



# CAPITAL MANAGEMENT IN THE LIGHT OF FINANCIAL ENVIRONMENT RISKS-AN APPLIED STUDY IN A SAMPLE OF IRAQI BANKS

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Article history:		Abstract:
Received:	11 <sup>th</sup> April 2025	<p>The current research aims to analyze and evaluate capital management methods in Iraqi banks in light of the escalating financial risks facing the banking environment, such as liquidity risks, credit risks, and economic fluctuations. The research adopted a practical approach by collecting data from a representative sample of Iraqi banks using a quantitative analytical approach. Financial data from a group of Iraqi banks was collected and analyzed during 2022 and 2023. The research utilized advanced statistical analysis tools, particularly simple regression and analysis of variance (ANOVA), to examine the relationship between capital management and financial risks in the banking environment. A number of basic financial indicators were also employed to measure capital adequacy levels, such as the capital adequacy ratio (CAR), liquidity indicators, and asset quality, along with indicators reflecting the various levels of risk facing banks. The research revealed a general weakness in capital management among the Iraqi banks in the research sample, particularly given the decline in the capital adequacy index during 2023 compared to 2022. This illustrates how these banks are more vulnerable to financial risks and are not adequately equipped to withstand shocks. The study's most significant recommendation is that Iraqi banks examine their capital management procedures, emphasizing the improvement of capital adequacy to handle any upcoming financial crises.</p>
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## INTRODUCTION

The foundation of banking operations is investment, which serves as the main source of capital growth and returns, supports the bank's sustainability, improves its capacity to serve client needs, and boosts the economy. However, the effectiveness of this investment is inseparable from the nature of the financial environment in which the bank operates, which is characterized by complexity and volatility, especially in Iraq, where financial risks are intertwined with local market challenges and political and economic instability. Since poorly thought-out investment choices can result in enormous losses that jeopardize the bank's financial stability, a thorough understanding and analysis of the nature of these risks is a necessary first step in creating effective investment strategies. Hence, the significance of this study, which examines actual data from a sample of Iraqi banks in order to offer a workable framework for the best possible investment in this complicated environment, This contributes to developing new insights for investment management and risk reduction.

## Chapter One : Research Methodology

### First: The Research Problem

Iraqi banks currently face increasing challenges due to the turbulent financial environment and growing levels of risk, particularly credit, liquidity, and interest rate fluctuations. Capital is one of the fundamental pillars upon which banks rely to absorb financial shocks and achieve stability. However, there are significant concerns regarding the effectiveness of capital management in these banks and their capacity to adjust to the rise in external risks given the notable drop in capital adequacy metrics in recent years. Hence, the research problem stems from an attempt to understand the



relationship between capital management and financial risks, and to assess the impact of these risks on the performance of Iraqi banks. The following questions can be posed:

1. How efficient was capital management in Iraqi banks during the study period?
2. How do financial risks (credit, liquidity, interest rates) affect capital management?
3. Is there a statistically significant relationship between capital adequacy and the level of financial risk in banks?

## **Second: The Importance of the Research**

The importance of this research stems from its addressing one of the most important issues facing the Iraqi banking sector: banks' ability to manage their capital efficiently in light of rising levels of financial risk. The importance lies in providing realistic analytical indicators based on actual data from a sample of banks. In addition, it contributes to assessing the effectiveness of financial policies and assists regulatory and supervisory authorities in making more accurate decisions to enhance financial stability and reduce defaults. The research also provides a framework for future studies related to capital and risk management in emerging economies.

## **Third: Research Objectives**

1. Analyze capital adequacy in Iraqi banks and determine their suitability for addressing financial risks.
2. Evaluate the impact of capital management on financial risks (credit, liquidity, interest rates).
3. Measure the relationship between capital adequacy and financial risks using statistical analysis tools.
4. Provide recommendations to improve capital management efficiency and enhance resilience to future financial crises.

## **Fourth: Research Hypotheses**

1. There is a statistically significant relationship between capital adequacy and financial risks in Iraqi banks.
2. Credit risks negatively impact capital management efficiency.
3. Liquidity and interest rate risks have a significant impact on the level of capital adequacy in banks.

## **Fifth: Research Methodology**

The research relies on a quantitative analytical approach, where the financial data of a group of Iraqi banks during 2022 and 2023 were analyzed using statistical analysis tools, particularly simple regression and analysis of variance. The degree of risk and capital adequacy were also assessed using a variety of financial indicators.

