A Correlation of CSR and Intellectual Capital, its Implication toward Company's Value Creation

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ABSTRACT:*Traditional accounting approach is not considered an intangible asset in determining the value of the company. Judging from the strategic aspect, the business is now growing process wherein, the company actively doing research, product innovation, development potential of the company, management and employee skill improvement and so on. So all the intangible aspects that are key to increasing the value of sustainable enterprises. One example of an intangible asset is intellectual capital (IC). On the other hand this aspect as neglected because it is not expressed in the financial statements which is the main basis in the valuation of the company. This study is exploratory research, has the main objective to assess the link CSR activities with IC in their influence on the creation of value for the company. Outcomes research studies be developed from the analysis of ratings and disclosures IC with antecedent and concequences which have been tested by previous research. However, these studies largely carried on the business environment in developed countries, and is still very limited studies conducted in developing countries that have a cultural background of eastern Indonesia.*
Based on reviews of an extant of literatures, several internal factors were identified as antecedents for IC. They are: CSR activities, firm growth and type of industry. The sample selection was based on certain criteria, and acquired 52 manufactured companies listed in IDX, from 2010-2014. Thisresearchfinds that CSR disclosure, specifically in the areas of social aspects and firm's size significantly influences IC and firm value. There was no evidence to support the existence of significant influence of growth toward IC. IC is an intervening variable for the influence of CSR toward company's value. Overall, findings of this research suggest that IC can be used to improve firm financial performance. The implication of this study is that companies should be concern to report their social activities and upgrade the quality of human capital who theirs.
Keywords: *Company's Value Creation, Intellectual Capital, CSR, Type of Industry.*

I.   INTRODUCTION

In most recent academicresearches have been concludedthat CSR haveaffectedtowardfirmvalue. Generally, theresultofthe previousstudiesstatethat CSR has positiveinfluencetofirmvalue. (Allouche, J. &Laroche, P., 2005, Orlitzky, M., etal, 1996, Wu, M.L., 2006; Steiner, G.A. &Steiner, 2006 atLuthan J.F., Elvira, 2012). Theses empiricalstudiesare basedonvarioustheories, includingthe theory of stakeholder, thelegitimacy theoryandsignallingtheory. The conclusionof the theories are thestakeholderswillrespondCSR ativitiespositivelywhich are reflected into an increase in stockmarketprices, theincrease in sales number and few number of despute from societies.

Eventhoughvariousempiricalstudies have been done, veryfewstudiedIntellectual Capital, whichispartof CSR activities. CSR isimplemented tobalancingthecompany'sactivitiestostakeholders, whichisreflected in the CSR report in theformofprofits, peopleand planet (3P orTripleBottom Line). Intellectualcapital (IC) isone of CSR's component in thecontextofpeople. If the companyconcernabout itsemployees, productquality, and customerservicewillimprove significantly. Thus CSR activitieshave a proportionalrelationshipwith IC company. (Razafindrambinina, D &Kariodimedjo, D. (2011), A.Salem Musibah1 & Wan Sulaiman (2013).

In the era ofglobalization, thecompany'sbusiness changefromtheindustrialagetotheinformationage, theknowledgebaseofgrowththecompany has graduallychangedfromtangibleassetsintointangibleassets. Thisledtothecompany'sinvestmentisnolongerfullyaffectedbyinvestment in buildings, machinery, andvariousotherphysicalfacilities, butalsotheknowledgethat has beenthe main sourceoftheeconomy as oneofthecompany'scompetitiveadvantage. Therefore, in creatingvalueforthecompany, thefocusshiftedfromtheuseof individual assetsintoassetclassesthat are mostlyintangibleassets, namelythe IC ortheknowledgecapitalinherent in theskills, knowledge, andexperience, as well as in thesystemsandproceduresoftheorganization. Petty andGuthrie (2000) statesthatthe IC was instrumental in determiningthevalueofthecompanyandtheperformanceofthenationaleconomy as well as thepotentialkeyto gain a sustainablecompetitiveadvantage.

