Intermediary Function, Capital Structure, Risk And Financial, Performance Of Islamic Bank In Indonesia

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Abstract: This study aimed to examine the influence of intermediary function and capital structure to financing risk and the influence of intermediary function, capital structure and financing risk to financial performance of islamic banks in Indonesia. This research use explanatory method which explains the effect of indpendent variables to dependent variables through a hypothesis test. The population of this research is islamic banks in Indonesia. Technique of samping uses a purposive sampling Research data is secondary data, consist of of 11 islamic banks during five years, 2013 upto 2017. Method of analysis data is strutural equation model with partial least square program. The finding of results concluded that (a) capital structure had a significant influence toward financing risk of islamic banks in Indonesia; (b) capital structure had a significant influence toward financial performance of islamic banks in Indonesia; (c) intermediary function had a significant influence toward financing risk of islamic banks in Indonesia; (d) intermediary function had no significant influence toward financial performance of islamic banks in Indonesia and (e) financing risk had a significant influence toward financial performance of islamic banks in Indonesia.

Index Terms: intermediary function, capital structure, risk, performance, islamic banks

1. INTRODUCTION

Islamic banking is very sensitive and closely affected by macroeconomic conditions. Indonesia's economic growth in 2013 was not as high as in previous years, which made the economic dynamics less conducive to the development of the real sectors. This had an impact on the performance of Islamic banks which experienced a slowdown from the previous year. This was marked by a decline in ROA of Islamic banking in 2013. Afifah and Hakim (2015) explained that profitability proxied by ROA in its development has always increased. But in 2013 the ROA of BUS and UUS decreased by 0.14 percent from the previous year. Profitability is the right indicator to measure a bank's performance and competitiveness (Sofyan 2002). One indicator used to measure the level of profitability is through Return on Assets (ROA) or the ratio of profit to assets. With the decline in ROA in 2013, an evaluation was needed regarding what could affect the financial performance of an Islamic bank. Departing from these problems, the researcherswere encouraged to examine the variables that had a direct or indirect influence on the financial performance of Islamic banks. By understanding the variables that influence the performance of Islamic banks, solutions could be obtained to solve the problems of financial performance of Islamic banks and answered the phenomenon of low financial performance of Islamic banks. Through theoretical and empirical studies, variables could be obtained which had a direct or indirect influence on the financial performance of Islamic banks as explained below.

Khan (2001) reveals that the survival and growth of Islamic banks depends in part on the ability of banks to manage risks related to bank business. This was also affirmed by Syed Jaafar Aznan that the success of Islamic banking in the future is highly dependent on the effectiveness of Islamic banks in managing their risks (Boediono, 2005). According to Arunkumar and Kotreshwar (2006) financing risk is the most dominant problem faced by banks, which is around 70% of total banking risk. The 30% rest is a combination of market risk and operational risk. This is in line with the opinion of Khan (2003) that financing risk is a source of uncertainty in a banking system. At the empirical level, Diallo et al (2015) found that there is a greater danger faced by Islamic banking related to the risk of financing compared to conventional banking. In addition, Fahrul et al (2012) and Afrianandra and Mutia (2014) found a significant relationship between the risk of murabahah and musharaka on the profitability of Islamic banks. The intermediation function is a key operational activity in the banking sector to support the achievement of expected bank performance. The intermediation function starts from collecting third party funds and then distributes funds collected in the form of financing. The results of Purwanto's (2012) study show that the intermediation function has a significant positive effect on the performance of Islamic banks in Indonesia directly or indirectly through financing risk. Decision on capital structure is very important influence on the company's financial performance because it relates to the proportion of funding that comes from the company's equity or liabilities. Salam (2012) uses debt variables such as short-term debt, long-term debt and total debt as a proxy for capital structure and he also found a negative relationship between capital structure and financial performance. Salam (2012) took samples from 237 companies from 1995-2011 listed on the Bursa Malaysia. This is in line with research by Pathak (2011) and Gleason et al (2000) who found that debt capital structure has a negative and significant effect on financial performance. Aji (2012) added a research reference using short debt to equity ratio, long term debt to equity ratio, total debt to equity ratio, firm size, and sales growth as factors that influence profitability. The result is a short debt to equity ratio, total debt to equity ratio, firm size, high sales growth which causes higher profitability. Different results were shown by Mireku, Mensah and Ogoe (2014) and Abor (2005) who concluded that the level of debt and capital structure had a positive effect on financial performance. Weston and Brigham (1994) state that one of the important decisions of financial managers to remain competitive in the long run is the decision regarding capital

