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Technical efficiency in banks: a review of methods, recent innovations and future research agenda

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Abstract

Technical efficiency in banking is a critical aspect of the financial industry and has been widely studied using various measurement techniques. This systematic literature review offers a comprehensive examination of 305 studies on the application of technical efficiency measurement techniques in both Islamic and conventional banking sectors from 1989 to 2019. Our comprehensive analysis not only provides a broad view of the efficiency measurement literature but also outlines a future research agenda. Despite the extensive research in this field, several issues remain unresolved, including input–output selection, a comparison of efficiency between Islamic and conventional banks, limited cross-country studies, and a lack of exploration into the impact of regulation and Shariah principles. To address these gaps, this review highlights the most commonly used methods, variables, and findings and provides three key recommendations for future research. Three key themes emerge from our examination. *First*, there is a need to better understand and the application of new frontier techniques other than the traditional methods, which currently dominate the existing literature. *Second*, the intermediation approach is the most frequently used in variable selection, thus more studies with comparative findings with applications of production and value-added approaches are suggested. *Third*, the most frequently used input variables are ‘labor’, ‘deposits’ and ‘capital’, whilst ‘loans’ and ‘other earning assets’ are the most popular output variables. We recommend three vital directions for future research: (i) non-interest expenses to be included amongst the inputs, while non-interest income should be added to the list of outputs, especially when estimating efficiency scores of Islamic banks. (ii) The impact of environmental variables such as, *inter alia*, Shariah principles, country-specific factors, and management quality is suggested to be considered simultaneously in models measuring and comparing the efficiency of Islamic and conventional banks. (iii) The selection of performance metrics employed should be expanded to include both the standard efficiency scores and the Malmquist Total Factor Productivity Index (TFP). The paper concludes with research needs and suggests directions for future research.

Extended author information available on the last page of the article

Keywords Bank efficiency · Parametric methods · Non-parametric methods · Two-stage analysis · Variable selection · DEA and SFA

JEL Classification G21 · D20

1 Introduction

The study of bank efficiency is central to the growth and long-term sustainability of the banking sector (Chen et al. 2021; Ghosh et al. 1994; Ramly et al. 2017), and there has been an abundance of research on the topic (Abreu et al. 2019; Aliyu et al. 2017; Bhatia et al. 2018; Jiang et al. 2020; Lopes et al. 2021; Rahman et al. 2021; Shaikh and Memon 2021). Given the large volume of literature on this subject and the ongoing expansion of research, it is imperative to evaluate the recent advances and current state of knowledge in this field (Zhu et al. 2021). The objective of this study is to bridge a research gap by conducting a critical review of recent technical efficiency methods applied to both Islamic banks (IBs) and conventional banks (CBs). This review seeks to elucidate patterns and trends in the field, as well as identify the key factors that influence efficiency. Furthermore, this study aims to provide a roadmap for future research in this area.

Islamic finance has grown tremendously over the last decade, with Islamic banking being the largest segment of the industry, accounting for 71% of the global Islamic finance assets and 6% of global banking assets (Mordor Intelligence 2021). In 2017, there were 505 Islamic banks, including 207 Islamic banking windows, and the Islamic banking assets comprised 28.8% of the total assets in Asia, 42.3% in Gulf Cooperation Council (GCC), 25.1% in the Middle East and North Africa (MENA), 0.8% in Africa, and 3.5% in other countries. Iran (32.1%) and Saudi Arabia (20.2%) held the highest shares of the global Islamic banking assets, followed by Malaysia (10.8%), United Arab Emirates (UAE) (9.8%), Kuwait (6.3%), and Qatar (6.2%) (Islamic Financial Services Industry Stability Report 2019). The COVID-19 pandemic impacted the growth of the Islamic finance markets, with Sukuk being the most affected sector (Mordor Intelligence 2021).

The rapid growth of Islamic banking has been attributed to the continuing interest of policymakers and regulators around the world (Yilmaz and Gunes 2015). However, a direct comparison between IBs and CBs should be approached with caution, as the two groups may differ significantly in their goals and operational circumstances (Khan 1986; Khan and Mirakhor 1987; Dar 2003). The technical efficiency of banks has been analyzed in the literature using various parametric and non-parametric frontier techniques, as well as accounting ratio analysis (Jarboui 2016; Mahajan et al. 2020; Sellers-Rubio and Más-Ruiz 2015; Wang et al. 2015, 2021; Wijesiri et al. 2019). Although each approach has its own advantages and disadvantages, frontier approaches are generally considered to be superior to standard financial ratio analysis as they are equipped with statistical

tools (Iqbal and Molyneux 2005). However, there is no consensus in the literature on the best technique or on the selection of input–output variables, and no agreement on the sources of differences in efficiency scores.

To address the current research gaps and provide guidance to researchers, we conducted a systematic literature review of 18,461 articles on bank efficiency measurement. The review aims to identify the most commonly used variables, countries of focus, empirical methods, and research gaps in the technical efficiency of IBs and CBs, with a focus on the impact of scale efficiency, environmental variables, innovative methods, and selected variables. Our systematic literature review is based on the screening of articles from seven prestigious journals listed in various databases. This review is unique in that it synthesizes studies that applied both parametric and non-parametric frontier techniques, as well as accounting ratios, to measure bank efficiency.

Despite that there are literature review papers published on bank efficiency measurement (e.g., Abreu et al. 2019; Aliyu et al. 2017; Bhatia et al. 2018; Hassan and Aliyu 2018; Lampe and Hilgers 2015; Liu et al. 2016; Sharma et al. 2013), they are either mainly focusing on (i) efficiency and/or productivity measurement with an application of DEA and/or SFA disregarding the other methods applied or (ii) reviewing applications on Islamic or conventional banks independently. This paper is unique in this respect in that it introduces a synthesis of studies that applied parametric and non-parametric frontier techniques as well as accounting ratios to measure technical efficiency scores of Islamic and conventional banks.

Considering the application of the systematic literature review technique, this paper provides an in-depth review as a product of screening 18,461 research articles from prestigious journals listed on seven databases. Moreover, we aim to identify the most popular input–output variables in the existing bank technical efficiency literature, help address the research gaps by offering critical reflections and propose suggestions for future research. We, thus, classify bank efficiency measurement studies into six categories as follows: (i) regulation in IBs as Shariah principals; (ii) stability; (iii) scale efficiency; (iv) input/output variable selection; (v) methods to incorporate environmental variables into the analysis, and (vi) technical efficiency measurement of Islamic and/or conventional banks.

Our paper makes several noteworthy contributions to the existing literature on technical efficiency measurement in the Islamic and conventional banking sectors. First, we provide a comprehensive and up-to-date review of the recent literature, spanning an extensive 30-year period from 1989 to 2019. Through this rigorous review, we systematically identify and synthesize key findings, revealing gaps in the literature that warrant further investigation. Second, we elucidate significant divergences in the efficiency measurement techniques utilized in the literature, underscoring the need for standardized evaluation methods. By emphasizing these areas of divergence, we advance the understanding of technical efficiency evaluation and provide a foundation for future research directions and collaborations across diverse banking systems and countries. Third, we shed light on the crucial role played by specific environmental factors, including Shariah principles, stability, and economies of scale, in shaping efficiency outcomes. By incorporating both standard efficiency scores and the Malmquist Total Factor Productivity Index (TFP), our study

offers valuable insights for policymakers and researchers seeking to comprehensively evaluate and compare the performance metrics of Islamic banks with their conventional counterparts. In an attempt of evaluating the efficiency scores of IBs and CBs in numerous countries, researchers investigated the main drivers of efficiency disparities among these groups of banks. Therefore, we structured this study in a way that identifies the factors that need more investigation for future research. Although recent research has extended the investigation of bank technical efficiency to include the impact of the Covid-19 pandemic, we have deferred this topic for a future literature review paper. Our decision is informed by the period of study in this paper, which focuses on the years spanning 1989 to 2019, immediately preceding the onset of the pandemic.¹

We argue that technical efficiency is a vital area to study as banks that are technically efficient are able to produce more outputs for a given level of inputs, such as labor, capital, and technology. This can help them reduce costs, increase profits, and remain competitive in the market. Some reasons to review technical efficiency studies in banks are as follows. First, the banking industry is highly regulated, and banks are often required to meet certain standards of efficiency in order to maintain their licenses and operate in the market. Second, banks operate in a highly competitive environment, and efficiency can be a key factor in determining which banks survive and thrive in the market. Third, the financial crisis of 2008 highlighted the importance of efficiency in banking, as many banks were found to be operating inefficiently and taking on excessive risks.

The rest of this paper is organized as follows: Sect. 2 introduces the research framework of the study, followed by the research method in Sect. 3, in which the selection criteria of the listed studies are explained. Section 4 reviews the existing literature on efficiency measurement methods identifying the main factors of the analysis and commonly used variable selection approaches. Section 5 highlights the main research gaps and areas for future research and Sect. 6 concludes.

2 Research framework

The COVID-19 pandemic has precipitated profound changes across the global economy, significantly impacting the banking sector. A substantial transition towards digital banking, alterations in customer borrowing and lending behavior, and the advent of new regulatory policies mark the sector's evolving landscape. This has consequently triggered an increasing interest in assessing the technical efficiency of banks during the pandemic period. Notably, research by Al Mamun et al. (2021) and Bele et al. (2021) has explored this in Bangladesh and Nigeria, respectively, revealing a significant

¹ The covid-19 pandemic represents a significant and unprecedented disruption to the global economy, and it is likely that the pandemic has had a significant impact on banking efficiency that has yet to be fully understood or quantified. Given the scope and magnitude of the pandemic's impact, it may be more appropriate to undertake a separate study that specifically focuses on the impact of the pandemic on banking efficiency. Additionally, by limiting the scope of the current study to the pre-pandemic period, it allows for a more focused and in-depth analysis of the technical efficiency patterns.

negative impact on banks' technical efficiency. Complementing this perspective, recent studies have furthered the understanding of this situation. For example, Boubaker et al. (2022) scrutinized the efficiency of 49 Islamic banks across ten countries during the pandemic, showing how input reduction could maintain efficiency amidst decreasing outputs. In addition, Shah et al. (2021) provided a comprehensive review of Islamic bank efficiencies, signifying the influence of variable choices and regional factors on efficiency, particularly during crises. Boubaker et al. (2023) elaborated on how Islamic banking, with its trade-off between reducing credit risk and increasing business risk due to higher operational costs, has contributed to banking sector fluctuations. Finally, Mateev et al. (2022) underscored the importance of efficiency and market competition in the performance of banks during the pandemic, emphasizing regulatory reforms that bolster efficiency to counter adverse impacts. While the present paper concentrates on the 1989–2019 period, we acknowledge the potential impact of the pandemic on bank technical efficiency. However, given the ongoing pandemic and limited data availability, it is premature to present conclusive results. The examination of the pandemic's impact on bank technical efficiency will, thus, be a focus of our future research.

This paper examines the literature on technical efficiency in Islamic and conventional banks from 1989 to 2019, using Tranfield et al.'s (2003) guidelines for conducting a systematic literature review. The analysis involves five steps: (1) Defining the topic and relevant keywords by exploring significant contributions to the subject and identifying selection criteria. (2) Conducting searches on seven scientific databases (JSTOR, Elsevier's Science Direct, Springer, Oxford Publishing, SCOPUS, Emerald Insight, and Wiley) for the terms 'bank efficiency', 'Islamic banks', and 'conventional banks' in combination with 'parametric' or 'non-parametric', with the search term 'bank efficiency' complementing terms like 'bank performance' and 'bank profitability' to obtain more relevant search results that cover studies using accounting ratios for bank efficiency measurement. (3) Screening and eliminating duplicates from the remaining articles and verifying their conformity to the pre-defined selection criteria; we developed a coding system, following Gough (2007), at this stage to ensure consistency among the two authors reviewing the data. (4) Examining the abstracts of all remaining articles for consistency with the selection criteria. (5) Following the review process of all remaining full papers in the dataset by the authors of this paper, we received third feedback from an academic scholar who has been in the research field of technical efficiency measurement over 25 years. (6) Creating summary tables accordingly. Table 1 summarizes the inclusion criteria, while excluding corporate governance, risk-adjusted efficiency, venture capital, management accounting, productivity measurement, hedging, joint ventures, managerial efficiency, and theoretical papers.

