ANNEXURE II

DISCLOSURE UNDER THE NEW CAPITAL ADEQUACY FRAMEWORK (BASEL II GUIDELINES) FOR THE YEAR ENDED 31ST MARCH 2010.

1. SCOPE OF APPLICATION

The Karnataka Bank Limited is a premier private sector bank which was incorporated on February 18th 1924 in Mangalore. The Bank does not have any subsidiary/Associate companies under its Management.

The Bank presently is not involved in insurance business. However, bank has entered in to a Joint venture agreement and holds equity investments to the extent of 15 percent in M/s Universal Sompo General Insurance Company Limited. The financials of the joint venture company are not considered with the balance sheet of the Bank. The investment in the joint venture is not deducted from the capital funds of the Bank but is assigned risk weights as an investment.

2. CAPITAL STRUCTURE

The capital structure of the Bank is as detailed below:-

(Rs. in crore)

	Particulars	No of equity Shares	Face value per share	Amount
1	Authorised Capital	200000000	10	200.00
2	Issued Capital	133999950	10	134.00
3	Subscribed Capital	133992872	10	133.99
4	Called up/Paid up Capital	133976322	10	133.98

The Bank’s shares are listed on the National Stock exchange and Bombay Stock Exchange. During the year ended March 31, 2010, the Bank undertook a Qualified Institutions Placement (QIP) of 12115564 equity shares at a price of Rs. 132.75 per share including the premium of Rs. 122.75 per share. As a consequence, the paid up share capital of the Bank has increased by Rs. 12.12 crore and the reserves of the Bank (share premium) have increased by Rs. 145.30 crore after charging issue related expenses.

During the year, the Bank has also allotted equity shares to employees under its Employee Stock Option Scheme.

Tier II capital of the Bank stood at Rs. 435.36 crores with Rs. 350.00 crores subordinated debt, as per the table below:

Date of allotment	Date of redemption	Rate of Interest	Amount (Rs in crore)
30-06-2007	30-06-2017	10.50 percent	120.50
29-03-2008	29-03-2018	10.25 percent	29.50
27-09-2008	27-09-2018	11.25 percent	200.00
TOTAL			350.00

Breakup of Capital Funds

The Tier I Capital of the Bank comprises of (Rs in crore)

1	Paid up Capital (including forfeited shares)	133.99
2	Reserves	1681.27
	Total	1815.26

The Tier II Capital of the Bank comprises of (Rs in crore)

1	Undisclosed reserves	12.45
2	General Provisions and Loss Reserves	72.91
3	Subordinated debts eligible for inclusion in Lower Tier 2 Capital	350.00
	Total	435.36

The Total eligible capital comprises of (Rs in crore)

1	Tier I Capital	1815.26
2	Tier II Capital	435.36
	Total	2250.62

An assessment of the capital requirement of the Bank is carried out through comprehensive projections of future business that takes cognizance of the strategic intent of the Bank, profitability of particular business and opportunities for growth. The proper mapping of credit, operational and market risks to this projected business growth enables assignment of capital that not only adequately covers the minimum regulatory capital requirements but also provides headroom for growth. The calibration of risk to business is enabled by a strong risk culture in the Bank aided by effective, technology based risk management systems.

A summary of the Bank's Capital requirement under Basel II for credit, market and operational risk and the capital adequacy ratio as on 31st March 2010:

(Rs in crore)

A	Capital requirement for Credit Risk	
	-Portfolios subject to Standardized approach	1437.79
	-Securitization exposures	0.00
B	Capital requirement for Market Risk	
	Standardized duration approach	101.11
	-Interest rate Risk	63.93
	-Foreign exchange risk	2.16
	-Equity Risk	35.02
C	Capital requirement for Operational Risk	
	-Basic Indicator approach	98.70
D	Total Capital requirement	1637.60
E	Total Capital Funds of the Bank	2250.62
F	Total Risk Weighted Assets	18195.47
G	Capital Adequacy Ratio of the Bank (percent)	12.37%
H	Tier I CRAR (%)	9.98%
I	Tier II CRAR (%)	2.39%

