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Banker' Perspective towards Credit Risk Management Policies: A Study

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Abstract

Credit risk management policies are crucial for financial institutions to mitigate credit risk exposure. These policies encompass various mechanisms such as policy frameworks, credit risk rating frameworks, credit risk limits, modeling, mitigation, audits, and loan review mechanisms.

The present study, which is descriptive in nature, attempts to examine the bankers' viewpoint towards credit risk management policies with a sample of 150 bankers' selected by using judgement sampling. To analyze the data, a set of statistical techniques such as frequency distribution, percentage, mean, standard deviation was used. ANOVA technique and t-test have been used validate the results. The study found that there is no significant difference among the demographic profile-wise bankers' viewpoint towards the credit risk management policies. Banks should further explore comprehensive credit risk assessments, establish clear lending criteria, diversify their credit portfolios, conduct regular credit monitoring and reviews, implement robust collection and recovery processes, leverage technology for credit risk management, and ensure regulatory compliance in their CRM practices.

Keywords: Credit risk management, credit risk, commercial banks and risk, etc.

1. INTRODUCTION

Banking is the backbone of the financial system of any country. In the banking system, commercial banks take a special spot. There are many risks associated with lending from banks. The banks are subject to interest rate, foreign exchange, and country risks in addition to counterparty creditworthiness challenges. Still, risk management is also more vital than ever for a variety of reasons. Today's banking sectors are continually impacted by technological advancements, growing usage of technology, and an e-commerce expansion in the variety, volume, and speed of financial transactions. In addition to competition from other banks, banks are facing an expanding array of financial institutions in an unprecedented level of local and worldwide rivalry (**Effros, 1998**). Credit risk is one of the significant risks of banks by the nature of their activities. Through effective management of credit risk exposure banks not only support the viability and profitability of their own business but also contribute to systemic stability and to an efficient allocation of capital in the economy (**Psillaki, Tsolas, & Margaritis, 2010**). The risk management process in banking typically involves six components i.e., nature and identification of risks, assessment and analysis of risk, mitigation of risk, monitoring, cooperation of risks, and mitigation strategies and reporting (**Unit21, 2023**). Credit risk management is defined as the identification, measurement, monitoring and control of risk arising from the possibility of default in loan repayments (**Early, 1996; Coyle, 2000**). Credit risk management is very important to financial institutions as it is an integral part of the loan process. It maximizes an institution risk, adjusted risk rate of return by maintaining credit risk exposure with view to shielding the financial institution from the adverse effects of credit risk. Financial institutions are investing a lot of funds in credit risk management modeling (**Campbell, 2007**). Credit risk management is a structured approach to managing uncertainties through risk assessment, developing strategies to manage it and mitigation of risk using managerial resources. The strategies include transferring to another party, avoiding the risk, reducing the negative effects of the risk, and accepting some or all of the consequences of a particular risk (**Chen, 2008**).

