Risk Management in Nigerian Banks

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Abstract: Effective and efficient risk management framework is a potent tool for the management of the banks and to reposition the banks profitably, as it makes them to be proactive and timely in mitigation of risks in accordance to their risk appetite. Therefore, banks should adopt the risk management framework as an integral part of organizational culture because of its obvious advantages. It is also observed that any bank that wants to operate profitably must embrace risks by understanding the types of risks facing it and the different strategies to adopt to mitigate the risks effectively.

1.1) INTRODUCTION

Risk is attached to all human activities whether they are undertaken purely for leisure or for profit. We are more concern here with profitable activities as undertaken by banking industry. One of the major functions of banks is financial intermediations, transferring funds from the surplus sector to the deficit sector which involves lending depositors’ funds to the real sector of the economy. Intermediation ensures efficient allocation of resources, and encourages capital accumulation thereby leads to growth and development. In performing this crucial function the banks encounter many risks inherent in it. David Murphy (2008) sees risk as the danger of loss. The net result of risk is the possibility of losing fund or not achieving the targeted objectives.

Joel Bassis (2010) defines risk as uncertainties potentially resulting in adverse variation of profitable or losses. He further noted that risk is not identical to uncertainty which refers to randomness of outcome while risk refers to the diverse effect on wealth that such outcome have. Risk therefore can be considered as a negative impact on the bank that can divert the bank’s management decision from achieving its stated objectives.

It must be noted that any policy decision taken by the management of the bank must have some element of risk attached to it. Therefore, for the bank to achieve its objectives it must factor in risk elements in its major decisions. Hence, risk is an unexpected event which can occur both in the short run and in the long run, banks must also adopt strategic risk framework to deal with the long term unexpected events. Strategic Risk is seen as those risks arising from long term wrong decisions or inadequate decisions by the bank.

Risk management involves the process of identification, planning, assessment and measurement. However, (Wikipedia Nov.2014) defined in ISO 3100 as the effects of uncertainty on object followed by coordinated and application of resources to minimize, monitor and control the probability. The objective of risk management is not only identification of various risk exposures but to measure, control and mitigate the risk and assigned resources on the different level of risks involved. Josison (2001) defined risk management as the process by which various risk exposures are identified, measured, and controlled, our understanding of the risk has improved by the development of derivatives market. In the final analysis, from the various definitions of the risk management, one can infer that risk management involves; identifications, measurement, and controlling of risk and through the process, the bank understands the type of risk, its impacts and formulate strategic policies to mitigate the risks in accordance to its risk appetite. The aim of risk management is therefore to prevent negative events that may trigger loss of funds in the bank.

1.2) Risk Management Process:

The risk management process involves defining, identifying quantifying and monitoring of risks and also making necessary provisions for the losses incurred through the risk. In the risk management process, the first task of the management is to identify the potential area of risk exposures. The potential risks could be internal or external. The external risk may originate by the government policy, for instance, the constant changes of government policies may affect the banks very negatively as the bank cannot plan strategically by taken future definite decisions. David Murphy (2008) sees Risk Management as a process to ensure the undesirable events do not occur. He went further to enunciate what good risk management requires:

- “A comprehensive definitions of the firms risk appetite.
In Nigeria, it is observed that the Regulatory Authorities such as Central Bank of Nigeria always coming up with many uncoordinated banking policies more especially if there a change of Central Bank Governor, each Governor comes up with different policies quite different from his predecessors which results in ensuing conflicting guidelines; thereby creating confusion in the banking industry. The banks should anticipate that, as a potential risk and take necessary steps to mitigate them for their long term survival.

