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A SYSTEMATIC LITERATURE REVIEW ON THE CAPITAL STRUCTURE OF ISLAMIC BANKS USING THE PRISMA

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Abstract:

The purpose of this study is to critically evaluate theoretical and empirical research into capital structure practices in Islamic Banks (IBs) from four perspectives, namely the theoretical aspect and its nature, the determinants of capital structure in IBs, the links between capital structure and risk management and the nexus between capital structure and the performance of IBs. The authors reviewed and examined past studies on IBs' capital structure from both theoretical and empirical research using the PRISMA approach. It was discovered that most of the literature on the IB capital structure is largely theoretical than empirical. Existing studies have various limitations, which suggest a need for detailed empirical work. Detailed empirical research in the field of capital structure will support bank managers and policymakers in making decisions about improving capital structure. This study will contribute to addressing literature gaps on the IB capital structure. Furthermore, the study identified areas for future research into capital structure practices and IB financing decisions. Lastly, the study will equip regulators with guidelines to establish sound capital requirements for IB.

Keywords: Capital structure, Islamic Banks, PRISMA approach

1. Introduction:

In recent decades, interest in Islamic banking and finance has increased as the number of full-fledged Islamic banks (henceforth, IB) and IBs windows have risen both in Muslim and non-Muslim nations (Sakti et al. 2017). The Islamic banking global capital market was estimated at US dollars 1.992 trillion in 2019, indicating a growth rate of 10.07 percent annually. The report also predicted that Islamic banking assets could reach US dollars 5.44 trillion at the end of 2030 (Ismail, 2022).

Islamic Banks operate under Sharia principles and are prohibited from engaging in any transaction that will lead to usury (riba), gambling (maysir), and excessive uncertainty (gharar) (Ebrahim and Safadi, 1995). The banks connect lenders (investors), borrowers, and other clients. However, Islamic finance's theoretical aspect offers three finance models for Islamic banks: equity-based, debt-based, and service-based (Ismail, 2010). The finance principles used in Islamic Banks often include profit and loss sharing (mudaraba and musharak) and non-profit and loss sharing, also known as debt based (Murabaha, salam, Istitsna, Ijarah, etc.). According to Chong & Liu (2009), equity-based finance dominates another finance method in Islamic banking operations.

Unlike Conventional Banks (CB), Islamic Banks are prohibited from interest-based transactions. They are motivated under Sharia Law to finance their activities with profit-loss sharing contracts, which will require banks to share their profit and loss with investors. A profit-loss sharing contract is a finance option that enables Islamic banks and their customers to pool found

together and invest without involving interest (Danlami et al., 2020). The contract does not promise a predetermined profit to investors, but they are eligible for a portion of the profit. Islamic Banks are expected to establish profit-sharing investment accounts (henceforth PSIAs) as part of bank equity. The capital structure in Islamic Banks is influenced by the inclusion of the PSIA as the class of equity with no governance right ((Archer et al., 2010; Archer & Karim, 2006) and led to the variation between the features of the Islamic banks' capital structure and that of conventional banks, which imposed constraints on the possibility of the Islamic Banks raising finance through the capital market.

Existing studies regard the Modigliani and Miller (M&M) theorem as a foundational theory for capital structure, explaining that a firm's market value is entirely independent of its capital structure (Hoque et al., 2022; Smaoui et al., 2020). The independence is due to perfect capital markets and the absence of corporate income tax. Hence, all capital structures remain fixed, as the cost of capital in their model remains unchanged independent of the capital structure. The market value maximization criterion serves as the foundation for these assumptions. IBs' financial decisions, in contrast to CBs, are heavily influenced by the moral standards of Shariah (Ayedh & Echchabi, 2015). Notably, these principles will prevent the projected utility from being maximized (Toumi et al., 2015). Notably, Al-Deehani et al. (1999) contended that because of contractual obligations' fundamental nature and the profit-sharing arrangement between banks and the holders of investment accounts, modern capital structure theories do not apply to IB.

Since the 1980s, capital structure literature has become popular among academics' professionals and policymakers. However, the study volume has significantly expanded through journal articles, book reviews, conference papers, and other resources. Nonetheless, the majority of this flood of capital structure literature has focused on non-financial enterprises and CB (Allen, 2013; Caglayan & Sak, 2010; DeAngelo & Stulz, 2015; Haron, 2014; Rajan & Zingales, 1995; Titman & Wessels, 1988). To the authors' best knowledge, not much study has been done on the capital structure and financing decision of IB As a result, this study aimed at breaching the gaps in the previous research on IB capital structure practices and their financing strategies by systematically reviewing the extant studies using Preferred Reporting Items for the Systematic Reviews and Meta-Analyses (henceforth PRISMA) approach.

2. Literature Review

2.1 Conceptual Issues

Concept of Capital Structure

The primary function of financial management and the core element of an organization's financial strategy involve deciding between debt and equity financing and determining whether to retain earnings or distribute dividends in the form of cash, stocks, or a combination of both. These decisions, referred to as capital structure decisions, have been the subject of extensive theoretical and empirical research to gain a comprehensive understanding. According to Al-Hunnayan (2020), capital structure choice becomes irrelevant for the firm in a frictionless market devoid of impurities like taxes, commissions, fees, information asymmetry, financial regulations, and factors that reduce market efficiency. Thus, regardless of the firm's level of leverage, investors seeking leverage and riskier opportunities can create their optimal capital structure at the portfolio level by using debt instruments, provided they have the same access to debt as the firm, with no difference in cost or privileges. Belkhir et al. (2016) suggest that the cost of equity is a linear function of the leverage ratio. As more debt is added and considering that creditors have a superior claim on assets compared to shareholders, the cost of equity increases, causing the stock price to decrease by a proportional amount. Consequently, as the capital structure changes, the weighted average cost of capital remains constant.

