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CSR Disclosure, Customer Loyalty, and Firm Values (Study at Mining Company Listed in Indonesia Stock Exchange)

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ABSTRACT

This study aimed to examine the association of Corporate Social Responsibility (CSR) disclosure and the firm values on customer loyalty as a mediating variable. The samples of this study were sourced from the mining companies listed on the Indonesia Stock Exchange of 2008-2014. The secondary data used was obtained from the annual reports accessed through idx.co.id, and the sales reports based on the mining's sub-sectors accessed through bi.go.id. The variables of CSR disclosure were measured by using scores of weighting the item categories of CSR disclosure, namely: special items, core items, and additional items. Meanwhile, customer loyalty was measured by using market share, and the firm values were measured by Tobin's Q. The results proved that customer loyalty was the intervening influence of CSR disclosure and the firm values. This was the first study that applied different weighting to the category of disclosure items to calculate the scores of CSR disclosure through a statistical testing. Further research, then, can use the survey or focus group discussion (FGD) to determine the weighting method.

1. Introduction

During the past three decades, Corporate Social Responsibility (CSR) has been intensively debated (Jamali, 2008), and, in the future, it will become one of the most important issues of business ethics (Holland and Albrecht, 2013). Research examining the effects of CSR on firm value has not been consistent yet. Balabanis, Phillips, and Lyall (1998); (Belkaoui and Karpik, 1989; Margolis, Elfenbein, and Walsh 2009; Orlitzky, Schmidt, and Rynes 2003) found that CSR disclosure made by a company could significantly impact on the company's financial performance. Aras, Aybars, and Kutlu (2010) found that there was no relationship between CSR and the company's financial performance, while Kang, Lee, and Huh (2010) found that the positive and negative effects of CSR on company performance might vary, depending on the types of industries. The inconsistency of these research results indicates that the effect of CSR on the company performance is spurious (Galbreath and Shum, 2012), meaning that there is a contingent factor that mediates the relationship between CSR and firm performance. The illogical CSR done by a company can directly affect the company performance that has been previously assessed by the stakeholders. The results of the assessment reflect the decisions made by the stakeholders and thus can affect company performance.

This study broadens the previous research examining the effects of CSR on firm performance, and extends the understanding of the influence process of CSR on the firm values by examining the contingent factors, namely customer loyalty as a mediation of the association of CSR and the firm values. This article consists of a literature review, method, results, and discussion. The literature review addresses the importance of CSR in increasing the firm values and research results, examining the effects of CSR disclosure and firm values and the relevance of CSR disclosure, customer loyalty, and firm values. The method section presents an explanation of the research approach used in this study, the operational definition, and how variables of CSR disclosure, customer loyalty, and firm values are measured. It also goes into the conceptual framework and the development of the research hypothesis. Furthermore, the results section provides the statistical results of the hypothesis testing and the interpretation of this. The final section of this article discusses the test results, implications, and recommendations for further research.

