IDEAS FOR LEADERS | DECEMBER 2018

banking insight

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EXCLUSIVE INTERVIEW WITH LEE LUNG NIEN FELLOW CHARTERED BANKER CEO CITI MALAYSIA

FUTURE-READY LEADERSHIP

A Balancing Act in Trade-Based Money Laundering Compliance

A NEW CYBER FRAMEWORK

GLOBAL FINANCIAL CRISIS DECENNIAL

AT BANKING'S 'TRUE NORTH'?

A decade since the global financial crisis, how much safer are banks today? We review the hits, misses, almost-theres, and future trends.

GREAT TO GOOD

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BLOCKCHAIN-ONLY BOND

The World Bank launched the first blockchain-only bond with Commonwealth Bank of Australia on 23 August 2018. The pioneering two-year debt instrument named bond-*i* – which formally stands for 'blockchain operated new debt instrument' but is likely also a silent nod to the continent's famous beach – raised AUD110 million with investors drawn from Australian banks and state treasuries. The uptake and range of state investors reflect the market's keen curiosity in distributed ledger technology. Increasingly, the World Bank has been piloting experimental proof-of-concepts out of its blockchain innovation lab launched in June 2017. These pilot projects are aimed at leveraging the use of disruptive technologies to achieve its twin goals of poverty alleviation and enhanced living standards. ✱

In the first six months of 2018, GBP503.4 million was **STOLEN BY CRIMINALS THROUGH AUTHORISED AND UNAUTHORISED FRAUD.** ~ UK Finance, *Fighting Fraud: Helping to Keep Customers Safe.*

MALAYSIA UPS ANTE ON INCLUSIVE FINANCE

Bank Negara Malaysia, Malaysia Digital Economy Corporation, and the United Nations Capital Development Fund upped the ante on financial inclusion for the nation's middle- and low-income groups with the launch of the Digital Finance Innovation Hub and Inclusive Fintech Accelerator Program. Launched on 26 September 2018, the hub encourages financial institutions and fintech start-ups to innovate and promote financially inclusive technologies to meet the needs of the underserved in Malaysia. Corollary goals include higher economic efficiency in financial intermediation and cost reduction by providing an expanded menu of options, faster provision of financial services as well as more effective utilisation. ✱

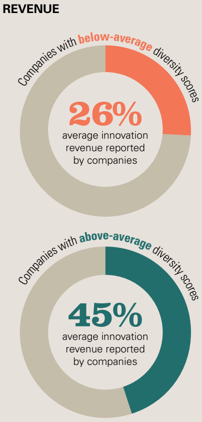
Close to 50% of the adult population in low- and middle-income Asia-Pacific economies **DOES NOT HAVE A BANK ACCOUNT.** ~ IMF, Financial Inclusion in Asia-Pacific.

Diverse Leadership Boosts Innovation

A Boston Consulting Group study suggests that more diverse leadership teams result in more and better innovation and improved financial performance. Companies with above-average diversity in their senior teams clocked significantly better payoff from innovation revenue – 19 percentage points higher compared to companies with below-average leadership teams – as well as higher EBIT margins.

The global consultancy's article, *How Diverse Leadership Teams Boost Innovation,* explained: "People with different backgrounds and experiences often see the same problem in different ways and come up with different solutions, increasing the odds that one of those solutions will be a hit. In a fast-changing business environment, such responsiveness leaves companies better positioned to adapt." ✱

EXHIBIT 1 COMPANIES WITH MORE DIVERSE LEADERSHIP TEAMS REPORT HIGHER INNOVATION REVENUE



SOURCE BCG diversity and innovation survey, 2017 (n=1,681)
NOTE Average diversity score calculated using the Blau index, a statistical means of combining individual indices into an overall aggregate index

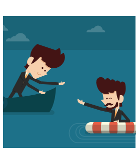
Future-Ready Leadership

BANKING INSIGHT CAUGHT UP WITH LEE LUNG NIEN, CEO CITI MALAYSIA AND A FELLOW CHARTERED BANKER, ON DIGITAL TRANSFORMATION, CLIENT-CENTRIC FINANCIAL SOLUTIONS AND A STRATEGY THAT IS FOCUSED ON SUSTAINABLE GROWTH.

Global Financial Crisis Decennial

AT BANKING'S 'TRUE NORTH'?

A decade since the global financial crisis, **how much safer are banks today?** We review the hits, misses, almost-theres, and future trends.



+ The GFC challenged the theory of 'too big to fail', i.e. that the downfall of certain large, highly interconnected financial institutions would be so disastrous to the status quo that they must be supported by government at any cost.

