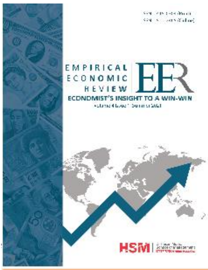

Empirical Economic Review (EER)

Volume 5 Issue 1, Summer 2022
ISSN: 2415-0304(P) 2522-2465(E)
Journal DOI: https://doi.org/10.29145/eer
Issue DOI: https://doi.org/10.29145.eer.51
Homepage: https://ojs.umt.edu.pk/index.php/eer

Article: **Impact of Maqasid al-Shariah Based Social Performance on the Financial Performance of Islamic Banks: Evidence from Pakistan**

Author(s): Muhammad Mansoor Javed[1], Rukhsana Kalim[2], Mohammad Ayaz[2]

Affiliation: [1]University of Gujrat, Gujrat, Pakistan
[2]University of Management and Technology, Lahore, Pakistan

Article DOI: https://doi.org/10.29145/eer.51.06

Article History: Received: August 11, 2021
Revised: December 23, 2021
Accepted: February 21, 2022
Published Online: May 30, 2022

Citation: Javed, M. M., Kalim, R., & Ayaz, M. (2022). Impact of Maqasid al-Shariah based social performance on the financial performance of islamic banks: evidence from Pakistan. *Empirical Economic Review*, *5*(1), 74–89. https://doi.org/10.29145/eer.51.06

Copyright Information: This article is open access and is distributed under the terms of Creative Commons Attribution 4.0 International License

Journal QR

Article QR

Muhammad Mansoor

Indexing

A publication of
The Department of Economics and Statistics, Dr. Hasan Murad School of Management, University of Management and Technology, Lahore, Pakistan

Impact of *Maqasid al-Shariah* Based Social Performance on the Financial Performance of Islamic Banks: Evidence from Pakistan

Muhammad Mansoor Javed*[1], Rukhsana Kalim[2] and Mohammad Ayaz
[1]University of Gujrat, Gujrat, Pakistan
[2]University of Management & Technology, Lahore, Pakistan

Abstract

The current study examined the impact of *Maqasid al-Shariah* based social performance of Islamic banks on their financial performance. It regressed financial performance on *Maqasid al-Shariah* based social performance using a robust fixed effect model after controlling for capital ratio, operating expense ratio, liquidity risk, and capital intensity. Unbalanced panel data was collected from the annual reports of all full-fledged Islamic banks operating in Pakistan for the period 2008-2018. The results revealed a significant positive influence of *Maqasid al-Shariah* based social performance on financial performance, inferring that an improved *Maqasid al-Shariah* based social performance leads to superior financial performance. Therefore, it is recommended that Islamic banks should increase their *Maqasid al-Shariah* based social performance. It will not only enhance their 'Islamic' image but will also improve their financial performance, resulting in creation of/increasing their shareholders' wealth. This study contributes to the literature on the relationship between social performance and financial performance by measuring social performance from the perspective of *Maqasid al-Shariah*.

Keywords**:** index development, *Maqasid al-Shariah*, social performance

Introduction

The term *Maqasid al-Shariah* is a combination of two separate words, that is, *'Maqasid'* and *'Shariah'*. The word *'Maqasid'* means objectives, whereas the word *'Shariah'* literally means 'pathway'. Technically, *Shariah* is defined as compliance with Allah Almighty's instructions. Collectively, *Maqasid al-Shariah* are defined as the "rationale of the *Shariah*" or "the wisdom behind the *Shariah* rulings". Their purpose is to pursue the betterment of humankind under divine directions and guidance (Dusuki & Abozaid, 2007).

Laldin and Furqani (2013) highlighted three *Maqasid al-Shariah* related to financial transactions. These *Maqasid* are the circulation of wealth, transparency, and justice. Circulation of wealth includes the creation, distribution, utilization, and consumption of wealth. The Holy Quran encourages the circulation of wealth among all the segments of the society in order to prevent the hoarding of money/wealth in a few hands (Quran 59:7; 6:141; 9:34). Therefore, *Shariah* has imposed *Zakat* (obligatory charity) to discourage the accumulation of idle wealth. Transparency requires that all the contracting parties should be well informed about the details of the covenant (Quran 2:282). As far as justice is concerned, the Quran describes it as fairness, equality, balance, harmony, and moderation. Justice has two dimensions: macro and micro. Justice at the macro level involves social justice. It requires that the basic needs of the individuals belonging to all the sectors/segments of the society should be satisfied.

*Corresponding Author: mansoor.javed@uog.edu.pk

Justice at the micro level requires that all individuals should have equal rights and opportunities and should be protected from biased dealing (Quran 2:188; 16:90).

Islamic banks can distinguish themselves from conventional banks by pursuing the above mentioned *Maqasid al-Shariah*. However, empirical studies have revealed that the main focus of Islamic banks remains profit maximization; consequently, they ignore the purpose/outcomes/implementation of *Maqasid al-Shariah* (Javed et al., 2020). As a result, they have been converging towards their conventional equivalents (Qoyum, 2018) . This argument is based on the notion that Islamic banks replicate the conventional financial products instead of inventing new ones, focusing only on the 'form' of the agreement and ignoring the 'substance' of the contract (Hanif, 2016). 'Focusing on the form of the agreement' entails the satisfaction of the basic requirements of an agreement regarding offer, acceptance, subject matter, and the capacity of the contracting parties. Whereas, 'ignoring the substance of the contract' refers to disregarding the intentions of the contracting parties regarding the purpose of the contract, along with its impact on the economy.

