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A Comparative Analysis of Financial Performance Between Islami Shariah and Non-Shariah Commercial Banks in Bangladesh

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Abstract

This research examines the financial performance of Islami Shariah and non-Shariah commercial banks in Bangladesh from 2015 to 2024, employing the CAMELS rating framework to assess efficiency, stability, and contributions to economic growth. The study utilizes secondary data derived from the annual financial statements of three Shariah banks (First Security Islami Bank Ltd., Al Arafah Islami Bank Ltd., Export Import Bank Limited) and three non-Shariah banks (BRAC Bank Limited, Bank Asia Limited, Arab Bangladesh Bank Ltd.), which were selected through simple random sampling from a total of 62 operational banks. The primary findings suggest that Shariah banks typically demonstrate superior capital adequacy, asset quality, and management efficiency, characterized by lower non-performing loans and operating expense ratios, indicative of effective risk management and cost control. In contrast, non-Shariah banks exhibit a stronger return on assets, while Shariah banks reveal significant growth in return on equity. Liquidity levels are generally sufficient across most institutions; however, certain Shariah banks are experiencing declining trends that may pose potential risks. Sensitivity analysis indicates that Shariah banks are more exposed to interest rate fluctuations due to their profit-loss sharing models. The composite CAMELS ratings categorize all banks as satisfactory overall, although some non-Shariah entities, such as BRAC Bank, receive occasional fair ratings. These findings highlight the operational strengths and weaknesses within Bangladesh's dual banking system, providing valuable insights for policymakers aimed at improving regulations for sustainable development, financial inclusion and sector balance.

Keywords: Financial Performance, Shariah Banks, Non-Shariah Banks, CAMELS Rating, Efficiency, Stability, Economic Growth, Bangladesh, Risk Management, Profit-Loss Sharing, Financial Inclusion.

Introduction

The banking sector in Bangladesh plays a vital role in promoting economic development, facilitating savings, and supporting investment. Within this sector, two distinct banking systems—Islami Shariah-compliant banks and conventional non-Shariah commercial banks—operate simultaneously, catering to diverse customer requirements. Since the establishment of Islami Bank Bangladesh Limited in 1983, Islamic banking has experienced considerable expansion, driven by the majority Muslim population in the nation and the rising demand for Shariah-compliant financial services. Unlike conventional banks that depend on interest-based mechanisms, Islamic banks adhere to principles of profit and loss sharing, risk-sharing agreements, and asset-backed financing, ensuring compliance with Islamic law. On the other hand, non-Shariah commercial banks hold a dominant position in terms of total assets, customer demographics, and variety of services. A comparative analysis of their financial performance is essential to analyze their efficiency, stability, and contributions to the economy.

This examination not only highlights their operational strengths and weaknesses but also provides valuable insights for policymakers, regulators, and investors. Given the evolving financial landscape in Bangladesh, understanding the relative performance of Shariah and non-Shariah banks is crucial for promoting sustainable growth, improving financial inclusion, and sustaining competitive balance within the sector.

Objective of the Study

The objective of this research is to assess and compare the financial performance of selected Islami Shariah-based and non-Shariah commercial banks in Bangladesh by means of appropriate financial techniques.

Rationale of the Study

The assessment of financial performance between Islami Shariah and non-Shariah commercial banks in Bangladesh is crucial for comprehending the complexities of the nation's dual banking system. As the economy of Bangladesh expands, consumers are increasingly pursuing banking alternatives that align with their financial requirements and ethical values. Islami Shariah banks function according to Islamic principles that forbid interest, advocate for profit-and-loss sharing, and promote ethical investments, whereas non-Shariah banks adhere to traditional banking practices. Analyzing their financial performance—encompassing profitability, liquidity, and asset quality—offers vital insights into their operational effectiveness, risk management, and market competitiveness. This research aids regulators, investors, and policymakers in refining banking strategies, improving financial inclusion, and bolstering the overall stability of Bangladesh's financial sector. In conclusion, the study contributes to the wider dialogue on how Islamic finance can coexist with and compete against conventional banking, thereby fostering a more diverse and resilient banking landscape.

