



DETERMINANTS OF ISLAMIC BANKING FINANCIAL PERFORMANCE: ANALYZING THE ROLE OF CSR, ZAKAT, AND GCG IN INDONESIA AND MALAYSIA

DETERMINAN KINERJA KEUANGAN PERBANKAN SYARIAH: ANALISIS PERAN CSR, ZAKAT, DAN GCG DI INDONESIA DAN MALAYSIA

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INFO ARTIKEL	ABSTRACT
<p><i>Histori Artikel:</i> Tanggal Masuk 14 Agustus 2023 Revisi Diterima 25 Maret 2024 Tanggal Diterima 26 Maret 2024 Tersedia Online 31 Maret 2024</p>	<p><i>The Islamic banking industry has shown rapid growth in recent years, becoming a primary focus in the financial sector. However, there remains a significant disparity in financial performance between Islamic and conventional banking. Therefore, the purpose of this study is to further investigate the factors influencing the financial performance of Islamic banks in Indonesia and Malaysia during the period 2015–2021. This study highlights the significant role of three main variables thought to affect the financial performance of Islamic banks: corporate social responsibility (CSR), zakat, and good corporate governance (GCG). Through a quantitative approach using panel data regression method, this research aims to explore the simultaneous and partial impacts of these three factors. The findings indicate that CSR, zakat, and GCG collectively have a significant effect on the financial performance of Islamic banks. However, when analyzed separately, only GCG demonstrates a significant influence, while CSR and zakat do not. This study provides recommendations for Islamic banks to continually enhance their CSR practices, zakat management, and implementation of GCG principles across all operational aspects. Thus, Islamic banks can strengthen their position and solidify themselves as leaders in the continually evolving Islamic banking industry.</i></p>
<p>Keywords: ROA, CSR, Zakat, GCG, Islamic Bank</p>	
<p>Kata Kunci: ROA, CSR, Zakat, GCG, Bank Syariah</p>	<p>A B S T R A K Industri perbankan syariah telah menunjukkan pertumbuhan yang pesat dalam beberapa tahun terakhir, menjadi titik fokus utama dalam</p>

sektor keuangan. Meskipun demikian, terdapat disparitas yang signifikan dalam kinerja keuangan antara perbankan syariah dan perbankan konvensional. Oleh karena itu, tujuan dari studi ini adalah untuk menginvestigasi lebih lanjut faktor-faktor yang mempengaruhi kinerja keuangan bank syariah Indonesia dan Malaysia selama periode 2015–2021. Studi ini mengangkat peran yang signifikan dari tiga variabel utama yang diduga memengaruhi kinerja keuangan bank syariah, yaitu corporate social responsibility (CSR), zakat, dan good corporate governance (GCG). Melalui pendekatan kuantitatif dengan menggunakan metode regresi data panel, penelitian ini bertujuan untuk mengeksplorasi dampak dari ketiga faktor tersebut secara simultan dan parsial. Temuan penelitian menunjukkan bahwa CSR, zakat, dan GCG secara keseluruhan berpengaruh signifikan terhadap kinerja keuangan bank syariah. Namun, ketika dianalisis secara parsial, hanya GCG yang menunjukkan pengaruh yang signifikan, sementara CSR dan zakat tidak. Studi ini memberikan rekomendasi kepada bank-bank syariah untuk terus meningkatkan praktik CSR, pengelolaan zakat, dan penerapan prinsip-prinsip GCG dalam semua aspek operasionalnya. Dengan demikian, bank syariah dapat memperkuat posisinya dan mengukuhkan diri sebagai pemimpin dalam industri perbankan syariah yang terus berkembang.

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1. Introduction

In recent years, global Islamic banking has grown its assets by up to US\$130 billion (Islamic Financial Service Board, 2022), indicating solid public support for this banking industry. Despite the significant growth, however, Islamic banking still needs help to outperform conventional banking since its market share is lower than the competitor (case in Indonesia and Malaysia). In 2021, Indonesia's Islamic banking market share was only 6.41%, much lower than its conventional banking at 93.59%. Meanwhile, the Malaysian conventional banking market share was 57.50%, superior to its Islamic banking at 42.50% (Bank Negara Malaysia, 2022; OJK, 2021). This issue underscores the urgency to investigate the elements that can enhance Islamic banking's financial performance to compete and outperform conventional banking.

