THE FACTORS THAT INFLUENCE THE FINANCIAL PERFORMANCE OF ISLAMIC BANKS

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Article history:
Received
4 July 2024

Revised
21 August 2024

Accepted
30 October 2024

Available online
22 January 2025

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How to Cite:
Yanti E. M., Syahrum A., MA., Denni, Yulianti R., Boihaki, & Al-Shaibah A. A. A. B. (2025). The Factors That Influence The Financial Performance of Islamic Banks. Jurnal Aplikasi Bisnis Dan Manajemen (JABM), 11(1), 66. https://doi.org/10.17358/jabm.11.1.66

Abstract:

Background: The distinction between sharia and conventional practices has enabled sharia banks to withstand monetary crises. It is crucial to assess Sharia Commercial Banks' performance using capital adequacy ratios, operating expenses to income, net operating margin, and non-performing financing. These metrics help increase bank income through return on assets and address high financing issues, ensuring operational efficiency and alignment with management expectations.
Purpose: This research aims to determine the factors that influence the performance of Sharia Commercial Banks which are proxied by return on assets as the dependent variable, capital adequacy ratio, operating expenses to operating income and net operating margin as the independent variable and non-performing financing as the intervening variable.
Design/methodology/approach: This research is quantitative research using secondary data through financial reports. The total population from 2017 to 2023 is 16 banks. The analytical method used in this research is panel data regression with the help of the Eviews application through the Chow, Hausman and Lagrange tests.
Finding/result: The research results show that the capital adequacy ratio has no effect on non-performing financing, operating expenses to operating income has no effect on non-performing financing, net operating margin has an effect on non-performing financing, the capital adequacy ratio has no effect on return on assets, operating expenses to operating income has an effect on return on assets and net operating margin has no effect on return on assets. Then the indirect influence is that non-performing financing is unable to mediate the influence of capital adequacy ratio on return on assets, non-performing financing is unable to mediate the influence of operating expenses to operating income on return on assets and non-performing financing is unable to mediate the influence of net operating margin on returns.
Conclusion: The capital adequacy ratio, operating expenses to operating income and net operating margin have no influence on non-performing financing, then the capital adequacy ratio, net operating margin and non-performing financing have no influence on returns. on assets, while operating expenses to operating income have an influence on return on assets. An indirect influence can be conveyed that non-performing financing is unable to mediate the capital adequacy ratio, operating expenses to operating income, net operating margin to return on assets. This research can be used as a guide for assessing business performance through the factors that influence it.
Originality/value (state of the art): In assessing the relationship between capital adequacy ratio, operating expenses to operating income and net operating margin to non-performing financing mediated by return on assets, this research explores the contributing factors to the prosperity of developing countries, especially Indonesia, which can help investors and policy makers in making decisions. appropriate way to improve company performance.

Keywords: capital adequacy ratio, net operating margin, return on assets, non-performing financing, operating expenses on operating income

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INTRODUCTION

Banks are companies that operate in the service business, where public trust will occupy a very large portion in maintaining their survival (Kweh et al. 2024). As a trust institution, banks in their operations use more funds from the public than their own capital from owners or shareholders (Gutiérrez-López & Abad-González, 2020), therefore bank managers in carrying out their business are required to be able to maintain a balance between maintaining liquidity sufficient to achieve reasonable profitability, as well as meeting adequate capital.

Indonesia has the largest Muslim majority in Asia, therefore it is natural that people choose sharia banks, especially after the sharia banking monetary crisis began to emerge (Hudayati, 2023). The differences in sharia and conventional practices resulted in banks being able to survive in the era of monetary crisis (Setiawan, 2023). Islamic banks adhere to profit sharing, while conventional banks adhere to interest. Sharia banks are banks that operate in accordance with sharia principles, the basic principles of sharia banking are the principles of being free from maysir, gharar, haram, usury and vanity (Sofilda et al. 2022).

According to Abasimel (2023), banks based on a service payment system are divided into two, namely banks based on interest payments (conventional) and banks based on payments in the form of profit sharing (syariah). Muhdar et al. (2023) state that Islamic banks are banks that operate without relying on interest. Or in other words, an Islamic Bank is a financial institution whose main business is providing financing and other services in payment traffic and money circulation whose operations are adjusted to sharia principles. Sharia banking as part of the national banking system has an important role in the economy.