Pulic (1998) proposed a measurement intellectual capital indirectly by using main component of VAIC™ which can be measured from physical capital of the company's resources (VACA- value added capital employed), human capital (VAHU-value-added human capital) and capital structure (STVA - capital structure of value-added). He also stated that the main aim of the economy based on knowledge is to create value added,

while creating added value required precise measurements that physical capital (monetary funds) and intellectual potential (represented by employees with all potentials and capabilities inherent in they) .Next Pulic (1998) stated that intellectual ability (which was then called VAIC ™) shows how these two sources (physical and intellectual potential of capital) has been efficiently utilized by the company (in Ulum 2008).

In Indonesia, the concept of IC in business practice is still a novelty, when compared to other countries. Shifting towards knowledge-based businesses have not responded adequately by the companies and business practitioners. In addition, the company in Indonesia has not reported IC explicitly. This has led to discrepancies between the management as the manager with stakeholders, so the company's stock rating to be low, which might lead to insider trading.

IC is one of the elements of intangible assets, however not disclosed transparently in the financial statements. This is due to inadequate recognition of intellectual capital. In PSAK No. 19 (revised 2000) mentioned that intangible assets are non-monetary assets that can be identified and does not have a physical form and held for use in generating or delivering goods or services, or leased to another party, (IkatanAkuntan Indonesia, 2007). Some elements of other intangible assets such as; human capital, innovation, customer or technology can not be included in the financial reporting for problem identification, recognition and measurement. Though IC has been a very valuable asset in today's modern business world and also a determinant of the company's operations.

Belkaoui (2003) and Firrer and Williams (2003) stated that in order to meet accounting conservatismin accounting practices, investment IC should be reported in the financial statements, which can becalculated from the difference between market value and book value of the firm. In efficient markets, the higher IC of the company, the higher the value of the firm. This is because investors are going to assess the company with higher IC.

Statement of The Problem

Over the last several years of research on IC on the performance and firm value much done in Indonesia, such as the research conducted by Purnomosidhi (2006), Boedi (2008), Kuryanto and Safruddin (2008), Ulum et al. (2008), Solikhah et al. (2010), Sir et al. (2010), Yuniasih et al. (2010), but there are still inconsistent results. In addition, very little research that examines simultaneously IC, CSR activities and value creation. This led the authors to conduct testing on these three variables. To sharpened the study, the research also incorporates elements of firm growth and type of industry. Both of these variables are also a determining factor IC's and the firm value in the capital market. Investors will be interested to invest in the growing company and on the type of specific industries.

II.   LITERATURE REVIEW

In a strategical perspective, a business corporation needs to consider its social responsibility towards environment where the business in. Business history and society has clearly shown when a business ignores its responsibility towards its stakeholders, society tend to response towards the government to limit its business authority. Business organizations have to identify all of their social responsibility to their own authority, and this has a very important influence on the effectivity and efficiency of the organizations (Hunger J David & Wheelen,2003 in Elvira,2010).This implied in the corporate social responsibility (CSR).

The concept of CSR is a developing and dynamic concept. Generally, CSR is a corporation way in reaching the balance or integration of economy, environment also social matter and at the same time could accomplish all the expectations of the stakeholders. CSR can be seen as a set of policies, practices and programs that integrated in a business operation, supply chain and decision making process in the whole corporation and used to cover some issues related to business ethic, social investment, environmental problem, government, human rights, also market and workplace (Tsoutsoura, 2004). A company that does CSR activity indicates its ability in fulfilling its internal and external needs. CSR activity is reported in a sustainability reporting that focuses on 3 performance aspects, those are economy (profit), environment (planet) and social (people) that used to known as TBL (Triple Bottom Line).

