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The Impact of Sectoral Financing to NPF of BPRS in Indonesia from January 2012-August 2018

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This study aims to analyse the effect of financing in the economic sector on Non-Performing Financing (NPF) in the Islamic Rural Bank (BPRS) in Indonesia in the period January 2012 - August 2018. Using quantitative methods, the data used in this study originated from Indonesia's Financial Services Authority's (OJK) official website. The research was tested using multiple linear regression analysis with a significance level of 0.05. Partially, the results of the study show that the financing variables in the economic sector of agriculture, forestry, and agricultural facilities; trade, restaurants and hotels have a significant negative effect on NPF. Meanwhile, the financing of the economic sector on the business services does not affect NPF. Simultaneously, all of the independent variables have a significant effect on NPF.

Key words: *BPRS, NPF, Financing Economic sector.*

Introduction

The Islamic Rural Bank (*Bank Pembiayaan Rakyat Syariah/*BPRS) is a financial institution that operates as an intermediary. However, in carrying out its activities, the BPRS cannot provide payment system services and focus on financing provision for micro, small and medium enterprises (MSMEs). The BPRS mainly operates in rural areas so that they can provide services across a wide area.

The BPRS in carrying out its business does not use the usury system, because in Islam, usury is prohibited since it is "premiums or additions" that must be paid by the borrower to the party bought along with the principal amount in maturity or until the end of the loan period

(Rivai, 2010: 232). This prohibition reflects the words of Allah SWT in the Qur'anic verse Ali-Imran verse 130:

"O you who have believed, do not consume usury, doubled and multiplied, but fear Allah that you may be successful."

The above verse is normative principle for the BPRS in carrying out its duties to adhere to Islamic teachings and to not carry out any usurious activities.

The main activity of the BPRS is to channel financing to MSMEs to support economic activities for various sectors. The economic sector plays an important role in increasing and encouraging community-owned enterprises. Financing based on the economic sector can be classified into ten sectors, namely: agriculture, forestry and agricultural facilities; mining sector; industrial sector; electricity, water and gas sector; construction sector; trade, restaurant and hotel sector; transportation, warehousing and communication sector; business services sector; social / community sector; and other sectors. But the data used in this study is only relevant to financing the economic sector of agriculture, forestry, and agricultural facilities; trade, restaurant and hotel sector; and business services sector. These sectors are taken because the BPRS channelled more funding to the mentioned sectors (Rivai and Arviyan, 2010: 725).

Financing in each economic sector has increased. Financing in the business services sector in 2013 increased by 46.97% from 2012, which amounted to Rp 388,850 million. Even though in 2017 it was decreased by 4.39%, in August 2018 the financing of the business services sector increased by 33.95%. The financing of the agricultural, forestry and agricultural facilities sector also increased by 23.69% in 2018. Likewise, the financing to trade, restaurants and hotels, which were recorded at 18.13% in 2013.

As a financial intermediary, financing by the BPRS must be selective and based on the principle of prudence. This is intended to minimise the occurrence of risk, for example the risk of financing problems. Problematic financing occurs if the BPRS cannot recover the principal instalments and/or interest from the financing provided (Muhammad, 2002: 310). Problematic financing in an Islamic bank can be measured by the Non-Performing Financing (NPF) ratio. NPF is a comparison ratio between the amount of problematic financing and the total financing channelled by the bank. If the NPF gets higher, the BPRS is considered as less healthy.

NPF can affect the amount of financing channeled by banks. NPF or problematic financing can result in a loss of opportunity to obtain income from the financing provided, so as to reduce profitability and affect bank profitability (Dendawijaya, 2005: 82). Seeing this, the trust of customers who will put their funds in Islamic banks will decline, so that the funds channeled to finance will also decrease. Then it can be concluded that if the NPF level increases it will reduce financing in Islamic banking.

Non performing financing of each economic sector financing continues to increase every year. The NPF of the BPRS, especially in the financing of the economic sector, increases every year in line with increasing financing in the economic sector. It can be concluded that the increase in financing has a positive effect on NPF. The higher the financing disbursed, the higher the risk of NPF occurring in the banks.

