Chapter V

Findings, Suggestions & Conclusions
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5.1 Findings
The researcher visited all ten public sector banks and interacted with the officers working in credit / risk related functional areas like Credit Appraisal, Credit Administration, Recovery / Management of Non performing loans, internal audit / Inspection, Risk Management and Credit Marketing.

The researcher has reviewed the circulars, internal guidelines and inspection comments of the banks. The credit manuals of the banks were also referred to, by the researcher. The researcher has scrutinized the existing application forms, appraisal memorandums, sanction letters, reporting forms, security documentations etc., that are used in the banks for the management of the credit risk functions. The researcher has also interacted with the top executive of the banks on all related topic of the research. In addition he had administered a structured questionnaire and obtained responses from officers working in the relevant area of credit risk management and statistically analyzed the responses. Based on these reviews and verifications the researcher has arrived at certain findings and the same are presented below:

5.1.1 Existing scenario of credit risk management department in banks
Banks in India have well designed application forms for loans. The application form calls for various information about the borrower, his business, financial standing and the purpose of the loan etc. Banks use structured formats for appraisal of credit proposals. Banks also rate the borrower internally using financial, managerial, economic and technical parameters. Banks generally follow the Credit Monitoring Arrangement formats suggested for Balance sheet analysis. Similarly recommendation to approving authorities is also on pre approved formats. The terms of sanction of facilities are mostly codified facility wise and are part of the sanction / approval letters. Documentation has been standardized across the branches all over the country. Reporting lines have been clearly specified and the reporting form for sanction, disbursement etc is periodically obtained from branches by the controlling authority. All these forms are pre printed with necessary blanks for filling up the details and do
not give room for error or omission of important information. Banks also issue detailed guidelines and circulars on each of the aspects of lending.

5.1.2 Recurrence of common lapses in credit risk management
Despite the various risk identification techniques and mitigation strategies, banks keep accumulating non-performing assets. A review of the internal audit reports, observations made by RBI during their inspections on the credit portfolio and the views of statutory auditors reveal that during their inspections/audits have found that many lapses recur despite the same being pointed out in earlier reports and banks instructing the operating functionaries to initiate necessary action to rectify the lapses and also to prevent such irregularities not being repeated in future.

5.1.3 Profile of officers working in credit risk management department
The survey revealed that credit risk management department is dominated by male offices.

77.4% of the respondents (271) are male bank officers and the remaining 22.6% (79) are female bank officers.

Younger officers are predominantly employed and managements prefer matured but not old people to work in risk management areas. (60% of all officers are less than 40 year of age, and 63.4% of officers are aged between 30-50)

The majority of the officers working in the risk departments is graduates and constitutes 62.6% (219) of the sample.

Scale II & Scale III officers (88.6%) are mainly managing the credit risk management departments with a total service 10 years and up to 30 years. Majority of the officers (72.3%) have worked more than 10-20 years in the credit risk related areas.

5.1.4 Awareness about risk management
Bank officers are well aware of the role of credit risk management. They agree that the most important role of the risk department is to maintain quality. They also agree that the most important function of the risk department is reconfirmation of rating of borrowers and the second most function is to suggesting risk based pricing, followed by security & mitigation measures. Bank executives strongly agree that Risk management policies and procedures are set by RBI and merely followed by banks and that Risk appreciation is not uniform at all levels of credit granting chain. According to the
officers surveyed Risk rating is more subjective and credit appraisal is the weakest link in the credit approval system.

Officers working in risk related areas opine that non compliance with terms of sanction (like obtaining securities, insurance, ensuring end use of funds etc.) is the major cause of risk assets. Poor credit appraisal and poor monitoring are the second and third important causes. Political interference and corruption are not mentioned as major causes for increase in risk assets.

It emerges from the study that corporate sector loans are the most contributing loan sector to delinquency resulting in non performing assets. SME loans and Agricultural loan are ranked as second and third most contributors to delinquency.

