A Systematic Study on Credit risk management policies and practices with special reference to Cooperative banks of Bangalore City

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***Abstract*- Credit risk is the risk of loss when a borrower fails to meet his contractual obligation to repay the debt in accordance with the agreed terms. The effective management of credit risk is crucial for the long term success of any financial organisation and it is a critical component of a comprehensive approach to risk management. Credit risk management any financial organisation plays vital role in maximizing risk-adjusted rate of return and it also helps to maintain the credit risk exposure within acceptable parameters. Reserve Bank of India (RBI), the regulatory body of all types of banks in India, has insisted Non-Banking Financial Corporations to devise a risk management framework, based on their requirements, which is dependent size, complexity of business, risk philosophy, marketing perception, risk aversion mentality etc. Accordingly the credit risk management Policy of TFCI encompasses identification of risks, evaluation, monitoring and mitigation of credit risks in compliance with the norms laid down by RBI.**

***Keywords*- Credit risk, Cooperative Bank, financial corporation, RBI**

I. INTRODUCTION

Credit risk is the risk of loss when a borrower fails to meet his contractual obligation to repay the debt in accordance with the agreed terms. The effective management of credit risk is crucial for the long term success of any financial organisation and it is a critical component of a comprehensive approach to risk management. Credit risk management any financial organisation plays vital role in maximizing risk-adjusted rate of return and it also helps to maintain the credit risk exposure within acceptable parameters. Reserve Bank of India (RBI), the regulatory body of all types of banks in India, has insisted Non-Banking Financial Corporations to devise a risk management framework, based on their requirements, which is dependent size, complexity of business, risk philosophy, marketing perception, risk aversion mentality etc. Accordingly the credit risk management Policy of TFCI encompasses identification of risks, evaluation, monitoring and mitigation of credit risks in compliance with the norms laid down by RBI.

II. REVIEW OF LITERATURE

Commercial banking plays a vital role in any economy, as commercial lending happens majorly through commercial banking (Allen & Gale, 2004). In the modern banking world, commercial banks have forayed into investment banking activities too by providing new forms of debt to their customers (Gande, 2008). The credit creation happens when funds are transferred from savers of the fund to seeker of the funds (Bernanke, 1993). There are many potential sources of risk, credit risk, market risk, currency risk, technology risk, interest rate risk and political risks (Campbell, 2007). But, Credit risk is the biggest risk of any financial organisation which is into lending business (Gray, Cassidy, & RBA., 1997). Credit risk can be indicated by the parameters like the quantity of Non-Performing Assets and/or provision for losses (Jiménez &Saurina, 2006). Credit risk is basically a non-receipt of loans either partially or fully on time, which is granted by a bank (Campbell, 2007). It can also be breach of financial contract by counter party or customer (Gray, et al., 1997).

Prior to deregulation of financial sector, banks were granting credit facility to any client who could express properly their creditworthiness (Bryant, 1999). After the deregulation, banks were able to find the wide range of borrowers who could meet their demands. At the same time, banks were too cautious to extend their credit because of the large mounted bad loans and advances of boom in 1980’s but subsequent failure to sustain the high growth of credit (Boyd, 1993; Bryant, 1999).

Credit risk management mainly focusses on establishing system/well laid down procedure for approving new credit and as extension of existing credit facility to its customers. These procedures also include risk monitoring with utmost care and other necessary steps to control the risk and mitigate the risk of connected lending as well (Basel, 1999).

A bank must have well laid down procedure and control systems for assessing the loan application, which will scrutiny the applications at the initial stage itself and ensure the quality of banks total loan portfolio as per its integrity (Boyd, 1993). Credit risk management encompasses the sound credit granting processes, proper credit administration, risk measurement, risk monitoring and control over credit risk which clearly defines the scope and allocation of its credit facilities as well as the way in which the overall credit portfolio of a bank is managed. Credit risk management will ensure the control checks at every step of loan origination, appraisal, how it is supervised, collected, disbursed and followed (Basel, 1999).

