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THE FEASIBILITY OF FINANCING INDONESIAN MIGRANT WORKERS BY ISLAMIC BANKS

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Abstract

This paper identifies the profile of migrant workers located in Banyumas regency, assesses the financial feasibility of the scheme, and gauges the viability of the migrant workers financing from conventional and Islamic banks' perspectives. The samples comprises potential migrant workers, ex-migrant workers and their relatives. The nature of the study is descriptive qualitative where both primary and secondary data were analysed during the study. The result of the study indicates that financing migrant workers to work abroad is economically desirable for both conventional and Islamic banks. Either mode of financing, Islamic and conventional, are advantageous to the Indonesian workers who want to work abroad.

Keywords: Feasibility study, financing, migrant workers, Islamic banks
JEL classification numbers: G21, G29

Abstrak

Makalah ini mengidentifikasi profil pekerja migran di kabupaten Banyumas, menaksir kelayakan keuangan dari skema tersebut, dan memperkirakan kelayakan pembiyaan para pekerja migran dari perspektif bank islam dan bank konvensional. Sampel yang digunakan terdiri dari para pekerja migran potensial, bekas pekerja migran, serta keluarga mereka. Penelitian ini bersifat deskriptif kualitatif menggunakan baik data primer dan data sekunder. Hasil analisis menunjukkan bahwa pembiayaan terhadap para pekerja migran untuk bekerja di luar negeri secara ekonomis adalah layak baik dari pserspektif bank islam maupun bank konvensional. Baik mode pembiayaan islam maupun konvensional memberikan keuntungan bagi para pekerja Indonesia yang bekerja di luar negeri.

Kata kunci: Studi kelayakan, pembiayaan, pekerja migran, bank islam
JEL classification numbers: G21, G29

INTRODUCTION

The migrant workers play a significant role in stimulating economic growth in Indonesia. They are in fact heroes which safe this country from recession through foreign currency inflow. Nonetheless, little attention has been given by the government to support them. Their contributions are almost forgotten by most people of this country. This paper provides an illustration about the feasibility of financing Indonesian manpower to work overseas. A comparison will be made between conventional and Islamic lending model.

Sending Indonesian manpower to work abroad has occurred since the Dutch colonization in 1887. The workers were sent to Suriname, New Calidonia, Thailand, and Malaysia. The Indonesian government policy to send workers abroad started in 1969, which was later supported by government regulation no. 4 1970. Among reasons for workers migration abroad are attributed to external factors such as higher salary as compared to domestic wages rate and internal factors such as limited number of jobs available as compared to the population size in Indonesia (Suparno, 2008).

The most crucial problem faced by the Indonesian labour market is the high unemployment. The Indonesian economy grows at lower speed which gives rise to inability to create jobs proportional to the population's growth. High level of unemployment leads to poverty. People would find any kind of jobs to survive even with low compensation. As a result, people shall start looking for better compensation even if they have to leave their home town or country.

Besides reducing unemployment rate and its dominant effect domestically, sending workers abroad will provide financial flow to the country in the form of remittance. The amount of remittance is continuously increasing every year. In 2004 the amount of remittance has reached up to US$1,9 billion and by the year 2007 the amount has increased significantly to US$5,84 billion. For Central Java the figure has reached up to 118 billion rupiah between January-April 2007. World Banks predicted that the amount of remittance contributed by the migrant workers in 2010 would reach a figure of 7.1 billion U.S. dollars which is almost 1 billion dollars increase since 2009, which was only 6.6 billion dollars (Poyuono, 2010).

One problem faced by Indonesian workers to go overseas is the lack of fund. The cost incurred to work abroad is fairly high for average Indonesian people. As a result, many workers are unable to work abroad due to financial problem.

Islamic lending model has unique characteristics as compared to the conventional mode of financing. Islamic financial institution includes Islamic rules (shariah) as part of the assessment criteria. Shariah finance operates on the principle of return goes along with risk, which critizes the conventional lending model. In other words, money must not generate money, instead, it must be invested in tangible economic activities or real sectors (for discussion on Islamic economics, see Haneef and Furqani, 2011; Zarqa, 2003; and Al-Attas, 2005, among others).

