

ASSET AND LIABILITY MANAGEMENT POLICY

IDF FINANCIAL SERVICES PRIVATE LIMITED

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Introduction

The Asset and Liability Management (ALM) Policy for IDF FINANCIAL SERVICES PRIVATE LIMITED (hereinafter referred to as "the Company") aims to establish a clear framework for managing liquidity, interest rate, and credit risks associated with the assets and liabilities of the Company. The policy ensures the maintenance of a robust financial position, adherence to regulatory guidelines, and alignment with the strategic objectives of the Company.

This policy is in accordance with the regulatory requirements issued by the Reserve Bank of India (RBI) and best practices in the microfinance industry.

Objective of the Policy

The primary objectives of the ALM policy are as follows:

- **Liquidity Management:** To ensure that the Company has adequate liquidity to meet its financial obligations in a timely manner.
 - **Interest Rate Risk Management:** To monitor and manage risks arising from fluctuations in interest rates that could impact the Company's financial position.
 - **Operational Risk Management:** To ensure the Company's assets and liabilities are managed effectively in line with its business strategy and regulatory requirements.
 - **Compliance:** To ensure adherence to the RBI's guidelines and the Company's internal limits.
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Scope

This ALM Policy applies to all aspects of asset and liability management within the Company, including:

- **Assets:** Loans provided to microfinance clients, investments, and other financial instruments.
 - **Liabilities:** Borrowings, deposits (if applicable), and equity capital.
 - **Capital Adequacy:** Ensuring the Company maintains an adequate level of capital to absorb shocks.
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Governance and Organizational Structure

- **Board of Directors:** The Board of Directors is responsible for approving the ALM policy, ensuring it is consistent with the Company's risk appetite, and reviewing its implementation.

- **Asset and Liability Committee (ALCO):** ALCO will be responsible for monitoring and reviewing the ALM policy's effectiveness, liquidity management, risk identification, and interest rate risk management.

- **Composition of ALCO:** Senior management members including the Head Finance, Head Risk Management and Managing Director and others as designated by the Board.
- **Frequency of Meetings:** ALCO will meet monthly or as needed, to review the Company's ALM status and any emerging risks.
- **Responsibilities of ALCO:** ALCO would also be responsible for ensuring adherence of liquidity risk limits set by the Board as well as deciding business strategies of COMPANY in line with the overall budget and risk management policy and shall review/decide the following:

The role of the ALCO with respect to liquidity risk shall also include, *inter alia*, decision on desired maturity profile and mix of incremental assets and liabilities, sale of assets as a source of funding, the structure, responsibilities, and controls for managing liquidity risk, and overseeing the liquidity positions of all branches.

- Review of Liquidity Mismatches.
- Review of Interest-Rate Sensitivity position.
- Review of Resource Raising and Deployment vis-a-vis Cost of borrowings / Yields on advances.
- Review the product mix and product pricing.
- Strategies for deployment of surplus funds.
- Concentration of funding.
- Availability of unencumbered assets.
- Review movements in book to equity ratio, Price to Book value, market price etc,
- Review coupon at which long term and short term debts are raised vis a vis the peers.
- Review of any other directions from RBI relating to ALCO functions

Risk Management Team: The Risk Management Team will support ALCO by identifying, assessing, and mitigating risks related to assets and liabilities.

The following areas of liquidity risks (Illustrative) should be deliberated by ALCO:

- Compliance to Liquidity risk tolerance levels
- Liquidity cost, benefits, and risks in internal pricing
- Off balance sheet exposures and contingent liabilities
- Funding and capital planning
- Collateral position management
- Profit planning and growth projection

Liquidity Management

Objective: To maintain sufficient liquidity to meet the Company's financial obligations as they come due, without disruption to operations.

