Effects of Risk and Sharia Compliance on Mudarabah Financing at Islamic Banks in Indonesia

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Abstract

Mudarabah financing is an ideal product of Islamic banks, therefore it should have a larger portfolio compared to other contracts. Data during the study period since 2011-2018 shows the opposite fact. The average mudarabah financing portfolio is only 2.42% compared to other contracts with a level of non-performing financing of 12.31%, and yet the level of sharia compliance reaches 84%. This study analyzes mudarabah financing from the perspective of sharia compliance and risk level considering both are important indicators of sharia bank performance. The analyzed data came in the form of secondary data from publication reports and primary data obtained through questionnaires and interviews. With the analysis method in the form of Structural Equation Model (SEM) with analysis units of 24 BPRS from 58 BPRS all over Indonesia that distribute mudarabah financing and 244 respondents consisting of owners, commissioners, directors, sharia supervisors and customers. The analysis shows that mudarabah financing is very low as a result of the high risk it possesses. While sharia compliance is a driving factor in increasing mudarabah financing. Another finding is that the success of the BPRS in channeling mudarabah financing is due to its ability to prepare specific human resources that manage mudarabah financing, market segmentation, ongoing assistance to educate mudarib responsibilities, as well as routine supervision to ensure financing runs according to the contract.

Keywords: mudarabah, risk, non-performing financing, sharia compliance

1.Background

Profit sharing system is an ideal product of Islamic banks, both in terms of fund raising and distribution in addition to other derivative products (Aziz et al. 2013). Profit sharing is a core product and also a fundamental differentiator with conventional financial systems, so that in the initial phase of its establishment, Islamic banks are more popular as profit sharing banks (Antonio, 2001). Profit sharing system or better known as mudarabah and musharaka allows economic actors who do not have material capital to start a business. This is due to mudarabah being a partnership or partnership that is mutually beneficial to both parties (Zuhaili, 2011). In addition, mudarabah provides open space for business growth and development in large, medium, and small scale (Suhendri et al. 2017).

In accordance with its definition that in mudarabah, business capital is fully provided by the owner of the fund or *sahibul mal*, while the ability and willingness to try by the entrepreneur or *mudarib* is sufficient (Hassan, 2009). This kind of mudarabah practice was once carried out by Muhammad and Khadijah through a mutually beneficial partnership mechanism (Udovitch, 2008).

The mudarabah system opene up business opportunities for those who do not have the financial capital. In this system, the capital owner hands over a certain amount of money to the individual who will run a business with the profit being shared between them (AAOIFI, 2015, and Zuhaili, 2011). A similar understanding was put forward by Sabik (1987), that mudarabah occurs when a malik or capital owner surrenders his capital to amil to trade with the capital, where profits are shared between the two with the portion according to the requirements of the contract.

The Indonesian Ulama Council or Majelis Ulama Indonesia (MUI) through the National Sharia Council or Dewan Syariah Nasional (DSN) provides a mudarabah fatwa stating that Sharia Financial Institutions as *sahibul mal* must provide 100% of the needs of a project, while entrepreneurs or *mudarib* act as managers (DSN MUI, 2000). From this definition, the profit sharing system is considered very relevant in business development. Entrepreneurs will have a chance to receive financing without having to provide their own capital (Ackerman, 2013).

As an ideal product, the practice of profit sharing systems still faces various obstacles, such as low entrepreneurial moral standards, the ineffectiveness of financing models for modern business needs, the character of entrepreneurs who do not want to be monitored, the high level of risk, and the complexity of financing administration (Mithcell, 2004). These constraints cause mudarabah financing to less develop compared to other contracts. The following is the development of financing Indonesian Sharia BPR since 2011-2018.

Table 1
Mudarabah Financing 2011-2018

Contract	2011	2012	2013	2014	2015 (Rp.000.000)	2016	2017	2018	Total	%
Murabahah	1,955,532	2,554,774	3,325,460	3,406,902	4,272,107	4,870,453	5,642,734	6,167,210	32,195,171	76.94%
Salam	20	197	-	20	15	14	-	-	266	0.00%
Istisna	23,673	20,780	17,614	12,881	10,631	4,657	21,426	35,394	147,055	0.35%
Qard	85,271	68,792	94,100	96,453	116,669	137,856	180,735	140,221	920,096	2.20%
Multijasa	136,570	91,975	245,184	228,153	312,872	515,041	684,753	840,300	3,054,849	7.30%
Mudarabah	70,124	73,026	113,763	123,449	186,724	154,779	121,505	168,621	1,011,991	2.42%
Musyarakah	224,755	307,330	417,438	543,576	615,257	728,467	750,660	813,455	4,400,938	10.52%
Ijaroh	10,053	8,258	8,201	3,759	32,438	7,127	8,582	33,130	111,549	0.27%
Total	2,505,997	3,125,133	4,221,760	4,415,193	5,546,712	6,418,395	7,410,395	8,198,331	41,841,917	100.00%

Source: Bank Indonesia (2018)

From the table of financing development presented in Table 1, it is evident that as an ideal product, mudarabah financing portfolio is still very low compared to other contracts, with the number being only 2.42%. In addition, the level of non-performing financing mudarabah financing is very high at 12.31% (Financial Services Authority, 2018).

