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Reasons for the transition of conventional banks to Islamic banking in Bangladesh: Evidence from balance sheets and factor analyses

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Abstract
The study aims to answer the research question of why conventional banks are interested in converting into Islamic banks. The study uses some financial and statistical tools for measuring the financial strength of some selected banks in the scenario of before and after conversion and also measures the perceptions of Bankers and Policymakers that lead to the conversion of the bankers by factor analysis covering the Islamic banks of Bangladesh, which were converted from conventional to Islamic in the era of private commercial banks. The study found a statistically significant difference in performance between the pre-conversion and the post-conversion scenarios of the selected banks based on different financial ratios like Profitability Ratios, Liquidity Ratios, Risk and solvency ratios and Efficiency ratios. However, the results have indicated that higher capitalization, lower credit risk, higher profitability, and significant market share from conversion are the main reasons for converting to the Islamic system rather than religious obligations.

Keywords Conversion, Conventional, Islamic, Bank, Profitability.

Paper type Research paper

Introduction
Islamic banking is based on moral values. Moral value is derived from the Shariah principles. Islam is a complete code of life, and the Quran is humanity's main guideline. The Holy Quran strictly prohibits transactions that are related to interest. Here, interest means anything, money or other things, which is taken extra with the principal amount and in fixed form. Islamic banking operations are wholly free from interest, whereas conventional banking operations are based on interest-based. From independence till 1983, the banking system was thoroughly captivated by the conventional banking system. Bangladesh entered the Islamic banking system in 1983 with the establishment of Islamic Bank Bangladesh Ltd. Currently, eight full-fledged Islamic banks

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and 825 Islamic banking branches of conventional banks have been operating (Bangladesh Bank Source).

Among eight Islamic banks, three Islamic banks were converted from the conventional banking system. The Islamic banking system is becoming popular in Bangladesh. It may be due to its intrinsic value, well and unique banking services, ethical issues, and the large Muslim population. The first conversion tendency took place in the Middle East with the conversion of the National Bank of Sharjah to Sharjah Islami Bank in 2002. After that, many banks converted into Islamic banks like NCB (Saudi Arabia), Emirates Islamic Bank, Dubai Islamic Bank, Khyber Bank (Pakistan) Kuwait International Bank. Most conventional banks like IFIC Bank Ltd., NCC Bank Ltd., and South East Bank ltd are becoming interested in converting their conventional banking system to an Islamic one. Bangladesh Bank (Central Bank of Bangladesh) is not, however, allowing banks to be converted to Islamic banking because of not have a central Sharia council to regulate this particular brand of banking. The question is here, What for conventional banks want to be convert their conventional banking system into an Islamic banking system? The study aims to highlight the reasons behind the conversion of the banking system. The study highlights the reasons for transition from two viewpoints. One is financial performance and the other is manager's and expert's perception. The study has conducted based on data from two banks. A structured questionnaire was distributed to the senior incumbents in these banks to collect their views and analyzed data by using ration analysis and by factor analysis.

1. Literature review

Iqbal(2001) evaluated the performance of twelve Islamic and twelve conventional banks worldwide by using trend and ratio analysis from 1990 to 1998 and found that Islamic banks are well-capitalized, profitable, and more stable than conventional but not cost-effective.

Zoubi and Olson(2007) measured financial characteristics of banking industry in the GCC region from Islamic vs. conventional point of view by using 16 financial ratios. They found that, on average, Islamic banks are more profitable than conventional banks; Islamic banks hold more cash to avoid the risk of withdrawal deposits and maintain lower provisions for loan losses.

Mahmud and Rahman(2020) compared conventional banks with Islamic Banks Bangladesh Limited by using some ratio analysis and found that the overall performance of Islamic Bank Bangladesh Limited is better than conventional banks.

Safiullah(2010) emphasized the financial performance of both Islamic and

conventional banks to draw a comparison. Using data from 2004 to 2008 on four Islamic and four conventional banks found that Islamic banks are superior to conventional banks in terms of business development, liquidity, profitability, and solvency.

Viverita(2011) used three financial efficiency ratios (cost efficiency ratio, revenue efficiency, and profit efficiency ratio) to compare conventional banks and Islamic banks from 2004 to 2008. T-test and F-test were used to check the significant difference and found that Islamic banks are cost-efficient and generate more revenue and profit than conventional banks.

Hamid and Azmi(2011) examined the financial performance of Islamic banks compared with conventional banks from 2000 to 2009. Using T-tests, they found that Bank Islam Malaysia Behad is relatively more liquid and less risky than conventional banks.

Ika and Abdullah(2011) compared and examined the financial performance of Islamic and conventional banks in Indonesia from 2000 to 2007. They found that the Islamic banks of Indonesia are more liquid than conventional banks. They also identified that consumers' awareness of Islamic products is deficient in

Indonesia.

Kouser, Aamir, Mehvish, and Azeem(2011) investigated financial performance between Islamic banking and conventional banking in Pakistan using the CAMEL model from 2006 to 2010. They revealed that Islamic banks were not performing at the level of conventional banks because of the branch size of Islamic banks and suggested that there is a need for awareness of Islamic financing and products and that the Government should also adopt friendly policies on the Islamic economic system.

Masruki, Ibrahim, Osman, and Wahab (2011) analyzed and compared Islamic banks and conventional banks in Malaysia over five years (2004-2008) and found that in terms of profitability, Islamic banks are less than conventional banks, but in terms of credit risk, conventional banks are higher riskier than Islamic banks. They argued that for higher net financing and asset quality, conventional banks are more profitable than Islamic banks.

Alani(2012) examined why traditional banks were motivated to convert to the Islamic banking system. Their study highlighted the recent success of Islamic banks that converted from the traditional model and found that the low-risk nature and higher profitability are the motivational factors to be converted into Islamic banking.

Siraj(2012) used some performance indicators to compare conventional and Islamic banking in the GCC region during 2005-2010. They found that Islamic banks are more equity-financed than conventional banks. They also

performed an ANOVA analysis and found that in terms of operating profit, profit as a percentage of deposits, profit as a percentage of total liabilities, and total equity as a percentage of total assets, there is a significant difference between Islamic banks and conventional banks.