2. Literature Review

Gray, Kouhy, and Lavers (1995) found that the CSR disclosure has several roles, namely (1) assessing the effect of firm activities on the environment and society; (2) measuring the effectiveness of firm's social and environmental programs; (3) reporting firm's environmental and social responsibilities; and (4) providing internal and external information systems that enable a comprehensive assessment on the firm resources and their impact on the sustainability of the company's operations. Thus, a company certainly attempts to be initiative to do the documentation and CSR disclosure of both its annual report and other media in order to get a positive response from the stakeholders. Research by Arya and Zhang (2009) found that investors in countries whose economies were growing responded to the CSR disclosure made by the companies. Likewise, research by Dhaliwal et al. (2011); (Francis, Khurana, and Pereira, 2005; Stuebs and Sun, 2010) found that customers, workers, and creditors also responded to CSR. Both the quantity and the quality of CSR done by industries in various countries, including the mining industry, are on the increase (Jenkins and Yakovleva, 2006). According to Walker and Howard (2002) in Jenkins and Yakovleva (2006), there are several reasons why CSR in mining companies becomes important. First, public opinion in the sector is not good. These opinions surrounding the natural resource extractive industry are influenced more by environmental and social performance than the performance related to product pricing, quality, and safety. Secondly, there is a consistent pressure on the sector at both local and international levels, as well as challenges to industries' legitimacy. Third, the funding sector increases the focus on the mining sector from the perspective of risk management and social responsibility. CSR disclosure is a complex phenomenon and has been studied by various disciplines that require different sources of literature to analyse (Taneja, Taneja, and Gupta, 2011). Stakeholders' expectations related to the company's contribution to society are also growing. This condition motivates the company's management to run the business by balancing acquiring profit and maintaining relationships with the stakeholders. CSR has evolved from firm philanthropy activities to a strategy that not only provides a social benefit, but also benefits to the company (Cochran, 2007). This condition requires the company to maintain the harmonisation with the stakeholders so that the company can still run the business, and the company's presence does not experience any rejection. When discussing and analyzing CSR, stakeholders' perspectives are inevitable (Branco and Rodrigues, 2007). While the company has the priority value when doing CSR, the stakeholders also have the priority value to assess any actions and motives of the company to conduct CSR. Reputation will be created due to stakeholders' trust in CSR as conducted by the company. Additionally, it will be able to provide benefits for the company. The value theory could explain the relationship between CSR and reputation that has been assessed by the stakeholders. The company conducts CSR, while the stakeholders assess the CSR undertaken by the company. Customers are one of the primary stakeholders that act as mediators of the relationship between CSR and market value of the company, because they generally prefer companies that practice CSR well, compared to ones that do not practice CSR (Xueming and Bhattacharya, 2006). Thus, this research aimed to examine customer loyalty as a mediator of the influence of CSR on the firm values.

CSR Disclosure and Customer Loyalty

Customers who have sufficient understanding of the importance of CSR practiced by a company are undoubtedly concerned with CSR disclosure. Concern for CSR practiced by the company is realised with the decision to use the company's products, and their good social performance will shape customer retention. Otherwise, a company's poor one will decrease the customer loyalty. Sen and Bhattacharya (2001) found that CSR initiatives conducted by the company in certain circumstances can reduce customer's intention to purchase the company's products. Changes in customer retention towards a company's products due to the customer's evaluation on the company's social performance can be represented by the market share of the company's products. Loyal customers will be able to increase sales of the company. In other words, customer loyalty is associated with market share (Al-Wugayan and Pleshko 2010; Keisidou et al., 2013). The difficulty of maintaining market share in a particular industry will motivate the company to increase CSR disclosure in its annual reports. Besides affecting the market share, CSR also increases and strengthens it (Epstein and Roy, 2001; Weber, 2008), and CSR will have an effect on the organization's reputation. Following on from the reputation perspective, communication between an organization and external parties on the levels of CSR performance will help to build a positive impression with customers, employees, investors, and creditors. Companies with good CSR performance can use CSR as an informational signal to their stakeholders. The stakeholders use this data as the basis of their ratings of the company's reputation. Thus, firms with a good reputation can build good relationships with customers. Research examining the effects of CSR on customer retention showed inconsistent results (Ali et al., 2010). This may arguably be due to the inability of the company to deliver CSR to the customers effectively. An effective understanding of CSR by customers can provide high satisfaction for the customers (Xueming and Bhattacharya, 2006). The positive perception of customers on the company's CSR initiatives can provide high satisfaction on the customer (Mandhachitara and Poolthong 2011). The positive perception of customers on the company's CSR initiatives can lead to high customer satisfaction (Hsu, 2012). In addition, satisfied customers will be loyal, continuing to either purchase more products or repeatedly use the services provided by the company. Referring to empirical evidence of the previous research, this research hypothesis is:

H1. The broader the CSR disclosure, the higher the customer loyalty.