Majority of the officers working in risk management areas (68%) have answered that the top management commitment is not absolute.

5.1.5 Risk polices and procedures:
On the issue of risk polices and procedure bank officers agree but not strongly that banks on their own also initiate risk management policies and procedures. Similarly they do not strongly support the notion that centralization of sanctions results in credit risk mitigation. According to them Risk Management training is more in the nature of credit appraisal and the tools for risk analysis like track record verification, pre sanction audit, system for early detection of delinquency, information exchange between banks are weak or not effectively used.

5.1.6 Risk control systems:
There is a strong agreement among offices working in credit risk management that there is a conflict of interest between Credit Management department and Risk Management department. They also strongly agree that Computerization has helped in better credit risk monitoring. While they agree that Committee approach to credit sanction really mitigates risk and verification of borrower identity, accounts, stock, valuation security, legal opinion for title etc, by external agencies results in no accountability to employees and is a major weakness in the credit risk management system. They do not strongly advocate them. Similarly they agree but not strongly that Delegation of powers of sanction may improve service
quality but impairs credit quality. However they strongly agree that Risk management tools help judge borrower’s ability, but not his willingness to pay strongly agree

5.1.7 Lapses that recur and causes for Causes for recurring
Most of the officers, (98%) agreed that there are recurring lapses in credit appraisal, credit disbursement and credit monitoring.

According to them ignorance about the procedure / the reason for the procedure is the most important cause for recurring lapses. Similarly trust on the borrower (that he will not default) and the perception that omissions may not pose any risk are the reasons why lapses repeatedly take place. They do not agree that compliance is tedious or lack of cooperation as the reason for recurring lapses. Similarly they do not give importance to promotions, transfer or job rotations or pressure of business or lack of incentive for compliance as major reasons for recurring lapses.

Majority of the officers (86%) said that audit department should close the audit reports.

5.1.8 Constraints in implementation;
Officers accepted that delay in obtaining information, sanction and communicating changes in process, procedures and policies create avoidable risk. But they rejected the notion that HR policies on promotion/ placement affect efficient credit risk management and present training given for Credit Risk Management is adequate

5.1.9 Human factor in building credit risk management system
Majority of (70 %) of officers stated that combined training (training on procedures, financial assessment and legal issues) is needed to handle credit / risk department. They have strongly agreed that professional qualifications help to function efficiently in Credit / Risk Management department and training helps to makes better credit analysis. But have agreed only moderately that

Previous experience in Credit department is necessary to work in Risk Management Department

5.1.10 Impact of adoption of risk management system in banks
The officers working in credit risk management system strongly agreed that adoption of credit risk management system in banks as per Basel committee recommendations and RBI guidelines has resulted in better credit management. According to them, Credit
appraisal, pricing of loans and credit administration are areas that have improved most respectively in the order of improvement.

The most important benefit the banks have gained are listed as Improvement in quality of loans Early detection of problems accounts Less provisioning and capital allocation. While expressing their opinion on further improvement of the risk management system, officers have accorded priority for improvement to Credit administration and Pricing of loans in that order.

The perceptions of the bank officers do not have any association with the gender, age, education levels, their scales, or experience in credit related areas. This means that officers irrespective of these variations (both male and female, young or elder, no graduate or post graduate or professional, scale II or scale VI, well experience in credit related areas or not) perceive the same type of notions. However total experience in service has an association with perceptions of the bank officers.

Credit risk management system of banks in India is mostly influenced by risk policies and procedures, recurring common mistake and human factor.
5.2 Suggestions

The researcher reviewed the existing practices of credit risk management in banks and conducted a survey using a structured questionnaire. The researcher analysed the results of the survey and arrived at certain findings. Based on the findings the following suggestions are made.

