

ISLAMIC BANK FINANCIAL PERFORMANCE ANALYSIS: INFLUENCE AND CAUSES

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ABSTRACT

Analysis of the financial performance of Islamic banks is mostly done by experts. This analysis uses many models, such as liquidity. In addition to assessing the financial performance of the Islamic bank itself, this financial performance analysis also refers to its influence on other factors such as economic growth. By using a literature study, this article analysis what influences and is influenced by the financial performance of Islamic banks. This article finds that the financial performance of Islamic banks influences external factors such as economic growth and internal factors such as credit risk. This financial performance is also influenced by external factors, such as economic growth, and internal ones, such as CSR disclosure. The financial performance of Islamic banks is also used to compare it with the performance of conventional banks and fellow Islamic banks in different countries. Each researcher in the sampled article uses a different analytical method according to his research objectives. Islamic banks have a unique performance analysis method that does not exist in conventional banks, namely financing measurement using non-profit loss-sharing and profit loss-sharing schemes

Keywords: *Performance; finance; Islamic bank; economic*

INTRODUCTION

To understand a company's performance, measurement is carried out by analyzing its condition and financial position. However, the financial position of the company's performance can also be used to see other aspects, for example, the effect of ROA and liquidity on company value (Marsha & Murtaqi, 2017). For Islamic banks, a study of their financial performance can be used for other specific purposes, such as the role of Islamic banks in economic growth (Ledhem & Mekidiche, 2020).

Islamic banks have the role of receiving public funds and then channelling them back to the community to carry out real economic activities. Islamic banks are not allowed to channel their funds to business sectors that are prohibited by Islamic law. This condition is different from the principles that exist in conventional banks. Therefore, the influence of the financial performance of Islamic banks is an interesting study for experts to

examine. This paper analyzes articles that have been published by experts regarding the financial performance model of Islamic banks and their role and influence on other aspects.

This paper finds that there are articles that discuss the role of Islamic banks as measured by financial performance on external and internal of the Islamic banks. In addition, this financial performance is also influenced by external and internal factors of the Islamic banks. Currently, Islamic banks are still new when compared to conventional banks. The conditions for the development of Islamic banks in each country are also different. The previous article also analyzed how the financial performance is compared between the Islamic banks and the conventional banks, and among the Islamic banks in each country.

There are many ways to measure a company's financial performance. This

performance measurement is carried out by analyzing the financial statements prepared by the company. In general, financial performance analysis is divided into 2 ways, namely using the common size and financial ratios. Common size is the percentage version of financial statements. Financial ratios are generally used to measure liquidity, capital structure, efficiency in using assets, profitability, and market value.

In analyzing the financial performance of Islamic banks, financial ratio analysis can use several ratios at once. Ledhem & Mekidiche (2020) uses 6 parameters in conducting their analysis, namely capital adequacy (C), asset quality (A), management efficiency (M), earnings (E), liquidity (L), and sensitivity to market risk (S). These six parameters are abbreviated as CAMELS. This several parameters or ratios are using to see the financial performance of Islamic banks themselves and their influence on, for example, economic growth. From this financial performance analysis, it will be known which factors have the greatest influence and no significant influence on the internal and external of Islamic banks.

Meanwhile, Biduri et al. (2022) use CAR, ROA, FDR, and total asset turnover when comparing the financial performance of Islamic banks in Indonesia and Malaysia. By using several financial performance measurement ratios, it can be seen which financial performance is superior or not good among the banks being compared. By using a comparison of several financial ratios, it can also be seen what are the differences and similarities in the financial performance of several Islamic banks.

Islamic banking companies have a specific way of working that is different from conventional banks and other non-bank companies. Therefore, the researchers added an analysis of financial performance that does exist in Islamic banks and does not exist in conventional banks and in other industries, for example, the Financing to Deposit Ratio (FDR). Because Islamic banks do not allow transactions that contain elements of usury, the distribution of financing is carried out in collaboration with profit sharing and the form of asset

purchases (*murabahah*). Therefore, Islamic banks take into account financial performance in the form of Non-Profit Loss Sharing and Profit Loss Sharing (Saleem et al., 2021).

