

IDEES – International Multidisciplinary Research Journal

(Peer Reviewed)

A STUDY OF CREDIT RISK MANAGEMENT IN SELECTED INDIAN PRIVATE BANKS

DIPIKA RAVALIYA

Research scholar

Veer Narmad South Gujarat University, Surat, Gujarat

ABSTRACT

Risk is a natural phenomenon of any business. Risk is undesired disagreeable and at time of disastrous probable events associate with human action or inaction. Risk is almost god like in qualities. It is omnipresent. Especially banking is a business of trust and confidence hence probability of risk is high. Indian banking system provided Basel I and Basel II for guideline of better risk management. This paper analyzed the selected AXIS bank, ICICI bank and HDFC bank credit risk management system including loan performance, total assets, Non-performing assets, Return on assets and capital adequacy ratio of banks. It's also focus on model of CRM. Such paper analysis carried out to highlight the NPA of selected bank from 2012 to 2014.

Key words: Credit Risk Management, Private Banks, NPA and ROA

INTRODUCTION

Economy of any country is closely linked with the financial system of the country. Stability and ideal liquidity of the financial system are closely depending upon strong and resilient Banking system. For the maintaining of efficient liquidity in the market credit risk management is a main basis to control credit risk. CRM is an undoubtedly among the crucial issues in the field of banking for banks as well as regulators. The system of the effective credit risk is based on Successful risk management, transparency and accountability. Banking is a business of trust hence transparent pricing of product and services, adequate and timely delivery of the information are required for maintaining the confidential business. Credit risk is generally more important than market risk.

DEFINING CREDIT RISK MANAGEMENT

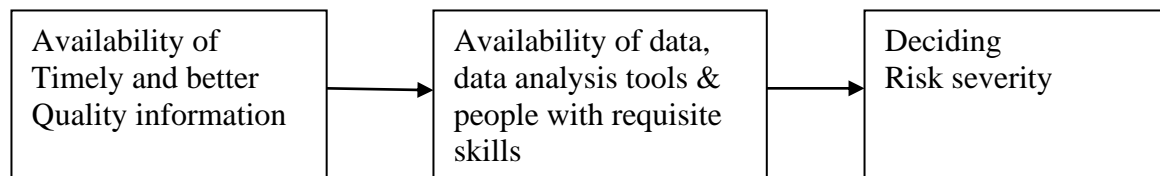
The risk loss of principal or loss of a financial reward stemming from a borrowing failure to repay a loan or otherwise meet a contractual obligation. Credit risk arises whenever a borrowing

is expecting to use future cash flows to pay a current debt. Credit risk means probability of loss from a customer's insolvency or default. Credit risk in banking sector is many factors are affected like interest rate in a loan, long term loan, higher the interest rate etc. CRM including the identification, measurement, monitoring and controlling of the credit risk exposures. The choice of appropriate strategies for control of credit risk by individual banks depends on their priorities and risk-appetites.

Generally banks suffer from two types of risk can be divided into business risk and control risk. Business risks arise from the arena of capital, credit, market, operational earnings, liquidity, environment, and business strategy and group risk. Control risks come out from lapses, loopholes in internal control, management, organization structure and non-compliances of various system and procedures. The Different kinds of risk including credit risk, market risk, operational risk, liquidity risk and operational risk. Out of this operational risk are more critical and vital. Expert believed that across the globe many losses occurred in various spectrums in financial services due to fail operation, or loss over internal process. Effective management of operational risk demand deep understanding and plausible assessment of existing risks, potential risk, misses, near misses, others visible and non-visible factors. Global risks and macroeconomic risks continue to be perceived as major risks affecting the financial system. The asset quality of banks continued to be a concern while regulatory risk, operational risk and the risk of low credit-off-take increased comparatively.

Ideal faces of risk management approach firstly indicate the availability of time and quality information about all related elements. Secondly availability of data and data analysis tools, such as stimulation, scenario analysis, data tabulation and using expert skill for converting raw data into risk measured. Thirdly, settle on risk strictness. For e.g. If a risk is expose to business line on a regular basis is called price moment and impact of price value are assess through the historical information.

