INDOSTAR	**Risk Management Framework and Policy**

IndoStar Capital Finance Limited

Risk Management Framework and Policy

FOR INTERNAL PURPOSE ONLY

March, 2023

Risk Management Framework and Policy

Risk Management Framework and Policy	
Geographic applicability: India	
Policy Approval authority	Board of Directors
Policy Owner	Risk Management Department (RMD)
Issue Date	March, 2023

Authorities overseeing compliance of the policy
Risk Management Department (RMD)

Purpose of document
This document is intended to provide details and guidelines on Risk Management Framework

INDOSTAR	**Risk Management Framework and Policy**

Introduction:

Risk Management Framework at IndoStar Capital Finance Ltd (hereafter referred to as ICF) will have two elements and is being designed and implemented to address significant risks which will have a major impact on the Company. This framework shall provide a coherent foundation for effective management of risk such as credit risk, market risk, liquidity risk, operational risk and compliance risk.

Regulatory risk compliance: ICF will need to comply with and report on regulatory requirements on portfolio characteristics. It will also need to comply with certain risk organization and process requirements as set out by RBI and as relevant in certain cases by SEBI. These will relate both to its constitution as an NBFC and as related to the business that it is engaged in. While the overall risk management framework will need to ensure compliance and reporting on these elements, it will not be limited to meeting regulatory needs alone.

NBFC exposure guidelines
Real estate exposure guidelines
Corporate governance guidelines
Risk and Asset liability committees and reporting
ECB, FII guidelines

Overall risk management framework and guidelines: This will form the actual framework for managing risk to meet business objectives. While core elements of the management team and the Board have deep experience with the deployment of capital in different forms and in managing attendant risks, this framework seeks to provide the basis for a common understanding of risk parameters and the mechanisms to achieve them. The rest of the document seeks to meet that objective (except the section(s) on regulatory compliance).

Risk organization and roles

Overall risk management at ICF will be carried out through oversight at different levels of the organization from the Board to elements of the operating team.
The roles of the different elements of the risk organization and broad delegation of authority are as below.
Board will conduct overall oversight and delegate authority to subordinate committees
Risk Management committee (RMC) will manage overall risk within a broad risk framework which it approves through the use of subordinate committees, the Credit Committee (CC) and Asset Liability Committee (ALCO). It will engage in approval of specific transactions only at the request of the CC, especially in cases where conflicts of interest prevent the approval at the CC level.
The CC will approve exposure through Corporate Lending committee and Retail Lending committee
approve divestment (sell down) of any exposures
ensure that regulatory (RBI) requirements on portfolio concentration and sectoral exposure are met through exposure approvals

direct the management team on what it needs for smooth and timely decision making
ensure compliance with its instructions and approvals using the services of other organs such as the CLC, RLC, audit committee and other mechanisms

The ALCO will Be responsible for managing ALM risk within agreed parameters (portfolio duration gap, period by period mismatches, etc.)
Approve and manage “passive” or “treasury” investments to deploy surplus beyond “core” business
Approve funding measures by the management team and specifically the CFO to meet these objectives

Work with the CC and the management team to ensure that transactions and overall portfolio characteristics are such that financing options are feasible
Managing and reporting compliance with RBI requirements on ALM and ALCO reporting

The Board will be will be responsible for managing risk at an overall level and accountable to the shareholders for returning a risk adjusted return in line with expectations, across time horizons.
To do this, the Board will delegate authority for overall risk management to the Risk Management Committee (RMC) to ensure focused oversight and committed board level capacity for this task. The RMC which in turn will delegate authority to various subordinate elements of the risk organization and oversee their roles in risk management.
The Board will directly only perform the following roles
Delegation of authority to the RMC initially and then review of powers as necessary from time to time
Reviewing the work of the RMC once/twice a year for directional guidance if any on the risk function of the company
Reviewing conflict issues if they cannot be resolved at the RMC and are referred to it

Risk Management Committee will be responsible for managing risk at an overall level. It will be accountable to the Board for managing risk parameters within expectations across time horizons.

Composition: The RMC will comprise of 6 members: CEO, CFO, CRO, one non-executive non-independent director nominated by Indostar Capital, Mauritius, one non-executive non- independent Director nominated by BCP V Multiple Holdings Pte. Ltd. and one non- executive independent director

Meeting frequency: At least two times a year and as needed for resolving issues referred to it.

