MCB BANK LIMITED - SRI LANKA BRANCH

Basel III - Disclosures under Pillar 3 as per the Banking Act Direction Number 01 of 2016

Disclosure 1

Key Regulatory Ratios - Capital and Liquidity

Selected Performance Indicators	Sri Lanka Operation	
	As at 31.03.2022	As at 31.12.2021
Regulatory Capital (LKR 000)		
Common Equity Tier 1 Capital	6,679,938	6,689,022
Tier 1 Capital	6,679,938	6,689,022
Total Capital	6,848,892	6,857,157
Regulatory Capital Ratio (%)		
Common Equity Tier 1 Capital Ratio (Minimum Requirement - 7.00%)	47.23	45.83
Tier 1 Capital Ratio (Minimum Requirement - 8.50%)	47.23	45.83
Total Capital Ratio (Minimum Requirement -12.50%)	48.42	46.99
Regulatory Liquidity		
Statutory Liquid Assets **(LKR 000)**	13,306,323	12,349,959
Statutory Liquid Assets Ratio % -Minimum requirement 20%		
Domestic Banking Unit (%)	68.0	70.2
Off Shore Banking Unit (%)	57.5	69.5
Liquidity Coverage Ratio (%)- Rupee (Minimum Requirement - 90%)	312.00	312.00
Liquidity Coverage Ratio (%)- All currencies (Minimum Requirement - 90%)	635.93	258.65

Disclosure 2

Basel III Computation of Capital Ratio

Item	Amount (LKR '000) As at 31.03.2022	Amount (LKR '000) As at 31.12.2021
Common Equity Tier 1 (CET1) Capital after Adjustments	6,679,938	6,689,022
Common Equity Tier 1 (CET1) Capital	6,707,141	6,720,968
Equity Capital (Stated Capital)/Assigned Capital	3,969,508	3,969,508
Reserve Fund	244,905	244,959
Published Retained Earnings/(Accumulated Retained Losses)	2,281,142	2,282,217
Published Accumulated Other Comprehensive Income (OCI)	211,586	224,283
General and other Disclosed Reserves	-	-
Unpublished Current Year's Profit/Loss and Gains reflected in OCI	-	-
Ordinary Shares issued by Consolidated Banking and Financial Subsidiaries of the Bank and held by Third Parties	-	-
Total Adjustments to CET1 Capital	**27,203**	**31,945**
Goodwill (net)	-	-
Intangible Assets (net)	27,203	31,945
Others (specify)	-	-
Additional Tier 1 (AT1) Capital after Adjustments	**-**	**-**
Additional Tier 1 (AT1) Capital	**-**	**-**
Qualifying Additional Tier 1 Capital Instruments	-	-
Instruments issued by Consolidated Banking and Financial Subsidiaries of the Bank and held by Third Parties	-	-
Total Adjustments to AT1 Capital	**-**	**-**
Investment in Own Shares	-	-
Others (specify)	-	-
Tier 2 Capital after Adjustments	**168,954**	**168,134**
Tier 2 Capital	**168,954**	**168,134**
Qualifying Tier 2 Capital Instruments	-	-
Revaluation Gains	-	-
Loan Loss Provisions	168,954	168,134
Instruments issued by Consolidated Banking and Financial Subsidiaries of the Bank and held by Third Parties	-	-
Total Adjustments to Tier 2	-	-
Investment in Own Shares	-	-
Others (specify)	-	-
CET1 Capital	**6,679,938**	**6,689,022**
Total Tier 1 Capital	**6,679,938**	**6,689,022**
Total Capital	**6,848,892**	**6,857,157**

Item	Amount (LKR '000) As at 31.03.2022	Amount (LKR '000) As at 31.12.2021
Total Risk Weighted Assets (RWA)	**14,143,986**	**14,593,799**
RWAs for Credit Risk	12,407,890	12,222,381
RWAs for Market Risk	178,520	778,661
RWAs for Operational Risk	1,557,576	1,592,758
CET1 Capital Ratio (including Capital Conservation Buffer, Countercyclical Capital Buffer & Surcharge on D-SIBs) (%)	**47.23**	**45.83**
of which: Capital Conservation Buffer (%)		
of which: Countercyclical Buffer (%)		
of which: Capital Surcharge on D-SIBs (%)		
Total Tier 1 Capital Ratio (%)	**47.23**	**45.83**
Total Capital Ratio (including Capital Conservation Buffer, Countercyclical Capital Buffer & Surcharge on D-SIBs) (%)	**48.42**	**46.99**
of which: Capital Conservation Buffer (%)		
of which: Countercyclical Buffer (%)		
of which: Capital Surcharge on D-SIBs (%)		

