RISK MANAGEMENT POLICIES

Liquidity Risks

Liquidity risk is the risk arising from not having adequate cash or not having adequate cash inflows to fund cash outflows on time due to to imbalance of cash flows.

Treasury Department, manages liquidity of the bank on a daily basis and informs the asset-liability committee every week about the Bank's liquidity level. Planning the liquidity management for weekly, monthly, yearly periods, taking the neccessary measures and informing the senior management about these is the responsibility of the treasury unit.

The Bank forms its assets and liabilities in balance in order not to create a negative space in the cumulutive basis in the maturity periods.

The bank has an liquidity and contingency funding plan for unexpected emergiencies. The bank monitors liquidity risk with early warning signals. Possible liquidity senarios and severity of risks are defined for every stres level.

For assets to provide and maintain the adequate liquidity to cover the liabilities in order to manage the liquidity risk in the Bank, total liquidity adequacy ratio and foreign currency liquidity adequacy ratios are calculated as of the term dates.

The weekly liquidity analysis, which is among the most important agenda topics of the weekly meetings held by ALCO, is controlled by Internal Control Unit. In accordance with the Committee resolutions, it is ensured that the liquidity analysis is managed under coordination of Treasury and Financial Planning units and under supervision of Internal Systems Group.

The Bank's Financial Planning Unit monitors the interest rate risks , calculates and reports the liquidity adequency ratio and measures the leverage ratio. Risk Management Unit applies stres tests and senario analysis. Internal Control Unit monitors compliance with policies, limits and indicators in relation to the liquidity.

Market Risks

Market risk is followed under two headings; market risk arising from trading activities and market risk arising from banking instructions. The basic principle of market risk management is creating a compliant asset/liability structure and providing protection by averting differences with derivative instruments when necessary.

By the Board of Directors, market risk limits introduced by the minimization of the risks involved were targetted. Defined risk limits are reviewed by the Board of Directors in 3 month period and updated if necessary. Standard method is used in the measurement of market risk in the extent of capital adequency ratio. Value at risk of the securities portfolio is monitored and is reported to senior management on a monthly basis.

The market risk arising from trading portfolio is monitored, measured and reported using Standard Approach according to the legal legislation. The monthly market risk report and the weekly currency risk reports prepared using Standard Approach are reported to BRSA.

Interest rate risk is the risk that expresses the effects of fluctuations in the market interest rates on the value increase/decrease of the Bank’s interest rate sensitive assets and liabilities.

The interest rate sensitivity of Assets, Liabilities and Off-balance sheet items is carefully followed up by the treasury department of the Bank. Assets and liabilities which are sensitive to interest are managed in such a way that minimizes the interest risk.

The interest rate risk of the banking items is measured legally in accordance with the “Regulation on Measurement and Assessment of Standard Shock Method on the interest rate risk arising from banking accounts”, and this legal limit is monitored and reported monthly, based on this measurement.

Credit Risks

Credit risk is the risk that a customer or a counterparty fails to comply with the agreement’s requirements and cannot perform its payment obligations.

The Bank, for the loans to be granted to a single borrower or Bank to be applied in risk limits are based on the regulations of the Banking Law. In order to avoid sectorial concentration, limits have been defined and adherence to limits is monitored on a transaction basis.

Daily loan and securities transactions, adherence to limits and concentration is monitored and reported by the risk management unit. In addition, the value at risk of securities are monitored by Risk management Unit. The compliance of credit risks with the credit limits are monitored by Marketing, Operations and Internal Control units by transaction basis.

Loans and other receivables are subjected to re-evaluation at least once a year by the credit allocation unit, internal borrower and transaction rating models are used for this purpose.

Detective controls are executed by Internal Systems units for lending activities.

Operational Risks

Operational risk is defined as the risk of direct or indirect loss resulting from inadequate or failed internal process, people and systems or from external events.

Operational risk which is inherent in all business activities is associated with human error, system failure and inadequate controls and procedures. Operational risk includes errors and omissions in business activities, internal and external fraud and natural disasters.

The Bank has Risk Management and Internal Control practices to keep operational risks under control and minimize it by operating under detailed written procedures. All documents, including Risk Management policies and contingency procedures, are kept up-to-date and accessible to all staff in electronic media.

Operational risk measurement and reporting is being executed with basic indicator approach and includes operational risk capital requirement. Regarding the operational risk management, our Bank takes out “Bankers Blanket Bonds” policy.

Legal Risks

The Bank operates with an integrated system of legal risk management according to defined targets. In this context; the Bank operates in compliance with laws and regulations, defines, evaluates, controls legal risks, provides compliance between legal risks and bank strategy, ensures relations between Bank employees, customers and the Bank to be consistent with legislative requirements within the legal framework in co-operation with Legal and Compliance Department.

Strategic Risks

The difference between strategic and other banking risks (e.g. credit, currency or legal risks) is the possibility that the Bank may sustain financial losses in consequence of managerial imperfections or incorrect determination of general strategic goals and objectives. Therefore to avoid from against strategic risk is one of the fundamental principles of each department of the Bank.