Credit Risk

A practitioner's point of view

Vienna, 02. February 2001

IBM Unternehmensberatung GmbH

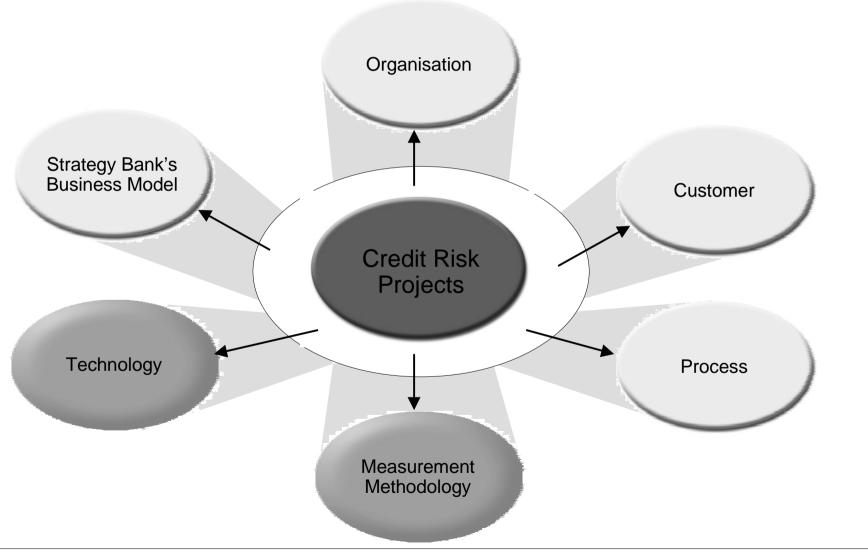
Dr. Rainer Fuhrmann (Practice Leader Trading & Risk)

Agenda

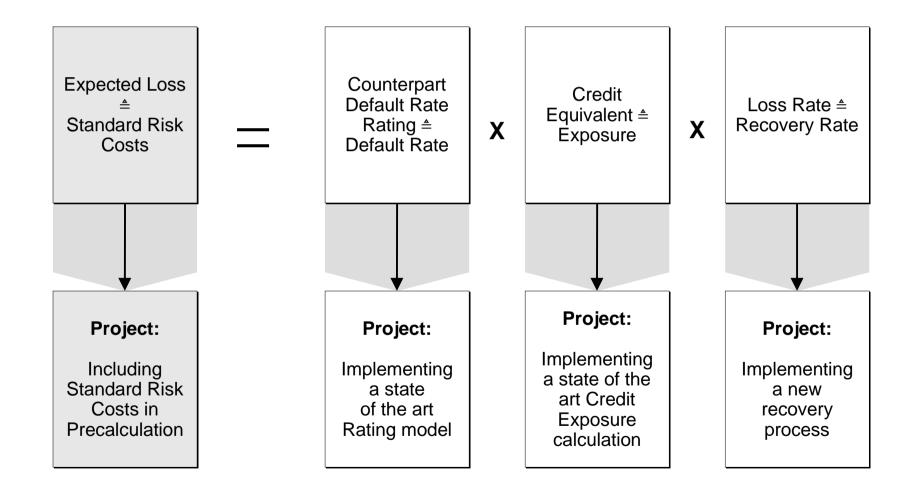
- 1 Impact and types of Credit Risk Projects
- 2 Impact examples
- 3 Critical Success Factors

