

DETERMINANTS OF ISLAMIC BANK'S PROFITABILITY IN INDONESIA FOR 2009 – 2013

Okky Paulin and Sudarso Kaderi Wiryono
School of Business and Management
Institut Teknologi Bandung, Indonesia
okky.paulin@sbm-itb.ac.id

Abstract – *Performance efficiency of a bank being reliable to keeping trust and loyalty of clients. Banking performance can be seen from its profitability value, and as a result, financial ratios analysis in financial statement become an issue. This research focus on finding financial ratios that possible to be the profitability determinants of Islamic banks in Indonesia. Besides that, this research used quantitative analysis with CAMEL Method which consists of five aspects; there are capital, asset, management, earning, and liquidity. Independent variables that tested as the determinants of profitability are NPF, BOPO, NIM, FDR, PPAP Compliance, NPA, EA, and LIQD. In other side, dependent variable which represents bank's profitability is ROA Through purposive sampling technique, selected 6 banks as samples that met with the criteria of 5 years observation period (2009 – 2013) from 11 population of Islamic banks in Indonesia. The samples data analyzed using SPSS and had passed classical assumption test and multiple linear regression to determine the regression model feasibility. Classical assumption tests that used are normality test, multicollinearity test, heteroscedasticity test, and autocorrelation test. While multiple linear regression shown in F-test and T-test. The result indicated that NPF, BOPO, NIM, FDR, PPAP Compliance, NPA, EA, and LIQD give significant effect simultaneously to ROA as profitability ratio of Islamic banks in Indonesia. Then partially, NIM and PPAP Compliance give significant positive effect to ROA, whereas BOPO has negatively significant influence to ROA. And other ratios, which are NPF, FDR, NPA, EA, and LIQD, have no significant effect on profitability of Islamic banks in Indonesia. Based on R-square value, the effect of those independent variables to ROA is 91.7%, so 8.3% residue is influenced by other variables outside this research. Based on that result, Islamic banks in Indonesia should increase the assets quality (PPAP Compliance), profit sharing income (NIM), and operational efficiency (BOPO). Its good for banks to give more focus on those area as an effort to gain public enthusiasm by showing the quality of banks with highest priority is BOPO by looking at its value which is 0.915. Second priority is NIM ratio, then third priority is PPAP Compliance ratio. Related to BOPO, bank management should validates every cost or expenses taken out by bank, whether it is necessary to issued or not. Related to NIM bank always calculates the cost of funds carefully so it can determines the competitive based profit sharing percentages. And related to PPAP Compliance ratio, bank management should observes the financing agreements that proper to be financed.*

Keywords: *NPF (Non-Performing Financing), BOPO (Operational Efficiency), NIM (Net Interest Margin), FDR (Financing to Deposit Ratio), PPAP (Allowance for Earning Asset Possible Losses) Compliance, NPA (Non-Performing Asset), EA (Equity to Total Asset), LIQD (Liquid Asset to Total Deposit), ROA (Return On Asset), and profitability*

Introduction

The role of Islamic banking in particular is the new nationalism adhesive, that means to be a facilitator of business networking in democratic economy, empowerment of the people economic, push down the speculation in financial markets, encourage equitable distribution of income, and increase the efficiency of funds mobility (Muhammad, 2005). While at 2015, ASEAN Free Trade Area become a challenge to all industry, so for banking. The competitors from other countries are stronger than Indonesia with good quality of human resource, while Indonesian people are just

become their largest market. So therefore, Islamic banks should increase their performance in order to keep the loyalty of the clients through profitability aspect. Because high profitability means good management performance of a bank.

Bank's performance indicators and efficiency can be measured through CAMEL Method which consist of five aspects. Each aspect represented by financial ratio; where each ratio has a relationship with risk management and bank's profitability which is the common objective of operational bank. One of the ratios that more appropriate to describe profitability is Return On Asset (ROA) because it focusing the bank capability on getting earning in operational activity with utilizing bank's assets. That is why the influential factors of profitability on Islamic banks in Indonesia become really important these days.

