

BASEL II PILLAR 3 DISCLOSURES - 31st MARCH 2009

1. Scope of application

ING Vysya Bank is the controlling entity for the group, which includes its wholly owned subsidiary ING Vysya Financial services Limited (IVFSL). IVFSL is engaged in touch point verification for liability products on behalf of the Bank. The consolidation with the subsidiary ING Vysya Financial Services Limited is as per Accounting Standard 21 (AS-21). While computing the consolidated Bank's Capital to Risk Weighted Assets Ratio (CRAR), the Bank's investment in the equity capital of the wholly owned subsidiary is deducted 50% from Tier 1 capital and 50% from Tier 2 capital. The subsidiary of the Bank is not required to maintain any regulatory capital. The Bank has no interest in any insurance entity.

2. Capital Structure

The authorized equity share capital of the Bank is Rs.350 Crore consisting of 35 Crore equity shares of Rs.10/- each. As of March 2009, the issued and subscribed capital stood at Rs.102.93 Crore consisting of 10.29 Crore of equity shares of Rs.10/- each. The paid up share capital is Rs.102.60 Crore consisting of 10.26 Crore equity shares of Rs. 10/- each. The equity share capital of the Bank is as per the provisions of the Companies Act, 1956 and any other applicable laws or regulations.

The debt capital of the Bank includes perpetual debt that qualifies as Tier 1 capital and subordinated and upper tier 2 debt that qualifies for inclusion as Tier 2 capital. The tier 1 perpetual bonds are non-cumulative and perpetual in nature and carry a call option after 10 years with an interest step up of 100 bps. The interest on these bonds is payable quarterly. The Upper tier 2 bonds are cumulative in nature with an original maturity of 15 years and a call option after 10 years. There is an interest step up option after 10 years of 100 bps. The interest on these bonds is payable quarterly. The Lower tier 2 bonds are cumulative and have an original maturity between 9-10 years. The interest on these bonds is payable annually.

The repayment of principal and payment of interest on all the types of bonds mentioned above are as per the RBI regulations issued in this regard.

Capital Funds

(Rs. in Crore)

Tier I Capital	1,516.32
Tier II Capital	1,046.09
Total Capital Funds	2,562.41
Tier I Capital	
Paid-up Capital	102.60
Reserves and Surplus	1,476.94
Innovative Perpetual Debt Instruments	94.71
Total Tier I Capital (Unadjusted)	1,674.25
Deductions	
Investments in Subsidiaries	1.05
Deferred Tax Asset	147.87
Other Intangible Assets	9.01
Total Deductions	157.93

Total Tier I Capital (Adjusted)	1,516.32
Tier II Capital	
Upper Tier II Bonds	322.14
Subordinated Debt eligible for Lower II	560.00
Revaluation Reserves	48.95
General Provisions and loss Reserves	105.93
Others	10.12
Total Tier II Capital (Unadjusted)	1,047.14
Deductions	
Investments in Subsidiaries	1.05
Total Deductions :	1.05
Total Tier II Capital (Adjusted)	1,046.09

Debt capital instruments eligible for inclusion under Tier-1 and Tier-2 capital

(Rs . in

Crore)

	Tier 1	Upper Tier 2	Lower Tier 2
Total amount outstanding as at 31 March 2009 – INR and Foreign currency	108.01 (JPY 2.09 bln)	325.73 (JPY 6.31 bln)	600.00
Amount raised during the year – INR and Foreign currency	108.01 (JPY 2.09 bln)	199.82 (JPY 3.66 bln)	210.00
Amount eligible to be reckoned as capital funds - INR	94.71	322.14	560.00

Note: FCY amounts are reported in INR at the fx rate as at 31 March 2009.

3. Capital adequacy

The Capital adequacy assessment process of the Bank is intended to ensure that adequate level of capital and an optimum mix of the different components of capital is maintained by the Bank to support its strategy. This is integrated with the Bank's annual planning process that takes into consideration the growth assumptions across business segments and mapping of the relevant risk weights to this projected growth so that adequate capital is maintained to cover the minimum regulatory requirement and a reasonable cushion over the regulatory minimum.

