

**YANGON UNIVERSITY OF ECONOMICS  
DEPARTMENT OF COMMERCE  
MASTER OF BANKING AND FINANCE PROGRAMME**

**EFFECT OF RISK MANAGEMENT PRACTICES ON  
FINANCIAL PERFORMANCE IN MYANMA ECONOMIC BANK**

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FINANCIAL PERFORMANCE IN MYANMA ECONOMIC BANK**

**A thesis submitted as a partial fulfillment towards the requirements  
for the degree of Master of Banking and Finance (MBF)**

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## **ABSTRACT**

This study is focused on the effect of risk management practices on the financial performance of Myanmar Economic Bank. The main objectives of this study are to identify and to examine the effect of the risk management practice on financial performance of Myanmar Economic Bank. This study is used by Descriptive Method and the primary data are collected by personal interview with the responsible person of Myanmar Economic Bank. Secondary data are obtained from the financial statements of Myanmar Economic Bank of the last five years for the period from 2013 to 2018. This study found that Myanmar Economic Bank has effectively managed their risk management practices since 2016 when State- Owned Bank reform started. This study revealed that Myanmar Economic Bank has highly liquid assets and limitations of lending activities. It is needed to encourage more lending for short-term and long-term borrowings based on their excess of deposits. As a result of analysis on financial performance of Myanmar Economic Bank, profitability of Myanmar Economic Bank is not strongly satisfied as expected. Myanmar Economic Bank needs to create new products and services review for getting profit with effective operational risk management practices. Myanmar Economic Bank should review on the varieties and bank needs skillful risk management analyst in long-run.

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## LIST OF ABBREVIATIONS

|      |                                  |
|------|----------------------------------|
| BOD  | Board of Director                |
| CBM  | Central Bank of Myanmar          |
| CAR  | Capital Adequacy Ratio           |
| IMF  | International Monetary Fund      |
| LDR  | Loan to Deposit Ratio            |
| MEB  | Myanma Economic Bank             |
| MOPF | Ministry of Planning and Finance |
| NPL  | Non- Performing Loan             |
| ROA` | Return on asset (ROA)            |
| SOB  | State –Owned Bank                |

# **CHAPTER I**

## **INTRODUCTION**

Bank means in general is taking deposits and lending money. Different kinds of bank include in the banking sector, namely such as public banks, state-owned banks, private banks, semi-government banks, cooperative banks, agricultural bank, etc. The state-owned banks in the country do not only provide commercial banking, but also participate in governmental financial performance and pilot banks in the regulatory changing process. Thus, the status of financial performance of the state-owned bank is supporting the financial sector improvement of the country.

Banking sector in any economy is performing the major role in the country. A well-established and managed banking sector can be absorbed major financial crisis in the economy and can be provided a platform for strengthening the economic system of the country. The bank financial performance is vitally important for all stakeholders, such as the owners, the investors, the debtors, the creditors, and the depositors, the managers of banks, the regulators and the government. The Financial performance of the bank is in the process of measuring the results of an organization policies and operations in terms of monetary value. These results are reflected in the bank's profitability, liquidity or leverage. Evaluating the financial performance of a bank allows decision-makers to judge the results of Bank strategies and activities of the bank. Thus, the evaluation of financial performance of a bank is a key factor of risk management practice in a bank. It is support to identify risks and to make preparation for risk management process.

Myanma Economic Bank is one of the state-owned banks in Myanmar and it provides not only commercial banking but also development banking to assist financial sector development in Myanmar. The role of the Myanma Economic Bank plays three main roles such as providing retail banking with the largest network in Myanmar, developmental financing Institution, supporting Governmental function and Central Bank of Myanmar function. Therefore, financial performance of the Myanma Economic Bank is essential for improving the effective financial sector development in Myanmar and the measurement of the risk management of the Myanma Economic Bank is a crucial role for getting effective financial performance . The complexity of the function of the Myanma Economic Bank is very difficult to

identify the risk management process. It needs to identify the effectiveness risk management practice in Myanmar Economic Bank and to examine the effect of risk management practice on financial performance in Myanmar Economic Bank for reforming state-owned bank in Myanmar.

## **1.1 Rationale of the study**

Myanmar Economic Bank, the largest state-owned bank in Myanmar, provides banking services to support Government sectors accordingly. In 2012, the Myanmar government bunched banking sector reform to build an open, modern and inclusive financial system. It is also related to include regulatory changes in the Central Bank of Myanmar and Ministry of Planning and Finance. According to the related regulatory laws in Myanmar changes on the Myanmar banks, private banks and state-owned banks in Myanmar are playing in level play field. Thus, Myanmar Economic Bank, one of the state-owned bank need to reform their organization structure and designed comply with new Myanmar Financial Institution Law (2016). In this reforming structure, Board of Director of Myanmar Economic Bank and all of the participants in this reform process need to deep understanding of the effect of risk management practices on the financial performance of Myanmar Economic Bank and need to identify effective risk management practices for Myanmar Economic Bank.

In reforming process, Myanmar Economic Bank organized Risk Management Committee, integrated risk management department and changed the risk management practices in Myanmar Economic Bank in the financial year 2016- 2017. This project has to implement effective risk management practices of Myanmar Economic Bank in the next five years. It is need to analyze the effect of risk management practices on the financial performance of Myanmar Economic Bank.

Therefore, the study on the effect of risk management practice on financial performance of Myanmar Economic Bank is to identify specific risks and effectiveness support to State - owned bank (SOB) reform and also supposed to develop Myanmar Financial Sector development. It is the rationale study on the effect of risk management practices on financial performance of Myanmar Economic Bank.

## **1.2 Objective of the Study**

The objectives of the study are as follows:

- (1) To identify risk management practices in Myanmar Economic Bank.
- (2) To examine the effect of the risk management practices in the financial performance of Myanmar Economic Bank

## **1.3 Method and Scope of the Study**

This study focus only on the conducting of the effect of risk management practice on the financial performance of the Myanmar Economic Bank. In studying on the financial performance of the Myanmar Economic Bank, the description research method is used. The research data are used by primary data and secondary data. The personal interview with 20% of responsible persons of executive level such as member of risk management committee, branch managers and 10% of non-executive level. Financial Statement of the last five years 2013-2014,2014-2015,2015-2016, 2016-2017 and 2017-2018 of Myanmar Economic Banks financial report are gathered for secondary data. Some data are from the external data form Central Bank Myanmar and other Financial Institution as like the World Bank , IMF and GIZ etc.

## **1.4 Organization of the Study**

A study on the effect of risk management practice on the financial performance of the Myanmar Economic Bank is composed of five chapters. Chapter one introduces the topic with rationale, and objective of the study, theoretical framework, method and scope are describes as introduces. Chapter two includes theoretical background and research framework with risk management process, the concept of risk management and balance sheet structure in banking services. Chapter three is to present background of Myanmar Economic Bank and risk management practices of Myanmar Economic Bank. Chapter four includes the effect of risk management practices on financial performance in Myanmar Economic Bank and finally Chapter five captures the summary of findings, suggestions and conclusion.

## **CHAPTER II**

### **THEORETICAL BACKGROUND OF THE STUDY**

This Chapter describes the theories used as a framework for this study. In order to study and understand the risk management in banking, concept of risk have to be defined first. Theories about Risk management process, organization of risk management in banking, Assets Growth Changes and liability growth changes and financial performance of a bank and measurement for Financial Performance of the Bank and Risk Management Assessment by the financial tool as Return on Assets (ROA), Loan to deposit Ratio (LDR), Capital Adequacy Ratio (CAR) ,Liquidity Ratio of a bank. These would be used later on to analyze and data compilation.

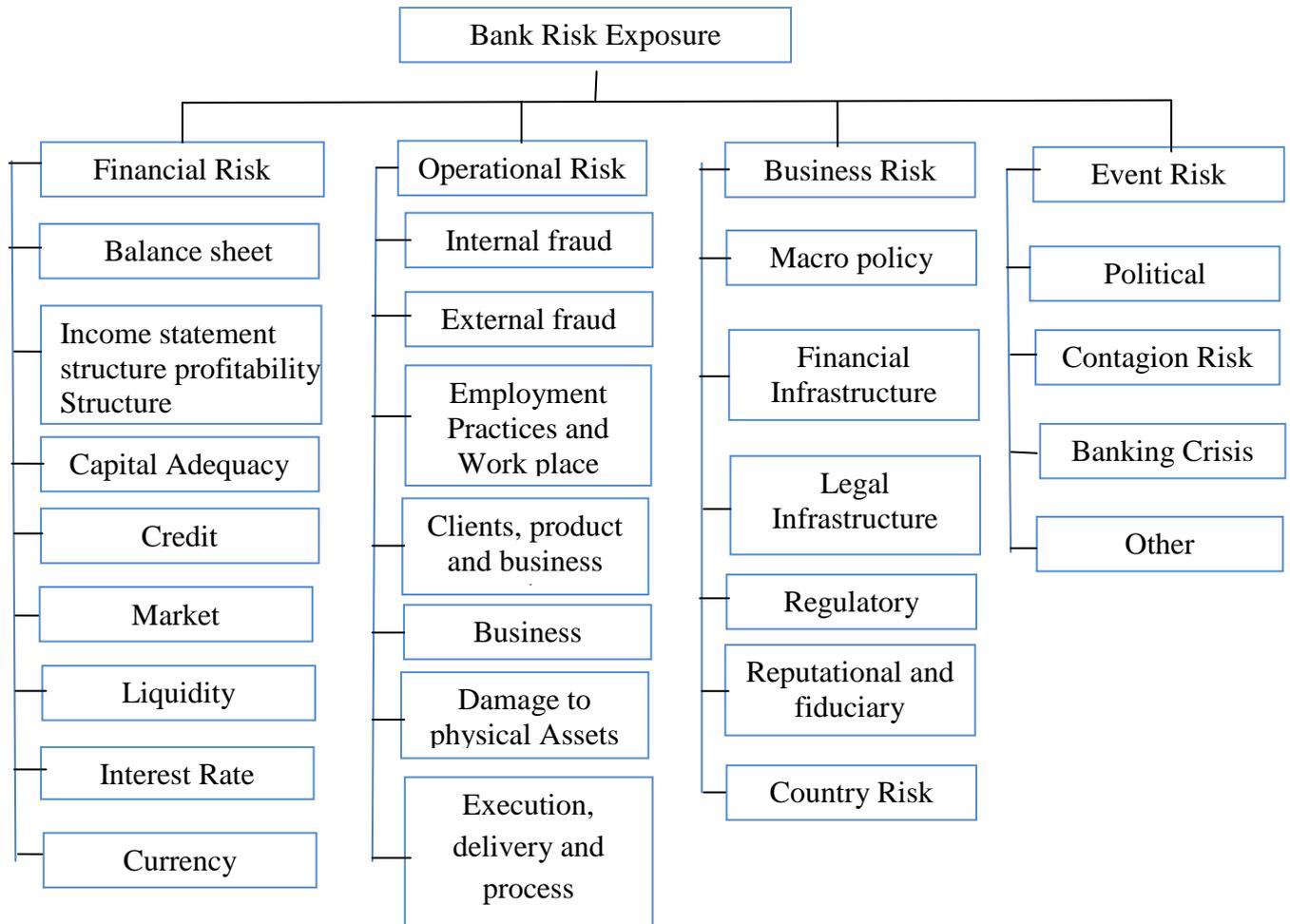
#### **2.1 Bank Exposure to risk**

Banks are faced with different types of risks that may have a potentially adverse effect on their business. Figure 2.1 indicates banks are faced with varieties of risk in the course of their operations in banking risk spectrum. Presents banking risks fall into four categories: financial, operational, business, and event risks.

Financial risk in turn comprises two types of risk - Pure risk and speculative risk. Pure risk including liquidity, credit and solvency risk can result in loss for bank and they are not properly managed. Speculative risk, based on financial arbitrage, can result in a profit if the arbitrage is correct or a loss if it is incorrect. The main categories of speculative risks are interest rate, currency and market price risk. Financial risks are also subject to complex interdependencies that may significantly increase a bank's overall risk profile. Operational risks are associated with a bank's overall organization and functioning of internal systems, including computer –related and other technologies) complies with banking policies and procedures and measures against mismanagement and fraud.

Business risks are related to a bank's business environment, including macroeconomic and policy consideration, legal and regulative factors and overall financial sector infrastructure and payment system. Event risk includes all types of exogenous risks which, if they were to materialize, could jeopardize a bank's operations or undermine its financial condition and capital adequacy. (Hennie Van Greuning, 2010)

**Figure2.1 Banking Risk Spectrum**



Source: Hennie Van Greuning, 2010

Banks need to establish a comprehensive and reliable risk management system, integrated in all business activities and providing for the bank risk profile to be always in line with the established risk propensity.

