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Impact of Ownership on Financial Performance of Islamic Banks: The Moderating Role of Deposits, Income and Assets

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Abstract

The study investigates the moderating impact of ownership structure when it interacts with deposits, income and assets empirically. The analysis of the study was performed through 120 Islamic banks globally spanning over a time period of 2005 – 2022. GMM was employed because of the nature of data. The study finds that moderating variables plays a key role in influencing owners for risk taking. For ROA the domestic ownership shows significant positive impact when interacting with deposits, income and liquid assets on Islamic banks performance and significant negative influence when interacts with total assets while foreign owned banks experienced significant negative impact when interacts with deposits and liquid assets. For ROE the study finds that interacting variables (liquid and total assets) with domestic ownership have significant negative impact on financial performance of Islamic banks similarly when foreign owned banks interacts with total deposits also show negative signs. The study conclude that owners of Islamic banks are influenced by moderating factors. Authors suggest transparency in owner's decision, strong and independent board oversight to monitor management decisions.

Keywords: Financial Performance, Islamic Banks, GMM, Ownership, Deposits, Income, Assets

1. Introduction

Financial performance plays a key role in growth and development of business organization. The utmost priority of every financial institution is to enhance their profitability. To increase the profitability banks, management take key decisions. These decisions are sometime influence by their owners. Because they want maximum returns on their investment but this returns may have a cost to depositors of Islamic banks. Where they can lose their deposits due to these decisions in case of loss. Hence creating an ethical and legal problem from Islamic perspective. Several empirical studies have empirically examined it. Some studies find that ownership types have positive impact on financial performance while other oppose these findings.

For instance, Boachie (2023) found positive relationship between foreign ownership and banks profitability because of the higher risk taking by the foreign owners. While, Boateng et al. (2015) states that domestic owned banks are more profitable as compared to foreign owned banks. While, Bousada and Hakimi (2020) found that banks profitability is negatively influenced by multiple large share-holders. Zouari and Taktak (2014) study revealed that inclusion of institutional and foreign shareholders in banking institutions does not influence its performance. Riewsathirathorn et al. (2011) found that increase in ownership concentration of banks decrease their financial performance. Micco et al. (2004) found that ownership have strong correlation ship with performance in developing countries while in industrial countries this relationship was not found. Shawtari (2018) believe that foreign and government owned banks performance is significantly influenced by country's GDP.

It is evident that from the above studies that ownership types can have positive or negative impact on financial performance of banks but what factors actually influence owners to increase or decrease risky investment decision. To answer this, we have selected three factors which are assets, deposits and income. For example, changes in assets may motivate owners to influence decision making. Previous research only focused on ownership type/structure and performance of banking sector. Previous literature has limitations to answer this question. Our study has first answer that whether foreign or domestic ownership has positive or negative impact on financial performance. Then we have explored the moderating impact of ownership with assets, deposits and income. To find out which factor among these actually influence owners to increase risk taking, which ultimately impact performance is the novelty of our study.

Similarly, income structure also impacts banks profitability which is evident from prior research. Mehzabin et al., (2023) is of the view that in the period of lower interest rates the banks non-interest based income plays a pivotal role. Some scholars have the view that income diversification plays an important role in financial performance of banks while other oppose it. For instance, Quyen et al. (2021) states that during crisis period income diversification have significant positive impact on financial performance of banks. Similarly, Vidyarthi (2020) also found that income diversification has a positive influence on performance of banks. Likewise, Luu et al., (2020) observed that income diversification has a significant positive impact on financial performance of commercial banks of Vietnam. While, Mercieca et al., (2007) find a negative correlation between a bank performance and non-interest income i.e. income from fee based activities. Ammar and Boughrara (2019) found that diversified revenue streams have the potential to increase the profitability of banks however the likelihood increase in non-interest income may leads to a bank run. Molyneux and Yip (2013) argue that income volatility of Islamic banks is lower as compared to conventional banks so have lower profitability on risk adjusted basis. Asif and Akhter (2019) contend that past research has not definitively determined the exact influence that diversified revenue streams have on the overall functioning of financial institutions such as banks. Which is why we have added income as an independent variable to our study. The rest of the study is structured as follows: Section#2 presents literature review, section#3 presents methodology, section#4 presents results and discussion and lastly section#5 presents conclusions and recommendations.

2. Literature Review

Numerous studies have examined the financial performance of banks from different perspectives highlighting the importance of financial performance for banking institutions. Atahau and Cronje (2021) examine the impact of various factors, including credit risk, liquidity, age, and equity, on the performance of banks in Indonesia. The authors note that the significance of these effects varies across different ownership types of banks. Zouari and Taktak (2012), carried out an empirical investigation to evaluate the relationship between ownership structure and financial performance. The outcomes of the research indicate that a positive influence on the performance of Islamic banks can be attributed to both family ownership and governmental ownership. On the other hand, banks that have institutional investors or stockholders from other countries are not performing particularly well. Magalhaes et al., (2010) found that the performance of banks that possess dispersed ownership structures is subject to the influence of the interplay between shareholder protection laws and ownership concentration. In circumstances characterized by inadequate shareholder protection, it becomes imperative to prioritize the enhancement of ownership concentration as a means of exerting influence on the performance of banks. Ferri et al., (2015) examined the correlation between ownership structure and performance within the European banking sector. Finding of the study revealed that banks with shareholders demonstrated elevated levels of profitability prior to the crisis.

However, amidst the crisis, it was observed that stakeholder banks, with the exception of private savings banks, exhibited enhanced profitability and loan quality when compared to general shareholder banks.

Mercieca et al., (2007) conducted a study to investigate the benefits obtained from the implementation of diversification strategies by small European banks, the researchers identified a negative correlation between non-interest income and bank performance. Kohler (2015) argue that savings and cooperative banks can greatly benefit from income diversification by increasing the share of non-interest income. Vidyarthi (2020) that income diversification has a positive influence on the performance of banks. Mehzabin et al., (2023) aimed to analyze the effects of non-interest income on bank profitability, taking into account the potential influence of capital structure and operating efficiency. The researchers have made the observation that during periods characterized by lower interest rates, non-interest income plays a pivotal role for banks. Sharma and Anand (2018) study demonstrate a positive association between income diversification and bank risk among medium and large banks, while a negative association was observed among small banks.

