The Mahaveer Co-op. Bank Ltd.,
1157, Shree Renuka Towers,
Anantshayan Galli,
Belagavi-590002
Phone : 0831-2407120/2407121/4212236

Asset – Liability Management Policy 2025-26

This Asset-Liability Management (ALM) 2025-2026
Approved by the Board of Directors at its meeting held on 29-07-2025, vide Resolution No. 10.

1. Introduction

This Asset-Liability Management (ALM) Policy shall be read in conjunction with, and is subject to, the applicable guidelines, circulars, and notifications issued by the Reserve Bank of India (RBI), as amended from time to time. It has been prepared in compliance with these RBI directives and has been duly approved by the Board of Directors.

In recent years, the Indian financial market has seen many changes, including increasing fluctuations in interest rates. These changes have made it necessary for banks to carefully manage their assets and liabilities to maintain profitability, stable income, and long-term sustainability.

This policy provides a clear framework to measure, monitor, and manage the structure and balance between the Bank's assets and liabilities. It is designed to protect the Bank's financial health and ensure smooth functioning in a changing and competitive market environment.**This Policy shall be read in conjunction with, and is subject to, the guidelines, circulars, and notifications issued by the Reserve Bank of India (RBI), as amended from time to time.**

2. Definition

Asset-Liability Management (ALM) means managing the Bank's assets and liabilities in a balanced way to ensure **safety, liquidity, and stable earnings**.

It also includes improving the skills of bank staff in handling financial risks. All business decisions should be based on a **well-planned and ongoing risk management system** that helps the Bank respond to changing market conditions.

3. Objectives of the ALM Policy

The primary objective of the Asset-Liability Management (ALM) Policy is to ensure that the Bank maintains adequate liquidity at all times. This enables the Bank to meet its financial obligations — such as customer deposit withdrawals, loan disbursements, investment commitments, and repayment of borrowings — promptly and efficiently.

In addition to managing liquidity, the policy is designed to protect the Bank's profitability, capital adequacy, and overall financial soundness. This is achieved by measuring, monitoring, and managing key balance sheet risks, particularly interest rate risk, liquidity risk, and funding concentration risk, which can impact the Bank's long-term sustainability.

The ALM Policy serves as a strategic risk management tool to align the maturity and pricing profiles of the Bank's assets and liabilities, thereby supporting optimal resource allocation, stable earnings, and regulatory compliance.

Main Objectives:

1.Liquidity Management

- Ensure the Bank always maintains sufficient cash and liquid assets to meet short-term and long-term obligations without disruptions.
- Identify and manage potential mismatches between inflows and outflows through structured liquidity gap analysis.

2.Interest Rate Risk Management (IRRBB)

- Monitor and manage the impact of interest rate fluctuations on the Bank's Net Interest Income (NII) and Economic Value of Equity (EVE).
- Use tools like Duration Gap Analysis, Rate Sensitive Gap Reports, and Stress Testing to assess and mitigate risk.

3.Earnings Stability

- Protect and stabilize the Bank's income by minimizing exposure to market volatility and mismatches in asset-liability maturity or repricing.

4.Regulatory Compliance

- Ensure adherence to applicable guidelines, circulars, and frameworks prescribed by the Reserve Bank of India (RBI) and other regulatory bodies, including requirements related to Liquidity Coverage Ratio (LCR) and Interest Rate Risk in the Banking Book (IRRBB).

5.Systemic Safety and Soundness

- Promote the Bank's long-term solvency and financial resilience by reducing vulnerabilities in funding sources, investment exposure, and cash flow dependencies.

6.Comprehensive Risk Management Framework

- Provide a structured framework to identify, quantify, monitor, and control balance sheet-related risks, using a combination of quantitative analysis, scenario planning, and real-time risk indicators.

7.Asset-Liability Committee (ALCO) Governance

- Establish a proactive governance mechanism through the Asset-Liability Committee (ALCO), which is responsible for reviewing risk metrics, formulating strategies, and ensuring policy implementation across all functions of the Bank.

---

4. ALM Framework

The **Asset-Liability Management (ALM) Framework** provides a structured and systematic approach for managing the Bank's **liquidity and interest rate risks**. It enables informed decision-making, enhances financial stability, and ensures compliance with regulatory guidelines. The framework is built upon three key components that collectively support the Bank's ALM function.

