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Available online at: www.jrrset.com

ISSN (Print) : 2347-6729
ISSN (Online) : 2348-3105

JIR IF : 2.54
SJIF IF : 4.334
Cosmos: 5.395

Volume 10 Issue 9 - September 2022 - Pages 1-7

A Study of Risk Management Policies and practices of SBI

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1.0 Introduction

This chapter explains various methodologies that were used in gathering data and analysis which are relevant to the research. This methodology will include areas such as Research Design, Area of Research, Review of literature, Data analysis and Interpretations.

1.1 Research Design

This study descriptive research design is defined as a research method that describes the characteristics of a Study of risk Management policies and practices of one among the well-known banks of India. More over this research helps us to understand Methodology deals with new prudential norms like capital adequacy and identification of bad debts in modern banking system.

1.2 Area of Research

The study was carried on State Bank of India, The Indian banking system is better prepared to adopt Basel II than it was for Basel I, the effective risk management lies with the ability to gauge the risks and to take appropriate measures. In the light of this, an analysis was carried out to highlight the NPA's position of SBI and associates and also capital adequacy ratio after the implementation of Basel II accord to focus on the risk management practices in state bank of India (SBI).

1.3 OBJECTIVES OF THE STUDY

The objectives of the study are as follows:

1. To study the summary of risk management in banking sector.
2. To access the various study conducted in risk management in banking sector.
3. To analyze the Basel I, Basel II and Basel III accord in bank credit risk management.
4. To highlight the trends of NPAs position in SBI and associates.
5. To analyze the status of capital adequacy ratio of SBI and associates; and
6. To offer findings, recommendations and conclusion in the light of the study.

1.4 Period of Study

The study associates for the period of six financial years from 2007-13.

1.5 RESEARCH METHODOLOGY

The present study is based on data gathered from secondary sources. The relevant secondary data were collected by making reference to the Government publications, Bulletins of the RBI, Bulletins of the Indian Banks Association, Mumbai, National Institute of Bank Management (NIBM), Pune.

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, The Journal of Indian Institute of Banking and Finance, RBI issues like reports on Trend and Progress of Banking in India. Annual Reports of various banks, apart from these different editions of daily newspapers such as Financial Express, Business Line and Business Standard were also used for the purpose of collection of data. In addition to above listed secondary sources, various reports of SBI were also widely used. In this study we have analyzed the credit risk management of SBI and associates. For this study we have divide the components of credit risk management of NPAs and capital adequacy ratio of SBI and associates. Non-Performing Assets (NPAs) are the primary indicators of credit risk. Capital Adequacy Ratio (CAR) is another measure of credit risk.

1.6 Methodology used in the study

The methodology used to analyze the NPAs of SBI and associates in three categories: (Non-Performing Assets (NPAs))

1.Priority sector;

2.Non-priority sector; and

3.Public sector.

Ratio analysis is used to analyze the data.

The study also divides the components of Capital Adequacy Ratio (CAR) of SBI and associates in two categories:

1.Basel I; and

2.Basel II.

Capital Adequacy Ratio is a measure of bank's capital and it is expressed as a percentage of a bank's risk weighted credit exposures.

CHAPTER II REVIEW OF LITERATURE

Review of literature has vital relevance with any research. The review helps researcher to remove limitation of existing work or may assist to extend prevailing study, the review of literature presented below covers credit risk, NPAs, Basel II and operational risk. Angbazo (1997). In this study, banks with a larger risky loan portfolio appear to require higher net interest margin to compensate the higher risk of default. This result suggests the significant relationship between net interest margin and credit risk

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The findings of Hassan, (1994) support the earlier findings that Size and Diversification are negatively related to risk. Brewer et al. (1996) find that loan sectors have a significant association with risk. Fixed-rate mortgage loans, investment in service corporations and real estate loans are found to be significantly negatively related to credit risk. However, non-fixed rate mortgage loan is significant and positively related to risk.

Bratanovic and Greuning (2000) recommended that credit risk ratios can be used as a measure of the credit risk associated with the banking sector and highlighted the usefulness of such ratios for banks to internally lower the ratio and avert any catastrophic failures.

Bhattacharya (2001) rightly points to the fact that in an increasing rate regime, quality borrowers would switch over to other avenues such as capital markets, internal accruals for their requirement of funds. Under such circumstances, banks would have no option but dilute the quality of borrowers thereby increasing the probability of generation of NPAs.

Rajaraman and Vasishtha (2002) is an empirical study provided an evidence of significant bivariate relationship between an operating inefficiency indicator and the problem loans of public sector banks.

