Edel Finance Company Limited

Risk Management Policy

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Preamble

The objective of this Risk Management Policy is to put in place a Risk Management framework for **Edel Finance Company Limited (the Company)**. The risks can broadly be classified into following broad categories:

1. Credit Risk
2. Operational Risk
3. Market Risk.
4. Liquidity Risk

This document provides the basic framework on how each of the above mentioned risks will be managed and monitored.

The Group Risk Management Committee (GRMC) to meet on quarterly basis to review and monitor the risks. The position of all perceived risks is periodically put up to the GRMC which critically evaluates the same and provides operational and policy guidance which paves the way for an effective risk management so as to safe guard the interest of the Company.

Terms of Reference

The terms of reference of the GRMC shall be as may be provided by the Board from time to time.

Roles and responsibilities of GRMC

GRMC is responsible to ensure that all the risks associated with the functioning of the Company are identified, controlled and mitigated and shall also be responsible for laying down procedures regarding managing and mitigating the risk through Integrated Risk Management Systems, Strategies and Mechanisms.

The GRMC will deal with issues relating to credit policies and procedures and manage the credit risk, operational risk, management of policies and process. The GRMC will also be responsible for identifying, measuring and monitoring various risks faced by the Company, assist in developing the Policies and verifying the Models that are used for risk measurement from time to time.

Credit Risk

Credit Risk is the potential that borrower/counterparty within Group fails to meet the obligations on agreed terms. Credit risk involves inability or unwillingness of a customer to meet their commitments. Credit risk is managed using set of credit norms and policies. There are defined roles and responsibilities for originators and approvers. All credit exposure limits are approved within a defined credit approval authority. Credit risk is inherent to the business of lending funds the objective of credit risk management is to minimize the risk and maximize organization's risk adjusted rate of return by assuming and maintaining credit exposure within the acceptable parameters.

Credit risk consists of primarily two components, viz individual transaction risk which is the Probability of Default of a particular Obligor and Portfolio Risk which is the risk to due portfolio due to concentration and external factors like real estate prices etc.

The credit policies would be comprehensive in nature and should detail the underwriting criterion based on various Group customers keeping in mind the organisational risk appetite as well as the prevailing regulatory framework. The portfolio performance and revision of policies shall be periodically reviewed.

Any deviation to the credit risk policy will be reviewed and monitored from time to time as part of the portfolio review.

The Credit Risk Policy also lay down the guidelines for managing the Collateral Risk.

Operational Risk

Operational Risk is defined as the risk of loss arising from inadequacy or omission of laid down internal processes and procedures.

Managing operational risk is given highest importance and at the core of all its process and operations. All processes, systems and policies are integrated with risk management procedures.

With a strong positive bias towards having strong risk management, the risks are carefully evaluated and divided as below with mitigating control aspects. These risks are managed by allocating to various functional units supported by workflow model and robust self-assessment and review mechanism.

Risk Type	Risk Control Framework
Financial Risk - Account reconciliations - Errors and omissions	• Daily proofing of accounts • Bank Reconciliation • Oversight by Group Financial control • Internal and statutory audits • Frequent financial reviews by Seniors
System failures	• Regular data back ups • Strong and robust IT infrastructure
Fraud Risk	• Strong MIS and review mechanism • Maker checker based banking transactions • Dual signatory based cheque issuance • Signing limits on cheques

Vendor Risk	• Legally vetted individual contracts with each vendor • Multiple vendors for mitigating dependency risk • Independent and in-house payment computation with approvals • Regular performance monitoring and vendor evaluation • Yearly renewal based on performance

CFO/CRO would be actively involved and participate in the risk evaluation and understanding of root cause analysis to mitigate risk and prevent errors.

Market Risk

The risk of decrease value of portfolio (stock prices/interest rates/foreign exchange rate/real estate etc.) due to change in the value of market risk factors. The Company faces the usual market risks on the liabilities as well as assets side. The risk framework ensures that the risks are monitored and necessary timely action is taken.

Additionally, the asset liability mismatch and collateral margins are regularly assessed, where required. Liquidity requirements are closely monitored and necessary care is taken to maintain sufficient liquidity cushion for maturing liabilities and for any unforeseen requirements. The Company to ensure diversification in source of borrowing to reduce dependence on a single source; also to pro-actively modify its liabilities profile in sync with the changing assets profile to ensure that it does not carry any material asset liability mismatch.

The Asset Liability Management Policy encompasses the strategic management of the balance sheet aimed at achieving sustained growth, profitability and solvency. It involves a multiplicity of management activities and responsibilities, including the formulation of long- term strategic goals and objectives and the management of various risks including liquidity risk, interest rate risk and market risk.

