially investors in order to increase the value of shares and the public society to consume the products of companies that implement CSR, which thus ultimately increases companies profit (Scott, 2009; Godfrey et al., 2010).

Many previous studies have been conducted to analyze the effect of CSR on Corporate Financial Performance and results are still inconclusive. The implementation of strategic CSR not only meets the embodiment of corporate responsibility to the surrounding environment but also makes the implementation of CSR have benefits to the company through positive image publication by considering firm strategy into the implementation of CSR (Lantos, 2002; Sayekti, 2015). Consideration of Firm Strategy in CSR implementation aims to support the achievement of corporate goals to maximize profits.

Berman et al. (1999) also found that firm strategy intervened the influence of stakeholder relationship on Corporate Financial Performance. Stakeholder relationship can be reflected by the quality of CSR performance because the existence of CSR is caused by the pressure of stakeholders (based on stakeholder theory). This study used Capital Intensity and Product Differentiation to measure firm strategy. Thus, the hypotheses of this study are as follows: (1) Capital Intensity (CI) intervenes the influence of CSR on Corporate Financial Performance and (2) Product Differentiation (PD) intervenes the influence of CSR on Corporate Financial Performance.

2. Methods

This research is quantitative research using secondary data i.e financial statements and annual reports of LQ-45 companies, for the period of 2013 to 2015. Sampling criteria for this study are: (1) companies already registered in LQ-45 per February 2014, February 2015, and February 2016 and (2) companies that published annual report and financial statement during the period of 2013 to 2015.

2.1 Measurement of Variables

There are 3 variables in this study. The measurements are as follows: (1) Corporate Social Performance (CSP): measured by using checklist of Global Reporting Initiative (GRI) Generation 4, year 2015, the concept of this GRI tries to measure CSR disclosure of companies based on the concept of the triple bottom line namely profit, people and planet (3P), consisting of 150 item checklists; (2) Firm Strategy (FS): Firm Strategy is measured by using two types of ratios namely capital intensity calculated by dividing total assets by the number of employees in the company and product differentiation calculated by dividing selling expense to total sales or revenues (Berman et al., 1999); (3) Corporate Financial Performance (CFP): measured by looking for value of Return On Asset (ROA), by dividing net profit to total assets. ROA is a profitability ratio that is intended to measure ability level of return of company on overall funding to the activities of company with the purpose of generating profits by exploiting its assets (Libby, et al., 2008).

2.2 Empirical Model

This study uses a model of path analysis in order to analyze the role of Firm Strategy to intervene the effects of Corporate Social Performance (CSP) on Corporate Financial Performance (CFP).

