

Basel - Pillar 3 Disclosures - June 30, 2019

Bandhan Bank Limited (hereafter referred as the “Bank”) aims to operate within an effective risk management framework to actively manage all the material risks faced by the Bank, in a manner consistent with the Bank’s risk appetite.

Bandhan Bank Limited commenced its banking operations on August 23, 2015. As per the Scheme of Arrangement, the entire balance sheet of Bandhan Financial Services Limited (BFSL) was transferred to Bandhan Bank Limited with effect from August 23, 2015. The Bank got listed on March 29th, 2018 on NSE & BSE.

As per the directions of RBI on Guidelines for Licensing of New Banks in the Private sector dated February 22, 2013, being a newly launched bank, Bandhan Bank Limited was required to maintain a minimum capital adequacy ratio of 13 per cent of its total Risk Weighted Assets (RWA) for a minimum period of three years after commencement of its operations till August 23, 2018. Subsequently, Bank’s capital requirement is guided by the Basel III Capital norms published by RBI. This document covers the Capital Adequacy status for Bandhan Bank Limited. It also describes the Risk Process and Governance at the Bank to effectively assess, monitor and report risk.

1. Scope of Application and Capital Adequacy**DF - 1: Scope of Application**

The framework of disclosures applies to Bandhan Bank Limited (hereinafter referred to as the Bank), a scheduled commercial bank, incorporated on August 23, 2015. Currently, the Bank does not have any financial or non-financial subsidiary.

DF - 2: Capital Adequacy*Qualitative Disclosure:*

The Bank has a process for assessing its overall capital adequacy in relation to the Bank's risk profile and strategy for maintaining its capital levels. The process provides an assurance that the Bank has adequate capital to support all risks inherent to its business and an appropriate capital buffer based on its business profile. The Bank identifies, assesses and manages comprehensively all risks that it is exposed to through sound governance and control practices, robust risk management framework and an elaborate process for capital calculation and planning.

In line with the Basel III guidelines which are effective since April 01, 2013, the Bank has calculated its capital ratios as per the extant RBI guidelines. The main focus of Basel III norms is on the quality and quantity of Tier I capital and these regulatory requirements are currently met with the quantum of capital available with the Bank. The Pillar I Risk Weighted Assets (RWA) Calculation covers the following risks:

- i. Credit Risk (Standardized Approach)
- ii. Market Risk (Standardized Approach)
- iii. Operational Risk (Basic Indicator Approach)

As on June 30th, 2019, the Bank had a total capital of Rs. 11,205.56 Cr, out of which Tier-I capital stood at Rs. 10,675.65 Cr. The Capital to Risk Assets Ratio (CRAR) of the Bank stood at 27.03% against regulatory requirement of 10.875%.

The Bank carries out Capital Planning to assess its capital adequacy in line with business projections and to allocate capital effectively across different business lines so as to ensure availability of capital in the future. The Bank also has in place the Internal Capital Adequacy Assessment Process (ICAAP) wherein, all risks relevant to the bank are

identified and the risk factors are stressed to measure the capital requirement for such risk. Capital is then allocated to each risk measure, accordingly.

Quantitative Disclosure

The standalone CRAR position of the Bank as on June 30th, 2019 stood as below

<u>Capital Requirement</u>	
	(Rs in crore)
(a) Risk Weighted Assets for Credit Risk:	
Portfolios subject to Standardised approach	33,210.54
Securitisation	-
(b) Risk Weighted Assets for Market Risk:	
Standardised duration approach	686.71
Interest Rate Risk	625.13
Foreign exchange Risk (including Gold)	56.25
Equity Risk	5.33
(c) Risk Weighted Assets for Operational Risk:	
Basic indicator approach	7562.64
(d) Total Risk Weighted Assets	
	41459.89
(e) Common Equity Tier 1, Tier 1 and Total capital ratio:	
CET 1	25.75%
TIER 1	25.75%
TIER 2	1.28%

2. Risk Exposure and Assessment

The Bank encourages calculated risk-taking, where risks are known, and are within the risk limits arising from the Board approved risk appetite. Also while evaluating the risks, the associated returns are also considered. The key constituents that promote “Risk aware culture” in the Bank are:

- Encourage employees to take business decisions in line with the Bank’s approved risk appetite;
- Treatment to whistleblowers who report on fraudulent activities;
- Treatment to employees who report potential risks; and

- Adequate and regular training of personnel in the business areas on their roles in risk management.

Risk transparency is fostered through reporting, disclosure, sharing of information and open dialogue on the risks arising from various activities across the Bank.

