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The Influence of Corporate Social Responsibility, Corporate Governance and Firm Size, on the Value of Manufacturing Companies in Indonesia: Profitability as Mediation

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This study tests the effect of Corporate Social Responsibility, Good Corporate Governance, and Firm Size on firm value, with profitability as an intervening variable. The population was 133 manufacturing companies listed on the Indonesia Stock Exchange in 2013-2018. A census method was used to sample secondary data from the financial statements of listed companies in that period. Path analysis was used to analysis data using the Partial Last Square (PLS) program. The results are that Corporate Social Responsibility, Good Corporate Governance, and Firm Size have a positive effect on profitability and firm value. Profitability is an intervening variable between the relationship of Good Corporate Governance, Corporate Social Responsibility, and Firm Size to firm value. The study is a reference for government in building policies about the extent of the implementation of corporate social responsibility in Indonesia. The area is regulated by Indonesian Law no. 40 (2007) about Limited Liability, and relates to increasing investor perceptions about financial performance, corporate governance, and firm size.

Key words: *Good Corporate Governance, Corporate Social Responsibility, Firm Size, Firm Value.*

Introduction

The perception of firms' value is based on investors' perceptions about high social values, such as attention to social conditions, the economy, and the environment. Investors believe that if a company cares about the environment, maintains good corporate governance, and increases the scale of the company, it can improve financial performance. Improved financial performance is a positive signal for investors, so that firm value will be higher. Most financial performance is measured by profitability (Ahmad and Sulaiman, 2004; Chen and Wang, 2011; Ding et al., 2016).

Many studies have related corporate social responsibility, good corporate governance, and firms size, to firm value and financial performance. But they have showed different results. Corporate social responsibility directly affects firm value (Chen and Wang, 2011; Wan Ahamed et al., 2014; Ding et al., 2016; Li et al., 2016). A Different result was achieved by (Aras et al., 2010; Becchetti et al., 2012). Corporate social responsibility directly affects financial performance as measured by profitability (Byus et al., 2010; Malik, 2014; Moser and Martin, 2012; Jang et al., 2013; Choi et al., 2010). A Different result was achieved by (Spitzeck, 2009; Wan Ahamed et al., 2014). Good corporate governance directly affects the value of a firm (Al-Rashed, 2010; Connelly et al., 2012; Wei, 2012; Singhal, 2014; Lozano et al., 2016) and is not in line with (Jo and Harjoto, 2011; Berthelot et al., 2012; Mouselli and Hussainey, 2014). Good corporate governance directly affects financial performance (Shleifer and Vishny, 1997; Jhunjhunwala and Mishra, 2009; Megawati, 2010), and is not in line with (Ragers and Hayibor, 2009). Study results show the firm size positively affects financial performance (Buzzell and Bradley, 1987; Siagian et al., 2013; Wei, 2012; Singhal, 2014; Lozano et al., 2016). The firm size has a directly affect on firm value (Chen and Wang, 2011; Li et al., 2016). Different results show that firm size does not affect profitability (Amato and Wilder, 2001; Al-Rashed, 2010) while Imelda (2011) shows that profitability affects firm value.

Many research results are inconsistent with the effects of corporate social responsibility, good corporate governance, and company size on profitability and firm value. These findings motivate researchers to conduct more complex research. Because of that, whether it is a theoretical explanation or empirical study which still happens to be controversial, the present researchers are interested in researching the effect of corporate social responsibility, corporate governance, and firm size on value firm with profitability as a mediator. Therefore this study addresses manufacturing companies listed on the Indonesian stock exchange between 2013 and 2018. A horizon time economics model is used. There is the threat of a trade war between America and China in 2018, forcing manufacturers to be able to continue to balance the desires of consumers and company offerings. It is also forcing companies to be competitive in both domestic and international markets. This period affects fluctuations in company value. The implication of this research is strengthened by the theory of legitimation, stakeholder theory, agency theory and signalling theory. Such theories are also a reference for government in building policies about how far the implementation of corporate social responsibility in Indonesia is to be implemented, under Indonesian Law no. 40 year 2007, which relates to limited liability.

Literature Review

Agency Theory

Agency problems (agency problems) arise from duties between management and shareholders. Managers can make decisions that are not in accordance with the aim of maximizing shareholder welfare. Agency problems can be minimized by stricter monitoring, through good corporate governance (Wan Ahamed et al., 2014; Ding et al., 2016; Li et al., 2016).