Agency theory is a theory that focuses on learning the contract design for solving agency problems and agency costs arising as a result of agency relations, especially the delegation of decision-making to agents. Agency theory is a part of positive accounting theory, game theory, and organizational theory. Positive accounting theory is a theory trying to explain and predict which company will not use certain accounting methods and accounting methods that have to be used for the company (Watts & Zimmerman, 1986). Game theory aimed to understand the situation where decision-makers interact (Osborne, 2000).

Sharia accounting principles are based on the principle of voluntarism, meaning that there should be no oppressors or disadvantaged parties, costs arise because there are business results and risks arise because there are profits (Apriyanti, 2017). A conceptual framework is an integrated structure that establishes a relationship between goals and their underlying premises (Faiz, 2020). Financial reports that adhere to accounting and reporting standards are expected to have transparent direction, function and boundaries, so that their objectives and foundation are solid.

The Sharia Accounting Committee and the Financial Accounting Standards Board (DSAK) must prepare and determine an absolute basic framework to be used as a basis for developing Financial Accounting Standards. KDPPLKS is a basic framework that has been developed for the preparation and presentation of Sharia Banking Industry Reports (Aulia & SE, 2020; Widiana, 2017).

The increase and decrease in the percentage of financial performance can be observed from 2017 to 2023. Based on data from the Financial Services Authority (www.ojk.go.id), we can see the trends and phenomena that occurred during this period.

Based on Figure 1 it can be explained that, he Return on Assets (ROA) in 2017 had an average percentage of 0.63%. In 2018, the ROA percentage increased to 1.28%, followed by 1.73% in 2019, 1.40% in 2020, 1.55% in 2021, and 2.03% in 2022. The ROA remained at 2.03% in 2023. Notably, from 2019 to 2020, the global pandemic significantly impacted various sectors of the economy, including Islamic banking, which experienced a downturn during this period (Amala et al. 2023).

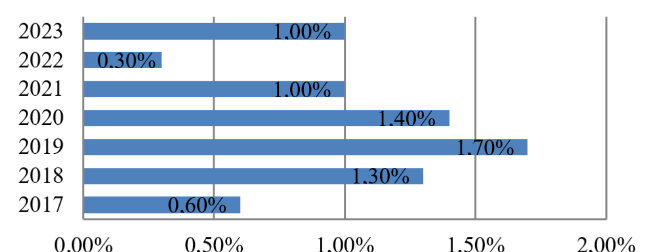


Figure 1. Percentage of return on asset

Arifian & Noor (2022); Hernawati et al. (2021); Priyadi et al. (2021); concluded that the capital adequacy ratio (CAR) has an effect on non-performing financing (NPF). Jusni et al. (2019) stated that operating expenses for operating income (OEOI) has no effect on non-performing financing (NPF). Jusni et al. (2019) stated that net operating margin (NOM) has an effect on non-performing financing (NPF). Marsintauli et al. (2023); Apau & Sibindi, (2023); Awwad, (2021); Puspitasari et al. (2021) states that the capital adequacy ratio (CAR) has a positive effect on return on assets (ROA) while according to Ali et al. (2023); Sugiono et al. (2023); Saleh & Paz, (2023); Widarjono, (2018) has no effect on Return on Assets (ROA) and Maya, M, (2017) capital adequacy ratio (CAR) has a negative effect on return on assets (ROA). Islam & Rana, (2017); Widarjono, (2018); Puspitasari et al. (2021); Karamoy & Tulung, (2020) states that operating expenses for operating income (OEOI) has a positive effect on Return on Assets (ROA) while according to Ali et al. (2023); Herciu & Șerban, (2018) has no influence on return on assets (ROA). Aysen Doyran, (2013); Puspitasari et al. (2021); Karamoy & Tulung, (2020) states that net operating margin (NOM) has a positive effect on Return on Assets (ROA) while according to Said & Ali, (2016); has no influence on Return on Assets. According to Islam & Rana, (2017); Priyadi et al. (2021); Ismail, D, (2021) non-performing financing (NPF) influences return on assets, whereas according to Ali et al. (2023); Widarjono, (2018) has no influence on return on assets.

Therefore, this study contributes to the existing literature in the following ways: first, by providing recent empirical evidence on the factors influencing the financial performance of Islamic banks in Indonesia from 2017 to 2023; second, by offering insights into the operational efficiency of Islamic banks and how it contributes to profitability, as proxied by Return on Assets (ROA); third, by serving as a resource for Islamic bank management to improve asset and capital management strategies to enhance financial performance; and fourth, by providing regulatory authorities, such as the Otoritas Jasa Keuangan (OJK), with findings that can inform policy formulation to support the stability and growth of Islamic banks in Indonesia.