Another important step for the bank to take after identification of the potential risk, is the analysis of the risks “Once risks have been identified they must then be assessed as to their severity of the impact (generally a negative impact, such as damage or loss) and to the probably of occurrence.” Therefore, in the assessment process it is critical to make the best educated decisions in order to properly prioritize the implementation of risk management” (Wikipedia 2014) This involved the bank to quantify the various risks to enable them know the risk to undertake in terms of cost. However, some high risk investment may even require fewer projects to execute. A bank that invested in bonds will anticipate less return as is a well secured investment than investing in oil and gas which is less secured but will yield more returns. Many of the banks that lent to oil and gas industry in Nigeria accumulated a lot of unserviceable loans because of the inability of the borrowers to liquidate the loans. This seriously affected the liquidity and capital adequacy of the banks. The large volume of None-Performing – Loans has prompted Central Bank to issue a circular to the banks to eliminate such loans to acceptable limit or face sanctions. It is noted that the volume of None-Performing-Loans (NPL) in Nigeria Banking Industry stood at 362.20 billion naira in 2013 as against 286.09 naira in 2012. (Central Bank of Nigeria, Annual Report (2014)

Therefore, the most important task of the risk management is to ensure realization of predictable results by reducing the divergence between what is expected and the outcome of the events. And that could only be achieved through a robust framework and a clearly defined transparent processes for identification of all factors that may lead to the said divergence (of risk identification) estimation of the likely hood of their occurrence and extent or severity of the impact in the event of occurrence (Risk Assessment /measurement) design of effective controls to minimize both the likelihood and the impact of the risk event (Risk Reporting); and the provision of sufficient capital to absorb the adverse impact of the event.

Therefore, when the major source of the risk has been identified, it can be investigated, and assessed, proactive measures should then be taken to deal with it. The bank should be encouraged to have an inbuilt system for the management processes for identification, analyzing, quantifying and then controlling risk because of the obvious advantage of the processes. Such a bank will have competitive advantage over others; the model leads to increase in its solvency and the capital adequacy of the bank. It will also be a tool for the management to take sound decisions in the management of portfolio transactions and its implementation strategy. We shall now examine in details different types of risks strategies:

**Risk Identification** Identifications involved getting the source of the problem. It is assumed that once a source of a problem is located it can easily be treated. The source could be internal or external. The external sources could be those risks outside the control of the bank such as government policy, Central Bank directives and natural disaster, even terrorism such as (boko haram) insurgents’ activities can impact negatively on the bank. Recently many banks have been destroyed or looted by the Boko haram insurgents – a terrorism organization in Nigeria and the activities of Boko Haram organization therefore potentate great dangers to the banks. The risk can be internal such as internal fraud, security challenges, none observation of corporate governance and lack of effective internal control. The bank must identify such risks and take positive steps to mitigate them. Banks should however be more concerned with the risk that involves much loss of funds.

In financial system the identification of the source of the problem will be easy if the relevant chain of command is determined, ensuring that each level in the chain understands the risk management philosophy and subscribed to it. In order words, the bank must make sure that every staff understands risk management framework and the need for each of them to be risk champion. The management should ensure an open communication if the above task is to be achieved.

**Risk assessment:** The main reason for the risk assessment is to determine the possibility of the occurrence of the risk and level of the loss encountered. Therefore, “in the assessment process it is critical to make the best educated decisions in order to properly prioritize the implementation of the risk management plan” (Wikipedia 2014). In
assessment of the risk the management must exercise caution and use that formula that will bring accurate results.

a) Although many formulae exist in assessment of risk, Wikipedia recommended Composite Risk Index. It is calculated thus;

Composite Risk Index = Impact of the event \times \text{Impact of occurrence}.

Suppose the impact of event = 5, and the impact of occurrence is 0.5, the then the composite risk index will be 5 \times 0.5 = 2.5.

