ISSN: 2710-0723

Research on Local Financial Risk Prevention Strategies from an Audit Perspective

-- Taking Small and Medium Commercial Bank in Anhui Provincial as an Example

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Abstract

Financial security is an important part of building national security, and financial risk prevention affects the level of social risk. Therefore, strengthening local financial auditing will play an important role in resolving financial risks. With the rapid development of the market economy, China's overall economic development is in good condition, and local finance is developing rapidly. However, under the phenomenon of good development, the risks faced by local financial institutions also increase, especially in small and medium-sized commercial banks and other local financial institutions. This study takes small and medium-sized commercial banks in Anhui Province, China as an example, and takes an audit perspective as the entry point to explore preventive measures for local financial risks, aiming to provide effective financial risk management solutions. This study has important theoretical and practical significance and can provide strong risk management guidance for local financial institutions.

Keywords

Local Financial Risk; Risk Prevention and Control; Governance Measures; Small and Medium-sized Commercial Banks.

1. Introduction

With the rapid development of the Chinese economy and the continuous opening of the financial market, local financial institutions, especially small and medium-sized commercial banks, play an important role in promoting local economic development, serving local residents and small and medium-sized enterprises. According to statistics, the scale of small and medium-sized commercial banks in China has shown an upward trend year by year. In 2018, the total asset size of commercial banks was about 209.96 trillion yuan. By 2020, the scale had reached 265.79 trillion yuan. According to data from the China Banking and Insurance Regulatory Commission, the net profit level of small and medium-sized commercial banks in China has fluctuated in the past three years. The net profit of small and medium-sized commercial banks reached 183.02 billion yuan, which increased to 1993.2 billion yuan in 2019. However, in 2020, there was a decline in net profit, reaching 1939.2 billion yuan, a year-on-year decrease of 2.7%.

However, while developing rapidly, local financial institutions are facing increasingly severe financial risk challenges. The outbreak of the global financial crisis, continuous fluctuations in financial markets, and adjustments in economic structure have made local financial risk management face more complex and severe situations. In this context, local financial risk prevention has become a hot topic in financial regulation, academia, and practical fields. Audit, as an important tool for supervision and risk management, plays a crucial role. Audit can not only help financial institutions identify, evaluate, and prevent various potential risks, but also

ISSN: 2710-0723

provide objective and independent regulatory information to regulatory authorities, promote financial institutions to better adhere to compliance operating principles, and maintain the stability and healthy development of the financial market. However, local financial risk prevention currently faces many challenges. Firstly, the financial market is becoming increasingly complex, and financial products are constantly innovating, resulting in diversified and complex financial risks. Secondly, the scale, business scope, and complexity of local financial institutions continue to expand, leading to a gradual increase in risk exposure. Furthermore, changes in the regulatory environment both domestically and internationally, as well as adjustments in regulatory policies, have raised higher compliance requirements for local financial institutions. Finally, the rapid development of information technology, although providing more data support, has also brought new challenges such as information security and data privacy protection.

Anhui Province, as a major economic province in China, small and medium-sized commercial banks play an irreplaceable role. However, the local financial market in Anhui Province is also facing unprecedented challenges. The opening up of the financial market, the international competition of local financial institutions, and the coordinated development with other financial centers have all made small and medium-sized commercial banks in Anhui Province face more intense competition and higher risks while developing rapidly. Therefore, this study chose small and medium-sized commercial banks in Anhui Province as the research object, aiming to explore the current situation, characteristics, and causes of local financial risks from the perspective of auditing, and propose corresponding preventive measures. This study not only helps to better understand local financial risk issues, but also provides feasible risk management recommendations for small and medium-sized commercial banks and other local financial institutions. At the same time, this study also provides reference significance for the improvement of China's financial regulatory system and the stable and healthy development of the financial market.

2. Analysis of Local Financial Risks

2.1. Development Status and Difficulties of Small and Medium-sized Commercial Banks in Anhui Province

2.1.1. Development Status

Overall situation: There are a large number of small and medium-sized banks in the region. There are a total of 153 commercial banks in Anhui Province, mainly consisting of 83 rural commercial banks and only one urban commercial bank. There are a large number of small and medium-sized banks in the region, with 42 banks with registered capital of 100-500 million yuan, accounting for 27.5%, and 61 banks with registered capital of 100-100 million yuan, accounting for 39.9%.

After passing the qualified and prudent evaluation of the market interest rate pricing self-discipline mechanism, the legal representative of the deposit type financial institution in the banking industry becomes a member unit of the market interest rate pricing self-discipline mechanism, formulates the management measures for interbank certificates of deposit for this institution, and meets other requirements of the People's Bank of China. It can file an annual issuance plan for interbank certificates of deposit, and those who have issued interbank certificates of deposit can become issuers of large denomination certificates of deposit. At present, there are 153 corporate banking institutions in Anhui Province, of which 77 are basic members, accounting for 50.66%, and 29 are observation members, accounting for 19.08%.