Previous research identifies several forms of financing for migrant workers in Indonesia (Bank Indonesia, 2007): (1) personal source of finance, (2) Agency source of finance (3) financial institutions source of finance. There are two forms of distribution used by the financial institutions: (a) individual level, the candidate can apply for loan directly to a bank (b) agency act as loan guarantor (avalist).

Financing Indonesian migrant workers has multiple advantages: (1) financial institutions will received fees in the form of international remittance from international transactions and receive profit sharing from the agency; (b) the multiplier effect to the local economy as a result of cash inflow to workers' area of origin can reduce poverty in the area.

The objectives of the study are three folds: first, to identify the profile of migrant workers located in Banyumas regency; second to assess the financial feasibility of the scheme; and finally to gauge the viability of the migrant workers financing from conventional and Islamic banks' perspectives.

Islamic banking and finance burgeoning popularity can be linked to religious fervour and people's trust on system of Islamic economy. Islamic banks function are similar to conventional banks, acting as an intermediary and trustee of other people's money, with the difference that it shares profit and loss with its depositors (Dar and Presely, 2001). In addition, based on their operational philosophy, banks are classified as Islamic banks, denotes a banking system that is coherent with Islamic law and guided by Islamic economics, and conventional banks, do not work on Islamic principles. In particular, Islamic law forbids usury, the collection and payment of interest, also known as *riba* in Islamic discourse (El-Qorchi, 2005; Lewis and Algaoud, 2007; Rice and Mahmoud, 2001). Moreover, Islamic law disallows ownership in unlawful business, such as trading alcohol or ham, or media businesses which against Islamic law or virtues.

The establishment of Islamic banks in Indonesia takes place because of strong public demands on the existence of alternative banking system. Islamic banks are expected to deliver sound financial services in accordance with Islamic (*Shariah*) rules. Actually, Islamic banks have been in operation long before IB formal legal declaration in 1992, where some non-bank financial institutions with share base contract existed.

As a respond to public demands, the government has implicitly allowed the *Shariah* banking operations based on: Act No. 7 of 1992, concerning banking, and Government Decree No. 72 of 1992, concerning Share Base Principles. The set of regulations followed by the Central Bank regulation No. 8/3/PBI/2006, introduce in March 2006 about *Office Channelling* Islamic Banks in Indonesia, served as legal basis for IBs operations in Indonesia. *Office Channelling* denotes a utilization of commercial bank branches to serve *Shariah* transactions provided the banks have Islamic Business Unit (IBU). In later years, IBs banking have grown rapidly with an average assets' growth of 74 percent per annum.

Forms of Islamic Finance

It is well discussed in Islamic economic literature that fund raising and mobilization must be based on interest-free instruments (Ahmed, 2008. See also Bidabad et al., 2011; Sole, 2007; and Wilson, 2008).

This practice has been adhered to by Islamic banks' worldwide and continuously refined and modified to meet the evolving needs of individual or even more sophisticated business practises. Islamic mode of financing lies on profit and loss (PLS) contracts, namely *mudharabah* and *musyarakah*.

These modes of financing allow not only profit sharing but also risk sharing to both supplier of the capital and the entrepreneurs. In this case all parties involved in the financing activities face equal benefits and consequences. Other of non-PLS contracts are *salaam* and *murabahah*. Certainly the aforementioned contracts are generally accepted amongst most Islamic scholars as long as both parties adhere to the condition of each contract (Ahmad, 2008). Thus, it can be concluded that the range of contracts offered by Islamic banks are varies according to customers' needs which is example of the efficiency-enhancing characteristics of spectrum filling (Iqbal and Llewellyn, 2000).

The need for Islamic Financing

The number of migrant workers is continuously increasing every year. Unfortunately, devaluation of Indonesian Rupiah against US$, makes it more difficult for prospective migrant workers to find source of financing. Conventional banks tend to offer high cost financing scheme. On the other hand Islamic finance based on PLS and non-PLS models provide win-win solution to both suppliers and entrepreneurs. Moreover, banks are reluctant to finance migrant workers due to high uncertainty in credit terms, periods and the amount of instalment to be paid periodically.