Capital is actively managed at an appropriate level of frequency and regulatory ratios are a key factor in the Bank's budgeting and planning process with updates of expected ratios reviewed regularly during the year by Asset and Liability Committee (ALCO). The Bank's ALCO has set internal triggers and target ranges for capital management, and oversees adherence with these on an ongoing basis. The Board also oversees the capital adequacy of the Bank on a quarterly basis.

Summary of the Bank's capital requirement as at 31 March 2009 is presented below:

		Amount (Rs. in Crore)
A	Capital requirements for Credit Risk	
	Portfolios subject to standardized approach	1,792.30

	Securitization exposures	-
B	Capital requirements for Market Risk	
	Standardized duration approach	77.61
	Interest rate risk	67.56
	Foreign exchange risk (including gold)	9.00
	Equity risk	1.05
C	Capital requirements for Operational Risk	
	Basic Indicator approach	110.04
	Capital Adequacy Ratio of the Bank	11.65%
	Tier 1 CRAR	7.00%

4. Credit risk – General disclosures

Credit risk management – Policy framework

For the identification, measurement, mitigation, monitoring and governance of Credit Risk, the Bank has laid down various Policies like Credit Risk Policy, Country Risk Policy, Counterparty Risk Policy, Customer Appropriateness and Suitability Policy, and Break Clause Policy. Other documents related to the New Capital Adequacy Framework implementation in the Bank like Stress Testing Policy, ICAAP Policy, Credit Risk Mitigation and Collateral Management Policy have also been laid down. The policies generally define

- Exposure Norms,
- Underwriting standards,
- Regulatory requirements, and
- Negative list and restricted exposures.

These policies are reviewed annually or more frequently if required. Exhaustive Credit Risk manuals and guidelines detailing the mode of implementation of the policies have also been put into practice.

Credit risk management – Structural framework

Risk Management & Review Committee of the Board (RMRC) is responsible for managing Credit Risk function, among others, and meets at least once a quarter.

Credit Risk Management Department (CRMD), headed by Chief Risk Officer (CRO), manages this function at the departmental level, both at Corporate Office and Regional levels. The CRO is assisted by senior executives dealing with credit risk of Wholesale assets, Retail assets and Consumer Finance portfolio, to ensure that growth in business is consistent with the internal risk appetite of the Bank and the credit quality of the portfolio is maintained at all times. Specialized Credit Risk Officers handle risk areas of Counterparty Risk, Country Risk, etc.

The organization structure further consists of:

- Credit Policy Committee, reporting to RMRC, which is involved in formulating all relevant policy guidelines and procedures, and for immediate action on RBI guidelines on credit related matters;
- Board Credit Committee, Executive Credit Committee, Zonal Credit Committee, and other executives at Corporate Office, Zonal Offices and Regional Offices, who have delegated credit approval power, as per well-defined guidelines;

- Operations Department to assure high standards of loan documentation, security creation and compliance with pre-disbursal terms and conditions;
- Asset Recovery Committees and Loan Review Department, which track delinquencies, identify ‘Watch List’ accounts, and give guidance on remedial management;
- Collections Department and Special Loans Management Group (SLMG), which is involved in recovery and management of delinquent accounts including enforcement of securities, legal action through Debt Recovery Tribunal (DRT) or other processes, etc. SLMG also computes the loan loss provisions as per regulatory requirements;
- Credit Audit Department, which performs the on-site audit of loans.

Credit risk management models / methods / processes

The Credit Risk Policy is a business oriented statement, within the purview of regulatory requirements. It is one of the core Credit Risk Management documents, and is reviewed at least once in a financial year, or more frequently if necessitated by the changing business environment. The policy describes what constitutes an “Acceptable Borrower / Facility” for the Bank. It also adheres to assessing financial requirements of the borrower, and specifies the exposure and the product lending norms. The exposure norms- prudential, industry, sector, etc., are also outlined in this document. The policy also specifies the norms relating to review / renewal of loans, conducting of sample review of credit approvals by higher authorities, conducting of portfolio review and review of irregular / stressed accounts. In addition, there are ‘Restricted Lists’ of industries to which either exposures should not be taken or taken selectively by the Bank. The ‘Negative Lists’ of industries / activities to which Bank ensures that exposures are not taken are in areas which are not in line with the Risk Appetite statement of the Bank.