Template 3

Computation of Leverage Ratio

Item	Amount (LKR '000) As at 31.03.2022	Amount (LKR '000) As at 31.12.2021
Tier 1 Capital	6,679,937	6,689,022
Total Exposures	27,713,694	27,079,268
On-Balance Sheet Items (excluding Derivatives and Securities Financing Transactions, but including Collateral)	27,068,160	26,193,921
Derivative Exposures	-	244,411
Securities Financing Transaction Exposures	-	-
Other Off-Balance Sheet Exposures	623,531	608,991
Basel III Leverage Ratio (%) (Tier 1/Total Exposure)	24.10%	24.70%

Disclosure 4

Bael III Computation of Liquidity Coverage Ratio - All Currencies

Item	Amount (LKR '000)			
	As at 31.03.2022		As at 31.12.2021	
	Total Un-weighted Value	Total Weighted Value	Total Un-weighted Value	Total Weighted Value
Total Stock of High-Quality Liquid Assets (HQLA)	9,300,467	9,300,467	9,077,030	9,077,030
Total Adjusted Level 1A Assets	9,300,467	9,300,467	9,077,030	9,077,030
Level 1 Assets	9,300,467	9,300,467	9,077,030	9,077,030
Total Adjusted Level 2A Assets	-	-	-	-
Level 2A Assets	-	-	-	-
Total Adjusted Level 2B Assets	-	-	-	-
Level 2B Assets	-	-	-	-
Total Cash Outflows	**24,402,044**	**5,767,025**	**21,692,230**	**6,497,325**
Deposits	7,585,097	758,510	6,886,145	688,615
Unsecured Wholesale Funding	9,912,234	4,397,970	9,409,091	5,326,717
Secured Funding Transactions	-	-	-	-
Contingent Funding Obligations	6,904,713	610,545	5,396,994	481,994
Additional Requirements	-	-	-	-
Total Cash Inflows	**6,455,339**	**4,304,529**	**4,873,969**	**2,987,900**
Maturing Secured Lending Transactions Backed by Collateral	-	-	-	-
Committed Facilities	-	-	-	-
Other Inflows by Counterparty which are Maturing within 30 Days	6,455,339	4,304,529	4,872,489	2,986,420
Operational Deposits	-	-	-	-
Other Cash Inflows	-	-	1,480	1,480
Liquidity Coverage Ratio (%) (Stock of High Quality Liquid Assets/Total Net Cash Outflows over the Next 30 Calendar Days) * 100		**635.93**		**258.65**

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Disclosure 5

Basel III Main Features of Regulatory Capital Instruments

Description of the Capital Instrument	Assigned Capital as at 31.03.2022
Issuer	MCB Bank Pakistan
Unique Identifier (e.g., ISIN or Bloomberg Identifier for Private Placement)	
Governing Law(s) of the Instrument	Pakistan
Original Date of Issuance	N/A
Par Value of Instrument	N/A
Perpetual or Dated	Perpetual
Original Maturity Date, if Applicable	N/A
Amount Recognised in Regulatory Capital (in LKR ‘000 as at the Reporting Date)	3,969,508
Accounting Classification (Equity/Liability)	Equity
Issuer Call subject to Prior Supervisory Approval	
Optional Call Date, Contingent Call Dates and Redemption Amount (LKR ‘000)	N/A
Subsequent Call Dates, if Applicable	N/A
Coupons/Dividends	
Fixed or Floating Dividend/Coupon	N/A
Coupon Rate and any Related Index	N/A
Non-Cumulative or Cumulative	N/A
Convertible or Non-Convertible	
If Convertible, Conversion Trigger (s)	N/A
If Convertible, Fully or Partially	N/A
If Convertible, Mandatory or Optional	N/A
If Convertible, Conversion Rate	N/A

Basel III - Disclosures under Pillar 3 as per the Banking Act Direction Number 01 of 2016

Disclosure 6

Summary Discussion on Adequacy/Meeting Current and Future Capital Requirements

The Bank prepares the strategic plan covering a period of 5 years on a rolling basis by taking in to account of the Capital Adequacy Ratio (CAR). The Bank analyses the CAR against increases in risk weighted assets in line with the budget expansion and business volumes.

Currently the Bank is adequately capitalized and its capital adequacy ratio (CAR) is well above the minimum regulatory requirements. Bank has a well-diversified assets portfolio which is neither overly exposed to any counterparty nor to any sector. Further, the Bank will deliberate on strategically curtailing risk weighted assets expansion, if required.

The Bank always strive to achieve the reasonable profit growth in line with the banking industry average and the repatriation of profit to Pakistan is based on the minimum requirement set by the State Bank of Pakistan. Part of the profit generated is retained for the future business expansion. Capital generated through retained profit over the years could be considered as one of the primary source of capital to the Bank.

