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An Integrated Governance-Risk Framework: Examining the Influence of Corporate Governance and Credit Risk Management on the Financial Performance and Sustainability of Rural Banks in the Philippines

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Abstract

The sustainability and resilience of rural banks have become increasingly important amid rapid digital transformation, evolving regulatory requirements, and heightened risk exposures. This study examined the combined influence of corporate governance and credit risk management practices on the financial performance of rural banks in the Philippines using an Integrated Governance-Risk Framework. A quantitative descriptive-correlational research design was employed involving 54 respondents from 18 rural banks in Central Luzon. Primary data were collected through structured questionnaires, while secondary data were obtained from the Bangko Sentral ng Pilipinas (BSP) Data Center and published financial statements . Descriptive statistics, Pearson correlation, and multiple regression analyses were used to examine the relationships among the variables. The findings revealed that rural banks exhibited high levels of corporate governance and credit risk management implementation. Corporate governance practices significantly influenced financial performance, demonstrating that stronger governance contributes to improved profitability and organizational effectiveness. In contrast, credit risk management practices showed no significant direct effect on financial performance, although they remained essential in maintaining financial stability, asset quality, and regulatory compliance. The study concludes that integrating sound corporate governance with effective credit risk management provides a comprehensive framework for enhancing the financial performance, sustainability, and long-term resilience of rural banks in the Philippines.

Keywords: *corporate governance, credit risk management, financial performance, rural banks, Philippines.*

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1. Introduction

The Philippine rural banking sector continues to play a vital role in promoting financial inclusion, agricultural development, and economic growth, particularly in underserved communities. However, rural banks operate in an increasingly complex environment characterized by digital transformation, evolving regulatory requirements, rising credit risks, economic uncertainties, and growing stakeholder expectations. Recent regulatory reforms by the Bangko Sentral ng Pilipinas (BSP) have strengthened governance standards, risk management frameworks, and capital adequacy requirements to enhance the resilience of financial institutions. The implementation of Basel-based risk management principles, digital banking initiatives, cybersecurity requirements, environmental and social governance (ESG) considerations, and strengthened board oversight responsibilities has heightened the need for robust corporate governance and effective credit risk management systems.

Corporate governance serves as the foundation of organizational accountability, transparency, fairness, and strategic oversight, while credit risk management ensures prudent lending practices and portfolio quality. Although both concepts have been extensively studied independently, limited empirical evidence exists regarding their combined influence on the financial performance and sustainability of Philippine rural banks.

This study therefore proposes an integrated governance-risk framework that examines how corporate governance practices and credit risk management mechanisms jointly contribute to financial performance and organizational sustainability among rural banks in the Philippines.

Statement of the problem

This study aims to examine the combined effects of corporate governance and credit risk management practices on the financial performance and sustainability of rural banks in the Philippines.

Specifically, it seeks to answer the following questions:

Corporate Governance

1. How may corporate governance practices of rural banks be described in terms of:
    - 1.1 Accountability;
    - 1.2 Transparency;
    - 1.3 Fairness;
    - 1.4 Board Independence;
    - 1.5 Board Effectiveness and Commitment;
    - 1.6 Board Size and Structure; and
    - 1.7 Directors' Education and Experience?

Credit Risk Management

2. How may credit risk management practices be described in terms of:
    - 2.1 Credit Risk Environment;
    - 2.2 Credit Granting Process;
    - 2.3 Credit Administration;
    - 2.4 Credit Risk Measurement and Monitoring; and
    - 2.5 Credit Risk Control Process?

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Financial Performance

3.What is the level of financial performance of rural banks in terms of:
- 3.1 Return on Assets (ROA);
- 3.2 Return on Equity (ROE);
- 3.3 Capital Adequacy Ratio (CAR); and
- 3.4 Non-Performing Loan Ratio (NPL)?

Relationship and Impact
1. Is there a significant relationship between corporate governance practices and financial performance?
2. Is there a significant relationship between credit risk management practices and financial performance?
3. To what extent do corporate governance and credit risk management practices jointly influence financial performance?
4. Which governance and risk management dimensions significantly predict financial performance?
5. Can an integrated governance-risk framework be developed to enhance the sustainability and resilience of rural banks?

