International Journal of Engineering & Technology, 7 (3.30) (2018) 587-591

International Journal of Engineering & Technology

Website: www.sciencepubco.com/index.php/IJET

Research paper

Profit Growth in Indonesian Sharia Bank: the Impact of RGEC

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Abstract

The purpose of this study aims to examine the impact of RGEC implementation on the growth of Sharia Banking profit in Indonesia. This study uses data of financial statements of 11 Sharia banking Indonesia during the year 2012-2014. This research uses panel regression model in testing RGEC factor on profit growth. Based on the data indicates that Sharia banking is still at risk, but GCG, ROA and CAR are still in a maintained position. Statistically this study found that NPF, CAR, inflation and Sharia banking activities affect the profitability of these banks. This indicates that Sharia banking has experienced risk and profitability problems. Economic problems inevitably affect Indonesian banks as it is seen that the level of profitability and inflation are not much different from each other.

Keywords: *Impact, RGEC, Risk, Sharia Banks*

1. Introduction

The world of banking today faces problems that can disrupt its growth. Baselga-Pascual (1) state that the banking business is facing economic problems, thus making the high and low bank risk. Economic problems include interest rate, high inflation rate, low national income of a country and the global economic crisis. The condition of the economic crisis also had a negative impact on bank profitability, (2). It has also spread to Sharia banking in various countries, (3). In addition to economic problems, according to Karbhari (4) Sharia banking also faces the problem of customer diversity, regulation, and competition with conventional banks and less qualified human resources. Bilal & Amin (5) mentioned that Sharia banking is also experiencing problems of efficiency and lower profitability compared with conventional banking. So, Alandejani et al.(6) and Alandejani & Asutay (7) explicitly say that Sharia banking has a high risk of failure and survival times shorter than conventional banks.

On the financial side of Doumpos et al. (8) Sharia banks are financially weaker than conventional banks. According to Zins and Weill (2017), it is necessary to strengthen banking stability by implementing regulations that lead to level of banks' risk. Furthermore, Ibrahim & Rizvi (10) mention that the institutions or parties that take the policy (the government in this case the central bank) to focus on improving regulations relating to the health stability of banks. Regulations made by policy makers can improve better governance or management as mentioned by (11), Sharia banking governance is still weaker than it should be. Thus, to reinforce governance to make it stronger, (12) suggest the need for greater emphasis and enforcement of governance. Good policy-making will improve the efficiency of bank performance, so that Sharia banking gets better profitability and capital improvement.

In Indonesian's context, to evaluate dynamics of banking development including Sharia banking has done by making regulations, both regulatory agencies and regulatory regulations. The regulation of Indonesian government agencies has established a Financial Services Authority (OJK) institution authorized by Law Number 21 of 2012. On the regulatory side, the Indonesian government through Bank Indonesia as the Central Bank has published the Circular Letter Number 3/24 / DPNP of 2011 on health Banks that come into effect since 2012. Health assessment in accordance with Circular Letter Number 3/24 / DPNP in 2011 contains four factors, namely; Risk Profile, Good Corporate Governance, Earning and Capital (RGEC). This RGEC assessment is then reinforced by the establishment of the Financial Services Authority Regulation No. 8 / POJK.03 / 2014.

The presence of these regulations is expected to affect the stability and profitability of the bonds and resistance in facing the macroeconomic and internal dynamics of banks. (13) claimed macroeconomic dynamics as a factor affecting the profitability of banks in Switzerland. (14) concluded ROA affects Sharia banking in Malaysia. (12) said the imposition of good governance mechanisms will make Sharia banking more effective and improve its profitability. (15) find that in Pakistan management practices governance, operating efficiencies and risk mitigation ultimately improving banking performance. While, (1) said capitalization of capital, profitability, efficiency and liquidity of banks greatly affect bank risk. In Sharia banks larger capital makes the bank unstable profitability (16).