2. LITERATURE REVIEW

Ping (2015) explored the sources of credit risk in Chinese commercial banks, analyzes Chinese commercial banks credit management experience and their insufficiency, and puts forward some countermeasures to control the credit risk of commercial banks in China under the new situation. **Asfaw and Veni (2015)** investigated the level of credit risk management practice of Ethiopian commercial banks. They found that credit risk, liquidity risk and operational risk are the three important types of risks the banks mostly faced. They also confirmed that four aspects of Basel's Credit risk management principles explain a significant level of variation on Credit risk management practice of Ethiopian commercial banks. Furthermore, establishing an appropriate credit risk environment and ensuring adequate controls over credit risk were found to be the most influential variables on level of credit risk management practice. **Sharma and Singh (2017)** discuss how the RBI's guidelines on asset classification, provisioning, and exposure limits have standardized credit risk management practices across the banking sector. **Aldayel and Fragouli (2019)** investigated the impact of credit risk management practices on the financial performance of Commercial Banks in Saudi Arabia. The study revealed that Saudi Commercial Banks engage in credit risk management practices to combat and avoid credit risks. It concluded that these banks embrace different approaches to risk screening and analysis before granting credit to clients to reduce loan losses. **Abdullah (2019)** conducted a study to find out the credit risk management practices of commercial banks in Bangladesh and examine whether commercial banks of Bangladesh follow the rules and regulations of credit risk management policies. The study observed that top management support is crucial for credit risk management and Credit limit system is key in controlling credit risk. **Sirus, et. al. (2019)** examined the impact of credit risk components on the performance of credit risk management and the growth in non-performing assets (NPAs) of commercial banks in India. **Khan (2020)** stated that the goal of credit risk management is to maximize a bank's risk-adjusted rate of return by maintaining credit risk exposure within acceptable parameters. Banks need to manage the credit risk inherent in the entire portfolio as well as the risk in individual credits or transactions. **Svitlana, *et. al.* (2022)** studied the substantiate the prerequisites, management components of the formation of the credit policy of a commercial bank and on theoretical and methodological basis, determine the directions of improvement of the credit policy formation management of a commercial bank, the methods of analysis, synthesis and generalization are applied. A systematic method was used to justify proposals for reducing the credit risk of commercial banks. It found that commercial banks are facing unprecedented credit risk challenges as the financial market becomes increasingly volatile. **Catalina (2023)** studied the Credit risk management policies in Moldovan banks involve defining risk management strategies, diversifying credit portfolios, setting risk limits, and adhering to regulatory norms to enhance bank performance and reduce income losses. It observed that Credit risk management reduces income losses and monitoring credit risk allows banks to analyse potential clients. **Gupta and Singhal (2024)** stated that Credit risk management policies in microfinance institutions should consider business experience, loan use, maturity, and profit motive to enhance sustainability by mitigating credit risks effectively. The study concluded that effective credit risk management involves decision-making process and follow-up and maturity period of loans impacts credit risk and sustainability.

3. RESEARCH METHODOLOGY

The research design for the present study is descriptive in nature. The study is descriptive in the sense that an attempt is made to examine the bankers' viewpoint towards credit risk management policies.

Null hypothesis of the Study

There is no significant difference among the demographic profile-wise bankers' viewpoint towards the credit risk management policies.

Sample Design

The population for the present study is all the public sector banks in the state of Haryana. To know bankers' viewpoints towards credit risk management policies, a sample of 150 bankers' was selected on the basis of judgement sampling from various branches of public sector banks.

Data Collection and tools

The data have been collected with the help of pre-tested structured questionnaire and analyzed with the help of ANOVA and Independent Sample t-test. Secondary data used for the study are collected from the various websites, Journal and annual reports.

4. Results and Discussions

Table 1 shows that 60 respondents (40 percent) strongly agree and 52 respondents (34.7 percent) agree with well-designed credit risk management policy of banks. Whereas, 48 respondents (32 percent) strongly agree and 56 respondents (37.3 percent) agree with CRM system of the bank needs review and change to increase effectiveness. Likewise, 29 respondents (19.3 percent) strongly agree and 83 respondents (55.3 percent) agree with the existence of internal control mechanism to avoid postponement of identification of NPAs. Further, 35 respondents (23.3 percent) strongly agree and 57 respondents (38 percent) agree that the responsibility for credit risk management is clearly set out thoroughly.

On the basis of analysis of bankers viewpoint, well-designed credit risk management policy of the banks is placed at the top (Mean=3.90, SD=1.19); followed by CRM system of the bank needs review and change to increase effectiveness (Mean=3.77, SD=1.16), existence of internal control mechanism to avoid postponement of identification of NPAs (Mean=3.70, SD=1.05), responsibility for credit risk management is clearly set out thoroughly (Mean=3.60, SD=1.10), inadequate appraisal of borrower's credit-worthiness is causing higher NPAs (Mean=3.57, SD=1.02), bank is aware of strengths and weaknesses of other banks' credit risk management system (Mean=3.52, SD=1.14), post-sanction loan monitoring is as important as loan approval process (Mean=3.50, SD=1.18), experience and judgment of risk manager is more important than to apply sophisticated CRM techniques (Mean=3.47, SD=1.15) and human resource needs better skill, training and motivation (Mean=3.43, SD=1.24) as credit risk management policies.