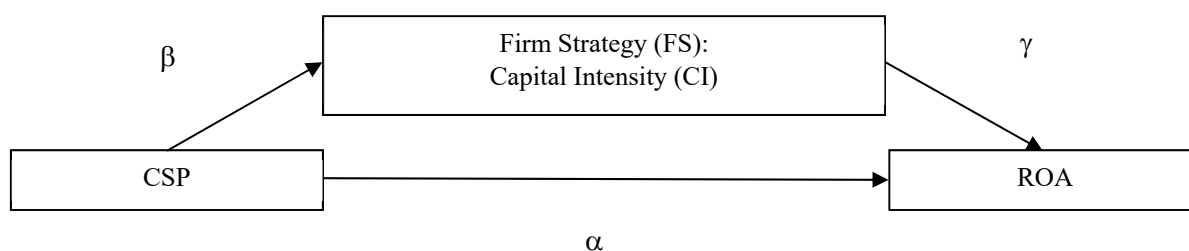


Figure 1. Model 1 of Intervening Test for Capital Intensity

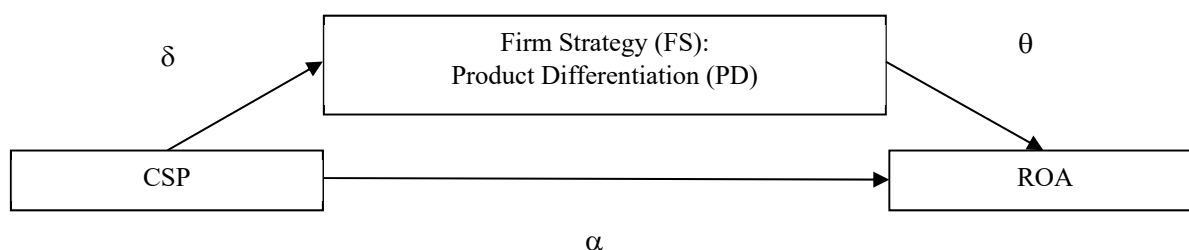


Figure 2. Model 2 of Intervening Test for Product Differentiation

$$ROA = \alpha_0 + \alpha_1 CSP \tag{1}$$

$$CI = \beta_0 + \beta_1 CSP \tag{2}$$

$$PD = \gamma_0 + \gamma_1 CSP \tag{3}$$

$$ROA = \delta_0 + \delta_1 CI \tag{4}$$

$$ROA = \theta_0 + \theta_1 PD \tag{5}$$

Where:

- CFP : Corporate Financial Performance
- ROA : Return on Asset
- CI : Capital Intensity
- PD : Product Differentiation
- α_0 : Constant coefficient for equation 1
- α_1 : CSP coefficient for equation 1
- β_0 : Constant coefficient for equation 2
- β_1 : CSP coefficient for equation 2
- γ_0 : Constant coefficient for equation 3
- γ_1 : CSP coefficient for equation 3
- δ_0 : Constant coefficient for equation 4
- δ_1 : CI coefficient for equation 4
- θ_0 : Constant coefficient for equation 5
- θ_1 : PD coefficient for equation 5

Following calculations to indicate direct effect, indirect effect, and total effect of firm strategy to intervene CSP on CFP:

Model 1:

- Direct Effect = α_1
- Indirect Effect = $\beta_1 \times \gamma_1$
- Total Effect = $\alpha_1 + (\beta_1 + \gamma_1)$

Model 2 :

- Direct Effect = α_1
- Indirect Effect = $\delta_1 \times \theta_1$
- Total Effect = $\alpha_1 + (\delta_1 \times \theta_1)$

3. Results

3.1 Descriptive Statistic

Table 1. Descriptive Statistic

	N	Minimum	Maximum	Mean	Std. Deviation
CSP	99	.1467	.4733	.3208	.0868
ROA	99	.0180	.7151	.0945	.0913
CI	99	749364.2332	10412881562579.1740	141651092790.1344	1055240296489.9170
PD	99	.0006	.9832	.1716	.2003
Valid N (listwise)	99				

In table 1 are seen the values of minimum. maximum, average, and standard deviations for each variable both the dependent variable and independent variables, where:

- Descriptive data from Corporate Social Performance (CSP), the minimum value is 0.1467 and maximum value is 0.4733, whereas the mean of CSP is 0.3208 and standard deviation is 0.0868
- Descriptive data from Return on Asset (ROA), the minimum value is 0.0180 and the maximum value is 0.7151, whereas the mean of ROA is 0.0945 and standard deviation is 0.0913.

- Descriptive data from Capital Intensity (CI), the minimum value is 749,364.2332 and maximum value is 10,412,881,562,579.1740 while the mean of CI is 141,65,092,790.1344 and standard deviation is 1,055,240,296,489.917.
- Descriptive data from Product Differentiation (PD), the minimum value is 0.0006 and maximum value is 0.9832 while the mean of PD is 0.1716 and standard deviation is 0.2003.

3.2 Regression Results

Table 2. The Influence of Corporate Social Performance (CSP) on Return On Asset (ROA)

	Coef. (t-value)	
Constant	0.104	***
	(2.934)	
CSP	0.030	
	(3.969)	
R ²	0.028	
Adj. R ²	-0.009	

*** Sign at $\alpha = 1\%$

** Sign at $\alpha = 5\%$

* Sign at $\alpha = 10\%$

As indicated in table above, Corporate Social Performance (CSP) variable which is measured by GRI checklist does not show significant result with positive coefficient. It can be concluded that CSP does not significantly influence Return On Asset (ROA) which measures Corporate Financial Performance (CFP).

