

## Determinants of Musyarakah Financing (A Study of Sharia Rural Banks in Indonesia for the 2020–2024 Period)

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### ABSTRACT:

*The development of Sharia Rural Banks (Bank Perekonomian Rakyat Syariah – BPRS) plays a strategic role in promoting profit-sharing-based financing, particularly musyarakah financing. However, fluctuations in financial performance and financing quality have led to differences in the capacity of BPRS to channel such financing. This study aims to analyze the effects of Total Assets, Third Party Funds (DPK), and Non-Performing Financing (NPF) on musyarakah financing, with Return on Assets (ROA) as a mediating variable, in BPRS in Indonesia.*

*This study employs a quantitative approach using panel data derived from BPRS financial reports published by the Financial Services Authority (Otoritas Jasa Keuangan/OJK) during the 2020–2024 period. The analytical methods applied include panel data regression, path analysis, and the Sobel test to examine the mediating role of ROA. The results indicate that, partially, Total Assets have a positive and significant effect on ROA, Third Party Funds have a significant negative effect on ROA, and Non-Performing Financing has a significant effect on ROA. Simultaneously, Total Assets, Third Party Funds, and NPF significantly influence ROA, with very strong explanatory power. Furthermore, ROA is proven to have a positive and significant effect on musyarakah financing.*

*The intervening variable analysis reveals that ROA is able to mediate the effects of Total Assets and Non-Performing Financing on musyarakah financing, but it does not mediate the effect of Third Party Funds. This study concludes that internal bank factors particularly asset size, financing quality, and profitability are the main determinants in promoting musyarakah financing in Sharia Rural Banks in Indonesia.*



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### INTRODUCTION

The rapid growth of Islamic financial institutions in Indonesia over the past few years reflects the increasing role of Sharia-based finance in supporting national economic development. One of the most prominent financing instruments within Islamic banking is musyarakah financing, which is based on

partnership and profit-and-loss sharing principles (Aziz, 2015). This financing scheme emphasizes risk sharing, fairness, and productive collaboration between banks and customers, making it particularly relevant for promoting inclusive and sustainable economic growth, especially in supporting small and medium enterprises (SMEs), which constitute the backbone of the Indonesian economy (Indonesia, 2023).

According to the Association of Indonesian Sharia Banks, total Islamic financing in Indonesia was estimated to reach approximately IDR 1,200 trillion in 2022, with *musyarakah* financing contributing around 18 percent of the total Sharia financing portfolio (Asosiasi Bank Syariah Indonesia [Asbisindo], 2022). Despite this potential, the development of *musyarakah* financing has not been consistent. Data from Bank Indonesia indicate that Islamic financing growth during the 2020–2023 period experienced significant fluctuations due to domestic and global economic pressures, including the COVID-19 pandemic, which began affecting Indonesia in early 2020 (Bank Indonesia, 2023).

The COVID-19 pandemic had a substantial impact on the performance of Islamic financial institutions, including Islamic Rural Banks (Bank Perekonomian Rakyat Syariah – BPRS). While Islamic financing growth stagnated in 2020, it showed gradual recovery in 2021 and 2022, followed by continued growth despite ongoing economic uncertainty. Data published by the Financial Services Authority show that total Islamic banking financing reached IDR 643.55 trillion in 2024, representing a year-on-year growth of 9.92 percent, with *musyarakah* financing maintaining a relatively stable and increasing proportion within the financing portfolio ([www.ojk.go.id](http://www.ojk.go.id), 2025).

Beyond macroeconomic conditions, previous studies emphasize that internal bank-specific factors play a decisive role in determining financing performance and profitability. Bank profitability, commonly measured by Return on Assets (ROA), reflects the efficiency of banks in utilizing their assets to generate income (Kasmir, 2017). Larger total assets expand financing capacity, while Third Party Funds (DPK) represent the primary funding source and indicate public trust in Islamic banks. However, profitability is also influenced by financing risk, which is commonly measured through the Non-Performing Financing (NPF) ratio. High NPF levels can deteriorate asset quality, increase provisioning costs, and ultimately reduce profitability (Yudianto et al., 2024).

Empirical evidence regarding the relationships among total assets, DPK, NPF, and ROA remains mixed. Several studies find that total assets have a positive and significant effect on ROA, while NPF negatively affects bank profitability. Other studies suggest that *musyarakah* financing may function as an intervening mechanism that transmits the effects of internal bank factors to profitability outcomes, depending on the effectiveness of risk management and financing supervision. In the context of BPRS, which play a strategic role in retail and SME financing, this issue becomes increasingly important, particularly given the relatively high NPF ratios observed during the study period (Anggreni et al., 2021).

