Bangkok Bank recognizes that effective risk management is fundamental to good banking practice. Accordingly, the Bank has established guidelines for managing risk in each area of its business to ensure that it has effective risk management mechanisms in place. Over the past few years, the Bank has continuously analyzed major risk factors which could affect its financial operations, revised its organizational structure and improved its processes for managing relevant risks. This is to ensure that its risk management system will be in line with international standards and be in accordance with the principles of Basel II.

The Bank’s Risk Management Committee plays a significant role in prescribing the risk management policy, reviewing the sufficiency of the risk management policy and systems, defining the strategy for risk management, and monitoring the Bank’s risk to an appropriate level, in compliance with the Bank’s risk management policy which has been approved by the Board of Directors based on the Risk Management Committee’s recommendation. The objectives are to manage the relevant risks within designated parameters, including the maintenance of capital in accordance with the revised capital adequacy requirements under the Basel II rules which have been in effect from the end of 2008, and the management of business to achieve an appropriate rate of return.

The important processes in the risk management system comprise the identification of significant risks which may potentially impact the Bank’s business operations, the assessment of each type of risk, the monitoring of risks to an appropriate level under the Bank’s policy, and the reporting of the status of each type of risk to relevant parties so as to enable them to manage and/or handle the risks in a timely manner.

Major risks that may affect the operations of the Bank include credit risk, market risk, liquidity risk, capital adequacy risk and operational risk. The Bank’s guidelines for the management of each type of risks are as follows.

**Credit Risk Management**

Credit Risk is the risk that the borrower may be unable or unwilling to repay the debt owed to the Bank, or to honor other contractual commitments.

**Credit Risk Factors** are those which may affect the ability of borrowers to fully repay loans and include factors which may affect the Bank’s ability to resolve non-performing loans.

A primary risk factor is the global economic crisis which has had a significant adverse impact on the demand for export goods in some industries. Consequently, a number of
companies in those industries have had to reduce their production capacity and to downsize their workforce. This has led to increased unemployment and decreased purchasing power in Thailand. The Bank therefore needs to closely monitor the industries affected by the crisis.

With the significant increase in downside risk as mentioned, the Bank has anticipated potential problems which may arise in 2009, and has therefore prescribed various measures focusing on greater precaution and close monitoring of loans extended to various industries which have been or are likely to be affected.

**Credit Risk Management**  In managing credit risk, the Bank has clearly specified the processes for credit approval which include the formulation of credit policy, the credit risk rating for customers, and the establishment of different levels of delegation of authority for credit approval depending upon the type of business and/or the size of the credit line. In considering the approval of loans in general, the Bank considers the purpose of the loan and assesses the repayment ability of the applicant, taking into account the applicant’s operating cash flows, business feasibility and the capability of management, as well as collateral coverage. The Bank also performs credit reviews which include reviewing credit risk rating levels on a regular basis.

The Bank has therefore set up the following units to monitor and manage the relevant risks.

- **Risk Management Unit** – This unit is responsible for analyzing and reporting to management on the status of risks in various areas of the Bank as well as providing recommendations for the review of the overall risk policy of the Bank in anticipation of, and in compliance with, new rules, regulations and international standards. The unit is also responsible for monitoring the management of each type of risk to comply with the Bank’s risk management policy.

- **Credit Management Unit** – This unit is independent from other business units of the organization. The unit is responsible for managing risks related to credit extension by supervising and monitoring credit extensions in accordance with the Bank’s credit policies. The Credit Management Unit comprises the Credit Policy Unit, the Credit Acceptance Unit, the Portfolio Management Unit, the Risk Asset Review Unit, the Special Asset Management Unit, the Loan Recovery and Legal Unit, and the Bank Property Unit. The functions of each unit are summarized below.

  - **Credit Policy Unit** oversees the credit policy framework and coordinates the improvement and adjustment of the credit policy. It is also responsible for disseminating the credit policy, credit standards and credit processes; for monitoring and overseeing exceptional cases which are inconsistent with the credit policy; and for gathering various inputs which
may be used for improving the credit policy.

- **Credit Acceptance Unit** oversees the quality of credit extensions to ensure they are in line with the credit policy and credit underwriting standards, reviews the appropriateness of loan structures as well as the results of customers’ credit risk ratings, promotes the development of a good credit culture, and maintains a systematic and reliable credit extension process.

- **Portfolio Management Unit** is responsible for analyzing and making recommendations for adjustments to the portfolio structure, recommending the appropriate portfolio composition and the provision of reserves for losses at the portfolio level, developing and overseeing credit risk management tools and methodologies, constructing credit databases and overseeing related management standards.

- **Risk Asset Review Unit** is charged with reviewing credit quality and credit management processes, assessing the adequacy of loan loss reserves, and evaluating compliance with credit policy, regulations and credit underwriting standards.

- **Special Asset Management Unit** is responsible for managing non-performing loans, and for determining and executing strategies for the resolution and restructuring of troubled loans.

