

Evaluation of Financial Performance of Islamic Banks in Jordan (2001-2010) “A Comparative Study”

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Abstract

The purpose of this research is to evaluate the financial performance of two of the oldest banks in Jordan, Jordan Islamic Bank and Arab Islamic International Bank. The study population consists of the Islamic banks operating in Jordan. The Islamic Bank of Jordan and the Arab Islamic Bank were selected to compare the two banks from different aspects of the study, based on the data of the two banks during the period from 2001 to 2010. This research intended to investigate the following hypotheses:

- 1) There are no statistically significant differences in the performance of the Islamic Bank of Jordan and the Arab Islamic International Bank through profit indicators.
- 2) There are no significant differences in the performance of the Islamic Bank of Jordan and the Arab Islamic International Bank through liquidity indicators.
- 3) There are no significant differences in the performance of the Islamic Bank of Jordan and the Arab Islamic International Bank through indicators of indebtedness.
- 4) There are no significant differences in the performance of the Islamic Bank of Jordan and the Arab Islamic International Bank through indicators of activity.

Both descriptive and inferential statistical analysis and results were as follows: The study found that there are no significant differences between the performance of the Arab Islamic Bank and the Jordanian Islamic Bank in the field of profitability, and no statistically significant differences in the field of liquidity, except for the percentage of total deposits / assets where the mean of this ratio to the Islamic Bank of Jordan was (87.55%) compared with Arab Islamic Bank where it was (60.78%), we conclude from that the Jordan Islamic Bank has the ability to meet short-term liabilities when due through its short-term assets more than Arab Islamic Bank. And there are statistical significance differences in the area of indebtedness.

Keywords: Islamic banks, financial performance, profit indicators, liquidity indicators, indebtedness indicators, activity indicators

1. Introduction

The banking system in Jordan consists of the Central Bank, licensed banks, agricultural lending institutions, other financial institutions and representative offices. The banks include both commercial banks and Islamic banks that have specialized in the performance of commercial transactions based on Islamic law and its rules. Islamic banks have recently developed and their ideas are derived from the Islamic Shari'a. They are based on the rejection of dealing with the interest between the Bank and its customers in the taking and giving, and this is dealt with in accordance with what Allah and the Noble Sunnah have revealed.

In order for the Bank to be Islamic, the services, operations and areas in which the Bank deals or finances must be entered into by the Halal Department, in accordance with Islamic law. Thus, Islamic property depends on the source of power in any bank and not in the board of directors or the total shareholders, but in the owner of everything is the source of power and the law, God Almighty.

Economic changes in Islamic countries have led to increased reliance on market mechanism, privatization, liberalization and fiscal restraint. This was accompanied by an Islamic revival that strongly pushed for the

development of Islamic financial systems. The work continues today to develop Islamic financial instruments that are compatible with Islamic assets. In order to create the required infrastructure for the movement of financial markets, and as a result of the large growth in deposits, financial institutions are seriously looking for investment opportunities. In contrast, banks and non-banking financial institutions in Western countries have responded to this request and contribute to it.

Financial analysis is one of the means used by economic enterprises to measure their ability to sustain economic life and to expand their activity by creating consistency and interaction between the material possibilities of the project and its optimal use, in order to achieve the highest quality of production with minimal effort and benefit from all sources that provide the project with a financial flow covers the shortage of funds and the return on them with an economic return that exceeds the cost of investment.

Financial analysis by ratios is an important and fundamental means of studying the financial position of the project in the light of the figures and data in its financial statements. The financial ratios are divided into a number of groups, each of which reflects a specific aspect of the project. And the other reflects the efficiency of the management of current and fixed assets, which measures the degree of indebtedness of the project and the possibility of borrowing. This study was conducted to evaluate the financial performance of Islamic banks in Jordan.

1.1 Research Problem

The opening of the Jordanian banking market to foreign banks has contributed to the intensification of competition between banks in providing the best banking services. Banks in Jordan are divided into commercial and investment banks on the one hand and Islamic banks on the other. These two types compete in attracting customers to deal with them. Banks are confused about access to a variety of banking services. This has necessitated evaluating the financial performance of Islamic banks in Jordan by comparing the financial performance of the Islamic banks in Jordan, including the Islamic Bank of Jordan and the Arab Islamic Bank by analyzing profitability, investment, liquidity and debt ratios from 2001-2010.

