MANAGING CORE RISKS
IN BANKING

ASSET LIABILITY RISK

Janata Bank
Head Office, Dhaka

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IN BANKING

ASSET LIABILITY RISK

Janata Bank
Head Office, Dhaka

Under the Supervision

of

SYED ABDUL HAMID

General Manager

Prepared

by

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From the desk of Managing Director
A Few Words

To streamline the financial discipline Bangladesh Bank has recently identified 5 (five) Core Risks in Banking Sector i.e., (1) Credit Risk (2) Asset Liability Management Risk (3) Foreign Exchange Risk (4) Internal Control & Compliance Risk and (5) Money Laundering Risk.

Among these Risks, Asset Liability Management is a vital element in the Balance Sheet Risk management. Balance Sheet Risk can be categorised into two major types of significant risks which are liquidity & interest rate risks. Change in financial liquidity or interest rates exposes banks to the risk of loss, which may have threaten the survival of institution. So, increasingly Asset Liability Risk Management has become an integral part of Bank Management. As such, it is very much essential that senior management as well as concerned officials should be conversant with existence of such risk on the Balance Sheet and should ensure that such risks are effectively managed. To minimize the balance sheet risk, effective policies and procedures are required.

For this purpose, Fund Management Division did commendable job by preparing an Asset Liability Management Manual. The Asset Liability Management Manual aims at providing instructions, procedures, guidelines and policies that can be followed for Balance Sheet Risk management. The Manual also highlights the role of the ALCO and is aimed at providing detailed guidlines on the key aspect to Asset Liability Management within the Bank in order to optimally manage Balance Sheet Risk.

The fundamental policies and guidelines laid down in this manual should be complied with meticulously and observed strictly. However, suggestions for making further improvements will be welcome and shall be implemented if found feasible after due examination and careful scrutiny.

S. M. Aminur Rahman

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PART-A

01.00 BACKGROUND

Asset Liability Management (ALM) is an integral part of Bank Management and so, it is essential to have a structured and systematic process for managing the Balance Sheet.

Banks are exposed to several major risks in course of their business viz., credit risk, interest rate risk, foreign exchange risk, equity/commodity price risk, liquidity risk and operational risks. It is therefore, important that banks introduce effective risk management systems that address interest rate risk, currency risk and liquidity risk.

Asset Liability Management is concerned with risk management and provides comprehensive & dynamic framework for measuring, monitoring and managing liquidity, interest rate, foreign exchange and equity/commodity price risks in the context of banks business strategy.

To manage these risk factors in a systematic manner there is a committee in the bank, known as Asset Liability Committee (ALCO).

02.00 METHODOLOGY

The guideline is based on the international tools and strategies practiced by the banks to manage its balance sheet risk. Different reports, researches, databases etc., published in Asset Liability Management are being used as primary input for this paper.

03.00 POLICY STATEMENT

ALCO of Janata Bank set out the following policies which should be reviewed annually taking into consideration of changes in balance sheet and market dynamics.

(a) Loan Deposit Ratio (LDR)

The Loan Deposit Ratio should be 80% to 84% in the following Sub-Divisions :

25% on account of Term Loan

15% on account of Rural Advance and Micro Enterprise Loan

15% on account of Export & Import Finance

Rest 29% on account of Working Capital & Other Demand Loans

(b) Commitments

A bank's liquidity is very much vulnerable to undrawn commitments by customers. Customers have the right to ask for this funds at any point in time and the bank is obligated to pay the customers. Thus a ceiling should be such on a bank's commitments to customers. Maximum 200% of unused Demand and Time Liabilities can be taken into consideration for undrawn commitments.

(c) Wholesale Borrowing Guidelines (WBG)

Wholesale Borrowing Guidelines limit is based on the match funding basis.

(i) Current deposit and part of savings deposit is considered as investment to meet legal requirements of CRR & SLR.

(ii) One year and above but less than 2 yrs. term deposit may be used for mid -term investment.

(iii) 3 months, 6 months but less than 1 year term deposit and part of savings deposit may be used to finance working capital & other demand loan.

(iv) Next day, 2 to 7 days, 7 days to 1 month and 1 to 3 months term deposit may be used for demand loan and short term investment i.e., Call money, Reverse REPO, 28 days, 91 days, 182 days Govt. Treasury Bills/Bonds and Govt. Securities.

(v) 2 yrs. and above term deposit can be taken upto the amount of long term loan.

(d) Maximum Cumulative Outflow (MCO)

Maximum Cumulative Outflow (MCO) guidelines control the net outflow (Inflow from asset maturity minus outflow from liability maturity) over the following periods :
Overnight, one week and one month.

MCO upto 1 month bucket should not exceed 10% of balance sheet to avoid funding mismatch (It may vary according to the volume of Asset Liability of a bank).

Fund Management Division & Overseas Banking Division of Janata Bank will review its funding capabilities and recommend the guidelines to higher management. These guidelines will be based on the estimated wholesale funding shortfall after calculating the forecast/contractual cash flow of the entity under normal business conditions.

The MCO guideline is a "business as usual" measure, which implies that necessary reserve liquidity must be maintained at all times and so cannot be counted towards meeting the MCO requirement. Whilst it may not be possible to include specific figures within MCO controls, banks should also be aware of cash flows from settlement of foreign exchange transactions and of intra-day exposures arising from the operation of the daily clearing systems.

(e) Medium Term Funding Ratio (MTF)

Banks earn money from mismatches, that is, by borrowing short term and lending long term. Bank has to find out the right combination for longer term mismatch. MTF ratio is based on the amount of liability with a contractual maturity of more than one year to assets with a contractual maturity of more than one year, that is MTF should be done on the basis of 1 (one) year and above but less than 2 (two) years term deposit. The desirable ratio of MTF should be 15% to 20%.