Shariah emphasizes that the requirements related to both 'form' and 'substance' should be satisfied. Moreover, the economic impact/basis of the contract should not contradict with the principles of the *Shariah*. However, *Shariah* scholars have divergent opinions when there is a trade-off between 'form' and 'substance'. *Shafi* scholars prioritize the 'form' of the contract, asserting that only Allah Almighty knows the hidden intentions of the people. Therefore, they focus on 'what is written' while validating the financial contracts. In contrast, *Hanafi*, *Maliki* and *Hanbali* scholars emphasize the 'substance' of the agreement, highlighting the Islamic legal maxim that states "In contracts, the primary consideration will be given to objectives and underlying meanings, not to their words and forms" (Bakar & Mansoor, 2020; Hamour et al., 2019).

The above debate regarding 'form vs. substance' has resulted in the classification of the financial products offered by Islamic banks into three categories, that is, pseudo-Islamic products, *Shariah* compliant products, and *Shariah* based products (Ahmed, 2011). Pseudo-Islamic products meet the criteria related to the 'form', only. Consequently, their effect on the economy is the same as that of their conventional equivalents. On the other hand, *Shariah* compliant products satisfy the criteria related to both 'form' and 'substance'. However, they fail to fulfill the *Maqasid al-Shariah* associated with them. In contrast, *Shariah* based products do not only fulfill the requirements related to both the 'form' and 'substance' of the contract but they also achieve the related *Maqasid al-Shariah*.

Considering the above classification of finanical products, Islamic banks claim that all of their products are legitimate or *halal* by highlighting the *Fatawa* (pronouncements) given by the members of their *Shariah* board. However, it is argued here that Islamic banks have developed their financial products using different *hiyal* (legal tricks) to meet the legal requirements of the contract imposed by the *Shariah*. This practice is treated with skepticism by their potential clients, who demand additional evidence regarding the *Shariah* legitimacy of these products. This 'additional' evidence can be provided by analyzing the financial products of Islamic banks using the framework of *Maqasid al-Shariah* (Elahi, 2011). It requires that while developing finanical products, Islamic banks should consider their social impact along with their financial outcomes (Ayub, 2018).

Accordingly, some studies constructed *Maqasid al-Shariah* based indices to evaluate *Maqasid al-Shariah* based social performance of Islamic banks. They reported unsatisfactory results, inferring that Islamic banks do not accomplish *Maqasid al-*

Shariah (Ascarya et al., 2016). These findings validated the criticism that Islamic banks have been converging towards their conventional equivalents. Therefore, they are required to improve their *Maqasid al-Shariah* based social performance, so as to distinguish themselves from their conventional counterparts (Zaheer & Rasool, 2017).

The objective of the current study is to determine how the top management of Islamic banks can be motivated to improve *Maqasid al-Shariah* based social performance. Therefore, it examines the impact of *Maqasid al-Shariah* based social performance on profitability, as better social performance may lead to superior financial performance, which results in creation of/increasing the shareholders' wealth. Accordingly, the expected creation of/predicted increase in wealth may motivate the top management of Islamic banks to enhance their *Maqasid al-Shariah* based social performance. The remaining parts of the current paper comprise literature review, methodology, results, and conclusion, respectively.

Literature Review

Intensive research has been carried out on the relationship between financial and social performances since the emergence of the stakeholder theory, which suggests that managers should keep in view the interests of all stakeholders instead of focusing on shareholders' interests only (Freeman, 1984). However, the results are still inconclusive due to mix findings with respect to both the sign and direction of the relationship. The existing literature has certain limitations in this regard including an unclear definition of corporate social responsibility (CSR), poorly identified control variables, self-developed CSR disclosure measures, and reporting bias for favorable findings (Beck et al., 2018).

Islamic worldview states that Allah Almighty has appointed humankind as His *Kahlifah* (vicegerent) on earth and endowed it with natural resources as *amanah* (trust), which should be managed for the benefit of all in order to improve the world on His behalf (Quran 2:30). Therefore, wealth should be considered as *fadl-e-Allahi* (bounty from Allah) and should be acquired through allowable means (Quran 4:29). Satisfying this condition will bring *barakah* (divine blessing), that is, an unexplainable increase in the benefit of wealth. It implies that adherence to the *Shariah* results in prosperity. Hence, a positive relationship between *Maqasid al-Shariah* based performance and profitability is expected.

This notion is also supported by some ethical and conventional theories that explain the association between social performance and profitability. For example, according to the good management theory, the eventual goal of top management is to increase shareholders' wealth by taking competitive advantages through fulfilling the expectations and aspirations of other stakeholders (Miles & Covin, 2000). Similarly, "social impact hypothesis" suggests that improved social performance results in increased profitability, since meeting the claims of all stakeholders enhances a firm's repute. Whereas, ignoring these claims increases risk which consequently increases the cost of the capital (Preston & O'bannon, 1997).

Conversely, the neoclassical finance theory suggests that the opportunity to invest in a socially responsible firm is a product, which can be sold to investors having interests other than wealth maximization. The demand and supply of such opportunities defines the association between social performance and profitability; hence, social performance may increase, decrease, or have no influence on the firm value (Rivera et al., 2017). Similarly, the "trade-off hypothesis" suggests that a higher social performance results in lower profitability, as social deeds involve/incur financial costs (Preston & O'bannon, 1997).

