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Determinant of Indonesian Islam Bank's Profitability: Lessons from the BRI Syariah case

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Abstract

Profit is the main key to the success and sustainability of Indonesian Islamic banks that join the banking industry in Indonesia as the last players. This study investigates the profitability of Islamic banks in Indonesia for the BRI Syariah case. Islamic banks' profitability is measured by two measurements, namely Return on Assets (ROA) and Return on Equity (ROE). This study uses the well-known Autoregressive Distributed lag model (ARDL) as a dynamic time series regression method using quarterly data from 2009Q1 to 2020Q4. The explanatory variables are asset, capital adequacy ratio (CAR), financing, cost-income ratio (CIR) and GDP. The findings indicate that specific bank variables and macroeconomic variables influence profitability. Size, CAR, and financing have a negative effect on profits while operating inefficiency has a negative effect on profits. This finding also shows that high economic growth will boost the profits of Islamic banks.

Keywords: *BRI Syariah, Return on Asset, Return on Equity, ARDL*

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1. INTRODUCTION

Profitability is widely used as the main indicator in examining performance in an Islamic bank. Profitability is intensively measured by ROA (Return on Assets) and ROE (Return on Equity). Based on ROA, if the ROA is more than 1.5%, it can be concluded that Islamic banks are very healthy. The ROA is between 1.2%-1.5%, and then the Islamic bank is classified as healthy. However, if the ROA is below 0.5%, it can be said that an Islamic bank is not a sound Islamic bank. The average ROA of Islamic banks during 2010-2021 was 2.13%, while the average non-performing financing (NPF) was 3.95%, which the average NPF is still below the maximum limit of 5%.

One of the Islamic banks that has an important role in the development of the Islamic banking sector in Indonesia is BRI Syariah. BRI Syariah officially started operating on November 17, 2008. On December 19, 2008, the spin-off between the Sharia Business Units of Bank Rakyat Indonesia was signed and split into BRI Syariah which is effective on January 1, 2009. Prior to the merger of three banks, namely Bank Mandiri Syariah, Bank BRI Syariah and Bank BNI Syariah, Bank BRI Syariah (BRIS) was the number 4 Islamic bank in Indonesia based on its asset. Total Islamic banking assets in Indonesia in 2020 amounted to 593,948 trillion, while BRI Sharia assets amounted to 57,715 trillion. In addition, BRI Syariah also has a wide network with 322 sub-branches throughout Indonesia and ranks in the number two position after Bank Mandiri Syariah with 428 sub-branches.

Many empirical studies have been conducted to analyze the profitability of Islamic banking in Indonesia. The method used is divided into two, namely panel data regression and time series data regression. In general, the results show that bank-specific variables and macroeconomic variables influence the profitability of Islamic banks. Several studies have shown that bank-specific variables such as total assets, Capital Adequacy Ratio (CAR), and Financing Deposit Ratio (FDR) positively influence the profitability of Islamic banking in Indonesia using

panel regression. While the inefficiency measured by operating cost to operating income and non-performing financing as measured by non-performing financing (NPF) has a negative effect on ROA (Sriyana, 2015; Aisyah & Hosen, 2018; Suwarno & Muthohar, 2018).

Several studies also employed time series data for aggregate data of Islamic banks in Indonesia using the ARDL method. The findings indicate assets, FDR, and CIR have a positive impact on profitability while the NPF has a negative effect on profitability in the long run (Widarjono, 2018; Dewi & Sudarsono, 2021; Widarjono, 2021). In contrast to previous studies that used the ARDL method, Hasibuan et al. (2021) investigated the profitability of Indonesian Islamic banking using the VAR (Vector Auto-Regressive) approach. The results documented that in the short and long term, the NPF is the most dominant variable in influencing the profitability of Islamic banks.

This study explores the profitability of Islamic banks in Indonesia by selecting the BRI Syariah case using ARDL dynamic regression. This research contributes to existing research in several ways. First, many studies analyze the profitability of Islamic banks in Indonesia using aggregate data from Islamic banks such as Widarjono (2021) and Dewi and Sudarsono (2021). However, empirical research on the profitability of individual Islamic banks is still rarely done. Second, this study employs the ARDL model. The advantage of ARDL is that it does not require the same data stationary and if the model has more than one cointegration (Pesaran & Shin, 1999).