Islamic banks' capital structure includes shareholders' equity and debt, with investment accounts and current accounts being the primary sources of debt (Siddik et al., 2017). The most significant component affecting the capital structure is debt, which forms the largest portion of the capital. Islamic banks raise funds from depositors to invest professionally, aiming for reasonable profits while managing risks. Capital structure is a critical factor that imposes important limitations on Islamic banks, and

they typically maintain capital levels above the required minimum to withstand potential shocks (Zeitun, 2012).

The literature on factors influencing capital structure has shown a strong correlation between a company's leverage level and the quality of its business, especially in the banking industry (Guizani, 2020; Khokher & Alhabshi, 2019). However, empirical findings regarding the determinants exhibit conflicts due to institutional differences that can impact the cross-sectional relationship between determinants and the leverage ratio. Amidu (2007) discovered that profitability, asset structure, risk, growth, size, and tax affect Ghanaian banks' capital structure, with insights drawn from both the trade-off and pecking order theories.

Similarly, Ahmed et al. (2010) demonstrated that profitability, liquidity, risk, and corporate age influence insurance companies' capital structure (leverage ratio), suggesting the relevance of pecking order and trade-off theories in the Pakistani context. Najjar and Petrov (2011) documented that tangibility, size, and liquidity significantly affect Bahraini insurance companies' capital structure (debt ratio), providing support for trade-off and pecking order perspectives. Meanwhile, Juca et al. (2012) found that leverage has an inverse association with size, profitability, growth, tangibility, risk, and executive managers' compensation programs, while it is positively related to deposits' market value in North American banks (Zeitun, 2012).

2.2 Theoretical Framework

The principles of Shariah governed all aspects of Islamic banks' operations. Based on principles, IBs must conduct distinct transactions, hold unique assets, establish a specific governance system, employ specific risk management approaches, and use different sources of funds compared to CBs (Zare et al., 2013). All these distinctive features of IBs have a significant impact on the capital structure. In conventional financial theories, capital structure decisions are driven by the concept of individual wealth maximization based on utility objectives, ultimately aimed at justifying the choice between equity and debt. However, in the case of IBs, capital structure decisions are primarily guided by Shariah principles, which prohibit issuing interest-bearing loans or accepting interest-based deposits (Zeitun, 2012).

In contrast to CBs, IBs employ distinct financing instruments to raise funds, such as shareholders' equity, investment accounts, and current accounts. Shareholders' equity serves as the primary source for increasing bank funding through the sale of common shares to the public, including any accumulated reserves from previous years. It's worth noting that IBs are not allowed to issue preference shares as Shariah prohibits them. Investment accounts are considered a form of equity financing rather than a liability. This unique and innovative funding mechanism sets IBs apart from their conventional counterparts, enabling them to invest funds on a profit-sharing basis. Current accounts also contribute to bank funding since customers have the right to withdraw their funds on-demand without receiving returns on their deposits.

Several researchers have explored capital structure in the context of Islamic banking. Kusasi (2013) examined profit-sharing contracts and found that increased funding through investment accounts enhanced market value and shareholder returns without increasing financial risk. More recently, Toumi et al. (2012) revisited theories like trade-off theory, agency theory, and pecking order theory from an Islamic perspective and concluded that the trade-off theory is more suitable for explaining Islamic banks' capital structure, particularly when measured by the equity ratio.

In addition, Kumar et al. (2017) investigated capital structure theory from an Islamic standpoint, focusing on the impact of Islamic debt (sukuk) based on trade-off, agency, and pecking order theories. They found that cost is a key determinant of Islamic banks' capital structure and is not influenced by trade. From an Islamic perspective, the optimal capital structure is linked to tangible asset value, excluding transaction costs. Therefore, this study adopts the trade-off theory within an Islamic framework to guide capital structure decisions, focusing on the leverage ratio.

2.3 Empirical Review

Past studies have predominantly emphasized empirical investigation of capital structure rather than theoretical

aspects (Guizani, 2020; Khokher & Alhabshi, 2019; Qayyum and Noreen, 2019). Consequently, many empirical studies have indicated that IBs tend to have a larger proportion of equity in their balance sheets when compared to Conventional Banks (CBs). For instance, Zoubi and Olson (2008) compared 28 CBs and 16 IBs operating in the Gulf region from 2000 to 2005. Their study revealed a significantly lower "non-equity/equity" ratio in IBs. Similarly, Asarpota and Kader (2007) compared eight conventional and Islamic banks in the UAE from 2000 to 2004. Their research affirmed that, on average, the "non-equity/equity" ratio is lower for IBs. Furthermore, Metwally (1997) examined a sample of 30 banks, including 15 Islamic ones, during the period from 1992 to 1994. The study suggested that a higher "deposits/assets" ratio is associated with a lower that the bank is Islamic. Conversely, it also indicated that a higher "capital/asset" ratio is linked to a greater probability that the bank is Islamic.

Caglayan and Sak (2010) analyzed capital structure decisions in the Turkish banking sector using a panel data analysis method. The results indicate that size and market-to-book ratio positively influence book leverage, while tangibility and profitability have a negative impact, aligning with the expectations of the pecking order theory. Kamran et al. (2014) examined capital structure decisions among banks in Pakistan through panel data analysis. The findings reveal that the determinants of capital structure include size, profitability (ROA and ROE after taxes), and gross domestic product (GDP) over a period of time. These findings are consistent with the predictions of the pecking order hypothesis.