There are so many researches about bank's profitability stated that financial ratio which had significantly effect to ROA is quite diverse. Accordingly, the determinants of bank profitability have been the subject of growing theoretical and empirical investigations. The central issue in this research is assessing the relationship between bank profit and internal (managerial related) factors believed to affect it.

Literature Review

1. Definition of Bank

Based on Law No. 10 of 1998 Amendment Act No. 7 of 1992 concerning Banking: Banks are business entities that raise funds from the public in the form of savings and channel them to the public in the form of credit and or other forms in order to improve the living standard of the people. Besides that, according to Law No. 7 of 1992 Article 3, the main functions of Indonesian banks are as collector and distributor of public funds.

2. Definition of Islamic Bank

Understanding the actual Islamic banks has been regulated in the Act. Article 2 of Regulation No. 6/24/PBI/2004 on Commercial Banks Conducting Business Based on Sharia Principles, provides a definition that Islamic commercial bank is a bank conducting business based on sharia principles and provides services in payment traffic. In the book entitled Management of Sharia Bank, outlines the economic relations based on Islamic law is determined by the relationship agreement which consists of five basic concepts of contract. These five concepts are: (1) a system of deposits, (2) the results, (3) profit margin, (4) leases, (5) service (fee).

3. Financial Report of Bank

The financial report is expected to provide information about financial performance and accountability of bank's management to all stakeholders. The financial report of Islamic banks include the balance sheet, income statement, cash flow statement, statement of changes in equity, notes of financial statements, statements of changes related to investment funds, sources and uses funds of ZIS statement, sources and uses funds of *qardhul hasan* statement (Dewi, 2010: 18). Then, something that must be analyzed from financial report is bank's financial ratios that are one of the most common tools of managerial decision making. A ratio is a comparison of one number to another. Financial ratios involve the comparison of various figures from the financial statements in order to gain information about a bank's performance. Ratio analysis is quantitative analysis of information contained in a bank's financial statements. Ratio analysis is used to evaluate various aspects of a company's operating and financial performance such as its efficiency, liquidity, profitability and solvency. The trend of these ratios over time is studied to check whether they are improving or deteriorating.

4. CAMEL Method

CAMEL Ratio is ratio that describes a relationship or comparison between one number to other number in financial report of a financial institution. This ratio analysis shows the condition or financial position at current year. CAMEL itself is abbreviation from capital (CAR), assets (PPAP Compliance), management (NPM), earning (NIM, BOPO, ROA, ROE) and liquidity (LDR). In Banking

Dictionary (Institut Bankir of Indonesia 1999), CAMEL is aspect which most influence to soundness level of financial institution. CAMEL becomes parameter of bank investigation object done by bank beadle.

5. Profitability

Profitability is a specific measure of the performance of a bank, where he is a management company with a goal of maximizing shareholder value, the optimization of the various levels of return, and minimizes the risks that exist (Adyani, 2011). Profitability is used as an indicator of management effectiveness of a company. Return on Assets (ROA) is a financial ratio which best to reflect bank's profitability, because it describes how banks obtain or optimize earnings by utilizing its assets. In addition, Bank Indonesia prioritize ROA rather than ROE to measure the performance of the bank because the priority value of a bank profitability measured by assets which funds most by public deposits (Dendawijaya, 2005).

6. Previous Research

This research is inseparable from previous studies that have related themes as the foundation framework or direction of this research.