The most important thing to note is that no matter which formula the management of the bank chooses to assess the risk, the formula should assess risks accurately to enable the Management take an informed decisions, because if the risks are not well assessed the bank will take wrong decisions based on such inaccurate assessment. It becomes necessary for the bank to use generally accepted financial concepts and risk measurement techniques to access the risk. In the assessment stage the bank should identify all risks associated with the bank’s assets. Liabilities, and even off balance sheet positions and then measure them accurately.

b) VALUE AT RISK (VAR) Another method of assessing risk is Value at risk (VAR) is referred to as expected maximum loss on portfolio with a given probability during a given period, while VAR parameters refers to a risk factor, probability, and time horizon. Geoffre Poitras (2003) observed that the introduction of VAR has resulted in a corresponding reduction in systematic risk in the financial sector. These obvious advantages of VAR have motivated many Nigerian banks to adopt the technique to protection their assets. The VAR methodology serve for defining of risk based capital or economic capital. Economic capital is the capital requirement to absorb potential unexpected losses at a present confidence level. The confidence level reflects the right appetite of the bank Joel Bassis (2010) pp123. David Murphy noted that Value at Risk is one of the methods of calculating market risk. He went further to say it assumes that portfolio respond liner to changes in each risk factor. However, he noted that the VAR concept is very important for three major reasons;

i) It provides a complete view of portfolio risk
ii) It measures economic capital
iii) It assigns tangible values to risk

It has its own limitations for example it simplifies the complexities of portfolio risk into positive in a relatively small number of risk and the assumption that the market risk is available for all risks. However, banks are encouraged to adopt any assessment method they deemed fit provided such method will be a key for the management to take positive decisions.

1.3 ENTERPRISE RISK MANAGEMENT

“In a financial Institutions Enterprise management is a combination of credit risk, interest rate risk, liquidity risk, market risk, and operational risk” (Wikipedia 2014) “Enterprise risk management is a process, effected by an entity’s board of directors, management personnel, applied in a strategy setting and across the enterprise, designed to identify potential events that may affect the entity, and manage the risk to be within risk appetite to provide a reasonable assurance regarding the achievement of the entity objects” Wikipedia (2014).

The bank must have a comprehensive risk framework that can easily identify the risks which will be communicated across the board. By identifying the type of risk confronting the bank, it becomes easier for the management of the Bank to deal with the situations adequately. It is a matter of fact that each identified risk will present different strategy of dealing with it.

Enterprise risk management process viewed risk as a whole because one type of risk could trigger series of risks in an organization. A massive fraud committed by the members of the staff is regarded as operational risk; it can also create a liquidity risk for the bank and even affects its total profit. Another example is where a bank accumulated a lot of non-serviceable loans, that is credit risk and may write it off after some years in accordance to their accounting system. This will impact negatively on the balance sheet of the bank by reducing the profits of the bank and may even erode its capital adequacy. It can also trigger a series of legal risk especially when the bank wants to realize the collaterals backing the loans. In Nigeria it is observed that many customers of the bank borrow funds from the bank without the intention of repaying the loans. The reason is that in many cases the borrower goes scout free because of inefficient justice system and court cases take many years to dispose. Many banks have even loss such cases in mere technical grounds. The constant court cases increase legal cost of the banks. It
means that banks must be diligent in administration of loan facilities to their customers.

In some cases, the accumulation of bad loans are even caused by the top management because of none observation of corporate governance by lending billions of naira to their family members or even friends without following the laid down procedure of lending by the banks. It needs not to be mentioned that such loans must turn to toxic assets in future. Alejo Jose G. Sison (2008) noted that such negative actions by the Management cause moral hazard to occur on the other hand when “agents shirk their tasks or not put forth their efforts”.

The bank should make Enterprise Risk Management as a culture which will be well integrated in the organization to enable the bank to have a more comprehensive approach to dealing with all types of risk. The management should therefore make all members of staff at all level to be conscious of the risks in the organization. Risks become integral part of the bank and decisions making process that is would be deep rooted in the bank from the top to the bottom. In other to encourage the staff to embraces the risk management process the bank must have a sound appraisal system that will reward the good and had working staff and sanctioned the bad ones.

The obvious advantage of this process is seen on how the Management of banks are deeply involved in this process as it enables them to identify risk at the early stage and take quick steps to mitigate the risks. Some of the risks mentioned earlier that lead to great loss should not have occurred, if the bank concerned observed enterprise risk management principles as those risk associated with internal lapses would have been discovered. The model would have provided earlier warning signal of such negative impacts, hence a quick intervention for mitigation of the risks would have been taken. In the final analysis, the process will increase the productivity of staff, which will also be translated into increase in the profit of the bank.

