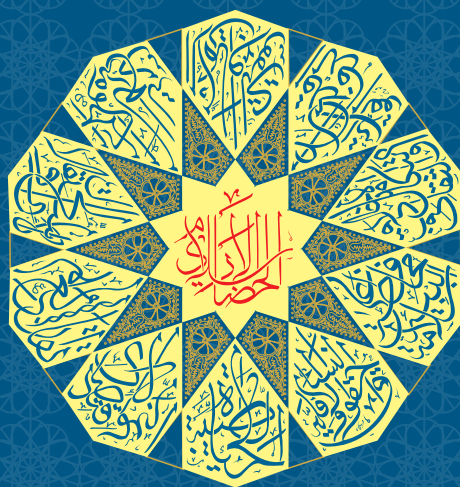


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A QUANTITATIVE STUDY OF THE ROLE SHARIAH BOARDS AND BANK OWNERSHIP STRUCTURES PLAY IN ENHANCING THE FINANCIAL PERFORMANCE OF ISLAMIC BANKS: A CASE STUDY OF PAKISTAN

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*Sheila Ainon Yussof***

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Abstract: Shariah governance is a central feature and the second layer of corporate governance for Islamic banks (IBs) and Islamic financial institutions (IFIs). Shariah governance is unique to IBs and IFIs due to their possession of Shariah Supervisory Boards (SSB). SSBs serve to ensure that the management of Islamic banking institutions complies with shariah principles. Shariah governance is not only designed to raise the confidence of investors and the public in terms of authenticity and compliance to Islamic banking practices, but also to minimise the fiduciary and reputational risks of Islamic banking institutions. Due to the importance of shariah governance and the role of SSBs in IBs, this research investigates the role of SSBs in influencing the financial performance of IBs with the moderation role of ownership structure in Pakistan. By using nine years of data (2009-2017) pertaining to three Islamic banks in Pakistan, we found that shariah supervisory board reputations, expertise, cross membership, change in composition, shariah qualification, and ownership have significant moderation relationships with the financial performance of IBs. This study is an attempt to provide a deeper understanding of the role of owners and Shariah Supervisory Boards in enhancing the financial performance of Islamic banks for both researchers and policymakers.

Keywords: shariah governance, Islamic banks financial performance, ownership structure of Islamic banks.

Introduction

An Overview of the Islamic Banking System in Pakistan

The Islamic banking system in Pakistan started in the 1970s and was initially focused on the elimination of *riba* ' among financial institutions. Later on, during the 1980s, it gained more importance. In 1985, support from the Pakistani

government contributed to its fast growth. However, soon after, political instability and inadequate jurisdiction restricted the growth and development of the Islamic banking system. In 1991, the “mark-up” charged by banks was declared un-Islamic by order of the Federal Sharia Court of Pakistan. In 2000, a special commission was established by the Pakistani government, known as the Commission for the Transformations of Financial System (CTFS). The CTFS is a special committee that works for the development and standardisation of financial instruments used by Islamic financial institutions.

After its establishment, CTFS played a crucial role in the development of Islamic banking in Pakistan. The State Bank of Pakistan (SBP) further established a Division of Islamic Banking in its department of banking policy. Later on, in 2003, this Division for Islamic Banking expanded and became a full-fledged Islamic banking department. In 2001, SBP focused on the establishment of Islamic banking services in the private banking sector by providing specified criteria as guidelines. For the incorporation of IBs, the SBP adopted three strategies, (1) establishment of Islamic banking in the private sector, (2) establishment of subsidiaries of IBs, and (3) establishment of Islamic windows within present commercial banks. Al Meezan Investment Bank Limited became the first to implement a purely Islamic banking system based on the specified criteria of SBP and applied to be an Islamic Bank in the State of Pakistan. In 2002, SBP issued a license to this end.

According to reports issued in March 2018, Islamic banking in Pakistan has a total market share of 13.5 per cent assets and 14.6 per cent market share of deposits. The IB industry in Pakistan consists of twenty-one (21) Islamic banks—in which five (5) are pure Islamic banks, while sixteen (16) are conventional banks with Islamic banking branches. The total number of Islamic bank branches in Pakistan, spanning across 111 districts, is about 2,589 (end of March 2018). On the other hand, Islamic banking windows established by conventional banks recorded a total of 1,283 branches (end of March 2018).