Table 1. Previous Researches

No	Researcher (year)	Title	Variable	Research Result
1.	Angela Roman, Adina Elena Danuletiu (2013)	An Empirical Analysis of The Determinants of Bank Profitability in Romania	Dependent: ROAA, ROAE Independent: EA, NPL, NIEA, LA, LIQA, FC, NIIR, LNTA, CR5, MKCGDP, GDP, INF	The ratio of NPL, NIEA and LIQA has a significant impact upon the banking profitability. Instead, other factors did not have an important effect. Regarding the four external independent variables used, only CR5 and GDP had significant impact upon the banking profitability.
2.	Dr. Husain Al-Omar, Dr. Abdullah Al-Mutairi (2008)	Bank-Specific Determinants of Profitability: The case of Kuwait	Dependent: ROA Independent: EA, LA, Operating Cost to Total Asset Ratio, NIAA, LogA	The EA, LA, operating expenses ratio, NIAA, and LogA explain about 67% of the variation in ROA. Only EA, NIAA, and LogA had significant impact to bank's profitability in Kuwait.
3.	Dr. Yoppy Palupi Purbaningsih (2014)	The Effect of Liquidity Risk and Non Performing Financing (NPF) Ratio to Commercial Sharia Bank Profitability in Indonesia	Dependent: ROA Independent: LTA, LIQD, FDR, NPF	The LTA, FDR, and NPF had not significant effect. Whereas LIQD negatively affect to profitability, but LTA, LAD, FDR and NPF simultaneously significantly affect to profitability.
4.	Febriyanti Farhah (2013)	<i>Pengaruh Kualitas Aktiva Produktif terhadap Profitabilitas Bank (Studi Pada PT Bank Tabungan Negara (Persero Tbk.)</i>	Dependent: ROA Independent: Clarified ratio of productive asset, PPAP compliance, and PPAP to productive assets	Clarified ratio of productive asset and PPAP to productive asset ratio had negatively significant effect to profitability, while PPAP compliance ratio had positively significant effect to profitability. All independent variables simultaneously had significant effect to profitability.
5.	Maria Regina Rosario Sianturi	<i>Pengaruh CAR, NPL, LDR, NIM, dan BOPO terhadap Profitabilitas</i>	Dependent: ROA Independent:	CAR, NPL, LDR, NIM, and BOPO are significant simultaneously influence ROA as profitability.

	(2012)	<i>Perbankan (Studi Kasus pada Bank Umum yang Listed di Bursa Efek Indonesia Tahun 2007-2011)</i>	CAR, NPL, LDR, NIM, BOPO	Meanwhile partially, the effects of independent variables to ROA are: CAR and LDR have positive effect but not significant, NPL has negative effect but not significant, NIM has positive and significant effect, and BOPO has significant negative effect
6.	Mohamed Khaled Al-Jafari, Mohammad Alchami (2014)	Determinants of Bank Profitability: Evidence from Syria	Dependent: ROAA, ROAE Independent: INF, GDP, HHI, CAP, PL, LIQD, OPEX, LogA	The results found a significant relationship of INF and real GDP growth rate to ROAE as bank profitability. The HHI and CAP ratio had no impact on ROAE. However, LIQD, LogA, OPEX, and PL significantly affect bank profitability measured by ROAA.
7.	Ruslim (2012)	<i>Analisis Pengaruh Capital Adequacy Ratio (CAR), Non Performing Loan (NPL), dan Loan to Deposit Ratio (LDR) terhadap Return On Asset (ROA) pada Bank Umum Syariah yang Terdaftar di Bank Indonesia</i>	Dependent: ROA Independent: CAR, NPL, LDR	CAR, NPL, and LDR simultaneously have closely related and significant influence to ROA. Meanwhile, partially CAR is not significantly influence ROA, NPL has negative effect and significant to ROA, and LDR has positive effect and significant to ROA.
8.	Suresh Kumar (2014)	Non-Performing Assets: An Indian Perspective	Dependent: ROA Independent: NPA	The NPA has adverse impact over ROA and CAR of banks. Every bank has to ensure that an asset does not become NPA. If it does, proper steps should be taken for early recovery, failing which profitability of the bank will be eroded. Therefore proper management of NPAs in banks is the necessity.

Methodology

This research consists of several steps from the beginning process until finishing result.

1. Problem Identification
It presents research background, formulation, objectives, and structure.
2. Theoretical Review
It consists a lot of theory related to Islamic bank and financial ratios as research variables. There is also come up with several former researches similar to this topic that can support as basic information.
3. Hypothesis
Based on problem background, related theories, and research framework before, research hypothesis composed as follows:
 - H1: NPF gives significant negative effect to profitability (ROA) of Islamic banks in Indonesia partially
 - H2: BOPO gives significant negative effect to profitability (ROA) of Islamic banks in Indonesia partially
 - H3: NIM gives significant positive effect to profitability (ROA) of Islamic banks in Indonesia partially

- H4: FDR gives significant positive effect to profitability (ROA) of Islamic banks in Indonesia partially
 - H5: PPAP Compliance gives significant positive effect to profitability (ROA) of Islamic banks in Indonesia partially
 - H6: NPA gives significant negative effect to profitability (ROA) of Islamic banks in Indonesia partially
 - H7: EA gives significant positive effect to profitability (ROA) of Islamic banks in Indonesia partially
 - H8: LIQD gives significant negative effect to profitability (ROA) of Islamic banks in Indonesia partially
 - H9: NPF, BOPO, NIM, FDR, PPAP Compliance, NPA, EA, and LIQD give significant effect to profitability (ROA) of Islamic banks in Indonesia simultaneously
4. Research Instruments Development
The population of this research is Islamic Banks in Indonesia amounted to 11 banks and the sample selected is 6 banks with criteria bank that listed and has publicly report the financial statement in Bank Indonesia.
 5. Data Collection
The data used in this research is secondary data that were obtained from annual report and financial report of each bank by searching at official website of Bank Indonesia and official website of Islamic Banks sample. Data collected from the study of literature through books, journals, thesis research, and others related to the topic to get the basic theory and analysis techniques in solving the problems.
 6. Data Processing and Analysis
It presents an explanation about tests used in this research and the results discussion.
 7. Comparison Analysis to Overall Islamic Bank Condition
Sample in this research covers the condition of major Islamic Banks in Indonesia, which amounted to six banks. So, the comparison between 6 huge banks condition and overall banking current condition is necessary, in order to get reliable and factual research result.
 8. Conclusion and Recommendation
It consists of conclusion describe analysis data gist result and also the recommendation to other related parties such as further researchers and banking industries.

Result and Analysis

Before performing this regression analysis, the data of samples already passed data adequacy test, classical assumption test for normality test, multicollinearity, heteroscedasticity and autocorrelation test. Then, it can be followed on the next stage of the analysis using multiple linear regression analysis. The test use multiple linear regression analysis with 5% significant level.

Multiple Linear Regression Result

Table 2. Model Summary

Model Summary ^b				
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.957 ^a	.917	.883	.3959784

a. Predictors: (Constant), LIQD, NIM, NPA, PPAP, BOPO, FDR, NPF, EA

b. Dependent Variable: ROA

From Table 2, the value of coefficient determination (R-Square) is 0.917 or 91.7%. It means independent variables (NPF, BOPO, NIM, FDR, PPAP Compliance, NPA, EA, and LIQD) simultaneously can explain about 91.7% of dependent variable (ROA) and another 8.3% is explained by other variables out of this research.

Table 3. F Test

ANOVA ^b						
Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	34.456	8	4.307	27.468	.000 ^a
	Residual	3.136	20	.157		
	Total	37.592	28			

a. Predictors: (Constant), LIQD, NIM, NPA, PPAP, BOPO, FDR, NPF, EA

b. Dependent Variable: ROA

Table 3 above shown that F value is 27.468 with 0.000 significance, so when significance value is lower than 0.05, that means independents variables (NPF, BOPO, NIM, FDR, PPAP Compliance, NPA, EA, and LIQD) simultaneously influence the dependent variable (ROA). Then the hypothesis is accepted. Every alteration that happens to independent variables (NPF, BOPO, NIM, FDR, PPAP Compliance, NPA, EA, and LIQD) simultaneously will give influence to profitability (ROA) of Islamic Banks in Indonesia. So hypothesis 9 is accepted.