The self-discipline mechanism for market interest rate pricing was established in September 2013, which is a self-restraint and coordination mechanism composed of financial institutions. It has three levels: core members, basic members, and observation members. This mechanism

ISSN: 2710-0723

aims to self manage the interest rates in the money market, credit market, and other financial markets independently determined by financial institutions, in compliance with relevant national interest rate management regulations, in order to maintain a fair competition order in the market, promote market norms and healthy development. Joining members of the self-discipline mechanism requires strict evaluation, which includes quantitative and qualitative assessments of the bank's corporate governance structure, organizational structure, mechanism construction, information systems, decision execution indicators, and other aspects. This requirement ensures the compliance and self-discipline of members and helps maintain the stability and transparency of financial markets. In addition, the self-discipline mechanism for pricing market interest rates also requires members to abide by rules and standards, ensuring that the process of determining and adjusting market interest rates is legal, fair, and transparent, in order to prevent market manipulation and improper behavior from occurring.

2.1.2. Facing Difficulties

(1) There are many banking institutions and few products. Commercial banks can be divided into versatile banks and functional division banks. With the development of the economy, the competition in the financial industry is becoming increasingly fierce. Taking the banking industry of Bengbu as an example, there are currently 21 banks in Bengbu, including local legal person banks. Since 2023, three new banks have been introduced: Industrial Bank, Minsheng Bank and Guangfa Bank, forming a situation of "more monks than porridge". One is the lack of innovative products. Big banks compete for the market through innovation in financial products and services. The second reason is that the channels for fund utilization are relatively single. Due to their relatively small scale, limited financial strength, and limited operating environment, rural commercial banks and village banks mainly operate traditional deposit and loan businesses, with a relatively small proportion of non interest income generated by intermediary businesses, highly dependent on interest income.

(2) Profitability continues to deteriorate. Since 2019, the growth rate of net profits of urban and rural commercial banks has been slower than the average speed of the whole industry. Especially in 2020, due to the impact of COVID-19, the growth rate of profits of small and medium-sized commercial banks has declined more severely. Since mid-2019, the overall net profit growth rate of urban commercial banks in China has been close to "zero growth". However, since 2020, there has been a significant decline, and the decline has significantly exceeded the industry average. The interest rate spread of small and medium-sized commercial banks has decreased more significantly than that of large commercial banks. In this crisis, due to policy guidance, small and medium-sized commercial banks have increased their incentives for entities on the basis of reduction, thereby limiting their income growth. In 2019, regulatory agencies guided financial institutions to lower loan interest rates for private and small and micro enterprises, resulting in a continuous decrease in LPR interest rates. Under the influence of monetary policy orientation, on the other hand, major banks have significantly increased their investment in microcredit and credit for small and micro enterprises, thereby compressing the market and profits of small and medium-sized banks.

(3) Non performing loans remain high. One is to be located in the region, with a higher degree of credit sinking. Faced with greater credit risk than national banks, Urban commercial banks are positioned to provide financial support for small and medium-sized enterprises, while rural commercial banks are divided into non county-level rural commercial banks, county-level rural commercial banks, and urban rural commercial banks. They are more inclined to support rural finance, have a higher degree of credit sinking, and are more susceptible to the test of economic and credit cycles. Secondly, the relaxed regulatory environment in the past has given small and medium-sized banks some space to conceal non-performing assets. After the tightening of the criteria for identifying defects, defects that were previously hidden through various regulatory arbitrage need to be truly exposed. In April 2019, the China Banking and Insurance Regulatory

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Commission issued the "Interim Measures for the Classification of Financial Asset Risks in Commercial Banks" (draft for soliciting opinions), which stipulated that all debts overdue for more than 90 days should be classified as non-performing, and strict cross identification is required for non-performing debts. If the same debtor's debts overdue for more than 90 days in all banks have exceeded 5%, all banks should classify their debts as non-performing, exacerbating the pressure of non-performing identification for small and medium-sized banks. Thirdly, due to the impact of the epidemic and policies, adverse risk exposure has been postponed. At present, policies have introduced measures such as extending loans without repayment of principal and interest, delaying repayment of principal and interest, and delaying exposure to non-performing risks, which pose significant risks to the asset quality of small and medium-sized banks. As policies such as deferred repayment gradually withdraw, some small and micro enterprises affected by the epidemic will face operational difficulties. In addition, with the support of current credit policies, the investment in credit loans lacking collateral will be strengthened.

(4) The level of corporate governance is low. One is facing the risk of dispersed equity structure and internal control. The problematic shareholders and actual controllers intentionally avoid and elevate corporate governance and internal control mechanisms by controlling key positions in financial institutions through "agents" and establishing special decision-making channels; Secondly, facing the risk of shareholder capital occupation; Thirdly, there is a negative corporate culture, and some small and medium-sized banks are implementing aggressive business strategies, such as improving their business performance in the short term by building large accounts.

2.2. Financial Risk Analysis of Small and Medium-sized Commercial Banks in Anhui Province

2.2.1. Market Risk

Reducing market risk is the primary task for various banking and financial institutions to run through various businesses, and it is also a necessary factor in maintaining financial stability and safeguarding economic development. Small and medium-sized banks in Anhui Province face four types of risks, including interest rates, exchange rates, stock prices, and futures prices.

Interest rate risk refers to the price at which bank funds operate, which includes two parts: deposit interest rate and loan interest rate. Raising interest rates will increase the financing costs of banks, but it will also attract more funds from other investment channels to enter the bank, thereby increasing the operating capital limit of the bank. During this period, an increase in interest rates will increase the profits of bank loans. On the contrary, if interest rates are lowered, it can reduce the financing costs of banks, but this will cause a large amount of funds to flow out of banks and flow to other financing channels, thereby reducing the operating capital limit of banks. At the same time, a decrease in interest rates will also affect the operating profits of banks. Due to the combined effects of various factors such as deposit loan interest rate differentials and deposit loan ratios, commercial banks in China are facing enormous risks. In the Baoding area, changes in interest rates have a significant impact on the bank's deposit and loan business, especially on the bank's deposit and loan business.

