

Islamic Organizational Culture, Islamic Corporate Social Responsibility, and Corporate Performance: Evidence From Sharia Bank in Indonesia

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Received: July 19, 2019

Accepted: August 17, 2019

Online Published: August 26, 2019

doi:10.5430/ijfr.v10n6p118

URL: <https://doi.org/10.5430/ijfr.v10n6p118>

Abstract

This paper aims to examine the importance of Islamic organizational culture and Islamic corporate social responsibility in improving corporate performance. The population of this study is all sharia banks in Central Java – Indonesia. By using census sampling method, 327 sharia banks are determined as samples of the study. Partial least squares (PLS) approach is applied to analyze the data. The results reveal that Islamic organizational culture has a significant role in improving Islamic corporate social responsibility, which in turn, increasing corporate performance.

Keywords: Islamic organizational culture, Islamic corporate social responsibility, corporate performance

1. Introduction

Sharia banking has grown endlessly since its establishment in the mid-1970s. This industry is increasingly carving out most of the global financial markets (Frag, Mallin, & Ow-yong, 2014). From Ernst & World Islamic Banking Young Competitiveness Report in 2016, international sharia banking assets exceeded USD 778 billion in 2014 and estimated to reach the US \$1.8 trillion in 2019 on six major sharia markets (e.g., Uni Emirat Arab, Qatar, Arab Saudi, Indonesia, Malaysia, and Turkey) (Nazim & Kasbati, 2016).

In Indonesia, the existences of sharia banks that operate in banking services increasingly enliven the financial industry (Ifada, 2017). According to the numbers released by OJK (Financial Authority Service) in early 2017, the financial assets of sharia banks in exceeded 891 trillion rupiahs, with the market share rate of 5.18 percent from the total financial industry (Faisal, 2017). With the religious identity of sharia banks and other Islamic business organizations that incorporate the Islamic religion values in its operations, it is expected to have more social responsibility than conventional banking.

In worldwide, organization realizes the importance of corporate social responsibility (CSR) (IRI, 2017). Many theories have been developed in the CSR literature that tries to explain CSR and answer why the company reveals social information (Tilt & Rahin, 2015). A company assumed to have an indirect commitment towards the public to argue the importance of CSR (Garriga, 2004). One of the problems of CSR theory is the lack of entering thoughts and spiritual values. It is not solely based on human moral rationality. Frederick (1994) argued that religious values and attitudes are one of the important reasons to raise corporate social responsibility obligations. As Allah has stated in Al-Ma'idah verse 2 "And corporate in righteousness and piety, but do not cooperate in sin and aggression. And fear Allah; indeed, Allah is severe in penalty".

Companies that operate the following Islamic principles tend to embrace organizational culture based on the idea of trust, morality, and accountability (IRI, 2017). With a strong religious value inherent to all elements of sharia banks, it will strengthen the organizational culture oriented to the Islamic values and will decide to implement CSR with Islamic concept. Katamba (2010) stated that in the financial industry, organizational culture will create an organizational basis in formulating and managing social responsibility. The cultural formation of the desired Islamic organization is the result of integrated effort from all members of the organization (Hoque, Khan, & Mowla, 2013).

Islamic social responsibility (ISR) is the benchmark of social responsibility implementation of sharia banks which contains items compilation in term of CSR standards items determined by Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI). Raimi (2013) argued that Islam and other religions have relationships with

CSR. Buddhist values report, if it is used as an economic strategy, it could also overcome the shortage of CSR in alleviating the tribulations associated with the modern economic system (Kovács, 2014)

According to Lee & Kim (2017), the company that applies strategic redistribution to the public (CSR) increase the value of the company. Ghoul & Kim (2016) also showed that social and environmental practices improve competitive advantage. In the perspective of sharia economics, CSR concept as quoted from AAOFI related to ISR can also be seen as the realization of Infaq. If sharia banking conduct CSR which part in the form of company infaq and zakat, it will positively impact the economy of society including the condition of the company itself and the company performance will also increase.

This study is expected to give a contribution to literature review and hypothesis. The methodology of this study will be discussed in the third part. Therefore, in part four, this study presents and discusses empirical findings and end with the conclusion.

2. Literature Review and Hypothesis Development

2.1 Islamic Organizational Culture (IOC) and Islamic Corporate Social Responsibility

Organizational culture represents the collective value, trust and organizational principal members (Needle, 2004). The members of organization which under the Islamic organization, are not separated from the Islamic concept in the work implementation, as well as praying at working hours in the workplace, using Moslem outfit for female workers and so on. According to the Islamic perspective, every Muslim is obliged to apply rules according to sharia including ethical or organizational culture.