Luu et al., (2020) finds a significant and favorable connection between the diversity of a bank's income sources and the institution's overall financial performance. In addition, the study offers evidence that the observed influence is contingent on the ownership structure of the financial organizations that were examined. The study further reveals that, banks with state or foreign ownership as well as banks with foreign ownership gain from revenue diversification, whereas privately owned domestic banks risk adverse effects. Uddin et al., (2022) study revealed that, there is a statistically significant and positive connection between the level of income and asset diversification present in financial institutions and the overall profitability of those institutions. Ammar and Boughrara (2019) carried out research with the purpose of investigating the impact that diversified revenue streams have on the overall financial performance of banks. According to the results of the study, increasing the variety of sources from which a bank generates revenue is one way for financial institutions to boost their overall profitability. However, it is important to highlight that participating in activities that generate non-interest income does increase the likelihood of financial run for banks. Haddawee and Flayyih (2020) found a significant positive relationship between profitability and deposits of commercial banks of Jordan. Where the profitability was highest impacted by time deposits then savings deposits contribution and lastly the current deposits contributions.

3. Methodology

This section details the different estimation techniques used in the study, data sources, variables and models.

3.1 Research Design

The study employs quantitative panel data approach to examine the impact of ownership, deposit and income structure on financial performance.

3.2 Data and Data Sources

To examine the impact of income, deposits and ownership structure on financial performance of Islamic banks we have taken a sample of 120 full-fledged Islamic banks[1] from 25 different countries. The data spans the period of 2005-2022. The data have been taken from different sources. Most of the data have been collected from EIKON data stream, banks annual reports, websites. The Macroeconomic data have been collected from World Development Index (WDI) of World Bank dataset.

3.3 Variables Construction and Definition

This section presents definitions and construction of variables under consideration. The dependent variable of the study is financial stability.

Among independent variables the ownership structure (OS_{ijt}) of Islamic banks is our main variable of our interest. Ownership structure is measure by further dividing it into four types Government, Private, Foreign and Domestic ownership. Bank ownership is measured in percentage form. We have considered a threshold level of 25% or more for a bank to be considered government, private, foreign or domestic owned bank. We have measured it in dummy form. For ownership structure it takes the value of 1 if the bank is privately owned and it takes the value of 0 if the bank is government owned. Similarly, for foreign and domestic owned banks it takes the value of 1 if the bank is foreign owned and takes the value of 0 if it is domestic owned. (DS_{ijt}) represents the deposits' structure which is divided into two types (non-PSIA and PSIA) in which non-PSIA represents current accounts deposits and PSIA represents non-current accounts measured by non-PSIA to total deposits and PSIA to total deposits. For deposits structure we have considered dummy variable by taking a threshold level which takes the value of 1 if the deposits are less than 30% and for non-PSA deposits it takes the value of 0 if the deposits are equal to 30% or more than it. (IS_{ijt}) represents the income structure which is also divided into two types (Non-PLS_Income and PLS-Income) in which Non-PLS_Income stands for income from fee and commission-based activities and PLS-Income represents income from financing activities of Islamic banks which is measured by non-PLS-

[1] See Appendix A for list of Countries and Banks.

Income to total income and PLS-Income to total income. For income structure we have considered dummy variable by taking a threshold level which takes the value of 1 if the income from non-pls activities is less than 30% and for pls income it takes the value of 0 if the deposits are equal to 30% or more than it. (BS_{ijt}) represents the banks specific variables for Bank specific a total of 6 variables are considered which are as follows ($TASS_{ijt}$) represents the total assets of the bank measured by taking natural log of total assets, (EQT_{ijt}) represents the equity to assets ratio of a bank. ($LASS_{ijt}$) presents liquid assets measured by current assets to total assets of a bank, and lastly the (CAR_{ijt}) presents the capital adequacy ratio of the banks. (ME_{ijt}) represents the Macroeconomic variables and a total of two macroeconomic variables are selected for the study which are ($GDPG_{ijt}$) which represents the percentage change in gross domestic products of a country and the (INF_{ijt}) represents the inflation rate. (D_{ijt}) represents the dummy variables which also represents two variables in which ($D1_{ijt}$) represents the financial crisis whether present or not, taking the value of 1 if present and 0 otherwise and ($D2_{ijt}$) represents the deposit insurance of a country whether present or not, taking the value of 1 if present and 0 otherwise.

3.4 Models

As one objective of the study is to explore the moderating impact of ownership structure with deposits on banking performance. Hence, the following empirical model 1 and 2 has been formulated.

$$ROA_{ijt} = \alpha + \beta_1(ROA-1)_{ijt} + \beta_2(OS_{ijt}) + \beta_3(Os_{ijt} * TD_{ijt}) + \beta_4(DS_{ijt}) + \beta_5(IS_{ijt}) + \beta_6(BS_{ijt}) + \beta_7(ME_{ijt}) + \beta_8(D_{ijt}) + f_j + \mu_i + \lambda_t + \varepsilon_{ijt} \ldots\ldots(1)$$

$$ROE_{ijt} = \alpha + \beta_1(ROE-1)_{ijt} + \beta_2(OS_{ijt}) + \beta_3(Os_{ijt} * TD_{ijt}) + \beta_4(DS_{ijt}) + \beta_5(IS_{ijt}) + \beta_6(BS_{ijt}) + \beta_7(ME_{ijt}) + \beta_8(D_{ijt}) + f_j + \mu_i + \lambda_t + \varepsilon_{ijt} \ldots\ldots(2)$$

