

Risk Management Policy

Introduction

KLM Axiva Finvest Limited ("Company") is a Middle Layer Non-Deposit taking Non-Banking Financial Company ("NBFC-ML") registered with the Reserve Bank of India ("RBI"). NBFCs are a critical component of the Indian financial system, and the Company acknowledges its responsibility to establish a robust framework for risk management, in line with the RBI guidelines and other relevant regulations.

This Policy is designed to provide a clear and structured approach to identifying, assessing, managing, and mitigating the various risks that may arise in the course of the Company's operations.

Objective and purpose

The principal objective of this Policy is to ensure the sustainable growth of the Company while maintaining financial stability. The Policy aims to promote a proactive approach to identifying, evaluating, and mitigating the risks inherent in the Company's business operations. It establishes a structured and disciplined framework for managing risk, ensuring that risk-related issues are addressed effectively and promptly.

General provisions

This Policy represents the basic standards of risk assessment to be followed by the Company. Changes to the Policy will become effective upon approval by the Board of Directors. All relevant employees must be thoroughly familiar with the Policy and must apply the principles and guidelines outlined.

Risk management

The Company recognizes that effective risk management is essential to the sustainability of its business. The management of risk is considered a business facilitator, enabling the Company to make informed decisions while balancing risk and reward. The Company will adhere to a disciplined process of risk management, taking business decisions that foster growth while maintaining an appropriate balance on the risk-reward matrix.

The following are the key risk categories identified by the Company, along with the corresponding mitigation measures:

➤ Credit risk

- A risk of loss due to failure of a borrower to meet the contractual obligation of repaying debt as per the agreed terms, is commonly known as risk of default.
- Credit risk encompasses both the loss of income resulting from inability to collect anticipated interest earnings as well as the loss of principal resulting from loan defaults.
- Risk mitigation -
 - (a) Location selection

Before establishing any branch, a detailed survey is conducted which takes into account the following factors:

 - (i) Credit culture: To see if there is a history of a good credit culture and some level of financial literacy.
 - (ii) Economic activity: To see if it is in an economically active area not overly dependent on seasonal demands or on monsoons, etc.
 - (iii) Political stability: To see if there is any history of local political influence on finance activities.
 - (b) Credit bureau check

A credit check can be done for customers who are applying for loan other than Gold loan. As part of this check, the Various parameters as specified in the loan policy are looked at to verify a customer's credit worthiness and also ensure that they are not overburdened. These will be dynamic and reviewed periodically based on RBI Regulations, directives and internal norms.
 - (c) Customer verification

The loan application is processed only after verification of customer's documents provided. Every Customer is met by the company before loan is approved to confirm the correctness of details furnished.
 - (d) Repayment history

The Company may assess the repayment history of customer including but not limited to frequency of repayments, to identify the customer behaviour in fulfilling their repayment obligations.
 - (e) Early Recognition of Financial Distress:

If a customer makes default in repayment of principal and interest proper follow up to be done. Before a loan account turns into an NPA, it is required to identify incipient stress in the account by creating a sub-asset category viz. 'Special Mention Accounts' (SMA) with the three sub-categories as given in the table:

SMA Sub-categories	Basis for classification – Principal or interest payment or any other amount wholly or partly overdue
SMA-0	Upto 30 days

SMA-1	More than 30 days and upto 60 days
SMA-2	More than 60 days and upto 90 days

Close monitoring and follow up is required from head Office/Branches in case of Loan accounts turns in SMA or NPA.

