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**EFFECT OF OPERATIONAL RISK MANAGEMENT PRACTICES ON
FINANCIAL PERFORMANCE OF AYA BANK**

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

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ABSTRACT

The purpose of this study was to investigate the effectiveness of operational risk management practices at AYA Bank. The study was conducted by the following objectives: to identify the internal and external operational risk management practices of AYA Bank and to analyze the effect of operational risk management practices on financial performance of AYA Bank. AYA bank has (258) branches and (259) Compliance officers. Among them, this study collected (92) compliance officers from Head Office and different branches of AYA Bank. The method used in this study was based on the descriptive research method. Structure questionnaires was used in the primary data collection. This study adopted the random sampling method. The findings found that most employees are given the right trainings to perform their tasks effectively and senior management provide the clear guidance and direction regarding the operational risk management processes. The study shows that the bank has the strong operational risk management culture. This finding shows that, most of the respondents agreed that employees performance of AYA bank can result the higher income to make a profit. Internal audit department should more examine of the management controls within an information technology infrastructure. AYA bank needs more developing ethical training program for employees to create ethical workplace. The result of this study are encouraging for policy makers in banking industry and guidelines and procedures provided by the AYA bank on operational risk management should be fully observed into to ensure the risk is well mitigated and improvement in financial performance.

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LIST OF ABBREVIATIONS

AYA	- Ayeyarwady Bank
BCBS	- Basel Committee on Banking Supervision
CBM	- Central Bank of Myanmar
BIS	- Bank for International Settlement
ROA	- Return on Assets
ROE	- Return on Equity
NIM	- Net Interest Margin

CHAPTER I

INTRODUCTION

A sound financial system is essential for an economy's health and it is necessary for financial institutions to monitor the risks associated with their products and services on an ongoing basis with the increase in competition. Banks and other financial institutions are continuously experiencing changes in the business environment, driven by rising customer expectations, evolving regulatory requirements, upgrading technological innovation, and stiff competition. It increases the likelihood of organizational failure or mistake and may result in increased operational risks. Traditional risk management practices have always concentrated on protection of the tangible assets reported on company's financials (African economic outlook, 2016).

An effective risk assessment process addresses both financial risks such as credit, market and liquidity risk and non-financial risks such as operational, legal and environmental risk. Among the various risks, operational risks are regarded as being the most important of financial institutions because they can lead to the destruction of a business. This could be the result of a loss of reputation or a loss of operation capability of a company. The Basel II defines operational (Basel Committee on Banking Supervision 2006) risk as the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events and clearly indicates that operational risk is now considered as including both internal errors and external influences.

Basel II provides a guideline for banks better risk management and provides a framework for identifying and managing operational risk. For regulatory purposes, the regulators of financial institutions and banks require a high awareness level by directors on controls that are in place to reduce and mitigate these risks. Further, compliance regulations, like Basel II demands firms focus on operational risks so as to be able to identify, measure, evaluate, and control or manage the risk (Rippel & Teply, 2011). In

Basel III, Operational risk is the second largest contributor to risk-weighted assets after credit risk for the typical commercial bank. Under Basel III regulations, banks must calculate operational risk capital using the standardized measurement approach.

Most operational risks arise from people incompetency and misuse of powers, failed processes during processing of information, transmission, and retrieval of data, and inaccuracy output. Information Technology and systems may also lead to operational risk when there is a failure of the system, hacking, and programming errors thus causing losses to the institution (Strachnyi, 2016). Internal causes of operational risks include issues of insufficient processes, existing systems failures, poor hardware and software maintenance as well as errors in communication. External factors includes natural disasters, political disturbances, fraud as well as weak financial policies within the institutions (Barakat, 2014). Operational risk is more complex and challenging to monitor, control and manage compared to financial risk.

In Myanmar, modern banking and financial services are currently in their infancy. Local Myanmar banks play a role in reform efforts by taking the advantages and opportunity to grow their branch network and introduce new financial products. The Central Bank of Myanmar (CBM) was allowed 45 representative offices of foreign banks currently operating in Myanmar to open new branches and later removed prohibition restricting loans to local businesses. Retail banking will allow foreign subsidiaries to act as local banks on May 2019 and will have full permission to do so. Whereas foreign banks may cooperate to provide additional services to local lenders, Myanmar's banking sector is in its formative stages of development. For this cause, leading banks in Myanmar can have the major challenges in giving the financial services. The more challenges lead to the more product innovations and technological innovation. The more innovation will cause the more errors and risks in operations.

The board of directors of AYA Bank has sound internal control and systems for risk management that are appropriate in relation to the extent and nature of the bank's activities. Risk management system and internal control should also cover the AYA bank's corporate values, ethical guidelines and guidelines for corporate social

responsibility. All employees who working in management level of AYA Bank have responsibility to manage the risks as part of their accountability for achieving objectives. Therefore, operating risk managers will have the opportunity to reduce current and future operating risk by concentrating on the mitigation and elimination of real operational losses.

1.1 Rationale of the Study

Effective risk management is critical to the survival of the bank. The risk management objective is to maximize the bank's operational capacity, ensure resource efficiency, evaluate existing opportunities, and maximize profit. To achieve this goal, a good and in-depth understanding of the existing risks is needed to implement an efficient internal control system to prevent or mitigate the risks. In addition, the financial crisis showed the importance of a strong risk management process and the need of important changes to improve the risk management process in each bank and for the whole banking system. On 10th June, 2019, the Central Bank of Myanmar (CBM) published the regulations that all banks need to perform effectively internal control system. In large banks, risk committee that specializes in the management of the bank's risks, and internal control system is set up for the role of observance of the risk, state of affairs and approaches taken for comprehensive risk identification, and maintenance of an efficient internal control system.

AYA bank is a fastest growing bank and leading private bank in Myanmar and it had 258 branches around the country. AYA Bank offers several retail banking, wholesale banking, foreign banking and commercial banking products and services. In AYA bank, operational risk management practices are effectively controlled because improvements in technology, CBM regulations and increased international competition. Therefore, this study to identify the internal and external operational risk management practices in AYA bank and how to effect on the financial performance of AYA Bank.

1.2 Objective of the Study

The objectives of the study are:

- (1) To identify the internal and external operational risk management practices of AYA Bank
- (2) To analyze the effect of operational risk management practices on financial performance of AYA Bank

1.3 Scope and Method of the Study

The method used in this study was based on the descriptive research method. The data collected for the study consisted of primary and secondary data. Structure questionnaires was used in the primary data collection. This study adopted the random sampling method. AYA bank has (258) branches and (259) Compliance officers. Among them, this study collected (92) compliance officers from Head Office and different branches of AYA Bank. The secondary data was obtained from the published annual reports and financial statements of AYA bank, Central Bank of Myanmar, internet website and some survey. This study focused only operational risk because operational risk management is important to protect the business from financial losses, liabilities and negative brand recognition.

