Research Journal of Finance and Accounting
ISSN 2222-1697 (Paper) ISSN 2222-2847 (Online)
Vol.7, No.9, 2016

Human Capital and its Impact on Banking Financial Performance

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Abstract

The importance of human capital has been increased during the last period because many financial institutions and banks faced a lot of problems. The reason of facing these problems or crises is that those companies had a lack of trained and professional staff. So, banks around the globe noticed this problem and tried very hard to attract the well trained employees and improve their employees' skills.

This study examines the impact of human capital on banking financial performance for Jordan Islamic Bank (JIB) during 2000 – 2014. The Dependent variable is financial performance which was presented by net income, return on assets, and return on equity. Meanwhile, the independent variable is human capital which was measured by number of employees, number of branches and offices, number of courses and seminars, and finally number of the participants in the courses and seminars.

The researchers found a positive and significant relationship between net income and number of employees, but the relationship between net income and number of branches and offices was negative and significant. Also, the researchers found the relationships between net income and each of number of courses and seminars, and number of participants in courses and seminars were not significant which indicate that focusing on the quality not such on the number of courses.

In addition, we found a negative and significant relationship between return on assets and number of branches. On the other hand, we did not find a significant relationship between return on assets and each of number of employees, courses and seminars, and participants in courses and seminars.

Unfortunately, the researchers found not significant relationships between return on equity on one hand, and every proxy of the independent variables.

Keywords: human capital, banking financial performance, Islamic banks, and Jordan.

1. Introduction

Human Resource Management (HRM) is a very vital sector in any financial institution, and many researchers try to improve HRM by lots of ways. For instance, publishing books, making research, giving courses and seminars, and improving the employees' skills by trainings in order to enhance the financial institutions' performance. More recently, in the emerging knowledge economy, value can be increasingly seen to reside in intellectual capital (IC) such as knowledge and information—assets that are generally embodied in people. Many conceptual frameworks have been created in order to understand, codify and examine intellectual capital (Moghaddam, Shakeri, and Tavakolnia, 2013).

Human capital is getting wider attention with increasing globalization and also the saturation of the job market due to the recent downturn in the various economies of the world. Developed and developing countries put emphases on a more human capital development towards accelerating the economic growth by devoting necessary time and efforts (Marimuthu, Arokiasamy, and Ismail, 2009).

The researchers consider the most important factors can improve the banking performance are technology, assets and buildings, and on top of that is human capital which we can call that as the triangle of success.

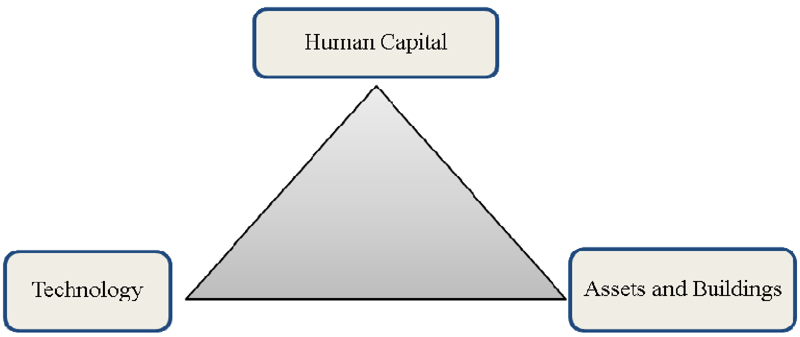

Figure (1) Triangle of Banking Success

In this study the researchers focused on human capital as an independent variable. It was measured by number of employees, branches and offices, courses and seminars, and participants in courses and seminars as well. On the other side, the dependent variable was banking financial performance which was measured by net income, return on assets (ROA), and return on equity (ROE). The sample of this study is Jordan Islamic Bank (JIB) during 2000 to 2014.

2. Research Problem

This study tries to reveal a side about the impact of human capital and its participation in making and achieving profits. So, we will try to answer the following question: is bank's profitability affected by human capital? And if the bank improved the employees' skills, can the bank achieve high levels of profitability and increase its market share in present and future?

3. Research Objectives

The objective of this research is to put a light on the human capital in Jordan especially on the human capital in banks; the researchers studied Jordan Islamic Bank (JIB) as a sample for this study. Human capital is represented by number of employees, number of branches and offices, number of courses and seminars, and number of participants in that courses and seminars. On the other hand, net income, return on assets, and return on equity are proxies of banking financial performance as dependent variables.

4. Research Hypotheses

We formulated the hypotheses by relaying on the research variables to investigate the research problems and to fulfill its goals.

