The role of Islamic banking system as the milestone towards Indonesia creative economy development

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THE ROLE OF ISLAMIC BANKING SYSTEM
AS THE MILESTONE TOWARDS
INDONESIA CREATIVE ECONOMY DEVELOPMENT

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ABSTRACT

A model of micro-finance system that allows developing creative industries has been introduced through the role of Shari’ a banking in Indonesia. Because of this phenomenon, many researchers have tried to compare the financial performances of Conventional Bank and Shari’ a Bank. In this study, two state-owned banks in Indonesia (PT. Bank Mandiri and PT. Bank Syariah Mandiri) serve as an object of research based on secondary data for the period of 2007-2011. During this period, Indonesia’s economic growth accelerated to a ten-year high of 6.3\% in 2007. Based on the Capital, Asset Quality, Management, Earnings, Liquidity (CAMEL) method, there is a difference in the capital aspect represented by Capital Adequacy Ratio (CAR), the profitability aspect represented by Return on Asset (ROA) and the liquidity aspect represented by Loan to Deposit Ratio (LDR) of PT. Bank Mandiri and PT. Bank Syariah Mandiri. Meanwhile, there is no difference in the asset quality aspect of both banks represented by Earnings Asset Quality (EAQ). Further result also found that PT. Bank Syariah Mandiri has a better financial performance compared to PT. Bank Mandiri based on CAR and LDR aspects, even though for the profitability aspect (ROA), PT. Bank Mandiri is better than PT Bank Syariah Mandiri. Based on the result, SME's of creative industry in Indonesia can choose the most suitable bank which can provide their needs of fund better. By
choosing the right bank, they can minimizing the fund risks, optimizing the fund for their business development and contribute on Indonesia economic development.

**Keywords**: Creative Economy, Islamic Banking, Conventional Banking, CAMEL, Financial Performance

**INTRODUCTION**

So far, people only know that bank is an institution where people can save money, withdraw money, transfer and others. However in the last few years, an Islamic principled bank emerged, refer to as Shari’a bank. So, now people know two types of bank, namely: Conventional Bank which is earlier known by public and Shari’a Bank which started to attract people’s attention. As the largest Muslim community in the world, Indonesia is optimist on implementing Islamic economy as one of the system (Rahajeng, 2013). Islam also offers a model of micro-finance system that enables actors and entrepreneurs in the creative industries to meet their financial needs, and its components have increased creative economic development in Indonesia.

Attention to the Indonesia’s Creative Economy development program in 2025 is a form of confidence and appreciation for Indonesia to realize the vision of becoming the Developed Countries. This includes the form of thoughts, ideals, imagination and dreams to become a community with a high quality of life, prosperity and creative. Creative economy that includes the creative industries is believed to contribute significantly to the economy of the nation. Various sub-sectors in the creative industries have the potential to be developed, because the Indonesian nation has the human resources and rich cultural heritage. Therefore, all efforts directed towards the development of creative industries to establish an independent industry at the same time the welfare of society.
Creative industry is one sector that is growing uniquely which continue to provide lots of jobs and value added to improve the economy of Indonesia. Creative, skill and talented of human resources are contributing to growth this sector. Creative industry is an industry that is not limited to a particular type of product, which can contribute for developing economic significantly. Indonesia's creative industry is one of the main pillars in developing the creative economy sector that can provide a positive impact for national life. Based on Performance Accountability Report of the Ministry of Tourism and Creative Economy in 2013, the creative economy create value added Rp. 641.82 billion or 7.05% of GDP through 14 sub-sectors of creative industries, while labor absorption reached 11.87 million workers, or 10.72% of the national trade. Meanwhile based on reported of Central of Bureau of Statistics, creative industries is capable to create income through net trade, reaching 5.72% of total national trade, or Rp 118.97 trillion in 2013.

