

Analysis Of Islamic Banks' Merger in Indonesia

Fitri Mareta^{a✉}, Heliani^b, Siti Elisah^c, Andini Ulhaq^d, Indri Febriani^e

^{abcde}Universitas Nusa Putra

✉ fitri.mareta@nusaputra.ac.id

ABSTRACT. Islamic bank is a bank that collects funds from the public by using system profit sharing for every profit it gets and in carrying out its activities in accordance with Islamic law. Remembering that in Indonesia most of the population is Muslim, therefore they need a bank that works in accordance with Islamic law. Considering the number of percentages of Islamic banks in Indonesia are still small and cannot yet dominate the market share, therefore this research is expected to find out whether the merging of 3 Islamic banks (BRIS, BSM and BNIS) able to control market share or not. To see the synergy resulting from this merger is used methods Discounted Cash Flow - Free Cash Flow to Equity and Relative Valuation - Price to Book Ratio. The data used are the financial statements of each bank from 2014 to 2019 which are available on the Indonesia Stock Exchange (IDX) or the websites of each bank.

Keyword: CPAM, FCFE, Islamic Bank, Merger, PVB

INTRODUCTION

Bank is an institution that is a place for financial intermediation. Meanwhile, according to Law Number 10 Year 1998 Article 1 Chapter 1 Paragraph 2 states that Bank is a business entity that collects funds from the public in the form of credit and / or other forms in order to improve the standard of living of the people at large (Purnamasari & Dodik, 2016). From this understanding, it can be concluded that there are 3 activities carried out by banks, namely as fund collectors, fund distributors, and other bank service providers to the public. According to Law Number 10 Year 1998 Article 1 Chapter 1 Paragraph 2 states that Commercial Banks are banks which carry out business activities conventionally and or based on sharia principles which in their activities provide services in payment traffic (Rahayu & Bambang, 2012). In this regard, Indonesia is the largest Muslim country in the world where 87.2% or around 207.176.162 of the 237.641.326 total population of Indonesia are Muslims (BPS, 2010). This is what makes Indonesia need a financial institution that does not involve interest in the transaction. Financial Services Authority on November 1, 1991, the first Islamic Bank in Indonesia was established, namely PT Bank Muamalat Indonesia (BMI), where this BMI officially operated on May 1, 1992 with an initial capital of IDR 106,126,382,000 (OJK, 2020).

Since the issuance of Law Number 10 Year 1998 as a substitute for Law Number 7 Year 1992 began to establish many Islamic banks in Indonesia such as Bank Syariah Mandiri, Bank BRI Syariah, Bank BTN Syariah, Bank Niaga Syariah, Bank Mega Syariah, and others (OJK, 2020). The penetration rate of Islamic bank assets is still below 8% in 2019, this is smaller than commercial banks in Indonesia. This is due to the absence of a sharia bank capable of gaining the share of the sharia market which is currently untouched and which fulfills customer needs both from a financial and technological perspective (Mediasumutku, 2020). For this reason, a synergy emerged to merge three Islamic banks in Indonesia, namely PT Bank BRISyariah Tbk (BRIS), Bank Syariah Mandiri (BSM) and BNI Syariah (BNIS). Where BRIS was the bank that accepted the merger, while BSM and BNIS were the merged banks. The bank resulting from this merger will later be named BRIS, where it is hoped that BRIS will have sufficient capital and assets, both in terms of finance, human resources, information systems and other matters that can assist customer needs and services in accordance with the principles of Islamic principles.

