

# RISK MANAGEMENT



**“We made excellent progress towards Group Risk's 2015 roadmap of high performance risk culture across the Group, as we have built robust and scalable foundations, enabling us to create value to support the Group’s regional aspirations.”**

**Dr John Lee**  
Group Chief Risk Officer

## OUR KEY ACHIEVEMENTS FOR 2013

- Embedded risk management into our business strategy and planning to ensure our risk-taking activities are aligned with our risk management more effectively.
- Defined, aligned and implemented our Risk Appetite framework across the Group to better define our risk-taking boundaries.
- Improved the Risk-Reward dynamics across the Group by enhancing our risk-informed pricing decisions and performance.
- Continued to reduce the cost structure of our balance sheet and optimise the capital across the Group.
- Continued to drive improvements across all risk frameworks, systems and processes to deliver value-added services to the business in a cost effective manner and enhance our stakeholder engagements.
- Established Centres of Excellence (COEs) to build deep specialisation of risk professionals to provide value-added risk insights to support business decision-making.
- Enhanced our Risk Talent Management blueprint to up-skill resources and set the platform to bridge competency gaps.
- Initiated various risk systems enhancements to ensure robust risk capabilities through technology.

# RISK MANAGEMENT

## OVERVIEW

Amidst the challenging global economic environment, Group Risk remained committed to its 2013 strategic priorities to enhance and integrate risk into the business to strengthen risk management effectively across the Group. Our robust risk management continues to play an integral part in driving value creation to support the Group's regional aspiration.

During the financial year, the Group's risk transformation efforts were driven by the following external and internal drivers:

### External Drivers

- Challenging economic and cost environment;
- Regulatory pressures on business model and cost structure;
- Increase in data and IT infrastructure requirements; and
- Talent shortages across the region.

### Internal Drivers

- Group's transformation initiatives gaining critical mass;
- Greater complexities in Group's Operating model;
- Products becoming increasingly sophisticated and technical; and
- The need to integrate strategic acquisitions.

With these external and internal factors, Group Risk's 2013 Strategic Priorities were:

### MEDIUM TERM

Enhance and Integrate

Optimising and integrating risk into the business to drive value creation for the Group

#### Enhancing overall risk frameworks, systems and processes

- Continue to drive process improvements across all risk frameworks, systems and processes to deliver value-added services to the business in a cost effective manner and enhance our stakeholder engagements.

#### Improving the Risk-Reward dynamics across the Group

- Improve risk-informed pricing decisions and performance.
- Embed Risk Appetite across all Group entities.
- Create and embed the Right Risk Culture.

#### Optimising capital and liquidity management across the Group

- Reduce the cost structure of our balance sheet.
- Optimise the capital across the Group.

## RISK GOVERNANCE

In accordance to the Group's structure and regionalisation aspirations, the Group continuously enhances its integrated risk management approach towards the effective management of enterprise-wide risks. The Group views the overall risk management process with a structured and disciplined approach to align strategies, policies, processes, people and technology with the specific purpose of evaluating all risk types in line with enhancing shareholder value.

## Risk Governance Structure

### Board of Directors

The Board of Directors is the Group's ultimate governing body, which has overall risk oversight responsibility. It approves the risk management framework, risk appetite, plans and performance targets for the Group and its principal operating subsidiaries, the appointment of senior officers, the delegation of authorities for credit and other risks, and the establishment of effective control procedures.

### Board Level Committees

#### Risk Management Committee (RMC)

The RMC is a dedicated Board Committee responsible for the risk oversight function within the Group. It is principally responsible to review and approve key risk frameworks and policies for the various risks.

#### Credit Review Committee (CRC)

The CRC is tasked by the Board to review/concur/veto fresh or additional loan applications subject to pre-determined authority limits as recommended by the Group Management Credit Committee.

