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ASSESSMENT OF CREDIT RISK MANAGEMENT EFFECTIVENESS IN INDIAN COMMERCIAL BANKS A Case Study on FEDERAL Bank

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Performance of Credit Risk Management in Indian Commercial Banks

ABSTRACT :

Credit risk has traditionally been a crucial element for banks and other financial organizations that must be effectively handled. Credit risk was the chance that a borrower from the other party wouldn't fulfil its commitments as agreed upon. Therefore, credit risk results from the bank's interactions with or lending to businesses, people, and other banks or financial institutions. Due to the nature of its operation, the bank had inherited the oldest and most significant risk. There are now several banks operating in India. The following public sector banks were chosen: State Bank of India, Punjab National Bank, Oriental Bank of Commerce, Bank of India, Indian Bank, Indian Overseas Bank, Syndicate Bank, Bank of Baroda, Canara Bank, Allahabad Bank, UCO Bank, and Vijaya Bank. The following private sector banks were chosen: Axis Bank, ICICI Bank, IndusInd Bank, ING Vysya Bank, Dhanlaxmi Bank, HDFC Bank. The researcher employed several regression models and 11 years' worth of data from each bank's return on asset (ROA), non-performing asset (NPA), and capital adequacy ratio (CAR) to determine the extent of its influence.

KEYWORDS: Banks, Commercial banks, Private sector banks, public sector banks.

INTRODUCTION :

The process of economic development had been ongoing. The level of resource and investment mobilization, as well as the operational effectiveness and economic discipline demonstrated by the various economic sectors, were the primary determinants of how successfully the economy developed. The banking industry has evolved into the cornerstone of contemporary economic growth. Banks contributed to a nation's economic growth by accepting and using significant sums of money in a fiduciary position as well as by leveraging such sums by generating credit. A commercial bank was a type of financial middleman that received deposits from the general population and loaned the money out for profit. Even though it could take deposits, a post office cannot be referred to be a bank since it does not lend money, which is one of a bank's primary functions.

The foundation of an economy's financial sector was its banking system. Commercial banks were crucial in the development of undeveloped nations through the improved allocation and mobilization of resources. A commercial bank would accept a variety of deposits, including current, savings, securing, and fixed deposits. It provided credit in a variety of ways, including loans, advances, the discounting of bills, and investments in assets traded on open markets. In order to issue securities to the public, it provided investment services such as underwriters and bankers.

Banks were institutions of finance that provided loans and took deposits. In India, commercial banks provided credit (loans) for a variety of objectives to various borrower groups.

Most clients could get debt financing primarily through bank credit, and for banks, productive loans were their most valuable assets.

According to several experts and writers, credit risk was the greatest risk overall in terms of the extent of prospective losses. Credit risk management has been the main focus of banks' risk management since it has always been at the heart of banking operations.

Better risk management by banks would provide them an advantage and boost performance (return). Better risk management revealed that banks managed their operations with reduced relative risk and less potential for conflict of interest.

REVIEW OF LITERATURE :

- Rekha and Koteshwar (2017), feel that the Credit Risk is the oldest and biggest risk that Banks, by virtue of their very nature of business inherit. The pre-dominance of credit risk is the main component in the capital allocation. As per their estimate credit risk takes the major part of the Risk Management apparatus accounting for over 70 per cent of all Risks. As per them the Market Risk and Operational Risk are important, but more attention needs to be paid to the Credit Risk Management in Banks.
- Vivek Singh (2016), in their study an attempt is made to understand the status and trend of NPAs in Indian Scheduled commercial banks, The factors contributing to NPAs, reasons for high impact of PAs on Scheduled commercial banks in India and recovery of NPAs through

various channels. This study shows that extent of NPA is comparatively very high in public sectors banks. The NPAs level of our banks is still high as compared to the foreign banks. • Nayan & Kumaraswamy (2014), in their study find that the profit in PSBs was declining trend due to competition, lack of diversity of banking services and stringent rules of RBI before economic reforms. The profit was declining initial period due to operation was not linked with profit and lack of diversity in the banking services.

- •Thiagarajan et al. (2011) examined how market discipline affects commercial banks' conduct regarding capital sufficiency. The analysis found that the Indian commercial banking sector's Capital Adequacy Ratio (CAR) indicated that the commercial banks were adequately capitalised and that the ratio was much higher than the legal minimum requirement.
- In comparison to public sector banks, private sector banks displayed a larger ratio of tier-I capital. The public sector banks, on the other hand, displayed greater tier-II capital levels. Although the level of capital adequacy in the banking industry may have been impacted by the regulatory authority's (RBI) full implementation of the Basel II accord.
  article evaluated the study's use of both private sector and public sector banks.
- Ghosh and Das (2005) examined whether and to what extent governments should mandate banks to maintain adequate capital levels as well as if market forces may also maintain the stability of banking systems. The study added to this discussion by demonstrating how market forces may lead banks to choose high capital adequacy ratios in order to reduce their borrowing costs. Evidence from empirical tests conducted on the public sector banks in India in the 1990s shows that banks with more capital had lower borrowing costs. These results showed that ongoing reform initiatives at the global level should prioritize boosting competition among banks and openness.

