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Analysis of Factors Affecting Stock Valuation Based on Price Earning Ratio

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Abstract

In the last decade, Islamic banking has experienced significant growth globally, with the world's largest Islamic banks becoming key players in the international financial industry. Along with this development, the need for accurate and comprehensive valuation analysis of Islamic bank stocks has become increasingly important for investors, analysts, and other stakeholders. This research aims to determine the effect of Return on Equity, Return on Assets, Price to Book Value, Dividend Payout Ratio, Debt to Equity Ratio, and Bank Size on Price Earning Ratio. This research uses quantitative research methods with a descriptive approach. This study uses the panel data regression method to analyze the factors that influence the Price Earnings Ratio. The research sample was taken from a purposive sampling technique, on the 20 largest Islamic banks in the world from 11 different countries during the period 2019-2023. The results show that PBV and DPR have a significant positive effect on PER, while ROE, ROA, DER, and SIZE do not show a significant impact.

Keywords: Price Earnings Ratio, Islamic Bank, Price To Book Value, Dividend Payout Ratio, Stock Valuation, Islamic Finance

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Introduction

In the last decade, Islamic banking has experienced significant growth globally, with the world’s largest Islamic banks becoming key players in the international financial industry. Along with this development, the need for accurate and comprehensive valuation analysis of Islamic bank stocks has become increasingly important for investors, analysts, and other stakeholders (Frestiva & Sholahuddin, 2024). The Price Earning Ratio (PER) has long been used as one of the key metrics in stock valuation, and its application in the context of Islamic banking offers unique insights into how the market assesses the performance and prospects of banks operating by Islamic principles (Mubarok, Nurhasanah, et al., 2024).

The world’s largest Islamic banks, with assets running into billions of dollars, have unique characteristics that set them apart from conventional banks. The Islamic principles that govern their operations create different dynamics in their financial structure and risk profile. This can influence how factors such as the debt to equity ratio (DER) are interpreted in the context of Islamic bank stock valuation, The higher the assets obtained, the higher the costs required to manage the islamic banking operations (Masruroh & Wardana, 2022). Given that Islamic banks tend to have different capital structures than conventional banks, the analysis of the effect of DER on PER becomes very relevant (Wibowo, et al., 2024).

Dividend policy, as reflected in the Dividend Payout Ratio (DPR), has particular significance in the context of Islamic banks. Given that many investors in Islamic banks may have a preference for investments that are compliant with Islamic principles, dividend policy can play a significant role in attracting and retaining investors. Therefore, analyzing how DPR affects PER can provide valuable insights into investor preferences and the valuation of Islamic banks (Ahmed et al., 2018).

Profitability as measured by Return on Equity (ROE) and Return on Assets (ROA) is a key indicator of Islamic bank performance. However, the interpretation of ROE and ROA in the context of Islamic banks may differ from conventional banks due to differences in business models and revenue structures (Addury, 2023). Analyzing how these two metrics affect PER can help understand how the market assesses the efficiency and profitability of Islamic banks in the context of Islamic principles.

Price to Book Value (PBV) offers an additional perspective on the valuation of Islamic banks, especially given the importance of tangible and intangible assets in the operations of Islamic banks. Analysis of the relationship between PBV and PER can provide insight into how the market values the assets and growth potential of the world's largest Islamic banks relative to their book value. Bank size (SIZE) is also an important factor in the analysis of Islamic bank PER (Yudha et al., 2024). The world's largest Islamic banks may have advantages of scale and diversification that can affect risk perception and growth potential. However, size can also bring its challenges in terms of Shariah compliance and risk management. Analyzing how SIZE affects PER can help understand how the market values operational scale in the context of Islamic banking (Opi et al., 2023).