This study examines and evaluates the factors influencing the financial performance of Islamic banks in Indonesia, as measured by Return on Assets (ROA). The specific objectives are to assess the impact of Capital Adequacy Ratio (CAR) on Non-Performing Financing (NPF) and ROA, to evaluate the effect of Operational Efficiency Ratio (OEOI) on NPF and ROA, to analyze the influence of Net Operating Margin (NOM) on NPF and ROA, and to investigate whether NPF mediates the relationship between CAR, OEOI, NOM, and ROA. Understanding the factors that affect the financial performance of Islamic banks is crucial for their sustainability and growth, especially in facing challenges such as economic crises and pandemics. Additionally, this research aims to fill the literature gap regarding the financial performance of Islamic banks.

METHODS

This quantitative research aims to measure the effect of independent variables on the dependent variable through an intervening variable in Islamic Commercial Banks in Indonesia, using secondary data. The independent variables include the Capital Adequacy Ratio, Operating Expenses to Operating Income, and Net Operating Margin. The dependent variable is Return on Assets, while the intervening variable is Non-Performing Financing.

The data were obtained from financial reports downloaded from the official websites of the respective banks and the official website of the Otoritas Jasa Keuangan (www.ojk.ac.id). Data collection in this study used census data, with all 16 Islamic Commercial Banks in Indonesia from 2017 to 2023 included as the research subjects. The number of research subjects from 2017 to 2023 can be seen in Table 1.

Table 1. Research population

The number of Islamic banks per year	Number of Companies
2017	15
2018	15
2019	15
2020	15
2021	13
2022	13
2023	13
Total	99

Source: OJK (www.ojk.go.id)

The analytical method used in this research is panel data regression with the help of software, namely Microsoft Excel and Eviews. Data processing carried out includes: 1) model selection, namely the Chow test is carried out to select the common effect model (CEM) or fixed effect model (FEM), the Hausman test is carried out to select the fixed effect model (FEM) or random effect model (REM).), the Legrange Multiplier test is carried out to select the Common Effect Model (CEM) or Random Effect Model (REM). In panel data regression based on Ordinary Least Squared (OLS) is the Common Effect Model (CEM) and Fixed Effect Model (FEM), thus it is necessary to test the classical assumptions. On the other hand, if the regression equation is more suitable using the Random Effect Model (REM), then there is no need to test classical assumptions, because the Random Effect Model (REM) uses the General Least Squared (GLS) approach in its estimation technique (Baltagi & Baltagi, 2008). 2) hypothesis testing, namely substructural hypothesis test I and substructural hypothesis test II consisting of: t test, F test, R Square. 3) Sobel test from 3 categories, namely z mediates x1 to y, z mediates x2 to y and z mediates x3 to y.

The Capital Adequacy Ratio (CAR) is a ratio that indicates the extent to which a bank's risk-weighted assets (loans/financing, investments, securities, claims on other banks) are financed by the bank's own capital, in addition to funds obtained from external sources (Gharaibeh, 2023). It can be explained that the Capital Adequacy Ratio is a bank performance ratio used to measure the sufficiency of a bank's capital to support its assets (Alrwashdeh et al. 2023). According to Fitriani (2023), Non-Performing Financing (NPF) refers to a situation where a customer is unable to meet part or all of their obligations to the bank as agreed upon (Alshubiri & Al Ani, 2023). Every bank must be able to manage its credit effectively, both in granting loans to the public and in ensuring loan repayment according to the applicable terms and conditions, to prevent the occurrence of non-performing financing. Therefore, there is a positive relationship between the Capital Adequacy Ratio and Non-Performing Financing.

H1: There is a positive relationship between the Capital Adequacy Ratio and Non-Performing Financing.

The Operating Expenses to Operating Income (OEOI) ratio is a financial metric used to measure the efficiency and effectiveness of a bank in conducting its operational activities. This ratio assesses the ability of operational income to cover operational expenses, providing insights into the bank's performance. According to Widarjono (2018), the OEOI ratio reflects a bank's efforts to minimize operational risk, which is the uncertainty associated with the bank's business activities. Operational risk stems from losses and the potential failure of the services and products offered. A high OEOI ratio indicates that a bank's operational expenses exceed its operational income. According to Islam & Rana (2017), Non-Performing Financing (NPF) refers to a situation where a customer is unable to meet part or all of their obligations to the bank as agreed upon. Therefore, there is a positive relationship between Operating Expenses to Operating Income and Non-Performing Financing.

