



Andrej Hronec, Head of Assets and Liabilities

## VUB manages risk by looking into the future

### Industry

Banking

### Business Issue

Improve asset and liability management, manage interest rate risk.

### Solution

SAS® for Enterprise Risk Management

### Benefits

VUB Bank can now more accurately predict the future structure of assets and liabilities; optimize cash flow to calculate interest rate risk with greater accuracy; and use various scenarios to predict the impact of future developments.

Thanks to SAS® analytical software for risk management, Slovakia's VUB Bank better optimizes its liquidity, manages interest rate risk and makes decisions while considering both current and future scenarios.

The global financial crisis has highlighted the two major vulnerabilities of worldwide banks: the threat of insufficient liquidity and the risk of banks' earnings being excessively dependent on interest rate fluctuations. Regardless of a bank's overall health, not incorporating strong analytical practices around asset and liability management (including interest rate risk) can negatively affect revenues and possibly lead to its collapse.

In recent years, VUB has become a risk management pioneer in Slovakia. The bank has always had a well-managed loan portfolio, resulting in minimal costs to cover credit risks. Its practices translated into strong profitability, and VUB received the "Bank of the Year" award from the weekly economic journal *Trend*.

### Higher aspirations

VUB managers are constantly trying to move risk management practices to a higher level. Naturally, the characteristics of liquidity and interest rate risk have always been closely monitored. However, VUB is now constantly seeking ways to refine its ratio analysis and calculations, which was not a priority in the past. "We wanted to look not only at the current risks, but to also have a view on what they could look like in the

future," explains Andrej Hronec, Head of Assets and Liabilities at VUB Bank.

It's extremely important for large banks to have the ability to predict future scenarios, as it's difficult to quickly change course and go in a new direction. Therefore, seeing future obstacles and assessing various influences as soon as possible are critical when developing forecasts. "A robust tool is needed," notes Hronec.

VUB, after many years of experience with SAS analytical software, decided to deploy SAS for Enterprise Risk Management. The primary incentive (for implementing SAS) was so that risk managers could generate forecasts to optimize liquidity. "Thanks to our new look into the future, we can better decide whether to gather financial resources for five or 10 years," explains Hronec. In other words, the bank can make better decisions about what level of cash (liquidity) it should keep/acquire. For example, VUB can now predict what the structure of its assets and liabilities will look like in six months, or in two years.

### Looking into the future

A look into the future not only helps VUB make decisions about its appropriate liquidity cushion, it also allows it to forecast net interest income. "Thanks to this [capability] we know our level of assets and liabilities – whether there will be a profit or a loss," says Hronec.

Simulations of new business gains, such as an increase in deposits and loans or

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what future interest rates may be, help managers estimate the development of the bank’s net interest income. These are particularly important forecasts since interest income forms the largest part of a bank’s earnings.

Of course, there’s always an inherent risk in predicting the future, especially for long-term forecasts. Plus, there can always be some event that no one expected. However, Hronec thinks it’s essential that the bank identifies as many different scenarios as possible, which will enable VUB to better adapt to the future. “Sophisticated tools increase the accuracy of predictions as they can analyze a number of factors and scenarios that would otherwise have not been taken into account. The bigger a bank is, the more diverse its products, and

thus the more difficult it is to manage risk,” notes Hronec, who feels that there is a growing need for sophisticated risk management tools.

For example, VUB has used future scenarios when deciding on bond purchases. “If we did not have this view, we would have not bought them in such a structure as what we finally decided,” he notes.

#### **Stability for clients**

Addressing risk management does not produce visible benefits to banking clients. However, managing risk allows the bank to ensure that client deposits are safe – which is particularly important for businesses since they do not have the same deposit protection as ordinary citizens.

Because it’s hard for banking clients to see the benefits of risk management – and difficult to prove the return on investment – banks may think it’s not necessary to use an enterprise risk management solution. However, Hronec notes that after his experience using SAS, he feels that the sooner a bank deploys a sophisticated risk management solution the better, because it brings new insights that help to make better decisions.

VUB is planning to use SAS to model future scenarios and manage risks in its subsidiaries – VUB Leasing and Consumer Finance Holding. In addition, VUB managers plan to use SAS for hedge accounting (accounting of derivatives under international accounting standards).



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