

Corporate Social Performance of Indonesian State-Owned and Private Companies

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ABSTRACT

The objectives of this study are to analyze the difference of corporate social performance between State-owned and private companies in Indonesia, and also to analyze the correlation between the corporate social performance (CSP) and the corporate financial performance by using company size, and institutional ownership as control variables. The population of this study is Indonesian state owned and private companies in the year of 2001-2004. Purposive sampling was used in this study, and final samples are 461 companies.

The CSP or CSR (Corporate social responsibility) score is measured by content analysis of corporate annual report using seven item developed by Michael Research Jantzi Research Associate, Inc. The data is tested by independent t-test to determine the mean difference and by using partial correlation test to know the correlation between the corporate social performance and financial performance.

The results of this study are that there is no significant difference mean of corporate social performance between state-owned and private owned companies in Indonesia. In addition, the correlation test indicates that there is no association between corporation social performance and financial performance both in SOCs and POCs.

Introduction

Baron (2000) defines altruism as action of people or group to voluntarily help somebody else regardless of the motives of the action or vested interest. A company has a role and responsibility to its environment and stakeholders. The stakeholder model states that the success of a company depends on its ability to maintain a good relationship with stockholders in its decision-making



(Ullman, 1984). If a company fails to do so, it faces problems raised by the constituents of stakeholder). Coffrey and Wang (1998) use the term corporate altruism to call the action of pro-social behavior conducted by business entity. During the last three decades, corporate altruism has received significant attention. Some studies describe that pro-social behavior is about how a company behaves in different countries. Moir (2001) contended that the hope for a company to be more responsible for its community and environment became debatable recently. Morimoto et al., (2004) emphasized the increasing pressures on companies to be more socially responsible. Several studies have been conducted on corporate social performance in the context of developed countries (e.g., see, Wardock and Grave, 1997; Preston and O'Bannon, 1997; Mahoney and Roberts, 2007); however, similar studies in developing countries setting are rare. The indexes for corporate social performance, as provided by Kinder Lydenberg Domini (2008) and also Jantzi Research Incorporated (2008) in developing countries are not available yet. Indonesia is no exception. Therefore, this research attempts to focus on Indonesian state-owned companies (SOCs) and private companies (POCs).

According to Republic of Indonesia (Law No. 19) (2003) on state-owned company, companies in Indonesia can be classified into state-owned company (SOCs), private-owned company (POCs), and companies under cooperative scheme (COCs). In SOCs, all stakes come from separated state asset, and are the economic actors contributing to Indonesian economic system. In operationalizing the business, SOCs, POCs, and COCs support each other based on democratic economy system (Republic of Indonesia, 2003). Currently, SOCs have served any sector of business line. Therefore, most of Indonesian people use the SOC's products and services. As stipulated in the law, the SOC's are ordered by the government (owner) to conduct public service offering (SOP) at the expenses of Government, especially for the products and

services not offered by POCs and COCs for economy viability. Thus, the issue is raised about the role of stakeholders including shareholder in affecting the Indonesian companies' policy to conduct corporate social responsibility, and how the social responsibility is reported to stakeholders?

Since 1998, changes have occurred in SOCs in order to be more transparent and accountable. It has happened when Indonesian Government created the Ministry of State-Owned Companies. According to Abeng (1999), the strategy of restructuring, profitability, and privatization was needed to manage the SOCs well. Restructuring strategy was implemented by setting the holding of SOCs. Amongst 150 SOCs, the companies are classified into 10-12 holding. The objective of such setting is to place a business focus based on certain business goals. The concept of Abeng (1999) is to set the super holding SOC, with Republic of Indonesian President as Chairman, under which the giant holding of SOCs was operated. The giant holdings will be then the world-class economic actors indicated by Fortune 500 list as one of the indicators. The idea almost succeeded in 1999 when team restructuring batch II, supported by some world class consultants, McKinsey, Booz Allen and Hamilton, Price Waterhouse & Coopers, Andersen, Ernst & Young, and AT Kearney), completed a blue book for restructuring per industry sector (Nugroho and Siahaan, 2005). The Indonesian government had the concepts of restructuring and privatizing SOCs to make them the world-class companies, and thus to be profitable.

In short, it can be said that some endeavors to improve the SOCs, blue print on SOCs reform had been set up in 1998-1999, and a master plan for SOCs had been developed during 2002-2006, and the law No. 19 (2003) had been approved by the lawmakers. The efforts to transform the SOCs toward modern and professional business institutional have been conducted by the government. It should be noted that Good Corporate Governance principles have been placed in

order to manage the SOCs well (Soedjais, 2005); that is, considering the required condition and given situation, the SOCs have a role (as corporate and good citizen) in taking corporate social responsibility. Therefore, it is interesting to observe empirically how social responsibility (which is often called social performance) is practiced in SOCs in comparisons with POCs as well as to analyze the relationship between corporate social performance and financial performance. This study has been focused on POCs to be compared to SOCs due to the same legal system as and the similarity of business nature to the SOCs. Differentiating factor between them is ownership only. COCs have different legal system from SOCs and POCs. The legal system for SOCs and POCs is Corporation (called “Perseroan” in Indonesian term), while COCs, as stipulated in the Indonesian cooperative law (Republic of Indonesia, 1992), must use the cooperative legal system (called “Koperasi” in Indonesian term). Thus, the objectives of this chapter are to discover difference of corporate social performance in state-owned and private companies, and correlation between corporate social performance and financial performance in SOCs and POCs

Corporate Social Performance

Concept of corporate social performance (CSP), in which environmental aspect is included, is synonymous with corporate social responsibility (CSR) and socially responsible behavior. They are used interchangeably in empirical research. Sometimes, concept of CSP is subsumed under the umbrella of CSR, and sometimes the reverse (Wood, 1991; Carroll, 1979, 1999; Barnett, 2007). Generally the term social and environment are covered in the concept of CSP including the aspect of environment in measurement construct. However, due to the growing importance of environmental issue, there was a need to separate the performance of environment from the

social performance. However, the concept of performance measurement focuses on three Ps: profit (financial), people (social), and planet (environment).