Al-Qudah (2014) conducted a study on the determinants of the capital structure of banks in Jordan using panel data analysis. The results reveal a significant and positive relationship between size and the total liabilities to equity, book leverage, and market leverage ratios. Additionally, the research indicates that the market-to-book ratio has a significant and positive relationship with leverage measures, except for non-deposit leverage. Basnet (2015) examined the capital structure of Nepalese commercial banks. They explored the impact of determinants such as profitability, asset tangibility, size, collateral, business risk, dividends, GDP growth, and inflation on capital structure. The results demonstrate that these standard determinants affect the market leverage of the banks, and this relationship is explained by the trade-off and pecking order theories. In the GCC, Al-Mutairi and Naser (2015) attempted to identify the determinants of commercial banks' capital structure in the GCC listed on stock exchanges. The study used data from 47 banks for the period between 2001 and 2010. The findings revealed a negative relationship between leverage, profitability, tangibility, and size and a positive relationship between growth and age.

3. Methodology

The study reviewed the literature on the capital structure of Islamic Banks using the PRISMA approach; articles/ journals were extracted from the Scopus database. The PRISMA process is a rigorous review that provides evidence for a literature review in any discipline. It also helps comprehend and relate text and content associated with a particular problem in previous studies in a specific field. Zuhroh (2022) mentioned that one of the advantages of the research methodology to content analysis is the flexibility to interpret the text, which is subdivided into concepts, themes, and subjects to help arrange the distribution of structured and unstructured texts and provide an adequate framework for answering research questions. Therefore, all the papers reviewed in this study were analyzed, classified, and categorized to highlight themes and topics that have received attention from the previous literature to achieve the principal aim of the study and point out areas and opportunities for future research.

Becheikh et al. (2006) asserted that the systematic literature review method has been employed and advocated in recent years in limiting bias and impacts through systematic reviews to improve the results' validity, authority, and dependability. In management research, the traditional narrative reviews have been widely criticized for the lack of relevance and due to subjective and biased methodology by authors (Becheikh et al., 2006; Fink, 1998). Tanfield et al. (2003) described specific principles for using systematic reviews in management research and argued that systematic reviews improve the quality of the review process by establishing a systematic, transparent, and reproducible literature review. Although there is adequate literature on capital

structure in Islamic Banks, we could not locate any systematic reviews related to the topic.

The Scopus database was used to search for the available literature on capital structure in Islamic banks. The keywords used were "capital structure" and "Islamic banks". The total number of articles/journals displayed at first was thirty-six. The process required a filter to gate match and qualitative literature for the study. Therefore, the topic was limited to the subjects of Management and Accounting, Economics, Econometrics, Finance, and Social Sciences. The language chosen was English. Another option was the source of the papers; only journals and conferences were selected for the study's reliability and quality, and the database automatically had thirty-four articles. We adapted the basic guidelines proposed by Janjua et al. (2021) for conducting a systematic management review. As shown in Figure One, we customized the steps as per our study requirement into a five-step process.

We generated an Excel sheet for further screening, and all documents that met the prescribed criteria were included in the study. Criteria for the inclusion and exclusion of the quality assessment of the papers are as follows.

3.1 Inclusion criteria

i. Studies that explicitly deal with capital structure in Islamic Banks.
ii. Studies that explore Capital structure decisions and underlying theories or philosophical aspects of Islamic Banks.
iii. Studies that present a comparison of the capital structure of Islamic Banks (IB) and Conventional Banks (CB.)
iv. Studies that propose solutions to the identified inherited Capital Structure of IB flaws and present new theories or suggestions for improvement.

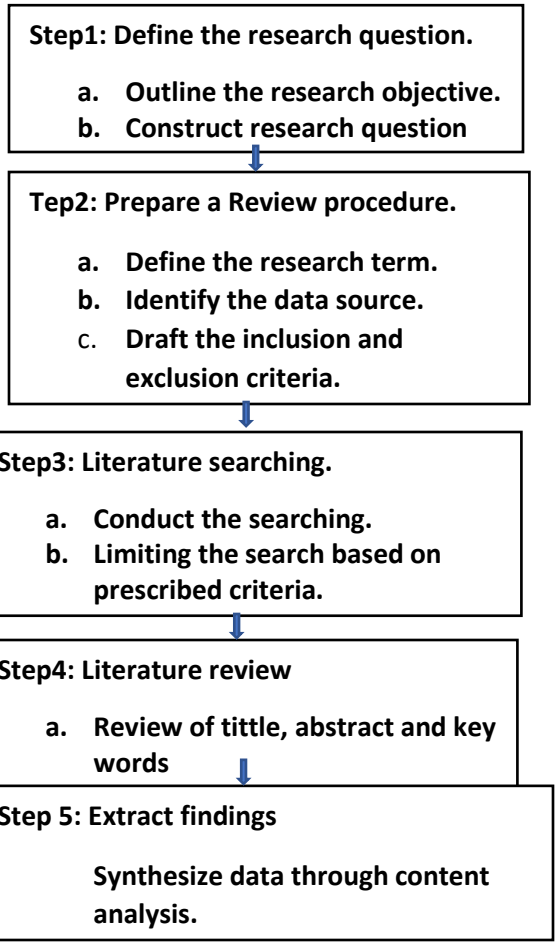

Figure 1. SLR process
Source: Adapted from Janjua et al. (2021)

3.2 Exclusion criteria

Studies that mentioned capital structure in the abstract only. We found few studies that mentioned it in their titles or opening sentences as a principal concept; however, they did not address it as the primary focus.

i. Studies that address capital structure from perspectives other than Islamic Banks, i.e., Conventional Capital structure.
ii. Introductory papers for books or book reviews and workshops.
iii. Editorials, keynotes, annals, tutorial summaries, tool demonstrations and panel discussions, books, technical reports, and other non-peer-reviewed publications.