Empirical studies on the association between social performance and profitability reported both confirmatory and contradictory results. Based on their findings, these studies can be divided into three groups. The first group consists of studies that found a significant positive relationship between social performance and profitability (Platonova et al., 2018). The findings of this group of studies are supported by the good management theory and social impact hypothesis. The second group of studies revealed that a negative association exists between social performance and profitability (Nguyen, 2018). The findings of this group of studies are consistent with the trade-off hypothesis. On the other hand, the third group of studies argued that a neutral relationship exists between social performance and profitability, mediated by other variables (Adeneye & Ahmed, 2015).

Nevertheless, the majority of empirical studies revealed a positive association between social performance and profitability. For instance, after reviewing 84 studies conducted on the relationship between social performance and profitability, Lu et al. (2014) reported a positive and bidirectional association between the two variables. Similarly, Chih and Chih (2014) examined the influence/effect/impact of the media coverage of engagement in social activities on profitability and found that the quality of news coverage has a significant positive relationship with profitability. Likewise, using a meta-analytic framework, Wang et al. (2016) evaluated 42 experimental studies and found a positive relationship between social performance and profitability, endorsing/strengthening the argument that commitment to social welfare increases profitability. They also found that such a relationship is stronger for companies operating in developed economies. Likewise, Blasi et al. (2018) conducted a multidimensional assessment of the social performance and profitability relationship by considering/incorporating 7 macro categories of social performance and 6 accounting-based and market-based indicators of profitability into their analysis. Their study was based on a sample of 988 US companies from 9 different sectors. They found that, depending on the social performance category in which a company invests, social performance generally increases a firm’s stock return. On the other hand, Sekhon and Kathuria (2019) examined the influence/effect/impact of engagement in social activities on profitability using 10-year data of 137 companies operating in India. They used three proxies to measure profitability, that is, return on equity, return on assets and profit margin. They found a neutral correlation between social performance and profitability, when the latter was measured using return on asset or profit margin. On the other hand, they found a negative correlation between these two variables, when profitability was measured as return on equity. In another study, using the data of 191 companies listed on Korean Stock Exchange, Cho et al. (2019) examined the relationship among social performance, profitability, and firm value. They measured social performance using KEJI index, profitability using return on asset, and firm value using Tobin’s Q. Their findings revealed a positive association between social performance and profitability, as well as between firm value and social performance. In a recent study, Lahouel et al. (2021) examined the relationship between social performance and profitability using a novel methodology. They explored the stated relationship keeping in view the endogeneity issues and by applying both dynamic and static models. Their findings explicated that commitment towards social activities influence/affects/imapcts profitability negatively.

Some studies examined the role of moderators and mediators while exploring the relationship between social performance and profitability. For example, Wang and Berens (2015) argued that the association between social performance and profitability is mediated by two categories/kinds of reputation, that is, reputation among public stakeholders and reputation among financial stakeholders. They argued that different forms of social activities impact these two kinds of reputation differently. Hence, this classification is essential to understand the effect of the various types of social activities on profitability. Likewise, while exploring the association between social performance and profitability, Sindhu and Arif (2017) observed a positive association between them, partially mediated by a firm’s reputation, customer satisfaction, and competitive advantage. Similarly, Martin et al. (2018) examined the moderating effect of high-low profile industry on the link between social performance and profitability. By analyzing three-year data of 9 low profile and 12 high profile Malaysian listed companies, they found that commitment towards social activities does not affect sales growth; however, it positively affects return on asset. In a recent study, Pereira et al. (2020) explored the impact of different moderators on the relationship between social performance and profitability. They found that disclosures related to sustainability did not influence the stated relationship.

In contrast, Wang et al. (2016) asserted that social performance and profitability have a non-static curvilinear association. Initially, commitment towards social activities deteriorates financial performance; however, further spending on social activities beyond a certain level improves profitability. Thus, their findings supported both the “trade off hypothesis” and “social impact hypothesis”, simultaneously. Similar results were found by Brower and Dacin (2020). They concluded that initially, engagement in social activities increases both profitability and firm value. However, further increase in social activities weakens the impact of social performance on profitability.

Some studies explored the association between social performance and profitability from the viewpoint of the Islamic banking industry. For example, Arshad et al. (2012) examined the impact of social activities disclosure on both profitability and reputation by analyzing the annual reports of Malaysian Islamic banks for a three-year period. Social activities disclosure was measured by constructing an index based on the Bursa Malaysia framework and the recommendations of prior studies; whereas, reputation was measured by constructing another index using GRI guidelines. The study found that social activities disclosure is positively associated with both reputation and profitability. Similar results were found by Iqbal, Ahmad, and Kanwal (2013). They analyzed the data of both conventional and Islamic banks of Pakistan for measuring social performance from/in three dimensions, that is, education, health, and donation. Likewise, Platonova et al. (2018) explored the association between social performance and profitability by analyzing fifteen-year data (2000-2014) taken from the annual reports of Islamic banks operating in the GCC region. Social performance index was developed using six dimensions including mission and vision statement, product and services, commitment towards employees, commitment towards debtors, commitment towards society, and charity funds. The results revealed that engagement in a composite social performance index improves profitability, not only in the current year but also in the upcoming year(s). However, as far as individual dimensions are concerned, it was found that only “mission and vision” and “product and service” dimensions had a significant positive effect on profitability.