The company that continuously implement CSR will be positively responded by the market because it can take a good image from the society. Employee's skill will also increase because company does employee training and building by the CSR activities. By doing CSR, there is also an incresing of the product quality because company concern on the customer needs. All of those are the intangible assets that include one of them, IC, and IC doesn't disclosed in the financial statement. This happen because the traditional accounting practice doesn't disclose, identify, and measure IC. Meanwhile the intangible includes staff competency, customer relations, simulation model, computer system, and administration doesn't get a recognition in traditional financial model and management reporting (Stewart, 1997 in Hong 2007).

Kuryanto in his research stated that IC has been a valuable asset in a modern business. This cause a challenge for the accountants to identify, measure, and disclose it in the financial report. Traditional financial

report failed to provide the information about IC. A company that mostly its assets are in the form of IC that doesn't disclose this information in its financial report will mislead the stakeholders because it can influence the decision making. Thus, a financial report has to be able to describe IC and its acceptable value. The big differences between the market value and reported value make the financial report become unusable for decision making.

In many researches, IC is measured by VAIC method (*Value Added Intellectual Coefficient*) {(Tan *et al.*, (2007);Pulic,(2000); Firer & Williams, (2003)Bontis*et al*, (2000), Ulum, (2008))}. VAIC measures the efficiency of three kinds of company's output human capital, structural capital, also physical and financial capitalthat consist of :

a. *Human Capital Efficiency* (HCE) is a value added efficiency of human capital indicator. HCE is a ration of the value added (VA) towards human capital.
b. *Structural Capital Efficiency* (SCE) is a value added efficiency of structural capital indicator. SCE is a ratio form SC towards VA.
c. *Capital Employed Efficiency* (CEE) is a value added efficiency of a used value added capital indicator. CEE is a ratio from VA towards CE.

Previous Research Study & Hypothesis Development

A research that test the relationship of intellectual capital with corporate market value done by Chen *et al.* (2005) by using VAIC and Public companies in Taiwan as the sample. The result of Chen *et al.* (2005) shows that intellectual capital (VAIC) positively influence corporate market value. Tan *et al.* (2007) did a research on 150 listed companies in Singapore stock exchange. The result of his research is consistent with the research done by Chen *et al.*(2005) that IC (VAIC) has positive relationship with future company performance. This research also indicates that intellectual capital contribution (VAIC) on corporate performance is different based on its industry types.

Rehman et al (2012) did a research that tested the influence of IC components; HCE, CEE, and SCE towards financial performance component. His research stated that HCE, CEE and SCE have positive relationships toward financial performance measurement components (ROA and ROE), Value Added (VA) has a positive relationships toward financial performance measurement components (ROA and EPS), but HCE, SCE, and CEE don't have significant relationship with financial performance indicator (EPS). The research of Sunarsih et al (2012) concluded that IC had positive relationship on financial performance, financial performance as intervening variable could mediated the relationship between IC and corporate value. The results of this research showed that market gives higher assessment on company that has higher financial performance. The financial performance increases because the company is able to manage its intellectual resource effectively and efficiently.

Solikhah, et al. (2010) tested the implication of IC towards financial performance, company's growth, and corporate market value on manufacturing companies listed on Indonesia Stock Exchange for period 2006-2008. Solikhah, et al. found that IC significantly give positive influence towards corporate financial performance. IC significantly influenced by the company's growth. IC contribution towards financial performance company's growth, and corporate market value is different for each industries although those differences aren't so big because those companies are still in the same sector, manufacturing companies. Followed by a research of Soewarno (2011), he concluded that types of industry influence IC and organizational financial performance (ATO). Non-manufacturing industry gives higher moderating effect compared with manufacturing industry towards the relationship with IC and organizational performance (ROA and MB). Tan et al. (2007), Intellectual Capital positively influence corporate performance in present or even in the future; the average of Intellectual Capital has positive relationship with corporate performance in the future; intellectual capital contribution towards company's performance is different based on its industry types.