The Role of Shariah Governance in Islamic Banks

The main aim of the Islamic banking system is shariah compliance, particularly in ensuring fair business practice in accordance with the shariah.¹ One of the ways to make this possible is through proper accountability and transparency.² For Islamic financial institutions, forms of shariah governance include: (1) an arrangement where managers act in the best interests of shareholders and their wealth; (2) the whole governance body, including all boards and committees, is organised to ensure efficient use of all resources for the best interests of

shareholders; and (3) implementation of shariah principles is enacted according to the guidelines provided by the Islamic Financial Services Board (IFSB) in 2016. Under the shariah governance system, SSB is considered an important element because it plays a crucial role in supervising, auditing, monitoring, as well as shaping expert opinions in terms of shariah compliance.³

This research will be investigating the role of shariah governance by using the ownership structure (managerial ownership or institutional ownership) as a moderator to assess its impact on the financial performance of IBs. It will use three proxies of performance: ROA, ROE, and operational efficiency.

Literature Review

The following parameters or characteristics of Shariah Supervisory Boards are used to measure shariah governance: SSB-reputation, SSB-qualification, SSB-expertise, SSB-cross membership, SSB-composition, and the moderating effect of ownership structure.

Shariah Supervisor Board Characteristics:

Reputation of Shariah Supervisory Board

Resource dependence theory posits that a Board of Directors plays a crucial role in providing skills and information to a firm.⁴ Thus, the Board of Directors has the potential to enhance the financial performance of firms,⁵ and establish a good reputation for them.⁶ In addition to the education and experience of board members, human capital plays a massive role in increasing financial performance.⁷ Consequently, there is a strong relationship between firm performance and the reputation of its directors.⁸ Similarly, there is also a strong relationship between the reputation of SSBs and the performance of IBs. Literature indicates that the reputation of shariah board members represents the level of knowledge in the industry.^{9,10} Hence, we hypothesise that:

H1: Shariah Supervisory Board reputation will be positively associated with IB financial performance.

Qualifications of the Shariah Supervisory Board

Education level is an important feature in determining the quality of any board.¹¹ Shariah supervisory board members who have doctoral degrees in shariah law or Islamic finance-related studies are considered well-qualified members of the board. Well-qualified board members can easily understand,

evaluate, and introduce complex products and services according to shariah rules. Additionally, shariah board members with credible religious education will enhance the credibility of an Islamic financial institution. There are many studies that show that a bank's financial performance and competitiveness level are positively influenced by their board members' level of education.^{12,13} Thus, we hypothesise that:

H2: The Shariah Supervisory Board's qualifications will be positively associated with IB financial performance.

Shariah Supervisory Board Expertise

The level of expertise of board members is crucial in ensuring that all operational activities of a bank are well managed.^{14,15} Directors that have in-depth financial knowledge can better understand business activities and deal with managers, thus positively affecting the performance of their institutions.¹⁶ On the other hand,¹⁷ some research has found that boards of directors with a higher level of expertise can negatively impact a firm's performance. In general, it can be concluded that the level of expertise of Shariah Supervisory Boards consisting of members who hold specialised degrees in accounting, finance, or economics significantly affect the performance of Islamic banks, therefore:

H3: Shariah Supervisory Board expertise will be significantly associated with IB financial performance.

Shariah Supervisory Board Cross Membership

From the theoretical perspective of RDT (resource dependence theory), directors who hold positions in different organisations have more diversified knowledge, which in turn enhances a firm's performance.^{18,19} Cross-membership involves those who have board memberships in more than one Islamic financial institution. Board interlocking is widely practised by financial institutions as a form of strategic management, more so due to its relatively low cost.²⁰ Board cross membership brings qualified directors from a pool of individuals from different, well-recognised financial institutions.^{21,22} Cross-membership provides access to well-experienced members, enhancing a firm's performance through the exchange of information and ideas^{23,24} and the creation of communication channels between different organisations.²⁵ Such practice also benefits the directors as they can get handsome salaries from different institutions.²⁶ Thus, we hypothesise that:

H4: Shariah Supervisory Board cross membership is positively associated with IB financial performance.

Shariah Supervisory Board Annual Composition

Annual composition refers to the number of board members in a bank's financial year.²⁷ Board members include executive and non-executive directors. A higher ratio of non-executive directors leads towards boarder independence, which ultimately leads to enhanced performance.²⁸ Based on the Agency Theory, independent directors usually provide good oversight of business activities, often work for the best interests of shareholders, and enhance a firm's performance.²⁹ There are some studies, however, that indicate a negative association between the composition of the board and firm performance.^{30,31} Thus, we hypothesise that:

H5: Shariah Supervisory Board annual composition will positively affect IB financial performance.

