

CHAPTER IV

THE DEVELOPMENT OF MONEY SUPPLY IN INDONESIA

A. Condition of Dual Monetary System in Indonesia on Financial Sector

Banking regulation in Indonesia was established in 1983. Bank Indonesia provides an opportunity to implement a system that uses interest rates. With hope, the implementation of this regulatory policy can create a more efficient banking condition and strengthen the economic sector. However, in the same year the Indonesian government had planned to be able to implement a system called "profit sharing" for credit, where the profit sharing system was a concept of Islamic banking.

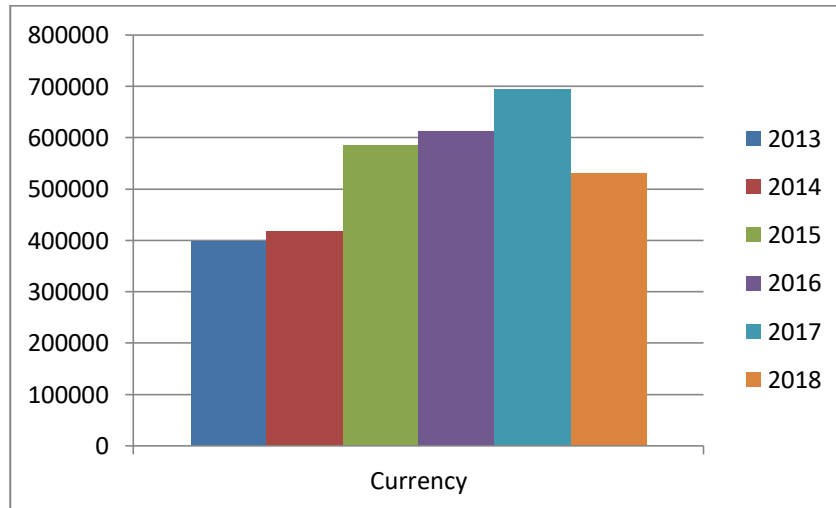
On August 18-20 1990 the Indonesian Ulema Council or well known as (MUI) formed a working group to establish Islamic Banks in Indonesia. Then, the first Islamic bank emerged in Indonesia, namely PT. Bank Muamalat Indonesia (BMI) which was established on November 1, 1991. Which officially began operating with first capital of Rp. 106,382,- on May 1, 1992.

The Government and the House of Representatives formally made improvements with Law No. 7/1992 became Law No. 10 of 1998 which clearly states that there are dual banking system in Indonesia, namely the conventional banking system and the Islamic banking system. Then came several other Islam, such as IFI, Bank Syariah Mandiri, Bank Niaga, Bank BTN, Bank Mega, Bank BRI, Bank Bukopin, and BPD in various regions of Indonesia.

Ratification of several legislative products that provide legal certainty and enhance the activities of the Islamic financial market, such as: (i) Law No.21 of 2008 concerning Sharia Banking; (ii) Law No.19 of 2008 concerning State Sharia Securities (sukuk); and (iii) Law No.42 of 2009 concerning the Third Amendment to Law No.8 of 1983 concerning VAT on Goods and Services. With the enactment of Law No.21 of 2008 concerning Sharia Banking, which was issued on July 16, 2008, the development of the national Islamic banking industry increasingly has an adequate legal basis and will encourage its growth faster. With the progress of its impressive development, which has achieved an average asset growth of more than 65% per year in the last five years, it is expected that the role of the Islamic banking industry in supporting the national economy will be increasingly significant. 11 BUS in less than two years (2009-2010).

Since the development of the Islamic banking system in Indonesia began, in two decades the development of national sharia finance, there has been much progress, both from institutional aspects and supporting infrastructure, regulatory and supervisory systems, and public awareness and literacy of sharia financial services. Our sharia financial system is one of the best and most complete systems that is internationally recognized. (Source : Otoritas Jasa Keuangan)

B. Condition of Observed Variables

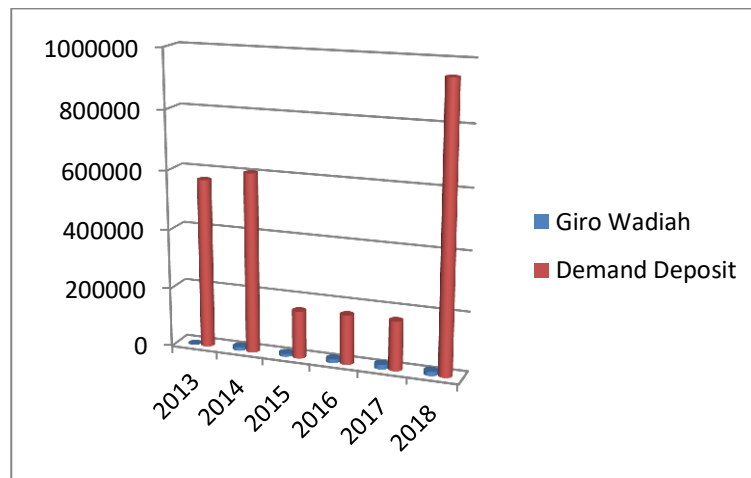


Source : Central Bureau of Statistics (BPS)

