

NEW MODEL OF SHARIA BANKING STRATEGY IN INDONESIA: KPPS ONLINE REPORT

This book is focused on sharia banking strategy to face ASEAN Economic Community (AEC). This topic is discussed broad and deep at the same time to give better understanding for economic and business student as well as lecturer and practitioner. A new strategy called KPPS Strategy is found by research based on this book.

Published by :



Office :
Jl. A. Yani, Sokajaya 59 Purwokerto
New Villa Bukit Sengkaling C9 No. 1 Malang
HP. 081 357 217 319 WA. 089 621 424 412
www.irdhcenter.com
email: buku.irdh@gmail.com

ISBN 978-602-0726-26-7



CAKTI INDRA GUNAWAN

NEW MODEL OF SHARIA BANKING STRATEGY
IN INDONESIA KPPS ONLINE REPORT

2018



International Research and Development
for Human Beings

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**NEW MODEL OF SHARIA BANKING
STRATEGY IN INDONESIA: KPPS
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Cakti Indra Gunawan

CV IRDH

NEW MODEL OF SHARIA BANKING STRATEGY IN INDONESIA: KPSS ONLINE REPORT

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Hak publikasi pada CV IRDH

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Cetakan Pertama Oktober 2018

Penerbit CV IRDH

Anggota IKAPI No. 159-JTE-2017

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ISBN: 978-602-0726-26-7

i-iii int + 200 hlm, 25 cm x 17.6 cm

FOREWORDS

I thank God Almighty who gave His grace and blessings so this book could finally be published. This book is projected for students, lecturer, practitioner, and others to understand better about sharia banking strategy in Indonesia to face challenges in ASEAN Economic Community. This book is based on research funded by Research and Community Development Department (*Direktorat Riset dan Pengabdian Masyarakat—DRPM*) of DIKTI 2017.

I would like to thank DRPM of DIKTI for funding the research resulted in this book. I would also like to mention Rector of Universitas Tribhuwana Tungadewi (UNITRI) and Head of LPPM UNITRI for never ending support given to us. It is Dean of Economic Faculty of UNITRI we would like to thank you for all the best of luck for us.

I wish this book would benefit many party, including economic and business student especially in comprehending sharia banking strategy. I also hope this book could fill the lack of knowledge in sharia banking topic needed in many area. If there is any correspondent needed though critics and suggestions, please, kindly contact me via email: cakti.gunawan@gmail.com.

Malang, October 1st, 2018

Author

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CHAPTER 1

INTRODUCTION

1.1 General Conditions of Banking in Indonesia

Indonesia, as one of the largest country in Asia, plays an important role in the development of the Asian economy and economic rotation (Widyastuti, 2013). With a dense population and a country that has very promising economic potential, Indonesia has become one popular country in economic competition in Asian countries. Sukarno (2016) explained that in an effort to improve the economy of a country, it is necessary to have financial institutions that can focus on managing the country's economic sector. Sukarno added that the existence of economic institutions, such as banking, was very important in the modern economic system. Jumono (2017) added that, banking as a business entity engaged in finance is in desperate need of trust from these customers to support and facilitate the activities that had been carried out. The smooth activities carried out by banks will be very supportive in achieving the welfare of stakeholders and will increase the value of the company. Indonesian banking activities in the 2011-2016 periods can be seen in the following table:

Table 1. Banking Profit and ROA Year 2011-2016

Year	Profit	ROA
2011	6,92 Trillion	0,90 %
2012	9,26 Trillion	1,37%
2013	17,75 Trillion	1,90%
2014	20,26 Trillion	2,50%
2015	29,64 Trillion	3,50%
2016	22,65 Trillion	2,20%

Source: Bank Indonesia, 2017

Based on the data above, banking profit and ROA for four consecutive years from 2011-2015 experienced an increase by 22.72 trillion, while ROA increased by 2.60 percent. In 2016 the banking sector experienced a decline in profits of 23.56 percent or 6.99 trillion, , while the decrease in ROA was 1.30 percent. This decline in profit and ROA was the first time in the last eighteen years since the 1998 crisis.

Furthermore, Athoilah (2007) explained the performance of banks in 2007, indicating that during 2007 the number of earning assets increased by Rp. 235.8 trillion (15.2%) due to an increase in credit by Rp. 12.8 trillion (25.5 %). The increase in the amount of loans disbursed also exceeded the 2007 Bank Business Plan target of 22%. This increase in credit was mainly sourced from Third Party Funds (TPF) which is 223.8 trillion (17.4%). The thing that needs to be concerned about the impact of the high increase in credit growth is the condition of banking non-performing loans (NPL) (LPP Banking Supervision Report, 2007).

The government, through several proclaimed programs, has attempted to restructure national banking so that there will be no crisis in the future. The government program includes, among others, (a) the banking recovery program which includes a *Blanket guarantee* program, namely the recapitulation program and credit restructuring; and (b) efforts to strengthen the banking resilience system which includes improving banking infrastructure, good governance and supervision and banking regulations (Medyawati, 2011).

The increase in banking competition in Indonesia actually began since the openness of Indonesian banking, which was initiated with the issuance of a policy package on June 1, 1983 (PAKJUN) with the aim of modernizing the banking. Continued with the October package (PAKTO) on October 27, 1988, which facilitated licensing for the establishment of a new bank, including the opening of a branch office. At that time, with only Rp10 billion in funds, investors could already establish a new bank (Hilman, 2014), and this led to a significant increase in the number of banks.

Widyastuti (2013) explained that, an increase in the number of banks has the potential to encourage banking sector businesses to become more competitive and improve banking efficiency and health. But for Indonesian banks, most banks were in the private sector before the crisis was owned by large entrepreneurs. As a result, when the business requires large funding, they tend to mobilize public funds through their banks for their business interests. This means that the aim of the Pakto 88 issuance, which was originally intended to channel public funds to the community, shifted to channeling to the group so that potential violations of the Legal Lending Limit (BMPK) emerged (Kristianti and Yovin, 2016). This condition weakened the banking industry's infrastructure; as a result when international financial markets were turbulent, which began with the exchange rate crisis in Asian countries, Indonesian banks were unable to survive. This condition resulted in an increase in the crisis of confidence in the rupiah and national banking, especially after the revocation of 16 bank business licenses in November 1997.

To overcome the crisis of trust that occurred, in 1999, the government issued Law No. 23 of 1999 concerning Bank Indonesia which emphasizes the recovery, maintenance and stabilization of the value of the rupiah so that economic growth can run (Widyastuti, 2013). The next step taken by the government is to publish the API (Indonesian Banking Architecture) as the basic framework of Indonesia's overall banking system through Bank Indonesia. This API aims to provide the direction, form and order of the banking industry for the next five to ten years (BI, 2007).

According to Hajiwidjaja (2016), there are 5 important things that must be considered by a banking institution in improving the quality of its institutions. First, of course is a healthy banking structure. Healthy in the sense that it is free from corruption. The banking aspect must be strengthened, so that Indonesia has good economic resilience and is not easy to fall. This is supported by Yusuf's statement (2015) in which a country's economic resilience will depend on how strongly the banking sector manages the country's finances.

The banking sector must also have adequate supporting infrastructure. Luintel (2008) explained that with the complete infrastructure facilities, the wheel of economic rotation managed by the banking sector will run smoothly. This will affect the economic stability of the country. Equally important is that banks must be able to provide protection to consumers to maintain public trust in the banking sector (Ang, 2007).

Ariyanto (2004), stated that the banking industry has certain characteristics that are very different from other industries, it requires clear regulations and laws to be able to regulate it to run in accordance with its main target; towards healthy banking. Business competition over competition in the banking industry will force banks to take excessive risk, especially in the competition for credit and deposit markets.

Again, competition in the banking industry is important. This is because all forms of market failure and anti-competitive behavior will have a considerable influence on the efficiency of production, public welfare and economic growth. Research related to the structure of the banking market and its distribution has been widely carried out in several countries such as research conducted by Mamatzkis et al. (2005) in Europe, Hondroyiannis et al. (1999) in Greece, Bikker and Haaf (2002) in 23 developed countries, Trifonova (2005) in Bulgaria and others. The results of the study will differ depending on the market conditions in each of these places or countries.

There are many factors that influence banking performance and profitability. There are also many studies on this problem by experts, but to date it has not provided consistent results. De Jonghe's (2008) and Yuan (2006) research show that the effect of Capital Adequacy Ratio (CAR) on profitability is positive. Trifonova (2005) research results show the opposite of the results obtained by Sofriza Syofyan and Werdaningtyas, where that the capital adequacy ratio (CAR) has a negative effect on profitability.

One of the risks faced by banks in running their business is liquidity risk. Findings of Wetztein (2005) in his research shows that liquidity risk proxied in the Loan to Deposit Ratio (LDR) ratio has a positive influence on profitability. The research of Yuan (2006) and De Jonghe (2008) shows that liquidity has a negative effect on profitability.

Research on credit risk is carried out by Baltagi (2005) which states that a high condition of Non Performing Loans (NPL) will increase the cost of both earning assets and other costs, thus potentially causing losses to the bank, or in other words NPL decreases bank profitability. This shows that NPLs negatively affect profitability. This research contradicts the research results obtained by Wetztein (2005) which shows that NPLs have a positive effect on bank profitability.

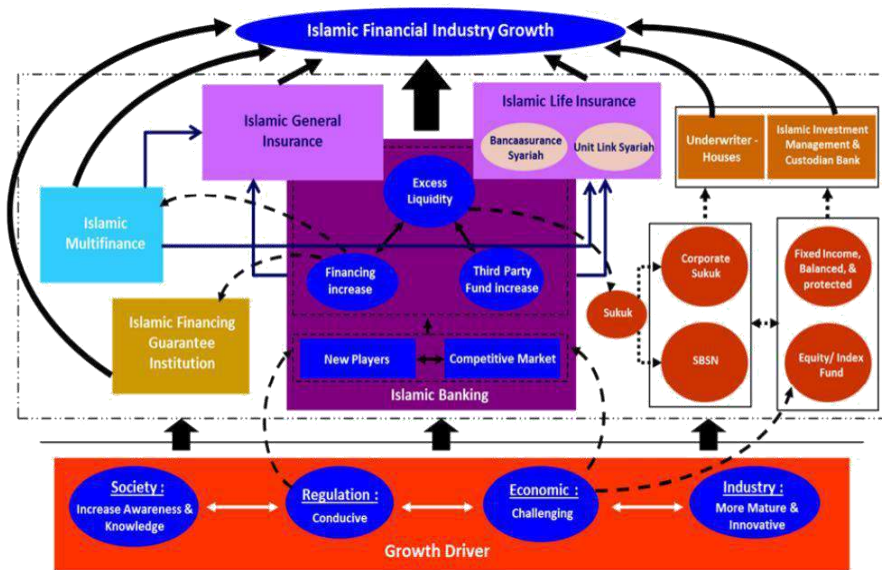
1.2 Conditions of Islamic Banking in Indonesia

The growth of Islamic banking in Indonesia experienced growth and dynamics (Hasan, 2014). Based on article 1 paragraph 1 of Law No. 21 of 2008 concerning sharia banking, it is everything concerning Islamic banks and Sharia Business Units (*Unit Usaha Syariah—UUS*), including institutions, business activities, as well as ways and processes in carrying out its business activities.

In the development of the Islamic banking system in Indonesia, it is carried out in the framework of dual banking or multiple banking systems (Mala, 2017). Law No. 10 of 1998 issued by Bank Indonesia (BI) explained that many conventional banks open UUS. Islamic banks opened in conventional banks include Sharia Bank Negara Indonesia (BNI), Sharia Rural Bank (BPR), West Java Bank (Jabar) Sharia, Indonesian International Bank (BII) Sharia, Bank Danamon Syariah, Indonesia Finance and Investment Company (IFI) Sharia and others. Not only domestic banks, but many foreign-owned banks also opened UUS, namely The Hongkong Bank and Shanghai Banking Corporation Limited (HSBC) Sharia. With no syariah units in conventional banks, it is very helpful in improving the development of Islamic banking and helping socialization to the public. The rapid development of Islamic

banking in Indonesia was also followed by the rapid study and publication of the principles and practices of Islamic banks, as well as the increasing public demand for usury-free banking services.

Based on information from the Financial Services Authority (*Otoritas Jasa dan Keuangan—OJK*) 2014 in the 2015 Sharia Banking Outlook, the Islamic financial industry system in Indonesia which consists of Islamic Banks, Sharia Insurance, Sharia Multifinance, Sharia Guarantee, Capital Markets, and other sharia financial institutions is a mutual entity relating and influencing each other in the growth of the Islamic financial industry in Indonesia. The linkage of the Islamic financial industry system can be seen in Figure 1 below.



Source: Sharia Finance Outlook, 2015

Figure 1 Industrial map of sharia finance

The interconnectedness of the Islamic financial industry system can be seen from the conditions when Islamic banks with other sharia institutions are increasing and competitive market conditions will affect the level of TPF and financing provided. In terms of TPF, when a large amount of deposited deposits and excess banks liquidity will affect the sharia capital market, for example, the increasing demand for *sukuk*, also increases Sharia Investment Management and Sharia Custodian

Bank. In terms of financing, when financing increases, it will affect financing guarantee institutions and Islamic finance. When Islamic finance and finance grow, it will also affect life insurance institutions and general insurance.

Sharia banking development reports published by the FSA explain that the development of Islamic banks in Indonesia has increased every year; this can be seen from the growth of the number of Islamic Commercial Banks (*Bank Unit Syariah—BUS*) and UUS. However, it has been declining, especially since 2013, reports on the development of Islamic banking from 2011 to 2015 as illustrated in the table below:

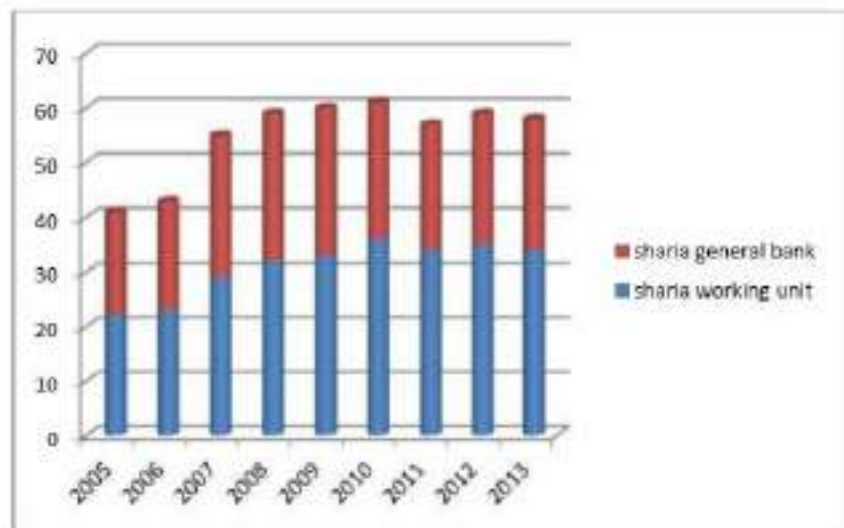
Table 2 Development of Islamic Banking

BUS amount	11	11	11	12	12	12	12
Conventional UUS-BUS amount	24	24	23	22	22	22	22
BPRS amount	155	158	163	163	162	162	162
Office network amount (BUS+UUS)	1,737	2,262	2,588	2,517	2463	2458	2248
Asset in total (IDR trillion)	145,47	195.02	242.28	272,34	268,36	269,47	272,389
Asset growth (Joy)	49%	34%	24%	12.41%	11.39%	10.35%	10.74%
Market share	3.98%	4.58%	4.89%	4.85%	4.68%	4.69%	1***
TPF (IDR trillion)	115.41	147.51	183.53%	217,86%	212,99%	213,97	215,339
Expenses (IDR)	102.66	147.51	184.12	199,30	200,71	201,53	203,894

Trillion)							
NPF (gross)	2.52 %	2.22 %	2.62 %	4.3 3%	4.8 1%	4.62 %	4.76 %
CAR	16.6 3%	14.13 %	14.4 4%	16. 10 %	13. 85 %	14.0 6%	14.0 6%
FDR	88.9 4%	100.0 %	100. 32%	91. 50 %	94. 24 %	94.1 8%	94.6 9%

Source: Sharia Banking Outlook, 2015

Table 2 can be put in a figure as follow.



Source: Sharia Banking Outlook, 2015

Figure 2 Development of sharia banking institution

From the picture above, it proves that in 2005 there were only 3 BUS, namely Muamalat Bank, Bank Syariah Mandiri and Bank Mega Syariah. If seen from the graph above the growth of UUS each year has increased compared to the growth of BUS, but in 2010 UUS decreased due to some UUS who spin off. And in 2013 there was also a reduction in the number of UUS due to the closure of HSBC Syariah and in mid-2014 there was also a reduction in the number of UUS due to the Sharia

National Pension Savings Bank (*Bank Tabungan Pensiunan Negara – BTPN*) which spin off in July 2014 so the number of BUS became 12 and the number of UUS became 22. However, the largest BUS growth occurred in 2010, namely 5 new BUS.

Based on a report from the 2015 Sharia Banking Outlook, there is an increase in the growth of the Islamic banking industry in Indonesia. This increase can be seen from the financing share of Rp 184.1 trillion in December 2013 to Rp 187 trillion of the total assets of BUS and UUS in June 2014, but the market share of sharia financing decreased and reached 3.69% until June 2014 from national banks.

The same thing happened to the percentage of Islamic bank financing growth until June 2014 which was only 2.14%, although there is still one semester remaining for Islamic banks to increase their growth, but it is not expected to reach the previous year's growth. For more details, see Figure 3 below regarding the development of financing and market share of Islamic banking.



Source: Sharia Banking Outlook, 2015

Figure 3 Development of expenses and market share sharia banking

The rapid growth of Islamic banking in Indonesia is the result of Bank Indonesia's work in developing Islamic banking in Indonesia by

formulating a grand strategy as a comprehensive strategy for the development of Islamic banking market covering several strategic aspects, namely: establishing a vision as a leading sharia banking industry in the Association of South East Asian (ASEAN), the formation of the new inclusive and universal national sharia banking, more accurate market mapping, improved product development, improved services, and new communication strategies that position more than just Islamic banking just a bank (beyond banking) (Rozalinda, 2014). The determination of this vision strongly supports the growth of Islamic banking in Indonesia, because precisely on the December 31st 2015, ASEAN countries entered the world economic system or the so-called ASEAN Economic Community (AEC) including Indonesia (Bakhri, 2015).

ASEAN 2015 single market has begun. This was created by the leaders of ASEAN countries through their joint commitment resulting from the 13th ASEAN Summit in Singapore in 2007. The Summit succeeded in formulating a blueprint for economic stability and political security in the ASEAN region (Konoras, 2014). The purpose of the establishment of the AEC is that it participates in the MEA to implement efficiency optimally. If the mechanism in regional economic integration runs smoothly in each ASEAN country, then every country that participates in the MEA can improve equitable economic development.

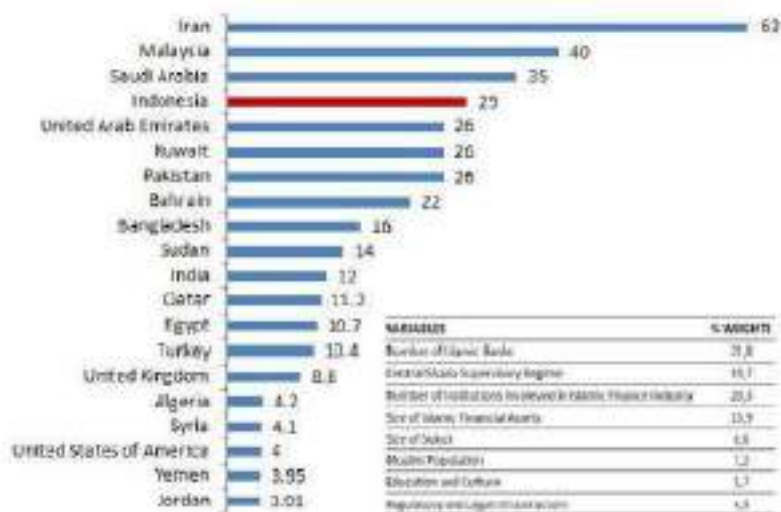
The forming of MEA can lead many sectors to gain wider market share and investment in South East Asia region. The meaning of the implementation of the MEA makes the economy fully integrated into the global economy to be involved in the five elements of a single market (free flow of goods, services, investment, capital, and labor) in a unified production base. ASEAN countries those who join the MEA are required to compete with each other by utilizing the opportunities that exist (Bakhri, 2015).

Indonesia's agreement in the MEA 2015 is a challenge for Islamic banking because the potential domestic market will be taken by competitors from other countries. Indonesia, which is a member of

ASEAN countries, is required to compete with nine other ASEAN countries, namely Laos, Brunei Darussalam, Philippines, Cambodia, Malaysia, Myanmar, Singapore, Thailand and Vietnam. Each ASEAN country has the same opportunity to win the AEC 2015 competition. Indonesia, which has a majority of Muslim population, should be the pioneer of economic development in the Islamic financial sector (Alamsyah, 2012).

From the information of the 8th Anniversary of the Association of Islamic Economics Experts, Indonesia has the potential to become a global Islamic financial player, including: (1) a large Muslim population becomes a potential Islamic sharia industry customer; (2) a bright economic outlook, reflected in relatively high economic growth (range of 6.0% -6.5%) supported by solid economic fundamentals; (3) increasing Indonesia's rating sovereign credit to investment grade which will increase investors interest in investing in the domestic financial sector, including the sharia financial industry; and (4) having abundant natural resources that can be used as underlying transactions in the Islamic financial industry. MEA which was intended to improve the economy in the Southeast Asia region, but this has made concerns for some Indonesian people (Alamsyah, 2012).

According to Halim Alamsyah, the Global Islamic Finance Report (GIFR) revealed that Indonesia has potential in the development of the sharia financial industry, because Indonesia ranks fourth after Iran, Malaysia and Saudi Arabia (Hayat, 2014). The development of the Islamic financial industry can be seen in Figure 4.



Source: 8th Milad of IAIEI, 2012

Figure 4 Islamic Finance Country Index (IFCI, 2011)

Indonesia as a country with Muslim population the biggest, it should be a reference and a *qibla* for sharia-based financial development in the world (Lo, 2014). This hope is not an impossible hope to achieve, given that Indonesia has enormous potential in the banking sector (finance and economy). Hasan (2007) identified several potentials that Indonesia has, including:

- a) the large Muslim population becomes the potential of sharia financial industry customers;
- b) a bright economic outlook, reflected in relatively high economic growth (range of 6.0% -6.5%) supported by solid economic fundamentals;
- c) increasing Indonesia's rating sovereign credit to investment grade which will increase investor interest in investing in the domestic financial sector, including the sharia financial industry; and,
- d) possessing abundant natural resources that can be used as underlying transactions in the sharia financial industry.

According to data from the Global Islamic Financial Report (GIFR) in 2011, Indonesia is in fourth position in terms of the potential and conduciveness of the development of the Islamic financial industry after Iran, Malaysia and Saudi Arabia. Irfan (2009) explained that the aspects seen in determining this ranking are the number of existing Islamic banks, the number of non-sharia financial institutions, and how much Islamic financial assets they have. By looking at these aspects, Indonesia is projected to be a country that has the potential to be ranked the first in the next few years. This optimism goes hand in hand with the pace of institutional expansion and increasingly high and improving banking asset growth, coupled with the increasing volume of *sukuk* issuance that has increased constantly.

Wangsawidjaja (2012) explained that the development of Indonesia's sharia-based finance that is market driven and encouraging bottom up so that it relies more on the real sector in meeting the needs of the community, can be a distinct advantage in economic competition among Islamic countries. In contrast to the development of Islamic finance in Iran, Malaysia, and Saudi Arabia, where the development of Islamic finance is more based on the financial sector, not the real sector, and the role of government is very dominant. Umam and Khaerul (2013) added that besides in the form of good regulatory support, the placement of government finances and state-owned companies in Islamic financial institutions made the country's total assets significantly increase, especially when these countries use windfall profits from rising oil and commodity prices.

Basran (2005) explains that Indonesia has other advantages in the banking industry, namely regulatory regimes that are considered better than other countries. In Indonesia, the authority to issue a Sharia financial fatwa is centralized by the National Sharia Council (*Dewan Syariah Nasional-DSN*) - the Indonesian Ulema Council (*Majelis Ulama Indonesia-MUI*) which is an independent institution. While in other countries, fatwas can be issued by individual scholars so that the chances of a difference are very large. This is supported by Kasmir (2000, p. 35) who provides information that in Malaysia, the

organizational structure of this fatwa institution is under Bank Negara Malaysia (BNM), not independently independent.

As one of the main drivers of the state banking sector, Bank Indonesia has shown seriousness in encouraging the development of Islamic banking (Mervyn, 2007, p. 89). This spirit is based on the belief that Islamic banking will bring benefits to economic improvement and the equitable distribution of people's welfare.

Sutrisno (2013) has identified several benefits offered by Islamic banking management.

- a) First, Islamic banks are closer to the real sector because the products offered, especially in financing, always use underlying transactions in the real sector so that the impact is more real in driving economic growth.
- b) Second, there are no speculative products (*gharar*) so that they have strong durability and are tested for their toughness from direct hit the global financial crisis. At macro level, Islamic banking can provide support for the creation of financial system stability and the national economy.
- c) Third, the profit sharing system that becomes the spirit of Islamic banking will bring fairer benefits to all parties, both for the fund owner as the depositor, entrepreneurs as debtors and banks as fund managers. This is supported by Widyastuti's (2013) statement that a fair Islamic banking system has built customer trust in the bank. This will support the government's efforts to develop the economic sector through the management of a strong and stable banking industry.

Hasan (2011) explained that his subordinates of Indonesian banks had formulated policies for developing Islamic banking in Indonesia, by publishing the "Blueprint for Sharia Banking Development in Indonesia" in 2002. Various aspects had been comprehensively considered in its preparation, including the actual conditions of the national Islamic banking industry along with related tools, trends in the

development of the international Islamic banking industry and the development of the national Islamic financial system, a more macro financial system framework such as the Indonesian Banking Architecture (API) and the Indonesian Financial System Architecture (ASKI) as well as international best practices formulated by institutions international Islamic financial institutions, such as the IFSB (Islamic Financial Services Board), AAOIFI (Accounting and Auditing Organization for Islamic Financial Institution) and IIFM (International Islamic Financial Market).

The target to be achieved within 10 years is the achievement of a significant market share of sharia banking through deepening the role of Islamic banking in national, regional and international financial activities, in the starting conditions the formation of integration with other Islamic financial sectors (Umam and Khaerul, 2013). In the short term, national Islamic banking is more directed to the service of the domestic market whose potential is still very large.

In other words, national Islamic banking must be able to become a domestic player but have an international quality of service and performance (Wangsawidjaja, 2012). In the end, the Islamic banking system that Bank Indonesia wants to realize is modern sharia banking, which is universal, open to all Indonesians without exception. According to Yuliadi (2013) Bank Indonesia has formulated a Grand Sharia Banking Market Development Strategy, as a comprehensive market development strategy that covers strategic aspects, namely determination of the 2010 vision as the leading sharia banking industry in ASEAN, the formation of a new national sharia banking image inclusive and universal, more accurate market mapping, more diverse product development, improved services, and new communication strategies that position Islamic banking more than just a bank. The commitment of the Indonesian government to develop Islamic banking seems to be large.

This is driven by the enormous market potential that makes a drastic increase in players in Islamic banks. Moreover, the Indonesian

population is mostly Muslim (Hasan, 2011). This commitment has been proven by the formulation of the Sharia Banking Law. Driven by development sharia banking industry which is very rapid in Indonesia, this article is prepared to show competition in the sharia banking industry and the competitive situation in the financial industry, so that it can provide information input for the preparation of competitive strategies of companies that play in the sharia banking industry.

In the government's efforts to actively develop Islamic banking in Indonesia, there were several problems and challenges encountered. According to Asnaini (2008) in the majority of Indonesians there is still a growing stigma that Islam can only be realized in *ubudiyah* ritualism and soliciting Islam as an aspect not related to the world of banking, capital markets, insurance, deposits, demand deposits, export-import transactions, and activities other economies, even there is an assumption that understanding in Islam will be able to slow down the pace of the economy. In fact this is a false assumption or stigma, Yusuf (2015) finds that Islamic-based economic activities will be able to make the country's growth and finance sector grow and increase.

In line with this, Zubair (2008) explained that in essence Islamic economics is universal and applied by everyone, even those who embrace religion other than Islam. This assumption was proven by the multi-dimensional crisis in the economic and monetary fields that had struck the country of Indonesia some time ago, even though it had come out of the crisis but the figure still felt until now, that in fact the economic system adopted and proud of all this time, especially in the banking sector, will not be able to cope with and overcome the conditions of the economic crisis, it may even be said that the system is far from the *syar'i* value as the operational basis, and the cause of the growth and development of a culture of corruption.

Wikaningrum (2011) also explained the facts and reality that said otherwise or vice versa the world of banking and Islamic Financial Institutions (*Lembaga Keuangan Syariah-LKS*) in its operations was sharia-based, so that the economic and monetary crisis that occurred

was a positive momentum to show and provide real and clear evidence to the banking world, that Islamic banking in fact remains and develops in a crisis. Because it's time for the government and the people of Indonesia to open their eyes and change their perspective towards Islamic banks as an alternative to be developed in the world of Indonesian Banking today (Muhammad, 2004, p. 78).