Quresh, and Rehman(2012) compared the consumers' perceptions of Islamic banking and conventional banking in Pakistan. Based on feedback from 341 respondents regarding their perceptions and by using the Likert scale, they found that transparency in transactions, practice of Islamic law and principles in transaction, ethical behavior of employees ,low service charges, and speedy transactions are the main factors of preferring the Islamic Banking System over the conventional banking system.

Elsiefy(2013) measured the performance of Qatari Islamic Banks, during, and after the financial crisis showed that Islamic banks of Qatar are more efficient, more capitalized, less leveraged, and maintain more robust total assets and more substantial deposits growth than conventional banks in pre and post-crisis.

Fayed(2013) compared the performance of conventional and Islamic banking in Egypt from 2008 to 2010 using seven financial ratios. In the study, Islamic banks were found to have a leading position in solvency, whereas conventional banks were in profitability, liquidity, and credit risk management.

From the reviewed literature it is found that almost all the studies compared the performance of Islamic banking with conventional banking by considering different sample banks from two categories where the results were mixed in nature. No studies were found where the same samples were used to compare the performance before and after conversion which is the most attractive point of the study. Moreover, all the studies concentrated on the information from the balance sheet rather than balance sheet information, there may have been some off-balance sheet reasons for conversion which were ignored in the previous studies and that motivated me to conduct the study.

The objective of the study

The objective of this study is to answer the research question of why conventional banks are interested to be converted into Islamic banks.

Methodology of the study

The study was conducted based on two Islamic banks (converted from conventional mode) out of three converted Islamic Banks at the time of research conduction. Secondary data have been collected on relevant

variables from different financial statements (balance sheets) of the sampled banks and a financial comparison has been made through the ratio analysis. Primary data have been collected from the top management of interested banks which have been waiting to be converted from the conventional to the Islamic banking system and from the industry experts by using a structured questionnaire to analyze them by using Factor Analysis. Financial data have been collected for ten years (five years before conversation and five years after conversion) from First Security Islami Bank Ltd. and for nine years (four years before conversation and five years after conversion) from EXIM bank Ltd. Both ratio analysis and factor analysis have been used for analyzing data.

Ratio analysis

Earlier studies in the literature review used the following ratios to measure the financial performance of both conventional and Islamic banks.

a. Profitability ratios

A bank's profitability means how it generates net profit by efficiently managing its operational activities. Most of the earlier studies used the following ratios to measure the profitability of a bank:

i. Return on assets (ROA)

Return on assets measures the net profit by using per unit of asset. It also measures the contribution of total assets to the net profit. A higher ratio indicates higher profitability of the bank.

ROA = Net Profit after tax / Total assets

ii. Return on equity (ROE)

Return on equity measures the net profit after tax as a percentage of total equity invested. In investing, bank investors justify ROE because it measures the capability of the bank to use owners' equity to generate a net profit. A higher ratio indicates higher profitability of the bank.

ROE = Net Profit after tax / Total Equity

b. Liquidity ratios

In the banking sector, liquidity is a vital factor in justifying bank performance because a bank always deals with borrowed and invested funds. A bank's liquidity defines the capability of fulfilling the demands of actual and potential customers. Previous research used the following ratios to measure the liquidity of the bank:

i. Loan to deposits ratio

The ratio measures the percentage of total loans embedded with total

deposits. Usually, the bank provides a portion of funds from total deposits as loans. So, the higher the ratio indicates, the higher the bank's liquidity risk.

LTD = Total Loans / Total Deposits

ii. Cash and cash equivalent assets to total liabilities

Cash and cash equivalent assets to total liabilities

The ratio measures the liquidity position of the bank. It indicates liquid assets to meet the per-dollar liability. The higher value of this ratio indicates the higher liquid position of the bank.

CTL = Cash and cash equivalent assets / Total liabilities

c. Risk and solvency ratios

i. Total equity to Net loans

The ratio measures the capability of bearing losses from loans. The higher value of this ratio indicates a lower credit risk.

LTD = Total Equity / net Loans

ii. Equity multiplier

This ratio indicates the total assets as a percentage of total equity. It measures the financial leverage of the bank. The higher value of this ratio indicates the higher financial leverage of the bank.

EM = Total assets / Total equity

d. Efficiency ratios

i. Asset management

It measures the capability of total assets to generate operating income. A higher ratio indicates the efficient management of assets by the bank.

AM = Operating Income / Total Assets

ii. Cost-income ratio

Here this ratio has been used as a proxy for the bank's operational efficiency. The ratio indicates the efficient management of operating expenses to generate operating income. A lower value of this ratio indicates a better performance of the bank.

CIR = O capital operating Income / Operating Expense

e. Factor analysis

Factor analysis is a statistical technique that reduces a set of variables by extracting all their commonalities into a smaller number of factors. It can also be called data reduction. When observing vast numbers of variables, some common patterns emerge, which are known as factors.

2. Analysis

Comparison by Ratio analysis (Pre and post-conversion)

The following tables show the results of ratio analysis under four categories. Standard deviation, maximum and minimum values are based on overall (pre- and post-conversion), where mean scores have been calculated separately for pre- and post-conversion periods.

a. Profitability ratios

i. Return on assets (ROA)

EXIM Bank Ltd.

Year	2000	2001	2002	2003	Mean	2004	2005	2006	2007	2008	Mean	SD	Max	Min
ROA	1.12	1.97	2.53	2.07	1.92	1.57	1.65	1.56	1.81	1.60	1.64	0.40	2.53	1.12
Growth (%)		75.77	28.73	-18.12	28.79	-24.16	5.07	-5.53	16.16	-11.35	-3.96			

The above table shows that according to return on assets (ROA), the average ROA (1.92%) of EXIM bank ltd. It was in a better position in the pre-conversion period than the post-conversion average ROA (1.64%). It indicates the profitability of EXIM bank ltd. It was well before converting from a conventional banking system to an Islamic one. The overall ROA of EXIM bank ltd. in both pre and post-conversion periods varies from 1.12% to 2.53%. Furthermore, the maximum ROA was in the pre-conversion period (ROA= 2.53% in 2002). The average growth rate of ROA of EXIM bank ltd. Itwas 28.79% in the pre-conversion period, but after conversion, the growth was reduced to -3.96% that indicated that EXIM was losing profitability after the conversion from the conventional banking system to the Islamic banking system.

