Factors Affecting Islamic Bank Financial Performance

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Abstract

Purpose – The study aims at evaluating the factors affecting financial performance in Islamic banks.

Methodology - The quantitative method is applied in this study with panel data analysis as analysis tool. This study measures the performance of Islamic Banks (IBs) in Türkiye and Indonesia. In total, there are 5 and 11 Islamic banks in Türkiye and Indonesia respectively used in this study, resulting 109 samples to analyze.

Findings - The results reveal that bank size, capital ratio, operating expense ratio and inflation are found to be significant on Return on Average Assets (ROAA) positively. However, bank age and loan ratio do not have significant effect on ROAA. It is important to evaluate these factors to improve financial performance of Islamic bank in both countries as big Muslim population.

Keywords: *Indonesia, Islamic bank, performance, ROAA, Türkiye.* .

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1. INTRODUCTION

After emergence of Islamic finance practice in the 1960s, constantly this industry shows incredible growth along with offering various innovative and unique financial instrument and business model. The total assets of Islamic finance reached USD 3.6 trillion in 2021, expanding by 7.8% year over year, and are expected to rise by 8% in 2022, according to Dinar Standard's State of the Global Islamic Economy Report 2022. After a difficult year during the height of the epidemic, this industry has recovered in the first half of 2021. This report also revealed that this industry is also expected to grow with assets estimated to reach USD 4.9 trillion in 2025 after new normal has been implemented in many countries.

Among Islamic finance institutions, Islamic banking is known as fast-growing industry. Although pandemic hit many sectors, Islamic banking continued to rise in 2020, registering year on year growth of 14% to USD 2.3 trillion in Islamic finance global assets. At the same time, the share of Islamic banking was 70% in 2020, making Islamic banking as the biggest contributor to global Islamic finance assets (Refinitive, 2021). While Islamic banking has shown progressive development, Islamic banking in most countries has recorded low market share of the total domestic banking. Only Iran, Sudan, Saudi Arabia, and Brunei still maintains a high market share of Islamic banking assets above 60% (IFSB, 2021).

Islamic banking industry needs to gain high market share to have more significant contribution on socio-economic welfare. According to Ismal (2013), a small Islamic banking market limits the operations of Islamic banks, Islamic financial markets, and Islamic banking's economic impact. Islamic banking should therefore be prepared to compete with traditional banking by enhancing its performance in order to gain a larger market share. Customers or investors are interested in using Islamic banks' goods and services if they continue to perform sustainably. As a result, the Islamic banking would expand its operation and business and provide large contribution to the economy of country.

Achieving good and sustainable performance is very important issue for banking sector. Islamic banks (IBs) must formulate strategies to improve the performance as a means to generate optimal benefit. In addition, IBs need to maintain excellent performance to make bank resilient and competitive. The study regarding factors that affect bank performance, therefore, become essential. The studies on Islamic bank (IB) performance have been conducted by previous researchers such as Al-Naseer Mohammed and Joriah Muhammed (2017); Platonova, et al. (2018); Ajili and Bouri (2018); Al-Malkawi and Pillai (2018); Khanifah, et al. (2020).

Most previous studies have examined variables from bank's internal data such as bank size, leverage, capital ratio, loan ratio, corporate social responsibility, corporate governance etc. as independent variables towards IB performance. Not many of them have applied external variables as factors affecting IB performance as stated by Furqani and Mulyany (2009), revealing that the studies concerning the relationship between IB and macroeconomics variables are still rare. It is, thus, important to analyze factors influencing IB performance using both internal and external variables.

2. LITERATURE REVIEW

Business sectors, including banking, usually evaluate the business activities to see the performance of the company throughout the year. Through this evaluation process, the industry may determine new business target and strategies for the coming year. In banking sector, the performance assessment is necessary as this sector is intermediary institution that must be responsible for the

management of funds coming from third parties as investors. The performance measurement, therefore, is very important in banking sector. Performance measurement, according to Moullin (2002), demonstrates how well a company is run and what results it produces for clients and other stakeholders.

2.1 Performance Measurement

The performance measurement tool might be different among enterprises, it is dependent on enterprises' needs, policies, and strategies. In general, the performance measurement method is divided into two categories i.e., classical method and modern method (Bouheni et al., 2016). The classical method is method that measure the performance of company based on earning (profit). In other terms, the classical method is tool to measure the performance of company using financial performance such as ratio analysis, income statement, market value added etc. At the same time, the modern method is method to measure company performance using both financial aspects and non-financial aspects such as innovation, customer satisfaction and employee's motivation.