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structure. Modigliani and Miller (1963) also argue that the level of debt affects the value of the company. Capital structure is important because it affects the financial position and risk of the company. The capital structure of financial institutions and banks is the determination of agency costs from the financial sector in the economy (Siddiqul and Shoaib, 2011) Based on the background that had been described before, some issues could be formulated as follows: (a) whether intermediary function had a significant influence on the financing risk of sharia banks in Indonesia; (b) whether intermediary function had a significant influence on the financial performance of sharia banks in Indonesia (c) whether capital structure had a significant influence on the financing risk of sharia banks in Indonesia; (d) whether capital structure had a significant influence on the financial performance of sharia banks in Indonesia and (e) whether financing risk had a significant influence on the financial performance of sharia banks in Indonesia.

2 LITERATURE REVIEW AND HYPOTHESIS DEVELOPMENT

2.1 Sharia Enterprise Theory

Islam is rahmatan lil alamin (mercy for all nature), this concept requires that the welfare created by the company be shared with the rightful, namely stakeholders in the broadest sense. The sharia enterprise theory does not only care about individual interests (in this case shareholders), but also other parties. Therefore the sharia enterprise theory has a big concern for broader stakeholders. According to the sharia enterprise theory, stakeholders include God, humans, and nature (Triyuwono, 2006b). God is the highest party and becomes the sole purpose of human life. The second stakeholders of sharia enterprise theory are humans who are divided into two groups, the direct and indirect stakeholders.Sharia enterprise theory balances between egoistic and altruistic values, material and spiritual values and finally, individual values andJama'ah ones. In Islamic sharia, this form of balance is concretely manifested in one form of worship, namely zakat (Triyuwono, 2006b). The consequence of this equilibrium value causes the sharia enterprise theory does not only concern the individual interests (in this case shareholders), but also other parties. Sharia enterprise theory has a broader range of accountability compared to entity theory. Accountability means accountability to God, humans, and nature (Triyuwono, 2006a: 35). Mulawarman et al (2006) explains that if Islamic banks are based on sharia ethics, Islamic banks automatically shouldnot make the results as the final goal. Instead, they also need to care about the process. The approach taken in this formulation was to proportionally position the process orientation and the results in the correct position.The approach proposed by Triyuwono (2006a) on performance in accordance with the definition of performance proposed by Prawiro (1997: 2), namely the work that can be achieved by a person or group of people in an organization, in accordance with the authority and responsibility of each in an effort to achieve goals the organization concerned is legal, not illegal and in accordance with moral and ethical ethics. This means that the work that has been achieved must go through the right process, one measure of which is not to violate the law and ethics. The sharia enterprise theory functions the religion law (sharia) as an integral part ofthe agency theory in order to create behavioral constraints in the form of a code of ethics for parties involved in the contractual relationship between principals and agents as well as between Islamic banks and mudharabah financing. If the parties involved in business transactions such as mudharabah contracts have faith in the eternal and prosperous life of the faith, it will affect the behavior of the parties involved as Islamic (ethical) and avoid actions that harm one another. Sarker (1999a) states that some researchers believe there are two reasons why the principal problem of agents will be small in the Islamic economy. First, Muslims believe in the eternal life of the faith, in which honest people will get a reward while dishonest ones will be punished. This is a nonmaterial incentive for dishonest people. Second, if all financial activities are based on division, honest entrepreneurs will encourage dishonest people out of the market.

