Financial and Social Performance of Indonesia’s State-Owned Islamic Banks

Utari Evy Cahyani
Faculty of Islamic Economics and Business, State Institute of Islamic Studies (IAIN) Padangsidimpuan, Padangsidimpuan, Indonesia
utari@iain-padangsidimpuan.ac.id

Rizal Ma'ruf Amidy Siregar
Faculty of Islamic Economics and Business, State Institute of Islamic Studies (IAIN) Padangsidimpuan, Padangsidimpuan, Indonesia
riza@iain-padangsidimpuan.ac.id

Abstract
The government has started the process of merging three state-owned banks’ sharia subsidiaries to accelerate the growth of Islamic banking in Indonesia. This study was conducted to see the effect of financial performance as measured by Return on Assets (ROA) and Firm Size on social performance as measured by Islamic Social Reporting (ISR) index. This study uses data that form of annual reports published by Bank Syariah Mandiri (BSM), Bank Negara Indonesia Syariah (BNIS) and Bank Rakyat Indonesia Syariah (BRIS) in 2010-2019. Islamic Social Reporting (ISR) is the dependent variable with Return on Assets (ROA) and Firm Size as independent variable. Fixed effect model is better than random effect model in this research. ROA have no effect on ISR. Whereas Firm Size have positive effect on ISR. It means that the larger banking size the better the social performance. The newly merged state-owned sharia bank with a larger size is expected to improve social performance.

Keywords: Islamic Social Reporting, Profitability, Firm Size, Islamic banking, panel data

Introduction

The growth of Islamic banking in Indonesia shows positive sign. There have been 14 sharia commercial banks, 20 sharia business units, and 164 sharia rural banks in the medieval of 2020 (OJK, 2020). On the other hand, the market share growth is relatively slow. Table 1 shows the growth of Islamic banking market share from 2010-2019.

Table 1 The Market Share of Indonesian Islamic Banking Industry

<table>
<thead>
<tr>
<th>Year</th>
<th>Islamic Banking (Rp Billion)</th>
<th>Conventional Banking (Rp Billion)</th>
<th>Market Share (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2010</td>
<td>97,519</td>
<td>2,911,334</td>
<td>3.24</td>
</tr>
<tr>
<td>2011</td>
<td>145,467</td>
<td>3,507,365</td>
<td>3.98</td>
</tr>
<tr>
<td>2012</td>
<td>195,018</td>
<td>4,067,569</td>
<td>3.58</td>
</tr>
<tr>
<td>2013</td>
<td>242,276</td>
<td>4,712,191</td>
<td>3.98</td>
</tr>
<tr>
<td>2014</td>
<td>244,197</td>
<td>4,763,898</td>
<td>4.89</td>
</tr>
<tr>
<td>Year</td>
<td>Islamic Banking (Rp Billion)</td>
<td>Conventional Banking (Rp Billion)</td>
<td>Market Share (%)</td>
</tr>
<tr>
<td>------</td>
<td>-----------------------------</td>
<td>-----------------------------------</td>
<td>------------------</td>
</tr>
<tr>
<td>2015</td>
<td>296,262</td>
<td>6,132,583</td>
<td>4.88</td>
</tr>
<tr>
<td>2016</td>
<td>356,504</td>
<td>6,729,799</td>
<td>5.29</td>
</tr>
<tr>
<td>2017</td>
<td>424,181</td>
<td>7,387,634</td>
<td>5.74</td>
</tr>
<tr>
<td>2018</td>
<td>477,327</td>
<td>8,068,346</td>
<td>5.92</td>
</tr>
<tr>
<td>2019</td>
<td>507,761</td>
<td>8,411,000</td>
<td>6.04</td>
</tr>
</tbody>
</table>

Source: Sharia Banking Statistics (2020)

The government has started the process of merging three state-owned banks’ sharia subsidiaries to accelerate the growth of Islamic banking in Indonesia. The merger of three state-owned banks, Bank Mandiri, Bank Rakyat Indonesia (BRI) and Bank Negara Indonesia (BNI), along with their sharia subsidiaries, Bank Syariah Mandiri (BSM), Bank Rakyat Indonesia Syariah (BRIS) and Bank Negara Indonesia Syariah (BNIS) aims to create a stronger Islamic bank. The state-owned Islamic Bank is expected to improve market share and to help improve the Islamic financial industry. Hence, it is also be a good financial and social performance.


