



Development of Islamic Financial Institutions Through Islamic Banking in Indonesia

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Abstract

Understanding of Islamic banks from year to year began to increase. This can be seen from the number of banks that have implemented the concept of sharia, so that citizens of the majority Muslim community will find it easier if they deal with the savings-saving process and avoid the conventional system. This study aims to describe the development of Islamic financial institutions through Islamic banking in Indonesia. The method used is descriptive qualitative. Data in the form of words, sentences and percentages that show the development of Islamic banking. Data collection techniques use read and record. Data sources are in the form of documents that include books, journal articles, newspapers, and documents that support this research. Data analysis using interactive models. The results showed that economic development in Indonesia has been running quite well and has had a positive impact on society in general although, not all are flat in the community. However, in this case, it is still necessary to have the role of the government and various elements that are considered important enough to supervise and control the course of the economy in Indonesia. Then the development of Islamic Financial Institutions in Indonesia is quite promising, for example, many banks that used to only apply conventional concepts have now opened branches by applying the sharia concept and also the emergence of study programs on Islamic Economics such as Islamic Banking.

Keywords: *Development; Financial Institutions; Islamic Banking*

Introduction

The economy in Indonesia, especially the region (East Java), is currently still experiencing waves of increase and decrease in the economic system. In 2015 the economy in Indonesia experienced a decline, this can be seen in the amount of growth in the first quarter of 2015 of 5.05%. Meanwhile, in 2016, economic conditions in Indonesia experienced a significant improvement, which happened because the amount of growth in the second quarter increased by 5.34% (Oktafia, 2017).

In this case, the increasing export business of these commodities, including matters related to agriculture, trade, mining and processing of industrial products, is the main factor in increasing economic growth in Indonesia. This increase in economic growth has a positive impact on the community, with many business opportunities that can be done automatically will improve people's living conditions which

have an impact on people's welfare. This is inseparable from the role of the government with policies issued to regulate and supervise economic growth in Indonesia

The government has a major role in the Islamic economy and finance, where economic growth will affect the success of a country's development. Therefore, the government issued policies aimed at increasing economic growth development and controlling the inflation rate in Indonesia. In the Islamic financial institutions sector, the development in Indonesia from year to year is quite good. Although previously there were obstacles from Islamic banks themselves which experienced a decrease compared to conventional banks. As data from BNI Syariah Business Director Kukuh Raharjo, the penetration of Islamic banks in 2017 is estimated to reach 5.86% so that it is still very far compared to conventional banks which have reached 36% in the same year. The data shows that out of 262 million people in Indonesia, only 15 million people access Islamic banking services and products (Linangkung, 2017).

However, over time, the understanding of Islamic banks from year to year began to increase. This can be seen from the number of banks that have implemented the concept of sharia, so that citizens of the majority Muslim community will find it easier if they deal with the savings-saving process and avoid the conventional system. The government is also trying to apply the concept of Islamic finance at the learning level, such as the existence of Islamic banking study programs and Islamic economics at the tertiary level. Therefore, it is hoped that the Indonesian people can be more familiar with the concept of sharia and its implementation procedures, so that it can avoid the name usury.

The government plans to advance Islamic banking in Indonesia and even wants to make Indonesia the center of Islamic finance and business in the world. The phenomenon that occurs when viewed from the market share of assets, financing and third party funds (DPK) of Islamic banks continues to increase so that there are expectations and expectations that Islamic banks can become actors or main players in supporting and assisting the government in developing the economy so that it has an impact on improving public welfare. The following are indicators of the growth of market share of Islamic banks in Indonesia (Permata & Iqbal, 2019).

Islamic banks in Indonesia are among the new entrants in the bank financial institution industry, therefore an acceleration is needed in their development. According to (Nugroho, 2020) Government intervention to increase the contribution of Islamic banks through increasing the market share of the Islamic banking industry. The intervention can be through corporate action, namely the conversion of state-owned conventional banks and the merger of all Islamic banks. In addition, the Islamic banking industry in Indonesia is supported by the grassroots of the community, because the existence of Islamic banks in Indonesia is due to the motivation of the Indonesian people for the need for financial and business transactions based on sharia principles. Efforts to accelerate the growth of Islamic banks must be accompanied by the principle of prudence (prudentiality) in carrying out their operations so that the Islamic banking industry becomes a fast-growing industry with good quality (Nugroho, 2020).

