

## **Asset Liability Management Policy**

In the normal course NBFCs are exposed to various risks in view of asset-liability transformation. NBFCs are now operating in a deregulated environment and interest rate of lending can be determined by the company based on the competition in the market. NBFCs are exposed to various risks like Interest rate risk, credit risk, liquidity risk, operational risk, market risk etc. in the course of business. NBFCs need to address these risks in a structured manner by upgrading their risk management and adopting more comprehensive Asset-Liability Management (ALM) practices. ALM system act as a frame work for measuring, monitoring and managing liquidity and interest rate risk in the financial system.

The objective of this policy is to create an institutional mechanism to compute and monitor periodically the maturity pattern of the various liabilities and assets of the company and to plug in the gaps occurring in the various time buckets of the Structural liquidity and Interest Rate Sensitivity Statements.

In order to ensure due compliance with the guidelines related to Asset Liability Management System issued by Reserve Bank of India (RBI) for the NBFCs and keeping in view the future activities, the company has formulated a policy on Asset Liability Management which is enumerated as under.

Successful implementation of risk management process would require strong commitment on the part of the senior management of the company. The Asset-Liability Management Committee (ALCO) constituted by the Board would be responsible for ensuring adherence to the limits set by the Board as well as for deciding the business strategy of the company (on assets and liabilities sides) in line with the company's budget and decided risk management objectives.

The Board of Directors believes that accepting some level of risk is necessary in order to achieve desirable results. The ALCO will be responsible for managing and directing the Asset/Liability Management policies and procedures. In addition to monitoring the risk levels of the company, the ALCO will review the results of and progress in implementation of the decisions made in the previous meetings. The frequency of holding the ALCO meetings will be quarterly or as and when required. The Board of Directors, in their meetings, will oversee the implementation of the system and review its functioning periodically. The Board of Directors, if necessary, can modify the recommended policy which is in the best interest of the company.

The company has laid down broad guidelines in respect of liquidity risk management systems in the company, which form part of the Asset-Liability Management (ALM) function. The initial focus of the ALM function would be to enforce the risk management discipline i.e., managing business after assessing the risks involved.

The business issues that an ALCO would consider, *inter alia*, will include desired maturity profile, mix of the incremental assets and liabilities, prevailing interest rates offered by other peer NBFCs for the similar services/product etc.

### **Liquidity Risk Management**

The ALCO consisting of the NBFC's top management shall be responsible for ensuring adherence to the risk tolerance/ limits set by the Board as well as implementing the liquidity risk management strategy of the NBFC. The whole-time Director should head the Committee. The CFO and other senior executives also will part of the Committee. The role of the ALCO with respect to liquidity risk should 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 in the Company.

- a) ALCO would measure not only the liquidity positions of the company on an ongoing basis but also examine how liquidity requirements are likely to evolve under different assumptions. Therefore, liquidity has to be tracked through maturity or cash flow mismatches. The format of the Statement of Structural Liquidity as prescribed by Reserve Bank of India (RBI) may be used for this purpose.
- b) The maturity profile based on assets liabilities could be used for measuring the future cash flows of company in different time buckets. The time buckets, may be distributed as under:
  - i. 0 day to 07 days;
  - ii. 8 days to 14 days;
  - iii. 5 days to 30/31 Days
  - 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

c) The statement of Structural Liquidity 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 will be a cash outflow while a maturing asset will be a cash inflow. While determining the tolerance levels, the company may take into account all relevant factors based on their asset-liability base, nature of business, future strategy etc.

d) In order to enable the company to monitor their short term liquidity on a dynamic basis over a time horizon spanning from 1 day to 6 months, company will estimate its short term liquidity process on the basis of business projections and other commitments for planning purposes. An indicative format issued by RBI for estimating Short Term Dynamic Liquidity will be used for the said purpose.

### **Liquidity Risk Tolerance**

An NBFC shall have a sound process for identifying, measuring, monitoring and controlling liquidity risk. It should clearly articulate a liquidity risk tolerance that is appropriate for its business strategy and its role in the financial system. Senior management should develop the strategy to manage liquidity risk in accordance with such risk tolerance and ensure that the NBFC maintains sufficient liquidity.

Measuring and managing liquidity needs are vital for effective operation of a NBFC. By ensuring company's ability to meet its liabilities as they become due, liquidity management can reduce the probability of an adverse situation developing. The importance of liquidity transcends individual institutions, as liquidity shortfall in one institution can have repercussions on the entire system. Senior Management shall measure not only the liquidity positions of the company on an ongoing basis but also examine how liquidity requirements are likely to evolve under different assumptions. Experience shows that assets commonly considered as liquid, like Government securities and other money market instruments, could also become illiquid when the market and players are unidirectional. Therefore, liquidity has to be tracked through maturity or cash flow mismatches. 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 dates is adopted as a standard tool.

Granular maturity buckets and tolerance limits the 1-30/31 day time bucket in the Statement of Structural Liquidity is segregated into granular buckets of 1-7 days, 8-14 days, and 15-30/31 days. The net cumulative negative mismatches in the maturity buckets of 1-7 days, 8-14 days, and 15-30/31 days shall not exceed 10%, 10% and 20% of the cumulative cash outflows in the respective time buckets. 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 main focus shall be on the short-term mismatches viz., 1-30/31 days. The net cumulative negative mismatches in the maturity buckets from one month to 1 year shall not exceed 10%, and 20% of the cumulative cash outflows in the respective time buckets. We, however, are expected to monitor cumulative mismatches (running total) across all time buckets by establishing internal prudential limits with the approval of the Board / Management Committee. In case, the current asset -liability profile and the consequential structural mismatches, needs higher tolerance level, it could operate with higher limit sanctioned by the Board / Management Committee giving specific reasons on the need for such higher limit. The discretion to allow a higher tolerance level is intended for a temporary period.

The statement of Structural Liquidity may 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 enable the company to monitor its short-term liquidity on a dynamic basis over a time horizon spanning from 1 day to 6 months, company shall estimate its short-term liquidity profiles on the basis of business projections and other commitments for planning purposes.

---

| Version | Date of Board Approval | Remarks         |
|---------|------------------------|-----------------|
| 1       | 23-05-2022             | Original Policy |
| 2       | 17-01-2025             | First review    |
| 3       | 13-02-2026             | Second review   |