Study by Adawiyah et al. (2008) concluded that lack of interest among banks to finance migrant workers should be taken as opportunity by Islamic banks due to the desirable returns in the financing scheme. Nonetheless, Islamic banks still consider that migrant workers have high risks provided it is financing using PLS scheme. Moreover, insufficient collateral to support the scheme has even discouraged Islamic banks from offering the scheme. Therefore, there is a need to assess the feasibility of financing migrant workers in order to provide guideline for banks regarding the prospect of it.

METHODS

The study was carried out in Banyumas Regency Central Java. The respondents were Indonesian migrant labors, migrant labor agency and financial institution. The study was conducted in 2010. Several methods were used to assed the feasibility of the financing scheme such as payback period, internal rate of return, net present value, and profitability index. The outcome of the analysis will determine whether the financing scheme is feasible or not.

RESULTS AND DISCUSSION

The Profile of Migrant Workers

It is indicated in table 1 that by December 2009, the number of migrant workers from Banyumas regency working abroad has reached 2,276 with variety of destination such as Saudi Arabia, Malaysia, Singapore, Hongkong and Taiwan. Malaysia is the most preferred destination by the workers because they perceive Malaysia share similar cultures with Indonesia, thus migrant workers do not have to work hard during pre-departure training provide they choose to work in Malaysia.

The main workers' motivations to work abroad is economic factor, desire to earn higher income. Before deciding to work abroad, most workers work in informal sector or just a housewife. Upon their return, migrant workers are expected to have better living standard, and have sufficient capital to create new venture in their home town. Majority of the migrant workers are secondary school graduates. With such qualification they are not able to earn high revenue domestically therefore they choose to work abroad.

Migrant Workers based on Gender

Out of 2.276 migrant workers from Banyumas, 91.91 percent or around 2,092 are female while the remaining number 184 or equivalent to 8.09 percent are male. Table 2 below present the number of migrant workers from Banyumas Regency working abroad in 2009 based on gender. In addition 2.113 workers are placed in informal sector while the rest, 163 workers, work in formal sector.

Table 1: The Number of Migrant Workers Abroad During 2007-2009

No.	Destination	sex	Year 2007	2008	2009	Total
1	Saudi A	M	14	6	6	26
		F	850	597	452	1899
2	Singapura	M	-	-	-	-
		F	425	363	574	1362
3	Malaysia	M	51	170	152	373
		F	464	688	241	1393
4	Hongkong	M	-	-	-	-
		F	214	255	270	739
5	Taiwan	M	1	-	4	5
		F	412	399	507	1318
6	Korea	M	-	165	-	165
		F	-	5	-	5
	Total		2431	2648	2206	7.285

Source: Disnakertrans Kabupaten Banyumas

Table 2: Migrant Workers based on Gender in 2009

Gender	Total	Percentage (%)
• Male	184	8,09
• Female	2.092	91,91
Total	2.276	100,00

Source: primary data

Table 3: Migrant Workers based on Job Field

Field of work	number	Percentage (%)
• Formal	163	7,17
• Informal	2.113	92,83
Total	2.276	100,00

Migrant Workers Agency

By the year 2008 the number of agencies operating in Banyumas was 35 companies. It is indicated in the study that the number has decreased significantly to 60 percent due to limited access to fund, complicated procedures, and the existence of 'satanic circle' which has boost up the operational costs. The amount of hidden costs has driven down many agencies from their business.

Table 4: Number of Migrant Workers Agency in Banyumas

Year	No of agency	Status
2008	35	All active
2009	27	Only 60% active

Source: Disnakertrans Kab. Banyumas

Cost of Sending Workers Abroad

The amount of expenditures required depends on the destination as follows: (i) Malaysia, cost around Rp 6.750.000 per head (informal sector). (ii) Taiwan, cost around Rp 20.000.000/head (Formal sector). (iii) Hongkong, cost around Rp 24.000.000/head. (iv) Singapore cost around Rp 2.500.000 up to Rp 3.000.000/head, (v) For Saudi Arabia worker do not have to pay for the cost of departure instead payment will be directly taken from workers salary. Prior to departure all cost are incurred by the agency.