In this study, BRI Syariah is chosen as a sample of Indonesian Islamic banks. The selection of BRI Syariah is based on several plausible reasons. First, BRI Syariah is a Sharia bank which is ranked 4th based on its assets. Second, the BRI Syariah bank has an extensive network throughout Indonesia. This study uses quarterly data from the first quarter of 2009 to the fourth quarter of 2020. This period was chosen after conventional BRI Bank as the parent bank carried out a spin-off of its sharia business unit in 2009. This study uses bank-specific and economic macro variables to analyze the explanatory variables that affect the profitability of BRI Syariah. The bank-specific variables consist of assets, efficiency, financing, and operating efficiency while the external variable is gross domestic product (GDP) as a proxy of macroeconomic conditions. The data used are quarterly financial data from March 2009 to December 2020. The data is extracted from the Indonesian Financial Services Authority (OJK).

2. RESEARCH METHOD

The method to analyze the Islamic bank's profitability is the regression method. The regression model used is ARDL as a dynamic regression model, as in previous studies on Islamic banks in Indonesia (Widarjono, 2018; Dewi & Sudarsono, 2021; Widarjono, 2021). The long-run regression model that indicates the influence of bank-specific and economic macro variables on the profitability of BRI Syariah can be written in the following equation:

$$PROFIT_t = \delta_O + \delta_1 LASSET_t + \delta_2 CAR_t + \delta_3 LFIN_t + \delta_4 CIR_t + \delta_5 LGDP_t + \varepsilon_t \quad (1)$$

Profitability is measured using two measures, namely ROA (%) and ROE (%). Assets are total assets (trillion Rupiah), CAR is capital adequacy ratio (%), Fin is total financing (trillion Rupiah), CIR is the ratio of operating costs to operating income (%) which measures operating efficiency and GDP is a gross domestic product, which measures domestic output. Asset, financing, and GDP variables are expressed in a natural logarithm (L).

The size of an Islamic bank can be proxied from its total assets. The larger asset of Islamic banks can lower efficiency due to economies of scale that Islamic banks can generate high profits. However, the larger Islamic bank also leads to inefficiency because Islamic bank cannot control their activities well and then reduces profits (Hamid, 2017). Assets are expected to have a positive or negative effect on the profitability of Islamic bank.

Capital Adequacy Ratio (CAR) describes the ability of a bank to provide sufficient capital to bear all risks that may occur when carrying out business activities. If the CAR is high, the bank's ability to finance is also high, so a high CAR will generate high profits and low CAR lower low profits (Sutrisno & Widarjono, 2018). This paper hypothesizes that CAR may have a positive or negative effect on profitability.

Financing is measured by the total financing consisting of profit-loss sharing (PLS) and non-PLS financing. The high or low total financing ratio indicates the liquidity rate of an Islamic bank. The high financing represents high disbursed financing, so high profits can be generated. However, high financing may generate high financing defaults and then lowers the profitability of Islamic bank (Widarjono et al., 2022). Therefore, we expect that

financing may have a positive or negative effect on profitability

CIR (Operating cost to Operating Income) shows operating efficiency. CIR measures the ability of Islamic banks to manage operating costs against operating income earned. A high CIR indicates inefficiency and vice versa (Dewi & Sudarsono, 2021). As the bank is efficient, the bank can generate high profits and otherwise. This study hypothesizes that CIR has a negative effect on ROA profitability.

Macroeconomic conditions persistently affect bank profits. Gross domestic product is used to measure macroeconomic activities. High GDP growth indicates good macroeconomic conditions. High economic growth causes the Islamic banks' ability to disburse their financing is high and the customers' capability to repay financing is also high (Nahar & Prawoto, 2017). Our study expects that GDP has a positive influence on profitability.

