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The role of credit risk control according to Basel II "An applied study on banks operating in Syria"

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***Abstract*:** *This paper aims to study the role are the oversight of the credit risk according to Basel II, the researcher used so the descriptive and analytical method, said measure oversight role using the questionnaire where they were taking a sample of 100 employees of banks in the Syrian Arab Republic.*

The research concluded that there is a significant relationship between the development of management systems credit risk under the new framework of capital adequacy in accordance with Basel II in banks, and operating in Syria, strategies and policies and procedures for credit risk management proper.

Whichdo the Council of money and credit and the instructions of the banking supervision, which reflects the probability of carrying the bank's credit risk, consider.

Moreover, there is a significant relationship between the developments of management systems credit risk under the new framework of capital adequacy in accordance with Basel II in banks operating in Syria and its orientation towards strengthening the discipline of market transparency and disclosure in the market, by providing information to market participants about the adequacy of capital.

Keywords: *Basel II, credit risk, Basel III*

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I. INTRODUCTION:

The experience of the banking sector in the Syrian Arab Republic considered small and primitive compared with neighboring countries, and the rapid development of this sector in recent years.

The urgent need to develop the oversight function of banks did not of great importance in the establish security and the protection of depositors, investors, borrowers and the banks themselves from the risks of this sector.(Abdul-Razzaq Al-Shahada,Muhammad Khaled, Makram al-Bayed,2011)

And access to the banking environment is suitable and safe and so by definition the basic principles of banking supervision effective prepared by the committee of Basel II Banking Supervision in cooperation with the supervisory authorities and the Council of money and credit.(Ihab Ghazi Zedan, 2011)

The purpose of which was to find guiding rules for assessing the robustness and performance of the regulatory system by shedding light on the implementation and implementation of these principles in the Syrian Arab Republic..(Aoukkbeh Al-Redda, Rim Ghannam, 2005).

This studyaims the development of methodology of credit risk management in banks operating in Syria according to the modern management of the risks the bank issued in accordance with the requirements of Basel II.

II. LITERATURE REVIEW AND HYPOTHESIS DEVELOPMENT

Basel II:

The Basel II agreement was initially published in June 2004 and was aimed at amending the international banking standards that were controlling the amount of capital banks required to keep them from the financial and operational risks faced by banks.

Basel II tried to achieve this by setting risk and capital management requirements to ensure that the bank has sufficient capital for the risks to which the bank is exposed through lending, investment and commercial activities. (Yetis,2008 ،Ahmet)

Uses the Basel II concept of "three pillars" - (1) minimum capital requirements (addressing risk), and (2) supervisory review and (3) market discipline.

The first pillar: minimum capital requirements

Where dealing with preservation of regulatory capital calculated for three major components of risks that the bank faces: credit risk, operational risk, and market risk. Other risks are not considered measurable at this stage.

1. Can account the element of credit risk in three different ways with varying degrees of complexity, namely standardized approach, Foundation IRB, and Advanced IRB. IRB stands for an "internal classification approach". (2019, JAMES CHEN)
2. For operational risks, there are three different approaches - basic indicator or BIA, standard or TSA, and internal measurement (advanced form is advanced measurement or AMA).
3. For market risk, the preferred approach is VaR (risk value), (Because of the recommendations of Basel II is introduced in stages by the banking industry, we will move from requirements to more precise requirements and have been developed for each risk category by each bank.

The upward trend of banks that are already developing their risk measurement systems is that they will be rewarded with lower risk capital requirements.

In the future, there will be closer links between the concepts of economic capital and regulatory. (Journal of the Federation of Arab Banks, 2004)

The second pillar: Oversight audit

This regulatory response of the first pillar, giving regulators "tools" better than those previously available do, it also provides a framework to deal with systemic risk.

The risk of the pension fund, risk concentration, and strategic risks, and reputation risk, liquidity risk and legal risks.