2.2 Islamic Accounting Theory

According to Triyuwono (2006a: 328) Islamic accounting theory was developed by internalizing Islamic values into enterprise theory. One of the Islamic accounting development is the use of sharia enterprise theory in justifying sharia accounting. Islamic accounting does not only serve the interests of stockholders, but also all parties involved or broader stakeholders. That means there is an effort to protect the interests of the community that are directly or indirectly related. Even the flora and fauna which are part of the nature are considered important stakeholders as well. Thus, Islamic accounting is not merely talking about numbers. Instead, the domain of Islamic accounting also measures behavior. Consequently, sharia accounting becomes the mizan in the enforcement of trade order, equitable distribution, prohibition of quality fraud, scales, even including monitoring so that there is no conflict of interest between companies that can harm other groups (Triyuwono, 2006a: 40). The basic purpose of accounting as a means of conveying information and accountability can only be truly achieved if accounting and accountants themselves are bound by a set of rules that have more value than just a set of rules of human creation. Islamic accounting considers that the two basic objectives of accounting, namely providing information and accountability, are considered as a unity that cannot be separated from each other and this is what makes a big difference with the basic objectives of conventional accounting. Islamic accounting considers that the basic goal of accountability is not just horizontal accountability (hablum min al-nas) but also vertical one, which can be accounted to God (hablum min al-Allah). Kamayanti (2007) explains that the basic purpose of sharia accounting does not only emphasize the aspects of worldly matters but also the divinity. The final responsibility is therefore to Allah SWT as the absolute owner of the world, not only to the stakeholders. According to AAOIFI, Islamic banking financial statements should contain useful information to users, among others, namely: a. information about the compliance of Islamic banks to sharia provisions; b. information about economic sources and obligations, the effect of transactions relating to liabilities; c. information that helps related parties in determining zakat; d. information to help cash flow, time and risk; e. information to help evaluate responsibility for saving funds and investing funds; and f. information about bank obligations to the community (Hameed, 2006).Syahatah (2001) concludes that the specific characteristics of Islamic accounting include: a. the basic rules of sharia accounting come from the Qur'an, As-Sunnah An-

Nabawiyyah, and the jurisprudence of the scholars; b. Islamic accounting is based on strong faith and recognition that God is God, Islam is a religion, Muhammad is a prophet and apostle, and believes in the Last Day; c. Islamic accounting is based on good principles; d. an accountant is considered responsible in front of the community and the Islamic ummah about how far the economic unity is influenced by Islamic Sharia laws, especially those related to muamalah; e. accounting in Islam is also related to legitimate financial processes; f. accounting in Islam is very concerned about the behavioral aspects as elements that also play a role in the economic unity.

2.3 Islamic Banks

Islamic banks are: a. banks operating in accordance with Islamic sharia principles; b. banks whose operating procedures refer to the provisions of the Qur'an and hadith, especially those concerning the procedure for doingmuamalat in Islam (Muhammad, 2005: 1). In the procedure of doing muamalat it is shunned by practices which are feared to contain elements of usury to be filled with investment activities on the basis of profit sharing and trade financing. The Islamic banking system does not only focus on avoiding the practice of interest, but also the need to apply all Islamic principles in a balanced economy. Therefore, the balance between maximizing profits and fulfilling sharia principles is fundamental to the operations of Islamic banks (Bank Indonesia, 2002). According to Arifin (2006: 11) financial and banking activities can be seen as a vehicle for modern society to bring them to, at the very least, the implementation of two teachings for the Qur'an: the principle of at-ta'awun(mutual assistance and mutual cooperation among community members for the good) as stated in the Qur'an Surah al Maidah verse 2 (Indonesia's Ministry of Religion, 2005: 2) and the principle of avoiding al-iktinaz, (holding money (funds) and leaving it idle and not spinning in transactions that benefit the general public), as stated in Qur'an Surah an-Nisa verse 29 (Indonesia's Ministry of Religion, 2005: 107). A special form of financial contract that has been developed to replace the interest mechanism in Islamic financial transactions (sharia) is a profit-sharing mechanism. This profit-sharing mechanism is a core product for Islamic financial institutions, such as Islamic banks, since Islamic banks explicitly prohibit the application of interest rates on all financial transactions.

2.4 Capital Structure

Capital structure is an essential part of a company. In the financial management study, capital structure is oriented to how to fund operations of a company. Funding can focus on using debt or issuing shares (equity). According to Brigham and Erhardt (2005), the capital structure is described as "the firm's mixture of debt and equity". Thus the capital structure is a combination of capital with long term debt. At least, there are two theories of capital structure that are used as a reference for researchers. First, the Static Trade-Off theory which states that companies need to optimize funding with debt because the amount of debt is not directly related to the value of the company. In this case, a company manager is free to use a variety of debt options to increase the capacity of his company without worrying about the impact on the company's value. Second, Pecking Order Theory which explains that companie tend to choose internal financing rather than extern financing. Therefore, Marquez and Santosa (2003) state th capital structure decision making processes need to consider trade-offs between incentives and governance. Based on these two theories, banks and Islamic banks should increase internal funding options to strengthen their capital structure due to low levels of volatility and costs (Siringoringo, 2012; Buchory, 2006; Kishan and Opiela, 2000).