There are several approaches to measure Islamic banks social performance using corporate social responsibility Amran et al., (2017), maqashid sharia Rusydiana & Sanrego, (2018), and Islamic social reporting (ISR). Based on sharia enterprise theory, principle gives the main form of accountability to God (vertical) which is then translated into the form of accountability (horizontal) to the human race and the natural environment. (Triyuwono, 2001) The ISR disclosure reflects the company’s social performance.

First, there are five themes in ISR disclosure that is finance and investment, product and service, employee, society, and environment (Haniffa, 2002). The theme of good governance added lately (Othman et al., 2009). The development of ISR disclosure in Indonesia is still relatively slow. The sharia-approved companies in the Indonesia Stock Exchange have not fully adopted ISR (Cahyani et al., 2020). According to the previous research, Islamic banks in Indonesia had not yet achieved 100% implementation and disclosure of ISR (Sofyani et al., 2012).
Research on the relationship between financial performance and social performance is interesting to study. The companies with good financial performance have more opportunities to provide social responsibility. According previous research, relationship of Profitability that proxied by return on assets (ROA) and ISR showed the various results. Some research concluded that ROA had no effect on ISR (Rama, 2014), (Rachmania & Alviana, 2018), (Noordin & Kassim, 2019). Other research conclude that ROA have positive effect on ISR (Hussain et al., 2020). On the other hand, research conclude that ROA have negative effect on ISR (Hajawiyah et al., 2019).

In terms of company size, the company with bigger assets have more opportunities to provide social responsibility. Previous research describe that company size have positive effect on ISR (Hajawiyah et al., 2019), (Sari & Helmayunita, 2019), (Hussain et al., 2020), (Mukhibad & Fitri, 2020), (Amyulianthy et al., 2020). Other studies suggest that firm size has no effect on ISR (Lestari, 2013), (Noordin & Kassim, 2019).

Based on the description above, several previous studies have proven that the effect of financial performances on disclosure of corporate social responsibility shows inconsistent results. This study was conducted to see the effect of financial performance as measured by Return on Assets (ROA) and Firm Size on social performance as measured by Islamic Social Reporting (ISR) index. This research have a novelty that explore relation of financial and social performance in state-owned Islamic banks before merger. The Islamic bank mergers are expected to improve performance not only financial performance but also social performance.

**Review of Literature**

*Islamic Social Reporting (ISR)*

This study uses Legitimacy theory and Sharia Enterprise Theory to explain Islamic Social Reporting as a research variable. Legitimacy theory asserts a social contract between a firm and communities where it operates (Deegan et al., 2002). Every firm is bound to consider this social contract and various implications of their operations on society. The sharia enterprise theory gives the main form of accountability to God (vertical) which is translated into the form of accountability (horizontal) to the human race and the natural environment (Triyuwono, 2001). The disclosure of Islamic social reporting is different from conventional social reporting framework. It is because of the fact that underlying principles for ISR is the Islamic principles. The disclosure of these items is imperative for spiritual needs of various Islamic bank stakeholders. The ISR reflects social performance of Islamic banks (Hussain et al., 2020).
The objectives of ISR (Haniffa, 2002) are (1) as a form of accountability to Allah and society, (2) to increase transparency of business activities by presenting relevant information by taking into account the spiritual needs of Muslim or sharia investors in decision making. The form of accountability in question, such as (a) providing halal and good products, (b) fulfilling the rights of Allah and society, (c) pursuing a reasonable profit in accordance with Islamic principles, (d) achieving business objectives, (e) Becoming employees and the community, (f) ensuring ecologically sustainable business activities, and (g) making work a form of worship. The form of transparency is (a) providing information regarding all halal and haram activities carried out, (b) providing relevant information regarding financing and investment policies, (c) providing relevant information regarding employee policies, (d) providing relevant information regarding the relationship with community, and (e) provide relevant information regarding resource use and environmental protection. There are six themes to estimate the ISR index namely finance and investment, products/services, employees, community, environment (Haniffa, 2002) and corporate governance (Othman et al., 2009).