However, in reality, it is very unfortunate that the development of Islamic banks in Indonesia seems rather slow because it is not managed professionally. The underdevelopment of Islamic banks lies in their own people, because there are still Muslims who do not understand Islamic economics or do not practice it in transacting business and daily finance, feeling afraid of being poor because of it (Siswanto, 2011).

If seen in practice, there are many challenges and problems faced in the development of Islamic banks especially in relation to the application of a new banking system and having very principle differences from the dominant profit system and has developed rapidly at this time. These problems are banking operations and aspects of the macro environment. El-Seodi (2012) suggested several challenges and problems faced in the development of Islamic Banks in Indonesia, such as follow.

a. Sharia Working Capital Financing

Capital is one of the most important aspects in the banking sector. Included in the effort to develop the quality of Islamic banks in Indonesia. The provision of strong capital will provide convenience in efforts to develop banking in Indonesia. The most basic problem is, (1) investors' doubts about the prospects for the success of Islamic banks in the future, (2) the calculation of the investor business that is not based on the sense of value of *ubudiyah* so that it seems solely to seek worldly profits and feel objected if it has to invest part of its funds in Islamic banks as capital, (3) the last is Bank Indonesia regulation in placing high capital.

b. Banking World Regulation

Existing banking regulations still need to be adjusted to meet sharia regulations so that Islamic banks can operate relatively and efficiently and be able to compete, among others; first, the instrument needed to overcome liquidity problems; second, monetary instruments in accordance with sharia principles for the purposes of carrying out the duties of the central bank; third, standardization of accounting, auditing and reporting systems; fourth, regulations governing the principle of prudence. The fourth provision of this regulation is needed so that Islamic banks can become the most important elements of the monetary system that can carry out their functions properly, able to develop and compete.

c. Lack of Human Resources

The number of Islamic banks in Indonesia which are increasingly spreading is not matched by quality of human resources (HR), so that the development of the banking sector becomes slow. Islamic banking system is still not long known in Indonesia, besides that education and training institutions are still limited, so that educated and experienced personnel in the field of sharia banking both from the side of executing banks and central banks (bank supervisors and researchers).

HR development is needed because the success of developing Islamic banks at the micro level is very much determined by the quality of management and the level of knowledge and skills of managing the bank. HR require general knowledge requirements in the banking sector, understand the implementation of sharia principles in banking practices and have a commitment to implement them in a consistent manner (*istiqamah*).

a. The Level of Understanding and Exclusion of the *Ummah*

Understanding and care of most people regarding the system and principles, even though sharia is not right, even among the ulamas and Muslim scholars themselves there is still no agreement to support the existence of Islamic banks. Even there are still clerics who have not had a firm opinion on the existence of Islamic banks, so it feels less

assertive. It is because: first, the lack of comprehensive information that reaches scholars and scholars about the dangers and destructive effects of the interest system, especially when the monetary crisis and the economy are hit by a downturn; second, the development of LKS has not yet been developed so that ulamas are in a difficult position to prohibit conventional financial transactions that have been running and developing widely and which are ingrained in society; third, the understanding of the operation of Islamic banks in depth and faith is not yet understood; fourth, intellectual rigidity and laziness that tend to be pragmatic so that there is an assumption that the prevailing interest system is currently operating or does not conflict with the provisions of sharia.

Whereas history knows the ulama is not just a figure of knowledge, but also as a motivator and motivator of the community. The scholars who are competent in sharia law have a very large function and role in Islamic banking, namely as a Council Sharia Supervisors and National Sharia Board. The lack of understanding of sharia banking may be due to relatively new systems and operational principles compared to the interest system, and their development is still in the early stages when compared to conventional banks have previously taken positions in the hearts of the people, as well as reluctance to conventional banking service users to move to Islamic banks due to the loss of opportunity to get a fixed income from interest

b. Islamic Bank Turns Out Not Sharia.

If observed by almost all existing banks, start developing the Islamic banking system. What opportunities will be achieved, it turns out Islamic banks thrive like mushrooms in the rainy season. But unfortunately in the field, the practice cannot be expected more to fight for the final value of sharia in practice. There are still banks struggling with the capitalist system, even though the clothes are worn by sharia. It is ironic indeed, when a banking researcher was astonished by the mechanism of Islamic banks that were anti-crisis, when 1998 became the bankruptcy of conventional banks almost nationally. After careful

research, it turns out that the Islamic bank in question still is capitalist, meaning that the bank only provides assistance to large business owners, while middle and lower business owners are not considered at all.

The desire to use the name of sharia cannot be denied to be its own to reach Muslim customers. Islamic bank products are introduced and packaged in such a way that they convince customers. But on the other hand Islamic bank practitioners have not mastered sharia practices in the field. Evidenced by the comparison of several people who tried to borrow from a particular Islamic bank, what happened turned out to be higher than the conventional bank. The case which has happened a little more, and must be followed up, in the long run there must be training about Islamic bank products in their daily practice, or now that is developing, each bank is looking for alternative supervisors consisting of ulama, or those who have mastered it properly Islamic products. With this supervisory alternative, the banking transaction process has been supervised by an expert, so that errors that occur in the field can be minimized.

The concept will certainly lift the face of the nation's economy, meaning that it strengthens the economic base of the nation that has been embracing the capitalist system. In the long run it will give understanding to the community; property is no longer private ownership, but social ownership. From this point of course it will lift again the nation's economy with the *ta'awun* system, the hope of the *aghni'a* can help the lower middle class (*dhuafa*) to raise their economic level to a more established level.

1.3 Summary

- With a dense population and a country that has very promising economic potential, Indonesia has become one of the countries considered in economic competition in Asian countries.

- The government, through several proclaimed programs, has attempted to restructure national banking so that there will not be a crisis in the future. The government program includes, among others, (a) the banking recovery program which includes a *Blanket guarantee* program, namely the recapitulation program and credit restructuring; and (b) efforts to strengthen the banking resilience system which includes improving banking infrastructure, good governance and banking supervision and regulations.
- The growth of Islamic banking in Indonesia has experienced growth and dynamics (Hayat, 2014). Based on article 1 paragraph 1 of Law No. 21 of 2008 concerning sharia banking, it is everything concerning Islamic banks and Sharia Business Units (UUS), including institutions, business activities, as well as ways and processes in carrying out its business activities.
- The percentage of sharia bank financing growth up to June 2014 was only 2.14%, although there is still one semester remaining for Islamic banks to increase growth, but it is not expected to reach the previous year's growth.
- The rapid growth of Islamic banking in Indonesia is the result of Bank Indonesia's hard work in developing Islamic banking in Indonesia by formulating a Grand Strategy as a comprehensive strategy.
- National Sharia Banking must be able to become a domestic player but have international quality service and performance.

CHAPTER 2

GENERAL BANKING PHENOMENON IN INDONESIA

2.1 History of General Banking in Indonesia

Knowledge of the banking legal system cannot be separated from the history of banking, the school of history itself states that the existing legal rules are a form of legal rules that cannot be separated from the history of a nation or past activities. Likewise, the existence of banking law cannot be separated from the banking history. Here are some brief descriptions of banking history in the world from the beginning of the rise of valuable objects storage systems, financial transactions to the creation of national banks in each country (BI, 2011).

Dendawijaya (2005) describes the words 'Bank' derived from the Italian *banque* or *banca* which means bench. The bankers in Florence during the Renaissance did their transactions by sitting at a money exchange table, in contrast to the work of most people who did not allow them to sit down while working. The banking business itself began only in the Babylonian era and then continued into ancient Greece and Rome. However, at that time the main task of the bank was only as a place to exchange money.

Haque (2013) added that along with the development of world trade, the development of banking was also increasing rapidly because the development of the banking world was inseparable from the development of trade. Development initial trade only in mainland Europe finally spread to West Asia. In contrast, the development of banking in the new British land began in the 16th century. However, because the British were so active in seeking trade areas that were later colonized, the development of banking was also brought to their colonies (Hanif, 2012). The following is an explanation of the history of the Bank's development in Indonesia in several decades:

a. Pre-Independence Period

The presence of the First banking institution in Indonesia was inseparable from the colonial Dutch East Indies Reestigde Oost-Indische Compagnie (VOC) in Indonesia. VOC was the holding company of Dutch trading companies, they established their authority in Batavia in 1619 (Denisari, 2014).

Ansari and Atiqah (2011) added, to facilitate and facilitate the trading activities of the VOC in the archipelago, De Bank van Leening was established precisely on August 20, 1746. In its journey, De Bank van Leening was unable to operate properly, then merged into De Bankcourant which was established on September 1, 1752 and its name changed to De Bankcourant en Bank van Leening on September 5, 1752. But De Bankcourant and Bank van Leening were also unable to operate properly and were finally closed due to bankruptcy. De Bank van Leening later changed to De Bank Courant en Bank van Leening in 1752. By the end of the 18th century, the VOC had suffered a setback, even bankruptcy. So the power of the VOC in the archipelago was taken over by the government of the Kingdom of the Netherlands. After the reign of Herman William Daendels and Janssen, the East Indies finally fell into British hands. Banking history also noted several banks that played an important role in the Dutch East Indies. The existing banks include:

1. De Javasce NV.
2. De Post Poar Bank.
3. Hulp en Spaar Bank.
4. De Algemenevolks Crediet Bank.
5. Netherlands Handles Maatscappi (NHM).
6. Nationale Handles Bank (NHB).
7. De Escompto Bank NV.

De Javasche Bank, which was founded in 1828, is a Dutch bank that succeeded in developing and was the forerunner of the Indonesian central bank in the future. Bank Indonesia (2007) writes that other

Dutch banks such as the Nederlandsch Indische Escompto Maatschapij, Nederlandsch Indische Handelsbank, and Nederlandsche Handel Maatschapij began operating successively in 1857, 1864 and 1883. De Javasche Bank by the Dutch East Indies government was given monopoly to issue money originally circulated by the government itself. Since then the bank is well-known as a circulation bank, or bank of issue (Hanif, 2012). From this function, the bank is a banker for the Dutch East Indies government, although it is not yet a full central bank, because it only carries out some of the tasks normally carried out by the Central Bank, namely: issuing and circulating banknotes; discount notes, short-term debt, and state bonds; become a government cashier; save and control foreign exchange funds; and has acted as the clearing center since 1909. Despite its duties as a circulation bank, the duties as a commercial bank remain in operation, thus competing with other banks.

This dualistic nature has repeatedly led to a variety of criticisms, stating the reasons, namely among others as follows:

1. With a lower interest rate than other banks, De Javasche Bank can easily attract the best customers.
2. Competition by a De Javasche Bank which, because of its duties, can have data from other banks, so that it is considered unnatural.

Along with the development of the archipelago economy, several other foreign banks also began operations, namely as follows:

1. The Chartered Bank of India, Australia and China, Batavia Tahun1862
2. Hong Kong and Shanghai Banking Corporation, Batavia Tahun1884
3. Yokohama-Specie Bank, Batavia in 1919
4. Taiwan Bank, 1915, Batavia, Semarang and Surabaya
5. China and Southern Ltd., Batavia in 1920
6. Mitsui Bank, Surabaya Year 1925

7. Overseas China Banking Corporation, Batavia Year 1932

Ningsih (2012) explained that during the colonial period, there were ups and downs in the number of banks. Near the outbreak of World War II, the Dutch East Indies Government liquidated three Japanese banks that were operating at that time. By the time Japan came to power over the Asia Pacific, Dutch, British, and including several Chinese banks were liquidated by Japan, the governing Japan only recognized the Japanese government that controlled the entire financial and banking system there was only one bank operating by the Indonesian son namely the People's Bank Indonesia (Algemeene Volkscrediet Bank) whose name is Japan, Syomin Ginko (Naili, 2013). De Javasche Bank in the Dutch era was a bank that acted as the Central Bank, and in the Japanese colonial era the bank was controlled by the Japanese army government. After independence, the bank then operated again, even for a number of years, it functioned again as a Central Bank, although it was domiciled as a private business entity and some of its shares were in foreign hands. In view of the aforementioned matters, De Javasche Bank nationalization was carried out pursuant to Law Number 24 of 1951 concerning De Javasche Bank Nationalization, the Act was ratified on 6 December 1951.

b. Early Period of Independence and Old Order

The situation of independence on August 17, 1945, brought fresh air to the Indonesian people to drive the wheels of banking by nationalizing the existing banks, with the success of the allies defeating Japanese imperialism to return Dutch banks and Foreign Banks to reappear and banking institutions other, the permit to open a Dutch bank in Indonesian territory was issued on January 2, 1946 by the Governor General of the Dutch East Indies. Dutch banks are also operating again in several parts of Indonesia.

The policy which was quite influential in the development of banking at the beginning of independence was the nationalization of De Javasche Bank (Denisari, 2014). De Javasche Bank after independent

Indonesia operated again even for several years functioning as the Central Bank even though it was domiciled as a private business entity and some of its shares were in foreign hands. In view of such matters, the nationalization of De Javasche Bank was carried out through Law Number 24 of 1951 concerning De Javasche Bank Nationalization. Ramadaniar (2012) added, then in 1953 with the consideration of making it easier to carry out monetary and economic policy, Law Number 11 of 1953 concerning the Establishment of the Bank Indonesia Basic Law and better known as the Bank Principal Law Indonesia 1953.

This was done considering that De Javasche Bank, despite being nationalized, was still a legal entity as a Limited Liability Company, so it was still not free in implementing its monetary policy. In accordance with the Act, BI as the central bank has the duty to supervise banks. However, the implementation rules of the supervisory provisions are only stipulated in Government Regulation (PP) No. 1/1955 which states that BI, on behalf of the Monetary Board, conducts bank supervision of all banks operating in Indonesia, in the interest of the solvency and liquidity of these credit agencies and healthy lending based on the principles of appropriate bank policies. From the supervision and inspection of BI, unfair practices were revealed, such as depositing fictitious capital or even bank practices in banks. To overcome the banking conditions, the Monetary Board Decree No. 25/1957 which prohibits banks from conducting activities outside banking activities.

In the period after Indonesia's independence, based on Government Regulation No. 1 of 1946 Article 1 states that BRI is the first Government Bank in the Republic of Indonesia (Munir, 2012), (Naili, 2013). Given the situation of the war to defend independence in 1948, BRI's activities were temporarily halted and only began to re-active after the Renville agreement in 1949 by changing its name to Bank Rakyat Indonesia Union. At that time through PERPU No. 41 of 1960 formed a Farmers and Fishermen Cooperative Bank (BKTN) which was a merger of BRI, the Farmers 'Farmers' Bank and the Nederlandsche Maatschappij (NHM).

According to Munir (2012), then based on Presidential Decree No. 9 of 1965, BKTN was integrated into Bank Indonesia under the name Bank Indonesia Affairs of Farmers and Fishermen Cooperatives. After walking for one month, the Presidential Decree No. 17 of 1965 concerning the establishment of a single Bank under the name Bank Negara Indonesia. In the new provisions, Bank Indonesia Affairs for Cooperatives, Farmers and Fishermen (ex BKTN) was integrated with the name Bank Negara Indonesia unit II in the field of Rural, while NHM became Bank Negara Indonesia unit II in the field of Import Export (Exim) (Handayani, 2005).

Based on Law No. 14 of 1967 concerning Law on Banking Principles and Law No. 13 of 1968 concerning the Central Bank Act, which essentially restores the functions of Bank Indonesia as the Central Bank and Bank Negara Indonesia. The Rular Unit II and Import Exports are separated into two Banks, namely Bank Rakyat Indonesia and Indonesian Import Export Bank. Furthermore, based on Law No. 21 of 1968 re-established the main tasks of BRI as a Commercial Bank (Kuncoro, 2007).

At the session of the Council of Ministers of the Republic of Indonesia on September 19, 1945 it was decided to establish a bank the session of the Council of Ministers of the Republic of Indonesia on September 19, 1945 was decided to establish a state-owned bank that served as a circulation bank. To prepare for its formation, the government gave a power of attorney to Mr. R.M. Margono Djojohadikoesoemo (late). As a first step on October 9, 1945, the Poesat Bank Indonesia Foundation was established. Furthermore, on July 5, 1946 a central bank was established under the name Bank Negara Indonesia (BNI), with 38 employees (BI, 2007).

Faqihuddin (2011) also explained that the Poesat Bank Indonesia Foundation which was the forerunner of the birth of BNI Bank was merged into it. In the following years various efforts were made by the Indonesian government to establish the position of Bank Negara Indonesia. In the Round Table Conference (KMB) in 1949, the

Governments of Indonesia and the Netherlands decided to change the function of Bank Negara Indonesia from the central bank to a commercial bank. Bank BNI began directing its business for economic development, while Bank Indonesia (which at that time was De Javasche Bank) was appointed as the central bank (BI, 2007).

The history of banks in Indonesia is more complete with the nationalization of several Dutch banks in 1959 to 1960, such as: Nationale Handels Bank NV, which changed into a State Commercial Bank, Escomptobank changed its name to Bank Dagang Negara and Nederlandsche Handels Maatschappij becomes the Indonesian Import Export Bank (Hanif, 2012). The government policy to nationalize Dutch companies is stipulated in Law No. 86/1958 which was retroactively applied until 3 December 1957. The nationalization of Dutch banks which were foreign exchange banks was carried out based on the principle of prudence so as not to cause losses on the country's foreign exchange reserves. For this reason, the Central Bank Supervisory Board maintains the old directors of supervised banks. Ismal (2011) explained, If Dutch-owned banks were nationalized by the government, then it would be different from foreign banks that did not belong to the Netherlands. With self-sustaining principles and a passionate spirit of nationalism, in the 1950s the government declared the closure of several foreign (not Dutch) banks, namely the Overseas Chinese Banking Corporation, the Bank of China, and the Hong Kong and Shanghai Banking Corp. based on Government Regulation No. 2/1959.

Correspondingly, Rivai (2010) explained that the nationalization of Dutch banks was due to the high nationalism spirit of the Indonesian people because the Dutch reneged on the Dutch Linggar teak agreement and the Dutch Military Aggression I was successfully terminated through Renville negotiations on January 17, 1948. Siregar (202) explained that even though the agreement had been made, the Netherlands reneged on the agreement of the Renville Agreement and returned to Aggression II. The new weapons conflict between Indonesia and the Netherlands actually stopped after the Council UN

Security passed a resolution on January 28, 1949. At the end of 1949, the Round Table Conference (*Konferensi Meja Bundar—KMB*) negotiations held in The Hague in the Netherlands resulted in the formation of the United Republic of Indonesia which covered the entire territory of Indonesia, except the West Irian region which would be completed in time one year. Until finally, the Republic of Indonesia dissolved the RIS in 1950, the problem of returning West Irian was not realized, so that the anti-Dutch feeling that was already in the minds of the people was getting bigger because of it.

Kasmir (2010) explained that in order to maintain the legality of the activities of nationalization of Dutch companies, the government then issued Law No. 86 of 1958, which was retroactively valid until 3 December 1957. The nationalization of Dutch banks began with the cessation of all foreign traffic activities of *Nationale Handelsbank N.V.* (NHB).

As of November 3, 1958, NHB is not permitted to make new transactions. NHB is only permitted to continue the process of foreign transactions that have previously been carried out before November 5, 1958. NHB requires correspondent banks abroad to transfer all foreign currencies on behalf of the State's Foreign Exchange Funds account (Setyowati, 2004). NHB's management was handed over to BPBB (the Bank-Supervisory Board consisting of representatives from the Army, Bank Indonesia and the Ministry of Finance, approved by the announcement of the Minister of Finance and Decree of the KSAD No. Kpts/MP/080/1957 dated 8 December 1957) and BPBB Center on April 20, 1959, and then nationalized on August 10, 1959.

All NHB assets were then transferred to the State Commercial Bank. The *Escomptobank Basic Budget* was amended through the General Meeting of Shareholders held on November 18, 1958. The board of directors and directors of PT *Escomptobank* in Jakarta, who were all original Indonesian citizens, were given more authority over the supervisory board / Branch leaders from *Escompto* offices overseas banks. PT *Escompto* bank shares that have been issued on the show,

must be changed to on behalf of. The Bank Indonesia Basic Law 1953, After the issuance of the Bank Indonesia Basic Law of 1953, Bank Indonesia as an institution that was very interested in the establishment of provisions concerning bank supervision had conducted research and assessment of similar provisions applicable in various countries, especially the Netherlands.

Deni and Djoni (2004) explained that in order that the number of private banks would not continue to increase without being monitored, starting from 1 January 1955 the Government Regulation No. 1, to arrange supervision of credit in Indonesia. This regulation regulates the supervision of all commercial banks and savings banks operating in Indonesia by Bank Indonesia on behalf of the Monetary Board for the benefit of banks' solvency and liquidity and for the benefit of healthy lending and based on the principles of appropriate bank policy.

After the issuance of Government Regulation No.1 Year 1955, national private banks that have existed within three months must apply for a business license to the Minister of Finance through Bank Indonesia. If the conditions for obtaining a permit have not been fulfilled, then the Minister of Finance will grant a temporary permit. The Minister of Finance grants permanent permits at the recommendation of Bank Indonesia. A number of banks still have not received permission because of capital requirements that they cannot meet.

In connection with this, the Monetary Board decided to extend the validity period of the temporary permit one more year, with the hope that the banks really shows its benefits for the community to have the opportunity to meet the required capital (Suhartati, 2004).

c. New Order period

Siregar (2002) explained that, the Supersemar incident of March 11, 1966 and the dissolution of the PKI on March 12, 1966 was a milestone in the birth of the new order. Furthermore, on July 25, 1966 an Ampera Cabinet was formed to replace the Dwikora Cabinet. The main task of the Ampera Cabinet is to implement a stabilization and rehabilitation

program that concentrates on controlling inflation, fulfilling food livelihoods, rehabilitating economic infrastructure, increasing exports, and fulfilling clothing needs. The New Order government wanted to consistently implement a balanced budget system, and free foreign exchange traffic. Kuncoro (2007) identified several Ampera Cabinet programs known as the Ampera Cabinet Work Chess namely:

1. Improve people's lives, especially in the clothing and food sectors;
2. Carry out general elections within the stipulated deadline, namely July 5, 1968;
3. Implementing a free and active foreign policy for the national interest;
4. Continuing anti-imperialism and colonialism struggles in all their forms and manifestations;

After the MPRS on March 27, 1968 established Soeharto as president of the Republic of Indonesia for a five-year term, a Development cabinet was formed with the task called Panca Krida which included:

- a) Creating political and economic stability;
- b) Formulate and carry out General Elections,
- c) To erode the remnants of the September 30th Movement and clean up the State apparatus at the center and area from the influence of the PKI.

The next step to improve banking in the New Order government began with strengthening invitations that regulate banking in the form of replacement and making new laws, for example making new regulations in the form of Law Number 14 of 1967 concerning Banking Principles, while those that in the form of replacing old regulations, namely in the form of Law Number 13 of 1968 concerning the Central Bank, in order to replace Law Number 11 of 1953 concerning the Principles of Bank Indonesia (Iqbal, 2005).

Sugiarti (2015) describes the improvement of banking institutions by strengthening their legal foundation, is a pillar for the implementation

of guidance, and supervision that supports the improvement of the ability of banks in carrying out their functions in a healthy, fair, efficient manner, while enabling Indonesian banks to make the necessary adjustments in line with the development of norms. international banking norms.

As a first step to improve national economy, the New Order government through Law Number 14 of 1967 concerning Banking Principles wants to clearly regulate banking business including credit issues. so management errors, such as uncontrolled credit expansion can be avoided. In addition to improving the effectiveness and efficiency of the collection and use of public funds. In addition, opportunities were also opened for the establishment of foreign banks, namely through the provisions of Government Regulation Number 3 of 1968 concerning Foreign Banks (Suhartati, 2004).

d. Facto Era of 88 (1983-1997)

Ansari (2011) explained that when entering this period, banks as part of the financial system must adjust their efforts to the deregulation and debureaucratization policies in the economic field set by the Government. The first deregulation package was set on June 1, 1983, known as Pakjun 1983. With the issuance of the policy, banks obtained freedom in determining the amount of credit given in accordance with public funds that could be collected. Alam (2011) added that state banks were given the freedom to determine their own interest rates, both in funds and credit interest rates. The policy aims to enable banks to finance their loans as much as possible with public savings funds and reduce banks' dependence on KLBI (Bank Indonesia Liquidation Liquidity).

Yovin (2013) explained that efforts to encourage the emergence of new products is needed in raising funds from the public. Besides that, healthy competition among banks is also needed as one of the elements driving efficiency improvements. For this purpose, on October 27, 1988 the Government issued the October 1988 Policy Package known

as the 1988 Pakto. With the policy summarized in the 1988 Pakto, the banking deregulation policy developed into a very broad deregulation because it included institutional aspects (BI, 2007).

The government reopens the licensing of the establishment of a new national private bank with a minimum paid-up capital of Rp10 billion and a rural bank (BPR) with a minimum paid-up capital of Rp50 million. The licenses had previously been frozen in 1971 and 1973 respectively. Thus, the requirements for being appointed as a foreign exchange bank and the opening of sub-branch offices and sub-branch offices that had previously been linked to the merger in this provision were no longer valid. The issuance of new bank business licenses that had been stopped since 1971 was reopened by Pakto 88.

Likewise, the permit to open a branch office or the establishment of an RB is made easier with the lighter capital requirements. An ease that was previously never felt by the banking world. One of the fundamental provisions in Pakto 88 is licensing for foreign exchange banks which only require the level of health and assets of banks to have reached a minimum of Rp 100 million. However, Pakto 88 also has side effects in the form abuse of freedom and convenience by bank managers. Along with the Pakto 88 policy, BI intensively started the development of secondary banks such as market banks, village banks, and village credit agencies.

Then the village work bank is converted into a Rural Bank (BPR) (Abustan, 2009). The aim of developing the BPR is to expand the reach of financing assistance to encourage economic improvement, especially in rural areas, in addition to modernizing the rural financial system. Entering the 1990s, BI issued the February 1991 Policy Package which contained provisions requiring banks to be careful in their management. In 1992 the Banking Law was issued replacing Law No. 14/1967. Since then, there have been changes in the classification of types of banks, namely commercial banks and BPRs. The Banking Law of 1992 also stipulates various provisions concerning the prudence of bank management and imposition of sanctions for bank managers who carry

out deliberate actions that harm banks, such as not carrying out proper recording and reporting, as well as providing fictitious credit, with the threat of criminal penalties. In addition, the Banking Act of 1992 also gave broad authority to Bank Indonesia to carry out the supervisory function of banks. To provide a stronger legal basis for the principles of deregulation contained in policy packages that have been issued since 1983, Law No. 7 of 1992 concerning Banking was stipulated on March 25, 1992.

Based on Law No. 7 of 1992 rearranged the banking structure, scope of activities, terms of establishment, increased protection of public funds by applying the precautionary principle and fulfilling the requirements of the bank's soundness level, as well as increasing the professionalism of the perpetrators, with the Law also stipulated legal arrangements government banks, the basis of bank business activities based on the principle of profit sharing (sharia), as well as sanctions for criminal threats against those who violate banking provisions (Adhim, 2011).

e. Reformation Period: Monetary Crisis and Liquidation Assistance Bank Indonesia

As a result of the financial and monetary crisis in 1997, an increase in national banking debt which resulted in liquidation of 16 banks eventually shook the economy in Indonesia. During the crisis, the rescue of the national banking system was carried out in high intensity.

Dianasari (2014) explained that on September 3, 1997, the Government decided to: help banks that still have life expectancy; ordered the merger or sale of several banks to more capable banks; and revoke the permits of bank who have no life expectancy. Banks deemed feasible continue to be assisted by Bank Indonesia Liquidity Assistance. Based on Hanif's note (2012), this step continued with 16 banks declared as Banks in Liquidation (BDL), 4 banks declared as Banks Taken Over (BTO), 10 banks as Operation Frozen Banks (BBO) and 39 banks as Frozen Bank Business Activities Certain (BBKU). In addition, in the efforts to restore banks, the Government is strengthening capital

(recapitalization) of the 10 Regional Development Banks (BPD) and 9 commercial banks. Establishment of IBRA on January 26, 1998, identification of banks based on criteria for recapitalization at the end of 1998, takeover of banks by the government in May 1998 and freezing of bank operations in May and August 1998 and termination of certain banks' business activities on March 13, 1999 .

In accordance with the Joint Agreement between the Governor of BI and the Minister of Finance on February 6, 1999, the BLBI value agreed upon was IDR 144.5 trillion and BLBI was given to PT Bank Ekspor Impor Indonesia at IDR 20 trillion (BI, 2011). Regarding the BLBI amounting to Rp 144.5 trillion, the government issued three debt securities, namely Debt Letter No. SU001/MK/1998 of Rp. 80 trillion, No. SU-003/MK/1999 amounted to Rp. 64.5 trillion, and No. SU-004/MK/1999 amounting to Rp. 53.8 trillion. The provision of BLBI funds to banks experiencing liquidity difficulties in an emergency refers to the provisions of Article 32 paragraph (3) and General Explanation of Number III letter b of Law No. 13 of 1968 concerning the Central Bank. Kasmir (2008) added that, in the law, the role of BI as lender of last resort was affirmed. In addition to the implementation of this function, the provision of BLBI was also carried out to implement BI's commitment to assist the government in carrying out national macroeconomic policies. Amendment of Law No. 7 of 1992 concerning Banking Principles into Law No. 10 of 1998 concerning Banking, the licensing authority in the banking sector was transferred from the Minister of Finance to the Chairman of Bank Indonesia.

