Bank Alfalah Limited
Bangladesh Operations
Disclosure under Pillar-III of Basel-II for the year ended December 2014

These qualitative and quantitative disclosures have been made in accordance with Bangladesh Bank vide BRPD Circular No. 10 dated March 10, 2010 and BRPD Circular No. 24 dated August 03, 2010. 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 Banks exposure to various risks.

Market Discipline Disclosures

As per Bangladesh Bank guidelines, the Bank has migrated to Basel-II framework as on 31.03.2009 under parallel reporting regime to existing BRPD Circular No. 10, dated November 24, 2002. From January 01, 2010 Basel-II regime has started into effect and the guideline on Risk Based Capital Adequacy (RBCA) has come into effect with its subsequent supplements/revisions.

Under Pillar-III of the framework, "Basel-II Disclosures" of Bank Alfalah Limited as on December 31, 2014 are as under:

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 goals of managing capital of the Bank are as follows:

- To be an appropriately capitalized institution, considering the requirements set by Bangladesh Bank.
- Maintain strong ratings and to protect the Bank against unexpected events; and
- Availability of adequate capital at a reasonable cost so as to enable the Bank to operate adequately and provide reasonable value addition for the shareholders and other stakeholders.

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 RBCA guidelines on Basel-II framework, 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.

In view of the above context, following disclosures are made by the Bank in terms of RBCA:

1. Scope of Application
2. Capital Structure
3. Capital Adequacy
4. Credit Risk
5. Equities: Disclosures for Banking Book Positions
6. Interest Rate Risk in the Banking Book (IRRBB)
7. Market Risk
8. Operational risk

1. Scope of Application

Bank Alfalah Bangladesh Operations has no subsidiaries or significant investments and Basel II is applied at the Bank level only.

2. Capital Structure

Qualitative Disclosure

Bank Alfalah Limited, Bangladesh capital structure consists of Tier-I and Tier-II capital. The regulatory capital is broadly classified into three categories - Tier-I, Tire-II and Tier-III. Tier-I capital includes paid-up equity capital, statutory reserves, other disclosed free reserves, capital reserves and innovative perpetual debt instruments (Tier-I bonds) eligible for inclusion in Tier-I capital that comply with requirement specified by Bangladesh Bank.

Elements of Tier-II capital include revaluation reserve, general provision and loss reserve, upper Tier-II instruments (upper Tier-II bonds) and subordinate debt instruments (lower Tier-III bonds) eligible for inclusion in Tier-II capital.

The use of Tier-III capital (short term subordinated debt) is limited only for part of the explicit capital charge for market risks. The Bank does not have any Tier-III capital.

As on December 31, 2014 the Bank has a paid up capital of BDT 442.06 crore. The computation of the amount of Core (Tier-I) and Supplementary (Tier-II and Tier-III) Capitals shall be subject to the following conditions:

1. Eligible Tier-II plus Tier-III capital shall not exceed total Tier-I capital.
2. Fifty percent (50%) of Asset Revaluation Reserves shall be eligible for Tier-II i.e. Supplementary Capital.
3. A minimum of about 20% of market risk needs to be supported by Tier-I capital. Supporting of Market Risk from Tier-III capital shall be limited up to a maximum of 250% of a bank's Tier-I capital that is available after meeting credit risk capital requirement.
4. Up to 50% of Revaluation Reserves for Securities shall be eligible for Supplementary Capital.
5. Subordinated debt shall be limited to a maximum of 30% of the amount of Tier-I capital and shall also include rated and listed subordinated debt instruments/bonds raised in the capital market.

Quantitative Disclosure

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

	2014 BDT	2013 BDT
a) Core capital (Tier-I)		
Fund Deposited with BB	4,420,627,471	4,423,756,326
Retained Earnings	181,923,322	(44,795,113)
	4,602,550,793	**4,378,961,213**
Deductions from Tier-1 (Core Capital)	-	-
Total Eligible Tier-I Capital	**4,602,550,793**	**4,378,961,213**
b) Supplementary capital (Tier II)		
General Provision (UC loans & OBS (Limited to 1.25% of RWA)	98,466,414	79,534,750
Revaluation Reserve for Securities up to 50%	35,075,770	13,808,686
	133,542,184	93,343,436
Deductions from Tier-2 (Core Capital)	-	-

