FINANCIAL STABILITY AND LIQUIDITY:
EVIDENCE FROM CONVENTIONAL AND ISLAMIC
BANKS IN THE GCC REGION

Doctorial Thesis

Doctor of Business Administration (DBA)

Submitted By

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# TABLE OF CONTENTS

## Contents

DECLARATION................................................................................................................................IV

ACKNOWLEDGEMENTS....................................................................................................................... V

ABSTRACT ....................................................................................................................................... VII

LIST OF TABLES .............................................................................................................................. VIII

LIST OF FIGURES ............................................................................................................................ IX

LIST OF ACRONYMS ......................................................................................................................... X

CHAPTER 1: INTRODUCTION ........................................................................................................... 1

1.1 INTRODUCTION .......................................................................................................................... 1

1.2 BACKGROUND AND MOTIVATION ......................................................................................... 1

1.3 RESEARCH OBJECTIVE ............................................................................................................ 5

1.4 DATA, METHODOLOGY AND RESULTS .................................................................................. 6

1.5 CONTRIBUTIONS AND LIMITATIONS ...................................................................................... 8

1.6 THESIS ORGANISATION AND CONTENTS ............................................................................. 9

1.7 SUMMARY ............................................................................................................................... 10

CHAPTER 2: LITERATURE REVIEW .............................................................................................. 11

2.1 INTRODUCTION ........................................................................................................................ 11

2.2 FINANCIAL STRUCTURE AND STABILITY ............................................................................. 14

2.3 NEW FORMS OF FINANCIAL INSTITUTIONS AND ASSOCIATED RISK .................................. 16

2.4 FINANCIAL INSTABILITY AND SYSTEMIC RISK .................................................................. 22

2.5 LIQUIDITY RISK IN FINANCIAL INSTITUTIONS ................................................................... 25

2.6 BASIC PRINCIPLES OF ISLAMIC BANKING ....................................................................... 33

2.7 FINANCIAL INTERMEDIATION WITHIN ISLAMIC BANKING ............................................ 38

2.8 STRUCTURE OF THE GCC FINANCIAL SYSTEMS ............................................................... 45

2.9 HOW DOES ISLAMIC BANKING RISK DIFFER FROM CONVENTIONAL? ...................... 53

2.10 RISKS SPECIFIC TO ISLAMIC BANKS .................................................................................. 57

2.11 THE GLOBAL FINANCIAL CRISIS ....................................................................................... 58

2.11.1 Contributing macroeconomic factors ............................................................................. 62

2.11.2 Lack of supervision, regulation and market discipline ................................................... 62

2.12 THE RELEVANCE OF ISLAMIC BANKING IN PROMOTING GLOBAL

FINANCIAL STABILITY ................................................................................................................... 67

2.13 SUMMARY ............................................................................................................................... 70
DECLARATION

I hereby certify that the work embodied in this Dissertation Project is the result of original research and has not been submitted for a higher degree to any other University or Institution.

Salwa Shafik
ACKNOWLEDGEMENTS

I would like to express my deepest appreciation to all the individuals who made it possible to complete this thesis. This dissertation would not have been possible without the help of so many people in so many ways.

It is with immense gratitude that I acknowledge the supervision, guidance and support of Professor Abul Shamsuddin throughout my thesis.

My gratitude is also extended to Associate Professor Suzanne Ryan for being an outstanding educator and providing her assistance, advice, and valuable feedback on a preliminary version of this thesis. Also I would like to acknowledge Associate Professor Guilherme Pires for providing his constructive feedback.

I am also grateful to my colleague Dr. Jean-Pierre Fenech (Monash University) for being an extraordinary committee member for my degree and showing me the road towards getting me started on the path to this degree. His enthusiasm, encouragement and faith in me throughout have been extremely helpful. He was always available for my questions and he was positive and gave generously of his time and vast knowledge.

This journey would not have been possible without the help, support and endless patience of my husband, George. He was always there cheering me up and stood by me through the good and more importantly, bad times.
I cannot find words to express my gratitude to my parents, brothers and family. They were always supporting me and encouraging me with their best wishes throughout my journey. In particular, I would like to give my special thanks to my youngest brother, Samer Lahdo, for all his great help in difficult times and my sister in law, Laudy Lahdo, for her constant encouragement and effective comments.