Which recollected by the convention under the title of residual risk. Banks can review their risk management system.

The process of assessing internal capital adequacy (ICAAP) is the result of Pillar 2 of Basel II. (Basel Committee, 2004)

The third pillar: market discipline

The aim of this pillar is to complement minimum capital requirements and the supervisory review,by requiring institutions to disclose details on the scope of application and exposure,risk and operations risk assessment and capital adequacy of the institution where it needs to be consistent with how the senior management including the board assess and manage enterprise risk. (Bruno Colmant et autres, 2005)

When market participants have sufficient understanding of the bank’s activities and the controls it has to manage its exposures from risks, they are better able to distinguish between banking institutions.

These disclosures must be disclosed at least twice a year, except for specific disclosures that provide a summary of the overall risk management objectives and policies that can Conducted annually.(Basel Committee, 2004)

Institutions are also required to establish a formal policy on what will be disclosed and their controls around it along with verifying and duplicating these disclosures.

In general,the disclosures under Pillar 3 apply to the higher unified level of the banking group to which Basel II applies. (Basel II International Converge, 2004)

As for Syria, with the aim of implementing control standards consistent with the Basel II agreement, Decision No. 253 of Risk Management and Banking Supervision was issued on 23/1/2007.

According to this decision, the banks operating in Syria must maintain a solvency ratio of not less than 8%. The solvency ratio means the ratio resulting from dividing the net private funds by total credit, market and operating risks.

The Central Bank of Syria announced after the approval of the Monetary and Credit Board that a plan and program for the transition to implement the Basel II criteria for capital adequacy and to obligate the banks operating in them, starting from 2011 at the latest, would be established.(, Dr. Linda Ismaiel , Ali Hatem,2012).

Credit risk:

The credit risk is still the primary source of the financial crises faced by banks at the global level, which belongs to low credit standards for borrowers, poor risk management portfolio, lack of sufficient attention to the variables of economic and other conditions that lead to deterioration of the credit parties dealing with the bank.(Basel Committee, 2006)

As for credit risk measurement methods, Basel 1 used a single standard for all banks without discrimination in the specific risk weights, replacing it with two capital measurement methodologies in Basel 2: standard classification, and internal measurement methodology. (BASEL II OVERVIEW, 2017)

Standard or Standard Approach: This method used to measure credit risk is considered one of the simplest ways to calculate capital requirements.

It is used by banks that perform uncomplicated activities and includes a more accurate classification of risks. It also includes expanding mortgages to cover credit risks, as part of new ways to reduce their risks and thus mitigate associated capital burdens. (Basel Committee revised framework, 2004)

The style classification procedure: calculate capital requirements in accordance with the methodology of the classification procedure over the mathematical equations provided by the Basel Committee through two methods: basic technique and style developed in the calculation of risk-credit (Basel Committee, 2004)

Basel III:

Basel III is a set of comprehensive reforms aimed at improving regulations, oversight, risk management of the banking sector at the level of the world, and improve his ability to stand in front of difficult economic conditions.. (, Dr. Linda Ismael, Ali Hatem, 2012).

Where he developed this new international standard on capital adequacy of banks will be by the Basel Committee in response to the gaps in financial legislation, and lessons learned released by the global crisis of (2007-2008).(Basel Committee, 2004)

Which resulted in tight liquidity and poor criteria for granting credit was affected by the accumulation of risk because of rising debt and weakening their capital in addition to the lack of appropriate incentives for liquidity (Liquidity Buffer). (Basel Committee, 2006)

Basel III: The main pillars of Basel Committee 03 are the following:

1. A new raise to the minimum reserve or initial capital ratio from 2 to 4.5 per cent, and another reserve margin consisting of ordinary shares of 2.5 per cent of assets and bank pledges to use it in the face of crises has been added, bringing the total to 7 per cent.•
2. Maintaining the overall capital threshold of 8% as before and adding a crisis Reserve would bring the minimum total required with this reserve to 10.5%. (Basel III summary, 2012)

Measure capital additional to meet these requirements, however, practice has proved that central banks in many of the Arab states managed to impose the capital adequacy ratio is high on the bank, but the states many of them make this limit of not less than 12% several years ago. (Basel Committee, 2011)

Could Basel III be applied to Syria?