The assets and liabilities shall be managed in a way to reduce the mismatch between the two arising as a result of the differences in the borrowing & lending tenors. The purpose also would be to protect the institution from any negative financial consequences arising from changes in interest rates. These objectives shall be pursued within the framework of written credit, capital, and investment policies.

Liquidity Risk Management framework

This framework aims to ensure that the Company maintains sufficient liquidity to meet its obligations as they fall due, both under normal and stressed conditions, without incurring unacceptable losses. The liquidity risk emanates from the possible mismatches due to differences in maturity and repayment profile of assets and liabilities. The Company will continue to get support from the parent company in the form of equity infusion and the necessary support to repay its dues on timely basis.

- **Liquidity Risk Strategy**

The Company shall maintain:

- **Adequate liquidity buffer** through high-quality liquid assets (HQLA): The Company should maintain a minimum of 10% of total liability cover for 30 days of stress cash flow in HQLA.
- HQLA for the above purpose shall mean cash and cash-equivalents, government securities and callable loans given to group companies.
- **Diversified funding sources**
- **Sound liquidity risk measurement** and monitoring tools
- **Strong governance** over inter-company funding and dividend distributions

- **Measurement and Monitoring Tools**

Maturity Profiling

- All cash inflows and outflows are categorized into 1–7 days, 8–14 days, 15–30 days, 1–2 months, 2–3 months, 3–6 months, 6–12 months, and beyond 1 year buckets. The net cumulative negative mismatches in the Asset Liability Statement 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 maturity buckets. Further, the mismatch shall not exceed 15% of the cumulative cash outflows in the maturity buckets beyond 30 dys and upto 1 year.
- Liquidity Gap to be monitored daily/weekly by Treasury and reported monthly to ALCO.

- **Stress testing framework**

- **Objective**

  To assess the impact of adverse but plausible events on the Company's liquidity position, ensuring the entity can withstand shocks and meet obligations.

  The Company shall use stress testing framework to:

- Assist the Board / RMC / Senior Management in risk identification and control, contemplating other risk management tools, improving capital and liquidity planning and facilitate in business decision-making.
- Alert the entity's management against adverse unexpected outcomes related to its material risks and provide an indication for additional capital that might be needed to absorb losses; should severe shocks occur.
- Seek to provide forward-looking assessments to its risks and facilitate monitoring.
- Assess the ability to withstand stressed situations resulting from unexpected losses in terms of profitability, liquidity, and capital adequacy.
- Facilitate the development of risk mitigation or contingency plans across a range of stressed conditions.

Stress testing framework is designed at par with the nature and scale of business. The Company shall focus on establishing a robust stress testing framework and ensure coverage across all material risk dimensions.

- **Frequency**
  - Conducted quarterly
  - Reviewed by ALCO and GRMC
  - Reporting to Board on a quarterly basis

- **Stress Test Scenarios**

  Stress scenarios, based on the severity of change in the risk drivers, are classified as having baseline, medium or severe impact. Liquidity risk stress testing to be carried out by stressing the cash inflows and cash outflows upto 1 year maturity buckets by below given percentages in each scenario.

Particulars	Baseline	Medium	Severe
Stressed Outflows	103%	105%	110%
Stressed Inflows	97%	95%	90%
Total Stress % (Inflow +Outflow)	6%	10%	20%

- **Stress test results and reporting**

  Summary of results (Baseline, Medium and Severe) to be reported to Board, ALCO and GRMC on a quarterly basis

Further, key vulnerabilities and mitigating actions to be taken into consideration in the stress test results.

- **Group leverage**

  The Group Risk Management Committee (GRMC) is responsible for articulating, monitoring and reporting on the group's leverage, ensuring that the leverage profile remains consistent with the group's overall risk appetite and regulatory expectations.

  We recognise that leverage (the ratio of borrowings to equity) is a key metric of risk that must be managed proactively and in line with our capital strength, liquidity and business model. In this regard, below would be the leverage limits and monitoring approach.

  Leverage limits:

  EFCL shall maintain leverage below 2.3 times under normal business conditions beyond which we will not operate without explicit Board (or Risk Committee) approval.

  EFCL's key subsidiaries are expected to operate at leverage below 6 times.

  Monitoring & escalation:

  The Board (through the Group Risk Management Committee) will review leverage metrics at least quarterly. If the actual leverage approaches to defined limits, the Group will escalate to the Board, initiate stress testing and corrective action, and consider deleveraging or strengthened liquidity / capital buffers.

  Intra group Transactions

  All intra group transactions shall be subject to approval/omnibus approval of the Audit Committee of the Company

Review by Board of Directors

The Policy shall be reviewed by the Board as and when necessary or at least on a yearly basis.