The Bank follows the below mentioned principles to manage credit risk:

Standard appraisal and underwriting standards for approval of credit exposures is followed. Different rating models, depending upon the type of borrower and size of exposure, are prescribed. For corporates, commodity traders, banks & financial institutions, etc., appropriate Basel Compliant Rating Models (developed originally by ING) are followed. For emerging corporate, SME and certain types of agriculture exposures, an internally developed rating model is in place. Basel Compliant models for these exposures are under development. Consumer assets and certain templated products under SME are put through score card based selection methods.

Credit policy prescribes exposure and tenor caps based on risk rating of the borrower. Individual and group exposure norms, as per the ‘Prudential Norms ’ of RBI are followed. These guidelines ensure that there is no credit concentration on any individual corporate or group. Apart from this, a Risk-grid has been established, where individual exposure limits and tenors are capped based on risk rating of the company/borrower. To ensure dispersal of credit risk across different industries / segments, the Bank has prescribed specific ceilings on those industries where it has exposures.

There is emphasis on efficient credit administration, comprising of obtaining proper legal documentation, putting through day-to-day transactions, periodical unit visits and security verification, monitoring & follow-up and recovery.

Country risk, counterparty risk are reviewed by specialized desks and deviations from established procedures or limits are reviewed on a regular basis by various Committees like Executive Credit Committee (ECC), RMRC, etc.

Credit Audit is conducted at various offices which act as dispensation points / approval authorities in addition to vertical audit of various credit products. Risk based audit of branches also addresses credit risk aspects at the time of audit of branches / offices. In addition to this, risk department visits branches and conducts sample reviews of credits approved at the branch / business unit level for better credit administration.

As a general principle, the Credit Risk Policy stipulates churning of 5% of accounts on a Year-on-Year basis.

Stress testing and scenario analysis

A detailed Stress Testing framework and a process of stress testing is already in place as elaborated in our “Stress Testing Policy”. The Policy applicable to the Bank is in accordance with the RBI circular DBOD.No.BP.BC.101/21.04.103/2006-07 on stress testing. Obligor Risk, Portfolio Risk, Concentration Risk, Exposure Risk, Environmental Risk, Model Risk and Analytics risks have been incorporated in this document.

As a part of this exercise, “Capital Assessment Model” for Credit Risk function (for Basel II ‘Standardized Approach’) is implemented.

Significant Risk Factors affecting the Bank in the preceding year with respect to default levels and economic conditions and management reactions to the same

CRMD constantly reviews credit growth, portfolio concentrations, delinquencies, NPA accretions, etc., at regular intervals. Based on this, decisions like tightening product norms, discontinuing certain products in specified geographies, moderating sector exposures, exiting potential problem accounts, etc., are taken. These are reviewed at Zonal and Corporate Office levels.

The Executive Asset Recovery Management Committee (EARMC) at the Corporate Office (for outstanding of \geq Rs 1crore) and Regional EARMCs (for outstanding of $<$ Rs 1crore) are the acting bodies for reviewing irregular accounts and suggest strategies for recovery. Portfolio / Industry / Product reviews are placed to the Risk Management Committees for their review and feedback.

In the current financial year, increased stress in borrower accounts and consumer loans was noticed. This was mainly due to the slowing down of the economy, reduced exports from India, elongated working capital cycle and job losses in some segments etc. Appropriate remedial steps were and are being taken to address the situation.

Due to volatile foreign exchange rate movements, negative MTM exposures were noticed for some customers on whom the Bank had taken Derivative exposures. These were dealt with appropriately based on size and complexity of the problem.

Restructuring of loans affected by business slow-down or for other valid reasons, was done in accordance with RBI’s guidelines.

Agricultural loans that were eligible for Debt Waiver and Debt Relief schemes of Govt. of India were given the benefit.

Definitions of “past due” and “impaired” within the Bank

Bank follows the prudential norms prescribed by RBI and the definitions of ‘Past due’,

‘Out of Order’ and ‘Overdue’ are as under:

1. Impaired / Non – Performing Assets (NPAs)

An asset, including a leased asset, becomes non-performing when it ceases to generate income for the bank. A NPA is a loan or an advance where:

- a) interest and / or installment of principal remain overdue for a period of more than 90 days in respect of a term loan;
- b) the account remains 'out of order' in respect of an overdraft / Cash Credit (OD / CC);

- c) a bill remains overdue for a period of more than 90 days in the case of bills purchased and discounted;
- d) for short duration crop loans, an installment of principal or interest thereon remains overdue for two crop seasons;
- e) for long duration crop loans, an installment of principal or interest thereon remains overdue for one crop season.