The data used in this study is time series data, so it is necessary to choose the right regression model that can describe the behavior of time series data. This study employs the Autoregressive Distributed Lag model (ARDL) method to estimate equation (1). The ARDL model was chosen for several reasons. First, ARDL can be used for models with different levels of data stationarity. Second, ARDL produces dynamic coefficients both in the short and long run. The ARDL model equation for equation (1) is written as follows:

$$\begin{aligned}\Delta PROFIT_t = {} & \theta_0 + \sum_{1=1}^{n} \theta_{1i}\, \Delta PROFIT_{t-1} + \\ & \sum_{1=1}^{n} \theta_{2i}\, \Delta LOGASSET_{t-1} + \\ & \sum_{1=1}^{n} \theta_{3i} \Delta CAR_{t-1} + \sum_{1=1}^{n} \theta_{4i}\, \Delta LFIN_{t-1} + \\ & \sum_{1=1}^{n} \theta_{5i}\, \Delta BOPO_{t-1} + \\ & \sum_{1=1}^{n} \theta_{6i}\, \Delta LGDP_{t-1} + \pi_1 PROFIT_{t-1} + \\ & \pi_2 LOGASSET_{t-1} + \pi_3 CAR_{t-1} + \\ & \pi_4 LFIN_{t-1} + \pi_5 BOPO_{t-1} + \\ & \pi_6\, LGDP_{t-1} + \varepsilon_t \end{aligned} \quad (2)$$

where Δ is lag.

As a time series model, the first step to estimating the ARDL model is to check the data stationarity. This study applies a unit-roots test to determine the level of data stationarity. Our study utilizes two methods, namely Augmented Dickey-Fuller and Phillip-Perron. The next step is the estimation of the ARDL model using the Akaike Info Criterion (AIC) method to select the length of the optimal lag. The next step is the cointegration test. The cointegration test is to determine whether there is a long-term relationship between variables in the ARDL model. Cointegration test employs the cointegration test Bound Testing Approach (Pesaran et al., 2001). The Bound Testing Approach is based on the F statistical test. The hypothesis in the test can be written:

$$H_0: \pi_1 = \pi_2 = \pi_3 = \pi_4 = \pi_5 = \pi_6 = 0$$
$$H_0: \pi_1 \neq \pi_2 \neq \pi_3 \neq \pi_4 \neq \pi_5 \neq \pi_6 \neq 0 \quad (3)$$

Ho is no cointegration while Ha is cointegrated. If the F-statistic is greater than I(1), then there is cointegration, the F-statistic (value) is smaller than I(0), then there is no cointegration and if the F-statistic is between I(0) and I(1) then there is no decision. The next step, if cointegration is found, is the estimation of the Error correction model. The ARDL ECM model can be written as follows:

$$\begin{aligned}\Delta PROFIT_t = {} & \rho_0 + \sum_{1=1}^{n} \rho_{1i}\, \Delta PROFIT_{t-1} + \\ & \sum_{1=1}^{n} \rho_{2i}\, \Delta LASSET_{t-1} + \\ & \sum_{1=1}^{n} \rho_{3i} \Delta\, CAR_{t-1} + \sum_{1=1}^{n} \rho_{4i} \Delta\, LFIN_{t-1} + \\ & \sum_{1=1}^{n} \rho_{5i}\, \Delta BOPO_{t-1} + \\ & \sum_{1=1}^{n} \rho_{6i}\, \Delta LGDP_{t-1} + \rho_7 ECT_{t-1} + \varepsilon_t \end{aligned} \quad (4)$$

Where ϑECT_{t-1} is lag of errors

3. RESULTS AND DISCUSSION

3.1. Descriptive Statistics

Table 1 describes descriptive statistics of the variables studied. The average profit rate of BRI Syariah was 0.82%. This rate of profit indicates that BRI Syariah is a healthy Islamic bank, but there were high fluctuations because the standard deviation was fairly large (0.586). Meanwhile, the average profit rate according to ROE was 5.791%, with a fairly high level of fluctuation due to the high standard deviation (4.65). The development of BRI Syariah is quite fast, according to the trend of its assets. At the beginning of its establishment, the number of assets was 15,128 trillion and by 2020, it was 57,715 trillion and was ranked in the top 4 Islamic banks in Indonesia. The average CAR was 19.631%, which is above the minimum threshold by 15%, implying that BRI Syariah is quite capable of maintaining capital adequacy to be able to act as a financial intermediary. The average level of financing was 53.235 trillion, with a high level of fluctuation based on variations in financing (39.96 trillion). The average level of operating efficiency (CIR) was 93.104%. This inefficiency rate is higher than the maximum threshold by 90%. With a low level of efficiency variation with a standard deviation of 4,663%, BRI Syariah may not achieve an efficient rate of operation.