Disclosure 7

Basel III Credit Risk under Standardised Approach –Credit Risk Exposures and Credit Risk Mitigation (CRM) Effects

As at 31.03.2022	Exposures before Credit Conversion Factor (CCF) and CRM		Exposures post CCF and CRM		RWA and RWA Density (%)	
	On - Balance Sheet Amount	Off -Balance Sheet Amount	On - Balance Sheet Amount	Off - Balance Sheet Amount	RWA	RWA Density (%)
	LKR '000	LKR '000	LKR '000	LKR '000	LKR '000	LKR '000
Claims on Central Government and CBSL	9,384,689	-	9,384,689	-	-	-
Claims on Foreign Sovereigns and their Central Banks	-	-	-	-	-	-
Claims on Public Sector Entities	3,030	-	3,030		3,030	100.00
Claims on Official Entities and Multilateral Development Banks	-	-	-	-	-	-
Claims on Banks Exposures	4,584,539	-	4,584,539	-	1,754,703	38.27
Claims on Financial Institutions	1,572,218	40,900	1,572,218	20,450	808,522	50.77
Claims on Corporates	5,799,030	571,372	4,999,675	361,449	5,264,066	98.19
Retail Claims	308,880	-	94,748	-	92,104	97.21
Claims Secured by Residential Property	836,730	10,000	836,730	5,000	799,911	95.03
Claims Secured by Commercial Real Estate	2,411,018	491,286	2,242,181	236,633	2,478,814	100.00
Non-Performing Assets (NPAs)	654,908	-	654,908	-	663,898	101.37
Higher-risk Categories	-	-	-	-	-	-
Cash Items and Other Assets	1,207,292	-	1,207,292	-	542,843	44.96
Total	**26,762,333**	**1,113,558**	**25,580,010**	**623,532**	**12,407,890**	**47.35**

Disclosure 8

Credit Risk under Standardised Approach: Exposures by Asset Classes and Risk Weights

Description	**Amount in (LKR '000) (Post CCF & CRM)**							
Asset Classes — As at 31.03.2022	**0%**	**20%**	**50%**	**75%**	**100%**	**150%**	**>150%**	**Total Credit Exposures Amount**
Claims on Central Government and Central Bank of Sri Lanka	9,384,689	-	-	-	-	-	-	9,384,689
Claims on Foreign Sovereigns and their Central Banks	-	-	-	-	-	-	-	-
Claims on Public Sector Entities	-	-	-	-	3,030	-	-	3,030
Claims on Official Entities and Multilateral Development Banks	-	-	-	-	-	-	-	-
Claims on Banks Exposures	-	3,347,435	303,777	-	933,327	-	-	4,584,539
Claims on Financial Institutions	-	6,551	1,557,810	-	28,307	-	-	1,592,668
Claims on Corporates	-	121,323	-	-	5,239,801	-	-	5,361,124
Retail Claims	-	-	-	10,577	84,171	-	-	94,748
Claims Secured by Residential Property	-	-	64,337	-	777,393	-	-	841,730
Claims Secured by Commercial Real Estate	-	-	-	-	2,478,814	-	-	2,478,814
Non-Performing Assets (NPAs)	-	-	-	-	636,928	17,980	-	654,908
Higher-risk Categories	-	-	-	-	-	-	-	**-**
Cash Items and Other Assets	664,449	-			542,843			**1,207,292**
Total	**10,049,138**	**3,475,309**	**1,925,924**	**10,577**	**10,724,614**	**17,980**	**-**	**26,203,542**

Disclosure 9

Market Risk under Standardised Measurement Method

Item	**RWA Amount (LKR' 000) as at 31st March 2022**	**RWA Amount (LKR' 000) as at 31st December 2021**
(a) RWA for Interest Rate Risk	-	-
General Interest Rate Risk	-	-
(i) Net Long or Short Position	-	-
(ii) Horizontal Disallowance	-	-
(iiii) Vertical Disallowance	-	-
(iv) Options	-	-
Specific Interest Rate Risk	-	-
(b) RWA for Equity	-	-
(i) General Equity Risk	-	-
(ii) Specific Equity Risk	-	-
(c) RWA for Foreign Exchange & Gold	**22,315**	**186,854**
Capital Charge for Market Risk [(a) + (b) + (c) * CAR	**22,315**	**53,318**

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Disclosure 10

Operational Risk under Basic Indicator Approach/The Standardised Approach/The Alternative Standardised Approach