H2: There is a positive relationship between Operating Expenses to Operating Income and Non-Performing Financing.

A higher Net Operating Margin (NOM) in a bank indicates better performance, as NOM positively affects profit growth. This ratio can also be used to measure the bank management's ability to manage productive assets to generate net interest income (Karamoy & Tulung, 2020). According to Ali et al. (2023), Non-Performing Financing (NPF) refers to a situation where a customer is unable to meet part or all of their obligations to the bank as agreed upon. Every bank must effectively manage its credit to the public and ensure loan repayments according to the applicable terms and conditions to prevent non-performing loans. Therefore, there is a positive relationship between Net Operating Margin and Non-Performing Financing.

H3: There is a positive relationship between Net Operating Margin and Non-Performing Financing.

The most important indicator for measuring a bank's performance is profitability. Profitability gauges the extent to which a company can generate profit in relation to sales, assets, and equity (Sharma et al. 2022). Bank Indonesia places significant emphasis on a bank's profitability, measured by assets predominantly funded by public deposits. Therefore, when assessing banking profitability, Return on Assets (ROA) more accurately represents a bank's performance. The Capital Adequacy Ratio (CAR) is a measure that indicates the extent to which a bank's risk-weighted assets (such as loans/financing, investments, securities, and claims on

other banks) are financed by the bank's own capital, in addition to funds obtained from external sources (Gharaibeh, 2023).

H4: There is a positive relationship between the Capital Adequacy Ratio and Return on Assets.

If the Operating Expenses to Operating Income (OEOI) ratio is high, it means that the bank's operational expenses exceed its operational income. When a bank's operational income is low, the bank's profitability (ROA) tends to be low as well. This indicates an inverse relationship between OEOI and the profitability (ROA) of a bank, consistent with the findings of Islam & Rana (2017), Widarjono (2018), Puspitasari et al. (2021), and Karamoy & Tulung (2020), who state that OEOI affects the ROA of Islamic banks.

H5: There is an inverse relationship between Operating Expenses to Operating Income and Return on Assets.

Net Operating Margin (NOM) is the ratio of net interest income to the average productive assets of a bank. A higher NOM indicates better bank performance, as NOM positively impacts profit growth (Sharma et al. 2022). This ratio can also be used to assess a bank's management capability in handling its productive assets to generate net interest income. As the net interest income generated by the bank increases, the bank's profitability, as indicated by the Return on Assets (ROA), also increases (Abdelmoneim & Yasser, 2023). This finding is consistent with research by Aysen Doyran (2013), Puspitasari et al. (2021), and Karamoy & Tulung (2020), which shows that NOM affects ROA.

H6: There is a positive relationship between Net Operating Margin and Return on Assets.

A higher Non-Performing Financing (NPF) indicates that a bank is exposed to greater financing risks (Natufe & Evbayiro-Osagie, 2023). Consequently, an increase in NPF will lead to a decrease in the bank's profitability (ROA). This is due to the higher costs incurred by the bank, including increased provisions for productive assets (Alshubiri & Al Ani, 2023). Thus, it can be concluded that NPF has a negative impact on the profitability of Islamic banks. This finding is consistent with research by Islam & Rana (2017), which states that NPF negatively affects ROA in Islamic banks.

H7: Non-Performing Financing has a negative relationship with Return on Assets.

Every bank must effectively manage its credit both in terms of lending to the public and in ensuring loan repayments according to the applicable terms to avoid non-performing financing. Profitability measures the extent to which a company can generate profit in relation to sales, assets, and equity (Sharma et al. 2022). Therefore, it can be concluded that high Non-Performing Financing (NPF) will influence the relationship between Capital Adequacy Ratio (CAR) and Return on Assets (ROA).

H8: Non-Performing Financing mediates the relationship between Capital Adequacy Ratio and Return on Assets.

The Operating Expenses to Operating Income (OEOI) ratio measures the ability of operational income to cover operational expenses, reflecting the performance of the bank. According to Islam & Rana (2017), the OEOI ratio represents a bank's effort to minimize operational risk, which involves uncertainties in the bank's business activities. Operational risk arises from losses and potential failures of the services and products offered. When financing problems are managed effectively, it can lead to an improvement in Return on Assets (ROA).

