



Effect of Risk Management Practices on Banks Performance Moderating Role of Managerial Expertise as a Competitive Edge

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Abstract

The main aim of this research study is to determine the effect related to risk management practices on a bank's performance in presence of managerial expertise. Expertise and low overheads are known to be an advantage on competitors in the market. In this study, we propose to use managerial expertise as a competitive force to drive forward the ventures in the industry. Banking is known to be an intensely competitive industry in the business globe. It greatly requires risk management and performance enhancement managerial expertise. The random method was utilized for data collection through summated scale on five Likert points. Data collected from 70 operational managers, branch managers, and senior risk managers of the bank. This study utilized reliability analysis, correlation, and regression analysis by using SPSS v.26. Results illustrated that effective risk management practices significantly influence the performance of banks with the moderating role of expertise based on managerial capabilities. This study prone to some limitations foremost inadequate sample size and cross-sectional study which influences the generalization of the study, root cause of the small sample size is a limited number of banks in Azad Kashmir. Moreover, this study recommends to bankers need to pay attention to risk management practices as well as managerial expertise to improve the performance of banks and achieve competitive advantage by using that managerial expertise

Keywords: Risk Management, Managerial Expertise, Bank's Performance, Risk Management Practices


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1) INTRODUCTION

The past decade's world is witnessing one of the most shocking financial failures. The crisis effect was universal hits in all sectors of the worldwide businesses. The supreme affected sectors are financial sector, especially banking sectors. The banking sector witnessed not only for dramatic disappearance but also became a most consistent target for tough regulation's community anger and academic blame or criticism. There are many justifications on the root of the current financial disaster. One factor that is received more attention during the crisis that is risk management disclosure. It looks like very important tool; which banks use to try to achieve acceptability by the public and regulators.

The term risk based on financial is uses like an umbrella term in which multiple risks are linked with financing. It constitutes transactions based on financial considerations, which include company loans at risk of default (Hassan Al-Tamimi & Mohammed Al-Mazrooei, 2007). Financial risk management is defined as maximization of performance and reducing the cost associated with it in the banks. The behaviors of the bank managers to the risk and corporate governance effect on the risk-management acuties. Lintner (1975) stated that healthy risk management framework helped banks to enhance ability to participate in market and reduce financial exposure. In the current era, the financial risk management involves a very vital role in operation of banks. All banks are exposed large numbers of risks considered as credit risk, foreign exchange risk, interest-rate risk and liquidity risk among others.

It is a very complex task for any financial institution to manage their risks, and progressively important where economic occasions and economic system are associated in the world. Most of the banking regulators and financial institution in the world are emphasized risk management as a basic component of organization's long-term success (Pérignon & Smith, 2010). Management should focus on organization's ability to find out and manage the future risk for the long-term success rather than focusing on current, previous, or historical performance. On the point is no finalized definition of hazard or risk. If we study extensive literature of risk, then we find concept of risk considered as expected value, possibility spreading, as an occasion or event. There is following information of risks.

1. The risk is an event or situation, where approximately of values of human is considered at stake and outcome is said to be uncertain (Aven & Renn, 2009).
2. Risk is ambiguous consequences of occasion or activity related to something values possessed by human.

Financial risk has only one category of the wide area of risks. Additionally, financial risk divided into three-subcategories first category is credit risk; second, one is liquidity risk, and third one is market risk. The third one market risk classified into four subcategories first one is foreign exchange risk, second is interest-rate risk, third is commodity risk and forth is equity risk. There is different definition of financial risk management, some researcher. The financial risk management states to practice of financial value creation within the firm to manage exposure, market

risk and credit risk by using financial instruments. There are following objective of current research study.

To determine impact of Risk management practices on bank's Performance in presence of Managerial Expertise.

This research study utilized survey method, which provides the objective kind of information that, studied. Study used summated scale, which measures on five-point Likert scale. Target population is operational manager of banks, branch manager, senior risk managers and bank practitioners in the state of Azad Jammu and Kashmir. Moreover, these bankers belonged to long-familiar banks in the state. Random sampling technique utilized because of long-familiar population. These bank's branches visited August 2018 to September 2018 and distributed 100 questionnaires among managers and practitioners and observed 70 were suitable filled and useful.

2) LITERATURE REVIEW

Risk management is the process of comprehensive planning, organizing, directing and controlling funds to accomplished objectives in which unexpected event (Good or Bad) may happen (Verbano & Venturini, 2013). The word risk in banking sector, mostly researchers utilized in research (Gallati, 2003). There are fundamentally two steps of risk management the one step is an origin of risk identification, and the second step is to develop a method to solve risk (Rosman, 2009).