4.1 ALM Information System

An effective Management Information System (MIS) forms the backbone of the ALM process. It provides the data and insights required for accurate assessment and strategic planning.
Key features of the ALM MIS include:

- Accuracy and Reliability: Ensures that asset and liability data is correct, up-to-date, and dependable.
- Timely and Adequate Data Flow: Facilitates the prompt availability of relevant financial data to enable proactive decision-making.
- Classification Support: Enables proper classification of assets and liabilities based on both contractual maturities and behavioral patterns, especially for products with uncertain cash flows (e.g., savings deposits or prepayable loans).

This robust information system assists the Bank in identifying and analyzing maturity mismatches, rate-sensitive gaps, and liquidity gaps, thereby improving the management of the balance sheet's interest rate sensitivity and liquidity position.

4.2 ALM Organization

The Bank is responsible for the effective implementation and oversight of the Asset-Liability Management (ALM) function, which forms a critical component of its overall risk management framework. The objective is to proactively manage liquidity risk, interest rate risk, and other related financial risks to ensure the Bank's stability and soundness.
The core responsibilities under ALM include:

- Formulating comprehensive risk management policies aligned with regulatory guidelines and internal risk appetite
- Setting prudential limits for liquidity risk, interest rate risk, and other market-related exposures
- Establishing sound internal systems for reporting, monitoring, control, and independent audit of ALM activities
- Conducting periodic assessments of the Bank's liquidity profile, interest rate sensitivity, and balance sheet structure
- Ensuring alignment between the Bank's assets and liabilities in terms of maturity, interest

rates, and currency denomination

These responsibilities are primarily carried out by the **Asset-Liability Committee (ALCO)**, which operates under the overall supervision and strategic guidance of the **Board of Directors**. The ALCO is composed of senior management personnel and is entrusted with the task of reviewing and guiding the Bank's ALM strategies, monitoring compliance with risk limits, and recommending corrective actions as necessary.

4.3 ALM Process

The Asset-Liability Management (ALM) process is a critical element of the Bank's risk management framework. It involves a systematic approach to identifying, measuring, monitoring, and managing the financial risks arising from the mismatch between assets and liabilities. The objective is to ensure the Bank maintains adequate liquidity, optimizes interest rate risk, and sustains a stable balance sheet under varying market conditions. The ALM process supports strategic decision-making by providing insights into potential vulnerabilities and helping the Bank take timely corrective actions to safeguard its financial health.

Key Steps in the ALM Process:

1. **Risk Identification**
   Identifying the sources of balance sheet risks, particularly liquidity and interest rate risks. This involves analyzing cash flow mismatches, asset-liability maturity patterns, and market conditions.
2. **Risk Measurement**
   Quantifying the level of risk using various tools and techniques such as:
   - **Gap Analysis** – To assess mismatches between rate-sensitive assets and liabilities across different time buckets
   - **Duration Analysis** – To understand the sensitivity of asset and liability values to interest rate changes
   - **Stress Testing and Scenario Analysis** – To evaluate the Bank's resilience under extreme but plausible market conditions
3. **Risk Management Strategies**
   Employing appropriate techniques to manage or mitigate risks, such as:
   - Repricing of assets/liabilities
   - Diversifying funding sources
   - Maintaining adequate high-quality liquid assets (HQLAs)

- Hedging through permissible instruments, if applicable

4. **Setting Risk Limits**
   Establishing internal risk tolerance levels and prudential limits approved by the Board/ALCO to ensure exposures remain within acceptable thresholds. These limits are subject to regular review based on changes in the Bank's profile or market conditions.
5. **Policy Formulation and Review**
   Based on ongoing risk assessments, policies governing liquidity and interest rate risk management are formulated and periodically reviewed. These policies align with regulatory requirements and reflect the Bank's strategic objectives and risk appetite.

Key Risks Managed under the ALM Framework:

- **Liquidity Risk**
  The risk of the Bank being unable to meet its financial obligations as they fall due, either because of an inability to convert assets into cash or due to insufficient access to funding sources.
- **Interest Rate Risk**
  The risk of negative impact on the Bank's net interest income (NII) or the economic value of equity (EVE) due to adverse movements in market interest rates.