Naili (2013) explained, as a bank supervisory authority, during this crisis Bank Indonesia exercised its authority to overcome difficulties that endanger the business continuity of the bank. Amendment to Law No. 7 of 1992 concerning the Principles of Banking into Law No. 10 of 1998 concerning Banking, the role of Bank Indonesia in banking policy experienced a drastic change. These changes, among others, regulate (Munir, 2012):

1. The transfer of licensing authority in the banking sector from the Minister of Finance to the Head of Bank Indonesia.
2. Ownership of banks by foreign parties is not limited but still takes into account the principle of partnership.
3. Development of a bank based on sharia.
4. Changes to the bank's confidential coverage that originally included the assets and liabilities sides of the bank's balance sheet, became the depositors and their deposits
5. Establishment of deposit insurance institutions (LPS) and
6. Establishment of a special temporary body in the context of banking restructuring.

In 1991 the Bank Muamalat Indonesia (BMI) stood as the only commercial bank that carried out business activities based on profit sharing principles. The introduction of banks based on the principle of profit sharing in positive law is through Law Number 7 of 1992 concerning Banking and Government Regulation Number 72 of 1992 concerning Banks Based on Profit Sharing Principles. Thus since 1992 the Indonesian banking industry is technically juridically familiar with the term Bank Based on the Profit Sharing Principle (Ningtyas, 2013).

Fayed (2013) explained, on the other hand we have known that Islamic banks in their operations are not solely based on the principle of profit sharing, but that there are other traditional Islamic contracts that can be implemented in the intended interest free bank practice. Traditional Islamic contracts or often referred to as sharia principles are instruments that replace conventional systems in the form of interest (usury), uncertainty (garar), gambling (maisyr), and ba'il which are elements that are prohibited in Islam (Hussein, 2012) .

Based on this paradigm, as well as the existence of empirical reality that shows that many conventional banks are unable to survive when the financial and monetary crisis hit, it encourages the government to amend Law Number 7 of 1992. Amendments to some of the contents of the Law Number 7 of 1992 set forth in Law Number 10 of 1998. This law is what reinforces the existence of Islamic banking in Indonesia.

f. Reform Period: Modern Banking System

Iqbal (2005) explains that, after the economic crisis followed by the fall of the new order government, the banking system began to study the loosening of the previous banking system by carrying out strict supervision which also involved funders from the International Monetary Fund, so that IBRA was formed. National Bank Restructuring) based on Presidential Decree Number 27 of 1998 concerning Establishment of IBRA. This institution was formed with the main task of banking restructuring, the settlement of problem assets and seeking to return state funds channeled to the banking sector. Because of its unsatisfactory performance, during the reign of President Megawati Soekarnoputri, this institution was dissolved on 27 February 2004 based on Presidential Decree No. 15 Year 2004 concerning Termination of Duties and Dissolution of IBRA (Setyowati, 2004).

Setyowati (2004) also added that the President wanted to appoint Finance Minister Boediono as Chairperson of the Indonesian Banking Restructuring Agency Team through Presidential Decree No. 16 of 2004 concerning the Establishment of IBRA's Delivery Team. Keppres is one of a number of legal bases issued by the president relating to the dissolution of IBRA. Asset Management Company (Persero) ("PPA") was established by the Government on February 27, 2004 through Government Regulation No. 10 of 2004 to carry out asset management of the former Indonesian Bank Restructuring Agency ("IBRA") which is not a legal person. In carrying out these management tasks, the Minister of Finance of the Republic of Indonesia and the Managing Director of the PPA signed the Asset Management Agreement dated March 24, 2004 for a period of five years and can subsequently be extended to each one year period (Manurung, 2004).

Through Government Regulation No. 61 of 2008 dated September 4, 2008. In accordance with the mandate of Law No. 23 of 1999 concerning Bank Indonesia, one of the tasks of Bank Indonesia is to regulate and supervise banks. The scope of this task includes setting

rules, granting and revoking permits on certain institutions or business activities of banks, carrying out supervision of banks, and imposing sanctions on banks in accordance with the provisions of the prevailing laws. According to Ariff (2006).

In addition to Bank Indonesia, there are also several institutions that oversee banks but with limited scope, namely:

1. The Supreme Audit Agency has the duty to supervise government-owned banks.
2. Bapepam has the authority to supervise banks that have gone public.
3. The Financial Transaction Reports and Analysis Center (PPATK) which was formed in 2002 (based on Law No. 15 of 2002 as amended by Act No. 25 of 2003 concerning Money Laundering) has the authority to request and receive reports from Providers of Financial Services and conduct audits of Financial Service Providers regarding compliance with obligations in accordance with the provisions of this Law and the reporting guidelines regarding financial transactions.
4. The Deposit Insurance Corporation (LPS) has the authority to obtain customer deposit data and bank financial statements and verify and confirm data in order to formulate and establish policies for the implementation of deposit guarantees and carry out deposit guarantees. 23 of 1999 concerning Bank Indonesia, one of the tasks of Bank Indonesia is to regulate and supervise banks.

During this period the banking system was strengthened by:

Table 3 Efforts to strengthen banking system

Infracstructure improvements	Good corporate governance application	Improvement of Organizing and Supervising
Firmness of service authority institution's competency	Feasibility and compliance screening of controlling shareholders, administrators, and executive officers	Firmness of sanctions for impropriety and impropriety
The assurance of skim of deposit guarantee	The requirement for a Compliance Director at the bank	Formation of cooperation in the framework of Law Enforcement
The assurance of financing sources for possible systemic problems		Implementation of International Standards in a bank supervision system
Development of BPR and Sharia Bank. Market segment for investment of both bank type is more resistant for turnover		

Source: Author's data

To realize a stable banking structure continuously, Bank Indonesia coordinates with the government in designing the AP). In the API scenario, banks are required to strengthen their capital in accordance with their operational scope (Fayed, 2013).

The wider the scope of operations, the greater also the required capital. Thus the bank small banks that have been vulnerable to turmoil so far pushed to become big, merged with other banks, taken over by another bank or dropped to BPR. In this scenario, the bank's operational scope is divided into 4 criteria, each Bank with Limited Business Activities, Focus Bank, National Bank and International Bank. The transfer of supervision of financial services to the Financial Services Authority

(OJK), which was formed based on Law Number 21 of 2011 which functions to organize an integrated regulation and supervision system for all activities within the financial services sector.

The Financial Services Authority, hereinafter referred to as OJK, is an independent institution that is free from interference from other parties, which has the functions, duties and authority to regulate, supervise, examine and investigate. OJK was established to replace the role of Bapepam-LK.

2.2 Competition between Commercial Banks in Indonesia

The increase in banking competition in Indonesia actually began since the openness of Indonesian banking, which was initiated with the issuance of a policy package on June 1, 1983 (PAKJUN) with the aim of modernizing the banking and then continued with the October package (PAKTO) on October 27, 1988, which facilitated licensing for the establishment of a new bank, including the opening of a branch office. At that time, with only Rp10 billion in funds, investors were able to establish a new bank (Deni and Djoni, 2004), and this led to a significant increase in the number of banks.

An increase in the number of banks has the potential to encourage banking sector businesses to become more competitive and improve banking efficiency and health. But for Indonesian banks, most private banks in the pre-crisis period were owned by big businessmen. As a result, when the business requires large funding, they tend to mobilize public funds through their banks for their business interests. This means that the aim of the Pakto 88 issuance was originally intended to channel public funds to the community, shifting to channeling to the group so that potential violations of the Legal Lending Limit (BMPK) emerged, (Deni and Djoni, 2004). This condition weakened the banking industry's infrastructure; as a result when international financial markets were turbulent, which began with the exchange rate crisis in Asian countries, Indonesian banks were unable to survive. This condition resulted in an increase in the crisis of confidence in the

rupiah and national banking, especially after the revocation of 16 bank business licenses in November 1997.

The government took the International Monetary Fund (IMF) to resolve the crisis, but the policies imposed by the IMF in the form of tightening liquidity actually made Indonesia's condition worse. Furthermore, the government and central bank try to implement a comprehensive stabilization and reform program to strengthen the national financial system and at the same time to restore public trust.

In 1999, the Act (Act) No. 23 of 1999 concerning Bank Indonesia was issued emphasizing that Bank Indonesia (BI) has a more focused goal of achieving and maintaining the stability of the rupiah, which is a precondition for sustainable economic growth. In the next few years, Bank Indonesia issued the Indonesian Banking Architecture (API) as the basic framework of Indonesia's comprehensive banking system. The API is expected to provide direction, form and order in the banking industry for the next five to ten years (BI, 2007, Indonesian Banking Architecture).

After the emergence of the API, which was supported by the strengthening of the bank's capital structure, it was hoped that Indonesian banks would become more stable and able to function as intermediary institutions. Stability will result in stronger national banking and eventually be able to compete with foreign banks in international markets⁴. Competition, which encourages increased competitiveness, is the main foundation of the process of strengthening national banking. Therefore, changes in the level of competition between banks will also change the behavior of banks in doing business.

Several previous studies have tried to examine banking competition in Indonesia, including Claessen and Laeven (2004) which estimate the level of competition in 50 countries including Indonesia using the Panzar-Rosse method during the period 1994-2001. From the study, it is stated that the structure of the Indonesian banking industry belongs to

the category monopolistic competition⁵. The results of this study were also supported by Setyowati (2004) who concluded that the overall Indonesian banking situation was monopolistic competition.

Regarding the implementation of the Indonesian Banking Architecture (API), the interesting question that arises is how does the API influence the level of stability and competition of the Indonesian banking industry? This research question will be answered in this study.

Fayed (2013) states that the banking market has several characteristics, among others, first, the presence of more than one credit provider, in this case the bank, in one area; both relationships between bankers and borrowers (debtors) are built based on experiences related to prior credit disbursement; third, large volume credit borrowers will get more credit offers while small borrowers face very limited supply; fourth, there are obstacles to the entry of new players that show a tendency to maintain monopoly or oligopoly conditions in order to gain positive benefits in the long run; and fifth, bankers' actions or decisions generally correlate with each other which is often referred to as agreement, mutual assistance, reduction of unhealthy competition, coordination, and so on. The reason for this collusion is the loss that occurs when competing with each other can be replaced by the profit obtained after the agreement is reached.

Fayed (2013) argues that competition in the banking industry is not perfect competition but a monopoly which is then supplemented by collusion to regulate price and non-price competition. Setyowati (2004) supports Chandler's statement by stating that banks are unlikely to be in a situation that is truly competitive because in a situation of new capital competition threatened to go bankrupt and this will endanger the economy macro because the collapse of a bank can spread to other banks (contagion effect).

Competition between banks can occur due to the struggle for productive resources, for example in deposits, savings, and credit distribution which are sources of income. Non-price interbank

competition can take the form of prizes and promotions to attract as many customers as possible. The competition can also take the form of new products and types of services supported by technological developments that can reduce production and distribution costs.

Several studies have concluded that the banking market is more concentrated and has a low level of competition, has a buffer in the face of vulnerability; this makes banking more stable. On the other hand, this condition also provides excessive risk taking incentives.

There are two opposing views about the relationship between the level of high banking competition and banking health; the first traditional view that states that high banking competition will increase credit supply for companies in need. This opinion is also supported by Claessens and Laeven (2003) who found that high competition in the financial sector can encourage increased production efficiency, financial product quality, and level of innovation. Increased competition is also expected to reduce the cost of intermediation services to be more efficient because the time needed to manage credit is much shorter and ultimately will increase bank income (Setyowati (2004). Conversely, high interest rates will reduce investment for research and development, so innovation will be hampered and company productivity will eventually decline, competitive banking markets will use their own power to reduce weak banks while encouraging the existence of healthy banks.

Contrary to the first view above, the second view states that competition actually has a negative impact on new companies and the future of the banking industry because borrowers face an increasing supply of credit when the banking competition increases. This model is based on the idea that competition will increase moral hazard and adverse selection problems from the borrower's side. When competition between banks increases, companies increasingly have a choice of banks or creditors. The bank's efforts to select prospective borrowers will decrease when the number of banks increases.

2.3 Summary

- 'Bank' comes from the Italian *banque* or *banca* which means bench. The bankers in Florence during the Renaissance did their transactions by sitting at a money exchange table, in contrast to the work of most people who did not allow them to sit down while working.
- The development of the original trade only in mainland Europe finally spread to West Asia. In contrast, the development of banking in the new British land began in the 16th century.
- The presence of the First banking institution in Indonesia was inseparable from the colonial Dutch East Indies re-Oest-Indische Compagnie (VOC) in Indonesia, the VOC which was the holding company of Dutch trading companies, they established their authority in Batavia in 1619.
- The Supersemar incident on March 11, 1966 and the dissolution of the PKI on March 12, 1966 was the milestone in the birth of the new order. Furthermore, on July 25, 1966 an Ampera Cabinet was formed to replace the Dwikora Cabinet.
- After the emergence of the API, which is supported by the strengthening of the bank's capital structure, it is expected that Indonesian banks will become more stable and able to function as intermediary institutions.
- Competition between banks can occur due to the struggle for productive resources, for example deposits, savings, and credit distribution which are sources of income.
- Competition in the banking industry is not perfect competition but a monopoly which is then supplemented by collusion to regulate price and non-price competition.
- The banking market is more concentrated and has a low level of competition, has a buffer in the face of vulnerability; this makes

banking more stable. On the other hand, this condition also provides excessive risk taking incentives.

CHAPTER 3

SHARIA BANKING PERSPECTIVE IN INDONESIA

3.1 History of Islamic Banking in Indonesia

Banking is the most important financial institution for the development of a country. This is because the function of the banking is as a financial intermediary institution as stated in Article 1 No. 2 Act No. 10 of 1998 concerning amendments to Act No. 7 of 1992 namely that banks are business entities that collect funds from the public in the form of deposits and channel it to the public in the form of credit and/or other forms in order to improve the standard of living of the people (Kasmir, 2012: 24).

Islamic banks in general is a bank whose operations are based on Islamic sharia principles. Other terms used to refer to Islamic bank entities other than Islamic banks themselves, namely Interest-Free Banks, Lariba Banks, and Sharia Banks. Indonesia is juridically technically called an Islamic bank using the term "Islamic Bank", or a complete one called "Bank Based on Sharia Principles" (Anshori, 2008).

Based on Law No. 21 of 2008 concerning Islamic banking is everything that concerns Islamic banks and Sharia Business Units (UUS), including institutions, business activities and ways and processes in carry out its business activities. From the research conducted by Lo and Leow (2014), Islamic banking is defined as a banking system based on sharia law with the main principle of doing business in accordance with the distribution of profit and loss and the prohibition of productive and beneficial interest. Mohamad, Burhan and Taswan (2013) in their research also concluded that the Islamic banking system is a system based on sharia principles that do not contain elements of riba (faedah), uncertainty (gharar), risk and speculation in addition to adhering to the principle of justice.

Types of banks according to Article 1 Act No. 21 of 2008 are as follows:

1. Sharia Commercial Banks are Islamic Banks which in their activities provide services in payment traffic.
2. The Sharia Business Unit is a work unit of the head office of a Conventional Commercial Bank that functions as the parent office of an office or unit that conducts business activities based on sharia principles, or a work unit at a branch office of a bank domiciled abroad that conducts business activities conventional function as the main office of sharia sub-branch offices and / or sharia units.

The results of Rozalinda's research (2014) describe one of the similarities of Islamic banks and conventional banks are both seeking profit. However, in its operations Islamic banking based on the principle of profit sharing provides an alternative banking system that is mutually beneficial for the community and parties banks, as well as highlighting aspects of fairness in transactions, ethical investments, promoting the values of togetherness and brotherhood in operation. In carrying out its operations, there are seven characteristics of sharia banking which are published and circulated in the form of a booklet "Sharia Bank for All of Us" (Saeed, 2004: 66). These seven characteristics include:

1. Universal, Considering that Islamic banks apply to everyone regardless of differences in economic abilities or religious differences.
2. Fair, Giving something only to those who are entitled and treating things according to their position and forbidding the existence of elements of maysir (elements of speculation or chancy), obscurity (gharar), illegitimacy, usury and taking profit margins mutually agreed between the bank and the customer.
3. Transparent, in its activities Islamic banks are very open to all levels of society.

4. Balanced, Developing the financial sector through sharia banking activities that include the development of the real sector and Small and Medium Enterprises (MSMEs).
5. *Maslahat*, Useful and good for all aspects of life.
6. Variative, products vary from Hajj and Umrah savings, general savings, demand deposits, deposits, profit-based financing, buying and selling, to custodian services, transfer services and payment services (debit cards, sharia charge)
7. Facilities, Receipt and distribution of zakat, infaq, alms, endowments, benevolence funds (qard), have Automated Teller Machines (ATMs), mobile banking, internet banking and interconnection between Islamic banks.

The characteristics of the Islamic banking system that operates based on the principle of profit sharing provides an alternative banking system that is mutually beneficial for customers and banks, and provides aspects of fairness in transactions, ethical investments, promoting values of togetherness and brotherhood in production, and avoiding speculative activities in transactions finance.

The concept is a term that consists of one or more words that describe a symptom or express a certain idea (idea) (Hasan, 2002: 17). There are 3 basic concepts in Islamic banking transactions, including:

1. Efficiency

Referring to the principle of mutual help to endeavor, with the aim of achieving as much profit as possible and the costs incurred appropriately.

2. Justice

Referring to a relationship that does not tyrannize (persecute), mutual sincerity expresses between the parties involved with a fair agreement about the proportion of profit sharing, both profit and loss.

3. The truth

Referring to the principle of offering mutual assistance and advice to increase productivity.

There are five transactions commonly practiced in Islamic banking transactions including:

1. Transactions that do not contain usury.

Mutasowifin's research (2015) explains the concept of usury from Islamic and non-Islamic circles.

a. The concept of usury in the Islamic community:

“Those who consume interest cannot stand [on the Day of Resurrection] except as one stands who is being beaten by Satan into insanity. That it because they say, “Trade is [just] like interest.” But Allah has permitted trade and has forbidden interest. So whoever has received an admonition from his Lord and desists may have what is past, and his affair rests with Allah. But whoever returns to [dealing in interest or usury] – those are the companions of the Fire; they will abide eternally therein.” (Al Baqarah: 275)

b. The concept of usury among Jews:

In the Book of Exodus / Exodus Article 22 Verse 25, "If you borrow money to one of my people, the poor among you, then do not be a debt collector against him; do not burden your interest on money."

c. The concept of usury in Christianity

The ban of usury on Kisten in Luke 6: 34-35, "If you lend something to someone because you expect to receive something from him, what is your attitude? Sinners even lend to sinners so they can receive as much. But you, pardon your musushes and do good to them and lend it with no expecting a reward, your wages will be great and you will

become the sons of the Most High God, for he is good toward those who do not know the grateful to the wicked. "

In terms of theory, Islamic banking uses two concepts (two tier *mudharabah*) or also called second level *mudharabah*. It is an Islamic bank that functions and operates as an investment intermediary institute that uses *mudharabah* agreements on financing (liabilities) and financing (assets) activities, and also acts as investment agents that bring together investment parties and entrepreneurs (Dahlan, 2014). The concept of *mudharabah* and *musyarakah* as a profit sharing system in the face of uncertainty is one of the fundamental principles of Islamic economics (Saeed, 2004: 76).

1. A transaction that is intended to own goods by way of sale and purchase (*murabahah*).
2. Transactions intended to obtain services by way of rent (*ijarah*).
3. Transactions intended to earn working capital by way of profit sharing (*mudharabah*).
4. Transaction of deposits, savings, demand deposits is the profit sharing (*mudharabah*) and deposit transactions (*wadi'ah*).

According to Rozalinda (2014) basically, Islamic banking entities in Indonesia have been started since 1983 with the issuance of the December 1983 Package (Pakdes 83) which contains a number of regulation in the banking sector, where one of them is a regulation that allows banks to give credit at 0% interest (zero interest). The

development was followed by a series of policies in the banking sector by the Minister of Finance Radius Prawiro as stated in the October 1988 Package (Pakto 88).

Anshori (2008) explained that the Pakto 88 was essentially a banking deregulation that provided facilities for the establishment of new banks, so that the banking industry at that time experienced very rapid growth. Only in 1991 stood Bank Muamalat Indonesia (BMI) as the only commercial bank carrying out business activities based on profit sharing principles. The introduction of banks based on the principle of profit sharing in positive law is through Law Number 7 of 1992 concerning Banking and Government Regulation Number 72 of 1992 concerning Banks based on profit sharing principles (Lo and Leow, 2014).

Thus since 1992 the Indonesian banking industry is technically juridical and has known the term Bank Based on the Profit Sharing Principles. Rozalinda (2014) explained, on the other hand we have known that Islamic banks in their operations are not solely based on the principle of profit sharing, but that there are other traditional Islamic contracts that can be implemented in the interest-free bank practice.

Rozalinda (2014) adds that his subordinates of traditional Islamic contracts or what is often referred to as sharia principles are instruments that replace conventional systems in the form of interest (usury), uncertainty (*garar*), gambling (*maisyir*), and *ba'il* which are elements which are prohibited in Islam. Based on this paradigm, as well as the existence of empirical reality that shows that many

conventional banks are unable to survive when the financial and monetary crisis hit, it encourages the government to amend Law Number 7 of 1992. Amendments to some of the contents of the Law Number 7 of 1992 set forth in Law Number 10 of 1998. This law reinforces the existence of Islamic banking in Indonesia (Lo and Leow, 2014). The era of Law Number 10 of 1998, the banking law policy in Indonesia adheres to a dual banking system.

This policy essentially provides an opportunity for conventional commercial banks to provide sharia services through an Islamic window mechanism by first forming a Sharia Business Unit (UUS). As a result, after this law raises many conventional banks that participate fairly in providing sharia services to their customers. Sharia service provision is made easier by the introduction of the concept of office channeling in Bank Indonesia Regulation (PBI) Number 8/3/PBI/2006. Office the core channeling is that to provide sharia services for Commercial Banks Conventional who already have a UUS at their head office, no longer need to open a new Branch Office/Sub-Branch Office but simply open a sharia counter in a conventional Branch Office / Sub-Branch Office.

This of course will save bank finances, because they no longer need new infrastructure such as buildings, office equipment, employees, and information technology. Rozalinda (2014) explains that, Islamic Commercial Banks (BUS) other than BMI, after Law Number 10 of 1998 is the establishment of Bank Syariah Mandiri which is the result of acquisition and conversion of PT. Bank Susila Bakti by PT. Bank Mandiri (Persero) "Tbk". In addition Bank Mega has also

carried out the same process by forming PT. Mega Syariah Bank. While other banks, such as PT. Bank Rakyat Indonesia (Persero) "Tbk", PT. Bank Negara Indonesia (Persero) (Sulaiman, 2014).

"Tbk", Bank Permata, and so on in providing sharia services are still within the framework of UUS. Business activities that can be carried out by BUS are wider than UUS from conventional banks. As for business activities that can only be done by BUS according to Lo and Leow (2014), namely:

1. guarantee the issuance of securities;
2. safekeeping for the benefit of others;
3. become trustee;
4. capital participation;
5. founders and managers of pension funds;
6. issuing, offering and trading sharia long-term securities.

On the product side, Islamic banking is based on a number of fatwas issued by the National Sharia Council-Indonesian Ulema Council (DSN-MUI), including Fatwa No. 04/DSN-MUI/IV/2000 concerning *Murabahah*, Fatwa No. 07/DSN-MUI/IV/2000 concerning *Mudharabah* Financing, Fatwa No. 08/DSN-MUI/IV/2000 concerning *Musyarakah* Financing (Sulaiman, 2014).

Rozalinda (2014) explained that the content material from the fatwa issued by DSN-MUI later became the content material in various PBIs. This is clearly seen in PBI No. 7/46/PBI/2005 concerning Agreement on Collection and Distribution of Funds for Banks Implementing Sharia-Based Business Activities (Sulaiman, 2014).

This PBI is currently revoked with PBI No. 9/19/PBI/2007 concerning Implementation of Sharia Principles in Fund Collection Activities and Distribution of Funds and Sharia Bank Services, as amended by PBI No. 10/16/PBI/2008. In PBI No. 9/19/2007 stated that the fulfillment of Sharia Principles in fund raising activities, distribution of funds and services, was carried out as follows:

1. in fund raising activities by using, among others, *Wadi'ah* and *Mudharabah* Contracts;
2. in the distribution of funds in the form of Financing by using, among others, *Mudharabah*, *Musyarakah* Contracts, *Murabahah*, *Salam*, *Istishna* ', *Ijarah*, *Ijarah Muntahiya Bittamlik* and *Qardh*; and
3. in service activities by using, among others, *Kafalah*, *Hawalah*, and *Sharf* Contracts. According to Wirdyaningsih, et al., up to the issuance of Law Number 10 of 1998, Indonesia has passed two stages of coaching, namely the "introductory stage" (introduction) which is marked by the enactment of Law Number 7 In 1992, and the "recognition stage" which was marked by the enactment of Law Number 10 of 1998. The next desired stage was "Stage of purification" which will later be marked by the enactment of a law specifically regulating Islamic banking.

According to Rozalinda (2014), the current "purification stage" was in sight, because on June 17, 2008 it had been Sharia Banking Act was enacted with the enactment in the State Gazette conducted on July 16, 2008, namely Law Number 21 of 2008 concerning Sharia

Banking. The law is intended to introduce some new content and new legal institutions aimed at supporting the implementation of national development in order to improve justice, togetherness and equal distribution of people's welfare. The realization of the intended purpose is realized in the function of Islamic banks and UUS (Saeed, 2004: 45), namely that:

1. Islamic Banks and UUS are obliged to carry out the function of collecting and distributing public funds;
2. Islamic Banks and UUS can carry out social functions in the form of *baitul mal*, namely receiving funds derived from *zakat*, *infaq*, alms, grants, or other social funds and channeling them to *zakat* management organizations;
3. Islamic Banks and UUS can collect social funds derived from money *waqf* and channel it to managers *waqf* (*nazhir*) according to the will of the *waqf* (*wakif*). The implementation of social functions is based on the relevant laws and regulations, namely Law Number 38 of 1999 concerning Management of *Zakat* and Law Number 41 of 2004 concerning *Waqf*. This shows that Islamic banking acts as a financial and social intermediaries institution. Institutionally, new issues introduced in the Sharia Banking Law are provisions concerning separation (spin-off) against UUS in Conventional Commercial Banks to become a BUS, either voluntarily or because they are required to have certain requirements are met (Lo and Leow, 2014).

Separation is the separation of business from the Bank into two or more business entities, in accordance with the provisions of the legislation (Sulaiman, 2014). The said statutory regulations, namely Law Number 40 Year 2007 concerning Limited Liability Companies and their implementing regulations, as well as special provisions in the banking sector in the form of PBI. But until now the operational provisions referred to do not yet exist, so that it will hamper the implementation of spin-off for banks that want to implement it, including PT. Bank Rakyat Indonesia (Persero) "Tbk".

The formation of BUS through the separation of UUS is a breakthrough in order to better "legitimize" Islamic banks. The existence of a BUS that is juridically independent will further optimize the services of Islamic banking so that it is expected that the operations of Islamic banks truly fulfill the principle of prohibition of mixing between halal and haram.

In the context of the preparation of the PBI, whose content was derived from the Indonesian Ulama Council Fatwa, Bank Indonesia established a sharia banking committee. The procedure for the formation, membership and duties of the sharia banking committee will be regulated by PBI (Lo and Leow, 2014). The existence of these provisions in the opinion of the author will bring up a synergy between the National Sharia Council and Bank Indonesia as the holder of the national banking authority (Sulaiman, 2014). PBI which is specifically the implementing regulation of Law Number 21 of 2008 concerning Sharia Banking and has been promulgated to date, namely:

1. PBI No. 10/16/PBI/2008 concerning Amendments to PBI No. 9/19/PBI/2007 concerning Implementation of Sharia Principles in Fund Collection and Fund Distribution Activities and Sharia Bank Services.
2. PBI No. 10/17/PBI/2008 concerning Sharia Bank Products and Sharia Business Units.
3. PBI No. 10/18/PBI/2008 concerning Financing Restructuring for Islamic Banks.
4. PBI No. 10/23/PBI/2008 concerning the Second Amendment to PBI No. 6/21/PBI/2004 concerning Statutory Reserves in Rupiah and Foreign Currency for Commercial Banks Conducting Business Activities Based on Sharia Principles.
5. PBI No. 10/24/PBI/2008 concerning the Second Amendment to PBI No. 8/21/PBI/2006 concerning Asset Quality Rating for Commercial Banks Conducting Business Activities Based on Sharia Principles.
6. PBI No. 10/32/PBI/2008 concerning the Sharia Banking Committee. Law Number 21 of 2008 also provides opportunities for foreign nationals and/or foreign legal entities to establish or own a BUS in partnership with Indonesian citizens and/or Indonesian legal entities.

