

Banking: According to Islamic Syaria Concepts and Its Performance in Indonesia

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This study investigates empirically Islamic Syaria Banking concepts and to determine the performance of its based on Bank Indonesia Act No.9/1/PBI/2007 on assesment system for performance level to Commercial Banks based on Islamic Principles which consists of the aspects: capital, assets, management, earning, and likuidity which called CAMEL. The all of aspects use financial ratios as follow CAR, ROA, NPF, OEOI, FDR and Depositor Funds as a comparison as a reflect level of public trust on Islamic banking. Samples were taken from Bank Indonesia as a central bank period of 2007-2009 with 31 sample of Islamic Bank (BUS, UUS, BPRS) which was chosen based on a purposive sampling method. Using descriptive method and multiple regression analysis, the results of this study indicate that the Islamic banking have a good performance reflected CAMEL on Depositor Funds.

Field of Research: Islamic Banking

1. Introduction

Bank is a business entity which collects funds from the public in savings and share to the public in loans or other forms in order to improve the standard of living of the majority. In this decade, Indonesian finance launch Islamic financial system in order to accommodate the Indonesian people that majority is *moslem*. Islamic system in Indonesia has expanded into the capital markets, insurance, mortgage, savings and loan institutions, banks, etc. It enriches the Islamic system over the conventional system was used that interesting to compare the performance and future prospects especially. Historical progress of Islamic banking in Indonesia as you can see at Figure 1. Formally began with the Workshop MUI on banking in 1990, which was subsequently followed by the issuance of Banking Act No.7/1992 about banking which accommodate banks activities with profit-sharing principle. However, during the period 1992-1998 there was only one Islamic Commercial Bank (BUS) and several Islamic Rural Bank (BPRS) as the perpetrators of Islamic banking industry. This is due during the six years of operation there is practically no other regulator that supports the system of Islamic Banking operation. The absence of these legal tools to support of Islamic Banking products to conform such as conventional product, as a result the characteristics of *syaria* (Islamic law) be disguised like conventional banks. The government made a strategic step development of Islamic banking that is granting permission to the conventional commercial banks to open branches Islamic Business Unit (UUS) namely a conversion of conventional banks into Islamic banks. This strategy is also a response and initiative from the changes in the Banking Act No.10/1998 as the successor Act No.7/1992, which expressly Islamic Banking Systems positioned as part of the national banking system.

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In 2008 the Government issued Islamic Banking Law No.21/2008, that expected to provide a more solid legal basis and greater opportunities in the development of Islamic Banking in Indonesia so that equal and parallel to the conventional banks. The impact of Islamic Banking Act provides a positive thing, the progress of Islamic banking branch until the end of 2009, among others 6 BUS, 25 UUS and 139 BPRS, if compare 2005 BUS grew 100%, UUS grew 86%, and BPRS grew 51%. The institutional side of the spread of Islamic banking branch network also experienced rapid growth. In 2009, adding service outlets have as many as 199 branch become 1.223 branch office and 1.742 office channeling (service Islamic bank in the conventional banks).