Phase of an Ideal Risk Assessment Approach



CREDIT RISK MANAGEMENT MODEL

Banks are managed credit risk using differential model. Risk-based pricing, Covenants, Credit insurance and credit derivatives, Tightening, Diversification and Deposit insurance are also used for mitigation of credit risk. Credit risk model including are as follows.

I.COMPLEX MODELS & THE MODEL RISK

This model is exposed by error wrong development, implementation and use the aggregate of this risk is called model risk. A key element of model is well developed by experts from statistical & financial domains, internal validation are organization and ongoing validation through back-testing, bench-marketing & quality control. Statistical model are based on certain assumption. This is model only serve the purpose for which built.

II.EMERGENCE OF CREDIT DERIVATIVES

It's a biggest financial innovation which separate and transfer the default risk into other entity other than the lender. Hedging and diversifying the credit risk already uses for the interest rate and currency risk. Credit derivatives in recently banking and finance crises has created lot of apprehensions and it called financial weapons of mass destruction. The play the role in selling structured product like the mortgage-backed securities (MBS), asset backed securities (ABS), collateralized debt obligations (CDO), collateralized loan obligation (CLO) etc come under scanner. It's raised the liquidity and reduced the different between market risk and credit risk management practices.

III.CREDIT RISK MANAGEMENT PRACTICES

Diversification is one of the best practices of the CRM. The risk of high losses is reduced by diversifying the investment over many uncorrected obligors. Bank provided the protection for depositors against severe losses, the firstly lending strategy of one single loan requires the bank to hold much more capital than the second lending strategy with a well-diversified portfolio. Portfolio model is determined by single facilities risk measures PD (probability of default), LGD (Loss given default), EAD (Exposure at default) and by concentration and correlation effect. Basel II and stress testing is also practice of CRM.

IV.RISK ADJUSTED PERFORMANCE MEASUREMENT & PRICING

The concept of the above model is adopted by many banks in other denominations like Return on risk-adjusted capital (RORAC) or Risk-adjusted return on risk adjusted capital (RARORAC) are also used. For the calculation of a risk adjusted return on capital (RAROC) number for an individual transaction or a sub-portfolio, all income, cost and economic capital components must be considered at that stage. RAROC used to identify for business segments, business units and individual deals create value. RAPM model related with risk adjusted revenue to economic capital is easy but its implementation, performance, measurement and pricing practice through the organization may be difficult.

V. CRM – INCREASING COMPLEXITIES

Internal and External credit rating play vital role in assessments of risk of the future outcomes. External credit rating agencies (CRAs) provide good track record quality information. Basel II is use for risk management and capital requirement. Rating system analyzed into two dimension first borrower dimension reflect default risk and second facility dimension reflect default and loss risk combined in the expected loss or only loss risk when the bank estimates the loss internally. In past credit scoring and rating model were primarily applied to estimate of the default risk but recently scoring function and rating model used.

LITERATURE REVIEW

Review of literature has considered as a major part of any research. Its helps to researcher to removed the limitation of present study or help to extended prevailing study. RBI and government of India had appointed various committees and study from time to time depth study of the aspects or banks credit, legal reform and non performing assets.

Andrew Campbell (2007) he concluded that the prevention control, managing impaired assets and treatment of insolvent banks are the different stages of risk management of non-performing loan. This study however faults some of the credit risk management policies in place the broad framework and detailed guidance for credit risk assessment & management is provided by the Basel new capital accord which is now widely followed internationally.

P. Veni & P. Shree Devi (2011) liquidity, solvency and profitability are cardinal principle of banking in mind. It was suggested credit granting application, appraisal, sanction, disbursement and control activities are essential for eliminate element of risk. Credit granting criteria indicate target market, purpose and structure of credit and its sources repayment.

Asha Singh (2013) study the CRM of commercial banks including the RBI expectation from banks, encompasses and mitigation. She concluded that the bank reflect the credit risk strategy. Out of this policy come out target limits, prefer level of diversification & concentration, credit risk measurement, monitoring & controlling mechanisms. Proper risk management practices in the bank will create competitive advantages in the market.