Business Lines (20.5.1.4.0.0)	Capital Charge Factor	Fixed Factor 'm' (20.5.1.6.0.0)	Gross Income (LKR '000) as at 31.03.2022		
			1st Year	2nd Year	3rd Year
The Basic Indicator Approach	15%		1,585,040	1,267,091	1,041,816
The Standardised Approach			-	-	-
Corporate Finance	18%		-	-	-
Trading and Sales	18%		-	-	-
Payment and Settlement	18%		-	-	-
Agency Services	15%		-	-	-
Asset Management	12%		-	-	-
Retail Brokerage	12%		-	-	-
Retail Banking	12%		-	-	-
Commercial Banking	15%		-	-	-
The Alternative Standardised Approach			-	-	-
Sub Total			-	-	-
Corporate Finance	18%		-	-	-
Trading and Sales	18%		-	-	-
Payment and Settlement	18%		-	-	-
Agency Services	15%		-	-	-
Asset Management	12%		-	-	-
Retail Brokerage	12%		-	-	-
Sub Total			-	-	-
Retail Banking	12%	0.035			
Commercial Banking	15%	0.035			
Capital Charges for Operational Risk (LKR'000)					
The Basic Indicator Approach	**1,557,576**				
The Standardised Approach	-				
The Alternative Standardised Approach	-				
Risk Weighted Amount for Operational Risk (LKR'000)					
The Basic Indicator Approach	**194,697**				
The Standardised Approach	-				
The Alternative Standardised Approach	-				

Disclosure 11

Differences between Accounting and Regulatory Scopes and Mapping of Financial Statement Categories with Regulatory Risk Categories – Bank Only

	Bank				
	a	b	c	d	e
As at 31.03.2022	**Carrying Value as Reported In Published Financial Statements**	**Carrying Value as under the Scope of Regulatory Reporting**	**Subject to Credit Risk Framework**	**Subject to Market Risk Framework**	**Not subject to Capital Requirements or Subject to Deduction from Capital**
	LKR '000	**LKR '000**	**LKR '000**	**LKR '000**	**LKR '000**
Assets	**27,068,160**	**27,068,160**	**25,259,585**	**-**	**1,815,400**
Cash and Cash Equivalents	664,449	664,449	664,449		
Balances with Central Banks	938,618	938,618	938,618		
Placements with Banks	5,093,753	5,093,753	5,093,753		6,824
Derivative Financial Instruments	-	-			
Other Financial Assets Held-For- Trading	-	-	-		
Financial Assets Designated at Fair Value through Profit or Loss	-	-	-	-	-
Loans and Receivables to Banks	7,808	7,808	7,808		
Loans and Receivables to Other Customers	11,344,384	11,344,384	9,563,012		1,781,372
Financial Investments - Available- For Sale	8,449,101	8,449,101	8,449,101		
Financial Investments - Held-To- Maturity	-	-	-		-
Investments in Subsidiaries	-	-	-		
Investments in Associates and Joint Ventures	-	-	-		
Property, Plant and Equipment	413,591	413,591.00	413,591		
Investment Properties	-	-	-		
Goodwill and Intangible Assets	27,203	27,203	-		27,203
Deferred Tax Assets	-	-	-		
Other Assets	129,253	129,253	129,253		
Liabilities	**19,525,097**	**19,525,097**	**-**	**-**	**-**
Due to Banks	2,502,196	2,502,196			
Derivative Financial Instruments	-	-			
Other Financial Liabilities Held-For-Trading		-			
Financial Liabilities Designated at Fair Value Through Profit or Loss		-			
Due to Other Customers	15,984,398	15,984,398			
Other Borrowings	-	-			
Debt Securities Issued	-	-			
Current Tax Liabilities	(48,712)	(48,712)			
Deferred Tax Liabilities	-	-			
Other Liabilities	1,087,215	1,087,215			
Due to Subsidiaries	-	-			
Subordinated Term Debts	-	-			
Off-Balance Sheet Liabilities	**9,766,155**	**9,766,155**	**623,533**	**-**	**-**
Guarantees	514,154	514,154	75,278		
Performance Bonds	101,879	101,879	270,378		
Letters of Credit	156,053	156,053	31,211		
Other Contingent Items	319,209	319,209	23,702	-	
Undrawn Loan Commitments	5,785,774	5,785,774	222,964		
Other Commitments	2,889,086	2,889,086			
Shareholders' Equity		-			
Equity Capital (Stated Capital)/Assigned Capital		**-**			
of which Amount Eligible for CET1	6,227,391	6,227,391			
of which Amount Eligible for AT1	-	-			
Retained Earnings	359,925	359,925			
Accumulated Other Comprehensive Income	318,951	318,951			
Other Reserves	636,796	636,796			
Total Shareholders' Equity	**7,543,063**	**7,543,063**	**-**	**-**	**-**

Disclosure 12

Explanations of Differences between Accounting and Regulatory Exposure Amounts

Under SLFRS 9: “Financial Instruments: Recognition & Measurement”, the Bank assesses the impairment of loans and advances individually or collectively based on the principles of “expected credit loss” (Refer Note 3.1) model which is expected to take into account future trends in the economy. However, the regulatory provision made on loans and advances under the Direction No. 03 of 2008 on “Classification of loans and advances, Income Recognition and Provisioning” (and subsequent amendments thereof) issued by the CBSL are “time/delinquency base”. Further, under SLFRS 9, other debt financial assets not held at FVTPL, together with loan commitments and other off balance sheet exposures such as financial guarantees and letter of credits, are subject to impairment provision, whereas no such regulatory provision is required for those financial assets as per CBSL direction. As a result, SLFRS 9 recognises higher provisions compared to CBSL guidelines.

