بسم الله الرحمن الرحيم

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شبكة المعلومات الجامعية
التوثيق الإلكتروني والميكروفيلم

شبكة المعلومات الجامعية

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جامعة عين شمس

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The Effect of Credit Risk on the Banks' Performance in Egypt

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Thesis Submitted in a Partial Fulfillment of the Requirements for the Degree of MSc in Business Administration

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Dedication

All the gratitude and thanks to those who stood by my side during my learning path and trusted me. If it were not for God and my mother (may her soul rest in peace) and her prayers to me, I would not have stood before you here discussing my research which I dedicate it to my mother who stayed up nights and spent her life to see me on this stage as I know that she is now proud of seeing me fulfilling her dream. I also want to thank my brother (Ahmed) and my father for giving me the energy to continue my journey, and I'm not going to forget the most precious person who stood beside me, as he gave me a lot of his time and patience to be by my side in every step, from choosing the topic to presenting it.

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Abstract

Banks today are the largest financial institutions around the world, with branches and subsidiaries throughout everyone's life. However, commercial banks are facing risks when they are *operating*. Credit risk is one of the most significant risks that banks face, considering that granting credit is one of the main sources of income in commercial banks. Therefore, the management of the risk related to that credit affects the performance of the banks. The aim of the research is to provide stakeholders withaccurate information regarding the credit risk management of commercial banks with its impact on banks' performance.

The main purpose of the research is to investigate if there is a relationship between credit risk management and banks' performance in Egypt. We also aim to *investigate* if the relationship is stable or fluctuating. In the research model, Capital Adequacy, Asset Quality, Earnings (ROE) and (ROA), Liquidity and Sensitivity are defined as measurements of performance while Loan Loss Reserves / Impaired Loans, Impaired Loans / Total Equity, Unreserved Impaired Loans / Total Equity, Net impairment charges / net interest income are defined as measurements of credit risk management. The research collects data from 15 commercial banks in Egypt from 2011 to 2018 and formulates six hypothesis which are related to the research question. A series of statistical tests are performed in order to test if the relationship exists. Other statistical tests are performed to investigate if the relationship is stable or not.

The findings reveal that there is no significant effect of credit risk management on the Liquidity and Sensitivity, while there is a significant effect of the credit risk management on the Capital Adequacy, Asset Quality and Earnings (ROE & ROA).

Keywords: Credit risk management, performance, commercial banks, Capital Adequacy, Asset Quality, Earnings (ROE & ROA), Liquidity, Sensitivity, Loan Loss Reserves / Impaired Loans, Impaired Loans / Total Equity, Unreserved Impaired Loans / Total Equity, Net impairment charges / net interest income.

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Chapter One

Research Framework

1.1 Introduction

The financial system's health is critical in the country (Das & Ghosh, 2007), as its failure will stymie the country's economic growth. Financial performance is measured by net income and funds from operations and is based on a company's ability to produce new resources from day-to-day operations over a given period of time. Traditional financial performance measures and market-based financial performance measures are two types of financial performance measures (Aktan & Bulut, 2008). When the financial and banking crises became global in the 1980s and 1990s, new risk management banking strategies arose. To be able to handle the various kinds of risk, it is necessary to first describe them. The risks that are most relevant to banks are as follows: Credit risk, Interest rate risk, Liquidity risk, Market risk, Foreign exchange risk and Solvency risk.

Credit risk is the danger of loss due to a debtor's non-payment of a loan or other line of credit (either the principal or interest or both) (Appa, 1996), while risk management is the human activity that incorporates risk identification, risk evaluation, designing strategies to handle it, and mitigating risk using managerial resources (Campbell, 2007). The probability of a borrower defaulting by failing to repay principal and interest on time is known as the default rate. A bank is a commercial or government-owned financial institution that offers financial services such as issuing money in multiple forms, accepting deposits, lending money, processing transactions, and generating credit (Campbell, 2007). Banks place a high value on credit risk management because it is an integral part of the lending process. It maximizes the bank's risk-adjusted rate of return by sustaining credit risk exposure in order to protect the bank from credit risk's negative effects. The bank is spending a significant amount of money on credit risk management modeling.

The case in point is the Basel II accord. There is need to investigate whether this investment in credit risk management is viable to the banks. This study therefore seeks to investigate the effect of credit risk management on the banks' financial performance in Egypt.

1.2 Research problem

Any banking institution's goal is to function profitably in order to preserve stability while both increasing and expanding. Lending is the lifeblood of commercial banking for the majority of citizens. Most banks' most valuable asset is loans, which produce the majority of operating profits and subject the bank to the most harm. The banking sector in Egypt has faced a variety of problems, including non-performing loans and interest rate volatility, among others, both of which have posed a danger to bank stability. Credit Risk Management is essential to bank management, according to Bessis (2005), because banks are "risk machines that take risks, turn them, and integrate them in banking products and services. Risk is a collection of unknowns that can result in either negative fluctuation in profitability, which shows the bank's financial performance, or losses, which shows the bank's failure.