Some previous studies provide evidence of a relationship between outstanding financing and NPF in Islamic banking. A study conducted by Taufiqurrochman (2008), showed that the financing of the economic sector of agriculture, forestry, and agricultural facilities; trade, restaurants and hotels; and business services partially has no effect on NPF. Another study conducted by Basori (2009), shows that financing the economic sector of agriculture, forestry, and agricultural facilities; financing of the economic sector of trade, restaurants and hotels; and financing of the business sector services economic sector partially affects NPF. Another study conducted by Mufidah (2016) resulted in the conclusion that partially financing the economic sectors of agriculture, forestry and agricultural facilities had an effect on NPF. While financing the economic sector of trade, restaurants and hotels; and financing of the business sector services economy does not affect NPF. However, simultaneously all independent variables affect NPF.

The results of the above research have different research results, thus creating room or research gaps to provide stronger evidence of a relationship between financing and NPF. Therefore, it is necessary to conduct research on the effect of economic sector financing on the NPF in the BPRS industry in Indonesia from January 2012 to August 2018.

The purpose of this study is to find out whether the financing variables in the economic sector of agriculture, forestry and agricultural facilities; trade, restaurants and hotels; and business services both partially and simultaneously affect the NPF on the BPRS in Indonesia.

Literature Review

Islamic Banking

According to Law No.10 of 1998 concerning amendments to Law No.7 1992, banking is a business entity whose main task is providing financial intermediaries, which channel funds from over-funded parties (idle funds / surplus units) to those in need of funds or lack of funds (deficit unit) at the specified time (Dendawijaya, 2005: 25). Islamic banks are financial institutions whose main business is providing financing and other services in payment traffic and money circulation; the operation is adapted to the Islamic sharia principles of Muhammad (2005: 13).

From the definition above it can be concluded that the meaning of the Islamic bank is as a business entity that serves as a financial intermediary institution and channels funds from parties with an excess of funds to those who lack funds through financing or services in accordance with Islamic *sharia* principles (Sukmana & Kassim, 2010). Islamic banks are currently struggling to meet the expectations of their customers through the creation of quality services that satisfy their customers as well (Asnawi, Sukoco, & Fanani, 2019).

BPRS

The BPRS is an Islamic banking institution that operates using sharia principles. According to Law No. 10 of 1998 on amendments to Law No.7 of 1992 on banking, the BPRS is a type of bank that carries out its business activities based on *sharia* principles and cannot provide payment system services. The BPRS only accepts deposits in the form of time deposits, savings and/or other similar forms, provides loans, provides funding and placement of funds based on *sharia* principles in accordance with the provisions stipulated by Bank Indonesia, and places its funds in the form of Bank Indonesia Certificates (SBI), time deposits, deposit certificates, and / or savings deposits with other banks. In essence, the BPRS is similar to a commercial bank with Islamic principles, but mainly located in sub-district areas and offering mainly microcredit for rural segments of the society (Nashihin and Harahap, 2014).

Non-Performing Financing (NPF)

Non Performing Financing (NPF) is financing that, in its implementation, has not fulfilled the desired target of the bank, such as the principal return or problematic profit sharing, financing which has the possibility of risk arising in the future for the bank, financing which includes special attention groups, doubtful, and traffic jams and current classes that have the potential to occur in arrears in returns (Veithzal, 2007: 477).
NPF is a type of credit risk and is defined as overdue payment of interest and principal of the financing by 90 days or more. High NPF share on overall financing causes lower profit margins and even crisis (Misman, et. al., 2015). One reason behind high NPF is the bank's inability to conduct prudential credit valuation and debt collection that leads to repayment failure (Bougatef, 2015).

Economic Sectors

According to Kholistyah (2010), financing based on the economic sector is divided into ten sectors. *First,* financing to agriculture, forestry and agricultural facilities, i.e. financing provided for businesses producing agricultural products, animal husbandry, fisheries, forestry for timber cutting and agricultural facilities. *Second,* financing to mining sectors and, i.e. financing provided for efforts to extract and collect natural mining materials in the form of solid, liquid, gas and the funding sector increases their focus on the mining sector (Isnalita & Narsa, 2017). *Third,* industrial sector financing, i.e. the financing provided for businesses in the industrial sector, includes changes in form (transformation), mechanical and chemical processing.

Fourth, electricity, gas and water sector financing, i.e. this type of financing includes the procurement of electricity, gas and water for both households and industries. *Fifth,* construction sector financing, i.e. financing for the construction and repair of markets, roads, railways, ports, airfields.

