

CHAPTER I

A. Introduction

The philosophical foundation of Islamic financial system stands beyond the interaction of factors of production and economic behavior. The conventional financial system mainly focuses on economic and financial aspects of the transaction, the Islamic system focuses on the dimensions of ethic, moral, social, and religious, which seeks to improve equality and justice for the good of society as a whole. This system can be fully appreciated only in the context of Islamic teachings about work ethic, wealth distribution, social and economic justice, and the role of the state. The Islamic financial system is on the absolute prohibition of the payment or receipt of any predetermined, guaranteed rate of return. This has close meaning to the concept of interest and precludes the use of debt-based instruments.

After basic understanding of Islamic financial system, the understanding of Islamic banks in general is a bank that the operation adapted the principles of Islamic law. Today, many terms given refer to entities other than the term of Islamic Bank itself, the Bank without interest (Interest-Free Bank), Bank Without Riba (Lariba Bank) and Bank Shariah (Shari'a Bank). Technically, in Indonesia jurisdiction mentions Islamic Bank to use the official term "Islamic Banking", or in full-called "Bank Syariah".

The characteristic of Islamic banking operation is based on partnership and mutual benefit principle provides an alternative banking system with mutual benefits both for the public and the bank. This system

will give priorities to the aspects related to fairness in transaction and ethical investment by underlining the values of togetherness and partnership in production, and by avoiding any speculative activity in financial transaction. By providing various products and banking services supported by variative financial scheme, Islamic banking will become credible alternative banking that can be benefitted by all of Indonesian people without exception.

In its development, Islamic banking has been given serious attention in encouraging the development of Islamic banking by BI (Bank Indonesia) as the regulator. This spirit is based on the belief that Islamic banking will bring the 'beneficiaries' for the improvement of the economy and public welfare distribution. First, Islamic banks closer to the real sector, particularly in finance, always use the underlying transactions in the real sector so that its impact is more evident in driving economic growth. Secondly, there is no speculative products (*gharar*) to have a strong endurance and tested the toughness of the direct hit of the global financial crisis. At the macro level, Islamic banking can provide carrying capacity of the stability of the financial system and the national economy. Third, the results of the system (profit-loss sharing) which becomes the spirit of Islamic banking will bring justice and benefit for all parties, both the owner of the funds as depositors, borrowers and businesses as the bank as fund manager.

Islamic banks proved to be a financial institution that can survive amid severe economic crisis. In the second half of 2008, crisis hit the world back. The financial crisis that originated from the United States eventually spread to other countries and expand into the global economic crisis. International Monetary Fund (IMF) expects a slowdown in world economic growth of 3,9% in 2008 to 2,2% in 2009. The slowdown is of course in turn will affect the performance of national exports, will eventually have an impact on national

economic growth. Islamic banking financing were still directed to domestic economic activity, so do not have a high level of integration with the global financial system is the reason one of the reasons why Islamic banks can survive.

Table 1
The growth of Financing Islamic Bank in Indonesia

Year	Financing
2012	147,505
2013	184,122
2014	199,330
2015	201,526

(Sources: Bank of Indonesia)

Based on table 1, in 2012, the total financing is IDR 147,505 billion. There is increasing financing by IDR 44,85 billion respectively. For the next year total financing is IDR 184,122 billion, in the other hand, the total financing in 2014 is IDR 199,330 billion. There is increasing of financing by IDR 36,617 billion. While, the increasing of financing is IDR 15,009 billion. The total financing in 2015 is IDR 201,526 billion. The increasing of total financing in 2015 is IDR 2,196 billion. Thus, the financing of Islamic banks in Indonesia have increased yearly. It gives impact on small bussiness that they can develop their bussines and also influence to increasing economic growth.

Financing fund is provided by one party to another to support the planned investment, either by themselves or institution. In other words, financing is funding issued to support the planned investment. The financial system is very important in the economic activities. As part of the economic system, the financial system serves to allocate funds from the surplus to the deficit experience. If the financial system is unstable and does not function efficiently, the allocation of funds will not run properly so it can hamper economic growth.

In June 2015, central bank data in Indonesia mentions a market share of Islamic banking in Indonesia is only 4,61%, or still below 5%. With the ongoing economic slowdown, the Islamic financial sector is also not optimal in supporting economic growth. Growth in the two main sectors of the Islamic financial industry is an increased capital market from minus 1,57 percent to 3,09%. On the other hand, Islamic banking slowed from 13% to just 9%. In line with the economic slowdown, growth in assets, depositor funds, Islamic banking and financing in the first half 2015 is also not optimal due to growth of only 9% of assets, depositor funds of 7,29%, and financing of 6,66%. Everything slowed when compared to the growth of assets, deposits and financing in the second half of 2014 respectively by 13%, 11,41% and 8,76%. Based on these indicators, it appears that there are still many challenges for Islamic finance Indonesia.

