The Advantages of Aqad *Shirkah* and it's Financial Performance Case Study: non-and Financial Institutions in Aceh, Indonesia

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Abstract: Shariah prohibits taking of the interest in the financing and investment activities includes providing fund for business activities. Nowadays, many businesspersons recognized that there is an opportunity to generate the profit from the intermediation between savers and investors or lenders and borrowers, and this led to the growth of varieties of financial system, one of them is Islamic non and institutions. In practices, the Islamic non-institutions as provider funds for business activities must be complying with the Shariah. This study is written to investigate the practice of aqad *Shirkah* and its advantages to the financial performance. A quantitative data analysis is used to calculate the Return on Asset (ROA), Return on Equity (ROE) and comparing the profits earned by both i.e. Non o Financial institutions. The secondary data were collected from two sources i.e. non-institutional (Jroh Production Company) and the institutional including BCA (Islamic) and BCA (Commercial) for one year (in 2016). The result of this study shows that the financial performance measured by ROA of non-institutional (e.g. *Jroh* Production Companies) and BCA (Islamic Bank) is categorized as very healthy. In contrast, the BCA (Commercial Bank) categorized as unhealthy. Meanwhile, by applying the value of ROE, their financial performance is still categorized as unhealthy. Further, the result of real profit earned from investment activities by non-institutional (e.g. Jroh Production Companies) is 4.29% (lower bound), 37% (upper bound) and in average, is 14.46%. It indicates the advantages of aqad *Shirkah* proved that the Islamic financial system more profitable and beneficial compared to other financial system utilized by Islamic and commercial bank in this case.

Keyword: Sharia, Shirkah, Return on Asset (ROA), Commercial Bank

1. Introduction

As Muslim, Islam is a complete way of life "*a mercy to all creation*" and regulates the relationship between God (*Khaliq*) and human beings (*Insaanun*) in the form of worships (Horrie and Chippindale, 2007) In addition, Islam also comes with regulating the relationships among human beings, includes the business activities namely *Muamalah* (An-Na'im, 2008). In the Holy Quran surah *Al Baqarah* verse 275, revealed "*...Allah has permitted trade and has forbidden interest.*" It means that Allah prohibited riba or usury from business transactions (Seniawski, 2000; Hanif, 2011; Jumadil Saputra, Kusairi and Sanusi, 2017). Syllabus Along with the globalization era, many of business institutions are created to generate and maximize profit that produced from investment activities through various financial system, either Islamic or commercial systems (Zamir, 1997; J Saputra, Kusairi and Sanusi, 2017). Nowadays, in a

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Muslim countries which practices Islamic Law or Shariah, the western financial system was leaving by the Muslim because does not comply the Shariah. Thus, taking its opportunity, numerous businesspersons were developed and created the non-and financial institutions to offer financial product that comply the *Shariah* such as Islamic banking, Islamic insurance (Takaful), Islamic investment (Sukuk) and others (Saputra *et al.*, 2016). Stated the issue in financial model todays, it comes from the modern financial systems that have a lack of regulations, deficiencies and risk management. Interestingly, the financial crises happen almost in rest of the world, except Islamic countries (Ahmed, 2010). Therefore, the Islamic scholars attempted to investigate regarding the financial system that applied by Islamic countries which had did not experiencing the economy crises in 2008 (Hasan and Dridi, 2010). Through the advantages of Islamic financial system, this study tries to investigate deeply the practice of aqad *Shirkah* and its financial performance. It is driven by the study regarding the application of aqad *Shirkah* still limited studied by researchers and there are lack of knowledge about the concept concerning *Shirkah* (joint venture).

