TOURISM FINANCE CORPORATION OF INDIA LTD.
NEW DELHI

ASSET LIABILITY MANAGEMENT POLICY 2018-2019

1. INTRODUCTION:

TFCI, as a systemically important non-deposit taking NBFC, is operating in a fairly deregulated environment and determines its own interest rates on assets on a periodic basis. The competition in business involving both the assets and liabilities has necessitated TFCI to maintain a stable balance among spreads, profitability and long-term viability. TFCI is exposed to several risks in the course of its business such as credit risk, interest rate risk, equity/securities price risk, liquidity risk and operational risk, etc., which require comprehensive risk management system & process.

Reserve Bank of India, has, from time to time, emphasized the need to address these risks, in a structured manner by upgrading the risk management systems, practices and procedures and for adopting more comprehensive asset liability management practices. It is therefore important to have effective risk management systems that address the issues inter-alia, related to interest rate and liquidity risks. TFCI is therefore basing its business decisions on a dynamic and integrated risk management system and process, driven by corporate strategy.

Asset Liability Management (ALM) can be termed as a risk management technique designed to earn an adequate return while maintaining a comfortable surplus of assets over liabilities. It takes into consideration interest rates, earning power and degree of willingness to take on debt and hence is also known as Surplus Management. ALM, among other functions, is also concerned with risk management and provides a comprehensive as well as dynamic framework for measuring, monitoring and managing liquidity and interest rate risks of major operators in the financial system, that need to be closely integrated with TFCIs business strategy. ALM is an integral part of the financial management process of TFCI. It is concerned with strategic balance sheet management, involving risks caused by changes in the interest rates, exchange rates and the liquidity position of TFCI. It involves assessment of various types of risks and altering the asset-liability portfolio in a dynamic way in order to manage risks.

The Reserve Bank of India (RBI), vide its circular No. DNBS (PD). CC.No.15/ 02.01/2000-2001 dated June 27, 2001, issued ALM guidelines for NBFCs, updated vide RBI Circular No.RBI/DNBR/2016-17/45 Master Directors DNBR.PD008/03.10.119/2016-17 dated September 1, 2016 (updated 23.2.2018), with focus on liquidity risk and interest rate risk. Further, RBI's Circular No.RBI/DNBS/2016-17/47 Master Directors DNBS.PPD.02/66.15.001/2016-17 dated September 29, 2016 specifies current reporting mechanism under ALM system, to be submitted

by Non-Deposit Taking Systematically Important NBFCs, which envisages submission of quarterly short term dynamic liquidity statement, half yearly structural liquidity statement and half yearly interest rate sensitivity statement.

2. SCOPE OF THE POLICY

The ALM Policy of TFCI has been framed in line with the extant Risk Management and ALM practices prevailing at TFCI and the guidelines issued by RBI, from time to time for NBFCS-ND-SI. It primarily lays down guidelines in respect of interest rate and liquidity risk management system in TFCI.

The ALM process would rest on three pillars:

(A) ALM Information Systems:
- Management Information Systems
- Information availability, accuracy, adequacy and expediency

(B) ALM Organization:
- Structure and responsibilities.
- Level of senior management involvement.

(C) ALM Process:
- Risk parameters
- Risk identification, measurement & management
- Risk policies and tolerance levels.

(A) ALM Information system:

A sound information system is the key to the ALM process. ALM has to be supported by the management clearly specifying the risk policies and tolerance limit. This framework needs to be built on a sound methodology with necessary information systems as back up. Thus, collecting information/ data in a timely manner is the key to the ALM process. At TFCI, ALM data is prepared based on certain assumptions and is analysed on the basis of residual maturity and re-pricing of various assets & liabilities. TFCI is operating from single office and its entire accounting functions are being operated on fully tested accounting software. The present status of Assets & Liabilities on a given date is being obtained from the accounting software. The other information with regard to future cash outflows including proposed disbursements, proposed recovery from NPAs, repayment schedule of borrowings

and other cash flows would be obtained from concerned departments of TFCI which would be analysed on the basis of residual maturity and re-pricing of various assets and liabilities.

(B) ALM Organisation:

Successful implementation of the risk management process requires strong commitment on the part of the senior management to integrate basic operations and strategic decision making with risk management. The Board of Directors of TFCI will have the overall responsibility to implement the policy and may specify limits for capital management, interest rates and liquidity risk, acting through the ALM Process. The organisational structure for Asset-Liability Management would continue as follows:

I. Risk Management Committee of Directors (RMCD)/Audit-Committee of Directors(ACD):

RMCD would be constituted by the Board and shall oversee the implementation of the system and review its functioning periodically. The RMCD would review the ALM policy, Credit Risk Management Policy, Treasury & Investment Policy and Information Technology Policy for a financial year and would recommend the same to Board of Directors for their approval.

ACD would review the tolerance limits for liquidity/ interest rate risks and would recommend to Board of Directors for its approval from time to time. As per the directions of the Board, the ALM statements would be reported to the Audit-Committee and Risk Management Committee on quarterly basis for necessary guidance.

