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HOW CSR PERFORMANCE AND FINANCIAL REPORT QUALITY AFFECT CORPORATE SHARE PRICES? CASE OF INDONESIA

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ABSTRACT

Purpose: *This research intends to investigate the impact of financial report quality and CSR performance on the firm share prices.*

Methodology/approach: *The 78 firms-years observation of LQ-45 public listed companies in Indonesia from 2019 to 2020 is used in this study. The financial report quality is measured by the accrual-based model of earning management, while CSR performance is measured by the amount of CSR spending. The OLS regression is applied to test the hypotheses.*

Findings: *The findings show that there is no effect of financial report quality on the share prices. On the other hand, CSR performance plays an important role in influencing a company's share prices. CSR performance has a positive effect on share prices. The financial report failed to ensure that there is no existing information asymmetry within the organization. While CSR performance is a form of social-engaged activities in order to achieve social benefits and legitimation.*

Practical implications: *In the context of legitimacy and agency theory, these findings provide fruitful insight into how the firm performance is valued by investors, which is not only based on financial performance but also based on non-financial performance.*

Originality/value: *By providing a new measurement of CSR performance, this study is different to most existing CSR kinds of literature.*

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ABSTRAK

Tujuan penelitian: Penelitian ini bertujuan untuk menguji pengaruh kualitas laporan keuangan dan kinerja CSR terhadap harga saham.

Metode/pendekatan: Sampel menggunakan 78 perusahaan LQ-45 yang terdaftar di BEI tahun 2019-2020. Kualitas laporan keuangan diukur dengan menggunakan moel manajemen laba berbasis akrual, sementara kinerja CSR diukur dengan menggunakan jumlah *CSR Spending.* Alat uji yang digunakan untuk menguji hipotesis adalah regresi OLS.

Hasil: Hasil penelitian menunjukkan bahwa tidak ada pengaruh kualitas laporan keuangan terhadap harga saham perusahaan. Sementara itu, kinerja CSR menunjukkan pengaruh positif terhadap harga saham perusahaan. Hal ini disebabkan karena dalam laporan keuangan tidak dapat menjamin adanya asimetri inormasi dalam laporan yang disajikan. Di sisi lain, kinerja CSR merupakan bentuk aktivitas perusahaan yang berkaitan dengan tanggung jawab social yang bertujuan untuk memperoleh legitimasi.

Implikasi praktik: Dalam konteks *legitimacy theory* dan *agency theory,* hasil penelitian ini memberikan bukti empiris mengenai penilaian kinerja perusahaan oleh investor, yang tidak hanya berfokus pada kinerja keuangan saja, tetapi juga pada kinerja non-keuangan.

Orisinalitas/kebaharuan: Penelitian ini berkontribusi pada pengembangan literatur CSR dengan memberikan proksi pengukuran kinerja yang berbeda, yaitu dengan jumlah *CSR Spending.*

KATA KUNCI: Informasi Akuntansi; Kinerja CSR; Kualitas laporan keuangan; Nilai perusahaan; harga saham; Kinerja keberlanjutan.

INTRODUCTION

Accounting becomes the most important language of business. Accounting provides the instruments that shape capital markets that is called accounting principles. Financial accounting is the calculation process in preparing financial statements using both internal and external data. Financial reporting provides not only information related financial condition of firms, but also disclosure regarding important aspects such as regulatory rule, management's decision on accounting methods, and other key performance of companies. Financial reporting is said to have a high quality, if it meets the high-quality standards (Collis et al., 2012). Qualify financial reporting can improve the decisions making process through the accurate and reliable information.

The LQ-45 consist of 45 companies and becomes the top index in Indonesia. The LQ-45 stock index have the highest capitalization rates and become the most active traded shares in the stock exchange. The LQ-45 share have the high demand by investors because of its high capitalization and have a lower risk, hence its share prices are higher than others (Gabrilia et al., 2022). As the most actively traded shares, companies listed in the LQ-45 index have a good financial performance. They have complete financial report and reported in a timely manner. Therefore, the LQ-45 index become the signal of good quality of financial report (Lestari, 2015).

