Micro, Small and Medium Enterprises Financing of Islamic Banking in Indonesia During The Covid-19 Pandemic

Ernawati[*1], Tajuddin[2], Mansyur Asri[3]

[1] Economics and Development Studies Department, Halu Oleo University, Kendari, Indonesia
[2] Economics and Development Studies Department, Halu Oleo University, Kendari, Indonesia
[3] Information Systems Department, STMIK Catur Sakti, Kendari, Indonesia
*ernawaty@uho.ac.id

Abstract

Introduction: Share of Micro, Small, and Medium Enterprises (MSMEs) financing in Islamic banking is still limited, however during the Covid-19 pandemic, the share of MSME financing had increased when the Indonesian economy contracted.

Purpose: This study aims to analyze the allocation of MSMEs financing of Islamic banking in Indonesia during the Covid-19 pandemic and determinants of MSME financing allocation.

Methodology: Research data is secondary data obtained from the Indonesian Islamic Banking Statistics, published by the Indonesian Financial Services Authority (OJK), for the 2015-2020 monthly period. The estimated Islamic banking consists of 3 types: Sharia Commercial Banks, Sharia Business Units, and Sharia Rural Banks. The independent variables tested were asset growth, non-performing MSMEs financing (NPF), profit rate, and two dummy variables, namely the threshold for NPF and the Covid-19 pandemic period. Data analysis using panel data regression.

Findings: The results showed that the NPF MSMEs variable, profit rate, and dummy pandemic period have a significant effect on MSME financing of Islamic banking in Indonesia, while the asset growth and dummy threshold NPF are not substantial. An increase in NPF will reduce the allocation of MSME financing, but an increase in profit will encourage an increase in the percentage of MSME financing. The percentage of MSME financing during the Covid-19 pandemic was higher than in the previous period. This implies that Islamic banking also contributed to national economic recovery.

Paper Type: Research Article
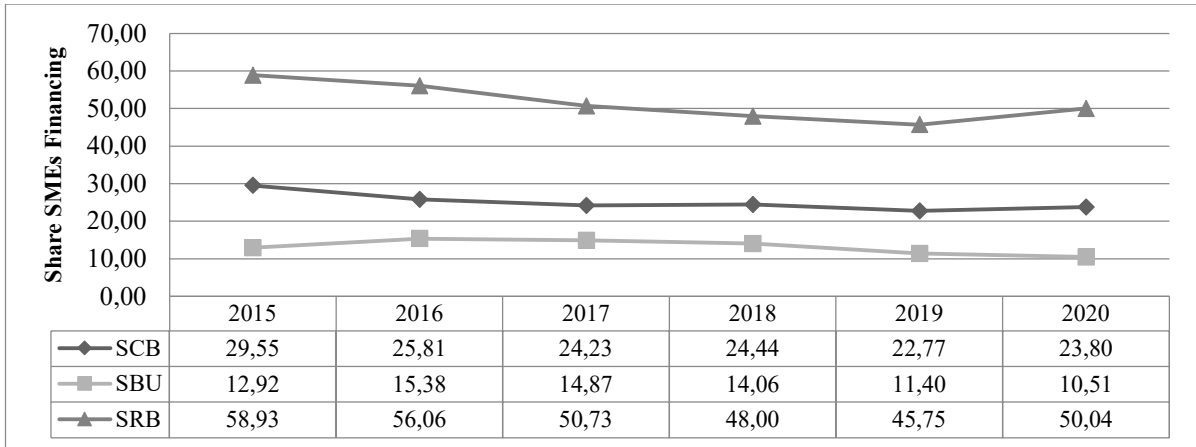**Keywords:** financing; MSMEs; Islamic; banking; Covid-19

Introduction

The Covid-19 pandemic has reduced economic activity in Indonesia. Indonesia's economic contraction in 2020 was 2.07, while in 2019, Indonesia experienced growth of 5.02 percent. The most profound economic contraction was shared by the Transportation and Warehousing sector with an increase of -15.04 percent; and the Provision of Accommodation, Food and Drink sector grew by -10.22 percent (BPS, 2021a). Economic contraction indicates a decrease in people's income and creates new poor people. The poverty rate in September 2020 was 10.19 percent, an increase of 0.41 percentage points against March 2020 and an increase of 0.97 percentage points against September 2019. The number of poor people in September 2020 was 27.55 million people, increasing 2.76 million against September 2019 (BPS, 2021b).

