# Comparing Islamic Banks with Conventional Banks During a Monetary Crisis in Indonesia

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## Abstract

The Monetary Crisis is one of the problems that really overshadows every country. Because, this case can occur in any country, even including Indonesia. Indonesia itself has experienced several periods of monetary crises. During these periods, there were also several levels of problems faced by the country. So this also affects banks in Indonesia. These banks have different resilience when experiencing this crisis. The banks referred to in this study are conventional banks and Islamic banks. In this study specifically to compare the resilience of the two banks during the Monetary Crisis in Indonesia. This study uses a qualitative study literature method. We found that the resilience of conventional banks is known as fairly strong resilience. However, this was broken when there was an Islamic bank. Conventional banks by implementing the Time Value of Money became the weak points of conventional banks during this monetary crisis. In addition, conventional banks' ROA, ROE, NPF, and BOPO levels are higher than Islamic banks. The average ratio of profit to assets and capital of Islamic banks is lower than that of conventional banks. When compared to Islamic banks, of course this bank has good resilience during a monetary crisis. This is because Islamic banks implement a profit-sharing system. Of course there is no interest rate at this bank because in Islam, interest or usury is forbidden in Islamic teachings. In addition, Islamic banking can be minimized or even avoided. For negative spillover effects, where banks still have to pay very high interest rates (financing costs) to borrowers, while customer rates cannot be adjusted or say deposits are higher than loans, resulting in losses for banks. and creditors can increase the default rate

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## Background

Monetary crises have occurred in several countries, during the period 1970 to 2007, at least 429 crisis cases occurred which were divided into 124 banking crises, 208 exchange rate cases, 63 foreign debt crises, 26 twin crises, and 8 triple crises. crisis. Thus, this monetary crisis has become a case that has attracted the attention of the global community in particular (Maliha & Marlina, 2019).

The monetary crisis in Indonesia occurred in 1997-1998. This monetary crisis was caused by the high private foreign debt, the result of this monetary crisis caused the closure of 16 banks in Indonesia (Prabowo, Sulisnaningrum, & Harnani, 2021). It's the same with inflation which soared to 77.6%, and economic growth which slumped to -13.2%. And it was also caused by the depreciation of the rupiah exchange rate which reached Rp. 10,000/US dollar causing a banking crisis due to the bankruptcy of several private banks which failed to repay their loans in foreign currency (Atikah, Syafi'i, Rohimi, & Rani, 2023). Apart from Indonesia, the financial crisis in 1997 also occurred in other Asian countries such as Thailand, Malaysia, Singapore, the Philippines and South Korea. Besides that, this makes the economy in Indonesia weak (Ghazouani, Boukhatem, & Sam, 2020).

What became a factor in the occurrence of the monetary crisis was the decline in the exchange rate of the rupiah against the US dollar. This happened during the period 2007-2008. What started in America started with the collapse of the stock market. So that multinational financial companies become bankrupt. So that in the United States there are many layoffs of workers. As a result of the financial crisis in the United States, many investors withdrew their funds from their shares. Thus, this also affects the exchange rate of the Asian rupiah against the dollar so that it reaches a value of Rp. 12,650 per dollar on November 24, 2008 (Kumar & Robiyanto, 2021).

Conventional Banks are said to have resilience in this crisis. Convention banks by applying interest rates are expected to be able to have resilience during this crisis. Because of course banks are also needed during this crisis (Korzeb & Niedziółka, 2020). In addition, conventional banks also receive direct protection from the OJK (Financial Services Authority). However, if you look at Islamic Banks, of course, this bank has stronger resilience. Because Islamic banking implements a Profit Sharing system. Where this system explains the profit sharing between the bank and the customer. And based on interest rates as applied in conventional banking (Hasan, 2020).

The monetary crisis in Indonesia was preceded by a euphoria, there was high growth in a long period of time which was described as an economic miracle by the world bank, developments appeared that showed signs of bubbles such as the oversized expansion of real estates and the growth of the money stock market at the same time. with excessive inflow of short-term foreign funds. Externally caused crises, namely rapid changes in money market sentiment that cause financial panic, financial panic with contagion that causes a crisis in Indonesia (James, 2022).

Islamic banking and conventional banking have the same goal because they have similarities in their function as intermediaries between two parties who need services. The first is a party that needs funds, while the second is a party that has excess funds. Islamic banking also plays a role as a profit-seeking business entity. The profits obtained can be reused by Islamic banking for business development and others. So the benefit that occurs is mutual benefit, namely Islamic banking and also the wider community or the people. Basically profit in banking is the range between total income and total costs in a certain period (Rahmayati, 2021).