Capital Adequacy Ratio of the bank under Basel I is detailed as below

		31.03.2010	31.03.2009
i	Capital Adequacy Ratio -- Tier – I	9.56	10.65
ii	Capital Adequacy Ratio -- Tier – II	2.29	2.89
iii	Total Capital Adequacy	11.85	13.54
iv	Capital Adequacy Norms prescribed by the Reserve Bank of India	9.00	9.00
v	Amount of subordinated debt raised as Tier II capital (Rs in crore)	350.00	350.00

3. RISK MANAGEMENT: OBJECTIVES AND ORGANIZATION STRUCTURE

The various risks the Bank is expored to during the course of the business development are identified, measured, controlled, monitored and reported effectively. The key components of the Bank's risk management rely on the risk governance architecture, comprehensive processes and internal control mechanism. The Bank's risk governance architecture focuses attention on key areas of risk such as credit, market and operational risk and quantification of these risks wherever possible for effective and continuous monitoring.

a. Objectives and Policies

The Bank's risk management processes are guided by well-defined policies appropriate for various risk categories, independent risk oversight and periodic monitoring through the sub-committees of the Board of Directors. The Bank has a well documented Board approved 'Risk Management Policy' in place. The Board sets the overall risk appetite and philosophy for the Bank. The Board of Directors, the Integrated Risk Management Committee and the Audit Committee of the Board review various aspects of risk arising from the businesses of the Bank.

b. Structure and Organization

The Bank has a risk management system that is centralized with a three track committee approach. The committees are Credit Policy Committee (CPC), Asset Liability Management Committee (ALCO) and Operational Risk Management Committee (ORMC). An Integrated Risk Management Committee (IRMC) evaluates the overall risk factors faced by the bank and directly reports to the Board of directors.

Credit Policy Committee deals with credit policies and procedures, Asset Liability Management Committee deals with Asset Liability Management (ALM) and Investment Policy of the Bank and Operational Risk Management Committee formulates policies and procedures for managing operational risk.

4. CREDIT RISK MANAGEMENT

Bank has developed online comprehensive risk rating system for all borrower accounts where the aggregate fund based exposures is Rs. 25.00 lakh and above or aggregate non-fund based exposure of Rs.200 lakhs and above irrespective of the amount of fund based exposure. The rating serves as a single point indicator of diverse risk factors of counter-party and for taking credit decisions. The risk rating system is drawn up in a structured manner, incorporating different factors such as borrower specific characteristics, industry specific characteristics etc. Bank also undertakes periodic validation exercise of its rating models and also conducts migration and default rate analysis to test robustness of its rating models. Presently the borrowers have been rated under 10 different categories as detailed below.

Symbols	Risk Level	Description of the Risks
KB1	Minimal	Strong Balance Sheet and excellent asset quality. Excellent management with depth.
KB2	Lowest	Good asset quality and liquidity with stable Balance Sheet. Probability of serious financial deterioration is minimal.
KB3	Lower	Average asset quality and liquidity. Satisfactory Balance Sheet performance and profitability. Vulnerability to default is remote
KB4	Low	Acceptable asset quality with marginally fluctuating earnings. Slight vulnerability to default.
KB5	Moderate	Acceptable asset quality but highly leveraged and fluctuating earnings. Inadequate capacity to sustain major setbacks.
KB6	Average	Watch list credit. Borrower's performance has not met expectations.
KB7	High	Marginally acceptable business credit with some potential weakness. Generally un-desirable business constituting an undue and unwarranted credit risk.
KB8	Very High	Unacceptable business credit. Normal recovery of debt is in doubt. The quality of the asset has deteriorated but not to the point of justifying a substandard classification
KB9	Sub Standard	Collection of debt in full improbable. The quality of the asset is substandard.
KB10	Doubtful/Loss (Critical)	Expected total loss. Cannot be classified as active assets of the Bank. Partial recoveries may occur in future. Loss asset.

While "KB4" is considered as the entry-level grade, "KB8" is treated as the exit grade.

The rating wise distribution of credit Exposure as on 31st March 2010 is detailed as below.

