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THE PERFORMANCE OF PROFIT AND LOSS SHARING (PLS) PRODUCTS: EVIDENCE FROM INDONESIAN ISLAMIC RURAL BANKING (IRB)

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Abstract

The main difference between Islamic banking and conventional is the concept of profit and loss sharing (PLS). Supposedly, banks have to use dominantly this concept. Nevertheless, products based on PLS are less of attention for the bankers to generate profit. Otherwise, the product based on the *Murabahah* contract is the first choice for the banker for profit-making. Therefore, this research generally aims to examine the performance of Islamic rural banking products as a source of generating revenue. Especially to prove that profit and loss sharing is the best way to generate profit. VECM analysis will apply to identify the contribution of Islamic rural banking products to generate income. In evaluating of financing performance of Islamic banks, the data was collected from the central banks' reports from 2009 to 2019. The result showed that in the long-run and short-run the PLS financing product (*Mudharabah* and *Musyarakah*) has a positive and significant effect on generating revenue. The study also revealed that the impulse response also showed that PLS gives a positive response and is stable in the long run. Furthermore, based on variance decomposition PLS has a bigger contribution to revenue.

Keywords: Islamic Rural Bank; Profit and loss sharing; Profitability; Financial performance; VECM.

INTRODUCTION

Historically, the spirit of the emergence of the Islamic banking system is profit and loss sharing. As time goes by, Islamic banking in Indonesia consists of three types namely, Bank Umum Syariah (BUS) or Islamic banks, unit Usaha Syariah (UUS) or Islamic business unit, and Bank Pembiayaan Rakyat Syariah (BPRS) or Islamic Rural Banks (IRB). IRB as a financial institution has uniqueness. One of the IRB's uniqueness is Islamic financial institutions based on financing that target the small and micro-enterprise (SME). The main purpose of IRB is to serve small and micro enterprises (SME) that need a fast, easy, and simple approval process. Because of its role in giving services to Micro and Small Enterprises, Islamic Rural Bank has an important role in improving financial inclusion.

From the data issued by the financial services authority (FSA) the number of IRB in Indonesia increased over the decades. Statistically, there are 164 banks are spreading approximately in 20 provinces out of 33 provinces in Indonesia (OJK, 2019). This is showing that the existence of the IRB provides tangible benefits towards the community at the level of the middle-lower classes.

In terms of the performance ratios as presented in figure 1, Return on Asset, the performance of Islamic rural banks fluctuates and tends to decrease respectively from 5 % and 21.55% in 2009 to 2.61% in 2019 correspondingly. However, return on equity tends to increase from 21.55% in 2009 to 27.30% in 2019. This phenomenon, in line with the OEOR ratio, which

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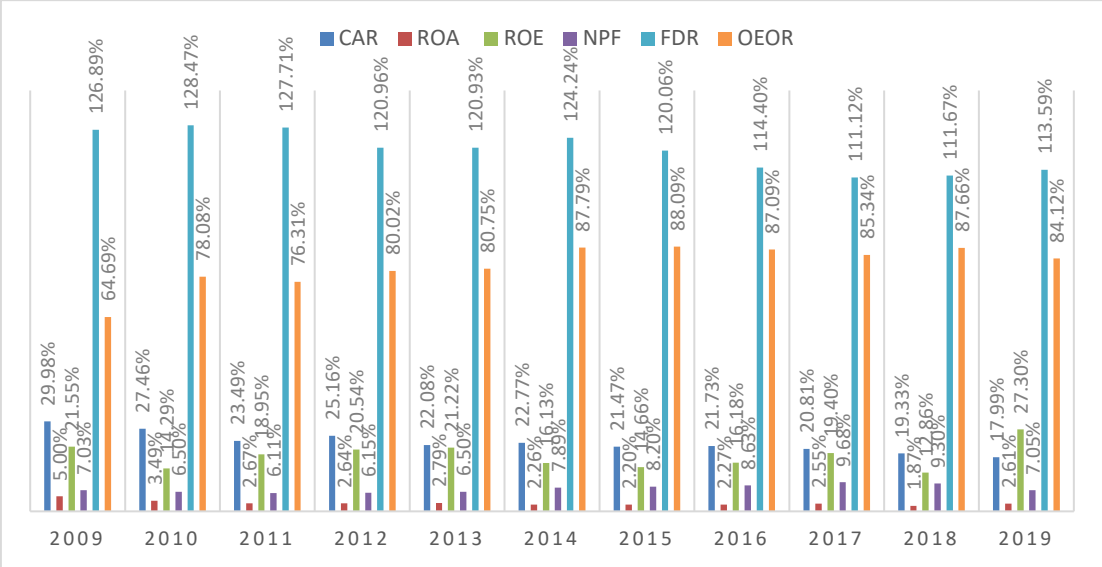
is it increases from 64.69% in 2009 to 84.12% in 2019. Nevertheless, the OEOR ratio is still below the maximum standard specified by the Central bank.

Figure 1
Ratios of Islamic rural bank 2009-2019



Source: Financial Services Authority (FSA)

Furthermore, looking at the NPF of Islamic Rural Banks, the ratio of NPF looks fluctuating and tends to be stable at 7.03% in 2009 and 7.05% in 2019. This ratio is quite high considering the maximum limit set by the Central bank of Indonesia (BI), which is 5%. This happened possibly caused by the high financing of FDR as shown in figure 1 more than 100%. Logically, the more financing distributed to real economy the more risk received. However, the study conducted by Nurmuliyani (2016) found that the quality of productive assets and rate of interest has a positive and significant effect on NPF, whereas Inflation has a negative and significant effect. Khoirunnisa (2016) found that inflation has no significant effect on NPF. Lusian *et.al.* (2014) Discovered the term of financing, the collateral the ratio of the balance of accounts receivable to the selling price significantly affects the NPF. Meanwhile, Firmasyah (2014) provides the result from external factors that caused the NPF of IRB. The result shows that GDP and Inflation negatively affect NPF. Lastly, Yasin and Widiastuti (2014) similarly found that GDP has a negative effect, but Inflation positively affects NPF.

However, looking at the data from figure 1, the financing of IRB during these years recorded an average of over 100%, which is the highest one is 128% in 2010. It means the absorption of third-party funds to real economics, especially to SMEs is very high. The increasing amount of funds used for financing means that it would increase the opportunities for gaining a greater profit. However, if seen from the initial spirit of the establishment of Islamic banks is profit-loss sharing, and then there is inequality on the portion of the distribution of the financing and it is far from what is expected. The profit-sharing pattern, besides being the essence of Islamic finance, is also more suitable to encourage the real sector, since it increases direct relations and risk-sharing between investors and entrepreneurs (Ascarya & Yumanita, 2005).

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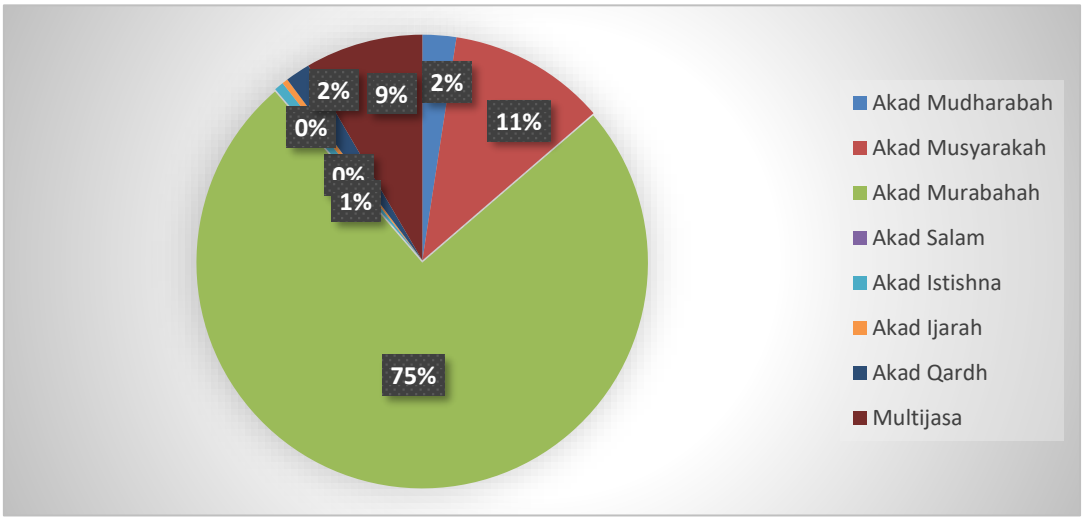
Figure 2
Composition of financing of Islamic rural bank (IRB) December 2019

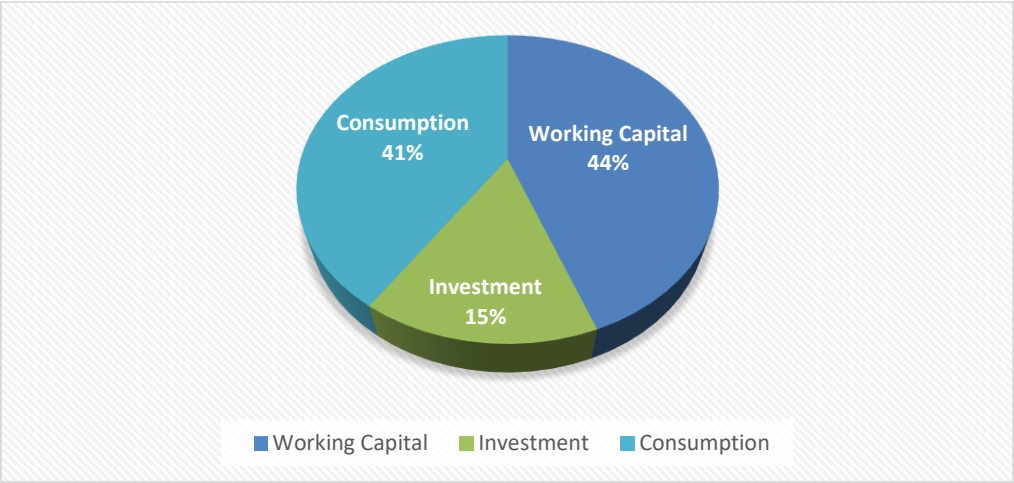


Source: Financial Services Authority (FSA)

According to FSA, in December 2019, the product with the *Murabahah* contract is the biggest part of more than 75% of total financing. The second largest is *Musyarkah* financing up to 11.27%. Whereas the products with the *Mudharabah* contracts as one of the pillars of Profit and loss-sharing are only 2.42%. Then, for the *Qardh* up to 1.78%, while *Istishna'* and *Ijarah* less than 1%, even zero percentage for Salam contract. It is quite interesting, multi-purpose financing is up to 9%.

Back into the data of FSA, the distribution of financing based on the type of usage, consumption occupies the highest rank followed by working capital and investment. It could describe why *murabahah* is the biggest portion of IRB financing.

Figure 3
Financing of Islamic Rural Banks based on Type of Usage December 2019



Source: Financial Services Authority (FSA)

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Some studies have tried to find the causes of the low portion of profit-loss sharing financing in Islamic banks or Islamic rural banks. Ascarya and Yumanita (2005) examined the cause of the lack of PLS financing of Islamic banks using the ANP approach. The finding showed there are several causes, mainly caused by the lack of understanding and human quality of Islamic bankers, and the lack of supportive regulations. This study was strengthened by Ramdani and Tanjung (2014). They found that in more detail, the primary problems are lack of knowledge of the human resource, lack of commitment of the authority, product, business-oriented of the top Management, and conventional competition on products. Furthermore, specifically, the study on the lack of portion PLS on IRB, identified the factors that affect the low portion of *mudharabah*, mainly are the high risk, uncertainty, report mechanism, high NPF, difficulty in analysis, partner's transparency, human resource capacity, lack of trust (Adnan & Purwoko, 2013). This finding is similar to what Nurhasah (2010) pointed out the cause of lack portion of PLS financing are the high risk, unstandardized products, imperfect regulations, the role of *shari'ah* supervisor boards, and equally essential is unpreparedness the communities to accept the consequence of the contracts.

Islamic rural banking as an intermediary institution facilitates the surplus unit and deficit unit in general. However, the differences are the contracts used in dealing with transactions between the banks and the customers. The third-party fund usually used *wadi'ah* and *Mudharabah* contracts. From the financing side, general, the financing of Islamic banking has been divided into three categories, namely sale such as *bai', salam*, and *istishana'* contracts; partnership such as *Mudharabah* and *Musharakah* contracts, and services. These contracts have differences in risks and returns in nature. Islamic Rural Banks in its business activities can use these various contracts and complementary contracts. The use of the contracts in the banking products has been legitimized by *fatawa* and it has been codified in positive law. However, as the data described above is not the entire contract is used proportionally in transactions with customers for various reasons. Profit loss and sharing, as the spirit of the emergence of the Islamic bank, should be placed at the forefront over the non- profit-loss sharing. Therefore, the main purpose of this study is to explore the performance of Islamic banking products in generating revenue, especially the contribution of the PLS financing product.

LITERATURE REVIEW

The performance of the financial ratios towards profitability

There are many studies focused on the performance of Islamic rural banks in Indonesia. Mostly their focus is on the determinants of financial ratios, such as CAR, FDR, NPF, OEOR, towards Islamic banks profitability. However, the results of empirical tests and patterns of effect appear to be vary depending on the size, the sample, and the type of data. These studies are summaries as follows. Khatimah (2010), Muhaemin and Wilasih (2016), and Harianto (2017) showed that Capital Adequacy Ratio (CAR) has a positive and significant effect on the profitability of IRB. On the contrary, Krisnawati (2014), Widyaningrum and Septiarini (2015), and Irwan Ch (2017) showed CAR has a positive but insignificant effect on ROA. Furthermore, Rizal (2016), and Azmy (2018) found that CAR has a negative relation and an insignificant effect on ROA and ROE. Hosen and Fitria (2014) found that CAR has a negative and significant effect on ROE but has a positive and insignificant effect on ROA. Nasution (2017) found that CAR has a Negative and significant effect on net operating margin (NOM). Maisyah and Mawardi (2015)

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also found that CAR has a negative and significant effect, which is strengthened Nasution's finding.

The result of the financing deposit ratio (FDR) towards ROA or ROE is varying. Muhaemin and Wilasih (2016) and Nasution (2017) showed that FDR has a positive and significant effect on ROA. Conversely, Widyanigrum, Septiarini (2015), and Harianto (2017) found that FDR has a positive relationship but is insignificant towards ROA. However, the negative sign found by Azmy (2018) and Irwan Ch (2017), however, it has significant according to Amzy (2018) and insignificant according to Irwan Ch (2017). Besides, Sumachdar and Hasbi (2011) discovered that FDR has a significant influence on third-party funds.

Next is the result of the influence of non-performing financing (NPF). Ma'isyah and Mawardi (2015), Muhaemin and Wiliasih (2016), Rizal (2016), Husaeni (2017), Harianto (2017), Nasution (2017), Irwan Ch (2017), and Azmy (2018) showed the result that NPF has a negative and significant effect towards ROA. However, Widyanigrum and Septiarini (2015) found that NPF has a negative but insignificant effect on ROA. Krisnawati (2014) discovered that NPF has a Negative but insignificant effect on ROE.

Whereas the influence of operating efficiency and operating revenue (OEOR) variables showed different results too. Widyaningrum and Septiarini (2015), Muhaemin and Wiliasih (2016), Rizal (2016), Harianto (2017), Nasution (2017), and Irwan Ch (2017) showed that the operating efficiency ratio has a negative and significant effect on ROA. Furthermore, Azmy (2018) found different results between ROA and ROE which is Operating efficiency towards ROA has the same result with previous studies, whereas ROE has a positive relationship. Conversely, Hosen and Warninda (2014) showed the negative sign and significance of ROE.

The performance of the products towards profitability

Meanwhile, the research tried to look at the performance of the products mostly focused on *Mudharabah, Musharakah, Murabahah* towards ROA, or ROE. The result shown is varying depending on the size, the sample of the data. The result of the influence of the *Mudharabah* product showed has negative sign of an insignificant effect towards ROE (Fatmawati, 2016), whereas it has a positive sign and insignificant effect on ROA (Fatmawati, 2016), and (Nawawi, Nurdiansyah, & Qodliyah, 2018). Interestingly, Anjani and Hasmarani (2016) revealed that *Mudharabah* has a negative and significant effect on ROE. Furthermore, Yuliana (2012) tested the performance of Islamic baking products in two models with and without non-financial variables. The result with and without non-financial showed that *Mudharabah* has a positive and significant effect on the profitability of ROA and ROE. Warninda (2014) discovered that *Mudharabah* Time Deposit (MTD) has a negative and significant impact on Islamic Rural Bank profitability either in the short or in the long run. However, *Mudharabah* Saving Deposit (MSD) has no significant effect on Islamic Rural Bank profitability either in the short or in the long run.

The result of the influence of the *Musharakah* product has negative and insignificant towards ROA and ROE (Fatmawati, 2016). However, Yuliana (2012) revealed that without a non-financial indicator, *Musharakah* has a positive and significant effect on ROA, whereas with non-financial indicators Mushairakah has a positive sign and significant towards ROE but insignificant towards ROE. Furthermore, Anjani and Hasmarani (2016) found that *Musharakah* also has a positive and significant effect on ROE. Otherwise, interesting findings by Nawawi, *et.al* (2018) and Agza and Darwanto (2017) which they found that *musharakah* has a negative sign and a significant influence on ROA. Additionally, Yuliana (2012) also showed that the

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performance of IRB is better than IB in the BPRS in managing *musharakah* financing. In general terms of profit and loss sharing (PLS), furthermore, Saleh et.al., (2018) found that PLS has a negative sign and does not have a significant effect on profitability.

Additionally, the Murabahah product has a positive sign and is insignificant towards ROA, but significant to ROE (Fatmawati, 2016). Furthermore, Agza and Darwanto (2017) found that *Muarabahah* has a positive and significant effect on ROA. Yuliana (2012) when it included the non-financial indicator showed that *Murabahah* has no significant effect on ROA and ROE. However, when it excluded the non-financial indicator showed different results which is a positive sign and insignificant toward ROA but significant towards ROE. Contrary, Anjani, and Hasmarani (2016) found that *Murabahah* financing does not affect ROE significantly. Lastly, the other products such as *Istishna, Qardh,* and *salam* have a different result in termination of the performance Islamic banking product, where most are not significant either positive or negative sign (Yuliana, 2012).

The influence of the external factors on profitability

Also, the study included the external factors found that inflation has a negative relationship and significant effect on the profitability of Islamic Rural Banks, meanwhile, the interest rate has a negative relationship but is insignificant towards the profitability of Islamic Rural Banks in Indonesia (Husaeni, 2017).

Furthermore, according to Warninda (2014) inflation has an insignificant effect on Islamic Rural Bank profitability in the short run but negatively significant towards IRB in the long run. Fithria and Sholihin (2018) showed that Inflation has a positive significant effect on profitability. Furthermore, Warninda (2014) showed that Money Supply (M2) has a positive significant effect on Islamic Rural Bank profitability either in the short-run or in the long run.

Then, the results showed that bank size has a positive and significant effect on the performance of Indonesian Islamic rural banks (Fithria & Sholihin, 2018). On the contrary, Warninda (2014) showed that Bank Size has an insignificant effect on Islamic Rural Bank profitability in the short run but has a negatively significant effect in the long run.

RESEARCH METHOD

The source of Data

To carry out this study, monthly time-series data from the period of January 2009 to December 2019, are collected for Indonesia Islamic banking. The Islamic banking data such as variables such as Revenue, *Mudharabah, musharakah, Ijarah, Murabahah, Qardh, Salam, Istishna',* and Multipurpose services are derived from the Financial Services Authority (OJK). The Inflation was retrieved from the Central Bank of Indonesia, which is published in the Bank scope database.

Method of Analysis

This study will employ VECM to provide evidence of the performance of profit-loss sharing (PLS) of IRB in Indonesia. Consequently, there are several steps before analyzing Islamic Rural Bank profitability determinants for the short and long run using VECM. These tests included the unit root test using ADF, and co-integration Tests. Soon after that knowing the figure of co-integration equations, then moves to the VECM analysis. VECM is a technique or model

for correcting short-run disequilibrium into long-run equilibrium. Because of its advantages in combining short and long-run effects, ECM becomes a model that can explain the explanatory variables well. This method is used when the variables of the research are cointegrated at the first difference. Generally, the VECM formula Specification is as below:

$$\Delta Y_t = \sum_{i=1}^{k-1} \Gamma_i \Delta Y_{t-1} + \mu_0 + \mu_{1t} + \alpha\beta Y_{t-1} + \varepsilon_t \qquad (1)$$

Where:

ΔY_t	=	$Y_t - Y_{t-1}$
k-1	=	Order of VECM from VAR
Γ_i	=	Regression coefficient matrix (b_1, ..., b_i),
μ_0	=	Intercept vector
μ_1	=	Regression coefficient vector
T	=	Time trend
α	=	Loading matrix
β	=	Cointegration vector
Y	=	Variables used in the analysis

To complement this study, impulse response function (IRF) and forecast error variance decomposition (FEVD). A method that is used to determine the response of an endogenous variable on a certain shock is namely Impulse Response Function (IRF). This shock maybe will transmit to the other dependent variables through a dynamic structure or lag structure in the VAR model. IRF fundamentally maps out the dynamic response path of a variable due to a one-period standard deviation shock to another variable. Furthermore, Forecast Error Variance Decomposition (FEVD) is used to examine how the change in a variable is affected by other variables. Through this method, the strength, and weaknesses of a variable in influencing other variables, in the long run, can be analyzed.

RESULT AND DISCUSSION

Unit Root Test

The results of the ADF tests at a level and first differences are reported in Table 1, by taking into consideration of trend variable in the regression (constant and linear trend). Based on the ADF test, maxlag=10, is only two variables are stationary. These indicate that these series are non-stationary at level form. Consequently, the next step of the test needs to do. After changing the data into the first difference, all variables are stationary.

Table 1
Unit root test at a level and a first different

Variables		ADF at level			ADF at first different	
	ADF Statistic	***CV 5%***	***P-Value***	***ADF Statistic***	***CV 5%***	***P-Value***
Revenue	-24.07422	-3.447383	0.0000*	-116.1460	-3.447699	0.0001*

Mudharabah	-2.349067	-3.444487	0.4045	-9.539228	-3.444756	0.0000*
Musharakah	-2.523435	-3.444487	0.3165	-9.951981	-3.444756	0.0000*
Murabahah	-3.034211	-3.444756	0.1271	-9.121724	-3.444756	0.0015*
Istishna	-3.351457	-3.447072	0.0630	-6.299202	-3.444756	0.0000*
Ijarah	-1.246004	-3.444487	0.8962	-12.69018	-3.444756	0.0000*
Salam	-3.934352	-3.444756	0.0133*	-8.965514	-3.444756	0.0000*
Qardh	-2.251736	-3.444487	0.4568	-11.36627	-3.444756	0.0000*
Services	-1.068284	-3.444756	0.9295	-5.195363	-3.444756	0.0002*
Inflation	-2.853632	-3.445030	0.1813	-7.901848	-3.445030	0.0000*

Lag Length Criteria

Once all the variables are stationary in level or first difference, find the number of maximum lag where at that number Vector Autoregressive system will be stable. From table 2, the maximum number of lags where the VAR system is stable can be found. Referring to the indicators i.e., LR, FPE, AIC, SC, and HQ, three of them have Lag length criteria at eight and one indicator at zero levels and one level. However, this study will choose the HQ criteria that is Lag 1.

Table 2
Lag length criteria

Lag	LogL	LR	FPE	AIC	SC	HQ
0	6356.478	NA	7.22e-58	-103.1948	-102.9661*	-103.1019
1	6541.993	337.8495	1.81e-58	-104.5853	-102.0703	**-103.5637***
2	6612.415	116.7969	3.01e-58	-104.1043	-99.30302	-102.1540
3	6686.123	110.2632	4.98e-58	-103.6768	-96.58918	-100.7978
4	6797.758	148.8466	4.81e-58	-103.8660	-94.49204	-100.0583
5	6955.730	184.9428	2.44e-58	-104.8086	-93.14835	-100.0722
6	7075.211	120.4525	2.73e-58	-105.1254	-91.17878	-99.46031
7	7212.650	116.2086	2.88e-58	-105.7342	-89.50122	-99.14038
8	7408.091	133.4720*	1.68e-58*	-107.2860*	-88.76678	-99.76356

Cointegration Test

Once upon all the variables are stationary in level or first difference, before conducting a VECM test, the thing to do is a cointegration test. Even if there is one or more variables in the system are not stationary but possess a cointegration relation, then the linear combination among the variables in the system will be stationary and form a stable long-run equilibrium.

Table 3
Johansen-Juselius Cointegration test

Null Hypothesis	**System with CR**		**Critical value at 5%**	
	Trace	**Max. Eig**	**Trace**	**Max. Eig**
r= 0	0.539770	0.539770	522.0511*	100.1077*
r= 1	0.483468	0.483468	421.9434*	85.21979*
r= 2	0.455968	0.455968	336.7236*	78.52839*

r= 3	0.372042	0.372042	258.1952*	60.02140*
r= 4	0.325023	0.325023	198.1738*	50.70680*
r= 5	0.309753	0.309753	147.4670*	47.82096*

** denotes rejection of the hypothesis at the 0.05 level*

As shown in the table above, at least there is one co-integration for Trace statistic and Maximum Eigenvalue in the long run cointegration. Based on both tests, it can be concluded that the revenue of Islamic rural banks and its determinants revealed a long-run relationship.

Vector Error Correction Analysis

As proved above the series are cointegrated, and then we proceed to determine the direction of causality within the VECM framework. VECM estimation results show a short-term and long-term relationship between revenue, *musharakah*, *mudharabah*, *murabahah*, *salam*, *Istishna*', *Qordh*, multipurpose services financing, and inflation. In this estimation, revenue is the dependent variable, while the rest is the independent variable. VECM is used to estimate the speed of adjustment on the instability relationships from short-term to long-term equilibrium. The results are presented in the equation below:

DRevenue = 000238 +10.35512DMudharabah +2.016868DMurabahah +4.028746DMusharakah
(1.65029) (0.77395) (1.61789)
[-6.27473] **[-2.60596]** **[-2.49012]**

-52.41253DQordh +29.22890DIjarah +19.22905DIstishna' -430.9967DSalam
(6.47060) (14.6847) (12.8373) (258.011)
[8.10010] **[-1.99043]** [-1.49791] **[1.67046]**

+2.156321DServices -0.581189Dinflation
(4.13898) (0.63987)
[-0.52098] [0.90829]

The equation above showed that *Qordh*, *Salam*, and Inflation negatively affect the performance of Islamic rural banks in generating revenue in the long run. That means, if there is a 1% increase in *Salam*, *Qordh* financing, and inflation, it will cause revenue to decrease by 52.4125%, 430.997%, and 0.581% respectively. However, Inflation does not affect significantly generating revenue of IRB. While the rest variables namely *Mudharabah*, *Musharakah*, *Murabahah, Ijarah, Istishna*, and multi-purpose Services have a significant and positive impact on the performance of Islamic rural banks generating revenue. That means, if there is a 1% increase in *Mudharabah, Musyarakah, Istishna',* and Multipurpose, it will cause revenue to increase 10.355%, 4.028%, 2.169%, 29.299%, 19.299%, and 2.156% correspondingly.

However, *istishna'* and multipurpose services financing have an insignificant effect on the IRB in generating revenue. Additionally, it is interesting to note that *Murabahah* is the biggest portion of financing (more than 70%) but its contribution on gaining revenue is only 2.169%. It is time to reconsider the financing priority not focusing on the financing of fixed-returns such as *Murabahah*. However, it is better to focus on PLS financings such as *Mudharabah* and *Musyarakah* as the result shown above.

Subsequently, based on the results presented in Table 5, in the short run, there are 6 significant variables at the five percent level and *error correction* variable. These variables are revenue, *Mudharabah*, *Murabahah*, *Musyarakah*, *Qordh*, and *Salam*. The presence of significance in *error correction* parameters proved the adjustment mechanism from the short-run to the long-run. The value of adjustment from short-term to long-term is -0.565%.