1.2 Research Importance

The banking sector is one of the most important economic sectors in Jordan. The banking sector in any country is a positive reflection on the development of this country and the prosperity of its economy. Islamic banks are one of the most important pillars of the banking economy in Islamic countries in general and in Jordan in particular. The importance of the study is as follows:

- 1) The Islamic banking sector in Jordan is generally focused on the use of certain financial ratios used to assess its performance in Jordan. The assets of Islamic banks have made considerable weight in the volume of assets of Jordanian banks.
- 2) The performance of banks affects a wide range of interested parties whether they are inside or outside the bank; they are dealing in the financial market or have the intention to deal in the future. The current and prospective investors benefit from the performance of the banks, focusing on the success of their investments and increasing profits. Banking departments also benefits from the evaluation, which seek to make their institutions, depositors and lenders successful, as they always want to make sure their money is in a safe place.
- 3) This research focuses on two of the oldest Islamic banks in Jordan, Jordan Islamic Bank and Arab Islamic International Bank. The Islamic Bank of Jordan was established in 1978 and the Arab Islamic International Bank was established in 1997.

1.3 Research Hypotheses

This research is based on the following hypotheses:

The first hypothesis: There are no statistically significant differences in the performance of the Islamic Bank of Jordan and the Arab Islamic International Bank through profit indicators.

The second hypothesis: There are no significant differences in the performance of the Islamic Bank of Jordan and the Arab Islamic International Bank through liquidity indicators.

The third hypothesis: There are no significant differences in the performance of the Islamic Bank of Jordan and the Arab Islamic International Bank through indicators of indebtedness.

The fourth hypothesis: There are no significant differences in the performance of the Islamic Bank of Jordan and the Arab Islamic International Bank through indicators of activity.

2. Theoretical Frame Work and Previous Studies

2.1 The Theoretical Framework of the Study

2.1.1 The First Topic: Islamic Banks

The distinctive features of Islamic banks

Islamic banks became a tangible reality that exceeded the framework of presence during the last quarter of the twentieth century, and moved towards the prospects of interaction and positive dealing with the problems of the age facing the world during the third millennium (Hamoud & Hassan, 1991).

The question now arises: What are the characteristics of Islamic banks and the distinctive features of their business? To answer this question, we need to introduce a definition of Islamic Bank, and then answer the question.

Islamic Bank is an investment financial institution with a developmental, humanitarian and social message. It aims at pooling funds and optimizing the use of its resources under Islamic Shari'a rules to build the Islamic Takaful community.

Islamic banks have certain characteristics and operate their banking business in a different manner from that of conventional commercial banks. Commercial banks are financial institutions that deal with debt or credit. The commercial bank's function is to borrow from depositors (lending money to its depositors), lend it to investors who need to finance their projects, and since borrowing is a debt obligation, lending is debt owed on the other hand, So the main function of the Commercial Bank is based on borrowing and lending, and the interest or usury by taking and giving. In other words, commercial banks trade and deal with debt.

As for Islamic banks, they do not trade in debt and do not deal with riba regardless of its forms and forms of deposit or lending, acceptance or deduction, taking or giving, either directly or indirectly. The non-trading of debt refers to the special relationship between the Islamic bank and its depositors, because it is not a relationship based on credit and debt. It is a partnership and trading, which takes the form of speculation, participation, trading or Murabaha in the buying and selling operations.

And "riba debt" is any financial increase in the origin of the loan that was concluded, each loan is a benefit is "riba". In other words, the riba of debt includes the receipt or payment of interest in various lending or borrowing situations and introduces any conditional increase in the money recovered instead of the money owed.

Therefore, Islamic banks are committed to several basic rules, the most important of which are the following:

First: Compliance with the provisions of Islamic Sharia in all its banking operations

It is committed to financing activities within the Halal circle and to avoid other activities in the circle of prohibition for serious harm to the community, such as: the activities of the alcohol industry, and the industries based on raising and slaughtering pork, dead or blood, drugs and gambling. It also avoids dealing with any activity involving riba, fraud, monopolization or exploitation of people's needs.

