Mary C Nkosi: Risk based supervision in Malawi

Speech by Mrs Mary C Nkosi, Deputy Governor of the Reserve Bank of Malawi, at the official launch of risk based supervision, Blantyre, 9 January 2009.

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The General Manager, Reserve Bank of Malawi;
The Chairman of Bankers Association of Malawi;
Board Members of various banks;
Chief Executives of banks and members of management;
External Auditors;
Representative of the Institute of Internal Auditors;
Representative of Society of Accountants;
The Executive Directors - Supervision of Financial Institutions; Corporate Services and Support Services, RBM
Heads of Department from Reserve Bank of Malawi;
Officers of Bank Supervision and Supervision of Non Bank Financial Institutions;
Members of the Press;
Ladies and Gentlemen.

Accept my warm welcome to this epic occasion and moment in the history of both the Reserve Bank of Malawi and the act of supervision and regulation of the banking industry in Malawi. The Reserve Bank of Malawi changes its mode of supervision from the traditional CAMEL based approach to Risk Based Supervision (RBS).

Such changes the world over, have always been clearly marked and remembered as major occasions. Authorities such as the Federal Reserve System of the USA and Financial Services Authority of the United Kingdom where much literature and practice on the subject may be drawn had to change at one point in order to improve the way supervision is conducted. The Reserve Bank of Malawi views this course in the same vein: Change to make improvements in risk management in banks and supervision of the same by the regulators.

Risk based supervision entails change of culture in one way or the other because certain things, like risk management can only be done that way now. I will emphasise a few changes that are expected of banks in order to yield and realize full benefits of the Risk Based Supervision initiative.

Firstly, the role of the board has been clarified and expectations heightened to an extent that the board can not be a peripheral figure of banks any more. Through the Risk Management Guidelines, the RBM calls for active board oversight in policy and strategy formulation, review and ensuring that management executes its responsibility or is held accountable.

Secondly, the governance structure should not impede proper risk management and reporting. Where this is the case, it should be addressed as a matter of urgency and priority.

Thirdly, all risks affecting the bank should be addressed by policy, (not just major and traditional financial risks) so that no single risk is over looked. Some of you will recall that one of the major findings of the RBS survey which the Reserve Bank conducted back in 2007 was apparent neglect of non financial risks. In the modern world of hi-tech and globalisation, transferability of risk across jurisdictions and the interrelationship between risks is very high. Worse still, across the boarder qualitative information about reputation, compliance or impact of quantitative financial risk matters more than the actual financial risk itself which may actually be addressed. Therefore, it is imperative that due attention should be given to at least nine risks identified in the Risk Management Guidelines namely, Strategic, Credit, Liquidity, Interest Rate, Foreign Exchange Rate, Price, Operational, Compliance and Reputation risks.

Fourthly, banks have to take stock of their resources to meet the requirement to identify, measure, monitor and control risk. Where there are bottlenecks, board members and management present here are requested to make investments in training and some Management Information Systems possibly. I may not be very wrong to submit that the size of the bottom line is not the only performance target in the long run. I am also reliably advised that the overall cost implications of such sacrifices are affordable across our banks.

Ladies and gentlemen, the Reserve Bank of Malawi is not spared of the need to re-look at its culture either. One such eminent change is that Bank Supervision Department will be restructured along portfolio lines such that all faces you know or just hear of on the phone or through e-mail will visit banks in an on site inspection. This was not the case before, when we had distinct on-site and off-site divisions.

So many good things have been sung about RBS already by the previous speakers. However, let me add two more. These are:

Firstly, RBS challenges and allows banks to demonstrate that they can assume more risk as long as it is managed to the satisfaction of the bank itself as determined by the Board and its policies. Of course, other eyes like risk management, internal audit and regulators as interested groups will have an independent opinion on the activities and quality of risk management.

Secondly, in RBS both banks and supervisors sit on the same side of the fence as far as risk is concerned, except that supervisors retain their assurance mandate. This gives supervisors better insight into what management is doing about inherent risk.

Ladies and gentlemen, my call to you therefore is let us do our job! As you are aware Enron, Adelphia, WorldCom, Société Générale and Barings Bank, to name but a few represent massive corporate failure resulting in untold damage to employees, investors, creditors and economies; but who is to blame? For sure, no one can claim to be doing their job and be ignorant of fraud or more precisely risk in the same line. Therefore, Directors, CEOs, Auditors, Risk Managers and Supervisors, let us do our job.

Consequences, of laxity in risk management can not be explained more than the recent financial crisis resulting in collapse of Bear Stearns, Indy Mac Bank and Lehman Brothers in the USA. While state intervention for Northern Rock, Fannie Mae, Freddie Mac and Citi Group just emphasise the cost of ineffective regulation and lack of capacity to fully understand risk being undertaken by the bank itself. We must have learnt lessons from these developments and we should not be scared to handle our challenges.

On its part, the Reserve Bank remains committed to its legal mandate which includes ensuring a safe and sound financial system knowing fully well how critical the banking system is in the development agenda of the country.

Lastly, on behalf of the Reserve Bank of Malawi, allow me to register our profound appreciation and recognize the contribution of the IMF East Africa Regional Technical Assistance Centre (IMF East AFRITAC). The centre sponsored the technical assistance of Carmencita Santos, the lead consultant on RBS to Malawi as well as Mackay Aomu and Peter Phelan who also worked with us at some stage of the project.

The Reserve Bank also appreciates the support and cooperation of banks in honouring and anchoring critical stages of the project. In addition, but not least though, there was a team of Reserve Bank officers who tirelessly worked on the project to its conclusion. It has been a job well done.

With these few remarks ladies and gentlemen, it is my singular honour and pleasure to officially launch Risk Based Supervision in Malawi!

Thank you for your attention.