One important factor that hinders the profit sharing agreement, especially mudarabah, to run smoothly is the asymmetric information (Balwin, 2000). Asymmetric information is a situation that shows that some investors have the necessary information and some others do not (Jogiyanto, 2000). The relationship between asymmetric information and investment opportunities has been investigated by Ross (1977), Harris and Raviv (1990) using the agency model. The results of both studies indicate a relationship between asymmetric information and investment models with a probability limit for investment opportunities. This means that asymmetric information affects the size of the investment income being carried out. Asymmetric forms of information are usually in the form of moral hazard and adverse selection (Iqbal, 2000).

These conditions result in the emergence of financing risk and profit sharing systems to have a higher level of risk than other contracts (Ahmed, 2012). Financing risk is a major risk and has a direct impact on the survival of Islamic banks (Ismal, 2010). One form of financing risk is the occurrence of non-performing financing (NPF) and the high NPF condition indicates the high risk of the financing system (Handayani, 2017). These various reasons cause mudarabah financing in BPR Syariah to fail in showing significant growth. Data from the OJK (2018), the average mudarabah financing in BPRS compared to other contracts during 2011-2018 was only 2.42% with an NPF rate of 12.31%.

Therefore, Islamic banks need to strengthen their risk management system to ensure financial stability (Sriyana, 2015), and increase sharia compliance, because sharia compliance is an important part of risk management (Ismal, 2010) as well as a preventive effort to increase public confidence in sharia financial institutions (Khan and Ahmed, 2001). National sharia compliance standards refer to the fatwa of the National Sharia Council of the Indonesian Ulama Council or Dewan Syariah Nasional Majelis Ulama Indonesia (DSN MU) and internationally refer to the Islamic Financial Services Board (IFSC) provisions.

To ensure that policies, procedures, products, and services are in accordance with and subject to sharia provisions, sharia bank has an organizational structure that has a special authority for sharia supervision (Iqbal and Mirakhor, 2008). The sharia supervision model in Indonesia is carried out by the Sharia Supervisory Board or Dewan Pengawas Syariah (DPS). DPS is a part of MUI DSN that is placed in every Islamic bank, including BPRS. Its main task is to ensure that the Islamic bank meets the provisions and fatwas of the DSN (DSN, 2003).

Data during the study period from 2011-2018 shows the fact that the average mudarabah financing portfolio is only 2.86% compared to other contracts with a level of non-performing financing of 10.66% (Financial Services Authority, 2016). The above condition shows that the performance of mudarabah financing is contrary to the ideal conditions that should occur in Islamic banks. This study analyzes mudarabah financing from the perspective of risk and sharia compliance.

2. Literature Review

2.1. Mudarabah

In *hasanah fiqh muamalat* and the theory of Islamic civilization, the mudarabah system is the oldest and most popular form of cooperation among the Arabs, both before Muhammad's prophethood and afterward (Sabiq, 1987). In the Middle Ages, cooperation (*syirkah*) and *commenda* (the term for *mabahabah*, *muqaradhah* and *qiradh*), which from now will continue to be used with the term mudarabah to represent all of them is the most important means in society, as it uses financial and human resources as well as to fulfill the trade objectives (Udovitch, 2008).

In terms of language (*lughawi*), Mudarabah comes from the word *dharb*, which has various meanings depending on the context of the sentence. The meanings of *dharb* includes hitting (*dharaba Ahmad al kab*), ticking (*dharaba al kalbu*), joining (*dharaba fi al amr*), avoiding (*dharaba 'an al amr*), mixing (*dharaba al laun ila al laun*) and walking (*dharab al fi al ard*) (Zuhaili, 2011). Etymologically the word mudarabah which comes from the word *adh dharb* has two relevance among the people, namely the first; those who do business are likened to people who walk on earth (*yadhribu fil ardhi*), to trade / do business therefore are entitled to benefit from the results of their efforts. As the word of Allah SWT in the Qur'an: "... and some people who walk on the face of the earth are looking for the gift of God (*QS. Al Mujamil*-20). Secondly, because people who are members of the *yadhribu bisahmin* (cut / take) part of the profits (Zuhaili, 2011).

In terms of understanding, mudarabah has been developed by the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI, 2015), "Mudarabah is a partnership in profit where one party provides capital (*rab al mal*) and the other party provides labor (*mudarib*)". A more operational understanding of mudarabah is contained in the DSN-MUI fatwa which states that mudarabah is a business cooperation agreement between two parties where the first party (*malik*, *shahib al mal*, *LKS*) provides all capital, while the second party (*amil, mudarib,* customer), act as manager and business profits are shared between them in accordance with the agreement set forth in the contract (DSN, 2000). Although the term mudarabah is not clearly mentioned in the Qur'an, the means of trade are widely mentioned in various narrations which show the habits of the Prophet PBUH and his close friends in carrying out mudarabah. According to a story, in the early days of Muhammad, he was an agent in a trade agreement with Khadijah who later became his wife (Sarakhsi in Udovitch, 2008).