The Bank classifies an account as NPA only if the interest charged during any quarter is not serviced fully within 90 days from the end of the quarter.

2. Out of order / past due status

An account is treated as 'out of order' if the outstanding balance remains continuously in excess of the sanctioned limit / drawing power. In cases where the outstanding balance in the principal operating account is less than the sanctioned limit / drawing power, but there are no credits for a continuous period of 90 days as on the date of Balance Sheet or credits are not enough to cover the interest debited during the same period, these accounts are also regarded as 'out of order'.

3. Overdue

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. Overdues greater than 30 days are reviewed at regular intervals. Overdues greater than 60 days are included in 'Watch List' / 'Stressed Accounts' and monitored on continuous basis.

Credit risk exposure

Gross Credit Risk Exposures as on 31-03-09	Rs. in Crore
Fund based exposures	25,350.69 (including investments)
Non fund based exposures	6,919.31 (including derivatives)

The Bank has exposures in the domestic segment only.

Distribution of credit risk exposure by Industry type

Industry classification	Fund based exposures (Rs. in Crore)	Non-fund based exposures (Rs. in Crore)	Total (Rs. in Crore)
Agri and allied activities	1,361.47	0	1,361.47
Industry - Micro and Small	3,859.14	433.96	4,293.1
Services	876.76	0	876.76
Trade	1,469.36	75.00	1,544.36
CRE	579.33	0	579.33
NBFC	205.17	0	205.17
CF	3,921.14	0	3,921.14
Others	13,078.32	6,410.35	19,488.67
Total	25,350.69	6,919.31	32,270.00

Residual contractual maturity breakdown of assets

Maturity Bucket	Cash and Balances with Banks	Investments	Advances	Other Assets including Fixed Assets
1 to 14 days	1,304.01	4,044.21	2,186.21	65.96
15 to 28 days	70.39	512.01	1,696.67	21.97
29 days to 3 months	174.53	975.41	1,935.66	110.60
Over 3 months and up to 6 months	199.86	1,177.02	1,972.34	45.91
Over 6 months and up to 1 year	287.02	1,525.49	1,985.15	816.08
Over 1 year and up to 3 years	62.74	598.94	3,045.59	247.16
Over 3 years and up to 5 years	81.39	553.93	1,856.16	482.91
Over 5 years	102.31	1,108.52	2,073.14	537.69
Total	2,282.25	10,495.54	16,750.93	2,328.27

Movement of NPAs and Provision for NPAs

Amount of NPAs (Gross)

	Rs. in Crore
Substandard	204.88
Doubtful 1	45.90
Doubtful 2	31.18
Doubtful 3	7.62
Loss	23.62

Net NPAs: Rs. 205.95 Crore

NPA Ratios:

Gross NPAs to gross advances	1.86%
Net NPAs to net advances	1.23%

Movement of NPAs (Gross)

	Rs. in Crore
Opening balance as on 1-04-08	203.15
(+) Additions	331.81
(-) Reductions	221.76
Closing balance as on 31-03-09	313.20

Movement of provisions for NPAs

	Rs. in Crore
Opening balance as on 1-04-08	86.91
(+) Provisions made during the period	106.43
(-) Write-off	89.53
(-) Write-back of excess provisions	0.00
Closing balance as on 31-03-09	103.81

Movement of Non-Performing Investments (NPIs) and Provision for depreciation on investments

Amount of Non-Performing Investment: Nil

Amount of provisions held for non-performing investments: Nil

Movement of provisions for depreciation on investments

	Rs. in Crore
Opening balance as on 01.04.2008	14.67
(+) Provisions made during the period	-
(-) Write-off/Write-back of excess provisions	8.79
Closing balance as on 31.03.2009	5.88

5. Credit Risk: Disclosures for Portfolios subject to the Standardized Approach

Use of rating agencies

The Bank has entered into a Memorandum of Understanding (MoU) with three (ICRA, CRISIL, Fitch) of the four External Credit Rating Agencies (ECRAs). The MOUs provide for extending concessional fees by the ECRAs, and do not contain an exclusivity clause to deal with. Borrowers have the option of approaching any of the RBI approved ECRAs, and get themselves rated.

