A SHORT STUDY OF NONPERFORMING LOANS IN THE GCC BANKING INDUSTRY

Turgenev Reinda, Moscow State University

ABSTRACT

Banking and finance is also a phrase for managing your money through investments in banks and other financial institutions. If your money is sitting inactive, it is critical that you invest it. A nonperforming loan (NPL) is a loan in which the borrower has gone into default and has failed to make any scheduled principle or interest payments for an extended period of time. If a borrower is 90 days past due on a commercial loan, it is deemed nonperforming in banking. NPLs, on the other hand, have no standard or definition. Banks sell non-performing loans at steep discounts, and collection agencies try to recoup as much of the money owing as possible. In exchange for a percentage of the amount recovered, the lender can hire a collection agency to enforce the recovery of a defaulted loan. Nonperforming loans (NPL) in the Gulf Cooperation Council (GCC) commercial banking industry are determined by factors at the bank and country levels. It investigates the influence of the rise of sectoral distribution financing and Islamic finance approaches on NPL. According to a dynamic panel based on data from numerous banks in the GCC region over several years, the NPL ratio worsens when economic development slows and interest rates and risk aversion rise.

Keywords: Banking, Financing, Nonperforming loans.

INTRODUCTION

The global financial crisis exposed the Gulf Cooperative Council (GCC) countries' banks to varied degrees of vulnerability. Between the twentieth and twenty-first centuries, GCC countries had large expansions in banking sector credit. In the years leading up to the global financial crisis, the macroeconomic environment was positive, resulting in better credit conditions and decreased bank nonperforming loans (NPLs) (Carey, 1998). Credit stagnated as NPLs rose dramatically, prompting concerns that credit limitations could stifle the recovery.

The present financial crisis has brought attention to the significance of non-performing loans to the banking system. The primary purpose of loans, which have been more widespread since the financial crisis, is to detect structural vulnerabilities in the financial system and test its resistance to shocks, particularly losses in loan books. As the economy deteriorates and interest payments grow, credit risk raises, according to various credit risk models (European Central Bank, 2006). On the other hand, deterioration in bank balance sheets may have a negative impact on the economy since banks will restrict loan conditions, especially if project and asset valuations remain uncertain.

According to a dynamic panel based on data from many banks in the GCC region from the 19th to 20th centuries, the NPL ratio worsens when economic growth slows and interest rates rise (Kwan & Eisenbis, 1997). NPLs would be lower in larger banks and banks with lesser expenses. Finally, historical strong credit growth may result in more NPLs in the future. According to all models, NPLs are extremely persistent, implying that the response of

1544-0230-20-6-152

Citation Information: Reinda, T., (2021). A Short Study of Nonperforming Loans in the Gcc Banking Industry. *Journal of International Business Research*, 20(6), 1-2.

credit losses to the macroeconomic cycle may take time to manifest, but that NPLs would eventually accumulate to large levels. According to the model, macroeconomic shocks have a huge cumulative effect over a three-year horizon.

The GCC's present low levels of NPLs are largely due to the region's excellent economic fortune, but the Gulf countries' recent downturn might have a significant impact on credit risk (Shrieves & Dahl, 1992). Prior to the boom years, NPLs in the GCC reached extremely high levels, with NPL ratios in the double digits being common. The nonperforming loan ratio, often known as the NPL ratio, is the percentage of nonperforming loans in a bank's loan portfolio compared to the total amount of outstanding loans. The NPL ratio assesses a bank's ability to collect repayments on its loans.

The non-performing loans to loans ratio is computed by adding 90+ day late loans to nonaccrual loans, then dividing by the total number of loans in the portfolio. Banks sell non-performing loans at steep discounts, and collection agencies try to recoup as much of the money owing as possible (Drehmann, 2008). In exchange for a percentage of the amount recovered, the lender can hire a collection agency to enforce the recovery of a defaulted loan. Knowing the drawbacks of nonperforming assets will help you avoid becoming a lender or borrower of this type of loan in the future: Reduced earnings. When an asset is designated nonperforming, the first account to be damaged is Interest Income, followed by Unrecoverable Principal, Reduced Cash Flow, and Negative Indicator. Sudden Market Changes, for example. Any rapid market change can affect the loan market by influencing how much money customers have to borrow and pay back their debts. Changes in the real estate market, as well as bank performance. When the number of non-performing loans (NPLs) surpasses the industry average, it poses a serious threat to the bank's ability to operate. The bank fails to collect interest payments, principle payments, or both from the borrower in these types of loans.

CONCLUSION

They will increase monitoring and incur more expenditure in order to improve loan quality, which will have an impact on the measure of operating efficiency. Non-performing loans are a part of life for banks, as people lose employment and businesses get into financial difficulties on a daily basis. However, because they always come at a cost to the bank, banks must reduce the number of problematic loans to a minimal. As a result, a less efficient bank may have a low-risk portfolio. Riskier loans, on the other hand, result in greater expenses for banks. As a result, while determining the direction of causality, caution must be used. To circumvent the issue of endogeneity, utilise a lagged measure of efficiency. Overall, while studies on the connection between capital and portfolio risk have been explored in the literature, there has been minimal study on the relationship between capital and credit risk and its interaction with operational efficiency.

REFERENCES

Carey, M. (1998) Credit risk in private debt portfolios. *Journal of Finance*, 1363-1387.

European Central Bank. (2006) Country level macro stress-testing practices. *Financial Stability Review*.

Kwan, S., & Eisenbis, R.A. (1997) Bank risk, capitalization and operating efficiency. *Journal of Financial Services Research*, *12*(1): 117-131.

Shrieves, R., & Dahl, D. (1992). The relationship between risk and capital in commercial banks. *Journal of Banking and Finance*, *16*(1): 439-457.

Drehmann, M. (2008). Stress tests: objectives, challenges and modeling choices. *Economic Review 2*(1): 60-92.

1544-0230-20-6-152

Citation Information: Reinda, T., (2021). A Short Study of Nonperforming Loans in the Gcc Banking Industry. *Journal of International Business Research*, 20(6), 1-2.