



Risks and Opportunities

Event: 1st of December 2009

Panel:

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There's a feeling of anticipation regarding the current economic situation in the USA, in Europe? Have we hit rock bottom yet?

We have not hit rock bottom yet, for banks – in difference to other industries, they experience or feel the crisis later in the cycle. A portfolio may be made up of quite a number of good customers. The quick optic may fool you – but we still see a growing number of jobless and still see unused capacity.

Some customers will run out of money - the consumer debt problem which has been anticipated. Most risk managers are conservative but not pessimistic. In an environment when you don't see the bottom, you should be more worried than when you see it.

Most likely 2010 will show huge credit losses, losses will be high next year and banks will decrease in speed.

What's been the history of risk policy in the CEE?

Banks who invested in CEE countries implemented or applied their risk policies continuously. For a long time we did not see any defaulted clients/customer in that area. Since the crisis we see portfolios which deteriorate, which is a new experience in a lot of CEE countries. We are now faced with the fact to apply instruments (like close monitoring, restructuring, work-out, etc.) e.g. in the credit process, with little experience in CEE banks.

In CEE there is a huge knowledge on risk as well as many educated risk people. Therefore these instruments found a fruitful base for developing measures.



What possible changes of the framework for banks to smooth the negative impact of cyclicality?

How can anti-cyclical regulation reduce risk in the banking system? The Spanish and the Croatian experience

Currently regulation tends to be pro-cyclical. In good times banks have better portfolio quality and may need fewer reserves. Through securitisation they were also able to transfer risk off-balance sheet.

One of the lessons of the current crisis is that regulators should include some anti-cyclical elements into the regulatory setup, forcing banks to slow down, put away reserves in good times and use these reserves in a cyclical downturn. The Spanish and Croatian examples show how it can be done in practical terms

What the requirements and key success factors for developing opportunities in a risk-averse environment?

- Risk adjusted pricing including true risk premiums.
- Creating opportunities based on non risk weighted assets earnings. Capital and further on capital ratios are the limiting factor, therefore into alternative streams need to be looked at.
- Key success factors are flexibility, creativity, a broad product portfolio and willingness to cross sell

What are the challenges in transitioning form an opportunistic banking culture to one tempered by risk?

I think especially the crisis has already led to a more risk sensitive awareness; let me stress one example: years ago when we started performing stress testing for the trading book, risk controller were treated as a manikin from mars, right now managers, regulatory authorities etc. can't get enough from scenarios.

The challenge therefore is to be transparent to put our ideas across the market with the goal to create a win – win situation for both parties.

What concerns are there about changes in the regulatory environment, what regulations will change will arise. Risk managers are not overly optimistic, but just like a patient who is ill needs time to heal and fully recover, so the problems which are already in the books will take time to rebound.



Optimism comes from the real economy when we see increasing salaries and a rise in exports. As soon as exports start, then things will be fine again. To indicate that the economy is on the road to recovery, however, we would need additional signs from the real economy. There are some signs – such as prices which indicate the current risk is better.

What have we learned from the crisis regarding risk management?

Only micro prudential regulation is not sufficient. Each market participant may behave in a logical way and still harm the system as a whole. Separate banks may not take care of the stability of the system, it is the job of the regulator. New methods of macro prudential regulation should be introduced like stress-tests, anti-cyclical regulation, etc. On the level of separate banks maybe the main lessons are that excessive aggressiveness is dangerous and the old good principles of conservative banking still apply.

Can Basel 2 be blamed for a part of current problems in banks?

Basel 2 application in the EU started just prior to the crisis, so it may be said that there is no way to blame these rules for the problems. On the other hand, banks started to prepare for Basel 2 long before and they built their risk management systems accordingly. The excessive attention to Basel 2 distracted banks from issues uncovered by the new rules and created the false feeling that by complying with Basel 2 banks become risk-proof. The weakest point however is probably the excessive use of models.

Comment on the types of opportunities you see in the future markets? What is an opportunity?

It can be said, that an opportunity can be defined as the likelihood of realizing a gain/profit from an allocation or reallocation of resources; realizing an opportunity produces a new risk or is changing existing risks or risk profile.

We should be prepared for opportunities. At the moment the whole world is talking about contingency planning, last will and testament for banks which are in trouble, everything is dominated by negative scenarios; we should more focus on positive scenarios, what are our chances, opportunities etc. in the coming years.



What are the specific risks in the banking sector of CEE?

Risk No.1: Asset Quality.

It will take some time to reach the bottom before the situation starts to improve.

Reasons: falling GDP, growing unemployment, decreased demand on main export markets.

Risk No.2: FX risk related to loans denominated in foreign currencies.

Reason: substantial devaluation of a number of domestic currencies in the region, increased volatility.

What comments do you have when CRO´s are elevated to CEO´s – as has recently been the trend.

CRO´s keep the organization in a disciplined mode. In 10 – 24 months, if you have to stay in survival mode, there is a need for a change, a downscale occurs. The main thought is that not everything is negative - there is quite a difference in perception. Risk managers are taken more seriously; they've voiced some issues and are now in prominent positions.

There are also changes in culture and mindset going on overall in /throughout organizations – thus begins a selective approach where both perspectives of sales and risk are presented on the same page. Risk managers are not the most creative – creativity in finance usually is in arbitrage or in circumventing regulations

To reallocate risk – if this is a major idea, then one need a sales person, but someone who understands risk and can put discipline into an organization. But how to download risk on a balance sheet – requires a profile more of an investment banker and market specialist

How does our panel see the new leader of Risk as an influencer?

- as active partner for the business
- as strategic partner for the managing board
- as creative partner for accounting and controlling
- as challenger for business opportunities



How have outsiders/externals to the bank been affected with regard to risk perception? What people changes have occurred?

Corporations are more careful in planning and are and will issue quite a lot of bonds. Their focus is on a clean balance sheet in terms of liquidity. People are more careful. As a result, many corporations are actually very sound. There is a decrease in the intermediary function of the bank.

In 2010, Banks will turn more optimistic – especially investment banks. Typical universal banks will look for more opportunities and are actively looking for good risk. Stricter standards will readjust to the bigger opportunities in the market but some banks will still be in trouble.

Opportunities will occur in areas such as factoring development, leasing. Before the start of the crisis, sales were in a strong position. Now it is well –balanced in the equation and it is no longer a power play. Instead, risk specialists have added value and a new type of cooperation is now occurring.