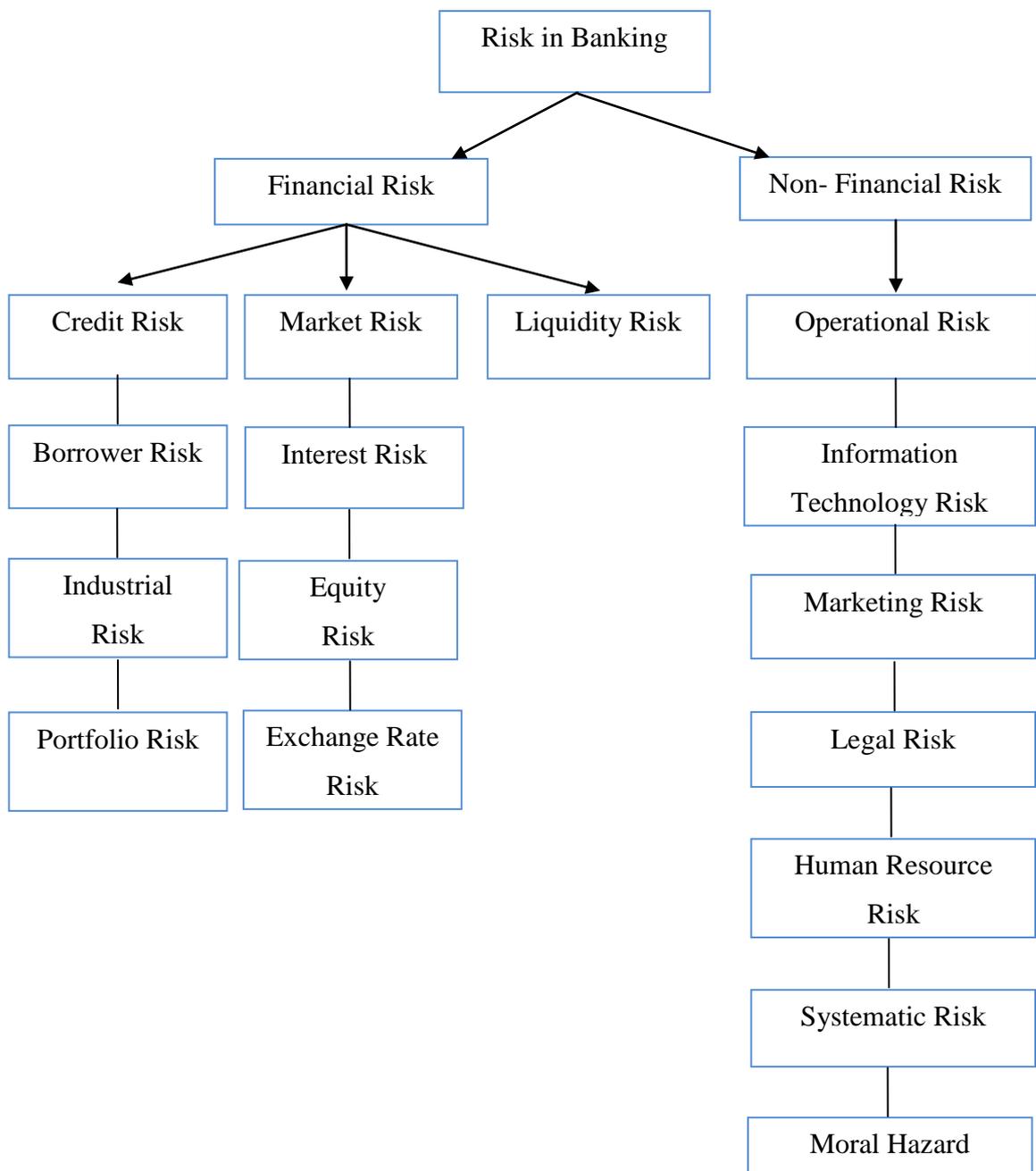
## 2.2 Types of Risk in Banking Industry

Risk is the possibility of losing something of values. Value (Such as physical health, social status, emotional wellbeing, or financial wealth) can be gained or lost when taking risk resulting from a given action or inaction, foreseen or unforeseen (planned or not planned). Risks re the opportunities and dangers associated with uncertain future events .Thus, risk also cause in the event which concern with cash

and services by using cash. Financial services especially banks are always face with the verities' of risk.

Figure 2.2 indicates banks usually fall into financial risks and non-financial risks. Financial risk includes credit risk (borrower risk, Industry risk, and portfolio risk), Market risk (interest rate risk, equity risk and exchange rate risk) and liquidity risk. On financial risk includes operational risk, strategic risk and political risk as follows:

**Figure 2.2 Risks in Banking**



Source: Sourav Shaw, 2016

Risk management analyst needs to clearly identify the type of risk on their services because identify the risk is important role in the risk management process. Therefore, the definition of risks is essential points in the prevention of the risk in the bank. The following types of risk in banking are faced in the banks according to the varieties situations.

**(a) Credit Risk**

It is the potential loss arising from the failure of a borrower to meet its obligations in accordance with agreed terms. Credit risk is one of the oldest and most significant forms of risk faced by banks as financial intermediaries (Broll, et al., 2002). Commercial banks are most likely to create a loss because of credit risk (Bo, et al., 2005). Generally, the larger the credit risk, the upper the credit premiums to be charged by banks are leading to an improvement in the net interest margin (Hanweck and Ryu, 2004). Credit risk occur borrower risk, industry risk and portfolio risk in the bank.

**(b) Market Risk**

Market risk is the risk of loss from adverse movements in financial market rates (interest and exchange rate) and bond, equity or commodity prices. A bank's market risk exposure is decided by each the volatility of underlying risk factors and the sensitivity of the bank's portfolio to movements in those risk factors (Hendricks and Hirtle, 1997). Market risk is also the risk of changes in income of the bank as a result of movements in market interest rates. Interest rate risk is a major concern for banks due to the nominal nature of their assets and the asset-liability maturity mismatch (Hasan and Sarkar, 2002). Some researchers emphasized that higher interest rates had a positive impact on banks (Hanweck and Ryu, 2004; Hyde, 2007). It arises from potential change in earnings resulted from exchange rate fluctuations, adverse exchange positioning or change in the market prices managed by the Treasury Division. Market risk includes in interest rate risk, equity risk and exchange rate risk.

**(c) Liquidity Risk**

It generates from the failure or inability to satisfy current and future financial obligations by bank because of shortfall of cash or cash equivalent assets. Banks are exposed to liquidity risk where the additional liquidity is generated, the greater are the possibility and severity of losses associated with having to dispose of illiquid assets to meet the liquidity demands of depositor (Diamond 1999; Allen and Jagtiani, 1996). However, besides depositor (Gatev, 2006) revealed that banks that make commitments to lend are exposed to the risk of unexpected liquidity demands from their borrowers.

**(d) Operational Risk**

Operational risk is defined as 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. Operational risk is the prospect of loss resulting from inadequate or failed procedures, systems or policies.

- Employee errors
- Systems failures
- Fraud or other criminal activity
- Any event that disrupts business processes.

In evaluating operational risk, practical remedial steps should be emphasized in order to eliminate exposures and ensure successful responses. Poor operational risk management can hurt an organization's reputation and cause financial damage. It is need to how much loss an organization is prepared to accept, combined with the cost of correcting those errors, determines the organization's risk appetite.

Operational risks in a bank or any other entity which have the potential to result in substantial losses can be understood bifurcated as under:

- Internal Fraud.
- External Fraud.
- Employment practices and workplace safety.
- Clients, products and business practices.
- Damage to physical assets.

- Business disruption and system failure.
- Execution, delivery and process management.

Operational risk is the risk of loss resulting from inadequate or failed internal processes, people, and systems, or from external events” (Basel Committee Jan 2001)

**(e) Equity Risk**

Equity risk typically refers to equity in companies through the purchase of stocks, and does not commonly refer to the risk in paying into real estate or building equity in properties.

The measure of risk used in the equity markets is typically the standard deviation of a security's price over a number of periods. The standard deviation will delineate the normal fluctuations one can expect in that particular security above and below the mean, or average. However, since most investors would not consider fluctuations above the average return as "risk", some economists prefer other means of measuring it. It is the risk of loss due to adverse changes in market price of equities held by the bank. Operational Risk: The potential financial loss as a result of a breakdown in day-to-day operational processes. Operational risk does not mean only failures in the bank’s operation, but also the causes of the failures, such as terrorist attacks, management failures, competitive actions and natural disasters (King, 1998). These caused are largely uncontrollable and unpredictable. Moreover, human or technological errors, lack of control to prevent unauthorized or inappropriate Transactions being made, fraud and faulty reporting may lead to further losses caused by internal process, people and operating system (Medova, 2001).

**(f) Information Technology Risk**

Information Technology Risk that customers may suffer service disruptions, or that customers or the Group may incur losses arising from system defects such as failures, faults, or incompleteness in computer operations, or illegal or unauthorized use of computer systems. (Medova, 2001).

**(g) Marketing Risk**

This risk is related to the different aspects of the promotion and branding of the bank, including image management, product promotion and advertising.

**(h) Human Resource Risk**

This type of risk is generated within the bank from failure to recruit the right people in the right place, inappropriate means of recruitment, failure to provide feedback to the employees on performance, over-reliance on key personnel, inappropriate training and development, etc. Journal of Business and Technology (Dhaka)

**(i) Legal Risk**

Legal Risk that the Group may incur losses due to violation of laws and regulations, breach of contract, entering into improper contracts or other legal factors, Moorhead, Richard & Vaughan, Steven. (2015).

**(j) Human Resources Risk**

Risk that the Group may incur losses due to drain or loss of personnel, deterioration of morale, inadequate development of human resources, inappropriate working schedule, inappropriate working and safety environment, inequality or inequity in human resource management or discriminatory conduct.( Hanweck and Ryu, 2004)

**(k) Systematic risk**

The global crisis of 2008 is the best example of a loss of all the financial institutions that occurred due to systematic risk. Systematic risk is the risk that doesn't affect a single bank or financial institution, but it affects the whole industry. Systematic risks are associated with cascading failures where the failure of a big entity can cause the failure of all the others in the industry. ( Hanweck and Ryu, 2004)

### **(1) Moral hazard:**

Moral hazard is a risk that occurs when a big bank or large financial institution takes risk, knowing that someone else will have to face the burden of those risks, any situation in which one person makes the decision about how much risk to take while someone else bears the cost if things go badly. (Martin Andersson and Staffan Viotti,1996)

### **2.3 Risk Management Partnership in Cooperate Governance of Banks**

A risk Management partnership is in which each key player has a clearly defined accountability for a specific dimension of every risk area. The working of the risk management partnership as follows:

**Bank regulators and supervisors** – Their primary role is to act as facilities in the process of risk management and to enhance and monitor the statutory frame work in which risk management is undertaken.

**Shareholders** – They are in a position to appoint the people in charge of the corporate governance process and should be carefully screened to ensure that they do not intend to use the bank solely to finance their own or their associate enterprises.

**Board of Directors**-Sometimes called Supervisory board .The Board has to set the strategic direction, appoint management ,establish operational policies and most importantly take responsibility for ensuring the soundness of the bank.

**Executive Management** is responsible for the implementation of the board’s policies through its running of a bank on a day to day basis, it is vital that it has intimate knowledge of the financial risks that are being managed.

**The audit committee** and internal auditor should be regarded as an extension of the board’s risk management policy function .The internal auditors traditionally performed an independent appraisal of a bank’s compliance with its internal control systems, accounting practices, and information systems.

**External Auditors** have come to play an important role in the risk –based financial information process.

**The Public/Consumers** as a market participants have to accept responsibility for their own investment decisions. In order to do so, they require transparent disclosure of financial information and informed financial analyst. The public can be assisted in this role as risk manager if the definition of the public.

## 2.4 Risk Management Process

Risk Management Approach is important not only for fulfilling regulatory requirements but also to improve financial and operational performance of the banks. Strong and integrated risk management is essential for the long-term sustainability of the bank's business. The comprehensive risk management policies and sophisticated risk management processes are required for systematic identification, measurement, monitoring and controlling of all business risks. All of the banks provide risk management practices based on the risk management process.

Figure (2.2) indicates Risk Management process in banking includes in the process of risk origination within the bank, Risk identification, Risk assessment and Measurement, Risk control, risk Monitoring and risk return Trade-off.

**Figure (2.3) Risk Management Process in Banking**



Source: Annual Report of Mercantile Bank in Bangladesh-2009

According to Figure 2.3 ,risk management process starts with risk analysis, which enables the bank to identify different types of risk, to recognize risk factors and to evaluate the potential consequences of risk by measuring risk exposure. Next stage - risk manipulation - includes different scenarios of actions that are prepared for each type of risk. The bank can use variety of risk management tools, both traditional (e.g. insurance) and modern ones (e.g. derivatives), that should be tailored to company's unique situation and needs. Taken actions should be continuously monitored and controlled to check up their results, compare them to the plan and introduce modification if it is required. Risk monitoring enables the company to forecast the level of risk and prepare the bank's actions in future. Thus, the risk assessment is a continuous process that is an important part of the risk management, and is realized at the first and the third stage – risk analysis and monitoring of risk.