Signalling Theory

Signalling theory explains how signals of success or failure of management (agent) inform the owner (principal) (Chen and Wang, 2011; Jang et al., 2013). Success in increasing profitability through corporate social responsibility reporting, the application of good corporate governance, and company size is a positive signal for investors. The market price of stocks responds well to this success, increasing company value (Moser and Martin, 2012; Jang et al., 2013).

Stakeholder Theory

Stakeholder theory states that companies are not entities that only operate for their own interests, but must benefit their stakeholders (Choi et al., 2010; Ding et al., 2016). This theory explains social and environmental disclosure behaviour, implementation of corporate governance, and company size. The company will try to satisfy stakeholders by disclosing the information needed (The company will try to satisfy stakeholders by disclosing the information needed) (Jang et al., 2013).

Legitimacy theory

A company has a contract with the community to carry out its activities based on the values of justice. Legitimacy theory encourages companies to ensure that their activities and performance are acceptable to the public through annual reports, to illustrate the impression of environmental, economic, and social responsibility (Choi et al., 2010; Ding et al., 2016;

Jang et al., 2013). Legitimacy from the community will impact financial performance and company value.

The Effect of Corporate Social Responsibility on Profitability

Disclosure of corporate social responsibility is one company mechanism that can be used to communicate with stakeholders. Corporate social responsibility becomes an entry point to gain profits or improve legitimacy, and to strengthen the brand image of goods and services produced. This strategy is an appropriate tool to increase company sales which impact on increasing profitability. Corporate social responsibility directly effects financial performance as measured by profitability (Byus et al., 2010; Malik, 2014; Moser and Martin, 2012; Jang et al., 2013; Choi et al., 2010). Based on this, the hypotheses tested are:

H_1: Corporate social responsibility effects the profitability of manufacturing in Indonesia.

The Effect of Good Corporate Governance on Profitability

The implementation of good corporate governance will minimize risks arising from a company's activities, so as to increase optimal profitability. Increased profits are directly related to the value of profitability. Good corporate governance directly affects financial performance (Shleifer and Vishny, 1997; Jhunjhunwala and Mishra, 2009; Megawati, 2010). Ownership of shares by financial institutions is a strong factor in maintaining good financial performance. Based on this, the hypotheses tested are:

H_2: Good corporate governance effects the profitability of manufacturing in Indonesia.

The effect of firm size on profitability

Big companies will be chosen more by investors because of the assurance of certainty of operations and better future business prospects. Large scale can create high profitability in a firm. The size positively affects financial performance (Buzzell and Bradley, 1987; Siagian et al., 2013; Wei, 2012; Singhal, 2014; Lozano et al., 2016). Based on this, the hypotheses tested are:

H_3: Firms' size affects the profitability of manufacturing in Indonesia.

The Effect of Corporate Social Responsibility of Firm Value

Social disclosures in the annual reports of companies that go public have been shown to increase share trading volume. Most investors respond well to the social information that companies present in annual reports. The wider social disclosure in the annual report can affect the trading volume of the company's shares; there is a surge in trade around the publication of the annual report. Corporate social responsibility directly affects firm value (Chen and Wang, 2011; Wan Ahamed et al., 2014; Ding et al., 2016; Li et al., 2016). Based on this, the hypotheses tested are:

H_4: Corporate social responsibility affects the value of manufacturing companies in Indonesia.

The Effect of Good Corporate Governance on Firm Value

The benefits of implementing good corporate governance can be seen from the premium that investors are willing to pay for the company's equity (market price). If investors are willing to pay more, then the market value of companies that implement corporate governance will be higher than companies that do not apply corporate governance practices. Good corporate governance directly affects the value of firms (Al-Rashed, 2010; Connelly et al., 2012; Wei, 2012; Singhal, 2014; Lozano et al., 2016). Based on this, the hypotheses tested are:

H_5: Good corporate governance affects the value of manufacturing companies in Indonesia.

The Effect of Firms' Size on Firm Value

Big companies have broader interests, so various large company policies will have a greater impact on the public interest compared to smaller companies. For investors, the company's policy will have implications for the prospect of cash flow in the future. Investors are more interested in the company's good financial condition, so that the company's value increases. The firm size directly affects firm value (Chen and Wang, 2011; Li et al., 2016). Based on this, the hypotheses tested are:

H_6: Firm size affects the value of manufacturing companies in Indonesia.