$H_{0.1}$: There is no statistically significant relationship between banking financial performance (net income after tax) and human capital.

$H_{0.1.1}$: There is no statistically significant relationship between net income after tax and number of employees.

$H_{0.1.2}$: There is no statistically significant relationship between net income after tax and number of branches and offices.

$H_{0.1.3}$: There is no statistically significant relationship between net income after tax and number of courses and seminars.

$H_{0.1.4}$: There is no statistically significant relationship between net income after tax and number of participants in courses and seminars.

$H_{0.2}$: There is no statistically significant relationship between banking financial performance (Return on Assets (ROA)) and human capital.

$H_{0.2.1}$: There is no statistically significant relationship between ROA and number of employees.

$H_{0.2.2}$: There is no statistically significant relationship between ROA and number of branches and offices.

$H_{0.2.3}$: There is no statistically significant relationship between ROA and number of courses and seminars.

$H_{0.2.4}$: There is no statistically significant relationship between ROA and number of participants in courses and seminars.

$H_{0.3}$: There is no statistically significant relationship between banking financial performance (Return on Equity (ROE)) and human capital.

$H_{0.3.1}$: There is no statistically significant relationship between ROE and number of employees.

$H_{0.3.2}$: There is no statistically significant relationship between ROE and number of branches and offices.

$H_{0.3.3}$: There is no statistically significant relationship between ROE and number of courses and seminars.

$H_{0.3.4}$: There is no statistically significant relationship between ROE and number of participants in courses and seminars.

5. Literature Review

In this part we will take a tour to look at some previous studies and researches that focused on the employees' skills and their capabilities in improving and enhancing the institutions' and firms' performance.

5.1. Maran Marimuthu, Lawrence Arokiasamy, and Maimunah Ismail (2009). Human Capital Development and its Impact on Firm Performance: Evidence from Developmental Economics.

This paper examines the extent to which human capitals have direct impacts on firm performance from various critical perspectives. Firm performance is viewed in terms of financial and non-financial performance; the conceptualization of human capitals is closely linked to some fundamentals of economics and firm performance. The study shows that there is reasonably strong evidence to show that the infusion of 'human capital enhancement' in organizations promotes innovativeness and greater firm performance. Financial performance is positively impacted through the consideration of human capitals.

In light of this, the understanding of firm performance in relation to human capitals should not be regarded as a phenomenon that only adds 'more zeros' in a firm's profits; it is rather transforming the entire workforce as the most 'valuable assets' in order for the organization to pave ways for greater achievements via innovativeness and creativity. Hence, companies should therefore, come up with some effective plans especially in investing the various aspects of human capital as not only does it direct firms to attain greater performance but also it ensures firms to remain competitive for their long term survival.

5.2. Oboh Jerry Sankay, Rahmah Ismail, Abu Hassan Shaari (2010). The Impact of Human Capital Development on the Economic Growth of Nigeria.

The overall objective of the paper is to investigate the impact of human capital development on economic growth in Nigeria during the period 1970 to 2008. The basic macroeconomic variables are: real gross domestic product, real capital expenditure on education, real recurrent expenditure on education, real capital stock, total school enrolments and labor force are used to proxy human capital development. The result indicated that human capital development has a significant impact on Nigeria's economic growth.

It reveals that investment in human capital, in the form of education and capacity building through training and orientation impacts positively on the economic growth in the long-run, but in the short-run only labor force tend to impact significantly on economic growth within one year lag period. The result also revealed that government spending on education does not impact positively on economic growth. The study supports human capital as a source of economic growth. To contribute significantly to economic growth and development, education must be of high quality and also meet the skill-demand needs of the economy; therefore, the Nigerian government should increase spending on education.

5.3. Muhammad Farhan Akhtar and others (2011). Extent of training in Banks and its Impact on employees' motivation and involvement in job.

Banking sector of Pakistan is characterized by the high competition and in order to survive in the market place, employers have understood the need for ongoing training and development to equip their employees to better cope up with the demands of the dynamic environment today. This study seeks to determine the impact of this training and development on motivation and job involvement along with what training methods are widely used in the banking sector of Pakistan. The primary data for this study was collected through a structured questionnaire that was tailored with the help of literature. The questionnaire comprised of 37 items, categorized into 5 sections, which are general perspective, motivation, job involvement, training & development and demographics. Survey was carried out on public and private banks of Pakistan (Punjab region). With the support of SPSS, correlation and regression analysis was conducted to generate results. We found that training and development has a positive association with both motivation and job involvement of the employees of banks in Pakistan. Moreover, job instructional training and informal learning are widely used techniques to impart the knowledge towards the employees in banking sector. These findings suggest that by boosting the training and development activities within the banking sector the employees could be motivated and get attached with their work.

