



**CREDIT RISK IN LOCAL ISLAMIC BANKS:  
A STUDY IN MALAYSIA**

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## **ABSTRACT**

Credit risk is the most predicted risk in the banking system either in conventional or Islamic banks. Credit risk exists as loan and financing is available for the public. Vary with the conventional banking system, Islamic banking have lack of empirical study on macro-credit risk. As such, further studies concerning the stability of the Islamic banking industry has become domineering. Therefore, the objective of this study is to determine the key factor affecting credit risk in Malaysian Islamic banks. This study uses the panel data methods to determine the key factors affecting credit risk in local Islamic Banks in Malaysia. The panel data was collected from 10 local Islamic Banks in Malaysia from year 2008 until 2015. Previous researcher has conducting a research correlated with this topic admit that credit risk is the most important risk available in banking system besides market risk and operational risk. The banking institutions fail to retrieve their financing on time. Thus, this research revealed the significance of some determinant that may affect the credit risk in Islamic banks in Malaysia. Hence, list of the factor affecting credit risk in Malaysian Islamic Banks are bank size, bank profitability, management efficiency, capital buffering and financing growth. Moreover, variables such as bank profitability and management efficiency have significance relationship with credit risk. The data was collected from the financial statement and annual report or any info from the website of those banks. Besides, E-views also used to conduct regression analysis. It is hoped that the findings could draw the attention to determinant of credit risk in Islamic banking so that they can manage the credit risk properly in future.

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## **CHAPTER 1**

### **INTRODUCTION**

#### **1.0 OVERVIEW OF ISLAMIC BANKS IN MALAYSIA**

Malaysia consist about 31,119,381 million number of population currently. Officially, it is about 61.3 percent which equivalent to 18,434,965 is Muslim. Having Muslim in Malaysia is one of the reason the needs of the establishment of Islamic Banking in Malaysia. Islamic banking was at first established at 1983. The first bank named Bank Islam Malaysia Berhad (BIMB). The intention to have Islamic financial system that operate banking and financial according to Shariah was strengthen by the successfulness of the establishment of Islamic Development Bank in Jeddah in 1974 as well as the formation of the Dubai Islamic Bank in 1975 that act as the first Islamic commercial bank.

Lembaga Urusan dan Tabung Haji (LUTH) had issue the proposal to establish the Islamic bank to be coordinated at national level and it was accepted by Government. On 30<sup>th</sup> July 1981, the Prime Minister Dato' Seri Dr. Mahathir Mohamad appointed a National Steering Committee (NSC) to make a revision about the proposal. On 5<sup>th</sup> July 1982, some recommendation was pointed out by NSC. One of the recommendations is only one Islamic bank should be established at initial due to the condition that Islamic banking concept is still new. However, it does not mean that other Islamic bank cannot be established. Other Islamic bank can be launch only after the Bank Islam Malaysia Berhad able to operate efficiently and smoothly.