

Credit Risk Management

Robust practices in managing credit quality

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Covid-19 and geopolitical tensions have undoubtedly brought a lot of challenges to the banking industry, especially to the business and credit environments. Executives from the Hong Kong Monetary Authority (“HKMA”) have shared in various occasions credit risk management has been and will always be one of the key regulatory focuses, with consideration of an appropriate balance between credit risk management and supporting the community. We are seeing an increasing trend of regulatory reviews and actions taken on banks in relation to credit management systems and internal controls by the HKMA.

It is imperative for banks to ensure sound credit risk management systems and internal controls are in place to cover risk assumed, even under the new ways of working. Here are some good practices identified from recent reviews conducted by KPMG.

Independent reviews

- Regular compliance review
- Regular assessment by internal audit
- Leverage of RegTech solutions in managing reviews and remedial actions

Governance

- Clear terms of reference for board and management committees
- Ongoing review of lending strategies
- Proper segregation of duties and authority delegation
- Clear accountability and disciplinary measures
- Sufficient resources and training on regulatory expectations

Classification and provisioning

- Timely update for accuracy of borrower and facility information
- Avoidance of over-reliance on collateral and days past due in determining loan classification



Policies and procedures

- Robust regulatory change management framework and periodic update of policies & procedures
- Criteria for assets acceptable as collaterals
- Maintenance of approved list of, and periodic assessment of external valuers

Post-lending Monitoring

- Ongoing assessment of effectiveness of limit setting and monitoring
- Robust processes to follow up of overdue credit reviews
- Monitoring of pre- and post-drawdown covenants

Pre-lending assessment and approval

- Pre-lending due diligence considering industry outlook, cash flow under stressed scenario and use of loan commensurate with business plan and repayment ability
- Critical independent assessment and robust documentation of assumptions in credit appraisals
- Avoidance of over-reliance on collateral or guarantee in credit approvals

How banks should react

Whether to prepare for upcoming regulatory activities or be ahead of the game to better manage credit portfolio in this everchanging credit environment, banks should consider taking the following actions.



Have a **complete understanding of regulatory expectations**



Assess appropriateness of existing governance structure, policies and procedures, processes and internal controls in addressing today's regulatory expectations and challenges in managing credit quality



Re-assess quality of existing credit portfolio and whether any action is required to address any credit quality concern, e.g. re-evaluation of collateral, re-classification, provisioning



(1) Re-visit roles and responsibilities of teams and individuals involved in lending processes and credit risk management and (2) ensure adequate training of regulatory requirements and expectations is provided to relevant staff



Assess appropriateness of existing technologies in managing credit quality, especially under the new ways of working

How KPMG can help

To support you in your journey of better monitoring credit quality, apart from providing assistance in relation to credit risk models, we are delighted to offer support in any of the abovementioned actions, including but not limited to,

-  Conducting a **sharing session** with you in relation to relevant regulatory requirements and expectations and assisting in **identifying any knowledge gap**
-  Benchmarking existing credit risk management tools, technologies, models, policies, processes and reporting to **industry better practices**
-  Assisting you in **understanding current gaps of compliance** with regulatory expectations, quality of your **credit portfolio** and the **remedial actions** required to meet regulatory expectations and in lieu of Covid-19
-  Assessing your **current status of resources** devoted to managing credit quality, e.g. human resources, technologies, and **sharing market practices and recommendations**
-  Identifying opportunities of **enhancing current lending processes and credit risk management** through use of **RegTech solutions**

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