5. Risk Management

Risk management is a foundational element of the Bank's Asset-Liability Management (ALM) framework. Among the spectrum of financial and operational risks, **Liquidity Risk** remains a primary focus due to its immediate impact on the Bank's ability to meet obligations, maintain customer confidence, and ensure regulatory compliance.

The Bank adopts a proactive and structured approach to risk management by identifying potential vulnerabilities, assessing their impact, setting tolerance levels, and implementing mitigation strategies. The ALCO, under the oversight of the Board, is responsible for continuously monitoring and managing liquidity and interest rate risks in accordance with approved policies.

5.1 Liquidity Risk

Liquidity Risk refers to the potential inability of the Bank to meet its financial obligations as they fall due, without incurring unacceptable losses. It can arise due to mismatches in the timing of cash inflows and outflows or disruptions in funding markets. Liquidity Risk is broadly categorized into two types:

a) Market / Product Liquidity Risk

This type of risk arises when the Bank is unable to sell specific assets or execute transactions at prevailing market prices due to limited market depth or dislocation.

- Example: Difficulty in liquidating government securities or other marketable assets during periods of financial stress or low market activity.

Mitigation Measures:

- Diversifying investments across multiple asset classes, instruments, and markets
- Setting internal exposure limits for individual products or market segments
- Ensuring adequate investment in high-quality liquid assets (HQLAs)

b) Cash Flow / Funding Liquidity Risk

This occurs when the Bank lacks sufficient cash or funding sources to meet its payment obligations—such as deposit withdrawals, loan disbursements, or maturing liabilities—on time. In extreme cases, the Bank may be forced to liquidate assets at a loss or borrow funds at unfavourable rates.

Mitigation Measures:

- Preparing and maintaining realistic and rolling cash flow forecasts across different time horizons
- Diversifying sources of funding, including retail and bulk deposits, refinance arrangements, and inter-bank borrowings
- Maintaining adequate liquidity buffers and contingency funding plans
- Regularly conducting liquidity stress testing under various scenarios

5.2 Liquidity Risk Measurement Approaches

In order to effectively assess and monitor liquidity risk, the Bank employs two primary approaches—Stock Approach and Flow Approach. Together, these provide a comprehensive view of the Bank's liquidity profile, both from a structural and dynamic perspective.

1. Stock Approach

The Stock Approach involves the use of key balance sheet ratios to evaluate the Bank's overall liquidity position. This method focuses on the structural aspects of the balance sheet and helps determine the strength and stability of funding sources relative to asset composition.

Key Ratios Monitored:

- Credit-Deposit (CD) Ratio – Indicates the proportion of deposits deployed for lending.
- Loans to Total Assets Ratio – Reflects the share of illiquid loans in the total asset base.
- Loans to Core Deposits Ratio – Measures reliance on stable, low-cost funding versus loan obligations.

These ratios are reviewed periodically by the ALCO to assess whether the Bank's balance sheet is aligned with its liquidity objectives and risk appetite.

---

2. Flow Approach

The Flow Approach focuses on the analysis of actual and projected cash inflows and outflows across defined time intervals or maturity buckets. This method helps the Bank monitor short-term liquidity and anticipate potential mismatches in the timing of cash flows.

Key Features:

- Tracks inflows and outflows in time buckets such as 1–14 days, 15–28 days, 29–90 days, etc.
- Identifies liquidity gaps and aids in real-time liquidity planning
- Supports preparation of the Structural Liquidity Statement (SLS) for regulatory and internal monitoring purposes

---

Guidelines for Managing Cash Flow Mismatches

To ensure prudent and proactive liquidity management, the Bank adheres to the following guidelines:

- Priority Monitoring: Special emphasis must be placed on short-term time buckets, particularly the 1–14 days and 15–28 days horizons, where liquidity pressure is most likely to occur.
- Mismatch Limit: The negative mismatch (where projected outflows exceed inflows) in any time bucket should not exceed 20% of the total outflows for that period.
- Structural Liquidity Statement (SLS): This statement must be prepared and updated regularly, placing all inflows and outflows in their respective maturity buckets, based on realistic assumptions.
- Horizon-Based Monitoring: The Bank must maintain and monitor a forward-looking liquidity profile over a 1–90 day horizon, incorporating anticipated business growth, seasonal variations, and known financial obligations.