Particularly for bank business entities, there is risk measurement related to financial performance. To get high profits and growth, Islamic banks must be careful and pay attention to existing risks. It is necessary to relate risk ratios to financial performance. Abbas & Ali (2021) explain that increasing loans will increase credit risk. To decrease the risk, the bank should pay attention to its capital. What is meant by capital here is the ratio between equity and total assets. Some analysis of financial performance is needed to be able to understand and predict the condition of Islamic banks.

METHODOLOGY

This study uses a qualitative method with content analysis from articles obtained in the Scopus database with specific criteria. The content analysis aims to get an overview of what themes are discussed in the selected articles in the specified period. The analysis of selected articles is positioned within the interpretivist paradigm, which provides an understanding of social reality based on the interpretation of the researcher's subjectivity (Bornman & Ramutumbu, 2019). The author of this article subjectively analyzes the literature obtained with certain criteria to understand how the financial performances of Islamic banking influence and are influenced, both externally and internally. In addition, this analysis also looks at other uses of Islamic banking's financial performance. Islamic banking's financial performance is measured by financial ratios and other indicators.

This article analyzes 21 articles published from 2018 to September 30, 2022, at 04.05 pm GMT+7. Articles were obtained using the Publish or Perish (PoP) application from the Scopus database. The keywords used are "Islamic bank" OR "shariah bank" OR "financial performance" AND "economic". At the time of withdrawal of articles from the Scopus database, 58 articles were obtained. After reading and analyzing

the content of the articles, 21 articles were obtained that are relevant to the purpose of writing this article.

After conducting content analysis, the selected articles are used for further discussion. The selected articles are in Table 1.

DISCUSSION

Article Description

Table 1. Articles for Content Analysis

No	Author, Year, Journal	Title	Data
1	(Abbas & Ali, 2021) <i>Kybernetes</i>	Economics of loan growth, credit risk and bank capital in Islamic banks	Data from 38 countries from South Asia, MENA, South Africa, East Africa, and Central Asia regions. The year 2010 to 2019.
2	(K. K. Abdo, 2021) <i>Journal of Sustainable Finance and Investment</i>	The effect of external economic variables on the conventional banks and Islamic banks financial performance in Jordan: a comparative study	Data from Jordan. The year 2010 to 2019
3	(K. Abdo et al., 2021) <i>Academy of Strategic Management Journal</i>	Impact Of Economic and Financial Determinants Affecting the Profitability of Jordanian Islamic Banks (2012 -2019)	Data from Jordan. The year 2012 to 2019
4	(Agustina et al., 2022) <i>International Conference on Decision Aid Sciences and Applications</i>	Islamic Banking, Economic Growth, and Poverty Reduction in Indonesia	Data from Indonesia. The year 2010 to 2019
5	(Alrawahdeh & Zyadat, 2021) <i>WSEAS Transactions on Business and Economics</i>	The role of the Islamic banks in increasing domestic saving funding economic development in Jordan	Data from Jordan. The year 2010 to 2019
6	(Alshebel et al., 2019) <i>International Journal of Innovation, Creativity and Change</i>	The impact of Islamic banking credits on Saudi Arabia's economic growth	Data from Saudi Arabia. The year 1990 to 2015
7	(Azzam & Rettab, 2022) <i>Singapore Economic Review</i>	Comparative TFP growth between GCC conventional and Islamic banks before and after the 2008 financial crisis.	Data from GCC (Bahrain, Kuwait, Qatar, Saudi Arabia, UAE). The year 1998 to 2012
8	(Ben Bouheni et al., 2022) <i>Annals of Operations Research</i>	Nonperforming loan of European Islamic banks over the economic cycle.	Data from the United Kingdom and Turkey. The year 2010 to 2019
9	(Bilgin et al., 2021) <i>Journal of Financial Stability</i>	Economic uncertainty and bank stability: Conventional vs. Islamic banking	Data from 20 Countries The year 2009 to 2018
10	(Ellili & Nobanee, 2022) <i>Environment, Development and Sustainability</i>	Impact of economic, environmental, and corporate social responsibility reporting on financial performance of UAE banks	Data from UAE The year 2003 to 2013

