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The Role of Risk Management in Banking

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ABSTRACT

The banking industry is an industry that is full of risks, especially because it concerns the management of people's money and is filtered in the form of investment. This article uses literature study research. To minimize the risks faced, bank management must have adequate expertise and competence, so that various risks that have the potential to arise can be anticipated from the beginning, and seen for better handling. The types of risks presented by economists are very diverse but substantially similar to each other. Broadly speaking, the grouping of risks carried out by economists is almost the same description and scope. The larger and more modern banks, the more and more complex the risks they face. Financial risks faced by the banking industry can be broadly grouped into 5 (five) major risks, namely: (1) credit risk, (2) market risk, (3) liquidity risk, (4) operational risk, and (5) capital risk. These risks are presented in financial ratios, which indicate that: the performance that management achieves in managing the bank.

Keywords*: Risk Management, Financial Ratios, Banking Industry*

INTRODUCTION

Banking or banks are business entities that collect funds from the community in the form of deposits and distribute funds from the community in the form of credit or other forms in order to improve the standard of living of many people. The banking industry has a strategic position as a financial intermediary institution to support the smooth running of the economy (Law of the Republic of Indonesia no. 10 of 1998). One of the functions of a bank is as a depository of funds, including individual and family funds. These individual and family funds are short-term deposits and have high liquidity. If banks fail to meet this deposit liquidity, it will have a wide impact on the community. In addition, banks also have the power to create money in easy-to-spend forms such as investments and loans. Changes in the amount of money created by banks appear to correlate with economic conditions, especially in the growth of employment and inflation (Rose, 2002: 34).

Based on the need for a national banking blueprint and as a continuation of the banking restructuring program that has been running since 1998, Bank Indonesia on January 9, 2004 has launched the API as a comprehensive framework for the policy direction of Indonesia's banking industry development in the future.

One of API's pillars states the importance of creating a strong and highly competitive banking industry, as well as having resilience in facing risks. The rapidly developing internal and external banking environment is accompanied by increasingly complex risks of bank business activities, requiring banks to implement adequate risk management, and implement it in a disciplined manner. The application of risk management in banking is very important in creating a healthy and integrated banking industry, so that the bank's business is run in a risk corridor that remains under control. The implementation of orderly risk management in every bank will in turn create an increasingly healthy industry.

The role of risk management itself is to reduce risks that vary and are related to banks. The implementation of risk management can increase shareholder value, providing an overview to bank managers about the possibility of bank losses in the future. The implementation of risk management for Bank Indonesia as the bank's supervisory authority will make it easier to assess the possible losses faced by banks that could affect the bank's capital.

METHOD

This research uses a literature study research method. This type of research is a series of activities with a method of collecting references or theoretical foundations from books and journals, literature studies can be carried out by collecting several references consisting of several previous studies by examining several journals related to the application of risk management in minimizing operational risks. The results of this literature or literature research process are used to review several things that cause operational risks and how to apply risk management in minimizing operational risks

RESULT AND DISCUSSION

Risk management in banking is often still a fundamental problem in the banking world in Indonesia and international banking, even in the context of banking. Every business, of course, has its own risks depending on the type of business being run, including the banking business. Although banking is sometimes seen as a safe business, there are also many risks that threaten so that all risks must be processed and all related risk management must be made so that it can reduce existing banking risks.

The risk referred to here is a risk that can indeed cause losses in the future, so the risk that may be the most threatening is credit risk which will be overcome by credit analysis. However, usually this credit analysis is not an efficient risk management. In addition, the effectiveness of this risk management still needs to be questioned because there are still various gaps that must be fixed.

Not only banking actors must update their knowledge about banking, but banking supervisors must also know about banking risk trends that may be faced in the future. However, in reality, these banking supervisors did not show a quick response in responding to changes in the world where banking continues to move dynamically, unlike bankers. Indeed, to create a stable bank, there are many factors that play a role, but banking supervision is considered to be one of the most important factors in creating a healthy banking climate.

Meanwhile, in practice itself, to create a stable banking supervision, several supporting factors are also needed, including good infrastructure, for example, independent public accountants, adequate banking regulations, good resolution of banking problems, and many other things that affect. Risk management in banking is also pursued through good banking supervision, not only with credit or financial analysis. Such an analysis is not effective enough to process the existing risks.

However, the important thing that we should not ignore is the establishment of a good banking supervision system, including whether or not the approach used in banking supervision is right or not, as well as how human resources are used as the main source of driving force or prime mover in this case. Therefore, below will be further described about the role of banking risk management to create a good banking climate.

a. The Importance of Banking Risk Management

In the current banking condition, it is undeniable that risk management is one of the things that must and must be done by every bank management to maintain the continuity of Indonesia's banking today. The banking business may be considered safe, but if we look closer, it turns out that Indonesia's banking itself has a much greater risk compared to other businesses that are developing in Indonesia.

