

Bank Alfalah
Bangladesh Operations
Disclosures on Risk Based Capital (Basel III) for the year ended December 2015

These qualitative and quantitative Disclosures have been made in accordance with Bangladesh Bank regulations for capital adequacy vide BRPD Circular No. 18 dated December 21, 2014. The purpose is to comply with the requirement for having adequate capital and the Supervisory review process under Pillar II. These disclosures are intended to assess information about the Bank's exposure to various risks.

Market Discipline Disclosures

Bank Alfalah Bangladesh Operations has migrated to Basel-III framework from January 2015 as per Bangladesh Bank guidelines and "Guidelines on Risk Based Capital Adequacy (Revised Regulatory Capital Framework for banks in line with Basel II)" issued vide BRPD Circular No. 35/2010 has been replaced with the "Guidelines on Risk Based Capital Adequacy (Revised Regulatory Capital Framework for banks in line with Basel III)" issued vide BRPD Circular no. 18/2014 with subsequent supplements/revisions.

Capital Management

The objective of managing capital is to safeguard the Bank's ability to continue as a going concern, so that it could continue to provide adequate returns to shareholders by pricing products and services commensurately with the level of risk. It is the policy of the Bank to maintain a strong capital base so as to maintain investor, creditor and market confidence and to sustain future development of the business. The impact of the level of capital on shareholder's return is also recognized and the Bank recognizes the need to maintain a balance between the higher returns that might be possible with greater gearing and the advantages and security afforded by a sound capital position.

Goals of managing capital

The bank manages its capital to attain the following objectives & goals:

- an appropriately capitalized status, as defined by Banking regulations by the central bank;
- acquire strong credit ratings that enable an optimized funding mix and liquidity sources at lesser costs;
- cover all risks underlying business activities; and
- retain flexibility to harness future investment opportunities, build and expand even in stressed times.

Risk Management

The variety of business activities undertaken by the Bank requires effective identification, measurement, monitoring, integration and management of different financial and non-financial risks that are constantly evolving as business activities change in response to concurrent internal and external developments. The Board Risk Management Committee (BRMC) is appointed and authorized by the Board of Directors (BOD) to assist in design, regular evaluation and timely updating of the risk management framework of the Bank. BRMC has further authorized management committees such as Central Management Committee (CMC), Central Credit Committee (CCC), Assets & Liabilities Committee (ALCO) and Investment Committee to supervise risk management activities within their respective scopes.

The risk management framework endeavors to be a comprehensive and evolving guideline to cater to changing business dynamics. The framework includes:

- Clearly defined risk management policies and procedures.
- Well constituted organizational structure, in the form of a separate risk management department, which ensures that individuals responsible for risk approval are independent from risk taking units i.e. Business Units.

- Mechanism for ongoing review of credit policies & procedures and risk exposures.

The primary objective of this architecture is to inculcate risk management into the organization flows to ensure that risks are accurately identified & assessed, properly documented, approved, and adequately monitored & managed in order to enhance long term earnings and to protect the interests of the Bank's depositors and shareholders.

The Bank's risk management framework has a well-defined organizational structure for effective management of credit risk, market risk, liquidity risk, operational risk, IT security risk.

In terms of Guidelines on RBCA, the Bank has adopted the Standardized Approach for Credit Risk, Standardized (rule based) Approach for Market Risk and Basic Indicator Approach for Operational Risk. In addition to regulatory capital requirement of computation as per Pillar-I, the Bank also assesses Interest Rate Risk, Equity Risk, and Foreign Exchange Risk on a regular basis to assess adequacy of the capital available as a cushion to withstand shocks from business environment adversities.

Under Pillar-III of the framework, "Basel-III Disclosures" of Bank Alfalah as on December 31, 2015 are as under:

a) Scope of Application

Bank Alfalah Bangladesh Operations (BAFL) has no subsidiaries or significant investments and hence, Basel III disclosure shall apply to the Bank level only.

b) Capital Structure

Qualitative Disclosures

BAFL's capital structure consists of Tier 1 and Tier 2 capital. Under Basel-III regime the regulatory capital is broadly classified into two categories: Tier I; & Tier II. Tier I capital has been bifurcated into Common Equity Tier 1 (CET1); and Additional Tier 1. CET1 includes funds from head office for capital adequacy purpose, & retained earnings after regulatory adjustments for deferred tax assets. The bank does not have any Additional Tier 1 capital.

Tier 2 capital includes general provisions subject to a to a maximum 1.25 percentage points of credit risk-weighted assets calculated under the standardized approach; and revaluation reserve for government securities which would follow phase in deductions as per audited revaluation reserve for securities amount as on December 2014 by 20% every year from 2015 till it fully phased out in 2019.

The computation of the amount of CET1, AT1; and Tier 2 capitals shall be subject to the following conditions as per the phase-in arrangement for implementation of minimum capital requirements:

1. CET1 should be at least 4.5% of the total Risk Weighted Assets (RWA)
2. Tier 1 capital should be at least 5.5% of the total RWA
3. Minimum Capital to Risk-weighted Asset ratio (CRAR) should be 10% of the total RWA
4. AT1 capital can be admitted maximum up to 1.5% of the total RWA or 33.33% of CET1, whichever is higher
5. Tier 2 capital can be admitted maximum up to 4.0% of the total RWA or 88.89% of CET1, whichever is higher
6. In addition to minimum CRAR, 0.625% of the total RWA is to be maintained as Capital Conservation Buffer (CCB) in the form of CET1 in every year up to 2019

Quantitative Disclosures

Bank Alfalah's capital structure is being enumerated as under:

	2015	2014
	Figures in BDT	
Common Equity Tier 1		
Fund Deposited with BB	4,423,010,704	4,420,627,471
Retained Earnings	503,765,211	181,923,322
	<u>4,926,775,915</u>	<u>4,602,550,793</u>
Regulatory adjustments: Deferred Tax Assets	(3,238,764)	-
Total CET1 Capital	<u>4,923,537,151</u>	<u>4,602,550,793</u>
Additional Tier 1 Capital	<u>-</u>	<u>-</u>
Tier 2 Capital		
General Provision (Limited to 1.25% of credit RWA)	90,883,500	98,466,414
Revaluation Reserve for Securities (with 20% phase-in deductions)	35,075,770	35,075,770
	<u>125,959,270</u>	<u>133,542,184</u>
Regulatory adjustments: (deduction of 20% of revaluation reserve)	(7,015,154)	-
Total Admissible Tier 2 Capital	<u>118,944,116</u>	<u>133,542,184</u>
Total Regulatory Capital	<u><u>5,042,481,267</u></u>	<u><u>4,736,092,977</u></u>

c) Capital Adequacy

Qualitative Disclosures

The Bank is subjected to the capital adequacy guidelines stipulated by Bangladesh Bank, which are based on the framework of the Basel Committee on Banking Supervision. As per the revised capital adequacy guidelines of 2014, the Bank is required to maintain a minimum Capital to Risk Weighted Asset Ratio (CRAR) of 10.00% with regard to Credit Risk, Market Risk and Operational Risk. In addition to this, capital adequacy ratio has to be maintained as per phase-in arrangements stipulated in the revised guidelines under Basel-III by Bangladesh Bank vide BRPD Circular no. 18/2014 dated December 21, 2014 which is as under:

Phase-in arrangement	2015
Minimum Common Equity Tier 1 Capital Ratio	4.5%
Capital Conservation Buffer	-
Minimum CET1 plus Capital Conservation Buffer	4.5%
Minimum Tier 1 Capital Ratio	5.5%
Minimum Total Capital Ratio	10%
Minimum Total Capital plus Capital Conservation Buffer	10%

BAFL has adopted Standardized Approach for Credit Risk, Standardized (rule based) Approach for Market Risk and Basic Indicator Approach (BIA) for Operational Risk for computing CRAR.

BAFL has a capital adequacy ratio (CRAR) of 55.36% as against the regularity 10% MCR, of which T-1 capital adequacy ratio is 54.05% against regularity minimum of 5.5%; and T-2 capital adequacy ratio is 1.31%. The capital adequacy ratio is achieved by the Bank through improvement in the capital base, asset quality at the existing volume level, ensuring better recovery management and composition of asset mix with low risk. Basel-III Framework enables a more risk-sensitive regulatory capital calculation to promote long term viability of the Bank. As the Bank carry on the business on a limited area network basis, it is desired that it is able to continuously monitor the exposure across entire organization and aggregate the risks so as to take an integrated

approach/view. Maximization of the return on risk-adjusted capital is the principal basis to be used in determining how capital is allocated within the Bank to particular operations. The Bank remained compliant with all externally imposed capital requirements throughout the year. Further, there has been no material change in the Bank's management of capital during the year.

Quantitative Disclosures

	2015	2014
	Figures in BDT	
RWA for on-balance sheet credit risk	6,043,289,252	7,011,022,141
RWA for off-balance sheet credit risk	,227,390,764	110,303,102
Total Credit Risk RWA	7,270,680,016	7,121,325,243
Market Risk RWA	478,266,151	341,918,523
Operational Risk RWA	1,359,860,355	1,042,974,517
Total Risk Weighted Assets	9,108,806,522	8,506,218,283
Amount of Regulatory Capital to meet unforeseen loss		
Capital requirement for Credit Risk	727,068,002	712,132,524
Capital requirement for Market Risk	47,826,615	34,191,852
Capital requirement for Operational Risk	135,986,035	104,297,452
Total Capital requirement	910,880,652	850,621,828
Common Equity Tier 1 Capital	4,923,537,151	-
Total Tier 1 Capital	4,923,537,151	4,602,550,793
Total Tier 2 Capital	118,944,116	133,542,184
A. Total Regulatory Capital	5,042,481,267	4,736,092,977
Capital Conservation Buffer	N/A	N/A
B. Total required capital	4,000,000,000	4,000,000,000
(10% of RWA or BDT 4,000,000,000 whichever is higher)		
Capital Surplus / (Shortfall) [A-B]	1,042,481,267	736,092,977
Capital adequacy ratio		
CET 1 Capital ratio	54.05%	N/A
Total Tier 1 Capital ratio	54.05%	54.11%
Total Tier 2 Capital ratio	1.31%	1.57%
Total Capital Ratio (CRAR)	55.36%	55.68%

Assets

Bank's assets comprises of cash, balance with other banks, investments in treasury bills and bond, investments in share portfolio, loan and advances, physical assets and other assets.

Loans and advances represented 42.23% of total assets of the Bank. The classified loan ratio was 6.82% indicating efficient asset management of the Bank.

Nature of Assets

Assets of Bank Alfalah are categorized as per the following:

- Banking Book Asset
- Trading Book Asset

In general, banking book assets comprise assets and liabilities, which are contracted basically on account of relationship or for steady income and statutory obligations and are generally held till maturity. On the contrary, trading book assets refer to the book of financial instruments held with the intention for short-term trading. It refers to those assets held primarily for generating profit on short-term differences in prices/yields.

Banking book and trading book assets represent 85.78% and 14.22% respectively of the total assets.

The major components of the earning assets and non-earning assets for the bank are as follows:

Earning Assets

- Loans & advance
- Investments in securities
- Money at call & short notice
- Balance with other banks and FIs

Non-Earning Assets

- Cash in hand
- Balance with Bangladesh Bank for CRR maintenance
- Fixed Assets
- Other assets

Assets are monitored under the purview of ALCO on a regular basis to cope with unexpected risk. Assets are classified as per the directive of the Bangladesh Bank. Classified assets are the Default Loans in respect to which recipient/beneficiary fails to make timely payment of interest or principal as per the agreed schedule for repayment.

Bank categorized classified loans in following three (03) categories following the Bangladesh Bank guidelines:

- Sub-standard
- Doubtful
- Bad/Loss

Addition/Reduction of Classified Assets

Classified loans stood at BDT 52.92 crore as on December 31, 2015 whereas it was BDT 35.21 crore as on December 31, 2014 representing an increase of BDT 17.71 crore.

