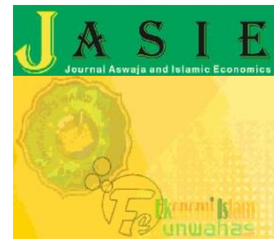
JASIE - Journal of Aswaja and Islamic Economics *Vol. 03 No. 01 - 2024*
Website Journal : https://www.publikasiilmiah.unwahas.ac.id/index.php/JASIE/index
DOI : 10.3194/jse.v1i1.6877
ISSN : 2962-5602 (Online) ISSN : 2963-7864 (Print)



LIQUIDITY RISK MANAGEMENT IN SHARIA BANKS

Nurfitriah[1]

[1] Sultan Ageng Tirtayasa University, Serang, Banten, Indonesia, 5554200043@untirta.ac.id

ABSTRACT

Liquidity management refers to the efforts of companies or financial institutions to manage and control the availability and use of sufficient funds to meet their immediate or sudden financial obligations. This aims to maintain smooth operations, fulfill payment obligations, and avoid the risk of a lack of liquidity. Liquidity management involves careful planning, monitoring and control of financial assets and liabilities.

The method this paper used to examine liquidity risk management in Islamic banks is a qualitative method. This method is used with due regard to materials which mostly come from literature study research. Literature study research begins by looking for bibliographical data, both primary and secondary, that have something to do with the focus of the discussion.

Liquidity management in Islamic banks has principles that are in accordance with Islamic principles in banking activities. Liquidity instruments at Islamic banks can be obtained from collecting third party funds (DPK), borrowing on the Islamic money market, purchasing Islamic SBIs, seeking domestic or foreign investors, or from other funding sources.

Keywords : Liquidity, Risk, Islamic Banks

INTRODUCTION

Islamic banking is a form of financial institution that can influence the growth of the national economy. The growth of Islamic banks in Indonesia is growing quite rapidly, seen from the market share value of 5.57% in 2017 and will increase in 2021 with a market share of 6.52%. The Financial Services Authority (OJK) noted that Indonesia's total Islamic financial assets (not including Islamic stocks) reached 151.03 billion United States dollars (US) or the equivalent of Rp. 2,375.8 trillion as of the end of December 2022. The increase in the growth of Islamic banks certainly had an impact on national economic growth.

In general, the main task of a bank is to collect funds from the public in the form of deposits. Then the funds that have been collected are channeled back to the community in the form of loans (credit), as well as providing other bank services. To be able to collect funds from the public, banks have a duty to convince customers that the money they deposit is guaranteed to be safe. Thus, in order to provide security to customers, the bank must be liquid.

According to Fahmi (2017: 121) the liquidity ratio is the ability of a company to fulfill its short-term obligations in a timely manner. The higher the amount of current assets to current liabilities, the greater the confidence that these current liabilities will be paid. Meanwhile, according to Hanafi in a book entitled Financial Management, the liquidity ratio measures a company's short-term liquidity capacity in view of the size of its current assets relative to its current debt.

Liquidity at the bank refers to the bank's ability to meet financial obligations immediately by using existing liquid resources. This means that banks must have sufficient assets that can be converted into cash quickly and efficiently to meet urgent cash needs, such as withdrawing funds from customers or paying short-term obligations. The importance of assessing the liquidity of a bank is one way to determine whether the bank is in a healthy, moderate, unhealthy or unhealthy condition. One of the causes of bankruptcy of a bank is due to the inability to meet its liquidity needs. Therefore, the available liquidity must be sufficient so as not to disrupt operational needs.

LITERATURE REVIEW

Liquidity risk can be defined as the risk of inability to liquidate in a timely manner at a reasonable price (Muranaga & Ohsawa, 2002). Banks face liquidity risk if they do not liquidate their assets at a fair price. Assets that are sold at low prices but the need to liquidate bank assets is very urgent, it is this phenomenon that causes losses and decreases income.