First Security Islami Bank Ltd.

Year	2004	2005	2006	2007	2008	Mean	2009	2010	2011	2012	2013	Mean	SD	Max	Min
ROA	0.63	0.05	-0.57	0.11	0.33	0.11	0.68	0.86	0.64	0.59	0.48	0.65	0.42	0.86	-0.57
Growth (%)		-92.06	-1240	119.3	200	-253.19	106.06	26.58	-26.1	-7.84	-19.07	19.74			

From the above table, it is seen that according to return on assets (ROA), the average ROA (0.65%) of FSIBL was in a better position in the post-conversion period compared to the pre-conversion average ROA (0.11%). It indicates that the profitability of FSIBL was well after converting from the conventional banking system. The overall ROA of FSIBL in both pre and post-conversion periods varies from -0.57% to 0.86%. Furthermore, the maximum ROA was in the post-conversion period (ROA= 0.86% in 2010). The average growth rate of ROA of FSIBL was negative (-253.19%) in the pre-conversion period. However, the negative trend was reduced after

conversion from the conventional to the Islamic banking system (Average ROA growth was 19.74%).

ii. Return on equity (ROE)

EXIM Bank Ltd.

Year	2000	2001	2002	2003	Mean	2004	2005	2006	2007	2008	Mean	SD	Max	Min
ROE	16.22	34.21	36.53	34.05	30.25	27.27	29.04	20.90	23.03	21.98	24.44	6.99	36.53	16.22
Growth (%)		110.92	6.78	-6.80	36.97	-19.91	6.48	-28.03	10.18	-4.54	-7.16			

The above table shows that , for EXIM bank, according to return on equity (ROE), the average ROE was 30.25% in the pre-conversion period which was 24.44%) in the post-conversion period which indicated that the profitability of EXIM bank was better before converting from a conventional banking system to an Islamic one. The overall ROE of EXIM Bank Ltd. In both pre and post-conversion periods varies from 16.22% to 36.53%. Furthermore, the maximum ROE was in the pre-conversion period (ROE= 36.53% in 2000). The average growth rate of ROE of EXIM bank was 36.97%, but the growth was reduced after the conversion period (Average ROE growth was -7.16%).

First Security Islami Bank Ltd.

Year	2004	2005	2006	2007	2008	Mean	2009	2010	2011	2012	2013	Mean	SD	Max	Min
ROE	19.11	1.2	-11.68	2.7	4.11	3.09	11.41	13.99	12.75	13.45	11.95	12.71	8.92	19.11	-11.68
Growth (%)		-93.7	-1069.52	-123.12	52.12	-308.55	177.62	22.69	-8.9	5.5	-11.12	37.16			

From the above table, it is seen that according to return on equity (ROE), the average ROE (12.71%) of FSIBL was in a better position in the post-conversion period compared to the pre-conversion average ROE (3.09%). It also indicates that the profitability of FSIBL is well after converting from the conventional banking system. The overall ROE of FSIBL in both pre and post-conversion periods varies from -11.68% to 19.11%. Moreover, the maximum ROE was in the pre-conversion period (ROE= 19.11% in 2004). The average growth rate of the ROE of FSIBL was negative (-308.55%), but the negative growth trend was reduced after the conversion period (Average ROE growth was 37.16%).

b. Liquidity ratios

i. Loan to deposits ratio

Year	2000	2001	2002	2003	Mean	2004	2005	2006	2007	2008	Mean	SD	Max	Min
LTD	55.75	70.65	79.98	80.62	71.75	27.27	101.33	91.97	93.18	96.75	93.14	14.54	101.33	55.75
Growth (%)		26.72	13.22	0.80	13.58	-66.17	271.57	-9.24	1.31	3.83	53.50			

EXIM Bank Ltd.

From the above table, it is seen that according to the loan to deposits ratio (LTD), the average LTD of EXIM bank was 93.14% in the post-conversion period compared to the pre-conversion average LTD (71.75%). It indicates that EXIM bank was in a risky position in terms of liquidity after the conversion from the conventional banking system. Overall LTD of EXIM bank,both pre and post-conversion periods, varies from 55.75% to 101.33%. And the maximum LTD was in post-conversion period (LTD= 101.33% in 2005). The average growth rate of LTD of EXIM bank was 13.58%, but the trend of growth has increased after the conversion(average LTD growth was 53.50%). It is also a negative sign for EXIM bank to be converted from a conventional system to an Islamic.

First Security Islami Bank Ltd.

Year	2004	2005	2006	2007	2008	Mean	2009	2010	2011	2012	2013	Mean	SD	Max	Min
LTD	75.68	76.52	77.57	79.33	90.50	79.92	85.08	85.38	83.43	87.62	82.14	84.73	4.97	90.50	75.68
Growth (%)		1.11	1.37	2.27	14.08	4.71	-5.99	0.35	-2.29	5.03	-6.26	-1.83			

From the above table, it is seen that according to the loan to deposits ratio (LTD), the average LTD of FSIBL was 84.73% in the post-conversion period compared to the pre-conversion average LTD (79.92%). It indicates that FSIBL was in a risky position in terms of liquidity after the conversion from the conventional banking system. Overall LTD of FSIBL in both pre and post-conversion periods varies from 75.68% to 90.50%. Furthermore, the maximum LTD was in the pre-conversion period (LTD= 90.50% in 2008). The average growth rate of LTD of FSIBL was 4.71%, but the growth trend reduced after the conversion period (Average LTD growth was -1.83%). It was also a positive sign to FSIBL for converting from a conventional system to an Islamic one.

ii. Cash and cash equivalent assets to total liabilities

EXIM Bank Ltd.