- **Liquidity Risk Framework:** The Company shall maintain a minimum level of liquid assets, such as cash, cash equivalents, or short-term investments, sufficient to meet its short-term liquidity needs.
- **Liquidity Gap Analysis:** The Company will conduct periodic liquidity gap analysis to assess mismatches between assets and liabilities across various maturity buckets (e.g., daily, weekly, monthly).
- **Liquidity Ratios:** The Company will maintain liquidity ratios in line with regulatory requirements and internal limits. These ratios will be reviewed regularly by ALCO.
- **Contingency Funding Plan:** A plan will be established to handle liquidity stress scenarios, including options for raising additional funds in the event of a liquidity shortfall.
- **Maturity Profiling:** Measuring and managing liquidity are vital for effective operation of COMPANY. By ensuring company's ability to meet its liabilities as they become due, liquidity management can reduce the probability of developing an adverse situation. Liquidity management involves measuring liquidity position on ongoing basis and also examine how liquidity requirements are likely to evolve under different assumptions. For measuring and managing net funding requirements, the use of a maturity ladder and calculation of cumulative surplus or deficit of funds at selected maturity bucket may be adopted as a standard tool, in line with RBI guidelines.
- **Time Buckets:** The maturity profile should be used for measuring the future cash flows of the company in different time buckets. The time buckets shall be distributed as under:
 - i. 1 day to 7 days
 - ii. 8 days to 14 days
 - iii. 15 days to 30/31 days (One month)
 - iv. Over one month and up to 2 months
 - v. Over two months and up to 3 months
 - vi. Over 3 months and up to 6 months
 - vii. Over 6 months and up to 1 year
 - viii. Over 1 year and up to 3 years
 - ix. Over 3 years and up to 5 years
 - x. Over 5 years

4.1.2 Maturity Profiling (Time buckets) for Cash Flows Under Investments: As COMPANY does not hold public deposits, all the investment securities would fall in the category of 'non-mandatory securities'. All non-mandatory securities may be kept in buckets of future time frame for the purpose of determining their cash flows based on maturity of such security and intention of holding such security till the time of such maturity.

The listed non-mandatory securities shall be placed in any of the "1 day to 7 days, 8 days to 14 days, 15 days to 30/31 days (One month)", "Over one month and up to 2 months" and "Over two months and up to 3 months" buckets depending upon the defeasance period proposed by NBFCs. (As these liquid securities are purchased to

meet maturing borrowing obligations defeasance period will not normally exceed one month.)

The unlisted non-mandatory securities (e.g.; equity shares, securities without a fixed term of maturity etc.) shall be placed in the "Over 5 years" buckets, whereas unlisted non-mandatory securities having a fixed term of maturity may be placed in the relevant time bucket as per residual maturity. Unlisted securities may be valued as per Prudential Norms Directions.

4.2 Focus to Cash Flow Mismatches: Within each time bucket, there could be mismatches depending on cash inflows and outflows. While the mismatches up to one year would be relevant since these provide early warning signals of impending liquidity problems, the focus shall be on the short-term mismatches, viz., 1-30/31 days. As per regulations the net cumulative negative mismatches in the Statement of Structural Liquidity in the maturity buckets 1-7 days, 8-14 days, and 15-30 days shall not exceed 10%, 10% and 20% of the cumulative cash outflows in the respective time buckets. As a prudent liquidity management measure, COMPANY will strive to restrict the negative cumulative mismatch of maturity buckets up to one year to a maximum of 10% of the cumulative cash outflows.

4.3 Statement of Structural Liquidity: This statement shall be prepared by placing all cash inflows and outflows in the maturity ladder according to the expected timing of cash flows. A maturing liability shall be a cash outflow while a maturing asset shall be a cash inflow.

In order to monitor short-term liquidity on a dynamic basis over a time horizon spanning from 1 day to 6 months, ALCO supporting group shall present short-term liquidity profiles on the basis of realistic business projections and other commitments for planning purposes in the short-term dynamic liquidity statement to RBI and ALCO. While estimating the liquidity profile in a dynamic way, due importance may be given to the:

- i. Seasonal pattern of loans; and
- ii. Potential liquidity needs for meeting new loan demands, unavailed credit limits, devolvement of contingent liabilities, investment obligations, statutory obligations, cash collateral for the securitisation transactions, margin calls from the derivative providers etc.

