

Risk Management

Risk Management Philosophy

In essence, the Group's risk management philosophy is to uphold a strong risk management culture that will enable us to generate returns that commensurate with our risk appetite and financing capabilities. The business and social landscape is constantly evolving, hence the Group proactively fine-tunes its risk management approaches to meet these changing needs.

Integrated Risk Management Framework

The Group faces various risks inherent to the banking industry. These include:



Reputational Risk is the risk arising from negative perception on the part of customers, counterparties, shareholders, investors, debt-holders, market analysts, other relevant key stakeholders or regulators that can adversely affect a bank's ability to maintain existing, or establish new, business relationships and continued access to sources of funding.

Strategic Risk is the risk of current or prospective impact on the Group's earnings and capital, arising from changes in the environment the Group operates in and from adverse strategic decisions, improper implementation of decisions, or lack of responsiveness to industry, economy or technological changes.

Credit Risk is the risk of financial loss as resulting from the failure of the Group's borrowers or counterparties, to fulfil their contractual obligations to repay their loans or to settle their financial commitments. The Group's credit risk exposures arise primarily from lending, investment and trading activities.

Market Risk is the risk of loss of earnings arising from changes in interest rates, foreign exchange rates, equity prices, commodity prices and in their implied volatilities.

Liquidity Risk refers to the Group's inability to:

- cover financial commitments when due;
- liquidate assets in an orderly manner, due to market disruptions, inadequate market depth and/or wider bid-ask spreads.

Operational Risk is the risk of direct or indirect loss resulting from inadequate or failed internal processes, people and systems, or from external events.

Legal and Regulatory Risks arises from potential breaches of applicable laws and regulatory requirements, unenforceability of contracts, lawsuits, or adverse judgments which may lead to potential losses, disruption in business or otherwise resulting in financial and reputational risks.

Shariah Non-Compliance Risk arises from the risk of failure to comply with Shariah rules and principles, as determined by the relevant Shariah advisory council. Shariah compliance issues in Islamic financing activities, inter-alia, includes prohibition of Riba (interest), Gharar (uncertainty) and Maisir (gambling).

In line with the Group's risk management philosophy, we implemented an Integrated Risk Management Framework (IRMF) to govern our businesses and operations. This enables the Group to deploy a structured and proactive approach to manage the various risks faced.

The following diagram shows the various elements that the Bank employs to manage risk; and in doing so, to uphold our reputation:



To summarise, key elements of the IRMF include:

- Risk Governance and the three Lines of Defence;
- Risk Culture;
- Risk Management Cycle: Risk Identification, Assessment, Control, Monitoring and Reporting;
- Risk Frameworks, Policies, Limits and Procedures;
- Risk Methodologies, Tools, Indicators and Dashboards;
- Stress Testing and Contingency Planning; and
- Risk Communication and Disclosures.

Risk Governance Structure

The Board of Directors is responsible for the overall risk oversight within the Group. In support of the risk management objectives, the Board is assisted by the following committees:

Group Risk Management Committee (GRMC)	To review and approve the Group's risk management frameworks, risk appetite and limits; and to ensure that the necessary infrastructure and resources are in place to manage risk.
Executive Committee (EXCO)	To aid the Board to govern over business issues, in particular to review large credit exposures.
Group Audit Committee (GAC)	To aid in ensuring adequacy and effectiveness of the Group's internal controls.
Shariah Committee	To aid in governing Shariah compliance issues.
Senior Management is responsible for managing and controlling the Group's day-to-day operations. Several risk-related committees have been established:	
Management Committee (MANCO)	To review the Group's financial performance and strategies.
Group Assets and Liabilities Management Committee (GALCO)	To govern: <ul style="list-style-type: none"> • Balance Sheet and Capital Management • Liquidity Risk Management • Interest/Profit Rate Risk Management
Portfolio Review Committees:	To monitor the health of the respective lending or financing portfolios of the respective Line of Business.
<ul style="list-style-type: none"> • Consumer Banking • SME Banking • Wholesale Banking 	
Group Operational Risk Management Committee (GORMC)/Operations Steering Committee	To manage the Group's operational risk profile and operations initiatives.
Shariah Review Committee	To monitor adherence to Shariah requirements.
Product Working Group	To govern the introduction of the Group's new products and Third Party products, e.g. Unit Trusts and Bancaassurance.