Meanwhile, the amount of salary earned varies according to each country is as follows: (i) Malaysia, around RM880 /month. (ii) Singapore around $ 350 up to $ 400/month. (iii), (iv) Hongkong $HK 3.580, and (v) Taiwan $NT 16.216 per month.

Financing Financial Forecast

The tool of analysis used in this paper to assess the financial consequence consists of payback period, internal rate of return, net present value, and profitability index.

***Payback Period* (PP)**

PP is employed to assess the period of time needed to get the initial investment back through cas inflow. Thus PP is athe ration of cash investment with cash inflow.

$$PP = \frac{\text{Initial investment}}{\text{Cash inflow}} \times 1 \text{ year}$$

$$PP = \frac{6.750.000}{16.200.000} \times 1 \text{ year}$$

$$PP = 5 \text{ months}$$

Payback period from financing migrant workers to work in Malaysia is less then 12 months thus this scheme is feasible.

***Internal Rate of Return* (IRR)**

IRR is used to determine the level of interest rate that equate the amount of present value of future cash inflow, or cash receive with initial investments (Umar, 2005).

$$I_o = \sum_{t=1}^{n} \frac{CF_t}{(1+IRR)^t}$$

where :

t is time

n is numbe of years

I_0 is initial investment at time zeor

CF is net cash inflow

IRR is level of interest rate required

The level of interest is calcuated based on trial and error. The attempt has to be continuously performed until the desired level of interest rate are resumed. The following formula is used to calculate the internal rate of return.

$$IRR = P_1 - C_1 \frac{P_2 - P_1}{C_2 - C_1}$$

where:

P_1 is interest rate at point 1

P_2 is interest rate at point 2

C_1 is NPV at point 1

C_2 is NPV at point 2

It is appeared during the survey that the amount of departure cost required by migrant workers to work in Malaysia is around Rp 6.750.000 per worker with the estimate monthly average earning is Rp 1.350.000 or Rp 16.200.000 per year. The average level of interest impose on lending hitherto is around 28% per annum (Adawiyah et al., 2009), If it assumed that the level of lending rate currently offered range from 28% dan 32%, the IRR can be estimated as follows:

$$IRR = 28 - 5.907.060 \frac{32-28}{5.523.120-5.907.060}$$

$$IRR = 28 - \frac{23.628.240}{-383.940}$$

$$IRR = 89,5\%$$

From the calculation the IRR to fiance migrant workers is higher than the level of interest currently offered by bank for lending, 89.5% > 28%, thus the scheme is feasible.

***Net Present Value* (NPV)**

NPV is the difference between initial investment at time zero with the present value of future cash inflow (Fred, 1995)

$$NPV = \sum_{t=1}^{n} \frac{CF_t}{(I_0 + K)^t}$$

where:

CFt is yearly cash inflow at time t

Io is Initial investment at time 0

K is discount rate

It is depicted in table 5 that NPV for financing migrant workers departure to Malaysia is positive thus the scheme is feasible to be financed.

Profitability Index (PI)

Profitability Index (PI) is another approach used to analyze investment. It is used to determine whether an investment is feasible or not. Provide the score of PI is greater than 1 the investment is feasible. The estimation is made by comparing the present value of net future cash inflow with the present value of ongoing investment. Estimation can also be made based on comparison between present value of cash inflow and present value of cash outflow.