The only study which examined the association between social performance and profitability from the perspective of *Maqasid al-Shariah* was carried out by Widarjono

(2018). The study analyzed the influence of *Maqasid al-Shariah* based performance on the profitability of 13 Indonesian Islamic banks. Three proxies were used to measure *Maqasid al-Shariah* based performance, namely *Maqasid al-Shariah* index, *muḍarabah* financing, and *musharakah* financing. The results revealed that the *Maqasid al-Shariah* index had no impact on financial performance, whereas *musharakah* financing had a positive impact and *muḍarabah* financing had a negative impact on financial performance. Moreover, the study used *Maqasid al-Shariah* index proposed by Mohammed, Dzuljastri, and Taib (2008). This index can be criticized on the grounds of having a limited scope, as it is based on fulfilling only three objectives.

The current study contributes to the existing literature by examining the influence/effect/impact of *Maqasid al-Shariah* based social performance on profitability using an improved index. The stated index consists of measures more reflective of a *Maqasid* oriented performance. Additionally, it overcomes the limitations of the existing indices. Moreover, as per authors' knowledge, no previous study has examined the association between social performance and profitability from the perspective of *Maqasid al-Shariah,* while targeting the Islamic banks operating in Pakistan.

Based on the above discussion, the following hypothesis was developed for the current study.

H1: *Maqasid al-Shariah* based social performance is positively related to financial performance.

Methodology

This study evaluates the influence of *Maqasid al-Shariah* based social performance on the profitability of all the five full-fledged Islamic banks operating in Pakistan, namely Meezan Bank, Al-Baraka Bank, MCB Islamic Bank, Bank Islami and Dubai Islamic Bank. The entire population comprised the sample of the study. Unbalanced panel data was taken from the annual reports for the period 2008-2018. Since MCB Islamic bank was established in 2015, only its three-year data (2016-2018) was available for consideration. Whereas, eleven-year data (2008-2018) of the other four banks was included in the analysis. As a result, the sample consisted of 47 observations for each variable (11 x 4 + 3 x 1 = 47). Sample size could not be increased as the relevant data was not available prior to 2008. Islamic banking branches of conventional banks were ignored/excluded for a more vivid analysis, following the example set by some earlier studies (Zaheer & Rasool, 2017). The following empirical model was developed to test the influence of *Maqasid al-Shariah* based social performance on financial performance.

$$ROAA = \alpha + \beta_1 MSSP + \beta_2 CpRato + \beta_3 OprExp + \beta_4 LiqRsk + \beta_5 CpInt + \acute{\varepsilon} \quad \ldots\ldots\ldots\ldots\ldots..(1)$$

where,

ROAA	Return on average assets
MSSP	*Maqasid al-Shariah* based social performance index
CpRato	Capital ratio
OprExp	Operating expense

LiqRsk	Liquidity risk
CpInt	Capital intensity

These variables are explained below.

Dependent Variable

Financial performance was the dependent variable of the current study. It can be measured using different market-based and accounting-based proxies. However, each proxy has its own limitations. Accounting based proxies are criticized on the grounds of subjectivity, whereas market-based proxies are affected by several unrelated factors. Nevertheless, the current study used an accounting-based proxy to measure financial performance, as all the sampled banks are not listed on the stock exchange. Hence, market-based proxies could not be applied. Additionally, despite their limitations, accounting-based indicators are considered more accurate and are widely used to assess financial performance (Simpson & Kohers, 2002).

Among accounting-based proxies for/of financial performance, return on average asset (ROAA) and return on average equity (ROAE) are frequently used in empirical studies. However, it has been argued that ROAE is not the best proxy to evaluate financial performance, since it ignores the higher risk associated with high leverage. Consequently, banks with higher equity or lower leverage report low ROAE but high ROAA (Dietrich & Wanzenried, 2011). Therefore, following Platonova et al. (2018), this study adopted ROAA as the dependent variable. It was computed as net income to average total assets.

Independent Variable

Maqasid al-Shariah based social performance was the independent variable of the current study. This variable was computed using the index constructed by (Javed et al., 2020). Javed et al. (2020) developed the index on the basis of five *Maqasid*, namely protection of faith, protection of life, protection of intellect, protection of family, and protection of wealth. By applying the behavioral science method introduced by (Sekaran & Bougie, 2019; Javed et al., 2020) operationalized these *Maqasid* into observable dimensions and measureable elements. These dimensions and elements were identified by applying the social accounting concept of the 'value added statement' and 'service-profit chain' logic, as well as by using the recommendations of some earlier studies (Mohammed et al., 2008; Mohammed et al., 2015; Zaheer & Rasool, 2017).

The proposed dimensions and elements were later validated through experts' interviews. Five experts of Islamic economics from the academia and five *Shariah* scholars associated with the Islamic banking industry were interviewed. Almost all the experts endorsed the appropriateness of the identified dimensions and related elements, after exhaustively discussing the relevant concepts. Later on, these elements, along with the stated *Maqasid*, were assigned weights based on their importance and relevance to Islamic banks through a survey conducted with 20 *Shariah* experts associated with these banks. This method of assigning weights has been used also in earlier/prior studies (Mohammed et al., 2008; Zaheer & Rasool, 2017). Table 1 shows the index developed by (Javed et al., 2020).