During the year, the respective committees meet regularly to perform their duties in monitoring the Group's activities, and to handle issues that arise.

Three Lines of Defence Concept

To strengthen the effectiveness of the risk management function, the Group is functionally segregated into three Lines of Defence, with oversight from the Board and Board-level Committees.



Functional Segregation	Key Responsibilities
1st Line of Defence <ul style="list-style-type: none"> • Customer-facing Units • Business Risk Officers • Support Risk Officers • Unit Risk Officers 	They have the primary responsibility of monitoring to ensure that their activities are conducted in adherence to the Group's approved policies and procedures.
2nd Line of Defence <ul style="list-style-type: none"> • Group Risk Management • Group Compliance • Shariah Review Team 	Responsible for: <ul style="list-style-type: none"> • Formulating and enhancing risk management and compliance frameworks; • Recommending risk management policies, parameters, methodologies and tools; • Reviewing the adequacy of control measures; • Performing independent risk monitoring and compliance reporting.
3rd Line of Defence <ul style="list-style-type: none"> • Internal Audit 	Provides independent assessments of the adequacy and effectiveness of risk policies and internal controls.

Risk Culture

The Group's risk culture relates to the underlying awareness that Management and all employees possess and practice in relation to risk-taking and compliance. The risk culture sets the tone within the Group. Hence, the Group makes an effort to instil in our employees the discipline of exercising prudence and to live up to our core values; to guide them in the conduct of their daily activities and in pursuit of our organisational and business objectives. A strong risk culture provides an essential foundation upon which the Group is able to better manage risks and opportunities in a rapidly changing environment.

Risk Management (cont'd)

Key themes include:

- Our corporate ethics and values: Respect, Integrity, Teamwork and Excellence
- Leadership
- Accountability
- Meritocracy
- Communication

Risk Management Cycle: Risk Identification, Assessment, Control, Monitoring & Reporting



We practice a life-cycle approach towards managing risks. Briefly:

- We start by identifying the various risks inherent to each product or activity.
- We adopt quantitative and qualitative approaches to measure and assess these risks, in terms of quantum, severity of impact and likelihood of occurrence.
- We examine various measures to mitigate/control these risks. We then proceed to select and implement an appropriate set of risk mitigants and control measures.
- The risks and controls are monitored at periodic intervals. Areas of significant risks are monitored on a more frequent basis. Such monitoring enables the identification of adverse trends, allowing corrective measures and realignment of risk strategies when necessary.
- Periodic risk reports/dashboards are provided to the Management and the Board. Key issues and exceptions are escalated to their attention.
- The feedback stemming from the risk cycle is included in our next round of risk assessment, for fine-tuning.

Risk Frameworks, Policies, Limits and Procedures

Risks are not easy to manage on an unstructured basis. Hence, our structured approach is to first develop a risk framework to govern the respective risk elements. We start off this process by formulating Group-wide risk frameworks that are based on regulatory requirements and recommended market practices.

Next, we dive down to the next level and start carving out risk policies that are applicable to the various bank entities, business segments and products. Typically, we engage representatives from both business and control functions when formulating our risk policies. To operationalise the policies, we add risk limits and parameters to the policies. To guide our staff, we add on procedural guidelines and manuals.

We strive for consistency whenever possible. The above process is adopted for the various risk frameworks, policies, limits and procedures.

Risk Methodologies, Tools, Indicators and Dashboards

For Credit Risk Management

The Group employs two main approaches to manage credit risks in lending activities.

