

DETERMINANTS OF SHARIA BANKING PERFORMANCE IN INDONESIA: A FINANCIAL PERSPECTIVE

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Abstract

This study investigates the determinants of the financial performance (FP) of Sharia banks in Indonesia. FP is defined using Return on Assets (RoA). This study utilizes secondary data sourced from the financial statements of Sharia Banks registered on the Indonesia Stock Exchange (IDX) 2019 to 2022. The measurement of each variable is adopted from prior research studies. The collected data is analyzed using multiple regression techniques. The data analysis yielded compelling evidence that Capital Adequacy Ratio (CARo) and Net Income (NI) exert a significantly positive influence on the profitability performance of Sharia banks in Indonesia. Conversely, Operational Expense Ratio (OERo) is found to have a significant negative impact on profitability. Interestingly, Non-Performing Financing (NPFi) and Debt-to-Asset Ratio (DARo) do not exhibit statistically significant effects on profitability, suggesting that these factors do not play a decisive role in determining the profitability of Sharia banks in Indonesia. Credit extension serves as a cornerstone of the banking sector, driving revenue generation and economic growth. While the study's findings indicate that NPFi does not exert a direct and consistent impact on profitability, it is imperative for Sharia banks to continuously strive for credit quality improvement.

Keywords: Performance, Profitability, Sharia Banks, Indonesia

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1. Introduction

The financial system of a nation is significantly influenced by the banking sector, contributing to economic stability and growth. Trust is the cornerstone of banking operations, enabling the mobilization and allocation of funds. The Financial Services Authority (OJK) is the regulatory entity in Indonesia, mandated to govern, inspect, and supervise all activities within the financial services sector independently and free from external influence.

One of the OJK's core functions is the intensive supervision of credit and financing activities. This encompasses a comprehensive oversight of all aspects of lending and financing, including the conduct of all bank officials involved. Such rigorous supervision is essential as credit extension is inextricably linked to interest rate management. A bank's performance is indicated by the ratio of net interest income to average productive assets. Additionally, the bank's capacity to repay its obligations to depositors who have entrusted their funds is paramount (Soetijati & Mais, 2019). During the pandemic, banks shifted assets to safer investments, and indicated that all banks had low levels of liquidity, but Islamic banks had higher levels of liquidity. The research results also state that the Indonesian government was able to preserve the economy during the covid-19 by employing economic stimulus (Viverita et al., 2023).

The Indonesian banking landscape encompasses two distinct operational categories: Islamic and conventional banks. Islamic banks, also known as Sharia banks, operate in accordance with Islamic principles, or Sharia law, as outlined in the fatwas (religious rulings) published by the Indonesian Ulema Council (Majelis Ulama Indonesia). These principles prohibit practices deemed unethical or harmful, such as gharar (excessive uncertainty), maysir (gambling), riba (usury), and zulm (injustice), while emphasizing fairness, balance, public welfare, and universalism (Maimun & Tzahira, 2022). Consequently, Islamic banks adhere strictly to Islamic law in all aspects of their business operations, particularly when conducting transactions aligned with Islamic principles.

The pricing mechanisms employed by Islamic banks differ significantly from those adopted by conventional banks. Islamic banks determine product pricing based on contracts established between customers and the bank. This pricing approach is tailored to the specific type of deposit and the deposit term. These agreements stipulate the customer's entitlement to a share of the profits generated. Islamic banks are prohibited from utilizing interest-based pricing schemes as they consider bank interest to be riba (usury) (Mawaddah, 2015). The business model of Islamic banks is different from the others. Islamic banks implement a sharia-based model that is predicted on equity or participatory contracts, whereas conventional one implement an interest-based model that is predicted on debt contracts (Boukhatem & Djauhi, 2020).

The impact of the Covid-19 is putting pressure on the economy throughout the world, as well as in Indonesia. This impact is not only on the financial sector, but also on the non-financial sector. Research conducted by Zulyanto (2023), obtained evidence that the banking sector, especially sharia banking, does not have effect on financial performance

(FP). The results of his research found that the FP of Sharia Banking was better during the pandemic, where the Capital Adequacy Ratio (CARo) indicator increased and Non-Performing Financing (NPFi) decreased significantly. Likewise, the efficiency level (OERo) and liquidity level (FDR) are improving. This research did not find significant differences in FP, thus showing that the system embedded in Islamic banking was proven to be able to respond better to the crisis. The effect of the Covid-19 on the banking intermediation function based on the results of a study on Sharia Banking, namely Financing, shows that there was a fluctuation from January to March 2020 which tended to experience an increase (Jayanti, 2021). The pandemic is not an obstacle for Sharia Financial Institutions, in this case Sharia banks, to continue to improve services, but the pandemic can be a stepping stone for Sharia banks to continue to improve services (Kumaidi & Padli, 2021).