3.3 Defining Research Questions

To get an overview of the current research work on the Capital structure in IB, we have defined the following three questions to achieve the objective:

Q1. To what extent has the literature addressed the capital structure of Islamic banks? The study will evaluate journals that published a high number of papers on capital structure in IB, which country leads in research on capital structure, and which year sees the highest publications.

Q2. What studies are presented in literature, and to what extent have they been addressed? This question investigates the gaps in the methods and types used in the Capital Structure in IB research and suggests the dimension for future research. We found several studies present different factors that determined the capital structure in IB. The study aimed to summarize the literature to get an overview of the capital structure in IB.

We began with conducting the search by using a simple string "Capital Structure" AND "Islamic Banks" in the Scopus databases to identify relevant journals and conferences publishing research on Capital structure. An overview of search results is shown in Table One, which explains further details of studies. Below is the title used in the Scopus database.

TITLE-ABS-KEY ("Capital structure" AND "Islamic Banks") AND (LIMIT-TO (DOCTYPE , "ar") OR LIMIT-TO (DOCTYPE , "cp")) AND (LIMIT-TO (SUBJAREA , "BUSI") OR LIMIT-TO (SUBJAREA , "ECON") OR LIMIT-TO (SUBJAREA , "SOCI")) AND (LIMIT-TO (LANGUAGE , "English")) AND (LIMIT-TO (SRCTYPE, "j") OR LIMIT-TO (SRCTYPE, "p"))

4. Result and Discussions

This section aims to synthesize the data. Therefore, we divided this section into general characteristics of the included studies (obtained from data extraction), an overview of capital structure theories, and the classification scheme we adopted in this study.

4.1 General characteristics of included studies.

This section presents some general characteristics of the included studies and answers to Research Question 1. We analyzed the studies to identify the publication trend, the distribution of the studies by years of publication, the country of research, and the journals mostly used to publish such studies. For this purpose, we recorded the basic information about the included studies in the data extraction form, such as author name, study title, journal, respective years of publication, country of research, research method, and nature of the study. The analysis based on this extraction is presented below.

The result in figure three showed that the publications on the capital structure of IB experienced a positive increase between 2009 to 2020, with articles sourced from scientific journals indexed by Scopus. This signifies that scholars, researchers, and practitioners began to pay attention to the issues of Islamic banking. However, these issues were caused by many factors, including this period after the global monetary crisis faced by many developing and Muslim countries around the world.

