

**DETERMINANTS OF ISLAMIC AND CONVENTIONAL BANKS
PROFITABILITY IN MALAYSIA**

By

NASHITA HANI BINTI RUSLAN



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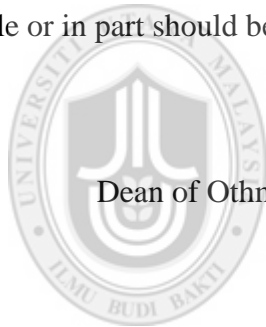
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ABSTRACT

This study investigates the determinants of Islamic and conventional banks profitability of 30 Malaysian commercial banks over the period from 2007 to 2012. Using the Ordinary Least Square (OLS), the result shows that capital significantly influences the return on assets (ROA) of Islamic and conventional banks in Malaysia. This implies that strong capital base is important in determining the profitability of commercial banks in Malaysia. For macroeconomic variables, inflation determines the profitability of Malaysian conventional banks only but not Islamic banks. As for the interest rate, which is measured by base lending rate (BLR), the findings demonstrate that BLR positively and significantly influences the ROA of the full sample. This study also controls for the effect of 2008 global financial crisis on the profitability of Malaysian commercial banks by introducing CRISIS dummy in the model. The result indicates that Malaysian bank profitability is not affected by the 2008 global financial crisis.

KEYWORDS: Bank profitability, Islamic bank, Conventional bank, Malaysia

ABSTRAK

Kajian ini mengkaji faktor-faktor penentuan keberuntungan untuk perbankan islam dan perbankan konvensional dengan menggunakan 30 sampel dari bank perdagangan di Malaysia dari tahun 2007 sehingga 2012. Dengan menggunakan teknik regresi *Ordinary Least Square*, keputusan menunjukkan bahawa modal mempunyai hubungan yang signifikan dengan keberuntungan kepada perbankan islam dan perbankan konvensional. Ini menunjukkan bahawa asas modal yang kukuh adalah penting dalam menentukan keberuntungan bank perdagangan di Malaysia. Untuk faktor luaran, kadar inflasi menentukan keberuntungan untuk perbankan konvensional di Malaysia, dan tidak kepada perbankan islam. Kadar faedah yang ditentukan oleh kadar asas pinjaman menunjukkan hubungan yang positif dan signifikan dalam mempengaruhi keberuntungan kepada perbankan konvensional dan perbankan islam. Kajian ini juga mengkaji kesan krisis kewangan pada tahun 2008 ke atas keberuntungan bank perdagangan di Malaysia dengan memperkenalkan *CRISIS dummy* di dalam model. Keputusan menunjukkan bahawa kadar keberuntungan bank di Malaysia tidak dipengaruhi oleh krisis kewangan pada tahun 2008.

KATA KUNCI: Keuntungan bank, perbankan islam, perbankan konvensional, Malaysia.

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Chapter One: Introduction

1.1 Background of the study

The banking sector is an important source of financing for the domestic economy. The development of the banking system, especially for domestic banking institutions is vital to facilitate and support the economic growth and transformation process. According to Anthanasoglou *et al.* (2005), a sound and profitable banking sector is better able to withstand negative shocks and contribute to the stability of the financial system. Moreover, Ramlall (2009) also stated that a level and sound profitable banking sector is prerequisite for financial stability after the 2008 US Subprime crisis which had affected many countries worldwide.

Malaysia is one of the unique countries which operate a dual banking where the Islamic banking system operates in parallel with the conventional banking system (Country Report, 2012). The dual financial system has proved to be viable as more competitive and sophisticated Islamic financial products have been introduced into the Islamic banking industry and gained popularity and even preference amongst the customers (Muda and Jalil, 2007). Figure 1.1 shows commercial bank asset and Islamic bank asset from the year 2009 until mid-June 2014. It shows that the Islamic bank asset has double increased from the year 2009 until mid- 2014.

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