This is proof that Islamic banks are open sectors for foreign investors who intend to establish or have a joint venture BUS, so that the provisions contained in Law Number 25 Year 2007 concerning Investment and its implementing regulations need to be considered and implemented by related parties. Based on Islamic Banking Statistics issued by Bank Indonesia in November 2008 the

Networking Office Network consists of 4 (four) Sharia Commercial Banks, namely PT. Bank Muamalat Indonesia, PT. Bank Syariah Mandiri, PT. Bank Syariah Mega Indonesia, and PT. BRI Islamic Bank. Sharia Business Units (UUS) of conventional banks that provide sharia services amount to 27 and Sharia Rural Banks amount to 128 (Sulaiman, 2014).

Seeing the legal developments that sustain the Islamic banking industry in Indonesia lasts so rapidly, it will have implications both positive and negative (Saeed, 2004, p. 99). For this reason, there needs to be readiness of business people in the banking sector to prepare human resources who have the competence and understanding related to aspects of sharia banking concerning the aspects of fiqh and positive legal aspects that surround it, as well as accuracy in the development of Islamic banking products (Sulaiman, 2014).

3.2 Sharia Banking Inter Competition in Indonesia

Banking business is a service business that is based on the principle of trust so that the problem of service quality is a very decisive factor in business success. Service quality is a form of consumer assessment of the level of perceived service with the expected service level. Getting tighter competition in the banking industry encourages the banking industry to quickly adjust to the development of the surrounding community. This was marked by the increasingly widespread expansion of foreign banks trying to enter the banking market in Indonesia. The banking industry is currently competing to improve services to customers, by providing facilities

that make it easier for customers to conduct financial transactions (Infobank, April 2008).

Strict competition between Islamic banks and conventional banks increases customer standards for banking services. So that the approach to using Islamic sentiment is no longer effective. People who are accustomed to conventional systems and have the image that conventional bank services are better than Islamic banks are a challenge for Islamic banks to find a more appropriate strategy to maintain customers and increase market share. The emergence of the concept of Islamic banks in Indonesia is made possible through the National Banking Act No. 7 of 1992 which states that banks are possible with a profit sharing system which ultimately inspires the birth of Bank Muamalat Indonesia. In line with the emergence of a monetary crisis which eventually became an economic crisis in Indonesia, which was marked by the number of liquidated banks. On the other hand, Bank Muamalat Indonesia still maintains its operations.

The amendment of Law No.7 of 1992 to Law No. 10 of 1998 provide stimulus for the emergence of Islamic banking in Indonesia. Because in the new law it is stated that it is possible for banks to operate in two systems, namely conventional banks and Islamic banks (dual banking system). As of June 17, 2008, the Indonesian Islamic banking industry officially entered a new era. The Sharia Banking Bill, which has entered the House of Representatives since mid-2005 as a bill on the initiative of the House of Representatives, has been ratified so that Indonesia is now officially in possession of

Islamic banking regulations, namely Law Number 21 Year of Islamic Banking (Yusuf Wibisono, 1999).

Conceptualization and measurement of service quality perceptions is one of the most contentious and controversial contemporary topics in the literature-marketing services (Brady and Cronin, 2001; Lang, 2016; Zins, 2001; Rust and Oliver, 2000). Because services are intangible, consumers value quality subjectively. As perceived quality services / products have been referred to as "difficult to understand" (Parasuraman et al., 1985; Smith, 1999), and various studies assume that this construct is still considered "unresolved" (Carhuana et al. 2000).

Measurement of the quality of service by Lang (2016) in his explanatory research, explained the service and the determining factors. In this study it was defined that the quality of service as a degree of incompatibility between the normative expectations of customers on services and customer perceptions of service performance received. From this research, SERVQUAL instrument is used, which is a scale consisting of 22 items to measure the quality of service covered in five dimensions, namely: reliability, responsiveness, assurance, empathy and tangibles. The results of his research show that the reliability dimensions are most important in determining customer satisfaction. Then followed by dimensions of responsiveness, assurance, empathy, and tangibles.

Research Lang (2016) managed to identify the profile and banking habits of sharia bank customers and their awareness, use, perceived importance and level of satisfaction with current products and

services provided by two leading Islamic banks operating in Bahrain. Lang (2016) develops attributes that affect customer behavior including: availability of credit, advice from relatives and recommendations, friends, advice and recommendations, convenient location, various service banks, quality of service, availability of ATMs, adequate bank hours, investment, friendliness personnel, understanding financial needs, special services for women, and bank names.

Islamic banking in Indonesia has entered its twentieth year, but in terms of market share it is still relatively small (less than 5%). This condition is certainly contradictory, considering that the majority of Indonesia's population are Muslims. In comparison, sharia bank customers in Singapore account for 50% of the non-Muslim group. The slowness of Islamic banks increasing market share cannot be separated from several things.

First, the rationality of Muslims in economics, where the pursuit of material benefits is not too considerate of the illegitimate halal issue of usury. Second, public understanding of Islamic banks is still low. Third, there is no unanimous support from religious institutions such as Nahdatul Ulama and Muhammadiyah regarding the prohibition of interest as usury. Fourth, Islamic banks in Indonesia, face challenges where banks operate in mixed economic systems that are not supported by regulation because their supervision is still integrated with conventional banks.

So that a strategy for developing Islamic banking is needed in the face of conventional banking competition. Direction and Challenges

of Sharia Banking Development requires a policy in developing Islamic banking in the future. The following are Islamic banking policies:

1. Encouraging production,
2. Reducing the gap between the real sector and the financial sector,
3. Minimizing money concentration,
4. Encourage governance and reduce moral hazard,
5. Inclusive and sustainable economic growth.

President Susilo Bambang Yudhoyono (SBY) stated the Islamic finance industry has a number of advantages over conventional financing. First, the Islamic financing scheme can reduce the potential vulnerabilities and bubbles that cause the economic crisis. The profit sharing system makes no distance between the financial system and the real sector. Second, expanding financial inclusion, especially in financing small and medium enterprises (SMEs). In addition, Islamic financing is in the form of *zakat*, *infaq*, and alms can complement social protection. Third, Islamic banking can play a major role in infrastructure financing in the Master Plan for the Acceleration of Expansion of Indonesian Economic Development. The Sharia Banking Prospects and Challenges are as follows.

1. Welcoming the formation of the ASEAN Economic Community (MEA) in 2015.
2. Encouraging creative and efficient innovation in Islamic banking products.

3. Preparation of human resources in adequate quantity and quality.
4. Improving the quality of excellent service for customers to be competitive with other banks.
5. Optimal use of IT to encourage the creation of superior products.
6. SMEs sector financing services and other productive sectors to encourage economic growth and job creation.
7. Socialization, education and dissemination of economic ideas to the public more intensively and massively.
8. Increasing the number of equity investments to meet the regulatory requirements of Bank Indonesia.

Market structure is an important key to conventional patterns in the industrial economy. Market structure shows attributes that affect the nature of the competition process. Economists classify markets by focusing on the number of companies in the industry. Economically micro, market structure can be grouped into four forms of market structure. The four market structures are as follows: First, perfect competition, is a market structure characterized by a large number of buyers and sellers. Transactions of each individual (buyer and seller) are very small compared to total industrial output so they cannot influence the price of the product.

There is no product differentiation. Buyers and sellers individually act only as price takers. Information about the price and quality of the product is complete and free. There is freedom to enter and exit the market. No company or industry receives profit above normal in

the long run in a perfectly competitive market. Second, Monopoly, is a market structure characterized by the existence of a single producer. Product differentiation is very high, similar substitution items are not available. Very high restriction to get information about prices and product quality. Obstacles that are very difficult to enter the market due to economies of scale, patents, copyright, franchise, or other factors. A monopolist company can simultaneously determine the product price and the amount of output. For a monopoly it is possible to make a profit above normal, even in the long run.

Third, monopolistic competition, is a market structure that is very similar to perfect competition, but slightly differentiated from perfect competition because in monopolistic competition. This consumer knows the differences between products from different companies (different producers). Information about prices and quality of products is not free, but cheap.

The conditions are easy to enter and exit the market. Just as in perfect competition, in this monopolistic competition above normal profit can be obtained in the short term, while in the long run it only receives normal profit. Fourth, oligopoly is a market structure where there are only a small number of companies that produce almost all industrial output and have mutually influential decisions. Product differentiation can be high or low depending on conditions to enter and exit the market. There are restrictions to obtain information about product prices and quality and production costs are often confidential. Barriers to entry into the market are quite high because

of the economic scale, the amount of capital requirements, advertising costs, development research, and other factors.

There is a potential for producers to gain profit above normal, both in the short and long term. This form of market is the most common in reality and is currently the target of research, especially in the form of industrial economics. Basically, oligopoly covers a variety of conditions so that there is no single economic model for it, meaning that there is no general theory to discuss oligopoly theories. Many compiled special theories, which are possible applies to certain industries, while in other industries it does not apply. In microeconomic theory, the oligopoly media is divided into two types, namely;

First, non-joining (/non collusive oligopoly) oligopoly consists of Cournot models, Bertran models, Chamberlain models, Sweezy models and Stackelberg models. Secondly, collusive oligopoly which consists of cartels and price leadership. Of the four forms of market structure, the market is perfectly competitive and monopoly has a very important role. Effective competition can make the market system run well, while monopoly power often causes unbalanced performance. The monopoly structure is often distinguished into natural monopolies and non-natural monopolies.

Natural monopolies are usually related to the provision of public services such as drinking water, electricity, telephone gas and others. This natural monopoly process is an unavoidable process and the effect on balance is positive because it is able to improve welfare through price emphasis. Unlike the non-natural monopoly that

occurs because a collusive oligopoly structure can collectively have policies in regulating and determining prices.

3.3 Summary

- Article 1 No. 2 Act No. 10 of 1998 concerning amendments to Act No. 7 of 1992 namely that a bank is a business entity that collects funds from the public in the form of deposits and channels it to the public in the form of credit and / or other forms in order to improve the standard of living of the people.
- Based on Law No. 21 of 2008 concerning sharia banking is everything concerning Islamic banks and Sharia Business Units (UUS), including institutions, business activities and ways and processes in carrying out its business activities.
- Types of banks according to Article 1 of Law No. 21 years 2008 are as follows:
 - a) Sharia Commercial Banks are Islamic Banks which in their activities provide services in payment traffic.
 - b) The Sharia Business Unit is a work unit of the head office of a Conventional Commercial Bank that functions as the head office of an office or unit that conducts business activities based on sharia principles, or a work unit at a branch office of a bank domiciled overseas that conducts conventional business activities. Function as the main office of the sharia sub-branch office and / or sharia unit.

- Characteristics of the Islamic banking system that operates based on the principle of profit sharing provides an alternative banking system that is mutually beneficial for the customers and banks, and provides aspects of fairness in transactions, ethical investments, promoting values togetherness and brotherhood in production, and avoid speculative activities in financial transactions.
- The occurrence of amendments to Law No.7 of 1992 to Law No. 10 of 1998 increasingly provided the stimulus for the emergence of Islamic banking in Indonesia.
- Market structure is an important key to conventional patterns in the industrial economy.

CHAPTER 4

COMPETITION IN THE ASEAN ECONOMIC COMMUNITY ERA

4.1 ASEAN Economic Community

Syukriah (2013) stated that the ASEAN Economic Community (AEC) is a form of ASEAN economic integration in the free trade system between ASEAN countries. AEC is an ASEAN (ASEAN Community) community in the ASEAN Economic field or (ASEAN Economic). The AEC community which was launched in Bali in 2003 at the 9th ASEAN Summit, known as the Bali Concord II. The formation of the community was initiated by the ASEAN Heads of State after the 1997 economic crisis in the Southeast Asian region.

There are 4 pillars of AEC, namely:

1. The formation of a single market and production base

Namely: (1) free flow of goods; (2) Free of services; (3) Free investment; (4) Free of labor; (5) Free of capital flows; (6) Priority integration sectors; (7) Development of the sector of food agriculture forestry.

2. High competitive area.

Namely: (1) competition policy; (2) Consumer protection; (3) Construction of infrastructure; (4) Energy cooperation; (5) Taxation; (6) E-commerce.

3. Regions with equitable economic development

Namely: (1) Development of SMEs; (2) Narrowing the development gap between ASEAN countries.

4. Integration with the world economy.

Namely: (1) a coherent approach to external economic relations; (2) Increasing participation in global supply networks.

There are 4 things that must be anticipated in the MEA, namely:

1. The implementation of AEC has the potential to make Indonesia merely a supplier of energy and raw materials for the industrialization in the ASEAN region, so that the benefits derived from natural resource wealth are minimal.
2. Widespread deposit of trade in services in line with increased trade in goods.
3. The implementation of the AEC will also free up the flow of labor so that it must anticipate by preparing a strategy because of the potential for the influx of Foreign Workers (TKA).
4. The implementation of the AEC will encourage the entry of investment into Indonesia from outside ASEAN.

Based on information quoted from the Ministry of Trade, Republic of Indonesia, which was accessed on February 20, 2016 stated there was some benefits, opportunities and challenges in dealing MEA, including:

a. Benefits

- 1) ASEAN economic integrity will strengthen ASEAN's position in the world economic arena.
- 2) ASEAN economic integration increases ASEAN economic growth in general and Indonesia in particular.
- 3) ASEAN integration will improve the welfare of all ASEAN Member States.
- 4) AEC provides wider employment opportunities for skilled workers in Indonesia.
- 5) Increasing Indonesia's Gross Domestic Product (GDP) or Gross Added Value.
- 6) The Service Sector contributed around 47% to ASEAN GDP and 47.2% to Indonesia's GDP in 2012.

b. Opportunity

- 1) World potential market. The realization of MEA 2015 will place ASEAN as the third largest market area in the world which is supported by the third largest population (8% of the total world population) after China and India.
- 2) As an exporting country. Economic prospects that are good enough cause ASEAN to become an investment destination.
- 3) The destination country of the investor. This opportunity opens up opportunities to improve Indonesia's investment climate. Especially in launching domestic infrastructure programs.
- 4) Competitiveness. The liberalization of trade in ASEAN goods will ensure the smooth flow of goods for the supply of

raw materials and finished materials in the ASEAN region due to tariff and non-tariff barriers that no longer exist.

- 5) Open service sector. The service sectors that have been determined are tourism, health, aviation, and then will be followed by logistics.

c. Challenge

- 1) The rate of increase in exports and imports. The challenges faced by Indonesia are not only internal but also external, especially competition with ASEAN countries and other countries outside ASEAN such as China and India.
- 2) Inflation rate. Another challenge is Indonesia's inflation rate which is still relatively high if compared with other countries in the ASEAN counterpart.
- 3) The negative impact of wider capital flows. The freer flow of capital to support more efficient financial transactions is one of the sources of development financing, facilitating international trade, supporting the development of the financial sector. So that it can increase a country's economic growth.
- 4) The level of economic development. The level of economic development of ASEAN Member States is still diverse. The high level of failure is one of the problems in the region that is quite urgent solved so as not to impede the acceleration of the region in the face of MEA.

During the establishment of Islamic banks in Indonesia, financial institutions that use sharia principles have very promising

opportunities in the future. Antonio (2007, p. 227) suggests that there are several advantages and disadvantages of Islamic banking which are obstacles in the development of Islamic banking, namely:

1. Strength of Islamic banking

The strength of Islamic banks can be a great opportunity for the extension of Islamic banks in the face of competition in the market. The strength of the Islamic bank is as follows:

- 1) Large-scale modern sectors that depend on currency exchange rates, people's economic sectors and export production sectors which are based on domestic raw materials are important and efficient sectors for providing interest-free redemption. This is a great opportunity that must be utilized by Islamic banks. But in practice Islamic banks still need interference from community leaders to help in socializing to the public.
- 2) In concept, Islamic financial institutions have advantages compared to the principles of conventional financial institutions. Because there is no significant objection to the superiority of economic concepts Islam as a whole, or Islamic financial institutions in particular.
- 3) Very large Muslim population in Indonesia. These conditions provide opportunities for Islamic banks to go even better. But if wrong in perceiving people's behavior, then these opportunities and strengths can change into weaknesses and challenges that will be faced by Islamic banks.

- 4) Government support and legal provisions. Islamic banks are recognized by the existence of Law No. 1998 which allowed the operation of banks with sharia principles.
- 5) The influence of the global Islamic economic movement. Because the development of Islamic economy does not only occur in Indonesia, but simultaneously in a number of other countries in the world.
- 6) The operational foundation of Islamic banks is based on Islamic ethics. It means that all products and operational management from Islamic banks do not conflict with Islamic law.
- 7) Credit is easy to obtain. Because Islamic banks have simple and uncomplicated procedures.
- 8) The profit sharing system is the strength of Islamic banks because the system is fairer than the interest system.

2. Weaknesses in Islamic banking

Weaknesses here can also pose challenges or major problems that will be faced by Islamic banks. These weaknesses include the following:

- 1) Limited capital.
- 2) Inadequate human resources.
- 3) Islamic banks have difficulty placing their money when excess liquidity. Because Islamic banks do not save their funds in conventional banks.

- 4) Management of Islamic banks that are less professional. This is because Islamic banks are still relatively new in operating in Indonesia.
- 5) Greater risk, or higher uncertainty compared to conventional banks. Because the profit sharing system of Islamic banks is guided by real gains in the business world.
- 6) Limited operating networks, especially fellow Islamic banks.
- 7) For novice Islamic banks, difficulties in finding investors. Because many doubt whether prospective Islamic banking is promising.

Rozalinda (2014) in his research describes various challenges in the development of Islamic banking in Indonesia which include the following:

- 1) Insufficient knowledge of human resources in academic and intellectual tasks to formulate various Islamic economic thoughts. In addition, human resources that practically work in Islamic financial institutions do not yet fully possess the capacity that is truly Islamic. This is because the human resources available in the sharia institution are taken from conventional financial institutions.
- 2) Sharia-based financing patterns are only limited to written agreements not yet in substance. That is, in transactions that occur in new Islamic banks only at the stage of eliminating the element of usury by designing legitimate transactions, the contract has not touched the fundamental problem in people who need sharia financial institutions. Hayat (2014) in his

research also explained that the establishment of AEC for Islamic banking is a challenge as the prospect of the Islamic economic market in the global arena. Good those are short-term and long-term challenges.

Challenges of Islamic banking in the long run short are as follows:

- 1) Fulfillment of intellectual human resources gap, both in quantity and quality. Because labor is the controller of goods, services, investment and capital.
- 2) Innovation in developing competitive banking products and services based on community needs.
- 3) Continuing socialization and education to the community.

While the challenges of Islamic banking in the long term include:

1. There is a need for a legal framework that can be used as a backbone in solving comprehensive Islamic financial problems.
2. The existence of codification of products and regulatory standards nationally and globally as a bridge in the difference between *fiqh muammalah*.
3. Required return value (route of return) for Islamic finance.

From Rozalinda's research (2014) shows that currently Islamic banking has a good opportunity in the development of facing AEC. For future developments, Islamic banking must continue to create new product innovations that will be offered to the public. Islamic banking opportunities are marked with 5 things, namely:

1. The number of Indonesian population with a majority of Muslims is a potential market for the development of Islamic banks in Indonesia.
2. The development of higher education institutions that teach Islamic economics is increasing rapidly, both under or post graduate.
3. MUI's fatwa regarding bank interest is still going to affect the growth of Islamic banking.
4. The government's political will to support the development of Islamic economics in Indonesia has been realized.
5. The entry of international financial institutions into Islamic banking business services in Indonesia is actually an indicator that the Islamic banking business in Indonesia is indeed prospective and trusted by foreign investors.

Alamsyah (2012) in his research also explained that Indonesia's potential in developing Islamic banking was very large, including;

1. The number of Indonesian population with the majority of Muslims being potential customers of the Islamic financial industry.
2. Indonesia's bright economic outlook is reflected in the relatively high economic growth (range of 6.0% -6.5%) which is supported by solid economic fundamentals.
3. Increasing Indonesia's rating sovereign credit to investment grade which will increase investor interest in investing in the domestic financial sector, including the sharia financial industry.

4. Having abundant natural resources that can be used as underlying transactions in the Islamic financial industry.

The high level of competition in the ASEAN market is expected to increase the concern of the Indonesian government by providing greater effort in an effort to increase the growth and expansion of the Islamic banking market as one of the priorities in the development program of Indonesia's economic master plan (Adawiyah, 2015).

4.2 Interbank Competition in Indonesia with Foreign Banks

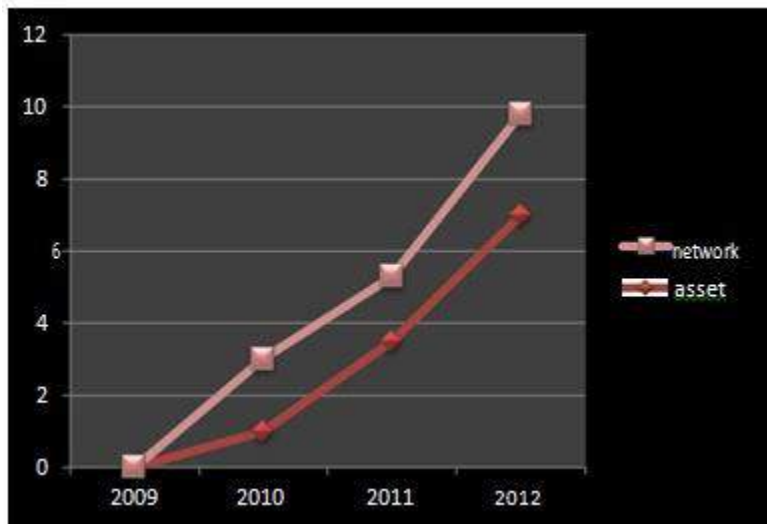
In Indonesia banks with foreign ownership are divided into three groups, namely those that operate: (i) as branch offices (referred to as foreign banks); (ii) as a subsidiary, either through joint ventures with domestic banks (called mixed banks), or through mergers and acquisitions in domestic banks that occurred in the post-1997 crisis period (divestment program); and (iii) as a representative office. As of June 2007, the number of foreign banks in Indonesia was 11 banks, increasing by only 1 bank with the operation of the Bank of China in April 2003, and a mixed bank of 20 banks, a decrease compared to the pre-crisis amount (excluding banks with foreign ownership through the program divestment. In general, as a foreign bank, the strategies for implementing operational activities and policies adopted by these banks will tend to be laden with the interests of their headquarters abroad. Every future plan and operational will be more dependent on the decision of the head office or regional office.

The background to opening up opportunities for foreign banks and mixed banks to operate in Indonesia is related to the need for foreign capital. In addition, the entry of these banks into Indonesia is expected to encourage banking development and the national economy. In general, the benefits derived from the entry of foreign banks, including mixed banks, include the capital inflows channel for the domestic economy, increasing inter-bank competition, and introducing more varied products. However, there is still a negative side that needs to be anticipated, especially in times of crisis, because these banks can act as a place for capital flight (capital flight), and besides that the incoming foreign funds can be more temporary and only for profit momentary (capital inflow during good times capital outflow during bad times). Meanwhile, the complexity of products and technologies brought by foreign banks from developed countries may not necessarily be seen and controlled by the host country supervisory authority, so instead of increasing the bank supervision arrangements and processes but it will be even worse (Claessens, Demirguc-Kunt, and Huizinga, 2001)

To assess the performance of banking companies generally five aspects of assessment are used, namely: 1) capital; 2) assets; 3) management; 4) earnings; 5) liquidity commonly called CAMEL. These aspects use financial ratios. This shows that financial ratios can be used to assess the level of bank soundness. Based on the description above, in this study, researchers want to find out how the role of CAMEL ratios in assessing the performance and role between foreign banks and commercial banks in Indonesia. The Camel ratio used in this study is LDR, ROA, BOPO and NPL.

With the problem of banking intermediation remaining and the possibility of continuing speculation by foreign banks that could affect domestic economic development, it is necessary to make a study of the role of foreign banks in the development of the Indonesian economy. Study It will discuss and compare the performance of foreign banks, and domestic banks, so that a picture can be obtained of the role of each bank group in the national economy. The proposed recommendations will depend on the results of the study, namely whether it is necessary to maintain the form of a foreign bank as a branch office but with certain restrictions, or change the branch office into a subsidiary, for an existing foreign bank branch office and for subsequent foreign bank office opening. .

Based on data from the Indonesian Banking Statistics in 2012, the number of assets of national private banks during the period 2008-2012 continued to increase, which in 2009 increased by 9.50% until in 2012 it increased to 17.17%. As with the total assets of foreign banks which had experienced a decline in the number of assets in 2009 but continued to increase in the following year until 2012 increased to 12.47%. This impacted the development of office networks which continued to increase every year from 2008 to 2012. For national private banks in the office network increased by 17.89% in 2009, up to 2012 increased by 7.02% from 2011 Meanwhile, foreign banks increased by 24.32% in 2009 to 2010.



Source: BI, 2012

Figure 5 Banking statistic in Indonesia

Banking business activities can be said to be successful if the bank can achieve business goals that have been set before, of course the highlight is how the banks are performing. One important aspect in measuring banking performance is efficiency. Measuring banking efficiency can be done by various methods such as looking at comparisons of banking performance indicators and financial ratios, in addition there are also several other methods, namely parametric and non-parametric approaches (Hadad et al., 2003). The parametric approach includes the Stochastic Frontier Approach (SFA), Distribution Free Approach (DFA), and Thick Frontier Approach (TFA), while the non-parametric ones are using the Data Envelopment Analysis (DEA) approach.

Efficiency measurement of Foreign Banks and National Private Banks usually uses non-parametric Data Envelopment Analysis (DEA) methods (Casu, 2007). Considering the importance of efficiency in the increasingly competitive banking world and to find out how efficient the foreign banks are operating in Indonesia and national private banks, the researchers are interested in conducting a study entitled "Comparative Study of Efficiency Between Foreign Banks and National Private Banks in Indonesia "using the Data Envelopment Analysis (DEA) method (Period 2008 - 2012).

4.3 Competition between Commercial Banks and Islamic Banks in Indonesia

The more rapid development of Islamic-based banks or better known as Islamic banks in Indonesia cannot be separated from the role of the banking system in Indonesia (BI, 2007). The role of Islamic banks in spurring regional economic growth is increasingly strategic in order to realize an increasingly balanced economic structure. Support for the development of Islamic banking is also demonstrated by the existence of a "dual banking system", where conventional banks are allowed to open sharia business units (Casu, 2007).

According to Hadad (2003) the understanding of the community about the products and the Islamic banking system is still very minimal, this is because the socialization carried out is still very limited. This is supported by data published by Bank Indonesia, that until October 2006, Islamic banking only had 1.5% of the total banking market share nationally (the Point, 2006). Although the majority of Indonesia's population is Muslim, the development of

Islamic products is slow and has not developed as well as conventional banks. Efforts to develop Islamic banks are not enough to only be based on legal aspects and legislation but must also be oriented to the market or society as service users (consumers) of banking institutions (Mervyn, 2007).

Mervyn also added that the existence of banks (conventional and sharia) generally has a strategic function as an intermediary institution and provides services in payment traffic, but the characteristics of both types of banks (conventional and sharia) can influence the behavior of prospective customers in determining their preferences for the selection between both types of banks. Furthermore, customer behavior towards banking products (conventional banks and Islamic banks) can be influenced by attitudes and public perceptions of the characteristics of the banking system itself (Feng, 2014).

The results of research conducted by Anny (2011) show that consumer behavior in this case is a customer is strongly influenced by their perspective on the banking system. The results of a survey conducted by the Islamic Banking Research and Development Team (Zahara, 2014), show that the perception of interest from a religious perspective can be divided into three opinions;

1. contrary to religious teachings,
2. does not conflict with religious teachings,
3. do not know / doubt. Surveys in West Java (2001) indicate that 62% of respondents stated that they were contrary to

religious teachings, while 22% of respondents said they were not in conflict and the rest (16%) said they did not know.

While the results of the 2001 Bank Indonesia study in West Sumatra showed that 20% of the people stated that interest was unlawful, 39% said they did not know / doubt, and the remaining 41% stated that the interest was not illegal. For the international level, research on customer behavior of Islamic Banks in Bahrain found that customers' decisions in choosing Islamic banks were driven more by religious factors through community support for banking adherence to Islamic principles. In addition, the people in the country are also influenced by the encouragement of their family and friends and the location of the bank (Antonio, 2004).

Al Hamzah (2013) explained that Islamic banks as an alternative banking service have become a separate phenomenon in the Indonesian economy. Its existence has given a new breath to the world of business in this country, especially the banking world. Although it is still relatively new in the banking world, Islamic Banks are able to advance and develop amid complicated competition.

This is evident from the statistics on the development of Islamic Bank business volume according to Bank Indonesia, on average by 70% year on year, a large number and shows continuity of the promising development of Islamic banks. In order to guarantee legal certainty for stakeholders and at the same time provide confidence in the community in using Sharia Bank products and services, in the Sharia Banking Law No.21 of 2008 regulated the type of business,

sharia implementation provisions, business feasibility, channeling of funds and restrictions on Islamic banks is a common part of conventional commercial banks (Zahara, 2014). Meanwhile, to give confidence to the people who still doubt the operational status of Islamic banks so far, business activities are also regulated that do not conflict with sharia principles including business activities that do not contain elements of usury, *maisir*, *gharar*, *haram* and *zalim*.