Islamic economics only views money as a medium of exchange, not as capital, or merchandise (commodities), so money cannot be traded and speculated freely. Money itself is not capable of providing use value. But the function of the money that is able to provide usefulness. In the economic concept known as the time value of money which states that the value of money now has more value than in the future. therefore, money must increase and grow because of the increase in time so that it does not erode in value to correlate between time and the value of money. This is inseparable from the implementation of the system of interest (interest) or usury. In the Islamic concept, the problem of usury is related to the problem of money (Mujahidin, 2022).

Islam confirms in the Qur'an that it is forbidden to use money-interest which is the same as usury. Islamic economics does not recognize the time value of money or the time value of money, but the theory of the economic value of time is considered correct from an Islamic economic perspective. This means that money itself has no time value. However, it is time that has economic value. An economic system that conforms to Islamic principles is the economic value of time. Borrowing money through conventional banks uses a time value of money system. This can be explained that the time value of money will not be accepted by Islamic banks. This concept uses interest which is strictly prohibited by Islamic economic principles (Samad & Sugeng, 2022).

Factors that determine the occurrence of a banking crisis include macroeconomic factors (growth, changes in TOT (Term of Trade), depreciation, real interest rates, inflation rate, budget surplus to GDP), financial, (ratio of M2 to foreign exchange reserves, ratio of bank cash dab reserves against bank assets, credit growth) and institutional (Ghardallou, 2021). The conventional monetary system contributes greatly to the occurrence of crises while the Islamic monetary system only contributes less to crises (Rabbani, Ali, Rahiman, Atif, Zulfikar, & Naseem, 2021). This shows that by using the Islamic monetary system, it will be able to minimize the probability of a financial crisis in Indonesia (Nugroho, Kurnia, Qoyum, & Fardila, 2020).

## Research Methods

This study uses a qualitative descriptive approach with data collection by means of library research. Library research is data or material needed to conduct research that comes from the library in the form of books, encyclopedias, dictionaries, journals, documents, and others. The collected data will be reduced and presented and conclusions drawn. The analysis was carried out by looking at previous findings about the impact of the monetary crisis on conventional banks, Islamic banks, time of money and value of time in Indonesia.

## Results and Discussion

The results of banking operations in 2011 developed positively. Global financial conditions, which did not improve after the European debt crisis and the US economic slowdown, did not have a significant impact on Indonesian banks. The outlook for the Indonesian economy in 2012 is expected to remain good, despite the high risk of a weakening global economy (Olivia, Gibson, & Nasrudin, 2020). The Indonesian economy is expected to experience inflation growth of 6.6% to 7.4%, slowing down to 4.0% +/- 1% growth in 2016. Current banking conditions encourage stakeholders to evaluate the health of banks. One of the parties who need to know the bank's return is the investor, because the better the bank's results, the greater the guaranteed security of the funds invested (Angelina & Nugraha, 2020).

**Table 1.** Development of Financial Ratios of 10 Commercial Banks in Indonesia with the Largest Assets for the 2007-2011 Period

| Ratio | BI standard | 2007 | 2008 | 2009 | 2010 | 2011 | Average |
|---|---|---|---|---|---|---|---|
| ROA | 1,50% | 2,45% | 2,02% | 2,00% | 2,69% | 2,67% | 2,37% |
| CAR | 8% | 18,72% | 15,63% | 16,28% | 14,82% | 15,12% | 16,11% |
| NIM | 6% | 6,71% | 6,69% | 6,56% | 6,41% | 6,03% | 6,48% |
| BOPO | 85% | 71,56% | 73,16% | 73,30% | 71,92% | 70,88% | 72,16% |
| NPL | 5% | 3,96% | 3,20% | 3,23% | 2,94% | 2,43% | 3,15% |
| LDR | 110% | 75,54% | 78,49% | 78,87% | 80,33% | 85,97% | 79,84% |

In looking at the table above, the development of the ROA, BOPO, NPL, NIM, and LDR ratios fluctuated during the 2007-2011 period. In this study, the Profitability ratio used is Return on Assets where the level of profit earned on assets owned by the bank can be measured by the level of return on Assets (ROA). A bank is said to be liquid if the bank concerned can fulfill its debt obligations, can repay all of its depositors, and can fulfill the credit requests it submits without delay.