Moderating Effect of Ownership Structure:

Ownership structure is the percentage of shares which are held by different types of shareholders. This may include managerial ownership, family ownership, foreign and institutional ownership. Ownership structure indicates how many categories of owners there are in a business (like partnership, proprietorship, or corporation) and how many shares are held by other partners. Any change in ownership structure without regulatory support may cause problems for a bank.³² Ownership structure highly affects the governance of a business, which will in turn affect its efficiency and performance.³³

Institutional Ownership and Financial Performance

There are two (2) divergent views on this.³⁴ First, that Institutional Ownership does not have any impact on bank performance. Second, that Institutional Ownership does have a positive association with the financial performance of a IB.³⁵ Based on this, we hypothesise that:

H6: Institutional ownership will be significantly associated with IB financial performance.

There is no study exploring the moderating impact of institutional ownership structures on the characteristics of shariah supervisory boards and financial performance of Islamic banks. Thus, this study will test this.

The following are sub-hypotheses of the moderation impact institutional ownership will have on the relationship between SSB characteristics and IB financial performance, derived from previously discussed literature:

H6 (a): Institutional ownership will positively moderate the relationship between Shariah Supervisory Board reputation and IB financial performance.

H6 (b): Institutional ownership will positively moderate the relationship between Shariah Supervisory Board qualification and IB financial performance.

H6 (c): Institutional ownership will positively moderate the relationship between Shariah Supervisory Board expertise and IB financial performance.

H6 (d): Institutional ownership will positively moderate the relationship between Shariah Supervisory Board cross membership and IB financial performance.

H6 (e): Institutional ownership will positively moderate the relationship between Shariah Supervisory Board composition and IB financial performance.

Managerial Ownership and Financial Performance

Managerial ownership is a type of ownership where a majority of shares are held by a management team. When managers or management teams have their own interest in the business, they make better decisions, making the business more efficient.³⁶ Firms with a higher proportion of managerial owners like to take more debt and increase their bank's performance.³⁷ Thus, we hypothesise that:

H7: Managerial ownership will be positively associated with IBs financial performance.

There are currently no studies exploring the moderating impact of ownership structure (managerial ownership) on the relationship between Shariah Supervisory Boards and the performance of Islamic banks. Thus, we further hypothesise the following sub-hypotheses regarding the moderation relationship of managerial ownership among SSB characteristics and IB performance:

H7 (a): Managerial ownership will positively moderate between Shariah Supervisory Board reputation and IB financial performance.

H7 (b): Managerial ownership will positively moderate between Shariah Supervisory Board qualification and IB financial performance.

H7 (c): Managerial ownership will positively moderate between Shariah Supervisory Board expertise and IB financial performance.

H7 (d): Managerial ownership will positively moderate between Shariah Supervisory Board cross membership and IB financial performance.

H7 (e): Managerial ownership will positively moderate between Shariah Supervisory Board annual composition and IB financial performance.

Research Methodology

Sample, Sources and Description of the Data

In this study, secondary data collected from the published annual reports of the selected IBs was used for analysis. There are five pure Islamic banks in Pakistan (Meezan Bank, Bank Islami, Burj Bank, Dubai Islamic Bank and Al-Baraka Bank). Burj Bank merged with Al-Baraka Bank in mid-2016, which leaves four remaining (Meezan Bank, Bank Islami, Dubai Islamic Bank, and Al-Baraka Bank). Out of these data on Dubai Islamic Bank is inaccessible, leaving only three for the purpose of research (Meezan Bank, Bank Islami and Al Baraka Bank). Nine years of data, from 2009 to 2017, were used for analysis. The data provided information about the characteristics of Shariah Supervisory Boards (SSB qualification, SSB reputation, SSB expertise, SSB cross membership, SSB composition), ownership structure (institutional ownership and managerial ownership) and performance (return on equity, return on assets and operational efficiency).

Measurement of Variables

| Variable Name | Measurement |
|---------------|---|
| SSB-REPUT | % of SSB members sit on AAOIFI |
| SSB-QUAL | % of SSB members with a PhD in shariah or Islamic financial studies |
| SSB-EXPR | % of SSB members with knowledge of banking and accounting |
| SSB-CRMB | % of SSB who sit on other Islamic financial institutions |
| SSB-COMP | Annual change in the composition of SSB. If board change then 1 otherwise 0 |
| INST-OWNERSHP | % of shares held by institutions |
| MNG-OWNERSHIP | % of shares held by managers |
| BANK-AGE | Total years since bank established |
| FIRM-SIZE | Log of total assets |
| ROE | Net income / total equity |

| | |
|---------|-----------------------------------|
| ROA | Net income / total assets |
| OPP-EFF | Total profit earned / total costs |

Variables discussed above are already used and measured by Nomran et al. (2018) and Lepore et al. (2019).