1.4 Organization of the Study

This paper is organized into five chapters: Chapter I consists of introductory elements to provide basic understanding as rationale of the study, objectives of the study, scope and method of the study. Chapter II reviews literature on the definition, types of risks faced in financial institutions, operational risk management in banks, risk management processes, operational risk management and financial performance. Chapter III includes the history of AYA bank, bank's products and services and organization structure of AYA bank. Chapter IV of the thesis presents analysis part of the study of risk management practices and effect of risk management practices on financial performance. Chapter V contains findings, suggestions and need for further research.

CHAPTER II

LITERATURE REVIEW

This chapter highlights on the types of risks faced by financial institutions, operational risk management in banks, internal and external operational risk management, operational risk management processes and operational risk management on financial performance.

2.1 Major Risks Faced by Financial Institutions

Risk can also mean a type of unplanned occurrence whose financial impact leads to lower earnings or losses. Any transaction or process resulting in loss or benefit may be referred to as a risky proposal due to the uncertainty or complexity of the trading activity. In simpler words, the risk can be defined as uncertainty to an outcome. The banking sector represents the world's largest economy with the greatest diversity of banking institutions and concentration of private credit. The banking industry has awakened to risk management, especially since the global crisis during 2007-08. There are eight major risks faced by banks that are credit risk, market risk, operational risk, liquidity risk, reputational risk, business risk, systemic risk, moral hazard risk. (Aboli Gangreddiwar, 2015)

2.2 Operational Risk Management in Banks

In the modern banking sector, operational risks are one of the problems affecting the industry, but they attract little attention. Some banks are going to be worried about the credit risk. Operational risk management focus on manageable and countable risks. The risk managers should ask themselves how best they can handle operational risks in the future.

According to the BCBS (2004), operational risks are the risks of the loss coming from a failed or an inadequate internal process, system, people or sometimes external

events. The definition comprises of legal risks and excludes reputation and strategic risks. The explanation provided by BCBS (2004) is a breakdown of four causes of operational risks in a financial institution: processes, people, and system and external events. Operational risk is the vast discipline focusing on the risks increasing from the people, systems, and processes through which a firm operates. It can also include other Categories of risk, such as legal risk, fraud, physical or environmental risks. Revell (1979). It arises from a wide range of activities like acts of frauds, errors, negligence, violations, events of technological failures, process deficiencies, systems flaws, actions of terrorists and vandalism, natural disasters, like floods, earthquakes, etc, Hussain et al. (2014). The advent of globalization and deregulation of financial institutions, along with technological advances and changing of global financial views, has made it necessary for financial institutions to pay greater attention to operational risks.

2.2.1 Internal Operational Risk Management

Banks are very friable institutions which are built on customers' trust, brand reputation and above all dangerous leverage. In case something goes wrong, banks can breakdown and failure of one bank is sufficient to send shock waves right through the economy. Therefore, bank management must take highest care in identifying the type as well as the degree of its risk exposure and tackle those effectively. The management should allocate necessary budget funds and human resources to operational risk management as their support has a significant impact on the risk management and control surroundings. In larger banks, risk committee that specializes in the management of the bank's risks, and internal control system is set up for the role of observance of the risk, state of affairs and approaches taken for comprehensive risk identification, and maintenance of an efficient internal control system. Such a centralized risk-controlling unit has the authority to lay down pointers and strategies of risk management. Internal operational risks involve issues of human error in processing, fraud, missing a control step, disruption or system failures (software, hardware, telecommunications), act of sabotage or vandalism, noncompliance with law and regulatory requirements, external dispute with employee as a result of discrimination or harassment, new service or change in the current processes (Weber, 2014).

People Risk

For any organization will need to perform a sufficient work force to deliver the objectives. When a firm is under operated, it results to higher workload resulting to hazards from poor experience and time. The continuum includes cases such as improper handling due to inadequate skills, clerical errors, and incorrect inputs in IT systems, omissions, or errors due to work-related or personal stress, etc. Employees need the skills to successfully do their jobs, and these skills are important for people, businesses, and communities.

Institute of Bankers Malaysia (2014), highlight that talent needed in investment banks requires employees to have the ability to interpret various risks, while organizing products and steering daily operations. The banking sector requires employees to possess the desired ethical behaviors to mitigate the against risk although Childress (2014) states that in the period between 2008 and 2013 the industry has been penalized and paid fines of about \$150 billion cases involving unethical and fraudulent practices.

According to Mohamed (2013) says that negligence in performance of duties or misconduct by employee arises due to failure of the worker to discharge of his duties with care. This may include tasks that involve rendering service towards the consumer; obeying set law and instruction; and duty to apply reasonable competence and skill among other prescribed descriptions of the job. According to Gee and Button (2015), financial report over the past years numerous form of misconduct by banking industry have been uncovered in the UK. Despite the mentioned challenges, the increasing globalization calls for more interaction among individuals from varied backgrounds. Employees are now a portion of a universal economy and have to compete effectively within a global context. For this reason, firms should adopt diversity to remain competitive although at the same time, managing diversity possesses a significant challenge that managers must adapt skills to accommodate in the work environs (Kelli, Mayra, & Allen, 2016).

Process Risk

Process risk is a loss in revenue as a result of ineffective and/or inefficient processes. Ineffective processes hamper the achievement of the organization's objectives, whereas the processes that are inefficient, may be successful in achieving objectives, yet fail to consider high costs incurred. Process Risk is considered to be a sub-component of operational risk. It exists when the process that supports a business activity lacks both efficiency and effectiveness, which may then lead to financial, customer, and reputational loss. (Wikipedia, 2019)

This form of risk may be present within any stage of a business transactions. For instance, an error in pricing may be seen as loss in sales revenue, while a disruption in the fulfillment process may cause financial losses in terms of production quality and customer relationships. The majority of operational risk events occur due to losses from ineffective processing of business transactions or process management, and from inadequate relations with trade counter parties and vendors. (Wikipedia, 2019)

IT Risk

Cavus, N. & Chingoka, D. N.C. (2015) define banks and financial institutions are now offering many services that benefit their potential and current customers in many ways. Information Technology has also brought about stiff competition wars within the industry. IT also aids the employees of the bank as well as the banks and financial institutions themselves. Operations are now automated making life simpler and easier. Telecommunication Mobile Operators, Internet Service Providers (ISPs), computer hardware manufacturers, software developers, mobile device manufactures and the operating software manufactures have all assisted in the giving the banking sector the much needed boost. Mobile banking customers are at great risk of receiving fake SMS messages and scams from hackers and scammers.

