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Corporate Social Responsibility Policies and Value Creation: Does Corporate Governance and Profitability Mediate That Relationship?

ABSTRACT

With a purpose to give a deep understanding relating to the manifestation of social responsibilities practices among Indonesian companies, this paper reflects the relationship of corporate social responsibility (CSR), corporate profitability (CP), value creation (VC) and good corporate governance (GCG). Kinder, Lydenberg, and Domini's (KLD) measurement approach is used in this study to measure the social responsibility practices as this gives cross-border analysis of social responsibility. Corporate Profitability captures return on assets which is accounting-based measurement, whereas value creation explains the economic value added which is shareholder-based measurement. Structural Equation Model (SEM) analysis is conducted for Indonesian listed companies which appeared in Corporate Governance Perception Index (CGPI). The empirical result suggests that CSR serves as a tool in assisting shareholders value and performance. Accordingly, firms should incorporate CSR practices to enhanced its strategic investment and sustain a strong relationship with its stakeholders. Subsequently, management should also take concern of having good corporate governance in order to improve company's performance by supervising and monitoring of the company's operation, ensure the fulfillment to the stakeholder's interest.

Keywords *Kinder Lydenberg and Domini's, Economic Value Added, Return on Assets, Corporate Governance Perception Index.*

JEL Classification: M4, Q5, G3

1. Introduction

In the traditional perspective, it is believed that business objective is to maximize the shareholder's wealth. However, as business grows, society come up with different perspective on how organization should operates. In this case, companies should shift from the mindset of enriching only shareholders to focusing on all the stakeholders, including environmental sustainability and community welfare. It is also becoming more important for companies to fulfill the environmental expectation in order to gain its reputation which further influence the firm's performance (Vargas, 2016).

Corporate social responsibility is considered to relate to corporate governance as governance is positively associated with the environmental strength of a firm (Stuebs and Sun, 2010). Not only that, previous study describes that good corporate governance could not able to increase reputation and performance of the company without also doing social responsibility practices (Chalise, 2014). Recent studies have also analysed the relationship of CSR and corporate governance from environmental performance perspective. The result shows a positive correlation on the study (Stuebs and Sun, 2010). This is because Corporate governance highlights the framework to form an environment which are transparent, accountable and trusted. It also refers to how companies are being directed and controlled to avoid disputes between agents and investors and ensure that funds managed by agents are used accordingly (Detthamrong, Chancharat & Vithessonthi, 2017).

However, looking at the enforcement of CSR in Indonesia, this has been just a voluntary disclosure for many years. Meanwhile, starting from July 2007, Indonesian government has enforced a new regulation regarding CSR practices disclosure for natural resources companies. Thus, CSR practices has not been engaged by a number of companies in Indonesia. Therefore, based on the importance of the variables, this study is the aims to analyse the relationship of CSR policies and company's performance using corporate governance (CG) as intervening variable. Hereinafter, this is the first study that attempts to give a deeper analyses regarding implementation of CSR practices. Insights obtained from this study may contribute to both theories and real practices of CSR policies. It could be done to improve the CSR understanding and management literature, as well as answering questions by different individuals or corporates regarding CSR, CG and firm's performance.

2. Literature review and hypothesis

2.1 Corporate social responsibility and corporate profitability

Many studies have been done to examine the effect of CSR, including towards company's profitability. Corporates' profitability refers to the analysis of the ability of company to generate income. In this study, return on assets (ROA) is used to analyze the overall effectiveness of company's ability to generate profit with its assets (Gitman & Zutter, 2012). CSR is an important element to build and maintain corporate's reputation and profitability, which also increase competitive advantage of the company (Park, 2017; Devie et al, 2019). This is considering the perspective of their customers which has various response relating to implementation of CSR policies. Hence, companies that intend to enhance their reputation, should focus on providing products with better quality that is able to satisfy its customers (Park et al, 2014). Therefore, good social reputation will leads to an increase of sales, especially to customers that are sensitive to social and environmental issues, thus increase corporate profits (Khojastehpour & Johns, 2014). Profitable and large firms also found to have a higher CSR disclosure in their report (Muttakin, Khan & Subramaniam, 2015). Moreover, there have been several studies done worldwide to analyse the impact of CSR on different company's outcome including profitability. Yet, many have questioned as to whether the CSR implemented that incurred costs has created more benefits to it. Besides, this relationship between CSR and CP still creates confusion and different results especially inconsistency for develop and developing countries. Among all the previous studies explained in the summary table of previous research, the positive relationship between CSR and corporate profitability can be mostly seen and found (LaGore, Mahoney & Thorne, 2013; Yu and Choi, 2014; Cheung, 2010). Thus, this research study come up with the following hypothesis.

H1: CSR policies has a positive impact on corporate profitability

2.2 Good Corporate Governance to corporate's profitability

Companies' corporate governance implementation creates a system for directing, controlling and supervising the entire resources of the company efficiently and effectively (Jackling and Johl, 2009). Corporate governance is made to maintain the various interest from the stakeholders of the company which may provide benefits for the company. A company with a higher Corporate Governance Perception Index (CGPI) means that the company has been managed with transparency, accountability, responsibility, independency and fairness. Therefore, an impact can be seen on the outputs of good corporate performance, such as ROA, ROE and EPS (Gompers et al, 2003). Some previous studies using the same governance index, found that companies with stronger stakeholder rights tend to have higher profits. Sheikh et al. (2013) also found a positive relationship between board size and company performance.

H2: GCG has a positive impact on corporate profitability.

2.3 Corporate social responsibility and Good Corporate Governance

Corporate social responsibility (CSR) is currently a crucial element of companies and their stakeholders and continues to reap attention atop the corporate strategy. Previous study reveals that higher commitments to CSR strongly and positively correspond to the qualifications and terms of directors, boards that exert strong stewardship and strategic leadership roles, and the management of capital market pressures, and that these various attributes combined constitute the hallmarks of good corporate governance (Lock & Seele, 2015). Hence, CSR actively seeks a greater balance or compatibility between profit and ethics, which is consistent with corporate governance mechanism. Besides, Corporate social responsibility is considered related to corporate governance as governance is positively associated with environmental strengths of a firm (Stuebs and Sun, 2010). Not only that, previous study shows that good corporate governance did not able to increase reputation of the company without also doing social responsibility practices (Chalise, 2014). Recent studies have also analysed the relationship of CSR and corporate governance from environmental performance perspective. The result shows a positive correlation on the study (Stuebs and Sun, 2010). This is because of the documentation of CSR performance of a firm has further give benefits to support the corporate governance improvement effort of a company.

H3: CSR policies has a positive impact on good corporate governance.

2.4 Corporate profitability and value creation

In the recent years, the influence of profitability or performance on firm value have attracted researches attention. In the competitive environment, companies are trying their best to sustain in the industry by optimizing their cost in order to gain more profit for their operations. Besides, management start concerning about its investment plans to maximize shareholder's wealth and firm value (Chen, 2011). Understanding the relationship of profitability and value creation is also important to financial decision making of the firm. Some researches has also proven the positive correlation between profitability and firm value (AlNajjar & Belkaoui, 1999; Crisóstomo et al, 2011; Osazuwa & Che-Ahmad, 2016). It was proven that as the firm profit got greater, more earnings would be distributable to shareholders. This is also inline with the agency theory about the management ability in managing assets in order to maximize profit, creating shareholder's trust to company's quality of management. Thus, the higher the financial performance, the higher the value of the company.

H4: CP has a positive impact on Value creation

2.5 Corporate social responsibility and value creation

A new method to measure firm's performance through value creation, is known as Economic value added (EVA). EVA is relevant for measuring the firm's performance as this tells us how much the companies have been creating for the stakeholders and how efficient the management is utilizing the capital from the stakeholders. It is also known as economic profit, which is believed to be a special way of measuring profit. This is because EVA is measured taking account into all the opportunity or cost of the capital invested in the business (Steward, 2014). Relating to CSR, CSR strategies need to be developed in order to have a proper CSR policy that is essential to satisfy the firm's goals. It is crucial to pay more attention to actives that may add scores to company's value. If the company is showing a positive VC, this also means that the company is working align with the corporate social responsibility. Besides, CSR creates value to the firm as the firm could be able to differentiate them from the competitors and also to reduce its costs. As the firm is having adequate management, this creates also value for the business and society. This shows the positive correlation between the company investment in CSR and the value creation of the firm (Green & Peloza, 2011). Likewise, there was also found to be a positive relationship between CSR and share price among companies in UK, especially those with an environmentally sensitive industry such as electricity, mining, and gas. Accordingly, the second hypothesis made for this research study is:

H5: CSR policies has a positive impact on value creation.

2.6 Good Corporate Governance and Value Creation

Corporate governance includes making sure that shareholders wealth as well as the other stakeholders are being taken into account in the management operation. This is also to prevent the corporate fraud and illegal accounting measure. Thus, value creation should be considered as to have a good corporate governance. Previous studies have found that significant corporate governance effect the greater shareholder's rights which by higher profit, sales growth and firm value (Gompers, Ishii, & Metrick, 2003). Some other researches are also showing different result for companies that implement good corporate governance in developed, developing and underdeveloped countries. Positive relations are found between good corporate governance practices with company's value (Klapper and Love, 2002; Black, Jang, and Kim, 2006).

H6: GCG has a positive impact on value creation.

2.7 Corporate social responsibility, good corporate governance and corporate profitability

The stakeholder theory defines that companies should do CSR practices as to fulfil their responsibility to stakeholders and able to maximize financial strength of the company. Supporting this, the corporate governance is describing as the intervening variable, strengthening the relationship of CSR and Corporate Profitability (CP). Besides, companies should have good corporate governance in addition to implementation of CSR practices, in order to give positive impact to the performance. This is because the importance of corporate governance take concern the welfare of all stakeholders, not only shareholder. Previous researchers also found positive relationship between CSR and performance (Salama, Anderson and Toms, 2018; El Ghoul et al., 2011; Lourenco et al., 2011). In addition to this, some also did research on the potential impact on CSR practices on firm's sustainability and resulted in corporate governance positively effecting CSR disclosure (Li et al., 2010)

H7: GCG could mediate the relationship between CSR policies and corporate profitability

2.8 Corporate social responsibility, good corporate governance and value creation

CSR could be considered as activities that create values for improving the firm's reputation, which further lead to improvement of economic performance of the company. CSR not only creates financial benefit to the company, but also strategic advantage. By engaging in social responsibility practices, firms can gain trust and goodwill from stakeholders, which is also a competitive advantage (Kolk and Pinkse, 2010). Research suggested that CSR activities would enhanced firm's image and reputation (Vanhamme et al., 2012). CSR policies help in increasing the company's value and satisfy its goals. Companies doing CSR practices creates positive Value Creation (VC) for the company. EVA which is a measurement of value created or lost is used to measure the performance and value creation made within the company. There is no previous research done regarding the relationship of CSR policies and value creation through GCG as intervening variable.

H8: GCG could mediate the relationship between CSR policies and value creation.

3. Research methodology

3.1 Sample

For the analysis of this study, as Structural Equation Model (SEM) is used. This model analysis covers gathering of secondary data, testing of hypothesis and evaluation of variable correlations. The sample of the study involves firms that are consistently listed as having good corporate governance by SWA-Magazine and Indonesia Institute for Corporate Governance (IICG) in 2016 and 2017. This study makes use of secondary data, including annual report, Bloomberg terminal and company's website.

Table I Summary of the sample observed

Sampling Criteria	*No. of Companies*
Companies listed in CGPI in the year 2016 and 2017 by SWA Magazine and IICG	39
Companies that were not consistently listed as having GCG in year 2016 and 2017	(13)
Companies that do not publish complete annual report in the required period	(10)
Number of companies which fulfill the criteria	16
Total sample used in the research (16 x 2)	32 firm-year

From the population of 39 companies included in the Corporate Governance Perception Index (CGPI) in 2016 and 2017, there are 23 companies that were not included for this research as the companies did not fulfilled the requirement of the research. It was those companies not consistently listed in CGPI and not publishing a complete annual report in the required period. Hence, there are 16 companies which fulfil the criteria and was the number of the companies observed. All samples that is used in the research are 32 reports derived from 16 companies multiplied by 2 years of observation.

3.2 Measures

Corporate Social Responsibility (CSR)

CSR policies is measured using Kinder, Lydenberg, and Domini's (KLD) method, chosen as a basic of CSR level. This measurement has been widely used in previous leading management journals (Nguyen and Nguyen, 2015; Li et al, 2010; Jo and Na, 2012; Devie et al, 2019). KLD provides benchmarking in 5 areas of CSR issue relevant to Indonesian companies, including diversity, community, environment, employee relation and products. In each of the KLD measurement, there are strengths and concerns. The strengths are considered to be positive CSR policies implemented, while concerns are as negative CSR policies implemented. If a company has a strength or even a concern, this would be given a “1” or “-1” On the other hand, companies without any would be indicated with a “0”. After scoring the 5 qualitative areas, the total score of strength and concerns should be calculated in order to get Net CSR.

Value Creation

EVA spread is used as the mesurement of value creation. EVA is a performance measurement to calculates the residual income from subtraction of additional charge from net operating profit after tax (Steward, 2014), which take into account cost of capital and cost of equity. EVA aims to figure out the economic profit of a company.

Corporate Profitability

Return on Asset (ROA) is used as the measurement of profitability. This is calculated by dividing net income by average total assets. ROA is also known as the overall effectiveness of company’s management in generating profits with its assets (Gitman & Zutter, 2012). ROA is widely used measurement of profitability in environmental studies (Nguyen & Nguyen, 2015; Park, 2017; Devie et al, 2019)

Good Corporate Governance

This research has been using GCG as the intervening variables. The GCG was measured using the measurement of Corporate Governance Perception Index (CGPI) that was published by IICG and SWA Magazine. This then had a scale of 0-100 values. CGPI score with the predicate "very trusted" for companies with scores of 85-100, "trusted" for companies with scores 70-84, and "quite reliable" for companies with a score of 55-69. The higher the score a company can get, the better the application of corporate governance is considered to be.

Table II Variable definitions and data source

Variable(s)	*Definitions*	*Data Source*
CSR Policies	Difference between total strengths score and total concerns score	Annual and Company' Websites
Corporate Profitability (ROA)	Percentage of net income over total assets	Annual Report and Bloomberg terminal
Value Creation (EVA)	Total of Net Operating Profit After Tax divided by the invested capital deducted by the weighted average of cost of capital	Bloomberg
Good Corporate Governance	Score of good corporate governance by SWA Magazine and IICG	SWA Magazine

3.3. Model

This study helps to analyze the relationship of CSR to Firm’s performance in a positive, negative or neutral way as well as the role of corporate governance (CG) as intervening variable that alters financial performance. A multivariate statistical model is used through validity, reliability, and collinearity tests (Kock, 2015). Validity test consists of convergent validity and discriminant validity test for each of the indicator.

Table III Combined loadings and cross-loadings

Indicator	CSR	GCG	CP	VC	P value
CSR	1.00	0.00	0.00	0.00	<0.001
CG	0.00	1.00	0.00	0.00	<0.001
ROA	0.00	0.00	1.00	0.00	<0.001
EVA	0.00	0.00	0.00	1.00	<0.001

The table above shows that all the factor loading value of each indicators are all above 0.5. These value means that all indicators of CSR, CG, ROA and EVA which were used to measure all the variables have fulfilled the convergent validity test.

The following table shows discriminant validity. The discriminant validity is to compare the square root of average variance extracted (AVE) of each latent variable with the correlation between latent variables. If the square root of AVE of one indicator is larger than the other coefficient correlations in one parallel row of column, then the validity is fulfilled. The result of the discriminant validity is explained in the table below.

Table IV AVE table

Indicator	CSR	GCG	CP	VC
CSR	1.00	0.010	0.717	-0.061
CG	0.010	1.00	0.157	-0.149
ROA	0.717	0.157	1.00	-0.642
EVA	-0.061	-0.149	-0.642	1.00

From the table above, the square root AVE shows a figure of 1.00 for all results. These are also bigger than the coefficient correlation of the other variables.

Composite Reliability, Cronbach's Alpha and Collinearity

From the composite reliability test, all the variables have the value of 1.00, therefore composite reliability criteria are fulfilled. Not only that, result also has the Cronbach's Alpha value of more than 0.6, which is 1.00 for all the variables. Thus, all the variables have been fulfilled the criteria of reliability.

Table V Collinearity table

	CSR	GCG	CP	CV
R^2		0.099	0.817	0.864
Adj. R^2		0.069	0.805	0.850
Full collinearity VIFs	3.24	1.054	3.149	3.188

In order to fulfill the collinearity test, VIFs must be lesser than 3.3 or 10 in a more relaxed criterion (Kock, 2015). According in Table V, all variables have passed the multicollinearity tests.

4 Research results and analysis

4.1 Descriptive analysis

Descriptive analysis is done through looking at the statistics of coefficients which combined up as the data set, either in form of population as a whole or a sample as a part of the population. This explains the overview of the research data as a whole, which includes the total number of data used, minimum and maximum value, mean and standard deviation.

Table VI Descriptive Statistics

Indicators	Minimum	Maximum	Mean	STDEV
CSR	6.00	13.00	8.78	1.81
CG	72.68	93.32	84.92	5.32
ROA	-45.60	22.07	1.30	10.51
EVA	-7.17	94.57	5.31	17.67

Comparing the range to the CSR policies mean result in this research, the companies that are listed in Corporate Governance Perception Index (CGPI) and used in this research, are presumably quiet well. Besides, the profile GCG for its weighted average of 2016 and 2017 shows that GCG has one indicator with minimum and maximum value of 72.68 and 93.32. As the companies taking account into this research are those that are consistently listed as having a good corporate governance, this means that the companies are showing a well performance which is considered as trusted company, which lies within the range of 70-84. Besides, the mean value of the GCG score is 84.92 which categorized as "most trusted companies", lies within 85-100. Thus, it computes that companies that are start to be concerned about it corporate governance.

4.2 Hypothesis Test (Direct, Intervening and Total effects)

The hypothesis test done by using the T-test and re-sampling. The hypothesis test divided into 3 parts of direct effect, mediation variable and the total effect of the variables in this research.