Table 3. The Influence of Corporate Social Performance (CSP) on Capital Intensity (CI)

	Coef. (t-value)	
Constant	-5.268	
	(-1.304)	
CSP	2.084	*
	(1.713)	
R ²	0.171	
Adj. R ²	0.019	

*** Sign at $\alpha = 1\%$

** Sign at $\alpha = 5\%$

* Sign at $\alpha = 10\%$

As indicated in the table above, Corporate Social Performance (CSP) variable shows a significant result with positive coefficient. It can be concluded that CSP significantly influence on Capital Intensity (CI) which measures Firm Strategy.

The result of PD as indicated in the table 4, Corporate Social Performance (CSP) variable does not show significant result with positive coefficient. It can be concluded that CSP does not significantly influence Product Differentiation (PD) which measures Firm Strategy.

Table 4. The Influence of Corporate Social Performance (CSP) on Product Differentiation (PD)

	Coef. (t-value)
Constant	0.124 (1.590)
CSP	0.150 (0.641)
R ²	0.065
Adj. R ²	-0.006

As indicated in the table 5 below, Capital Intensity (CI) variable does not show significant result with negative coefficient. It can be concluded that CI does not significantly influence Return On Asset (ROA) which measures Corporate Financial Performance (CFP).

Table 5. The Influence of Capital Intensity (CI) on Return On Asset (ROA)

	Coef. (t-value)	
Constant	0.096 (10.324)	***
CI	-1.082 (-0.935)	
R ²	0.095	
Adj. R ²	-0.001	

*** Sign at $\alpha = 1\%$
 ** Sign at $\alpha = 5\%$
 * Sign at $\alpha = 10\%$

As indicated in the table 6 below, Product Differentiation (PD) variable does not show a significant result with negative coefficient. It can be concluded that PD does not significantly influence Return On Asset (ROA) which measures Corporate Financial Performance (CFP).

Table 6. The Influence of Product Differentiation (PD) on Return On Asset (ROA)

	Coef. (t-value)	
Constant	-0.018 (8.027)	***
PD	-0.018 (-0.394)	
R ²	0.040	
Adj. R ²	-0.009	

*** Sign at $\alpha = 1\%$
 ** Sign at $\alpha = 5\%$
 * Sign at $\alpha = 10\%$

3.3 Intervening Model Result

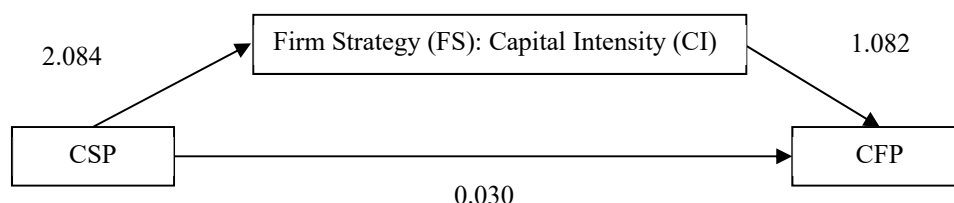


Figure 3. Model of Intervening Test of Capital Intensity

From this result indicates that the effect of CSP on CI through its beta value is 2.084 and the effect of CI on CFP through the beta value is 1.082. Multiplication result of both beta value is 2.2549 which shows the amount of indirect effect of CSP on CFP. Meanwhile the direct effect of CSP on CFP is 0.030 and the total effect is 2.2849. The result of sobel test shows a value of 1.7138 with a significance level of 0.087. It shows that Capital Intensity as measurement variable of Firm Strategy does not significantly intervene the influence of CSP on CFP with a significance value of <0.05 . It can be concluded that Hypothesis 1 of this study is rejected.