Sixth, financing the trade, restaurant and hotel sector. Trade is an economic / business activity in the field of large and retail trade of various types of goods, and is rewarded for services from the sale of goods (Ministry of Finance, 2012: 4). The hotel sector includes lodging, dining and drinking services as well as other public services, commercially managed and fulfill the requirements stipulated in government decisions (Ministry of Finance, 2012: 6). Whereas the restaurant includes the activities of serving and selling food / drinks to the public at the place where the business is right in part or the whole building permanently equipped with the manufacturing process (kemenkkeu, 2012: 7). This financing is usually used for export, import, retail trade, restaurant and hotel activities.

Seventh, financing the transportation, warehousing and communication sector, i.e. financing for public transportation activities both on land, water and air; travel agency, providing storage/rental facilities; communication: includes post, telephone, telegram, telecommunications. *Eighth*, business services sector financing, i.e. business services consisting of service industries in the fields of fashion, art, culture, etc. for example: workshop, salon, convection, gymnasium, etc. This financing is usually used for leasing activities or leasing to buy capital goods such as photocopiers, and for professions other than doctors, namely the services of lawyers and engineers. Ninth, social / community service sector financing, i.e. financing for entertainment, health, and cultural activities such as services of doctors, hospitals and polyclinics. *Tenth,* other financing, i.e. is a sector that is not included in the economic sector above. For example, consumption financing (Rivai and Arviyan, 2010: 725).

Research Method

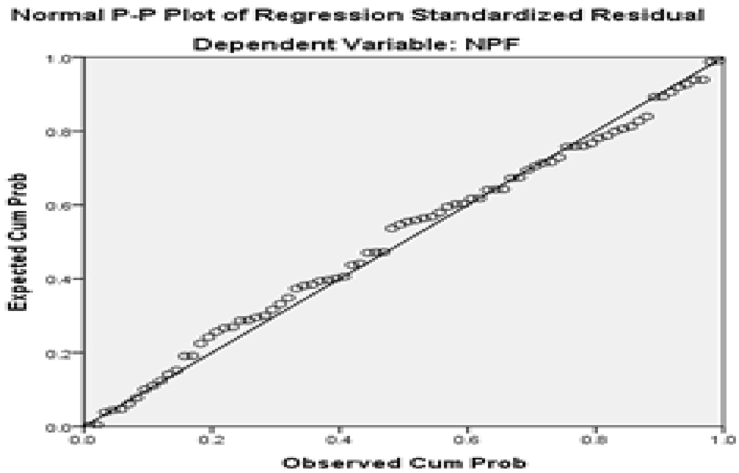
This study uses a quantitative approach, since it focuses on testing hypotheses, the data used must be measurable and will produce conclusions that can be generalised (Anshori, 2009:

155). This research will examine the influence of financing to agriculture, forestry, and agricultural facilities (*Pertanian, Kehutanan dan Sarana Pertanian*/PKS) sectors; financing to trade, restaurants and hotel (*Perdagangan, Restoran dan Hotel*/PRH) sectors; and financing to the business services (*Jasa Dunia Usaha*/JDU) sector, towards the Non-Performing Financing (NPF) of the BPRS industry in Indonesia. The variables, i.e., sectoral financing and NPF are expressed as percentage share to total BPRS. The data used in this study is gathered from Islamic Banking Statistics listed on the OJK website from January 2012 to August 2018.

Results and Discussion

Before estimating the model, some diagnostic tests are conducted to ensure the robustness of the estimated model.

Figure 3: Normality Test



Based on the diagram, we can know that the data has been normally distributed, because the data is spread around the diagonal line following the direction of the line or the pattern of the histogram. This shows that the pattern is normally distributed; the regression model fulfils the assumption of normality.

Table 1: Multicollinearity Test

Coefficients[a]								
Model		Unstandardised Coefficients		Standardised Coefficients	t	Sig.	Collinearity Statistics	
		B	Std. Error	Beta			Tolerance	VIF
1	(Constant)	17.586	.660		26.629	.000		
	PKS	-.514	.069	-.562	-7.490	.000	.294	3.397
	PRH	-.149	.027	-.406	-5.453	.000	.299	3.343
	JDU	-.083	.042	-.083	-1.965	.053	.932	1.073

a. Dependent Variable: NPF

Based on Table 1 above, all independent variables do not have any indication of multicollinearity, because it meets the requirements of VIF value to be less than 10 and tolerance value to be more than 0.1.

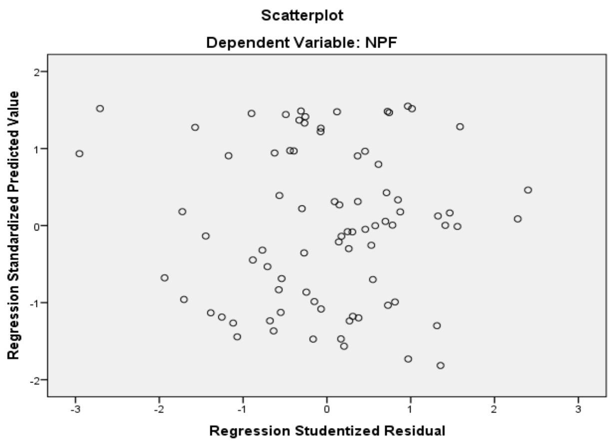
Table 2: Autocorrelation Test

Model Summary[b]					
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Durbin-Watson
1	.935[a]	.874	.869	.58186	1.252

a. Predictors: (Constant), JDU, PRH, PKS
b. Dependent Variable: NPF

Table 2 above shows that the Durbin Watson test value is 1.252, where the result is located in the region between -2 to +2 so that the data in this study show no indication of autocorrelation.

Figure 4: Heteroscedasticity Test



By looking at the scatterplot graph above, the points have formed randomly, above and below the point of origin (0) on the Y axis. Then it can be concluded that this regression model does not experience symptoms of heteroscedasticity.

Table 3: Output of the Regression Model

Variable	**Coefficient (β)**	**Sig.**
Constant	17,586	0.000
PKS	-0,514	0.000
PRH	-0,149	0.000
JDU	-0,083	0.053

Above, the estimated result shows that higher financing for each sector will significantly reduce NPF, with a stronger effect found on the agriculture related sector (PKS). This finding is parallel with several previous studies. The research by Mufidah (2016) explained that the financing of the agriculture, forestry and agricultural facilities has a significant effect on NPF. Funding in this sector has risks that cannot be controlled because the agriculture, forestry and agricultural facilities are highly dependent on nature, with the uncertainty of the quantity and quality produced, and disasters that can come at any time such as landslides, floods, droughts and other disasters. The existence of this risk has the potential to lead to problematic financing.

Basori (2009) conducted research, which found that the financing of the economic sectors of trade, restaurants and hotels had a significant effect on NPF. This is because Islamic banks prefer to channel their financing to this sector because the profits obtained are greater in the short term, so banks continue to entrust their funds to this sector. Whereas the research conducted by Suryadi (2014), found that this happened because the higher problematic financing from the PHR sector (trade, hotel and restaurant), would cause the *sharia* compliant funds to be unable to circulate from one customer to another, due to congestion of the financing. High problematic financing causes banks to form larger reserves of elimination. This can reduce the interest of Islamic banks to channel financing to the PHR sector and divert it to other sectors with lower NPF rates.

Meanwhile, a study from Taufiqurrachman (2008) stated that although services are not a basic need for the community, aspects of services tend to be needed by the community for various things so that the level of demand is also relatively stable. The problematic financing growth (NPF) has continued to decline, basically because the amount of financing channeled to banks is getting bigger and also banking management is more selective and careful, both in determining the size of the financing scheme portion and in analysing financing, always trying to implement policies that are in accordance with Islamic sharia principles in all their operational activities so that a good and certainly mutually beneficial relationship can be created in the cooperation between the bank and the customer.

Conclusion

This study found that financing to each economic sector significantly affects NPF in the BPRS in a negative direction, which means higher financing outstanding will lead to lower rate of NPF. This implies that more financing being disbursed is one of the keys to lower NPF in the Islamic banks. In other words, better quality financing can be achieved through higher financing outstanding.

This finding leads to some recommendations. *First,* the management of the BPRS should be able to maintain the precautionary principle that has been implemented and improve quality in analysing the financing to be channeled so that it can continue to minimise NPF in Islamic banking. *Second*, future research may add independent variables, for example, using overall financing in the economic sector, extension of research period and research subjects or using other dependent variables such as profitability to get better research results.

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