Risk Exposure of Islamic Financial Institutions: Evidence from Gulf Co-operation Council Countries

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STATEMENT OF ORIGINALITY

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DEDICATION

This dissertation is dedicated to my most beloved parents “Ghalia Ghanem” (have Allah’s Mercy on her souls and grant her eternal happiness and peace in Paradise) and “Mobarak Naser”, without whose sole contribution I could not achieve anything in my life.

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Abstract

This study examines the determinants of major risks faced by both Islamic and conventional banks, and the relationship between different risks and bank performance in the context of Gulf Cooperation Council (GCC) countries. The data used in the study has been collected from the annual reports of banks and Gulf database from 2006-2010. The GCC includes six Arab states: the Kingdom of Saudi Arabia, Kingdom of Bahrain, Kuwait, Qatar, United Arab Emirates and Oman. The study covered 63 banks from these countries. Those banks can be divided into two types: 47 conventional banks and 16 Islamic banks. Foreign banks have been excluded from the list due to their different style of operation and management. This study uses multiple regression models for investigating the factors driving the bank's risk exposure and financial performance. It found no significant difference between Islamic banks and conventional banks in relation to credit risk exposure but both the liquidity risk and the profit-rate risk are significantly higher for the Islamic banks compared to the conventional banks in the GCC region. In the case of Islamic banks, credit risk was found to have a significant positive correlation with leverage, but a negative correlation with bank size. For conventional banks, credit risk is positively correlation with loan to deposit ratio but negatively correlation with management efficiency. Liquidity risk was found to be positively correlation with the degree of financial leverage in the case of Islamic banks, whereas it was found to be positively correlation with fund cost in the case of conventional banks. This study has not been able to identify any significant determinants for the profit-rate (interest-rate) risk in case of Islamic banks. For conventional banks, it has been found that growth of total assets and size negatively affects the interest-rate risk. Further, this study found weak but significant negative relationship between credit risk, liquidity risk and

performance in conventional banks whereas there was no significant relationship between performance and risks in Islamic banks.

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