	2015	2014
	Figures in BDT	
1. Cash in Hand & Balance with BB (Excluding Fcy)	908,282,292	762,826,019
2. Balance with BB (Fcy as part of Capital)	334,120,704	331,737,471
3. Claims on Other Banks	1,498,937,433	1,065,060,672
a) Balance with other banks	1,498,937,433	1,065,060,672
b) Money at Call & Short Notice	-	-
4. Investment (HTM)	4,540,966,564	4,185,170,528

a) Government (under lien with BB as part of Capital)	4,340,966,564	4,185,170,528
b) Qualifying (banks, etc)	-	-
c) Others	200,000,000	-
5. Loans & Advances	7,758,425,232	7,508,280,374
a) Classified	529,195,301	352,085,649
SS	43,813,934	-
DF	4,827,377	1,129,761
BL	480,553,991	350,955,888
b) Unclassified	7,229,229,931	7,156,194,725
6. Risk Weighted Assets	7,270,680,016	7,121,325,242
a) Below 100% RW	1,688,692,094	434,505,248
b) 100% RW	1,708,132,691	5,601,298,792
c) Above 100% RW	3,873,855,230	1,085,521,202
7. Rated Status	7,270,680,016	7,121,325,242
a) Rated Assets	1,759,507,533	4,206,591,498
b) Unrated Assets	5,511,172,483	2,914,733,744
8. Other assets (Including Fixed Assets)	718,882,976	591,671,316
A. Total Banking Book Assets (1+2+3+4+5+8)	15,759,615,201	14,444,746,380
B. Trading Book Assets		
1. FC held in Hand	450,804	2,909,897
2. FC held in BB & Nostro Account	199,003,341	156,225,712
3. Investment (Trading)	2,413,977,181	1,950,087,049
a) Govt. (Part of Govt. HTM, if held above the required SLR amount)	-	-
b) HFT	2,413,977,181	1,950,087,049
c) AFS (if any)	-	-
B. Total Trading Book Assets (1+2+3)	2,613,431,326	2,109,222,658
Total Assets (A+B)	18,373,046,527	16,553,969,038

d) Credit Risk

Overview of the Bank's Credit Risk Management Policy

Credit risk is the identification of probability that counterparty will cause a financial loss to the Bank due to its inability or unwillingness to meet its contractual obligation. This credit risk arises mainly from both direct lending activities as well as contingent liabilities. Credit risk management processes encompass identification, assessment, measurement, monitoring and control of Bank's exposure to this credit risk. The Bank's credit risk management philosophy is based on Bank's overall business strategy / direction as established by the Board. The Bank is committed to the appropriate level of due diligence to ensure that credit risks have been properly analyzed, fully disclosed to the approving authorities and appropriately rated, also ensuring that the credit commitment is appropriately structured, priced (in line with market practices) and documented.

The Bank, as per Central Bank Guidelines, has migrated to Basel-III from January 2015 with the standardized approach. For credit risk, procedural manual has been developed, which also incorporates a comprehensive system of cross-checks for data accuracy. Simultaneously, processes have been set for fine-tuning systems & procedures, information technology capabilities and risk governance structure to meet the requirements of the advanced approaches as well.

The Bank has built and maintained a sound loan portfolio in terms of well-defined credit policy approved by BOD. Its credit evaluation system comprises of well-designed credit appraisal, sanctioning and review procedures for the purpose of emphasizing prudence in lending activities and ensuring the high quality of asset portfolio. In order to have an effective and efficient risk assessment, and to closely align its functions with Business, Credit Division has separate units for corporate banking, Islamic banking, commercial & SME banking, agricultural financing, and overseas operations.

The Bank manages its portfolio of loan assets with a view to limit concentrations in terms of risk quality, industry, maturity and large exposure. Internal rating based portfolio analysis is also conducted on regular basis. This portfolio level oversight is maintained by Risk Management Division.

A sophisticated internal credit rating system has been developed by the Bank, which is capable of quantifying counter-party & transaction risk in accordance with the best practices. The system takes into consideration qualitative and quantitative factors of the counter-party, transaction structure & security and generates an internal rating vis-à-vis anticipated customer behavior. The system is continuously reviewed for best results in line with the Bangladesh Bank's guidelines for Internal Credit Rating. Moreover, the system is backed by secured database with backup support and is capable of generating MIS reports providing snapshot of the entire portfolio for strategising and decision making. The System now also has the capability to auto generate alerts on accounts showing weakness in financials and hence requiring a more vigilant monitoring.

A Centralized Credit Administration Division under Operations Group is working towards ensuring that terms of approval of credit sanctions and regulatory stipulations are complied, all documentation including security documentation is regular & fully enforceable and all disbursements of approved facilities are made only after necessary authorization by CAD. CAD keeps a watch on the quality of the credit portfolio in terms of borrowers' behavior, identifies weakening accounts relationships and reports it to the appropriate authority with a view to arrest deterioration. Special attention is paid by the management in respect of Non-performing Loans (NPL). The Risk Management Division also monitors the NPL portfolio of the Bank and reports the same to BRMC.

Proactive credit-risk management practices in the form of Integrated Bank-wide Risk Management and Internal Control Framework, adherence to Basel-III accord, constitute the important risk management measures the bank is engaged in for mitigating these exposures. The current focus is on augmenting the Bank's abilities to quantify risk in a consistent, reliable and valid fashion which will ensure advanced level of sophistication in the Credit Risk measurement and management in the years ahead.

Qualitative Disclosures

BAFL is using The Standardized Approach (TSA) of BB Basel-III accord for the purpose of estimating Credit Risk Weighted Assets. Under TSA Banks are allowed to take into consideration external rating(s) of counter-party's for the purpose of calculating Risk Weighted Assets. A detailed procedural manual specifying return-based formats, methodologies and processes for deriving Credit Risk Weighted Assets in accordance with the BB Basel-III Standardized Approach is in place and firmly adhered.

External Ratings

Bangladesh Bank Basel-III guidelines require banks to use ratings assigned by specified External Credit Assessment Agencies (ECAIs) namely CRAB, CRISL, ECRL, NCRL, ACRSL, Alpha Credit Rating Limited (ACRL), WASO Credit Rating Company (BD) Limited, The Bangladesh Rating Agency Limited, Moody's, Fitch, and Standard & Poor's (S&P). The Bank uses these ECAIs to rate its exposures denominated in Bangladeshi currency on certain corporates and banks incorporated in Bangladesh.

The Bank uses external ratings for the purposes of computing the risk weights as per the Basel-III framework. For exposures with a contractual maturity of less than or equal to one year, short-term rating given by approved Rating Agencies is used, whereas for long-term exposure with maturity of greater than one year, long-term rating is used. Where there are two ratings available, the lower rating is considered and where there are three or more ratings the second - lowest rating is considered.

Credit Risk Mitigation Policy

BAFL defines collateral as the assets or rights provided by the borrower or a third party in order to secure a credit facility. The Bank would have the rights of secured creditor in respect of the assets/contracts offered as security for the obligations of the borrower/obligor.