Econometric Models

The following econometric model was adopted from a study entitled “Managerial Ownership, Board Monitoring and Firm Performance in a Family-concentrated Corporate Environment” by Cheng et al., (2010).

$$\begin{aligned}
 ROE &= \beta_0 + \beta_1 SSB-REPUT_{it} + \beta_2 SSB-QUAL_{it} + \beta_3 SSB-EXPR_{it} + \beta_4 SSB-CRMB_{it} + \beta_5 SSB-COMP_{it} + \mu_{it} \\
 ROE &= \beta_0 + \beta_1 SSB-REPUT_{it} + \beta_2 SSB-QUAL_{it} + \beta_3 SSB-EXPR_{it} + \beta_4 SSB-CRMB_{it} + \beta_5 SSB-COMP_{it} + \beta_6 INST-OWN_{it} + \beta_7 MNG-OWN_{it} + \beta_8 BANK-AGE_{it} + \beta_9 FIRM-SIZE_{it} + \mu_{it} \\
 ROE &= \beta_0 + \beta_1 SSB-REPUT * INST-OWN_{it} + \beta_2 SSB-QUA * INST-OWN_{it} + \beta_3 SSB-EXPR * INST-OWN_{it} + \beta_4 SSB-CRMB * INST-OWN_{it} + \beta_5 SSB-COMP * INST-OWN_{it} + \mu_{it} \\
 ROE &= \beta_0 + \beta_1 SSB-REPUT * MNG-OWN_{it} + \beta_2 SSB-QUAL * MNG-OWN_{it} + \beta_3 SSB-EXPR * MNG-OWN_{it} + \beta_4 SSB-CRMB * MNG-OWN_{it} + \beta_5 SSB-COMP * MNG-OWN_{it} + \mu_{it} \\
 ROA &= \beta_0 + \beta_1 SSB-REPUT_{it} + \beta_2 SSB-QUAL_{it} + \beta_3 SSB-EXPR_{it} + \beta_4 SSB-CRMB_{it} + \beta_5 SSB-COMP_{it} + \mu_{it} \\
 ROA &= \beta_0 + \beta_1 SSB-REPUT_{it} + \beta_2 SSB-QUAL_{it} + \beta_3 SSB-EXPR_{it} + \beta_4 SSB-CRMB_{it} + \beta_5 SSB-COMP_{it} + \beta_6 INST-OWN_{it} + \beta_7 MNG-OWN_{it} + \beta_8 BANK-AGE_{it} + \beta_9 FIRM-SIZE_{it} + \mu_{it} \\
 ROA &= \beta_0 + \beta_1 SSB-REPUT * INST-OWN_{it} + \beta_2 SSB-QUA * INST-OWN_{it} + \beta_3 SSB-EXPR * INST-OWN_{it} + \beta_4 SSB-CRMB * INST-OWN_{it} + \beta_5 SSB-COMP * INST-OWN_{it} + \mu_{it} \\
 ROA &= \beta_0 + \beta_1 SSB-REPUT * MNG-OWN_{it} + \beta_2 SSB-QUAL * MNG-OWN_{it} + \beta_3 SSB-EXPR * MNG-OWN_{it} + \beta_4 SSB-CRMB * MNG-OWN_{it} + \beta_5 SSB-COMP * MNG-OWN_{it} + \mu_{it} \\
 OP-EFF &= \beta_0 + \beta_1 SSB-REPUT_{it} + \beta_2 SSB-QUAL_{it} + \beta_3 SSB-EXPR_{it} + \beta_4 SSB-CRMB_{it} + \beta_5 SSB-COMP_{it} + \mu_{it} \\
 OP-EFF &= \beta_0 + \beta_1 SSB-REPUT_{it} + \beta_2 SSB-QUAL_{it} + \beta_3 SSB-EXPR_{it} + \beta_4 SSB-CRMB_{it} + \beta_5 SSB-COMP_{it} + \beta_6 INST-OWN_{it} + \beta_7 MNG-OWN_{it} + \beta_8 BANK-AGE_{it} + \beta_9 FIRM-SIZE_{it} + \mu_{it} \\
 OP-EFF &= \beta_0 + \beta_1 SSB-REPUT * INST-OWN_{it} + \beta_2 SSB-QUA * INST-OWN_{it} + \beta_3 SSB-EXPR * INST-OWN_{it} + \beta_4 SSB-CRMB * INST-OWN_{it} + \beta_5 SSB-COMP * INST-OWN_{it} + \mu_{it} \\
 OP-EFF &= \beta_0 + \beta_1 SSB-REPUT * MNG-OWN_{it} + \beta_2 SSB-QUAL * MNG-OWN_{it} + \beta_3 SSB-EXPR * MNG-OWN_{it} + \beta_4 SSB-CRMB * MNG-OWN_{it} + \beta_5 SSB-COMP * MNG-OWN_{it} + \mu_{it}
 \end{aligned}$$