➤ **Operational risk**

- Operational risk is the risk of possible losses, resulting from inadequate or failed internal processes, people and systems or from external events.
- The risk can emanate from procedural lapses arising due to higher volumes of transactions; lapses in compliance with established norms; regulatory as well as internal guidelines; misplaced/ lost documents, collusion and fraud; breakdown or non-availability of core business applications, manipulation of accounts, unhealthy relationship with customers like spurious gold entertainment, KYC mismatch for theft Gold, Malpractices etc., pledging of land in which customer not having legal title, pledge of theft Gold.
- Skill gap and sudden attrition of key personnel in the Company, is also an operational risk, which needs to be countered and addressed by the application of appropriate HR strategies.
- Risk mitigation –
 - (a) Process compliance
 - (i) Surprise checks on branches and rate them on pre-defined compliance parameters, identify gaps in process compliance and roll out initiatives to correct loopholes.
 - (ii) Ensure that the designed processes are being followed including interaction with the customers during various stages of the relationship lifecycle.
 - (iii) Ensure all branch activities are carried out as per norms/ procedures as mentioned in the operational manual.
 - (iv) Identify any process lapses/ deviations and provide guidance to branches/ employees to ensure compliance.
 - (v) Insure all the assets to cover risk of loss due to theft, fire or natural calamities.
 - (vi) The branches are rated on various pre-defined criteria for its adherence to the processes by the Internal Audit Team. Based on their assessment and performance further actions for improvement are taken.
 - (vii) Training of employees is conducted so as to avoid process violations and ensure strict compliance.
 - (viii) Verification of employee's credentials at the time of onboarding.

(b) Document storage and retrieval

- (i) The Company recognizes the need for proper storage of documents as also their retrieval for audit and statutory requirements.
- (ii) Physical storage: The Company shall maintain an established record of all the physical loan documents and shall store them in the branch or Document Room as per the nature of loan. Gold Loan documents can store in the branch itself.
- (iii) Scanned copies: The Company can store scanned copies of the loan documents for easy retrieval especially for audit purposes where physical documents are not required.

(c) Non-compliance reporting

- (i) The Company encourages all its employees to report any non-compliance of stated processes or policies without fear.
- (ii) All issues reported shall be categorized for nature and severity as financial or non-financial; major or minor; procedural lapse or gross violation; and breach in process or disciplinary issue.

(d) Internal audits

- (i) The key objective of internal audit department is to cross check the functions and various internal controls existing in the Company, the standards viz. RBI directions, credit policies, KYC aspects etc.
- (ii) Deviations will be reported for correction in a timely manner. All significant audit observations of internal audits and follow-up actions are presented to the management.

➤ **Liquidity risk**

- Liquidity risk is the possibility of negative effects on the interests of stakeholders resulting from the inability to meet current obligations in a timely and cost-efficient manner.
- Liquidity risk arises largely due to maturity mismatch associated with assets and liabilities of the company. Liquidity risk stems from the inability of the company to fund increase in assets, manage unplanned changes in funding sources and meet financial commitments when required.
- Due to the high reliance on external sources of funds, the Company is exposed to various funding and liquidity risks.

- Concentration of a single source of funds exposes the Company to an inability to raise funds in a planned and timely manner and resort to high cost emergency sources of funds. Further, concentration of funding sources can also result in a skewed maturity profile of liabilities and resultant asset-liability mismatch.
- A high degree of leverage can severely impact the liquidity profile of the Company and lead to default in meeting its liabilities.
- Risk mitigation –
 - (a) Short term liquidity forecasts to identify gaps and thereby take immediate corrective actions to bridge the same.
 - (b) The exposure profile to the lenders is regularly updated to ensure that skewness does not creep in, in respect of the sources of external funds.
 - (c) With the major borrowings of the Company in the form of long tenor NCDs, Subordinated Debts, etc the Company adequately plans its business to meet its repayment obligations in the event of adverse impact on business.
 - (d) The Company is exposed to perception risk because of inherent industry characteristics. At the risk of negative carry on its funds, it is prudent to maintain some amount of excess liquidity. This enables Company to meet its repayment obligations as well give time to take necessary corrective actions to ensure an adequate funding pipeline.
 - (e) The Company targets adequate leverage and healthy levels of capital adequacy to safeguard itself against the impact of adverse market conditions. It also affords reasonable time to tie-up timely equity infusion.

➤ **Portfolio concentration risk**

- This is the risk to Company due to a very high credit exposure to a particular business segment, industry, geography, location, etc.
- Risk mitigation –
 - (a) The Company intends to maintain a diversified exposure in lending to customers across various states to mitigate the risks that could arise due to political or other factors within a particular state.
 - (b) With this in mind, the Company has steadily diversified business activities across multiple business segments like Gold Loan, Micro Finance and MSME segment.
 - (c) Company expanded its presence to 6 (six) States and is planning to extend its business portfolio to other States as well to avoid portfolio concentration in a single geographical area/ state. The Company follows district wise allocation of loan portfolio without any religious or community barriers.