II. Risk Management Committee of Executives:

The Risk Management Committee of Executives (RMCE) constituted by the Board comprises of Managing Director, Executive Director and Chief Financial Officer/Chief General Manager. The RMCE shall meet on a quarterly basis or earlier as and when required to manage the risks associated with the operations. The broad responsibilities of the committee would be as under:

i) Examination of and recommending approval for risk-related policies of the Institution before these are submitted to the RMCD and Board of Directors seeking its approvals.
ii) Implementation of the approved credit-risk related policies of TFCI.
iii) Continuously monitoring and reviewing the effectiveness of the credit risk management processes established in the Institution and recommending changes/modifications, if required.

iv) Incorporation of the regulatory compliance with regard to asset liability management and credit risk in the Institutions policies and guidelines.
v) Monitoring of asset liability mis-match, credit risk on an institution–wide basis and ensuring adequate liquidity, compliance with the prudential limits and risk parameters approved by the Board and RMCD.
vi) Laying down procedures, effective control and comprehensive risk reporting framework.
vii) Creating strong MIS for reporting, monitoring and controlling risks.
viii) Monitoring of quality of the Institutions loan portfolio on a periodical basis, identifying problems and recommending measures to correct deficiencies.

III. Asset Liability Committee (ALCO):

The ALCO shall be headed by Managing Director and comprise of Executive Director and Chief Financial Officer/Chief General Manager. ALCO is responsible for implementing ALM policies and for managing the liquidity risk as well as interest-rate risks. ALCO would meet every month and review the cash flows as well as the prevailing interest rate scenario, its' likely impact on the profitability and the steps to be initiated for effectively meeting the liabilities on the due dates. ALCO would also be responsible for ensuring adherence of limits set by the Board as well as deciding business strategies of TFCI in line with the overall budget and risk management policy and shall review/decide the following:

- Review of Liquidity Mismatches
- Review of Interest-Rate Sensitivity position
- Decision on 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
- Decision on Entering into interest rate derivatives contract.

IV. ALM Support Group:

The ALM support group comprises of DGM/AGM/Manager/Asst.Manager of Credit Risk, Treasury, Resources, Credit and Accounts Department who will prepare the ALM statements apart from analysing, monitoring and reporting the ALM statements to ALCO. The group would scan the macroeconomic environment to provide key information to ALCO for taking critical decisions, if required.

(C) ALM Process:

The scope of ALM function would include the following:

- Liquidity risk management
- Interest risk management.
- Funding and capital planning

Out of the above mentioned functions, the most important functions of ALM are management of liquidity and interest rate risks. Considering the volatility of such risks as also for certain limit/parameters as per RBI norms required for preparation/submission of ALM statement, these risks are detailed below:

I. Liquidity Risk Management

a) Measuring and managing liquidity needs are vital for effective operation of TFCI. By ensuring TFCI'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. 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 stipulations.

b) In line with RBI guidelines, the following maturity profile would be used for measuring the future cash flows of TFCI in different time buckets:

i. 1 day to 30/31 days (one month)
ii. Over one month and up to 2 months
iii. Over 2 months and upto 3 months.
iv. Over 3 months and up to 6 months
v. Over 6 months and up to 1 year
vi. Over 1 year and up to 3 years
vii. Over 3 years and up to 5 years
viii. Over 5 years

c) Within each time bucket, there could be mismatches depending on cash inflows and outflows. While the mismatches up to 1 year would be relevant since these provide early warning signals of an impending liquidity problem, the main focus has to be short term mismatches i.e 1 day to30/31 days (one month). RBI has therefore advised NBFCs to monitor their cumulative mismatches across all time buckets and establish/ fix internal prudential limits for the time buckets. As per the RBI guidelines, the mismatches occurring in 1-14 days & 15–30/31 days buckets in normal course may not exceed 15% of the cash

outflows in each time bucket & the cumulative gap upto 1 year may not exceed 15% of the outflows. TFCI shall also adhere to these prudential limits and the tolerance/prudential limits for structural liquidity under different time bucket would be as follows:

Sl. No.	Time Bucket	Structural Liquidity	
		Negative Gap as % of outflow	Cumulative Negative Gap as % of outflow)
1.	1-30/31 days	15%	-
2.	1 to 2 months	15%	15%
3.	2 month to 1 year	15%	15%
4.	1 year to 5 years	30%	30%
5.	5 years onwards	40%	40%

d) The Statement of Structural Liquidity (as per the format prescribed by RBI) shall be prepared on quarterly basis by placing all cash inflows and outflows in the maturity ladder according to the expected timing of cash flows. A maturing liability will be treated as a cash outflow while a maturing asset will be a cash inflow. Likely cash inflows / outflows would be estimated based on TFCI's asset - liability profile. The bi-annual Structural Liquidity Statement shall be filed with RBI within the specified timelines.

e) In order to monitor its short-term liquidity on a dynamic basis over a time horizon spanning from 1 day to 6 months, TFCI would estimate its short-term liquidity profile on the basis of business projections and other commitments for planning purposes.

f) After studying the behavioural pattern of cash flows of TFCI, it is observed that short terms mismatches can be managed by appropriate Treasury Operations. With reference to the longer time buckets, TFCI may plan raising long term resources to reduce the negative gaps prevailing at the higher end of the time buckets.