The success of the creative industries in supporting the national economy derived from the growing trade in goods and services. The support of the banking industry (both conventional and Sharia 'bank) as the intermediary is able to develop a successful business for the Creative Industries sector. The higher of the economic growth and sustainability expected to be felt by the creative industries as it has been designed in the master plan for the Acceleration and Expansion of Indonesian Economic Development (in Indonesia usually called as MP3EI)

Some of the fundamental things that distinguish both kinds of Bank are shown in table 1. Table 1 shows 5 (five) points that distinguish Shari’ a Bank and conventional Bank. The presence of a bank based on Shari’ a principles in Indonesia is relatively new; it has just started in the early 1990s, although Indonesia has the world largest Muslim communities. It makes the development of Shari’ a banking an interesting phenomenon, since it is a new in-
Industry that its development is still extended. Moreover, Shari’ a bank is full of Islamic values principles, so the development is very interesting to follow (Kasmir, 2012).

**Table 1:** Comparison of Shari’ a Bank and Conventional Bank

<table>
<thead>
<tr>
<th><strong>SHARI’A BANK</strong></th>
<th><strong>CONVENTIONAL BANK</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td>Legal investments according to Islamic principles</td>
<td>Legal (halal) and illegal (haram) investment according Islamic principle</td>
</tr>
<tr>
<td>Based on the principle of sharing, sale or rent</td>
<td>Use interest;</td>
</tr>
<tr>
<td>Profits and <em>falah</em> (reward from God) oriented</td>
<td>Profit oriented</td>
</tr>
<tr>
<td>Relationships with customers in the form of a partnership</td>
<td>Relationships with customers in the form of debtor-creditor</td>
</tr>
<tr>
<td>The collection and distribution of funds should be in accordance with the legal regulation of the Shari’ a Supervisory Board</td>
<td>There is no board like that of Shari’a bank.</td>
</tr>
</tbody>
</table>

Shari’ a bank in Indonesia is the form of people’s demand of banking system based on Islamic principles that provide healthy financial services (Syafi’i, 2001). In the early 1980s, discussions over Shari’ a bank as an Islamic base of economic had begun. Several trials on a relatively limited scale have been done. The Government has incorporated the possibility of realization of a banking system that is in accordance with Shari’ a principles in the new legislation. Undang-undang No. 7 Tahun 1992 concerning about banking implicitly has opened
the opportunity for banking business with sharing principle which is described in detail in Government Regulation No. 72 of 1992 about bank with sharing principle. After the issuance of the regulations, Shari’a banking system has shown very rapid development since 1998, which is about 74% asset growth per year (Halim, 2012).

As a regulator, Bank Indonesia has put serious and thorough attention in pushing the development of Shari’a banking. This encouragement is based on the belief that shari’a banking will bring 'beneficiaries' to improve the economy and the distribution of society welfare. Up to February 2012, Shari’a banking industry has had 11 Public Bank Shari’a (PBS), 24 Business Unit Shari’a (BUS), 155 Rural Bank Shari’a (RBS), with the total office networks that reaches 2380 spread almost all over Indonesia. This is shown in Table 2.

Table 2: Institutional development and performance of Shari’a banking Indonesia

<table>
<thead>
<tr>
<th>Indicators</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
<th>2012*</th>
</tr>
</thead>
<tbody>
<tr>
<td>PBS</td>
<td>3</td>
<td>3</td>
<td>5</td>
<td>6</td>
<td>11</td>
<td>11</td>
<td>11</td>
</tr>
<tr>
<td>BUS</td>
<td>20</td>
<td>26</td>
<td>27</td>
<td>25</td>
<td>23</td>
<td>24</td>
<td>24</td>
</tr>
<tr>
<td>RBS</td>
<td>105</td>
<td>114</td>
<td>131</td>
<td>138</td>
<td>150</td>
<td>155</td>
<td>155</td>
</tr>
<tr>
<td>Office work</td>
<td>693</td>
<td>802</td>
<td>1.069</td>
<td>1.258</td>
<td>1.763</td>
<td>2.101</td>
<td>2.380</td>
</tr>
<tr>
<td>Assets (bilions)</td>
<td>27.618</td>
<td>37.754</td>
<td>51.249</td>
<td>68.212</td>
<td>100.258</td>
<td>148.987</td>
<td>149.321</td>
</tr>
<tr>
<td>PYD (bilions)</td>
<td>21.060</td>
<td>28.837</td>
<td>39.455</td>
<td>48.473</td>
<td>70.190</td>
<td>105.331</td>
<td>106.532</td>
</tr>
</tbody>
</table>