2. Literature Review

Shirkah or *Musharakah* or *sharikah* can be defined as a form of partnership between two or more individuals whereas they combined a portion of their capital or labor in order to share the profits and bearing of losses from business activities, enjoying similar rights and liabilities (Lewis, 2001). In Islamic law, Hanafis and Hanbalis school of thought were dividing the *Shirkah* into two types namely *Shirkah al-milk* (joint ownership on a non-contractual basis) and *Shirkah al-uqud* (contractual partnership). Further, the school of thought of Hanafis and Hanbalis also have divided the Shirkah al-milk into two types; first, *Shirkah al-milk iktiyari* (voluntary co-ownership) and seconds, *Shirkah al-milk mirath* (without partner willingness). However, al-Kasani, (2000) revealed that *Malikis* have classified the *Shirkah al-milk* into three categories which are *Shirkah irth* (partnership because of inheritance), *Shirkah al-ghaniah* (partnership among soldiers in assets left) and *Shirkah al-Mubta'in* (partnership among purchasers). A study was focuses on concept of *Shirkah* was conducted by (Hasanuzzaman, 1971; Lewis, 2001; Farooq, 2007). Further, (An-Na'im, 2008) discuss the issue of musharakah mutanaqisah home financing as practiced by Islamic banks in Malaysia. This study found that the shirkat al-milk is a form of home financing but it is cannot be considered permanently because it does not comply all the features of shirkat al-milk. Further, this study also found that the scholars were dispute to allow a pre-determined price of the bank's portion or share in the house and to stipulate a second promise in the event of default.

Besides that, a study was conducted by (Farooq, 2007) found that a partnership is the least common form of business organization for practical reasons to cover equity-financing. Islamic Financial Institution (IFIs) are organized as banks, but rather than being financial intermediaries, they are primarily merchant banks. Further, while paying lip service to Profit and Loss Sharing (PLS) modes to define themselves as interest-free aka Islamic entities, IFIs continue to marginalize PLS, packaging conventional banking products under Islamic labels. Further, (Dar and Presley, 2001) studied the lack of profit loss sharing (PLS) in Islamic banking. They found that without the types of management and control, Islamic banks will persist in taking the easy and risk averse route and avoid profit and loss sharing (PLS) contracts. As in earlier discussion above, we found that previous studies only focused on financial institution such as bank or both conventional and Islamic bank and they concern on the practice of profit sharing and loss bearing (PLS) either assessment, management and concept. A study about practice of Shirkah in non-financial institution still none of being focus of researchers. Thus, in the present paper, we investigate the concept of Shirkah practiced by non- and financial institutions. Further, we also compare the financial performance of non- and financial institutions which applying aqad *Shirkah* through return on asset (ROA) and return on equity (ROE).

3. Methodology

One of the challenges in the development of Islamic financial system is lack of measurement tools to assess the financial performance, either by non-financial or financial institutions that comprehensively comply with the Shariah. As the result, many researchers have adopted a general measurement tool that used by the commercial bank through financial ratios to assess their financial performance and it's applied also to assess the Islamic financial performance using the value of Return on Assets and Return on Equity. Therefore, the ratio of net income to assets and indicates the firm's net profit generated from capital (money) invested in total assets can be formulated as below:

$$ROA = \frac{NIC}{ATA} X100\% \quad \ldots\ldots\ldots\ldots (1)$$

Where, return on asset denotes by ROA, NIC is earning after tax (net income) and ATA is average total asset. Furthermore, to determine the fitness ratios of the company which measured by Return on Asset (ROA) can be categorized as follows:

Table 1. The level of business health - ROA criteria

Ratio Interval	**Rank**	**Category**
ROA > 1.5%	1	Very Healthy
1.25% < ROA ≤ 1.5%	2	Healthy
0.5% < ROA ≤ 1.25%	3	Fair
0 ≤ ROA ≤ 0.5%	4	Unhealthy
ROA < 0%	5	Very Unhealthy

Source: Bank Indonesia (2007)

Further, the ratio of net income to shareholders' equity and represents the profit generated from capital (money) of shareholder's investment (shareholder's equity) can be determined the following formula as seen as below:

$$ROE = \frac{NIC}{EIC} X100\% \quad \ldots\ldots\ldots\ldots (2)$$

Where, return on equity denotes by ROE, NIC is earning after tax (net income) and EIC is equity income. Further, utilizing the measurement tool was developed by Bank of Indonesia, the level of business health - ROE criteria can be presented as below:

Table 2. The level of business health - ROE criteria

Ratio	**Rank**	**Category**
ROE > 15%	1	Very Healthy
12,5% < ROE ≤ 15%	2	Healthy
5% < ROE ≤ 12,5%	3	Fair
0 < ROE ≤ 5%	4	Unhealthy

ROE ≤ 0%	5	Very Unhealthy

Source: Bank Indonesia (2007)

Having that, in further section, this study presents the result of data analysis and discussion

4. Result And Discussion

To achieve the research objective, we use financial report of Jroh Production in the period of 2016. Using Table 3 below, we found that the ratio of profit of Jroh Production in 2016 is 16.38%. A current earnings for 1 year is IDR 197,066,556.11 and total income is IDR 1,202,856,917.78.

Table 3. Financial Report of Jroh Production in the year of 2016

Balance Sheet and Loss/ Profit	
Total income (1 year)	1,202,856,917.78
Initial capital	1,049,312,527.84
Total capital (1 year)	10,580,041,311.53
Capital in the end of the year plus initial capital	11,629,353,839.37
Ratio profit *(profit/income x 100%)*	16,38%
Retained earnings for 1 year	178,240,466.43
Current earnings for 1 year	197,066,556.11
Current earnings at the end of the year plus earning from initial capital	222,246,200.80

Source: Report of the Shirkah investment of Jroh Production (2017)

Table 4. Result of Financial Ratio (ROA and ROE)

Financial Ratios	Percent
Return On Assets (ROA)	1,91%
Return On Equity (ROE)	1,91%

Utilizing the financial report in Table 3 above, we calculate the financial ratios including return on assets (ROA) and return on equity (ROE). After calculating both of financial ratios, we found that the ROA and ROE of Jroh Production are 1.91 percent. Further, it can be interpreted that ROA of Jroh Production as big as 1.91 percent shows the level of business health is categorized as very healthy. Meanwhile, ROE indicates the level of business health is categorized as unhealthy. In addition, as mentioned in previous discussion, we also use financial report of Islamic bank i.e. Bank Central Asia in the period of 2016 to investigate the advantages of aqad *Shirkah* and its financial performance through the value of ROA and ROA between non- and financial institutions.

Table 5. Financial Report of BCA Islamic in 2016

Balance Sheet (in billion - IDR)	
Total assets	1.602,2
Total Earning Assets	1.523,6
Current accounts with Bank Indonesia	58,8
FASBIS	258,0
Conventional Credit - Gross	-
Shariah Financing - Gross	1.077,7

Balance Sheet (in billion - IDR)	
Securities	206,9
Third-party funds	1.261,8
Giro	143,2
Savings	133,0
Deposit	985,5
Loans received	0,1
Equity	304,4
Profit and Loss (in billion - IDR)	
Net profit sharing revenue	64,7
Net interest income	-
Revenue-sharing and net interest	64,7
Other operating income	7,5
Other operating expenses	59,6
Allowance for write-off of other assets	1,5
Operational profit	11,0
Earnings before income tax	11,0
Net profit	8,4
Financial Ratios (Percentage)	
ROA	0.8%
ROE	2.8%
Net Core Operating Margin (NCOM)	9,6%
Capital Adequacy Ratio (CAR)	31,5%
Credit / Financing Ratio to Deposits (LDR / FDR)	79,9%
Ratio of NPL / NPF to total credit / Financing - Gross	0,1%

Source: Bank Indonesia (2017)

Table 5 shows the financial report of BCA - Islamic bank in the year of 2016 that comprises of balance sheets, profit - loss and financial ratios. We found that the value of ROA is 0.8% and ROE is 2.8%. It indicates that the level of business health of BCA - Islamic bank is categorized as unhealthy.