Table 1
Maqasid al-Shariah based Social Performance Index

Maqasid	Weight	Elements/Indicators	Weight
Faith	0.30	Non-controversial financing/total financing	0.50
		Non-controversial investment/total investment	0.50
		Dimension Total	**1.00**
Life	0.14	Individual Financing/Total Financing	0.31
		Charity distributed/Distributable charity	0.32
		Charity for health and welfare /Total charity	0.37
		Dimension Total	**1.00**
Intellect	0.05	Investment in Technology/Investment in operating assets	0.22
		Advertisement Expense/Total expense	0.24
		Charity for Education/Total charity	0.54
		Dimension Total	**1.00**
Family	0.23	Value distributed to employees/total value added	0.19
		Value distributed to depositors/total value added	0.27
		Value distributed to shareholders/total value added	0.26
		Value distributed to government/total value added	0.08
		Bank's financing/Total financings of the IB sector	0.20
		Dimension Total	**1.00**
Wealth	0.28	Net financing/Gross financing	0.25
		Liquid asset/Total deposit	0.20
		Profit after tax/Net assets	0.35
		Available capital/Risk weighted assets	0.20
Total	**1.00**	**Dimension Total**	**1.00**

Source: Javed et al. (2020)

Using the weights shown in Table 1, *Maqasid al-Shariah* based social performance was measured using the following equation.

$$MSSP = \sum W_i \left(\sum W_j E_j\right)_i \qquad (2)$$

where,

MSSP *Maqasid al-Shari'ah* based social performance Index
W_i Weight of the *Maqasid*
W_j Weight of the element
E_j Value of the element

Control Variables

Using the recommendations of the existing literature, the current study analyzed the influence of *Maqasid al-Shariah* based social performance on financial performance by controlling certain variables, namely capital ratio, operating expense, liquidity risk, and capital intensity.

Banks with a high capital ratio can follow up business opportunities more efficiently; therefore, they are more adept to cover potential losses and earn higher profits (Platonova et al., 2018). The positive influence/effect of capital ratio on profitability was confirmed by several empirical studies (Athanasoglou et al., 2008). Following Platonova et al. (2018), the current study measured capital ratio as "equity to average total assets".

Operating expense is an important determinant of a bank's financial performance. It has a negative relationship with profitability. Following Athanasoglou et al. (2008), the current study measured operating expense as the ratio of "total non-interest expense to average total assets".

Liquidity risk can affect a bank's profitability as it restricts the bank from availing other investing or financing opportunities (Arif & Anees, 2012). Empirical literature also suggests that liquidity risk affects the relationship between social and financial performances (Barnett & Salomon, 2012). The current study measured liquidity risk as "financing to deposit ratio" following (Widarjono, 2018).

Capon et al. (1990) argued that capital intensity negatively affects a firm's profitability. Following Wang and Berens (2015), this study measured capital intensity as the ratio of "fixed assets to total assets". Table 2 exhibits/provides the description of the variables used in the current study.

Table 2

Description of Variables

Variable	Abbreviation	Measurement	Sign
Dependent			
Return on Average Asset	ROAA	Net income to average assets	
Independent			
Maqasid al-Shariah Based Social Performance	MSSP	Using index developed by Javed et al. (2020)	+
Control			
Capital Ratio	CpRto	Equity capital to average total assets	+
Operating Expense Ratio	OprExp	Total non-interest expense to average total assets	-
Liquidity Risk	LiqRsk	Total financing to total assets	-
Capital Intensity	CpInt	Fixed assets to total assets	-

Data Analysis and Results

Descriptive Statistics

Table 3 exhibits the descriptive statistics. It depicts that the maximum and minimum values of ROAA range between 0.019 and -0.031. The mean value of ROAA is 0.002, while the value of standard deviation is 0.010. Thus, the value of standard deviation is higher than the mean value. It indicates that ROAA is overdispersed, that is, the data does not follow a homogenous pattern for all Islamic banks. A possible reason for this over dispersion is that some banks suffered financial losses in particular years, while others earned profit during the same period.

For *Maqasid al-Shariah* based social performance index, the maximum and minimum values vary between 0.572 and 0.462. The mean value of the index is 0.522, while the value of standard deviation is 0.027. Thus, the value of standard deviation is lower than the value of mean. This infers/It indicates that the *Maqasid al-Shariah* based social performance index is underdispersed, that is, data follows a homogenous pattern for all Islamic banks. Hence, the role/contribution of all Islamic banks in *Maqasid* realization is almost the same.

As far as control variables are concerned, the maximum and minimum values of capital ratio are 0.531 and 0.047, respectively. The value of mean is 0.116 and the value of standard deviation is 0.087. For operating expense, the maximum value is 0.079 and the minimum value is 0.023. The value of mean is 0.040 and the value of standard deviation is 0.014. Liquidity risk has the maximum and minimum values of 1.133 and 0.348, respectively. The value of mean is 0.596 and the value of standard deviation is 0.165. The values for capital intensity vary between 0.006 and 0.100. The values of mean and standard deviation are 0.034 and 0.022, respectively. These statistics indicate that all the four control variables, namely capital ratio, operating expense, liquidity risk, and capital intensity are underdispersed, manifesting that the data follows a homogenous pattern for all Islamic banks.