2.1.2 Second: Islamic Banks Derive Their Economic Intellectual Framework from the "Theory of Fragmentation"

This theory is based on the fact that God is the creator of this universe, and that the property in this universe is God alone, He is the king's owner. As for man, he is a mukhtar from God in this land, and it is not the ownership of money that is the property of people, but it is acquired by the difference, and possession of it depends on the terms of this differentiation identified by God in the Koran (Al-Ashqar, 1995).

2.1.3 Third: Working on the Development of the Money and Not to Seize It and Keep It from Trading

Islamic banks are also committed to developing the funds they own, whether they are shareholders or depositors, as they are acting on behalf of their owners. And choose the best way to manage legitimate rational management away from excessive or scaling so that invest funds in projects and activities of feasibility, and in a manner that maximizes productivity, and thus increases the welfare of citizens.

It should be noted that the imprisonment of money from trading and treasure, that is, the disruption of the performance of social function, is considered an economic crime in Islamic economic thought, because it leads to freezing and disrupt the wheel of economic growth in the state. Those who stockpile funds lock the benefit away from people do not share benefits and harm productive and consumer forces in society.

Fourth: Commitment to the pursuit of the elements of social solidarity among the members of society

The provision of social services aimed at reviving the images of organized social solidarity is one of the

distinctive features of Islamic banks. These dances include the financing of social activities aimed at deepening the meaning and content of positive cooperation and active participation among citizens.

2.2 Previous Studies

The researchers reviewed some previous studies as follows:

Al-Ghusain and Nashwati study (2014) entitled: Evaluating the financial performance of Islamic and traditional Jordanian banks using CAMEL model indicators. The study aimed at evaluating the performance of Islamic and traditional Jordanian banks in terms of Capital Adequacy Index, Asset Quality Index, Performance Quality Index, Profitability and Liquidity Index and comparing these ratios between the traditional and Islamic Jordanian banks from 2006-2012 and using the average ratios and linear regression analysis. The study found that the performance of conventional banks is better than the performance of Islamic banks. As for public confidence, Islamic banks came better than conventional banks.

Masoudi Study (2015) entitled: Assessing the financial performance of the commercial banks. This study aimed at how the financial performance of commercial banks evaluated in terms of return and risk, where the theoretical framework of this study included both general concepts about the commercial banks of the origins and definitions of types and objectives of this process, errors and properties, as well as the generalities about the financial performance evaluation of the long stages that are possible occurring during the evaluation process, the practical part of this study was a field study of the National Bank of Algeria's popular Algerian loan was given the emergence and definition of both banks and the organizational structure of the two, then the sample application return on equity for both banks during the period of Extended from 2009 to 2012 by calculating the yield indicators and indicators of risk for both banks and extract the results and comment and comparison between them.

Matar (2017) conducted a study entitled: Evaluating the Performance of Islamic and Commercial Banks in Jordan: A Comparative Study. The study assesses the performance of commercial banks compared to Jordanian Islamic banks during the period 2000-2013 through the adoption of a performance analysis methodology using financial ratios analysis and data analysis between the Islamic and Jordanian commercial banks, which were hired to perform the evaluation process. The analysis included the recruitment of liquidity, profitability, risk ratios and financial reliability. The results showed a slight difference between the profitability of Islamic and commercial banks in Jordan, and the performance of commercial banks was better than Islamic banks. On the other hand, the results showed that Islamic banks are less risky than commercial banks, suggesting that Islamic banks are less vulnerable to financial crises and volatility.