H9: Non-Performing Financing mediates the relationship between Operating Expenses to Operating Income and Return on Assets.

In Islamic banks, Net Interest Margin (NIM) can also be referred to as Net Operating Margin (NOM) because Islamic finance does not involve interest principles. A higher NOM indicates better bank performance, as NOM positively affects Return on Assets (ROA) (Riadi, 2018). In addition to emphasizing high Non-Performing Financing, effective management of NOM can lead to improved ROA, helping the bank maintain its financial health.

H10: Non-Performing Financing mediates the relationship between Net Operating Margin and Return on Assets.

Based on Figure 2, the conceptual framework can be explained as follows: The Capital Adequacy Ratio (CAR), which measures a bank's financial health, has a relationship with Non-Performing Financing (NPF). Operating Expenses to Operating Income (OEOI) also influences Non-Performing Financing (NPF). Likewise, the Net Operating Margin (NOM) affects Non-Performing Financing (NPF). Return on Assets (ROA), which measures profitability based on the assets held,

is directly impacted by Non-Performing Financing (NPF). Furthermore, Non-Performing Financing (NPF) mediates the effect of the Capital Adequacy Ratio (CAR), Operating Expenses to Operating Income (OEOI), and Net Operating Margin (NOM) on Return on Assets (ROA) in Islamic Commercial Banks in Indonesia.

RESULTS

Selection of sub structure models I

Based on the Chow test carried out, the value of prob. is 0.000 < 0.05, then the Fixed Effect Model (FEM) model is chosen. then the test carried out is the Hausman test, prob value. obtained is 0.8482 > 0.05 then the REM model was selected. And finally, Based on the Lagrange Multiplier (LM) test carried out, if 0.00 < 0.05 then REM is selected. REM assumes that each company has a different intercept, where the intercept is a random variable. Because the model chosen is REM (Least Dummy Variable), there is no need to make classical assumptions. REM and FEM do not need to make classical assumptions.

The model chosen is REM

t test (Partial influence)

Based on Table 2, it can be explained that the value of 0.3493 > 0.05, so Hypothesis 1 is rejected, which means that the capital adequacy ratio has no effect on non-performing financing in Islamic commercial banks. Prob value. x2 has a value of 0.8121 > 0.05, so the hypothesis 2 is rejected, which means that operating expenses to operating revenues have no effect on non-performing financing. Prob value. x3 has a value of 0.4910 > 0.005, so the hypothesis 3 is rejected, which means the net operating margin has no influence on non-performing financing.

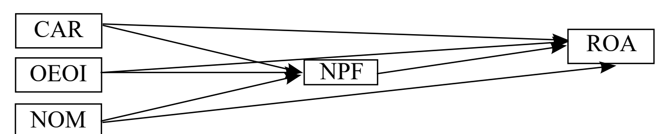
F Test

Based on Table 3, it can be explained that, Prob value. 0.6935 > 0.05, then the hypothesis 4 is rejected, namely the capital adequacy ratio, operating expenses to operating revenues and net operating margin variables together have no effect on the non-performing financing variable. In addition, based on table 3, it can be explained that Variables capital adequacy ratio (X1), operating expenses to operating income (X2), and net operating margin (X3) are unable to explain variable non-performing financing (Z), this can be seen from the Adjusted R-squared value, namely -0,016190.

Sub-Structural Hypothesis Test II

t test (partial influence)

Based on Table 4, the obtained Prob value for the Capital Adequacy Ratio (X1) is 0.0662. This indicates that the Capital Adequacy Ratio has no relationship with on return on assets (Hypothesis 5). Meanwhile, the Prob value for Operating Expenses to Operating Income (X2) is 0.0001. This indicates that Hypothesis 6 is accepted, meaning that Operating Expenses to Operating Income (X2) has a relationship with return on assets. And the Prob value for Net Operating Margin (X3) is 0.5243, which explains that Hypothesis 7 is rejected. This means that the Net Operating Margin (X3) has no relationship with Return on Assets. It can be explained that prob x3 is 0.5243, so the hypothesis 8 is rejected, which means the net operating margin has no effect on return on assets. Prob. z is 0.3462, then the 9th hypothesis is rejected, namely non-performing financing has no effect on return on assets in Islamic commercial banks.