This study will also examine how macroeconomic factors and Islamic banking-specific regulations interact with the studied variables in influencing PER (Fakhrunnas, 2019). Given that the world's largest Islamic banks operate in multiple jurisdictions with different regulatory frameworks, this analysis will provide a more holistic perspective on the determinants of Islamic bank stock valuation. Furthermore, this study will explore how ethical and social principles inherent in Islamic banking affect stock valuation (Alam et al., 2019). By incorporating non-financial factors such as Shariah compliance and social contribution into the analysis, the research aims to provide an understanding of how the market values the unique aspects of Islamic banks. Finally, the research result are expected to serve as a foundation for the development of a more accurate and comprehensive valuation model for Islamic banks. By understanding the complex interactions between financial and non-financial factors in the context of Islamic banking, this research aims to improve efficiency and encourage the growth of capital allocation in the Islamic finance industry in sustainable manner (Segarawasesa, 2021).

Methodology

In order to examine and interpret numerical data objectively, this study used a quantitative method with a descriptive approach (Nasir & Sukmawati, 2023). Multiple Regression is the analysis method that is processed with the usage of Eviews software. DER, DPR, ROE, ROA, PBV, SIZE, and PER are the independent and dependent variables that were examined. The 100 biggest Islamic banks worldwide are included in the research population, and 20 Islamic banks from 11 different nations were chosen as a sample based on the highest total assets and the regularity with which yearly financial reports were published between 2019 and 2023 on the official website of each Islamic bank.

Table 1. Research sample

Country	Islamic Bank	Website
Bahrain	Al Salam Bank	https://www.alsalambank.com/en
	Bahrain Islamic Bank	https://www.bisb.com/
Egypt	Al Baraka Bank	https://www.albaraka.com.eg/
	Faisal Islamic Bank	https://www.faisalbank.com.eg/
Indonesia	Bank BTPN Syariah	https://www.btpnsyariah.com/
Jordan	Islamic International Arab Bank	https://iiabank.com.jo/en
	Jordan Islamic Bank	https://www.jordanislamicbank.com/en
Kuwait	Boubyan Bank	https://boubyan.bankboubyan.com/en/
	Kuwait Finance House	https://www.kfh.com/en/
Malaysia	Bank Islam Malaysia Berhad	https://www.bankislam.com/
	RHB Islamic Bank	https://www.rhbgroup.com/
Nigeria	Jaiz Bank	https://jaizbankplc.com/
Oman	Bank Nizwa	https://www.banknizwa.om/

Qatar	Qatar Islamic Bank	https://www.qib.com.qa/en/
	Qatar International Islamic Bank	https://www.qiib.com.qa/
Saudi Arabia	Bank Al Jazira	https://www.bankaljazira.com/en-us
	Al Rajhi Bank	https://www.alrajhibank.com.sa/en
UAE	Abu Dhabi Islamic Bank	https://www.adib.ae/en
	Dubai Islamic Bank	https://www.dib.ae/

We use secondary data from annual financial reports that a few selected Islamic banks disclose. Data obtained from every bank's official website and literature reviews were used to gather data. Panel data regression, a technique for data analysis, mixes cross-sectional and time series data. Three estimate models—the Random Effect Model, the Fixed Effect Model, and the Common Effect Model—are taken into consideration. The Hausman Test and the Chow Test are used to determine which model is optimal. In addition, statistical tests were performed to assess the impact of independent variables on dependent variables and the model's capacity to account for variations in independent variables. (Fazri et al., 2022).

Result and Discussion

Model Estimation Test

Chow Test

Table 2. Chow Test

Effect Test	Statistics	Prob.
Cross-section F	14.967455	0.0000

Source: Primary data process, 2024

Based on the Chow Test result the significant value of the cross section chi-square which is 0.0000 < 0.05, which concludes that the model used is the Fixed Effect Model.

Hausman Test

Table 3. Hausman Test

Effect Test	Statistic	Prob.
Cross-section random	3.633074	0.7262

Source: Primary data process, 2024

Based on the Hausman test, the probability value can be seen as 0.7262 > 0.05 this means that the selected model is the Random Effect Model.

