FACTORS AFFECTING NET INTEREST MARGIN OF COMMERCIAL BANKS IN MALAYSIA

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MASTER OF SCIENCE (BANKING)
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FACTORS AFFECTING NET INTEREST MARGIN OF COMMERCIAL BANKS IN MALAYSIA

By

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A Dissertation Submitted in Partial Fulfillment of the Requirements for the Degree of Master of Science (Banking) at the Othman Yeop Abdullah Graduate School of Business, Universiti Utara Malaysia

June 2012
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ABSTRAK


Kajian mendapati bahawa kesemua bank yang dipilih ini mempunyai kekuatan dan keupayaan dari segi aset tetap, pusingan modal yang tinggi, deposit kewangan yang kukuh serta keuntungan yang tinggi. Walaubagaimanapun, kewujudan bank perdagangan asing turut memberi persaingan sengit kepada bank tempatan dari segi perkhidmatan yang berkualiti dengan kos yang lebih rendah yang dipengaruhi oleh faktor-faktor dalaman dan luaran lain.

Kaji selidiki menggunakan sejumlah 10 nisbah kewangan iaitu nisbah keuntungan, nisbah kualiti aset, saiz firma, Margin keuntungan bersih, leveraj, nisbah kecairan, nisbah pertumbuhan pinjaman, nisbah pasaran, nisbah industri, kadar inflasi serta kadar faedah bank. Analisa regresi pelbagai (multiple regression analysis) pula telah digunakan untuk mengenalpasti penentu-penentu yang mempengaruhi 'net interest margin' bank-bank tempatan ini. Kedua, mengkaji jenis-jenis risiko yang signifikan ke atas 'net interest margin' dan akhir sekali mengenalpasti kesan-kesannya (faktor luaran dan dalaman).

Hasil kaji selidik ini mendapati bahawa; pertama 'net interest margin' selain dari dipengaruhi oleh persaingan pasaran ia juga dipengaruhi oleh kesan faktor-faktor lain, keduanya adalah secara rasional mempertimbangkan kos-kos seperti kos operasi, kos modal, nisbah jumlah pinjaman berbanding jumlah aset, nisbah pinjaman tidak berbayar serta peluang kos simpanan. Ketiga, saiz aset bank-bank berkenaan juga kualiti pengurusan yang sederhana dan keempat pendedahan risiko credit yang besar juga menpengaruhi 'net interest margin'. 

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ABSTRACT

The purpose of this study is to analyze and compare the performance determinants of one commercial bank with other commercial banks operating in Malaysia for the period of 5 years from 2006 to 2010. There are 6 commercial banks selected in this study namely Maybank, CIMB Bank, Public Bank, RHB Bank, Hong Leong Bank dan Affin Bank. All of these banks are local commercial banks.

We found that all selected banks have their own strengths and capability in fixed asset, strong capital, large deposit size and also high profitability. However, existing foreign banks give a healthy competitions to local banks in terms of quality service with low cost banking services for customers. The competition makes it more relevant for domestic banks to focus on their performance predictors in this case net interest margin.

In this study, there are 10 financial ratios selected namely, profitability ratio, Asset Quality Ratio, Size, Net Interest Margin, Leverage, Liquidity Ratio, Loan Growth Ratio, Market ratio in industry, Inflation rate and also bank interest rate. To identify the determinants influencing net interest margin of commercial bank, this study has chosen multiple regression analysis. Secondly, this study also the effects of credit risk on net interest margin.

The results of the study reveal the following findings. Firstly, in addition to the degree of market competition that narrows the interest margin, the study shows other factors which significantly affect the interest margin of commercial banks in Malaysia namely capital intensity investment and inflation rate whereby both factors are significant and positively influenced net interest margin.
ACKNOWLEDGEMENTS

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A very grateful to Allah S.W.T with all His guidance and blessing finally I have completed my paper as a dissertation to obtain my Master of Science Degree in Banking. Special thanks to my dear supervisor Prof. Dr Nor Hayati Ahmad for all her guidance, understanding, attention, kindness and encouragement. Her supervision, ideas, guidance, critics and examination of the thesis have been an enormous help. Words alone cannot express my greatest appreciation and gratitude to her. I am very grateful from her not only for her assistance, but also she is a great person as a human being. I will not forget such kind people like her. Not forgotten to my beloved examiner, Assoc Prof Norafifah Ahmad for her kind support.

