

# THE EFFECT OF FINANCING OR CREDIT RISK, LIQUIDITY AND CAPITAL ADEQUACY ON THE PROFITABILITY OF ISLAMIC BANKS IN 2016-2021

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## ABSTRACT

In Indonesia, there are two types of banking operations: conventional and sharia. The existence of these two types of banks has a positive impact, namely the emergence of motivation to improve their performance better than other banks. The purpose of this research was to find out how the influence of financing or credit risk, liquidity risk, and capital adequacy risk have affected the profitability of Islamic banking in Indonesia in 2017–2021, both partially and simultaneously. This research uses a type of quantitative-descriptive research. The conclusion that can be drawn from this study is that the variables of financing or credit risk, liquidity risk, and capital adequacy risk significantly influence profitability. In the t (partial) test, the financing or credit risk variable has a significant effect on the profitability of Islamic banking in 2016–2021. The t (partial) test of the liquidity risk variable has no effect on the profitability of Islamic banking in 2016–2021. And the partial t test for capital adequacy risk has a significant effect on the profitability of Islamic banking in 2016–2021.

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## 1. INTRODUCTION

In Indonesia, there are two types of banking operations, namely conventional and sharia. The existence of these two types of banks has a positive impact, namely the emergence of motivation to improve their performance better than other banks (Maharudin et al, 2018). Banks are financial institutions that mediate between parties who have capital and those who need capital, besides that banks also provide other financial services (Sante et al, 2021). The main goal of the bank as a business activity is to maximize profitability or profit (Qurotulaeni, 2022). Profitability is the ability possessed by Islamic banks to benefit from the activities carried out (Qurotulaeni et al, 2022). Where profitability can find out how Islamic banks achieve the goals of the activities that have been carried out (Quratulaeni et al, 2021). To determine the level of profitability of Islamic banks can use the ratio of ROA or return on assets.

Effective ROA or return on assets can reflect good bank performance. And conversely, if ROA is bad, it will have an impact on Islamic bank profits due to decreased performance (Sante et al, 2021). The decline in the financial performance of Islamic banks was caused by one of the failures of customers to fulfill their obligations to banks, causing Islamic banks to experience increased credit risk or financing risk (Sante et al, 2021). On the other hand, if an Islamic bank fails to pay by a customer, it will cause the bank to experience an increase in liquidity risk. Islamic bank liquidity risk has an impact on Islamic banks experiencing difficulties in fulfilling their obligations at maturity and will disrupt cash and financial flows (Santa et al, 2021).

Capital adequacy is a regulation that exists in banking to establish a framework for how banks and depository institutions must handle their capital (Kartika, 2014). Capital adequacy describes a bank's ability to maintain capital that can cover the risk of losses that may occur from investing in risky productive assets, as well as for financing in fixed assets and investments (Setiawati et al, 2017).

According to Sante et. al (2021), it is known that partially the ratio of NPL for credit risk and LDR for liquidity has no effect on profitability. And simultaneously credit risk, liquidity risk, and operational risk have a significant effect on profitability. According to Qurotulaeni et. al. (2022), data profitability is affected by liquidity risk, while capital adequacy risk has an influence on profitability. According to Madarudin et al. (2018), financing or credit risk has a negative and significant impact on the efficiency

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performance of Islamic banks. Operational risk has a significant negative effect on efficiency, and liquidity risk has a positive and significant impact on the efficiency of Islamic banking.

From the results of different studies that have been done previously, it makes researchers interested in re-examining these variables on the profitability of Islamic banks. So that it can be concluded whether the financing or credit risk variables, liquidity, and capital adequacy will affect the profitability of Islamic banks.

## 2. METHOD

This research uses a type of quantitative-descriptive research. According to Sugiyono (2017), a method based on positivism is used to examine research samples with the intention of finding the truth of the hypotheses that have been made. The type of data used in this research is banking financial reports issued by the Financial Services Authority for 2016-2021. The technique used for data collection is sourced from secondary data such as official websites, news, previous research, financial reports, and so on. The sampling technique in this study was purposive sampling. The criteria used to select the sample are as follows: 1. Banking companies are included in Islamic banking. 2. Published financial report data at the Financial Services Authority. 3. Published financial reports from 2016-2021.

## 3. RESULT AND DISCUSSION

### Descriptive Analysis

The data used in this study is Islamic banking statistical data released by the Financial Services Authority from January 2016 to December 2021 or for approximately 72 months. The data is taken from sharia banking statistics, namely ROA as the ratio used to see the profitability of Islamic banks, NPF ratio to see the level of financing risk or credit risk, FDR for liquidity risk, and CAR as capital adequacy risk.