Collateral Valuation and Management

As stipulated in the BB Basel-III guidelines, the Bank uses the comprehensive approach for collateral valuation. Under this approach, the Bank reduces its credit exposure to counterparty when calculating its capital requirements to the extent of risk mitigation provided by the eligible financial collateral as specified in the Basel-III guidelines. In line with Basel-III guidelines, the Bank makes adjustments in eligible collaterals received for possible future fluctuations in the value of the collateral in line with the requirements specified by BB guidelines. These adjustments, also referred to as 'haircuts', to produce volatility-adjusted amounts for collateral, are reduced from the exposure to compute the capital charge based on the applicable risk weights.

Types of Collateral taken by the Bank

BAFL determines the appropriate collateral for each facility based on the type of product and counterparty. In case of small and medium enterprises financing, fixed assets are generally taken as security for long tenor loans and current assets for working capital finance usually backed by mortgage. In case of working capital facilities for large corporate relationships, facilities are also being allowed against creation of charges over current & fixed assets of the respective companies to mitigate any eventuality. For project finance, security of the assets of the borrower and assignment of the underlying project contracts is generally obtained. Other security such as cash collateral, TDRs, charges on receivables are also obtained by the Bank. Moreover, in order to cover the entire exposure Personal Guarantees of Directors are also obtained by the Bank. The valuation of the properties is carried out by an approved independent valuation agency.

The decision on the type and quantum of collateral for each transaction is taken by the credit approving authority as per the credit approval authorization approved by the BoD. For facilities provided as per approved product policies (retail products, loan against shares etc.), collateral is taken in line with the policy.

Types of Eligible Financial Collateral

For credit risk mitigation purposes, the Bank considers all types of financial collaterals that are eligible under BB Basel-III accord. This includes Cash/TDRs, securities issued by Government of Bangladesh such as T-Bills & T-Bonds, certain debt securities rated by a recognized credit rating agency, and guarantees from certain specified entities. In general, for Capital calculation purposes, in line with the BB Basel-III requirements, the Bank recognizes only eligible collaterals as mentioned in the BB Basel-III accord.

In addition to collaterals, Guarantees also secure the transactions by reducing credit risk. Where guarantees are direct, explicit, irrevocable and unconditional banks may consider such credit protections in calculating capital requirements through a substitution approach e.g., lower rating/risk weight of guarantor than the counterparty will lead to reduced capital charges.

Credit Concentration Risk

Credit concentration risk arises mainly due to concentration of exposures under various categories viz, industry, geography, and single/group borrower exposures. Within credit portfolio, as a prudential measure aimed at better risk management and avoidance of concentration of risks, the BB has prescribed regulatory limits on banks' maximum exposure to single borrower and group borrowers. Moreover, in order to restrict the industry concentration risk, BAFL's annual credit plan spells out the maximum allowable exposure that it can take on specific industries. Additionally, the newly developed Internal Rating System allows the Bank to monitor risk rating concentration of counterparties against different grades/scores ranging from 1 – 12 (1 being the best and 10 – 12 for defaulters).

Total Exposures of Credit Risk

2015
2014
Figures in BDT

1. Funded

- a) Domestic
- b) Overseas

2015	2014
18,849,198,969	17,092,544,705
18,849,198,969	17,092,544,705
-	-

2. Non-Funded	1,901,951,409	139,407,834
a) Domestic	1,901,951,409	139,407,834
b) Overseas	-	-
3. Distribution of Risk Exposure by Claims		
Claims on Sovereigns and Central Banks	8,169,382,233	7,293,408,580
Claims on Banks and Securities Firms	1,892,520,477	2,017,631,048
Claims on Corporate (excl Medium Enterprise loan)	5,821,849,757	658,948,226
Claims on the Retail & Small Enterprises (excl consumer loan)	80,011,198	3,987,900
Claims secured by residential property	-	-
Other Categories:	2,115,539,300	300,936,794
Past due Loans / NPL	213,587,892	161,528,960
Off-Balance Sheet Items	1,901,951,409	139,407,834
4. Credit Risk Mitigation		
Claims Secured by Financial Collateral	917,158,299	399,442,606
Net Exposure after the Application of Haircuts.	6,534,943,560	4,250,174,545
Claims Secured by Eligible Guarantee	-	-
Maturity wise Classification of Loans and advances :		
With a residual maturity of BDT		
Re-payable on Demand	67,534,538	1,379,900,093
Not more than 3 months	774,880,931	1,427,290,112
Over 3 months but not more than 1 year	5,606,337,623	4,132,070,281
Over 1 year but not more than 5 years	1,184,383,909	569,019,888
Over 5 years	125,288,232	-
	7,758,425,232	7,508,280,374
Country-wise Classification of Loans and advances:		
Inside Bangladesh		
Conventional Banking		
Current Finance	2,397,542,924	2,815,480,846
Term Finance	2,356,841,768	1,615,498,410
Payments against Documents (PAD)	24,644,297	-
Credit Card	-	-
Staff Loan	4,060,966	4,834,047
Trust Receipts	47,177,881	26,438,841
	4,830,267,836	4,462,252,144
Islamic Banking		
Morabaha (LPO)	2,447,552,063	2,357,868,987
Trust Receipts	71,812,999	80,263,298
Own acceptance Purchased	-	49,169,806
Payment against documents (PAD)	-	-
Finance Against Foreign Bill	19,355,667	-
Morabaha Manual	5,053,916	40,761,848
Staff Morabaha	39,775,547	54,826,477
	2,583,550,192	2,582,890,416
Outside Bangladesh	-	-
	7,413,818,028	7,045,142,560
Bills purchased and discounted (Morabaha export bills) :		
Inside Bangladesh	344,607,204	463,137,814

Outside Bangladesh

-	-
344,607,204	463,137,814
7,758,425,232	7,508,280,374

Maturity wise Classification of Bills Purchased and discounted:

Re-payable:-

Within 1 month

Over 1 month but less than 3 months

Over 3 months but less than 6 months

6 months or more

117,455,080	131,792,408
143,201,681	171,546,548
83,950,444	159,798,858
-	-
344,607,204	463,137,814

Sector-wise Classification of loans and advances:

Agriculture, forestry, hunting and fishing

Automobile and transportation equipment

Chemical and pharmaceuticals

Cement

Sugar

Construction

Electronics and electrical appliances

Financial institution

Garments (Knit and woven)

Information technology and telecom

Iron and steel

Footwear and leather garments

Paper, printing and packaging

Power/electricity, gas, water, sanitary

Wholesale and retail trade

Exports and imports

Transport, storage and communication

Textile, yarn and spinning

Services

Others

223,811,488	70,690,066
35,670,910	24,447,000
367,048,126	295,153,485
230,870,535	50,540,426
-	9,289,603
26,167,441	85,445,141
35,042,346	129,608,554
238,491,749	446,386,422
-	-
-	-
1,130,573,994	1,280,994,300
201,406,762	197,453,000
150,471,164	5,979,422
995,267,421	-
301,403,801	562,982,409
284,420,554	617,972,004
20,122,658	41,554,425
663,271,425	673,715,040
2,949,418	3,013,000
2,851,435,441	3,013,056,076
7,758,425,232	7,508,280,374

Grouping of Loans and advances as per Classification Rules of Bangladesh Bank:

Unclassified:

Standard including staff loan.

Special Mention Account (SMA)

7,227,469,200	7,143,063,794
1,760,732	13,130,931
7,229,229,931	7,156,194,725

Classified:

Substandard

Doubtful

Bad or loss

43,813,934	-
4,827,377	1,129,761
480,553,991	350,955,888
529,195,301	352,085,649

Total

7,758,425,232	7,508,280,374
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Maintenance of Specific Provision

BAFL follows BB guidelines regarding loan classifications, provisioning and any other issues related to Non Performing Loan (NPL). Bank's internal credit guidelines also directs on managing of NPL, loan provisioning review procedure, debt write-off, facility grading, reporting requirements, interest recognitions. While dealing

with NPL, bank's decision is always complied by local rules and regulations as well as group guidelines which are more conservative than the local regulations.

Specific provision for all classified loan i.e. Sub-standard, Doubtful, and Bad Loss are maintained by the bank as per Bangladesh Bank guideline. In the year Bank provided BDT 36.48 crore for specific provisions.

Policies and processes for maintaining specific provision

Bank mainly maintained specific provision against classified loan accordingly to Bangladesh Bank BRPD Circular No. 08 "Loan Classification and Provisioning" dated August 02, 2015 and BRPD Circular No. 14 "Master Circular: Loan Classification and Provisioning" dated September 23, 2012 and other guidelines time to time issued by the Bangladesh Bank.

Banks maintained specific provision at the following rates in respect of classified Continuous, Demand and Fixed Term Loans:

1. Sub-standard 20%
2. Doubtful 50%
3. Bad/Loss 100%

At the time of determining Gross Income for calculating operational risk, specific provision and other items are grossed up with Net Profit.

	2015	2014
	Figures in BDT	
A. Gross Non Performing Assets (NPAs)		
Non Performing Assets (NPAs) to Outstanding Loans & Advances	6.82%	4.69%
B. Movement of Non Performing Assets (NPAs)		
Opening Balance	352,085,649	578,473,121
Additions	303,924,695	-
Reductions	126,815,043	226,387,472
Closing Balance	<u>529,195,301</u>	<u>352,085,649</u>
C. Movement of Specific Provisions for NPAs		
Opening Balance	439,683,400	392,407,643
Provisions made during the period	35,245,096	67,072,112
Write-off	35,707,932	-
Write-back of Excess Provisions/Prov. Reversed	74,352,423	19,796,355
Closing Balance	<u>364,868,141</u>	<u>439,683,400</u>

e) Equities: Disclosures for Banking Book Positions

Qualitative Disclosures

BAFL does not hold any trading position in equities (neither quoted nor unquoted).

f) Interest Rate Risk in the Banking Book (IRRBB)

Qualitative Disclosures

The interest rate risk arises from the fluctuation in the value of financial instruments consequent to changes in

market interest rates. The Bank is exposed to interest rate risk as a result of mismatches or gaps in the amounts of assets and liabilities and off-balance sheet instruments that mature or is re-priced during a given period. Treasury is primarily responsible for management of interest rate risk on a daily basis. The Bank's Asset and Liability Committee (ALCO) is responsible for the oversight of the interest rate risk. In order to ensure that this risk is managed within acceptable limits, RMD monitors & reports various gap limits, management action point limits and re-pricing of the assets and liabilities on a regular basis. Bank adopts maturity method in measuring interest rate risk in respect of securities in trading book. The capital charge for entire market risk is computed under the standardized approach using the maturity method and in accordance with the guideline issued by Bangladesh Bank.

Quantitative Disclosures

Interest rate risk in banking book as of Dec 31, 2015 is calculated as change in Market Value (MV) of equity as under -

Change in Interest Rate	Duration (in Years)	1%	2%	3%
Duration of Assets	1.59			
Duration of Liabilities	0.33			
Duration Gap	1.36			
Change in Market Value of Equity (in BDT)		(247,276,691.20)	(494,553,382.30)	(741,830,073.50)

The above result implies that bank may lose more value in its interest rate sensitive assets than its liabilities and thus an increase in interest rate may cause a decline in the economic value of bank's capital.

g) Market Risk

Qualitative Disclosures

Trading book consists of positions in financial instruments held with trading intent. A capital charge is applicable for financial instruments which are free from any restrictive covenants on tradability in line with Basel-III guidelines issued by Bangladesh Bank. Generally, investments in 'Held for Trading' portfolios are focal parts of the Trading Book. In addition, positions should be valued prudently.

BAFL has a comprehensive Treasury and Investment Policy which inter alia covers assessment, monitoring and management of all the above market risks. Bank has defined various internal market risks and is computing the capital requirement as per standardized approach of Basel-III.

Methods used to measure Market risk

BAFL defines market risk as the risk of loss in on-balance sheet and off-balance sheet positions arising from movements in market prices. Under market risk management, interest rate risk, equity price risk and foreign exchange risks are monitored. Bank adopted Standardized (rule based) Approach for measuring Market Risks.

Interest Rate Risk

The possibility of a reduction in the value of a security, especially T-Bill & T-Bond, resulting from a rise in interest rates. This risk can be reduced by diversifying the durations of the fixed-income investments that are held at a given time.