## **Sixth: Research Population and Sample**

The research population consists of Iraqi banks listed on the Iraq Stock Exchange. A purposive sample was selected, including six banks: (United Investment Bank, Dijlah and Euphrates Bank, Iraqi Investment Bank, Baghdad Bank, Sumer Bank, and Al-Tanmiyyah Bank). These banks were selected based on the availability of published and analyzable financial data.

## **Seventh: Research Limits**

- **Temporal Limits:** The research covers financial data for the years 2022 and 2023.
- **Spatial Limits:** The study is limited to a sample of Iraqi banks operating within Iraq
- **Substantive Limits:** The research focuses on the relationship between capital management and financial risks (credit risk, liquidity risk, interest rate risk).

## **Section Two : Financial Investment and Banking Risks**

### **First: Financial Investment**

- 1- **Concept:** According to Rajendra Prasad G R (2022), investment banks play a pivotal role in mobilizing financial resources and directing them toward productive investments, which promotes economic growth. He defines investment banking as "the process of employing available financial resources in various financial instruments with the aim of generating future returns, taking into account the associated risk levels" (Krause, 2023, p. 45).
- 2- **Objectives:** Objectives of investment banking according to the study: Objectives of investment banking according to (Sharif & Ena, 2023).
  - A. Providing financial advisory services: Advising companies on financial structure, governance, and growth strategies.
  - B. Facilitating mergers and acquisitions: Assisting companies in executing mergers and acquisitions efficiently.
  - C. Ownership structuring: Analyzing and providing recommendations on optimal ownership structures to enhance financial performance.



- D. Improving corporate governance: Enhancing governance practices to make certain transparency and responsibility.

**3- Types:** According to Wang (2023, p. 90), investment banking consists of numerous foremost sorts, including:

- A. Securities Underwriting: Providing underwriting services to companies wishing to trouble new shares or bonds.
- B. Financial Consulting: Advising organizations on financial structure, governance, and growth techniques.
- C. Asset Management: Managing investment portfolios for character and institutional clients.
- D. Mergers and Acquisitions Facilitation: Assisting corporations in executing mergers and acquisitions effectively.
- E. Secondary Market Activities: Trading securities in secondary markets to provide liquidity to traders.

**4- The Impact of Investment on Market Value:** Recent literature shows a tremendous and giant relationship between return on investment (ROI) and market cost of banks. ROI is a key indicator that reflects a monetary organization's operational efficiency in deploying its assets to attain tangible monetary returns. Shubita's (2023) have a look at established that a excessive ROI without delay contributes to enhancing investor confidence in a bank's stock, main to expanded call for for the inventory within the economic market and, therefore, a better marketplace fee.

When a higher ROI is achieved, financial markets interpret it as a signal of management's efficiency in generating returns using minimal resources, which increases the bank's investment attractiveness in the eyes of both individual and institutional investors. The results of the study's regression analysis also indicate that the effect of ROI on market value was highly statistically significant, confirming that investment performance is not only an internal indicator of operational efficiency but also plays a direct role in shaping a bank's market value on stock exchanges (Shubita, 2023, p. 14).

## Second: Financial Risks

- 1- **Concept:** Refers to the possibility of incurring financial losses as a result of multiple factors that affect the ability of individuals or institutions to meet their financial obligations. These risks are an integral part of the financial environment (Investopedia, n.d.).
- 2- **Types:** According to many studies, risks are divided into:
  - A- Market risk: This arises from fluctuations in the prices of financial assets such as stocks, bonds, currencies, and commodities. This risk includes interest rate risk, exchange rate risk, equity risk, and commodity risk.
  - B- Credit risk: This relates to the inability of a borrower to repay debts or financial obligations, resulting in losses for lenders or investors (Investopedia, 2024, n.d.).
  - C- Liquidity risk: This occurs when an organization cannot convert its assets into cash quickly enough to meet short-term financial obligations, which could lead to financial distress. (SAS Institute, n.d.).
  - D- Operational risk: This results from failures in internal processes, systems, or people, or external events, such as fraud, human error, or natural disasters.
  - E- Legal and regulatory risk: This relates to changes in laws and regulations that could affect an organization's financial operations (Fabozzi & Peterson). (Drake, 2009, p. 55)
  - F- Environmental risks: These relate to the financial impacts resulting from climate change and natural disasters, which may affect asset values and repayment capacity. (Popova et al., 2021, p. 3)
- 3- **The impact of banking risks on bank performance:**

The impact of credit and liquidity risks on the performance of commercial banks. Credit risk: The study showed that an increase in the non-performing loan (NPL) ratio leads to a decrease in the return on assets and return on equity, indicating a negative impact on bank performance. Liquidity chance: The study outcomes showed that an increase within the mortgage-to-deposit ratio (LDR) negatively impacts the go back on fairness, reflecting the impact of liquidity on a financial institution's potential to generate earnings.