In the company, organizational culture will form the basis to formulate and manage social responsibility. Companies that operate following Islamic principles tend to embrace organizational culture based on the idea of trust, morality, and accountability (IRI, 2017). The indicators of Islamic culture include a very high social relations and social care level by spreading peace for the environment. As said by Rasulullah “*The best of people are those that bring the most benefit to the rest of mankind*”. This indicates that human existence including in the organization which is a group of people with the same purpose, is determined by the benefit to others. With the strong religious values inherent to all elements of the sharia banks, it will strengthen organizational culture oriented to the values of Islam and will decide to apply CSR with Islamic concept. CSR with Islamic concept has the purpose of creating a virtue that commanded by Allah in the form of zakat, infaq, charity, and waqf and then it is not through the riba activity. In the context of organizational culture (Pasricha, 2017) and (Katamba, 2010) prove that organizational culture affects CSR. Thus,

H1: Islamic organizational culture affects Islamic corporate social responsibility

2.2 Islamic Corporate Social Responsibility and Corporate Performance

The index of social disclosure to Islamic entity as stated by Maali, Casson, & Napier (2006) that there are zakat, qordul hasan, sharia supervisory board report about the transactions traits that violate the law (Haram), charity and social activities, disclosure of employees, late repayments and clients who suffer losses, environment, and other aspects of community involvement. It is sharing implementation of business organizations that demonstrate social responsibility following Islamic perspectives and commitment to maintaining social contracts in its operations. Some rules limited by the rules of halal and haram by sharia supervisory board towards how to obtain and utilize the funds.

The role played of sharia banks as Islamic financial institutions of society in social activities, is expected to improve organizational image that leads to organizational performance. In the study of stakeholder theory, it assumes that there is a positive effect between CSR and financial performance. From the conventional side that always measures the cost-benefit ratio, the benefits are greater than the costs incurred for social activities or the implementation of CSR to fulfill the interests of various parties. Furthermore, all of them will be able to improve the company's image and performance, but it is much more fundamental than this is to seek the blessing and ridha from Allah for the sharing culture to the society around the company. The empirical study of Lee & Kim, (2017) showed the company which conducts CSR improves corporate performance, as well as the finding of Farag et al. (2014) in 90 sharia banks in 13 countries. Therefore,

H2: Islamic corporate social responsibility affects corporate performance

2.3 Islamic Organizational Culture and Corporate Performance

Organizational culture from Islam perspective is value collection based on the Quran and hadith that helps organizational members to understand the goal of the organization (Hoque et al., 2013). Besides, Hoque et al., (2013) explained that to reach the organizational goals, the members of organization have philosophy understanding, vision,

mission, values, trust, norms, knowledge, and organization operation skills according to Qur'an and Hadith to gain Allah's ridha.

Organizational culture represents collective phenomenon arising from trust and social interaction of organizational members that contain the mutual value, understanding, confidence patterns, and the expectation of behavior that binds individuals in organization, together from time to time (Schneider 1987 in Uz Kurt, Kumar, Semih Kimzan, & Eminoglu, 2013). By having shared value, culture plays an important role in shaping the behavior of all organization members in facing certain key situations. The commitment from the organization member contributes to the success of the organization. Several studies in the literature have focused on the relationship between organizational culture and corporate performance (Bakhri, Udin, Daryono, & Suharnomo, 2018; Hersugondo, Pertiwi, & Udin, 2019; Ngo & Loi, 2008). Uz Kurt, Kumar, Semih Kimzan, & Eminoglu, (2013) showed the empirical support that organizational culture affects corporate performance. Thus,

H3: Islamic organizational culture affects corporate performance.

3. Research Methods

This study is intended to conduct a quantitative approach. The primary data uses Islamic organizational culture, Islamic corporate social responsibility, and corporate performance. The population of this study is 327 sharia banks in Central Java - Indonesia. Data is determined using census sampling method. Partial least squares (PLS) furthermore are applied to analyze the data. PLS is not only used to confirm theories, but also to explain the presence of relationships between latent variables. PLS can analyze the constructs that are formed by reflexive and formative indicators.

3.1 Measurement

Islamic organizational culture and Islamic corporate social responsibility use instruments which developed by (Hoque et al., 2013) include a group of values based on Quran, Sunnah, Ijma, and Qias. Corporate performance uses instruments which developed by (Govindarajan & Fisher, 1990).

4. Results and Discussion

The result of this study (Table 1) shows that every construct has a composite reliability value above 0.8 indicating internal consistency between constructs. It can be concluded that the construct of Islamic organization culture, Islamic corporate social responsibility measured by (Islamic economic responsibility, Islamic legal responsibility, Islamic ethical responsibility and Islamic philanthropic responsibility) and corporate performance have a good reliability. The value of loadings also above 0.70 which considered as valid.

Table 1. Reliability and validity testing

Construct	Cronbach's Alpha	Composite Reliability	(AVE)	R-Square
Firm Performance	0.961	0.974	0.741	0.041
IER	0.882	0.920	0.742	0.805
ILR	0.818	0.879	0.646	0.805
IEtR	0.906	0.941	0.842	0.854
IPR	0.711	0.834	0.626	0.417
ISLAMIC_CSR	0.932	0.943	0.65	0.756

The average variance extracted (AVE) value of all constructs is > 0.60 . It meets the reliability requirements. Similarly, the results of Cronbach's alpha are very good, which is above > 0.70 . The R-square of corporate performance is 0.041 and Islamic CSR is 0.756. The higher R-square means that the larger independent variable can explain the dependent variable.