Customer Loyalty and Firm Values

Company performance is determined by the contribution of several parties. These parties are the company's stakeholders, including customers, and will evaluate the CSR activities practiced by the company through CSR disclosure in its annual reports, assessing whether the CSR activities make significant contributions to the survival of the company or not. CSR performance will be good if CSR activities conducted by the company meet the stakeholders' expectations. Stakeholders will provide positive responses if they agree with the company's goal of practicing CSR and, otherwise, if the CSR practiced by the company, according to their perceptions, is not beneficial, it will make company's social performance poor. Social performance as an assessment result of the company's CSR will be reflected in the decisions made by the stakeholders depending on their own portion. Furthermore, a company's social performance is one of the factors influencing the firm values, customers being one of the stakeholders that make a direct contribution to the creation of firm values. Purchasing goods or using firm services is a direct role performed to generate revenue for the company. Normatively, customers who are concerned with the environment will undoubtedly use products created by companies that have no issues with the environment. The companies, on the other hand, also try to maintain customer loyalty, one of which is by maintaining harmony with the environment. Loyal customers can keep the company's revenue through the sales of its products and can further maintain the company's business continuity. Smith and Wright (2004) show that customer loyalty is positively related with the level of sales growth. Additionally, customer satisfaction has a significant positive impact on financial performance (Chi and Gursoy, 2009). Good sales growth and performance are the aspects assessed by the investors. The result of the investors' assessment is reflected in the firm values. Based on the description, this research developed the following hypothesis:

H2. The higher the customer loyalty, the better the firm values.

CSR Disclosure and Firm Values

CSR disclosure is a manifestation of the fact that a company is established not only to maximize its profits, but also to have a long-term goal in order to keep its business going. In the beginning, CSR disclosure was voluntary so that companies would consider any CSR activities merely an accessory, thus unimportant for the company's success. However, in recent times, CSR disclosure in companies' annual reports has been deemed to be essential and, thus, must be present. At this point, a company becomes aware of the importance of CSR activities for the business' continuity. CSR disclosure in both the company's annual reports and other information media is responded to by the users of the report reflecting on the company's financial performance (Akanbi and Ofoegbu 2012 ; Ekatah et al., 2011; Weshah et al., 2012). Environmental information is relevant for the users of financial reports in determining their support for the company's operational sustainability (Deegan and Gordon, 1996). CSR disclosure in the company's annual report is a medium that is currently considered to be effective and efficient to communicate CSR activities practiced by the company. The CSR disclosure is expected to help the company to show its social performance to stakeholders. Generally, content analysis is used in the literature of social and environmental reporting to evaluate the disclosure of certain items (Hackston and Milne, 1996). Companies need guidelines for CSR disclosure standards in order to express CSR transparently. These guidelines will also help report users obtain comprehensive information about CSR activities practiced by the company. Global Reporting Initiative (GRI) provides standardized reporting guidelines that encourage companies to report positive and negative aspects of sustainability performance (Hahn and Lülfs, 2013). CSR is a strategy for the company to create values for the company itself and the community through an interaction between the company and its stakeholders, and to be able to demonstrate a good reputation for the company (Puente, Sabate, and Garcia, 2007). Meanwhile, Aras et al. (2010) found that there is no significant relationship between CSR and financial performance.

The CSR disclosure practiced by a company could provide information to stakeholders on CSR activities that the company has performed. Essentially, the company tries to convey adequate disclosure in order to get responses from the customers, employees, debtors, or creditors associated with the company. The responses made by the stakeholders can eventually affect the firm values. Van Beurden and Gossling (2008) showed inconsistent results where they found positive relationship, no relationship, and negative relationship between Firm Social Performance (CSP) and Firm Financial Performance (CFP). Based on the description, a hypothesis proposed is:

H3. The broader the CSR disclosure, the better the firm values.

CSR Disclosure, Customer Loyalty, and Firm Values

Customers are stakeholders that could affect the firm values after receiving any information about the company's social performance. Theoretically, CSR has a positive effect on customers through their evaluation on the company's products (Maignan, 2001). CSR is a strategy for a company to show that it acknowledges its stakeholders. This strategy is applied so that the customers, as one of the primary stakeholders, choose to use the company's products because it has a good social performance compared to competition whose social performance may not be up to standard. Institutional CSR programs are more effective in increasing customer loyalty and reduce customer distrust in the companies (Pirsch, Gupta, and Grau, 2007). Good relationships with

