

Comparative Study of Financial Performance of Islamic Banks and Conventional Banks in Indonesia

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Abstract

The presence of Islamic banks with the concept of profit sharing has created new competition in the national banking business. Since its inception, Islamic banks have been required to improve their performance to compete with conventional banks, which have long dominated the market share. This study aims to compare Islamic and conventional banks' financial performance in Indonesia for the 2016-2020 period. The research method used is comparative research with a quantitative approach. The research sample consisted of Islamic and conventional banks, each taken by the five largest banks based on asset value. Samples were taken using a purposive sampling technique. Data collection techniques using documentation. The data type used is secondary data in the form of financial ratio reports obtained through the official OJK website. Data analysis techniques used descriptive and comparative analysis in the form of independent sample t-test and Mann-Whitney test. The results of this study indicate that Islamic banks have better performance than conventional banks in terms of the CAR ratio. However, when viewed from the ratio of NPL/NPF, ROA, NIM/NOM, BOPO, and LDR/FDR, Conventional Banks have a better performance. Based on the results of the different tests, it was found that there was no significant difference between the performance of Islamic banks and conventional banks when viewed from the CAR ratio. However, when viewed from the ratios of NPL/NPF, ROA, NIM/NOM, BOPO, and LDR, there are significant differences between the financial performance of Islamic and conventional banks.

Keywords: Financial Performance; Islamic Banks; Conventional Banks; Financial Ratios

A. Introduction

Since the enactment of the dual banking system in Indonesia in 1998, the growth of Islamic banking has continued to increase. Islamic banking experienced a peak growth in 2009-2013, with an average asset growth of 43% in five years. This positively impacts the issuance of Law Number 21 of 2008 concerning Islamic banking.

However, in 2015 Islamic banking experienced a drastic slowdown in growth. Islamic banking assets were only able to grow by 7.98%, much lower than in 2013, which was recorded to increase by 49%. Channeled Financing (PYD) only grew by 5.55%, lower than conventional banking credit growth of 8%. The declining absorption of third-party funds by Islamic banks triggered this. In addition, the problem of inefficient operational

cost management and the increasing ratio of non-performing to financing (NPF) non-performing financing (NPF) to 4.89% are also contributing factors (Rossiana, 2015).

Compared to the development of Islamic banking (Bank Islam) in neighbouring Malaysia, as of December 2019, the market share of Islamic banking has reached more than 20% of the total banking market share in the country. Malaysia is recorded to have 16 Islamic Commercial Banks, with total assets of Islamic Banks in Malaysia reaching USD 254 billion or equivalent to IDR 3,556 trillion (exchange rate of IDR 14,000) and total deposit placement reaching 38% of the total third-party funds in Malaysia (Central Bank of Malaysia, 2020).

When viewed from the history of the birth of Islamic banks is the result of the thoughts of Muslim figures for the needs of Muslims; of course, Indonesia is a country with great potential in developing Islamic banking. This is supported by the large Muslim population in Indonesia, even occupying the first position of the largest in the world. However, the fact is that the market share of Indonesian Islamic banks is still tiny. Even much more minor than countries with smaller Muslim populations, such as Malaysia. Of course, this is very unfortunate, with the title of Indonesia as the largest Muslim country in the world.

For this reason, a more comprehensive evaluation of Islamic banking performance is needed regularly. Moreover, newly present Islamic banks must compete with conventional banks that have long controlled the national banking financial market. Therefore, a comparative performance analysis between Islamic and conventional banking is needed. So that it can be known the disadvantages and advantages between the two can then be used as evaluation material to improve the performance of Islamic banks in the future; this comparison can be made by comparing the financial performance achievements of both types of banks from previous years.

Bank performance achievements can usually be seen in the financial statements that have been published. Bank financial statements can be obtained through the OJK and each bank's websites. The bank's performance can be seen in summary from these financial statements, one of which is from the financial ratio statement. As revealed in the research, financial ratios are used as a basis for measuring bank performance (Sari & Shinta, 2019). Financial ratio analysis is to measure financial performance at banks.

An illustration of the comparison of the financial performance of Islamic Banks and Conventional Banks in Indonesia for the 2016-2020 period, as measured by banking ratios, can be seen in the following table.