(Rs in crore)

Symbol	Risk Level	Current year		Previous year	
		Gross Advances	% to Total Gross Advances	Gross Advances	% to Total Gross Advances
KB1 *	Minimal	2515.14	17.05	2219.25	18.31
KB2	Lowest	3252.25	22.05	2998.20	24.73
KB3	Lower	2231.28	15.13	1380.47	11.39
KB4	Low	2616.13	17.73	2556.72	21.09
KB5	Moderate	875.31	5.93	678.22	5.59
KB6	Average	184.78	1.25	86.79	0.72
KB7	High	218.74	1.48	105.47	0.87
KB8	Very High	68.85	0.47	19.97	0.16
KB9	Sub Standard	151.14	1.02	97.98	0.81
KB10	Doubtful/Loss	398.49	2.70	345.22	2.85
	Unrated	2239.56	15.19	1634.68	13.48
	Total	14751.67	100.00	12122.97	100.00

* Includes Gold Loan, Loans against Deposits and Staff Loans

The bank has formulated a comprehensive Loan Policy by incorporating various parameters and prudential limits to manage and control default, transaction and intrinsic/concentration risk. The credit exposures are taken after subjecting the proposals to analysis of various risk factors such as financial risk, industry risk, management risk, business risk, transaction risk etc.

The bank analyses the migration of borrowers in various risk rating categories to gauge the quality of the loan portfolio. In addition to the above, the bank also conducts periodical review of the loan assets to ascertain conduct of the accounts. The bank conducts periodical Credit Audit and Stock Audit of large credit exposures to limit the magnitude of credit risk and interest rate risk.

Credit sanction and related processes

1. Know Your Customer is a leading principle for all activities.
2. Sound credit approval process with well laid credit-granting criteria is in place.
3. The acceptability of credit exposure is primarily based on the sustainability and adequacy of borrower's normal business operations and not based solely on the availability of security.
4. Portfolio level risk analysis and reporting to ensure optimal spread of risk across various rating classes to prevent undue risk concentration across any particular industry segments and monitor credit risk migration.
5. Sector specific studies are periodically undertaken to highlight risk and opportunities in those sectors.
6. Rating linked exposure norms have been adopted by the Bank.
7. Industry-wise exposure ceilings are based on the industry performance, prospects and the competitiveness of the sector.
8. Separate risk limits are set out for credit portfolios like advances to NBFC and unsecured loans that require special monitoring.

Review and Monitoring

1. All credit exposures, once approved, are monitored and reviewed periodically against the approved limits. Borrowers with lower credit rating are subject to more frequent reviews.
2. Credit monitoring involves independent review of credit risk assessment, compliance with internal policies of the Bank and with the regulatory framework, compliance of sanction terms and conditions and effectiveness of loan administration.

3. Customers with emerging credit problems are identified early and classified accordingly. Remedial action is initiated promptly to minimize the potential loss to the Bank.

Concentration Risk

The Bank controls concentration risk by means of appropriate structural limits and borrower limits based on creditworthiness. These include:

Large exposures to individual clients or group

The Bank has individual borrower-wise exposure ceilings based on the internal rating of the borrower as well as group-wise borrowing limits. The Bank monitors the level of credit risk (Low/Moderate/High/Very High) and direction of change in credit risk (increasing /decreasing/ stable) at the portfolio level based on the following six parameters that capture concentration risk.

1. Highest geographic concentration in a region.
2. Exposure to Top 20 accounts as a percentage of Credit Risk Exposure (CRE).
3. Percentage of term loans with residual maturity more than 3 years to total loans.
4. Percentage of unsecured loans to total loan and advances.
5. Number of single borrower exposures exceeding 15percent of capital funds.
6. Number of group exposures exceeding 40 percent of capital funds.

a) Geographic Concentration (Rs in crores)