customers can increase stakeholders' value, an intangible asset that can create a competitive excellence for companies, creating values for their stakeholders (Hillman and Keim, 2001). Most of the company's revenue is obtained from customers, and therefore customer satisfaction and loyalty is an important goal to achieve. Customers' awareness of the environment will make customers recognise the social responsibilities performed by the company. Customers' evaluation on CSR activities practiced by the company will thus affect the company's reputation. CSR disclosure made by the company will be assessed first by the customers, who can further determine the customer behavior related to the use of the company's products. Customers show that satisfaction and loyalty are generally useful for predicting the company's financial performance and, in particular, can create firm values (Anderson, Fornell, and Mazvancheryl 2004). This research considered customer loyalty a mediating variable due to inconsistent research results when conducting the direct examination of the relationship between CSR disclosure and the financial performance of the companies. This study was also based on the findings of Galbreath and Shum (2012), stating that the direct effect of CSR on company performance was spurious. Based on the description, a hypothesis proposed is:

H4. Indirectly, the broader the CSR disclosure, the better firm values through customer loyalty.

3. Research Method

This research used a quantitative approach, in accordance with the problems and the objectives of the study, namely explaining the association between the breadth of CSR disclosure and firm values with customer loyalty as a mediating variable. The population of this research was the mining industries listed in Indonesia Stock Exchange (BEI) in 2008-2014. The sample of this study was mining companies that published an annual report, and the data used for this research was available.

The CSR disclosure was measured using the GRI content index. Score 1 was for the disclosure, while 0 applied to the others. Furthermore, the disclosure items of the ones that were reported were calculated based on GRI version 3.0 about the sustainability reporting guidelines and mining and metals sectors supplement (GRI version 3.0 MMSS). The number of items disclosed by the companies in a particular year was documented in a working paper. Then, the items were grouped into 3 categories, namely: special items, core items, and additional items. This research measured the breadth of CSR disclosure using scores by giving weight to the types of standard disclosure based on materiality viewed from the reporting companies and the stakeholders. Materiality was determined by its impact on the stakeholders' evaluation and decisions, as well as its impact on the economic, environmental, and social decisions (GRI 2007). Since each item of disclosure had unequal materiality, different weights were applied. It is calculated by using the following formula:

$$\text{Score disclosure} = 50\% \sum Sp_{it} + 33\% \sum Cr_{it} + 17\% \sum Ad_{it}$$

$\sum Sp_{it}$ = the amount of special items disclosure of the company i in the t year.

$\sum Cr_{it}$ = the amount of core items disclosure of the company i in the t year.

$\sum Ad_{it}$ = the amount of additional disclosure of company i in the t year.

Customer loyalty is the customer's decision to keep purchasing the companies' products. This was measured by using the company's market share. Market share is the percentage of sales of companies in the industry, in this case, the mining industry in Indonesia. It is calculated by using the following formula:

$$\text{Market Share}_{i,t} = \frac{\text{Total of Company's Sales}_{i,t}}{\text{Total of Industry's Sales}_t} \times 100\%$$

$\text{Market Share}_{i,t}$ = the amount of the market share of company i in the t year.

$\text{Total of Company's Sales}_{i,t}$ = Total sales of company i in the t year.

$\text{Total of Industry's Sales}_t$ = Total sales of the mining industry in the t year.

The firm values can be measured on the basis of both accounting and capital market (Balabanis et al., 1998). Tobin's Q is a proxy that shows the company's market prices (Klapper and Love, 2004). This ratio has proved to attract academicians and financial practitioners to measure the firm values (Chung and Pruitt, 1994). The company's financial performance is formulated by using a market-based ratio. The market-based ratio used is Market Value (MV). MV is represented by Tobin's Q ratio.

$$\text{Tobin's Q} = \frac{\text{MVCS} + \text{STL} - \text{STA} + \text{BVLTD}}{\text{BVTA}}$$

MVCS = Market Value of Common Stock.

STL = Short-term Liabilities.

STA = Short-term Assets.

BVLTD= Book Value of Long-term Debt.

BVTA= Book Value of Total Assets.

4. Results

Table 1 panel A, 'Direct Effect', shows that CSR disclosure has significant positive effect on firm values (path coefficient = 0.154; $p = 0.011 < 0.05$, $R = 0.02$). This supports H3 stating that the broader the CSR disclosure, the better the firm values. Furthermore, customer loyalty variable as a mediator associating between the CSR disclosure and firm values.