Research in Indonesia on RGEC has been done with various models and several previous studies in have been conducted on the bank's health to profit growth finding partially inconsistent results but simultaneously affect to profit growth. (17) tested RGEC against stock price changes. (18) examines of RGEC was against profitability. But research in Sharia Banks refers to (19) but he does not include Good Corporate Governance variables. FDR and NPF is the proxies of risk profile have a positive effect on Return on Assets (20) But (21), NPL, LDR and CAR have no effect on the profit growth of national private foreign exchange banks. (22) say the NPL is influential on ROA and CAR does not affect ROA. Penelitian lain (23) stattes NPF has a positif effect ob profit

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growth while NPF has a positive effect on profit growth while FDR negatively affects profit growth as well as CAR. While, RGEC risk proflile. Thus, the purpose of this study examined the effect of RGEC implementation on IDX Sharia banking profit growth.

2. RGEC Factors and Profit Growth

The first factor of RGEC is Risk. Bank Indonesia regulation number 5/8 / PBI / 2005 defines risk management as the procedure, methodology for identifying, measuring, controlling risks arising from bank operations. Bank Indonesia Regulation number 13/1 / PBI / 2011 article 7 paragraph 1 is said to be 8 sets of risks, namely: credit, market, operations, liquidity, law, strategic, compliance and reputation. Because of the object of Sharia banking research, this study used nonperforming loan or financing (NPF) and Financing to Deposits ratio (FDR) in measuring credit and substantial risk for Sharia banking. In measuring the health of banks with the RGEC model, Bank Indonesia has established standards such as Table 1 below:

Table 1: Standard of bank health predicates of RGEC

No	RGEC Variables Predicates					
1	NPF	0<NPF< 2	2≤ NPF <5	5≤N NPF <8	8<N NPF <11	NPF > 11
2	FDR	50<FDR ≤75	75<FDR ≤85	85< FDR≤10 0	100<FDR≤ 120	FDR>1 20
3	GCG	NK < 1.5	1.5 <NK<25	2.5<NK< 3.5	3.5<NK<4 5	NK>4. 5
4	ROA	2 < ROA	1.25< ROA≤ 2	0.5<RO A≤ 1.25	0< ROA≤ 0.5	ROA≤ 0
5	CAR	12<CAR	9<CAR≤ 12	8<CAR≤ 9	6<CAR≤8	CAR< 6
Rank.		VH	H	EN	LH	U

Source: Bank Indonesia

Based on Table 1 above, all RGEC variables have been assigned their respective values and predictions of that value. Predicate VH = very healthy, H = healthy, EN = healthy enough, LH = less healthy and U = unhealthy.

The second factor of RGEC is Good Corporate governance. The explanation of Good Corporate Governance has been mentioned in Bank Indonesia Regulation Number 8/4 / PBI / 2006 relating to the principles of guarantee, accountability, responsibility, independence and fairness. These five premises serve as the basis for the bank to conduct its own assessment which includes 11 assessments which have been mentioned in Bank Indonesia Circular Letter Number 15/15 DPNP. The third factor is earning. In RGEC, this profit factor is the main condition to be achieved banks. In measuring the rate of earning ROA is measured using Bank Indonesia regulation no.6 / 9 / PBI / 2004. The Fourth Factor of RGEC is Capital. Each banking must provide a minimum capital of 8% of risk-weighted assets (RWA). This assessment of capital is re-regulated in Bank Indonesia Regulation No.13 / 1 / PBI / 2011 stating that banks should link capital with bank risk, if the risk is greater than big capital should be provided to anticipate risks.

3.Methodology

The data used in this research is the (12) Sharia banking data registered in the Banking in Indonesia (IDX) period 2011-2014. All data is accessed through www.bi.go.id; and www.ojk.go.id. However, there were only eleven banks published their financial statement and good company management in the period of study. The eleven Sharia banks are Bank MUAMALAT Indonesia, Bank MANDIRI Sharia, Bank Mega Sharia Indonesia, Bank BRI Sharia, Bank Bukopin Sharia, PANIN Sharia Bank, BCA Islam Bank, Bank JABAR and BANTEN Sharia, Bank BNI Sharia and May Bank Indonesia, while BTPN Sharia is not included in the data research. Having obtained all financial statements, then calculation of financial performance is measured based on RGEC.