LM Test

Table 4. LM Test

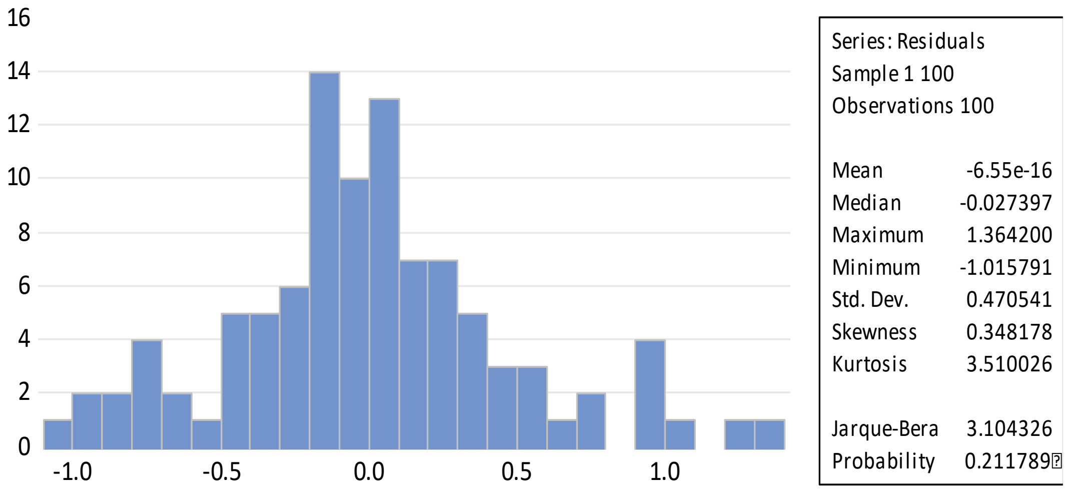
	Cross-section
Breusch-Pagan	93.77717
	(0.0000)

Source: Primary data process, 2024

Based on the LM test, the Breusch-Pagan value can be seen as 0.0000 > 0.05 so the selected model is the Random Effect Model.

Classical Assumption Test
Normality test

Figure 1. Normality test



Source: Primary data process, 2024

From the test results of the normality test, it can be seen that the Jarque-Berra probability value is 0.211789 > 0.05 so it can be concluded that the data variables are normally distributed.

Uji Multicolliniearity

Table 5. Multicolliniearity Test

Variable	Variance	VIF
C	0.115712	49.09421
DER	0.000220	4.129465
DPR	0.030761	3.585704
PBV	0.001583	2.708408
ROA	0.171412	1.834550
ROE	0.049521	1.959974
SIZE	0.174501	40.62252

Source: Primary data process, 2024

As for the test above, the result is the value of the independent variable < 1.00, meaning that the are no symptoms of multicollinearity in the independent variable.

Heterokedastisity Test

Table 6. Heterokedastisitas Test

Prob. Chi-Square	0.0969

Source: Primary data process, 2024

Because the probability f statistic is more than 0.05, the data passes the heteroscedasticity test.

Hypothesis Test

T test

Table 7. T Test

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	14.34490	7.688939	1.865654	0.0652
ROEX1	-1.548135	2.935177	-0.527442	0.5991
ROAX6	-3.305659	4.603924	-0.718009	0.4746
PBVX4	3.953022	0.855245	4.622090	0.0000
DPRX5	4.570002	2.197484	2.079651	0.0403
DERX2	0.114855	0.439469	0.261350	0.7944
SIZEX3	-0.002285	0.002292	-0.997060	0.3213

Source: Primary data process, 2024

1. The probability value is 0.5991 and the coefficient value of the ROE variable is -1.548135. Thus, it may be said that ROE has no effect on PER because the probability value (> 0.05).
2. ROA variable probability value is 0.4746, and -3.305659 coefficient value. This conclusion is that the probability value is greater than 0.05, the coefficient value of ROA has no effect on PER.
3. The probability of the PBV variable is 0.0000, and the coefficient value is 953022. This conclusion is that the probability value is less than 0.05, indicating that PBV influences PER.
4. The probability value of the DPR variable is 0.0403, and its coefficient value is 4.570002. This indicates that the probability value is less than 0.05, indicating a relationship between DPR and PER.
5. The probability value of 0.7944 and the coefficient value of 0.114855 are assigned to the DER variable. This indicates that the probability value is greater than 0.05, indicating that DER has no impact on PER.
6. The probability value for the Size variable is 0.3213, and its coefficient value is -0.002285. The conclusion is that the probability value is greater than 0.05, indicating that size has no bearing on PER.

