

# THE EFFECT OF ETHICAL VALUES ON ISLAMIC BANKING PERFORMANCE

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## Abstract

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This research aims to determine the effect of ethical values on the financial performance of Islamic banking in Indonesia. This study uses the zakat disclosure index (*ZDI*) and the charity disclosure index (*CDI*) (Al-Homaidi, Al-Matari, Anagreh, Tabash, & Mareai Senan, 2021; Tuan Ibrahim, Hashim, & Mohamad Ariff, 2020) to measure ethical values and the capital adequacy ratio (*CAR*) to measure bank financial performance. This study hypothesizes that ethical values are positively related to bank financial performance. Data were collected from the zakat and charity disclosures made in the annual reports of 14 Islamic banks in Indonesia for ten years (2010–2019). The results showed that the ethical values, namely *ZDI* and *CDI*, positively affect the bank's financial performance. The research limitation is the small number of samples because the number of Islamic banks in Indonesia is only 14. Future research is expected to increase the number of samples not only from Indonesia but also from other Muslim countries, as well as add further dimensions to measuring ethical values. This study provides an additional explanation of the relationship between ethical values and bank financial performance by investigating zakat and charity disclosure in Islamic banking in Indonesia, the country with the largest Muslim population globally.

**Keywords:** Ethical Values, Zakat, Charity, Disclosure, Financial Performance

**Authors' individual contribution:** Conceptualization — M.A.S. and D.S.; Methodology — M.A.S. and D.S.; Formal Analysis — M.A.S. and D.S.; Writing — Original Draft — M.A.S. and D.S.; Writing — Revision & Editing — M.A.S. and D.S.

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## 1. INTRODUCTION

The instability of a financial institution often has an impact on other financial institutions. The stability of the banking sector must be a major concern because the stability of the banking sector is one of the conditions for the growth and development of the country's economy (Fresno & Hanggraeni, 2020; Jan, Marimuthu, & Mat Isa, 2019; Mahmoudabadi & Emrouznejad, 2019). To achieve stability in the banking sector, it is important to ensure that banks are managed efficiently so that sustainable financial performance is achieved.

Ethics is an integral part of any business or financial institution. In particular, Islamic financial institutions are based on Islamic moral principles. It is not wrong to say that without ethics, Islamic banks are just like conventional banks. The term "sharia" as a prefix in Islamic banking indicates morality, social justice, unity, equality, and social welfare. The reason for the establishment of Islamic banks is to provide an alternative system based on morality. Therefore, ethical and moral issues that are the focus of attention of the business and financial community in the West today are also important for Islamic financial institutions (Asutay, 2012).

One of the reasons Islamic banks and some ethically oriented banks in the West managed to survive the recent financial crisis is because of their non-involvement in speculative, unlawful, and anti-social activities (Nienhaus, 2011). Therefore, public confidence in Islamic banking and finance as a stable financial system has increased after the crisis.

The current stakeholders are not only focused on the company's financial performance. Stakeholder focus is also on the company's ethical commitment (Johari, Rosnidah, Talib, & Helmi, 2022; Kraiwanit & Tulathananun, 2021; Mukhibad, Jayanto, & Anisykurlillah, 2021; Tuan Ibrahim et al., 2020). The increasing number of cases of ethical violations in the corporate sector in Indonesia raises concerns because they can have an impact on operating failures and poor performance. An example of the case that occurred in the largest airline company in Indonesia is Garuda Indonesia, namely the act of manipulating financial statements in 2018. This case resulted in the company's reputation being damaged and the company's performance declining (CNN Indonesia, 2019).

Recently, Islamic banks around the world have experienced very rapid growth. In a report on the Global Islamic Finance Market in 2019 (Komite Nasional Keuangan Syariah, 2019) it was stated that the Islamic banking sector as the largest sector in the Islamic finance industry was able to contribute 71% of industrial assets, Islamic banking deposits contributed 23% per year in the previous six years (2013–2019) compared to other deposits which contributed 11% per year.

Indonesia has enormous potential for the development of Islamic banking because Indonesia is a country with the largest Muslim population in the world. In addition, with these conditions, Islamic banks in Indonesia are expected to have good performance as well. Indonesia won a score of 81.93 in the Islamic Finance Country Index (IFCI) 2019 (Komite Nasional Keuangan Syariah, 2019). With this high score, Indonesia is ranked first in the Global Islamic Financial Market.