3 Research method

3.1 Databases and search results

A total of 18,461 articles in English were listed in the seven scientific databases specified, namely JSTOR, Elsevier's Science Direct, Springer, Oxford Publishing,

Table 1 Criteria for inclusion.
Source Authors' own table

Characteristics	Inclusion criteria
Language	English
Timeframe	1989–2019
Databases	JSTOR (3605 papers), Elsevier's Science Direct (4136 papers), Springer (7944 papers), Oxford Publishing (189 papers), SCOPUS (39 papers), Emerald Insight (1947 papers) and Wiley (601 papers). Total of 18,461 papers are identified
Scope	Business, economics, finance, accounting
Content	Empirical research articles on technical efficiency in banking excluding corporate governance, risk-adjusted efficiency, venture capital, management accounting, productivity measurement, hedging, joint ventures, managerial efficiency and theoretical papers

SCOPUS, Emerald Insight, and Wiley. The use of multiple databases aims to avoid publication bias and ensure a comprehensive literature review. JSTOR is considered one of the most relevant databases for social sciences, according to George State University Library. Meanwhile, Scopus is the largest abstract and citation database of multidisciplinary peer-reviewed literature search, introduced by Elsevier Science in 2004, and is considered the best database as an alternative to Web of Science (WOS) in social sciences in terms of coverage, according to Norris and Oppenheim (2007). Moreover, Vieira and Gomes (2009) found that Scopus covers 20% more research than WOS. Consequently, this paper focused mainly on Scopus and Elsevier's Science Direct, rather than WOS. Additionally, Springer and JSTOR were observed to index a significant number of publications on bank efficiency measurement. Table 1 summarizes the number of papers identified in each database.

After a rigorous screening of titles and keywords, 435 articles were identified for the abstract screening stage. The majority of the excluded articles (18,026) were due to duplication (189), irrelevance to banking applications (6572), being theoretical studies (186), and not fitting the inclusion criteria (11,079). Following the abstract screening process, 113 articles were further excluded, leaving 322 articles, of which 10 were literature reviews and 312 were related to banking efficiency applications. Subsequently, 7 articles were excluded due to the use of different methods, resulting in a final sample of 305 articles for this study. To ensure the consistency of the data reviewing process, a coding system was created following Gough's (2007) recommendation. The weight of evidence concept was applied to make separate judgments on various review-specific criteria and combine them to form an overall judgment of the contributions of each study to answering the review question. Thus, a weight of evidence framework was established for bank technical efficiency measurement (Weight of Evidence A), a review-specific judgment of bank types (i.e., Islamic versus conventional banks) (Weight of Evidence B), and a review-specific judgment of application methods

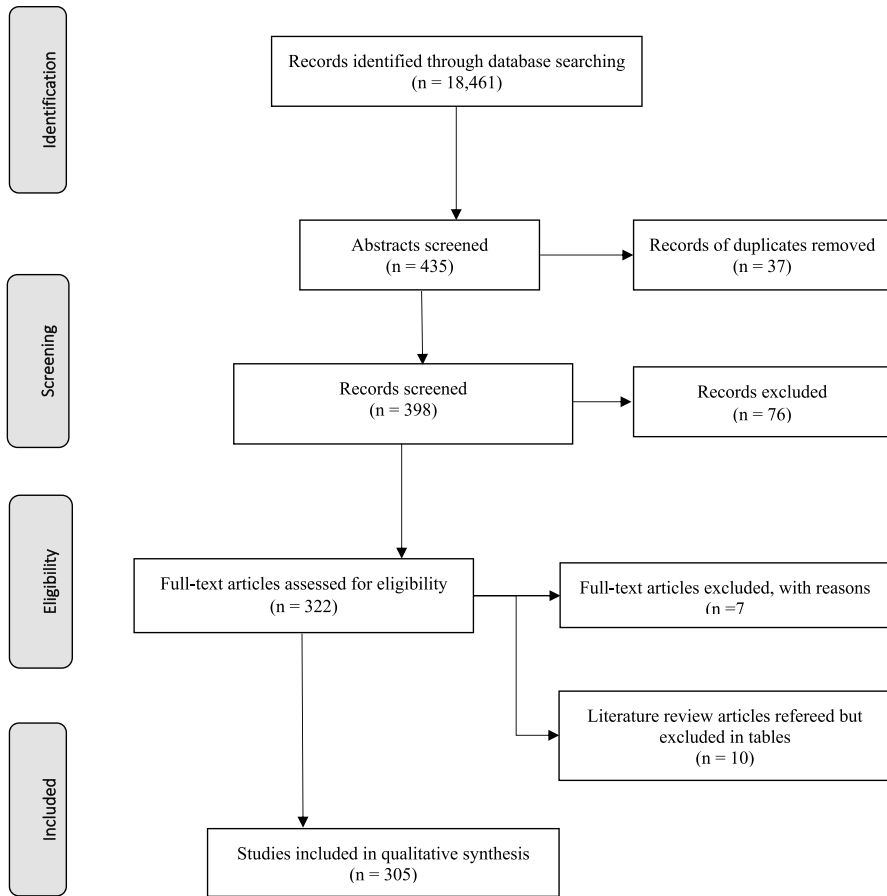


Fig. 1 PRISMA flow chart. *Notation:* Authors' own figure, adapted from Moher et al. (2009, 2010)

(Weight of Evidence C), as well as an overall judgment (Weight of Evidence D). To avoid overlooking significant contributions, we also screened the references cited at least five times in the selected 305 articles for their relevance to the criteria outlined in Table 1.

The PRISMA flow chart depicted in Fig. 1 demonstrates the selection process, which resulted in the inclusion of 305 articles that met all the pre-defined criteria. The subsequent analysis involved the collection of article characteristics such as the country of origin and research methodology. The empirical findings of the selected articles were then analyzed and categorized based on recurring themes. Additionally, the articles were analyzed in terms of the selection of input–output variables.

Table 2 Frequency statistics of reviewed studies. *Source:* Authors' own table

Methods	No. of papers (%)
Financial ratios	33 (11%)
Frontier methods	264 (89%)
Parametric	83 (28%)
SFA	65 (22%)
TFA	3 (1%)
DFA	15 (5%)
Non-parametric	181 (61%)
DEA	178 (60%)
FDH	3 (1%)
Two-stage	69 (23%)
Tobit	18 (26%)
GLS	12 (17%)
Bootstrap	9 (13%)
OLS	10 (15%)
Logit	3 (4%)
TOPSIS	3 (4%)
Fixed effect	6 (9%)
Other	8 (12%)
<i>Field distribution</i>	
Islamic banking papers	105 (35%)
Conventional banking papers	158 (51%)
Islamic versus conventional banking papers	42 (14%)
Total number of papers	305

This table presents efficiency methods and variable selection frequency statistics in %. Percentages under each of the inputs and outputs do not add to a 100% due to the overlap across different studies. Others category in the two-stage applications include generalized method of moments (GMM), seemingly unrelated regressions, random effects model (REM), fixed effect model (FEM), slack-based measure. Two-stage analysis is applied as a second stage econometric analysis in selective studies

3.2 Summary statistics of reviewed articles

The statistical data presented in Table 2 indicates that among the selected 305 articles, 89% of the studies preferred frontier methods for their technical efficiency estimations, with 28% utilizing parametric and 61% non-parametric methods. Specifically, the non-parametric DEA method was the most frequently used (60%), followed by SFA (22%) among the parametric methods. Moreover, two-stage techniques such as Tobit (26%) and GLS (17%) were the most commonly used methods to analyze the impact of environmental variables on efficiency scores. Interestingly, the least frequently used methods were the Thick Frontier Approach (TFA) (1%),

Free Disposable Hull (FDH) analysis (1%), and the Technique for Order Preference by Similarity to Ideal Solution (TOPSIS) (4%).

In terms of bank type, the analysis shows that 51% of the studies focused solely on conventional banks (CBs), while 35% of the studies analyzed the technical efficiency scores of Islamic banks (IBs) only. Furthermore, 14% of the studies compared the technical efficiency scores of IBs versus CBs. It is worth noting that the paper excluded ten literature review articles, as they did not meet the inclusion criteria of being banking application papers.

This literature review analyzed a total of 305 articles, which were published in 128 scientific journals. The majority of the articles were published in journals with a focus on business, economics, and finance. Notably, the *Journal of Banking and Finance* had the highest number of published articles (27), followed by the *European Journal of Research* (13), *Managerial Finance* (11), *Expert Systems with Applications* (8), the *International Journal of Islamic and Middle Eastern Finance and Management* (8), the *Journal of Productivity Analysis* (7), and *Research in International Business and Finance* (7).

4 Review of studies

4.1 Regulation as Shariah principals

Islamic banks (IBs) are subject to strict regulatory guidelines rooted in Shariah principles (Elamer 2017; Elamer et al. 2019). The unique characteristics of Islamic finance instruments can pose significant challenges for IBs in terms of efficiency and profitability. For instance, some of the specific forms of Islamic banking/finance, such as *mudarabah* (profit-sharing), *murabaha* (cost-plus), *musharakah* (joint-venture), *bai-muajjal* (deferred payment sale), *ijarah* (leasing), and *istisna* (processing and manufacturing contracts) may increase traditional agency conflicts, such as adverse selection and moral hazard problems, and worsen non-traditional agency problems by providing more opportunities for managerial expropriation of bank assets (Elamer 2017; Elamer et al. 2019).

However, some researchers have argued that these strict guidelines are also among the key factors that have enabled IBs to withstand the 2007/08 financial crisis better than most conventional banks (CBs) (Willison 2009; Yilmaz 2009; Hasan and Dridi 2010). These studies have also demonstrated that IBs have exhibited relatively high levels of efficiency and profitability during periods of financial uncertainty. Therefore, identifying the factors that account for the relatively higher performance metrics observed for IBs represents an important research agenda.

The extant literature indicates that the differences in the banking practices between Islamic and conventional banks account for the divergent efficiency and stability levels observed between the two types of banks. Islamic banking operates under the guidance of Shariah principles that prohibit the charging of interest (Hasan and Bashir 2003a, b, c). Instead, IBs generate earnings through transactional and intermediation contracts (El-Hawary et al. 2004). The main source of difference between Islamic and conventional banks is their approach to the use of money

(Al-Omar and Abdel-Haq 1996). In this regard, IBs are prohibited from charging interest and, therefore, offer alternative financial products and services that conform to the principles of Shariah law, which allows for profit and loss sharing (PLS) through instruments like Musharaka and Mudarabah.

Chong and Liu (2009) defined the PLS model as a system in which profits and losses are shared among banks, depositors, and borrowers. Murabaha, which is commonly used for financing real estate, consumer durables, and the acquisition of raw materials, equipment, or machinery, is the most popular method of Islamic financing (Ahmad and Haron 2002). Empirical research by Beck et al. (2013), Metwally (1997), and Olson and Zoubi (2008) has shown that the activities of IBs differ from those of CBs. However, Aggarwal and Yousef (2000), Chong and Liu (2009), Khan (2010), Ariff and Rously (2011), and Suzuki et al. (2020) have argued that there is no fundamental difference between the banking activities of IBs and CBs.

4.2 Stability

Bank efficiency measurement has been a topic of interest in academic research and policymaking for a considerable period, with a noticeable increase in attention following the global financial crisis. Therefore, investigating the relationship between banks' efficiency and stability has become an important topic. Issavi et al. (2018) employed DEA as the analysis method and the intermediation approach to select variables to examine the relationship between efficiency and stability of eleven Iranian private and public banks between 2004 and 2016. The findings suggested an inverse relationship between banks' efficiency and stability indexes, with bank stability significantly impacting financial stability in an economy.