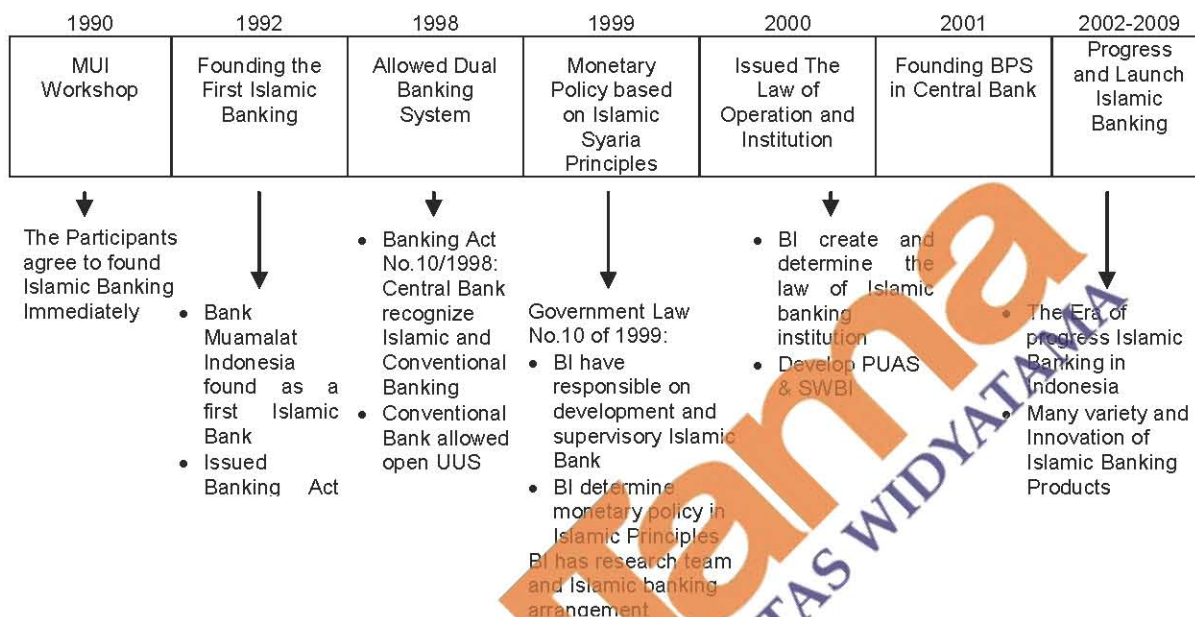


Figure1. The Historical Progress of Islamic Banking

The growth of financing Islamic banking in 2009 reach Rp.46.9 trillion, grew 22.8%, Financing to Deposit Ratio (FDR) 89.7%, ROA 1.5%, ROE 26.1%, CAR 10.77% and 4.0% for NPF. Seen the financial statements of Islamic banking in 2009 had good ratios, Financing grow above 20%, FDR below 100%, CAR and NPF above provisions. Astuti (2007) add that the good performance for Islamic banking because they implement the good corporate governance (GCG), implement the precautionary principle for Islamic banking and implement risk management well. Meanwhile, the growth of depositor funds in 2009 rich 41.7% or Rp.52.3 trillion to last year, this growth was the highest since 2005, that we can be concluded that significant growth is a sign of Islamic banking in Indonesia is on the growth stage, but in total, the depositor funds and market share of Islamic banking only 39% and 6.4%. of the total deposits of the nation. This indicates that the performance of conventional banking is still dominant compared with the performance of Islamic banking.

Becomes important (Budiharto;2001 and Wijaya;2004) that to see the performance Islamic banking through CAMEL can increase public trust who have excess funds an increase in savings and also an increase new customer numbers which influence on increasing depositor funds in Islamic banks. If the performance through financial ratios in CAMEL well, it will have an impact on increasing depositor funds, this means that the market provides a significant response.

2. Literature Review

Islam is a *deen* (Way of Life) practically, which teaches all things good and beneficial to mankind, regardless of time, place or stages of its development. Islam is a *fitrah* religion, which according to human nature. Financial and banking activities can be viewed as a place for modern society to bring them to two kinds of *syaria* of the Al Quran, namely:

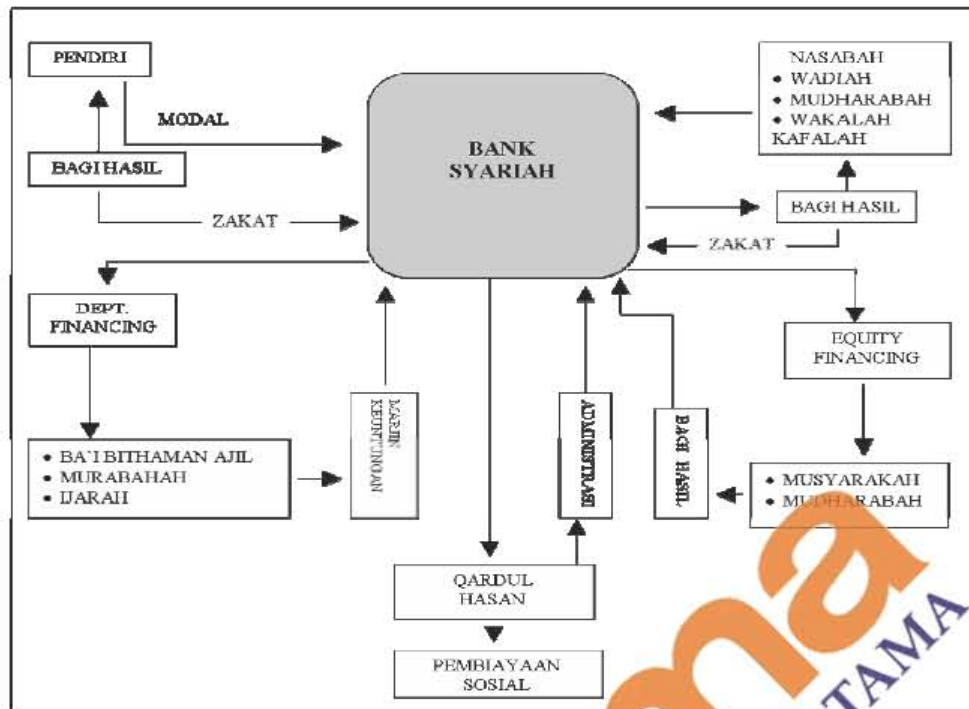
- Principle of *Al Ta'awun*, namely mutual assistance and cooperation among members of society for good, as stated in the Al Qur'an: "*Dan tolong menolonglah kamu dalam (mengerjakan) kebajikan dan taqwa, dan jangan tolong menolong dalam berbuat dosa dan pelanggaran*" (QS 5:2)
- The principle of avoiding *Al Iktinaz*, which is holding the money (fund) and let it idle and does not rotate in transactions that the benefit for publics, as stated in the Al Qur'an: "*Hai orang-orang yang beriman, janganlah kamu saling memakan harta sesamamu dengan jalan batil, kecuali dengan jalan perniagaan yang berlaku dengan suka sama suka di antara kamu...*" (QS 4: 29)

Just like other financial intermediary institutions, the basic mechanism of Islamic bank is to receive funds from customers and channel money to other customers in need. The difference in the provision of benefits received both of customers and banks, which is conducted with appropriate financing schemes in Islamic law that free of *riba*-free. In principle there are five concepts in its operations, as follow:

- Contract (*Akad*); all transactions must use *wa'ad ala wa'ad* (promise over promise) where there are two clauses promise. The first clause of what promises associated with itself and the second clause dealing with the consequences if the promise is ignored.
- Profit-Sharing; used the concept of Islamic bank is profit sharing. Customer funds channelled by the bank in financing the scheme. The revenue of the financing will be divided according to contract between customer and bank
- Financing Targets; bank was restricted of Islamic principles in distribute the funding. Financing should not be distributed on business sectors that opposed or forbidden the Islamic law, such as gambling business, beverages and foods that are forbidden.
- Customers are Partners; for Islamic banking customers are business partners, not a customer who require funds and who save their funds in the banks, so that business can be run based on mutual need.
- Profit Oriented and Prosperity; for business continuity, operational Islamic bank needs funds to hire and conduct its business, for that the bank needs funds drawn from the operations revenue. While the rest of the other businesses provided to customers in the form of profit-sharing for their welfare.

The operating system of Islamic bank in Figure 2 illustrates that Islamic bank in operate their business get started with capital from the founders, in addition get funds from a depositor funds, the profit-sharing will be given to the founders and customers over the invested funds to banks, from the profit-sharing of each set aside sharing into *zakat*. Funds are distributed to customers require, bank share their operations in two terms of distribution of these funds (1) the financing in *Ba'i bithaman Ajil*, *Murabahah*, and *Ijarah* (2) Equity Financing in *Musharakah* and *Mudharabah*. Profit-sharing for debtors and creditors in financing is done by contract containing an agreement margin of gains/losses on the business and equity financing in profit-sharing for each. In addition to distribution of funds by 2 mechanisms above, Islamic banks also have a mechanism for channeling other funds namely *Al Qard al Hasan* was the provision of funds in order to realize a social responsibility to debtors who deserve it, the Islamic debtor is obliged to repay only the loan principal only.