No	Author, Year, Journal	Title	Data
11	(Eti et al., 2019) <i>Handbook of Research on Creating Sustainable Value in the Global Economy</i>	Predicting the role of Islamic banking on sustainable economic development: An analysis for Turkey with ARIMA Model	Data from Turkey The year 2010 to 2018
12	(Gulaliyev et al., 2021) <i>Comparative Economic Research</i>	The economic efficiency of traditional and Islamic banking (a comparative analysis of the Turkish, Azerbaijani, and Iranian banking sectors)	Data from Azerbaijan, Turkey, and Iran. The 2018 year.
13	(Jan et al., 2019) <i>International Journal of Asian Business and Information Management</i>	Bankruptcy forecasting and economic sustainability profile of the market leading Islamic banking countries	Data from Malaysia, Saudi Arabia, Iran, UAE, and Kuwait. The year 2009 to 2013
14	(Khasanah et al., 2021) <i>Banks and Bank Systems</i>	Intermediary performance of Islamic banks in the disruption era: Does it contribute to economic growth?	Data from Indonesia The year 2007 to 2019
15	(M. Anwar et al., 2020) <i>International Journal of Islamic and Middle Eastern Finance and Management</i>	Islamic bank contribution to Indonesian economic growth	Data from Indonesia The year 2009 to 2019
16	(Marlina & Sudana, 2020) <i>Journal of Critical Reviews</i>	Does the population number, the economic growth, and the inflation influence the growth of Islamic Bank in Indonesia?	Data from Indonesia The year 2009 to 2018
17	(Mensi et al., 2020) <i>Economic Systems</i>	Impact of Islamic banking development and major macroeconomic variables on economic growth for Islamic countries: Evidence from panel smooth transition models	Data from 16 Islamic countries, MENA and non-MENA The year 1994 to 2014
18	(Saleem et al., 2021) <i>Economic Annals-XXI</i>	Modes of Islamic financing and aggregate economic output: Evidence from Islamic banking industry of Pakistan	Data from Pakistan The year 2005 to 2019
19	(Solarin et al., 2018) <i>Journal of International Financial Markets, Institutions and Money</i>	Influence of economic factors on disaggregated Islamic banking deposits: Evidence with structural breaks in Malaysia	Data from Malaysia The year 2007 to 2016
20	(Sumarti et al., 2018) <i>4th IEEE International Conference on Engineering Technologies and Applied Sciences</i>	Has the growth of Islamic banking had impact to economic growth in Indonesia?	Data from Indonesia Then year 2003 to 2013
21	(Ullah et al., 2021) <i>International Journal of Finance and Economics</i>	Exploring asymmetric relationship between Islamic banking development and economic growth in Pakistan: Fresh evidence from a non-linear ARDL approach	Data from Pakistan The year 2007 to 2017

Table 1 describes that there were 2 articles published in 2018 (9.52%), in 2019 there were 3 articles (14.28%), in 2020 there were 3 articles (14.28%), in 2021 there were 9 articles (42.87%), and in 2022 there will be 4 articles (19.05%). There are 7 articles (33.33%) using data from several countries and only 14 articles (66.67%) from a single country. Articles that use data from a single country are from Jordan (3 articles), Indonesia (5 articles), Saudi Arabia (1 article), UAE (1 article), Turkey (1 article), Pakistan (2 articles), and Malaysia (1 article).

Content Analysis

The results of the content analysis of the selected articles explain that studies related to the analysis of financial performance in Islamic banks can be grouped into 3, namely (1) the influence of financial performance on other variables, (2) variables that influence financial performance, and (3) comparing values certain financial performance with other financial performance values.