From Ibn Abbas it was explained that, "If Abbas bin Abdul Munthalib gave up his mudarabah property, he requsted the mudarib to not use it to sail the ocean, go down the valley, nor to buy livestock. If the request is violated, then the mudarib must bear the risk. When these requests were heard by Rasulullah PBUH, he confirmed it. (HR. Ad Daruqutni, number 3033, Sunan ad Daruqutni).

2.2. Sharia Compliance

Sharia compliance is the compliance of Islamic banks to Islamic law and its derivative rules. According to Ali (2013), sharia compliance means, "adherence and confirmation with the sharia principles in the context of Islamic financial transactions, this means that all financial and rules of commercial transactions (*ahkam fiqh al muamalat*). These laws and rulles on the other hand are derived and deduced from the primary sources of the sharia (that are divine in origin), injunctions of the Qur'an and directives and practices of the Prophet pbuh, normally refered to the sunnah, as well as the secondary sources of sharia that are basse on human interpretation and seasoning, whether at the strongest level of *ijma* (consensus of all jurists) or in the form of *qiyas, istihsan, istishab istihsan* etc ".

To measure the extent to which financial business practices are in accordance with and compliant to sharia principles, sharia compliance parameters need to be formulated. In this study, the parameters adopted using the maqashid sharia approach, the covenant approach, the financial documentation approach, and the legal document approach (Rosly, 2011).

In the discipline of *ushul fiqh*, *maqashid sharia* occupies its own urgency compared to other disciplines. Muslim scientists must master the Islamic maqasid in their jihad to respond to global and regional economic developments. It can be concluded that *maqshid sharia* is the most important core of the science of *ushul fiqh* occupies the highest position compared to the provisions of Islamic texts if the text stands alone and is partial (Auda in Al Ghazali, 2008).

Efforts to *ijtihad* in the complexity and dynamization of contemporary economics require a deep understanding of *sharia maqashid*. The understanding of *sharia maqashid* cannot stand alone but must start from mastership and good understanding of various interdisciplinary disciplines, such as Islamic legal philosophy, *tarikh tasyri'*, *ulumul qur'an*, *ulumul hadith, qawaid fiqiyah* and other sciences related to the field of *ijtihad*.To ensure that Islamic banks comply with *sharia maqashid*, it is necessary to have more intensive Islamic supervision (DSN, 2000).

2.3. Risk of Financing

Risk is the potential loss due to certain events and the risk of loss is a loss that occurs as a direct or indirect consequence of the event. These losses can be financial or non-financial (PBI, 2011). Khan and Ahmed (2001), define it with, "risk can be defined as the variability or volatility of unexpected outcomes".

While financing risk is the risk arising from the failure of customers or other parties to meet their obligations to the banks in accordance with the previously approved agreements (PBI, 2011). Financing risks are the main groups of risk faced by banks, including Islamic banking. What is meant by customer failure in this case includes intentional failure triggered by character factors and failure due to bankrupt businesses, and so the customer fails to return the financing in accordance with the mutual agreement (Preda, 2015).

In sharia perspective, financing risk can also be influenced by the financing agreement used (Preda, 2015). In murabahah financing contracts, the cause of the bottleneck is due to bank errors in assessing prospective borrowers and lack of monitoring, while in mudarabah agreements, bottlenecks are caused by incomplete information, debtors' lack of transparency, difficulty in seeing the debtor's business, and limited information about the debtor's business productivity as well as the presence of moral hazard (Edwin,

M. and Wiliasih R., (2007).

Problematic financing or non-performing financing (NPF) is the impact of the occurrence of financing risks which also have an impact on reputation risk. Financing risk is a major factor that can lead to other risks (Enrisman, 2015). Therefore Islamic banks must be able to control these financing risks. An important indicator of the risk of financing is measured by the level of collectability of financing or the level of problem financing which is classified into four namely; smoothly, substandard, doubtful, and freeze (Arifin, 2002).

3. Research Methods

This research is intended to prove the influence of mudarabah financing with sharia compliance and risk management, especially financing risks and the internal and external factors. Therefore, this type of research combines qualitative and quantitative research or empirical data analysis as well as theoretical studies.

3.1. Population and Sample

The study population is BPRS in Indonesia, especially those that channel mudarabah financing as many as 58 BPRS (OJK, 2016). While the research sample is 24 BPRS that are willing to be examined. 264 respondents consisted of 144 internal factors, namely owners, commissioners, directors, sharia supervisors and employees as well as 120 mudarabah financing customers.

3.2. Data

This study uses primary data and secondary data sourced from all study samples. Primary data needed in this study include all variables directly related to the research theme which includes management and customer commitment to mudarabah financing while secondary data in the form of BPRS financial reports that have been published by the Financial Services Authority since 2011-2018. Data collection techniques were carried out by filling out questionnaires, and in-depth interviews with structured guidance.