The COVID-19 pandemic has had an impact on both consumers and producers. The impact of the 1997 economic crisis was different from the impact of the Covid-19 pandemic on producers, where the 1997 economic crisis most impact large businesses. Still, during the Covid-19 pandemic, also affected MSMEs. A survey of 3,136 MSMEs showed that 80 percent of micro-businesses experienced a decline in sales turnover, while small businesses experienced a decrease of 82 percent and medium businesses by 83 percent (OJK & BCG, 2020). Several programs implemented in the context of National Economic Recovery specifically for MSMEs are cash assistance of 2.4 million rupiahs per MSME with a funding target of 22 trillion rupiahs, cooperative investment financing of 1 trillion rupiahs, placement of low-interest funds of 52.3 trillion rupiahs, interest subsidies 7.7 trillion rupiahs, MSME loan guarantees of 6 trillion rupiahs, and the MSME Final Income Tax subsidy of 2.4 trillion rupiahs (BI, 2021). Banking participation in the national economic recovery program is in the fund placement program, interest subsidies, and credit guarantees. The economic program launched during the pandemic is expected to help MSMEs to survive. Moreover, the Central Bank of Indonesia has encouraged efforts to strengthen MSME financing access, both from the supply and demand sides. The Central Bank of Indonesia has set a minimum MSME Credit Ratio Policy of 20 percent as stated in PBI No. 17/12/PBI/2015 to improve access to financing or credit for MSMEs in the banking sector Islamic banking.

Islamic banking in Indonesia consists of Sharia Banks and Sharia Rural Banks (SRB). The main difference is that Sharia Rural Banks are prohibited from accepting deposits in demand deposits and prohibited from participating in payment system traffic. Institutionally, there are Islamic commercial banks in full-fledged Islamic banks or Sharia Commercial Banks (SCB) and Sharia Business Units (SBU) of conventional commercial banks. The development of MSME financing in Islamic banking in 2015-2020 (on a monthly average) in the three groups is presented as Figure 1 shows that Islamic banking has a low motivation towards the allocation of MSME financing as indicated by the expected share of MSME financing in the Sharia Commercial Banks group and Sharia Business Units. There was a decrease in the percentage of MSME financing from 2016 to 2019. Still, in 2020 there was an increase in the share of MSME financing in the Sharia Commercial Banks and Sharia Rural Banks groups, while the MSME financing share in the Sharia Business Units group continued to decline. The MSME financing ratio in the Sharia Business Units group is also not in line with the minimum credit ratio as the Central Bank of Indonesia regulations.

Figure 1. Share SMEs Financing Based on Islamic Bank Group 2015-2020

	2015	2016	2017	2018	2019	2020
SCB	29,55	25,81	24,23	24,44	22,77	23,80
SBU	12,92	15,38	14,87	14,06	11,40	10,51
SRB	58,93	56,06	50,73	48,00	45,75	50,04

Source: OJK (2021), processed

The allocation of MSME financing, which generally has a downward trend until 2019, shows the low willingness of Islamic banks to allocate MSME financing, driven by various factors. The determinant of MSME financing allocation is credit risk in the micro and small business groups. Credit or financing risk is reflected by non-performing financing (NPF). The Central Bank of Indonesia has set 5 percent as the NPF threshold. In comparison, the average non-performing financing for MSME financing in Islamic banking based on OJK data for the 2020 period is greater than 5 percent or riskier. Several research findings show that NPF has a significant effect on allocating financing or credit for MSMEs (Ratnasari, 2016; Prihartini & Dana, 2018; Anis et al., 2020).

On the other hand, the allocation of bank financing on the supply side is determined by the bank size, where smaller banks provide more credit to MSMEs than larger banks. (Rahman et al., 2016). However, the findings in conventional banks have not been justified in the case of Islamic banks. Furthermore, the higher the profit level will also increase financing (Barus & Lu, 2013; Handayani, 2018). Profit is one form of equity, will be used in business operations. However, during the pandemic, the economy experienced a contraction which affected the allocation of financing. When the economy is expansionary, banking profits increase (Amzal, 2016), then the percentage of financing increases, otherwise if it is contractionary. The Covid-19 pandemic will naturally reduce the allocation of MSME financing that has a high risk. However, access to MSME financing in 2020 in Islamic banks experienced an increase in the share of total financing compared to the previous period. It is necessary to study whether inferentially the allocation of MSME financing in Islamic banking tends to increase during the pandemic period and play a role in national economic recovery. This study also examines the determinants of MSME financing allocation in Islamic banking. This research is expected to contribute to the development of the role of Islamic banking during a crisis when the economy experiences uncertainty. This research is also expected to be a consideration in making policies related to the participation of Islamic banking in the Indonesian economy.

