Malayan Banking Berhad

Brunei Darussalam Branch

Basel II Pillar 3 Disclosures

For the financial year ended 31 December 2020

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Malayan Banking Berhad - Brunei Darussalam Branch

Basel II Pillar 3 Disclosures

I. OVERVIEW

The Pillar 3 Disclosures for the financial year ended 31 December 2020 for Malayan Banking Berhad – Brunei Darussalam Branch ("Maybank" or the "Branch") are in accordance with Autoriti Monetari Brunei Darussalam ("AMBD") Guidelines on Pillar 3 Public Disclosure Requirements, which are the equivalent of that issued by the Basel Committee on Banking Supervision ("BCBS") entitled International Convergence of Capital Measurement and Capital Standards (commonly referred to as Basel II).

Following the methodology employed by Malayan Banking Berhad ("Head Office" or the "Group"), the Branch adopts the following approaches in determining the capital requirements of Pillar 1 in accordance with AMBD's Guidelines on Capital Adequacy Framework (Basel II – Risk-Weighted Assets):

- Credit Risk -Standardised Approach ("SA") and will migrate to the Internal Ratings-Based ("IRB") approaches progressively.
- Market Risk - Standardised Approach ("SA").
- Operational Risk - Basic Indicator Approach ("BIA")

LOCATION OF DISCLOSURE

The Pillar 3 Disclosures will be made available to the public upon request via hard copy or electronically.

II. CAPITAL MANAGEMENT

The Branch's approach to capital management is to ensure that the Branch maintains adequate level of capital necessary to support its business and growth and to meet regulatory capital requirements at all times.

The Branch's capital planning and assessment process is guided by Branch's Capital Management Framework. The Branch is required to develop own Capital Management Framework based on the overarching principles of the Maybank Group Framework taking into account the nature of business, risk profile and the local operating environment. This will ensure that capital is managed on an integrated approach and in compliance with all internal and external regulatory requirements across the Maybank Group.

The Capital Management Framework is to be reviewed and updated either on an annual basis or whenever necessary to reflect changes in policies, governance or regulatory environment, amongst others.

III. RISK MANAGEMENT FRAMEWORK

The Group's risk management approach, which is followed by the Branch, has evolved into an important driver for strategic decisions in support of business strategies while balancing the appropriate level of risk taken to the desired level of rewards. As risk management is a core discipline of the Group, it is underpinned by a set of building blocks which serves as the foundation in driving strong risk management culture, practices and processes:

Building Blocks	Description
Risk Culture	Risk culture is a vital component in strengthening risk governance and forms a fundamental principle of strong risk management.
Risk Coverage	The Branch must determine its business strategy; its goals and objectives, and assesses the risk implied in that strategy before it can articulate its risk appetite.
Risk Appetite	The risk appetite defines the level of risk the Branch is willing to assume within its risk capacity.
Risk Response	Selection of the appropriate risk response is imperative to align the risks with Branch's risk tolerance and risk appetite.
Governance & Risk Oversight	There is a clear, effective and robust governance structure with well-defined, transparent and consistent lines of responsibility.
Risk Management Practices & Processes	Robust risk management processes are in place to actively identify, measure, control, monitor and report risks inherent in all products and activities undertaken by the Branch.
Stress Test	Stress testing should be used to identify and quantify possible events or future changes in the financial and economic condition that could have unfavourable effects on the Branch's exposure.
Resources & System Infrastructure	Ensure sufficient resources, infrastructure and techniques are established to enable effective risk management.

RISK APPETITE

The Group's risk appetite is an integral component of the Maybank Group's robust risk management framework and is driven by both top-down Board leadership and bottom-up involvement of management at all levels. Our risk appetite enables the Board and Senior Management to

communicate, understand and assess the types and levels of risk that the Maybank Group is willing to accept in pursuit of its business and strategic goals while taking into consideration constraints under stressed environment.
The risk appetite is integrated into the strategic planning process, and remains dynamic and responsive to the changing internal and external drivers such as market conditions, stakeholder's expectations and internal capabilities. In addition, the budgeting process is aligned to the risk appetite in ensuring that projected revenues arising from business transactions are consistent with the risk profile established. Our risk appetite also provides a consistent structure in understanding risk and is embedded in day-to-day business activities and decisions throughout the Group.