With the rise of the presence of banks with sharia principles, of course it triggers competition between banks. This situation certainly requires conventional banks and Islamic public banks to be extra hard in improving their performance (Boot, 2005). Each bank is required to improve its bank management to the maximum and as efficient as possible. One management tool that can be used is the analysis of financial statements.

According to Boot (2005), to conduct interpretation and analysis of a bank's financial statements requires a certain size. The measure that is often used to analyze is the ratio. Ratio is a tool used in arithmetic which is used to explain the relationship between two or more financial data (Zahara, 2014). From this ratio it can be seen that the bank's performance is presented in the form of numbers that can analyzed and the results of the ratio analysis will be used as a source of information and work procedures guidelines by the bank, as well as being the basis for decision making by other interested parties.

4.4 Summary

- The ASEAN Economic Community (AEC) is a form of ASEAN economic integration in the free trade system between ASEAN countries. AEC is an ASEAN community in the ASEAN Economic field.
- The formation of a single market and production base, namely: (1) Free flow of goods; (2) Free of services; (3) Free investment; (4) Free of labor; (5) Free of capital flows; (6) Priority integration sectors; (7) Development of the sector of food agriculture forestry.
- The strength of Islamic banks can be a great opportunity for the extension of Islamic banks in the face of competition in the market.
- The establishment of the AEC for Islamic banking is a challenge as the Islamic economic market prospects in the global arena. Be it short-term or long-term challenges.
- In Indonesia banks with foreign ownership are divided into three groups, namely those operating: (i) as branch offices (referred to as foreign banks); (ii) as a subsidiary and (iii) as a representative office.
- To assess the performance of banking companies generally five aspects of valuation are used, namely: 1) capital; 2) assets; 3) management; 4) earnings; 5) commonly called liquidity CAMEL.
- Measurement of efficiency of Foreign Banks and National Private Banks usually uses non-parametric Data Envelopment Analysis (DEA) methods.
- The role of Islamic banks in spurring regional economic growth is increasingly strategic in order to realize an increasingly balanced

economic structure. Support for the development of Islamic banking is also demonstrated by the existence of a "dual banking system", where conventional banks are allowed to open sharia business units.

CHAPTER 5

SHARIA BANKING STRATEGY OF HUMAN RESOURCES SIDE

5.1 Human Resouce of Islamic Banking and Its Reality

Human resources or commonly we are familiar with the term HR, is one aspect in very important management (Suharto, 2006). The central role of human resources in the management system and economy greatly influences how the development of an organization or company. Without adequate human resources, all of the company's operational activities will be hampered (Hasibuan, 2001). Thus, human resource must be able to compete tightly with other human resource so that superior and quality human resources emerge.

One aspect in dealing with the ASEAN Economic Community (AEC) is human resource (Hasibuan, 2002). Indeed, the fulfillment of human resources, especially Indonesia, will be increasingly intense, because competition is not only inside Indonesia but also from abroad.

Human resource development is one of the most effective ways to deal with challenges and problems that might arise in AEC (Sondang, 2006). The development of human resources is considered very important because through the development of existing activity actors will be able to minimize the dependence of the organization on the use of experts outside the organization. According to Ibrahim

(2006) and Handoko (2001), this is one of the weaknesses of the development of Islamic banks in Indonesia.

Handoko further (2001) explained that due to limited human resources who are experts in the field of Islamic banking, causing Islamic banks to recruit workers who are less experts in the field of Islamic banking, especially in human resource support (second layer). This is in line with the opinion expressed by Asnaini (2008) regarding the scarcity of human resources in the field of Islamic banking. Obstacles in the field of human resource in the development of Islamic banking are due to the fact that the Islamic banking system is still not long known in Indonesia. In addition, the academic and training institutions are still limited, so that educated and experienced personnel in the field of sharia banking both from the side of executing banks and central banks (bank supervisors and researchers) are also still limited (Khan, 2015).

The success of the development of Islamic banks at the micro level is largely determined by the quality of management and the level of knowledge and skills of bank managers (Asnaini, 2008). Therefore, the quality of human resources must be improved by both knowledge of banking management and knowledge about sharia banking through workshops. This training is not only given to the leadership level, but also everyone in the Islamic bank starting from the operator, customer service, directors to owners, so they are better-skilled and can function as a good socialist or educator about Islamic banking in the community.

As the Islamic finance industry grows, Islamic banking also requires qualified human resources (Ghazali, 2012). It is needed that not only those who understand the ins and outs of banking operations and sharia principles in the banking industry, but also have other expertise. What is that?

Rowley & Keith (2012) said there are at least five things that will be seen from an individual regarding whether he is qualified to work in Islamic banks. First, administration is a personnel record that historically has an influence on management decision making. Second, human resource will be seen from its performance in the form of a series of work experiences experienced by a person during a career with various positions. Third, job exposure is a standard measure in achieving the performance targets set. Fourth, human resource will also be assessed from the typical tendency of his personality that can support performance. Fifth, have technical skills that must be possessed by each position. Meanwhile, the last point is to have soft skills, namely behavioral competencies that must be possessed by each position.

5.2 Improving Human Resource Quality

Is this quantity development followed by the development of its quality? In other words, whether the sharia bank's operational management has been carried out in accordance with the principles of Islamic sharia, as the basis of sharia banking practices? This is what is now the concern of all parties, both academics, Islamic economists and bank practitioners think hard about how Islamic economic theories whose rules are clear, good and true will be

applied clearly, well and correctly. If this is the goal, then the implementers of Islamic banks must understand and understand the problems associated with Islamic banking (Sadano, 2011). So if the sharia bank is perceived as difficult, expensive and substantially no different from other banks, then this statement needs to be discussed again. Banks are financial institutions in which there is management.

According to Abdul Halim Usman (2015), management, personnel, human resource or whatever the name implies, will not be separated from the people in the bank, namely the human resources available. In Indonesia human resource problems are very complex. Like "tangled thread" especially the last ten years. There are several indicators that characterize this, namely:

1. Incompatibility of human resource competencies with the job market;
2. Distribution of population between regions is not evenly distributed;
3. The growth of the workforce is greater than the availability of employment;
4. Imbalance of public service needs with the number of officers;
5. Distribution of information about a slow or unequal job market;
6. Unemployment and poverty which causes low education and health.

The United Nations Development Program (UNDP) Report in the 2003 Human Development Report on the quality of human

development, out of 174 countries, Indonesia is ranked 112th. While Singapore reached 28th place, 31st Brunei Darussalam, 58th Malaysia, 74th Thailand, and 85th Philippines. In addition, the ease of "trying" in Indonesia in 2005-2006 was ranked 135th out of 175 countries (International Finance Corporation (IFC) and World Bank). This condition causes Indonesia's business competitiveness to reach 60th rank from 61 countries (International Institute for Management Development: 2006 survey).

Based on the research conducted by Yusuf (2015), there are three major indicators of the low competitiveness of Indonesia. First, macroeconomic factors, such as recession expectations and the condition of a country's surplus or deficit are still a concern. The level of economic growth is still relatively slow, the employment rate is still low, investment is slow and poverty is still high. Second, public institutions and policies taken in serving the needs of the community are still far from optimum, the public is still faced with the difficulty of obtaining maximum services. Third, the technology used in the production process still does not produce products that are able to compete in the global market.

And if traced, the final, that the downturn in Indonesia is currently sourced from the low quality of human resources in various sectors, government and private. This fact is a strong enough reason to say the importance of human resource management on the earth in Indonesia today, especially for sharia banking which is classified as not long ago in Indonesia.

In addition, Amalia and Rianto (2013) explained that the importance of human resource management functions is also caused by:

1. Increased competition in the work environment;
2. Increased rules and laws;
3. Legal developments related to human resource;
4. Changes in the characteristics of the workforce; and
5. Incompatibility between knowledge, skills and the ability of the workforce with defined work requirements.

The current work challenge is oriented to a human resource development system that is skilled, flexible, and retrainable based on the development of entrepreneurship skills. Often these changes have not been responded well by the world of education, which is one of the best quality human resources printing institutions. As a result the output offered is not in accordance with the needs of the world of work (Hafidudin and Tanjung, 2009). Educational institutions are still far above the sky. The campus world has not touched many real problems in the community. Finally the institution education is the biggest contributor to the low quality of human resources in Indonesia (Sadano, 2011). If sharia banking is of poor quality, the question is who is the biggest contributor and who is responsible?

The answer to this question depends very much on who and from what perspective to see it. If viewed from the perspective of the vision, mission and objectives of the implementation of education, the answers to these two questions are educational institutions, especially Islamic higher education institutions, and the possibility of personal Islamic figures and Muslims in general (Ghazali, 2012).

The terms "development of Indonesian people as a whole", "development of human resources", and "development of human morality" become very popular and become a policy orientation in the development process in Indonesia. It reminds us of the Al-Quran paradigm which has been believed to contain use values for the development of human resources (Rahmat, 2015). Allah said, "Verily we have created man in the best form".

Besides that, in a hadith of the Prophet Muhammad. said: "Verily I (Muhammad) was sent to perfect morals, manners, behavior" (HR. Ahmad, Baihaqie and Hakim). The mistake so far, in quoting the verses of the Koran is taking part, not seeing it in a more comprehensive context. In the at-Tiin letter above, continued in paragraphs 5 and 6: "Then we returned him to the lowest place; except those who believe and do good deeds, so for them the reward is incessant".

In another verse also stated: "O ye who believe if it is said to you:" Wander in the majlis ", then spread it, surely Allah will give you spaciousness. And if it is said: "Stand ye", then stand, surely Allah will exalt the believers among you and those who are given knowledge some degree. And Allah is Knower of what you are doing. "Based on the above verse, the best and highest degree of human being is a man of faith, good deeds and knowledge.

This means that a person who always maintains his faith, carries out righteous deeds and prioritizes knowledge in each of his work, then he is a human being of good shape and high degree. *Naman* if three things (faith, pious deeds and knowledge) are not nurtured and

nurtured in humans, then humans will become *asoalasafilein* (humans as low as possible).

If so, the direction of Indonesian human development carried out so far has been very true (Barthos, 2010). But in its implementation this has not been realized. This is then the problem in Indonesian human resources. In Islam, human development is in principle equipped with God. According to Mustaqim (2016), in humans there is potential or power that can be built. These powers are:

1. The power of the body, which allows humans to have among others technical abilities and skills.
2. Power of heart, which allows humans to be able to have moral abilities, aesthetics, ethics and be able to fantasize, believe, and feel divine greatness.
3. Power of mind, which allows it to have the ability to develop science and technology.
4. Life force, which allows it to have the ability to adjust to the environment, maintain life, and face challenges.

If humans are built according to Divine instructions, then humans will become national and international assets in order to provide productive human resources in entering the third millennium. In this case, from the very beginning the Al-Quran underlined the need to develop these powers in a balanced manner. The Qur'an clearly states that "man loses, except when the time is understood in the framework of Yaumu ad-Diin, that is faith and good deeds, inform the truth with patience." In a saying, when planting a vine, it will see growth fruiting trees (Faustino, 2003). But such belief will bring

benefits when doing good deeds, in this case planting vines. With such an example, it will be known that faith in God should be actualized in life and life (Usman, 2015).

Knowledgeable men always increase their faith and pious deeds. Therefore, Islamic education, as a system self-transformation, should be actuated through: Preservation of practice; godly child; charity; and spaciousness of the chest; and useful knowledge. Thus for Muslims, there is no vain breath, no wasted steps. Every breath and behavior is offered to God and to seek His pleasure.

Humans must build themselves (to be the best), because humans on earth are as "human gods", where humans must be able to actualize all the values of His God in everyday life and be able to benefit the environment (El -Seoudi, 2012). This is what God promised in His verse: "... Allah will lift the ranks of believers and knowledge among you several degrees ..." Islam does not accept the people are stupid and don't want to try to improve themselves (Amalia, 2013).

According to Khan (2015), the importance of developing the quality of sharia banking human resources, the authors of the analysis of several opinions and facts that are developing at this time. The factors that cause the importance of sharia banking human resource quality are as follows:

a. Sharia Banking Prospects Are More Promising

In Indonesia sharia banking began to be discussed further in the IV National Assembly of the MUI on August 22-25, 1990. The results of the meeting were born of Bank Muamalat on November 1, 1991.

Then followed by other banks. The following table shows that the development of Islamic banking in Indonesia has increased from year to year.

Table 4 Development of Sharia Banking in Indonesia

	2004	2005	2006	March-2007	June-2007	September-2007
Bank Amount						
Sharia General Bank	3	3	3	3	3	3
Sharia Working Unit	15	19	20	21	23	25
Sharia BPR	88	92	105	105	107	109
Total	106	114	128	129	133	137
Office Network						
Sharia General Bank	266	304	349	365	376	386
Sharia Working Unit	89	154	182	187	190	191
Sharia BPR	88	92	105	105	107	109
Total	433	550	636	657	673	686
Office Channeling						
Bank amount	-	-	10	12	13	15
Service amount	-	-	456	467	983	1.046

Source : BI, Direktorat Syari'ah BI, Kebijakan Pengembangan Perbankan Syari'ah Tahun 2017

Data (BI) Yogyakarta notes, in 2017 the development of Islamic banks in Yogyakarta will improve. This can be seen from the addition of three Sharia Rural Banks or BPRS within a relatively short period of time. Unfortunately the supply of human resources or human resources for Islamic banking is minimal. The three BPRS that are ready to operate are BPRS Dana Sejahtera, BPRS Mitra Amal Mulia, and BPRS Mandiri Sejahtera. All three BPRS licensing

processes are complete. This addition makes the map of interbank competition, especially among Islamic banking, increasingly stringent. They are also required to expand their share to exit DIY. What's more BI has a program that seeks to continue to spur the market share of Islamic banks to 5% of national banking in 2008.

b. Sharia Bank Share Revenue Implementation is not Optimal

According to Nawawi (2011), efforts should be made to promote Islamic banking accompanied by an increase in human resources that truly understand the principles of Islamic banking. It is undeniable that all this time, a lot of human resource is a diversion from conventional banks. This has resulted in the abandonment of a "profit sharing" system (*musyarakah* or *murabahah*) (Ismail, 2012).

This condition is seen in the magnitude of the Islamic bank financing scheme which actually tends to rely on financing on the basis of buying and selling (*murabahah*). Of course, the predicate as a "profit sharing" bank does not run optimally (Amin, 2010). He said the calculation of "profit sharing" was more complicated than the interest system. For faster reasons, sometimes the calculation of "profit sharing" is generalized to the amount of "profit sharing" with the amount of "interest" being applied. In fact, he considered that the existence of Islamic banks at this time had not all been purely Islamic principles. Going forward, training in human resources in Islamic banking must be improved to realize a conducive Islamic banking system (Jusmaliani, 2011).

c. Islamic Banking Needs Reliable Human Resource

According to the Head of Bank Indonesia (BI) Semarang, Amril Arief, Islamic banking in Indonesia needs to have reliable human resources who are able to understand the principles of sharia. So far there are still many Islamic banking human resources originating from conventional banks so that the conditions caused the application of profit sharing systems (*murabahah*) to be somewhat abandoned, all Islamic banking in Indonesia until now have not been many that apply sharia principles (Zainul, 2002). This needs to be a trigger for Islamic banking to have reliable human resource who understand sharia principles. Islamic banking human resource training is time to be increased to realize the correct Islamic banking system. Moreover, BI now has a program that continues to spur the market share of Islamic banking to 5% of national banking in 2008.

The Directorate of BI Sharia Banking Research Division Head, Agus Fajri Zam, said that the public's understanding of Islamic banks was still low. Many consider Islamic banks to be the same as other conventional banks and the difference is only the workers with headscarves, caps and greetings. Even though the fundamental difference between Islamic banks and conventional banks is not from caps, hijabs and greetings. In Islamic banks, customers not only entrust funds but include as capital owners. The capital owner will get the profit sharing from the bank's profit not in the form of interest as applicable in a conventional bank (Wahyudi, 2014). Then according to Rowley and Keith (2012), the constraints in Islamic banking are the lack of human resources who understand sharia financial management. For this reason, cooperation with Islamic universities with Islamic banking majors should be done. But in

reality, many Islamic banks use HR on the basis of conventional banking.

d. Less Human Resource Banking

Deputy Governor of BI, Siti Fajriyah said that the development of sharia banking quantitatively was not supported by the availability of sufficient human resources. Human resource needs for Islamic banks reach 40,000 people per year, while sharia economic graduates are very limited, the lack of stock of college graduates who understand sharia economics makes some banks, especially those opening office channeling, choose to transfer employees from conventional banks. This is an instant step, which is actually not good. The employees are familiar with conventional bank mindset, and suddenly they have to change their thinking. One of the effects of this instant method is the dissatisfaction of Islamic bank customers, because the employees cannot explain the principles of Islamic economics properly (Rahmat, 2015). For example, the term profit sharing, many still use the term interest.

BI Medan once held training for journalists, BI's Economic and Monetary Team Head, Medan, Maurids Damanik told SIB that the training for journalists was held to add insight to journalists. Especially to journalists who often write news about banking and the economy. In addition, training that is often conducted every year in different places shows the closeness and openness of BI with the press. From some of the opinions above, it is illustrated that currently sharia banking runs modestly and has a very serious problem about "human resource" both in quantity and quality.

Banking, society (Muslims), educational institutions and also mass media each have duties and obligations in developing and advancing the Islamic sharia banking in the country. The following is according to the author the things that need to be considered and implemented in the context of Indonesia's human resource development efforts (Munawir, 2005).

In Islam, "Government" is as a caliph, God's representative on earth to uphold God's laws and prosper the universe, uphold justice among humans, therefore humanity is commanded to obey and obey the government as obedient to Allah and His apostles. If the government does not do that then there is no reason humans are told to obey it. In Indonesia, building human beings is the mandate of the constitution, written clearly in the 1945 Constitution. The development of "whole people" is the ideals of the Indonesian people for a long time and is clearly stated in the opening of the 1945 Constitution.

The 3rd Alinia of the 1945 Constitution, affirmed "Later than that to form an Indonesian State Government that protects all the people of Indonesia and all of Indonesia's bloodshed and to advance the general welfare, educate the life of the nation, and participate in carrying out world order based on independence, eternal peace and social justice,...". In article 28C, the second amendment to paragraph 1, stated: "Everyone has the right to develop themselves through the fulfillment of their basic needs, the right to education and benefit from science and technology, art and culture, in order to improve the quality of life and for the welfare of mankind." Article 31 of the 1945 Constitution, the fourth amendment is also stated: Paragraph

(1) Every citizen has the right to education. (2) Every citizen is obliged to attend basic education and the government must pay it. (3) The Government endeavors and organizes a national education system, which increases faith and piety as well as noble character in the framework of educating the life of the nation, which is regulated by law. (4) The State prioritizes the education budget of at least twenty percent of the state's revenue and expenditure budget as well as from the regional budget and revenues to meet the needs for national education. (5) The Government promotes science and technology by upholding religious values and national unity for the advancement of civilization and mankind welfare."

There is no reason for the government to neglect people's education, because education and improving the quality of the nation's human resources are mandated by the constitution. Breaking the constitution is sin. And that will bring prolonged misery (Irianti, 2004). Therefore all parties must support the government's efforts in order to improve the quality of Indonesian human resources. The government must have a reliable strategy in improving the quality of existing human resources. The government must be committed to upholding the constitution that has been established (Herman, 2006).

Indra Yuheri, the Superintendent of the Bank Indonesia Senior Bank Office (KBI) Semarang, said that many Indonesian Islamic bank human resources were studying in London England to meet the needs of Islamic banking, rather than Middle Eastern countries. The reason is, the financial system actually developed rapidly in the

country, as well as the United States. This phenomenon shows that Islamic banks have become a global financial system.

Therefore, it is a challenge in the development of Islamic banks in Indonesia. The managers are required to be able to innovate in products and instruments. These demands are one way to pursue the realization of the BI acceleration program in 2008. They cannot rely on the spiritual market segment, but must be able to capture from the rational market side (Solihin, 2012). He said the acceleration program included institutional strengthening, product development, intensification of public education and strategic partner alliances, enhancing the role of the government and strengthening the legal framework, strengthening human resources, and strengthening supervision. According to Fahmi (2014), Islamic banks have the opportunity to be developed, "Moreover there is investment potential from Middle Eastern countries in the Islamic banking industry."

This condition is a challenge that can motivate domestic children to develop Islamic economic higher education. Universities with Islamic institutions both state and private have great and equal opportunities to hold institutional developments, establish faculties/departments of Islamic economics with various study programs tailored to the needs of the sharia banking market (Rivai, 2009).

Therefore the institutional development of higher education will not be successful if it does not cooperate with the government (in this case the Ministry of Education and the Ministry of Religion), which usually involves administrative matters, such as licensing; banking

world (as user); and college (as organizer) (Nafis, 2016). Three components this must work together and earnestly, so that the resulting output is not sterile. And can be beneficial for the progress of the nation, especially the Islamic economy.

The implementation of education that has been carried out so far is not known where the tip and base are, impressed by the road itself. It is seen that between the labor market, the government, educational institutions and the resulting output goes around in their own way. According to Ahmad Ibrahim (2006), all carry out their duties and obligations, without considering the rights of the outputs to be issued.

The human resource problem faced today is enough to answer whether this system is successful or not, it is time for the development of the education system, especially the Islamic economy, to be directed at "synergistic education". In synergistic education, the writer describes the following: that the government as the responsible party for the implementation of good education communicated it to Bank Indonesia (BI) as the highest institution and the Indonesian banking supervisor, then BI and the Syari'ah Bank coordinated with the Higher Education to educate and prepare output is needed, so that with this communication students are not sacrificed, after graduating they can easily apply the knowledge gained in the world of work in accordance with their competencies.

5.3 Summary

- Human resources or commonly known as HR are one of the most important aspects of management.
- One aspect of dealing with the ASEAN Economic Community (AEC) is human resource.
- The development of human resources is considered very important because through the development of existing activity actors will be able to minimize the dependence of the organization on the use of experts outside the organization.
- The success of developing Islamic banks at the micro level is largely determined by the quality of management and the level of knowledge and skills of bank managers.
- In Indonesia human resource problems are very complex. Like "tangled thread" especially the last ten years. There are several indicators that characterize this, namely:
 - 1) Incompatibility of human resource competencies with the job market;
 - 2) Uneven distribution of population between regions;
 - 3) The growth of the workforce is greater than the availability of employment;
 - 4) Imbalance of public service needs with the number of officers;
 - 5) Distribution of information about a slow or unequal job market;
 - 6) Unemployment and poverty that cause low education and health.

- If so, the direction of Indonesian human development carried out so far has been very correct. But in its implementation this has not been realized. This is then the problem in Indonesian human resources.
- In human beings there is potential or power that can be built. These powers are:
 - 1) The power of the body, which allows humans to have among others technical abilities and skills.
 - 2) Power of heart, which allows humans to be able to have moral abilities, aesthetics, ethics and be able to fantasize, believe, and feel divine greatness.
 - 3) Power of mind, which allows it to have the ability to develop science and technology.
 - 4) Life force, which allows it to have the ability to adapt to the environment, maintain life, and face challenges.

CHAPTER 6

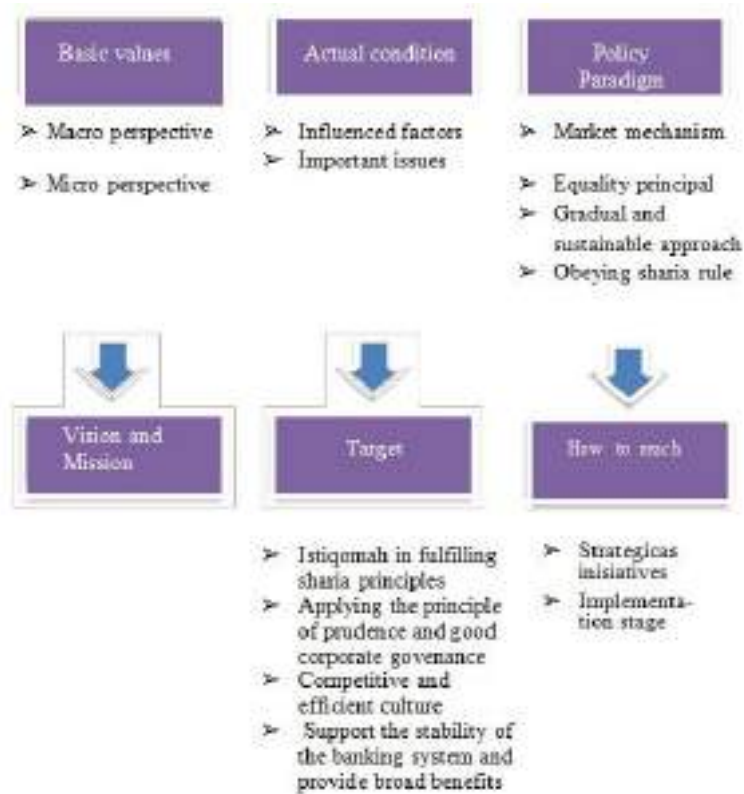
SHARIA BANKING STRATEGY FROM THE FINANCIAL SIDE

6.1 Reality of Islamic Banking Financial Management

Rosiana (2016) explained that Islamic banking or Islamic banking is a banking system based on Islamic sharia principles. Islamic banking applies profit sharing and risk between providers of funds (investors) and users of funds (entrepreneurs). Similar to conventional banking, the maximum level of profit in accordance with Islamic values must also be considered so that the parties involved can enjoy these benefits. Likewise, if there is a loss, the parties involved share it (Jahja, 2012). In addition, Islamic banking manages zakat, avoids transactions related to illicit goods and contains elements of *maisir*, *gharar* and *riba*.

According to Manunggal (2011), the banking sector has a very important role in providing access to unbankable people, the banking sector in Indonesia has experienced development from year to year. This can be seen from the increasing number of branch offices, and reaching remote areas that have not been touched before. Banking services that reach the people in all provinces will be able to distribute banking services and products owned. This can be measured by the level of financial inclusion (Nengsih, 2015). An increasingly inclusive financial system can allocate productive and increasingly efficient resources.

In conventional banking, banks use savings money to lend to debtors, both individuals and entrepreneurs. Profits are derived from the difference between the interest charged to the debtor and the interest paid to savers.



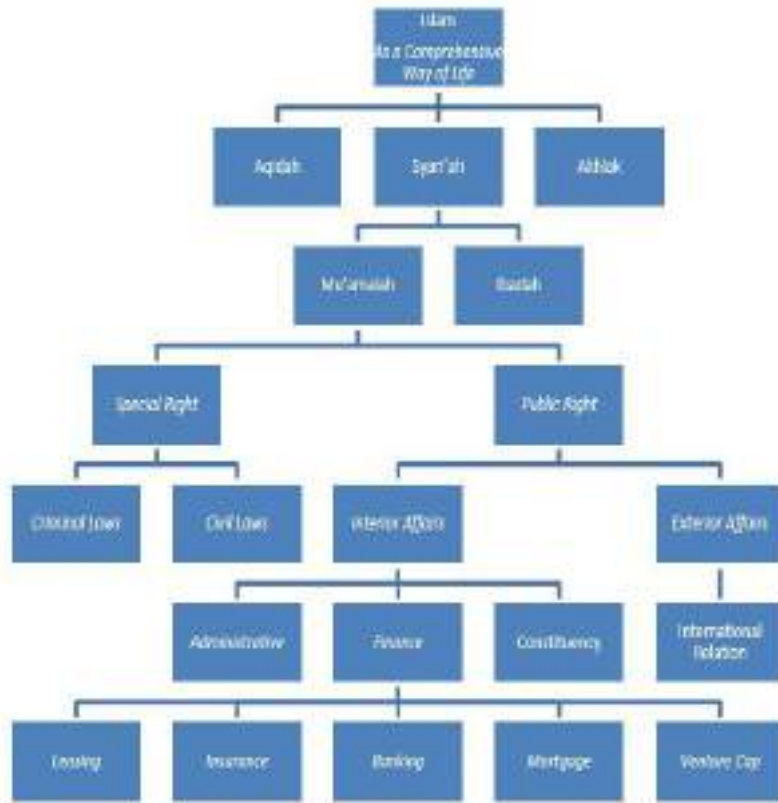
Source: Bank Indonesia, 2017

Figure 6 Banking product services based on financial inclusion

As seen in Figure 7, it can be seen that Islamic financial or economic management also deals with the rational aspects of the economy as being the conventional economic focus. So that the value of Islam is not a completely separate aspect of the rational aspects of economic

reality. Both are very related, in fact. Therefore, we understand that Islamic financial or economic management is said to work also to realize economic motives / principles, namely to achieve the greatest profit with the smallest energy (Ardiansyah, 2009) even though it is not absolute as well as the practice of economic motives in reality.

Strong economic practices or even absolute motives can have a bad impact, oppress other human beings in a cruel way. But for some people in the world, economic motives are not a fundamental law in human business, because there is a "world view" as Islam has become a living and real force. As a country where the majority of the population adheres to the Islamic worldview with the tradition of infaq shadaqah zakat (as an example of generosity / altruism), the worst impact of economic motives does not occur.



