Inspira- Journal of Modern Management & Entrepreneurship (JMME)
ISSN : 2231–167X, Impact Factor: 5.647, Volume 10, No. 03, July, 2020, pp. 247-251

RISK MANAGEMENT OF CREDIT RISK IN BANKS

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ABSTRACT

While risk has always been a part of financial activity, the 1990's saw risk management become a key business function within banks and other financial institutions. Major reasons for its growth in importance were the large losses incurred by some huge global companies during the 1990's, which shocked financial institutions into placing more emphasis on risk management and controls. In recent decades credit risk has become pervasive. Companies borrow to create acquisitions and to grow, small business borrow to expand their capacity and individuals use credit for other purpose. At the international banking arena, there's relentless effort for creating the financial supervision extremely efficient and proactive to cope with the unprecedented and sudden risks emanated from the system. As there are increased number of innovative products within the portfolio of most of the banks, which provides them competitive edge over others, at the identical time they're facing increased level of uncertainty due to the volatility of the market. They need to strengthen internal controls, enhance disclosure and transparency of economic information and ensure effective supervision, so as to take care of the sound operation of the banking and financial markets. This includes identifying and quantifying various risks before, in addition as establishing and ending effective risk management. Basel committee has already prescribed Basel III norms, although there's a growing concern amid worldwide banking fraternity that whether the banks those are operating in a very fragile position under Basel II regime, could manage themselves to keep up the minimum Capital Adequacy Ratio (CAR, which is 2% above the previous one) and remain profitable. Most of the central banks across the nations try hard to manage their economic system during a systematic way, so as RBI just in case of India.

KEYWORDS: *Risk Management, Credit Risk Analysis, Credit management, Financial Market, Banking Structure.*

Introduction

Risk is inherent in every walk of life. Managing risks was for an extended time considered to be beyond the ability of mankind and only within the hands of the gods. The etymology of the word “Risk” are often traced to the Latin word “Rescum” meaning Risk baffled or that which cuts the risk. The general meaning of the word risk is perhaps uncertainty. The very word ‘Risk’ is related to every walk of calling. Credit risk is that the oldest style of risk that’s faced by the bankers across the world. It’s the chance of fail loans. Credit risk is that the biggest risk the bank face by the virtue of nature of business, inherits. If credit may be defined as “nothing but the expectation of a sum of cash within some limited time” then credit risk is that the possibility that this expectation won’t be fulfilled. Credit risk is old as lending. Bank shall consider the existence of the relationship between the credit risk and other risk too. In general terms if we talk the risk is commonly known and understood the level of uncertainties as connected with various outcomes of the organizations such as profits or revenue. But Mu (2007) described a very clear line of distinction between the 2 terms ‘Risk’ and ‘Uncertainty’ by means of classifying unquantifiable risk as ‘uncertainty’ and using the term ‘risk’ particularly for quantifiable risk. Risks, thus, represent ‘expected losses’. Risk emanates from the situations when both macro and micro environment is exposed to sudden shifts in policies, regulations, and systems. Risk management involves identification of the danger furthermore on evolve strategies to contain its intensity. The mechanisms of controlling risk differ from institution to institution and country to country.

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However, industry globalization and consolidation, product complexity and also the increasingly sophisticated requirements of shoppers were already resulting in a greater emphasis on ensuring that losses weren't incurred because of negative conditions of the market or failure on the part of other party or not having proper controls or people etc. Risk management is that the process of identifying ‘key‘ risk, obtaining consistent, understandable and operational risk measures, choosing which risk to cut back and which to extend and by what means and establishing procedures to observe the resulting risk position. Managing risk is that the commencement towards sustaining profitability just in case of any establishment.

Objective of Study

With the passage of time most the economies are changing at a really fast pace, so as their regulation regarding financial institutions, thereby making them more independent in deciding. The standard concept of doing business by staying under well guided regulations and stereotypical thinking now not exists, which is bringing fresh air for the market but at the identical time increases the extent of volatility. The main objective of the study is to assess the character and quantum of risks of Indian banking sector with special relation to Credit Risk. The concise objetive and purposes of the above research is:

- To look at the chance profile of Indian banking sector.
- To check asset quality of Indian banking sector over time.
- To assess the credit risk of the banks over time and also the impact of the chance on growth of Indian banking sector.
- To suggest some remedial measures for minimizing the credit risk of the banks.
- To guage credit risk management policy determines the monitoring of credit of banks.
- To judge credit risk management policy determines the credit risk models of banks.
- To look at credit risk management determines the credit limit management of banks.

Review of Litreature

Treacy and Carey (2000), found that the qualitative factors played more of a job in determining the ratings of loan to small and medium sized firms, with the loan officer chiefly to blame for ratings, in contrast to large firms within which the credit staff primarily set the ratings using quantitative methods.