II. Interest Rate Risk (IRR)

a) RBI has allowed NBFCs to price most of their assets and liabilities. Thus there is a need for the financial system to hedge the Interest Rate Risk. Interest rate risk is the risk where changes in market interest rates might adversely affect TFCI's financial condition and the changes in interest rates affect TFCI in a larger way. The immediate impact of changes in interest rates is on earnings (i.e. reported profits) by changing its Net Interest Income (NII). A long-term impact of changing interest rates is on Market Value of Equity (MVE) or Net Worth as the economic value of TFCI's assets, liabilities and off-balance sheet positions get

affected (re-priced) due to variation in market interest rates. The interest rate risk when viewed from these two perspectives is known as 'earnings perspective' and 'economic value perspective', respectively. The risk from the earnings perspective can be measured as changes in the Net Interest Income (NII) or Net Interest Margin (NIM).There are many analytical techniques for measurement and management of Interest Rate Risk. However, in line with RBI guidelines, to begin with, the traditional Gap analysis is considered as a suitable method to measure the Interest Rate Risk for TFCI.

b) The Gap or Mismatch risk can be measured by calculating Gaps over different time intervals as at a given date. Gap analysis measures mismatches between rate sensitive liabilities and rate sensitive assets (including off-balance sheet positions). An asset or liability is normally classified as rate sensitive if:

i) within the time interval under consideration, there is a cash flow;
ii) the interest rate resets/re-prices contractually during the interval;
iii) dependent on RBI changes in the interest rates/Bank Rate;
iv) it is contractually pre-payable or withdrawal before the stated maturities.

c) The Gap Report would be generated by grouping rate sensitive liabilities, assets and off-balance sheet positions into time buckets according to residual maturity or next re-pricing period, whichever is earlier. All investments, advances, borrowings, purchased funds, etc. that mature/re-price within a specified timeframe are interest rate sensitive. Similarly, any principal repayment of loan is also rate sensitive if it is expected to be received it within the time horizon. This includes final principal payment and interim instalments. Certain assets and liabilities receive/pay rates that vary with a reference rate. These assets and liabilities are re-priced at pre-determined intervals and are rate sensitive at the time of re-pricing. The Gaps would be identified in the following time buckets:

i. 1 day to 30/31 days (one month)
ii. Over one month and up to 2 months
iii. Over 2 months and upto 3 months.
iv. Over 3 months and up to 6 months
v. Over 6 months and up to 1 year
vi. Over 1 year and up to 3 years
vii. Over 3 years and up to 5 years
viii. Over 5 years
ix. Non-sensitive

The various items of rate sensitive assets and liabilities and off-balance sheet items would be classified as per the RBI guidelines and reporter as per the format provided by RBI. The bi-annual Interest Rate Sensitivity Statement shall be filed with RBI within the specified timelines.

d) The Gap is the difference between Rate Sensitive Assets (RSA) and Rate Sensitive Liabilities (RSL) for each time bucket. The positive Gap indicates that TFCI has more RSAs than RSLs whereas the negative Gap indicates that it has more RSLs than RLAs. The Gap reports indicate whether the institution is in a position to benefit from rising interest rates by having a positive Gap (RSA>RSL) or whether it is in a position to benefit from declining interest rates by a negative Gap (RSL>RSA). The Gap is, therefore, used as a measure of interest rate sensitivity.

e) RBI has advised NBFC's to set prudential limits on individual Gaps with the approval of the Board/Management Committee. The prudential limits shall have a relationship with the Total Assets, Earning Assets or Equity. The objective of the interest rate sensitive analysis will mainly be focused on interest rate gap for more than one year period. It is proposed to continue with the present prudential limit approved by the Board viz. such positive/negative gap should not exceed 30% of Risk Sensitive Assets (RSA). In case the gap exceeds 30% it will be hedged/reduced by restructuring of composition of fixed/floating assets/liabilities or interest rate derivatives as decided by ALCO.

(III) Funding & Capital Planning:

a) Maintaining Adequate Capital:

TFCI would ensure that the capital adequacy ratio is always above the minimum level prescribed by RBI. This would be possible by ensuring increased profitability and thus an increase in the Tier I and Tier II Capital on one hand and to ensure reduction in risk-weighted assets on the other.

b) Funding planning:

TFCI would ensure that both short and long term funds requirement for its business are made available by way of bank borrowings, commercial papers, bonds, debentures and any other financial instrument.

3. POLICY REVIEW

The Policy would ideally be reviewed at periodic intervals, preferably on an annual basis. However, the policy can be reviewed at short notice depending on the exigencies/extraordinary situations, which may emanate during the course of TFCI's business. Such extraordinary situations may include significant changes in Government/Reserve Bank of India policies, global/national macro-economic conditions, financial performance, etc. This Policy shall remain in force till the next revision is carried out and disseminated.

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