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The Effect of GCG and Islamic ISR On Company Value with Financial Performance as Moderating Variable in Companies Registered

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Abstract

As the sharia economy in Indonesia continues to grow, sharia-based investments, such as sharia stocks, have gained traction. Among these, the Jakarta Islamic Index (JII) stands out as the first sharia stock index, comprising 30 of the most liquid sharia-compliant stocks. The liquidity and performance of companies within JII can be assessed through annual financial reports, which follow sharia principles. This study aims to investigate the influence of Islamic Social Reporting (ISR) and Good Corporate Governance (GCG) on Company Value, with Financial Performance acting as a moderating variable. Specifically, the research focuses on companies listed in JII in 2019, providing insights into how GCG and ISR disclosures impact investor perceptions and firm valuation in the context of sharia-compliant investments. Employing quantitative methods, this research analyzes secondary data obtained from annual financial reports available on the Indonesian Stock Exchange website. The findings will contribute to understanding the role of ISR and GCG in enhancing Company Value and how Financial Performance influences this relationship, offering valuable insights for stakeholders, investors, and policymakers aiming to strengthen the sharia finance sector in Indonesia.

Keywords	Good Corporate Governance (GCG), Islamic Social Reporting (ISR), Company Value, Financial Performance, Jakarta Islamic Index (JII)

INTRODUCTION

The growth of the sharia economy in Indonesia has been remarkable, driven by an increasing demand for sharia-compliant products. This growth reflects the rising awareness and interest among Indonesians for financial services that align with Islamic principles. The Indonesian government has been actively supporting this sector, aiming to establish Indonesia as a global hub for Islamic finance. Sharia-based products in Indonesia now encompass a wide range, including mortgages, banking services, and investment instruments, showing the sector's expanding appeal and robustness.

Sharia finance in Indonesia comprises various products structured to comply with Islamic law, which prohibits riba (interest), gharar (excessive uncertainty), and maysir (gambling). Sharia mortgages, for instance, avoid interest payments and instead use profit-sharing arrangements. Sharia banking is another fast-growing area, providing savings and financing options based on profit-sharing principles, which appeal to consumers seeking ethical alternatives to conventional finance.

Sharia-based investments are primarily categorized into equity-based investments, like stocks and mutual funds, and debt securities, notably sukuk (Islamic bonds). Sukuk, issued by either government or corporate entities, offer investors ownership in an asset or project rather than conventional debt repayment, aligning with the Islamic value of tangible assets. Sukuk are a preferred investment for those looking to combine financial returns with ethical principles.

However, the variety of sharia stocks remains limited compared to traditional investments. Investors interested in sharia-compliant shares often rely on indices like the Jakarta Islamic Index (JII) and the broader Indonesian Sharia Stock Index (ISSI), which include companies meeting Islamic ethical standards. These indices serve as benchmarks for sharia-compliant investments, guiding investors in adhering to religious principles.

Sharia stocks have shown impressive performance, contributing to overall stock market growth in Indonesia. In 2021, the Indonesian stock market saw over 10% growth in sharia stocks, highlighting the sector's appeal and investor confidence. On December 30, 2021, ISSI reached a market capitalization of IDR 3,983.65 trillion, marking a 19.36% increase from IDR 3,344.93 trillion in 2020. This growth aligns with the broader Composite Stock Price Index (IHSG), underscoring sharia investments as a key part of Indonesia's financial ecosystem.

The Sharia Securities List (DES), a regulatory framework ensuring listed companies' adherence to Islamic standards, expanded its membership in 2021, increasing from 141 companies in 2020 to around 494. DES membership verification, conducted twice annually by the Financial Services Authority (OJK), bolsters investor confidence and reflects the sector's growth.

Indonesia's sharia capital market began in 1997 with sharia-compliant mutual funds, a milestone in Islamic finance development. The launch of the Jakarta Islamic Index (JII) in 2000 was another major step, creating a dedicated index for sharia-compliant stocks. Today, JII tracks 30 of the most liquid and compliant companies on the Indonesian Stock Exchange (IDX), each operating in sectors that comply with Islamic ethics.

In 2011, the broader Indonesian Sharia Stock Index (ISSI) was introduced, expanding the range of sharia-compliant stocks and offering investors a wider view of Islamic finance opportunities in Indonesia. ISSI serves as a key indicator of the health and growth of the sharia economy, reflecting the increasing number of companies adopting sharia-compliant practices.

Regulatory support from the Financial Services Authority (OJK) and Bank Indonesia (BI) has been instrumental in the expansion of sharia finance. Policies include tax incentives for sukuk issuance and capital requirements supportive of sharia banking. Regular assessments by OJK help maintain compliance and trust in the sector.

Indonesia's government is committed to developing the sharia finance sector, aiming for innovations in sharia-compliant digital banking solutions and new investment vehicles, such as sharia-based exchange-traded funds (ETFs). However, challenges remain, including the need for a more diverse range of sharia-compliant investment options. The limited selection of companies on JII and ISSI suggests room for growth.