The dependent variables in model 1 and 2 is return on assets and return on equity, the first independent variable is ownership structure (domestic and foreign), the second independent variable plays moderating role when (ownership structure interacts with deposits), the third independent variable is deposit structure, fourth is income structure, fifth is bank specific (EQT for equity and CAR for capital adequacy ratio), sixth is macroeconomic (GDP and inflation), seventh is Dummy (D1 for financial crisis and D2 for deposit insurance), i denotes Islamic banks, t represents the time period and ,.. j represents the country, μ represents cross-sectional specific effects and λ stands for time specific effects. As one objective of the study is to explore the moderating impact of ownership structure with total assets on banking performance. Hence, the following empirical model 3 and 4 has been formulated.

$$ROA_{ijt} = \alpha + \beta_1(ROA-1_{ijt}) + \beta_2(OS_{ijt}) + \beta_3(OS_{ijt} * TA_{ijt}) + \beta_4(DS_{ijt}) + \beta_5(IS_{ijt}) + \beta_6(BS_{ijt}) + \beta_7(ME_{ijt}) + \beta_8(D_{ijt}) + f_j + \mu_i + \lambda_j + \varepsilon_{ijt} \ldots\ldots(3)$$

$$ROE_{ijt} = \alpha + \beta_1(ROE-1_{ijt}) + \beta_2(OS_{ijt}) + \beta_3(OS_{ijt} * TA_{ijt}) + \beta_4(DS_{ijt}) + \beta_5(IS_{ijt}) + \beta_6(BS_{ijt}) + \beta_7(ME_{ijt}) + \beta_8(D_{ijt}) + f_j + \mu_i + \lambda_j + \varepsilon_{ijt} \ldots\ldots(4)$$

3.4 Estimation Technique

As data set is panel hence to came with an appropriate estimation technique, we apply a number of specification tests. For instance, to make a choice between pooled OLS and random effects we apply B&P (1979) test than Breush-Pagan (1979) than Hausman (1978) then Redundant fixed effects and all of these tests results leads us to Arrelano and Bond's (1991) Generalise Method of Movement (GMM) to estimate our dynamic model of panel data.

4. Results and Discussions

This section presents and discuss the empirical findings of the study.

Table 1: Moderating Effects of Domestic Owned Islamic Banks on Financial Performance

Dependent Variable is ROA (Financial Performance)						
Variables	**Model 1**	**Model 2**	**Model 3**	**Model 4**	**Model 5**	**Model 6**
ROA_{it-1}	.2662	.2381	.2522	.2287	.2378	.2391
	(.0112)***	(.0100)***	(.0121)***	(.0124)***	(.0096)***	(.0117)***
EQT_{it}	-.0000	-.0005	.0025	-.0000	-.0017	-.0014
	(.0015)	(.0020)	(.0018)	(.0016)	(.0019)	(.0015)
CAR_{it}	-.0075	-.0054	-.0073	-.0063	-.0061	-.0056
	(.0015)***	(.0022)**	(.0017)***	(.0014)***	(.0020)***	(.0016)***
$GDPG_{it}$	.0119	.0108	.0119	.0095	.0117	.0112

	(.0016)***	(.0009)***	(.0016)***	(.0010)***	(.0012)***	(.0017)***
INF_{it}	-.0000	.0001	-.0001	.0000	.0001	-.0000
	(.0001)	(.0002)	(.0001)	(.0002)	(.0003)	(.0001)
$D1_{it}$	.0452	-.0125	.0499	.0016	.0184	.0417
	(.0035)***	(.0107)	(.0039)	(.0091)	(.0084)***	(.0041)***
$D2_{it}$	-.0343	.0291	-.0239	.0120	-.0263	-.0345
	(.0034)***	(.0350)	(.0035)***	(.0324)	(.0304)	(.0033)***
$DEPS_{it}$			-.0025	-.0090	-.0160	-.0181
			(.0045)	(.0070)	(.0076)**	(.0097)*
INC_{it}	.0418	.0311			.0359	.0344
	(.0090)***	(.0101)***			(.0108)***	(.0115)***
LA_{it}	.0039		.0033			
	(.0008)***		(.0008)***			
TA_{it}		-.0549		-.0398		
		(.0103)***		(.0068)***		
$DOWN * TD_{it}$	.0174	.1711				
	(.0306)	(.0366)***				
$DOWN * TI_{it}$			.0348	.0514		
			(.0216)	(.0262)*		
$DOWN * TA_{it}$				-.0292		
				(.0047)***		
$DOWN * LA_{it}$						.0076
						(.0011)***
Constant	.6933	1.854	.2522	1.612	1.207	.7046
	(.0450)***	(.2184)***	(.0121)***	(.1450)***	(.0634)***	(.0337)***
Panel B						
No. of Obs.	1142	1146	1142	1146	1146	1146
No. of Firms	89	89	89	89	89	89
No. of Inst.	146	146	146	146	146	146
AR(1)	-5.508	-5.226	-5.369	-5.169	-5.280	-5.204
P-value	.0000	.0000	.0000	.0000	.0000	.0000
AR(2)	.5909	.8373	.5052	.6896	.7403	.8020
p-value	.5546	.4024	.6134	.4904	.4591	.4225
J-stat	82.65	82.74	79.94	83.38	83.42	81.69
p-value	.90	.89	.90	.89	.89	.89

Note: *, **, *** shows the significance level at 1%, 5% and 10%. To examine the over identification restriction of instruments J-statistics test it by considering the null hypothesis that that instruments are valid. To examine the second order correlation AR(2) tests it with the null hypothesis that no second order correlation is included in null hypothesis. The values closed in the parenthesis represents std. error. Banking Stability is measured by Z-score which is the dependent variable for every model.

