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IMPACT OF CREDIT RISK MANAGEMENT ON PERFORMANCE OF BANKS

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ABSTRACT: The meaning of the risk varies depending on the situation and its application., From one point of view, “risk” refers to issues in the future that can be avoided or mitigated rather than issues in the present that need to be addressed right away. While risk is present in all aspects of life, it is particularly significant in the financial sector., Literature on risk demonstrates that banks could not afford to take risks because of the regulated environment., However, over the past two decades, banks have consistently been confronted with a variety of risks that have the potential to harm their operations., These, chances, to, which, banks, are, uncovered, to, be, market, risk,, functional, risk,, credit, hazard, and, liquidity, risk., Out, of, them,, the, credit, risk, is, most, basic, for, the, endurance, of, the, banks, as, it, is, straightforwardly, connected, to, the, major, as, indeed, as, the, essential, action, of, banks, i.e.,, loaning, assets, to, the, borrowers, as, cash, or, other, instruments., The study aims to identify the various parameters underlying the concept of credit risk management in banks because of its critical importance., Additionally, the study aims to investigate the effect that various credit risk parameters have on bank efficiency., The research makes use of secondary data gathered from various data sources regarding credit risk management and the various institutions that facilitate risk management in banks.

Keywords: credit, risk, financial, sector, risk, management, bank, performance

Introduction:

The concept of risk varies depending on the environment in which it operates., A risk is a possibility or a threat of harm, injury, liability, loss, or any other negative occurrence that can be avoided by taking preventative action and is caused by internal or external vulnerabilities. Risk is inherent in every aspect of life, both generally and specifically in the financial sector., In, finance, risk, is, the, likelihood, that, an, genuine, return, on, an, venture, will, be, lower, than, the, normal, return., Risk, at, the, peak, level, may, be, pictured, as, the, likelihood, of, a, banks’, monetary, wellbeing, being, disabled, due, to, at least one, contingent, factors., Banks were unable to take risks until recently because of environmental regulations., A bank is both a financial institution and a financial intermediary that accepts deposits and directs those deposits into lending activities, either directly through lending or indirectly through capital markets. In, doing, their, organizations, banks, are, frequently, confronted, with, a, twofold, edged, blade, of, risk, and, returns, and, they, have, to, balance, the, two, in, request, to, get by, and, produce, benefits., When the concept of risk management is applied to the banking industry, banks are invariably confronted with a variety of risks that have the potential to harm their operations. According to guidelines issued in October 1999 by the Reserve Bank of India, the major financial and non-financial risks that the banking sector faces are market risk, operational risk, credit risk, and liquidity risk. The possibility of losses associated with a decrease in the credit quality of borrowers or counterparties is referred to as credit risk., The outright default of a customer or counterparty in relation to commitments in relation to lending, trading, settlement, and other financial transactions is the source of losses in a bank's portfolio., The risk of loss arising from a debtor's failure to pay back a loan or other line of credit (either the principal or interest (coupon), or both) is known as credit risk. A borrower's bankruptcy, a delay in repayments, and a restructuring of repayments are all examples of events that constitute default.

Credit, risk, is, most, basic, for, the, endurance, of, the, banks, as, it, is, straightforwardly, connected, to, the, major, as, indeed, as, the, essential, action, of, banks, i.e.,, loaning, assets, to, the, borrowers, as, cash, or, other, instruments., Due to the recent global economic meltdown brought on by the subprime mortgage crisis in the United States in July 2007 and its negative impact on financial markets, the significance of credit risk came to the forefront. Since, openness, to, credit, risk, proceeds, to, be, the, main, source, of, issues, in, banks, world-, wide,, banks, and, their, bosses, are, expected, to, be, capable, to, draw, valuable, examples, from, past, encounters., Banks, ought to, presently, have, a, sharp, mindfulness, of, the, need, to, distinguish, measure,, screen, and, control, acknowledge, risk, as, indeed, as, to, decide, that, they, hold, sufficient, capital, against, these, dangers, and, that, they, are, enough, redressed, for, chances, caused, (Basel,, 1999), [3]., Because credit risk is a part of their business, banks need to be prepared to deal with it. Credit, Hazard, the executives, is, the, human, action, which, incorporates, acknowledgment, of, risk,, risk, appraisal,, creating, procedures, to, make due, it,, and, alleviation, of, risk, utilizing, administrative, assets., Credit, risk, the executives, is, extremely, significant, to, banks, as, it, is, an, fundamental, part, of, the, advance, process., Failures in the financial sector and weaknesses in the banking sector in recent years have prompted policymakers to develop prudent risk management mechanisms., Against, this, setting,, Basel, Capital, Ampleness, standards,, initially, imagined, during, 1988,, brought, about, wide, arrangement, among, G-10, focal, banks, for, applying, Normal, Least, Capital, Principles, to, their, banking, enterprises., These standards are intended to promote banking safety and soundness by leveling the playing field for all banks in terms of capital sufficiency. RBI issued guidelines on credit risk management on October 12, 2002, keeping in mind the seriousness of credit risk and the need to appropriately manage it., These, rules, engaged, that, the, banks, ought to, give, credit, risk, prime, consideration, and, ought to, put, set up, a, advance, strategy, to, be, cleared, by, their, sheets, that, covers,