The list of some old and new technologies used in banking today: Automated Teller Machine (ATM), Mobile Banking, Internet Banking, Video Teller Machine (VTM), Secure Short Messaging Service (SSMS), SIM Application-toolkit and

Telephone Banking or Interactive Voice Response (IVR) and so on. The banking sector realises that customers' needs have changed with the advancements in technology and their own needs. Information Technology has allowed for improved banking products, competitive markets, implementation of consistent methods for control of threats and has aided mobile banking services to reach geographic distance and varied markets. Extensive work needs to be done in the acceptance of IT in the banking sector so that the risks are eradicated. To avoid failure regular security checks are also required. Back-up and recovery plans to restore customer confidence in IT. Information systems' audit is a complex function done to assess an information system and providing a qualified opinion about the compatibility that enable a firm use its system to meet the organization's strategic objectives (Cavus, N. & Chingoka, D.N.C., 2015).

2.2.2 External Operational Risk Management

Operational risks are the outcome of the people in charge, the financial system in place, the financial process applied or other external events that can affect a financial institution (Aloqab,A., Alobaidi, F., Raweh, B, 2018). Knežević (2013) contends that external events as a source of operational risk are beyond the control of the banks. Often, there is a higher possibility of customer forgeries and fraud. Banks operate in a working environment that is characterized by corruption, and it is no surprise some clients attempt to forge documentation on their financial results as well as providing false certification on properties (Embrechts et al., 2003).

Natural Disaster

External risk events include natural hazards, both environmental and weather influenced. A natural disaster is a grave event caused by the components in the terrestrial, atmospheric, or terrestrial atmosphere affecting the firm's operation that is capable of causing losses to human life and or property and which, due to the extent of damage, is improbable to be fully accomplished by the enterprise itself (Cornalba & Giudici, 2004).

World Economic Forum states that natural disasters affect firm activities in a variety of ways. They disrupt business operations directly through the loss of lives and

the destruction of buildings and equipment, and indirectly through the impact on firms' transaction partners such as their customers, suppliers, and providers of finance. When banks suffer physical or capital damage as a result of a natural disaster, they may not be able to provide sufficient funds at the same interest rates as before.

Political Disturbances

Political risk should be a concern for almost every organization with assets abroad including banks, investment firms and other financial institutions. Political risk insurance should be a vital part of the risk management program for banks with loans backed by cross-border assets or foreign governments, investment firms seeking to expand globally and other financial institutions with global exposures (Josh Bradford, 2013). As Mrs. Kobayashi notes, the desire to become world economic hubs has led some developing countries to adopt more business friendly policies. A growing number also have more stable and reliable business environments as regulations and controls are introduced. But despite these developments, many fast-growing countries are still considered developing economies with political, legal and financial systems that often are volatile compared to the standards of more developed economies. Consequently they expose foreign investment to a higher degree of risk from such things as civil disturbances, export/import embargoes, expropriation of assets, currency convertibility restrictions, and arbitrary changes in regulations.

Fraud

Fraud may generally be characterized as an intentional act, misstatement, or omission designed to deceive others, resulting in the victim suffering a loss or the perpetrator achieving a gain. Fraud is typically categorized as internal or external. Internal fraud occurs when a director, an employee, a former employee, or a third party engaged by the bank commits fraud, colludes to commit fraud, or otherwise enables or contributes to fraud. External fraud consists of first-party fraud and victim fraud. External fraud is committed by a person or entity that is not a bank employee, a former employee, or a third party engaged by the bank. First-party fraud occurs when an external party,

including a bank customer, commits fraud against the bank. Victim fraud occurs when a bank customer or client is the victim of an intentional fraudulent act. Banks with significant and far-reaching retail-oriented business activities should have well-documented fraud risk management programs with appropriate monitoring, measurements and reporting, and mitigation (OCC Bulletin, 2019).

2.3 Risk Management Process

The risk management process can be summarized with the following three steps:

1. Identifying and assessing the potential risk in the banking business,
2. Developing and executing an action plan to deal with and manage these activities that incur potential losses,
3. Continuously reviewing and reporting the risk management practices after they have been put into action/operation.

The overall purpose of the risk management process is to evaluate the potential losses for the banks in the future and to take precautions to deal with these potential problems when they occur. (Turgut Türsoy, 2018)

2.4 Operational Risk Management on Financial Performance

A well-established and managed banking sector can absorb major financial crisis in the economy and can provide a platform for strengthening the economic system of the country (Aburime, 2009). Bank financial performance is vitally important for all stakeholders, such as the owners, the investors, the debtors, the creditors, the depositors, the managers of banks, the regulators and the government (Podder, 2012). Financial performance is the level of performance of a firm over a specific period of time and expressed in terms of the overall profits or losses incurred over the specific period under evaluation (Bodie, Kane and Marcus, 2005).

The most common measure of bank performance is profitability. Profitability is measured using the following criteria: Return on Assets (ROA) net profit/total assets 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 profitable the bank. Return on Equity (ROE) net profit/ total equity. ROE is the most important indicator of a bank's profitability and growth potential. It is the rate of return to shareholders or the percentage return on each of equity invested in the bank. Net Interest Margin (NIM) Net interest margin measures the gap between the interest income the bank receives on loans and securities and interest cost of its borrowed funds. It reflects the cost of bank intermediation services and the efficiency of the bank. The higher the net interest margin, the higher the bank's profit and the more stable the bank is. Thus, it is one of the key measures of bank profitability. However, a higher net interest margin could reflect riskier lending practices associated with substantial loan loss provisions (Khrawish, 2011).

Risk management is all about making right decisions that contribute overall achievements of a firm's objectives by applying them both to functional areas and individual activity. Therefore, ensures mission, vision, and goals are met due diligence, accountability, innovation and responsible risk-taking. Safety management subsumes all activities relating to the organization, planning, supervision of work activities and administration. For better management of operational risks in banks, there is the need to comply with both the national and international regulations and procedures. The period during and after 2008 was important in providing insight on how important operational risk management is vital to financial institutions and how best these risks can be managed (Aloqab.A , Alobaidi.F & Raweh.B, 2018).

2.5 Previous Study of the Framework

According to Basel Committee on Banking Supervision (BCBS), the Basel II defines operational risk as the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events and clearly indicates that

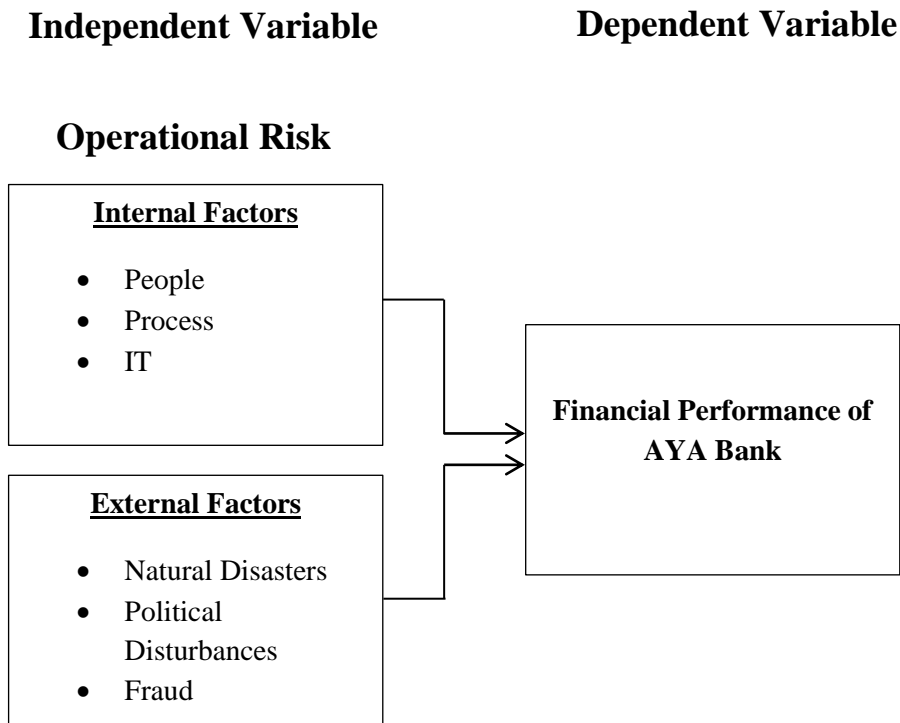
operational risk is now considered as including both internal errors and external influences.