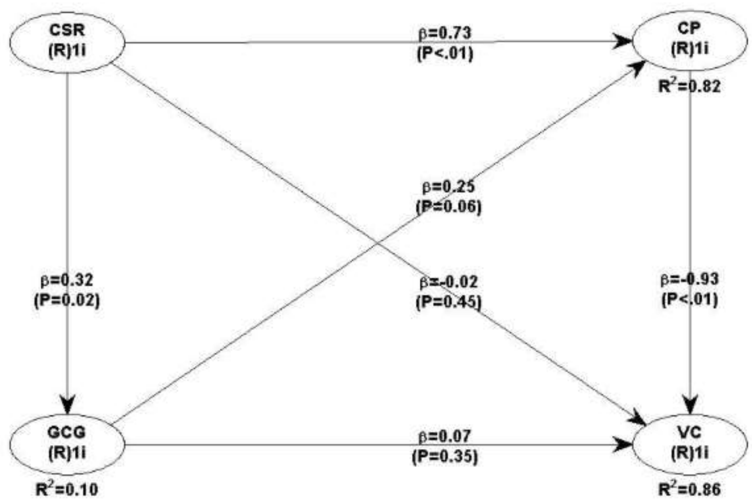

Figure I Structural model result

4.2.1 Direct Effect

Table VII Path Coefficient and P values

Independent / Control variable	Dependent Variable	Path Coefficient	P-value	Note
CSR	CP	0.73	<0.01	Highly significant
CSR	Value creation	-0.02	0.45	Insignificant
CSR	GCG	0.32	0.02	Significant
GCG	CP	0.25	0.06	Weakly significant
GCG	Value creation	0.07	0.35	Insignificant
Profitability	Value creation	-0.93	<0.01	Highly significant

Figure 1 and table VII shows that corporate social responsibility policies affect corporate governance with the coefficient value of 0.32 and p value 0.02, and it also give effect on corporate's profitability with 0.73 coefficient value and $p<0.01$. In another words, the higher score of CSR policies would increase the profitability of the company (ROA), supported by the p value of lower than 5% significant level of both. This also means that **hypothesis 1** is accepted as the relationship between CSR policies and profitability shows a positive and highly significant direct relationship, hence **hypothesis 3** is also accepted as the CSR also having a direct positive relationship with good corporate governance. The first hypothesis result is line with the stakeholder theory that when firms are taking CSR practices into consideration, they would read a better performance (Yu and Choi, 2014). On the other hand, the acceptance of the hypothesis 3 is in line with the believe that higher commitments of CSR could strongly impact in the qualifications of directors and other members of the company which combined into a good corporate governance hallmark. Besides, good corporate governance may not able to increase reputation of the company without also taking care of the socially responsibility practices in the company (Chalise, 2014). Moreover, good corporate governance is showing a positive correlation of 0.25 and p=0.06, which is deemed to be weakly significant. Thus, **hypothesis 2** explains the relationship between GCG and profitability that is positive but weakly significant, and acceptable. This means that when companies are directed and controlled properly, the company could be more efficient in the work and operation and resulted in a better performance. This is because the increase in efficiency of the work and profit of the company could also get impacted (Sheikh et al, 2013).

Furthermore, the relationship of CSR Policies to value creation shows a value of -0.02 with p=0.45, which means that a higher score of CSR policies, the value of the firm would decrease and this is insignificant. Hence, the **hypothesis 5** is rejected. This is supported by the theory that CSR practices could create long-term value for the company's financial performance instead of giving short-term impact (Gregory, Tharyan & Christidis, 2011). Moreover, the data also describes there is an insignificant effect of good corporate governance on value creation of 0.07 and p=0.35. this means that there is an insignificant positive relationship between the two variables, so **hypothesis 6** is rejected. It possibly happens because corporate governance implementation in a company can not directly influence the firm's value, but it takes some time. Likewise, the relationship between profitability and value creation shows a negative 0.93 with p<0.01. This means that profitability doesn't give a rise to value creation as it increases. Thus, **hypothesis 4** is also being rejected. If profit do not provide increase of funding of the company, the firm still has to decrease its dividends or choose to increase its debt level for the funding. These both gives negative impact to the markets and usually result in a decrease of share price and destroy the shareholders value.

4.3.2. Intervening Effect

The table below shows the indirect effect and P values of intervening variables.

Table VIII Indirect Effect and P values

Independent variable	Intervening variable	Dependent variable	Path coefficient	P value
CSR	CP GCG	VC	-0.657	<0.001
CSR	GCG	CP	0.079	0.258
GCG	CP	VC	-0.233	0.023

Looking at the table above, the p value of CSR towards corporate's profitability with good corporate governance as the mediating variable is 0.258. This figure shows a big percentage which is more than 5% significance, thus this consider to be insignificant. It can be concluded that good corporate governance fails to act as a mediating variable between the relationship, therefore **hypothesis 7 is rejected.** Additionaly, for the result of **hypothesis 8 is rejected**, since the mediating variables shows a significant value of 0.023 (<0.05) with path coefficient for this is at -0.233. Hence, corporate profitability acts as the mediates between the good corporate governance and value creation but negatively.

4.3.3. Total Effect

The total effect refers to the p values for all variables included in the research. This includes all the direct and indirect effect and being discussed further below:

Table IX Total Effect and P Values

	CSR	GCG	CP	VC
CSR	-	-	-	-
GCG	0.32 (=0.023)	-	-	-

CP	0.807 (<0.001)	0.25 (=0.06)	-	-
VC	-0.752 (<0.001)	-0.167 (=0.158)	-0.93 (<0.001)	-

The detailed calculation of the absolute contribution between variables is discussed below:

CSR to GCG = $(0.32)^2$ X 100% = 10.24%

CSR to CP = $(0.807)^2$ X 100% = 65.12%

CSR to VC = $(-0.752)^2$ X 100% = 56.55%

GCG to CP = $(0.25)^2$ X 100% = 6.25%

GCG to VC = $(-0.167)^2$ X 100% = 2.79%

CP to VC = $(-0.93)^2$ X 100% = 86.49%

The calculation of the overall total effect is taking account into both direct and indirect variables. As concluded in the results, the strongest absolute effect is the relationship between corporate profitability and value creation, which is 86.49% as compared to other variables. Meanwhile, the relationship between corporate governance and value creation holds the weakest effect as compared to other variables of only 2.79%. The correlation between CSR to profitability is 65.12% which is higher than if corporate governance act as the mediating variable. This result is found when adding the result of CSR to corporate governance of 10.24% and corporate governance to profitability 6.25%, which comes out with 16.49% value. Thus, it can be concluded that the indirect effect does not exist between those two variables and corporate governance does not mediate the relationship between CSR and profitability. In addition, looking at the corporate governance as the mediating variable for CSR and VC relationship, there is also no indirect effect exists. This is concluded from the value of CSR to value creation of 56.55%. The value is higher than the sum of CSR to corporate governance 10.24% and corporate governance to value creation 2.79%, summed up to 13.03%. Thus, indirect effect does not exist when corporate governance mediates the second the relationship. In conclusion corporate governance do not have indirect effect for both of the relationship when it mediates the relationship between CSR to profitability and CSR to value creation.

5. Conclusion, Contribution and Implication

The objective of doing this research paper is to analyze the impact of corporate social responsibility (CSR) policies towards profitability and value creation, as well as whether the corporate governance (CG) is able to become the mediation variable to the relationship. The analysis shows a significant positive relationship between CSR and profitability. Our contribution to this study has been provide that higher CSR practices and corporate governance is associated with higher profitability obtained by the company as proposed in H1 and H2. This result could also mean that consumers are not only concerning about the products they consume and but also the company which produces it. Thus, companies with higher CSR practices could lead to increase in sales and profit. Besides, good corporate governance makes the company is working more efficient and effectively, which reduces cost or increasing margin, resulted in profitability increases. Companies having good corporate governance ensures that companies are run in as socially responsible way and there should be a lucidly ethical basis to the business complying with the accepted norms of the society in which it is operating. Hence, CSR actively seeks a greater balance or compatibility between profit and ethics, which is consistent with corporate governance mechanism, proven in H3.

However, profitability has negative effect on value creation measured. Unless profits provide the increased funding, the firm has to decrease its dividends or increase its debt level. Both are negatively perceived by the markets and usually result in share price drop, eventually destroying shareholder value. This finding showed that for some

Indonesia companies that listed in Corporate Governance Perception Index (CGPI), CSR practices level still not able to create long-term performance in term of EVA.

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Journal: Investment Management and Financial Innovations

Manuscript title: CSR Policies and Value Creation: Does GCG and Corporate Profitability Mediate That Relationship?

Authors Information

Author - Correspondent

First Name: Josua

Last Name: Tarigan

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Degree: Dr

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Department: Accounting

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Co-Author’s ORCID: N/A

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Co-Author’s ORCID: N/A

Co-Author’s Researcher ID: N/A

Kind regards,

undefined

Corporate Social Responsibility Policies and Value Creation: Does Corporate Governance and Profitability Mediate That Relationship?

ABSTRACT

With a purpose to give a deep understanding relating to the manifestation of social responsibilities practices among Indonesian companies, this paper reflects the relationship of corporate social responsibility (CSR), corporate profitability (CP), value creation (VC) and good corporate governance (GCG). Kinder, Lydenberg, and Domini's (KLD) measurement approach is used in this study to measure the social responsibility practices as this gives cross-border analysis of social responsibility. Corporate Profitability captures return on assets which is accounting-based measurement, whereas value creation explains the economic value added which is shareholder-based measurement. Structural Equation Model (SEM) analysis is conducted for Indonesian listed companies which appeared in Corporate Governance Perception Index (CGPI). The empirical result suggests that CSR serves as a tool in assisting shareholders value and performance. Accordingly, firms should incorporate CSR practices to enhanced its strategic investment and sustain a strong relationship with its stakeholders. Subsequently, management should also take concern of having good corporate governance in order to improve company's performance by supervising and monitoring of the company's operation, ensure the fulfillment to the stakeholder's interest.

Keywords *Kinder Lydenberg and Domini's, Economic Value Added, Return on Assets, Corporate Governance Perception Index.*

JEL Classification: M4, Q5, G3

1. Introduction

In the traditional perspective, it is believed that business objective is to maximize the shareholder's wealth. However, as business grows, society come up with different perspective on how organization should operates. In this case, companies should shift from the mindset of enriching only shareholders to focusing on all the stakeholders, including environmental sustainability and community welfare. It is also becoming more important for companies to fulfill the environmental expectation in order to gain its reputation which further influence the firm's performance (Vargas, 2016).

Corporate social responsibility is considered to relate to corporate governance as governance is positively associated with the environmental strength of a firm (Stuebs and Sun, 2010). Not only that, previous study describes that good corporate governance could not able to increase reputation and performance of the company without also doing social responsibility practices (Chalise, 2014). Recent studies have also analysed the relationship of CSR and corporate governance from environmental performance perspective. The result shows a positive correlation on the study (Stuebs and Sun, 2010). This is because Corporate governance highlights the framework to form an environment which are transparent, accountable and trusted. It also refers to how companies are being directed and controlled to avoid disputes between agents and investors and ensure that funds managed by agents are used accordingly (Detthamrong, Chancharat & Vithessonthi, 2017).

However, looking at the enforcement of CSR in Indonesia, this has been just a voluntary disclosure for many years. Meanwhile, starting from July 2007, Indonesian government has enforced a new regulation regarding CSR practices disclosure for natural resources companies. Thus, CSR practices has not been engaged by a number of companies in Indonesia. Therefore, based on the importance of the variables, this study is the aims to analyse the relationship of CSR policies and company's performance using corporate governance (CG) as intervening variable. Hereinafter, this is the first study that attempts to give a deeper analyses regarding implementation of CSR practices. Insights obtained from this study may contribute to both theories and real practices of CSR policies. It could be done to improve the CSR understanding and management literature, as well as answering questions by different individuals or corporates regarding CSR, CG and firm's performance.

2. Literature review and hypothesis

2.1 Corporate social responsibility and corporate profitability

Many studies have been done to analyse the effect of CSR, including towards company's profitability. Corporates' profitability refers to the analysis of the ability of company to generate income. In this study, return on assets (ROA) is used to analyze the overall effectiveness of company's ability to generate profit with its assets (Gitman & Zutter, 2012). Since customers may have different perspectives on the implementation of CSR policies, CSR becomes an important element to build and maintain corporate's reputation and profitability, as well as to increase competitive advantage of the company (Park, 2017; Devie et al, 2019). Hence, companies that intend to enhance their reputation should focus on providing products with better quality that is able to satisfy their customers (Park et al, 2014). Therefore, good social reputation will lead to increase of sales, especially to customers that are sensitive to social and environmental issues, thus increase corporate profits (Khojastehpour & Johns, 2014). Profitable and large firms are also found to have a higher CSR disclosure in their reports (Muttakin, Khan & Subramaniam, 2015). Moreover, there have been several studies done worldwide to analyse the impact of CSR on different company's outcome including profitability. Yet, many have questioned as to whether the CSR implemented that incurred costs has created more benefits to it. However, this relationship between CSR and CP still creates confusion and different results especially inconsistency between develop and developing countries. Among all the previous studies explained in the summary table of previous researches, the positive relationship between CSR and corporate profitability can be mostly seen and found (LaGore, Mahoney & Thorne, 2013; Yu and Choi, 2014; Cheung, 2010). Thus, this research study comes up with the following hypothesis.

H1: CSR policies has a positive impact on corporate profitability

2.2 Good Corporate Governance to corporate's profitability

The practice of companies' corporate governance creates a system for directing, monitoring and supervising the entire resources of the company efficiently and effectively (Jackling and Johl, 2009). Corporate governance is established to maintain the various interests of company's stakeholders that may provide benefits for the company. A company with a high Corporate Governance Perception Index (CGPI) indicates that it is managed with transparency, accountability, responsibility, independency and fairness. Therefore, the impact can be seen on the outputs of good corporate performance, such as ROA, ROE and EPS (Gompers et al, 2003). Some previous studies using the same governance index, found that companies with stronger stakeholder rights tend to have higher profits. Sheikh et al. (2013) also found a positive relationship between board size and company performance.

H2: GCG has a positive impact on corporate profitability.

2.3 Corporate social responsibility and Good Corporate Governance

Corporate social responsibility (CSR) is currently a critical element of companies and their stakeholders and continues to gain attention atop the corporate strategy. Previous study discloses that higher commitments to CSR strongly and positively explain the qualifications and terms of directors, boards that put forth strong stewardship and strategic leadership roles, and the management of capital market pressures, and that these various attributes combined compose the hallmarks of good corporate governance (Lock & Seele, 2015). Hence, CSR actively searches for a greater balance or compatibility between profit and ethics, which is consistent with corporate governance mechanism. Besides, corporate social responsibility is considered related to corporate governance as governance is positively related to environmental strengths of a firm (Stuebs and Sun, 2010). Moreover previous study shows that good corporate governance could not increase reputation of the company without social responsibility practices (Chalise, 2014). Recent studies have also analysed the relationship between CSR and corporate governance from environmental performance perspective. The result showed a positive correlation between CSR and corporate governance (Stuebs and Sun, 2010). In this case the documentation of CSR performance of a firm has given benefits to support the corporate governance improvement effort of a company.

H3: CSR policies has a positive impact on good corporate governance.

2.4 Corporate profitability and value creation

In the recent years, the influence of profitability or performance on firm value has gained much attention in many studies. In the competitive environment, companies are trying their best to sustain in the industry by optimizing their cost in order to gain more profit for their operations. Besides, management starts to concern about its investment plans to maximize shareholder's wealth and firm value (Chen, 2011). Understanding the relationship of profitability and value creation is also important to financial decision making of the firm. Some researches have also proven the positive correlation between profitability and firm value (AlNajjar & Belkaoui, 1999; Crisóstomo et al, 2011; Osazuwa & Che-Ahmad, 2016). It was proven that as the firm profit got greater, more earnings would be distributable to shareholders. This is also in line with the agency theory about the management ability in managing assets in order to maximize profit, creating shareholder's trust to company's quality of management. Thus, the higher the financial performance, the higher the value of the company.

H4: CP has a positive impact on Value creation

2.5 Corporate social responsibility and value creation

A new method to measure firm's performance through value creation, is known as economic value added (EVA). EVA is relevant for measuring the firm's performance as this tells us how much the companies have created wealth for the stakeholders and how efficient the management has utilized the capital from the stakeholders. It is also known as economic profit, which is believed to be a special way of measuring profit. This is because EVA is measured taking account into all the opportunity or cost of the capital invested in the business (Steward, 2014). Relating to CSR, CSR strategies need to be developed in order to have a proper CSR policy that is essential to satisfy the firm's goals. It is crucial to pay more attention to actives that may add scores to company's value. If the company is showing a positive VC, this also means that the company is working align with the corporate social responsibility. Besides, CSR creates value to the firm as the firm could be able to differentiate them from the competitors and also to reduce its costs. As the firm is having adequate management, this creates also value for the business and society. This shows the positive correlation between the company investment in CSR and the value creation of the firm (Green & Peloza, 2011). Likewise, there was also found to be a positive relationship between CSR and share price among companies in UK, especially those with an environmentally sensitive industry such as electricity, mining, and gas. Accordingly, the second hypothesis made for this research study is:

H5: CSR policies has a positive impact on value creation.

2.6 Good Corporate Governance and Value Creation

Corporate governance includes making sure that shareholders wealth as well as the other stakeholders are being taken into account in the management operation. This is also to prevent the corporate fraud and illegal accounting measure. Thus, value creation should be considered as to have a good corporate governance. Previous studies have found that significant corporate governance effect the greater shareholder's rights which by higher profit, sales growth and firm value (Gompers, Ishii, & Metrick, 2003). Some other researches are also showing different result for companies that implement good corporate governance in developed, developing and underdeveloped countries. Positive relations are found between good corporate governance practices with company's value (Klapper and Love, 2002; Black, Jang, and Kim, 2006).

H6: GCG has a positive impact on value creation.

2.7 Corporate social responsibility, good corporate governance and corporate profitability

The stakeholder theory defines that companies should do CSR practices as to fulfil their responsibility to stakeholders and able to maximize financial strength of the company. Supporting this, the corporate governance is describing as the intervening variable, strengthening the relationship of CSR and Corporate Profitability (CP). Besides, companies should have good corporate governance in addition to implementation of CSR practices, in order to give positive impact to the performance. This is because the importance of corporate governance take concern the welfare of all stakeholders, not only shareholder. Previous researchers also found positive relationship between CSR and performance (Salama, Anderson and Toms, 2018; El Ghoul et al., 2011; Lourenco et al., 2011). In addition to this, some also did research on the potential impact on CSR practices on firm's sustainability and resulted in corporate governance positively effecting CSR disclosure (Li et al., 2010)

H7: GCG could mediate the relationship between CSR policies and corporate profitability

2.8 Corporate social responsibility, good corporate governance and value creation

CSR could be considered as activities that create values for improving the firm's reputation, which further lead to improvement of economic performance of the company. CSR not only creates financial benefit to the company, but also strategic advantage. By engaging in social responsibility practices, firms can gain trust and goodwill from stakeholders, which is also a competitive advantage (Kolk and Pinkse, 2010). Research suggested that CSR activities would enhanced firm's image and reputation (Vanhamme et al., 2012). CSR policies help in increasing the company's value and satisfy its goals. Companies doing CSR practices creates positive Value Creation (VC) for the company. EVA which is a measurement of value created or lost is used to measure the performance and value creation made within the company. There is no previous research done regarding the relationship of CSR policies and value creation through GCG as intervening variable.

H8: GCG could mediate the relationship between CSR policies and value creation.

3. Research methodology

3.1 Sample

For the analysis of this study, as Structural Equation Model (SEM) is used. This model analysis covers gathering of secondary data, testing of hypothesis and evaluation of variable correlations. The sample of the study involves firms that are consistently listed as having good corporate governance by SWA-Magazine and Indonesia Institute for Corporate Governance (IICG) in 2016 and 2017. This study makes use of secondary data, including annual report, Bloomberg terminal and company's website.