Investors and creditors, as the capital providers, become the most valuable users of financial statements (Mohammadi & Saeidi, 2022). Since their decision could affects the capital proportion, companies tried to provide the accounting information more relevance and reliable. The relevant accounting information is defined as accounting information that can be used by the users and meet what they need (Kaawaase et al., 2021a). The users are investors, debt holders, and the other users. However, measuring the quality of accounting information directly is quite difficult, because of the characteristics of information itself (Kaawaase et al., 2021a). Some researchers, therefore, focuses on observable indicators to measure financial reporting quality (Atwood et al., 2011; Noury et al., 2020).

The quality of accounting information can increase the accuracy of decision making for market participants. The company's ability to provide information about their business conditions is a form of company responsibility in managing the limited resources they have. Therefore, the confidence of investors and potential investors will increase, and have an impact on increasing investment opportunities in the company (Ghayoumi et al., 2011). Information on earnings also shows the level of company profitability which becomes an important indicator for investors before making investment decisions (Yang & Pangastuti, 2016).

The Advance investors, who concerns on long-term profitability, are not only focuses on the solely accounting earnings information, but also on the sustainability aspects (Rezaee et al., 2020). Earnings are no longer the main indicators to assess the business sustainability. Corporate social responsibility is a form of company's responsibility to protects the shareholders wealth, which becomes the primary concern of investors. In the stakeholder theory perspectives, the corporate responsibility to fulfill their social responsibility is a form of maintaining its business activities, because its existence is already accepted in society (Rezaee & Tuo, 2017). Most researchers have investigated the relationship between sustainability performance and financial performance (Baboukardos & Rimmel, 2016; Chauhan & Kumar, 2018; Y. Qiu et al., 2016). Companies with good social performance will have an impact on financial performance which can be seen from the increase in the company's stock price (Zuraida et al., 2016). This is because of the community legitimacy that is obtained by the company (Y. Qiu et al., 2016), can enhance the level of investor's trust (Rezaee & Tuo, 2017), that will drive the increase of stock prices (Baboukardos, 2018).

The assessment of firm's financial performances cannot be conducted separately using the only financial performance indicators. Investors tend to assess the company's potential in the long term rather than short-term earnings measures. The company's ability to continuously maintain its business activities and provide continuous profits is a more attractive aspect for investors than historical accounting profits only. (Bernardi & Stark, 2018). On the other hand, financial performances information does not mean become not important. The relevant and reliable financial information remains a consideration for investors in assessing the potential and the growth of a company (Kaawaase et al., 2021a).

Research on the effect of financial performances on firm value is conducted by (ElBannan & Farooq, 2019a) The research investigated how relevant earnings information is in influencing stock liquidity. The results showed that there was a positive influence between stock liquidity and earnings information. (Noury et al., 2020) conducted research on the value relevant of cash flows as decision making basis. The results show that cash flow information provides predictive value that is more accurate than profit because of the ability of cash flow information to detect future declines in the company's financial condition. The ability of cash flow to predict the condition of a company's financial difficulties is an important indicator for investors before making investment decisions. The accuracy of cash flow information also shows a predictive value indicator which is one of the qualitative characteristics of accounting information.

On the other hand, sustainability information becomes as important as accounting information in the investment valuation process (Dhaliwal et al., 2012; Y. Qiu et al., 2016; Semenova et al., 2010). Sustainability aspect is an important indicator to ensure that company can maintain its activities for long-time. Sustainability performance It is also an indication that the company is committed to continuously protecting shareholder value from time to time. An aspect of sustainability is the existence of social responsibility (CSR) activities. CSR is a form of company's consequence that they are socially responsible for the community, and have an obligation to protect the interests of its stakeholders (Y. Qiu et al., 2016).

Researches on the relationship between CSR performance and firm value has been explored extensively. Rezaee et al.(2020) focuses on the influence of CSR and earning quality. This research conducted within public Chinese listed firms during 2009 to 2015. The research indicated that firms those with higher level of CSR performance were tend to be had the better earnings quality than those with lower CSR performance. The earnings quality was observed through accrual-based earnings management as the measurement proxy. (Rezaee et al., 2020) was supported by the research of (Kareem AL Ani, 2021a), which focuses on the link between CSR disclosure on the financial reporting quality. This study is also use accrual quality, as the same proxy to measure the quality of financial reporting. The findings show that CSR disclosure have a positive impact on the accrual quality of financial reporting.