Training for employees of an organization is considered very much important in order to achieve excellence and competence. Training has a positive impact on both motivation and job involvement. This study emphasizes the need and importance of training on the employees in the banking sector characterized by low morale due to high work stress.

5.4.Neelam Tahir and others (2014). The Impact of Training and Development on Employees Performance and Productivity a case study of United Bank Limited Peshawar City, KPK, Pakistan.

This paper main objective was to investigate whether training and development has impact on employees' performance and productivity and to find the impact of training and development on employees' performance and productivity. There were two variables training and development (independent) and employees' performance and productivity (dependent). Eight united banks limited were selected for the study. The goal was to see whether training and development has an impact on employees' performance and productivity. The result showed that there was significant relationship between the variables. Human Resource Management (HRM) plays an important role in managing an organization, such as the effects of HRM on innovation, new way of working principles for working relations and enhancing employees' capability. Training and development is an important aspect of HRM. It is important for organization to get skilled and capable employees for better performance, and employees will be than competent when they have the knowledge and skill of doing the task. Training and development would provide opportunities to the employees to make a better career life and get better position in organization. In doing so, organizations efficiency would be increased. On the other hand, employees are the resources and assets of an organization if they are skilled and trained would perform better than those who are unskilled and untrained.

We consider training and development as a main factor of employees' performance and productivity. This study revealed that banks' administrations interested in their productivity and efficiency is left with no other option than to adopt training and development.

5.5. Quazi Samina and Laila Zaman (2015). Cash Compensation of CEO or All Employees? Which Affect the Profitability of Private Commercial Banks' of Bangladesh.

This paper aims to examine the impact of cash compensation of CEO and all employees on banks' profitability. The study uses the Annual Reports of 10 private commercial banks of Bangladesh over the period of 2001-2013 Regression analysis is used to test hypotheses where return on equity and net interest margin are considered as dependent variable and CEO compensation, total salary expense of the bank, total assets, number of employees and number of branches are considered as independent variables.

The study found rather than CEO's cash compensation, total compensation of all the employees of the bank has statistically significant impact on banks' profitability. This study gives result based on the monetary benefits given to CEO and all employees in banks. The finding of the study is representative of the banking sector of the country which may help the policymakers to decide about the compensation package for CEO and employees of the organization.

6. Data Analysis

In this section the researchers will try to take the readers to have a simple journey with the figures, tables, and statistical analysis by considering human capital as independent variable which was measured by number of employees, branches and offices, courses and seminars, and participants in courses and seminars. On the other side, net income after tax, return on assets, and return on equity would be considered as banking financial performance.

By taking a look at figures 2, 3, and 4 we can observe the trend of net income after tax, ROA, ROE for Jordan Islamic Bank (JIB) (study sample) during 2000 – 2014.