4.1 Outer Model (Measurement Model)

Figure 1 shows the direct and indirect effect of Islamic organization culture and Islamic corporate social responsibility on corporate performance.

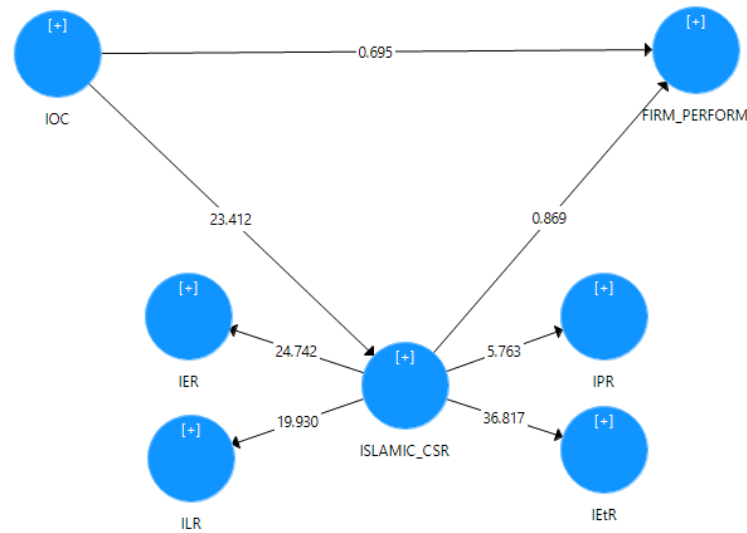


Figure 1. Structural model

In hypothesis testing, the analyzed value is T-statistic value and P-value resulted from PLS output. The hypothesis acceptance criteria are determined based on the significance rate (α) 5%.

Table 2. Hypothesis testing

Result for Inner Weights	Sample Estimated	STDEV	t-Statistics	P-Value
IOC → FIRM_PERFORMANCE	0.296	0.425	0.695	0.244
IOC → ISLAMIC_CSR	0.869	0.037	23.412	0.000
ISLAMIC_CSR → FIRM_PERFORM	-0.399	0.459	0.869	0.193
ISLAMIC_CSR → IER	0.897	0.036	24.742	0.000
ISLAMIC_CSR → IEtR	0.924	0.025	36.817	0.000
ISLAMIC_CSR → ILR	0.897	0.045	19.93	0.000
ISLAMIC_CSR → IPR	0.646	0.112	5.763	0.000
IOC → I_CSR → FIRM_PERFORM	-0.347	0.409	0.848	0.198

Based on Figure 1 and Table 2, it can be concluded that the effect of IOC on I_CSR is 0.869 and t-statistic value is 23.412 with significant p-value < 0.000. It performs that H1 is successfully supported. Meanwhile, the effect of I_CSR on corporate performance has a negative value of -0.399 and t-statistic value is 0.869 with significant p-value 0.193. It can be concluded that there is no evidence to support H2. As well as H3 where t-statistic value is 0.695 and p-value is 0.244. These results are far from the critical value ± 1.96 . It can be concluded that H3 cannot be supported.

The direct effect of Islamic organization culture on corporate performance is 0.296 and R^2 value is 0.041. It shows that corporate performance can be explained by Islamic organization culture and Islamic CSR with dimension (IER, ILR, IEtR, and IPR) of 4.1%. In Table 2, the indirect effect of Islamic organization culture on corporate performance via Islamic CSR is $0.869 \times -0.399 = -0.347$ with t-statistic value is $0.695 < \pm 1.96$. It can be concluded that Islamic CSR is unable to mediate the relationship between Islamic organization culture and corporate performance.

In this study, organizational culture is developed based on the Islamic point of view. According to Castro-González & Bande (2018) and Katamba (2010), organizational culture has an important effect on the disposition of CSR. The result of this study also shows the same finding where Islamic corporate culture influences on how the company runs its Islamic CSR. In this case, the cultural formation of Islamic organizations is not only formed by all members of the organization, however, it must also be supported and run by the owner of the organization. The owner holds the key role and determinant on how the system in the organization will run. It therefore can be said that if the owner of the

organization formed an Islamic organization culture and all members of the organization implement the work following the instructions from Allah with high commitment; it can be influential for Islamic CSR strategy.

The results also showed that ICSR does not affect corporate performance. This result is similar to the finding of (Lee & Kim, 2017) that CSR is not related to corporate performance. This happens because of the expected impact of Islamic CSR programs on sharia banks is not seen as significant for corporate performance since the programs held are supposed as long term programs. The results of this study furthermore showed that Islamic organizational culture does not affect corporate performance. This results showed that ICSR is unable to mediate the relationship between Islamic organization culture and corporate performance.

5. Conclusion

This study concludes that Islamic organizational culture has a significant role in improving Islamic corporate social responsibility, which in turn, increasing corporate performance. It is realized that this study has the limitation including the value of R-square obtained only 0.041. It means that the two variables (e.g., Islamic organizational culture and Islamic corporate social responsibility) are only able to explain 4.1% of corporate performance. Nevertheless, these results also allow an opportunity for future research to involve other variables or expand the research area.

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