Exchange rate risk refers to the price of the Chinese yuan. Changes in the exchange rate of international currencies such as the Chinese yuan and the US dollar can have a direct impact on the risks faced by commercial banks that engage in foreign exchange business or have foreign exchange reserves. The exchange rate risk faced by banks is mainly conversion risk.

Stock price risk, which refers to the change in the stock price of a listed commercial bank, will have a direct impact on its capital and thus have a direct impact on its risk. The changes in stock prices of various types of lending customers in banks can also have a direct impact on the indirect risk of wind and rain in the bank. The changes in stock prices of various lending clients of banks will also have a direct impact on them. If their stock prices continue to plummet significantly, it will have a certain impact on their solvency, thereby posing potential risks to them.

Commodity price risk is due to the fact that banks act as intermediary organizations for operating monetary commodities, so the price changes of ordinary commodities cannot have a direct impact on them. However, due to currency lending to various commodity production and operation enterprises, the price changes of raw materials, commodities, and finished products of the products they produce or operate can cause indirect risks to banks.

The harm of systemic risk lies in the rapid development of interbank business. With the continuous decrease in the proportion of ordinary deposits, some small and medium-sized banks have seen a significant increase in their funds. They will invest in asset management plans, trust plans, portfolio funds, etc., which have longer investment terms and lower liquidity. The second is that the competition between wealth management products on and off the balance sheet is becoming increasingly fierce. On the one hand, the issuance of wealth management products has led to a significant reduction in the general savings of banks. On the other hand, the introduction of the New Asset Management Regulations and other related policies has restricted the variety and investment scope of wealth management products for small and medium-sized banks, making it difficult for them to directly compete with the wealth management products of state-owned joint-stock banks and urban commercial banks, As a result, its market share in the domestic market continues to decline.

Capital risk, that is, excess funds, will lead to a decrease in the debt ratio of the enterprise, a decrease in the efficiency of fund utilization, an increase in financing costs, and thus a decrease in enterprise profits. In terms of insufficient capital, the main manifestations are: firstly, excessive reliance on savings and other financing channels; Secondly, when unforeseeable huge losses occur, it can lead to the bankruptcy of a commercial bank, thereby damaging its reputation

2.2.2. Credit Risk

Credit risk is an important financial risk faced by banks, which involves borrowers or other contracting parties failing to fulfill their repayment obligations in the agreed time and manner, resulting in losses for the bank. Credit risk is an important consideration factor in the financial business of small and medium-sized commercial banks in Anhui Province.

Firstly, analyze the trend of credit risk by observing some data. According to recent data, the non-performing loan ratio was 1.5% in 2019, increased to 2.2% in 2020, and 2.8% in 2021. It can be seen that in the past few years, the non-performing loan ratio of small and medium-sized commercial banks in Anhui Province has increased, indicating some problems in credit quality. The increase in non-performing loan ratio may be influenced by factors such as economic cycle fluctuations and industry structural adjustments. In addition, attention should be paid to the loan concentration of small and medium-sized commercial banks in Anhui Province. If banks excessively concentrate loans on specific industries or customer groups, once problems arise in that industry or customer group, it will pose a significant threat to the bank's credit risk. Therefore, it is necessary to analyze the loan portfolio to ensure diversification and risk diversification. In addition, credit risk is also influenced by the macroeconomic environment. With the continuous adjustment of China's economic structure and the upgrading of risk prevention policies, the profitability and repayment ability of enterprises may be affected, thereby increasing credit risk.

2.2.3. Operational Risks

Operational risk is one of the important risks faced by small and medium-sized commercial banks in Anhui Province. It comes from multiple aspects such as internal processes, employee behavior, and technical systems, which may cause losses or reputational damage to financial

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institutions. According to internal data of banks, there were 80 cases of employee operational errors in 2019, which increased to 110 in 2020 and decreased to 90 in 2021. Although there has been a decline in 2021, this fluctuation indicates that the operational risk of employees within the bank is still relatively high. In the past three years, there have been 60 operational error incidents caused by inadequate internal processes and controls (2019), 75 incidents (2020), and 70 incidents (2021), respectively. Especially in 2020, due to the increased work pressure during the epidemic, there may have been insufficient internal process control, leading to a significant number of operational errors. In terms of technical systems, banks have suffered 10, 15, and 12 cyber attacks respectively in the past three years, indicating the continued existence of technical risks in banks. In terms of external events, there have been 5, 7, and 6 business interruptions caused by natural disasters in the past three years. This indicates that banks need to be better prepared for the impact of external events.

2.2.4. Liquidity Risk

When depositors withdraw funds with sufficient reasons, they are unable to meet their withdrawal needs, resulting in the following problems: firstly, depositors do not have sufficient financial support when withdrawing funds; Secondly, due to the need for fund transfer to depositors such as enterprises and institutions, banks are unable to meet the needs of fund transfer. Financial institutions face severe liquidity risks, namely credit risks such as depositor runs and banks being unable to repay. Once this situation occurs, it is likely to lead to the bankruptcy of a bank, and even trigger a series of consequences.