Year	2000	2001	2002	2003	Mean	2004	2005	2006	2007	2008	Mean	SD	Max	Min
CTL	32.53	23.15	14.01	14.14	20.96	10.55	14.58	12.25	12.45	13.84	12.73	7.02	32.53	10.55
Growth (%)		-28.85	-39.48	0.93	-22.47	-25.39	38.22	-15.96	1.62	11.16	1.93			

From the above table, it is seen that according to cash and cash equivalent assets to total liabilities, the average CTL of EXIM bank was 20.96% in the pre-conversion period compared to the post-conversion average CTL (12.73%) which has indicated that EXIM bank has maintained higher liquidity in the pre-conversion period compared to the post-conversion period. Overall CTL of EXIM bank ltd. in both pre and post-conversion periods varies from 10.55% to 32.53%. Moreover, the maximum CTL was in the pre-conversion period (CTL= 32.53% in 2000). The average growth rate of CTL of EXIM bank was -22.47%, but the trend of growth increased after conversion from the conventional banking system (Average CTL growth was 1.93%).

First Security Islami Bank Ltd.

Year	2004	2005	2006	2007	2008	Mean	2009	2010	2011	2012	2013	Mean	SD	Max	Min
Cast to TL	27.88	16.39	28.85	25.53	12.19	22.17	12.78	9.68	14.86	17.19	16.69	14.24	6.80	28.85	9.68
Growth (%)		-41.20	75.98	-11.50	-52.27	-7.25	124.45	-24.25	53.49	15.69	-2.93	33.29			

The above table shows that according to cash and cash equivalent assets to total liabilities, the average CTL of FSIBL was 22.17% in the pre-conversion period compared to the post-conversion average CTL (14.24%). It indicates that FSIBL maintained higher liquidity in the pre-conversion period compared to the post-conversion period. Overall CTL of FSIBL in both pre and post-conversion periods varies from 9.68% to 28.85%. Furthermore, the maximum CTL was in the pre-conversion period (CTL= 28.85% in 2006). The average growth rate of CTL of FSIBL was -7.25%, but the growth trend increased after the conversion period (Average CTL growth was 33.29%).

Risk and solvency ratios

i. Total equity to net loans

EXIM Bank Ltd.

Year	2000	2001	2002	2003	Mean	2004	2005	2006	2007	2008	Mean	SD	Max	Min
CR	13.67	9.00	6.93	6.09	8.92	7.24	7.34	9.53	10.06	9.30	8.69	2.28	13.67	6.09
Growth (%)		-34.15	-23.01	-12.15	-23.10	18.88	1.39	29.84	5.50	-7.51	9.62			

The above table shows that according to total equity to net loans, which measures credit risk, the average CR of EXIM bank was 8.92% in the pre-conversion period compared to the post-conversion average CR (8.69%) which indicates that the credit risk of EXIM bank was lower in the pre-conversion period compared to the post-conversion period because the higher value of this ratio indicates lower credit risk. EXIM bank ltd. in both pre and post-conversion periods varies from 6.09% to 13.67%.

Furthermore, the maximum CR was in the pre-conversion period (CR= 13.67% in 2000). The average growth rate of CR of EXIM bank was -23.10% in the pre-conversion period, but the growth trend increased after the conversion period (Average CR growth was 9.62%) which indicates that the credit risk of EXIM bank has been decreased after the conversion from the conventional banking system to the Islamic banking system.

First Security Islami Bank Ltd.

Year	2004	2005	2006	2007	2008	Mean	2009	2010	2011	2012	2013	Mean	SD	Max	Min
TE to NL	6.25	7.66	7.35	6.08	10.96	7.66	8.05	8.23	7.06	5.88	5.61	6.97	1.58	10.96	5.61
Growth (%)		22.56	-3.93	-17.29	80.14	20.37	-26.55	2.28	-14.22	-16.66	-4.56	-11.94			

The above table shows that according to total equity to net loans, which measures credit risk, the average CR of FSIBL was 7.66% in the pre-conversion period compared to the post-conversion average CR (6.97%). It indicates that the credit risk of FSIBL was lower in the pre-conversion period compared to the post-conversion period because the higher value of this ratio indicates lower credit risk. Overall CR of FSIBL in both pre and post-conversion periods varies from 5.61% to 10.96%. Moreover, the maximum CR was in the pre-conversion period (CR= 10.96% in 2008). The average growth rate of CR of FSIBL was 20.37% in the pre-conversion period, but the growth trend reduced after the conversion period (Average CR growth was -11.94%). It also indicates that the credit risk of FSIBL increased after the conversion from the conventional banking system to the Islamic banking system.

ii. Equity multiplier

EXIM Bank Ltd.

Year	2000	2001	2002	2003	Mean	2004	2005	2006	2007	2008	Mean	SD	Max	Min
EM	14.49	17.39	14.43	16.42	15.68	17.40	17.63	13.43	12.74	13.72	14.98	1.92	17.63	12.74
Growth (%)		20.01	-17.02	13.79	5.59	5.97	1.32	-23.82	-5.14	7.69	-3.80			

From the above table, it is seen that according to the equity multiplier, which measures solvency, the average EM of EXIM bank was 15.68 in the pre-conversion period compared to the post-conversion average EM of 14.98 which indicates that the solvency of EXIM bank was lower in the pre-conversion period than the post-conversion period because the higher value of this ratio indicates a higher dependency on debt to finance assets than equity. The average EM of EXIM bank in both pre and post-conversion periods varies from 12.74 times to 17.63 times.

Furthermore, the maximum EM was achieved in the post-conversion period (EM= 17.63 times in 2005). The average growth rate of EM of EXIM bank was 5.59% in the pre-conversion period, but the growth trend was reduced after the conversion period (Average EM growth was -3.80%). It also indicated that EXIM bank was relying more on total equity to finance assets than debt after the conversion from the conventional banking system to the Islamic banking system.

First Security Islami Bank Ltd.

Year	2004	2005	2006	2007	2008	Mean	2009	2010	2011	2012	2013	Mean	SD	Max	Min
EM	30.45	24.68	20.37	23.75	12.31	22.31	16.74	16.23	20.01	22.90	25.15	20.21	5.25	30.45	12.31
Growth (%)		-18.95	-17.45	16.58	-48.19	-17.00	35.99	-3.07	23.28	14.47	9.82	16.10			

From the above table, it is seen that according to the equity multiplier, which measures solvency, the average EM of FSIBL was 22.31 times in the pre-conversion period compared to the post-conversion average EM (20.21 times). As with EXIM bank ltd, the solvency of FSIBL was lower in the pre-conversion period compared to the post-conversion period. The overall EM of FSIBL in both pre and post-conversion periods varies from 12.31 to 30.45 times. Furthermore, the maximum EM was in the pre-conversion period (EM= 30.45 times in 2004). The average growth rate of EM of FSIBL was -17.00% in the pre-conversion period, but the growth trend increased after the conversion period (Average EM growth was 16.10%).

c. Efficiency ratios

i. Asset management (AM)

EXIM Bank Ltd.