Table 3

Descriptive Statistics

Variable	N	Mean	Minimum	Maximum	Standard Deviation
ROAA	47	0.002	-0.031	0.019	0.010
MSSP	47	0.522	0.462	0.572	0.027
CpRato	47	0.116	0.047	0.531	0.087
OprExp	47	0.040	0.023	0.079	0.014
LiqRsk	47	0.596	0.348	1.133	0.165
CpInt	47	0.034	0.006	0.100	0.022

Source: Self-constructed Diagnostic Tests

Some diagnostic statistical tests were applied to examine the authenticity of the extracted data for multiple regression. Variance inflation factor (VIF) and correlation matrix were used to examine multicollinearity. Furthermore, Wooldridge test was applied to check autocorrelation, Modified Wald test was applied to check heteroscedasticity, and Hausman tests was applied for model selection between the random effect panel model and fixed effect panel model. However, it was assumed that data is normally distributed following the central limit theorem, which suggests that if the number of observations is more than 30 then their distribution is almost normal (Gravetter & Wallnau, 2016).

Pearson correlation matrix and VIF values (See Table 4) revealed that there is no issue/the absence of multicollinearity in the data. Moreover, the table also shows that VIF values are below 10 and correlation values for all the variables are less than 0.8 (Brooks, 2008).

Table 4

Pearson Correlation Matrix and VIF

	VIF	ROAA	Index	CpRato	OprExp	LiqRsk	CpInt
ROAA		1.000					
MSSP	1.44	0.329	1.000				
CpRato	5.09	-0.409	0.065	1.000			
OprExp	3.19	-0.627	0.066	0.739	1.000		
LiqRsk	2.32	-0.213	-0.283	0.520	-0.298	1.000	
CpInt	4.93	-0.681	-0.045	0.767	0.793	0.164	1.000

The results of Hausman test (probability= 0.000) suggested that fixed effect model is more suitable for the given data. However, the results of Modified Wald test (probability = 0.000) suggested that the issue of heteroscedasticity exists, which can be managed by applying the robust fixed effect model. Lastly, the results of Wooldridge test (probability = 0.749) indicated that no autocorrelation exists/the absence of autocorrelation in the given data.

Regression Analysis

Table 5 shows the results of regression analysis using the robust fixed effect model. The results indicate that the model is highly significant (probability=0.000) and explains 62.8% variation in ROAA. The positive relationship between *Maqasid al-Shariah* based social performance index and profitability is significant since *p*-value is below 0.05, indicating that improved *Maqasid al-Shariah* based social performance results in better profitability. The coefficient value of *Maqasid al-Shariah* based social performance index indicates that ROAA improves by 7.3% if *Maqasid al-Shariah* based social performance is increased by one unit. This finding supports the hypothesis of the current study. It is also consistent with the good management theory and social impact hypothesis, which suggest that superior social performance leads to better profitability. The results are also consistent with the findings of some earlier studies (Platonova et al., 2018).

The results also reveal a significant positive relationship of ROAA with capital ratio, as well as a negative relationship with operating expense and capital intensity. It indicates that financial performance improves with an increase in capital ratio but declines with an increase in operating expense and capital intensity. These results also comply with the findings of earlier studies (Platonova et al., 2018; Russo & Fouts, 1997). It proves that regression is a reliable equation. These findings suggest that Islamic banks should concentrate on improving their *Maqasid al-Shariah* based social performance. It will improve their public image as being 'Islamic' and allow them to differentiate themselves from their conventional counterparts. Moreover, it will also improve their financial performance resulting in creation of/increasing their shareholders' wealth.

Table 5

Panel Data Regression Analysis with Robust Fixed Effect Model

	Coefficient	T-Values	P-Values
MSSP	0.073	4.05	0.016**
CpRato	0.702	5.86	0.004***
OprExp	-0.445	-6.51	0.003***
LiqRsk	0.005	0.59	0.585
CpInt	-0.220	-2.71	0.054*
Constant	-0.022	-2.66	0.056*
Model Significance		12.52	0.000***
R^2			0.628

*Significant at 10%, **Significant at 5%, ***Significant at 1%
Dependent Variable: ROAA

Conclusion

The current study assessed the impact of *Maqasid al-Shariah* based social performance on the profitability of five full-fledged Islamic banks operating in Pakistan by analyzing unbalanced panel data for the period 2008-2018. After controlling for the variables capital ratio, operating expense, liquidity risk, and capital intensity, the study found a positive relationship between *Maqasid al-Shariah* based social performance and profitability, indicating that improved *Maqasid al-Shariah* based social performance results in better profitability. These results are consistent with the good management theory, social impact hypothesis, and the findings of earlier studies. Hence, it is recommended that Islamic banks should concentrate on improving their *Maqasid al-Shariah* based social performance.

Implications

Based on the findings of the current study, it is recommended that Islamic banks should concentrate on improving their *Maqasid al-Shariah* based social performance. It will improve their public image as being 'Islamic' and allow them to differentiate themselves from their conventional counterparts. It will also improve their financial performance resulting in creation of/increasing their shareholders' wealth.

Future Research Directions

The current study examined the relationship between *Maqasid al-Shariah* based social performance and financial performance using a small data set taken from five full-fledged Islamic banks. Future studies should explore the same relationship using a large data set, preferably including the data from the Islamic branches of conventional banks.

