

The Influence of Islamic Social Reporting and Islamic Corporate Governance on Financial Performance in Islamic Banking in Indonesia

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Abstract

This study aims to determine the influence of Islamic Social Reporting and Islamic Corporate Governance partially and simultaneously on financial performance. The population of this study is Islamic Banking companies registered with the Financial Services Authority in 2019 - 2023. Sampling was carried out using the purposive sampling method, namely the sample was selected using certain considerations according to the established criteria. The sample selected in this study was Islamic Banking Companies registered with the Financial Services Authority, did not carry out mergers, acquisitions or spin-offs with other Islamic Banking companies, and had annual reports, and GCG implementation reports consistently and completely from 2019 - 2023. Data analysis in this study used multiple regression analysis. The results of this study indicate that Islamic Social Reporting partially has a significant influence on financial performance, while Islamic Corporate Governance partially does not have a significant effect on financial performance. The results of simultaneous testing indicate that Islamic Social Reporting and Islamic Corporate Governance together have a significant effect on the financial performance of Islamic Banking in Indonesia.

Keywords: *Financial Performance, Islamic Sosial Reporting, Islamic Corporate Governance*

INTRODUCTION

The Islamic banking sector in Indonesia has experienced remarkable growth in recent years, both in terms of financial assets and public interest. Unlike conventional banks, Islamic banks operate under the principles of Shariah, which are derived from the Qur'an and Sunnah, and integrate not only economic dimensions but also social and spiritual values into their operations (Meutia, 2010). One of the core characteristics that sets Islamic banking apart is its commitment to social justice and service to underprivileged communities, which is seen as an essential form of social accountability (Kamla & G. Rammal, 2013).

As of August 2023, the total assets of Islamic banks in Indonesia reached approximately IDR 817.6 trillion, reflecting a growth of 9.79% (OJK, 2023). This upward trend is supported by Indonesia's predominantly Muslim population, whose preference for Islamic banking continues to increase (Khan & Zahid, 2020). With this rapid development, it becomes essential to evaluate the financial performance of Islamic banks, particularly through key indicators such as Return on Assets (ROA), which Bank Indonesia sets at a minimum benchmark of 1.5% (PBI No. 6/9/PBI/2004).

In line with their spiritual and ethical foundations, Islamic banks are also expected to practice a high level of social responsibility. According to Asyraf (Asyraf Wajdi & Dar, 2007), Islamic financial institutions are morally obligated to serve society, avoid exploitation, and reduce poverty in accordance with divine commandments. Hence, their performance should be assessed not only through financial metrics but also through their alignment with social welfare objectives.

Transparency in annual reporting is increasingly critical as stakeholders demand greater accountability, especially in a sector claiming religious legitimacy. Despite this, several studies have found that Islamic banks often fall short in disclosing meaningful social justice initiatives. For instance, (Kamla & G. Rammal, 2013) argue that while Islamic banks frequently emphasize their religious identity, they rarely provide detailed disclosures about programs aimed at poverty alleviation or social equity. Similarly, (Lina & Febrian, 2020) found that Indonesian Islamic banks struggle to clearly articulate their contributions toward poverty reduction or the promotion of social justice.

To address these issues, the Shariah Enterprise Theory (SET), developed by (Triyuwono, 2011), has been proposed as a more holistic framework for evaluating Islamic institutions. SET places Allah as the ultimate stakeholder and promotes a balance between individual and communal interests, material and spiritual values, and human and environmental concerns. This theory suggests that organizations, including Islamic banks, should operate with a heightened sense of moral and social accountability that transcends conventional business logic.

Furthermore, Islamic Corporate Governance (ICG) is a critical factor in ensuring that Islamic banks adhere to ethical practices. ICG represents an extension of Good Corporate Governance (GCG), incorporating Shariah principles in the governance structure to safeguard stakeholder interests ethically and transparently (Triyuwono, 2011). Given the increasing incidence of fraud within the Islamic banking sector—such as recent cases involving corruption and misappropriation of funds (Kompas.com, 2021; KompasTV, 2022; MediaJatim, 2023)—strong governance is more crucial than ever. According to data from the Association of Certified Fraud Examiners Indonesia (2019), financial institutions were the most affected by fraud, incurring 41.5% of total losses, surpassing even governmental institutions.

