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Effect Of Risk Management Practices On The Financial Performance Of Commercial Banks In Iraqi

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Abstract

During the last years, banks have been facing heavy mergers and acquisitions, in particular, universal and commercial banks all over the world. Such activities hamper the degree to which the Financial System is included and decrease the public's trust. The research aims to demonstrate the need to pay more attention to risk management for banks. In this study, the main issue was to examine how risk management activities in Iraqi commercial banks help boost these banks ' performance. The study revealed that the key variable to evaluate the performance of the commercial banks is risk management. The study further stated, when counterparties fail to meet their commitments, risk management substantially impacts the financial performance of commercial banks.

Efecto De Las Prácticas De Gestión De Riesgos En El Desempeño Financiero De Los Bancos Comerciales En Iraq

Resumen
Durante los últimos años, los bancos han enfrentado fuertes fusiones y adquisiciones, en particular bancos universales y comerciales en todo el mundo. Dichas actividades obstaculizan el grado de inclusión del sistema financiero y disminuyen la confianza del público. La investigación tiene como objetivo demostrar la necesidad de prestar más atención a la gestión de riesgos para los bancos. En este estudio, el tema principal fue examinar cómo las actividades de gestión de riesgos en los bancos comerciales iraquíes ayudan a impulsar el rendimiento de estos bancos. El estudio reveló que la variable clave para evaluar el desempeño de los bancos comerciales es la gestión de riesgos. El estudio indicó además que, cuando las contrapartes no cumplen con sus compromisos, la gestión de riesgos impacta sustancialmente el desempeño financiero de los bancos comerciales

1- Introduction

Due to the continuous change in commodity prices, foreign exchange swings, interest rates, and capital flows, the global financial market has undergone enormous instability over the past several decades. In many developed countries, all these have had a significant role in supporting investments and external deficits. (KOSMAS, 2013) stated that the financial crisis we experience these days is due to primarily weak risk management strategies which, in some instances, involve high house loans, risky lending, and an enormous credit concentration. Moreover, financial institutions face a range of threats such as risks of interest-rate, risks of currency exchange, risks related to politics, market risk, liquidity risk, operational risk, and credit risk. There is a risk of losing consumers' earnings, more than 85 percent of deposits are very vulnerable, the structure of banking deposits itself is also related (Aldayel, 2018) .

Deposits at the risk of depositors are liabilities(Akkizidis and Khandelwal, 2008) (Al-tamimi and Al-mazrooei, 2007) . highlight the strong importance of good risk management as it offers greater profits to investors. showed a continued paucity of risk management, poor portfolio management and inattention to changes to the external and internal situation which could lead to a reduced number of clients, and thus reduced deposits as the main reason why severe banking challenges remain directly associated to lack of application. Unsuccessful risk management, according to (Kao et al., 2017) , will contribute to the bank failure or eventually the break-up of the banking system as a whole. In addition, (Darryll Hendricks, John Kambhu, 2006) argued that a misconception of risk assessment and risk management evaluation results in an inconsistent equilibrium of managed threats and expense. As well as the current technological advancement, banks often look at multiple threats, such as liquidity risks, the danger of the economy, interest risks and risk of foreign currency exchange.

Iraqi banks are still experiencing many problems and difficulties in applying the terms of both the First and Second International Basel Agreements and also the Third Basel Agreement. These challenges are as follows: (i) the failure to estimate the amount of capital needed for risk-taking based on the amount of the real capital, (ii) the lack of a trustworthy robust, credible database; (iv) the inability to keep pace with changes in the world banking industry, (iv) weak implementation of risk management (v) Incompetence to report risk and accounting policies to assess the bank's profits and losses and inability to expose the bank's plan of dealing with risks; and (vi) Complete Iraqi Banks ' low assets and capital relative to international banks (Rahat Javaid, 2014) .

Iraq struggles to fight an economic history of fighting, terrorism and a variety of other problems. Considering that Iraq is only vulnerable to open-market activities, financial institutions are now exposed and likely to be vulnerable to many threats. As the position of a facilitator that functions among many variables, risk management strategies must therefore be successfully implemented. For example, the banking operations which are subjected to risks have to be identified, the risks evaluated and all these risks controlled to reduced. Consequently, risk management activities are one of the banks ' key regulation frameworks to guarantee compliance with the standards of ISO 31000 put forth by the Central Bank of Iraq.

There are several issues in the Iraqi economy. An important economic challenge is the Iraqi economy's downturn in the past fifteen years, as due to the underperformance of the manufacturing sector (World Economic Forum, 2010) (Partnerships, Zhang and Soomro, 2015) and the Baghdad Stock Exchange (2014-2015) have seen it as well. However, the US intervention in the Gulf Region (Rahat Javaid, 2014) , including the first Gulf War and the occupation of Iraqi in 2003 and the preceding eight-years of war between Iran and Iraq, have seriously impacted negatively on both of the public and the private sectors. These financial institutions have been exposed to air bombing, robberies, sabotage, economic blockade and the like for over a decade. This model uses the bank's particular variables as a controlling one, which illustrates the association between financial performance and risk management. Depending on the findings, the present study presents several recommendations for regulating the banking sector, especially universal banks in Iraq.