Risk Governance Model

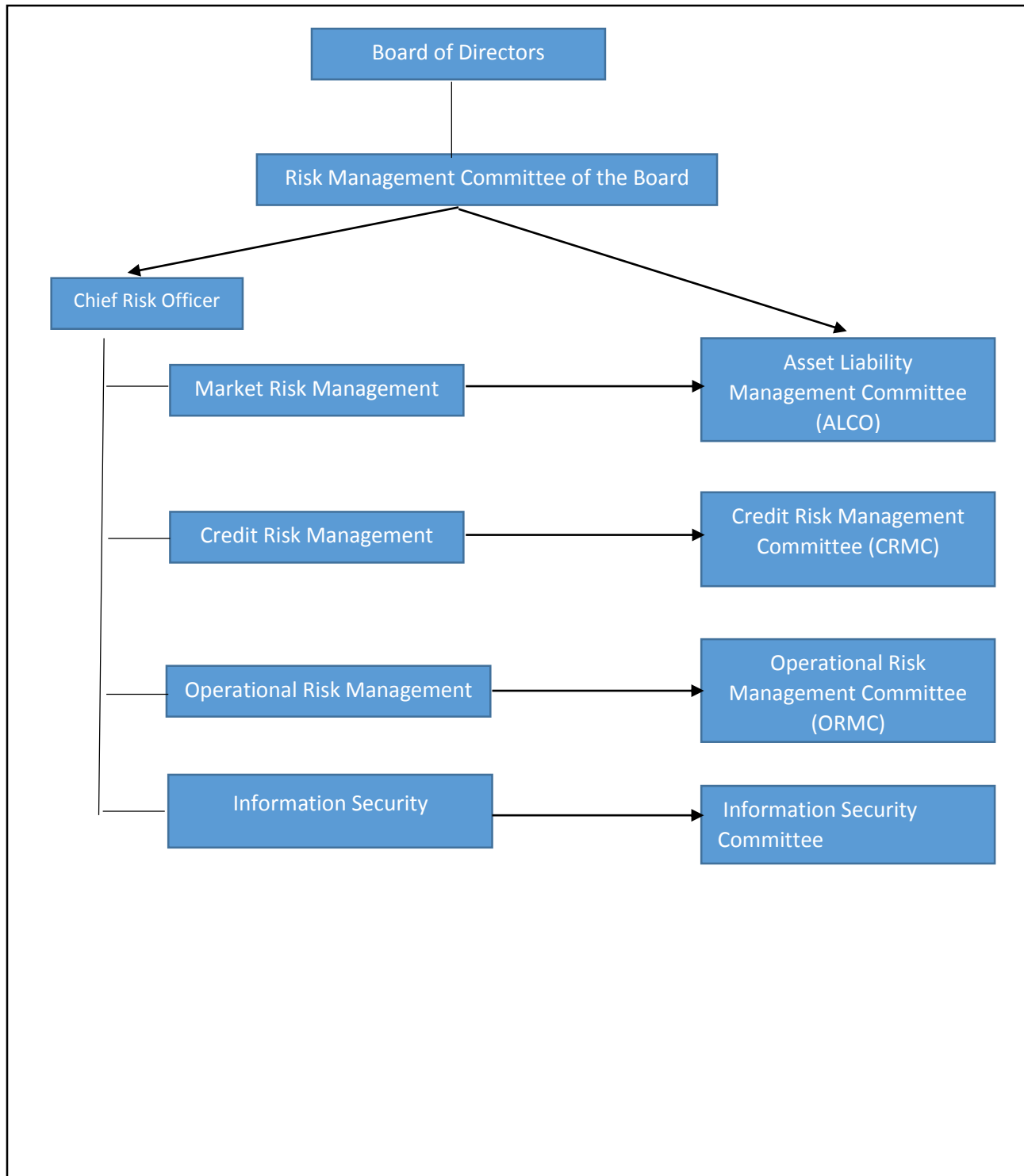
The Bank has established a robust system for directing and controlling the management of various risks within and across the Bank. This governance model defines three key roles:

- Business that take, manage, and assess risk;
- Risk Management that provide risk appetite, governing policies, analysis, monitoring, and reporting; and
- Internal Audit that provide independent inspection and assurance.

Risk Management Department is responsible for setting up the appropriate risk control mechanism to quantify and monitor risks in timely manner.

Risk Governance Framework

The Bank believes that the role of risk management should not be biased by consideration of profits or performance evaluation and should be in line with regulatory guidelines and international good practices. The risk governance framework has been designed taking this into account.

Risk Governance Structure

The risk governance framework provides guidance on adopting a more holistic approach to manage risk, emphasizing four related elements:

- Developing the corporate risk profile;
- Establishing an risk function that manages risk in an integrated manner;
- Practicing integrated risk management; and
- Ensuring continuous risk monitoring.

The risk governance framework for the Bank is supported by the detailed roles and responsibilities within the Bank.

Governance Committees

Key roles and responsibilities relating to risk management are clearly defined and stated below:

Board of Directors

Board of Directors (BoDs) has the overall responsibility for management of all the Risks. The key responsibilities of BoDs are the following:

- Be aware of the major aspects of the bank's risks that should be managed, and should approve an appropriate risk management framework for the bank and review it periodically;
- Based on the recommendation of RMCB and individual RMCs, approve and periodically review the risk appetite, risk management policies, and processes;
- Establish a management structure, which can effectively implement the Bank's risk management framework and define clear lines of management responsibility, accountability and reporting;

- Provide senior management with clear guidance and direction with respect to promotion of risk management culture and awareness in the bank;
- Ensure that the Bank has adequate internal controls (empower internal audit) in place to oversee the implementation of policy and procedures;
- Approve ICAAP and the underpinning capital requirements periodically;
- Ensure that the Bank has in place appropriate methods for monitoring compliance with laws, regulations, and supervisory and internal policies; and
- Obtain assurance (through internal audit and external reviews) that the Bank's risk management policies for significant risks are being adhered to.