The literature presents a lack of consensus on the stability of Islamic banks (IBs) compared to their conventional counterparts (CBs). Kuran (2004) indicated that the stability of IBs is not higher than CBs, while Kabir and Worthington (2017) found IBs to be less stable than CBs in their analysis of 16 developing economies between 2000 and 2012. Ghosh (2016) proposed that capital adequacy ratios and reserve requirements are the most important factors for bank stability, with Beck et al. (2013) and Khediri et al. (2015) corroborating that liquidity and capitalization ratios are better in IBs, thereby improving their stability. Abedifar et al. (2015) found this to be the case in their analysis of data from 553 banks in 24 countries, while Rahim and Zakaria (2013) confirmed this for Malaysian IBs.

The Organisation for Economic Co-operation and Development (OECD) (2010) reports that banks that rely primarily on interbank funding and money markets suffered severe losses during the global financial crisis. In contrast, IBs, which rely heavily on depository funding, proved to be more stable than CBs. Khan (1986) found that IBs apply 100% reserve for demand deposits and are expected to be more stable. However, high reserve requirements mean IBs have less available funds for investment, leading to lower efficiency compared to CBs.

4.3 Scale efficiency

Efficiency is a key aspect of the banking industry, and Islamic banks (IBs) have been subject to numerous studies examining their efficiency. One important component of efficiency is scale efficiency, which is the ability of a bank to optimize its operations in relation to its size. Several studies have investigated the impact of scale efficiency on the overall technical efficiency of IBs.

Havid and Setiawan (2015) found a statistically significant correlation between scale inefficiency and technical inefficiency in Indonesian IBs. Yildirim (2015) demonstrated that scale inefficiency is the most important cause of technical inefficiency in IBs in Malaysia. Rahman and Rosman (2013) examined IBs in Asian and MENA countries, concluding that IBs experienced scale efficiency problems. By reviewing numerous studies in the literature, Rahman and Rosman (2013) identified Malaysia as one of the most popular countries which attracted the interest of researchers on the efficiency of IBs relative to conventional banks (CBs). Rahman and Rosman (2013) also showed that Zainal and Ismail (2012), Ada and Dalkilic (2014), Yildirim (2015), Sufian et al. (2016) and Kamarudin et al. (2017a, b), Abdul-Majid et al. (2008, 2010) preferred stochastic frontier analysis (SFA) and Alrawashedh et al. (2014) chose financial ratios in measuring efficiency. Findings from these studies are mixed. For example, Alrawashedh et al. (2014) and Kamarudin et al. (2017a, b) noted that IBs are more efficient/profitable than CBs, contrary to the conclusions by Abdul-Majid et al. (2008, 2010, 2011a, b).

Comparing the Malaysian and Turkish banking sectors, Ada and Dalkilic (2014) utilized the Malmquist Total Factor Productivity (TFP) index as well as data envelopment analysis (DEA) and proposed that TFP change decreased in Turkey during 2010–2011 compared to 2009–2010, while it increased for most banks in Malaysia. In addition, scale efficiency was higher in Turkey during 2009 but lower for Malaysian banks in 2010 and 2011. Further, Yildirim (2015) identified scale efficiency as the main source of overall technical efficiency. This is similar to a report by Zainal and Ismail (2012) that the technical efficiency and scale efficiency of domestic IBs are higher, while foreign IBs operated at higher pure technical efficiency. Berger (2007) investigated bank efficiency differences in various countries and compared the efficiency divergence among foreign and domestically owned banks. Findings indicated that foreign-owned banks have a disadvantage compared to domestic banks in developing countries.

Singh and Fida (2015) investigated the technical efficiency of Omani commercial banks by using DEA. Technical efficiency scores were decomposed into pure and scale efficiency components. Results suggested that scale efficiency has a higher impact on technical efficiency than pure technical efficiency. In addition, the largest bank of Oman is experiencing decreasing returns-to-scale. In the second stage analysis, the impact of capital adequacy, bank size, liquidity, and profitability on efficiency is examined by using the Tobit model. Liquidity and profitability are found to be significant, whilst bank size is an insignificant factor in bank efficiency.

Several studies have applied both parametric and non-parametric methods to try to identify consistency among the results. These include, among others, Cummins and Zi (1998), Bauer et al. (1998), Hassan (2005, 2006), and Nguyen et al. (2016),

who concluded that average efficiency scores varied significantly among the methods. Even though efficiency scores and rankings of banks are similar among different parametric methods, studies confirmed that the findings from parametric and non-parametric methods are inconsistent and rankings of banks are diverse (Yildirim and Philippatos 2007; Maudos et al. 1999; Weill 2004, 2009). Perera et al. (2007), Hauner and Peiris (2008), and Camanho and Dyson (1999) found bank's size as the main factor on efficiency due to scale effects. Consistent with these studies, Shamsuddin and Xiang (2012) illustrated that large banks in Australia experienced higher cost and technical efficiency than small banks, whilst lower profit efficiency.

Last but not the least point on scale efficiency, Kassim et al. (2009) showed that IBs in Malaysia are more sensitive to monetary policy changes than CBs. In line with this finding, analyzing the Turkish banking sector, Ergeç and Arslan (2013) concluded that IBs are more sensitive to interest rate change than CBs. Therefore, sensitivity to interest rate changes could be suggested as another important factor that should be considered when measuring the efficiency scores of IBs (Table 3).

4.4 Variable selection

The process of selecting appropriate variables to measure banks' economies of scale, efficiency, and productivity is a complex undertaking due to the intangible nature of the products offered to customers (Olgu 2007). Within the literature, there is no consensus on how to select input and output variables, and the Production, Value-Added, and Intermediation approaches are the three primary methods utilized, as shown in Table 4.

In the Production approach, banks are defined as firms that convert labor and capital into deposits and loans. New variable selection applications have been introduced by Resti (1997), Favero and Papi (1995), Bauer et al. (1993), Berger and DeYoung (1997), and Swank (1996). The Value-Added method, on the other hand, classifies assets or liabilities as inputs or outputs depending on whether they create or destroy value (Berger and Humphrey 1992). Finally, the Intermediation approach perceives banks as firms that transfer money from depositors to borrowers.

Table 4 provides insight into the most commonly used inputs and outputs for measuring banks' economies of scale, efficiency, and productivity. The selected inputs include labor, deposits, personnel expenses, and physical capital, while off-balance-sheet items, loans, and other earning assets are commonly used as outputs. The selection of inputs, however, remains largely dependent on the investigator's preferences. Nonetheless, the literature provides evidence on the role of deposits as either inputs or outputs. Empirical tests conducted in various studies, such as Hughes and Mester (1993) and Hughes and Mester (2019), indicate that deposits typically function as inputs. Personnel expenses have also been highlighted as a crucial input variable by Chortareas et al. (2012), Drake and Hall (2003), and Lozano-Vivas et al. (2002), given their significant role in general and administration expenditures (Johnes et al. 2014). Table 5 presents a frequency distribution of input-output variable selection based on the approaches employed in the reviewed studies.

Table 3 Survey of studies on Islamic and conventional bank efficiency. *Source:* Authors' own table

Author/s	Countries	Method	Findings
<i>Islamic bank efficiency studies</i>			
Najjar (2013)	Bahrain	Financial Ratios	Corporate excellence identified in asset management and value equity shares
Saaid (2005)	Sudan	SFA	No comparison; IBs only
Saaid et al. (2003)	Sudan	SFA	No comparison; IBs only
Hassan (2005, 2006)	21 Islamic countries	SFA and DEA	No comparison; IBs only
Hassan and Hussein (2003)	Sudan	SFA	No comparison; IBs only
Hussein (2004)	Bahrain	SFA	No comparison between efficiency of IBs and CBs
Yudistira (2004)	Qatar, Jordan, UAE, Algeria, Malaysia, Bahrain, Yemen, Egypt, Sudan, Gambia, Kuwait and Indonesia	DEA	No comparison; IBs only
Zainal and Ismail (2012)	Malaysia	DEA	TE: domestic IBs > foreign IBs SE: domestic IBs > foreign IBs PTE: domestic IBs < foreign IBs
Viverita et al. (2007)	Qatar, Kuwait, Algeria, UAE, Bahrain, Yemen, Brunei, Jordan, Bangladesh, Egypt, Malaysia, Sudan and Indonesia	DEA	No comparison; IBs only
Kamarudin et al. (2017a, b)	Brunei, Indonesia, and Malaysia	DEA	Efficiency: domestic IBs > foreign IBs
Khediri et al. (2015)	Malaysia	Financial Ratios	Profitability and liquidity: IBs > CBs Risk: IBs < CBs
Alam (2013)	Egypt, Indonesia, Bahrain, Kuwait, Bangladesh, Malaysia, Qatar, Pakistan, Turkey, Saudi Arabia, UAE	DEA + SUR	Regulation, strict monitoring and increased supervision have a positive impact on IB efficiency. But, decreased efficiency observed with higher restrictions on IB' risk taking behaviour

Table 3 (continued)

Author/s	Countries	Method	Findings
Nguyen (2018)	Vietnam, Indonesia, the Philippines, Cambodia, Malaysia, Thailand	SFA	More income diversified banks have lower cost efficiency while more asset diversified ones have lower persistent cost efficiency. More funding diversified banks have higher profit efficiency. Both funding and asset diversified foreign banks are less profit efficient
Rossazana and Chiang (2016)	Malaysia	DEA + OLS	Competitive banking sector due to less market concentration and banks are operating below their capacity. Market concentration and bank efficiency determines profitability performance of banks
Chan et al. (2015)	Malaysia, Indonesia, Singapore, the Philippines, Thailand	DEA + GMM	There is a need for increased market discipline, monitoring and transparency
<i>Islamic versus conventional bank efficiency studies</i>			
Milhem and Istaiteyeh (2015)	Jordan	Financial Ratios	<i>Profitability:</i> IBs < CBs <i>Liquidity:</i> IBs > CBs <i>Efficiency:</i> IBs < CBs <i>Riskiness:</i> IBs < CBs
Alrawashedh et al. (2014)	Malaysia	Financial Ratios	<i>Profitability and productivity:</i> IBs > CBs
Saeed and Izzeldin (2016)	Bahrain, Qatar, Kuwait, UAE, Saudi Arabia, Bangladesh, Pakistan, Indonesia	SFA + VAR	CBs in GCC countries have lower efficiency with decreased default risk. An inverse relationship between profit efficiency and default risk for IBs. Efficiency and default risk are early warning indicators of IB stability
Said (2012)	USA and randomly chosen countries	DEA	No comparison between efficiency of IBs and CBs
Hamid (1999)	Bangladesh	Financial ratios	<i>Profitability and liquidity:</i> IBs > CBs <i>Productivity:</i> IBs > CBs

Table 3 (continued)

Author/s	Countries	Method	Findings
Hassan and Bashir (2003c)	21 Islamic countries	Financial ratios	<i>Asset quality</i>: IBs > CBs <i>Capital adequacy</i>: IBs > CBs <i>Liquidity</i>: IBs < CBs <i>Profitability</i>: IBs > CBs <i>Cost efficiency</i>: IBs < CBs Growth rate in equity, deposits, investments and total assets of IBs > CBs
Iqbal (2001)	12 Islamic banks from various countries	Financial ratios	<i>Efficiency</i>: IBs > CBs <i>Profitability</i>: IBs > CBs <i>Liquidity</i>: IBs < CBs <i>Risk</i>: IBs < CBs
Kader et al. (2007)	UAE	Financial ratios	CBs and banks from GCC experienced lower efficiency associated with a decrease in default risk but inversely related in IBs <i>Efficiency</i>: IBs < CBs
Saeed and Izzeldin (2016)	UAE, Qatar, Pakistan, Bahrain, Indonesia, Bangladesh, Saudi Arabia and Kuwait	SFA	
Srairi (2010)	UAE, Qatar, Bahrain, Saudi Arabia, Oman and Kuwait	SFA	
Zuhroh et al. (2015)	Indonesia	SFA	
Majid et al. (2003)	Malaysia	SFA	
Mokhtar et al. (2006)	Malaysia	SFA	
Kamarudin et al. (2016a, b)	Bahrain, Oman, Kuwait, Saudi Arabia, Qatar, UAE	DEA + OLS	<i>Technical efficiency</i>: IBs > CBs <i>Cost efficiency</i>: IBs < CBs <i>Efficiency</i>: IBs = CBs <i>Efficiency</i>: IBs < CBs IBs > Foreign > Domestic banks
Abdul-Majid et al. (2010)	Yemen, Indonesia, Bahrain, Sudan, Malaysia, Bangladesh, Tunisia, Iran, Lebanon, Jordan	SFA	IBs are less efficient than CBs. Macroeconomic variables are important on revenue efficiency <i>Efficiency</i>: IBs < CBs