Guided by these principles, our risk appetite is articulated through a set of Risk Appetite Statements for all material risks across the Group and Branch to ultimately balance the strategic objectives of the Group.

RISK GOVERNANCE AND OVERSIGHT

The risk governance model provides a formalised, transparent and effective governance structure that promotes active involvement from the Board and Senior Management in the risk management process to ensure a uniform view of risk across the Maybank Group and the Branch.

The governance model places accountability and ownership in ensuring an appropriate level of independence and segregation of duties between the three lines of defense. The management of risk broadly takes place at different hierarchical levels and is emphasized through various levels of committees, business lines, control and reporting functions.

INDEPENDENT GROUP RISK FUNCTION

Maybank Group Risk Management provides an oversight of risk management on an enterprise-wide level through the establishment of the Maybank Group's risk strategies, framework and policies with independent assessment and monitoring of all risks challenges.

The key pillars of Maybank Group Risk functions are as follows:

- Provides close support and oversight within key businesses and countries in managing day-to-day risk;
- Drives and manages specific risk areas on an enterprise-wide level for a holistic risk view within the Maybank Group and the Branch; and
- Supports sustainable and quality asset growth with optimal returns.

IV. CREDIT RISK

Credit risk is the risk that a counterparty fails to meet its obligations in accordance with the agreed terms of a credit facility. The exposures to credit risk are unilateral and only the lending bank faces the risk of loss.

REGULATORY CAPITAL REQUIREMENT

Amongst the various risk types the Branch engages in, credit risk continues to attract the largest regulatory capital requirement.

MANAGEMENT OF CREDIT RISK

The Branch manages its credit risk using a two-pronged approach to ensure they remain within the boundaries of Branch's risk appetite statement.

• Managing the Credit Risk; and
• Managing the Credit Portfolio.

Corporate credit risks are assessed by business units, where each customer is assigned a credit rating based on the assessment of relevant qualitative and quantitative factors including the customer's financial position, future cash flows, types of facilities and securities offered. These credits are then evaluated and approved by a party independent of the originator.

All corporate and retail credit risks are subject to regular periodic credit classification and impairment assessment to determine appropriate early intervention on top of reviews conducted at least once a year with updated information on the customer's financial position, market position, industry and economic conditions, and conduct of account. Corrective actions are taken when the accounts show signs of credit deterioration.

Retail credit exposures are managed on a programme basis guided by the Product Development Assessment (PDA) as an underwriting standard. Credit programmes are assessed jointly between credit risk and business units. Reviews on the credit programmes are conducted at least once a year to assess the performances of the portfolios. During the COVID-19 pandemic, in a collective effort to assist and reduce the financial burden of all customers (businesses and individuals), the following measures were extended to customers pursuant to the AMBD Notice on 15 April 2020 as a temporary regulatory relief:

- Temporary deferment of existing monthly repayment
- Restructuring of existing credit facilities
- Conversion of credit card receivables to fixed term loans with tenor not exceeding 36 months

Credit approving authorities and committee structures are in place to ensure appropriate underwriting standards are enforced consistently throughout the Group and Branch level.

Management of Concentration Risk

Concentration risk can materialise from excessive exposures to a single counterparty and persons connected to it, a particular instrument or a particular market segment/sector.

In managing large exposures and to avoid undue concentration of credit risk in its loans and financing portfolio, the Branch has put in place, amongst others, limits and related lending guidelines for:
• Business segments;
• Economic sectors;
• Single customer groups;
• Banks and Non-Bank Financial Institutions ("NBFIs") and
• Collaterals.

Reviews of the said limits and related lending guidelines are undertaken on a periodic basis, whereupon any emerging concentration risks are addressed accordingly. Any exception to the limits and lending guidelines would be subjected to approvals from higher credit authorities.

Asset Quality Management

The Branch has dedicated teams to effectively manage vulnerable corporate and consumer credits. Special attention is given to these vulnerable credits where more frequent and intensive reviews are performed in order to prevent further deterioration or, where necessary, accelerate remedial actions. With the pandemic, the Branch has stepped up effort to proactively monitor and manage affected credits via several measures including but not limited to moratoriums.

