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Brief Contents

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This study is aimed at fill in the literature gap. To be more particular, this study aims to empirically investigating the contribution of liquidity, capital, cost efficiency, revenue diversification, asset quality, and market concentration to Islamic bank's profitability and growth, as well as to assess whether profitability leads to Islamic bank's growth. We observed all Islamic banks operating in Indonesia using monthly data from January 2011 to December 2013. Since the three models developed in the study show correlation among responding variables, we follow Seemingly Unrelated Regression (SUR) procedures.

The results indicate that management oshould carefully handle quality of their assets since it significantly determines Islamic banks' profitability. Moreover, the management may accelerate growth of Islamic banks if they could sufficiently manage revenue diversification, capital adequacy and asset quality. We also prove that when Islamic banks sustain their profitability level, they can achieve the desired growth.

Keywords : Bank characteristics, Asset growth, Profitability, Islamic Bank

Forecasting World Oil Price and its Volatility

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Fossil fuel like oil is one major commodity that can affect many aspects of economic activities. Forecasting world oil price can be useful in making prediction of its movement in the future. On the other hand, forecasting world oil price volatility plays a fundamental role in terms of oil risk management.

There are many techniques that can be utilized in forecasting oil price and its volatility. Volatility models, such as Autoregressive Conditional Heteroscedasticity (ARCH) and Generalized Autoregressive Conditional Heteroscedasticity (GARCH) become two popular methods in analysing the historical behavior of a series. ARCH and GARCH class models can capture the characteristic of a series, like fat tail and leptokurtic, as the existence of volatility clustering.

Forecasting world oil price and its volatility can benefit governments and fuel companies. Efficiency in making prediction of oil price and its volatility can be utilized as hedging strategy in terms of oil investment.

This research found that technical analysis can be useful in forecasting Brent and West Texas Intermediate (WTI) oil price. We found that Holt-Winters exponential smoothing is better than ARIMA technique in forecasting Brent and WTI oil price.

On the other hand, by employing Threshold GARCH, we found that volatility of Brent and WTI oil price are significantly sensitive to bad news in global economy. The presence of unanticipated bad event in previous month produce higher volatility in the next month.

Furthermore, by employing Vector Auto Regression technique, specifically from the information of variance decomposition, Brent oil price, on 10 months average, contributes for about 89.9% to WTI oil price movement, while US\$/EUR exchange rate contributes 1.36%. WTI oil price itself contributes only 2.94% to Brent oil price movement, while US\$/EUR contributes smaller than WTI oil price, that is 0.83% to Brent oil price movement.

Keywords : Forecasting, Oil Price, Threshold GARCH, VAR, Volatility

Constructing Indonesia Financial Stability Index

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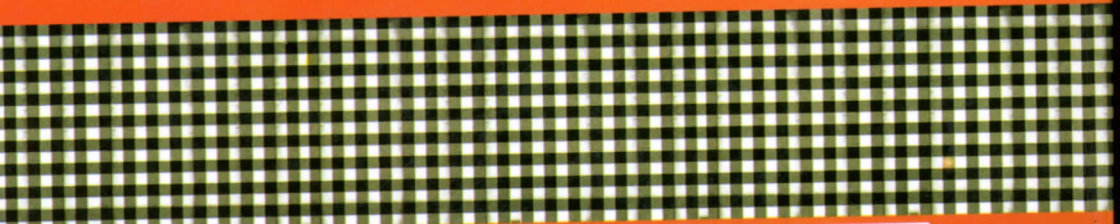
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Financial system stability is required to ensure a sustainable economic development. Indonesia's financial system has experienced some major shocks in its history (e.g., panics in banking sector in 1992, Asian Financial Crisis in 1997, and most recently 2008 sub-prime mortgage crisis). These financial shocks to certain extent affect the stability of Indonesia financial system, then, transmitted to contraction of Indonesia's economic growth. By this point, one might consider that financial stability and economic performance are highly correlated.

Given the correlation between financial stability and economic performance, this paper has two objectives: (a) constructing Indonesia Financial Stability Index (IFSI); and (b) forecasting Indonesia financial stability index. We offer two methods to construct Indonesia financial stability index namely Aggregation with Variance Equal Weight, and Principal Component Analysis (PCA) in monthly basis. Construction of financial stability index can benefit both government and financial institution as a tool in monitoring historical stability of financial system. On the other hand, forecasting financial stability index can be utilized as an early warning system.

We found that Indonesia financial stability index constructed by the two approaches have the same trend pattern. By reducing dimension of variables in PCA technique without having to lose the information on the movement of the Indonesia financial stability index variation, we found that banking performance and interest rate are variables contribute Indonesia financial stability the most. More over, in context of forecasting the Indonesia financial stability index, we found that Adaptive Holt Winters Exponential Smoothing is superior to Autoregressive Moving Average (ARMA) technique, in terms of forecast performance.

Keywords : Adaptive HW Exponential Smoothing, Aggregation with Variance Equal Weight, ARMA, Indonesia Financial Stability Index, Principal Component Analysis.



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