References

Adeneye, Y. B., & Ahmed, M. (2015). Corporate social responsibility and company performance. *Journal of Business Studies Quarterly, 7*(1), 151-166.

Ahmed, H. (2011). Maqasid al-Shari'ah and Islamic financial products: a framework for assessment. *ISRA International Journal of Islamic Finance, 3*(1), 149-160.

Arif, A., & Anees, A. N. (2012). Liquidity risk and performance of banking system. *Journal of Financial Regulation and Compliance*, *22*(2), 182-195. https://doi.org/10.1108/13581981211218342

Arshad, R., Othman, S., & Othman, R. (2012). Islamic corporate social responsibility, corporate reputation and performance. *International Journal of Economics and Management Engineering*, *6*(4), 643-647. https://doi.org/10.5281/zenodo.1074857

Ascarya, Rahmawati, S., & Sukmana, R. (2016). Measuring the Islamicity of Islamic banks in Indonesia and other countries based on Shariah objectives. *Paper presented at 11th Islamic Conference on Islamic Economics and Finance.* Kuala Lumpur, Malaysia.

Athanasoglou, P. P., Brissimis, S. N., & Delis, M. D. (2008). Bank-specific, industry-specific and macroeconomic determinants of bank profitability. *Journal of International Financial Markets, Institutions And Money*, *18*(2), 121-136. https://doi.org/10.1016/j.intfin.2006.07.001

Ayub, M. (2018). Maqasid realisation in Islamic finance: Components of framework for measurement index. *Journal of Islamic Business and Management, 8*(1), 1-9.

Bakar, M. A., & Mansoor, R. (2020). Form and Substance in Islamic Finance: from the Perspective of Islamic law of Contract. *Hazaraislamicus, 9*(02), 73-92.

Barnett, M. L., & Salomon, R. M. (2012). Does it pay to be really good? Addressing the shape of the relationship between social and financial performance. *Strategic Management Journal*, *33*(11), 1304-1320. https://doi.org/10.1002/smj.1980

Beck, C., Frost, G., & Jones, S. (2018). CSR disclosure and financial performance revisited: A cross-country analysis. *Australian Journal of Management*, *43*(4), 517-537. https://doi.org/10.1177/0312896218771438

Blasi, S., Caporin, M., & Fontini, F. (2018). A multidimensional analysis of the relationship between corporate social responsibility and firms' economic performance. *Ecological Economics*, *147*, 218-229. https://doi.org/10.1016/j.ecolecon.2018.01.014

Brooks, C. (2008). *RATS Handbook to accompany introductory econometrics for finance*. Cambridge Books.

Brower, J., & Dacin, P. A. (2020). An institutional theory approach to the evolution of the corporate social performance–corporate financial performance relationship. *Journal of Management Studies*, *57*(4), 805-836. https://onlinelibrary.wiley.com/doi/abs/10.1111/joms.12550

Capon, N., Farley, J. U., & Hoenig, S. (1990). Determinants of financial performance: a meta-analysis. *Management Science*, *36*(10), 1143-1159.

Chih, H.-H., & Chih, H.-L. (2014). Doing good with or without being known? Media coverage of corporate social performance and its impact on corporate financial performance. *Managerial Finance*, *40*(9), 883-902. https://doi.org/10.1108/MF-10-2013-0305

Cho, S. J., Chung, C. Y., & Young, J. (2019). Study on the Relationship between CSR and Financial Performance. *Sustainability, 11*(2), 343. **https://doi.org/10.3390/su11020343**

Dietrich, A., & Wanzenried, G. (2011). Determinants of bank profitability before and during the crisis: Evidence from Switzerland. *Journal of International Financial Markets, Institutions and Money*, *21*(3), 307-327.

Dusuki, A. W., & Abozaid, A. (2007). A critical appraisal on the challenges of realizing maqasid Al-Shariaah in Islamic banking and finance. *International Journal of Economics, Management and Accounting*, *15*(2), 143-165.

Elahi. (2011). The Objectives and Intents of Islamic Shari'ah As a Paradigm of Development Strategies and Policies. *IIUC Studies, 7*, 321-336 https://doi.org/10.3329/iiucs.v7i0.12496

Freeman, E. (1984). *Strategic management: A stakeholder approach*. Pittman-Ballinger, Boston.

Gravetter, F. J., & Wallnau, L. B. (2016). *Statistics for the behavioral sciences*. Cengage Learning.

Hamour, M., Shakil, M. H., Akinlaso, I. M., & Tasnia, M. (2019). Contemporary issues of form and substance: an Islamic law perspective. *ISRA International Journal of Islamic Finance*, *11*(1), 124-136. https://doi.org/10.1108/IJIF-01-2018-0006

Hanif, M. (2016). Economic substance or legal form: an evaluation of Islamic finance practice. *International Journal of Islamic and Middle Eastern Finance and Management, 9*(2), 277-295.

Iqbal, N., Ahmad, N., & Kanwal, M. (2013). Impact of corporate social responsibility on profitability of Islamic and conventional financial institutions. *Applied mathematics in Engineering, Management and Technology, 1*(2), 26-37.

Javed, M. M., Ayaz, M., & Kalim, R. (2020). Revisiting the Index to Measure Maqasid al-Shariah Oriented Performance of Islamic Banks: Evidence from Pakistan. *Journal of Islamic Business and Management*, *10*(1), 12-27.