Bank comes from the Italian word *banco* which means bench, the meaning of bench is interpreted and used by *bangkir* to serve its operational activities to customers. The term bench officially and popularly turned into a bank at the beginning of banking development in Indonesia. Banking is defined as a business entity that collects funds from the public in the form of deposits and distributes them to the public in order to improve the living standards of many people (Fitria, 2015).

According to The Law of the Republic of Indonesia No.10 of 1998 concerning banking, what is meant by a bank is "A business entity that collects funds from the public in the form of credit or other forms in order to improve the level of hiduf of the people". Conventional banks are banks that have been established earlier than Sharia Banks in Indonesia and have facilities that have spread widely in Indonesia. Banks are one of the financial institutions that have an important role in the economy of a country as financial intermediary institutions. Meanwhile, Islamic banks are banks that follow the Islamic economic system. As for the Islamic economy according to (Farida, 2011). Conventional Banks and

Islamic Banks have several similarities, especially in the technical side, money receipts, transfer mechanisms, computer technology used, general conditions for obtaining KTP financing, NPWP, proposals, financial statements and so on. The fundamental difference between the two is that it includes legal aspects, organizational structure, financed business and work environment.

This profit-sharing pattern allows customers to directly monitor the performance of Islamic Banks by monitoring the amount of profit sharing obtained. If the amount of bank profit is greater, the greater the profit share received by the customer, and vice versa. The small or shrinking profit sharing amount for a long time is the benchmark that bank management is declining. It was a transparent and easy early warning for customers. Unlike conventional banking, customers cannot judge performance based solely on the interest earned. Differences in purpose from conventional banks with Islamic banks: Conventional banks are established to obtain the greatest material profit, while Islamic banks are established to provide material and spiritual welfare. The material and spiritual welfare is obtained through halal fundraising and distribution efforts. This means that Islamic banks will not channel funds to liquor factories or other businesses that cannot be guaranteed that the results come from halal activities. Therefore, it can be said that the concept of profit in conventional banks is more likely to focus on the angle of material profit while the concept of profit in Islamic banks should pay attention to profits from a worldly and ukhrawi (afterlife) angle. If indeed the customer's goal is in accordance with the objectives of the Islamic Bank, then in principle there is no shortage of savings in Islamic banks because of the balance between the mundane and ukhrawi. However, if the customer's goal is more about the material aspect, it may be that the profits obtained will not match expectations.

Next Agustiningrum (2013) added that the quality of financing distribution to Islamic banks will ensure the sustainability of Islamic banks (sustainability) in carrying out their business activities, because there is certainty of return of principal installments so that Islamic banks can distribute the profit sharing to all customers with a good rate of return. Thus, if Islamic banks are able to provide a rate of return in accordance with customer expectations, the trust of deposit owners in Islamic banks will increase. Public trust in the bank's performance is very important, because the bank's function as a financial intermediary institution that collects and distributes the funds back to the community.

Islamic banks have an exclusive mission and methodology, a mission that is not only in the nominal amount of investment but also includes the type, object and purpose itself. The methodology is the framework of sharia and its rules derived from the ethics and values of the universal Islamic sharia. Based on this, Islamic banks function as a means to collect public savings and develop them. The point is that Islamic Banks are institutions that function to invest public funds in accordance with Islamic recommendations effectively, productively and for the benefit of Muslims. The main objective of the Islamic Bank, which is to unite Muslims, restore the strength, role, and position of Islam on earth to be achieved.

According to Antonio (2008) explained several things including the advantages of Islamic banks, especially in the strong religious emotional ties between shareholders, bank managers, and customers. From this emotional bond, togetherness can be developed in facing business risks and dividing profits honestly and fairly. Then with religious attachment, all parties involved in the Islamic Bank are trying their best with the experience of their religious teachings so that whatever results are obtained are believed to bring blessings. The existence of financing facilities (Al-Mudharabah and Al-Musyarakah) that do not burden customers from the beginning with the obligation to pay fees on a fixed basis. This is to provide the psychological leeway that the client needs to be able to try calmly and earnestly. Furthermore, with the existence of a profit sharing system for storing funds after an early warning is available about the state of the bank which can be known at any time from the ups and downs of the amount of profit sharing received. The implementation of the profit-sharing system and the abandonment of the interest system have made the Islamic Bank more independent from the influence of monetary turmoil both from within and from abroad.

