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*Conceptual Paper*

# Strategic Management of Islamic Banking in Indonesia to Increase Market Share

**Muhammad Ali Imran Caniago [1*]**
[1] Sunan Kalijaga State Islamic University, Yogyakarta
* Correspondence: aliimranc7@gmail.com; Tel.: 0822-7787-2027

**Abstract**

Indonesia is a country with the largest Muslim population in the world. The large Muslim population has not been able to make Indonesia the center of the world's sharia economy. One component of the Islamic economy in Indonesia is Islamic banking. The market share of Islamic banking in Indonesia is still very small, so the competition for market share in national banking is still won by conventional banks. This study aims to identify the market share of Islamic banking in Indonesia and strategies for developing and increasing the market share of Islamic banking to contribute to the national economy and development. The method used in this study is a qualitative method with a descriptive analysis approach. Data is collected through library research. The results of the study show that several strategic issues impede the growth of Islamic banking in Indonesia, namely: Islamic banks do not yet have a significant business model or product differentiation, Islamic bank literacy and inclusion indexes are still low, Islamic banks are still only focused on business objectives, The quantity and quality of Islamic Bank human resources are not optimal, and information technology is not yet sufficient. Knowing these strategic issues, three strategies are formulated in the development of Islamic banking: Strengthening Islamic Banking Identity, Synergy of the Islamic Economic Ecosystem, and Strengthening Licensing, Regulation, and Supervision.

**Keywords:** Strategic Management; Islamic Bank; Market Share.

## 1. Introduction

The first establishment of a Shariah bank in Indonesia was marked by the establishment of Bank Muamalat in 1991, which officially started operating in May 1992. Since the enactment of Law Number 7 of 1992 on Banking, which stated that banks operating on profit-sharing principles, later replaced by Law Number 10 of 1998 on the amendment of Law Number 7 of 1992 on Banking, Shariah banking has been recognized. Ten years later, in 2008, the government issued Law Number 21 of 2008 on Shariah banking, which specifically regulates Shariah banking. In 2023, the government issued Law Number 4 of 2023 on the development and strengthening of the financial sector (Pemerintah Indonesia, 2023), which made some changes that ultimately replaced the previous laws. The purpose of the issuance of this law is to develop and strengthen the national financial system. The law regulates the overall financial institutions and systems in the country, both conventional and Shariah systems. The comparison of the number of conventional banks with Shariah banks in Indonesia is still very far apart, based on data released by the Central Statistics Agency as follows:

*Figure 1*

*Number of Conventional Banks and Sharia Banks in Indonesia 2008-2022*

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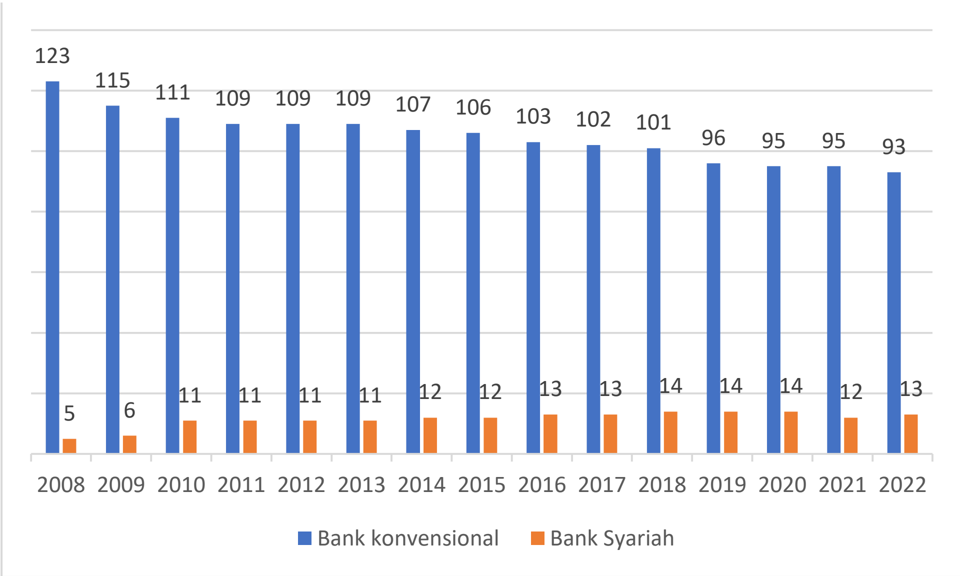



*Source: Indonesian statistic center*

From 2008 until 2022, the number of conventional banks is still greater than that of Islamic banks in Indonesia, even though the Law Number 21 of 2008 on Islamic banking has specifically regulated Islamic banking in the country. This law was expected to accelerate the growth of Islamic banking in Indonesia, especially with the provision that obligates the spin-off of Shariah business units from their conventional parent banks when their assets reach 50% of the parent bank's assets, and the spin-off obligation must be fulfilled no later than June 2023. However, this law has been replaced by the Law Number 4 of 2023, which removes the provision on the spin-off requirement.

On the other hand, Indonesia is the country with the largest Muslim population in the world. In 2022, the Central Statistics Agency released data stating that the population of Indonesia is 275,773,800 people (Statistik, 2023). According to the Royal Islamic Strategic Studies Centre (RISSC), in 2022, the Muslim population in Indonesia was 237.56 million people, or 86% of the total population. With such a large Muslim population, Islamic banking in Indonesia should be able to dominate the banking market in the country. However, this large Muslim population has not yet made Islamic banking a bank with a large market share.

Generally, the performance of Islamic banking can be evaluated based on three indicators: total assets, third-party funds (DPK) collected, and financing disbursed by the bank (Hidayat & Trisanty, 2020).

*Table 2*

*Total assets, Disbursed Financing (PYD), Third Party Funds (DPK), and Market share of sharia banks 2018-2022 (trillion Rupiah)*

| **Unit/Year** | **2018** | **2019** | **2020** | **2021** | **2022** |
|---|---|---|---|---|---|
| Total Asset | 489,69 | 499,34 | 608,9 | 646,21 | 686,29 |
| Disbursed Financing | 329,28 | 342,81 | 394,63 | 413,31 | 440,78 |
| Third Party Funds | 379,96 | 394,72 | 475,79 | 503,83 | 548,26 |
| Market share | 5,96% | 5,95% | 6,51% | 6,52% | 6,62% |

*Source: sharia banking snapshot, OJK*

The data table above shows a positive trend in the growth of assets, financing (PYD), and third-party funds (DPK) in Islamic banking from 2018 to 2022. However, despite this growth, the market share of Islamic banking is still very low. In 2022, Islamic banking only had a market share of 6.62%, while conventional banks dominated the remaining 93.38%.