Methodology

This research is a correlational and causal-comparative study. The researcher describes the condition of MSME financing allocation in a quantitative context reflected in the variables and then examines the determinants of MSME financing allocation. Some of the estimated comparisons are based on bank group, NPF threshold, and pandemic period. Research data is secondary data from the Islamic Banking Statistical Document, published by the Indonesian Financial Services Authority, 2015-2020 monthly. The estimated Islamic banking consists of three types: Sharia Commercial Banks, Sharia

Business Units, and Sharia Rural Banks. The independent variables tested were asset growth, non-performing SMEs financing, profit rate, and the dummy variable threshold for non-performing financing, as well as the dummy for the Covid-19 pandemic period. The data were analyzed using panel data regression which was processed with Eviews. The initial panel data regression model is presented as equation (1), where Y_{it} is the dependent variable, X_{it} is the independent variable, i and t indicate individual, and time is the cross-section error.

$$Y_{it} = \alpha + \beta_1 X_{1it} + \beta_2 X_{2it} + \cdots + \beta_n X_{nit} + e_{it} \qquad (1)$$

Research Model:

$$Y_{it} = \alpha_0 + \alpha_1 X_{1it} + \alpha_2 X_{2it} + \alpha_3 X_{3it} + \alpha_4 D_{1it} + \beta_5 D_{2it} + \mu_{1it} \qquad (2)$$

MSME financing (Y) is the total MSME financing (log), asset growth (X_1) is the growth in total Islamic banking assets (%). Non-performing financing (X_2) is the percentage of non-performing financing to complete financing of MSMEs. The profit rate of Islamic banking (X_3) is measured by return on assets (ROA). The non-performing financing threshold variable (D_1) is the NPF limit set by the Central Bank of Indonesia at 5 percent, given a score of 1 if NPF ≤ 5 and 0 if NPF > 5. Dummy period of pandemic (D_2) is scored with one if during the pandemic period (April-December 2020) and scored with 0 for the others. The research hypotheses are:

H1.1	:	Asset growth has a significant effect on the allocation of MSME financing.
H1.2	:	Non-performing financing of MSME financing has a significant effect on the allocation of MSME financing.
H1.3	:	The level of profit has a significant effect on the allocation of MSME financing.
H1.4	:	There is a significant difference in the allocation of MSME financing based on the NPF threshold set by the Central Bank of Indonesia.
H1.5	:	There are differences in the allocation of MSME financing during the pandemic and before the Covid-19 pandemic.

The Chow test is used to determine the best model between the standard effect model (CEM) or fixed effect model (FEM) with the chi^2 probability criterion from cross-section data. The probability of chi^2<0.05, the best model chosen is FEM, and CEM otherwise. In this study, no tests were conducted to determine the best model between FEM and the random effect model (REM) or Hausman test because the number of cross-sections of the study is smaller than the number of coefficients for between estimators to estimate RE innovation variance. The estimation of the research equation using the fixed-effect model will show the difference in the cut-off point between banks or the autonomy of MSME financing between SCB, SBU, and SRB. Thus hypothesis 6 is proposed, that:

H1.6	:	There are differences in the allocation of MSME financing as a result of differences in bank size.

Results and Discussion
Description of research variables

The descriptive statistics of the research variables presented in Table 1 show that in terms of total financing (log), the amount of financing allocation for SMEs in the Sharia Rural Banks group is lower than for other groups. However, as Figure 1 shows, the share of MSME financing allocations in the Sharia Rural Banks reaches around 50 percent of the total financing allocation.

Table 1. Descriptive Statistics of Research Variables

| Type of Bank	Descriptive	SMEs Financing	Assets Growth	NPF	Profit Rate
SCB	Max	13.814	11.612	9.706	1.875
	Min	13.552	-3.696	4.166	0.162
	Mean	13.667	0.945	6.296	1.080
	Stdev	0.053	2.160	1.414	0.433
SBU	Max	13.241	10.487	13.316	2.818
	Min	12.783	-6.694	4.346	1.680
	Mean	13.055	1.559	7.962	2.198
	Stdev	0.118	3.491	2.885	0.269
SRB	Max	12.790	4.329	17.816	2.734
	Min	12.479	-2.919	8.451	1.730
	Mean	12.608	1.155	13.228	2.347
	Stdev	0.083	1.212	2.314	0.179
Total	Max	13.814	11.612	17.816	2.818
	Min	12.479	-6.694	4.166	0.162
	Mean	13.110	1.220	9.162	1.875
	Stdev	0.444	2.473	3.735	0.646