Table 4. T Test
Coefficients^a

Model	Unstandardized Coefficients			Standardized Coefficients		T	Sig.
	B	Std. Error		Beta			
1	(Constant)	3.518	1.576			2.232	.037
	NPF	-.064	.097	-.068		-.660	.517
	BOPO	-.051	.006	-.915		-8.945	.000
	NIM	.132	.026	.382		5.099	.000
	FDR	-.008	.008	-.117		-.998	.330
	PPAP	.023	.010	.165		2.224	.038
	NPA	.001	.105	.001		.006	.996
	EA	.014	.019	.106		.744	.466
	LIQD	-.002	.003	-.052		-.585	.565

a. Dependent Variable: ROA

From Table 4, it can be seen there are only 3 from 8 independent variables that partially give significant influence to dependent variable, which are BOPO, NIM, and PPAP Compliance with each significance value are 0.000, 0.000, and 0.038.

▪ Hypothesis Testing

The explanation about each variable will be shown as follows:

- Non-Performing Financing (NPF)

From the result, known that higher NPF percentage would make ROA goes down. It happens because amount of bad debt can increase loss risk, and the payback that does not collected on time would hamper the development of operational activities. In addition, the NPF could happen not because the debtor cannot pay, but tight regulation of Bank Indonesia in terms of credit classification resulting the debtor was located in the current category can drop to less smoothly. But when the bank still has enough reserve funds, NPF ratio does not give many changes to bank's profitability. This result is also supported by studies that have been conducted Maria Regina Rosario Sian (2014) which says that NPL has a negative effect but not significant to ROA. Also in the journal of Dr. Yoppy Palupi Purbaningsih (2014) and the results of Saladin M. Fahmy (2013) shows that risk of banking business is reflected in the NPF did not have significant effect on ROA. On the other hand, Dani Pranata, Raden Rustam Hidayat, and Nila Firdausi Nuzula (2014) found that NPF has a significant negative effect on ROA. Such differences may occur due to differences in the observation period and the population used in the study, such as those who chose a sample of the population of foreign private bank in Indonesia with the data from 2010 to 2012. So hypothesis 1 is rejected.

- *Operational Efficiency (BOPO)*

Based on Table 4, higher BOPO means smaller ROA. This is due to the rising cost of bank operations both influenced by external factors such as inflation and internal factors in an effort to renew the facilities and services provided. While most banks' income derived from its operations. When the increase in revenues not as much as its operational costs, it can be due to the proliferation of competition between banks, then profitability is declining. These results are also in line with research of Maria Regina Rosario Sianturi (2012) and the journal made by Dhian Dayinta Pratiwi and Drs. H. M Kholiq Mahfud, MP. found that the effect of BOPO to ROA is significantly negative. So hypothesis 2 is accepted.

- *Net Interest Margin (NIM)*

With significance value of 0.000, it can be said that higher NIM brings higher ROA. Each improvement in net interest income, which represents the difference between the total interest costs and total interest income resulted in an increase in profit before tax, which in turn resulted in an increase of ROA. It is one of the result from success marketing that influence people to borrow money from the bank, so bank can gets much income from sharing profit. Then, NIM also explains that net interest income take a big part of earning assets that deliver revenue for the bank. As stated by Maria Regina Rosario Sianturi (2012) and Marnov PP Nainggolan (2009), that NIM has a positive significant effect on ROA. So hypothesis 3 is accepted.

- *Financing to Deposit Ratio (FDR)*

Result on Table 4 shown that higher FDR means smaller ROA but not significant. This result supported by Suryani (2011) who proven that there was no significant effect of FDR to ROA. Amount of financing which excess distributed makes bank liquidity is in danger, because that condition can increase bad debts risk which result in smaller bank's profitability. But since that bank has enough capital reserve, the effect of FDR is not too important. It is different with Ruslim (2012) who stated that FDR gives positive and significant influence to ROA. This differences caused by number of Islamic bank's sample that had been chosen by Ruslim, which only 3 banks with observation period 2004 – 2010. Where those banks are huge banks with nice reputation in public eyes, so it right if amount of big distributed financing can also deliver big profit. So hypothesis 4 is rejected.