*Position February 2012
The Performance of Indonesian Shari’a Bank

Assessment of the health of Shari’a bank is conducted based on Indonesian Bank Regulation (IBR) No. 9/1/PBI/2007 concerning the Rating System for Commercial Banks based on Shari’a principles effectively started from January 24, 2007. From the explanation of the Deputy Governor of Bank Indonesia, Siti Chalimah Fadjrijah, the implementation is conducted by estimating the Shari’a banking products and services for further which will be more varied and complex, so it will be more exposed to risks. The increasing risk exposure will change the risk profile of the Shari’a banks, which in turn will affect the health of the bank. In measuring the bank health, Shari’a banks have included the risks associated in the bank’s activity (inherent risk) which is part of the risk management assessment process.

Indonesia’s largest Shari’a Bank currently can only book assets of approximately US $ 5.4 billion, so that no Shari’a bank has entered yet the 25 Shari’a banks with largest assets. While three Shari’a banks are on list. It shows that the economic scale of Indonesian Shari’a bank is still under the Malaysian Shari’a bank which will become a major competitor. The unreachable economic scale makes Shari’a bank operational in Indonesia less efficient, moreover most of them are still in the expansion phase that requires a significant infrastructure investment.

Challenges and Problems Faced by The Shari’a Bank in Indonesia

In general, Halim (2012) mentioned that Shari’a banks in Indonesia are facing challenges and problems. The challenges that have to be solved in the short-term (immediate) are:

a. The gap fulfillment of human resources, both in quantity and quality.

b. The innovation development of competitive Shari’a banking products and services based on people’s needs.

c. The continuity of socialization and education program for the society
While challenges that have been resolved in the long-term are:

a. The need for legal framework that is able to solve comprehensively Shari’ a financial problems.

b. The need for national and global product codification and regulation standards to allign the differences in the 'fiqh muammalah'.

c. The need of the rate of return references for Shari’ a financial.

**Problems and Research Objectives**

The concept of Shari’ a banking is a relatively new and applicable in many countries in the world. It is quite logical to assess the financial performance of banks from various aspects. This research investigates financial performance of Shari’ a bank and compares it with that of conventional bank that has been operating in Indonesia.

Developing creative industries has been introduced through the role of Shari’ a banking in Indonesia. Because of this phenomenon, many researchers have tried to compare the financial performances of Conventional Bank and Shari’ a Bank. In this study, two state-owned banks in Indonesia (PT. Bank Mandiri and PT. Bank Syariah Mandiri) serve as an object of research based on secondary data for the period of 2007-2011. To analyze the performance of Shari’ a Banks that operates in Indonesia and to compare Shari’ a banks and conventional banks using the result from the CAMEL assessment.

**LITERATURE REVIEW**

Rashid (2009) conducted a study in Pakistan during 1999-2006 to evaluate the performance of Shari’ a banks using financial ratios. The authors use the profitability, liquidity, risk ratio, solvency and community development for the analysis instrument. Mean, standard deviation, t-test and f-test were used to measure the significance of financial ratios on bank performance. The author used three Shari’ a banks which are Meezan Bank, Al-Baraka Islamic
Bank and Shari’a banking division of Bank Al-Falah and other eight conventional banks. According to the author, conventional bank is more profitable than Shari’a bank.

Another study, Khan, Farouq and Fawad (2010) trying to figure out which bank that has a more feasible and profitable system. A sample of four banks, two of Shari’a and two of conventional bank, have been chosen and applied on financial ratios. The findings suggest that Shari’a banks are as profitable as conventional bank although Shari’a bank is a new player in the Pakistan banking industry. Liquidity and Solvency ratio suggests that Shari’a banks are better than conventional banks because Shari’a banks maintain a lower debt ratio and a higher equity in the capital structure to reduce the risk of failure. Shari’a banks are more efficient in cost but are less efficient in profit and revenue compared to conventional banks.

