FINANSIA : Jurnal Akuntansi dan Perbankan Syariah
P-ISSN: 2621-4636 E-ISSN: 2621-4644
Vol. 7 No. 2 July-December 2024
http://e-journal.metrouniv.ac.id/index.php/FINANSIA
DOI: https://doi.org/10.32332/finansia.v7i2.9516

PROFITABILITY DETERMINANTS OF INDONESIAN ISLAMIC BANKS: FINANCING TO DEPOSIT RATIO AND GOVERNANCE

Tri Wahyudi[1*], Fiesty Utami[1], Nur Sabrina[2]
[1]Sultan Ageng Tirtayasa University, Indonesia
[2]MARA University of Technology, Malaysia
*fiestyutami@untirta.ac.id

Accepted: June 28, 2024	Revised: September 09, 2024	Published: December 04, 2024

Abstract: This study aimed to thoroughly examine the impact of financing-to-deposit ratio (FDR) on profitability of Islamic commercial banks in Indonesia, with Good Corporate Governance (GCG) acting as an intervening variable. In order to achieve the objective, financial data spanning 2015 to 2019, collected from annual reports and financial statements of selected banks were analyzed. Accordingly, regression and mediation analyses were adopted to test the hypotheses. The results showed that FDR did not significantly affect profitability (measured by Return on Assets (ROA)). GCG was also observed to not efficiently mediate the relationship between FDR and ROA. These findings suggest that other factors may play a more substantial role in determining profitability of Islamic banks. The present study underscores the importance of adopting conservative financing strategies and enhancing corporate governance frameworks designed specifically in adherence to Sharia regulations. Essentially, the insights provide valuable recommendations for bank managers and policymakers to improve financial performance and ensure sustainable growth in Islamic banking sector.

Keywords: FDR; Profitabilty; Islamic Banks; Corporate Governance

Abstrak: *Penelitian ini menguji dampak FDR terhadap profitabilitas bank umum syariah di Indonesia, dengan mempertimbangkan GCG sebagai variabel intervening. Analisis ini menggunakan data keuangan dari tahun 2015 hingga 2019, yang dikumpulkan dari laporan tahunan dan laporan keuangan bank-bank terpilih. Penelitian ini menggunakan analisis regresi dan mediasi untuk menguji hipotesis. Hasil penelitian menunjukkan bahwa FDR tidak secara signifikan mempengaruhi profitabilitas, yang diukur dengan ROA. Selain itu, GCG tidak memediasi hubungan antara FDR dan ROA. Temuan ini menunjukkan bahwa faktor-faktor lain mungkin memainkan peran yang lebih penting dalam menentukan profitabilitas bank syariah. Studi ini menggarisbawahi pentingnya mengadopsi strategi pembiayaan yang konservatif dan meningkatkan kerangka kerja tata kelola perusahaan yang disesuaikan dengan kepatuhan Syariah. Wawasan ini memberikan rekomendasi yang berharga bagi para manajer bank dan pembuat kebijakan untuk meningkatkan kinerja keuangan dan memastikan pertumbuhan yang berkelanjutan di sektor perbankan syariah.*

Kata Kunci: *FDR; Profitabilitas; Bank Syariah; Tata Kelola Perusahaan*

Citation of this article with the format Tri Wahyudi, Fiesty Utami, And Nur Sabrina, "Profitability Determinants Of Indonesian Islamic Banks: Financing To Deposit Ratio And Governance," *FINANSIA : Jurnal Akuntansi dan Perbankan Syariah* 7, no. 2 (2024): p.
DOI: https://doi.org/10.32332/finansia.v7i2.9516

Introduction

Islamic banking in Indonesia has witnessed significant growth over the past decade, and this was driven by the increasing demand for Sharia-compliant financial products and services.[1] According to data from Financial Services Authority (OJK), the market share of Islamic banking in Indonesia was observed to increase significantly from around 3-4% in 2010 to approximately 6-7% in 2020. This increase was attributed to the principles of Islamic banking, namely the prohibition of interest (riba) and emphasis on risk-sharing, ethical investments, and asset-backed financing, which have appealed to a large segment of Indonesian population.[2] To further support the elucidation, a report from Bank Indonesia stated that the demand for Sharia-compliant financial products had risen due to increased awareness of Sharia principles, including the prohibition of riba, risk-sharing mechanisms, and ethical investment practices.[3] The expansion of this sector is not only a reflection of religious adherence but also a response to the global financial crises, which emphasized the need for a more resilient and ethical banking system.[4]

