The Effect of Banking Relationship on Firm Performance in Malaysian Public Listed Companies

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The Effect of Banking Relationship on Firm Performance in Malaysian Public Listed Companies

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ABSTRACT

Funds from banks play an important role in the growth and maintenance of a firm. Hence, it is important that a firm creates and maintains a good relationship with its bank in order to secure the funds. Establishing a good bank-firm relationship can also help to reduce conflicts between shareholders and creditors since close bank relationship helps the firm to get funding from other financial institutions. Relationships between a bank and a firm consist of two types: bank-borrower relationship and consumer-supplier relationship. The bank-borrower relationship involves primarily a loan agreement between two interested parties. Cooperation between a bank and a firm is more durable than customer-supplier relationships in terms of provision of financing. This thesis investigates the effect of banking relationships on firm performance on companies in Malaysian capital market. Seventy eight firms from the Top 100 public-listed companies in Bursa Malaysia are examined. Investigation is performed to show the effects of number of banking relationships, short-term financing, long-term financing, firm size, and foreign ownership on the firms' performance as measured by return on assets (ROA), return on equity (ROE), and Tobin's Q. Findings show a significant and negative relationships on the number of bank relationships for all of firm performance measures, consistent with previous studies. For ROA measurement, result shows a significant positive relationship with short-term financing, a finding also consistent with past studies. Short-term loan and long-term loan impact ROA and ROE positively, while affecting negatively firm performance measured by Tobin's Q. ROA and ROE have a positive correlation with foreign ownership, while Tobin's Q is negatively correlated with foreign ownership. In general, the study contributes to banking literature by investigating and evaluating the relationship of firm performance and lending banks in shareholders' perspectives.

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LIST OF ABBREVIATIONS

BNR	Number of bank relations
FBMKLCI	FTSE Bursa Malaysia Kuala Lumpur Composite Index
FSZ	Firm Size
FOW	Foreign ownership
LTF	Long-term financing
LAsset	Log of asset
ROA	Return on asset
ROE	Return on equity
STF	Short-term financing

Chapter 1

Introduction

1.1 Introduction to Study

As the business world today becomes more competitive and challenging, firms must have good management in order to improve their performance and sustain it. The management includes the board of directors as a resource provider because they provide social and business contacts, and influence the environment in favors of the firms (Carpenter and Westphal, 2001). It is also believed that managers have the capability as a resource to provide connections to other business sectors and also to the external environment (Zahra and Pearce, 1989). However, there is a separation between management and owners, where the managers tend to act with self-interest that are not always in the best interest of the owners (Jensen and Meckling, 1976).

In order to avoid any irresponsible and unethical acts, the regulatory bodies and shareholders are required to impose a monitoring and control process via corporate governance code to control risks. Corporate governance generally refers to the mechanisms, processes and relations by which firms are controlled and directed. It identifies the rights and responsibilities among different participants in the corporation (such as the board of directors, managers, shareholders, creditors, auditors, regulators, and other stakeholders) and includes the rules and procedures for making decisions in corporate affairs. Corporate governance

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