According to Dr. Laurence M Crane says that measurements for financial analysis are grouped into five categories: liquidity, solvency, profitability, repayment capacity and financial efficiency. Four useful measures of farm profitability are the return on farm assets (ROA), the rate of return on farm equity (ROE), operating profit margin and net farm income. The ROA measures the return to all farm assets and is often used as overall index of profitability and the higher the value, the more profitable the farm business. The ROE measure the rate of return on the owner’s equity employed in the farm business.

2.6 Conceptual Framework of this Study

The conceptual framework for the study is constructed based on the Basel Committee on Banking Supervision (BCBS) and Dr. Laurence M. Crane. This conceptual framework describes as follow.

Figure (2.1) Conceptual Framework of this Study



Source: Own Compilation from BCBS & Dr. Laurence M. Crane

In this framework, independent variables are namely internal factors and external factors. Internal factors are caused by people, system, information technology and external factors are caused by natural disasters, political disturbances, frauds etc; have a significant on the effects on financial performance of the bank.

CHAPTER III

PROFILE OF AYA BANK

This chapter is given detail profile of AYA Bank. The background history of AYA bank, branch network, products and services, organization structure and internal and external operational risk management practices of AYA bank are explained.

3.1 History of AYA Bank

AYA Bank is the second largest commercial bank in Myanmar with branch network, Asset size and deposit amount. AYA bank commenced operations on 11 August 2010 with the opening of the Naypyitaw Head Office, and had grown rapidly since then. At the end of 2019, AYA Bank has 258 branches. The stakeholder of AYA bank are proud and honored by continuously receiving the “Best Private Bank in Myanmar” award from 2013 to 2017. AYA bank rapidly improving its corporate governance, risk management and compliance measures by adopting global best practices. The bank has also attracted and retained talented staff with both domestic and international exposure and has invested significantly in Learning & Development as a way to ensure long-term sustainable growth for the communities it serves.

AYA Bank is also the first bank in Myanmar to introduce Centralized Core Banking System (access to data), the first to introduce mobile and internet banking platforms (democratization of financial services), the first to adopt International Financial Reporting Standards (IFRS – standardized financial transparency) and to undergo international audit (Deloitte). This is evidence of commitment across all levels of the organization. AYA bank's management believe that every individuals of the bank plays an important role and it is necessary to provide them with continuous training and upgrading of skills. AYA bank has own training school offering on-job training and in-house programmes.

AYA bank has been expanding its branch network and creating numerous job opportunities to people across the country. AYA bank's total employee headcount has

increased from 1,130 people as at 31 March 2012 to over 8500 as at 31 Nov 2019. Continuous training are being provided to the staff in AYA Bank to build their capacity and to upgrade their skills. Within 10 years, AYA Bank can expand the branch network 258 branches around Myanmar. The following table shows the branch network progress of AYA Bank. AYA bank expands all the states and divisions the whole Myanmar.

Table (3.1) AYA Bank Branch Network

No.	Financial Year	No. of Branches
1	2009 - 2010	5
2	2010 - 2011	13
3	2011 - 2012	12
4	2012 - 2013	24
5	2013 - 2014	46
6	2014 - 2015	32
7	2015 - 2016	68
8	2016 - 2017	34
9	2017 - 2018	8
10	2018 - 2019	16
Total		258

Source: www.ayabank.com

According to this table, AYA bank branch network increases from 2010 to 2019. The highest growth rate is in 2016. At that time, AYA bank expands its branch network very rapidly within a year. It shows that AYA Bank can manage the human resource effectively. It can be a good recruitment and selection procedures and retaining the existing talented candidates in AYA Bank. The expansion of branch network needs much more capital investment. It shows that AYA Bank has sufficient capital investment, can get the public trustworthiness. Due to the public trustworthiness, the deposit amount of AYA bank grows significantly, year by year.

3.2 AYA Bank Products and services

AYA bank is the fastest growing bank in Myanmar Banking industry, AYA bank can provide many banking services based on the dynamic economic and customers' requirements. The products and services can be categorized as: Daily banking services,

Loans and advances, Local and Global remittance services, Cash Management, Card Payment services, E banking services, Trade services, AYA Royal Banking services and other services including Foreign Exchange services and Safe Deposit Boxes.

3.2.1 Daily Banking services

AYA Bank daily banking services are including the traditional banking services as well as modern banking services. The daily banking services are namely as : Current Account, AYA Foreign currency account, AYA Seafarer saving account, AYA Saving account, AYA Interest Maximizer account, AYA Loyal account, AYA Fixed Deposit and AYA Premium saving account. Among these services, Current Account, Foreign Currency account are not provided the interest. The rest products can be got the interest rate from 8% to 10% per annum respectively based on types of account, bank's policy and practices.

3.2.2 Loans and Advances

AYA Bank Loans and Advances are including Lien Letter (Lien Letter is an agreement letter in which Bank has a Borrower's consent to obtain or control their deposits or receivable account when there is an absent of repayment of loan or their obligations. It is suitable for the individual who want to borrow money by giving their savings account as a collateral. Project Financing (AYA Bank will provide long term financing of business's infrastructure, industrial projects and public services based on your cash flows of the projects). Invoice Financing (AYA Bank shall give the cash in advance to get better cash flow for trading businesses. The sellers or buyers may discount their invoices to obtain better liquidity. The bank may provide short-term advanced money to companies' receivables or help them pay their due invoices). Floor Stock Financing (Floor Stock Financing of AYA Bank is mainly targeted at the automobile industry in which Automobile Dealers are able to pledge their vehicles with AYA Bank and get required finance for their businesses, enabling better liquidity). AYA Bank also provided AYA Home Loan , Education Loan and Auto Loan to meet the requirements of people and to get the high living standard.