Risk Management Committee of the Board (RMCB)

RMCB has overall responsibility to oversee the Integrated Risk Management program including Credit, Market, Operational and other key risks. The committee is responsible to:

- Oversee risk management function and obtain assurance from the respective committees and risk departments that the key risks facing the Bank have been properly identified and are being appropriately managed;
- Define the risk appetite of the Bank within overall parameters set by the Board including business strategy & growth and review Risk Profile on quarterly basis
- Ensure effectiveness in the conduct of the overall risk governance;
- Approve risk limits at the bank-wide level for various portfolios such as product, industry, geography, risk types etc.;

- Approve risk management and measurement policies/ guidelines and procedures before submission to the Board;
- Allocate and maintain sufficient resources (including IT support) for risk identification, measurement, monitoring and reporting;
- Approve risk capital computation and place it to the Board for approval;
- Reinforce the culture and awareness of risk management throughout the organization.
- Approve and ensure robustness of financial models and effectiveness of systems used to measure Credit Risk whenever applicable, which include:
 - Approve all material credit risk models
 - Approve the use of risk rating systems for business and risk management purposes;
 - Ensure effectiveness and performance of rating system and associated processes and controls
 - Approve all material credit risk models and rating systems along with changes if any made to them; and
- Discuss the findings of the Audit Committee of the Board (ACB) whichever and whenever deemed necessary

Audit Committee of the Board

The Audit Committee of the Board (ACB) is responsible to:

- Assist the Board in carrying out its oversight responsibilities as they relate to the Banks financial and reporting practices, internal control and compliance with laws, regulations and ethics

Financial and Other Reporting

- Provide assurance to the governing board that financial information reported by management reasonably portrays the Bank's financial condition, results of operations, and plans and long-term commitments;
- Review of financial and/or fiscal policies and policy decisions;
- Review of the financial statements including interim financial statements, auditors opinion and management letter;
- Recommendations on the selection of the external auditors or participation in the selection of external auditors;
- Oversight of the external audit coverage; and
- Review of other reports that require approval by the BOD prior to submission.

Internal Control

- Understand the Bank's key risk areas and the internal controls structure;
- Monitor the control process through the results of internal and external audits;
- Examining and evaluate the planning, organization and directing processes to determine that the objectives and goals will be achieved; and
- Evaluate systems, processes, operations, functions & activities within the organization.

Compliance with Laws, Regulations and Ethics

- Provide reasonable assurance to the governing board that the Bank is in compliance with pertinent laws and regulations, is conducting its affairs ethically, and is maintaining effective controls against conflicts of interest /fraud.

Market Risk Management Committee (MRMC)

The Market Risk Management Committee (MRMC) is responsible for:

- Setting policies and guidelines for market risk measurement, management and reporting and placing before the Board for approval;
- Identification, assessment, monitoring, reporting and analysis of market risk associated with treasury operations, setting of risk parameters, overseeing compliance with risk parameters etc.;
- Reviewing and ensuring adherence to market risk limits, including triggers or stop-losses for traded and accrual portfolios;
- Risk research and analysis, development of risk mitigation strategies;
- Ensuring robustness of financial models, and the effectiveness of all systems used to calculate market risk;
- Ensure appointment of qualified and competent staff and support RMCB in the conduct of effective market risk governance;
- Ensure effective management of currency and country risk;
- Review the stress testing results.

Currently, the responsibilities of MRMC is being carried out by ALCO.

Asset Liability Management Committee (ALCO)

The Asset Liability Management Committee (ALCO) is responsible for:

- Manage the liquidity gaps and the interest rate risk by deciding on desired maturity profile and mix of incremental assets and liabilities and effectively articulate the balance-sheet management strategies;
- Approve risk limits and triggers for liquidity and interest rate risks and ensuring adherence to the limits set by the Board;
- Ensure the effectiveness of the Contingency Funding Plan;

- Articulating interest rate view of the Bank and deciding on the future business strategy;
- Review and articulate the fund management;
- Approve the transfer pricing mechanism for the Bank and ensure the effective balance sheet management;
- Review micro and macro-economic factors;
- Approve pricing for deposits and advances;
- Review the stress testing results.