Mahadeva Murthy & S.N. Pathi (2013) conducted a study of the risk management system of the SBI and its associate banks. The outcomes of the study are internal management system checked frequently against the possible risk and external credit risk management agencies regularly controlling and managed risk effectively. Risk is threats of banks of course, RBI is issuing guidelines from time to time to maintain solvency of each and every banks

Smita Shukla & Rakesh Malusare (2014) conducted the survey of risk analysis system of the private and public sector banks. Finding of the study is risk in public banks is greater than private banks. Based on the risk management policy bank decided the quantum and quality of capital. Bank was best for the judge deciding its capital requirement. Prudent demand that in the economic decision making, the bank due to consideration provided with the objective of survival in worst case scenario. Leverage decision adequately linked with quantity and quality of the capital will be in the long term interest of the banks.

Asha Singh (2015, January) analyzed the effect of credit risk management in private and public banks. Under the study were considered ROA, CAR and NPA of the banks using regression analysis and test has been applied. The study shown that there is significant relationship between bank performances (Return on Assets) and credit risk management (Loan performance). Better CRM improved return on assets. Main finding of the study has performance of private sector banks are much better than public sector banks. The banks those who are facing low competitiveness on credit risk management and positive change in productivity should improved their CRM to maintain high productivity.

ADDRESSING THE PROBLEM

Risk is like threat for banking business. One of the major functions of the bank are mobilizing the fund in the economy and lending to the needy/counterparty. Difference between rate of interest of the lending and taking deposit is an income of banks. Trading activity is main function of banks. Whenever the borrower fails to meet the obligation of agreed terms and conditions becomes the credit risk of loan and advances are creating. Default assets are considered uncollectible and of such little value that its continuance as a bankable asset is not war-ranted although there may be some salvage or recovery value.

OBJECTIVE OF THE STUDY

- Understand the concept of the credit risk management system of the banks.
- To analyzed the growth of loan performance of selected private sector banks.
- To study the Total assets, Return on assets, Non-performing assets and Capital adequacy Ratio of selected private sector banks.

RESEARCH METHODOLOGY

This research paper including the secondary data are basically more concentrate on private sector banks. Such kind of require data are collected from annual report of RBI publication, Indian bank association, Related statistical table from private sector banks, related articles, magazines and research paper related to the CRM and NPAs published in different journal have also been used.

PRIVATE SECTOR BANKS IN INDIA

Personally provided the finance is old concept running from incidents period. Banking services are traditionally offered to a bank's rich, high net worth individuals (HNWIs). For wealth management purposes, HNWIs have accrued far more wealth than the average person, and therefore have the means to access a larger variety of conventional and alternative investments. Private banking goes beyond managing investments to address a client's entire financial situation. It's Services including the protecting and growing assets in the present, providing specialized financing solutions, planning retirement and passing wealth on to future generation. Examples of private banks including ICICI bank, AXIS bank, HDFC bank and yes bank etc.

FEATURE OF PRIVATE SECTOR BANKS

Private sector bank is considered as a pillar of the economy. It's provided the loan to the individual, industries, entrepreneurs and business firms.

- I. Encourage saving
- II. Provided Finance to trade & industry
- III. Security of loan
- IV. Personal credit
- V. Financial assistant

**TABLE 1: TREND OF LOAN PERFORMANCE OF PRIVATE SECTOR BANKS
(Rs. Cr)**

Bank Name	2012	2013	2014
AXIS Bank	169759	196990	232381
ICICI Bank	253727	290249	338702
HDFC bank	195420	239720	303000

Source: Indian bank association

From the above table loan performance of the all banks was increased from Rs. 695973 crores to Rs. 962742 crores from 2012 to 2014. Loan performance of all banks was increased constantly. Loan performance of HDFC bank was growing highest compared to other banks. To, concluded loan of performance of banks is follows increasing trends.

