Internet Appendix A39: Islamic Finance

A39.1 Illustrative Pitch Template Example on Islamic Banking

Pitcher's Name	Robert Faff	FoR category	Islamic Banking	**Date Completed**	18/7/15
(A) Working Title	"Capital, Charter Value, and Risk: Are Islamic and Conventional Banks Different?"				
(B) Basic Research Question	What is the impact of bank disciplinary tools (separately and interactively) on bank risk (taking) for conventional versus Islamic banks?				
(C) Key paper(s)	Abedifar, P., Molyneux, P. & Tarazi, A. 2013. Risk in Islamic banking. Review of Finance, 17(6): 2035-2096. Baele, L., Farooq, M., & Ongena, S. 2014. Of religion and redemption: Evidence from default on Islamic loans. Journal of Banking and Finance forthcoming. Beck, T., Demirgüç-Kunt, A., & Merrouche, O. 2013. Islamic vs. conventional banking: Business model, efficiency, and stability. Journal of Banking and Finance, 37(2): 433-447.				
(D) Motivation/Puzzle	The GFC was a destructive event that occurred as a result of excessive borrowing, risky investments and lack of transparency. Interestingly, Islamic banks suffered significantly less than conventional banks, as a result of their Shar'iah compliant practices that limit risk-taking. The Islamic banking industry has experienced rapid growth over the past few decades and has extended its reach into many Western countries. An examination of the different approaches to risk-taking employed by conventional and Islamic banks is timely and might shed light on how Islamic banks weathered the GFC so well.				
THREE	**Three** core aspects of any empirical research project i.e. the "**ID**io**T**s" guide				
(E) Idea?	To examine the differing characteristics between conventional and Islamic banks, a comprehensive sample of banks from around the world will be studied to identify the impact of bank capital and charter value on key alternative measures of bank risk. Examine the individual effects, as well as the conditioning effects of each mechanism on each other's impact on risk. Further, examining moderating roles of efficiency, revenue diversification and deposit insurance. Also, examine the pre-, during and post-GFC period. Charter value = NPV (future economic rents). Tension: "moral hazard" effect vs. "market rents" effect (competing incentives). **Basic hypotheses:** Bank risk deceases with higher Bank Capital (Charter Value)				
(F) Data?	Extensive sample comprising > 2,000 banks across 22 countries = > 17,000 firm-years. Period 1998 – 2011. Including 15 member countries of the Organization of Islamic Cooperation (OIC) and G7 countries. Distinguish conventional banks, Islamic banks and Islamic window banks. Three alternative risk measures: insolvency, credit and liquidity risk Charter Value (CV): normally proxied by Tobin's Q (MV/BV), here will use ratio of [Demand Deposits / Total Deposits] Data sources: Bankscope (careful to check accuracy of Islamic classifications), World Bank database (country level variables) and International Association of Deposit Insurers. No hand collecting required. Exclusions: banks with < 3 years of valid data; subsidiaries when parent data available.				
(G) Tools?	Baseline model: Risk = f (CAP, CV, EFF, Rev Diversification, Size, Concentration, GOV, GDP, Infl) Supplement with a range of interaction terms: Islamic & GFC dummies, K*CV, others. Use of Excel and STATA – standard software Recognition of panel data issues, plus challenge of endogeneity/ causality identification				

Cued Template taken from Faff, Robert W., Pitching Research (March 22, 2015). Available at SSRN: http://ssrn.com/abstract=2462059 or http://dx.doi.org/10.2139/ssrn.2462059

TWO	**Two** key questions
(H) What's New?	First study to examine the impact of bank capital and charter value on measures of bank risk for conventional vs. Islamic banks. Moreover, novelty is around examining various intermediating effects – most notably Capital vs. Charter Value. Data and Tools are standard, but strong.
(I) So What?	GFC has focused attention on instability/systemic risk linked to the role/function of the global banking system. Basel III focus on higher capital requirements, but: does it matter if Charter Value is high or low? Does it matter if it is a conventional bank or an Islamic bank? Answers will help us better understand how to strike a balance between allowing banks to make value creating decisions while keeping a close watch on risk taking.
ONE	**One** bottom line
(J) Contribution?	Add to a relatively small and immature Islamic banking literature. Strengthen bridge between research on conventional and Islamic banks. By taking a more comprehensive research design (Capital vs. CV; conventional vs. Islamic banks; non-crisi vs. GFC), pose and help resolve the question: with regard to bank disciplinary tools, does "one size does not fit all"? Findings will inform the regulatory debate eg about any need to redesign bank regulatory procedures. This then relates to the bigger question: has Basel III got it "right"? Or are adjustment warranted?
(K) Other Considerations	Is Collaboration needed/desirable? -Idea: no; -Data; no, all databases available/ legally accessible at UQ -Tools; no, have all necessary basic skills and will improve "on the job" Target journals– Journal of Banking and Finance "Risk" assessment: -"no result" risk: low. Bank risk-taking has been identified as a key contributor to the GFC and it is likely linked to bank capital and charter value. -"competitor risk" (i.e. being beaten by a competitor): moderate/high. Data are not unique and available from public sources. -"obsolescence risk": low, as crises seem a regular thing in C21 and circumstances change all the time. Scope: perhaps too many "moving parts"?

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