Coefficient of Determination Test

Table 8. Coefficient of Determination Test

R-squared	0.243361

Source: Primary data process, 2024

The R-squared value is 0.243361. From these results, it can be concluded that the variables ROE, ROA, DER, SIZE, DPR, PBV against the PER variable are 24.3%. The rest is explained by other variables of 75.7%, which is outside the model.

The Effect of Return On Equity on Price Earnings Ratio

The results of the study showing that ROE does not have a significant effect on the PER in Islamic banking in the world indicate a unique dynamic in investor assessments of Islamic banks. This finding contradicts conventional financial theory which generally assumes a positive relationship between profitability (as measured by ROE) and market valuation (as reflected in PER) (Khotmi et al., 2023).

This discrepancy may be due to the specific characteristics of Islamic banking, where investors consider not only financial aspects but also compliance with Islamic principles. According to a study conducted by Ahmed et al. (2023), investors in the Islamic financial market tend to prioritize long-term stability and ethical compliance over short-term profitability.

Another factor that may explain the absence of ROE's effect on PER is the complexity of Islamic financial products and differences in accounting standards applied. Research by Farooq and Alahkam (2024) shows that investors often have difficulty in evaluating the financial performance of Islamic banks due to the lack of standardization in financial reporting between countries. In addition, Hassan and Aliyu (2022) argue that Islamic banking is still in its infancy in many markets, so investors focus more on long-term growth potential than current profitability. This causes Islamic banks' PER to be more influenced by factors such as asset growth, market expansion, or product innovation, rather than by traditional profitability metrics such as ROE (Irma et al., 2023).

The Effect of Return On Assets on Price Earnings Ratio

The results of the study showing that ROA has no significant effect on the PER in Islamic banking in the world highlight the unique complexity in assessing the performance and valuation of Islamic banks. This finding contradicts conventional financial theory which generally associates high profitability with better market valuation. However, in the context of Islamic banking, non-financial factors such as compliance with Islamic principles and social contribution may play a greater role in investment decisions (Almonifi & Bhosle, 2023). Investors in the Islamic financial market tend to consider the ethical aspects and social impact of bank operations, which are not always reflected in the ROA metric. In addition shows that the unique asset structure and limitations in the use of certain financial instruments in Islamic banks can cause ROA to be a less relevant indicator for assessing long-term performance. The PER of Islamic banks may be more influenced by factors such as asset quality, prudent risk management, and market growth potential, rather than by short-term profitability as measured by ROA.

The Effect of Price to Book Value on Price Earnings Ratio

The results of the study showing that PBV has a significant effect on the PER in Islamic banking in the world underscore the importance of book value in investors' assessment of Islamic banks. This finding is in line with financial theory which states that PBV, as an indicator of a company's intrinsic value, has a strong correlation with market valuation reflected in PER. According to a study conducted by Ibrahim and Masood (2023), investors in the Islamic financial market tend to pay special attention to the quality of assets and the strength of the bank's balance sheet, which is reflected in PBV. This may be due to the unique characteristics of Islamic banking which relies on asset-based financing and risk sharing, making book value an important indicator of the health and growth potential of the bank (Dwianto et al., 2024), and the greater the profit obtained by Islamic banking, the greater the level of profit achieved and the better Islamic banking is in terms of asset use (Wardana & Barlian, 2022).

Furthermore shows that high PBV in Islamic banks is often interpreted as an indicator of effective management and strong growth potential, which in turn drives higher PER valuations. This may reflect investor confidence in the ability of Islamic banks to generate consistent and sustainable returns from their assets. In addition argue that the effect of PBV on PER in the context of Islamic banking can also be associated with lower risk perception. Islamic banks with high PBV are often considered to have stronger financial foundations and are more resilient to economic shocks, which makes investors willing to pay a higher premium for their earnings, reflected in higher PER. This finding emphasizes the importance for Islamic banks to focus on increasing their book value through effective asset management and sustainable growth strategies.