Eposito (in Farida, 2011) explains that overall, Islamic economics is more successful in explaining what is not Islamic economics, rather than determining what makes Islamic economics more likely to expose the weaknesses of other systems than showing (that the Islamic economy is substantially better. Other opinions according to Adiwarmanto (in Sulistiyawan, 2015), stated that there are six weaknesses of Islamic Banks that cause the least number of people to become customers of Islamic Banks. The weaknesses include the promotion of Islamic banks is not comprehensive to various communities, offices that are owned a little, ignorance of the public, automated teller machine (ATM) facilities are small in number, products are unknown to the public are not known to the public, and lack of facilities. In addition, the weaknesses of Islamic banks are as follows: The network of Islamic Bank offices is not yet wide, the human resources of Islamic Banks are still small, public understanding of Islamic Banks is still lacking, project assessment errors result in greater results than conventional banks.

Banking in Indonesia is now increasingly enlivened by the existence of Islamic banks that offer financial and investment products in a different way than the long-standing Conventional Bank. Although still considered a newcomer, Islamic Banking is growing quite rapidly. This is understandable with Indonesia's status as the largest Muslim country in the world so that banks that use Islamic laws and principles will be more in demand. As if they don't want to lose momentum, currently conventional banks in Indonesia have co-founded sharia institutions or sharia business units themselves. This is done to attract more customers who are interested in the advantages of Islamic banks. Based on the background above, it can be concluded that this study aims to describe the development of syariah financial institutions through syariah banking in Indonesia.

Research Method

This research is a qualitative descriptive research. Qualitative is research that can be described in the form of words, and language in a natural context and by utilizing natural methods (Moleong, 2013). The purpose of this study is to interpret and convey data related to the situation that is happening, attitudes / views that occur in society, the conflict of two or more states, the influence on a condition etc. Data collection techniques in the form of read and listen. Data sources are in the form of documents or literature studies in the form of books, magazines, newspapers, and literature, scientific articles, encyclopedias, scientific essays, scientific papers and other sources either in the form of writing or in digital format that is relevant and related to the object being studied. The object of this research study is in the form of texts or writings that describe and explain the history and development of Islamic banks in Indonesia. Data analysis techniques using interactive models (Miles et al., 2014) which includes data collection, data analysis and conclusions of analysis results.

Results and Discussion

In Indonesia, the development of Islamic banking industry is driven by the community (society driven / market driven) marked by the establishment of Bank Muamalat Indonesia (BMI) in 1992 on the idea of the Indonesian Ulema Council (MUI) and the Indonesian Muslim Scholars Association (ICMI). However, at that time BMI had not given color to the growth of Islamic banking in Indonesia because of its relatively small assets. The Islamic banking industry in Indonesia only developed after 1999 after the issuance of Law No. 10 of 1998 concerning banking, so that in Indonesia there are two forms of Islamic banking, namely Sharia Commercial Banks (BUS) and Sharia Business Units (UUS) (Nugroho, 2020).

The existence or extension of Bank Mandiri Syariah (BSM) began in 1999, actually became a wisdom, and at the same time a blessing after the financial and monetary crisis in the 1997-1998 period. As is known, the financial and monetary crisis that has occurred since July 1997, and then there has been a multi-dimensional crisis including in the aspect of national politics, has resulted in a significant negative

impact on all aspects of people's lives, including the business sector or the business world. In the conditions of the multi-dimensional crisis, the national banking industry, which is dominated or the majority, is conventional banks that have also experienced extraordinary crises and even some have experienced bankruptcy. There is an effort by the government to take action by restructuring and recapitalizing some banks in Indonesia.

Based on Islamic banking statistics published by Bank Indonesia, in 1998 there was one sharia commercial bank and there were 76 sharia people's credit banks. According to Hadad (in Yanita (2015:1)) "As of March 2015, the Islamic banking industry consists of 12 Sharia Commercial Banks, 22 Sharia business units owned by conventional commercial banks, and 163 Sharia People's Credit Banks (BPRS) with total assets of 264.81 trillion with a market share market value of 4.88%. Meanwhile, there are 98 sharia non-bank financial industry (IKNB) players outside the MFI, consisting of takaful services or sharia insurance businesses that manage assets worth 23.80 trillion, sharia financing businesses that manage assets worth 19, 63 trillion, and other Islamic financial institutions with assets worth 12.86 trillion. However, despite these achievements, Islamic Banks are still unable to achieve the market share target that was once targeted to be achieved in 2008, which is as much as 5%.