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the, technique, for, estimation,, checking , and control, of, credit, risk., The, major, issue, previously, the, banks, right now, is, to, distinguish, measure,, make due, and, carry out, the, strategies, in, request, to, decrease, risk, and, consent, with, the, mandates, and, at, the, same, time, be, capable, to, keep, a, balance, between, the, productive, speculation, potential open doors, and, the, capital, sufficiency., Additionally, the, banks, have, to, give, exceptional, treatment, to, the, credit, risk, the executives, in light of the fact that, of, its, immediate, bearing, on, its, monetary, execution, and, productivity.

REVIEW OF LITERATURE:

Most, current, credit, demonstrating, structure, set up, is, Basel, II, Accord., This agreement has positively contributed to the drive toward developing credit risk modeling and capital adequacy requirements that are applicable., Nonetheless,, for, these, exercises,, banks, must, have, a decent, information, about, risk, the executives,, evaluating, of, credit, on, cutthroat, market,, negligible, risk, changed, commitment,, observing, of, financial, capital, **(Cuthberston, and, Nietzsche,, 2003),** [12]., Poor lending practices frequently affect the banks **(Koford, & Tschoegl, 1999,** [23])., Hence, checking,, and, other, proper, steps,, are, fundamental, to, control, or, alleviate, the, risk, of, associated, loaning, when, it, goes, to, organizations, or, people, (Basel,, 1999), [3]., RBI issued guidelines on credit risk management on October 12, 2002, keeping in mind the seriousness of credit risk and the need to appropriately manage it., These guidelines emphasize that banks should prioritize credit risk and implement a loan policy that covers the methodology for measuring, monitoring, and controlling credit risk and must be approved by their boards. A, legitimate, approach, to, risk, recognizable proof,, estimation, and, control, will, shield, the, interests, of, banking, organization, in, long, run., Froot and Stein (1998), [15] discovered that banks' investments in risky loans are affected by credit risk management through active loan purchase and sales activity. Banks, that, buy, and, sell, credits, hold, more, hazardous, advances, (Credit, Chance, and, Misfortune, advances, and, business, genuine, domain, credits), as, a, rate, of, the, balance, sheet, than, other, banks., Again, these results stand out because banks that manage their credit risk (by buying and selling loans) hold more risky loans than banks that simply buy loans (but don't sell them), or banks that simply sell loans (but don't buy them). Treacy, and, Carey, (1998), [30], analyzed, the, credit, risk, rating, component, at, US, Banks., They, featured, the, engineering, of, Bank, Inside, Rating, Framework, and, Working, Plan, of, rating, framework, and, made, a, examination, of, bank, framework, relative, to, the, rating, organization, framework., They came to the conclusion that the internal rating system of banks aids in credit risk management, profitability analysis, and product pricing., According to Ferguson's (2001) [13] analysis of credit risk management models and judgments, proper risk modeling provides firms with a formal, systematic, and disciplined way to measure changes in the riskiness of their portfolio and aids them in designing the appropriate strategic framework for managing changes in their risk. The goals and factors that determine the direction of a bank's policies on credit risk management were emphasized by Muninarayanappa and Nirmala (2004), [26]. They came to the conclusion that the proper credit risk environment, credit strategy, and policies are necessary for the success of credit risk management. Additionally, they observed that proper credit risk management is essential to banks' survival., According to Campbell (2007) [7], there are numerous potential risk sources, such as credit, interest rate, market, foreign exchange, and political risks. Gray and others (1997), [19], finished up, that, out, of, in this way, many, chances,, credit, risk, is, the, greatest, risk, confronted, by, banks, and, monetary, middle people., Financial distress and bank failures have afflicted numerous banks, many of which have been closed down by regulatory authorities (Brown bridge and Harvey, 1998) [5]. Credit risk management weakness has long been cited as the primary cause of bank problems, among other factors (Chijoriga, 1997; Richard et al., 1998). 2008), [9,, 10,, 29]. Accordingly, there, are, many, perspectives, in, which, credit, risk, and, its, the board, is, related, with, the, proficiency, of, banks., These, viewpoints, have, been, fantastically, broke down, by, Berger, et, al., (1997), who, found, that, there, is, a, negative, relationship, among, proficiency, and, chance, in, fizzled, banks., The, achievement, of, banks, business, depends, on, exact, estimation, and, proficient, the board, of, credit, risk, to, a, more noteworthy, degree, than, any, different dangers, (Gieseche,, 2004), [16]., In order to provide a framework for comprehending the impact of credit risk management on banks' profitability, it was even discovered that credit risk management maximizes the risk adjusted rate of return of a bank by Maintaining credit risk exposure within acceptable limits (Kargi, 2011).

