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Competition-stability relationship in dual banking systems: evidence from efficiency-adjusted market power

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Abstract:

This research attempts to explore the impact of banking competition on financial stability employing a more precise measure of market power. It was found that Islamic banks are less stable and are enjoying lower market power. The analysis shows that higher market competition makes the banking sector vulnerable to defaults, supporting the "competition-fragility view". This research finds no difference in the relationship for Islamic banks indicates that Islamic banks might be involved in traditional banking activities as conventional banks. The results are consistent and robust to different estimation approaches and subsamples. This research carries regulatory and policy implications.