- *Allowance for Earning Asset Possible Losses (PPAP) Compliance*

From Table 4 it can be seen that PPAP Compliance give positive significant influence to ROA of Islamic banks in Indonesia. If PPAP Compliance value rise, ROA also would goes up. That means higher PPAP compliance may reduce the probability of a bank in danger condition, because there are fund reserves to covering the potentially loss of assets. With enough proportion of fund reserves, bank can develop its business or operational activities so the income would rise. Febriyanti Farhah (2013) also proven that PPAP Compliance had positive and significant effect to ROA. This research result is different from a journal which wrote by Enggar Koesoema Sari and Prof. Dr. H. Imam Ghozali, M. Com., Ph.D., Akt., where is effect of PPAP Compliance does not significant to ROA. The differences could happens because the number of possible losses assets is just a few, so those assets did not give much contribution for bank in gain some revenue. So hypothesis 5 is accepted.

- *Non Performing Assets (NPA)*

The unstandardized beta coefficient 0.001 indicates that NPA has positive influences to ROA, so high NPA would increase ROA value but not significant. It can be happen because some assets that potentially bring losses not in proportion to profit growth which come from productive assets, so the influence of NPA assumed not too important. This research result is different with Suresh Kumar (2014) and Khalid Ashraf Chisti (2012) who found that NPA had negative and significant influence to ROA with sample of banks in India, so the differences is possible since the economic condition and banking regulations of every country also different. So hypothesis 6 is rejected.

- *Equity to Total Assets Ratio (EA)*

Based on Table 4, EA gives positive but not significant effect to ROA of Islamic banks in Indonesia. High value of EA makes value of ROA increase. That means amount of bank capital used only support a half of activities that generate profit such as development in bank business, so the impact is not big enough. This result supported by Angela Roman AED. (2013) who found that EA did not had an important effect to ROA, but Dr. Husain Al-Omar and Dr. Abdullah Al-Mutairi (2008) stated in their journal that EA had significant impact to ROA with sample of Kuwait banking for 1993 - 2005. In addition, the difference appears because equity supports bank's business, acting as a safety net in the case of adverse developments on Kuwait banks. So, equity to asset ratio give high contribution to bank's profitability at that period of time. So hypothesis 7 is rejected.

- *Liquidity Assets to Total Deposits Ratio (LIQD)*

LIQD give negative but not significant effect to ROA of Islamic banks in Indonesia. Higher LIQD ratio cause smaller value of ROA. This ratio has an influence on the level of profitability because if cash is available in a bank, it is big signifying inefficient state banks. In another side, Mohamed Khaled Al-Jafari and Mohammad Alchami (2014), also Dr. Yoppy Palupi Purbaningsih (2014) stated that LIQD significantly affect bank profitability measured by ROA. So hypothesis 8 is rejected.

The equation of multiple linear regression model in this research is

$$\text{ROA} = 3.518 - 0.064 \text{ NPF} - 0.051 \text{ BOPO} + 0.132 \text{ NIM} - 0.008 \text{ FDR} + 0.023 \text{ PPAP} + 0.001 \text{ NPA} + 0.014 \text{ EA} - 0.002 \text{ LIQD}$$

- The constant value of the equation is 3.518. When the independent variables (NPF, BOPO, NIM, FDR, PPAP Compliance, NPA, EA, and LIQD) are stable, then ROA will rise about 3.518%.
- In this regression model, coefficient of NPF is -0.064 , coefficient of BOPO is -0.051 , coefficient of NIM is 0.132 , coefficient of FDR is -0.008 , coefficient of PPAP Compliance is 0.023 , coefficient of NPA is 0.001 , coefficient of EA is 0.014 , and coefficient of LIQD is -0.002 .