The above table present the moderating effects of domestic owned Interest free banks on bank performance when it interacts with deposits, income, total assets and liquid assets. The lagged dependent variable is highly significant in all specifications, which indicates that current performance of Interest free banks depends on its past. The study first moderating variable is domestic owned Interest free banks when it interact with total deposits ($DOWN_{ijt} * TD_{ijt}$) specification 1 results revealed positive results. The coefficient value of (.0174) reveals that domestic ownership increases the bank performance of Interest free banks by .0174 units but since this influence is insignificant this means that bank performance is not increased in real sense by domestic owners. The specification 2 results revealed significant positive influence at 1%. Which further revealed that when domestic ownership interacts with total deposits it has a significant positive impact. The coefficient value of (.1711) reveals when domestic owners interacts with deposits it increases the bank performance of Interest free banks .1711 units. Specification 3 revealed positive results when domestic ownership interacts with income

($DOWN * TI_{it}$). The coefficient value of (.0348) reveals that domestic ownership increases the bank performance of Interest free banks by .0348 units but since this influence is insignificant this means that bank performance is not increased in real sense by domestic owners when they interact with income but this influence changes in specification 4 and the results reveals a significant positive influence at 10%. The coefficient value of (.0514) reveals that when domestic ownership interacts with income the bank performance increases by .0514 units. Specification 5 results reveals that significant negative influence on bank performance by at 1% when domestic owned banks interacts with total assets ($DOWN * TA_{it}$). The coefficient value of (-.0292) reveals that when domestic owned banks interact with total assets it decreases their bank performance by .0292 units. Specification 6 results reveals significant positive influence at 1% when domestic owned banks interacts with liquid assets ($DOWN * LA_{it}$). The coefficient value of (.0076) reveals when domestic owners interacts with liquid assets it increases their bank performance by .0076 units.

The study second independent variable is total deposits the specification 3 and 4 results reveals insignificant negative influence of deposits on bank performance of domestic owned banks. Since the results are insignificant this means that it has no real influence on bank performance. Specification 5 reveals significant negative influence on bank performance at 5%. The coefficient value of (-.0160) reveals that total deposits decreases the bank performance of domestic owned Interest free banks by -.0160 units. Specification 6 results also reveals significant negative influence of domestic owned banks by 10%. The coefficient value of (-.0181) reveals that deposits decreases the bank performance of domestic owned Interest free banks decreases by .0181 units. The study third independent variable is total income and the specification 1 results reveals significant positive results at 1% level which means income levels have significant influence on bank performance of domestic owned Interest free banks in a positive way. The coefficient value of (.0418) indicates that income level increases the bank performance of domestic owned Interest free banks by .0418 units. Specification 2 results reveals significant positive results at 1% level which means income levels have significant influence on bank performance of domestic owned Interest free banks in a positive way. The coefficient value of (.0311) indicates that income level increases the bank performance of domestic owned Interest free banks by .0311 units. Specification 5 results reveals significant positive results at 1% level which means income levels have significant influence on bank performance of domestic owned Interest free banks in a positive way. The coefficient value of (.0359) indicates that income level increases the bank performance of domestic owned Interest free banks by .0359 units. Specification 6 results reveals significant positive results at 1% level which means income levels have significant influence on bank performance of domestic owned Interest free banks in a positive way. The coefficient value of (.0344) indicates that income level increases the bank performance of domestic owned Interest free banks by .0344 units.

Equity value (EQT_{ijt}) is statistically significant for all of the specifications positively. Capital adequacy ratio (CAR_{ijt}) is also positively significant for all of the specifications.

However, liquid ($LASS_{ijt}$) and total assets ($TASS_{ijt}$) of Interest free banks have a negative and significant influence on the financial soundness of Interest free banks. The ($GDPG_{ijt}$) is negatively significant for specification 1,2,3 and 5 while it is positively significant for specification 4 and 6 where the domestic owned banks interact with total income and liquid assets. Inflation (INF_{ijt}) positively and significantly influence the financial soundness when using the interaction for all of our models. Dummy variable (D_{ijt}) is positively significant for specification 1 when domestic owned banks interact with total deposits (TD_{ijt}) . For specification 2,4,5 and 6 the dummy variable ($D1_{ijt}$) is positive and highly significant. While the dummy variable ($D1_{ijt}$) is negative and highly significant for specification 3 when the domestic owned banks interact with total income. The dummy variable ($D2_{ijt}$) is highly positively significant in all specifications.

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Table 2: *Moderating Effects of Foreign Owned Islamic Banks on Financial Performance*

Dependent Variable is ROA (Financial Performance)						
Variables	**Model 1**	**Model 2**	**Model 3**	**Model 4**	**Model 5**	**Model 6**
ROA_{it-1}	.3449	.3887	.3866	.2048	.4149	.3481
	(.0743)***	(.0957)***	(.0951)***	(.0911)**	(.0816)***	(.0921)***
EQT_{it}	-.0065	-.0098	.0013	-.0026	.0029	.0030
	(.0076)	(.0096)	(.0089)	(.0081)	(.0095)	(.0083)
CAR_{it}	.0029	-.0022	-.0054	.0018	-.0026	.0044
	(.0045)	(.0064)	(.0055)	(.0068)	(.0065)	(.0046)
$GDPG_{it}$	-.0025	.0060	.0024	-.0015	.0020	-.0041
	(.0049)	(.0042)	(.0045)	(.0051)	(.0041)	(.0048)
INF_{it}	.0002	.0002	-.0008	-.0001	-.0010	-.0006
	(.0006)	(.0003)	(.0004)*	(.0004)	(.0005)*	(.0005)
$D1_{it}$	-.0357	.0815	.0207	-.1056	.0308	-.0114
	(.0148)**	(.0563)	(.0314)	(.0819)	(.0821)	(.0104)
$D2_{it}$	.0013	.0315	.0014	-.0084	.0490	-.0019
	(.0082)	(.0644)	(.0213)	(.0244)	(.0790)	(.0108)
$DEPS_{it}$			.0258	.0635	.0026	.0275
			(.0394)	(.0397)	(.0404)	(.0278)
INC_{it}	-.0113	-.0178			-.0373	-.0455
	(.0242)	(.0199)			(.0221)*	(.0203)**
LA_{it}	-.0168		-.0192			
	(.0054)***		(.0061)***			
TA_{it}		.1154		-.1117		
		(.0505)**		(.0662)*		
$FOWN * TD_{it}$	-.6281	-1.110				
	(.3341)*	(.4760)**				
$FOWN * TI_{it}$			.3419	.1571		
			(.2513)	(.2623)		
$FOWN * TA_{it}$					.0155	
					(.0466)	
$FOWN * LA_{it}$						-.0217
						(.0077)***
Constant	1.133	-1.3841	.7628	2.850	.1905	.7912
	(.2145)***	(.8772)	(.1851)***	(1.409)**	(.8675)	(.1312)***
Panel B						
No. of Obs.	397	399	397	399	399	399
No. of Firms	31	31	31	31	31	31