Table 1: Frequency Distribution of Bankers' viewpoint towards Credit Risk Management Policies

Statements	N/P	SD	D	N	A	SA	Total	Mean	S.D.
Bank has a well-designed credit risk management policy	N	2	33	3	52	60	150	3.90	1.19
	P	1.3	22.0	2.0	34.7	40.0	100.0		
There is an internal control mechanism to avoid postponement of identification of NPAs	N	1	34	3	83	29	150	3.70	1.05
	P	0.7	22.7	2.0	55.3	19.3	100.0		
Inadequate appraisal of borrower's credit-worthiness is causing higher NPAs	N	1	33	18	75	23	150	3.57	1.02
	P	0.7	22.0	12.0	50.0	15.3	100.0		

The post-sanction loan monitoring is as important as loan approval process	N	2	47	7	62	32	150	3.50	1.18
	P	1.3	31.3	4.7	41.3	21.3	100.0		
The human resource needs better skill, training and motivation	N	9	38	13	59	31	150	3.43	1.24
	P	6.0	25.3	8.7	39.3	20.7	100.0		
Experience and judgment of risk manager is more important than to apply sophisticated CRM techniques	N	2	46	9	65	28	150	3.47	1.15
	P	1.3	30.7	6.0	43.3	18.7	100.0		
Responsibility for credit risk management is clearly set out thoroughly	N	0	37	21	57	35	150	3.60	1.10
	P	0	24.7	14.0	38.0	23.3	100.0		
Bank is aware of strengths and weaknesses of other banks' credit risk management system	N	3	39	15	63	30	150	3.52	1.14
	P	2.0	26.0	10.0	42.0	20.0	100.0		
CRM system of the bank needs review and change to increase the effectiveness	N	1	35	10	56	48	150	3.77	1.16
	P	0.7	23.3	6.7	37.3	32.0	100.0		

Source: Survey. N= No. of respondent, P= Percent.

5. Demographic Analysis

Tables 2 to 6 show the gender-wise, age-wise, qualification-wise, income-wise and experience-wise results of the bankers' viewpoint towards credit risk management. Independent Sample t-test has been used to study the difference between mean scores of two groups of respondents (bankers) based on gender, whereas ANOVA has been applied for studying the difference in the mean scores of more than two groups based on age, qualification, income and experience.

Gender-wise Analysis

Table 2 presents the results of gender-wise bankers' viewpoint towards the credit risk management policies, which shows that well-designed credit risk management policy of banks is placed at the top by male (Mean=3.96) and female (Mean=3.78), followed by the CRM system of the bank needs review and change to increase effectiveness in case of male (Mean=3.82) and female (Mean=3.67) and existence of internal control mechanism to avoid postponement of identification of NPAs by male (Mean=3.74) and female (Mean=3.63).

Table 2: Gender-wise Analysis of Bankers' Viewpoint

Statements	Males (N=99)	Females (N=51)	Total (N=150)	Independent t-test	
				T	Sig.
Bank has a well-designed credit risk management policy.	3.96	3.78	3.90	0.853	0.395
There is an internal control mechanism to avoid postponement of identification of NPAs.	3.74	3.63	3.70	0.608	0.544
Inadequate appraisal of borrower's credit-worthiness is causing higher NPAs.	3.59	3.55	3.57	0.203	0.839
The post-sanction loan monitoring is as important as loan approval process.	3.53	3.45	3.50	0.364	0.716
The human resources need better skill, training and motivation.	3.46	3.37	3.43	0.419	0.676
Experience and judgment of risk manager is more important than to apply sophisticated CRM techniques.	3.53	3.37	3.47	0.769	0.443
Responsibility for credit risk management is clearly set out thoroughly.	3.65	3.51	3.60	0.693	0.490

Bank is aware of strengths and weaknesses of other banks' credit risk management system.	3.59	3.39	3.52	0.967	0.336
CRM system of the bank needs review and change to increase effectiveness.	3.82	3.67	3.77	0.728	0.469

Source: Survey, **Note**: *Significant at 5 percent level of significance.

Statistically, the results of t-test shows that there is no significant difference between the viewpoint of males and females towards the credit risk management policies, therefore the null hypothesis is accepted.