Responsibilities and authority:
Approval of delegation of authority to various subordinate elements of the risk organization including (as detailed in later sections) the Credit Committee (CC), the Asset Liability management committee (ALCO), the Chief Executive Officer (CEO) and the Chief Financial Officer and controller (CFO). From time to time it will review the performance of these organizational bodies against their mandated roles under these delegated authorities and if necessary refine the extent and nature of delegated authority to these subordinate organs of risk management.
Approval of risk framework and changes. The RMC will approve the risk framework ((i.e. principles, policies, strategies, process and controls) used by the CC and ALCO under which ICF (detailed below) will operate and under which subordinate organs of risk management will function. This will include definitions of core and supporting business activity, broad threshold levels of concentration or exposure for each type of activity or risk as it sees fit, the delegation of these decisions to the credit committee, direction to the credit committee on changes in risk guidelines from time to time, if warranted.

Review of risk management performance: The RMC will have to periodically review various metrics and MIS on risk management to satisfy itself that the company goals on risk management are being met. The crucial roles of the RMC are Forward looking course corrections on current risk parameters or guideline elements if needed
Review (retrospective) of all elements of risk guidelines and their execution for identification of future risks from internal guidelines or risk management processes
Review reports from management concerning changes in the
- factors relevant to projected strategy, business performance or capital adequacy

Approval or review of, any exposures with conflict of interest:

The RMC will have to review (and in some cases if requested by the Credit Committee, approve) Corporate Lending transactions or issues with any element of conflict of interests.

Companies/ promoters in which any of the shareholders of ICF have a material interest directly or indirectly Companies/ promoters in which any of the members of the Board or subordinate organs have material personal interests directly or indirectly Review and approval of changes in key management personnel.

This element of risk management will involve the RMC satisfying itself on the changes in personnel taking up key positions that are crucial for the company.

The Credit Committee (CC): The credit committee is empowered by the Board through the RMC, to

approve the deployment of all capital through the core business of lending to companies, in line with the risk framework, with reference to both taking on and divesting exposures

define and interpret the risk framework in approving individual transactions and in deciding portfolio composition both through incremental disbursements and divestments.

set out the guidelines, principles and approach to manage credit risks for ICF and contain a framework to identify, assess, measure, monitor and control credit risks in a timely and effective manner in retail lending.

Composition: The CC will comprise of 4 members namely independent director who shall be the Chairman, the CEO, CFO and one non-executive non- independent director nominated by BCP V Multiple Holdings Pte. Ltd.

Meeting frequency:

As when needed for approving the transactions Responsibilities and authority across products:

Approval of under-writing guidelines The CC has to ensure that Corporate Lending business is equipped with efficient and effective under-writing guidelines that are agreed and understood in the main, for use in proposing transactions to the CC for approval. This forms the basis of time- efficient, standardized and effective under- writing. The CC has to, in consultation with business management, adopt and approve a set of under-writing guidelines (refer annexure 1) that can deal with the majority of the issues in the majority of cases brought before it for approval.

For retails loans the CC will empower RLC to approve the underwriting guidelines for the retail business

Deployment of capital by approving loans: The CC has the authority to deploy capital by approving transactions brought before it by the Corporate Lending business team for approval. It has the authority and responsibility to do this by examining proposals prepared for its consideration using under-writing guidelines it has approved; and in line with RMC delegated authority to interpret and define the company’s risk framework.

Recommending changes in overall risk framework if necessary: The CC is responsible for recommending to the RMC and Board, any changes to the larger risk framework with supporting arguments, after review of the portfolio and of the external environment.