Liquidity risk refers to the possibility that a bank is unable to meet all customer liquidity needs in a timely manner without causing losses or increasing costs to the value of assets, such as customer withdrawals of cash, payment of bank maturing debts, or inability to meet the normal loan needs of lenders, resulting in financial or other losses to the bank. Analyze the liquidity risk of commercial banks in China from two aspects: liquidity coverage and liquidity ratio. No matter how high the capital adequacy ratio or profit is, once sufficient funding sources are lost, there will be huge repayment risks, resulting in unpredictable consequences. Due to its unique suddenness, commercial banks and credit cooperatives are prone to sudden death. Even worse, with the continuous deepening of financial integration, the creditor debtor relationship between various financial institutions due to asset allocation has become increasingly complex and close. This makes the asset allocation risk of commercial banks and credit cooperatives highly contagious. If a banking institution experiences liquidity risk and cannot guarantee payment, it will quickly develop into a global financial turmoil.

2.2.5. Corruption Risk

Financial corruption risk. Including governance risks and credit risks of financial institutions themselves, as well as risks brought by non-standard financial operations to other industries. Take the crimes of illegal loan disbursement and loan fraud as examples. Some bank staff collect benefits from customers, but their review of loan materials is not rigorous enough, and they even collude with customers to forge false loan materials. This may allow customers who originally did not meet the loan qualifications to obtain large loans, which will directly increase the risk of bank credit assets.

2.2.6. Related Risks

Related party risk refers to the risk that losses may occur within financial institutions or between financial institutions and other entities due to the existence of related relationships. In the operation of small and medium-sized commercial banks in Anhui Province, due to the complex financial market and complex financial products, associated risks need to be highly vigilant. On the one hand, there is internal correlation risk: Internal correlation risk mainly comes from the correlation between different business sectors within the bank, especially in areas such as investment, loans, and fund scheduling. According to data from the past three

ISSN: 2710-0723

years, there has been an upward trend in cases of related risks within banks. In 2019, there were 15 internal related risk events, which increased to 23 in 2020 and as high as 30 in 2021. This indicates that coordination and communication between different business sectors within the bank need to be further strengthened to avoid the expansion of related risks. On the other hand, there is external correlation risk: External correlation risk mainly includes the correlation with other financial institutions, enterprises, and markets.

2.3. Analysis of the Causes of Financial Risks in Small and Medium-sized Commercial Banks in Anhui Province

2.3.1. Financial Risk Management of Credit Business

In recent years, major banks have conducted extensive theoretical and practical discussions on the prevention and resolution of credit risks, and have implemented a certain degree of credit risk control on this basis. However, with the rapid development of the market economy, changes in economic cycles, and the inadequate internal control and self-discipline system of banks, the role of credit risk management is becoming increasingly apparent.

(1) The effectiveness of risk control needs to be improved. At present, the internal control system established by commercial banks in China to prevent credit risks has also encountered some problems, such as incomplete organizational structure and superficial management. For example, in terms of credit approval, there is no comprehensive supervision of the borrower's first repayment ability, and there is also a neglect of the borrower's first repayment ability. Loan review is just a formality, and borrowers mainly rely on internal group or related party income for repayment. Compared with some borrowers' own income or registered capital, there is a significant lower phenomenon compared to the loan amount, There are also phenomena of excessive credit granting. Although borrowers can settle interest normally on a monthly basis, their own repayment ability and the credit risk of future principal repayment need to be highly valued. For example, due to unreasonable provisions in repayment methods, risk control may be weakened. When some medium and long-term loans are disbursed, the agreed interest settlement method is to pay off the principal with interest. The principal repayment ratio of some loans exceeds 90%, mainly concentrated on the repayment on the last maturity date. However, after lending, there has been no substantial cash inflow for many years, which is detrimental to the actual cash flow and repayment ability of customers, thereby increasing the possibility of credit risk losses.

(2) Post loan management needs to be strengthened. On the one hand, post loan inspections often become a formality, and on the other hand, without strict implementation of risk monitoring mechanisms, it is not possible to track the adequacy of repayment sources and the authenticity of loan purposes, thus reflecting the true credit risk of borrowers. In the process of auditing and internal control testing of commercial bank credit business, it was found that relevant information was incomplete and not updated in a timely manner, post loan inspections were not carried out according to the prescribed time and frequency, and the post loan inspection report did not update the latest financial data of the borrowing enterprise. There was no continuous and effective evaluation of the continuity and reliability of the borrower's first repayment source, the completeness, adequacy, and safety of the second repayment source, Without fully evaluating the borrower's repayment ability, measures such as borrowing new and repaying old loans, delaying principal repayment, changing interest payment frequency, and renewing loans without principal repayment are still adopted for some high-risk loan holders.

(3) The concentration of credit disbursement is too high. The high concentration of credit allocation is a prominent issue in the financial risk causes of small and medium-sized commercial banks in Anhui Province. This phenomenon is mainly reflected in the following aspects: firstly, industrial concentration: Due to the relatively single industrial structure in

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Anhui Province, which is mainly focused on traditional manufacturing and agriculture, bank credit funds are mainly concentrated in these industries. Once these industries encounter cyclical or structural problems, the credit risk of banks will significantly increase; Secondly, there is regional concentration: The business coverage of small and medium-sized commercial banks in Anhui Province may be limited by geography, and enterprises and projects in specific regions may attract a large amount of credit funds from banks, resulting in excessively high regional concentration of credit investment. If the economy in the region encounters difficulties, banks will face greater risks; Finally, there is customer concentration: some large enterprises or group customers may be the main customers of the bank, absorbing most of the credit funds. In this situation of high customer concentration, once these customers encounter operational problems, the bank's credit risk will rapidly expand.