Source: OJK (2021), processed

The portion of MSME financing in the Sharia Commercial Banks group is 25 percent, and in the Sharia Business Units group, about 13 percent. The low amount of MSME financing in Sharia Rural Banks is due to limited assets or funds. Comparison of the contribution of total assets of each bank group from data of the Indonesian Financial Services Authority (OJK) in December 2020 shows that the share of Sharia Rural Banks assets to total assets of Islamic banking is around 2.5 percent; while the contribution of Sharia Business Units assets is 32.33 percent; and Sharia Commercial Banks more than 65 percent.

The Sharia Business Units group has the highest average asset growth than the Sharia Rural Banks. The highest NPF is experienced by the Sharia Rural Banks group, with achievement of 17.816 percent. Meanwhile, the highest NPF in the Sharia Business Units group was 13.316 percent, and the highest NPF for the Sharia Commercial Banks bank group was 9.706 percent. The Sharia Commercial Banks

group also has the lowest NPF achievement of 4.166 percent. This implies that larger banks are better than smaller banks in controlling NPF. However, based on the mean and standard deviation values, the Sharia Rural Banks group produces a higher and more stable average profit than the two other larger bank groups. Based on the pandemic period, as Figure 2 shows, the profit rate of Islamic banking from April until December 2020 as measured by return on assets (ROA) is in a positive trend even though it is slowing down. Profit rate growth is still profitable for Islamic banking for financing expansion during the pandemic.

Figure 2. Return on Assets by Islamic Bank Group 2015-2020
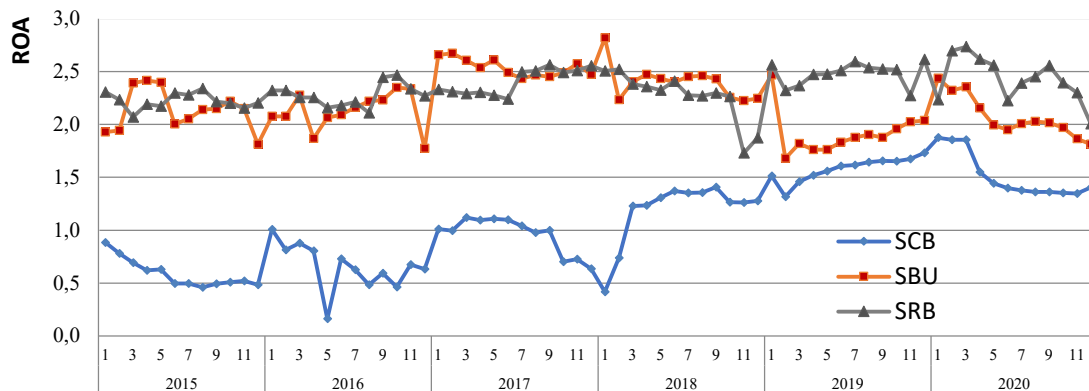
Source: OJK 2021, processed

Estimated Results

Panel data regression testing was conducted to select the best model between FEM and CEM. Table 2 presents the Chow Test, which shows the probability of a chi-square cross-section of 0.000 < 0.05. Therefore the fixed effect model was chosen. The results of the classical assumption test show that the regression model has heteroscedastic and autocorrelation symptoms. Breusch-Pagan LM probability is 0.000 < 0.05 due to the cross-section dependence test showing that the regression model also has symptoms of cross-section dependence. The multicollinearity assumption test uses correlation criteria between research variables > 0.80. Table 3 indicates that all coefficient values between research variables are not more than 0.80, there is no symptom of multicollinearity between research variables. This study's estimation of FEM data uses a cross-section of SUR (seemingly unrelated regressions) to correct several ordinary least square assumptions.

Table 2. Chow Test

Effects Test	Statistic	d.f.	Prob.
Cross-section F	337.317	(2,208)	0.000
Cross-section Chi-square	312.200	2	0.000

Source: secondary data, processed

The correlation of several research variables, as shown in Table 3, shows a significant correlation. The variable non-performing financing (X_2) and the level of profit (X_3) have a negative and significant

correlation. Non-performing financing (X_2) also negatively correlates with the threshold and the allocation of MSME financing. On the other hand, the profit rate has a positive correlation with the percentage of MSME financing.