---

6. Maturity Profile for Liquidity Measurement

To assess future cash flows and manage liquidity risk effectively, the Bank will adopt the following **maturity profile classification**, placing each component of assets and liabilities into relevant time bands:

A. Outflows	
Head of Account	**Classification into Time Bands**
1. Capital, Reserves & Surplus	Over 5 years
2. Demand Deposits (Savings & Current Accounts)	Volatile portion: 10% of Savings and 15% of Current Deposits – 1–14 days band; Core portion – Over 1–3 years band. Banks may use behavioural maturity based on empirical data with Board/ALCO approval.
3. Term Deposits / Tier II Deposits	Respective residual maturity bands. Retail deposits may be behaviourally bucketed; Wholesale (>₹15 lakhs) under residual maturity.
4. CDs, Borrowings, Subordinated Bonds	Respective residual maturity bands
5. Other Liabilities & Provisions	- Bills Payable: 1–14 days
	- Branch Adjustments (Net Credit): 1–14 days
	- Provisions (other than loan loss): Respective bands
	- Other Liabilities: Respective bands; non-cash items like advance guarantee fees – Over 5 years
6. Export Refinance Availed	Based on underlying residual asset maturity
B. Inflows	
Head of Account	**Classification into Time Bands**
1. Cash	1–14 days
2. Balances with RBI / SCBs / DCCBs (CRR / SLR)	Excess over CRR/SLR: 1–14 days; Statutory: Distributed per DTL maturity with 28-day lag
3. Balances with Banks	- Current Account: Non-withdrawable – Over 1–3 years; Remaining – 1–14 days
	- Other Deposits & Placements: Respective residual bands
4. Investments (Net of Provisions)	- Approved Securities: Residual maturity excluding amounts to maintain SLR

	- PSU Bonds, CPs, CDs, MF Units (Closed-ended): Respective bands
	- NPIs: Sub-standard – Over 3–5 years; Doubtful – Over 5 years
	- Equity Shares: Listed – 1–14 days (with 50% haircut); Others – Over 5 years
	- MF Units (Open-ended): 1–14 days
	- Trading Book Securities: 1–14, 15–28, 29–90 days based on defeasance period
5. Advances (Performing)	- Bills Purchased/Discounted: Residual maturity
	- CC/OD/Demand Loans: Volatile – Near term bands; Core – Over 1–3 years
	- Term Loans: Instalments under respective bands
6. NPAs (Net of Provisions)	- Sub-standard: Over 3–5 years
	- Doubtful/Loss: Over 5 years
7. Fixed Assets	Over 5 years
8. Other Assets	- Branch Adjustments (Net Debit): 1–14 days
	- Intangibles: Over 5 years
	- Leased Assets: Residual maturity
C. Contingent Items / Commitments	
Category	**Classification into Time Bands**
1. CC/OD Limits (Un-availed)	Based on behavioural analysis; to be placed in time bands within 12 months
2. Export Refinance (Un-availed)	1–14 days
3. LCs / Guarantees Devolvement	Based on historical behaviour and spread across relevant bands
4. Repos, Forex Forwards, Swaps, Rediscounted Bills	Respective residual maturity
5. Accrued Interest Payable/Receivable	Respective time bands

Notes:

- Overdue liabilities: 1–14 days
- Overdue advances/investments (<1 month): 3–6 months; if over 1 month but before NPA: 6–12 months

- Known event liabilities (e.g., CRR/SLR shortfall, capex): Respective maturity bands

---

D. Financing of Gaps

If **negative mismatches** in the 1–14 or 15–28 day buckets exceed **20%** of outflows, the Bank must indicate how the gap will be financed. Options include:

- Call/term money borrowings
- Bills rediscounting
- Repos
- Deployment of foreign currency resources (un-swapped)

<u>7. Interest Rate Risk Management</u>

With the deregulation and increasing volatility of interest rates in the financial markets, banks are exposed to Interest Rate Risk (IRR)—a key component of market risk. This risk can significantly impact both the current earnings (Net Interest Income) and the economic value of equity (balance sheet value) of the Bank.