**Profitability**

Based on Stakeholder Theory, management provides information to stakeholders (shareholders, creditors, customers, suppliers, government, society, and other parties) to maintain the company’s success (Freeman, 2010). The existence and success of the company is dependent on the persistence of support from stakeholders (Ullmann, 1985) The higher profitability is associated with more environmental disclosure. (Gamerschlag et al., 2011) In the ISR context, profitable company practice ISR increasing the stakeholders’ confidence for huge. (Mallin et al., 2014) However, based on the legitimacy theory, profitability can be regarded to be either positively or negatively related to CSR disclosure. Furthermore, every firm must make complete disclosure, whether it is profitable or not under the Islamic perspective. (Surtono, 2009) With regard to the relationship between firm profitability and corporate social reporting, the higher profitability of firm the more driven to disclose of ISR. (Othman et al., 2009)

H1. There is a positive relationship between profitability and ISR.

**Firm Size**

The legitimacy theory provides that businesses are bound by the social contract in which the company agree to perform various socially desired actions in return to approval of their objectives and other rewards. (Brown & Deegan, 1998) The larger companies are more visible to the public, have more market power and more newsworthy (Watts & Zimmerman, 2006). With regard to the relationship between
firm size and social reporting, larger companies have complex portfolio of activities and resources, which cause more disclosure about the environment and stakeholders (Othman et al., 2009). In the context of banking industry, larger banks have serious agency concern that make practice of more social disclosure. Based on the agency theory considerations, risk-related information is disclosed by a firm to a larger extent in their narrative section of company annual report (Elzahar & Hussainey, 2012).

H2. There is a positive relationship between firm size and ISR).

**Research Method**

This research use three Islamic banks namely BSM, BNIS, and BRIS. This study uses data that form of annual reports published by the company in 2010-2019. Islamic Social Reporting (ISR) is the dependent variable in this study. Variable independent in this study are Return on Assets (ROA) and Firm Size.

ISR is calculated using the content analysis (Klaus Krippendorff, 2004) method on the company’s annual report. There are 43 statements items to estimate ISR. (Haniffa, 2002),(Othman et al., 2009) Each item gets 1 if there is disclosure in the annual report and gets 0 if there is no disclosure about it. ISR Index calculate as (Number of Disclosed Items/Maximum Number of Score)*100%. ROA is measured by comparing net income with total assets. While Firm Size is measured by the natural logarithm of Total Assets.

This study use panel data regression with 10 years data from 2010-2019 data and the number of companies is 3. The panel data equation used in this study is:

\[
ISR_{it} = \beta_0 + \beta_1 ROA_{it} + \beta_2 Firm\ Size_{it} + \epsilon_{it}
\]

Where:

- \(i\) = Companies (1-3),
- \(t\) = Year (2010-2019),
- \(\beta_0\) = constant,
- \(\beta_1, \beta_2\) = coefficient,
- \(ISR\) = Islamic Social Reporting Index,
- \(ROA\) = Return on Assets (Net Income/Total Assets),
- \(Firm\ Size\) = Ln Total Assets, and
- \(\epsilon\) = error term.

This research uses significance level (\(\alpha\)) 5 %.

In this study, to estimate the parameters with panel data, there are two techniques namely the Fixed Effect Model (FEM) and the Random Effect Model (REM)
(Firdaus, 2020). This research use Hausman test to choose between FEM and REM. The null hypothesis (H0) in this test is Random Effect Model. While the alternative hypothesis (H1) is Fixed Effect Model. If the F probability of the Hausman test results is greater than alpha (0.05) H0 is rejected, which means the REM model is better (Widarjono, 2018).

