

IMPACT OF NON-PERFORMING LOANS ON BANK'S PROFITABILITY: EVIDENCE FROM THE BANKING SECTOR OF PAKISTAN

BY

AQSA ARIF	69855
BISMA JAVED	69860
SYEDA NEHA SADAQAT	69888

A Project submitted to Department of Management Studies, Bahria Business School, Bahria University – Karachi Campus, in partial fulfillment of the requirement for BS A&F Degree



**BS (ACCOUNTING & FINANCE)
SPRING-2024**

Bahria University Karachi Campus

PROJECT APPROVAL STATEMENT

APPROVAL FOR EXAMINATION

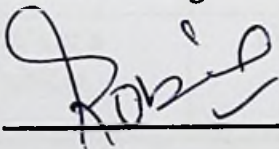
Candidate's Name: Syeda Neha Sadaqat **Enrollment No.:** 02-112202-043

Candidate's Name: Aqsa Arif **Enrollment No.:** 02-112202-002

Candidate's Name: Bisma Javed **Enrollment No.:** 02-112202-007

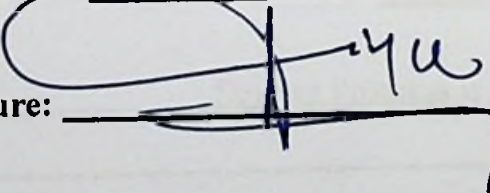
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Supervisor's Signature:  _____

Date: 24.07.24

Supervisor's Name: SOBIA MURTAZA

HOD's Signature:  _____

Date: _____

1st Half Semester Progress Report & Thesis Approval Statement

Name of Student(s)	Syeda Neha Sadaqat, Aqsa Arif, Bisma Javed
Enrolment No.	02-112202-043, 02-112202-002, 02-112202-007
Thesis/Project Title	Impact Of Non- Performing Loans on Bank's Profitability: Evidence from Banking Sector of Pakistan

Supervisor Student Meeting Record

No.	Date	Place of Meeting	Topic Discussed	Signature of Student
1	12.02.2024	Ma'am's Cubicle	Topic for FYP	<i>[Signatures]</i>
2	26.02.2024	Ma'am's cubicle	Contents of the report and discussion of each chapter in detail	<i>[Signatures]</i>
3	10.03.2024	Ma'am's Cubicle	Queries related to Chapters 1 and 2	<i>[Signatures]</i>
4	05.03.2024	Ma'am's Cubicle	Detailed discussion related to the first three chapters.	<i>[Signatures]</i>

Progress Satisfactory

Progress Unsatisfactory

Remarks: Student Progress is Satisfactory

Signature of Supervisor: *[Signature]*

Date: 24.7.24

Name of Supervisor: Sobia Murtaza

2nd Half Semester Progress Report & Thesis Approval Statement

Name of Student(s)	Syeda Neha Sadaqat, Aqsa Arif, Bisma Javed
Enrolment No.	02-112202-043, 02-112202-002, 02-112202-007
Thesis/Project Title	Impact Of Non- Performing Loans on Bank's Profitability: Evidence from Banking Sector of Pakistan

Supervisor Student Meeting Record

No.	Date	Place of Meeting	Topic Discussed	Signature of Student
1	25.04.2024	Ma'am's Cubicle	Discussion related to the remaining two chapters	<i>[Signatures: Aqsa, Bisma]</i>
2	36.04.2024	Ma'am's Cubicle	Ran the tests and discussed the interpretations	<i>[Signatures: Aqsa, Bisma]</i>
3	06.05.2024	Ma'am's Cubicle	Discussed the correction of errors	<i>[Signatures: Aqsa, Bisma]</i>

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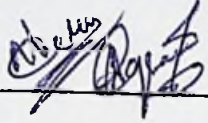

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Name of Supervisor: Sobia Murtaza

Declaration of Authentication

I, hereby, declare that no portion of the work referred to in this project has been submitted in support of any application for another degree or qualification of this university or any other institution of learning.

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Abstract

Purpose

This study examines the relationship between non-performing loans and bank profitability with a focus on the banking sector in Pakistan.

Design/Methodology/Approach

Using deductive research and causality research, the study analyzes data from 15 listed commercial banks in Pakistan. Using empirical analysis and theoretical frameworks, the study identifies the key factors influencing non-performing loans and their impact on bank profitability in different market contexts.

Findings

Findings show significant correlations between non-performing loans, capital adequacy ratio (CAR), liquidity (LQDT), and return on capital (ROA). Specifically, higher NPL and liquidity are linked with lower ROA, while an increase in CAR is linked with higher ROA. However, *gross domestic product (GDP) does not significantly affect ROA in the considered models. In addition, a diagnostic test is done to ensure the reliability of regression analysis by demonstrating the normal distribution of the data and finding the absence of heteroscedasticity and serial correlation, both fixed and random effects models are used, with the Hausman specification test favoring the fixed effects model.*

Originality/Value

This research provides valuable information to policymakers, investors, and financial institutions, improving the understanding of the challenges posed by non-performing loans. By examining the background factors and systemic effects of non-performing loans, the study informs evidence-based policies and risk management practices aimed at ensuring financial stability and promoting sustainable economic development.

Keywords: NPLs, Credit Risk, ROA, GDP, Profitability

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and Meehan (2013) et al. have contributed to the definition of non-performing loans, emphasizing that they do not generate profits during certain periods. The phenomenon extends beyond developing countries to include both emerging and developed countries, as emphasized in paper by Akhtar & Roy (2017).

Non-performing loans, often referred to as bad debts or delinquent loans, have become a growing challenge in the banking sector due to their negative impact on the performance and operational efficiency of financial institutions. The persistence and extent of non-performing loans highlight the need for a detailed understanding of their determinants and their impact on bank profitability. Despite efforts to mitigate their impact, the proliferation of non-performing loans continues to pose a challenge to financial stability and economic development worldwide.

In the past, non-performing loans were viewed with pessimism due to their negative impact on a company's profitability. Comprehensive data from the World Bank and the banking sector of Pakistan highlights the significant presence of non-performing loans across all sectors, with commercial banks particularly reliant on generating income from loans and advances. On the other hand, poor management of these assets can expose banks to credit risk and thereby reduce their profitability.

Commercial banks, as important financial intermediaries, play a key role in allocating financial resources and supporting economic growth. However, their profitability depends on the quality of their portfolio and efficient credit risk management. Non-performing loans represent a