### Executive Level Management Committees

#### Group Executive Risk Committee (ERC)

#### Group Operational Risk Management Committee (GORMC)

#### Group Asset & Liability Management Committee (ALCO)

#### Group Management Credit Committee (GMCC)

The ERC, GORMC, ALCO and GMCC are Executive Level Management Committees responsible for the management of all material risks within the Group. The scope of ERC encompasses all risk types, whilst the GORMC caters specifically to operational risk matters. The ALCO is primarily responsible for the development and implementation of broad strategies and policies for managing the consolidated balance sheet and associated risks. The GMCC is empowered as the centralised loan approval committee for the Group.

## Risk Management Framework

Key components of the Enterprise Risk Management (ERM) framework include:

### ERM ROLES AND FUNCTIONS



In line with the ERM approach, the Group has adopted and consistently practices the Seven Broad Principles of Risk Management to ensure integration of purpose, policy, methodology and systems across its regional footprint.

## RISK MANAGEMENT

### Maybank Group's Seven Broad Principles of Risk Management

The Seven Broad Principles define the key principles on accountability, independence, structure and scope.

#### Principles

1. The risk management approach is premised on three lines of defence – risk-taking units, risk control units and internal audit.
2. The risk-taking units are responsible for the day-to-day management of risks inherent in their business activities, while the risk control units are responsible for setting up risk management frameworks and developing tools and methodologies for the identification, measurement, monitoring, control and pricing of risk. Complementing these is internal audit, which provides independent assurance of the effectiveness of the risk management approach.
3. Risk management provides risk oversight for the major risk categories including credit risk, market risk, liquidity risk, operational risk and other industry-specific risks.
4. Risk management ensures that the core risk policies of the Group are consistent, sets the risk tolerance levels and facilitates the implementation of an integrated risk-adjusted measurement framework.
5. Risk management is functionally and organisationally independent of the business sectors and other risk-taking units within the Group.
6. The Board, through the Board Risk Management Committee, maintains overall responsibility for risk oversight within the Group.
7. Risk management is responsible for the execution of various risk policies and related business decisions empowered by the Board.

The key strategic initiatives undertaken by the Group this year to accomplish the risk transformation that we have envisaged are highlighted below.

### STRATEGY

#### • Enhance Risk Adjusted Performance Measurements (RAPM)

The Group continues to enhance the RAPM methodology and further embed RAPM measurement and risk-informed pricing into management/customer processes.

#### Driving Value from Risk-Informed Pricing

In demonstrating risk management as a key strategic differentiator for the Group, we have strengthened our RAPM process to drive improved risk-reward dynamics. We have operationalised our risk-informed pricing across the Group and instilled greater discipline in our pricing based on appropriate risk-reward thresholds.

Our initiative is in line with regulatory expectation as per the Risk-Informed Pricing guideline issued by Bank Negara Malaysia (BNM). We believe there is greater advocacy on the standards that define the responsibilities of financial service providers to adopt the risk-informed approach in the pricing of retail loan/financing products. This is to ensure that decisions on retail loan/financing pricing are consistent with the approved risk appetite. Presently, financial service providers should clearly define risk measurement and pricing mechanisms as well as control their costs in order to meet profit maximisation objectives. The guideline highlights prudential standards in the following areas:

- ▶ Expectations of the Board of Directors and internal policies for loan/financing pricing; and
- ▶ Minimum pricing components to be incorporated in the loan/financing pricing and supervisory expectations on the methodology used for the estimation of these components.

With the objective of remaining competitive and delivering adequate returns to the shareholders, financial service providers are required to scrutinise their operations to ensure that their earning assets are effectively deployed. In this context, proper pricing of loans/financing is now becoming crucial from business and regulatory perspectives.

Group Risk is committed to continuously embed and enhance the risk-informed pricing across the Group to improve our performance. The observed benefits derived from this initiative are as follows:

- ▶ Enables an institution to know early on the type of pricing/fees that will satisfy its risk/return preferences;
- ▶ Enhances shareholder value by ensuring that risks associated with the transaction are appropriately measured and priced; and
- ▶ Enhances the achievement of credit portfolio goals and objectives.