SISTEM OPERASIONAL BANK SYARIAH



Sumber : Muhammad, Sistem & Prosedural Operasional Bank Syariah, 2005; 4

Figure2. Islamic Banking Operational System

Islamic Syaria Management concepts in Al Quran and Al Hadith as following:

- Amar Ma'ruf Nahi Munkar's Principle: *"Hendaklah ada diantara kamu ummat yang menyeru kepada kebajikan, menyuruh berbuat yang ma'rif dan mencegah perbuatan keji"* (QS 3 : 104)
- The Obligations to uphold of Truth: Truth (*haq*) according to the size and the norms of Islam, among others implied Allah says in chapter (17) *Al-Isra* ayat 81: *"Katakanlah ya Muhammad, Telah datang kebenaran dan telah sirna yang batil. Sesungguhnya yang batil itu akan lenyap"*
- The Obligations to uphold of Justice; Islamic law requires us to uphold justice, anytime and anywhere. Allah says in chapter (4) *An-Nisa* ayat 58: *"Jika kamu menghukum di antara manusia, hendaknya kamu menghukum (mengadili) secara adil"*
- The Obligations of Mandated; Allah and Rasul commanded every Moslem to fulfill the mandate. Otherwise to fulfill the obligations mandated by Allah in chapter (4) *An Nisa* chapter 58: *"Sesungguhnya Allah memerintahkan kamu untuk menyampaikan amanat kepada yang berhak menerimanya"*.
- Regarding the mandate of fulfilling obligations in the field of *muamalah*, Allah says in chapter (2) *Al-Baqarah* ayat 283: *"Maka hendaklah (orang) yang dipercayai itu menunaikan amanatnya (hutangnya) kepada yang berhak (yang berpiutang)"*.
- Planning, *"Wahai orang-orang yang beriman bertaqwalah kepada Allah dan rencanakanlah masa depanmu. Dan bertaqwalah kepada Allah, sesungguhnya Allah Maha Tahu atas apa-apa yang kalian perbuat"* (QS 59:18)
- Organizing, *"Allah membuat syariat dari dien, yakni apa yang Kami wasiatkan kepada Nuh, Muhammad, Ibrahim, Musa dan Isa bahwa hendaklah kalian menegakkan dien dan janganlah berpecah-belah padanya. Memang berat bagi orang musyrik apabila kalian mengajaknya ke jalan menuju kebaikan. Allah memilih siapa-siapa yang"*

dikehendakiNya dan memberi petunjuk kepada siapa-siapa yang ingin kembali ke jalan Allah”(QS 42:13).

- Controlling, covers all activities of research, observation and measurement of the operation based on a predetermined plan, interpretation and comparison of results achieved with the required standards, perform corrective actions deviations, and comparisons between the results (output) reached with the input (input) that used

It is clear that the rights and obligations of a person in management expressly provided in Islamic law. The arrangements such as contained in the Islamic law, chapter *Al Buyu*, the Law of Agreement, or chapter *Imarah* and *Khilafah* which is indicated by *dalil* and *nash* in the Al Qur'an and Al-Hadith. All laws must be implemented and obeyed like other laws. Similarly, the principles of management contained in the Al Qur'an and Al Hadith, natural and fairly that are applied in our life. Islam gives flexibility to *ijtihad*, with *dalil nash* Al Qur'an and Al Hadith capabilities supported by modern science, a manager will be able to *ijtihad* to get the satisfactory results (*natijah*).