Table 6. Financial Report of BCA Commerce in the year of 2016

Balance Sheet	
Total Current Assets (in millions - IDR)	381,092,371.00
Cash	11,054,208.00
Net Assets Net	370,038,163.00
Fixed assets book value	6,406,625.00
Business assets	376,444,788.00
Total miscellaneous activity	6,265,653.00
Total current liabilities	5,839,495.00
Long-term obligation	128,018.00

Total Liability	5,967,513.00
Account payable	5,839,495.00
Accounts receivable	4,487,552.00
Stock	48,474.00
Forex position	-
Total Equity	51,897,942.00
Number of shares	4,396,429.00
Profit / Loss (in millions - IDR)	
Net sales	27,613,956.00
Operating profit	14,255,568.00
Interest Cost	7,647,167.00
Exchange rate / loss	21,134.00
Cost (result) others	2,729.00
Profit before Income	14,686,046.00
Net income after income tax	11,718,460.00
Deposits from customers	368,789,454.00
Financial Ratios (Percentage)	
ROA	0,23%
ROE	0,04%
Dividend	857.07

Source: Bank Indonesia (2017)

Table 6 displays the BCA - commercial bank financial report in the year of 2016 that consist of balance sheets, profit - loss and financial ratios. Similar to the Islamic bank, we also found that the value of ROA is 0.23% and ROE is 0.04%. It indicates that the level of business health of BCA - commercial bank is categorized as unhealthy. In addition, as aforementioned in previous section, this study also presents a real investment returns received by investor (*Sahibul mal*) under aqad *Shirkah* or joint venture (*Al Musharakah*).

Table 7. The value of Profit Sharing (PS) received by *Sahibul mal*

Initial value of Investment	Panel 1	Panel 2	Panel 3
	50,000,000.-	80,000,000.-	100,000,000.-
Lower Bound (π %)	4.29	4.29	4.29
Upper Bound (π %)	37	37	37

Month	Value of profit sharing (in IDR)		
1	872,618.93	1,396,190.28	1,745,237.85
2	433,691.26	693,906.01	867,382.51
3	626,873.32	1,002,939.70	1,253,674.63
4	414,089.55	662,543.27	828,179.09
5	719,544.76	1,151,271.61	1,439,089.51
8	310,458.14	496,733.03	620,916.28
10	451,944.14	723,110.62	903,888.28
11	725,390.09	1,160,624.14	1,450,780.18
12	2,676,300.12	4,282,080.18	5,352,600.23
Total	7,230,874.28	11,569,398.85	14,461,748.57

Initial value of Investment	Panel 1	Panel 2	Panel 3
	50,000,000.-	80,000,000.-	100,000,000.-
Average (π %)	14.46	14.46	14.46

Table 7 shows the value of Profit Sharing (PS) received by Sahibul mal based on their investment values. We use three panels (e.g. Panel 1, Panel 2 and Panel 3) and each of them (Sahibul mal) is assumed investing their money (e.g. IDR 50,000,000.-, IDR 80,000,000.-, and IDR 100,000,000.-). Using three panels, the ratio of profit for lower bound is 4.29%, upper bound is 37%, and in average, is 14.46%. There are two months are not obtain the profit, it caused by fasting month or the business activities were stopped. Thus, we can conclude that when increase the initial value of investment, it would give effects on the increasing the value of investment return received by *Sahibul mal.*

5. Conclusion

Among three institutions being focused in this study, we found the level of business health of Jroh Production Company have assessed by return on assets (ROA) can be categorized as very healthy. Further, followed by BCA Islamic is healthy meanwhile, BCA commerce categorized as Unhealthy. Further, utilizing the ratio of return on equity (ROE), all of the business either by non- and financial institutions obtained the value of ROA is less than 0.5% or can be categorized as unhealthy. In others word, through the aqad Shirkah (*al musharakah*), the Jroh Production earned the higher profit compared to BCA (Islamic and Commerce). It means that, the Islamic financial system through aqad *Shirkah* more effective and efficient used to achieve the level of business health and proved its advantages compared to other financial system utilized by Islamic and commercial bank in this case.

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