So far there have been four main models in understanding CSR construct: Carroll's (1979), Wartick and Cochran's (1985), Wood's (1991), and Clarkson (1995). Carroll defined CSR as the intersection at a given moment in time of three dimensions: Corporate Social Responsibility (CSR) principles should be apprehended at four separate levels (economic, legal, ethical and discretionary); the sum of the social problems that a firm faces (i.e., racial discrimination, etc.); and, the philosophy underlying its responses, which can range anywhere along a continuum going from the firm's anticipation of such problems to the outright denial. Wartick and Cochran (1985) adjusted this model, re-sculpting its final dimension by borrowing from the strategic management of social issues.

Wood (1991) proposed a renewed CSP model that soon became an omnipresent yardstick in the construct's theoretical development (Gerde and Wokutch, 1998). In line with earlier studies, the authors define CSP as a business organization's configuration of the principles of social responsibility, processes of social responsiveness, and policies, programs, and observable outcomes as they relate to the firm's societal relationship (Igalens and Gond, 2005). The second orientation was based on a more pragmatic observation of how hard it is to apprehend CSP using the preceding typologies, and applying Stakeholder Theory as a framework to model CSP, which would then be defined as a firm's ability to manage its stakeholders in a way that is satisfactory to them (Clarkson, 1995). Igalens and Gond (2005) summarize CSR models in Table 1.

Table1: Models of CSP

Authors	Definition of CSP	CSP Dimensions
Carroll (1979)	The articulation and interaction between (a) different categories of social responsibilities; (b) specific issues relating to such responsibilities; and (c) the philosophies of the answers	Definition of Corporate Social Responsibility Levels: economic, legal, ethical, discretionary Philosophy of Responsiveness Stances: responsive, defensive, accommodative, proactive Social Issues involved Examples: Consumerism; Environment; Discrimination; Product safety; Safety at work; Shareholding
Wartick and Cochran (1985)	“The underlying interaction among the principles of social responsibility, the process of social responsiveness and the policies developed to address social issues” (p.758)	Corporate Social Responsibilities Levels: economic, legal, ethical, discretionary Corporate Social Responsiveness Stances: responsive, defensive, accommodative, proactive Social Issues Management Approach: Identification; Analysis; Response
Wood (1991)	“A Business organization’s configuration of principles of social responsibility, processes of social responsiveness, and policies, programs, and observable outcomes as they relate to the firm’s societal relationship”(p.693)	Principles of Corporate Social Responsibility Levels: Institutional, Organizational and Individual Processes of Corporate Social Responsiveness Includes: Environmental Assessment and Analysis; Stakeholder Managements; Issues Management Outcomes of Corporate Behavior Combines: Societal Impacts; Corporate Social Programs and Policies
Clarkson (1995)	The ability to manage and satisfy the different corporate stakeholders	This model identifies specific problems for each of the main stakeholder categories it distinguishes: Employees; Owners/Shareholders; Consumers; Suppliers; State; Stakeholders;

		Competitors
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Approach to Measuring CSP

There have been five approaches to measuring Corporate social performance: (1) Measurement based on analysis of the contents of annual reports, (2) Pollution indices, (3) Perceptual measurements derived from questionnaire-based surveys, (4) Corporate Reputation indicators, and (5) Data produced by measurement organizations (Igalens and Gond, 2005). In the first approach, CSR is measured using content of corporate annual report. This method of measuring CSR is focused on the disclosure in the annual report. According to the second approach, measurement of CSR is focused on one dimensions of CSR (i.e., environment.) This method generally is concerned with external party. Corporate Reputation indicator is an approach to measuring CSR using reputation indicators as perceived by external parties of company. Data produced by measurement organizations is a result of measurement approach of CSP conducted by external agency using multidimensional measurement. Igalen and Gond (2005) summarize the approaches in Table 2.

Table 2: Approach to Measuring CSP

Type of measurement	Suitability in terms of the SP concept	Characteristics / problems	Mode of production
Contents of annual reports	A measurement that is more symbolic than	Subjective measurement	By the company

	substantive (discourse) and which contains no reference to the construct's varying dimensions	/that can be easily manipulated	
Pollution indicators	Measures just one of the construct's dimensions (its environmental aspects)	A measurement that is objective but which does not apply to all firms	By an entity that is external to the company
Questionnaire based surveys	Depends on what measurements have been suggested. Can be a very good fit with the concept but actors' perceptions remain a priority in such measurements	Perceptual measurement that can be manipulated depending on how it is administered	By a researcher who uses a questionnaire to gather info directly from the company
Corporate Reputation indicators	Overlapped with Corporate Reputation. Enables a measurement of overall CSP but is still relatively	Perceptual measurement. Halo effects	By an entity that is external to the company

	ambiguous		
Data produced by 'measurement entities'	Multidimensional measurement, with the extent of a theoretical model's "fit" depending on the operational modes and benchmarks that agencies are using	Depends on the agencies' operational mode. Halo effects	By an entity that is external to the company