NEED OF THE STUDY:

Based on the review of previous studies, it has been determined that banks should place credit risk management at the center of their operations in order to maintain financial sustainability and reach more customers. The literature demonstrates that the majority of studies in the field focused on developing a conceptual framework for credit risk management., Be that as it may, some, of, the, explores, have, likewise, been, directed, on, distinguishing, the, impact, of, credit, risk, the board, on, banks, yet, exceptionally, few, explores, engaged, on, investigating, the, relationship, between, credit, chance, the executives, and, proficiency, in, banks., Additionally, the majority of these studies have been carried out in other regions of the globe., This, makes, a, hole, and, opportunity, to, investigate, this, undiscovered, region, of, research., Hence, the, present, study, points, at, tending to, this, hole, and, understanding, the, influence, of, credit, risk, the executives, on, productivity, of, banks., The, proposed, paper, will, survey, the, complexities, of, credit, risk the executives, in, banking, area, by and large, and, its, connection, to, the, bank, execution.

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OBJECTIVES OF THE STUDY:

The following objectives have been set for the study:

•To, break down, the, relationship, between, credit, hazard, the board, and, bank, proficiency.
•To investigate the impact of credit risk management on the performance of the bank in terms of profitabilitability.

METHODOLOGY AND DATA COLLECTION:

The, study, is, observational, in, nature, based, on, optional, information., HDFC, Bank, has, been, chose, for, the, study, as, it, is, the, spearheading, private, area, bank, in, India., The research was carried out over a ten-year period, from 2006-2007 to 2015-2016., The selected bank's information was derived from its annual reports, financial statements, and Basel III disclosures., The various variables that have been taken for the purpose of the study include the capital adequacy ratio, net non-performing assets, and net NPA ratio (i.e., percentage of net NPA to net advances) for studying credit risk management. Profit figures, earning per share (EPS), and average return on assets (ROA) are also variables that have been studied in relation to bank performance. Correlation has been used to test the hypotheses

By analyzing the data.

HYPOTHESIS:
On, the, premise, of, the, goals, considered, for, the, study,, the, accompanying, speculations, are, created:
1 hypothesis: Capital, ampleness, proportion, does, not, altogether, impact, net, benefit.
2 hypothesis: The NPA ratio has no significant effect on net profit.
3 hypothesis: Net profit is not significantly affected by NPA.
4 hypothesis: EPS is not significantly influenced by the NPA ratio.
5 hypothesis: Capital, ampleness, proportion, does, not, essentially, impact, EPS.
6 hypothesis: EPS is not significantly impacted by NPA.
7 hypothesis: NPA, does, not, altogether, impact, return, on, resources.
8 hypothesis: The capital adequacy ratio has no significant effect on ROA
9 hypothesis: ROA is not significantly influenced by the NPA ratio.
Data, Analysis, and, Findings:
T-test for mean comparison between SCBs and PCBs:
T-test for Return on Assets ROA
Hypothesis:
Ho: Mean of Return on Assets of state-owned commercial banks and private commercial banks are equal.

H1: Mean of Return on Assets of state-owned commercial banks and private commercial banks are not equal.

Table 1 group statistics

	Type of the bank	N	Mean	Std.deviation	Std.error mean
Return on asset	SCB	68	5216	1.09445	1.3272
	PCB	102	1.1937	.89580	.08870

Interpretation:

Mean values of Return on Assets of state-owned commercial banks is .5216 and private commercial banks is 1.1937. Mean difference is -.67211.

The value of "t" is -4.210 and it is significant (p value < 0.01) at 1% level. That means there is significant

Difference between Return on Assets of state-owned commercial banks and private commercial banks. Here,

Return on Assets of private commercial banks is significantly higher than that of state-owned commercial

Banks.