The Effect of Profitability on Firm Value

Every company wants high company value because it shows the prosperity of shareholders. Investors believe that high profits can provide a high level of return (dividends), so the perception of potential investors towards the company is higher, followed by an increase in the company's stock market price. The higher the ability to obtain profits, the greater the return expected by investors, heightening the company's value. Profitability is influential upon firm value (Imelda, 2011). Based on this, the hypotheses tested are:

H_7: Profitability affects the value of manufacturing companies in Indonesia.

Research Method

Types, and Data Resources

The type of data used is secondary data received by www.idx.co.id. The population of this research is manufacturing companies listed in the Indonesian Stock Exchange from 2013 until 2018; 133 companies. The saturated population technique was used to acquire 42 manufacturing companies for the research.

Definition of Operation

The study consists of three variables, namely the independent variable (good corporate governance, corporate social responsibility, and firm size), the dependent variable (firm value), and mediating variable (profitability). Corporate social responsibility (X1) was measured based on the corporate social responsibility disclosure index, under the Global Reporting Index (Chen and Wang, 2011; Jo and Harjoto, 2011; Li et al., 2016). This index will be scored at 1 if the firm discloses and 0 if the firm does not disclose. The good corporate governance measure is based on institute authority (Jang et al., 2013; Jhunjhunwala and Mishra, 2009; Megawati, 2010). Firm size is based on total assets at year end, as adopted from Amato and Wilder (2001) and Wei (2012). Profitability uses the proxy of Return on Equity (Jang et al., 2013; Jhunjhunwala and Mishra, 2009). Firm value is based on the Price to Book Value (Li et al., 2016; Ding et al., 2016).

Data Analysis

This research uses path analysis with the help of Partial Least Square (PLS). PLS testing criteria consists of outer (indicators) and inner model (structural) testing. Several reasons for choosing PLS are that it is based on (a) theory; (b), empirical research results; (c) analogies of relationships between variables of difference knowledge fields; (d) normative cases, such as government rules, laws, etc.; and (e) other rational relationships.

Results and Discussions

This research consists of 42 samples of manufacturing companies. The variables' descriptive statistics used in this research are summarised in Table 1.

Table 1. Descriptive Statistic

Variable	Sample	2013	2014	2015	2016	2017	2018	Mean
Social Responsibility of Firm (X_1)	42	0.7519	0.7988	0.8716	0.8923	0.9178	0.9378	0.8617
Good Corporate Governance (X_2).	42	71.5200	73.3490	73.4952	73.7831	73.8988	74.6324	73.3984
Firm Size (X_3).	42	11.9494	11.9916	12.0537	12.4167	12.5304	13.0217	12.3272
Profitability (Y_1)	42	0.2140	0.1710	0.1939	1.1408	1.6721	1.8354	0.8712
Firm Value (Z_1)	42	1.8580	1.9335	2.3166	2.6781	2.8117	2.9072	2.4175

Based on Table 1 the mean of corporate social responsibility is 0.8617. The value is close to 1. That means the responsibility disclosure is already vast, and appropriate to the Global Reporting Index standards. The mean of good corporate governance is 73,3984 or mostly authority of institute stock is 73%. This indicates that the side of institute investors may encourage managers to focus attention on firm's performance, decreasing opportunistic or selfish acts. The mean of firm size with indicator of total assets is 12.3272. This indicates that manufacturing companies have total assets above 100 billion Rupiah, in the category of big companies. The mean of profitability with ROE indicator is 0.8712. This indicates a capacity to produce net profit from firm equity in the amount of 87%. The mean of firm value with indicator PBV is 2.4175. This indicates that manufacturing has a decent firm value in the eyes of investors.

Outer Model Test (Indicator Test)

An outer model principally tests indicators of latent variables, or how far the indicator can explain latent variables. For reflective indicators like the one used in this research, the test was done by reading the result of outer loadings (convergent validity) presented in Table 2, discriminant validity presented in Table 3, and composite reliability presented in Table 4.

Table 2: Convergent Validity

Indicator	Original Sample (0)
institute Authority < GCG	1.000
CSDI < CSR	1.000
ROE < Profitability	1.000
Total Assets < Firm Size	1.000
PBV < Firm Value	1.000

Table 3: Discriminant Validity

Variable	**AVE**
GCG	1.000
CSR	1.000
Firm Size	1.000
Profitability	1.000
Firm Value	1.000

Table 4: Composite Reliability

Variable	**Composite Reliability**	**Variable**	**Composite Reliability**
GCG	1.000	Profitability	1.000
CSR	1.000	Firm Value	1.000
Firm Size	1.000		

Based on the results of outer loadings (convergent validity shown in Table 2), every indicator is already valid because they have a loading value above 0.5. From Table 3, it can be known that every variable has enough discriminant validity, because the result was shown in the amount above 0.5. The result of composite reliability shown in Table 4 shows that every construct is worthy of inner model testing, because the result was shown in the amount above 0.5.