Table 1. Performance Ratio of Sharia Banks and Conventional Banks 2016-2020 (%)

Ratio	ISLAMIC BANK					CONVENTIONAL BANKS					Ratio
	2016	2017	2018	2019	2020	2016	2017	2018	2019	2020	
CAR	16,63	17,91	20,39	20,59	21,64	22,93	23,18	22,97	23,40	23,39	CAR
ROA	0,63	0,63	1,28	1,73	1,40	2,23	2,45	2,55	2,47	1,59	ROA
NOM	0,68	0,67	1,42	1,92	1,46	5,63	5,32	5,14	4,91	4,45	NIM
FDR	85,99	79,61	78,53	77,91	76,36	90,70	90,04	94,78	94,43	82,54	LDR
BOPO	96,22	94,91	89,18	84,45	85,55	82,22	78,64	77,86	79,39	86,58	BOPO

Source: www.ojk.go.id

The table above shows that the Capital Adequacy Ratio (CAR) performance in Islamic banks has been in a good position and has a positive CAR growth from 16.63% in 2016 to continue to increase 21.24% in 2020. In conventional banks, CAR fluctuates from year to year. Despite the fluctuations, CAR in conventional banks is higher than in Islamic banks, with a difference of about 2% higher than in Islamic banks. However, both have met the minimum CAR standard set by Bank Indonesia at 8%.

The Profitability ratio of Return on Assets (ROA) at Islamic banks experienced quite good growth during 2016-2019 but slightly decreased in 2020 by 0.33%. In conventional banks, ROA fluctuated with the lowest value in 2020 of 1.59% after the previous four years was at an average of 2%. From the standard ROA ratio set by Bank Indonesia of 0.5%, Islamic banks are still below the set target. The profit shown by Islamic banks' Net operation Margin (NOM) ratio is still relatively small at zero point. In contrast, in Conventional banks, the Net Interest Margin (NIM) ratio is very good at above 4%. Then in terms of Operating Costs to Operating Income (BOPO), Islamic banks have a reasonably high value compared to conventional banks but continue to experience a pretty good decline throughout 2016-2020.

The Liquidity Financing to Deposit Ratio (FDR) at Islamic banks is still relatively small from the number of deposits and tends to decrease from 85% in 2016 and 76% in 2020. Meanwhile, in conventional banks, the Loan Deposit Ratio (LDR) disbursement is relatively high, in the range above 90%, although in 2020, it decreased to 82%.

The comparison was made to see the achievements of bank management in managing its operations well so that it could compete with similar businesses. Moreover, newly present Islamic banks must compete with conventional banks that have long controlled the banking financial market. The comparison is helpful for bank management as evaluation material to improve bank performance for future periods and for regulators to determine future policy directions. For investors as a guide in making investment decisions for the future.

Related to the comparison between the performance of Islamic and conventional banking in Indonesia, research has previously been conducted by (Purwanto & Juliani, 2017) with the title "Comparative Analysis of Financial Performance between Islamic and Conventional Banks in Indonesia". The findings showed significant differences in CAR, LDR, NPL and OER. While in the ROA ratio, there is no significant difference.

In addition to Indonesia, similar research is also carried out abroad using the Sharia banking system. One of them is the Pakistani state conducted by (Majeed & Zainab, 2021), "A comparative analysis of the financial performance of Islamic banks vis-à-vis conventional banks: evidence from Pakistan". The findings show that Islamic banks' capital is better, low risk and has high liquidity than conventional banks. However, in terms of profitability, Islamic banks are lower than traditional banks. In addition, a similar study was also conducted in Malaysia by (Nathan et al., 2014), "Comparison between Islamic and Conventional Banking: Evidence from Malaysia". The results showed that the profitability performance of conventional banks was better. Islamic banks performed well on liquidity and credit risk.

Based on the background presentation above and supported by several related studies. Researchers feel the need and are interested in further comparing financial performance between Islamic banking and conventional banks. Because in previous studies, the data used was old and added to the ratio to be studied. In addition, changes in economic conditions at any time also require periodic banking performance evaluation. Therefore, this study will use the latest data titled Comparative Study of Financial Performance of Islamic Banks and Conventional Banks in Indonesia.