Risk profile is made using credit risk indicator that is the ratio of non-performing loan and Financing to Deposit ratio. These two risks are the most common and fundamental risks faced by banks. The GCG factor used value based on composite self-assessment by each bank. While the profitability factor is measured by return on asset. While capital factor using Capital Adequacy Ratio. Profit growth is also measured based on the financial statements of eleven Sharia banking that became the research sample. Furthermore, the results of data processing then grouped in accordance with the criteria of Bank Indonesia. In the NPF indicator, FDR, GCG, ROA and CAR symbols are; very health (VH) health (H): healthy enough (EN); less healthy (LH) and unhealthy (U). In each of the years into the research period. While profit growth is calculated by distributing the current year's profit and minus the previous year divided by the previous year's inter-year growth. The P symbol represents the position or rangking of each RGEC indicator for 3 years of research. Finally, after getting all the data according to the variables used then in by using regression panel. The last, made as general dummy bank variable of Sharia foreign exchange bank and non-foreign exchange bank as dummy variable. So, the research model used is:

$GE_{it} = \beta 0_{it} + \beta_1 NPF_{it} + \beta_2 FDR_{it} + \beta_3 GCG_{it} + \beta_4 ROA_{it} + \beta_5 CAR_{it} + \beta_6 D + \varepsilon_{it,}$ where: GE is profit earning; NPF is Non Performing Financing; FDR is Financing Debt to Ratio; GCG is composite of principle GCG; ROA is rate of eaning; CAR is capital must be provided of banks; D is dummy Sharia devisa bank which 1 and 0 for non devisa Sharia banks.

4. Result and Finding

This section discusses the data descriptions of each RGEC variable and then test results on the impact of RGEC implementation and profit growth on Sharia banking in Indonesia. Based on Table 1 below it can be explained that the value of Non Performing Financing tends toward decline although overall still on the healthy predicate. But initially in 2014 there are banks that have a fairly healthy value in particular; Bank JABAR and BANTEN Sharia, MANDIRI Sharia, MUAMMALAT and Victoria and Maybank compared to the previous year's health status. In other credit indicators, FDR, it is found that the value of risk that is not so good, especially in 2012 which has less healthy and quite healthy risk.

Table 2: Descriptives data

No	**Bank**	NPF (%)				
	Islam	2012	P	2013	P	2014
1	BCA	0.1	VH	0.1	VH	0.12
2	BNI	2.02	H	1.86	VH	1.86
3	BRI	3	H	4.06	H	4.6
4	BJB	4.46	H	1.86	VH	5.84
5	MANDIRI	2.82	H	4.32	H	6.84
6	Mega	2.67	H	2.98	H	3.89
7	MUAMALAT	2.09	H	1.35	VH	6.43
8	PANIN	0.2	VH	1.02	VH	0.53
9	BUKOPIN	4.57	H	4.27	H	4.07
10	Victoria	3.19	H	3.71	H	7.1
11	Maybank	2.49	H	2.69	H	5.04
	Average	**2.51**	H	**2.57**	**H**	**4.21**
	Max	**4.57**		**4.32**		**7.1**
	Min	**0.1**		**0.1**		**0.12**

Table 2: Descriptives data (continued)

No	**Bank**	FDR (%)					
	Islam	2012	P	2013	P	2014	P
1	BCA	79.9	H	83.48	H	91.17	EN
2	BNI	84.99	H	97.86	EN	92.98	EN
3	BRI	103.03	LH	102.7	EN	93.9	EN
4	BJB	87.99	EN	97.04	EN	84.02	H

5	MANDIRI	94.4	EN	89.37	EN	82.13	H
6	Mega	88.88	EN	93.37	EN	93.61	EN
7	MUAMALAT	94.15	EN	99.99	EN	84.14	H
8	PANIN	105.66	EN	90.4	EN	99.04	EN
9	BUKOPIN	91.98	EN	100.29	LH	92.89	EN
10	Victoria	73.78	EN	84.65	H	95.91	EN
11	Maybank	197.7	U	152.87	U	157.77	U
	Average	**100.2**	**LH**	**99.3**	EN	**97.6**	EN
	Max	**197.7**		**152.87**		**157.77**	
	Min	**73.78**		**83.48**		**82.13**	