The government has taken several steps to promote the growth and development of Islamic banking in Indonesia, such as merging several HIMBARA Islamic commercial banks into one to increase capitalization and accelerate the growth of Islamic banking and the economy in Indonesia. On the other hand, there is a need for strategies to develop Islamic banking further to make a significant contribution to the national economy and development. Previous studies have shown that marketing strategies impact banking performance (Rianto, 2021)and can also increase the number of banking customers (Siregar, 2015). Based on the above presentation, this study aims to identify the market share of Islamic banking in Indonesia and develop strategies to increase this market share to contribute to the national economy and development.

## 2. Theoretical Review

This section may be divided by subheadings. It should provide a concise and precise description of the experimental results, their interpretation, as well as the experimental conclusions that can be drawn.

### A. Strategic Management

According to Fred R. David & Forest R. David, Strategic Management is the art and science of compiling, formulating, implementing, and evaluating cross-functional decisions to achieve company goals (David & David, 2015). Strategic Management in the form of unifying management of marketing, finance, production, research & development, as well as management of information systems whose goal is to achieve company success (Taufiqurokman, 2016).

#### 1) Stages Of Strategic Management Preparation Stages

There are several stages in preparing strategic management: formulation, implementation, and evaluation.

a. Formulation of strategy: This includes preparing the company's vision and mission, identifying company opportunities and challenges, identifying company strengths and weaknesses, making company long-term goals, making alternative strategic steps, and choosing the right strategy.
b. Implementation of strategy: setting the company's annual goals, determining policies, motivating employees, and allocating resources so that the company's strategy formulation can be implemented. In addition, strategy implementation includes developing a culture that supports strategy, developing effective organizational structures, optimizing marketing, preparing budgets, developing and maximizing information systems, and linking employee compensation to company performance.
c. Strategy evaluation: At this stage, the manager will review the internal and external factors of strategy formulation and implementation. Then measure performance and take corrective action. This evaluation phase must be carried out continuously by considering changes in the company's internal and external environment.

#### 2) Strategy Level

a. Corporate strategy (Corporate Strategy): This strategy is determined by the highest management in a company and leads to business orientation and utilization of resources. This strategy relates to the company's long-term goals.
b. Business strategy: This strategy is set at the business unit level of corporate strategy. Business-level managers formulate this strategy through negotiations with corporate managers.

c. Functional level strategy: This strategy has a smaller scope than business and corporate level strategies. This strategy is within the divisional divisions of the company. Such as HR, finance, marketing, and research & development divisions.

**3) Characteristics of Strategic Management**

There are several distinguishing characteristics between strategic management and other management, namely: Strategic Management aims for the long term, is dynamic, integrates with operational management, is initiated by high-level managers of the company, is future-oriented, and Strategic management must be encouraged and supported by available economic resources

**4) Benefits of Strategic Management**

There are several benefits that companies will get when they implement Strategic Management, namely: directing the company's long-term goals, helping companies adapt to changes that occur, increasing company effectiveness, identifying company comparative advantages in risky environments, with the formulation of a strategy that will make companies able to prevent problems in the future, motivating company employees because they are involved in preparing company strategy, reducing overlapping activities, and reducing employee reluctance to change.

**5) Steps In the Development of The Company**

a. Identify activities that must be carried out directly or indirectly, from preparing activity proposals, testing & assessment, planning, implementation, control, and supervision processes.
b. Analyzing company profiles by looking for linkages from various activities, both main activities and supporting activities
c. Looking for potential synergies that arise from every activity owned by the company.

**6) Strategic Environment**

Strategic Management is all about gaining and maintaining a competitive advantage. This means that everything that can only be done in particular by one company without being able to be done by a rival or competitor company can be considered superior in the competition. To gain a competitive advantage, a company needs to pay attention to the strategic environment because, in this strategic environment, the strengths and weaknesses of the company's internal factors and opportunities and threats from external factors will be identified (David & David, 2015).

**a. Internal strengths and weaknesses**

Internal strengths and weaknesses arise in management, marketing, finance or accounting, production or operations, research and development, and management information systems activities. Strengths and weaknesses are determined relative to competitors. Internal factors can be measured in various ways, such as calculating ratios, performance, employee work ethic, product efficiency, advertising effectiveness, and customer loyalty.

**b. External threats and opportunities**

External threats and opportunities refer to economic, cultural, social, demographic, environmental, legal, political, governmental, technological, and competitive trends and events likely to benefit or disadvantage a company significantly. On the other hand, opportunities and threats can include articles in the law, social disasters, declining currency values, and competitors' introduction of other products. The basic principle of Strategic Management is that companies must formulate strategies to take advantage of external opportunities and reduce or avoid the impact of external threats. Companies need to identify, monitor, and evaluate the company's external opportunities and threats to achieve success.

**B. Sharia Banking**

Based on Law Number 4 of 2023 concerning the development and strengthening of the financial sector, a Bank is a business entity that collects funds from the public in the form of savings and distributes them to the public in the form of credit and or other forms, in order to improve the standard of living of the general public. From now on, Sharia Banks are Banks that carry out their business activities based on Sharia Principles and by type consist of Sharia Commercial Banks and Sharia People's Financing Banks.

In Indonesia, the banking system can be divided into two systems: conventional banking and Islamic banking. Functionally, conventional banking and Islamic banking are the same. It is just that the most basic differentiator is that Islamic banks carry out their business activities based on Sharia principles. In contrast, Sharia principles are based on the Qur'an and hadith. Furthermore, the basic principle of Islamic banking is the prohibition of maysir, gharar, and usury. The orientation of Sharia banking is not just worldly business but achieving falah (happiness in the world and the hereafter) so that the orientation of the world and the hereafter is clear.

In general, the function of a bank is as a business entity or intermediary institution, namely collecting funds from the community and channeling them back to the community in the form of credit or financing (Darmawan & Fasa, 2020). In the theory of financial intermediation, banks act as intermediaries who function as a medium for collecting deposits and lending these deposits to benefit from loan interest (Chowdhury & Haron, 2022).

On the fundraising side, Islamic banking offers products with a profit-sharing principle that aims to attract people to save their funds in Islamic banking. Products usually offered are in the form of savings, current accounts, and time deposits. So that people's needs to save and invest in banks are met. Savings are deposits or third-party funds whose withdrawals can only be made as agreed upon and cannot be withdrawn using a check, current account receipt, or equivalent device (Brilian & Rohman, 2023). Current accounts are deposits or third-party funds whose withdrawals can be made anytime using checks, current accounts, and other payment order media. Deposits are a type of savings that have a minimum balance requirement for a certain period. Customers cannot withdraw their cash before the specified maturity date. Apart from functioning as a savings account, deposits can also be used as an investment (Linda, 2022). In principle, Islamic banking fundraising products use two contracts, namely wadiah and mudharabah (Pradesyah, 2019).

On the other hand, Islamic banking also distributes financing as a business. Financing is funding support for requesting or procuring certain goods/assets/services. The mechanism usually involves the donor, the provider of certain goods/assets/services, and the party who utilizes certain goods/assets/assets/services. Financing channeled by Islamic banks principally uses sale and purchase agreements (bai'), leasing (ijarah), and the principle of profit sharing or cooperation (Pradesyah, 2019). The products offered by Islamic banks with sale and purchase agreements: Murabahah, istishna, and salam. In cooperation products, Islamic banks use mudharabah and musyarakah contracts. In leasing products, Islamic banks use ijarah Munltahia bittamlik (IMBT) contracts, while Islamic bank financial services products offer products with wakalah, kafalah, hiwalah, rahn, qardh, and sharf contracts (Mashuri, 2015).

Islamic banking as a commercial institution has a company vision and goals in the short, medium, and long term. To achieve this vision and goal, Islamic banking must develop Strategic Management that provides guidelines, descriptions, and ways to achieve its goals following its vision and mission (Ritonga, 2020). There are several best ways to formulate banking strategy management according to (Sri Anugerah Natalina & Arif Zunaidi, 2021), namely:

1) Identify the environment to be penetrated; The meaning of penetration here is the environment you want to penetrate because by identifying prospective market share environments, Islamic banks can determine their vision and mission. The more focused the vision and mission, the clearer the choice of corporate strategy will be.
2) Analyzing the company's internal and external environment; This analysis aims to determine the company's weaknesses and strengths and measure opportunities and threats from outside the company or competitors. With the results of this analysis, it will be easier for the company to realize the vision and mission that has been made
3) Determine indicators of success of the strategies that have been made; This is so that when indicators of success have been achieved, they can move on to other strategies.
4) Evaluate company goals and targets; If the company experiences difficulties in achieving the targets and goals set, then the company makes another alternative strategy. Because the company's targets and goals are prepared with the consideration of the company's resources. Likewise, with external factors, companies must pay attention to competitors as a comparison
5) Choose short-term and long-term company strategies; This election aims to determine the desired achievement of the company in the short term and long term.

**C. Market Shares**

Market share is a marketing strategy that divides a comprehensive target market into small subsets, such as consumers, companies, or countries with similar requirements, interests, and priorities, and targets them. Depending on the specific demand, market share is usually applied to the target market analysis of each product segment (Niswah & Tambunan, 2022). Market share, or market share, is the percentage of market control by a company from the total area of the market as a whole. Market share is used in measuring the performance of competing companies. In banking, market share can be measured from banking assets, disbursed financing, and the collection of third-party funds (Hidayat & Trisanty, 2020). Factors influencing market share are inseparable from the company's internal factors, such as asset turnover rate, productivity level, total assets, operational cost control, and company profitability level (Setyowati, Sartika, & Setiawan, 2019).

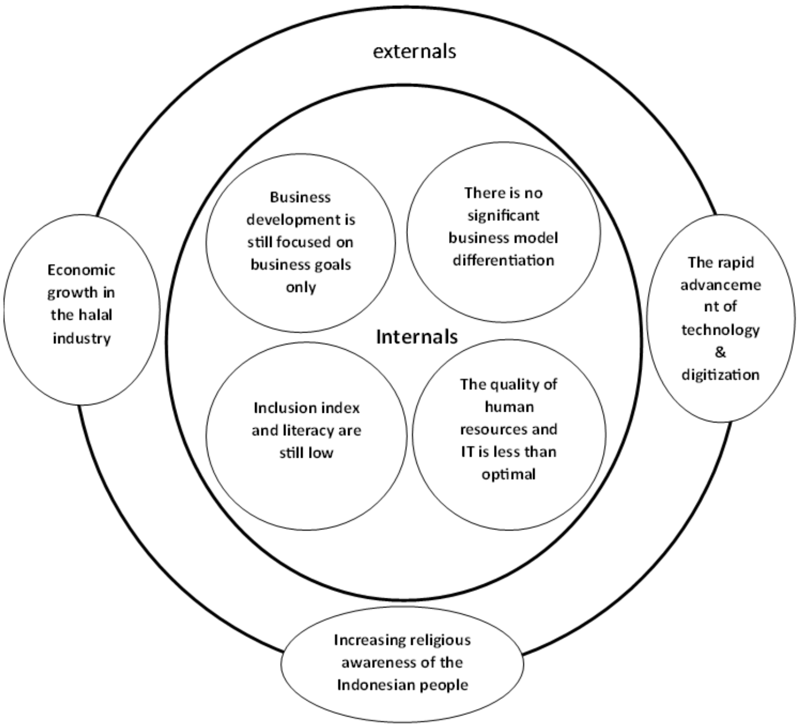
**D. Strategic Environment of Islamic Banking**

In the development of Islamic banking in Indonesia, some factors influence its development. These factors come from internal banking itself and external factors from banking. These internal factors are in the form of internal strengths and weaknesses of Islamic banking, such as the absence of significant business model differentiation, business development that is still focused on business objectives only, quality of human resources and IT that is less than optimal, as well as the index of inclusion and literacy which is still low. On the other hand, external factors in the form of opportunities and challenges have also influenced the development of Islamic banking itself, such as the rapid advancement of technology and digitalization, economic growth in the halal industry, and the increasing religious awareness of the Indonesian people (OJK, 2020).

From the presentation of David & David's strategic environmental theory (2015) and the 2020-2025 sharia banking roadmap issued by OJK (2020), the strategic environment consists of internal and external companies. Then a picture of the strategic environment of Islamic banking can be made as follows:

*Figure 2*

*Strategic Environment of Islamic Banking*




## 3. Methods

This type of research is qualitative research with a descriptive analysis method. In data collection, researchers used the literature study method, which collected data from various existing writings, books, articles, banking financial reports, and writings from various related agencies. Then the researcher sorts and selects data related to the theme of this research. After collecting the data, the researcher develops a theory related to the research variable. Furthermore, researchers analyzed descriptively the data and theories that had been compiled. Then the researcher interpreted the analysis results and concluded the research results.

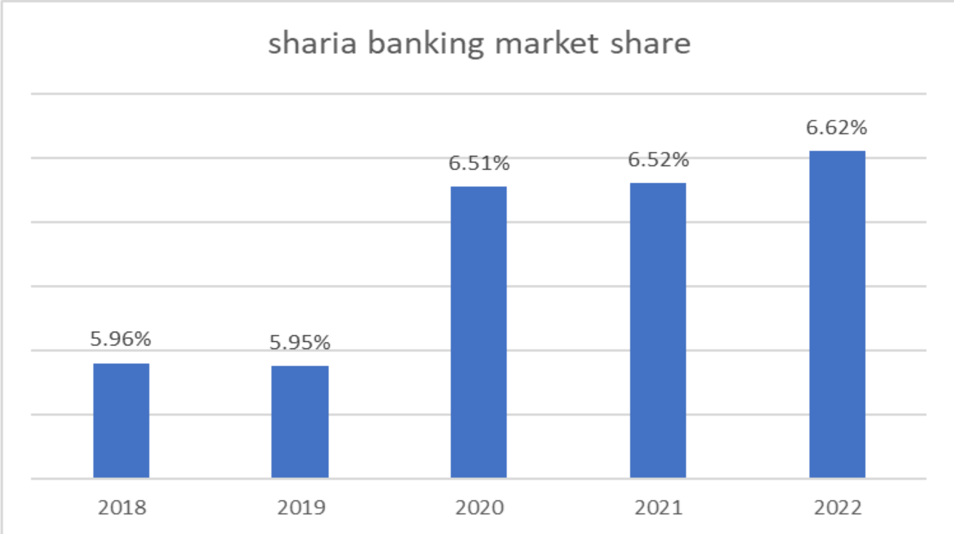
## 4. Results

### A. Market Share of Sharia Banking

Islamic banking in Indonesia has entered the age of three decades, marked since the establishment of Bank Muamalat in 1992. Until 2022, Islamic banking is experiencing growth. One indicator of Islamic banks' growth is looking at their market share. Market share is the percentage of market control by a company from the total market area. There are three indicators in measuring the market share in banking: total assets, third-party funds (DPK) collected, and financing disbursed by banks (Hidayat & Trisanty, 2020).

*Figure 3*

*Indonesian Sharia banking market share*




*Source: sharia banking snapshot, OJK*

In the last five years, 2018-2022, the market share of Islamic banking has shown a positive trend. A sharp increase occurred in 2020, when the HIMBARA Islamic commercial banks, namely: Bank Syariah Mandiri, BNI Syariah, and BRI Syariah, merged to become Bank Syariah Indonesia or BSI. The market share growth has not been able to keep up with the large market share of its competitor banking, namely conventional banking. If seen in 2022, the market share of Islamic banking in Indonesia is only 6.62%. This means 93.38% market share of the national banking industry is dominated by conventional banking.

There are several reasons for the low market share of Islamic banking in Indonesia (Barmana, 2015), namely:

1) Understanding and knowledge of Islamic banking are still very low; for example, some religious leaders lack adequate knowledge of Islamic economics and hold biased opinions about Islamic banking.
2) There is no significant Joint Movement to promote Islamic economics.
3) Lack of experts and human resources
4) The government's contribution to fostering and developing the Islamic economy is still minimal.
5) The role of the clergy is still relatively small. So far, scholars who have struggled to propagate Islamic economics have been limited to the National Sharia Council and certain academic circles
6) Islamic banking academics have not been maximized in several universities, including Islamic universities.
7) In promoting Islamic banks to the public, Bank Indonesia and Islamic banks do not yet have a precise and effective strategy.

**B. Strategic Issues in Islamic Banking Development**

Several factors still hamper the development of Islamic banking in Indonesia. In the 2020-2024 Islamic Banking Roadmap issued by the OJK (2020), there are two strategic issues faced by Islamic banking in Indonesia, namely: the issue of Sharia compliance and low competitiveness. Furthermore, Abubakar & Handayani (2018) mentions that strategic issues that hinder the development of Islamic banking are the quantity and quality of human resources, which are still low in ensuring compliance with Islamic principles and misunderstandings and low levels of trust in Islamic banking products and services. Furthermore, the results of research by Nor Firman & Alwi (2020), strategic issues that impede the growth of Islamic banking are: a. the absence of varied products and services that are still not following the expectations of society, b. the quantity and quality of human resources are still low, c. low public understanding and awareness, causing misperceptions of sharia banking, d. views on the high cost of transactions in Islamic banking, e., regulation and supervision of Sharia banking is not yet optimal.

### C. Sharia Banking Development Strategy

In order to develop and increase the competitiveness of Islamic banking, the Financial Services Authority of Islamic banking practitioners, customers, academics, regulators, and business actors develop strategies for dealing with competition in the national banking industry, where this strategy is compiled in the Islamic banking roadmap 2020-2025. The vision of this strategy is to create Sharia banking that is resilient, highly competitive and contributes significantly to the national economy and social development. Three strategies are formulated in the development of Islamic banking: Strengthening Islamic Banking Identity, Synergy of the Islamic Economic Ecosystem, and Strengthening Licensing, Regulation, and Supervision (OJK, 2020).

**1) Strengthening Islamic Banking Identity**

**a. Strengthen Sharia values**

Sharia values are the cornerstone of Islamic banking and must be applied to every aspect of the industry, including business practices and human resource management. In the eyes of the public, who are now more aware of practicing religion correctly, a more comprehensive application of Sharia values will create a more integrated, professional, and disciplined Sharia banking identity. In strengthening Sharia values, several strategies can be carried out, namely:

**a) Encouraging the establishment of a Code of Conduct and Competency Standards for Sharia Bankers**

Sharia values must be integrated into Islamic banking operations and embedded in all Islamic bank employees as a social norm. In order to provide a positive customer experience towards the application of Sharia principles in Sharia banking, these Sharia ideals must also be reflected in the services offered to consumers. They are making a code of ethics for Sharia bankers, which forms the basis for patterns of rules, procedures, and ethical guidelines in carrying out work as Sharia bankers. It is one way to instill Sharia values in employees. Islamic bankers must also apply for competency certification of Islamic bankers to increase their professionalism and abilities. For the code of ethics and competency standards to be successfully implemented, periodic monitoring and evaluation of the process must be carried out.

**b) Strengthening the Implementation of the Compliance Function and Internal Audit on Compliance with Sharia Principles**

The Sharia Supervisory Board and all organs of Islamic banking are responsible for upholding Islamic principles in the industry. Internal audit compliance and responsibility support more effective supervision of Sharia principles. Non-compliance with Sharia principles has an impact on individual Islamic banks and also hurts the industry's image. In order to properly protect the reputation risk of the Sharia banking sector, supervisory policies that focus more on Sharia compliance risk need to be improved.

**b. Develop Unique, Highly Competitive Sharia Products**

Islamic banking should be responsible for the creation of new Sharia-compliant products. Excellent products, unique, and cannot be applied in conventional banking is one of the benefits that must be utilized by Islamic banking. Industry players and regulators need an innovative and creative product development paradigm to develop distinctive products to win over consumers.

a) **Encouraging product development that can provide added value to customers**
Through the creation of products that provide added value for customers and have practical and spiritual benefits, such as bundles of Islamic banking products with social-religious fund products such as endowments, zakat, infaq, and alms, Islamic banking products can have competitiveness. In addition, Sharia banking products must meet all customer needs. Islamic banking is expected to be the first choice for all customers by encouraging the development of various features of Islamic banking products that can be adapted to customers' needs and life cycles.

b) **Encouraging the Implementation of Products that Support National Priority Programs**
With its characteristics closer to the real sector, Islamic banking must be able to make a greater contribution to the national economy. Existing Sharia banking products will continue to be improved and developed to boost the country's economy significantly. By promoting products such as Krishna financing in the public housing sector or salam financing in supply chain-based industries such as agriculture, processing, textiles, and other industries, Islamic banking can maximize its contribution to developing the government's priority sectors.

c) **Preparing a Legal Basis That Can Accommodate the Acceleration of Product Licensing and Bank Business Activities to Increase Innovation**
OJK will offer an accommodative regulatory environment so market players can encourage innovation and creativity in creating Sharia banking products. One of the steps that can be taken to provide opportunities for the implementation of new products within a certain period so that they can be used as material for licensing evaluations to ensure the continuity and sustainability of these products is to implement piloting reviews in product licensing and review business model planning.

c. **Strengthening Capital and Efficiency**
Strengthening capital must be increased to increase the capacity of Islamic banking in developing its business and facing industry challenges and opportunities, such as the growth of the halal industry and digital disruption. This will increase the competitiveness of Islamic banking. It is also hoped to increase the effectiveness of Sharia banking operations to make it more competitive and open up space for growth.

a) **Capital Strengthening for BUS and UUS Through Consolidation, Additional Capital from the Parent, as well as Subsidiary Development Plans**
The banking consolidation strategy that controls the increase in the minimum core capital of BUS can be used to strengthen capital. In addition, the strategy for strengthening the UUS can strengthen financing capacity to always uphold the principle of prudence by cultivating profits to grow working capital. By assessing BUK's dedication to realizing Sharia banking and reviving the BUS-UUS regulations, OJK is also pushing for an increase in the portion of BUS-UUS to parent BUK. The policy aims to ensure that BUS-UUS is established with a strong dedication to growing Islamic banking.

b) **Strengthening BPRS Capital and Institutions**
OJK has issued a capital strengthening policy through minimum core capital provisions that must be met to create a BPRS industry with a level

playing field and close the gap in business size between BPRS. By strengthening its capital, BPRS will better support regional economic growth. In addition, policies related to BPRS institutions need to be re-evaluated to encourage more competitive BPRS while upholding ethical and Sharia principles.

c) **Improvement of Sharia Banking Efficiency Through POJK Banking Synergy and Apex/Bank Settlement for BPRS**
OJK issued the Banking Synergy POJK to support the synergy and interconnection of Sharia banking with its ecosystem to compete with conventional banking. BUS can use BUK infrastructure under one ownership to improve service access, product quality, and operational efficiency by adopting POJK Synergy Banking. BPRS should boost output and liquidity by forming an APEX with BUS/UUS. APEX will help BPRS complete payment traffic transactions.

d. **Encouraging Digitalization of Islamic Banking**
In a world without borders and faster technological advances, Islamic banking must continue to improve its technological infrastructure to serve its customers faster, more comfortably, and efficiently.

a) **Encouraging the Preparation of IT Infrastructure that Can Support the Implementation of Digitalization of Sharia Banking Through the Implementation of Banking Synergy POJK**
One of the biggest problems in Islamic banking IT is the lack of Islamic Digital Banking Services (LPD) compared to LPDs in conventional banks. This is due to the poor standard of Islamic banking digital services, which is a direct result of the industry's inadequate IT infrastructure. Islamic banking is expected to use POJK synergy banking to analyze the gap between existing LPDs and parent bank LPDs, map these gaps, and create action plans for new services, to optimize conventional parent bank infrastructure.

b) **Preparing Policies that Support the Implementation of Digitalization of Islamic Banking with the Latest Technology**
Digitalization can increase Islamic financial inclusion. Online customer onboarding and e-forms can broaden public access to Islamic banking. Digitization services accelerate client interaction and increase access. Customers can use the Application Programming Interface and Quick Response Code Indonesian Standard (QRIS) to carry out Islamic banking activities anywhere and anytime. In the post-Covid-19 normal era, Islamic banks need policies to accelerate digitalization to remain competitive.

c) **Encouraging the Application of the Common Platform to Support BPRS Digitalization**
Implementing a shared platform that allows large and small banks to share IT infrastructure to support digitalization is one alternative strategy that can be used. It allows banks to continue implementing digital products and services at a lower cost.

d) **Encouraging the Development of Funding and Financing Modules following the Characteristics of Sharia Contracts**
Islamic banks must have different modules because Islamic contracts have different funding and financing characteristics. Operational procedures separate this special module for Islamic banks, such as margin calculations and profit sharing. OJK encourages Sharia banks to create funding and financing modules based on Sharia contracts for operational procedures such as recording, calculating, and reporting. Digitalization and millennial domination require unique new ideas. Islamic banks aim

to capture these ideas through hackathons and matching businesses with technology start-ups.

2) **Sharia Economic Ecosystem Synergy**

The four main sectors in the Islamic economic ecosystem are the halal industry, Islamic financial services, Islamic social finance, and the religious sector. The Islamic economic ecosystem is a container that can facilitate the four sectors by linking economic activities with Islamic financial transactions that occur within the ecosystem. All financial activities in an Islamic economic ecosystem must utilize Islamic financial services, which require synergy and integration of all ecosystem components. Islamic banking must provide highly competitive Islamic financial products and services to meet the demand for financial services in the Islamic economic ecosystem.

a. **Synergy with the Halal Industry**

The halal business is growing rapidly at the national and international levels. The growing halal industry in Indonesia has received attention from various foreign publications. In line with that, the halal industry, including the financial and economic sectors, is currently receiving increasing attention from the government. Islamic finance needs to take advantage of this momentum by providing a significant contribution to the growth of the halal sector in Indonesia.

a) **Encouraging the Increasing Role of Islamic Banking in Financial Transactions in the Halal Industry**

One of the Priority Projects in the 2020–2024 National Medium Term Development Plan (RPJMN), where one of the indicators is the number of industrial estates facilitated, is the creation of infrastructure for the halal sector. Economic and financial operations can occur in the Halal Industrial Zone (KIH). Financial transactions in the halal sector should benefit the most from the contribution of Islamic banks, which carry out their business operations following Islamic principles. In order to encourage everyone involved in transactions in the halal industry to use Islamic banking products and services, it is important to coordinate with the relevant industry and authorities.

b) **Encouraging the Contribution of Islamic Banks in the Value Chain Implementation of the Hajj/Umrah Pilgrimage**

Indonesia has the largest number of pilgrims in the world, with 220 thousand people recorded annually. Likewise, Umrah pilgrims reach 1.3 million per year. This graph shows the enormous potential for collaboration between Islamic banking and financial transfers for Hajj and Umrah activities. Creating an Islamic banking business model that meets the requirements of business owners for Hajj and Umrah trips can initiate this collaboration. In addition, a business match between Islamic banks and the association of Hajj and Umrah travel entrepreneurs is needed to create the best possible collaboration.

c) **Encouraging Sharia Banking to Distribute Sharia Curriculum in MSMEs Financing in Line with Strengthening the Halal Industry**

Micro, Small, and Medium Enterprises (MSMEs) dominate the business landscape in Indonesia. The majority of these companies operate in the halal field. Islamic banks have a great opportunity to finance this industry because there are over 50 million MSMEs. The Sharia KUR scheme is one of the financing plans that must be increased to support this industry. The MSME sector is expected to take advantage of this program by adopting a cutting-edge business model that more accurately represents the uniqueness of sharia and responds to community needs.

d) **Encouraging an Increase in Transactions Using Sharia Bank Products and Services in Transactions on the Halal Marketplace**
Rapid technological advances have changed people's lives, especially regarding consumption habits. The marketplace, which functions as a platform to meet various community needs, shows this. Conventional shops that only sell directly have changed due to this situation. Halal marketplaces are now starting to appear following this. Islamic banking must be able to take advantage of market advances to offer reliable financial transaction services. This is important for educating halal market participants about Islamic banking products and services. This will make halal market players more aware of the benefits of using Islamic banks as a transaction medium.

b. **Synergy between Islamic Financial Institutions**
Islamic banking must work closely with the Islamic capital market industry and other non-bank financial institutions, including fintech companies, so Islamic finance can progress in Indonesia. Expanding access to Sharia banking services and motivating Sharia banks to participate more actively in the operations of other Sharia financial institutions can be done through cooperation between Sharia banking and other Sharia financial institutions.

a) **Encouraging the Use of Islamic Bank Services Through Synergy with Other Islamic Financial Institutions**
Thanks to information technology, Islamic banks can collaborate to expand their services. Islamic Non-Bank Financial Services Institutions (LKJNB) must use Islamic banking for operations and investment. Sharia institutions can lend and provide Lender Fund Account (RDL) services to fintech peer-to-peer loans. Islamic banks and Micro Waqf Banks can open Islamic bank accounts for people who do not have bank accounts.

b) **Encourage Sharia Commercial Banks to be actively involved in Islamic capital market activities**
Islamic stock market assets control over 50% of national Islamic financial assets. Islamic capital market products now dominate the Islamic financial market. Islamic banks must become intermediaries in the Islamic stock market. Banking synergy allows Islamic banks to operate following their parent BUK, enabling more Syariah Commercial Banks to actively participate in Islamic capital markets activities such as custodian banks and placement banks for corporate sukuk yields.

c. **Synergy with Islamic Social Finance Institutions**
According to the 2019 CAF World Giving Index report, Indonesia is the tenth most socially conscious country globally. This is a great opportunity for Islamic banks to be more involved in social growth in Indonesia. Apart from focusing on its commercial function, Islamic banks are currently required to maximize their social functions. One of them is optimizing the function of Islamic banks in managing zakat, infaq, alms, and waqf funds. (ZISWAF).

a) **Optimizing ZISWAF Funds as well as Increasing the Integration of Social Functions of Islamic Banks**
Islamic social finance innovation is developing in management and distribution, allowing Islamic banks to take a bigger position in this field. The administration and distribution of ZISWAF funds must be developed in partnership with Amil Zakat Institutions (LAZ) and nadir (waqf fund managers) to be more integrated with Islamic bank products and business models. Integrating social and commercial finance tasks into Islamic banking will strengthen the distinctiveness of Islamic banking, which will further contribute to the social and economic progress of the country.

b) **Optimizing the Use of Islamic Bank Accounts in Islamic Social Financial Institutions**
The number of Social Finance institutions in Indonesia is, of course, influenced by the high level of social awareness. More than 60 (sixty) Amil Zakat Institutions are registered in Indonesia, according to data from the National Amil Zakat Agency (BAZNAS). This figure does not include other unlisted organizations, such as donation-based crowdfunding platforms. However, not all Islamic social finance institutions collect and deposit funds using Islamic bank accounts. Coordinating with BAZNAS and BWI is very important to assess the issues and challenges of using Islamic bank accounts in social, financial institutions. To further encourage public acceptance of the use of Islamic banks in social fund transactions, socialization and collaboration with BAZNAS and BWI in increasing public knowledge about Islamic banking must also be expanded.

d. **Synergy with Ministries and Institutions**
Islamic banking must be integrated into every strategic work program and other financial operations through collaboration with various ministries and institutions. Islamic banking will contribute more to national economic growth and financial equity for the people of Indonesia.

a) **Encouraging Islamic Banks in the Housing Financing Program**
Building new houses is one of the Ministry of Public Works and Public Housing (PUPR) initiatives, which is included in the 2020–2024 RPJMN. Government and banking assets are sources of money used to build houses. Currently, Sharia banks channel less than 20% of housing construction financing, a very small percentage. For Islamic banks, this presents a challenge and an opportunity to increase the proportion of Islamic banking in the housing finance program; it is necessary to collaborate with the Ministry of PUPR.

b) **Optimizing the Role of Islamic Banks in Supporting Government Programs and State-Owned Enterprises Financial Activities**
Every government and BUMN financial action uses banking products and services. It is promoting Islamic banking to increase its role in the financial operations. Since there are few salary distribution banks in Islamic banking, the increasing number of projects managed by BUMN and financed by State Sukuk requires policy advice to use Islamic banking products and services to facilitate financial transactions in these projects.

c) **Optimizing the Use of Islamic Banks in All Islamic Education Institutions**
Many Islamic schools can be found throughout Indonesia. The Ministry of Religion reports 796 tertiary institutions, 229,000 Islamic boarding schools, and 82,000 Madrasahs in Indonesia. The widespread use of Islamic banks in Islamic universities should reflect their widespread presence. Coordination with the Ministry of Religion is needed to increase the use of Islamic banking products and services in all Islamic academic institutions. Of course, the growth of Islamic banks and the dissemination of Islamic banking knowledge will be greatly influenced by educational institutions, students, and parents of students.

d) **Cooperation with Islamic organizations**
Indonesia has the world's largest Muslim population and many Islamic community organizations (Armas). Islamic organizations must carry out banking transactions. Islamic banking is expected to meet this need, especially in the largest Islamic organizations in Indonesia, such as Muhammadiyah and Nahdlatul Ulama. Encourage Islamic organizations to

use Islamic bank accounts for their cash needs to grow Islamic banking in Indonesia.

**e. Increasing Community Awareness Within the Framework of the Islamic Economic Ecosystem**

In order to increase the customer base and foster wider knowledge of Islamic banking among the public, public awareness of Islamic banking must be continuously increased. If the strategy for increasing inclusion and literacy is only implemented by one industry, then it will not be as effective as it should be. In order to maximize the literacy effect of Islamic banking, all players in the Islamic economic and financial ecosystem need to participate.

**a) Conducting Educational Activities Together in the Islamic Economic and Financial Ecosystem**

The existence of an Islamic economic ecosystem needs to be utilized to increase public awareness of Islamic banking. Together with the stakeholders of the Sharia economic ecosystem, literacy campaigns can be carried out by holding large-scale, national, and international Sharia economic events and expos. Stakeholder collaboration can also be carried out by collecting teaching materials (audio-visual) on Islamic economics and financial literacy. All parties involved in Islamic finance and economics can use this information to promote financial knowledge nationwide via social media.

**b) Increasing Public Awareness of Brand iB**

Since its launch in 2007, Islamic banking branding known as iB (Islamic banking) has been used to identify institutions and branch offices that offer Islamic banking services. It is hoped that it can develop into an Islamic banking identity to increase public knowledge of the availability of Islamic banking services. OJK and Islamic banking will assess whether the iB brand has succeeded in raising public awareness after more than ten years of using the logo. This assessment is expected to follow up the Sharia banking brand campaign more effectively and positively impact all levels of society.

**c) Increasing the Role of Religious Figures in Campaigning for Islamic Banking**

Religious figures are important in educating the public about conducting financial transactions following Sharia principles. It is hoped that by providing training and sermon books in partnership with the Indonesian Mosque Council (DMI), Friday sermons can cover Islamic finance. This will enable religious leaders to emphasize to the public the importance of conducting business according to Sharia principles. Religious leaders with sizable followers are also important in educating the public about the value of Islamic banking in everyday life.

**d) Supporting Implementation of Research Development**

Implementation studies are needed to support the development strategy of Islamic banking. The study of Islamic banking is expected to identify unique business models in line with consumer demands to support strong economic growth. The growth of the Islamic banking sector can be greatly assisted by cooperation with universities in the context of collecting relevant research.

**3) Strengthening Licensing, Regulation, and Supervision**

**a. Acceleration of Licensing Process through Technology Adoption**

With product differentiation, strong capital, and good governance, Islamic banking requires many changes to business processes, organizational management, and capital. Business models and product innovation need to be improved to add value and differentiate Islamic banking. To keep up with the dynamics of change and maintain good institutional governance, OJK will encourage a faster and more responsive licensing process.

a) **Carrying out IT Development to Support the Acceleration of the Licensing Process**
All activities, especially business processes, require IT. Business processes in the licensing process must be evaluated to produce SLAs that are faster while maintaining process quality. Business process efficiency can be implemented by using appropriate and user-friendly IT systems while maintaining the confidentiality of licensing data after various evaluations, such as Business Process Re-engineering. OJK will create an IT-supported licensing system to accelerate SLA and make it easier for OJK and institutions applying for permits.

b) **Evaluating Licensing HR Needs**
Islamic banking continues to grow to attract the interest of banking industry players to increase the number of Islamic banking institutions by establishing new banks, launching Islamic business units, and converting conventional banks into Islamic banks. In addition, the transition to Islamic banking with a differentiated business model demands a lot of product innovation from industry players. These diverse conditions require licensing procedures that are more dynamic and adaptable to the pace of industry changes. Evaluating the number of human resources required to support licensing procedures with appropriate SLAs is critical.

c) **Conduct HR Capacity Building for Sharia Banking Licensing**
Islamic banking should differentiate its products and engage more with the real and social areas of the Islamic economic ecosystem. A fast and dynamic licensing process must be accompanied by productive and high-capacity human resources to keep up with economic and technological dynamics. OJK will always adopt best practices to develop Sharia banking licensing human resources to support business innovation in developing the Sharia industry and economy. This will guarantee fast approval and good governance.

**b. Develop Credible and Adaptive Arrangements**

To increase the growth of the Sharia banking industry, which makes a major contribution to the national economy, OJK plays an important role in building a credible and flexible regulation of the Sharia banking industry. Advances in technology and an increasingly dynamic business environment demand that the Islamic banking industry be more adaptive to change. Regulation is needed to support the development of Sharia banking in dealing with potential disruptions while maintaining stability and resilience.

a) **Formulate Provisions Prioritizing Outcomes and Considering the Characteristics and Complexity of the Bank**
The development of information technology and the business world, which is getting faster and more dynamic after the Covid-19 pandemic, must be addressed by the Islamic banking industry in an agile and adaptive manner. Various service and product innovations, technology adoption, and business process efficiency must be carried out immediately to maintain market competitiveness. To accommodate various dynamics and disruptions that will occur, more adaptive and forward-looking banking regulations are needed. For this reason, regulation must follow a pattern based on principles, be adaptive to changes in the banking structure and ecosystem, and be forward-looking. This principle is intended to provide space for innovation as the industry develops while maintaining stability and prudent considerations. In this regard, OJK will review several provisions that adhere to the rule-based 'extreme' principle, which hinders

the resolution of a problem in certain circumstances. These rule-based provisions will be refined with a principle-based methodology that prioritizes results and considers the bank's characteristics and complexity.

b) **Align provisions with developments in best practice or international standards**
As a result of its growing asset base, the global Islamic banking industry is considered capable of causing global systemic disruption. Maintaining the viability of the global Islamic banking industry requires the standardization of prudential Islamic banking regulations. As a member of the Islamic Financial Services Board (IFSB), the standard-setting body for the Sharia financial industry, OJK will continue to align banking regulations concerning best practices or international standards, following developments in national banking and considering national interests.

c) **Conduct HR Capacity Building for Sharia Banking Regulations**
In the industrial era, Sharia banking must innovate to stand out and contribute to the national economy, especially the Sharia economic ecosystem. To adapt to economic and technological changes, adaptive and agile settings require human resources with a wider range of skills and expertise. For this reason, OJK will continue to increase human resource capacity in managing Sharia banking by keeping abreast of best practice developments and applying various international standards, ensuring reliable and flexible regulations that support business innovation in the sector and support the development of Sharia banking.

c. **Improving Supervision Effectiveness**
Technology-based supervision is OJK's main goal in developing banking supervision. The innovation of Sharia banking financial services and products is increasingly complex. It requires a more responsive pattern of supervision to anticipate potential problems that could disrupt banking in line with strengthening information technology-based supervision. For this reason, OJK will use the latest technology to improve supervision.

a) **Encouraging the Development of Sharia Banking Supervision Tools**
The need for supervisory technology to assist the supervisory process is driven by digital disruption in the financial sector. Information technology can improve the efficiency and usability of controls by streamlining and speeding up data analysis to enable rapid decision-making. In order to keep abreast of technological developments, OJK, as a regulator of Islamic banking, has contributed to implementing technological regulations for Islamic banking regulations. One of the approaches is to make maximum use of technology when conveying Sharia banking information to the OJK. OJK will also use integrated data analysis supported by technology such as data warehousing, big data analytics, and artificial intelligence to support overall supervisory analysis.

b) **Evaluate Organizational and Supervisory HR Needs**
The bigger and more complex the Islamic banking industry, the more supervisory personnel with the capacity to concentrate on analyzing the supervised bank are needed. Every supervised Islamic bank must have adequate human and organizational resources for effective supervision. Taking into account the changes in the Sharia macro and microeconomic climate, which are increasingly demanding the development of a more agile and competitive Sharia banking industry, the completeness of Sharia bank supervisory organizations must be studied further so that Sharia bank supervisors can always keep abreast of developments in the dynamics of the sharia banking business going forward, ensuring banking

stability. Sharia is still achieved by always maintaining the principle of prudence.

c) **Conduct Capacity Building for Sharia Banking Supervisors**
Islamic banking increasingly demands to be more innovative in product differentiation and interact more with the actual and social sectors of the Islamic economic ecosystem. This will make Islamic banking business processes more diverse and complex, requiring supervisors with greater capacity and expertise to keep up with these changes. For this reason, OJK will always build capacity for Islamic bank supervisors by continuously following the development of best practices and applying various existing international standards. This will ensure the acceleration of business innovation in the Islamic banking industry in supporting the development of the Islamic economy is always well supervised by Islamic bank supervisors.

## 5. Conclusions

Indonesia's Sharia banking market share is currently still low; OJK data shows that in 2022 the Sharia banking market share will still be 6.62%. The data shows that the competitiveness of Islamic banking is still low. Several strategic issues impede the growth of Islamic banking in Indonesia, namely: Islamic banks do not yet have a significant business model/product differentiation, Islamic bank literacy and inclusion indexes are still low, Islamic banks are still only focused on business objectives and the quantity and quality of human resources. Islamic banks are not optimal, and Information technology is not sufficient.

To develop and increase the competitiveness of Islamic banking, the Financial Services Authority, Islamic banking practitioners, customers, academics, regulators, and business actors develop strategies to face competition in the national banking industry, where this strategy is compiled in the Islamic banking roadmap 2020-2025. The vision of this strategy is to create Sharia banking that is resilient, highly competitive and contributes significantly to the national economy and social development. Three strategies are formulated in the development of Islamic banking: Strengthening Islamic Banking Identity, Synergy of Islamic Economic Ecosystems, and Strengthening Licensing, Regulation, and Supervision.

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