RELATIONSHIP BETWEEN NON-PERFORMING LOANS (NPLs) AND MACROECONOMICS VARIABLES

FARIDAHTUL HAZIMAH BINTI FAZOLI
2008404208

Submitted in Partial Fulfillment of the Requirement for the Bachelor of Business Administration (Hons) Finance

FACULTY OF BUSINESS MANAGEMENT
UNIVERSITI TEKNOLOGI MARA
MELAKA

APRIL 2011

ACKNOWLEDGEMENT

IN THE NAME OF ALLAH S.W.T. THE MOST GRACIOUS AND THE MOST MERCIFUL

All praises to almighty ALLAH, the most merciful and the most benevolent for giving me the opportunities in completing this research paper. It would be impossible for me to spent time to complete this study without the grace and help of ALLAH S.W.T.

I am greatly indebted to Encik Amirudin bin Mohd Nor, whose excellence in supervision and plays a big role in inspired my work. Without his untiring encouragement, suggestions, ideas and comments throughout this study, this research could not be completed.

I also would like to convey my deepest gratitude and indebted to all librarian of Universitiy Teknologi MARA, Johor Campus for their co-operation and help throughout the duration of this research especially during find data on data stream.

I dedicate this research to my beloved parents and for their endless support and understanding and also to the rest of my families for their help and

TABLE OF CONTENTS

ABSTRACT

Non-Performing Loans (NPLs) can be defined as defaulted loan in which banks are unable to form profit. Usually loans falls due if no interest has been paid in 90 days. This will reduce the bank's profit if customer did not pay the interest. But, there are few ways for customer if they cannot pay the interest, such as reschedule their loans. The purpose of this study is to analyze the relationship between the NPLs with interest rate, inflation rate and unemployment rate. There is an significant and insignificant relationship between interest rate, inflation rate and unemployment rate with NPLs. This research is appertained with commercial banks in Malaysia.

Data were collected from secondary data which published by Bank Negara Malaysia from February 2006 - December 2010 in monthly. The technique used is single linear regression method to see the relationship between dependent and independent variables. Non-Performing Loans (NPLs) will be used as dependent variables and interest rate (INT), inflation rate (INF) and unemployment rate (UNP) will be used as independent variables.

CHAPTER 1

INTRODUCTION

As introduction, this chapter will briefly explain the history, background, problem statement, research questions, research objectives, significance, scope, limitation and also definition of term in the overall study.

1.0 HISTORY OF BANKING SYSTEM

Financial crises became a serious threat for the world economy especially after the financial deregulation process of the 1980s. This process and increased competition affected banking system safety and soundness therefore banking system vulnerability increased during last decades. It is agreed that a stable macroeconomic environment is not sufficient for achieving high and sustained growth, macroeconomic stability needs to be complemented and strengthened by the development of a strong financial sector. The relationship between financial sector and real sector makes the intermediation efficiency, the indicator of capital accumulation and productive efficiency.

Therefore the stability of financial system is very important to economic growth. After the banking deregulation process in 1980's, international over-borrowing syndrome became an important threat for the banking systems of developing countries. In this process, the banking sectors in developing countries faced with the default risk because of inefficient portfolios, specifically, in terms of international funds. Over-borrowing problem follows a cyclical pattern in the recovery phase of business cycle. Increased demand leads prices to rise and attracts new investment. In a feedback relationship the new investments stimulates income.