Table 3. Correlation Coefficient of Research Variables

Variable		X_1	X_2	X_3	D_1	D_2	Y
X_1	Correlation	1.000					
	Probability	-----					
X_2	Correlation	-0.057	1.000				
	Probability	0.403	-----				
X_3	Correlation	0.026	0.399	1.000			
	Probability	0.708	0.000	-----			
D_1	Correlation	0.093	-0.494	-0.006	1.000		
	Probability	0.174	0.000	0.931	-----		
D_2	Correlation	-0.002	0.047	0.027	0.205	1.000	
	Probability	0.982	0.493	0.689	0.003	-----	
Y	Correlation	-0.045	-0.744	-0.788	0.382	0.079	1.000
	Probability	0.507	0.000	0.000	0.000	0.245	-----

Source: secondary data, processed

The estimation results of the determinants of MSME financing in Islamic banking as shown in Table 4. The variables that affect the allocation of MSME financing (Y), namely non-performing financing (X_2), profit rates (X_3), and the pandemic period (D_2), while the asset growth (X_1), and the NPF threshold (D_1), are not significant. Thus, the research hypotheses H1.1 and H1.4 are rejected, while hypotheses H1.2, H1.3, and H1.5 are accepted. An increase of 1 percent of non-performing financing will reduce the allocation of MSME financing by 0.011 percent. An increase of 1 percent of the profit rate will increase 0.032 percent of the percentage of MSME financing. The dummy variable for the pandemic period (D_2) shows differences in the allocation of the funding in the period before and during the pandemic, with a positive coefficient value of 0.086. The measurement of the D_2 variable as a dummy variable is determined by a score of 1 in the pandemic period and 0 for others. The positive coefficient D_2 indicates that the allocation of MSME financing during the pandemic period is higher than in the non-pandemic period. The personal equations of the Islamic bank group are presented as follows:

$$Y_{SCB} = 13.689 - 0.001X_1 - 0.011X_2 + 0.032X_3 + 0.010D_1 + 0.086D_2 + e_{it} \qquad (3)$$

$$Y_{SBU} = 13.061 - 0.001X_1 - 0.011X_2 + 0.032X_3 + 0.010D_1 + 0.086D_2 + e_{it} \qquad (4)$$

$$Y_{SRB} = 12.670 - 0.001X_1 - 0.011X_2 + 0.032X_3 + 0.010D_1 + 0.086D_2 + e_{it} \qquad (5)$$

Equations (3), (4), and (5) show that there are differences in the slope of the regression model between groups of Islamic banks in Indonesia, where the Sharia Commercial Banks slope is higher than the other two groups of banks. Furthermore, the second-highest intersection point is the Sharia Business Units, and the last is the Sharia Rural Banks. This implies that the autonomy of MSME financing at Sharia Commercial Banks is higher than other bank groups. Thus, the research hypothesis H1.6 is accepted, where the higher the size of the bank, the higher the allocation of MSME financing in the Indonesian Islamic banks.

Table 4. Estimation Results

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	13.140	0.028	466.392	0.000
X_1	-0.001	0.001	-0.629	0.530
X_2	-0.011	0.002	-7.006	0.000
X_3	0.032	0.010	3.061	0.002
D_1	0.010	0.011	0.848	0.397
D_2	0.086	0.011	7.707	0.000
Cross-section fixed				
SCB		0.549		
SBU		-0.079		
SRB		-0.470		
R-squared	0.991	F-statistic		3216.647
Adjusted R-squared	0.991	Prob (F-statistic)		0.000

Source: secondary data, processed

Discussion

The research findings show that asset growth has no significant effect on allocating MSME financing in Islamic banks. The size of Islamic banks is still tiny or more significant does not affect the size of the allocation of MSME financing. The estimation of research variables shows that non-performing funding has a significant adverse effect on the percentage of the funding for MSMEs. An increase in non-performing financing will reduce the allocation of the funding for MSMEs. This study aligns with previous research (Handayani, 2018; Prihartini & Dana, 2018). There are three levels of non-performing financing, namely sub-standard, doubtful, and lost collectability. Sub-standard funding occurs when the debtor is in arrears in principal or profit-sharing between 91-120 days. Doubtful collectability if the debtor is in arrears in payment of principal or profit-sharing between 121-180 days. If the debtor is in arrears in payment of principal and/or profit-sharing for more than 180 days, lost collectability is lost. The share of non-performing collectability financing in December 2020 based on Indonesian Financial Services Authority data for the Sharia Rural Bank group was 67.52 percent. The high collectability of lost debts indicates the high risk of financing in Sharia Rural Banks. Whereas, in

general, the handling of non-performing funding is carried out by various financing restructuring steps, the risk of non-performing financing is still high.