Sl No	State/Union Territory	No of Branches	Total Gross Loans and Advances	percent to total Loans and Advances
1	Andhra Pradesh	33	1374.75	9.32
2	Assam Bihar	1	17.96	0.12
3	Chandigarh	1	1.66	0.01
4	Chhattisgarh	1	210.30	1.43
5	Delhi	4	104.71	0.71
6	Goa	17	1528.43	10.36
7	Gujarat	5	66.82	0.45
8	Haryana	5	294.44	2.00
9	Jharkhand	4	474.27	3.22
10	Karnataka	2	9.95	0.07
11	Kerala	281	5035.95	34.14
12	Madhya Pradesh	11	115.24	0.78
13	Maharashtra	3	79.02	0.54
14	Orissa	34	2622.96	17.78
15	Pondicherry	3	310.11	2.10
16	Punjab	1	12.13	0.08
17	Rajasthan	4	190.35	1.29
18	Tamilnadu	3	363.83	2.47
19	Uttar Pradesh	32	1254.76	8.51
20	Uttarakhand	9	209.20	1.42
21	West Bengal	2	11.20	0.08
22		8	463.64	3.14
	TOTAL GROSS ADVANCE	464	14751.67	100.00

b) Other Exposures

(Rs in crore)

Sl No	Details of the Exposure	No of Accounts	Total Gross Loans and Advances	percent to total Loans and Advances
1	Exposure to Top 20 accounts	20	3144.22	21.31%
2	Term loan with residual maturity of more than 3 years	54566	5425.27	36.78%
3	Unsecured loan	24788	1103.88	7.49%
4	Individual exposure exceeding 15% of capital funds	1	192.85	1.31%
5	Group exposure exceeding 40% of capital funds	0	0	0

While determining level and direction of credit risk, parameters like percentage of low- risk credit (investment grade and above) to credit risk exposure and migration from investment to non-investment grade (quantum as percentage of credit risk exposure) are also considered. The Bank also monitors the rating-wise distribution of its borrowers.

Exposure to Industries

Industry analysis plays an important part in assessing the concentration risk within the loan portfolio. Particular attention is given to industry sectors where the Bank believes that there is a high degree of risk or potential for volatility in the future. The Bank has fixed internal limits for aggregate commitments to different sectors so that the exposures are evenly spread over various sectors.

The credit policy deals with short term as well as long term approach to credit risk management. The policy of the bank embodies in itself the areas of risk identification, risk measurement, risk grading techniques, reporting and risk control systems /mitigation techniques, documentation practice and the system for management of loans.

Disclosure for portfolios subject to the standardized approach

Large corporate borrowers and Public Sector Enterprises are being encouraged to solicit ratings from approved external rating agencies and wherever such ratings are available the bank will use the same in calculation of risk weighted assets. Bank has approved 4 domestic credit rating agencies identified by RBI i.e CRISIL, CARE, FITCH India and ICRA. The ratings available in public domain are mapped according to risk profile and specific risk characteristics of each rating grade of respective agencies as envisaged in RBI guidelines.

The Corporate exposure after risk mitigation (subject to the standardized Approach) in different risk buckets are as under:

(Rs in crore)

Sl No	Risk weight	Exposure Outstanding
1	Below 100%	388.89
2	100%	5619.65
3	More than 100%	965.58
	Total	6974.12

Credit Risk Mitigation: Disclosures for Standardized Approach

As stipulated by the RBI 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 Base II guidelines.

Types of eligible financial collateral / Guarantors:

The Bank recognizes only specified types of financial collateral and guarantees (counter-guarantors) for providing capital relief in line with Basel II guidelines on credit risk mitigation.

This includes cash, Bank own deposits, gold (including bullion and jewellery, subject to collateralized jewellery being notionally converted/benchmarked to 99.99 percent purity), securities issued by the Central and State Governments, Kisan Vikas Patra, National Savings certificates, life insurance policies with a declared surrender value which is regulated by IRDA, certain debt securities rated by a recognized credit rating agency, certain debt securities not rated but issued by Banks and listed on a recognized exchange and are classified as senior debt, certain mutual fund units where daily Net Assets Value (NAV) is available in public domain.

In addition to the above, in the case of NPA accounts, the following collaterals are considered, as stipulated by the RBI under Basel II guidelines:

(i) Land and building which are valued by an expert valuer and where the valuation is not more than three years old and (ii) Plant and machinery in good working condition at a value not higher than the depreciated value as reflected in the audited balance sheet of the borrower, which is not older than eighteen months.