In light of these dynamics, this study aims to examine the effect of Islamic Social Reporting (ISR) and Islamic Corporate Governance (ICG) on the financial performance of Islamic banks in Indonesia from 2019 to 2023. By using a five-year observation period, this study offers updated insights that build upon previous research and provides a more comprehensive understanding of how ethical disclosures and governance influence financial sustainability in the Islamic banking industry.

RESEARCH METHODS

This study employs a quantitative approach, which, according to Sugiyono (2017), is a research method used to examine specific populations or samples, typically through data collection and analysis using statistical tools. This research aims to investigate the influence of Islamic Social Reporting (ISR) and Islamic Corporate Governance (ICG) on Financial Performance, with the study population comprising all Islamic banks in Indonesia. The sampling method used is purposive sampling, with the selection criteria including Islamic banks that published annual reports and financial reports during the 2019–2023 period, included data on ISR, ICG, and financial performance, and were registered with the Financial Services Authority (OJK). The data used in this research are secondary data obtained from annual reports and official websites of the respective Islamic banks. The analysis technique applied is multiple linear regression analysis, processed using the IBM SPSS Statistics 25 software.

Descriptive Analysis

Tabel Shows that the study consists of 35 observations from 7 companies over a 5-year period (2019–2023). The descriptive statistical analysis results are as follows: the average Islamic Social Reporting (ISR) index is 0.4949, indicating that most Islamic banks disclose less than 50% of the total ISR indicators, with scores ranging from 0.37 to 0.67 and a standard deviation of 0.07532. The average Islamic Corporate Governance (ICG) index is 3.8571, with a minimum score of 3.00, a maximum of 5.00, and a standard deviation of 0.60112. The average financial performance, measured by Return on Assets (ROA), is 1.3597, suggesting generally positive performance among Islamic banks. However, the ROA ranges from -5.67 to 9.10, with a standard deviation of 2.74856, indicating that some banks experienced losses during the study period

Tabel 1. Descriptive Statistical Result

	N	Descriptive Statistics			
		Minimum	Maximum	Mean	Std. Deviation
ISR	35	.37	.67	.4949	.07532
ICG	35	3.00	5.00	3.8571	.60112
ROA	35	-5.67	9.10	1.3597	2.74856
Valid N (listwise)	35				

Source: SPSS Data Processing Result

Classical Assumption Test

Normality Test

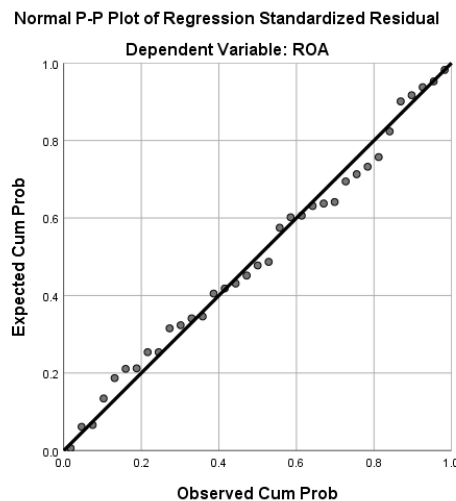


Figure 1. Normality Test Result

Source: SPSS Data Processing Result

Based on the graph above, it can be seen that the data points are spread around and follow the direction of the diagonal line, indicating that the regression residual scores meet the normality assumption.

Multycolenierity test

It can be inferred that there is no multicollinearity between the independent variables, as reflected in the tolerance scores for all independent variables, which are above 0.1. Additionally,

the VIF score for ISR is 1.012, and the VIF score for ICG is also 1.012, indicating the absence of multicollinearity between both ISR and ICG variables.

