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Performance Evaluation of Co-Operative Banks of Telangana – An Empirical Study

K.Vaeshnavi*

PHD Research Scholar, Department of Business management, University College of Commerce and Business management, Satavahana University. Karimnagar, Telangana

Abstract - The Co-operative Banks of Telangana approach to risk management is examined in this article. As a result of the ever-changing nature of the market, the growth of technology, the shifting wants of consumers, and other factors, banks in the contemporary period are forced to deal with several financial crises and issues. Banking in India has been around for more than two centuries. In 1786, it began its trip. After the nationalization of banks in 1969, the industry underwent a major transformation. The liberalization, privatization, and globalization policies of the government aided the fast growth of this business. From lending and purchasing to other financial amenities, banking liberalization and economic reforms in India opened up various avenues for the banks. Because of this, banks began to see several beneficial developments and subsequent growth. This was a significant development in the Indian financial landscape. The cooperative bank's most pressing worry is the growing volume of non-performing assets (NPAs) (NPAs). The entire risk exposure associated with banking operations necessitates a systematic risk management approach. Co-operative Banks in India were examined in this research for their risk management practices. This research relied on secondary data.

Keywords - Non-performing assets; credit risk; liquidness risk; interest rate risk; risk management.

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INTRODUCTION

Additionally, there are a number of non-financial hazards associated in the intermediation of financial assets and services. These include credit, interest and exchange rate risks as well as liquidity issues. Bank executives should thus prioritize strengthening their ability to recognize, analyze, Monitor, and manage total risk as a matter of priority.

The scope of risk management should include the following:

i) Administrative configuration;

ii) A systemic approach to risk assessment;

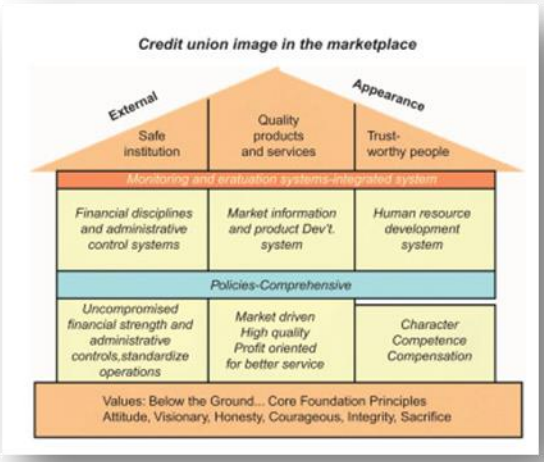
iii) Board-approved risk governance rules should be in line with overall business strategy, capital strength, managerial competence, and a company's inclination to accept threat.

iv) Techniques besides criteria recycled to control menace-enchanting; a full framework of sensible restrictions is included.

v) Robust MIS for registering, surveying and handling risks.

vi) Pleasingly applied techniques, adequate authority and exhaustive hazard reporting framework.

vii) Detached risk administration framework autonomous of functional Branches.



STRUCTURE FOR THE MANAGEMENT OF RISK

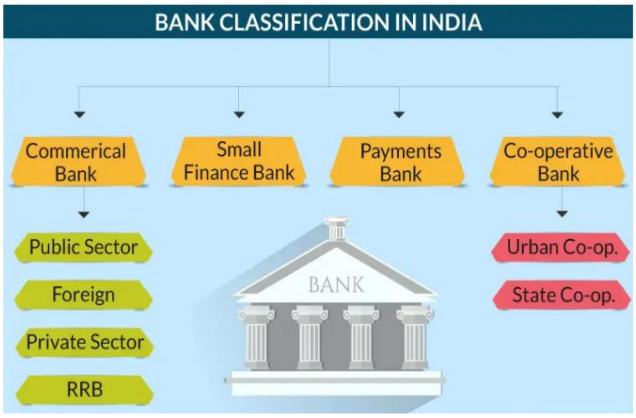
Building a robust risk management organisation starts with picking among a centralized and decentralized structure. Understanding the bank's risks and ensuring their correct management should be a priority aimed at board of directors. All of the bank's overall risks will be analysed by a single group, which will also decide on the amount of trouble that is in the bank's best interest. The evaluation of the total risks that the bank is exposed to, as well as the determination of the degree of difficulty that is in the bank's best interest, will fall entirely within the purview of a single group. A high-quality MIS is a requirement for implementing an effective risk management strategy. The present MIS requires a major overhaul and strengthening of the data collection equipment in order to retain the integrity and reliability of data.