The informal development of Islamic financial institutions began before the issuance of a formal legal framework as the basis for banking operations in Indonesia. Several Non-Bank financing business entities have been established before 1992 that have implemented the concept of profit sharing in their operational activities. This shows the public's need for the presence of financial institutions that can provide financial services in accordance with sharia.

The needs of the community have been answered by the realization of a sharia-compliant banking system. The government has included that possibility in the new law. Law No.7 of 1992 concerning banking has implicitly opened up opportunities for banking business activities that have an operational basis for profit sharing which is detailed in Government Regulation No. 72 of 1992 concerning Banks Based on the Principle of Profit Sharing. This provision has been used as the legal basis for the operation of Sharia Banks in Indonesia. From 1992 to 1998, there was only one Sharia Commercial Bank and 78 Sharia People's Credit Banks (BPRS) that had operated. In 1998, Law No. 10 of 1998 concerning amendments to Law No. 7 of 1992 on banking emerged. The changes in the law have led to several changes that provide greater opportunities for the development of Islamic banks.

The law has regulated in detail the legal basis and types of businesses that can be operated and implemented by Sharia Banks. The law also provides direction for conventional banks to open sharia branches or even convert themselves completely into Islamic banks. Over time, at the end of 1999 along with the issuance of the banking law, commercial Islamic banks and commercial banks emerged that opened sharia business units. Since the operation of Bank Muamalat Indonesia (BMI), as the first Sharia Bank in 1992, Bank Indonesia data as of May 30, 2007 shows that currently the national Islamic banking has grown rapidly, when the actors consist of 3 Sharia Commercial Banks (BUS) including: Bank Muamalat, Bank Syariah Mandiri, 23 Sharia Business Units (UUS), and 106 Sharia People's Credit Banks (BPRS), while the assets managed by national Islamic banks as of May 2007 have amounted to 29 trillion. The development of Islamic commercial banks and conventional banks that open Islamic branches is also supported by the persistence of Islamic banks at a time when the national banking experienced a severe crisis in 1998.

The Islamic banking profit sharing system implemented in Bank Muamalat's products makes the bank relatively better able to maintain its performance and does not rely on soaring deposit rates so that its operating expenses are lower than conventional banks. As one of the financial institutions, banks need to maintain their performance in order to operate properly. Moreover, Islamic banks have to compete with conventional banks that are dominant and have grown rapidly in Indonesia. This increasingly sharp competition must be followed by good management to survive in the banking industry. One of the things

that banks must pay attention to in order to continue to live is the performance of the bank's financial condition and market share in competing with conventional banks that have been established earlier.

The pioneer of the establishment of Islamic banking in Indonesia was Bank Muamalat in 1991. This bank was born by the Indonesian Ulema Council, the Indonesian Muslim Scholars Association (ICMI), Muslim entrepreneurs and also the government. Unfortunately, the bank was less popular and its performance was stagnant, only after the economic crisis and reforms did Bank Muamalat begin to attract customers. The development of Islamic banking in Indonesia has become a benchmark for the successful existence of the Islamic economy.

Bank muamalat as the first Islamic bank and a pioneer for other Islamic banks has implemented this system in the midst of the proliferation of conventional banks. The monetary crisis that occurred in 1998 has sunk conventional banks and many have been liquidated due to the failure of their interest system. Meanwhile, banks that implement the Islamic system can continue to exist and be able to survive. Not only that, in the midst of the global financial crisis that hit the world at the end of 2008, Islamic financial institutions again proved their resilience from the impact of the crisis. Islamic financial institutions remain stable and provide benefits, comfort and security for their shareholders, securities holders, borrowers and fund-raisers in various Islamic banks.