Eligible Guarantors (counter-guarantors):

Credit protection given by the following entities will be recognized:

(i) Sovereigns, sovereign entities (including BIS, IMF, European Central Bank and European Community as well as those MDBs, ECGC and CGTSI), banks and primary dealers with a lower risk weight than the counterparty;

(ii) Other entities rated AA (-) or better. This would include guarantee cover provided by parent, subsidiary and affiliate companies when they have a lower risk weight than the obligor. The rating of the guarantor should be an entity rating which has factored in all the liabilities and commitments (including guarantees) of the entity.

The extent of total credit exposure (under the standardized approach) covered by eligible financial collaterals after application of haircuts is as under:

(Rs in crore)

Eligible financial collaterals after haircuts	1446.80
Eligible guarantees	409.57

Definition of Non-Performing Assets

Any amount due to the bank under any credit facility is overdue if it is not paid on the due date fixed by the bank. A non performing asset (NPA) is a loan or an advance where;

i. Interest and/or instalment of principal remain overdue for a period of more than 90 days in respect of a term loan,

ii. The account remains 'out of order' as indicated at paragraph 2.2 below, in respect of an Overdraft/Cash Credit (OD / CC),

iii. The bill remains overdue for a period of more than 90 days in the case of bills purchased and discounted,

iv. The instalment of principal or interest thereon remains overdue for two crop seasons for short duration crops,

v. The instalment of principal or interest thereon remains overdue for one crop season for long duration crops,

vi. The amount of liquidity facility remains outstanding for more than 90 days, in respect of a securitisation transaction undertaken in terms of guidelines on securitisation dated February 1, 2006.

vii. In respect of derivative transactions, the overdue receivables representing positive mark-to-market value of a derivative contract, if these remain unpaid for a period of 90 days from the specified due date for payment.

A.Total gross credit exposure including geographic distribution of exposure (Rs in crore)

	Domestic	Overseas	Total
Fund Based	14751.67	0.00	14751.67
Non Fund based	2227.59	0.00	2227.59
Total	16979.26	0.00	16979.26

B. Distribution of Credit Exposure by Industry/Sectors (Rs in crore)

Sl No	INDUSTRY CLASSIFICATION	FUND BASED	NON FUNDED
1	Coal & Mining	44.06	15.06
2	Iron & Steel	257.44	74.03
3	Metal & Metal Products	37.47	9.47
4	Other Engineering	278.23	135.78
5	Electronics	33.05	1.17
6	Cotton Textile	503.96	83.91
7	Jute Textile	4.36	0.00
8	Other Textile	518.23	40.36
9	Tea Industry	38.37	0.30
10	Khandasari & Sugar	26.31	0.02
11	Vegetable Oil	6.49	0.00
12	Tobacco & Tobacco Products	0.89	0.00
13	Paper & Paper Products	107.32	6.89
14	Rubber & Rubber Products	8.67	13.77
15	Chemicals & Dyes	50.15	9.42
16	Drugs & Pharmaceuticals	65.85	13.22
17	Cement & Cement Products	202.47	2.07
18	Leather & Leather Products	21.41	4.41
19	Petroleum Products	13.60	0.85
20	Food Processing	70.24	5.01
21	Gems & Jewellery	555.91	46.62
22	Automobiles	117.92	10.18
23	Computer Software & Hardware	23.84	14.05
24	Infrastructure Advances	2110.31	451.30
25	Wood Based Industry	48.92	48.35
26	Plastic & Plastic Products	115.18	15.50
27	All Other Industries	232.39	104.32
	Gross Industrial Advances	5493.04	1106.06

The details of the Industry/sectors wherein the bank's exposure in the related Industry/sectors has exceeded the 5 percent of total gross credit exposure as detailed here below.