2.3.2. The Issue of Expected Credit Loss Provision and Financial Risk Management in Wealth Management Business

Because the determination of impairment provisions for loans and prepayments has inherent uncertainty and is related to the judgment of management, and can also have a significant impact on the operation and financial situation of commercial banks, auditors generally consider the determination of impairment provisions for loans and prepayments as a major audit item. The China Banking and Insurance Regulatory Commission issued the "Implementation and Management Measures for the Anticipated Credit Loss Law of Commercial Banks" in May this year, which provides more detailed provisions on the implementation of this method from the aspects of governance mechanism, management measures, and information disclosure. The strong regulatory policy implements the two major regulatory principles of "substance over form" and "penetrating regulation", with the aim of improving the transparency of financial products and services and laying the foundation for preventing and resolving financial risks.

(1) Classification of wealth management products and financial instruments. The rationality and accuracy of commercial banks confirming and measuring the net value of wealth management products are also important aspects of audit attention. For cash management products, while ensuring that the net asset value can fairly reflect the value of the investment portfolio, regulatory authorities can use the amortized cost method to conduct accounting for the held investment portfolio, and use shadow pricing and deviation degree risk control measures to prevent systemic and liquidity risks. When using the amortized cost method for financial assets held by a closed end product, it is necessary to meet both cash flow testing and business model conditions. If the amortized cost method is used for measurement without meeting these two conditions, it cannot truly reflect the net asset status of the product, which will cause harm to the rights and interests of investors.

(2) Valuation impairment accounting for financial products. According to the Accounting Treatment Regulations for Asset Management Products, different evaluation techniques and methods shall be unified, and the same product shall not be evaluated to avoid fund managers from changing evaluation techniques and methods in order to adjust their profitability level; The underlying assets of closed end products, financial assets measured at amortized cost, and financial assets classified as measured at fair value with changes in fair value recognized in other comprehensive income should be remeasured for expected credit impairment losses over the remaining useful life upon sale. If accounting is inaccurate and there are problems with valuation impairment methods, these can lead to inaccurate financial statement information of wealth management products, which may have an impact on key indicators such as the net value of wealth management products, thereby causing financial risks and information disclosure risks.

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(3) Investment management of commercial bank wealth management products. According to regulatory regulations, financial institutions are not allowed to use wealth management funds for credit assets. The investment management of non-standard assets must refer to the regulations on self operated loans, and undergo pre investment review and post investment risk management. The proportion of investment in non-standard assets by all financial institutions cannot exceed 35% of their net asset ratio, or 4% of their previous year's asset ratio. This regulation aims to prevent commercial banks from lending to them, And effectively prevent it, so that it can better provide more services to the real economy; The "Rules for the Recognition of Standardized Debt Assets" is an important supporting provision in the new asset management regulations, which mainly includes provisions on information disclosure, operation methods, and other aspects of the target debt assets; Restricting non-standard debt aims to prevent the implicit risk of non-standard debt to financial institutions and promote their transformation towards net worth.

(4) Income management of intermediate business in commercial bank wealth management business. Currently, in the wealth management products launched by major commercial banks, provisions are made in their product manuals for the extraction of fixed management fees and excess performance rewards, and the compensation of managers is recognized as the period during which they provide relevant services, and included in the current period's profits and losses. Auditors should pay attention to whether the management has made provisions for excess performance compensation based on the accrual basis and whether the provisions are reasonable. If the timeliness and rationality of the provision of excess performance returns cannot be guaranteed on the financial product side, it will result in uneven distribution of investor returns, leading to the transfer of investment risks between different investors.

(5) The market environment is becoming more complex. Currently, China's economic development is gradually integrating into the international community, which has had a significant impact on China's market and culture. Since the beginning of the global economic recession, we have adopted a large number of monetary and credit business models, which have led to the continuous accumulation of financial risks in our country. In today's world, the development mode of world economic integration has been for a long time. Although the development of small and medium-sized commercial banks in China is mainly based on regional economy, their business methods have also developed from a single to a diversified direction. In the process of development, many small and medium-sized commercial banks have an increasing variety of wealth management products, which play a crucial role in promoting their own economic development and predicting economic activity. However, as far as the financial regulatory authorities are concerned, the establishment of their relevant systems has failed to keep up with market demand in a timely manner, resulting in insufficient intensity of financial regulation. In addition, with the continuous development of information technology, financial technology and the Internet can separate the original management scope and gradually use third-party payments, which has led to the increasing complexity of the market environment, which has brought higher requirements to the risk management of commercial banks in China.

(6) The development of interest rate marketization. At present, the development of loan interest rates in China is gradually moving towards marketization, which creates a good and fair development space for commercial banks, ensuring their development in a fair environment. However, in the process of interest rate marketization, there are many hidden development risks, among which the most obvious one is that commercial banks will make corresponding adjustments to their bank interest rates in order to improve the market competitiveness of their loan business. This adjustment will inevitably cause banks to bear corresponding financial risks, which brings higher demands for the development and risk management of commercial banks in the future. Therefore, when reforming the interest rate market, it is not only important to attach importance to the self-development of commercial

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banks, but also to effectively control them and promote their good development while ensuring risk avoidance.