The high collectability of non-performing financing in the Sharia Rural Bank group seems to be compensated by a higher profit level. Table 1 presents the average profit rate of the Sharia Rural Bank group for the 2015-2020 period of 2.347 percent, which is higher than the other two bank groups. The high level of profit will affect the allocation of MSME financing. The estimation results of the research variables show that the level of profit has a significant positive effect on the percentage of MSME financing, where an increase in profit will increase MSME financing, which is in line with previous research (Barus & Lu, 2013; Prihartini & Dana, 2018; Handayani, 2018). Profit is an addition to the bank's equity. When equity increases, the bank has additional funds to finance business operations, both for financing and other expenses. Profit is a cheap fund for banks because it comes from internal sources, does not have a cost, in contrast to third-party funds, which have rewards for using the funds. The increase in the profit of Islamic banks will increase the availability of unrestricted funds for Islamic banks to expand their business activities. Especially during the pandemic, using own capital will reduce the cost of profit-sharing for third parties. MSMEs that have slow business prospects can still be covered with relatively cheap financing. The effect of the pandemic period on the allocation of MSME financing to Islamic banks shows significant estimation results.

The allocation of MSME financing during the pandemic period is higher than in other periods. Naturally, the economic conditions improved, the percentage of the funding increased. If the general economic conditions decline, the allocation of financing will also decrease. Research findings show the opposite: the macroeconomy is experiencing a slowdown, but the percentage of MSME financing increases. The pandemic is one of the critical periods for MSMEs. Where is a pandemic that causes an economic contraction that has an impact on MSMEs SME owners face many operational and financial difficulties (Nawaiseh, 2021). Increasing access to Islamic banking finance during a pandemic will be a long-term solution for MSMEs to survive and get out of the crisis. Islamic bank financing has a positive influence on the performance of SMEs (Faisol, 2017; Purnamasari & Darmawan, 2017; Sabiu & Abduh, 2021). If Islamic bank financing increases, the performance of the SME increase. Furthermore, this shows that Islamic bank financing has a significant influence on the welfare of the SME sector.

Allocation of financing at Islamic banks and using sales contracts, profit-sharing contracts, and other contracts. The sales contract is a sale-purchase agreement between the bank and the customer. Islamic banks buy goods needed by customers and then sell them to the customer concerned at the acquisition price plus a profit margin agreed between the Islamic bank and the customer. Meanwhile, profit-loss sharing financing is financing carried out by Islamic banks by providing a certain amount of funds to the fund manager, and the operating results are divided based on an agreement. MSMEs access these two types of financing for both working capital and investment funds. The most suitable financing for MSMEs in a pandemic is profit-loss sharing financing. Profit-sharing financing practiced in Islamic banking in Indonesia is *mudharabah* and *musharakah. Mudharabah* financing is financing carried out by Islamic banks by providing 100 percent of business capital to fund managers (*mudharib*), while financing Musharaka is joint financing between Islamic banks and partners. Islamic banking tends to behave risk-averse (Ernawati, 2016), which is indicated by the high level of contract sales (*Murabaha*) financing, which has a fixed return compared to profit-sharing financing, which has fluctuating returns for banks. The share of *mudharabah* financing of Islamic banks (Sharia Commercial Banks & Sharia Business Units) of 3.09 percent of the total financing, while the Sharia Rural Banks is

2.44 percent (OJK, 2021). MSMEs have limited capital, the risk-averse behavior of Islamic banking is an obstacle in increasing MSME business. The bank can manage the risk of this profit-sharing financing. Because the profit-sharing system of Islamic banks has encouraged Small and Medium Enterprises to be more sustainable by reducing internal principal-agent problems where: if partners have a share of returns, then they will work hard to produce the expected returns, and as partners, if they have a sense of belonging encourages him to strive to maintain the growth of the company, so that the expected return and sense of ownership will promote the sustainability of Small and Medium Enterprises (Manzilati, 2015).