A study that aimed to investigate Shari’a banking system in Pakistan has been conducted by Kouser, Asmir, Mehvish and Azeem (2011). The financial performance of Shari’a Bank and Conventional Bank are assessed using CAMEL models. The research used every category of Pakistan bank with a large number of branches. The number of top ten bank same numbers from both categories) which are included in the study of financial data with the five-year (2006-10) statistical methods consisting of Leverets, t-test, and Mann-Whitney test. The conclusion implies that the Shari’a bank in Pakistan does not have any stronger financial health compared to conventional banking. There is a strong need for awareness, improve, and expansion in Pakistani Shari’a banking system. The Government should formulate economic policies that support Shari’a banking in Pakistan to the best level.

According to Kouser and Saba’s (2012) study, they found that Shari’a banks have sufficient capital and good assets quality in compare with Islamic branch of conventional Bank and conventional banks. In addition, Shari’a banks generally have a good manage-
ment competence in comparison with Conventional Bank. Revenues of conventional Banks that have branches of Shari’a are larger compared to conventional banks and Shari’ a banks.

**CAMEL Model**

CAMEL framework was originally proposed to determine the schedule of bank examination. A popular framework used by regulators is a CAMEL which uses several financial ratios to help evaluate the performance of a bank (Yue, 1992). Five factors of CAMEL are Capital Adequacy (capital), assets quality (assets), health management (management), revenue and profitability (earning), and liquidity, when one of the five factors proved inadequate, this indicates possible increase in bank failures. The selection of the five factors of CAMEL are based on the idea that each is a key element in the financial statements of a bank.

Tarawneh (2006) analyzed the comparative financial performance of Oman Public Bank using CAMEL model and he worked on the scaled relationship between management efficiency bank asset, operational and financial performance. He used the period of 1999-2003 for the data. In a quantitative study, he checked the variety and the different performances among other commercial banks that differ from Oman. He classify and rank based on their financial performances that function as guidelines for future development. The main financial indicators used and developed were from the financial statement of commercial banks and used it to evaluate their internal performances such as return on assets, asset utilization, operation efficiency, the size of assets and interest income in assessing the bank performance. Those data were taken from the annual report sample period. Variance analysis (ANOVA) was used to test the hypothesis and to measure the differences and similarities between the bank samples in accordance with different characteristics. Pearson Correlation Coefficient was also used to investigate the correlation between 5% level of confidence in accordance with SPSS package.
Hypotheses

Some previous researchers conducted research on banks that operated in their country. In some of the above literature above, it is stated that Conventional Banks are likely to be better than Shari’a Banks in the term of bank health. So, the researcher of this study is motivated to do further research on banks operating in Indonesia.

This study analyzes the financial performances between conventional banks and Shari’a banks. The hypotheses used are:

- **H1**: there is a significant difference between the financial performances of Shari’a banks and conventional banks in terms of CAR. The CAR of Shari’a banks are better compared to that of conventional banks.

- **H2**: There is a significant difference between the financial performances of Shari’a banks and conventional Banks in terms of EAQ. The EAQ of Shari’a banks are better compared to that of conventional banks.

- **H3**: there is a significant difference between the financial performances of Shari’a banks and conventional banks in terms of ROA. The ROA of Shari’a banks are better compared to that of conventional banks.

- **H4**: there is a significant difference between the financial performances of Shari’a banks and conventional banks in terms of LDR. The LDR of Shari’a banks are better compared to that of conventional banks.
The researcher use the Independent Samples to Test or the average 2 different test to examine both averages on the two independent sets of data.