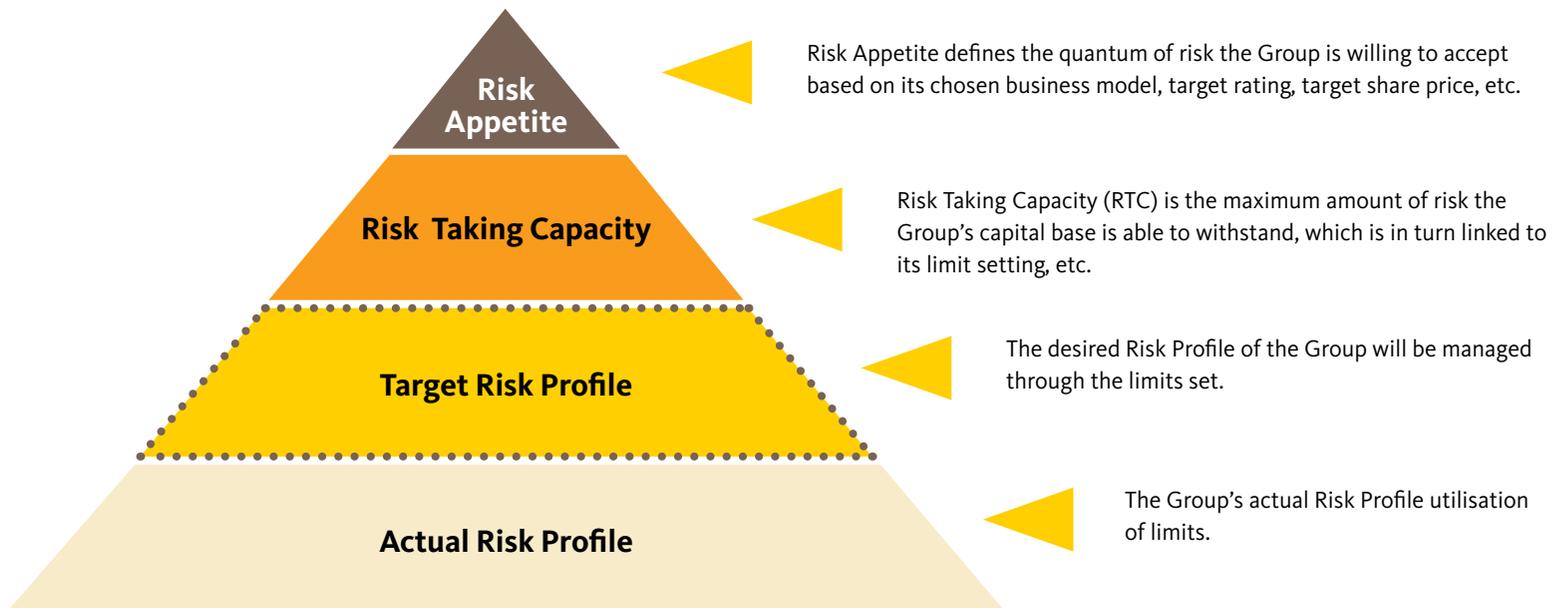
#### • Align Our Risk Appetite

The Group has successfully embedded a Risk Appetite Framework across the Bank, our major subsidiaries and key branches. The Risk Appetite Framework defines our risk capacity, establishes and regularly confirms our risk appetite, translates risk appetite into risk limits and tolerances as guidance, and regularly measures and evaluates our risk profile.

A key element of the Risk Appetite Framework is a set of Board-approved Risk Appetite Statements (RAS) that define the boundaries and drivers that the Group has chosen to limit or otherwise influence the amount of risk it is willing to take. The Group's Risk Appetite Framework and RAS were first approved by the Board in 2011 and have since been reviewed and updated annually.

The goal of risk management is not to eliminate risk, but to manage it effectively to provide our stakeholders with long term returns that commensurate with the risk. Hence, The Group's RAS, is in essence, the Board and Senior Management's statement of intent and 'posture' on its risk-taking activities as well as the management of it.