All used variables in these equations are defined below.

Details of Variables

SSB-REPUT is the reputation of SSB members represented by the percentage who are also members of the AAOIFI (Accounting and Auditing Organization for Islamic Financial Institutions). SSB members are considered reputed if they have membership of the AAOIFI because the latter is an international standard-setter and the highest shariah board for Islamic Financial Institutions. SSB-QUAL measures the number of SSB members with PhDs in shariah or Islamic finance-related studies. SSB-EXPRT represents the level of expertise of SSB members, referring to board members who have accounting and finance knowledge. SSB-CRMB denotes the cross-membership of SSB members. SSB-COMP refers to the annual composition of SSB members.

In this research, the performance of Islamic banks is measured in three ways: (i) ROE, which is measured through net income divided by total equity; (ii) ROA, which is measured through net income divided by total assets; and (iii) Operational Efficiency, which is measured through total earned profits and total operational costs over a certain period. Bank age refers to years of bank operation, and firm size refers to a bank's log of total assets.

Results and Discussion

Descriptive Statistics

| | ROE | ROA | OP_EFF | SSB-QUAL | SSB-EXPR | SSB-CRMB | SSB-COMP | SSB-REPUT | BANK_AGE | FIRM_SIZE | MNG-OWN | INST-OWN |
|-----------|--------|--------|--------|----------|----------|----------|----------|-----------|----------|-----------|---------|----------|
| Mean | 0.108 | 0.008 | 0.247 | 0.377 | 0.273 | 0.866 | 0.370 | 0.477 | 14.333 | 7.927 | 0.189 | 0.040 |
| Median | 0.118 | 0.010 | 0.299 | 0.333 | 0.333 | 1.000 | 0.000 | 0.333 | 12.000 | 7.906 | 0.196 | 0.007 |
| Maximum | 0.191 | 0.019 | 0.535 | 1.000 | 0.333 | 1.000 | 1.000 | 1.000 | 27.000 | 8.972 | 0.371 | 0.453 |
| Minimum | -0.100 | -0.018 | -0.119 | 0.000 | 0.167 | 0.667 | 0.000 | 0.000 | 4.000 | 7.119 | 0.008 | 0.004 |
| Std. Dev. | 0.073 | 0.007 | 0.178 | 0.386 | 0.081 | 0.151 | 0.492 | 0.382 | 6.978 | 0.565 | 0.151 | 0.119 |
| Skewness | -0.926 | -2.035 | -0.334 | 0.304 | -0.553 | -0.363 | 0.537 | 0.357 | 0.399 | 0.218 | 0.040 | 3.251 |
| Kurtosis | 3.707 | 8.417 | 2.042 | 1.480 | 1.323 | 1.345 | 1.288 | 1.662 | 1.871 | 1.816 | 1.438 | 11.574 |

Table 1: Descriptive Statistics

SSB-REPUT is the reputation of SSB members, SSB-QUAL is the education level of SSB members, SSB-EXPR is the expertise of SSB members, SSB-CRMB is the cross-membership of SSB members, and SSB-COMP is the annual composition of SSB members.

