

The Effect of Third Party Funding and Non Performing Financing on The Development of Islamic Banking Finance in Indonesia

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Abstract: This study was performed to determine how much influence of third-party funds and non-performing financing to financing development of Islamic banking in Indonesia. In this study the influence of the amount independent variables partially or simultaneously on the dependent variable. The hypothesis for this research is third-party funds and non-performing financing affects the lending of Islamic banking financing in Indonesia. The data used in this research is secondary data of Bank Indonesia report on the development of Islamic banking. Multiple regression analysis is performed to find the influence of third-party funds and variable non-performing financing the development of financing. The data used in the regression must be pass the classical assumption test. The results of this research note that the third-party funds have a significant effect and non-performing financing no significant effect on the development of Islamic banking financing. Simultaneously, a third-party funds and non-performing financing a significant effect on the development of Islamic banking financing in Indonesia. Both independent variables have contributed as much as 24.7% of the change in the independent variable with a strong enough relationship level by 50%.

Keywords: financing; third party funds; NPF

1. Introduction

Islamic banks are financial institutions that provide credit and other services in payment traffic and money circulation that operate according to sharia principles. Therefore, a bank's business will always be related to money issues as its business merchandise.

Financing is an activity that is the main operational activity in Islamic banking. According to law No. 21 of 2008 Financing is the provision of funds or bills equivalent to it based on an agreement between Islamic banking and other parties which requires the party who is given the funding facility to return the funds after a certain period of time in return for *ujrah*, without compensation, or for results.

Money collected by banks from the public is known as third party funds. Islamic banking can attract third party funds from the public in the form of deposits (*wadiah*), *mudharabah muthlaqah* investments, and special *mudharabah muqayyadah* investments (Muhammad, 2005).

NPF (Non Performing Financing) is a situation where the customer is no longer able to pay part or all the obligations to the bank as promised (Kuncoro, 2002). If not handled

properly, problematic financing is a very potential source of loss for bank. Therefore, a systematic and sustainable treatment is needed. NPF (Non Performing Financing) is very influential in controlling costs and at the same time also influences the financing policies that will be carried out by the bank itself.

This becomes more interesting and important to examine the influence of third party funds (TPF) and non-performing financing (NPF) on the Development of Islamic Banking Financing in Indonesia. Moreover, the growth of sharia banking financing in the last few years has fallen drastically. In 2011 financing growth was recorded at 50.56%, then in 2012 it was 43.68% and then continued to decline and only recorded growth of 24.82% in 2013.

Third party funds and non-performing financing are very interesting to study their effect on financing based on the discrepancy that occurs between Rukiah's research on the effect of third party funds and non-performing financing on financing using data for 2005-2008 (Rukiah, 2010) with initial observations researchers who use Islamic banking data for the last twelve years.

In addition, the results of research from Haryadi stated that non-performing financing had a positive and significant effect on Islamic banking financing in Indonesia (Haryadi, 2009). This is also the case with initial observations using Islamic banking data with a longer range of twelve years. The results show that only in 2007 and 2012 did non-performing financing have a positive effect on financing. Apart from these two years, non-performing financing has a negative effect on sharia banking financing in Indonesia.

2. Literature Review

Financing is the main activity in Islamic banking operations. According to law No. 21 of 2008 Financing is the provision of funds or bills equivalent to it based on an agreement between Islamic banking and other parties which requires the party who is given the funding facility to return the funds after a certain period in return for *ujrah*, without compensation, or for results.

As an intermediary institution, Islamic banking will function as a party that distributes financing as well as collects funds from the public. Distribution of financing is very important because it is the main activity which is the largest source of income for Islamic banking. The activity of collecting funds from the public is also very important because it is the source of the largest portion of funds in Islamic banking. The source of funds from the community will later be used by Islamic banking as financing to other parties.

Money collected by banks from the public is known as third party funds. Islamic banking can attract third party funds from the public in the form of deposits (*wadiah*), *mudharabah muthlaqah* investments, and special *mudharabah muqayyadah* investments. Custody (*wadiah*) is a deposit that is guaranteed security and returns. This form of *wadiah* is usually applied to *wadiah* savings products or *wadiah* current accounts in Islamic banking. *Mudharabah muthlaqah* investment is a general investment, the bank will share the capital and share the risk and will pay a share of the profits in accordance with the portion of each investment. This form of *mudharabah muthlaqah* investment is usually applied to *mudharabah* savings products and *mudharabah* deposits. *Mudharabah muqayyadah* investment is a special investment account where the bank acts as an investment manager to obtain a fee (Muhammad, 2005).

