

**FINANCIAL PERFORMANCE OF THE COMMERCIAL
BANKS IN THE KINGDOM OF SAUDI ARABIA: AN
EMPIRICAL INSIGHT**

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KINGDOM OF SAUDI ARABIA: AN EMPIRICAL INSIGHT**

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**Thesis Submitted to
Othman Yeop Abdullah Graduate School of Business
Universiti Utara Malaysia
In the Fulfillment of the Requirement for the Degree of Master of Finance**

DECLARATION

I hereby declare that the thesis is based on my original work except for quotations and citations that have been duly acknowledged.

I also certify that the substance of this project paper has never been submitted for any degree and is not currently being submitted for any other qualifications.

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ABSTRAK

Kajian ini bertujuan untuk meneliti prestasi kewangan bank perdagangan di Arab Saudi dalam tempoh 2000-2013. Sampel kajian yang digunakan adalah 21 buah bank perdagangan yang terdiri daripada 10 bank milikan asing yang beroperasi dalam negara dan 11 buah bank tempatan Arab Saudi untuk tempoh 14 tahun. Walaupun terdapat kajian terhadap bank perdagangan dalam negara tersebut, setakat ini belum ada penilaian komprehensif yang turut memasukkan bank-bank asing sebagai sampel kajian. Penyelidik mahu mengisi jurang ini dalam literatur. Data panel model Linear Regresi Berganda dan model Kuasa Dua Terkecil Biasa telah digunakan dalam kajian ini untuk menganggar nisbah kesan pemacu seperti kecukupan modal (CAR), kualiti aset (AQ), kecekapan operasi (OE), saiz bank (SAIZ), pinjaman bersih kepada jumlah deposit (LIQR-1), aset cair kepada jumlah aset (LIQR-2) pada parameter kewangan seperti Pulangan ke atas Ekuiti (ROE), Pulangan atas Aset (ROA), Margin Faedah Bersih (NIM) dan Q Tobin. Kajian ini mendapati bahawa di peringkat pengumpulan, CAR, OE, SAIZ, LIQR-1 dan LIQR-2 mempunyai hubungan yang positif dan signifikan dengan ROA tetapi AQ mempunyai hubungan yang negatif dan signifikan dengan ROA. Begitu juga, CAR, SAIZ dan LIQR-2 mempunyai hubungan yang signifikan positif dengan ROE, manakala LIQR-1 mempunyai hubungan yang positif tetapi tidak signifikan dengan ROE. AQ mempunyai hubungan yang negatif dan signifikan dan OE mempunyai hubungan negatif tetapi tidak signifikan dengan ROE. Semua pemboleh ubah penentu kecuali CAR dan OE bank mempunyai hubungan yang signifikan positif dengan NIM. CAR mempunyai hubungan yang positif tetapi tidak signifikan dengan NIM dan OE mempunyai hubungan negatif yang signifikan dengan NIM. Q Tobin mempunyai hubungan yang signifikan positif dengan LIQR-2. CAR, OE, dan LIQR-1 mempunyai hubungan yang negatif dan tidak signifikan dengan Q Tobin. Juga didapati bahawa AQ dan SAIZ mempunyai hubungan negatif yang signifikan dengan Q Tobin. Dalam bank-bank tempatan pula, semua pemboleh ubah bebas mempunyai kesan yang tidak signifikan pada semua pemboleh ubah bersandar, kecuali CAR yang mempunyai hubungan yang positif dan signifikan dengan ROA. AQ mempunyai hubungan negatif yang signifikan dengan ROA, ROE dan Q Tobin. SAIZ mempunyai hubungan negatif tetapi signifikan dengan Q Tobin dan LIQR-1 mempunyai hubungan yang signifikan positif dengan NIM; dan LIQR-2 mempunyai hubungan yang positif dan signifikan dengan ROE, dan Q Tobin. Akhir sekali, dalam bank asing, kesemua pemboleh ubah pemalar mempunyai kesan yang tidak signifikan pada ROA, ROE, NIM dan Q Tobin, kecuali CAR, OE dan LIQR-1 yang mempunyai hubungan yang positif dan signifikan dengan ROA. AQ dan LIQR-1 mempunyai hubungan yang signifikan positif dengan NIM. CAR, AQ dan SAIZ mempunyai hubungan negatif dengan Q Tobin. LIQR-2 mempunyai hubungan yang positif dan signifikan dengan ROE, NIM dan Q Tobin.