Age-wise Analysis

Table 3 depicts that well-designed credit risk management policy of banks (Mean=3.65) is placed at the top by the respondents of age group of 18-25 years, followed by CRM system of the bank needs review and change to increase effectiveness (Mean=3.35) and an internal control mechanism to avoid postponement of identification of NPAs (Mean=3.29). Likewise, the respondents of age group of 25-35 years placed CRM system of the bank needs review and change to increase effectiveness (Mean=3.96) at the top, followed by well-designed credit risk management policy (Mean=3.90) and existence of internal control mechanism to avoid postponement of identification of NPAs (Mean=3.72).

Table 3: Age-wise Analysis of Bankers' Viewpoint

Statements	18-25 yrs. (N=34)	25-35 yrs. (N=50)	35-45 yrs. (N=36)	45 yrs. and above (N=30)	Total (N=150)	ANOVA	
						F	Sig.
Bank has a well-designed credit risk management policy.	3.65	3.90	3.83	4.27	3.90	1.511	0.214
There is an internal control mechanism to avoid postponement of identification of NPAs.	3.29	3.72	3.72	4.10	3.70	3.319	0.022*
Inadequate appraisal of borrower's credit-worthiness is causing higher NPAs.	3.06	3.66	3.58	4.00	3.57	5.164	0.002*
The post-sanction loan monitoring is as important as loan approval process.	2.82	3.60	3.58	4.00	3.50	6.308	0.000*
The human resource needs better skill, training and motivation.	2.59	3.52	3.58	4.07	3.43	9.539	0.000*
Experience and judgment of risk manager is more important than to apply sophisticated CRM techniques.	2.74	3.54	3.64	4.00	3.47	8.061	0.000*
Responsibility for credit risk management is clearly set out thoroughly.	3.06	3.62	3.61	4.17	3.60	5.952	0.001*
Bank is aware of strengths and weaknesses of other banks' credit risk management system.	3.18	3.40	3.50	4.13	3.52	4.398	0.005*
CRM system of the bank needs review and change to increase the effectiveness.	3.35	3.96	3.53	4.20	3.77	4.079	0.008*

Source: Survey, **Note**: *Significant at 5 percent level of significance.

However, the respondents of age group of 35-45 years placed the well-designed credit risk management policy of banks (Mean=3.83) at the top, followed by existence of internal control mechanism to avoid postponement of identification of NPAs (Mean=3.72), and experience and judgment of risk manager is more important than to apply sophisticated CRM techniques (Mean=3.64). On the other hand, the respondents of age group of 45 years and above placed the well-designed credit risk management policy of banks (Mean=4.27) at the top, followed by CRM system of the bank needs review and change to increase effectiveness (Mean=4.20) and responsibility for credit risk management is clearly set out thoroughly (Mean=4.17). Statistically, the results of ANOVA shows that there is no significant difference among bankers' viewpoint of different age groups towards the bank has a well-designed credit risk management policy (*p*=0.214), therefore the null hypothesis is accepted.

Qualification-wise Analysis

Table 4 describes the results of qualification-wise bankers' viewpoint towards credit risk management policies, which shows that well-designed credit risk management policy of banks (Mean=3.96) is placed at the top by the respondents who are graduate, followed by the CRM system of the bank needs review and change to increase effectiveness (Mean=3.43) and existence of internal control mechanism to avoid postponement of identification of NPAs (Mean=3.38). Likewise, the post graduate respondents placed the well-designed credit risk management policy of banks (Mean=3.90) at the top, followed by the CRM system of the bank needs review and change to increase effectiveness (Mean=3.83) and internal control mechanism to avoid postponement of identification of NPAs (Mean=3.75). On the other hand, the respondents who have other qualification(s) other than graduation and post-graduation placed well-designed credit risk management policy of banks (Mean=4.04) at the top, followed by the CRM system of the bank needs review and change to increase effectiveness (Mean=3.96) and responsibility for credit risk management is clearly set out thoroughly (Mean=3.96). Statistically, the results of ANOVA shows that there is no significant difference among the bankers' qualification-wise viewpoint towards the well-designed credit risk management policy (*p*=0.463), existence of internal control mechanism to avoid postponement of identification of NPAs (*p*=0.054), bank is aware of strengths and weaknesses of other banks' credit risk management system (*p*=0.087) and CRM system of the bank needs review and change to increase effectiveness (*p*=0.077) as credit risk management policies, therefore the null hypothesis is accepted.