The researcher recommends the necessity of a decision issued by the Monetary and Credit Council that obliges Syrian banks to work to implement the requirements of Basel III gradually and over a specific period consistent with the recommendations of the Basel Committee, which supports the continuity of Syrian banks

It increases the confidence of external banks in dealing with them, knowing that the current crisis and unfair sanctions on Syria have led to a delay in its implementation.

Hypothesis:

H1:Development of systems for credit risk management in accordance with the new framework of capital adequacy in accordance with Basel II in banks operating in Syria, strategies and policies adopted by the Council of money and credit and instructions of the banking supervision.

H2:Development of systems for credit risk management in accordance with the new framework of capital adequacy in accordance with Basel II in banks operating in Syria and its orientation towards strengthening the discipline of market transparency and disclosure in the market, by providing information to market participants about the adequacy of capital.

Search variables:

1- Dependent variable: Basel II capital adequacy framework for developing credit risk management systems in banks operating in Syria.

2- Independent variables: the existence of the possibility of applying the advanced approach to credit risk management in banks operating in Syria, namely:

a. Strategies, policies and practices for managing the risk of credit are appropriate management, measurement and control of credit.

b. Safe disclosure of information, about management strategies, the credit risk facing the bank. Sound and effective credit risk management strategies, policies and practices commensurate with the new Basel II guidelines.

III. RESEARCH METHODOLOGY

Data Collection and Sample:

Through a questionnaire on the study variables requested as a key tool for the study. And distributed analytic and using (SPSS), where they were to distribute 100 questionnaire in a random manner on the working banks in the Syrian Arab Republic.

Questionnaire contains three sections: the use of closed questions for the first demographic information, and estimate using the Likert scale quintet concerning the second measure of credit risk, and the second scale guide banks towards strengthening the discipline of market transparency and disclosure in the market of Damascus.

Been testing the internal consistency of the questionnaire using the reliability coefficient Alpha Cross, where he showed results that the value of the reliability coefficient is acceptable for all areas because it is higher than the value of (0.70). Showed coefficients of reliability (Alpha cross) the paragraphs of the Spheres also link each paragraph to the total paragraphs in each area.

To process data and analyze the results of the field study, the following statistical methods were using:
1. Descriptive statistics
2. "One sample T test".

First: using the Frequencies descriptive statistical test to analyses the first axis on demographic information, to learn the results of random sampling and the relationship between variables:

Where it turns out that the number of individuals of the sample who answered this question by 66.3 of males and females was 32.7, the ages have increased by 38.6 of more than 18 years of age and 34.7 of 25-35 years of age and 13.9 of 35-45 years of age and 11.9 of the most in a year.

The percentage was 17.8 from a secondary school, 39.6 from a university and 18.8 from a graduate school, and a percentage of 22.8 from the other,

Moreover, the percentage was 43.6 from a worker or trainee in a bank, 55.4 from a non-worker or a trainee in a bank, and the proportion was 30.7 with an account in a public bank and 35.6 with an account in a private bank and the percentage of 32.7 has a two-account.

Second: To improve the paragraphs of the questionnaire, (One Sample T test) for the sample one T-test were used and significance level of the t attribute in the following tables we find they contain the arithmetic average of the relative weight of the average value of each paragraph,

In addition, the paragraph is positive in the sense that the respondents agree on its contentpreferably, either this test in the discovery of the existence of differing moral Significant Difference.

To the average community in which pulled from the sample about the value of a fixed Constant added to the possibility of estimating the confidence interval for the average community uses this test the sample is small.