Year	2000	2001	2002	2003	Mean	2004	2005	2006	2007	2008	Mean	SD	Max	Min
AM	4.36	5.22	7.39	6.84	5.95	4.97	4.78	11.89	12.44	12.21	9.26	3.43	12.44	4.36
Growth (%)		19.85	41.62	-7.49	17.99	-27.34	-3.90	148.67	4.68	-1.87	24.05			

From the above table, it is seen that according to assets management, the average AM of EXIM bank ltd. It was 9.26% in the post-conversion period compared to the pre-conversion average AM (5.95%). It indicates the assets management efficiency of EXIM bank ltd. It was good after the conversion from the conventional banking system to the Islamic one. EXIM bank ltd. in both pre and post-conversion periods varies from 4.36% to 12.44%. Furthermore, the maximum AM was in the post-conversion period (AM= 12.44% in 2007). The average growth rate of AM of EXIM bank ltd. It was 17.99% in the pre-conversion period, and the growth trend increased after the conversion period (Average AM growth was 24.05%).

First Security Islami Bank Ltd.

Year	2004	2005	2006	2007	2008	Mean	2009	2010	2011	2012	2013	Mean	SD	Max	Min
AM	3.66	1.61	2.06	1.54	1.83	2.14	2.77	3.28	3.01	2.88	2.72	2.93	0.73	3.66	1.54
Growth (%)		-56.05	28.32	-25.44	19.17	-8.50	51.37	18.45	-8.21	-4.32	-5.34	10.39			

The above table shows that according to assets management, the average AM of FSIBL was 2.93% in the post-conversion period compared to the pre-conversion average AM (2.14%). It indicates that the assets management efficiency of FSIBL was good after the conversion from the conventional banking system to the Islamic banking system. Overall AM of FSIBL in both pre and post-conversion periods varies from 1.54% to 3.66%. Moreover, the maximum AM was in the pre-conversion period (AM= 3.66% in 2004). The average growth rate of AM of FSIBL was -8.50% in the pre-conversion period, but the growth trend increased after the conversion period (Average AM growth was 10.39%).

ii. Cost income ratio

EXIM Bank Ltd.

Year	2000	2001	2002	2003	Mean	2004	2005	2006	2007	2008	Mean	SD	Max	Min
CIR	2.14	2.88	2.92	3.02	2.74	3.23	3.70	1.10	1.79	1.43	2.25	0.89	3.70	1.10
Growth (%)		34.80	1.42	3.55	13.26	6.95	14.65	-70.15	61.74	-19.83	-1.33			

From the above table, it is seen that according to the cost-income ratio, the average CIR of EXIM bank was 2.74% in the pre-conversion period compared to the post-conversion average CIR (2.25%) which indicates that the cost efficiency of EXIM bank was good after the conversion from the conventional banking system to the Islamic banking system. Because the lower value of this ratio indicates better cost efficiency. Overall CIR of

EXIM bank ltd. in both pre and post-conversion periods varies from 1.10% to 3.70%. And the maximum and minimum CIR were in the post-conversion period (CIR= 3.70% in 2005 and CIR= 1.10% in 2006). The average growth rate of CIR of EXIM bank ltd. It was 13.26% in the pre-conversion period, but the growth trend is decreased after the conversion period (Average CIR growth was -1.33%).

First Security Islami Bank Ltd.

Year	2004	2005	2006	2007	2008	Mean	2009	2010	2011	2012	2013	Mean	SD	Max	Min
CIR	2.85	1.62	1.92	1.45	1.49	1.87	2.30	2.37	2.38	2.08	1.85	2.20	0.45	2.85	1.45
Growth (%)		-42.93	18.46	-24.66	3.13	-11.50	54.36	2.76	0.79	-12.61	-11.21	6.82			

The above table shows that according to the cost-income ratio, the average CIR of FSIBL was 2.20% in the post-conversion period compared to the pre-conversion average CIR (1.87%). It indicates that the cost efficiency of FSIBL was good before conversion from the conventional banking system to the Islamic banking system. Overall CIR of FSIBL in both pre and post-conversion periods varies from 1.45% to 2.85%. Furthermore, the maximum and minimum CIR were in the pre-conversion period (CIR= 2.85% in 2004 and CIR= 1.45% in 2007). The average growth rate of CIR of FSIBL was -11.50% in the pre-conversion period, but the growth trend was increased after the conversion period (Average CIR growth was 6.82%).

Overall financial performance of Islamic banks in both the pre and post-conversion period

Category		EXIM bank Ltd.		First Security Islami Bank Ltd. (FSIBL)	
		Pre-conversion (Mean)	Post-conversion (Mean)	Pre-conversion (Mean)	Post-conversion (Mean)
A. Profitability	ROA	1.92	1.64	0.11	0.65
	ROE	30.25	24.44	3.09	12.71
B. Liquidity	LTD	71.75	93.14	79.92	84.73
	CTL	20.96	12.73	22.17	14.24
C. Risk Solvency	CR	8.92	8.69	7.66	6.97
	EM	15.68	14.98	22.31	20.21
D. Efficiency	AM	5.95	9.26	2.14	2.93
	CIR	2.74	2.25	1.87	2.20

The above table indicates the overall average financial performance of Islamic banks (EXIM bank Ltd. and First Security Islami Bank Ltd.) converted from conventional to Islamic banking. In terms of profitability measured by the return on assets and equity, only FSIBL was in a better position after converting from the conventional banking system to the

Islamic banking system. The e ROA after conversion is 0.65%, whereas ROA before the conversion was 0.11%, 12.71% (after conversion) compared to 3.09% (before conversion) of FSIBL. For EXIM bank, ROA and ROE were decreased (before conversion, ROA was 1.92% compared to after conversion ROA 1.64%, and before conversion, ROE was 30.25% compared to after conversion ROE 24.44%).