No. of Inst.	146	146	146	146	146	146
AR(1)	-3.315	-3.638	-3.322	-2.810	-3.627	-3.215
P-value	.0009	.0003	.0009	.0049	.0003	.0013
AR(2)	.2020	.0144	.7039	.0259	.5450	.2938
p-value	.8399	.9885	.4815	.9793	.5857	.7688
J-stat	19.61	18.46	23.92	19.62	23.66	17.22
p-value	.90	.90	.90	.90	.90	.90

The above results present the moderating effects of foreign owned Interest free banks on bank performance when it interacts with deposits, income, total assets and liquid assets. The lagged dependent variable is highly significant in all specifications, which indicates that current performance of Interest free banks depends on its past. The study first moderating variable is foreign owned Interest free banks when it interact with total deposits ($FOWN_{ijt} * TD_{ijt}$) and specification 1 results revealed significant negative results at 10%. The coefficient value of (-.6281) reveals that foreign ownership decreases the bank performance of Interest free banks by .6281. The specification 2 results revealed significant negative influence at 5% level. Which further revealed that when foreign ownership interacts with total deposits it has a significant negative impact. The coefficient value of (-1.110) reveals when domestic owners interact with deposits it decreases the bank performance of Interest free banks 1.110 units. These results are contrary to specification 1 and 2 results in case of domestic owned banks. Specification 3 revealed insignificant positive results when foreign ownership interacts with income ($FOWN * TI_{it}$). The coefficient value of (.3419) reveals that foreign ownership increases the bank performance of Interest free banks by .0348 units but since this influence is insignificant this means that bank performance is not increased in real sense by foreign owners when they interact with income. Specification 4 results also reveals insignificant positive results when foreign ownership interacts with income ($FOWN * TI_{it}$). The coefficient value of (.1571) reveals that foreign ownership increases the bank performance of Interest free banks by .1571 units but since this influence is insignificant this means that bank performance is not increased in real sense by foreign owners when they interact with income. Specification 5 results also reveals insignificant positive results when foreign ownership interacts with income ($FOWN * TA_{it}$). The coefficient value of (.0155) reveals that foreign ownership increases the bank performance of Interest free banks by .0155 units but since this influence is also insignificant this means that bank performance is not increased in real sense by foreign owners when they interact with total assets. Specification 6 results reveals that significant negative influence on bank performance at 1% level when foreign owned banks interacts with liquid assets ($FOWN * LA_{it}$). The coefficient value of (-.0217) reveals that when foreign owned banks interact with total assets it decreases their bank performance by .0217 units. This means foreign owners are not efficient in managing liquid assets from investment perspective.

The study second independent variable is total deposits which shows insignificant positive results for all of the specification. Since the results are insignificant this means that it has no real influence on bank performance. This means foreign owned Interest free banks are not efficient in managing their deposits efficiently which results in no contribution to bank performance from deposits level of foreign owned banks. The study third independent variable is total income and the specification 1 and 2 results reveals insignificant negative results which means that income levels have no significant influence on bank performance of foreign owned Interest free banks in a positive way. The coefficient value of (-.0113) in specification 1 indicates that income level decrease the bank performance of foreign owned Interest free banks by .0113 units and coefficient value of (-.0178) in specification 2 indicates a decrease in bank performance of foreign owned banks by .0178 units. Since this influence is insignificant this means that the decrease in bank performance will be not effective. Specification 5 results reveals significant negative results at 10% level which means income levels has significant influence on bank performance of foreign owned Interest free banks in a negative way. The coefficient value of (-.0373) indicates that income level decreases the bank performance of foreign owned Interest free banks by .0373 units. Specification 6 results reveals significant negative results at 10% level which means income levels have significant influence on bank performance of domestic owned Interest free banks in a negative way. The coefficient value of (-.0455) indicates that income level decreases the bank performance of foreign owned Interest free banks by .0455 units.

The bank specific variable Equity (EQT_{ijt}) does not show any statistically significant influence on bank performance for all of the specifications. The variable Capital adequacy ratio (CAR_{ijt}) is also not significant for all of the specifications. However, liquid ($LASS_{ijt}$) of Interest free banks have a negative and significant influence on the financial soundness of Interest free banks while total assets ($TASS_{ijt}$) show significant positive influence for specification 2 and significant negative influence for specification 4. The macroeconomic variable gross domestic product growth ($GDPG_{ijt}$) shows insignificant for all of the specifications. The variable inflation (INF_{ijt}) shows significant

negative results for specifications 3 and 5 while it does not show any significant influence for specification 1,2,4 and 6. Dummy variable (D_{ijt}) shows significant negative influence for specification 1 when domestic owned banks interact with total deposits (TD_{ijt}) and for specification 2,4,5 and 6 the dummy variable ($D1_{ijt}$) does not show any significant impact. The dummy variable ($D2_{ijt}$) is doesn't show any significant influence in all specifications.