1 Impact and types of Credit Risk Projects

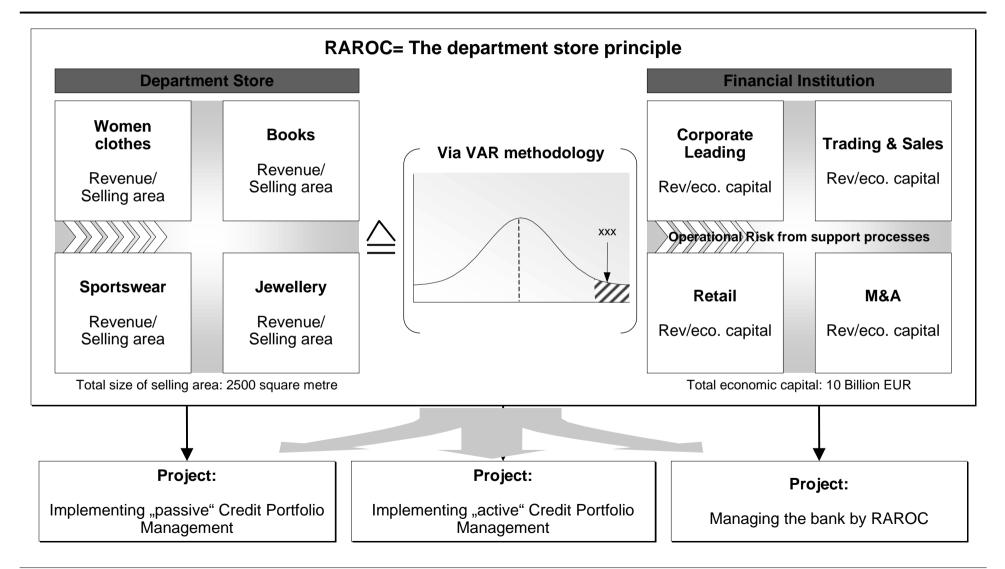
Successful implementation of credit risk projects has wide ranging impacts on the bank.



The following categories of Credit Risk Projects can be derived from the Expected Loss formula.



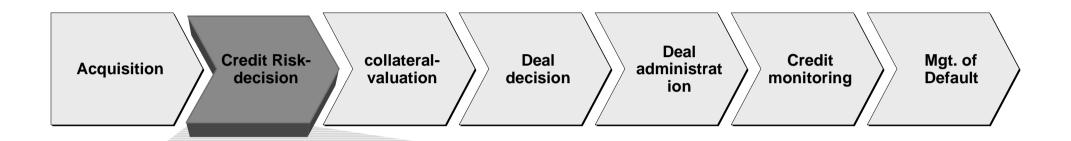
The following categories of Credit Risk Projects can be derived from Unexpected Loss.

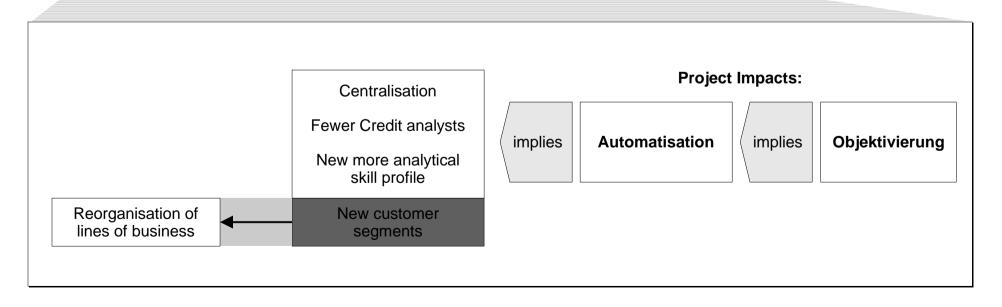


2 Impact Examples

- 2.1 Rating
- **2.2** Exposure
- 2.3 Recovery Rate
- **2.4** Credit Portfolio Management

Impact Example: Rating project may have major impacts on organisation and processes.



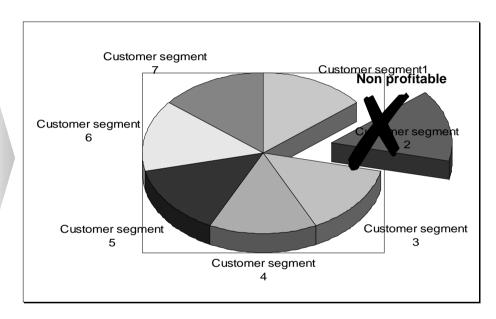


Impact Example: Rating project may have major impacts on organisation and customers.