PT. BRISyariah Tbk was originally named PT. Bank Djasa Arta was founded in 1969, which in 2008 was taken over by PT. Bank Rakyat Indonesia Tbk. BRIS has 9.716.113.498 shares of which 73% is owned by PT Bank Rakyat Indonesia Tbk (BBRI) 8,53% owned by DPLK BRI - Sharia Shares and 18,47% owned by the community. On In 2019 BRIS was able to generate net profit of IDR 67.870.000.000 (IDX, 2020). Reporting from the official website of Bank Syariah Mandiri, Bank Syariah Mandiri was established on June 15, 1955 with its initial name was PT Bank Nasional, BMS had previously changed its name several times until November 1, 1999 BSM officially operated under the name Bank Syariah Mandiri. This is based on the Decree of the Governor of Bank Indonesia No. 1/24 / KEP.GBI / 1999 dated 25 October 1999. The number of shares owned by BMS was 628.403.736 and 100% owned by PT. Bank Mandiri Tbk in 2019 BMS received a net profit of IDR 1.206.670.000.000 (www.mandirisyariah.co.id, 2020).

BNI Syariah operated as a sharia commercial bank on June 19, 2010 based on the decision of the Governor of Bank Indonesia N0. 12/41 / KEP.GBI.2010 dated May 21, 2010. The number of

BNIS shares outstanding was 2.921.335 with a 99,95% share held by PT. Bank Negara Indonesia Tbk and 0,05% held by PT BNI Life Insurance. In 2019 BNI Syariah received a net profit of Rp. 596.930.000.000, - (www.bnisyariah.co.id, 2020). Based on the description above, the researcher took the title "Mega Merger Analysis of Islamic Banks in Indonesia.

Discounted Cash Flow Method

The DCF method is a method for ranking investment proposals that uses the concept of the time value of money. This method is an investment proposal appraisal technique based on financial measures (Rosyid, 2012). Project appraisal techniques that can be classified into the DCF method include Net Present Value (NPV), Internal Rate of Return (IRR), and Profitability Index (PI). The use of the DCF method requires that DCF parameters are met in advance, which include: (1) the future cash flows of a project, (2) an adjusted risk discount rate, (3) the impact of the project on cash flows generated from other assets, and (4) the impact of the project on future investment opportunities (Khalisah & Gusman, 2020). The theory that underlies this method is that all money flowing in the company in the future, when discounted is the fair value of the shares, or commonly known as discounted cash flow (Nurhadiman & Septariani, 2019). DCF is also a method of calculating using cash flows such as net income, free cash flow, and operating cash flow which are calculated future value and then discounted to get the fair price value of shares (Martia et al., 2018).

Sharia Bank

According to Law no. 21 of 2008 states that Islamic banking is everything that concerns Islamic banks and sharia business units, business activities, including institutions and processes in carrying out their business activities (Lestari, 2015). According to Muchlis (2018), the characteristics of Islamic banks are as follows:

1. Money is used as a medium of exchange, not a traded commodity.
2. Business risks faced jointly between customers and Islamic banks.
3. There is a sharia supervisory board to supervise the operational activities of sharia banks so as not to deviate from sharia values.
4. Use the profit-sharing method of service profits or real transactions instead of the interest system in exchange for the owner of the money, the amount of which is determined in advance.

Sharia bank is an institution that has a function to carry out economic mechanisms in the real sector in buying and selling or investing activities and providing savings and banking services to customers in accordance with sharia regulations. Sharia principles are an agreement rule based on Islamic law between banks and other parties that are in accordance with sharia values which are micro and macro in nature (Umardani & Abraham, 2017). As for what is meant by macro values are goodness (*maslahat*), justice, free from usury, free from obscurity (*gharar*), the use of money as a measuring tool, free from gambling (*maysir*), using the zakat system, and free from illegitimate or things that are broken (false). while the micro values that must be possessed by Islamic banking are trustworthiness, *shiddiq*, *fathanah* and *tabligh*. Then the success of a sharia bank is the success of the world and the hereafter (long term oriented) which pays great attention to the correctness of the process, the benefit of the results and the cleanliness of the source (Wibowo, 2013). The main principles of Islamic banking operate on six principles, namely the principle of loans such as *qard* and *qardhul hasan*, the principle of savings (*wadiah*), the principle of buying and selling such as *murabahah*, *salam* and *istishna*, the principle of service (fee based serviced), the principle of leasing such as *ijarah* and the principle of profit sharing such as *mudharabah* and *musyarakah* (Fadhila, 2015).