Sl No	Industry / Sectors Classification	Percentage of the total Credit Exposure
1	Infrastructure advances	14.31%

C. Residual Contractual Maturity breakdown of Assets/Liabilities (Rs in crore)

	1 day	2 to 7 days	8 to 14 days	15-28 Days	29 Days to 3 Months	Over 3 Months to 6 Months	Over 6 Months to 12 Months	Over 1 Year to 3 years	Over 3 Years to 5 Years	Over 5 Years	Total
Loans & Advances	209.67	309.91	347.98	319.78	1624.24	1493.93	2073.35	3542.73	3126.18	1387.92	14435.69
Investments	306.20	138.94	0.00	0.00	188.54	104.06	46.89	910.05	902.13	7395.23	9992.04
Deposits	460.82	491.29	541.59	506.35	2032.83	2916.60	4272.45	5434.44	6842.93	231.35	23730.65
Borrowings	149.85	0.00	0.00	0.00	27.81	63.68	50.15	50.15	0.00	0.00	341.64
Foreign Currency Assets	40.49	370.85	127.46	89.12	1838.25	602.16	659.73	27.50	0.00	0.00	3755.56
Foreign Currency Liabilities	39.70	377.72	79.58	42.72	1808.41	628.93	717.85	46.45	12.20	0.10	3753.66

D. Movement of NPAs and Provision for NPAs

(Rs in crore)

		31.03.2010	31.03.2009
A	Amount of NPA's (Gross)	549.64	443.20
	-Substandard	151.14	97.98
	-Doubtful 1	194.87	102.81
	-Doubtful 2	95.71	62.12
	-Doubtful 3	53.02	94.75
	-Loss	54.90	85.54
B	Net NPAs	188.61	116.10
C	NPA Ratios		
	- Gross NPAs to Gross Advances	3.73	3.66
	- Net NPAs to net Advances	1.31	0.98
D	Movement of NPAs (Gross)		
	a) Opening Balance	443.20	379.57
	b) Additions during the year	300.28	162.44
	Sub Total (i)	743.48	542.01
	Less :		
	a) Upgradations	49.80	19.23
	b) Recoveries (excluding recoveries made in upgraded accounts)	67.91	71.18
	c) Write Off	76.13	8.40
	Sub Total (ii)	193.84	98.81
	Closing Balance	549.64	443.20

E	Movement of Net NPAs		
	a) Opening Balance	116.10	106.48
	b) Additions during the year	202.03	93.39
		318.13	199.87
	c) Reductions during the year	129.52	83.77
	d) Closing Balance	188.61	116.10
F	Movement of provisions for NPAs		
	a) Opening balance	301.23	247.04
	b) Provisions made during the year	81.00	47.00
	c) Write off/write back of excess provisions	(76.62)	7.19
	d) Closing balance	305.61	301.23
	Movement of Floating Provisions		
	a) Opening Balance	11.69	13.00
	b) The quantum of floating provisions made during the year	0.00	0.00
	c) Purpose and Amount of draw down made during the year	1.31	1.31
	d) Closing balance	10.38	11.69

E. Non Performing Investments and movement of provision for depreciation on Investments

(Rs in crore)

		31.03.2010	31.03.2009
A	Amount of Non performing Investments	0.00	0.00
B	Amount of Provision held for Non performing Investments	0.00	0.00
C	Movement of provisions for depreciation on Investments		
	a) Opening balance	47.83	44.31
	b) Add: Provisions made during the year	0.00	33.35
	c) Less: Write off/write back of excess provisions	18.22	29.83
	d) Closing balance	29.61	47.83

5. MARKET RISK & LIQUIDITY RISK

The objective of investment policy is to assess and minimize risks associated with treasury operations by extensive use of various risk management tools. Broadly, it encompasses Policy prescriptions for managing systemic risk, credit risk, market risk, operational risk and liquidity risk in treasury operations.

For market risk arising out of various products in treasury and its business activities, the bank has set regulatory/ internal limits and ensures the adherence thereof. Migration of ratings is tracked regularly. Limits for exposures to counter-parties, industries and countries are monitored and the risks are controlled through Stop Loss Limits, Overnight limit, Daylight limit, Aggregate Gap limit, Individual gap limit, Value at Risk (VaR) limit for Forex, Inter-Bank dealing and investment limits etc.

For the Market Risk Management the bank has a Mid Office. The functions of Mid Office are handled by Integrated Risk Management Department.