Where bank loan ratings are available (mainly Corporates and PSEs) in the public domain, these are used, and where not available, public issue ratings of RBI approved ECRAs are reviewed for applicability and used accordingly. The rules applied while using public issue ratings and transferring the same to comparable assets in the banking book are as per the RBI requirements.

The Bank uses the ratings assigned for any type of exposure by any of the ECRAs, as accepted and provided by the borrowers. While applying these ratings, the rules specified by RBI like date of assignment of rating, selection of rating from multiple ratings available, etc. are followed.

Details of Gross credit exposure based on Risk Weight

Risk bucket	Amount outstanding (Rs. Crore) as on 31-03-09
Below 100% risk weight	16,013.17
100% risk weight	15,086.84
More than 100% risk weight	1,169.99
Deducted	Nil

6. Credit Risk Mitigation: Disclosures for Standardized Approaches

Policies and processes for collateral valuation and management

The Credit Risk Mitigation and Collateral Management Policy approved by the Board sets the framework for collateral acceptability, valuation and management within the Bank. This covers the types of collateral taken by the Bank and defines the process for valuation and management of these collaterals. This covers collateral management on a Macro level and from Basel point of view.

Bank has adopted netting off of Bank's own deposits, Government Securities, Debt Oriented Mutual Funds and gold, wherever the Collateral is identifiable, marketable and enforceable and complies with the RBI requirements. Sovereign exposures and Sovereign guaranteed exposures are risk weighted as per RBI directives.

A system of physical verification /periodical updation of the valuation of the collateral (within a period not exceeding three years) is followed. Periodicity for unit visits also is prescribed in the Credit Risk Policy and the Credit Risk Manuals. The Bank has set up Centralized Asset Processing Units (CAPUs) at all important centres to ensure perfection of documentation and to comply with charge registration matters. Electronic filing of Charge Registration with ROC in digital format is ensured by CAPU. Insurance of securities is also assured. The Bank complies with RBI requirements for collateral eligibility to be treated as a Credit Risk mitigant.

Types of collateral taken by the Bank

The main types of collateral taken by the Bank are Current Assets, Plant and Machinery, Land and Building, Liquid Assets like gold, cash or fixed deposits with the Bank, Capital Market related collateral, Guarantees provided by promoters/ Central Government/State Government/Banks/ Financial Institutions/ Other Corporates/ ECGC, etc.

Type of Guarantor / Counterparty and their Credit Worthiness

The types of guarantees recognized for credit risk mitigation are guarantees by Central Government, State Governments, ECGC, Banks and Corporates. The effect given for these guarantees are in line with RBI stipulations.

Concentration risk within the Credit Risk Mitigants taken

The Bank does not face concentration risk arising out of certain types of borrowers/ industries/ tenor as Caps have been set and are monitored. Concentration risk in terms of the mitigation taken also does not arise as the range of collateral taken, the type of borrower offering it, the location of the collateral are varied.

The Exposure covered by eligible financial collateral after the application of haircuts is Rs. 984.01 Crore as at 31 March 2009. This does not include the impact of guarantor benefit.

7. Securitization: Disclosure for Standardized Approach

The Bank purchases / sells loans through securitization and direct assignments. The primary objective for undertaking securitization activity by the Bank are enhancing liquidity; optimize the usage of capital and churning assets as part of risk management strategy.

The Bank enters into purchase / sale of home and vehicle finance loans through SPVs/ assignment. In most of the cases, the role played by bank is that of an investor. The Bank follows the standardized approach prescribed by the RBI for the securitization activities.

In accordance with the RBI guidelines, with effect from 1 February 2006, the Bank accounts for any loss arising from securitization immediately at the time of sale. The profit/premium arising from securitization is amortized over the life of the securities issued or to be issued by the special purpose vehicle to which the assets are sold.