Table 1 Descriptive statistics

	Mean	Std. Dev.	Maximum	Minimum
ROA (%)	0.820	0.576	3.110	0.030
ROE (%)	5.791	4.650	22.110	0.240
ASSET (Trillion)	22.358	14.485	57.715	15.128
CAR (%)	19.631	6.957	45.270	11.030
FIN (Trillion)	53.235	39.960	152.329	1.927
CIR (%)	93.104	4.663	101.380	80.800
GDP (Trillion)	2197.52	372.289	2783.726	1579.42

3.2. The results of the ARDL model

The first step in the estimation of the ARDL model is the unit root test to check data stationery. This study utilizes the Augmented Dickey-Fuller (ADF) and Philips Perron (PP) methods. The unit-roots test was carried out using constant without trend (C) and constant and time trend (T). Table 2 presents the results of unit roots. The ROA, ROE, Asset, CAR, Financing, and CIR are stationary at the level data, but GDP is not stationary at the level data using either the ADF or PP test. However, all first difference data, all variables are stationary. This test indicates that the level of data stationarity is different, but all variables are stationary at the first difference data. These findings indicate that ARDL is suitable for estimating the profitability of BRI Syariah in this study.

Table 2 Unit root test

	ADF		PP		ADF		PP	
	C	T	C	T	C	T	C	T
ROA	-2.974**	-4.739***	-4.874***	-4.541***	-7.571***	-7.644***	-7.546***	-7.612***
ROE	-2.877*	-2.967	-4.848***	-4.708***	-8.838***	-8.620***	-8.800***	-8.589***
LASSET	-5.696***	-4.870***	-5.680***	-7.479***	-4.220***	-5.317***	-4.238***	-5.479***
CAR	-4.345***	-4.938***	-4.141***	-4.711***	-5.859***	-5.827***	-6.089***	-6.069***
LFIN	-5.486***	-6.633***	-3.996***	-5.366***	-3.978***	-4.002**	-4.390***	-3.951**
CIR	-4.578***	-4.837***	-3.751***	-3.810**	-9.445***	-9.418***	-9.376***	-9.343***
LGDP	-1.862	-1.269	-2.635	-1.138	-6.342***	-5.887***	-6.323***	-7.421***

Note: *, **, and *** indicates significant at 10%, 5% and 1%

The ARDL estimation results are shown in Table 3. There are two measures to calculate the profitability of BRI Syariah, namely ROA as model 1 and ROE as model 2. Model 1 produces ARDL (4,0,1,4,3,4) while model 2 generates ARDL (4,0,0,0,3,0). The coefficient of determination (R^2) for each model is 0.9320 and 0.8785, respectively. Based on R^2, the ARDL model can explain the behavior of time series data reasonably well because models 1 and 2 can explain 93.32% and 87.85%, respectively. According to the autocorrelation test with the LM test, Model 1 contains autocorrelation problems, model 1 contains autocorrelation problems, while model 2 is free from autocorrelation problems. Accordingly, model 1 is estimated using the HAC method to produce an unbiased and consistent estimator. Based on the heteroscedasticity test with the ARCH test, models 1 and 2 are also free from heteroscedasticity problems. The CUSUM and CUSUM squares tests that are presented in Figures 1 and 2 reveal that both models have stable parameters.

Table 3. The ARDL model

	ROA		ROE	
Variable	Coefficient	Prob.*	Coefficient	Prob.*
C	13.5959	0.1052	44.4705	0.2806
ROA(-1)	-0.2412	0.1467	0.1307	0.1155
ROA(-2)	-0.3354**	0.0339	-0.3614**	0.0024
ROA(-3)	0.2033	0.1242	0.0827	0.5725
ROA(-4)	-0.2629***	0.0046	-0.3159**	0.0240