Table I Summary of the sample observed

Sampling Criteria	*No. of Companies*
Companies listed in CGPI in the year 2016 and 2017 by SWA Magazine and IICG	39
Companies that were not consistently listed as having GCG in year 2016 and 2017	(13)
Companies that do not publish complete annual report in the required period	(10)
Number of companies which fulfill the criteria	16
Total sample used in the research (16 x 2)	32 firm-year

From the population of 39 companies included in the Corporate Governance Perception Index (CGPI) in 2016 and 2017, there are 23 companies that were not included for this research as the companies did not fulfilled the requirement of the research. It was those companies not consistently listed in CGPI and not publishing a complete annual report in the required period. Hence, there are 16 companies which fulfil the criteria and was the number of the companies observed. All samples that is used in the research are 32 reports derived from 16 companies multiplied by 2 years of observation.

3.2 Measures

Corporate Social Responsibility (CSR)

CSR policies is measured using Kinder, Lydenberg, and Domini's (KLD) method, chosen as a basic of CSR level. This measurement has been widely used in previous leading management journals (Nguyen and Nguyen, 2015; Li et al, 2010; Jo and Na, 2012; Devie et al, 2019). KLD provides benchmarking in 5 areas of CSR issue relevant to Indonesian companies, including diversity, community, environment, employee relation and products. In each of the KLD measurement, there are strengths and concerns. The strengths are considered to be positive CSR policies implemented, while concerns are as negative CSR policies implemented. If a company has a strength or even a concern, this would be given a “1” or “-1” On the other hand, companies without any would be indicated with a “0”. After scoring the 5 qualitative areas, the total score of strength and concerns should be calculated in order to get Net CSR.

Value Creation

EVA spread is used as the mesurement of value creation. EVA is a performance measurement to calculates the residual income from subtraction of additional charge from net operating profit after tax (Steward, 2014), which take into account cost of capital and cost of equity. EVA aims to figure out the economic profit of a company.

Corporate Profitability

Return on Asset (ROA) is used as the measurement of profitability. This is calculated by dividing net income by average total assets. ROA is also known as the overall effectiveness of company’s management in generating profits with its assets (Gitman & Zutter, 2012). ROA is widely used measurement of profitability in environmental studies (Nguyen & Nguyen, 2015; Park, 2017; Devie et al, 2019)

Good Corporate Governance

This research has been using GCG as the intervening variables. The GCG was measured using the measurement of Corporate Governance Perception Index (CGPI) that was published by IICG and SWA Magazine. This then had a scale of 0-100 values. CGPI score with the predicate "very trusted" for companies with scores of 85-100, "trusted" for companies with scores 70-84, and "quite reliable" for companies with a score of 55-69. The higher the score a company can get, the better the application of corporate governance is considered to be.

Table II Variable definitions and data source

Variable(s)	*Definitions*	*Data Source*
CSR Policies	Difference between total strengths score and total concerns score	Annual and Company’ Websites
Corporate Profitability (ROA)	Percentage of net income over total assets	Annual Report and Bloomberg terminal
Value Creation (EVA)	Total of Net Operating Profit After Tax divided by the invested capital deducted by the weighted average of cost of capital	Bloomberg
Good Corporate Governance	Score of good corporate governance by SWA Magazine and IICG	SWA Magazine

3.3. Model

This study helps to analyze the relationship of CSR to Firm’s performance in a positive, negative or neutral way as well as the role of corporate governance (CG) as intervening variable that alters financial performance. A multivariate statistical model is used through validity, reliability, and collinearity tests (Kock, 2015). Validity test consists of convergent validity and discriminant validity test for each of the indicator.

Table III Combined loadings and cross-loadings

Indicator	CSR	GCG	CP	VC	P value
CSR	1.00	0.00	0.00	0.00	<0.001
CG	0.00	1.00	0.00	0.00	<0.001
ROA	0.00	0.00	1.00	0.00	<0.001
EVA	0.00	0.00	0.00	1.00	<0.001

The table above shows that all the factor loading value of each indicators are all above 0.5. These value means that all indicators of CSR, CG, ROA and EVA which were used to measure all the variables have fulfilled the convergent validity test.

The following table shows discriminant validity. The discriminant validity is to compare the square root of average variance extracted (AVE) of each latent variable with the correlation between latent variables. If the square root of AVE of one indicator is larger than the other coefficient correlations in one parallel row of column, then the validity is fulfilled. The result of the discriminant validity is explained in the table below.

Table IV AVE table

Indicator	CSR	GCG	CP	VC
CSR	1.00	0.010	0.717	-0.061
CG	0.010	1.00	0.157	-0.149
ROA	0.717	0.157	1.00	-0.642
EVA	-0.061	-0.149	-0.642	1.00

From the table above, the square root AVE shows a figure of 1.00 for all results. These are also bigger than the coefficient correlation of the other variables.

Composite Reliability, Cronbach's Alpha and Collinearity

From the composite reliability test, all the variables have the value of 1.00, therefore composite reliability criteria are fulfilled. Not only that, result also has the Cronbach's Alpha value of more than 0.6, which is 1.00 for all the variables. Thus, all the variables have been fulfilled the criteria of reliability.

Table V Collinearity table

	CSR	GCG	CP	CV
R^2		0.099	0.817	0.864
Adj. R^2		0.069	0.805	0.850
Full collinearity VIFs	3.24	1.054	3.149	3.188

In order to fulfill the collinearity test, VIFs must be lesser than 3.3 or 10 in a more relaxed criterion (Kock, 2015). According in Table V, all variables have passed the multicollinearity tests.

4 Research results and analysis

4.1 Descriptive analysis

Descriptive analysis is done through looking at the statistics of coefficients which combined up as the data set, either in form of population as a whole or a sample as a part of the population. This explains the overview of the research data as a whole, which includes the total number of data used, minimum and maximum value, mean and standard deviation.

Table VI Descriptive Statistics

Indicators	Minimum	Maximum	Mean	STDEV
CSR	6.00	13.00	8.78	1.81
CG	72.68	93.32	84.92	5.32
ROA	-45.60	22.07	1.30	10.51
EVA	-7.17	94.57	5.31	17.67

Comparing the range to the CSR policies mean result in this research, the companies that are listed in Corporate Governance Perception Index (CGPI) and used in this research, are presumably quite well. Besides, the profile GCG for its weighted average of 2016 and 2017 shows that GCG has one indicator with minimum and maximum value of 72.68 and 93.32. The samples in this research are those companies consistently listed as having a good corporate governance. It means that the companies show good performance and are considered as trusted companies, which lies within the range of 70-84. Besides, the mean value of the GCG score is 84.92 which categorized as "most trusted companies", lies within 85-100. Thus, it indicates that companies begin to be concerned about their corporate governance.

4.2 Hypothesis Test (Direct, Intervening and Total effects)

The hypothesis test done by using the T-test and re-sampling. The hypothesis test divided into 3 parts of direct effect, mediation variable and the total effect of the variables in this research.

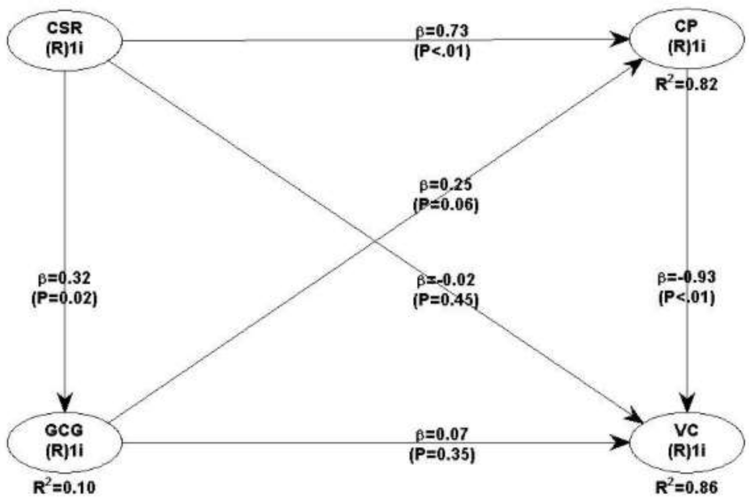

Figure I Structural model result

4.2.1 Direct Effect

Table VII Path Coefficient and P values

Independent / Control variable	Dependent Variable	Path Coefficient	P-value	Note
CSR	CP	0.73	<0.01	Highly significant
CSR	Value creation	-0.02	0.45	Insignificant
CSR	GCG	0.32	0.02	Significant
GCG	CP	0.25	0.06	Weakly significant
GCG	Value creation	0.07	0.35	Insignificant
Profitability	Value creation	-0.93	<0.01	Highly significant

Figure 1 and table VII show that corporate social responsibility policies affect corporate governance with the coefficient value of 0.32 and p value 0.02, and it also gives effect on corporate profitability with 0.73 coefficient value and p<0.01. In other words, the higher score of CSR policies will increase the profitability of the company (ROA), supported by the p value of lower than 5% significant level of both. This also means that **hypothesis 1** is accepted since the relationship between CSR policies and profitability shows a positive and highly significant direct relationship, hence **hypothesis 3** is also accepted as the CSR has a direct positive relationship with good corporate governance. The first hypothesis result is in line with the stakeholder theory that when firms put CSR practices into consideration, they will read a better performance (Yu and Choi, 2014). On the other hand, the acceptance of the hypothesis 3 is in line with the believe that higher commitments of CSR could strongly impact on the qualifications of directors and other members of the company which combined into a good corporate governance hallmark. Besides, good corporate governance may not able to increase reputation of the company without also taking care of the socially responsibility practices in the company (Chalise, 2014). Moreover, good corporate governance is showing a positive correlation of 0.25 and p=0.06, which is deemed to be weakly significant. Thus, **hypothesis 2** explains the relationship between GCG and profitability that is positive but weakly significant, and acceptable. This means that when companies are directed and controlled properly, the company could be more efficient in the work and operation which then result in better performance. In this case, an increase on efficiency of the work will impact the profit of the company (Sheikh et al, 2013).

Furthermore, the relationship of CSR Policies to value creation shows a value of -0.02 with p=0.45, which means that a higher score of CSR policies, the value of the firm will decrease and this is insignificant. Therefore, the **hypothesis 5** is rejected. This is supported by the theory that CSR practices could create long-term value for the company's financial performance instead of giving short-term impact (Gregory, Tharyan & Christidis, 2011). Moreover, the data also describes there is an insignificant effect of good corporate governance on value creation of 0.07 and p=0.35. This means that there is an insignificant positive relationship between the two variables, so **hypothesis 6** is rejected. It possibly happens because corporate governance implementation in a company can not directly influence the firm's value, but it takes some time. Likewise, the relationship between profitability and value creation shows a negative 0.93 with p<0.01. This means that profitability doesn't give a rise to value creation as it increases. Thus, **hypothesis 4** is also rejected. If profit does not provide an increase on funding of the company, the firm still has to decrease its dividends or choose to increase its debt level for the funding. Both of them give negative impact to the markets and usually result in a decrease of share price and destroy the shareholder's value.

4.3.2. Intervening Effect

The table below shows the indirect effect and P values of intervening variables.

Table VIII Indirect Effect and P values

Independent variable	Intervening variable	Dependent variable	Path coefficient	P value
CSR	CP GCG	VC	-0.657	<0.001
CSR	GCG	CP	0.079	0.258
GCG	CP	VC	-0.233	0.023

Looking at the table above, the p value of CSR towards corporate's profitability with good corporate governance as the mediating variable is 0.258. This figure shows a big percentage which is more than 5% significance, thus this is considered to be insignificant. It can be concluded that good corporate governance fails to act as a mediating variable, therefore **hypothesis 7 is rejected.** Additionaly, **hypothesis 8 is also rejected**, since the mediating variables shows a significant value of 0.023 (<0.05) with path coefficient for this is at -0.233. Hence, corporate profitability mediates the good corporate governance and value creation but negatively.

4.3.3. Total Effect

The total effect refers to the p values for all variables included in the research. This includes all the direct and indirect effect and being discussed further below:

Table IX Total Effect and P Values

	CSR	GCG	CP	VC
CSR	-	-	-	-
GCG	0.32 (=0.023)	-	-	-

CP	0.807 (<0.001)	0.25 (=0.06)	-	-
VC	-0.752 (<0.001)	-0.167 (=0.158)	-0.93 (<0.001)	-

The detailed calculation of the absolute contribution between variables is discussed below:

CSR to GCG	$= (0.32)^2 \times 100\%$	= 10.24%
CSR to CP	$= (0.807)^2 \times 100\%$	= 65.12%
CSR to VC	$= (-0.752)^2 \times 100\%$	= 56.55%
GCG to CP	$= (0.25)^2 \times 100\%$	= 6.25%
GCG to VC	$= (-0.167)^2 \times 100\%$	= 2.79%
CP to VC	$= (-0.93)^2 \times 100\%$	= 86.49%

The calculation of the overall total effect is taking account into both direct and indirect variables. As concluded in the results, the strongest absolute effect is the relationship between corporate profitability and value creation, which is 86.49% as compared to other variables. Meanwhile, the relationship between corporate governance and value creation holds the weakest effect as compared to other variables of only 2.79%. The correlation between CSR to profitability is 65.12% which is higher than if corporate governance acts as the mediating variable. This result is found when adding the result of CSR to corporate governance of 10.24% and corporate governance to profitability 6.25%, which comes out with 16.49% value. Thus, it can be concluded that the indirect effect does not exist between those two variables and corporate governance does not mediate the relationship between CSR and profitability. In addition, looking at the corporate governance as the mediating variable for CSR and VC relationship, there is also no indirect effect. This is concluded from the value of CSR to value creation of 56.55%. The value is higher than the sum of CSR to corporate governance 10.24% and corporate governance to value creation 2.79%, summed up to 13.03%. Thus, indirect effect does not exist when corporate governance mediates the second the relationship. In conclusion corporate governance does not have indirect effect for both of the relationship when it mediates the relationship between CSR to profitability and CSR to value creation.

5. Conclusion, Contribution and Implication

The objective of doing this research paper is to analyze the impact of corporate social responsibility (CSR) policies towards profitability and value creation, as well as whether the corporate governance (CG) is able to become the mediation variable to the relationship. The analysis shows a significantly positive relationship between CSR and profitability. Our contribution to this study is that higher CSR practices and corporate governance is associated with higher profitability obtained by the company as proposed in H1 and H2. This result indicates that consumers are not only concerned about the products they consume but also the manufacturers. Thus, companies with higher CSR practices could lead to increase in sales and profit. Besides, good corporate governance makes the company work more efficiently and effectively, which reduces cost or increasing margin and increases profitability. Companies with good corporate governance ensure a socially responsible way of how the companies are run and a lucidly ethical basis for complying with the accepted norms of the society where they operate. Hence, CSR actively seeks a greater balance or compatibility between profit and ethics, which is consistent with corporate governance mechanism (H3).

However, profitability has negative effect on the value creation measured. Unless profits provide the increased funding, the firm has to decrease its dividends or increase its debt level. Both are negatively perceived by the markets and usually result in share price drop, eventually destroying shareholder value. It means that for some

Indonesian companies listed in Corporate Governance Perception Index (CGPI), the CSR practice level still can not create long-term performance in terms of EVA.

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Josua Tarigan <josuat@petra.ac.id>

MA299: Notification on Submission

1 message

o.vorozhko@manuscript-adminsystem.com <o.vorozhko@manuscript-adminsystem.com> Tue, Mar 5, 2019 at 5:09 PM
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To: Josua Tarigan <josuat@petra.ac.id>
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Sent: Friday, February 15, 2019 10:16 AM
To: o.vorozhko@manuscript-adminsystem.com
Subject: Re: MA299: Notification on Submission

Dear Editor,

the revised reference list and also cover letter was uploaded.

thanks

--

Josua Tarigan, PhD, CMA, CFP, CSRA, CIBA, CBV

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To: Olga Vorozhko <o.vorozhko@manuscript-adminsystem.com>
Cc: Saarce Elsye Hatane <elsyehat@petra.ac.id>

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Corporate Social Responsibility Policies and Value Creation: Does Corporate Governance and Profitability Mediate That Relationship?

ABSTRACT

With a purpose to give a deep understanding relating to the manifestation of social responsibilities practices among Indonesian companies, this paper reflects the relationship of corporate social responsibility (CSR), corporate profitability (CP), value creation (VC) and good corporate governance (GCG). Kinder, Lydenberg, and Domini's (KLD) measurement approach is used in this study to measure the social responsibility practices as this gives cross-border analysis of social responsibility. Corporate Profitability captures return on assets which is accounting-based measurement, whereas value creation explains the economic value added which is shareholder-based measurement. Structural Equation Model (SEM) analysis is conducted for Indonesian listed companies which appeared in Corporate Governance Perception Index (CGPI). The empirical result suggests that CSR serves as a tool in assisting shareholders value and performance. Accordingly, firms should incorporate CSR practices to enhanced its strategic investment and sustain a strong relationship with its stakeholders. Subsequently, management should also take concern of having good corporate governance in order to improve company's performance by supervising and monitoring of the company's operation, ensure the fulfillment to the stakeholder's interest.

Keywords *Kinder Lydenberg and Domini's, Economic Value Added, Return on Assets, Corporate Governance Perception Index.*

JEL Classification: M4, Q5, G3

1. Introduction

In the traditional perspective, it is believed that business objective is to maximize the shareholder's wealth. However, as business grows, society come up with different perspective on how organization should operates. In this case, companies should shift from the mindset of enriching only shareholders to focusing on all the stakeholders, including environmental sustainability and community welfare. It is also becoming more important for companies to fulfill the environmental expectation in order to gain its reputation which further influence the firm's performance (Vargas, 2016).

Corporate social responsibility is considered to relate to corporate governance as governance is positively associated with the environmental strength of a firm (Stuebs and Sun, 2010). Not only that, previous study describes that good corporate governance could not able to increase reputation and performance of the company without also doing social responsibility practices (Chalise, 2014). Recent studies have also analysed the relationship of CSR and corporate governance from environmental performance perspective. The result shows a positive correlation on the study (Stuebs and Sun, 2010). This is because Corporate governance highlights the framework to form an environment which are transparent, accountable and trusted. It also refers to how companies are being directed and controlled to avoid disputes between agents and investors and ensure that funds managed by agents are used accordingly (Detthamrong, Chancharat & Vithessonthi, 2017).

However, looking at the enforcement of CSR in Indonesia, this has been just a voluntary disclosure for many years. Meanwhile, starting from July 2007, Indonesian government has enforced a new regulation regarding CSR practices disclosure for natural resources companies. Thus, CSR practices has not been engaged by a number of companies in Indonesia. Therefore, based on the importance of the variables, this study is the aims to analyse the relationship of CSR policies and company's performance using corporate governance (CG) as intervening variable. Hereinafter, this is the first study that attempts to give a deeper analyses regarding implementation of CSR practices. Insights obtained from this study may contribute to both theories and real practices of CSR policies. It could be done to improve the CSR understanding and management literature, as well as answering questions by different individuals or corporates regarding CSR, CG and firm's performance.

