

## PROBLEMS AND PROSPECTS OF DEVELOPMENT OF RISK MANAGEMENT IN THE SECOND-TIER BANKS OF KAZAKHSTAN

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The introduction of the risk management system is important from the standpoint of the efficiency of the bank, bank's reputation, and decrease in losses from realization of the bank resources. The article discusses the current issues on risk management in the banking sector. Furthermore, credit risk in the banking field was identified and recommendations for quality enhancement of risk management were given.

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The purpose of efficient risk management in banking activities is formed by divisions of risk management. In most meaningful procedure is considered to be a quantitative risk assessment and its bounding volumes. The problem of the banks is to choose portfolio of their clients which has an acceptable balance between active and passive operations, and also maintain the sufficient level of liquidity and profitability which is necessary for the smooth operation level.

The purpose of risk management is to ensure the existence and further development by detecting, analyzing and minimizing risks.

Bank crisis revealed significant drawbacks in risk management. Some banks do not properly built risk management system and also could not provide independence for this function. Top managers also could not properly respond for warnings and occurred problems from risk managers.

In crisis situations, one of the main tasks of bank manager are how quickly and accurately they can controls and eliminate the growth of bad debts of the banking sector and take appropriate action.

According to consultant B. Zhiger from the Institute for Economic Strategies – Central Asia, “crisis scenarios in the banking system include: volatility in oil price; decline in property price; redistribution of property, entry of foreign banks and the post-IPO risk” [1].

Prudential standards contributed decline in credit risks by taking into account the credit risk and maximum risk for per borrower, also including affiliates or insiders. These requirements are provided in the Regulations “On normative values and methods of calculation of prudential standards for second-tier banks”, September 30, 2005 № 358 as amended on 08.27.2014, the [2].

A risk manager, who is responsible for the management and coordination of risk, needs to examine at the proper level the specificity of the Bank's businesses and materials regarding general risk trends. The main responsibilities of risk managers is to provide risk management func-

tions with clear and meaningful information and sizes to what is necessary to ensure that: a continuous stream of information about the risks; control of correctness; interaction interest of the structural unit; monitoring of risks in the bank's activities; verification process performance measures for compliance with the requirements of risks; the use of approved risk assessments, models and prerequisites; promotion and implementation of elements of internal controls.

Risk managers in financial services are required to support structural units daily, while have been holding their interaction should be described in the specific rules, regulations and instructions. In addition, the position of risk managers in banks needs to be held by highly qualified specialists who are familiar with the individual banking products and services, and also operation in the banking business (in general).

The Basel 3 is the basic document according to the whole process of risk management in banks exists and evaluates. This document will undoubtedly contribute to the incentives for risk managers and the extent of the cost to implement and improve the process of risk management in banks.

Risk management is important and closely interrelated elements of banking supervision and regulation. In accordance with the decision of the National Bank of Kazakhstan on February 26, 2014 № 29 “On Approval of the Regulations for the formation of risk management and internal control for second-tier banks” banks should create a sufficient concept of risk management and internal control which considers the use of bank risk control methods that provide effective identify, analyze and reduce the risks of the bank based on the type and size of their operations [3].

Currently, all banks have a personal system of risk management, namely, risk management system, which brings together all kinds of databases for each individual type of risk. At the same time, banks also seek to implement the methodology of personal risk assessment and on the basis of the effective solutions to top-managers of the bank.