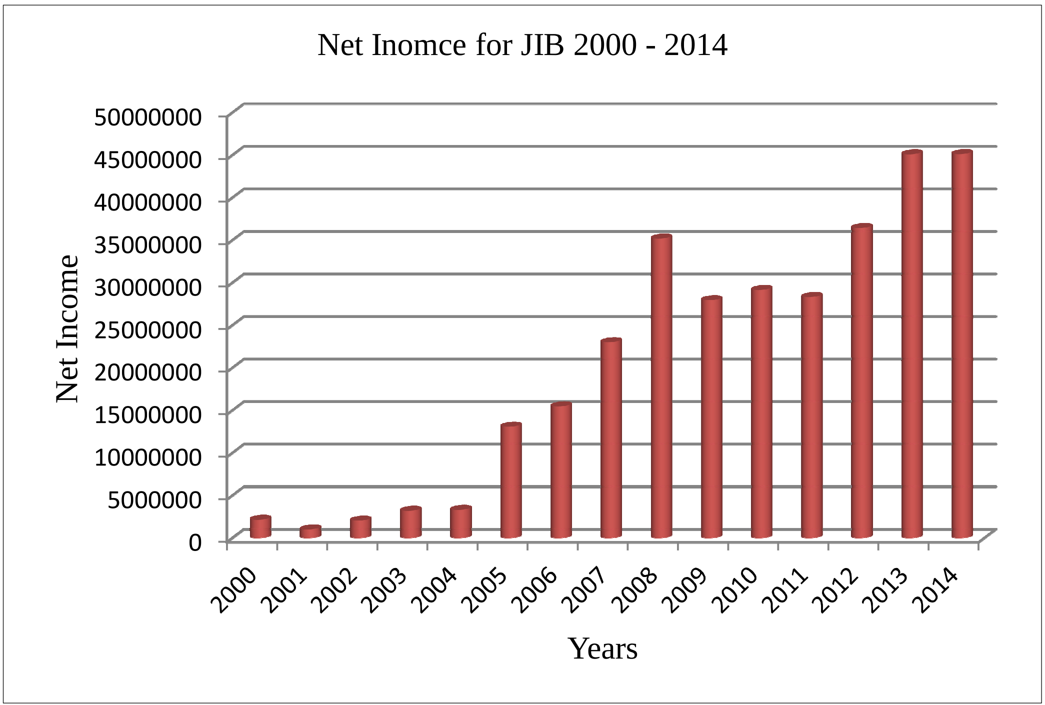

Figure (2) Net Income after Tax for Jordan Islamic Bank 2000 – 2014

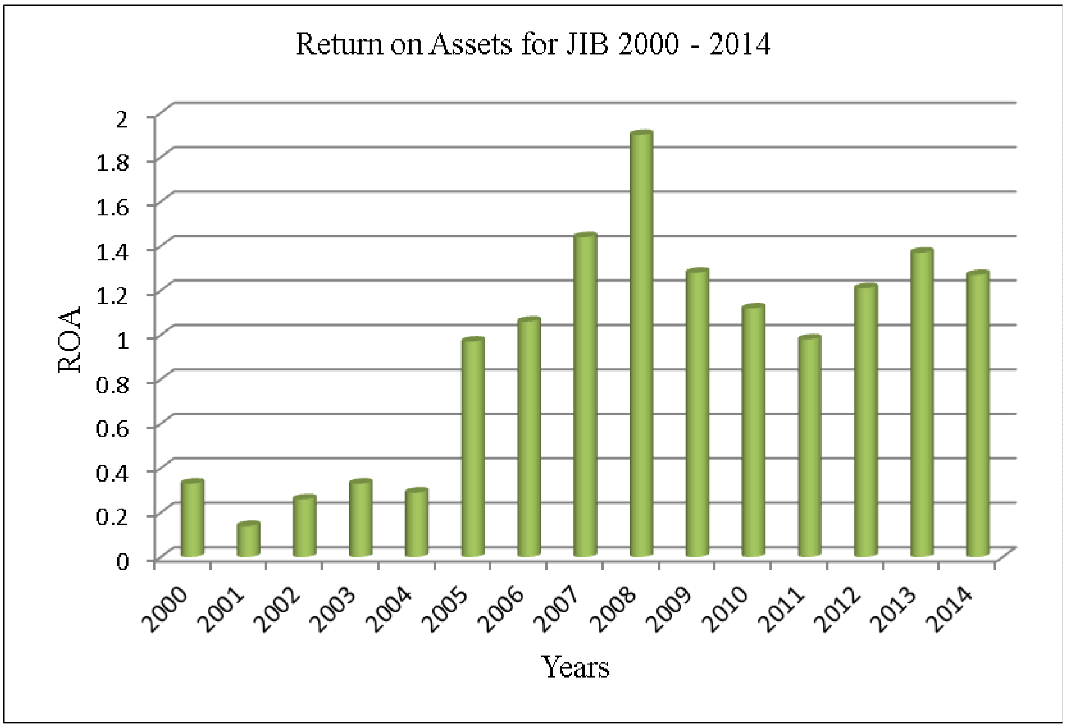

Figure (3) Return on Assets for Jordan Islamic Bank 2000 – 2014

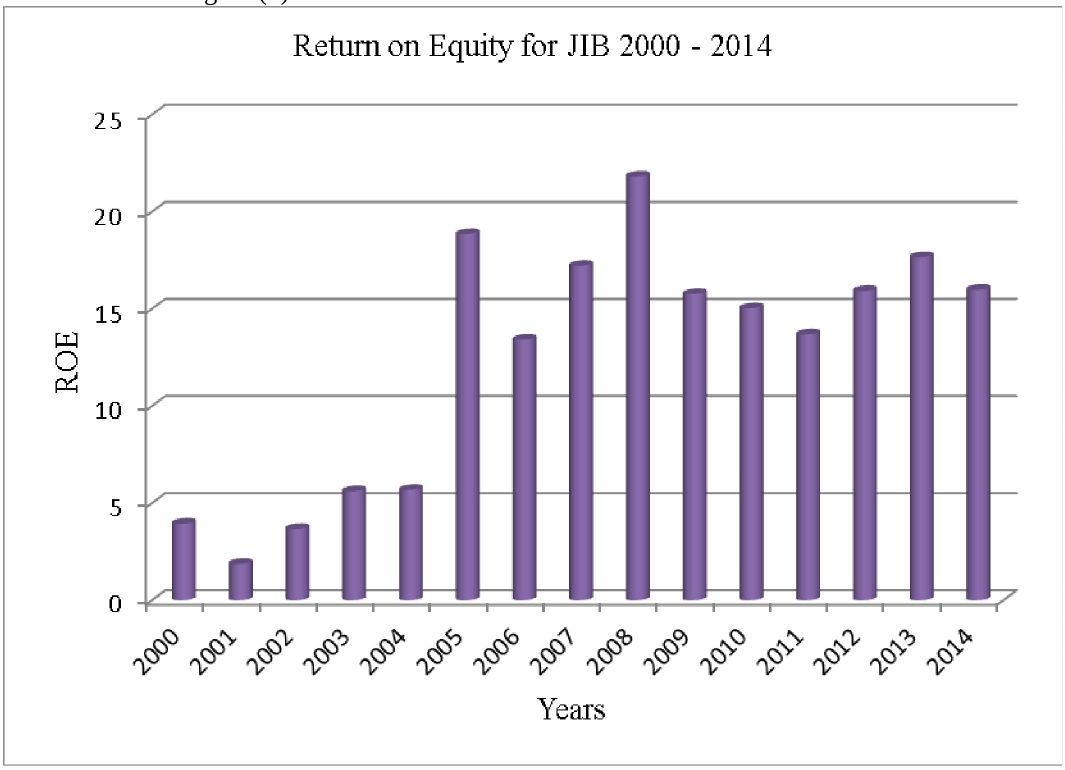

Figure (4) Return on Equity for Jordan Islamic Bank 2000 – 2014

By noticing table (1) correlation matrix for net income, we can find correlation is significant at the 0.01 level between net income and each of number of employees, branches and offices, courses and seminars, but not with the participants in these courses and seminars. Also, correlation is significant at the 0.05 level between branches and offices and number of participants in courses and seminars. For more information the reader can review table (1).

	Net Income	Employees	Branches	Courses	Participants
Net Income	1				
Employees	0.84**	1			
Branches	0.65**	0.92**	1		
Courses	0.90**	0.92**	0.78**	1	
Participants	0.23	0.44	0.51*	0.30	1

** Correlation is significant at the 0.01 level.
* Correlation is significant at the 0.05 level.

Table (1) Correlation Matrix for Net Income.

	ROA	Employees	Branches	Courses	Participants
ROA	1				
Employees	0.70**	1			
Branches	0.46*	0.92**	1		
Courses	0.80**	0.92**	0.78**	1	
Participants	0.15	0.44	0.511*	0.303	1

** Correlation is significant at the 0.01 level.
* Correlation is significant at the 0.05 level.

Table (2) Correlation Matrix for Return on Assets.

	ROE	Employees	Branches	Courses	Participants
ROE	1				
