RISK MANAGEMENT

To consistently deliver value to our various stakeholders, we are always cognizant of the risks inherent in our business — from deposit taking, lending and securities investment, to trading, foreign exchange, and operational support. Risk Management is increasingly becoming more important in today's business landscape characterized by disruptions and dynamism.

The key to effective risk management lies in the ability to identify and monitor such risks, and striking a good balance with organizational objectives and business opportunities.

Using a set of qualitative standards and quantitative metrics, we are able to determine our risk appetite. These are aimed at maintaining a strong capital and liquidity position, stable funding, good risk-reward balance, acceptable business practices, and dynamic compliance culture. Our risk metrics allow us to monitor our risk exposure under normal and stressed scenarios versus established trigger levels and limits. To avoid a breach in our risk limits, we institute a hierarchy of approval and observe escalation processes. Reports on our risk profile are presented to the senior management and the Board of Directors. Board-approved risk manuals are revisited annually or more frequently based on the changing risk environment and evolving regulatory landscape.

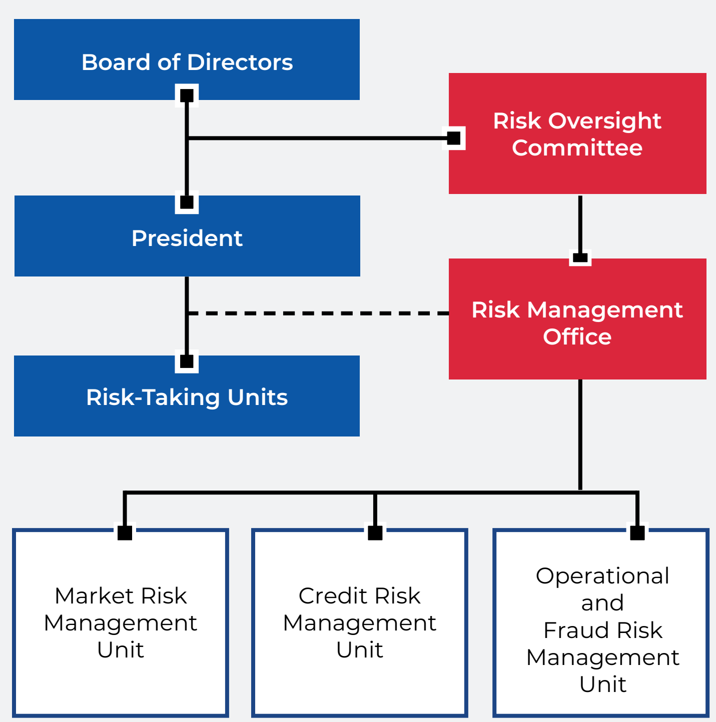
RISK MANAGEMENT STRUCTURE

Our Board of Directors takes the lead on all major risk management initiatives. It approves broad strategies and policies, and ensures that these are consistent with our overall objectives. The Risk Oversight Committee (ROC) is composed of at least three members of the Board, the majority of whom are independent directors, including the Chairperson who does not chair the Board or any other committee. The ROC members possess expertise and knowledge of our risk exposures, which enable them to develop appropriate strategies for preventing or minimizing the impact of losses.

The Board may also appoint non-Directors to the ROC as part of the Metrobank Group's risk oversight measures. However, only bank Directors shall be considered as voting members. Non-voting members are appointed in an advisory capacity. The ROC oversees our Enterprise Risk Management (ERM) framework, the consistency of current and emerging risk exposures with our strategic direction and overall risk appetite and the effectiveness of our risk management function in monitoring our risk-taking activities. It formulates policies and strategies to identify, measure, manage and limit risks. The ROC ensures that the system of limits approved by the Board remains effective. It also makes certain that limits are observed and that immediate corrective actions are taken whenever needed.

The Risk Management Office (RMO), together with the President, various committees, and Senior Management, support the ROC in the fulfillment of its duties and responsibilities. The RMO is independent from executive functions, business line responsibilities, operations, and revenue-generating functions. It reports directly to the Board through the ROC. (See our Risk Organization below.)