Significance of the study

Rural Banks
The findings will provide empirical evidence regarding the governance and risk management practices that contribute to improved profitability, sustainability, and institutional resilience.
Board of Directors
The study will assist directors in strengthening oversight responsibilities, strategic decision-making, accountability, and risk governance.
BSP and Financial Regulators
The findings may serve as a basis for enhancing supervisory frameworks and policy interventions that promote sound governance and prudent risk management.
Investors and Depositors
The study will provide insights into organizational practices that promote stability, financial soundness, and long-term value creation.
Compliance Officers, Internal Auditors, and Risk Officers
The results may guide the enhancement of governance structures, internal controls, and risk management systems.
Academic Institutions and Researchers
The study will contribute to the growing body of knowledge on governance, banking, and risk management and may serve as a reference for future studies.
Rural Banking Industry
The proposed framework may support industry-wide efforts to strengthen financial stability, competitiveness, and sustainability.

2. Methodology

Research Design

This study employed a quantitative descriptive-correlational research design to examine the combined influence of corporate governance and credit risk management practices on the financial performance of rural banks in the Philippines. A quantitative approach was selected because it enables the collection of measurable data and the use of statistical techniques to determine the relationships among the variables.

The descriptive component was used to determine the extent to which corporate governance and credit risk management practices are implemented by rural banks. Meanwhile, the correlational component examined whether these practices are significantly associated with financial performance and identified their predictive influence. The study was primarily cross-sectional because the survey data on governance and credit risk management practices were collected from respondents at a single point in time. However, to provide a more comprehensive assessment of financial performance, the study incorporated a longitudinal element by analyzing secondary financial data from 2020 to 2024. Using five years of financial records helped minimize the effects of short-term economic fluctuations and offered a more reliable picture of the banks' financial condition. While this approach strengthens the analysis, the study remains predominantly cross-sectional because the governance and risk management practices were measured only once rather than repeatedly over the five-year period.

Research Locale

The study was conducted among selected rural banks in Central Luzon, specifically member institutions of the Confederation of Central Luzon Rural Bankers and the Pampanga Federation of Rural Banks**.** Central Luzon was selected because it has a well-established network of rural banks that play a significant role in providing financial services to agricultural communities, microenterprises, and small businesses. These institutions operate under the regulatory supervision of the Bangko Sentral ng Pilipinas (BSP), making them an appropriate setting for examining corporate governance, credit risk management, and financial performance.

Sampling Technique

The study employed purposive sampling to select both the participating rural banks and the respondents. This sampling technique was appropriate because the study required information from individuals who possess direct knowledge and experience in governance, risk management, and banking operations. Accordingly, the respondents included members of the Board of Directors, Chief Compliance Officers, Internal Auditors, Risk Officers, Managers, and Loan Officers, whose responsibilities allow them to provide informed and reliable responses.

Despite its advantages, purposive sampling has certain limitations. Because the participants were selected based on specific criteria rather than through random selection, the findings cannot be generalized to all rural banks in the Philippines with statistical confidence. In addition, there is a possibility of selection bias, as the sample may not fully represent the diversity of rural banks nationwide. Nevertheless, these limitations were minimized by including respondents from multiple rural banks across Central Luzon and selecting individuals with extensive knowledge and decision-making

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responsibilities related to governance and credit risk management. This approach enhanced the credibility and practical relevance of the study while ensuring that the data collected were appropriate for addressing the research objectives.

Respondents of the Study

The respondents consisted of key personnel directly involved in governance, compliance, risk management, and lending operations of rural banks. These included:

Position	Role in the Study
Members of the Board of Directors	Oversight and governance functions
Chief Compliance Officers	Regulatory compliance and governance implementation
Internal Auditors	Internal control and risk assurance
Bank Managers	Strategic and operational management
Loan/Credit Officers	Credit evaluation and loan administration

A purposive sampling technique was utilized to ensure that respondents possessed sufficient knowledge and experience regarding governance and credit risk management practices. The study covered eighteen (18) rural banks from Central Luzon. A total of fifty-four (54) respondents participated in the survey, consisting primarily of Loan/Credit Officers, Internal Auditors/Compliance Officers, Managers, and Members of the Board of Directors. Most respondents possessed between 10 to 15 years of banking experience, indicating adequate expertise in governance and risk management functions.