Table 2: Descriptives data (continued)

No	**Bank**	GCG (%)					
	Sharia	2012	P	2013	P	2014	P
1	BCA	1.8	H	1.55	H	1.55	VH
2	BNI	1.25	VH	1.3	VH	2.12	H
3	BRI	1.38	VH	1.35	VH	1.74	H
4	BJB	2.53	EN	3	EN	2	H
5	MANDIRI	1.67	H	1.85	H	2.1	H
6	Mega	1.6	H	1.87	H	2	H
7	MUAMALAT	1.15	VH	1.15	VH	2.5	H
8	PANIN	1.35	VH	1.35	VH	1.4	VH
9	BUKOPIN	1.5	H	1.5	H	2	VH
10	Victoria	2.07	H	1.66	H	1.93	H
11	Maybank	2.3	H	2.17	H	2	H
	Average	**1.69**	**H**	**1.70**	**H**	**1.94**	**H**
	Max	2.53		3		2.5	
	Min	1.15		1.15		1.4	

Table 2: Descriptives data (continued)

No	**Bank**	ROA (%)					
	Sharia	2012	P	2013	P	2014	P
1	BCA	0.84	EN	1.01	EN	0.76	EN
2	BNI	1.48	H	1.37	H	1.27	H
3	BRI	1.19	EN	1.15	EN	0.08	LH
4	BJB	-0.59	U	0.91	EN	0.72	EN
5	MANDIRI	3.81	VH	2.33	VH	0.29	LH
6	Mega	1.54	H	1.37	H	0.17	LH
7	MUAMALAT	3.48	VH	1.03	EN	1.99	H
8	PANIN	0.55	EN	0.69	EN	0.27	LH
9	BUKOPIN	2.25	VH	1.53	H	0.17	LH
10	Victoria	1.43	H	0.5	EN	-1.87	U
11	Maybank	2.88	VH	2.87	VH	3.61	VH
	Average	**1.71**	**H**	**1.34**	**H**	**0.68**	**EN**
	Max	**3.81**		**2.87**		**3.61**	
	Min	**-0.59**		**0.5**		**-1.87**	

GCG Factor of all Sharia banking shows a good predicate as a whole although in the period of research there are also banks that have good predicate value at Bank JABAR and BANTEN Sharia. From profitability factor, ROA shows all banks toward profitability that leads to decline but still healthy enough. Except, Maybank has a very healthy ROA profitability while 10 other banks have instability in profitability. However, by 2014 there is a decrease in ROA value from 2012-2013 at 1.71 and 1.34 to 0.68.

No	**Bank**	CAR (%)					
	Islam	2012	P	2013	P	2014	P
1	BCA	31.47	VH	22.35	VH	29.57	VH
2	BNI	19.07	VH	16.23	VH	18.42	VH
3	BRI	11.35	H	14.49	VH	12.89	VH
4	BJB	21.09	VH	17.99	VH	15.78	VH
5	MANDIRI	13.82	VH	14.1	VH	14.76	VH
6	Mega	13.51	VH	12.99	VH	19.26	VH
7	MUAMALAT	11.57	H	17.05	VH	14.15	VH
8	PANIN	32.2	VH	20.83	VH	25.69	VH
9	BUKOPIN	12.78	VH	11.1	H	15.85	VH
10	Victoria	28.08	VH	18.4	VH	15.27	VH
11	Maybank	63.89	VH	59.41	VH	52.13	VH
	Average	**23.53**	VH	**20.45**	VH	**21.25**	VH
	Max	**93.89**		**59.41**		**52.13**	
	Min	**11.35**		**11.1**		**12.89**	