RISK ORGANIZATION



The RMO supports the ROC in carrying out its responsibilities by:

- Analyzing, communicating, implementing, and maintaining the risk management policies approved by the ROC and the Board;
- Spearheading the regular review of our risk management policies and elevating recommendations that enhance the risk management process to the ROC and the Board, for their approval;
- Ensuring that the risks arising from the Bank's activities are identified, measured, analyzed, reported, and understood by risk takers, management, and the Board. It analyzes limit exceptions and recommends enhancements to the limits structure;
- Monitoring the risk exposures and determining the corresponding capital requirement in accordance with the Basel III capital adequacy framework and based on our internal capital adequacy assessment on an ongoing basis;
- Monitoring and assessing decisions to accept particular risks whether or not these are consistent with Board-approved policies on risk tolerance and appetite as well as the effectiveness of the corresponding risk mitigation measures; and
- Reporting on a regular basis to Senior Management and the Board the results of risk assessments and monitoring.

TYPES OF RISKS

The nature of our business exposes us to different types of risks.

CREDIT RISK

This arises when a counterparty fails to meet its contractual obligations. Due to our low tolerance for nonperforming loans, our lending business follows strict credit policy guidelines set by the Board and ROC. These guidelines serve as our minimum standards for extending credit. Everyone engaged in the credit process is required to understand and adhere to these policies.

Our product manuals contain business plans and define the business parameters by which credit activity is to be performed. Before extending a loan, we observe a system of checks and balances, including the approval of at least two credit approvers through the Credit Committee (Crecom), Executive Committee (Excom), and the Board.

The ROC reviews our business strategies and ensures that revenue-generating activities are conducted within our overall risk appetite and meet the Board-approved credit risk thresholds. We hold regular audits across our organization. The Board — through the Excom, Crecom, and ROC ensures that all business segments follow sound credit policies and practices.

We assess our portfolio growth and health using key performance indicators. We use expected credit loss (ECL) models to measure the credit quality of financial assets, credit scoring models and decision systems for consumer loans, and borrower risk rating and facility risk rating models for SME loans, as approved by ROC and the Board. We carry out stress testing analyses using Board-approved statistical models, relating the default trends to macroeconomic indicators.

CREDIT CONCENTRATION RISK

Credit concentration is managed by type of individual or group of borrowers, by geographical region, and by industry sector. This is closely monitored with sufficient senior-level oversight to ensure that our low risk tolerance and policies for credit concentration are enforced.

We compute for additional risk-weighted assets attributed to credit concentration following the methodology of the Metrobank Risk Group. Concentration risk is scoped in two dimensions: name (or concentration due to specific obligors) and industry (or concentration due to specific industries).

MARKET RISK

This covers the areas of trading, interest rate, and liquidity risks. Trading market risk is the risk to earnings and capital arising from changes in the value of traded portfolios of financial instruments. Interest rate risk arises from movements in interest rates. The Assets and Liabilities Committee (ALCO), ROC, and the Board regularly review our market risk policies and implementing guidelines to ensure that these are up-to-date, in accordance with our low appetite for market risks, and in line with changes in the economy, environment, and regulations. The ROC and the Board set a comprehensive market risk limit structure and define the parameters of market activities that we can engage in. We utilize various measurement and monitoring tools to ensure that risk-taking activities are managed within instituted market risk parameters.

TRADING MARKET RISK

Our trading portfolios are currently composed of peso and dollar-denominated debt securities and Foreign Exchange (FX) positions that are marked-to-market daily. We use BSP-approved Type 3 Derivative License for plain vanilla FX forwards to manage our FX risk against adverse exchange rate movements.

We use Value-at-Risk (VaR), a statistical measure that calculates the maximum potential loss from a portfolio.

Our current VaR model is based on a historical simulation methodology with a one-day holding period and a 99% confidence level. We also perform backtesting to validate the VaR model, and stress testing to determine the impact of extreme market movements on our portfolios. We establish limits for trading portfolios and VAR, and comply with regulatory standards. We closely monitor our daily profit and loss against loss triggers and stop-loss limits. These ensure that our trading activities are in line with our low tolerance for market risk.

INTEREST RATE RISK

We have a risk management system and processes to quantify and manage interest rate risk in the banking book. We use measurement tools such as Interest Rate Repricing Gap, Earnings at Risk (EaR), Delta Economic Value of Equity (ΔEVE), and Sensitivity Analysis. An independent auditor regularly validates all these models.