Merger

A merger is defined as a merger of two or more businesses in which only one company remains alive as a legal entity, while the others stop their activities or dissolve (Akinbuli & Kelilume, 2013). In most of the merger cases, the larger company will be kept alive and will retain its name and legal status, while the smaller company or the merged company will cease activities or be dissolved as a legal entity. A party that is still alive or who receives a merger is called a surviving firm or an issuing firm. Meanwhile, companies that stop and dissolve after the merger are called merged firms (Al-Hroot, 2016). Companies choose mergers as a strategy because the merger is considered a fast way to realize company goals where the company does not need to start from scratch.

METHODS

This study uses financial reports between 2014 and 2019, besides that the Risk-Free Rate used is the FR0037 series. In this study, researchers also used historical stock data from 2018 to November 2020. The object of this research is BUMN Islamic Bank, namely BRI Syariah Bank, Bank Syariah Mandiri and Bank BNI Syariah. This research is a quantitative study, where the calculated data in the form of numbers, which aims to calculate the company value and the synergy value if the companies are combined. The research method used is Discounted Cash Flow - Free Cash Flow to Equity and Relative Valuation - Price to Book Ratio. The data used are the financial statements of each bank from 2014 to 2019 which are available on the Indonesia Stock Exchange (IDX) or the websites of each bank.

Free Cash Flow to Equity (FCFE) is the amount of cash that can be paid by a company to shareholders after deducting all expenses, reinvestments, and debt payments (Gardner et al., 2012). In the banking sector, the capital structure consists only of the cost of equity. There is no cost of debt because the bank is an intermediary institution where the liabilities or debt positions come from third parties or from bank customer deposits. In addition, operational and financing decisions cannot be separated from interest, besides income and expenses (part of financing) are important elements in bank operating income (Anggelopoulos, 2017). Calculation of Cash Flow to Equity according to Anggelopoulos (2017) is as follows:

FCFE = Net Income + Depreciation – Net Increase in Loans - Net Increase in Securities and Investment – Net Increase in in Amounts due from banks – Net Capital Expenditure + Net Increase in Deposits + Net Increase in Interbank Fund

Stock market value and book value or Price to Book Value (PBV) can be used to measure company value, the greater the company value, the greater the PBV ratio, the higher the company is valued by investors. Companies that have run well will generally show the ratio reaches above one, which indicates that the stock market value is greater than its book value (Husnan, 2010). Price to Book Value is formulated by:

$$\text{Price to Book Value} = \frac{\text{Market Price}}{\text{Book Value}}$$

A higher ratio indicates that investors place a higher value on every investment made in the company by its general shareholders. This ratio shows the valuation of the company's shares relative to the investments made by shareholders in the company (Sheridan Titman, et al. 2018).

The formula for the synergy value according to Ross, et al. (2012) is: Synergy = VAB – (VA + VB) Where VAB = Value of firms when combined VA = Value of firm A VB = Value of firm B