Adam (2014) conducted a study entitled "Evaluating the Financial Performance of Banks Using Financial Ratios-A Case Study of Erbil Bank for Investment and Finance". This study examines the financial performance of Erbil Bank for Investment and Finance in the Kurdistan Region of Iraq during the period 2009-2013. Many financial performance measures are used, such as financial ratios analysis, which is used to measure the financial position of the Bank and to wider statistical tools. It has also been used for the analysis of several variables that would affect the banking system in general. The results of the study showed the positive behavior of Erbil Bank's financial position and some of the financial factors affecting the Bank's financial performance. Subsequently, the overall financial performance of Erbil Bank is improving in terms of liquidity ratios, asset quality ratios or credit performance, profitability ratios (NPM, return on assets and return on investment), suggesting a set of recommendations for the development and consolidation of some which will enhance the Bank's profitability and improve the Bank's financial performance.

3. Methodology of Study

The study was based on the analytical descriptive approach to arrive at accurate and detailed knowledge about the problem of research and to achieve a better and accurate understanding of the phenomena related to it, in addition to providing the data and facts about the problem that is the subject of the research to interpret it and identify its implications.

The descriptive approach was used to present the theoretical side of the research phenomenon and then to use the analytic method in the practical aspect by analyzing the financial data extracted from the financial statements. Hence, the semantics and relationships between the items of the financial statements are analyzed through quantitative analysis of the financial ratios.

3.1 The Population of the Study and Its Sample

The study population consists of the Islamic banks operating in Jordan. The Islamic Bank of Jordan and the Arab Islamic Bank were selected to compare the two banks from different aspects of the study, based on the data of the

two banks during the period from 2001 to 2010.

3.2 Hypotheses Test

In this aspect, the hypotheses of the study were tested. Significant differences were observed between the two banks, using the oneway ANOVA test to compare the differences between the individual financial ratios.

3.2.1 The First Null Hypothesis

H01: There are no significant differences between the Islamic Bank of Jordan and the Arab Islamic Bank in the field of profitability ratios.

The researcher used this hypothesis to test the OnewayANOVA at the significance level ($\alpha = 0.05$), which tests significant differences between the averages of the financial ratios that fall under the profitability ratios. The results are shown in the following table according to the decision rule that governs this decision: Reject the null hypothesis (Ho) and accept the alternative hypothesis (Ha) if Sig is $\leq (0.05)$ and vice versa.

Table 1. Results of one-way analysis of variance (ANOVA) between the average profitability ratios between Jordan Islamic Bank and Arab Islamic Bank

Ratio		Sum of Squares	df	Mean Square	F	Sig.
Return to total assets	Between Groups	.004	1	.004	.012	.913
	Within Groups	5.255	18	.292		
	Total	5.259	19			
Return to shareholders' equity	Between Groups	103.481	1	103.481	2.942	.103
	Within Groups	633.112	18	35.173		
	Total	736.593	19			
Net profit and commission / net operating income	Between Groups	456.672	1	456.672	.723	.406
	Within Groups	11373.162	18	631.842		
	Total	11829.834	19			
Profit / Net Facilities	Between Groups	36796.799	1	36796.799	3.384	.082
	Within Groups	195718.602	18	10873.256		
	Total	232515.401	19			
Net profit / total revenue	Between Groups	17.731	1	17.731	.104	.751
	Within Groups	3077.552	18	170.975		
	Total	3095.283	19			

The table above shows that there are no statistically significant differences between the profitability ratios mentioned in the table because the level of significance of all the differences (Sig) was greater than 0.05. Therefore, we reject the null hypothesis and accept the alternative which states:

There are significant differences between the Islamic Bank of Jordan and the Arab Islamic Bank in the field of profitability ratios.

3.2.2 The Second Null Hypothesis

H02: There are no statistically significant differences between the Islamic Bank of Jordan and the Arab Islamic Bank in the area of debt ratios.

To test this hypothesis, the researcher used OnewayANOVA and at a significance level ($\alpha = 0.05$), which tests significant differences between the average of the financial ratios that fall under the debt ratios. The results are shown in the following table according to the decision rule that governs this decision which is: Reject the null hypothesis (Ho) and accept the alternative hypothesis (HA) if Sig is $\leq (0.05)$ and vice versa.