Research Gap

The research conducted on the financial performance of Islamic Shariah and non-Shariah commercial banks in Bangladesh has primarily focused on growth trends, market share, and operational aspects. However, it falls short of providing a comprehensive comparative analysis of essential productivity metrics such as efficiency, profitability, and risk management. Significant topics, including the implications of the Shariah-based risk-sharing model and the impact of transitioning conventional banks to Islamic banking, have not been sufficiently examined. The recent challenges encountered by Islamic banks, such as liquidity constraints and governance issues, further underscore the necessity for updated empirical research to evaluate their financial stability in comparison to conventional banks in a post-crisis environment. This study aims to rectify these gaps by offering a timely, empirical comparison of the financial performance of both banking systems, exploring various performance indicators and the influence of governance and regulatory disparities. Such findings will aid policymakers, investors, and bank managers in effectively navigating the dual banking landscape of Bangladesh.

Literature Review

Between 2009 and 2013, Islam and Ashrafuzzaman (2016) ^[1] discovered that both Islamic and conventional banks in

Bangladesh exhibited comparable outcomes in terms of capital adequacy, management quality, and earnings as assessed by CAMEL components, with Islamic banks being uniquely characterized by their asset quality strategies. Beck, Demirgüç-Kunt, and Merrouche (2013) ^[2] performed a worldwide analysis that indicated Islamic banks are generally less cost-efficient; however, they outperform conventional banks in asset quality, capitalization, and intermediation, particularly during crises, which supports enhanced stability. Abedifar, Molyneux, and Tarazi (2013) ^[3] noted that smaller Islamic banks across 24 nations encounter lower credit risk, demonstrate greater resilience against insolvency, and practice conservative risk management, as shown by minimal rent extraction. Overall, these findings suggest that while Islamic and conventional banks exhibit similar performance in most aspects, Islamic banks provide enhanced stability and prudent asset management, particularly in unstable conditions.

Johanes, Izzeldin, and Pappas (2014) ^[4] analyzed Islamic and conventional banks from 2004 to 2009 and found that Islamic banks showed comparable gross efficiency and surpassed conventional banks in net efficiency, although the results were influenced by institutional context and bank size. Olson and Zoubi (2008) ^[5] determined that accounting ratios could effectively differentiate between Islamic and conventional banks in the GCC, with Islamic banks generally possessing stronger capitalization and unique profitability patterns—characteristics influenced by their operational principles. Bourkhis and Nabi (2013) ^[6] investigated the performance during the 2007–2008 financial crisis, revealing that failure rates were similar for both types of banks. Despite the differences in their business models, Islamic banks did not exhibit increased systemic risk or a higher likelihood of failure, demonstrating soundness and resilience comparable to conventional institutions during economic distress.

Ben Khediri, Charfeddine, and Youssef (2015) ^[7] discovered that Islamic banks typically exhibit lower revenue volatility and risk levels compared to conventional banks; however, their risk is influenced by economic conditions. Arif and Alam (2023) ^[8] conducted an analysis of Islamic banks in Bangladesh from 2009 to 2019 utilizing Z-score models, revealing that strong capital adequacy, earnings, and management efficiency contribute to stability, while non-performing investments and bank size present complex effects. Nobi *et al.* (2024) ^[9] compared efficiency from 2014 to 2020 and determined that conventional and mixed banks are more efficient than Islamic banks, primarily due to the difficulties Islamic banks face in generating diversified income beyond their investments. In summary, Islamic banks demonstrate context-dependent stability and reduced volatility but encounter challenges in operational efficiency related to income diversification.