Interest Rate Repricing Gap is a tool that distributes rate sensitive assets and liabilities to predefined tenor buckets according to time remaining to their maturity (if fixed rate) or repricing (if floating rate). Items lacking definitive repricing schedule (e.g., current and savings accounts) are assigned to repricing tenor buckets based on analysis of deposit behavioral patterns, past experience and/or expert judgment.

EaR is a tool used to evaluate the sensitivity of the accrual portfolio to changes in interest rates in the adverse direction over the next 12 months. We calculate our EaR using a historical simulation on interest rate volatility using 1,300 data points. Based on this, EaR is derived as the 99th-percentile biggest drop in net interest income. We use various stress scenarios such as largest historical movement in interest rates, predefined increase in interest rates, flattening, and steepening yield curves. We use Delta Economic Value of Equity (ΔEVE) to measure changes in the net present value of our banking book at different interest rate shocks and stress scenarios. It reflects changes in the economic value of equity over the remaining life of the assets and liabilities. ΔEVE is calculated by slotting the notional repricing cash flows arising from rate sensitive assets and liabilities into pre-defined tenor buckets. The present value of the net repricing cash flows is then calculated using various interest rate scenarios or changes in the yield curve such as steepener, flattener, parallel up, parallel down, short rates up and short rates down.

We generate and monitor our monthly EaR and ΔEVE exposures. EAR and ΔEVE levels are assessed vis-à-vis limits which are based on a percentage of net interest income or capital. Aside from the EaR and ΔEVE, we perform regular sensitivity and stress testing analysis on our banking book to further broaden our forward-looking analysis. This way, our management can craft strategies to address and/or mitigate probable risks, if necessary. The EaR, ΔEVE, and stress testing reports are prepared monthly.

The ALCO is responsible for managing our structural interest rate exposure. Its goal is to achieve a desired overall interest rate profile within our low appetite for interest rate risk and maintain flexibility to interest rate movements and changes in economic conditions. RMO and ROC review and oversee our interest rate risks.

LIQUIDITY RISK

Liquidity risk is the inability to meet obligations when they fall due without incurring unacceptable losses. In managing our liquidity position, we ensure that we have more than adequate funds to meet maturing obligations. We use the Maximum Cumulative Outflow (MCO) model to measure liquidity risk arising from the mismatches of our assets and liabilities. We administer stress testing to assess our funding needs and strategies under various conditions. Stress testing enables us to gauge our capacity to withstand both temporary and long-term liquidity disruptions.

Our Liquidity Contingency Funding Plan (LCFP) helps us anticipate a liquidity crisis under various stress scenarios. Liquidity limits for normal conditions cap the outflows on a cumulative basis. We discourage dependence on Large Fund Providers (LFPs) and monitor our deposit funding concentrations versus our High Quality Liquid Assets (HQLA). This way, we will not be vulnerable to a substantial drop in deposit level should there be an outflow of large deposits. ALCO is responsible for managing our liquidity while RMO and ROC review and oversee our overall liquidity risk management. We have zero appetite for non-compliance with liquidity requirements and ensure this through the close monitoring and management of our High Quality Liquid Assets vis-a-vis our net cash outflows. Our Liquidity Coverage Ratio (LCR) and Net Stable Funding Ratio (NSFR) are managed on a daily basis to ensure our strong liquidity posture and compliance with the regulatory ratios.

OPERATIONAL RISK

This is the risk of loss resulting from inadequate or failed internal processes, people and systems, or from external events. To mitigate these and meet our low tolerance for operational risks, we constantly strive to maintain our strong control culture, prudently use technology, and adopt an effective internal control system. We consider these as key factors in our continuous self-improvement under a "no-surprise" operating environment.

We have zero appetite for fraud and constantly improve our policies, processes, and tools to prevent these instances. We also have zero tolerance for non-compliance to our internal policies as well as applicable local regulations and laws. As part of ensuring an appropriate risk management environment, the operational risk framework is consistently implemented throughout the organization. The Bank recognizes the principle of having three levels of defense in mitigating operational risk exposures. The first level involves all personnel, the second are the risk and compliance teams, and lastly, the internal audit team. Our Board-approved, bank-wide organizational chart clearly establishes areas of management responsibility, accountability, and reporting lines for all senior officers. Senior Management is responsible for developing policies, processes, and procedures for managing operational risk in all the Bank's material products, services, processes, and systems. Operational risk management policies and frameworks are regularly reviewed and updated, subject to ROC and Board approval to ensure that they remain relevant, effective and aligned with those of the parent bank. Performance gaps are identified and resolved by strengthening existing controls and implementing additional controls. Risk awareness is implemented through various training curricula that the PSBank Business Campus designs and implements. This is a key component and embedded in the regulatory training for all employees.For high-potential and high-performing employees undergoing management training programs, this is a component of the Ladderized Programs, Staff Professional Enhancement and Educational Development – Accelerated Learning (SPEED AX-L), Redefining Institutional Sales Efficiency (RISE), ELEV8: Future-Proofing the Leadership Bench, and other initiatives.