The relationship of IC and CSR is examined by Razafindrambinina,D.&Kariodimedjo, D. (2011). Their result concluded that IC measured by VAIC didn't has a significant relationship with CSR disclosure although one of its component, CEE had significant impact towards CSR disclosure, while HCE and SCE didn't have significant effect. This research also concluded that CSR perception is still in the phase where company does CSR by ad-hoc instead of putting it into company's strategy.

A. Salem Musibah& Wan Sulaiman (2013) conducted research on financial syariah sector in Gulf Cooperation Council, Malaysia. The research shows that VAIC has negative impact towards CSR. They also found that CSR has positive correlation with CEE and has negative correlation with HCE. However, their findings failed to find significant correlation between SCE and CSR.

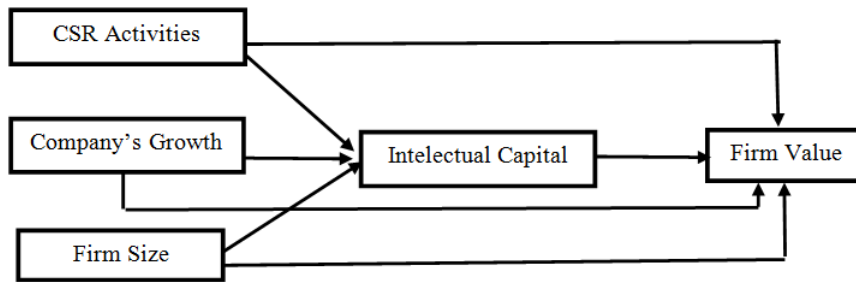Based on different result and studies above, so the framework can be seen as follow (Figure 2.1).

Figure 2.1. Research Framework

Based on framework above, the hypotheses are:
➢ *Hypothesis 1: CSR activities influence to company's intellectual capital.*
➢ *Hypothesis 2: CSR activities influence to firm value towards intellectual capital.*
➢ *Hypothesis 3: Company's growth influencetointellectual capital.*
➢ *Hypothesis 4: Company's growth influence to firm value.*
➢ *Hypothesis5: Firm size influence to intellectual capital.*
➢ *Hypothesis6: Firm size influence to firm value.*

III.   RESEARCH METHOD
3.1. Research Design
This research is designed to explore the relevancy between CSR implementation with intellectual capital and its implication towards the increasing of company's value. The exploration of the relevancy of these two variables is the first step to identify the strength of influence the other variables toward company's intellectual capital. Testing multiple models of relationships between these variables is an explanatory research that would explain the patterns of relationships between variables in a form of relationship simultaneously.

3.2. OperationalVariabel
In this study, the endogenous variables is intellectual capital and Firm Value. Whereas exogenous variables are implementing CSR, Firm Size and Growth of the Company. CSR activities are the primary data that the questionnaire is designed based on GRI index with the indicators of labor practices and the work feasibility, human rights practices, society aspect and product responsibility and environment.

Intellectual capital variable using primary data, the questionnaire was designed referring to the dimensionof Human Capital Efficiency, Structural Capital Efficiency, and Capital Efficiency Employed.

Firm value can be seen from the financial report analysis through financial ratio and the changing of the stock price. In this research, firm's value is measured by secondary data and use Tobin's Q. Tobin's Q is calculated with a formula as follows:

$$Q = \frac{EMV + D}{EBV + D}$$

Q   = Compay's value
EMV   =Equity market value (closing price x numbers of shares issued)
EBV   = Book value from total of equity
D   = Book value from total liability (current liability – current asset) + available book value + long term liability.

Asset's Growth is a increasing of ratio or the declining of total assets at the end of the year that is calculated based on the formula:

$$Growth = \frac{Total\ Assets_t - Total\ Assets_{t-1}}{Total\ Assets_{t-1}}$$

Firm size is measured based on the average of natural log from total assets.

3.3. Source and Determination Way of Data/Information
Research population is all companies listed in IDX whereas the one used as research sample is firms that published complete audited financial report from the period of 2011 till 2014. The data used in this research is consisting of two types of data; those are primary and secondary data. The respondent determination is purposive and questionnaires are expected to be given, filled and returned to the researcher by the managers who involved in the CSR activities or financial performance such as financial manager or operational manager. On the other hand, the secondary data is gotten from bibliography testing, scientific journals, documentation, financial report, sustainable report that published.