LOG(ASSET)	-1.1196*	0.0509	-3.4547	0.1481
CAR	0.0076	0.5205	-0.3701***	0.0000
CAR(-1)	-0.0134	0.3296		
LOG(FIN)	-0.5813	0.1159	-4.0008**	0.0132
LOG(FIN(-1))	0.3144	0.4442		
LOG(FIN(-2))	0.5408	0.3822		
LOG(FIN(-3))	-1.4266	0.1000		
LOG(FIN(-4))	0.8634	0.1208		
CIR	-0.0762***	0.0000	-0.5666***	0.0000
CIR(-1)	-0.0489**	0.0131	-0.1798	0.3015
CIR(-2)	-0.0268**	0.0372	-0.2377*	0.0539
CIR(-3)			-0.2617*	0.0613
LOG(GDP)	-0.0923	0.9221	26.7780***	0.0032
LOG(GDP(-1))	-7.3775***	0.0063		
LOG(GDP(-2))	33.8256**	0.0228		
LOG(GDP(-3))	-149.6008**	0.0315		
LOG(GDP(-4))	126.7136**	0.0271		
R-squared	0.9320		0.8785	
Diagnostic				
LM	14.8315***	0.0006	2.6432	0.2667
ARCH	0.7802	0.3771	0.0303	0.8618
Cointegration				
F-statistic	4.7920***		5.3846***	

Note: *, **, and *** indicate significant at 10%, 5% dan 1%. The critical value of upper bound I(1) for the bound testing approach at 10%, 5% and 1% are 3, 3.38, and 4.15, respectively.