Source: Bank Indonesia, 2017

Figure 7 The relationship of sharia economic finance towards rational aspect of economic reality

In addition, we also assume that humans generally do not agree that the motive is carried out purely and absolutely, regardless of morality. *Homo economicus*, that is, human beings who always act according to economic motives, are only in theory (Ardiansyah, 2009). The principle of economics according to normative economics is impossible in absolute terms. In this case, economic motives that occur in society are economic motives according to positive economics.

In reality in the community, economic motives are realized with various modifications or changes that are not infrequently caused by various factors or multi-dimensional humans. So it is necessary to distinguish economic motives between normative economics and positive economics. Because the economic motives (*Homo Economicus*) according to positive economics do not differ much from the economic motives in the understanding of mainstream Islamic sharia economics (*Homo Islamicus*) (David, 2005, p. 12).

In Islamic banking interest is prohibited, then a profit sharing system is used. In this system the relationship between the lender, the borrower and the intermediary is a relationship based on trust and partnership. Islamic banking has the same objectives as conventional banking, namely that banking institutions can make a profit by lending capital, saving funds, financing business activities, or other suitable activities. Andriansah (2009) explains some principles of Islamic law prohibiting elements in below in these banking transactions:

1. trade in illicit goods,
2. interest,
3. deliberate gambling and speculation,
4. obscurity and manipulative.

Comparisons between Islamic banks and conventional banks are as follows.

Table 8 Comparison Between Sharia and Conventional Bank

Sharia Bank	Conventional Bank
Doing only lawful investments according to Islamic law	Doing only lawful investments according and not to Islamic law
Use the principle of profit sharing, buying-selling, and renting	Use interest principle
Profit- and falah-oriented (the happiness of the world and the afterlife according to Islamic teachings)	Profit-oriented
Relationships with customers in the form of partnerships	Relationships with customers in the form of creditor-debitur
Collection and distribution of funds in accordance with the fatwa of the Sharia Supervisory Board	Collection and distribution of funds in doesn't follow any supervisory board
More emphasis on Islamic systems	More emphasis on general banking system

Source: Author's data, 2017

Law No. 10 of 1998 which is a substitute for Law No.7 of 1992 and became the basis of banking law in Indonesia has officially adopted a dual banking system which means conventional banks in Indonesia are recommended to open a sharia business unit or even convert fully into a bank sharia.

Conventional banks and Islamic banks in some ways have similarities, especially in the transfer mechanism, computer technology used, general requirements for obtaining financing such as KTP (Indonesian ID card), NPWP (Indonesia tax number), proposals, financial statements, and so on.

According to Muhammad in Abustan (2009) the fundamental thing that distinguishes between conventional financial institutions and sharia is that they rest on the return and distribution of benefits provided by customers to financial institutions and/or provided by financial institutions to customers. Sharia bank operational activities use profit and loss sharing principles. Islamic banks do not use interest as a tool to obtain income or distinguish interest on the use of funds and loans because interest is an usury which is forbidden.

The emergence of banks with sharia principles, of course triggers competition between banks. This situation requires bank management to be extra hard in improving their performance (Subaweh, 2008). The banking industry is a business that relies heavily on trust, namely the trust of the public as users of banking services. There are few issues related to the bank's unhealthy condition, so the customer will immediately withdraw funds from the bank, so that it will further worsen the condition of the bank.

The influence of the customer's trust factor will greatly impact the development progress of the banking company. The important function of banks in supporting a country's economy is the reason why the bank's financial performance must always be analyzed to determine its health level.

According to Sun (2011), this analysis is also important for companies to provide incentives and self-control of the company and is an important channel for company stakeholders to obtain information on company performance. The results of financial

performance analysis will also be useful to obtain or maintain customer trust.

There are two methods of financial statement analysis that can be used, namely vertical analysis (static) and horizontal (dynamic) analysis. In addition to the method of financial performance analysis there are also several financial performance analysis techniques namely comparative analysis between financial statements, trend or trend analysis, percentage analysis per component or common size, source and use analysis of funds, analysis of sources and uses of cash, credit analysis, gross profit analysis, breakeven point analysis and ratio analysis (Kasmir, 2010, p. 68).

Financial ratio analysis is an analysis technique that is often used, because it is the fastest technique to find out the financial performance of a bank (Ramadaniar, et al., 2012). Based on financial ratio analysis, information will be obtained that is easier to read and estimate than financial statements, it can also be known how the development of company activity reflects the past management performance, in the present and for future trends based on changes in the internal environment as well as the company's external environment.

Ratio analysis also helps in determining the bank's financial position compared to other banks (Lin et al., 2005). Haque (2013) has the same opinion that measuring performance using ratio analysis is very simple and has been commonly used by many previous researchers. The main advantage of ratio analysis is eliminating gaps and making data more comparable.

Financial ratios in banks can be calculated using ratios such as liquidity, solvency, profitability and efficiency ratios. The liquidity ratio measures the ability to meet its short-term obligations and is very important for the sustainable survival of banking institutions (Kumbirai and Robert, 2010). Banks will face liquidity problems if there is an excess withdrawal from demand deposits and savings (Ansari and Atiqa, 2011). The liquidity ratio in this study is proxied by the Loan to Deposit Ratio (LDR) ratio.

LDR is one of the liquidity ratios that is often used to measure bank performance. The LDR ratio measures the total amount of credit provided by a bank compared to the amount of public funds and own capital. The results of the LDR calculation will give an overview of the level of liquidity of a bank because it shows the bank's ability to fulfill its obligations when depositors withdraw funds from the bank. A high LDR indicates that banks lend some of the funds that banks have in the form of credit, so that in such conditions the bank will have difficulty meeting its short-term obligations, such as sudden withdrawals of deposits from customers (Qin and Dickson, 2012b). Conversely, low LDR shows banks are in a liquid state, the condition of increasingly liquid banks shows idle funds (idle funds), which can reduce the opportunity for banks to obtain greater income. Therefore each bank must pay attention to the bank's LDR position to remain in the position determined by Bank Indonesia.

Several studies regarding the calculation of LDR in Islamic and conventional banks have been carried out namely research from Abustan (2009) and Ningsih (2012) which found results that there

were significant differences between conventional banks and Islamic banks while Naili (2013) found that there were no significant differences between conventional bank LDR and Islamic bank.

Of the three results of the study found results if Islamic banks have a greater LDR value compared to conventional banks. Conventional bank LDR is below the LDR value determined by Bank Indonesia in accordance with regulation No. 15/7 / PBI / 2013 which is 78% - 92%. However, this is different from the research conducted by Munir (2012) comparing LDR in Muamalat bank and State Savings bank that found results if conventional banks have higher LDR compared to Islamic banks but Islamic banks' LDR values are still in the required LDR range by Bank Indonesia, Hanif et al. (2012) also found the same results, namely conventional banks have a higher LDR.

The reason Islamic banks have a higher LDR than conventional banks is that first Islamic banks do not have sufficient investment opportunities. Second, Islamic banks are religiously bound and allowed to invest only in approving Sharia projects. Third, Islamic banks rely more on their equity in providing loans so they lack loan opportunities (Ansari and Atiqa, 2011).

Almazari (2011) in his research found that banks with higher total assets, credit, deposits, or equity shareholders do not necessarily mean that they get profitable performance. The same results are shown by research conducted by Raza et al. (2011) and Tarawneh (2006) also explained that a company that has better efficiency does not mean that it will always show better effectiveness. Research

conducted by Alam et al. (2011) concluded that bank ratings differed due to changes in financial ratios. According to Brigham and Houston (2010: 132), financial analysis involves comparing company performance with other companies, especially those engaged in the same industry, and evaluating trends in financial position.

6.2 Improving the Quality of Management of Financial Management

Islamic banking or commonly called sharia banking in Indonesia³ is a new phenomenon at this time in the global banking industry. Modern Islamic banking was first born in the form of rural savings in Egypt's Mit Ghamr in 1963. He began to show the scale and growing in the 1970s. At this time the resurrection time is said again Islamic banking in the world (Siddiqi, 1996). This matter then reinforced by Salleh's (2003) statement that in general, the emergence of all development based on Islam this was seen around the 1970s.

Nearing the beginning of the 1980s, Islamic banks did not only emerge in Islamic countries but also emerged in non-Islamic countries and were increasingly accepted in non-Islamic countries (Ebrahim & Tan Kai Joo, 2001; Alam & Shanmugam, 2007). In the 1990s the number of Islamic banks around the world reached 50 including non-Islamic countries (Hussein, 1991). Then in the 2000s there were more than 180 financial institutions whose operations were based on Islamic sharia which managed assets exceeding US \$ 200 billion (IDB, 2003). Data from Info Bank News showed that in

2001 alone there were around 267 Islamic financial institutions and banks operating throughout the world.

According to the IDB report, the value of the increase in the value of Islamic banks exceeded 15% per year, and budgeted assets of Islamic financial institutions at the end of 2003 were as much as US \$ 230 billion (www.ameinfo.com). In 2009, the Islamic banking industry was growing, there were around 396 Islamic banks in 53 countries. The amount of funds managed has increased to approximately US \$ 700 billion (Antonio, 2009). According to Amin (2011), the latest developments in Islamic banking have entered the world's main financial channels. Ismal (2011) states that the world Islamic banking industry has progressively develops with an average growth of around 1020% per year. There are at least 300 Islamic financial institutions at this time in 75 countries with assets of not less than US \$ 1-2 trillion. Indonesia is no exception than the development of Islamic banking.

The large number of Muslim communities in the Republic of Indonesia is essentially a great potential for Islamic banking to grow and develop. The latest statistics conducted by the Indonesian Statistics Agency (BPS) in 2010 the total population of Indonesia is 237,556,633 people, most of which are based on Java.

Instead of this total around 204 million people are Muslims. Based on this amount, Indonesia is said to be a country with the largest Muslim population in the world. Based on Law No.23 of 1999 and later amended to Law No.3 of 2004 concerning Bank Indonesia (BI), it states that Indonesia applies dual financial and banking systems,

namely the Islamic system and conventional systems. This means that under this law the Indonesian government has recognized and accepted the sharia financial and banking system as one of the financial and banking systems in Indonesia and has also denied banking law No. 14 of 19674. This is also stated in law No. 7 of the year 1992 and has been amended into law No. 10 of 1998. In Law No. 10 of 1998 stated that banks get wider opportunities to carry out its activities by being allowed to run dual banking system activities.

The existence of a dual banking system in which conventional banks are allowed to open a sharia or Islamic window business unit. This regulation is a momentum and has opened wide opportunities for conventional banks who want to open their sharia products while maintaining a conventional system. Unlike in the 1992 law, the term sharia banking is stated vaguely, in this law the mention of "banks based on profit sharing principles" has been changed to "banks based on sharia principles" or abbreviated as "sharia banking" 5. As well as phenomena in other Muslim countries, Islamic banking in Indonesia also recorded progressive developments. This was spurred on by the large Muslim population, the support of the government, banking regulations, and the role of ulamas, Muslim scholars and Islamic organizations (Ismal, 2011).

The government's support was at least indicated by the issuance of several laws concerning Islamic banking as stated earlier. Support also came from Islamic scholars and organizations, namely in the beginning of 2004 the Indonesian Ulema Council (MUI) issued a fatwa on the legal prohibition of bank interest⁶. Then followed by

the Muhammadiyah fatwa⁷ in 2006 which stipulated bank interest is haram.

In 2008 the government issued a more comprehensive law on sharia banking, namely Law No.21 of 2008 and was followed by the State Sukuk Law No.19 of 2008. With the enactment of this law, it further strengthens the foundation law to the Islamic financial and banking system. Therefore, with the enactment of all these laws provides greater opportunities in the development of Islamic banking in the future (Ismal, 2011). He made Islamic banking more free to move in the national banking industry.

The development of sharia banking from an institutional standpoint began in 1991 with the establishment of Bank Muamalat Indonesia (BMI) and officially operated in 1992. According to Rae (2008), the development of sharia banking that was only rapid after 1998. Islamic banking increasingly gained attention after several series economic crisis occurs. The crisis in question was the world economic crisis of the year. In 1998 an economic crisis occurred, with the effect felt by countries in Asia, including Indonesia.

Then the latest is the global economic crisis in 2009 whose influence is almost evenly felt by the countries of the world, especially the United States. Based on two years (2007 to 2009) field studies in Amman, Jordan, conventional banks experienced a greater negative influence than the sharia banking sector as a result of the global economic crisis. This applies because the guidelines set by Islam make the investment approach used more ethically and less risky than conventional banks (Tobin, 2009). This scenario has opened up

room for better acceptance of Islamic finance in general and Islamic banking in particular and provides alternatives to conventional systems (Smolo, 2009; Iyer, 2009). In 2000 the number of Islamic banking institutions increased to 3 Sharia commercial banks (BUS) and 3 sharia business units (UUS).

In 2005 there were 3 BUS and 19 UUS units or Islamic windows. Meanwhile, the total assets of Islamic banking have grown from Rp. 479 billion in 1998 to Rp. 30,145 billion at the end of 2007 (BI, 2005). At that time was the "honeymoon" period where the drastic growth of Islamic banking took place in Indonesia The development of Islamic banking in the last 7 years from the range of 2005-2011 was seen in terms of institutions, assets⁸, TPF (Third Party Funds) ⁹, financing and market share can be seen in the Table 1. From 2005 to 2011, it was seen from the institutional perspective that a significant increase was recorded in 2011 where BUS amounted to 11 units, UUS 23 units compared to 2005 where there were only 3 BUS and 19 UUS. Table 1 also shows the growth of TPF assets. In 2005, the assets of Islamic banks DPK were recorded at Rp. 15.58 trillion and in 2007 had increased to Rp. 28,012. At the end of 2008 the total deposits also increased to Rp. 36.84 trillion and continued to increase to Rp. 76.00 trillion in 2010. Funds deposited by third parties, mostly in the form of Mudharabah deposits, which reached 54.66% of the total DKP.

Table 9 Development of Sharia Banking

Year	2005	2006	2007	2008	2009	2010	2011
BUS amount	3	3	3	5	6	11	11
UUS amount	19	20	26	27	25	23	23
BPRS amount	92	105	114	131	138	150	151
Office amount	550	567	683	951	1223	1763	1796
Third Party Fund (IDR Trillion)	15.58	20.67	28.01	36.84	50.94	76.00	75.81
% TPF increased	31.4	32.7	35.5	31.6	37.7	45.1	-0.25
Expenses (IDR Trillion)	15.23	20.44	27.94	39.76	46.90	68.00	69.72
% increase	32.6	34.2	36.7	42.0	22.8	45.4	2.53
BUS and UUS assets	20.880	26.72 2	33.016	49.555	66.090	97.519	95.74
Shared BUS and UUS	1.42	1.63	1.77	2.14	2.40	3.2	3.2
BPRS asset (IDR Trillion)	1.325	2.147	1.203	1.693	2.126	2.739	-

Source: Bank Indonesia, 2017

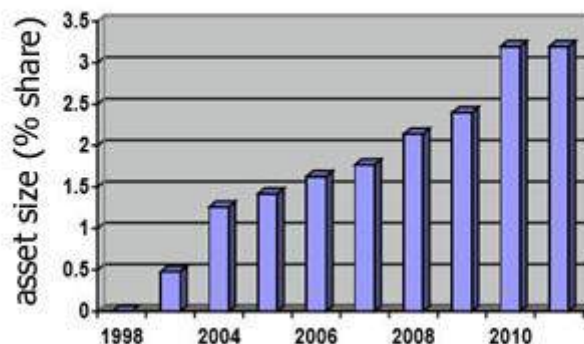
When viewed from the percentage increase, there was a decrease in the percentage increase in 2008 (31.6%) compared to 2007 (35.5%). As a result of the decline in the percentage of third party funds, the growth in the number of third party funds also decreased. In 2009, the percentage of TPF growth had increased to 37.7%. In 2008, Islamic banking financing (42.0%) had increased to 42%, but this increase in financing was not supported by an increase in deposits. The decrease in TPF percentage from 2007 to 2008 led to the Deposit Financing Ratio or Financing of Deposit Ratio (FDR) 10 broke 104% in 2008 (BI, 2008). At the end of 2010, the total assets of Islamic banking (BUS and UUS) were around Rp 97 trillion or around US \$ 12.8 billion together with RM 32.3 billion (BI 2010).

In terms of increasing percentage of consumers, the increase tends to decrease from year to year except in 2010 which was caused by the addition of 5 BUS. This decline can also be seen in 2011, namely for TPF in 2011 (Rp. 75.81 trillion) decreasing compared to 2010 (Rp.76 trillion). A rough calculation according to Karim (2008) of 200 bank customers or consumers, only one person who uses the services of Islamic banks or Islamic bank account holders is only about 0.5% of the total number of bank account holders in Indonesia¹². In terms of the development of financing as well, in 2011 (Rp.68 trillion), although the number increased compared to 2010 (Rp.68.00 trillion), the percentage of increase was very small (2.53%). When overall assets recorded a decline from (Rp. 97.52 trillion) in 2010 to (Rp. 95.74 trillion) in 2011.

Although viewed in terms of asset development, TPF and Islamic banking institutions showed positive developments. Even the average growth of sharia banking has been (47%), higher than the average growth of conventional banking which is only around 15-20% per year. However, when viewed from the overall market share, overall Islamic banking is still too small compared to conventional banking. After 2 decades of sharia banking it operated in Indonesia the market is only 3.2% of the total market share of the national banking industry. The reality as above is termed by Adnan (2010) that the control of public funds by Islamic banking is still low. This situation, the same means that the Islamic economy is still in the stage of opinion, where the evidence is that only about 3% of Islamic banking takes an economic role in Indonesia. This number is very small and it is not appropriate for Indonesia whose domination is Muslim (Amin, 2010). However the rapid development of assets or institutions but the development of market share also remains important because it will show the existence of a company in the industry.

Sula (2011) asserted that the development of Islamic banking in Indonesia must be followed by an increase in market share. This is important because as Schuster stated (1984) in Stiawan (2009), market share reflects the marketing achievements associated with the competitive position of companies in an industry. If viewed from the consumer side, it is calculated roughly according to Karim (2008) of 200 bank customers, only one person uses the services of an Islamic bank. Islamic banking consumers are only 2.8% of the number of people who use national level financial services.

This situation is of course rather disappointing as said by Rais (2008) that the small market share is caused by limited funds both in terms of capital and the amount of public funds that were collected¹³. The small amount of public funds in Islamic banking has implications to the small market share of Islamic banking. This situation finally realizes issues related to consumer uncertainty and the issue of Muslim consumers' compliance with Islamic banking. Considering the large number of Muslims, Islamic banking is considered unable to take advantage of the potential of the existing market. Below is a description of the growth in the percentage of Islamic banking assets seen from the growth of market share compared to conventional banking. The market share is still stiff standing at a number below 3.5% as shown in Figure 2



Source: Bank Indonesia, 2011

Figure 10 Market share growth of sharia bank

6.3 Summary

- Islamic banking or Islamic banking is a banking system based on Islamic sharia principles. Islamic banking applies profit sharing and risk between provider of funds (investors) with fund users (entrepreneurs). Similar to conventional banking, the maximum level of profit in accordance with Islamic values must also be considered so that the parties involved can enjoy these benefits.
- the banking sector has a very important role in providing access to unbankable people, the banking sector in Indonesia has experienced growth from year to year. This can be seen from the increasing number of branch offices, and up to remote areas that were previously untouched. Banking services that reach the people in all provinces will be able to distribute banking services and products owned.
- So that the value of Islam is not a completely separate aspect of the rational aspects of economic reality. Both are very related, in fact. Therefore, we understand that sharia financial or economic management is said to also work towards realizing economic motives / principles, namely achieving the greatest profit with the smallest power.
- In reality in the community, economic motives are realized with various modifications or changes that are not infrequently caused by various factors or multi-dimensional human beings. So it is necessary to distinguish economic motives between normative economics and positive economics.

- Islamic banking has the same objectives as conventional banking, namely that banking institutions can generate profits by lending capital, saving funds, financing business activities, or other suitable activities.
- The fundamental thing that distinguishes between conventional financial institutions and sharia is the restoration and distribution of benefits provided by customers to financial institutions and / or provided by financial institutions to customers. Sharia bank operational activities use profit and loss sharing principles.
- The influence of customers' trust factors will greatly affect the development progress of the banking company. The important function of banks in supporting a country's economy is the reason why the bank's financial performance must always be analyzed to determine its health level.

CHAPTER 7

SHARIA BANKING STRATEGY FROM MARKETING ASPECT

7.1 Reality of Marketing Management in Islamic Banking

Marketing, according to Boyd (2000) in his book "Mark Plus On Strategy", is, "A strategic business discipline that directs the process of creating, offering, and changing values from one initiator to stakeholders." Marketing deals with identifying and meeting human and community needs. Therefore, solid marketing is important for success in all organizations. A simple definition of marketing is the process of managing profitable customer relationships. The two marketing objectives are to attract new customers by promising value excellence and maintaining and growing existing customers by giving satisfaction.

According to Philip Kotler (2010) marketing is "the process by which a company creates value for customers and builds strong relationships with customers in order to capture the value of the customer in return. Then according to Bram & Yudi (2005), marketing is "a social process in which individuals and groups get what they need and want by creating, offering, and freely exchanging valuable products with other parties. Marketing is an organizational function and a set of processes for creating, communicating, and delivering value to customers and managing customer relationships in a way that benefits the organization and its shareholders. Rosly (2009) identifies, essentially in marketing three important points are found:

- 1) Organizational functions;
- 2) activities to create, communicate, submit values and;
- 3) managing customer relationships.

From this event the term marketing management emerged, which is the art and science of choosing a target market and obtaining, maintaining and growing customers by creating, submitting, communicating superior customer value Gerrard (2004). From the above definitions it can be concluded that marketing is a social process in which individuals and groups get what they need and want by creating, offering, and freely exchanging valuable products with others. The purpose of marketing itself is to know and understand the customer in such a way that the product or product matches the customer.

Gerrard also added that the task of marketers is to plan marketing activities and assemble a fully integrated marketing program to create, communicate and deliver value to consumers. The marketing program consists of a number of decisions about marketing activities that increase value for use.

Marketer activities appear in all forms. One traditional painting about marketing activities is in terms of the marketing mix, which has been defined as a tool of marketing tools that companies use to pursue their marketing goals. The concept of the marketing mix was first conceived by Neil Borden in his article entitled "The concept of the marketing mix" published in the Journal of Advertising Research in 1964. The marketing mix is a set of marketing tools used by companies to pursue their marketing goals. While the marketing mix

according to Kotler & Amstrong is as follow, "Marketing mix is a collection of controlled tactical marketing tools that are integrated by the company to produce the desired response in the target market."

The marketing mix is a controlled variable that is combined to produce the expected response from the market. And for service businesses there are seven elements of marketing mix (Marketing Mix-7p), namely: Product, Price, Promotion, Place, Participant, Process, and Physical Evidence.

1) Product (product)

Products are important elements in a marketing program, opinion strategies affect other marketing strategies. Purchasing a product is not only to have the product but also to meet the needs and consumer desires. Besides that, the position is defined as: Something that can fulfill and leave a customer. Whatever it means, as long as it can fulfill the customer's wishes and our needs can be said as a product (Kasmir, 2004: 186)

2) Price (Price)

Price is an economic sacrifice made by a customer to obtain a product or service. In addition, the price of one of the important factors of a consumer in making a decision to do a transaction or not (Engel, Blackwell and Miniard, 1996). Prices are said to be expensive, cheap or mediocre from each individual does not have to be the same, because it depends on individual perceptions that are motivated by the environment of life and individual conditions (Schifman and Kanuk, 2001).

3) Promotion (promotion)

Promotion is an activity of communicating information from a seller to a consumer or other party in the channel sales to influence attitudes and behavior. Through advertising a company directs persuasive communication to target buyers and the community through media called mass media such as newspapers, magazines, tabloids, radio, television and direct mail (Baker, 2000: 7). Media promotions that can be used in this business include:

- a) Sales promotion,
- b) Publicity and public relations, and
- c) Direct marketing.

The determination of the promotional media to be used is based on the type and form of the product itself.

1) Place (distribution channel)

Kotler (2000, p. 96) states that, "Distribution channels consist of a set of institutions that carry out all activities (functions) that are used to distribute products and services that are the same as the owner from producer to consumer. From the above definition can be interpreted that the distribution channel of an item is the whole activity or function to move the product accompanied by the owner's right from the producer to the final consumer or industrial user. Distribution is related to the ease of obtaining products on the market and is available when consumers look for them. Distribution shows various activities carried out by the Company to make products or services obtained and available to target consumers.

2) People

According to Hendri Sumanto (2004), what is meant by participants here are employees of service providers and sales, or people who are directly or indirectly involved in the service process itself, including tellers, and customer service.

3) Process

The process is an activity that shows how service is provided to consumers during the purchase of goods. Clinic manager through front liners often offer various forms service for the purpose of attracting consumers.

4) Facilities

Free doctor consultation services, product delivery, credit card, member card and service facilities influence the company's image.

5) Physical evidence

The physical environment is the condition or condition that is in it also includes the clinic's atmosphere the place of operation of maintenance services skin beauty.

6) Characteristics of the physical environment

It is the most visible aspect in relation to the situation. What is meant by this situation is the situation and condition of the geography and environment of the institution, decoration, room, sound, aroma, light, weather, visible layout and layout or an important environment as an object of stimuli. Of the seven elements of the marketing mix which

is the key to success for a clinic including the completeness of service products that are ready to offer (one stop beauty service), strategic location, hospitality and effectiveness of service, adequate parking, and other facilities supporting consumer comfort in care such as the room from the waiting room to the cool treatment room and the right light. Besides that, strategy is defined as something that can meet the needs and desires of customers. Whatever the form, as long as it can meet the needs of customers and our needs.

7.2 Marketing Management Improvement Strategies

The concept of marketing is the most important factor in achieving the success of a company, because it is oriented to customer satisfaction. According to Kotler (2000, p. 22), the concept of marketing is the key to achieving organizational goals that are defined as the company must be more effective than competitors in creating, submitting, and accommodating customer value to the selected target market. The definition above has four basic ideas contained in it, namely:

a. Target market

A company may not be able to develop properly, but many companies can achieve what is targeted in managing the company by determining its target market.

b. Customer needs

Various customer needs are not always simple, companies must be able to predict what will be the needs of consumers in the future.

c. Integrated marketing

There was a collaboration between the company and related departments to serve the interests of customers. So that marketing can run optimally to serve customer needs together.

d. Ability to generate profits

The final goal of the marketing concept is to help the organization achieve its goals. Most of the companies' main goal is just to make a profit. However, here not only prioritizes profits but earns profit as a result of satisfaction obtained by consumers rather than competition. According to Gupta (2012), the marketing concept is a business philosophy which states that satisfying consumer needs is an economic and social requirement for the survival of a company. In the marketing concept there are 3 important factors:

a. Orientation to consumers

The company always wants to meet all consumer needs, so it will always be oriented towards meeting the needs of consumers. Companies that want to practice consumer orientation must do several things, including:

- 1) Determine the basic needs of buyers who will be served and fulfilled.
- 2) Determine product and marketing programs.
- 3) Conducting research on consumers to measure, assess, and interpret consumer desires, attitudes, and behavior.
- 4) Determine and implement the best strategy.

b. Coordination and integration with consumers

To be able to provide satisfaction to consumers optimally, all existing market elements must be coordinated and integrated. This means that every person and every part of the organization takes part in a coordinated effort to provide customer satisfaction so that the company's goals can be achieved.

c. Get profit from consumer satisfaction

By being able to satisfy the needs of consumers, it is expected that the company's goal to get a profit will be achieved. This means that the company must be able to meet all the needs and desires of consumers with the products offered.

In the era of globalization, the competitiveness of companies needs to be increased, not only aspects of production, but also aspects of marketing. Although the management functions of each contribution when developing strategies for different levels, but the range of control of the company to the external environment tends to be limited. In this condition, the company needs to put a marketing strategy in order to play an important role in its sustainability. This function of management having the greatest contact with the outside world is the marketing function. There are several definitions of marketing strategies from Robinson (2000) including:

a. "The marketing strategy is a statement both explicitly and implicitly about how a brand or product line reaches its objectives".

b. "The marketing strategy is a basic tool that is planned to achieve company goals by developing competitive advantages that are sustainable through the market entered and marketing programs that are used to serve the target market."

In principle, marketing strategies provide direction in relation to variables such as market segmentation, identification of target markets, positions, marketing mix elements and marketing costs, where marketing strategies are an integral part of business strategies that provide direction for all management functions of an organization. (Sari, 2012).

Each company directs its business activities to produce products that can provide satisfaction to consumers so that in a certain period of time and in a certain number of products profit can be obtained as expected. Through the products it produces, the company creates, fosters and maintains confidence in the product. The success of a company can be determined by the accuracy of the manufacturer in providing satisfaction and the target consumers that are determined, where marketing efforts are directed to consumers who are intended as market targets.

In this case, marketing efforts to support the success of the company are based on the marketing concept to be able to determine the marketing strategy that leads to the target real market. The importance of marketing strategies for a company arises and the inability of the company to control all factors that are outside the company's environment. Similarly, the changes that occur in these factors are not known in advance.

