

CHAPTER I

INTRODUCTION

1.1 Background of the Study

The establishment of Indonesia's Shariah banking system dates back to 1992, following the enactment of the government's regulatory framework under Law No. 7 of 1992 concerning the Banking System. This pivotal law facilitated the operation of Bank Muamalat, the first Islamic bank in Indonesia, which marked the beginning of Islamic banking in the country. However, it was not until 1998 that a broader banking regulation was introduced, allowing the simultaneous operation of both conventional and Islamic banking systems in the country. This shift opened the door for the inclusion of Islamic finance as an alternative to conventional banking, aligning with the growing interest in Shariah-compliant financial services among Indonesia's predominantly Muslim population.

In 1999, the government made a strategic move to further promote the development of Islamic banking by establishing Bank Syariah Mandiri, which was positioned as a subsidiary of the state-owned Bank Mandiri. This marked a significant milestone in the Indonesian financial landscape. Subsequently, other Islamic banks were formed, including BRI Syariah, BNI Syariah, Bank Mega Syariah, and BCA Syariah, representing a combination of both state-owned and private institutions offering Shariah-compliant banking services. These institutions operate primarily in two forms: Shariah Commercial Banks (which provide full-fledged Shariah-compliant banking services) and Shariah Units or Islamic Windows (which are

conventional banks offering Islamic banking products alongside their regular services).

Over the years, Islamic banking has played an increasingly important role in the broader development of the Islamic financial ecosystem in Indonesia. This ecosystem encompasses various segments, such as Islamic insurance (Takaful), non-banking financial institutions, Sukuk (Islamic bonds), Islamic mutual funds, Bancassurance, Shariah-compliant bonds, and venture capital. The integration of these sectors has led to the creation of a robust Islamic Economic Industry that supports Indonesia's economic growth. This is particularly significant given Indonesia's demographic profile, as it has one of the largest Muslim populations globally, making it a key market for the expansion of Islamic finance.

By 2020, nearly three decades after the first regulatory framework was introduced, Islamic banking in Indonesia had undergone substantial growth. The industry had expanded its reach across the nation, with 14 Shariah Commercial Banks, 20 Shariah Units/Islamic Windows, and over 3,000 service outlets. The total assets held by these institutions exceeded IDR 608.90 trillion, contributing more than IDR 1,802.86 trillion to Indonesia's broader Islamic financial sector, which is valued at approximately USD 127.82 billion. These figures indicate the growing significance of Islamic finance in the country's banking sector.

The following table outlines key indicators of the Shariah banking industry's performance as of December 2020:

Tabel 1 1. Syariah Banking Industry Statistic December 2020 (Source: Otoritas Jasa Keuangan)(Bersama, 2021)

Industry	Institution	Outlet	Asset <i>Trillion IDR</i>	Financing <i>Trillion IDR</i>	Funding <i>Trillion IDR</i>
Syariah Commercial Bank	14	2.034	397,07	246,53	322,85
Syariah Unit/Islamic Window	20	392	196,88	137,41	143,12
Syariah Rural Bank	163	627	14,95	10,68	9,42
Total	197	3.053	608,90	394,63	475,79

Additionally, the following figures illustrate the growth of the Syariah banking industry in terms of key financial indicators—assets, financing, and funding—from 2015 to 2020. This data highlights the steady annual growth of the sector and demonstrates that Islamic banking is increasingly viewed as a viable alternative to conventional banking services by the broader Indonesian society.

