ABSTRACT

In the research paper, quarterly data on Non-performing Loan (NPL) for commercial banks in Malaysia over the time period of quarter 1, 1998 to quarter 4, 2009 together with 5 macroeconomic indicators i.e. Gross Domestic Product (GDP), Consumer Price Index (CPI), FTSE Bursa Malaysia KLCI (KLCI), Unemployment rate and House Property Index are collected to form a credit risk model. The estimated model is employed to analyse banking credit risks conditional on current macroeconomic conditions. Stepwise multiple regression method has been used which to select the useful subsets of variables and to evaluate the order of importance of variables.

Furthermore, the paper presents some examples of applying the model to macro stress testing, i.e. analysing the effects of the most adverse macroeconomic events on the banks’ credit risks stemming from the corporate and consumer sectors. The vulnerability of the Commercial Banks’ credit book had been tested with different level of stress scenarios i.e. severe stress scenario, moderate stress scenario and mild stress scenario, which these scenarios were identified by GDP. In short, this research shows a macro-prudential concept of credit risk linked to financial stability indicators and presents the simulation results.
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