Heteroscedasticity test

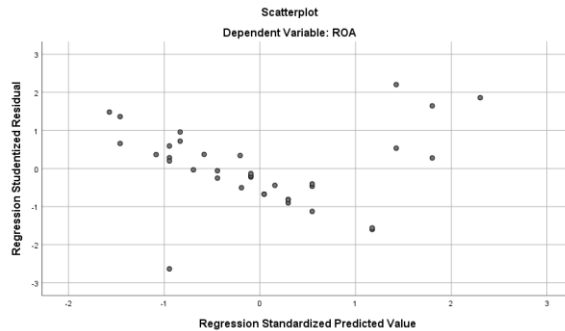


Figure 2. The Scatterplot for the Heteroscedasticity Test
Source: SPSS Data Processing Result

The points on the scatterplot are spread both above and below the zero line, without showing any specific pattern. Based on this analysis using the scatterplot, it can be concluded that the data does not exhibit signs of heteroscedasticity.

Autocorrelation test

The Durbin-Watson score reaches 1.966, which falls within the interval $1.5838 < DW \leq 2.4162$. This indicates that, after adding the Lag variable, the model analysis is free from autocorrelation disturbances.

Partial Test (T-Test)

The decision criterion is based on comparing the t-statistic score (t-hitung) with the t-table score (t-tabel) at a significance level of α (0.05), with degrees of freedom (df) calculated as $n - k = 35 - 2 = 33$ for each regression coefficient of the independent variables.

Model		t	Sig.
1	(Constant)	-3.308	.002
	ISR	3.353	.002
	ICG	1.880	.070
	LAG ROA	2.473	.019
a. Dependent Variable: ROA			

The test shows a t-statistic of 3.353, while the t-table value at α (0.05) with $df = 33$ is 2.035. Since $t\text{-statistic} > t\text{-table}$, H_0 is rejected, and H_a is accepted. Therefore, Islamic Social Reporting has an impact on the financial performance of Islamic Banks (ROA). The test shows a t-statistic of 1.880, while the t-table value at α (0.05) with $df = 33$ is 2.035. Since $t\text{-statistic} < t\text{-table}$, H_0 is accepted, and H_a is rejected. Therefore, Islamic Corporate Governance does not impact the financial performance of Islamic Banks (ROA).

Impact of Islamic Social Reporting on the Financial Performance of Islamic Banks in Indonesia

This study shows that Islamic Social Reporting (ISR) significantly impacts the financial performance of Islamic Banks in Indonesia. The hypothesis testing reveals that the t-statistic is greater than the t-table at a significance level of $\alpha = 0.05$. Therefore, ISR is a good predictor of financial performance, meaning that improvements in ISR scores enhance the financial performance of Islamic Banks in Indonesia. Specifically, a 1% increase in ISR leads to a 17.486% improvement in financial performance.

These findings align with previous studies by (Nurhayati & Rustiningrum, 2021), (Fatmala & Wirman, 2021), and (Sutapa & Hanafi, 2019), which also found that ISR influences financial performance. This study is consistent with (Adisaputra, 2021), who stated that social responsibility disclosures through ISR in Islamic commercial banks in Indonesia help improve financial performance. However, this result contrasts with (Trilaksono et al., 2021), who found that ISR does not significantly affect financial performance, and (Hadinata, 2019), who suggested a negative impact of ISR on Return on Assets (ROA).

ISR disclosures in Islamic Banks create a positive sentiment among stakeholders, especially Muslim customers in Indonesia. Increased disclosure of information through ISR raises customer trust, which in turn boosts profit scores and company performance, as reflected by ROA. For example, BTPN Syariah, with an ISR index above 0.6, consistently has an ROA above 5.0, while Panin Dubai Syariah, with a low ISR index of 0.37, has a low ROA of 0.00.

Islamic banks operate based on Islamic principles, so their social activities should align with the values in the Qur'an and Hadith. Social responsibility is not just a moral obligation but also an act of worship that reflects care for others and the environment. When Islamic banks actively engage in and report social activities, the public perceives them as trustworthy, which is crucial for gaining community support. As the community perceives the bank as responsible and caring, they are more likely to use the bank's services, which boosts the bank's profitability.