There are many risk assessment methods – one of them is financial analysis, that can be used both at the stage of risk analysis and risk monitoring. Financial analysis is a financial management tool that uses different sources of information concerning bank's past and current activities as well as its present and future financial situation. The most important sources of information used in the financial analysis are financial statements provided by the accounting system, translating a bank's diverse activities into a set of objective numbers that inform about the bank's performance, problems and prospects. Financial data included in the financial statements can be used to identify the types of risk and their factors, to recognize the reasons and consequences of the corporate risk, to analyze the results of risk management tools and to forecast the level of risk in future.

## **2.5 Measurement for Financial Performance of the Bank**

Financial Statement and Balance sheet of a bank are vital roles of a measurement for financial performance of a bank. The analysts of risk management need to understand about the structure and composition of balance sheet of a bank. The composition of a bank's balance sheet is one of the key factors that determine the risk level faced by institution. Growth in the balance sheet and changes in the structure of assets or liabilities can impact the risk management process. Changes in the relative structure of assets and liabilities should be a conscious decision of a bank's policy maker- the board of directors. Monitoring key balance sheet

components may alert the analyst to negative trends in relationship between asset growth and capital retention capability. A bank balance sheet is a key way to draw conclusions regarding a bank's business and the resources used to be able to finance lending. The volume of business of a bank is included in its balance sheet for both assets (lending) and liabilities (customer deposit) the three crucial elements in all financial analyses include:

- (a) **Liquidity:** Ability to meet the obligations of liquid funds.
- (b) **Solvency:** Credit quality and adequacy of the bank's own resources (indebtedness).
- (c) **Profitability:** Ability to generate income/profit from allocated capital deposits or other financial instruments).

Using Balance Sheet Information to assess the financial risk in the bank is fundamental of risk management practices. The first element of the financial statement is the balance sheet presenting the bank's financial position at a single point of time, including bank's assets and the liability and equity claims against those assets [see more about balance sheet elements and its construction in: Basic elements of the balance sheet are presented in table2.1

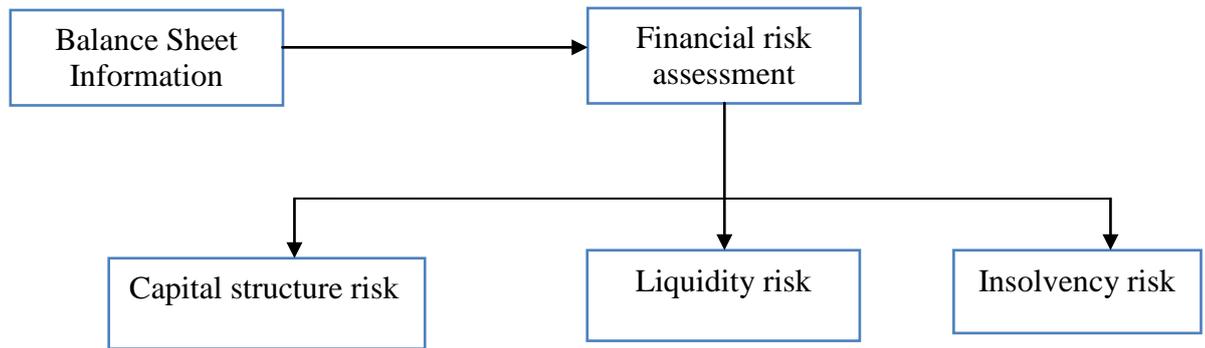
**Table (2.1) Basic Elements of Balance sheet**

| Assets  | Capital   |
|---|---|
| Fixed assets:<br>1. Intangible assets<br>2. Net plant and equipment<br>3. Long-term accounts receivable<br>4. Long-term investment<br>Current assets:<br>1. Inventory<br>2. Accounts receivable<br>3. Short-term investment | Equity capital:<br>1. Common stock<br>2. Additional paid-in capital<br>3. Retained profit<br>Debt capital:<br>1. Long-term debt capital<br>2. Current liabilities |

Source: Financial Risk Identification based on the Balance Sheet Information  
 Joanna Błach ,2010

By using balance sheet information the three components of the financial risk can be identified and analyzed: capital structure risk, liquidity risk and insolvency risk .It can be also affected on risk management practices.

**Figure (2.4) Balance Sheet Information and Financial Risk Assessment**



Source: Financial Risk Identification based on the Balance Sheet Information  
Joanna Błach ,2010

The composition of bank 's balance sheet structure require understanding not only for the bank but also of its business and competitive environment ;the overall regulatory, economic and policy environment and the customer mix. The structure of typical balance sheet is with deposits from customer on the liability side and loan and advances to customer on the asset side.

There is a close relationship between analysis of financial statements and effective performance business decision-making. The management of enterprise is depending on accounting information for taking various strategic decisions. Financial statements provide such information. This information is made useful by analyzing and interpretation of financial statements with help of financial analysis techniques. (. ( Lamarck Harvey , 2003).

### **2.5.1 Asset Structure Growth and Changes**

The banking sector's assets comprise item that are a reflection of individual banks balance sheet, although the structure of balance sheet may vary significantly depending on business orientations, market environment, customer mix, economic development .The composition of a bank's balance sheet is normally a result of asset –liability and risk management decision.

Overall liquidity of assets liquid asset is needed to accommodate expected and unexpected fluctuations. Cash and balances with the central bank represent the holdings of highly liquid and bullions as well as assets represent the holding of highly

liquid assets such as bank notes, gold coins and bullion as well as deposit with the central bank. Loans and advances to the customer are normally the most significant component of a bank's assets. Other investment could comprise a bank's longer-term equity-type investments such as equities and recapitalization non-trading bonds held in the bank's long term investment portfolio this includes equity investments in subsidiaries, associates and other listed and unlisted entities. Fixed assets represent the bank's infrastructure resources and typically include the bank's premises, the fixed property, computer equipment, vehicles, furniture and fixtures. Other assets including intangible asset management should understand on which asset they are spending their energy and how this relates to source of income.

### **2.5.2 Liabilities Structure Growth and Changes**

Liabilities are already a good indication of the risk levels and types of risk to which a bank is exposed. The types of liabilities present a bank's balance sheet by the price and supply characteristics of different types of liabilities at any given point in time. The structure of a bank's liabilities also reflects the specific asset-liabilities and risk management policies of a bank. Deposit usually constitutes the largest portion of a bank's total liabilities. A change in the level of deposit in a banking system is therefore one of the variables that influence monetary policy. The structure of a bank's liabilities also reflects the specific asset-liability and risk management policies of a bank.

### **2.6 Effective Risk Management on Financial Performance of the Bank**

The goal of financial management is to maximize the value of a bank as defined by its profitability and risk level. The key aspect of financial management is risk management, which covers strategic and capital planning, asset-liability management, and the management of bank's business and financial risk. The central components of financial risk are the identification, quantification and monitoring of the risk profile, of both banking and financial risks. It is need to measure financial ratio to identify risk on a bank. Among the key ratios of financial ratio of the bank, Return on Asset (ROA) ratio, Capital Adequacy Ratio (CAR), loan-to-deposit ratio (LDR) are effective tools of risk management assessment.

### **2.6.1 Return on Assets (ROA) ratio of a bank**

Return on Assets (ROA) defines as net profit divided by total assets. It shows the ability of management to acquire deposits at a reasonable cost and invest them in profitable investments (Ahmed, 2009). The higher the ROA, the more the profitable the bank. Return on Asset (ROA) is chosen as an indicator of financial performance of banking because Return on Asset is used to measure the effectiveness of companies in generating profit by utilizing own assets. If the Return on Asset increases, the profitability of the company increases. It affects the increase in profitability gained by shareholders (Husnan, 1998).

Return on Asset (ROA) ratio is a profitability ratio that measures the net income created by total assets amid a period by contrasting net income with the average total assets. At the end of the day, the return on assets ratio or ROA measures how effectively an organization or company can deal with its assets to produce profit during some period. The formula of calculation of Return on Asset (ROA) ratio is as follows:

$$\text{Return on Assets (ROA)} = \frac{\text{Net Income}}{\text{Total Assets}}$$

It can be review of the status of a bank's strength and weakness on their profitability on the Return on Asset (ROA) ratio of the bank. According to Return on Asset (ROA) ratio, risk management analyst can make risk identifying and risk assessment for prevention of decreasing profitability of a bank.

### **2.6.2 Capital Adequacy Ratio**

The capital adequacy ratio (CAR) is a measurement of a bank's available capital expressed as a percentage of a bank's risk-weighted credit exposures. The capital adequacy ratio is used to protect depositors and promote the stability and efficiency of financial systems around the world. Two types of capital are measured: tier-1 capital, which can absorb losses without a bank being required to cease trading, and tier-2 capital, which can absorb losses in the event of a winding-up and so provides a lesser degree of protection to depositors.

## Calculating CAR

The capital adequacy ratio is calculated by dividing a bank's capital by its risk-weighted assets. The capital used to calculate the capital adequacy ratio is divided into two tiers.

$$\text{CAR} = \frac{\text{Tier 1 Capital} + \text{Tier 2 Capital}}{\text{Risk Weighted Asset}}$$

### Tier-1 Capital

Tier-1 capital, or core capital, consists of equity capital, ordinary share capital, intangible assets and audited revenue reserves. Tier-1 capital is used to absorb losses and does not require a bank to cease operations. Tier-1 capital is the capital that is permanently and easily available to cushion losses suffered by a bank without it being required to stop operating. A good example of a bank's tier one capital is its ordinary share capital.

### Tier-2 Capital

Tier-2 capital comprises unaudited retained earnings, unaudited reserves and general loss reserves. This capital absorbs losses in the event of a company winding up or liquidating. Tier-2 capital is the one that cushions losses in case the bank is winding up, so it provides a lesser degree of protection to depositors and creditors. It is used to absorb losses if a bank loses all its Tier-1 capital.

### 2.6.3 Loan-to-Deposit Ratio (LDR)

The loan-to-deposit ratio (LDR) is used to assess a bank's liquidity by comparing a bank's total loans to its total deposits for the same period. The LDR is expressed as a percentage. If the ratio is too high, it means that the bank may not have enough liquidity to cover any unforeseen fund requirements. Conversely, if the ratio is too low, the bank may not be earning as much as it could be

$$\text{LDR} = \frac{\text{Total Loan}}{\text{Total Deposits}}$$

Therefore, the key factors of financial performance of a bank are effective tool of the measurement of risk management and it can be always used as risk management practices of a bank. Risk management analyst used as a tool for identifying risk and how to manage on varieties of risk on a bank and can be provided risk management practices and procedure.

## **Chapter III**

### **Background and Risk Management Practices in Myanma Economic Bank**

This chapter consists of the background, organization structure and operational highlights of Banking Services of the Myanma Economic Bank and risk management structure risk management practices of Myanma Economic Bank before and after SOB reforming process .And also provide in details of new risk management practices in Myanma Economic Bank.

#### **3.1 Background of Myanma Economic Bank**

Myanma Economic Bank (MEB), which was established on 2 April 1976, was originated from the State Commercial Bank (SCB) founded in 1954. In accordance with the State Commercial Bank Law, the State Commercial Bank (SCB), the first and foremost state-owned commercial bank in Myanmar, was established in 1954 with the aim to raise the entire people's economic development through a nation-wide banking system. Since its establishment, the SCB expanded its service areas as well as its number of branches throughout the country year by year. There were 40 SCB branches throughout the country in 1962.

Myanmar changed its course to socialism in 1962 and all existing banks were nationalized in 1963. To be in line with the People's Bank of the Union of Burma Act of 1967, all the nationalized banks were merged together as a monolithic bank called People's Bank of the Union of Burma. However, well aware of inefficiency of the monolithic banking system to the economy, the Bank Act of 1975 was promulgated and the People's Bank was re-established into four state-owned banks- Union of Burma Bank (UBB), Myanma Economic Bank (MEB), Myanma Foreign Trade Bank (MFTB) and Myanma Agricultural Bank (MAB) with effect from 2 April 1976.

Though MEB was the successor of the former SCB, it provided only domestic banking services while the MFTB and MAB rendered foreign exchange transactions and seasonal loans for agricultural development, respectively.

In 1988, Myanmar has pursued market oriented economy and accordingly, the Central Bank of Myanmar (CBM) Law and Financial Institutions of Myanmar (FIM) Law were promulgated in 1990 in order to restructure the financial sector to be in line with the market economy. The FIM Law recognized MEB as an existing state-owned commercial bank. As FIM Law grants a wider coverage of banking services to all banks in the country, MEB now operates both domestic and foreign banking services.

