Exclusive Interview

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Mr. Shazad Dada
President & CEO
United Bank Limited

ICMA: How is the banking sector playing a role in the country's business and economic development?

Shazad Dada: Banks play a pivotal role in the smooth functioning of any economy. Traditional services provided by the Banks for economic development include helping capital formation, providing credit to all sectors, acting as an intermediary for foreign trade, facilitating foreign remittances, mobilizing savings, and acting as trustworthy custodians of over PKR 20 trillion in individual, corporate, private and public sector deposits in Pakistan.

Banks have provided PKR 11 trillion in credit to various sectors of the economy including textile, telecommunication, industrial, energy, manufacturing, construction, agricultural, small and medium-sized entities, and individuals. This also includes funding large-scale projects that pave the way for the development of infrastructure in Pakistan.

The Pakistani Banking sector is very resilient. Contrary to the developed world, as an industry, we have never had any major Bank failures. This provides the foundations of trust that both domestic and foreign stakeholders can place on Pakistani Banks when conducting their transactions.

Foreign trade in the modern world is not possible without the role that Banks play as intermediaries. In the last twelve months, Pakistani Banks facilitated approximately USD 125 billion in trade. Banks are also the channel for marketing and attracting foreign remittances. These annual remittances of approximately USD 30 billion are a major contributor to Pakistan's foreign currency reserves and economic activity.

In addition, all Banks as good corporate citizens, allocate significant resources towards the betterment of the communities they operate in. Such allocations are used to support education, healthcare, community welfare, and several other causes. Banks are also playing an important role in a number of government and regulatory initiatives including poverty alleviation programs, subsidized loans for low-cost housing, temporary economic relief facility for COVID-19-affected exporters, etc.

ICMA team headed by Mr. Ather Saleem, Vice President & Chairman, R&P Committee visited the UBL Head Office, Karachi for meeting with Mr. Shazad Dada, President & CEO, UBL for his interview

At UBL, under our Environmental, Social, and Governance ('ESG') agenda, in addition to these initiatives, UBL is spearheading the promotion of renewable energy and water conservation, and sponsoring the development of arts, literature, and culture across Pakistan. We are also very proud to be leading the way in Women's Empowerment through our flagship product UBL Urooj.

Finally, UBL's innovation lab is an incubator for startups and Fintech, where we partner and invest in the research and development of emerging technologies, contributing to the efficiency and ease of doing business in Pakistan.

ICMA: Considering the vast unbanked population, do you think there is much potential for investment and growth in Pakistan's digital banking and payments industry?

Shazad Dada: There is immense potential for investment and growth in Pakistan's digital banking and payments industry. Pakistan has a population of 230 million. We are also a very young country where 70% of our population is millennials or younger. In addition, Pakistan's teledensity is one of the highest in the regions. Yet only 20% of the population has a bank account. Imagine what we could achieve if we were to bring access to financial services to the remaining 80%?

In the past, the key hindrances to expanding the scope of financial services have been the physical proximity of our target customers to a Bank branch, socio-economic barriers, and the economic viability of catering to customers in unbanked areas. Investment in digital technology has removed these barriers. For example, UBL as the market leader in technology and innovation is investing heavily in its digital offerings. This has enabled us to reach out to the large unbanked population beyond our 1,300+ branches and 35,000+ branchless banking agents ('UBL Omni'), through our state-of-the-art digital channels. These offerings are also at a fraction of the cost and provide customers with affordable and easy-to-use financial services. We firmly believe that providing the unbanked population of our country with affordable and easy-to-use financial services is the first step towards poverty alleviation.

The other key ingredient of digitization of any economy is a conducive regulatory environment. In many ways, the Pakistani Banking and payments industry has a visionary regulator in the form of the State Bank of Pakistan ('SBP'). SBP's policies and regulations on Digital Banking, Electronic Money Institutions, RAAST, Asaan Mobile Account, Roshan Digital Account to name a few, have played the role of a catalyst in the digital transformation of the industry. In conclusion, tapping into the unbanked population, in my view, will be the game changer for Pakistan in the years to come and truly accelerate the national objective of financial inclusion and developing a digitized economy.