Responsibilities and authority for Corporate Lending:

Divestments of loans/ assets: The CC has a specific responsibility to implement RMC mandated risk policy in the context of divestment of assets by ensuring that

Terms of each divestment are the best terms possible to deliver value to ICF and do not adversely affect the original return assumptions on the transaction where possible, except when done for avoiding more adverse characteristics

Approvals for divestment both in the form of 1) pre-approved divestment schedules during under-writing or 2) separate divestment approvals; meet the test of incremental value addition to the portfolio characteristics

Divestments ensure optimal use and availability of capital in the context of other opportunities available at the same time, and their risk-return profiles

Divestments are in line with ALM considerations of the ALCO.
Monitoring operational risk elements: The CC is responsible for monitoring operational element of risk as part of its obligation. This means reviewing other elements of risk apart from under-writing and divestments using the findings of the Audit Committee; or ALM risks as follows:
Ensuring legal risks of loan documentation are examined by internal and external counsel; and provide adequate cover to the company
Ensuring all external partner agencies involved in all aspects of under- writing, valuation, documentation, divestments, among others, are examined for conflicts of interest in general and in each transaction and found to be non-conflicted.
Ensuring compliance of all personnel to policies on conflicts of interest, insider trading, and other regulatory and internal declaration requirements.

Identifying and reporting conflicts of interests: A key responsibility of the CC is to identify and report all conflicts of interest within its own members, or other organs of risk management and larger organization to the RC for oversight, review and approval wherever necessary. In order to execute against this responsibility:
Individual members of the CC with the conflict of interest must identify themselves and must be recused from deliberations
Similarly, individual members of the CC or other parts of the organization must identify themselves and must be recused from deliberations.

Sectoral Risk: Sectoral risk is the risk to the company due to a very high credit exposure to a particular business segment, and industry.
The Company maintains a diversified exposure in advances across various sectors and industries. The Company also lends to retail and individual customers under asset lending, and commercial / industrial funding under SME segment to maintain sectoral coverage.
The Company has a robust Credit policy in place to ensure unbiased sectoral concentration through its underwriting system, with reference to any particular sector or industry.

Sustainability (particularly, ESG (Environmental, Social and Governance) related risks
The Company is engaged in the financial services sector and hence the Company's operations have no direct impact on the environment, however, in its effort of contributing towards environment protection, the Company is engaged in supporting various organisations working in the fields of environment conservation and social activities.
Roles and Responsibilities: - The CSR Committee is responsible for implementation and monitoring of the CSR Policy in compliance with the CSR Objectives the Company.

Information Security and Cyber risk: Information security risk comprises the impacts to an organization and its stakeholders that could occur due to the threats and vulnerabilities associated with the operation and use of information systems and the environments in which those systems operate. Cyber risks are an ever-expanding area as professionals combat a continual wave of attacks, fraudsters and criminals.

Roles and Responsibilities: As per Information Security policy, the Business Functions and IT Department, with the assistance of the Management Information Security Committee (MISC) and Chief Information Security Officer (CISO), shall determine the appropriate level of controls to safeguard Company's information and assets.

AssetLiabilitymanagementcommittee(ALCO):This is another risk sub-committee accountable to the RMC, with a focus on managing the asset liability mismatches for the Company. It is responsible to the RMC for managing risks arising out Asset-liability mismatches including exposures to interest rate changes and risks from instruments used to manage duration mismatches. It would also be responsible for all deployment of capital in “treasury management”.

Composition: The ALCO comprise of the senior management of ICF (including the Chief Executive Officer)

Meeting frequency: as needed Responsibilities and authority: as per the ALCO and LCR policy

Annexure 1

Under-writing process - Corporate Loan:
The origination/relationship and structuring team will jointly propose loans/deals to the credit committee in the form a proposal /credit memo to the CC. They will include both an analysis of the proposed deal by itself and it’s impact on the portfolio as a whole.

The credit committee will examine the proposals and sanction or reject the proposal and/or specify the terms/structure under which the proposal can be approved. In the case of any exceptions or related party transactions, these will be referred to the RMC and if needed to the full board.

All under-writing risk guidelines will be subject to RBI and other regulatory boundary conditions and will also be superseded by an overall risk management framework for the portfolio. This part of the document deals with risk guidelines for under-writing specifically. The credit proposal or memo prepared by the origination and structuring teams for consideration by the credit committee will need to explicitly cover two aspects:

Details of proposed transactions (Part A)
Impact on portfolio if proposed transaction is approved (Part B)

Details of proposed transaction (Part A):
The credit memo proposing the loan to the credit committee must cover explicitly the following details:

Size of loan and percentage of ICF portfolio and net-worth that the transaction will entail
Loans need to be examined for compliance with RBI guidelines on single borrower or group exposure and if action is needed to adjust portfolio composition for compliance, the same needs to be flagged to the credit committee.