OBJECTIVES

1. To understand the concept and nature of Credit Risk Management of Commercial Banks (public and private sector in India.
2. To know the different types of credit risks and the techniques to manage risk in Indian banks.

HYPOTHESIS

Hypothesis 1 (H0): credit risk management had an effect on the bank performance.
Hypothesis 2 (H1): credit risk management had no effect on the bank performance.

DATA ANALYSIS AND INTERPRETION

AUTOCORRELATION

Dependent Variable: MONTH

Method: Least Squares

Date: 03/20/23 Time: 18:09

Sample: 2018M01 2023M03

Included observations: 63

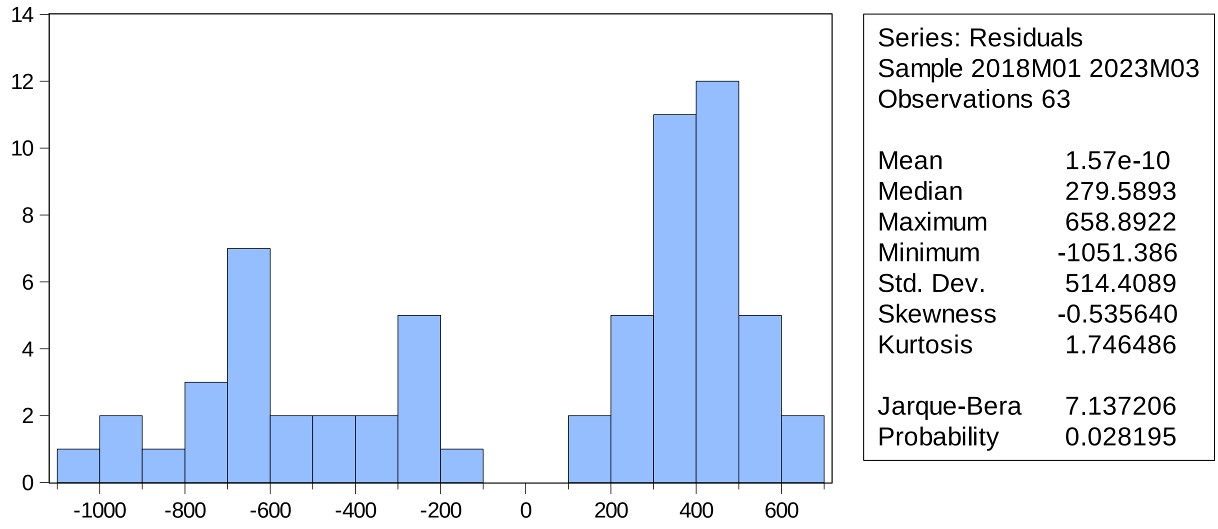
Variable	Coefficient	Std. Error	t-Statistic	Prob.
CLOSE_PRICE_OF_FEDRAL_BA	9.331710	3.060762	3.048820	0.0034
RETURNS_OF_FEDRAL	2.842083	5.863184	0.484734	0.6296
C	736808.0	277.2023	2658.015	0.0000

R-squared	0.150139	Mean dependent var	737636.7
Adjusted R-squared	0.121810	S.D. dependent var	558.0003
S.E. of regression	522.9121	Akaike info criterion	15.40315
Sum squared resid	16406224	Schwarz criterion	15.50521
Log likelihood	-482.1993	Hannan-Quinn criter.	15.44329
F-statistic	5.299878	Durbin-Watson stat	0.066064
Prob(F-statistic)	0.007593		

Interpretation

From the above table it is evident that the d value is about 0.066064 which is less than 2 Hence there is evidence of positive autocorrelation in the given time series data.

NORMALITY TEST



Interpretation

From the above table, conclusion has been drawn on the basis of probability value. If the probability value of Jargue Bera (P – value = 0.028195) is less than 0.05 at 5% level of significance, we reject the null hypothesis for normality and conclude that the observed series follows normal distribution.

CONCLUSION :

In this global economic environment, better credit risk management offers the chance to significantly boost overall performance and ensure competitive advantage. Better credit risk management lowers financial risk, which produces income for the bank and raises profitability. When the bank is in good shape, the nation's economy is in good shape, which raises GDP. Thus, a mutual relationship exists. Effective risk management techniques have therefore become more important. The main objective of efficient credit risk management is to uphold the essential elements of best practices that are widely used and accepted around the world. Federal Bank also highly focus on this area. Banks are currently continually expanding the boundaries of risk management. Banks are under pressure from growing competition, agency issues between owners, management, and other stakeholders, and other factors to look at newer avenues to increase revenues while reducing costs. Without a question, risk management, competition, and consolidation are essential to the future of banking. To help our customers use credit risk management to increase customer profitability and maintain shareholder value.
Federal Bank has the knowledge, insights, and experience necessary. Faced with rising shareholder demands, they have assisted over 422 top companies in streamlining their credit risk management procedures and gaining actual advantages like a decrease in net bad debt, cost savings in operations, and a reduction in customer churn.

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