RISK MANAGEMENT

The Group embraces risk management as an integral part of the Group's business, operations and decision-making process. In ensuring that the Group achieves optimum returns whilst operating within a sound business environment, the risk management team is involved at the early stage of the risk-taking process by providing independent inputs, including credit evaluations, new product assessments, quantification of capital requirements and relevant operational requirements. These inputs enable the business units to assess the risk-vs-reward propositions, thus mitigating the risks whilst enabling residual risk to be priced appropriately in relation to the expected return.

ENTERPRISE RISK MANAGEMENT FRAMEWORK

The Group's risk management approach is supported by a sound and robust Enterprise Risk Management Framework ("Framework"), which is continuously enhanced to remain relevant and resilient against the background of a versatile risk landscape and evolving industry practices. The Framework involves an on-going process of identifying, evaluating, monitoring, managing and reporting significant risks affecting the achievement of the Group's business objectives. It provides the Board and the management with a tool to anticipate and manage both the existing and potential risks, taking into consideration the changing risk profiles as dictated by changes in business and the regulatory environment, the Group's strategies and functional activities throughout the year.

The Framework forms part of the Group culture and is embedded into its business processes and practices. The Framework is targeted towards achieving the Group objectives and is divided into four categories:

GROUP'S OBJECTIVES

STRATEGIC

High-level goals, aligned with and supporting the Group's mission

OPERATIONS

Effective and efficient use of resources

REPORTING & COMPLIANCE

Reliability of reporting and compliance with applicable laws and regulations

FINANCIAL

Profitability and sustainability of performance

RISK MANAGEMENT
(CONTINUED)

RISK MANAGEMENT GOVERNANCE

In line with the Framework, three lines of defence in managing risks are adopted within the Group. The following diagram summarises the responsibility and accountability of the various parties involved in the risk management governance of the Group.

Board of Directors

- sets the overall strategic direction for the Group.
- provides oversight to ensure that the management has an appropriate risk management system and practices to manage risks associated with the Group's operations and activities.
- sets risk appetite and tolerance levels that are consistent with the Group's overall business objectives and desired risk profile.
- reviews and approves all significant risk management policies and risk exposures.

Board Risk Committee ("BRC")

- assists the Board in the development of strategies, policies and infrastructure to manage the Group's risks and ensure that there is effective oversight.

President/ Chief Executive Officer ("CEO")
supported by management committees which address the key risks identified

Management Executive Committee ("MEC")	Asset Liability Committee ("ALCO")

The committees comprised of the management are chaired by the CEO and undertake the following:

- oversight function for overall risk limits and capital allocation, aligning them to the risk appetite set by the Board.
- implementation of policies laid down by the Board and ensuring that there are adequate and effective operational procedures, internal controls and systems to support these policies.

First Line of Defence Business and Support Units	**Second Line of Defence** Risk Management & Compliance Division ("RMD")	**Third Line of Defence** Internal Audit Division ("IAD")
• primary responsibility of identifying, mitigating and managing risks within their lines of business. • ensure day-to-day activities are carried out within the established risk and compliance policies, procedures and limits.	• independently assess risk exposures and the coordination of risk management on an enterprise-wide basis. • ensure that risk management and compliance policies are implemented accordingly. • ensure compliance with the applicable laws and regulations.	• the IAD being the third line of defence is responsible for independently reviewing the adequacy and effectiveness of risk management processes, system of internal controls and conformity with risk and compliance policies.

RISK MANAGEMENT (CONTINUED)

Management has identified and manages the following key risks that could prevent the Group from achieving its objectives as part of its enterprise risk management:

Type of Risk	Definition and Management
Strategic Risk	Strategic risk is the risk of not achieving the Group's corporate strategy and goals. This may be caused by internal factors such as deficiency in performance planning, execution and monitoring as well as external factors such as changes in the market environment. Strategic risk management is addressed by the Board's involvement in the setting of the Group strategic goals. The Board is regularly updated on matters affecting corporate strategy implementation and corporate direction.
Credit Risk	Credit risk is defined as the potential financial loss arising from the failure of a borrower or counterparty to fulfil its financial or contractual obligations. Credit risk within the Group arises from Purchase With Recourse ("PWR") and Purchase Without Recourse ("PWOR") business, mortgage guarantee programmes, investments and treasury hedging activities. The primary objective of credit risk management is to proactively manage credit risk and limits to ensure that all exposures to credit risks are kept within parameters approved by the Board. Investment activities are guided by internal credit policies and guidelines that are approved by the Board. Specific procedures for managing credit risk are determined at the business level based on the risk environment and business goals.
Market Risk	Market risk is defined as the potential loss arising from movements of market prices and rates. Within the Group, market risk exposure is limited to interest/ profit rate risk and foreign exchange risk as the Group does not engage in any equity or commodity trading activities. The Group manages market risk by imposing threshold limits and entering into derivative hedging contracts. The limits are set based on the Group's risk appetite and risk-return considerations. These limits are regularly reviewed and monitored. The Group has an Asset Liability Management System which provides tools such as duration gap analysis, interest/ profit sensitivity analysis and income simulations under different scenarios to assist in managing and monitoring the interest/ profit rate risk. The Group also uses derivative instruments such as interest rate swaps, profit rate swaps, cross currency swaps and Islamic cross currency swaps to manage and hedge its market risk exposure against fluctuations in interest/ profit rates and foreign currency exchange rates.
Liquidity Risk	Liquidity risk arises when the Group does not have sufficient funds to meet its financial obligations as and when they fall due. The Group manages liquidity risk by adhering to a strict match-funding policy whereby all asset purchases are funded by bonds of closely matched size, duration, and are self-sufficient in terms of cash flow. A forward looking liquidity mechanism is in place to promote efficient and effective cash flow management while avoiding excessive concentrations of funding. The Group plans its cash flow and monitors closely every business transaction to ensure that available funds are sufficient to meet business requirements at all times. Reserve liquidity, which comprises of marketable debt securities, is also set aside to meet any unexpected shortfall in cash flow or adverse economic conditions in the financial markets.

RISK MANAGEMENT
(CONTINUED)

Type of Risk	Definition and Management
Operational Risk	Operational risk is the potential loss resulting from inadequate or failed internal processes, people and systems, or from external events. Each business or support unit undertakes self-assessment of its own risk and control environment to identify, assess and manage its operational risks. The Group has established comprehensive internal controls, systems and procedures which are subject to regular reviews by both internal and external auditors. Exposure to operational risk also entails the management of the following risk categories: • Technology Risk: Technology Risk management involves structured and consistent risk assessment pertaining to technology and cyber security risks. The Group has embedded sound governance and effective management of technology risk which encompass strong information technology ("IT") security, reliability, resiliency and recoverability to address technology risk elements such as availability, accuracy, accessibility and agility. • Business Disruption Risk: The Group has a robust Business Continuity Management ("BCM") program to minimise the impact and likelihood of any unexpected disruptions to its business operations through implementation of its BCM framework and policy, business continuity plans and regular BCM testing exercises. The Group has also identified enterprise-wide recovery strategies to expedite business and technology recovery and resumption during catastrophic events.
Reputational Risk	The Group's reputation and image as perceived by clients, investors, regulators and the general public is of utmost importance to the continued growth and success of the Group's businesses and operations. Invariably, reputational risk is dependent on the nature/ model of business, selection of clients and counterparties and reliability and effectiveness of business processes. Stringent screening of potential clients and the design of business practices in accordance with high standards and regulatory compliance have been incorporated to safeguard the Group's business reputation and image.
Shariah Non-Compliance Risk	Risk of legal or regulatory sanctions, financial loss or non-financial implications including reputational damage, which the Group may suffer arising from the failure to comply with the rulings of the Shariah Advisory Council ("SAC") of Bank Negara Malaysia ("BNM") and/ or Securities Commission of Malaysia ("SC") (collectively referred to as SACs), standards on Shariah matters issued by BNM or advice of the Shariah Advisors that are consistent with the rulings of the SACs. The Group consults and obtains endorsements/ clearance from an independent Shariah Advisor for all its Islamic products, transactions and operations to ensure compliance with relevant Shariah requirements. From a regulatory standpoint, the Group does not have direct access to the SACs for Shariah ruling/ advice. Where applicable, the Group will obtain approval of the SACs through the counterparty or intermediary that falls under the purview of BNM, and/ or through the principal adviser of the sukuk programme for submission of its Islamic financial products to SC. Periodic Shariah Compliance Reviews and annual internal audits are performed to verify that Islamic operations conducted by the business units are in compliance with the decisions endorsed by the Shariah Advisor. Any incidences of Shariah non-compliance are reported to the Shariah Advisor, Group Board Audit Committee, BRC and Board.