Table 3: ***Empirical Findings "Moderating Effects of Domestic Owned Islamic Banks on ROE"***

Dependent Variable is ROE (Financial Performance)						
Variables	**Model 1**	**Model 2**	**Model 3**	**Model 4**	**Model 5**	**Model 6**
ROE_{it-1}	.4100	.3851	.4111	.4115	.3907	.4079
	(.0053)***	(.0098)***	(.0048)***	(.0063)***	(.0075)***	(.0088)***
EQT_{it}	-.0701	-.1103	-.0728	-.0849	-.0820	-.0679
	(.0154)***	(.0161)***	(.0111)***	(.0129)***	(.0122)***	(.0137)***
CAR_{it}	.0031	-.0213	-.0055	.0079	.0119	-.0028
	(.0171)	(.0111)*	(.0136)	(.0134)	(.0107)	(.0125)
$GDPG_{it}$	.1059	.0934	.1123	.1156	.0972	.1138
	(.0100)***	(.0084)***	(.0065)***	(.0092)***	(.0095)***	(.0071)***
INF_{it}	.0222	.0224	.0211	.0219	.0224	.0218
	(.0009)***	(.0005)***	(.0012)***	(.0012)***	(.0007)***	(.0007)***
$D1_{it}$	.1496	-.0413	.2685	-.0104	-.0112	.1609
	(.0579)**	(.0518)	(.0826)***	(.0793)	(.0763)	(.0560)***
$D2_{it}$	-.9160	-.4836	-.3937	-.5577	-.7937	-1.028
	(.1243)***	(.1934)**	(.2771)	(.2757)	(.2027)***	(.1910)***
$DEPS_{it}$			-.0767	-.3249	-.3634	-.4689
			(.1536)	(.0801)***	(.0597)***	(.0497)***
INC_{it}	.1671	.2468			.2116	.2216
	(.0507)***	(.0324)***			(.0412)***	(.0399)***
LA_{it}	.0509		.0550			
	(.0041)***		(.0046)***			
TA_{it}		-.1869		-.1084		
		(.0515)		(.0615)*		
$DOWN * TD_{it}$	-.2488	.3170				
	(.3352)	(.2691)				
$DOWN * TI_{it}$			.1576	.4078		
			(.1760)	(.2534)		
$DOWN * TA_{it}$					-.1356	
					(.0703)*	
$DOWN * LA_{it}$						.1051
						(.0066)***
Constant	4.899	10.41	4.420	7.931	7.861	4.900
	(.4598)***	(1.349)***	(.4671)***	(1.065)***	(.9039)***	(.2684)***

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Panel B						
No. of Obs.	1142	1146	1142	1146	1146	1146
No. of Firms	89	89	89	89	89	89
No. of Inst.	146	146	146	146	146	146
AR(1)	-5.092	-4.942	-5.119	-5.118	-5.084	-5.083
P-value	.0000	.0000	.0000	.0000	.0000	.0000
AR(2)	-.5822	-.4557	-.4673	-.3599	-.4992	-.4311
p-value	.5604	.6485	.6402	.7189	.6176	.6663
J-stat	83.71	77.16	79.91	86.24	81.30	83.15
p-value	.89	.90	.90	.89	.89	.89

The above results present the moderating effects of domestic owned Interest free banks on bank performance when it interacts with deposits, income, total assets and liquid assets. The lagged dependent variable is highly significant in all specifications, which indicates that current performance of Interest free banks depends on its past. The study first moderating variable is domestic owned Interest free banks when it interact with total deposits ($DOWN_{ijt} * TD_{ijt}$) and the results revealed insignificant influence on bank performance in specifications 1&2. The second moderating variable is the interaction between domestic owned banks and total income ($DOWN_{ijt} * TI_{ijt}$) also show insignificant influence on bank performance of Interest free banks in specification 3&4. The third moderating variable in which domestic owned banks when they interact with total assets ($DOWN_{ijt} * TA_{ijt}$) the results shows a significant negative influence on bank performance. The fourth moderating variable where liquid assets when interacts with domestic owned Interest free banks ($DOWN_{ijt} * LA_{ijt}$) has a significant positive influence on bank performance of Interest free banks. The second independent variable of interest of the study is total deposits (TD_{ijt}) which indicates no significant influence on bank performance for specification 3 and highly significant negative influence in specification 4,5&6. The third independent variable is total income (TI_{ijt}) has a highly significant influence on bank performance in specifications 1,2,5&6.

For bank specific variables the study first variable is total equity (EQT_{ijt}) is highly negatively significant for all of the specifications. Capital adequacy ratio (CAR_{ijt}) shows significant negative influence on bank performance in specification 2 and has no significant influence for the remaining specifications. However, liquid ($LASS_{ijt}$) in specification 1&3 show highly significant positive influence on bank performance and total assets ($TASS_{ijt}$) of Interest free banks has a negative significant influence on the financial soundness of Interest free banks in specification 3 while it doesn't show any significant influence on bank performance in specification 2. The macroeconomic variable ($GDPG_{ijt}$) is positively significant for all of the specification which means that GDP growth is crucial for positive bank performance of Interest free banks. Inflation (INF_{ijt}) positively and significantly influence the financial soundness when using the interaction for all of our models which means that when domestic ownership interacts with deposits, income and assets the influence of inflation changes. Dummy variable ($D1_{ijt}$) is positively significant for specification 1,3&6 when domestic owned banks interact with total deposits (TD_{ijt}), total income () and liquid assets (). While for specification 1,4,&5 the dummy variable ($D1_{ijt}$) has insignificant impact. The dummy variable ($D2_{ijt}$) is highly negatively significant in specifications 1,2,5&6 while has insignificant influence on bank performance in specification 3&4.

Table 4: ***Empirical Findings "Moderating Effects of Foreign Owned Islamic Banks on ROE"***

Dependent Variable is ROE (Financial Performance)						
Variables	**Model 1**	**Model 2**	**Model 3**	**Model 4**	**Model 5**	**Model 6**
ROE_{it-1}	.3036	.4032	.3812	.3807	.3380	.3231
	(.1207)**	(.0686)***	(.0969)***	(.0872)***	(.1323)**	(.1090)***
EQT_{it}	.0106	.0136	-.0003	.0420	.0680	.0951
	(.0887)	(.0753)	(.0892)	(.0937)	(.0633)	(.0879)
CAR_{it}	-.0836	-.0822	-.0164	-.0341	.0065	.0370
	(.0551)	(.0590)	(.0563)	(.0419)	(.0594)	(.0480)