Figure 4.1

Statistics of Currency in Indonesia in Billion Rupiah (2013-2018)

The currency in question is to fulfill the variable of M1, where the currency experiences an increase every year except in 2018. According to sources found by the Central Bureau of Statistics or BPS, in 2018 in February the money supply in the current category was 531209.28, while in 2013 as many as 399606.17, in 2014 as many as 419261.84, in 2015 as many as 586762.55, in 2016 as many as 612544.71, and last year which was in 2017 the highest number reached 694,830 (in billion rupiah).



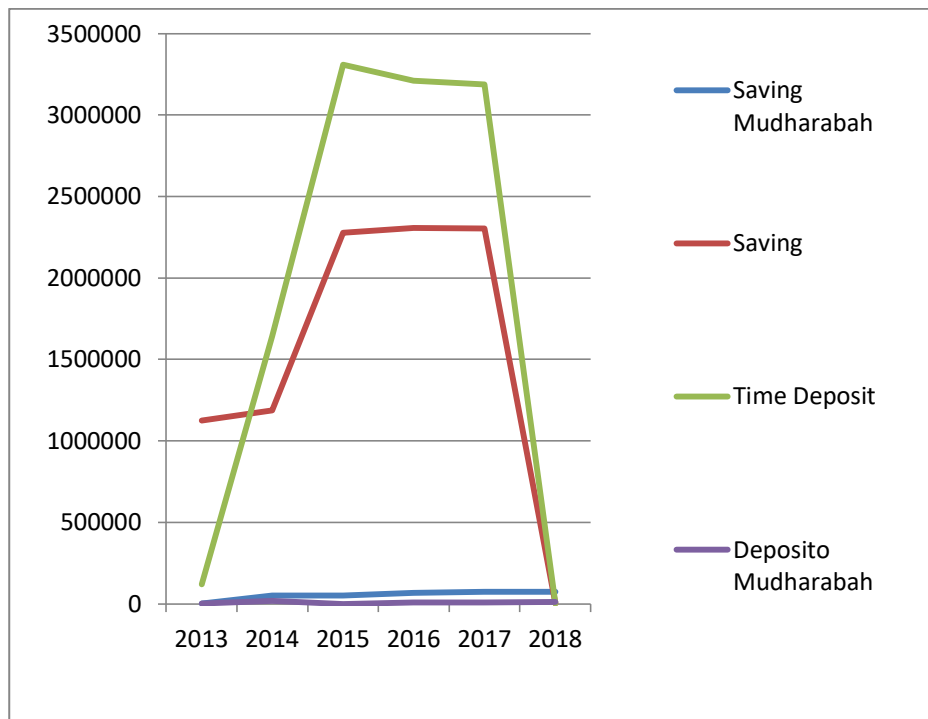
Source : Journal of Bank Indonesia

Figure 4.2
Amount of Money in Demand Deposit and Giro Wadiah in Billion Rupiah
(2013-2014)

The next component used to fulfill the variables M1 on conventional banks and M1ISL on Sharia Bank are Demand Deposit and Giro Wadiah components. The demand Deposit component is to fulfill M1 variable, while Giro Wadiah account to fulfill M1ISL varied. The table shows that more dominating the two components found in Indonesian banks from 2013 to 2018 are components owned by conventional banks, namely the Demand Deposit, which peaked in 2018. At the end of 2013 the amount of money in the demand deposit was as much as 569,927, then in 2014 as many as 605,276, in 2015 it decreased compared to previous years with only 161,030, in 2016 as many as 167,053, in 2017 as many as 166,957 was quite stable when viewed from 2015 to 2017 but then increased in the year 2018 which is to be as much as 949,960 (in billion rupiah).

In M1ISL variables other than currency, there is another component, namely Giro Wadiah account, which is implemented by Islamic banks. Although

the amount is not as much as the Demand Deposit component that is owned by conventional banks, there is an increase in the amount of money contained in the Giro Wadiah account. In 2013 there were 668.25, then in 2014 as many as 12,561, in 2015 as many as 10,195, in 2016 as many as 12,638, in 2017 as many as 15,777 and in 2018 decreased from the previous year with a slight difference of 14,549 (in billion rupiah).