Inner Model Test (Structural Test)

An inner model tests a hypothesis between a latent variable and other latent variables. This test looks at the result of analysis path. Stability in this estimation is tested by using a t-statistic test which is achieved by a bootstrapping procedure.

Path Analysis

Path analysis shows the influence and significance between latent variables in research. The result of analysis path can be seen by how large the coefficient of a structural path (path coefficients) and the value of t-values show the significance of the prediction model (Table 5). The resulting intervening variable test, as to direct and indirect influence, could be shown in Table 6.

Table 5: The Result of Path Coefficients (Hypothesis Test)

Coefficient Beta	Statistic	(0/STERR)	Significance (>1.96)	Hypothesis
GCG : Profitability	0.678	20.742	Significant	Accepted
CSR : Profitability	0.868	4.751	Significant	Accepted
Firm Size : Profitability	0.772	6.816	Significant	Accepted
GCG : Firm Value	0.353	2.464	Significant	Accepted
CSR : Firm Value	0.371	2.715	Significant	Accepted
Firm Size : Firm Value	0.364	2.795	Significant	Accepted
Profitability : Firm Value	0.808	18.890	Significant	Accepted

Table 6: Direct and Indirect Influence

Independent	Dependent	Mediation		Effect	
Variable	Variable	Variable	Direct	Indirect	Notes
GCG	Firm Value	Profitability	0.353	0.547	Mediation
CSR	Firm Value	Profitability	0.371	0.701	Mediation
Firm Size	Firm Value	Profitability	0.364	0.623	Mediation

Mediating Test

Based on Table 6, the coefficient direct influence of corporate social responsibility to firm value is 0,353. Then, its coefficient indirect is 0,547. Coefficient direct influence of good corporate governance to firm value is 0,371. Then, its coefficient indirect is 0,701. Coefficient direct influence of firm size to firm value is 0,353. Then, its coefficient indirect is 0,547. The conclusion is that profitability is a mediating variable, because coefficient value indirect is biggest than coefficient value direct of corporate social responsibility, good corporate governance, and firm size to value firm.

Discussions

The Effect of Corporate Social Responsibility to Profitability of Manufacturing Companies

Based on Table 5, corporate social responsibility is a positive effect on profitability, with a T-statistic 4,751 (4,751>1,96), and coefficient of 0,868. The result of this research supports legitimation theory. The companies have contracts with people to do their activities based on the value of justice, and how firms handle several groups of interests, to legitimate firm actions, and so revealing and performing social responsibility functions, affects how the firm gets its entrance to achieve profit and legitimation (Byus et al., 2010; Malik, 2014; Moser and Martin, 2012). Vaster disclosures will give positive signals to the sides cancerous to the firm (stakeholder) and also stakeholders (shareholder) (Jang et al., 2013; Choi et al., 2010). The vaster the information sent to stakeholder and shareholder, the more information regarding the firms is received.

The Effect of Good Corporate Governance on the Profitability of Manufacturing Companies

Based on Table 5, good corporate governance has a positive effect on profitability, with a T-statistic of 20,742 (20,742>1,96), and a coefficient 0,678. The result of this research receives empirical support from Shleifer and Vishny (1997), Jhunjhunwala and Mishra (2009), and Megawati (2010). Decent corporate governance is related to how sure the investors are that the manager will give them profits, not steal, obfuscate or invest in projects not related to the funds or capital transferred by investors, and it is related to how the investor controls the manager (Shleifer and Vishny, 1997; Megawati, 2010). The institution of ownership will professionally review the improvement invested by the firm, having high controls over management acts. This case will minimize the management potential of cheats, and can align management priority and other stakeholder priorities, to improve profitability.