Previous studies (Lee & Suh, 2022; Masvoic, 2018) explained that social and business factors are able to significantly contribute to improving a company's financial performance. Thus, this present study investigates the role of CSR and zakat funding as social factors as well as the role of GCG as a business factor in enhancing Islamic banking's financial performance in two countries, Indonesia and Malaysia. Companies that are consistent and competent in implementing CSR and zakat funding tend to maintain positive perceptions of stakeholders and, as a result, benefit from financial success (Faisal et al., 2020). Likewise, a good governance system will help a company because it can create a fair, appropriate, and effective performance (Mahrani & Soewarno, 2018). Therefore, combining the roles of CSR, zakat, and GCG is a

strategic approach in order to address the challenges faced by the Islamic banking industry and improve its financial performance.

Studies conducted in numerous countries have explored the factors that influence financial performance through the role of financial and social factors (Oh et al., 2015). However, most of them only focus on developed countries; therefore, new studies must explore the condition in developing countries (Nerlekar et al., 2021). Studies in the Southeast Asian region (Auliyah & Basuki, 2021; Mahrani & Soewarno, 2018; Tuan Ibrahim et al., 2020) revealed that CSR, zakat, and GCG have a significant effect on financial performance while others reported that CSR has a significant impact, but zakat does not (Astuti & Suharni, 2020; Faturohman et al., 2021; Trisna, Afifudin, & Anwar, 2020). Finally, studies conducted outside Southeast Asia (Al-Homaidi et al., 2021; Chenini et al., 2021; Gangi et al., 2019; Ho et al., 2019; Javaid & Al-Malkawi, 2018; Nerlekar et al., 2021; Platonova et al., 2018; Ramzan et al., 2021) discovered that CSR, zakat, and GCG take hold of financial performance in a company.

This study offers novelty by observing the integrative role relationship between CSR, Zakat, and GCG with Financial Performance. This approach is different from previous studies that only focus on CSR and Zakat, thus providing a comprehensive understanding of the factors that affect the financial performance of Islamic banks. Through involving GCG as a predictor, this study becomes unique and sharp in providing solutions to improve the ROA of Islamic banking.

This discrepancy prompts this study to examine the variables of CSR, Zakat, and GCG simultaneously so that the perspective of the financial performance of Islamic banking becomes more comprehensive, accurate, and appropriate for strategic decision-making. This study focuses on Indonesia and Malaysia as both countries hold a crucial position in shaping the growth and expansion of Islamic banking in the ASEAN region. Besides, they have a crucial contribution to the growth of the halal industry globally. Therefore, conducting a special investigation of the financial performance of Islamic banking in Indonesia and Malaysia is expected to increase the competitiveness of Islamic banking in these two countries against conventional banking at both local and global levels.

2. Literature Review

This study utilizes signaling theory as a basis for thinking. According to (Brigham, 2006), signaling theory is a practice that informs the prospects of a company to investors. Those that are able to publish their convincing company's prospects will raise the enthusiasm of investors to invest (Tabash, 2019). Profitability is a leading company prospect metric (Alarussi, 2021). However, the analysis is limited to the role of commercial factors. Therefore, studies need to explore more on spiritual values. This present study overcomes this gap by combining social and commercial roles through the involvement of CSR, zakat, and GCG. Thus, the view of signaling

theory becomes more comprehensive and meets the demands of today's Islamic banking investors.

Experts generally view financial performance through profitability because this factor represents the company's productivity in managing capital and resources (Abdallah & Bahloul, 2022). The maximum profitability ratio is ROA, defined as company's ability to generate profits in relation to its existing assets (Jihadi et al., 2021). ROA is measured based on the current year's profit distribution to total assets with an ideal metric $> 5\%$ (Lessambo, 2018). A large ROA means a significant company profit and, at the same time, indicates the company's ability to compete.