Measures

Statistical results for testing the first hypothesis:

Development of systems for credit risk management in accordance with the new framework of capital adequacy in accordance with Basel II in banks operating in Syria, strategies and policies adopted by the Council of money and credit and instructions of the banking supervision.

Table No. (1)

		Arithmetic mean	**Relative weight**	**The value of the tabular T**	**Significance level**
1	**There is a clear and written credit policy in the bank under the terms of the cash and Loan Board.**	2.45	82.75	**4.07**	**.000**
2	**The bank makes field statements before granting credit.**	**2.29**	87.45	**5.064**	**.000**
3	**The bank monitors the customer's financial position after granting credit.**	**2.39**	85.45	**4.231**	**.000**
4	**There is a fear that the troubled customer will be treated for fear of the bank's reputation.**	**2.34**	85.64	**4.972**	**.000**
5	**In your opinion, the requirements and preconditions for effective banking supervision according to Basel II, and whether they are sufficient and comprehensive.**	**2.52**	83.85	**3.32**	**.001**
6	**In your opinion, the standards, precautionary rules and basic requirements for oversight are sufficient according to Basel II in banks.**	**2.33**	84.91	**4.81**	**.000**
7	**In your opinion, to determine the continuous control methods by adopting a system of early preventive measures in relation to credits according to Basel II.**	**2.53**	83.64	**3.439**	**.001**
8	**Do you think that the powers given to the regulatory authority according to Basel II are sufficient and to measure credit risks accurately and efficiently.**	**2.38**	79.27	**4.481**	**.000**
9	**In your opinion, does the supervisory authority require foreign banks operating within the scope of its supervision to exercise in their domestic operations the standards and information that the supervisory authority needs in order to carry out unified supervision?**	**2.48**	81.09	**3.706**	**.000**
10	**Do you think that oversight is outside the borders by exercising a unified and comprehensive supervision of international banking institutions that are subject to its supervision?**	**2.18**	81.09	**6.645**	**.000**
11	**Is the central bank based in its oversight on other banks based on the Basel II principles of oversight?**	**2.14**	85.82	**7.283**	**.000**

12	**Do you think the Basel II principles of banking supervision are appropriate for the work of supervision of banks operating in Syria?**	**2.30**	85.27	**4.988**	**.000**
13	**Are the decisions of the Central Bank of Syria tending to privacy in order to effectively serve its oversight**	**2.30**	82.91	**4.988**	**.000**
14	**Do you see the commitment of the Central Bank to Basel II principles of banking supervision as a contributing role in mitigating the risks that banks are exposed to**	**2.43**	84.67	**3.819**	**.000**
15	**Do you think that the number of field monitors with the Central Bank is sufficient for field supervision in banks in Syria**	**2.43**	86.00	**3.985**	**.000**
	All paragraphs	**2.37**	**83.99**	**4.65**	**0.000**

Data Source: Author

Table No. (1) analysis of the paragraphs of section first where it follows that the views of the respondents in all the paragraphs positive as the relative weight of each item greater than 60% and the level of moral less than 0.05 as equals 0.000 .

In general, the calculation average for all first hypothesis paragraphs is 2.37, and the relative weight is 83.99%, which is greater than 60% .The calculated t value is 4.65, which is greater than the tabular t value of 1.98. Which means acceptance of the hypothesis i.e. there is significant relationship between the development of management systems credit risk under the new framework of capital adequacy in accordance with Basel II in banks operating in Syria, strategies and policies adopted by the Council of money and credit and instructions of the banking supervision.

Statistical results for testing the second hypothesis:

Development of systems for credit risk management in accordance with the new framework of capital adequacy in accordance with Basel II in banks operating in Syria and its orientation towards strengthening the discipline of market transparency and disclosure in the market, by providing information to market participants about the adequacy of capital.