Financial investments and financial liabilities (other than FVTPL) are carried at "cost" for regulatory reporting purposes while they are classified as "Financial assets measured at fair value through other comprehensive income" carried at fair value or Financial assets/liabilities at amortised cost under the SLFRS 9. The "Fair value" is defined as the best estimate of the price that would be received to sell an asset or be paid to transfer a liability in an orderly transaction between market participants at the measurement date. A variety of valuation techniques combined with the range of plausible market parameters at a given point in time may still generate unexpected uncertainty beyond fair value. An “amortised cost” of a financial asset or financial liability is the amount at which the financial asset or liability is measured at initial recognition, minus principal repayments, plus or minus the cumulative amortisation using the EIR method of any difference between the initial amount recognised and the maturity amount, minus any reduction for impairment. Hence, the amortised cost of financial investments and financial liabilities under SLFRS 9 is different to the carrying value for regulatory reporting which is the "cost".

As per SLFRS 16, the Bank recognises a lease liability for leases previously classified as operating leases. Accordingly, the Bank measures the lease liability at the present value of the remaining lease payments, discounted using the Incremental Borrowing Rate (IBR). In addition, the Bank recognises right-of-use asset at an amount equal to the lease liability, on a lease-by-lease basis, adjusted by the amount of any prepaid or accrued lease payments relating to that lease. However as per regulatory reporting, the Bank charges the operating lease rentals as expense to profit or loss on an accrual basis.

Disclosure 13

Bank Risk Management Approach

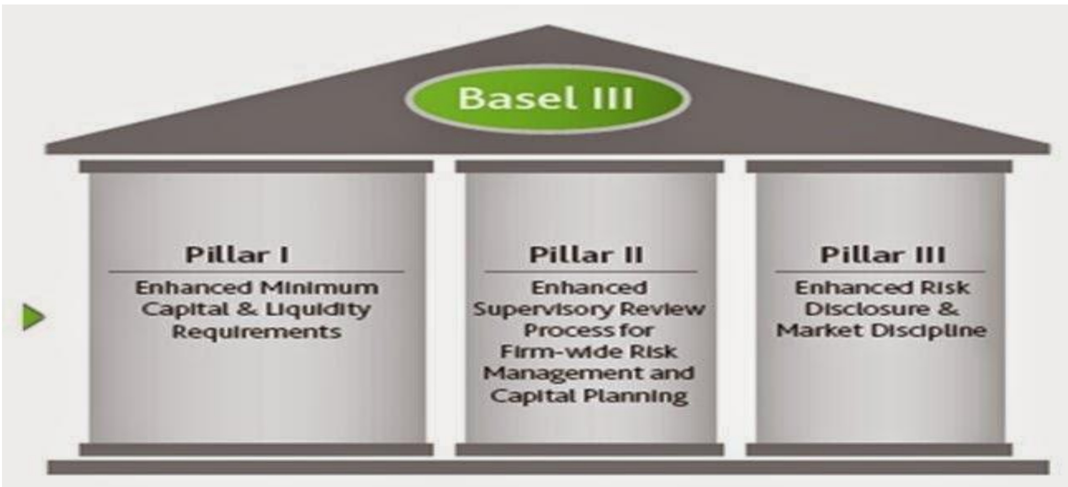
The management of MCB Bank Limited - Sri Lanka Branch actively drives the risk management framework wherein it provides an active approach in dealing with factors that influence the financial standing of the Bank. With the valuable guidance of management, the Bank has a proactive approach to generate recurrent earnings and to maximize shareholder's value by achieving an appropriate trade-off between risk and returns. All Effective Risk Management Framework along-with Robust Risk Governance Structure, Strong Capital & Liquidity Position and Good Quality of Credit Portfolio, remains a cornerstone to accomplish vision of the Bank.

Empowerment and independence are the basic principles in risk management and it is implemented as a fundamental part of management's vision. Independence of areas that are responsible for measuring, analyzing, controlling and monitoring risk from the frontline risk takers (i.e. business soliciting groups) is ensured within the bank.

The management and its Risk Management & Portfolio Review Committee have ensured formulation and implementation of a comprehensive Risk Management Framework. Under managements' guidance, the Bank executed risk strategy and continued to undertake controlled risk-taking activities within the risk management framework; combining core policies, procedures and process design with active portfolio management. The Risk Management Framework requires strong integrated risk management practices in key strategic, capital and financial planning processes and day-to-day business processes across the organization, with a goal to ensure that risks are appropriately considered, evaluated and responded to in a timely manner.