Regardless of this growth, profitability of Islamic commercial banks remains a critical issue, as these institutions were reported to have faced unique challenges compared to respective conventional counterparts.[5] As stated in a prior study, key profitability metrics such as Return on Assets (ROA) and Return on Equity (ROE) are very important in assessing the financial performance of these institutions.[6] Islamic banks in Indonesia have also been reported to face significant challenges related to liquidity management, and these issues are reflected in financing-to-deposit ratio (FDR) of the institutions. To support this elucidation, another study reported that FDR of Islamic banks averaged between 80-90%. This signified a high utilization of deposits for financing and posed liquidity risks that must be carefully managed.[7] FDR plays an important role in this context, as the metric directly impacts liquidity management and profitability.[8]

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[1] Agus Alimuddin, Fani Monada Essa Putri, Immawan Azhar Ben Atasoge, And Risa Alvia, "Baitul Mal Dan Ghanimah Studi Tentang Ijtihad Umar Bin Khattab Dalam Penguatan Lembaga Keuangan Publik," *Jurnal Akuntansi Dan Perbankan Syariah* 05, no. 01 (2022): 31.

[2] U Priyadi, "Determinants Of Credit Risk Of Indonesian Sharīʿah Rural Banks," *ISRA International Journal Of Islamic Finance* 13, no. 3 (2021): 284.

[3] Ali İhsan Akgün, "The Relationship Between The Accounting Standards And The Global Financial Crisis: Empirical Analysis Of Mergers And Acquisitions In Banking Industry," *China Accounting And Finance Review* 26, no. 3 (2024).

[4] Cut D Hasrina and Azlim Yusri, "The Development Analysis of Sharia Bank in Province of Aceh in Last Decade," 2019.

[5] Wahyu Wastuti, Riris Aishah Prasetyowati, And Ratna Anggraini, "Financing Growth And Bank Risk: Empirical Evidence From Indonesia," 7, no. 1 (2024): 1.

[6] Bun Yamin, "The Effect Of Return On Asset (ROA), Operational Efficiency Ratio (BOPO), Inflation, Credit Interest Rate And Gross Domestic Product (GDP) Towards Murabahah Financing In Sharia Banking In Indonesia (2016-2019)," *Asian Journal Of Economics Business And Accounting*, (2022): 94.

[7] Sutrisno, "Islamic Banking Profitability in Indonesia," *International Journal of Finance & Banking Studies* 12, no. 1 (2023): 1.

[8] Lucky Nugroho, Ahmad Badawi, Erik Nugraha, And Yananto M Putra, "What Determines Islamic Performance Ratio Of Islamic Banking In Indonesia? An Analysis Using Financing To Deposit Ratio As Moderator," *Share Jurnal Ekonomi Dan Keuangan Islam* 10, no. 1 (2021): 104.

Additionally, effective corporate governance is essential for maintaining the trust of stakeholders and ensuring the sustainable growth of these banks.[9]

Table 1. ROA Development of Indonesian Sharia Commercial Banks in 2015-2019

	2015	2016	2017	2018	2019
ROA	0.48	0.62	0.62	1.27	1.72

Source: www.ojk.go.id 2020

As shown in Table 1, ROA variable experienced significant growth between 2015 and 2019. The variable began at 0.49% in 2015 and increased to 0.62% in 2016, maintaining this level in 2017. In 2018, ROA significantly rose to 1.27% and further increased to 1.72% in 2019. Based on this data, an inference can be made that from 2016 to 2017, the profits of Islamic banks remained stable, without significant changes. This stability occurred despite a slowdown in growth, attributed to unfavorable economic conditions that had not yet improved.