Credit Risk Management Committee

CRMC is responsible for overseeing implementation of Credit Risk Management Framework across the Bank and providing recommendations to the RMCB. Key responsibilities of the committee include:

- Review and approve the Risk profile of the Bank.
- Review and recommend policies pertaining to Credit Risk Management to the RMCB for review and approval;
- Clear policies on standards for presentation of credit proposals, financial covenants, rating standards and benchmarks and recommend to the Board, for its approval.
- Reviewing Credit Approving Powers (CAM) as per Credit Policy, prudential limits on large credit exposures, standards for loan collateral, portfolio management, loan review mechanism, risk concentrations, risk monitoring and evaluation, provisioning, regulatory / legal compliance.
- Ensure implementation of credit risk policy and strategy approved by the Board as per the directions of the RMCB;
- Monitor credit risk on a bank wide basis and ensure compliance with limits approved by Board

- Monitor quality of loan portfolio at periodic intervals, identifying problem areas and issuing directions for rectifying deficiencies;
- Monitor credit risks on the Bank-wide basis and ensuring compliance with the approved risk parameters/ prudential limits and monitor risk concentrations including industry exposures;
- Ensure regulatory compliance in the Bank's policies and guidelines in regard to credit risk;
- Recommending changes in Delegation of Power (DOP) to appropriate authority within the overall limit approved by Board.
- Review all rating system validation results to assess efficacy and effectiveness of model performance and the need for any adjustments, and placing recommendations before RMCB if required
- Review the use of internal risk rating systems for business and risk management purposes and placing recommendations before the RMCB;
- Bring to the attention of RMCB material issues for information / recommendation / approval; and
- Review and approve the credit risk stress testing scenarios, results and outcome analysis.

Operational Risk Management Committee

The Operational Risk Management Committee is responsible for:

- Develop ORM Framework in terms of all the policies and procedures, methodologies, models, tools and system for their effective implementation;
- Assess operational risk inherent in new areas (e.g. products, activities, processes and systems) before they are introduced, and identify risks tied to new or existing product development and significant changes in order to ensure that the risk profiles of product lines are updated regularly;.

- Review and ensure that Bank has adequate business continuity and disaster recovery mechanism in place which are reviewed and timely tested for their working effectiveness;
- Review and assess the results of compliance risk and information security risk management related processes including key issues, risk incidents, internal and external changes, their inclusion in the overall risk profile of the Bank and issue the necessary guidance;
- Ensure that operational risk issues are effectively communicated to appropriate staff responsible for managing credit, market and other risks, as well as those managing third-party outsourcing arrangements;
- Ensure integration of operational risk management practices into day to day operations of the Bank; and
- Ensure the responsibilities and accountabilities at all levels of the staff with adequate number of resources having requisite level of qualification, experience and training in order to effectively manage operational risk.

Audit Committee of Executives

The Audit Committee of Executives is responsible to:

- Provide an independent assurance to the Board on their assessment of compliance with the risk processes across the Bank;
- Independently validate the ratings/ scores assigned Credit Risk Management Team post sanction of loans and reporting the deviations;
- Review (at least annually) the scoring/ rating system and its operations, capital calculations under various approaches including the estimation of PDs, LGDs and EADs;
- Independently validate proper implementation of risk mitigation plans drawn out by the focus group or committees for various key risks;

- Independently validate that the significant risks identified under RCSA process is incorporated in the Operational loss warehouse;
- Give assurance to the board on the management of risks, including the effectiveness of the controls and the compliance and irregularities;
- Give assurance to the board on the accuracy of the reporting and the appropriateness of the risk reporting design; and
- Feedback on the adherence to the Bank's values and code of ethics.

DF -3: Credit Risk***Qualitative Disclosure***

Credit risk is the risk of loss that may occur due to default of the counterparty or from its failure to meet its obligations as per terms of the financial contract. Any such event will have an adverse effect on the financial performance of the Bank. The Bank faces credit risk through its lending, investment and contractual arrangements. To counter the effect of credit risks faced by the Bank, a robust risk governance framework has been put in place. The framework provides a clear definition of roles as well as allocation of responsibilities with regard to ownership and management of risks. Allocation of responsibilities is further substantiated by defining clear hierarchy with respect to reporting relationships and Management Information System (MIS) mechanism.

i. Credit Risk: Strategies and processes

The Bank has defined and implemented various risk management policies, procedures and standards with an objective to clearly articulate processes and procedural requirements that are binding on all concerned Business groups. The Credit Policy and the Credit Risk Management Policy of the Bank is guided by the objective to build, sustain and maintain a high quality credit portfolio by measurement, monitoring and control of the credit exposures. The policies also address more granular factors such as

diversification of the portfolio across companies, business groups, industries, geographies and sectors. The policies reflect the Bank's approach towards lending to borrowers in light of prevailing business environment and regulatory stipulations.

The Bank's Policies also detail the standards, processes and systems for growing and maintaining its diversified portfolio. The policies are reviewed annually in anticipation of or in response to the dynamics of the environment (regulatory & market) in which the Bank operates or to change in strategic direction, risk tolerance, etc. The policies are approved by the Board of Directors of the Bank.

To avoid concentration of credit risk, the Bank has put in place internal guidelines on exposure norms in respect of single borrower, groups, exposure to sensitive sector, industry exposure, unsecured exposures, etc. Norms have also been detailed for soliciting new business as well as for preliminary scrutiny of new clients. The Bank abides by the directives issued by RBI, SEBI and other regulatory bodies in respect of lending to any industry including NBFCs, Commercial Real Estate, and Capital Markets. In addition, internal limits have been prescribed for certain sensitive segments based on prudential considerations.

