

CBE Risk Appetite Statement

1. Introduction

The Central Bank of Egypt (CBE) is an independent supervisory body, has a public legal personality and enjoys technical, financial and administrative independence, and acts as consultant on draft laws and regulations related to CBE field of work and CBE works in accordance with the authorities and powers vested therein by Law No. 194 for 2020.

The Central Bank aims at the integrity of the monetary and banking system and price stability within the framework of the general economic policy of the state. The Bank undertakes all the necessary competencies to achieve its objectives, which include setting and implementing monetary policy, setting and implementing the foreign exchange rate system and policy, regulating and controlling the foreign exchange market, developing a policy for managing risks in the banking system and its implementation. The Central Bank also takes the means to ensure the achievement of its objectives and the advancement of its functions, which include carrying out any tasks or taking any measures required for the application of monetary, credit and banking policies.

This statement considers the most significant risks to which the CBE may be exposed to and provides a general approach to managing those risks. All strategic and business plans for functional areas must be consistent with this statement.

2. Risk Governance

Governance of risk management consist of three basic elements where are; overall responsibility, managing bank's day-to-day operations and activities and systems. In order to achieve a consistent approach that is applied to all sectors / departments across CBE, the overall responsibility for managing these risks lies on the bank's senior management. As for managing the risks related to Day-to-day risk operations & activities relies within the responsibilities of sectors / departments / units and employees. To enhance the Consistency of this approach, a common methodology has been adopted which is developed and coordinated by Risk Management and Information Security Sector which, among other tools and practices, prepares reports that includes detailed data about risks and regulatory recommendations for them in order to follow up their implementation by all related departments across bank's sectors / departments. In addition to preparing a summarized high-level report to Senior Management / other Sub-Risk Committees, Audit Committee and Board of Directors.

Within the context of the Bank's overall governance structure, the bank's Board of Director "BOD" is responsible for ensuring the independent management of risks to which the bank may be exposed, including Operational Risk and Information Security, and for ensuring the periodic review and compliance of the Bank's activities with policies and procedures.

3. General Statement of Appetite

In context of fulfilling the responsibilities entrusted to the Central Bank of Egypt as a supervisory and regulator, which implies facing a broad range of risks resulting from its responsibilities aiming at the safety of the monetary and banking system and price stability within the framework of the state's general economic policy, as well as its day-to-day operational activities.

CBE fully recognize that the more complex the operations of the bank are, the more likely it will be exposed to specific risk events that may affect its reputation. In this regard, Risk Management & Information Security Sector in CBE has a robust framework that includes structured processes which reduce the probability of risks being realized and its severity to an acceptable level that have been determined according to CBE's approved Risk Appetite according to Risk type.

Generally, CBE has a low appetite for risk. The Bank will allocate needed resources to control these risks to acceptable levels.

4. The Risk Management Framework

CBE Risk Management depends on basic principles to achieve an appropriate balance between risk and return; these principles are implemented within a framework that comprises both qualitative elements, such as policies and procedures, and quantitative elements, such as risk metrics and credit limits. The Risk management framework is flexible enough to cover the CBE's current activities and also what may evolve in the future.

The board of director (BOD), the Senior Management and the relevant committees of the CBE is responsible authority for determining the risk appetite and risk tolerance across CBE sectors / departments; along with their optimal allocation. CBE sectors/departments are accountable and responsible for all the risks that they may face within the scope of their work; in addition to mitigating these risks by applying the appropriate procedures and controls, the Risk Management and Information Security Sector is responsible for ensuring that there is an effective process in place to manage risks across the Bank.

Adopting Transparency and disclosure principles, through providing the CBE's senior management, BOD, Audit Committee and relevant executive committees (Credit Committee - Operational Risk Committee - Crisis Management and Business Continuity Program Committee - Information Systems Steering Committee) with periodical reports of existing and potential risks along with the recommendations of Risk Management and Information Security Sector for corrective actions to be implemented.

5. Coverage areas of Risk

The Bank's attitude towards its key Strategic, Financial, Operational risks, Business Continuity and Information Security is described below.

5.1 Strategic Risks

Strategic risks relate to factors that could prevent the Bank from fulfilling its mission, particularly achieving bank's objectives that was set out in its Strategic Plan. Strategic risks can arise due to a wide range of internal and external factors

The Bank has a low appetite for threats that may affect its effort in achieving its purposes and objectives effectively and efficiently and has a zero appetite for reputation risk.

CBE has a framework in place that ensures that all of its initiatives towards achieving its desired objectives are well set and prioritized appropriately, and the associated risks are well managed and reported on a consistent basis through its committees (Monetary Policy Committee/ Investment and Capital Markets and Banking Reform Committee/ Audit Committee) and these committees submit their recommendations to the BOD for review and approval.