Kata Kunci: Prestasi kewangan, bank perdagangan, faktor-faktor tertentu bank, Arab Saud.

ABSTRACT

The purpose of this study is to investigate the financial performances of Saudi commercial banks during the period 2000-2013. A sample of 21 commercial banks comprising of 10 foreign owned banks operating in the country and 11 Saudi domestic banks for the captioned 14 years period have been used in the study. Though there are studies on Saudi domestic commercial banks, no comprehensive evaluation have so far been made by including foreign banks in their sample. The researcher has aimed to fill-in this gap in the literature. Using panel data Linear Multiple Regression model and Ordinary Least Squares have been used in the present study to estimate the impact of the driver ratios like capital adequacy (CAR), asset quality (AQ), operational efficiency (OE), bank size (SIZE), net loan to total deposits (LIQR-1), liquid assets to total assets (LIQR-2). on the financial parameters like Return on Equity (ROE), Return on Asset (ROA), Net Interest Margin (NIM) and Tobin's Q. The study found that at the pool level, that CAR, OE, SIZE, LIQR-1 LIQR-2 have positive and significant relationship with ROA but AQ has negative and significant relationship with ROA. Similarly, CAR, SIZE and LIQR-2 have positive significant relationship with ROE, whereas LIQR-1 has positive but insignificant relationship with ROE. AQ has negative and significant relationship and OE has negative but insignificant relationship with ROE. All the determinant variables excepting CAR and OE of banks have positive significant relationship with NIM. CAR has positive but insignificant relationship with NIM and OE has negative but significant relationship with NIM. Tobin's Q has positive significant relationship with LIQR-2. CAR, OE and LIQR-1 have negative insignificant relationship with Tobin's Q. It's also found that AQ and SIZE have negative but significant relationship with Tobin's Q. In the case of domestic banks, all independent variables have insignificant impact on all dependent variables, except CAR which has positive and significant relationship with ROA. AQ has negative but significant relationship with ROA, ROE and Tobin's Q. SIZE has negative significant relationship with Tobin's Q and LIQR-1 has positive significant relationship with NIM; and LIQR-2 has positive and significant relationship with ROE, and Tobin's Q. Finally, in the case of foreign banks, all deriver variables have insignificant effect on ROA, ROE, NIM and Tobin's Q, except CAR, OE and LIQR-1 which have positive and significant relationship with ROA. AQ and LIQR-1 have positive significant relationship with NIM. CAR, AQ and SIZE have negative relationship with Tobin's Q. LIQR-2 have positive and significant relationship with ROE, NIM and Tobin's Q.

Keywords: Financial performance, Commercial banks, Bank Specific Factors, Saudi Arabia

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LIST OF ABBREVIATIONS

SAMA	Saudi Arabian Monetary Agency
SAR	Saudi Arabian Riyal
IMF	International Monetary Fund
ROA	Return on Assets
ROE	Return on Equity
NIM	Net Interest Margin
TQ	Tobin's Q
CAR	Capital Adequacy Ratio
AQ	Asset Quality
OE	Operational Efficiency
SIZE	Bank Size
LIQR1	Liquid Risk Ratio (Loan to Deposits)
LIQR2	Liquid Risk Ratio (Liquid Asset to Total Assets)
NPL	Non-performing Loans
SARIE	Saudi Arabian Riyal Interbank Express
SADAD	Saudi Arabia Payment System
FSAP	Financial Sector Assessment Program
ROD	Return on Deposit

CHAPTER ONE

INTRODUCTION

1.1 Background of Study

The banking sector plays a significant role in enhancing and developing a nation's economy. Banks provide a safe link between the savers who deposit their money and the investors. In addition, banks are involved in current and future development plans of an economy by providing capital for innovation, and infrastructure, and create job opportunities. It is therefore, necessary evaluate the financial performance of banks in order to identify their strengths and also possible weaknesses in their managerial skills and competencies which can be strengthened to enhance the services of they provide. In addition, banks must make future plans to develop their service standards to facilitate balanced economic and technological growth in the country.

Efficiency in Financial performance of banks is very important in all societies and economic systems. One of the most important challenges faced by bank managers, therefore, is how to optimally use their scarce financial resources. In-depth analysis and evaluation of the financial performance of different banks can identify the strengths and weaknesses in the system further improvement. In other words, analysis of financial performance provides an insight into how efficient a bank is in using its assets to generate profits and how sound was its financial health was over a given period of time. It can also, be used to compare and assess similar firms across the domain of banking in the country.

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