A broad variety of specialised knowledge and expertise is required for efficient risk management. Modern risk management strategies have become more important for banks. Internal risk management models should be developed by large banks and those operating in overseas markets to compete effectively with their competitors. Risk management is becoming more important for banks as the global and local economies grow more linked. Risk modelling and analytical techniques need to be taught at a higher level to the important staff at corporate headquarters. As a consequence, all financial institutions should work to enhance the skills of their workers at all levels. Adopting a consistent framework for risk management in India is difficult due to the wide range of balance sheet profiles. A bank's size, complexity of operations, degree of knowledge, and MIS quality should be taken into account when determining the architecture of its risk management function. There are only basic criteria set out in the proposed standards, and each bank is free to devise its own procedures in accordance with its own risk management architecture and expertise.

There has been an increase in the use of risk management committees around the globe. It is the ALCO and the Credit Policy Committee's job to deal with various kinds of market risk (CPC). A two-pronged approach by banks to market and credit risk management is the consequence. To manage credit and market risk, institutions may create a joint committee. Volatility in the value of the collateral might have an impact on the quality of the loans. In order for ALCO and CPC activities to be integrated, a dialogue mechanism examining how market and credit risks effect a bank's financial soundness should be established. As a result, banks may seek to include market risk indicators into their risk assessment approach.

THE GOAL OF THE RESEARCH

Researching India's risk management system from a global perspective. A study of the different types of risk management systems used by co-operative banks in India, with a focus on Telangana. Methodology used in this research The data utilized in this study was obtained from the official websites of the Reserve Bank of India and the Ministry of Finance.



MANAGEMENT OF CREDIT RISKS

It's not easy to get a loan. Banks are vulnerable to interest rate, exchange, and nation risk in addition to counterparty creditworthiness risk.

Financial commitments may not be met if the customer fails to meet their financial responsibilities, known as default risk or credit risk. Most of the credit risk comes from transaction, default, and portfolio risk.

Portfolio risk is composed mostly of two types of risks: intrinsic and concentration. A bank's credit risk is affected by both external and internal influences. Counterparty risk occurs when contractual commitments are not met.Negative price changes or other external limitations that the primary did not expect might cause non-performance by the counterparty. Instead of a typical credit risk, counterparty risks are often considered to be temporary financial risks linked with trade.

Top management should be involved in credit risk management, which should include the following steps:

1. Credit rating/scoring as a tool for measuring risk;

2. Risk pricing based on scientific evidence;

3. Having a good loan reviewer it is possible that mechanisms and portfolio management will help to reduce the dangers.

CREDIT RISK MANAGEMENT RESOURCES AND INSTRUMENTS

It is possible for banks to reduce credit risk by using a variety of management practises grouped under the term "Credit Risk Management."

Approval Authority for Receiving Credit

The distribution of power in a bank should be carefully worked out by each institution. Another option for bank approvals is to create an "Approval Grid" or a "Committee" for loan requests. To the extent that one officer represents CRMD, the Grid or Committee may authorise credit facilities in excess of an agreed-upon amount.A credit approval committee for big branches could be established (where required).