2.5 Intermediation Function

In general, the main function of banks is to conduct financial intermediation by carrying out the phase of transfer of funds covering the household, business and government sectors to parties experiencing a funding deficit. Quoting Saunders (2008) the occurrence of the banking intermediation process is due to the high price risk, liquidity costs and monitoring costs. This condition results in information asymmetry that encourages the role of banks as an intermediary institution that is trusted by both parties. In the perspective of Islamic banking, the intermediation function has fundamental differences with conventional banking. distribution of funds to the public using a financing approach not in the form of a loan. Intermediation in the context of isalmic banks are more directed to assist customers in developing their business, this is in line with the principle of mutual help (ta'awun). Through the concept of profit sharing and risk sharing, making Islamic banking and customers are in the same position and fair.

2.6 Financing Risk

In Muhammad's view (2002) the majority of Islamic banking products carry many risks such as moral hazard, system risk and information asymmetry. Therefore it becomes a challenge for Islamic banking how to minimize risk to get optimal profits (Sholahuddin, 2004). Although it must be realized that there is no government regulation that specifically and specifically regulates how to manage syari;ah banking risk (Samsudin et al, 2003). There are two financing models in their sharia contracts, they are Natural Certainty Contracts (NCC) based financing and Natural Uncertainty Contracts (NUC) based financing. NCC financing has definite properties in terms of profit, quantity and delivery time. Conversely, NUC financing is uncertain. This NUC has a high risk of uncertainty, thereby driving up the risk of Islamic bank financing.

2.7 Financial Performance

Banking financial performance shows the financial condition of the bank which includes aspects of raising funds and distributing funds (Mutia and Musfirah, 2017). According to Mulyadi (2001) performance appraisal is more focused on determining organizational effectiveness on a regular basis based on predetermined criteria. In fact some financial ratios used in conventional banking can be used with some modifications to adjust the situation and conditions that exist in Islamic banking

Research Conceptual Framework

Based on the theoretical basis that has been described, here is the conceptual framework in this study to describe the influence of intermediary function and capital structure toward financing risk and financial performance and the influence of risk toward financial performance of sharia banks in Indonesia.

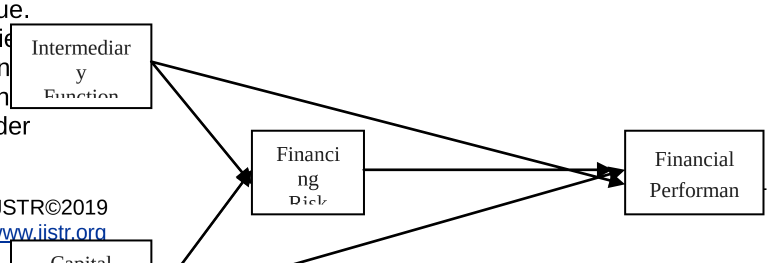

Figure 1. *Research Conceptual Framework*

Based on theoretical basis and research conceptual framework above, the research hypothesis were as follows:

H1 : intermediary function had a significant influence toward the financing risk of islamic banks in Indonesia;

H2 : intermediary function had a significant influence toward the financial performance of islamic banks in Indonesia

H3 : capital structure had a significant influence toward the financing risk of islamic banks in Indonesia;

H4 : capital structure had no significant influence toward the financial performance of islamic banks in Indonesia, and;

H5 : financing risk had a significant influence toward the financial performance of islamic banks in Indonesia.

Research Methods

The type of research used was explanatory research, which aims to analyze the relationships between one variable with another variable or how a variable affects other variables. This study was intended to explain the causal relationship between the research variables and test the hypotheses that had been formulated. The type of data used in this study was secondary data. Secondary data is a source of research data obtained by researchers indirectly through intermediary media or obtained and recorded by other parties. The data was obtained from annual reports and financial statements of Indonesia's sharia banks between the year 2013 to 2017. These reports were obtained from the Indonesian Banking Directory at the Financial Services Authority and the official website of each sharia commercial bank. The populations in this study were all Islamic Commercial Banks that have been registered in the Indonesian Banking Directory. The research sample was taken by using purposive sampling method, in which the sample is not selected randomly due to certain goals being targeted (Indriantoro and Supomo, 2009). The research samples are all sharia commercial banks that have been registered in the Indonesian Banking Directory and had published annual reports, and the financial reports between the year 2013 to 2017. This study used two types of research variables, exogenous variables and endogenous variables. Exogenous variables are variables that are considered to have an influence on other variables, but are not influenced by other variables in the study. Exogenous variables in this study are intermediary functions and capital structure. Endogenous variables in this study are financing risk and financial performance of sharia commercial banks.