LOAN PERFORMANCE OF PRIVATE BANKS (fig. in crore) – CHART 1

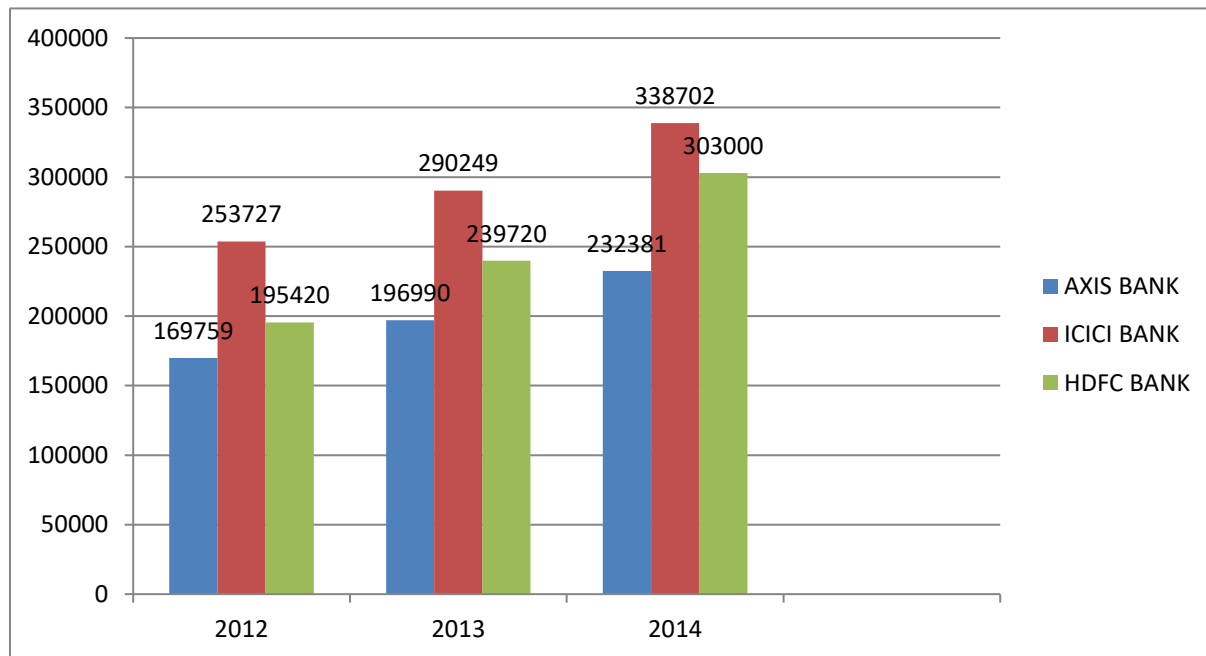


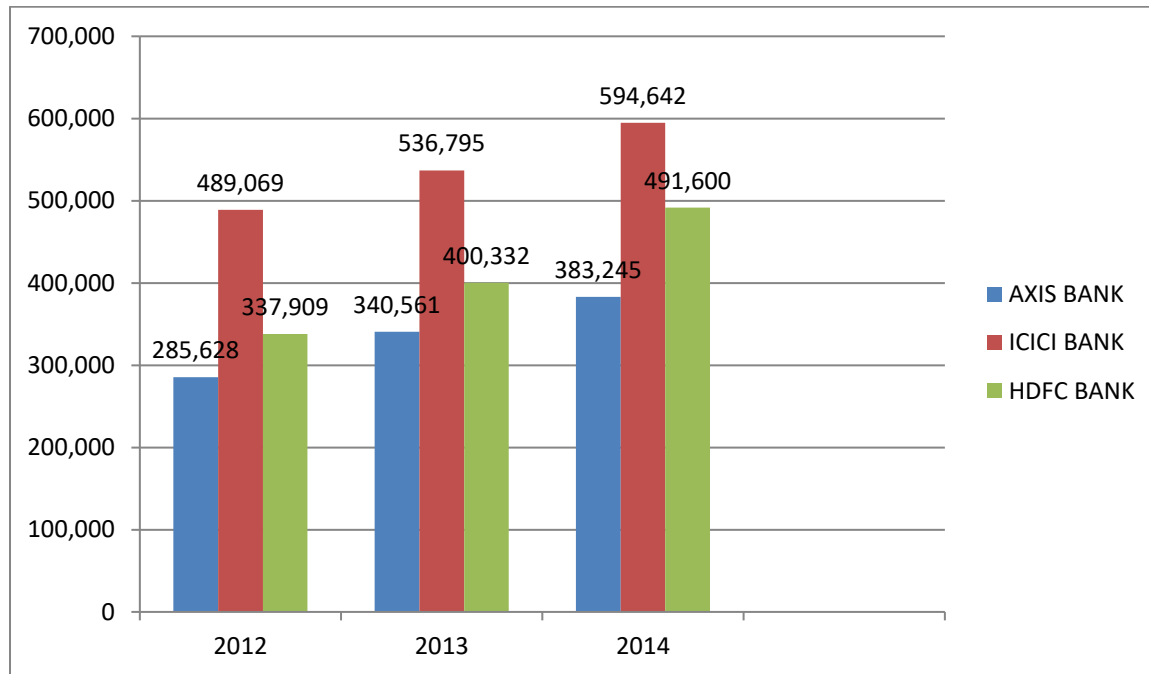
TABLE 2: PRIVATE SECTOR BANKS: ASSETS/ GROSS & NET NON-PERFORMING ASSETS

BANK NAME	TOTAL ASSETS			GROSS NPA			NET NPA		
	2012	2013	2014	2012	2013	2014	2012	2013	2014
AXIS BANK	285,628	340,561	383,245	1806	2393	3146	473	704	1015
ICICI BANK	489,069	536,795	594,642	9,475	9,608	10,506	1,999	2,335	2,989