The important factors of credit risk management are credit scoring procedures, the probability of happening of negative events and the consequent losses arising out of these events, all the parameters should be carefully implemented (Altman, Caouette, & Narayanan, 1998). Some of the studies are of the opinion that it is more important to develop a sound risk management strategy for any organisation rather than expecting a strong regulatory and legal framework for the prevention and control of these losses. Because of the nature, size and complexity might vary from organisation to organisation which is case, a better risk management will benefit the organisation more than the controlled framework form external forces. (Campbell, 2007).

III. OBJECTIVES OF THE STUDY

• To identify the parameters constituting the aspects of “Credit Risk Management Policies and Practices”.
• To assess the association between personal profile of respondents and parameters of credit risk management policies and practices.
• To ascertain the relationship between dimension of credit risk management policies / practices and influencing factors.
• To percolate the preferences of credit risk management policies / practices while considering the aspect of implementation at bank level.

Research Methodology

The research design for the current study is descriptive in nature as the information been collated is concerned with current phenomena of credit risk management practices been followed at various cooperative banks of Bangalore city. The respondents for the study are the managers or senior employees working in cooperative banks. Responses have been collected using a structured questionnaire through scheduling technique from a sample of fifty respondents. In-order to assess the internal consistence of the questionnaire test of reliability is been computed. Going ahead to assess the difference in mean scores over the aspect of credit risk management policies and practices, T-test and one-way analysis of variance has been carried out. Lastly to assess the relationship between dimension of credit risk management policies / practices as whole and influencing factors, correlation analysis has been computed.

Data Analysis

The analysis has been segregated into two major heads being descriptive and inferential. Test of data duplication and reliability assessment if items deleted is been calculated to understand the internal consistence of the questionnaire.

Table 1: Data duplication

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Primary Case	50	100.0	100.0	100.0

Source: Computation of analysis bases collected data

Test of reliability has been carried out using SPSS version 23 and identified that the Cronbach's alpha on the items in the questionnaire is 0.815. This signifies that the items in the questionnaire are closely related as a group.

Table 2: Reliability Analysis

Cronbach's Alpha	N of Items
.815	87

Source: Computation of analysis bases collected data

The respondents for the study based on their educational qualification have been segregated in two groups being: Under Graduate and Post Graduate. To assess the difference in mean scores of the respondents based on their educational qualification on the aspect of credit risk management policies and practices, T-test is been computed

IV. RESEARCH HYPOTHESIS

H_0: There is no difference in mean scores of respondent's personal profile on parameters of credit risk management policies and practices

H_1: There is difference in mean scores of respondent's personal profile on parameters of credit risk management policies and practices

A. T-test to assess the difference in mean scores of respondent's educational qualification on parameters of credit risk management policies and practices

H0: There is no difference in the mean scores of respondent's education on credit risk management policies and practices

H1: There is difference in the mean scores of respondent's education on credit risk management policies and practices

Table 3: Independent Samples Test

	Levene's Test for Equality of Variances	t-test for Equality of Means

		F	Sig.	T	Df	Sig. (2-tailed)	Mean Difference	Std. Error Difference	95% Confidence Interval of the Difference	
									Lower	Upper
CRM	Equal variances assumed	1.225	.274	.076	48	.940	.481	6.339	-12.265	13.227
	Equal variances not assumed			.075	45.610	.940	.481	6.378	-12.360	13.322

Source: Computation of analysis bases collected data

The p value for Levene's Test is observed to be 0.274 being more than 0.05 level of significance. This indicates that there is equal variance been assumed within the groups of educational qualification. As a result the p value of 0.076 is been considered which is observed to be more than 0.05 level of significance. Hence the null hypothesis is failed to be rejected, which specifies that the responses towards the aspect of credit risk management policies and practices are uniform in-spite of the differences in educational qualification.