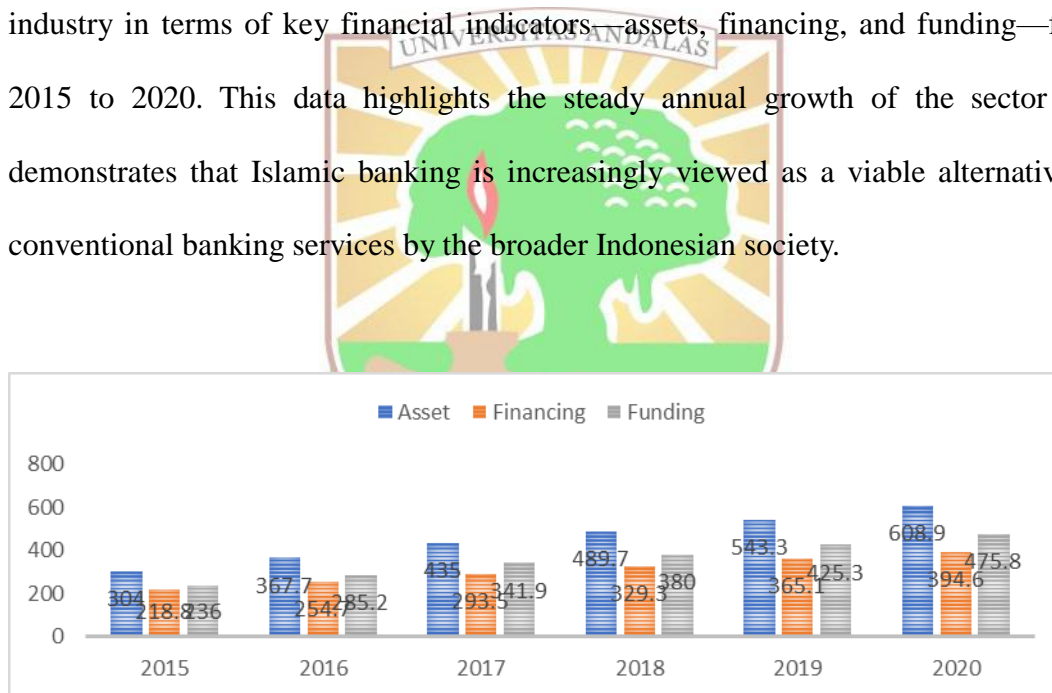


Figure 1 1 Syariah Banking Industry growth Statistic 2015- 2020 (Source: Otoritas Jasa Keuangan)(OJK, 2022)

Despite the impressive growth of Islamic banks in Indonesia, this progress has not been fully mirrored by an increase in market share. The market share of Islamic banking, while growing, remains relatively small compared to conventional banking, reflecting the challenges Islamic banks face in penetrating the broader banking

market. As of 2020, the market share of Shariah-compliant banking in the country was approximately **6.51%**, while conventional banks maintained a much larger share.

The following table presents the market share data for Islamic banking in Indonesia:

Tabel 1 2 Syariah Banking Industry Statistic December 2020 (Source: Otoritas Jasa Keuangan)(Bersama, 2021)

Industry	Asset <i>Trillion IDR</i>	Market Share
Syariah Commercial Bank, Syariah Unit/Islamic Window and Syariah Rural Bank	608,90	6,51 %
Coventional Commercial Bank, Syariah Banking and Rural Bank	9.347,94	

In an effort to address these disparities and strengthen the overall banking sector, the Otoritas Jasa Keuangan (OJK) introduced POJK No. 12/POJK.03/2020, which is focused on the consolidation of commercial banks. This regulatory policy was designed to encourage banks to increase capital and consolidate in order to enhance their competitiveness, efficiency, and organizational capacity. Through such consolidation, the banking sector's resilience and ability to withstand economic pressures would be improved, ultimately contributing to greater national economic stability. Additionally, this policy aims to drive improvements in operational efficiency through economies of scale, which is particularly crucial in a rapidly evolving financial landscape (Bersama, 2021)

Further strengthening of the Shariah banking sector was also pursued by the Indonesian government, through the Ministry of State-Owned Enterprises, by

implementing regulations such as Perppu No. 1/2020 and POJK No. 18/POJK.03/2020. These regulations facilitated the merger of three prominent state-owned Shariah banks—Bank Syariah Mandiri, Bank BNI Syariah, and Bank BRI Syariah—into a single institution: Bank Syariah Indonesia (BSI), which officially launched in February 2021.

The financial highlights of the three merged banks prior to consolidation in January 2021 are as follows:

Tabel 1 3 Financial Highlight before merger of BSM, BNIS, and BRI Syariah (Source: Otoritas Jasa Keuangan 2022)(OJK, 2022)

Entity	Asset <i>In Million</i>	Equity <i>In Million</i>	Net Profit <i>In Million</i>
Bank Syariah Mandiri	112.291.867	9.245.835	1.275.034
Bank BNI Syariah	49.980.235	4.735.076	603.153
Bank BRI Syariah	43.123.488	5.088.036	74.016
Total	205.395.590	19.068.947	1.952.203

This merger consolidates three major players in the Indonesian Islamic banking industry and creates a more powerful, competitive entity with a combined asset value of IDR 205 trillion. The new institution, Bank Syariah Indonesia (BSI), commands approximately 51.72% of the commercial Shariah banking market share. This consolidation is expected to result in a stronger financial entity capable of enhancing Indonesia's presence on the global stage as a reputable player in the Shariah-compliant financial sector.

However, this transformation is not without challenges. The consolidation of these three institutions is likely to reshape the competitive landscape within

Indonesia's Islamic banking sector, with significant implications for market efficiency, competition, and the overall market influence of Islamic banks. While BSI is poised to become a dominant force, the remaining 11 Shariah banking institutions will now compete for a smaller share of the market. The increased concentration in the sector could also lead to strategic shifts among market leaders, as they adapt to the changing competitive environment.


This study aims to explore the impact of the merger of state-owned Islamic enterprises on the competition within the Shariah banking industry in Indonesia. It seeks to understand how the consolidation policy has altered the competitive dynamics in the market, and what effect it has had on other participants in the industry. The research also aims to examine how government policies, such as this merger, influence market structure and competition, which remains a relatively under-explored area in existing literature.