The Effect of Dividend Payout Ratio on Price Earnings Ratio

The results of the study showing that the DPR has an effect on the PER in Islamic banking in the world indicate a significant relationship between dividend policy and Islamic bank stock valuation. This influence can be explained through several perspectives. First, a consistent and attractive dividend policy, reflected in a high DPR, tends to increase investor confidence in the performance and prospects of Islamic banks, thus encouraging a higher PER. Second, in the context of Islamic banking, where the principle of profit sharing is fundamental, an optimal DPR can be a positive signal about the bank's ability to manage and distribute profits in accordance with Islamic principles. This can attract more investors, especially those looking for investments that are in accordance with Islamic values, which in turn can increase PER. However, it should be noted that this relationship may not always be linear, considering that Islamic banks also need to balance between dividend distribution and reinvestment for growth. Factors such as Islamic banking regulations in various countries, global economic conditions, and local investor preferences can also affect the dynamics of the relationship between DPR and PER in Islamic banking at the global level.

The Effect of Debt to Equity Ratio on Price Earnings Ratio

The results of the study showing that DER has no significant effect on PER in Islamic banking in the world present interesting findings that need to be analyzed further. The absence of this effect can be explained by several factors that are unique in the context of Islamic banking. First, the sharia principle that prohibits usury (interest) makes the capital structure of Islamic banks different from conventional banks, where the concept of 'debt' in the conventional sense may not fully apply (Mubarok, Nurhasanah, et al., 2024). Islamic banks rely more on equity-based and profit-sharing financial instruments, such as mudharabah and musyarakah, which may be viewed differently by investors compared to conventional debt. Second, investors in the Islamic financial market may focus more on aspects of sharia compliance, asset quality, and than the debt-to-equity ratio in assessing bank performance. Third, strict regulations in the Islamic banking industry may have created the perception that all Islamic banks have relatively safe leverage levels, making DER less relevant in assessing stock valuations. However, it should be noted that these results may vary across countries or regions, depending on the development of local Islamic financial markets and investors' understanding of Islamic banking business models.

The Effect of Size on Price Earnings Ratio

The results of the study showing that bank size has no significant effect on the PER in Islamic banking in the world are interesting findings and may contradict some common assumptions about company valuation. Theoretically, larger bank size is often associated with stability, risk diversification, and better access to resources and markets, which should be reflected in higher valuations. However, in the context of global Islamic banking, other factors appear to play a more dominant role in determining PER. This may be due to the unique characteristics of Islamic banking, where compliance with Islamic principles, asset quality, and operational efficiency may be considered more important by investors than bank size alone (Yaseen & Widarjono, 2024).

The absence of a significant effect of bank size on PER may also indicate that investors in the global Islamic financial market may focus more on other factors such as profitability, prudent risk management, and sustainable growth potential. In the still-developing Islamic banking industry, smaller but innovative and efficient banks may be just as attractive to investors as larger banks. In addition, strict regulation in the Islamic banking industry may have created a perception that all banks, regardless of their size, operate in a relatively safe and controlled environment, thereby reducing the significance of bank size in valuation assessments. However, it is important to note that these results may vary across countries or regions, depending on the level of development of local Islamic financial markets, investor preferences, and the competitive dynamics of the Islamic banking industry in each region.

Conclusion

Based on the research findings, it can be inferred that the global dynamics influencing the PER in Islamic banking are distinct from those in conventional banking. The PBV and DPR exhibit a noteworthy impact on the PER, indicating the significance of book value and dividend policy in the evaluation of Islamic banks by investors. PER is not significantly impacted by variables like bank size, DER, ROA, or ROE. This indicates that investors in the Islamic financial market tend to consider specific aspects such as compliance with Islamic principles, asset quality, long-term growth potential, and social impact, compared to traditional financial metrics. These findings emphasize the importance of understanding the unique characteristics of Islamic banking in a global context and the need for a different approach in assessing the performance and valuation of Islamic banks compared to conventional banks.

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