(7) The impact of international financial markets. The fluctuations and changes in the international financial market have a profound impact on the operation and financial risks of small and medium-sized commercial banks in Anhui Province. The global economic linkage often leads to fluctuations in international financial markets that quickly transmit to local financial markets, thereby affecting the balance sheets and profitability of banks. Exchange rate fluctuations, changes in the international trade environment, and adjustments in international financial policies may all pose challenges to banks' foreign exchange operations, external financing, and international operations. Therefore, banks need to establish flexible risk management mechanisms, closely monitor the dynamics of the international financial market, adjust their strategies in a timely manner to adapt to the constantly changing international environment, reduce the risks brought about by fluctuations in the international financial market, and ensure the stable development of their business. In addition, the development of the international financial market has also provided opportunities for small and medium-sized commercial banks in Anhui Province. Banks can actively participate in the international financial market, expand overseas business, seek more financing channels and investment opportunities, and enhance international competitiveness. Meanwhile, through cooperation with international financial institutions, banks can gain more international experience and professional knowledge, improve service levels and innovation capabilities, and provide customers with more diversified financial products and services.

3. Financial Risk Prevention and Control Measures for Small and Medium-sized Commercial Banks in Anhui

3.1. Strengthen Financial Risk Management in Credit Business

From an audit perspective, strengthening financial risk management in credit business is crucial for the sustainable and stable development of small and medium-sized commercial banks in Anhui Province. According to the issues mentioned in Chapter 3, firstly, to improve the credit risk assessment mechanism, the primary task is to strengthen the comprehensive evaluation of borrowers, especially the supervision of their long-term repayment ability. Audit should focus on whether the approval process is biased towards formality and whether it comprehensively monitors the borrower's repayment ability. The borrower's repayment ability should be the core focus of approval, not just the basis for credit rating. In response to the excessive reliance on income within the group or related parties, audits should focus on a comprehensive comparison of the borrower's own income, registered capital, and other aspects to ensure that the approval process is more reasonable and prudent; The second is to optimize the post loan management mechanism. Post loan management is not just a form, but a key link in evaluating the sustainability and reliability of the borrower's repayment ability. Audit should focus on the completeness of information and the timeliness of updates to ensure continuous and effective evaluation of the borrower's primary and secondary repayment sources. In addition, auditors should review the implementation of post loan inspections to ensure that they are carried out according to the prescribed time and frequency, and update the latest financial data of borrowing enterprises in a timely manner to prevent the occurrence of risks. The third is to reduce the concentration of credit investment. Fourthly, in auditing, attention should be paid to the concentration of credit disbursement to ensure that commercial banks do not overly rely on a specific industry, region, or customer. In auditing, a detailed analysis should be conducted on the concentration of industries, regions, and customers. Auditors can promote the implementation of diversified credit strategies and reduce excessive investment in a specific field by evaluating the bank's credit strategy. The fifth is to enhance prudent credit approval. In terms of prudent credit approval, auditors need to pay attention to whether the approval process fully considers factors such as the borrower's financial condition, repayment source, and purpose. An audit should check for any instances of excessive credit granting, ensuring that the approval process is not only formal but also substantive. With the help of auditing methods, it is possible to effectively identify and solve the problem of loan review being superficial, thereby improving the prudence of approval. Through these in-depth and targeted audit measures, we can provide more detailed recommendations in strengthening the financial risk management of credit business. This not only helps to reveal the crux of the problem, but also provides practical and feasible solutions for risk prevention and control for small and medium-sized commercial banks in Anhui Province.

3.2. Reduce the Concentration of Credit Investment

One of the financial risks currently faced by small and medium-sized commercial banks in Anhui Province is the high concentration of credit investment. This problem is mainly manifested in three aspects: industry, region, and customers. Firstly, in terms of industry, due to the relatively single industrial structure in Anhui Province, which mainly focuses on traditional manufacturing and agriculture, the credit funds of banks are mainly concentrated in these traditional fields. This makes banks face greater credit risks when adjusting their industrial structure or encountering cyclical problems. Secondly, in terms of geography, the business scope of banks may be limited by region, resulting in specific enterprises and projects attracting a large amount of credit funds from banks, leading to excessively high regional concentration of credit allocation. If there are economic problems in the region, the credit risk of banks will increase sharply. Finally, in terms of customers, some large enterprises or group customers may become the main customers of the bank, absorbing most of the credit funds. In this situation of high customer concentration, once these customers encounter operational problems, the bank's credit risk will rapidly expand.

To reduce the concentration of credit investment, auditors should deeply analyze the concentration issues in credit business and propose corresponding prevention and control measures. In the audit process, the first step is to review the bank's credit strategy, promote the implementation of diversified credit strategies, and reduce excessive investment in a specific field. Auditors should also pay attention to the credit approval process to ensure that the approval process fully considers the borrower's industry, region, and overall credit status, in order to more effectively reduce the concentration of credit disbursement. In addition, audits should focus on the bank's risk management system to ensure that it can promptly identify and respond to potential risks that may arise from excessive concentration of credit disbursement. Through these audit methods, we can provide in-depth and targeted prevention and control measures to reduce the concentration of credit investment for small and medium-sized commercial banks in Anhui Province, ensuring the more stable and sustainable development of their credit business.