The approach to CSP measurement classified by Igalen and Gond (2005) is not so clear as an approach strategy to measuring as they merely indicate source of data (as in content of annual report and questionnaire as well as in other classifications). In the context of the approach to CSP measurement, one will expect to have clear idea on some approaches to measuring CSP. To resolve complication of the classification of the approach to CSP measurement four types of measurement strategy proposed by Orliczky (2003) can be used. They are: (1) disclosure, (2) reputation rating, (3) social audit; CSP process; and observable outcome, and (4) managerial CSP principle and value. The disclosure approach uses content analysis method of documented materials such as annual report. The objective of this approach is to find certain attributes contained in the documents that are considered to reflect a company's socially responsible behavior. This approach has been used by the previous studies (see for example Andersson and Frankie, 1980; Fredman and Jaggi, 1981 and 1986). The reputation rating approach to measuring CSP is based on the company's perception of one of the stakeholders using single or multi-dimensions of CSP. In this case, it is assumed that the perceived items represent a good

reputation of the company. Previous studies using this approach are many (Cochran and Wood, 1984; Spencer and Taylor, 1987; 1987; McGuire et al., 1988; Simerly, 1995; Sharfman, 1996; Belkaoui, 1997; and Turban and Greening, 1997). The next category of measurement method for CSP is social audit, CSP process, and observable outcome. This is a systematic process in which the third party assesses a company's behavior of CSP, normally using multi dimension measures to have a ranked index of CSP. The third party includes KLD (Kinder Lydenberg Domini) and CEP (Council on Economic Priorities). This approach has been used previously (Wartick, 1988; Turban and Greening, 1997; and Russo and Fouts, 1997). Their approach of measuring CSP is using managerial CSP principle and value. Under this approach, survey has been carried out to assess a company's activities using values and principles of CSR developed initially by Carroll (1979) and extended by Aupple (1984). The values and principles of CSR include four dimensions: economy, legal, ethics, and discretionary. The previous studies adopting this approach include Ingram and Frazier (1980); Aupple et al (1985); Freeman and Jaggi (1986); Cowen (1987); O'Neal et al. (1989); and Hansen and Wemerfelt, (1989). Cochran and Wood (1984) contended that there are two generally accepted methods to measure CSP: content analysis, and reputation index. Based on their argument, the last three classifications of Orlitzky et al. (2003) fall in the reputation index method. In line with Cochran and Wood (1984), Margolis et al (2001 and 2003) use other term for the two generally accepted methods: (i) subjective and (ii) behavior indicators. Subjective indicators refer to reputation index method of Cochran and Wood (1984) and the last three classifications of Orlitzky et al. (2003), while the behavior indicators represent content analysis method of Cochran and Wood (1984) and disclosure strategy of Orlitzky et al. (2003). Furthermore, some measures for CSP have been also developed based on single or multidimensional measurement. The approaches include eight

attributes of reputation (often called fortune measure); five aspects focusing on key stakeholders and three pressure variables (often called KLD measure); quantitative measure of environmental aspect (often called TRI measure); quantitative aspect of company philanthropy (often called Corporate philanthropy measure); and, return of six social measure on customer, employee, community, environment, minority, and non US stakeholder (often called best corporate citizen). For some approaches, it may be possible to use similar measurement but with different judgment or evaluation, the overall CSR measurement may result in different perspective. Itkonen (2003) summarizes different perspective of CSR in Table 3.

Table 3: Types of Corporate Social Performance Measure

Measure	Dimensions	Judge	Source
Fortune	Eight attributes of reputation	Financial analyst, senior executives and outside managers	Griffin and Mahon (1997)
KLD	Five attributes of CSR on focusing on key stakeholder relation, there on topics with which companies have recently experienced external pressures	External audiences	Waddock and Grave (1997)
TRI	Qualitative measure of companies' environmental	No external judge needed,	Griffin and Mahon (1997)

	discharge to water, air and landfill, and disposal of hazardous waste	companies themselves give the data	
Corporate Philanthropy	Quantitative measure of companies philanthropy, how much	No external judge needed, companies themselves give the data	Griffin and Mahon (1997)
Best Corporate Citizen	Three-year average shareholder return and six social measures: company's influence on customer, employee, community, environment, minorities, and non US stakeholders	Social investment research firm	Murphy (2002)

Mahoney and Roberts (2007) used the measures of social performance, developed by Michael Jantzi Research Associate, Inc. (long partner with KLD), in their study on social and environment performance and their relation to financial and institutional ownership, and included the following variables: community and society, corporate governance, customer, employee, environment, human rights, controversies business activities. Their modified measures of social performance are presented in Table 4.