No	**Bank**	GE (%)					
	Islam	2012	P	2013	Ave. growth	2014	Ave. growth
1	BCA	0.273	-	0.434	-0.566	0.323	-0.677
2	BNI	0.707	-	0.907	-0.093	0.104	-0.896
3	BRI	5.05	-	0.123	-0.877	0.852	-0.148
4	BJB	0.387	-	0.338	-0.662	0.494	-0.506
5	MANDIRI	0.093	-	0.319	-0.681	0.470	-0.53
6	Mega	1.411	-	0.388	-0.612	0.875	-0.125
7	MUAMALAT	0.013	-	0.675	-0.325	0.66	-0.34
8	PANIN	3.142	-	0.248	-0.752	0.165	-0.835
9	BUKOPIN	0.196	-	0.295	-0.705	0.708	-0.292
10	Victoria	0.091	-	0.167	-0.833	0.089	-0.911
11	Maybank	0.612	-	0.38	-0.62	0.447	-0.55
	Average	**0.414**		**0.388**		**0.471**	
	Max	**5.05**		**0.907**		**0.875**	
	Min	0.013		0.123		0.089	

The fourth RGEC factor of CAR can be explained that all Sharia banking in Indonesia has a healthy CAR of all> 8%. In other words, Sharia banks are still able to keep the risks because the CAR ratio is still above 8%. The term is related to the macroeconomic variables that serve as one of the macroeconomic variables used in this study.

The inflation data for 2012 is 4.19 percent, in 2013 at 8.13 percent and 2014 at 8.08 percent or on an average of 0.349, 0.6775 and 0.6733 per annum respectively. The value of inflation when compared with the development of Sharia banking ROA shows almost no difference in 2014 between the two variables. This clearly makes the position of Sharia banking at risk in its operations. (Table 2 below)

Month	**Inflation (%)**		
	2012	2013	2014
1	0.76	1.03	1.07
2	0.05	0.75	0.26
3	0.07	0.63	0.08
4	0.21	(0.1)	(0.02)
5	0.07	(0.03)	0.16
6	0.60	1.03	0.43
7	0.70	3.29	0.93
8	0.95	1.12	0.47
9	0.01	(0.35)	0.27
10	0.16	0.09	0.47
11	0.07	0.12	1.5
12	0.54	0.55	2.46
Sum	**4.19**	**8.13**	**8.08**

5. The Effect of RGEC on Profit Growth

Before explaining the results of research, identification research model suitable for this research is conducted, i.e. the Pooled Least Squares or Fixed Effect Model (FEM) research model. Then, chow test are conducted to select both regression model. The test results of this Chow test needs to be done with respect to the probability value of cross section test value. If the value of F test more> 0.05% then the use of Pooled Least Square only is suggested without Hausman test. Based on the results of the research shows that cross section F-7.225> 0.05, then this research is enough with Pooled Least Square.

Table 4: Testing with Pooled Least Square the influence of RGEC to GE

Dependent Variable: GE			
Variable	Coefficient	t-Statistic	Prob.
C	131.7070	1.240789	0.2159
NPF	-23.85028**	-2.177923	0.0304
FDR	1.383676	1.088348	0.2776
GCG	-8.298324	-0.186916	0.8519
ROA	-26.56164	-1.499908	0.1350
CAR	-5.325023**	-2.144567	0.0330
Inflation	-65.77300**	-2.432190	0.0158
Dummy	112.2356***	2.932462	0.0037