ICMA: What types of risks are faced by a commercial bank and how these risks are managed by the Boards?

Shazad Dada: Banking as an industry is unique due to the role it plays in the money supply of an economy i.e. by intermediating between those who have surplus funds and those who need financing. Problems in the banking system can lead to wider instability in the economy, which is why there is a clear public interest in the timely identification and sound management of banking risks.

Risks specific to a Bank include credit risk (the risk that Bank loans will not be repaid in full), liquidity risk (the risk that a bank may not have sufficient funds to repay depositors who wish to withdraw their funds e.g. when banks fund long-term loans through short-term deposits), market risk (Bank's assets and liabilities will be adversely affected by changes in market prices and interest rates), operational risk (collection of risks due to e.g. operational failure, system failure, cyber security, technology risk, strategic risk, loss of key staff), conduct risk (the risk that a customer is disadvantaged due to the fault of the bank causing customer detriment), reputational risk (risk of reputational damage) and regulatory risk (risk of non-compliance with regulations and related penalties from regulatory authorities).

The UBL Board of Directors manages these risks firstly by setting a clear tone from the top on transparency, controls, governance, regulatory compliance, customer protection, accountability, and monitoring.

In addition, the UBL Board ensures that the Bank recruits, trains, manages, and motivates its people to create a culture based on the right values and behaviors. The Board has played a key role in empowering control functions at the Bank including risk, internal audit, finance, compliance, and operations to allow them to challenge business generators more effectively in highlighting, managing, and monitoring key risks.

Our Board is actively involved in understanding the risks, approving organizational risk appetite, and tolerance, and providing increased guidance and oversight over business decision-making. This translates into a comprehensive risk management framework, along with its associated policies, standard operating procedures, and practices. Compliance with the risk framework is monitored through regular Board meetings, various sub-committees of the Board, and management committees.

Every quarter there are detailed reports presented by me as Chief Executive Officer, the Chief Risk Officer, the Chief Compliance Officer, and the Chief Internal Auditor on emerging risks and how best to mitigate them, keeping in mind the interests of all stakeholders of the Bank. It is also crucial that the risk management framework is continuously refreshed with changing business conditions so that it remains relevant to the dynamic and ever-evolving nature of the Banking business.

ICMA: What are the key elements of an effective risk management strategy, especially in a banking business?

Shazad Dada: Banking is inherently risky and our job as Bankers is to analyze and mitigate such risks. Risk management has always been a core competency of a financial institution, but the extraordinary developments in the financial markets, the broader economy, and the fast-changing environment that we operate in have made it an even greater priority.

As one of the largest Banks in Pakistan, UBL manages risk across the organization. This is also known as Enterprise Risk Management, which encompasses all areas of the organizational exposure to risk. This includes embedding a transparent and easy-to-understand risk strategy, risk appetite, and risk management framework across the organization.

Having said that, beyond the methodologies, frameworks, governance structures, data and technology capabilities (which are all very important), developing a pervasive risk-aware culture throughout the organization and creating an environment and incentive structure (both for risk takers and risk controllers) that sustains this culture over time is essential to navigating the risks faced by financial institutions today. For example, at UBL, the 'risk management is everyone's responsibility' mindset is infused throughout the organization and integrated into

Mr. Athar Seleem, Vice President ICMA and Chairman Research & Publications Committee is presenting souvenir to Mr. Shazad Dada, President & CEO, United Bank Ltd.

performance goals and compensation decisions. The different roles of different functions in risk management can be best explained using the three lines of defense model for risk management:

First Line of Defense - the risk takers (business), the first line is responsible for taking, owning, managing, and escalating all the risks within their specific business areas.

Second Line of Defense - risk oversight - (Risk and compliance) - oversight of all key risks must be positioned within the second line of defense. The reporting lines are free from influence and avoid conflict of interest.

Third line of Defense - risk assurance (Internal audit) providing independent risk assurance to the Board.

Finally, it's always best practice to include in your risk management strategy a continuous self-assessment of risk and controls and formal risk management training across all three lines of defense.