Table No. (2)

		Arithmetic mean	Relative weight	The value of the tabular T	Significance level
1	**The bank abides by the administrative and accounting policies set by the senior management**	2.55	86.00	-3.027	.003
2	**Transparency and financial disclosure of the bank's financial statements periodically towards strengthening market discipline, "transparency and disclosure in the market", and the role of the central bank in its application by providing information to market participants about the extent of capital adequacy, the quality and size of credit risks to which the bank is exposed**	2.58	86.00	-2.952	.004
3	**There are severe penalties for employees when violations of integrity and honesty are discovered at work**	2.55	86.67	-3.041	.003
4	**The Central Bank studies the risks to which the bank is exposed and periodically assesses its financial position**	2.53	82.26	-3.051	.003
5	**The bank shall abide by the percentages prescribed by the central bank to form the legal reserve**	2.51	85.64	-3.208	.000
6	**The bank shall abide by the percentages prescribed by the central bank with liquidity**	2.07	80.73	-6.812	.000
7	**The bank shall abide by the percentages prescribed by the central bank to grant credit**	2.41	79.27	-3.903	.003
	All paragraphs	2.46	83.80	3.71	0.003

Data Source: Author

Table No. (2) analysis of the paragraphs of the second hypothesis where it follows that the views of the respondents in all the paragraphs positive as the relative weight of each item greater than 60% and the level of moral less than 0.05 as equal to 0.003 .

In general reached the arithmetic mean of all paragraphs of the second hypothesis equals 2.46, weight 80 relative helps 83.80%, which is greater than 60% .The calculated t value is 3.71 and is higher than the tabular t value of 1.98. Which means accepting the hypothesis, which explains the significant relationship the development of management systems credit risk under the new framework of capital adequacy in accordance with Basel II in banks operating in Syria and its orientation towards strengthening the discipline of market transparency and disclosure in the market, by providing information to market participants about the adequacy of capital.

IV. CONCLUSION

The study concludes a set of results showing the environment of credit risk management in banks operating in the Syrian Arab Republic as follows:

1. There is a statistically significant relationship between developing credit risk management systems according to the new framework for capital adequacy in accordance with Basel II in banks operating in Syria, strategies and policies adopted by the Monetary and Credit Council and banking supervision instructions.
2. There is an agreement to define continuous methods of control by taking a system of early preventive measures in relation to credits in accordance with Basel 2 and the basic requirements for the availability of control information applied by operating banks, by maintaining proper records prepared in accordance with integrated accounting policies and practices.
3. There is a significant relationship with developing credit risk management systems according to the new framework for capital adequacy in accordance with Basel II in banks operating in Syria and their orientation towards strengthening market discipline, transparency and market disclosure, by providing information to market participants on the extent of capital adequacy.
4. The bank is subject to government policies through the central bank and the Monetary and Credit Board, which studies the risks to which the bank is exposed and periodically assesses its financial position. The bank is committed to the rates stipulated by the central bank by forming legal reserves, liquidity, and credit provision.

Suggestions for Future Research

The research concludes a set of recommendations, constitute a whole systems development methodology and credit risk management are as follows

1. That banks work to improve the management of banking risks in their diversity and strict application of these principles, which require banks to adhere to the application of international standards in the areas of capital adequacy, audit, accounting, transparency and disclosure.
2. Work to ensure that the credit policies of banks are compatible with changes in economic conditions, which increases the expectations of credit risks in banks, especially in the current crisis
3. Increased disclosure and transparency of financial and non-financial information, especially about the current risks the potential facing the bank, which motivates the banks to improve the exercise of its business strongly and the strictness in applying commitment to the stipulated ratios in terms of granting credit, liquidity and formation of legal reserves.
4. In order to enhance the effective role of supervision by the Central Bank and the Monetary and Credit Council, an increase in the number of its monitors must be carried out in order to activate its role by reducing credit risks to all its subsidiaries in the Syrian governorates.

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