Correlations among the variables related to credit risk ratios:

Table-02 correlation

		ROA	NPL	CAR	ADR
ROA	Pearson correlation	1	-437	.204	.461
	Sig. (2-tailed)		.000	.008	.000
	N	170	170	170	170
NPL	Pearson correlation	-437	1	-464	-230
	Sig. (2-tailed)	000		000	.003
	N	170	170	170	170
CAR	Pearson correlation	.204	-464		.184
	Sig.(2-tailed)	.008	.000		.017
	N	170	170	170	170
ADR	Pearson correlation	.461	-230	.184	1
	Sig.(2-tailed)	000	.003	.017	
	N	170	170	170	170

Correlation is significant at the 0.01 level (2 tailed)

Correlation is significant at the 0.05 level (2-tailed)

CORRELATION COEFFICIENT ANALYSIS:

Interpretation: Correlation co-efficient between return on assets and non-performing loan is r = -0.437Which is significant (p value< .01) at 1% level. That means there is significantly negative relationship between Return on assets and non-performing loan. Correlation co-efficient between return on assets and Capital Adequacy Ratio is r = 0.204 which is significant (p value< .01) at 1% level. That means there is significantly Positive relationship between return on assets and Capital Adequacy Ratio. Correlation co-efficient between return on assets and Advance-Deposit Ratio is r = 0.461 which is significant (p value< .01) at 1% level. That means there is significantly positive relationship between return on assets and Advance-Deposit Ratio. Correlation co-efficient between non-performing loan and Capital Adequacy Ratio is r = -0.464 which is Significant (p value< .01) at 1% level. That means there is significantly negative relationship between nonperforming loan and Capital Adequacy Ratio. Correlation co-efficient between non-performing loan and Advance-Deposit Ratio is r = -0.230 which is significant (p value< .01) at 1% level. That means there is significantly negative relationship between non-performing loan and Advance-Deposit Ratio.

Correlation co-efficient between Capital Adequacy Ratio and Advance-Deposit Ratio is r= 0.184 which is Significant (p value< .05) at 5% level. That means there is significantly positive relationship between Capital Adequacy Ratio and Advance-Deposit Ratio. The study found that there is no perfect or nearly perfect Correlation among the independent variables. That is the variables are free from multi-collinearity effects. Since the independent variables are free from multi-collinearity effects, so it is logical to fit regression model

Of profitability variable on credit risk variables.

HYPOTHESIS TESTING:

Hypothesis can be tested by using the P-value (Sig. Level) of each β coefficient of independent variables.

Confidence interval of accepting hypotheses is 95%.

To achieve this confident interval, P – value should Be equal to or less than 0.05. If it is not equal to or Less than 0.05, null hypothesis cannot be rejected.

P – Value of β coefficient of Non-Performing Loan Ratio is 0.000 which denotes that Non Performing Loan Ratio effect on Return on Assets with 100% Confident interval. Here the probability of rejecting Null hypothesis is 100% since the P – value is 0.000 Which is less than 0.05. Based on this result, H1 can Be accepted and H0 is rejected. Non-Performing Loan Ratio has a significant effect on Return on Assets. P- Value of β coefficient of Capital Adequacy Ratio is 0.610 which indicates that the Capital Adequacy Ratio effect on Return on Assets with 39% Confident interval. Here the probability of rejecting Null hypothesis is 61% since the P- value is 0.610, Which is more than 0.05. Based on this result H2 Can be rejected and H0 is accepted. So it can be said That, Capital Adequacy Ratio effect on Return on Equity but not statistically significant. P- Value of β Coefficient of Advance Deposit Ratio is 0.000 which Indicates that the Advance Deposit Ratio effect on Return on Assets with 100% confident interval. Here The probability of rejecting null hypothesis is 100% Since the P-value is 0.000, which is less than 0.05.

Based on this result H3 can be accepted and H0 Is rejected. So it can be said that, Advance Deposit Ratio effect on Return on Equity that is statistically Significant.

From the above analysis it is found that, the most Of the coefficients are significant at 5% level. So, Null hypothesis that there is no significant impact of Credit risk management on Return on Assets (ROA) Of commercial banks in Bangladesh can be rejected.

The study found that Capital Adequacy Ratio has No statistically significant impact on Return on Assets. And it also found that Non-Performing Loan Has negative impact and Advance-Deposit Ratio Has positive impact on return on assets, and it is Statistically significant. So it can be concluded that Credit risk management has significant impact on Return on assets.

Conclusion and Recommendations:

The, study, examined, the, influence, of, credit, risk, on, the, execution, and, effectiveness, of, HDFC, bank., The, examination, of, the, information, uncovers, that, the, non-performing, resources, proportion, has, an, reverse, relationship, with, the, execution, and, productivity, measures, of, the, bank, which, demonstrates, that, the, lower, the, NPA, proportion,, the, better, the, execution, of, the, bank., Based on the findings, it can be safely concluded that the levels of non-performing loans and the capital adequacy ratio have an impact on bank performance indicators like ROA, EPS, and profit, putting them at significant risk of illiquidity and distress.

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