Table 4: Dimensions of CSP

Dimension	Indicator	Micro level Indicator
Community and society	<ul style="list-style-type: none"> -Public reporting -Charitable donation program -Community relation -Aboriginal relation -Impact on society 	<ul style="list-style-type: none"> -Policy statement on community donation - Cash donations as a percentage of pre-tax profit - Policy statement on engagement/consultation - Benefit sharing agreement with local communities -Policy statement on aboriginal relation - Policy statement on bribery and corruption - Impact/initiatives related to marginalized groups
Corporate governance	<ul style="list-style-type: none"> -Management Systems - Governance data 	<ul style="list-style-type: none"> -Statement of social responsibility principles or values -Code of business conduct -Board independence -Separate chairman and chief executive officer -Share structure -Shareholder proposals
Customer	<ul style="list-style-type: none"> -Management system 	<ul style="list-style-type: none"> -Policy statement on safety of product/service

	-Impact on customer	-Policy statement on the treatment of customers -systems/programs to ensure product safety or fair treatment of customers
Employee	-Employee data -Reporting -Employee program and benefit -Diversity -Health and safety -Union relation -other data employee	-Total number of employee -Employee turnover -Public reporting on employee issues -education and development -ownership program -Policy on employee diversity -public reporting on diversity issues -Policy on occupational health and safety -Employee wellness programs -Description of relations -No. of strikes/lockouts in the last five years -Employee controversies
Environment	-Exposure to Environmental Issues -Management Systems -Public Reporting -Impact and Initiatives -Regulatory Compliance	-Potential environmental impacts -Formal Environmental Management System -Environmental policy -Systems to measure and monitor environmental performance -Audits - Life -cycle analysis

	-Other Environmental Data	- The company's environmental reporting -Resource use - Pollution control -Environmental penalties over the last five years -Environmental liabilities -Total environmental expenditures
Human rights	-Exposure to Human Rights Issues -Management Systems -Impact and Initiatives	-Exposure related to countries in which the company operates -Human rights policy/code of conduct -Systems/programs to manage human rights issues -Community engagement -Implication in the abuse of human rights
Controversies Business Activities	-Alcohol -Gambling -Genetic Engineering -Tobacco -Use of animal	-Level of involvement (% of annual revenues) -Nature of involvement

Corporate Financial Performance¹

¹ This section is based on the section of Fauzi (2004), Fauzi et al. (2007), and Fauzi (2008). They have been modified to greater extent for the purpose of the section of this chapter.

Basically it is also the responsibility of management to improve the financial performance. Component of stakeholder like investor, creditor, and labor are very concerned about the performance. The higher financial performance leads to the increase in wealth of the stakeholders. In addition, based on the slack resource theory (Waddock and Graves in Dean, 1999), improving financial performance make the companies has more opportunities to improve social performance in all aspects.

There are many measures used to represent the financial performance. They include three categories: ROA and ROE (Waddock and Graves, 1997; Mahoney and Roberts, 2002), profitability in absolute term (Stanwick and Stanwick, 1987), and multiple accounting based measure with the overall index using the score of 0 –10 (Moore, 2001). Using score of 0-10 to have overall index of financial performance raises a problem of objectivity of scoring process and of validity of the end result of index.

Corporate financial performance (CFP) can also be measured using three alternative approaches: (1) market based measure, (2) accounting-based measure, and (3) perceptual measure (Orlitzky et al, 2003). Under the first approach, the market value of a company derived from stock price of the company is used to measure CFP. This approach reflects notion that primary stakeholder of the company is shareholder. Some researchers using this approach include Cochran and Wood, 1984; Shane and Spicer, 1983; Preston, 1978; Vance, 1975; Simerly, 1994. Accounting-based measure is one to measure CFP derived from a company's competitive effectiveness and a competitive internal efficiency as well as optimal utilization of assets, for some certain measures. Measures such as net income, ROA, and ROE are some examples of this approach. This approach has been in previous studies by Simerly, 1994; Turban and Greening, 1997; Waddock and Grave, 1997; Russo and Fouts, 1997.

The last approach to measuring CFP is using perceptual method. In this approach, some subjective judgments for CFP will be provided by respondents using some perspectives such as ROA, ROE, and financial position relative to other companies. The previous studies using this approach include the ones of Reimann, 1975; Wartick, 1988.

The Relationship between CSP and CFP ²

relationship between CSP and CFP: direction and causality of the relationship (Preston and The importance of the relationship between CSP and CFP states that social responsibility is an important corporate duty. Given the importance of the CRS in corporate decision-making, the relationship between CSP and financial performance is an important topic (McGuire et al., 1988). In practice, social performance requires some costs that may reduce financial performance. As a result, the question arises, which should come first—social performance or financial performance. Justification to explain the importance is thus needed by management.

There are two important issues in the O'Bannon, 1997). The direction of the relationship refers to positive, negative or neutral. The positive direction of the relationship between CSP and CFP occurs when increase in CSP leads to the increases in CFP. The change in CSP leading to the change in CFP in different way is negative direction of the relationship. If a change in CSP does not affect the change in CFP, then neutral effect in the direction of the relationship occurs. The causality of the relationship denotes if CSP or CFP is independent or dependent variable. In this case, two possibilities exist: CSP as independent variable and CFP as independent variable. If CSP is an independent variable, it affects CFP. If CSP is a dependent variable, CFP affects CSP.

The positive link between CSP and CFP can be explained in three ways (Waddock and Grave, 1997). First, firms trying to lower its implicit cost by acting socially irresponsibly, its explicit cost will increase and, in turn, result in competitive disadvantage (decrease in profit). Second argument of Waddock and Graves (1997) is using the better management theory.

² This section is based on the section of Fauzi (2008b), paper entitled "The Determination of the Relationship between Corporate Social Performance and Corporate Social Performance" accepted for presentation in the AAA event in California, August 2008. It has been modified for the purpose of the section of this chapter.