Table 4: Qualification-wise Analysis of Bankers' Viewpoint

Statements	Graduates	Post	Others	Total	ANOVA

	(N=40)	Graduates (N=60)	(N=50)	(N=150)	F	Sig.
Bank has a well-designed credit risk management policy	3.73	3.90	4.04	3.90	0.774	0.463
There is an internal control mechanism to avoid postponement of identification of NPAs	3.38	3.75	3.90	3.70	2.982	0.054
Inadequate appraisal of borrower's credit-worthiness is causing higher NPAs	3.15	3.65	3.82	3.57	5.387	0.006*
The post-sanction loan monitoring is as important as loan approval process	2.88	3.60	3.88	3.50	9.362	0.000*
The human resource needs better skill, training and motivation	2.65	3.55	3.92	3.43	14.269	0.000*
Experience and judgment of risk manager is more important than to apply sophisticated CRM techniques	2.85	3.57	3.86	3.47	9.952	0.000*
Responsibility for credit risk management is clearly set out thoroughly	3.13	3.62	3.96	3.60	6.936	0.001*
Bank is aware of strengths and weaknesses of other banks' credit risk management system	3.30	3.43	3.80	3.52	2.477	0.087
CRM system of the bank needs review and change to increase the effectiveness	3.43	3.83	3.96	3.77	2.605	0.077

Source: Survey, **Note**: *Significant at 5 percent level of significance.

Income-wise Analysis

Table 5 exhibits the results of income-wise bankers' viewpoint towards the credit risk management policies, which shows that well-designed credit risk management policy of banks (Mean=3.68) is placed at the top by less than Rs. 3 lakh income group respondents, followed by the CRM system of the bank needs review and change to increase effectiveness (Mean=3.46) and existence of internal control mechanism to avoid postponement of identification of NPAs (Mean=3.32). Similarly, the respondents of Rs. 3-5 lakh income group placed the well-designed credit risk management policy of banks (Mean=3.79) at the top, followed by the existence of internal control mechanism to avoid postponement of identification of NPAs (Mean=3.77) and CRM system of the bank needs review and change to increase effectiveness (Mean=3.70). Whereas the respondents of income group of more than Rs. 5 lakh placed well-designed credit risk management policy of banks (Mean=4.09) at the top, followed by the CRM system of the bank needs review and change to increase effectiveness (Mean=3.97) and responsibility for credit risk management is clearly set out thoroughly (Mean=3.89). Statistically, the results of ANOVA shows that there is no significant difference among the income-wise bankers' viewpoint towards the well-designed credit risk management policy of banks (p=0.186), bank is aware of strengths and weaknesses of other banks' credit risk management system (p=0.231), and CRM system of the bank needs review and change to increase the effectiveness (*p*=0.083) as credit risk management policies, therefore the null hypothesis is accepted.

Table 5: Income-wise Analysis of Bankers' Viewpoint

Statements	Less than Rs. 3 Lakh (N=37)	Rs. 3-5 Lakh (N=43)	More than Rs. 5 Lakh (N=70)	Total (N=150)	ANOVA	
					F	Sig.
Bank has a well-designed credit risk management policy	3.68	3.79	4.09	3.90	1.703	0.186
There is an internal control mechanism to avoid postponement of identification of NPAs	3.32	3.77	3.86	3.70	3.359	0.037*
Inadequate appraisal of borrower's credit-worthiness is causing higher NPAs	3.11	3.65	3.77	3.57	5.635	0.004*
The post-sanction loan monitoring is as important as loan approval process	2.86	3.51	3.83	3.50	8.934	0.000*
The human resources needs better skill, training and motivation	2.65	3.47	3.83	3.43	12.720	0.000*
Experience and judgment of risk manager is more important than to apply sophisticated CRM techniques	2.81	3.44	3.84	3.47	11.072	0.000*
Responsibility for credit risk management is clearly set out thoroughly	3.08	3.58	3.89	3.60	7.020	0.001*
Bank is aware of strengths and weaknesses of other banks' credit risk management system	3.24	3.58	3.63	3.52	1.481	0.231
CRM system of the bank needs review and change to increase the effectiveness	3.46	3.70	3.97	3.77	2.536	0.083

Source: Survey, **Note**: *Significant at 5 percent level of significance.