HDFC BANK	337,909	400,332	491,600	1,999	2,335	2,989	1,860	2,231	3,298

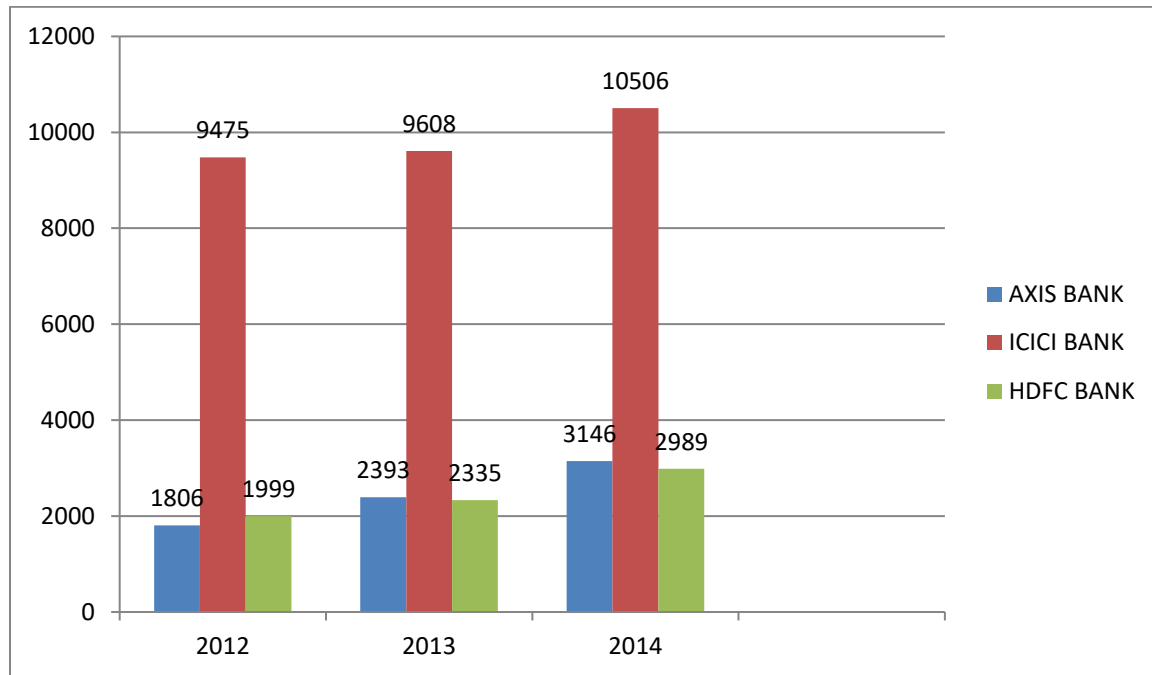
Source: Indian bank association

The above table indicates that total assets, gross and net NPA of the selected banks. Net NPA increment of the AXIS bank, ICICI bank and HDFC bank was 542 cr., 990 cr., and 1438 cr. respectively from 2012 to 2014. Value of Net NPA of the banks was less than 1 percentage of total assets of banks. It's concluded that NPA of all the banks was increase every year.