According to this theory, socially responsible firms improve relationship with their stakeholders. The relationship improves competitive advantage and, in turn, increases financial performance. This argument is equivalent to the social impact and synergy hypothesis of Preston and O’Bannon (1997). The last argument used by Waddock and Graves (1997) for positive relationship is the slack resource theory. According to this theory, firm’s financial resource will determine activities in social responsibility, because given the resource, the firm has more chances to invest in socially responsible activities. This argument is comparable to the fund hypothesis of Preston and O’Bannon (1997).

Explanation of the negative CSP-CFP link is based on neoclassical economic theory which states that socially responsible firms’ costs are considered unnecessary, and thus can lead to a competitive disadvantage; that is, a decrease in companies’ profit and shareholder wealth (Preston and O’Bannon, 1997; Waddock and Garve, 1997). Neutral link between CSP and CFP exists as the relationship is by coincidence (Waddock and Grave, 1997). Argument for this link is that a company acting socially responsibly to customer can have different demand curve as compared to less responsible companies. Therefore, the activities are the only way to attain differentiation, and thus do not impact on company’s profit (McWilliam and Siegel, 2001). The relationships of CSP and CFP are summarized in Table 5.

Table 5: Positive, Negative, and Neutral Direction of the Relationship of CSP and CFP

Study	Sample	CSR Measure	Control Variables
Positive relationship			

Worrell, Davidson III and Sharma (1991)	Market's reactions to announcements of 194 layoffs studied		
Preston and O'Bannon (1997)	Multiple industries, 67 large U.S. corporations	Fortune	
Waddock and Graves (1997)	Multiple industries, 469 companies	KLD	Firm size, risk, industry
Frooman (1997)	Meta-analysis of 27 event studies		
Roman, Hayibor and Agle (1999)	Reconstruction the literature study of Griffin and Mahon (1997), 4 studies added		
Orlitzky (2001)	Meta-analysis of 20 studies		Firm size
Orlitzky and Benjamin (2001)	Meta-analysis on the relationship and risk		
Ruf et al. (2001)	Multiple industries 496 firms	KLD	Firm size, industry
Murphy (2002)	S&P 500	Best Corporate Citizens	
Simpson and Kohers (2002)	Banking industry, 385 banks	Community Reinvestment Act Rating	Industry
Neutral relationship			

Griffin and Mahon, (1997)	Chemical industry, 7 companies (includes also a wide literature study)	Fortune, KLD, TRI, philanthropy	Industry
McWilliams and Siegel (2000)	Multiple industries, 524 firms	KLD	Investment in R&D
McWilliams and Siegel (2001)	Theoretical study, outlining supply and demand model of CSR		
Moore (2001)	U.K. supermarket industry, 8 companies	16 measures of soc. performance and disclosure	Industry
Negative relationship			
Wright and Ferris (1997)	Multiple industries, 116 divestments	Divestments of South African businesses =CSR	

Conclusion can now be drawn from the previous findings on the relationship between CSP and CFP, which is not positive and the same under all conditions. The use of contingency perspective is needed to understand under which condition the relationship will be valid (Hedesström and Biel, 2008). That is why Fauzi (2008b) proposes a proposition on corporate performance explaining that the relationship between CSP and CFP can be contingent upon four variables: (1) business environment, (2) business strategy, (3) organization structure, and (4) control system.

Griffin and Mahon (1997) raised another issue of causality of the relationship between CSP and CFP. In an effort to meet the stakeholder's expectation, company should try to improve CSP from time to time in light of economic/financial condition. However, the question on the priority arises; that is, which one (CSP and financial performance) come first. Waddock and Graves (1997) and Dean (1999) put forward two theories to answer the question: Slack resource theory and good management theory. Under the slack resource theory, a company should have a good financial position to contribute to the corporate social performance. Conducting the social performance needs some fund resulting from the success of financial performance. According to this theory, financial performance comes first. Therefore, CFP is independent variable to affect CSP. A good management theory holds that social performance comes first. Based on the theory, CSP is an independent variable resulting in CFP. A company perceived by its stakeholders as having a good reputation will make the company easier to get a good financial position through market mechanism.

Hypotheses Development

1. The Difference of CSP between SOCs and POCs

Rudjito (2005) states that one of the problems resulting in SOCs to have inferior business performance in past was the drawback in the direction of SOCs' policy. Since the ministry of SOCs had been set up, the direction of the SOCs policy is clear and it became clearer when the Law No. 19, 2003 (Republic of Indonesia, 2003) has been passed. One of the functions of the Ministry of SOCs is to emphasize the role of the government as the owner of SOCs (different from the role of the government as the regulator). The Law No.19 (Republic of Indonesia, 2003) firmly differentiates the role of owner, regulator, supervisor, and operator. With the different

roles, political interventions in SOCs will be minimized. As a result, SOCs can work professionally based on the principles of good corporate governance. In addition, the increasing demand, resulting from global situation, for SOCs to be corporate citizen is the also the condition the SOCs are facing (Soedjais, 2005). Given the positive direction in managing SOCs, it is expected that the factors can encourage the SOCs to improve their performance in different dimensions; that is social, environment, and financial. Therefore, it is hypothesized that:

H1: There are no differences in social performance of SCOs and POCs.

2. The Relationship Between CSP and CFP³

Based on the literature review, the relationship between corporate social performance and corporate financial performance could be positive, negative, or neutral. But most of the result of studies indicated the positive relationship and very few provided the negative and neutral relationship (Worrell et al., 1991; Preston et al., 1997; Waddock et al., 1997; Frooman, 1997; Roman et al., 1999; Orlitzky, 2001; Orlitzky et al., 2001; Rufel et al., 2001; Murphy, 2001; Simpson et al., 2002; Griffin et al., 1997; McWilliam et al., 2000 and 2001; Moore, 2001).