Regardless of the size of the third party funds collected, Islamic banking is obliged to channel these funds for financing. The allocation of this financing distribution is adjusted to the policies that have been outlined, both by banks and by Bank of Indonesia policies. Policies and regulations related to financing are static, while third party funds are dynamic. Therefore,

the size of third party funds will greatly affect the amount of financing channeled by Islamic banking.

Warjiyo (2004) argues that the growth of Islamic banking financing is influenced by internal factors and external factors. Included in the internal factors that can affect the amount of financing are third party funds, the amount of non-performing financing and capital as measured by the capital adequacy ratio (capital adequacy ratio).

This is reinforced by the results of research conducted by Siregar (2004) and Rukiah (2010). The results of this study suggest that third party funds have a very significant effect on the distribution of Islamic banking funds in Indonesia.

Rivai (2008) and Andria stated: Funding essentially means I Believe, I Trust, 'I believe' or I place my trust'. The word financing which means trust, means that the financing institution as shahibul mal places trust in someone to carry out the mandate given. These funds must be used properly, fairly, and must be accompanied by clear terms and conditions, and mutually beneficial for both parties.

In channeling this financing activity, Islamic banking has risks. This risk can arise when the party receiving the financing is unable to return the funds. This financing risk can be seen from the collectability of financing. Collectability is categorized into five types, namely current, substandard, doubtful, on special mention and loss (Muhammad, 2005).

Financing that is included in the category of doubtful, under special mention and loss is problematic financing in Islamic banking. This problematic financing can affect productive assets that are usually used as funds to be channeled as financing. With non-performing financing, there will be a write-off of productive assets, the amount of which is adjusted as a reserve for possible losses that may occur. Therefore, the greater the non-performing financing, the greater the loss of productive assets by the banks. The fewer productive assets, the less allocation of sharia banking financing distribution will be reduced.

The term commonly used to measure problem financing is non-performing financing. Its influence on financing is strengthened by research results from Siregar (2004) and Haryadi (2009). The results of this study indicate that non-performing financing has a significant effect on the amount of distribution of Islamic banking funds in Indonesia.

Factors that can affect the distribution of financing other than third party funds are non-performing financing in Islamic banking. These two variables can jointly influence the development of Islamic banking financing in Indonesia. The above framework can be described as a research model as follows:

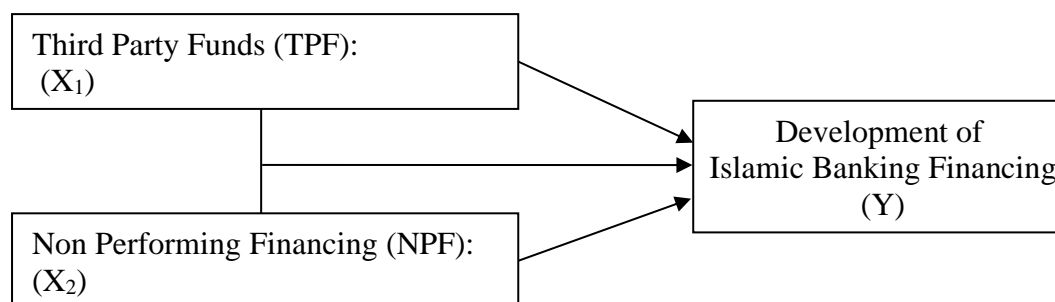


Figure 1. Research Framework

3. Research Methods

Based on the nature of the problem, the method used in this research is quantitative. According to Sugiyono, the quantitative research method is a research method that is based on the nature

of positivism, is used to examine certain populations or samples, collects data using research instruments, analyzes quantitative or statistical data with the aim of testing established hypotheses (Sugiyono, 2012).