### **3.2 Organization Structure of MEB**

MEB mainly conducts commercial banking services in Myanmar through its network consisted of 315 bank branches, 14 State and regional Banking Offices and 7 Head Office Departments. MEB's management, together with the support from its 3 policy development entities – the Board of Directors, the Credit Committee and the Executive Committee– oversees MEB's daily operations.

MEB 's Vision as a stated owned financial institution, MEB aims to provide financial services to public by law, regulations and procedures that change in policy from financial sector.

MEB organized Policy Boards of management and directives on administrative matters and risk management on the bank.

#### **1. Board of Directors**

Board of Directors has responsibilities for reviewing the MEB's performance to achieve its objectives and strategy, reviewing the bank's internal controls. The Board of Directors is appointed by the Ministry of Finance and Revenue and the managing director of the MEB is the Chairman of the BoD. The members of the BoD are:

1. Chairman ( Managing Director of MEB)
2. Member ( General Manager, MEB )
3. Member ( General Manager, MEB )
4. Member ( General Manager, MEB )
5. Member ( General Manger, MEB )
6. Member ( Director, Budget Department )

7. Member ( Director, UAGO)
8. Member ( Director, CBM )
9. Secretary ( Deputy General Manager, MEB )

## **2. Executive Committee**

The EC decides the extraordinary cases of operations and administrative matters. The managing director of MEB is also chairman of the executive committee. Members of Executive Committee are:

1. Chairman ( Managing Director of MEB)
2. Member ( General Manager, MEB )
3. Member ( General Manager, MEB )
4. Member ( General Manager, MEB )
5. Member ( General Manger, MEB )
6. Member ( Deputy General Manager, MEB )
7. Secretary ( Assistant General Manager, MEB )
8. Secretary ( Assistant General Manager, MEB )

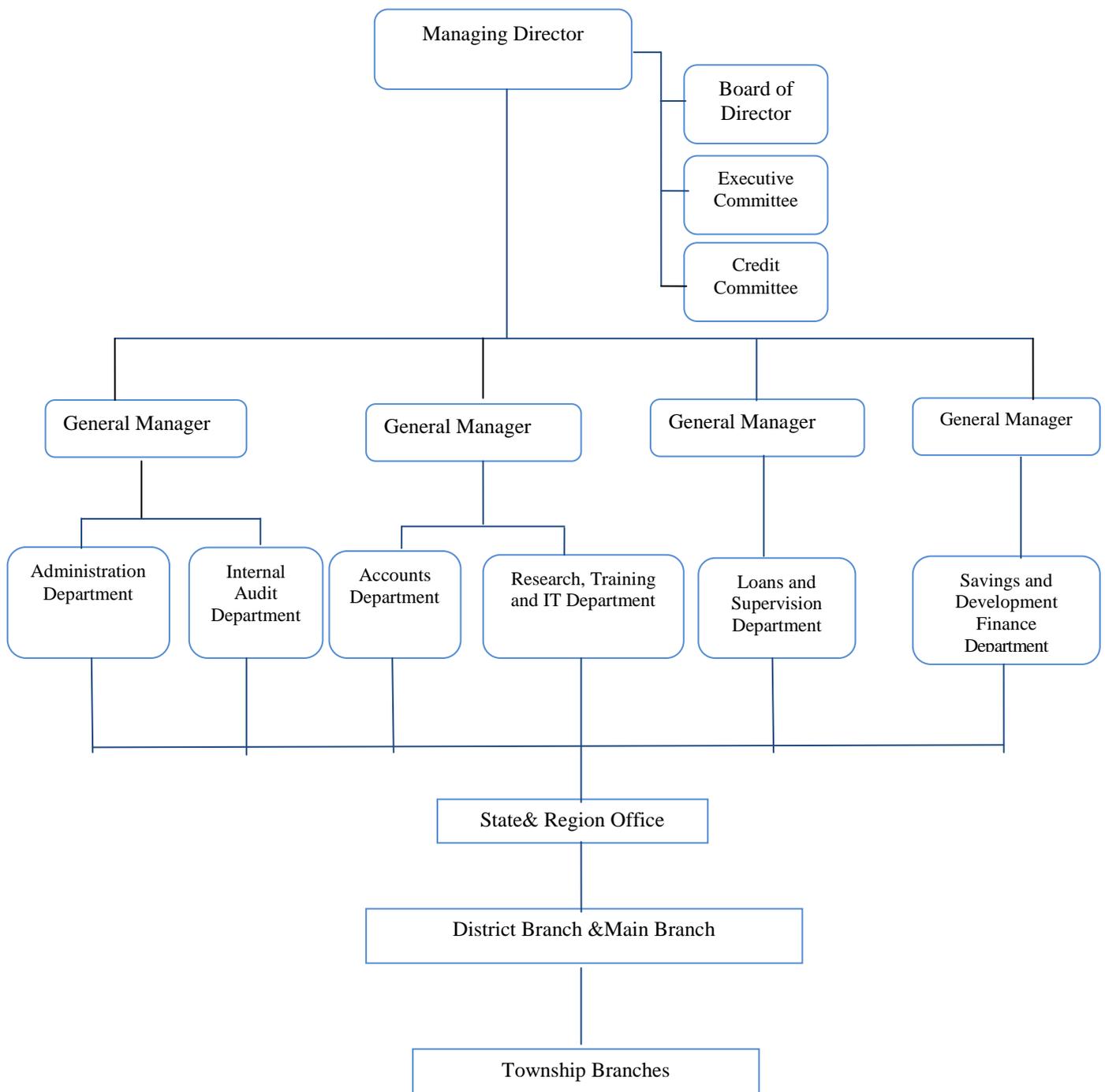
## **3. Credit Committee**

Various loan proposals are examined by the Credit Committee. Credit Committee also supervises and controls credit management of the MEB, the members of Credit Committee are:

1. Chairman ( Managing Director of MEB)
2. Member ( General Manager, MEB )
3. Member ( General Manager, MEB )
4. Member ( General Manager, MEB )
5. Member ( General Manager, MEB )
6. Secretary (Manager, MEB )

Figure 3.1 shows the organizational structure of Myanmar Economic Bank and three of Myanmar Economic Bank Management Committee and (6 ) Head Offices supervise (14 )State and Divisional offices and Bank Branches.

**Figure 3.1 Organizational Structure of Myanmar Economic Bank**



Source: MEB Annual Report, 2018

Figure 3.1 shows that Managing Director leads Management committee such as Board of Directors, Executive Committee and Credit committee. Head of seven departments of Head office are General Manager level and they manage and supervise the operational services of Myanmar Economic Bank Branches.

### 3.3 Highlights for Banking Services of Myanmar Economic Bank

MEB provides not only commercial banking services but also developmental banking services. MEB Banking services are including Commercial banking service, Policy Banking Service, Currency Maintaining on Currency Chest on behalf of Central bank of Myanmar and Treasury banking Services illustrate as Figure 3.2.

MEB offering deposit ,commercial loans, consumer loans, remittances, G2P payments (salaries and pensions), non-customer (cash) services and other retail services through its vast distribution channels (branch network services/ATMs/Mobile). offering commercial loans, consumer loans, remittances, G2P payments (salaries and pensions), non-customer (cash) services and other retail services through its vast distribution channels (branch network services/ATMs/Mobile); MEB is also a developmental Financial Institution Thus, MEB is involved in financing infrastructure/development lending, MADB loans and JICA fund management. MEB support functions to the Government and Central bank function; focused on treasury, state accounts handling, Central Bank chest. The main services of MEB is depositing and borrowing from Private and public sector.

**Deposit-** MEB accepts deposit classified into Deposit of financial institutions and Deposit by NFIs and other clients. Types of deposit of MEB are Demand Deposit, Saving Deposit , Saving Certificate, Fixed and special Deposit and other deposit.

**Loans and Advances** –MEB branches provide short –term borrowings and long – term borrowings and types of Loans and advances as follows:

Housing Loans

Personal and professional loans

Loans to MADB

Loans to MSME

Loans to MSME(TSL)

Loans to private sector

Loans to interbank Lending

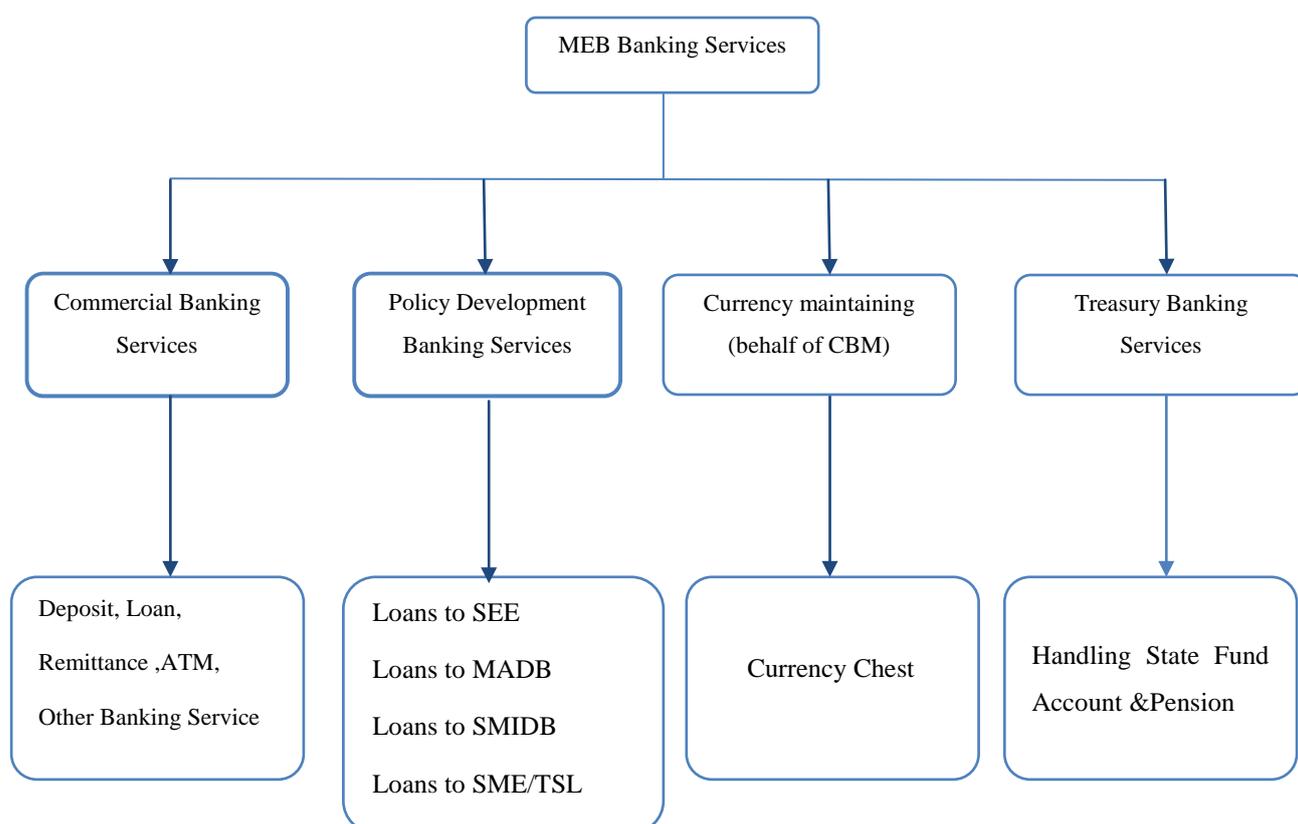
Bilateral interbank lending to Foreign Bank

Loans Classified by types of business such as Production, Trading (local), Transportation, Construction, Services, SMEs.

**Internal Remittance** MEB provides remittance services through MEB Branches in the whole country.

**Other Banking Services-** MEB also provides other banking services such as Foreign Exchange Services, paying agent bank as Government loan and grant, Performance Guarantee, Payment Order, etc.