2- Risk Management in Iraqi Financial Sector

The banking sector is essential for economic development and growth in any nation as a major source of funding for most firms (Mahmood, S., Qadeer, F. & Ahmad, 2015) Banks, whether state-owned or private, have begun to update risk management and control systems in about all regions of the globe. Various regulations are utilized to eliminate bank risks, such as risk evade, risk mitigation, transfer of risks, risk toleration and elimination (Doherty, 2001).The implementation of risk management is not modern. Such old methods require a new method and framework. Modern risk management for governments who hold a forward-looking position in the loss assessment will include individual, commercial and industrial businesses through an orchestrated structured risk management strategy. Risk management may lead to economic development by reducing property risks.

If local trade and industry companies are able to permit this to happen, (Izdihar, 2007) states that the risk management process will only be an essential part of management in developing countries. Although Iraqi private banks have taken various steps to assess risk, in particular, credit risk, through the usage of certain instruments, experience is needed for efficient utilization of these resources. Throughout addition to identifying threats and mitigating risks, all aspects of banks ‘ hazards need to be taken into account. Thus, a solid understanding of the performance of the Iraqi banking sector is highly important.

3- Financial Performance

The business dictionary shows that financial performance requires monetary measurement of the results of a company's policies and procedures. The effects of the investment return, asset gain and value-added represent the Company's performance. As referred to in Turyahebya (2013), Stoner (2003) describes financial accomplishment as the capacity for effective, productive service, sustainability, development and reaction to environmental incentives and risks. Solvency measures demonstrate the ability of a company to pay back all its debt through selling its assets. It also tells about the capacity of an organization to survive after a major financial collapse. The financial performance is an aggregate indicator of how well a bank earns profits from its investments (Toutou and Xiaodong, 2011) . This also demonstrates over a period of time the total financial stability of a financial institution and can also compare different institutions in the banking industry. The financial performance of the bank will usually be regarded as consistent and profitable. Their stability applies to their risk factors and their benefit is the financial return.

Financial performance is the capacity of the institution to generate new resources from daily processes over the duration of a given period. This performance is measured by net income and cash from such processes. For their potential operating practices, the financial performance of commercial banks is extremely important. Profitability prior to going into debt and liquidity assessment is the first thing you comprehened about financial performance. It is obvious from the argument above that banks are not doing so well because they do not control their risks management. The inadequacy of transparency and documentation of all risk management activities compromises the risk management process, which in effect reduces the ability for risk management strategies. (Mahmoud, 2014) , states that the inability of the Iraqi banks to monitor risks or to enforce ISO 31000 standards led to weak performance and results.

4- Relationship between Risk Management Practices and Financial Performance

The theoretical link between good risk risk management management practices and better banking efficiency is focused on the empirical association between risk management and financial performance of banks (Miller, 1992) . It is not enough to recognize or keep a record of past performance measures. Risk management and measurement of performance should be brought together to enable companies to control their risk profile and to define their strategic vision.

(ALAM&MASUKUJJAMAN,2011) analyzed further the risk management procedure for Bangladesh commercial banks. For that reason, they gathered the actual data of bank managers chosen by means of questionnaires, along with the use of descriptive statistical methods of data analysis. Their analysis found that all risk management practices relating to credit risk, market risks and operational risks were being implemented by selected Bangladeshi banks.

(Fayman, 2011) , conducted a study in which he analyzed the influence of the prepaid risk on commercial banks ' performance in the United States. The assumption is that an interpretation of how different risks influence bank performance can increase financial institutions ' performance and stronger calculate the risk of banks in relation to customers-approved loans. The findings suggest that the added prepaid risk variable to regression models can typically enhance the capability to understand bank performance measurements. This study confirms that the effect of the prepayment risk on different components of bank performance is not measured in previous research.

(Amelino-camelia et al., 2011) stated in their research that the income capacity would probably be lowered and might also lead to failure when the banks are mismanaged and risks are ignored. When banks lend, threats should be expected to occur by the doubtful debtor or by the bank's financial system. With the banks operating in a competitive atmosphere, external and internal influences could contribute to risks. Risk management typically involves recognizing and evaluating risk, reducing and managing danger, assessing risk and financing through debiting or transferring general or individual reserves.