Bank Indonesia Regulation (PBI) No.11/25/2009, the definition of liquidity risk is a bank risk resulting from the bank's inability to fulfill its maturing bank obligations from funding cash flows and or liquid assets without disturbing the bank's daily activities. From this understanding, it means that the bank must be able to provide reserve funds when there is a sudden withdrawal of customer funds and the assets invested by the bank are also sufficiently liquid when they must be disbursed to cover funding needs.

Bank liquidity risk is also caused by the emergence of depositors or depositors who are present together (collectively) and massively to disburse their funds in large quantities. The amount of funds disbursed exceeds the amount of funds available at the bank itself (Hubbard, 2002). Liquidity risk not only affects bank performance but also its reputation (Jenkinson, 2008). A bank may lose depositor confidence if funds are not provided in a timely manner. In

this situation the reputation of the bank can be at stake. In addition, a bad liquidity position can lead to sanctions from regulators. Therefore, it is imperative for banks to maintain a healthy liquidity position.

Liquidity risk has become a serious concern and a challenge for banks in the modern era. High competition in customer funds, a variety of funding products offered with advances in technology have changed the fund and risk management structure (Akhtar, 2007). A bank having good asset quality, strong earnings and sufficient capital, may fail if it does not maintain adequate liquidity (Crowe, 2009).

According to Goodhart (2008), there are two basic aspects of liquidity risk: maturity transformation (the maturity of bank liabilities and assets) and the inherent liquidity of a bank's assets (the extent to which an asset can be sold without causing a significant loss of value under market conditions).). In fact, the two elements of a bank's liquidity are closely related. Banks do not need to worry about maturity transformation if they have assets that can be sold without incurring a loss. Meanwhile, banks with assets that will mature in a shorter time may not need to maintain liquid assets.

Apart from the maturity mismatch above, liquidity risk arises due to economic recession conditions, causing a shortage of resources. This increases the demand for deep depositors creates liquidity risk. This can lead to the failure of certain banks or even the entire banking system due to contagion effects (Diamond & Rajan, 2001). High liquidity increases influence and high influence banks can change from providers to consumers of liquidity (Clementi, 2001).

RESEARCH METODOLOGY

The method used to examine liquidity risk management in Islamic banks is a qualitative method. This method is used with due regard to materials which mostly come from literature study research. Literature study research begins by looking for bibliographical data, both primary and secondary, that have something to do with the focus of the discussion. After that data processing is carried out to obtain research results to then be written down as research findings and interpreted to get the final conclusion of the research.

RESULT AND DISCUSSION

The business activities carried out by Islamic banks in channeling financing are very depending on the availability of liquid funds. Liquid funds are obtained through the intermediation function of Islamic banks. According to the foundation of the intermediation theory, there are two reasons for the need for the existence of banks as intermediary institutions, including the provision of liquidity and financial services. As a provider of liquid finance or funds, Islamic banks collect (fund) funds originating from savers to then channel them to the real sector, and in other situations there must also be guarantees for the availability of liquidity when any of the customers withdraws the deposit. Diamond and Rajan, 2001). On the other hand, banks must be able to make changes from initially short-term savings to long-term financing, this causes banks to be very vulnerable to liquidity risk.

Types of liquidity risk

There are two types of liquidity risk. The Risk Management Certification Agency (2008) states that there are two different types of liquidity risk, namely endogenous liquidity and exogenous liquidity. Endogenous liquidity is liquidity that is attached or inherent in the asset itself while exogenous liquidity is often referred to as funding liquidity. Endogenous liquidity relates to a bank's ability to sell assets in a liquid market quickly and at a small bid/offer spread and is not too affected by the size of the transaction. While exogenous liquidity is liquidity that is created through a bank's liability structure, banks can see this funding mismatch by using a liquidity ladder.

Based on the underlying sharia principles, there are two types of fundraising contracts, namely wadi'ah or mudharabah. Products with wadi'ah contracts have a higher liquidity risk because the owner of the funds does not share in losses or income from the use of the funds by the bank. Banks must be responsible for the integrity of customer funds.

Liquidity management in islamic banks

The main cause of the emergence of liquidity risk originates from an imbalance in assets and liabilities and a maturity mismatch that occurs because of this imbalance. In the picture of the liquidity gap and being careful to regulate the maturity structure of assets so that they remain solvent, banks need to maintain short-term assets.