The major aims of bank management to enhance shareholder's return boosting performance of banks. Banks face different kind of risks such as interest-rate risk, credit risk, foreign exchange risk, market risk, liquidity risk, operational risk, off-balance risk, insolvency risk and technology and operational risk (Tandelilin et al., 2007). The motivation of banks comes from the risk, which can direct to the banks' loss. The risk-management issue in banking sector has a not only larger impact on banks but has an also greater impact on growth of economy (Tandelilin et al., 2007). The recently focused by risk management authority on ensuring regulatory compliance and developing control variable rather than improving financial results or outcomes (Vedenov et al., 2006). It is noted that well managed and controlling the risk can lead to enhance the worth of the firm. Management of financial risk is to reduce monetary troubles and associated costs.

There is a plethora of studies conducted on financial risk management. The following research study attempted to summarize results of some related studies. Hassan Al-Tamimi & Mohammed Al-Mazrooei (2007) founded that banks of UAE are slightly effective at handling risk identification, understanding risk, risk monitoring and risk assessment is most central and influence variable in risk-management practices. This research study also inspected that clear difference between UAE banks and foreign banks participating in the risk assessment, monitoring and controlling the risk.

Research study conducted by Rosman (2009) determined that the significant

variance among the risk-management process and risk management practices. All determinants of Risk Management Process are significantly associated with Risk-management practices. Furthermore, Khalil & Ali (2015) showed that the risk assessment and risk analysis, risk management practices and risk analysis has significantly influence, risk monitoring and risk identification has insignificantly influenced on risk management practices. Moreover, According to Nazir et al. (2012) mentioned that Pakistani banks are efficiently performed in risk credit risk analysis, risk understanding and risk monitoring, Channar et al. (2015) conventional banks affectively managed risk management process as compared to Islamic bank, this study also illustrates that the risk management has negative and insignificant association with operational performance and positive link with financial performance.

A study illustrated that the influence of URM, RI, RM and RA on risk-management practices and also explore risks which Islamic banks faced frequently are interest-rate oriented risk, liquidity risk and operating risk (Khattak et al., 2013; Muhammad et al., 2018). This is why efficiently management of risk is really essential for the Islamic banks (Hassan Al-Tamimi & Mohammed Al-Mazrooei, 2007). Additionally, research study shows that the risk-management process is very essential for banking sector in Pakistan, this is not necessary for only the regulatory requirements but also very essential for the performance of the banks (Pulka et al., 2018) concluded stronger risk management can reduce risk exposure and increase bank's value (Ellul & Yerramilli, 2013).

Making decision rely not only on collecting business intelligence but also depends on the competency of individuals (Lönnqvist & Pirttimäki, 2006). A study illustrated that managerial expertise significantly positive influence on the organization performance (Alfayo Bonface 2015).

A study concluded that an organization can achieve his objectives when the employee of that organization has skills (Panagiotakopoulos, 2012). Managerial competency defined by Bhardwaj & Punia (2013) is a combination of skills and knowledge, which is required for the effectiveness of the organization. Researchers examined that there is positive relation between organization performance and managerial competency (Hawi et al., 2015; Levenson et al., 2006; Purohit & Shah, 2018; Šparl et al., 2013) also association between managerial competency and business performance (S. Ali et al., 2013; Velu & Manxhari, 2017).

Managerial skills defined that the combinations of behaviors, which are very fruitful for the organizations' performance without that in many cases managerial knowledge does not have any effect (Al-Madhoun & Analoui, 2002), capability to convert info and knowledge into practices (Bharadwaj, 2000). A study examined there is a positive and direct relationship between managerial skills and bank's efficiency (Javadin et al., 2010). Furthermore, a study Rehman & Anwar (2019) conducted in Pakistan to examine effect of competitive strategies on the performance with mediating role of ERM practices and found significant direct and indirect effect. The major limitation was that the ERM practices measure with indicators not with determinants. The study recommended to increase ERM practices to improve

the organizational performance (Saeidi et al., 2019). Furthermore, study explored positive and significant impact on performance (Sarfraz et al., 2018; Sleimi, 2020). Studies also suggested that the ERM practices are compulsory most of the banks in Nigeria (Dabari & Saidin, 2016).

3) METHODOLOGY

3.1) RESEARCH DESIGN

This is the explanatory study which is based on the theory to test the hypothesis. Primary data was collected from the banking managers (operational managers, branch managers, and senior risk manager and bank practitioners). Current study also employed cross-sectional method due to availability of time and resources which is also showed valid results (W. Ali et al., 2019; W. Ali et al., 2020).

3.2) SAMPLE SIZE AND METHOD

Current study used the non-probability (pic and drop) sampling method to elaborate effect of risk management practices on performance of banks in presence of managerial expertise. The population was unknown and unavailability of sampling frame the non-probability sampling is quite useful and appropriate. There were approximately 105 questionnaires collected and 35 were omitted due to missing values >5% and respondents were not engaging with the questionnaires. The response rate which is 66.66% was consider enough (Mugenda & Mugenda, 2003), stated that response rate >50% consider enough and >60% consider good.