Table 4
Short-term Equation

Error Correction:	Coefficients	S.E	t-test
CointEq1	-0.564950	(0.11027)	**[-5.12346]**
D(DREVENUE (-1))	-0.437048	(0.08540)	**[-5.11749]**
D(DMUDHARABAH (-1))	8.568749	(1.92849)	**[4.44325]**
D(DMURABAHAH (-1))	-1.408051	(0.60539)	**[-2.32587]**
D(DMUSYARAKAH (-1))	9.252565	(1.70796)	**[5.41731]**
D(DQORDH (-1))	16.92984	(4.60312)	**[3.67791]**
D(DIJARAH (-1))	0.236840	(8.76817)	[0.02701]
D(DINFLATION (-1))	-0.309827	(0.58218)	[-0.53218]
D(DISTISHNA (-1))	17.79444	(16.9668)	[1.04878]
D(DSALAM (-1))	513.6695	(214.638)	**[2.39319]**
D(DSERVICES (-1))	-1.160210	(4.41462)	[-0.26281]
C	-3.73E-05	(0.00396)	[-0.00943]

Short-term estimation results showed that the revenue variable at lag 1 has a negative effect, at the level of five percent by -4.437. This means, if there is an increase of 1% in the previous year, it will reduce revenue by -4.437% in the current year. *Mudharabah* positively will increase the revenue by approximately 8.568% if the financing increases by 1% in the previous year. However, in *Murabahah* financing, if there is financing increased by 1% in the previous year, the revenue decreased by 1.408% in the current year. Furthermore, if there is a 1% increase in *Musyarakah* financing in the previous year, there will be an increase in revenue by 9,253% in the current year. Something is interesting here, namely the *Qordh* variable if there is an increase in *Qordh* which is financing that does not generate profits, contributes to increasing revenue by 16.930% if in the previous year increased by 1%. The last is *Salam* financing, the results show that if there is an increase of 1% in Salam financing in the previous year it will increase revenue by 513.669% in the current year.

Impulse Response Function (IRF)

The vertical axis in the IRF figure displays the standard deviation used to measure how much the response will be given by the financing of *Mudharabah, Musyarakah, Murabahah, Qordh, Salam, Istishna',* Multipurpose services, and Inflation if there is a shock to Revenue. Meanwhile, the horizontal axis presents the length of response time if there is a shock to the revenue. If the revenue response above the horizontal axis indicates that the shock will have a positive effect and vice versa.

Figure 4 shows the 44 periods that each period consists of 3 months. Figure 3 presents that there is a shock response from all variables. Four variables namely, Qordh, Salam, and inflation

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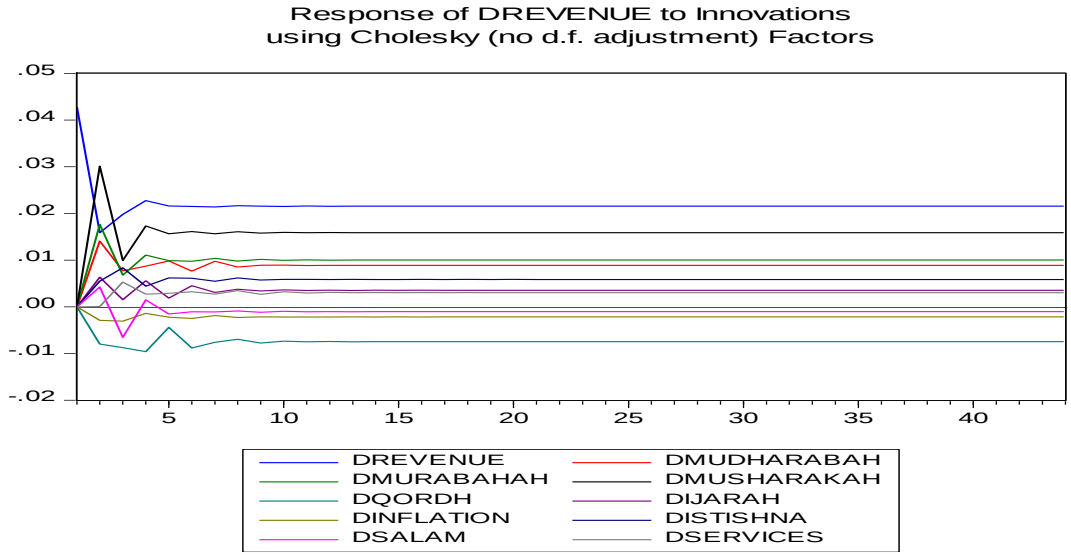
have negative responses. Whereas the rest variables such as *Mudharabah, Murabahah, Musyarakah, Istishna',* and Multipurpose services have positive responses. Generally, the shock response occurred during 5 periods namely 15 months. Then the next period, the response seems to lower fluctuate until the period of 10, then after the period of 10, the response becomes stable until the end of the period.