Influence of financial performance on other variables

An Islamic bank's financial performance affects the Islamic bank's external, for example, economic growth, and can also affect other performance in the Islamic bank (internal), such as the credit risk provided. Previous research explained that several performance measurements of Islamic banks can have the same and different effects on economic growth. Some of the previous articles that explain several financial performance measurements that affect economic growth include:

- a) Financing channeled by Islamic banks influences economic growth positively and significantly (Alshebel et al., 2019). This article also uses control variables such as money supply (M3), capital market index, and the existence of an open market.
- b) Net interest margin, non-interest income, and the loan granted

positively affect the country's economy (Gulaliyev et al., 2021).

- c) There is a 2-way relationship between deposits and economic growth in both the long and short term, and financing influences the economic relationship simultaneously in the long term (M. Anwar et al., 2020).
- d) Loans, net loans, deposits, and sizes affect economic growth positively during normal times, and negatively when the economy is strengthening (Mensi et al., 2020).
- e) The growth of Islamic banks does not significantly affect economic growth (Sumarti et al., 2018).
- f) Deposits and financing positively affect economic growth if there is a positive shock from Islamic banks both in the long and short term (Ullah et al., 2021).
- g) Financing and third-party funds cannot as an intermediary as a whole contribute to long-term economic growth (Khasanah et al., 2021).

In general, the results of this analysis explain that the financial performance of Islamic banks moderately influences the country's economy positively. Even so, it still appears that the role of Islamic banks has not been optimal in increasing economic growth, especially in Indonesia.

Besides influencing economic growth, the financial performance of Islamic banks also influences:

- a) Islamic banks and economic growth together play a role in reducing poverty (Agustina et al., 2022). The role of Islamic banks is measured by total financing, financing-to-deposit ratio, ROA, and third-party funds.
- b) Islamic banks influence the business community (Saleem et al., 2021). Financing in the form of Non-Profit Loss Sharing (Non-PLS) has a

positive influence, PLS does not affect, and Non-performing Assets have a negative influence on the business community.

The previous article explained that Islamic banks directly improve the economic level of society. With the increase in the financial performance of Islamic banks, the economic life of the people increases. When analyzed further, the type of financing that has a greater influence on increasing welfare is the channeling of non-profit loss sharing (NPLS) financing.

The financial performance of Islamic banks that affects the other performance of Islamic banks themselves (internally), among others:

- a) An increase in the amount of financing will increase the amount of credit risk. Equity as a moderate variable positively influences the relationship between financing and credit risk (Abbas & Ali, 2021).
- b) Increasing ROA will increase Non-Performing Loans (NPL). A decrease in ROE will increase NPL. The interaction between ROA and ROE is a trade-off in risk mitigation (Ben Bouheni et al., 2022).
- c) Increasing customer savings in the bank as measured by increasing assets positively affects the channeling of funds (financing) used for economic development (Alrawahdeh & Zyadat, 2021).
- d) Current financial performance is used to predict future financial developments and performance (Eti et al., 2019). The variables used are total assets, ROA, total capital, NPL, liquidity position, and items on the off-balance sheet.
- e) Financial performance can predict bankruptcy (Jan et al., 2019). The variables used are working capital to total assets, retained earnings to total assets, EBIT to total assets, and the book value of equity to total equity.

Islamic banks' financial performance in the past can be used to predict what could

happen to financial performance in the future. Analysis of financial performance that has occurred can be the basis for making decisions and actions to achieve the desired financial performance goals in the future.

Variables influence financial performance

The values of financial performance in Islamic banks are influenced by the banks external factors, such as the economy, and banks internal factors, such as bank liquidity. Several articles discussing external factors that influence the financial performance of Islamic banks include:

- a) Inflation, economic growth, and financial market indices influence the financial performance of Islamic banks as measured by ROA, ROE, and EPS (K. K. Abdo, 2021).
- b) Population, economic growth, and inflation positively influence the growth of Islamic banks as measured by the development of third-party funds in the banks (Marlina & Sudana, 2020).
- c) The industry index has a positive influence on the number of deposit funds in Islamic banks. Interest rates on savings in conventional banks have a positive influence on deposits in Islamic banks. The role of Islamic indexes and foreign exchange rates influence deposits in Islamic banks in various ways (Solarin et al., 2018).
- d) Increased economic uncertainty does not influence the financial performance and risks of Islamic banks (Bilgin et al., 2021). Islamic bank financial performance measurement uses ROA and comparison of equity with total assets.