$GDPG_{it}$	.1125	.1647	.1814	.1427	.1479	.1358
	(.0277)***	(.0283)***	(.0297)***	(.0191)***	(.0251)***	(.0269)***
INF_{it}	.0161	.0186	.0086	.0093	.0078	.0112
	(.0025)***	(.0040)***	(.0030)***	(.0029)***	(.0033)**	(.0017)***
$D1_{it}$	-.0424	.1203	.0482	-.0524	.1182	-.1525
	(.4721)	(.9228)	(.5004)	(.3456)	(.8420)	(.3887)
$D2_{it}$	-.3164	.5404	.4867	.2217	.2679	-.5248
	(.5146)	(.3804)	(.7002)	(.2918)	(.4709)	(.4582)
$DEPS_{it}$			-.7685	-.3873	-1.088	.1424
			(.8025)	(.9858)	(1.217)	(.8102)
INC_{it}	-.2389	-2.234			-.5610	-1.088
	(1.495)	(1.272)*			(.8599)	(1.056)
LA_{it}	-.0341		-.0268			
	(.0421)		(.0414)			
TA_{it}		.1974		-.3328		
		(.7131)		(.2963)		
$FOWN * TD_{it}$	-5.121	-12.07				
	(2.721)*	(3.916)***				
$FOWN * TI_{it}$			4.599	.7915		
			(3.504)	(1.645)		
$FOWN * TA_{it}$					.0642	
					(.7724)	
$FOWN * LA_{it}$						-.0501
						(.0488)
Constant	8.764	5.510	2.409	10.62	3.093	4.394
	(2.802)***	(15.97)	(1.935)	(6.682)	(11.11)	(2.271)*
Panel B						
No. of Obs.	397	399	397	399	399	399
No. of Firms	31	31	31	31	31	31
No. of Inst.	146	146	146	146	146	146
AR(1)	-2.775	-2.967	-3.277	-3.003	-2.895	-2.743
P-value	.0055	.0030	.0010	.0027	.0038	.0061
AR(2)	.6716	.7232	1.156	1.091	.7662	.5429
p-value	.5018	.4695	.2476	.2751	.4435	.5871
J-stat	20.02	18.33	22.83	24.79	24.07	21.34
p-value	.90	.90	.90	.90	.90	.90

The above results present the moderating effects of foreign owned Interest free banks on bank performance when it interacts with deposits, income, total assets and liquid assets. The lagged dependent variable is highly significant in all specifications, which indicates that current performance of Interest free banks depends on its past. The study first

moderating variable is foreign owned Interest free banks when it interact with total deposits ($FOWN_{ijt} * TD_{ijt}$) and the results revealed a significant negative influence on bank performance for specifications 1&2. The second moderating variable is the interaction between foreign owned banks and total income ($FOWN_{ijt} * TI_{ijt}$) shows no significant influence on bank performance of Interest free banks. The third moderating variable in which domestic owned banks when they interact with total assets ($FOWN_{ijt} * TA_{ijt}$) the results shows no significant influence on bank performance. The fourth moderating variable where liquid assets when interacts with domestic owned Interest free banks ($FOWN_{ijt} * LA_{ijt}$) also has insignificant influence on bank performance of Interest free banks.

The second independent variable of interest of the study is total deposits (TD_{ijt}) which is not significant for all of the specifications which means total deposits does not influence bank performance. The third independent variable total income (TI_{ijt}) is negatively significant for specification 2 only and insignificant for all other specifications. The bank specific variable Equity (EQT_{ijt}) does not show any statistically significant influence on bank performance for all of the specifications. The variable Capital adequacy ratio (CAR_{ijt}) is also not significant for all of the specifications. Liquid ($LASS_{ijt}$) of Interest free banks also has no significant influence on the financial soundness of Interest free banks and same is the case for total assets ($TASS_{ijt}$). The macroeconomic variable gross domestic product growth ($GDPG_{ijt}$) is highly significant for all of the specifications. The variable inflation (INF_{ijt}) is also highly significant for all of the specifications which means that when moderating variables is used the result for inflation changes. Dummy variable (D_{ijt}) shows insignificant influence for all of the specification. The dummy variable ($D2_{ijt}$) also doesn't show any significant influence in all specifications.

5. Conclusion and Limitations of the Study

The analysis covered 120 Interest free banks in 25 countries worldwide. We employed a difference GMM estimation approach to estimate the empirical models. For (ROA) we conclude that domestically owned banks show a significant positive influence on bank performance when interacting with total deposits, total income, and liquid assets, but a significant negative influence when interacting with total assets. Foreign-owned banks show a significant negative influence on bank performance when interacting with total deposits and liquid assets, but no significant influence when interacting with total income and total assets.

For (ROE) we conclude that the interaction of domestic-owned banks with total deposits and total income does not significantly influence bank performance (ROE), while the moderating effects of total assets and liquid assets have a negative impact. Foreign-owned banks have a negative influence on financial performance when interacting with total deposits, but no significant influence when interacting with total income, total assets, and liquid assets. We conclude that moderating variables play a significant role in affecting financial soundness and performance.

We have only considered the full-fledged Interest free banks. This can be further extended by considering the Islamic windows. A comparative analysis can be made among Islamic and traditional banks around the globe which can further reveals which banking system manage their resilience and profitability in a better way. Further comparison can also be made among different regions whereas this comparison can also be made towards traditional banks.