3.4. Data Analysis Methode
This research used *multiple statistical techniques*, thus this analysis can be done by using SPSS and PLS.

IV.   RESULT AND DISCUSSON
Data analysis is done by using the of SMARTPLS 2nd Version. Therefore the result of statistical analysis is done after excluding the indicators that did not fulfill the criteria of reliability and validity (see fig 4.1 research model after excluded non valid indicators).

4.1. Data Analysis Result
The following table (4.1.) was produced by SMART PLS. It can be concluded that the disclosure of CSR denoted CSR Index significantly influence to the IC Index. CSR Index did not significantly affect to Tobin's Q. Company size significantly affected to the IC, but did not significantly affect Tobins'Q. The company's growth was not significant its influence both the IC Index and also Tobins'Q. IC Index significantly affected toTobins'Q.

Fig. 4.1. The Final Research Model
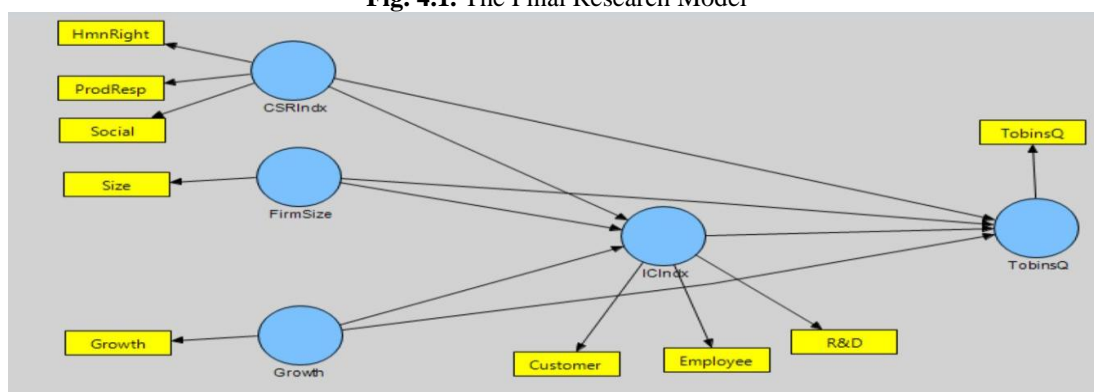
Source :Result from SMART PLS 2nd process.

Table 4.1. Path Coefficients

	Original Sample	Sample Mean	Standard Deviation	Standard Error	T Statistics
CSRIndx ->ICIndx	-0.287035	-0.341295	0.086683	0.086683	3.311341
CSRIndx ->TobinsQ	0.344340	0.087627	0.072665	0.072665	1.210193
FirmSize ->ICIndx	0.073227	0.065422	0.103231	0.103231	2.709347
FirmSize ->TobinsQ	-0.097934	-0.105776	0.073779	0.073779	1.327393
Growth ->ICIndx	-0.010893	-0.000606	0.150725	0.150725	0.072268
Growth ->TobinsQ	0.031700	0.059760	0.064562	0.064562	0.491001
ICIndx ->TobinsQ	-0.063574	-0.055688	0.094643	0.094643	1.981725

Source:Result from SMART PLS 2nd process.

4.2 Discussion
4.2.1   The influence of CSR towards Company's Value
From the CSR disclosure based on GRI, the aspect of social disclosure, there were some aspects that aren't disclosed by the companies at all during the analysis period. Those aspects that averagely aren't disclosed as follows:
a.   **Compliance:** In form of sanction that will be gotten by the company as the consequence of the violation of regulations in the society.
b.   **Non-discrimination:** A statement of no discrimination action in the company.
c.   *Forced and Compulsory Labor Practice*: A disclosure that is related to activities that can cause a risk of the employee's pressure.
d.   **Indigenous rights:** A disclosure that is related to the violation of native's rights.
e.   **Customer privacy:** A disclosure that is related to the customer advantage with the loosing of customer privacy that can happen in a certain time.
f.   **Child labor:** A disclosure that is related with the indication of under-age employee in an organization.