Table 3 (continued)

Author/s	Countries	Method	Findings
Al-Jarrah and Molyneux (2005)	Saudi Arabia, Egypt, Bahrain and Jordan	SFA	Efficiency of IBs and CBs are measured but variation not tested
El-Gamal and Inanoglu (2005)	Turkey	SFA	<i>Efficiency</i> : IBs = CBs
Abdul-Majid et al. (2008, 2011a, b)	Malaysia	SFA	<i>Efficiency</i> : IBs < CBs
Batir et al. (2017)	Turkey	DEA + Tobit	<i>Efficiency</i> : IBs > CBs. Expenses and loan quality have significant negative impact on efficiency of CBs and positive on IBs. Total loans have a significant positive impact on efficiency of both IBs and CBs while external variables have a significant negative impact
Moin (2008)	Pakistan	Financial ratios	<i>Liquidity</i> : IBs = CBs <i>Efficiency</i> : IBs < CBs <i>Profitability</i> : IBs < CBs <i>Risk</i> : IBs < CBs
Sufian et al. (2012)	Malaysia	DEA	<i>Efficiency</i> : IBs > CBs
Ismail et al. (2013)	Malaysia	DEA	<i>Efficiency</i> : IBs < CBs
Johnes et al. (2009)	UAE, Kuwait, Bahrain, Saudi Arabia, Qatar and Oman	DEA	<i>Efficiency</i> : IBs > CBs
Kamarudin et al. (2016a, b)	GCC countries	DEA	<i>Efficiency</i> : IBs < CBs
Johnes et al. (2014)	18 Muslim countries	DEA, Meta Frontier Approach, and two stage approach	<i>Efficiency</i> : IBs > CBs
Mokhtar et al. (2007, 2008)	Malaysia	DEA	<i>Efficiency</i> : IBs < CBs
Shawtari et al. (2019)	Yemen	DEA + OLS	Bank margin steadily decreased except 2011. CBs have higher bank margin than IBs. Bank margins are not related with efficiency but are affected by capitalisation, size, cost of reserves and liquidity

Table 3 (continued)

Author/s	Countries	Method	Findings
Samad (2004)	Bahrain	Financial ratios	<i>Liquidity risk</i> : IBs < CBs
Samad and Hassan (1999)	Malaysia	Financial ratios	<i>Profitability</i> : IBs < CBs <i>Managerial efficiency</i> : IBs = CBs <i>Efficiency</i> : IBs = CBs
Sarker (1999)	Bangladesh	Financial ratios	
Scale efficiency			
Almaqtari et al. (2018)	India	Financial Ratios	Bank size, number of branches, assets management ratio, operational efficiency and leverage ratio are the most important bank specific factors on profitability. Macroeconomic factors have significant impact on ROA and ROE, but demonization has no impact on ROE
Huang et al. (2017)	China	Network SFA	Joint-stock banks are the most technically efficient while larger commercial banks are the least technically efficient
Yannick et al. (2016)	Cote d'Ivoire	DEA (window analysis)	Ivorian banks are inefficient in loan allocation <i>Efficiency</i> : Foreign banks > public banks Inefficiency is due to scale inefficiency
Ada and Dalkilic (2014)	Malaysia and Turkey	DEA, Malmquist	Average scale efficiency is higher in Turkey in 2009 but lower in 2010 and 2011 than Malaysian banks. TFP change decreased in Turkey during 2010–11 compared to 2009–2010, while increased in Malaysia except from 3 banks
Rahman and Rosman (2013)	MENA countries	DEA	Technical inefficiency of IBs is due to scale inefficiency
Rosman et al. (2014)	Middle Eastern and Asian countries	DEA	Most IB operate inefficiently at DRS, profitability and capitalization are the main determinants of IB efficiency

Table 3 (continued)

Author/s	Countries	Method	Findings
Saha et al. (2015)	Malaysia	DEA	Positive <i>relationship</i> between bank size, capital, profit and efficiency
Bauer et al. (1998)	US	DEA, SFA, TFA, DEA	Negative <i>relationship</i> between expenses, non-performing loans and efficiency
San-Jose et al. (2014)	Spain	DEA + OLS	Consistency among parametric approaches but inconsistency among non-parametric and parametric approaches
<i>Ownership structure</i>			Investment banks are socially more efficient than other banks, but they all have similar efficiency scores
Sufian and Kamarudin (2014)	Malaysia	DEA, Malmquist, Bootstrap	Domestic and foreign banks experienced productivity growth due to progress in technological change
Azad et al. (2017)	Malaysia	DEA + Bootstrap	Bank ownership, bank nature and GDP have significant impact on bank efficiency. IBs outperformed CBs
Chen et al (2018)	China	DEA + Support Vector Machine Regression	Overall efficiency is low due to ownership and cost structure. Policy implications proposed to improve corporate governance and credit allocation
Matousek and Taci (2004)	Czech Republic	DFA	<i>Efficiency</i> : Foreign banks > other banks
Wanke et al. (2019)	Algeria, Egypt, Israel, Kuwait, Malta, Oman, Saudi Arabia, Bahrain, Iran, Jordan, Lebanon, Morocco, Qatar, UAE	Dynamic Network DEA	Bank type, origin and ownership impact efficiency levels differently in terms of profit sheet, balance sheet and financial health indicators and also culture and regulation barriers are important at country level

Table 3 (continued)

Author/s	Countries	Method	Findings
Fukuyama and Matousek (2011)	Turkey	Network DEA	Gap exists between efficiency scores of best and worst banks and there is no evidence of foreign banks having higher efficiency than domestic banks

Table 4 Survey of studies on input–output variable selection. *Source:* Authors' own Table

Author	Sample	Method	Approach	Inputs	Outputs
Alam (2013)	Egypt, Indonesia, Bahrain, Kuwait, Bangladesh, Malaysia, Qatar, Pakistan, Turkey, Saudi Arabia, UAE <i>From 2006 to 2010</i>	DEA + SUR	Intermediation	Personnel expenses Fixed assets Deposits Short-term funding	Total loans Total earning assets
Azad et al. (2017)	Malaysia <i>From 2010 to 2015</i>	3-Stage Network DEA	Intermediation	Node 1: equity, deposits Node 2: earning assets, interest expense Node 3: loans, non-interest expense	Node 1: earning assets, non-earning assets Node 2: loans, liquid assets Node 3: net income, loan loss provisions
Batir et al. (2017)	Turkey <i>From 2005 to 2013</i>	DEA + Tobit	Intermediation	Personnel expenses, fixed assets, total deposits	Total loans, OBS
Belanès et al. (2015)	Saudi Arabia, Bahrain, Qatar, Kuwait, UAE <i>From 2005 to 2011</i>	DEA	Intermediation	Salary expense, fixed assets, total deposits	Total loans, other revenues, liquid assets
Henriques et al. (2018)	Brazil <i>From 2012 to 2016</i>	DEA	Intermediation	Fixed assets, total deposits, personnel expenses	Total loans
Huang et al. (2017)	China <i>From 2002 to 2015</i>	Network SFA	Intermediation	Stage 1: price of labour, physical capital Stage 2: deposits, price of labour, physical capital	Stage 1: deposits Stage 2: total loans, investments, non-interest income
Kamarudin et al. (2017a, b)	Malaysia, Brunei, Indonesia <i>From 2006 to 2014</i>	DEA	Intermediation	Deposits, labour, capital	Loans, investments
Rossazana and Chiang (2016)	Malaysia <i>From 2000 to 2011</i>	DEA + OLS	Intermediation	Personnel expenses, deposits, short-term funding	Total loans, OEA

Table 4 (continued)

Author	Sample	Method	Approach	Inputs	Outputs
Miah and Uddin (2017)	Bahrain, Qatar, Kuwait, UAE, Saudi Arabia <i>From 2005 to 2014</i>	Ratio analysis, SFA, OLS	Intermediation	Cost of labour, cost of capital	Loans, securities
Saeed and Izzeldin (2016)	Bahrain, Qatar, Kuwait, UAE, Saudi Arabia, Bangladesh, Pakistan, Indonesia <i>From 2002 to 2010</i>	SFA + VAR	Intermediation	Net total loans, OEA	Price of physical capital, price of labour, price of financial capital
San-Jose et al. (2014)	Spain <i>From 2000 to 2011</i>	DEA + OLS	Intermediation	Equity, total assets, total deposits	Profit, risk, social contracts, no of jobs, consumer credit
Zimková (2014)	Slovakia <i>2012</i>	DEA	Intermediation	Fixed assets, deposits, no of employees	Earning assets
Chan et al. (2015)	Malaysia, Indonesia, Singapore, the Philippines, Thailand <i>From 1998 to 2012</i>	DEA + GMM	Intermediation	Expenses, interest expense, other non-interest expense	Interest income, investments, income from OBS
Kamarudin et al. (2016a, b)	Bahrain, Oman, Kuwait, Saudi Arabia, Qatar, UAE <i>From 2007 to 2011</i>	DEA + OLS	Intermediation	Personnel expenses, deposits	Loans, income
Ada and Dalkilic (2014)	Malaysia and Turkey <i>From 2009 to 2011</i>	DEA Malmquist	Intermediation	Total equity Total assets	Net income/loss Total deposits
Al-Jarrah (2007)	Saudi Arabia, Egypt, Bahrain and Jordan <i>From 1992 to 2000</i>	DEA	Intermediation	Physical capital Labour Deposits	Loans Off-balance sheet Other earning assets (OEA)
Al-Jarrah and Molyneux (2005)	Egypt, Saudi Arabia, Bahrain and Jordan <i>From 1992 to 2000</i>	SFA	Intermediation	Deposit Labour Physical capital	Total costumer loans Off-balance sheet items

Table 4 (continued)

Author	Sample	Method	Approach	Inputs	Outputs
Al-Muharrami (2007)	GCC countries <i>From 1993 to 2002</i>	DEA	Intermediation	Fixed assets Deposits Equity Labour	OEA Total loans Off balance sheet items Other operating incomes
Ariff and Can (2008)	China <i>From 1995 to 2004</i>	DEA Tobit	Intermediation	Physical capital Total deposits Number of employees	Investments Total loans
Ataullah and Le (2006)	India <i>From 1992 to 1998</i>	DEA	Intermediation	Interest expenses Operating expenses	Loans and advances Investment Interest income Operating income
Athanassopoulos (1997)	Greece Questionnaire	DEA	Intermediation	Non-interest expense Interest expense Employees ATMs terminals	Non -interest income
Athanassopoulos and Curram (1996)	UK Questionnaire	DEA Neural Networks	Intermediation	Counter transactions ATMs Potential Market Employees	Insurance policies sold Loans sales Investments
Avkiran (2009)	UAE 2005	Network DEA	Intermediation	Non-interest expenses Interest expense	Non-interest income Interest income
Ayadi et al. (1998)	Nigeria <i>From 1991 to 1994</i>	DEA	Intermediation	Total deposits Interest on deposits Personnel expenses	Non-interest income Total loans Interest income
Barros et al. (2011)	China <i>From 1998 to 2008</i>	DEA	Intermediation	Deposits Number of employees Total assets	Securities Loans