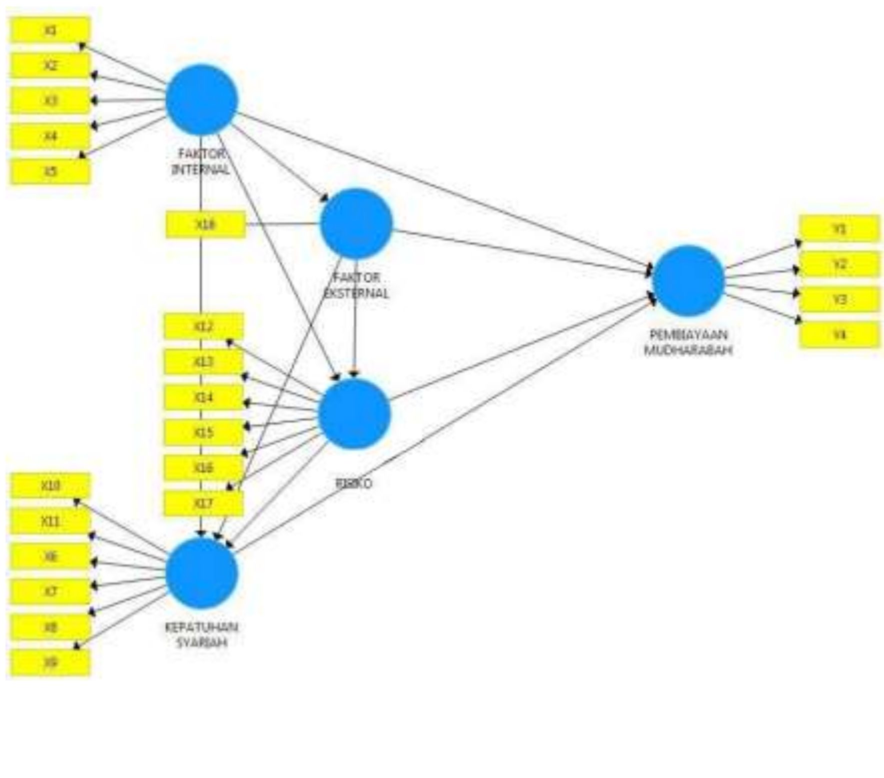
3.3. Analysis Tool

The mudarabah financing model, the influence of internal, external, shariah ompliance and financing risks that are built, will be analyzed using the Structural Equation Modeling (SEM) method, whose model is measured by Second Order Confirmatory Factor Analysis (2ndCFA). The SEM method is used to formulate the causality relationship of a self contained system by including the relevant variables. Based on this perspective, SEM is the best tool to test (confirm or disconfirm) a causal structure based on theory and not to find the relationship between the actual causality structure. The data processing uses the Stastical Product and Service Solution (SPSS) technique, while the existing data is tested using statistical assumptions which include multivariate outliers, normality testsm and multicollinearity tests. The analysis of the data uses qualitative descriptive analysis and quantitative analysis.

The determination of whether the model is correct or not in this study uses several measures, namely average path coefficient (APC), average R-Square (ARS) and average variance inflation factor (AVIF). To get the right model, the APC and ARS test values must be less than 0.05 and the AVIF value as an indicator of multicolonity must be greater than 5. While the hypothesis test in this study uses the PLS method. The argument underlying the use of this PLS is that the PLS method is a powerful method due to it not assuming the data must be of a certain scale size and even a small sample size can also be used to confirm the theory. In addition, PLS can also be used to explain the presence or absence of relationships between latent variables.

Structural equation model or SEM is a multivariate analysis technique that allows researchers to test the relationship between variables that are very complex in order to obtain a comprehensive picture of the model. SEM is also a combination of factor analysis and path analysis into a comprehensive statistical method. In econometrics, SEM is used to describe mathematical models of economic phenomena.

The following is a picture of the path of influence between latent variables with other latent variables and the indicators for each variable;



Picture 1
Correlation Between Variables

The path picture shows the indicators of each latent variable. The mudarabah financing latent variable has four indicators, the sharia compliance latent variable has six indicators, the financing risk latent variable has six indicators, the internal factor has five indicators, the external factor with one indicator and the risk has six indicators, so that all of them have 21 indicators.

3.4. Definition of Variable Operations

Sharia compliance means compliance and conformity to business practices with sharia principles, which in sharia financial business means all financial transactions must comply with and conform to Islamic law (Rosly, 2011). These principles is able to simultaneously prove that Islamic values can be practiced in businesses and is able to maintain and even improve the business continuity of Islamic financial institutions (Ali, 2013). In this study, sharia compliance indicators are measured by *shariah maqashid*, covenant approach, financial documentation approach, and legal documents.

Internal factors are the owners of Islamic banks which are represented by the controlling shareholders or Pemegang Saham Pengendali (PSP) as they greatly influence company policy (Maharaj, 2008). Employee policies that favor employees can increase business productivity. Internal factors discussed by owners or commissioners, directors, sharia supervisors and employees of sharia banks.

External factors are parties outside Islamic banks that have direct relationship with the bank (Shaharudin et al. 2016). The success of mudarabah financing in Islamic banks is greatly influenced by its customers. According to Kasim and Kasri (2011), the return of mudarabah financing is very much determined by the moral hazard and adverse selection of its customers, as Iqbal and Khan (2000) have examined, where the customer greatly influences the return of financing. Analysis of external factors in this study is the customer receiving mudarabah financing.

Risk is the potential loss due to a particular event while the risk of loss is a loss that occurs as a direct or indirect consequence of the event (Bilal, 2013). While financing risk is a potential loss due to failure of customers to meet their obligations, and these conditions might occur during the financing process in which the customer engineers the conditions of his business so that Islamic banks get the wrong data (Bacha, 1997). In this study, financing risk is measured by non-performing financing indicators, principal installment patterns, profit sharing installments, moral hazard, adverse selection, asymmetric information, and financing guarantees.

3.5. Hypothesis test

The decision to reject the null hypothesis (Ho) is made using a hypothesis test based on the statistical probability t, assuming that the residual has a normal distribution. This probability value is also called the ρ (ρ-value) value. Where the probability value ρ illustrates the true significance of level α. In the statistical probability test t or ρ value, it is measured by comparing the probability value ρ with a significant value α. If the probability value ρ is smaller than the selected α, then Ho is rejected and it means accepting the alternative hypothesis (Ha). But if the probability value ρ is greater than α, then Ho is accepted and rejects Ha.

4. Data Analysis and Discussion

The distribution of SRB populations in Indonesia is still concentrated in Java or Western Indonesia in general. Based on regional division based on time, the BPRS that are in the Western Indonesia Time or Waktu Indonesia Barat (WIB) are 148 or equivalent to 89.7%, Central Indonesia Time or Waktu Indonesia Tengah (WITA) are 13 BPRS is equivalent to 9.1% and Eastern Indonesia Time or Waktu Indonesia Timur (WIT) 2 BPRS and equal to 1.2%. Based on the distribution of islands, the dominance of the island of Java is still very large, which is 63.2%, Sumatra 26.3%, Kalimantan 2.5%, Sulawesi 4.9%, Nusa Tenggara / Bali 1.8% and Papua / Maluku amounting to 1.9%.

This population distribution is important to analyze, because respondents with different backgrounds and cultures will have different responses. From the population distribution, the sampling also takes into account the representation of the SRB based on the origin of the archipelago, time, and province and even regencies or cities in Indonesia. Meanwhile the sample is taken at least 30% of the total 58 BPRS or a minimum of 17 BPRS and must represent the spread of all regions of Indonesia. The sample data collected in this study were 24 BPRS or 41.3% far exceeding the minimum sample of 30%, therefore the sample was declared valid. From these data, the unit of analysis in this study is 24 BPRS throughout Indonesia.

The analytical tool used is the Partial Least Square (PLS), which is variance-based SEM, with SmartPLS software 2. The indicator test or also called the Outer model is to test the correlation between the indicator and its construct variable. From this indicator test the output of the validity and reliability of the model is measured by the criteria: Convergent Validity,Discriminant Validity, an Composite Reliability.

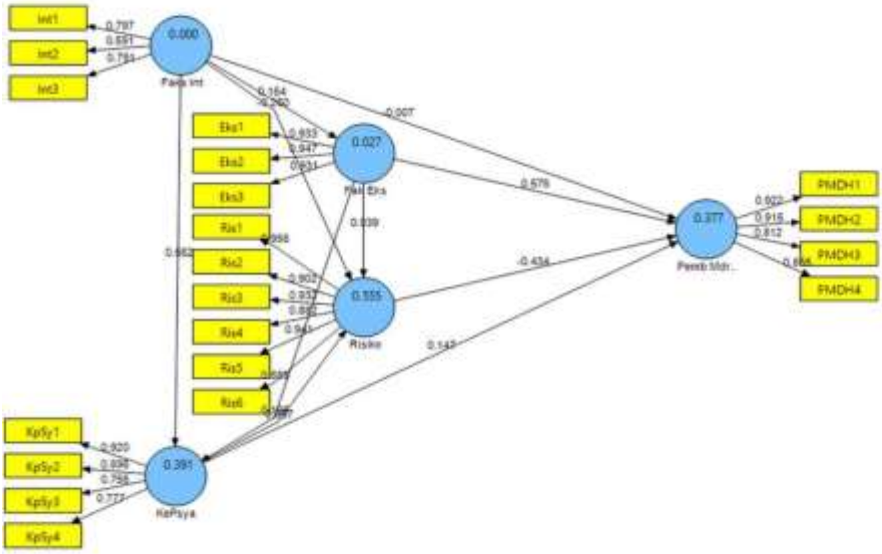


Figure 2
Indicator Test

Information:

Int1: Commitment of the Board of Commissioners
Int2: DPS Commitment
Int3: Board of Directors' Commitments
Int4: Employee Commitment
EX1: Moral Hazard
Eks2: Adverse Sellection
EX3: Guarantee
Ris1: NPF
Ris2: Basic Installment Patterns
Ris3: Basil's Installment Pattern
Ris4: Moral Hazard
Ris5: Adverse Sellection
Ris6: Guaranteed
KpSy1: Maqashid Sharia Approach
KpSy2: Contract Approach
KpSy3: Financial Documentation Approach
KpSy4: Legal Documentation Approach
PMDH1: Number of Submissions
PMDH2: Financing Volume
PMDH3: Outstanding Financing
PMDH4: Number of Customers

From the results of the Convergent Validity above, it is seen that all indicators already have a correlation value above 0.50. This means that all indicators of each latent variable have been declared valid. Discriminant Validity is measured by the cross loading between the indicator and its construct. From the test results it can be concluded that there is no loading factor value for each indicator of each latent variable which has a loading factor value smaller than the loading factor value if it is associated with other latent variables. This means that there are no more latent variables that have poor discriminant validity.

The construct is declared reliable if the composite reliability has a value above 0.70. The Reliability Block Indicator that measures a construct can be evaluated using the output produced by PLS. The test results show that all variables have AVE values> 0.5 and have composite reliability and Cronbachs Alphaberada values above 0.60. All constructs have satisfactory values, ie the value of each variable is above the minimum value except for the internal factor variable. Based on these values it can be said that the consistency and stability of the indicators used meet the standards. Thus, the results of the above analysis can be concluded that the reliability of each variable indicator is met.

Bootstraping model after testing the indicators can be seen in the following figure: (Nama variabel di lingkaran???) Beri tanda signifikansi koefisien...

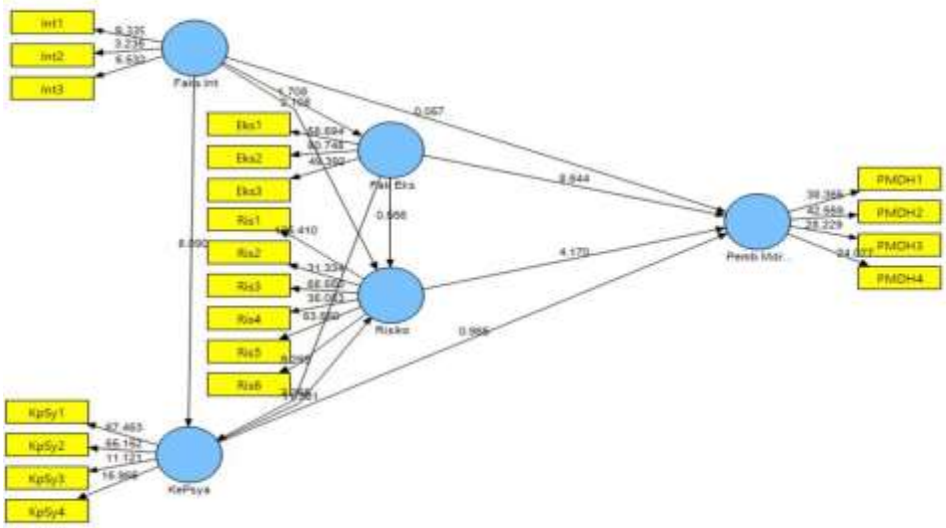


Figure 3
Bootsraping Model

From Figure 4.2 it can be explained that covariable measurement of indicators is influenced by latent constructs or reflects variations from undimensional constructs with several arrows from construct to the indicator. This hypothesized model shows that changes in latent constructs affect changes in indicators. Furthermore hypothesis testing consists of partial and simultaneous testing.

Table 2
Empirical Model Based on SEM Estimation

Variabel	*Original Sample*	*Sample Mean*	*Standard Deviation*	*Standard Error*	*R Square*	*T Statistics*	Description
Eksternal Fact -> Syariah Comp	0,196	0,184	0,083	0,083	0.391	2,355*	Significant
Internal Fact ->Syariah Comp	0,561	0,559	0,069	0,069		8,090*	Significant
Internal Fact-> Eksternal Fact	0,164	0,162	0,096	0,096	0,027	1,708***	Significant
Eksternal Fact -> Mudarabah Fin	0,576	0,573	0,066	0,066		8,644*	Significant
Internal Fact -> Mudarabah Fin	-0,006	-0,011	0,116	0,116	0,377	0,067	Insignificant
Syariah Com -> Mudarabah Fin	0,147	0,168	0,152	0,152		0,965	Insignificant
Risk -> Mudarabah Fina	-0,433	-0,441	0,104	0,104		4,170*	Significant
Eksternal Fac -> Risk	0,039	0,038	0,069	0,069	0.555	0.566	Insignificant
Internal Fac -> Risk	-0,259	-0,249	0,123	0,123		2,108*	Significant
Syariah Com -> Risk	0,857	0,859	0,075	0,075		11,360	Significant

Source: Primary data processed, 2019

Note: * Sig Level 99% ** Sig Level 95% *** Sig Level 90%

With a significance level of 10%, a variable that is said to have a significant effect is a variable that which has a t value of 1.64. Based on the analysis results shown in the table above, it can be seen the direct and indirect effects. The positive significant direct effect was found in the external factor pathway to mudarabah financing with a t- statistic value of 8.644> 1.64, while internal factors and sharia compliance did not have a significant positive effect because the results of the t-statistical calculation were not 0.067<1.64 and 0.965>1.64.The level of risk has a significant negative effect because it has a t-value of 4.170> 1.64.

From the picture, it can also be seen that there is an indirect influence, namely internal factors that do not have a direct influence (positive influence is not significant) on mudarabah financing, and it turns out that it has an indirect effect through external factors. The level of direct significance with the value of t statistic 0.0526 <1.64 but the indirect effect of t statistic9,149> 1.64, so that the total value of t statistic is 9,2016> 1.64. The sharia compliance which has no direct effect on financing mudarabah due to it having a statistical t 0.965 <1.64, but has an indirect effect through the level of risk with a statistical t value of 4.170> 1.64, and so the total t statistic is 5.135>1.64.

4.1. The Effects of Various Factors on Mudarabah Financing

4.1.1. Effect of Internal Factors (Management) on Mudarabah Financing

The results of the analysis of the influence of internal factors on mudarabah financing indicate an insignificant influence. With a t-statistic value of 0.067 $\leq$ 1.64, it indicates that internal factors such as the Board of Commissioners, Directors and Employees have no significant effect on mudarabah financing.

While Ahmed's research (2016), also corroborates the findings of the researcher, for the results show that stakeholders in Islamic banks, especially shareholders, are not merely pursuing worldly profits but also *ukhrawi*. The results of his research show that the owner of an Islamic bank in addition to wanting a profitable investment, also wants the benefits of others and the desire that the investment is in accordance with Islamic sharia. The aim of maximizing social value or benefits is also the desire of stakeholders in Islamic banks (Ahmad, 2000).

4.1.2. Effect of External Factors (Customers) on Mudarabah Financing

External factors namely Islamic bank customers are mudarabah financing objects that have a very large influence in creating a healthy financing system. Failure in mitigating financing risk is not only influenced by bank internal factors, but also by external factors, namely customer commitment in fulfilling all agreements in the contract (Aebi,2012). The findings in his research indicate that, internal factors such as decision makers and external factors such as customers have significant influence on bank performance including Islamic banks. The influence of customers on bank risk, starting from the initial process of filing a financing carried out until when the financing decision making will be processed (Hamza, 2013).

The description of the various studies and research results above is relevant to the findings of this study, namely the influence of external factors on the mudarabah financing portfolio. The results show that the influence of external factors, namely BPRS mudarabah financing customers in Indonesia, had a t-statistic value of 8.644 $\geq$1.64. These results indicate that external factors namely the customer have a significant positive effect on mudarabah financing.

4.1.3. Effect of Shariah Compliance on Mudarabah Financing

In general, the basic function of sharia compliance is to ensure that the operations of Islamic financial institutions meet Islamic regulations (Iqbal, 2011). Sharia compliance is a preventive effort to increase public confidence in Islamic financial institutions. The practice of mudarabah financing in Islamic banks is faced with difficult situations, both due to internal factors of Islamic banks and external factors such as customers (Ahmed, 20016). Internal factors namely the owners, management and employees of BPR Syariah prefer to maintain the level of sharia compliance compared to increasing its mudarabah financing portfolio. In testing the influence of sharia compliance, it was found that the level of sharia compliance did not have a positive effect on mudarabah financing, because the t- statistic value of 0.965 $\leq$1.64 indicates that mudarabah financing was not influenced by sharia compliance.

4.1.4. Effect of Risk on Mudarabah Financing

Mudarabah financing has a higher risk compared to other contracts (Suwailem, 2003), therefore sharia banks prefer contracts with lower risk (Mokni and Rajhi, 2016). The level of risk of mudarabah financing is because mudarabah is a financing agreement with greater uncertainty, so that both *sahibul mal* and *mudarib* are both unwilling to use it (Ahmed,2016).

The results of testing the effect of the level of risk on mudarabah financing show a significant negative effect. With a t-statistic value of 4,170 $\geq$ 1.64, it shows that the level of risk has a significant negative effect on mudarabah financing on Sharia BPR in Indonesia. This means that the high level of risk makes mudarabah financing under developed.

Based on these tests it can be stated that internal and compliance factors do not have a positive significant influence on mudarabah financing, which means that sharia management and compliance does not cause low mudarabah financing. While external factors have a significant positive influence on mudarabah financing, meaning that customer's interest in mudarabah financing influences the amount of mudarabah financing. In addition, the level of risk has a significant negative effect on mudarabah financing, meaning that the higher the risk, the lower the mudarabah financing.

