EVALUATION of NON-PERFORMING LOANS and ITS IMPACT to OVERALL FINANCIAL PERFORMANCE of FINANCING and LEASING COMPANIES : CASE of OMAN

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Abstract

Purpose: This research paper was conducted to evaluate and investigate on the impact of non-performing loans (NPLs) on the financial performance of financing and leasing companies in Oman. This research has covered research objectives such as the evaluation of the factors of NPLs on financing and leasing in Oman, determining the influence of NPLs on financial performance of financing and leasing in Oman and the evaluation of the impact of the decline and incline of NPLs to Oman's economy.

Design/methodology/approach: This research paper used the descriptive quantitative approach to collect information. The questionnaire was distributed among 150 respondents of 5 NPLs organizations and after data collection, the data has been analyzed through SPSS 23.0 software.

Findings: The ultimate objective of the research was to look at the link between NPLs and financial performance of financing and leasing companies in Oman.
The descriptive statistics for external factors depicts that externally mostly global crises (Mean= 3.6, S.D= 1.08) and stock share prices (Mean= 3.88, S.D=1.05) impacted loans which turn it into non-performing loans while inflation in economy negatively influence NPLs having low mean and S.D from all other external factors it means inflation affected NPLs but not at that extent which other factors impacted.

Research limitations/implications: Restrictions point to the limitations that analysts experience when conducting research. When analyzing the relationship between the NPL and the financial processes of financial and leasing companies, the analyst experiences some limitations in this consideration, such as limited time period, limited test measurement, etc.

Social Implications : There should be no social harm during the investigation process. It involves challenges in individual contact, separation or any other physical and emotional injury.

Originality / Value: No research was found regarding the financial NPLs performance. This research was an attempt to tackle the situation and thrown light.

Keywords: NPLs, financial performance, financing and leasing companies, non-performing loans

Introduction

Leasing and financing corporations play an integral part of the economy and act as a mediator between investors and borrowers. The reason for reviewing NPLs in financing and leasing is clear: "financial pollution" can be generated by them and at the same time can be catastrophic for financial development and social welfare. Expansion of the budget division can be a step closer to improving the economy so that it can be a key factor in growth. (Besmir & Aliu, 2021) states diversified economies have the reason for the bank's frustration and increase in non-performing advances. The reasons may be components of the situation such as financial situation or interbank variables. NPLs affect the liquidity and productivity of financial institutions, which is generally one of the key components of financial institutions' performance.

As per (Islam et al., 2020), increases non-performing loans, reduces profits within the economy. NPLs need to be carefully considered because of their impact on bank survival and the survival of the economy. The incompatibility among resources and liabilities makes liquid assets an opportunity for banks that deviate from the typical picture of a bank's credit rating calculations. NPLs have created a number of problems in the financial spheres of the nations. Along with financial growth, the expansion of NPLs also affects the management and distribution of accounts. The growing number of non-performing advances in any economy indicates a monetary emergency. The main objective of this research paper is to explore the factors of NPLs and its influence on the financial performance of financing and leasing in Oman that has also impacted the economic growth of a nation.

Research Questions
i.   What are the factors involved for the occurrence of NPLs in finance and leasing companies in Oman?
ii.   In what way the NPLs influence the financial performance of financing and leasing companies in Oman?
iii.   Either the decline or incline of NPLs has any impact to Oman's economy?

Objectives of the Research
i.   To evaluate the factors of NPLs in finance and leasing companies in Oman.
ii.   To determine the influence of NPLs on financial performance of financing and leasing companies in Oman.
iii.   To evaluate the decline and incline of NPLs to Oman's economy.

Statement of the Research Problem
The problems statement relies on how many NPLs occurring currently in Oman which influences its economy in a negative ratio. Is the ratio of NPLs decreased or increased from last 7 years. The ratio of Non-Performing Loan for Oman's leasing companies was fluctuated within the previous decade in Oman's finance and leasing company. In any case, it started to

increase compellingly from 2007 till 2008. A small decrease was famous in 2009 in any case at that point it started to increase again and had a large number of NPLs within the year 2015. Research updates had compelled on investigating as well the factors impacting the customers to perform their loans as non-performing? Is the finance and leasing companies has any influence on their financial performance through NPLs?

Literature Review

A writing survey may consist primarily of an overview of major sources, but in the social sciences, a writing audit typically includes an organizational form and involves both rundown and aggregation, frequently within certain conceptual categories. In this research, all the preceding studies regarding the factors of NPLs, its impact on the financial performance of financing and leasing companies, and the influence to the economy were considered for further review.

Financial Performance of Financial Institutions

According to (Ravikumar et al., 2019), the slant created in NPLs between 2000 and 2020 accounted for more than 35% of the total advances allowed and this created financial problems for the financial institutions as a whole. Financial institutions defaulting on their debts were found to be abandoning their obligations in many cases and resorting to other uninformed financial institutions to negotiate unused liabilities, which in turn led to non-performing credits, it's likely to go bad. Bilateral status reports have not been successfully used to differentiate between such objectionable multiple advance defaulters. Thus, the need for a centralized database that has made it mandatory for borrowers to have the required stable credit data. It provoked the Central Bank, while maintaining that inefficient administration is often associated with higher operational costs which led to investment in the affected financial institutions.