Employees	0.662**	1			
Branches	0.443*	0.92**	1		
Courses	0.749**	0.92**	0.78**	1	
Participants	0.104	0.44	0.51*	0.30	1

** Correlation is significant at the 0.01 level.
* Correlation is significant at the 0.05 level.

Table (3) Correlation Matrix for Return on Equity.

According to table (2) correlation matrix for return on assets the correlation is significant at the 0.01 level between ROA and each of number of employees, and courses and seminars. In addition, we found a correlation at a 0.05 significant level between ROA and number of branches and offices. Unfortunately, we did not find a significant correlation between ROA and number of participants in courses and seminars.

By going to table (3) the researchers reached to correlation is significant at the 0.01 level between ROE and each of number of employees, and courses and seminars. Also, correlation is significant at the 0.05 level between ROE and number of branches and offices. The correlation is not significant between ROE and number of participants in courses and seminars as well.

7. Regression Analysis

Net Income = $\beta_0 + \beta_1$ (Employees) + β_2 (Branches) + β_3 (Courses) + β_4 (Participants) + ε

ROA = $\beta_0 + \beta_1$ (Employees) + β_2 (Branches) + β_3 (Courses) + β_4 (Participants) + ε

ROE = $\beta_0 + \beta_1$ (Employees) + β_2 (Branches) + β_3 (Courses) + β_4 (Participants) + ε

When:

Dependent variable is banking financial performance which is measured by:

Net income: net income after tax.

