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ANALYSIS OF FACTORS AFFECTING PROFIT DISTRIBUTION MANAGEMENT AT ISLAMIC BANKS IN ASIA

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Abstract: This study aims to analyze factors that affect Profit Distribution Management (PDM) at Islamic Banks in Asia. Data used are secondary data with the observation period of 152 financial statements of Islamic banks in Asia in 2010-2013. The method is quantitative with panel data with regression test. The results of the study showed that capital adequacy, Third Party Fund Effectiveness (EDPK), and Third Party Fund Proportion (PDPK) have a significant negative effect to PDM. Inflation and growth of Gross Domestic Product (GDP) have significant positive effect to PDM. While, age variable has no significant effect on PDM.

Keywords: Profit, Distribution, Management, bank, Sharia,

1. Introduction

The rapid development of Islamic banking in the 21st century was caused by the strong resilience of Islamic banks over the impact of global financial crisis (Rosman, Wahab, and Zainol, 2013). This resulted in an increase of public interest in Islamic products offered by Islamic banks, thus creating Islamic banks developed rapidly. One of the famous Islamic products collected by Islamic banks from the public is the deposit or in Islamic banks called with third party fund.

Some studies concerned with the motivation of customer in choosing Islamic banks as a deposit of funds has not been based on Islamic values, but to seek maximum profit (Rachmawati and Eki, 2004; Karim and Afif, 2006; Kasri and Salina, 2009; Andriyanti, 2010). All the studies
were measured by observing the activity of Islamic bank customers who usually transferring fund of saving. Deposit fund was transferred from Islamic banks to conventional banks due to get bigger income of interest rates. In fact, Islam has banned the use of interest as applied by conventional banks with the term *riba*. Ibn Al-A’rabi in Nurhayati and Wasilah (2013) stated that the basic principles of Islamic economics are prohibiting the interest, unfair treatments, uncertainty, and considering issues based on the benefits of mankind.

Ismal (2011) found the possible determination of interest rate on savings and loans by conventional banks to saving amount of customer savings in Islamic banks. Chong and Liu (2009) stated that Islamic banks are not interest-free but still interest-based as strong relationship between profit-sharing of Islamic banks and the conventional bank interest rates. By the strong effect of interest rate, Islamic banks need to manage the distribution of profit-sharing by considering factors that can affect the distribution of profit-sharing. The management performed by Islamic banks against the profit-sharing given to its customers is called Profit Distribution Management (PDM) (Farook, Hassan, and Clinch, 2012).

PDM actually is not a new issue and study, it has been conducted many times. Sundararajan (2005) in Farook, Hassan, and Clinch (2012) found that Islamic banks have PDM which refers to interest rate and implicitly affected by fee management. Interest rate had a significant relationship to PDM. Furthermore, Farook, Hassan, and Clinch (2012) conducted research on the effect of PDM relationship using asset spread with determinant factors derived from internal and external Islamic banks. The result found that Brunei, Malaysia, and the United Arab Emirates perform a low PDM, while Bahrain, Indonesia, Pakistan and Saudi Arabia perform a high PDM. Mulyo (2012) and Rizaludin (2013) conducted a study on PDM based on internal and external factors of Islamic banks in Indonesia. The result showed that Islamic banks in Indonesia perform high PDM (Farook, Hassan, and Clinch, 2012).

2. Theory

In general, a company is an entity that not only operates for its own purpose, but must also provide benefits to stakeholders. Freeman (1984) defined stakeholder as “any group or individual who can affect or is affected by the achievement of the firm’s objectives”. It means that stakeholder is a group or individual able to influence or be influenced by the achievement of corporate goals. In Islamic banking activities, Islamic banks need to maintain a good
relationship with stakeholder, especially customers willing to deposit their funds in Islamic banks. The other perspective is by offering an interesting profit-sharing for customers.