**RESEARCH METHOD**

**Variables**

A measure to assess the health of the bank have been set by Bank Indonesia in the Bank Indonesia Regulation number 6/10/PBI/2004 about the level of health assessment system in public Bank. To determine the condition of a bank, CAMELS analysis is usually used. However, in this study, the researcher analyzes only the aspect of capital assets, asset quality, profitability and liquidity.

CAR (Capital Adequacy Ratio) is used to assess the capital adequacy of the bank, KAP (Assets Quality) is used to assess the quality of the assets used, ROA (Return on Assets) is used to assess the profitability, while LDR (Loan to Deposit Ratio) is for assessing liquidity.

**Unit analysis and period of the study**

The followings are banks that will be analyzed in this study; there are PT.Bank Syariah Mandiri (as Shari’a Bank) and PT.Bank Mandiri (as Conventional Bank). The secondary data in this study is taken from the financial statements of each Bank for the period of 2007 - 2011.

**RESULTS AND DISCUSSION**

**Descriptive Analysis**

The value of CAR for PT.Bank Mandiri in a whole, lot better than PT.Bank Syariah Mandiri (see Figure 1). The highest CAR of Bank Mandiri was found in 2007 with a value of 21.1. Meanwhile, the highest CAR of Bank Syariah Mandiri was found in 2011 with the val-
ue of 14.57. Overall, both the CAR of Bank Mandiri and Bank Syariah Mandiri had been fluctuated during 2007-2011.

In Figure 2, the EAQ value of Bank Mandiri is better compared to PT.Bank Syariah Mandiri. The lowest EAQ of PT.Bank Mandiri was found in 2011 which is 2.18, while the lowest EAQ of PT.Bank Syariah Mandiri was found in 2011 which is 2.44. Overall, the EAQ of both banks were getting better during 2007-2011.

![Figure 1. CAR ratio growth of PT.Bank Mandiri and PT.Bank Mandiri Syariah Period 2007-2011.](image1)

![Figure 2. EAQ ratio growth of PT.Bank Mandiri and PT.Bank Mandiri Syariah Period 2007-2011.](image2)

The value of ROA for PT.Bank Mandiri in a whole, lot better than PT.Bank Syariah Mandiri (see Figure 3). The highest ROA of PT.Bank Mandiri was found in 2010-2011 with the value of 3.4, meanwhile the highest ROA of PT.Bank Syariah Mandiri was found in 2009 with the value of 2.23. Overall, The ROA of PT.Bank Mandiri was getting better during 2007-2011, but the ROA of PT.Bank Syariah Mandiri was fluctuating at that period.

Then, in Figure 4, the LDR of PT.Bank Mandiri is better than PT.Bank Syariah Mandiri. The lowest LDR value of PT.Bank Mandiri was found in 2007 with the value of 54.3, while the lowest LDR value of PT.Bank Syariah Mandiri was found in 2010 with the value of
Overall, LDR value of PT.Bank Mandiri was getting worse in that period, but the LDR value of PT.Bank Syariah Mandiri was fluctuating during 2007 - 2011.

![Figure 3](image1.jpg)  ![Figure 4](image2.jpg)