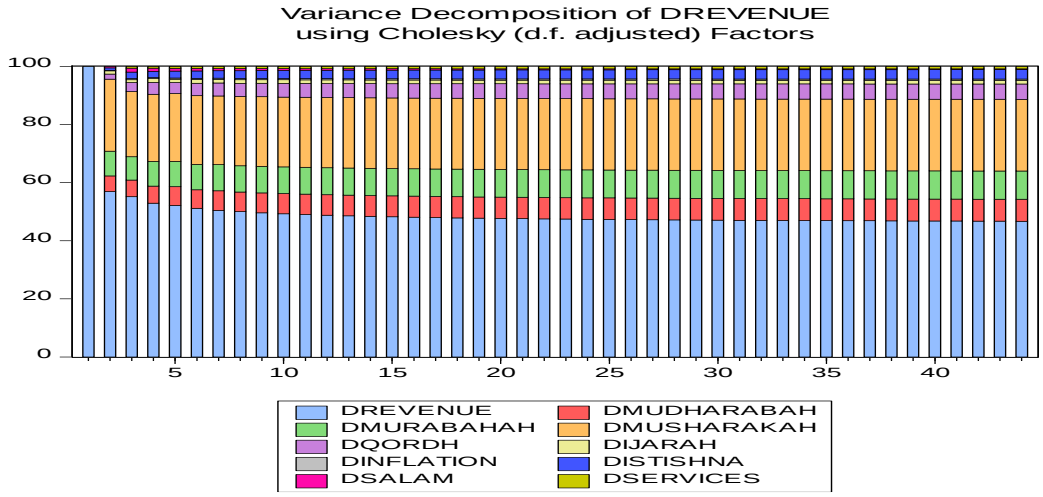
Figure 4
Impulse Response Function test



Forecast Error Variance Decomposition (FEVD)

Figures 4 present the result of Forecast Error Variance Decomposition (FEVD) for Revenue determinants. In the first period, all proportions of error variance of Revenue can be explained by revenue's shock. However, in the second period until the 44th month, it shows that the diversity of Revenue is influenced by other variables such as *Musyarakah, Mudharabah, Murabahah, Salam, Ijarah, Qordh, Istishna'*, Multipurpose services, and inflation.

Figure 5
Forecast Error Variance Decomposition



The figure shows that in generating revenue, *Musyarakah* has the biggest proportion to the behavior of Revenue with 24.685% followed by *Murabahah*, *Mudharabah*, and *Qordh* financing with 9.721%, 7.558%, and 5.287% respectively. Meanwhile, the rest variables contribute to the behavior of revenue with fewer than 5%. The result of variance decomposition shows that the influence of PLS financing (*Musyarakah* and *Mudharabah*) on revenue reached more than 30 percent bigger than fixed return financing (*Murabahah, istishna', Salam,* Services) is only 15.3%. It is proved that PLS is a better financing product in influencing the revenue of IRB.

CONCLUSION

Based on the data of FSA, the use of PLS financing products is still unsatisfactory. The portion of PLS is less than 30% of total financing. The biggest financing is *Murabahah* financing the portion of more than 70%. Based on this phenomenon, this study tries to examine the role of PLS in generating revenue for IRB in Indonesia. Therefore to satisfy this study all products of the financing were examined. The study used the VECM approach to know the performance of PLS financing products of IRB in generating revenue.

Based on the result above, in the long run, *Mudharabahah, Musyarakah, murabahah*, and *Ijarah* have a positive and significant effect on revenue. However, *Qordh* and Salam have a negative and significant effect on revenue. This study found that PLS financing products (*mudharabah* and M*usyarakah*) have a bigger effect on revenue than *Murabahah* financing products. In the short run, the result shows that error correction is significant which means the long term will be adjusted by the short term with -0.565%. Furthermore, the outcome shows that the variables that influenced the revenue are revenue in the previous year, *Musyarakah, mudharabah, murabahah, qordh,* and *Salam,* while the rest are insignificant variables.

The results of impulse response indicate that shocks that occur in *Mudharabah, Murabahah, Musyarakah, Istishna',* and Multipurpose services are responded positively by Revenue and have stable conditions within almost the same period for all variables. Shocks that occur in other variables such as *Qordh, Salam,* and inflation are responded negatively by Revenue and have a stable condition in a period that is not much different. Moreover, the result of the variance decomposition indicates that *Musyarakah* financing has the largest contribution among other variables, followed by *Murabahah, Mudharabah,* and *Qordh* financing in influencing the amount of income. Meanwhile, the rest of the financing has a very small contribution of less than 2%.

Hence, based on these results, IRB should reconsider a new strategy to increase performance of PLS. IRB should give more priority to the PLS financing product than other products to generate revenue.

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