The financial crisis that occurred in the United States (US) turned out to have affected the face of global finance (Echarte Fernández, Náñez Alonso, Jorge-Vázquez, & Reier Forradellas, 2021). The direct impact of this financial crisis for Indonesia was the loss of several Indonesian companies investing in US financial institutions. Non-bank financial companies that allocate funds to alternative sources of income, through buying stocks or bonds in foreign financial instruments, while the indirect impact of the crisis is reduced liquidity, soaring interest rates, falling commodity prices, weakening the rupiah exchange rate and weakening growth in funding sources . Likewise, the decline in the level of consumer, investor and market confidence in various financial institutions resulted in a weakening of the capital market (Ascarya, 2022).

The impact of the crisis on the Indonesian economy was marked by the withdrawal of funds in foreign currencies, especially US dollars, by creditor financial institutions and investors in the US. The withdrawal is made by selling stock securities and debt securities which were previously purchased in rupiah and then purchased in dollars, also withdrawal of funds is carried out by disbursing funds that have been placed with banks in Indonesia and directly in dollars. Then after that the financial crisis caused large amounts of funds to be repatriated, causing the sale of shares and debt securities in large quantities. This situation causes the price of stock securities and debt securities to fall so that the stock price index drops sharply (Fitrah, Alhamdi, Majid, Marliyah, & Handayani, 2022).

The financial crisis caused Bank Indonesia to increase the BI rate to reduce inflation caused by the decline in the value of the rupiah against the dollar. The increase in the BI rate was responded by a massive increase in conventional bank interest rates. An increase in interest rates causes the attractiveness of saving funds in conventional banks to increase, but this increase in interest rates will not be attractive to investors who will receive higher interest expenses. In the 1990s, more precisely in 1998, the economy experienced a crisis in Indonesia causing the collapse of the economy and banking, especially conventional banks, were not spared, only one Islamic bank survived from that period, namely Bank Muamalat Indonesia. Several banks affected by the 1998 crisis were motivated to apply sharia principles (Yusuf, Ichsan, & Suparmin, 2021).

Islamic banking is a banking solution based on Islamic sharia principles, especially in relation to transaction processing. They are kept away from practices that are feared to involve usury and are endowed with profit-sharing investment activities and business finance always follow the rules and stay away from the prohibitions listed in the Quran and Hadith (Roslan, Bamahriz, Muneeza, Chu, Mustapha, & Ahmad, 2020). Meanwhile, the Sharia Banking Act No. 21 of 2008, Article 1 Paragraph 12, Sharia Principles are the principles of Islamic law in banking based on fatwas issued by institutions authorized to issue fatwas in the field of Sharia to issue them. In this monetary crisis, sharia banking also provided a lot of business capital for the development of the people's economy (Winarsi, Hajati, Kholiq, & Thalib, 2021).

Islamic banking can be minimized or even avoided. For the negative spillover effect, where banks still have to pay very high interest rates (financing costs) to borrowers, while the customer rate cannot be adjusted or says deposits are higher than loans, resulting in losses for banks and creditors, it can increase the default rate. Because Islamic banking uses a profit-sharing system: company profits and losses are paid by the bank and the debtor jointly or the bank and the debtor in a reasonable relationship with a mutually agreed contact. Banks are also not subject to interest payments on debtors' money, so that banks are not trapped in the economy due to the crisis caused by weak public purchasing power and neglect of creditors (Bahlous-Boldi, 2021).

## Conclusion

Conventional bank resistance is known as a fairly strong resistance. However, this was broken when there was an Islamic bank. Conventional banks by implementing the Time Value of Money became the weak points of conventional banks during this monetary crisis. In addition, conventional banks' ROA, ROE, NPF, and BOPO levels are higher than Islamic banks. The average ratio of profit to assets and capital of Islamic banks is lower than that of conventional banks. When compared to Islamic banks, of course this bank has good resilience during a monetary crisis. This is because Islamic banks implement a profit-sharing system. Of course there is no interest rate at this bank because in Islam, interest or usury is forbidden in Islamic teachings. In addition, Islamic banking can be minimized or even avoided. For negative spillover effects, where banks still have to pay very high interest rates (financing costs) to borrowers, while customer rates cannot be adjusted or say deposits are higher than loans, resulting in losses for banks. and creditors can increase the default rate.

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