

## OPERATIONAL RISK MANAGEMENT PRACTICES OF PRIVATE SECTOR BANKS IN KERALA

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### Abstract

Risk management is the most important subject in finance and it is the foundation of the modern Finance theory. In view of growing complexity of bank business and the dynamic operating environment, Operational Risk Management has become very significant, especially in the financial sector. Operational Risk management analysis, in a broad sense, is any method – quantitative and qualitative for assessing the impact of risk on decision. Operational Risk management is applicable to of proactive strategy to plan, lead, organize and control the wide Variety of risks that are rushed into the fabric of an organizations daily and long – term the decision maker choose a course of action, give a better understanding of the possible outcome occur. The present attempts to review the operational risk management practices followed by the two selected private sector banks namely Federal Bank Ltd and Catholic Syrian Bank Ltd and suggests suitable measures to minimize the operational risks.

**Keywords :** Risk management, operational risks, Federal Bank Ltd and Catholic Syrian Bank Ltd.

### 1. Introduction

Commercial banks are a type of financial institution and intermediary. It is a bank that lends money and provides transactional, savings, and money market accounts and that accepts time deposit. While performing these activities there could be different inherent risks that the banks are to bear. Thus, to serve its purpose and to achieve its objectives of being profitable, safe and having liquidity to the interest of its shareholders in particular and to the public in general, it need to undertake and have a health risk profile and sound risk management system. Risk is something which is unfavorable to the business and whose happening can't accurately forecast. The risks differ in their natures and occurrences pertaining to different business activities. That's to say that certain risks are particular in their natures that specifically affect the operations of a particular firm or industry, for instance banking industry. Likewise, risks associated with banking service differ by type of service rendered. Banks face a number of risks in order to conduct their business, and how well these risks are managed and understood is a key driver behind profitability, and how much capital a bank is required to hold. The major risks associated with banks are Credit risk, Market risk and operational risks.

The importance of risk management of banks recognized globally in the later decades of the 20<sup>th</sup> century the major financial powers felt the importance of unified guidelines of banking process and better management of risk. BASEL convection put forward guideline in 1988 and 2004 for credit risk management and operational risk management respectively. In the importance of the operational risk management in banks where identified with the 2004 BASEL recommendation which was followed by RBI in formulating its guideline for effective risk management practices. The operational risk identification is the major question in this sector and fact that no major studies thrown light to this area increase the relevance of the research. The researcher attempt to find out the major contributory factors of operational risk and exciting operational risk management practices of the private sector banks in Kerala.

### 2. Objective of the Paper

The objective of the present paper is to review the existing operational risk management practices of private banks with particular reference to Federal bank and catholic Syrian bank Pvt Ltd. and to suggest suitable measures for minimizing the risks.

### 3. Methodology and Database

The present research work is descriptive in nature. The study based on both secondary and primary data. The secondary data have been collected from Books, Research dissertations, Website and Research journals. The Primary data have been collected from bank managers. For this purpose, the following sample procedure has been followed.

- **Selection of Sample Private Sector Banks:** The Federal Bank Ltd and Catholic Syrian Bank Ltd have been selected as sample private sector scheduled commercial banks for the study, on account of their predominant role in risk management.
- **Selection of Sample Districts:** Five districts namely Ernakulum, Idukki, Thrissur, Plakkad and Malappuram have been selected for the detailed study. The selection of the five districts has been done due to the fact that the head offices of the sample bank are located in the districts.

- **Selection of Sample Branch Managers:** In the five sample district, Federal Bank operates 275 branches and Catholic Syrian Bank operates 185 branches in the sample district. A picture of the same is shown in the table 1.

**Table 1: Sample Frame**

District	Branch Managers of Federal Bank	Branch Managers of Catholic Syrian Bank
Ernakulum	112	44
Idukki	26	4
Thrissur	67	103
Malappuram	40	18
Palakkad	30	16
<b>Total</b>	<b>275</b>	<b>185</b>

**Table 2: Sample Size**

Sample unit	Sample Size
Catholic Syrian bank	123
Federal bank	165
<b>Total number of sample</b>	<b>288</b>

The method of convenient sampling has been adopted for the selection of sample branches.