In the financial year ended 31 March 2009, the Bank has not securitised any assets as an originator and does not have any impaired/past due assets securitized or losses recognized in the current period. The total outstanding exposures securitized by the Bank and subject to securitization framework as on 31 March 2009 is Nil

Aggregate amount of securitization exposures retained or purchased as on 31st March 2009

(Rs. in Crore)

S. No	Type of securitization	Amount
1.	Securities purchased	
	- Home and Home equity loans	120.00
2.	Liquidity facility	Nil
3.	Credit enhancement	Nil
4.	Other commitments	Nil

Risk weight bands of securitization exposures on the basis of book value

(Rs. in Crore)

Risk weight bands	Amount
Less than 100%	120.00
100%	-
More than 100%	-
Deductions	
-Entirely from Tier I capital	-
-Credit enhancing I/Os deducted from Total Capital	-
-Credit enhancement (cash collateral)	-

Comparative position of two years of the portfolio securitized by the Bank

(Rs. in Crore)

S.No	Type of Securitization	As at 31 March 2009	As at 31 March 2008
1.	Total number of loan assets securitized		
	-Corporate Loan (in numbers)	-	3
2.	Total book value of loan assets securitized		
	-Corporate loan		140.00
3.	Sale consideration received for securitized assets	-	140.30
4.	Gain / loss on sale on account of securitization	-	0.30
5.	Form and quantum (outstanding value) of service provided		-
	- Credit enhancement	-	-
	- Outstanding servicing liability	-	-
	- Liquidity support	-	-

8. Market risk in trading book

Market risk management – policy framework

The base for management of market risk is the Board approved Investment Policy that lays down the scope. It also reflects the market risk appetite of the Bank and lays down adherence to regulatory guidelines. All limit types pertaining to investment or trading activities are detailed in this policy. In addition, product mandates control the type and nature of products invested or traded in.

The Board has approved the Investment Policy for the financial year 2008-09. The policy is reviewed on a half-yearly basis or earlier as deemed appropriate.

Market Risk Management – governance framework

The Market Risk Management Department (MRMD) reports to the CRO. MRMD identifies, measures, reports and controls the market risk exposures in the Bank. The market risk due to the volatility of market variables is managed by active monitoring of Board-approved limits. Further to limit setting and monitoring, the Bank's market risk is monitored through statistical tools like VaR, bpv, PV01 and event risk calculations on all trading portfolios.

The Board and senior management are kept informed of the market risk issues and exposures on a regular basis. The Board approves the objectives, processes and policies of the market risk department. At regular intervals, notes are placed before the senior management and Board to assess the treasury operations and market risks inherent in such operations. The treasury review is placed on a monthly basis and includes a separate section on market risk. Any approval for limit excesses is sent to the appropriate authority (including the Board, if required) as per the Investment Policy on delegated authority.

ALCO actively meets and discusses the Investment, interest rate risk and liquidity issues besides looking into Asset Liability Management (ALM) and investment policies related matters. The Financial Markets Department (FM), on behalf of ALCO, manages the day-to-day operations. ALCO reports to the Board through the RMRC.

The Market Risk Management Department in the Bank operates independently of the treasury dealing room. It monitors the operations of the treasury front office and checks the limits as laid down in the policy. The exposures are reported finally to management.

Financial Market Operations operates independently of the dealing room, with its own independent processing systems. Their staff handles all confirmations, payments and authorizations in the Financial Market operations systems, etc.

Market risk management models/ methods/ processes

The tools used for measuring, monitoring and controlling market risks are commensurate with the nature and composition of the investments and trading activities of the Bank.

Limit checks, revaluation and pricing of securities are independently done on a daily basis through MRMD's own systems. The Bank uses an in-house developed module to capture VaR, and the same is back tested for model effectiveness as well. The variance covariance method is used for calculating VaR for a 1-day horizon at 99% confidence level. Historical method is used to calculate FX-Options VaR. 250-days historical simulation is applied at 99% confidence. The module also calculates the bpv's and stress scenarios.

FX risk in the books is independently controlled on an overall basis by MRMD through monitoring:

- Day light limits
- Overnight limits
- Nostro limits
- Stop loss limits
- Gap limits
- Overall Position limits

The Investment Policy does not allow any fresh equity positions. The current minor equity positions are largely illiquid but the Bank explores the possibility of a sale as and when an opportunity arises.