Previous studies concerning the financial performance of Islamic Banking trough CAMEL ratio that using Performance Banking Level Ratio that created of Central Bank as a benchmark on CAR, ROA, NPF, OEOI, FDR in CAMEL (Sumarti, 2007; Seri, 2007; and Mubarak, 2004) the conclusion that the ratio CAR, NPF and OEOI in good performance categories, however ROA and FDR in attention category. Others research about Islamic Banking performance that evaluate, challenge, trend and its prospective (Agustiano, 2010; Wijaya, 2010; Swandani, 2010; Rohendi, 2010; Kamal, 2008; Muhammad, 2006; Setiawan, 2006; and Rais, 2002) expressing that Islamic banking have a most potential and business and market in the future. With using Profit and Value Added to assess Islamic Banking performance (Nurhafita, 2010; Agustiano, 2010; Wahyudi, 2005) also gives the conclusion that profit will increase with better financial performance in the bank. The last Islamic Banking efficiency analysis by Suswandi (2007) where the management of Islamic banking is still inefficient, maybe the Islamic banking still needs promotion, employee training, expanding office, etc that need more expenditure.

3. The Methodology and Model

This research approach to determining the performance of Islamic Banking based on Bank Indonesia Act No.9/1/PBI/2007 which using CAMEL method with five financial ratios as a tools, namely CAR, ROA, NPF, OEOI, FDR. The ratios would compared with Depositor Funds as a reflect level of public trust for Islamic banking industry. If the ratios indicate a good performance, it sign that the bank can manage all of the aspect well and supposed to increase depositor funds in Islamic bank. The model calculates ratio CAR, ROA, NPF, OEOI, FDR from Islamic banking that registered in Bank Indonesia, which eventually became a multiple regression model. Using descriptive method to describe Islamic banking data, where the description and explanation of these data as a reference to see the characteristics that ended with a draw conclusions (Cooper, 2009) and determine that the good performance of Islamic banks which will increase the depositor funds. Inputs to the model are:

- Balance Sheet and Income Statement, both of them are financial statements used in this study, and not use other financial reporting
- Using monthly data over the 3 financial periods of 2007 to 2009
- The type of Islamic banking which this subject of this research are Islamic Commercial Bank (BUS) Islamic Business Unit (UUS) excluding Islamic Rural Bank (BPRS)
- There are 31 Islamic banking which is used as a sample, which consists of 6 Islamic commercial banks and 25 Islamic business unit.

The output of the model are the value of CAR, ROA, NPF, OEIO, FDR and Depositor Funds to be used as financial models to predict the future of Islamic banking business and with the results of the ratios calculation the expected level of public trust to Islamic banks has increased and eventually they entrust their money to be saved in Islamic banks as well if they need funds for business needs, consumption and others. The output is determined as:

$$CAR = \frac{\text{Equity}}{\text{ATMR}} \quad (1)$$

Equation (1) is Capital Adequacy Ratio (CAR), the ability of banks offset a decline in assets due to losses on bank assets using its own capital. The greater this ratio, it means the better bank's capital adequacy ratio.

$$ROA = \frac{\text{Net Income}}{\text{Total Asset}} \quad (2)$$

Equation (2) is Return on Assets (ROA), which measures the effectiveness of the company in utilizing all resources in order to measure the ability to generate profits. The higher this ratio, it means the more effective use of assets to obtain income and the better performance of the bank.

$$NPF = \frac{\text{Total NPL}}{\text{Total Financing}} \quad (3)$$

Equation (3) is Non-Performing Financing (NPF), which measures the level of bad debt that had to be reserved. The smaller this ratio, it means that the better performance of the bank

$$OEIO = \frac{\text{Operating Expense}}{\text{Operating Income}} \quad (4)$$

Equation (4) is Operating Expense to Operating Income (OEIO), which measures the level of efficiency and distribution of the bank in conducting its operations. The smaller this ratio, it means that the better performance of the bank

$$FDR = \frac{\text{Total Financing}}{\text{Total Deposits}} \quad (5)$$

Equation (5) is Financing to Deposit Ratio (FDR), ability to repay the bank withdrawals by customers with relying on loans as a source of liquidity

The results of these equations will form a multiple regression model as follows:

$$Y_{syaria} = \alpha + CAR_1 X_1 + ROA_2 X_2 + NPF_3 X_3 + OEIO_4 X_4 + FDR_5 X_5 + e_6$$

Then, to find out whether the good performance of Islamic banking using the CAMEL method with CAR, ROA, NPF, OEIO, FDR ratios will actually increase the depositor Funds. This study will test the hypotheses with the Student-test (partial) and Fisher-test (simultaneous) assisted program SPSS 13.0 for Windows.

