Risk Management for Banking

What is risk?

Danger that a certain unpredictable contingency can occur, which generates randomness in cash flow .

- Risk and uncertainty – risks may be described using probability analysis (business cycle, company failures), while events subject to uncertainty cannot (financial crises, wars etc.)

Main forms of risk

Credit risk

- risk that party to contract fails to fully discharge terms of contract

Interest rate risk

- risk deriving from variation of market prices owing to interest rate change

Market risk

- more general term for risk of market price shifts

Liquidity risk

- risk asset owner unable to recover full value of asset when sold (or for borrower, credit not rolled over)

Market liquidity risk

- risk that a traded asset market may vary in liquidity of the claims traded

Other risks

- o operational risk
- o risk of fraud
- o reputation risk

Systemic risk – that the financial system may undergo contagious failure following other forms of shock/risk

Risks in secured lending - particular reference to real estate

Why do banks overland to real estate?

- - alternatives?
- - Collateral
- - Balance sheet growth

Issues

- - externalities of lending severe
- - potential “disaster myopia”
- - vulnerability to macroeconomic
- shocks

Example of the consequences - Swedish banking crisis

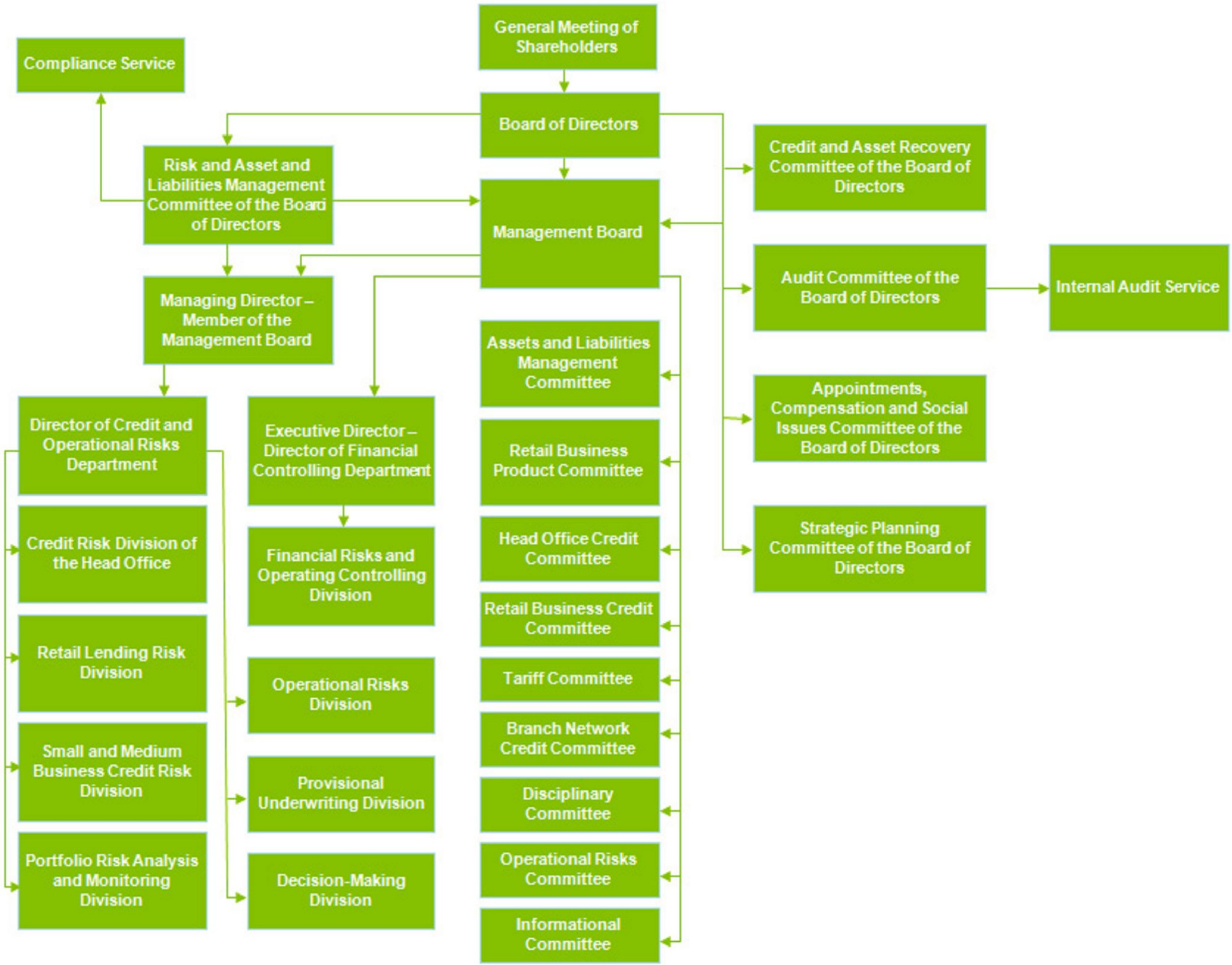
- Financial liberalisation – banks and
- authorities unfamiliar with liberalised
- regime
-
- Growth in bank lending (140% 1985-90)
- and private sector debt, particular focus
- on real estate lending, encouraged by tax
- deductibility
-
- Market share competition among banks
-
- Shocks - global recession, high interest
- rates to hold exchange rate, tax reform
- abolishing interest deductibility
-
- Majority of banks insolvent, non
- performing assets 14% of GDP
- Cost of public rescue 4.5% of GDP

Risk Management

BTA BANK

- Risk management system structure of BTA Bank JSC as one of the main components of corporate governance is focused on minimizing influence of any risk to the corporate financial status and its ability to perform assumed liabilities. BTA Bank JSC monitors and controls its risks in compliance with the main ethical principles and limits approved by the Board of Directors. The Board of Directors determines medium- and long-term strategies and supervises Company’s operations. Management Board, Risk and Asset and Liabilities Management Committee of the Board of Directors and other bodies responsible for risk management in due term submit reports on Company’s performance, information on risks and financial status for consideration and approval by the Board of Directors.

- Delegation of responsibility and liabilities between supervising and executive bodies in BTA Bank JSC is based on the principles of corporate governance in order to monitor and control the following risks related to banking activities:
- *Credit risk;*
- *Country risk;*
- *Market risk, including currency, interest and price risks;*
- *Liquidity loss risk;*
- *Operational risk;*
- *Compliance risk;*
- *Legal risk;*
- *Business reputation loss risk*


General Meeting of Shareholders
Compliance Service
Board of Directors
Risk and Asset and Liabilities Management Committee of the Board of Directors
Credit and Asset Recovery Committee of the Board of Directors
Management Board
Audit Committee of the Board of Directors
Internal Audit Service
Managing Director – Member of the Management Board
Assets and Liabilities Management Committee
Appointments, Compensation and Social Issues Committee of the Board of Directors
Director of Credit and Operational Risks Department
Executive Director – Director of Financial Controlling Department
Retail Business Product Committee
Credit Risk Division of the Head Office
Financial Risks and Operating Controlling Division
Head Office Credit Committee
Strategic Planning Committee of the Board of Directors
Retail Business Credit Committee
Retail Lending Risk Division
Tariff Committee
Operational Risks Division
Branch Network Credit Committee
Small and Medium Business Credit Risk Division
Provisional Underwriting Division
Disciplinary Committee
Operational Risks Committee
Portfolio Risk Analysis and Monitoring Division
Decision-Making Division
Informational Committee