The Effect of Firm Size on the Profitability of Manufacturing Companies

Based on Table 5, good corporate governance positively affects profitability, with a T-statistic of 6,816 (6,816>1,96) and a coefficient of 0,772. This research strengthens the empirical discovery that the firm with large total assets has already stepped into a mature stage, and also has the prospects of producing large profits compared to firms with small total assets (Buzzell and Bradley, 1987; Siagian et al., 2013; Wei, 2012). The large amount of consumer demand creates numerous manufacturing firms with large numbers of total assets, doing large-scale production, so that the number of total assets owned by firms will be automatically growing (Singhal, 2014; Lozano et al., 2016). The increase of total assets results in more funds for its operation, one of them being self-funding to achieve larger profit and improve the firm's performance (profitability).

The Effect of Corporate Social Responsibility on the Value of Manufacturing Companies

The implementation and disclosures of social responsibilities may give new functions to manufacturing companies, functions which decrease risks and the accouchement of deviation acts by the firm. The firms which have already performed their social responsibilities consistently will get vast support from the community which feels the utility of such activity. The result of this research receives empirical support (Chen and Wang, 2011; Wan Ahamed et al., 2014; Ding et al., 2016; Li et al., 2016). Corporate social responsibility will lift a firm's image, which in long term will improve the reputation of firms, influencing the increase of firm value (Ding et al., 2016; Chen and Wang, 2011). Corporate social responsibility can function as a protector, and help firms minimalize the bad effects of some crises.

The Effect of Corporate Governance on the Value of Manufacturing Companies

Institutional ownership is part of implementing corporate governance in firms. One of the roles of that ownership in realizing corporate governance is to encourage the building of adequate surveillance structures which improve the disclosure of financial reports. With decent corporate governance, firm's funds will be well-managed, which potentially improves both the capability of firms to create profits, and firm value. The result of this research accepts earlier research (see Al-Rashed, 2010; Connelly et al., 2012; Wei, 2012; Singhal, 2014; Lozano et al., 2016). These values are decided by market perceptions of the continuity of firm performance, as reflected by revolving stock market values. This result is also appropriate to agency theory. Numerous methods are implementable. One of them is surveillance by an outer investor, which limits company acts by the manager, decreasing the chances of deviation by managers. This will later improve firm value. The mechanism of the surveillance is the institutional stakeholder.

The Effect of Firm Size of the Value of Manufacturing Companies

The size of total assets owned by manufacturing firms show maturity. In this stage firms' cash flow is very good and also able to produce profits even though disturbed by the economic slowdown. Moving past the global crisis, the firm starts to rise and conditions became more stable, so there are many manufacturing firms which have huge total assets. The result of this research accept Chen and Wang (2011) and Li et al. (2016). It shows assets used in firms' operations. The improvement of assets, followed by growing the firm, can increase the trust between investors or other stakeholders towards firms, because the total of large assets can improve financial and market performance toward firms. Trust makes the investors interested in investing their funds with the firm. Therefore, manufacturing firms undergo improvement in firm value.

The Effect of Profitability on the Value of Manufacturing Companies

The profitability of manufacturing firms influences firm value. It causes the firm to be capable of producing profits for stakeholders with owned self-funds. High profits will give an indication of a firm with good prospects, so it can acquire the interest of investors who increase stock demand. Growing stock demand will then increase the firm's value. This result is also reflected by Imelda (2011). High profitability shows decent prospects, so that investors will respond positively and the firm's value will improve. The larger prosperity level given by the firm will interest investors to own the firm, and positively influence stock prices in the market. This will improve the value of the firm.

Conclusion

The conclusion of this research is that corporate social responsibility, good corporate governance, and firm size positively affects profitability and the value of manufacturing companies. Profitability is a mediating variable between the effect of corporate social responsibility, good corporate governance, firm size and firm value.

Limitations

Some of the limitations in this research are:

1. There is subjectivity in deciding indices, because there are no provisions which can be turned into standards or triggers, so the decision of an index for a fellow GRI indicator will differ between researchers.
2. The analysed period was only five years, so the results cannot be generalized to every type of firm listed in the BEI. Also, other similar conditions were not reflected.
3. The sample selection in this research used a non-probabilistic method, so that the firm was used as a sample for decided criteria.

Advice

Based on the conclusion and limitations of the described research, several recommendations can be made:

1. It is hoped that later researchers will do additional or other exogenous variable changes, to explain firm value on profitability more extensively.
2. Further, later researchers could add research samples, so result are more generalized, stronger and supplement each other even more.
3. It is recommended that later reearchers use a measuring index with numbers, such as a scale of 1-5 (litre scale), to avoiding subjective evaluations.
4. To improve profitability and firm value, firms in Indonesia must improve the revelations of corporate social responsibility, improve corporate governance, and have huge firm sizes.

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