Finally, and most importantly, I wish to thank my three wonderful children, Christopher, Jennifer and Stephanie, who have experienced and shared with me all the highs and lows of this journey - providing me with unending inspiration. Thank you for giving me strength to reach for the stars and chase my dreams. This thesis is dedicated to my three angels for their endless love, support and encouragement.

Thank you, Lord, for always being there for me.
ABSTRACT

This thesis examines the determinants of banks’ financial stability in countries of the Gulf Cooperation Council (GCC). In particular, we estimate empirical models using the Generalized Method of Moments (GMM) to test four hypotheses concerning the determinants of financial stability of conventional and Islamic banks. Our results are as follows: (i) Bank liquidity has a positive effect on its financial stability; and an increase in bank liquidity causes conventional banks in the GCC region to be more financially stable than their Islamic counterparts; (ii) Bank income diversity has a positive effect on its financial stability; (iii) Islamic banks on average are less financially stable than commercial banks; and (iv) The Global Financial Crisis (GFC) had no impact on banks’ financial stability in the GCC region. This study contributes to the academic literature in many different ways. Empirical research into bank financial stability and its determinants in the GCC region appears to be relatively scarce. Therefore, this study contributes to the banking literature by being the first to investigate the impacts of liquidity, income diversity, bank type and the GFC on banks’ financial stability in the GCC region.
LIST OF TABLES

Table 1.1: Research question and hypotheses

Table 2.1: Essential Features of Islamic Finance

Table 2.2: Risk sharing and transfer in both banking systems

Table 2.3: Balance Sheet of an Islamic bank

Table 2.4: Time line of major financial crisis over the years

Table 3.1: Sample selection criteria

Table 3.2: Detailed representation of variables used in the model

Table 3.3: Correlation matrix

Table 3.4: Diagnostic testing statistics

Table 4.1: Summary statistics

Table 4.2: Difference in means of summary statistics

Table 4.3: Regression results – \( LIQ_1 \)

Table 4.4 Regression Results – Dependent variable \( FSI \) with \( LIQ_2 \) and \( LIQ_3 \) as liquidity measures

Table 4.5 Comparing Islamic and conventional banks across different size groups

Table A4.1 Regression Results – \( LIQ_1 \)

Table A4.1 Regression Results – \( LIQ_2 \)
LIST OF FIGURES

Figure 2.1: The boom phase

Figure 2.2: The bust phase

Figure 2.3: GCC Banks Support Package (2008-2009)
# LIST OF ACRONYMS

<table>
<thead>
<tr>
<th>Acronym</th>
<th>Description</th>
</tr>
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<tbody>
<tr>
<td>2SLS</td>
<td>2 Stage Least Squares</td>
</tr>
<tr>
<td>AAOIFI</td>
<td>Accounting and Auditing Organization for Islamic Financial Institutions</td>
</tr>
<tr>
<td>BCBS</td>
<td>Basel Committee on Banking Supervision</td>
</tr>
<tr>
<td>BIS</td>
<td>Bank for International Settlements</td>
</tr>
<tr>
<td>CDS</td>
<td>Credit Default Swap</td>
</tr>
<tr>
<td>CoVAR</td>
<td>Covariance Value-At-Risk Model</td>
</tr>
<tr>
<td>FDI</td>
<td>Foreign Direct Investment</td>
</tr>
<tr>
<td>GCC</td>
<td>Gulf Cooperation Council</td>
</tr>
<tr>
<td>GDP</td>
<td>Gross Domestic Product</td>
</tr>
<tr>
<td>GFC</td>
<td>Global Financial Crisis</td>
</tr>
<tr>
<td>GMM</td>
<td>Generalized Method of Moments</td>
</tr>
<tr>
<td>IAS</td>
<td>International Accounting Standards</td>
</tr>
<tr>
<td>IMF</td>
<td>International Monetary Fund</td>
</tr>
<tr>
<td>IVS</td>
<td>Instrumental Variables</td>
</tr>
<tr>
<td>LLR</td>
<td>Lender of Last Resort</td>
</tr>
<tr>
<td>OLS</td>
<td>Ordinary Least squares</td>
</tr>
</tbody>
</table>
PD  Probability of Default

PLS  Profit-and-Loss Sharing

PSIA  Profit Sharing Investment Account

UAE  United Arab Emirates

VaR  Value-at Risk

VIF  Variance Inflation Factor