4.2. Mudarabah Model Findings

The results of this study are not limited to looking for these correlations, but are deeper because they have succeeded in finding an ideal mudarabah financing model, so that it can be replicated in other BPRS in Indonesia. With the findings of an ideal mudarabah model, it is expected to be able to increase the mudarabah financing portfolio. Indicators of mudarabah financing performance are measured by the risks seen in NPF and sharia compliance.

With NPF level indicators, the ideal mudarabah financing model is found in BPRS Amanah Umah, BPRS Mitra Amal Mulia and BPRS Metro Madani, with an average NPF specifically for mudarabah financing of 2.01%, lower than the national average NPF of 5.36% for all BPRS and 9.76% for BPRS specifically as research samples. Indicators of sharia compliance, the three BPRS models have sharia compliance levels of 84.68% higher than the average of all study samples of 80.11% . Whereas if measured by the DPS assessment, the three BPRS models have sharia complian at 87.10%, higher than all samples at 81.33%.

The success of the three BPRS in carrying out mudarabah financing is due to the fact that the three processes carried out the financing well, namely preparing specific labor, planning specific mudarabah markets, conducting socio-economic assistance, and regular supervision. The results of this study are in line with the results of previous studies namely research conducted by Echchabi and Aziz (2012), regarding customer perceptions of Islamic bank services in Morocco shows that in addition to normative belief factors towards religion, also Islamic services performed by sharia bank employees influence customer decisions in choose Islamic bank products. The sharia behavior of bankers, shown by their ability to provide detailed explanations of sharia products, daily behavior, such as timely prayer and closing office services while entering prayer time also influences customer choices (Othman and Owen, 2001).

Mudarabah financing as a special product and different market segmentation, requires certain techniques or approaches in marketing it (Amin et al. 2011). The success of companies in marketing products with special segmentation is greatly influenced by their personal ability (personal selling) because not all markets can be entered in the same way (Pour et al. 2013). The special segmentation can be based on religion or beliefs because religious factors greatly influence the choice of Islamic banking products Awan and Bukhari (2011). Lee and Ullah (2011), also found that customers who have a better religious level, have a stronger desire in choosing Islamic bank products.

According to Iqbal and Mirakhor (2004), the mudarabah and musyarakah models are able to build better social relations than other contracts. Mutual social relations between sahibul mal and mudarib, can increase mutual trust and makes a very good social capital. The findings of this study reinforce the practice of mudarabah that is able to reduce risk, if a good communication is established between *sahibul mal* and *mudarib*. Therefore mudarabah financing with a social approach, is expected improve business ability for customers.

Business activities financed with mudarabah contracts are exclusive rights for mudarib, but the Islamic Financial Institution (LKS) has the authority to supervise the mudarib business (DSN, 2000). Although in general mudarib does not want to be monitored because it might disrupt their business, but supervision of mudarib business is needed to maintain commitment in fulfilling obligations by customers or mudarib (Chatta and Alhabshi, 2017), as well as increasing efficiency for banks (Chatta and Bacha, 2010).

Supervision of customer business becomes more important, as the mudarabah financing model possesses high risks and uncertainties. The problem of micro business which has become a special market for BPRS, also requires better supervision. Research by Shaikh et al. (2017), shows that micro finance in Pakistan conducts tight controls, so that problematic financing can be suppressed. Furthermore, his findings also state that the success of micro finance in developing the business of its customers is carried out through non-financial approaches, such as ease of procedures, and building good social relations.

Research conducted by Uddin (2018), on sharia governance shows results that support the importance of strict supervision. Supervision of mudarib business carried out by Sahibul Mal directly or through other parties, will encourage mudarib to be more responsible in fulfilling sharia principles. Conversely, lack of supervision opens opportunities for violations of sharia principles. Failure to fulfill sharia principles has a negative impact on Islamic banks and customers (Zain and Ali, 2017).

5. Conclusion and Future Reserach

The mudarabah financing portfolio is still very small, and has a higher level of risk compared to financing with other contracts, but has a high level of formal sharia compliance. Mudarabah financing is not influenced by BPRS management and sharia compliance but is influenced by customers and risks. The successful implementation of mudarabah financing is due to the financing process, by preparing a specific workforce that manages, plans for mudarabah specific markets, conducts socio-economic assistance, and routine supervision.

The limitation of this study are measurement of mudarabah financing is only use the size of the financing volume and NPF level and has not been measured by its effect on the BPRS revenue and profit. Sharia compliance indicators are limited to looking at formal documents and have not measured them with the maqashid index and the impact of mudarabah financing on mudarib, especially micro and small businesses. The measurement of sharia compliance also has not compared with other contracts.

The evaluation of the success of the BPRS that has become a model has not yet measured the impact of its existence on the development of mudarib businesses and the perspective of its customers. The success of the three BPRS in implementing mudarabah financing is not only measured by its ability to control risks and the high compliance of sharia, but also needs to be measured by its effect on the development of mudarib businesses. Further research is suggested to develop the results by developing the standard of success of mudarabah financing in BPRS.

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