The population in this study is Islamic banking financing throughout Indonesia. The banking in question is a bank financial institution that uses sharia principles in its operations including sharia commercial banks, sharia business units and sharia rural credit banks. In determining the sample of this study using purposive sampling technique. This technique selects a sample based on the knowledge that the sample is considered the key to the existing population (Bungin, 2010: 125). The sample used as the object of this study is the financing disbursed by Islamic commercial banks and Islamic business units with a time limit from 2004 to 2020. This sample was chosen because it facilitates research and financing of Islamic commercial banks and Islamic business units is considered the main key. of sharia banking financing throughout Indonesia.

The type of data used in this research is secondary data. In this study using data collection methods with documentation. The use of documentation techniques because this method is commonly used to collect data in the form of written data containing information and explanations, as well as thoughts about phenomena that are still actual and in accordance with research problems.

In accordance with the title of this study, the influence of third party funds and non-performing financing on the development of Islamic banking financing, there are three variables to be examined. These variables are the variables of third party funds and non-performing financing variables which are included in the independent variables, and the variable development of Islamic banking financing which is the dependent variable. The following research model is used:

$$Y = \alpha + \beta_1 X_1 + \beta_2 X_2 + \varepsilon$$

Y	= Development of Islamic banking financing (DIBF)
α	= Constant
$\beta_1 - \beta_2$	= Regression coefficient
X_1	= Third party funds (TPF)
X_2	= Non Performing Financing (NPF)
ε	= Error

In this study, several tests and statistical analysis were carried out on the research data. First, a classic assumption test is carried out to avoid biased research results. Furthermore, multiple regression analysis was carried out to determine the relationship and influence of the independent variables on the dependent variable. And the last thing to do is testing the hypothesis that has been determined at the beginning of the study. Data analysis in this study was assisted by a computer program, namely the SPSS 24.0 program.

4. Results and Discussion

The data used in this research is secondary data. To determine the accuracy of the multiple regression model, it must pass tests on several classical assumptions. the tests used are: Normality Test, Multicollinearity, Heteroscedasticity, and Autocorrelation. Following are the results of the classic assumption test using SPSS 24.0:

The normality test is carried out based on the assumption that a good regression equation is one that has a normal or close to normal data distribution. To find out whether the data used is normally distributed or not in this study by looking at the normal probability plot.

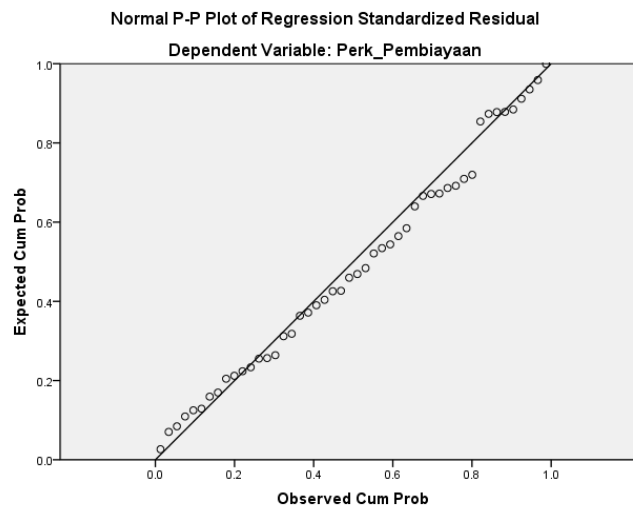


Figure 2. Normal Probability Plot

Figure 2 shows that the data points seem to spread around the diagonal line and the distribution also follows the direction of the diagonal line. Based on this picture, the data used to create the multiple regression model has a normal distribution. therefore, the multiple regression model that uses these data is appropriate to use to predict how much influence the independent variable has on the dependent variable.

The multicollinearity test is used to determine whether in the multiple regression model the independent variables are correlated or not. To get a good multiple regression model, the independent variables should not be correlated with each other. The method used to detect multicollinearity in this study is to use the k value taken from the eigen value.

Table 1. Collinearity Diagnostics^a

Model	Dimension	Eigenvalue	Condition Index	Variance Proportions		
				(Constant)	TPF	NPF
1	1	2.643	1.000	.01	.04	.01
	2	.330	2.830	.01	.70	.05
	3	.027	9.808	.98	.26	.94

a. Dependent Variable: DIBF

Table 1 shows that the maximum eigen value is 2.643 while the minimum eigen value is 0.027. After being calculated by dividing the largest and smallest eigenvalues, a k value of 97.9 is obtained. Because the resulting value is $95.89 < 100$, it can be concluded that the regression model has low multicollinearity or does not have multicollinearity between the independent variables.