3.3) INSTRUMENT SCALE

Self-administrated and adopted questionnaires distributed among managerial position respondents. However, Questionnaires consists on designation of respondent and qualification. Second category consists of practices related to risk management which includes understanding risk identification, risk monitoring and assessment of risk used (Hassan Al-Tamimi & Mohammed Al-Mazrooei, 2007). Managerial skills, managerial competency used to measurement of managerial expertise. Organizational performance measured by financial performance used by (Zehir et al., 2016) developed by (Baker & Sinkula, 1999; Lynch et al., 2000) and performance of employees developed by (Fuentes-Fuentes et al., 2004; Rahman & Bullock, 2005).

3.4) ANALYTICAL TOOLS AND METHODS

Current study utilized the SPSS v. 26 for the data cleaning, screening and analyzing. Study employed the reliability, correlation and regression through SPSS syntax process. All questionnaires were measured on the 5-likert scale which is universal scale for the data collection.

4) RESULTS AND INTERPRETATION

Table 1: Gender

| | | Frequency | Percent | Cumulative Percent |
|-------|--------|-----------|---------|--------------------|
| Valid | Male | 67 | 95.7 | 95.7 |
| | Female | 3 | 4.3 | 100.0 |
| | Total | 70 | 100.0 | |

This above Table 1 shows that 67(95.7%) respondents are male, and 3(4.3%) respondents are females. The low female percentage as compare to male indicate that some social or cultural factor influence on female job. In addition, Azad Kashmir is male dominant society that is also reason for the large respondents were males.

Table 2: Experience

| | | Frequency | Percent | Cumulative Percent |
|-------|-------|-----------|---------|--------------------|
| Valid | 1-5 | 45 | 64.3 | 64.3 |
| | 6-10 | 25 | 35.7 | 100.0 |
| | Total | 70 | 100.0 | |

The above Table 2 states that 45(64.3%) of the participants have experience between 1-10 years and 25(35.7%) had 6-10 years' experience in the banking field. Therefore, majority of the respondents were new in the banking field.

Table 3: Designation

| | | Frequency | Percent | Cumulative Percent |
|-------|---------------------|-----------|---------|--------------------|
| Valid | Operational Manager | 38 | 54.3 | 54.3 |
| | Branch Manager | 30 | 42.9 | 97.1 |
| | Senior Risk manager | 1 | 1.4 | 98.6 |
| | Bank Practitioners | 1 | 1.4 | 100.0 |
| | Total | 70 | 100.0 | |

The above Table 3 illustrate that designation of participants 38(54.3%) were operational manager, 30(42.9%) were branch managers, 1(1.4%) was senior risk management officer and 1(1.4%) was bank practitioner. Results shows that most of the respondents were operational and branch manager.

Table 4: Reliability Analysis

| Variables | Cronbach's Alpha | No of Items |
|-----------------------|------------------|-------------|
| Risk Identification | .777 | 5 |
| Understanding risks | .711 | 7 |
| | .851 | 6 |
| Risk Monitoring | .767 | 7 |
| | .735 | 8 |
| Risk Assessment | .858 | 7 |
| Managerial Skills | | |
| Managerial Competency | .842 | 10 |
| Bank's Performance | | |

This Table 4 illustrates reliability analysis, which indicates the internal consistency is good between substantive variables. Results illustrated that the risk identification scale has 0.777, Understanding risk has 0.711, risk monitoring has 0.851, risk assessment has 0.767, managerial skills, managerial competency, managerial experience and organizational performance has 0.735, 0.858, 0.768 and 0.842 internal consistency respectively. All above variable's value are ≥ 0.70 , which shows all variables are internally consistent. Nunnally (1978), suggested the value ≥ 0.70 is acceptable for basic research and internal consistency between 0.90-0.95 in major decision making consider excellent.

Table 5: Correlation Analysis

| | UR | RI | RA | RM | MS | MC | BP |
|----|--------|--------|-------|-------|-------|--------|----|
| UR | 1 | | | | | | |
| RI | .541** | 1 | | | | | |
| RA | .584** | .596** | 1 | | | | |
| RM | .056 | .021 | -.125 | 1 | | | |
| MS | -.232 | -.176 | -.117 | .180 | 1 | | |
| MC | .085 | -.094 | -.175 | .221 | .076 | 1 | |
| BP | .077 | -.154 | -.077 | -.177 | -.065 | .757** | 1 |

** . Correlation is significant at the 0.01 level (2-tailed).

The above Table 5 represents the relationship between variables. This analysis shows two things first is strength and second is direction. Strength shows how much close to one and directions shows positive or negative association between variables. There is no link between both variable when value = 0, weak relationship when value lies between $\pm 0-0.3$, moderate relationship when values lies between $\pm 0.3-0.7$ and strong relationship when value lies between $\pm 0.7-1$ (Ratner, 2009). There is moderate association between understanding risk, risk identification and

assessment, and low link between managerial skills, competency and experience.