B. ANOVA test to assess the difference in mean scores of respondent's depending upon bank location on credit risk management policies and practices

H0: There is no difference in the mean scores of bank location on credit risk management policies and practices

H1: There is difference in the mean scores of bank location on credit risk management policies and practices

Table 4: One Way Analysis of Variance

	Sum of Squares	Df	Mean Square	F	Sig.
Between Groups	809.787	2	404.893	.818	.448
Within Groups	23266.713	47	495.036		
Total	24076.500	49			

Source: Computation of analysis bases collected data

It is been identified that the responses towards the dimension of credit risk management policies and practices is uniform in-spite of the respondents being different in terms of the location of work. The p value for one way analysis of variance is observed to be more than 0.05 level of significance being 0.448, which results in failing to reject the null hypothesis.

C. ANOVA test to assess difference in the mean scores of number of employees working in the bank on credit risk management policies and practices

H0: There is no difference in the mean scores of number of bank employees on credit risk management policies and practices

H1: There is difference in the mean scores of number of bank employees on credit risk management policies and practices

Table 5: One Way Analysis of Variance

	Sum of Squares	Df	Mean Square	F	Sig.

Between Groups	179.693	2	89.847	.177	.839
Within Groups	23896.807	47	508.443		
Total	24076.500	49			

Source: Computation of analysis bases collected data

Number of employees working in the bank is been segregated in five different categories being: 5-8, 9-12, 13-16, 17-20, and Above 21. The significance value is identified to be more than 0.05 level of significance being 0.839. Therefore the null hypothesis is failed to be rejected which specifies that in-spite of the respondents being different in number of employees working for the organization their responses towards the aspect of credit risk management policies and practices is uniform.

D. Correlation analysis between dimension of credit risk management policies / practices as whole and influencing factors

H_0: There is no relationship between dimension of credit risk management policies / practices as whole and influencing factors
H_1: There is relationship between credit risk management policies / practices and as whole and influencing factors

Table 6: Correlation Analysis

		CRM	IF
CRM	Pearson Correlation	1	.714**
	Sig. (2-tailed)		.000
	N	50	50
IF	Pearson Correlation	.714**	1
	Sig. (2-tailed)	.000	
	N	50	50

**. Correlation is significant at the 0.01 level (2-tailed).

Source: Computation of analysis bases collected data

The correlation analysis between the dimension of credit risk management policies / practices and as whole and influencing factors indicate strong and positive correlation of 0.714 being highly statistically significant at 0.01 level of significance. Therefore credit risk management policies / practices have strong impact on influencing factors.

V. FINDINGSAND SUGGESTIONS OF THE STUDY

- The below mentioned parameters are considered as the most predominant factors that are acting as key enabler for banks in attaining enhanced overall process of banking, reduction of nonperforming assets (NPA) and attainment of sustainability overall organization sustainability being: We have credit risk policy committee in our bank, We have credit counseling cell in our bank, We have credit audit committee in our bank, We have credit data management cell in our bank, We have a specialised credit risk officer in the Finance, economics orExperienced banker, We have separate credit administration process to manage the credit risk in our bank, We have specialised unit in the bank to manage the problem credit account, In our bank the training is provided to the credit risk officers on regular basis, The delegation of credit approval authority is based on the total number of experience of the employee, The delegation of credit approval authority is based on the professional qualification of the employee, The delegation of credit approval authority is based on the risk rating assign to borrower account,