Note: Capital Adequacy Ratio (CAR); Non-Performing Financing (NPF); Operating Expenses to Operating Income (OEOI); Net Operating Margin (NOM); Return on Assets (ROA),

Figure 2. Framework of thought

Table 2. Partial influence

Dependent Variable: Z				
Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	2.318641	0.505841	4.583732	0.0000
X1	-0.004038	0.004293	-0.940602	0.3493
X2	-6.73E-06	2.82E-05	-0.238339	0.8121
X3	-0.000902	0.001304	-0.691496	0.4910

Table 3. F Test

R-squared	0.015239
Adjusted R-squared	-0.016190
S.E. of regression	1.390208
F-statistic	0.484872
Prob(F-statistic)	0.693599

Table 4. t test (partial influence)

Dependent Variable: Y				
Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	3.071421	0.517705	5.932760	0.0000
X1	0.007976	0.004290	1.859142	0.0662
X2	-0.000161	3.79E-05	-4.239787	0.0001
X3	-0.000689	0.001078	-0.639118	0.5243
Z	-0.118378	0.125030	-0.946796	0.3462

Based on Table 5, Prob value. 0.000853, then the hypothesis 9 is accepted, meaning that the variables capital adequacy ratio, operating expenses to operating revenues, net operating margin and non-performing financing jointly influence return on assets in sharia public bank. In calculating the R Square it is based on the table 5, it can be explained that capital adequacy ratio, operating expenses to operating revenues, net operating margin and non-performing financing jointly influence return on assets. This can be seen from the Adjusted R-squared value of 0.1462 or 14%. It can be concluded that the 10th hypothesis is accepted.

Intervening versus independent variables and Independent variable for intervening

Uji Sobel

$$t = \frac{ab}{\sqrt{(b^2SEa^2) + (a^2SEb^2)}}$$

Information: a (Path of the independent variable towards the intervening variable); b (Path of the intervening variable to the dependent variable); SE (Standar error).

Based on the calculations conducted on the capital adequacy ratio (CAR) against return on assets (ROA) through non-performing financing (NPF), the t-value obtained is 0 < 1.985 (t-table), which means that the capital adequacy ratio has no effect on return on assets through non-performing financing. Then, based on the calculations conducted on operating expenses to operating income (OEOI) against return on assets through non-performing financing, the t-value obtained is 0.88 < 1.985 (t-table), which means that operating expenses to operating income has no effect on return on assets through non-performing financing. Lastly, for the net operating margin (NOM) against return on assets through non-performing financing, the t-value obtained is 0.88 < 1.985 (t-table), meaning that the net operating margin also has no effect on return on assets through non-performing financing.

Based on the results shown in Table 2, it can be explained that the Capital Adequacy Ratio has a value of 0.3493, which is greater than 0.05, thus it can be concluded that the capital adequacy ratio has no effect on non-performing financing. The results of this test are contradictory to Hernawati et al. (2021); Priyadi et al. (2021) which states that the capital adequacy ratio has an effect on non-performing financing. Capital is an important factor for banks in developing their business and accommodating the risk of loss. Basically, the capital owned by a bank must be sufficient to cover all business risks faced by the bank. Bank capital is represented by the capital adequacy ratio (CAR). The capital adequacy ratio shows how much of all bank assets contain risk, which is financed from its own capital. Meanwhile, non-performing financing (NPF) is a comparison between the total problematic financing and the total financing provided to debtors. Non-performing financing (NPF) shows how much collectibility the bank has in collecting back the financing that has been disbursed. If problematic financing exceeds the limit, it will become a serious problem that will disrupt the profitability of the Islamic bank, leading to the cessation of operations. Bank Indonesia sets Gross non-performing financing at 5% as a tolerance figure for the health of a bank.

Table 5. F test (Simultaneous influence)

R-squared	0.181471
Adjusted R-squared	0.146265
S.E. of regression	2.067581
F-statistic	5.154598
Prob(F-statistic)	0.000853

Based on the results shown in Table 2, it can be explained that the operating expenses to operating income has a value of 0.8121 > 0.05, it can be explained that operating expenses to operating income has no effect on non-performing financing, the results of this test are in line with research results (Jusni et al. 2019). Non-performing financing (NPF) is an indicator in assessing the performance of bank functions, where the bank's function is as an intermediary institution, a high level of non-performing financing indicates low bank health because this indicates that there is a lot of problematic financing in the bank's operational activities. Operating expenses to operating income (OEOI) is an efficiency ratio used to measure bank management's ability to control operational costs relative to operational income.

