

HEDGE FINANCE LIMITED
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RISK MANAGEMENT POLICY

INTRODUCTION

Non Ranking Financial companies (NBFCs) form an integral part of the Indian financial system. NBFCs are required to ensure that a proper policy framework on Risk Management Systems with the approval of the Board is formulated and put in place. Risk Management (RM) at Hedge Finance Ltd (HFL) encompasses practices relating to identification, assessment, monitoring and mitigation of various risks to its business model. The purpose of this Policy is to address unanticipated and unintended losses to human resources, financial assets and property of the organization without unnecessarily limiting the activities that advance the organization's mission and goals. This policy document has been prepared in line with the RBI guidelines. The Board is responsible to frame, implement and monitor the Risk Management Plan of the Company.

AIMS & OBJECTIVE

The main objective of this policy is to keep the Board of Directors and Top Management apprised of the applicable risks promptly and regularly. This risk management policy also aims to protect the reputation of the organization, enable the Company to make consistently profitable and prudent business decisions across all its offices and ensure an acceptable risk-adjusted return on capital or any other equivalent measure. In a nutshell it seeks to ensure growth with profitability within the limits of risk absorption capacity. It is expected to facilitate the Company to acquire and maintain a pre-eminent position amongst NBFCs especially those engaged in the business of loans against equipment's, machinery, vehicles, MSME loans etc.

GENERAL PROVISIONS

This Policy represents the basic standards of Risk Assessment to be followed by the company. Changes in the Policy will become effective upon approval by the Board of Directors of the Company. All relevant employees must be thoroughly familiar or made familiar with it and make use of the material contained in this Policy. Specific Risk Management criteria relating to each category of loans has been prescribed in the relevant loan policies.

RISK MANAGEMENT

Risk management is a business facilitator by making more informed decision with balanced risk- reward paradigm. The Company shall follow a disciplined risk management process and has been taking business decisions, ensuring growth and balancing approach on risk reward matrix. Effective management of risk is vital to the continued growth and success of HFL. For risk management to be effective, all operations must apply the following principles to the context of their particular business and its objectives: -

- i. To continuously scan the subsisting risks in the organization which directly or indirectly effect the functioning of the organization
- ii. To ensure the protection of rights & values of stake holders by establishing a well organized Risk Management framework.
- iii. Selecting, maintaining and enhancing the risk management tools used by the program to provide analysis that inform and support the investment actions of the entire organization.

Identification, Measurement and Assessment of Risk:

- i) Management's responsibility as delegated Zby the Board is to operationalize the Risk Management Program and ensure that formal procedures are in place to identify and define risk with input from representatives across the enterprise.
- ii) Measurement of risk is completed considering both quantitative and qualitative means using the likelihood and impact criteria as developed by Management and as reviewed by the Board.

Risk Categories

Following broad categories of risks have been considered in HFL's risk management framework.

1. Credit Risk

A risk of loss due to failure of a borrower/counterparty to meet the contractual obligation of repaying his debt as per the agreed terms is commonly known as risk of default. Credit risk is an essential factor that needs to be managed. Credit risk is inherent in all aspects of a commercial operation. However for financial institutions credit risk is an essential factor that needs to be well managed.

Credit Assessment: A thorough credit and risk assessment should be conducted prior to opening of client account and at least. Branch Head should be owners of the customer relationships and must be held responsible to ensure the accuracy of the entire credit application submitted for approval. Branch Heads should be familiar with the Company's margining policies and should conduct due diligence on every client. In addition the following risk areas should be addressed:

- a) Financial **capacity** - An insight is absolutely necessary to draw in mind the financial capacity of the client,
- b) KYCs should ask for nature of income of the prospective client and the quantum of such income
- c) Payment history — The delay between incidence of payment and the time when the payment becomes due needs close monitoring. A deteriorating situation is alarming and may require reduction of exposure to the party concerned.

2. Market Risk

Risks emanating out of the choices we make on markets, resources and delivery model that can potentially impact our long term competitive advantage. Risks relating to inherent characteristics of our industry including competitive structure, technological landscape, extent of linkage to economic environment and regulatory structure. This is majorly external market dynamics, which gives rise to Risks like Liquidity risk, Interest rate risk and Funding risk. Liquidity risk is the inability to meet financial obligations in a timely manner and without stress. The Company shall resort to proper ways to manage such risks.

Risks inherent to business operations including those relating to client acquisition, service delivery to clients, business support activities, information security and business activity disruptions. Any eventuality arising from the act relating to people, technology, infrastructure and external factors, which can give rise to some type of loss

in the organization, is termed as Operational Risk. Majorly it is internal and unknown. Therefore, the persons responsible shall keep continuous watch and shall gather the symptoms/warning signals to manage Operational risk.

4. Interest Rate Risk

Interest rate risk is the risk where changes in market interest rates might adversely affect an NBFC's financial condition. The changes in interest rates affect the Company substantially. The immediate impact of changes should be reviewed by the Board. The Audit Committee assists the Board in overseeing the risk profile of the Company and is responsible for overseeing management's actions in the identification, management and reporting of material business risks.

Risk Mitigation

- a) As a contingency plan the Company shall maintain sufficient approved but un- drawn credit lines on a continuous basis as buffer to manage eventuality of liquidity constraints.
- b) The Company shall be compliant in terms of regulatory norms and therefore shall effectively manage regulatory risk.
- c) Effective Customer redressal mechanism and fair practices shall keep legal risk under control.
- d) The Company shall have processes in place, to manage the risk of fraud and the suspected frauds are reported, wherever necessary.

5. Regulatory Compliance Risk

- a) The Company is an NBFC coming under the regulatory purview of the Reserve Bank of India RBI. In addition the Company is also required to comply with various central. State and commercial laws applicable in the conduct of the various activities of the business. Rising numbers and expectations of stakeholders, robust growth in the business of NBFCs, increasing dependency on non-equity sources of funding and some 'Corporate' frauds have increased the regulatory gaze, increased the complexity of the regulations and sometimes necessitate investments / costs,
- b) Meeting with compliance requirements: The Company recognizes that the regulatory landscape is under periodical review and this requires the Company to be proactively prepared, as best as possible, to meet with the challenges posed by

the changes. There is also an element of unpredictability over possible future regulatory action. The Company will respond effectively and competitively to regulator changes. maintain appropriate relationship with the regulators / authorities, strengthen the reliance on capital and improve the quality of in-house compliance. All reports, returns and disclosures stemming from regulations will be submitted promptly and accurately to reflect the correct position.

- c) Business processes will be defined in a manner to ensure comprehensive regulatory compliance considering the multitude of regulatory agencies the Company has to deal with.

- d) Responsibility: Competent and knowledgeable specialist officers will be put in place to ensure compliance. The responsibility for ensuring compliance with regulatory requirements and directives on a day to day basis will rest with the Business Heads. Such compliance will be overseen and confirmed by the Compliance Officer and the Internal Audit Dept of the Company.

6. IT Risk

the Company has been ahead of other similarly placed NBFCs in adoption of a fully computerized environment for conducting its business operations. The Company has adopted a comprehensive IT Policy encompassing acceptability of various usages, asset management, applications management, infrastructure management and IT security.