Sathe (2003), while studying the performance of Indian commercial banking sector found that the public sector banks performed better than their private sector counterparts with regards to their overall efficiency. He also raised concern over the higher level of Non-performing assets (NPAs) in the banking system and suggested that policies be implemented to reduce the bad loans.

Safakli (2007) did an extensive study of credit risk associated with the banking sector and Northern Cypress and found that the credit risk ratios were indicative of

the credit risks associated with the banking sector and correlated the risk ratios with key macroeconomic indicators.

Radhakrishnan and Ravi (2009) state that capital requirements not only protect investors but also safeguard them against the possibility of failure of big banks. They also improve market discipline.

Kumar (2010) conducted a study in Delhi to find out the various methodologies used by the banks in their operational risk management activity complaining the rules and regulations. The study reveal that the operational risk management functions is predominantly gaining importance in banking operations in India along with credit risk. He concluded that the banks are ready to improve their existing risk management framework in accordance with Basel II to deal with risks more effectively.

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Ayyappan and Ramachandran (2011) conducted a study of 22 public sector and 15 private sector banks to predict the determinants of the credit risk in the Indian Commercial banking sector by using an econometric model. The outcome of the study is the non-performing assets had a strong and statistically significant positive influence on the current non-performing assets. They opined that the problem of NPA is not only affecting the banks but also the whole economy.

Gupta and Meera (2011) feel that Basel II regulations have led to a significant improvement in the risk structure of banks because their capital adequacy has improved. Also, there exists an inverse relation between CAR and Non-Performing Assets (NPAs), which clearly indicates that due to capital regulation, banks have to increase their CAR which leads to decrease in NPAs.

Choudhary Navin (2011) designed to develop an internal credit rating model for banks which improves their current predictive power of financial risk factors. He highlights how banks assess the creditworthiness of their borrowers and how can they identify the potential defaulters so as to improve their credit evaluation. He concluded that the business of lending has given rise to credit risk, which is the risk of default.

CHAPTER III AN OVERVIEW - SBI

3.0 STATE BANK OF INDIA

On 1st July State Bank of India was constituted under the State Bank of India Act 1955, for the purpose of taking over the undertaking and business of the Imperial Bank of India. On September 1959, the State Bank of India (subsidiary bank act was passed). On October State Bank of Hyderabad become the first subsidiary of SBI. In 1960 State Bank of Jaipur, State Bank of Bikaner, State Bank of Indore, State Bank Travancore, State Bank of Mysore, State Bank of Patiala, State Bank of Saurashtra become subsidiaries of the bank. SBI is that country's largest commercial bank. The government-controlled bank, the Indian government maintains a stake of nearly 60 per cent in SBI through the Central Reserve Bank of India and also operates the world's largest branch network. As of March 31st 2012, the bank had a network of 20193 branches, including 5096 branches of its five associate banks. management, custodian services, general insurance (non-life insurance) and primary dealership in the money market.

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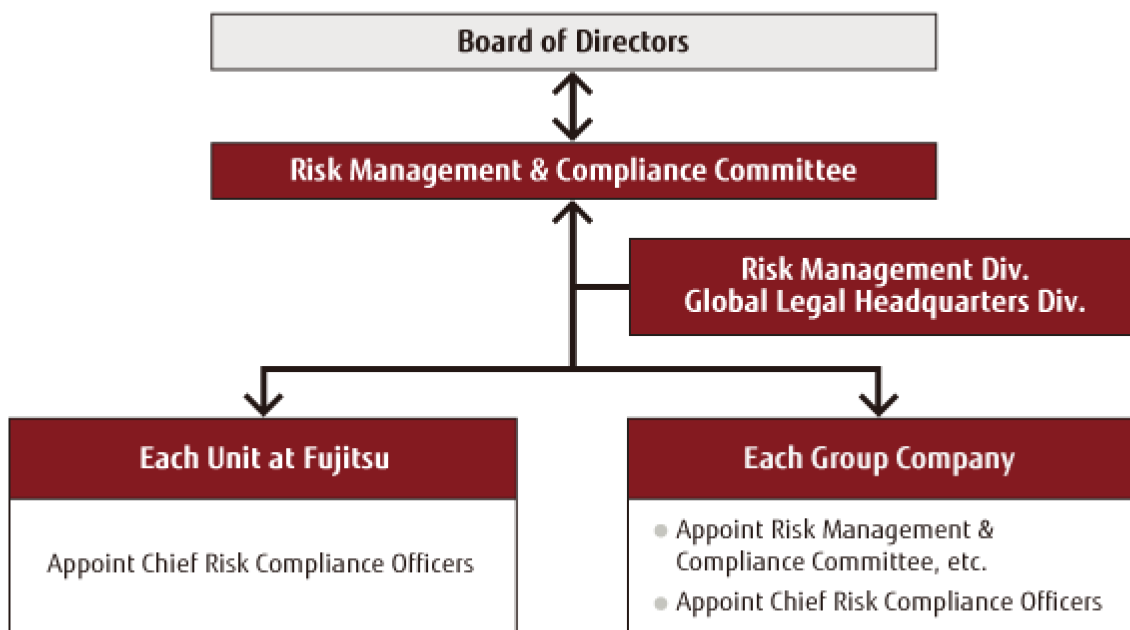
In addition to banking, the company through its various subsidiaries provides a range of financial services, which includes life insurance, merchant banking, mutual funds, credit card, factoring, security trading, pension fund management, custodian services, general insurance (non-life insurance) and primary dealership in the money market.