Based on the results shown in Table 2, it can be explained that the net operating margin has a value of 0.4910 > 0.005, which means that the net operating margin has no effect on non-performing financing. The results of this test are contradictory to (Jusni et al. 2019). Net operating margin (NOM) is one of the instruments used to view and analyze the ratio of bank expertise on how to manage asset funds in order to obtain large profits. Non Performing Financing is one of the instruments used to measure the performance ratio of Islamic banks in terms of customers' inability to repay credit and measure the risk of financing failure.

Based on the results shown in Table 4, it can be explained that the capital adequacy ratio is 0.0662 > 0.05, indicating that the capital adequacy ratio has no effect on return on assets. The results of this test are contradictory to Marsintauli et al. (2023); Apau & Sibindi, (2023); Awwad, (2021); Puspitasari et al. (2021) stated that the capital adequacy ratio (CAR) has a positive effect on return on assets (ROA) and is in line with research results Ali et al. (2023); Sugiono et al. (2023); Saleh & Paz, (2023); Widarjono, (2018), namely that it has no effect on Return on Assets (ROA).

The capital adequacy ratio is a ratio that shows the extent to which all bank assets containing risk (credit/financing, investments, securities, claims on other banks) are financed from the bank's own capital funds, in addition to obtaining funds from sources outside the bank such as public funds, bank loan funds (debt) (Gharaibeh, 2023).

Return on assets is a comparison between the bank's net profit and its own capital. This ratio is used to measure the performance of bank management in managing available capital to generate profits after tax. Return on assets shows the ability of bank management to generate profits from managing the assets owned (Herciu & Șerban, 2018).

Based on the results shown in Table 4, it can be explained that operating expenses to operating income is 0.0001<0.05, indicating that operating expenses to operating income (OEOI) has an effect on return on assets. The results of this test are in line with Ali et al. (2023); Herciu & Șerban, (2018) Islam & Rana, (2017); Widarjono, (2018); Puspitasari et al. (2021); Karamoy & Tulung, (2020) states that rating expenses for operating income (OEOI) has a positive effect on Return on Assets (ROA) and is in contrast to Ali et al. (2023); Herciu & Șerban, (2018) stated that it has no influence on return on assets (ROA). Operational costs and operational income are one of the instruments used to measure the ratio between operational costs and operational income of an agency in each period. Return on assets shows the ability of bank management to generate profits from managing the assets owned. In determining the health level of a bank, Bank Indonesia places more importance on assessing the amount of return on assets and does not include the element of return on assets. This is because Bank Indonesia, as a supervisor and supervisor of banking, prioritizes the value of a bank's profitability as measured by assets whose funds are mostly from public savings.

Based on the results shown in Table 4, it can be explained that the net operating margin is 0.5243 > 0.05, this explains that the net operating margin has no effect on return on assets, the results of this test are contradictory to Aysen Doyran, (2013); Puspitasari et al. (2021); Karamoy & Tulung, (2020) states that net operating margin (NOM) has a positive effect on Return on Assets (ROA), whereas according to Said & Ali, (2016) it has no effect on Return on Assets. Net operating margin (NOM) is a ratio used to measure bank management's ability to manage its productive assets to generate net interest income. Net interest income is obtained from interest income minus interest

expenses (Widarjono, 2018). Increasing or decreasing return on assets is not a net operating problem that is the main problem.

Based on the results shown in Table 4, it can be explained that non-performing financing has a probability value of 0.3462 > 0.05, this shows that non-performing financing has no effect on return on assets, the results of this test are contradictory to Islam & Rana, (2017); Priyadi et al. (2021) non-performing financing (NPF) influences return on assets and is in line with research results Ali et al. (2023); Widarjono, (2018) which states that it has no influence on return on assets. non-performing financing is an indicator in assessing the performance of bank functions, where the bank's function is as an intermediary institution. A high level of non-performing financing indicates low bank health because this indicates that there is a lot of problematic financing in the bank's operational activities. The bank has a procedure that if problematic financing increases, the distribution of financing will be stopped until the problem of bad financing has been resolved properly so that it does not cause new problems that cause a decrease in bank income.

Based on the Sobel tests that have been carried out, it can be concluded that non-performing financing is unable to mediate the effect of the capital adequacy ratio on return on assets. Non-performing is problematic financing, if problematic financing increases then banks tend to stop distributing financing to customers. It is a capital adequacy ratio that measures capital adequacy which functions to accommodate the risk of loss that a bank may face. The higher the capital adequacy ratio, the better the bank's ability to bear the risk of any risky credit/productive activities. So that bank performance can be maintained well.