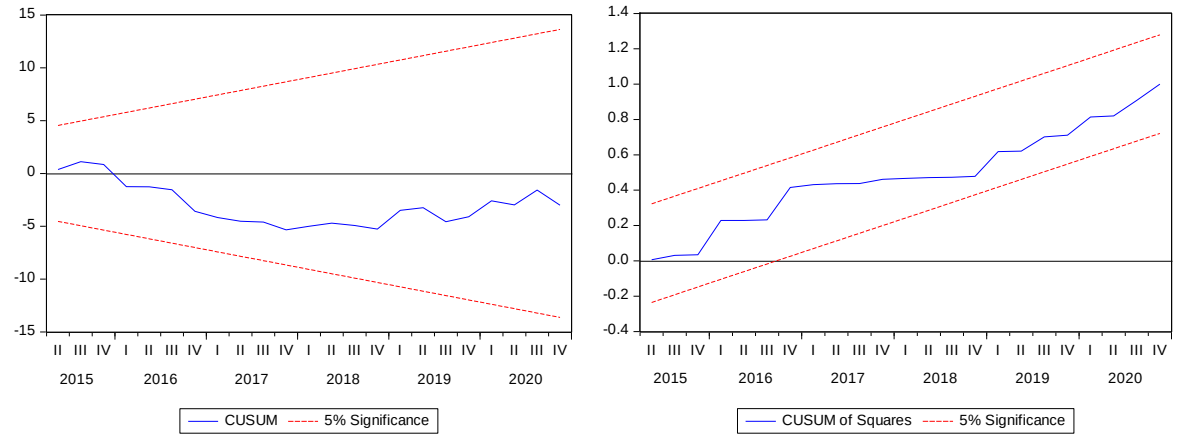

Figure 1 Stability test of ROA

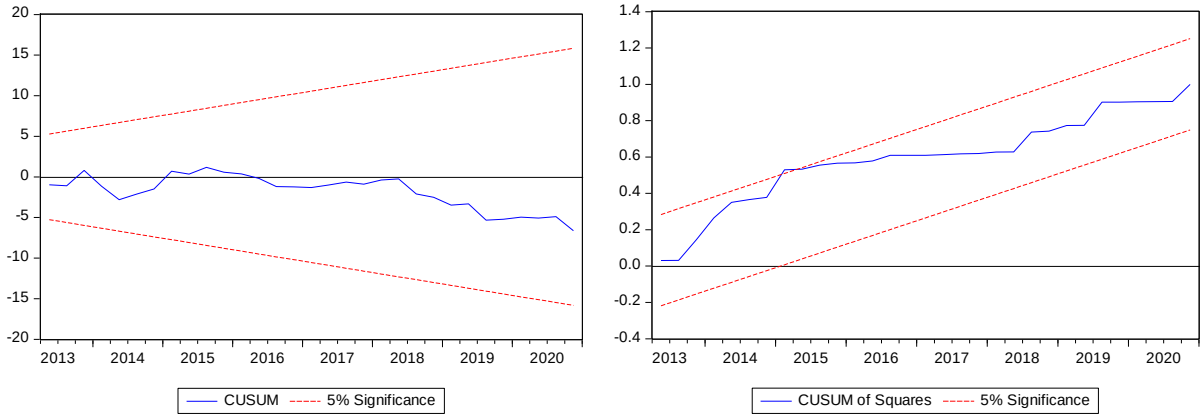

Figure 2 stability test of ROE

The ARDL model is a dynamic regression model so short-run and long-run estimates depend on the cointegration test. This cointegration test is to determine the long-term relationship between the variables studied. The findings of the cointegration test with the Bound testing approach using the F distribution can be seen in table 3. The calculated F values in models 1 and 2 are 4.792 and 5.385, respectively. This calculated F value is greater than the upper bound value (1) at 1% significance. In conclusion, there is a long-run relationship between the variables studied even though there are some data that are not stationary at the level. Thus, this ARDL model will produce a short-run estimation model, namely the ECM ARDL and a long-run model.

The short-run estimation results of the ARDL ECM model are presented in Table 4. The validity of the ARDL ECM model is evaluated based on the error coefficient of the previous period (CointEg(-1)). The CointEq(-1) variable is negative and significant for both models. These results imply that the ECM-ARDL model is able to correct the imbalance in the short run. The speed of adjustment of short-run imbalances towards long-run equilibrium for the quarterly period is 1,473 for model 1 and 1,340 for model 2, respectively.

In model 1, there are several explanatory variables that affect profit. The previous profitability, namely D(ROA(-1)) and D(ROA(-3)) had a positive effect. The DLOG(FIN), and DLOG(FIN(-3)), which indicate the previous financing, have a positive effect while DLOG(FIN(-2)) has a positive effect. Operating efficiency variables (CIR) have a negative effect, and some have a positive influence. Meanwhile, there are macro variables (GDP) that have positive and negative effects. While in model 2, the previous profitability, as measured by ROE also affects the profit in the current period. In the short run, the operating efficiency variable also affects profits.

Table 4 ECM ARDL

	ROA		ROE	
Variable	Coefficient	Prob.	Coefficient	Prob.
D(ROA(-1))	0.3544**	0.0311	0.3449*	0.0746
D(ROA(-2))	0.0126	0.8717	0.0975	0.5584
D(ROA(-3))	0.2866***	0.0002	0.2091**	0.0271
LOG(ASSET)	0.0101	0.3567	2.4097	0.3613
CAR			-0.0593	0.2674
D(CAR)	0.0025	0.7960		
DLOG(FIN)	-0.8594**	0.0187	-1.3858	0.4329
DLOG(FIN(-1))	0.1671	0.5718		
DLOG(FIN(-2))	0.5107*	0.0847		
DLOG(FIN(-3))	-0.9445***	0.0016		
D(CIR)	-0.0770***	0.0000	-0.5556***	0.0000
D(CIR(-1))	0.0232*	0.0980	0.4035**	0.0474
D(CIR(-2))			0.1048	0.3990
LOG(GDP)			-2.3873	0.3837
DLOG(GDP)	1.0682	0.5487		
DLOG(GDP(-1))	-9.4986**	0.0002		
DLOG(GDP(-2))	26.9330***	0.0008		
DLOG(GDP(-3))	-137.2377***	0.0001		
CointEq(-1)	-1.4733***	0.0000	-1.3401***	0.0000

Note: *, **, and *** report significant at 10%, 5%, and 1%

The results of the long-run coefficient of the ARDL model are exhibited in Table 5. Assets and CIR have a negative effect on ROA. While the CAR, financing and CIR variables have a negative effect on ROE. The GDP variable has a positive effect on ROA and ROE. These findings show that the specific bank variables (size, equity, and financing), which indicate the bank's ability to carry out expansionary financing, have a negative effect on profits. The bank's inefficiency also has a negative effect on profits. The macroeconomic variable positively influences bank

profits. Therefore, high economic growth encourages the profitability of Islamic banks.

