

Sustaining growth through ERM

Bank Mandiri partnered Oracle to implement a risk management system to address Basel II requirements and improve capital efficiency

By Foo Boon Ping

Indonesia's largest bank, Bank Mandiri, runs a diverse portfolio of business lines, spanning six business segments: Institutional, Corporate, Treasury, Commercial and Business, Consumer Finance, and Micro and Retail Banking. These segments feature in eight of the bank's subsidiaries: Syariah Mandiri, AXA Mandiri Financial Services, Mandiri Sekuritas, Mandiri Tunas Finance, Bank Sinar Harapan Bali, Mandiri AXA General Insurance, Mandiri International Remittance and Bank Mandiri Europe Ltd.

The bank's management understands the critical need for supporting infrastructure and technology to enhance enterprise value, optimise the bank's risk-return profile and support its decision-making process.

"Risk management proactively supports the bank in achieving a healthy and sustainable growth while maintaining optimal risk-adjusted return," said Bank Mandiri's Chief Risk Officer, Sentot Sentausa.

Its risk management principles and practices follow the enterprise risk management (ERM) approach which was built on four building blocks: organisation and human resources, policies and

procedures, systems and data, and methodology/ models and analytics.

The framework was implemented in an ERM technology system in 2009. The project completed in 2011 and is widely regarded as the first comprehensive ERM project ever implemented in Indonesia.

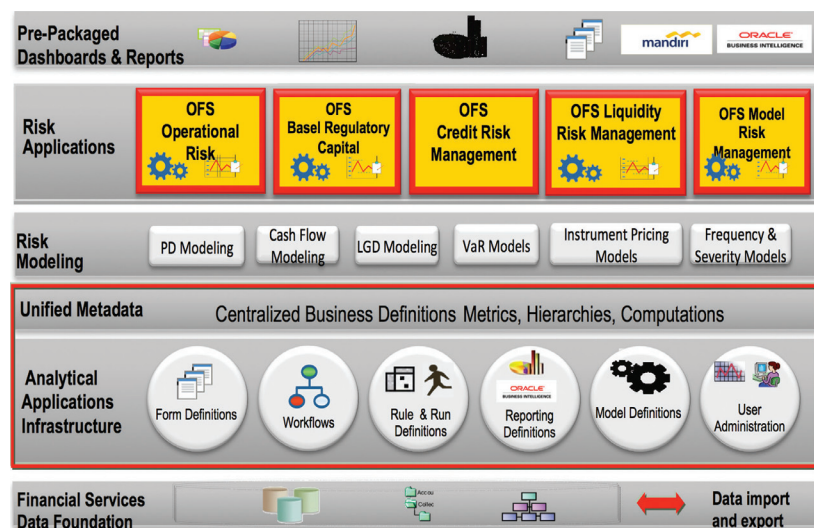
The challenge

The global financial crisis in 2008 provided useful lessons for the bank to significantly improve its risk management infrastructure and capabilities. It sought to create a comprehensive approach to identify, measure, prioritise, manage and monitor the portfolio of business risks impacting business, operations and organisation, and to pursue business opportunities that optimise risk-adjusted return and shareholder value.

This required an effective ERM infrastructure that encompasses an overall risk management policy, a chartered risk committee, an active board of management, clarity of risk management roles and responsibilities, and an enterprise-wide risk assessment process. It also needed integration of risk measurements, risk responses and business plans, a risk-based performance measurement and management, and a value-based management, as well as dashboard and other risk reporting measures.

The bank aims to take an enterprise-wide approach to managing all types of risk

Figure 1. An effective and cost-efficient risk platform that provides Basel II solutions and beyond



Source: Oracle and Bank Mandiri

The solution

The ERM system Bank Mandiri implemented provided it with the capability to move from the old Basel I regime to the more capital efficient Basel II framework. Although Bank Indonesia, the country's regulator, has yet to issue regulations encapsulating the more advanced approach of Basel II, the bank has already armed itself with the capability of calculating its capital charge under this method.

However, regulatory compliance was not the main reason for the implementation. "Aside from regulatory compliance purposes, the ERM system will provide a platform to support the implementation of a risk-adjusted performance management, portfolio management, and capital optimisation," Sentausa explained.

The selected solution, Oracle Financial Services Analytical Applications, provided capabilities for business segment and performance analytics in terms of risk-adjusted returns, which can then be optimised under the risk-adjusted performance management framework (value-based management).

As the ERM project aimed to provide an alignment between business and risk, implementation required coordination and collaboration among the bank's risk, business and IT units. Project management required shared responsibilities between business and risk units and vendor.

The ERM project was the first of its kind to be implemented in Indonesia, so there were no benchmarks available. Therefore the project required various subject matter experts from different units to contribute their knowledge and experience to the implementation.

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Another major hurdle related to availability and access to good quality data. “Some of the biggest challenges of the ERM project involved data availability and quality, as well as changing the mind-set that decision-making should align with risk management,” Sentausa commented.

Bank Mandiri's ERM System implementation aimed to provide the bank with a comprehensive risk technology to support an integrated risk management framework, with a focus on the implementation of the Basel II Accord and a risk-adjusted return framework. The ERM system provides the bank with the capability to calculate and manage capital requirements under Pillar 1 of Basel II as well as under the economic capital framework. The system also provides the bank with risk-adjusted return methods designed as a mechanism to allocate capital and manage its portfolio in a granular manner. It shifted focus from operating on a cost-benefit framework to a risk-reward approach.

With limited resources in ERM technology and complex risk management requirements, the bank decided to procure a customised solution. This approach leveraged the vendor's risk management knowledge and technical expertise from prior implementations.

Its ERM Steering Committee considered several proposals from a number of solution vendors in the area of Basel II and ERM solutions. The bank evaluated their ability to service the product, support end-users, provide product enhancement and customise technology as well as cost of customisation and the location of the vendor's development team (e.g. local partners).

“Oracle Financial Services Software came with a solid, effective and cost-efficient risk platform that provided Basel II solution and beyond. Oracle and its local partner were also very supportive during the implementation process,” said Sentausa.

The benefits

While the ERM system was mainly intended to address regulatory Basel II requirements, the greater benefit came from the improvement in capital efficiency as a result of using a more accurate granular approach.

The implementation of Oracle Financial Services Analytical Applications allowed Bank Mandiri to scrutinise its loan portfolio in more detail based on its risk and performance profile. By doing so, it is able to optimise the portfolio composition, selecting attractive and promising sectors and industries over risky and laggard ones.

“Oracle enables forward-looking institutions like Bank Mandiri to actively manage risk-adjusted performance management on an enterprise-wide basis,” said Sultan Khan, group vice president and general manager, Oracle Financial Services Analytical Applications. “It is excellent that Bank Mandiri is taking a proactive and strategic enterprise-based approach to risk management; and playing a leadership role in the region.”

The system also allows the bank to take an enterprise-wide approach to managing all types of risk. By deploying this solution, the bank is able to compute capital adequacy more effectively, improve capital planning, define its risk appetite and set risk limits.

Bank Mandiri now has the ability to determine how much capital is needed to offset risk across the enterprise, allocate capital across different business lines in an efficient and rational manner, and identify opportunities for diversification and hedging. By establishing risk levels, the bank can define its risk appetite and develop business plans that are closely aligned with corporate strategies and comply with regulatory requirements. **TAB**

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