Based on the Sobel tests that have been carried out, it can be concluded that non-performing financing is unable to mediate the effect of operational costs on operating income (OEOI) on return on assets. Increases or decreases in financing problems are not the main factor in improving bank performance. This is controlled by the ratio which is used to measure a bank's performance when generating profits. The smaller the value of operational costs in relation to operational income, the more efficient the bank is in carrying out its activities.

Based on the Sobel tests that have been carried out, it can be concluded that non-performing financing is unable to mediate the effect of net operating margin on return on assets. Net operating margin is a ratio used to measure bank management's ability to manage its productive activities to generate profit sharing income. Profit sharing income is obtained from operating income minus profit sharing funds minus operational costs, so that problematic financing is not able to cause new problems that have an impact on return on assets, which is a ratio that measures bank profits.

Managerial Implications

The implications for Islamic Commercial Banks in Indonesia are that bank management should enhance the quality of their productive asset management to generate higher net interest income, thereby effectively handling financing. Effective asset management strategies can be developed to maximize the utilization of capital for higher returns. Additionally, the ratio of operating expenses to operating income (OEOI), which compares total operating expenses to total operating income, is crucial. This study highlights the importance of managing operating expenses relative to operating income (OEOI).

Banks should focus on improving operational efficiency to enhance profitability. This can involve the adoption of cost-effective technologies, process simplification, and service enhancement to reduce operational risks. The relationship between Non-Performing Financing (NPF) and profitability underscores the need for strong risk management practices. Banks should strengthen their credit assessment processes and monitoring systems to minimize the occurrence of non-performing loans, which directly impact profitability. Given that Net Operating Margin (NOM) positively influences Return on Assets (ROA), banks should continue to focus on increasing NOM by optimizing income from productive assets. This could involve diversifying income sources and focusing on high-yield investments that comply with Sharia principles.

For regulators like the Otoritas Jasa Keuangan (OJK) in Indonesia, these findings emphasize the importance of monitoring NPF levels to ensure the stability and health of the banking sector. Policymakers may consider implementing stricter guidelines or support systems to help banks effectively manage their NPFs. The implications for Islamic banking are particularly

significant due to its unique characteristics, such as the absence of interest. The importance of NOM and its impact on profitability are highlighted, and Islamic banks must continue to innovate within the framework of Sharia compliance to enhance profitability while effectively managing risk.

CONCLUSIONS AND RECOMENDATIONS

Conclusions

In order to increase bank profits, management needs to make changes and efforts to advance the company. Besides that, there are many indications that influence improving bank business and performance. Based on the background, testing and discussion, it can be concluded that the capital adequacy ratio, operating expenses to operating income and net operating margin have no influence on non-performing financing, then the capital adequacy ratio, net operating margin and non-performing financing have no influence on returns on assets, while operating expenses to operating income have an influence on return on assets. An indirect influence can be conveyed that non-performing financing is unable to mediate the capital adequacy ratio, operating expenses to operating income, net operating margin to return on assets. This research can be used as a guide for assessing business performance through the factors that influence it.

Recomendations

Apart from exploring the relationship between bank performance as proxied by return on assets as the dependent variable, capital adequacy ratio, operational costs to operating income and net operating margin as independent variables and non-performing financing as an intervening variable, future research can test how factors such as technological innovation, social responsibility, and the influence of supply chain management on financial performance affect Sharia Banks. These areas can offer valuable insights into the performance of Islamic Banking in developing countries.

Given the importance of macroeconomic conditions on bank performance, future researchers may consider examining the impact of macroeconomic variables such as inflation, economic growth, or exchange rates on the performance of Islamic banks. This would provide a more comprehensive view of the factors influencing bank profitability. In addition to quantitative analysis, future researchers could complement this study with qualitative analysis. Interviews with bank managers, regulators, or Islamic finance experts could offer deeper insights into risk management practices and operational strategies used in the Islamic banking industry. By taking these suggestions into account, future research is expected to contribute more comprehensively and deeply to the literature on the financial performance of Islamic banks.

FUNDING STATEMENT: This research did not receive any specific grant from public, commercial, or not-for-profit funding agencies.

CONFLICTS OF INTEREST: The author declares no conflict of interest.

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