The sharia banking sector in Indonesia has witnessed remarkable expansion, necessitating a corresponding enhancement in professionalism, management, and adherence to Sharia principles. To effectively support this growth trajectory, rigorous supervision by banking authorities is paramount. Profitability serves as a critical indicator of a bank's FP, reflecting its ability to conduct business efficiently. This efficiency is determined by comparing the generated earning to the managed capital or assets. A higher profitability level signifies superior performance (Suryani, 2011). Various factors influence profitability, including CARo, OERo, NPFi, NIn, and DARo.

2. Literature Review

2.1. *Sharia Bank*

Serving as financial intermediaries, banks occupy a central role within the economic system. Their core function centers on managing and moving money, facilitating a diverse range of financial activities. These activities encompass fund transfers, deposit and payment processes on savings accounts, discounting negotiable instruments like bills of exchange and promissory notes, trading securities, buying and selling checks, bills of exchange, and trade instruments, and providing bank guarantees. (Wilarjo, 2014).

Islamic banks, also known as Sharia banks, run in accordance with the fundamental of Islamic law. A key distinction between sharia and conventional banks lies in their pricing mechanisms. Sharia banks determine product pricing based on contracts established between the bank and depositors, considering the type of deposit and agreed-upon duration. These agreements stipulate the proportion of profits to be shared with depositors. Islamic banks adhere strictly to Quranic and hadith-based guidelines in their operations. A defining characteristic of Islamic banks is their avoidance of interest-based systems, as they consider bank interest to be *riba* (usury) (Mawaddah, 2015).

Sharia banks are institutions of finance that run in accordance with Sharia principles, primarily focusing on providing payment transaction services such as loans and money

circulation (Kusumastuti & Alam (2019). Aligned with Islamic law, the governing contracts of Islamic banks involve agreements between the bank and other parties for depositing funds, or engaging in other activities compliant with Sharia principles. According to Kusumastuti & Alam (2019), Islamic banks commonly employ various financing models, including *mudharabah*, *musyarakah*, and *murabahah*.

As outlined by Sudarsono (2003), the role and functions of sharia banks, in line with the standardized accounting guidelines published by Accounting and Auditing Organization for Islamic Financial Institutions, encompass:

1. Investment Management: Islamic banks can function as investment managers, utilizing their expertise to manage client investment funds.
2. Investment: Islamic banks also play an investor role, both by investing their own funds and those entrusted to them by clients.
3. Payment Facilities and Financial Services: Islamic banks serve as suppliers of payment facilities and financial services, engaging in a range of conventional banking activities.
4. Social Responsibility: Islamic banks bear the responsibility of undertaking social activities in accordance with the inherent principles of Sharia finance.

2.2. Financial Indicators

A bank's profitability reflects its ability to generate profit over a specified period. A bank is considered financially sound if its profitability consistently improves and exceeds established benchmarks (Suryani, 2011). Profitability stems from the policies implemented by management. Profitability ratios are employed to assess how effectively management's ability to steer the entity is contemplated in the level of profit. Various methods can be used to evaluate a company's profitability, depending on the ratio between earning and the assets or capital used as the calculation basis. Companies with consistently high profitability typically do not engage in earnings smoothing practices, as their managers have confidence in the entity's performance, which is judged based on the profit generated. However, if a company's profitability is low, performance of the owner-management will be questioned, and their reputation in the community will be doubted. Consequently, such companies may be more inclined to engage in earnings smoothing practices (Kusumastuti & Alam, 2019).

Return on Assets (RonA) is a ratio that gauges an entity's capacity to produce profit from the assets it employs. A company's performance is considered better if RONA is high and shows an upward trend over time. This will lead to an increase in stock prices and higher returns, hence RONA is considered to have an influence on stock returns (Almira & Wiagustini, 2020).