2. Literature review and hypothesis

2.1 Corporate social responsibility and corporate profitability

Many studies have been done to analyse the effect of CSR, including towards company's profitability. Corporates' profitability refers to the analysis of the ability of company to generate income. In this study, return on assets (ROA) is used to analyze the overall effectiveness of company's ability to generate profit with its assets (Gitman & Zutter, 2012). Since customers may have different perspectives on the implementation of CSR policies, CSR becomes an important element to build and maintain corporate's reputation and profitability, as well as to increase competitive advantage of the company (Park, 2017; Devie et al, 2019). Hence, companies that intend to enhance their reputation should focus on providing products with better quality that is able to satisfy their customers (Park et al, 2014). Therefore, good social reputation will lead to increase of sales, especially to customers that are sensitive to social and environmental issues, thus increase corporate profits (Khojastehpour & Johns, 2014). Profitable and large firms are also found to have a higher CSR disclosure in their reports (Muttakin, Khan & Subramaniam, 2015). Moreover, there have been several studies done worldwide to analyse the impact of CSR on different company's outcome including profitability. Yet, many have questioned as to whether the CSR implemented that incurred costs has created more benefits to it. However, this relationship between CSR and CP still creates confusion and different results especially inconsistency between develop and developing countries. Among all the previous studies explained in the summary table of previous researches, the positive relationship between CSR and corporate profitability can be mostly seen and found (LaGore, Mahoney & Thorne, 2013; Yu and Choi, 2014; Cheung, 2010). Thus, this research study comes up with the following hypothesis.

H1: CSR policies has a positive impact on corporate profitability

2.2 Good Corporate Governance to corporate's profitability

The practice of companies' corporate governance creates a system for managing, monitoring and overseeing the whole resources of the company cost-effectively and functionally (Jackling and Johl, 2009). Corporate governance is established to preserve the different interests of company's stakeholders that could give advantages for the company. A company with a highly elevated Corporate Governance Perception Index (CGPI) indicates that it is managed with lucidity, responsibility, accountability, equity and independency. Consequently, the impact can be seen on the results of good corporate performance, such as ROE, ROA and EPS (Gompers et al, 2003). Some previous studies using similar governance index, discovered that companies with more powerful stakeholder rights are likely to produce higher profits. Sheikh et al. (2013) also discovered a positive association between company performance and board size.

H2: GCG has a positive impact on corporate profitability.

2.3 Corporate social responsibility and Good Corporate Governance

Corporate social responsibility (CSR) is recently a critical component of companies and their stakeholders and persists to gain attention on the top of the corporate strategy. Previous study discloses that stronger commitments to CSR significantly and positively explain the prerequisites and provisions of directors, boards that put forth strong stewardship and strategic leadership roles, and the management of capital market hassles, and that these different features combined compose the distinguishing characteristics of good corporate governance (Lock & Seele, 2015). Hence, CSR actively searches for a larger equilibrium or consistency between profit and ethics, which is consistent with corporate governance mechanism. Besides, corporate social responsibility is considered related to corporate governance as governance is positively related to environmental strengths of a firm (Stuebs and Sun, 2010). Moreover previous study shows that good corporate governance could not increase reputation of the company without social responsibility practices (Chalise, 2014). Recent studies have also analysed the relationship between CSR and corporate governance from environmental performance perspective. The result showed a positive correlation between CSR and corporate governance (Stuebs and Sun, 2010). In this case the documentation of CSR performance of a firm has given benefits to support the corporate governance improvement effort of a company.

H3: CSR policies has a positive impact on good corporate governance.

2.4 Corporate profitability and value creation

In the recent years, the influence of profitability or performance on firm value has gained much attention in many studies. In the competitive environment, companies are trying their best to sustain in the industry by optimizing their cost in order to gain more profit for their operations. Besides, management starts to concern about its investment plans to maximize shareholder's wealth and firm value (Chen, 2011). Understanding the relationship of profitability and value creation is also important to financial decision making of the firm. Some researches have also proven the positive correlation between profitability and firm value (AlNajjar & Belkaoui, 1999; Crisóstomo et al, 2011; Osazuwa & Che-Ahmad, 2016). It was proven that as the firm profit got greater, more earnings would be distributable to shareholders. This is also in line with the agency theory about the management ability in managing assets in order to maximize profit, creating shareholder's trust to company's quality of management. Thus, the higher the financial performance, the higher the value of the company.

H4: CP has a positive impact on Value creation

2.5 Corporate social responsibility and value creation

A new method to measure firm's performance through value creation, is known as economic value added (EVA). EVA is relevant for measuring the firm's performance as this tells us how much the companies have created wealth for the stakeholders and how efficient the management has utilized the capital from the stakeholders. It is also known as economic profit, which is believed to be a special way of measuring profit. This is because EVA is measured taking account into all the opportunity or cost of the capital invested in the business (Steward, 2014). Relating to CSR, CSR strategies need to be developed in order to have a proper CSR policy that is essential to satisfy the firm's goals. It is crucial to pay more attention to actives that may add scores to company's value. If the company is showing a positive VC, this also means that the company is working align with the corporate social responsibility. Besides, CSR creates value to the firm as the firm could be able to differentiate them from the competitors and also to reduce its costs. As the firm is having adequate management, this creates also value for the business and society. This shows the positive correlation between the company investment in CSR and the value creation of the firm (Green & Peloza, 2011). Likewise, there was also found to be a positive relationship between CSR and share price among companies in UK, especially those with an environmentally sensitive industry such as electricity, mining, and gas. Accordingly, the second hypothesis made for this research study is:

H5: CSR policies has a positive impact on value creation.

2.6 Good Corporate Governance and Value Creation

Corporate governance includes making sure that shareholders wealth as well as the other stakeholders are being taken into account in the management operation. This is also to prevent the corporate fraud and illegal accounting measure. Thus, value creation should be considered as to have a good corporate governance. Previous studies have found that significant corporate governance effect the greater shareholder's rights which by higher profit, sales growth and firm value (Gompers, Ishii, & Metrick, 2003). Some other researches are also showing different result for companies that implement good corporate governance in developed, developing and underdeveloped countries. Positive relations are found between good corporate governance practices with company's value (Klapper and Love, 2002; Black, Jang, and Kim, 2006).

H6: GCG has a positive impact on value creation.

2.7 Corporate social responsibility, good corporate governance and corporate profitability

The stakeholder theory defines that companies should do CSR practices as to fulfil their responsibility to stakeholders and able to maximize financial strength of the company. Supporting this, the corporate governance is describing as the intervening variable, strengthening the relationship of CSR and Corporate Profitability (CP). Besides, companies should have good corporate governance in addition to implementation of CSR practices, in order to give positive impact to the performance. This is because the importance of corporate governance take concern the welfare of all stakeholders, not only shareholder. Previous researchers also found positive relationship between CSR and performance (Salama, Anderson and Toms, 2018; El Ghoul et al., 2011; Lourenco et al., 2011). In addition to this, some also did research on the potential impact on CSR practices on firm's sustainability and resulted in corporate governance positively effecting CSR disclosure (Li et al., 2010)

H7: GCG could mediate the relationship between CSR policies and corporate profitability

2.8 Corporate social responsibility, good corporate governance and value creation

CSR could be considered as activities that create values for improving the firm's reputation, which further lead to improvement of economic performance of the company. CSR not only creates financial benefit to the company, but also strategic advantage. By engaging in social responsibility practices, firms can gain trust and goodwill from stakeholders, which is also a competitive advantage (Kolk and Pinkse, 2010). Research suggested that CSR activities would enhanced firm's image and reputation (Vanhamme et al., 2012). CSR policies help in increasing the company's value and satisfy its goals. Companies doing CSR practices creates positive Value Creation (VC) for the company. EVA which is a measurement of value created or lost is used to measure the performance and value creation made within the company. There is no previous research done regarding the relationship of CSR policies and value creation through GCG as intervening variable.

H8: GCG could mediate the relationship between CSR policies and value creation.

3. Research methodology

3.1 Sample

For the analysis of this study, as Structural Equation Model (SEM) is used. This model analysis covers gathering of secondary data, testing of hypothesis and evaluation of variable correlations. The sample of the study involves firms that are consistently listed as having good corporate governance by SWA-Magazine and Indonesia Institute for Corporate Governance (IICG) in 2016 and 2017. This study makes use of secondary data, including annual report, Bloomberg terminal and company's website.

Table I Summary of the sample observed

Sampling Criteria	*No. of Companies*
Companies listed in CGPI in the year 2016 and 2017 by SWA Magazine and IICG	39
Companies that were not consistently listed as having GCG in year 2016 and 2017	(13)
Companies that do not publish complete annual report in the required period	(10)
Number of companies which fulfill the criteria	16
Total sample used in the research (16 x 2)	32 firm-year

From the population of 39 companies included in the Corporate Governance Perception Index (CGPI) in 2016 and 2017, there are 23 companies that were not included for this research as the companies did not fulfilled the requirement of the research. It was those companies not consistently listed in CGPI and not publishing a complete annual report in the required period. Hence, there are 16 companies which fulfil the criteria and was the number of the companies observed. All samples that is used in the research are 32 reports derived from 16 companies multiplied by 2 years of observation.

3.2 Measures

Corporate Social Responsibility (CSR)

CSR policies is measured using Kinder, Lydenberg, and Domini's (KLD) method, chosen as a basic of CSR level. This measurement has been widely used in previous leading management journals (Nguyen and Nguyen, 2015; Li et al, 2010; Jo and Na, 2012; Devie et al, 2019). KLD provides benchmarking in 5 areas of CSR issue relevant to Indonesian companies, including diversity, community, environment, employee relation and products. In each of the KLD measurement, there are strengths and concerns. The strengths are considered to be positive CSR policies implemented, while concerns are as negative CSR policies implemented. If a company has a strength or even a concern, this would be given a "1" or "-1" On the other hand, companies without any would be indicated with a "0". After scoring the 5 qualitative areas, the total score of strength and concerns should be calculated in order to get Net CSR.

Value Creation

EVA spread is used as the mesurement of value creation. EVA is a performance measurement to calculates the residual income from subtraction of additional charge from net operating profit after tax (Steward, 2014), which take into account cost of capital and cost of equity. EVA aims to figure out the economic profit of a company.

Corporate Profitability

Return on Asset (ROA) is used as the measurement of profitability. This is calculated by dividing net income by average total assets. ROA is also known as the overall effectiveness of company's management in generating profits with its assets (Gitman & Zutter, 2012). ROA is widely used measurement of profitability in environmental studies (Nguyen & Nguyen, 2015; Park, 2017; Devie et al, 2019)

Good Corporate Governance

This research has been using GCG as the intervening variables. The GCG was measured using the measurement of Corporate Governance Perception Index (CGPI) that was published by IICG and SWA Magazine. This then had a scale of 0-100 values. CGPI score with the predicate "very trusted" for companies with scores of 85-100, "trusted" for companies with scores 70-84, and "quite reliable" for companies with a score of 55-69. The higher the score a company can get, the better the application of corporate governance is considered to be.

Table II Variable definitions and data source

Variable(s)	*Definitions*	*Data Source*
CSR Policies	Difference between total strengths score and total concerns score	Annual and Company' Websites
Corporate Profitability (ROA)	Percentage of net income over total assets	Annual Report and Bloomberg terminal
Value Creation (EVA)	Total of Net Operating Profit After Tax divided by the invested capital deducted by the weighted average of cost of capital	Bloomberg
Good Corporate Governance	Score of good corporate governance by SWA Magazine and IICG	SWA Magazine

3.3. Model

This study helps to analyze the relationship of CSR to Firm's performance in a positive, negative or neutral way as well as the role of corporate governance (CG) as intervening variable that alters financial performance. A multivariate statistical model is used through validity, reliability, and collinearity tests (Kock, 2015). Validity test consists of convergent validity and discriminant validity test for each of the indicator.

Table III Combined loadings and cross-loadings

Indicator	CSR	GCG	CP	VC	P value
CSR	1.00	0.00	0.00	0.00	<0.001
CG	0.00	1.00	0.00	0.00	<0.001
ROA	0.00	0.00	1.00	0.00	<0.001
EVA	0.00	0.00	0.00	1.00	<0.001

The table above shows that all the factor loading value of each indicators are all above 0.5. These value means that all indicators of CSR, CG, ROA and EVA which were used to measure all the variables have fulfilled the convergent validity test.

The following table shows discriminant validity. The discriminant validity is to compare the square root of average variance extracted (AVE) of each latent variable with the correlation between latent variables. If the square root of AVE of one indicator is larger than the other coefficient correlations in one parallel row of column, then the validity is fulfilled. The result of the discriminant validity is explained in the table below.

Table IV AVE table

Indicator	CSR	GCG	CP	VC
CSR	1.00	0.010	0.717	-0.061
CG	0.010	1.00	0.157	-0.149
ROA	0.717	0.157	1.00	-0.642
EVA	-0.061	-0.149	-0.642	1.00

From the table above, the square root AVE shows a figure of 1.00 for all results. These are also bigger than the coefficient correlation of the other variables.

Composite Reliability, Cronbach's Alpha and Collinearity

From the composite reliability test, all the variables have the value of 1.00, therefore composite reliability criteria are fulfilled. Not only that, result also has the Cronbach's Alpha value of more than 0.6, which is 1.00 for all the variables. Thus, all the variables have been fulfilled the criteria of reliability.

Table V Collinearity table

	CSR	GCG	CP	CV
R^2		0.099	0.817	0.864
Adj. R^2		0.069	0.805	0.850
Full collinearity VIFs	3.24	1.054	3.149	3.188

In order to fulfill the collinearity test, VIFs must be lesser than 3.3 or 10 in a more relaxed criterion (Kock, 2015). According in Table V, all variables have passed the multicollinearity tests.

4 Research results and analysis

4.1 Descriptive analysis

Descriptive analysis is done through looking at the statistics of coefficients which combined up as the data set, either in form of population as a whole or a sample as a part of the population. This explains the overview of the research data as a whole, which includes the total number of data used, minimum and maximum value, mean and standard deviation.

Table VI Descriptive Statistics

Indicators	Minimum	Maximum	Mean	STDEV
CSR	6.00	13.00	8.78	1.81
CG	72.68	93.32	84.92	5.32
ROA	-45.60	22.07	1.30	10.51

EVA	-7.17	94.57	5.31	17.67

Comparing the range to the CSR policies mean result in this research, the companies that are listed in Corporate Governance Perception Index (CGPI) and used in this research, are presumably quite well. Besides, the profile GCG for its weighted average of 2016 and 2017 shows that GCG has one indicator with minimum and maximum value of 72.68 and 93.32. The samples in this research are those companies consistently listed as having a good corporate governance. It means that the companies show good performance and are considered as trusted companies, which lies within the range of 70-84. Besides, the mean value of the GCG score is 84.92 which categorized as "most trusted companies", lies within 85-100. Thus, it indicates that companies begin to be concerned about their corporate governance.

4.2 Hypothesis Test (Direct, Intervening and Total effects)

The hypothesis test done by using the T-test and re-sampling. The hypothesis test divided into 3 parts of direct effect, mediation variable and the total effect of the variables in this research.

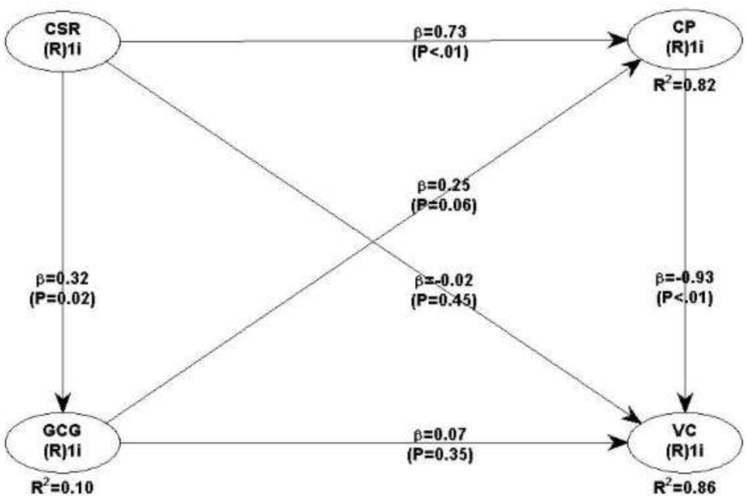

Figure I Structural model result

4.2.1 Direct Effect

Table VII Path Coefficient and P values

Independent / Control variable	Dependent Variable	Path Coefficient	P-value	Note
CSR	CP	0.73	<0.01	Highly significant
CSR	Value creation	-0.02	0.45	Insignificant
CSR	GCG	0.32	0.02	Significant
GCG	CP	0.25	0.06	Weakly significant
GCG	Value creation	0.07	0.35	Insignificant
Profitability	Value creation	-0.93	<0.01	Highly significant

Figure 1 and table VII show that corporate social responsibility policies affect corporate governance with the coefficient value of 0.32 and p value 0.02, and it also gives effect on corporate profitability with 0.73 coefficient value and p<0.01. In other words, the higher score of CSR policies will increase the profitability of the company (ROA), supported by the p value of lower than 5% significant level of both. This also means that **hypothesis 1** is accepted since the relationship between CSR policies and profitability shows a positive and highly significant direct relationship, hence **hypothesis 3** is also accepted as the CSR has a direct positive relationship with good corporate governance. The first hypothesis result is in line with the stakeholder theory that when firms put CSR practices into consideration, they will read a better performance (Yu and Choi, 2014). On the other hand, the acceptance of the hypothesis 3 is in line with the believe that higher commitments of CSR could strongly impact on the qualifications of directors and other members of the company which combined into a good corporate governance hallmark. Besides, good corporate governance may not able to increase reputation of the company without also taking care of the socially responsibility practices in the company (Chalise, 2014). Moreover, good corporate governance is showing a positive correlation of 0.25 and p=0.06, which is deemed to be weakly significant. Thus, **hypothesis 2** explains the relationship between GCG and profitability that is positive but weakly significant, and acceptable. This means that when companies are directed and controlled properly, the company could be more efficient in the work and operation which then result in better performance. In this case, an increase on efficiency of the work will impact the profit of the company (Sheikh et al, 2013).

Furthermore, the relationship of CSR Policies to value creation shows a value of -0.02 with p=0.45, which means that a higher score of CSR policies, the value of the firm will decrease and this is insignificant. Therefore, the **hypothesis 5** is rejected. This is supported by the theory that CSR practices could create long-term value for the company's financial performance instead of giving short-term impact (Gregory, Tharyan & Christidis, 2011). Moreover, the data also describes there is an insignificant effect of good corporate governance on value creation of 0.07 and p=0.35. This means that there is an insignificant positive relationship between the two variables, so **hypothesis 6** is rejected. It possibly happens because corporate governance implementation in a company can not directly influence the firm's value, but it takes some time. Likewise, the relationship between profitability and value creation shows a negative 0.93 with p<0.01. This means that profitability doesn't give a rise to value creation as it increases. Thus, **hypothesis 4** is also rejected. If profit does not provide an increase on funding of the company, the firm still has to decrease its dividends or choose to increase its debt level for the funding. Both of them give negative impact to the markets and usually result in a decrease of share price and destroy the shareholder's value.

4.3.2. Intervening Effect

The table below shows the indirect effect and P values of intervening variables.