CSR (corporate social responsibility) refers to a company's commitment to actualizing responsibility toward marginalized communities and the environment (Mc Williams & Siegel, 2018). In the CSR program, Islamic banking supports marginalized communities by providing scholarships, free health services, compensation for orphans, donation to disaster victims, and restoring damaged environments (Kartini, 2020). This study measures CSR based on Islamic Social Reporting (ISR) indicators because they represent social justice for vulnerable communities and the environment, and they follow AAOIFI standards. Several experts have discovered the influence of CSR on financial performance; the result reveals that the effect is significant (Auliyah & Basuki, 2021; Coelho et al., 2023; Gangi et al., 2019; Ho et al., 2019; Homayoun et al., 2023; Mahrani & Soewarno, 2018; Ramzan et al., 2021). Based on the prior explanation, this study assumed that CSR is able to enhance the performance of Islamic banking entities. Thus, the hypothesis proposed is as follows.

H₁: CSR has a positive and significant effect on the ROA.

Islamic literature explains various types of zakat, including zakat al-fitr, zakat al-maal, professional zakat, and corporate zakat (Haron et al., 2021). This study only focuses on corporate zakat. Corporate zakat is a type of zakat paid by companies for business activities that have been carried out. It is based on the value of assets owned and added to the value paid by following *niṣâb* and *haul* (Alfitri, 2022). Zakat analyzed in this study particularly refers to the disclosure of zakat funding in the annual reports of Islamic banking. Previous studies have shown that zakat can affect financial performance (Al-Homaidi et al., 2021; Auliyah & Basuki, 2021; Javaid & Al-Malkawi, 2018; Tuan Ibrahim et al., 2020). This study adapted these findings by assuming that corporate zakat can significantly affect the financial performance of Islamic banking. In detail, we describe this assumption in the following hypothesis.

H₂: Zakat has a positive and significant effect on the ROA.

GCG (good corporate governance) is defined as corporate governance that is actualized credibly and comprehensively in order to fulfill the requirements and expectations of stakeholders (Cadbury, 1992). In today's Islamic banking, GCG is identified through the annual report of Islamic banking (Ginena & Hamid, 2015). Previous studies have established the link between GCG and

financial performance (Nerlekar et al., 2021; Ningsih et al., 2023; Nurul Amalia Nandasari et al., 2023). The findings guided the authors in formulating the following hypothesis.

H₃: GCG has a positive and significant effect on the ROA.

The descriptions above produce a model of Islamic banking financial performance. The complete picture of the model is presented in Figure 1.

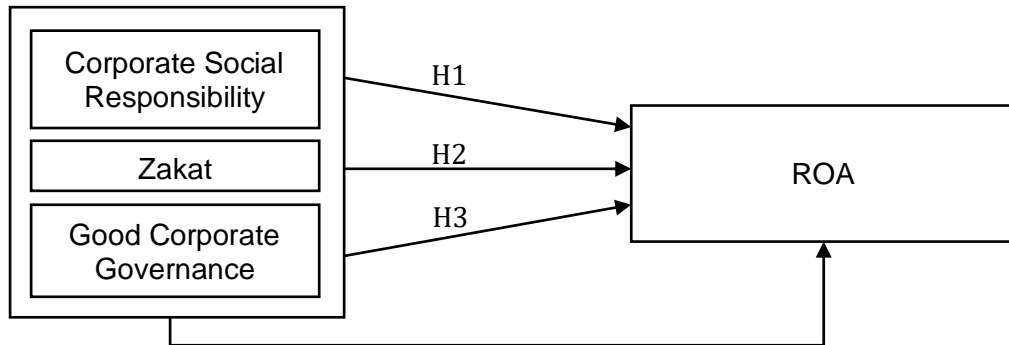


Figure 1. Research Model

3. Method of Research

This study employed a quantitative method with an explanatory approach. The population for this study was Indonesian and Malaysian Islamic banking which had been operating for more than ten years. The sample was selected through simple random sampling because this method allows all Islamic banks to be included. The research data was obtained from the published annual reports of the Indonesian and Malaysian Islamic banks for 7 years (2015-2021). Through the sampling method and the annual report period, this research obtained 98 observations.