Current studies primarily focus on areas such as Market Concentration (Fatwa, 2024), Enhance Efficiency and Income from Financing Product (Hijriah, Amanah ; Rusmita, 2024), Employee Performance (Harahap et al., 2024), Economic Development (Dinda Kusumaningrum et al., 2023) global competitiveness (Atikah et al., 2021), and critical from organization perspective (Kusuma, 2024). This study contributes to the literature by providing insights into the policy's effects on market structure and its broader implications for the competitive landscape in Indonesia's Islamic banking sector.

Based on this background, the researcher is interested in conducting a study titled **'The Impact of the Islamic Banking Merger on Competition in the Indonesian Islamic Banking Industry.'**

1.2 Problem Statement

This study tries to analyze the influence of the merger policy to the whole Islamic banking industry in Indonesia, the purposed of this study was to address the following question:

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- The logo of Universitas Andalas is a shield-shaped emblem. At the top, a banner reads "UNIVERSITAS ANDALAS". The central part of the shield features a green tree with a red flame-like shape at its base. Below the tree, a banner reads "UNTUK KEDJAJAAN BANGSA".
1. How do changes in market competition following merger events affect the profitability of the Islamic banking industry?
 2. How do changes in market concentration resulting from mergers influence the profitability of the Islamic banking industry?
 3. How do changes in Financing To Deposit (FDR) ratio after mergers impact the profitability of the Islamic banking industry?
 4. How do changes in the Bank Operating Expense Ratio (OER) ratio after mergers affect the profitability of the Islamic banking industry?

1.3 Research Objective

The research questions addressed in this study are:

1. To examine the impact of changes in market competition following merger events on the profitability of the Islamic banking industry.

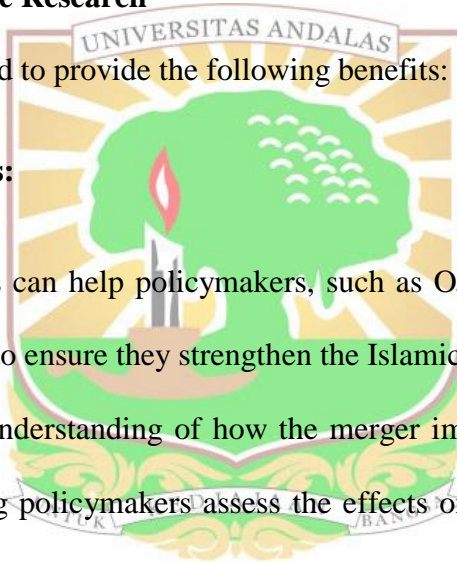
2. To assess the effect of changes in market concentration resulting from mergers on the profitability of the Islamic banking industry.
3. To analyze the impact of post-merger changes in Financing To Deposit (FDR) ratio on the profitability of the Islamic banking industry.
4. To evaluate the effect of post-merger changes in the OER ratio on the profitability of the Islamic banking industry.

1.4 Contribution of The Research

This research is expected to provide the following benefits:

1.4.1 For Policymakers:

1. The study's findings can help policymakers, such as OJK, evaluate and improve the merger policies to ensure they strengthen the Islamic banking sector.
2. It will provide an understanding of how the merger impacts different players in the industry, helping policymakers assess the effects on competition and market stability.
3. The research can highlight areas where regulations may need to be adjusted to keep the sector competitive and resilient.
4. It may also guide future policies to encourage growth and innovation in the Islamic banking sector.



1.4.2 For Stakeholders

1. The study will serve as a reference for future research on Islamic banking mergers, helping other researchers and practitioners.
2. It will offer insights into the challenges and opportunities within the Islamic banking industry, improving understanding of market dynamics.

1.5 Scope of the research

The research focuses on the merger of three state-owned Islamic banks—Bank Syariah Mandiri, BRI Syariah, and BNI Syariah—in 2022, using data from Otoritas Jasa Keuangan and company financial reports from 2021 to 2023.

This research aims to examine the impact of the merger on other players in the industry. The main indicators used in this study are total assets, financing, and profit margin.

1.6 Outline of the research

To provide a clear understanding of this study, the material is organized into several sub-chapters, presented in a systematic manner as follows:

CHAPTER I: INTRODUCTION

This chapter introduces the background of the study, problem formulation, research objectives, research benefits, scope, and the structure of the research.

CHAPTER II: LITERATURE REVIEW

This chapter presents the theoretical framework, including definitions and concepts related to the research topic, types of research, types and sources of data, data collection techniques, research population and samples, operational definitions, measurement of variables, and the data analysis methods used to test the hypotheses.

CHAPTER III: RESEARCH METHODS

This chapter outlines the research design, research objects and locations, population and sample, sampling techniques, data sources, data collection methods, data processing, research variables, variable measurements, and data analysis techniques.

CHAPTER IV: RESULTS AND DISCUSSION

This chapter presents the analysis and discussion of the research findings, comparing the results with the theoretical framework discussed in Chapter II.

CHAPTER V: CONCLUSION

This chapter provides the conclusions based on the research findings, discusses research limitations, and offers recommendations for further research.