Table 1 shows the output of descriptive statistics for this study. The mean value of IB performance in terms of ROE is 10.8 per cent, ROA is 0.8 per cent, and Operational Efficiency is 24.7 per cent, which shows that the overall performance of the IBs is good. The mean value for SSB-qualification is 37.7 per cent, indicating that 37.7 per cent of Shariah Supervisory Boards consist of members with doctoral degrees in Islamic finance, shariah law, or Islamic studies. The mean value for SSB-expertise is 27.3 per cent. The mean value for SSB-cross membership is 86.6 per cent, the highest percentage compared to other Shariah Supervisory Board characteristics. The mean value for SSB-composition is 37 per cent. The mean value for SSB-reputation is 47 per cent, meaning that 47 per cent of shariah board members are also members of the AAOIFI. The mean value for bank age is 14.33 and firm size is 7.9 per cent. The mean value for managerial ownership is 18.9 per cent which means that about 18.9 per cent of Islamic banks in Pakistan are controlled by the management team. The mean value for institutional ownership is 4 per cent which shows that a very low proportion of the shares of Islamic Banks in Pakistan are controlled by institutions.

Correlation Analysis of the study

| Probability | ROE | ROA | OP_EFF | SSB-QUAL | SSB-EXPR | SSB-CRMB | SSB-REPUT | SSB-COMP | BANK_AGE | FIRM_SIZE | MNG-OWN | INST-OWN |
|-------------|---------|---------|---------|----------|----------|----------|-----------|----------|----------|-----------|---------|----------|
| ROE | 1.0000 | | | | | | | | | | | |
| ROA | 0.5677 | 1.0000 | | | | | | | | | | |
| | 0.0000 | | | | | | | | | | | |
| OP_EFFICNCY | 0.6565 | 0.5383 | 1.0000 | | | | | | | | | |
| | 0.0002 | 0.0000 | | | | | | | | | | |
| SSB-QUAL | 0.2019 | 0.0154 | -0.0670 | 1.0000 | | | | | | | | |
| | 0.3126 | 0.9391 | 0.7400 | | | | | | | | | |
| SSB-EXPR | 0.0882 | -0.1251 | -0.6183 | 0.1832 | 1.0000 | | | | | | | |
| | 0.6618 | 0.5341 | 0.0006 | 0.3602 | | | | | | | | |
| SSB-CRMB | 0.5558 | 0.3676 | 0.4376 | 0.0335 | 0.0073 | 1.0000 | | | | | | |
| | 0.0026 | 0.0592 | 0.0224 | 0.8681 | 0.9711 | | | | | | | |
| SSB-REPUT | 0.3547 | 0.4539 | 0.3216 | 0.3965 | 0.3142 | 0.4905 | 1.0000 | | | | | |
| | 0.0000 | 0.0174 | 0.1019 | 0.0406 | 0.1105 | 0.0000 | | | | | | |
| SSB-COMP | 0.0105 | 0.1440 | 0.4527 | -0.4078 | -0.5446 | 0.0464 | -0.1906 | 1.0000 | | | | |
| | 0.9585 | 0.4736 | 0.0177 | 0.0348 | 0.0033 | 0.8181 | 0.3409 | | | | | |
| BANK_AGE | 0.3582 | 0.4953 | 0.5575 | -0.3087 | -0.3946 | 0.2514 | 0.0343 | 0.5675 | 1.0000 | | | |
| | 0.0666 | 0.0086 | 0.0000 | 0.1171 | 0.0000 | 0.2059 | 0.4651 | 0.0020 | | | | |
| FIRM_SIZE | 0.3658 | 0.0110 | -0.3234 | 0.2962 | 0.4405 | 0.3571 | 0.6651 | -0.4333 | -0.4710 | 1.0000 | | |
| | 0.0606 | 0.9566 | 0.0999 | 0.1335 | 0.0000 | 0.0675 | 0.0002 | 0.0239 | 0.0131 | | | |
| MNG-OWN | -0.3126 | 0.0116 | 0.3696 | -0.4542 | -0.2636 | -0.3400 | -0.6699 | 0.5968 | 0.6577 | -0.5986 | 1.0000 | |
| | 0.1124 | 0.9540 | 0.0578 | 0.0173 | 0.0000 | 0.0827 | 0.0001 | 0.0010 | 0.0002 | 0.0000 | | |
| INST-OWN | -0.0181 | 0.2049 | 0.1873 | 0.4775 | -0.3698 | -0.3753 | -0.2218 | 0.0674 | 0.2055 | -0.3802 | 0.3301 | 1.0000 |
| | 0.9285 | 0.3053 | 0.3494 | 0.0118 | 0.0576 | 0.0537 | 0.2663 | 0.7385 | 0.3039 | 0.0504 | 0.0927 | |

Table 2

*** level of significant at 1 per cent, ** level of significant at 5 per cent, * level of significant at 10 per cent. SSB-REPUT is the reputation of SSB members, SSB-QUAL is the education level of SSB members, SSB-EXPR is the expertise of SSB members, SSB-CRMB is the cross-membership of SSB members, and SSB-COMP is the annual composition of SSB members.