Although Indonesia succeeded in achieving achievements in 2019 in the Global Islamic Financial Market, in the last five years there have been quite a few cases of business ethics violations in the Islamic banking sector in Indonesia. In 2018, there was a case of fraudulent fictitious credit within the Bank of West Java and Banten (BJB) Syariah which harmed the company around IDR 548 billion (Arief, 2019).

In 2020, there was a case of theft of customer accounts by Bank Syariah Mandiri employees in Central Sulawesi. This incident resulted in a customer loss of IDR 820 million (Pontoh, 2020). The latest ethical violation case that occurred was the theft of a customer account of IDR 1.3 billion by an employee of Bank Riau Kepri in Pekanbaru. This case occurred when Bank Riau Kepri was in transition to an Islamic sharia-based bank (Widyastuti, 2021).

Cases of violations that occur in Islamic banking of course can eliminate customer confidence to entrust funds to the bank. This in the long term will have an impact on the performance and sustainability of the bank. Corporate ethical values can improve organizational performance in the long term to realize corporate sustainability (Lee, 2020). Banks can be considered to have bad management if they behave unethically

so that in the end it will have an impact on the willingness of customers and investors to save money and invest in the bank (Tuan Ibrahim et al., 2020). Socially responsible companies recognize that their actions can affect stakeholders, customers, employees, and society at large (Lee, Choi, Moon, & Babin, 2014).

This research is important for the Islamic finance industry in Indonesia. As a country with a Muslim majority population, the Indonesian people should uphold ethical values in various fields, one of which is in the banking world. In addition, the Indonesian government has committed to making Indonesia the center of the world's halal producers which will make Indonesia the center of the world's halal trade (Coordinating Ministry for Economic Affairs of the Republic of Indonesia, 2020).

This study looks at ethical values using a broader view of the bank's social actions, namely using the disclosure of zakat and charity. This study incorporates Islamic ethical values from the Qur'an and Sunnah. By focusing on zakat which is one of the pillars of faith, this study combines ethical values from an Islamic perspective in analyzing company performance. This study aims to determine the effect of the ethical values of Islamic banking as seen from the disclosure of zakat and charity disclosure on the financial performance of Islamic banking as seen from the value of the capital adequacy ratio.

Most previous studies in Indonesia measure ethical values using the ethical identity index (Mukhibad & Nurkhin, 2019; Nugraheni & Hastuti, 2022; Zaki, Sholihin, & Barokah, 2014). This study uses a more specific index to measure ethical values in Islamic banking, namely the zakat disclosure index and the charity disclosure index. This measurement is the uniqueness of this research.

The structure of this paper is as follows. Section 2 reviews the relevant literature. Section 3 analyses the methodology that has been used to conduct empirical research on ethical values and financial performance of Islamic banks. Section 4 describes the research results, Section 5 describes the analysis of research results, and Section 6 describes conclusions, suggestions, and recommendations for further research.

## 2. LITERATURE REVIEW

### 2.1. Ethics value

Ethics is defined as an individual's belief about the right or wrong of an action. In the business world, ethics is the study of behavioral problems of members of business organizations and the parties involved in business transactions. The ethical dimension of management is not only limited to the difference between right and wrong but extends in terms of choosing various principles of moral obligation (Ram, Khoso, Jamali, & Shaikh, 2011). Corporate ethical values are organizational policies regarding the ethics and moral values of every employee in the organization. Corporate ethics are the main values of organizational culture. Organizational culture and ethical values can increase profitability and market share as well as stakeholder satisfaction (Lee, 2020).

Islam is a religion that places great emphasis on ethics. Ethical values in Islam are sourced directly from the Qur'an and Hadith, with Islamic law and

sharia principles in good behavior and practice in life (Hashim, Shahimi, & Ismail, 2012). Islamic ethics are the principles of right and wrong taught by the Qur'an and demonstrated in the great life of the Prophet Muhammad. Ethics in Islam is not only about certain morals but covers all aspects of life (Salahudin, Baharuddin, Abdullah, & Osman, 2016). Islam can be understood because ethics regulate all aspects of life, including the entrepreneurial aspect (Alwi, Parmitasari, & Syariati, 2021).