Limitations of prudential judgment

To minimize credit risk, prudent controls should be implemented on the following credit-related aspects:

a) The Loan Policy should clearly state when and by whom modifications are permitted.

b) Financial institutions may impose lower limits on individual or group borrowing to function as a kind of "floodgate."

c) Single-borrower credit facilities are defined as those that provide a borrower access to more than 10% or 15% of a bank's capital funds.

d) Acquaintance boundaries towards high-volatility asset types like stocks and real estate, as well as particular firms that are exposed to many economic cycles, might be tightened in the near future. The bank should also remove its restrictions on high-risk sectors. Any new risk exposure must have appropriate collateral or strategic reason.

e) A bank's balance sheet, risk assessment capacity, liquidity, and other factors may be taken into account when assessing a loan's maturity profile.

DEGREE OF RISK

A thorough risk scoring/rating system must be in place for banks in order to consistently evaluate the creditworthiness of counterparty in a consistent manner. It's not conceivable without a high degree of homogeneity in credit ratings among the borrowers. Additionally, it is vital that lenders use this grading system as a guideline for determining interest rates on loans, as well as when deciding on non-price factors like collateral. It is important that the risk assessment accurately reflects the true credit risk of the loan portfolio. Additionally, credit providing authorities may take some confidence in knowing the quality of their loans at any given time via the rating procedure.

PRICING OF RISK

In risk management, risk-return pricing is a key principle. When it comes to risk and reward, borrowers in a bad financial condition should be charged more.Risk assessment or credit quality should be used as a factor in determining loan price. In the previous five years or so, the loan Portfolio's historical behaviour, as measured by loan loss provisions and charge-offs, may be used to Estimate default risk. For borrowers with similar ratings and quality, however, there is a need for pricing Comparisons from competing lenders. There would be a 'Adverse Selection' if price-cutting was attempted towords gain market share.

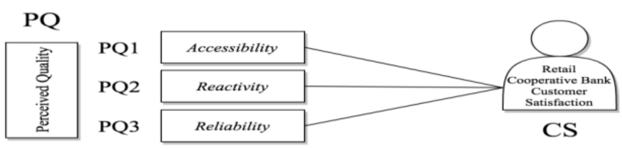


Figure 3. Perceived Quality for cooperative banking customers (Baqué, Ferati, Singh, 2021)

MANAGEMENT OF PORTFOLIO

Because of the way non-performing loans are currently tracked around the balance sheet date, it is impossible to determine the overall health of a company's Loan Book using this method. Prior to any financial crisis, banks should create an effective method for recognising credit difficulties.International banks use a variety of portfolio management methods to assess the quality of their assets. The CRMD, which was established at Head Office, should be responsible for conducting regular portfolio checks. As long as ratings are updated quarterly or semi-annually, this system may be regarded beneficial.The nature and makeup of the loan book may be gleaned from data on grading category changes.

MECHANISM FOR THE REVIEW OF LENDERS

In order to regularly evaluate the quality of the loan book and enhance credit administration, LRM is an excellent instrument. In most cases, the level of complexity and breadth of LRM varies with the size, type, and management practices of the bank. Depending on the size of the bank, it may be a different department from the CRMD.

INVESTMENT BANKING AND CREDIT RISK

In investment banking, there is a significant amount of credit risk, as well as market risk. The same level of credit risk analysis should be applied to investment proposals as it is to loan proposals. Financial and non-financial criteria of the issuers, as well as their susceptibility to external events, should all be taken into account when evaluating and assessing the proposals. Bank-wide exposure should cover all exposures taken on by the Credit and Treasury Departments.

CREDIT RISK IN EXPOSURE TO OFF-BALANCE SHEET FINANCIAL INFORMATION

Financial instruments such as currency forward contracts and swaps must be managed appropriately as part of the overall credit to individual customer relationship through a framework that has been developed. Banks should categorise their off-balance sheet exposures into the following three categories: There are several examples of low-risk contracts that don't support current financial responsibilities. These include standby letters of credit, money guarantees, and more.