This study contributes to, and differ from the existence literature in several ways. Most of recent researches investigate the financial performance and CSR disclosure in separate ways (Atan et al., 2018; Kareem AL Ani, 2021a; S. (Charles) Qiu et al., 2021; Rezaee et al., 2020). CSR disclosure is mostly measured by the existence of the standalone sustainability or CSR reporting. CSR disclosure could not be an assurance that companies have the good quality of CSR performance. Disclosing CSR activity is the means to prove as a good firm without focusing on the quality of the performance itself (Rezaee et al., 2020). This research is focus on the measurement of CSR performance with the use of CSR spending as a proxy, which becomes more reliable indicator. CSR spending is the cost incurred to engage CSR activities. As stated by (Y. Qiu et al., 2014) companies with better CSR performance are more likely to have a higher level of CSR costs than those have the lower performance. By using CSR spending as the measurement of CSR performance, this research contributes to the new development of CSR performance measurement. This study also examines the effect of both financial and non-financial aspects on the firm values simultaneously in order to get the broader aspects on what factors that can affect firm values. Moreover, this study implies practically to provide empirical evidence on what factors that should be incorporated in the investments decision making process. Since the use of share price as a measurement of firm values, this study provides the more reliable and informative information for investors in enhancing the quality of decision making process (ElBannan & Farooq, 2019b).

Firm is a business entity in the society that have responsibility to obey the rule and social contract within society (Atan et al., 2018). Stakeholders have a perception that firms tend to be socially responsible. Firms also have to proof that their activities have obeyed the social norms within society (Fatemi et al., 2018), therefore, they can be legitimate. Firms which have been legitimate have the right to access all the resources, such as legal right, capital, employees, and soon (Y. Qiu et al., 2014). That is why, companies need to perform CSR as much as they can to gain legitimation within society.

Prior researches have investigated the sustainability aspects of the firms. Getting the short-term financial profit is no longer becomes the concern of investors. The priority of investors had been changed since short-term earnings can only provide a temporary profit. The sustainability aspects include green investments (Y. Qiu et al., 2014), social welfare and responsibility (Semenova et al., 2010), and also good corporate governance (Ibrahim & Hanefah, 2016). According to (Rezaee & Tuo, 2019), firms with good environmental performers will have better reputation than those have the worse one.

Information is the important aspect for users, especially shareholders in order to make business decision. Shareholders need the relevant information to assess the business widely and comprehensively (Y. Qiu et al., 2014). In the process of reporting information, the risks of gap between principal and agents might occur (Shaikh & Colarelli O'Connor, 2020). Agents often behave opportunistically and selfishly in order to gain financial incentives to themselves. The presence of agency problems within organizations leads to the decrease of information quality (Shaikh & Colarelli O'Connor, 2020). This is because agents might disclose incompletely the main information to shareholders.

In line with legitimacy theory, firms have responsibility to protect the shareholder value, by ensuring that all the business activities have been conducted properly. Companies with the superior performances are likely to disclose information that is relevant and reliable to all shareholders (Noury et al., 2020). Hence, the agency problems, which might harm the quality of accounting information can be minimized (Rezaee & Tuo, 2017). Since the sustainability performances become the main goal of business, companies tend to pay attention on the quality of information, both financial and non-financial information. In order to get legitimation, companies try hard to reduce the information asymmetry caused by the agency problems (Shaikh & Colarelli O'Connor, 2020).

Financial statements, which have an essential function in decision making process, must be clear and comprehensive reported. Financial statements contain business information that is captured by the standard accounting records. The ability of firms to capture and record economical events within organization, can increase the usability of the information (Kareem AL Ani, 2021b).

Disclosing information is a crucial process for companies because the unequal interest between a user to another. Companies need to ensure that accounting information had been fully disclosed along with standard to increase the reliability (Burnett, 2020). The quality of accounting information reflects the commitment of firms to disclose comprehensively as the need of stakeholders (Shaikh & Colarelli O'Connor, 2020). The qualitative characteristics, as in the standard accounting framework, are completeness, comparability, verifiability and understandability (Burnett, 2020). The quality of accounting information can increase the level of trust of investors (Iwatsubo & Watkins, 2021). Investors will put their trust on the firms that provides useful information disclosure because they can meet their expectation through the easiness to obtain information (S. (Charles) Qiu et al., 2021).