### Risk Appetite Building Blocks



#### Balancing Risk Strategy and Business Strategy

From an organisational perspective, the Risk Appetite links the Group's risk strategy to the business strategy through desired target ratings (solvency), earnings volatility and risk limits, among other factors. The process of developing the RAS has been integrated into the Group's annual budget and business planning cycle as we continue to ensure that our risks, returns and capital are managed on an integrated basis.

The Risk Appetite setting process has also put in place the concept of 'Risk Posture', which is a description of the business' willingness to take risk considering internal and external factors and is forward-looking. The 'Risk Posture' will be determined by the business strategy, which in turn will drive the Group's risk-taking capacity and finally the setting of the RAS.

- **Enhance Risk Culture**

Risk Culture is defined by the Institute of International Finance (IIF) as "the norms and traditions of behaviour of individuals and of groups within an organisation which determine the way in which they identify, understand, discuss and act on the risks the organisation confronts and assumes".

We view Risk Culture as the foundation upon which a strong enterprise wide risk management framework is built and it is an essential building block for effective risk governance. The 'Risk Culture Index' aimed at measuring our current state of risk culture across the Group was successfully launched in the fourth quarter of 2012. The survey results were cascaded to the Board, Group Executive Committee, Management Committees, Strategic Business Units and entities throughout the Group in 2013.

Arising from the survey results, specific action plans and initiatives have been developed and operationalised across the Group in 2013. At the industry level, strong advocacy on embracing the 'Right Risk Culture' is demonstrated by our active participation as a key member in the IIF's Effective Supervision Advisory Group on issuing the Financial Stability Board Guidance on Risk Culture. We endeavour to continuously embed the 'Right Risk Culture' across the Group in complementing our sustainable growth with a responsible and risk-aware manner.

#### PEOPLE

- **Institutionalise our Talent Management Blueprint**

The Group has developed a comprehensive risk talent management blueprint to clearly articulate core risk competencies required by our risk professionals. The blueprint has been successfully rolled-out to the key business units and subsidiaries in December 2013.

The Group has re-designated its Internal Assessment of the Core Credit Personnel Programme to Maybank Internal Credit Accreditation Programme (MICAP) to better reflect the credit role. The MICAP was fully implemented to the relevant sectors domestically during the year while Maybank Cambodia was the first overseas unit to implement this programme in July 2013. The programme will also be rolled-out to Maybank Hong Kong and Maybank Philippines Incorporated in the third quarter of 2014, with the rest of the Group by 2015. The programme is aimed to strengthen our credit origination and positively impact overall asset quality across the Group upon implementation.

In our continued effort to up-skill risk management resources, the Annual Risk Masterclass was held successfully for the third consecutive year. Various risk subject matter experts from across the Group were engaged to share their knowledge covering multiple risk management topics and current risk trends.

#### PROCESS

- **Establish Centres of Excellence (COEs)**

During the financial year, Group Risk functions were reorganised to create risk centres of excellence to drive efficiency. The COEs were established to build deep specialisation of risk professionals, to provide value-added risk insights to support business decision-making and increase economies of scale to drive down the cost of delivery.

The identified COEs have also set consistent standards in terms of enterprise risk reports, risk policy architecture and risk modelling implementation across the Group.

## RISK MANAGEMENT

- **Institutionalise Shariah Compliance**

Shariah principles are the foundation for the practice of Islamic finance through the observance of the tenets, conditions and principles prescribed by Shariah as resolved by BNM's and Securities Commission's Shariah Advisory Council (SAC) and the Shariah Committee of Maybank Islamic Berhad. Comprehensive compliance with Shariah principles in the Islamic business activities and operations will lend confidence to stakeholders.

In accordance to BNM's regulatory requirements, the Group has implemented a comprehensive Shariah Governance Framework to ensure effective and efficient oversight by the Board of Directors, Board Committees and the Shariah Committee on the business activities and operations of Islamic products and services carried out by the Group's Islamic banking businesses.