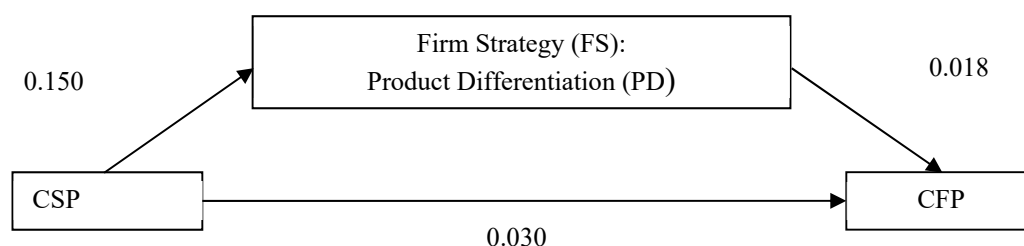


Figure 4. Model of Intervening Test of Product Differentiation

The results indicate that the effect of CSP on PD through its beta value is 0.150 and the effect of PD on CFP through its beta value is 0.018. Multiplication result of both beta value is 0.0027 which shows the amount of indirect effect of CSP on CFP. While the direct effect of CSP on CFP is 0.030 and the total effect amounted to 0.0327. The result of sobel test shows a value of 0.3340 with a significance level is 0.7384. It shows that Product Differentiation as measurement variable of Firm Strategy does not significantly intervene the influence of CSP on CFP with a significance value of <0.05 . It can be concluded that Hypothesis 2 of this study is rejected.

4. Discussion

The purpose of this study is to analyze the role of Firm Strategy to intervene the influence of Corporate Financial Performance (CSP) on Corporate Financial Performance (CFP). Samples used in this study is 33 companies had consistently been in the LQ-45 Indonesia Stock Exchange in 3 periods from 2013-2015. This study used Corporate Social Performance (CSP) as another proxy of Stakeholder Relationship based on the pressure of stakeholder to implement CSR. Strategic CSR base is particularly used to indicate how Firm Strategy intervenes the influence of CSP on CFP. Firm strategy is measured by two ratios, namely Capital Intensity (CI) and Product Differentiation (PD).

The results of this study show that both ratios do not show any intervening role in the influence of CSP on CFP. Thus, these results do not support the result of Berman et al. (1999), which indicating that Firm Strategy intervenes the influence of Stakeholder Relationship on Corporate Financial Performance. This study also does not show any consideration of firm strategy in the implementation of CSR. It means that there is no implementation of Strategic CSR in 33 companies listed in the LQ-45. An obvious reason why there is no firm strategy role in intervening the influence of CSP on CFP is because of the measurement of CSP. This study uses GRI checklist to measure CSP. CSP is a global standard of CSR reporting and measurement. It has possibility to be unsuitable with the Indonesian setting. Therefore, it needs more suitable measurement of CSP. Besides, the CSR implementation in Indonesia does not grow as well as that in European Countries. The mining Indonesian companies probably just implement CSR without any other motives as mandated by the government, and non-mining companies probably just implement CSR voluntarily also without other motives. Those can be another reason why firm strategy is not considered in the CSR implementation in Indonesia.

The result of this study also does not support the result of study of Sayekti (2015) that show that Strategic CSR positively influences Corporate Financial Performance. The difference of both study results can be explained by the object of both study. This study involved only 33 companies in LQ-45. So that, it only shows

the specific CSR implementation practice in LQ 45 companies, not a whole companies in Indonesia Stock Exchange.

Therefore, future studies can be conducted by using the other objects or type of company which probably show different results with this study. Besides, future studies are also expected to employ the other ratios representing Firm Strategy. Firm Strategy can be measured by some other ratios. Porter (1980) divides the measurement dimensions of firm strategy into two: cost leadership and product differentiation. Cost leadership can be measured in two ways: cost efficiency and asset parsimony, asset parsimony can be measured by capital intensity and capital expenditure. Then product differentiation is measured by using selling intensity (Hambrick, 1983). The last recommendation for future studies is employing the other financial ratios representing the measurement of corporate financial performance.

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