The primary problem addressed in this study includes the impact of FDR on profitability of Islamic commercial banks in Indonesia. According to a prior investigation, understanding the dynamics between FDR and profitability is very important for Islamic banks to optimize respective financial strategies and ensure sustainable operations.[10] The larger assets enable the banks to offer more significant financing, and this potentially leads to higher profitability.[11]

Effective corporate governance can help mitigate the risks associated with high FDR by promoting better management practices, transparency, and accountability.[12] In this context, a risk that can be mitigated includes the fact that although Islamic banks distribute financing to support economic activities, the efforts has not consistently increased profitability.[13] Generally, FDR is an important metric used to measure the liquidity and financing capacity of any bank. This statement is supported by previous studies where it was shown that a balanced FDR was essential for maintaining liquidity while ensuring sufficient financing activities to generate profits in banks.[14] Explorations have also shown that a higher FDR can strain bank liquidity, potentially leading to

[9] Muhammad S Shahid And Usman Shahid, "CEO Overconfidence And Corporate Investment: Moderating Role Of Corporate Governance Practices," *Review Of Applied Management And Social Sciences* 3, No. 1 (2020): 41.

[10] Saleh Sitompul And Siti K Nasution, "The Effect Of Car, BOPO, NPF, And FDR On Profitability Of Sharia Commercial Banks In Indonesia," *Budapest International Research And Critics Institute (Birci-Journal) Humanities And Social Sciences* 2, no. 3 (2019): 234.

[11] Agus Widarjono and Sahabudin S Sidiq, "The Sectoral Financing Diversification and the Profitability of Islamic Banking in Indonesia," *Jurnal Ekonomi Dan Bisnis Islam (Journal of Islamic Economics and Business)* 8, no. 2 (2022): 201.

[12] Alex Abugri, "Effect Of Corporate Governance On Financial Distress: Evidence From Listed Firms At Ghana Stock Exchange," *International Journal Of Multidisciplinary Research And Analysis* 05, no. 02 (2022).

[13] Hasan Mukhibad And Muhammad Khafid, "Financial Performance Determinant Of Islamic Banking In Indonesia," *Jurnal Keuangan Dan Perbankan* 22, no. 3 (2018).

[14] Ahmad I Rahmansyah, Nasya S Balqis, Yekti Rahajeng, Muhammad S H Elmas, And Siti Masluha, "The Effect Of Non Perfoming Financing And Financing To Deposit Ratio On Return On Assets," *Assets Jurnal Ilmiah Ilmu Akuntansi Keuangan Dan Pajak* 6, no. 2 (2022): 100.

financial instability and reduced profitability.[15] Meanwhile, a lower FDR may signify underutilization of funds, limiting the bank income-generating potential.[16] The impact of FDR on profitability is influenced by factors such as Non-Performing Financing (NPF), Capital Adequacy Ratio (CAR), and Operating Efficiency Ratio (OER).[17]

Islamic banks must balance the ethical and financial aspects of respective operations, adhering to risk-sharing mechanisms and avoiding interest-based transactions.[18] As stated in a previous study, the integration of FDR with other financial indicators, such as NPF and CAR, provides a holistic view of the financial health and operational efficiency of a bank.[19] This integrated method has been observed to help Islamic financial institutions navigate the complexities of maintaining liquidity and profitability while complying with Sharia principles.[20]

Based on previous observations, effective corporate governance is an important requirement for every financial institution.[21] This is evidenced by the fact that studies have consistently emphasized the positive impact of effective governance practices on financial performance.[22] Strong corporate governance frameworks invariably enhance decision-making processes, reduce capital expenditure, and improve entire financial outcomes.[23] In Islamic banks, these frameworks must be implemented in line with Sharia compliance, adding a layer of complexity and ethical considerations.[24] By fostering transparency, accountability, and ethical management, corporate governance can significantly influence profitability of Islamic commercial banks.[25] Accordingly, various considerable studies have been carried out with the aim of exploring the impact of FDR on profitability, each producing either mixed or inconclusive results. This uncertainty

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[15] Septi A Mulyana And Wirman Wirman, "Pengaruh Non Performing Financing (NPF) Dan Financing To Deposit Ratio (FDR) Terhadap Profitabilitas," *Al-Kharaj Jurnal Ekonomi Keuangan & Bisnis Syariah* 5, no. 3.

[16] Sutrisno, "Financing Scheme and Determinant Factors," (2022): 18.

[17] Mokhammad Ridho, "Does Non-Performing Financing And Capital Adequacy Impact Profitability Of Islamic Banks In Indonesia?," (2023): 160.

[18] Taufikur Rahman And Khusna Fatmawati, "The Influence Of Financial Ratios On Non Performing Financing Of The Sharia Rural Banks Of Special Region Of Yogyakarta (BPRS DIY) Period 2015 – 2018," *Asian Journal Of Islamic Management (AJIM)* 2, no. 1 (2020): 25.