Griffin & Mahon (1997) reviewed 51 studies discussing the relationship between CSP and CFP from the 1970's through the 1990's. The Griffin & Mahon's study (1997) mapped the issue of direction of the relationship between CSP and CFP for the periods. In the 1970s, there were 16 studies reviewed with 12 of which had positive relationship. During the period of the 1980s and 1990s, the positive direction of the relationship accounted for 14 of 27 studies and seven of the eight studies, respectively. Negative results were supported by only one study in the 1970s, 17

³ This subsection is based on the section of Fauzi et al. (2007). It has been modified for the purpose of the subsection of this chapter.

studies in the 1980s, and 3 studies in the 1990s. Inconclusive findings were found by four studies in the 1970s, five studies in the 1980s, and no finding in the 1990s. It should be noted that one or more studies could have one or more findings in the work of Griffin and Mahon (1997).

As the study of Griffin & Mahon (1997) was not all inclusive, there are additional studies contributing to the direction of the association between CSP and CFP relationship in the 1990s. During this period, positive direction of the relationship has been supported by Worrell et al. (1991), Preston & O'Bannon (1997), Waddock & Graves (1997), Frooman (1997), and Roman et al. (1999). Negative results are supported by Wright & Ferris (1997). Furthermore, in the 2000s, there are some researchers adding to the debate on the link between CSP and CFP with different perspectives of methodology. Positive results were supported by the works of Orlitzky (2001), Orlitzky & Benjamin (2001), Ruf et al. (2001), Konar & Cohen (2001), Murphy (2002), Simpson & Kohers (2002), Orlitzky et al. (2003), and Mahoney & Roberts (2007). Patten (2002) found a negative correlation. Researchers such as McWilliams & Siegel (2000 and 2001) and Moore (2001) found inconclusive results. Fauzi (2004) using content analysis of annual reports of companies listed on the New York Stock Exchange for the period of 2004 also provided support for inconclusive results

In a more recent work, Margolis & Walsh (2003) also mapped studies investigating the relationship between CSP and CFP. They followed the works of Griffin & Mahon (1997) but used a wider time period (1972 – 2002) resulting in analysis of 127 published studies. Of these studies, 70 studies (55%) reported having a positive relationship, seven studies suggested a negative relationship, 28 studies supported inconclusive results, and 24 studies found the relationship went in both directions. Gray (2006), in his review of studies investigating the relationship between CSP and CFP, argued that results are inconclusive. This argument is also supported by Murray et al. (2006) in their cross section data analysis. However, using a

longitudinal data analysis, they found evidence to the contrary. Hill et al. (2007) investigated the effect of corporate social responsibility on financial performance in terms of a market-based measure and found positive results in the long-term.

Given that discussion, it is expected to have concern that the relationship between corporate and financial performance is positive. Hence, it is proposed that:

H2: There is positive relationship between corporate social performance and financial performance.

There are other variables affecting corporate social performance such as company size and institutional ownership.

Company Size

According to Waddock and Graves (1997) and Itkonen (2003), company size is related to corporate social performance; that is, bigger companies behave in a more socially responsible manner than smaller ones. In addition, company size can have a relationship with institutional ownership; that is, bigger companies get more attention from the external stakeholder groups than smaller companies, and so, they need to respond to them. Orlitzky (2001) demonstrates that size is a factor in the relationship. Further, CSP is related to the firm size, because, in the beginning, entrepreneurial strategies focus on the basic economic survival and not on ethical and philanthropic responsibilities. Based on the arguments, is expected that the size of the company can be related to CFP, resulting from, for example, the economies of scale.

Financial Risk

For companies to have low risk, they should consider and manage social responsibility. Consequently, a company with low CSP will have adverse impact in terms of risk. Lawsuits against cigarette manufacturers and water and air polluters are some examples of companies in which low CSP has caused high financial risk (Orlitzky and Benjamin, 2001; Itkonen, 2003).

Institutional Ownership

Institutional ownership is generally a large investment in a company, and so, the investor has less ability than individual investor to move quickly without affecting the company's share price (Pound, 1988). Therefore, it is related to company's financial as well as overall performances (Johnson and Greening, 1999; Mahoney and Robert, 2003). To have a company's stake, institutional investors normally consider return and risk. A company with low CSP faces high risk to be pressured, and in turn, will endanger their investment. Therefore, they prefer to look for a company with higher CSP as the choice improves their potential return. The higher the CSP companies have, the more institutional ownership in those companies. In that case, CSP is a means to reduce the risk of investment.

Methodology

Data and Sample Selection

Population of this study is state-owned companies and private-owned companies. Sampling method used is purposive sampling. The sample was based on the following criteria: (1) POCs have been registered in Jakarta Stock Exchange (JSX) during 2001-2004; (2) SOCs, registered in JSX, are treated as SOCs, and those that are not registered are listed in the SOCs list; and, (3) They have issued annual report in JSX and SOCs Ministry.

Measurement of CSP

CSP is measured and calculated through content analysis for each company following the approaches of both by Kinder, Lydenberg Domini (KLD), an United States based independent rating company and by Michael Jantzi Research Associate (MJRA), an independent rating company in Canada. Both these companies measure several dimensions of the CSP to arrive at a total measure of CSP. These dimensions include community issues, diversity in the workplace, employee relations, environmental performance, international issues, product and business practices, and other variables concerning compensation, confidentiality, and ownership in other companies.