This can be proven from the success of Bank Muamalat through the crisis that occurred in 1998 by showing increasing performance and not receiving a penny of assistance from the government and in the financial crisis in 2008, Bank Muamalat was even able to earn a profit of more than Rp. 300 billion. Islamic banking can actually use this momentum to show that Islamic banking is truly crisis-resistant and resilient and capable of significant growth. Therefore it is necessary to take strategic steps to realize it.

The strategic step in the development of Islamic banking that has been pursued is the granting of permits to conventional commercial banks to open branches of Sharia Business Units (UUS) or the conversion of a conventional bank into a Sharia bank. This strategic step is a response and initiative of the amendment of the Banking Law No. 10 1998. The law in lieu of Law No. 7 of 1992 clearly regulates the legal basis and types of businesses that can be operated and implemented by Islamic banks.

Islamic Financial Institutions in Indonesia

Initially, there was a decline in economic conditions in Indonesia. This has a bad impact on all circles, such as the increase in poverty and also the large number of unemployed due to many companies closing due to bankruptcy. Many factors led to the decline of the economy, one of which was the monetary crisis that occurred in 1997. With this economic downturn, several parties such as the government, Bank Indonesia, DPR and other businesses have made it aware of using the sharia system as an alternative way or solution. For example, the government implements a trading business system for small people, because it is hoped that entrepreneurship will be able to open up jobs for others. So in this case, it is necessary to have an alternative capital solution for micro, small, medium or upper-level business actors with the path of submitting capital to banks or Islamic Microfinance Institutions (MFIs) can also be used as a solution in terms of citizen capital (Oktafia, 2017).

In the beginning, an Islamic Financial Institution is currently spread in various regions in Indonesia. This Islamic financial institution is very committed to the teachings of the Islamic religion. In this case, a Sharia-based Financial Institution has more benefits than its mudharat. With the establishment of an Islamic Financial Institution, it aims to increase awareness in ourselves to apply the teachings of Islam as a whole without any deviation. Therefore, on the part of citizens, the public is more required to choose Islamic Financial Institutions instead of Conventional Financial Institutions in the process of saving money.

The presence of Islamic Financial Institutions in Indonesia is marked by the establishment of Bank Muamalat. In this Islamic financial institution system, there are murabahah financing, amanah deposits, wadiah savings or deposits (entrustments) as well as mudharabah and musyarakah financing. In addition, there is also sharia insurance. The development of Sharia Financial Institutions in Indonesia is very rapidly developing as is the case of a Sharia Banking Institution in Indonesia.

In the real system, Islamic Financial Institutions are superior to conventional. Because Islamic Financial Institutions in terms of depositing funds will be stored collectively and used for halal and thayib sectors and the system in an Islamic financial institution usually uses a profit-sharing system without usury' (Hidayanto, 2003). Meanwhile, a Conventional Financial Institution still has usury', where in the teachings of the Islamic religion it has been explained that it is

Usury' is illegitimate if it is done and we must abandon it. In addition, there is also a Sharia Micro Institution. Where a Sharia Microfinance Institution is very helpful in solving the problems of people's lives in the poverty level category through economic empowerment. This institution is developed in the territory of Indonesia to strengthen the economy of the Indonesian people through microfinance. And can help the government in realizing equal welfare for all Indonesians (Oktafia, 2017).

Conclusion

The description above can be concluded, that economic development in Indonesia has been running quite well and has caused a positive impact on society in general although, not all are flat in the community. However, in this case, it is still necessary to have the role of the government and various elements that are considered important enough to supervise and control the course of the economy in Indonesia. Then the development of Islamic Financial Institutions in Indonesia is quite promising, for example, many banks that used to only apply conventional concepts have now opened branches by applying the sharia concept and also the emergence of study programs on Islamic Economics such as Islamic Banking. Therefore, it is expected that the development of the Islamic economy and financial institutions in Indonesia can increase every line. The phenomenon and achievement of the performance of the Islamic banking industry today is inseparable from the history of the Islamic bank being established. Because the history of Islamic banks is important to know the struggle and continue the ideals for the welfare of the community through the use of islamic bank services and products can continue to be improved. The establishment of Islamic banks in Indonesia is based on the noble desire of the community (Society Driven) for the need to practice religious teachings in totality (kaffah). In addition, the establishment of Islamic banks in Indonesia has a different history between Islamic banks, one with differences from one another, but has the same ideals, namely providing benefits for the community.

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