The Capital Adequacy Ratio (CARo) can be determined by dividing a company's total capital by its Risk-Weighted Assets (RWA). Bank Indonesia has set a minimum CARo stanDARod of 8%. If a company's CARo ratio falls below 8%, it is considered to indicate an inadequate capacity to absorb potential losses arising from banking activities, potentially impacting the company's financial performance (Saputra & Lina, 2020). Research has established a link between CARo and profitability. Studies by Alfianda & Widiyanto (2020), Awintasari & Nurhidayati (2021), Basnawati (2022), and Ramadhan (2023) provide evidence that CARo positively influences profitability levels. Similarly, Imamah & Munif (2018) and Bernardin (2016) found a positive relationship between CARo and profitability. However, studies by Syachreza & Gusliana (2020) and Maulla & Wirman (2022) did not find any significant relationship between CARo and profitability..

Operational Expenses on Operating Income Ratio (OERo) serves as an indicator to evaluate the efficiency and performance of entities in managing their operations. As per Bank Indonesia's Circular Letter, OERo is determined by comparing operating expenses to operating income (Wibisono & Wahyuni, 2017). A low OERo ratio indicates that a bank operates more efficiently in managing its operational costs. This suggests overall better bank performance. Therefore, the OERo ratio, which serves as a proxy for bank operational efficiency, has an impact on bank performance (Kusumastuti & Alam, 2019). This argument is encouraged by research findings from Syachreza & Gusliana (2020); Alfianda & Widiyanto (2020); Awintasari & Nurhidayati (2021); and Maulla & Wirman (2022), which demonstrate that a lower OERo ratio leads to a higher profitability ratio.

Non-Performing Financing (NPFi) serves as an indicator for assessing troubled financing and has a significant impact on the FP of sharia banks. NPFi is directly linked to the financing provided by sharia banks to the customers. When NPFi remains at a low level, revenue will increase, leading to higher profits. Conversely, if the NPFi level is high, revenue tends to decline, resulting in lower profits (Riyadi & Yulianto, 2014). While Maulla & Wirman (2022) did not uncover any evidence of correlation between NPFi and profitability in their study, research conducted by Syachreza & Gusliana (2020); Alfianda & Widiyanto (2020); and Awintasari & Nurhidayati (2021) demonstrates that NPFi has a negative impact on profitability.

Net Income (NIn) is used to assess the capability of a entities productive assets to generate profit by comparing operating income minus average returns and bonuses to productive assets (Awintasari & Nurhidayati, 2021). Net Interest is an indicator that measures the difference or gross margin between credit and investment assets held by a bank (Ramadhan, 2017).

Debt to Asset Ratio (DARo) is a ratio between total debt and total assets. This ratio shows the portion of debt used to finance the entities assets. DARo is also used to determine how much debt is used to fund a company's operations. The amount of borrowed capital used to invest in assets to generate profits for the company increases

as this ratio increases (Oktaviani et al., 2020). However, research by Rohmawati & Pratama (2020) found no evidence of a relationship between DARO and profitability.

2.3. Capital Adequacy Ratio (CARo) and Profitability

The Capital Adequacy Ratio (CARo) degree to which a bank's assets carry risk. This risk also stems from capitalization, which occurs when a bank obtains capital from sources outside the bank (Kusumastuti & Alam, 2019). The performance of Islamic banking is improving as the CARo ratio increases, indicating the strength of the bank's capitalization. The profitability of sharia banking companies in the market of capital is also affected by the increased attractiveness of the company to investors as a result (Fitriana, 2016). The CARo serves as a performance indicator for banks to assess the sufficiency of their capital to sustain risk-bearing or risk-generating assets. A higher CARo for Islamic banks indicates that the bank is able to manage its risky assets efficiently and effectively, leading to improved profitability. This argument is supported by research findings from Basnawati (2022); Ramadhan (2023); Alfianda & Widiyanto (2020); and Awintasari & Nurhidayati (2021), who demonstrate that CARo has a positive impact on RonA.

H1: CARo has a positive effect on RonA

2.4. Operational Expenses on Operating Income Ratio (OERo) and Profitability

Operational Expenses on Operating Income Ratio (OERo) measures a entities management's ability to manage operating expenses and income. Banks in the healthy category have the highest OERo ratios, ranging from 94 to 96 percent (Bank Indonesia, 2004). An excessively high OERo value can negatively impact the performance of Islamic banks, which can decrease profitability automatically (Sihotang et al., 2022). Banks with excessively high OERo ratios are considered inefficient in their operations. Research conducted by Ramadhan (2023); Magalhaes (2022); Syachreza & Gusliana (2020); Alfianda & Widiyanto (2020); Awintasari & Nurhidayati (2021); and Maulla & Wirman (2022) indicates that OERo has a negative effect on RonA.