B. Literature Review

1. Conventinal and Sharia Banks

According to the Law of the Republic of Indonesia Number 10 of 1998 dated November 10, 1998, concerning banking (Republic of Indonesia, 1998), what a bank means is *"a business entity that collects funds from the public in the form of deposits and distributes them to the public in the form of credit and or other forms to improve the standard of living of many people"*. Generally, banks' primary function is to collect public funds and distribute them back to the public for various purposes or as financial intermediaries (Hrp & Saraswati, 2020).

Islamic banks are banks that operate by not relying on interest. Islamic (Islamic) banks, or called interest-free banks, are financial / banking institutions whose operations and products are developed based on the Qur'an and Hadith of the Prophet SAW. In other words, Islamic banks are financial institutions whose primary business is to provide financing and other services in the traffic of financing and money circulation whose operations are adjusted to the principles of Islamic Sharia (Rusby, 2017).

According to Law No. 21 of 2008 concerning Islamic banking (Republic of Indonesia, 2008), "Sharia Bank is a Bank that carries out its business activities based on Sharia Principles and according to its type consists of Sharia Commercial Banks and Sharia People's Financing Banks". Sharia principles are Islamic legal principles in banking activities based on fatwas issued by institutions that have the authority to determine fatwas in the field of Sharia.

2. Functions and Objectives of Banking

Generally, banks' primary function is to collect public funds and distribute them back to the public for various purposes or as financial intermediaries (Hrp & Saraswati, 2020).

3. Fundraisers and Distributors

The bank collects funds from the community and distributes them back to the community.

4. Banking Service Provider

The Bank is banking services, such as transfers, withdrawals etc. At the same time, the function of the Bank is as an *Agent of Trust, Agent of Development and Agent of Service*.: (Dangnga & Haerudin, 2018: 17)

5. Bank Financial Ratios

Bank financial ratios are ratios used to measure the level of health of the Bank; banking financial ratios are not much different from financial ratios in general. However, banking companies have particular ratios that are only used by banks. Banking financial ratios consist of many types; in this study, not all financial ratios will be discussed; only some ratios are solvency, asset quality, profitability, BOPO, and liquidity ratios

C. Research Methods

The type of research used in this study is comparative research, with a design or quantitative approach. Comparative research is a method used to determine whether, between two variables, there are differences in an aspect under study (Lajuli, 2020, p. 40). The location of this study is at Syariah Commercial Bank and Conventional Commercial Bank, which are registered and supervised by the Financial Services Authority (OJK) which can be accessed through the official OJK website, namely www.ojk.go.id and to complete the required data can also be accessed on the official website of each bank used in this study.

The population contained in this study is all commercial banks registered with the Financial Services Authority (OJK) in 2016-2020. While the sample in this study is ten banks consisting of five Sharia Commercial banks and five Conventional Commercial Banks consisting of.

Islamic Banks:

1. Bank Syariah Mandiri
2. Bank Rakyat Indonesia Syariah, Tbk.
3. Bank Muamalat Indonesia, Tbk.
4. Bank Negara Indonesia Sharia
5. Bank Tabungan Pensiun Nasional Syariah, Tbk,

Coventional Banks:

1. Bank Rakyat Indonesia, Tbk.

2. Bank Mandiri, Tbk.
3. Bank Central Asia, Tbk.
4. Bank Negara Indonesia, Tbk.
5. Bank Tabungan Negara, Tbk.

The data used is in the form of financial report data from 2016-2010, then the analytical tools used in this study are an *independent sample t-test* and *Mann Whitney* test. *Independent sample t-test* is used if the data is usually distributed. The basis for the decision on the independent sample t-test is as follows:

1. Sig: $p < 0.05 (\alpha)$, there is a significant difference
2. Sig: $p > 0.05$, no significant difference

While *Mann Whitney* is used if it cannot test independent sample t-test because the assumption of normality cannot be fulfilled and aims to see the difference between 2 unpaired samples. The basis for the decision on the *Mann-Whitney* test is the same as the *independent test* of this t-test sample as follows:

1. Sig: $p < 0.05 (\alpha)$, there is a significant difference
2. Sig: $p > 0.05 (\alpha)$, no significant difference

D. Result and Discussion

Result

Result of Independent Sample t-test

This study used the t-test to compare Islamic and conventional banks' financial performance. Before conducting data analysis, a normality test was carried out. From these tests, the normal distribution is the NPL/NPF ratio, so this analysis can be carried out. From the calculation of the Independent sample t-test, the following results are obtained:

Table 2. The result calculation Independent sample t-test

Independent Samples Test		
	Levene's Test for Equality of Variances	t-test for Equality of Means

		F	Sig.	t	Df	Sig. (2-tailed)	Mean Difference	Std. Error Difference	95% Confidence Interval of the Difference	
									Lower	Upper
NPL/NPF	Equal variances assumed	5.368	.025	-2.609	48	.012	-.92840	.35590	-1.64399	-.21281
	Equal variances are not assumed			-2.609	40.842	.013	-.92840	.35590	-1.64724	-.20956

The table above shows that equal variances are not assumed with the value of sig. (2-tailed) of 0.013. This means that the value < 0.050 indicates a significant difference between the NPL / NPF of Islamic and conventional banks.

Test Result *Mann Whitney* Difference Test

In this study, the Mann-Whitney test was used to compare Islamic and conventional banks' financial performance. This analysis is used because the normality assumption is unmet or the data are not generally distributed for parametric statistical testing. Based on normality testing with Shapiro Wilk CAR, ROA, NIM/NOM, BOPO and LDR/FDR data are not normally distributed.

Table 3. Calculation results in Mann Whitney difference test

Test Statistics					
	CAR	ROA	NIM/NOM	BOPO	LDR/FDR
Mann-Whitney U	244.000	174.000	123.000	128.000	160.000
Wilcoxon W	569.000	499.000	448.000	453.000	485.000
Z	-1.329	-2.687	-3.677	-3.580	-2.959
Asymp. Sig. (2-tailed)	.184	.007	.000	.000	.003
a. Grouping Variable: Types of banks					

The Mann-Whitney difference test results above obtained CAR Asymp's value. Sig. (2-tailed) > 0.05 , which is 0.184, indicates no significant difference. So it can be concluded that there is no significant difference between conventional bank CAR and Islamic banks. Instead, the value of Asymp. Sig. (2-tailed) < 0.05 at ROA 0.007, NIM/NOM 0.000, BOPO 0.000 and LDR/FDR 0.003 means a significant difference. So it can be concluded that there

are significant differences in ROA, NIM/NOM, BOPO, and LDR/FDR between conventional and Islamic banks.

Discussion

Comparison of CAR Islamic Banks and Conventional Banks

Based on the results of the descriptive analysis above, it can be seen that Islamic banks have a higher percentage of CAR than conventional banks. The average CAR value of Islamic banks is 21.71%, while in conventional banks, it is slightly smaller at 20.71%. Then, when viewed from the average CAR development annually, Islamic banks had a positive performance development from 2016-2020. As shown in Figure 4.1, this shows that the CAR of Islamic banks continues to increase yearly from 17.22% in 2016 to 24.22% in 2020. In conventional banks, the annual development of CAR fluctuates slightly in each period. In 2016 it was 21.17%, down to 19.83% in 2017, then in 2019, it rose to 21.36% and fell again in 2020 to 20.09%.

Then, the results of different tests using Mann Whitney obtained the value of CAR Asymp. Sig. (2-tailed) > 0.05, which is 0.184, means no significant difference exists. So it can be concluded that there is no significant difference between the performance of Islamic and conventional bank CAR. This is also supported by the results of research (Hardianti, 2018), which found that from the CAR ratio, there is no significant difference between the financial performance of conventional and Islamic commercial banks.

From the results of descriptive analysis, Islamic banks have a reasonably good CAR performance because they can increase CAR value from year to year. From the results of the different tests, there is no significant difference between the CAR of Islamic banks and conventional banks. So it can be concluded that the performance of Islamic banks is better than conventional when viewed from the CAR ratio. Although Islamic banks have superior CAR than conventional banks, these two types of banking have met the minimum CAR standard of 8% set by Bank Indonesia, so both types of banking can be said to have outstanding capital because they are above 8%.

Comparison of NPL/NPF of Islamic Banks and Conventional Banks

Based on the results of descriptive analysis, it can be seen that conventional banks recorded an average NPL value of 2.64%, while in Islamic banks, the average NPF was

3.57%. From this, it can be seen that conventional banks' NPL value is smaller than Islamic banks' NPF. Then when viewed from the development of NPL / NPF on an average yearly basis, Islamic banks recorded NPF that moved fluctuating from 3.56% in 2016 increased to 3.99% in 2017, then fell to 3.12% in 2019 and rose again in 2020 to 3.57%. Meanwhile, in conventional banks, NPLs have tended to increase since 2018-2020 from 2.21% to 3.33%.

In the difference test using an independent sample t-test, a < 0.05 significance value of 0.013 was obtained, meaning there is a significant difference. Thus, it can be said that there is a significant difference in NPL/NPF between the performance of conventional banks and Islamic banks for the 2016-2020 period.

Based on the theory that the greater the NPL / NPF value will be equally bad, on the contrary, if the smaller, the better. From the results of the explanation above, it can be seen that the NPLs of conventional banks are smaller than those of Islamic banks. So it can be concluded that the NPL of conventional banks is better than the NPF of Islamic banks.

However, referring to the NPL/NPF standard set by Bank Indonesia, the excellent value is below 5% (Akbar, 2019: 22). On average, both types of banks have values below this standard, so it can be said that the NPL / NPF of both banks is in good condition. However, when compared between the two, conventional bank NPLs are superior to Islamic bank NPFs.

Comparison of ROA Islamic Bank and Conventional Bank

Conventional banks have an average ROA of 2.60% and Islamic banks of 2.80%. Then, if we observe the development of average ROA on an annual basis, The ROA of conventional banks tends to move steadily from 2.84% in 2016-2019 but increases in 2020 to 3.85%. Meanwhile, in Islamic banks, ROA experienced good growth from 2016-2019, from 2.44% to 3.49%, but in 2020 it fell to 2.31%

Based on the assessment of ROA, the greater the value, the better; on the other hand, if it is smaller, it will be less good. ROA shows the level of profitability performance of the bank in managing assets to generate profits. Regarding Bank Indonesia regulations, the ROA value is at least 0.5%. From the explanation above, it can be seen that the ROA of both banks is above 2%, so both have an excellent level of asset security.

Furthermore, when viewed from the results of the Mann-Whitney difference test contained in the table getting a result of 0.007, which means < 0.05 , there is a difference between the performance of conventional ROA and Islamic banks. So it can be concluded that there is a significant difference between the performance of conventional banks and Islamic banks in terms of ROA. This is also to the research results (Nurrahmania & Huda, 2021), which found a significant difference between conventional and Islamic banks. Hence this analyst concludes that the ROA of conventional banks is superior to that of Islamic banks.

Comparison of NIM/NOM of Islamic Banks and Conventional Banks

Conventional banks have an average NIM of 5.66%, and Islamic banks have 2.76%. Then, when viewed from the development of the average annual NIM/NOM, the NIM of conventional banks has decreased yearly from 6.45% in 2016 to continue to fall until 2020 to 4.45%. Meanwhile, NOM at Islamic banks experienced a pretty good average growth from 2.49 in 2016 to increase well until 2019 to 3.43% but decreased in 2020 to 2%.

NIM/NOM in banking indicates the bank's profitability level or the ability to profit from operations. The higher the value of NIM/NOM, the greater the level of profit the bank generates. Conversely, the smaller the profit, the smaller (Hasan, 2014, p. 181). The average comparison above shows that the NIM of conventional banks is greater than the NOM of Islamic banks. In terms of operating profit, the NIM of conventional banks is better than the NOM of Islamic banks.

However, even though the NOM of Islamic banks is less than the NIM of conventional banks, based on Bank Indonesia regulations, the NIM/NOM is still considered good, which is above 1.5%. From the analysis above, both banks have been above the standard quite well. So it can be said that both have a good NIM/NOM on average.

Furthermore, when viewed from the results of the difference test, it can be known in the table that shows the *value of Asymp. Sig. (2-tailed)* of 0.000 means a significant difference between conventional bank NIM and Islamic bank NOM. So it can be concluded that conventional banks have superior performance in NIM/NOM.

Comparison of BOPO Islamic Banks and Conventional Banks

The results of the descriptive analysis obtained an average BOPO value for conventional banks of 73.80% and Islamic banks of 86.73%. Then from the observation of the average annual development of BOPO the ratio of conventional bank BOPO has decreased slightly from 73.21% in 2016 down to 69.72% in 2018, then increased in 2019 and 2020 to 81.29%.

Based on Bank Indonesia regulations, the smaller the BOPO value, the better. The minimum standard BOPO value is 85%. From the results above, it can be seen that the BOPO of conventional banks, on average, is 73.80%. Meanwhile, in Islamic banks, the average BOPO value is above the Indonesian bank regulation of 86%. If the BOPO value is getting bigger, it indicates that the bank is less efficient in managing operational costs, which will impact bank profits. From the BOPO side, it can be seen that conventional banks have a better value.

Then, when viewed from the difference test results, it can be seen in the table obtained sig value. < 0.05 , which is 0.00, which means there is a difference. So it can be said that there is a significant difference in the performance of BOPO conventional and Islamic banks. This is also supported by the results of research conducted (Zulidar, 2018), which found significant differences between the performance of conventional and Islamic banks.

Comparison of LDR/FDR Islamic Banks and Conventional Banks

The average LDR of conventional banks is 89.23%, while in Islamic banks, the average FDR value is 81.22%. Then, suppose you look at the average annual development for the 2016-2020 period. In that case, it can be seen in Figure 4.6 that the LDR of conventional banks experienced fluctuating movements, increasing from 83.29% in 2017 to 93.11% in 2019 but decreasing to 83.57%. In Islamic banks, the FDR ratio tends to decrease every period, from 86.62% in 2016 to 78.19%. This means that Islamic banks' distribution of funds or financing tends to decrease.

Based on Indonesian bank regulations, the ideal value of LDR/FDR ranges from 80% - 100%. If the LDR/FDR value is below 80%, banks at less than optimal values disburse credit/financing so that it will have an impact on profit generation. However, if the

LDR/FDR value is more than 100%, it will increase liquidity risk, which will impact the shortage of funds in the event of a significant withdrawal of funds. In addition, LDR/FDR that is too high will also risk increasing bad loans or non-performing financing at banks (Adrianto et al., 2019, p. 265). For this reason, banks are required to continue to maintain the ideal value of the ratio.

From the results above, it can be seen that both types of banks have LDR/FDR values in the ideal range set by Bank Indonesia, so it can be said that both have good LDR/FDR. However, the LDR of conventional banks tends to be more stable, maintaining the ratio. So it can be said that conventional banks perform better in terms of LDR/FDR.

Furthermore, when viewed from the results of the LDR/FDR difference test contained in the table, the Asymp value is obtained. Sig. (2-tailed) < 0.0, which is 0.003, which means there is a difference. So it can be said that there is a significant difference between the LDR of conventional banks and the FDR of Islamic banks. Therefore, from this result, it is concluded that conventional banks are superior to Islamic banks. This is also supported by research results (Muchlish & Umardani, 2016), which found a significant difference between the LDR performance of conventional banks and FDR Islamic banks.

E. Conclusion

The results of the analysis and discussion of comparisons between the financial performance of Islamic banks and conventional banks for the 2016-2020 period show that Islamic banks have better CAR performance than conventional banks. However, in the ratio of NPL/NPF, ROA, NIM/NOM, BOPO and LDR/FDR, conventional banks performed better than Islamic banks. Furthermore, based on the results of the difference test, it was found that there was no significant difference between the financial performance of Islamic banks and conventional banks in terms of the CAR ratio. Meanwhile, there is a significant difference between Islamic and conventional banks' financial performance in the ratio of NPL/NPF, ROA, NIM/NOM, BOPO, and LDR/FDR.

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