Therefore, this study aims to analyze the effects of total assets, Third Party Funds, and Non-Performing Financing on *musyarakah* financing, with Return on Assets as a mediating variable, using panel data from BPRS in Indonesia for the 2020–2024 period. This research is expected to provide a more comprehensive understanding of the internal determinants of *musyarakah* financing and profitability in Islamic rural banking and to offer empirical insights for strengthening risk management and financing strategies within BPRS.

## METHODS

This study employs a quantitative research approach using panel data analysis to examine the determinants of *musyarakah* financing in Sharia Rural Banks (Bank Perekonomian Rakyat Syariah/BPRS) in Indonesia during the 2020–2024 period. The quantitative approach is selected because it enables objective testing of causal relationships among variables through statistical analysis based on numerical data (Sujarweni, 2018).

The research population comprises all monthly financial reports of BPRS in Indonesia published by the Financial Services Authority (Otoritas Jasa Keuangan/OJK) over the 2020–2024 period. Based on these criteria, the total population consists of 60 monthly financial reports. Since all population units meet the data completeness and relevance requirements, the study applies a census (saturated sampling) technique, whereby the entire population is used as the research sample. Accordingly, the total number of observations analyzed in this study is 60.

The research subjects include all BPRS officially registered and supervised by OJK. The data are obtained from official BPRS financial reports published in the Sharia Banking Statistics issued by OJK. The observation period is chosen to capture the performance dynamics of BPRS during the COVID-19 pandemic and the subsequent post-pandemic economic recovery.

The research procedure begins with data collection and verification, followed by data classification according to the research variables. The variables examined consist of Total Assets, Third Party Funds (DPK), and Non-Performing Financing (NPF) as independent variables; Return on Assets (ROA) as a mediating variable; and musyarakah financing as the dependent variable. All variables are measured using financial ratios and nominal values commonly applied in Islamic banking performance analysis (Ajayi, 2023).

Data collection is conducted through documentation techniques by extracting relevant information from BPRS financial reports published by OJK. The collected data are subsequently structured in the form of panel data, combining time-series and cross-sectional dimensions.

The data analysis techniques include descriptive statistical analysis and inferential analysis (Pabloe, 2019). Panel data regression is performed using the Common Effect Model (CEM), Fixed Effect Model (FEM), and Random Effect Model (REM), with the selection of the most appropriate model determined through the Chow test, Hausman test, and Lagrange Multiplier test. To examine the mediating role of ROA, path analysis is applied, followed by the Sobel test to assess the significance of indirect effects. All statistical analyses are conducted using econometric software (Ghozali, 2018).

This methodological framework enables a comprehensive examination of both direct and indirect relationships between internal banking factors and musyarakah financing in Sharia Rural Banks in Indonesia.

## FINDINGS AND DISCUSSION

### 1. The Effect of Total Assets, Third Party Funds, and Non-Performing Financing on Return on Assets

The results of the panel data regression analysis indicate that Total Assets (X1), Third Party Funds (X2), and Non-Performing Financing (X3) simultaneously have a significant effect on Return on Assets (ROA) as the intervening variable. This is evidenced by an F-statistic value of 717.1629 with a probability value of 0.000000, which is below the 5 percent significance level. Therefore, the hypothesis stating that Total Assets, Third Party Funds, and NPF jointly influence ROA is accepted.

The coefficient of determination ( $R^2$ ) of 0.981188 indicates that 98.12 percent of the variation in ROA can be explained by the three independent variables, while the remaining 1.88 percent is influenced by other factors outside the research model. The very high  $R^2$  value suggests that the model has a strong explanatory power in explaining changes in the profitability of Sharia Rural Banks (BPRS) in Indonesia during the 2020–2024 period.

Partially, the results show that Non-Performing Financing (X3) has a significant effect on ROA, with a regression coefficient of 0.122792, a t-statistic of 2.009640, and a probability value of 0.0493 ( $< 0.05$ ). Meanwhile, Total Assets (X1) and Third Party Funds (X2) do not exhibit a statistically significant partial effect on ROA. These findings indicate that during the study period, financing quality was the most dominant factor influencing the profitability of BPRS compared to asset size and public fund mobilization.

### 2. The Effect of Total Assets, Third Party Funds, and Non-Performing Financing on Musyarakah Financing

The subsequent analysis reveals that Total Assets (X1), Third Party Funds (X2), and Non-Performing Financing (X3) simultaneously have a significant effect on musyarakah financing (Y). This simultaneous test result confirms that asset capacity, liquidity levels, and financing quality jointly determine the ability of BPRS to distribute profit-sharing-based financing.