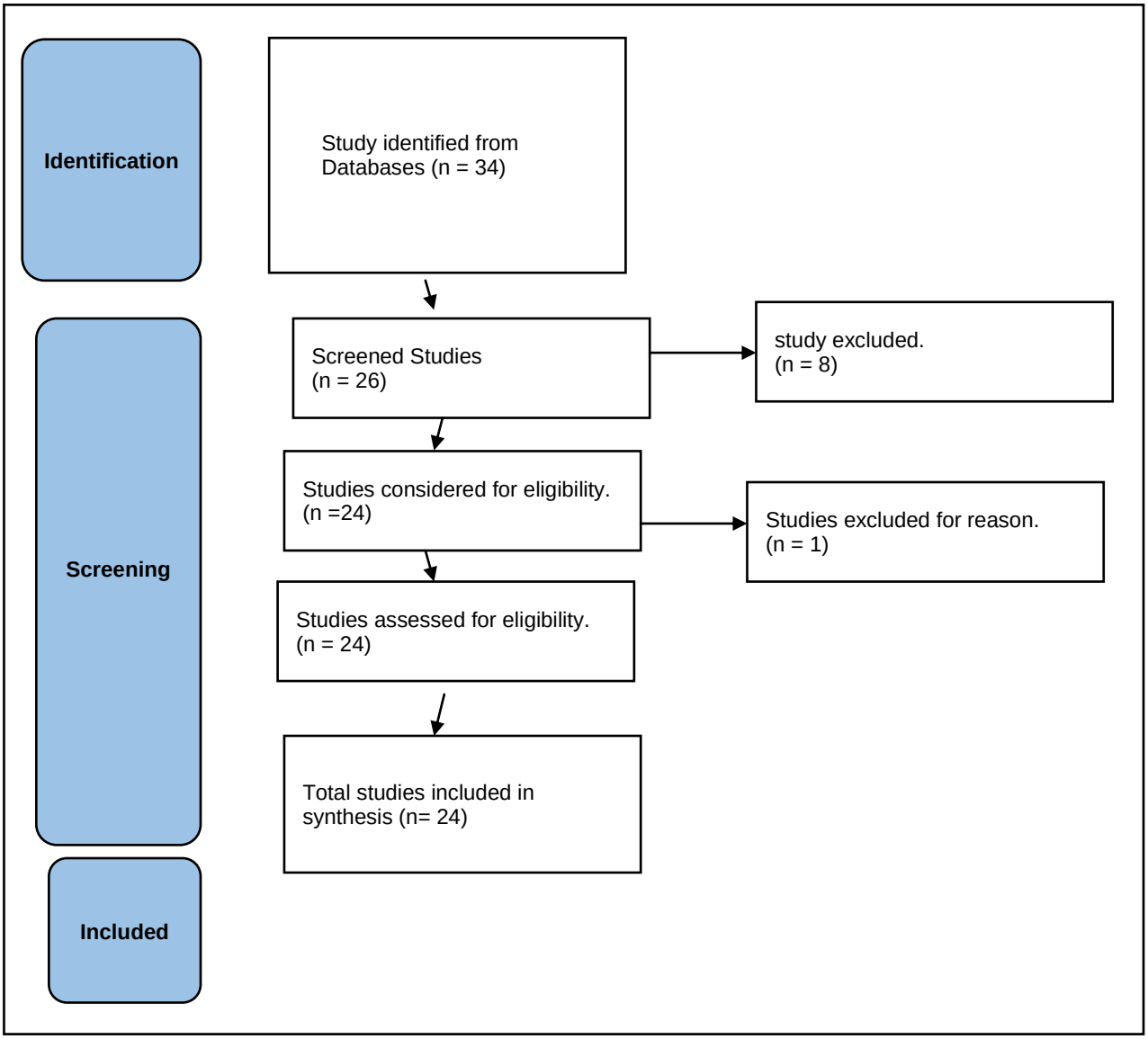

Figure 2: A PRISMA flowchart for the literature screening process.
Source: Adapted from Janjua et al. (2021)

Furthermore, after this crisis, several studies revealed that Islamic banking was able to withstand an economic crisis. In fact, it was disclosed that Islamic banking is capable of playing a maximum role in restoring the country's economy and increasing economic growth. Therefore, scholars, researchers, and practitioners began to focus on the issues of Islamic banking. However, they examined the factors that affect the performance of Islamic banking, capital Structure, the role of Sharia Law, the design of organizations, and a comparison of management and conventional banking.

However, the increase in the number of publications further shows a consistent increase in the number of publications on the capital structure of IB, except for 2017, 2018, and 2020. This confirms that the study of Capital Structure is becoming an attractive object for researchers, scholars, and practitioners in the field of Islamic banking. Furthermore, it is for the purpose of developing theories, concepts, models, and conceptual frameworks. Also, it is practical, such as making capital structure decisions on Islamic banking, service innovation, developing policies, adopting Sharia Law, and formulating strategies to increase capital finance.

Furthermore, the consistent increase in the number of publications shows that the topic of Islamic Bank capital structure will continue to receive serious attention from scholars, researchers, and practitioners. This impacts the development and expansion of the study area related to Islamic banking issues, which in turn contributes to the increase in the number of publications and high public interest in the studies in all developing and Muslim countries.

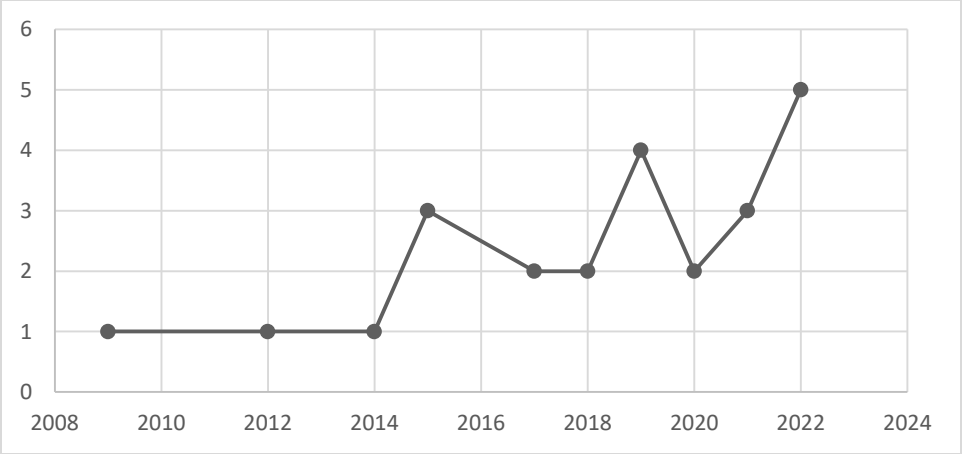

Figure 3: Distribution of publications by year
Source: Author's Computation

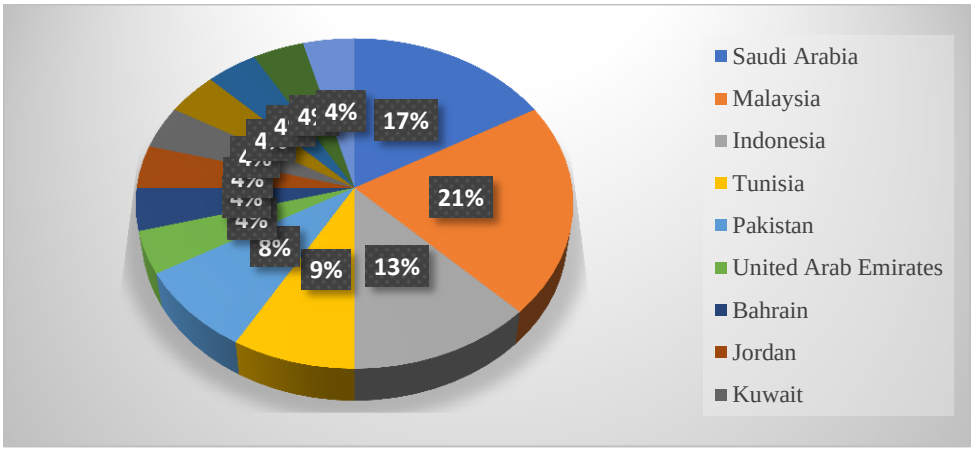

Figure4: the number of Journals based on the country's names in the last 14 years.
Source: Author's Computation