Stress testing and scenario analysis

The framework and scenarios for stress testing have been outlined in detail in the Market Risk Measurement Policy. While the Value at Risk methodology assumes ‘normality’, reality has shown problems with this assumption. In general, it turns out that extreme scenarios are more likely to happen than what is to be expected under the assumption of normality. In order to be aware of extreme swings, the Bank undertakes stress tests. For event risk, a set of possible combinations is calculated. Based on the outcome of the results, limits may be adjusted and re-approved by competent authority.

There are broadly two categories of stress tests used, viz. sensitivity and scenario tests. Sensitivity tests are normally used to assess the impact of change in one variable on the Bank’s position. Scenario tests include simultaneous moves in a number of variables.

As per Basel II, the stress test limits are set in such a way that it never exceeds more than 20% of the Bank’s capital. Accordingly, the other risk limits are derived from this principle.

Portfolios covered by standardized duration approach

The following portfolios are covered by the standardized duration approach:

- AFS (available for sale)
- HFT (held for trading) for MM, FX and derivatives
- FX from banking books

Capital requirements for Market Risk

		(Rs. in Crore)
Interest Rate (a+b)		67.6
	a. General Market Risk	36.7
	b. Specific Risk	30.9
Equity(a+b)		1.0
	a. General Market Risk	0.5
	b. Specific Risk	0.5
Foreign Exchange and Gold		9.0
Total Capital Charge for Market Risk		77.6
RWA for market risks		862.4

9. Operational risk

ING Vysya Bank Ltd has defined operational risk as the risk of direct or indirect loss resulting from inadequate or failed internal processes, people and systems or from external events. It also includes the risk of reputation loss as well as legal risk; whereas strategic and business risks are not included.

The Bank has various Policies (Operational Risk Policy, Information Risk Policy, Security Policy, Outsourcing Policy, Crisis Management Policy and Anti-Fraud Policy) in place to ensure effective management of Operational risks.

Key stages of the operational risk management processes is risk identification, risk measurement, risk monitoring and risk mitigation. In order to make the process more effective and integrated for the business units, legal, compliance and operational risk functions in the Bank work in an integrated manner with similar processes.

Operational Risk Management framework

For effective management of the Bank's operational risk exposure, the Bank has set up an independent Operational Risk Management function, which is responsible to develop and implement policies and procedures for effective management of the Bank's operational risk exposure. The unit follows the Board approved Operational Risk Management Policy for effective implementation of operational risk management across various business units of the Bank.

Risk management structure

An Operational Risk Committee (ORC) with representation from all business lines and critical support functions has been set up to ensure effective implementation of the operational risk management across all units of the Bank. The committee meets once in every month and discusses the operational issues identified and takes necessary steps to mitigate the risks. The Bank also has Regional Operational Risk Committees (RORC) at the regional level that meet regularly to discuss the region's operational issues and takes necessary steps to mitigate the risks.

In addition to the ORC and RORC, the Risk Management and Review Committee (RMRC) of the Board at the highest level meets periodically to analyze and take necessary steps to mitigate the risks that the Bank is exposed to. The Board and senior management are kept informed of operational risk issues on a periodic basis.

Risk Reporting

A clear defined risk reporting system has been set up in the Bank. At the regional level, RORCs have been set up to monitor the operational risk exposure with representation from the departments and senior management at the regional level. At the Corporate Office level, ORC has been set up with representation from the departments and senior management from all business lines and critical support functions of the Bank. The committees meet regularly to discuss the operational issues and take necessary steps to mitigate the risks.

The Bank uses the Non-Financial Risk Dashboard (NFRD) as an operational risk reporting tool. This report highlights the identified operational risks as well as the action taken to mitigate the risks. It also provides an overview on the progress of the mitigation plans of the identified operational risks.

Strategies and Processes

The Bank promotes effective management of operational, information and security risk by involving the Business Units in the risk management process. This is achieved by raising operational risk awareness, increasing transparency, improving early warning information system, and allocating risk ownership and responsibilities. While the Operational Risk Management function supports the Business Units in identifying and assessing the operational risk exposure, the Business Units are responsible to take appropriate steps to put controls in place for the operational risks.

The Bank has developed a comprehensive framework supporting the process of identifying, measuring, monitoring, and managing operational, information and security risks. The operational risk assessment has been made an integral part of the Bank's risk management process through assessment of outsourced activities, product reviews, product approval, and project risk assessment.