These results emphasize the importance of effective banking risk management to ensure the stability and performance of banks. (Abbas & Ullah, 2023, p. 210)

## 4- The Relationship Between Investment and Financial Risk:

Oehler and Horn (2024) imply that the relationship among investment and monetary chance is drastically influenced with the aid of individuals' level of financial awareness. The researchers located that investors with high economic cognizance are better able to manage the monetary dangers associated with excessive-hazard funding assets, reducing their aversion to these property and increasing their possibilities of collaborating in economic markets. This way that financial cognizance not best directly impacts investment decisions however also acts as a mediating factor that reduces the psychological dangers associated with making an investment. The take a look at also showed that net really worth

and the level of monetary training are motivating elements for powerful participation in financial markets, as they offer a better foundation for information and assessing investment dangers. (Oehler & Horn, 2024, p. 25)

A. The Relationship Between Risk and Return within the Stock Market: Oyedeko et al.'s study addressed this issue. (2023) The effects discovered that the connection among risk and go back is not as easy as conventional models count on. The take a look at showed that methodical hazard has a poor effect on economic returns, even as unsystematic danger tends to beautify returns. This indicates that buyers want to cautiously examine the diverse dimensions of risk, no longer simply systematic danger, with the intention to make more accurate and powerful funding selections in developing monetary markets (Oyedeko et al., 2023, p. 72).

A. The Impact of Financial Risk on Investment Decisions in Emerging Markets: Chen and Wang (2023) tested the impact of monetary risk on funding decisions in rising markets, focusing on how buyers respond to exceptional tiers of monetary hazard. The effects confirmed that extended financial danger appreciably reduces investors' willingness to have interaction in excessive-danger initiatives, specially in emerging markets that lack a robust monetary infrastructure. The examine additionally confirmed that traders have a tendency to select decrease-chance investments, even supposing the expected returns are decrease, confirming that monetary chance control is a critical element in funding choice-making (Chen & Wang, 2023, p. 12). This reflects the importance of developing financial risk assessment and management mechanisms to help investors make informed investment decisions, especially in highly volatile economic environments (Amponsah, Ntim, & Mensah, 2025, p. 1).

### Section Three : The Practical Aspect

This have a look at analyzes the real reality of capital management inside the research sample, through analyzing a set of financial signs and regulatory requirements, in addition to tracking the impact of surrounding dangers—inclusive of market risks, credit risks, and liquidity risks—on capital control decisions. A quantitative evaluation method became adopted, relying on the annual financial records of the research pattern, together with using statistical gear to help check the proposed hypotheses and explain the relationships among the variables below have a look at.

#### First: Capital Management

In a financial environment characterised by means of instability and increasing risks, the importance of capital management emerges as a fundamental tool for making sure the steadiness and sustainability of banking performance. The capital adequacy ratio is one of the most important supervisory equipment used in this context, because it measures a bank's capacity to cover its belongings through equity, reflecting the level of financial security and the capability to resist potential losses. Therefore, assessing this ratio gives a essential indicator of the performance of capital management in banks and their preparedness to address unexpected monetary demanding situations.

Equation used:

Capital adequacy = Equity / Total assets

Percentage change = Ratio in 2023 - Ratio in 2022

**Table 1 Capital adequacy ratio**

Bank	2022	2023	Change (%)
<b>United Investment</b>	0.502	0.434	-0.068
<b>Dijlah &amp; Furat</b>	0.696	0.422	-0.273
<b>Iraqi Investment</b>	0.492	0.464	-0.028
<b>Baghdad</b>	0.242	0.196	-0.045
<b>Sumer</b>	1.000	0.789	-0.211
<b>Development</b>	0.350	0.264	-0.086
<b>Total</b>	<b>55%</b>	<b>43%</b>	<b>-12%</b>

**Source: Prepared by the researcher based on published financial data.**

The capital adequacy table indicates a significant decline in Iraqi banks' ability to cover their assets with equity during 2023 compared to 2022, with the average declining from 55% to 43%. Dijlah and Euphrates Bank recorded the largest decline (-0.273), while Sumer Bank maintained the highest adequacy despite its decline. This overall decline

demonstrates weak capital management amid escalating environmental and economic risks, reflecting the urgent need to strengthen capital and raise financial efficiency to avoid exposure to potential financial crises and achieve better banking sustainability in the future.