Table 5 long-run ARDL

	ROA		ROE	
Variable	Coefficient	Prob.	Coefficient	Prob.
C	8.3092	0.0688	30.3776	0.2433
LOG(ASSET)	-0.6842**	0.0382	-2.3599	0.1546
CAR	-0.0035	0.5633	-0.2528***	0.0000
LOG(FIN)	-0.1768	0.3117	-2.7329**	0.0171
CIR	-0.0928***	0.0000	-0.8509***	0.0000
LOG(GDP)	2.1199**	0.0411	18.2920***	0.0075

Note: *, **, and *** denote significant at 10%, 5%, and 1%

3.3. Discussion

The total asset represents the Islamic bank's size. The results of this study show that the larger the bank is, the lower the profit as measured by ROA. The larger size of the Islamic bank causes the bank's capacity to exceed its optimal capacity, causing diseconomies of scale (Hamid, 2017). Diseconomies of scale lead to Islamic banks operatiing inefficiently, thereby reducing the bank's ability to generate profits. The results of this study are in line with previous research on the case of the Islamic banking industry in Indonesia (Widarjono, 2018; Kasanah et al., 2022).

The next variable is equity which is measured by CAR. CAR has a negative effect on ROE as an alternative to measuring Islamic banks' profitability. Islamic banks that run prudential policies have a high CAR. This prudential policy must be carried out by Islamic banks because the financing of Islamic banks must comply with Sharia principles where speculative activities are prohibited (Widarjono, 2021). This result confirms the previous empirical study for Islamic banking in Indonesia (Dewi & Sudarsono, 2021) and for Islamic banks in ASEAN that apply the dual banking system (Chen, Liang, & Yu, 2018).

The main activity of Islamic banks as financial intermediaries is to disburse their funds. The results of the study indicate that financing has a negative effect on Islamic banks' profitability (ROE). The higher financing lowers the profitability of BRI Syariah. High financing causes banks to be unable to control their financing, resulting in high non-performing financing (Ikramina & Sukmaningrum, 2021; Widarjono & Rudatin, 2021). In general, Islamic banks in Indonesia face high NPF because profit and loss sharing (PLS) financing, such as Mudharabah, is subject to moral hazard (Azad et al., 2018; Warninda et al., 2019). This finding supports the existing empirical studies on the case of Indonesian Islamic banking (Anggraini & Mawardi, 2019; Widarjono et al., 2022).

The next explanatory variable is operating efficiency, which is measured by the cost-income ratio, where the higher the CIR is, the less efficient operation of the Islamic bank. The outcome of the study reveals that a high CIR will reduce the profits of BRI Syariah, both measured by ROA and ROE. The high CIR signifies the low operating efficiency of Islamic banks, reducing profits. The low efficiency of Islamic banks is due to the small scale of Islamic banks in Indonesia (Aisyah & Hosen, 2018). The market share of Islamic banks in the Indonesian banking industry is low (6%). This study is in line with previous research (Paulin & Wiryono, 2015; Suwarno & Muthohar, 2018).

The last explanatory variable is GDP as a proxy of macroeconomic conditions. The result reveals that GDP has a positive effect on the profitability of BRI Syariah, both ROA and ROE. High economic growth causes the production of goods and services to increase. Subsequently, the capability to disburse financing of Islamic banks is high and the ability of customers to repay their financing is also fairly high (Kasri & Azzahra, 2020). As a result, non-performing financing is also low and further increases the profitability of Islamic banks (Ikramina & Sukmaningrum, 2021). This study confirms the previous studies on Islamic banking in Indonesia (Nahar & Prawoto, 2017; Widarjono, 2018).

4. CONCLUSION

This study aims to analyze the profitability of Indonesian Islamic banks by investigating the case of the BRI Syariah, which is an Islamic bank with a fairly national network in Indonesia. This study employs

bank-specific variables and macroeconomic variables. The method is ARDL as a dynamic time series model that can capture well the short-run and long-run conditions of Islamic banks' profitability.

The results show that specific bank variables and macroeconomic variables affect the profits of Islamic banks. Assets, equity, financing, and operating inefficiency weaken Islamic banks' profitability while high economic growth enhances profits. These findings imply that the expansionary policies of Islamic banks have a negative effect on profitability. In addition, operating efficiency is also the key to driving the profitability of Islamic banks. Good macroeconomic conditions also encourage banks to generate high profits.

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