ASSESSMENT OF CAPITAL REQUIREMENTS OF COMMERCIAL BANKS IN MALAYSIA

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ABSTRACT (ENGLISH)

We analyze the determinants of Capital Adequacy Ratio (CAR) using a sample of twenty local and foreign commercial banks operating in Malaysia based on Basel II Accord for the period of 5 years, from 2005 to 2009.

The main objective of this study is to identify the problem of complying with Basel II Accord, to find out the level of CAR of commercial banks and to identify the component of risk consists of credit risk, market risk and operational risk in commercial banks.

This study has chosen multiple regression analysis to identify the determinants of capital requirements in Malaysian foreign and domestic commercial banks based on Basel II Accord for the period of 2005-2009. The dependent variable is CAR, where as the independent variables are credit risk (CRR), market risk (MRR), operational risk (MRR), LogSize, loan loss provision (LLP). The study has found that all Malaysian banks were committed by a minimum 8 % capital adequacy ratio while most of them had higher than 8% ratio.

By doing this research we have found that both local and foreign commercial banks showed more confidence and adequate. Both existing local and foreign banks are affecting financial services quality in Malaysia, because all banks offer better and low cost banking services for customer during cut-throat competition.

ABSTRAK

Kajian ini menggunakan sampel daripada dua puluh bank perdagangan tempatan dan asing yang beroperasi di Malaysia berdasarkan Perjanjian Basel II dalam tempoh 5 tahun, dari tahun 2005 hingga 2009 untuk mengenalpasti analisis Nisbah Kecukupan Modal . Objektif utama kajian ini adalah untuk mengenalpasti masalah yang dihadapi oleh "Basel II Accord", mengetahui tahap Nisbah Kecukupan Modal dan mengenalpasti komponen-komponen risiko yang terdiri daripada risiko kredit, risiko pasaran dan risiko operasi terhadap bank perdagangan.

Kajian ini juga menggunakan analisis penurunan gandaan untuk mengenalpasti penentu-penentu kepada keperluan modal di Malaysia terhadap bank perdagangan asing dan tempatan berdasarkan Perjanjian Basel II sepanjang tahun 2005 sehingga 2009. Kajian ini menggunakan Nisbah Kecukupan Modal sebagai pembolehubah bersandar dan risiko kredit, risiko pasaran dan "loan loss provision (LLP)" sebagai pembolehubah tidak bersandar. Kajian ini mendapati keseluruhan bank-bank di Malaysia mencapai sekurang-kurangnya 8% nisbah kecukupan modal dan kebanyakannya mencapai nisbah lebih tinggi daripada 8%.

Berdasarkan kajian yang dijalankan, mendapati bank-bank perdagangan tempatan dan asing menunjukkan keyakinannya dalam nisbah kecukupan modal. Selain itu, kualiti perkhidmatan kewangan di Malaysia memberi kesan kepada bank-bank tempatan dan asing kerana bank-bank berusaha menawarkan perkhidmatan perbankan yang lebih baik dan pembiayaan yang rendah kepada pelanggan sepanjang tempoh persaingan.

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LIST OF ABBREVIATIONS

AMA	Advanced Measurement Approaches
BAFIA	Banking and Financial Institutions Act
BCBS	Basel Committee on Banking Supervision
BIS	Bank for International Settlements
BNM	Bank Negara Malaysia
CAR	Capital Adequacy Ratio
CR	Credit risk
FDICIA	Federal Deposit Insurance Corporation Improvement Act
IRB	Internal Ratings Approaches
LGD	Loss Given Default
LLP	Loan loss provision
MR	Market Risk
NIM	Net Interest Margin
NPL	Non-Performing Loans
OR	Operational Risk
PCA	Prompt Corrective Action
RWA	Risk Weighted Assets
VIF	Variance Inflation Factor

CHAPTER ONE

INTRODUCTION

1.1 Introduction

Capital requirements for banks are paramount importance to ensure financial stability in the sense that they are intended to minimize the probability of banks failure at a reasonable cost. In fact, past episodes of widespread insolvency of the bank proved to be very costly in terms of taxpayers' money and highly disruptive to the real sector of the economy, for example, the output losses and sharp rises in unemployment. The role of capital requirements works at least when it provides a loss absorbing cushion for unexpected events and, if properly designed, introduces incentives for banks to limit the risk of their activities. Given that capital is the most expensive source of financing for banks, capital requirements have an effect on return on equity while potentially influencing the competitive position in the financial sector. Against this background and given the growing international capital mobility, global harmonization of prudential supervision, ensuring a level playing field among banks in different countries, is crucial.

Banks spread out their operations internationally by establishing subsidiaries and new branches or by taking over established foreign banks. This internationalization of banking systems has been encouraged by the liberalization of international financial markets.

The contents of the thesis is for internal user only

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