**Figure3.2 Banking Services of Myanmar Economic Bank**



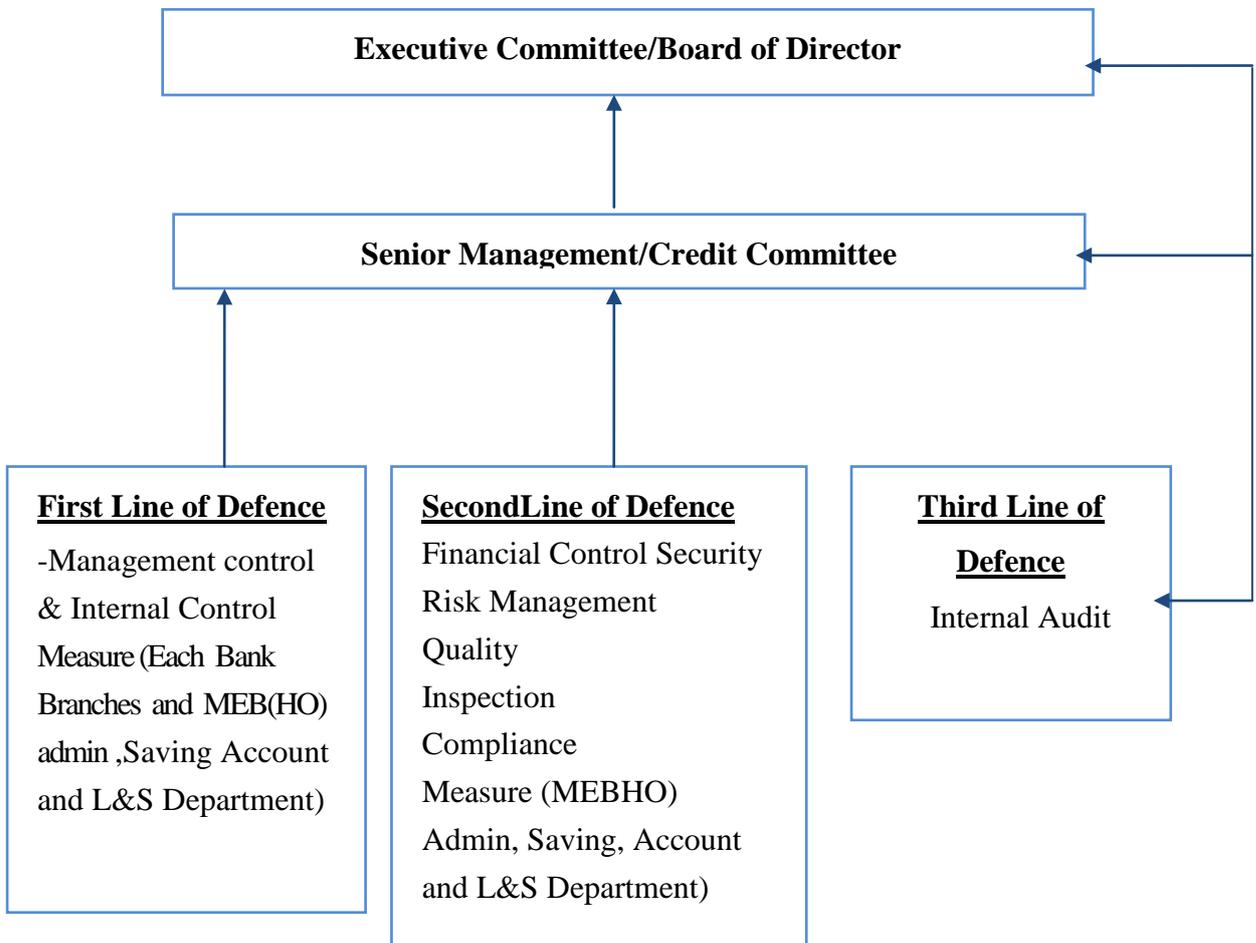
Source: Myanmar Economic Bank Annual Report, 2018

### **3.4 Risk Management Practices in Myanmar Economic Bank**

Myanmar Economic Bank had lack of Risk management committee until 2016. Risk Management in General in MEB, risk is organized as functions within the respective departments. There are subdivisions that focus on specific risks, like the Supervision subdivision within the Loans and Supervision Department. These subdivisions have their own risk focus, and as a result they do not see beyond their own focus in order to pick up risks outside of their current duty. Overall within MEB there is no general risk culture and no formal risk management framework in place. Only Credit Risk is embedded within the overall structure, as there is a Credit Committee who oversees the credit activities of the bank. There is a credit policy in place, and there are specific guidelines from the Central Bank of Myanmar (CBM)

towards dealing with credit risk on loans. The Credit Committee convenes weekly to approve loan applications. Except for Credit, there is no clear and active 2nd line of defense and formal risk management framework in place at MEB. The main department that in practice focuses on the operational performance and pick out weaknesses is Internal Audit. MEB Management considered the 3<sup>rd</sup> line of defense in risk management process until 2016 as Figure 3.3.

**Figure 3.3 Risk Management Governance Structure in Myanmar Economic Bank before 2016-2017**



Source: Myanmar Economic Bank Risk Management Report ,2010

Figure 3.3 shows the risk management organization structure used in Myanmar Economic Bank until 2016-2017 before reforming process and risk management practices of Myanmar Economic Bank used in three line of defense as follows:

**First line of Defense** - Each bank branches focus on their own risk and Bank branch Manager measures risks, identify risk on their branches and submit to concerning sub department Head office for controlling risks through divisional office.

**Second line of Defense-** Each Head office department supervise and inspect on the risks problems and submit to MEB management committee depends on the volume of risk problems .Also instructed rules and regulations, procedures, directives for risk management practices.

**Third line of Defense** - Oversight by the audit committee is with independent check and quality assurance of internal controls and functions of 1<sup>st</sup> and 2<sup>nd</sup> lines of defense. Internal Audit Department and Divisional offices inspect monthly, quarterly and annually on banking operation and internal process of MEB bank Branches. MEB management team identifies measurement and controlling of risk management on MEB branches according to Audit report submitted by Internal Audit Department.

Myanma Economic Bank used these risk management practices before 2016-2017 reforming process periods and MEB management concluded it was not effective risk management practices on financial performance and it was need to change in reforming process.

### **3.4.1 The Changes of Risk Management Practices of Myanma Economic Bank in State –Owned Bank Reform.**

According to New financial Institution Law (2016) and SOBs reforming process in Myanmar, MEB need to change risk management practice and organized risk management committee. MEB also have to plan for implementation of integrated risk Management frame work within next three years as follows:

#### **(a) Organizational Structure of Risk Management Function**

MEB Board of directors is responsible for maintenance of prudent risk management mechanism and implementation of risk management framework. The Board of Directors will approve the polies, Strategies and system and operation approach for risk management.

Figure 3.5 indicates New Organizational Structure of risk management Function of the Myanmar Economic Bank in reforming structure have to implement risk management frame work within next three years.

**Figure 3.4 New Organizational Structure of Risk management Practices of Myanmar Economic Bank**



Source: Myanmar Economic Bank's Reform Report, 2018

Figure 3.5 indicates Board of Directors of Myanmar Economic Bank and Risk Management Committee manage and supervise Integrated risk Management Department, led by Credit risk officer. Integrated risk Management Department includes Credit Risk Management Team, Market Risk & ALM Management Team, Operational Risk Management Team and FX Risk Management Team. Risk Management process of Myanmar Economic Bank use in three line of defence of risk management practice.

(b) Three line of defence of risk management practice of MEB are as follows:

**First Line of defense** –Involvement by the board , Managing Director, Senior Management Committees, accountability and responsibility of senior and middle management supported by internal control, governance structure,

processes and risk. Risk Management committee specialize in overall process of risk management practices and guidance on risk management practices.

**Second line of Defense-Oversight** by Chief of risk management led with Integrated Risk management department and handle with independent risk monitoring and compliance & legal. Credit risk management team, market risk &ALM management team, operational risk management team and FX risk management team support data and information for risk management practice.

**Third line of Defense** – Oversight by the audit committee make with independent check and quality assurance of internal controls and functions of 1<sup>st</sup> and 2<sup>nd</sup> lines of defense. Audit committee and risk management committee are controlling, monitoring, mitigation and supporting to Management of Myanmar Economic Bank.

- (c) The Risk Management Practices of Myanmar Economic Bank includes Identification, Measuring, Controlling; Monitoring and Mitigation Identification is the first stage of the risk management process. The identification or recognition of risk is the first step in an effective risk management process. Beyond identifying risk it is equally important to measure or quantify risk. An important aspect of a framework for controlling risk is the establishment of clear lines of authority and reporting lines and responsibilities. Effective control of risk is also dependent on the bank's ability to communicate its policies, procedures and limits to all employees and business units involved in the management of the risk.
- (d) Integrated Risk Management Department analyse Monthly Analysis of Balance Sheet Structure, and Financial Statement and reviewing the asset growth and liabilities growth of MEB, accountability Limits and Financial performance ratio such as Return on Assets (ROA) are used as tool for measurement and management of risk.

Myanmar Economic Bank changed the organizational structure of risk management practices to make effective risk management in reforming process. It is need to measure the new risk management practices are effective risk management on financial performance of Myanmar Economic Bank.

## **CHAPTER IV**

### **EFFECT OF RISK MANAGEMENT PRACTICES ON FINANCIAL PERFORMANCE IN MYANMA ECONOMIC BANK**

This Chapter consists of three sections: the financial position of Myanmar Economic Bank, Common Size Analysis on Financial Statement, Composition of Income Statement of Financial Position and Risk management practices based on secondary data from 2013-2014 to 2017-2018. Profitability of Myanmar Economic Bank is using analysis of Return on Assets for measurement of effective risk management for a period from 2013 to 2018 and it can be revealed that changes of financial performance based on effectively risk management practices.

#### **4.1 Profile of Respondent**

The primary data are collected by personal interview with the responsible person of Myanmar Economic Bank. The personal interviews with the responsible persons are 20% of responsible person of executive levels such as member of risk management committee, Branch Manager and 10% of non-executive level.

#### **4.2 Research Methodology**

The description research method is used in this study .The secondary data are gathered from data Financial Statement of the last five years 2013-2014,2014-2015,2015-2016, 2016-2017 and 2017-2018 of Myanmar Economic Banks financial report and some data are from the external data form Central Bank Myanmar and other Financial Institution as like the World Bank , IMF and GIZ etc. This study used Common size analysis on Financial data for evaluating financial performance of Myanmar Economic Bank.

#### **4.3 The Financial Position of Myanmar Economic Bank**

Risk Analysts can analyze the structure of balance sheets as well as individual balance sheet items with specific risks such as liquidity risk and market risk. In this process, the interaction between various types of risk must be understood to ensure that the key principles of effective risk management.

An evaluation of balance sheet structure required understanding not only of the bank but also of its business of and competitive environment, the overall regulatory, economic, and the policy environment and the customer mix. The structure of balance sheet is with deposit from customers on the liability side and loans and advance to the asset side.

Risk Management committee reviews on monthly balance sheet and financial statement of Myanmar Economic bank and identify risk on the bank and instruct and control on MEB branches for prevention of risk on the banks and submit to the Management committee of the bank. Risk Management Committee and Board of Director (BOD) of Myanmar Economic Bank mainly emphasis on the following items of financial position of the bank :

**ASSET**

- a. Cash
- b. Accounts With C.B.M
- c. Claims On Financial Institutions
- d. Bills Purchased
- e. Investment account
- f. Loans To NFIs And Other Clients
- g. Other Assets
- h. Total Assets

**LIABILITIES AND CAPITAL**

- a. Total Deposits
- b. Term Borrowings
- c. Other Liabilities
- d. Equity Capital
- e. Total Liabilities And Capital

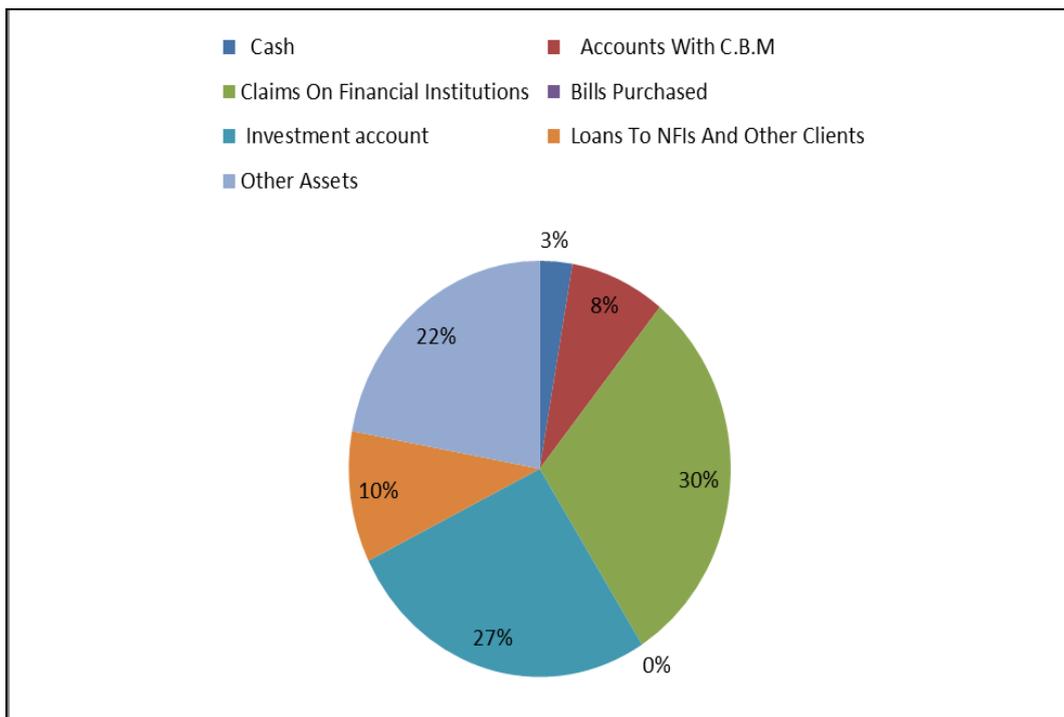
As a review on updated financial statement of Myanmar Economic Bank at 31.3.2018, it is found that the various element in balance sheet and highlights the importance of the structure and the composition of Liabilities and Assets.