- **Enhance Key Risks Early Warning Systems**

The Group has instituted a process to identify the emerging risks. The process includes:

- ▶ Conducting scenario planning exercises;
- ▶ Assessing the risks according to likelihood and impact for the next five years; and
- ▶ Utilising the results for our stress testing, capital management and limit setting.

On top of managing the emerging risks, the respective countries and business risk teams are developing key risk indicators that are forward-looking for effective identification of risk.

- **Enhance Regulatory Management**

Group Risk has formulated strategies to further improve our regulatory rating. Implementation of the strategic initiatives and areas for improvement are currently on-going.

The Group is diligent in its pursuit to adopt The Standardised Approach (TSA) for Operational Risk Capital Charge Calculation. The use of TSA is subject to BNM's approval. For this purpose, the Group has mapped its business activities into eight business lines as prescribed by Basel II and the BNM Risk-Weighted Capital Adequacy Framework.

The Group is in preparation to meet the Basel III regulatory requirements on capital and liquidity compliance.

- **Enhance Capital & Liquidity Techniques**

The Group's approach to capital management is driven by its strategic objectives and takes into account all the relevant regulatory, economic and commercial environments in which the Group operates. The Group regards having a strong capital position as essential to the Group's business strategy and competitive position. As such, implications on the Group's capital position are taken into account by the Board and senior management prior to implementing major business decisions in order to preserve the Group's overall capital strength.

The Group's key thrust of capital management and planning are to diversify its sources of capital; to allocate and deploy capital efficiently guided by the need to maintain a prudent relationship between available capital and the risks of its underlying businesses; and to meet the expectations of key stakeholders, including investors, regulators and rating agencies.

The Group's capital management is guided by the Group Capital Management Framework to ensure consistency and alignment of capital management policies and procedures across the Group. The Group Capital Management Framework, which is approved by the Board, applies across the Group and its entities.

Liquidity risk appetite is approved by the RMC while ERC and ALCO are responsible for the overall operational implementation and controls that are guided by the approved liquidity risk management framework and policy.

The Group runs liquidity stress scenarios to assess the areas of vulnerability and determines its funding capacity and adequacy for normal and stressed market situations. The Group also activates its Contingency Funding Plan (CFP) to avert any potential liquidity disasters affecting its liquidity soundness and financial solvency.

In line with leading practices, the Group is preparing to meet the Basel III Liquidity Coverage Ratio (LCR) compliance by 1 January 2015 while considering the requirements for the Net Stable Funding Ratio (NSFR), which comes into effect from 1 January 2018.

### Risk-Weighted Assets (RWA) Optimisation

The RWA Optimisation Programme (ROP) was designed as a collaborative effort between Group Risk and the Business to implement various initiatives to optimise the Group's RWA, as part of our continuous capital management process.

The ROP continues to optimise the Group's RWA through the following key determinants:

- ▶ Business model – impact on risk profile such as loan origination and strategic business focus;
- ▶ Risk management – approaches to calculate credit, market and operational risk, regular review of risk models and methods;
- ▶ Processes – the direct and indirect impacts on RWA covering front and back office operations such as proactive management of 'stale ratings'; and
- ▶ Collateral management.

## SYSTEMS

- **Risk Technology Architecture**

There is a growing need to derive a holistic view of the risk landscape both from a business and technology perspective. Moving forward, the Group will adopt the business driven risk architecture to improve management of key risks across the enterprise. The enterprise-wide solution to cater for the unique requirement of each business user would promote speed to market for business and regulatory changes as well as enable business process optimisation.

Strong strategic alignment between risk and business would enhance the Group's risk management through the provision of timely, accurate and informative approach for forward-looking analytics. Some key benefits from a robust IT architecture are:

- ▶ Business process efficiency;
- ▶ Single source of risk information;
- ▶ Flexible platform to carry out business impact analysis; and
- ▶ Lesser time to respond to regulatory requirements or business changes.