Interest Rate Risk primarily arises due to mismatches in the timing and pricing of the Bank's assets and liabilities. The following are the main contributing factors:

- **Term Deposits**: These carry **fixed interest rates** for their entire tenure, limiting the Bank's ability to adjust outflows in response to changing market rates.
- **Advances (Loans)**: Many advances are linked to floating or periodically reset rates, which may be re-priced at intervals, leading to an asymmetric re-pricing of assets and liabilities.

Measuring Interest Rate Risk

Interest Rate Risk (IRR) can be assessed from two primary perspectives: Earnings Perspective and Economic Value Perspective. The Bank primarily adopts the Earnings Perspective, which focuses on the short-term impact of interest rate changes on the Bank's profitability.

Under this approach, the Bank evaluates the effect of interest rate fluctuations on:

- **Net Interest Income (NII)** – the difference between interest earned on assets and interest paid on liabilities
- **Net Interest Margin (NIM)** – the ratio of NII to average earning assets

Gap Analysis Methodology

The recommended and widely used tool for measuring Interest Rate Risk under the earnings perspective is the Gap Analysis. This method identifies mismatches between:

- **Rate Sensitive Assets (RSAs)** – assets that will be repriced or mature within a specific time frame
- **Rate Sensitive Liabilities (RSLs)** – liabilities that will be repriced or mature within the same time frame

The difference between RSAs and RSLs within a particular time band is called the Interest Rate Gap. A positive gap indicates that more assets than liabilities are repriced, while a negative gap shows the opposite.

All rate-sensitive components, including off-balance sheet exposures (such as interest rate derivatives, if applicable), must be included in the analysis to ensure a comprehensive view of the Bank's interest rate sensitivity.

Standard Gap Buckets for Analysis

To facilitate structured analysis, all rate-sensitive assets and liabilities are categorized into the following time bands:

1. **Up to 3 months**
2. **Over 3 months and up to 6 months**
3. **Over 6 months and up to 1 year**
4. **Over 1 year and up to 3 years**
5. **Over 3 years and up to 5 years**
6. **Over 5 years**

The cumulative gaps across these buckets help the Bank assess its exposure under various interest rate scenarios and develop appropriate risk mitigation strategies.

<u>Classification of Rate-Sensitive Items</u>

The various items of rate-sensitive assets, liabilities, and off-balance sheet items should be classified under the following heads based on their rate sensitivity and time bands:

Heads of Accounts	**Rate Sensitivity & Time Band**
Liabilities	

1. Capital, Reserves & Surplus	Non-sensitive
s	Non-sensitive
3. Savings Bank Deposits	Sensitive to the extent of the interest-bearing (core) portion; place under 'Over 3–6 Months' band. Non-interest-bearing portion is non-sensitive.
4. Term Deposits, Long-Term Deposits (Tier II), and Certificates of Deposit	Sensitive; reprice at maturity. Allocate based on residual maturity.
5. Borrowings – Fixed	Sensitive; reprice at maturity. Allocate based on residual maturity.
6. Borrowings – Floating	Sensitive; reprice on interest rate reset date. Allocate to corresponding band.
7. Borrowings – Zero Coupon	Sensitive; reprice at maturity. Allocate to maturity band.
8. Borrowings from RBI	Allocate to 'Up to 3 Months' band.
9. Refinances from Other Agencies	Fixed: Allocate as per residual maturity; Floating: Allocate to the repricing date.
10. Other Liabilities & Provisions	
i) Bills Payable	Non-sensitive
ii) Branch Adjustments	Non-sensitive
iii) Provisions	Non-sensitive
iv) Other Liabilities	Non-sensitive
11. Repos / Bills Rediscounted / Swaps	Sensitive; reprice on maturity. Allocate to maturity band.

Asset / Subcategory	Sensitivity Classification
1. Cash	Non-sensitive
2. Balances with RBI	Interest-earning portion may be shown in over 3–6 months' time band. The balance amount is non-sensitive.
3. Balances with Other Banks	—
i) Current Account	Non-sensitive
ii) Money at Call and Short Notice, Term Deposits, Long Term Deposits (Tier II), and Other Placements	Sensitive on maturity. Amounts should be distributed to respective maturity bands.