Lahouel, B. B., Zaied, Y. B., Song, Y., & Yang, G.-l. (2021). Corporate social performance and financial performance relationship: A data envelopment analysis approach without explicit input. *Finance Research Letters, 39*, 101656. https://doi.org/10.1016/j.frl.2020.101656

Laldin, M. A., & Furqani, H. (2013). Developing Islamic finance in the framework of maqasid al-Shari'ah. *International Journal of Islamic and Middle Eastern Finance and Management*, *6*(4), 278-289. https://doi.org/10.1108/IMEFM-05-2013-0057

Lu, W., Chau, K., Wang, H., & Pan, W. (2014). A decade's debate on the nexus between corporate social and corporate financial performance: a critical review of empirical studies 2002–2011. *Journal of Cleaner Production*, *79*, 195-206. https://doi.org/10.1016/j.jclepro.2014.04.072

Martin, R., Yadiati, W., & Pratama, A. (2018). Corporate Social Responsibility Disclosure and Company Financial Performance: Do High and Low Profile Industry Moderate the Result? *Indonesian Journal of Sustainability Accounting and Management*, *2*(1), 15-24.

Miles, M. P., & Covin, J. G. (2000). Environmental marketing: A source of reputational, competitive, and financial advantage. *Journal of Business Ethics*, *23*(3), 299-311.

Mohammed, M. O., Razak, D. A., & Taib, F. M. (2008, June). The performance measures of Islamic banking based on the maqasid framework. In *Paper of IIUM International Accounting Conference* (INTAC IV) held at Putra Jaya Marroitt (pp. 1-17). http://irep.iium.edu.my/10121/

Mohammed, M. O., Tarique, K. M., & Islam, R. (2015). Measuring the performance of Islamic banks using maqāṣid-based model. *Intellectual Discourse*, *23*. 401-424.

Nguyen, N. (2018). The effect of corporate social responsibility disclosure on financial performance: Evidence from credit institutions in Vietnam. *Available at SSRN 3101658*. https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3101658

Pereira, A. F. A., Stocker, F., Mascena, K. M. C. d., & Boaventura, J. M. G. (2020). Corporate Social Performance and Financial Performance in Brazilian Companies: Analysis of the Influence of Disclosure. *BBR. Brazilian Business Review*, *17*, 540-558. https://doi.org/10.15728/bbr.2020.17.5.4

Platonova, E., Asutay, M., Dixon, R., & Mohammad, S. (2018). The impact of corporate social responsibility disclosure on financial performance: Evidence from the GCC Islamic banking sector. *Journal of Business Ethics*, *151*(2), 451-471. https://doi.org/10.1007/s10551-016-3229-0

Preston, L. E., & O'bannon, D. P. (1997). The corporate social-financial performance relationship: A typology and analysis. *Business & Society*, *36*(4), 419-429. https://doi.org/10.1177/000765039703600406

Qoyum, A. (2018). Maqasid Ash-Shari‘ah framework and the development of Islamic finance products: The case of Indonesia. *Tazkia Islamic Finance and Business Review*, *12*(2), 169-188. https://doi.org/10.30993/tifbr.v12i2.150

Rivera, J. M., Munoz, M. J., & Moneva, J. M. (2017). Revisiting the relationship between corporate stakeholder commitment and social and financial performance. *Sustainable Development*, *25*(6), 482-494. https://doi.org/10.1002/sd.1664

Russo, M. V., & Fouts, P. A. (1997). A resource-based perspective on corporate environmental performance and profitability. *Academy of management Journal*, *40*(3), 534-559.

Sekaran, U., & Bougie, R. (2019). *Research methods for business: A skill building approach*: john wiley & sons.

Sekhon, A. K., & Kathuria, L. M. (2019). Analyzing the impact of corporate social responsibility on corporate financial performance: evidence from top Indian firms. *Corporate Governance: The International Journal of Business in Society, 20(1),* 143-157. https://doi.org/10.1108/CG-04-2019-0135

Simpson, W. G., & Kohers, T. (2002). The link between corporate social and financial performance: Evidence from the banking industry. *Journal of Business Ethics, 35*(2), 97-109.

Sindhu, M. I., & Arif, M. (2017). The inter linkage of corporate reputation between corporate social responsibility and financial performance. *Pakistan Journal of Commerce and Social Sciences*, *11*(3), 898-910.

Wang, Dou, & Jia. (2016). A meta-analytic review of corporate social responsibility and corporate financial performance: The moderating effect of contextual factors. *Business & Society, 55*(8), 1083-1121.

Wang, H., Lu, W., Ye, M., Chau, K., & Zhang, X. (2016). The curvilinear relationship between corporate social performance and corporate financial performance: Evidence from the international construction industry. *Journal of Cleaner Production*, *137*, 1313-1322. https://doi.org/10.1007/s10551-011-0894-x

Wang, Y., & Berens, G. (2015). The impact of four types of corporate social performance on reputation and financial performance. *Journal of Business Ethics, 131*(2), 337-359.

Widarjono, A. (2018). Maqasid Sharia Index, Banking Risk and Performance Cases in Indonesian Islamic Banks. *Asian Economic and Financial Review*, *8*(9), 1175-1184.

Zaheer, S., & Rasool, W. (2017). Maq Asid Al-Shari ‘Ah Index for Islamic Banking Institutions. *Journal of Islamic Business and Management*, *7*(1), 28-38.