In their study, (Khalid and Amjad, 2012) , reported that banks are exposed to different risks since the principal goal of bank management is to maximize the profits of owners. Banks ought to be able to control the threats until they emerge to achieve this goal. Strategies in risk management help to avoid capital depletion. (Asemeit, 2014) aimed at defining the impact of risk management activities on the financial performance of Kenyan Banks, the information given by top management operating personnel allows banks to focus on the threats they intent to reduce. Data were obtained by submitting questionnaires, with the response of 44 Kenyan banks. By utilizing SPSS software and its regression analyzes method, the respondents' rsponses were analyzed. The application of risk management strategies appeared to have a strong impact on their financial performance. The risk analysis has been the most critical impact variable on financial performance accompanied by risk mitigation, application of the risk management system, tracking and evaluation. This research has shown that risk management activities are in a positive relationship with banks ' financial performance in Kenya. In addition to its risk management activities, it was recommended that financial institutions in Kenya follow a multidimensional strategy to risk management.

(Afande, 2014) intended to examine current credit risks management methods by commercial banks in Kenya by (i) investigating how far commercial banks employ credit risk management practices and methods while confronting various kinds of risks: (ii) evaluating the efficacy of credit risk management techniques by commercial banks; (iii) investigating the inner performance of bank lending by commercial banks in Kenya The data were obtained using a questionnaire. The researcher presented the data utilizing frequency tables, maps and bar graphs to follow a descriptive research design. The findings of his analysis stress the correlations between strong relations and credit risk management's achievements and banks ' internal operations. Commercial banks in Kenya have been found not to follow covenants, credit rationing, securitization of loans, and lending activity. They utilize credit risk management techniques. Commercial banks in Kenya have verified their successful credit risk management systems (CRM). Successful CRM implies a sound credit issuing process involving the development of an acceptable CR environment; ensuring an adequate credit management system that includes the tracking process and proper credit risk regulation. A study by (Dragos, 2012) supports the above observations.

An examination of the management system utilized in Russian banking has been carried out by (Aliv, 2015) The study aimed at identifying patterns in commercial banks ' growth, which culminated in the banks ' risk exposure. The study focused on a qualitative assessment of the banking industry in the Russian Federation through the analysis of patterns in commercial banks ' performance. His study has shown that monitoring has enabled banks to predict the most important trends leading to a decrease in doubtful and bad loans and major bank asset credit risk. The study found that commercial banks will assess financial risk management outcomes as fast and efficiently in order to keep banks viable in current circumstances. They will take precautions to ensure continuity, efficiency and consistency, and to respond to negatory adjustments.

The research focus studied by (Matis, 2015) consists of different tracking and reducing risk management policies and procedures that closely reflect the risk incident category, the limitations and the structured financial performance measurement. It focuses on the impact of corporate culture on performance management and on banking risks management. The analysis included a quantitative method of analysis, the descriptive method, and the illustrating approaches. Finally, it reinforces the requirement for an appropriate and reliable system to define, track, assess and control danger incidents. A comparative study examining the banking system's risk management and its effect on their performance was carried out (Zahid Ali Channar1, Abbasi2 and Maheshwari3, 2015). The aim of the research was to assess the application of risk management in traditional and Islamic banks and to examine the correlation between risk management and bank performance. Primary data were obtained from a closed-ended survey for this research and evaluated via an independent sample T-Test and correlation. Stratified and random approaches for the collection of data have been used. The necessary sample size was 65, with 20 of middle-stage management, 20 of the lower management stage and 25 clients for Islamic banks and traditional banking institutions. The results have shown that traditional banks were more productive than Islamic banks in credit risk management. The results further highlight the positive correlation between credit risk control and financial performance in traditional banks.

5- Theoretical Framework

(uma sekaran, 2004) was cited that "A theoretical framework is the conceptualization of the nature of the relationships between various factors (variable) that are defined as essential to the issues, of how many hypotheses or principles make sense." A theoretical framework is a great idea for this research so that the correlation between risk management strategies and financial performance could be experimentally examined. This research explores the effect on the financial performance of risk management technique. No research has addressed a comprehensive collection of risk management practices and financial performance through risk management research has been performed in the past. Figure (1) illustrates the framework used in this study.

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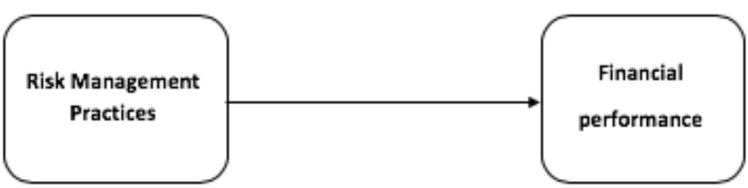

Figure 1: Research model

6- Conclusions

The research shows that risk management has a positive effect on profitability against the argument that the examined literature has a negative effect. The results are therefore not in line with the many empirical studies suggesting that bank performance has a positive correlation with credit risk, asymmetry of knowledge contributes to more NPLs that affect the competitiveness of universal banks adversely. The findings of the study have showed that bank risk management has a significant positive influence on universal banks ‘ profitability in Iraq.

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