In view of putting in place a comprehensive credit risk framework to aggregate overall credit risk perception of the Bank Risk Profiling is carried out as a part of Risk Appetite Framework to access, monitor and communicate the risk perception to Board & senior management. The framework is approved by the Board of Directors via Risk Management Committee of the Board and any change in the appetite, credit risk limits or credit risk parameters get approved by the Board of Directors only. This process of quantification and benchmarking via credit risk helps senior leadership to understand the risk and monitor by way of constant tracking.

ii. Credit Risk: Structure and organization

The organizational structure for Credit Risk Management is as follows:

- Board of Directors
- Risk Management Committee of Board (RMCB)
- Credit Risk Management Committee (CRMC)
- Chief Risk Officer (CRO)
- Head - Credit Risk Department
- Credit Risk Department

iii. Credit Risk: Scope and nature of measurement systems

The Bank's approach for credit risk identification and assessment of credit risks underlying both funded and non-funded exposures is explicitly set out. All credit proposals are subject to a credit risk scoring process / risk rating process based on the quantum of advance value to support credit approvals and decision making as well as to enhance risk management capabilities for portfolio management, pricing and risk based capital measurement.

iv. Credit Risk: Policies for hedging and/or mitigating risk

Credit risk is defined as the possibility of losses associated with default by or diminution in the credit quality of Borrowers or Counterparties arising from:

- Outright default due to inability or unwillingness of a borrower or counterparty to meet commitments in relation to lending, trading, settlement and other financial transactions; or
- Reduction in portfolio value arising from actual or perceived deterioration in credit quality of borrowers or counterparties.

Credit Risk emanates from the Bank's dealings with an individual, non-corporate, corporate, bank, financial institution or sovereign.

The Bank's credit risk governance framework is being built up to strengthen risk evaluation and management of credit whilst positioning the Bank to effectively and efficiently manage changes in the environment. Through an effective, Board approved risk governance framework, the Bank seeks to ensure adequate risk oversight, monitoring and reporting of credit risks.

The responsibilities for managing credit risk extend throughout the Bank. Key principles of credit risk governance are:

- Adequate oversight, monitoring and control of credit risk through the Board, risk committees and senior management.
- Clearly defined roles and responsibilities for overall credit risk management.
- Establishment of functional independence of Credit Risk Management function from personnel and management functions responsible for credit origination and credit administration.
- Appropriate mechanisms to ensure that the Board and senior management understand credit risk rating systems design and operations through regular training and involvement in the model review and approval processes.
- Business units monitor and manage credit risk in their businesses and report

Quantitative Disclosures

a. Total gross credit risk exposure by facility:

(Rs in Cr)	
Facility Type	Credit Exposure
Fund Based	42,104.43
Non-Fund Based	94.70
Total	42,199.13

b. Total gross credit risk exposure by geography:

(Rs in Cr)

Category	Fund Based	Non-Fund Based	Total Credit Exposure
Domestic	42,104.43	94.70	42,199.13
Overseas	-	-	-
Total	42,104.44	94.70	42,199.13

c. Total gross credit risk exposure by industry:

(Rs in Cr)

Industry	Fund Based	Non-Fund Based	Total Credit Exposure
A. Mining and Quarrying	0.01	-	0.01
B. Food Processing	541.41	-	541.42
C. Beverages (excluding Tea & Coffee) and Tobacco	2.20	-	2.20
D. Textiles	1698.25	5.00	1703.25
E. Leather and Leather products	83.95	-	83.95
F. Wood and Wood Products	137.49	-	137.49
G. Paper and Paper Products	1.98	-	1.98
H. Petroleum (non-infra), Coal Products (non-mining) and Nuclear Fuels	5.27	-	5.27
I. Chemicals and Chemical Products (Dyes, Paints, etc.)	21.23	1.00	22.23
J. Rubber, Plastic and their Products	38.36	-	38.36
K. Glass & Glassware	51.13	-	51.13
L. Cement and Cement Products	14.37	-	14.37
M. Basic Metal and Metal Products	49.38	21.45	70.83
N. All Engineering	666.14	-	666.14
O. Vehicles, Vehicle Parts and Transport Equipment	0.71	-	0.71
P. Gems and Jewellery	58.26	-	58.26
Q. Construction	-	-	-

Industry	Fund Based	Non-Fund Based	Total Credit Exposure
R. Infrastructure	0.09	-	0.09
S. Other Industries	2573.36	-	2573.36
Residuary other advances (to tally with gross advances)	36160.84	67.25	36228.09
Total	42104.44	94.70	42199.13

d. Residual maturity breakdown of Assets:
(Rs in Cr)

