RISK MANAGEMENT SYSTEM IN INDIAN BANK

(1) Dr. Gautamkumar P. Kanani

Shree J. D. Gabani Commerce College & Shree S.A.S College of Mgt, Surat,

(2) Dr. Mayurpuri M. Gauswami

M. K. Commerce College, Bharuch.

Abstract: Recent recession across the world and particularly in Indian economy highlighted the need for banks to incorporate the concept of Risk Management into their regular procedures. The various aspects of increasing global competition to Indian banks by foreign banks, increasing deregulation, introduction of innovative products, and have emphasized the need for Indian banks to be prepared in terms of risk management. Indian banks have started to expand and diversify at a rapid rate and have been making great advancements in technology and quality of performance. Thus the need for an efficient risk management framework is paramount in order to factor in internal and external risks. In banks and other financial institutions, risk plays a major part in the earnings of a bank. The higher the risk, the higher the return, hence, it is essential to maintain a parity between risk and return. Hence, management of financial risk incorporating a set systematic and professional methods especially those defined by the Basel norms becomes an essential requirement of banks.

Key Words: Risk, Risk Management, Practices, Role of RBI etc.

Introduction

Risk management in Indian banks is a relatively newer practice, but has already shown to increase efficiency in governing of these banks as such procedures tend to increase the corporate governance of a financial institution.

Risk management refers to the exercise or practice of forecasting the potential risks thus analyzing and evaluating those risks and taking some corrective measures to reduce or minimize those risks.

Whenever any organization makes any decision related to investment they try to find out the number of financial risks attached with it.

What is Risk ? Risk refers to 'a condition where there is a possibility of undesirable occurrence of a particular result which is known or best quantifiable and therefore insurable'. A risk can be defined as an unplanned event with financial consequences resulting in loss or reduced earnings. An activity which may give profits or result in loss may be called a risky proposition due to uncertainty or unpredictability of the activity of trade in future.

In other words, it can be defined as the uncertainty of the outcome. As risk is directly proportionate to return, the more risk a bank takes, it can expect to make more money.

Objectives of the study:

1) To identify the risk management practices in India.

2) To be aware about the types of risk

3) To examine the role of RBI in risk management.

Research methodology:

This paper is theoretical modal based on the extensive research for which the secondary source of information has gathered. The sources include online publications, Books and journals and websites.

Type of Risks: Risk may be defined as 'possibility of loss', which may be financial loss or loss to the image or reputation. Banks like any other commercial organization also intend to take risk, which is inherent in any business. Higher the risk taken, higher the gain would be. But higher risks may also result into higher losses. However, banks are prudent enough to identify measure and price risk, and maintain appropriate capital to take care of any

eventuality. The major risks in banking business or 'banking risks', as commonly referred, are listed below –

- ✓ Liquidity Risk
- ✓ Interest Rate Risk
- ✓ Market Risk
- ✓ Credit or Default Risk
- ✓ Operational Risk etc..

Risk Management Practices in India: Risk Management, according to the knowledge theorists, is actually a combination of management of uncertainty, risk, equivocality and error. Uncertainty – where outcome cannot be estimated even randomly, arises due to lack of information and this uncertainty gets transformed into risk (where estimation of outcome is possible) as information gathering progresses. As information about markets and knowledge about possible outcomes increases, risk management provides solution for controlling risk. Equivocality arises due to conflicting interpretations and the resultant lack of judgment. This happens despite adequate knowledge of the situation. That is why; banking as well as other institutions develops control systems to reduce errors, information systems to reduce uncertainty, incentive system to manage agency problems in risk reward framework and cultural systems to deal with equivocality.

Initially, the Indian banks have used risk control systems that kept pace with legal environment and Indian accounting standards. But with the growing pace of deregulation and associated changes in the customer's behavior, banks are exposed to mark-to-market. Therefore, the challenge of Indian banks is to establish a coherent framework for measuring and managing risk consistent with corporate goals and responsive to the developments in the market. As the market is dynamic, banks should maintain vigil on the convergence of regulatory frameworks in the country, changes in the international accounting standards and finally and most importantly changes in the clients' business practices. Therefore, the need of the hour is to follow certain risk management norms suggested by the RBI and BIS.

Role of RBI in Risk Management

Here, we will discuss the role of RBI in Risk Management and how the tools called CAMELS was used by RBI to evaluate the financial soundness of the Banks. CAMELS is the collective tool of six components namely

- ✓ Capital Adequacy
- ✓ Asset Quality
- ✓ Management
- ✓ Earnings Quality
- ✓ Liquidity
- ✓ Sensitivity to Market risk

- The CAMEL was recommended for the financial soundness of bank in 1988 while the sixth component called sensitivity to market risk (S) was added to CAMEL in 1997.
- In India, the focus of the statutory regulation of commercial banks by RBI until the early 1990s was mainly on licensing, administration of minimum capital requirements, pricing of services including administration of interest rates on deposits as well as credit, reserves and liquid asset requirements.
- RBI in 1999 recognised the need of an appropriate risk management and issued guidelines to banks regarding assets liability management, management of credit, market and operational risks. The entire supervisory mechanism has been realigned since 1994 under the directions of a newly constituted Board for Financial Supervision (BFS), which functions under the aegis of the RBI, to suit the demanding needs of a strong and stable financial system.
- A process of rating of banks on the basis of CAMELS in respect of Indian banks and CACS (Capital, Asset Quality, Compliance and Systems & Control) in respect of foreign banks has been put in place from 1999

References:

http://www.iosrjournals.org/iosr-jbm/papers/ies-mcrc-ibrc/volume-2/RC-15.pdf

https://dspace.lib.uom.gr/bitstream/2159/13869/1/Karaviti_Msc2009.pdf

https://www.academia.edu/21490692/PROJECT_REPORT_ON_RISK_MANAGEMENT_IN_BANKING_SECTOR_

http://www.onlinejournal.in/IJIRV2I8/203.pdf