1.3 DIFFERENT TYPES OF RISK

Enterprise risk management is the process of identification of the sources of risk and breaking them down into operational risk, credit market, market risk and also calculating the fund apportion to each risk factor. Central Bank of Nigeria, had in circular dated September 10, 2013 to the banks, and discount houses directed that all banks were expected to adopt basic approaches for the computation of capital requirement, credit risk, market risk, and operational risk. This is to encourage the banks to have a common strategy in assessments and calculation of such risks.

a. Market risk: Market risk is defined in Basel II “as the risk of adverse market value of the trading portfolio due to market movements, during the period required to liquidate the transaction” Market risk is therefore the risk that will cause financial loss as a result of changes in the price of equity such as federal government stock, equities, exchange rate changes. However, the period of liquidation is critical to assess such adverse deviations. The liquidation period is determined by the type of the financial instrument. Some of these financial instruments may take only one day to liquidate while others take more than 30 days. In effort to get accurate measurement some banks in Nigeria are using “Sensitivity Analysis” to measure market risks which is defined as “the total profit and loss a firm made by a movement in a risk factor. It also captures the change in the price of bonds by a small change in interest rate “David Murphy (2008). The most important thing is that banks should use measurement process which is capable of identifying market risk factors that affect the value of portfolios, income streams, and other business actions. In order words, the bank should use acceptable techniques to measure their marketing risks that will enable the Management to be able to quantitatively measure risk and allocate the necessary capital and liquidity requirement to the risks that face the bank.

Because of fluctuations in the exchange rate market, many banks customers even the banks normal hedge their exchange rate transactions against depreciation of Naira. Recently CBN introduced flexible Exchange Rate Management which devalues the currency to about 350 naira to a dollar. Those who hedge their currency will be at advantage than those who did not. This is a market risk on the part the banking industry as the liquidity position of the bank will be greatly affected and with a multiple negative effects in the economy.

Banks also faces market risk if they hold some financial instruments in their books and there is a sudden fall in the prices such assets which will make the bank to realize less fund from the instruments. The scenario was clearly illustrated between 2006 and 2008 when there was a boom in the capital market, the value of equities were rising on daily basis and many investors were attracted to buy shares of many blue chip companies in the capital market. The situation made some investors to even sell their houses and invested the proceeds in the capital market. Banks attracted their customers with soft loans to purchase their shares or other equities from the capital market. The
The mad rush continued until the bubble boosted the price of equities nearly drop to zero and some companies’ shares became worthless papers. In the light of the sudden crash, banks started to realize their loans and many of the loans had gone bad, as some of the shares became worthless, that affected not only the liquidity profile and also the capital adequacy of those banks. This scenario demonstrated that banks are not insulated from marked risk.

b. Operational Risks: Basel 11 made adequate provisions for operational risks which laid much emphasize in people, system and internal processes. It encourages increased attention to operational risk and risk management practiced in financial institutions and as well as improved disclosure and market discipline. Basel 11 encourages the bank to adopt the best management practice in dealing with operational risk and capital adequacy of the bank to avoid systematic distress. Banks should put in place an appropriate set of system and procedure for identifying, measuring, monitoring, controlling its operational risks.

Operation risk permeates all operations of the banking system which may take the form of system failure, obsolete information technology, inadequate tools or equipment. Bamidele. A.(2006) noted that” the application of the ICT in Nigeria banking industry has resulted in improved business performance with positive impact on the domestic economy, it has a lot of challenges such as inclusive regulatory, surveillance, system integrity and legal risk.” However reliance of ICT to provide services could be problematic if systems are neither reliable nor available on daily basis. The constant breakdown of banking ICT in service delivery could erode public confidence in the banking system where time is critical in transactions. A typical example is the application of ICT in the provision of internet banking services. The internet services have been most unreliable in almost all the banks; this has led to waist of valuable time not only that of the employees of the banks but that of customers who always being frustrated.