For our awards and recognition, refer to page 63.

## STRATEGIC INITIATIVES FOR 2014

Against the backdrop of an improving global economy and further regulatory reforms, banks will be competing to benefit from the recovery of developed markets, adapt to new regulatory landscapes and also take advantage of the next wave of expansion in rapid-growth markets. Moving forward, there is an increased need for Group Risk to further enhance and fully integrate into our business to work more effectively to value-add across the Group.

Hence in 2014, Group Risk will be embarking on the following strategic themes to align with the Group in order to accelerate our value creation efforts.

Collaboration and Innovation	Risk Regionalisation	Optimisation and Efficiency
<ul style="list-style-type: none"> <li>Strengthen Group Risk's role as a business partner across the Group.</li> <li>Enhance relationship management with stakeholders across the Group.</li> </ul>	<ul style="list-style-type: none"> <li>Regionalise risk resources, systems, frameworks and processes.</li> <li>Ensure seamless provision of risk management across the Group.</li> </ul>	<ul style="list-style-type: none"> <li>Optimise resources effectively and efficiently across the Group.</li> <li>Improve synergies within the business by utilising risk management as a competitive advantage to optimise returns.</li> <li>Ensure constant improvement of processes for better efficiency.</li> </ul>

Based on the strategic themes above, we have identified the following key initiatives for 2014 with the ultimate objective to establish a regional platform for risk management to enable scalability and alignment of risk management practices across the Group. As we continue with our journey of regionalisation, we believe that the successful implementation of these initiatives will propel Group Risk further towards achieving the Group's regional aspirations.

- 1 Fortify Risk Management's Role in Strategic Decisions**
  - Link the Risk Appetite statement setting process with budget and business planning.
  - Ensure the Risk Appetite framework and process are embedded across the Group.
- 2 Enhance Group Risk's Research and Knowledge Base**
  - Build up Group Risk's research and knowledge capabilities to provide better support across the Group.
  - Continue to build deep specialisation of risk professionals to provide value-added risk insights to support the business across the Group.
- 3 Improve Regulatory Management**
  - Enhance relationship with the regulatory authorities locally and across region, and to be more proactive in managing and participating in the regulations discussions.
- 4 Develop a Group Risk IT Architecture**
  - Develop a Group-wide Risk IT architecture to support the Group's regional aspirations.
  - Consolidate stand-alone systems to a regional risk operating platform.
- 5 Accelerate Regionalisation Initiatives**
  - Accelerate and streamline risk management practices across the Group.
  - Ensure clarity and consistency of risk practices to support regional business across the Group.
  - Embed Centres of Excellence.
- 6 Entrench the Right Risk Culture Behaviour and Risk Awareness Across the Group**
  - Continue to ensure that the Right Risk Culture is embedded across the Group.
  - Continue to improve the Risk Culture Index scoring.
- 7 Enhance our Talent Management Blueprint Across the Group**
  - Leverage on Group Risk's regional structure to optimise the risk resources across the Group and provide seamless risk management to the business.
  - Develop a regional talent competency framework and reduce competency gaps.
- 8 Optimise Capital and Liquidity Practices**
  - Optimise our cost structure through RWA optimisation and balance sheet management.
  - Continue to enhance our liquidity management techniques and meet regulatory requirements.
- 9 Enhance the Group's Risk-Reward Analytics and Dynamics**
  - Institutionalise risk-informed pricing across the Group.
  - Improve key risks early warning systems as part of risk reporting.
  - Enhance and automate key risk processes to facilitate better risk-reward analysis.
  - Enhance our risk analytics to work better with the business to optimise returns to the Group.
- 10 Improve Risk Processes**
  - Enhance our credit quality processes including key measures to enhance the monitoring and reporting of credit encompassing Process, People and Systems.
  - Leverage on the new Group Risk structure to provide seamless risk management to the business across the Group.

Please refer to "Basel II Pillar 3 Disclosure" for detailed disclosures on Risk Management.