Financial indicators are used in this study as a traditional way to gauge the performance of Islamic banks in Indonesia and Turkey. Financial indicators are used in financial performance to show the firm's economic success. Additionally, this study uses ratio analysis to analyze the financial performance of Islamic banks in these two nations. Calculating and comparing ratios based on data from a company's financial report is known as ratio analysis. Inferences regarding the financial health of the company can be drawn from the level and past patterns of these ratios. A company's finances and activities can be explained by a variety of categories in financial ratio analysis. (Bouheni et al., 2016; Gupta et al., 2011).

Return on assets (ROA) is a financial measure that is frequently used to evaluate a company's performance. The efficiency with which a business generates profit from its assets is measured by its return on assets (ROA). Managers, analysts, and investors use ROA to assess the financial health of a business. This metric contrasts the profits during a given time period with the asset value of the business. This indicator represents the overall profitability of the banking industry. Since the ROA assesses how well a bank uses its financial resources, it is thought to be the most accurate indicator of banking activity (Birken, 2021). In actuality, a company's asset value varies over time as a result of shifting asset costs or market conditions and demand. The average total assets for a period can therefore be calculated more accurately than the total assets for a single period. The total asset at the start and end of the year is averaged to determine the average asset. Therefore, it is much better to use return on average assets (ROAA) in this study. Generally speaking, a company's ability to generate profits is correlated with its ROAA.

There are some previous researchers conducting studies regarding performance of bank such as Al-Naseer Mohammed and Joriah Muhammed (2017); Alsartawi (2019); Al-Kayed et al. (2014); Athanasoglou et al. (2008); Al-Tamimi (2010); Al-Malkawi and Pillai (2018); Wasiuzzaman and Gunasegavan (2013); Khanifah et al. (2020). The research examined the variables that affect return on assets (ROA), a measure of bank profitability. There are not many studies on the elements impacting IBs' performance using bank internal and external variables, claim Al-Naseer Mohammed and Joriah Muhammed (2017). In order to close the existing gap, this study incorporates both internal and external variables related to banks in order to investigate their influence on IB performance. Following a review of earlier research, this study considers inflation as an external variable and uses bank size, loan ratio, capital ratio, operating expense ratio, and bank age as independent and internal variables.

2.2 Hypothesis Development

In this study, there are some hypotheses proposed after reviewing literature and previous studies. The hypotheses proposed are as follows:

3.3.1. The influence of bank size on ROAA (H1)
According to earlier research, bank size and ROA are related. According to Alsartawi's (2019) research, bank size has a favorable and significant impact on ROA. A stand-in for bank size is the log of total assets. Additionally, Haron (1996) claimed that because big banks are thought to benefit from economies of scale, they can manufacture their goods and services more cheaply and effectively than small banks. Large banks will consequently make more money. Thus, the following is the hypothesis on the relationship between bank size and ROAA:

H1. Bank size has positive impact on ROAA

3.3.2. The influence of loan ratio on ROAA (H2)
Platonova et al. (2018) investigated the connection between ROA and loan ratio. The study's findings demonstrated that the loan ratio significantly improves ROA. Total loans divided by total assets yields the loan ratio. One of the primary capital sources used by Islamic banks to make money is the loan. Therefore, it is anticipated that the lending ratio will positively affect ROA for Islamic banks in Indonesia and Turkey. Thus, the following is the second hypothesis for this research:

H2. Loan ratio has positive impact on ROAA

3.3.3. The influence of capital ratio on ROAA (H3)
The capital ratio and ROA are related, according to earlier research. For instance, the study of Al-Kayed et al. (2014) showed that ROA and the capital ratio had a positive association. Total equity divided by total assets yields the capital ratio. By lowering the anticipated cost of bankruptcy, the increase in capital might boost expected profitability. Furthermore, banks that have a high capital ratio can lower the cost of outside funding. Consequently, the banks might become more profitable (Kosmidou, 2008). Thus, the following is the third hypothesis for this research:

H3. Capital ratio has positive impact on ROAA

3.3.4. The influence of operating expense ratio on ROAA (H4)
According to several empirical research, one of the key factors influencing bank profitability is operating expense. Athanasoglou et al. (2008) investigated the connection between ROA and the operating expense ratio. By dividing total operating expenses by total assets, one can determine the operating expense ratio. The study's findings demonstrated that operating expenses have a detrimental impact on ROA. In order to increase bank profitability and efficiency, operating expenses must be managed effectively. Consequently, it is anticipated that operational expenses will have a negative impact on ROA for Islamic banks in Indonesia and Turkey. Thus, the following is the fourth hypothesis for this research:

H4. Operating expense ratio has negative impact on ROAA

3.3.5. *The influence of bank age on ROAA (H5)*

Al-Malkawi and Pillai (2018) investigated the connection between bank profitability and age. The study's findings demonstrated that bank age significantly increases bank profitability. Nonetheless, a study by Majumdar (1997) revealed that older businesses are less profitable and more productive. Also, Alsartawi (2019) revealed that bank age has negative impact on ROA. Therefore, research on the connection between bank age and profitability has been controversial up to this point. As of right now, bank age and profitability have both positive and negative relationships. Therefore, the following hypothesis is used in this study to examine the relationship between bank age and ROA for Islamic banking in Turkey and Indonesia:

H5. The bank age has impact on ROAA

3.3.6. *The influence of inflation on ROAA (H6)*

The impact of inflation, one of the macroeconomic variables, on bank profitability will also be investigated in this study. According to Wasiuzzaman and Gunasegava's (2013) research, ROA is positively impacted by inflation. The annual percentage change in the consumer price index (PCI) is used to calculate inflation. Costs and income may increase as a result of the increased inflation. The impact of inflation will boost bank profits if the bank can effectively control costs. Thus, the following is the study's hypothesis:

H6. The inflation has positive impact on ROAA

3. METHODOLOGY

This study aims to examine the financial performance of Indonesian and Turkish IBs. The research for this project is being conducted using a quantitative technique. A research strategy that prioritizes quantification in data gathering and analysis is known as the quantitative approach (Bryman, 2012).

3.1 Data and sample

This study selects the number of IBs in Turkey and Indonesia as sample. In total, Turkey has six IBs as listed in Türkiye Katılım Bankaları Birliği (TKBB). However, this study uses five IBs as one IB is new entrant into Islamic banking industry in Turkey. At the same time, Indonesia has various Islamic bank types available. The type of Islamic bank used in this study is Islamic commercial bank (ICB) because this type operates independently and possesses large bank capital. The total ICB in Indonesia is 14 as listed in Otoritas Jasa Keuangan (OJK). However, this study uses 11 ICB as sample because three ICB are new entrant into industry and do not provide enough data to be investigated.

In the analysis of factors influencing bank performance, this study uses internal data collected from annual reports of IBs available in each bank's website. In addition to that, this study also uses the external data obtained from Türkiye Cümhuriyet Merkez Bankası (TCMB) and Bank Indonesia (BI) as central banks in both countries. The type of data employed in this study is panel data.

3.2 3.2. Panel data analysis

This study examines the factors affecting IB financial performance using variables commonly used in the conventional bank as well. Panel data analysis is used in this work to perform this analysis. Combining cross-sectional and time-series data is known as panel data analysis (Andreb et al., 2013). A large number of data points are typically provided using panel data analysis, which raises the degree of freedom and lowers the collinearity between explanatory factors. As a result, it makes econometric estimates more efficient. More crucially, panel data enables researchers to examine some significant economic issues that are not possible to answer with time-series or cross-sectional data (Hsiao, 2003). The following table lists the variables that were used in this study:

Table 1. The definition of dependent and independent variables

Variables	Definition
Dependent variable	
Return on average assets (ROAA)	Net Income/average total assets
Independent variables	
Internal variables	
Bank size (BS)	The Natural logarithm of total assets
Loan ratio (LR)	Total loans/average total assets
Capital ratio (CR)	Total equity/average total assets
Operating expense ratio (OER)	Total operating expense/average total assets
Bank age (BA)	The difference between the establishing date of Islamic bank and the report date
External variable	
Inflation (INF)	Per annum percentage change in the consumer price index (PCI)

After determining and defining the variables, the specification of the model can be formed. The following is the specification of panel data regression model for this study:

$$ROA_{it} = \beta_0 + \beta_1 BS + \beta_2 LR + \beta_3 CR + \beta_4 OER + \beta_5 BA + \beta_6 INF + \mu_{it}$$

Explanation:

ROA	= Return on assets
i	= Cross-sectional unit
t	= Time-series
β_0 to β_6	= Intercept
BS	= Bank size
LR	= Loan ratio
CR	= Capital ratio
OER	= Operating expense ratio
BA	= Bank age
INF	= Inflation
μ_{it}	= Error term

In this study, unbalanced panel data analysis will be employed due to data availability. The observation year used for this study is shown in the table below:

Table 2. The number of observations

	No.	Bank	Observation Year	Total Observation
Turkey	1.	Albaraka Türk Participation Bank	2014-2020	7
	2.	Kuveyt Türk Participation Bank	2014-2020	7
	3.	Türkiye Finans Participation Bank	2014-2020	7
	4.	Ziraat Participation Bank	2015-2020	6
	5.	Vakıf Participation Bank	2016-2020	5
Indonesia	6.	Muamalat Bank	2014-2020	7
	7.	Victoria Islamic Bank	2014-2020	7
	8.	BRI Islamic Bank	2014-2020	7
	9.	BJB Islamic Bank	2014-2020	7
	10.	BNI Islamic Bank	2014-2020	7
	11.	Mandiri Islamic Bank	2014-2020	7
	12.	Mega Islamic Bank	2014-2020	7
	13.	Panin Dubai Islamic Bank	2014-2020	7
	14.	Bukopin Islamic Bank	2014-2020	7
	15.	BCA Islamic Bank	2014-2020	7
	16.	BTPN Islamic Bank	2014-2020	7
		Total		**109**

4. RESULTS AND DISCUSSION

4.1 Descriptive statistics

Table 3 shows the results of descriptive statistics computed by EViews 12. The total observation for panel data analysis in Turkey is 32 while in Indonesia it consists of 77 observations. So, in total this study has 109 observations for period between 2014-2020. It also indicates that more IBs operates in Indonesia than in Turkey. Nevertheless, Turkey disclosed bigger IBs' average assets in 2020 than Indonesia at 38,160 million of Turkish Lira (TL) or 4,711 million of USD (1 USD = 8.1 TL in 2020) and 23,104 billion of IDR or 1,593 million of USD (1 USD = 14,500 IDR in 2020) respectively.

The mean of ROAA for IBs in Turkey during 2014-2020 was 1.03%. The minimum ROAA was owned by Ziraat Participation Bank in 2015 at -0.55%. This bank had negative ROAA because the bank was newly established in 2015. Meantime, the mean of ROAA for IBs in Indonesia was at 0.64%, lower than in Turkey. The minimum of ROAA was at -11.14, reached by Panin Dubai Islamic bank in 2017. This bank had the negative performance as there was tough situation in the bank management, resulting in misappropriation of funds (Salih, 2019). In general, ROAA of IBs in both countries is under 2%.

The mean of loan ratio of IBs in Turkey and Indonesia was between 70% and 80%. Also, the capital ratio of IBs in these countries was between 10% and 20%. In the terms of the average operating expense ratio, the ratio difference between two countries was only 2,45%. So, there were no great differences in these matters, indicating that IBs were nearly in the same performance.

Until 2020, the average of bank age for IBs in Turkey was 17 years old. Meanwhile, the average age of IBs in Indonesia was 12 years old. IB operation in Turkey has started earlier than in Indonesia, pioneered by Albaraka Participation Bank established in 1985. In the terms of

inflation, from 2014 to 2020, the average annual inflation in Turkey was 11.58%. Based on data from world bank (World Bank, 2021), the inflation in Turkey was above 10% since 2017. Meanwhile, from 2014 to 2020 the mean of inflation in Indonesia is 3.70%. The inflation rates every year in Indonesia is under 5%. The big difference of annual inflation rate in Turkey and Indonesia was caused by different political economy and policies conducted by central bank of the country

Table 3. Descriptive statistics

	Variables	Observations	Mean	Minimum	Maximum	Stand. Dev.
Turkey	ROAA (%)	32	1.03	-0.55	1.90	0.51
	BS (in Millions of TL)	32	38,160.56	2,177	128,365	25,668
	LR (%)	32	77.61	57.35	109.66	13.46
	CR (%)	32	10.69	6.23	31.62	5.68
	OER (%)	32	8.05	4.64	11.85	1.58
	BA (Year)	32	16.88	1	35	12.42
	INF (%)	32	11.58	7.67	16.33	3.30
Indonesia	ROAA (%)	77	0.64	-11.14	10.21	2.66
	BS (Billions of IDR)	77	23,104.05	1,382	119,600	27,167.82
	LR (%)	77	72.81	41.01	124.63	10.80
	CR (%)	77	15.33	3.15	41.10	8.18
	OER (%)	77	10.49	4.93	45.90	6.21
	BA (Year)	77	11.72	4	28	6.01
	INF (%)	77	3.70	1.68	8.36	2.00

4.2 Panel Data Regression results

This study selects random effects as the best panel regression model because based on p-value of the Hausman test, the null hypothesis is accepted as p-value is higher than 5% as shown in the table 5, signifying that intercept differences between individuals can be accommodated by the error terms of each unit. Random effects use Generalized Least Square (GLS) estimator in its analysis (Greene, 2003). Consequently, to investigate the econometric problem, only multicollinearity test is conducted while heteroscedasticity test is not needed (Gujarati, 2004). As can be seen in table 4, all variables have VIF value under 10. Garson (2016) emphasizes that the maximum VIF for multicollinearity is value of 5. So, there is no multicollinearity statistically in this study.