Role of NPLs on Economy

As per (Vidal & Vidal, 2021), modeling credit looks at the growth of the economy as promotion increases utilization and achieving such an encouraging social benefit, while NPLs are considered a cause of economic contamination. The author has separated the two financial proposals of NPLs. First, the growth of NPLs may lead to a slowdown in financial growth, which will result in the wasteful allocation of assets. Moreover, the development of NPLs will result in an increase in capital requirements as the depletion of capital is due to the stores getting entangled in such materials, leading to innovative, financially sound projects for financial institutions and financing becomes incomprehensible. The author also affirmed that the growth of NPLs may lead to a slowdown in financial growth, which will result in the wasteful allocation of assets, as well as the development of the NPL that will result in an increase in capital requirements.

Research Methodology

This research study was descriptive and analytical in nature. Descriptive research design was used to describe the phenomenon while analytical research design was used to analyse the relationship between NPLs and financial performance of financing and leasing companies through correlation, regression, T-test, ANOVA. The quantitative research approach has been utilized to collect the information and analyzed it afterwards in statistical software SPSS easily. The statistical tools utilized the descriptive statistics, regression, and correlation to check the relationship between non-performing loans (NPLs) on the performance of financing and leasing companies. The paired sample T-test and ANOVA were used to correlate that either the internal or external factors affect the loans to become non-performing.

Data Analysis

Descriptive Statistics for Internal Factors of NPLs

Table 1.0 Descriptive Statistics For Internal Factors of NPLs

	N	Minimum	Maximum	Mean	Std. Deviation
NPLs affected by the size of the firm	150	1.00	5.00	3.6467	1.13597
Higher lending/interest rates generated NPLs	150	1.00	5.00	2.3467	1.18710
Higher amount of loans generated NPLs.	150	1.00	5.00	3.3267	1.36837
ROE ratio has significantly important for NPLs	150	1.00	5.00	3.0867	1.11088
NIM ratio has positive influence on NPLs.	150	1.00	5.00	3.2267	.97724
CAR has a negative effect on net non-performing loans	150	1.00	5.00	3.1067	1.13603
Valid N (listwise)	150				

The above table shows that the minimum value in entire data collected is 1 and maximum value is 5 that demonstrates the higher perception of responses. The higher mean indicates the higher perceptive variable that respondents feel has highly affected factor for non-performing loans. The higher the mean has lower standard deviation means that it highly deviate from their means. In the above table, the statement NPLs affected by the size of the firm has higher mean=3.65 with S.D=1.14, it means if the size of the firm is large then the possibility of NPLs is more than the smaller in size bank or financing/leasing companies (Gjini, 2021). Similarly, the internal factor higher amount of loans generated higher NPLs as it has mean=3.33 with S.D= 1.68. It shows that when amount was high, it also has higher interest amount on total original amount that makes it impossible to borrower to give back the loan and gone under non-performing loan category (Bayer, 2019). According to the responses, it is estimated that when ratio increases, the NPLs increases in positive. The statement that higher lending/interest rates creates NPLs has lower mean in all statements which depicts that in Oman banks and financing/leasing companies there has not been so much lending/ interest rates or mostly banks lend or finance any project without markup. This was contrary to the findings of (Hassan et al., 2016).

Descriptive Statistics for External Factors of NPLs

Table 2.0. Descriptive Statistics for External Factors of NPLs

	N	Minimum	Maximum	Mean	Std. Deviation
Global crises positively influences NPLs.	150	1.00	5.00	3.6000	1.08064

	N				
Inflation in economy negatively influence NPLs	150	1.00	5.00	3.3267	.90855
NPLs also generated due to the increase in stock share prices	150	1.00	5.00	3.8800	1.04862
Valid N (listwise)	150				

The descriptive statistics for external factors depicts that externally mostly global crises (Mean= 3.6, S.D= 1.08) and stock share prices (Mean= 3.88, S.D=1.05) impacted loans which turn it into non-performing loans (Abdelbaki, 2019) while inflation in economy negatively influence NPLs having low mean and S.D from all other external factors it means inflation affected NPLs but not at that extent which other factors impacted. The current research opposite to the findings of (Alromaihi et al., November, 2020)

Correlation Analysis

As per (Makowski et al., 2020), investigating the relationship is related to measuring the affinity between two endless factors, and for this case, a subordinate and independent variable or between two independent factors is called correlation analysis.

Table 3.0 Correlation Analysis

		NPLs	Financial Performance
NPLs	Pearson Correlation	1	-.913[**]
	Sig. (2-tailed)		.000
	N	150	150
Financial Performance	Pearson Correlation	-.913[**]	1
	Sig. (2-tailed)	.000	
	N	150	150

**. Correlation is significant at the 0.01 level (2-tailed).

The correlation analysis said that there is a strong negative relationship between NPLs and financial performance of financing and leasing companies both of the variables and it has the value =-.913 depicts the higher negative association between both of them which states that an increase in NPLs decrease the financial performance of financing/leasing companies. It is critically analyze that (Serwadda, 2018) supports the findings that NPLs have negative relationship with financial performance but with large sample size of 300 employees of banks in Oman.