Foreign Exchange Risk

The Bank has fixed maximum overnight exposure for foreign exchange exposures (NOP) in various currencies. Also, stop loss limit and single deal limits are in place for monitoring the forex operations of the Dealers. Foreign Exchange Gap limits are in place for evaluating the bank's long or short position in currencies applicable for forward transactions. VaR analysis is conducted on regular basis to measure and monitor the FX

risk.

Market Risk Management system

Bank has well defined Risk Management Policy, Investment Policy, Asset-Liability Management Policy etc. which covers important areas of market risk management.

Policies and processes for mitigating market risk

Detailed policies are operational for Investment Management, Asset Liability Management and Market Risk Management, which deal in detail the various strategies and processes for monitoring Market Risk.

In order to deal with the market risk issues, the Bank has in place a Treasury and Investment Policy. The policy details the various tools and guidelines for market risk identification, market risk measurement and risk mitigation. Bank has constituted Asset Liability Management Committee to oversee the Risk Management and ALM functions in the Bank and monitor the progress in its implementation.

Besides these following tools are used for market risk management / mitigation:

- (a) Delegation of Powers- Bank has well-defined discretionary powers for different level of authorities of the Bank for taking investment decisions.
- (b) Prudential Limits - Various limits such as exposure limit, stop loss limits, duration etc. have been fixed.
- (c) Asset Liability Management Committee (ALCO) - Under Risk Management architecture of Bank ALCO committee of executives is constituted and is monitoring management of liquidity and interest rate risk. ALCO support group of executives / officers is constituted to support ALCO.

	2015	2014
	Figures in BDT	
Capital Requirements for -		
Interest Rate Risk	29,074,171	26,580,461
Equity Position Risk	-	-
Foreign Exchange Risk	18,752,444	7,611,391
Commodity Risk	-	-
	<u>47,826,615</u>	<u>34,191,852</u>

h) Operational Risk

Qualitative Disclosures

Basel III defines Operational risk as, “the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events”. This definition includes legal risk, but excludes strategic and reputation risk.

Policies and processes for mitigating operational risk

Bank has put in place the following measures to control and mitigate operational risks:

- Instructions, circulars, job descriptions, training programmes etc. including Operational and Other Manuals
- Delegation of financial powers at various levels of officers for different type of financial transactions
- Inputs on operational risk are included in the relevant training programmes
- Bank obtains insurance coverage for potential operational risks
- A system of prompt submission of reports on frauds is in place

- A Key Risk Indicator (KRI) module is in place to gauge operational risk against set parameters
- An automated Operational Loss Database (OPLDB) module provides early warning signals about occurrence of risk events that enable modeling of future operational loss events.

BAFL adopted Basic Indicator approach for calculating operational risk which is as under:

Quantitative Disclosures

	2015	2014
	Figures in BDT	
Capital Requirements for Operational Risk	135,986,035	104,297,452

i) Leverage Ratio

Qualitative Disclosures

Building up of excessive on & off-balance sheet leverage in the banking system was widely believed to have contributed to the global financial crisis in 2008. With a view to address this, international community has proposed the adoption of a non-risk-based capital measure, the leverage ratio, as an additional prudential tool to complement minimum capital adequacy requirements. Hence, leverage ratio had been introduced under Basel III. Leverage ratio is the relative amount of Tier 1 capital to total exposure (after related deductions) of the Bank (not risk-weighted) which has been set at minimum 3%.

Under Basel III, a simple, transparent, non-risk based regulatory leverage ratio has been introduced to achieve the following objectives:

- constrain leverage in the banking sector, thus helping to mitigate the risk of the destabilizing deleveraging processes which can damage the financial system and the economy
- introduce additional safeguards against model risk and measurement error by supplementing the risk-based measure with a simple, transparent, independent measure of risk

The Risk Management Division regularly reviews the leverage ratios and advice the management to strictly monitor leverage ratio in addition to the Pillar 1 Minimum Capital Requirement.

The bank reviews its leverage position as per the Guidelines on Risk Based Capital Adequacy (revised regulatory capital framework for banks in line with Basel III). In addition, the bank has Risk Appetite as per Credit Risk Management Policy and Risk Appetite Framework of the Bank. It also employs annual budget plan and capital growth plan for managing excessive on and off-balance sheet leverage.

The bank calculates the exposure under standardized approach as per Basel III guideline. The capital measure for the leverage ratio is based on the new definition of Tier 1 capital with relevant deductions of items which do not contribute to leverage. The exposure measure for the leverage ratio will generally follow the accounting measure of exposure. In order to measure the exposure consistently with financial accounts, the following will be applied by the bank:

- On balance sheet, non-derivative exposures will be net of specific provisions & valuation adjustments (e.g. surplus/deficit on HFT positions).
- Items deducted from Tier 1 capital also applies here (e.g. DTA)
- Physical or financial collateral, guarantee or credit risk mitigation purchased is not allowed to reduce on-balance sheet exposure.
- Netting of loans & deposits is not allowed.

Quantitative Disclosures

	2015	2014
	Figures in BDT	
Tier 1 capital (considering all regulatory adjustments)	4,943,505,286	N/A
On-balance sheet exposure	18,283,779,563	N/A
Off-balance sheet exposure	1,901,951,409	N/A
Regulatory adjustments made to Tier 1 capital	3,238,764	N/A
Total Exposure	20,182,492,208	N/A
Leverage Ratio	24.49%	N/A

j) Liquidity Ratio

Qualitative Disclosures

Liquidity risk is the potential for loss to the bank arising from either its inability to meet its obligations or to fund increases in assets as they fall due without incurring an unacceptable cost.

The Bank's Asset and Liability Committee (ALCO) is primarily responsible for the formulation of the overall strategy and oversight of the asset liability function including liquidity management. The BoD has approved a comprehensive Market & Liquidity Risk Management Policy which stipulates the various parameters to monitor and control liquidity risk including maintenance of various liquidity ratios. RMD is responsible for independent monitoring of the overall liquidity risk in line with regulatory requirements and BoD approved Risk Framework. It also monitors & reports the maintenance of liquidity buffer in form of excess Govt. securities over regulatory requirement, liquidity ratios and depositors' concentration both in terms of the overall funding mix and avoidance of undue reliance on large volume deposits. As core retail deposits form a considerable part of the Bank's overall funding mix, significant importance is being given to the stability and growth of these deposits. Maturity gaps and sources of funding are also reviewed in order to ensure diversification in terms of tenor, currency and geography. Moreover, the bank also prepares a 'Contingency Funding Plan' (CFP) to address liquidity issues in times of stress / crisis situations containing early warning indicators to pre-empt unforeseen liquidity crisis. In addition to this, the Bank has designed different scenarios of cash outflows to stress test adequacy of its liquid assets.