[19] Faaza Fakhrunnas, Riska D Astuti, And M B H Anto, "Determinants Of Non-Performing Financing In Indonesian Islamic Banks: A Regional And Sectoral Analysis," *Banks And Bank Systems* 17, no. 4 (2022).

[20] Ismail Nura, Nurlaila Nurlaila, And Marliyah Marliyah, "Pengaruh CAR, BOPO, FDR Dan NPF Terhadap Tingkat Bagi Hasil Mudharabah Dimediasi ROA Di Bank Umum Syariah Indonesia," *Owner* 7, no. 1 (2023): 908.

[21] Abul Hassan, M Sadiq Sohail, And Md Mahfuzur Rahaman Munshi, "Sharīʿah Governance And Agency Dynamics Of Islamic Banking Operations In The Kingdom Of Saudi Arabia," *ISRA International Journal Of Islamic Finance* 14, no. 1 (2022): 89.

[22] Monica V Achim, Sorin N Borlea, And Codruţa Mare, "Corporate Governance And Business Performance: Evidence For The Romanian Economy," *Journal Of Business Economics And Management* 17, no. 3 (2015): 458.

[23] Alex Abugri, "Effect of Corporate Governance.

[24] Darwanto And Anis Chariri, "Corporate Governance And Financial Performance In Islamic Banks: The Role Of The Sharia Supervisory Board In Multiple-Layer Management," *Banks And Bank Systems* 14, no. 4 (2019).

[25] Muhammad Ishtiaq And Hina Mushtaq, "Corporate Governance Regulations And Practices Under COVID-19 Crisis: Time To Rethink," *Journal Of Law & Social Studies* 3, no. 2 (2021): 153.

invariably emphasizes the need for further explorations to better comprehend the manner in which FDR factually influences profitability, specifically when considered in a broader context such as Good Corporate Governance (GCG).[26]

Previous studies have extensively explored the relationship between FDR and bank profitability, and emphasized its important role in liquidity management and financial stability.[27] However, there remains a gap in understanding how corporate governance practices mediate this relationship in the context of Islamic banking. This study adds novelty to the existing body of knowledge by analyzing the mediation effect of GCG between FDR and ROA, a topic that has not been widely explored in previous studies. GCG has been explored to play an essential role in profitability of Islamic banks, but no investigations have been made into how the variable might mediate the relationship between FDR and ROA.[28] As a result, this study focuses on the context of Sharia economics in Indonesia, which has unique characteristics and has not been widely discussed in international publications. The focus in this context is particularly important because while corporate governance is known to enhance financial performance, its specific impact as an intervening variable between FDR and profitability in Sharia-compliant banks has not been thoroughly investigated.[29] The majority of existing studies have also been observed to primarily focus on conventional banking systems, with limited explorations addressing the unique operational and ethical frameworks of Islamic banks.[30] The relationship between Sharia principles, corporate governance, and financial performance presents a distinct area that requires deeper exploration.[31] Furthermore, the dynamic nature of corporate governance practices alongside respective adaptability to market conditions, particularly in novel economies such as Indonesia, remains underexplored.[32]

This present study essentially addresses existing gaps by examining the impact of FDR on profitability of Islamic commercial banks in Indonesia, with a specific focus on the mediating role of GCG. The objectives include analyzing how FDR affects profitability, evaluating GCG as an intervening variable, identifying key factors influencing profitability, and offering recommendations to enhance profitability through effective financing and governance practices.

[26] Anafil Windriya, "Macroeconomic Sensitivity And Financial Performance On Islamic Banks Profitability," *Jurnal Ilmiah Ekonomi Islam* 9, no. 2 (2023): 2620.

[27] Ahmad I Rahmansyah, Nasya S Balqis, Yekti Rahajeng, Muhammad S H Elmas, And Siti Masluha, "The Effect Of Non Perfoming Financing.

[28] Nabila F Iman And Umiyati Umiyati, "Analisis Determinan Atas Profitabilitas Bank Syariah Di Indonesia," *Jurnal Akuntansi Dan Keuangan Islam* 10, no. 1 (2022): 31.

[29] Muhammad S Shahid And Usman Shahid, "CEO Overconfidence And Corporate.

[30] Shaleh Yudiansyah, Srinita, Suriani, And Eddy Gunawan, "Does Sharia Banking Have The Capability To Increase Micro, Small And Medium Enterprises Financing?," *International Journal Of Finance Economics And Business* 1, no. 4 (2022): 250.