➤ Compliance risk

- The Company is present in an industry where the Company has to ensure compliance with regulatory and statutory requirements. Non-compliance can result in stringent actions and penalties from the regulator and/ or statutory authorities and which also poses a risk to the Company reputation.
- These risks can take the form of non-compliance with RBI regulations, Income Tax Act, Companies Act, SEBI Regulations, Labor Laws and other applicable statutory regulations, non-compliance with covenants laid down by lenders etc.
- Risk mitigation – The Company regularly monitors and reviews shortfalls in compliance system and implements measures to rectify variations, if any.

➤ Reputation risk

- It is the risk to earnings and capital arising from adverse perception of the image of the Company, on the part of customers, counterparties, shareholders, investors, other stakeholders and regulators.
- It refers to the potential adverse effects, which can arise from the Company's reputation getting tarnished due to factors such as unethical practices, political activism, regulatory actions, customer dissatisfaction and complaints leading to negative publicity.
- Risk mitigation –
 - (a) Strict adherence to Fair Practices Code: All employees are trained and instructed to follow fair practices in all their dealings.
 - (b) Grievance redressal mechanism: The Company has a defined grievance redressal mechanism in place and the same is communicated to all customers.
 - (c) Customers connect: The Company pro-actively reaches out to its customers to ensure service quality and adherence to Company policies/ processes by the field employees.
 - (d) Delinquency management: The Company does not resort to any coercive recovery practices and ensures delinquency management including restructuring of loans where necessary.

➤ Interest rate risk

- Interest rate risk is the risk of financial loss from changes in regulatory changes and market interest rates.
- The greatest interest rate risk occurs when the cost of funds goes up faster than the Company can or is willing to adjust its lending rates.

- Risk mitigation –
 - (a) Maintain a financial model that reflects the investment and loan portfolio so as to test the Company's sensitivity to an increase or decrease in interest rates. Company's sensitivity to changes in interest rates affects short and long term profitability.
 - (b) Asset and liability management functions to cost-effectively manage borrowed funds and the investment portfolio.

➤ **Governance risk**

- This risk is associated with inadequate governance or a poor governance structure with an organization.
- As the Company face the challenges of management succession and the need to recruit managers that can balance social and commercial objectives, the role of Directors becomes more important to ensure the Company's continuity and focus.
- Risk mitigation –
 - (a) The Board of Directors shall clearly communicate performance expectations and lines of accountability.
 - (b) Proper direction and accountability from Board of directors & Risk Management Committee, to oversee effective governance mechanisms and strategic decisions of the company.

➤ **External business environment risk**

- External business environment risk refers to the inherent risks of the Company's business activity and the external business environment. The Company's business is directly affected by external business environment such as competition, disasters, customer satisfaction etc. The Company needs to check the validity of their assumptions against reality on a periodic basis, so as to respond accordingly.
- While external business risks are out of Company's direct control, Company can still anticipate them and prepare for their impact.
- Risk mitigation –
 - (a) Integrate an effective system of risk management into the Company's business culture and operations. An effective risk management system to encourage Directors and senior managers to ask whether they are prepared for certain possible internal and external situations and whether they have built in sufficient cushion for unexpected events.

- (b) Reduce vulnerability to external risks by systematically analyzing preparedness for potential events.

➤ **Transaction risk**

- It arises on a daily basis in the Company as transactions are processed and is particularly high as the Company handle high volume of small transactions daily. As the Company make many small, short-term loans, the degree of cross-checking is not cost-effective, so there are more opportunities for error and fraud.
- Inconsistencies between the loan management system data and accounting system data, inadequate loan tracking information, disbursement and payment received information.
- Risk mitigation –
 - (a) The Company has implemented simple, standardized and consistent procedures for transactions throughout the branches. Effective internal controls are incorporated into daily procedures to reduce the chance of human error and fraud at the branch level.
 - (b) Regular MIS reporting, monitoring, rectification and minimizing the number of times data has to be manually entered, reduces the chance and frequency of human error. MIS reflect loan tracking, e.g., disbursements, payments received, current status of outstanding balances etc.
 - (c) MIS collect data and transforms it into the information which can ensure decision making.