Disclosure 13

FINANCIAL STABILITY THROUGH RISK MANAGEMENT



A clear understanding of risks surrounding the business activities is essential for any organisation to create sustainable stakeholder value through executing its strategies. It is therefore, essential to reinforce the overall strategy of an organisation with a prudent risk management strategy so that the opportunities could be optimised while minimising the effects of down-side risks. Banks which are responsible for the vital role of financial intermediation in the economy should be more committed to managing their risks in a prudent and transparent manner compared to a normal business organisation. Accordingly, Basel Committee on Banking Supervision has formulated broad supervisory standards and guidelines to inculcate industry best practices across the banking institutions through 'Basel Accords' (Basel II, the second of the Basel Accords which has been extended by Basel III). While Basel Accord encourages convergence towards common approaches and standards, the ultimate purpose of these rules is to create financial stability and resilience in financial sector institutions.

MCB BANK LIMITED - SRI LANKA BRANCH APPROACH

MCB Bank Limited, Sri Lanka operation has also been identified Risk Management as the forefront of the future banking business. Accordingly in line with bank's global procedures and practices, the bank has developed a robust Risk Management Framework for its Sri Lanka operation as well.

INTEGRATED RISK MANAGEMENT COMMITTEE

Integrated Risk Management Committee of MCB Bank limited Sri Lanka operates as the forefront of bank's Risk Management functions.

Risk Management functions are underpinned by a comprehensive, Integrated Risk Management Policy, which is constantly evolving and enhancing to remain relevant and most effective. The policy which is approved by the Board spells out the Bank's approach to Risk Management. The policy sets out the process of identifying, measuring, monitoring and controlling the different types of risks and the risk governance structure in place. The main objectives of the framework are;

Disclosure 13

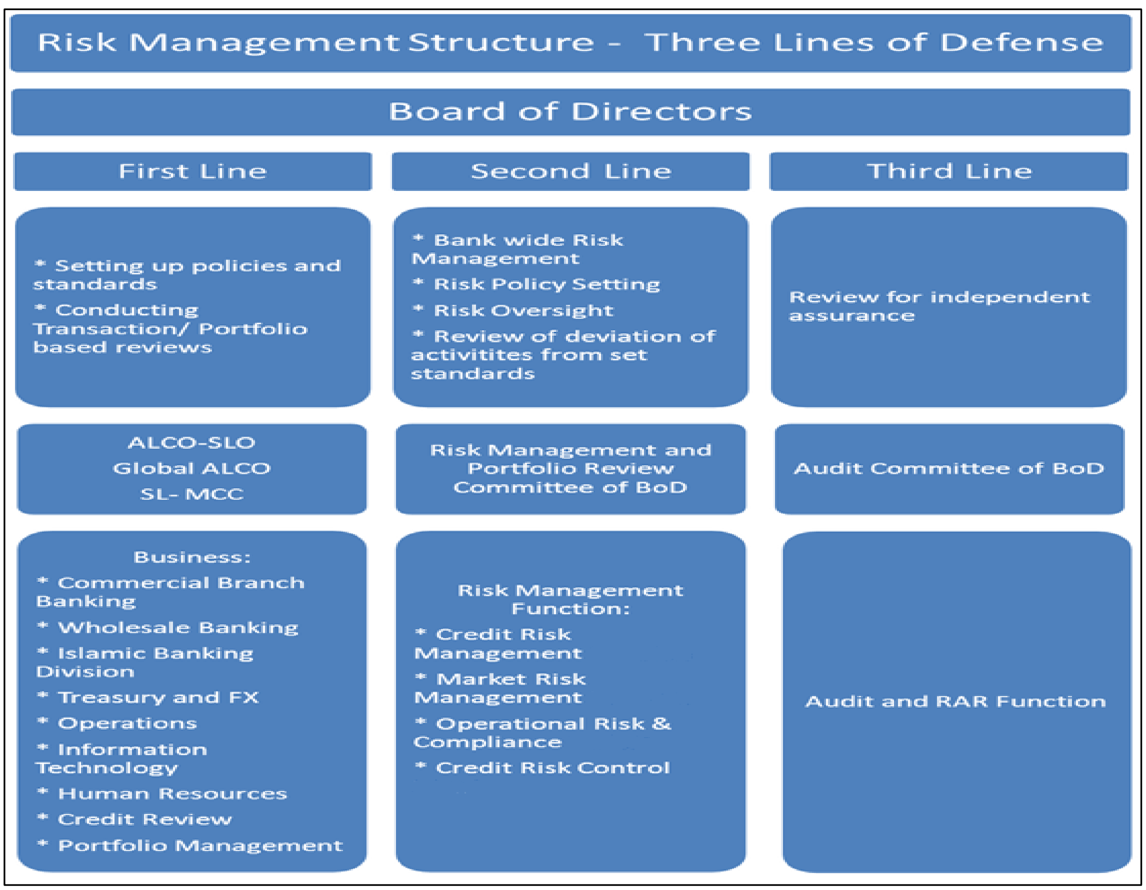
· To establish common principles, standards for the management and control of all risks and to inform behavior across the Bank.
· Provide a shared framework and language to improve awareness of risk management processes among all stakeholders.
· To provide clear accountability and responsibility for Risk Management.
· To ensure consistency throughout the Bank in Risk Management
· Define the Bank's risk appetite and align its portfolios and business strategy accordingly.
· Optimize risk return decisions.
· Maintain/manage the Bank's capital adequacy and liquidity position.
· Further strengthen governance, controls and accountability across the organization