For lending to large commercial/corporate organisations, we assess each related group of borrowers. This assessment is premised on the health of their enterprise, as evidenced by their business performance, financial ratios and conduct of account. Fresh/additional/existing loans are vetted based on the business outlook, changes in operating environment; with emphasis on the structuring appropriate credit facilities that commensurate with the borrower's repayment capability, risk mitigants and collateral.

For retail loans and small and medium-sized business loans, we adopt a programme lending approach, developed through distilling traditional lending decisions into a set of risk parameters, e.g. borrower's credit profile, sources of income, debt burden, repayment capability and collateral. These are then carved into credit scorecards/rating templates to derive a preliminary 'accept' or 'decline' credit decision. As our use of these tools are still at a relatively young stage, we overlay this quantitative approach with a qualitative approach that allows credit underwriters to override or reject loans that do not meet the judgmental parameters.

To ensure that our credit scorecards are able to distinguish a good loan from a potential bad loan, the scorecards and models used are periodically back-tested/validated.

To monitor the health of the respective lending segments and products, we use risk dashboards that set out key risk indicators/statistics. Early warning risk triggers are also set and closely monitored.

For Market Risk, Liquidity Risk and Capital Management

We adopt a similar approach, wherein we set portfolio limits and risk indicators/triggers. These are then monitored and reported in our risk dashboards.

For market risk, we set additional triggers to monitor the sensitivity of the portfolio to adverse market movements. Independent valuation of treasury positions and risk exposures are carried out using rates obtained from market sources. In addition, we carry out back-testing to ensure that the Bank can continue to rely on our Value-at-Risk model.

For liquidity risk, we monitor the various liquidity ratios/triggers. These tasks include carrying out simulations to gauge our capacity to handle liquidity shocks and early monitoring of the proposed Basel III liquidity ratios.

For capital management, we monitor the various capital adequacy ratios prescribed under Basel II and transition Basel III ratios. Under Basel II, we perform a periodic Internal Capital Adequacy Assessment Process (ICAAP), to estimate the additional buffer capital that the Group should maintain, above the minimum Basel capital requirement. To make this process more robust, our buffer capital computation adds-on the results from our stress testing exercise. The simulated results are projected onto our business plans for the current financial year and across our capital planning horizon. This is to ensure that the Group is adequately capitalised to support business growth.

For Operational Risk Management

In line with best market practices, the Group employs the following tools for the management of operational risks, which are used in tandem with each other:

Tool	Purpose
Risk and Control Self-Assessment (RCSA)	To identify and assess operational risks as well as to identify the controls and assess their effectiveness.
Control Self-Assessment	To test/validate the effectiveness of the controls as stated in the RCSA.
Key Risk Indicators	To monitor and manage operational risk exposures over time.
Loss Event Data Collection	To collect and report loss incidents involving actual losses and 'near misses'.

The operational risk profiles are then populated into 'heat maps' to visually assist the Management to identify and address areas of concern.

The use of these tools are supplemented by a network of business/support risk officers that are deployed to assist the various business and support functions.

For Legal and Regulatory Risks

Legal risk is managed by in-house legal counsel and where necessary, in consultation with external legal counsels.

Compliance awareness training is also conducted on a regular basis to ensure that staff keep abreast with laws, regulations and other regulatory developments. The training programmes help staff to develop their skills to identify compliance issues as well as cultivate good corporate ethics.

Anti-Money Laundering and Fraud Detection

The Group has implemented systems to analyse trends and behavioural patterns of banking transaction. These tracking and reporting processes enable the Group to detect probable fraudulent and abnormal transactions; and to mitigate potential monetary losses arising from such incidents.

The Group also has in place a Whistleblower Policy which is designed to provide an avenue for staff to report any possible financial improprieties, such as manipulation of financial results, misappropriation of assets, intentional circumvention of internal controls, inappropriate influence on related party transactions by related parties or other improprieties. The Whistleblower Policy is also an avenue for employees to raise concerns in relation to the specific issues that fall outside the scope of other Group policies and procedures.

