

Effect Of Financing For Islamic Banking On The Profitability In Indonesia

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Abstract: The purpose of this research is to prove the performance of Financing for Islamic banking in Indonesia. Based on most types of financing that are already operating, this study will prove is financing profitable for Indonesian Islamic Banking? And which financing is most profitable in Indonesian Islamic banking? The research method used is descriptive research with quantitative approaches and empirical studies on Islamic Commercial Banks registered at Bank Indonesia during 2013-2017. This study uses secondary data through the official website of the Islamic Commercial Bank. With purposive sampling there are 43 data and tested using multiple linear regression analysis. Result of the analysis proved that Murabahah, Mudharabah, Musyarakah and Ijarah Financing are profitable. The most profitable is mudharabah, while the lowest contributing to profit is Ijarah financing. These finding can be used as a reference for banking institutions to take strategic decisions related to the development of Islamic banking in Indonesia.

Index Terms: Profitability, Financing, Islamic Banks, Indonesia

1. INTRODUCTION

Indonesian Islamic banking is currently growing rapidly. In fact, many conventional banks have developed Sharia Business Units (UUS). This condition caused intense competition between banks, so the Bank was required to plan a strategy to attract the interest of its customers. As of June 2018, there are 13 Sharia Commercial Banks, 21 Sharia Business Units, and 166 Sharia Community Financing Banks (OJK, 2018). This phenomenon is almost the same as SMEs, in the current era of globalization. SMEs are required to make changes in order to improve their competitiveness, this impacts more quickly in the banking sector (Azizah, 2017). Based on the positive development of Islamic banking, a measure of development is needed such as profitability. Profitability is a very important element in assessing bank financial performance. Profitability describes the ability of a company to earn profits through sales, cash, capital, number of employees, number of offices and others. (Harahap, 2008). A method for assessing profitability is the ratio of Return on Assets (ROA). ROA or return on assets is a way of calculating a company's financial performance through a comparison of net income with the total assets of a company. The greater the ROA, the greater the profitability of the bank. (Dendawijaya, 2009).

From figure 1, it shows fluctuations in profitability for BUS in Indonesia during 2012 to 2017. The highest ROA in 2012 and the lowest in 2014. In 2014 there was a significant decline, this was because the inflation rate reached 8.36% which had an impact on the performance of Islamic banks. Then the development of ROA in 2014 until 2017 continues to increase (Bank Indonesia, 2018).

TABLE 1

Comparison of ROA and Financing for Sharia Banks in 2018

Months	Financing (in Milion)	ROA (%)
January	275.163	0.42
February	276.677	0.74
March	280.818	1.23
April	281.634	1.23
May	283.759	1.31
June	289.481	1.37
July	292.306	1.35

Source: Islamic Banking Statistics (data processed).

According to Pratama et al. (2017) an increase in the amount of financing affects the increase in the amount of profitability. Conversely, if financing decreases, profitability also decreases. However, based on table 2, not all amounts of financing are directly proportional to the profitability obtained as in July 2018.

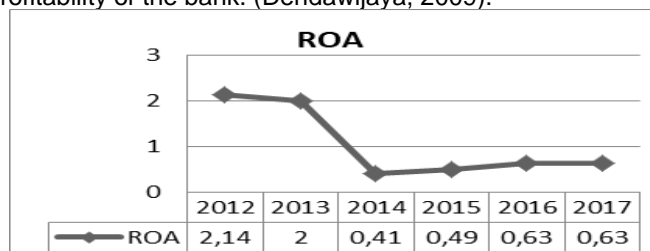


FIGURE 1: Profitability (ROA) of Islamic Banks in 2012-2017 (%)

Source: Islamic Banking Statistics (data processed).

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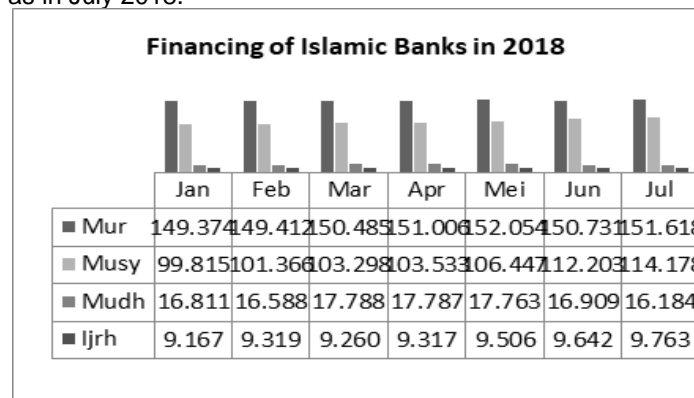


Figure 2: Financing of Islamic Banks in 2018 (in millions)

Source: Islamic Banking Statistics (data processed).