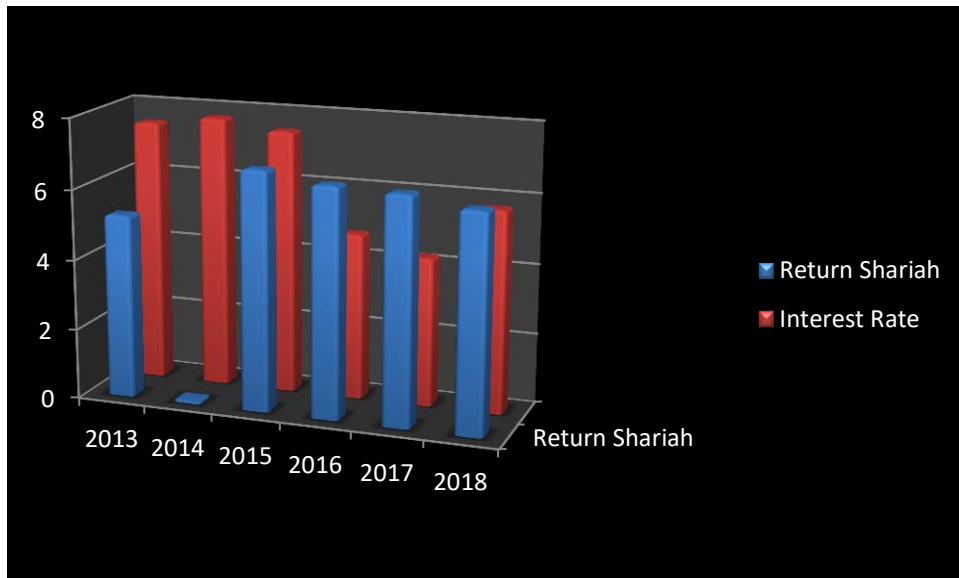


Source : Journal of Otoritas Jasa Keuangan

Figure 4.3
Amount of Money in Time Deposit, Saving, Saving (Mudharabah), Deposito (Mudharabah) in Billion Rupiah.

To complete the M2 and M2ISL variables, there is a need for components from Savings and Time Deposits in conventional banks. Whereas in Sharia banks using components from Saving Mudharabah and Mudharbah Deposits. As found in the table, it is clear that the components found in conventional banks still

dominate. But when viewed from the improvement and stability of the Shariah bank far more shows that there is a progressive increase not as volatile as conventional banks.



Source : Bank Indonesia

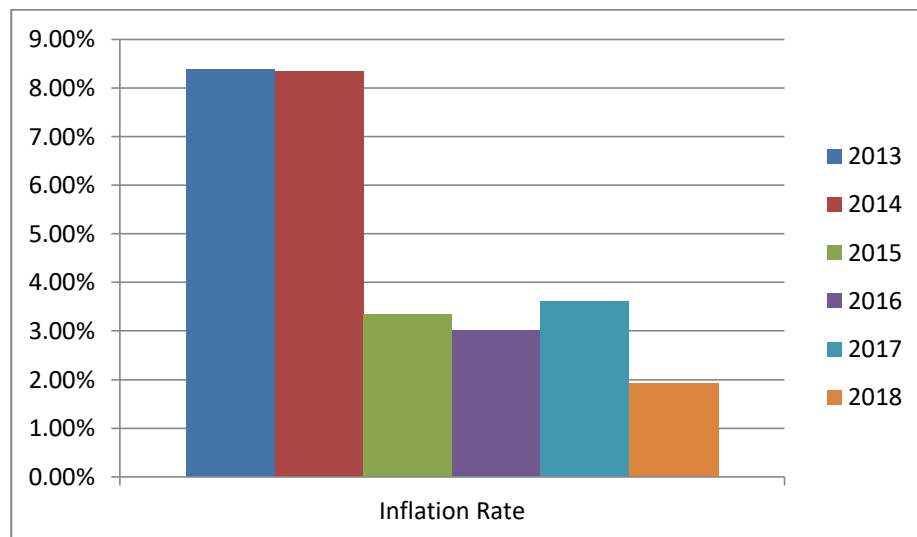
Figure 4.4
Statistics of Return Syariah and Interest Rate

The most distinguishing thing between institutions that implement conventional systems and institutions that implement Shariah systems is in interest rates. Islam has very clearly prohibited usury in transacting so that sharia institutions have a Shariah return.

The table in this table is the Interest Rate set from 2013 to 2018 by conventional banks as well as the Shariah Return determined by sharia banks from 2013 to 2018. In conventional banks the interest rates are quite high at 7.5% in 2013, at in 2014 amounted to 7.75%, in 2015 amounted to 7.5%, in 2016 amounted to 4.75, in 2017 amounted to 4.25%, and in 2018 amounted to 5.77%. In contrast to the conditions found in sharia banks that implement a sharia return

system not based on economic conditions that can change at any time so that changes received by customers often make conventional customers more difficult.