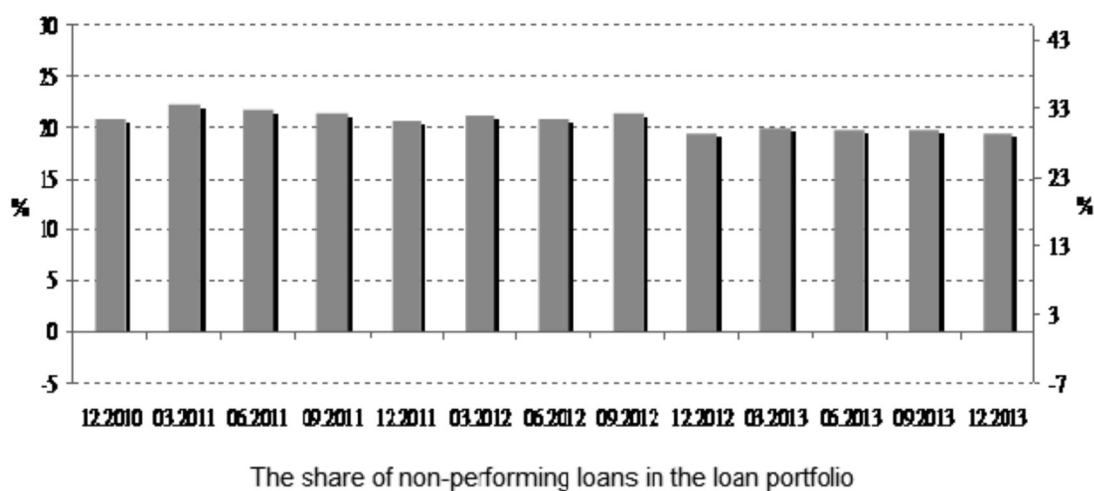


Fig. 1. Non-performing loans of banks RK for 2012–2013

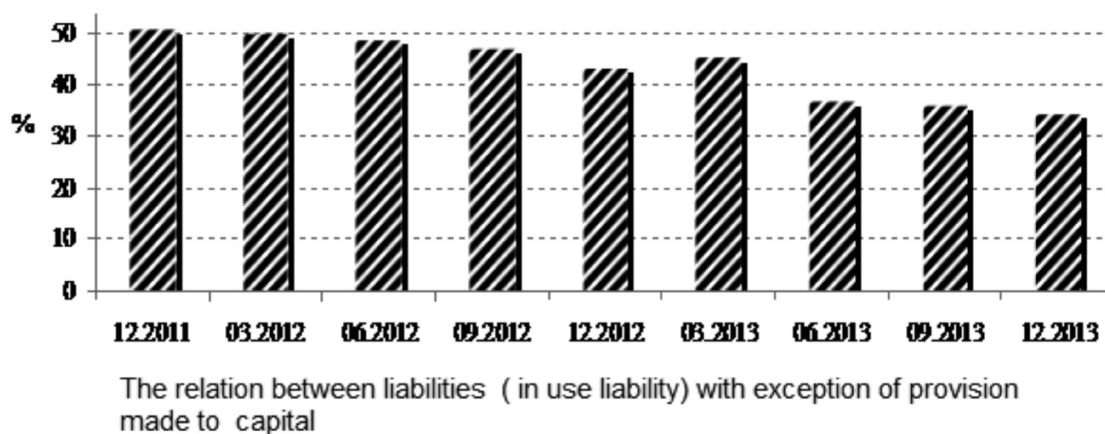


Fig. 2. The ratio of non-performing loans (net of provisions) of banks of Kazakhstan (to the total regulatory capital for 2012–2013)

In general, the procedure of risk management in banks must meet the requirements of corporate governance practices in the conduct of operations with different financial instruments, practice, asset and liability management, as well as the operating conditions to ensure the bank's work.

The concept of risk management makes it possible to obtain a quantitative assessment of the risks of banking activities and find a respective compensation for risk and also acceptable size (reserve) to cover potential losses.

The provision provides a more stable environment bank financial activities and avoids vibrations profit margins associated with writing off losses on credit [4].

The current state of risk management indicates a sufficient difference in the level of im-

plementation of risk management systems in banks. In particular, the larger the pot, the better the implemented risk management system. It shows the possibilities of ready-made software products created both in Kazakhstan and in foreign countries, where the most recommendations are taken into account according to Basel 3 capital adequacy. Furthermore, the big banks established special unit, an activity that was aimed at the management of the various risks, such as credit risk management is carried out by the Department of troubled loans, acting separately from the Risk Management Department. Accordingly, with such narrow specialized techniques used in the management of one or another risk, they received more thorough development and implementation. At the same time, medium and medium-sized banks have

a chance to establish a multi-purpose system of risk management and learn more regarding complex risks faced by the bank, and, consequently, higher effectiveness of the risk management system.

Consequently, the role of risk management in the banking sector is expressed as a function of the methods used and tested methods and systematization skills which affect the interest of the state. This involves the fact that the effective activity depends largely on banks welfare of the people and the economy.

