FACTORS INFLUENCING PERFORMANCE OF HOUSING LOAN IN MALAYSIAN COMMERCIAL BANKS

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ABSTRACT

This paper empirically investigates the factors that influencing the performance of housing loan in Malaysian commercial bank industry. The commercial banks, as part of financial institution in Malaysia have played an important role in order to improve as well as to expand the housing loan industry in Malaysia banking sector. However, the successful and the performance of the housing loan industry of that institution depend on several factors. The data for this study will be collected for 36 months started from January 2006 until December 2008. The data from all 22 commercial banks were aggregated and combined in order to acquire the total performance of the housing loan product in that particular industry. In order to see the correlation between the dependent and independent variables, we will apply Multiple Linear Regression method. The performance of housing loan will be measured in terms of monthly disbursement volume. The independent variables are; interest rate, repayment and supply. The findings indicate that the three variables show significantly related with the housing loan performance.

Keywords: performance, housing loans, commercial banks, interest rate, repayment, supply

INTRODUCTION

As a part of player in financial system in Malaysia, commercial banks have played a vital role in order to improve as well as expanding the housing loan industry in Malaysian banking sector. The successful and the performance of the housing loan industry depend on several factors. The aims to create a well-functioning housing markets and the expansion of a safe and sound housing loan system is not a simple thing. This study was conducted to investigate the factors that may influence the performance of housing loan in Malaysian commercial banks.

Since its infancy for about 30 years ago, the property development industry in Malaysia has progressed and developed into a modern and advanced sector of the economy. Over the years, housing programmes have focused on the eradication of poverty and restructuring of our society through promoting the integration of the various ethnic communities in Malaysia. Until the early 1970s, building societies have become the biggest providers of housing finance. The commercial bank became the major player in the origination market in the 1990s.

Houses are expensive. Consequently, the availability and cost of house financing are critical determinant of how well housing market function in Malaysia. Changes in house finance mechanisms are drivers in explaining the dramatic changes in housing market and housing activity seen in industrialized countries in recent years (Green & Watcher, 2007). This study focuses on industry-based unit of analysis. It is because the area of study covers the housing loan provided by twenty two commercial banks in Malaysia banking industry. The data were aggregated and combined in order to see the performance of the housing loan product in that industry.

LITERATURE REVIEW

According to Lacoviello & Minetti (2007), one of the aspects that can affect the performance of the housing finance system is the efficiency. Several aspects, in particularly, are also relevant for the measure of the performance such as the depth of the funding system for housing finance institutions, the presence of a diversified range of mortgage lenders and sharing of credit risk. Case *et al* (2005) found that the efficiency and performance of housing finance system is the result of the historical evolution of the system and the regulatory constraints. After tight money, a regulatory ceiling on deposit rates can prevent banks from offsetting the drain in deposits by increasing the return paid to depositors. Diamond (2000) mentioned in his research, if there are no commercial banks offering housing loans, it may be because there are implicit or explicit restrictions or distortions affecting the activity.

Diamond (2000) found that if effective real rate of interest is well over 10%, it becomes distinctly unappetizing to borrow long term. In the research also proposed that the other causes of diminished demand for home loan may include the presence of large remittance flows or large home equities. Brick & Palia (2003) stated that the performance of loan has no significant correlation with loanôs interest rate. Meanwhile, they found that fees are positively related to fixed rate loans. It suggests that fess and loan interest rates are complementing each other. Petersen & Rajan (1995) found that the loan interest rate is related to macroeconomic variables such as the prime rate, the term structure and the default premium. Berger & Udell (1995) found that the borrowers with higher liquidity have a lower loan interest rate. There were no significant relationship being found between the loan interest rate and borrowerôs debt levels and the borrowerôs profitability. Diamond (2000) stated that the higher the default premium in the economy, the higher the loan interest rate. The study also found no significant relationship between the loanôs maturity and loan interest rates. According to Zhao & Moser (2005), loan charge has a negative association with loan growth.

As reported by Lapenu & Zeller (2001), if weighted by loan volume, the repayments rates for the larger financial institutions are better than smaller financial institution. Their study suggests that the disciplining of borrowers to repay loan is strongly dependent on the existence of an institutionalized information-sharing mechanism. Order et al (2007) suggest that when the default is higher, the performance is worse. According to Silwal (2003), there is a need to put careful analysis and thought into repayment rates because they are used expensively as the evidence of the purported success of the financial institutions. Meanwhile, the evidence from Rosenberg (1999) suggest that peer selection, peer monitoring , dynamic incentives and regular repayment schedules will all ensure that clients of the organizations will repay their loans on time.

Diamond (2000) mentioned that not all the commercial banking sectors are well functioning enough to support a minimal amount of housing lending. He found; if housing finance is a high enough priority, a special circuit can be created. Nier & Zicchino (2007) found that the demand for loan being weaker in periods of weak economic growth. The significant question is whether loan supply is pro cyclical; bank unwilling or unable to provide loans in periods of weak economic growth. It seems that the fluctuation in bank loan supply have the potential to amplify the macro-economic situations.