Table 4. Variance Inflation Factors (VIF)

Variables	VIF
BS	2.1339
LR	1.4882
CR	1.9087
OER	1.3946
BA	2.2607
INF	1.3261

After examining validity of data, the next step is to see the significance of independent variables towards dependent variable. Based on results that can be seen in Table 5, four of six variables

are found to be significant at 0.01. Also, the f-statistic is significant at 001, meaning that the equation proposed is reliable.

Table 5. Panel data regression analysis with random effects

Variables	Coefficient	t-Statistic
C	-18.2151	-5.5720***
BS	1.0071	5.4588***
LR	-0.0264	-1.5978
CR	0.2086	8.4225***
OER	0.1028	3.1110***
BA	-0.0148	-0.5737
INF	0.0870	2.4896***
Adj. R^2	: 0.4871	
F-Statistic	: 18.0935***	
Hausman	: 0.3313	
Total panel (unbalanced) observations	: 109	

Dependent variable: ROAA, *** P < 0.01

The study's initial premise is that ROA is positively impacted by bank size. According to the econometric results of the hypothesis test, the study's H1 is accepted if the p-value is less than 0.05. This result validates some earlier research by Bukair and Rahman (2015), Ajili and Bouri (2018), and Alsartawi (2019). The earlier research also shows that bank size and ROA are positively correlated. According to Haron (1996), big banks can manufacture their goods or services more cheaply and effectively than small banks because they are thought to benefit from economies of scale. So, the finding indicates that larger IBs are able to reduce the costs and risk in the financial market. As a result, larger IBs are more efficient than small IBs. The efficient IBs have opportunity to earn higher profit. Finally, the bank size has positive impact on financial performance of IB.

Due to the p-value over 0.05, the second hypothesis is not accepted. However, the outcome indicates that the loan ratio has a negative impact on ROAA. Some earlier research, like Hidayat and Abduh (2012), Al-Harbi (2019), Simpson and Kohers (2002), and Ali and Khattak (2020), supports the negligible effect of loan ratio on ROAA. The second hypothesis's insignificant outcome suggests that the loan ratio has no bearing on IBs' financial success. The adverse effect suggests that a larger loan ratio has a detrimental impact on bank earnings.

One of causes that makes loan ratio insignificant on ROAA is inappropriate loan management conducted by some IBs in Indonesia. For example, in 2016-2017 Panin Dubai Islamic bank experienced loss because of inappropriate loan management. The bank disburse loan with big amount to wrong company. The company made fictitious credit so that bank cannot collect given debt. In 2018, the company makes bank loss at IDR 141 billion (Salih, 2019). In addition to that, Muamalat Bank, as the first IB in Indonesia, recently has the high non-performing finance ratio. Since 2015, this bank implemented inappropriate loan management or wrong business strategy. As a result, in 2019, the profit bank decreased by 94,1%. So, this condition may cause loan ratio insignificant on ROA for IBs in Indonesia (Saragih, 2019).

According to a number of earlier research, including Al-Kayed et al. (2014), Athanasoglou et al. (2008), Zarrouk et al. (2016), Kosmidou (2008), and Al-Harbi (2019), the third hypothesis is accepted. These earlier studies demonstrated that the capital ratio considerably improves ROA.

This hypothesis's outcome shows that the demand for outside investment decreases with a higher capital ratio. As a result, the bank can lower the price of outside funding. Additionally, a bank with adequate capital can pursue a wide range of commercial options. Lastly, there is a chance for the bank to make more money (Athanasoglou et al., 2008; Zarrouk et al. 2015).