Most studies have investigated the relationship between accounting information on firm value (Rezaee et al., 2020) (Iwatsubo & Watkins, 2021). Research conducted by (Burnett, 2020) focused on the association between financial statements and corporate values. The findings showed that the equity value represents the financial statements information, even though that was not publicly disclosed (Burnett, 2020).

Since the sustainability of business activities becomes the main goal of the firms, companies tend more careful in the process of disclosing accounting information. In order to gain legitimation, companies also try to reduce the agency problems within organization, through the fully-disclosed accounting information. The quality of financial reporting can reduce the information asymmetry within organization, thus it can enhance the stakeholder's level of trust (Kaawaase et al., 2021b). Companies which focus on the quality of accounting information will have a good reputation (Rezaee et al., 2020), because they have been legitimated within society. Therefore, companies will receive premium on the stock prices, as the reflection of investors' trust to the companies. The higher the quality of accounting information, the higher firm value that is reflected on the share prices. From the given reason, the first hypothesis is written as follows:

H_1: Financial reporting quality have a positive impact on the share prices.

Sustainability performance is a broader aspect which includes environmental, social, and business continuity. Non-financial performance becomes more important than short-term financial performance because the paradigm has been changed from profit oriented to sustainability oriented (Rezaee & Tuo, 2019). Corporate social responsibility (CSR) is the representation of companies commitment to fulfill their obligation under the social contract (Rezaee et al., 2020). Companies which can prove that their business activities has obeyed the social rule, will benefit the social legitimation and become granted among society (Y. Qiu et al., 2016). Therefore, disclosing CSR activity is the form of company's commitment to gain legitimation.

CSR disclosure include all the environmental and social activities that are carried out by the companies. Several research on the effect of CSR disclosure on the firm performances has become the interest thing for most researchers (Kaawaase et al., 2021b; Y. Qiu et al., 2016; Rezaee et al., 2020; Rezaee & Tuo, 2019). A research conducted by (Purbawangsa et al., 2020) examined the effect of CSR performance on the corporate value. The findings show that CSR performance have a positive impact on the corporate value. CSR disclosure also plays important role in enhancing the relationship between corporate governance and corporate value. It can be inferred that, CSR disclosure can increase the firm performance through a good corporate governance, because company have an interest to gain legitimation (Purbawangsa et al., 2020). The quality of CSR disclosure represents the commitment of companies to contribute in the social responsibility within society. CSR disclosure also can reduce the information asymmetry within companies, because both financial and non-financial aspects are disclosed comprehensively. Company which a superior performance in CSR tends to have a higher firm value than those have the lower CSR performance. The more CSR information is disclosed, the higher investor's trust, that can be reflected on the stock prices. Therefore, the second hypothesis is written as follows:

$H_{2:}$ CSR performance have a positive impact on the share prices

METHOD

The population of this study is Indonesian public listed companies in the Indonesian Stock Exchange (IDX). The sample is companies which is listed in the LQ-45 index. The LQ-45 is an index for companies which have some criteria, such as have been listed at least for three months have high volume of stock transaction, have high capitalization within 12 past months, and companies also must be in a good financial condition. Since the advance criteria of the LQ-45 index, companies which are listed in the index must have a good financial statement. Therefore, we choose the LQ-45 as our sample.

Sample is taken using purposive sample technique. The criteria that we used is based on the data availability. Thus, companies which do not disclose CSR will not be selected as sample. We observe the 2019 and 2020 observations.

Financial report quality has the broad measurement indicators. Since the quality of financial report is quite difficult to be measured directly, most scholars developed models to observe it (Kaawaase et al., 2021a) (Rezaee & Tuo, 2019). This study use the model from (Lari Dashtbayaz et al., 2019). The measurement model that is used to define the financial report quality is earning management model. Earning quality can be assess from the low level of earning management. Earning management can be observed through the level of total Accrual (TAC). Total accrual is defined as the number of net operating profit minus by net operating cash flow, divided by initial assets (Lari Dashtbayaz et al., 2019). Financial report quality is measured by the absolute value of residual value from TAC (Rezaee & Tuo, 2019). The discretionary earning quality measurement uses correlation which scores 1 means the maximum quality while 0 is the worst quality of financial report (Rezaee & Tuo, 2019).