3.2.3 Remittances

AYA Bank provided Local online remittance service (A telegraphic transfer is the quickest means whereby the beneficiary generally receives payment within 24 hrs of dispatch in local or foreign currency.), World remit (AYA World Remit allows you to send money easily and securely to your friends, family and business partners around the world simply and affordably.), SWIFT telegraphic transfer (A very fast, safe and reliable way of transferring money between two persons or entities anywhere in the world through use of AYA's wide correspondent relationships and the SWIFT network)and AYA Payment Order (Payment order is a form of payment settlement to individual, company and associations. It can be purchased at any AYA branches. Payment order is designed as a normal payment order to pay a particular amount for a third party that is not a Bank).

3.2.4 Cash Management

AYA bank served the cash management services as Receivable Management (Collect payments quickly and manage your account receivables efficiently with AYA Collection Services), Payable Management (Manage and control your account payables efficiently and easily with our full range of payment solutions) and Liquidity Management (Improve and optimize your liquidity through automated sweeping of funds).

3.2.5 Card Payment

Myanmar is cash based society. Myanmar is almost fifty years use the close economy, before 2010. After 2010, the demanding power of new banking services, AYA bank introduced the well-known and famous cards such as Master card, VISA card, Union Pay card and Myanmar Payment Union card, Credit card and Visa credit cards.

3.2.6 E Banking Services

AYA bank has been offering E banking services such as internet banking and mobile banking that allows bank users to manage their accounts on computers, tablets, or mobile phones via the internet. Through online banking, users can make basic banking functions such as balance inquiry, fund transfer, bill payment, etc., without having to come the banks in person. By allowing customers to manage their money more quickly and efficiently at any place and any time, it provides a much more convenient way for customers to deal with banks.

3.2.7 Trade Services

AYA bank already giving the Trade services such as Export Services (Letter of Credit Advising and Negotiation, Pre and Post Shipment Financing, Outward Documentary Collections), Import Services (Opening of Letter of Credit, Inward Documentary Collections, Trust Receipts, Shipping Guarantee), Bank Guarantee (These are issued for common commercial or statutory requirements, including contract tenders and payment guarantees).

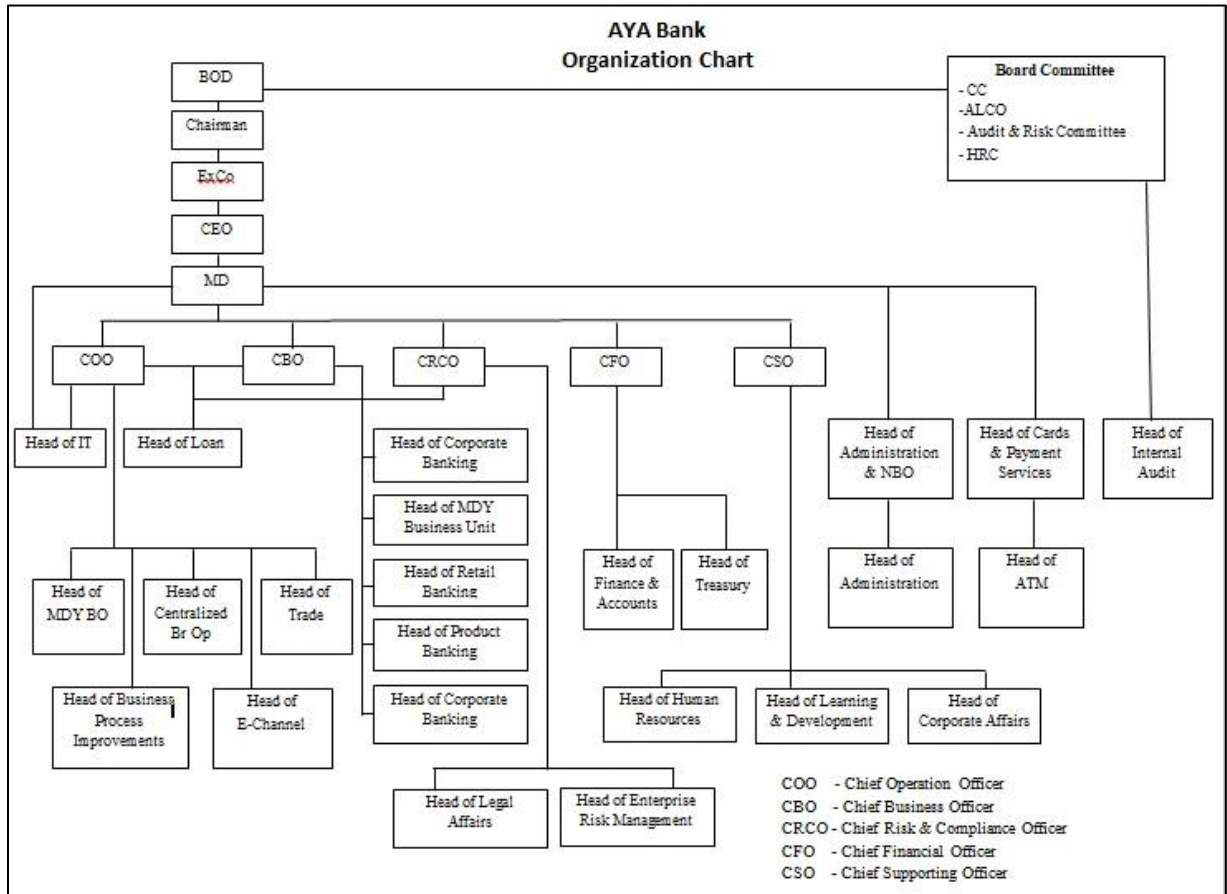
3.2.8 Royal Banking

AYA Royal Banking is an exclusive membership that provides premium benefits for our high valued customers. We dedicated for long time sustainable investment; and relationships beyond banking.

3.3 Organization Structure of AYA Bank

The following figure shows the organization structure of AYA bank. There are 9 Directors on the Board of Directors, these include the Executive Chairman, the Managing Director, four other Executive Directors and three Independent Non-Executive Directors. The roles and responsibilities of Board include setting the corporate direction and strategic aims, reviewing management performance and establishing a framework of prudent and effective control.

Figure (3.1) Organization structure of AYA Bank



Source: AYA bank annual report (2016-2017)

Figure (3.1) shows that BOD is the leading row. Guided by the Board’s strategic objectives, the chairman will articulate the corporate direction set by the Board. Chairman is a motivator and leads the Bank in communicating and demonstrating the Bank’s corporate values. Managing director oversees day-to-day operations and is directly responsible for raising the profitability and profile of the bank and ensuring that effective risk management and operational controls are implemented at the ground level. Under the Managing Director, there are five Chief level officers. Chief level officers control and manage the day to day operations to be achieve the organization’s goals.