- **Loan Recovery and Legal Unit** is responsible for taking legal actions, negotiating loan settlements, or seizing collateral for sale by public auction.

- **Bank Property Unit** is responsible for managing and selling foreclosed assets obtained from loan recovery processes and from legal actions.

**Market Risk Management**

Market Risk is the risk that arises from fluctuations in interest rates, exchange rates and the prices of instruments used in the money and capital markets, all of which may affect the financial performance of the Bank.

**Interest Rate Risk** The rate of interest is a major factor in determining the Bank’s interest income from assets and interest expenses on liabilities. The Bank is exposed to interest rate risk as interest rates for its assets and liabilities may be adjusted at different times, or assets and liabilities may be subject to different contractual maturities, or movements of the benchmark interest rates on assets and liabilities may be inconsistent with one another, thus having impact on the Bank’s net interest income.

**Interest Rate Risk Factors** Major interest rate risk factors include the monetary policy adopted by the Bank of Thailand to maintain the balance between economic growth and pricing stability, as well as to maintain interest rates at an appropriate level in light of the global economic situation, particularly the current US sub-prime mortgage and structured-product crisis and the significant reduction of the Federal Funds rate by the US Federal Reserve which may have a significant impact on financial markets worldwide. Furthermore, competition among banks for market share, especially with regard to deposits which are the Bank’s primary source of funding and credit extensions, may narrow the spread between deposit and lending interest rates which would affect the Bank’s net interest income.

**Foreign Exchange Rate Risk** Foreign exchange rate risk may arise when the Bank makes transactions in foreign currencies which may lead to an overbought or oversold position in a particular currency. These transactions include foreign currency exchange, investments, loans, borrowings, contractual commitments, and the use of financial derivatives in foreign currencies. The Bank may incur gains or losses as a result of movements in exchange rates.

**Foreign Exchange Rate Risk Factors** Foreign exchange rate risk factors include the increasing volatility of foreign exchange rates as a result of imbalances in global trade, and the trend towards depreciation of the US dollar against Asian currencies, due partly to the reduction in US interest rates to avoid or alleviate the economic slowdown caused by the sub-prime mortgage and structured-product crisis.

**Market Risk Management** The Bank aims to manage market risks to a level which is deemed appropriate, acceptable, and in compliance with the overall risk management policy of the Bank. In general, the Bank’s policy is to match assets and
liabilities denominated in both Baht and foreign currencies. In the case of mismatches, the Bank will typically hedge the exposures in various ways, for example by engaging in foreign currency and interest rate swaps, forward contracts, or using derivative instruments to hedge against interest rate and/or exchange rate risks. The Board of Executive Directors approves the appropriate limit for foreign currency positions within the risk appetite as determined by the Risk Management Committee and the Board of Directors, while the Asset and Liability Management Committee, the Treasury Division and the Market Risk Unit are responsible for monitoring, managing and making recommendations for enhancing the policy and monitoring references as appropriate, given the prevailing market conditions.

Asset and Liability Management Committee (ALCO) is responsible for establishing guidelines for the management of assets and liabilities. ALCO is also responsible for monitoring and managing interest rate risks at an acceptable level with minimal fluctuations, and in compliance with the policies set by the Risk Management Committee and the Board of Directors. ALCO operates with support from the Market Risk Unit, a working unit under the Risk Management Unit, which is responsible for identifying, assessing, monitoring, reporting and controlling the Bank’s market risk.

 Treasury Division manages and controls day-to-day trading of foreign currencies and manages the Bank’s liquidity portfolio in line with the Bank’s policy. The Treasury Division’s activities are monitored by the Market Risk Unit to determine whether the risks taken are in line with the relevant monitoring references. The Market Risk Unit reports to ALCO which in turn reviews the appropriateness of the overall position and the limits of the monitoring references on a regular basis. In addition, the Bank may enter into interest rate and currency derivative transactions with the purpose of managing the Bank’s position against imbalances in interest rate and foreign exchange positions, or of providing limited derivative services to certain selected major corporate customers and/or large domestic and international financial institutions. Such financial derivatives include foreign exchange forward transactions as well as currency rate and interest rate swaps.

Liquidity Risk Management
Liquidity Risk is the risk that the Bank may not be able to meet cash flow obligations within a stipulated timeframe. The purpose of the Bank’s liquidity risk management is to maintain suitable and sufficient funds to meet present and future liquidity obligations while managing the use of the funds to generate an appropriate return in light of prevailing market conditions.

Liquidity Risk Factors
Liquidity risk factors include the structure of the sources and uses of funds, the competition among commercial banks for a larger market share in deposits, the political situation and domestic unrest, the fluctuation of the Baht, and government policies which may affect capital movements in and out of Thailand. Other factors include the overseas money markets conditions, particularly in markets affected by the worldwide financial crisis, which may consequently affect the bank’s liquidity in foreign currency denominations.