| New Rating | | |
|------------|------------------------|--|
| Rating | Default Probability | |
| 1 | 0,01% | |
| | | |
| 6 | 1,1% | |
| | | |
| 12 | 100,0% | |



Including Standard Risk Costs in Precalculation



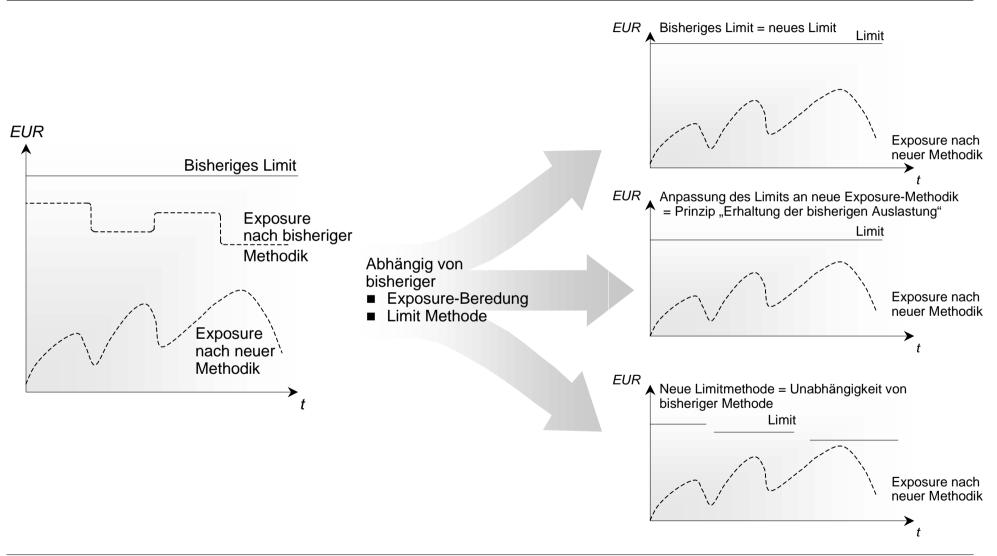
Business with particular customer segments will be stopped.

Sales staff redundancies

2 Impact Examples

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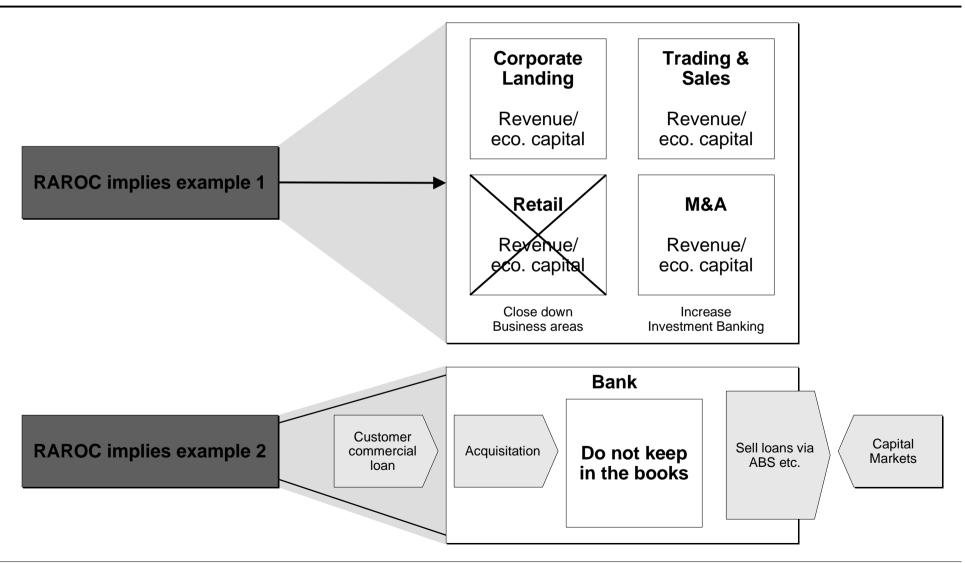
Changing credit exposure calculation methods have impacts on the limit attributed to the customer. So it will affect the business with the customer.