Particulars	Day 1	2 to 7 days	8 to 14 days	15 to 28 days	29 days to 3 months	Over 3 month & up to 6 months	Over 6 month & up to 1 year	Over 1 Year & up to 3 years	Over 3 Years & up to 5 years	Over 5 years	Total
Liabilities											
Borrowings	-	-	-	-	297.60	-	-	160.00	-	-	457.60
Deposits	155.21	1,035.13	1,033.26	434.87	1,355.79	2,296.40	13,028.42	22,472.82	1,505.34	384.22	43,701.46
Foreign Currency Liabilities	-	13.80	-	-	8.28	-	-	2.14	-	-	24.22
Total	155.21	1,048.93	1,033.26	434.87	1,661.67	2,296.4	13,028.42	22,634.96	1,505.34	384.22	44,183.28
Assets											
Advances	195.93	823.64	1,017.64	2,254.67	7,694.20	9,878.26	11,018.94	6,120.33	469.90	2,012.19	41,485.70
Investment	-	549.09	250.16	-	1196.93	276.30	2231.37	44.03	989.50	5199.84	10737.22
Foreign Currency Assets	23.31	-	-	-	-	-	5.66	1.24	-	-	30.21
Total	23.31	1372.73	1,267.8	2,254.67	8,891.13	10,154.56	13,255.97	6,165.6	1459.4	7,212.03	52,253.13

e. Position of Non-Performing Assets (NPA):
(Rs in Cr)

Particulars	As on June 30, 2019
Gross Advances	42,104
Net Advances	41,485
Gross NPA	851
1. Substandard	773

Particulars	As on June 30, 2019
2. Doubtful 1	74
3. Doubtful 2	2
4. Doubtful 3	2
5. Loss	-
NPA Provision	619
Net NPA	232
NPA Ratios	
Gross NPA to Gross Advances (%)	2.02%
Net NPA to Net Advances (%)	0.56%

f. Movement of Non-Performing Assets (NPA Gross):
(Rs in Cr)

Particulars	As on June 30, 2019
Opening Balances	820
Additions	137
Write Offs	82
Reductions	24
Closing Balances	851

g. Movement of Specific & General NPA Provisions:
(Rs in Cr)

Particulars	As on June 30, 2019	
	Specific Provisions	General Provisions
Opening Balances	592	354
Add: Provisions made during the period	118	24
Less : Transfer to Counter cyclical Provisional Buffer	-	-
Less : Write offs	82	
Less : Write Back of excess provision	9	
Closing Balances	619	378

Specific Provisions represents provisions for NPAs.
General Provisions represents provisions for Standard Advances.

h. Geography based position of NPAs, Specific provisions and General provisions:
(Rs in Cr)

Particulars	As on June 30, 2019	
	Domestic	Overseas
Gross NPA	851	-
Provision for NPA	619	-

i. Position of Non-Performing Investments (NPI) as on June 30, 2019:
(Rs in Cr)

Particulars	As on June 30, 2019
Amount of Non-performing Investments (NPI)	Nil
Amount of provisions held for Non-performing Investments	Nil

j. Movement of provisions for depreciation on investments as on June 30, 2019.
(Rs in Cr)

Particulars	As on June 30, 2019
Opening Balance	9
Provisions made during the period	-
Write offs / Write Back of excess provisions	(9)
Closing Balance	-

DF - 4: Credit Risk- Disclosures for Portfolios Subject to Standardized Approach
Qualitative Disclosure

In line with RBI guidelines, the Bank has employed Standardized Approach under Basel III capital regulations for computing risk-weighted assets of its credit portfolio.

As per regulations, the Bank is using issuer ratings, short-term ratings, long-term instrument ratings and /or bank facility ratings issued by the specified accredited External Credit Rating Agencies (ECRA) and published in public domain in order to assign credit risk weights to its counterparties.

The Bank is using ratings issued by only those External Credit Rating Agencies (ECRA) which have been accredited for the purpose of risk weighting the banks' claims for capital adequacy purposes by the Reserve Bank of India. These ECRA's are CARE Ratings, CRISIL, India Ratings (FITCH India), ICRA, Brickwork Ratings, SMERA and INFOMERICS Valuation and Rating Pvt. Ltd. (INFOMERICS). Ratings issued by either of these ECRA's are used, however, in case an exposure is rated by more than one ECRA, the lower of the two ratings is considered.

Quantitative Disclosure

(Rs in Cr)	
Category	As on June 30, 2019
Below 100% Risk Weight	42,129.87
100% Risk Weight	1,626.20
More than 100% Risk Weight	1,130.17

DF 5: Credit Risk Mitigation- Disclosures for Standardized Approaches

Qualitative Disclosure

As per the Credit Policy and Credit Risk Management Policy of the Bandhan Bank, all credit proposals of over Rs. one lakh (excluding Micro Loan & Personal Loan) is subject to internal rating (based on score card model as well as Internal Rating model as per the quantum and nature of the exposure) process to support credit approvals and decision making as well as to enhance risk management capabilities for portfolio management and pricing.

Credit scorecards are mathematical models which attempt to provide a quantitative estimate of the probability that a customer will display a defined behavior (e.g. loan

default, bankruptcy or a lower level of delinquency) with respect to their current or proposed credit position with a lender in case of small value loans. Scorecards are built and optimized to evaluate the credit file of a homogeneous population. Main Objective of the score card rating model is to

- Identify credit-worthy customers
- Decide whether to extend credit, and how much credit to extend.
- Forecast the future behavior of a new credit applicant
- Predict the future payment behavior of existing debtors

Scoring is a two or three level process (approval wise) consisting of an analyst at the branch / analyst of the credit processing team submitting the model inputs and generating the score which subsequently gets approved by the respective sanctioning authority. For exposures beyond a certain threshold, the credit rating score gets approved by the Credit Risk Management Department before sanction of the credit appraisal.