3.4 Internal and External Operational Risk Management Practices of AYA bank

AYA Bank recognizes that an effective risk management system must be in place to mitigate various risks to the bank operations. AYA Bank adopts the risk management policy to affirm its awareness of the need to establish a program for Enterprise Risk Management (ERM). The Board further commits to providing sufficient personnel and other resources to ensure full implementation of an enterprise risk management program. Top management of AYA bank is responsible for all the risks of the bank, planning and implementing its risk strategy. Therefore, the management should assign necessary budget and human resources to operational risk management. In AYA bank, audit and risk committee that specializes in the management of the bank's risks and internal control system.

Internal operational risk involves human error in operation, fraud, missing a control steps, software and hardware system failure, incorrect processing due to inadequate skills, clerical mistakes, and wrong inputs in IT systems, errors owing to work-related or personal stress. AYA bank issued the instructions and set the policies to reduce the internal operational risks. Operations manual includes policies and procedures for the concerned business and a support unit comprises of the key operational controls to mitigate key operational risks from the process.

Moreover, any proposed mitigation plans for key risks are appraised by the Enterprise Risk and Management, Human Resources Management, Head of Internal Audit before escalation to the senior management and incorporating the same in the operations of the concerned business and support unit. Implementation of the existing and proposed policies and procedures are monitored by the operations group along with audit and compliance. The effectiveness of operational risk management and the quality control of the internal control system may be affected by the functioning of the BOD and the organization.

To cover the external operational risks, AYA bank takes the insurance by the elements like fire, external risk events include flood and earthquake. It is necessary to design measures for safety of employees and clients affected by the risk. AYA bank has constructed a bank building's earthquake safety depends on its height, year of

construction, structure, use in it ground and vertical plan duration of an earthquake. Special measurements taken by the bank for natural disasters depend on local conditions and range from measures to secure buildings and assets to plan for continuing business operations. All risk managers identify the major importance of risk management to the banks performance.

Successful business is depend on the getting knowledge, skill and capability of the persons involved in the business processes. Sound policies and procedures for risk management practices are critical in the management of the bank. AYA bank is clearly defined its vision "To be recognized as the leading bank in Myanmar through pursuit of excellent and long term sustainable growth for the bank and its stakeholders". AYA bank plans to establish a socio-economic program to develop a Banking and Finance Institute as a center of excellence in Myanmar.

CHAPTER IV

ANALYSIS ON EFFECT OF OPERATIONAL RISK MANAGEMENT PRACTICES ON FINANCIAL PERFORMANCE OF AYA BANK

This chapter shows the outcomes of the study and their interpretations. This chapter includes on the demographic data of the respondents such as gender, duration of employment, employee level and education level, analysis on internal operational risk management practices, external operational risk management practices and financial performance of AYA bank.

4.1 Demographic Profile of Respondents

The demographic profile of respondents are divided into two. They are respondents and non respondents.

Table 4.1 Response Rate

	Number of Respondents	Percentage
Respondents	92	92
Non Respondent	8	8
Total	100	100

Source: Survey Result

According to Table (4.1) shows the total number of respondents are 100 and only 92 respondents were filled and returned. This represents a response rate of 92% .

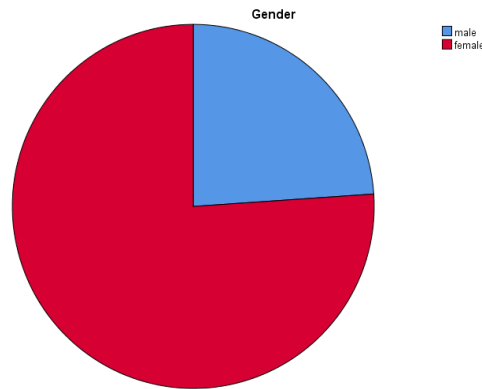
4.2 Demographic Information of Respondents

In demographic characteristic of respondents, the gender, duration of employment, management level and level of education of respondents are shown in as follow.

4.2.1 Gender of Respondents

The samples of 92 respondents are categorized by their genders as shown in Fig (4.1).

Figure (4.1) Gender of Respondents



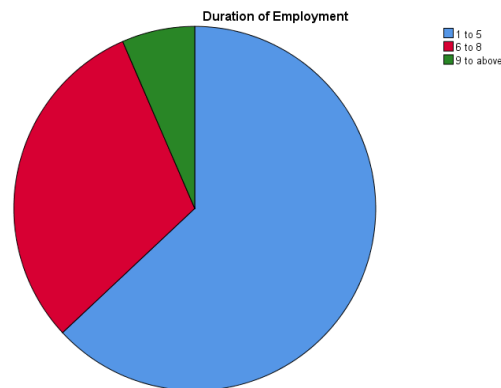
Source: Questionnaires Result

This figure shows the data according to Gender of respondents. Out of all the respondents surveyed, 76% of the respondents are female and 24% of the respondents are Male.

4.2.2 Duration of Employment

The study finds out to know for how long the respondents had worked in AYA bank. In this study, there are three groups of banking service years such as 1-5 years, 6-8 years and 9 years and above.

Figure (4.2) Duration of Employment



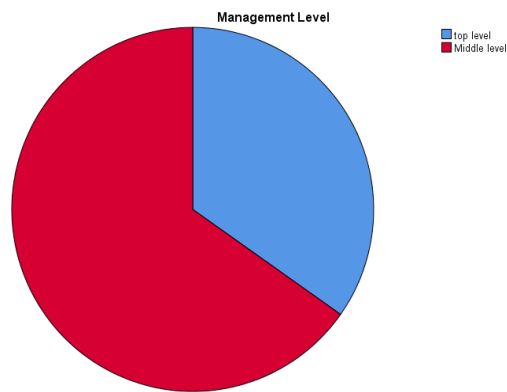
Source: Questionnaires Result

According to the figure (4.2), the respondents with the highest proportion were employees who have been at the bank between 1-5 years at (63%), those of between 6-8 years (30%) and those of 9 years and above had (7%).

4.2.3 Management Level

In this study, there are three categories for management level in questionnaires. There are top level, middle level and low level. The following figure shows the management level of the respondents.

Figure (4.3) Management Level



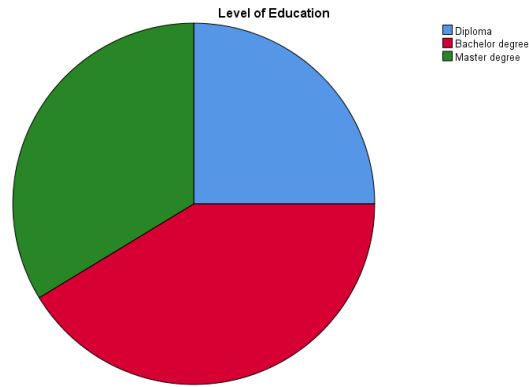
Source: Questionnaires Result

From the findings, the respondents with the highest proportion were employees in the middle level at (65%) and those of top level at (35%). These are shown in figure (4.3).

4.2.4 Level of Education

In this study, there are four categories for education level in questionnaires. There are certificate level, additional diploma level, bachelors' degree level, master degree level. There is no certificate level in the respondents. The following figure shows the education level of the respondents.