Hossain and Matin (2023) ^[10] found that high liquidity and credit risk adversely impact the operational efficiency of Islamic banks in Bangladesh, underscoring the necessity for effective risk management. Akter and Sultana (2019) ^[11] noted that Islamic banks in Bangladesh manage costs effectively but struggle with asset utilization when compared to conventional banks, indicating potential for improvement in asset deployment to enhance efficiency. Furthermore, Akter and Sultana (2021) ^[13] reported that both Islamic and conventional banks-maintained solvency over time, with Islamic banks generally exhibiting stronger solvency buffers, suggesting greater financial stability under varying economic

conditions. Collectively, these studies highlight that effective risk management, cost control, and asset utilization are essential for improving the performance and stability of Islamic banks in Bangladesh.

Muhiuddin and Jahan (2018) ^[14] discovered that Islamic banks in Bangladesh typically achieve higher levels of profitability, with internal and industry factors having a more significant impact than macroeconomic variables. Hossain (2015) ^[15] presented mixed results regarding profitability between Islamic and conventional banks from 2008 to 2012, indicating that while Islamic banks excelled in certain metrics, they did not consistently outperform in all areas. Safiullah (2010) ^[16] pointed out that conventional banks surpassed Islamic banks in terms of profitability and efficiency, whereas Islamic banks exhibited better liquidity and capital adequacy, showcasing their complementary strengths. In summary, conventional banks generally excel in profitability and operational efficiency, while Islamic banks uphold stronger liquidity and capital reserves, which are essential for financial stability in the Bangladeshi banking sector.

Rakib and Hasan (2024) ^[17] examined the profitability disparities between Islamic and conventional banks in Bangladesh from 2018 to 2022 in the context of economic fluctuations following COVID-19. Their findings revealed that Islamic banks demonstrated competitive return on assets (ROA) and return on equity (ROE) in several years, despite facing margin pressures, indicating their resilience. Rahman and Islam (2018) ^[18] employed CAMEL ratings to assess selected private banks and noted considerable variation in composite scores, with differences being more associated with individual banks rather than the type of banking. Alam and Uddin (2017) ^[19] evaluated the broader Bangladeshi banking sector using CAMEL and composite scoring, identifying an average moderate performance characterized by strengths in capital adequacy and liquidity, but weaknesses in asset quality. Collectively, these studies imply that Islamic banks sustain resilient profitability in the face of challenges, while the overall stability of the sector is heavily reliant on effective asset quality management alongside strong capital and liquidity.

Johne *et al.* (2021) ^[20] examined the global efficiency convergence between Islamic and conventional banks, discovering that both types attain similar steady-state efficiency and convergence rates over time, which suggests a reduction in efficiency gaps despite their structural differences. This convergence illustrates adaptive and competitive dynamics on a global scale. Farooq and Zaheer (2015) ^[21] investigated the risk profile of Islamic banks through the lens of depositor discipline, concluding that there is no intrinsic higher risk associated with Islamic banks. However, their distinct profit-and-loss sharing contracts influence depositor behavior and risk monitoring in a manner that differs from conventional banks, while still maintaining an overall risk profile that is comparable. Čihák and Hesse (2010) ^[22] conducted an analysis of insolvency risks on a global scale using Z-scores, revealing that smaller Islamic banks tend to be more stable than their larger Islamic and conventional counterparts. Their research underscored the significance of bank size and the composition of regional banking markets as critical factors influencing stability, highlighting the importance of scale and market structure in evaluating insolvency risks within the realm of Islamic banking internationally. In summary, these studies

collectively emphasize the increasing operational similarities between different banking types, the intricate risk management strategies employed by Islamic banks, and the vital influence of size and market conditions on global banking stability.