Table 6: Moderation Analysis

| Model Summary | | | | | |
|---------------|----------|--------|-------|---------|------|
| R | R-square | F | df1 | df2 | p |
| .512 | .262 | 21.017 | 3.000 | 299.000 | .000 |

| Model | Coefficient | SE | t | p |
|-----------------|--------------|--------------|---------------|-------------|
| CONSTANT | 1.399 | 0.105 | 13.324 | .000 |
| ME (M) | 0.656 | 0.122 | 5.377 | .002 |
| ERM (X) | 0.759 | 0.083 | 9.145 | .000 |
| INT_1 | 0.345 | 0.112 | 3.080 | .003 |

Interactions: int_1 = ME xERM

Outcome Variable: OP (Y)

The above Table 6 indicates consequences of moderation analysis recommended. In this considered method, regression analysis is done by utilizing SPSS Syntax Process. Result of Risk Management Practices (X) shows significant association with Organization Performance (Y) (Coefficient. 0.759, $p < 0.05$). Managerial Expertise (M) and Organization Performance (Y) has significant relationship (Coefficient. 0.656, $p > 0.05$) and Interaction term (ME x ERM) is significant (Coefficient. 0.345, $p < 0.05$). Based on results, we can say that Managerial Expertise is playing vital role as moderating variable in this model. Therefore, we can conclude that our finding support moderation of Managerial Expertise between Risk Management Practices and Organization Performance.

5) DISCUSSION

From the results of descriptive statistics, a large percentage of working staff in AJ&K is male. There are many reasons, such as AJ&K is male dominant areas as well as due to cultural implications female are mostly not allowed to work in banking sector. These results are coherent with the results of (Ghulam et al., 2019). The findings of our research study further elaborate that risk identification, understanding risks, risk monitoring, risk assessment, managerial skills, managerial competency, organization performance are consistent on concrete basis as internal reliability is within the threshold value. We can reveal with the results that demographic analysis can be a vital difference to influence Risk Management Practices shows significant association with Organization Performance.

Therefore, these variables as considered as sound for this research results and inferences can be drawn. Our analysis of correlation of variable show consistency with range of correlation values. As per results of correlation values, all variables are depicting moderate association as well as somehow low link between variables. these correlation results are coherent with the results of (Wu & Wu, 2014). According to results of Moderation Analysis, Risk Management Practices shows significant association with Organization Performance. Managerial Expertise and Organization Performance has significant relationship Interaction term is significant. Risk Management Practices should be dealt in very serious manner as it has much significant association with Organization Performance.

5.1) CONCLUSION

Worth sharing results illustrate that risk management practices can improve organization performance which is very essential for long-term benefits. This study also shows that managerial expertise (Managerial skills, Managerial competency and Managerial Experience) can also influence on the organizational performance significantly. Management of the banks has managerial expertise in the specific field, which is beneficial for organization to reduce risk exposure.

Based on results and observation we recommended organizations should need to focus on risk management practices as well as managerial expertise to improve organizational performance which necessary for organizational life and to get competitive advantage. We can increase managerial expertise through on job training or off job training. As we know that risk management practice has positive impact on performance of bank. Result of study also similar with the studies of (Girangwa et al., 2020; Rehman & Anwar, 2019). Study also found that the moderating role of managerial expertise also playing significant role. This study employed moderating role between the ERM practices and bank's performance which is the uniqueness and contribution of the study.

5.2) RECOMMENDATION

Recommending was made based on results of study. Managers of the banks should focus on the ERM practices for managing the risks on daily basis. Researchers stated that any kind of strategy you can used but the risk management is complementary. While managing risk managerial expertise is necessary for performance of banks, which is associated with the daily operations. Study recommended that the managerial expertise can plays as competitive advantage for the banks. Study also recommended that the banks should focus on training and development of employees, which plays crucial roles for the banks.

5.3) LIMITATION AND FUTURE SUGGESTION

Present study has limitation likes prior studies. The major limitation of this study is sample size is small and cross-sectional approach which might be has some impact on the generalizability of the study. We suggested to future scholars to conduct study to examine comparison between Islamic and conventional banks to determine

which bank's management have high managerial expertise. This study conducted on the organization such as insurance companies. Future study may conduct to take other component to measure managerial expertise. Future study should be conducted with longitudinal approach and new dimension should be used for managerial expertise.

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