#### 4. Result and Discussion

##### 4.1. Operational Risk Management Practices of Federal Bank Pvt Ltd

The survey data revealed that the Federal Bank considered the operational risk management factor as a relevant element in the virtue of staying competitive. The board has established excellent operational risk tolerance level for better strategic direction. The strategic direction of the bank stay in line with the operational risk management and the board sculptures excellent operational risk policies for strategic direction. The management shows excellent involvement in framing operational risk policy. The operational risk policies are framed in accordance with the people, process and systems of the banks .the policy fairly define the jobs of each individual entity and operational risk management policy is regularly defined. The operational risk management policy has a faire level of implementation at branch level and the policy tackle its market risk at faire level the human resource policy of bank is framed by into extend to operational risk management policy

The organizational structure of the bank is made in mind the risk tackling to measures the bank has made good effort to identify operational risk and the bank has a good monitoring system. The bank has a good system of internal control and the actual situation of bank confine to actual level of acceptable level of risk management. The control system of bank has fair level of integration. The compliance officer has good level of responsibility and compliance issues are given good level recognition. Here the qualitative tools of operational risk management highly fit to risk profile of the bank .the backup data is highly protected there smooth follow of communication between different levels. The banks make a very good performance in this respected by 50 point out of 55.

##### 4.2 Operational Risk Management Practices of Catholic Syrian bank Pvt Ltd

The survey data revealed that the board has established excellent risk tolerance levels. The operational risk management strategies has good flexibility with other risks, the board of directors have should excellence in approving operational risk management policy .They have excellent involvement in framing operational risk management policy . The operational risk management policy identifies people, process and systems in a good manner. The policy has good definition about role of each individual identity. the bank make a good review of operational risk management policy an a regular basis , the policy is implemented at branch level at a good degree . the bank have reviews an frames operational risk management policy with a fair regularity and they framed policy is excellently at the branch level . It can also be noted that the present market risk are effectively managed by the policy and stays in line with the excellent human resource management policy of the bank

The structure of bank highly correlate with the risk management measures taken and the bank is making good efforts in identifying the risk. The bank has good reporting system and monitoring system; the operational risk management framework

is controlled and verified at a fair level. the bank has only an affordable level of operational risk and the bank has an excellently integrated risk controlling system the responsibility of compliance officer is defined with a good level of accuracy and the compliance issue which compliance officer confront are treated as really important to the bank . The quantitative and qualitative measures excellently fit to the banks risk profile and the bank is able to recover back up data with a good accuracy in situation of emergency. There is excellent flow of information from low level to top level and vice versa.

### 5. Demographical Profile of the Respondents

A brief profile of the sample bank managers is presented in the following Table.

**Table 3: Summarized demographical Profile of the Respondent**

S. No	Demographical Variable	Frequency	Percentages
1	<b>Gender</b>		
	Male	210	72.9
	Female	78	27.1
	<b>Total</b>	<b>288</b>	<b>100.0</b>
2	<b>Age of Respondent</b>		
	30-39	65	22.6
	40-49	128	44.4
	50-59	95	33.0
	<b>Total</b>	<b>288</b>	<b>100.0</b>
3	<b>Qualification of Respondent</b>		
	Graduate	109	37.8
	Post Graduate	98	34.0
	Professional (CA, MBA.CMA.LLB etc)	81	28.2
	<b>Total</b>	<b>288</b>	<b>100.0</b>
4	<b>Scale of Respondent</b>		
	Scale II	120	41.7
	Scale III	125	43.4
	Scale IV	43	14.9
	<b>Total</b>	<b>288</b>	<b>100.0</b>
5	<b>Year of Service</b>		
	1-10	75	26.0
	11-20	159	55.2
	21-30	54	18.8
	<b>Total</b>	<b>288</b>	<b>100.0</b>
6	<b>Year of Experience in Operational Risk Dept.</b>		
	1-10	75	26.0
	11-20	159	55.2
	21-30	54	18.8
	<b>Total</b>	<b>288</b>	<b>100.0</b>

Source: Primary Data

The table depicted the demographical profile of the banks shows a domination of male (72.9 %). Most of the respondent falls within the age group of 40-49. Majority of the bank managers are graduate and post graduate percentages are 37.8 and 34 respectively. It is evident that most of the bank managers' salary scale third category and salary scale second category. Most of the employees have 11-20 years service in banking and operational risk management department.