Farook, Hassan, and Clinch (2012) stated that Profit Distribution Management (PDM) is an activity of managers in allocating the distribution of profit-sharing of Islamic banks to their customers. Bank Indonesia defines profit-sharing distribution is the profit-sharing of Islamic banks to deposit customers based on the agreed ratio every month. It is concluded briefly that PDM is an activity conducted by managers in allocating the distribution of profit-sharing of Islamic banks to their customers every period/month agreed.

The capital adequacy describes bank’s ability to maintain sufficient capital to cover possible losses which may occur from risky earning assets fund, as well as for financing in fixed assets and investment (Idroes, 2008). Capital Adequacy Ratio (CAR) is the ratio used to measure capital adequacy. The greater this ratio means the healthier of the bank to perform their performance.

High CAR creates banks able to reduce possible risks that cause bank managers to perform Profit Distribution Management (PDM) wider from the asset return because the bank is in a safe condition. The argument is in line with Mulyo’s (2012) findings that there is a positive relationship between capital adequacy and the level of profit-sharing of Islamic banks. Thus, the proposed hypothesis is:

$$H_1: \text{Capital adequacy has positive effect to the Profit Distribution Management (PDM)}$$

High inflation rate cause costs to increase and less profitable productive activities. To maintain customers from withdrawing their funds to other investment schemes (Sukirno, 1998), Islamic banks would tend to raise the profit-sharing rate. This is similar to the study by Kartika (2013). The hypothesis is then:

$$H_2: \text{Inflation has negative influence to the Profit Distribution Management (PDM)}$$

A good economic condition may indicate healthy domestic production activities and is reflected by the growth of Gross Domestic Product (GDP). In such condition, population as the owner of production factor in aggregate earns higher income (Nasution, 2009). This greater income has a good impact on the financial health of the bank. On the other hand, in opposite the poor condition of a country’s economy such as recession, there is an increase in unemployment and decrease in an economic growth.
At recession, GDP growth does not exist, but the decrease in GDP exists. In a recession, there is the possibility that individual and business would be difficult to pay their obligation to the bank. As a result, asset funded by depositors may have poor performance. Thus, the financing provided by Islamic banks becomes bad debt and reduces revenue received by Islamic banks. To maintain good relationships to customers or to minimize withdrawing deposits, however, Islamic banks distribute profit-sharing revenue higher that asset return. Therefore, to prove the relationship, the proposed hypothesis is:

H₃: Gross Domestic Growth (PDB) has negative influence to the Profit Distribution Management (PDM)

The Third Party Fund Effectiveness (EDPK) reflects the bank’s intermediary function, for example how effective the Islamic banks in distributing third party funds in financing. The higher this ratio is (according to Bank Indonesia 85% - 100%), the better of the health of the bank due to bank financing distribution smoothing, so the bank’s revenue is increasing. High FDR indicates a high level of financing and this has an impact on the increased returns generated from financing. It can automatically raise revenue that can be shared to customers. However, large third party funds absorbed through financing will cause liquidity risk faced by Islamic banks due to the lack of available funds. Bank would find difficulty in distributing profit-sharing t customers. The argument is in line wit the results of Mulyo (2012) and Rizaludin (2013) who found a negative relationship between FDR with the level of profit-sharing. Thus, the proposed hypothesis is:

H₄: Third Party Fund Effectiveness (EDPK) has negative effect to the Profit Distribution Management (PDM)

The ability of banks in collecting public fund would affect the growth of banks. The amount collected would increase the efficient factor of the bank. Third party fund is fund entrusted by the society under a depositary agreement. Fund is the most important item for the bank as a financial institution, because the fund collected from the community is the operational motor of a bank. If the fund is not sufficient, the bank cannot perform its functions with the maximum efforts or even does not work at all. The Third Party Fund Proportion (PDPK) is a proxy representing how much the bank is dependent on the third party fund. Farook, Hassan and Clinch (2012) and Mulyo (2012) found a negative effect of PDPK to PDM. This is because
Islamic banks with high PDPK values tend to manage PDM based on their asset returns. This is due to strict supervision from customers, thus discouraging Islamic banks to manage the distribution of profit-sharing. Therefore, the hypothesis proposed in this study is:

H₅: Third Party Fund Proportion (PDPK) has negative effect to the Profit Distribution Management (PDM)

Experience in running the business for banks would affect the existence of banks in facing the competition. Nurhidayanti and Indriantoro (1998) showed that the age of the company can show the information to potential investors to invest. According to Farook, Hassan, and Clinch (2012), in the context of banks, a new bank is similar to a new company. New bank has a lack of information about the condition of the bank itself and its business environment. In addition, new bank must be able to develop trust with stakeholders. They found a negative effect between the age of Islamic banks and the PDM as it is difficult for a new company to start their business to generate profit in the early years of its operations. For Islamic banks, this may not be a good issue due to profit-sharing system. The difficulty in generating income caused the distribution of profit-sharing smaller. On the other hand, to maintain good relationships with customers, Islamic banks must be able to distribute competitive profit-sharing with conventional banks. This is conducted in order to keep depositors do not withdraw their funds and move to other banks which give better returns (displacement funds). Thus the proposed hypothesis is:

H₆: The age of bank has negative effect the Profit Distribution Management (PDM)

3. Method

The sample uses purposive sampling method from existing Islamic bank population in 2010-2013 in bankscope database. They are 38 Islamic banks in 10 countries with 152 reports of Islamic banks in the period of 2010-2013.

This study refers model used by Farook, Hassan, and Clinch (2012) then modifying the independent variables used. The model formulated in this study is:

\[ PDM = \alpha_0 + \alpha_1 KM_{it} + \alpha_2 INF_{it} + \alpha_3 PDB_{it} + \alpha_4 EDPK_{it} + \alpha_5 PDPK_{it} + \alpha_6 UMUR_{it} + \alpha_7 LN_ASET_{it} + \varepsilon \] .................................(1)

\[ PDM = \text{Profit Distribution Management using asset spread} \]
KM = Capital adequacy using Capital Adequacy ratio (CAR)
INF = Inflation using changes in Annual Consumer Price Index (CPI).
PDB = Gross domestic product growth using changes in annual gross domestic product
EDPK = The third party fund effectiveness using the Financing to Deposit Ratio (FDR)
PDPK = The third party fund proportion of using the ratio of the amount of third party funds divided by total assets
UMUR = Age of Islamic banks using dummy variable, score 1 for Islamic bank that has been established 4 years or more, score 0 for Islamic bank that has been established less than 4 years
LN_ASET = The Natural Logarithm of the total assets of Islamic banks from the value of the US dollar currency in thousands

Calculating PDM uses Asset Spread. Asset Spread can be formulated as follows (Farook, Hassan, and Clinch, 2012):

\[
Asset\ spread = (|ROA - ROIAH|) .................................................. \text{(2)}
\]

Asset spread is the absolute value of Return on Asset (ROA) minus Return on Investment Account Holder (ROIAH). It means if ROA is smaller than ROIAH, it is said that Islamic banks provide profit-sharing rate to its customers greater than the asset return generated by the bank and vice versa. This indicates the existence of other factors that cause Islamic banks to do so.

4. Analysis

Descriptive statistics can provide a brief overview of Islamic banks. The PDM variable has a minimum of 0.08 for Shahjalal Islami Bank Ltd in 2013. While the maximum of 5.11 is PT Bank BNI Syariah in 2011. The average PDM is 2.07 with a standard deviation of 0.99. It indicates the data in the research sample averagely have PDM which is far from asset return with normal distribution of data.