Table 4 (continued)

Author	Sample	Method	Approach	Inputs	Outputs
Barros et al. (2012)	Japan <i>From 2000 to 2007</i>	Russell Directional Dis- tance Function	Intermediation	Total deposits Physical capital Number of full time employees	Total loans
Batir et al. (2017)	Turkey <i>From 2005 to 2013</i>	DEA	Intermediation	Personnel expenses Fixed assets Total deposits	Off balance sheet items Total loans
Battacharya et al. (1997)	India <i>From 1986 to 1991</i>	DEA SFA	Intermediation	Operating expenses Interest expense	Investments Deposits Advances
Beccalli et al. (2006)	Spain, France, Italy, Ger- many, UK <i>From 1999 to 2000</i>	DEA SFA	Intermediation	Total expenses	OE/A Total loans
Bos et al. (2009)	European countries and USA <i>From 1993 to 2005</i>	SFA	Intermediation	Physical capital Financial capital Labour	Investments Loans
Brockett et al. (1997)	USA <i>From 1984 to 1985</i>	DEA CAMEL	Intermediation	Total deposits Interest expenses Furniture and equipment Buildings	Off-balance sheet items Loans net of unearned income Allowances for loan losses
Canhoto and Dermine (2003)	Portugal <i>From 1990 to 1995</i>	DEA	Intermediation	Physical capital Number of employees	Assets/liabilities Loans Interbank securities Deposits
Casu and Girardone (2009)	Spain, Italy, France, UK and Germany <i>From 2000 to 2005</i>	SFA and DEA	Intermediation	Interest paid Non-interest expense Total personnel expenses Other administrative expenses	OE/A Total loans

Table 4 (continued)

Author	Sample	Method	Approach	Inputs	Outputs
Casu and Molyneux (2003)	Italy <i>From 1996 to 1999</i>	DEA	Intermediation	Labour Deposits Capital	OEA Total loans
Chen and Yeh (2000)	Taiwan <i>1996</i>	DEA	Intermediation	Staff Deposits Assets	Non-interest income Provision of loan Portfolio investment
Chen et al. (2005)	China <i>From 1993 to 2000</i>	DEA	Intermediation	Capital Non-interest expenses Interest expenses	Non-interest income Deposits Loans
Chortareas et al. (2012)	27 EU countries <i>From 2001 to 2009</i>	DEA	Intermediation	Personnel expenses Fixed assets Deposits	OEA Total loans
Degl'Innocenti et al. (2017)	Top 1000 banks world-wide <i>From 2004 to 2010</i>	Order-M Approach	Intermediation	Total customer deposits Fixed assets Number of employees	Total securities Gross loans
Delis and Papanikolaou (2009)	Bulgaria, Slovenia, Estonia, Romania, Czech Republic, Lithuania, Poland, Hungary, Slovakia and Latvia <i>From 1994 to 2005</i>	DEA	Intermediation	Total deposits Operating expenses (non-interest and personnel expenses)	Total securities Total loans
Emrouznejad and Anouze (2010)	GCC countries <i>2009</i>	DEA	Intermediation	Total assets Deposits Capital	Net profit Loans
English et al. (1993)	USA <i>1982</i>	Shephard's distance function	Intermediation	Borrowings Capital Deposits Labour	Commercial loans Investments income Consumer loans Real estate loans

Table 4 (continued)

Author	Sample	Method	Approach	Inputs	Outputs
Favero and Papi (1995)	Italy 1991	DEA	Intermediation	Employees Capital Loanable funds Deposits	Non-interest income Loans Investments in securities
Fukuyama (1993)	Japan 1990	DEA	Intermediation	Deposits Capital Employees	Other revenues Loan revenue
Fukuyama (1996)	Japan 1992	DEA	Intermediation	Deposits Labour Capital	Securities Loans
Fukuyama and Matousek (2011)	Turkey From 1991 to 2007	Network DEA	Intermediation	Capital Labour	Securities Loans
Gardener et al. (2011)	Thailand, Malaysia, Indonesia, the Philippines and Vietnam From 1998 to 2004	DEA	Intermediation	Personnel expenses Fixed assets Deposits	OE Net loans
Isik and Hassan (2002)	Turkey From 1988 to 1996	DEA and Economic Frontier Approach	Intermediation	Deposits Capital Labour	OE Off balance sheet items Short-term loans Long-term loans
Isik and Hassan (2003)	Turkey From 1988 to 1996	DEA	Intermediation	Deposits Labour Physical capital	OE Loans Off-balance sheet items
Johnes et al. (2014)	18 Muslim countries From 2004 to 2009	DEA, Meta Frontier Approach	Intermediation	General expenses Deposits Equity Fixed assets	OE Total loans

Table 4 (continued)

Author	Sample	Method	Approach	Inputs	Outputs
Kablan and Yousfi (2003)	UK, Jordan, Iran, UAE, Kuwait, Sudan, Qatar, Egypt, Lebanon, Tunisia, Yemen, Saudi Arabia, Bahrain, Brunei, Malaysia and Pakistan <i>From 2011 to 2008</i>	SFA	Intermediation	Labour Physical capital Deposits	Net loans Net liquid assets Securities
Kamarudin et al. (2016a, b)	Bangladesh <i>From 2004 to 2011</i>	DEA	Intermediation	Deposits Labour Capital	Loans Investments
Kamarudin et al. (2017a, b)	Brunei, Indonesia and Malaysia <i>From 2006 to 2014</i>	DEA	Intermediation	Total deposits Labour Capital	Loans Investments
Lang and Welzel (1996)	Germany <i>From 1989 to 1992</i>	Translog Cost Function	Intermediation	Fixed assets Total cost Volume of labour Deposits Price of labour Price of deposits Price of capital No of employees Volume of deposits	Cash Real estate Short term loans to non-banks Fees and commissions Loans to banks Bonds Investment Long term loans to non-banks Number of offices Revenue from sales
Le (2017)	Vietnam <i>From 2008 to 2015</i>	DEA	Intermediation	Operating expenses Physical capital Deposits	Total loans Securities Off balance sheet items
Lee and Chih (2013)	China <i>From 2004 to 2011</i>	DEA, Tobit	Intermediation	Fixed assets Deposits	Investments Loans

Table 4 (continued)

Author	Sample	Method	Approach	Inputs	Outputs
Maresh and Rajeev (2009)	India From 1985 to 2004	SFA	Intermediation	Fixed assets Deposits Labour Borrowings Borrowed funds Labour	Non-interest income Investments Credits Interest margin OEA Loans
Mamatzakakis et al. (2008)	Slovenia, Slovakia, Hungary, Latvia, Poland, Lithuania, Czech Republic, Cyprus, Malta and Estonia	SFA	Intermediation		
Matousek and Taci (2004)	Czech Republic From 1993 to 1998	DFA	Intermediation	Average price of funds Average price of capital Average annual salary per employee	Average volume of demand deposits Average volume of loans
Mester (1996)	USA From 1991 to 1992	SFA	Intermediation	Deposits Labour Funding Physical capital	Agricultural loans Private loans to individuals Other loans Real estate loans Commercial and industrial loans Lease financing receivable Loans Securities Securities
Miah and Uddin (2017)	GCC countries From 2005 to 2014	Fin. Ratios, SFA, OLS	Intermediation	Cost of labour Cost of capital	
Mokhtar et al. (2006)	Malaysia From 1997 to 2003	SFA	Intermediation	Operating expenses Personnel and other expenses Total deposits	
Mokhtar et al. (2008)	Malaysia From 1997 to 2003	DEA	Intermediation	Total deposits Total overhead expenses	Total earning assets

Table 4 (continued)

Author	Sample	Method	Approach	Inputs	Outputs
Mostafa (2009)	IBs in middle East 2005	DEA	Intermediation	Assets Equity	Net profits ROA ROE
Moualhi (2015)	MENA From 2006 to 2012	DEA	Intermediation	Assets Total deposits	Investments Total income Total loans
Nguyen et al. (2016)	Vietnam From 2000 to 2014	DEA and SFA	Intermediation	Personnel Fixed assets Total deposits	OEI Net loans
Nikiel and Opiela (2002)	Poland From 1997 to 2000	DFA	Intermediation	Price of labour Interest rates on funds	Securities Household loans Business loans
Olson and Zoubi (2011)	10 MENA countries From 2000 to 2008	Translog Cost Function	Intermediation	Deposits, Labour Physical capital	Loans Securities
Ong et al. (2011)	Malaysia From 2002 to 2009	DEA	Intermediation	Total deposits Fixed assets	Total loans Total investments
Oral and Yolalan (1990)	Turkey From 1976 to 1986	DEA	Intermediation	Personnel expense Administrative expense Depreciation Interest expense	Interest earned Non-interest income
Pasioursa (2008)	95 countries 2003	DEA, Tobit	Intermediation	Interest and non-interest expense Equity Total deposits	Non-interest income OEI Loans

Table 4 (continued)

Author	Sample	Method	Approach	Inputs	Outputs
Rekik and Kalai (2018)	Malaysia, Egypt, Yemen, Syria, Sudan, Jordan, Iraq, Lebanon, Tunisia, Kuwait, UAE, Qatar, Bahrain, Saudi Arabia From 1999 to 2012	Financial ratios, Regression, SFA	Intermediation	Deposits Physical capital labour	Securities Liquid assets Net loans
Saeed and Izzeldin (2016)	Saudi Arabia, Kuwait, Bahrain, Qatar, Bangladesh, Pakistan, Indonesia and UAE From 2002 to 2010	SFA	Intermediation	Price of physical capital Price of labour Price of financial capital	Net total loans Other earning assets
Şakar (2006)	Turkey From 31 December 2002 to 31 March 2005	DEA Malmquist	Intermediation	Branch numbers Employees per branch Assets Loans Deposits	Interest income/assets Non-interest income/assets ROA Interest income/operating income ROE
Sufian (2006)	Malaysia From 2001 to 2004	DEA	Intermediation	Total deposits Labour Fixed assets	Income Total loans
Sufian (2009a)	Malaysia 1997	DEA	Intermediation	Labour Capital Interest expenses	Deposits Loans Investments
Sufian and Abdul Majid (2007)	Malaysia From 2002 to 2003	DEA	Intermediation	Interest Income Non-interest income	Personal expenses Non-interest expenses
Sufian and Kamarudin (2014)	Malaysia From 1998 to 2008	DEA	Intermediation	Total deposits Capital Labour	Total loans Investments Non-interest income

Table 4 (continued)

Author	Sample	Method	Approach	Inputs	Outputs
Sufian et al. (2012)	Malaysia <i>From 1998 to 2008</i>	DEA	Intermediation	Deposit Labour Physical capital	Loans Investments Off-balance sheet items
Sufian et al. (2013)	Malaysia <i>From 2006 to 2010</i>	DEA	Intermediation	Deposits Number of employees Physical capital	Loans Investments
Sufian et al. (2016)	Malaysia <i>From 1999 to 2008</i>	DEA	Intermediation	Total deposits Capital Labour	Total loans Investments Non-interest income
Tecles and Tabak (2010)	Brazil <i>From 2000 to 2007</i>	SFA	Intermediation	Deposits Number of employees Fixed assets Equity	Other non-interest fee based incomes Investments Loans and advances
Thoraneemitiyan and Avkiran (2009a, b)	Philippines, Indonesia, Thailand, South Korea and Malaysia <i>From 1997 to 2001</i>	DEA	Intermediation	Deposits Labour Capital Physical capital	Loans Investment and OEA Off-balance sheet items Fee income
Yannick et al. (2016)	Cote d'Ivoire <i>From 2008 to 2010</i>	DEA Window analysis	Intermediation	Deposits	Loans
Yildirim and Philippatos (2007)	12 transition countries <i>From 1993 to 2000</i>	SFA, DFA	Intermediation	Labour Deposits Physical capital	Investments Loans Deposits
Yilmaz and Gunes (2015)	Turkey <i>From 2007 to 2013</i>	DEA	Intermediation	Total deposits Capital	Total loans Total income Investments
Yin et al. (2013)	China <i>From 1999 to 2010</i>	SFA	Intermediation	Equity Deposits Fixed assets	Pre-tax profit or loans