This study used panel data regression with the random effect procedure (REM) as the analytical tool. The advantage of panel data regression is its ability to analyze extensive data by integrating time-series and cross-sectional data, thereby providing more robust results. Additionally, this analysis tool is highly proficient in analyzing complex and diverse data.

Table 1 below presents the operational definitions of each variable, which were crucial in assuring consistency throughout the study.

Table 1.
Operational Definition of Variables

Variable	Notation	Measurement	Scale
Dependent			
Financial Performance	ROA	Net income / total assets	Ratio
Independent			
CSR	CSR	CSR items disclosed in bank's annual report / total items in the Islamic Social Reporting index	Ratio
Zakat	ZAKAT	Zakat funding disclosed in bank's annual report / total items in the Zakat Disclosure Index	Ratio
GCG	GCG	GCG items disclosed in bank's annual report / total items in the Good Governance Business Syariah index	Ratio

Source: Author's analysis of the literature (2023)

4. Result and Discussion

4.1 Result

Table 4.1
Descriptive Statistics Estimation

	Mean	Max.	Min.	Standard Deviation
ROA (Y)	0.00551	0.03829	-0.05482	0.01045
CSR (X1)	0.68204	0.88000	0.40000	0.11216
Zakat (X2)	0.59438	1.00000	0.00000	0.24218
GCG (X3)	0.81663	0.97000	0.67000	0.07024

Source: Data processed with Eviews12

Table 4.1 presents the descriptive statistics of ROA, CSR, zakat, and GCG based on the criteria of average, maximum, minimum, and standard deviation values. This study observed 98 observations from 14 Islamic banks from 2015 to 2021. Regarding ROA, 0.00551 is the average value and the standard deviation is 0.01405. CSR shows a standard deviation value that is lower than the average CSR ($0.11216 < 0.68204$). Furthermore, zakat also shows an excellent standard deviation value because $0.24218 < 0.59438$. Finally, GCG shows a good average of 0.81, and the standard deviation is also reasonable because it is lower than the average value ($0.07024 < 0.81663$).

Table 4.2
Chow Estimation

Effects Test	Stat.	Degrees f.	Probability
Cross-sec. F	2.805163	(13,81)	0.0024
Cross-sec. Chi-square	36.427508	13	0.0005

Source: Data processed with Eviews12

Table 4.2 presents the outcomes of the chow analysis. The analysis indicates that the profitability value of the chi-square is 0.0005 (< 0.05). This suggests that H_0 is rejected, and the common effect model is deemed to be inappropriate for the analysis.

Table 4.3
Hausman Estimation

Summ.	Chi-Square Stat.	Chi-Square degree f.	Probability
Cross-sec. random	7.517997	3	0.0571

Source: Data processed with Eviews12

Table 4.3 presents the results of the hausman test. The analysis indicates that the profitability value of the cross-sec. random is 0.0571 (> 0.05), leading to the acceptance of H_0 . Therefore, the appropriate model for the analysis results is the random effect model.

Table 4.4
Lagrange Multiplier Estimation

	Cross-sec.	Time	Both
Breusch-Pagan test	4.188650 (0.0407)	1.146335 (0.2843)	5.334985 (0.0209)

Source: Data processed with Eviews12

Table 4.4 shows the results of the lagrange multiplier analysis. The value of both is 0.0209 (< 0.05) indicating the rejection of H_0 . As only one model can be applied, we find out the most appropriate model for the analysis results is the random effect model.

After conducting three-panel data analysis models, this study relied on the REM procedure. The results of the common effect estimation are as follows:

Table 4.5
REM Estimation

Var.	Coeff.	Std. Error	t-Stat.	Probability	Result
CSR (X_1)	-0.028568	0.310841	-0.790361	0.4313	Not Significant
ZAKAT (X_2)	-0.321278	0.145565	-0.229719	0.0688	Not Significant
GCG (X_3)	0.230252	0.048412	4.643074	0.0010	Significant
Probability (F-stat.) 0.000002					

Source: Data processed with Eviews12

Table 4.5 describes the findings of the hypothesis testing regarding the effect of CSR, zakat, and GCG on ROA. The empirical analysis reveals that CSR does not optimally affect ROA ($p > 0.05$), leading to the rejection of H_1 . Zakat does not significantly affect ROA ($p > 0.05$), so H_2 is also rejected. On the other hand, GCG can significantly affect ROA ($p < 0.05$), which means that H_3 is accepted. Finally, the table above shows that CSR, zakat, and GCG can simultaneously

influence ROA ($p > 0.05$). The results of the simultaneous influence test reveal that these three variables can be relied upon in generating Islamic banking ROA.