H2: OERo has a negative effect on RonA

2.5. Non-Performing Financing (NPFi) and Profitability

NPFi serves as a tool to identify financing problems related to the potential for debtors to neglect to accomplish their obligations to repay the bank on time (Almunawwaroh, 2022). Users of financial statements are reminded that the bigger the NPFi, the bigger the bank's losses, which will then lower the bank's profits, and vice versa (Ishak & Pakaya, 2022). Research conducted by Ramadhan (2023), Basnawati (2022), and Almunawwarah (2022) found that NPFi has a negative impact on RonA.

H3: *NPFI has a negative effect on RonA*

2.6. Net Income (NIn) and Profitability

Net Income (NIn), is a ratio used to assess the capability of a companies productive assets to produce profit by comparing operating income minus average returns and bonuses to productive assets (Awintasari & Nurhidayati, 2021). The magnitude of NIn indicates that operating income less profit-sharing funds less operating expenses exceeds the average profitability of assets, causing profit-sharing income to rise above the average productivity of assets and the bank to become healthier (Yuniar et al., 2022). Research by Setyarini (2021) indicates that NIn has a positive effect on RonA.

H4: *NIn has a positive effect on RonA*

2.7. Debt-to-Assets Ratio (DARo) and Profitability

DARo is used to determine the extent to which debt is used to fund a company's operations. The amount of borrowed capital used to invest in assets to generate profits for the company increases as this ratio increases (Oktaviani et al., 2020). According to (Chandra, 2021), this ratio can be said to represent the proportion of funds obtained from both long and short-term loans. Due to the higher degree of security, creditors prefer a low total DARo. Research conducted by Luckieta (2021) indicates that DARo has a positive effect on RonA.

H5: *DARo has a positive effect on RonA*

3. Research Methodology

This research employs a quantitative methodology utilizing secondARoy data. The research subjects are Islamic banks registered on the Indonesia Stock Exchange (BEI) that have released annual financial statements from 2019 to 2022. The total sample size is four Islamic banks. Saturaterd sampling technique was employed to select a sample of the entire population. The reason for using the saturated sampling technique is because the research examines the performance of Islamic banks in Indonesia that are only listed on the IDX. The independent variables examined are CARo, OERo, NPFI, NIn, and DARo (Adetama et al., 2021; Adyani & Sampurno, 2018; Ridwan et al., 2021; Awintasari & Nurhidayati, 2021 ; Maulita & Tania, 2018). Profitability serves as the dependent variable, measured using RonA (Almira & Wiagustini, 2020). In order to investigate the functional relationship between variables, multiple regression analysis was implemented.

The measurements for all variable were adopted from several past studies. Table 1 presents the measurement.

Table 1. Variables Measurement

Variables	Measurement
Capital Adequacy Ratio (CARo)	Modal divided by ATMR x 100%
Operational Expenses on Operating Income Ratio (OERo)	Operational Expenses/ Operating Income x 100%
Non-Performing Financing (NPFi)	Non-Performing Financing divided by Total Credit x 100%
Net Returns (NIn)	Income Distribution of funds after profit sharing- Operational Expenses / Total Productive Assets X 100%
Debts to Assets Ratio (DARo)	Total Debt divided by Total Assets x 100%
Profitability Return on Assets (RonA)	Profit Before Tax/Total Aset x100%

4. Data Anlysis and Discussion

According to the Financial Services Authority (OJK) Indonesia, there were 14 sharia banks registered during the period of 2019-2022. However, 10 of these banks were not listed on the BEI, resulting in a total sample size of 4 banks with 16 observations.

Table 2. Descriptive Statistical Test

	Frequency	Min	Max	Average	Std. Dev
CARo	16	0.140	3.910	0.961	1.230
OERo	16	0.560	4.280	1.234	1.109
NPFi	16	0.000	0.030	0.008	0.010
Nin	16	0.010	0.310	0.102	0.106
DARo	16	0.020	0.300	0.139	0.090
RonA	16	-0.110	0.140	0.026	0.074

Testing Classical Assumptions

Table 3 presents that the results of the Kolmogorov-Smirnov test show a probability value of 0.137, which is >0.05 . This suggests that the data utilized in the research model is normally distributed.