The MSME group consists of subsistence, potential, success, digital, and exports (BI, 2021). Subsistence MSMEs are MSMEs that receive social assistance and have business startups. Meanwhile, potential MSMEs are MSMEs that have prospective businesses but are still informal, have not separated financial records, limited production capacity, poor product quality, and are oriented to the local market, and still using the offline system. According to Bank Indonesia, successful MSMEs are MSMEs that have business licenses, record financial transactions, increase production scale, regional markets, and are feasible to finance. Digital MSMEs are MSMEs that use digital, online marketing, complete financial reports, certified/licensed products, and the national market. Export MSMEs are MSMEs that are characterized by: sustainability of productivity and product quality, passes curation, national/global markets, and has complete export documents, and environmentally friendly production. Thus, MSMEs that can access banking services are successful MSMEs and above with cash flow records as consideration for banks to receive financing.

Meanwhile, subsistence and potential MSMEs are still difficult to access financing services because they are unbankable. The efforts are needed to foster the unbankable MSMEs, especially for those affected by the Covid-19 pandemic. In addition to being carried out by the government, the development efforts can also be carried out by Islamic banking parties as fostered MSMEs, especially for banks that have more significant assets, or in this case, the Sharia Commercial Bank and Sharia Business Unit groups. Moreover, these two bank groups can perform social functions as recipients of social funds (*zakah, infaq, sadaqah*, and others), then distribute in fostering unbankable MSMEs. The social part of Islamic banking can improve people's welfare (Arumsari & Rikawati, 2020; Asiyah et al., 2019). This is also in line with research findings which show that the autonomy of MSME financing at Islamic commercial banks is higher than other bank groups. Autonomous funding shows that the allocation of MSME financing for Shariah commercial banks regardless of asset factors, NPF, profit rate, thresholds, and pandemic conditions are higher than other bank groups. This shows that the larger the size of the Islamic bank, the more it will provide access to financing for the MSME group. This finding is not in line with the previous study which showed that smaller bank groups would provide larger funds for MSMEs (Rahman et al., 2016).

Conclusion

The share of MSME financing allocation in Islamic banking experienced a downward trend in the period before Covid-19 but increases during the pandemic. The contribution of Islamic banking is needed to recover the national economy during the pandemic because the allocation of Islamic banking financing that uses profit-loss sharing shows risk sharing between banks and fund managers (MSMEs). Therefore, MSMEs have incentives to manage their businesses during the pandemic period, especially since the rate of return on MSME financing assets is still showing a positive trend, even though it is experiencing a slowdown so that it is still

profitable for banks to continue to expand financing during the pandemic. Based on the bank group, it appears that the share of MSME financing in the Sharia Rural Bank group is on average more than 50 percent. In contrast, in the Shariah Commercial Bank group, it is 25 percent, and the Shariah Business Unit is 13 percent. The high allocation of MSME financing to Sharia Rural Banks is also accompanied by a high NPF, where the NPF of Islamic banking, in general, has passed the 5 percent threshold. Based on the hypothesis test on the variables estimated as determinants of MSME financing, there is no difference in the expansion of MSME financing over the NPF threshold. Islamic banking will reduce MSME financing if the NPF increases, regardless of the threshold set by the Central Bank of Indonesia.

Furthermore, Islamic banking will continue to expand MSME financing in line with increasing profits. MSME financing during the pandemic period also showed significant differences with periods other than the pandemic, where MSME financing during the Covid-19 pandemic period was higher than different periods. This implies that Islamic banking will also contribute to helping MSMEs during the Covid-19 pandemic. This finding is a consideration for the government to involve Islamic banking in national economic recovery in the new normal era, especially Islamic banking has a social function in receiving and distributing social funds for MSMEs. This study has limitations because it only generalizes the total financing of MSMEs that the types of sales contract financing and profit-loss sharing financing have not been separated. This study has not estimated MSME financing by sector. There are sectoral differences in the business prospects of MSMEs during the Covid period, which affect the risk-averse behavior of Islamic banking. So that further researchers e estimate the determinants of MSME financing during the Covid-19 period based on the type of financing and the economic sector.

References

Amzal, C. (2016). The Impact of Macroeconomic Variables on Indonesia Islamic Banks Profitability. *Jurnal Ekonomi Dan Bisnis Islam*, *4*(1), 71–86. https://dx.doi.org/10.20473/jebis.v2i1.1968

Anis, A., Putra, H., & Putri, Y. (2020). Determinant of SMEs Credit in Indonesia: Intern vs. Extern Factor. Advances in Economics, Business and Management Research, Volume 152 Proceedings of the 5th Padang International Conference On Economics Education, Economics, Business and Management, Account. *Advances in Economics, Business and Management Research*, *152*, 195–208.