4.2 Discussion

This study shows that CSR is insignificant in influencing the ROA of Islamic banking in Indonesia and Malaysia. This finding explains that the efforts of Islamic banking in carrying out social activities, financing marginal micro businesses, and environmental conservation are not able to increase business profits. It means other factors have a significant influence. This finding does not align with previous studies (Coelho et al., 2023; Homayoun et al., 2023; Ramzan et al., 2021). Given this fact, this study encourages exploring more precise variables in predicting Islamic banking ROA.

This study also discovers that zakat could not be more optimal in influencing the ROA of Islamic banking in Indonesia and Malaysia. It indicates that the annual distribution of Islamic banking zakat to various sectors cannot increase profits. It implies that other factors are better able to affect ROA, including net profit margin, earnings per share, etc. This empirical study does not support previous findings (Tuan Ibrahim et al., 2020; Umiyati, 2020). Thus, the use of other variables will improve the accuracy of the predictions of ROA.

This study also analyzes the role of GCG as a determinant of ROA. The empirical results discover that GCG has a significant effect on the ROA of Islamic banking in Indonesia and Malaysia. This finding explains that the company's ability to run a professional management system, business according to rules, and total responsibility to consumers can increase company profits. This result is in accordance with previous studies (Nerlekar et al., 2021; Ningsih et al., 2023; Nandasari et al., 2023). Therefore, good GCG management will increase the capability of Islamic banking to enhance competitiveness.

Simultaneously, this study reveals that CSR, zakat, and GCG can influence the ROA of Islamic banking in Indonesia and Malaysia. This finding means that Islamic banking's concern for the social environment, distribution of zakat for the poor, and professionalism of corporate governance together can increase the profits of Islamic banking. Therefore, Islamic banking must recognize the existence of these three factors in enhancing the performance of Islamic banking.

5. Conclusion

The study investigates how CSR, zakat, and GCG affect Islamic banking's return on assets (ROA) in Indonesia and Malaysia. The actual results demonstrate that GCG significantly improves ROA while the role of zakat and CSR could be more optimal. In addition, the study indicates that the simultaneous role of GCG, zakat, and CSR can significantly impact ROA.

Theoretically, this study adds to the literature on Islamic banking profitability, particularly in Indonesia and Malaysia. Effective corporate governance is essential for improving the financial success of Islamic banking because GCG has a partial impact on ROA. The significant effect of CSR, zakat, and GCG on ROA demonstrates the importance of raising social programs, zakat distributing, and governance procedures to predict the future growth of Islamic banking. Therefore, a more promising future for Islamic banking in Indonesia and Malaysia can result from enhancing the GCG's partial function and the simultaneous roles of CSR, zakat, and GCG.

This study offers managerial implications for Islamic bank management as well. First, Islamic banking managers must grant the development of good corporate governance as their top priority because of its significant predictive ability on ROA. Increasing independence, accountability, obligation, equality and fairness, and transparency will be related to this good corporate governance. Second, the study demonstrates that a strategy to improve the general quality of social programs, provide an equal zakat distribution system, and encourage professional corporate governance will enhance the combined effect of CSR, zakat, and GCG on ROA. Implementing these two implications will increase Islamic banking's business viability in society.

Despite providing theoretical and managerial implications, this research still has limitations that need to be improved in future studies. First, this study only takes samples from fourteen Islamic banks, which consist of seven Indonesian Islamic banks and seven Malaysian Islamic banks. This limitation is caused by other Islamic banks that are not included in the samples because they do not fully disclose CSR, zakat, and GCG in their annual reports. Second, the period of observation in this research is only seven years due to the limited access to the annual report data before 2015, provided by several official websites of Islamic banks. Third, there are some test results that are not sufficient to comply with the theories used, including the dependent variables, such as financial performance measured by only ROA.

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