Partially, each independent variable shows an influence on musyarakah financing. Total assets reflect the bank's capacity for financing expansion, third party funds indicate liquidity support, while NPF serves as a risk indicator that affects banks' prudence in channeling musyarakah

financing. These findings reinforce the view that musyarakah financing is highly influenced by internal banking conditions, particularly in the context of risk management and fund management

### 3. The Effect of Return on Assets on Musyarakah Financing

The regression results indicate that Return on Assets (ROA) has a significant effect on musyarakah financing. The ROA coefficient of  $-51.21224$ , with a t-statistic of  $-6.404712$  and a probability value of  $0.0000$ , demonstrates that ROA has a negative and statistically significant effect on musyarakah financing.

This finding suggests that an increase in BPRS profitability is not necessarily followed by an increase in musyarakah financing. This phenomenon aligns with the mechanisms of behavioral risk aversion and moral displacement (Tandon et al., 2020), whereby the achievement of profitability targets actually triggers excessive caution in offering high-risk contracts such as musyarakah, as also reflected in the gap between the ethical attitudes and behaviors of digital consumers (Zollo, 2024)(Rahman, 2025). BPRS with higher profitability levels tend to be more selective and cautious in distributing profit-sharing-based financing, considering that musyarakah contracts involve relatively higher risk compared to trade-based financing schemes.

### 4. The Mediating Role of Return on Assets

The results of the intervening variable analysis using the Sobel test indicate that Return on Assets (ROA) is able to mediate the effects of Total Assets (X1) and Non-Performing Financing (X3) on musyarakah financing (Y). This finding implies that the influence of asset size and financing quality on musyarakah financing operates through the bank's profitability performance.

However, ROA does not mediate the effect of Third Party Funds (X2) on musyarakah financing. The absence of a mediating role for ROA confirms that the availability of liquidity does not automatically lead to productive financing if fund allocation is driven more by extrinsic motivations or short-term operational pressures (Shah et al., 2023), rather than by a planned profitability strategy (Rahman, 2025). This result indicates that third party funds have a more direct influence through liquidity availability rather than through profitability mechanisms.

### 5. Discussion of Research Findings

Overall, the findings of this study indicate that internal factors of BPRS, particularly financing quality and profitability levels, play a crucial role in determining musyarakah financing. These results are in line with the research objective, which emphasizes the importance of risk management and financial performance efficiency in promoting profit-sharing-based financing.

The findings are also consistent with previous studies suggesting that high financing risk is one of the main factors constraining the expansion of musyarakah financing in Islamic financial institutions. Therefore, increasing musyarakah financing in BPRS should be accompanied by strengthened risk management practices and improved financing quality

## CONCLUSION

This study examines the determinants of musyarakah financing in Sharia Rural Banks (BPRS) in Indonesia during the 2020–2024 period by incorporating internal banking factors and profitability as a mediating variable. The findings demonstrate that Total Assets, Third Party Funds, and Non-Performing Financing simultaneously influence Return on Assets, indicating that internal financial conditions play a crucial role in shaping the profitability of BPRS.

The results further reveal that Non-Performing Financing has a significant effect on profitability, highlighting the importance of financing quality management in maintaining the financial performance of BPRS. In contrast, Total Assets and Third Party Funds do not exert a significant partial effect on profitability, suggesting that asset size and fund mobilization alone are insufficient to enhance profitability without effective risk management.

Regarding musyarakah financing, the study finds that Return on Assets significantly influences the allocation of musyarakah financing, with a negative relationship indicating that higher profitability does not necessarily encourage greater distribution of profit-sharing financing. This suggests that BPRS tend to adopt a more cautious approach toward musyarakah financing, particularly when profitability targets have been achieved.

The mediation analysis confirms that Return on Assets mediates the effects of Total Assets and Non-Performing Financing on musyarakah financing, while it does not mediate the effect of Third Party Funds. This finding implies that asset capacity and financing quality affect musyarakah financing decisions through profitability considerations, whereas liquidity derived from public funds influences financing more directly.

Overall, this study concludes that profitability and financing quality are key determinants of musyarakah financing in BPRS, while asset growth and fund mobilization must be accompanied by effective risk management to support the sustainable expansion of profit-sharing-based financing. These findings provide practical implications for BPRS management in formulating strategies to strengthen musyarakah financing through improved financial performance and risk control.

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