Assets consists of Cash in vault, Current Account with CBM ,Claims on Financial institution ,Bill purchased, Government Instruments, Equity , Loans to NFIs and other clients, other Assets, and Premises and other Asset. Liabilities and

capital consists of Total deposits, Long term borrowings, suspense accounts, Other Liabilities and equity capital.

Figure (4.1) shows Current Asset Components of Myanmar Economic Bank and it can be easily seen that the component structure of current asset of Myanmar Economic Bank as follows:

**Figure 4.1 Current Asset Components of Myanmar Economic Bank**



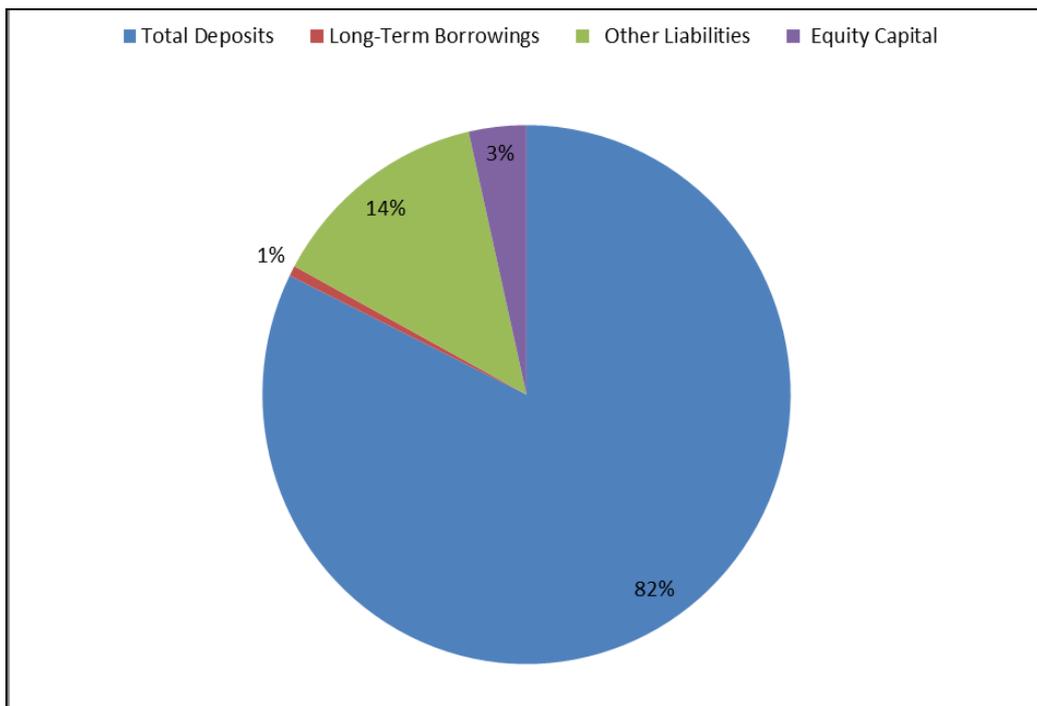
Source: Balance sheet of Myanmar Economic Bank, 2018

According to Figure 4.1, it can be seen that the portion of Claims on financial Institution is 30% of total Asset is the largest portion of total asset of Myanmar Economic Bank. Claims on financial Institution include the account balance of local and abroad of Myanmar Economic Bank. It is clearly to know about Myanmar Economic Bank is easily made settlement between other banks and financial institutions, cash reserve for financial institution to pay individual and firms and also reserve of financial institutions subject to reserve requirement system. But Foreign Currency account in Nostro account in abroad, MEB need to manage Foreign exchange rate risk management. Loan to NFIs and other clients portion is 10% of total asset, it seem that MEB encourage to increase borrowing amount to the NFIs and

other clients portion to get more profitability but to manage to make reducing Non performing Loans.

Figure (4.2) shows Current Liabilities Components of Myanmar Economic Bank and it can be easily seen that the component structure of current liabilities of Myanmar Economic Bank as follow:

**Figure 4.2 Current Liabilities Components of Myanmar Economic Bank**



Source: Balance sheet of Myanmar Economic Bank,2018

According to Figure 4.2, it can be seen that the portion of total deposit is 82% of total liabilities of Myanmar Economic Bank shows that MEB is 100% public trustee bank in Myanmar. But MEB need to find the ways to get profitability with utilization of large amount of deposit. The Portion of Investment portion is 27% of the total liabilities include investment with Myanmar Securities Exchange Centre (MSEC) and Yangon Stock Exchange (YSX), Investment on Government Treasury Bill and Government Treasury Bond and Investment on share for Credit Bureau. It means that MEB also participate in development in Capital Market in Myanmar.

#### 4.4 Common Size Analysis on Financial Statement of Myanmar Economic Bank

Common-size analysis (also called *vertical analysis*) converts each line of financial statement data to an easily comparable, or common-size, amount measured as a percent. This is done by stating income statement items as a percent of net sales and balance sheet items as a percent of total assets (or total liabilities and shareholders' equity). Vertical analysis is a method of financial statement analysis in which each entry for each of the major categories of the financial statement. Vertical analysis is also used across other financial statements as a percentage measure. The composition of a bank's balance sheet is normally a result of asset and liability and risk management decision. Bank assets comprise items are a reflection of individual bank's balance sheet. The analysis of financial position of Myanmar Economic Bank actually support to find out the effective risk management practices. The common analysis of assets of Myanmar Economic bank provide in Table 4.1. It can be seen the structural change and asset growth of Myanmar Economic Bank in the year 2013-2014.

**Table 4.1 Structural Change in Assets of MEB**

|                                     | 2013-2014 | 2014-2015 | 2015-2016 | 2016-2017 | 2017-2018 |
|-------------------------------------|-----------|-----------|-----------|-----------|-----------|
| 1. Cash In Vault                    | 1%        | 2%        | 2%        | 1%        | 3%        |
| 2. Current Accounts with C.B.M      | 2.8%      | 1.9%      | 1.9%      | 2%        | 8%        |
| 3. Claims On Financial Institutions | 16%       | 22%       | 20%       | 20%       | 30%       |
| 4. Bills Purchased                  | 0%        | 0%        | 1%        | 0%        | 0%        |
| 5. Investment Account               | 28%       | 28%       | 19%       | 27%       | 27%       |
| 6. Loans To NFI's and Other Clients | 25%       | 29%       | 26%       | 24%       | 10%       |
| 7. Other Assets                     | 2%        | 1%        | 12%       | 26%       | 22%       |
| Total Assets                        | 100%      | 100.00%   | 100%      | 100%      | 100%      |

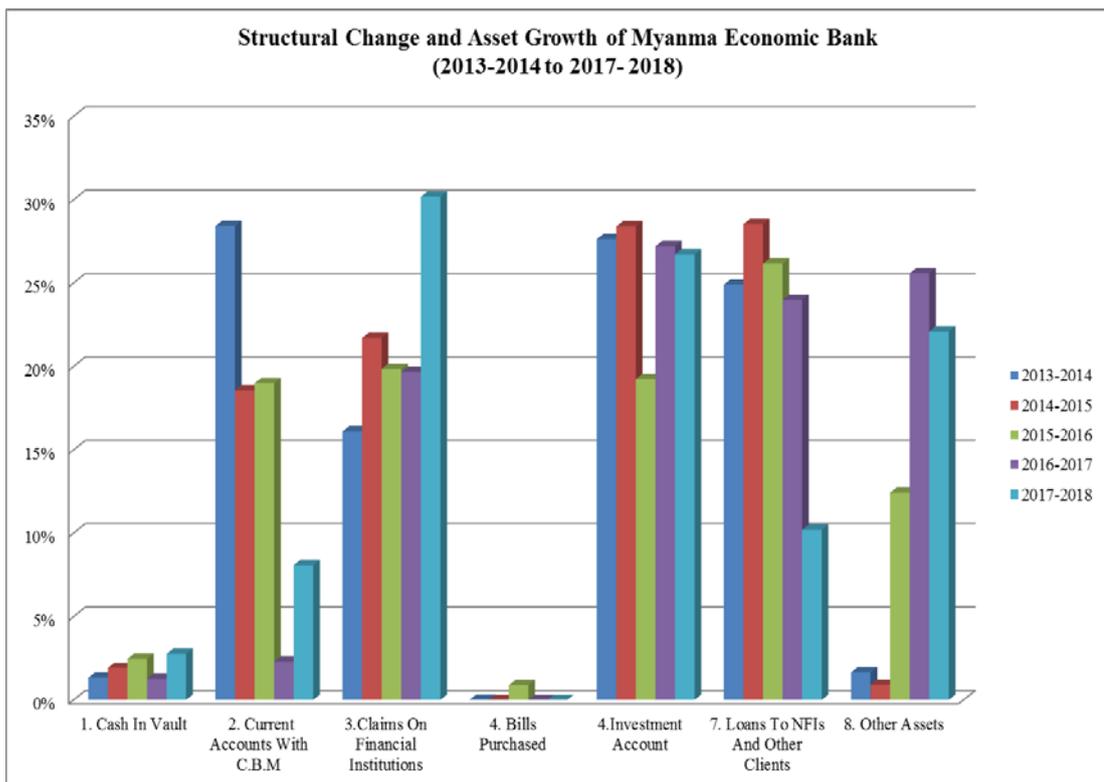
Source : Balance sheet of Myanmar Economic Bank(FY 2013 to FY 2018)

According to table 4.1, it can be seen that cash in vault slightly increase from 1% in the year 2012-2013 to 3% in the year 2017-2018, current accounts with CBM

increase from 2% in the year 2012-2013 to 8% in the year 2017-2018, claims on financial institutions increase from 16% in the year 2012-2013 to 20% in the year 2016-2017 and after that prominently increase 30% changes in the year 2017-2018, means that liquidity risk management is more effective in Myanmar Economic Bank after changing risk management practice in Myanmar Economic Bank.

It can be made prevention of liquidity risk of a bank. Loans to NFIs was 25% in the year 2012-2013 and it was decrease 24% in the year 2016-2017 and then more decrease to 22% in the year 2017-2018 .It means credit risk management made controlling of Non-performing loans risk and more systematically lend quality loan to customer. Figure 4.3 shows the structural change and asset growth of Myanmar Economic Bank from FY 2013-2014 to FY 2017-2018.

**Figure 4.3 Structural Changes in Asset of Myanmar Economic Bank**



Source : Balance sheet of Myanmar Economic Bank(FY 2013 to FY 2018)

According to Figure 4.3, it can be seen clearly that the changes of assets structural and asset growth of Myanmar Economic Bank .In 2016, Myanmar Economic Bank change the governance structure of risk management committee and risk

management practices in banking services .It can be seen in the year 2017- 2018, the controlling of liquidity of cash management and borrowing of quality loan for non-performing loan risk although changing period in only one year.Table 4.2 indicates the common analysis of assets of Myanmar Economic bank and it can be seen the structural change and Liabilities growth of Myanmar Economic Bank.