RESULT AND DISCUSSION

The growth of Islamic banking assets continued to decline from 2016 to 2019. Despite the decline, the growth of Islamic banking assets is still in the positive quadrant. The growth of Islamic banking assets was recorded at 20,28% (yoy), 18,97% (yoy), 12,57% (yoy) dan 9,39% (yoy) from 2016 to 2019, respectively. Meanwhile, in Q1 and Q2 2020, asset growth also showed a decrease of 9,53% (yoy) and 9,22% (yoy). This is inversely proportional to conventional banks which only recorded 5,5% in the first quarter of 2020. In Q1 and Q2 2020 Third Party Funds (TPF) Islamic banks recorded 9,24% and 8,99% while for Distribution of Financing 2-digit numbers of 10,14% and 10,13%. For conventional banks, TPF and distribution of financing were recorded at 8,87% and 3,04% respectively in Q1 2020. In June 2020, Islamic banking market share of 6,18% consisting of Islamic Commercial Banks of 65,33%, Sharia Business Unit of 32,17%, and Islamic People's Financing Bank (BPR) of 2,50%. Total Islamic banking assets amounted to Rp 545,39 trillion with details BUS Rp 356,33 trillion, UUS 175,45 trillion and BPRS 13,61 trillion. Meanwhile, Indonesia's total Islamic financial assets in June 2020 reached Rp 1.608,50 trillion or USD 112,47 billion (Rp 14.302/USD) from Indonesia Islamic Banking amounting to Rp 545,30 trillion, IKNB Syariah at Rp 107,22 trillion and Sharia Capital Market 955,89 trillion with an increase of 20,4%.

The valuation of BRIS, BSM, and BNIS banks uses 2 methods, namely the first, Discounted Cash Flow (DCF) with an approach Free Cash Flow to Equity (FCFE) if the cash flow received by each company will experience growth with a certain level of growth and within a certain period of time, where it is assumed that the growth of cash flow occurs within the next 5 years. And secondly, Relative Valuation (RV) with Price to Book Value (PBV) approach using the comparison of the value of each company with other banking companies listed on the Indonesia Stock Exchange (IDX).

In the FCFE calculation the discount factor to be used in the cost of equity is the first, Risk Free Return (RF) with serial number FR0037 with a rate of 12%. Second, the market risk premium based on Damodaran's total equity risk premium for Indonesia is 7,08%. Third, the beta calculation of each company as shown in table 1 below.

Table 1. Company Beta Valuation

BRIS			BSM			BNIS		
FIRM	BETA	DER	FIRM	BETA	DER	FIRM	BETA	DER
BBRI	0,07	5,78	BMRI	1,58	5,00	BBNI	2,11	5,80
BDMN	0,26	3,36	BBCA	0,93	4,33	BBTN	2,53	11,97
BTPN	0,35	0,43	BBTN	2,53	11,97	BSIM	0,33	5,60
BBCA	0,93	4,33	PNBS	0,66	0,43	BBKP	2,44	10,20
MEGA	0,14	5,29	BNGA	1,56	5,54	BDMN	0,26	3,36
Average	0,35	3,84	Average	1,45	5,45	Average	1,53	7,39
	DER BRIS	2,53		DER BSM	1,93		DER BNIS	2,53
	Tax Rate	22%		Tax Rate	22%		Tax Rate	22%
	Unlevered	0,09		Unlevered	0,28		Unlevered	0,23
	Levered	0,28		Levered	0,70		Levered	0,68

Source: Data Processed (2020)

Fourth, after calculating the beta of each company, then calculate the cost of equity by using the CAPM model. The calculation of cost of equity is listed in table 2.

Table 2. Cost of Equity

Company	Rf (1)	Beta (2)	RP (3)	CAPM (4) = 1+(2*3)
BRIS	12%	1,35	7,08%	21,56%
BSM	12%	0,70	7,08%	16,96%
BNIS	12%	0,68	7,08%	16,81%

Source: Data Processed (2020)

After knowing the Cost of equity from table 2, then look for the Price to Book Value (PBV) of each bank in 2019 as stated in table 3.

Table 3. Price to Book Value

Company	Total Equity (IDR) (1)	Book Value per Share (IDR) (2)	PBV (IDR) (3) = (1)/(2)
BRIS	5.088.036.000.000	9.716.113.498	524
BSM	9.245.835.000.000	628.4037.36	14.713
BNIS	4.735.076.000.000	2.921.335	1.620.860

Source: Data Processed (2020)

Calculate the Compound Annual Growth Rate (CAGR) historically by using the income data contained in each company's financial statements from 2014 to 2019. This CAGR is used for growth rate in FCFE calculations. Based on the CAGR calculation, it was obtained that BRIS revenue growth was 10,41%, BSM was 8,94%, and BNIS was 15,04%. As for the company value listed in table 4.