## Second: Financial Risks

In the modern business environment, banks face increasing challenges in the form of financial risks that directly impact their stability and financial performance. These risks include multiple factors such as credit risk, liquidity, and interest rate fluctuations, which represent the most significant challenges facing capital management. Therefore, this research relies on an analysis of a set of key financial risk indicators: the credit risk index, which measures asset quality and the volume of non-performing loans; the liquidity risk index, which reflects the bank's ability to meet cash obligations; and the interest rate risk index, which reflects the bank's exposure to interest rate fluctuations and their impact on the bank's profitability and financial stability. These indicators aim to provide a comprehensive view that enables assessing the effectiveness of capital management in light of the surrounding financial risks.

### 1- Credit Risk Index

This index is one of the most widely used indicators for determining credit-related risks. The higher the index value, the higher the volume of loans granted and the greater the likelihood of borrowers defaulting. Equation used:

Credit risk index = Provision for doubtful debts / Total loans

Rate change = Ratio in 2023 – Ratio in 2022

**Table 2 Credit risk index**

Bank	2022	2023	Change (%)
United Investment	0.153	0.225	+0.072
Dijlah & Furat	0.745	0.749	+0.004
Iraqi Investment	0.022	0.023	+0.001
Baghdad	0.164	0.218	+0.054
Sumer	0.026	0.038	+0.011
Development	0.009	0.020	+0.011
<b>Total</b>	<b>19%</b>	<b>21%</b>	<b>+3%</b>

**Source: Prepared by the researcher based on published financial data.**

Table (2) of the Credit Risk Index indicates a significant increase in the ratio of the provision for doubtful debts to total loans between 2022 and 2023 in a sample of Iraqi banks. The overall average rose from 19% to 21%, reflecting a rise in the level of credit risk. United Investment Bank was the most affected, recording the largest increase in the index of 0.072, indicating a deterioration in its asset quality and an increased likelihood of customer default. In contrast, Iraqi Investment Bank maintained relative stability, recording a very slight increase of 0.001. Baghdad and Sumer Banks also witnessed moderate increases, indicating a worsening of their credit risks. The index's overall rise illustrates the continued difficulties banks face in controlling credit risk and the necessity of tightening regulations and preventative measures to lower default rates and enhance asset quality.

### 2- Liquidity Risk Index

Represents banks' ability to cover cash outflows and emergency financing.

Equation used:

Liquidity Index = Cash / Total Assets

Rate of change = Ratio in 2023 – Ratio in 2022

**Table 3 Liquidity Risk Index**

Bank	2022	2023	Change (%)
United Investment	0.018	0.040	+0.022
Dijlah & Furat	0.169	0.175	+0.006
Iraqi Investment	0.531	0.675	+0.144
Baghdad	0.610	0.729	+0.119
Sumer	0.679	0.752	+0.072
Development	0.413	0.520	+0.107





<b>Total</b>	<b>40%</b>	<b>48%</b>	<b>+8%</b>
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Source: Prepared by the researcher based on published financial data.

Table (3) of the Liquidity Risk Index reflects a significant improvement in Iraqi banks' ability to cover cash obligations during 2022 and 2023. The overall average of the index increased from 40% to 48%, indicating improved liquidity and enhanced banks' readiness to address cash outflows and emergency financing. The Iraqi Investment Bank stands out as the most improved, recording a significant increase of 0.144, followed by Baghdad and Development Banks, which also achieved significant increases of 0.119 and 0.107, respectively. United Investment Bank witnessed a relatively smaller but significant improvement (+0.022), while Dijlah and Euphrates Bank achieved the lowest increase (+0.006). These results indicate banks' efforts to enhance liquidity and improve their financial position following the impact of the COVID-19 pandemic, enhancing their ability to meet obligations and reducing potential liquidity risks.

### 3- Interest Rate Risk Index

This index measures banks' exposure to interest rate fluctuations by comparing interest-sensitive assets and liabilities. The formula used is:

Interest Rate Index = Interest-sensitive assets / Interest-sensitive liabilities

Percentage change = 2023 rate – 2022 rate

**Table 4 Interest rate index**

Bank	2022	2023	Change
<b>United Investment</b>	26.346	28.804	+2.458
<b>Dijlah &amp; Furat</b>	2.445	2.492	+0.047
<b>Iraqi Investment</b>	0.642	0.472	–0.170
<b>Baghdad</b>	0.225	0.179	–0.046
<b>Sumer</b>	1.525	1.017	–0.508
<b>Development</b>	1.509	1.218	–0.291
<b>Total</b>	<b>545%</b>	<b>570%</b>	<b>+25%</b>

Source: Prepared by the researcher based on published financial data.