4. The findings/Discussion

In Table 1 shows a illustration of the performance of the Islamic Bank using the CAMEL method which consists of 5 financial ratios and a ratio comparator (Depositor Funds) which data is analyzed as much as 36 months of January 2007 to December 2009 that showed for 36 months period, where the lowest Islamic Bank CAR of 10.4% and the highest of 13.9% with an average Islamic Bank CAR of 11.5% which is above the requirement of Bank Indonesia rate of 8%, the bank's ability to optimize assets in a business of taking risks to earn profits called ROA had minimum of 1.4% and maximum of 2.6%, also average of 1.9%, it means the above requirement of Bank Indonesia rate of 1%. NPF Islamic banking lowest of 4% and still exists that exceeds the requirement of BI

maximum of 5% where the highest NPF Islamic banking of 5.72%. The level of efficiency and distribution of the bank in conducting its operations called OEOI lowest of 67.6% and the highest of 84.4%. Bank is called efficient if they have a small percentage and till now, there is still Islamic banks which have efficiency above 75%. The ability to repay the bank withdrawals by customers with relying on loans as a source of lowest liquidity of 89.7% and the most worrying for Islamic banks that use all depositor funds added using internal capital to get profit-sharing or wide spread margin. The term of this ratio according to Bank Indonesia are below 80% to depositor funds compiled by the bank. It is expected that with the best value of any financial ratio above could increase public confidence due to the management of Islamic banks are able to manage the bank well in order to give a sense of security to the public to save their money in Islamic banks.

Table 1. Discriptives of CAMEL for Islamic Banking

CAMEL	N	Min.	Max.	Mean	Std. Dev
CAR	36	0,104	0,139	0,115	0,010
ROA	36	0,014	0,026	0,019	0,003
NPF	36	0,040	0,572	0,045	0,005
OEOI	36	0,676	0,844	0,763	0,039
FDR	36	0,897	1,122	1,011	0,400
Depositor Funds	36	21176	52271	33173	8581,1

Test results of multiple regression and t-test as shown in Table 2

1. Financial performance BPRS using CAMEL using CAR and OEOI partially significant influence to increase depositor funds with probability value (Sig. column) is smaller than 5% as alpha, while the variable ROA, NPF and FDR are insignificant. Obtained simultaneously with the F count = 3.981 with Sig. 0.007 smaller than $\alpha = 0,05$. This means that the independent variable CAR, ROA, NPF, OEOI and FDR simultaneously significant influence to increase depositor funds at Islamic Banking.

2. Regression model that created:

$$Y_{\text{syaria}} = -211261 + 0,366.x_1 + 0,502.x_2 + 0,456.x_3 + 0,701.x_4 + 0,143.x_5 + e_6$$

Table 2. Counting of Multiple Regression Result

Variables	Koef Regression	t-count	Sig.
CAR	0,366	1,866	0,025*
ROA	0,502	1,812	0,072
NPF	0,456	2,385	0,080
OEOI	0,701	2,317	0,024*
FDR	0,143	0,837	0,409

* significant at 5% probability

Constant : -211261
 Adjusted R² : 0,299
 F Count : 3,981
 F Sig. : 0,007
 Alpha (α) : 0,05

5. Conclusions

- Islamic syaria had concept by Al Qur'an and Al Hadits
- The present study found that CAR and OEOI are significant effects to increase depositor funds in Islamic banking however ROA, NPF and FDR are insignificant.

- Simultaneously obtained by the independent variable CAR, ROA, NPF, OEOI, and FDR are significant to depositor funds.

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