The fourth hypothesis of this study is that the operating expense ratio has negative impact on ROA. Based on the test result statistically, there is positive relationship between operating expense ratio and ROAA significantly at 0.01, meaning that the hypothesis is not supported. This result of this study is consistent with previous studies such as Platonova et al. (2018); Vong and Chan (n.d.); Naceur (2003). This result may be caused by different bank characteristic and condition. As known previously, the structure funding of IBs in Turkey and Indonesia is dominated by participation account. This kind of account is more expensive than saving account for Islamic bank because the bank should give return to customer in certain period. So, there is high operating expense in Islamic bank. Furthermore, if the bank manages participation fund so well, the bank also has opportunity to earn profit. So, it is assumed that there is positive relationship between operating expense ratio and ROAA for Islamic banking in Turkey and Indonesia.

In Islam, there are *fiqh* principles about the relationship between expense, risk and profit. They are *al-ghunmu bil ghurmi* (profit goes with loss) and *al-kharaj bi al-dhaman* (Rewards goes with expense) (Ayub, 2007). So, it is normal if Islamic banks has positive relationship between expense and profit because expense, risk and profit is always together.

The study's fifth hypothesis is that ROAA is impacted by bank age. As previously mentioned, there are differing opinions about the connection between ROA and bank age. Prior research has indicated that bank age has a beneficial effect on ROA in some cases and a negative influence in others. Since the p-value is greater than 0.05, H5 is statistically rejected based on the test results. According to Zouari and Taktak (2014) and Ajili and Bouri (2018), the fifth hypothesis is rejected. These earlier investigations demonstrated that bank age and ROA are unrelated. Because older banks can be less efficient than young ones in terms of greater costs, older assets, less spending on R&D, deteriorated governance rules, and huge boards, bank age may have a negative impact on ROAA (Al-Malkawi & Pillai, 2018). For instance, Muamalat Bank, the original IB, has experienced financial difficulties since 2015. It causes this bank's profit to decline. Therefore, it has been determined that in Turkey and Indonesia, there is a negative correlation between ROAA and IB age.

Recently, the older bank and the new bank are competing to attract customer by improving their product and service quality. In this time, banking sector has developed digital banking in many countries including Turkey and Indonesia to provide fast and easy services to customers. So, the older bank is not guaranteed to have better performance, the success of the banks is depended on the creativity and innovation they have.

The study's final premise is that ROA is positively impacted by inflation. In Turkey and Indonesia, there is a positive correlation between ROAA and inflation, according to the test results. The p-value for this hypothesis is less than 0.05. The hypothesis's acceptance is consistent with some earlier research, including Izhar and Asutay (2007), Al-Naseer Mohammed and Joriah Muhammed (2017), and Wasiuzzaman and Gunasegavan (2013). These previous studies show that the inflation has positive impact significantly on ROA. The financial industry is encouraged to predict changes in inflation due to the significant fluctuations in the inflation rate. For instance, according to data from the World Bank (2021) and TCMB (2021), Turkey's inflation rate has been more than 10% since 2017. The bank can correctly modify the profit rate to raise revenues higher than costs if the management of the bank anticipates the rate of inflation. Therefore, profitability

should benefit from inflation (Zarrouk et al., 2016). As a result, ROAA and inflation have a positive association.

5. CONCLUSION

Having good financial performance is very important in banking sector as it demonstrates the quality of the bank such as serving and empowering society. Assessing IB performance based on conventional approach is not enough as it does not evaluate other important performance indicators in IB. This study analyses performance of IB using Islamic and conventional approach to have assessment more comprehensive. IBs in Turkey and Indonesia are used as sample for performance analysis as IBs in these countries show similar characteristic.

This study uses ROAA as performance indicator in IB. ROAA is included in classical method as it measures the performance of company based on earning. Further analysis is to see the factors affecting ROAA in IBs in Turkey and Indonesia using panel data analysis. Bank size, capital ratio, operating expense ratio, and inflation are found to have statistically significant impact on ROAA while loan ratio and bank age do not show significant effect on ROAA. Islamic bank with big asset size, capital ratio and operating expense ratio have more chance in generating profit. Meanwhile, in this study loan ratio is not found to be significant as some Islamic banks suffer high non-performing loan and mismanage in financing business sector. However, if the bank manage financing properly, the increase in financing might optimize to earn profit. Also, this study reveals that bank age does not determine to have better performance, meaning that older and experienced IB might have lower profit than newcomers. In this digital era, the innovation, creativity, and big impact on society are crucial to win the competition.

It is anticipated that this work will theoretically increase the body of knowledge on financial performance analysis in Islamic banks. It is anticipated that practitioners and associated parties will use this study as a basis and point of reference to improve Islamic banks' financial performance in order to gain market share and have a significant social impact.

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