5.2.1 Credit Risk Management Practices

The existing credit risk management policies practices are mostly designed by Reserve Bank of India and the banks in India merely follow the same. However the practices and policies are adequate to manage the credit risk in the Indian context. It is suggested that banks should also strive to supplement these policies and procedure by using their expertise and experience gained over the years, calling for suggestions from employees and customers and industry associations like Indian Bank Association, confederation of Indian Industry and Indian Chartered Accountant Institute etc.,

There is enough awareness about risk management among the officers of the bank. However risk perception is not uniform at all levels of the credit granting chain. Therefore banks must ensure that every person involved in the granting of credit appreciates the risks fully and in a similar way. This could be achieved by structured training programmes to officers.

It is felt by the officers that the rating process is subjective. While it may not be possible to have a totally objective rating system due to judgmental elements in credit rating, the factors considered for rating may be redesigned and more variables incorporated to make the rating more objective and less subjective.

The study found that non compliance with terms of sanction is the major cause of risk assets. To over come this lacunae a pre release check should be conducted by an independent officer before release.

Poor monitoring continues to be an important factor in creating risk assets. Under the present system of branch banking, it the manager who is responsible for the entire credit risk management. It is suggested that a separate centralized department for credit
administration is created to look after obtaining securities, insurance charge creating etc.

Poor credit appraisal despite improvement is another important factor. This can be remedied by creating a data base of customer information for appraisal and computerizing the same. Training intervention is also another measure to be undertaken for improving appraisal skills.

Corporate sector dominates as the major contributor to risky loans. While corporate loans are an essential part of the credit portfolio of any banking institution both for profitability concerns and national economic reasons, stringent measures to avoid risk assets must be taken. A few such measures are suggested here under:

If a company defaults to the bank, companies in which the directors of the defaulting company are holding office should be restricted for credit. Obtaining personal guarantees of directors of all directors is another way of curbing corporate misuse of bank funds. Every director must be individually credit rated along with the corporate before loans are given to corporates. In each Board of directors of bank assisted companies there shall be an independent observer appointed by the bank (not a nominee director who participates and becomes responsible for decisions) who reports the proceeding of the board meeting to the bank directly.

SME loans contribute for risk assets only next to corporate loans. Though there are laws to ensure that SME’s a paid with in 120 days many corporates do not pay the SME’s in time which leads to blocking of working capital and the loan becomes bad. To void banks must incorporate a suitable loan covenant in their loan agreement to corporates and monitor compliance.

Agricultural loans are basic necessity of the economy and government’s policy is involved. Banks must closely interact with governments to ensure a health portfolio of agricultural loans. Payment of any subsidy or government purchases must be made directly to the bank which has financed. Since agriculture is monsoon dependent, Comprehensive Agricultural Insurance must be compulsory like motor vehicles insurance and government should discourage write offs and waivers etc to inculcate better credit culture.
The officers indicted that Risk Management training is more in the nature of credit appraisal. The training must be orientated towards risk identification, risk avoidance, risk mitigation measures etc as separate course.

The officers also indicted that the tools for risk analysis like track record verification, pre sanction audit, system for early detection of delinquency, information exchange between banks are weak or not effectively used. Banks can put in place suitable procedures to ensure effective risk management.

The top management commitment is not absolute is another finding. This is a policy matter and the board of directors, reserve bank of India and Government of India are the competent persons to remedy this malady. Possibly when persons of impeccable integrity and competence are appointed to the board this could be addressed.

There is a strong agreement among offices working in credit risk management that there is a conflict of interest between Credit Management department and Risk Management department. This can be resolved only by properly defining the role of each department and fixing the functional responsibility.

Officers strongly agree that Risk management tools help judge borrower’s ability, but not his willingness to pay. Banks can introduce with the help if experts, some physiological profiling for borrower’s values and beliefs systems and views on repayment of loans and tests as part of deciding the willingness of the borrower to pay in addition to his track record and references currently relied upon.