Stress Testing & Contingency Planning

Periods of economic stability and prosperity tends to lull organisations into a state of complacency. To counter this, the Group carries out stress testing to estimate the potential impact of extreme events on the Group's earnings, balance sheet and capital. These stress tests also aim to gauge our sensitivity/vulnerability to a business sector, product segment or customer segment.

The Group has applied a stress testing framework to identify:

- Potential vulnerable risk areas of the Group's portfolio to stress events. It examines an alternative future that could cause problems to the Group's portfolio. These 'what-if' simulations enable the Group to assess the potential worst case scenarios. We then proceed to make contingency plans to face critical situations.
- Possible events or future changes in financial and economic conditions that could have unfavourable effects on the Group's ability to withstand such changes. In particular, we examine the Group's capital and earnings capacity to absorb potentially significant losses. We can then take steps to manage these risks and safeguard our enterprise.

The stress test parameters are formulated internally, taking into account the economic scenario, plus current and forecasted key indicators. The scenario, parameters and computed stress test results, covering the estimated impact on earnings and capital of the respective entities and Group are analysed and reported to the Stress Test Working Group, GRMC and Board. Where applicable, proactive action is taken to address areas of weakness/vulnerability.

In addition, the Group has also established various Risk Triggers to monitor and detect potential risk events that may critically affect the Group's financial health.

Our contingency plans are not merely limited to desktop exercises. We carry out periodic exercises involving simulations of systems failures, evacuation procedures and activation of alternate work-sites and 'buddy branches'.

Risk Communication and Disclosure

Effective risk management requires active communication. This includes:

- Documenting our products, policies, procedures and systems;
- Training our employees;
- Tracking and reporting on our progress, performance and activities;
- Highlighting exceptions and new developments to Management and the Board; and
- Communicating to customers, regulators and other stakeholders.

Under Basel II Pillar 3, banks are required to provide consistent and comprehensive disclosures for risk management practices, to improve transparency in the financial markets and enhance market discipline. This has been in place since March 2011. Please refer to the Basel II Pillar 3 Disclosures in the Notes to the Financial Statements for further details.

Islamic Banking Risk Management

Compliance to Shariah principles is the foundation of our Islamic banking business and operations. This includes observing the tenets, conditions and principles prescribed by Shariah as resolved by Bank Negara Malaysia (BNM)'s Shariah Advisory Council as well as the Bank's Shariah Committee. In accordance with BNM's regulatory requirements, the Group had instituted a comprehensive Shariah Governance Framework to ensure efficient oversight by the Board of Directors, Shariah Committee and Management on the business activities and operations of our Islamic banking business.

The Shariah Committee forms one of the key governance bodies in respect of Shariah compliance. The Group has engaged qualified persons to be on our Shariah Committee to deliberate on Shariah issues and provide sound Shariah decisions. Furthermore, at least one member of the Shariah Committee is also appointed to the Board of Directors, to serve as a bridge between the Shariah Committee and Board.

Shariah governance includes establishing appropriate frameworks and policies which serve as guidance on the Shariah rules and principles. Amongst others, we have established the Shariah Governance Framework, Islamic Operational Risk Management Framework and guidelines for reporting Shariah non-compliance events.

The above is further supplemented by continuous risk awareness programmes to enhance employee knowledge and competencies on Shariah requirements. This is performed by the Shariah Review team concurrently with the business partners. In addition, this unit carries out independent Shariah reviews to ensure end-to-end Shariah compliance in the Group's activities and operations. The Shariah review reports are tabled to Shariah Committee as well as Group Operational Risk Management Committee.

The Group had initiated a Group-wide Shariah compliance initiative to assess and address end-to-end Shariah compliance within the overall business and operations of our Islamic banking unit. This ensures comprehensive compliance with Shariah principles in order to build confidence on the credibility of our Islamic business operations.