[31] Rendra A Hidayat, Indah Shofiyah, And Hendra Hendra, "Comparative Analysis Of The Performance Of Sharia Banks And Conventional Banks In Indonesia," *Akrual Jurnal Akuntansi* 13, no. 2 (2022): 251.

[32] Bridget Mcnally And Thomas O'Connor, "The Corporate Governance Lifecycle In Emerging Markets The Case Of The Republic Of Korea," *Corporate Governance* 23, no. 5 (2023): 1046.

Methods

This present study aims to examine the impact of FDR on profitability of Indonesian Islamic commercial banks, with a specific focus on Islamic financial institutions registered with Bank Indonesia from 2015 to 2019. The study methodology was structured in several key stages to ensure clarity and reproducibility. These stages include data collection, sampling procedure, data validation, variable measurement, statistical analysis, and hypothesis testing. Accordingly, secondary data was sourced from the annual financial statements of Islamic commercial banks and OJK Annual Reports. It is also important to state that the selection of banks and relevant data points was based on purposive sampling. This ensured that only banks with complete data across the variables of interest were included in the study. The summary of the sampling results is presented in Table 2.

Table 2. Sampling Results

Bank Criteria	Quantity
BUS registered with OJK during the period 2015-2019	14
Number of samples that meet the criteria	8
Banks that have complete data based on the variables to be studied	8
Years of observation	5

Source: Author's Calculation 2024

The sample preparation included a rigorous process of data collection and validation to ensure accuracy and completeness. Data were gathered through the documentation method, which comprised reviewing relevant literature, studies, and financial reports available on the official websites of Islamic commercial banks included in the study. Following this, the set of data extracted from the annual financial statements available on the official websites were cross-referenced with OJK Annual Reports to ensure consistency. The experimental setup comprised performing a series of statistical analyses to test the hypotheses and the primary variable of interest, FDR, was calculated using the formula:

FDR = (Total Financing/Total Deposits) x 100

Profitability was measured using Return on Assets (ROA), calculated as:

ROA = (Net Profit/Total Assets) x 100

Corporate governance was assessed using a comprehensive set of disclosure items, as presented in Table 3. Corporate governance score of each bank was calculated based on these disclosures, with GCG Index calculated as:

GCG = (Total Score Disclosed)/(Maximum Score) x 100

Table 3. Disclosure of Corporate Governance Items

Disclosure Items
Sharia Commercial Banks
Corporate Governance Self-Assessment
Share Ownership >5% of Paid-Up Capital

Disclosure Items
Board of Commissioners
Board of Directors
Financial Relationships (Board Members, Controlling Shareholders, Commissioners, Direct
Family Ties (Board Members, Controlling Shareholders, Commissioners, Directors)
Concurrent Roles (Board of Commissioners)
Sharia Supervisory Boards
Committee Structure and Expertise
Consultants/Advisors Disclosure (Name, Purpose, Scope)
Remuneration Policy (Board of Commissioners, Board of Directors, Sharia Supervisory)
High-To-Low Pay Ratio
Board of Commissioners Meetings (Frequency, Attendance)
Sharia Supervisory Board Meetings (Frequency, Attendance)
Internal Frauds and Resolutions
Legal Issues And Resolutions (Civil, Criminal)
Interest-Laden Deals
Buyback of Bonds/Shares
Social Fund Distribution
Non-Halal Revenue Usage
Sharia Commercial Banks
Corporate Governance Self-Assessment
Share Ownership >5% of Paid-Up Capital
Board of Commissioners
Board of Directors
Financial Relationships (Board Members, Controlling Shareholders, Commissioners)
Family Ties (Board Members, Controlling Shareholders, Commissioners, Directors)
Concurrent Roles (Board of Commissioners)
Sharia Supervisory Boards
Committee Structure and Expertise
Consultants/Advisors Disclosure (Name, Purpose, Scope)

Source: Sofana et al. 2021

The primary parameters measured in this study include FDR, ROA, and GCG index. FDR represents the ratio of total financing provided by the bank to the total deposits received, signifying the liquidity and risk levels of the bank.[33] ROA measures the bank profitability relative to its total assets, thereby providing insight into its financial performance.[34] Meanwhile, GCG index, calculated based on a comprehensive set of governance disclosures, evaluates the quality of corporate governance practices in the banks.[35]

[33] Lucky Nugroho, Ahmad Badawi, Erik Nugraha, And Yananto M Putra, "What Determines Islamic.