Results and Discussion

Variable Description

ISR disclosure in BSM, BNIS and BRIS from 2010 until 2019 indicate a positive trend. Table 2 explains the disclosure average scores in the ISR for each theme. Based on ISR calculation from 3 Islamic banks in 2010-2019, corporate governance theme has the highest average score of 95.0%, followed by product/services, community, employee, and financial and investment. While the lowest disclosure score is environment theme at 42.8%. Corporate governance theme have perfectly implemented in BSM, BNI Syariah and BRI Syariah since 2016 and all objects achieved a perfect score (100%). Environmental themes are not widely expressed in financial reports because the focus of the banking business is not directly related to the environment. BSM implemented a green banking program in 2011 followed by BRI Syariah in 2015 and BNI Syariah in 2017. The main targets are set to reduce GHS emissions by conducting green operations activities and providing green financing within the context of Green Banking.

Table 2 The Disclosure Average Scores in the ISR

<table>
<thead>
<tr>
<th>Year</th>
<th>Finance and Investment</th>
<th>Product/Services</th>
<th>Employee</th>
<th>Community</th>
<th>Environment</th>
<th>Corporate Governance</th>
</tr>
</thead>
<tbody>
<tr>
<td>2010</td>
<td>67</td>
<td>75</td>
<td>57</td>
<td>64</td>
<td>14</td>
<td>87</td>
</tr>
<tr>
<td>2011</td>
<td>67</td>
<td>83</td>
<td>63</td>
<td>70</td>
<td>19</td>
<td>87</td>
</tr>
<tr>
<td>2012</td>
<td>67</td>
<td>83</td>
<td>67</td>
<td>79</td>
<td>29</td>
<td>93</td>
</tr>
<tr>
<td>2013</td>
<td>67</td>
<td>83</td>
<td>73</td>
<td>82</td>
<td>33</td>
<td>93</td>
</tr>
<tr>
<td>2014</td>
<td>67</td>
<td>83</td>
<td>73</td>
<td>85</td>
<td>33</td>
<td>100</td>
</tr>
<tr>
<td>2015</td>
<td>67</td>
<td>92</td>
<td>80</td>
<td>85</td>
<td>38</td>
<td>93</td>
</tr>
<tr>
<td>2016</td>
<td>67</td>
<td>92</td>
<td>90</td>
<td>88</td>
<td>38</td>
<td>100</td>
</tr>
<tr>
<td>2017</td>
<td>67</td>
<td>100</td>
<td>93</td>
<td>88</td>
<td>48</td>
<td>100</td>
</tr>
<tr>
<td>2018</td>
<td>67</td>
<td>100</td>
<td>97</td>
<td>94</td>
<td>48</td>
<td>100</td>
</tr>
</tbody>
</table>
The descriptive statistical results of this study are in Table 3. The average value of the ISR is 73.83%. While the highest ISR value is 86.00%, namely BSM in 2018-2019 and BNI Syariah 2017-2019. The lowest value is 44 %, namely BRI Syariah in 2010-2011. ISR value of close to 100% indicates that the company has reported sharia social responsibility reporting.

The highest ROA is 2.25 % and the lowest is -0.04 % and the average is 1.06 %. The average ROA is 1.06 %, which means that the bank produce Rp 106 of profit every Rp 10,000 it has invested in its assets. The highest and lowest Firm Size are 11.63 and 8.76 while the average is 10.30767.