**Table 1.** Descriptive Test

	ROA	NPF	FDR	CAR
Mean	1.291.667	4.016.667	8.017.292	6.406.181
Median	1.350.000	3.535.000	7.956.500	2.036.500
Maximum	2.150.000	6.170.000	8.932.000	1.646.000
Minimum	0.16	2.590.000	7.012.000	1.472.000
Std. Dev.	0.453885	0.871638	4.139.680	2.649.837
Skewness	-0.32208	0.550496	0.462368	5.748.269
Kurtosis	2.379.212	2.079.793	2.957.047	3.405.695
Jarque-Bera	2.400.927	6.176.893	2.570.949	3.290.114
Probability	0.301055	0.045573	0.276519	0
Sum	9.300.000	2.892.000	5.772.450	4.612.450
Sum Sq.				
Dev.	1.462.680	5.394.240	1.216.723	4985363
Observations	72	72	72	72

Source : data processed (2023)

Based on Table 1 above, it can be seen that the observations made were as many as 72 data samples from Islamic banking statistical reports. From the table it is known that the mean or average ROA of Islamic banking in Indonesia is 1.29%. With a median value of 1.35% and followed by the highest or maximum CAR at 2.15% and the lowest at 0.16%. Furthermore, for the NPF ratio which is used as an effort to see the risk of financing or credit carried out by Islamic banking in Indonesia, it is known that the average (mean) of the NPF ratio is 4.01%. With a mean value of 3.53% and the highest NPF ratio was 6.17% and the lowest was 2.59%. The FDR ratio owned by Islamic banking in Indonesia from 2016 to 2021 has an average value of 80.1% with a median value of 79.56%. Then the highest FDR ratio is 89.32% and the lowest is 70.12%. The CAR ratio for Islamic banking in Indonesia in 2016-2021 has an average of 64.06% with a median value of 30.36%. The lowest CAR is being assessed at 14.72%.

### Regression Test

Multiple linear regression test is a test that is carried out using independent variables or independent variables of more than one variable. Multiple linear regression test techniques were carried out by researchers to be able to determine the effect of the significance of two or more independent variables on the dependent variable (Mona and Prang, 2015).

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**Table 2.** Regression Test

Variable	Coefficient	Std. Error	T-Statistic	Prob
C	-0.594060	1.325924	-0.448035	0.6556
NPF	-0.280470	0.057630	-4.866703	0.0000
FDR	0.018446	0.012545	1.4703350	0.1462
CAR	0.078904	0.020677	3.816023	0.0003
R Squared	0.808218	Mean dependent var		1.309253
Adjusted R Square	0.799500	S.D dependent var		0.447785
F-Statistic	92.71330	Hannan-Quinn criter		-0.269470
Prob(F-Statistic)	0.00000	Durbin-Watson stat		0.524776

Source: Eviews Data Processing (2023)

It is known that the t test (partial) for financing or credit risk (NPF) variables obtained a significance value of 0.0000, with a coefficient of -0.280470. This shows that NPF has a significant negative influence on the profitability of Islamic banking in Indonesia in 2016-2021. The results of this study are in accordance with research conducted by Sante et al (2021), Aji et al (2021), Wibiyanto (2020) and Nugroho et al (2019) which examined that financing or credit risk carried out by banks has a significant negative influence on profitability. Because the higher the risk of problem financing owned by Islamic banking, the profitability of Islamic banks is not optimal. However, this study contradicts the research of Korompis et al (2020).

Based on the t (parisal) test it can be seen that FDR liquidity risk has a probability above 0.05, namely with a value of 0.1462. This result is in line with the research of Bani et al (2016) and Wahyudi (2020). Which explains that there is no influence between liquidity risk (FDR) and Islamic bank profitability (ROA). However, these results are not in line with the research of Syakhrun et al (2019), Munir (2018), and Almunawwaroh et al (2018).

The t (partial) test shows that the risk of capital adequacy (CAR) has a significant effect on the profitability of Islamic banking in Indonesia in 2016-2021. It is known from the profitability value of 0.0003. Where the results are below the significance value of 0.05. These results are in accordance with research conducted by Syakhrun (2019) and Setiawati et al (2017). This happened because the increase in profitability by Islamic banking was also followed by the increase in the need for reserves in order to anticipate the consequences of increased risk in line with optimizing asset productivity. However, these results contradict Almunawwaroh et al (2018), Munir (2018), Rahmawati (2020), and Wahyudi (2020).

By means of the f test (simultaneously) or jointly it can be seen that financing or credit risk, liquidity risk, and capital or capital adequacy risk have a significant effect on the profitability of Islamic banking in Indonesia in 2016-2021. This is known from the probability F-statistic of 0.000000. This value is below the significance value of 0.05. As seen from the R-square coefficients of the three variables studied (financing risk, liquidity, and capital adequacy) are able to explain the effect on the profitability of Islamic banking by 80.82%. while the remaining 19.17% is explained by other variables not examined in this study.

#### 4. CONCLUSION

The conclusion that can be drawn from this study is that the variables of financing or credit risk, liquidity risk, and capital adequacy risk significantly affect profitability and are able to explain the profitability of Islamic banking in 2016-2021 of 80.82%. In the t (partial) test, the financing or credit risk variable has a significant effect on the profitability of Islamic banking in 2016-2021. The t (partial) test of the liquidity risk variable has no effect on the profitability of Islamic banking in 2016-2021. And the (partial) t test for capital adequacy risk has a significant effect on the profitability of Islamic banking in 2016-2021.

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