Liquidity Risk Management
The Bank manages its liquidity risk by diversifying the sources of funds. Liquidity management is done through domestic money and capital markets including swap and repurchase markets, and through international money and capital markets in such currencies as US dollar and Euro. The Bank seeks to minimize its liquidity costs and risks in line with market conditions by closely managing its
liquidity position on a short-term and long-term basis, as well as exercising due care in using short-term and medium-term borrowings from overseas to fund foreign currency loans extended to domestic and overseas customers. The Bank also considers raising long-term funding as market conditions permit.

**Capital Adequacy Risk Management**

Capital Adequacy Risk is the risk that the Bank may not have sufficient capital reserves to operate its business or to absorb unexpected losses arising from credit, market and operational risks.

**Capital Adequacy Risk Factors** Commercial banks in Thailand are required to comply with the Bank of Thailand's Basel II rules for capital adequacy starting from the end of 2008. The framework has established new risk weightings for different types of assets, and imposes minimum capital requirements for market risks and operational risks, all of which have had a direct impact on the bank's capital adequacy ratio and the provisioning for doubtful accounts. The Bank began to prepare to comply with the framework in 2007 and was able to submit a report on quarterly capital adequacy under the Basel II framework in parallel with its report under the Basel I framework on schedule in 2008. The Bank has sufficient capital to cover the risk assets in full and is prepared to submit the monthly capital adequacy report as required by the notification on capital adequacy requirements effective as from December 31, 2008.

**Capital Adequacy Risk Management** The objective of the Bank’s capital management policy is to maintain an adequate level of capital to support growth strategies under an acceptable risk framework, and to meet regulatory requirements and market expectations. Any proposal to raise additional capital is required to be presented to the Board of Executive Directors and the Board of Directors for ultimate approval by shareholders. In addition, the Bank regularly assesses and calculates its capital position under various scenarios for the purpose of capital planning and management so that capital remains at the level suitable for the business conditions.
Operational Risk Management

Operational Risk is the risk of loss from failed or inadequate internal processes, people and systems or from external events. This includes legal risks, but does not include strategic risks and reputational risks.

Operational Risk Factors Significant operational risk factors include the following.

Internal factors
- Factors related to the efficiency of internal processes and internal control systems, including operational processes supporting business operations and processes for taking care of personnel.
- Factors related to personnel, including appropriate staffing levels, staff qualifications and efficiency.
- Factors related to the operating systems of the Bank, including the capability to support business operations, the complexity of systems which may cause risks, the issue of data security, the accuracy of data processing, and the development of and changes in technologies.

External factors
- Factors outside the Bank’s control including actions by outsiders such as theft or embezzlement of assets or data, and catastrophic or natural disasters that damage the Bank’s assets.

The Bank understands that good operational risk management is vital to long-term and sustainable business success, particularly in the current environment of increasing uncertainty, both domestic and international, including economic factors where the global economy is currently in recession, political factors, terrorism, natural disasters and pandemics. The Bank therefore places great importance on effective operational risk management with sufficient coverage of all aspects of operations in order to be able to deal promptly with any event, and to ensure sustainable stability of the organization.

Operational Risk Management The Bank’s operational risk management includes defining, assessing, monitoring, mitigating and controlling risk. Every unit in the Bank is directly responsible for managing its operational risk and for establishing measures to mitigate and control risk to the designated level by allocating appropriate resources and establishing an organizational culture for managing operational risk.

A key principle underlying the Bank’s operational risk management is to educate staff throughout the organization by providing them with a consistent understanding of operational risks, so that they are able to accurately and completely identify the operational risks, assess the significance of each potential risk, analyze details to find appropriate solutions to mitigate risks, and implement the selected solutions to minimize risks. This is followed by the systematic monitoring of progress, and the measurement of potential risk, as well as regular reviews of the entire process.

The Bank has set up a dedicated unit for operational risk management under its Risk Management Unit which has taken steps to enhance its operational risk management system to be in line with international standards. This includes establishing a clear definition of operational risks, educating staff with consistent knowledge and understanding of risk throughout the organization, and involving every unit in managing operational risk at the unit level. The Operational Risk Unit is also responsible for managing operational risk at organization level, preparing for the calculation of the capital required for operational risk in line with the Basel II framework, the maintenance of a data loss database arising from operational risk, the groundwork for the development of business continuity management and the preparation of business continuity plans.

The Bank has taken various initiatives to manage its operational risk in accordance with international best practices. The Bank is prepared to comply with all three principles of the Basel II framework, namely readiness in maintaining capital adequacy to cover operational risk, readiness in establishing a good risk management system by implementing processes for managing operational risk throughout the organization, and readiness in terms of information to support concerned parties in assessing the risks surrounding the Bank.

In addition to preparing to manage operational risk within the organization, the Bank will also make preparation for managing operational risk across the Bangkok Bank Group.

The Bank will continue to monitor and develop its operational risk management systems so they remain appropriate in light of future changes in the environment from both internal and external factors, in order to maintain its status as a leading bank at national and regional levels.