In a sharia bank, the Shariah return rate is determined by the bank and the customer on the agreement at the beginning, so that the customer does not need to worry if there is a turmoil that arises in the economy and difficulty in raising an increasingly high or unstable interest rate. The Shariah return set in 2013 was 5.25%, in 2014 7.34%, in 2015 6.82%, in 2016 6.54%, in 2017 6.46%, and in 2018 amounted to 6.20%.



Source : Central Bureau of Statistics (BPS)

Figure 4.5
Inflation Rate (2013-2018)

The inflation rate is the monetary condition of a country and can trigger the stability of the country's economy. There are times when Indonesia is truly in an alarming position due to the turbulence caused by inflation. Source from Bank Indonesia, In 1960, economic policies that prioritized political interests almost

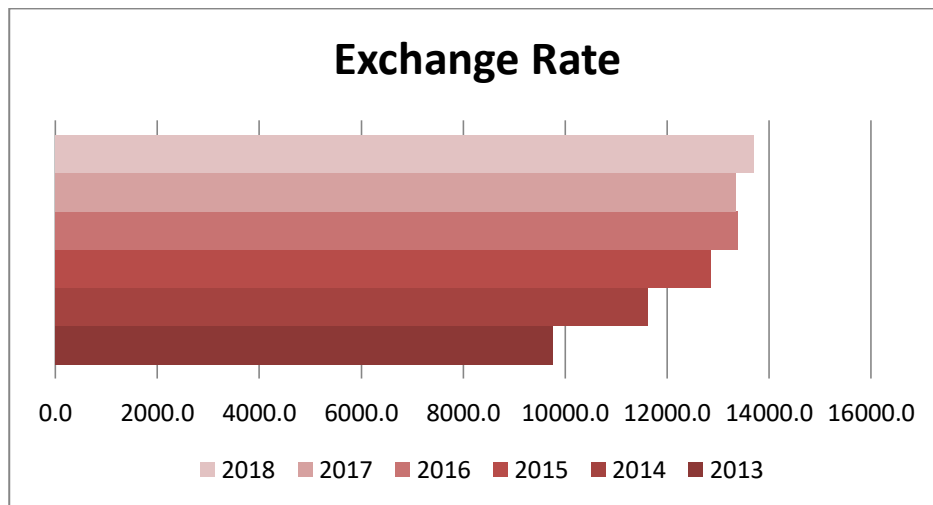
consumed all of Indonesia's potential. Therefore, this factor affects Indonesia's GDP growth, which is very low so that the impact on the inflation rate reaches 635% in 1966. With the high inflation rate, the government issued monetary tightening policies. Not even there, even in 1997 there was also a return to the monetary crisis which caused inflation in Indonesia to reach 77.63% up to 1998.

The factors that cause inflation are triggered by 3 things as follows:

Demand Pull Inflation. Demand Pull Inflation occurs because of an increase in the number of requests that arise in the community, both in demand for goods and services. Then the increase in demand for these types of goods or services occurs on aggregate demand triggered by an increase in government spending, increasing demand for goods for exports, and increasing demand for goods for the private sector.

Cost Pull Inflation. What triggers the occurrence of Cost Pull Inflation is the increase in production costs because the prices of raw materials have increased. As fuel prices rise and also the cost of labor costs rises.

Money Supply. If the amount of money circulating in the community is more, it will trigger inflation because the amount of money circulating in the community triggers more consumption as well. If in a situation like this, then the government implements a deficit budget where the budget shortfall is overcome by printing new money, which will cause an increasing amount of money in circulation, then there is no denying the occurrence of hyperinflation.



Source : Bank Indonesia

Figure 4.6
Exchange Rate in thousand rupiah (January 2013-February 2018)

Exchange rates can be interpreted as a comparison between one country's currency and another country's currency. Exchange rates are also referred to as these rates are interpreted as the price of a currency when exchanged for another country's currency. Conditions that affect the exchange rate can be caused by the amount of money in the country. The amount of money in circulation also affects the price of goods and services. Then the state of demand and supply of domestic currency against foreign currencies and the exchange rate system applied by the country will also affect the exchange rate of a country.

As is the case in Indonesia, which every year experiences an increase in exchange rates from year to year since 2013 until 2018. From the data obtained there are as large as Rp 9,760.00, then in 2014 amounted to Rp 11,634.00, in 2015 amounting to Rp 12,863.00, in 2016 amounting to Rp 13,395.00, in 2017 amounting to Rp 13,347.00, in 2018 last February it was still around Rp 13,707.00

and continued to increase until the beginning of November reaching Rp 15,000.00.