Table 2 shows the correlation analysis of the study, which indicates that there is no problem of multicollinearity in this model.

| Variables | ROE | ROA | OPE |
|-------------------------|--------------------------|--------------------------|--------------------------|
| SSB-REPUT | 0.2485 (0.003) *** | 0.0041 (0.4541) | 0.396729 (0.0051) *** |
| SSB-QUAL | -0.0441 (0.1974) | 0.0015 (0.5728) | -0.09534 (0.2021) |
| SSB-EXPR | -0.2240 (0.1716) | 0.1754 (0.0000) *** | -1.72798 (0.0001) *** |
| SSB-CRMB | -0.2266 (0.0953) *** | -0.0057 (0.5044) | -0.27115 (0.3500) |
| SSB-COMP | 0.0075 (0.7639) | -0.0013 (0.4159) | 0.041218 (0.4512) |
| INST-OWN | -0.2667 (0.0314) ** | -0.0218 (0.0001) *** | -0.19911 (0.2096) |
| MNG-OWN | 0.3236 (0.2206) | 0.0014 (0.0004) *** | -0.70718 (0.0729) * |
| BANK_AGE | -0.0065 (0.4595) | 0.0118 (0.2661) | 0.038433 (0.0000) *** |
| FIRM_SIZE | 0.0706 (0.4472) | 0.0208 (0.4148) | -0.38838 (0.0000) *** |
| SSB-REPUT * INST-OWN | 20.8560 (0.0000) *** | 1.260956 (0.3501) | 38.70888 (0.0000) *** |
| SSB-QUAL * INST- OWN | -2.2249 (0.5774) | -0.77555 (0.3239) | -6.70119 (0.2846) |
| SSB-EXPR * INST- OWN | 116.0258 (0.0001) *** | 16.08262 (0.0112) *** | 172.1766 (0.0015) *** |
| SSB-CRMB * INST- OWN | -30.8845 (0.0072) *** | -2.23065 (0.3782) | -42.6769 (0.0151) *** |

| | | | |
|---------------------|------------------------|--------------------------|-------------------------|
| SSB-COMP * INST-OWN | 0.0170 (0.8702) | -0.00206 (0.8761) | -0.00646 (0.9683) |
| SSB-REPUT * MNG-OWN | 0.1985 (0.5976) | 0.021396 (0.5855) | -0.8898 (0.1931) |
| SSB-QUAL * MNG-OWN | -0.3489 (0.0331) ** | -0.0615 (0.0011) *** | -0.28581 (0.1103) |
| SSB-EXPR * MNG-OWN | 2.5005 (0.0194) *** | 0.358762 (0.0025) *** | -2.8557 (0.0198) *** |
| SSB-CRMB * MNG-OWN | -0.8618 (0.0216) ** | -0.14603 (0.0007) *** | -0.5033 (0.3737) |
| SSB-COMP * MNG-OWN | -0.0586 (0.4599) | -0.01016 (0.2255) | 0.255665 (0.0636) ** |
| C | 0.2605 (0.0448) ** | 0.0659 (0.0131) *** | 0.7849 (0.0078) *** |
| R-squared | 0.8265 | 0.8809 | 0.7246 |
| Adjusted R-squared | 0.8069 | 0.8371 | 0.6591 |
| F-statistic | 15.8659 | 20.0943 | 11.0546 |
| Prob(F-statistic) | 0.0000 | 0.0000 | 0.0000 |
| Durbin-Watson stat | 2.3659 | 1.8313 | 1.1780 |

Table 3:Regression results, ROE (dependent variable).

*** level of significant at 1 per cent, ** level of significant at 5 per cent, * level of significant at 10 per cent. SSB-REPUT is the reputation of SSB members, SSB-QUAL is the education level of SSB members, SSB-EXPR is the expertise of SSB members, SSB-CRMB is the cross-membership of SSB members, and SSB-COMP is the annual composition of SSB members.

We tested all our hypotheses individually with all three proxies of performance (ROE, ROA and Operational Efficiency). The objective behind individual hypothesis-testing with each proxy of performance was to see how shariah governance and ownership structures affect ROE, ROA, and Operational Efficiency at all levels. The first regression tested all hypotheses in terms of return on equity; the second in terms of return on assets; and the third in terms of Operational Efficiency.