4. Investments (Performing)	—
i) Fixed Rate / Zero Coupon	Sensitive on maturity
ii) Floating Rate	Sensitive at the next repricing date
5. Shares of All-India FIs / Other Cooperatives / Eligible Mutual Funds	Sensitive; may be shown under 3 months category
6. Advances (Performing)	—
i) Bills Purchased and Discounted (including under DUPN)	Sensitive on maturity
ii) Cash Credits / Overdrafts / Loans Repayable on Demand / Term Loans	Sensitive; may be shown under 3–6 months' time band
7. NPAs (Advances &Investments) *	—
i) Sub-standard	Over 3–5 years' time band
ii) Doubtful and Loss	Over 5 years' time band
8. Fixed Assets	Non-sensitive
9. Other Assets	—
i) Inter-office Adjustments	Non-sensitive
ii) Leased Assets	Sensitive on cash flows; distributed to maturity bands as per flow dates
iii) Others	Non-sensitive
10. Reverse Repos / Swaps (Sell-Buy) / Bills Rediscounted (DUPN)	Sensitive on maturity
11. Other Products (Interest Rate)	—
i) Swaps	Sensitive; distribute under relevant maturity bands
ii) Others	To be suitably classified when introduced
* Amounts should be shown **net of provisions**, **Overdue Interest Reserve**, and **claims received from ECGC**.	

c) Market Risks

Market Risk refers to the potential for losses due to adverse movements in market variables such as interest rates, exchange rates, equity prices, and commodity prices. These fluctuations can directly impact the Bank's investment portfolio, trading activities, and overall earnings.

Market Risk can be further categorized into:

- Absolute Risk: The potential rupee loss arising from the total volatility in returns, without reference to any benchmark.
- Relative Risk: The risk of underperformance relative to a benchmark index, commonly referred to as tracking error.

Effective market risk management involves continuous monitoring of exposures, setting risk limits, conducting scenario analyses, and ensuring compliance with regulatory and internal guidelines.

---

d) Credit Risks

Credit Risk refers to the potential loss the Bank may incur if a borrower, counterparty, or obligor fails to meet their contractual financial obligations in full or in part, either on the due date or at any point during the term of the agreement. It is one of the most significant and inherent risks in banking operations, particularly in the areas of loans, advances, guarantees, investments, and inter-bank exposures.

Credit risk directly impacts the Bank's asset quality, profitability, capital adequacy, and liquidity position. If not effectively managed, it can lead to an increase in Non-Performing Assets (NPAs), provisioning requirements, and erosion of stakeholders' confidence.

Forms of Credit Risk

Credit Risk can manifest in multiple forms, including but not limited to:

- **Default Risk**
  The risk that a borrower or issuer will fail to make required payments (principal or interest) on time or at maturity. This is the most direct and observable form of credit risk.
- **Credit Migration Risk (or Downgrade Risk)**
  The risk that the creditworthiness of a borrower or security is downgraded by a recognized credit rating agency or internal credit assessment mechanism. A downgrade reduces the market value of the exposure and may increase the cost of future borrowings for both the borrower and the Bank.
- **Settlement Risk**
  The risk that one party fails to deliver the terms of a contract at the time of settlement. This risk is especially relevant in inter-bank lending, forex transactions, and derivative trades.
- **Concentration Risk**
  The risk arising from excessive exposure to a single borrower, group, sector, or geography. High concentration increases the Bank's vulnerability to correlated defaults.
- **Country and Sovereign Risk**
  The risk of loss arising from the inability or unwillingness of a foreign government or

counterparties in a particular country to fulfil their obligations due to political or economic instability.

---

e) Operational Risks

Operational Risk refers to the risk of loss resulting from inadequate or failed internal processes, people, systems, or from external events. It is inherent in all banking activities and can arise from human errors, system failures, frauds, or unforeseen disruptions.

Operational risk can manifest in various forms, including:

- **Inadequate or Ineffective Systems and Controls** – Systems that are outdated, poorly integrated, or lacking necessary safeguards
- **Management or Process Failures** – Poor decision-making, weak governance structures, or lack of oversight
- **Fraud and Human Error** – Internal or external fraudulent activities, negligence, or unintentional mistakes
- **Execution and Transaction Failures** – Errors in transaction processing, settlement failures, or data entry lapses
- **Technology and Cybersecurity Threats** – Unauthorized access, data breaches, system tampering, malware attacks, or denial-of-service incidents