Table 4 (continued)

Author	Sample	Method	Approach	Inputs	Outputs
Zhang et al. (2012)	China From 1999 to 2008	SFA	Intermediation	Interest expenses Non-interest expenses Net value of fixed assets	Net interest income Non-interest income Total deposits OEA Total loans
Hall et al. (2012)	Hong Kong From 2000 to 2006	DEA	Intermediation / Production	Total operating expenses Fixed assets Total provisions	Other operating income Net commissions Total loans OEA Trading income
Kenjegalieva et al. (2009)	Eastern European countries From 1999 to 2003	DEA	Intermediation/ Production	Loan loss provisions Labour Capital Deposits	Other income Net commissions OEA Loans
Holod and Lewis (2011)	Top tier bank holding companies From 1986 to 2008	DEA, Network DEA	Intermediation/production	Number of employees Fixed assets (Deposits)	OEA Total loans (Deposits)
Drake et al. (2009)	Japan From 1995 to 2002	DEA	Intermediation/Production/Revenue based	Total other operating expenses Total provision Total non-interest expense Total deposits Total operating expenses	Other operating income Net commission Total OEA Non-interest income Total loans
Shawtari et al. (2019)	Yemen From 2009 to 2013	DEA + OLS	No defined approach	Not identified	Not identified
Cherchye et al. (2001)	EU countries 1997	FDH and DEA	No defined approach	Operating costs Equity capital Debt capital	Total earning assets (securities)

Table 4 (continued)

Author	Sample	Method	Approach	Inputs	Outputs
Halme et al. (2014)	Finland <i>From 2007 to 2010</i>	FDH, FDH value efficiency	No defined approach	Investment services Financial services	Work of the sales force
Quaranta et al. (2018)	Italy <i>2014</i>	DEA, Collinearity, Clustering, Deterministic Frontier Model, Deterministic SF, SFA, DEA	No defined approach	Operating costs Number of employees	Total financial assets
Chen et al. (2018)	China <i>From 2008 to 2011</i>	DEA + Support Vector Machine Regression	Production	Loans, equity, operational costs, personnel expenses, no of employees, no of branches, depreciation	Total assets, fixed assets, gross loans, total securities, total customer deposits, pre-tax profit, net-interest income, total-non-interest income
Wanke et al. (2019)	Algeria, Egypt, Israel, Kuwait, Malta, Oman, Saudi Arabia, Bahrain, Iran, Jordan, Lebanon, Morocco, Qatar, UAE <i>From 2009 to 2013</i>	Dynamic Network DEA	Production	Net loans, total earning assets, non-earning assets, loan loss provisions	Net interest margin, equity, income
Du and Sim (2016)	China, Indonesia, Russia, India, Malaysia, Thailand <i>From 2002 to 2009</i>	DEA	Production	Fixed assets, total non-interest expense, interest expense	Net interest income, other operating income
Lozano-Vivas et al. (2002)	10 European countries <i>1993</i>	DEA	Production	Personnel expenses Non-interest expenses	OEA Deposits Loans

Table 4 (continued)

Author	Sample	Method	Approach	Inputs	Outputs
Paradi et al. (2011)	Canada 2001	DEA, Slacks-Based measure	Production (1) Interme- diation (2)	Other resources (1) Labour (1) Net non-performing (2) Loans (2) Fixed assets (2) Funding (2) Deposits (2)	Loans (1) Others (1) Deposits (1) Investments (2) Mortgages (2) Loans (2)
Azad et al. (2017)	Malaysia From 2009 to 2013	DEA + Bootstrap	Production, Intermedia- tion and Value Added	Production: interest expense, salary expense, operating expense Intermediation: total capi- tal, total deposits, salary expense Value-Added: total capital, salary expense, interest expense	Production: interest income, net income Intermediation: total loans Value-Added: total depos- its, total loans
Nguyen (2018)	Vietnam, Indonesia, the Philippines, Cambodia, Malaysia, Thailand From 2007 to 2014	SFA	Value-Added	Labour, capital, funds interest expense	Loans to customer, inter- bank loans, OE/A

Table 4 (continued)

Author	Sample	Method	Approach	Inputs	Outputs
Carvallo and Kasman (2017)	Argentina, Bolivia, Chile, Costa Rica, Ecuador, Bahamas, Brazil, Colombia, Dominican Republic, Guatemala, Mexico, Paraguay, Trinidad and Tobago, Venezuela, El Salvador, Honduras, Panama, Peru, Uruguay <i>From 1999 to 2013</i>	SFA	Value-Added	Price of labour and physical capital, price of borrowed funds	Total loans, OEA, total deposits, OBS
Bauer et al. (1998)	US <i>From 1977 to 1988</i>	DEA, SFA, TFA, DFA	Value-Added	Labour Physical capital Time deposits Purchased funds	Demand deposits Real estate loans Instalment loans Commercial loans
Berg et al. (1992)	Norway <i>From 1980 to 1989</i>	DEA Malmquist	Value-Added	Buildings Material Labour Machine	Short-term loans Long-term loans Demand deposits Time deposits Other services
Berg et al. (1993)	Finland, Norway and Sweden <i>1990</i>	DEA	Value-Added	Capital Labour	Number of branches Loans Deposits
De Young (1997)	USA <i>From 1984 to 1994</i>	DFA	Value-Added	Physical capital Borrowed funds Price of labour	Fee-based income Transactions Deposits Total loans
Dietsch and Lozano-Vivas (2000)	Spain and France <i>From 1988 to 1992</i>	DFA	Value-Added	Labour Financial factor Physical capital	Loans Assets Deposits

Table 4 (continued)

Author	Sample	Method	Approach	Inputs	Outputs
Gioakas (1991)	Greece 1988	DEA Cobb–Douglas	Value-Added	Utilized branch space Operating expenses Labour	Number of transactions
Golany and Storbeck (1999)	USA From 1992 to 1993	DEA	Value-Added	Labour Operating expenses Economic status Market size Competitive activities	Deposits No of accounts per customer Loans
Mukherjee et al. (2002)	India From 1996 to 1999	DEA	Value-Added	Net worth Borrowings Operating expenses Employees Number of branches Employees Capital	Non-interest income Interest income Deposits Advances Net profit Non-interest income Deposits Loans
Resti (1997)	Italy From 1988 to 1992	DEA SFA	Value-Added		
Zhao and Murinde (2011)	Nigeria From 1993 to 2008	DEA Conjectural variations regression	Value-Added	Interest expenses Non-interest expenses Financial capital	Deposits Loans
Sufian (2009b)	Thailand and Malaysia From 1992 to 2003	DEA	Value-Added and Inter-mediation	Labour Capital Interest expenses	Deposits Loans Investments

Table 5 Statistics on variable selection. *Source:* Authors' own Table

Variable selection			
Inputs	%	Outputs	%
<i>Intermediation approach (81%)</i>			
Labour	68	Loans	79
Deposits	72	Other earning assets	25
Capital	40	Investments	30
Assets	30	Interest income	5
Interest expense	18	Non-interest income	16
Non-interest expense	11	Off balance sheet items	14
<i>Value-added approach (12%)</i>			
Labour	90	Loans	82
Capital	64	Other earning assets	90
Deposits	9	Non-interest income	18
Interest expense	18		
Operating expense	27		
<i>Production approach (7%)</i>			
Labour	50	Loans	100
Non-interest expense	33	Other earning assets	83
		Deposits	50

Magrianti (2011) conducted a study that compared the efficiency scores of Indonesian Islamic banks (IBs) and conventional banks (CBs) using different variable selection approaches. The results revealed that CBs had above-average efficiency scores when assets and production methodologies were employed, whereas IBs had higher efficiency scores than average when the intermediation approach was used. The study also found that the Intermediation approach was the most commonly used approach (81%), followed by the Value-Added approach (12%) and the Production approach (7%). 'Labor' was the most frequently selected input variable, while 'loans' was the most frequently chosen output variable. The review suggests that including both 'interest expense' and 'non-interest expense' as inputs, and 'interest income' and 'non-interest income' as outputs, could significantly affect efficiency scores when comparing IBs and CBs.

4.5 Incorporating environmental variables

Efficiency measurement methods were initially applied in individual country studies. However, in the last decade, cross-country studies have become more popular in order to capture the impact of country-specific characteristics, such as regulation, market structure, macroeconomic conditions, and various bank-specific factors. Studies such as Pastor et al. (1997), Fecher and Pestieau (1993), and Berg et al. (1993) employed common or country frontiers, using both Data Envelopment Analysis (DEA) and the Distribution Free Approach (DFA) in their cross-country

analyses. Nevertheless, they failed to account for the potential influence of environmental variables over which bank managers have no control. Applying a common frontier assumes that all decision-making units use the same technology, which could lead to misleading results (Chaffai et al. 2001). Therefore, Pastor et al. (1997) and Chaffai et al. (2001) recommend incorporating a range of environmental variables in empirical modelling of banking efficiency, including customers' ease of access to banking services, intermediation, concentration, and average capital ratios.

Altunbas and Chakravarty (1998), Cavallo and Rossi (2001), and Carbo et al. (2003) were among the first to conduct cross-country studies on European countries. Subsequent studies examined transition countries (Bonin et al. 2005; Kasman 2005), countries in Latin America and the Caribbean (Carvallo and Kasman 2005), developing countries (Boubakri et al. 2005; Clarke et al. 2005), and the achievements of Asian countries (Karim 2001; Williams and Nguyen 2005). More recently, researchers have compared the performance of Islamic banks (IBs) with conventional banks (CBs) in response to the increasing use of Islamic banking in many countries (Alpay and Hassan 2007; Al-Jarrah and Molyneux 2005; Yudistira 2004; Brown 2003; Hassan 2003). However, controlling for environmental variables remains a controversial issue.

The "two-stage" methodology is often used to control for environmental factors. In this method, efficiency scores measured in "stage one" using either of the frontier techniques or the financial ratios discussed in the previous sections are regressed on selected environmental factors in "stage two." Bashir (1999, 2001) used a two-stage approach to confirm the fundamental components of performance among IBs using Middle Eastern bank-level data. The results suggest that bank-specific factors such as non-interest-earning assets, customer short-term funding, and overheads influence banks' estimated efficiency scores. Bashir (1999, 2001) also recommended a negative correlation between bank deposits (measured as share reserves) and performance metrics.

A bootstrap approach is generally used in the second stage of analysis. However, Casu and Molyneux (2003) used it in the first stage to demonstrate the correlation among the covariates of the second-stage regression and error terms from the first stage. Brissimis et al. (2008) and Delis and Papanikolaou (2009) created an algorithm that relied on a double bootstrap procedure. Other models used to detect the impact of environmental variables on bank efficiency include Logit, Gaussian and Markov, and Bootstrap-Tobit, which were employed by Pastor (2002) and Casu and Girardone (2004), Wang and Huang (2007), and Casu and Molyneux (2003) and Hahn (2007) respectively. Several studies have utilized a two-stage approach to examine bank efficiency, with a focus on the Malaysian banking sector. Ismail et al. (2013), Saha et al. (2015), Defung et al. (2016), Sufian et al. (2016), and Wanke et al. (2016a, b, c) are among the most recent studies that have used this approach. With the exception of Defung et al. (2016), which employed Tobit to examine Indonesian banks, the other studies have focused on the Malaysian banking sector. The first two studies used Tobit, while Sufian et al. (2016) preferred Bootstrapping and Wanke et al. (2016a, b, c) utilized TOPSIS. According to Table 2, Tobit regression was the most commonly used two-stage technique (about 26% of the reviewed studies), followed by Generalized Least Squares (GLS), which accounted for around

17% of studies. The remaining 32% of studies employed various techniques such as Bootstrap, Ordinary Least Squares (OLS), and TOPSIS.