In addition to the main risks (viz. Credit Risk, Market Risk and Operational Risk), the Bank has considered several other risks which are material to it. These additional risk categories include, Liquidity Risk, Interest Rate Risk in the Banking Book, Compliance Risk, IT Security Risk and Reputational Risk.

RISK GOVERNANCE

THREE LINES OF DEFENSE

MCB Bank limited promotes strong risk governance applied rationally and consistently with strong emphasis on the concept of “Three Lines of Defense”. This governance structure encompasses accountability, responsibility, independence, reporting, communications and transparency, both internally and with external stake holders.



Disclosure 13

RISK APPETITE AND TOLERANCE

Risk appetite is an expression of the amount of risk that the bank is prepared to accept in delivering its promises and meeting the responsibilities to the stakeholders at large. It is inevitable that the Bank will accept risks, hence risk taken within appetite may give rise to expected losses, but these as analyzed and accepted will be sufficiently absorbed by the expected earnings.

The Bank strives to make the integrated risk management function as one of its most critical core competency. Bank relies upon the overall policy framework to ensure the maintenance of consistent high standards in its operations and to encourage the risk decision making process by raising the risk awareness that could hinder the risk and return relationship.

CREDIT RISK

Credit risk refers to the potential loss of interest, capital or value of the collateral due to an obligor's failure to meet the term of a contract or otherwise failing to perform as agreed. Credit risk can arise from both on and off balance sheet activities consisting of contingent liabilities incurred by the Bank and due to the Bank, from counterparties such as letters of credit, letters of guarantee etc. The Bank has adopted stringent credit risk management process to mitigate the risk associated with the loan book by way of following strategic initiatives:

· Credit risk management organization structure incorporating a Credit Risk & Review Unit reporting to Chief Risk Officer (CRO) who in turn reports to the Group Head – Risk Management at Head office level.

· Written policies on credit granting and procedure bank - wide risk management, credit risk management, loan review mechanism and review of such policies on periodically.

· Instructions and guidance to employees in credit chain on annually/quarterly review of credit facilities, credit origination and maintenance procedures and guidelines for portfolio management.

· Established accountability of branch managers, relationship managers and business unit heads for managing risk within risk management framework of the Bank.

· Assignment of borrower risk rating for all general credit facilities.

· Risk based pricing: When a borrower's credit risk increases, the Bank demands a higher credit risk premium by way of increasing the interest rate.

· Established independent Credit Administration Unit to ensure accuracy and maintenance of security documentation of credit facilities and limit setting.

· Established credit risk limits for risk rating and concentration on segment, industry, geography, and personal banking products.

· Independent loan reviews carried out by the Group Audit Department as a special assignment by way of pre and post disbursement examinations of credit papers in order to ensure the quality of the loan book.

· Impairment on the potential delinquents by way of reviewing objective evidence assessments by the business units and adequacy of impairment provisions to absorb credit risk of the lending book.

· A constant stress testing methodology is applied on all significant credit exposures and stress tests are carried out on a regular basis.

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MARKET RISK

Market risk is the risk associated with movements in market factors, including foreign exchange rates, interest rates, equity prices and commodity prices which have an impact on the Bank’s income or the value of its portfolios. Its effective recognition could minimize the potential loss of earnings or economic values arising principally from customer driven transactions and banks relevant investments.

The categories of market risk of the Bank are:
- Interest rate risk
- Foreign exchange risk
- Equity price risk
- Commodity price risk

Market risk exposures arising from the trading book are managed by the Treasury Department whilst the non trading activities relating to market risks are managed through the ALCO (Assets and Liabilities Committee).

The Integrated Risk Management Committee (IRMC) is responsible for policies and other standards for the control of market risk. Market Risk goals are closely monitored by Treasury Middle Office and discussed on a periodic basis for appropriate and timely action.

The Bank measures the risk of losses arising from future potential adverse movements in market rates, prices and volatilities using VaR methodology. VaR, in general, is a quantitative measure of market risk that applies recent historical market conditions to estimate the potential future loss in market value that will not be exceeded in a set time period at a set statistical confidence level. This exercise is carried out by Treasury Middle Office with the help of Bloomberg system. Results are reviewed periodically at the Integrated Risk Management Committee (IRMC) meetings.

Stress testing is an integral part of the market risk management framework and considers both historical market events and forward-looking scenarios. A consistent stress-testing methodology is applied to trading and non-trading books. Regular stress-tests are carried out on liquidity risk (both bank specific and market specific scenarios), foreign exchange risk and equity risk.