Both positive and negative social responsible information was collected through examining the CAR (Corporate annual report), company corporate social reports, along with information obtained from the capital market directory, Jakarta stock exchange websites, other websites and other electronic news of sampled companies. The CSP for each company was assessed on a scale of -2 to +2 for each rating. A -2 rating for any dimension indicates major concern, -1 indicates a notable concern, 0 indicates no notable or major strength and concern, +1 indicates a notable strength and +2 indicates a major strength. A composite CSP score was then calculated by summing the scores of each dimension for each company. Table 6 reports the dimensions of CSP.

Table 6: Dimension of CSP

Dimension	Strength	Concern
Community Issues	<ul style="list-style-type: none">• <i>Generous giving</i>• <i>Innovating giving</i>	<ul style="list-style-type: none">• <i>Lack of consultation/engagement</i>

	<ul style="list-style-type: none"> • <i>Community consultation/ engagement</i> • <i>Strong aboriginal relationship</i> 	<ul style="list-style-type: none"> • <i>Breach of covenant</i> • <i>Weak aboriginal relation</i>
<i>Diversity in Workplace</i>	<ul style="list-style-type: none"> • <i>Strong employment equity program</i> • <i>Woman on board of directors</i> • <i>Women in senior management</i> • <i>Work/ family benefit</i> • <i>Minority/women contracting</i> 	<ul style="list-style-type: none"> • <i>Lack of employment equity initiative</i> • <i>Employment equity controversies</i>
<i>Employee Relations</i>	<ul style="list-style-type: none"> • <i>Positive union relation</i> • <i>Exceptional benefit</i> • <i>Workforce management policies</i> • <i>Cash profit sharing</i> • <i>Employee ownership/ involvement</i> 	<ul style="list-style-type: none"> • <i>Poor union relation</i> • <i>Safety problem</i> • <i>Workforce reduction</i> • <i>Inadequate benefits</i>
<i>Environmental Performance</i>	<ul style="list-style-type: none"> • <i>Environmental management strength</i> • <i>Exceptional environment planning and impact assessment</i> • <i>Environmentally sound resource use</i> • <i>Environmental impact reduction</i> • <i>Beneficial product and service</i> 	<ul style="list-style-type: none"> • <i>Environment management concern</i> • <i>Inadequate environmental planning impact assessment</i> • <i>Unsound resource use</i> • <i>Poor compliance record</i> • <i>Substantial emissions/ discharges</i> • <i>Negative impact of operation</i> • <i>Negative impact of products</i>
<i>International</i>	<ul style="list-style-type: none"> • <i>Community relations</i> • <i>Employee relations</i> 	<ul style="list-style-type: none"> • <i>Poor community relations</i> • <i>Poor employee relations</i>

	<ul style="list-style-type: none"> • <i>Environment</i> • <i>Sourcing practice</i> 	<ul style="list-style-type: none"> • <i>Poor environmental management/ performance</i> • <i>Human rights</i> • <i>Burma</i> • <i>Sourcing practice</i>
<i>Product and Business Practice</i>	<ul style="list-style-type: none"> • <i>Beneficial products and service</i> • <i>Ethical Business Practice</i> 	<ul style="list-style-type: none"> • <i>Product safety</i> • <i>Pornography</i> • <i>Marketing practices</i> • <i>Illegal business practices</i>
<i>Other</i>	<ul style="list-style-type: none"> • <i>Limited compensation</i> • <i>Confidential proxy voting</i> • <i>Ownership in companies have</i> 	<ul style="list-style-type: none"> • <i>Excessive compensation</i> • <i>Dual-class share structure</i> • <i>Ownership in other companies</i>

Measurement of Financial Performance

Following the works of Waddock and Graves (1997) and Roman et al. (1999), Return on Assets (ROA) and Return on Equity (ROE) were used to measure a firm's financial performance. ROA is defined as the ratio of net income after tax to total assets, and ROE is defined as the ratio of net income after tax to outstanding shares. Information on ROA and ROE was collected from the CAR.

Measurement of Control Variables

There are three approaches to measure company size in literature: (1) Total asset (Tsoutsoura, 2004; Fauzi, 2004); (2) The number of people employed (Simerly and Li, 2001); and, (3) Annual sales of the firm (Simerly and Li, 2001; Moore, 2001; Tsoutsoura, 2004). The present study

follows the measure used by Mahoney and Robert (2007) with the argument that total asset is “money machine” to generate sales and income.

Based on the literature survey, the institutional ownership variable, as used by Mahoney et al. (2007), is measured by the number of institutions owning the company shares.

Sample Characteristics

Tables 7-10 report sample characteristics and descriptive data.

Table 7: The Number of Sample of SOCs

Description	Number
Total annuals provided by SOCs in 2001-2004	47
Annual report not eligible for samples	(10)
Annual eligible for samples	37

The number of annual report collected from SOCs is 47. Of the total samples, 10 (21%) annual reports are not eligible for reasons such as damaged files, too short contents, leaving the number of 37 samples (79%).