Table 2. Results of one-way analysis of variance (ANOVA) between average debt ratios between Jordan Islamic Bank and Arab Islamic Bank

Ratio		Sum of Squares	df	Mean Square	F	Sig.
Debt ratio	Between Groups	150.700	1	150.700	38.633	.000
	Within Groups	70.214	18	3.901		
	Total	220.915	19			

Debt to Equity ratio	Between Groups	185.745	1	185.745	29.604	.000
	Within Groups	112.937	18	6.274		
	Total	298.682	19			
Provision for credit facilities / net facilities	Between Groups	4257.654	1	4257.654	4.443	.049
	Within Groups	17247.996	18	958.222		
	Total	21505.649	19			

The table above shows significant differences in the ratios between the Islamic Bank of Jordan and the Arab Islamic Bank (sig = 0.000) for the debt ratio, the debt to equity ratio (sig = 0.000) and the credit facility / net facility ratio (sig = 0.049)) Are all less than 0.05, so we reject the nihilistic hypothesis and accept the alternative which states:

There are significant differences between the Islamic Bank of Jordan and the Arab Islamic Bank in the area of debt ratios.

3.2.3 The Third Null Hypothesis

H03: There are no statistically significant differences between the Islamic Bank of Jordan and the Arab Islamic Bank in the area of liquidity ratios.

The researcher used this test to test the OnewayANOVA variance analysis at a level of significance ($\alpha = 0.05$), which tests significant differences between the average ratios of the financial ratios that fall under the liquidity ratios. The results are shown in the following table according to the decision rule that governs this decision which is: Reject the null hypothesis (Ho) and accept the alternative hypothesis (Ha) if Sig is $\leq (0.05)$ and vice versa.

Table 3. The results of one-way analysis of variance (ANOVA) between average liquidity ratios between Jordan Islamic Bank and Arab Islamic Bank

Ratio		Sum of Squares	df	Mean Square	F	Sig.
Total deposits / total assets	Between Groups	3583.165	1	3583.165	16.602	.001
	Within Groups	3884.889	18	215.827		
	Total	7468.053	19			
Liquidity Ratio	Between Groups	.003	1	.003	.018	.895
	Within Groups	2.653	18	.147		
	Total	2.656	19			
Cash + Investments / Total Deposits	Between Groups	353.809	1	353.809	.198	.662
	Within Groups	32174.857	18	1787.492		
	Total	32528.665	19			
Cash + Financial assets held for trading / Total deposits	Between Groups	.003	1	.003	.020	.890
	Within Groups	2.648	18	.147		
	Total	2.651	19			

The table above shows significant differences in the ratio of total deposits / total assets (sig = 0.01), which is less than 0.05, while the other ratios did not reveal any differences between the two banks, where the sig of other ratios was greater than 0.05, So we accept the null hypothesis regarding these percentages and reject the alternative that states:

There are significant differences between the Islamic Bank of Jordan and the Arab Islamic Bank in the area of liquidity ratios.

3.2.4 The Fourth Null Hypothesis

H04: There are no statistically significant differences between the Islamic Bank of Jordan and the Arab Islamic Bank in the field of activity ratios (total revenues / assets).

The researcher used One-way analysis of variance (ANOVA) to test this hypothesis at a level of significance ($\alpha = 0.05$), which tests the existence of significant differences between the averages of the financial ratios that fall under the activity ratios. The results are shown in the following table, according to the decision rule that governs this decision: Reject the null hypothesis (Ho) and accept the alternative hypothesis (Ha) if Sig is $\leq (0.05)$ and vice versa.

Table 4. Results of one-way analysis of variance (ANOVA) between the averages of activity ratios between the Islamic Bank of Jordan and Arab Islamic Bank

Total revenue/ assets	Sum of Squares	df	Mean Square	F	Sig.
Between Groups	5.821	1	5.821	11.851	.003
Within Groups	8.841	18	.491		
Total	14.662	19			

The table above shows that there are significant differences in the ratio of total revenues / assets, where (sig = 0.003) which is less than (0.05), so we reject the null hypothesis and accept the alternative that states: There are significant differences between the Islamic Bank of Jordan and the Arab Islamic Bank in the field of activity ratios (total revenues / assets).