[34] Cathy Ismantara And Irwanto Handojo, "Factors Affecting Firm Value With Capital Structure As Intervening Variable," *Media Bisnis* 14, no. 1 (2022): 9.

[35] Nida Ulya Sofana, Faris Shalahuddin Zakiy, Muchammad Fauzi, Singgih Muheramtohadi, And Najim Nur Fauziah, "The Effect Of Sharia Share Selection Based On Financial Ratio And Corporate Governance Mechanism On The Quality Of Company Profit," *Journal Of Islamic Accounting And Finance Research* 3, no. 2 (2021): 241.

The statistical analysis comprised several steps to test the hypotheses. Descriptive statistics and correlation analysis were performed to understand the relationships between FDR, ROA, and GCG. Regression analysis was conducted using SPSS software to test the direct impact of FDR on ROA. Subsequently, mediation analysis was performed using the Sobel test to determine if GCG acted as an intervening variable between FDR and ROA.

Result and Discussion

Descriptive Statistics

The dataset analysis results, as presented in Table 4, show the mean and standard deviation values for FDR, ROA, and GCG. The obtained mean FDR is approximately 85.185 with a standard deviation of 7.597, suggesting moderate variability in financing activities relative to deposits among the banks. ROA had a mean of approximately 0.814 and a standard deviation of 0.598, signifying that profitability levels were relatively low. GCG showed a mean of approximately 95.754 with a standard deviation of 8.153, reflecting consistent governance practices across the sample.

Table 4. Descriptive statistics

	N	Minimum	Maximum	Mean	Std. Deviation
FDR	37	71.87	98.46	85.185	7.597
CG	37	57.15	100.00	95.754	8.153
ROA	37	0.05	2.63	0.814	0.598
Valid N (listwise)	37				

Source: SPSS, Data Processed by the Authors

Correlation Matrix

Correlation matrix, as presented in Table 5, shows the relationships between the study variables. The correlation between FDR and ROA is 0.146, implying a weak positive relationship. The correlation between FDR and GCG is -0.123, suggesting a weak negative relationship. Finally, the correlation between ROA and GCG is -0.164, also signifying a weak negative relationship. The correlation results suggested that higher FDR was slightly associated with increased profitability, though the relationship is minimal. It also emphasizes how higher FDR is weakly related to lower GCG scores and better corporate governance is weakly associated with reduced profitability.

Table 5. Correlation Matrix

	FDR	GCG	ROA
FDR	1.000	-0.123	0.146
GCG	-0.123	1.000	-0.164
ROA	0.146	-0.164	1.000

Source: SPSS, Data Processed by the Authors

Regression Analysis

The subsequent procedure comprised testing the classical assumptions, including heteroscedasticity, multicollinearity, and correlation tests. Specifically, the multicollinearity test was applied only to regression equation 1 during the multiple regression analysis. In this study, the variables of FDR, corporate governance, and profitability were analyzed using multiple linear regression analysis with two equations:

(1) ROA = α + FDR + GCG + e

(2) CG = α + FDR + e

In general, regression analysis is typically carried out with the aim of determining the direction and strength of the relationship between dependent and independent variables in an equation. This analysis is validated through classical assumption tests. In the context of time series multiple linear regression analysis, these standard tests include assessments for autocorrelation, multicollinearity, and normality. After evaluating the classical assumptions, regression analysis was performed on equations 1 and 2, with the results provided in Tables 6 and 7.

Table 6. Regression Test Results Equation 1

ROA = α + β_{1b} FDR + β_{2b} GCG + e			
Variable	Coeff	t - Stat	Prob.
const	0.997398	0.572591	0.570689
FDR	0.010047	0.7554	0.455211
GCG	-0.010853	-0.875636	0.387373
Adjusted R-squared	-0,013401		
F – statistic	0.761968		
R- squared	0.042899		

Source: SPSS, Data Processed by the Authors

The regression analysis results of Equation 1 (Table 6) show that the significance value of the impact of FDR on ROA is 0.570689. Since 0.570689 > 0.05, the null hypothesis (Ho) was rejected, implying that FDR did not significantly affect ROA. This result support hypothesis 1, also resulting in its rejection. Accordingly, R Square value signified that FDR contributed 4% to ROA. From an Agency Theory perspective, this weak positive relationship suggests how the principals (bank owners) and agents (bank managers) might be prioritizing conservative financial decisions, thereby limiting the potential impact of FDR on profitability.[36]