Table VIII Indirect Effect and P values

Independent variable	Intervening variable	Dependent variable	Path coefficient	P value
CSR	CP GCG	VC	-0.657	<0.001
CSR	GCG	CP	0.079	0.258
GCG	CP	VC	-0.233	0.023

Looking at the table above, the p value of CSR towards corporate's profitability with good corporate governance as the mediating variable is 0.258. This figure shows a big percentage which is more than 5% significance, thus this is considered to be insignificant. It can be concluded that good corporate governance fails to act as a mediating variable, therefore **hypothesis 7 is rejected.** Additionaly, **hypothesis 8 is also rejected**, since the mediating variables shows a significant value of 0.023 (<0.05) with path coefficient for this is at -0.233. Hence, corporate profitability mediates the good corporate governance and value creation but negatively.

4.3.3. Total Effect

The total effect refers to the p values for all variables included in the research. This includes all the direct and indirect effect and being discussed further below:

Table IX Total Effect and P Values

	CSR	GCG	CP	VC
CSR	-	-	-	-

GCG	0.32 (=0.023)	-	-	-
CP	0.807 (<0.001)	0.25 (=0.06)	-	-
VC	-0.752 (<0.001)	-0.167 (=0.158)	-0.93 (<0.001)	-

The detailed calculation of the absolute contribution between variables is discussed below:

CSR to GCG = $(0.32)^2$ X 100% = 10.24%

CSR to CP = $(0.807)^2$ X 100% = 65.12%

CSR to VC = $(-0.752)^2$ X 100% = 56.55%

GCG to CP = $(0.25)^2$ X 100% = 6.25%

GCG to VC = $(-0.167)^2$ X 100% = 2.79%

CP to VC = $(-0.93)^2$ X 100% = 86.49%

The calculation of the overall total effect is taking account into both direct and indirect variables. As concluded in the results, the strongest absolute effect is the relationship between corporate profitability and value creation, which is 86.49% as compared to other variables. Meanwhile, the relationship between corporate governance and value creation holds the weakest effect as compared to other variables of only 2.79%. The correlation between CSR to profitability is 65.12% which is higher than if corporate governance acts as the mediating variable. This result is found when adding the result of CSR to corporate governance of 10.24% and corporate governance to profitability 6.25%, which comes out with 16.49% value. Thus, it can be concluded that the indirect effect does not exist between those two variables and corporate governance does not mediate the relationship between CSR and profitability. In addition, looking at the corporate governance as the mediating variable for CSR and VC relationship, there is also no indirect effect. This is concluded from the value of CSR to value creation of 56.55%. The value is higher than the sum of CSR to corporate governance 10.24% and corporate governance to value creation 2.79%, summed up to 13.03%. Thus, indirect effect does not exist when corporate governance mediates the second the relationship. In conclusion corporate governance does not have indirect effect for both of the relationship when it mediates the relationship between CSR to profitability and CSR to value creation.

5. Conclusion, Contribution and Implication

The objective of doing this research paper is to analyze the impact of corporate social responsibility (CSR) policies towards profitability and value creation, as well as whether the corporate governance (CG) is able to become the mediation variable to the relationship. The analysis shows a significantly positive relationship between CSR and profitability. Our contribution to this study is that higher CSR practices and corporate governance is associated with higher profitability obtained by the company as proposed in H1 and H2. This result indicates that consumers are not only concerned about the products they consume but also the manufacturers. Thus, companies with higher CSR practices could lead to increase in sales and profit. Besides, good corporate governance makes the company work more efficiently and effectively, which reduces cost or increasing margin and increases profitability. Companies with good corporate governance ensure a socially responsible way of how the companies are run and a lucidly ethical basis for complying with the accepted norms of the society where they operate. Hence, CSR actively searches for a larger equilibrium or consistency between profit and ethics, which is consistent with corporate governance mechanism as proven in H3.

However, profitability has negative effect on the value creation measured. Unless profits provide the increased funding, the firm has to lower the dividends or raise the debt level. The market perceives them negatively and generally leads to price drop, finally damaging shareholder value. It means that for some Indonesian companies listed in Corporate Governance Perception Index (CGPI), the CSR practice level still can not create long-term performance in terms of EVA.

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2.2 *Good Corporate Governance to corporate's profitability*

Companies' corporate governance implementation creates a system for directing, controlling and supervising the entire resources of the company efficiently and effectively (Jackling and Johl, 2009). Corporate governance is made to maintain the various interest from the stakeholders of the company which may provide benefits for the company. A company with a higher Corporate Governance Perception Index (CGPI) means that the company has been managed with transparency, accountability, responsibility, independency and fairness. Therefore, an impact can be seen on the outputs of good corporate performance, such as ROA, ROE and EPS (Gompers et al, 2003). Some previous studies using the same governance index, found that companies with stronger stakeholder rights tend to have higher profits. Sheikh et al. (2013) also found a positive relationship between board size and company performance.

H2: GCG has a positive impact on corporate profitability.

2.3 *Corporate social responsibility and Good Corporate Governance*

Corporate social responsibility (CSR) is currently a crucial element of companies and their stakeholders and continues to reap attention atop the corporate strategy. Previous study reveals that higher commitments to CSR strongly and positively correspond to the qualifications and terms of directors, boards that exert strong stewardship and strategic leadership roles, and the management of capital market pressures, and that these various attributes combined constitute the hallmarks of good corporate governance (Lock & Seele, 2015). Hence, CSR actively seeks a greater balance or compatibility between profit and ethics, which is consistent with corporate governance mechanism. Besides, Corporate social responsibility is considered related to corporate governance as governance is positively associated with environmental strengths of a firm (Stuebs and Sun, 2010). Not only that, previous study shows that good corporate

5. Conclusion, Contribution and Implication

The objective of doing this research paper is to analyze the impact of corporate social responsibility (CSR) policies towards profitability and value creation, as well as whether the corporate governance (CG) is able to become the mediation variable to the relationship. The analysis shows a significant positive relationship between CSR and profitability. Our contribution to this study has been provide that higher CSR practices and corporate governance is associated with higher profitability obtained by the company as proposed in H1 and H2. This result could also mean that consumers are not only concerning about the products they consume and but also the company which produces it. Thus, companies with higher CSR practices could lead to increase in sales and profit. Besides, good corporate governance makes the company is working more efficient and effectively, which reduces cost or increasing margin, resulted in profitability increases. Companies having good corporate governance ensures that companies are run in as socially responsible way and there should be a lucidly ethical basis to the business complying with the accepted norms of the society in which it is operating. Hence, CSR actively seeks a greater balance or compatibility between profit and ethics, which is consistent with corporate governance mechanism, proven in H3.

However, profitability has negative effect on value creation measured. Unless profits provide the increased funding, the firm has to decrease its dividends or increase its debt level. Both are negatively perceived by the markets and usually result in share price drop, eventually destroying shareholder value. This finding showed that for some

Corporate Social Responsibility Policies and Value Creation: Does Corporate Governance and Profitability Mediate That Relationship?

ABSTRACT

With a purpose to give a deep understanding relating to the manifestation of social responsibilities practices among Indonesian companies, this paper reflects the relationship of corporate social responsibility (CSR), corporate profitability (CP), value creation (VC) and good corporate governance (GCG). Kinder, Lydenberg, and Domini's (KLD) measurement approach is used in this study to measure the social responsibility practices as this gives cross-border analysis of social responsibility. Corporate Profitability captures return on assets which is accounting-based measurement, whereas value creation explains the economic value added which is shareholder-based measurement. Structural Equation Model (SEM) analysis is conducted for Indonesian listed companies which appeared in Corporate Governance Perception Index (CGPI). The empirical result suggests that CSR serves as a tool in assisting shareholders value and performance. Accordingly, firms should incorporate CSR practices to enhanced its strategic investment and sustain a strong relationship with its stakeholders. Subsequently, management should also take concern of having good corporate governance in order to improve company's performance by supervising and monitoring of the company's operation, ensure the fulfillment to the stakeholder's interest. This paper presents fresh insights into applications of corporate social responsibility principles and corporate governance in indonesia context that has not received systematic attention and consideration in the literature.

Keywords *Kinder Lydenberg and Domini's, Economic Value Added, Return on Assets, Corporate Governance Perception Index.*

JEL Classification: M4, Q5, G3

1. Introduction

In the traditional perspective, it is believed that business objective is to maximize the shareholder's wealth. However, as business grows, society come up with different perspective on how organization should operates. In this case, companies should shift from the mindset of enriching only shareholders to focusing on all the stakeholders, including environmental sustainability and community welfare. It is also becoming more important for companies to fulfill the environmental expectation in order to gain its reputation which further influence the firm's performance (Vargas, 2016).

Corporate social responsibility is considered to relate to corporate governance as governance is positively associated with the environmental strength of a firm (Stuebs and Sun, 2010). Not only that, previous study describes that good corporate governance could not able to increase reputation and performance of the company without also doing social responsibility practices (Chalise, 2014). Recent studies have also analysed the relationship of CSR and corporate governance from environmental performance perspective. The result shows a positive correlation on the study (Stuebs and Sun, 2010). This is because corporate governance highlights the framework to form an environment which are transparent, accountable and trusted. It also refers to how companies are being directed and controlled to avoid disputes between agents and investors and ensure that funds managed by agents are used accordingly (Detthamrong, Chancharat & Vithessonthi, 2017).

However, looking at the enforcement of CSR in Indonesia, this has been just a voluntary disclosure for many years. Meanwhile, starting from July 2007, Indonesian government has enforced a new regulation regarding CSR practices disclosure. Despite the large number of studies on CSR in the context of developed and moderately developed economies, whether or not CSR promote financial performance in the context of less developed and emerging ecnomies has been relatively unexplored. Additionally, very few studies have examined the roles of corporate governance (CG) as intervening variable. Therefore, this study refocuses on the debates around CSR and financial performance. In this case, corporate governance (CG) is inserted/ included to strengthen the relationship. Insights obtained from this study may contribute to both theories and real practices of CSR policies. It could be done to improve the CSR understanding and management literature, as well as answering questions by different individuals or corporates regarding CSR, CG and financial performance performance.

2. Literature review and hypothesis

2.1 Corporate social responsibility and corporate profitability

Many studies have been done to analyse the effect of CSR, including towards company's profitability. Corporates' profitability refers to the analysis of the ability of company to generate income. In this study, return on assets (ROA) is used to analyze the overall effectiveness of company's ability to generate profit with its assets (Gitman & Zutter, 2012). Since customers may have different perspectives on the implementation of CSR policies, CSR becomes an important element to build and maintain corporate's reputation and profitability, as well as to increase competitive advantage of the company (Park, 2017; Devie et al, 2019). Hence, companies that intend to enhance their reputation should focus on providing products with better quality that is able to satisfy their customers (Park et al, 2014). Therefore, good social reputation will lead to increase of sales, especially to customers that are sensitive to social and environmental issues, thus increase corporate profits (Khojastehpour & Johns, 2014). Profitable and large firms are also found to have a higher CSR disclosure in their reports (Muttakin, Khan & Subramaniam, 2015). Moreover, there have been several studies done worldwide to analyse the impact of CSR on different company's outcome including profitability. Yet, many have questioned as to whether the CSR implemented that incurred costs has created more benefits to it. However, this relationship between CSR and profitability still creates confusion and different results especially inconsistency between developed and developing countries. Although empirical results reported in previous studies about the CSR and profitability relationship are mixed, these study findings are mostly suggestive a positive relationship between CSR and corporate profitability (LaGore, Mahoney & Thorne, 2013; Yu and Choi, 2014; Cheung, 2010). Thus, this research study comes up with the following hypothesis.

H1: CSR policies has a positive impact on corporate profitability

2.2 Good Corporate Governance to corporate's profitability

The practice of companies' corporate governance creates a system for managing, monitoring and overseeing the whole resources of the company cost-effectively and functionally (Jackling and Johl, 2009). Corporate governance is established to preserve the different interests of company's stakeholders that could give advantages for the company. A company with a highly elevated Corporate Governance Perception Index (CGPI) indicates that it is managed with lucidity, responsibility, accountability, equity and independency. Consequently, the impact can be seen on the results of good corporate performance, such as ROE, ROA and EPS (Gompers et al, 2003). Some previous studies using similar governance index, discovered that companies with more powerful stakeholder rights are likely to produce higher profits. Sheikh et al. (2013) also discovered a positive association between board size and company performance.

H2: GCG has a positive impact on corporate profitability.

2.3 Corporate social responsibility and Good Corporate Governance

Corporate social responsibility (CSR) is recently a critical component of companies and their stakeholders and persists to gain attention on the top of the corporate strategy. Previous study discloses that stronger commitments to CSR significantly and positively explain the prerequisites and provisions of directors, boards that put forth strong stewardship and strategic leadership roles. Additionally the management of capital market hassles and that these different features combined compose the distinguishing characteristics of good corporate governance (Lock & Seele, 2015). Hence, CSR actively searches for a larger equilibrium or consistency between profit and ethics, which is consistent with corporate governance mechanism. Besides, corporate social responsibility is considered related to corporate governance as governance is positively related to environmental strengths of a firm (Stuebs and Sun, 2010). Moreover previous study shows that good corporate governance could not increase reputation of the company without social responsibility practices (Chalise, 2014). Recent studies have also analysed the relationship between CSR and corporate governance from environmental performance perspective. In this case the documentation of CSR performance of a firm has given benefits to support the corporate governance improvement effort of a company.

H3: CSR policies has a positive impact on good corporate governance.

2.4 Corporate profitability and value creation

In the recent years, the influence of profitability or performance on firm value has gained much attention in many studies. In the competitive environment, companies are trying their best to sustain in the industry by optimizing their cost in order to gain more profit for their operations. Besides, management starts to concern about its investment plans to maximize shareholder's wealth and firm value (Chen, 2011). Understanding the relationship of profitability and value creation is also important to financial decision making of the firm. Some researches have also proven the positive correlation between profitability and firm value (AlNajjar & Belkaoui, 1999; Crisóstomo et al, 2011; Osazuwa & Che-Ahmad, 2016). It was proven that as the firm profit got greater, more earnings would be distributable to shareholders. This is also in line with the agency theory about the management ability in managing assets in order to maximize profit, creating shareholder's trust to company's quality of management. Thus, the higher the financial performance, the higher the value of the company.

H4: CP has a positive impact on Value creation

2.5 Corporate social responsibility and value creation

Departing from the conventional system of the prior studies (LaGore, Mahoney & Thorne, 2013; Yu and Choi, 2014; Cheung, 2010; Gitman & Zutter, 2012; Khojastehpour & Johns, 2014) and instead of only focusing on a single financial measurement, a new method to measure firm's performance through value creation, is known as economic value added (EVA) are used this study. EVA is relevant for measuring the firm's performance as this tells us how much the companies have created wealth for the stakeholders and how efficient the management has utilized the capital from the stakeholders. It is also known as economic profit, which is believed to be a special way of measuring profit. This is because EVA is measured taking account into all the opportunity or cost of the capital invested in the business (Steward, 2014). Relating to CSR, CSR strategies need to be developed in order to have a proper CSR policy that is essential to satisfy the firm's goals. It is crucial to pay more attention to actives that may add scores to company's value. If the company is showing a positive VC, this also means that the company is working align with the corporate social responsibility. Besides, CSR creates value to the firm as the firm could be able to differentiate them from the competitors and also to reduce its costs. As the firm is having adequate management, this creates also value for the business and society. This shows the positive correlation between the company investment in CSR and the value creation of the firm (Green & Peloza, 2011). Likewise, there was also found to be a positive relationship between CSR and share price among companies in UK, especially those with an environmentally sensitive industry such as electricity, mining, and gas. Accordingly, the second hypothesis made for this research study is:

H5: CSR policies has a positive impact on value creation.

2.6 Good Corporate Governance and Value Creation

Corporate governance includes making sure that shareholders wealth as well as the other stakeholders are being taken into account in the management operation. This is also to prevent the corporate fraud and illegal accounting measure. Thus, value creation should be considered as to have a good corporate governance. Previous studies have found that significant corporate governance effect the greater shareholder's rights which by higher profit, sales growth and firm value (Gompers, Ishii, & Metrick, 2003). Some other researches are also showing different result for companies that implement good corporate governance in developed, developing and underdeveloped countries. Positive relations are found between good corporate governance practices with company's value (Klapper and Love, 2002; Black, Jang, and Kim, 2006).

H6: GCG has a positive impact on value creation.

2.7 Corporate social responsibility, good corporate governance and corporate profitability

The stakeholder theory defines that companies should do CSR practices as to fulfil their responsibility to stakeholders and able to maximize financial strength of the company. Supporting this, the corporate governance is describing as the intervening variable, strengthening the relationship of CSR and Corporate Profitability (CP). Besides, companies should have good corporate governance in addition to implementation of CSR practices, in order to give positive impact to the performance. This is because the importance of corporate governance take concern the welfare of all stakeholders, not only shareholder. Previous researchers also found positive relationship between CSR and performance (Salama, Anderson and Toms, 2018; El Ghoul et al., 2011; Lourenco et al., 2011). In addition to this, some also did research on the potential impact on CSR practices on firm's sustainability and resulted in corporate governance positively effecting CSR disclosure (Li et al., 2010)

H7: GCG could mediate the relationship between CSR policies and corporate profitability

2.8 Corporate social responsibility, good corporate governance and value creation

CSR could be considered as activities that create values for improving the firm's reputation, which further lead to improvement of economic performance of the company. CSR not only creates financial benefit to the company, but also strategic advantage. By engaging in social responsibility practices, firms can gain trust and goodwill from stakeholders, which is also a competitive advantage (Kolk and Pinkse, 2010). Research suggested that CSR activities would enhanced firm's image and reputation (Vanhamme et al., 2012). CSR policies help in increasing the company's value and satisfy its goals. Companies doing CSR practices creates positive Value Creation (VC) for the company. EVA which is a measurement of value created or lost is used to measure the performance and value creation made within the company. There is no previous research done regarding the relationship of CSR policies and value creation through GCG as intervening variable.

H8: GCG could mediate the relationship between CSR policies and value creation.

3. Research methodology

3.1 Sample

For the analysis of this study, as Structural Equation Model (SEM) is used. This model analysis covers gathering of secondary data, testing of hypothesis and evaluation of variable correlations. The sample of the study involves firms that are consistently listed as having good corporate governance by SWA-Magazine and Indonesia Institute for Corporate Governance (IICG) in 2016 and 2017. This study makes use of secondary data, including annual report, Bloomberg terminal and company's website.

Table I Summary of the sample observed

Sampling Criteria	*No. of Companies*
Companies listed in CGPI in the year 2016 and 2017 by SWA Magazine and IICG	39
Companies that were not consistently listed as having GCG in year 2016 and 2017	(13)
Companies that do not publish complete annual report in the required period	(10)
Number of companies which fulfill the criteria	16
Total sample used in the research (16 x 2)	32 firm-year

From the population of 39 companies included in the Corporate Governance Perception Index (CGPI) in 2016 and 2017, there are 23 companies that were not included for this research as the companies did not fulfilled the requirement of the research. It was those companies not consistently listed in CGPI and not publishing a complete annual report in the required period. Hence, there are 16 companies which fulfil the criteria and was the number of the companies observed. All samples that is used in the research are 32 reports derived from 16 companies multiplied by 2 years of observation.