**Table 4.2 Structural Change in Liabilities of MEB**

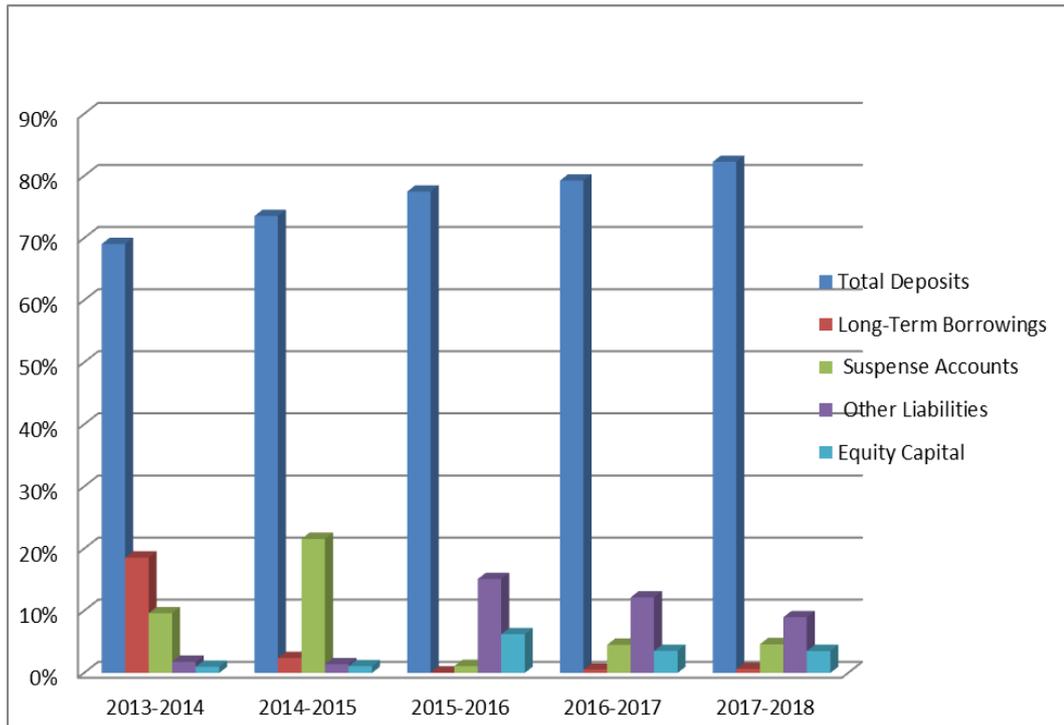
| LIABILITIES AND CAPITAL       | 2013-2014 | 2014-2015 | 2015-2016 | 2016-2017 | 2017-2018 |
|-------------------------------|-----------|-----------|-----------|-----------|-----------|
| Total Deposits                | 69%       | 74%       | 77%       | 79%       | 82%       |
| Long-Term Borrowings          | 19%       | 3%        | 0%        | 1%        | 1%        |
| Suspense Accounts             | 10%       | 21%       | 1%        | 5%        | 5%        |
| Other Liabilities             | 2%        | 1%        | 15%       | 12%       | 9%        |
| Equity Capital                | 1%        | 1%        | 6%        | 4%        | 4%        |
| Total Liabilities And Capital | 100%      | 100%      | 100%      | 100%      | 100%      |

Source : Balance sheet of Myanmar Economic Bank(FY 2013 to FY 2018)

According to Table 4.2, total deposit raise from 69% in the year 2013-2014 to 77% in the year 2015-2016 and after that sharply increase 82% in the year 2017-2018. It means that Myanmar Economic Bank get the more public trust deposit after changing risk management practices .But it is also need to manage and utilization of the huge amount of deposit to get the more profit for the bank. And MEB also need to control and manage the interest rate risk on the huge amount of deposit. Equity and capital changes isn't prominent because Myanmar Economic bank is one of the state – owned bank and MEB have to plan for increase paid up capital amount according to SOB reform program.

Figure 4.4 shows the structural change and growth of Capital and liabilities of Myanmar Economic Bank in the year 2013-2014 to 2017-2018. It can easily be seen the structural change and growth of capital and liabilities. Total deposit is significant growth in Myanmar Economic Bank.

**Figure 4.4 Structural Changes in Liabilities of MEB**



Source : Balance sheet of Myanmar Economic Bank(FY 2013 to FY 2018)

Figure 4.1 shows clearly changes of structural change and growth of Capital and liabilities of Myanmar Economic Bank .It can be seen that MEB need to measure the identification or recognition of risk in the huge deposit amount and to make effective risk management process. Beyond identifying risk it is equally important to measure or quantify risk.

#### 4.5 Analysis on Composition of Income Statement of Myanmar Economic Bank

Income status is one of the measurement tools of risk management of a bank. Risk management Analysts need to review the income status of a bank for identifying risk and to make more profit of a bank. Table 4.4 indicates the common size analysis on income status of Myanmar Economic Bank in the year 2013-2014 to 2017-2018

**Table 4.3 Income Status of Myanmar Economic Bank  
(2013-2014 to 2017-2018)**

| Income                                 | 2013-2014   | 2014-2015   | 2015-2016   | 2016-2017   | 2017-2018   |
|--|-------------|-------------|-------------|-------------|-------------|
| Interest on Loans and Overdraft        | 18%         | 23%         | 18%         | 20%         | 30%         |
| Interest on Deposit Auction            | 0%          | 1%          | 4%          | 5%          | 2%          |
| Interest on MADB, JICA and Policy loan | 8%          | 10%         | 8%          | 13%         | 20%         |
| Exchange on Foreign Transaction        | 45%         | 29%         | 32%         | 33%         | 33%         |
| Exchange on Internal Remittance        | 2%          | 2%          | 1%          | 1%          | 1%          |
| Interest on Investment                 | 22%         | 29%         | 24%         | 25%         | 9%          |
| Other Income                           | 5%          | 7%          | 14%         | 4%          | 5%          |
| <b>Total Income</b>                    | <b>100%</b> | <b>100%</b> | <b>100%</b> | <b>100%</b> | <b>100%</b> |

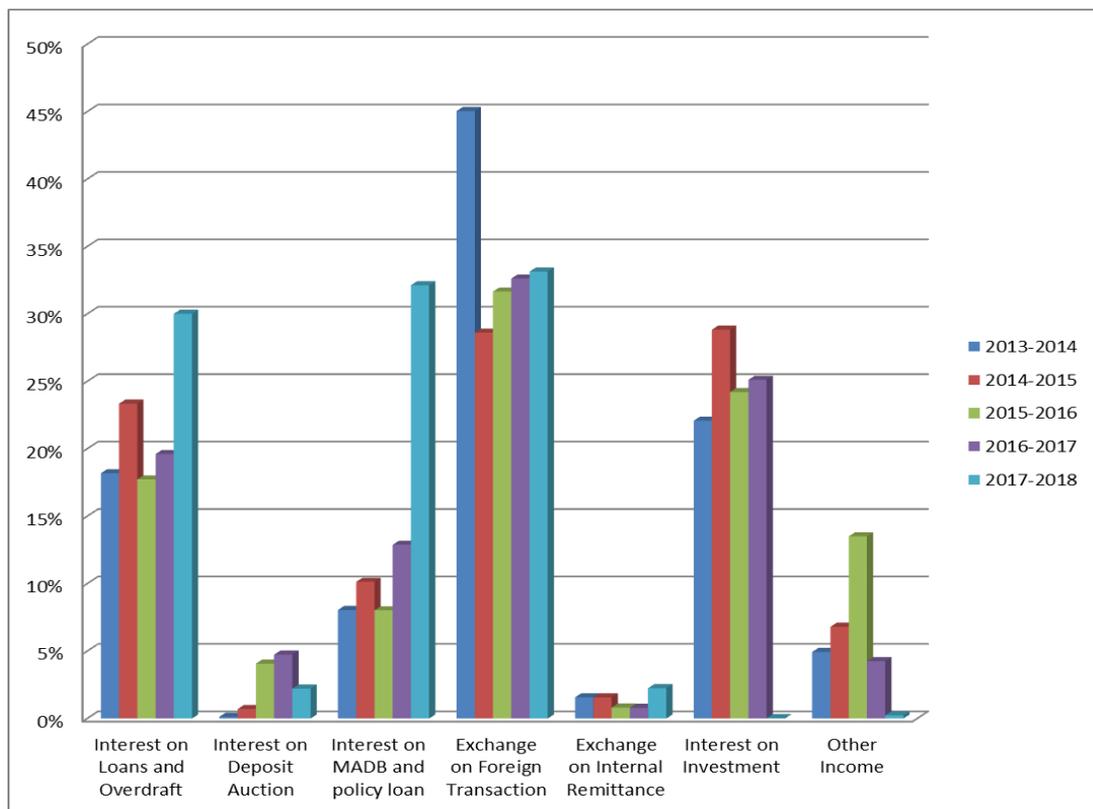
Source: Income Statement of Myanmar Economic Bank

According to Table 4.3, Interest on Loans and Overdraft of MEB prominently increase from 18% in the year 2013-2014 to 20% in the year 2016-2017 and after that it raise to 30% in the year 2017-2018. It shows that quality loans paid to the interest regularly to the bank and the effectiveness of controlling risk management on Non

Performing Loan and lending policy change to quality loan. Interest of MADB, JICA and other policy loan increase from 8% in the year 2013-2014 increase to 13% in the year 2016-2017 and prominently increase to 32% in the year 2017-2018 and it shows the success of MEB participation of development of Agricultural sector and development project of the country. But, Interest on investment and other income are decrease. It shows MEB need to more investment for more profit and to create the new services to get profit of the bank.

Figure 4.5 indicates the income status of Myanmar Economic Bank in the year 2013-2014 to 2017-2018. It seems clearly the income status of Myanmar Economic Bank.

**Figure 4.5 Income Status of Myanmar Economic Bank (2013-2014 to 2017-2018)**



Source : Balance sheet of Myanmar Economic Bank(FY 2013 to FY 2018)

According to Figure 4.5, Income of Myanmar Economic Bank includes interest of loan and overdraft, Interest on Deposit Auction, Interest on MADB and policy loan, Income of exchange on foreign transactions, Income of exchange on internal remittance, Interest on investment and other income. After changing the risk management governance structure and risk management practices in Myanmar

Economic Bank, the effect of income status of Myanmar Economic Bank is slightly changes and it is need to make new products and mechanism for getting more profit of the bank.

#### **4.6 Analysis on Financial Position of Myanmar Economic Bank**

Analysis on Financial Position of Myanmar Economic Bank is the key factor of risk management practices .The situation of financial position of a bank can review risk identifying and prevention of risks on a bank. Table 4.5 indicates the Financial Position of Myanmar Economic Bank in FY 2013 to FY 2018 and it can be easily seen that the status of financial performance of Myanmar Economic Bank.

**Table 4.4 Financial Position of Myanmar Economic Bank**

| <b>Year</b> | <b>Loan to Deposit Ratio</b> | <b>Liquidity Ratio</b> | <b>Capital Adequacy Ratio</b> |
|-------------|------------------------------|------------------------|-------------------------------|
| 2013-2014   | 36.05                        | 104.27                 | 80.25                         |
| 2014-2015   | 38.78                        | 98.3                   | 57.65                         |
| 2015-2016   | 33.74                        | 81.1                   | 26.81                         |
| 2016-2017   | 31.00                        | 98.1                   | 21.75                         |
| 2017-2018   | 28.38                        | 100.6                  | 22.86                         |

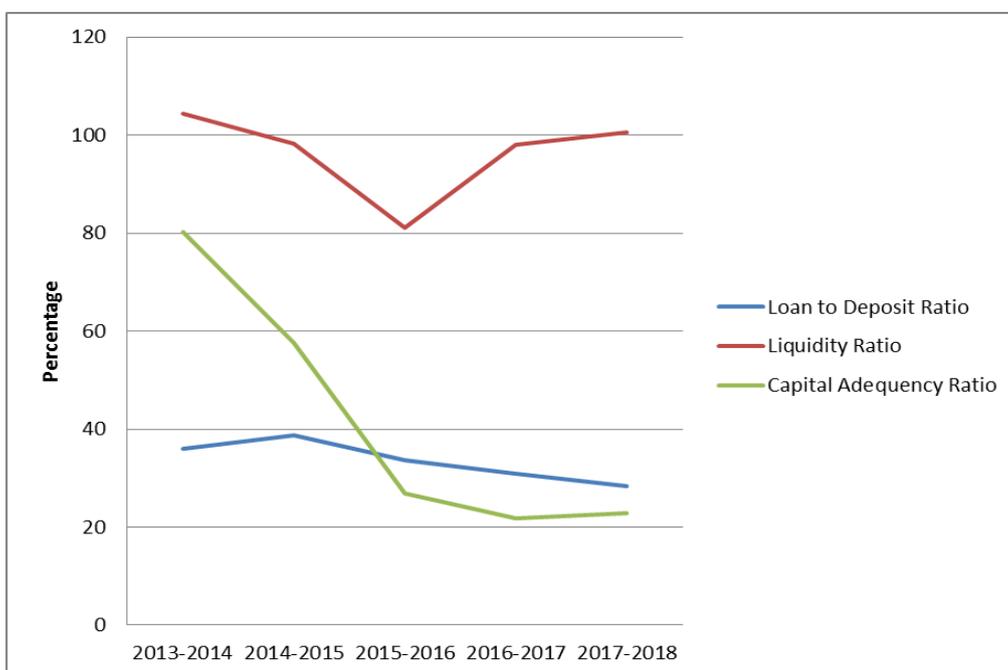
Source: Annual Report of Myanmar Economic Bank (FY 2013 to FY 2018)

According to Table 4.5, it can be compared about Loan to Deposit Ratio, Liquidity Ratio and Capital Adequacy Ratio before and after the year 2016-2017. Loan to deposit ratio of Myanmar Economic Bank was decrease from 36.05% in the year 2013-2014 to 31% in the year 2016-2017 and more decrease 28.38% in the year 2017-2018 . Liquidity Ratio decrease from 104.27 in the year 2013-2014 to 98.1% in the year 2016-2017 and increase 100.6% in the year 2017-2018. Capital adequacy ratio decrease 80.25% in the year 2013-2014 to 21.75% in the year 2016-2017 and increase 22.86% in the year 2017-1018 . It can be seen that Liquidity Ratio and Capital Adequacy Ratio are better than the year before 2016-2017 but Loan to Deposit Ratio need to be increased. It shows Myanmar Economic Bank need to lend more quality loan to customer.

Capital Adequacy Ratio (CAR) is important to examine the key financial performance of the bank. CAR of MEB is reviewed from the year 2013 to 2108.MEB would not suffer from capital shortage and capital surplus is more than enough. Therefore, MEB should introduce multiple functions or new products or services by using its well position capital for sustainable development and growth.

Figure 4.6 indicates the status of Financial Position of Myanmar Economic Bank with the Loan to Deposit Ratio, Liquidity Ratio and Capital Adequacy Ratio before and after the year 2016-2017.It can be clearly seem that the changes of key factor of risk management assessment.

**Figure 4.7 Financial Position of Myanmar Economic Bank**



Source: : Annual Report of Myanmar Economic Bank (FY 2013 to FY 2018)

According to Figure 4.7 , it can be clearly seem that the financial performance of Myanmar Economic Bank slightly changes in loan to deposit ratio ,liquidity ratio and capital adequacy ratio between the period of the year 2016 to the year 2018.

In overall, Myanmar Economic Bank has a strong financial structure with efficient and stable financial system by lowering the risk of bank becoming insolvent. The higher of MEB’s capital adequacy ratio ensure the higher degree of protection of depositor’s monies. Loan to deposit ratio is used to assess a bank's liquidity and should be less than 100%.Myanmar Economic Bank has an average 34% of LDR over 5 years. This shows that Myanmar Economic Bank need to manage the liquidity risk

prudently which is enough to cover the unforeseen funding requirement and used its own deposits to make loans to customers. On the other hand, Myanmar Economic Bank has an increase in LDR which indicates the decrease in the liquidity of bank to make use of its own deposits in funding purpose.

Liquidity ratio is a measure of how easily Myanmar Economic Bank can get cash. It can be measured whether Myanmar Economic Bank has enough liquid assets to meet its financial obligations and prevention of risk. Myanmar Economic Bank is required to meet the needs of CBM's liquidity ratio which maintain the level of its liquidity asset against its eligible liabilities at not than 20 percent. Myanmar Economic Bank is highly liquid. High liquidity can be a future driver for growth.

#### **4.7 Analysis on Return on Assets (ROA) of Myanmar Economic Bank**

Ratio of return on Asset (ROA) is a kind of earning ability .Earning quality reflects quality of a bank's profitability and its ability to earn consistently. Profitability of Myanmar Economic bank is measured by Return on asset (ROA) method and it is very useful for risk management practices and clearly define in weakness of the bank. Myanmar Economic bank also use Return on asset (ROA) method in risk management practice in Myanmar Economic Bank. Table 4.4 indicates the Return on Assets (ROA) of Myanmar Economic Bank in the year 2013-2014 to 2017-2018. It is clearly seen in the return on asset of the bank and the strength and weakness of the financial performance of the bank .

**Table 4.5 Return on Assets (ROA) of Myanmar Economic Bank**

(MMK in Millions)

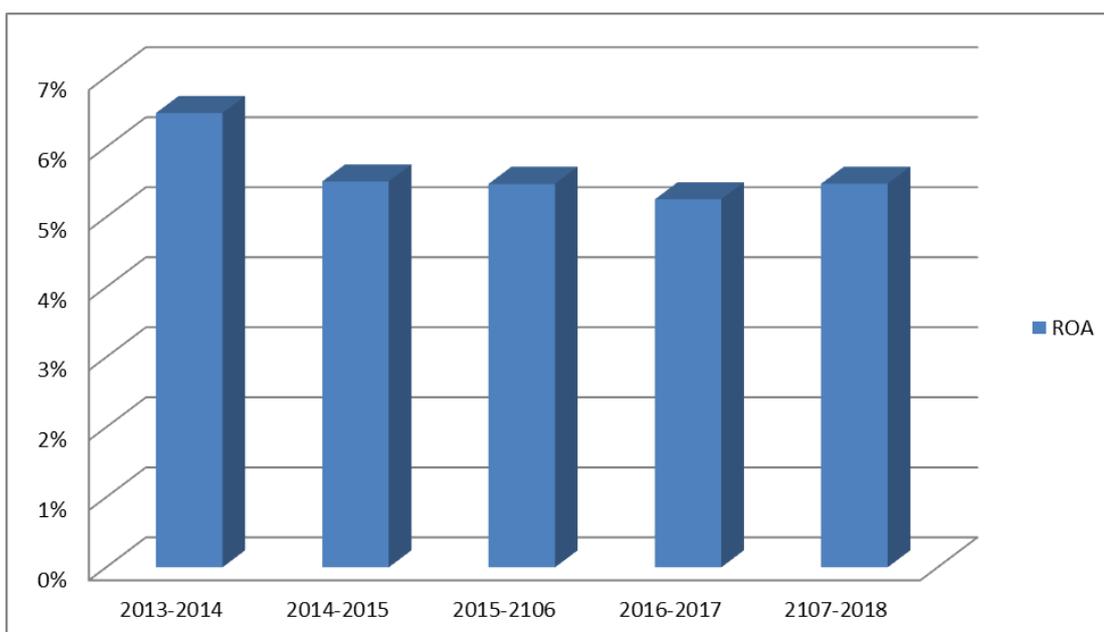
| <b>Year</b>            | <b>2013-2014</b> | <b>2014-2015</b> | <b>2015-2106</b> | <b>2016-2017</b> | <b>2107-2018</b> |
|------------------------|------------------|------------------|------------------|------------------|------------------|
| Net Income             | 319936           | 280660           | 374415           | 432513           | 547456           |
| Average<br>Total Asset | 4931804          | 5094157          | 6838836          | 8231520          | 9996081          |
| ROA                    | <b>6.49%</b>     | <b>5.51%</b>     | <b>5%</b>        | <b>5%</b>        | <b>5.5%</b>      |

Source : Balance sheet of Myanmar Economic Bank (FY 2013 to FY 2018)

According to table 4.4, return on asset (ROA) of Myanmar Economic Bank decrease from 6.49% in the year 2013-2014 ,5.51% in the year2014-2015 to 5% in

the year 2016-2017 and slightly increase 5.5% in the year 2017-2018. Banking sector should strive to record the ROA of 1.5% and above. Myanmar Economic Bank meets the expectation by achieving 1.8% of ROA over the years. This shows that Public Bank has efficiently used their assets to generate profit. It seems that financial performance of Myanmar Economic Bank after reforming process is better than financial performance of Myanmar Economic Bank before reforming process. The effect of risk management practices on financial performance of Myanmar Economic Bank is more effective after reforming process. Figure 4.6 indicates Return on asset (ROA) of Myanmar Economic Bank in the year 2013-2014 to 2017-2018.

**Figure 4.6 Returns on Asset (ROA) of Myanmar Economic Bank  
FY (2013-2014) to FY (2017-2018)**



Source : Balance sheet of Myanmar Economic Bank (FY 2013 to FY 2018)

According to Figure 4.1, the Return on asset (ROA) of Myanmar Economic Bank shows improvement of profit of the bank is slightly changes and it means the effect of risk management practices on financial performance of Myanmar Economic Bank is more effective than after reforming process but it is need to create profitable new product and using effective risk management practice in a bank.

In SOB reforming process, Myanmar Economic Bank changed risk management practices and tools of the measurement of risk and created effective risk management practices and procedure. It is clearly seen that the effect of risk managements practices on financial performance of Myanmar Economic Bank and profitability of Myanmar Economic Bank is not strongly satisfied as expected . It shows that it is need to create effective risk management practices for financial performance assessment and new product for profitability.

## **CHAPTER V**

### **CONCLUSION**

The conclusion section has two main parts: findings and suggestions for Myanmar Economic Bank. First part is findings, which represent the risk management practices in Myanmar Economic Bank and to analyze the effect of risk management practice on the financial performance of Myanmar Economic Bank. It is clearly understood about the concept of risk management and financial performance of a bank and Financial Statement and Balance sheet of a bank are useful tools for review and identify risk management of a bank. It is easy to know the weakness of the bank with balance sheet structure. To implement the reforming process of SOB reform, the effectiveness of risk management practice is a vital role of management of Myanmar Economic Bank. It also needs to make the risk management organizational structure with efficient and skillful bank analysts. The second part presents the suggestions and then provides limitations and needs for further study.

#### **5.1 Findings**

In this study, there are two objectives to identify the risk management practices in Myanmar Economic Bank and to examine the effect of the risk management process on the financial performance of Myanmar Economic Bank. According to the New Financial Institutions Law in Myanmar (2016) and State-Owned Bank reform Project, Myanmar Economic Bank has to change the Governance structure of Risk Management Committee and risk management practices of Myanmar Economic Bank in 2016. This study has therefore concluded that risk management practices in Myanmar Economic Bank. The study also concluded that risk measurement, Risk management environment and adequate internal controls have the highest impact on the financial performance of Myanmar Economic Bank.

Myanmar Economic Bank needs to put more efforts in risk management practices in order to improve financial performance of the bank. Should also check their risk management policy, Procedures and practices and streamline them with global standards. In this study, analyze the balance sheet structure of Myanmar Economic Bank in the year 2012-2013 to 2017-2018. It is found that the structural change and growth of assets and liabilities using common size analysis.

It is found that the portion of the cash Account with CBM and other financial Institution is the largest portion of assets of Myanmar Economic Bank and it seems that easily liquidity for the bank. But Foreign Currency deposit in other banks makes foreign exchange rate risk. Deposit of foreign Currency makes more profit, but it can be faced more risk. The portion of Loans to NFIs and other client's portions in the assets of Myanmar Economic Bank in 2017- 2018 are lower than 2016-2107. It seems that decreasing the borrowing amount of MEB because the credit risk management team made controlling of Nonperforming loans and only makes borrowing for quality loan. The portion of the investment account remains unchanged and it is needed to make new investments.

It is also found the portion of the deposit amount is very huge amount and the interest for these deposits has to make decreasing of profit from a bank. Thus, Interest rate risk can suffer not only for deposit to other banks, but also a customer deposit of a bank. The portions of long term borrowing are very small portions seems no burden for long term borrowings. In this study also analyze income status of Myanmar Economic Bank and it is also found that Interest on loans and overdraft is a large portion of the income of Myanmar Economic Bank but it is needed to borrow for quality loan for controlling of NPL and prevention of credit risk.

It is also found that the portion of exchange of foreign transactions is also a large portion because foreign currency deposit on the foreign correspondent bank can get the interest on Time /Demand deposit and commission for foreign exchange transactions. It needs to create new products to get profit of a bank but also need to be effective foreign exchange rate risk management mechanism and skillful foreign exchange management analyst.

In an Implementation period of changing risk management practices in Myanmar Economic Bank in the year 2016-2017 to 2017-2018 ,the effect on the financial performance of Myanmar Economic Bank is slightly changed and has reorganized systematic risk management organizational structure .It has also well adopted the risk management practice of Myanmar Economic bank with effective policies and procedures.

## **5.2 Suggestion**

According to analysis and findings, it is found that a highly liquid resource allocation is observed at Myanmar Economic Bank, but limitation of lending activities, it is need to make an effectiveness risk management framework and encourage increasing lending amount with short term and long term borrowings for utilizations of excess huge amount of deposit. Myanmar Economic Bank needs to create new products for getting profit with operational risk management framework. Myanmar Economic Bank should be noted about the efficient and skillful risk management analyst on the varieties of risks on the bank is essential for risk management practices. MEB management should daily or weekly reviewing instead of monthly reviewing of the balance sheet and financial statement on the bank by using core banking system.

## **5.3 Limitation and Needs for Further Study**

This study is focused on the structure of the Balance Sheet and financial statement and limitation of the details figure of data of Myanmar Economic Bank and it can be provided ratio analysis .The practices of risk management of Myanmar Economic Bank after 2016 is implementing period and it is not complete set and it is need for further analysis. Furthermore, it is analyzed by using descriptive methods with tables, graph and charts. Therefore, it is needed continuous study by using other useful and effective analytical tool for risk management practices. Financial performance analysis is the effectiveness tool in risk management practices. Since this study just emphasizes on Myanmar economic Bank only.

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