2 Impact Examples

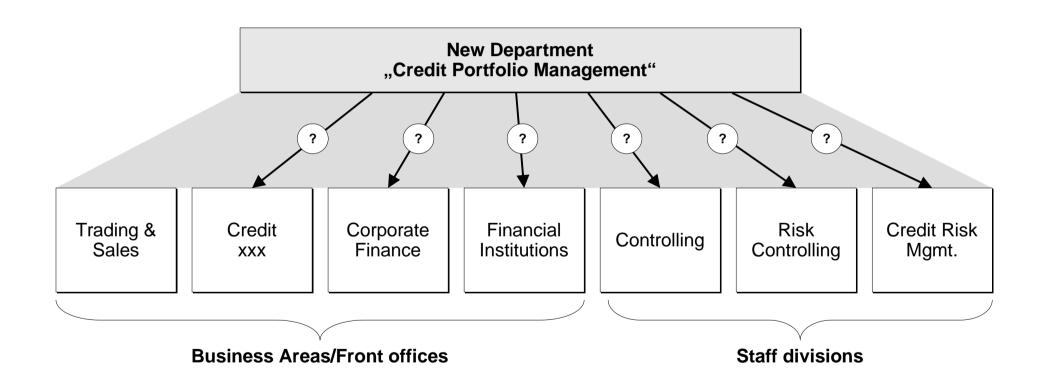
- 2.1 Rating
- **2.2** Exposure
- 2.3 Recovery Rate
- **2.4** Credit Portfolio Management

Impact Example: Credit portfolio management projects may have major impacts on business strategy.



Impact Example: Credit portfolio management projects may have major impacts on organisation.

Where to put the new department?



Impact Example: Credit portfolio management projects may have major impacts on customer relationships.

"Active"
Credit Portfolio
Management

- Replacing descrete "Yes/No" Decision with continuous pricing when granting loan.
- Replacing limits by pricing

Customers have to get used to

- no longer getting limits, even though still necessary for their internal financial planning
- changing backoffice counterparties

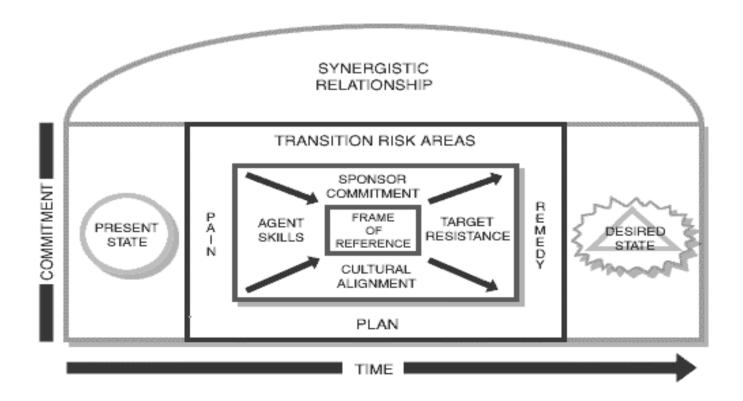
3 Critical Success Factors

At the end of the day, successful change of the credit risk measurement methods means business transformation. Therefore a business transformation approach must be adopted.

| Assess | Plan | Design | Implement |
|--|--|---|---|
| Transformation Management Change Readiness Assessment. Enterprise Capabilities Capability Model Capability Scenarios Organisation Current Organisation Assessment Financial Financial Assessment | Financial Financial Benchmarks Financial Workplan and Model Transition Management Organisation Job Roles, Responsibilities and Competencies | Transition Management Transition Strategy Risk Analysis Financial Business Case Organisation Future Organisation Scope and Requirements | Transition ■ Integrated Transition Plan |

The Transition Management Framework positions the bank for successful change by addressing variables such as: commitment, time, and relationships.

One major reason that projects fail is that the executive team often does not understand or agree upon their roles and responsibilities in leading change.



Credit risk projects will fail, if the business transformation scope is underestimated.

The following are eight critical success factors for the transition management strategy