The important finding in the study is that scientific publications on Islamic banking have shown positive developments in the last fourteen years. However, the Muslim-majority countries, such as Malaysia, Saudi Arabia, Indonesia, Pakistan, and others, contributed to the increase in the number of scientific publications on Islamic banking. The findings of this study confirm that the Capital Structure in IB has received much attention from scholars and researchers in various countries and will continue developing the concept and complexity of problems (González et al., 2019; Ifada et al., 2019).

Figure 5: The number of articles on Islamic banking based on journals in the last fourteen years.
Source: Author's Computation.

However, the development of the Islamic Bank Capital Structure is related to the yearly increase in the number of countries, perspectives, approaches, and publications. This shows that the study of Islamic banking is not only explained from the perspective of economics, accounting, and Sharia but also the social sciences, humanities, and other disciplines. Therefore, the diversity of perspectives shows that Islamic banks are an object of study, which is explained by various disciplines that allow Islamic banking issues to be well-expressed and conceptualized.

From the above figure based on inclusion criteria, this review clearly shows that only journal articles and conferences are eligible for this review. The highest number of studies observed for this research are from "The International Journal of Islamic and Middle Eastern Finance" with a frequency of seven studies, The second-highest frequency of four studies is from "The Journal of Islamic Accounting and Business Research". However, three studies are from "Afro Asian Journal of Finance and Accounting" and two articles are from the journal of "International Journal of Business and Management Science, Journal of Asian Finance Economics and Business, and Journal of Financial Services Marketing". Journals with one frequency include the International Journal of Finance and Economics, Journal of Economic Cooperation Among Islamic Countries, Journal of Financial Reporting and Accounting and Research in International Business and Finance, respectively.

4.2 An Overview of Capital Structure Theories

According to Guizani and Ajmi (2021) The seminal papers of Modigliani and Miller (i.e., MM Theory) provided new insight into an optimal capital structure by proving the irrelevance of capital structure decisions under restrictive assumptions in which neither capital structure nor dividend policy should have any effect on the firm's value. With that, their seminal works have been acknowledged as a milestone of corporate finance literature. Since then, subsequent works have relaxed some of the restrictive assumptions of MM and introduced market frictions into the model, for instance, taxes, bankruptcy costs, and asymmetric information (Baker & Wurgler, 2002). Factors that influence capital structure decisions are connected to these types of friction.

It is worth pointing out that a consensus of capital structure models that can explain all the basic facts does not exist in the corporate finance literature. For instance, all available capital structure models, such as trade-off theory, pecking order theory, agency theory, signaling theory, and market-timing theory, tend to contradict and have problems with different facts (Bessler et al., 2011). Initially, trade-off theory postulated that the firm balances the benefits of debt (tax shield) against the cost of using

debt (financial distress and bankruptcy). Selecting debt over equity can enhance the firm's value, yet it comes with a trade-off in the form of debt costs, potentially leading to bankruptcy. As the firm's leverage ratio increases, the risk of bankruptcy also rises (Khasawneh, 2020; Issa, 2020).

Furthermore, the pecking order theory suggests that a firm's capital structure evolves based on its changing financing needs and its efforts to reduce adverse selection issues (Qayyum & Noreen, 2019; Myers & Majluf, 1984). The pecking order theory ranks sources of financing based on the degree to which they are affected by asymmetric information. In that, the firm prioritizes its internal funds over equity. In other words, the pecking order theory is primarily based on the notion of asymmetric information between firm insiders and outsiders and the resulting adverse selection problem.

Agency theory explains that capital structure is the result of a manager's attempts to minimize the cost associated with the separation of management and control (Myers, 2001; Jensen and Meckling, 1976). Managers have the incentive to maximize equity value rather than the firm's value. Particularly, managers tend to engage in risky projects and even negative net present value (NPV) projects. In the case of successful projects, this attempt will benefit the shareholders as the gains from these projects accrue to the shareholders. However, in the case of failure, the debt holders will bear the losses. Because the debt is too risky, debt holders will demand a risk premium and eventually a high-interest payment as compensation for risky projects.

4.3 Classification Scheme

We categorized the selected studies into four perspectives. Each perspective is described below.

a. the theoretical feature of the capital structure of Islamic Banks.
b. accounting standard of Islamic banks
c. Factors determine capital structure decisions in Islamic Banks.
d. Islamic Banks' capital structure and performance and
e. Capital structure and Risk-taking.

a. The theoretical aspect of Islamic Banks' capital structure

The conventional theories in the capital structure include Modigliani and Miller's theory, the trade-off theory, the Agency cost theory, and the pecking order theory. These theories were developed to justify the preference between equity and debt, which contradict the principle governing Islamic banks' operation and capital structure decisions. Because of Sharia principles that dominate their operations, prohibiting the issuance or acceptance of the interest-bearing loan encourages the capital structure decision using the profit and loss sharing principle. The Islamic banks' capital structure has unique features different from Conventional Banks. The Islamic Bank's capital structure theory is considered all equity. The tenet of Sharia Law's dominance in the operation of Islamic banks requires banks to have a unique governance mechanism, transaction, assets, sources of raising funds, and risk management compared to conventional banks (Bukair, 2017).