The Maybank Group's credit approving process encompasses pre-approval, approval and post-approval evaluation. Maybank Group Risk is responsible for developing, enhancing and communicating effective and consistent credit risk management policies, tools and methodologies across the Group to ensure appropriate standards are in place to identify, measure, control, monitor and report such risks.

In view that the authority limits are directly related to the risk levels of the borrower and the transaction, a Risk-Based Authority Limit structure is implemented based on the Expected Credit Loss principle and internally-developed Credit Risk Rating System.

Table 1 presents the geographical analysis and distribution of credit exposures for the Branch.

Table 2 presents the credit risk exposures by various industries for the Branch.

Table 3 presents the credit risk exposures by maturity periods of one year or less, over one year to five years and over five years for the Branch.

Table 1: Disclosure on Credit Risk Exposure - Geographical Analysis for the Branch

Exposure Class	Brunei (BND'000)	Singapore (BND'000)	Total (BND'000)
As at 31 December 2020			
Bank, Development Financial Institutions & Multilateral Development Banks	602	210,591	**211,193**
Corporates	101,922	-	**101,922**
Regulatory Retail	84,814	-	**84,814**
Residential Mortgages	1,374	-	**1,374**
Other Assets	3,146	-	**3,146**
Total	**191,858**	**210,591**	**402,449**

Table 2: Disclosure on Credit Risk Exposure for Loan & Advances and Contingencies - Industry Analysis for the Branch

Exposure Class	Agriculture BND'000	Manufacturing BND'000	Infrastructure, Constructions & Property Financing BND'000	Wholesale, Retail Trade, Restaurants & Hotels BND'000	Finance, Insurance, Real Estate & Business BND'000	Transport, Storage & Communication BND'000	Household BND'000	Total BND'000
Bank, Development Financial Institutions & Multilateral Development Banks	-	-	-	-	602	-	-	**602**
Corporates	3,169	5,154	15,550	76,791	1,070	188	-	**101,922**
Regulatory Retail	-	-	16,559	509	-	-	67,746	**84,814**
Residential Mortgages	-	-	-	-	-	-	1,374	**1,374**
Total	**3,169**	**5,154**	**32,109**	**77,300**	**1,672**	**188**	**69,120**	**188,712***

**The above amount excludes cash and short-term funds.*

Table 3: Disclosure on Credit Risk Exposure - Maturity Analysis for the Branch

Exposure Class	One year or less BND’000	Over one year to five years BND’000	Over five years BND’000	Total BND’000
As at 31 December 2020				
Bank, Development Financial Institutions & Multilateral Development Banks	203,223	7,970	-	**211,193**
Corporate	9,272	70,729	21,921	**101,922**
Regulatory Retail	1,328	10,271	73,215	**84,814**
Residential Mortgages	-	-	1,374	**1,374**
Other Assets	-	3,146	-	**3,146**
Total	**213,823**	**92,116**	**96,510**	**402,449**

BASEL II REQUIREMENTS

In line with Basel II requirements for capital adequacy purposes, the parameters are calibrated to a full economic cycle experience to reflect the long-run, cycle-neutral estimations:

- **Probability of Default (“PD”)**

PD represents the probability of a borrower defaulting within the next 12 months. The first level estimation is based on portfolio’s Observed Default Rate of the more recent years’ data.

- **Loss Given Default (“LGD”)**

LGD measures the economic loss the bank would incur in the event of a borrower defaulting. Among others, it takes into account post default pathways, cure probability, direct and indirect costs associated with the workout, recoveries from borrower and collateral liquidation.

For Basel II purpose, LGD is calibrated to loss experiences during period of economic crisis whereby for most portfolios, the estimated loss during crisis years is expected to be higher than that during normal economic period. The crisis period LGD, known as Downturn LGD, is used as an input for Risk-Weighted Assets (“RWA”) calculation.

- **Exposure at Default (“EAD”)**

EAD is linked to facility risk, namely the expected gross exposure of a facility should a borrower default. The “race-to-default” is captured by Credit Conversion Factor (“CCF”), which should reflect the expected increase in exposure amount due to additional drawdown by a borrower facing financial difficulties leading to default.

CREDIT IMPAIRMENT POLICY AND CLASSIFICATION AND IMPAIRMENT PROVISIONS FOR LOANS AND ADVANCES

Refer to Notes 2.5 and 3.4 of the Financial Statements for the accounting estimates on impairment assessment for loans and advances and accounting policies and, respectively. The disclosures on reconciliation of loss allowance for loans and advances can be found in Note 29.5.6 of the Financial Statements.