Sources of Data

The study utilized both primary and secondary data.

Primary Data

Primary data were obtained through a structured survey questionnaire designed to assess:

Corporate Governance Practices
- Accountability
- Transparency
- Fairness
- Board Independence
- Board Effectiveness and Commitment
- Board Size and Structure
- Directors' Education and Experience

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Credit Risk Management Practices

- Credit Risk Environment
- Credit Granting Process
- Credit Administration
- Credit Risk Measurement and Monitoring
- Credit Risk Control Process

Secondary Data

Secondary data were obtained from:

- Published Financial Statements of Rural Banks
- Bangko Sentral ng Pilipinas (BSP) Data Center
- Annual Reports
- Corporate Governance Reports

Financial performance was measured using:

- Return on Assets (ROA)
- Return on Equity (ROE)
- Capital Adequacy Ratio (CAR)
- Non-Performing Loan Ratio (NPL)
- Financial statements covering the period 2020–2024 were analyzed.

Research Instrument

A structured questionnaire adapted from established banking governance and credit risk management frameworks was utilized. The instrument consisted of three sections:

1. Respondents' Profile
2. Corporate Governance Practices
3. Credit Risk Management Practices

Responses were measured using a five-point Likert Scale:

Scale	Verbal Interpretation
5	Always
4	Often
3	Sometimes
2	Rarely
1	Never

Statistical Treatment of Data

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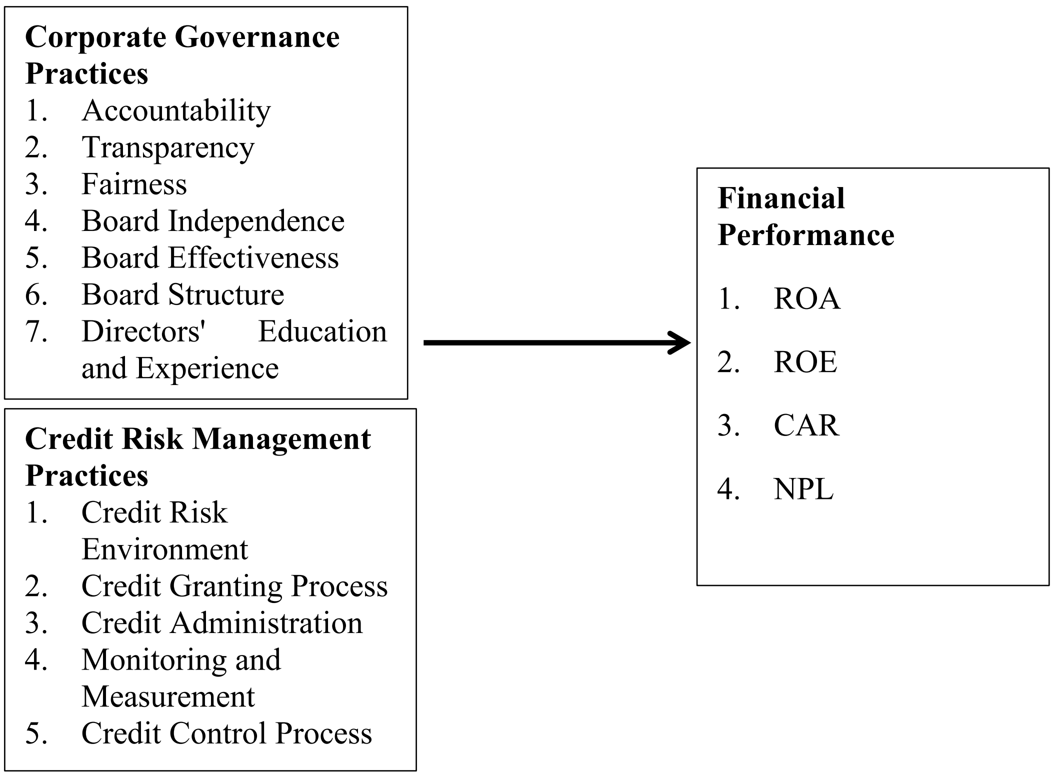
The following statistical tools were employed:

Research Objective	Statistical Tool
Describe governance and risk management practices	Frequency, Percentage, Mean, Standard Deviation
Determine financial performance indicators	Descriptive Statistics
Examine relationships among variables	Pearson Product-Moment Correlation
Determine the effect of governance and risk management on financial performance	Multiple Linear Regression Analysis
Test significance of predictors	F-test and t-test

Conceptual Framework

Independent Variables *Dependent Variables*



This methodology provides a robust framework for examining how governance and risk management practices jointly influence the financial performance and sustainability of rural banks in the Philippines.

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3. Results and Discussion

Corporate Governance Practices

Table 1. Summary of Corporate Governance Practices

Dimension	Result
Accountability	Highly Practiced
Transparency	Highly Practiced
Fairness	Highly Practiced
Board Independence	Moderately High
Board Effectiveness and Commitment	Moderate Improvement Needed
Board Size and Structure	Highly Practiced
Directors' Education and Experience	Very Highly Practiced

The findings indicate that the participating rural banks generally maintain strong corporate governance practices. Accountability, transparency, fairness, and board size and structure were rated as highly practiced, while directors' education and experience received the highest assessment, reflecting the banks' commitment to appointing competent and qualified board members. However, board independence was rated only moderately high, and board effectiveness and commitment were identified as areas requiring further improvement. These findings suggest that although governance structures are well established, strengthening board independence and enhancing board performance could further improve strategic oversight and decision-making. This observation supports the studies of Shleifer and Vishny (1997) and Jensen and Meckling (1976), which emphasize that effective corporate governance minimizes agency conflicts, strengthens accountability, and enhances organizational performance. The results also reinforce the BSP's governance framework, which recognizes an effective and independent board as fundamental to sound banking operations.

Table 2. Summary of Credit Risk Management Practices

Dimension	Composite Assessment
Credit Risk Environment	Always Implemented
Sound Credit Granting Process	Always Implemented
Credit Administration	Always Implemented
Risk Measurement and Monitoring	Frequently Implemented
Credit Risk Control Process	Always Implemented

The results show that rural banks consistently implement sound credit risk management practices. The credit risk environment, credit granting process, credit administration, and credit risk control process were all assessed as always implemented, while credit risk measurement and monitoring was frequently implemented. Overall, the findings indicate strong compliance with BSP guidelines and the presence of structured lending policies and risk control mechanisms. These findings are consistent with the principles of the Basel Committee on Banking Supervision, which emphasizes that effective credit risk management is essential for preserving asset quality and ensuring financial stability. They also support the findings of Bhattarai (2016) and Li and Zou (2014), who reported that well-defined credit policies and continuous monitoring contribute to prudent lending decisions and effective risk control.

Table 3. Impact of Corporate Governance on Financial Performance

Financial Indicator	Result
ROA	Significant Positive Relationship
ROE	Significant Positive Relationship

The analysis revealed that corporate governance has a significant positive influence on the financial performance of rural banks, particularly in terms of Return on Assets (ROA) and Return on Equity (ROE). Rural banks with stronger governance practices tend to achieve higher profitability and generate better returns for shareholders. This finding supports previous studies by Aebi, Sabato, and Schmid (2012), Zagorchev and Gao (2015), and Fernandes et al. (2017), which concluded that effective governance strengthens strategic decision-making, improves oversight, and enhances organizational performance. Strong governance enables boards to provide clear direction, monitor management effectively, and promote accountability, thereby creating conditions that support sustainable financial performance.