Total Eligible Tier-II Capital	**133,542,184**	**93,343,436**
c) Additional supplementary capital (Tier III)	-	-
A. Total Eligible Capital	**4,736,092,977**	**4,472,304,649**

3. Capital Adequacy

Qualitative Disclosure

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 capital adequacy guidelines, the Bank is required to maintain a minimum CAR of 10.00% with regard to Credit Risk, Market Risk and Operational Risk. Subsequently this minimum CAR as prescribed by Bangladesh Bank vides BRPD Circular No.10 dated March 10, 2010 as follows:

Period	CAR %
January 01, 2010 to June 30, 2010	8%
July 01, 2010 to June 30, 2011	9%
July 01, 2011 to ongoing	10%

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

Quantitative Disclosure

At the close of business on December 31, 2014 in terms of aforesaid Circular, available Core Capital of the Bank was BDT 4,602,550,793 as against a minimum capital requirement of BDT 4,000,000,000 or BDT 850,621,828 (10% of RWA as per Basel-II). Supplementary Capital of the Bank was BDT 133,542,184 thus resulting in a total of BDT 4,736,092,977 thereby appearing a surplus capital of BDT 736,092,977 over and above BDT 4 billion at that date. Details are shown below:

	2014 **BDT**	**2013** **BDT**
Total assets including off-Balance Sheet items	19,385,025,434	18,383,526,249
Total risk-weighted assets (RWA)	8,507,758,283	8,875,000,975
10% of Total RWA	850,775,828	887,500,098
A. Total Eligible Capital	**4,736,092,977**	**4,472,304,649**
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]	736,092,977	472,304,649
Capital adequacy ratio	55.67%	50.39%
Amount of Regulatory Capital to meet unforeseen loss		
Amount to meet Credit Risk	712,132,524.23	775,482,386
Amount to meet Market Risk	3,419,185.23	58,273,264
Amount to meet Operational Risk.	10,445,145	53,744,448
Some additional capital over MCR maintained by the banks	736,092,976	472,304,649

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 45.36% of total assets of the Bank. The classified loan ratio was 4.69% 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 87.26% and 12.74% 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 35.21 crore as on December 31, 2014 whereas it was BDT 57.85 crore as on December 31, 2013 representing a decrease of BDT 22.64 crore.

	2014 BDT	2013 BDT
1. Cash in Hand & Balance with BB (Excluding Fcy)	762,826,019	634,957,749
2. Balance with BB (Fcy as part of Capital)	331,737,471	2,214,693,949
3. Claims on Other Banks	1,065,060,672	731,839,782
a) Balance with other banks	1,065,060,672	731,839,782
b) Money at Call & Short Notice	-	-
4. Investment (HTM)	4,185,170,528	2,395,365,362
a) Government (under lien with BB as part of Capital)	4,185,170,528	2,335,365,362
b) Qualifying (banks, etc)	-	-
c) Others	-	60,000,000
5. Loans & Advances	7,508,280,374	6,580,837,872
a) Classified	352,085,649	578,473,121
SS	-	15,068,845

DF	1,129,761	57,911,904
BL	350,955,888	505,492,372
b) Unclassified	7,156,194,725	6,002,364,751
6. Risk Weighted Assets	7,121,325,242	7,754,823,859
a) Below 100% RW	434,505,248	565,682,301
b) 100% RW	5,601,298,792	5,333,485,648
c) Above 100% RW	1,085,521,202	1,855,655,909
7. Rated Status	7,121,325,242	7,754,823,859
a) Rated Assets	4,206,591,498	4,695,668,982
b) Unrated Assets	2,914,733,744	3,059,154,876
8. Other assets (Including Fixed Assets)	591,671,316	470,724,676
A. Total Banking Book Assets (1+2+3+4+5+8)	**14,444,746,380**	**13,028,419,390**
B. Trading Book Assets		
1. FC held in Hand	2,909,897	2,696,681
2. FC held in BB & Nostro Account	156,225,712	8,551,748
3. Investment (Trading)	1,950,087,049	2,188,598,474
a) Govt. (Part of Govt. HTM, if held above the required SLR amount)	-	-
b) HFT	1,950,087,049	2,188,598,474
c) AFS (if any)	-	-
B. Total Trading Book Assets (1+2+3)	2,109,222,658	2,199,846,903
Total Assets (A+B)	**16,553,969,038**	**15,228,266,293**

4. 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-II as on March, 2009 with the standardised 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-II 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

Bank Alfalah Limited is using The Standardized Approach (TSA) of BB Basel-II 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-II Standardized Approach is in place and firmly adhered.