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Appendix A: List of Variables

Variables		Symbols	Definitions	Data Sources	
Dependent	Stability of Islamic Banks	Z-Score	Measured by the ratio of ROA plus EA to the standard deviation of ROA.	Refinitiv Eikon and Banks annual reports	
	Return on Assets	ROA	Return on assets measured by net income divided by total assets.	Refinitiv Eikon and Banks annual reports	
	Return on Equity	ROE	Return on equity measured by net income divided by total assets.	Refinitiv Eikon and Banks annual reports	
Independent	Domestic Ownership	DOWN	Proportion of equity held by the domestic owners	Refinitiv Eikon and Banks annual reports, websites	
	Foreign Ownership	FOWN	Proportion of equity held by the governments	Refinitiv Eikon and Banks annual reports	
	Government Ownership	GOWN	Proportion of equity held by the foreign owners	Refinitiv Eikon and Banks annual reports	
	Private Ownership	POWN	Percentage of shareholding by the private owners	Refinitiv Eikon and Banks annual reports	
	Non–Profit sharing investment accounts	Non-PSIA	The ratio of non-profit sharing investment accounts deposits to total assets.	Refinitiv Eikon and Banks annual reports	
	Profit sharing investment accounts	PSIA	The ratio of profit sharing investment accounts deposits to total assets.	Refinitiv Eikon and Banks annual reports	
	Income from non-traditional activities of IB's	Non-PLS_Income	Ratio of net non-profit and loss sharing income to total operating income	Refinitiv Eikon and Banks annual reports	
	Income from the traditional activities of IB's	PLS-Income	Ratio of net profit and loss sharing income to total operating income.	Refinitiv Eikon and Banks annual reports	
Banks Specific	Size of a bank	TA	Size of a bank measured by taking natural log of total assets.	Refinitiv Eikon and Banks annual reports	
	Equity	EQU	Total equity divided by the total assets.	Refinitiv Eikon and Banks annual reports	
	Liquid Assets	LA	Current assets divided by the total assets.	Refinitiv Eikon and Banks annual reports	
	Return on Assets	ROA	Return on assets measured by net income divide by total assets.	Refinitiv Eikon and Banks annual reports	
	Return on equity	ROE	Return on equity measured by net income divide by total assets.	Refinitiv Eikon and Banks annual reports	

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	Capital adequacy ratio	CAR	Measured by the bank's capital divided by the total risk weighted assets	Refinitiv Eikon and Banks annual reports	
Macroeconomic	Percentage change in Gross Domestic Product	GDPG	Percentage change in gross domestic product of the country.	World bank database	
	Inflation rate	INF	Annual average rate of inflation	World bank database	
Dummy	Financial Crisis	D1	Will take the value of 1when the year of observation is during crisis period (2007-2012) otherwise 0.	Self-observations	
	Deposit Insurance	D2	Will take the value of 1 if a country has deposit insurance otherwise 0.	International association of deposit insurance website	

Appendix C: List of Countries

S.No	Country	Banks	Total No of Banks (120)
1	Afghanistan	Islamic bank of Afghanistan	1
2	Bahrain	Albaraka Islamic Bank Ithmaar Bank Al Salam Bank Kuwait Finance House Bahrain Islamic Bank ABC Islamic Bank Bank Alkhair Ibdar Bank Al Salam Bank Khaleeji Commercial Bank Central Bank of Bahrain	11
3	Bangladesh	Islamic Bank Bangladesh Limited ICB Islamic Bank Limited Al Arafah Islami Bank Limited Social Islami Bank Limited EXIM Bank Limited First Security Islami Bank Limited Shahjalal Islami Bank Limited Union Bank Limited Standard Bank Limited Global Islami Bank Limited	10
4	Brunei Darussalam	Bank Islam Brunei Darussalam The Islamic bank of Brunei	4

		Perbadanan Tabung Amanah Islam Brunei Bank Usahawan	
5	Egypt	Faisal Islamic Bank of Egypt Al Baraka Bank Egypt Abu Dhabi Islamic Bank Egypt	3
6	Indonesia	Bank Syariah Mandiri Muamalat Bank Bank Indonesia Dubai Islamic Bank PT Bank Maybank Indocorp Hong Leong Islamic Bank CIMB Islamic Bank HSBC Amanah	11
7	Iran	Parsian Bank Sina Bank Bank Keshavarzi	3
8	Iraq	Elaf Islamic Bank Al Janoob Islamic Bank	2
9	Jordan	Jordan Islamic Bank Islamic International Arab Bank Safwa Islamic Bank	3
10	Kazakhstan	Al Hilal Bank Kazakhstan	1
11	Kuwait	Kuwait Finance House Boubyan Bank Warba Bank Kuwait International Bank	4
12	Lebanon	Al Baraka Bank Lebanon Banque du Liban	2
13	Libya	Islamic Bank of Libya	1
14	Malaysia	Maybank Islamic Bank Rakyat CIMB Islamic Bank RHB Islamic Bank Bank Islam Malaysia Public Islamic Bank AmBank Islamic Hong Leong Islamic Bank Affin Islamic Bank	15

		Bank Muamalat Malaysia HSBC Amanah Malaysia OCBC Al-Amin Bank Kuwait Finance House Malaysia Affin Islamic Bank Berhad Am Islamic Bank Berhad	
15	Morocco	Bank Assafa Umnia Bank Chaabi Bank Bank Al yousr Al Akhdar Bank BTI Bank (Bank Al Tamwil wal Inmaa)	6
16	Nigeria	Jaiz bank	1
17	Oman	Bank Nizwa Alizz Islamic Bank	2
18	Pakistan	Meezan Bank Dubai Islamic Bank BankIslami Pakistan Al Baraka Bank	4
19	Palestine	Palestine Islamic Bank Arab Islamic Bank Safa Bank	3
20	Qatar	Qatar Islamic Bank Masraf Al Rayan Qatar International Islamic Bank Barwa Bank	4
21	Saudi Arabia	Alinma Bank Bank AlBilad Bank AlJazira Al-Jazira Bank Al-Rajhi Banking and Investment Corporation National Commercial Bank Saudi British Bank	7
22	Sudan	United Capital Bank Al Jazeera Sudanese Jordanian Bank Al Salam Bank Bank of Khartoum Byblos Bank Africa Ltd	7

		Faisal Islamic Bank Tadamon Islamic Bank	
23	Turkey	Albaraka Turk Participation Bank Kuwait Turkish Participation Bank Ziraat Katilim Bankasi	3
24	United Arab Emirates	Dubai Islamic Bank Abu Dhabi Islamic Bank Emirates Islamic Bank Noor Bank Sharjah Islamic Bank Al Hilal Bank Ajman Bank Emirates Islamic Bank Mashreq Al Islami	9
25	United Kingdom	Al Rayan Bank Islamic Bank of Britain Qatar Islamic Bank UK	3
Total Countries = 25		120	