Correspondence

Revenue structure and risk of regional development banks in Indonesia during the COVID-19 pandemic

Dear Editor,

Based on the socio-economic effects that occurred in the research conducted by Akhter et al., this also happened in Indonesia. We will review it as follows. Many experts have done research on the structure of bank income. Lepetit et al. examines the relationship between the structure of bank income and risk on banks in Europe and concludes that in small-scale banks, income which is more dominantly obtained from non-operating income does not have a significant relationship to risk. On the other hand, in large-scale banks, the relationship between income structure and risk becomes significant. Busch and Kick examine the determinants of income activity in commercial banks in Germany. The results of his study concluded that the bank’s expansion into fee-based services affected its interest margin. Banks that are more focused on business costs charge lower interest margins.

Research conducted by Maudos found that an increase in the share of non-interest income has a negative impact on profitability, although the effect is only significant during the crisis. This study observes the income structure and risk of Regional Development Banks in Indonesia during the COVID-19 period to find out the extent of the implications of the pandemic on the two observed variables. Using secondary data published by the Financial Services Authority of the Republic of Indonesia, it was found that the portion of regional development bank income sourced from interest income increased during the COVID-19 pandemic. At the beginning of the pandemic, the proportion only reached 74.57%. Meanwhile, when the pandemic began to end, the proportion increased to 84.77%. During the pandemic, the average proportion of income originating from interest was 78.11%. This fact shows that the proportion of interest income is still dominant in the income structure of Local Development Banks in Indonesia. As a result, the risk of default from borrowers will greatly affect the bank’s income level and its resilience to face external shocks.

Analyzed by using the standard deviation of income, it was found that income derived from interest has a higher risk value. It can be concluded that the business risks of Regional Development Banks in Indonesia during the COVID-19 pandemic have increased and are structural in nature. The greater the proportion of income derived from interest on loans and with a high standard deviation, the higher the risk faced.

To recover and increase business resilience that can reduce the risk of financial distress, it is necessary to improve the income structure with a more balanced proportion of income from interest and income from other businesses outside of credit. Uppal found that fee-based income is very important in strengthening the stability of bank income because income derived from interest is very sensitive to banking competition.

Although the results of research by literature state that diversification income represented by the ratio of non-interest income can increase bank profits. Research by Busch and Kick found that growth in non-interest income had a positive impact on the financial performance and risk profile of German banks between 1995 and 2005. Trivedi research in India found that innovation adoption which leads to income diversification in a bank has a positive impact on profitability and strengthens income stability. Referring to the various research results, the findings of this study strengthen the evidence that diversification of bank income that can reduce dependence on interest income through product development, technological innovation and service improvement will increase profits and maintain income stability and mitigate business risks.

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Edyanus Herman Halim¹, Ledya Oktavia Liza², and Dominikus David Biondi Situmorang³

¹Department of Management, Riau University, Kota Pekanbaru, Riau 28293

²Department of Special Education, Lancang Kuning University, Kota Pekanbaru, Riau 28266

³Department of Guidance and Counseling, Faculty of Education and Language, Atma Jaya Catholic University of Indonesia, DKI Jakarta 12930

Address correspondence to Dominikus David Biondi Situmorang, E-mail: david.biondi@atmajaya.ac.id

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