External Ratings

Bangladesh Bank Basel-II 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-II 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

The Bank defines collateral as the assets or rights provided to the Bank 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-II 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-II guidelines. In line with Basel-II 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

Bank Alfalah Limited 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-II 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-II requirements, the Bank recognizes only eligible collaterals as mentioned in the BB Basel-II 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, BAL'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	**2014 BDT**	**2013 BDT**
1. Funded	**17,092,544,705**	**15,394,734,234**
a) Domestic	17,092,544,705	15,394,734,234
b) Overseas	-	-
2. Non-Funded	**139,407,834**	**459,461,063**
a) Domestic	139,407,834	459,461,063
b) Overseas	-	-
3. Distribution of Risk Exposure by Claims		
Claims on Sovereigns and Central Banks	7,293,408,580	7,303,087,641
Claims on Banks and Securities Firms	2,017,631,048	1,744,602,456
Claims on Corporate (excl. Medium Enterprise loan)	658,948,226	1,017,447,939
Claims on the Retail & Small Enterprises (excl. consumer loan)	3,987,900	123,080,909
Claims secured by residential property	-	-
Other Categories:	300,936,794	672,642,469
Past due Loans / NPL	161,528,960	213,181,405
Off-Balance Sheet Items	139,407,834	459,461,063
4. Credit Risk Mitigation		
Claims Secured by Financial Collateral	399,442,606	837,451,831
Net Exposure after the Application of Haircuts.	4,250,174,545	5,091,086,554
Claims Secured by Eligible Guarantee	-	-

Maturity wise Classification of Loans and advances :

With a residual maturity of BDT

Re-payable on Demand	1,379,900,093	1,416,915,625
Not more than 3 months	1,427,290,112	1,406,239,874
Over 3 months but not more than 1 year	4,132,070,281	3,579,529,501
Over 1 year but not more than 5 years	569,019,888	178,152,873
Over 5 years	-	-
	7,508,280,374	**6,580,837,873**

Country-wise Classification of Loans and advances:

Inside Bangladesh

Conventional Banking

Current Finance	2,815,480,846	2,353,039,323
Term Finance	1,615,498,410	1,361,950,372
Own acceptance purchased	-	-
Credit Card	-	-

Staff Loan	4,834,047	10,944,321
Trust Receipts	26,438,841	381,360,222
	4,462,252,144	**4,107,294,238**
Islamic Banking		
Morabaha (LPO)	2,357,868,987	1,445,948,453
Trust Receipts	80,263,298	102,219,042
Own acceptance Purchased	49,169,806	181,266,792
Payment against documents	-	-
Morabaha Manual	40,761,848	40,761,848
Staff Morabaha	54,826,477	64,251,835
	2,582,890,416	**1,834,447,970**
Outside Bangladesh	-	-
	7,045,142,560	**5,941,742,208**
Bills purchased and discounted (Morabaha export bills) :		
Inside Bangladesh	463,137,814	639,095,665
Out side Bangladesh	-	-
	463,137,814	**639,095,665**
	7,508,280,374	**6,580,837,873**

Maturity wise Classification of Bills Purchased and discounted:

Re-payable:-		
Within 1 month	131,792,408	276,119,406
Over 1 month but less than 3 months	171,546,548	235,719,644
Over 3 months but less than 6 months	159,798,858	127,256,615
6 months or more	-	-
	463,137,814	**639,095,665**

Sector-wise Classification of loans and advances:

Sectors		
Agriculture, forestry, hunting and fishing	70,690,066	108,586,320
Automobile and transportation equipment	24,447,000	72,711,782
Chemical and pharmaceuticals	295,153,485	592,565,461
Cement	50,540,426	49,399,868
Sugar	9,289,603	28,070,717
Construction	85,445,141	59,800,087
Electronics and electrical appliances	129,608,554	64,022,000
Financial institution	446,386,422	320,833,905
Garments (Knit and woven)	-	-
Information technology and telecom	-	-
Iron and steel	1,280,994,300	1,503,279,074
Footwear and leather garments	197,453,000	199,477,000
Paper, printing and packaging	5,979,422	132,890,049
Power/electricity, gas, water, sanitary	-	
Wholesale and retail trade	562,982,409	181,649,419
Exports and imports	617,972,004	518,793,323
Transport, storage and communication	41,554,425	171,145,453
Textile, yarn and spinning	673,715,040	501,205,605
Services	3,013,000	3,806,000
Others	3,013,056,076	2,072,601,810
	7,508,280,374	**6,580,837,873**