The financial performance of Islamic banks is influenced by economic conditions. This is a natural thing because with increasing economic activity, economic agents need the role of banks in running their businesses. However, there are interesting things in the study of Bilgin et al. (2021), namely, when there is economic uncertainty, there is no effect on the financial

performance of Islamic banks. This could be due to Islamic bank customers who are emotional. Whatever the economic or environmental conditions that occur, these customers remain loyal to using the services of Islamic banks in their business affairs.

Several articles discuss internal factors that influence the financial performance of Islamic banks, including:

- a) ROE is influenced by the liquidity factor and ROA is not affected by the liquidity factor (K. Abdo et al., 2021). Liquidity is measured by CAR and other liquidity ratios.
- b) Disclosure on sustainability, economics, and the environment does not significantly influence bank performance. Social Disclosure (CSR) positively and significantly influences bank performance (Ellili & Nobanee, 2022).
- c) Deposits in Islamic banks are influenced by the rate of return on savings and deposits in Islamic banks as well (Solarin et al., 2018).

The strategies and policies implemented by management influence the financial performance of Islamic banks. Therefore, all actions taken by management must consider the impact on financial performance.

Comparison of financial performance

Financial performance data can also be used to make comparisons between Islamic banks and conventional banks, and the performance of Islamic banks between countries. Articles that discuss comparisons between Islamic banks and conventional banks include:

- a) Islamic banks excel compared to conventional banks on TFPG measurements both before and after the crisis (Azzam & Rettab, 2022). TFPG (Total Factor Productivity Growth) consists of total assets, labor costs, physical capital costs, and borrowed money costs.
- b) There are differences in disclosure between Islamic banks and conventional banks (Ellili &

Nobanee, 2022). Disclosures compared are economic, environmental, and CSR. Conventional banks are more open than Islamic banks.

The characteristics of Islamic and conventional banks are different. Therefore, a comparative analysis was carried out on the financial performance of the two types of banks. What is good about each type of bank can be applied to produce an increase in financial performance, for example, it is necessary to increase disclosure on Islamic banks so that they have a positive effect on their financial performance.

A comparison of the financial performance of Islamic banks between countries is explained by Gulaliyev et al. (2021). Financial performance of Islamic banks that affects economic growth is different in each of the countries of Azerbaijan, Iran, and Turkey (Gulaliyev et al., 2021). In Azerbaijan, the net interest margin, and the ratio of non-interest income to total income, the ratio of loans granted to state enterprises, are influencing economic growth. In Iran, the ratio of loans granted to state enterprises is influencing economic growth. In Turkey, the ratio of costs to income, net interest margin, the ratio of non-interest income to total income, and return on bank capital (before tax), are influencing economic growth.

Each country has unique characteristics. Therefore, there is a certain financial performance that has a significant influence on a country and not too a significant influence on other countries. However, some similarities apply in all countries, for example, Islamic banks in all countries innovate to survive. However, the types of innovations carried out are different and adapted to existing conditions.

CONCLUSION

Many methods to measure the financial performance of a company. Measure the financial performance of Islamic banks, the method can be the same or different from the method of measuring the financial performance of conventional banks.

Measurement of this financial performance is not only to find out how the Islamic bank's performance is during a certain period but also for other purposes, such as the influence of Islamic bank performance on economic growth. By using a literature review, this article observes that several kinds of literatures analyze how the financial performance of Islamic banks influences external variables, such as economic growth and the business community. Previous studies have also analyzed how the financial performance of Islamic banks is influenced by external factors, such as economic growth and inflation. Besides external variables, the financial performance of Islamic banks is influenced by internal factors, such as CSR disclosure, and internal variables, such as credit risk.

Several previous studies have also made comparisons of the financial performance of Islamic banks with conventional banks, such as financial performance before and after the crisis. Comparison of the financial performance of Islamic banks in different countries has also been carried out, such as the influence of the financial performance of Islamic banks on economic growth in Azerbaijan, Iran and, Turkey.

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