In the above Table 3, ROE is used as the first proxy of performance and results show that both SSB-reputation and SSB-cross membership have a significant impact on the performance of IBs with values of 0.003 and 0.09, respectively. Thus, H1 and H4 are accepted. Institutional ownership also has a significant impact on ROE performance. So, H6 is accepted. Institutional ownership has a

moderating impact of 0.000, 0.0001, and 0.0072 on the relationship between SSB reputation, SSB-expertise, and SSB-cross membership and ROE performance, respectively. Thus, with respect to the moderation effect of institutional ownership, we accept H6 (a), H6 (c) and H6 (d). Managerial ownership has a moderating impact of 0.03, 0.01 and 0.02 on the relationship between SSB-qualification, SSB-expertise and SSB-cross membership and ROE performance, respectively. Thus, H7 (b), H7 (c) and H7 (d) are accepted.

Regression results using ROA as a proxy for IB financial performance indicates that SSB-expertise (0.0000) has a significant impact on ROA performance and thus we accept H3. Both institutional ownership and managerial ownership have a significant impact on ROA performance (0.0004, 0.0001), therefore H6 and H7 are accepted. Results show that institutional ownership only has a moderating relationship between SSB-expertise and ROA performance, and thus H6 (c) is accepted. On the other hand, managerial ownership has a moderating impact of 0.0011, 0.0025, and 0.007 on SSB-qualification, SSB-expertise, SSB-cross membership and ROA performance. Thus H7 (b), H7 (c) and H7 (d) are accepted.

By using Operational Efficiency as a proxy for financial performance, results show that SSB-reputation, SSB-expertise, and managerial ownership have a significant impact. Thus, we accept H1, H3 and H7. Additionally, both control variables (bank age and size) have a significant impact (0.0000, 0.0000) on operational efficiency. The moderation impact on Operational Efficiency of institutional ownership is 0.0000, 0.0015, and 0.0151 for SSB-reputation, SSB-expertise, and SSB-cross membership, respectively. Thus, on the basis of these results, we accept H6 (a), H6 (c), and H6 (d). Further results also show that managerial ownership has moderation influence on SSB-expertise, SSB-composition and Operational Efficiency. Thus, H7 (c) and H7 (d) are accepted.

Conclusion

The main aim of this study is to answer questions about the role of SSBs in the performance of Islamic Banks and the moderation effect of ownership structures. By using a sample of 3 Islamic Banks in Pakistan, this study explored the role of Shariah Supervisory Boards (SSB-size, SSB-reputation, SSB-qualification, SSB-expertise, SSB-cross membership, SSB-composition) and ownership structure (institutional and managerial ownership) in influencing the performance of these banks. In this study, we analysed the above variables with three different proxies of performance (ROE, ROA and Operational Efficiency). Additionally, the impact of shariah governance and ownership structure were also measured to investigate whether they influence a bank's performance. We found that the

reputation of SSBs and institutional ownership have a significant impact on all proxies of performance. Both institutional ownership and managerial ownership only have a moderation impact with regards to the expertise of SSBs on the same three proxies. In terms of ROE, institutional ownership has a moderating impact on SSB-reputation, SSB-expertise and SSB-cross membership, while managerial ownership has a moderating impact on SSB-qualification, SSB-expertise, SSB-cross membership, and SSB-composition. In terms of ROA, institutional ownership has a moderating impact only on SSB expertise, while managerial ownership has a moderating impact on SSB-qualification, SSB-expertise, and SSB-cross membership. In terms of Operational Efficiency, institutional ownership has a moderating impact with regards to SSB-reputation, SSB-expertise, and SSB-cross membership, while managerial ownership has moderation impact on SSB-expertise and SSB-compositions.

Policy Recommendations

Based on our results we propose the following policy recommendations:

- First of all, policymakers should focus more on institutional and managerial owners because they have equity-based investments and can further enhance the performance of IBs in terms of return on equity.
- We also recommend that policymakers rely more on managerial owners for the investment of assets because they have a better understanding of managerial activities that can further enhance performance.
- Shariah Supervisory Boards, as well as institutional and managerial types of ownership, significantly affect the operational efficiency of IBs. Policymakers should give more attention to such elements.

Limitations of the study

This study has limitations in terms of sample size. Due to the complex model of the study, only three Islamic banks in Pakistan were selected. Future studies could benefit from expanding the sample size to include other Islamic countries. This study also limits its scope to two types of ownership structures (institutional and managerial) and does not include other types, such as local ownership and foreign ownership.

Notes

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