## 6. Operational Risk Management practices (Branch level)

An attempt is made to find out the role of management in framing operational risk management policy and internal control system and to what extent this attempt is complimented by the efforts of employees. Summarized analysis in this respect is given below.

**Table 4: Operational Risk Management practices**

Policy and procedure	Frequency (fed)	%	Frequency (Csb)	%
Excising management system				
v good	99	66	76	62
Good	66	40	47	38
Operational risk management policy				
v good	57	34	72	59
Good	108	66	51	41
Excising systems and procedures				
v good	96	59	76	62
Good	69	41	47	38
Current manual in areas of operations and procedures				
v good	98	60	107	87
Good	57	40	16	13
<b>Internal Control and Reporting</b>				
Effectiveness of the internal audit tackle OR				
v good	86	52	63	51
Good	79	48	61	49
Logic and suitability of the reporting format				
v good	75	46	44	36
Good	90	54	79	64
Regular and timelines is the reporting system				
v good	87	52	78	48
Good	55	48	68	56
The speed and promptness of communicating				
v good	69	41	47	38
Good	96	59	76	62
<b>Role of Employee</b>				
Degree of clarity of the role of individual				
v good	57	40	16	13
Good	98	60	107	87
Degree of confidentiality of various transaction				
v good	86	52	72	51
Good	79	48	59	41
Role of compliance officer				
v good	122	73	88	72
Good	43	27	35	22

Source: Primary Data

Table 4 shows that the current operational manual properly identifies people, process, and system of the bank and regularly monitor the operational risk policy. The internal control and reporting system of the bank is logically sculptured for the effective tackling of operational risk in timely and prompt manner. The transaction remain confidential with the authorized person as his and responsibility is clearly define which include that of the compliance officer.

### 6.1 Regular Staff Rotation

Regular staff rotation of bank employee in branch level the result is shown in table Table 5.

**Table 5: Staff Rotation**

Name of the bank	Staff rotation		Total
	Yes	No	
Federal Bank	165	0	165
Catholic Syrian Bank	123	0	123
<b>Total</b>	<b>288</b>	<b>0</b>	<b>288</b>

Source: Primary Data

Table 5 shows that staff rotation is carried out regularly in the banks, as a tool of operational risk management. This helps the management in effective location of operational risk such as fraud and clerical mistakes.

### 6.2 Risk Management Cell

Existence of risk management cell at branch level is represented and the details are shown in the table 6.

**Table 6: Risk Management Cell**

Risk management cell	Name of the bank		Total
	Fed	Csb	
Yes	0	0	0
No	165	123	288
Total	165	123	288

Source: Primary Data

It clear from table 6, that Risk Management Cells are absent in branch level of both the banks.

### 6.3 Role of Compliance Officer

The Role of compliance officer in branch level is analyzed and the results are shown below.

**Table 7: Role of compliance officer**

Timely report	Name of the bank		Total
	Fed	Csb	
Yes	117	71	188
No	48	52	100
Total	165	123	288

Source: Primary Data

Table 7 shows that 71% of the federal bank managers and 58 % of the catholic Syrian bank managers are of the opinion that the compliance are timely reported to the top management by the compliance officer.

### 7. Conclusion and Suggestions

It is evident from the analysis that the current operational manual properly identifies people, process, and system of the bank and regularly monitors the operational risk policy. The internal control and reporting system of the bank is logically sculptured for the effective tackling of operational risk in timely and prompt manner. The transaction remain confidential with the authorized person as his responsibility is clearly define which include that of the compliance officer and the bank have staff rotation is carried out on regularly. It help to the management eliminate operational risk at a level.

#### **The following suggestions are offered to minimize the operational risks in the Private sector banks.**

Bank can introduce a database management system, it will help the banks to record the incidents associated with operational risks timely and accurately that will be strengthen the capability of quantifying those risks, and eventually will boost the prediction capability. A regulatory and supervisory body, the central bank should establish a data base management system in which the historic loss data of the peer banks will be stored and used when need arise in the measurement (quantification) of their inherent loss events. Bank can introduce risk management cell at branch level, this will help to identify the risk at the



initial stage and take apt measure to eliminate risk at the earlier stage, and the manager of the branch should be person in charge of this cell.

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