Table 1. Descriptive Statistic

<table>
<thead>
<tr>
<th>Variable</th>
<th>N</th>
<th>Min</th>
<th>Max</th>
<th>Average</th>
<th>Std. Dev</th>
</tr>
</thead>
<tbody>
<tr>
<td>PDM</td>
<td>152</td>
<td>0.08</td>
<td>5.11</td>
<td>2.07</td>
<td>0.99</td>
</tr>
<tr>
<td>KM</td>
<td>152</td>
<td>10.36</td>
<td>48.22</td>
<td>20.23</td>
<td>7.39</td>
</tr>
</tbody>
</table>
The following Table 2 is a descriptive statistical description outlined per country. The per-country analysis displayed uses the mean variable which is in detail the characteristics of each country of the variables used in this study.

<table>
<thead>
<tr>
<th>Negara</th>
<th>N</th>
<th>PDM</th>
<th>KM</th>
<th>INF</th>
<th>PDB</th>
<th>EDPK</th>
<th>PDPK</th>
<th>AGE</th>
<th>ASET</th>
</tr>
</thead>
<tbody>
<tr>
<td>UEA</td>
<td>16</td>
<td>0,97</td>
<td>20,84</td>
<td>0,88</td>
<td>4,09</td>
<td>85,4</td>
<td>78,13</td>
<td>0,88</td>
<td>15.893.542</td>
</tr>
<tr>
<td>Bangladesh</td>
<td>8</td>
<td>1,43</td>
<td>12,64</td>
<td>7,94</td>
<td>6,26</td>
<td>83,9</td>
<td>77,44</td>
<td>1</td>
<td>1.504.917</td>
</tr>
<tr>
<td>Bahrain</td>
<td>16</td>
<td>1,3</td>
<td>23,05</td>
<td>1,91</td>
<td>3,78</td>
<td>80,8</td>
<td>72,42</td>
<td>1</td>
<td>6.472.053</td>
</tr>
<tr>
<td>Brunei</td>
<td>4</td>
<td>3,67</td>
<td>26,32</td>
<td>0,8</td>
<td>1,3</td>
<td>51,11</td>
<td>73,98</td>
<td>1</td>
<td>4.617.967</td>
</tr>
<tr>
<td>Indonesia</td>
<td>24</td>
<td>3,18</td>
<td>20,86</td>
<td>5,22</td>
<td>6,19</td>
<td>84,27</td>
<td>69,83</td>
<td>0,5</td>
<td>1.903.174</td>
</tr>
<tr>
<td>Yordania</td>
<td>8</td>
<td>2,05</td>
<td>22,67</td>
<td>4,91</td>
<td>2,59</td>
<td>83,84</td>
<td>78,62</td>
<td>0,87</td>
<td>2.913.697</td>
</tr>
<tr>
<td>Kuwait</td>
<td>12</td>
<td>2,37</td>
<td>24,27</td>
<td>3,09</td>
<td>4,44</td>
<td>83,52</td>
<td>67,89</td>
<td>1</td>
<td>4.883.652</td>
</tr>
<tr>
<td>Malaysia</td>
<td>40</td>
<td>1,72</td>
<td>16,31</td>
<td>2,16</td>
<td>5,75</td>
<td>63,51</td>
<td>77,83</td>
<td>1</td>
<td>17.138.160</td>
</tr>
<tr>
<td>Qatar</td>
<td>12</td>
<td>2,19</td>
<td>19,68</td>
<td>1,11</td>
<td>9,82</td>
<td>73,62</td>
<td>69,55</td>
<td>1</td>
<td>13.355.250</td>
</tr>
<tr>
<td>Arab Sauda</td>
<td>12</td>
<td>3,01</td>
<td>25,43</td>
<td>3,91</td>
<td>6,5</td>
<td>88,97</td>
<td>68,52</td>
<td>1</td>
<td>27.738.619</td>
</tr>
<tr>
<td>Total</td>
<td>152</td>
<td>2,07</td>
<td>20,23</td>
<td>3,02</td>
<td>5,51</td>
<td>77,13</td>
<td>73,78</td>
<td>0,9</td>
<td>11.148.705</td>
</tr>
</tbody>
</table>