Credit risk is one of the key risks of the banking sector in Kazakhstan. The qualities of loans in recent years are an important source of uncertainty analysis of the prospects and for development in both at the level of individual banks and the entire banking system of Kazakhstan. Banks have to decide on a number of difficult problems. In most of them are undeniable – a high degree of problem assets, as evidenced by the increase in the growth of non-performing loans from 7.4% in 2012 to 14.8% in 2013 (fig. 1) [4].

It should be noted that the increase in coverage of idle reserves portfolio in 2013 reflects the revaluation of a portfolio and decrease the reliability of collateral. Height compliance provisions for non-performing loans, accrued in accordance with IFRS, with 57.4% on 31.12.2012 to 65.6% as of 31.12.2013 that had a positive impact on reducing the proportion of non-performing loans in the total regulatory capital from 43.2% to 34.4% over this period (fig. 2).

The main objectives of the risk management for any bank is facilitating decision-making process – namely, to ensure the ratio of these decisions with the strategic objectives of the bank, lowering the costs of the various ongoing operations and increase profitability of the banking business.

In general, the course of risk management and the formation of methods of analysis of financial risks is an undisputed fact that the concept of an effective risk management system is not enough to entrust the function of analysis and control of risk on a single structural unit of the Bank and to provide for this software conforms with the exact installation. Procedures for the identification and analysis of risks should be integrated with virtually all processes of the bank [6].

The risk management strategy of Kazakh banks are an integral part of the audit report of the consolidated financial statements, which are prepared in accordance with IFRS and the NBK and should include analysis and justification of having a bank risk management systems. The review of results of the audit report shows that not all banks have an adequate

risk management system. Therefore, NBK is working, and aimed at motivating those banks that implement the risk management system in accordance with international standards of banking.

The predominant role of the banking sector in the financial system cannot be underestimated. So, it needs to carefully assess the financial stability of banks which a whole depends on the stability of the entire financial system. Therefore, first of all, an analysis of possible risks of the financial system should start with an analysis of the financial stability of the banking sector.

The purpose of risk management in banks is a complex sequential basis for the assessment and disclosure of risks, definition of tools for analysis and systematization, development of programs recommendations for their prevention, and the use of these programs.

In order to enhance the quality of risk management and improvement of corporate governance in banks need to reconsider the problem of the exact distribution of duties and responsibilities of the bank's management. Also needs to establish procedures for the timely interaction between its divisions and ensure the availability of an effective system of adoption of the conclusions on the performance of activities. Particularly, increasing importance and responsibility of the Board of Directors of the Bank for monitoring. Management of risks associated with the operations of the bank's various derivative financial instruments. Also requires revising the definition of more practical requirements in setting limits on possible risks associated with the operations of the bank in the financial market, the modernization of procedures, the use of bank stress-testing and planning of basic capital sufficient. Also taking risks that arise in the normal course of operations, as provisioning in the event of unexpected losses in order to maintain solvency at the set time, which helps to improve the efficiency of work due to profitable operations with regard to the relevant "risk-return" and provide additional help in making effective decisions.

The system of risk management and internal control systems should be improved mechanisms for prevention of money laundering and financing of terrorism (AML / CFT), and is subject to revision policy of rewards and incentives to banks to increase transparency and to ensure effective monitoring. Furthermore, this policy should be assessed as a necessary part of the analysis of financial stability and the determination of its inconsistency degree of stability risks inherent in the bank.

Compliance with the law is considered an important tool using which the bank may have to protect themselves from the risk of

being involved in money laundering and terrorist financing. In this case, the main purpose of the risk – oriented approach is to optimize the performance of the functions of labor costs for financial monitoring without harming the quality of the work performed in the field of AML / CFT. Practical action in recent time shows convincingly that the financial institution, which is unable and unwilling to carry out activities of internal control for AML / CFT, is uncompetitive in the international market.

The quality and effectiveness of risk management and general management should be based on ensuring the availability of effective decision-making procedures. It allows the authorized body to make appropriate decisions, have an unlimited list of information materials as the positive outcome of this decision, and the likely risks. Such decision-making procedure implies involvement in the course of the preparation of information and discussion of all divisions of the bank. The main attention

should be paid to increase the responsibility and the establishment of requirements for the competence of managers and employees of departments of risk management, as well as the government banks.

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