Bader *et al.* (2008) ^[23] employed Data Envelopment Analysis (DEA) to assess the cost, revenue, and profit efficiency of Islamic and conventional banks on an international scale, revealing that efficiency levels differ by region. Islamic banks frequently demonstrate performance levels that are on par with those of conventional banks, indicating a regional variation in operational efficiency. Shamsuddeen and Selim (2018) ^[24] examined the efficiency of Islamic banks before, during, and after the global financial crisis, observing that ownership structures and market characteristics played a role in the efficiency disparities when compared to conventional banks. Beck, Demirgüç-Kunt, and Merrouche (2013) ^[25] discovered that, on a global scale, Islamic banks possess slightly distinct business models but are generally better capitalized and experience fewer loan losses during periods of financial stress, which contributes to their resilience. Raihan and Sultana (2023) ^[26] found that in Bangladesh, the CAMEL factors predict profitability in varying ways: for Islamic banks, earnings quality and liquidity are more significant, whereas asset quality and capital adequacy are more critical for conventional banks. These collective findings emphasize that Islamic banks exhibit robust regional efficiencies, resilience during crises influenced by institutional factors, and unique financial priorities in comparison to conventional banks, highlighting their distinct operational frameworks and risk management strategies both globally and locally.

Haque and Rahman (2020) ^[27] assessed Bangladeshi banks through the CAMEL framework and discovered that Islamic banks have more robust liquidity buffers, which enhance their resilience. In contrast, conventional banks demonstrate superior operational efficiency, indicating that both types of banks possess complementary strengths in liquidity and cost management. Rahman and Akter (2022) ^[28] emphasized the differences in governance, revealing that Islamic banks exhibit stronger Shariah governance, which contributes to improved stability and efficiency. Rafiq (2020) ^[29] affirmed that Islamic banks are competitive in terms of profitability and liquidity, while conventional banks excel in cost efficiency, highlighting the unique advantages of each banking type. Hossain and Rahman (2022) ^[30] conducted a review of studies that compared profitability and efficiency, indicating that Islamic banks frequently have better capitalization and liquidity, whereas conventional banks generally maintain higher cost efficiency. These findings underscore that performance evaluations are influenced by the methodology employed and the temporal context, reflecting the changing dynamics within Bangladesh's banking sector. Collectively, these insights demonstrate that Islamic banks prioritize liquidity and governance, which bolster financial stability, while conventional banks focus on operational efficiency and cost management, thereby illustrating a balanced banking ecosystem characterized by distinct yet complementary strengths.

Methodology of the Study

This research is characterized by its descriptive, analytical, and empirical format, relying on published financial statements from banks.

Sample Composition

The research examines domestic Islami shariah and non-shariah banks. For this analysis, there are 62 commercial banks operating in Bangladesh, comprising 10 Islami Shariah banks and 52 non-shariah banks. The sample includes three fully operational Islami Shariah banks and three non-shariah banks. These six banks were chosen through a simple random sampling technique from the total of 62 banks in Bangladesh.

Serial No.	Name of the Banks	Category
1	First Security Islami Bank Ltd.	Islami Shariah
2	Al Arafah Islami Bank Ltd.	
3	Export Import Bank Limited	
4	BRAC Bank Limited	Non-Shariah
5	Bank Asia Limited	
6	Arab Bangladesh Bank Ltd.	

Data Sources

This study relies entirely on secondary data. The financial information of the selected banks has been gathered from the financial statements of the respective banks. These financial statements were obtained from the official websites of the

chosen banks.

- www.fsiblbld.com
- www.al-arafahbank.com
- www.eximbankbd.com
- www.bracbankcom
- www.bankasia-bd.com
- www.abbl.com

Study Period

A ten-year period (2015-2024) has been chosen to assess the financial performance of selected Islamic Shariah and non-Shariah banks in Bangladesh.

Data Analysis Tools

This research utilizes the CAMELS Rating to assess the financial performance of banks, which is presently the latest tool used for this evaluation. The CAMELS framework includes Capital Adequacy, Asset Quality, Management Quality, Earnings Ability, Liquidity, and Sensitivity. The study adopts the CAMELS Rating approach because it offers a detailed, systematic, and reliable framework for evaluating both financial performance and risk, thus enabling a thorough comparison of banks. These are outlined as follows:

Serial No.	CAMELS	Ratios
1	Capital Adequacy	Total Capital / Risk Weighted Assets
2	Asset Quality	Non-Performing Loans / Total Loans
3	Management Quality	Operating Expenses / Operating Incomes
4	Earnings Performance	a. Return on Assets
		b. Return on Equity
5	Liquidity Performance	Liquid Assets / Total Assets
6	Sensitivity	Rate Sensitive Assets / Rate Sensitive Liabilities

Source: Mahmud A. & Rahman M. H. – 2020^[12], CAMEL and profitability

Composite Rating under CAMELS Rating Analysis

There are a total of five categories for composite CAMELS ratings. Calculation of Composite Value = C+A+M+E+L+S. These consist of:

Serial No.	Composite Range	Rating	Description
1	1.00-1.50	Strong	Solid Bank
2	1.50-2.50	Satisfactory	Average Performance
3	2.50-3.50	Fair	Require Attention
4	3.50-4.50	Marginal	Risky
5	4.50-5.00	Unsatisfactory	Significant Risk

Source: FDIC, Composite Ratings Definition List

Analysis and Interpretation

Capital Adequacy (C)

The Capital Adequacy Ratios (CAR) for selected Islamic (Shariah) and non-Shariah banks in Bangladesh from 2015 to 2024 indicate that EXIM Bank consistently leads the sector, with CAR values ranging from 10.52% to a peak of 22.34% in 2017. FSIBL and AIBL typically comply with regulatory standards (8%-10%), with FSIBL increasing from 7.18% in 2015 to over 9% in recent times. In contrast, non-Shariah banks like BRAC have seen a decline from 19.28% in 2015 to 7.76% in 2024, falling below the required CAR, while Bank Asia and AB Bank have also experienced decreases, suggesting a higher risk exposure among non-Shariah banks.

Asset Quality (A)

Asset Quality (A), assessed through the Non-Performing Loans (NPLs) to Total Loans ratios, is benchmarked at 2%-5%. The Islami Shariah banks—FSIBL, AIBL and EXIM—

maintain NPL ratios that are within or below this standard, demonstrating effective credit management. Conversely, BRAC and AB Bank frequently surpass the upper limit, indicating poorer asset quality. Bank Asia's ratios are often close to the standard, occasionally dipping below it. Overall, Islami banks exhibit superior asset quality and risk management compared to their non-Shariah counterparts, particularly highlighted by the elevated NPLs of BRAC and AB Bank.

Management Quality (M)

Management Quality (M), defined by the Operating Expenses to Operating Income ratios, is benchmarked between 50%-70%. The Islami Shariah banks predominantly operate below or near the lower threshold, reflecting strong operational efficiency and cost control, with FSIBL consistently demonstrating low ratios. Non-Shariah banks, especially BRAC and AB Bank, frequently exceed 70%, with BRAC's expense ratios exceeding 100% in certain years, indicating operational inefficiency where expenses surpass income. Bank Asia generally remains close to the benchmark, indicating moderate efficiency. Therefore, Islami banks excel over non-Shariah banks in terms of cost management and operational quality.

Earnings Performance (E)

The data illustrates the Return on Assets (ROA) and Return on Equity (ROE) for Islami Shariah and non-Shariah banks from 2015 to 2024. Non-Shariah bank BRAC consistently achieved a higher ROA, reaching up to 1.95% in 2017, in contrast to FSIBL's peak of 0.72% in 2024 among Islami

Sariah banks. Regarding ROE, FSIBL of the Islami Sariah banks experienced significant growth from 8.80% in 2015 to 18.81% in 2024, exceeding BRAC's ROE, which increased from 13.32% to 17.43%. Bank Asia exhibited mixed results, while AB Bank remained the lowest in both metrics. The findings suggest that non-Sariah banks demonstrate superior asset efficiency, whereas some Islami banks show stronger growth in equity returns.

