THE DETERMINANTS OF ISLAMIC BANKS PROFITABILITY: A PANEL DATA ANALYSIS OF MALAYSIA ISLAMIC BANKS

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Abstract

This paper is aims to investigate the factor that affect the Islamic Bank's profitability in Malaysia. This study will focus on 13 Islamic banks in Malaysia that registered under Bank Negara Malaysia. The internal factors that may influences the bank profitability will be observe closely. The dependant variable in this study is Islamic Bank's profitability that will be measure by Return on Asset. Four selected independent variable in this study is bank size, operation cost and asset turnover.The data from the sample of 13 Islamic Bank in Malaysia are pooled for 7 years (2008-2014). The data will be relied on the annual statement of Islamic Bank. Total number of observation is 90. The data can be obtained from Bank Scope.

This study used quantitative secondary data which is panel data and multiple regression model represented by the ordinary least squares (OLS) as the technique to look Factor that affect the Islamic Bank's profitability in Malaysia. It involves the Return on Asset to measure the profitability of Islamic Bank as dependant and the independent variables are bank size, operation cost and asset turnover.

The result from this study reveal that operation cost have a negative significant effect in determining banks' profitability while asset turnover have a positive significant relationship effect in determining banks' profitability. However, the finding in this study indicates that bank size are not be able to explain the variability of profitability of Islamic banks because the result shows an insignificant relationship between bank size and profitability.

TABLE OF CONTENT **PAGE**

CHAPTER 1: INTRODUCTION

1.1 Background of Study

Islamic banking is an activity that is reliable with the principles of shariah and it is suitable to be applying through the development of Islamic economics. Thus, the more accurate term for Islamic banking is actually Shariah compliant finance because it is backed by the principles of Shariah. Despite looking new or seing as the modern trend, actually Islamic finance is old as the religion itself because all the principles that have been use in Islamic Finance is actually derived from Al-Quran.

Accepting of specific interest or fees for loans of money or usury (Riba), whether the payment is fixed or floating is definitely prohibited under the law of Shariah. Investment in business that is contrary with Islamic principles such as alcohol and pork is also prohibited (haram). Although this prohibition has been applied historically in Islamic country, but only in the late of 20th century, the Islamic bank was form to apply this shariah principles to comply with the rightful way in doing a business (Wikipedia,2015).

As of 2014, 1% of the world total assets is represented by the shariah compliant financial institutions. There were over 300 banks and 250 mutual funds around the world complying with shariah principles in 2009 and in 2014 the total assets of shariah compliant is around $2 trillion (Wikipedia,2015). This is the evidence that Islamic banking assets are growing more rapidly year by year.