Our products and operating manuals, policies, and procedures spell out internal controls that our business and operating support units implement. Our Internal Audit Group (IAG) provides independent reasonable assurance on control adequacy and compliance with these manuals. We identify and assess operational risks across the organization and develop controls to mitigate and manage them as part of our continuing efforts to enhance our Operational Risk Management Framework in close coordination with our parent bank. We perform this vis-a-vis the Board-approved operational loss thresholds and benchmarks and through the ORM tools such as the Institutional Key Risk Indicator (KRI) Report, Business Unit Level (BU Level) KRI Report, Risk Incident Report (RIR), Risk and Control Self-Assessment (RCSA), Loss Event Database (LED), and various risk assessments. The operational risks are regularly monitored and reported to senior management, and Board through the ROC. The Bank has a robust Business Continuity Plan (BCP) and a Disaster Recovery Program (DRP) that are reviewed and tested annually for continuous improvement and to ensure readiness and effectiveness in case of business disruptions, system failures and disasters. These provide activities for testing critical systems and other systems in the Business Recovery Center (BRC) on a per segment basis. In 2023, our BCP testing yielded excellent results, encompassing bank-wide call tree testing, BRC activation, BCP simulation, and evacuation drills.

TECHNOLOGY RISK

This is the risk to earnings or capital arising from deficiencies in design, implementation, maintenance of systems or equipment, and the failure to establish adequate security measures, contingency plans, testing and audit standards. We invest in information technology to provide simpler, faster, more convenient, and secured banking services to our growing clientele. We also utilize an advanced management information system so we can make quick and well-informed business decisions. We continuously venture into core business process automations, key system enhancements, and information security solutions while ensuring we meet our low appetite for technology risks.

Given the heavily automated operating environment, we ensure that we identify and quantify risks to the greatest extent possible. We also establish standards and controls to manage technology-associated risks through effective planning, proper implementation, periodic measurement and monitoring of performance.

We have a Bank-wide IT Risk Management Framework which is revisited annually to ensure its conformity with existing and/or latest bank-wide processes and compliance with related local regulatory requirements. This defines the responsibilities of all employees involved in identification, assessment, reporting, and management of technology risks and the guidelines that govern the IT Risk Management process. This also provides for the annual conduct of IT Risk Assessment to identify, assess, monitor and control the technology-related risks.

We have an IT Steering Committee that oversees IT performance and institutes appropriate controls to manage significant IT issues. The Information Technology Group (ITG) and Information Security Division (ISD) provide support through their technology and information security initiatives, projects and well-defined policies and controls.

LEGAL RISK

This is the potential loss arising from regulatory or legal action, disputes for or against us, failure to correctly document, enforce or adhere to contractual arrangements, inadequate management of non-contractual rights, or failure to meet non-contractual obligations. We have low tolerance for legal risks and employ a legal review process to control and manage these risks.

The Legal Services Division plays a significant role in protecting the Bank's rights and interests by ensuring that legal activities of the Bank are carried out in accordance with laws and regulations, established legal processes, prescribed practices, customary or ethical standards, Bank policies and goals. The Legal Services Division also conducts necessary legal review of products, services, policies, manuals, bank documents including legal capacities of the parties to a transaction. Legal risk is difficult to measure, but it can be defined, understood, and controlled with the end view of limiting and minimizing exposure to such risks. The Legal Services Division conducts legal risk assessment of cases filed against the Bank and recommends legal risk mitigation measures. The appropriate actions include reducing exposures of sources of legal risk, establishing an appropriate legal risk management process and strengthening the compliance function in the Bank. The legal risks are tracked in the monthly Institutional KRIs and Business Unit Level KRIs of the Legal Services Division. Breaches and the corresponding action plans are reported by the Operational and Fraud Risk Management Unit to the ROC and Board.