---

Operational Risk Mitigation Measures

To manage and mitigate operational risk, the Bank adopts a proactive and structured approach that includes:

- **Establishing Strong Internal Controls** – Policies, procedures, maker-checker mechanisms, and internal audit processes to detect and prevent lapses
- **Clearly Defined Roles and Responsibilities** – Proper delegation of authority and accountability across departments and functions
- **System Redundancy and Backup Mechanisms** – Deployment of alternate systems, data recovery processes, and business continuity solutions
- **Regular Contingency and Disaster Recovery Planning** – Preparation for unexpected disruptions through simulation exercises and response planning
- **Staff Training and Awareness Programs** – Enhancing employee knowledge on risk awareness, compliance, and cybersecurity
- **Incident Reporting and Root Cause Analysis** – Mechanisms for prompt reporting, documentation, and review of operational failures or near-misses

Operational Risk is monitored through **Key Risk Indicators (KRIs)**, internal audits, and **Loss Event**

Databases to enable early detection and timely corrective action. The Bank's **Operational Risk Management Framework (ORMF)** is periodically reviewed by the Risk Management Committee and the Board to ensure ongoing resilience and regulatory compliance

---

f) Legal Risks

Legal Risk refers to the possibility of financial loss, reputational damage, or regulatory sanctions arising from the Bank's failure to comply with applicable laws, rules, regulations, contractual obligations, or from misinterpretation of legal requirements. It also includes exposure to litigation, disputes, and penalties due to non-adherence to legal norms.

Legal risk is closely linked to **compliance risk** and may arise from:

- **Breach of Statutory or Regulatory Requirements** – Failure to comply with banking, tax, employment, or other applicable laws
- **Market Misconduct** – Involvement in activities such as **market manipulation**, **insider trading**, or misuse of confidential information
- **Non-Compliance with Product Suitability and Disclosure Norms** – Offering financial products that are not aligned with the customer's risk profile or failure to provide adequate disclosures
- **Contractual Disputes** – Misunderstandings, ambiguities, or lapses in contractual documentation with clients, vendors, or third parties
- **Regulatory Misinterpretation** – Incorrect application of circulars, notifications, or legal provisions, which may lead to supervisory action or litigation

Misinterpretation or non-compliance with regulatory frameworks can lead to significant penalties, reputational damage, and enforcement actions by regulatory authorities. Therefore, the Bank must establish robust compliance systems, internal controls, and monitoring mechanisms to ensure adherence to all applicable laws, regulations, and guidelines, thereby preventing violations and safeguarding its operational integrity.

---

g) Options Risks

Option Risk arises from the **embedded options** in certain banking products that allow customers or counterparties to alter the expected cash flow behavior. These include, but are not limited to, the **prepayment of loans**, **early withdrawal of fixed deposits**, or **non-utilization of sanctioned credit limits**. Such options are exercised at the discretion of the customer, often influenced by changes in interest rates, liquidity needs, or market conditions.

Common Scenarios of Option Risk:

- **Loan Prepayments** – Borrowers may choose to repay term loans before the scheduled maturity, especially during falling interest rate environments, affecting projected interest income and asset-liability duration.
- **Premature Deposit Withdrawals** – Depositors may withdraw fixed deposits before maturity, resulting in unexpected outflows and potential liquidity shortfalls.
- **Undrawn Credit Lines** – Corporate clients may draw down large sanctioned but previously unused limits during stress periods, placing sudden demands on liquidity.

---

h) Reputation Risks

Reputation Risk refers to the potential for negative public perception, adverse media coverage, customer dissatisfaction, regulatory action, or operational failures to damage the Bank's credibility and public image. Such incidents may erode stakeholder trust and can lead to a **sudden loss of business**, including **large-scale withdrawal of deposits**, disruption of customer relationships, and diminished access to funding markets.

Key Sources of Reputation Risk:

- Regulatory non-compliance or penalties
- Governance failures or unethical practices
- Poor customer service or dispute handling
- Data breaches, frauds, or system outages
- Negative publicity from social or traditional media

Impact of Reputation Risk:

- Run on deposits and funding stress
- Loss of existing and prospective customers
- Downgrades by rating agencies
- Increased scrutiny by regulators and investors
- Long-term damage to market position and brand value

Mitigation Measures:

To safeguard its reputation and mitigate associated risks, the Bank shall:

- **Maintain Transparent and Ethical Practices** – Uphold high standards of governance, compliance, and integrity in all operations.
- **Implement Strong Customer Grievance Mechanisms** – Ensure timely redressal of complaints to prevent dissatisfaction from escalating.
- **Ensure Regulatory Compliance** – Adhere to all applicable laws, regulations, and supervisory

expectations to avoid penalties and reputational damage.