This credit impairment policy is applicable to the Branch.

Table 4 provides details on impaired and past due loans for the Branch.

Table 4: Impaired and Past Due Loans, Advances and Financing and Allowances - Industry Analysis for the Branch

	Impaired Loans, Advances and Financing BND'000	Past Due Loans BND'000	ECL BND'000
As at 31 December 2020			
Agriculture	-	-	17
Manufacturing	-	-	12
Infrastructure, constructions & property financing	20,408	573	8,212
Wholesale, retail trade, restaurants & hotels	700	3,151	1,006
Finance, insurance, real estate & business	-	-	-
Transport, storage & communication	-	-	1
Household	57	2,865	55
Total	**21,165**	**6,589**	**9,303**

CREDIT RISK MITIGATION

The Branch takes a holistic approach when granting credit facilities and credit assessment based on the repayment capacity of the borrower, rather than placing the credit risk mitigation as a primary source of repayment. As a fundamental credit principle, the Branch generally does not grant facilities solely on the basis of collaterals provided. Credit facilities are granted based on the credit standing of the borrower, source of repayment and debt servicing ability.

Depending on a customer's credit standing and the type of product, facilities may be provided on an unsecured basis. Nevertheless, collateral is taken whenever possible to mitigate the credit risk assumed. The Branch's general policy is to promote the use of credit risk mitigation, justified by commercial prudence and good practice as well as capital efficiency. The value of collateral taken is also monitored periodically. The frequency of valuation depends on the type, liquidity and volatility of the collateral value. The main types of collateral taken by the Branch include cash, property, commercial, industrial, marketable

instruments, bank guarantees, land, stand-by letter of credit and assigned insurance policies. For IRB purposes, personal guarantees are not recognised as an eligible credit risk protection.
Corporate guarantees are often obtained when the borrower's credit worthiness is not sufficient to accommodate an extension of credit. To recognise the effects of guarantees under the Foundation Internal Ratings-Based ("FIRB") Approach, the Branch adopts the Probability of Default substitution approach whereby exposures guaranteed by an eligible guarantor will utilise the PD of the guarantor in the computation of its capital requirement.

As a general rule-of-thumb, the following eligibility criteria must be met before the collateral can be accepted for IRB purposes:

• **Legal Certainty**
The documentation must be legally binding and enforceable in all relevant jurisdictions.

• **Material Positive Correlation**
The value of the collateral must not be significantly affected by the deterioration of the borrower's credit worthiness.

• **Third-party Custodian**
The collateral that is held by a third-party custodian must be segregated from the custodian's own assets.

Tables 5 show the credit risk mitigation analysis for the Branch.

Table 5: Disclosure on Credit Risk Mitigation Analysis for the Branch

Exposure Class	Exposures before CRM BND'000	Exposures Covered by Guarantees/ Credit Derivatives BND'000	Exposures Covered by Eligible Financial Collateral BND'000	Exposures Covered by Other Eligible Collateral BND'000
As at 31 December 2020				
On-Balance Sheet Exposures				
Banks, Development Financial Institutions & Multilateral Development Banks	210,591	-	-	-
Corporates	89,451	-	9,418	20,759
Regulatory Retail	84,814	-	400	73,844
Residential Mortgages	1,374	-	-	1,283
Other Assets	3,146	-	-	-
Total On-Balance Sheet Exposures	389,376	-	9,818	95,886
Off-Balance Sheet Exposures				
Banks, Development Financial Institutions & Multilateral Development Banks	602	-	-	-
Corporates	12,471	-	-	-
Total for Off-Balance Sheet Exposures	13,073	-	-	-
Total On and Off-Balance Sheet Exposures	402,449	-	9,818	95,886

V. MARKET RISK

Market risk is defined as the risk of loss or adverse impact on earnings or capital arising from fluctuations of market rates or prices such as interest rates/profit rates, securities prices and foreign exchange rates.

Non-traded market risk is primarily inherent risk arising from banking book activities. The major risk classes are interest rate risk in the banking book and foreign exchange risk.

The Branch is not exposed to significant market risk in 2020.