Table (4) reflects the interest rate index (IRI) of Iraqi banks, measuring the ratio of interest-sensitive assets to interest-sensitive liabilities during 2022 and 2023. The index measures the ratio of interest-sensitive assets to interest-sensitive liabilities. United Investment Bank saw the largest increase in this index, rising by 2,458 points, indicating increased exposure to interest rate risk. On the other hand, the index decreased for Iraqi Investment Bank, Baghdad Bank, Sumer Bank, and Development Bank. This could be a sign of better interest rate risk management or less exposure to these swings. Overall, the overall average increased from 545% to 570%, a 25% increase, reflecting a general increase in banks' sensitivity to interest rate changes. These results underscore the need to develop effective strategies for managing interest rate risk to protect profitability and ensure financial stability in a volatile economic environment.

### Third : Analysis of Research Hypotheses

There is a correlation and influence between capital management and financial risks in the banks in the research sample. Below is a table summarizing the results of a simple regression between "Capital Management (CA)" as an independent variable and "Financial Risk (RF)" as a dependent variable:

**Table (5):**

Table 5 Hypothesis Analysis

Independe nt Variable	Correlatio n Coefficient t (R)	Coefficient of Determinati on (R <sup>2</sup> )	Calculate d F	Significanc e (F)	Regressio n Coefficient t (B)	Calculate d t (CA)	Significanc e (t)
<b>Working Capital Managemen t</b>	0.412	0.630	15.135	0.986	1.136	15.018	0.006

Source: Prepared by the researcher based on SPSS V.26



A statistically significant positive correlation between capital management ("CA") and financial risk ("RF") in the banks that were part of the study is demonstrated by simple regression analysis in Table (5). The correlation coefficient was  $R=0.412$ ,  $R^2=0.630$ , indicating a moderate upward correlation, while the coefficient of determination  $R^2=0.630$  showed that 63% of the variance in financial risk can be explained by changes in capital management alone. The F test for the model as a whole demonstrated its explanatory power, with a calculated value of 15.135 at  $p=0.006$ , while the regression coefficient  $B=1.136$ , with a calculated value of  $t=15.018$ ,  $t=15.018$  (significance  $p=0.006$ ,  $p=0.006$ ), confirmed that every one-unit increase in the capital adequacy index is accompanied by an average increase of 1.136 units in the financial risk index. Based on these results, it can be confidently stated that capital management has a positive and significant impact on the level of financial risk in the banks in the research sample, supporting the hypothesis that capital management has a significant impact on financial risk.

## **SECTION FOUR : CONCLUSIONS AND RECOMMENDATIONS**

### **Conclusions:**

1. It was found that there is a general weakness in capital management among the Iraqi banks in the research sample, especially in light of the decline in the capital adequacy ratio during 2023 compared to 2022. This illustrates how these banks are more vulnerable to financial risks and are not adequately equipped to withstand shocks.
2. Credit risk indicators showed a clear increase, indicating a deterioration in asset quality and an increase in non-performing loans, which poses a real threat to the stability of these banks.
3. Most banks achieved an improvement in their liquidity indicators during 2023, indicating an increase in their ability to meet monetary obligations and an improvement in their financial position to face emergencies.
4. Banks varied in their level of exposure to interest rate fluctuations. Some banks demonstrated improvement in managing this type of risk, while others experienced a decline, reflecting the absence of a unified policy for managing interest rate risk.
5. The results of the regression analysis indicate a statistically significant relationship and influence between capital management and financial risks, reflecting the close interaction of these elements in the Iraqi banking environment.
6. Relying on strong capital and managing it effectively is a key element in enhancing the competitiveness and financial stability of banks, especially in an unstable economic environment.

### **Recommendations:**

1. The need for Iraqi banks to review their capital management policies, with a focus on enhancing capital adequacy to address any future financial crises.
2. Tighten credit risk oversight by developing creditworthiness analysis tools and enhancing early warning systems for non-performing loans.
3. Support liquidity management strategies by strengthening cash reserves and improving asset and liability management practices to effectively address short-term liabilities.
4. Adopt more sophisticated mechanisms for managing interest rate risk, especially in light of market volatility and changing monetary policies, to ensure profit margins are protected and reduce sensitivity to sudden shifts.
5. The importance of enhancing coordination between the financial department and senior management in banks to ensure informed strategic decisions regarding capital structure and associated risks.
6. Encourage regulatory authorities and the Central Bank to implement capital adequacy standards in accordance with the Basel III framework, taking into account the specificities of the Iraqi economic environment.

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