Table 3 Descriptive Statistic

<table>
<thead>
<tr>
<th>Variables</th>
<th>N</th>
<th>Mean</th>
<th>Median</th>
<th>Max</th>
<th>Min</th>
<th>Std. Dev.</th>
</tr>
</thead>
<tbody>
<tr>
<td>ISR</td>
<td>30</td>
<td>0.738333</td>
<td>0.770000</td>
<td>0.860000</td>
<td>0.440000</td>
<td>0.113626</td>
</tr>
<tr>
<td>ROA</td>
<td>30</td>
<td>1.064667</td>
<td>1.170000</td>
<td>2.250000</td>
<td>-0.040000</td>
<td>0.608054</td>
</tr>
<tr>
<td>Firm Size</td>
<td>30</td>
<td>10.30767</td>
<td>10.37500</td>
<td>11.63000</td>
<td>8.760000</td>
<td>0.797594</td>
</tr>
</tbody>
</table>

Source: Source name (Year)

Model Selection in Panel Data

The next stage is model selection using Hausman test. This test evaluate which panel model is the most suitable model to estimate the relationship between financial and social performance. Table 4 describe output of panel data selection model. According to the Hausman Test results, the probability value is 0.0000 < 0.05, so the FEM model is better than the REM model.

Table 4 Test Results of Panel Data Model Selection

<table>
<thead>
<tr>
<th>Chi-Square Statistic</th>
<th>Chi-Square d.f.</th>
<th>Probability</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cross-section random</td>
<td>53.099604</td>
<td>2</td>
</tr>
</tbody>
</table>

Relationship between Financial and Social Islamic Banking Performance

The next stage after model selection is the estimation of panel data model. Table 5 describe regression result fixed effect model.

Table 5 Regression Results Fixed Effect Model and Random Effect Model

<table>
<thead>
<tr>
<th>Coefficient</th>
<th>Probability</th>
</tr>
</thead>
</table>

22
<table>
<thead>
<tr>
<th></th>
<th>Coefficient</th>
<th>P-Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>C</td>
<td>-0.894537</td>
<td>0.0000</td>
</tr>
<tr>
<td>ROA</td>
<td>-0.012297</td>
<td>0.4368</td>
</tr>
<tr>
<td>Firm Size</td>
<td>0.159683</td>
<td>0.0000</td>
</tr>
<tr>
<td>Adj R-Square</td>
<td>0.873907</td>
<td></td>
</tr>
<tr>
<td>N</td>
<td>30</td>
<td></td>
</tr>
</tbody>
</table>

The coefficient of determination (adjusted R-square) is 0.873907 or 87.39%. This value indicates that the variation of the ISR can be explained by the variation of ROA and Firm Size. The rest is explained by other variables outside the model.

Based on the regression result, the probability value for ROA is 0.4368 > 0.05. This means that there are no influence between ROA to ISR in state-owned Islamic banks 2010-2019. This result is in line with previous research which state that ROA have no effect to ISR (Noordin & Kassim, 2019; Rachmania & Alviana, 2018; Rama, 2014; Rizfani & Lubis, 2019). Disclosing ISR should be a responsibility no matter whether the company is making more or less profit or even loss (Haniffa, 2002).

The probability value for Firm Size is 0.0000<0.05 and positive coefficient sign. It means that Firm Size have a positive effect on ISR in state-owned Islamic banks 2010-2019. The studies of (Amyulianthy et al., 2020; Hajawiyah et al., 2019; Hussain et al., 2020; Mukhibad & Fitri, 2020; Sari & Helmayunita, 2019) validated a positive impact on ISR. The large size of firms have the lower agency costs and disclose more information to their stakeholders. With the merger process, the new state-owned Islamic bank can increase social performance.

**Conclusion**

The objectives of this research was to investigate the relationship between financial and social performance of state-owned Islamic bank 2010-2019. Financial performance proxied by profitability (ROA) and firm size (Ln Total Assets). While, the social performance proxied by Islamic Social Reporting. Panel data with the fixed effect model is used to analyze these relationships. The results showed that firm size have a positive effect on ISR. It means the large size of firms have the lower agency costs and disclose more information to their stakeholders. The new state-owned Islamic bank can increase social performance.

**Limitation**

The weakness of this research is sample size (only 3 Islamic banks). Further research on financial and social performance of state-owned Islamic bank also needs to be done after the merger. Because of this research using Islamic Social Reporting as
a proxies of social performance, need to consider other indicators to see social performance

References


Indonesia, 5(2), 131–145.