The involvement of under-age employee is a very contrary to the law of employment number 13 year 2003. So, many companies realize that under-age employees will bring a high risk toward the continuity of the companies.Social disclosure value (the disclosure of labor aspect, training and educating, social activities, customer relationship, etc) in average of 0.6629 showed that companies in Indonesia have been aware on the

importance of CSR disclosure (economic disclosure, environmental disclosure, social disclosure). This showed that sampled companies were aware on the prosperity and employee's development, and the importance of relationship maintenance with society in order to participate to society prosperity accomplishment.

Based on the citation of the social disclosure above, it can be seen that there were such big concern of the companies on their employee's quality improvement. Besides that, it is gotten information that the companies and society have a very strong relationship maintained by the good corporation and communication. Communication becomes the key success of CSR program and plays an important role in building the brand power by initially outing social and environmental awareness then improve the brand and associate the goods and services produced by the company that will shape the good image from the stakeholders toward the company. Good image will push forward the investor to invest in a company which in the end will increase the stock price and company's value. This is proved by the hypothesis testing that CSR significantly influenced IC index and IC also significantly influenced the company' value.

So, CSR disclosure in annual report is valued as able to give information about the sustainability of a company business to increase the economic activity to improve the success of the company. Investors feel secure in investing in the company (NurleladanIslahudin, 2008; Cheng, Megawati and YulisLogiChristiawan2011).

4.2.2 *The Influence of Intellectual Capital towards Company's Value*

To refer to the research done by Elramadani (2014), the biggest contribution in intellectual capital was VAHU that averagely contributed for about 75%. This means that the biggest contributor in creation of company's value in giving additional value for the company comes from the employees. Special attention on the employees suitable with the business condition where the company has the biggest human resource in running its business. The employee's development cost spent by the company is no longer recognized as expense but for knowledge based business. Employee expense recognized as long term investment that will give additional valueto the company in a long period.

By giving a big attention to the employees such as giving attention, softskill improvement, the giving of allowance for employees, and so forth will create value added by the company. With a good empowerment on the employees, this will motivates them on doing their activities based on the company purposes. This will results in a good performance, creates customer loyalty on product quality that is given by the employee, also the improvement of customer trust on the companies in Indonesia.

So, by the use and utilization of a better human capital, the profitability of the company will increase then the performance will increase and so does the company's value.Thus, the ability of the company in generating the profit with the current total assets owned will be more increase if the company can maximize human capital performance.

This result is consistent with the research of Belkaoui (2003), Firrer and William (2003), Iswati and Muslich (2007), Ulum (2008) that showed the intellectual capital has positive influence towards corporate financial performance. This research is also consistent with the research done by Guest (2003) that showed human capital influences the financial performance and assets turn over. Financial performance is one of the proxy of the company's value.

V. CONCLUSION

5.1. Conclusion
• CSR activity form people perspective or social disclosure significantly influenced the disclosure of IC especially the activity that related with employee building. Even though CSR disclosure didn't influence the company's value.
• IC influenced to the company's value that proxed by Tobins'Q value. So, market will response the implicit information of IC in the annual report of the sampled companies.
• Company's size positively influenced IC and company's value.
• Company's growth didn't influence neither IC and company's value.
• The result of this research can be used for theory development or anticipation for economic and business science developments especially accounting theory, social accounting and financial management.

5.2. Limitations and Implications for the next research.

Several variables in this research are done by using content analysis so there might be still subjectivity of the researcher in it. The next researcher can find another proxy for CSR activity and intellectual capital. This research didn't differentiate the types of industry so this couldn't cover the phenomenon if there is some certain laws for certain industry.

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