7. Competition Risk

- a) Competition risk represents the challenges to business arising from an increasing number and intensity of other existing or new firms engaged in the same business which threaten business growth and could eat away the market share of the Company's business. The Company faces intense competitive pressures from similarly placed NBFCs and of late from Banks and other financial institutions which have taken up loans intensively especially in the light of the phenomenal growth expected in the MSME arena.
- b) Coping with competition: The Company will broadly address the risks of competition by:
- i) Accepting and recognizing the presence of competitors as a fact or business. Such competition could be universal and or area specific.
 - ii) Identifying the major and nearest competitors for benchmarking performance.
 - iii) Assessing the business strategies of competitors and ensuring suitable countervailing mechanisms to meet such threats.
 - iv) Studying and comparing (with) the performances of the competitors with judiciously collected information and data.
 - v) Continuously reviewing existing product and services to ensure that they are in tune with market demand and customer expectations keeping in view the regulatory guidelines.
 - vi) Recognising the need to reduce unproductive costs and improve the

productivity of employees to make the offerings more competitive.

- vii) Studying or anticipating customer preferences and accordingly developing new products and services with visible value addition to be ahead of other market players.
- viii) Ensuring transparency and fairness in dealings with customers and adopting / promoting customer service excellence as an important selling tool.

c) Responsibility: The Head, Sales and Marketing Department will be responsible to identify and suggest initiate measures to meet the threats of competition. The Company will not be induced to adopt any unethical practices to meet with competition even if other market participants do so. Risk Management Dept will study the risk.

RISK MANAGEMENT OF BORROWER(S)

It is generally recognized that certain borrowers may be of a higher or lower risk category depending on the customer's background, type of business, our references, borrowers net worth and the ability to refund and pay interest etc. As such, the principal officer shall apply to each of the customers due diligence measures on a risk sensitive basis and shall divide the same in three categories

- High, Medium & Low Risks which shall be reviewed every year. Initially all the new clients are to be marked as high — risk category, however they may be subsequently recategorized depending on their performance based on our own experiences. The basic principal enshrined in this approach is that the concerned persons should adopt an enhanced customer due diligence process for higher risk Customers. Conversely, a simplified customer due diligence process may be adopted for lower risk of categories of customers. In line with risk based approach, the type and amount of information and documents shall vary depending on the risk category of a particular borrower and should be collected from the client. The beneficial owners working should be done for all corporate clients and background check of all Directors.
- In case of a borrower who subsequently has turned out to be a Politically Exposed person (PEP), proper risk management system should be put in place to determine the beneficial ownership from such clients or potential clients. Once we are privy to such publicly available information or the commercial electronic database of PEPs, we should seek additional relevant information from such client pertaining to ownership issues and other risks associated with such persons and take call whether such exposure to him or his company we should continue or terminate the relationship after giving notice in advance. As a policy without concurrence of top management, no such identified PEP account is to be granted loan.
- Suspicion of ML/FT(Money laundering and terrorism financing) activities or other factors give rise to belief that the client does not fall under the low risk category. and the risk perception shall accordingly be changed.

OBLIGATIONS OF THE PRINCIPAL OFFICER.

The Principal Officer is required to carry out risk assessment to identify, assess and take effective measures to mitigate its money laundering and terrorist financing risk with respect to such borrower, countries or geographical areas, nature and volume of transaction, payments method used by borrowers. The risk assessment shall also take into account any country specific information provided or circulated by Government of India and SEBI from time to time, as well as the updated list of individuals and entities who are subjected to sanction measures as required under the various United Nations Security Council .

The risk assessment carried out shall consider all the relevant risk factors before determining the level of overall risk and the appropriate risk level and type of mitigation to be applied. This assessment shall be documented, updated regularly and made available to competent authorities and self regulating bodies as and when required.

RISK MANAGEMENT COMMITTEE

The implementation of the Risk Management Policy by the Risk Management Department and the various business units will be overseen by the Risk Management Committee (RMC) of the Company. The constitution of the RMC shall be as under:

- i) MD/ WTD/
- ii) CEO, COO & CFO.
- iii)
- iv) RMC shall be chaired by MD/ WTD

Company Secretary shall be Secretary of the RMC.

The RMC shall meet at least twice in a year to review the Risk Management Policy, document and improve risk management practices, ensure appropriate / adequate reporting to the Board, review the functioning of the Risk Management Department and any other matter as the Committee may deem fit.