TOTAL ASSETS OF PRIVATE BANKS – CHART 2



GROSS NPA OF PRIVATE BANKS – CHART 3



NET NPA OF PRIVATE BANKS – CHART 4

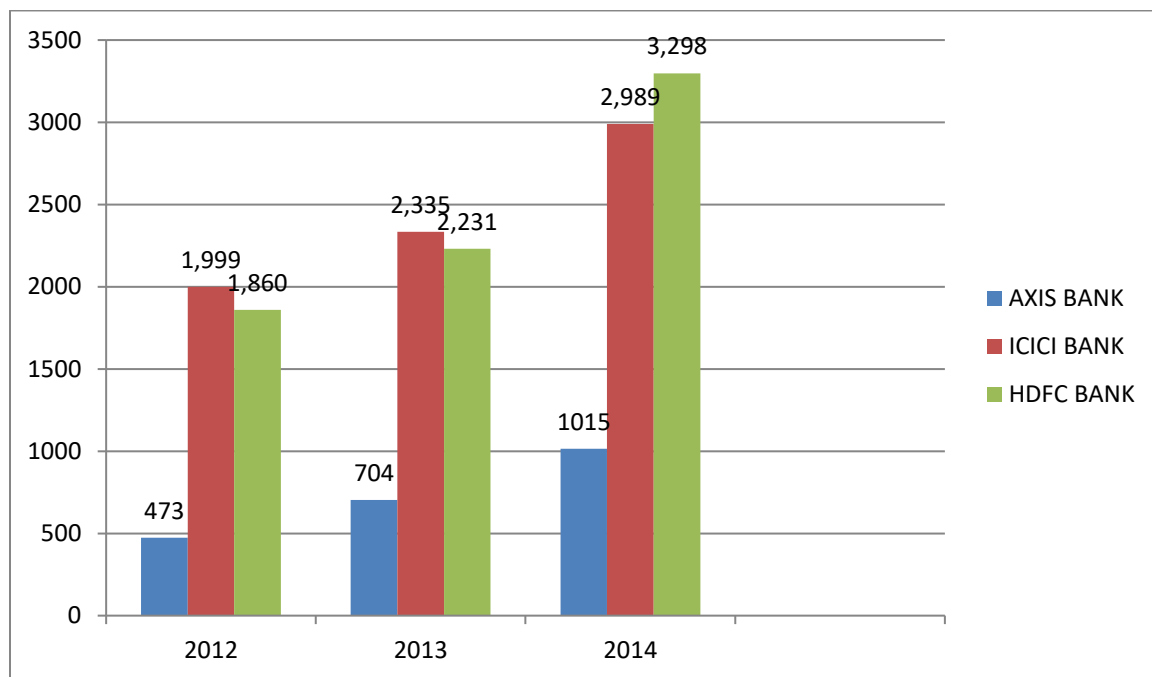


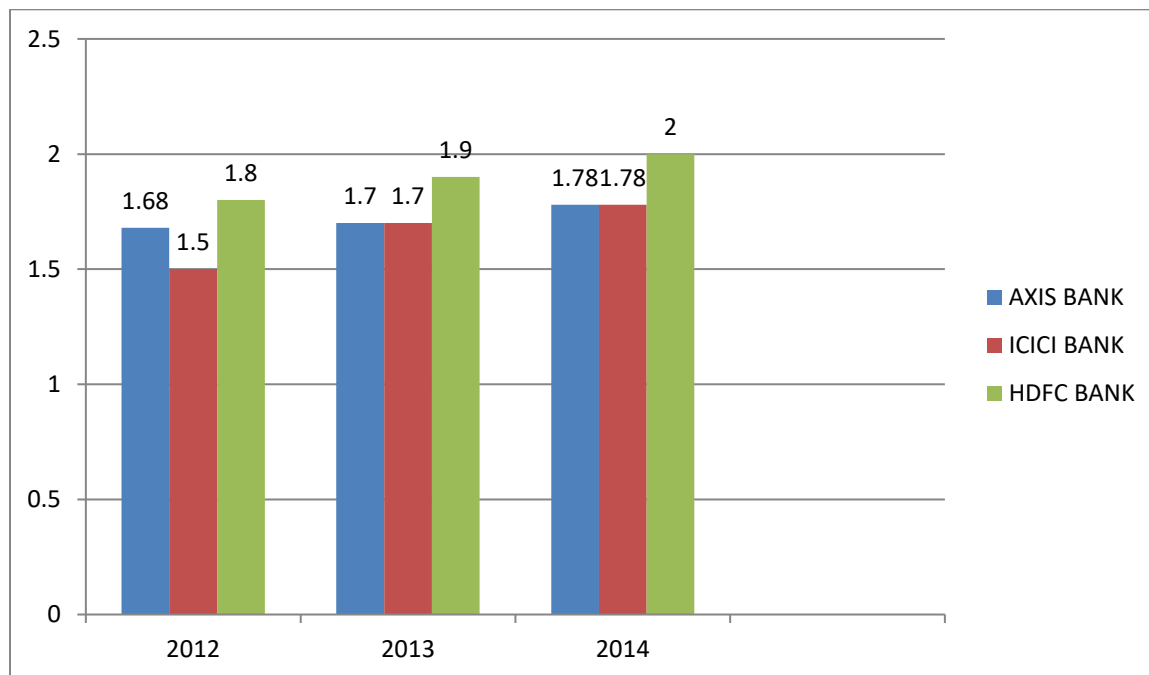
TABLE 3: TREND OF ROA AND CAR OF PRIVATE BANKS

BANK NAME	ROA			CAR		
	2012	2013	2014	2012	2013	2014
AXIS BANK	1.68	1.70	1.78	13.66	17.00	16.70
ICICI BANK	1.50	1.70	1.78	18.52	18.74	17.70
HDFC BANK	1.80	1.90	2.00	16.22	16.80	16.07

