

# CHAPTER I

## INTRODUCTION

### 1.1 Background of the Study

Corporate Governance emerges as a value system in determining a company's value. Good Corporate Governance is an essential for companies nowadays, as the problems of business accountability and business ethics are increasing. By the end of 2017, the implementation of GCG in Indonesia was the lowest among ASEAN countries. There are 50 companies in Southeast Asia that have implemented GCG properly as Wimboh Santoso, the Chairman of the Board of Commissioners of the Financial Services Authority (OJK) once put. Only 2 Indonesian companies penetrate the ranks of companies along with the best GCG implementation in ASEAN. While Thailand has been a successful country because it has 50 best companies and 23 others, the Philippines has 11 companies, Singapore has 8 companies and Malaysia has 6 companies (OkeZoneFinance, 2017).

Thus, the application of GCG in Indonesia is now on legal basis, which is *Undang-undang Nomor 8 Tahun 1995 tentang Pasar Modal, Undang-undang Nomor 1 Tahun 1995 tentang Perseroan Terbatas, Undang-undang Nomor 10 Tahun 1998 tentang Perubahan atas Undang-undang Nomor 7 Tahun 1992 tentang Perbankan*. It is believed that implementation of good corporate governance is a business ethic and helps build the company's image. The government realizes it by issuing various regulations concerning the economy based on good corporate

governance principles as a manifestation of the global paradigm in conducting international businesses (Muryanto, 2016).

Corporate Social Responsibility (CSR) is a business model that gives positive impact on society. With the emergence of crucial global-scale challenges such as climate change for these last decades, scholars are recommending that CSR needs to transform from a voluntary activity to an immediate and integrated response, recognizing the business' major role and impact (Allen & Craig, 2016). Corporate Social Responsibility usually helps the companies to build customer loyalty, improves brand value and generates healthier financial performance. CSR shows relationship among companies, customers, investors, employees, and society as a whole. Implementation of CSR offers new images for firms. Society will have another point of views that a company does not only exist to earn profit, nevertheless, also socially responsible for environment. The purpose of CSR is for the welfare of the society and affect firm's performance, depending on each firm's implementation. Thus, the CSR implementation is no longer optional, however, it is compulsory for companies in Indonesia based on law *UU No. 40 Tahun 2007 Tentang Perseroan Terbatas (UU PT)*.

Banking Industries is one of the most important sectors worldwide, including Indonesia. Bank is a type of financial institution which handles debits and credits. It gives loans, accepts and deposits money, connects the gap between the lenders and the borrowers (Prabhavathi K, Dr.Dinesh G P. 2018), Those activities need to gain trust and good relationship with its customers. Thus, it is essential for banking industries to build and maintain good images in public.

In the last few decades, many banks from various countries have appeared in Indonesia and caused the banking sectors in Indonesia to be more competitive. In order to maintain a healthy and stable company, companies in banking sector should strive not only financially, but also non-financially. Therefore, banking sectors are implementing non-financial factors, such as Good Corporate Governance (GCG) and Corporate Social Responsibility (CSR).

The effect of Corporate Social Responsibility and Good Corporate Governance towards a firm's performance varies in many aspects, such as profitability. Therefore, there is a need to conduct this research. Profitability ratio measures the amount of profit that a company generates. There are various ratios that a company can use to measure the profitability.

In this research, the profitability will be proxied by Return on Assets (ROA). This ratio is usually used by many investors in decision-making. It is assumed that high ROA shows the capability of a company to develop and grow its business. The CSR of a company is measured by the Corporate Social Responsibility Index (CSRI) according to Global Reporting Initiative (GRI) G4 standards and GCG will be represented by the Institutional Ownership, which is one of Good Corporate Governance mechanism.

**Table 1.1 Data of CSRI, Institutional Ownership and ROA of 2 banking sector companies listed on IDX in 2017-2019**

Company	Year	Institutional Ownership	Corporate Social Responsibility Index (CSRI)	ROA (Return on Assets)
PT Bank Mandiri (Persero) Tbk	2017	60%	0.13	2.58%
	2018	60%	0.20	2.50%
	2019	60%	0.36	2.43%
PT Bank Negara Indonesia (Persero) Tbk	2017	98.14%	0.15	1.94%
	2018	97.41%	0.16	1.87%
	2019	96.18%	0.15	1.83%

Source: Prepared by the writer (2021)

Table 1.1 shows the percentage of Institutional Ownership, CSR Index and ROA from two banking sector companies. The amount of Institutional Ownership and CSRI are retrieved from the companies' annual reports and sustainability reports. PT Bank Mandiri (Persero) Tbk shows that the company has stagnant amount of Institutional Ownership, increasing CSRI and decreasing ROA from 2017-2019. PT Bank Negara Indonesia (Persero) Tbk shows that the company also has decreasing amount of Institutional Ownership, fluctuating CSRI and decreasing ROA from 2017-2019.

Hence, this study will analyze whether the company that implements Good Corporate Governance and Corporate Social Responsibility give impact to the profitability. Based on these descriptions, the writers are interested in conducting research under the title **"The Impact of Good Corporate Governance and Corporate Social Responsibility towards Firm Profitability in Banking Sector Companies Listed in Indonesia Stock Exchange"**.

## **1.2 Problem Limitation**

The writer will have some limitations while conducting the research. Corporate Social Responsibility and Good Corporate Governance are vast topics that cannot be fully-cover in a single report, thus, the writer will only concentrate on banking sector companies that is listed in IDX. The writer will only analyze one of Corporate Governance mechanism, which is Institutional Ownership. The scope of this research is limited as it only takes data from the period of 2017-2019.

## **1.3 Problem Formulation**

Based on the background study, therefore, the problem formulation for this study are as follow:

1. Does Corporate Social Responsibility partially affect firm profitability in Banking Sector Companies Listed in Indonesia Stock Exchange?
2. Does Good Corporate Governance partially affect firm profitability in Banking Sector Companies Listed in Indonesia Stock Exchange?
3. Do Corporate Social Responsibility and Good Corporate Governance simultaneously affect firm profitability in Banking Sector Companies Listed in Indonesia Stock Exchange?

#### **1.4 Objective of the Research**

The objective of the research are to answer the problems formulations, as follows:

- To identify whether Corporate Social Responsibility partially affects firm profitability in Banking Sector Companies Listed in Indonesia Stock Exchange.
- To identify whether Good Corporate Governance partially affects firm profitability in Banking Sector Companies Listed in Indonesia Stock Exchange.
- To identify whether Corporate Social Responsibility and Good Corporate Governance simultaneously affect firm profitability in Banking Sector Companies Listed in Indonesia Stock Exchange.

#### **1.4 Benefit of the Research**

The benefits of this research are expected to be useful for many parties.

##### **1.5.1 Theoretical Benefit**

- For writer  
From this study, the writer is able to apply the theories and knowledge that have been studied during her studies in university. The writer are able to

have deeper and broader understanding about the research topic, especially about firm profitability.

- For academic

This research may be additional references and literatures for future researchers, who are interested in Good Corporate Governance and Corporate Social Responsibility topics.

### **1.5.2 Practical Benefit**

- For firms

From this research, the firms can increase awareness toward the importance of GCG and CSR implementation. In addition, firms can get additional references and another point of views for decision-making, especially for profitability matters.

- For Investors

This research can give additional knowledge and another views for investors while analyzing the companies. Investors are informed the impact for a firm's profitability that implements GCG and CSR.