The highest BUS financing is a murabahah contract, which is a financing contract for a sale and purchase transaction between the capital owner and the buyer (customer). The owner of capital sells goods by confirming the purchase price of the goods to the buyer. The selling price of the item is obtained from the purchase price plus the profit in accordance with the agreement of both parties. Prices may not change throughout the contract (Muljono, 2015; Ahmad & Ahmad, 2018). Muslim et al. (2014) stated that Murabaha had a positive effect on profitability while Widiyanti et al. (2016) Murabaha had no effect on Profitability (ROA). Furthermore, financing with the Musyarakah contract is a cooperation agreement between two or more parties to form a particular business. Each party must contribute funds. The rate of profit is divided by agreement, while the loss is based on the portion of the contribution of funds. The greater the musyarakah financing channeled it will increase the profitability of Islamic banks (Pratama, 2017). Ogilo (2016), Wibowo and Sunarto (2015) stated that Musyarakah financing had a positive effect on profitability, but Rahayu et al (2016) stated that it had a negative effect on profitability. In addition, financing with mudharabah contract is a contract of cooperation between capital owners (shohibul maal) and capital managers (mudharib). Shohibul Maal's capital entrusts mudarib to manage capital. The profit level is divided according to the agreement at the time of the contract while the risk of loss is borne in full by the shohibul maal, except for losses caused by mistakes and deviations from mudharib (Muljono, 2015). Pratama et al (2017) Rizal and Mahendra (2016) stated that Mudharabah financing had a positive effect on the level of profitability, while Faradila et al (2017) and Afkar (2017) stated that mudharabah had no effect on profitability. Lastly, financing lease with Ijarah is an agreement between the owner of the goods from the tenants who allow tenants take advantage of such goods. The tenant pays rent to the owner of the goods in accordance with the agreement of both parties. According to Muljono (2015) the greater the ijarah financing, the greater the level of profitability. Ogilo (2016) and Pratama et al (2017) state that ijarah has a positive effect on profitability, while Faradila et al (2017) Ijarah has no effect on profitability. The type of financing examined in this study is the most important financing offered by Islamic banks in Indonesia. So that the results of this study can be used as a reference for banking management to determine the banking strategy in the future.

2. LITERATURE STUDY AND HYPOTHESIS DEVELOPMENT

This study used the Stewardship Theory by Donaldson and Davis in 1989 which was built on the basis of philosophical assumptions about human nature, namely in essence can be trusted, able to act responsibly, have integrity and honesty towards others. Based on the theory further developed in the research model used in this study as follows:

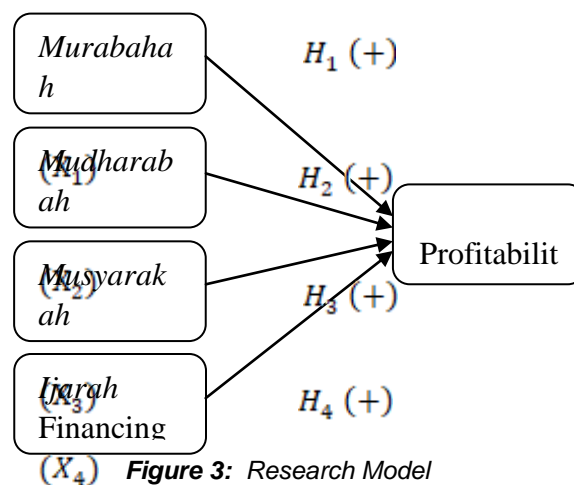


Figure 3: Research Model

Murabahah financing in Islamic banks is a sale and purchase transaction between the bank and the customer in which Islamic banks are sellers and customers as buyers. Islamic banks must notify the acquisition price of the goods the customer will buy and the level of profit determined by agreement between the two parties. In line with the theory of stewardship where the bank (steward) does not only prioritize the interests of the company but prioritizes its customers as well as the aim of prospering the community and the bank benefits from the sale of these goods. Mulim (2014), Sari (2015) and Faradila et al. (2017) states that murabahah financing has a positive effect on profitability. Murabahah is one of type of financing that possible to provide profit for banks. Based on the reason, hypothesis declared as :

H1 : Murabahah financing has a positive effect on profitability.

Mudharabah financing is a collaboration between sharia banks (shahibul maal) and customers (mudharib) where banks provide capital to customers to make business. The level of profit is divided according to the agreement of both parties and the loss is borne by the bank during the loss is not due to customer negligence in carrying out its business (Muhammad, 2013). In line with the theory of stewardship where the bank (steward) serves customers (principals) by providing capital and entrusting the capital to customers to form a business. Ogilo (2016), Rizal and Mahendra (2016), Susi and Devi (2016), Pratama et al. (2017) states that mudharabah profit sharing financing has a positive influence on profitability. Mudharabah financing is the most profitable financing for banks. Based on the reason, hypothesis declared as :

H2 : Mudharabah financing has a positive effect on profitability.

Musyarakah Financing is a profit sharing transaction between two or more people who collect funds and integrate all resources to form a business. Both parties contribute funds with the provision that the profit rate is divided according to the contribution of funds (Muljono, 2015). Based on the theory of stewardship where the bank (steward) has collective behavior is not only concerned with its own company, characterized by the existence of cooperation between banks and customers to form a business. Sari (2015), Ogilo (2016), Pratama et al. (2017) states that musyarakah financing has a positive effect on profitability. Bank usually get some profit from Musyarakah Financing as productive financing. Based on the reason, hypothesis declared as :

H3 : Musyarakah financing has a positive effect on profitability.

Ijarah Financing is a lease agreement for an item between the party that rents (muajjir) and the tenant (mustajjir) for a certain period of time agreed upon. In line with the theory of bankruptcy, the bank (steward) acts according to the wishes of the customer (principal) to rent an item and does not override the interests of the company. Ogilo (2016) and Pratama et al. (2017) states that ijarah financing has a positive effect on profitability. Ijarah is rent agreement that profitable for rental company then some institution like banks. Based on the reason, hypothesis declared as :

H4 : Ijarah financing has a positive effect on profitability.

3. RESEARCH METHOD

The type of research used in this study is quantitative research with a population of all Sharia Commercial Banks registered at Bank Indonesia through a purposive sampling technique. The sampling technique in this study through the following stages:

TABLE 2
Sampling Technique

N	Criteria	Number
O.		
1.	Islamic Bank registered at Bank Indonesia	13
2.	Islamic banks do not fit the criteria	(3)
3.	Number of sample companies	10
4.	Number of sample data 2017 (10x5)	50
5.	Incomplete data sample	(7)
6.	Number of sample data	43

Source: Islamic Banking Statistics (data processed).

Independent variables in this study are murabahah (X1), mudharabah (X2), musyarakah (X3) and ijarah (X4) financing. While the dependent variable in this study is Profitability (Y) which is measured using Return on Assets (ROA). Technique of analysis in this study used multiple linear regression analysis. Classic assumption test is used to test the data before use multiple linear regression. Multiple linear regression analysis is used to see the relationship between the independent variables namely murabahah, mudharabah, musyarakah, and ijarah financing towards profitability. The regression equation used is as follows:

$$Prfit = \alpha + \beta_1 PMur + \beta_2 PMudh + \beta_3 PMusy + \beta_3 Pijr + e$$

Description:

- Prfit : Profitability
- α : Constant
- β : Regression Coefficient
- PMur : Murabahah Financing
- PMudh : Mudharabah Financing
- PMusy : Musyarakah Financing
- Pijr : Ijarah Financing
- E : Error

4. RESULT AND DISCUSSION

Before the influence test was carried out, this study used the classic assumption test in the form of normality, multicollinearity, heteroscedasticity and autocorrelation. All classical assumption tests were passed, so that it was followed by multiple linear regression tests with the following results:

The multiple linear regression equation is as follows:

$$Prfit = -33.715 + 0.348 PMur + 0.474 PMudh + 0.339 PMusy + 0.310 Pijr + e$$

The Adjusted R Square (R2) is equal to 0.689. This means that the ability of independent variables namely murabahah, mudharabah, musyarakah, and ijarah financing can explain the variation of the dependent variable namely profitability as reflected by return on assets (ROA) of 68.9% and the remaining 31.1% explained by other variables. The partial test results (t-test) in this study, test whether murabahah, mudharabah, musyarakah and ijarah financing partially have a positive effect on profitability as reflected by return on assets (ROA).

TABLE 3
T Test Results

	t-count	Sig.	Regression Coefficient
H1	7.673	0.000	0.348
H2	4.689	0.000	0.474
H3	8.129	0.000	0.339
H4	2.513	0.016	0.310

Source: Islamic Banking Statistics (data processed).

4.1. Effect of Murabahah Financing on Profitability

Partial test results obtained $t_{count} > t_{table}$ that is $7.673 > 1.68595$ and a significant value of $0,000 < 0,05$, murabahah financing has a positive effect on profitability. Murabahah financing has a smaller risk compared to other financing because it is a short-term investment with profits set at the beginning so that it reduces the risk of bad financing. Easy management and a fast process make murabahah financing much in demand by the public. So from that murabahah financing is an Islamic bank asset that is useful for increasing income and will affect the level of profits obtained by the bank.

4.2. Effect of Mudharabah Financing on Profitability

The partial test results show the value of $t_{count} > t_{table}$ is $4.689 > 1.68595$ and a significant value of $0,000 < 0,05$, then mudharabah financing has a positive effect on profitability. Mudharabah financing is financing with a large risk due to the fact of profit uncertainty. If the customer's business goes well, the bank will get a large profit in accordance with the proportion of profits that have been agreed upon during the contract. But if the customer's business suffers a loss, the bank will bear the risk of not making a profit. Islamic banks apply a prudent or selective system in selecting mudharabah financing customers, so that Islamic banks can control the risks posed by mudharabah financing to maintain bank profitability.

4.3. Effect of Musyarakah Financing on Profitability

The partial test results showed that $t_{count} > t_{table}$ is $8.129 > 1.68595$ and a significant value of $0.000 < 0.05$, then musyarakah financing has a positive effect on profitability. Musharaka financing transactions are based on the desire to increase the value of assets held jointly by combining all resources. The Bank is very careful in providing financing to customers because this financing is long-term. However, the profits generated are also long-term. This means that if the

financing produces large profits in the long run, it will have an impact on the bank's financial profitability that is significant and consistent in the long run. So that Islamic Banks are very careful in choosing prospective customers of this type of financing, and only good business will be funded by the Bank.

4.4. The Effect of Ijarah Financing on Profitability

Partial test results obtained by $t_{count} > t_{table}$, namely $2.513 > 1.68595$ and a significant value of $0.016 < 0.05$, then ijarah financing has a positive effect on profitability. Ijarah financing is one of the distribution of funds in the form of leases made by Islamic banks with their customers for a certain period of time that has been mutually agreed upon. The customer pays the rent to the bank without being followed by the transfer of ownership rights to the leased item. Banks get profits through rental services, especially on high value rental goods. Therefore, banks strongly prioritize ijarah financing with high-value goods so as to produce a large profit for the Bank.

5. CONCLUSION, LIMITATION AND CONTRIBUTION

1. Murabahah financing has a positive effect on profitability because this financing is a type of short-term financing that has a low risk.
2. Mudharabah financing has a positive effect on profitability because banks are very careful in providing this type of financing, so even though it is at high risk, this financing still produces profits for the bank.
3. Musyarakah financing has a positive effect on profitability because banks can selectively select the type of business of the customer so that this financing can generate long-term profit for the bank.
4. Ijarah financing has a positive effect on profitability because banks choose high value ijarah products so that they generate more profits for the bank.

This study is limited to only the dominant types of financing available in Islamic banks, so that not all types of financing can be measured in this study. So that if the development of the other parties' financing, further analysis is needed. The results of this study can be utilized by banking businesses in processing data financing. In addition, the results of this study can also be used as information in making decisions related to the development of Islamic banking in the future.

6. IMPLICATION

The implication in this research is for bank directors and managers regarding decision making in banking. the decision taken is expected to increase the profitability that the bank expects for the development of the banking business. so the results of this study are used as a reference so that decision making techniques in banking related to increasing profits can run on target.

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