

BANKING WITH A FOCUS ON CREDIT RISK

Abstract

This paper's objective is to focus on the bank and its credit risk. The findings hereby focus on how the bank is affected by credit risk and the results related to several causes of credit risk in the banks. It is suggested that an enhanced expense of the credit risk initially decreased the profitability of the bank and therefore the bank must be focused and active towards the credit risk.

Keywords: Banking, Credit Risk, Loan, Money.

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I. INTRODUCTION

Industry of banking is initially providing a financial base or capital to the business society or community as well as for the individual consumers. The banks eventually do this with the ultimate expectation of grasping the target rates of return (ROI) on the extension of the rate of credit over a certain time span, and also initially reclaiming their principal along with the interest. However, the credit extension carries the risk of non-payment under the terms and conditions of the financial connection among the corporate organisations, financier or an individual (Kwashie et al. 2022). Banks highly focus on credit risk and they have a strong interest which is vested in extensive performance due to diligence and also minimising the credit risks and achieving increased value for the concerned organisations.

Credit risk is one of the most significant risks for banks. Credit risk in banks generally occurs when the counterparties or the borrowers eventually fail to meet their contractual obligations. The credit risk in banks should be adequately managed so that if the client or the customer does not pay their credit money then the lender initially loses the entire amount. Moreover, credit risks also arise when the obligatory eventually fails to perform its core section of obligations under a loan or trading contract or when those set of obligations is impaired out-coming in an economic loss to the bank. Collectively it does not only arise when the ultimate borrower defaults on the process of repayment of a certain settlement or loan of the interest or principal but significantly when the ability declines of the repayment. Apart from these, the problem of credit risk in activities lending for the banks is one of the prime concerns or facts for the bank and other regulators or authorities because of huge levels of perceived risk which results from some features of the customers or clients and also their environment of the business, which effectively cause symptomatic distress towards the banks.

II. LITERATURE REVIEW

As per the viewpoint of Kayode et al. (2015), credit is termed as a circumstance whereby the card is eventually issued by the banks and allows the client or the customer holding it to draw money from the branches of the bank and utilised its cheque in payments of services and goods with the maximum amount on every occasion. Credit in banks can be the financial way of resources such as personal loans, overdrafts, order credit, riding loans, direct credit facilities, local purchases, export credit, probate advance, equipment leasing, import facility and so on which is made by the bank for the clients or the account holders in

the bank at a certain rate of interest which the later will surely pay on the prime facility to pave way for the margins of profits.

According to Kwashie et al. (2022), the credit risk arises initially from the potential that the effective creditor is either not willing to perform certain obligations or his capability to perform certain obligations is initially impaired which results in the bank's economic loss. Moreover, it is stressed that the credit risk in the bank is the risk of a certain loan or asset which becomes irrecoverable in the ultimate case of total default amount or the deployment of the risk in advances or serving the loans. Collectively, when it initially takes place or occurs with persistence the bank's performance or focus is affected hugely. In the portfolio of the bank, losses often stem outright from the unwillingness or inability of a consumer to meet certain commitments connected to trading, lending, financial transactions or another kind of settlements. On the other hand, losses may outcome from the decrease in the value of the asset due to the perceived or actual deterioration in the quality of the credit. The bank along with the focus on credit risk emanates the financial exposure to deal with financial institutions, individuals, sovereigns or corporations.

As noted by Ekinici & Poyraz (2019), credit risk is referred to as the risk which is based on a certain assumption of the borrower that it would default in the repayment towards the lender. Moreover, the direct loss of accounting, the credit risk could also be initially viewed in the core context towards the exposure of the economic field. This however encompasses the transaction cost, opportunity cost and expense which is associated with the non-performing set of assets above and over the loss of accounting. Collectively, this can also be further segregated into sub-categories on the core basis of the responsible reasons for default. For instance, the bad mode of the portfolio may initially attract the problem of liquidity. As inspired by Kwashie et al. (2022), in most banks, the section of loans is the most obvious and significant source of credit risk. Therefore credit risk eventually stems from the activities relating to both the off and on the balance of sheet transactions.

III. METHODOLOGY

This section of the research study focuses on the methods that are utilised in achieving the core objective of the study which is the prime concentration of the banks in accordance with the credit risk (Kwashie et al. 2022). In the previous part of the report which is the literature review, the credit risk and its focus on the bank are discussed in detail. Moreover, this section of the report clearly depicts the different types of data collection methods that are utilised in this report to proceed further with more authenticity. Collectively, the secondary set of data collection is adopted by consulting with the existing peer-reviewed articles and journals which are available in the database such as Google scholar. The collection of data is referred to as the systematic approach that is implemented in the report or study so that the information is collected or gathered appropriately from different sources to get the correct answers along with authenticity. Official reports of the banks on focus towards credit risk are also implemented in this report for adhering to high-depth information following the credit risk of the bank. Moreover, the thematic data analysis is followed in this report taking into consideration the secondary data collection method. This helps in reaching through the secondary data set and also identifying the patterns in terms of data and its meaning.