Details of any past transaction with the borrower

Any prior transactions with the prospective borrower need to be explicitly detailed especially any defaults but also any details such as puts/calls being triggered and any past actions needed to maintain cover ratio.

Credit rating and other data with a bearing on past credit behavior of the promoter and of any of the entities that are to be involved in the transaction
External rating data on any of the entities directly or indirectly involved in the transaction should be explicitly mentioned CIBIL data including any suit filed data on the promoters and entities should be reviewed explicitly. All DRT and other debt arbitration and appellate tribunal actions and data related to any entity or part of the borrower group should be explicitly mentioned. Similarly, any past or present referrals to the BIFR of any entity in the borrower group must be explicitly reviewed

SEBI and other regulatory data on defaults, legal actions and cautionary notices to any of the promoters or entities must be explicitly reviewed.

Shareholding/ownership pattern of entities that will either be borrowers, stand guarantee, offer collateral or recourse, or own a stake in any of the borrower entities, directly or indirectly; or lend substantially to the entities or do substantial business with any of these entities. This data is to be used to identify and review any potential conflicts of interests, misalignment of incentives and "leakages" that could affect risk on loan. This information must include Extent of ownership directly and through subsidiary or peer companies
All wholly owned, majority owned and minority owned subsidiaries and promoter and third-party interests/ shareholding in each
All third-party holdings of relevance in group entities.
All listed entities in the group and linkages between these and other entities; and shareholding pattern for listed entities
Extent of free-float and volumes of trading in all listed shares
Extent of lending directly and through subsidiary or peer companies with group entities
Extent of business flows between companies with ownership interests and extent of dependence on these flows
Nature of business and source of operating cash flows of all relevant entities with relevant sensitivities to risks
Primary areas/sectors of business and composition of revenues and profits from each area of business- current, historical and projected
Mapping of each business line/area/sector to entities within the borrower group
Revenue, cost and cash flow diagram for each entity in the group
Revenue and profit concentrations- by customer, related party/ inter-group flows and by entity, by product/business line, by currency (if relevant), by geography
Growth projections and dependence on key assumptions and sensitivities to risks on key assumptions
Details of cash flows of key entities (borrower, guarantor, recourse, holding company, entities whose shares or assets will serve as significant collateral) and sensitivity of cash flows to risks on different assumptions
Extent and source of non-operating income
Whether significant operating cash flows come from real estate or capital markets and how much, nature of flow of cash and income

Purpose/ end-use of loan
Will benefit which entity most in terms of operating cash flows, profits and valuation
If expansion or new venture or M&A/inorganic initiative
For expansions and new ventures, analysis of project case for expansion and sensitivities on profits, and cash flows of different assumption risks
Business: Strategic and execution risks and impact on cash and profit projections
Regulatory risks
For M&A financing/ inorganic initiatives, analysis and presentation of
Price and other transaction risks and sensitivities
Sensitivities on realizing acquisition/merger benefits
Regulatory and compliance sensitivities
Revenue expense or capital expense
Analysis of changes in expense mix and dependence on long term funds for short term needs if any
Use for acquiring land or capital market assets
Transaction risks Sensitivities influencing value realization in different entities

Promoter and hold-co analysis:

This data and analysis are to be used to specifically examine promoter and hold-co alignment of interests with respect to borrower, guarantor entity interests and performance

concentration of promoter interests and flows from holdings to determine and review relative value of different entities and hence value of collateral in form of shares of individual entities other than the hold-co

concentration of hold-co interests and flows from holdings to determine and review relative value of different entities and hence value of collateral in form of shares of individual entities other than the hold-co

Relative value to promoter and hold-co under different scenarios of direction/re- direction of revenues, costs and cash flows across different entities in particular those with borrower/guarantor role

Extent and structure of operating cash flows debt cover of all entities:

Must cover all related party flows and explicit analysis of concentration of flows and impact on debt coverage ratios

Debt servicing capacity under different scenarios- overall and for ICF after seniority: DSCR and ISCR measures at different levels and under different scenarios

Other obligations

Extent and structure of existing debt of all entities:

Must cover quantum, nature, structure of all debt of all entities linked to the transaction (borrower, guarantor, owner of borrower/guarantor)

Bank, institutional, NBFC borrowing: names of primary lenders and analysis of debt relationship