5.2 Financial Risks

The bank has a low appetite for financial risk. The Bank is exposed to various financial risks types including; Credit Risk, Credit Risk Monitoring, Market risk, Liquidity Risk or those associated with Operational Risk.

- **Credit Risk:** Credit risk is defined as the losses arising if a counterparty (obligor/bank) to the Central Bank of Egypt (CBE) fails to meet a financial obligation for full or partial value on due date.

In this regard, the Credit Risk Department conducts sovereign risk analysis, along with comprehensive quantitative and qualitative analysis for the CBE counterparties, to establish Credit limits additionally; Credit risk department follows up and studies the solvency of non-bank international securities traders that the CBE deals with. To establish credit limits, the Credit Risk Department conducts the appropriate assessment for countries and financial institutions; including country risk (political, economic, fiscal and banking sectors) and bank quantitative and qualitative analysis, taking into consideration the CBE Obligor Risk Rating (ORR). CBE counterparties are assigned an ORR according to their lowest rating grade given by the 3 big international rating agencies (Fitch/Moody's/ Standard & Poor's) Furthermore the Credit Risk Department continuously monitors the developments that may have an impact on CBE Counterparties and/or the countries where they are headquartered to identify any potential any potential risk to the CBE and initiate the appropriate action (whenever needed).

- **Credit Risk Administration & Monitoring:** It is the absence of Following up and monitoring of Credit risks' exposures on the CBE's financial statements which can result in financial losses to the bank. In this regard, credit administration and monitoring department works to maintain the efficiency of credit administration, measurement and monitoring process and ensures

adequate controls over credit risk. The department operates according to the best international practices within Enterprise Risk Management Framework, that assures adequate monitoring and reporting, along with ensuring that appropriate corrective actions are implemented.

Credit Limits shapes CBE's risk appetite when dealing with financial institutions. The concerned Sectors/Departments of the CBE are informed of these limits to be adhered to during their dealings with financial institutions.

In this regard, Credit Administration and Monitoring Department validates that all needed approvals for the limits are granted by Credit Committee according to its quorum in light of CBE's Credit Risk Policy, and that all limits are within maximum allowable exposure per counterparty set by CBE's Investment Guidelines. Moreover, the department continuously monitors the utilization of the authorized limits by concerned Sectors/Departments, reports any breaches of the limits to Sub-Governor & Assistant Sub-Governor of Risk Management and Information Security Sector and concerned Sectors/Departments, and follow up on the implementation of needed corrective actions / controls. Also, the department continuously monitors that all trade transactions are executed through Authorized International Banks/Non-Banks Securities Traders.

In addition, the department monitors the developments of CBE investments in Capital Shares of IFIs, Associates and Subsidiaries, along with developments of CBE initiatives to support the Egyptian Economy, making sure both are properly reflected on CBE's financial statements.

- **Market Risks:** it is the risk of losses in financial position (on and off-balance-sheet positions) arising from movements in market prices, which aims to ensure compliance of the CBE concerned departments/sectors with the Investment Guidelines approved by the CBE's Investment and capital markets Committee. The Department's main roles are to identify potential risks through advanced financial analysis tools that are generated from the decisions of Basel Committee on monitoring market risks to take escalatory actions in accordance with the approved reporting matrix to highlight those risks, in order to minimize any potential losses or costs resulting from movements in the global or local markets and to maintain the level of foreign exchange reserves.

The Market Risk Department monitors the risks of interest rates through the approved investment limits for the payback period, which measures the sensitivity of investment portfolios to the change in the market rate of return, and thus the impact of this on the value of the portfolios and their profit and loss rate.

In addition to monitoring investment criteria, concentration risks, currency allocation, and exposure to assets associated with investments in international reserves, in accordance with approved investment determinants.

In this regard, the CBE adopts a conservative investment guideline, investing only in high-quality, low-risk financial instruments that must be rated by at least two out of the three big international rating agencies and the least of them is being chosen.

▪ **Liquidity Risk:**

Liquidity risk arises from the bank's inability to finance any increase in assets or offset liabilities as they become due without incurring unacceptable losses, or from restrictions on the bank's disposal of some of the assets it owns, or the ability to do so but at prices significantly less than their acquisition value (i.e. incurring capital losses) this is to ensure that the investment is made using highly liquid instruments.

CBE must be able to meet its obligations in the financial markets. In addition, the Bank needs to maintain sufficient high-quality liquidity as well as maintain maximum utilization with counterparties as per the CBE investment guidelines approved by the CBE's Investment and Capital Markets Committee.

5.3 Operational Risks

▪ **Operational Risk**

Operational risk is the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events, this definition includes legal risk, but excludes strategic and reputational risk.

The implementation of Operational Risk Management Framework shall be coordinated by a dedicated and independent team under Risk Management and Information Security Sector, which is called Operational Risk Management (ORM) in order to achieve excellence in operational efficiency and effectiveness and to ensure compatibility with best market practice in cooperation and coordination with all CBE various sectors/department.