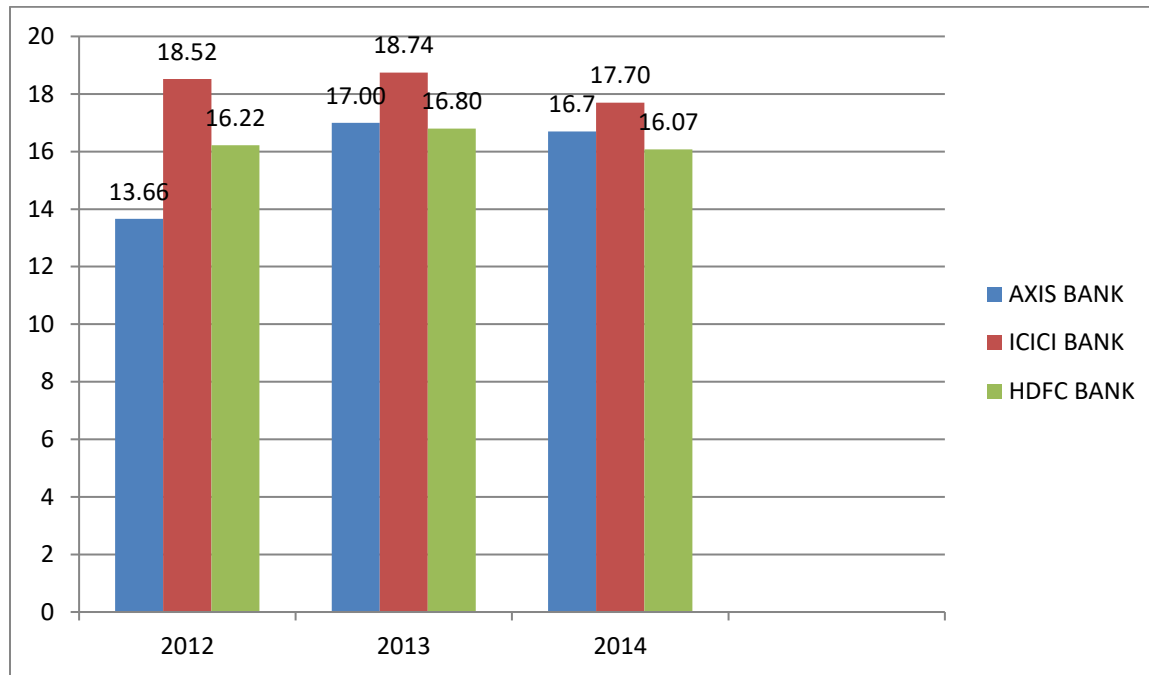
Source: Indian bank association

From the above table indicate the Trend of ROA (Return on Assets) and CAR (Capital Adequacy Ratio). The trend of ROA of all the banks was growing from 2012 to 2014. CAR of HDFC banks highest in 2013 is 18.74. CRA of AXIS bank was increase 3.04% from 2012 to 2014. It is more than other banks. ROA of AXIS bank and ICICI bank was less than HDFC bank. Growth of CAR of all banks was increase from 2012 to 2013 but after that in 2014 CAR of all banks was decrease. CAR of ICICI bank was more compared to others.

RETURN ON ASSETS OF PRIVATE BANKS – CHART 5



CAPITAL ADEQUACY RATIO OF PRIVATE BANKS – CHART 6



CONCLUSION

The study showed that private sector bank managed credit risk through using different model of risk management. The study reveals that loan performance and total assets was increased year by year. Loan performance is closely connected with NPA. Out of three banks ICICI bank were more expanded than AXIS bank and HDFC bank. Performance of all banks in relation to CAR is satisfactory. In recent period loan recovery system of private sector banks is equally monthly installment based and EMI recovered through online clearing system. Hence the probability of NPA is decreased. Risk management system of private banks is satisfactory. The concept of Credit risk management is very wide and it is difficult to covered all aspects of credit risk management of private sector banks.

REFERENCES

Campbell, A. (2007). Bank insolvency and the problem of nonperforming loans. *Journal of banking regulation*. 9(1), 25-45

Veni P., Shree Devi (2011, June). Credit risk management in state bank of India – A study on perception of SBI managers in Vishkhapatnam Zone. *International journal of research in commerce, economics & management*. vol.1. issue 2. Pp. 31-37