▪ Comparison Analysis to Overall Islamic Bank Condition

Table 5. Model Summary of 11 banks

Model Summary^b

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.830 ^a	.689	.586	.83670

a. Predictors: (Constant), LIQD, NIM, PPAP, NPA, BOPO, NPF, EA, FDR

b. Dependent Variable: ROA

The observation results of 11 Islamic banks in Indonesia (2011-2013) shown that 8 independent variables used in this study are able to explain 68.9% overall condition of Indonesian Islamic banking profitability. With five independent variables have a significant effect on ROA, they are BOPO (-), FDR (-), PPAP Compliance (+), EA (+), and LIQD (+). This is contrast to this study, where only variable ROA (-), NIM (+), and PPAP Compliance (+) which has a significant effect on ROA. Then the regression model of all population based on Table 6 below is

$$\text{ROA} = 5.179 + 0.377 \text{ NPF} - 0.097 \text{ BOPO} + 0.022 \text{ NIM} - 0.034 \text{ FDR} + 0.049 \text{ PPAP} + 0.042 \text{ NPA} + 0.055 \text{ EA} + 0.005 \text{ LIQD}$$

Table 6. T test Result of 11 banks

Coefficients^a

Model	Unstandardized Coefficients		Standardized Coefficients	T	Sig.	Collinearity Statistics	
	B	Std. Error	Beta			Tolerance	VIF
1 (Constant)	5.179	2.793		1.854	.076		
NPF	.377	.196	.346	1.917	.067	.398	2.515
BOPO	-.097	.020	-.856	-4.903	.000	.424	2.356
NIM	.022	.050	.052	.437	.666	.909	1.100
FDR	-.034	.011	-1.122	-3.190	.004	.105	9.556
PPAP	.049	.017	.362	2.822	.009	.785	1.274
NPA	.042	.189	.040	.223	.825	.412	2.429

EA	.055	.024	.546	2.261	.033	.222	4.501
LIQD	.005	.002	.622	2.477	.021	.205	4.880

a. Dependent Variable: ROA

- On the banks that relatively new, the factors that affect the profitability began to emerge from the aspect of capital, liquidity, operational, and assets. Although the percentage of the effect is not large enough and other factors outside the research began to enter and taking place at 31.1%. Perhaps because more and more risks arising both from within and from outside, as competition among banks also problems arising from the globalization system. So each aspect had its own role to deliver income to the bank, but only in small proportion. While for the banks that already have more experienced, their profitability sufficiently most described by the asset and operational aspects. Then, because they already have strong resistance, those huge banks are survive from globalization risk issues.

- The differences of two observation about Islamic banks in Indonesia are explain below

- *Non-Performing Financing (NPF)*

On all population observation of Islamic banks in Indonesia at 2011-2013, the effect of NPF become positive but not significant to ROA. That can be happen because PPAP value of half major banks and another five minor banks can cover their bad credits. It is different with research result about six major Islamic banks in Indonesia that has negative and not significant influence of NPF to ROA. Banking profitability may still increase with higher NPF because income sources out of fee-based income are relatively high. So that both positive and negative influences, ROA will not get much disturbed by the NPF value.

- *Operational Efficiency (BOPO)*

Similar to this research result, the negative effect on BOPO to ROA of 11 Islamic banks last 3 years (2011-2013) still has a high significance level. It indicates that bank's income from operational activities give high contribution in deliver profitability of all kind of bank.

- *Net Interest Margin (NIM)*

NIM's influence become positive insignificant in overall ROA of Islamic banking. That happens because the profitability growth of banks dominated by its business operational income. As well as the net sharing income is not too large because the sharing received from financing is smaller. But the sharing percentage to customer who deposit money is high, as an effort of marketing strategy so that the public is more interested in saving their money. That kind of thing is usually done by new banks. While in the steady banks, they still got high demand from customers even the profit sharing for bank's management which puts on the market is higher than its competitor. It means banks already gained trust from public, so the net sharing income brought significant effect to profitability.