ROA: return on assets.

ROE: return on equity.

In contrast, the independent variable is human capital which is measured by:

Employees: number of employees.

Branches: number of branches.

Courses: number of courses and seminars.

Participants: number of participants in courses and seminars.

According to the statistical analysis R square equals 0.868 which means we could explain about 86.8% of the variations in the dependent variable (banking financial performance- net income) at 1% significant level. The researchers found a positive and significant relationship between net income and number of employees, but the relationship between net income and number of branches and offices was negative and significant. Also, the researchers found the relationships between net income and each of number of courses and seminars, and number of participants in courses and seminars were not significant.

Secondly, when the researchers make the regression analysis for banking financial performance (ROA), we reached to the value of R square was 0.780 and the significance level at 1%. In addition, we found a negative and significant relationship between return on assets and number of branches & offices. On the other hand, we did not find a significant relationship between return on assets and each of number of employees, courses and seminars, and participants in courses and seminars.

Finally, according to the regression analysis for ROE, R square was 0.668 and the significance at 5% level. Unfortunately, the researchers found not significant relationships between return on equity on one hand, and every proxy of the independent variables.

8. Conclusion and Recommendations

Human capital development is one of the fundamental solutions to enter the international arena. Specifically, banks must invest necessary resources in developing human capital which tend to have a great impact on performance in general (Marimuthu, Arokiasamy, and Ismail, 2009).

Enhancing and improving employees' skills can be considered as social and economic participation in the community, and that reflects on banking profits. Banks contribute positively to the welfare of stakeholders, and improve the quality of life of the local community and society at large (Odetayo, Adeyemi, Sajuyigbe, 2014). So, we recommend that banks must make allocations to improve and train their employees.

Also, by reviewing the correlation matrix for net income, ROA, and ROE with the number of employees, we can find an improving in banking financial performance which can give an indicator about focusing on human capital for a long term that will reflect on the banks' performance. Moreover, according to the regression analysis we found a significant and positive relationship between human capital (number of employees) and net income after tax. So, that can give an indicator as well if the banks focused more on training their employees, which would increase banks' financial performance during long term. Furthermore, by taking a look at the following trends, you can observe the trend of number of employees, branches and offices, courses and seminars, and number of participants in that courses and seminars which are the proxies of human capital.