Figure (4.4) Level of Education



Source: Questionnaires Result

From the figure (4.4) the respondents with the highest proportion were employees with a bachelor's degree (41%), master degree (34%) and those of respondents were getting the additional diploma (25%).

4.3 Internal Operational Risk Management Practices

This research obtained data on the effectiveness of internal operational risk management practices by using a Liker Scale. The respondents were asked to indicate their perception about people risk, process risk and IT related risk. Internal operation risk management factors are based on People, Process and IT system in AYA bank.

4.3.1 Internal Factors caused by people

For any organization, there need to perform well a sufficient work force to meet the objectives. In the banking sector, employees have to possess ethical behaviors, have to follow the policies and procedures to reduce the risk in banking operations. The following table shows the influencing factors, mean and standard deviation.

Table (4.2) The Internal Factors caused by people

NO.	Factors	Mean	Std. Deviation
1	Employees at AYA bank have the necessary skills to perform their work effectively	4.14	1.280
2	Employees at AYA Bank possess ethical behaviors necessary to mitigate the bank against people risk	3.92	1.207
3	Staff have to comply with policy requirement of the Bank	4.09	1.065
4	The bank has recorded cases of dishonesty among its employees	4.30	0.992
5	Some officials with a supervisory responsibility don't misuse it for their personal benefit	3.98	1.301
6	AYA Bank has a wide diversity of employees in the working environments	4.27	0.996
7	Senior management provide with clear guidance and direction regarding the operational risk management processes	4.49	0.883
	Overall Mean Value	4.17	1.10

Source: Survey result (2019)

According to the Table (4.2), the largest mean value is 4.49. This means that senior management provide with clear guidance and direction regarding the operational risk management processes was one of the important factor out of influencing factors. The lowest mean value is 3.92. This means that employees at AYA Bank possess ethical behaviors necessary to mitigate the bank against people risk.

4.3.2 Internal Factors caused by process

Bank's operations are strengthened through variety of systems and processes, like human resource, information technology, credit, market and liquidity risk management system. Weak designed system and processes can also lead to operational losses. This section consist of six factors to find out which are influenced factors on the process.

Table (4.3) The Internal Factors caused by process

NO.	Factors	Mean	Std. Deviation
1	AYA bank has a strong operational risk management culture exists throughout the whole industry	4.32	0.755
2	AYA bank adopt policy decisions concerning the operations of the bank and establish adequate and functioning internal control mechanisms	4.45	0.761
3	AYA bank give the right training to help in lowering operational losses.	4.53	0.818
4	AYA bank's operational risk management policies and procedures are secured and followedup	4.30	0.861
5	AYA bank has the effective internal control system to reduce the operational losses.	4.09	1.164
6	Policies and Procedure of AYA bank help to get the strong ORM practices	4.21	0.908
	Overall Mean Value	4.32	0.88

Source: Survey result (2019)

According to the Table (4.3), the maximum mean value is 4.53. This means that AYA bank give the right training to the employees by their the management level. This is one of the important factor out of influencing factors. The minimum mean value is 4.09. This means that AYA bank has the effective internal control system to reduce the operational losses.

4.3.3 Internal Factors caused by IT system

Every company need to upgrading, improving and checking out its information system, especially in banking industry, to meet the users wants, market competition and regulatory adjustments. This section consist of nine factors to find out which are influenced factors on information security system.

Table (4.4) The Internal Factors caused by IT

NO.	Factors	Mean	Std. Deviation
1	AYA bank has experienced system disruptions which have interrupted business	2.97	1.537
2	Reasonable security measures have been put in place to prevent unauthorized access to the banks network	4.13	1.242
3	AYA bank has experienced unreliable hardware and or software issues	2.60	1.576
4	Staffs are given good practice guidance on password security	4.28	1.009
5	AYA Bank has suffered financial losses from acts of IT related risks	2.93	1.568
6	Internal Audit Department regularly conducts system audit	3.86	1.173
7	The volume of transactions consistently exceeds the technology's ability to deliver	4.25	0.909
8	Functionality of systems have not been aligned with business objectives	2.55	1.455
9	AYA bank has the effective monitoring system with IT related risks	4.26	1.057
	Overall Mean Value	3.54	1.28

Source: Survey result (2019)

On analyzing the results, the largest mean value is 4.28. This means that all the employees of the bank are given good guidance and policies on password security. The lowest mean value is 2.55. This means that functionality of systems have not been aligned with business objects. It can be conclude that AYA bank set the rules and regulations for systems effectively and meet the business objectives.

4.4 External Operational Risk Management Practices

The research obtained data on the effectiveness of external operational risk management practices using a liker scale, the respondents were asked to indicate their perception about the effectiveness of external operational risk management practices.

The external operational risk management practices are considered based on Regulatory requirement, Customer preferences and External factors. This section consist of seven factors to find out which are influenced factors on external effects.

Table (4.5) External Operational Risk Management practices

No .	Factors	Mean	Std. Deviation
1	Some AYA Bank clients have failed to comply with contractual arrangements	2.60	1.576
2	Clients and counterparties of the bank make known sensitive and confidential information to third parties without authority to do so.	2.93	1.568
3	Changes and restrictions in the regulatory environment have a significant impact on the banks	2.65	1.270
4	AYA bank has had initiatives of competitors that have influenced product offering of the bank	3.86	1.173
5	AYA bank has experienced negative reporting in the press on the activities of the bank and its employees	2.07	1.324
6	AYA bank has experienced financial losses caused by political disturbances	1.55	0.930
7	AYA bank has experienced financial losses caused by natural disasters.	1.50	1.074
	Overall Mean Value	2.45	1.27

Source: Survey Result (2019)

Table (4.5) represents the analysis on the seven studies factors of influencing on external factors of AYA bank. The maximum mean value is 3.86. This means that AYA bank has had initiatives of competitors that have influenced product offering of the bank. The minimum mean value 1.50 means that AYA bank has experienced financial losses caused by natural disasters. It can be concluded that it is one of the challenges to get the initiatives of competitors to offering the products and services of the bank. AYA bank is very innovative and initiative in offering new products and services.

4.5 Financial Performance of AYA Bank

Most of the firms use past and present financial performance as the measurements of how well the firm is operating but they focus on the performance of other firms. To

measure the financial performance, the ratios are used as proxies growth of sale, Return on Assets, Return on Equity and Return on Investments. The effectiveness on financial performance are considered based on internal and external operational risk managements practices of AYA Bank.