Regression Analysis

According to (Heimann & Isaacs, 2018), "The analysis was completed by pointing to the regression to examine the relationship between the result variable and one or more factors. Outcome variables are known as subordinate or reaction variables and opportunity

components, and co-founders are known as indicators or independent factors. The subordinate variable is denoted by "y" and the independent factor is indicated by "x" in the re-examination." Here in this study regression also has been used to determine the slope and association of the dependent and independent variables.

Table 4.0. Regression Model Summary[b]

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	-.913[a]	.834	.833	.21461

a. Predictors: (Constant), NPLs

b. Dependent Variable: Financial Performance

The value of coefficient of correlation value is R=-.913 which shows negative correlation between both of the variable but R^2=0.834, which shows that it has a positive association between one another as its values always lies between ±1 and it shows that if the financial performance of the financing/ leasing companies impact it is mostly due to large number of NPLs.

Table 5.0. Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	.674	-.085		-7.931	.000
	NPLs	-.674	-.025	-.913	27.232	.000

a. Dependent Variable: Financial Performance

The slope of the equation has been determined by the coefficients of the regression equation and it indicates that it has negative slope. Non-performing loans have a major impact on financial performance of financing and leasing companies, as shown in the table above. Non-performing loans have a significance value of less than 0.05 in the model, indicating that there is a negative and significant association between them. Non-performing loans (b=-.674) is significant, with a negative coefficient, implying that higher Non-performing loans is associated with lower financial performance.

Paired Sample T-test

Paired sample t-test always calculated to estimate the difference from population means and would be determined and forecasted according to the p-value in a distribution. Higher the t-test and lower p-value indicates that the pair has significant affect upon one another. The pair sample t-test for external and internal factors significance upon NPLs shown below:

Table 6.0 Paired Samples Statistics

		Mean	N	Std. Deviation	Std. Error Mean
Pair 1	NPLs	3.3631	150	.71066	.05803
	Internal Factors	2.2726	150	.34739	.02836
Pair 2	NPLs	3.3631	150	.71066	.05803

External Factors	3.6027	150	.81370	.06644

Above table is the paired sample statistics for NPLs and internal factors and NPLs and external factors which shows the mean, S.D and S.E among all and determines that NPLs have significantly impacted by external factors.

Table 7.0 Paired Samples Correlations

		N	Correlation	Sig.
Pair 1	NPLs & Internal Factors	150	.707	.000
Pair 2	NPLs & External Factors	150	.877	.000

The table 7.0 depicts that the positive correlation of both internal and external factors with NPLs means if any of the factor involved the NPLs increases but on the whole NPLs has negative correlation with financial performance of financing and leasing companies.

Table 8.0 Paired Samples Test

		Paired Differences					t	df	Sig. (2-tailed)
					95% Confidence Interval of the Difference				
		Mean	Std. Deviation	Std. Error Mean	Lower	Upper			
Pair 1	NPLs - Internal Factors	1.09047	.52575	.04293	1.00564	1.17529	25.403	149	.000
Pair 2	NPLs - External Factors	-.23960	.39054	.03189	-.30261	-.17659	-7.514	149	.000

According to the above table the p value is smaller than 0.05 significance value and the t-value for internal factors for NPLs indicates the significant difference between two means and indicates that it is positively significant with NPLs while on the other hand external factors have negatively significant with NPLs and also have lower p-value than significance value. Both internal factors and external factors impacted the financial performance of financing and leasing companies. By applying t-test it is observed that the value of p=0.000 which is less than significance level 0.05, hence, it was concluded that there is an association between NPLs and financial performance of financing and leasing companies.

Conclusions

After all the discussion and analysis, it was concluded that both internal and external factors plays significant and important role in generating NPLs which ultimately affect the financial performance of financing/leasing companies in Oman. Also it is significantly known that size of firm, profitability and return on investments have immense impact on NPLs as internal factors and global crises and stock share prices impacted NPLs more than inflation on NPLs as external factors that would have immense worse impact on the financial performance of

financing/leasing companies in Oman. It is also revealed that there is a higher negative association between NPLs and financial performance of financial institutions which also impact the GDP of Oman's economy.

Recommendations

The directors or managers of financing and leasing companies including banks should make the policies regarding maintenance of size of firm, capital adequacy ratio (CAR), and return on investment to the extreme level that the chance of NPLs become so minimal. The managers at banks should reorganize their banking reforms about lending to the borrowers of large amount loan and ensure about the collateral mortgage against taking loan, as when any loan would be gone under NPLs the financial institutions will be able to recover it. Thus, the need for a centralized database has made it mandatory for borrowers to have the required stable credit data. The Government of Oman should formulate its best strategy for stock market share prices, inflation factors which are the main cause or effect of NPL as external factors. The government of Oman should take step to give interest free loans to the borrowers who want to start their own business, or make a house or any other personal reason so that the borrower feel free to give back the loan easily.

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