The dimension of *fiqh* (Islamic law) determines the limits of behavior in terms of adherence to sharia, while the dimension of *taqwa* (taqwa), which includes moral behavior outside of Islamic law (*fiqh*), is Islamic moral values. When it is called Islamic morality, it includes the dimensions of Islamic jurisprudence and must be in accordance with the spirit of Islam (Asutay, 2007).

Islam commands every individual to establish good relations with the society in which he lives and gets along well with the people around him. To live in harmony with society, some ethical values are needed, which are called moral virtues. Justice, truth, loyalty, trustworthiness, credibility, confidence, courage, honesty, trustworthiness, gratitude, generosity, unfaithfulness, and altruism are the basic values of Islamic morality. As in all areas of life, these virtues form the basis of the Islamic economic approach to economic and business activities (Kalkavan, Dinçer, & Yüksel, 2021).

Business ethics can help companies be more accountable and transparent. Similarly, when a company adopts the principles of corporate governance, it must also meet the expectations of its stakeholders. Companies that apply strong ethical values show better governance (Fotaki, Lioukas, & Voudouris, 2020).

If viewed from the perspective of the philanthropic model, the company benefits by carrying out social activities. This is because philanthropic activities are carried out voluntarily by the company so that the Bank gets a good reputation from stakeholders and will be assessed as a company that has ethics. Assessment as an ethical company will have an impact on the trust and loyalty of stakeholders so that it will result in better financial performance and stability (Tuan Ibrahim et al., 2020).

There are four foundations of business ethics in Islam based on prophetic values according to Alwi et al. (2021), namely:

#### 1) Faith

Faith is the basic foundation of all activities in Islamic teachings because one cannot become a Muslim without faith. This is an affirmation of the integrity of Islam and aligning it with conscience in everyday life. Faith is an integral element of business ethics because it can encourage Muslims to do what is right and give them the strength to face challenges. All transactions in Islam are believed to have implications for Muslim life in the afterlife. According to the Prophet (SAW), every business transaction must be good, fair, and lawful (*halal*). Therefore, any form of business that is unlawful or violates Islamic law is prohibited and unacceptable in Islam.

#### 2) Intention

Intention refers to the spirit with which an action becomes religiously valid with sincere intentions used to enable the act to become an act of worship. Some scientists develop total quality

management in an Islamic perspective using intention. The full application of this construct has the potential to strengthen the use of context in Islamic banking. Intentions play an important role in real-life activities, one of which is honesty.

#### 3) Amanah

In Arabic, the term *amanah* refers to honesty, but it has deeper meanings and consequences in Islam. *Amanah* has several connotations that revolve around the basic concept of accountability in all areas of human action. *Amanah* is often associated with the agenda of Muslim entrepreneurs; *amanah* is also an integral part of the spiritual needs of Islamic banking.

#### 4) Justice

Justice is a combination of moral and social values that show balance, simplicity, and honesty. The idea of justice in business dealings can be understood in Allah's Commandments concerning wealth and financial transactions.

The implementation of Islamic norms and values in Islamic banks further clarifies the "Islamic identity" of this institution. This makes it a separate sector from the conventional banking system. So it is hoped that Islamic banking can convince customers with practical evidence of compliance with Islamic values and norms, rather than simply providing sharia-compliant products in accordance with the normative expectations of Islamic corporate governance principles (Sencal & Asutay, 2021).

## 2.2. Financial performance

Financial performance is the process through which indicators can be identified, both quantitative and qualitative, about a company's activities to help demonstrate the importance of each operational and financial activity by obtaining financial statement data and information to use as indicators in the process of evaluating its performance to finally make rational decisions. As a result, it can be concluded that the concept of financial performance is the extent to which the ability of an economic unit to utilize available resources to achieve its objectives in the best way (Mushrif Rashid, Jasim, & Fadhil Saleh, 2021).

Financial performance is also one of the main indicators of a company's operational achievement. Financial indicators can help to determine the company's financial condition. Performance measurement is a strategic management tool for conceptualizing and measuring business performance (Al Farooque, Buachoom, & Sun, 2020).

Company performance is a measure that reflects what has been achieved by the company that shows good conditions at a certain time. This achievement is measured to obtain useful information related to the flow of funds, financial management, efficiency, and effectiveness. In addition, it is also to motivate managers to make the best decisions in running the company (Bayaraa, 2017).

