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How does Fintech effect profitability and risk of Islamic and Conventional banks in Pakistan

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ABSTRACT

In this thesis, the profitability and risk profile of Conventional and Islamic banks with the empirical effect of financial technology are investigated. The study isolates the uneven performance results across various institutional paradigms using a complete balanced panel dataset of scheduled Conventional and Islamic banks operating throughout the ten-year period from 2015 to 2024. The Non-Performing Loans (NPL) ratios serve as a proxy for bank risk and financial soundness, whereas for profitability, return on asset and return on equity ratios are used to quantify the financial performance of the banks. For bank specific unobserved heterogeneity, the methodology used in this is Hausman specification test, from which we can find out which model to prefer either random effect or fixed effect. The evidenced based results show that although the adoption of digital channels generally lowers long-term cost-to-income ratios, structural differences cause its overall impact on profitability and stability to diverge considerably. Conventional banks show rapid digital integration due to aggressive product scalability and profit maximization, which results in immediate profitability increases but increased vulnerability to operational and technology hazards. In contrast, Islamic banks exhibit a delay in the initial adoption of FinTech between 2015 and 2024 because of the complexity of product structuring and strict Shariah-compliance verifications. While Fintech adoption shows no significant baseline effect on credit risk for either banking models the interaction effect reveal a more nuanced picture for Islamic banks. ATM and Mobile banking adoption are associated with higher non performing loans ratios suggesting that the risk implications of digital adoption for the Islamic banks depends on the specific channel and require close monitoring rather than assuming uniform resilence. In addition to providing crucial strategic benchmarks for commercial bank executives and the regulator of banks, the State Bank of Pakistan (SBP) is navigating the digital banking transformation, this research makes a distinct contribution to the dual-banking research in emerging nations. For bank managers, legislators, and regulators looking to advance technological innovation while preserving efficient risk management and the financial stability within the banking sector, the findings provide insightful information.

Keywords: Islamic banking, Conventional banking, Fintech Adoption, Panel Data, Non Performing Loans, Credit Risk

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