➤ **Human Resource risk**

- Human resource risk in the Company arises due employee turnover, replacements, training, skill, etc. Shortage of critical skills within the Company's workforce, compliance/regulatory issues, succession planning/ leadership, gap between current talent capabilities and business goals also accounts for human resource risk in the Company.
- Risk mitigation –
 - (a) Ensuring that the right person is assigned to the right job and that they grow and contribute towards Company's excellence.
 - (b) Company properly analyses and implements methods for recruitment of personnel at various levels in the branches and head office.
 - (c) Company has proper appraisal systems with the participation of the employee, consistent with job content, peer comparison and individual performance for revision of compensation on a periodical basis which is followed regularly.

- (d) A sense of belonging and commitment is inculcated in the employees and also effectively train them in spheres other than their own specialization. Activities relating to the welfare of employees are undertaken.
- (e) Employees are encouraged to give suggestions and discuss any problems with superiors. Efforts are made to keep cordial relations with employees at all level.
- (f) Job profiles are specified, police verification and house verification of employees are conducted, and recruitment of employees is done from various communities.

Risk assessment of borrowers

It is generally recognized that certain borrowers may be of a higher or lower risk category depending on the customer's background, our references, borrowers net worth and the ability to refund and pay interest etc. As such, each customer's due diligence measures on a risk sensitive basis which shall be reviewed periodically. The basic principle enshrined in this approach is that the concerned persons should adopt an enhanced customer due diligence process for higher risk customers. Conversely, a simplified customer due diligence process may be adopted for lower risk of categories of customers. In line with risk based approach, the type and amount of information and documents shall vary depending on the risk category of a particular borrower and should be collected from the client. The customers can be classified as low, medium or high based on the risk assessment of customers.

Obligations of the Principal Officer

The Principal Officer is required to carry out risk assessment to identify, assess and take effective measures to mitigate its money laundering and financing risk with respect to such borrower or geographical areas, nature and volume of transaction, repayments by borrowers etc. The risk assessment shall also take into account any specific information provided or circulated by Government of India and RBI from time to time. The risk assessment carried out shall consider all the relevant risk factors before determining the level of overall risk and the appropriate risk level and type of mitigation to be applied. This assessment shall be documented, updated regularly and made available to competent authorities and self-regulating bodies as and when required. In case of change in perception, the risk assessment should be again done to ascertain whether it is prudent to continue with the exposure with such borrower or not. In case it is felt that the funds are not safe, the funds should be recalled immediately without delay.

The Principal Officer is also required ensure compliance with the Prevention of Money Laundering Act, 2002 and rules and regulations made thereunder.

Stress Testing

Stress testing is integral to the Company's governance and liquidity risk management framework. The Company conducts stress tests on asset-liability matching and other key products to evaluate its resilience under various hypothetical scenarios. These stress tests are performed at regular intervals and are a critical component of risk management.

1. Stress testing helps gauge investments risk and the adequacy of assets as well as to help evaluate internal processes and controls.
2. Stress test can use historical, hypothetical or simulated scenarios.
3. NBFC to carry out various stress test scenarios and report on their internal procedures for managing capital and risk.

The Company should conduct the following stress tests starting on a going basis at half yearly interval.

1. Asset and liability matching stress test
2. Stress test of all assets and liability products.

Audit review and policy renewal

The effectiveness of the risk management system is periodically evaluated through internal audits. Based on audit findings, the Policy may be revised and updated, subject to the approval of the Board of Directors.

Review

The Board of Directors or the Risk Management Committee shall oversee the implementation and review of this Risk Management Policy. The Policy shall be reviewed periodically to ensure its relevance and effectiveness in addressing emerging risks.

Revised by the Board of Directors on March 18, 2025.