Dhirag jain., & nasreen sheikh. (2012, September). A comparative study of loan performance, non-performing assets and net profit in selected Indian private banks. International journal of marketing, financial services and management research. Vol. 1 issue 9. Pp 43-59.

Asha singh (2013, july). “Credit risk management in indian commercial banks” international journal of marketing, financial services & management research. Vol. 2. No. 7. www.indianresearchjournals.com

Mahadev murthy A., & pathi S.N. (2013, july-august) Risk management in banking: a study with reference to state bank of india (SBI) and associates. International journal of management. Vol. 4. Issue 4. Pp. 119-130.

Smita shukla., & rakesh malusare (2014). Risk analysis of select public and private sector banks operating in India . Journal of economic and finance. Pp. 48-59 www.iosrjournals.org

Ashly lynn joseph., & prakash M. (2014, july). A study of analyzing the trend of non-performing asset level in private sector banks and public sector banks. International journal of scientific and research publication. Vol. 4 issue 7 www.ijsrp.org

Asha singh. (2015, January). Effect of credit risk management on private and public sector banks in india. International journal of academic research in business and social sciences. Vol. 5. No. 1

Financial Stability Report .(2014, December) Including “Trend and Progress of Banking in India” (2013-14).

Axis bank. ICICI bank and HDFC bank. 2012-2014. Annual report & financial ratio. <http://www.moneycontrol.com/financials/axis>

Shah, M. B. (May, 2015.). A Financial Ratio Analysis of Hindustan Unilever Limited (HUL) Research Hub: International Multidisciplinary Research Journal

Shah, M. B., & Chavda, K. N. (April, 2015). Financial Ratio Analysis of Gujarat Narmada Valley Fertilizer & Chemicals Ltd. Research Hub: International Multidisciplinary Research Journal, 1-5.