Table 8: The Number of POCs’s Samples

Description	Number
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Total annual report provide by POCs in 2001-2004	508
Annual repors not eligibles for samples	(84)
Number of annual report eligible efor samples	424

The numbers of POCs supplying annual report were 424. Amongst the Samples, 84 (17%) annual reports are not eligible for sampling. As a result, total samples for both SOCs and POCs are 461 companies. Descriptive statistics are presented by computing mean and deviation standards of CSR, ROA, total assert, risk management, and institutional ownership between state-owned companies and private-owned companies

Table 9: Statistics of Descriptive –SOC

Variable	Mean	Standard Dev	Cases
CSP	4.11	1.76	37
ASSET(in billion Rp)	22.38	38.54	37
ROA (in%)	4.75	5.75	37
ROE (in%)	12.50	14.75	37
IO	12.38	38,03	37

Notes:

CSP= Corporate Social Performance indicates score of SOCs' CSP measured by using the dimension of MJRA

ASSET= Total asset as stated in SOCs's balance sheet

ROA=Return on Asset computed by dividing SOCs' net income by total asset

ROE=Return on Equity computed by dividing SOCs' net income by total asset

IO=Institutional Ownership indicated by the number of SOCs' shares owned by institutional owner

Table 10: Statistics of Descriptive-POCs

Variable	Mean	Standard Dev	Cases
CSR	4.62	2.24	424
ASSET	4.26	13.54	424
ROA	4.99	35.44	424
ROE	23.01	693.24	424
OWN2	3.00	2.25	424

Notes:

CSP= Corporate Social Performance indicates score of POCs' CSP measured by using the dimension of MJRA

ASSET= Total asset as stated in POCs's balance sheet

ROA=Return on Asset computed by dividing POCs' net income by total asset

ROE=Return on Equity computed by dividing POCs' net income by total asset

IO=Institutional Ownership indicated by the number of POCs' shares owned by institutional owner

Results

For H1, t-test analyzed the differences between SOCs and POCs. Table 11 reports the statistics.

Table 11: Testing Mean Difference of CSP/CSR's Score

Description	SOCs	POCs
CSP Mean	4.11	4.62
Deviation standard	1.86	2.24
Sig.(2-tailed)	0,37	0.37

Difference	0,37	0,37
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Table 11 shows no significant mean difference between social performance in SOCs and POCs. As result, the hypothesis (H1), stating that there is mean difference in social performance of SOCs and POCs, cannot be accepted.

Table 12 indicates the result of correlation test between social performance and financial performance at SOCs situation. It is found that (as shown in the table, using the three control variables for both measures of financial performance), there is no a significant correlation between social performance and financial performance.

Table 12: The Correlation Test between Social Performance and Finacial Performance at SOCs

Description	Coefficient	Prob (5%)
CSR-ROA	-0,0480	0,787
CSR-ROE	0,1300	0,464
CSR-ASET	-0,0116	0,949
CSR-IO	-0,0969	0,592

Table 13 shows the correlation test between corporate social performance and financial performance at POCs. As indicated in the table, it is found that there is no significant correlation between social performance and financial performance at POCs situation.

Table 13: Correlation Test Between Social Performance and Financial At POCs

Description	Coefficient	Prob (5%)
CSR-ROA	0,0364	0,457
CSR-ROE	-0,0386	0,429
CSR-ASSET	0,1572	0,001
CSR-OWN	0,0403	0,410

Comparisons are needed specially in developing countries. Al-Khadash (2003) included (34) companies that have annual reports during 1998-2000. Compared to that study, our study has a larger sample. In addition, the classification used in Al-Khadash (2003) is disclose and undisaclose, while this study classifies the sample companies as the SOCs and POCs.

Conclusion

The objective of this chapter was to analyze the difference in social performance in SOCs and POCs and the relationship between corporate social performance and financial performance at SOCs and at POCs using the control variables of company assets and institutional ownership. The score of CSP is determined using content analysis of annual reports of the sampled companies. The independent t-test is used to analyze the mean difference between CSP in SOCs and POCs, while the partial correlation technique is to test correlation between CSP and financial performance. The results indicate no significant mean difference between CSP in the state-owned companies and in the private-owned companies. In addition, this study finds no significant correlation between corporate social performance at SOCs and POCs situation. It is also found that only one variable (company size) has correlation with the SCP.

Recommendation for Managers

The CSR (corporate social responsibility) activities in the Indonesian economics do not seem to contribute to business performance. This study demonstrates that Indonesian companies are increasingly trying to accommodate CSR and emphasizing on CSR as costs than stakeholder relationship. This could be due to the companies' objection of the Indonesian Law No. 40 (2007) on Indonesian Corporation. One of the articles of the law stipulates that Indonesian companies are obliged to conduct CSR. The reason for the objection is their un-readiness to carry out CSR responsibilities.

This study recommends that the authority of SOCs and POCs need to issue the regulations for the companies to disclose the CSR activities in their annual report. The awareness to disclose the CSR activities is expected to encourage them to conduct the CSR. This effort is especially important as CSR activities in developing countries such as Indonesia. The neutrality of the relationship of this study finding may be due to the incompleteness of the annual reports used (as the key data in the content analysis approach) in measuring CSP/CSR.

Direction for Future Research

Further research should include other approaches to measuring the CSP and financial performance. The reputation approach to measuring CSP, for example, as suggested by Orliczky et al. (2003) is an alternative to content analysis or disclosure approach. In addition, financial performance also needs to be extended, and not only should be based on accounting-based measure but also be based on market-based measure and perceptual approach. Longitudinal approach is important to be used as alternative to cross sectional approach. That endeavors are meant to get good understanding of CSR in Indonesia as well as in other developing countries.

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