A great acknowledgement to my beloved husband, Encik Ahmad Faizal Abd Rahim, my son Muhammad Ikmal Farhan and my daughter, Nur Dania Sara. Not forgotten to my beloved parents, Hjh Siti Aishah, Zainol Abidin, Norihan and Abd Rahim for all the support and "Doa", love and understanding showered to me. And for my CIMB Jalan Kampung Baru Branch Manager, Pn Sarini Suzaini Ibrahim, thank you for your strong support and I am very grateful to have a manager like you. I would like to express my sincere appreciation to all my lecturers of College of Business, especially lecturers of Finance and Banking Department. Lastly sweet thanks too to all my coursemates, Zuraida, Rosilawati and Rosmariniwati who directly or indirectly helped me to complete this thesis. May ALLAH bless all of you. Finally, I hope this study could add a new knowledge and get better understanding on the topic discussed.
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<td>BNM</td>
<td>Bank Negara Malaysia</td>
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<tr>
<td>NIM</td>
<td>Net Interest Margin</td>
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<td>ROA</td>
<td>Return On Asset</td>
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<td>LEV</td>
<td>Leverage</td>
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<td>LIQ</td>
<td>Liquidity</td>
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<td>AQ</td>
<td>Asset Quality</td>
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<tr>
<td>CII</td>
<td>Capital Intensity Investment</td>
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<tr>
<td>INDSG</td>
<td>Total loan growth of each bank as percentage of all banks total loan</td>
</tr>
<tr>
<td>INDCII</td>
<td>Total asset growth of each bank as percentage of all banks total asset</td>
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<tr>
<td>GDP</td>
<td>Growth Domestic Product</td>
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<td>IRMM</td>
<td>Interest Rate of Money Market</td>
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<td>IFL</td>
<td>Inflation Rate</td>
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DECLARATION

I hereby declare that the project paper is based on my original work except for quotations and citations that have been duly acknowledged. I also declare it has not been previously or concurrently submitted for any other Master's programme at Universiti Utara Malaysia or other institutions.

______________________________________________
KAMARIZAH BT ZAINOL ABIDIN

Date: 30 June 2012
This paper is represents a theoretical review of the net interest margin of commercial banks in Malaysia. This study aims to analyze and investigate the behavior impact of bank operating in determining their net interest margin for the period of 5 years and to find out the factors affecting Net Interest Margin (NIM) in Malaysia banking industry. The determinants of NIM and theories used in this study are those frequently described in conventional banking studies and literature. The NIM determinants were basically divided into two main categories, namely as internal determinants and the external determinants.

In order to incorporate the internal and external determinants into a single net interest margin model, it was necessary to pool cross-section and time-series data. As a result, pooled regression analysis was applied to a linear model to analyze the factors affecting net interest margin of commercial banks.

The data that will be used in this case study derived from Bank Annual Financial Report of six commercial bank in Malaysia from year 2006 until 2010. The six commercial banks have selected in this case study namely Maybank, CIMB Bank, Public Bank, RHB Bank, Hong Leong Bank and Affin Bank. We will focused more
on local bank instead of foreign bank by using of financial ratios as a measurement tools to compare the NIM and performance among this bank.

**Keywords:** Commercial banks, net interest margins (NIM), internal and external determinant NIM, bank performance and Financial ratios.
CHAPTER 1

INTRODUCTION

1.1 Background of Top Malaysia Banks

According to Bank Negara Malaysia (BNM), the Central Bank of Malaysia, there are a total of 25 licensed commercial Malaysian banks consisting of 8 domestic bank and 17 foreign banks. As a result of the restructuring and consolidation of the banking sector in Malaysia, six commercial banks were grouped as anchor banks or top banks.

The top 6 Malaysia banks are:

1) **Maybank (Malayan Banking Berhad)**: Established in 1960, Maybank is the largest financial services group in Malaysia. It has over 450 branches worldwide with considerable banking operations in Indonesia, the Philippines and Singapore. It was recognized as the "Most Valuable Brand in Malaysia in 2008" at ALBSE Asia Law Awards. The operations of Maybank include investment banking, asset management, insurance, Islamic banking and commercial banking.
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REFERENCES


