## RISK POLICIES AND CONTROL

The mission of the Office of Risk Policies and Control is to identify, assess and monitor the risks associated with the Bank business, maintaining an adjusted design of specific policies and controls, taking an integrated approach aligned with the mission and strategic objectives of our Bank.

BROU has a methodological framework approved by a Resolution of the Board dated December 23, 2008, containing guidelines as a basis for an integrated approach, consistent and aligned with our mission and strategic objectives in order to identify, evaluate, respond to and monitor key risks affecting the achievement of our Bank objectives.

This methodological framework contains basic definitions and key concepts for a Comprehensive Risk Management, and a description of the steps to follow, factors to consider, techniques to be used and the main roles and responsibilities related to such management.

### Credit Risk

The Units of Credit Risk and Regulations are mandated to identify, measure, monitor and control non-financial sector credit risks, and to develop and promote best practices and the design and implementation of information systems for monitoring and analyzing the loan portfolio.

Regarding risk acceptance, this Office is present in the various Credit Committees when borrowings higher than USD 200,000 are approved. An adverse technical opinion of this Office would require that a Senior Professional Body treat the credit. Also, this Office is present whenever the Board deals with business matters, assisted by the Credit Committee.

This Office also monitors that the risk credit positions assumed adhere to the ceilings provided for by the Regulation and Control Rules of the Financial System and by internal regulations.

This Office regularly prepares reports to the Board and the Risk Committee on the portfolio of our Bank by sector of activity and by higher exposures, analyzing among others, credits volume, risk categories, provisions and guarantees, besides monitoring the credit risk ceilings of the Non-financial Sector, established in the Credit Manuals and the Risk Appetite.

Reports were prepared on special credits lending, the portfolio of the Social Credit Division and sectoral portfolios.

Regarding the monitoring of credits, this Office keeps track of credits identified as potentially problematic either due to delay in payment or for belonging to a jeopardized business sector, sending warnings of such situations.

The credit risk performance of the non-financial sector portfolio in 2015 maintained the good indexes of the previous year, with 80% of transactions in this portfolio located in the lower risk categories.

The delinquency indicator of the non-financial sector portfolio, defined as the ratio between gross overdue credits (60 days or more: past due, with collection in process and delinquent credits) and gross total credits, reached 3.3%, a figure somewhat higher than the previous year.

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**Market, Liquidity, Country and Counterparty Risks**

The mandate of the Market and Liquidity Risk unit is to identify, measure, monitor and control the following risks: liquidity, interest rate, exchange rate, price, counterparty and country risk. By using standard techniques and practices in the industry, this Department provides analytical support to the corporate decision-making related to the main financial risks control and policies.

This unit promotes risk management using traditional measurements such as gap, duration and Value at Risk, with specific limits for each financial portfolio.

These metrics provide key calculations to understand the nature of the "exchange rate" and "interest rate" risks. The VAR technique on the exchange rate at the end of 2015 showed an estimated maximum loss of UYU 498,893,925, equivalent to USD 16,700,496 at the exchange rate used taking Uruguayan pesos as the unit of measure.

Likewise, compliance with the rules on minimum capital requirement established by the BCU, provided calculations also very useful for corporate purposes. In December 2015, the Head Office had to maintain as capital requirement for foreign exchange rate risk the equivalent to USD 19,435,581, and for interest rate risk the equivalent to USD 111,624,731. About this rate risk, our Bank made substantial progress implementing a technological working environment, including where possible other metrics for monitoring the joint portfolio of financial instruments, such as VAR, ensuring the maintenance of complete information databases that allow access at transaction level.

Also important information on the management of structural interest rate risk is provided, not only identifying such risk in the balance sheet, from its accounting and economic perspective, but with sensitivity tests based on rate curves taken as a reference. By applying standard testing in the industry, the results for our Bank are successful in terms of impact measured both on equity and on financial margin.

In relation to the process of monitoring and controlling liquidity risk, there is a work environment that allows displaying the cash flow of our Bank from different perspectives, with access to information at transaction level. In addition to said analysis, stress test scenarios were generated for said cash flow, following the Basel test design.

The Market and Liquidity Risk Department also provides the rating of financial institutions, highlighting the rating of multiple correspondents that maintain regular relationships with our Bank. Likewise, a matrix design is regularly kept and reviewed, adding the country risk to all other risks and updating discount factors per exposure allowed. The strong participation of this Department in 2015 must be highlighted in the monitoring and follow up of adequate operational implementation and best practices in the new Core Banking system (Phase 1), promoting risk identification and control in terms of financial sector counterparts and country risk. The supporting methodologies allow continued monitoring of country risk performance in a highly volatile international scenario, with estimates based on adequate provisions, such as the large-scale financial investments held by our Bank.

In the fiscal year 2015, analytical support for the Assets and Liabilities Committee has been maintained. Ratios, indicators and specific tests on liquidity risk and interest rate risk have been submitted for consideration of such Committee following the Basel III recommendations, particularly in response to their revaluation in the terms of the international supervision, regulation and the industry itself.

### Operational and Compliance Risk

The Operational Risk Unit has responsibilities for the identification, measurement, monitoring and control of operational risk defined as the risk that the earnings or assets of our Bank might be affected by losses from inadequate or defective processes, staff or systems, or by external events.

This year Compliance Risk was added, defined as the present and future risk that the profits or assets of BROU might be affected by violations of laws, regulations, standards and practices of the industry or ethical standards. This includes compliance with our Bank's own rules or self-regulation.

Software was purchased for Operational Risk management, which includes a database for recording Loss events, for capturing incidents and events as well as features for performing risk assessments, self-assessments and questionnaires on Internal Control environments and Compliance among others.

Progress was made in the analysis and specification of requirements for registration and traceability of transactions related to operational risk in the new Core Banking system, to which our Bank is currently conducting a migration process.

Regarding Compliance Risk, the Board approved the relevant policies containing guidelines for the management and allocation of responsibilities, roles and tools for its treatment.

### Reputational Risk

Monitoring and control was deepened in this fiscal year, and the information base was expanded to issue reports addressed to the Risk Committee.


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