



The Influence of Savings, Equity, Non Performing Financing and Profit Sharing on The Financing of Islamic Banks in Indonesia

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ABSTRACT

The importance in Islamic banking is a healthy process of financing. Financing is the main indicator to measure the growth of Islamic banking. Financing is funding spent to support the planned investment, either self-operated or managed by a third party. In determining the distribution of funds, there is a scheme using a principle of profit sharing (profit and loss sharing). Mudharabah is an agreement in which the owner of the fund business provide all the funds, while fund managers act as manager, and the profits divided among them according to the agreement while the financial loss is borne only by the owner of the funds. Musyarakah is agreements for a certain business, where each party provides the fund contribution within agreement that the profits is divided accordingly while the loss is divided based on the portion of the funding requirements. This study examined whether savings, equity, Non Performing Fund (NPF) and Profit sharing affect the financing of Islamic Banks. Statistical methods used in this study is a multiple regression analysis and hypotheses are tested using t test. The results of this study showed that partially, savings, NPF and profit sharing have significant effect on the financing of Islamic Banks whereas partially, equity has no effect on the financing.

Keywords: Savings, Equity, Non-Performing Financing, Profit Sharing, Financing

1. INTRODUCTION

The development of Islamic banking in Indonesia begins with the establishment of Bank Muamalat Indonesia (BMI) on 1 November 1991, followed by the release of Act Law No. 7 in the year of 1992, which allows the bank's operations with profit-sharing system. Currently, the growth of Islamic banking in Indonesia showed encouraging development. This development is characterized by the development of Islamic Banking office networks. According to the statistics of the development of Islamic banking, in January 2009, the number of Islamic Banks (BUS) is as much as 5 BUS, however, it has grown into 11 BUS by October 2010 (Islamic Banking Statistics, 2010).

Financing is a key indicator to measure the growth of Islamic banking. Growth performance of Islamic bank financing remains high until January 2009 with a



performance of good financing (NPF below 5%). The statistics also shows that the development of Islamic Banking in January 2009 have consistently continued to increase with a growth of 32.3% in September 2009 and the increase to be 33.3% in September 2010. Data from Central Bank of Indonesia (BI) shows that Islamic banking fund raising activities in the form of demand deposits, savings and time deposits with a growth rate 43% higher than the same period in 2010 by 35%. A better practice in applying the precautionary principle when extending financing as well as a better risk- management skills has resulted in a decline in ratio of Non-Performing Financing (NPF), which decreased into 4.00% for the period September 2010.

There are some factors that can affect the distribution of funds / financing to communities namely savings and equity as factors that show the efficient use of resources, NPF as the controlling factor of cost and risk positions, and the percentage of revenue as a factor that indicates the level of competence of financial institutions or banks (Pratin-Adnan, 2005).

2. LITERATURE REVIEW

2.1 Islamic Banking

Sharia Bank is operated based on Islamic law in which it is based on the rule agreement between the bank and other parties who deposit their funds or financing or other banking activities (Kasmir, 1999: 38). According to Act Law no. 10 of 1998 which is an amendment to Act Law no. 7 of 1992 concerning banking, Islamic banks are commercial banks conducting business based on Sharia principles in their activities providing services in fund payment activities.

2.2 Savings

Bank as a financial institution has a function of collecting funds from the public. Therefore it must have sources in raising its funds before channeling it back to the market (Machmud and Rukmana, 2010: 26). Savings is a third-party funds or public funds which is deposited into and kept in the bank, which then can be withdrawn at any time without prior notice to the bank (Zulfiki, 2003:93). According Zainul Arifian (2006: 47), cash savings is funds owned or controlled by the bank in a form of cash, or other assets that can be readily converted into cash. Collection of funds in Islamic banks can take in forms of demand deposits, savings and time deposits. Islamic Operational principles applied in raising funds are wadiah and mudharabah (Sholahuddin, 2005: 22).

2.3 Equity



Bank is an institution of trust which is gained by sustaining adequate funds. Therefore Fund is a very important factor for the development and progress of maintaining public confidence in banks (Muhammad, 2005: 244). Fund is money coming from the banks or shareholders plus share premium and results of operations from banking operations (Riyadi, 2003: 77). Zainul Arifin (2002: 135) said that capital represents the interests of owners in a company. Based on book value, fund is defined as net wealth (net worth), namely the difference between the book value of assets less the book value of liabilities (liabilities).

2.3 Non-Performing Financing (NPF)

The failure of banks is shown by the increased number in their non performing financing which could cause the losses banks. One of the risks faced by banks is a credit risk in conventional bank or a risk of non performing financing in Islamic banks. Credit risks arises if the bank is not able to get back installments of principal and or interest on a loan or investment made (Arifin, 2006: 225). The main cause of the credit risk/non performing financing is financing that is easily distributed (Sutojo, 2000: 186). According to Amir Machmud and Rukmana (2010: 106), a good understanding of the main causes of the Non-Performing Financing (NPF) will be an important considerations of the banks in order to establish a comprehensive and prudential policy analysis on understanding the funds which considers all inherent risks in any fund investment decision.

2.4 Profit Sharing

One of the reasons why someone saving the money in the bank is to obtain interest. High interest rates will encourage someone to save and sacrifice current consumption to be used in the future (Smithin, 1994 in Yendrawati & Margasati, 2007:595). According to the Shafi'i Antonio (2001), Muhammad (2002), and Karim (2004), the level of financing costs (profit margin) has effect on the number of Islamic bank financing request. A lower rate of profit margin / profit sharing in comparing with the average national rate shows a more competitive Islamic financing (Pratin and Adnan, 2005). Profit sharing is defined as a form of cooperation between the investors and the saving account owners, the term is shahibul maal with the manager or mudarib, and there will be profit sharing in a form of the percentage share of profit sharing (ratio) referring to the agreement between two parties.

2.5 Financing

The importance in Islamic banking is a healthy process of financing. A Healthy financing is financing that imply to a lawful and safe financing which is also able to



generate returns as expected. In general financing is financing or expenditures to support funding of planned investments either self-operated or managed by a third party. In a narrow sense, financing is used to define a financing of such Islamic bank to its customers (Muhammad, 2005: 304). The main function of Islamic banks is to collect and distribute funds. The funds are granted by Islamic banking to finance the borrowers in need, either for working capital or consumption.

There are several schemes of distribution of funds used in Islamic Banking. Two of them are Mudharabah and musyarakah (Wiroso, 2005: 137). Mudharabah is a business cooperation contract between two parties in which the first (lenders) to provide all of the funds, while the second party (the fund manager) to act as manager, and the profits divided among them according to the agreement while the financial loss is borne only by the owner of the funds (SFAS 105-IAI, 2007).

Musyarakah is a partnership agreement between two or more parties to a particular business, where each party contributes funds provided that the profits are shared based on the agreement while losses by serving the needs of the fund (SFAS No. 106, 2007). Financing the principle of sharing the Mudharabah and musyarakah is different from the principle of fixed interest at which banks will finance charge revenue (customers) a fixed rate regardless of the amount of profit generated customer, even though loss and crisis.

2.6 Conceptual Framework

Islamic banking is one of the alternatives for the financing needs of the community. Musyarakah and Mudharabah financing are the most preferred by the people due to the fact that in Musyarakah, the society acts as the manager of the funds. In Musyarakah the borrowers do not have to worry about their capital to start a business. They just only need to focus on the work needed by the project. Whereas in Musyarakah the capital is partly funded by the public as users of capital and by banks (Islamic Banking Community, 2011).

Based on previous studies, there are several factors related to the disbursement of financing. The most dominant factors of financing are savings (deposits, Third Party Fund), equity, non-performing financing (NPF, financing problems), and profit sharing.

Savings (DPK) is a public fund which is deposited to the bank as an intermediary institution, savings bank is a major source of funding in the conduct of its business, and the capital itself is a source of funds that have a role as a buffer to absorb operating losses and other losses. Savings and capital can be used as a fund to finance. The level of



non-performing financing (NPF) and the results can also affect the financing. Problematic funding such as bad debts will result in an increasing number of NPF funds; when the fund to be redistributed is not collectable. In a long run it can affect the going concern of the banks.

Moreover profit sharing will also affect the amount of financing disbursed. If the financing goes well, the benefits gained as a result of operations should be larger. The sharing of percentage of the profit sharing agreed upon will increase the amount of bank revenue which further increases the amount of financing to be distributed.

2.7 Hypotheses

The purpose of this study is to see the impact of the savings, equity, NPF, and profit sharing on the financing of Islamic banks in Indonesia during the period 2007 to 2010:

Hypotheses of the research are as follows:

- H1: Savings is partially influence the financing of Islamic Banks in Indonesia***
- H2: Equity partially influence the financing of Islamic Banks in Indonesia***
- H3: Non-Performing Financing (NPF) partially influence the financing of Islamic Banks in Indonesia***
- H4: Profit Sharing partially influence the financing of Islamic Banks in Indonesia***

3. RESEARCH METHOD

Object of research used in this study is Sharia Commercial Banks (BUS) in Indonesia listed in Islamic Banking Statistics Report, Bank Indonesia during the years 2007-2010 (Bank Muamalat, Bank Syariah Mandiri and Bank Mega Syariah). Islamic banks become the choice because the Islamic banks conducts their operation to raise funds from the public and distribute it back to the community in the form of financing, based on the teachings of Sharia and the principle of Islam. The research was limited to the period 2007-2010. The population in this research is Sharia banking companies registered in Bank Indonesia listed in Islamic Banking Statistics report (SPS) for the period 2007-2010. This study use the purposive sampling in selecting a sample of the population. So the researchers collected a sample in accordance with the predetermined criteria of the population. The criteria of the sample are: (1) Banking companies are included in the



category of Islamic Banks, (2) Sharia Commercial Banks registered in Bank Indonesia for four consecutive years, namely in 2007, 2008, 2009 and 2010, (3) Sharia Commercial Bank publishes quarterly financial statements during the period 2007 to 2010.

This study exercised secondary data derived from quarterly financial statements of Islamic banks are presented on the website of each Islamic bank and quarterly financial reports obtained from the website of Bank Indonesia. A literature review is conducted which refer to theories and previous studies related to this research.

The data analysis in this study is using multiple linear regression analysis. Equations used in this study is

$$Y = a + b_1 X_1 + b_2 X_2 + b_3 X_3 + b_4 X_4 + e$$

4.RESULT AND DISCUSSIONS

The result of the t test in this research shows an equation as follows:

$$Y = 125,418 - 5,348SAV - 1,061EQ + 8,015NPF - 0,641PS + e$$

The test results showed that partial three of the four independent variables (Savings, NPF and profit sharing) have a significant influence on the dependent variable (financing), while the capital itself does not significantly affect the financing.

Savings (SAV) affects the financing with a significance of 0.000. The results of this study showed a significant negative correlation; it means that the higher savings can be collected by the bank; the amount of funding that is channeled down. NPF (NPF) significant positive effect of 0.000 on financing, which is means the higher ratio of the amount of financing NPF also growing up. Profit sharing (PS) significantly affects financing with a significance of 0.000. The results of this study showed a significant negative correlation; it means that the higher value of the results obtained by the bank the amount of financing disbursed is decrease. Equity (EQ) with a significance number of 0.201 has no significant effect on the financing.

5. CONCLUSIONS AND RECOMMENDATIONS

5.1 Conclusions

Based on the research that has been done, it can be summed up as follows: This study examines the influence of deposits, equity, Non-Performing Financing (NPF) and the results of the financing on Islamic Banks in Indonesia. From the results of the partial regression testing, three of the four independent variables investigated, namely Savings,



NPF and Profit Sharing display significant influence on the financing of Islamic banks in the years 2007-2010, while the other variable of Equity has no significant effect on financing of Islamic banks in the year 2007-2010. Savings displayed a significant negative effect on financing. The Islamic banks reduce the amount of financing disbursed by banks to concentrate on reducing the ratio of NPF / non-performing loans and to hold expansion on financing.

NPF has a significant positive effect on financing. As written in Business Indonesia, an increase in the distribution of funding coupled with an increase in the ratio of the amount of financing problems (Non Performing Financing / NPF). Those are due to a static level of income with an increasing need of financing especially for the funding of working capital.

The profit sharing is the amount of income earned by the bank from its financing activities. One of the reasons why Islamic banks reduce funding even though the yield increases is because the bank wants to maintain its ratio on NPF and restrain its expansion on financing.

Equity has no effect significant to financing of Islamic Banks in Indonesia. Equity is one of the factors used to calculate CAR (Capital Adequate Ratio) as an indicator of the ability of absorption losses as a maximum credit / financing. Therefore the banks do not solely rely on the equity because banks can obtain loans and subordinated debt as supplementary equity.

5.2 Limitations of Research

Limitations of this study are as follows:

1. This study has limitations that researchers only examined three Islamic Banks whereas until the end of 2010 there were 11 Islamic banks registered in Bank Indonesia. It is because other 8 Islamic banks were not been registered in 2007 and did not issued quarterly financial statements for the year study conducted by the researchers from 2007 until 2010.
2. For variable Non Performing Financing (NPF) in this study, researchers used the ratio of the NPF that are already available on the publication of quarterly financial statements issued by bank umum Sharia. The NPF variable can not be recalculated / manual by researchers because according to the NPF is funding formula non current divided by the total financing, data on non-current financing can not be published by the Islamic banks.



3. Due to the limitations of existing data, for the variable results of researchers conducted an interview with the directorate of Islamic banking at Bank Indonesia to ensure that the calculation of the results.

5.3 Suggestions

Based on the constraints faced by the researchers on this study, it can be given some suggestions in order to improve the quality of future research. For that future studies should:

1. Expanding the sample firms other than Islamic banking Islamic Banks also use Sharia as the study sample.
2. For the next study period, try in future studies using the current-year period so that the research results can describe the conditions for the development of Islamic banking.
3. Use one of the existing types of Islamic financing such as Mudharabah or ijara as the dependent variable (the dependent).

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