INTERBANK RISK AND COUNTRY RISK

In order to give a centralized perspective of the whole exposure to other banks, an appropriate framework should be developed. There should be a single location from which all of the operational centers may monitor and assess the restrictions established. Banks may utilize country ratings from international rating organisations to categories nations as low, moderate, or high risk when it comes to exposure to foreign banks. A bank's internal risk matrix should take into account the risks posed by its customers and the countries in which they operate. As long as existing nation and bank exposure limitations are followed, the maximum amount of risk may be assumed to be acceptable.

RISK IN THE MARKET

Historically, banks faced the most significant issue in managing credit risk. Unpredictable changes in market factors such as interest rates, foreign exchange rates, stock prices, and commodity prices have increased the relevance of market risk as markets have become more deregulated in recent years. Even the tiniest changes in market conditions may have a huge influence on a bank's profitability and value.

The following are examples of market risk:

1. Cash flow Risks
2. The Risk of Interest Rates
3. Risks Associated With Changing Exchange Rates
4. Commodity Risk and Price Risk
5. Price Risk Equity

RISK MANAGEMENT IN THE MARKET

All of the bank's exposure and the bank's effect on a combined basis should be captured through risk measuring methodologies that are clearly specified. Establishing both operational constraints and the line management's responsibilities is essential. Following the Board's performance/risk standards, ALCO will be the central functional unit managing the company's balance sheet.At any given time, it's essential for Treasury and ALCO to be aware of any deviations from prudential/risk norms and how much market risk the bank has taken on.

RISK OF LIQUIDITY

Risk management frameworks in banks include a significant component called liquidity planning. As the loan portfolio grows and off-balance sheet claims are funded, liquidity must be available to absorb declines in deposits and other liabilities. In order for a bank to have enough liquidity, it must be able to obtain cash quickly and at a reasonable cost, either by expanding liabilities or converting assets. Borrowings from the money and capital markets and foreign exchange markets are covered in this category of liquid assets and borrowings. As a result, liquidity should be seen as a kind of protection against losses on asset sales. Banks face a variety of liquidity risks, including:

It is necessary to replenish net outflow of deposits (whole and retail) owing to unplanned withdrawal/non-renewal of deposits.The risk of crystallizing contingent liabilities and not being able to take advantage of profitable business opportunities when they are present.

TOTAL ASSETS TO LOANS

Loans to bank accounts that have cash reserves

It's regarded a short-term investment if the investment matures in less than a year and a long-term investment if the investment is kept in the trading book and can be readily sold on the market.

When it comes to overall assets, purchased funds include all interbank and other money market borrowings, including CDs and institutional deposits. The proportion of total loans that have been lost due to default.

INTEREST RATE RISK (IRR)

Controlling interest rate risk is an essential part of a bank's market risk management strategy. Because of strict regulations, numerous dangers to the banking industry have been greatly minimised. Although interest rates have been deregulated, this has rendered them more susceptible to interest rate risk. A bank's net interest income may be affected by a variety of factors, including interest rate changes. The bank's NII and NIM values may be affected by differences in cash flows (e.g., from assets or liabilities) or periods of repricing (floating assets or liabilities). Volatility in interest rates has made financial assets and liabilities more closely related to one other.

Risk of Gap or Mismatch:

The hazard of holding acquisitions and burdens with additional chief portions, maturity dates, reproducing dates, and off-balance sheet things are referred to as a "gap" or "mismatch" risk.

Accordingly, there is a certain level of risk

Over the course of a year, market interest rates for several securities seldom fluctuate at the same rate. An asset's or liability's interest rate or off-balance sheet item's value may change to a greater or lesser extent, which is known as "basis risk." There is a high degree of basis risk for banks that create composite assets out of composite liabilities.

Entrenched Choice Risk

Term deposits that are withdrawn early before their declared maturities are another source of risk to banks' profitability because of the early payback of demand and term loans as well as the exercising of call and put options on bonds and debentures.