3.2 Measures

Corporate Social Responsibility (CSR)

CSR policies is measured using Kinder, Lydenberg, and Domini's (KLD) method, chosen as a basic of CSR level. This measurement has been widely used in previous leading management journals (Nguyen and Nguyen, 2015; Li et al, 2010; Jo and Na, 2012; Devie et al, 2019). KLD provides benchmarking in 5 areas of CSR issue relevant to Indonesian companies, including diversity, community, environment, employee relation and products. In each of the KLD measurement, there are strengths and concerns. The strengths are considered to be positive CSR policies implemented, while concerns are as negative CSR policies implemented. If a company has a strength or even a concern, this would be given a "1" or "-1" On the other hand, companies without any would be indicated with a "0". After scoring the 5 qualitative areas, the total score of strength and concerns should be calculated in order to get Net CSR.

Value Creation

EVA spread is used as the mesurement of value creation. EVA is a performance measurement to calculates the residual income from subtraction of additional charge from net operating profit after tax (Steward, 2014), which take into account cost of capital and cost of equity. EVA aims to figure out the economic profit of a company.

Corporate Profitability

Return on Asset (ROA) is used as the measurement of profitability. This is calculated by dividing net income by average total assets. ROA is also known as the overall effectiveness of company's management in generating profits with its assets (Gitman & Zutter, 2012). ROA is widely used measurement of profitability in environmental studies (Nguyen & Nguyen, 2015; Park, 2017; Devie et al, 2019)

Good Corporate Governance

This research has been using GCG as the intervening variables. The GCG was measured using the measurement of Corporate Governance Perception Index (CGPI) that was published by IICG and SWA Magazine. This then had a scale of 0-100 values. CGPI score with the predicate "very trusted" for companies with scores of 85-100, "trusted" for companies with scores 70-84, and "quite reliable" for companies with a score of 55-69. The higher the score a company can get, the better the application of corporate governance is considered to be.

Table II Variable definitions and data source

Variable(s)	*Definitions*	*Data Source*
CSR Policies	Difference between total strengths score and total concerns score	Annual and Company' Websites
Corporate Profitability (ROA)	Percentage of net income over total assets	Annual Report and Bloomberg terminal
Value Creation (EVA)	Total of Net Operating Profit After Tax divided by the invested capital deducted by the weighted average of cost of capital	Bloomberg

Good Corporate Governance	Score of good corporate governance by SWA Magazine and IICG	SWA Magazine

3.3. Model

This study helps to analyze the relationship of CSR to Firm's performance in a positive, negative or neutral way as well as the role of corporate governance (CG) as intervening variable that alters financial performance. A multivariate statistical model is used through validity, reliability, and collinearity tests (Kock, 2015). Validity test consists of convergent validity and discriminant validity test for each of the indicator.

Table III Combined loadings and cross-loadings

Indicator	CSR	GCG	CP	VC	P value
CSR	1.00	0.00	0.00	0.00	<0.001
CG	0.00	1.00	0.00	0.00	<0.001
ROA	0.00	0.00	1.00	0.00	<0.001
EVA	0.00	0.00	0.00	1.00	<0.001

The table above shows that all the factor loading value of each indicators are all above 0.5. These value means that all indicators of CSR, CG, ROA and EVA which were used to measure all the variables have fulfilled the convergent validity test.

The following table shows discriminant validity. The discriminant validity is to compare the square root of average variance extracted (AVE) of each latent variable with the correlation between latent variables. If the square root of AVE of one indicator is larger than the other coefficient correlations in one parallel row of column, then the validity is fulfilled. The result of the discriminant validity is explained in the table below.

Table IV AVE table

Indicator	CSR	GCG	CP	VC
CSR	1.00	0.010	0.717	-0.061
CG	0.010	1.00	0.157	-0.149
ROA	0.717	0.157	1.00	-0.642
EVA	-0.061	-0.149	-0.642	1.00

From the table above, the square root AVE shows a figure of 1.00 for all results. These are also bigger than the coefficient correlation of the other variables.

Composite Reliability, Cronbach's Alpha and Collinearity

From the composite reliability test, all the variables have the value of 1.00, therefore composite reliability criteria are fulfilled. Not only that, result also has the Cronbach's Alpha value of more than 0.6, which is 1.00 for all the variables. Thus, all the variables have been fulfilled the criteria of reliability.

Table V Collinearity table

	CSR	GCG	CP	CV
R^2		0.099	0.817	0.864
Adj. R^2		0.069	0.805	0.850
Full collinearity VIFs	3.24	1.054	3.149	3.188

In order to fulfill the collinearity test, VIFs must be lesser than 3.3 or 10 in a more relaxed criterion (Kock, 2015). According in Table V, all variables have passed the multicollinearity tests.

4 Research results and analysis

4.1 Descriptive analysis

Descriptive analysis is done through looking at the statistics of coefficients which combined up as the data set, either in form of population as a whole or a sample as a part of the population. This explains the overview of the research data as a whole, which includes the total number of data used, minimum and maximum value, mean and standard deviation.

Table VI Descriptive Statistics

Indicators	Minimum	Maximum	Mean	STDEV
CSR	6.00	13.00	8.78	1.81
CG	72.68	93.32	84.92	5.32
ROA	-45.60	22.07	1.30	10.51
EVA	-7.17	94.57	5.31	17.67

Comparing the range to the CSR policies mean result in this research, the companies that are listed in Corporate Governance Perception Index (CGPI) and used in this research, are presumably quite well. Besides, the profile GCG for its weighted average of 2016 and 2017 shows that GCG has one indicator with minimum and maximum value of 72.68 and 93.32. The samples in this research are those companies consistently listed as having a good corporate governance. It means that the companies show good performance and are considered as trusted companies, which lies within the range of 70-84. Besides, the mean value of the GCG score is 84.92 which categorized as "most trusted companies", lies within 85-100. Thus, it indicates that companies begin to be concerned about their corporate governance.

4.2 Hypothesis Test (Direct, Intervening and Total effects)

The hypothesis test done by using the T-test and re-sampling. The hypothesis test divided into 3 parts of direct effect, mediation variable and the total effect of the variables in this research.

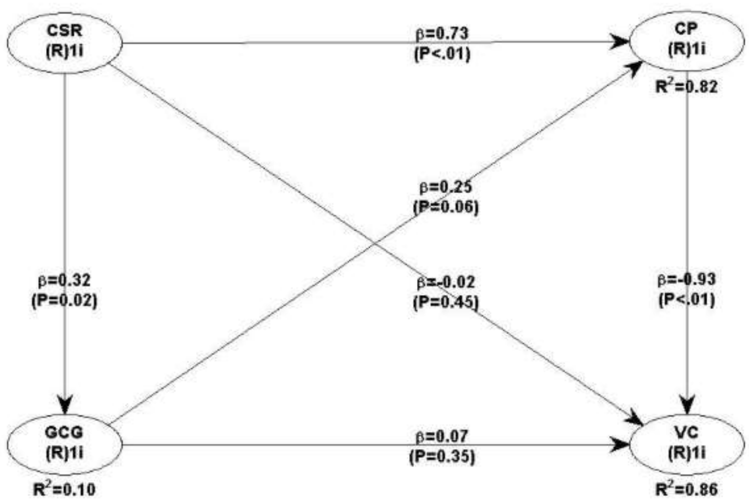

Figure I Structural model result

4.2.1 Direct Effect

Table VII Path Coefficient and P values

Independent / Control variable	Dependent Variable	Path Coefficient	P-value	Note
CSR	CP	0.73	<0.01	Highly significant
CSR	Value creation	-0.02	0.45	Insignificant
CSR	GCG	0.32	0.02	Significant
GCG	CP	0.25	0.06	Weakly significant

GCG	Value creation	0.07	0.35	Insignificant
Profitability	Value creation	-0.93	<0.01	Highly significant

Figure 1 and table VII show that corporate social responsibility policies affect corporate governance with the coefficient value of 0.32 and p value 0.02, and it also gives effect on corporate profitability with 0.73 coefficient value and p<0.01. In other words, the higher score of CSR policies will increase the profitability of the company (ROA), supported by the p value of lower than 5% significant level of both. This also means that **hypothesis 1** is accepted since the relationship between CSR policies and profitability shows a positive and highly significant direct relationship, hence **hypothesis 3** is also accepted as the CSR has a direct positive relationship with good corporate governance. The first hypothesis result is in line with the stakeholder theory that when firms put CSR practices into consideration, they will read a better performance (Yu and Choi, 2014). On the other hand, the acceptance of the hypothesis 3 is in line with the believe that higher commitments of CSR could strongly impact on the qualifications of directors and other members of the company which combined into a good corporate governance hallmark. Besides, good corporate governance may not able to increase reputation of the company without also taking care of the socially responsibility practices in the company (Chalise, 2014). Moreover, good corporate governance is showing a positive correlation of 0.25 and p=0.06, which is deemed to be weakly significant. Thus, **hypothesis 2** explains the relationship between GCG and profitability that is positive but weakly significant, and acceptable. This means that when companies are directed and controlled properly, the company could be more efficient in the work and operation which then result in better performance. In this case, an increase on efficiency of the work will impact the profit of the company (Sheikh et al, 2013).

Furthermore, the relationship of CSR Policies to value creation shows a value of -0.02 with p=0.45, which means that a higher score of CSR policies, the value of the firm will decrease and this is insignificant. Therefore, the **hypothesis 5** is rejected. This is supported by the theory that CSR practices could create long-term value for the company's financial performance instead of giving short-term impact (Gregory, Tharyan & Christidis, 2011). Moreover, the data also describes there is an insignificant effect of good corporate governance on value creation of 0.07 and p=0.35. This means that there is an insignificant positive relationship between the two variables, so **hypothesis 6** is rejected. It possibly happens because corporate governance implementation in a company can not directly influence the firm's value, but it takes some time. Likewise, the relationship between profitability and value creation shows a negative 0.93 with p<0.01. This means that profitability doesn't give a rise to value creation as it increases. Thus, **hypothesis 4** is also rejected. If profit does not provide an increase on funding of the company, the firm still has to decrease its dividends or choose to increase its debt level for the funding. Both of them give negative impact to the markets and usually result in a decrease of share price and destroy the shareholder's value.

4.3.2. Intervening Effect

The table below shows the indirect effect and P values of intervening variables.

Table VIII Indirect Effect and P values

Independent variable	Intervening variable	Dependent variable	Path coefficient	P value
CSR	CP GCG	VC	-0.657	<0.001
CSR	GCG	CP	0.079	0.258
GCG	CP	VC	-0.233	0.023

Looking at the table above, the p value of CSR towards corporate's profitability with good corporate governance as the mediating variable is 0.258. This figure shows a big percentage which is more than 5% significance, thus this is considered to be insignificant. It can be concluded that good corporate governance fails to act as a mediating variable, therefore **hypothesis 7 is rejected.** Additionaly, **hypothesis 8 is also rejected**, since the mediating variables shows a significant value of 0.023 (<0.05) with path coefficient for this is at -0.233. Hence, corporate profitability mediates the good corporate governance and value creation but negatively.

4.3.3. Total Effect

The total effect refers to the p values for all variables included in the research. This includes all the direct and indirect effect and being discussed further below:

Table IX Total Effect and P Values

	CSR	GCG	CP	VC
CSR	-	-	-	-
GCG	0.32 (=0.023)	-	-	-
CP	0.807 (<0.001)	0.25 (=0.06)	-	-
VC	-0.752 (<0.001)	-0.167 (=0.158)	-0.93 (<0.001)	-

The detailed calculation of the absolute contribution between variables is discussed below:

CSR to GCG $= (0.32)^2 \times 100\% = 10.24\%$

CSR to CP $= (0.807)^2 \times 100\% = 65.12\%$

CSR to VC $= (-0.752)^2 \times 100\% = 56.55\%$

GCG to CP $= (0.25)^2 \times 100\% = 6.25\%$

GCG to VC $= (-0.167)^2 \times 100\% = 2.79\%$

CP to VC $= (-0.93)^2 \times 100\% = 86.49\%$

The calculation of the overall total effect is taking account into both direct and indirect variables. As concluded in the results, the strongest absolute effect is the relationship between corporate profitability and value creation, which is 86.49% as compared to other variables. Meanwhile, the relationship between corporate governance and value creation holds the weakest effect as compared to other variables of only 2.79%. The correlation between CSR to profitability is 65.12% which is higher than if corporate governance acts as the mediating variable. This result is found when adding the result of CSR to corporate governance of 10.24% and corporate governance to profitability 6.25%, which comes out with 16.49% value. Thus, it can be concluded that the indirect effect does not exist between those two variables and corporate governance does not mediate the relationship between CSR and profitability. In addition, looking at the corporate governance as the mediating variable for CSR and VC relationship, there is also no indirect effect. This is concluded from the value of CSR to value creation of 56.55%. The value is higher than the sum of CSR to corporate governance 10.24% and corporate governance to value creation 2.79%, summed up to 13.03%. Thus, indirect effect does not exist when corporate governance mediates the second the relationship. In conclusion corporate governance does not have indirect effect for both of the relationship when it mediates the relationship between CSR to profitability and CSR to value creation.

5. Conclusion, Contribution and Implication

The objective of doing this research paper is to analyze the impact of corporate social responsibility (CSR) policies towards profitability and value creation, as well as whether the corporate governance (CG) is able to become the mediation variable to the relationship. The analysis shows a significantly positive relationship between CSR and profitability. Our contribution to this study is that higher CSR practices and corporate governance is associated with higher profitability obtained by the company as proposed in H1 and H2. This result indicates that consumers are not only concerned about the products they consume but also the manufacturers. Thus, companies with higher CSR practices could lead to increase in sales and profit. Besides, good corporate governance makes the company work more efficiently and effectively, which reduces cost or increasing margin and increases profitability. Companies with good corporate governance ensure a socially responsible way of how the companies are run and a lucidly ethical basis for complying with the accepted norms of the society where they operate. Hence, CSR actively searches for a larger equilibrium or consistency between profit and ethics, which is consistent with corporate governance mechanism as proven in H3.

However, profitability has negative effect on the value creation measured. Unless profits provide the increased funding, the firm has to lower the dividends or raise the debt level. The market perceives them negatively and generally leads to price drop, finally damaging shareholder value. It means that for some Indonesian companies listed in Corporate Governance Perception Index (CGPI), the CSR practice level still can not create long-term performance in terms of EVA.

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UNIVERSITAS KRISTEN PETRA

Josua Tarigan <josuat@petra.ac.id>

MA299: comments to be addressed

Josua Tarigan <josuat@petra.ac.id> Thu, Sep 29, 2022 at 8:06 PM
Draft

---------- Forwarded message ---------
From: <o.vorozhko@manuscript-adminsystem.com>
Date: Thu, May 23, 2019 at 7:46 PM
Subject: MA299: comments to be addressed
To: <josuat@petra.ac.id>

Dear Josua Tarigan,

Your manuscript “Corporate Social Responsibility Policies and Value Creation: Does Corporate Governance and Profitability Mediate That Relationship?” MA299 needs to be revised.

Below I present the comments:

“The paper seek to reflects the relationship between CSR and corporate value through the mediating role of corporate governance and profitability. While it does a good job in engaging with the variety of relevant literature, there are some issues that need to be attended to for the paper to provide significant contribution.

Rationale and positioning:

The paper needs to provide a compelling reason for why studying the variables under consideration are important or relevant in Indonesian context. The newly emerged government regulation can be something that may be used here, and by telling the readers more about this and relating it to your variables. Further, there is a confusion over what paper intends to do. I would suggest the authors to mention clear contribution upfront.

Literature:

While the paper engage with the considerable amount of literature on the said variables and assessing their relationship. For example, the authors refer to a number of studies but most of the discussion appears to be descriptive here and it lack critical evaluation of the studies conducted previously. Overall, the literature is overly presented as a list. The authors need to do more work to better aggregate the previous research, define the boundaries of knowledge which the build on.

Methodology, findings and discussions:

While the paper engage with the considerable amount of literature on the said variables and assessing their relationship. For example, the authors refer to a number of studies but most of the discussion appears to be descriptive here and it lack critical evaluation of the studies conducted previously.

Overall, the literature is overly presented as a list. The authors need to do more work to better aggregate the previous research, define the boundaries of knowledge which the build on.

The topic appears to be appealing and it will be of interests to many. However, in order to get published, the authors need to make significant contribution to the body of knowledge. Currently, the rationale, literature and discussions sections of the paper need urgent attention.”

The deadline for revisions is the 27th of May or let me know preferred terms.

Please acknowledge a receipt of this letter.

With best regards,

Olga Vorozhko

UNIVERSITAS KRISTEN PETRA

Saarce Elsye Hatane <elsyehat@petra.ac.id>

MA299: Manuscript is Agreed for Publication

1 message

Manuscript Administration System <noreply@manuscript-adminsystem.com> Tue, Jun 4, 2019 at 7:53 PM
To: elsyehat@petra.ac.id

Dear Saarce Elsye Hatane,

The manuscript CSR Policies and Value Creation: Does GCG and Corporate Profitability Mediate That Relationship? submitted to Investment Management and Financial Innovations is agreed for publication on 04.06.2019

The data about the author is below:

Author's First Name: Josua

Author's Last Name: Tarigan

University country: ID

University city: Surabaya

University email: josuat@petra.ac.id

The data about co-authors is below:

Co-Author's First Name: Saarce Elsye

Co-Author's Last Name: Hatane

Co-Author's University: Petra Christian University

Co-Author's Faculty: Business

Co-Author's Department: Accounting

Co-Author's Degree: MBA

Co-Author's Email: elsyehat@petra.ac.id

Co-Author's ORCID: N/A

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Co-Author's First Name: Linneke

Co-Author's Last Name: Stacia

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Co-Author's Faculty: Business

Co-Author's Department: Accounting

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Co-Author’s ORCID: N/A

Co-Author’s Researcher ID: N/A

Managing Editor/Publisher Coordinator of Investment Management and Financial Innovations Journal will contact you soon and provide with further information (Acceptance letter, Publication Agreement and Copyright & Licensing).

Kind regards,

undefined

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Saarce Elsye Hatane <elsyehat@petra.ac.id>

RE: MA299: proof-reading before publishing (IMFI Journal)

1 message

Olga Vorozhko <o.vorozhko@manuscript-adminsystem.com> Tue, Jun 11, 2019 at 7:56 PM
To: Josua Tarigan <josuat@petra.ac.id>
Cc: elsyehat@petra.ac.id, linnekezzz@gmail.com

Dear Josua Tarigan,

Attached you'll find a manuscript for proofreading before publication. Please check the text of your manuscript and correct mistakes (if any). Inform me if there are any corrections indicating page/line/column. Please make all changes in the PDF file with the aid of Comment function in Adobe Acrobat if it possible and separate explenations in Word file in case you want specify some corrections. Pay attention to yellow marks.

Would you please send us yours and co-authors' ORCID identificator (https://orcid.org/)?

We added new box near author's information on our site.

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Please, return proofs during next 2 days.

Please check your (and for your co-authors) affiliation, scientific rank, University (or organization), country (this information will be placed on the first page of your paper and on our site).

Also inform us about the process of payment. The paper will be published once the fee is received.