- The delegation of credit approval authority is based on the amount of credit facility or transaction, We have independent credit risk inspection Group to conduct periodic inspection of credit portfolio, We have credit risk management policy in our bank, The CRM policies are predominantly defined on size of advance portfolio, The CRM policies are predominantly defined on Market share value, The CRM policies are predominantly defined on Optimizing share value, The CRM policies are predominantly defined on Total acceptable risk at portfolio level, The CRM policies are predominantly defined on Different interest rate or risk premium, We have organisational unit is responsible for framing the CRM policy, We have defined the credit risk management with well documented form, We have review the CRM policy in our bank, The CRM policies are reviewed quarterly in our organization, The CRM policies are reviewed yearly in our organization, The CRM policies are reviewed in our organization when time persist, We have updating the CRM policy, Credit risk management policy defined the target markets and business sector, Credit risk management policy defined the cost of funds relevant for credit decision, Credit risk management policy defined preference level of diversification and concentration of advances, We have set the maximum exposure limits to each borrowers, The credit exposure norms in our bank is defined based on the total deposits, The credit exposure norms in our bank is defined based on total assets, The credit exposure norms in our bank is defined based on risk weighted assets capital, The credit exposure norms in our bank is defined based on both RWA and capital,The credit exposure norms in our bank is defined based on both total assets and capital, Our bank is member of credit information Bureau of India (CIBIL), We have concentration credit exposure limits fixed, Our bank have set the credit exposure limits fixed on the bases of cost of fund, We set the CRM policy of single borrowers exposure limits, We set the CRM policy by fixing the group of borrower's limits, We set the CRM policy to the priority sector exposure norms, We set the weaker sector exposure norms, Our banks fix the exposure limits to single borrowers up to a limit funds on capital, Our banks fix the exposure limits to single borrowers up to a limit working capital on capital, Our banks fix the exposure limits to group of borrowers up to a limit funds on capital, Our banks fix the exposure limits to group of borrowers up to a limit working capital on capital, Our banks fix the exposure limits to priority and weaker sector limits, Our staff quickly identify the breach in credit limits on real time bases, Our staff quickly identify the breach in credit limits on over night bases, Our staff quickly identify the breach in credit limits on longer than overnight bases, Our banks pricing the credit on the basis of Cost of funds,

- Our banks pricing the credit on the basis of Price quoted by the competitors, Our banks pricing the credit on the basis of Market conditions, Our banks pricing the credit on the basis of Future business potential, Our banks pricing the credit on the basis of RAROC (Risk adjusted return on capital), Our banks pricing the credit on the basis of Value of collateral, Parameters confining dimension of Credit risk Management practices, We have apply KYC norms while introducing the customers, In our bank we have introduced the customers as a registered members, In our bank we have introduced the customers by existing customers, In our bank we have introduced the customers by employees or offices, In our bank we have introduced the customers by local people, We have upto 5 years experienced credit risk officers in our bank, We have upto 10 years experienced credit risk officers in our bank, We have upto 15 years experienced credit risk officers in our bank, We have upto 20 years experienced credit risk officers in our bank, We have provide the delegation of power to individual branch managers, We have internally audited the bank branches, Our bank is externally audited by the chartered accountant appointed by the bank, Our bank is collect the proper documents while approving the credit, Our bank is collect the collateral security from small borrowers, Credit riskmodel is used by our bank, Our bank has monitoring and follow up to recover the credit through sending reminders, Our bank has monitoring and follow up to recover the credit through counseling, Our bank has monitoring and follow up to recover the credit through visiting unit by the bank staff, Our bank has monitoring and follow up to recover the credit through providing incentives, Our bank has monitoring and follow up to recover the credit through early repayment option, Our bank has option of filling suits to recover the credit, Our bank has option of restricting rescheduling compromise to recover the credit, Our bank has option of securitization notice to recover the credit, Our bank has option of seize of assets (SURFAESI)/KCS to recover the credit, Political interference are the major reasons for credit default, Wilful default are the major reasons for credit default, Diversion of funds are the major reasons for credit default, Lack of legal support are the major reasons for credit default, Deficiency in the credit appraisal standards are the major reasons for credit default, Lack of supervision and follow up are the major reasons for credit default and High rate of interest are the major reasons for credit default.

VI. CONCLUSION

Co-operative banks in India are undoubtedly one of the most predominant source of finances to Indians. However in recent past, few of the representatives from the cult have left undermining bitter instances by involving themselves in unconventional financial practices. Such instances are hampering the well-being of the sector and the banks are paving hard to establish their footholds by offering multidimensional avenues to its customers. In-order to sustain, the banks are undertaking strong decisions in terms of lending and borrowing of funds. Such decisions are keeping them exposed to the aspect of "Credit risk". In connection to this RBI has facilitated banks the policies and practices pertaining to Credit risk management. The current study makes an attempt in understanding the various parameters that will mitigate the uncertainties of credit risks.

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