Interest Rate Risk Management

Objective: To manage and minimize the impact of interest rate fluctuations on the Company's profitability and financial stability.

- **Interest Rate Sensitivity:** The Company will regularly assess the sensitivity of its balance sheet to interest rate changes, focusing on both fixed and floating rate assets and liabilities.

- **Repricing Gap Analysis:** The Company will assess the repricing gaps between assets and liabilities based on their interest rate reset periods.
 - The Company will aim to minimize large mismatches in the repricing of interest-sensitive assets and liabilities.
 - **Interest Rate Risk Limits:** The Company will establish internal limits for duration gaps and will aim to reduce exposure to adverse interest rate movements.
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Capital Adequacy and Prudential Norms

Objective: To maintain capital adequacy ratios that are in compliance with regulatory guidelines and that support the Company's growth and risk management strategies.

- **Capital Adequacy Ratio (CAR):** The Company will maintain a minimum CAR as per the RBI's requirements, ensuring it has sufficient capital buffers to absorb potential losses.
 - **Capital Buffer:** A buffer will be maintained above the regulatory minimum CAR to safeguard against unforeseen financial shocks.
 - **Prudential Lending Norms:** The Company will adhere to RBI's guidelines for the classification of loans and will maintain a conservative approach toward loan loss provisions.
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Asset and Liability Matching

Objective: To ensure that the Company's assets and liabilities are appropriately matched in terms of maturity, repayment schedules, and interest rate structures.

- **Maturity Profile:** The Company will ensure that its liabilities, including borrowings, deposits, and other payables, are matched by assets that provide the necessary cash flow to meet these obligations.
 - **Asset-Liability Matching Process:** ALCO will monitor asset-liability gaps and take corrective measures as necessary to align maturity profiles.
 - **Short-Term vs Long-Term Liabilities:** A proportion of long-term liabilities will be matched with long-term assets, while short-term liabilities will be matched with liquid or short-term assets.
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Stress Testing and Scenario Analysis

Objective: To assess the resilience of the Company's financial position under various adverse scenarios.

- **Liquidity Stress Testing:** The Company will conduct stress tests to simulate potential liquidity crises, such as large-scale client withdrawals or disruptions in the financial market.

- **Interest Rate Risk Stress Tests:** The Company will test the impact of changes in interest rates on its portfolio, profitability, and capital adequacy.
 - **Scenario Analysis:** Regular scenario analysis will be performed to understand the impact of economic downturns, regulatory changes, or adverse market conditions.
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Monitoring and Reporting

Objective: To ensure continuous monitoring of the asset-liability position and the effectiveness of risk mitigation strategies.

- **ALCO Reports:** ALCO will receive detailed reports on liquidity, interest rate risk, and asset-liability management at regular intervals.
 - **Risk Management Reports:** The Risk Management Team will provide periodic reports on emerging risks, including credit, liquidity, and operational risks.
 - **Regulatory Reporting:** The Company will comply with RBI reporting requirements regarding liquidity positions, capital adequacy, and other ALM-related disclosures.
 - **Internal Reports:** The Company will submit monthly ALM reports to the Board of Directors for review.
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Review and Revision of ALM Policy

The ALM policy will be reviewed at least annually, or more frequently if there are significant changes in the business environment, market conditions, or regulatory guidelines. The review process will be conducted by the Board of Directors, based on recommendations from ALCO.

Compliance with Regulatory Norms

The Company will adhere to all relevant regulations set by the RBI, including those specific to microfinance institutions (MFIs), such as:

- **Prudential Norms for Microfinance Institutions.**
 - **RBI Guidelines on ALM for Non-Banking Financial Companies (NBFCs).**
 - **Risk Management Frameworks and Compliance Standards.**
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Conclusion

This ALM policy is designed to ensure that the Company's assets and liabilities are managed effectively to maintain financial stability, mitigate risks, and ensure long-term growth. The Company's management and ALCO are responsible for the policy's implementation, monitoring, and review.

Approval and Implementation

This policy was approved by the Board of Directors on [Date].

Signed: