COMPARATIVE STUDY ON PRODUCTIVITY GROWTH AND EFFICIENCY CHANGE BETWEEN ISLAMIC BANKS AND CONVENTIONAL BANKS IN MALAYSIA

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This dissertation submitted in partial fulfilment of the requirement for the degree of
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ABSTRACT

This study investigates the changes in the productivity and efficiency of Islamic banks and Conventional banks in Malaysia from the impact of 2007 US sub-prime crisis. It analyses the technological changes (TC) and technical efficiency changes (TEC) of the Islamic banks and Conventional banks using a nonparametric Data Envelopment Analysis (DEA) and Malmquist Productivity Index (MPI). TEC is again decomposed into pure efficiency change (PEC) and scale efficiency change (SEC). This study adopts the intermediation approach of banking services, employing inputs such as interest and non-interest expenses to produce outputs such as net interest and non-interest incomes.

It was found that the mean Total Factor Productivity (TFP) for the whole industry recorded an increase of 4.0%. Both TC and TEC are found to be the important source of productivity growth to Malaysia's banking industry to the overall TFP growth. This increase was attributed by the technological advances and the technical efficiency change, showing that technology and innovation as well as the scale size optimization in the banks is on the upward trend.

Islamic banks (9.0%) achieved higher growth in productivity compared with Conventional banks (3.0%). Islamic banks records higher results in TEC (5.0%), TC (4.0%) and SEC (5.0%). Conventional banks only achieve TEC (1.0%), TC (2.0%) and SEC (1.0%). Both Islamic and Conventional banks PEC unchanged from 2004 to 2010. BMMB recorded the highest growth of TFP 13.0%, TEC 7.0%, SEC 7.0% and TC 6.0%. Thus, Islamic banks are more productive and efficient compared with Conventional banks. Moreover, this study finds that Alliance Bank Malaysia Berhad exhibited lower productivity and efficiency levels with TFP -14.0%, TEC -7.0% and TC -6.0%. Affin Bank and Hong Leong Bank Berhad also recorded negative result in TEC where both show -1.0% regressions.

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