5.2.2 Lapses that recur and causes for Causes for recurring

Since most of the officers, agreed that there are recurring lapses in credit appraisal, credit disbursement and credit monitoring the bank management should immediately take steps to address this problem.

Giving clear guidelines, better monitoring, sensitizing and training the offices are the ways to go solve this problem.

Majority of the officers said that audit department should close the audit reports. The present system prevailing in banks is that audit department only closes the report. But we suggest that the closure of report shall be made after the same has been
recommended by the credit and risk departments to avoid repeat of lapses and to introduce an element of accountability.

5.2.3 **Constraints in implementation:**
Officers state that delays in obtaining information, sanction and communicating changes in process, procedures and policies create avoidable risk. There is system of time norms in banks specifying time frames for each activity. A time frame of 45 days has been the norm for considering a credit application and sanction of loans. Bank can exposure ways to reduce this time frame. Possibly as earlier suggested, creating a database of customer information for appraisal computerization of borrower track record could help to reduce the time.

Officers opined that present training given for Credit Risk Management is not adequate and combined training (training on procedures, financial assessment and legal issues) is needed to handle credit / risk department. The banks have to redesign training programmes so that it is comprehensive for credit skills and risk management.

5.2.4 **Impact of adoption of risk management system in banks**
Credit risk management system of banks in India is mostly influenced by risk policies and procedures, recurring common mistake and human factor. Officers have accorded priority for further improvement in Credit administration and Pricing of loans.

It is suggested that bank according to their risk profile desired should initiate steps to address all the above areas and better training could be a starting point.
5.3 Conclusions

After detailed study and analysis the researcher has reached the following conclusions. Reserve Bank of India plays a major role in the guiding and directing banks to establish and maintain a credit risk management system to international standards.

Banks in India have well designed systems and procedures in place to handle credit risk management. Adoption of credit risk management system in banks as per Basel committee recommendations and RBI guidelines has resulted in better credit management.

Despite the various risk mitigation strategies, banks still strive to control the problem of non performing loans. There are recurring lapses which aggravate the problem. The main causes of recurring lapses are ignorance about the procedures or the reason for the procedure and a sense of complacency that nothing can go wrong in my watch. Delays in decisions in approving loans or recovery contribute to risk assets.

Indian banking has not been afflicted by the influence of political interference or corruption to any significant extent and it is good sign of sensible banking.

Effectiveness of credit risk management system is mostly influenced by risk policies and procedures, recurring common mistake and human factor. Training emerges as an important intervention to remedy the lapses and shortcomings and improve the credit risk management system.

The top managements of banks has to fully commit themselves for better credit risk management systems and appointment of persons of impeccable integrity and competence to the boards of the banks is a must to ensure such commitment.
5.4 Scope for further research:

The research has concluded that in Indian banking effectiveness of credit risk management system is mostly influenced by risk policies and procedures, recurring common mistake and human factor. Training emerges as an important intervention to remedy the lapses and shortcomings and improve the credit risk management system. The research has shown that Risk Management training is more in the nature of credit appraisal. The training must be oriented towards risk identification, risk avoidance, risk mitigation measures etc as separate course. Therefore there is a lot of scope for research in the area of training for risk management.

There is scope for research in the area of top management role and commitment. Causes for absence of full commitment in credit risk management systems, how commitment of top management can be improved are emerging areas of interest for research. This is important as major banks in India have sizable government ownership and government relies on the banks for policy intervention.

The research reveals that Risk management tools help judge borrower’s ability, but not his willingness to pay. The researcher has suggested that banks can introduce with the help of experts, some physiological profiling for borrower’s values and beliefs systems and views on repayment of loans and tests as part of deciding the willingness of the borrower to pay in addition to his track record and references currently relied upon. This is another very interesting and important area of research that can be undertaken.

Banking and risk management are dynamic processes and scope for further research enormous in the areas of risk policies and procedures, recurring common mistake and methods to control them.