I look forward to hearing from you soon.

Thank you in advance.

With best regards,

Olga Vorozhko

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From: Josua Tarigan [mailto:josuat@petra.ac.id]
Sent: Monday, June 3, 2019 11:59 AM
To: Olga Vorozhko <o.vorozhko@manuscript-adminsystem.com>
Subject: Re: Pls confirm a receipt of the invoice MA299: invoice

Dear Editor,

yes we received the invoice. we will back to you by next week.

unfortunately when we received the invoice from you, our campus close already for Indonesia long public holiday (Eid Mubarak).

Thanks for your understanding

On Mon, Jun 3, 2019 at 3:10 PM Olga Vorozhko <o.vorozhko@manuscript-adminsystem.com> wrote:

> ---
>
> **From:** Olga Vorozhko [mailto:o.vorozhko@manuscript-adminsystem.com]
> **Sent:** Thursday, May 30, 2019 5:03 PM
> **To:** 'Josua Tarigan' <josuat@petra.ac.id>
> **Subject:** RE: MA299: invoice
> **Importance:** High
>
> Dear Josua Tarigan,
>
> Please, find attached the invoice and the agreement.
>
> We ask you to sign the agreement and to send the scan back to us.
>
> Have a nice day.
>
> With best regards,
>
> Olga Vorozhko

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From: Josua Tarigan [mailto:josuat@petra.ac.id]
Sent: Wednesday, May 29, 2019 6:28 PM
To: Olga Vorozhko <o.vorozhko@manuscript-adminsystem.com>
Subject: Re: MA299: Manuscript is accepted for publication

Dear Editor,

I have two questions:

- Is it fine if we only pay for the APC (495) without order the hard copy?

- and for the APC payment, when is the deadline? may I proposed the invoice first to my institution?

Thanks

On Wed, May 29, 2019 at 6:54 PM Olga Vorozhko <o.vorozhko@manuscript-adminsystem.com> wrote:

> Dear Josua Tarigan,
>
> I would like to inform you that your manuscript titled "Corporate Social Responsibility Policies and Value Creation: Does Corporate Governance and Profitability Mediate That Relationship?" has been accepted for publication, and will be published in the issue 2, 2019 of the journal "Investment Management and Financial Innovations".
>
> As soon as the payment will be done, I'll provide you with APC confirmation letter to let you have the reimbursement from your institution (if you need).
>
> The article processing charge (APC) is 495 euro. Also we propose to order a hard copy of the journal for 125 EURO per one copy.
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> We offer 3 methods of payment: 1) by invoice; 2) by bank transfer; 3) to pay online on our web-site via a credit card. Please, let me know, which one is convenient for you?
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Please sign Publication Agreement (see attached), tick boxes 1-8 and send it back and inform preferred payment option.

I look forward to hearing from you soon.

With best regards,

Olga Vorozhko

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From: Josua Tarigan [mailto:josuat@petra.ac.id]
Sent: Wednesday, May 29, 2019 1:16 PM
To: Olga Vorozhko <o.vorozhko@manuscript-adminsystem.com>
Subject: Re: REMINDER MA299: updated Cover letter is required as soon as possible

Dear Editor,

attached is the cover letter.

Thanks

--

Josua Tarigan, PhD, CMA, CFP, CSRA, CIBA, CBV

Head of International Business Accounting (IBAcc)

Petra Christian University

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Surabaya 60236, Indonesia

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On Wed, May 29, 2019 at 3:13 PM Olga Vorozhko <o.vorozhko@manuscript-adminsystem.com> wrote:

From: Olga Vorozhko [mailto:o.vorozhko@manuscript-adminsystem.com]
Sent: Tuesday, May 28, 2019 3:33 PM
To: 'Josua Tarigan' <josuat@petra.ac.id>
Subject: RE: MA299: comments to be addressed
Importance: High

Dear Josua Tarigan,

I received the revised version.

According to the journal's standard it is possible to include one more author but you should complete and sign the Cover letter again and indicated current date (see attached) .

With best regards,

Olga Vorozhko

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From: Josua Tarigan [mailto:josuat@petra.ac.id]
Sent: Monday, May 27, 2019 6:21 PM
To: Olga Vorozhko <o.vorozhko@manuscript-adminsystem.com>
Subject: Re: MA299: comments to be addressed

Dear Editor,

attached the file for author response for reviewer comments. please let us know if we need to upload it in the system.

by the way, I would like to ask whether possible to add one more author/contributor who help us to revise the article since beginning (plagiarism, layout formatting until the last revision to response the reviewer comments).

Thanks

On Mon, May 27, 2019 at 7:55 PM Olga Vorozhko <o.vorozhko@manuscript-adminsystem.com> wrote:

> Dear Josua Tarigan,
>
> The revised version is received.
>
> Woulf you please send a separate file with explanation of all your changes (point by point) named Response to Reviewers as soon as possible.
>
> With best regards,
>
> Olga Vorozhko
>
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> Follow us on **Twitter**: https://twitter.com/LLC_BP
>
> **From:** Josua Tarigan [mailto:josuat@petra.ac.id]
> **Sent:** Monday, May 27, 2019 2:42 PM
> **To:** Olga Vorozhko <o.vorozhko@manuscript-adminsystem.com>
> **Subject:** Re: MA299: comments to be addressed
>
> Dear Editor attached is the revised file.
> We have revised accordingly as suggested:
> 1) significant contribution: blue highlight
> 2) critical evaluation of the studies conducted previously: green highlight.
>
> also done through the online system
>
> thanks
>
> On Fri, May 24, 2019 at 4:21 PM Olga Vorozhko <o.vorozhko@manuscript-adminsystem.com> wrote:
>
>> Dear Josua Tarigan,
>>
>> Thanks for response.
>>
>> I'll wait for the revised version.

With best regards,

Olga Vorozhko

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From: Josuat [mailto:josuat@petra.ac.id]
Sent: Friday, May 24, 2019 12:09 PM
To: Olga Vorozhko <o.vorozhko@manuscript-adminsystem.com>
Subject: Re: MA299: comments to be addressed

Dear Editor,

Noted and will try to return it on 27th May

Regards

On 23 May 2019, at 19.47, Olga Vorozhko <o.vorozhko@manuscript-adminsystem.com> wrote:

> Dear Josua Tarigan,
>
> Your manuscript "The Effect of Working Capital Management Strategies on Profitability of Jordanian Food Companies Listed in Amman Stock Exchange" MA299 needs to be revised.
>
> Below I present the comments:
>
> "The paper seek to reflects the relationship between CSR and corporate value through the mediating role of corporate governance and profitability. While it does a good job in engaging with the variety of relevant literature, there are some issues that need to be attended to for the paper to provide significant contribution.
>
> Rationale and positioning:
>
> The paper needs to provide a compelling reason for why studying the variables under consideration are important or relevant in Indonesian context. The newly emerged government regulation can be something that may be used here, and by telling the readers

more about this and relating it to your variables. Further, there is a confusion over what paper intends to do. I would suggest the authors to mention clear contribution upfront.

Literature:

While the paper engage with the considerable amount of literature on the said variables and assessing their relationship. For example, the authors refer to a number of studies but most of the discussion appears to be descriptive here and it lack critical evaluation of the studies conducted previously. Overall, the literature is overly presented as a list. The authors need to do more work to better aggregate the previous research, define the boundaries of knowledge which the build on.

Methodology, findings and discussions:

While the paper engage with the considerable amount of literature on the said variables and assessing their relationship. For example, the authors refer to a number of studies but most of the discussion appears to be descriptive here and it lack critical evaluation of the studies conducted previously.

Overall, the literature is overly presented as a list. The authors need to do more work to better aggregate the previous research, define the boundaries of knowledge which the build on.

The topic appears to be appealing and it will be of interests to many. However, in order to get published, the authors need to make significant contribution to the body of knowledge. Currently, the rationale, literature and discussions sections of the paper need urgent attention."

The deadline for revisions is the 27th of May or let me know preferred terms.

Please acknowledge a receipt of this letter.

With best regards,

Olga Vorozhko

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From: Josua Tarigan [mailto:josuat@petra.ac.id]
Sent: Thursday, May 16, 2019 12:07 PM
To: Olga Vorozhko <o.vorozhko@manuscript-adminsystem.com>
Subject: Re: REMINDER: MA299: comments

Dear Editor,

Do you have any news regarding our article " **MA299** "

Thanks

--

Josua Tarigan, PhD, CMA, CFP, CSRA, CIBA, CBV

Head of International Business Accounting (IBAcc)

Petra Christian University

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W: www.petra.ac.id

On Tue, Mar 26, 2019 at 6:26 PM Olga Vorozhko <o.vorozhko@manuscript-adminsystem.com> wrote:

> Dear Josua Tarigan,
>
> The revised version is received and will be considered.
>
> With best regards,
>
> Olga Vorozhko
>
> Managing Editor | International Research Journal “Investment Management and Financial Innovations” | LLC “CPC “Business Perspectives”
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From: Josua Tarigan [mailto:josuat@petra.ac.id]
Sent: Tuesday, March 26, 2019 4:11 AM
To: Olga Vorozhko <o.vorozhko@manuscript-adminsystem.com>
Subject: Re: REMINDER: MA299: comments

Dear Editor,

attached is the revised article and also plagiarism check 13%.

we have uploaded the revise version.

thanks

--

Josua Tarigan, PhD, CMA, CFP, CSRA, CIBA, CBV

Head of International Business Accounting (IBAcc)

Petra Christian University

Jl. Siwalankerto 121-131

Surabaya 60236, Indonesia

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On Thu, Mar 21, 2019 at 3:08 PM Olga Vorozhko <o.vorozhko@manuscript-adminsystem.com> wrote:

> **From:** Olga Vorozhko [mailto:o.vorozhko@manuscript-adminsystem.com]
> **Sent:** Thursday, March 14, 2019 1:08 PM
> **To:** 'Josua Tarigan' <josuat@petra.ac.id>
> **Subject:** RE: MA299: comments
> **Importance:** High
>
> Dear Josua Tarigan,
>
> The revised manuscript was considered.
>
> Please pay attention to the section 2.2. and Conclusion.
>
> There is still a lot of similarities with another works.
>
> Please see the attached file.

Don’t forget to upload the revised version of the manuscript to the system.

With best regards,

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- Citing of previous study

- Abbreviation

- Section 2.3,2.4 & 5.2

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--

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the revised reference list and also cover letter was uploaded.

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--

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CORPORATE SOCIAL RESPONSIBILITY POLICIES AND VALUE CREATION: DOES CORPORATE GOVERNANCE AND PROFITABILITY MEDIATE THAT RELATIONSHIP?

Abstract

With a purpose to give a deep understanding relating to the manifestation of social responsibilities practices among Indonesian companies, this paper reflects the relationship of corporate social responsibility (CSR), corporate profitability (CP), value creation (VC) and good corporate governance (GCG). Kinder, Lydenberg, and Domini's (KLD) measurement approach is used in this study to measure the social responsibility practices, as this gives cross-border analysis of social responsibility. Corporate profitability captures return on assets, which is accounting-based measurement, whereas value creation explains the economic value added, which is shareholder-based measurement. Structural Equation Model (SEM) analysis is conducted for Indonesian listed companies, which appeared in Corporate Governance Perception Index (CGPI). The

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JEL Classification M4, Q5, G3

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INTRODUCTION

In the traditional perspective, it is believed that business objective is to maximize the shareholder's wealth. However, as business grows, society comes up with different perspective on how organization should operate. In this case, companies should shift from the mindset of enriching only shareholders to focusing on all the stakeholders, including environmental sustainability and community welfare. It is also becoming more important for companies to fulfill the environmental expectation in order to gain its reputation, which further influences the firm's performance (Vargas, 2016).

Corporate social responsibility is considered to relate to corporate governance, as governance is positively associated with the environmental strength of a firm (Stuebs & Sun, 2010). Not only that, previous study describes that good corporate governance could not be able to increase reputation and performance of the company without also doing social responsibility practices (Chalise, 2014). Recent studies have also analyzed the relationship of CSR and corporate governance from environmental performance perspective. The result shows a positive correlation on the study (Stuebs & Sun, 2010). This is because corporate governance highlights the framework to form an environment,

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which is transparent, accountable and trusted. It also refers to how companies are being directed and controlled to avoid disputes between agents and investors and ensure that funds managed by agents are used accordingly (Detthamrong, Chancharat, & Vithessonthi, 2017).

However, looking at the enforcement of CSR in Indonesia, this has been just a voluntary disclosure for many years. Meanwhile, starting from July 2007, Indonesian government has enforced a new regulation regarding CSR practices disclosure. Despite the large number of studies on CSR in the context of developed and moderately developed economies, whether or not CSR promote financial performance in the context of less developed and emerging economies has been relatively unexplored. Additionally, very few studies have examined the roles of corporate governance (CG) as intervening variable. Therefore, this study refocuses on the debates around CSR and financial performance. In this case, corporate governance (CG) is inserted/included to strengthen the relationship. Insights obtained from this study may contribute to both theories and real practices of CSR policies. It could be done to improve the CSR understanding and management literature, as well as answer questions by different individuals or corporates regarding CSR, CG and financial performance.

1. LITERATURE REVIEW AND HYPOTHESES

1.1. Corporate social responsibility and corporate profitability

Many studies have been done to analyze the effect of CSR, including towards company's profitability. Corporates' profitability refers to the analysis of the ability of company to generate income. In this study, return on assets (ROA) is used to analyze the overall effectiveness of company's ability to generate profit with its assets (Gitman & Zutter, 2012). Since customers may have different perspectives on the implementation of CSR policies, CSR becomes an important element to build and maintain corporate's reputation and profitability, as well as to increase competitive advantage of the company (Park, 2017; Devie et al., 2019). Hence, companies that intend to enhance their reputation should focus on providing products with better quality that is able to satisfy their customers (Park et al., 2014). Therefore, good social reputation will lead to increase of sales, especially to customers that are sensitive to social and environmental issues, thus increase corporate profits (Khojastehpour & Johns, 2014). Profitable and large firms are also found to have higher CSR disclosure in their reports (Muttakin, Khan, & Subramaniam, 2015). Moreover, there have been several studies done worldwide to analyze the impact of CSR on different company's outcome, including profitability. Yet, many have questioned as to whether the CSR implemented that incurred costs has created more benefits to it. However, this relationship between CSR and profitability still creates confusion and different results, especially inconsistency between developed and developing countries. Although empirical results reported in previous studies about the CSR and profitability relationship are mixed, these study findings mostly suggest a positive relationship between CSR and corporate profitability (LaGore, Mahoney, & Thorne, 2013; Yu & Choi, 2014; Cheung, 2010). Thus, this research study comes up with the following hypothesis.

H1: CSR policies have a positive impact on corporate profitability.

1.2. Good Corporate Governance and corporate's profitability

The practice of companies' corporate governance creates a system for managing, monitoring and overseeing the whole resources of the company cost-effectively and functionally (Jackling & Johl, 2009). Corporate governance is established to preserve the different interests of company's stakeholders that could give advantages for the company. A company with highly elevated Corporate Governance Perception Index (CGPI) indicates that it is managed with lucidity, responsibility, accountability, equity and independency. Consequently, the impact can be seen on the results of good corporate performance, such as ROE, ROA and EPS (Gompers et al., 2003). Some previous studies using similar governance index discovered that companies with more powerful stakeholder rights are likely to produce higher profits. Sheikh et al. (2013) also discovered a positive association between board size and company performance.

H2: GCG has a positive impact on corporate profitability.

1.3. Corporate social responsibility and Good Corporate Governance

Corporate social responsibility (CSR) is recently a critical component of companies and their stakeholders and persists to gain attention on the top of the corporate strategy. Previous study discloses that stronger commitments to CSR significantly and positively explain the prerequisites and provisions of directors, boards that put forth strong stewardship and strategic leadership roles. Additionally, the management of capital market hassles and that these different features combined compose the distinguishing characteristics of Good Corporate Governance (Lock & Seele, 2015). Hence, CSR actively searches for a larger equilibrium or consistency between profit and ethics, which is consistent with corporate governance mechanism. Besides, corporate social responsibility is considered related to corporate governance, as governance is positively related to environmental strengths of a firm (Stuebs & Sun, 2010). Moreover, previous study shows that Good Corporate Governance could not increase reputation of the company without social responsibility practices (Chalise, 2014). Recent studies have also analyzed the relationship between CSR and corporate governance from environmental performance perspective. In this case, the documentation of CSR performance of a firm has given benefits to support the corporate governance improvement effort of a company.

H3: CSR policies have a positive impact on Good Corporate Governance.

1.4. Corporate profitability and value creation

In the recent years, the influence of profitability or performance on firm value has gained much attention in many studies. In the competitive environment, companies are trying their best to sustain in the industry by optimizing their cost in order to gain more profit for their operations. Besides, management starts to concern about its investment plans to maximize shareholder's wealth and firm value (Chen, 2011). Understanding the relationship between profitability and value creation is also important to financial decision making of the firm. Some researches have also proven the positive correlation between profitability and firm value (AlNajjar & Belkaoui, 1999; Crisóstomo et al., 2011; Osazuwa & Che-Ahmad, 2016). It was proven that as the firm profit got greater, more earnings would be distributable to shareholders. This is also in line with the agency theory about the management ability in managing assets in order to maximize profit, creating shareholder's trust to company's quality of management. Thus, the higher the financial performance, the higher the value of the company.

H4: CP has a positive impact on value creation.

1.5. Corporate social responsibility and value creation

Departing from the conventional system of the prior studies (LaGore, Mahoney, & Thorne, 2013; Yu & Choi, 2014; Cheung, 2010; Gitman & Zutter, 2012; Khojastehpour & Johns, 2014) and instead of only focusing on a single financial measurement, a new method to measure firm's performance through value creation, known as economic value added (EVA), is used in this study. EVA is relevant for measuring the firm's performance, as it tells us how much the companies have created wealth for the stakeholders and how efficient the management has utilized the capital from the stakeholders. It is also known as economic profit, which is believed to be a special way of measuring profit. This is because EVA is measured taking account into all the opportunity or cost of the capital invested in the business (Steward, 2014). Relating to CSR, CSR strategies need to be developed in order to have a proper CSR policy that is essential to satisfy the firm's goals. It is crucial to pay more attention to actives that may add scores to company's value. If the company is showing a positive VC, this also means that the company is working align with the corporate social responsibility. Besides, CSR creates value to the firm, as the firm could be able to differentiate them from the competitors and also to reduce its costs. As the firm is having adequate management, this creates also value for the business and society. This shows the positive correlation between the company investment in CSR and the value creation of the firm (Green & Peloza, 2011). Likewise, there was also found a positive relationship between CSR and share price among companies in the UK, especially those with an environmentally sensitive industry such as electricity, mining, and gas. Accordingly, the second (fifth???) hypothesis made for this research study is:

H5: *CSR policies have a positive impact on value creation.*

1.6. Good Corporate Governance and value creation

Corporate governance includes making sure that shareholders' wealth, as well as the other stakeholders, are being taken into account in the management operation. This is also to prevent the corporate fraud and illegal accounting measure. Thus, value creation should be considered as to have Good Corporate Governance. Previous studies have found that significant corporate governance effect the greater shareholder's rights which by higher profit, sales growth and firm value (unfinished sentence???) (Gompers, Ishii, & Metrick, 2003). Some other researches are also showing different result for companies that implement Good Corporate Governance in developed, developing and underdeveloped countries. Positive relations are found between Good Corporate Governance practices and company's value (Klapper & Love, 2002; Black, Jang, & Kim, 2006).

