

The Efficiency Performance of Global Islamic Banks

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ABSTRACT

This paper examines the efficiency performance of the Islamic banks that consist of 14 countries namely Bahrain, Bangladesh, Iran, Jordan, Kuwait, Lebanon, Malaysia, Pakistan, Qatar, Saudi, Tunisia, Turkey, UAE, and Yemen during the period of 2004-2011 with 44 Islamic banks involved. The efficiency estimates of individual banks are evaluated using the Data Envelopment Analysis (DEA) approach. The empirical findings suggest that during the period of study, pure technical efficiency outweighs scale efficiency in the global Islamic banking sector implying that the Islamic banks have been managerially efficient in exploiting their resources to the fullest extent. The empirical findings seem to suggest that the global Islamic banks have exhibited high pure technical efficiency. During the period of study it is found that pure technical efficiency has greater influence in determining the total technical inefficiency of the Global Islamic banking sectors.

INTRODUCTION

The Islamic banking assets with commercial banks had globally reached USD1.54 trillion in 2012 and set to cross USD1.7 trillion in 2013, suggesting an annual growth of 17.6% over the last four years (EY World Islamic Banking Competitiveness Report 2013/2014). The global Islamic banking asset distribution of the rest of the world (including Iran) comprises of 60%, Malaysia 8%, UAE 5%, Kuwait 4%, Qatar 3%, Turkey 2%, Indonesia 1%, Bahrain 1%, and Saudi Arabia 16% (Ernst and Young, 2013). The profitability of Islamic banking has reach the average return on equity of 12.6% for top 20 Islamic banks as compared to comparable conventional average of 15%. Thus, Islamic banking continues to be an exciting growth story characterized by robust macro outlook of core Islamic finance market and increasing share system assets. This indicates the rapid growth and emergence of Islamic banking sectors as one of the determinants in the world's financial health.

Islamic banks are largely protected from the 2008 financial crisis (Willison, 2009; Yilmaz, 2009). Hasan and Dridi (2010) explain that Islamic banking system have highly regulated operational environment guided by Shariah principles prohibited investment in the type of instruments which adversely affected conventional banks and which influenced the crisis. Hence, Islamic financial industry was brought into the spotlight as a possible alternative for investment and banking since recent global financial crisis (Smola and Mirakhor, 2010). As an alternative banking system, Islamic banking emerged in the global landscape with the advent of Islam. Beck et al. (2013) pointed that Islamic financial institutions have a relatively