The more frequently and transparently an Islamic bank reports its social activities through Islamic-based standards like the ISR index, the better its financial performance. Conversely, when a bank rarely reports or engages in social responsibility, its financial performance tends to decline. This shows that a bank's financial success is not only dependent on business operations but also on its social responsibility efforts. Social performance can be measured through annual reports and the level of CSR funds distributed. Active involvement in community programs, such as health, environmental conservation, or empowering the poor through entrepreneurship training, builds a positive public image, which ultimately drives customer trust and increases company profits.

Impact of Islamic Corporate Governance on the Financial Performance of Islamic Banks in Indonesia

This study shows that Islamic Corporate Governance (ICG) does not significantly impact the financial performance of Islamic Banks in Indonesia. This is supported by the hypothesis testing, where the t-statistic is smaller than the t-table at a significance level of $\alpha = 0.05$. Therefore, ICG is not a good predictor of financial performance. Although higher ICG could theoretically improve financial performance, it is not a significant factor in this context.

These findings are in line with the study by (Trilaksono et al., 2021), which also found that ICG does not significantly affect the financial performance of Islamic Banks. The lack of influence of ICG in this study may be due to the fact that the assessment of corporate governance is not a primary concern for Islamic Bank customers. Corporate governance is generally understood by internal stakeholders, while financial performance measured by ROA is more

affected by operational performance, which depends on consumer perception. Additionally, the ICG evaluation in this study was based on self-assessment, which is subjective. This may lead to a lack of significant consumer trust in the ICG assessment results.

Corporate governance is a system and method for controlling a company to achieve its vision, mission, and objectives in a sustainable way, ensuring long-term operations. Islamic Banks, as entities with frequent interactions with stakeholders, are required to have good governance based on Islamic principles, namely ICG. Proper implementation of ICG according to sharia principles can improve financial performance, and thus, ICG could have a partial impact on the performance of Islamic commercial banks. However, if ICG is not implemented effectively and merely aims to meet disclosure requirements with a "sharia" label, it could negatively impact financial performance (Maulida, 2024).

The Impact of Islamic Social Reporting and Islamic Corporate Governance on the Financial Performance of Islamic Banks in Indonesia

This study demonstrates that, simultaneously, Islamic Social Reporting (ISR) and Islamic Corporate Governance (ICG) have a positive and significant impact on the financial performance of Islamic Banks. This is evidenced by the hypothesis testing results, where the F-statistic is greater than the F-table at a significance level of 0.05, with degrees of freedom $dk_1 = 32$ and $dk_2 = 34$. This shows that both independent variables, ISR and ICG, collectively have a significant influence on the financial performance of Islamic Banks.

ISR and ICG together significantly impact the financial performance of these banks. The support of corporate governance based on Islamic principles, combined with consumer evaluations of social responsibility, enhances the perception of Islamic banking products, which, in turn, improves the operational performance of the company. This finding aligns with the legitimacy theory, which suggests that companies undertake social responsibility in response to expectations and pressures from their environment, including economic, social, or political factors. According to legitimacy theory, for a company to survive, it must align its values with the values of the society in which it operates. Through annual reports, companies demonstrate their commitment to social and environmental issues to gain public support. When the public perceives a company as responsible and beneficial, they are more likely to accept and support its existence. This support is crucial for improving the company's reputation, attracting more customers and investors, and ultimately boosting profits and overall company value.

CONCLUSION

Based on the research findings, it can be concluded that Islamic Social Reporting has a significant partial effect on financial performance, meaning that every increase in the Islamic Social Reporting index will improve the financial performance of Islamic Banks in Indonesia. In contrast, Islamic Corporate Governance does not have a significant partial effect on financial performance, indicating that improvements in the application of Islamic Corporate Governance do not necessarily enhance the financial performance of Islamic Banks in Indonesia.

However, when considered together, both Islamic Social Reporting and Islamic Corporate Governance have a significant impact on financial performance, meaning that, simultaneously, they effectively explain the financial performance of Islamic Banks in Indonesia.

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