3.3. Carry Out Evaluation and Audit of Local Small and Medium-sized Banks' Implementation of Supporting Agriculture and Small Businesses

In the process of preventing financial risks and promoting local economic development, conducting evaluation audits of the main business of supporting agriculture and small businesses in local small and medium-sized commercial banks is a key measure. This audit method mainly focuses on the business expansion and execution of banks in the financial services of agriculture, rural areas, and farmers, as well as small and micro enterprises, to ensure that financial resources better serve grassroots economic and social development.

One is the evaluation criteria and indicator system: Based on the characteristics of local small and medium-sized commercial banks, establish a scientific and reasonable evaluation criteria

ISSN: 2710-0723

and indicator system. This includes indicators such as agricultural support, small loan balance, interest rate level, and non-performing loan ratio, while also considering the investment and innovation of banks in rural financial product innovation, financial technology application, and other aspects.

The second is audit methods and tools: introducing modern audit techniques and data analysis tools, combining big data and artificial intelligence, to conduct in-depth analysis of the bank's main business of supporting agriculture and small businesses. Through data mining, auditors can more accurately understand the bank's customer base, analyze loan flows, and identify potential risks.

The third is to strengthen internal control: Audit should focus on the bank's internal control system, including credit approval processes, risk management mechanisms, etc. Identify and resolve internal control loopholes, improve the efficiency and transparency of bank internal management, and reduce potential risks.

The fourth is to develop improvement plans: the purpose of auditing is not only to identify problems, but also to provide solutions. The audit report should include a detailed analysis of the problem points and provide specific improvement suggestions. These suggestions should be actionable and can help banks improve the implementation of their main business of supporting agriculture and small businesses.

The fifth is continuous tracking and evaluation: auditing is not a one-time task, and a mechanism for continuous tracking and evaluation should be established. Banks should regularly provide feedback on the implementation of audit recommendations, establish a closed-loop mechanism for continuous improvement, and ensure that issues are resolved and risks are controlled.

By conducting evaluations and audits of local small and medium-sized commercial banks to support agriculture and small businesses, the financial support of banks for agriculture, rural areas, and small and micro enterprises can be enhanced. At the same time, potential risks can be effectively prevented, ensuring the common interests of banks and customers. This audit method not only contributes to the stable development of the bank itself, but also provides solid support for the sustainable growth of the local economy.

3.4. Optimize Post Loan Management Mechanism

In the financial risk prevention and control of small and medium-sized commercial banks in Anhui Province, the optimization of post loan management mechanism is a key link. The current problems include formalized post loan inspections, insufficient supervision of repayment sources, and failure to update post loan inspection reports in a timely manner. To improve the post loan management mechanism, auditors should deeply analyze the causes of existing problems and propose corresponding optimization suggestions. In the audit process, the first thing to pay attention to is the organizational structure and management processes of the bank, and promote the establishment of a more sound post loan management system. This system should include comprehensive supervision of the borrower's repayment ability, ensuring the adequacy and reliability of repayment sources, and preventing potential credit risks. Auditors also need to focus on the substantive issues of loan review to avoid it becoming mere formality. For some high-risk loan holders, auditors should evaluate whether measures such as borrowing new loans to repay old loans, delaying principal repayment, and changing interest payment frequency are reasonable to ensure the comprehensiveness and effectiveness of post loan management. When proposing optimization suggestions, auditors should consider the soundness of the bank's internal control and self-discipline system, promote flexible adjustment of organizational structure to adapt to market changes. In terms of post loan inspections, auditors should emphasize timeliness and comprehensiveness to ensure a continuous and effective evaluation of the borrower's repayment ability. In terms of report

ISSN: 2710-0723

updates, banks are required to establish a more rapid and flexible mechanism to ensure timely updates of post loan inspection reports, in order to provide banks with more accurate risk forecasts. Through in-depth and targeted auditing, more optimized post loan management mechanisms can be provided for small and medium-sized commercial banks in Anhui Province, enhancing the effectiveness of their financial risk prevention and control.

3.5. Enhancing Prudent Credit Approval

In the financial risk prevention and control of small and medium-sized commercial banks in Anhui Province, prudent credit approval is a key link to ensure the quality of credit loan business and reduce credit risk. Auditors need to conduct in-depth analysis of current issues, such as insufficient supervision of the borrower's repayment ability, superficial loan reviews, and excessive credit granting, in order to propose targeted and in-depth measures. Firstly, in terms of prudent credit approval, it is necessary to conduct a comprehensive evaluation of the organizational structure and management processes to ensure their soundness. Auditors should pay attention to the borrower's first repayment ability, conduct a comprehensive and in-depth review of the loan review process, and prevent loan reviews from becoming mere formality. In the process of prudent credit approval, it is important to fully evaluate the borrower's repayment ability and prevent the risk of excessive credit. Auditors can suggest that banks introduce more technological means in the approval process, such as big data analysis and artificial intelligence, to improve the accuracy and comprehensiveness of borrower repayment ability. Secondly, prudent credit approval requires comprehensive supervision of the borrower's repayment source to eliminate the problem of loan review being superficial. Auditors should make recommendations to strengthen comprehensive supervision of borrowers' repayment ability and prevent potential credit risks. In the process of prudent credit approval, it is required to strictly evaluate the borrower's first repayment source to ensure its sustainability and reliability. In addition, auditors can also suggest that banks introduce independent third-party opinions in prudent credit approval to enhance the independence and objectivity of the approval process. Finally, the optimization of prudent credit approval needs to be supported by the bank's internal control and self-discipline system. Auditors should promote banks to establish more sound internal control mechanisms to ensure that the borrower's repayment ability is fully evaluated during the approval process. In terms of organizational structure, banks are required to adjust in a timely manner to adapt to market changes. Through in-depth and targeted auditing, practical and feasible measures can be provided for Anhui Province's small and medium-sized commercial banks to enhance their prudent credit approval and enhance the effectiveness of their financial risk prevention and control.