Liquidity Performance (L)

The liquidity performance data for the years 2015-2024 indicates that FSIBL consistently exceeded the 15% standard, achieving a high of 20.00% in 2015 and a low of 13.15% in 2019, before rising above 18% in recent years. AIBL's liquidity ratio decreased from 13.34% in 2015 to 7.48% in 2024, falling below the standard in the later years. EXIM Bank maintained a stable liquidity ratio ranging from 12.59% to 12.70%, consistently near but slightly below the 15% benchmark. Among non-Shariah banks, AB Bank consistently surpassed the standard with ratios around 16.5% to 16.7%, while BRAC and Bank Asia maintained stable but lower liquidity ratios, approximately between 13.5% and 9.5%, respectively. This trend demonstrates that most banks adhered to or approached standard liquidity levels, although AIBL's declining ratio indicates potential liquidity risks.

Sensitivity (S)

The sensitivity ratio (S), which is defined as the proportion of rate-sensitive assets to liabilities, reflects the exposure of banks to fluctuations in interest rates. In the case of Islamic Shariah banks (FSIBL, AIBL, EXIM), the S values typically surpass 100% in the later years, indicating that these banks have asset-heavy structures that may benefit from increases in interest rates but are also at-risk during downturns. Conversely, non-Shariah banks (BRAC, Bank Asia, AB Bank) demonstrate lower and more stable ratios, frequently remaining below 100%, which suggests a more conservative approach to liability management. In summary, Islamic banks are showing a trend of increasing sensitivity (for instance, AIBL is projected to rise to 126% by 2023), which reflects the dynamics of Shariah-compliant financing, while their non-Islamic counterparts continue to uphold balanced profiles in the face of economic volatility.

Composite Rating Analysis under CAMELS Rating Method

The data indicates that all six banks—FSIBL, AIBL, EXIM, BRAC, Bank Asia, and AB Bank—consistently attained a composite rating of "1," which signifies satisfactory performance from 2015 to 2024. First Security Islami Bank and Export Import Bank exhibited stable composite values predominantly ranging from 1.75 to 2.06, consistently categorized as satisfactory. Al-Arafah Islami Bank began with lower composite ratings (1.20, 1.26) classified as "Strong," but transitioned to satisfactory as scores experienced a slight increase. BRAC Bank demonstrated more variability, with higher composite values reaching above 2.5 in certain years, resulting in "Fair" classifications in 2018, 2020, 2021, and 2022, before reverting to satisfactory ratings. Both Bank Asia and AB Bank showed consistently satisfactory values and descriptions, with composite values concentrated between 1.78 and 2.13. These patterns suggest stable and robust ratings for the majority of banks, with the exception of the occasional performance fluctuations observed for BRAC Bank over the past decade.

Discussion

The Islamic Shariah and non-Shariah banking sectors in Bangladesh from 2015 to 2024 reveal considerable differences in financial stability, efficiency and growth. Islamic banks, including EXIM Bank, consistently exhibit higher Capital Adequacy Ratios (CAR) and lower Non-Performing Loan (NPL) ratios, reflecting greater resilience and superior risk management capabilities. Their management practices are more cost-efficient, as demonstrated by lower operating expense-to-income ratios, whereas non-Shariah banks such as BRAC attain a higher Return on Assets (ROA), indicating effective asset utilization. Islamic banks, particularly FSIBL, report an increased Return on Equity (ROE), which further benefits shareholders. Liquidity levels are generally adequate across all banks; however, the declining position of AIBL raises concerns. Sensitivity ratios suggest that Islamic banks are more vulnerable to rate-sensitive assets due to Shariah-compliant financing models, which increases their interest rate risk compared to non-Shariah banks. In conclusion, Islamic banks excel in capital strength, asset quality, and cost efficiency, positioning themselves as stable institutions, while non-Shariah banks offer higher profitability but encounter challenges related to capital adequacy and asset quality. This scenario highlights the need for customized regulatory interventions. All six banks—FSIBL, AIBL, EXIM, BRAC, Bank Asia, and AB Bank—achieved consistent composite ratings of '1' and largely satisfactory performance, with the exception of BRAC Bank, which faced significant volatility.

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