3.3 Results of Statistical Analysis

Through the statistical analysis of the financial ratios of the Islamic Bank of Jordan and Arab Islamic Bank, and depending on the output of SPSS software, the following results were obtained:

- 1) There are no significant differences between the Islamic Bank of Jordan and the Arab Islamic Bank in terms of profitability and the following ratios: Return to Total Assets, Return on Equity, Net Profit and Commissions / Net Operating Income, Net Profit / Net Facilities and Net Profit / Total Revenues.
- 2) There were significant differences between the Islamic Bank of Jordan and the Arab Islamic Bank in the area of indebtedness and the following ratios: debt ratio, debt-to-equity ratio and credit facility allocation / net facilities.
- 3) There are no statistically significant differences between the Islamic Bank of Jordan and the Arab Islamic Bank in the area of liquidity and the following ratios: Liquidity ratio, cash / investments / total deposits, cash + financial assets for trading / total deposits.
- 4) There were statistically significant differences between the Islamic Bank of Jordan and the Arab Islamic Bank in the field of liquidity in relation to the ratio of total deposits / total assets.
- 5) There were statistically significant differences between the Islamic Bank of Jordan and the Arab Islamic Bank in the field of activity in relation to the ratio of total revenues / total assets.

4. Results of the Study

- 1) The study found that there are no significant differences between the performance of the Arab Islamic Bank and the Jordanian Islamic Bank in the field of profitability.
- 2) The study found that there are no statistically significant differences between the performance of the Arab Islamic Bank and the Jordanian Islamic Bank in the field of liquidity, except for the percentage of total deposits / assets where the mean of this ratio to the Islamic Bank of Jordan was (87.55%) compared with Arab Islamic Bank where it was (60.78%), we conclude from that the Jordan Islamic Bank has the ability to meet short-term liabilities when due through its short-term assets more than Arab Islamic Bank.
- 3) The study found that there are statistical significance differences between the performance of the Arab Islamic Bank and the Jordanian Islamic Bank in the area of indebtedness and details as follows:
 - Jordan's Islamic Bank's average debt ratio reached (92.79%), while Arab Islamic Bank reached (87.30%). This increase reflects the Bank's inability to service its debt, increase the risks of its lenders and increase investors' risk.
 - The ratio of the debt to equity ratio of Jordan Islamic Bank reached (7.39%), while Arab Islamic Bank reached (12.75%). This increase reflects the bank's use of short-term borrowings rather than long-term sources to finance its long-term operations because Arab Islamic Bank is new in this field.
 - The accounting average for the credit facility/facility holders for Jordan Islamic Bank reached (5.79%), while the Arab Islamic Bank reached (34.97%). This indicates that Arab Islamic Bank is working to provide higher credit facilities. This indicates the customers' interest in the bank due to the diversified banking services provided by the Islamic Bank, but increasing these credit facilities at the same time means an increase in the risks borne by Arab Islamic Bank.
- 4) The study found that there are statistical significant differences between the performance of the Arab Islamic Bank and the Jordanian Islamic Bank in the field of activity in relation to the ratio of total revenues

/ total assets known as the turnover rate of total assets. The mean of this ratio to the Islamic Bank of Jordan reached (4.35%) while for the Arab Islamic Bank it reached (3.27%). This is the most comprehensive measure of activity; the high percentage indicates the efficiency of the management in using its assets to achieve its goal in revenues and the extent to which it is also efficient in exploiting the assets.

5. Recommendations

The researchers suggested the following recommendations

- 1) The Islamic banks must maintain their investment in their deposits in a suitable manner, in addition to increasing their ability to operate their resources in general, taking into account their ability to meet their short-term obligations without having to break their deposits with other banks when investing money.
- 2) The need for Islamic banks to balance liquidity and profitability so that profits can be maximized at the lowest possible cost.
- 3) Islamic banks should seriously consider increasing the number of branches to meet the growing demand for Islamic banking services and work to improve the quality of banking services offered in the face of strong competition with traditional banks.
- 4) Islamic banks should aim to finance their long-term investments with long-term financing sources to reduce the risk of indebtedness.
- 5) The importance of Islamic banks to employ competent and qualified human resources capable of managing the Bank's resources well.

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