- *Financing to Deposit Ratio (FDR)*

FDR gives negatively significant effect to overall profitability's of Islamic banking in Indonesia since 2011 – 2013. It happens because start up banks provides many financing funds as an effort to get more clients, although their capitals and fund reserves are minus. Actually that is really dangerous to the bank's sustainability with increase of liquidity risk. In other side, steady banks have many strategy to deliver income. They are not only focus on distribute financing but also focus on other business development. So from 6 Islamic banks observation, FDR does not give significant effect to ROA as profitability.

- *Allowance for Earning Asset Possible Losses (PPAP) Compliance*

PPAP Compliance had positive and significant influence to profitability (ROA), both all population of Islamic banking in Indonesia for 2011 – 2013 observation periods and 6 major Islamic banks in Indonesia for 2009 – 2013. It indicates that prevent strategy in managing risks always being

important to decrease asset possible losses and increase bank's profitability, especially with allowance for earning asset possible losses.

- *Non Performing Assets (NPA)*

NPA for all population of Islamic banks in Indonesia has a positive but does not give significant effect to ROA. It also occurred on observation of 6 major Islamic bank. That happens because NPA of most Islamic banks in Indonesia are still in Sub-Standard Asset category, which is NPA for a period less than or equal to 12 months. In case of such assets, the current net worth of the borrower/guarantor or the current market value of the security charged is not enough to ensure recovery of the dues to the bank in full. But sub-standard asset is NPA category with smallest losses possibility, so the influence of NPA assumed not too important.

- *Equity to Total Assets Ratio (EA)*

EA give positive and significant influence to profitability of 11 Islamic banks in Indonesia for 2011 – 2013 because at those years, the capital becomes more important in order to compare with growth of banking risk. Different with this research result that stated EA does not give significant influence to ROA. While in steady banks, capital is not the most important issue to keep the bank's management development up, but capital still needed in enough proportion.

- *Liquidity Assets to Total Deposits Ratio (LIQD)*

LIQD has positive and significant influence to ROA of 11 Islamic banks in Indonesia with 2011 – 2013 observation periods. It can be happen because appropriate amount of liquid asset can reduce the risk, if the customers suddenly want to withdraw their fund. Moreover, LIQD give negative and insignificant influence to profitability on observation of six major Islamic banks in Indonesia. Because with high level of LIQD, banks are left with less liquidity in hands to handle the day to day operations while steady banks have many kind of business than start up banks.

Conclusion and Recommendation

Conclusion

Based on discussion and results of data analysis described in the previous chapter, it can be concluded as follow:

1. BOPO, NIM, and PPAP Compliance influence the profitability (ROA) of Islamic banks in Indonesia simultaneously and partially. While BOPO gives negative and significant effect to ROA, NIM gives positive and significant effect to ROA, and PPAP Compliance gives positive and significant effect to ROA
2. When other variables (NPF, FDR, NPA, EA, and LIQD) only influence profitability (ROA) of Islamic banks in Indonesia simultaneously

Recommendation

When globalization risks are arise and take large portion in the market competition, the stakeholders will find another bank which provide better financial performance to save their money. So it is necessary to Islamic banks to defend their existence through increasing the profitability from every opportunities. Based on the obtained results, Islamic banks in Indonesia can improve their profitability, especially by focus on the quality of assets (PPAP Compliance), profit sharing income (NIM), and operational efficiency (BOPO). Related to BOPO, bank management should validates every cost or expenses taken out by bank, whether it is necessary to issued or not. Related to NIM bank always calculates the cost of funds carefully so it can determines the competitive based profit sharing percentages. And related to PPAP Compliance ratio, bank management should observes the financing agreements that proper to be financed.

As future research directions, it should add more samples and observation periods so the research scope can be more large and the result more better and varieties. And to achieve high number of

Rsquare which explains how far independent variables influence the dependent variable; further research should add another financial ratios and risk factors as independent variable that not yet include in this research, such as interest rates, asset size, and capital adequacy.

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