Relationship between Information Sharing and Risk Management Practices with Financial Performance: Evidence from Pakistani Banking Sector

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Abstract

This research aimed at determining the effects of information sharing and risk management on the financial performance of banks in Pakistan. A sample included ten banks top in the ranking on assets and questionnaires were distributed among 200 managers of different levels. Correlation and regression analysis is used to determine relationship between information sharing and risk management on the financial performance. The results revealed that both information sharing and risk management has positive effect on the financial performance of selected banks.

Keywords: Information sharing, Risk Management, Financial performance, Banking sector and Regression.

Introduction

The liberalization and commercialization of banking industry and financial institutions in a country like Pakistan has resulted in to intense competition and survival of the firm now hinges upon the performance delivered. The variety of factors like increase in interest rates and high loan default and shrinking profit and declining service quality have eroded the performance indicators and success rate of many banks. Quality in service sector is rated most crucial factor as customers satisfaction and loyalty is directly associated with it (Baloch, Gohar and Jamshed, 2014). In banking sector's operational and service quality domains, the factors like risk management and information sharing are very pivotal in building customers trust and loyalty and enhancing customers' satisfaction level as risk is predominant factor in banking business (Hussein et al, 2010). Carey (2001) argues that the practices of

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risk management have got more importance in financial sector than any other in any economy. According to the survey conducted by the Ernst & Young (2000) bank's internal audits sometimes failed to identify bank's most vulnerable areas and therefore about eighty percent of frauds are committed by the organizations employees themselves and hardly 30 percent of those could be managed.

Besides risk management, banks are also lacking information sharing amongst staff members as well as with customers who lead to mis-coordination, duplicity of efforts and misinformation therefore needs to be properly managed need proper management but which is mainly due to the low qualification or incompetency. The positions they have occupied in different banks are not as per their qualification. Due to this evidence it is found that the employees in banks have limited information exposure, which has caused asymmetry level of information within the staff. The reason being it is given more importance to information sharing and risk management so as to improve their financial performance and establish a well organized and effective system.

The banks in Pakistan exhibits tough competition, increasing number of dormant account holders, increasing level of interest rates and high loan default continue to exist, which has posed problems for the decision makers and top management. If this sector ignore these issues and remained uncheck than it will be definitely a misery in this particular banking sector.

This study is aimed at establishing the relationship between information sharing risk management practices and financial performance of commercial banks in Pakistan and knowing the impact of both information sharing and risk management on the banks financial performance.

Research Questions

- What kind of practices of information sharing and risk management are there in banking sector in Pakistan?
- What is the effect of risk management and information sharing on the financial performance of these banks in Pakistan?

Literature Review

Banks decreases the price and cost of monitoring and helps resolve the issue between borrowers and lenders (Diamond, 1984 & 1991). In line with this specific traditional view a close relationship between bank and firm is very vital as it helps in improving the information production and then this help increase corporation access to investment capital in very good business prospects. However, in case banking institutions acquire monetary rental prices in the purchaser firms through facts monopolizing, they will decrease firm's motivation for you to do brandnew along with successful initiatives (Rajan, 1992). Additionally, in case if banking institutions are entrenched with their sort of client then bank can improve and play role in economic development, banking institutions can easily impede monetary development (Matsuura, Pollitt, Takada, and Tanaka, 2003)

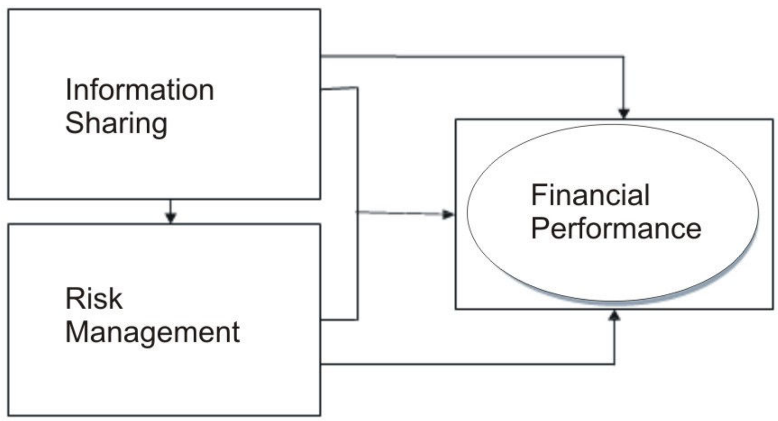
Wafula (2009) illustrated that risk management is portfolio of activities designed to improve performance and to reduce the possible losses of the firm. Handling risk happens to be one of the area usually checked out to guarantee the achievement in term of financial performance, and help its achievements (Scholtens et al 2000). Commercial banks usually feel that they are having riskier business and risk management for any financial institution is very vital (Hussein et al 2012). Different studies argued that risk management is very vital for the firm efficiency as this can really improve the performance of banks. Risk management is very vital for each bank and every bank tries to manage its risk as per its capacity the bank holds (Erturk, Ismail, and Stefano Solari (2007). This is series having BCBS (2006) which often flatly reported which the long term associated with banking will certainly rest in danger managing mechanics. The general disagreement is actually of which bank's emergency depends en route danger managing practices usually are executed and checked.

