SIZE AND RISK TAKING OF FINANCIAL INSTITUTIONS: EVIDENCE FROM FINANCIAL SECTOR OF PAKISTAN

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A thesis is presented to Bahria University, Islamabad in partial fulfillment of the requirements for the degree of Master in Science

April, 2016

Abstract

This study is to investigate how size of a firm is related to the risk taking behavior of financial institutions in Pakistanfrom year 2004 -2014. Theory Too big to fail is of view that large firms take advantage of their TBTF status and take on high risk. Sample used for the empirical testing of the present study is 38 financial institutions including commercial banks, investment banks and insurance companies regulated under State Bank of Pakistan. The data is obtained from the annual reports of the financial institutions and Karachi stock exchange (KSE-100).

This study measures risk taking by z-score and Merton distance to default. The size of the firm is measured by total assets and revenue of the institutions. This study has included other variables including insider ownership, firm age, charter value and financial crisis indicator to see their impact on risk. To seek answers of the research questions, e-views software is used to run the descriptive statistics analysisand multiple regression analysis on the collected data. The results of the present study indicate that the size of the firm is positively related to the risk taking of financial institutions. Experienced Firms are better at handling risk and charter value decreases the risk taking. The insider ownership and financial crisis are insignificant to the risk taking of financial institution in Pakistan. Furthermore investment companies are the most risk takers as compared to commercial and insurance companies.

Keywords: Financial crisis, Bank size, Bank risk, Too big to fail.