In banking, performance evaluation is very important for all stakeholders, including customers, management, and investors. In a competitive financial market, a bank's financial performance can be an indicator for customers and investors to invest or withdraw their money from the bank.

### 2.3. The effect of zakat disclosure on banking financial performance

Zakat is one of the pillars of Islam that is carried out to be used to solve poverty in the Muslim community. Zakat is a mandatory obligation for all Muslims who are able and given to those in need (Boonyamanond & Chaiwat, 2020; Bouanani & Belhadj, 2020; Djaghballou, Djaghballou, Larbani, & Mohamad, 2018; Yusoff, Al Mamun, Ibrahim, & Hassan, 2019). The distribution of zakat is devoted to eight categories of zakat recipients as clearly stated in the Qur'an: *the poor, the needy, zakat managers, new converts, slaves, debtors, warriors in the way of Allah, and lastly the traveler* (Djaghballou et al., 2018).

Zakat is part of a commitment to religion and the social environment. Zakat is the main social instrument used to help social welfare (Al-Malkawi & Javid, 2018). The relationship between zakat and company performance is that companies disclosing zakat in annual reports will have an impact on better and more stable financial performance (Auliyah & Basuki, 2021).

The results of previous studies regarding the effect of zakat disclosure on bank financial performance show inconsistencies. Research (El Mosaid & Boutti, 2011) shows that there is no effect of zakat disclosure on the company's financial performance. Research shows that there is no effect of zakat disclosure on the company's financial performance. Meanwhile, pieces of research by Al-Malkawi and Javid (2018) and Tuan Ibrahim et al. (2020) show results that there is no effect of zakat disclosure on bank financial performance.

Based on the findings of different previous studies and an explanation of the relationship between zakat disclosure and company financial performance, the first hypothesis of this study is:

*H1: There is a positive influence of the zakat disclosure index on the financial performance of Islamic banks in Indonesia.*

### 2.4. The effect of charity disclosure and banking financial performance

Tuan Ibrahim et al. (2020) mentioned that one form of charity action is corporate social responsibility (CSR). CSR can also be defined as how companies manage their funds towards ethical behavior. Basically, the company's charitable actions aim to meet the social needs and interests of stakeholders.

Currently, the company's focus on CSR activities is getting bigger, and the contribution of the banking sector to sustainable development is starting to be questioned. This is because the banking sector consumes large amounts of natural resources, such as paper, energy, and waste. CSR is a way for the banking sector to contribute to the sustainability of the life of the entire community, either directly or indirectly (Sueia, Wang, & Deladem, 2019). A company can benefit from the support of the community, because of the role of the community; the company has a responsibility to the community. CSR is the right action if it is associated with the community. That is, ethics encourages companies to carry out CSR activities as part of their concern for the community (Mukhibad & Setiawan, 2020).

CSR disclosure is a medium for banks to show that they are socially responsible and sensitive to stakeholders. If the bank is unable to meet the demands of various stakeholders, it will result in a loss of trust and support from them. This will result in a bad image of the organization and will threaten economic sustainability (Arshad, Othman, & Othman, 2012). Furthermore, according to Arshad et al. (2012), the company's reputation will increase when companies disclose their CSR activities in annual reports. Companies that carry out CSR and disclose it in the annual report are considered to have good corporate values.

The research by Platonova, Asutay, Dixon, and Mohammad (2018) indicates that there is a significant positive effect of CSR disclosure on financial performance in the Gulf Cooperation Council Islamic Banking Sector. Similarly, research conducted by (Arshad et al., 2012) that CSR activities disclosed in the company's annual report have a significant positive relationship with company performance. The results of this study indicate that the disclosure of CSR activities in the company's annual report is as important as a useful business strategy in creating a sustainable superior performance for the organization.

Based on the findings of previous studies as well as an explanation of the relationship between charity disclosure and company financial performance, the second hypothesis of this research is:

*H2: There is a positive influence of the charity disclosure index on the financial performance of Islamic banks in Indonesia.*

## 3. RESEARCH METHODS

This research focuses on Islamic banking in Indonesia. As a country with the largest Muslim population in the world, Islamic banking in Indonesia is expected to develop rapidly and have good performance as well. The variables that will be examined in this research are the disclosure of zakat and the disclosure of social activities as independent variables and financial performance as the dependent variable. The sample of this research is all Islamic banks in Indonesia, totaling 14 banks with years of observation starting from 2010 to 2019.