The heteroscedasticity test was carried out with the aim of testing the variance of the residual variance from one observation to another. If the results are different, it is called heteroscedasticity. To detect the presence or absence of heteroscedasticity in this regression model by observing the scatter plot graph.

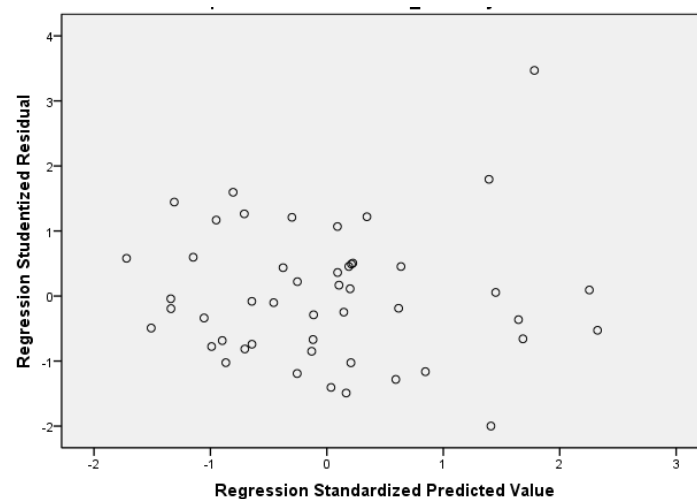


Figure 3. Scatterplot

In Figure 3, the data plot points are randomly distributed and do not form a specific pattern. The dots in the scatterplot image spread to the left, right, up and down from zero. The spread of the dots indicates that heteroscedasticity does not occur.

The autocorrelation test was carried out to test the assumption that the data used is independent. To detect the presence or absence of autocorrelation in this study, the Run Test statistical test was used. Based on data processing using SPSS 24.0, the following results are obtained:

Table 2. Runs Test

	Unstandardized Residual
Test Value ^a	-.44011
Cases < Test Value	24
Cases >= Test Value	24
Total Cases	48
Number of Runs	18
Z	-1.897
Asymp. Sig. (2-tailed)	.058
a. Median	

From table 2 it is known that the significance value of Asymp. Sig. (2-tailed) is 0.058. The significance value is greater than $\alpha = 0.05$, which means it is not significant. Based on the results of the Run Test it can be concluded that the data used in the multiple regression model is free from autocorrelation problems.

From the results of all the tests above, it can be concluded that this study is free from classical assumption problems. That way, the resulting multiple regression model can be used as a good estimator for determining research conclusions. Likewise, being free from classical assumptions makes the results of hypothesis testing more accurate.

The independent variables of third party funds and non-performing financing jointly influence the distribution of sharia banking financing. the size of the determination of the two independent variables can be seen in the table below:

Table 3. Model Summary^b

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.570 ^a	.325	.295	4.91726

a. Predictors: (Constant), NPF, TPF

b. Dependent Variable: DIBF

The coefficient of determination or R Square is a quantity that provides information on the goodness of fit of the regression equation, it gives the proportion or percentage of the strength of the variable that explains (X1 and X2) simultaneously on the variation of the dependent variable (Y). The R Square value in the table above is 0.325 or 32.5%. These results indicate that the independent variables, namely third party funds and non-performing financing, simultaneously have an effect of 32.5% on changes in the dependent variable, namely the development of Islamic banking financing variable. While the remaining 67.5% change from the dependent variable is influenced by other variables.

After knowing the contribution of the two independent variables simultaneously, the next step is to test the significance of the two independent variables simultaneously. ANOVA test was conducted to simultaneously test the research hypothesis.

Table 4. ANOVA^b

	Model	Sum of Squares	df	Mean Square	F	Sig.
1	Regression	523.423	2	261.711	10.824	.000 ^a
	Residual	1088.075	45	24.179		
	Total	1611.497	47			

a. Predictors: (Constant), NPF, TPF

b. Dependent Variable: DIBF

The probability value of the third party funds variable in the ANOVA table is 0.000. The significance level used in this study is 95% or degree $\alpha = 5\%$. The probability of the resulting independent variable of 0.000 is below the α level of 0.05. The results of calculations using ANOVA and paying attention to the probability value accept the alternative hypothesis. Based on the hypothesis test, it can be stated that the variables of third party funds and non-performing financing simultaneously have a significant effect on the development of Islamic banking financing in Indonesia.