CSR performance is defined as the activity that carried out by the companies in order to perform social responsibility (Rezaee et al., 2020) CSR performance and CSR disclosure are associated. CSR disclosure is the tool to proof CSR performance and differentiate to another firms (Rezaee et al., 2020). There were so many indicators to measure CSR performance in the literature. CSR performance is measured by natural logarithm of CSR spending that is disclosed in the sustainability reporting. CSR spending is defined as the amount of CSR expense during a year. CSR spending data indicate the commitment of firms to engage CSR activities.

Share price, which become the dependent variable, is measured by closing price as of 31th December. Firm size as a control variable is also used in this study. Control variable is applied to control the other effect from variable which not be focus on the study. The Bigger company might disclose information more complete than those the smaller one. Bigger company also engaged in CSR activity better than the smaller company. Hence, firm size is applied as control variable. Firm size is measured by the natural logarithm of total assets.

To investigate the research hypotheses, we use ordinary least square (OLS) regression. First, to get the residual value of total accrual which is the proxy of financial report quality, a regression is applied to total accrual and operating activities. The OLS equation is defined as follows:

TACit $\left(\frac{NOPit-NOCit}{ASit-1}\right) = \alpha + \beta 1 \left[\frac{1}{ASi,(t-1)}\right] + \beta 2 \left[\frac{\Delta R-\Delta S}{ASi,(t-1)}\right] + \beta 3 \left[\frac{PPEit}{ASi,(t-1)}\right] + \beta 4\, ROAit + \varepsilon it$............................... (1)

$SP_{it} = \alpha + \beta 1\ FRQ_{it} + \beta 2\ CSR_{it} + \varepsilon_{it}$ .... (2)

Where:

TACit : Total Accrual of company i year t-1

NOPit : Nett operating profit company i year t

NOCit : Nett operating cash flow company i year t

α : Constanta

β : regression coefficients

AS_{it-1} : initial total assets

ΔR : change in account receivable

ΔS : change in year sales

PPEit : plant, property, and equipment company *i* year *t*

ROAit : return on asset firm *i* year *t*

SPit : share price firm i year t

FRQit : financial report quality firm i year t

CSR_{it} : CSR performance firm i year t

εit : other factors outside the model

The research framework is presented in figure 1.

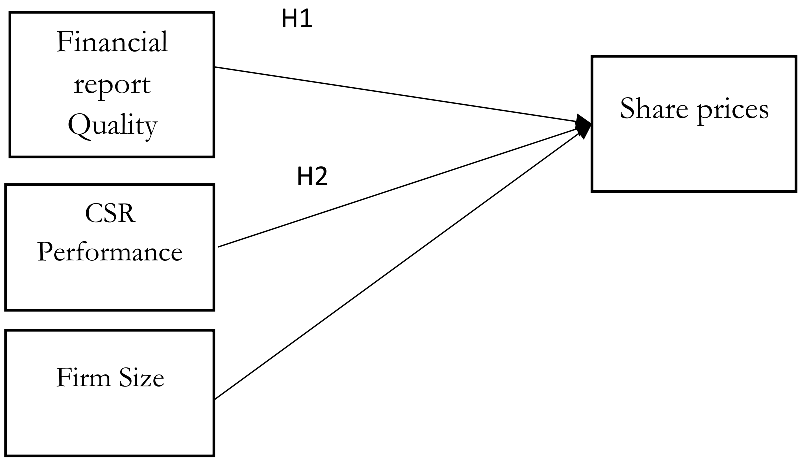

Figure 1. Research Framework

RESULTS AND DISCUSSION

Table 1. Sample Distribution

Number of Sample	2019	2020	Total
LQ-45 public listed companies	45	45	90
Bank and finance companies	(6)	(6)	(12)
Final Sample	39	39	78

Source: Primary Data, 2023

Table 2. Descriptive Statistics

Variables	*Min*	*Max*	Mean	Std. Dev
Financial Reporting Quality	0.12	0.92	0.39	0.16
CSR performance	19.28	28.01	25.05	1.91
Share prices	338	134.277	13.520	24.984
Firm Size	0.40	3.81	3.65	0.38

Source: Primary Data, 2023

Table 3. Regression Result Test

Variables	KS	DW	Coef	Sig	Adj R-Sq	F	F sig
Financial Reporting Quality			-0.12	0.12			
CSR performance	0.20	1.04	0.02	0.00*	0.137	5.08	0,00*
Share prices							
Firm Size			-0.01	0.69			