Types of Financing in Islamic banks are: acceptable financing, investment financing, liquidity financing, consumer financing, working capital financing, inventory financing and accounts receivable financing. Sources of financing are *giro wadi'ah*, deposits *mudarabah*, *musharaka* financing, *murabaha* receivables, receivables greeting, *istishna* receivables, *etc.* The most popular financing in the society is *Murabaha* Financing.

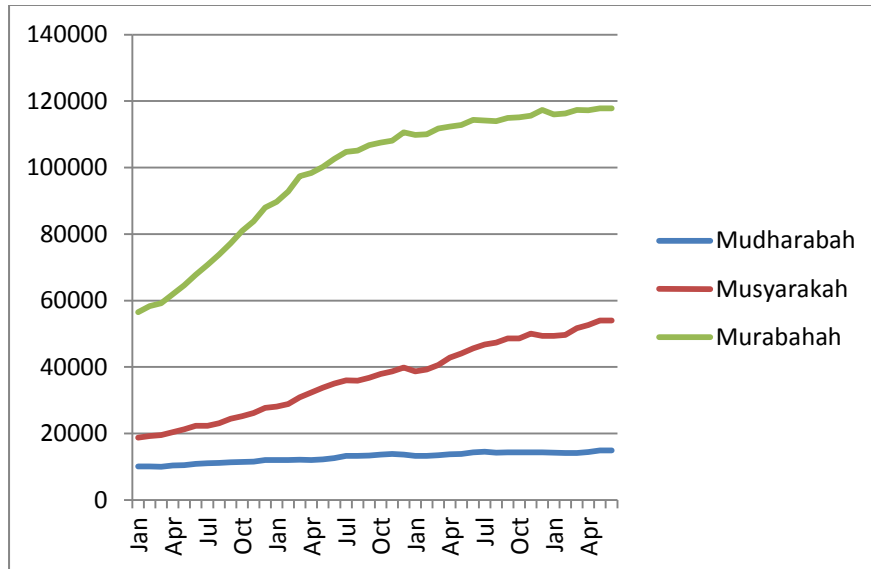


Figure 1.1
Mudharabah, Musyarakah and Murabahah on Islamic banks in Indonesia

Murabahah financing is the most desirable because *murabahah* dominates the revenue contribution of the Islamic bank products. It happened because of the amount of interest in Islamic banking customer on products *murabahah* financing scheme. The fact is, products with *amurabah* sale and purchase agreement is in great demand by customers of Islamic banking, as it is considered to have the smallest risk. In addition, *murabahah* financing agreement is clear, as well as the relative goods, and its safety.

Bai'al-Murabah is the term most often used in Islamic banks or Islamic financial institutions as a contract which is used in the products of financing the purchase transaction with the customer. Most of the Islamic banks and Islamic financial institutions using the *Bai'al-Murabah* financing emerges in banking products customers are buying and in the selling scheme. In real practice in Islamic banking and finance industry in the country, *akad Murabahah* plays an important role in improving the business performance of Islamic banks.

The most fundamental thing is that the Islamic banking industry has a great opportunity because it proved resistant to the crisis. Even after the failure of the capitalist economic system, *sharia* system is seen as an alternative and solution to solve the problems of the world economy. The proliferation of Islamic financial institutions is a proof that the system is resilient to the crisis. It has also been proven as Economic Crisis of 1988, when the conventional banks experienced a negative spread, but the *Syariah* banking appear as healthy and resistant to the crisis and demonstrate its existence until now. Bank of Indonesia also gives serious consideration to encourage the development of Islamic banking due to the belief that it will bring the 'beneficiaries' for the improvement of the economy and public welfare distribution. First, Islamic banks provide a more tangible impact in encouraging economic growth because it is closer to the real sector, as has been stated above. Secondly, there is no speculative products (*gharar*) that need strong resistance and had been tested by the toughness of the global financial crisis. Third, the system for the results (profit-loss sharing) which becomes the spirit of Islamic banking that will bring benefits more equitable for all parties.

Hence, the financing of Islamic banks is very interesting because of the resilience of Islamic banks in Indonesia in the period 2008-2009 was not affected by the global crisis at all. In the process, there have been 12 Islamic banks with 2,121 offices spread throughout Indonesia. Within a fairly short period, Islamic banking in Indonesia showed a positive development and the community was not overly concerned about the existence of Islamic banking itself. It does not arrange the possibility of banking in Indonesia that will be mastered by the Islamic banking which is more just by interest free and to be the first choice in terms of financing, loan or other by all people of Indonesia in supporting the realization of significant economic growth.

Many factors affect the banks in distributing funding. Two of the factors are derived from the internal factors and the external ones originating from the bank. To view the internal conditions of banking, the bank usually refers to the bank's financial statements indicated by various financial ratios. Internal conditions of banking can be seen from several financial ratios. In this study, the independent variables using a factor derived from the internal bank financing on the entire Islamic banking in Indonesia.