A number of studies, including those by Sufian and Noor (2009), Ismail et al. (2013), and Saha et al. (2015), have used a two-stage Data Envelopment Analysis (DEA) approach (DEA and Tobit). Sufian and Noor (2009) examined the efficiency of Islamic Banks (IBs) in the Middle East and North Africa (MENA) and Asian countries between 2001 and 2006. They found that loans, size, capitalization, and profitability were positively correlated with bank efficiency, while non-performing loans were negatively correlated. Saha et al. (2015) focused solely on the efficiency scores of Conventional Banks (CBs) in Malaysia between 2005 and 2012, and their findings were consistent with those of Sufian and Noor (2009). Ismail et al. (2013) analyzed both CBs and IBs in Malaysia between 2006 and 2009. They found that CBs had higher efficiency scores than IBs, and that there was a negative relationship between equity, size, and efficiency of IBs, but a positive relationship for CBs. Interestingly, a positive relationship was found to exist between expenses and efficiency in both IBs and CBs.

Azad et al. (2017) conducted a recent study that used a network DEA (NDEA), a three-stage DEA approach, to measure and compare the efficiency scores of IBs and CBs in the Malaysian banking sector between 2010 and 2015. They found that IBs performed better than CBs in terms of profitability and production, while the opposite was true in terms of intermediation. This study is important, as it highlights the limited application of NDEA in the examination of bank efficiency, which has been noted by Avkiran (2015) and Kao (2014). Kao (2014) has also argued that dynamic NDEA is rarely used in practice. Table 6 summarizes the studies that have used a two-stage analysis approach.

4.6 Islamic versus conventional bank technical efficiency

This paper reviews studies that examine the technical efficiency of Islamic banks (IBs) or conventional banks (CBs) or compare the technical efficiency of both types of banks. The studies analyzed in this paper are authored by Bader (2007), Kamarudin et al. (2017a, b), Le (2017), Aghimien et al. (2016), Islam et al. (2013), Hassan (2005), Brown and Skully (2005), Yudistria (2004), Nguyen et al. (2016), Yannick et al. (2016), Ozkan-Gunay et al. (2013), Assaf et al. (2013), Bos and Kool (2006), Weill (2004), Miah and Uddin (2017), Batir et al. (2017), Kamarudin et al. (2016a, b), Alrawashedh et al. (2014), Johnes et al. (2014), Abdul-Majid et al. (2008, 2010, 2011a,b), Al-Jarrah and Molyneux (2005), Hussein (2004), and Al-Shammari (2003).

The literature has utilized various financial ratios to evaluate bank performance, and research indicates that the relative performance of Islamic banks (IBs) and conventional banks (CBs) differs depending on the financial data analyzed. Popular financial ratios include debt-to-equity, return on investment (ROI), return on equity (ROE), and return on assets (ROA). Some studies, including Miah and Uddin (2017), Khediri et al. (2015), and Alrawashedh et al. (2014), support the assertion that IBs are more profitable, liquid, and less risky than CBs. However, others such as

Table 6 Survey of studies incorporating environmental variables. *Source:* Authors' own Table

Method used	Author/s	Sample
Tobit	Ariff and Can (2008)	China From 1995 to 2004
	Azad et al. (2017)	Malaysia From 2010 to 2015
	Avkiran (2009)	New Zealand and Australia From 1996 to 2003
	Batir et al. (2017)	Turkey From 2005 to 2013
	Casu and Molyneux (2003)	UK, Italy, Germany, France and Spain, From 1993 to 1997
	Chang and Chiu (2006)	Taiwan From 1996 to 2000
	Defung et al. (2016)	Indonesia From 1998 to 2008
	Drake et al. (2006)	Hong Kong From 1995 to 2001
	Fukuyama and Weber (2009)	Japan From 2002 to 2005
	Hahn (2007)	Austria From 1996 to 2002
	Hauner (2005)	Germany, Austria From 1995 to 1999
	Ismail et al. (2013)	Malaysia From 2006 to 2009
	Johnes et al. (2009)	Malaysia

Table 6 (continued)

Method used	Author/s	Sample
Ordinary least square (OLS)	Laurenceson and Qin (2008)	China <i>From 2001 to 2006</i>
	Lee and Chih (2013)	China <i>From 2004 to 2011</i>
	Pasiouras (2008)	95 countries <i>2003</i>
	Pastor (2002)	Spain, Italy, France, Germany <i>From 1988 to 1994</i>
	Saha et al. (2015)	Malaysia <i>From 2005 to 2012</i>
	Ataullah and Le (2006)	India <i>From 1992 to 1998</i>
	Chen et al. (2018)	China <i>From 2008 to 2011</i>
	Chan et al. (2015)	Malaysia, Indonesia, Singapore, the Philippines, Thailand <i>From 1998 to 2012</i>
	Fung (2006)	US <i>From 1996 to 2003</i>
	Kamarudin et al. (2016a, b)	Bahrain, Oman, Kuwait, Saudi Arabia, Qatar, UAE <i>From 2007 to 2011</i>
	Nikiel and Opiela (2002)	Poland <i>From 1997 to 2000</i>
	Rossazana and Chiang (2016)	Malaysia <i>From 2000 to 2011</i>
	Shawtari et al. (2019)	Yemen <i>From 1996 to 2011</i>

Table 6 (continued)

Method used	Author/s	Sample
Generalized method of moments (GMM)	Saeed and Izzeldin (2016)	Bahrain, Qatar, Kuwait, UAE, Saudi Arabia, Bangladesh, Pakistan, Indonesia From 2002 to 2010
	Weill (2004)	Spain, France, Switzerland, Italy and Germany, From 1992 to 1998
	Ataullah and Le (2006)	India From 1992 to 1998
	San-Jose et al. (2014)	Spain From 2000 to 2011
	Wang and Huang (2007)	Taiwan From 1982 to 2001
GLS	Aysan and Ceyhan (2008)	Turkey From 1990 to 2006
	Dogan and Fausten (2003)	Malaysia From 1989 to 1998
	Isik (2007)	Turkey From 1981 to 1990
	Isik and Hassan (2002)	Turkey 1988, 1992, 1996
	Kyj and Isik (2008)	Ukraine From 1998 to 2003
	Maudos et al. (2002)	10 EU countries From 1993 to 1996
	Molyneux et al. (2013)	Transition countries From 1994 to 2002
	Mukherjee et al. (2001)	US From 1984 to 1990

Table 6 (continued)

Method used	Author/s	Sample
Fixed effects model	Sanyal and Shankar (2011)	India <i>From 1997 to 2004</i>
	Sufian (2011a, b)	Malaysia <i>From 1993 to 2006</i>
	Tanna (2009)	75 countries <i>From 2000 to 2004</i>
	Yildirim and Philippatos (2007)	12 Central and East European countries <i>From 1993 to 2000</i>
	Aysan and Ceyhan (2008)	Turkey <i>From 1990 to 2006</i>
	Dogan and Fausten (2003)	Malaysia <i>From 1989 to 1998</i>
	Isik (2007)	Turkey <i>From 1981 to 1990</i>
	Isik and Hassan (2002)	Turkey <i>1988, 1992, 1996</i>
	Sufian (2011a, b)	Malaysia <i>From 1993 to 2006</i>
	Tanna (2009)	75 countries <i>From 2000 to 2004</i>
Bootstrap	Alam (2013)	Egypt, Indonesia, Bahrain, Kuwait, Bangladesh, Malaysia, Qatar, Pakistan, Turkey, Saudi Arabia, UAE <i>From 2006 to 2010</i>
	Brissimis et al. (2008)	10 new EU countries <i>From 1994 to 2005</i>
	Casu and Molyneux (2003)	UK, Italy, Germany, France and Spain, <i>From 1993 to 1997</i>

Table 6 (continued)

Method used	Author/s	Sample
Logit	Defung et al. (2016)	Indonesia From 1998 to 2008
	Delis and Papanikolaou (2009)	Bulgaria, Slovenia, Estonia, Romania, Check Republic, Lithuania, Poland, Hungary, Slovakia and Latvia From 1994 to 2005
	Azad et al. (2017)	Malaysia From 2009 to 2013
	Fukuyama and Matousek (2011)	Turkey From 1991 to 2007
	Hahn (2007)	Austria From 1996 to 2002
	Sufian et al. (2016)	Malaysia From 1999 to 2008
	Casu and Girardone (2002)	Italy From 1996 to 1999
	Kumar and Gulati (2008)	India From 1993 to 2006
	Pastor (2002)	Spain, Italy, France, Germany From 1988 to 1994
	Wanke et al. (2016a, b, c)	Malaysia From 2009 to 2013
TOPSIS		Taiwan From 1982 to 2001
AR, Markov and correlation	Wang and Huang (2007)	Canada 2001
Slack-based measure	Paradi et al. (2011)	18 Muslim countries From 2004 to 2009
Random effects model (REM)	Johnes et al. (2014)	

Table 6 (continued)

Method used	Author/s	Sample
SUR	Alam (2013)	Egypt, Indonesia, Bahrain, Kuwait, Bangladesh, Malaysia, Qatar, Pakistan, Turkey, Saudi Arabia, UAE From 2006 to 2010
3-stage network DEA	Azad et al. (2017)	Malaysia From 2009 to 2013
Support vector machine regression	Batir et al. (2017)	Turkey From 2005 to 2013
VAR	Miah and Uddin (2017)	Bahrain, Qatar, Kuwait, UAE, Saudi Arabia From 2005 to 2014

Milhem and Istaiteyeh (2015) demonstrate that IBs are less profitable and efficient than CBs. Sufian and Kamarudin (2016) propose that banks operating in more economically globalized nations generally have better performance metrics than their counterparts in economically protected countries.

Nienhaus (1988) discovered that Islamic banks (IBs) and conventional banks (CBs) had comparable achievements in terms of asset size, profit, and capital. Hamid (1999) proposed that IBs outperformed CBs in liquidity, profitability, productivity, and risk management. Samad and Hassan (1999) attributed this to a higher investment in government-backed securities and a higher equity-to-assets ratio. Nevertheless, the return on equity and return on assets were not significantly different for both types of banks. Iqbal (2001) compared private IBs with CBs and observed that IBs achieved greater growth in total equity, deposits, investments, total assets, and profits. However, they were less cost-efficient in terms of the total expense-to-income ratio.

In Pakistan, Moin (2008) conducted a study that found IBs and CBs had similar liquidity figures. However, the IBs in the sample were less efficient and profitable than the average for CBs, which was attributed to the IBs being younger and less experienced than CBs. Bashir (1999, 2001) corroborated these findings and identified higher costs of obtaining adequate capital ratios, loan portfolios, non-interest-earning assets, and short-term financing as crucial factors contributing to the decreasing profitability of IBs. Moreover, Hassan and Bashir (2003a, b, c) suggested that IBs' inferior asset quality compared to CBs also affects their performance.

However, Samad (2004) challenged the findings of Hassan and Bashir (2003a, b, c), stating that IBs in Bahrain are less exposed to liquidity risks due to the restrictive Shariah-compliant principles, which promote more conservative lending. Samad's study examined the performance of IBs versus CBs in Bahrain and found no significant differences in their profitability or liquidity estimates. Nevertheless, there was a significant disparity in the credit performance of both types of banks. Kader et al. (2007) observed that IBs in UAE experienced rapid growth in selected performance metrics due to the sharing of profit and loss (SPL) principle. This indicates that IBs and CBs have different characteristics in practice and should be regulated and controlled differently. The authors also suggested that IBs are generally more efficient and profitable but less liquid and less risky than CBs.

Mokhtar et al. (2006) utilized the Stochastic Frontier Analysis (SFA) approach to investigate the overall average efficiency of IBs in Malaysia, revealing that IBs were less efficient than CBs despite significant growth in asset size, deposits, and financing compared to CBs. Furthermore, the study concluded that domestic banks were less efficient than foreign banks, regardless of organizational charter. This finding was supported by Srairi (2010), who confirmed that Western banks in the Gulf Cooperation Council (GCC) countries were more cost and profit-efficient than their domestic Islamic bank counterparts.