**Figure 3.** ROA of Bank Mandiri and Bank Mandiri Syariah Period 2007-2011.

**Figure 4.** LDR of Bank Mandiri and Bank Mandiri Syariah Period 2007-2011.

**Table 3: Independent Sample Test**

<table>
<thead>
<tr>
<th></th>
<th>Levene's Test for Equality of Variances</th>
<th>t-test for Equality of Means</th>
<th>95% Confidence Interval of Difference</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>F</td>
<td>Sig</td>
<td>t</td>
</tr>
<tr>
<td>CAR</td>
<td>Equal variances assumed</td>
<td>1.344</td>
<td>.280</td>
</tr>
<tr>
<td></td>
<td>Equal variances not assumed</td>
<td>3.313</td>
<td>6.269</td>
</tr>
<tr>
<td></td>
<td>.307</td>
<td>.595</td>
<td>-.342</td>
</tr>
<tr>
<td></td>
<td>Equal variances assumed</td>
<td>-.342</td>
<td>7.535</td>
</tr>
<tr>
<td>KAP</td>
<td>Equal variances not assumed</td>
<td>3.005</td>
<td>.121</td>
</tr>
<tr>
<td></td>
<td>Equal variances assumed</td>
<td>3.713</td>
<td>6.367</td>
</tr>
<tr>
<td>ROA</td>
<td>Equal variances assumed</td>
<td>1.859</td>
<td>.210</td>
</tr>
</tbody>
</table>
By conducting the test (see Table 3), it appears that there is a difference between the health performance of PT.Bank Syariah Mandiri and PT.Bank Mandiri on the components of CAR, ROA and LDR. However, there is no difference on EAQ between PT.Bank Mandiri and PT.Bank Syariah Mandiri. So, the hypothesis H1, H3, H4 are accepted and H2 is rejected.

By looking at the comparison charts and statistical group in the above results, PT.Bank Mandiri is very dominant on the component of CAR and ROA with an average of each component is 16.8600; 2.9200. Meanwhile, the average yield CAR and ROA of PT.Bank Syariah Mandiri is 12.5600; 1.9500. It can be concluded that the CAR component of PT.Bank Syariah Mandiri is better than PT.Bank Mandiri. Although CAR of PT.Bank Mandiri is safer than PT.Bank Mandiri Syariah, those with large capital will pose a highliability. On the other side, PT.Bank Syariah Mandiri has a lowerliability because the capital is not too large. The ROA of PT.Bank Mandiri is better than PT.Bank Syariah Mandiri.

In terms Of the capital expenditure, PT.Bank Mandiri has a greater capital compared to PT.Bank Syariah Mandiri. It is normal because PT.Bank Mandiri emerged earlier so that investors have greater trust toward PT.Bank Mandiri.

From profitability aspect, PT.Bank Mandiri has greaterprofit in comparison with PT.Bank Syariah Mandiri. This is due to the investment made by the bank is not more selective compared to PT.Bank Syariah Mandiri. Islamic banks invested only in investment, which is lawful according to Islamic rule, while Conventional Bank can be invested in lawful and unlawful investment. In the profit-sharing system, the customer and the bank should be equally gain profit, and in determining the result for the system there should be a contract between the bank and the customer. But, with the interest rate, Bank gain more profit compared to its customers. The two different systems were clearly affect the profits of each bank.
From the asset quality aspect, PT. Bank Mandiri has not been better yet in terms of EAQ compared with PT. Bank Syariah Mandiri. Each of average EAQ is 3.6440 and 3.9460, the difference is only 0.302. This indicates that asset quality of banks is good enough which is under 6%.

Then from the aspect of liquidity, the LDR of PT. Bank Syariah Mandiri is considered better than PT. Bank Mandiri. Although both banks are considered healthy by PT. Bank Indonesia, PT. Bank Syariah Mandiri, however, have the higher score because the largest LDR range between 85%-110%, and the average LDR of PT. Bank Syariah Mandiri is 86.7440. This is because of PT. Bank Mandiri's inability in distributing the third-party funds in the form of credit. The use of third-party funds in PT. Bank Mandiri then become questioned since 85% of the third-party funds are not distributed in the form of credit. The unexpected thing is that the third-party funds will be distributed for financing the fix assets and or non-current assets.

CONCLUSION

The results of the comparison and the average of each variables conclude that there is a difference in the financial performance between both banks, and the financial performance of Bank Syariah Mandiri is better compared to Bank Mandiri. Bank Syariah Mandiri is better in 2 (two) of the four (4) aspects analyzed, i.e. CAR and LDR, while Bank Mandiri is better in one (1) of the four (4) aspects analyzed i.e. ROA. The KAP ratio of both banks are considered similar because there is no significant difference. Based on the result, SME's of creative industry in Indonesia can choose the most suitable bank (between Conventional bank and Shari’ a bank) which can provide their needs of fund better. By choosing the right bank, they can minimizing the fund risks, optimizing the fund for their business development and contribute on Indonesia economic development.
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