Table 4. Company Valuation

Firm	Total Shares	Value of Company per Share	Jumlah Liabilities (in million/IDR)	Cash (in million/IDR)	Value of Company
BRIS	9.716.113.498	500	11.880.036	262.485	16.475.607.749.000
BSM	628.403.736	5000	19.052.303	1.591.962	20.602.359.680.000
BNIS	2.921.335	1.000.000	13.072.213	355.843	15.637.705.000.000

Source: Data Processed (2020)

The next step is to calculate the company's synergy with the following stages: First, the growth of bank mergers is assumed with the average income growth of each bank, with an income growth rate of 11,46%, while for the terminal growth rate is assumed to be 5,02 % where this figure is the rate of economic growth in Indonesia in 2019. Second, beta BRIS, BSM, and BNIS will be a comparative beta and beta bank merger is calculated using a report on the performance of the Bank's financial position as of June 30, 2020. The calculation is shown in table 5.

Table 5. Bank Merger Beta

Company	Beta	DER
BRIS	1,35	2,53
BSM	0,70	1,93
BNIS	0,68	2,53
Average	0,91	2,33
DER Bank Merger		2,56
Tax Rate		22%
Unlevered		0,32
Levered		0,96

Source: Data Processed (2020)

Third, after the beta of the merger bank is known to then calculate the cost of equity using the CAPM model. If the Risk-Free Rate (R_f) is 12% and risk premium is 7.08%, with the calculation of CAPM model as follows: $CAPM = R_f + (\beta \times R_p)$

$$CAPM = 12\% + (0,96 \times 7,08\%)$$

$$CAPM = 18,79\%$$

Fourth, calculate the PBV of the bank's merger results based on the report on the performance of the Bank's financial position as of June 30, 2020 as stated in table 6 as follows:

Table 6. Price to Book Value Bank Merger

Company	Total Equity (IDR) (1)	Book Value per Share (IDR) (2)	PBV (IDR) (3) = (1)/(2)
Bank Merger	20.417.623.000.000	40.846.813.743	499,86

Source: Data Processed (2020)

Based on table 6 above obtained stock valuation Islamic bank merger by 1x. Bank merger valuation results are shown in table 7.

Table 7. Value of Synergy

Value of Bank Merger	70.701.783.871.500
Value of Combination	52.715.672.429.000
Value of Synergy	17.986.111.442.500
PBV	499,86
Equity Book Value	214.649.424.000.000

Source: Data Processed (2020)

CONCLUSION

Based on calculation using DCF-FCFE method, the company value of BRIS is Rp 16.475.607.749.000, the company value BSM is Rp 20.602.359.680.000, and the company value of BNIS is Rp 15.637.705.000.000. While for PBV BRIS of 524, PBV BSM of 14.713, and for PBV BNIS of 1.620.860. Islamic bank merger valuation based on DCF-FCFE method of Rp 70.701.783.871.500 and the combined value of the company Rp 52.715.672.429.000, so that the synergy value obtained is Rp 17.986.111.442.500. Thus, the merger of this company is worth doing. The merger of the three Islamic banks will be the largest Islamic bank in Indonesia in terms of assets with total assets of Rp 214,6 trillion and will rank 7th or 8th in the list of top 10 largest banks in Indonesia in terms of assets. In addition, the bank because of this merger will have a core capital of Rp 20,4 trillion and will be included in BUKU III.

The conclusions section shall consist of answers to research problems, limitations of the study, managerial implications, and future research recommendations.

This study has several limitations, namely the study only analyzes bank mergers based on financial measures without paying attention to non-financial measures and the researcher only focuses on Islamic banks. Further research can conduct merger analysis using non-financial measures and for financial measures, other methods such as free cash flow to firm or free cash flow to equity can be used.

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