Al-Shammari (2003) evaluated the impact of bank types and country dummy variables such as the quality of loans and capital to directly influence inefficiency. The study concluded that IBs and CBs in GCC countries were significantly less efficient than IBs. Alpay and Hassan (2007) found that, on average, IBs in Turkey were more efficient than CBs, despite having limited Shariah-compliant investment

opportunities. However, unlike CBs, the productivity and technical efficiency of IBs reduced over time. In line with Alpay and Hassan (2007), Omar et al. (2007) suggested that IBs in Indonesia operate at higher profit efficiency scores compared to Western banks in the country.

Ariff and Can (2008) found that Islamic banks (IBs) and Western banks operate at similar efficiency scores, except for the age of the bank, where older Western banks are less cost-efficient compared to their Islamic bank peers. They also found that older banks are more efficient than newer banks due to their larger asset size and more experience.

In Malaysia, Kamarudin et al. (2008) discovered that the overall cost efficiency of Islamic financial institutions is lower than that of conventional banks (CBs). However, Magrianti (2011) and Rosyadi and Fauzan (2011) both reported that, in Indonesia, IBs are more efficient than CBs when the Intermediation approach is employed.

Studies on the impact of mergers and acquisitions (M&A) on bank efficiency have yielded mixed results. While Al-Khasawneh (2013) found that bank mergers have a positive correlation with efficiency gains, Montgomery et al. (2014) disagreed. Le (2016) reported no efficiency gains from M&A for both IBs and CBs in Vietnam, and Le (2017) found that efficiency scores improved in most acquired banks but showed no clear pattern in acquiring banks.

Different studies have shown contrasting results on the efficiency of IBs compared to CBs. Abdul-Majid et al. (2008, 2010, 2011a, b), Havid and Setiawan (2015), Johannes et al. (2009, 2014), Kamarudin et al. (2016a, b), Milhem and Istaiteyeh (2015), Mokhtar et al. (2007, 2008), and Srairi (2010) suggested that IBs are less efficient than CBs. In contrast, Al-Muharrami (2008), Alrawashedh et al. (2014), Batir et al. (2017), Khediri et al. (2015), Er and Uysal (2012), and Zuhroh et al. (2015) found that IBs are more efficient/profitable than CBs.

In GCC countries, Aghimien et al. (2016), Kamarudin et al. (2016a, b), Saeed and Izzeldin (2016), and Miah and Uddin (2017) compared the efficiency scores of IBs and CBs. Aghimien et al. (2016) proposed that banks in GCC countries operated at optimal scale, indicating constant or decreasing returns to scale in large banks and constant or increasing returns to scale in smaller banks. Kamarudin et al. (2016a, b) found that IBs are less efficient than CBs, consistent with the findings of Srairi (2010). Saeed and Izzeldin (2016) discovered that CBs from GCC countries had lower efficiency scores but a decrease in default risk.

Dijkstra's (2017) dissertation examines the relationship between bank economies of scale and scope and various factors such as government intervention, corporate strategy, and market power. The empirical findings reveal a positive relationship between economies of scale and mixed relationship with economies of scope.

5 Research gaps and suggestions for future research

Based on the findings of this paper, several future research paths could be identified, and recommendations can be offered. First, IBs can increase their technical efficiency scores by using their stronger stability advantage which may require

regulatory flexibility in terms of asset requirements. Even though it can be suggested as an important topic both for IBs and CBs, studies reviewed in this paper focused mostly on efficiency measurement leaving stability and liquidity issues deeply unexplored. Our study broadens the technical efficiency research spectrum by suggesting diverse methodologies, contexts, and variables, including the less explored influence of interest rate changes and nuanced regulatory practices on Islamic Banks (IBs). While IBs do not directly interact with interest, economy-wide interest rate variations indirectly affect their efficiency by modifying the overall economic context. Importantly, we argue that the distinct business model of IBs, underpinned by principles such as risk-sharing and prohibition of interest, calls for a more considered regulatory approach. Rather than adopting a 'one-size-fits-all' strategy, regulators should account for the unique operational and risk profiles of IBs. Standard banking regulations like minimum capital requirements and capital conservation buffers, while universally applicable, could be fine-tuned to address the specific risks inherent to IBs, such as those amplified by extraordinary events like a pandemic. Thus, a regulatory framework considering aspects like capital adequacy, liquidity risk management, and customer protection should be informed by the distinct characteristics of Islamic banking.

Secondly, due to their structural differences and investment limitations by the *Shariah* principles, we recommend that IBs should be regulated and treated differently than CBs by the authorities. This is an important policy implication that needs to be addressed in future studies which attempt to evaluate and compare the performance metrics of IBs with their conventional counterparts. Thirdly, even though investment accounts of IBs are operating on PLS principles, losses in the asset side are absorbed by equity holders. To the best of our knowledge, this may create uncertainty about the level of transparency and disclosure, which has not been clearly researched in the existing literature.

Fourthly, comparative studies of the results obtained by using different variable selection approaches are scarce. The highest proportion of studies applied the Intermediation approach in defining input–output variables, whilst studies comparing efficiency scores of both IBs and CBs with different approaches is very limited. The consistency among the efficiency scores with various input–output variable combinations can be extended in future research. Fifthly, in terms of methodological applications, future research could be extended to cover more cross-country empirical investigations using both the TFA and the DFA as parametric frontier methods.

Other areas for further research could comprise, *inter alia*: (i) a comparison of the robustness of different methods used in calculating banks' efficiency scores. Evidence from existing literature shows that the three groups of methods reviewed in this paper produced diverse efficiency scores. (ii) The inclusion of non-interest expense in the choice of input variables and non-interest income in the list of output variables could have an important impact on the estimated efficiency scores, particularly for IBs. Then, the contribution of environmental factors such as *Shariah* principles, country-specific characteristics and management quality should be considered concurrently when estimating bank efficiency scores. (iii) The selection of performance metrics employed should be expanded to include both the standard efficiency scores and the Malmquist Total Factor Productivity Index (TFP). Such should help

policymakers to achieve a more accurate rating of banks in terms of their productivity and efficiency management. A summary of research gaps and recommendations for possible future research directions is presented in Table 7.

6 Conclusions

In this paper, we presented a comprehensive systematic literature review of 305 studies focusing on the 1989–2019 period. We collected the sample after a careful review of 18,461 articles from seven leading databases by following the PRISMA flowchart. Our aim was to critically evaluate the recent technical efficiency methods of Islamic banks (IBs) and conventional banks (CBs), highlight patterns and trends, identify significant factors on bank efficiency and offer a guide to researchers as a summary of existing studies by emphasizing opportunities for future research.

Our review identified several important findings with practical and theoretical implications. First, there is mixed evidence on which group of banks i.e. IBs or CBs are more efficient; whilst more recent papers on cross-country analysis found no difference between the two types of banks. Therefore, regulators and policymakers should consider the mixed findings when evaluating the performance of different types of banks, and more research is required to reach a more definitive conclusion on this issue. Second, several studies concluded that a two-stage procedure is a more appropriate method for estimating bank efficiency since it allows for the simultaneous inclusion of variables that capture the impact of bank-specific factors as well as regional and environmental conditions, which may be incorporated more in future studies. Thus, practitioners and academics should consider employing a two-stage procedure to capture a more comprehensive view of bank efficiency. Third, our review found that applications of parametric and non-parametric techniques produce different efficiency scores. But remarkably, studies comparing findings from different methods are very limited, indicating a potential area for further research, particularly incorporating consistency tests on findings. Therefore, researchers should consider comparing different methods to provide a more comprehensive analysis of bank efficiency. Fourth, our review found that many studies applied DEA as a non-parametric method and SFA as a parametric method. However, applications of other innovative methods such as TFA, DFA and FDH in the bank efficiency context are less frequent. Therefore, there is a need for new methodological applications, and researchers should explore innovative methods to capture a more comprehensive view of bank efficiency.

Fifth, there is no consensus in the literature on the procedure for selecting input and output variables. The Intermediation approach is the most widely applied method in which ‘labor’, ‘deposits’ and ‘capital’ are the most widely chosen input variables, whilst ‘loans’ and ‘other earning assets’ are the most frequently used output variables. Other approaches such as Value-Added and Production can be employed at the same time for a comparative analysis. Thus, practitioners and academics should consider multiple approaches to selecting input and output variables to provide a more comprehensive analysis of bank efficiency.

Table 7 Research gap and future research fields. *Source:* Authors' own table

Theme	Research gap	Future research
Variable selection	There is no consensus on input–output variable selection. Comparative studies using different approaches is scarce. 81% of reviewed studies applied Intermediation approach	Different variable selection approaches can be applied to the same dataset to identify the divergence among efficiency scores as future research
IBs versus CBs efficiency	There is mixed evidence in the reviewed studies from different countries on which group of banks are more efficient	Future research can investigate and identify the environmental and country specific factors on why one group of banks is more efficient than the other. Further research is needed to investigate the impact of ownership structure
Cross-country studies	There is no clear findings in cross-country studies	Future research can include regulatory factors, liquidity, solvency and financial riskiness in multi-stage analysis
Methodology	Most of the studies focused on either parametric or non-parametric analysis Literature is dominated by DEA and SFA applications	Parametric and non-parametric methods may generate different results. Therefore, application of different methods to the same dataset is suggested as future research FDH, TFA, DFA and stochastic frontier methods are suggested
Robustness	Very limited number of studies applied more than one technique to measure efficiency	Application of various techniques supported by robustness check for consistency is proposed
Regulation	IBs follow strict Shariah principals. Impact of these principals compared to regulator principals for CBs have not been identified	Future research can focus on the impact of specific regulatory differences among IBs and CBs
Efficiency versus productivity	Efficiency and productivity methods may rank banks differently. Studies mainly focus on either efficiency or productivity measurement	There is a need for further research on applying both efficiency and productivity methods such as Malmquist total Productivity Index to investigate consistency
Scale efficiency	Various groups of banks behave differently due to asset size	Scale efficiency can be an important factor to be identified in future research
Accounting/financial ratios	There is no clear evidence on which group of banks are performing better	Future research can disaggregate the accounting/financial ratios in multi-stage applications which can introduce interesting insights to bank efficiency
Two-stage analysis	Only 20% of reviewed studies applied a two (multi)-stage analysis mainly using Tobit or GLS	Bootstrap, OLS, Logit or TOPSIS can be applied in future research
Input variables	Labour, deposits, and capital are the main inputs selected	Future research can consider non-interest expense in input selection
Output variables	Loans and other earning assets are the main outputs selected	Future research can consider non-interest income in output selection

While this review contributes to the literature on bank efficiency by providing a comprehensive analysis of technical efficiency methods used in Islamic and conventional banks, there are some limitations to our study. First, the sample size may not be fully representative of all studies on technical efficiency in Islamic and conventional banks, as we focused on papers published in seven databases only. Second, our review only covers studies published between 1989 and 2019, and it is possible that there have been developments in technical efficiency methods since then, especially after COVID-19 era. It is worth noting that the COVID-19 pandemic has had a significant impact on the banking industry and may have affected the efficiency of banks in various ways. Future research in this area may investigate the effects of the pandemic on bank efficiency and performance. Third, our review focused on technical efficiency and did not consider other forms of efficiency such as scale efficiency and cost efficiency. Fourth, we did not consider the impact of external factors such as macroeconomic conditions, regulatory frameworks, and political stability on bank efficiency, which could be explored in future studies. Finally, while we identified several important research gaps and opportunities, the suggestions for future research are not exhaustive and should be considered as indicative rather than definitive.

In conclusion, this review provides a summary of the recent technical efficiency methods of IBs and CBs, highlights patterns and trends, identifies significant factors on bank efficiency and offers a guide to researchers as a summary of existing studies by emphasizing opportunities for future research. The practical and theoretical implications of this review can help practitioners, academics, and policymakers better evaluate the performance of different types of banks, and contribute to a more comprehensive understanding of bank efficiency.

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