Source: data

From Table 2, it can be seen that Brunei, Indonesia, and Saudi Arabia have a high level of PDM by using asset spread in its calculation because it has a PDM value above 3 (Three). While, UAE, Bahrain, Bangladesh and Malaysia have low PDM with value less than 2 (Two). These results are consistent with findings conducted by Farook, Hassan, and Clinch (2012) in which Indonesia, and Saudi Arabia perform high PDM, then Malaysia and UAE perform low PDM.
The model is based on Fixed Effect model as proposed by Chow and Hausman test. As the model has problem in heteroscedasticity and autocorrelation, so it is used Generalized Least Square (GLS) (Suwandi, 2011). The significance test of the research model in Table 3 has value of $R^2 = 0.2303$ which means that 23.03% of independent variable and control variable in this research model, namely capital adequacy, Inflation, growth of Gross Domestic Product (GDP), Third Party Fund Effectiveness (EDPK), Third Party Fund Proportion (PDPK), Age, and Assets can explain the effect to dependent variable.

The result shows that independent variables and control variables used in the study, namely Third Party Fund Effectiveness (EDPK), Third Party Fund Proportion (PDPK) can explain together and influence significantly according to the hypothesis of the dependent variable used, namely Profit Distribution Management (PDM).

The Third Party Fund Effectiveness shows that customer funds are distributed as much as possible in order to provide a high profit-sharing rate so that customers can enjoy the funds deposited in Islamic banks. This result is consistent with the study of Farook, Hassan, and Clinch (2012) and Mulyo (2012). The same result is also found in the Third Party Fund Proportion which has negative and significant results. In this case, there is prioritizing the interest of the savings account holders.

Tabel 3. Result

<table>
<thead>
<tr>
<th>Variabel</th>
<th>Prediksi</th>
<th>Koefisien</th>
<th>Z-Stat</th>
<th>Probabilitas</th>
</tr>
</thead>
<tbody>
<tr>
<td>KM</td>
<td>+</td>
<td>-0,02</td>
<td>-3,30</td>
<td>0,0005***</td>
</tr>
<tr>
<td>INF</td>
<td>-</td>
<td>0,048</td>
<td>1,77</td>
<td>0,00385**</td>
</tr>
<tr>
<td>PDB</td>
<td>-</td>
<td>0,06</td>
<td>4,17</td>
<td>0,000000***</td>
</tr>
<tr>
<td>EDPK=</td>
<td>-</td>
<td>-0,0</td>
<td>-1,63</td>
<td>0,051*</td>
</tr>
<tr>
<td>PDPK=</td>
<td>-</td>
<td>-0,01</td>
<td>-1,89</td>
<td>0,029**</td>
</tr>
<tr>
<td>UMUR</td>
<td>-</td>
<td>0,13</td>
<td>0,46</td>
<td>0,323</td>
</tr>
<tr>
<td>LN_ASET</td>
<td>+</td>
<td>-0,04</td>
<td>-0,80</td>
<td>0,2115</td>
</tr>
</tbody>
</table>

R-Squared 0,2303 No. Observation 152
F-Stat | 4,57 | Wald chi-square | 1260,19
--- | --- | --- | ---
Prob (F-stat) | 0,00002 | Prob (chi-square) | 0,0000***

***Significant α = 1%, **Significant α = 5%, *Significant α = 10%

Source: Data

5. Conclusion

This study reinforces that Islamic banks in Asia do have a role in performing Profit Distribution Management (PDM), especially in Indonesia and Saudi Arabia that have high PDM value. The factors affecting Profit Distribution Management (PDM) are Third Party Fund Effectiveness and Third Party Fund Proportion. Both factors have significant and negative effect on PDM. From the results, it can be concluded that customers of Islamic banks receive different treatment. In this case, Islamic banks seek to maintain the loyalty of Islamic bank customers.

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