In this study, the Partial Least Square (PLS) approach using SmartPLS software was used to analyze the data. PLS is a variant-based structural equation (SEM) analysis that can simultaneously test measurement models while testing structural models. PLS is an alternative approach that shifts from a covariant SEM-based approach to a variant based. Covariance-based SEM generally tests causality or theory while PLS is more predictive. PLS is a powerful analytical method because it is not based on many assumptions.

4 RESULTS AND DISCUSSION

Path analysis was used to analyze the pattern of relationships between variables in order to determine the direct or indirect effects of a set of independent variables (exogenous) on the dependent variable (endogenous). Through this path analysis, which path was the most precise and short of an exogenous variable towards the endogenous variable that was bound could be found easily. The following is the path analysis model shown in figure 2 on the path analysis results.

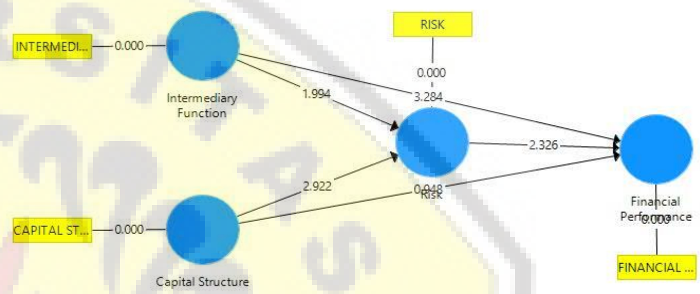

Figure 2. *Path Analysis Model*

The test results on the hypothesis proposed in this study were obtained based on testing the path coefficient of the path analysis model in table 1. If the p value is smaller than 0.05 then the influence relationship between the variables is considered significant. Conversely, if the p value is greater than 0.05 then the influence relationship between variables is considered not significant. Hypothesis test results were explained in the following table.

Table 1. Result ofPath Coefficients

	Original Sample (O)	Sample Mean (M)	Standard Deviation (STDEV)	T Statistics (O/STDEV)	P values
Capital Structure -> Financial Risk	0.595	0.577	0.187	3.175	0.002
Capital Structure -> Financial Performance	0.349	0.344	0.171	2.038	0.042
Intermediary Function -> Financial Risk	-0.319	-0.342	0.143	2.229	0.026
Intermediary Function -> Financial Performance	-0.074	-0.065	0.076	0.978	0.328
Financial Risk -> Financial Performance	0.292	0.320	0.096	3.036	0.003

Based on table 1, the results of hypothesis testing were explained as follows:

1. Hypothesis one (H1): Capital structure had a significant effect on financingrisk.Testing of the first hypothesis was seen from the coefficient of 0.595 with p-value of 0.002 and

t-value 3.175. Hypothesis one was proven to be valid because the p-value <α and t-value >t-tabel then capital structure had a significant effect on financial risk. Hypothesis one (H1) was therefore accepted. Based on these statistical calculations, it is known that the capital structure owned by Islamic banking is positively related to the increased risk of financing. Sharia principles encourage Islamic banks not to use debt mechanisms in their capital funding, but rather rely on their own capital (equity). This has an effect on the increasing potential for failure to repay financing from customers because the agreed contract is based on the principle of profit sharing and risk sharing between the Islamic bank and the customer.

2.Hypothesis two (H2): Capital structure had a significant effect on financialperformanceTesting the second hypothesis was seen from the coefficient of 0.349 with p-value of 0.042 and t-value 2.038. The second hypothesis was proven valid because the p-value <α and t-value >t-table then the capital structure had a significant effect on financial performance. Hypothesis two (H2) was therefore accepted. This finding confirms that in the sharia agreement, the nature of mutual trust becomes a strong foundation to produce "barokah" profits for both Islamic banks and customers. The use of own capital for Islamic banks does not have a negative impact, instead it gives trust to customers to increase their business so that it can generate profits and greater profit sharing.

