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BANKS WITH POOR OPERATIONAL RISK MANAGEMENT MAY INCUR SIGNIFICANT LOSSES

Asian banks that have suffered huge losses in the past today take a more serious look at insurance as an integral part of their operational risk management strategy.

JAKARTA, INDONESIA – 19 November, 2008 – Indonesian banks may incur significant losses if they do not focus on operational risk management, and fail to meet regulatory requirements. This was the message that Mr. Halim Alamsyah, Director of Banking Research and Regulation at Bank Indonesia, the country's central bank, drove home to bankers at a recent seminar organised by PT Jardine Lloyd Thompson in Jakarta.

Mr. Halim characterised the recent subprime mortgage crisis in the US that led to the financial meltdown as essentially one due to a lack of proper operational risk management. "Operational risk management was the root cause," he said. "When banks fail to meet lending guidelines, what they take on is an unknown level of risk and loss of confidence in loan data. While there has been considerable focus on Basel II in the past few years, the recent crisis has illustrated that we need to look beyond just meeting regulatory requirements."

Senior risk practitioners from eight banks attended the event, titled "Managing Risks in Turbulent Times - A Holistic Approach to Operational Risk Management". Besides Mr. Halim, regional experts from JLT's financial solutions teams - Shan Sagoo and Rob Russell – elaborated further on the steps that banks needed to take to avoid the kind of operational risk management lapses that have caused banks to suffer significant losses or even fail.

One of the key points raised was the role of insurance in mitigating losses due to fraud and bank-related crime. In the past, many banks across Asia suffered losses due to not having in place a crime insurance policy. Since then, major Asian banks have taken a more serious look at this exposure and now have insurance as an integral part of their operational risk management strategy. A crime insurance policy reduces the financial impact of an operational loss by providing contingent capital in the event of an operational loss. Scenario



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analysis can also play a pivotal role in the identification, quantification and prioritisation of operational risks.

Besides mitigating the financial impact of a catastrophe, robust operational risk management is today seen as critical to confidence in the bank. Halim pointed out that a robust operational risk management framework sends a strong message in two key areas – the ability of the bank to protect its customers' assets and in dissuading fraudulent and criminal activities.

While the benefits of operational risk management cannot be quantifiably measured like market or credit risk, and its value is only appreciated in the event of a catastrophe, considering the reputational damage that a loss can cause, it arguably represents the most important component of a bank's overall risk management framework.

Setia Hadidjaja, Managing Director of PT JLT, said: "The current complexity and turbulence of financial markets have significantly changed risk profiles, making it even more imperative for banks to institute sophisticated risk transfer programmes. The Basel committee on Banking Supervision has identified fraud as one of the greatest sources of potential operational losses. To combat fraud, constant vigilance through a comprehensive set of internal controls, coupled with insurance as a second line of defence is necessary."

Setia added: "JLT has been increasingly involved in arranging operational risk transfer programmes to protect banks in the event of crime-related losses, due mainly to fraud and computer crime. Banks that have incorporated these policies into their operational risk management framework have enjoyed extra protection for both their shareholders and their regulators. PT JLT has the ground specialist team in respect of other financial professional products such as Bankers Blanket Bond, Directors & Officers Liability, Professional Indemnity, Mortgage Indemnity, Credit Card, etc."

About Jardine Lloyd Thompson (JLT) Asia's Financial Solutions Team

JLT Asia established its focus on the Asian financial institutions sector in 1989 and has since built up extensive market knowledge as well as strong relationships with insurers and market regulators. Our team of senior brokers are widely experienced in the design, negotiation and



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implementation of sophisticated insurance programmes. We have a strong track record in providing creative solutions for premier banks, stockbrokers, fund managers, investment advisers, venture capital firms and stock exchanges across the region.

About PT Jardine Lloyd Thompson

PT Jardine Lloyd Thompson (JLT) has been operating in Indonesia since 1976, specialising in the insurance and risk management requirements of corporate clients. We are the first foreign joint venture insurance broker to establish operations in the country. Our industry specialisations include aviation, communications & technology, construction, employee benefits, energy & industry risks, financial solutions, marine cargo, mining and pharmaceuticals.

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