According to Danaputra & Gita (2013) that marketing strategy is a form of plan that is directed in the field of marketing to obtain maximum results. To make a consideration and see the possibilities that arise in an effort to influence marketing, the leader decides to develop a new product design that suits the tastes of consumers at this time, then conducts marketing through distributors in the areas targeted by the product.

According to Chotimah (2014) said that marketing strategy is a written plan that is usually comprehensive which describes all activities related to achieving a particular marketing goal and their relationship with each other in relation to their respective time and area. This includes short-term and long-term sales forecasts. Production targets and pricing policies, marketing strategies and sales strategies, conditions for filling vacancies, as well as selected marketing and expenditure budgets.

In terms of strategy, planning is always contained which is a process that continues -continuous in a company. Therefore, the marketing strategy and each company is a distribution plan where the company hopes to achieve a predetermined goal which ultimately will realize the main objectives of the company concerned. For the banking world, the most appropriate marketing concept is a social marketing concept. This concept emphasizes the determination of the needs, desires, and interests of the target market and provides expected satisfaction more effectively and efficiently than competitors so as to guarantee or provide prosperity for consumers and society (Kasmir, 2003, p. 17)

Because the current market conditions are buyer's market, customers are everything. Needs, desires and customer satisfaction must be truly considered. While the purpose of this concept is for customers to remain loyal (loyal) to use products or services produced by the bank. To aim at these goals, the exchange activity or process must be managed well by humans and their organizations in order to generate income for themselves and decisions for other parties. It cannot be denied that marketing activities require a strategy because without a strategy it will be difficult to achieve the desired goals.

Therefore every marketer (all employees in the company) must have values or strong values so that he does not cheat, does not cheat, does not force it, and so on (Prasetyo, 2012). So, the perception that the market conventional is always more profitable and the sharia market is defined as the Muslim market alone is not right. Even so, changing perceptions is not something that is not possible in line with the changing needs and desires of humans in the future, now there has been a market shift from intellectual/rational level, to emotional, and finally to spiritual transformation. According to Effendy (2014), this spiritual market will consider the suitability of the product, financial benefits, and spiritual values that it believes. However, not the whole rational market will move to the spiritual. This is where the biggest challenge of the Islamic system in targeting rational markets because rational markets are the biggest market (Koksal, 2014). Therefore, a concept of solution emerged to bring this rational market to the spiritual market area, namely the concept commonly called sharia marketing.

Marketing itself is a form of *muamalah* that is justified in Islam, as long as in all its transaction processes are maintained from prohibited matters by the provisions of sharia (Laksamana, 2009). Thus simply, Sharia Marketing is the application of a strategic business discipline that is in accordance with sharia values and principles. So sharia marketing is carried out based on the Islamic concept taught by the Prophet Muhammad. This means that in sharia marketing, the entire process, both the creation process, the bidding process, and the process of changing values (values), must not be anything that contradicts the Islamic contract and principles of muamalah. Sari & Tanjung (2012) argue, insofar as this can be guaranteed, and disregarding the principles of Islamic muamalah not occurring in any transaction in marketing can be permitted. According to Hermawan Kartajaya, the core value of sharia marketing is Integrity and transparency, so that marketers cannot lie and people buy because they need and are in accordance with their wants and needs, not because of their discounts. Sharia marketing is not just a marketing that is added to sharia because there are more values in sharia marketing, but marketing is further a role in sharia and sharia plays a role in marketing (Antonio, 2001). Marketing plays a role in sharia, meaning that sharia-based companies are expected to work and be professional in the business world, because with professionalism can grow consumer confidence. Sharia plays a role in marketing, meaning an understanding of how to create and offer can even change a value to stakeholders so that the company can maintain the balance of the pace of its business so that it becomes a sustainable business.

In sharia marketing technical matters, one of them is that there is sharia marketing strategy to win mind-share and sharia marketing values to win heart-share (Warsono, 2010). Sharia marketing strategy carries out segmenting, targeting and positioning markets by looking at market growth, competitive advantage and competitive situation so that they can see good market potential in order to win mind-share. Furthermore, sharia marketing value seeing a brand as a good name that becomes the identity of a person or company, so for example a company that gets the best customer service in its business so that it can get heart-share.

As a solution, sharia marketing is implemented by doing business following the way of the Prophet Muhammad. Prophet Muhammad as a merchant gave a good example in every business transaction (Alqoud, 2005). He made transactions honestly, fairly and never made his customers complain, let alone disappointed. He always kept his promises and delivered his merchandise with quality standards in accordance with customer requests. His reputation as a true and honest trader has been well planted since young. He always shows a sense of responsibility for every transaction made. He really follows the principles of fair trade in his transactions.

Therefore, in his business transactions as a professional trader there is no bargaining and quarrel between Muhammad and his customers, as is often witnessed at that time in markets throughout the Arabian Peninsula (Alqoud, 2005). All the problems between Muhammad and his customers are always resolved fairly and honestly, but even continue to lay down the basic principles for fair and honest trade

relations. Here it is seen that he not only works professionally, but also practices professionalism when he is appointed become a Prophet. He leads his friends with the principles of professionalism; give him an assignment in accordance with the capabilities and capacities possessed. Everything works professionally and of course with the guidance of Allah.

In addition, he has eroded commercial transactions of all kinds of practices that contain elements of fraud, usury, gambling, gharar, doubt, exploitation, excessive profit taking and black markets (Alqoud, 2005). He also standardizes scales and sizes, and forbids people from using scales and other measures that cannot be used as standard handles. The Prophet Muhammad also prohibited several types of trade, both because of the system and because there were elements which were forbidden in it. Trading objects prohibited in the Quran is haram. Furthermore, the Prophet Muhammad forbade the price paid for blood, and condemned those who received and paid *riba* (interest), people who tattooed on the skin, people who tattooed themselves, and sculptors (HR Al-Bukhari), because clean goods "meant healthy and obtained in a halal manner. Because of that what is produced becomes halal (Muhamad, 2004). We can see in the daily life of business, how the wisdom of swearing falsely in convincing buyers to be a daily sight. Fake oaths are often used as "weapons" in convincing buyers. Because we are not sure of the superiority of our merchandise, we cannot provide good service, us vow to convince buyers. This habit besides showing low professionalism is also prohibited in sharia business. In addition, we should also care about our sources of income, because this will

greatly affect the blood and meat raised from non-halal sources. If a lump of blood or the heart of our child and wife is formed from a non-halal source, then it will also produce generations whose morals are broken, their morals deviate and their behavior is not commendable.

In sharia marketing also introduced how to do business with heart. Because the heart is the main source for all one's goodness and happiness. Indeed, the most important of our lives is the choice of our person, and the essence of our person, and the essence of our person is the state of our heart or heart. No matter how smart the mind, if the heart is rotten and evil, then intelligence will actually cause havoc. Likewise, the strength and beauty of the body will bring harm when it is not accompanied by the maintenance of clarity of heart (Muhamad, 2004). If our hearts are clean and healthy, the mind can be clear and healthy and can be smart and productive, because there is no time to think cunning, jealousy, or the desire to overthrow others. If not careful, this life is very tiring.

Once we don't like someone, the hatred will take time, productivity and eat our happiness. We will be tired of thinking about our people hate. If the heart is clean, the mind can become clear. When there is no time for envy, everything will enter easily, because there will be no room to underestimate anyone. As a result, we will have very high data access, access to information that is truly abundant, access to truly extensive knowledge. In the end, we will be able to produce bright, creative and innovative ideas in building new ideas in a company.

We easily bring our company to face such a tight competitive situation. The connection between business and *qalibun salim* (the heart that survives; survivors of all decay) is certainly very close. We must realize that the biggest problems faced in business activities are human problems, whereas man himself depends on his mood. This is where new knowledge is needed in managing the business, which is how to manage the business with heart. In the end, we can say that if a businessman has run his business honestly, with a clear heart, then the business he runs, God willing, will be of high quality, have a high value of service, can build a good brand, create a good positioning in the minds of his customers, so he will be very loved by his customers.

One of the interesting things in Islamic marketing is the implementation of a marketing model known as Sustainable Marketing Enterprise (SME). In the SME model, the marketing concept here does not mean marketing as a function or department within the company, but how can we see the market creatively and innovatively. Marketing is not just like what people think, a study to sell. or as understood by some circles is just marketing mix, namely the making of a strategy for a product (product), price (price), place (place) or promotion (Kotler, 2012). But the understanding of marketing itself is broader in scope. In sharia marketing strategy the first must be done in exploring the market. The size of the market size (market size), market growth (market growth), competitive advantage (competitive advantages) and competitive situation. After strategizing, we must devise tactics to win market share called Tactic Sharia Marketing (Yulianto, 2010).

First of all, after having a clear positioning in the minds of the community, companies must distinguish themselves from other similar companies. It requires differentiation as a core tactic in terms of content (what is offered), context (how to offer it) and infrastructure (which includes employees, facilities and technology). Then apply differentiation creatively in the marketing mix (product, price, place, promotion). Therefore marketing-mix is called tactic creation. Even though selling which plays an important role as capture tactic must also be considered because it is an important element that deals with transaction activities and is directly able to generate income.

From this explanation regarding the study of sharia marketing, it can be concluded that sharia marketing is a solution in the face of conventional marketing practices that do not uphold the values of morality and the rights and obligations of undervalued buyers in buying and selling transactions, this condition is felt by society is very detrimental to consumers, so that there is a change in people's perceptions who want market conditions that are far from the practice of lies and cheating that is often done by sellers or businessmen today. In sharia marketing, the entire process, both the creation process, the bidding process, and the process of changing values (values), should not be anything that is contrary to the Islamic contract and principles of *muamalah*. As long as this can be guaranteed, and the disregard for the principles of Islamic *muamalah* not happening in any transaction in marketing can be permitted. The Messenger of Allah himself gave an example to us, about ways of doing business that hold fast to the truth, honesty, trustworthiness

and still gain profit. These values are the basis or law in doing a business. Rasulullah is the profile of success in marketing marketing.

Therefore, we can imitate the attitude of the prophet by prioritizing spiritual values (Islam). In doing marketing and business we should fulfill it with the values of worship. Besides that, making God as the last stop of the spirit of economic activity we do (Muhamad, 2004). In the Qur'an (Surah Al-An'am (6): 162) stated "Verily my prayers, my worship, my life and my death are only for Allah". This sharia marketing practice does not only apply to Muslims, but also non-Muslims can practice sharia because the Prophet Muhammad spread the teachings of Islam certainly not only for Muslims. So it's okay if the Islamic marketing value is an Islamic initiative so that it can inspire others. The more non-Muslims who take part in applying this value, the better it is to create marketing conditions that prosper the sellers and buyers by avoiding fraudulent or fraudulent practices in marketing. This sharia marketing concept itself is currently developing as the Islamic economy develops.

Some companies and banks, especially sharia-based ones, have adopted this concept and have received positive results. In the future, it is predicted that Islamic marketing will continue to grow and be trusted by the community because of its values that are in accordance with what the community needs, namely honesty. Finally, a businessman should implement this sharia marketing practice as a form of worship to Allah so that the business carried out will receive blessings and blessings from Allah with success in the world and later in life and this spiritual marketing should not be a trend, but

systemically formed in activities our daily business (Muhamad, 2004). Honesty is an important instrument in grabbing competitive advantage. Thus competition is not again smeared with cheating and oppression. Wa'Allahu alam can answer.

7.3 Summary

- Marketing is: "A strategic business discipline that directs the process of creating, offering, and changing values from one initiator to stakeholders. Marketing deals with identifying and meeting human and community needs. Therefore, solid marketing is important for success in all organizations. A simple definition of marketing is the process of managing profitable customer relationships. The two marketing objectives are to attract new customers by promising value excellence and maintaining and growing existing customers by giving satisfaction.
- Marketing management which is the art and science of choosing a target market and gaining, maintaining and growing customers by creating, submitting, communicating superior customer value.
- The task of marketers is to plan marketing activities and assemble a fully integrated marketing program to create, communicate and deliver value to consumers. The marketing program consists of a number of decisions about marketing activities that increase value for use.
- The marketing mix is controlled variables that are combined to produce the expected response from the target market. And for service businesses there are 7 elements of marketing mix (Marketing

Mix-7p), namely: Product, Price, Promotion, Place, Participant, Process, and Physical Evidence.

- This spiritual market will consider the suitability of the product, financial benefits, and spiritual values that it believes.
- The biggest challenge of the sharia system in targeting rational markets because rational markets are the biggest market.

CHAPTER 8

SHARIA BANKING STRATEGY FROM THE ASPECT OF PRODUCTION SERVICES

8.1 Product Reality in Islamic Banking

The fundamental difference between conventional banking and Islamic banking based on interest and profit sharing is not enough to maintain customer loyalty. There are many factors that can be used as reasons for customers to remain loyal to financial institutions. One of them is excellent service (service excellence). This service is very important to maintain and attract more customers.

Service excellence is caring for customers by providing the best service to facilitate ease, fulfillment of needs and realize satisfaction, so that they are always loyal to the company (Lovelock and Wirtz, 2004). Good service is important as a promotional tool for prospective customers. Service excellence at the bank can be said as a service to give satisfaction to customers so that they get what they want easily and get more than what they want so far.

Islamic banking must be able to apply this concept so that public trust will increase. This service excellence must be a differentiator from the services in conventional banks. Don't let the difference lie only in the application of the interest system or profit sharing. So the concept of service excellence is the concept of Islam in general. So there is no reason for Islamic banks not to apply this concept in providing services to their customers.

Regarding the importance of service excellence, Harvard Business Review, US News and World Report have conducted a survey of customers who left. As a result, as many as 14 percent of them left because of untreated complaints, 9 percent because they were attracted by competitors' offers, another 9 percent because they moved out of town and lastly 68 percent because of disappointing service attitudes.

If we look at the survey results above, the basic reason why customers go is because they feel dissatisfied with the attitude of employees, which is as much as 68 percent. That is, the behavior of the company towards customers becomes the main parameter to measure customer loyalty.

According to Muhammad Idris in his idea of Initiating Sharia Banking Service Excellence (2012) one of the main factors of customers choosing a bank is based on the quality of services provided by the bank. The better the quality provided, the more customers will choose the bank and vice versa.

Therefore, Islamic banks need to pay attention to service issues, considering the sharia-based industry is still relatively young compared to conventional banking. Islamic banking must be different not only in terms of the application of profit sharing, but also in terms of service excellence. At least there several things that need to be considered by Islamic banking related to service excellence.

First, Islamic banking does not differentiate customers from social classes such as rich or poor even against customers of different religions. Islamic banking must provide good service to all Muslim and non-Muslim customers.

Second, polite appearance. Appearance is also an important factor for customer satisfaction. Moreover, Islamic banking is a financial industry that is based on Islamic principles, so in the interpretation must also reflect Islam. Do not assume that Islamic banking only sells sharia labels while the behavior or appearance of employees is not in accordance with the sharia itself.

Third, improve the quality of human resource. Islamic banking employees are required not only to understand conventional economics but equally important is the mastery of sharia aspects. Employees must be able to explain the product or contract that has to do with sharia. In other words, the bank also provides explanations and education about various sharia-compliant products and contracts. For this reason the Islamic bank must be selective in recruiting new employees with a benchmark that the employee must master two sciences at once, namely conventional science and sharia. In addition, the Islamic bank needs to increase the knowledge of its employees through various trainings, especially in the aspect of sharia most of the employees in Islamic banks now come from conventional.

As a business entity in the service sector, Islamic Banking is faced with the fact that consumer behavior is getting smarter and always developing in accordance with environmental conditions both micro

and macro. Consumers not only utilize the services offered and their advantages, but more than that will pay attention to how a service is provided.

Customer satisfaction is the key to success in the Sharia Banking services business. This goal can certainly be achieved one of them by means of excellent service. The main concept is how customers feel comfortable and easy in each process of enjoying Islamic Bank products. This is in line with what was conveyed by the Messenger of Allāh in a hadith, "Whoever facilitates the affairs of people who experience difficulties will Allah facilitate his affairs both in the world and in the hereafter" (HR Muslim).

A prospective customer who wants to take advantage of Islamic Bank services shows that he actually has an initial interest in Islamic bank products. This momentum must be utilized by intellectual human resources in Islamic banks to provide a comprehensive understanding of the advantages of the sharia banking system compared to the conventional banking system. Sharia bank's human resources actually also carry out the applicative *da'wah* function of calling for goodness on the principle of profit sharing and provide an understanding of the dangers of usury. However, customers also not only consider the halalness of Islamic bank products but will further assess how well the services are. Services to customers include:

1. Physical conditions include buildings, room layout, cleanliness and comfort.
2. Products offered to customers through the development process of products that customers want today. It is not

always that Islamic banks do product marketing through a "halal-haram" approach. Because in fact customers want products that are definitely halal but provide better benefits from conventional banks and their convenience such as the availability of ATM networks and so on.

3. Front liner services;
 - Security guards open doors and greet with greetings and smiles to customers who come and go.
 - Customer Services who have product understanding (product knowledge) and are able to communicate well in explaining to customers. Able to receive customer complaints both directly and through remote communication.
 - Teller: serve customers with friendly, fast and accurate entry of transactions.

To maintain the quality of service should be carried out the pattern of implementation supervision and give awards to employees for their best achievements provide services to customers. Aspects of customer service include:

1. SMILE

A smile is the most easily understood body language. A smile in relation to excellent service is a smile by presenting the heart, so that it will emit a signal of sincerity for every customer. A customer who comes with a smile from the front office officer will feel comfortable and welcome. Every practice of makruf (virtue) is sodaqoh. Indeed, among the practices of makruf is to meet friends with a cheerful face

(smile) and reduce the contents of your bucket to be filled in the bowl of your friend. (HR. Ahmad)

2. GREET

Immediately proceed with greeting customers with greetings "assalamualaikum" and show readiness for help by saying "Is there anything we can help you with?" From Abu Ayyub Radliyahuah 'anhu that the Prophet sallallaahu' alaihi wa Sallam said: "It is not lawful for Muslims to decide on friendship with their siblings for more than three nights. They meet, then someone turns away and others compete. The best of them is to start greeting Muttafaq Alaihi.

3. HEARING

Some customers have different types and characters, some are used to talking and expressing the purpose of coming to Islamic banks, some are otherwise or even tend to be quiet. This is where the role of Islamic bank SDI is to communicate with customers, so that customers feel directed to express the goals that they actually think about. Listen to what customers say so they can determine what solutions will be given.

4. HELP

After understanding the customer's wishes, help him immediately. Give the best and fastest solution to achieve maximum satisfaction for customers. No matter how good the solution given if not done quickly will reduce its value. Let's just say that customers who come

to Islamic banks are people who are busy and have a lot of business that will be completed at the next opportunity.

From Abu Hurairah *radhiallohu 'anhu*, the Prophet *sallallaahu' alaihi wa sallam* said, "He who releases a believer from the distress of living in the world, surely Allah will deliver from his distress on the Day of Resurrection, whoever facilitates the affairs (believers) that are difficult surely Allah will facilitate his affairs in the world and the hereafter (Hadith with editors like this are narrated by Muslims).

Excellent service (excellent services) is an important aspect in successfully winning the hearts of customers. Customers as humans, if they are also treated humanely (people behavioral oriented) so they don't just get satisfaction but get a joy or pleasure. This is an emotional experience that impresses customers and encourages loyalty. Therefore, Islamic Banking must manage services quality to be able to seize and maintain customer satisfaction. Furthermore, Islamic Banking must also make customers not just feel satisfaction. Because satisfied customers are still open the possibility to switch to other company products or competing products. So that Islamic Banking must be able to create pleasant feelings and experiences for customers (customer delight).

8.2 Production Management Improvement Strategies

The decision to save at a Sharia Bank by a customer is certainly closely related to how consumer behavior in deciding to buy a product. Consumer behavior is individual activities that are directly

involved in using goods and services including decision making in the preparation and activities.

Consumers who are faced with various types of products have various alternative choices before making a decision. Consumers can, make purchasing decisions as well as embody their requests through the process of observation and selection. Several factors that influence consumers in giving buying decisions, namely:

- 1) Cultural factors, sub-cultures and consumer social classes;
- 2) Social Factors consisting of reference groups, families, and roles and status;
- 3) Personal factors consisting of: characteristics of age and stage of life cycle, occupation, economic conditions, lifestyle and personality and self-concept of the buyer;
- 4) Psychological factors, namely: motivation, perception, knowledge, belief and conviction.

To increase the market share of Islamic banking, it is also required to have competitiveness. This of course can be achieved by having an effective marketing strategy. This is also aimed at efforts to service customers. The quality of products and services is considered a very important factor in a company because global and international markets are increasingly developing. The quality of customer service is seen as the main philosophy by managers in Indonesia if they still want to play an important role in the Indonesian economy.

Efforts to improve the quality of services provided by Islamic Banks must be market-oriented or the public as users of banking services.

This relates to people's expectations, they want to get a good relationship with a bank that is convenient and easy to make transactions. In the Quran, the letter of Ali Imron verse 159, has given instructions for being gentle to someone which means, "It is because of Allah's mercy that you are gentle toward them. If you behave hard again rough-hearted, they certainly distance themselves from your surroundings. therefore forgive them, ask forgiveness for them, and deliberate with them in this matter [246]. then if you have made up your mind, then put your trust in Allah. Verily Allah loves those who put their trust in Him. "

According to Othman and Owen (2001), the reason Islamic banks must be aware of the importance of service quality are: first, Islamic bank products and services must be accepted as high-quality products and services by consumers. God is happy to see the work done on the Itqan tingat which means preparing and giving the best results or doing everything with high quality. Second, using quality services in Islamic banks is important because of their relationship to costs, profits, customer satisfaction, consumer memory, and positive words from the mouth of the consumer.

For companies engaged in banking services, satisfying customers is the main thing that should not be ignored, where customer satisfaction is a very strategic factor in winning the competition, maintaining the company's image in the wider community. Consumer satisfaction is determined by the quality of products and services, for customer satisfaction with services, there are two main things that are closely related, namely consumer expectations for

service and consumer perceptions of service quality. Customers always assess a service that is received compared to what is expected or desired.

According to Kotler service is something that is intangible which is an action or performance offered by one party to another party and does not cause any transfer of ownership.⁷ According to Valarie A. Zeithmal and Mary Jo Bitner defines service as all economic activities whose results are not physical or construction products, which are generally produced and consumed simultaneously and provide added value. Whereas Lovelock defines service as a process rather than product, where a process involves input and transforms it as output. Service is a pleasant feeling given to consumers followed by an attitude of friendliness and ease of meeting needs.

Service is provided as an action or attitude of a person or company to provide satisfaction to customers. Inevitably almost all products offered in each company require good service, both directly and indirectly. In practice consumers need help with services to meet the satisfaction of their needs, and this is divided into 4 (four) types, namely:

1. Customers / customers need to help someone (customer service, sales clerk or cashier) to guide or obtain information about everything related to the product. Starting from searching for the desired product, choosing a product, asking for an explanation about the product to payment at the cashier.

2. Customers / customers need assistance only as needed, meaning that customers come in and then search for themselves, choosing themselves only last to contact the officer when paying.
3. Customers need help but by telephone. so in this case the customer does not face physically with us, but only through voice.
4. The customer / customer does not need to ask for help from the officer if it is not in an emergency, meaning that the customer is in this case a machine such as an automatic teller machine (ATM).

According to Pasuraman there are five dimensions of service, namely:

- a. Tangible, namely the ability of a company to show its existence to external parties. Appearance and capability of the company's physical facilities and infrastructure that can be relied on in the circumstances of the surrounding environment are concrete evidence of the services provided by service providers. This includes service waiting rooms, equipment used and Appearance of Service Officers.
- b. Reliability is the ability of the company to provide services as promised in an accurate and reliable manner. The performance must be in accordance with customer expectations, the reliability of the officers in providing service information, the officers 'accuracy in smoothing the

service procedures, and the officers' accuracy in facilitating technical services.

- c. Responsiveness is a policy to help and provide fast and appropriate services to customers by delivering information.
- d. Guarantee and Certainty (assurance), namely knowledge, politeness of compensation and the ability of company employees to foster a sense of customer trust in the company. This includes the administrative ability of service personnel, the technical capabilities of service personnel and the social ability of service personnel.
- e. Empathy that is giving sincere and individual or personal attention given to customers by trying to understand the desires of consumers. This includes the attention of service personnel, caring officers and the friendliness of service personnel.

Parasuraman, Zeithaml and Berry (1991) form a service quality model that highlights the main requirements that provide the quality of service expected.

The model identifies five gaps that result in failure of service delivery, namely:

- 1) The gap between consumer expectations and management perceptions. In this case, management does not always understand exactly what the customer wants.
- 2) The gap between management perceptions and service quality specifications. In this case management may be

correct in understanding customer desires, but not setting specific implementation standards.

- 3) Gap between service quality specifications and service delivery. In this case the personnel may not be well trained and unable to meet the standards.
- 4) The gap between service delivery and external communication. In this case consumer expectations are influenced by statements made by representatives and advertising of the company.
- 5) The gap between services experienced and services expected. In this case, it occurs when consumers measure the company's performance in a different way and have a wrong perception about the quality of service.

For the calculation of SERVQUAL scores, we can use the calculation formula as follows (Zeithaml, 1990): $\text{SERVEQUAL Score} = \text{Perception Score} - \text{Expectation Score}$ By comparing the expectations and perceptions of customers, their satisfaction will be known, both for each attribute, dimension, and overall. But in its use there are several disadvantages, namely:

1. SERVEQUAL only measures two factors: intrinsic service quality and extrinsic service quality. Does not measure construct in service quality (Lovelock, 2004).
2. To implement SERVEQUAL, specific definitions are needed that can be operationally applied to each service industry (Jasfar, 2003).

There are several dimension models and service quality models in Islamic banks, namely:

1. Model Othman and Owen (2001)

In the last few decades, researchers have acknowledged the need to make a measure of service quality to improve the service industry. Servqual (Service quality) is indeed proven as a method that can be accepted as a measurement. However, service quality measurements face many criticisms. Othman and Owen introduced an alternative in measuring service quality called CARTER (Compliance of law, assurance, reliability, tangibility, empathy and responsiveness).

- a) Compliance is compliance which means the ability to submit to Islamic law and operate according to Islamic banking and economic principles.
- b) Assurance is the knowledge and politeness of employees and their ability to convey truth and confidentiality. This also includes verbal and written communication between bank employees and customers.
- c) Reliability is the ability to provide promised, consistent and accurate services.
- d) Tangible (reality) which means the appearance of physical facilities of equipment, personnel and communication material.
- e) Emphaty (empathy) is an individual's attention where Islamic banks provide it to consumers.
- f) Responsiveness is the willingness to help consumers and provide requested services.

2. Jabnoun and Khalifa Models (2005)

The quality of service component according to this model was developed through brainstorming and training. This model asks 15 managers who take TQM (Total Quality Management) courses in the MBA program at Sharjah University using 5 dimensions of Servqual plus 2 other dimensions, namely: Value and Images.

3. Model al-Zaabi (2006)

Zaabi uses Servqual modified to measure customer perceptions about the quality of service in Islamic banks. Zaabi includes variables that directly affect perception through other dimensions of servqual. These variables are: Shariah compliance in Islamic banking services and products, competitive costs, competitive financial levels, good profit and loss sharing, Islamic bank employee awareness, Sharia bank performance

8.3 Summary

- The fundamental difference between conventional banking and Islamic banking which is based on interest and profit sharing is not enough to maintain customer loyalty. There are many factors that can be used as reasons for customers to remain loyal to financial institutions. One of them is excellent service (service excellence).
- Service excellence is caring for customers by providing the best service to facilitate ease, fulfillment of needs and realize their satisfaction, so that they are always loyal to the company.

- One of the main factors for customers choosing a bank is based on the quality of service provided by the bank. The better the quality provided, the more customers will choose the bank and vice versa.
- To increase the market share of Islamic Banking is also required to have competitiveness. This of course can be achieved by having an effective marketing strategy. This is also aimed at efforts to service customers. The quality of products and services is considered a very important factor in a company because global and international markets are increasingly developing.

CHAPTER 9

CONCLUSION

Islamic economics has two main things that become the legal basis of the Islamic economic system, namely the Quran and Sunnah of the Prophet, the laws taken from both of these basic principles in concept and principle are fixed (cannot change at any time and anywhere). The following are some of the meanings of Islamic Economics from several book sources:

1. According to Monzer Kahf in his book *The Islamic Economy* explains that Islamic economics is part of an interdisciplinary economics in the sense that the study of Islamic economics cannot stand alone, but it needs good and deep mastery of the sharia sciences and the supporting sciences as well towards sciences that function as tool of analysis such as mathematics, statistics, logic and ushul fiqh (Rianto and Amalia, 2010: 7).
2. M.A. Mannan defines Islamic economics as a social science that studies people's economic problems inspired by Islamic values (Mannan, 1992: 15).
3. The definition of Islamic economics based on the opinion of Muhammad Abdullah Al-Arabi (1980: 11), Islamic Economics is a set of general economic basics that we conclude from the Qur'an and the Sunnah, and is a building the economy that we establish on the basis of these

foundations is in accordance with each environment and time.