Internal factors also affect the number of Islamic finance in the entire Islamic banking in Indonesia in which it's distributed. The financial ratios are often used to assess the internal conditions of banking, among others: the ratio of bank capital represented by the ratio of *Capital Adequacy Ratio* (CAR), the ratio of bank profitability represented by *Return on Assets* (ROA) and *Return on Equity* (ROE), liquidity banks represented by the *Depositor Funds* (DF), the ratio of financing problems represented by *Non-Performing Finance* (NPF), and the division result represented by *Profitshare* (PF).

Perry Warjiyo (2004) mentions that the bidding behavior of financing, in addition affected by available funds sourced from DF (Depositor Funds), is also influenced by the perception of banks on the prospects of the debtor's business and the banking system itself such as capital or CAR (Capital Adequacy Ratio), the amount of non-performing loans or NPL (Non Performing loans) and LDR (Loan to Deposit Ratio). Other aspects that influence the bank's decision to extend credit to the debtor is a profitability or rate of profit which is reflected in Return On Assets (ROA). (Suseno and Piter, 2003)

The global economic recovery is already beginning to be felt at the end of 2012, although in some parts of the world it's still a new entrant to the financial and economic crisis. However, the general direction of development of the economy in 2013 is predicted to

be better than in 2012. Moreover, for the performance of the Indonesian economy with relatively high levels of domestic consumption and rising middle class and supported by macroeconomic conditions relatively well preserved, are some of the factors that cause the national economy was less affected by the global economic crisis. Similarly, the national Islamic banking, relatively not so significantly exhibited and affected by the global economic crisis in early 2012 in line with the focus of Indonesian banks that are oriented to the domestic market is still large, and the potential for the share of Islamic banking is still high in Indonesia, with a market share up by the end of 2012 was close to 5%..

Throughout the year 2012, the performance of national Islamic banking industry is still dominated by the structure of its assets to around ±98% by Islamic Banks and Unit Syariah Business relatively well, evidenced by: (i) the intermediary function are at an optimum level with FDR average of 97.16%; (ii) capital adequacy ratio (CAR) is still well above the minimum 8% with an average CAR of ±15.17%; and (iii) the level of financing problems (Non Performing Financing/NPF) is still below 5% with an average of 2.72%, and even to the position in December 2012 reached 2.22%.

This study is performed to illustrate the influence of these variables on the growth rise and fall of the amount of the finance portfolio of Islamic banks in Indonesia during the research period January 2012-June 2015. The researcher is interested in researching Islamic Bank due to it is now in Indonesia predicted to grow at a sufficiently high growth rate. Researcher is also interested in conducting this study because many gaps on researches resulted from the outcome of previous studies, so it needs to be re-examined through the factors that affect the financing of Islamic banks. This research is also done because of a difference between the data with the theory, such as the rise and fall of the CAR is not

necessarily followed by an increase in financing, as well as the ROA. Therefore, researcher wanted to determine the effects of these variables.

Based on the background of the problem that have been raised, researcher wanted to conduct research and compile them in a thesis entitled **"Analysis of Factors Affecting Total Financing on Islamic Bank in Indonesia (period January 2012-June 2015)"**

B. Problem Statement

In this study, the problems to be examined is limited only about financing in Islamic Bank affected by the CAR, ROA, ROE, Depositor funds, Profit Sharing and NPF.

C. Problem Limitation

Based on the explanation above, the problem formulated in this research is to see whether the financing done by *Syariah* Bank has touched the whole society or has it just shown that Islamic banking is still under the shadow of Conventional Banking. In 2016, Indonesia has entered the AEC (Asean Economic Community) so that competition does not only take place in the domestic competition but became broader as it covers other countries. Here, financing product is capable of and can assist economic factor in running the economy as well as local products which are capable and can compete with global markets.

D. Research Problem

Based on the background and the formulation of the problems that have been raised, the purpose of this study is:

1. How is the influences of CAR to financing in islamic Banks?
2. How is the influences of ROA to financing in islamic Banks?
3. How is the influences of ROE to financing in islamic Banks?
4. How is the influences of NPF to financing in islamic Banks?
5. How is the influences of Profit Share (PF) to financing in islamic Banks?
6. How is the influences of Depositor funds (DF) to financing in islamic Banks?

E. Research Objective

1. To analyze the long-run and short-run of finance, CAR, ROA, ROE, NPF, profit share and depositor funds in islamic banking.
2. To analyze the effect of shock on finance, CAR, ROA, ROE, NPF, profit share and depositor funds in islamic banking.

F. Research Contribution

This study is expected to provide several benefits, including for:

1. Empirical

Research on the financing has been done, but specifically for financing research in Islamic Banking has not yet been done. Hopefully, the results of this study can add insight and knowledge to readers on this matter.

2. Methodological

This study uses VECM, because this method is appropriate for observing short and long term analysis. This research is expected to be used as reference material for the next research.

3. Policy

The results of this study are expected to be used for information in a policy of financing for economic players in Indonesia, especially the financing committed by Islamic Banking.