- **Establish Robust IT and Security Systems** – Prevent operational disruptions, cyber incidents, and data breaches that could undermine public confidence.
- **Maintain Sufficient Marketable Investments and Liquidity Buffers** – Enable the Bank to withstand sudden outflows and maintain depositor trust during periods of stress.
- **Proactive Communication Strategy** – Effectively manage public perception through clear, transparent, and timely communication during adverse events.

---

4. Asset-Liability Committee (ALCO)

The **Asset-Liability Committee (ALCO)**, chaired by the Chief Executive Officer (CEO), plays a pivotal role in managing the Bank's balance sheet risks and aligning its asset-liability profile with strategic objectives.

Key Responsibilities of ALCO:

- Ensuring adherence to the policies, risk limits, and guidelines approved by the Board of Directors
- Formulating and reviewing strategies related to the Bank's assets and liabilities, including pricing, maturity profiles, and funding mix
- Monitoring and managing liquidity risk, interest rate risk, and other market risks
- Supporting the overall risk management framework by evaluating risk-reward trade-offs in business decisions
- Reviewing key risk indicators, stress testing results, and reports on structural liquidity and interest rate sensitivity

Composition of ALCO

The Asset-Liability Committee (ALCO) is a high-level decision-making body tasked with managing the Bank's balance sheet risks and ensuring alignment with overall business and risk management strategies.

Members of ALCO:

1. President and Vice President – Serve as the Chairperson and Co-Chairperson, providing leadership and strategic direction.
2. Three Directors – Represent the Board and contribute to oversight and policy alignment.
3. Operational Support Staff – Includes senior officials from Treasury, Finance, Credit, and Risk

Management, who provide analytical support and data inputs for informed decision-making.

Functions and Responsibilities:

- Review and monitor the Bank's liquidity position, interest rate risk, and funding strategy on an ongoing basis.
- Analyze the risk-return trade-offs in asset-liability decisions in line with market conditions and regulatory expectations.
- Assess and approve assumptions used in liquidity modeling, behavioral maturity of deposits, and embedded options (e.g., prepayments, early withdrawals).
- Set internal risk limits and tolerance thresholds in line with the Bank's risk appetite.
- Recommend pricing strategies for deposits and advances, maturity profiles, and investment mix.

Meeting Frequency and Reporting:

- The ALCO shall convene at least once every quarter to evaluate key reports and initiate strategic decisions.
- More frequent meetings may be held in response to volatile market conditions or major regulatory developments.
- The committee is responsible for reviewing:
    - Structural Liquidity Statement (SLS)
    - Interest Rate Sensitivity Reports
    - Dynamic Liquidity Forecasts
    - Stress Testing Results
- All decisions, observations, and recommendations of the ALCO shall be formally recorded and reported to the Board of Directors on a quarterly basis to ensure transparency and oversight.

---

5. Reporting

Asset-Liability Management (ALM)-related statements and regulatory returns shall be compiled as of the last reporting Friday of March, June, September, and December, or as otherwise specified by the Reserve Bank of India (RBI) from time to time.

These statements shall be:

- **Prepared in a timely and accurate manner**, reflecting the Bank's liquidity and interest rate risk positions.
- **Placed before the Board of Directors or the designated committee** within **one month** from the reporting date for review and approval.

- **Submitted to the RBI and other regulatory authorities** only after obtaining the necessary internal approvals.

---

6. Revision of Policy

The Board of Directors shall review the Asset-Liability Management (ALM) Policy at least once every financial year. Based on evolving operational requirements, market conditions, and any regulatory updates or guidelines issued by the Reserve Bank of India (RBI), the Board shall incorporate necessary revisions or enhancements to ensure the policy remains effective, relevant, and compliant.

The Mahaveer Co-operative Bank Ltd., Belagavi

Sd/-
Chief Executive Officer/Vice-Chairman/Chairman