In terms of liquidity position measured by the loan to total deposits and cash & cash equivalent to total liabilities, both banks (EXIM bank and FSIBL) were in a better position in the pre-conversion period. Liquidity risk of EXIM bank was increased after the conversion (LTD= 93.14the %) compared to pre-conversion (the LTD= 71.75%) and also EXIM bank ltd. held higher liquid assets in the pre-conversion period (CTL= 20.96%) compared to post-conversion (CTL= 12.73%). The liquidity risk of FSIBL increased after the conversion (LTD= 84.73%) compared to pre-the conversion (LTD= 79.92%) and FSIBL held higher liquid assets in the pre-conversion period (CTL= 22.17%) compared to post-conversion (CTL= 14.24%).

On the side of credit risk and solvency measured by the total equity to net loans and total assets to total equity, both banks (EXIM bank ltd. and FSIBL) are in a better position in the post-conversion period. Credit risk of EXIM bank ltd. decreased in the post-conversion period (CR= 8.69%) compared to pre-conversion (CR= 8.92%) and the equity multiplier decreased in the post-conversion period (EM= 14.98 times) compared to pre-conversion (EM= 15.68 times). Credit risk of FSIBL decreased in the post-conversion period (CR= 6.97%) compared to pre-conversion (CR= 7.66%) and the equity multiplier decreased in the post-conversion period (EM= 20.21 times) compared to pre-conversion (EM= 22.31 times).

In terms of efficiency that was measured by the assets management ratio and cost-income ratio, both of the banks (EXIM bank ltd. and FSIBL) were in a better position in the post-conversion period except FSIBL in cost-income ratio. Assets management ratio of EXIM bank ltd. increased in the post-conversion period (AM= 9.26%) compared to pre-conversion (5.95%) and the cost-income ratio decreased in the post-conversion period (CIR= 2.25%) compared to pre-conversion (CIR= 2.74%). The assets management ratio of FSIBL increased in the post-conversion period (AM= 2.93%) compared to the pre-conversion period (AM= 2.14%). However, regarding the cost-income ratio, FSIBL was in a better position in the pre-conversion period as CIR vary from 1.87% to 2.20% (lower CIR indicates better position).

Managers' and experts' perceptions regarding conversion (By factor analysis)

Data have been collected from 196 respondents,sample managers and experts opinions, on the 5 points Likert Scale to identify the reasons for conversion from the conventional to the Islamic banking system. Varimax Rotated Factor Analytical techniques have been employed for grouping the variables based on their inherent relationship and ranking the group based on their magnitudes. The study has identified the variables undertaken for the study as most significant, significant, and insignificant based on the mean score of opinions taken from 5 points Likert scale.

Reasons for conversion from Conventional banking system to Islamic banking system based on mean Weighted Scores.

In the table-1, it is seen that getting the benefit of bank reserve and seeing the success of Islamic Banks in the global market as the most significant reasons of convertion from conventional to the Islamic banking system. It has also identified eleven variables as significant for converting. These are to cope with market share in the banking industry of Bangladesh; to make more profit because the Islamic banking system allows the participation of banks and clients in the business; lower cost of raising fund; customers demand of Islamic products and services which are not available in conventional banking, to get the Govt. support by believing on religious faith, most of the population belief Islam from their heart, by seeing the success of Islamic Banks in Bangladesh, profit is not predetermined because of the profit-loss sharing mode, more careful evaluation of investment demand and lower price of ancillary services of Islamic banks hence attract more customers. The study also found three variables as insignificant, which were :one, getting more deposits because most of the population is Muslim and wants to keep their wealth in the interest-free bank, two ,safety of customers fund because Islamic banks run activities under Islamic rule and ,third, Islamic products are less riskier than conventional banking products.

Table 1
Reasons based on mean Weighted Scores

ID No.	Variables	Weighted Mean Score
More Significant		
X_8	To get the benefit of bank reserve	4.16
X_{16}	Seeing the success of Islamic Banks in the global market	4.01
Significant		
X_{11}	To cope with market share in the banking industry of Bangladesh	3.99
X_{10}	To make more profit because the Islamic banking system allows the participation of banks and clients in the business	3.90
X_{13}	Low cost of fundraising	3.88
X_2	Customers demand Islamic products and services which are not available in conventional banking	3.79
X_{12}	To get the Govt. support	3.70
X_1	By believing in religious faith	3.71
X_5	Most of the population believes Islam from their heart. Hence, they prefer Islamic banking	3.67
X_7	Seeing the success of Islamic Banks in Bangladesh	3.66
X_{15}	Profit is not predetermined because of the profit loss-sharing mode	3.64
X_6	More careful evaluation of Investment Demand	3.60
X_{14}	Low cost of ancillary services of Islamic banks and hence attract more customer	3.59
Insignificant		
X_9	To get more deposits because most of the population is Muslim and want to keep their wealth in the interest-free bank	3.56
X_4	Ensure the safety of customers because Islamic banks run activities under Islamic rule	3.51
X_3	Islamic products are less risky than conventional banking products	3.04

Analysis of correlation matrix

From the zero-order correlation matrix of 16 variables (See Appendix-1), it has been found that some variables are the most significant factors. In the case of variable X_9 it has been found to be highly correlated with variables X_4, X_5, and X_6 at a 5% significance level. Variable X_{10} is highly correlated with X_4 and X_6 at a 5% significance level. Variable X_{14} is also highly correlated with X_1 and X_8 at a 5% significance level. Variables X_5 and X_7 are highly correlated with X_4 at a 5% significance level. Finally, variable X_{11} with X_8 and variable X_{12} with X_2 are highly correlated at the 1% significance level.

Principal component analysis

An examination of Eigenvalues has led to the retention of 7 factors (See Appendix 2). These factors have accounted for 9.077%, 8.528%, 8.387%, 7.824%, 7.823%, 7.531%, and 7.203% of the variation. This implies that the total variance accounted for by all seven factors is 56.374% and the remaining variance is explained by other factors.