b. Accounting standard of Islamic banks

The value of firms with a high debt ratio in their capital structure is much better compared to those with having low debt ratio. Ju et al. (2005) found that the value of firms maintaining a low debt ratio is lower than those maintaining a higher debt ratio. However, this financial instrument (debt) is a controversial issue in Islamic finance. Islamic firms are not free to choose the level of debt they want in their capital structure due to the unfair returns associated with debt financing (Zaher and Hassan, 2001). Accordingly, Islamic regulatory bodies have issued regulations that restrict the use of debt financing. The purpose of these regulations is to verify that all activities of firms listed in Islamic capital markets do not contradict the Sharīʿah. For example, the Accounting and Audit Organization for Islamic Financial Institutions (AAOIFI) Sharīʿah standard No. 21 states that Islamic institutions are allowed to use debt financing up to 30% of their total capital (AAOIFI, 2010).

The uniqueness of the Islamic banks' products brings many risks that require unique risk measurement and capital adequacy measures compared to conventional banks. Any failure of an Islamic bank will generate systemic risk for the financial system overall.

Furthermore, any failure will damage the Islamic banking sector. Also, in order for Islamic banks to receive international recognition they will have to fulfill many criteria, and compliance with international standards is one of them. According to AAOIFI (1999), the capital of Islamic banks is exposed to three types of risks: commercial risk, fiduciary risk, and displaced commercial risk.

They also suggest that PLS accounts should not be included in the risk-bearing capital. All assets financed by the debt-bearing liabilities and own capital should be included in the calculation of the capital adequacy ratio. The weight of PLS accounts within the capital adequacy calculation should be 50 percent of the total PLS Separate capital adequacy standards may be applied for PLS accounts and current accounts in order to establish comparability (Khan and Ahmed, 2001, Chapra and Khan, 2000). Muljawan et al suggest that the amount of PLS accounts should not exceed the combined amount of equity capital and the mark-up amount of trade-related credit instruments. Hassan and Choudhury suggest that the suggested risk weight of 50 percent by AAOIFI for investment accounts should be raised to 100 percent to determine capital adequacy as per Basel II.

c. **The determinant of Islamic Banks' capital structure**

The remaining part of the literature category explains the determinant of the Islamic Bank capital structure, the studies that investigate the determinant include Guizani, (2020); Guizani and Ajmi, (2021); Al-Hunnayan, (2017) and Bukair, (2017). Previous literature shows a significant association between capital structure and the following determinant factors: tangibility, profitability, Bank size, growth opportunity, and liquidity. The study by Guizani (2020) categorized the determinant factors of capital structure into (1) Banks level determinants: tangibility, nondebt tax shield, bank size, profitability, liquidity, growth opportunity, and risk. (2) Macroeconomic determinants consist of gross domestic product (GDP) growth, financial market development, and oil price. The oil price was included because the study focused on GCC countries with oil-based economies. However, our focus is on the variables that appear in most studies.

Tangibility: The tangibility of the bank asset represents the collateral in case of any financial distress. Tangibility is measured as the ratio of the fixed asset to the firm's total asset. Money lenders recognize the tangible asset as having much value when the firm faces a liquidation problem. Therefore, tangibility is expected to impact the level of leverage in the firms positively. The studies that revealed the positive impact of tangibility on leverage include Batira (2017), Sekiti et al. (2017), and Guizaini (2020). While Bukairi (2017) found no relationship between tangibility and leverage. Other studies found a negative relationship, such as Toumi (2019), ALhunayyi (2019), and Guizaini (2020)

Profitability: Islamic Banks raised funds through the mobilization of Profit-sharing investment, which changes their capital structure and reduces their exposure to risk and leverage as a result of banning ribba and the requirement of profit-sharing principles. Under this agreement, Islamic banks share profit generated with PSIAs on the bases of the pre-agreed ratio. Losses in PSIAs funds are to be borne by holders except in the case of negligence by Islamic banks. Consequently, Islamic banks' characteristics allow them to pass financial shock on the asset side to financiers. The total Islamic Banks' risk is theoretically less than conventional Banks, considering banning interest principles (Toumi, 2019).

The deposits generated by Islamic Banks should positively affect their overall profit. The greater the amount realized through deposits, the better the bank can expand and diversify its operations to realize more profit. However, there are inconclusive results on the relationship between capital structure and profitability in I.B. Batire et al. (2017) revealed a positive relationship between profitability and leverage. The studies by Guizaini (2020) and Guizani and Ajma (2021) revealed a negative result while Bukair (2017) and Khokher and Alhabshi (2019) showed no significant effects.

Bank size: larger banks are frequently able to diversify resources due to their experiences and reputations and are less prone to bankruptcy. The large is able to furnish outside investors with better information and minimize information asymmetry, which motivates equity

financing. Guizani (2021) argued that larger Islamic Banks are also better off managing risk due to the type of their business contract rooted in Sharia principles. Consequently, larger Islamic banks have more leverage. The literature revealed inconclusive results on the impact of Bank size on leverage. However, several studies have shown a positive impact of Bank size on leverage, including Guizaini (2021), Guizani and Ijmi (2021), Alhunnaya (2022), Bukair (2017) but Qayyum and Noreen (2019) and Bateri et al. (2017) revealed negative impact.