Experience-wise Analysis

Table 6 showed the results of experience-wise bankers' viewpoint towards the credit risk management policies, which shows that well-designed credit risk management policy of banks (Mean=3.67) is placed at the top by the respondents who are having less than 2 year experience, followed by the CRM system of the bank needs review and change to increase effectiveness (Mean=3.47) and existence of internal control mechanism to avoid postponement of identification of NPAs (Mean=3.33). Likewise, the respondents who are having 2-5 year experience placed the well-designed credit risk management policy of banks (Mean=3.84) at the top, followed by the existence of internal control mechanism to avoid the postponement of identification of NPAs (Mean=3.78) and CRM system of the bank needs review and change to increase the effectiveness (Mean=3.71). On the other hand, the respondents who are having more than 5 year experience placed well-designed credit risk management policy of banks (Mean=4.09) at the top, followed by the CRM system of the bank needs review and change to increase the effectiveness (Mean=3.96) and responsibility for credit risk management is clearly set out thoroughly (Mean=3.90).

Table 6: Experience-wise Analysis of Bankers' viewpoint

Statements	Less than 2 year (N=36)	2-5 year (N=45)	More than 5 year (N=69)	Total (N=150)	ANOVA	
					F	Sig.
Bank has a well-designed credit risk management policy	3.67	3.84	4.06	3.90	1.352	0.262
There is an internal control mechanism to avoid postponement of identification of NPAs	3.33	3.78	3.84	3.70	3.031	0.051
Inadequate appraisal of borrower's credit-worthiness is causing higher NPAs	3.11	3.64	3.77	3.57	5.372	0.006*
The post-sanction loan monitoring is as important as loan approval process	2.83	3.51	3.84	3.50	9.617	0.000*
The human resource needs better skill, training and motivation	2.61	3.51	3.81	3.43	13.041	0.000*
Experience and judgment of risk manager is more important than to apply sophisticated CRM techniques	2.78	3.49	3.83	3.47	11.157	0.000*
Responsibility for credit risk management is clearly set out thoroughly	3.11	3.53	3.90	3.60	6.660	0.002*
Bank is aware of strengths and weaknesses of other banks' credit risk management system	3.25	3.62	3.59	3.52	1.344	0.264
CRM system of the bank needs review and change to increase the effectiveness	3.47	3.71	3.96	3.77	2.188	0.116

Source: Survey, **Note**: *Significant at 5 percent level of significance.

Statistically, the results of ANOVA shows that there is no significant difference among the experience-wise bankers' viewpoint towards the well-designed credit risk management policy of banks (p=0.262), existence of internal control mechanism to avoid postponement of identification of NPAs (p=0.051), the bank is aware of strengths and weaknesses of other banks' credit risk management system (p=0.264), and CRM system of the bank needs review and change to increase the effectiveness (p=0.116) as credit risk management policies, therefore the null hypothesis is accepted.

6. CONCLUSION

The effective management of credit risk is a critical component of a comprehensive approach to risk management and is essential to the long-term success of any banking organization. For most banks, loans are the largest and most obvious source of credit risk; however, other sources of credit risk exist throughout the activities of a bank, including in the banking book and in the trading book, and both on and off the balance sheet. Banks are increasingly facing credit risk (or counterparty risk) in various financial instruments other than loans, including acceptances, interbank transactions, trade financing, foreign exchange transactions, financial futures, swaps, bonds, equities, options, and in the extension of commitments and guarantees, and the settlement of transactions. In the context of the credit risk management policies, the study found that banks having well-designed credit risk management policy; CRM system of the bank needs review and change to increase effectiveness; existence of internal control mechanism to avoid postponement of identification of NPAs; responsibility for credit risk management is clearly set out thoroughly; and inadequate appraisal of borrower's credit-worthiness is causing higher NPAs. Further, the study suggested that banks should more explore the comprehensive credit risk assessment, establish clear lending criteria, diversification of credit, conduct regular credit monitoring and review, robust collection and recovery processes, use of technology for CRM, and regulatory compliance for CRM.

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