Information sharing as well as risk operations & management are crucial in any bank as the kind of risk management and information sharing help in bank success and ultimate achievement. The same was argued by Kun Liano (2011) who argued that information sharing help in improving the operation of the bank and through information sharing help reducing the information gap. In such a case ownership is much concentrated and the stockholders are less worried.

Barger A, (1994) discovered that profitability of the bank is dependent upon the bank information sharing system and risk management it does. These two can bridge the gap. Hussiein et al (2010) argued that the purpose of financial institutions should be to make best use of earnings as well as provide the majority of benefit to help shareholders by giving selection of monetary providers particularly by controlling pitfalls. This is furthermore based on who argued that the Ferrier, Gary D. and C.A. KnoxLovell (1990) tactical position and survival of the bank is dependent on its information sharing and risk management.

Theoretical Framework

The following theoretical framework developed as a result of in-depth review of the related literature for this research study.



The theoretical frame work shows that the dependent variable of this research study is financial performance and Information sharing and risk management are independent variables. Information sharing is measured by modifying the scales developed by Marchand et al. (2001) and Kun Liano (2010). Risk management is measured with scales developed by Devellis (1991) & Hussein et al (2010) whereas, Financial performance is measured through the scale of Lyles et al (1996).

Hypotheses

H1: Information sharing has positive impact on the financial Performance of banking sector in Pakistan.

H2: Risk Management has positive impact on the financial performance of Banks in Pakistan.

Research Model

Financial performance = B0 + B1 information sharing + μ.

Financial performance = B0 + B1 Risk management + μ.

Research Methodology

This study has used a cross sectional and correlation research design. Correlation and Regression approaches have been used to investigate the relationships between the variables of study. The population of this study was comprised of all commercial banks registered in KSE in Pakistan. The data has been collected through questionnaires using stratified sampling techniques. The data has been collected from operation managers, branch managers, risk managers and credit managers. Total 200 respondents have been included in the data analysis of this research. The data of this research has been statistically analyzed through, Reliability analysis, correlation and regression.

Data Analysis

The data analysis of this research paper comprises of the reliability analysis, correlation analysis and regression analysis.

Reliability analysis

Variables	Cronbach alpha values
Financial performance	0.76
Information sharing	0.72
Risk management	0.81

The above table reflects the reliability of the data which was obtained from the respondents. The alpha values of the data collected from the respondents of all the three variables are well above the desired values. There is consistency in the responses of the respondents of this research study hence the data is reliable for knowing and testing the hypothesis of this research paper.

Correlation Analysis

Variables	Financial performance	Information sharing	Risk management
Financial performance	1.000		
Information sharing	0.256	1.000	
Risk management	0.354	.0567	1.000

The above table shows the correlation between the variables of this study. Usually correlation is used in research to understand the strength and direction of association between variables. The correlation of this research paper suggests that both information sharing and risk management are significantly positively correlated with the financial performance of banks. Both information sharing and risk management has correlation value i.e. 0.256 and 0.354 respectively which is well above the critical values of significant level of correlation i.e. r = 0.200.

Regression Analysis

Model 1: The impact of information sharing on the financial performance

Financial Performance

Predicator	Beta	R.square	Adjusted R.square	F.value	T.value	P.value
Information sharing	0.421	0.321	0.314	12.342	2.565	0.0213

The above table shows the results of the model-1 of this research paper i.e. the impact of information sharing on the financial performance of banks. The results of this model suggest that information sharing has positive significant impact on the financial performance of banks in Pakistan. The T-value of information sharing is 2.565 which is well above the critical value i.e t=2.So meaning that information sharing is individually statistically significant. The R.square is 0.321 meaning that almost 32% change in dependent variable financial performance is caused by the independent variable information sharing. The F. value 12.342 suggests that the overall model is significant. The beta value reflects the dimension of a unit change. The above results of the first model of this study indicates that in Pakistani commercial bank the information sharing in employees have significant impact on the financial performance of banks.

Model 2: The impact of Risk management on the financial performance
Financial Performance

Predicator	Beta	R. .square	Adjusted R.square	F. value	T. value	P. value
Risk management	0.478	0.384	0.376	15.367	3.234	0.001

The above table shows the results of the model-2 of this research paper i.e. the impact of risk management on the financial performance of banks. The results of this model suggest that information sharing has positive significant impact on the financial performance of banks in Pakistan. The T-value of information sharing is 3.234 which is well above the critical value i.e. t=2.So meaning that risk management is individually statistically significant. The Square is 0.384 meaning that almost 34% change in dependent variable financial performance is caused by the independent variable information sharing. The F. value 15.367 suggests that the overall model is significant. The beta value reflects the dimension of a unit change. The above results of the 2ndmodel of this study indicates that in Pakistani commercial the risk management has got more importance as it has positive significant impact on the financial performance of these commercial banks.

Conclusion

The results of this study revealed that there is positive correlation between information sharing, risk management and financial performance. The results clearly indicated that both information sharing and risk management positively impact the financial performance. Due to this study it is evidenced that highly informative structure and information support based system will definitely support the risk management of the bank. The research establishes that information sharing positively impacts the financial performance. Keeping in view this fact it is very vital for the management to share information with in the bank in employees and to costumer so that to reduce the information gap. Since the main purpose of any financial institution is to maximize profit and to avail adequate financial services to shareholders and customers through the risk management mechanism therefore, adequate information system and risk management will improve the financial position of the banks.

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