Scoring is carried out broadly on the following:

- Financial Risk (FR Risk).
- Business & Industry Risk (B & I Risk).
- Promoter Risk / Management Risk (MR Risk).

As per the best industry practice and to maintain prudent credit risk management principle, various internal rating grades have been devised as per the score obtained by the borrower. Rating grade signifies the creditworthiness of the borrower. Higher the rating, higher the creditworthiness.

The sanction of credit proposals is in accordance with the delegation structure approved by the Board of Directors. Beyond a certain threshold of individual loan proposal, Committee based sanctioning approach is adopted. There are various Head Office Level Committees comprise of senior officials of the Bank who sanctions the credit proposals. Risk vetting is compulsory for all proposals above a certain threshold.

Definitions of non-performing assets:

The Bank classifies its advances into performing and non-performing advances in accordance with the extant RBI guidelines.

The non-performing asset (NPA) is a loan or an advance where;

- Interest and/ or installment of principal remains overdue for more than 90 days for a term loan,
- The account remains 'out of order' in respect of an Overdraft/Cash Credit (OD/CC). 'Out of order' means if the account outstanding balance remains continuously in excess of the sanctioned limit/ drawing power. In cases where the outstanding balance in the principal operating account is less than the sanctioned limit/ drawing power, but there are no credits continuously for 90 days as on the date of Balance Sheet or credits are not enough to cover the interest debited during the same period, these accounts are treated as 'out of order'.
- The bill remains overdue for a period of more than 90 days in the case of bills purchased and discounted.

NPAs are further classified into sub-standard, doubtful and loss assets based on the criteria stipulated by RBI. A substandard asset is one, which has remained as NPA for a period less than or equal to 12 months. An asset is classified as doubtful if it has remained in the sub-standard category for more than 12 months. A loss asset is one where loss has been identified by the Bank or by the internal / external auditors or the RBI inspection but the amount has not been written off fully.

Quantitative Disclosures
Exposure covered by Credit Mitigants

Particulars	Amount (In Rs. Cr)
Total exposure covered by eligible financial collateral	424.48
Total exposure covered by guarantees	-*

*No exposure is covered by sovereign guarantee.

DF-6: Securitization Exposures: Disclosure for Standardized Approach

As on June 30, 2019, the Bank doesn't have any Securitization Exposures.

DF-7: Market Risk in Trading Book*Qualitative Disclosure*

The Bank for International Settlements defines market risk as “the risk that the value of ‘on’ and ‘off’ balance sheet positions will be adversely affected by movements in market interest rate, currency exchange rates, equity and commodity prices.” This definition is adopted by the Bank for the purposes of identifying and managing the risk. Market risk has the following components:

- **Interest Rate Risk:** The risk that changes in market interest rates may adversely affect the Bank's financial condition. While the immediate impact is on the Net Interest Income (NII) and also the value of investments, the long term variations in interest rates would also impact the Bank's net worth.
- **Equity Risk:** The risk that changes in the equity prices of various stocks may diminish the value of equity portfolio held by the Bank (also includes investments in equity based mutual funds)
- **Exchange Rate Risk:** The risk that the Bank may suffer losses as a result of adverse exchange rate movements during a period in which it has an open position, either spot or forward, or a combination of the two, in any foreign currency.

i. Strategies & Processes

Risk identification entails ensuring all instruments that result in Market Risk both on and off the balance sheet of the Bank are identified and monitored centrally. To achieve this

objective, all new instruments/ products in which the Bank engage should be assessed. The Asset Liability Management Committee (ALCO) reviews all new instruments to evaluate whether they result in market risk. Modifications to existing instruments is reported to the ALCO to enable such evaluation.

ii. Structure and organization

The organizational structure for Market Risk Management is as follows:

- Board of Directors
- Risk Management Committee of Board (RMCB)
- Asset Liability Management Committee (ALCO)
- Chief Risk Officer (CRO)
- Head - Market Risk Department
- Market Risk Department

iii. Scope and nature of measurement systems

There are a number of methods for measuring market risks encountered in trading operations. All these require adequate information on current positions, market conditions, and instrument characteristics.

Of the various measures available, the Bank may use sensitivity indicators for market risk measurement. Different products are measured by certain parameters. At present, in the trading book, Bank only has Interest Rate Sensitive products.