Quantum

Seniority

Overall structure of debt

Collateral provided and extent and number of charges on collaterals

Terms of debt: fixed/ floating rate, coupon, bullet, maturity/ tenor

Overall and specific encumbrance

Servicing obligations

Debt issuances

Quantum

Structure of debt issuances

Level of encumbrances

Direct servicing obligations

Structure of loan being proposed: Credit committee will need to review each of the following with a view to

Amount

Bilateral or subscription to debt issue

Hold vs sell-down proposed

Repayment terms

- principal and interest servicing
- duration of asset; and VaR at X months from disbursement
- Door-to-door term

Interest rate:

- Fixed/ floating
- Benchmarks

Put and call terms if any

Warrants and convertible terms offered: strikes and dates

Which entities will borrow/ guarantee /provide partial recourse

Total collateral/cover being offered:

- Total cover being offered
- Split of cover by type of collateral
- Sensitivities of cover to movements in each collateral and total cover sensitivity
- Land/real estate in any form with title details with current/adjacent valuation

Title of land if land directly as collateral

In case of real estate developments, nature of charge/ lien on development and its cash-flows

Escrow mechanisms

Shares of SPV

Valuations of land, developments by third party valuation agencies
Nature of charges and encumbrances on land/development
Other debt to the SPV/ project and clearances obtained from other bank and institutional lenders
 Shares of entity:
Whether operating company, target (in acquisition) company, holdco, SPV, subsidiary, peer company and relationship to borrower/guarantor/promoter entities
Listed or unlisted
For listed
Shareholding pattern
Market cap, P/E, P/B, EPS
Free float
%age of free float represented by collateral
F&O or not
VaR for trailing X months
Beta of stock
Impact cost
Warrants and other structures outstanding
For unlisted
Shareholding pattern: third party shareholders and existing valuation
Value of underlying assets
Operating cash flows and concentration of related entity flows
Existing drags, tags and ROFRS; and other poison pills
%age represented by collateral: 51%+; 26-50% or less than 26%
Existing warrants and other calls/puts on stock
Existing convertible debt
 Other assets: plant and machinery: valuation and liens/charges on each
Yield curve and ALM mismatch risks:
In light of proposed structure, risks due to interest rate changes need to be modeled and reviewed for each transaction
In light of the proposed structure and whether in-going strategy is hold to maturity or sell-down; and depending on extent of balance sheet usage, risks of sell-down need to be evaluated
In general liquidity risks for class of loan across life-cycle for sell-down is required, need to be modeled and presented for review by the credit committee
Related party elements: The credit committee will have responsibility for identifying and reporting to the Board, all potential conflicts of interest and linkages of ICF with the borrower

If the deployment decision relates to a pool of exposures or a portfolio of loans, in addition to all elements mentioned above as applicable the following may need to be examined depending on underlying:
Independent rating if available
Portfolio concentration measures
Vintage-wise delinquencies and flow through rates and resultant PD (probability of default) and LGD (loss given default) and resultant loss rates at different time horizons and hence threshold IRR and benchmark NPVs of the portfolio Insurance, escrow amounts available and recourse levels available on the portfolio under different scenarios

<u>Impact of transaction on overall portfolio:</u> Part B
Each transaction will need to be accompanied by an impact summary of the transaction if approved. This will need to cover the following aspects in detail:
Resultant total exposure of ICF to borrower and to group and compliance with RBI guidelines
Resultant exposure to real estate sector
Resultant exposure to sector of company
Resultant exposure to class of end use (M&A, expansion, new venture etc)
Resultant overall cover of portfolio with respect to real estate
Resultant overall cover of portfolio with respect to capital markets
Resultant sensitivity of cover to capital market movements: Beta of cover to capital markets
Resultant sensitivity of cover to real estate market movements: Beta of cover to real estate
Resultant duration/ modified duration of portfolio
Resultant ALM at a monthly level
Resultant %age of portfolio with interest and principal servicing and monthly and quarterly levels
Resultant debt-equity and CAR impact
Resultant exposure to class of collateral:
Unlisted stock with minority position
Unlisted stock with majority holding
Listed stock with Beta of X
Commercial real estate
Residential real estate
Undeveloped land
Plant and machinery
Measures to correct any temporary imbalances as viewed by the credit committee or board