R-squared	0.092689	R	0.304448
F-statistic	3.385788	Prob. F-statistic	0.001842

Based on Table 4 above, the regression model obtained is:
GE it = 131.7070-23.85028NPF + 1.383676FDR-8.298324 - 26.56164ROA-5.325023CAR-65.77300 + 112.2356 Dummy bank.
The result of the research found the ability of determination of all independent variables (NPF, FDR, GCG, ROA, CAR and Inflation) in explaining to statistical dependent variable showed low R-Square value, that is; 0.092689. This explains that the research variables used in this study are only able to affect as much as 9.2689% affecting profit growth in Sharia banking, while 90.7% is still influenced by other factors. The simultaneous test results of F test also found that all NPF, FDR, GCG, ROA, CAR and Inflation variables influence profit growth in Sharia banking in Indonesia. This is indicated by the value of F test 3.385788 with probability <0.05 or 0.001842.
The partial test results also show that NPF, CAR, inflation and dummy variables affect earnings growth in Sharia banks in Indonesia, while FDR, GCG and ROA do not affect profit growth in Sharia banking in Indonesia. The value of the NPF coefficient is negative -23.85028 ** with 5% significant means any decrease in loans or financing made by Sharia banking 100 points will increase the profit growth by 23 points. In other words, any increase in lending or financing of 100 points done by Sharia bank will lower profits by 23 points. The results of this study are aligned with (7) which state that Sharia banking today has been at risk. Another problem Sharia banking is facing is that high idle money that is not channeled for financing so as to increase profits. This condition requires Sharia banking management to require better governance (6, 10, 12)
While the CAR constant is negative -5.325023 ** with a significant value of 5%. This means any 100-point increase in Sharia banking capital will reduce the profit growth by 53 points, or any decline in value of CAR 100 will increase the profit growth of 53. This finding is as stated by Bilal & Amin (5); which mentions Sharia banking is still lower compared with other non sharia banking. Furthermore, Sharia banking required a more courageous policy in channeling funds but still in providing the customer with the essential. The same is also seen from the negative inflation coefficient -65.77300 ** with a significant value of 5%. This means that any 100-point inflation increase will reduce profit growth by 65 points, otherwise if inflation is lowered 100 will increase profit by 65 points. The findings of this study support the statement of (1,13) stating that Sharia banking faces challenges from the macroeconomics and internal factors of the bank. While the dummy variable of Sharia bank of foreign exchange has value 112.2356 *** with significant value 1%. This means that sharia and non-Sharia banks that operate as foreign exchange banks and non-foreign exchange have different performance between them.

5. Conclusion

This study focuses on Indonesian bank regulations or the Financial Services Authority that has circulated a rule on the implementation of risk profile indicators, good corporate governance, earning and capital. In addition, it includes inflation variable as one of macroeconomic indicators and Sharia bank of foreign exchange and non-foreign exchange or bank operational type as control variable. The results of the study found that the indicators of non-performing loans of Sharia banks are still high which makes Sharia banking at not at a very healthy level and make the banking conditions at risk. Indicators Capital Adequacy Ratio in Sharia banking is high enough which indicates idle money. This situation leads Sharia banking toward dilemma in high-risk intense financing or reducing to some extent to increase its profit growth. Furthermore, inflation in Indonesia has also contributed to eroding profit growth in Sharia banking. Because the current inflation with profit growth Sharia banks do not have much difference.

In addition, the study also found that the banking operations of Sharia banks that make foreign exchange and non-foreign exchange also affect the profit growth. This study has limitations because it only uses RGEC variables that serve as a measure of profit growth in Sharia banking in Indonesia. It is better to add some research variables such as quality of human resources, operational costs, wide range of bank operations, and also need to be studied Sharia banking products that trend in the community, especially sharia wisdom in Sharia banking locations that have branches in the district or city in the provinces of Indonesia.
The empirical results of this study imply that the management of Sharia banking is still grappling with internal and external issues. Internal bank problems, Sharia bank management needs to pay attention to credit disbursement (NPF) that has been channeled to customers. Because at this time, the condition of bank's risk profile is very high that is almost 24 percent make the decline in profit growth. It can be said that the financing of sharia banks have been congested so far has been channeled to customers. The external side, the management of sharia banks to be more prudent and aware of customer behavior and its relation to macroeconomic environment changes. Because macroeconomic significantly affect the decline in profit growth Bank Sharia up 65%. Another condition that pleases the sharia bank is still improving the GCG is still healthy average. However, the sharia bank also needs to consider its high capital adequacy level almost three times its minimum limit. In general, this condition makes Sharia banks still idle money but minimal distribution of financing.

Acknowledgement

We are happy to thank the AIC 2017 committee especially to Dr. Muhammad Imran Qureshi who has reviewed our article. And to Faculty Economic and Bussiness Universitas Malikussaleh Lhokseumawe who has provided financial support.

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