Prasad and Veena (2011) has tried to determine the trends of gross and net NPA in Indian Scheduled commercial banks which they need categorized as Public sector banks, Old Private sector banks, New Private sector banks and foreign banks for the amount 2000-2010

Adem Anbar (2006) evaluates the credit risk management applications within the Turkish bank sector. His findings also indicate that banks should accelerate their studies and preparations which are associated with data about borrowers and loans that are utilized in credit risk measurement.

Kasuya (2003) in his study on NPAs of Japanese banks found that Japanese banks were also holding an oversized amount of non-performing assets within the inter-war period. The experiences of Japan within the inter-war period may provide useful lessons for the matter of today's Japanese banks. Additionally, it analyzes economic meanings of these effects. The study inferred that the prompt action in required collection and required redemption of non-performing assets may well be effective within the recovery of economic intermediation.

Chan, Greenbaum and Thakor (2004) explained the recent decline in bank asset quality using the notion of knowledge reusability. Goldstein (1996) in his study on capital norms of banking sector argued that developing countries, with few exceptions, haven't set metropolis standard much above the Basle minimum norms and their banks haven't held actual capital much above that for banks in countries with significantly more stable operating environments.

World Bank Group (2007) the study describes the most features of the provision side of SME financing by analyzing the perceptions of banks in Argentina and Chile regarding lending to SME. The study identifies that the lending practices and risk management will change substantially within the years to come back, because the involvement with SME matures.

Taori (2000) studied the management of NPA in banks and revealed that NPAs can only be controlled by preventing the possibilities of normal assets bobbing up to be NPAs. He further suggested proper risk management, strong and effective credit monitoring, co-operative working relationship between banks and borrowers as a number of the essential tenets of designing NPA management policy.

Rational Of Study

This study is a trial to know the position of Indian Banking Sector in terms of varied Risk components and also to establish the amount of risk Indian Banks are exposed to. This successively will help to measure and identify the viability of risk based methods within the wake of mounting level of NPA. There's need for special attention to risk management in modern corporate have heighten thanks to following factors

- Large corporate with over increasing hierarchy and levels of manager; therefore proper tools are essential to realize the well-liked results by covering the risks.
- Global markets became very intricate therefore the financial transactions and instruments too.
- Drastic increase within the number of international transactions (which carries its own risks).
- Dependence of latest & Emerging markets.

Research Methodology

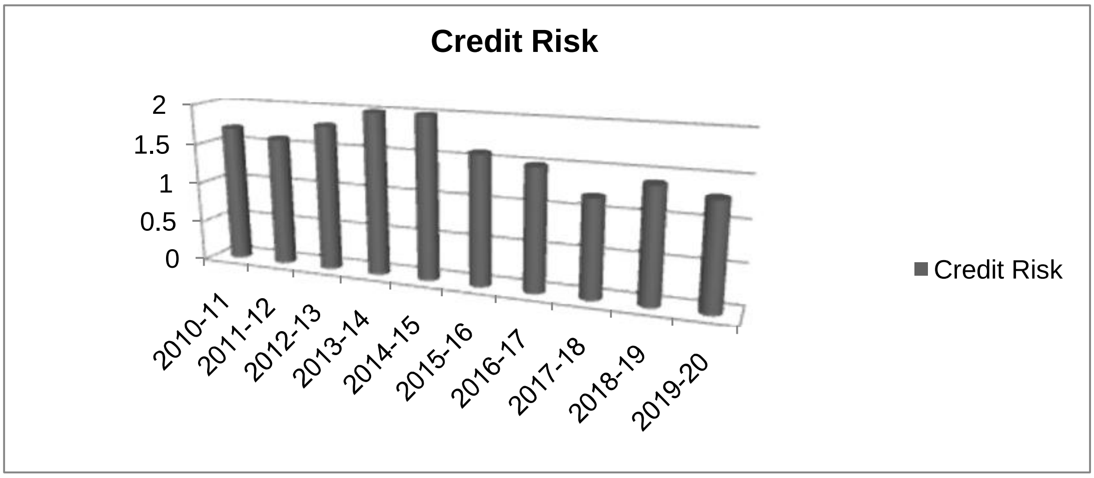
The research paper is predicated on study conducted on the Management with relevance to finance sector. For undertaking analysis of the Risk management practices in finance sector we've had personal interview and discussion round with finance professionals from various areas within finance as banking, capital market, taxation. The stress of this paper was to review the criticalness of Risk Management in current environment, its types & techniques to mitigate the adverse impact of every type. To spot the appliance of Credit risk management in banks a questionnaire as prepared to assess the banks that strictly follow credit risk management policy. For the aim of the study few banks including nationalised are considered as they found suitable for the aim of the research. The collected secondary data are going to be analyzed by both qualitative and quantitative techniques. The information collected from the reports are going to be analyzed by appropriate statistical techniques.