Joel Besses (2008) observed that operational risks resulted from fluctuations of information system, reporting system, interest rate and the risk monitoring rules, and internal procedures designed to take timely corrective actions, or the compliance with internal risk policy. He further posited that operational risk appears in different levels: human error, processes, technical and information technology.

Operational risk is seen as the residual of all risk inherent in the banking system. The bank can never meet its profit level if the employees are inefficient and lacks basic knowledge of banking. In this era of massive unemployment in Nigeria, we discovered that employment in some banks is not done on merit but ‘whom you know’. The banks has thrown strict processes of employing staff to the winds, that notwithstanding some banks prefer employing graduates of other fields without the basic knowledge of banking. Those graduates who specialized in banking could not gain employment in banking industry because they do not have ‘God fathers ‘ or ‘connections’ and such action breads inefficiency and systematic risk in the banking industry and intensifies the operational risk as well.

Banks must take measures to train their staff both in internal and external courses so that their staff will be much equipped with modern banking skills and knowledge. They should undergo on the job training as well as organized courses. Banks that want to achieve their goals and objectives must invest huge sum of money in human capital. They should encourage their staff to take up professional courses such as being a member of Nigerian Chartered Institute of Banking; banks should make it compulsory for all employees to register as student members and encouraged them to be professional bankers in future. This can be done by the banks undertake to pay both the examination and membership fess of the staff that registered and give them time to attend lectures. It is noted that such investment in the training of the staff will be translated into increase in productivity and profitability of the banks.

The operational risk can also trigger other risks which may constitute systematic danger to the progress of the bank. The use of Information Communication Technology has brought a lot of advantages to the banking industry in their services delivery to the customers such as automatic teller machines in making payments, settling of utility bills and money transfers, the use of POS in settling bills and making purchases. To the banks it has increased their revenue base and enhances their profits and such banks have competitive advantages over others. Such advantages cannot be achieved if banks deploy outdated Information Communication Technology (ICT), it will be faced with constant breakdown of the system, delay in operations, inaccurate data generations and etc. This will result to delay in rendering banking services to the customers and the frustration on the part of employees. It may prompt the customers to
move their accounts to other banks with better services. Therefore, constant system failure accompanied by inability of the staff to understand the application of the ICT has resulted to series of inefficiency and low level productivity on the part of the staff. In some instances, customers account are wrongly debited or credited without authorization and on enquiry they will simple told the customer that is ‘a system error’ and the customer would wait for months before such debits are reversed. Banking is based on confidentiality and when the reputation of the bank is put at risk it will make many customers to lose confidence in the bank and may trigger legal risk.

In view of such of frequent cases, Central Bank of Nigeria established a Department known as Consumers Financial Department. The main function of the Department is to intervene in such cases and carefully examine them and advice the contending parties accordingly and “to further engender public confidence in the banking system and enhance customer protection” Anyanwu C, M. (2010) The CBN has resolved many of such cases between the bank and the customers. It is noted that “in the first months of its operations about 600 consumer complaints were received by the Department which was a manifestation of the absence of effective consumer complaints resolution mechanism in banks.” Anyanwu, C.M (2010) in the same vein, the Governor has issued a circular directing all the banks to establish a ‘self help desk’ to resolve customers conflicts.

Despite the above, external factors can constitute operational risk in the banks for example the constant changes of the Central Bank of Nigeria policies. It must be mentioned that some of the policies may benefit the banks while some may impact negatively on them.

A typical example is the outcome of Monetary Policy Committee (MPC) held on November 26, 2014, some sweeping policy changes were made in the banking industry and the economy as a whole to address the economy and protect the naira because of the global falling of crude oil prices. The Nigeria economy continues to be affected by external shocks due to the fact that about 90% of their external revenue is derived from oil receipts. The Central Bank of Nigeria has to step in to address the situation by taking under mentioned actions:

I) The mid-point exchange rate was moved from N155 to N168 to dollar thereby deprecating the naira against the dollar. The band of exchange rate was now widens around mid-point from +/-3% to +/-5%.