Table (4.6) Financial Performance

No.	Factors	Mean	Std. Deviation
1	Employees performance of AYA Bank can result the higher income to make a profit.	4.41	0.698
2	Senior Management have the right decisions and set the financial guidelines to get the better financial performance.	4.39	0.695
3	People's errors in banking operation can lead to weak financial health of AYA bank.	3.79	1.245
4	Organizational Performance can reflect the positive impact in financial performance of AYA bank	4.12	0.947
5	IT system errors in banking operations can cause the weak financial profit.	2.92	1.557
6	Polices and practices related with IT system are secure and update to run the banking operations.	4.50	0.584
7	IT security system of AYA bank can protect internal and external fraud.	3.83	1.228
8	Natural disasters faced by AYA bank can cause the financial losses.	2.24	1.440
9	AYA bank has experienced with the external fraud like robbery and burglary.	1.64	0.566
10	AYA bank has the strong protection plan for bank building and assets against by flood and earthquake.	4.26	0.709
	Overall Mean Value	3.61	0.97

Source: Survey result (2019)

According to the research Table (4.6), the largest mean value is 4.50. This means that AYA bank's polices and practices related with IT system are secure and update to run the banking operations. The lowest mean value is 1.64. This means that AYA bank hasn't experienced with the external fraud like robbery and burglary. It can be concluded that AYA bank has strong financial performance by building the efficiency work load and getting the individuals competencies and AYA bank fully comply the instruction and guidance issued by Central Bank of Myanmar.

4.6 Overall Mean Values of Operational Risk

The following table shows the overall mean values of operational risks.

Table (4.7) Overall Mean Values of Independent Variables

No.	Statement	Mean	Std Deviation
1	Internal Factors	3.95	1.11
2	External Factors	2.45	1.27

Source: Survey Results, 2019

According to Table (4.7), the maximum mean value 3.95 was internal factors and the minimum mean value 2.45 was the external factors. It can be assumed that internal factors are the most important factor on financial performance.

4.7 Analysis on Effective of Internal and External Operational Risk Management Practices on Financial Performance

This table shows the model summary and ANOVA table of the result.

Table (4.8) Model Summary and ANOVA Table

Model Summary				
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.993 ^a	0.986	0.986	1.03857

a. Predictors: (Constant), External, Internal

ANOVA ^a						
Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	6938.916	2	3469.458	3216.560	.000 ^b
	Residual	95.998	89	1.079		
	Total	7034.913	91			

a. Dependent Variable: Financial performance

b. Predictors: (Constant), External, Internal

According to Table (4.8), the value of R square was 0.986 and adjusted R square was 0.986 which indicates that the independent variables can count more than 98.6% of variance in dependent variable. The F-ratio was 3216.560 ($p < 0.000$) which indicates that the regression analysis was statistically significant overall.

Table (4.9) Coefficient of Influencing Factors on Financial Performance

Coefficients						
Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	6.552	0.499		13.142	0.000
	Internal	0.269	0.009	0.692	28.866	0.000
	External	0.360	0.026	0.334	13.903	0.000

a. Dependent Variable: Financial Performance

As shown in Table (4.9), linear regression was conducted to examine the effect of operational risk management practices on financial performance. The two factors of internal ($b = 0.269$, $t = 28.866$, $p < 0.001$), external ($b = 0.360$, $t = 13.903$, $p < 0.001$) were significant in predicting financial performance. For the regression coefficient and significant level of each independent variable, it can be seen that all variables, internal and external factors have a positive impact on financial performance (coefficient of 0.269 and 0.360) at the statistical significant level of 1 percent and 1 percent (p -value=0.000, and 0.000).

CHAPTER 5

CONCLUSION

This chapter presents the research study summarizing key findings, suggestions and needs for further study of this study. The research was targeted on the effect of operational risk management practices on financial performance of AYA Bank.

5.1 Findings

The purpose of this study was to investigate the effectiveness of operational risk management practices of AYA bank. The research was proposed the following objectives: to identify the internal and external operational risk management practices of AYA Bank and to analyze the effect of operational risk management practices on financial performance of AYA Bank. The target population of this study was AYA employees in the Head Office and branches in Yangon. The data obtained was analysed through Microsoft excel. Both qualitative and quantitative data was analysed and the results presented in percentages, means, standard deviations and frequencies.

The demographic characteristics of respondents in the study are explored according the variables such as gender, working experience, management level and education level. Regarding with gender, majority of respondents are female. According to the working experience, respondents who have working experience 1-5 years portion is the largest and the respondents who have working experience 9 years and above portion is the smallest. According to the management level, respondents who are working in middle level share is the largest and the respondents who are working in top level share is the smallest. According to the education level, the largest proportion is respondents who got bachelor degree and the smallest proportion is additional diploma.

The first objectives of the study was to identify the internal and external operational risk management practices of AYA Bank. The findings found that most of the respondents greatly agreed that AYA bank give the right training and seminars to their employees by their management level. Another finding is that AYA bank's senior management provide with the clear guidance and direction regarding the operational risk

management processes. AYA bank establish policy decisions concerning the operations of the bank and establish adequate and functioning internal control mechanisms. Therefore, AYA bank has the effective internal control system and strong operational risk management culture. Most of the respondents greatly disagreed that AYA bank has experienced unreliable hardware and software issues and has suffered the financial losses from acts of IT related risk. Moreover, the respondents disagreed that AYA bank has experienced financial losses caused by political disturbances and natural disasters.

The second objectives of the study was to analyze the effect of operational risk management practices on financial performance of AYA Bank. Most of the respondents are greatly agreed that AYA bank has effective policies and procedures related with IT system are secured and updated to run the banking operations. Another influence factors is that AYA bank's employee performance can result the higher income to make a profit. Most of the respondents disagree that AYA bank has experiences with the external fraud like robbery and burglary and AYA bank's IT system can cause the weak financial profit. According to the analysis result, internal and external factors have a positive impact on financial performance.

5.2 Suggestions

AYA bank is the second largest private bank with nationwide presence, providing a full suite of corporate, retail and commercial banking products and solutions for both local and international customers; through the extensive branch network present in every state and division of the country. Leveraging on technology and differentiated customer service has been key to rapidly growing the customer base.

Employees need not only giving initiatives customer services and also a productive relationships with their coworkers to get the objectives of the banks. AYA bank needs more diversity of employees and should give more ethical training program to create ethical workplace. AYA bank has a positive perceptions on ethical culture and set the instructions to meet the financial goals. Another finding was that AYA bank has recorded the dishonesty cases among its employees and need more effective action taking to make the well management for implementing the operational risks management

practices. In addition, internal audit department should more examine of the management control within an information technology infrastructure. According to the results, both internal and external factors are the influencing factors for measuring the effective on the financial performance. Therefore, guidelines and procedures provided by the AYA bank on operational risk management should be fully observed into to ensure the risk is well mitigated and improvement in financial performance.

5.2 Need for Further Studies

This study concentrated only on the effectiveness of internal and external operational risk management on financial performance of AYA bank. It is endorsed that another studies be done to determine how operational risk management affect the reputational risk and liquidity risks of the organization. This study only concentrated on one bank and therefore this result are skewed and data from AYA bank. Thus, all private banks should be explored as a further study in order to know the effect of operational risks on financial performance. A further study could also be undertaken in other industries such as manufacturing, distribution and profit and non-profit institutions to help drive the implementation and management of their strategies.

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