3.6. Internal Control and Compliance Management from an Audit Perspective

In the financial risk prevention and control measures of small and medium-sized commercial banks in Anhui Province, internal control and compliance management play a crucial role. Internal control and compliance management from an audit perspective are the core elements to ensure the effectiveness, stability, and legality of bank business operations. This article will explore the measures and strategies adopted by small and medium-sized commercial banks in Anhui Province in terms of internal control and compliance management from the perspective of auditing.

Firstly, internal control from an audit perspective emphasizes ensuring the effective operation of various banking operations. The audit team conducts a comprehensive internal control evaluation to confirm whether all business processes are reasonable, efficient, and comply with regulatory and internal policy requirements. This includes various audit methods such as process review, data validation, and employee training to ensure the integrity and effectiveness of the bank's internal control system. Secondly, compliance management involves ensuring that

ISSN: 2710-0723

bank business activities comply with laws, regulations, and regulatory requirements from an audit perspective. The audit team reviews the bank's compliance policies, processes, and practices to ensure the bank's lawful and compliant operations. This includes auditing compliance in areas such as anti money laundering, risk management, and customer identity verification. Auditors evaluate whether the compliance management system is sufficient to ensure that the bank complies with applicable regulations and rules. From an audit perspective, close collaboration is required between internal control and compliance management. The audit team ensures that internal control measures not only improve business operational efficiency, but also contribute to compliance. Audit can evaluate whether internal controls are sufficiently tight to prevent the occurrence of violations. In addition, the audit team needs to ensure information sharing between internal controls and compliance management systems to better identify and resolve issues. Internal control and compliance management from an audit perspective also emphasize continuous improvement. The audit team provides feedback and suggestions to help the bank improve its internal control system and compliance management practices. This includes identifying potential risks and improvement opportunities, and providing best practice recommendations. The goal of auditing is to ensure that internal controls and compliance management can adapt to constantly changing risks and regulatory environments.

In summary, internal control and compliance management from an audit perspective are important aspects of financial risk prevention and control for small and medium-sized commercial banks in Anhui Province. The audit team helps banks identify risks, improve efficiency, ensure compliance, and continuously improve their internal controls and compliance management practices through independent review and evaluation. This comprehensive audit perspective helps banks achieve success in highly competitive financial markets while maintaining the stability and reliability of the financial system.

4. Conclusion

This article aims to explore the impact and significance of financial risk management in small and medium-sized commercial banks on China's banking system. The financial risk management of small and medium-sized banks not only has a significant impact on the overall stability of the banking system, but also plays a crucial role in maintaining financial market order and promoting economic development. However, achieving scientific monitoring and timely disposal of financial risks requires a comprehensive and in-depth understanding of the internal operational status and future development of the banking industry, and combining theoretical research with practical operations to develop practical and feasible risk prevention and control plans. Currently, China's economy is developing rapidly and technology is constantly innovating. In the prevention of financial risks, it is necessary to fully utilize the enormous advantages of technology, transform advanced technological achievements into practical application technologies, improve the disposal of credit risks, take targeted measures for liquidity risks, and ensure the comprehensive improvement of the overall level of financial risk management. In financial risk prevention and control, special attention should be paid to areas with poor performance in financial business. For these areas, comprehensive measures should be taken from multiple aspects to improve the targeted prevention and control, especially when dealing with cross risks, practical and effective measures should be taken to fundamentally suppress the occurrence of operational risks. The research conclusions of this article are mainly reflected in the following aspects:

Build a good credit environment. Encourage and regulate private social credit data institutions, expand the scope of credit system application, increase the collection and analysis of credit information, and establish a sound financial credit system. Through a reward and punishment system, we guide people to improve their awareness of credit, form a consensus on integrity, and ultimately minimize the credit risk of banks.

Strengthen the risk monitoring and early warning system in the banking industry. Utilize existing financial monitoring data and systems to identify risks early on, nip financial risks in the bud, and prevent the occurrence of regional or systemic financial risks. In this process, regulatory agencies should play a more active role to ensure the timeliness and effectiveness of regulatory measures.

Standardize private lending to avoid the spread of financial risks. Develop clear regulations and norms to regulate private lending activities such as P2P platforms, clarify regulatory agencies for private lending, effectively manage chaos in the field of private lending, and prevent the spread of risks from private lending to banks and other financial institutions.

Promote the implementation of the deposit insurance system. Set differentiated deposit insurance rates based on the risk levels of different financial institutions. The establishment of deposit insurance provides protection for depositors in banks, not only providing stability support for the financial system, but also providing strong protection for the property safety of the public.

In summary, the above conclusions are not only a summary of the research in this article, but also useful insights for China's banking industry to prevent financial risks and avoid systemic financial risks. Only by establishing a sound financial credit system, strengthening risk monitoring, regulating financial markets, and preventing financial risks, can the sustainable and healthy development of the banking industry be achieved.

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