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### CREDIT RISK MANAGEMENT PRACTICES AND PERFORMANCE OF CO-OPERATIVE BANKS IN KERALA

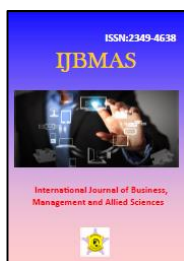
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#### ABSTRACT

The banks and financial institutions face the problem of considerable rise in Nonperforming Assets and the issue becoming more relevant with regard to survival of Indian banking sector. In order to manage the situation tactically, several solution mechanism and legal framework have been setup by Reserve Bank of India. The co-operative banking sector tries to manage the problem through the adherence of rules and regulations put forward by the authorities concerned. At the same time they adopt some strategies of their own to control the quantum of stressed assets. In India the existence of strong Co-operative sector is inevitable as it fill the gap of banking needs of small and medium income group. The banks are urged to ensure uniform and consistent application of prudent norms and other legal measures for reducing the burden of nonperforming Assets. The realistic approach towards credit risk management practices prompt the repayment by the borrowers and improve the record of recovery in various loans. This paper tries to study credit risk management practices and performance of co-operative banks in Kerala.

**Key words:** Nonperforming Assets, stressed Assets, Credit risk, Strategy

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#### 1. INTRODUCTION

The Co-operative Banking has been playing an important role in the Socio -economic development by satisfying financial requirement of rural people. The long term and short term Co-operative banking system in the country fulfilling the financial need for agriculture and allied activities of Indian farmers. Most of the Co-operative Societies have close touch with rural people catering the credit needs of them. With a view to promoting agricultural activities and small scale units in different part of the country especially in backward area, the Co-operative movement was started in 1904. After independence the emergence of Co-operative movement have remarkable role in poverty eradication

and economic development of the Nation. At present, there are more than five lakh co-operative societies which have spread over the rural economy. Co-operative credit societies are mainly constituted to encourage thrift, self-help and co-operation among the members. It also aims to disseminate latest development in agriculture, handicraft, weaving etc. The obstacle for the survival of the system is high over dues from the part of borrowers. Recently there is tendency to demand for the cancellation of debt due to the Co-operative Societies by the farmers Union. Co-operative banks are under Political pleasure to write off loan given to different purpose. The development of banking system is entirely based on effectiveness of debt recovery. The credit risk due to the default of the customer should be properly administered. Proper credit risk management strategies significantly reduce the amount of Nonperforming assets; nurture a good credit culture in the area of banking system.

In the books of a bank there are different types of assets such as current assets, loans and advances, long term investments, fixed assets and other assets. The credit risk concept is confined to loans and advances. When loan asset ceases to generate income in the form of interest, it will become Nonperforming asset. Profitability and earning capacity of the banks are badly affected due to the increasing amount of NPA. In India various Committee recommendations in this regard suggested several measures to reduce the quantum of NPA. Moreover Reserve bank of India issues norms and strategies to control the alarming situation of accumulated amount of NPA in banking sector

## 2. REVIEW OF LITERATURE

**Verma and Bhagavan (2000)** studied the main reason for defaults and recommended some remedies for reducing the NPA. Defaults could be reduced if the amount of credit had been linked to production on a scientific basis. The study reveals major causes of default by the cultivators were inadequate market prices for their products. The conclusion of the study is that inappropriate prices, lack of income, ineffective recovery process, willful defaults by the customers and political intervention were the influencing factors contributing accumulated NPAs.

**NABARD (2005)**, a study on "Developments in Cooperative Banking" conducted to assess the financial performance of selected urban cooperative banks and rural cooperative credit institutions. The study reveals that in the rural sector, the quantum of NPAs in sub-standard category has been reduced. But the doubtful assets, the amount of NPA have increased resulting deterioration in asset quality. The credit institution under the study is able to meet the norms requirements for NPAs. The NPA ratio is more for the central cooperative banks as compared to State co-operative banks. It further revealed that the percentage of NPAs in Central co-operative banks varied considerably across the states.

**Campbell (2007)** Conducted study on the establishment of internal control systems in accordance within the banking institution to monitor the effectiveness of NPA management system. Suggested the necessity of implementing the Basel Norms to minimize the problem of increasing trend in Nonperforming loans. This is possible after having effective system of prudential norms and proper supervision. Sufficient power should be given to the supervisor to discharge the task effectively.

**J. Nivethitha and G. Brindha (2014)**, this research paper gives emphasis on Management of Non-Performing Assets. The conclusion is that the accumulated NPA of Cooperative banks highly affects the probability. It also has a negative impact on the net worth of the banks resulting erosion in the value of assets. Systematic credit risk management system is the only solution for reducing this situation. The bank should strengthen credit appraisal and monitoring system

## 3. SIGNIFICANCE OF THE STUDY

Today the banks give prime importance to retain their customers as a part of the banking business. In the liberalized economy the competition is increasing; the survival is possible only by maintain the profitability and liquidity of baking business. If the borrower fails to pay the due amount on time it will badly affect the financial capacity of the banks. The aim of credit risk management is to maintain required risk adjusted return in future. The co-operative banks are considered as the major institution in fulfilling the credit needs of rural mass. Effective NPA management system is inevitable for boosting better credit culture in the Co-operative banking sector. The present study assures the importance of credit risk management and focus on the existing strategies and norms followed to solve the crisis of NPAs.