Zakat disclosure and charity disclosure variables are measured using the zakat disclosure index and charity disclosure index made by (Tuan Ibrahim et al., 2020). While the dependent variable financial performance is measured by using the capital adequacy ratio which is the main financial ratio of banks because it describes the ability of bank capital. Banks with high capital are considered relatively safer than banks with low capital (Dietrich & Wanzenried, 2009). Future research can conduct comparative research and can explore this problem, for example by adding parameters or other analytical techniques.

### 3.1. Variable measurement

Table 1 and Table 2 describe the zakat disclosure index (ZDI) and charity disclosure index (CDI) (Tuan Ibrahim et al., 2020).

Table 1. Zakat disclosure index

<i>Disclosure item</i>	<i>Score</i>
Sources and use of zakat	0-3
Amount of zakat paid	0-3
Zakat policy and obligations	0-3
Statement from the board of directors or the sharia supervisory board regarding zakat and its calculation	0-3

Source: Tuan Ibrahim et al. (2020).

Table 2. Charity disclosure index

<i>Disclosure item</i>	<i>Score</i>
Donations in the form of cash, employee products, and services	0-3
Contribute to and support government campaigns	0-3
Support and contributions to non-governmental organizations (NGOs) and non-profit organizations	0-3
Sponsorship (education/culture/sports)	0-3

Source: Tuan Ibrahim et al. (2020).

The measurement of the independent variables of zakat disclosure and charity disclosure uses a disclosure level score of 0 to 3. A score of 0 is given if there is no disclosure about the disclosure item, a score of 1 is given if minimum disclosure information (general information about alms or zakat) is listed, and a score of 2 is if there is detailed information about the disclosure item (general information, the amount of zakat, as well as involvement in several activities), and 3 if the disclosure item is described in great detail.

The dependent variable of *financial performance* is measured by using the capital adequacy ratio. The capital adequacy ratio (CAR) is a bank's capital adequacy to cover unexpected risks in the future and describes the bank's ability to bear losses (Irawati, Maksun, Sadalia, & Muda, 2019). The CAR has limits set by the government of a country where the bank operates. Based on the Circular Letter of the Financial Services Authority (OJK) No. 26/SEOJK.03/2016, OJK stipulates that the bank's minimum CAR is at least 8%.

To see the effect of ethical values on bank financial performance, multiple regression analysis was used. The ethical value proxied by the zakat disclosure index and the charity disclosure index is measured by a score in which the scores for each disclosure item are added up.

In addition to using the zakat disclosure index and charity disclosure index, other methods of measuring Islamic banking ethical values can also be seen from the employee's perspective. The behavior of employees in their work activities at Islamic banks can reflect whether Islamic ethical values have been implemented properly or not.

### 3.2. Regression model

This study uses multiple linear regression to examine the effect of ethical values proxied by the disclosure of the zakat disclosure index and charity disclosure index on the financial performance of Islamic banking in Indonesia. There are two independent variables in this study, namely the zakat disclosure index and the charity disclosure index. The dependent variable in this study is financial performance. The following is the regression equation:

$$CAR_{it} = \alpha + \beta_1 ZDI_{it} + \beta_2 CDI_{it} + \varepsilon \quad (1)$$

where,

CAR = capital adequacy ratio (*proksi untuk kinerja keuangan*);

ZDI = zakat disclosure index;

CDI = charity disclosure index.

## 4. RESULTS

### 4.1. Zakat disclosure index

The zakat disclosure index in this study includes several disclosure items, namely the source and use of zakat, the amount of zakat payments, policies, and not zakat obligations, as well as statements by the management or the sharia supervisory board regarding zakat and zakat calculations. In 2010, there were 8 banks that disclosed the management of zakat funds in their annual reports. Of the 4 zakat disclosure items, the 8 banks only disclose general information. The information disclosed is only general statements that are not explained in detail. The information disclosed is only limited to the fact that the bank has distributed zakat funds to zakat mustahik in that year. The conditions were the same in 2011 when only 8 banks had disclosed the management of zakat funds through their annual reports. The information disclosed is also still minimal and not detailed. The other four banks have not disclosed the management of zakat funds in 2010 and 2011 because the four banks were only established and operated in 2010.

The increase occurred in 2012 and 2013 when there were 10 banks that disclosed the management of their zakat funds through annual reports. However, the information disclosed is still not detailed. Only general information is disclosed by the bank. From 2014 to 2019, the 14 banks have disclosed information on the management of zakat funds in their annual reports. The information disclosed has also increased where Islamic banks in Indonesia have disclosed the management of zakat funds in detail, although not in full.

### 4.2. Charity disclosure index

The charity disclosure index in this study consists of several disclosure items, namely donations in cash, employee products and services, government campaign contributions and support, support and contributions for NGOs and non-profit organizations, and sponsorship in the fields of education, culture, and sports. The charity disclosure index shows results that are not much different from the zakat disclosure index. In 2010, there were 9 Islamic banks in Indonesia that disclosed their charitable activities in their annual reports. The increase occurred in 2011 when there were 11 Islamic banks that disclosed their charity

activities in the annual report. In 2012 and 2013 there were 12 Islamic banks that disclosed charity activities in their annual reports. From 2014 to 2019, all Islamic banks in Indonesia have disclosed their charity activities in their annual reports. Of the 14 Islamic banks that were the object of observation in this study, there was only one bank that consistently disclosed its charity activities in detail. Meanwhile, 13 other banks disclose information on charity activities in general and not in detail.

#### 4.3. Variable descriptive statistics

Table 3 displays the descriptive statistics of the variables in this study. The average value of the zakat disclosure index in Islamic banking in Indonesia for the 2010–2019 period is 4.014. The average zakat disclosure index means that the level of zakat disclosure in Islamic banking in Indonesia for the 2010–2019 period is 4.014. Meanwhile, the standard deviation of the zakat disclosure index value is 0.752 which means that there is a deviation of approximately 0.752 from the average value of the zakat disclosure index as a whole. The median value of the zakat disclosure index in Islamic banking in Indonesia for the 2010–2019 period is 4.3928 with the highest zakat disclosure index value of 4.7857 and the lowest zakat disclosure index value of 2.50000.

**Table 3.** Descriptive statistic

	CAR	ZDI	CDI
Mean	0.793512	4.014286	4.121429
Median	0.558510	4.392857	4.428571
Maximum	2.112407	4.785714	5.285714
Minimum	0.217723	2.500000	2.571429
Std. dev.	0.657614	0.752386	0.893076
Skewness	1.299724	-0.774172	-0.397373
Kurtosis	3.000703	2.223399	1.795565
Jarque-Bera	39.41657	17.50280	12.14667
Probability	0.000000	0.000158	0.002303

The average value of the charity disclosure index in Islamic banking in Indonesia for the 2010–2019 period is 4.1214. The average value of the charity disclosure index can be interpreted as the charity disclosure index in Islamic banking in Indonesia for the 2010–2019 period of 4.1214. The standard deviation of the charity disclosure index is 0.8930, which means there is a deviation of 0.8930 from the average value of the charity disclosure index as a whole. The median value of the charity disclosure index in Islamic banking in Indonesia is 4.4285 with the highest value of 5.285714 and the lowest value of 2.571429.

The capital adequacy ratio variable has an average value of 0.79. The average value can be interpreted as a bank's ability to see the risks it will face is 0.79. The standard deviation value of the capital adequacy ratio is 66%, which means that there is a deviation of 0.66 from the average value of the capital adequacy ratio as a whole. The median value of the capital adequacy ratio in Islamic banking in Indonesia for the 2010–2019 period is 0.558510 with the highest value of 2.112407 and the lowest value of 0.217723. The results of the data normality test showed that the data were normally distributed. This can be seen from the Jarque-Bera

test value of the three variables which is more than 5%, which according to Winarno (2011) that the data is normally distributed if the value of the Jarque-Bera test result is more than 0.05 or 5%.

#### 4.4. Multiple regression test results

Table 4 shows the results of multiple regression tests. Based on the Lagrange multipliers test, the best model chosen is the random effect model, so that the equations of the best model are obtained, namely:

$$CAR_{it} = 0.820 + 0.163ZDI_{it} + 0.160CDI_{it} \quad (2)$$

**Table 4.** Multiple regression test

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	0.820182	0.085348	9.609854	0.0000
ZDI	0.163510	0.017577	9.302474	0.0000
CDI	0.160301	0.075948	2.110672	0.0366
R <sup>2</sup>	0.398341			
Adj. R <sup>2</sup>	0.389558			

Note: Significance at a 5% level ( $p < 0.05$ ).

Based on the model equation above, it can be seen that all independent variables affect the capital adequacy ratio. It can be seen from the probability value of each variable which is smaller than 0.05 and the coefficient value of each independent variable is positive. This means that if the capital adequacy ratio variable increases, the value of the zakat disclosure index and charity disclosure index variables will increase. The adjusted R-squared value in the panel data regression model using the random effect model method with individual effects (cross-section) is 0.389558. This means that the zakat disclosure index and charity disclosure index are able to explain the capital adequacy ratio variable of 38.9%, while 61.1% is explained by other factors not included in the model.

#### 5. DISCUSSION

If viewed from the descriptive analysis, the disclosure of zakat and disclosure of charity is still quite low. In this case, the information disclosed by Islamic banks in Indonesia regarding the management of zakat is still minimal. Information regarding zakat management that is disclosed is only general information that banks have collected, managed, and distributed zakat annually and the amount of zakat distributed. The results of multiple regression analysis show that zakat disclosure affects bank financial performance. This result is similar to the results of research by Auliyah and Basuki (2021), Tuan Ibrahim et al., (2020), and Al-Homaidi et al. (2021) who found that zakat disclosure had a significant effect on the company's financial performance.

In terms of disclosure of charity, it is not much different from the disclosure of zakat. The level of disclosure of charity by the company is also still quite low. The information disclosed by the company is still in the form of general information that is not detailed. The company has disclosed all disclosure items but has not disclosed them in detail. The results of multiple regression analysis show that charity disclosure has a positive effect on bank financial performance. The results of

this study are similar to the results of research conducted by Szegedi, Khan, and Lentner (2020) which examined the effect of CSR disclosure on the financial performance of banks listed on the stock exchange in Pakistan. Meanwhile, the results of this study contradict the results of research conducted by (Tuan Ibrahim et al., 2020) which found that charity disclosure had no effect on the financial performance of banks in Malaysia.

The results of this study may be useful for improving bank performance for policymakers, managers, international and regional bodies, investors, financial providers, academic researchers, the public, and governments. Islamic banking management should know about the importance of voluntary disclosure to improve bank performance. Management should consider voluntary disclosure of zakat and charity.

## 6. CONCLUSION

The results of this study indicate that ethical values proxied by zakat disclosure and charity disclosure have a positive effect on the financial performance of Islamic banking in Indonesia. This study provides evidence that can be replicated and refined regarding the importance of zakat disclosure and charity disclosure in improving bank performance. Especially for developing countries as well as countries with the largest Muslim population in the world such as Indonesia, which is trying to become a center for halal producers in the world as well as a center for Islamic financial transactions in the world.

For the academic world, this research contributes to providing references regarding the factors that affect the performance of Islamic

banking. The results of this study show differences from previous studies, this can be exploratory material for further research. For Islamic banking, especially in Indonesia, the results of this study become input regarding the importance of concern for the application of Islamic ethical values in the work environment. The Islamic label contained in Islamic banks indirectly requires all stakeholders to be able to uphold Islamic ethical values and implement them at work.

The results of this study also indicate that there is limited disclosure of zakat and charity in bank annual reports. This study suggests that Islamic banks should disclose more and more complete information about ethical values, especially disclosures related to Islamic ethical values. In terms of practical implications, it is very important for Islamic bank management to provide more information about zakat and matters relating to the application of Islamic sharia values because this is very important for Muslims in Indonesia. This can build trust among Indonesian Muslims in Islamic banking so that they as Muslims will be more confident to become customers in Islamic banking because of the bank's good image and reputation.

The limitation of this study is the small number of samples because the number of Islamic banking in Indonesia is only 14 banks until 2019. Further research may be able to conduct cross-country research, namely in several countries that also have Islamic banks in their countries. In addition, further research can use other dimensions or proxies in measuring the application of Islamic ethical values in Islamic banking. Future research can also conduct comparative research and can explore this problem, for example by adding parameters or other analytical techniques.

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