II) The Cash Reserve Ratio (CRR) for private sector fund was raised from 15% to20%

III) And the Monetary Policy interest rate was raised from 12% to 13%, this will surely increase interbank rate.

It is anticipated that the devaluing of the currency will affect those banks that borrowed in the international market, as the loans to the banks were dollar dominated and such fund were lent to their customer in Nigerian currency; now the currency is devalued it means that banks will source for more funds to service such loans. In the short run, it will seriously affect the profitability of the banks as the cost of bowing have increased but in the long run, the banks will factor in such additional costs when lending to their customers. Also it will put many banks at the risk of capital erosion and accumulation of huge toxic assets.

Again by Central Bank of Nigeria raising monetary policy interest rate in the interbank will increase cost of borrowing by the banks, and the banks will now increase the interest rates and thereby discouraging customers from borrowing. This will surely affect the real sector. As noted by Nigeria Punch December 09, 2014 “The Central Bank of Nigeria’s Monetary Policy Committee raised Cash Reserve Ratio on private Sector deposits from 15per cent to 20 per cent Deposit Money Banks are experiencing difficulties in raising adequate cash to meet daily operations and obligations” The development had made the overnight lending rate to rise from 33 per cent to 36 per cent.

In view of the above, the banks are encouraged to put in place strategic risk management framework to mitigate such operational risk, as effective risk management framework provides early warning signals of potential problems, hence, opportunity for timely mitigation. The Board of the bank should anticipate such risk and allocate enough funds to mitigate the risks to ensure their long time survival.

2.2) Credit risk: One of the major services bank renders to their customers is giving loan facilities to them. In the course of performing such task the bank is confronted with many risks such as the risk of default by the customers, loan extension, and decrease in the value of borrowed money due to inflation. Such a risk the bank encounters by offering credit facilities to their customers is referred to as credit risk. The credit risk is therefore losses arising from exposure to none repayment of the loan or default on obligation of the borrower. The banks in order to mitigate such risk should develop a sound risk management framework that will cover credit administration from the originating of the loan to the repayment.
The management of the bank must ensure that appropriate plan and procedures for lending are efficient and the management as well as individual responsible to giving loans possess the necessary requisite skills and the knowledge for loan administration. This will surely reduce credit risk. Credit risk is one of the risks that lead to bank failures as it erodes the capital of the bank, although David Murphy (2008) observed that credit risk can also be mitigated by the use of various techniques such as collateral or the provision of guarantees by third party. If land is given as collateral, the bank must make sure of the perfection of the title deeds by conducting the necessary searches to ensure there are no encumbrances and registering the title deeds with the land Registrar to avoid unnecessary legal costs when the chips are down. In case of giving guarantees, the guarantor must be a man of substance and known to the bank for easy recovering of their money in case of default. Again bank’s management must ensure that overall credit risk exposure is maintained to a prudent level and consistent with available resources.

2.3) Liquidity Risk: The risk which arises when a bank cannot realize all cash timely and economical in order to meet its financial needs as they fall due. (Investor World .com) defines liquidity risk as that arises from the difficult of selling an asset. However some of the assets are highly liquid and have a low liquidity risk, a typical example is given as stock or bond while other assets are highly illiquid and have a higher risk attached to it. Banks should prefer to hold those assets that are highly liquid and easily reliable when it is facing liquidity problem as prices of the assets that could be realized in the long run are faced with market risk resulting from price fluctuations.

David Murphy (2008) is of the opinion that liquidity risk is the inability to meet expected and unexpected demands for cash. Liquidity risk should not be seen, that the bank is insolvent it only means that such a bank has more assets than cash. That is why in financial management, liquidity risk is seen as the risk that an asset cannot be traded quickly enough in the market to realize cash. The credit ratings of the bank will drastically fall if it facing cash trap as this may trigger unexpected cash outflow that will further compound its liquidity problem.