3.1SBI and Associates

This group comprises of State Bank of India and its seven subsidiaries viz., State Bank of Patiala, State Bank of Hyderabad, State Bank of Travancore, State Bank of Bikanar and Jaipur, State Bank of Mysore, State Bank of Saurashtra and State Bank of India.

3.2 Risk Management in SBI

From the chart it is clear that an independent risk governance structure is in place for integrated risk management covering enterprise, credit, market, operational and group risks. This frame work visualizes empowerment of business units at the operating level with technology being the key driver enabling identification and management of risk at the place of origination.



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CHAPTER IV

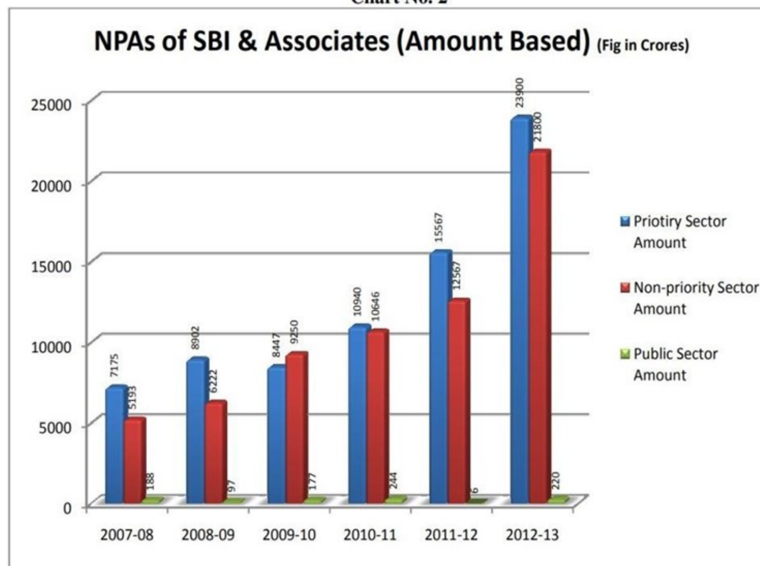
DATA ANALYSIS AND INTERPRETATIONS

Non-Performing Assets (NPAs)

Position in SBI and Associates Non-Performing Assets (NPAs) are the primary indicators of credit risk. Capital Adequacy Ratio (CAR) is another measure of credit risk. CAR is supposed to act as a buffer against credit loss, which is set at 9 per cent under the RBI stipulation companies against the Basel Committee stipulation of 8%.

Years	Priority Sector		Non-priority Sector		Public Sector		Amount
	Amount	% to total	Amount	% to total	Amount	% to total	
2007-2008	7175	57.15	5193	41.36	188	1.50	12556
2008-2009	8902	58.49	6222	40.88	97	0.63	15220
2009-2010	8447	47.76	9250	51.75	177	0.99	17874
2010-2011	10940	50.11	10646	48.77	244	1.12	21831
2011-2012	15567	55.32	12567	44.66	6	0.02	28140
2012-2013	23900	52.30	21800	47.70	220	4.90	45700

Chart No. 2



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CONCLUSION

Risk management is not something new. Every employee joining a bank starts learning about the risk inherent in banking operations from day one. Risk management is one of the most important practices to be used especially in banks. Risk is threats of banks of course; RBI is issuing guidelines from time to time to maintain solvency of each and every banks. From this view, internal management of SBI and associates should be checked frequently against this possible risk. And it is also important that the external credit and risk management agencies should be consulted by each other regularly so that risk can be controlled and managed. An efficient risk management system is the need of time.

This paper has provided an overview of 1) the conceptualization of risk management, 2) the management of credit risk by SBI and associates, 3) The components of credit risk management in SBI and associates were analyzed i.e., Non-performing Assets for the period of six years and capital adequacy ratio for the period from 2008 to 2013 (six years period). Due to time and study constraint, we have covered only credit risk management. Credit risk management is a vast subject and it is very difficult to cover all the aspects of credit risk management in SBI and associates.

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