FOREIGN EXCHANGE RISK

Foreign exchange risk is the risk of loss in value arising from exchange rate movements.

The Branch's foreign exchange exposures comprise non-trading foreign exchange exposure principally derived from interbranch nostro accounts. The Branch is not exposed to foreign exchange risk for Singapore Dollar (SGD) due to the currency Interchange Agreement between Singapore and Brunei which interchange the two currencies at par.

Foreign exchange risk is managed through policies and risk limits approved by the Asset and Liability Committee (ALCO). The limits, such as exposure by currency are independently monitored by Middle Office (MO). A summary of quantitative data about the Branch's net exposure to major foreign currencies is provided below, followed by a sensitivity analysis (assuming all other risk variables remain constant):

	GBP	USD	Others	Total
As at 31 December 2020				
Financial assets				
Group balances receivable	60	1,479	70	1,609
Financial liabilities				
Group balances payable	-	-	3,194	3,194

A 10% strengthening of BND against the foreign currencies as at year end, would have increased profit or loss and equity by B$131 thousand. The analysis assumes that all other variables, in particular interest rates, remain constant.

A 10% weakening of BND against the foreign currencies as at year end would have had the equal but opposite effect on the amount mentioned above, on the basis that all other variables remain constant.

INTEREST RATE RISK

Interest rate risk is the risk to both earnings and capital arising from adverse movement in interest rates.

As at 31 December 2020, the interest rate profile of the Branch's interest-bearing financial instruments is as follows:

	BND '000
Fixed-rate assets	223,752
Floating-rate assets	168,340
Fixed-rate liabilities	(291,073)
	101,019

The Branch does not account for any fixed rate financial assets and liabilities at fair value through profit or loss. Therefore, a change in interest rates at the reporting date would not affect profit or loss for fixed rate financial instruments.

At the reporting date, an increase of 100 basis points in interest rates would have increased profit or loss by B$176 thousand for variable rate financial instruments. A decrease of 100 basis points in interest rates would have the opposite effect on profit or loss. This analysis assumes that all other variables remain constant.

EQUITY POSITION IN THE BANKING BOOK

The Branch is not exposed to equity price risk as there are no equity investments carried in the books.

VI. OPERATIONAL RISK

Operational risk is one of the principal risks in the overall Risk Management Framework and defined as the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events (this includes legal risk, but excludes strategic and reputational risk).

The table below outlines the definition of the four (4) casual categories of operational risk:

Casual Categories	Definition
People	Risks resulting from staff defaulting in expected behavior or the organization being ineffective/inefficient in the management of its human capital.
Process	Risks resulting from inadequate/failed internal business processes or transaction process flows.
System	Risks resulting from inadequate or defaulting IT/communication systems, or the unavailability or integrity of data.
External Events	Risks resulting from events and actions from outside the organisation's immediate control having negative impact on the business.

Operational risk incidents that occurred may have different financial impact as illustrated below:

Impact Type	Definition
Actual Loss	Financial loss is incurred (either by a third part cost, or by writing-off a provision) and/or provision for loss is made, impacting the profit or loss account.
Potential Loss	Potential loss is a conservative estimate of the loss amount but the actual loss has yet to be determined.
Near Miss	Financial loss was averted by controls or mitigating actions for an operational risk incident.

Group Operational Risk Management strategy provides the overall principles, philosophy, objectives and goals for the management of operational risk.

The key components of the Group's ORM strategy are as follows:

(i) ORM Methodology Design Principles
(ii) Operational Risk Appetite

Under the Basel II rules, the Branch has adopted the Basic Indicator Approach to operational risk in which the charge for operational risk may be expressed as follows:

$\boldsymbol{KBIA} = [\ \Sigma \boldsymbol{GI1} \ldots \boldsymbol{n} \times \boldsymbol{\alpha}\ ]/\boldsymbol{n}$

where:
$KBIA$ = the capital charge under the Basic Indicator Approach
GI = annual gross income, where positive, over the previous three years
N = number of the previous three years for which gross income is positive
α = 15%

Certification

I certify that the above statements give a true and fair view of the Pillar 3 Disclosures of the Brunei Operations of Malayan Banking Berhad ("the Branch") for the financial year ended 31 December 2020.

Sulaiman bin Isa
General Manager

Noor Hajirah Saban
Head, Finance