Effects of Credit Risk Management on Financial Performance: A study on the Indian Commercial Banks

Krishnendu Ghosh
Department of Commerce, Sidho-Kanho-Birsha University

Abstract

Purpose of the Study: High credit risk is a result of economic downturn of commercial banks and financial institutions. It is inherited with the nature of their business and needed to be managed well for their survival. The present study finds whether credit risk has a dual impact on commercial banks' financial performance in India.

Study design/methodology/approach: For the study, secondary financial data are taken from published annual reports of 20 commercial banks consisting of 12 public sector and 8 private sector commercial banks during 2013-14 to 2018-19. Credit risk of commercial banks is measured through Non-performing loan ratio (NPLR), Capital adequacy ratio (CAD). The financial performance of banks is measured through two alternative measures of profitability namely return on assets and return on equity. Pooled data have been used for multiple regression analysis.

Findings: Empirical study results reveal mixed and varied indications about credit risk management and its influence on the financial performance of commercial banks. The study results also indicate that the profitability of Indian commercial banks is declining due to increase in NPAs. Inspite of having a strong capital adequacy ratio, profitability has not increased every year.

Implications of the study: Present study is helpful to the various stakeholders in the banking industry to know how various types of credit risk variables behave with financial performance.

Keywords: *Commercial banks, NPAs, profitability, credit risk management, India.*