Conducting multiple regression analysis of the independent variables on the dependent variable, the results are known as follows:

Table 5. Coefficients^a

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	8.493	3.253		2.610	.012
	TPF	.432	.117	.478	3.679	.001
	NPF	-1.041	.712	-.190	-1.463	.151

a. Dependent Variable: DIBF

The probability value of the third party fund variable in the coefficients table is 0.001. The significance level used in this study is 95% or degree $\alpha = 5\%$. The probability of the

resulting third party fund variable of 0.001 is below the α level of 0.05. The results of the calculation using the t test and the level of significance by paying attention to the probability value both accept the alternative hypothesis. Based on the hypothesis test, it can be stated that the third party fund variable has a significant effect on the development of Islamic banking financing in Indonesia.

Third party funds have a direct relationship with financing channeled by Islamic banking in Indonesia. In the coefficients table, there is a multiple regression coefficient value of third party funds of (+) 0.432. The positive value of the coefficient indicates that the relationship between the third party fund variable and the dependent variable is unidirectional. This means that the more third party funds increase, the more Islamic banking financing will develop in Indonesia.

Third party funds collected by Islamic banking every year always increase. Over the past ten years the amount of third party funds has increased by 31 times. At the beginning of 2004 the amount of third party funds only amounted to 5.7 trillion rupiah. At the end of 2013 Islamic banking managed to collect third party funds amounting to 183.5 trillion rupiah.

The high growth of third party funds occurred after the global financial crisis in 2008. The crisis had a good effect on the collection of Islamic banking funds in Indonesia. People were traumatized by the 1998 crisis that made several conventional banks bankrupt. People are more confident in keeping their money in Islamic banking for fear that the events of 1998 will be repeated. This can be seen from the growth of third party funds in 2009, 2010 and 2011 which increased quite high.

The development of financing channeled by Islamic banking every year also always increases. Over the last twelve years the amount of financing has grown by 36 times. At the beginning of 2004 the amount of financing disbursed only amounted to 5.8 trillion rupiah. At the end of 2015, Islamic banking managed to distribute financing of 212.996 trillion rupiah.

The mandate received by Islamic banking from the public should not be misused. Third party funds that have been collected must be managed and channeled properly by Islamic banking. Financing development always increases every year following the development of third party funds. Islamic banking has managed to maintain its development to continue to increase every year. This shows that the intermediary function in Islamic banking is very good.

5. Conclusion

This study observes the development of financing carried out by Islamic banking in Indonesia. This study also examines the influence of third party funds and non-performing financing variables on the development of Islamic banking financing. Based on the research results and data analysis, the following conclusions were drawn:

- 1) Third party funds partially have a positive and significant effect on the development of Islamic banking financing in Indonesia. The positive effect is concluded from the amount of P Value (0.001) obtained which is smaller than 0.05 or 5%. This shows that third party funds have a significant effect on financing development. Because third party funds have a positive and significant effect, changes that occur in third party funds will be directly proportional to changes in the development of Islamic banking financing in Indonesia.
- 2) Non-performing financing partially has a negative but insignificant effect on the development of Islamic banking financing in Indonesia. The negative effect is concluded from the amount of P Value (0.151) which is greater than 0.05 or 5%. This shows that non-performing financing has no significant effect on financing development. It shows that the changes that occur in non-performing financing are inversely proportional to the changes that occur in the development of Islamic banking financing in Indonesia. However, this is

not necessarily always the case because the effect of non-performing financing is not significant on the development of Islamic banking financing in Indonesia.

- 3) Third-party funds and non-performing financing simultaneously have a significant effect on the development of Islamic banking financing in Indonesia. Third-party funds and non-performing financing simultaneously contribute to changes in development of Islamic banking financing by 32.5%. Even so, the relationship between the variables of third-party funds and non-performing financing with financing development is quite strong at 57%. Changes that occur in the development of Islamic banking financing must always include these two variables as a consideration. Even so, there are still other variables that have contributed to changes in the development of Islamic banking financing.

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