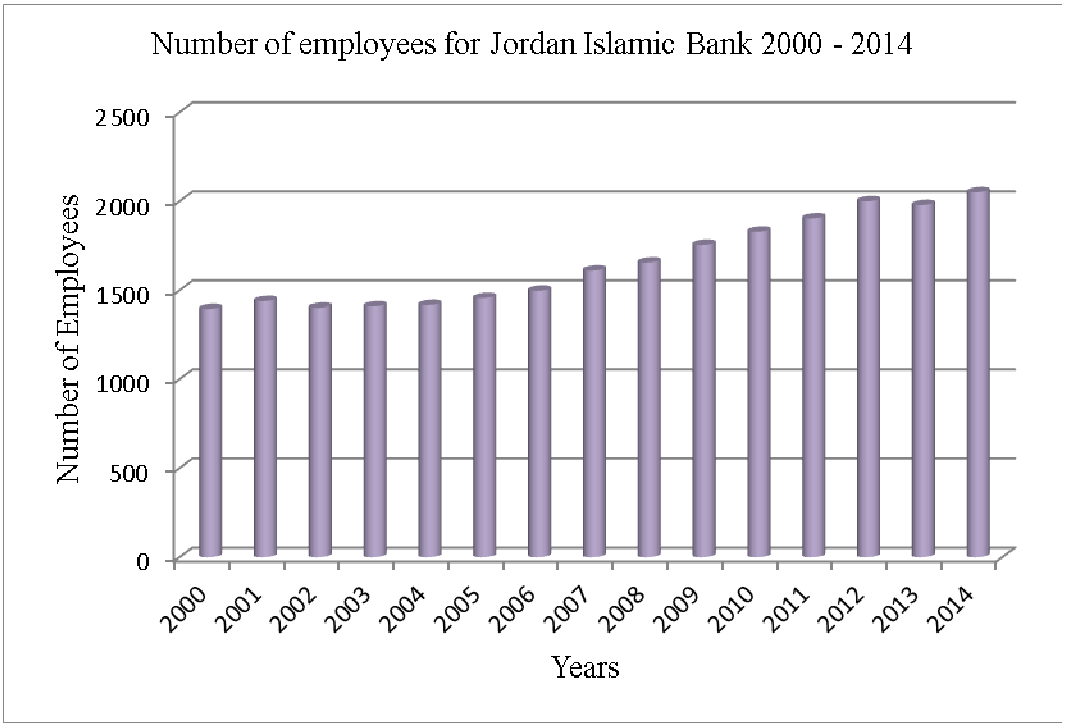

Figure (5) Number of Employees for Jordan Islamic Bank 2000 – 2014

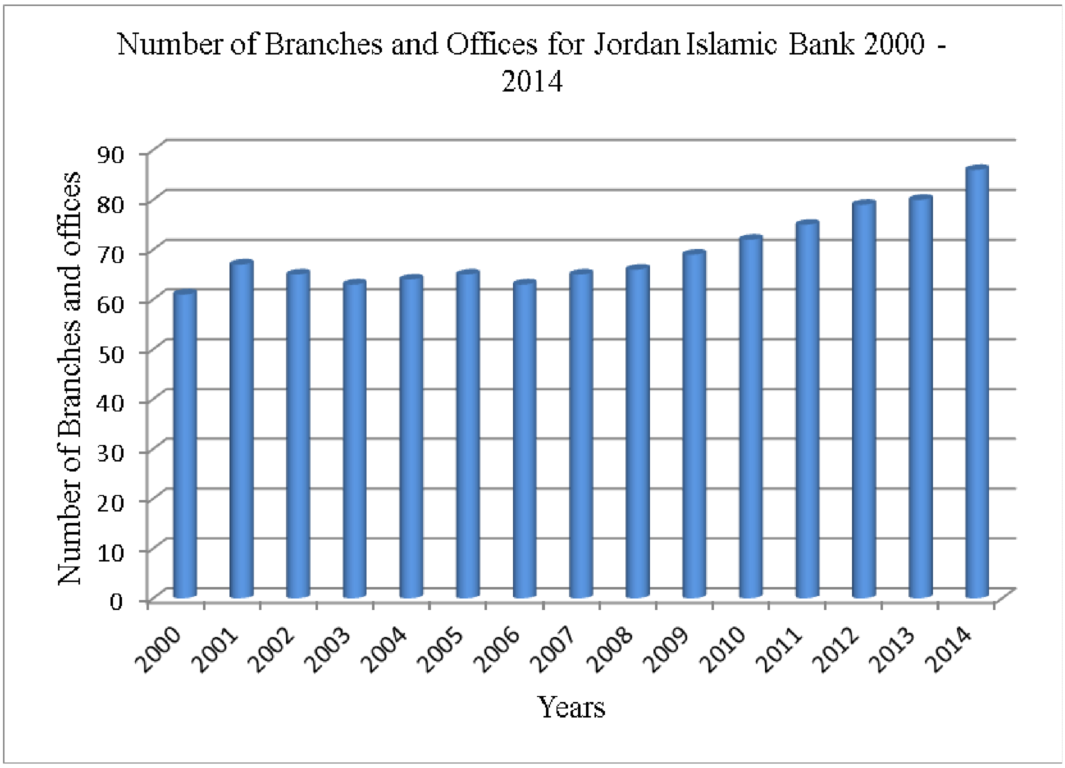

Figure (6) Number of Branches and offices for Jordan Islamic Bank 2000 – 2014

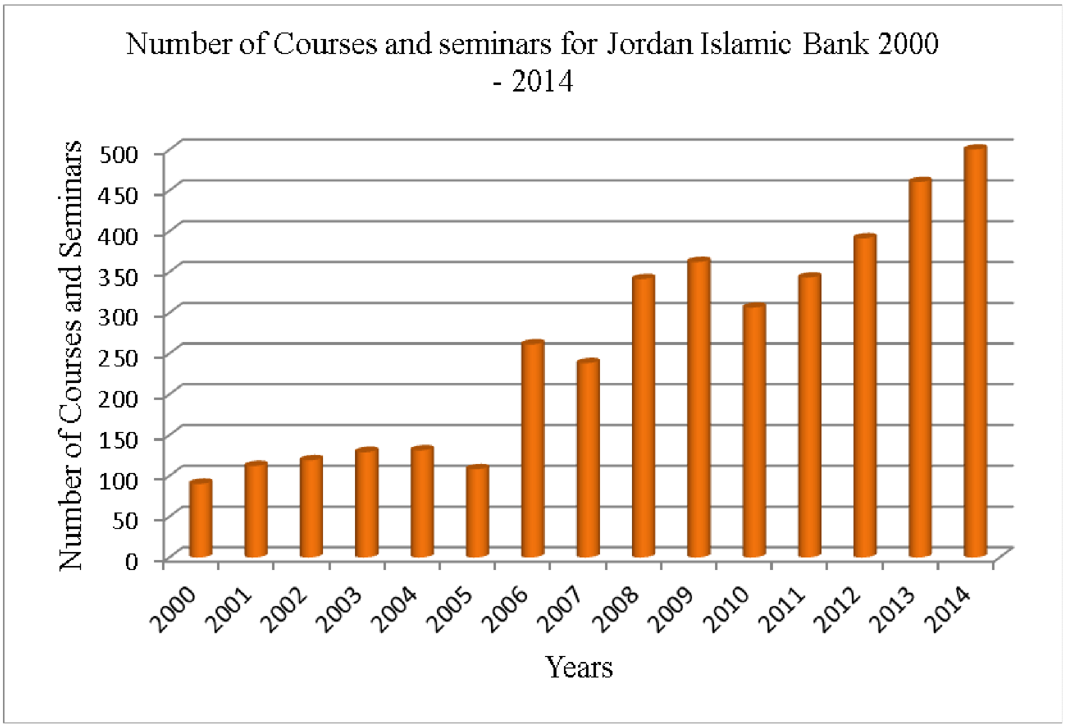

Figure (7) Number of Courses and Seminars for Jordan Islamic Bank 2000 – 2014

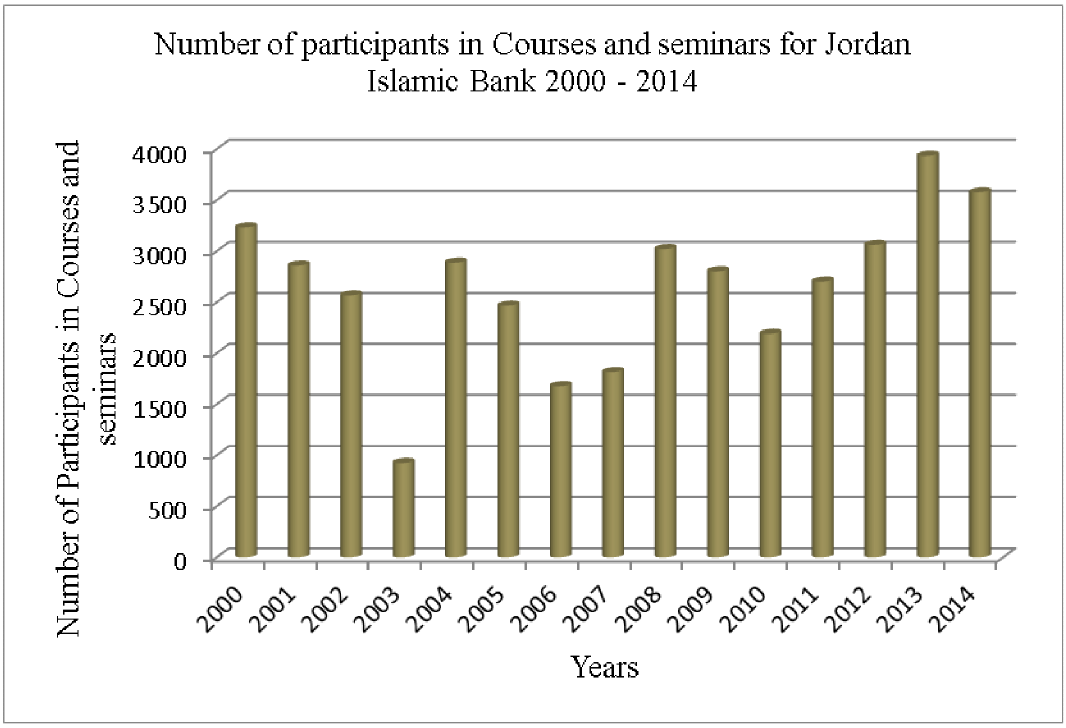

Figure (8) Number of Participants in Courses and Seminars for Jordan Islamic Bank 2000 – 2014

Finally, all financial institutions and banks should attract efficient employees and improve their employees' skills for enhancing and improving the working environment and their financial performance as well especially the banks because we consider them as the backbone for the financial system.

The researchers recommend that for future paper and research, studying the whole banking sector with increasing the period. Furthermore, we advise to focus on the financial sector and the impact of human capital on economic and social sides.

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