Liquidity risk is very critical in banking industry as experienced in 2008, following the global financial crises some banks were badly affected because they were in a grave condition and faced a serious liquidity problem. “Going to their significant exposure to the capital market in the form of margin trading loans which stood at about N900bn bullion as at December 2008, Banks total exposure to the oil industry stood at over N754 billion representing over 10% of the industry total and 27% of the shareholders fund” Anyanwu C.M.(2008). The serious liquidity problem was evident in banking industry 2008, which made the Central Bank of Nigeria to establish ‘Expanded Discount Window’ was closed and stress test conducted by a joint special examination by Central Bank of Nigeria (CBN) and Nigeria Deposit and Insurance Company (NDIC), it was revealed that 8 banks were in a grave liquidity problems and they were acquired by Central bank of Nigeria that bailed them out by injecting about N620BN as Tier 2 capital into banking system and that lead to the removal of the their Executive Directors as well.

Furthermore, because of the serious liquidity problems in the banking industry then, the Federal government on July 9, 2010 established Asset Management Corporation of Nigeria (AMACON) “It was anticipated then, that AMCON will help to stimulate the recovering of the financial system of Nigeria from recent crises by boosting the liquidity of the troubled banks through buying of none performing loans. The objective of the AMCON, to purchase bad debts from the troubled banks in place of collateral and to fill in the banks’ capital deficiencies and receive equity and or preferential shares in that banks that did not pass the Audit test” Omoh Gabriel, business Editor Finance January 24, 2011

The bank will return their equity-to-asset ratio’s back to 11%. It was noted that AMACON has approved purchases of none-performing loans totaling 2.5 trillion and it has actually purchased loans totaling 1.3 trillion from the banks and planned to another 2.0 trillion. The main aim of AMACON is to return confidence in the banking sector and to stimulate growth and development in the economy.

In view of the above, the banks should adopt liquidity risk management strategies that enable them to obtain funds easily from interbank and other markets, in case of any financial crises arising from government policies. Banks should be encouraged to have ‘a Contingent Funding Plan’ to enable them meet their liquidity needs under different stress scenarios.

3.0) Strategies of risks management: Once the management has identified and assessed the risks the next stage is to manage them. Therefore, the management adopts four strategies in the
management of risks namely: risk avoidance, risk retentions, risk reductions, and risk transfer.

a. Risk avoidance: The bank may decide to withdraw in all activities that may involve risks, which is practical impossible for any bank to undertake, unless the bank is not in business to make profit. More so, all the activities of the banks carry some elements of risk or the other, therefore, banks should embrace risks and plan and adopt strategies to mitigate them.

For instance, the bank will not stop lending because of risks of bad debits associated with it, nor the banks will refuse to accept deposits and make payments because of risk involved. Recently, many banks have lost huge sum of money through burglary, that made the Central bank of Nigeria issuing a circular directing all banks to move cash with bullion lories. In the final analysis, risk avoidance is not the best option for the banks to adopt.

b. Risk retentions: Another strategy open to the banks is risk retention. Any risk that cannot be avoided or transferred is automatically retained. The banks may decide to retain all the risks they cannot avoid, for instant, banks must retain the risks of internal frauds committed by their employees, in this situation the banks should try to mitigate the risk by putting strict internal control to track down any staff that will commit fraud. The Board must exist for policy making and therefore must also retain the risk of corporate governance mostly committed by the top management.

In all cases, the bank should assess the cost of retaining the risk and the cost of avoiding them and take the best option. But it may not be as simple as that because cost implication of risk may not be the only determinant of risk retentions. The long term financial implication must be put into focus before final decision is taken. Risk retention needs a carefully balancing between the short and the long run advantages.