ICMA: Are the priorities and strategies for risk management and control in commercial and Islamic banks the same or are different?

Shazad Dada: The general principles of risk management are common across Conventional and Islamic Banking. There are, however, a few very distinct differences.

Apart from credit and regulatory compliance, an important aspect of risk management for an Islamic Bank is Shariah compliance. At UBL Ameen, which is the Islamic Banking arm of UBL, we pay particular attention to ensuring Shariah Compliance. We understand that this is important for our customers, so we ensure strict compliance and ensure there is no 'mixing' between conventional assets and liabilities and that of UBL Ameen.

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UBL Ameen has a Shariah Board, comprising of three renowned Shariah scholars who provide guidance on Shariah principles and their compliance. The Shariah Board is supported by Shariah Compliance, Shariah Risk Management and Shariah Audit functions.

Other Special Islamic Risk Management expertise is required due to differences like the Islamic Banking business. For example, an Islamic Bank only conducts asset-based transactions (Diminishing Musharakah, Ijarah Murabaha, Salam and Istisna) and therefore are more exposed to fluctuation in asset and commodity prices; or risks associated with the customer's business.

ICMA: Non-performing loans (NPL) are the major cause of credit risk in financial institutions. What strategies are normally adopted by the banks to deal with the NPL?

Shazad Dada: The best strategy for a Bank is to have sound risk management practices in place, such that they prevent NPL formation in the first place. This starts with the risk assessment process at asset origination and requires robust underwriting of assets with an in-depth understanding of our customers, their businesses, and their financial position.

UBL uses several robust credits and analytical tools with forward-looking information to assess the credit risk of each asset underwritten. These models are continuously validated and modified to take account of changes such as macroeconomic, industry, and customer-specific factors.

Once an asset has originated, we work closely with our borrowers and closely monitor various risk characteristics to assess and flag early warning triggers.

Of course, eliminating the risk of NPLs is not possible for any Bank. Once an asset becomes an NPL, we have specialist remedial asset management teams that apply various techniques to recover the loans. These include helping the clients with relaxed/additional support, if we assess the problems as short-term and genuine in nature; providing longer-term restructuring to enable businesses to get back on their feet; debt asset swaps, liquidation of security, repossession of assets, litigation, etc.

ICMA: How important is diversification of products and services by the banks in controlling the credit risk?

Shazad Dada: Concentration Risk is a sub-category of Credit Risk and is used by Banks to monitor exposure across a single borrower, sectors, industries, and types of assets. If Banks concentrate on particular types of business activity, this leaves them particularly exposed to any problems in those activities. Therefore, portfolio diversification plays an important role in the reduction of credit risk, as it enables the Bank to withstand shocks in cyclical sectors and industries or the default of a customer or particular group of customers. In short, it ensures that a Bank does not, proverbially, 'put all its eggs in one basket'. In addition, for a global bank like UBL that operates in 8 countries, international diversification also plays a key role in reducing the risk of a specific country's economic downturn, currency depreciation, or adverse changes to regulatory, monetary, or fiscal policies.

ICMA: Are Pakistani banks investing in risk management technology and data analytics? Do you think adopting technology can help improve risk assessment in the banking sector?

Shazad Dada: Absolutely, in fact, in my view, Banks that are not investing in technology platforms will be left behind. Financial Institutions today need a more robust, integrated IT infrastructure that can quickly achieve a broad picture of risk across multiple lines of business, portfolios, products, and geographies.

As Pakistan's most innovative Bank, it's in UBL's DNA to invest in the use of cutting-edge technologies to make everything 'simpler, better, and faster'. Risk management is no different for us.

Using the traditional hard credit characteristics (age, demographics, employment status, income and expense, balance sheet) to predict future credit behavior is no longer considered adequate for assessing risk. UBL has invested in predictive data analytics and Artificial Intelligence ('AI') that use forward-looking information for credit scoring and risk assessment. This not only provides a more accurate risk assessment but also provides operational efficiencies, reduced costs, and an ability to reach out to previously untapped customers and markets.

