

# RISK MANAGEMENT

## Management Tools Upgrading at the Global Crisis

Risk management policy is one of the key elements of the corporate governance system.

In 2008 the Bank established an independent structural subdivision – the Risk Management Center, reporting directly to the Management Board. The main objective of this subdivision is risk management and risk minimization to ensure maximum results for the Bank.

Professionals of Ameriabank strive to ensure compliance with the standards of classic risk management, aimed at mitigating not only such financial risks as market or credit risks, but also operational risks. The Bank also pays due attention to creative risk management approaches.

Risk management in Ameriabank is based on the following principles:

- ▶ introduction of a single risk management system,
- ▶ formation of proactive risk management position,
- ▶ performance of operations based on most accurate risk assessment and the principle of ensuring efficiency adequate for the risk,
- ▶ ensuring risk measurability, setting thresholds for transactions and operations, conducting monitoring, etc

## Risk Management during the Crisis

- ▶ Relevant subdivisions of the Bank conduct regular client monitoring to ensure continuous control over the loan portfolio. The monitoring reports are presented at the meetings of the Credit Committee to take appropriate measures to prevent possible defaults.
- ▶ Along with the toughening of lending terms, the requirements for LTV (loan to value) were also reviewed to minimize possible losses of the Bank in case of defaults, even if the price of collateral drops.
- ▶ The Risk Management Center of the Bank conducts regular stress testing for assessment and management of credit risk, foreign exchange and interest rate risk, based on various development scenarios. The Bank Management takes into consideration the results of these tests.

The main tools of credit risk regulation are:

- ▶ regular monitoring of disbursed loans,
- ▶ stress testing of the portfolio quality.
- ▶ To manage interest rate risk, the Bank applies the Duration Gap methodology for assets and liabilities, which renders it possible to balance them by terms. Liquidity risk is managed at the level of the corresponding committee on a weekly and monthly basis, due to which it is possible to predict possible problems in advance.
- ▶ To mitigate foreign exchange risks under the conditions of AMD devaluation and difficulties in projection of the anticipated rate, the Bank conducts a policy of closed currency position, if formation of long or short position is not an extreme necessity.

To assess foreign exchange risk the Bank applies:

- ▶ VaR model,
- ▶ results of stress tests with more pessimistic scenarios.

## Risk Management Methods of the Bank

The following methods are applied by the Bank to ensure management of possible risks:

- ▶ setting internal economic standards and parameters of risk management
- ▶ setting thresholds restricting various operations for the person in charge of the operation and other participants of the process
- ▶ diversifying assets and liabilities
- ▶ conducting regular monitoring of loan investments, which will render it possible to identify potential deterioration of the clients' financial position on timely basis
- ▶ conducting stress tests
- ▶ creating an internal managerial reporting system

Target markets for the Bank are set pursuant to the minimum requirements for credit risk management.

Ameriabank manages market risks applying Stop Loss and VaR limits, instruments mitigating interest rate risks. The Bank also expressly outlines the targets and policy of investment activity, setting limits according to the rating of securities.

The Quality Management System (QMS) is implemented in the Bank in accordance with the ISO 9001:2008 standard, ensuring not functional management, but process management. The Bank strives to ensure the maximum application of control mechanisms in all processes.

The Bank manages internal operational risks through the following tools: documentation of all business processes through internal legal acts regulating said processes, applicable restrictions for all transactions and operations, the "double entry/approval" mechanism employed in any operation of the Bank, a reporting mechanism including types and frequency of reports, etc.

Thanks to the effective performance of relevant structural subdivisions of the Bank and the development of internal risk management standards, which are tougher and more conservative as compared with the standard requirements of the Central Bank of Armenia, in 2008 almost all the risks the Bank was exposed to were mitigated to the minimum.

The Bank has considerable potential for further growth, as evidenced by the data on compliance with economic standards.

**Table. Data on the Main Economic Standards of Ameriabank**

Standard		CBA standard requirement	12/31/07	03/31/08	06/30/08	09/30/08	12/31/08
N <sub>1</sub>	Total capital/risk-weighted assets	12.00	78.78	42.81	38.47	78.55	65.33
N <sub>2</sub> <sup>1</sup>	Highly-liquid assets/total assets	15.00	66.87	38.12	27.86	26.11	20.08
N <sub>2</sub> <sup>2</sup>	Highly-liquid assets/demand liabilities	60.00	172.43	131.76	80.00	116.80	107.83
N <sub>3</sub> <sup>1</sup>	Maximum risk per borrower	20.00	19.15	12.74	17.91	7.82	15.69
N <sub>3</sub> <sup>2</sup>	Maximum risk per large borrowers	500.00	109.71	105.44	188.91	48.55	85.04
N <sub>4</sub> <sup>1</sup>	Maximum risk per Bank-related party	5.00	0.20	0.30	2.64	1.80	0.26
N <sub>4</sub> <sup>2</sup>	Maximum risk per all Bank-related parties	20.00	1.25	2.34	6.57	3.90	2.32

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