PI = PV cash inflow/PV cash outflow

PI = Rp 16.200.000/Rp 6.750.000

PI = 2,4

Table 5: NPV Calculation

Month	Revenue	df 28%	Present value
1	Rp 1.350.000	0,7813	Rp 1.054.755
2	Rp 2.700.000	0,6104	Rp 1.648.080
3	Rp 4.050.000	0,4768	Rp 1.931.040
4	Rp 5.400.000	0,3725	Rp 2.011.500
5	Rp 6.750.000	0,291	Rp 1.964.250
6	Rp 8.100.000	0,2274	Rp 1.841.940
7	Rp 9.450.000	0,1776	Rp 1.678.320
8	Rp 10.800.000	0,1388	Rp 1.499.040
9	Rp 12.150.000	0,1084	Rp 1.317.060
10	Rp 13.500.000	0,0847	Rp 1.143.450
11	Rp 14.850.000	0,0662	Rp 983.070
12	Rp 16.200.000	0,0517	Rp 837.540
Total PV from procceds			Rp 17.910.045
PV *Outlays*			Rp 6.750.000
Nett Present Value (NPV)			Rp 11.160.045

Based on the above calculation the PI is positive indicating the financing migrant workers departure to work abroad is profitable for banks.

Table 6: Summary of Financial Analysis

No	Analysis	Result	Description
1	*Payback Period*	5 months	< 12 months
2	IRR	89.5%	> ROR 28%
3	NPV	Rp 11.160.045	Positive
4	Profitability Index (PI)	2.4	Positive

Comparing Islamic Banks and Conventional Banks

The economic and monetary turmoil happening during the period 1997 to 1998 resulted in tremendous impact to the Indonesian economy. During the period of crisis, many financial institutions, including banking institutions, experienced financial hardship. High interest rate has resulted in a high cost of capital to the entrepreneurs i.e. the real sector and finally caused low productivity. The quality of bank assets has deteriorated significantly while the banking system was burdened by a high cost of funds caused by high market interest rates. Furthermore, low productivity and high risk investments have prevented the banks from investing their funds in the real sector. As the consequence, the banking system started to loss its intermediary function as indicated by a low Loan to Deposit Ratio (LDR).

Contrariwise, during the economic crisis, *sharia* banking could still perform better than the conventional banking as indicated by a relatively low level of non-performing loans and the absence of negative spread in the operational activities. This could be understood since the rates of returns paid to the depositors are not determined by market interest rates. Therefore, *sharia* banks are able to channel a relatively lower cost of funds to the entrepreneurs. The evident shows that *sharia* banks are relatively more able to conduct lending as indicated by a relatively high LDR ratio i.e. between 99.75 – 112.37 percent between 2002 and 2007 (Bank Indonesia, 2007). This experience has brought a hope to the public for the presence of *sharia* banking as an alternative banking system that is capable of both delivering economic benefits and ensuring compliance with *sharia* principles.

Conventional banks operate on the basis of interest rates while Islamic banks operate on the basis of profit sharing. The amount of interest rates imposed by conventional bank affect the amount of installment paid by debtors.

Based on a survey, it is found that the average amount of spending made by Manpower Supplier (PJTKI) to send migrant workers abroad is around 200 million rupiah per month. Out of those spending, the agency will earn profit around 5 million rupiah per month. The amount of spending is determined by the level of demand on manpower supply every month.

Table 7: Profit Calculation based on Shariah/Islamic principles (in Million rupiah)

Condition	Cost million	Margin (20 %)	Fixed Cost	Variable Cost	Net profit	Bank (40%)	PJTKI (60%)
pesimist	200	40	5	30	5	2	3
moderate	400	80	5	60	15	6	9
optimist	600	120	5	90	25	10	15

Table 8: Profit Calculation in Conventional method (in Million rupiah)

Condition	Cost million	Interest (24 %)	Fixed Cost	Variable Cost	Net profit	Bank (40%)	PJTKI (60%)
pesimist	200	48	5	30	10	4	6
moderate	400	96	5	60	31	12.4	18.6
optimist	600	144	5	90	49	19.6	29.4

In any condition the manpower supplier (agency) will always earn profit. However in Optimistic condition the amount of profit earned using the conventional method of financing is higher than Shariah method.

CONCLUSION

Banyumas regencies which consist of 27 districts possess quite significant number of migrant workers abroad, most of them are female. The cost of sending Indonesian workers abroad is potential to be financed with Shariah Financing System as well as conventional methods. Both source of financing, shariah and conventional, are advantageous to Indonesian workers who want to work in Japan.

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