Attracting foreign investment also presents challenges, as the unique regulatory environment of sharia finance requires specialized understanding. Additionally, many Indonesian consumers and investors remain unfamiliar with Islamic finance principles, which could hinder the sector's growth. Increasing awareness through financial literacy programs could help bridge this gap and make sharia finance more accessible.

Sharia finance plays an increasingly important role in Indonesia's economy, promoting financial inclusion by offering products aligned with religious and ethical values. This inclusivity fosters economic growth and reduces poverty by providing financial access to a segment of the population that may otherwise be excluded from traditional banking.

Moreover, sharia finance aligns with Indonesia's commitment to sustainable and socially responsible investing. Many sharia-compliant companies uphold environmental, social, and governance (ESG) standards, making them attractive to ethical investors. This alignment with ESG principles could help Indonesia attract a growing number of investors focused on sustainability, thus contributing to the country's sustainable development goals.

LITERATURE REVIEW

Definition of Good Corporate Governance

Good Corporate Governance (GCG) refers to a structured system comprising inputs, processes, and outputs that defines the relationships between various stakeholders, including the board and shareholders. This system aims to establish and maintain effective governance practices to achieve GCG, facilitate constructive interactions, prevent potential conflicts related to organizational planning, and ensure prompt resolution of issues (Zarkasyi, 2008). According to the UK Turnbull Report (2006), "Corporate Governance is a company's internal control mechanism, implemented to preserve company wealth, enhance capital investment value, and achieve business objectives as envisioned by shareholders." Thus, GCG is essential for managing significant risks to safeguard the company's long-term assets and realize its strategic goals.

Definition of Islamic Social Reporting

Howard R. Bowen introduced the concept of social responsibility in 1953 through his work *Social Responsibility of the Businessman,* which laid the foundation for business professionals to align their goals with societal values. Later, Keith Davis (1960) expanded the concept, coining *corporate social responsibility* (CSR) and emphasizing that companies bear responsibilities beyond financial profit, which include ethical and social obligations (Solihin, 2009:16). In the 1990s, CSR evolved to include *Corporate Social Reporting* (CSR), which allowed companies to disclose their social and ethical contributions in alignment with Islamic principles, forming what is now known as Islamic Social Reporting (ISR).

Definition of Company Value

A high company value is crucial as it often reflects an increase in stock prices, thereby representing shareholder wealth. For managers, company value serves as a key metric of performance. According to Brigham and Gapenski (2006), company value can be assessed using the *Price to Book Value* (PBV) ratio, which compares the company's share price to its book value per share. An increasing company value generally indicates improved company productivity and market performance.

Definition of Financial Performance

Financial performance is a measure used to evaluate a company's success in generating profits. It provides insight into the company's health and effectiveness in managing its resources. According to Sucipto (2003), financial performance significantly determines a company's success in profitability. Financial performance reflects the company's capacity to organize and manage its resources effectively. Strong financial performance is often a benchmark of high company value when evaluated fundamentally, as it reflects the company's ability to optimize and utilize its assets efficiently.

Data Source

This study utilizes secondary data, which is collected indirectly by researchers through third-party sources (Sugiyono, 2011:137). Specifically, data for this study is sourced from the Indonesian Stock Exchange's official website (www.idx.co.id). The research employs data from the Annual Financial Reports of companies listed on the Jakarta Islamic Index (JII) for the year 2019.

METHOD

Research Design

This study adopts a quantitative approach with an associative method to identify the influence of Good Corporate Governance (GCG) and Islamic Social Reporting (ISR) on company value, as well as the moderating role of financial performance. The research data is derived from the annual financial reports of companies listed on the Jakarta Islamic Index (JII) for the year 2019.

Data Collection

Secondary data is obtained from the Indonesia Stock Exchange website (www.idx.co.id). The collected data includes components related to GCG, ISR, financial performance, and company value from the annual reports of companies listed in the JII index for 2019.

Operational Definition of Variables

1. Good Corporate Governance (GCG): Measured using a scoring assessment technique based on FCGI guidelines.
2. Islamic Social Reporting (ISR): Measured based on ISR components that align with sharia principles.
3. Financial Performance (Moderating Variable): Used as a moderating variable to measure the influence of GCG and ISR on company value. Financial performance is calculated using Return on Equity (ROE).

4. Company Value (Dependent Variable): Measured using Price to Book Value (PBV), as an indicator of company value.

Data Analysis
1. Descriptive Statistics: Used to obtain the mean, minimum value, maximum value, and standard deviation of the studied variables.
2. Classical Assumption Tests: Includes normality, multicollinearity, heteroscedasticity, and autocorrelation tests to ensure the regression model meets classical assumptions.
3. Multiple Regression Analysis: Used to determine the effect of the independent variables (GCG and ISR) on the dependent variable (company value).
4. Moderated Regression Analysis (MRA): Applied to test the moderating effect of financial performance on the relationship between GCG and ISR on company value.
5. Hypothesis Testing: Utilizes the T-test for individual effects and the F-test for simultaneous effects of the independent variables on the dependent variable.