Risk associated with the Yield Curve

The NII would be affected by non-parallel fluctuations in yield curves if banks price assets and liabilities using two distinct instruments maturing over two different time periods.

Risk Price

When an asset is sold before its declared maturity, there is a price risk. Bond prices and yields have an inverse relationship in the financial market. Traders use the trading book to benefit from short-term changes in interest rates, which are strongly correlated with price risk.

Risk Reinvestment

Interest rate apprehension refers to the possibility of reinvesting future financial flows at a specific rate. NII oscillations occur when market interest rates move in different directions, and cash flows do not match.

RISK OF FOREX (FOREX)

The increase in volatility of forex prices has given rise to new dimensions in banks' risk profiles, which has, in turn, increased the inherent risk in holding foreign currency positions. Banks that have a vacant position in a specific foreign currency, whether spot or forward, are at risk of losing money. Even though spot and future holdings in a particular currency are equal, the maturity structure of forwarding transactions can produce imbalances. A currency reward/discount may lead to banks losing money. A currency reward/discount may lead to banks losing money.

Measures to Manage Forex Risk

The Var technique should be used to assess exposure risk at the highest levels of management as well. The Reserve Bank of India has utilised maturity and position besides attention rate compassion to measure FX hazard exposures. In order to keep track of their FX risk exposures, banks should utilise these statements.

Liquidity to Counteract Market Uncertainty

The Basel Committee on Banking Supervision (BCBS) has developed specific rules for banks that require an explicit capital buffer for pricing risk. Banks can now use their internal models based on VaR to assess market risk to replace the Basle Committee's conventional measurement methodology.

Risk in Operational Activities

Operational risk management is becoming more important in today's financial markets by way of the dramatic growth in contract capacity, the significant structural changes that have occurred, and the complexity of the support systems. When internal controls and corporate governance fail, an operational risk is created. For example, if an employee commits fraud, or fails to meet a deadline, the bank may suffer financial losses that might threaten its interests.

Measurement

Operations risk in the financial sector does not follow a consistent methodology. Although several multinational banks must prepared significant progress in creating added complex procedures aimed at distributing wealth in relation to operational risk, the present methods are rather basic and experimental. The likelihood of an operative damage occurring besides the possible extent of damage must be estimated in order to accurately measure operational risk. It depends on a risk factor that indicates the possibility of an operational loss occurrence. If you want a clear picture of operational risk's impact on your company's goals, you need to know how likely it is that a given risk will occur, how severe it will be, and what alternatives are available to manage and mitigate the risks.

Monitoring Risk

The operational performance criteria included in risk management systems are volume, turnover, settlement, delays, and errors. In addition to keeping track of functioning losses consistently, it may also be necessary to investigate and explain the kind and causes of each loss.

The reduction of operational dangers

Management uses internal controls and an internal audit to reduce risk. Based on operational risk metrics, banks might also consider imposing operational risk restrictions. It is possible to mitigate the negative effects of operational risk by using the contingent processing capabilities. Some types of operational risk may be mitigated in part via the use of insurance. Reduced operational risk may also be achieved by educating all levels of workers about the complexities of the operations.

Internal Control

An internal control system that includes defined roles and responsibilities, management reporting lines, and standard operating procedures. Typically, operating risk occurrences result from faulty internal control systems or poor implementation of strategies.

Allocation of Capital and Risk Aggregation

When it comes to determining a bank's capital requirements, most internally active banks have devised their own methods and ways to do so. When evaluating a company's economic capital, these institutions use both qualitative and quantitative indicators. To maintain a long-term soundness of banks, the Basle Committee now recognises that banks must have enough capital in response to economic risk.

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Corresponding Author

K.Vaeshnavi*

PHD Research Scholar, Department of Business management, University College of Commerce and Business management, Satavahana University. Karimnagar, Telangana