Operational risk includes those risks related to technology, information Security, fraud risk, legal risk, material risks, absence of business continuity, non-compliance with the Code of Conduct and Compliance.

The bank has a low appetite for Operational Risk, the framework of operational risk management includes a set of tools and practices according to the decisions of the Basel Committee & the latest applications and international standards, which are used to identify, assess, measure, mitigate, monitor and report operational risks and incidents in addition, follow-up the implementation of recommendations and controls related to operational incidents and submit the necessary reports in this regard.

▪ **Fraud and Corruption**

The Bank has no appetite for any dishonest or fraudulent behavior and is committed to deterring and preventing such behavior. It takes a very serious approach to cases, or suspected cases, of fraud or corruption perpetrated by its staff, and responds fully and fairly in accordance with provisions of the Code of Conduct.

▪ **Project Risk**

Project risks are the uncertain events or conditions which, if occurred, may have a positive or negative impact on project objectives/activities which aims to ensure the optimal utilization of available resources by coordinating, organizing various project activities, prioritizing them and the associated risks to support and achieve the objectives of the CBE using best practices and highest quality standards. Therefore, Project Risk Management is an integral part of the daily activities and procedures of projects in order to identify and assess risks, set priorities, propose solutions and establish proactive regulatory controls and corrective measures and follow up on the implementation of these controls and measures to reduce the risks, improve project outcomes and provide project owners with necessary information to effectively manage project resources.

The work scope of the Department includes identifying risks according to the project's nature that may have an impact either financially, operationally, technically, then analyzing and/or addressing risks that affect the project through:

- Reviewing the project objectives, framework and timeline.
- Setting performance measures in accordance with the objectives and strategic plan, as well as precautionary measures to deal with uncertainty project risks.

▪ **People and Culture Risks**

It includes the risks related to the competency of the bank's employees related to culture and awareness includes:

- **Caliber of People:** The Bank relies on motivated, diverse and high-quality staff to perform its functions. The bank aims to create an environment where staff are supported & empowered to the full extent of their abilities.
- **Conduct of People:** The Bank expects staff to conduct themselves with a high degree of integrity, to respectfully strive for excellence in the work they perform and the outcomes they achieve, and to promote the public interest. The appetite for behaviors which do not meet these standards is very low. The Bank deals with any breaches of its Code of Conduct very seriously.

- **Work Health & Safety (WHS):** The Bank is committed to creating a safe working environment for all of its staff, where people are protected from physical or psychological harm. It has a very low appetite for practices or behaviors that could be expected to lead to staff being harmed while at work.

5.4 Business Continuity

Business Continuity Management System “BCMS” has been established, within the framework of Business Continuity Management Policy according to ISO international standard 22301, that shall be evaluated periodically through the Business Continuity Plan of the Central Bank of Egypt (BCP), where periodic tests are conducted to ensure the effectiveness and efficiency of the plan, this BCM system aims to identify the CBE's critical activities provided to banks, government, and economic authorities to maintain / ensure the continuity of all related systems (RTGS, SWIFT payments, international reserves management, open market operations and any related activities) in order to preserve, ensure the continuity of all operations and activities of the Central Bank, as well as achieving the desired objectives of the Central Bank of Egypt under any abnormal circumstances, whereby the Bank’s ability to face crises, protect its employees and continue to perform its activities/services is measured in order to meet its obligations whether locally or globally and maintain its reputation.

5.5 Information Security

CBE seeks to provide and meet the security requirements necessary to protect confidentiality, integrity and availability of its information assets according to the relevant standards, laws, and regulations in order to ensure a safe working environment that supports achieving the CBE goals, in line with the country-wide objectives and sustainable development.

The Bank has a low appetite to Information Security Risk, and accordingly, Information Security Department works to lay the foundations of "Information Security Governance” that sets an integrated strategy to preserve the security of the CBE's information assets, promotes the awareness and effective coordination between all the CBE sectors and departments through applying best practices (For example, but not limited to: (ISO27K - NIST)) and in line with the general framework of cyber security issued by the Central Bank of Egypt and Continuously improve the information security policies and procedures to ensure that they are applied effectively across all departments.

Information Security department reports to CBE's Senior Management all related updates in order to ensure achieving and maintaining the CBE information security.

6. Implementation & Publishment

All Heads of Divisions / Departments are responsible for the implementation of, and compliance with this Statement.

The CBE Risk Appetite Statement is being published on the Bank's website.

7. Review

This CBE Risk Appetite Statement is reviewed annually, or whenever there is a significant change in the Bank's work environment and/or when force majeure event takes place, this review is coordinated by the Risk Management and Information Security Sector. Changes to the Risk Appetite Statement must be approved by CBE Senior Management and BOD.