REGULATORY RISK

Regulatory risk, also known as compliance risk, covers the potential loss from non-compliance with laws, rules and regulations, policies and procedures, and ethical standards. We recognize that compliance risk can diminish our reputation, reduce our franchise value, limit business opportunities, and reduce our potential for expansion. Guided by our Compliance Office, we continuously promote a strong culture of compliance. The Bank's internal policies, local rules and regulations, and laws support our zero appetite for regulatory risk amid an ever dynamic banking regulatory landscape and zero tolerance specific to Money Laundering and Terrorist Financing (ML/TF) risks.

STRATEGIC RISK

This is the current and prospective impact on earnings or capital arising from adverse business decisions, improper resolution of conflicts, and slow response to industry changes. Strategic risk can shape our long-term goals, business strategies, and resources. We utilize both tangible and intangible resources to carry out our business strategies and meet our low appetite for strategic risk. These include communication channels, operating systems, delivery networks, and managerial capacities and capabilities.

REPUTATIONAL RISK

This refers to the current and prospective impact of negative public opinion on our earnings or capital which may affect our ability to establish new relationships or services, or manage existing ones. The risk may also expose us to litigation, financial loss, or a decline in customer base. All employees are responsible for building our brand reputation and exercising an abundance of caution when dealing with customers and communities to support our zero tolerance for reputational risk. To further mitigate reputational risk, we have policies and procedures on financial consumer protection, client complaint handling, employee conduct and the use of social media, and crisis management.

Reputational risks may also arise from our outsourced services. These are part of items assessed and approved by our Outsourcing Oversight Committee, and by the Board, whenever needed. We have a Crisis Management Team that formulates, implements, and coordinates the approach to managing a reputational event. Our Emergency Committee (EMCOM) ensures the management and monitoring of the effective implementation of our Business Continuity Plan (BCP) related to an emergency scenario or event which may lead to reputational damage. Reputational risk controls are established through the source risk areas of credit, market and operational risks. Management and reporting of the reputational events are performed by the business units, as the first line of defense, through the established risk indicators.

RISKS RELATED TO TRUST

These risks take into account the impact of compliance, reputational, or operational risks on our managed funds. These are part of the overall risks taken by the Bank or the enterprise risk. The Trust Committee oversees the implementation of the risk management framework for trust and ensures that controls are in place relative to fiduciary activities. The Trust Division is governed by risk management and various policies and procedures for trust.

ENVIRONMENTAL AND SOCIAL RISK

This refers to the potential adverse financial, legal, and/or reputational impact on the Bank when faced with environmental and social issues such as environmental pollution, climate risk (both physical and transition risks), hazards to human health, safety and security, and threats to the community, biodiversity and cultural heritage. Cognizant that these could pose concerns for us and our stakeholders and guided by the Bangko Sentral ng Pilipinas (BSP) Circular No. 1085, in September 2021, we formally instituted our Sustainable Finance Framework to articulate the integration of environmental, social, and governance criteria into our day-to-day business operations and our financial products and services. The framework provides basis for defining our targets and metrics to deliver on our commitment to support sustainable economic growth and the transition to a low-carbon economy. The principles and standards are embedded in our Environmental and Social (E&S) Risk Management Policy Manual in accordance with BSP Circular No. 1128 issued in October 2021 and BSP Circular No. 1149 issued in September 2022. In 2022, we integrated environment and social-related risks in our product manuals, policies and procedures, and employee functions. We improved our banking, credit, and investment operations with environmental risk metrics and introduced physical risk assessments for our credit, and capital assets and third party service providers. In 2023, these were refined to consider climate hazards' severity and frequency, enabling the Bank to mitigate and further reduce residual risk exposure. We developed tools that allow us to measure and manage our E&S risk and physical risk exposures based on industry-acceptable parameters. Further, our ICAAP exercise was expanded to include assessment of our resilience against transition risk arising from aggressive government push on environmental, social and governance initiatives, and geopolitical crisis. Our internal sustainability reporting policies were formalized to document and capture efforts in our sustainable finance journey while maintaining transparency and accountabilities among our contributors.

For a complete discussion of PSBank's capital details, please refer to the Supplementary Management Discussion and Notes to the Financial Statements on Financial Risk Management Policies and Objectives.

AUDITED FINANCIAL STATEMENTS