Analysis of factors

Factor 1

ID No.	Variables	Factor Loading
X_{14}	Low cost of ancillary services of Islamic banks and hence attract more customer	.635
X_{1}	By believing in religious faith	.621
X_{8}	To get the benefit of bank reserve	.486
X_{16}	Seeing the success of Islamic Banks in the global market	.466
	Variance accounted for	9.077%

Factor-1 explains 9.077% of the total variations existing in the variable set. This includes variables: X_{14}, X_{1}, X_{8}, and X_{16}. In this factor, four more significant variables formed a cluster. Except for the X_{1} variable, all variables are market-oriented reasons. Only the X_{1} variable is a religious reason for converting.

Factor 2

ID No.	Variables	Factor Loading
X_{6}	More careful evaluation of investment demand	.703
X_{10}	To make more profit because the Islamic banking system allows the participation of banks and clients in the business	.591
	Variance accounted for	8.528%

Factor 2 explains 8.528% of the total variations existing in the variable set. This includes variables: X_{6} and X_{10}. This factor has two significant variables. Variable X_{10} is a market-oriented reason and X_{6} is a religious reason.

Factor 3

ID No.	Variables	Factor Loading
X_{11}	To cope with market share in the banking industry of Bangladesh	.782
X_{15}	Profit is not predetermined because of the profit loss-sharing mode	.480
	Variance accounted for	8.387%

Factor-3 explains 8.387% of the total variations existing in the variable set. This includes variables: X_{11} and X_{15}. This factor also has significant variables

which formed a cluster and both of them are market-oriented reasons to be converted from conventional to the Islamic banking system.

Factor 4

ID No.	Variables	Factor Loading
X_2	Customers demand Islamic products and services which are not available in c onventional banking	.813
X_{12}	To get the Govt. support	.520
	Variance accounted for	7.824%

Factor 4 explains 7.824 % of the total variations existing in the variable set. This includes variables: X_2 and X_{12}. This factor has significant variables which form a cluster. As with Factor-2 this factor also has one religious-oriented reason and market-oriented reason.

Factor 5

ID No.	Variables	Factor Loading
X_5	Most of the population believes Islam from their heart. Hence, they prefer Islamic banking	.845
X_4	Ensure the safety of customers because Islamic banks run activities under Islamic rule	.457
X_9	To get more deposits because most of the population are Muslim and want to keep their wealth in the interest-free bank	.402
	Variance accounted for	7.823%

Factor 5 explains 7.823% of the total variations existing in the variable set. This includes variables: X_5, X_4, and X_9. This factor has three variables that formed a cluster and except for variable X_9, all are religious-oriented reasons.

Factor 6

ID No.	Variables	Factor Loading
X_3	Customers demand Islamic products and services which are not available in conventional banking	.660
X_{13}	To get the Govt. support	.540
	Variance accounted for	7.531%

Factor 6 explains 7.531% of the total variations existing in the variable set. This includes variables: X_3 and X_{13}. As like as Factor-2, this factor also has one variable related to market-oriented and another one is religious-oriented reason.

Factor 7

ID No.	Variables	Factor Loading
X_7	Seeing the success of Islamic Banks in Bangladesh	.813
	Variance accounted for	7.203%

Factor-7 explains 7.203% of the total variations existing in the variable set. This includes variable: X_7. This factor formed a cluster by having only one significant variable related to market-oriented.

From the above tables, it is seen that all factors cover the maximum variables which are related to the market-oriented reasons for being converted from the conventional to the Islamic banking system in Bangladesh. That is, market-oriented factors are the main dynamics of the banks that wanted to be converted their conventional banking activities to Islamic banking activities, where religious issues are less important to be converted.

Ranking of factors

Finally, the ranking is based on factor-wise average scores (Table 2). The factor rakings show Factor-VII as the first and most important factor. This factor includes only one variable: the success of Islamic Banks in Bangladesh which has reflected the actual scenario of Bangladesh. Banks that have already converted their conventional banking activities and banks, that want to be converted were motivated by the success of existing Islamic banks in the banking sector of Bangladesh. Islamic banks' growing success encourages conventional banks to adopt the Shariah model. In 2014, according to the Bangladesh Bank source, the net profit of Islamic banks rose 10.4 per cent year on year. The second factor is Factor 3, which also includes market-oriented reasons for converting from a conventional banking system to an Islamic one. The variables are also related to "cope with market share" in the banking industry of Bangladesh, and as profit is not predetermined because of the profit-loss sharing mode, banks may get benefit from the contract.The variables of Factor-3 are also supporting the variable of Factor-7 that ,by converting their conventional activities, the converted banks want to boost up their earnings because the profit in the contract (Islamic banks deal with clients with the participation of ownership contract) is not predetermined and that is the way they want to cope the market share of Islamic banks in Bangladesh. The growth of investment of Islamic banks was 24.60% in the last five years till 2013 compared to 20% for conventional banks. Total deposits of the Islamic banks stood at Tk. 1.198 trillion, holding a market share of 19.3%. The third important factor is

Factor 4, which comprises two variables one is a religious-oriented reason, and another one is also a market-oriented reason. These customers demand Islamic products and services, not available in conventional banking, and get Government support. The present scenario of conventional banks in Bangladesh highlights the religious-oriented reason that by opening new Islamic windows, conventional banks of Bangladesh are providing Islamic products and services because of customers' demand. Our study indicates that for fulfilling customers' demand for Islamic products and services, conventional banks want to convert their conventional banking to a full-fledged Islamic banking system. The fourth and fifth important factors are, Factor-5 and Factor-2. Factor 5 includes three variables which made a cluster where only one is market-oriented, and the other variables are religious-oriented. Factor 2 includes two variables that made a cluster, and in the cluster, one variable is market-oriented, and another is religious-oriented. Finally, the sixth and seventh important factors are Factor-6 and Factor-1.