c. Risk reductions: Risk reduction is a decision taken by the banks to minimize and greatly optimized the risks the bank decided to take, this may involve putting the necessary control to reduce the risk. In case of the employment of the members of staff in the bank, the bank normally undertakes background information of the employee before the employment is offered to them. Another precaution is the use of bullion lorry and armed police escort to move currency to avoid being attack by armed robbers. Additional precaution banks take to avoid loss of funds when moving fund is to select members of staff at random to convey the cash to its destinations without informing the staff beforehand. The main focus of the banks therefore is to reduce risks by employing various strategies that will mitigate the risks in accordance to their risk appetite.

d. Risk Transfer: Another option open to the banks to mitigate risk is risk transfer or risk sharing. Risk transfer involves paying another party to undertake the risk of the party that transfers the risk to third party such as insurance companies. It does not follow that transfer of risk will absolve all risk from the banks, as the main liability of the risk still lies with the bank.

The bank because of unexpected risk may decide to ensure its buildings, equipment, vehicles and even the cash in the Strong Room against any potential risk. We observed that despite the introduction of cash-less policy, cash transaction in Nigeria remains heavy, in view of the fact, banks may transfer currency movement to third parties as a risk mitigation strategy. In addition, for the bank to avoid loss of money as result of exchange rate fluctuations the bank may decide to hedge its foreign currency transaction as well.

4.0) RECOMMENDATIONS:

a. Profit making organization such as Deposit Money Bank must take risk management very seriously by establishing a risk management framework in the bank. The risk management framework will assist the bank management to identify, plan, monitor and mitigate the problems of risk in the organization. It means they should adopt a sound risk management processes as an integral part of the bank. It should have experience staff known as risk champions to propel the course of the risk management. The bank should put in place effective and appropriate infrastructure that can identify the risk for timely and proper mitigating actions.

b. The Management should adopt risk management as a culture in the bank. It means that the entire employee from top to bottom will be made to be conscious of the risks existing in the bank and subscribe to them by taken consistent proactive mitigation actions. Here communication is very necessary. The employees should be communicated the necessity of taking risks very seriously by quickly identifying them and necessitating actions to mitigate them. There should be very well defined policies and procedures which should be aligned to the overall business strategy and should support the continuous improvement of the risk management.
c. It is advisable for the management of the bank to assess the risks being taken both qualitatively and quantitatively not only to know the cost implication but the strategic implications as well before taken decisions. It means that bank should develop accurate risk measurement process to make risk assessment very effective.

d. It is also very important for the bank to adopt integrated and a comprehensive risk management framework to quickly identify and mitigate risks. Effective risk management framework provides early warning signals of potential problems, hence opportunity for timely mitigation actions to be taken. This will make the management of the bank to be very proactive in the handling of the risks situations. In order words the banks should consider establishing Key Risk Indicators (KRI) in order to make the process of monitoring operating risk very effective.

e. The corporate governance structure of the banks should be strengthened, for instance the lending limit and procedure for giving loans should be strictly followed to avoid unserviceable loans.

f. Management must go a step further to ensure that the interest of the bank is aligned with that of the individuals in the bank, that can be achieved by mutual trust and respect between different functions as performed by the Staff of the bank, by ensuring independence, competence and authority are maintained in all functions and that must be respected by all.

g. Banks should consider installing appropriate ‘fireworks’ that guarantee access only to authorized users to avoid the activities of hackers and crackers from defrauding the banks and the customers.

CONCLUSIONS:

The paper has shown the importance of establishing the risk management framework and the mechanism of identifying different types of risks such as market risk, operational risks, credit risks and liquidity risks and their implications on the operation of the banks. It went further to prove that accurate risk assessments and measurement process makes risk management effective as it will enable the management to take accurate decisions by apportioning funds more appropriately to different types of risks and to mitigate them effectively.

Again risk management process of identifying, assessing, planning, and monitoring risks will enable the bank to take proactive actions to quickly mitigate the risks accordingly to their risk appetite. This quick intervention on the part of management will prevent loss of funds in the bank.

In summary, banks should take risk management very seriously because it will help them to eliminate internal frauds considerable, respond to external risk quickly and these will surely lead to increase in profitability. The management of the banks must play central roles in defining the risk appetite of their banks and enthrone a culture of risk management in the banking industry.

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