In 1962, as President John F. Kennedy stood on a podium and announced the winner of a coveted science award, disagreement broke out backstage amongst organisers on how to proceed with the ceremony.

Oblivious that their bickering could be heard over the public announcement system, the president threw a glance over the nervous audience and said drily: "This is the way the administration is really run."

Ten years since the global financial crisis (GFC), time's up for banking to take a leaf out of JFK's book and ask ourselves: "How has this administration really been run?"

Is the financial world any closer to making itself more stable, robust, and ethical?

Here's an overview of the big issues – what we did, didn't and have yet to get right – en route to banking's True North.

TOO BIG TO FAIL

Some survived, some didn't, others grew bigger than before.

The GFC challenged the theory of 'too big to fail', i.e. that the downfall of certain large, highly interconnected

 | BY AMALINA ANUAR

CENTS AND SUSTAINABILITY

SUSTAINABILITY IS INCREASINGLY RELEVANT TO THE FINANCIAL SERVICES SECTOR, DRIVEN BY ETHICS AND PROFIT. HOW HAVE FINANCIAL INSTITUTIONS PERFORMED AND JUST HOW FAR ARE WE BANKING ON SUSTAINABILITY?

Promoting higher levels of financial inclusion is also a positive sum agenda: In addition to potentially reducing poverty, the banking industry can capitalise on the shared prosperity to be gained from serving the global bottom 40% whose spending power is set to nearly double from US$3 trillion to US$5.8 trillion.

FINANCIAL CRIME RISK MANAGEMENT IN ASIA PACIFIC

A RISING COST & URGENT IMPERATIVE

How firms can get a **grip and prioritise.**

Costs for financial crime are rising and financial institutions in Asia are having to bear them. In February 2018, a large state-owned Indian bank was involved in fraudulent transactions of total value exceeding US$2 billion. As a direct cause of the market's reaction to the news, the bank's shares dropped by almost 40% of its market value in three weeks.

This happened due to the lack of adequate controls in the bank, which allowed criminals to work through the loopholes in the system and bribe internal employees to help them implement the fraud. While this has been dubbed as the biggest fraud in India's banking history, it is by no means an isolated incident in the region. This is an issue that financial services institutions all over Asia Pacific should deal with urgently, or the costs may become unwieldy for the industry and society at large.

BANKS HAVE FAILED TO RECOGNISE THE LEGITIMACY OF MONEY

Asia has long been a key market of interest with consistent financial flows from the West. Foreign direct investment (FDI) is generally desirable for growing economies, not only in terms of immediate available cash flow for the local economy, but also in terms of

 | BY JULIA CHONG

THIRD-PARTY RISK: GETTING TO LOCKDOWN

You can outsource the work, but you **can't outsource the risk.**

Even the best-laid plans can unravel when it involves external or third-party vendors at any point of the value chain.

As financial institutions (FIs) turn to outsourcing of work functions like customer service, audit, security, facilities management, IT, document management, and form new synergistic partnerships with fintech for efficiency gains, the scope of risk is increasingly multifold and multidimensional.

Third-party vendors may prove to be one of the weakest links. Time and again, cybercriminals have exploited this vulnerability to, quite literally, break the bank.

2016's Bangladesh Bank cyber heist (see page 70) is proof positive that banks cannot assume zero failure of their systems at any point in time, and protocols for lockdown must be clearly defined from the onset.

DIAGRAM 1

10 STEPS TO IMPLEMENTING AN EFFECTIVE THIRD-PARTY RISK MANAGEMENT PROGRAMME

STEP 1 ▸ ESTABLISH ROLES & RESPONSIBILITIES

Begin implementation by establishing a third-party risk management policy that makes clear where the programme's authority resides and clearly defines roles and responsibilities. Banks and financial services companies with a more mature model centralise third-party risk within their enterprise risk management or operational risk management functions. Centralising the third-party risk management programme in

this way provides the authority to support cross-functional collaboration among the procurement, contracting, and legal departments. In addition to representatives of these functions, the implementation team should determine risk domain subject matter experts in the areas of information security, compliance, physical security, privacy, finance, business resiliency, and any other areas where there may be significant inherent risk for the firm.

STEP 2 ▸ INVENTORY THIRD-PARTY RELATIONSHIPS

Identify and inventory traditional and non-traditional third-party relationships throughout the organisation and map third-party relationships to the company's business processes, products, or services. The best place to begin identifying and

inventorying third-party relationships is in accounts payable, since many of these relationships will eventually generate payments.

Similarly, examining receivables can reveal non-customer revenue sources