Since the difficulties experienced by some banks during the financial crisis were due to lapses in basic principles of liquidity risk management, the bank has already implemented regulatory ratios pertaining to liquidity management as per Basel III accord i.e. the Liquidity Coverage Ratio (LCR) and the Net Stable Funding Ratio (NSFR). The LCR aims to ensure that a bank maintains an adequate level of unencumbered, high-quality liquid assets that can be converted into cash to meet its liquidity needs for 30 calendar days while the NSFR aims to limit over-reliance on short-term wholesale funding during times of abundant market liquidity and encourage better assessment of liquidity risk across all on- and off-balance sheet items with minimum acceptable value of more than 100 percent, indicating that available stable funding (ASF) should be greater than required funding (RSF).

In addition to regulatory liquidity standards, the bank also uses a number of ratios on daily basis to assess the liquidity. The most important being Advances to Deposits ratio. Other ratios include large volume deposits (LVD) to Total Deposits, Liquid Assets to Total Demand and Time liabilities, Unencumbered T-Bills, T-Bonds to Liquid Assets, etc. These ratios are monitored as per predefined capping set by the ALCO however; the limits are subject to change in line with external & internal regulatory environment duly approved by the relevant authorities. The bank also monitors Maturity Gaps with percentage of bucket-wise gap to total assets and conducts liquidity stress testing on daily basis to gauge out the liquid resources available after cash outflows.

An effective MIS is the backbone of liquidity management. The procedures adopted to support liquidity management include: reporting of heavy withdrawal (BDT 100 mln or above) by the branches to the Treasury

Division at least one working day in advance; reporting of maturity mismatch in various time bands GAP; report on contingent liabilities on quarterly basis; credit portfolio, overdue schedule and NPLs over a number of time periods;. For periodic monitoring and controlling liquidity risk within limits a Funds Flow Analysis (FFA) is prepared and tolerance limits are assigned for gaps identified. FFA estimates all the cash inflows and outflows of the Bank and thus determines the net deficit or surplus which shall be broken down into appropriate time-bands after considering the behavior of assets, liabilities and off-balance sheet items included in these time-bands. To maintain sufficient liquidity the bank has set strategy to keep a margin of excess liquidity of minimum 5% over regulatory requirement; and liquidity needs should be estimated in variety of scenarios in the CFP and in stress testing conducted by the RMD.

The bank remains stringent in maintaining the ratios with a considerable cushion over and above the regulatory requirement to be able to mitigate liquidity risk. Therefore, the bank focuses to keep LCR and NSFR ratio over and above regulatory threshold level. The RMD proactively calculates these two ratios in regular interval and assists ALCO in setting strategies to keep the ratios at a considerable level to comply with the Basel regulations.

Quantitative Disclosures

	2015	2014
	Figures in BDT	
Liquidity Coverage Ratio (LCR)	164.44%	N/A
Net Stable Funding Ratio (NSFR)	102.75%	N/A
Stock of High quality liquid assets	3,657,094	N/A
Total net cash outflows over the next 30 calendar days	2,223,906	N/A
Available amount of stable funding	14,718,059	N/A
Required amount of stable funding	14,323,626	N/A

k) Remuneration

Qualitative Disclosures

Information relating to the bodies that oversee remuneration

The Bank has a Group specified remuneration policy which is designed to positively reward the achievement of long-term sustainable performance to keep the performing resources motivated to pursue long-term career in the bank while remain committed to perform their assigned roles for achieving organizational goals and meeting stakeholders expectations; as well as to attract the best of quality external resources from the market when required to meet organizational needs. The Group has a dedicated Board Human Resources & Nomination Committee (BHR&NC) consisting of 3 Members of Board of Directors and President/CEO of the bank; which periodically reviews competitiveness of banks remuneration, compensation & benefits packages in line with industry and also initiates systematic measures to bring necessary changes in the remuneration policy to ensure fairness and competitiveness in rewarding, motivating and retaining banks valued resources. The proposals of committee therefore gets reviewed and approved by the Board of Directors, ensuring due consideration and effective mitigation of possible associated risks (if any) arising out of the proposal under review. The BOD and all its committees are stationed at our Head Office in Karachi-Pakistan and liaison with Bangladesh management from time to time in this regard.

During the year of 2015, bank had not sought advice of any external consultant with regards to remuneration of Senior Staff. Moreover the Bank Alfalah - Bangladesh Operations does not have any foreign subsidiaries and branches, thus scope of region or business line wise separate remuneration policy is not in place.

The operation of the bank in Bangladesh is manager mainly by Management Committee Team (MANCOM) chairman of which is Country Head of Bangladesh. The MANCOM operates under a controlled function and requires Head Office approval for taking significant risk exposure in excess of their respective functional limit. Thus, there is no significant risk taker in the bank, that can cause significant material effect. The MANCOM

consists of 7 Senior Management staff comprise of Country Head, Country Operations Head, Country Credit Head, Head of Retail, Head of Treasury, Head of Finance and Administration and Head of Compliance.

Information relating to the design and structure of remuneration processes.

Bank maintains a well designed and competitive remuneration and compensation plan as an integral part of its organization strategy to ensure that employees remain focused and motivated toward achievement of organization goals and excels with it. Bank Alfalah to succeed in this increasingly competitive baking industry stress to ensure a well-designed compensation plan for their staff ensuring internal & external equity to keep them motivated on long term basis as well as controlling costs against forecasted return thus mitigating the associated managerial, financial and regulatory risks. Bank is not in practice of following any separate remuneration and compensation structure for senior executives of the bank. The remuneration structure of banks senior executives also comprises same components as other staff and mainly consists 3 major differentials as below:

- Direct Financial Compensation
- Indirect Financial Compensation
- Non-Financial Compensation

Direct Financial Compensation

The major portion of the direct financial compensation components are govern by the monthly remuneration paid to the each staff based on their Job Description, Job Role Evaluation and contribution towards the overall goals. Other components are either fixed or variable or incidental in nature and different loan facilities granted to staff. The major components of the Direct Financial Benefits are:

Period	Nature	Particulars
Monthly	Fixed	<ul style="list-style-type: none"> • Basic Salary • Other Allowances
	Variable	<ul style="list-style-type: none"> • Cell Phone Allowance • Fuel Facility
Annual	Fixed	<ul style="list-style-type: none"> • Leave Fare Assistance • Festival Bonuses
	Variable	<ul style="list-style-type: none"> • Performance Bonuses
Other	Incidental	<ul style="list-style-type: none"> • Spot / Cash Rewards • Travel Allowance
	Loans Facility	<ul style="list-style-type: none"> • Personal Loan • Car Loan • House Loan

All components of financial compensations are reviewed at individual / organizational level on periodic basis on grounds to align with market practices, ensure internal and external equity, cost of living adjustment, job-role change, merit increase and promotion to higher responsibility.