The use of technology is not just limited to credit risk. It plays an important role in reducing other risks, in particular, operational risk and compliance risk.

For example, UBL's development of Robotics Process Automation ('RPA') has eliminated the risk of human error in several processes which could have led to reputational damage or regulatory penalties. Our investment in technological platforms ensures uninterrupted services to our customers at all hours and during natural calamities.

Another good example of the use of technology is in managing compliance risk. The modern Banking world requires significant manual, expensive, and time-consuming compliance processes, and checks.

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UBL's response to this has been the implementation of a technology-based governance and controls framework (including Financial Crimes Compliance 'FCC') coupled with 'RegTech' solutions and processes. This has enabled us to set the gold standard in regulatory compliance for the Banking industry in Pakistan and reduced turnaround time for our customers.

ICMA: The recent devastating floods have caused massive losses to the national economy. How will the banking sector play its role in the rebuilding process, especially in financing agriculture, livestock, and small businesses?

Shazad Dada: Pakistan has experienced one of the worst natural disasters in recent history. My thoughts and prayers are with the flood affected, who are suffering an unprecedented crisis.

The Banking sector must play its role in the rebuilding process. I can share with you some of the areas that UBL is working on. UBL's specialized rural banking and small and medium enterprise functions and our associated entity Khushali Micro Finance Bank are actively working with and supporting customers, particularly in the agriculture, livestock, and small/medium businesses sectors. UBL also has a dedicated Project Finance function that is working with Governmental bodies to provide advisory and financing solutions to large-scale infrastructure projects to help in the rebuilding process.

In partnership with local NGOs, UBL is providing immediate relief in the form of dry rations, cooked meals, and basic medical facilities in the most affected regions of Sindh and Balochistan. A more long-term program is under development that will assist in the settlement of the displaced providing them with the means to start rebuilding their lives. UBL is also proud to announce that our parent organization Bestway Group in the United Kingdom has also announced financial and material support worth USD 1 million.

We feel that the scale of the devastation calls for more concerted efforts. To initiate such a collaborative platform for this noble cause, the Bestway Group has organized a fundraiser in London. The event will also promote Roshan Digital Account and Roshan Samaji Khidmat to further attract both remittances and donations from overseas Pakistanis.

ICMA: Was the 'flood' identified as a risk factor in your Risk Management Strategy and if so what mitigating strategy do you have in place to deal with the current situation?

Shazad Dada: Ever since the global financial crisis, Banks have been criticized for limitations in assessing the risks of extremely rare events such as the recent floods in Pakistan. Such risks are often called “tail risks”. UBL's risk management framework uses methodologies such as stress tests for extreme scenarios such as floods, severe economic downturn, a slump in property / collateral values, political risk, etc. The high degree of correlation across asset classes, risk categories, and geographies in times of stress is factored into portfolio management decisions and enterprise-level capital needs. To a large degree, our risk models were able to accurately estimate the impact on our portfolio; however, the extent of damage to infrastructure and displacement of people has been far greater than anyone anticipated.

UBL is also piloting a program with our 'AgriTech' partners to use satellite imagery and sensors to assess the impact of crop health/yields and weather patterns to build predictive statistics and data insights on farmer profiles for grower financing limits for attaining seeds, fertilizer, pesticides, machinery. This will further enhance our capabilities to assess the risk of events such as the recent floods and incorporate this into our risk management framework in the future.

During this crisis, UBL's first and foremost priority has been the well-being of our employees and our customers. We have a large network with structured protocols as part of our Business Continuity and Disaster Recovery Plans that were invoked to ensure we continued to provide uninterrupted services to our customers for their Banking needs. After a detailed impact assessment, we are mobilizing our large network of branches and staff to work closely with customers in helping them recover from the destruction.

Despite the challenges brought about by the floods, I have complete faith in the resilience of our country and the irrepressible spirit and generosity of our people that will enable us to emerge out of this crisis with a much brighter future.

*The Editorial Board thanks **Mr. Shazad Dada, President & CEO United Bank Limited** for sparing from his precious time to give exclusive interview for Chartered Management Accountant Journal.*