The Board, IRMC & ALCO oversee the market risk management of the bank, procedures thereof, implementing risk management guidelines issued by regulator, best risk management practices followed globally and ensure that internal parameters, procedures, practices/policies and risk management prudential limits are adhered to.

The policies for hedging and/or mitigating risk and strategies and processes for monitoring the continuing effectiveness of hedges/mitigates are discussed in ALCO and based on views taken by / mandates of ALCO, hedge deals are undertaken.

Liquidity risk of the bank is assessed through daily gap analysis for maturity mismatch based on residual maturity in different time buckets as well as various liquidity ratios and management of the same is done within the prudential limits fixed thereon. Advance techniques such as Stress testing, simulation, sensitivity analysis etc. are conducted on regular intervals to draw the contingency funding plan under different liquidity scenarios.

Market Risk in Trading Book

Bank has adopted the Standardized Duration Approach as prescribed by RBI for computation of capital charge for market risk and is already fully compliant with the guidelines. Bank is now preparing itself for the Advanced Approach based on a Value at Risk (VaR) model, which is under implementation.

The capital requirements for market risk are as under: (Rs in crore)

Sl No	Risk Category	Capital Charge
I	Interest Rate (a+b)	63.93
a	General Market Risk (i to iv) Net	46.46
i	Positions (parallel shift) Horizontal	45.88
ii	disallowance (Curvature) Vertical	0.00
iii	disallowance (basis) Options	0.58
iv		0.00
	Specific Risk	
b		17.47
	Equity (a+b)	
II	General Market Risk	35.02
a	Specific Risk	15.46
b		19.56
	Foreign Exchange, Gold and Derivatives	
III		2.16
IV	Total Capital Charge for market Risk (I+II+III)	101.11

6. INTEREST RATE RISK IN THE BANKING BOOK (IRRBB)

Interest rate risk is managed through gap analysis and duration gap analysis. Prudential limits have been fixed for impact on net Interest Income (NII), Net Interest margin (NIM), Minimum ROA.

The economic value i.e. impact on the capital fund due to change in interest rate by 200 bps on the economic value is assessed on regular intervals through duration gap method. As a prudential measure, a limit has been fixed for net duration gap of the assets and liabilities and the same is monitored at regular intervals.

7. OPERATIONAL RISK

Strategies and Processes

Bank has initiated several measures to manage operational risk through identification, assessment and monitoring. A framework has been laid to capture loss data which can be mapped to operational risk events to measure the impact quantitatively. Bank has put in place a hierarchical structure to effectively manage operational risk through the formation of internal committee viz., Operational Risk Management Committee (ORMC).

Scope and Nature of Operational Risk Reporting and Measurement Systems

A systematic process for reporting risk events, loss events, "near misses" and non-compliance issues relating to operational risks have been developed and implemented. The information gathered shall be used to develop triggers to initiate corrective actions to improve controls. All critical risks and potential loss events are reported to the Senior Management/ORMC/IRMC as appropriate for their directions and suggestions.

An Operational Risk Management Policy approved by the Risk Management Committee of the Board details the framework for hedging and/or mitigating operational risk in the Bank. As per the policy, all new products are being vetted by the New Product Approval Committee to identify and assess potential operational risks involved and suggest control measures to mitigate the risks.

Approach for Operational Risk Capital Assessment

As per the RBI guidelines, the Bank has adopted Basic Indicator Approach for computing capital charge for Operational Risk. Steps have been initiated to migrate to the Advanced Measurement Approach.

8. COUNTRY RISK

The Bank has put in place a risk monitoring system for the management of country risk. The Bank uses the Nine-category classification i.e. insignificant, low, moderately low, moderate, moderately high, high, very high, restricted and off-credit. The ratings of countries are being undertaken at monthly intervals or at more frequent intervals if the situation so warrant i.e. in case of a significant change in the condition of a country involving sharp deterioration of its ratings. Exposure to a country includes all credit-related lending, trading and investment activities, whether cross border or locally funded. The Bank has set up exposure limits for each risk category as also per country exposure limits and the exposure limits are monitored at weekly intervals except for those on high, very high categories through approval from appropriate authorities at the transaction level.