H6: *GCG has a positive impact on value creation.*

1.7. Corporate social responsibility, Good Corporate Governance and corporate profitability

The stakeholder theory defines that companies should do CSR practices as to fulfil their responsibility to stakeholders and be able to maximize financial strength of the company. Supporting this, the corporate governance is describing as the intervening variable, strengthening the relationship of CSR and corporate profitability (CP). Besides, companies should have Good Corporate Governance in addition to implementation of CSR practices, in order to give positive impact to the performance. This is because the importance of corporate governance takes concern over the welfare of all stakeholders, not only shareholder. Previous researchers also found positive relationship between CSR and performance (Salama, Anderson, & Toms, 2018; El Ghoul et al., 2011; Lourenco et al., 2011). In addition to this, some also did research on the potential impact on CSR practices on firm's sustainability and resulted in corporate governance positively affecting CSR disclosure (Li et al., 2010).

H7: *GCG could mediate the relationship between CSR policies and corporate profitability.*

1.8. Corporate social responsibility, Good Corporate Governance and value creation

CSR could be considered as activities that create values for improving the firm's reputation, which further lead to improvement of economic performance of the company. CSR not only creates financial benefit to the company, but also strategic advantage. By engaging in social responsibility practices, firms can gain trust and goodwill from stakeholders, which is also a competitive advantage (Kolk & Pinkse, 2010). Research suggested that CSR activities would enhance firm's image and reputation (Vanhamme et al., 2012). CSR policies help in increasing the company's value and satisfy its goals. Companies doing CSR practices create positive value creation (VC) for the company. EVA, which is a measurement of value created or lost, is used to measure the performance and value creation made within the company. There is no previous research done regarding the relationship of CSR policies and value creation through GCG as intervening variable.

H8: *GCG could mediate the relationship between CSR policies and value creation.*

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2. RESEARCH METHODOLOGY

2.1. Sample

For the analysis of this study, Structural Equation Model (SEM) is used. This analysis model covers gathering of secondary data, testing of hypotheses and evaluation of variable correlations. The sample of the study involves firms that are consistently listed as having Good Corporate Governance by SWA-Magazine and Indonesia Institute for Corporate Governance (IICG) in 2016 and 2017. This study makes use of secondary data, including annual report, Bloomberg terminal and company's website.

Table 1. Summary of the sample observed

Sampling criteria	No. of
Companies listed in CGPI in the years 2016 and 2017 by SWA-Magazine and IICG	39
Companies that were not consistently listed as having GCG in the years 2016 and 2017	13
Companies that do not publish complete annual report in the required period	10
Number of companies which fulfill the criteria	16
Total sample used in the research (16 x 2)	32 firm-year

From the population of 39 companies included in the Corporate Governance Perception Index (CGPI) in 2016 and 2017, there are 23 companies that were not included in this research, as the companies did not fulfilled the requirement of the research. It was those companies not consistently listed in CGPI and not publishing a complete annual report in the required period. Hence, there are 16 companies, which fulfil the criteria and this was the number of the companies observed. All samples that are used in the research are 32 reports derived from 16 companies multiplied by 2 years of observation.

2.2. Measures

Corporate social responsibility (CSR)

CSR policies are measured using Kinder, Lydenberg, and Domini's (KLD) method, chosen as a basis of CSR level. This measurement has been widely used in previous leading management journals (P. Nguyen & A. Nguyen, 2015; Li et al., 2010; Jo & Na, 2012; Devie et al., 2019). KLD provides benchmarking in 5 areas of CSR issue relevant to Indonesian companies, including diversity, community, environment, employee relation and products. In each of the KLD measurement, there are strengths and concerns. The strengths are considered to be positive CSR policies implemented, while concerns are as negative CSR policies implemented. If a company has a strength or even a concern, this would be given a "1" or "–1". On the other hand, companies without any would be indicated with a "0". After scoring 5 qualitative areas, the total score of strength and concerns should be calculated in order to get net CSR.

Value creation

EVA spread is used as the mesurement of value creation. EVA is a performance measurement to calculate the residual income from subtraction of additional charge from net operating profit after tax (Steward, 2014), which take into account cost of capital and cost of equity. EVA aims to figure out the economic profit of a company.

Corporate profitability

Return on asset (ROA) is used as the measurement of profitability. This is calculated by dividing net income by average total assets. ROA is also known as the overall effectiveness of company's management in generating profits with its assets (Gitman & Zutter, 2012). ROA is widely used measurement of profitability in environmental studies (P. Nguyen & A. Nguyen, 2015; Park, 2017; Devie et al., 2019).

Good Corporate Governance

This research has been using GCG as the intervening variables. The GCG was measured using the measurement of Corporate Governance Perception Index (CGPI) that was published by IICG and SWA-Magazine. This then had a scale of 0-100 values. CGPI score with the predicate "very trusted" for companies with scores of 85-100, "trusted" for companies with scores 70-84, and "quite reliable" for companies with a score of 55-69. The higher the score a company can get, the better the application of corporate governance is considered to be.

Table 2. Variable definitions and data source

Variable(s)	Definitions	Data source
CSR policies	Difference between total strengths score and total concerns score	Annual and company' websites
Corporate profitability (ROA)	Percentage of net income over total assets	Annual report and Bloomberg terminal
Value creation (EVA)	Total of net operating profit after tax divided by the invested capital deducted by the weighted average of cost of capital	Bloomberg
Good Corporate Governance	Score of Good Corporate Governance by SWA-Magazine and IICG	SWA-Magazine

2.3. Model

This study helps to analyze the relationship of CSR to firm's performance in a positive, negative or neutral way, as well as the role of corporate governance (CG) as intervening variable that alters financial performance. A multivariate statistical model is used through validity, reliability, and collinearity tests (Kock, 2015). Validity test consists of convergent validity and discriminant validity test for each of the indicator.

Table 3. Combined loadings and cross-loadings

Indicator	CSR	GCG	CP	VC	*P*-value
CSR	1.00	0.00	0.00	0.00	< 0.001
CG	0.00	1.00	0.00	0.00	< 0.001
ROA	0.00	0.00	1.00	0.00	< 0.001
EVA	0.00	0.00	0.00	1.00	< 0.001

Table 3 shows that all the factor loading values of each indicators are above 0.5. These value means that all indicators of CSR, CG, ROA and EVA, which were used to measure all the variables, have fulfilled the convergent validity test.

Table 4 shows discriminant validity. The discriminant validity is to compare the square root of average variance extracted (AVE) of each latent variable with the correlation between latent variables. If the square root of AVE of one indicator is larger than the other coefficient correlations in one parallel row of column, then the validity is fulfilled. The result of the discriminant validity is explained in Table 4.

Table 4. AVE table

Indicator	CSR	GCG	CP	VC
CSR	1.00	0.010	0.717	–0.061
CG	0.010	1.00	0.157	–0.149
ROA	0.717	0.157	1.00	–0.642
EVA	–0.061	–0.149	–0.642	1.00

From Table 4 the square root AVE shows a figure of 1.00 for all results. These are also bigger than the coefficient correlation of the other variables.

Composite reliability, Cronbach's alpha and collinearity

From the composite reliability test, all the variables have the value of 1.00, therefore composite reliability criteria are fulfilled. Not only that, result also has the Cronbach's alpha value of more than 0.6, which is 1.00 for all the variables. Thus, all the variables have been fulfilled the criteria of reliability.

Table 5. Collinearity table

Variables Criteria	CSR	GCG	CP	CV
R^2	–	0.099	0.817	0.864
Adj. R^2	–	0.069	0.805	0.850
Full collinearity VIFs	3.24	1.054	3.149	3.188

In order to fulfill the collinearity test, VIFs must be less than 3.3 or 10 in a more relaxed criterion (Kock, 2015). According to Table 5, all variables have passed the multicollinearity tests.

3. RESEARCH RESULTS AND ANALYSIS

3.1. Descriptive analysis

Descriptive analysis is done through looking at the statistics of coefficients, which combined up as the data set, either in form of population as a whole or a sample as a part of the population. This explains the overview of the research data as a whole, which includes the total number of data used, minimum and maximum value, mean and standard deviation.

doi

Table 6. Descriptive statistics

Indicators	Minimum	Maximum	Mean	STDEV
CSR	6.00	13.00	8.78	1.81
CG	72.68	93.32	84.92	5.32
ROA	–45.60	22.07	1.30	10.51
EVA	–7.17	94.57	5.31	17.67

Comparing the range to the CSR policies mean result in this research, the companies that are listed in Corporate Governance Perception Index (CGPI) and used in this research are presumably quite well. Besides, the profile GCG for its weighted average of 2016 and 2017 shows that GCG has one indicator with minimum and maximum value of 72.68 and 93.32. The samples in this research are those companies consistently listed as having a good corporate governance. It means that the companies show good performance and are considered as trusted companies, which lies within the range of 70-84. Besides, the mean value of the GCG score is 84.92, which, categorized as "most trusted companies", lies within 85-100. Thus, it indicates that companies begin to be concerned about their corporate governance.

3.2. Hypotheses test (direct, intervening and total effects)

The hypothesis test was done by using the *T*-test and re-sampling. In this research, the hypothesis test was divided into 3 parts: direct effect, mediation variable and the total effect of the variables.

3.2.1. Direct effect

Table 7. Path coefficient and *p*-values

Independent/ control variable	Dependent variable	Path coefficient	*P*-value	Note
CSR	CP	0.73	< 0.01	Highly significant
CSR	Value creation	–0.02	0.45	Insignificant
CSR	GCG	0.32	0.02	Significant
GCG	CP	0.25	0.06	Weakly significant
GCG	Value creation	0.07	0.35	Insignificant
Profitability	Value creation	–0.93	< 0.01	Highly significant

Figure 1 and Table 7 show that corporate social responsibility policies affect corporate governance with the coefficient value of 0.32 and *p*-value 0.02, and it also gives effect on corporate profitability with coefficient value of 0.73 and $p < 0.01$. In other words, the higher score of CSR policies will increase the profitability of the company (ROA), supported by the *p*-value of lower than 5% significance level of both. This also means that Hypothesis 1 is accepted, since the relationship between CSR policies and profitability is positive, highly significant and direct, hence, Hypothesis 3 is also accepted, as the CSR has a direct positive relationship with Good Corporate Governance. The Hypothesis 1 result is in line with the stakeholder theory that when firms put CSR practices into consideration, they will read a better performance (Yu & Choi,

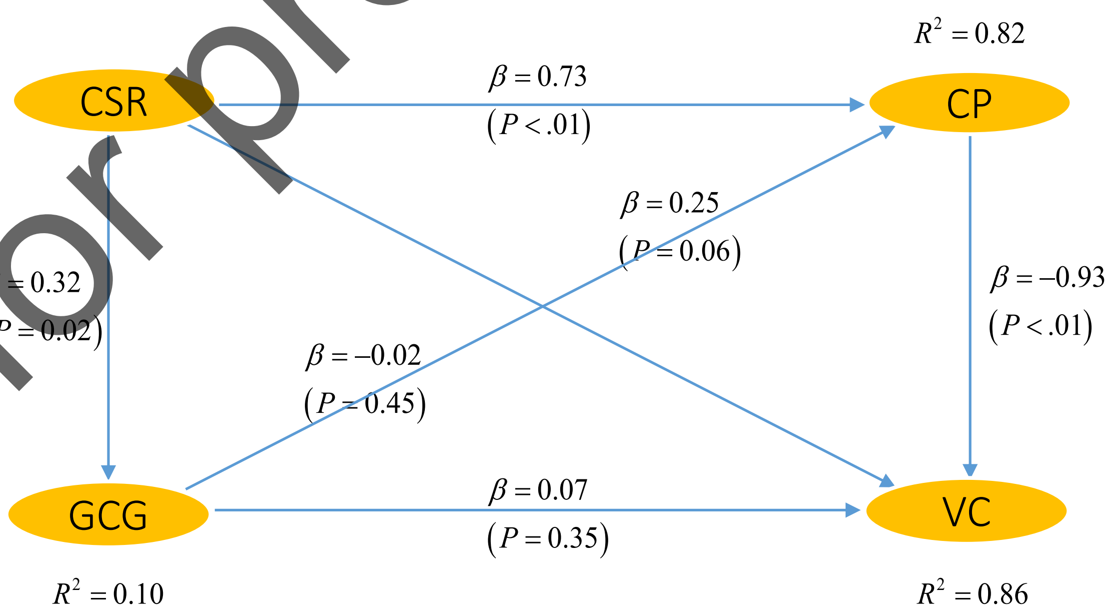

Figure 1. Structural model result

2014). On the other hand, the acceptance of the Hypothesis 3 is in line with the belief that higher commitments of CSR could strongly impact on the qualifications of directors and other members of the company, which combined into a Good Corporate Governance hallmark. Besides, Good Corporate Governance may not be able to increase reputation of the company without also taking care of the social responsibility practices in the company (Chalise, 2014). Moreover, Good Corporate Governance is showing a positive correlation of 0.25 and $p = 0.06$, which is deemed to be weakly significant. Thus, Hypothesis 2 explains the relationship between GCG and profitability that is positive but weakly significant, and acceptable. This means that when companies are directed and controlled properly, the company could be more efficient in the work and operation, which then results in better performance. In this case, an increase on efficiency of the work will impact the profit of the company (Sheikh et al., 2013).

Furthermore, the relationship of CSR policies to value creation shows a value of –0.02 with $p = 0.45$, which means that a higher score of CSR policies, the value of the firm will decrease and this is insignificant. Therefore, Hypothesis 5 is rejected. This is supported by the theory that CSR practices could create long-term value for the company's financial performance instead of giving short-term impact (Gregory, Tharyan, & Christidis, 2013). Moreover, the data also describe an insignificant effect of Good Corporate Governance on value creation of 0.07 and $p = 0.35$. This means that there is an insignificant positive relationship between the two variables, so Hypothesis 6 is rejected. It possibly happens because corporate governance implementation in a company cannot directly influence the firm's value, but it takes some time. Likewise, the relationship between profitability and value creation shows a negative value of 0.93 with $p < 0.01$. This means that profitability doesn't give a rise to value creation as it increases. Thus, Hypothesis 4 is also rejected. If profit does not provide an increase on funding of the company, the firm still has to decrease its dividends or choose to increase its debt level for the funding. Both of them give negative impact on the markets and usually result in a decrease of share price and destroy the shareholder's value.

3.2.2. Intervening effect

Table 8 shows the indirect effect and *p*-values of intervening variables.

Table 8. Indirect effect and *p*-values

Independent variable	Intervening variable	Dependent variable	Path coefficient	*P*-value
CSR	CP GCG	VC	–0.657	< 0.001
CSR	GCG	CP	0.079	0.258
GCG	CP	VC	–0.233	0.023

Looking at Table 8 the *p*-value of CSR towards corporate's profitability with Good Corporate Governance as the mediating variable is 0.258. This figure shows a big percentage, which is more than 5% significant, thus this is considered to be insignificant. It can be concluded that Good Corporate Governance fails to act as a mediating variable, therefore, Hypothesis 7 is rejected. Additionaly, Hypothesis 8 is also rejected, since the mediating variables show a significant value of 0.023 (< 0.05) with path coefficient for this being at –0.233. Hence, corporate profitability mediates the Good Corporate Governance and value creation, but negatively.

3.2.3. Total effect

The total effect refers to the *p*-values for all variables included in the research. This includes all the direct and indirect effect and being discussed further in Table 9.

Table 9. Total effect and *p*-values

Variables	CSR	GCG	CP	VC
CSR	–	–	–	–
GCG	0.32 (= 0.023)	–	–	–
CP	0.807 (< 0.001)	0.25 (= 0.06)	–	–
VC	–0.752 (< 0.001)	–0.167 (= 0.158)	–0.93 (< 0.001)	–

The detailed calculation of the absolute contribution between variables is discussed below:

$$\text{CSR to GCG} = (0.32)^2 \cdot 100\% = 10.24\%$$

$$\text{CSR to CP} = (0.807)^2 \cdot 100\% = 65.12\%$$

$$\text{CSR to VC} = (-0.752)^2 \cdot 100\% = 56.55\%$$

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$$\text{GCG to CP} = (0.25)^2 \cdot 100\% = 6.25\%$$

$$\text{GCG to VC} = (-0.167)^2 \cdot 100\% = 2.79\%$$

$$\text{CP to VC} = (-0.93)^2 \cdot 100\% = 86.49\%$$

The calculation of the overall total effect is taking account both direct and indirect variables. As concluded in the results, the strongest absolute effect is the relationship between corporate profitability and value creation, which is 86.49% as compared to other variables. Meanwhile, the relationship between corporate governance and value creation holds the weakest effect as compared to other variables of only 2.79%. The correlation between CSR and profitability is 65.12%, which is higher than if corporate governance acts as the mediating variable. This result is found when adding the result of CSR to corporate governance of 10.24% and corporate governance to profitability 6.25%, which comes out with value of 16.49%. Thus, it can be concluded that the indirect effect does not exist between those two variables and corporate governance does not mediate the relationship between CSR and profitability. In addition, looking at the corporate governance as the mediating variable for CSR and VC relationship, there is also no indirect effect. This is concluded from the value of CSR to value creation of 56.55%. The value is higher than the sum of CSR to corporate governance of 10.24% and corporate governance to value creation of 2.79%, summed up to 13.03%. Thus, indirect effect does not exist when corporate governance mediates the second relationship. In conclusion, corporate governance does not have indirect effect for both of the relationship, when it mediates the relationship between CSR and profitability and CSR and value creation.

CONCLUSION, CONTRIBUTION AND IMPLICATION

The objective of this research paper is to analyze the impact of corporate social responsibility (CSR) policies towards profitability and value creation, as well as whether the corporate governance (CG) is able to become the mediation variable to the relationship. The analysis shows a significantly positive relationship between CSR and profitability. Our contribution to this study is that higher CSR practices and corporate governance are associated with higher profitability obtained by the company, as proposed in H1 and H2. This result indicates that not only consumers are concerned about the products they consume, but also the manufacturers. Thus, companies with higher CSR practices could lead to increase in sales and profit. Besides, Good Corporate Governance makes the company work more efficiently and effectively, which reduces cost or increasing margin and increases profitability. Companies with Good Corporate Governance ensure a socially responsible way of how the companies are run and a lucidly ethical basis for complying with the accepted norms of the society where they operate. Hence, CSR actively searches for a larger equilibrium or consistency between profit and ethics, which is consistent with corporate governance mechanism as proved in H3.

However, profitability has negative effect on the value creation measured. Unless profits provide the increased funding, the firm has to lower the dividends or raise the debt level. The market perceives them negatively and generally leads to price drop, finally damaging shareholder value. It means that for some Indonesian companies listed in Corporate Governance Perception Index (CGPI), the CSR practices level still cannot create long-term performance in terms of EVA.

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