Interest Rate Sensitive Products

- Macaulay Duration
- Modified Duration
- Convexity
- Basis Point Value (BPV) or PV01

iv. Processes for monitoring

The Bank fixes appropriate action triggers or stop limits for all marked to market risk taking activities. The Bank has procedure that monitors activity to ensure that they

remain within the approved limits at all times. Limits are classified into general (applicable to all portfolios) and specific portfolio related limit. For the purpose of market risk management the following minimum limits are monitored:

- Portfolio-wide Position limits
- Dealer-wise limits
- Single Deal Size Limit
- Stop-loss limits
- Value at Risk (VaR)
- Specific Limits (Interest Rate Related Instruments)
- Modified Duration Limit
- PV01 Limit (Tenor Wise and Portfolio Level)

Quantitative Disclosures

<u>Capital Requirement</u>	
	(Rs in crore)
Risk Weighted Assets for Market Risk:	
Standardised duration approach	686.71
Interest Rate Risk	625.13
Foreign exchange Risk (including Gold)	56.25
Equity Risk	5.33

DF-8: Operational Risk

Qualitative Disclosures

Operational risk, which is intrinsic to all the material products, activities, processes and systems, has emerged as an important component of the enterprise-wide risk management system. Operational Risk is defined as the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events. Operational risk may result from various internal and external factors e.g. failure to obtain proper internal authorizations, improperly documented transactions, breach of information security procedures, failure of IT and / or communication infrastructure /

equipment, non-compliance of regulatory requirements, contractual terms and corporate policies & procedures, commitment of fraud, natural disasters, inadequate training to employees etc.

i. Strategies & Processes

The Bank's strategy for operational risk management focuses on:

- Minimizing the losses to an acceptable level as per risk appetite of the Bank;
- Providing operational risk capital which is sensitive to the Bank's risk profile;
- Using results of operational risk management in day to day business operations and decision making process;
- Carrying out risk based performance measurement;
- Analyzing the impact of failures in technology / systems and develop mitigants to minimize the impact; and
- Developing plans for external shocks that will adversely impact the continuity in the Bank's operations.

ii. Structure and organization

The operational risk management governance structure is as follows:

- Board of Directors
- Risk Management Committee of Board (RMCB)
- Operational Risk Management Committee (ORMC)
- Chief Risk Officer (CRO)
- Head - Operational Risk Department
- Operational Risk Department

iii. Scope and nature of measurement systems

As per the Basel III Capital Regulations issued by RBI for banking institutions based on the Basel framework, banks need to use an approach that is risk sophisticated and commensurate to the risk profile of the institution. The Bank is currently performing risk

measurement under the Basic Indicator Approach (BIA). The Bank also computes the capital requirements for Operational Risk under the Basic Indicator Approach and over a period of time shall move to the Standardized Approach after defining the Business Lines as per New Capital Adequacy Framework.

iv. Processes for monitoring

The Bank plans to have risk mitigates like a strong internal control system, resorting to an optimal insurance cover, outsourcing of activities, BCP / DRP etc. For example, losses that might arise on account of natural disasters are insured; losses that might arise from business disruptions due to telecommunication or electrical failures are mitigated by establishing available backup facilities, loss due to internal factors, like employee fraud or product flaws, will be mitigated through strong internal auditing procedures.

DF-9: Interest Rate Risk in Banking Book

Qualitative Disclosures

Bank has identified the risks associated with the changing interest rates on its exposures in the banking book from both, a short-term and long-term perspective. This includes the impact of changes due to parallel shocks, yield curve twists, yield curve inversions, changes in the relationships of rates (basis risk) on rate sensitive assets and liabilities up to 1 year. Stress testing and scenario analysis has also been used in the analysis of interest rate risks.

The main components of the approach for identification and measurement are as under:

- a) The assessment takes into account both the earnings perspective and economic value perspective of interest rate risk.
- b) The impact on income or the economic value of equity have been calculated by applying a notional interest rate shock of 200 basis points.

- c) The methods followed in measuring the interest rate risk are:
- i. Earnings perspective: Earnings at Risk combined with Gap Analysis,
 - ii. Economic perspective: Gap analysis combined with duration gap analysis.

Quantitative Disclosures

Increase (decline) in NII with 200 bps increase (decline) in interest rates	-327.26 Cr
Decline in MVE as a percentage of Net worth with 200 bps increase in interest rates	-2.74%

DF-10: Exposures related to Counterparty Credit Risk

Counterparty Credit Risk (CCR) is the risk that the counterparty to a transaction could default before the final settlement of the transaction's cash flows. An economic loss would occur if the transactions or portfolio of transactions with the counterparty has a positive economic value at the time of default. The Counterparty Credit Risk is managed and controlled through Counterparty Credit Risk Policy and Country Risk Management Policy of the Bank.

As on June 30, 2019, Bank had outstanding forward contracts worth USD 1 million. The settlement of the contracts is guaranteed by qualified central counterparty Clearing Corporation of India Ltd (CCIL). The residual tenors of the forward contract is less than 3 months.

Quantitative Disclosures

Sl. No.	Particulars	Amount in Rs. Cr
1	Gross Positive Value of Contracts	0.04
2	Netting Benefits	-
3	Netted Credit Exposure	0.04
4	Collateral Held	-
5	Net Derivative Credit Exposure	0.04

Item	Notional Amount	Current Credit Exposure (as per CEM)
Forward Contract	6.97	0.18

LEVERAGE RATIO

The leverage ratio has been calculated using the definitions of capital and total exposure. The Bank's leverage ratio as on June 30, 2019 calculated in accordance with the RBI guidelines under consolidated framework is as follows:

Particulars	Amount in Rs. Cr
Tier I Capital	10,675.65
Exposure Measure	58,667.75
Leverage Ratio	18.20%