3. Hypothesis three (H3): Intermediary function had a significant effect on financingrisk. The testing of the third hypothesis was seen from the coefficient of -0.319 with p-value of 0.026 and t-value 2.229. The third hypothesis was proven to be valid because of the p-value <α and t-value >t-table then intermediary function had a significant effect on financial risk. Hypothesis three was thereforeaccepted. Referring to the banking literature, the intermediation function is described as banking activities in collecting third party funds and distributing them in the form of financing. It has an impact on increasing the risk of financing due to uncertainty in the return of the financing. The findings of this research are in line with the results of the research of Firmansyah and Nasrulloh (2013) and Lestari and Hisamuddin (2016) which state that the intermediation function in Islamic banking can increase the risk of financing.

4. Hypothesis four (H4): Intermediary function hadno significant effect on financial performance. Testing the fourth hypothesis was seen from the coefficient of -0.074 with p-value of 0.328 and t-value 0.978. The fourth hypothesis was proven to be invalidbecause the p-value >α and t-value <t-table then the intermediary function had no significant effect on financial performance. Hypothesis four was therefore rejected. This result provides an important justification that the amount of the intermediation function is not able to improve financial performance. Supporting the findings of the previous hypothesis that the magnitude of the intermediation function actually increases the risk of financing and does not have any impact on the financial performance of Islamic banking.

5. Hypothesis five (H5): Financing risk had a significant effect on financial performance. Testing the fifth hypothesis was seen from the coefficients of 0.292 with p-value of 0.003 and t-value 3.036. The fifth hypothesis was proven to be valid because the p-value <α and t-value >t-table then financial risk has a significant effect on financial performance. In other words, hypothesis five was therefore accepted. These results indicate that the higher the risk of financing the higher the financial performance of Islamic banking. In line with the concept of high risk high return, this also occurs in Islamic banking. Even though the financing funds issued by Islamic banks are large that makes the risk of financing is also getting bigger, but it actually increases the profits of Islamic banks. This finding is in line with the results of the study of Afrianandra and Mutia (2014) and Dzulkarnain and Asrori (2017) which show a positive impact between financial risk and financial performance.The coeffici90ent of determination (R^2) essentially measures how far the model's ability explains the variation of the dependent variable. The coefficient of determination is between zero and one. The small value of R^2 means that the ability of independent variables to explain variations in the dependent variable is very limited. A value close to one means that the independent variables provide almost all the information needed to predict variations in the dependent variable (Ghozali, 2006). The following is the result of the analysis of the coefficient of determination which can be seen in the adjusted R square table:

Table 2. Determination Coefficient Test Results

Model		R Square	Adjusted R Square
1	Financing Risk	0.219	0.170
2	Financial Performance	0.332	0.267

Based on Table 2 above there was a coefficient of determination (Adjusted R square) of 0.170 for the regression model 1. The percentage effect of the intermediary function and capital structure variable on the financing risk variable can be obtained by multiplying the R square value by 100%. Then the results obtained from the test of the coefficient of determination are 17%. This value indicated that the ability of independent variables in this case intermediary function and capital structure can explain the dependent variable in this case financing risk is equal to 17% while the remaining 83% is explained by other variables not examined or which are not included in the regression model. In the regression model 2, the coefficient of determination (Adjusted R square) is 0.267. The percentage of the influence of intermediary function, capital structure and financing risk variables on financial performance variables can be obtained by multiplying the R square value by 100%. Then the results obtained from the test coefficient of determination rose to 26.7%. This value showed that the ability of the independent variable in this case intermediary function, capital structure and financing risk can explain the dependent variable in this case financial performance is 26.7% while the remaining 73.3% is explained by other variables that are not examined or that are not entered in the regression model.

CONCLUSION

This study aims to examine the factors that influence financial performance by placing financing risk as a mediating variable. The results showed that: first, Capital structure had a significant influence on the financing of risk of sharia banks in Indonesia, second, capital structure hada significant influence on the financial performance of sharia banks in Indonesia, third, intermediary function had a significant influence on the financing of risk of islamic banks in Indonesia, forth, intermediary function had no significant influence on the financial performance of sharia banks in Indonesia, and fifth, Financing risk had a significant influence on the financial performance of islamic banks in Indonesia. The theoretical and practical implications of this research are at least able to provide different scientific treasures in the discussion about the risks of financing and financial performance in Islamic banking. Although the empirical findings of this research are not new, at least it can provide another perspective, especially regarding the influence of capital structure and intermediation factors on the financial performance of Islamic banking in Indonesia. The limitations of this study are in one variable that does not significantly affect financial performance namely the intermediation function. Therefore recommendations for future studies of moderation or mediation variables can be developed using these intermediation function variables.

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