RESULT AND DISCUSSION
Overview of Research Object
The Jakarta Islamic Index (JII) is a sharia-compliant stock index that was first launched in the Indonesian Sharia Capital Market on July 3, 2000. JII includes 30 companies that adhere to sharia-based principles. Companies listed on JII are those that operate according to Islamic sharia principles, reflecting a commitment to the values and ethical standards of Islam. The evaluation of sharia stocks registered in JII is conducted twice a year, in May and November, to ensure that these stocks continue to meet sharia compliance standards as verified by the Financial Services Authority (OJK).

Descriptive Analysis Results
This research involves three types of variables: independent, dependent, and moderating variables. The independent variables are Good Corporate Governance (GCG) and Islamic Social Reporting (ISR). The dependent variable is Company Value, while Financial Performance serves as the moderating variable.

Descriptive Statistical Test
The purpose of the descriptive statistical test is to calculate the mean, minimum value, maximum value, and standard deviation of each variable. Below is the output of the descriptive statistical test:

Table 1. Descriptive Statistical Test

Variable	N	Minimum	Maximum	Mean	Std. Deviation
ISR	55	0.5	0.75	0.6333	0.0658
EPS	55	-20.42	969	264.322	254.0354
ROE	55	-0.01	32.44	12.8596	8.76383
GCG	55	0.57	0.97	0.7558	0.11652

Source: Data processed in 2023

Classical Assumption Test

1. Normality Test: This test evaluates whether the residuals of the regression model follow a normal distribution. Using the Kolmogorov-Smirnov test, data is considered normal if the significance (sig.) value is greater than 0.05. If the points on the P-Plot are close to and follow the diagonal line, the data is deemed normally distributed. If the points deviate significantly from the diagonal, the normality assumption is not met.
2. Multicollinearity Test: This test assesses whether there is correlation among the independent variables. The model is free from multicollinearity if the tolerance value is greater than 0.1 and the VIF value is less than 10. Otherwise, multicollinearity exists, indicating a problematic regression model (AN Kolmogorov, 1933).
3. Heteroscedasticity Test: This test checks whether the residuals are homoscedastic, meaning their variance is constant across observations. If the scatterplot displays no clear pattern and the points are evenly distributed above and below the Y-axis, the model is free from heteroscedasticity.
4. Autocorrelation Test: This test measures whether there is autocorrelation in the regression model, where errors from one period correlate with those of the previous period. According to Ghozali (2012:110), the Durbin-Watson (DW) test is used to make this assessment.

Multiple Regression Test

The multiple regression test identifies whether one or more independent variables significantly affect the dependent variable.

T-test

The T-test determines whether each independent variable individually influences the dependent variable. The significance value is compared to an alpha level (typically 0.05) to decide if the effect is statistically significant.

F Test

The F test assesses whether the independent variables, when considered together, significantly impact the dependent variable. If the significance level is below 0.05, the combined effect is considered statistically significant. In this study, the variables ISR and GCG have a significance of 0.000, indicating a substantial joint influence on company value.

Coefficient of Determination Test

The coefficient of determination (R Square) measures the extent to which the independent variables explain variations in the dependent variable. An R Square value of 0.375 implies that GCG and ISR explain 37.5% of the variation in company value, with the remaining 62.5% attributed to factors outside this study.

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Interaction Test (Moderated Regression Analysis/MRA)

The Moderated Regression Analysis (MRA) tests whether the moderating variable (Financial Performance) influences the relationship between the independent variables and the dependent variable.

a. First Stage: The initial test yields a beta of 0.378 with a significance value of 0.088, which is greater than 0.05. This indicates that Financial Performance does not moderate the relationship between GCG and Company Value, leading to the rejection of Hypothesis 3.
b. Second Stage: The second test yields a beta of 0.400 with a significance value of 0.003, which is below 0.05. This indicates that Financial Performance does moderate the relationship between ISR and Company Value, supporting Hypothesis 4. These results suggest that Financial Performance acts as a pure moderator in this context.

CONCLUSION

Based on the results of the data analysis conducted on the research variables, the following conclusions can be drawn:

1. Good Corporate Governance (GCG): Measured using a scoring assessment method based on the FCGI Self-Assessment Checklist, GCG has a significant influence on Company Value. GCG practices are evaluated through aspects such as shareholder and investor rights, corporate governance practices, policies, disclosures, and audit functions, which serve as a foundation for building stakeholder trust and maximizing Company Value.
2. Islamic Social Reporting (ISR): ISR does not significantly impact Company Value. Sharia-compliant stocks listed on the 2019 Jakarta Islamic Index (JII) do not increase stakeholder trust through the disclosure of Islamic CSR in Annual Financial Reports, and therefore, they do not enhance Firm Value from the perspective of investors.
3. Financial Performance as a Moderating Variable: Financial Performance effectively moderates the influence of GCG on Company Value. This finding suggests that stronger financial performance enhances the effect of Good Corporate Governance on Company Value, increasing shareholder or investor confidence and subsequently boosting the company's value. However, Financial Performance does not moderate the impact of ISR on Company Value. In the Indonesian context, investors predominantly consider financial performance as a primary benchmark for increasing company value, often overlooking non-financial indicators such as ISR when making investment decisions.

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