Arumsari, V., & Rikawati, R. (2020). Islamic Social Funds: Enabling The Unable To Be Able. *Journal of Applied Business Administration*, *4*(1), 88–97. https://doi.org/10.30871/jaba.v4i1.1902

Asiyah, B. N., Nasir, M., & Ahsan, M. (2019). The philanthropy of Islamic Banking: A Strategy In Strengthening The Economic Growth and Prosperity. *Share, Jurnal Ekonomi Dan Keuangan Islam*, *8*(2), 162–180. http://dx.doi.org/10.22373/share.v8i2.4842

Barus, A., & Lu, M. (2013). Pengaruh Spread Tingkat Suku Bunga dan Rasio Keuangan Terhadap Penyaluran Kredit UMKM Pada Bank Umum di Indonesia. *Jurnal Wira Ekonomi Mikroskil*, *3*(1), 11–20.

BI. (2021). *Laporan Perekonomian Indonesia 2020*.

BPS. (2021a). *Pertumbuhan Ekonomi Indonesia Triwulan IV-2020 No. 13/02/Th. XXIV*.

BPS. (2021b). *Profil Kemiskinan di Indonesia September 2020, Berita Resmi Statistik No. 16/02/Th. XXIV*.

Ernawati. (2016). Risk of Profit Loss Sharing Financing: The Case of Indonesia. *Al-Iqtishad: Jurnal Ilmu Ekonomi Syariah (Journal of Islamic Economics)*, *8*(1), 101–116. https://doi.org/10.15408/aiq.v8i1.2511

Faisol. (2017). Islamic Bank Financing and Its Impact on Small Medium Enterprise's Performance. *Ekonomi*, *16*(1), 13–24. https://doi.org/10.15408/etk.v16i1.4404

Handayani, A. (2018). Pengaruh DPK, NPL dan ROA Terhadap Penyaluran Kredit Pada Bank Umum yang Terdaftar di Bursa Efek Indonesia Periode 2011-2014. *Jurnal Penelitian Ekonomi Dan Akuntansi*, *3*(1), 623–631. http://dx.doi.org/10.30736%2Fjpensi.v3i1.129

Manzilati, A. (2015). How Profit and Loss Sharing System (PLS) Encourage Small & Medium Enterprises Sustainability. *Rev. Integr. Bus. Econ. Res.*, *4*(3), 99–109.

Nawaiseh, K. (2021). The Effect of COVID-19 Pandemic on SMES Management in Jordan. *Journal of Contemporary Issues in Business and Government*, *27*(1), 20–29.

OJK. (2021). *Statistik Perbankan Syariah Indonesia Desember 2020*.

OJK & BCG. (2020). *Bagaimana UMKM & Perbankan Dapat Sukses di Era Disrupsi Ekonomi & Digital*.

Prihartini, S., & Dana, I. (2018). Pengaruh CAR, NPL, dan ROA Terhadap Penyaluran Kredit Usaha Rakyat (Studi Kasus pada PT Bank Rakyat Indonesia Tbk). *E-Jurnal Manajemen Unud*, *7*(3), 1168–1194. https://doi.org/10.24843/EJMUNUD.2018.v7.i03.p02

Purnamasari, F., & Darmawan, A. (2017). Islamic Banking and Empowerment of Small Medium Enterprise. *Etikonomi*, *16*(2), 221–230. https://doi.org/10.15408/etk.v16i2.5355

Rahman, A., Rahman, M., & Kljucnikov, A. (2016). Bank Size, Relationship Lending, and SME Financing: Evidence From Bangladesh. *Actual Problems of Economics*, *9*(183), 294–307.

Ratnasari, N. (2016). Variabel - Variabel Yang Mempengaruhi Penyaluran Kredit Kepada UMKM Oleh Perbankan Di Indonesia Tahun 2011-2015. *Jurnal Pendidikan Ekonomi (JUPE)*, *4*(3), 1–10. https://doi.org/10.26740/jupe.v4n3.p%p

Sabiu, T., & Abduh, M. (2021). Impact of Islamic Banking Inclusion on SME Employment Growth in Nigeria. *Journal of Islamic Monetary Economics and Finance*, *7*(1), 77–106. https://doi.org/10.21098/jimf.v7i1.1354