Islamic banks must be able to manage the management of the supply and demand for liquidity. Management must be carried out properly and profitably so that the business can be run properly, safely, and have good relations with the government as the regulator. Liquidity risks arising from improper fund management must be able to be analyzed and scrutinized so that large losses do not hit the banks. Good liquidity management (robust) is a challenge in itself in treading an open economic system with various influences from both external and internal. Bank failure in managing in a global financial environment occurs because the liquidity management system has not worked optimally, especially in solving detrimental problems (Ismal, 2010).

Management of liquidity management in islamic banks

Liquidity risk management is a separate challenge for Islamic banks, given the prohibition of usury-based instruments. Islamic banks are not given the opportunity to carry out their financial management in sectors that are prohibited by sharia, for example investments containing usury, ghoror, deception, the presence of elements of gambling and others. Fund management can only be carried out by Islamic banks in halal sectors, so as not to damage the reputation of Islamic banks as an intermediary institution (Mahir, 2010).

The intermediation functions of Islamic banks can be carried out in various ways pioneering especially in bringing in bank liquidity. One of the pioneering steps can be carried out by accommodating investment in the capital market and money market which have been declared permissible in accordance with the fatwa provisions of the National Shariah Council of the Indonesian Ulema Council. Similar things have also been accommodated by other countries such as Malaysia, Bahrain and Saudi Arabia. These countries have allowed Islamic banks to invest their funds in the capital market and money market even though they are classified as sharia only. Future development of Islamic banks is expected to carry out various product, institutional and regulatory innovations to open space for Islamic banks to invest.

On the other hand, banks can increase maturity transformation by holding highly liquid assets because these assets can be sold or used to meet funding risks in a short time (Goodhart, 2008). A bank may have to increase cash reserves to reduce liquidity risk, but this may be costly in practice (Holmstrom & Tirole, 2000). The liquidity of an asset should be based on its capacity to generate liquidity, not its trading book classification or accounting treatment. A bank always tries to avoid capital injections from the government because this can place a given bank at the government's mercy (Jeanne & Svensson, 2007). Therefore, banks hold minimum cash balances to avoid liquidity problems (Jenkinson, 2008).

According to Gatev and Strahan (2003), deposits provide protection for banks against liquidity risk. Under depressed market conditions, banks are seen as a haven for investors who do not intend to issue funds against their loan commitments. Cash flows in any bank complement each other. Inflows of funds provide protection for banks for outflows due to advances in loans. Therefore, banks use deposits for liquidity risk protection.

One measure to reduce liquidity pressure is the transformation of illiquid assets into cash. During times of great fund pressure, securitization techniques are usually used by the banking system to liquidate assets such as mortgages (Jenkinson, 2008). A bank must respond to funding shortfalls by acting on the asset side of its balance sheet if it faces restrictions on increasing liquidity. It will be forced to reduce the progress of lending to its clients to reduce funding requirements.

Despite its features to support funding and increase liquidity, Ali (2004) have narrated two main drawbacks of the above policies. First, this strategy takes a little longer to set up. Many credit decisions are made in advance and are difficult to reverse right away, so they don't generate quick liquidity. Second, reduced lending affects a large part of the economy. In the non-availability of funds for firms and households, it becomes difficult to support long-term investment and consumption in the economy.

CONCLUSION

Liquidity risk management is the management of a bank to avoid liquidity risk caused by the bank's inability to pay its short-term obligations. The inability is caused by the unavailability of funds at the bank concerned. In order for banks to avoid liquidity risk, banks must ensure that sufficient funds are available, especially enough to pay obligations, sufficient to disburse customer funds that are due, sufficient to finance operational activities and sufficient funds to face the possibility of a deteriorating economy.

Based on the underlying sharia principles, there are two types of fundraising contracts, namely wadi'ah or mudharabah. Products with wadi'ah contracts have a higher liquidity risk because the owner of the funds does not share in losses or income from the use of the funds by the bank. Banks must be responsible for the integrity of customer funds.

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