IV. RESULTS

The empirical results or outcomes of different studies show mixed trends on the core effect of the bank performance or focus on the credit risk. Moreover, both negative and positive focus of banks towards credit risk has been highlighted and found significant. However, in the more extreme section, there is also found no relationship between the performance and focus of the banks and credit risk (Ekinici & Poyraz, 2019). Several problems have also been highlighted due to the issue of credit risk on the bank which has to be focused on primarily, these are as discussed below:

1. Credit Concentration: Credit concentration takes place when the majority of the lending power of the bank is focused on particular borrowers or particular sectors. The conventional form of the credit set of concentrations involves lending towards individual borrowers, a particular industry or sector or a team of a connected set of borrowers. This particular cause in the bank is highlighted very significantly and also focused effectively. Some examples of credit concentration are listed below;

- A major bank concentrates on the lending amount or credit to a certain company and also its team entities. However if the concerned team incurs a prime loss, the bank would also lose the prime section of its amount of lending. However, the bank in focusing on the credit risk should not initially restrict its power of lending to a specific team of companies alone in order to minimise risk.
- A bank lends to clients or borrowers in the sector of real estate. However, if the entire sector faces a loss or slump then the bank would also eventually lead with loss as it cannot eventually recover the monies lent. There is always a very high level of credit risk in the bank and the bank should concentrate more on how to get recovery from this prime issue.

2. Credit Issuing Process: This particular issue that the bank should focus on is the credit process of issuing. This involves the flaws in the credit granting of the bank and the process of monitoring (Ekinici & Poyraz, 2019). Although the credit risk is therefore inherent in the process of lending, it can be thus kept at a minimum with the ultimate sound credit practices. Moreover few instances are added that result in the bank credit loss and which should be focused on in more depth by the bank as discussed below:

- **Incomplete Credit Assessments:** To initially evaluate the creditworthiness of any type of client or borrower, the banks significantly news to check for the capacity to repay, the credit history of the clients or the borrower, the capital, collateral and the conditions of the loans. However, the credit worthiness of the borrower cannot be initially evaluated. Therefore the bank must focus and exercise caution during the processing of lending.
- **Subjective Decision-Making:** Through subjective decision-making, the bank also focuses more depth on credit risks. This is regarded as the most common practice in banks and also other organisations wherein the top-level management is given free rein into making certain sets of decisions. However, the top-level management is therefore allowed to make certain decisions independently towards the policies of the

company, which is all subject to any kind of approval, there should also be several instances where the loans are eventually granted and are also related to the parties and the clients with not evaluations of credit. Therefore the credit risk of default is also enhanced.

- **Inadequate Monitoring:** When the process of lending is for the long-term settlement, they are most secure against the core sets of assets. Moreover, the asset value may also deteriorate over time a period. It has resulted in that is not only significant to monitor or control the bank's performance and the borrowers, but also to effectively monitor and control the asset value.
3. **Cyclical Performances:** Each and every industry or organisations go through a depression period or boom period. During the period of boom, the evaluations of the bank lead to good creditworthiness of the customer or the borrower. Moreover, the cyclical performance of the ban must also be taken into core consideration to arrive at the outcome of the credit evaluations in more accurate forms.

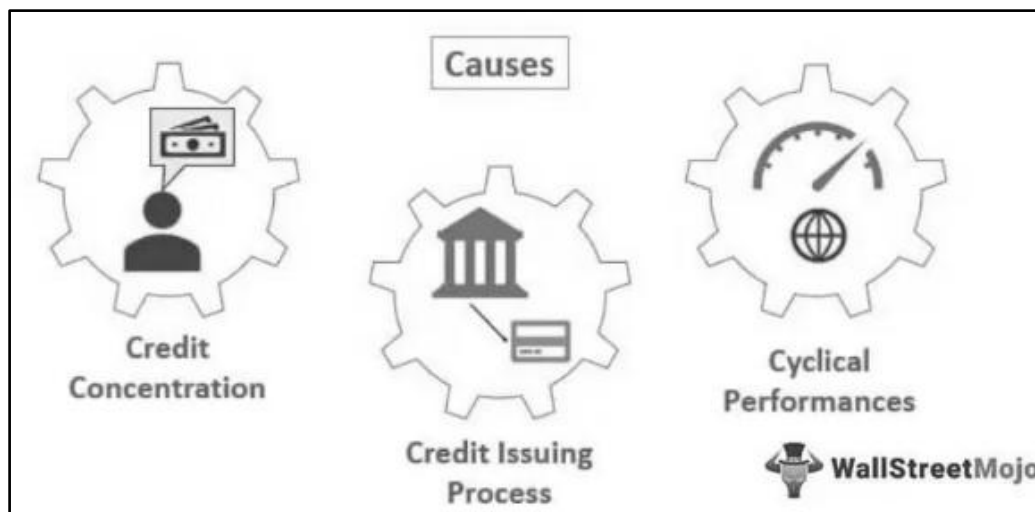


Figure: Credit Risk in Banks
(Source: As inspired by Ekinici & Poyraz, 2019)

V. CONCLUSION

The banks and the credit risks are inherent towards the function of lending. They cannot be neglected or discarded entirely. The impact of the credit risk on the banks can be minimised with proper controls and evaluations, Therefore it has been concluded that the banks are more prone to incur greater risk due to their huge functions of lending. It becomes very significant that they recognise the major cause of credit issues or problems and eventually implement a sound system of risk management to initially maximize the return while risk minimising. The study hereby investigates the bank and its focus on credit risk. Therefore to maximise the sets of sprouts and also to edge it against loss, the banks should therefore also adopt an aggressive mode of deposit to increase the availability of credit and also develop the credit risk reliability and the strategy of the management. Collectively the banks should also engage in a proper mode and assessment of credit risk before giving out

loans to the borrowers and also in promoting the loan process and recovery reliably with adequate punishment of loan repayment.

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