RISK MANAGEMENT (CONTINUED)

KEY HIGHLIGHTS

In light of the changing business environment, RMD had put in place the following initiatives during the year 2020 to strengthen risk resilience and to support the Group's objectives:

1. Aligning the Group's Portfolio to the Risk Appetite and Strategies

    - The risk appetite is a critical component that enables the Board and management to communicate, understand and assess risks that the Group is willing to accept in pursuit of its strategies. The Risk Appetite Statement is reviewed on an annual basis taking into consideration, all material risks and future business activities as part of the annual Internal Capital Adequacy Assessment Process ("ICAAP").
    - RMD has continuously ensured that business initiatives are aligned with the risk appetite by providing independent assessment and risk input for new and additional credit limits as well as new business proposals. Various assessments and simulations were performed during the year, such as portfolio review conducted to determine vulnerabilities arising from the pandemic, ad-hoc stress tests performed to determine capital adequacy based on various adverse scenarios and portfolio optimisation exercise conducted to determine potential new business volume.
    - Acknowledging the importance of technology risk and to be in line with BNM Risk Management in Technology ("RMiT") requirements, a risk appetite statement relating to technology and cybersecurity was established as a guiding parameter on the acceptable level of IT risk that the Group is willing to accommodate.

2. Enhancing Risk Management Governance, Controls and Processes.

    - Risk management policies, methodologies and processes were continuously enhanced to be in line with industry best practices and regulatory requirements. During the year, various policies and guidelines were reviewed and updated to ensure internal controls and risk management practices remained relevant. RMD had also undertaken an independent review of policies and processes in line with the requirements of BNM's Credit Policy with no major gaps identified.
    - In view of the challenging economic landscape, controls relating to approving limits for investments were tightened, whilst the concentration limits by counterparties rating bands were streamlined to reflect a more effective risk categorisation.
    - In response to technology evolution which requires adoption of new technology vis-à-vis agility to enhance technology capability and capacity to meet the business requirements, Technology Risk Management Framework and Cyber Resilience Framework were developed based on BNM RMiT requirements. These frameworks serve as overarching documents in managing risks pertaining to technology and cyber threats.
    - Seamless business recovery and continuity are imperative to minimise adverse impact to business operations during the pandemic crisis (i.e. COVID-19). The Crisis Management Committee ("CMC") convened several times during this period to deliberate on appropriate business strategies, resources allocation and managing stakeholders' expectation.
    - A digitalised Business Continuity Management ("BCM") mobile application known as MyBCM was developed and installed for all staff to facilitate access to Cagamas' quick reference guide on the Business Continuity Plan, encompassing information on disaster declaration procedures, emergency response actions, key external contacts and contact numbers of all staff to ease the business continuity process.
    - The scope of compliance review was broadened and extended to new areas to ensure adherence to applicable laws and regulatory requirements. Periodic independent assessments were conducted on an on-going basis to identify potential gaps and provide recommendations to address the gaps.

3. Strengthening Risk Culture

    - The Group believes that a strong risk culture is an essential building block for effective risk governance. In order to inculcate the right risk culture for employees at all levels of business and activities within the Group, employees are encouraged to undertake continuous learning and communicate issues on a timely basis.
    - As part of the on-going efforts to elevate the risk and compliance culture, two issues of RMD's newsletter incorporating various risk and compliance issues were published, incorporating activities to create enthusiasm amongst staff. In addition, several workshops on various risk management and compliance topics were conducted for management and staff to create awareness and enhance their understanding of risk and compliance matters.