Note: Tol = Tolerance, H = Heteroscedasticity, KS = Kolmogorov-Smirnov, DW = Durbin-Watson Coef = Beta Coefficients
*Significant at 0.05 level
Dependent variable: Share prices

Source: Primary Data, 2023

There were 45 companies which is listed in the LQ-45 index. Six companies were excluded from the observation data because it belongs to bank and finance industries. Bank and finance companies have different indicators in financial ratios measurement. thus, the final sample was 39 companies, that resulting 78 firms-years observation during 2019 to 2020. Table 1 shows the sample distribution data.

Table 2 represents the descriptive statistics. The mean value of financial reporting quality is 0.39 and its standard deviation is 0,16. The average of CSR performance is 25, while the maximum score is 28. It indicates that firm's CSR performance is considered as high performance. Since the CSR disclosure become mandatory in Indonesia, many companies paid attention on the CSR activity.

The average of share price is IDR 13.520 while the standard deviation is IDR 24.984. It means that data have distributed in variety ways. The average of firm size is 3.65, and the minimum and the maximum size is 0.40 and 3.81 respectively.

The regression result test is presented in the table 3. Before the regression test is run, the classical assumption test is applied to get the best model. As shown in table 3, the model had fulfilled all the classical assumption tests. It means that the model can be used as OLS model.

Hypothesis 1 states that there is a positive effect of financial report quality on the share prices. The hypothesis's result test is 0,12, which has p value > 0,05. Thus, hypothesis 1 cannot be supported by empirical evidence. There is no effect of financial report quality on share price. Accounting information is a historical information that is reported after the economic events happened. Since the process of information recording need time to be publicly disclosed, accounting information will lost its relevance to users (Baboukardos & Rimmel, 2016). According to (Baboukardos & Rimmel, 2016) shareholders have predicted firm's financial condition before it publicly disclosed, in order to reduce future risks. It becomes the reason that accounting information had been reflected in the prior share prices (Baboukardos & Rimmel, 2016).

Hypothesis 2 predicts the positive effect of CSR performance on the share prices. The hypothesis is supported by empirical evidence which has significance level below 0,05 (P value 0,00 < 0,05). Thus, CSR performance have a positive impact on the share prices. According to (Rezaee et al., 2020), CSR performance is a form of marketization to differentiate the superior CSR performers and those the poorer one. Thus, CSR performance can mitigate the future firm risks and help to enhance the firm value (Rezaee et al., 2020). In the frame of legitimacy theory, firms with a high CSR performance can achieve long-term and stable financial healthy, because firms had been legitimate within society (Rezaee et al., 2020). Thus, they can get the social benefits. This finding supports the work of (S. (Charles) Qiu et al., 2021). They found that CSR performance can help to protect firm value, even during crisis conditions. CSR performance is a form of investment to protect communities. The community-engaged activities will benefit firms with social incentives. Thus, CSR performance have a strong effect on the firm value, which is reflected on the increase of stock prices (S. (Charles) Qiu et al., 2021).

CONCLUSION

This research investigates whether accounting information and CSR performance, which a part of business sustainability, have an impact on the firm value. We observed 78 firms-years observation of public listed companies in Indonesia during 2019 to 2020. The empirical evidence proves that accounting information have no impact on the share prices. On the other hand, CSR performance influence the firms stock prices positively. These findings also prove that accounting information have less important role in reducing information asymmetry within companies. Moreover, CSR performance is highly valued by investors, which is reflected on the increasing stock prices.

This study contributes to the development of the usefulness financial and non-financial information based on the framework of legitimation and agency theory. The use of both theories provides a broader insight in assessing the effect of financial and non-financial information. This research contributes to business practitioners, especially on how to assess the company's sustainability aspects and its relevance on the firm values. However, this study also has several limitations. First, since the accounting information is historical information, the use of accrual-based indicators might lead to the absence of its effect on stocks prices. The market-based approach might become an interesting topic in the future research. Second, there are several factors that influence the CSR performance which is not investigated yet, such as the quality of CSR disclosure (Rezaee et al., 2020) and the role of corporate governance (Purbawangsa et al., 2020). This is also become the next research areas that can be investigated sophisticatedly.

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