Table 4. Impact of Credit Risk Management on Financial Performance

Financial Indicator	Result
ROA	No Significant Effect
ROE	No Significant Effect
CAR	No Significant Effect

Although credit risk management practices were found to be highly implemented, they did not exhibit a statistically significant direct effect on the financial performance indicators included in this study. This finding indicates that while rural banks maintain sound credit risk management systems, these practices alone do not necessarily result in immediate improvements in profitability. The finding contrasts with those of Alshatti (2015), Boahene et al. (2012), and Li and Zou (2014), who reported that effective credit risk management enhances profitability by reducing credit losses and improving loan portfolio quality. However, the present results are consistent with Battaglia and Gallo (2015) and Aebi et al. (2012), who argued that risk management primarily serves as a protective mechanism rather than a direct source of financial returns. Several factors may explain this outcome. First, rural banks generally operate under standardized BSP regulations that require minimum credit risk management practices. Because most participating banks demonstrated similarly high levels of implementation, there was limited variation to explain differences in financial performance. Second, profitability is

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influenced by numerous factors beyond credit risk management, including economic conditions, operational efficiency, market competition, interest rate movements, and management decisions. Furthermore, the financial data covering 2020–2024 coincided with the COVID-19 pandemic and the subsequent economic recovery, during which borrower repayment capacity and lending activities were significantly affected. These external conditions may have reduced the direct impact of credit risk management on profitability. Rather than directly increasing profits, effective credit risk management contributes to financial stability, asset quality, regulatory compliance, and long-term sustainability. Its primary value lies in preventing loan losses and maintaining the soundness of the bank's loan portfolio, benefits that may not be immediately reflected in profitability measures such as ROA and ROE.

Table 5. Integrated Governance-Risk Framework Results

Variable	**Influence on Financial Performance**
Corporate Governance	Strong Direct Influence
Credit Risk Management	Moderate Indirect Influence
Governance + Risk Management	Strong Combined Influence on Sustainability

The findings demonstrate that corporate governance and credit risk management perform complementary roles in promoting the sustainability of rural banks. Corporate governance emerged as the primary strategic driver of financial performance by strengthening leadership, accountability, and decision-making. In contrast, credit risk management functioned as a stabilizing mechanism that safeguards institutional assets, preserves loan portfolio quality, and minimizes potential losses.

Taken together, the results support the proposed Integrated Governance-Risk Framework, which suggests that sustainable financial performance is achieved not through governance or risk management alone, but through their combined application. Strong governance provides the strategic direction necessary for organizational success, while effective risk management protects the institution from financial vulnerabilities. This integrated approach enables rural banks to enhance profitability while maintaining resilience, regulatory compliance, and long-term sustainability in an increasingly complex banking environment.

4. Conclusion

This study highlights the important role of corporate governance in enhancing the financial performance of rural banks in the Philippines. The findings show that banks with stronger governance practices are more likely to achieve better financial outcomes, emphasizing the value of effective board leadership, accountability, transparency, and sound decision-making. These results reinforce the idea that good governance is not merely a regulatory requirement but a strategic asset that contributes to organizational success.

Although credit risk management did not show a significant direct influence on financial performance, its consistent implementation across the participating rural banks underscores its importance in protecting institutional stability. Rather than directly improving profitability, effective credit risk management helps preserve asset quality, reduce potential losses, and ensure compliance with regulatory standards. As such, it remains an essential component of a sound and resilient banking system.

Overall, the findings suggest that sustainable performance is best achieved when strong corporate governance is complemented by effective credit risk management. The proposed Integrated Governance-Risk Framework provides a practical guide for rural banks to strengthen governance, enhance resilience, and sustain long-term growth amid an increasingly complex and competitive banking environment.

Recommendations

Based on the findings of the study, the following recommendations are proposed:

Rural banks should continue strengthening board effectiveness and independence by investing in the continuous development of directors and enhancing board oversight. A more competent and independent board can make better strategic decisions that contribute to improved financial performance. Banks should adopt a more integrated approach to governance and risk management. Embedding enterprise risk management into strategic planning and board decision-making will enable banks to respond more effectively to emerging financial, operational, and digital risks.

While credit risk management did not directly influence profitability, banks should maintain and continuously improve their credit monitoring and loan portfolio management practices. Sustaining high credit quality and minimizing non-performing loans remain essential to long-term financial stability.

Future research may expand the scope of this study by including rural banks from other regions of the Philippines, using larger samples and longitudinal or panel data analyses. Examining emerging issues such as digital governance, environmental, social, and governance (ESG) practices, and cybersecurity may also provide deeper insights into the factors influencing the long-term performance and sustainability of rural banks.

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