LIQUIDITY RISK

Liquidity risk is defined as the risk that the Bank will encounter in meeting obligations associated with financial liabilities that are settled by delivering cash or another financial asset. It is the policy of the Bank to ensure that adequate liquidity is maintained in all currencies to meet its obligations. This is performed through cash flow management, maintenance of liquidity ratios such as statutory reserve ratio, statutory liquid asset ratio, liquidity coverage ratio and advances to deposit ratio.

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MANAGING INTEREST RATE RISK

Interest Rate Risk is the risk to the Bank's earnings and capital that arises out of meeting customers' demands for interest rate-related products with various re-pricing profiles and the bank's interest rate mismatch strategy. As interest rates and yield curves change over time, theoretically the Bank may be exposed to a loss in earnings and capital due to the re-pricing structure of all on- and off-balance sheet items. Movements in interest rates can affect the Bank's earnings by changing its net interest income (NII).Changes in interest rates also affect the economic value of the bank's assets, liabilities and off-balance sheet items. An effective risk management process that maintains interest rate risk within prudent levels is essential not only to safety and soundness but also to the Bank's profitability.

ASSETS AND LIABILITIES COMMITTEE (ALCO)

The Bank's exposure is controlled by limits approved by the Board which are monitored by the Assets and Liabilities Committee. ALCO overlooks the management of the Bank's overall liquidity position, and is responsible for Liquidity Risk and Interest Rate Risk Management of the Bank and implementation of liquidity management policies, procedures and practices approved by the management. This is achieved through proper representation of key business heads, frequent ALCO meetings and continuous monitoring of the liquidity position of the Bank through reports submitted by Treasury Middle Office.

OPERATIONAL RISK

Operational Risk is the risk of loss resulting from inadequate or failed Internal Processes, People, and System or from External events.

Operational Risk is relevant to every aspect of the Bank's business and covers a wide spectrum of issues. Losses arising through fraud, unauthorized activities, errors, omissions, inefficiency, and system failure or from other external events fall within the operational risk definition. Bank follows below detailed process to ensure that the Operational Risk is within the tolerance limits

- Loss event data collection

Loss event data are historic and backward looking which provides valuable insights into current operational risk exposures. All staff members are responsible to report risk/ loss events as soon as they perceive or materialize and are responsible to record such risk/ loss events immediately as an actual loss, a potential loss or a near misses.

- Risk & control self-assessment (RCSA)

In a RCSA program, branches and departments takes the ownership of its own risks & controls and assess the risks that may exist in its area. RCSA programs are done on a set frequency to assess the risk areas of the bank and apply controls where necessary.

- Ad-hoc incident reporting

Bank encourages staff to report any operational lapses or potential or actual frauds directly to designated senior management officials as described in the Bank's Whistleblower policy, if the staff member is fearful to route the concerns through the line management. Bank views this method as a useful method of communication to reduce potential losses to a greater extent and proved effective.

- New product, service or process launch

Prior to launching new products, services or processes, the owners must evaluate the risks as per new product policy and then to incorporate sufficient safe guards.

- Staff Training

Internal training sessions are conducted to enhance/inculcate the need of risk reporting for new recruits and refresher training sessions too conducted for existing staff.

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COMPLIANCE RISK

Compliance risk is the current and prospective risk to earnings or capital arising from violations of, or nonconformance with, laws, rules, regulations, prescribed corporate governance practices, internal policies and procedures, or ethical standards. Compliance risk also arises in situations where the laws or rules governing certain bank products or activities of the bank's clients may be ambiguous or untested. This risk exposes the institution to fines, penalties, payment of damages, and the voiding of contracts. Compliance risk can lead to diminish reputation, limited business opportunities, reduced expansion potential, and an inability to enforce contracts. Bank has identified this risk as a material risk and various internal controls, policies, procedures are in place to manage risk.

REPUTATION RISK

Reputation Risk refers to the potential adverse effects, which can arise from the Bank's reputation being tarnished due to factors such as unethical practices, regulatory actions, subsidiary/ associate company's actions, customer dissatisfaction and complaints, negative/adverse publicity etc. The Bank remains committed to continuously strive to maintain and improve its reputation in all the businesses it operates.

IT RISK

In the wake of increasing financial cyber-crimes, IT Security has become one of the important areas of banking operation. Accordingly a comprehensive IT Security platform has been developed by bank's IT team to guide, monitor and implement necessary processes and procedures specified in the Information Security Policy (ISP) to align with the bank's overall Risk Management Framework. The purpose of the ISP to protect the cyber threats and ensure IT security of the bank.

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Risk management related to key risk exposures

The quantitative disclosures relating to key risk areas such as credit, market,liquidity, operational and interest rate risk in the banking book are presented and discussed in the Financial risk management report in note 6.