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

Unclassified:		
Standard including staff loan	7,143,063,794	5,975,574,325
Special Mention Account (SMA)	13,130,931	26,790,427
	7,156,194,725	**6,002,364,752**
Classified:		
Substandard	-	15,068,845
Doubtful	1,129,761	57,911,904
Bad or loss	350,955,888	505,492,372
	352,085,649	**578,473,121**
Total	**7,508,280,374**	**6,580,837,873**

Maintenance of Specific Provision

Bank 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 4.73 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. 19 "Loan Classification and Provisioning" dated December 27, 2012 and BRPD Circular No. 14 "Master Circular: Loan Classification and Provisioning" dated September 24, 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.

	2014 BDT	2013 BDT
A. Gross Non Performing Assets (NPAs)		
Non Performing Assets (NPAs) to Outstanding Loans & Advances	4.69%	8.79%
B. Movement of Non Performing Assets (NPAs)		
Opening Balance	578,473,121	339,173,505
Additions	-	239,299,616
Reductions	226,387,472	-
Closing Balance	**352,085,649**	**578,473,121**
C. Movement of Specific Provisions for NPAs		
Opening Balance	392,407,643	74,790,962
Provisions made during the period	67,072,112	317,616,680
Write-off	-	-
Write-back of Excess Provisions/Prov. Reversed	19,796,355	-
Closing Balance	**439,683,400**	**392,407,642**

5. Equities: Disclosures for Banking Book Positions

Qualitative Disclosures

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

6. 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 are 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 Disclosure

Interest rate risk in banking book as of Dec 31, 2014 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	1.56			
Duration of Liabilities	0.37			
Duration Gap	1.29			
Change in Market Value of Equity (in BDT)		(200,404,724.90)	(400,809,449.80)	(601,214,174.70)

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.

7. Market Risk

Qualitative Disclosure

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-II 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.

Bank 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-II.

Methods used to measure Market risk

Bank 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.

Quantitative Disclosure	**2014**	**2013**
	BDT	**BDT**
Capital Requirements for -		
Interest Rate Risk	26,580,461	30,816,469
Equity Position Risk	-	-
Foreign Exchange Risk	7,611,391	27,456,795
Commodity Risk	-	-
	34,191,852	**58,273,264**

8. Operational Risk

Qualitative Disclosure

Operational Risk is defined 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.

Quantitative Disclosure

	2014	**2013**
	BDT	**BDT**
Capital Requirements for Operational Risk	104,451,452	53,744,448

Internal Capital Adequacy Assessment Process (ICAAP)

ICAAP is a bank's explanation of its internal capital adequacy assessment process. Pillar 2 of Basel-II capital accord links capital requirement more closely to bank's own internal evaluation of risk. Bank Alfalah Ltd firmly believes that the spirit of ICAAP lies in the implementation of advanced approaches and hence in order to obtain full benefits of ICAAP, the bank would have to conduct its ICAAP based on the advanced approaches. However, to start with, the bank had prepared its ICAAP based on 'Standardized + Stress Testing' methodology.

Stress tests are an important tool for analyzing a bank's risk profile. As part of the Basel-II implementation, Bangladesh Bank had launched the mandatory stress testing on banks from June 2010 with the objective as to assess the effect of possible unfavorable events on the bank's regulatory capital requirements, internal assessments of its capital needs and earnings. The ICAAP conducted by the bank entails a number of stress tests intended to determine the additional capital needed to ensure that the capital requirement is always complied with, even during severely distressed economic conditions.

The Bank's ICAAP includes an assessment of the capital requirement under Pillar 2 as well as bank's internal evaluation of risks for operational risk. The ICAAP conducted by Bank Alfalah not only ensures that it has sufficient capital in relation to its risk profile but adequate risk management techniques and systems are also being used and further developed by the bank.