The results of this study differ from previous explorations, which have typically emphasized the significant impact of FDR on profitability. For instance, Rivandi and Gusmariza (2021) and Mulyana and Wirman (2022) suggested a negative impact of a

[36] Mohd Haniff Zainuldin, Tze Kiat Lui, And Kwang Jing Yii, "Principal-Agent Relationship Issues In Islamic Banks: A View Of Islamic Ethical System," *International Journal Of Islamic And Middle Eastern Finance And Management* 11, no. 2 (2018): 297.

higher FDR on profitability due to increased liquidity risks.[37] However, the results of this study show the presence of a weak positive and statistically insignificant relationship, which may reflect the unique characteristics of Indonesian Islamic banking sector.[38]

Table 7. Regression Test Results Equation 2

$GCG = \alpha + \beta_{1b}\ FDR + e$			
Variable	Coeff	t - Stat	Prob.
const	107.041005	6.954016	0.000000
FDR	-0.132495	-0.736081	0.466586
Adjusted R-squared	-0.012891		
F – statistic	0.541815		
R- squared	0.015244		

Source: SPSS, Data Processed by the Authors

The regression analysis results of Equation 2 (Table 7) show that the significance value of the influence of FDR on GCG is 0.000. Since 0.000 < 0.05, FDR was concluded to significantly affect GCG. However, in regression Equation 1 (Table 6), the significance value of FDR on GCG is 0.570689. Considering that 0.570689 > 0.05, suggesting that GCG did not mediate the effect of FDR on ROA. The obtained coefficient of determination is 0.015, implying that the combined influence of FDR and GCG on the ROA variable is 1%. In accordance with Signaling Theory, while FDR might serve as a signal of the financing capacity of the bank, its negative relationship with GCG suggests that a higher FDR might be perceived as a risk by stakeholders, potentially leading to lower governance scores.

The mediation hypothesis was tested using the Sobel test, which assessed the strength of the indirect effect of FDR on ROA through GCG. The results of this mediation test are as follows:

Table 8. Intervening Variable Effect Test Results

Variable	Indirect effect	Sobel Test Statistic	p-value
GCG	-0.001433	-0.738630	0.460227

Source: SPSS, Data Processed by the Authors

These results suggest that the indirect effect of FDR on ROA through GCG is not significant, with a p-value exceeding 0.05. Based on the observations made, the mediation coefficient was considered insignificant, signifying no mediation effect. Sequentially, the hypothesis testing result confirmed that FDR had a direct impact on ROA but did not have any indirect influence through GCG. This implied that GCG could not elucidate the indirect relationship between FDR and ROA, leading to the rejection of hypothesis 2. These results

[37] Muhammad Rivandi and Tania Gusmariza, "Pengaruh Financing to Deposit Ratio, Capital Adequacy Ratio Dan Non Performing Financing Terhadap Profitabilitas Pada Bank Umum Syariah," *Owner* 5, no. 2 (2021): 473; Septi A Mulyana And Wirman Wirman, "Pengaruh Non Performing Financing.

[38] Taufikur Rahman And Khusna Fatmawati, "The Influence Of Financial Ratios.

challenge the conventional view that strong governance practices universally enhance financial performance by mitigating agency conflicts.

The negative correlation between FDR and GCG observed in this study is not in line with Shahid and Shahid (2020), who reported how effective corporate governance enhanced financial performance by mitigating risks.[39] This discrepancy, according to another study, was due to the distinct governance frameworks and Sharia compliance requirements in Islamic banking, which can influence the efficacy of traditional governance practices.[40] Furthermore, the weak and statistically insignificant impact of FDR on ROA challenges conventional theories that emphasize the direct positive relationship between financing activities and profitability. This suggests that other factors, potentially unique to the operational environment and regulatory landscape of Islamic banks in Indonesia, may play a more significant role. [41]