Indirect Financial Compensation

The compensation plan of the bank also consist a number of indirect financial compensation components for their staff through which the bank clearly differentiates its compensation plan competitiveness within the industry and amongst its competitors. The major components of the banks indirect Financial Benefits are:

- Medical Benefits
- Life Insurance Benefits
- Mortgage Insurance Benefits
- Provident Fund

- Gratuity Fund
- Paid / Unpaid leave Facility
- Education supplement benefits
- Subscription payments for newspaper, magazines and other publications related to job roles

Such benefits are also subject to review from time to time to ensure its competitiveness.

Non-Financial Compensation

In a competitive market while all banks offers market equitable financial benefits, the span of competitive edge of financial benefits tends to shorten with time. Thus the non-financial components play a vital role to attract and retain competent human resources on long term basis as it becomes very hard to imitate by any organization following others. These particular components of the bank's compensation plan had always remained the key factors of management's focus point to stress on, while devising long-term HR strategy to achieve organizational goals. Some of the key components of the same are as below:

- Professional development opportunities
- Career opportunities
- Organizational culture
- Systematic job sharing and rotation
- Career counseling and mentorship
- Periodic and systematic participatory performance review system
- Transparent succession planning process
- Professional work environment
- Employee empowerment
- Performance acknowledgement & recognition system etc.

There is no Corporate Incentive Plan or equity Program in vogue for the senior management in Bangladesh Operations.

Description of the ways in which current and future risks are taken into account in the remuneration processes.

The remuneration / compensation plan initiates with identification of individual goals / objectives on 5 major broad performance areas in line with the organization's overall goals / objective thus tying compensation components with performance ensuring internal and external equity. The 5 major broad performance areas are as below:

- Financial Objective
- Managing for Values (both in term of business initiative and Operations Objectives)
- Audit, Compliance and Control
- Personal Development and
- People Development

While assigning individual goals / objective adequate measures are ensured to cover all material risk factors under the 5 broad categories and recorded in terms of goals and objectives for the year. Thus failure to mitigate those risks in the year effects year end appraisal which has direct link with the yearly remuneration revision and award of performance bonuses for the year under question. Thus by linking risk factors with performance measurement / evaluation vis-à-vis remuneration fixation criterion; risk mitigation measures by senior management gets ensured / covered.

Description of the ways in which the bank seeks to link performance during a performance measurement period with levels of remuneration.

The major portion of senior management remuneration is governed by the fixed portion of the total

compensation package. The absence of intense variable salary component other than annual performance bonus constitutes lower risk factor overall, since fixation of performance bonus and remuneration revision falls beyond the scope of controlled function of senior management and under purview of Board of Directors based on senior managements performance review for the previous year.

The Compensation and reward plan of Bank Alfalah is governed by the compensation philosophy to remain aligned & competitive with the market and reward performance appropriately. The basic philosophy of this plan is to retain and motivate its core staff on long term basis to perform at a desired level and provide reward for the same upon performing. At the same time it also sets standards for others to have a clear understanding of what to expect from them in order to motivate them to improve their performance to the desired level.

Depending upon the performance of an individual during a year, each executive gets rated on a scale of 1 to 5 where 5 considered as the highest rating. Thus depending upon the financial performance of the bank Board of Directors approves a bonus pool and remuneration review / revision pool, which in turn gets distributed amongst executives in the form of performance bonus and increments, depending upon their individual and unit / department performance. Thus performing individuals of performing units gets justified reward as opposed to less performing individuals / units. Accordingly, senior management staffs are also getting rewarded following the process based on their performance. Thus link between remuneration and performance is established in a transparent and justifiable process.

Description of the ways in which the bank seek to adjust remuneration to take account of longer-term performance.

Bank Alfalah – Bangladesh Operation is currently not offering variable incentive plans to the likes of Corporate Incentive Plan or Equity Participation Program to its senior management staff. Thus this section is not applicable for the bank.

Description of the different forms of variable remuneration that the bank utilizes and the rationale for using these different forms.

Bank Alfalah – Bangladesh Operation is currently not offering variable incentive plans to the likes of Corporate Incentive Plan or Equity Participation Program to its senior management staff. Thus this section is not applicable for the bank.

Quantitative Disclosures:

2015
Figures in BDT

Number of meetings held by the main body overseeing remuneration during the financial year and remuneration paid to its member.	Meeting - 3 Nos. Remuneration amount not available
Number of employees having received a variable remuneration award during the financial year.	7 Nos.
Number and total amount of guaranteed bonuses awarded during the financial year.	2 Nos. 7,402,038/-
Number and total amount of sign-on awards made during the financial year.	1,600,000/-
Number and total amount of severance payments made during the financial year.	3,851,457/-
Total amount of outstanding deferred remuneration, split into cash, shares and share-linked instruments and other forms.	N/A
Total amount of deferred remuneration paid out in the financial year.	N/A

Breakdown of amount of remuneration awards for the financial year to show:	
- Fixed and variable.	57,612,962/-
- Deferred and non-deferred.	N/A
- Different forms used (cash, shares and share linked instruments, other forms).	N/A
Quantitative information about employees' exposure to implicit (eg fluctuations in the value of shares or performance units) and explicit adjustments (eg clawbacks or similar reversals or downward revaluations of awards) of deferred remuneration and retained remuneration:	N/A
Total amount of outstanding deferred remuneration and retained remuneration exposed to ex post explicit and/or implicit adjustments.	N/A
Total amount of reductions during the financial year due to ex post explicit adjustments.	N/A
Total amount of reductions during the financial year due to ex post implicit adjustments.	N/A