Table 3. Normality Test

	Unstandardized Res.
Number of samples	16
Normality parameters	Average
	0.000
	Std. Dev
	0.016
The most extreme difference	Absolut
	0.187
	Positive
	0.184
	Negative
	-0.187
Test Statistics	0.187
Asymp. Sig. (2-tailed)	0.137

Table 4 presents multicollinearity information, indicate that VIF values of variables below ten and tolerance above 0.10. This suggests that the regression model does not exhibit signs of multicollinearity.

Table 4. Multicollinearity Test

Variables	Tolerance	VIF
CARo	0.304	3.285
OERo	0.453	2.205
NPFi	0.217	4.609
Nin	0.272	3.671
DARo	0.616	1.622

The heteroscedasticity test has various models, one of which is the Glejser test (Gujarati, 2006). Table 5 presents the Glejser results, indicating that the significance value of all variable is >0.05 . This implies that the regression model on this data does not exhibit signs of heteroscedasticity.

Table 5. Heteroscedasticity Test

Variables	Sign. (2-tailed)
CARO	0.812
OERO	0.765
NPFI	0.601
NI	0.922
DARO	0.952

Table 6 shows the autocorrelation test. The regression analysis generated a Durbin-Watson (DW) statistic of 2.088. Since the DW value falls within the range of 1.8433 to $(4 - Dw) = 3.8500$, it suggests a possibility of autocorrelation. Therefore, further steps are necessary to determine definitively whether autocorrelation exists in the regression model. The Runs Test can be employed for this purpose. The significance value of the Runs Test will be examined to determine if it is >0.05 . If the sig. value (sig) is >0.05 , the model does not exhibit autocorrelation. Conversely, a sig. value <0.05 indicates the presence of autocorrelation in the regression model.

Table 6. Autocorrelation

Conclusion	Range	DW Test
Autocorrelation Present	< 0.6150	
No Conclusion	$0.6150 - 2.1567$	
No Autocorrelation Present	$2.1567 - 1.8433$	
No Conclusion	$1.8433 - 3.8500$	2.088
Autocorrelation Present	> 3.8500	

The Runs Test results, presented in Table 7, indicate that the p-value is >0.05 . This suggests that autocorrelation is not present in the regression model.

Tabel 7. Runs Test

	Unstandard. Res.
Test Value ^a	0.00043
Cases < Test Value	8
Cases $\geq$ Test Value	8
Cases Quantity	16
Numb. of Runs	11
Z	0.776
Asyp. Sig. (two-tailed)	0.438

3.1 Multiple Regression Analysis

The results of the hypothesis testing are presented in Table 8. According to Table 8, it can be inferred that the significance values for the influence of CARo (X1), OERo (X2), NPFi (X3), Nin (X4), and DARo (X5) on RonA (Y) are no more than the established sig. level of 0.05. Additionally, the Sig.F value is 0.000. These results indicate that this model is appropriate and relevant for use in this study.

The analysis of the data reveals an Adjusted R-squared of 93.3%. This implies that 93.3% of the variation in the profitability can be explained by CARo, OERo, NPFi, Nin, and DARo. The remaining 6.7% is attributed to factors that not investigated by this research.

Table 8: Multiple Regression Analysis Results

Variables	Regression Coefficient (β)	T	Sig.	Decision
(Constant)	-0.004	-0.131	0.899	
CARo	0.029	3.911	0.003	Not significant
OERo	-0.249	-7.428	0.000	Significant
NPFi	1.321	1.220	0.251	Not significant
Nin	0.445	4.967	0.001	Significant
DARo	0.053	0.756	0.467	Not significant
R = 0.977		F statistic = 42.736		
R Square = 0.955		Sig. F = 0.000		
Adj R-Square = 0.933				

3.2 Discussion

CARo has a positive influence on RonA (sig. $0.003 < 0.05$; regression coefficient 0.029), supporting the first hypothesis that CARo positively impacts RonA. Bank profitability

increases in line with an improvement in CARo. A high CARo value significantly impacts profitability by enabling banks to optimize loan disbursement and reduce potential losses. With strong capital, bank management can allocate funds to profitable investment operations with greater flexibility. A bank's capital protection correlates positively with its RonA. Efficient capital also expands credit availability. In addition to enhancing RONA, high capital adequacy can also encourage customers to deposit their money in the bank and support credit growth.