The observations made during the course of this study further showed that there was no significant mediating effect of GCG on the relationship between FDR and ROA. This is not in correspondence with the results of Sofana et al. (2021), which emphasized the role of strong corporate governance in enhancing financial performance by reducing agency conflicts and ensuring better management practices.[42] Meanwhile, the negative correlation between FDR and GCG, even though weak, suggested that higher financing ratios may be associated with lower governance scores, reflecting potential governance challenges in managing higher levels of financing. These results have significant implications for Islamic commercial banks in Indonesia. The weak and statistically insignificant relationship between FDR and profitability signifies that Islamic banks may need to adopt more comprehensive and effective strategies in managing respective FDR in order to avoid liquidity issues without compromising profitability. This invariably shows the importance of conservative financing strategies that are in line with the risk-averse nature of Sharia-compliant banking. [43]

The lack of a significant mediating effect of corporate governance on the relationship between FDR and profitability signifies the need for Islamic banks to strengthen respective governance frameworks. Given the ethical and operational requirements specific to Islamic banking, specifically designed governance practices that incorporate Sharia principles and promote transparency and accountability are essential.[44] Essentially, enhancing governance mechanisms could mitigate risks and improve overall financial performance.

For policymakers and bank managers, comprehensively understanding the relationship between financing ratios, governance, and profitability is very important. This knowledge can inform the development of effective strategies to enhance financial

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[39] Muhammad S Shahid And Usman Shahid, "CEO Overconfidence And Corporate.

[40] Darwanto And Anis Chariri, "Corporate Governance And Financial.

[41] Shaleh Yudiansyah, Srinita, Suriani, And Eddy Gunawan, "Does Sharia Banking.

[42] Nida Ulya Sofana, Faris Shalahuddin Zakiy, Muchammad Fauzi, Singgih Muheramtohadi, And Najim Nur Fauziah, "The Effect of Sharia Share.

[43] Ahmad I Rahmansyah, Nasya S Balqis, Yekti Rahajeng, Muhammad S H Elmas, And Siti Masluha, "The Effect Of Non Perfoming Financing.

[44] Muhammad S Shahid And Usman Shahid, "CEO Overconfidence And Corporate; Alex Abugri, "Effect of Corporate Governance.

performance while adhering to Sharia principles. Additionally, the results contribute to the broader discourse on Islamic banking by offering evidence-based recommendations for optimizing financing strategies and strengthening corporate governance frameworks.[45] Incorporating insights from agency theory and signaling theory can further refine governance practices by emphasizing the importance of corresponding to the interests of principals and agents to ensure transparency, accountability, and ethical conduct in financial activities.[46] As stated in a previous study, signaling theory emphasizes the role of governance and financial disclosures in enhancing investor confidence and market perceptions.[47] By integrating these theoretical perspectives, Islamic banks can develop comprehensive governance structures that support sustainable profitability and stakeholder trust.

Conclusion

In conclusion, the impact of FDR on profitability of Indonesian Islamic commercial banks was examined during the course of this study, with the consideration that GCG would serve as a possible mediator. The results showed that FDR did not significantly affect profitability (measured by ROA) and GCG did not mediate the relationship between the dependent and independent variables, thereby challenging previous study. Accordingly, the results also suggests that other factors may be more important in determining profitability in Islamic banks. This was evidenced by the weak negative correlation observed between FDR and GCG, which raised concerns about the effectiveness of current governance practices. Several limitations were observed to be associated with this present study, including a narrowed focus on 2015-2019 data, a limited sample of Indonesian banks, reliance on secondary data, and the exclusion of other influential factors such as macroeconomic conditions. This study calls for broader future explorations incorporating more variables and alternative theoretical perspectives to better understand profitability in Islamic banking. It also recommends more conservative financing strategies and improved governance frameworks that correspond with Sharia principles, enhance transparency, and maintain profitability.

Acknowledgments

The authors are grateful to the observed universities for the invaluable support in various capacities, as well as to the entire team for the dedication to discussions and idea exchanges, which have significantly contributed to the refinement of this manuscript and the sourcing of relevant internationally reputable articles. Furthermore, the authors are also grateful to Professor Rudi Zulfikar from Universitas Sultan Ageng Tirtayasa, Banten, for his willingness to review this work and provide constructive feedback.

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Author Contribution Statement

TW contributed as the originator of the idea and the primary author of this manuscript. FU structured the manuscript, established fundamental theories, analyzed data, and discussed study results. NS contributed as a collaborator by sharing ideas, engaging in discussions, and assisting in locating references. Additionally, NS and FU served as reviewers, enhancing and refining the manuscript.

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