This risk arises because basically, banks always provide credit to customers with a large amount that is usually quite large and for a long period of time. Maybe for a short period of time, the flow of funds from credit will still flow smoothly, but in the long term, it will not necessarily still be good. In addition, the bank's own management still uses the principle of prioritizing corporate profits so that it often clashes with the risks that are usually inherent in every policy taken.

b. Management Role

To implement a policy, of course, this cannot be separated from the role of bank management who participate in supervising and determining the course of the policy. Likewise, in the implementation of risk management where managers, senior managers and the board of directors are required to guide the implementation of risk management and supervise whether risk management in the banking that is carried out can effectively reduce the risk of losses in the future.

c. Banking Management Risks

Risk management in banks can be carried out with several risk management processes, namely by the process of identification, monitoring, risk control and risk management information systems. Risk identification includes the definition of various risks, all bank activities are carried out to analyze the sources and causes of risks and their impacts (Goyal, 2010) where the types of risks are divided into

two risk groups, namely financial risks and non-financial risks. Financial risks include market risk and credit risk which are the second pillars in Basel II while Non-Financial Risk which refers to risks that may affect the growth of the bank's business, sales of products and services, possible failure of strategies aimed at business growth and others, risks that may arise due to management failures, competition, non-availability of products/services, Operational Risk is part of non-financial risk which is defined as the risk of loss due to inadequacy or failure of internal processes and systems or due to external events, in the application of Basel II is the second pillar.

Furthermore, banks need to measure risk in accordance with the characteristics and complexity of business activities which include:

a. Credit risk
b. Operational risks
c. Market risk
d. Liquidity risk
e. Risk capital

Meanwhile, operational risks include:

a. Strategic risk measurement
b. Capital risk
c. Political risks
d. Legal Risks

In addition, the effectiveness of the implementation of risk management needs to be supported by risk control by considering the results of risk measurement and monitoring (Bank Indonesia, 2011).

d. Opinion

As is well known, risk management is identifying, measuring, monitoring, and controlling the course of a bank's business activities with a reasonable level of risk in a directed, integrated, and mutually sustainable manner.

Then there are various ways to overcome risks and make the bank's function even better, one of which is the need for good management, so that it can minimize unexpected things. Risk management is one of the functions of various banks that serve risk management which consists of identifying risks and controlling them.

Banks must also have monitoring systems and procedures that include risk exposure, risk tolerance, compliance with internal limits, and consistency of implementation with established policies and procedures.

Basically, risk management is an action to anticipate losses from business activities carried out. In terms of banking, risk management can also be used to analyze a risk in the future. But in reality, future events are impossible to know. As Allah said in Q.S Luqman: 34

اِنَّ اللّٰهَ عِنْدَهٗ عِلْمُ السَّاعَةِۚ وَيُنَزِّلُ الْغَيْثَۚ وَيَعْلَمُ مَا فِى الْاَرْحَامِۗ وَمَا تَدْرِيْ نَفْسٌ مَّاذَا تَكْسِبُ غَدًاۗ وَمَا تَدْرِيْ نَفْسٌۢ بِاَيِّ اَرْضٍ تَمُوْتُۗ اِنَّ اللّٰهَ عَلِيْمٌ خَبِيْرٌ

"Indeed, Allah, only in His side is the knowledge of the Day of Resurrection; and He is the one who sends down the rain, and knows what is in the womb. and no one can know (with certainty) what he will do tomorrow and no one can know on what earth he will die. Indeed, Allah is All-Knowing, All-Knowing."

CONCLUSIONS

Banking or banks are business entities that collect funds from the community in the form of deposits and distribute funds from the community in the form of credit or other forms in order to improve the standard of living of many people. One of the functions of a bank is as a depository of funds, including individual and family funds.

The risk referred to here is a risk that can indeed cause losses in the future, so the risk that may be the most threatening is credit risk which will be overcome by credit analysis. Meanwhile, in practice itself, to create a stable banking supervision, several supporting factors are also needed, including good infrastructure, for example, independent public accountants, adequate banking regulations, good resolution of banking problems, and many other things that affect. To implement a policy, of course, this cannot be separated from the role of bank management who participate in supervising and determining the course of the policy.

The types of risks presented by economists are very diverse but substantially similar to each other. Broadly speaking, the grouping of risks carried out by economists is almost the same description and scope. The larger and more modern banks, the more and more complex the risks they face. Financial risks faced by the banking industry can be broadly grouped into 5 major risks, namely credit risk, market risk, liquidity risk, operational risk, and capital risk. These risks are presented in financial ratios, which indicate that: the performance that management achieves in managing the bank.

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