Table 2
Ranking of factors

Factor	Weighted factor score ranking	Ranking
7	2.35	1
3	2.11	2
4	2.05	3
5	2.04	4
2	1.75	5
6	1.63	6
1	1.60	7

3. Conclusion

According to Bangladesh Bank source, the deposit growth of Islamic banks was 25.83% compared to 20.58% in conventional banks. It may be a positive sign to the Islamic banking industry that customers prefer Islamic banks to keep their savings to the banks. Our study found that except for EXIM Bank, First Security Islami Bank Ltd. (FSIBL) earned more profit after converting its banking activities from conventional to Islamic mode. Both the return on assets (ROA) and return on equity (ROE) of FSIBL indicate it. In the case of risk and solvency, Islamic banks gained a significant benefit in that both banks reduced their credit risk and debt financing after converting from a conventional banking system to an Islamic one. However, both banks lost their liquidity position because they incurred higher liquidity risk after converting from the conventional system. EXIM Bank gained remarkable

efficiency after converting, where FSIBL achieved better asset management quality. Results may conclude that due to higher capitalization and lower credit risk, banks are interested to be converted their banking activities from conventional into Islamic practices.

From the factorial analysis, it has been found that conventional banks want to convert their banking activities to Islamic mode for significant market-oriented reasons. Among the most significant variables are getting the benefit of bank reserve and seeing the success of Islamic Banks in the global market. In Bangladesh, Islamic banks have to keep a lower statutory liquidity ratio: only 11.5 per cent against 19 per cent for conventional banks. As a result, Islamic banks have more investible funds than other banks. The annual growth rate of assets of Islamic banks in the world market was around 17% from 2009 to 2013, which attracted the conventional banks of Bangladesh to be converted into Islamic banking. From our study, some other significant variables have been found, most of which are related to market-oriented reasons. It indicates that conventional banks waiting to convert their conventional banking activities to Islamic banking activities so that they could be benefited from the market.

There were some limitations in conducting the study. The first limitation is data insufficiency. Though three banks were converted from conventional to Islamic banking, two banks were selected as sample bank due to data insufficiency, third one was not included in the sample. For the EXIM bank, only four-years data were used before conversion because the bank was established in 1999, and the data were not found for that year. Another limitation was that the study covered few ratios to measure financial performance under four categories. These limitations may be the motivations for further study. Further study is suggested to cover long-run data and more financial ratios to measure the financial performance as well as more variables to judge managerial and expert's perception.

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Appendix

A-1: Zero-order correlation matrix

	X1	X2	X3	X4	X5	X6	X7	X8	X9	X10	X11	X12	X13	X14	X15	X16
X1	1.00															
X2	0.12	1.00														
X3	-0.03	0.05	1.00													
X4	0.08	0.07	-0.05	1.00												
X5	0.02	0.08	0.00	0.15*	1.00											
X6	0.14	0.06	0.10	0.12	0.00	1.00										
X7	-0.02	0.10	-0.01	0.15*	0.06	0.06	1.00									
X8	0.12	-0.10	-0.10	0.04	0.02	0.07	0.08	1.00								
X9	0.08	-0.04	0.05	0.15*	0.16*	0.16*	0.05	0.14	1.00							
X10	0.09	0.07	-0.01	0.16*	0.09	0.14*	0.04	-0.03	0.08	1.00						
X11	0.09	0.03	-0.03	0.00	0.07	0.01	-0.08	0.21**	0.04	-0.03	1.00					
X12	0.07	0.19**	0.07	0.14	0.04	0.13	0.07	0.06	0.06	0.13	-0.02	1.00				
X13	0.08	0.04	0.04	0.00	0.06	0.06	0.01	0.01	0.08	-0.07	-0.04	0.06	1.00			
X14	0.16*	0.01	-0.01	0.08	0.10	0.10	0.02	0.17*	0.05	0.00	0.00	-0.01	0.07	1.00		
X15	0.07	0.09	0.13	0.03	0.02	-0.04	0.09	0.03	0.11	0.04	-0.17	0.00	0.08	0.11	1.00	
X16	-0.13	-0.04	0.01	-0.12	-0.10	-0.03	0.01	-0.02	0.00	-0.04	0.12	-0.04	-0.05	-0.12	-0.13	1.00

* Correlation is significant at the 0.05 level (2-tailed)
** Correlation is significant at the 0.01 level (2-tailed)

A-2: Total variance explained

Total Variance Explained

Component	Initial Eigenvalues			Extraction Sums of Squared Loadings			Rotation Sums of Squared Loadings		
	Total	% of Variance	Cumulative %	Total	% of Variance	Cumulative %	Total	% of Variance	Cumulative %
1	1.921	12.004	12.004	1.921	12.004	12.004	1.452	9.077	9.077
2	1.423	8.894	20.898	1.423	8.894	20.898	1.365	8.528	17.606
3	1.288	8.052	28.950	1.288	8.052	28.950	1.342	8.387	25.992
4	1.162	7.263	36.212	1.162	7.263	36.212	1.252	7.824	33.816
5	1.127	7.043	43.255	1.127	7.043	43.255	1.252	7.823	41.640
6	1.055	6.595	49.850	1.055	6.595	49.850	1.205	7.531	49.171
7	1.044	6.524	56.374	1.044	6.524	56.374	1.152	7.203	56.374
8	.971	6.068	62.442						
9	.892	5.576	68.017						
10	.877	5.480	73.497						
11	.822	5.139	78.636						
12	.770	4.810	83.447						
13	.745	4.656	88.103						
14	.710	4.435	92.538						
15	.621	3.882	96.420						
16	.573	3.580	100.000						

Extraction method: Principal component analysis.

A-3: Rotated Component Matrix

Rotated Component Matrix

	Component						
	1	2	3	4	5	6	7
Low cost of ancillary services of Islamic banks	.635						
Believing in religious faith	.621						
To have the benefit of bank reserve	-.486		.450				
By seeing the success of IBs in the world market	.466		.425				.428
More careful evaluation		.703					
To get more profit		.591					
To cope with the market share			.782				
Profit is not predetermined			-.480			.376	
Customers demand Islamic products and services				.813			
To get the Govt. support		.360		.520			
Most of the population belief Islam					.845		
Ensure the safety of customers		.324			.457		
To get more deposits		.397		-.322	.402	.337	
Islamic products are less risky						.660	
Low cost of fund						.540	
By seeing the success of IBs in Bangladesh							.813

Extraction method: Principal component analysis.

Rotation method: Varimax with Kaiser normalization.

a. Rotation converged in 25 iterations.