#### 4. STATEMENT OF PROBLEM

The co-operative credit institutions face the problem of credit risk as it unable to collect the dues from the borrowers. The existence of strong Co-operative sector in the field of credit distribution is essential to address the credit needs of rural people. If the bank fails to manage the NPA, it will create survival crisis; unable to earn proper required profitability. The effectiveness of profitability and financial stability mainly depends on credit risk management activities of the organization. Credit risk management pave way for reducing the amount of NPA and facilitate effective implementation of debt recover process. Taking in to account the importance of credit risk management it is considered appropriate to study the practices and performance of co-operative banks in Kerala

#### 5. OBJECTIVES

- 1) To identify factors affecting non-performing asset in co-operative banks.
- 2) To analysis the strategies and norms adopted by banks for credit risk management.
- 3) To make suggestions and recommendations based on study.

#### 6. RESEARCH METHODOLOGY

Based on the objective both primary and secondary method has been adopted to collect the data. The primary data have been collected with the help of pre-structured questionnaire. Secondary data are collected from magazines, newspapers and financial journals.

#### Factors affecting credit risk.

There are many causes for credit risk to the banking sector. The increasing trend of NPA may due to internal or external factors. For the study purpose no categorization of variable is made as internal and external. In this study total of 12 factors have been identified and tabulated on the following table.

#### FACTORS AFFECTING CREDIT RISK FOR THE BANKS

SL.NO	Factors	Total Score	Mean score
1	Poor credit appraisal system of the bank	145	2.9
2	Delay in settlement of recovery process	236	4.72
3	Existence of staff and board members in credit	204	4.08
4	Lack of strong credit information system	228	4.56
5	Wrong selection of the customer	219	4.38
6	Burden of interest and penal interest	198	3.96
7	Crisis in agriculture sector	237	4.74
8	Industrial recession in small scale sector	148	2.96
9	Collapse of retail shops	235	4.7
10	Political interference	222	4.44
11	Government policy	168	3.36
12	Natural calamities and economic crises	238	4.76

(Source: primary Data)

The above table shows natural calamities and economic crises are the main factors contributing credit risk to the bank. Natural calamities affecting the activities of agriculture sector and the farmers are not able repay the credit amount on due date. Lack of required minimum support price also create problem to the farmers. Most of the customers in the co-operative sector borrowings belong to farmers and the traders running small scale units. Collapse in the area of retail shop numbered as another important external cause for accumulated NPA in Co-operative banks. The major problem from the part of these banks is delay in settlement of recovery process.

### Strategies for credit risk management

The following are the main strategies adopted by the Co-operative banks for speedy recovery of debt due from the customers.

### STRATEGIES FOR CREDIT RISK MANAGEMENT

No	Strategies	Total	Rank
1	Recovery through SARFAESI Act	13	9
2	Debt through Adalath	37	3
3	Arriving settlement with customer	46	1
4	Waiving interest and avoiding penal interest	40	2
5	One time settlement system	33	4
6	Legal suit and attachment of property	17	8
7	Risk assessment mechanism	29	5
8	Ensure proper security for land	23	6
9	Moratorium for repayment of loan	19	7

(Source: primary Data)

Table shows the ranking of appropriate strategies for credit risk management. According to opinion of bank officials arriving settlement with the customer of bank is the best strategy for reducing the NPA. Waving the interest and avoiding penal interest may also act as positive measure for cutting down the quantum of credit risk. Recovery through SARFAESI Act may not consider as effective practice in credit risk management process.

### Findings of the Study

- The study reveals that the agricultural sector contribute major portion of NPA in Co-operative banks.
- Poor credit appraisal system of the bank is the least factor contributing credit risk to the bank. The natural calamities and economic crises are the main factors contributing the credit risk.
- Arriving settlement with customer may be considered as the positive strategy for credit risk management and reducing the amount of accumulated NPA.
- Motivation to customers through waiver of interest and avoiding of penal interest may also a good practice in credit risk management.
- Accumulated NPA affects the credit expansion capacity of banks. Adverse effect on reputation of bank among general public create problem in mobilizing the savings and reduce the lending capacity in future

### Suggestions for development

- Adequate manpower is essential for effective NPA management because it involves the analysis of credit risk, deciding the best practice of debt recovery, immediate action and follow up.

- Awareness campaigning for the borrowers may create positive interaction between bank officials and borrowers. Arriving settlement with customers become easy through this process.
- Since most of customers belong to agriculture sector, incentives may be given in the form of concession of interest rate, avoiding penal interest etc. This kind of incentives may prompt repayment debt.

## CONCLUSION

The element of credit risk in lending is key factor which influence the profitability and liquidity position of banking institutions. Now the NPA remain a matter of concern for all banks including the institutions functioning under Co-operative sector. The banking institutions should ensure more control over increasing trend of NPA to safeguard the interest of all the stakeholders. The policy makers should adopt appropriate strategies for solving the problem of alarming situation of NPA in Indian banking sector. The practice prevailing in bank should facilitates interaction between bank officials and borrowers.

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