Sharia Economic Goals are aligned with the objectives of Islamic law itself (*maqashid asy shari'ah*), which is to achieve happiness in the world and the hereafter (*falah*) through a good and honorable system of life (*hayyah thayyibah*). The objective of the Sharia Economy to be achieved includes the micro or macro aspects, including the world time horizon or the hereafter (P3EI, 2012: 54). An Egyptian *fuqaha* named Prof. Muhammad Abu Zahrah said there were three objectives of Islamic law which showed that Islam was revealed as a blessing for all humanity, namely (Alqaoud, 2005).

1. Cleansing the soul so that every Muslim can be a source of good for the community and its environment.
2. Upright justice in society. Justice in question covers aspects of life in the field of law and *muamalah*.
3. The achievement of *maslahah* (the peak). The scholars agreed that the *maslahah* which became the peak of the above targets included five basic guarantees, namely: the safety of religious beliefs (*al din*), the salvation of the soul (*al nafs*), the salvation of reason (*al aql*), family safety and descent (*al nasl*) and salvation property (*al mal*).

The implementation of Islamic economics must carry out the following principles (Prasetyo, 2012):

1. Various resources are seen as gifts or deposits from Allah to humans.

2. Islam recognizes private ownership within certain limits.
3. The main driving force of Islamic Economics is cooperation.
4. Sharia economy rejects the accumulation of wealth controlled by a few people.
5. Sharia economy guarantees community ownership and its use is planned for the benefit of many people.
6. A Muslim must fear Allah Almighty and the day of determination in the hereafter.
7. Zakat must be paid for wealth that has met the limit (*Nisab*).
8. Islam forbids usury in all forms.

Like a building, the Islamic economic system must have a useful foundation as a foundation and be able to sustain all forms of economic activity in order to achieve noble goals. The following are the basic principles in Islamic economics, including (Booms, 1981):

1. Do not hoard (*Ihtikar*). Hoarding, in Arabic is called *al-ihlikar*. In general, *ihlikar* can be interpreted as an act of buying merchandise with the aim of holding or storing the item for a long time, so the item is declared a rare and expensive item.
2. Do not do monopoly. Monopoly is an activity to hold the goods from being sold or not circulated in the market, so that the price becomes expensive. Monopoly activity is one of the things that is prohibited in Islam, if the monopoly is created intentionally by hoarding goods and increasing the price of goods.

3. Avoid prohibited sales. Buying and selling activities that are in accordance with the principles of Islam, fair, lawful, and do not harm one of the parties are those which are greatly appreciated by Allah. Because indeed that everything that contains elements of *munkar* and disobedience is unlawful.

If implementing the Islamic economy will bring great benefits for Muslims by itself, namely:

1. Realizing the integrity of a disgraceful Muslim, so that Islam is no longer half-hearted. If it is found that there are Muslims who are still struggling and practicing conventional economics, showing that their Islam has not been broken.
2. Implementing and practicing Islamic economics through Islamic financial institutions, whether in the form of banks, insurance, pawnshops, or BMT (*Baitul Maal wat Tamwil*) will benefit the world and the hereafter. Profits in the world are obtained through profit sharing, while the advantage in the afterlife is free from the element of usury which is forbidden by Allah.
3. Economic practices based on Islamic law contain the value of worship, because they have practiced the sharia of Allah.
4. Implementing Islamic economics through Islamic financial institutions, means supporting the progress of Islamic economic institutions.
5. Implementing Islamic economics by opening savings, deposits or becoming a sharia insurance customer means supporting efforts to empower the people of the economy.

Because the funds collected will be collected and channeled through the real trade sector.

6. Implementing the Islamic economy means supporting the movement of the *amar ma'ruf nahi munkar*. Because the funds collected Sharia financial institutions can only be distributed to lawful businesses and projects.

Disputes in the field of Islamic economics are disputes in the fulfillment of rights and obligations for parties who are bound in the contract of sharia economic activity (Ahmad, 2014).

1. The Way of Peace (*as-shulh*) There are three pillars that must be fulfilled in the peace agreement that must be carried out by people doing peace, namely consent, *qabul* and forgiveness from the peace agreement. If all three of these have been fulfilled, the agreement has proceeded as expected. From the peace agreement was born a legal bond, each party is obliged to carry it out. Please note that the agreed peace agreement cannot be canceled unilaterally. If there are parties who do not agree to the contents of the agreement, then the cancellation of the agreement must be with the agreement of both parties (Ghozali, 2001).
2. In Arbitration (*at-tahkim*) or Sharia Arbitration. Arbitration is an alternative institution held by and based on the will and good faith of the disputing parties so that their disputes are resolved by judges they appoint and appoint themselves, with the understanding that the decision taken by the judge is a decision that is final and binding on both parties to carry it

out (Gunawan Widjaja & Ahmad Yani, 2001, p. 16) The implementation of this arbitration must be based on the Qur'an, Hadith, and Ijma.

3. Through the Judiciary (*al-qadha*) or the Religious Courts. If the parties are in dispute, do not succeed in doing *as-shulh* or *at-tahkim*, or the parties do not want to do both methods, then one party can submit the matter to the Religious Court.

Banking business is a service business that is based on the principle of trust so that the problem of service quality is a very decisive factor in business success. Service quality is a form of consumer assessment of the level of perceived service with the expected service level. The increasingly intense competition in the banking industry encourages the banking industry to be fast adjust to the development of the surrounding community. This was marked by the increasingly widespread expansion of foreign banks trying to enter the banking market in Indonesia. The banking industry is currently competing to improve services to customers, by providing facilities that make it easier for customers to conduct financial transactions (Infobank, April 2008).

Strict competition between Islamic banks and conventional banks increases customer standards for banking services. So that the approach to using Islamic sentiment is no longer effective. People who are accustomed to conventional systems and have the image that conventional bank services are better than Islamic banks are a challenge for Islamic banks to find a more appropriate strategy to maintain customers and increase market share. The emergence of the

concept of Islamic banks in Indonesia is made possible through the National Banking Act No. 7 of 1992 which states that banks are possible with a profit sharing system which ultimately inspires the birth of Bank Muamalat Indonesia. In line with the emergence of a monetary crisis which eventually became an economic crisis in Indonesia, which was marked by the number of liquidated banks. On the other hand, Bank Muamalat Indonesia still maintains its operations.

The amendment of Law No.7 of 1992 to Law (UU) No. 10 of 1998 increasingly provided the stimulus for the emergence of Islamic banking in Indonesia. Because in the new law it is stated that it is possible for banks to operate in two systems, namely conventional banks and Islamic banks (dual banking system).

As of June 17, 2008, the Indonesian Islamic banking industry officially entered a new era. The Sharia Banking Bill, which has entered the House of Representatives since mid-2005 as a bill on the initiative of the House of Representatives, has been ratified so that Indonesia now officially has sharia banking regulations, namely Law Number 21 Year of Islamic Banking (Koksal, 2014).

Conceptualization and measurement of service quality perceptions is one of the most contentious and controversial contemporary topics in the literature - marketing services (Brady and Cronin, 2001; Zeithaml, 2000; Mavry, 2008; Rust and Oliver, 2000; Warsono, 2010). Because services are intangible, consumers value quality subjectively. As perceived quality services / products have been referred to as "difficult to understand" (Consuegra, 2007; Effendy,

2014), and various studies assume that this construct is still considered "unresolved" (Laksono, 2011).

CHAPTER 10

CONDITION OF SHARIA BANKING IN MALANG CITY

Facing the challenges of sharia banking in 2017 all the leaders of Bank Rakyat Indonesia and branches held a coordination meeting to organize the strategy. Located at Harris Hotel Convention Malang, the event which was attended by the President Director of PT BRI BRI Syariah Moch Hadi Santoso was held as an evaluation and structuring of management strategies and development in the Islamic economic sector.

To Jawa Pos Radar Malang, Hadi did not deny that the growth of sharia banking in 2016 was not as great as in 2013. The reason was, it was due to the impact of global economic conditions which are currently also unstable. "But thank God, the effect of Trump has so far not affected the stability of Islamic banks," said Hadi. Speaking about the growth of Islamic banking in the city of Malang, Hadi assessed the progress of BRI Syariah Malang was very good. The target of economic growth that exceeds the central target makes Malang City one of the spearheads of the national Islamic economic movement. "Malang is the best city in East Java after Surabaya, the progress is extraordinary," he explained.

The instability of Islamic banking conditions, Hadi said, was caused by several factors such as the selling value of world coal, palm oil, stocks and oil which continued to move fluctuatively. For the target market share BRI is optimistic in the coming 2017 they can exceeded this year's target. "Now we have exceeded 5 percent to

5.13 percent. "Next year's target is to increase to 17 percent," said Hadi.

If the BRI Syariah center targets to increase to 17 percent, the Malang Branch of Islamic Banks has gone far with the target of 24 percent. "If the center raises the target, we also have to follow, we are targeting to increase to 30 percent," said Branch Manager of BRI Syariah Malang Miftahul Ulum. As an evaluation of the Malang Branch of BRI in line with Hadi, Ulum agreed that the property sector would be their development priority. "So far, we have implemented a public housing credit (KPR) model, which we will continue to develop," said Ulum.

Furthermore, the man who also served as chairman of the Malang Branch of the Indonesian Sharia Bank Association (Asbisindo) said that the program segmentation would be expanded. "What is clear is that we will cover all segments, ranging from subsidized housing to elite housing," explained Ulum. As a target, Ulum said that he would also continue to make improvements in terms of services ranging from service quality, speed, to improving the quality of their human resources (<http://bisnis.radarmalang.id/2017-bri-syariah-bidik-sektor-properti/>)

In the last seven years, Islamic banks have grown rapidly. In fact, it beats the growth of conventional banks. On average, the growth of Islamic banks reached 24 percent, while the growth of banks conventional only 10 percent. This was revealed by the Executive Vice President of Bank Syariah Mandiri (BSM) Achmad Fauzi when he was a speaker at the Islamic University of Malang (Unisma)

yesterday (13/5). "So, it is very appropriate if in 2017 Unisma opens a syariah banking department," explained Fauzi before the students and lecturers of the Unisma Faculty of Economics.

Fauzi explained, of the 119 banks in Indonesia, 34 of them had implemented the sharia system. "Although the numbers are still small, but the development is fast," he said. "For example, BSM has been ranked 18th among other banks in Indonesia," he added (<http://www.radarmalang.id/bank-syariah-tumbuh-pesat/>).

Efforts to combat moneylenders are now being fueled by many parties. Malang Mayor, HM Anton, said that the effort could be achieved by optimizing many parties, including utilizing cooperatives. "We have cooperated with many circles, including cooperatives, Baznas and so on, to combat moneylenders," Anton said.

As a teacher in the world economy, cooperatives are expected to be able to grow Micro, Small and Medium Enterprises (MSMEs) through cheap and easy capital injections. "We hope a lot from the role of this cooperative," he said. The same effort was apparently carried out by Bank BNI Syariah Malang. They are currently collaborating with microfinance institutions and Islamic cooperatives to combat moneylenders. Some financial institutions that have signed the cooperation include Baitul Maal wat Tamwil (BMT) Sidogiri,

Puskopsah, Masalahah Cooperative and Al Yasini Islamic Boarding School Cooperative.

"Collaboration for savings and loan needs and sharia credit. We chose this financial institution because the Ministry of Cooperatives was considered healthy and worthy to cooperate with banks," said BNI Syariah Branch Head, Yudi Trisnavastiah. The financial institution also markets a number of banking products, such as credit for the micro industry starting from Rp. 5 million - Rp. 50 million.

This pattern of cooperation is considered beneficial for both parties. Evidently the collaboration contributes to the funds collected reaching Rp 450 billion. While BNI Syariah data mentions, financing disbursement in 2015 amounted to Rp 231 billion (<http://malangvoice.com/bni-syariah-malang-serius-perangi-rentenir/>).

BNI Syariah Malang City enters a new phase in early August 2017. Starting this month, this subsidiary of Bank Negara Indonesia (BNI) has a new skipper from the general meeting of shareholders (GMS) last week.

BNI Syariah President Director Imam Saptono said, his party would still focus on the consumer segment. At present, BNI Syariah's consumer financing portfolio is 50%, especially housing loans (KPR). In addition, BNI Syariah will fatten the financing sector of micro, small and medium enterprises (MSMEs). In this segment, BNI Syariah targeting the financing market ranging from Rp. 1 billion to Rp. 15 billion.

There is also a commercial financing sector with ceilings ranging from Rp. 15 billion to Rp. 200 billion. In general, Imam added, he focused on working on sectors that rely on the domestic economy.

Because, global economic conditions are still unstable. The total financing targeted by BNI Syariah this year is IDR 20.7 trillion or grew 16.9% compared to December 2015 which was IDR 17.7 trillion.

Senior EVP of BNI Syariah, Dhias Widhiyati, said that his company would also maximize financing from the parent company. BNI Syariah Strategy, this year's financing targets prospective borrowers who enter the business chain financed by the parent of BNI.

Simply put, BNI Syariah works on a company with the status of a subsidiary or partner company that has become a BNI debtor. Through this strategy, the risk of non-performing financing can be minimized. BNI Syariah will also expand into mutanaqisah (MMQ) and ijarah muntahiya bittamlik (IMBT) based financing agreements. The reason, two types of contracts have great potential. Various financing strategies are believed to boost profits. This year, BNI Syariah believes it can pocket a profit of Rp 290 billion or grow 27.19% compared to the same period last year which amounted to Rp 228 billion. In terms of liquidity, third party funds (TPF) are targeted to increase by IDR 3.5 trillion to IDR 23.3 trillion at the end of 2016. This target is up 17.67% from the previous position of IDR 19.8 trillion.

Thus, the financing to financing ratio (FDR) of BNI Syariah is predicted to loosen from the 92% level at the end of the year to 86% this year. The company also still hopes for additional liquidity from the hajj savings that still settle in conventional banks. "BNI Syariah's parent company has 136,000 Hajj savings customers with a total

balance of Rp 700 billion," Imam said last weekend. Although plans to spur financing, BNI Syariah has not planned to release debt instruments. Because, at this time BNI Syariah's liquidity is overstated after Bank Indonesia (BI) lowered interest rates. Meanwhile, in terms of asset acquisition, BNI Syariah targets asset growth to reach Rp. 26.3 trillion. This figure is up 14.34% compared to last year which amounted to Rp 23 trillion.

PT Bank Muamalat Indonesia Tbk yesterday (30/1) launched priority services. The first Islamic bank in Indonesia could only launch priority services because last year it was still struggling with fund recomposition. Bank Muamalat last year managed to reduce the cost of funds by 1.2 percent. "Our funding remains selective by trying to keep up with the cost of funds that we will continue to strive to decrease," said Bank Muamalat President Director Endy Abdurrahman during the grand launching of Muamalat Prioritas yesterday.

According to him, banks must press the cost of funds so that financing can be more competitive. In terms of liquidity, Endy considered it still safe. However, he admitted that the bank also did not want excess liquidity.

Because, the decrease in cost of funds can be hampered. The Muamalat loan to deposit ratio (LDR) last year was quite large, namely 95 percent. "The growth of financing did not experience a significant increase. This year, if the government targets 9-12 percent credit growth, we target 10 percent," he said (<http:>

[//www.jawapos.com/read/2017/01/31/106133/bank-muamalat-l](http://www.jawapos.com/read/2017/01/31/106133/bank-muamalat-l)
Launch-prioritas-syariah#).

The results showed that in the implementation of the calculation of profit sharing of *mudharabah* financing at Bank Muamalat Indonesia Malang Branch using revenue sharing method in which the income or sales proceeds obtained by the customer multiplied by the percentage ratio agreed at the beginning of the cooperation agreement without having to reduce the business operating expenses, calculation This is to find out the amount of principal installments that must be paid by the customer and how much the results obtained by the bank. This method is chosen by the bank because when using the profit / loss sharing method it is possible that the funds will be mixed with the customer's business capital and to avoid unwanted risks in the form of loss or reduced capital provided by the bank to the customer.

The results obtained are fluctuating from the income or proceeds from the sale of the business received every month, for that the customer must report the profit and loss condition of his business every month to the Bank Muamalat Indonesia Malang Branch. Therefore, Bank Muamalat Indonesia Malang Branch distributes *mudharabah* financing to financial institutions, namely BMT, BPRS, Sharia cooperatives, cooperatives savings and loans, KPRI because it is more effective and avoids unwanted risks (<https://zelikalaila.wordpress.com/2017/05/09/studi-pada-bank-muamalat-indonesia-cabang-malang/>).

CHAPTER 11

CONDITION OF SHARIA BANKING IN JAKARTA

The Financial Services Authority (OJK) recorded the market share of market growth of sharia banking to 4.86% until July 2016. This position rose when compared to last year in the same period which was 4.46%.

OJK Deputy Commissioner for Banking Supervision I Mulya E Siregar said that the market share of Islamic banking is expected to continue to increase. According to him the market share of sharia banking is 4.86%, in line with the improving national economic conditions that have impacted the market share of Islamic banking. "Economic conditions can encourage the participation of Islamic banking. In the midst of a world economic slowdown, Indonesia still shows positive numbers and happens to also be banking on sharia," Mulya said in a written statement in Jakarta, Tuesday (09/27/2016).

He further hoped that the market share of Islamic banking could be increased again. Considering, the majority of the population in Indonesia is Muslim. According to him, the potential of Islamic banking is very large. "Share rose compared to the previous year, up from 4.6% in July last year, to 4.86% as of July 2016. However, this share has not taken into account in September. Market share can be more than 5%," he said. The OJK will also hold the Indonesia International Conference on Islamic Finance on September 29, 2016 at the Fairmont Hotel, Jakarta. In the conference will be discussed

about the challenges of the Islamic financial industry in facing the normal new cycle of the era in the global economy.

His Majesty explained that the new normal era was a new era where an economy that was in a fluctuating condition or up and down and economic actors were accustomed to these conditions. The new normal condition of this era will be elaborated in more detail in the conference with two discussion discussions namely from the regulator and sharia financial industry. "In terms of regulators will be discussed how the strategies and policies to deal with the impact of the economic slowdown on the Islamic financial industry. Then, in terms of the Islamic financial industry will be discussed how to deal with the new normal era in order to survive," he said.

Furthermore, it is expected that through the discussion held at the conference it can map the Islamic finance industry in the future, and encourage the growth of the sharia financial industry in a fluctuating economic era. In addition, the series of Indonesia International Conference on Islamic Finance will also be connected with the Global Islamic Finance Awards event. In the event President Joko Widodo will be awarded as the 2016 Global Islamic Finance Leadership Award. The Indonesia International Conference on Islamic Finance will be attended by a number of speakers from several countries including Deputy Governor of State Bank of Pakistan Saeed Ahmad, Kazakhstan Governor of Astana International Financial Center Kairat Kellimbatov, Assistant Governor of Bank Negara Malaysia Bakarudin Ishak, and CEO of Edbiz Consulting London Humayon Dar

(<https://ekbis.sindonews.com/read/1142707/178/market-share-bank-syariah-terus-increased-1474974140>).

The national Islamic banking industry still recorded quite encouraging growth in 2016 amid unfavorable economic conditions. From the asset side and market share, national Islamic banking posted significant growth. Secretary of the Jendeeal Association of Indonesian Islamic Banks (Asbisindo) Achmad K Permana said, as of September 2016 the total assets of Islamic banking reached Rp 331.76 trillion. The figure increased by 17.58 percent compared to the same period in the previous year. "We can still grow almost 18 percent was driven first by the conversion. Beyond that we were also supported by the growth of hajj funds and Islamic finance campaigns," Permana said at a press conference in Jakarta, Monday (11/21/2016).

According to Permana, the total asset growth of sharia banking was supported by an increase in third party funds (DPK) of 20.16 percent to Rp. 263.52 trillion. As for the financing of sharia banking recorded an increase of 12.91 percent reaching Rp 235.01 trillion. Accordingly, the market share of Islamic banking for the national banking industry reached 5.3 percent. Thus, the national Islamic banking industry has managed to surpass the 5 percent market share growth trap. "We have reached a market share of more than 5 percent. That is a psychological limit or a 5 percent trap," Permana said. According to Permana, the achievement of the performance of the sharia banking industry should be grateful. The reason is this achievement recorded in the midst of domestic and global

macroeconomic situations that are less conducive to business growth (http://ekonomi.kompas.com/read/2016/11/21/154101926/perbankan.syariah.nasional.sudah.lakhir.jebakan.pertumbuh.5.persen).

Head of Maybank Indonesia Syariah Banking Herwin Bustaman said the sharia banking industry is ready if the government is involved in the distribution of the state budget. Since 2014, he said, Islamic banks have been trusted to work on transactions with large nominal. One example is Jasa Marga's transaction which is worth Rp 1.1 trillion. "There are several large transactions that can be worked on by sharia," Herwin said, when a reporter was met at the Islamic Finance News Forum at the Four Seasons Hotel, Jakarta, Thursday (27/7). If the government wants to distribute only five percent of the total state budget through Islamic banks, Herwin predicts the industry will grow rapidly. Because, that means there will be funds of around Rp 100 trillion to be worked on by Islamic banks. Meanwhile, the banking industry in general is only currently working on IDR 389 trillion.

If the proposal is made, Herwin also believes that Islamic banking is able to achieve the target market share of 10 percent faster. "If that can be done it's really good." The proposal regarding the distribution of APBN through Islamic banks was first conveyed by the Chairman of the Indonesian Ulema Council Ma'ruf Amin. He hopes that 10 percent of the state budget funds of around Rp 2,000 trillion can enter the sharia financial system. He thinks that this needs to be done to encourage the development of Islamic economics in the country

([http://www.republika.co.id/berita/ekonomi/syariahekonomi/17 / 07/27 / otrd9t299-banking-sharia-ready-if-requested-channel-apbn](http://www.republika.co.id/berita/ekonomi/syariahekonomi/17/07/27/otrd9t299-banking-sharia-ready-if-requested-channel-apbn)).

The Indonesian Ulama Council (MUI) suggested that the government could channel 10 percent of the State Budget (APBN) funds through Islamic banks. The goal is that Islamic finance can grow quickly.

Deputy Chairman of the National Sharia Council (DSN) MUI and Sharia Economic Observer Adiwarman A Karim said, the new flow of Indonesia's economy must reflect circular dependencies between the top-down approach and the bottom-up approach. This is to develop the economy. "Building mutual trust between the government and the community in development is mutually recursive," he told *Republika* on Wednesday (7/26). So, according to him, economic empowerment of the community needs to go through various government programs and the economic power of the community. "The government's program and the economic strength of the community through self-managed self-financing are waqf activities. So waqf is a form of joint responsibility of the government and society in developing Indonesia," Adiwarman explained. He said, endowments have similarities with some long term funding such as sovereign wealth funds. However, there are some limitations that distinguish it from other long term funding. "So it must be considered not to violate sharia," said Adiwarman. Thus the distribution of APBN funds through Islamic banks may not leave sharia rules ([http://www.republika.co.id/berita/ekonomi/syariahekonomi/17 / 07/26 /](http://www.republika.co.id/berita/ekonomi/syariahekonomi/17/07/26/)

otpb86415-questions-distribution-apbn-through-bank-shariah-ini-kata-dsn-mui).

Sharia Economic Researcher Aziz Setiawan assesses, the idea and proposal of the Indonesian Ulema Council (MUI) so that 10 percent of the APBN funds are channeled through Islamic banks both for the acceleration of Islamic finance. Technically, 10 percent of the state budget does not mean that funds are deposited.

Because the APBN is in the current year revenue is used directly for state expenditure. So, he said, it was not automatic that the Rp. 2,000 trillion state budget would increase the assets of Islamic banks to Rp. 200 trillion. But its nature will increase spinning liquidity through Islamic banks at that rate in one year. "But I think this is one part of many policies that can be taken by the government to spur the growth of Islamic finance," said Aziz, when contacted by *Republika* on Wednesday (7/26). According to him, the distribution of APBN funds through Islamic banks will significantly increase liquidity even though it has not spurred an increase in the assets of Islamic banks. Asset enhancement that might be done is from the conversion of state-owned banks or transformation from BUMN subsidiaries to state-owned enterprises by capital injection through large State Capital Investment (PMN), or mergers with large capital injection from the government.

Aziz hopes, in addition to pushing the State Budget via Islamic banks that can increase liquidity, there are also more progressive Sharia National Finance Committee (KNKS) policies to increase assets and market share. He stated, the government's role for

developing Islamic banks is still not visible. The issue of Islamic banks and Islamic finance is still just rhetoric from the government. With the new Islamic bank assets of Rp. 357 trillion or a new market share of 5.18 percent compared to large potential, the development of Islamic banks is still tending to be bottom up or market driven, because there are no significant government policies. Therefore, if the APBN is channeled through Islamic banks, it can increase the assets of Islamic banks themselves. "But maybe the MUI does not have too much detail related to the mechanism of the state budget funds that are funded in one fiscal year, which does not automatically boost assets by 10 percent from Rp. 2,000 trillion," explained Aziz.

Because, he continued, in the APBN practice, the funds that settle in the whole bank are only hundreds of trillions. Because, state revenue is then directly used for state expenditure. "The proposed MUI is good, but other policies that are strategic as above need to be encouraged through the KNKS," he said (<http://www.republika.co.id/berita/ekonomi/syariah> Ekonomi / 17/07/26 / otpae5415-this-how-to-speed-sharia-financial-rate-).

National Islamic banking in the February 2017 period is still growing positively. Call it in terms of capital, based on data from the Financial Services Authority (OJK) the growth of the capital adequacy ratio of Islamic banks (BUS) was recorded at 1.64% on an annual basis to 17.04% .b Then, in terms of assets, Islamic banks recorded Rp. 355, 88 trillion. This amount contributed 40% for the national Islamic finance industry. Meanwhile, in terms of financing

recorded a growth of Rp 252.69 trillion or grew 16.22% compared to the same period the previous year of Rp 217.4 trillion. While for third party funds (DPK) was recorded at Rp. 287.08 trillion or grew 21.28% compared to the same period last year of Rp. 236.7 trillion.

According to the OJK the intermediation of Islamic banks is still going well, this is reflected in the Financing Deposit Ratio (FDR) for Islamic Commercial Banks (BUS) and Sharia Business Units (UUS) which are at 87.45%. Operating Expenses and Operating Income recorded 89.22% down 175 basis points compared to the same period the previous year.

"OJK as a regulator will continue to strive to encourage the growth of the Islamic financial services industry in the country. Among others, by increasing public understanding of Islamic financial products and services," said Deputy Commissioner of OJK Non Bank Financial Industry Supervisory I Edi Setiadi, in a statement written, Saturday (29/4/2017).

Sharia subsidiary of Bank Negara Indonesia (BNI), based on the company's financial report as of the first quarter of 2017, recorded total assets of Rp. 29.86 trillion or grew by 21.01% compared to the same period in the previous year of Rp. 24.68 trillion. This was supported by financing that grew by 17.83% and third party funds (DPK) to Rp 4.89 trillion or grew 23.38%.

In addition to BNI Syariah, CIMB Niaga Syariah as of the first quarter of 2017 also recorded positive growth, to finance Rp 10.98 trillion or grow 44.5% on an annual basis. Then TPF was recorded at

Rp. 9.71 trillion or grew by 19%. From the first quarter 2017 financial statements, Bank Mandiri Syariah recorded total assets of Rp. 80 trillion. Then the total financing was IDR 55.4 trillion and the total DPK was IDR 71 trillion (<https://finance.detik.com/moneter/3487471/how-is-the-banking-syariah-condition-ri-this-explanation-ojk>).

Governor of Bank Indonesia (BI) Agus DW Martowardojo said the development of Islamic commercial finance in Indonesia has experienced a downward trend in line with the conditions that occur in the development of global sharia commercial finance.

This was particularly the case in the period 2012 to 2015. In 2015, the growth of Islamic banking reached its lowest point on an annual basis, which was 8.8 percent. This was compared to 9.2 percent growth in conventional banking on an annual basis. However, in 2016, the growth of Islamic banking in Indonesia rebounded to reach 12 percent on an annual basis (year on year / yoy).

Meanwhile, conventional banking growth only reached 7.2 percent (yoy). Despite achieving double-digit growth, Islamic banking still has a stagnant market share of 4.8 percent. "Nevertheless, Indonesian Islamic banking is claimed to be the largest sharia retail banking in the world with more than 18 million customers and more than 4,500 branch offices in the year 2015," Agus said in his remarks at the Indonesia Syari'a Economic Festival in Surabaya, East Java, Thursday (27/7/2017). On the occasion, Agus also highlighted the development of sukuk in Indonesia which showed a downward trend

in corporate sukuk in the period 2009-2014 and government sukuk in the 2011-2014 period.

However, sukuk growth has rebounded by 39.4 percent in 2015 and 29.8 percent in July 2016 for corporate sukuk. Meanwhile, government sukuk growth in 2015 reached 39.7 percent and 36.28 percent in July 2016. The sukuk market share in July 2015 reached 3.8 percent for corporate sukuk and 15.6 percent for government rate (http:

[//ekonomi.kompas.com/read/2017/7/27/124500226/perbankan.syariah.indonesia.diklaim.sebagai.yang.terbesar.di.dunia](http://ekonomi.kompas.com/read/2017/7/27/124500226/perbankan.syariah.indonesia.diklaim.sebagai.yang.terbesar.di.dunia)).

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