Results and Analysis

Table 1: Credit Risk Scores of the Banks during 2010-11 to 2019-20

Year	Credit Risk
2010-11	1.7
2011-12	1.6
2012-13	1.8
2013-14	2
2014-15	2
2015-16	1.6
2016-17	1.5
2017-18	1.2
2018-19	1.4
2019-20	1.3

Source- Researcher's own Calculation

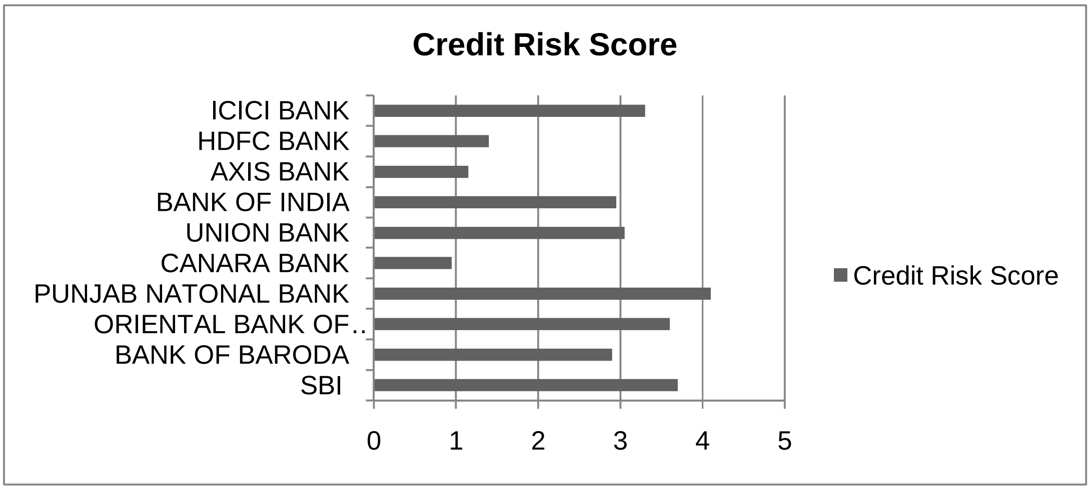


The aforesaid table reveals lowering of credit risk over the years during 2010 to 2019. Post recession, in the year 2013, again the credit risk started increasing and continued to increase till 2014, depicting the vulnerability of the banking sector. However, after that it has started again to decrease and has shown a downfall trend.

Table 2: Credit Risk Scores of the Banks

Name of Banks	Credit Risk Score
SBI	3.70
Bank of Baroda	2.90
Oriental Bank of Commerce	3.60
Punjab Natonal Bank	4.10
Canara Bank	0.95
Union Bank	3.05
Bank of India	2.95
Axis Bank	1.15
HDFC Bank	1.40
ICICI Bank	3.30

Source: Researcher's own Calculation



As we can see in the table 2 nationalised banks are having more or less nearing score as the NPA level of all these banks are quite high compared to the private players. Thus the highest credit risk score is observed in case of Punjab National Bank, followed by SBI and Oriental bank of Commerce. Whereas lowest credit score is observed in case of CANARA Bank. Banks like Bank of Baroda, Union Bank and CANARA Bank are also showing higher scores of credit risk. In the category of private sector banks, ICICI bank is having the highest credit risk score, due to accumulation of more toxic assets. These scores indicate the need for taming the unbridled growth of credit risk in public sector banks of India. This indicates that since credit risk is showing a zigzag trend and not at all stable in either side. The trend which do not indicates a consistent approach, is a clear indication of lower risk management on the part of the Banks. This has to be any how need a proper system of Credit Management.

Conclusion and Suggestions

For any business to grow and stay within the market, management style could be a key and Risk management is essentially the management sort of managing the risks. Risk is inherent in every business and each organization should manage it in line with its size and nature of operation because without it no organization can survive in long term. Additionally thereto the quantum of risk is higher in finance sector than the other sector. Indian banks have gone an extended way in adopting credit risk management policy and procedures as stated by the BASEL. Since exposure to credit risk continues to be the leading source of problems in banks world-wide, banks and their supervisors should be ready to draw useful lessons from past experiences. Banks should now have a keen awareness of the requirement to spot, measure, monitor and control credit risk likewise on determine that they hold adequate capital against these risks which they're adequately compensated for risks incurred. The above research confirms implementation of the credit risk management policy by the Banks. The necessity for the banks is to implement a robust credit risk models in banks to avoid loan defaulters. If banks will implement better credit risk models to spot the status of the borrowers they're going to be removed from the particular credit risk. Banks have to foresee not only in implementation of regulatory framework but risk models to avoid risk.

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