METHODOLOGY

In order to obtain the reliability in the finding, manner of data gathering is important. This is significant for the purpose of analysis, testing of hypotheses and answering the research questions. The aim of this study is to collect data in Malaysia which is related to the housing loan product in commercials banks. The data was collected from Monthly Statistical Bulletin (MSB) from January 2006 until December 2008 which is available at the Knowledge Management Centre of Bank Negara Malaysia (BNM).

Initially, the population number for this study is 39 nine commercial banks in Malaysia. In addition, this study will use non-probability sampling. To secure an acceptable result, this study decided to use 22 samples out of 39 numbers of commercial banks that being listed by Bank Negara Malaysia as at December 2008.

The decision to use conventional banks as sample was due to the availability of data. Another reason due to the differences of banking transaction and sources of fund for both conventional Islamic banks. The sources for both types of banking may not be combined since the Islamic bank must comply with Syariah. The data for all variables gathered for 36 months. The collection started from January 2006 until December 2008.

The dependent variable for this study is the performance of housing loan in Malaysian commercial banks, where the performance was measured in terms of volume of disbursement every month. In this study also there are three independent variables being measured; interest rate, repayment and supply. Interest rate proxy in term of monthly Average Lending Rate (ALR). Repayment proxy in term of monthly repayment. Supply proxy in term of monthly loan repayment.

In order to examine the simultaneous effects between the independents and dependents, we use the multiple linear regressions. The model develop are as below :

Y = Ŭ+ ɓ1x1 + ɓ2x2 + ɓ3x3 + ‘

Equation 1

Where ;

Y = dependent variables represent the performance of housing loan
Ŭ = constant number of equation
ɓ = coefficient of beta value
X1 = independent variable which represent interest rate
X2 = independent variable which represent repayment
X3 = independent variable which represent supply
ɭ = error term

HYPOTHESES STATEMENT

In order to test whether the variables may significantly affect the performance of housing loan, we construct the hypotheses as below;

Hypotheses 1

H_0 : There is no significant relationship between interest rate and the performance of housing loan in Malaysia

H_a : There is a significant relationship between interest rate and the performance of housing loan in Malaysia

Hypotheses 2
H_0 : There is no significant relationship between repayment and the performance of housing loan in Malaysia
H_a : There is a significant relationship between repayment and the performance of housing loan in Malaysia

Hypotheses 3
H_0 : There is no significant relationship between supply and the performance of housing loan in Malaysia
H_a : There is a significant relationship between supply and the performance of housing loan in Malaysia

FINDINGS AND ANALYSIS

The objective of this study is to investigate the relationship between the independent variables (interest rate, repayment and supply (loan provision)) and dependent variables. Table 1 was constructed to indicate the relationship between the three independent variables and the housing loan performance for commercial banks in Malaysia.

Independent variables	**Coefficient**	**p-value**
Interest rate	-0.334	0.034
Repayment	0.544	0.009
Supply	0.227	0.016
R-Square	***0.882***	

Table 1 : Multiple linear regression result

By observing the result between the performance of housing loan and the interest rate it shows statistically significant since the coefficient having p-value less than 5 percent. Therefore our study rejects the null hypotheses. The result also suggests that a negative relationship between housing loan performance and the interest rate. This findings was consistent with Zhao & Moser (2005), they also found loan charge has negative relationship with the loan performance. However, our result contrasts with Brick & Palia (2005). They found the performance of loan has no significant correlation with the interest rate.

Repayment variables also show a significant result. Our study is able to reject the null hypotheses. Besides that, our study indicates that there is a positive relationship between the repayment and the housing loan performance. As the amount of repayment increase, the performance of housing loan will also increase. On the other hand, we also found there is significant relationship between supply (loan provision) with the performance of housing loan. This finding also rejects the null hypotheses. The sign of the coefficient suggest that the supply and the housing loan performance positively related. We also found our result consistent with Order et al (2007). According to them, the performance of loan increase by higher repayment rate. We may suggest that, a good repayment is necessary to be sustainable.

As the supply (loan provision) increased, the performance of housing loan will also increase. The R-square resulted from the analysis is 0.882. The variables being used in developing the model as in equation 1 has the variation of 88.2 percent. It suggests that, the variables used able to explain the model very well. R-square is an overall measure of the strength of association and it does not reflect the extent to which any particular independent variables associate with the dependent variable. Our findings were supported by Sharpe & Acharya (1992). The study found that there is a positive association between the bank supplies of fund with the performance of loan.

Based on the result gathered from the analysis, we found that all three independent variables have statistically correlated with the performance of housing loan. We may suggest that the three variables may consider as the factors that contribute to the performance of the housing loans. The determinants factors of the performance come from side, bank and borrowers. The commercial bank had been seen able to increase the monthly loan provision as the bank has strong fund position.

Although the findings indicate that all three independent variables influence the performance of housing loan, we recommend and would like to suggest other researcher to identify other significant factors.

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