Risk Management Processes

Risk Governance

Examples of risk management tools

- Operational Risk Committee
- Compliance program
- Product Approval process
- Risk awareness training

Risk Identification	- Risk and Control Self Assessments - Risk Awareness programs
Risk Measurement	- Incident Reporting and Analysis - Quality of Control Scorecards
Risk Monitoring	- Audit Findings Action Tracking - Key Risk Indicator reporting - Operational risk dashboard
Risk Mitigation	- Information Security plans and implementation - Crisis management planning - Personal and physical security planning

The Bank has an internal risk footprint, which it uses as threshold to decide the severity of an operational event. Further, the Bank has a centralized loss data capture mechanism that it uses for the quantification of the operational losses. The Bank currently uses the scorecard approach to measure the implementation of the operational risk management across the Bank. This approach is based on the maturity of the operational risk management in the Bank.

Operational risk capital:

The Bank currently qualifies for the Basic Indicator Approach operational risk capital assessment. The capital requirement for operational risk has been estimated as per the Basel II related regulatory guidelines prescribed by the Reserve Bank of India.

10. Interest Rate Risk (IRR) in the banking book

Changes in interest rates affect a Bank's earnings by changing its net interest income and the level of other interest sensitive income and operating expenses. For the purpose of monitoring and management, interest rate risk is separated into four sources, viz.,- re-pricing risk, yield curve risk, basis risk and optionality.

Identification, measurement, mitigation, monitoring and governance of IRR are prescribed in and followed as per the directions in the Market Risk Measurement Policy and the Investment Policy.

Interest rate risk arising due to re-pricing of those assets and liabilities which do not have a maturity date (e.g. Current and Savings Accounts and Cash Credit/Overdraft products) is managed by distributing these assets into various maturity buckets based on an approved 'replication model'. The model is independently developed by Market Risk and is approved by ALCO as directed by RBI before application. This model is reviewed on a yearly basis (or in case of changing market conditions as deemed appropriate). The model primarily assumes a core portion of these products as long-term assets/liabilities and replicates the same in higher tenure buckets (versus volatile portion which is replicated in the short term).

Similarly, risk arising due to loan prepayments and/or deposits pre-closures is also managed by levying a penalty on such transaction. Market Risk independently ascertains the cost of such 'optionality' through respective behavioral studies on an annual basis and the same is approved by ALCO on a yearly basis. The cost of optionality in the study is derived using the historical pre-closure values and option pricing theories.

Market risk manages the interest rate risk of the banking books by pro-actively and periodically employing the tools as mentioned above. Managing and monitoring the interest rate risk exposure arising out of normal business activity is executed within the following risk limits / framework:

- Mismatch per bucket (cumulative and normal gap limits)
- Earning at Risk limit

- VaR limit for ALM book and fraction VaR limit for the Capital book
- Event risk limit and
- Duration mismatch

The type and level of structural and mismatch interest rate risk of the Bank is managed and monitored from two perspectives, being an economic value perspective and an earnings perspective.

Economic Value perspective involves analyzing the impact of changes in interest rates on expected cash flows on assets, minus the expected cash out-flows on liabilities, plus the net cash flows of off-balance sheet items.

Earning perspective involves analyzing the impact of changes in interest rates on accruals or reported earnings in the following year. This is measured by Net Interest Income (NII) or Net Interest Margin (NIM).

The Bank combines both methodologies to analyze both effects simultaneously.

Earnings impact perspective

(Org cur in
mln)

	TOTAL	INR	EUR	USD	GBP	JPY
Net Interest Income year 1						
EaR +100 bps parallel	303.1	197.2	(0.0)	0.8	0.9	0.0
Net Interest Income year 2						
EaR +100 bps parallel	16.2	14.8	0.0	0.0	0.0	0.0
EaR y3 ramped						
EaR +100 bps parallel	(20.2)	(20.7)	0.0	0.0	0.0	0.0

Economic value perspective

(INR in

mln)

NPV Impact	Total	INR	EUR	USD	GBP	JPY
+ 50 bps	(10.49)	(31.76)	0.15	16.54	4.57	0.00
+100 bps	(20.98)	(63.52)	0.31	33.09	9.14	0.00