Growth opportunity: The Pecking order Theory states that a firm's leverage is positively impacted by growth opportunities because firms with higher opportunities require a higher amount of cash to meet their cash shortfall and restrict their commitment to costly external finance. The reason for the higher growth opportunities in Islamic Banks is the quick exhaustion of the internal sources of finance and more external finance is required to meet the growth opportunities. Contrarily, the study by Bitare et al. (2018) clarified the negative effect of growth opportunities on Islamic Banks' leverage. They have recommended that Islamic banks be more transparent in their transaction in compliance with Sharia Law and less exposed to information asymmetric. The result of Alhunnaya (2017) revealed a positive relationship between growth opportunities and the leverage of Islamic Banks, while Guizani and Ajmi (2021) and Bulair (2017) showed that the relationship was not significant.

Liquidity: Liquidity is the ratio of current assets to current liability. It demonstrates a company's capacity to fulfill its immediate responsibilities (short-term liability). Therefore, liquidity is vital in leverage decisions. According to the trade-off theory, banks with higher liquidity are less vulnerable to bankruptcy costs and have a better chance of raising debt. In the case of IBs, there is limited liquidity due to the Sharia Law. They cannot raise funds through debt or the use of financial derivatives. But Islamic Banks prefer to hold liquidity to maintain higher capital to restrict financial risk. Bukair (2019) opined that banks holding more liquidity may have increased the capital structure by minimizing the liquidity risk by reducing debt demand. Bukair (2017) and Batire et al. (2017) show the positive impact of liquidity on leverage, while Guzaini (2020), Guzaini and Ijma (2021), and AlHunnaya (2017) revealed a negative effect.

d. **Islamic Banks' Capital Structure and Performance**

The relationship between capital structure and firms' performance has been broadly examined in Islamic banks with mixed results. Some research revealed no association between capital structure and Islamic banks (Rozaq et al., 2021), while other studies support a negative impact of capital structure on financial performance (Khasawneh, 2020).

Saiti and Akhtar (2017) stated that prior research revealed that banks with high capital ratios could experience negative effects on their profit efficiency, that is, the large capital ratio adversely affects the profit performance. Furthermore, the results also revealed that the negative effect of capital structure on financial performance was higher in Islamic banks than in conventional Banks. Therefore, IB management is required to enhance its financial performance and efficiency.

Maher (2018) investigated the impact of the capital structure on the Banks' performance in Pakistan between 2011 and 2017. The study proxied the capital structure with three leverage variables: total debt ratio, long-term to total equity, and short-term to total equity. The result showed a significant variation in the impact of the capital structure variables on performance. In another vein, Sadiki et al. (2017) examined the effect of capital structure on the financial performance of Banks in Bangladesh for the period 2005 to 2014. The result underpinned the inverse relationship between capital structure and the financial performance of Islamic Banks. It is worth concluding that the impact of capital structure on Islamic banks' financial performance is unclear.

e. **Capital Structure and Risk-taking in Islamic Banks**

Previous studies indicate the impact of capital structure on banks' risk. Banks with high leverage are able to absorb more economic shocks, which makes them riskier (Khasawneh, 2020; Khan & Ahmed, 2001) . In the conventional finance literature, higher leverage is related to the increase in the cost of debt, which affects performance and increases risk. In the case of Islamic

Banks, a few studies investigated capital structure and risk. Rozaq et al. (2021) examined the effect of capital structure and operational efficiency on Islamic banks' risk from 2014 to 2018. The result showed that capital structure had no effect on the risk while operational efficiency significantly impacts the risk of Islamic Banks. Guizani (2020) revealed that risk was negatively related to the leverage of Islamic Banks. Another study by Khokher Alhabshi (2019) showed that risk absorbed by PSIA had a negative and significant impact on the leverage of Islamic Banks.

5. Conclusion and Recommendations

The study reviewed the literature on the capital structure of IB for the last fourteen years using the PRISMA approach. The descriptive results presented include the distribution of the publications by the years, journals, and countries. There is a yearly increase in the number of publications due to factors, such as the period to be after the crisis of global monetary faced by many developing and Muslim countries around the world. As a result, scholars, researchers, and practitioners began to focus on the issues of Islamic banking. Contribution by countries revealed that the capital structure of Islamic banks is produced mostly in Asian countries, such as Malaysia, Pakistan, Kuwait, Saudi Arabia, and the United Arab Emirates, where Islamic Banks predominantly operate. Limited literature in the field related to theories necessitated the need for more effort to develop an analytical framework and address contemporary issues facing Islamic banks' capital structure.

This study is not free from limitations. First, it only employed a single database, namely Scopus. Further studies may use other databases, such as Web of Science, Google Scholar, PubMed, etc. to generate more search results with different publication quality. Combining those databases is also possible to obtain more diverse results. Besides, using less-prestigious indexing bodies may allow for more up-to-date documents because their publication criteria are not strict as the slots indexed in Scopus. Second, further studies may expand the document types to other sources, such as Book chapters and series, because this study included various types. Selecting only journal articles and conference proceedings may allow focusing on the peer-review slots.

However, based on the analysis of the literature, the capital structure of IB showed no conclusive result queries, such as the determinant of capital structure, the nexus between a capital structure with performance, and capital decision, which create the opportunity for future research. The theoretical aspect is still debated, as some scholars use conventional theory in capital structure decisions in Islamic Banks. In contrast, others oppose the adoption of contemporary capital structure alongside Islamic Banks' moral values. Most previous research on the capital structure of Islamic banks has theoretical constraints; therefore empirical studies with strong theoretical backing are needed to help management and policymakers to make better judgments about the capital structure of Islamic banks.

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