Table 1 The results of PLS (path coefficient (t statistic), P Value, and R^2).

Panel A. Direct Effect

Variable	To the path	
	Firm values	
The CSR Disclosure	0,154(2,333)**	
R^2	0,02	

Panel B. Indirect Effects / Mediation (path coefficient (t statistic), P Value, and R^2)

Variable	To the path	
	Customer loyalty	Firm values
CSR Disclosure	0,610(8,841)***	0,074(0,813)
Customer loyalty		0,150(1,304)*
R^2	0,37	0,29

*** $p < 0.01$.

** $p < 0.05$.

* $p < 0.10$.

Table 1 panel B, 'Indirect Effects/Mediation', shows that CSR disclosure is significantly and positively associated with customer loyalty (path coefficient = 0.610 and $p < 0.001$), meaning that it supports H1 stating that the broader the CSR disclosure, the higher the customer loyalty. The association between the customer loyalty and firm values is not significant (path coefficient = 0.150 and $p = 0.097 > 0.05$), meaning it does not support H2 stating that the higher the customer loyalty, the better the firm values. However, entering the customer loyalty variable in the model examining the association of CSR disclosure (path coefficient = 0.074 and $p = 0.209 > 0.05$) shows insignificant results. Thus, it supports H4 which states that, indirectly, the broader the CSR disclosure, the better the firm values through customer loyalty. In other words, customer loyalty variable is the intervening element of the association between CSR disclosure and the firm values.

5. Discussion

Companies that practice CSR will create a good assessment from the customers. CSR can provide high customer satisfaction (Hsu 2012). Thus, customer loyalty to keep purchasing the company's products is formed. These results support Mandhachitara and Poolthong (2011) who found a significant positive association between CSR disclosure and customer loyalty. The significant positive result of association between CSR disclosure and customer loyalty in this study means the company has the ability to deliver CSR to customers effectively, and the customers are concerned with CSR conducted by the company. The research results support the signaling theory, meaning that the customers responded to the CSR disclosure practiced by the company in its annual report. CSR disclosure is a signal informing the activities of social responsibility undertaken by the company in its environment. Meanwhile, the customer response to the signal is evidenced by the statistical results, indicating the wider the CSR disclosure, the higher the customer loyalty represented by the large market share. This study proves that customer loyalty represented with market share shows insignificant association with firm values, meaning that the higher the market share of the company, the higher the firm values. These results support the findings of Al-Wugayan and Pleshko (2010); (Anderson et al., 2004) that customer loyalty does not significantly impact on the company's financial performance. Meanwhile, Smith and Wright (2004) found that customer loyalty was significantly associated with the company's performance. Company's concern on environmental responsibility is responded to positively by the customers, by making decisions to purchase products, indicating customers' willingness to support the implementation of social responsibility performed by the company (Maignan, 2001). This is evidenced by the statistical results, stating that the broader the CSR disclosure practiced by companies, the higher the market share obtained by companies in the industrial sector. The customer loyalty variable can explain 37% of the association between the breadth of CSR disclosure and customer loyalty, and this is a material value. Mohr, Webb and Harris (2001) found that the majority of customers were concerned with social responsibility taken by the company, those concerns additionally influencing their decision to purchase the company's products. Specifically, loyalty can be useful to create firm values (Anderson, Fornell, and Lehmann, 1994; Anderson et al., 2004). This research proved that customer loyalty was an intervening variable of the association between CSR disclosure and firm values, meaning that a significant association between CSR disclosure and firm values shown by the statistical results

(path coefficient = 0.154; $p = 0.011 < 0.05$) was false (spurious). This is consistent with the findings of Galbreath and Shum (2012).

6. Conclusion

This study found that CSR practiced by the company could not directly affect the firm values, but it had to be assessed first by the stakeholders, who, in this case, were the customers. Thus, in performing CSR, the manager of the company must pay attention to the values referred to by the customers for the CSR to be performed effectively. This research provides different weighting according to the statistical test results in the category of CSR items, based on the level of responses given by the stakeholders. Further research should confirm the stakeholders through surveys and/or Focus Group Discussion (FGD), to improve the validity and reliability of the category of CSR items.

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