The positive influence of CARo on RonA aligns with previous studies conducted by Alfianda & Widiyanto (2020); Awintasari & Nurhidayati (2021); Basnawati (2022); and Ramadhan (2023), who found evidence that CARo positively impacts profitability. Similarly, studies by Imamah & Munif (2018) and Bernardin (2016) support the positive relationship between CARo and profitability. However, the current study's findings contradict those of Syachreza & Gusliana (2020) and Maulla & Wirman (2022), who concluded that there is no association between CARo and profitability. The research results do not support research founded by Said & Ali (2016), CARo has no effect on RonA.

OERo has a negative influence on RonA (sig. $0.000 < 0.05$; regression coefficient -0.249), supporting the second hypothesis that OERO negatively impacts profitability. OERo has a detrimental effect on profitability. In other words, an increase in OERo can lead to a decline in RonA profitability in Islamic banking in the BEI. If a bank operates its business efficiently, the OERo ratio will decrease. Consequently, the bank's revenue will increase, ultimately contributing to improved profitability. The data analysis results support studies conducted by Ramadhan (2023); Magalhaes (2022); Syachreza & Gusliana (2020); Alfianda & Widiyanto (2020); Awintasari & Nurhidayati (2021); and Maulla & Wirman (2022), which found that OERo has a negative impact on RonA.

NPFi does not significantly impact RonA (Sig $0.251 > 0.05$), failing to support the third hypothesis that NPFi negatively influences profitability. NPFi does not have a statistically significant impact on RonA in sharia banks listed on the BEI. It is possible to conclude that by implementing effective risk management practices, banks can effectively identify and manage potential risks associated with NPFi. This would allow them to mitigate the negative impact of NPFi on profitability. Alternatively, banks may have other advantages that can offset the impact of NPFi on profitability (RonA). These findings align with research conducted by Wibisono & Wahyuni (2017), who found that NPFi does not influence RonA. However, they contradict the findings of studies by Ramadhan (2023), Basnawati (2022), and Almunawwarah (2022), which suggest that NPFi has a negative effect on RonA.

IN has a positive influence on RonA (Sig. $0.001 < 0.05$; regression coefficient 0.445), supporting the fourth hypothesis that NIn positively impacts RonA. Bank profitability increases in line with the enhancement in the NIn ratio. The likelihood of financial problems in a bank decreases in line with the increase in this ratio, as it indicates that

the bank will earn more income from the productive assets it manages. This study is in line with that study done by Setyarini (2021), who was able to prove that NIn has an effect on RonA, but does not support the study conducted by Awintasari, & Nurhidayati (2021), which stated that there is no influence between NIn and profitability.

DARo does not have a significant influence on RonA (Sig. 0.467 > 0.05), failing to support the fifth hypothesis that DARo positively impacts profitability. DARo does not affect profitability, as measured by RonA, in Islamic banks listed on BEI. These results indicate that Islamic banks have relatively low debt levels, resulting in a minimal impact on RonA. This is supported by effective debt management practices, enabling entities to manage their debt efficiently, minimizing any negative impact on RonA. However, this results contradicts the study done by (Luckieta et al., 2021), who suggest that companies with high profitability levels tend to have high debt levels as well. The results of this article align with study founded by Alfiani (2022) and Rohmawati & Pratama (2020), which found no significant relationship between DARo and RonA.

4. Conclusion and Implication

The research results shows that CARo and NIn had a positive impact, OERo had a negative effect, while NPFi and DARo had no effect on profitability. Research data shows that during the Covid-19 pandemic, many companies experienced difficulties in their business, so they needed capital to maintain the continuity of their business. The research results obtained evidence that Islamic banks are able to expand credit availability because they can be efficient in managing their capital. This is also supported by research results showing that Islamic banks are able to maintain their sustainability, because they are able to make operational costs more efficient, which shows that operational costs are getting smaller, so that profitability increases.

A core function of banking operations is lending, which carries the inherent risk of non-performing loans (NPLs). To mitigate the occurrence of NPLs, banks must exercise due diligence in assessing the creditworthiness of potential borrowers. The research results indicate that NPFi does not exert a significant impact on profitability, implying that neither favorable nor unfavorable NPFi ratios influence RonA. Nevertheless, maintaining healthy NPFi ratios remains crucial for banks, particularly Islamic banks, which were the focus of this study. Therefore, Islamic banks must continuously strive to enhance their credit quality.

Sharia banks must be able to improve their performance, because study results display evidence that NPFi has no impact on RonA, even though NPFi is used as an indicator for assessing problematic financing and has an effect on the profitability of sharia banks. Therefore, future researchers can re-examine the influence of NPFi on RonA by taking longer data, it is suspected that the data used is of a very short period.

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