(f) Liquidity Contingency Plan

A liquidity contingency plan needs to be approved by the ALCO. A contingency plan needs to be prepared keeping in mind that enough liquidity is available to meet the fund requirements in liquidity crisis situation. An annual review of the contingency planning should be made.

(g) Local Regulatory Compliance

There is a firm policy on compliance to the Bangladesh Bank in respect of CRR, SLR, Capital adequacy etc., in our bank.

4.00 MATURITY PROFILE MISMATCH

A typical strategy of a bank to generate revenue is to run mismatch i.e., borrow short term and lend longer term. However, mismatch is accompanied by liquidity risk and excessive longer tenor lending against shorter-term borrowing would put a bank`s balance sheet in a very critical and risky position.

To address this risk and to make sure a bank does not expose itself in excessive mismatch, a bucket-wise (e.g., next day, 2 to 7 days, 7 days to 1 month, 1 to 3 months, 3 to 6 months, 6 months to 1 year, 1 to 2 years, 2 to 3 years, 3 to 4 years, 4 to 5 years, over 5 years) maturity profile of the assets and liabilities is prepared to understand mismatch in every bucket.

Most deposits and loans of a bank matures next day (Call, savings, current, overdraft etc.,). Bucket-wise assets and liabilities based on actual maturity reflects huge mismatch; although we know that all of the shorter tenor assets and liabilities will not come in or go out of the bank`s balance sheet. As a result, banks prepare a forecasted balance sheet where the assets and liabilities of the nature of current overdraft etc., are divided into core and non-core balances, where core is defined as the portion that is expected to be stable and will stay with the bank; and non-core to be less stable. The distribution of core and non-core is determined through historical trend, customer behavior, statistical forecasts and managerial judgement; the core balance can be put into over 1 year bucket whereas non-core can be in 2-7 days or 3 months bucket.

PART-B

05.00 ALCO OF JANATA BANK

To manage and monitor ALM risk, ALCO is headed by Deputy Managing Director-1 with the following Executives :

1. Deputy Managing Director-1	:	Chairman
2. General Manager, Fund Management Division	:	Member
3. General Manager, Overseas Banking Division	:	Member
4. General Manager, Local Office	:	Member
5. Deputy General Manager, Overseas Banking Division	:	Member
6. Deputy General Manager, Fund Management Division	:	Member-Secretary

06.00 MEETING

Committee sits once at least in every 2 (two) months to review the performance of the Division for setting targets and to guide the Division.

07.00 THE KEY ROLES AND RESPONSIBILITIES OF ALCO

The key roles and responsibilities of ALCO are as follows :

a. Directing general policies on risks exposures
b. Setting portfolio risk limit
c. Setting interest rate mismatch/gap limit
d. Liquidity limit
e. Establishing monitoring system for exposure control and limit management

08.00 DIFFERENT TYPES OF RISKS PERTAINING TO ALM

The following types of risks are faced by the bank in managing asset liability portfolio :

a. Liquidity risk management
b. Management of market risk
c. Funding and capital planning
d. Profit planning and growth projection
e. Trading risk management

Among these five functions Asset Liability Management mainly is concerned with liquidity and interest rate risk management.

09.00 ASSET LIABILITY MANAGEMENT (ALM)

Asset Liability Management (ALM) is a key financial and risk management discipline. ALM concerns the management of the bank's on and off balance sheet position in such a way that the bank is able to offer competitively priced products and services to customers, whilst maintaining and appropriate risk/reward profit that creates shareholders value.

The key roles and responsibilities of the ALM desk are followings :

1. To assume overall responsibilities of money market activities.
2. To manage liquidity and interest rate risk of the bank.
3. To comply with the Local Central Bank Regulations in respect of bank's statutory obligations as well as thorough understanding of the risk elements involved with the business.
4. Understanding of the market dynamics i. e., competition, potential target markets etc.
5. Provide inputs to the treasurer regarding market views and update the balance sheet movement.
6. Deal within the dealer's authorized limit.

Generally this policies will be implemented through and controlled by ALCO.

09.01 Money Market Operations

Available funds are invested in money market through call money, repo, reverse repo, purchase of treasury bill/bonds and other Govt. approved securities. Funds are also reserved in Bangladesh Bank in the form of SLR through treasury bills /bonds and other Govt. approved securities . Besides that CRR is also maintained the following instructions of Bangladesh bank. Surplus funds are deposited in Commercial Banks/Non-Banking Financial Institutions in the form of FDR's to activate the money market operation. During available surplus fund, following steps should be taken by Head Office Fund Management Division :

a. Purchase treasury bills
b. Reverse repo with Bangladesh Bank
c. Inter-bank reverse repo
d. Invest fund in the form of call money
e. Discourage deposit at a higher rate of interest

On the other hand, during shortfall of fund following steps are usually taken by the authority :

a. Mobilisation of deposit by offering prime rate
b. Discourage sanction of new loans in less priority sectors
c. Crush programme are taken for recovery of bad loans & advances

10.00 KEY AGENDAS OF ALCO MEETINGS

ALCO attends the following issues while managing balance sheet risks :

a. Review of actions taken in previous ALCO
b. Economic, market status and outlook
c. Liquidity risk related to the balance sheet
d. Review of the price/interest rate structure
e. Actions to be taken

11.00 ALCO PAPER

An ALCO paper is produced every month (Usually by Fund Management Division) which covers various issues related to balance sheet risk management. The ALCO paper is prepared before the ALCO meeting as the committee reviews the ALCO paper to set strategies. An ALCO paper typically covers the followings as per policy statement described earlier :

(a) Commentary

A brief summary on the following issues for the last month are provided for review :

- Combined as well as segmented (Current, STD, Term etc.) deposit trend for local and foreign currency
- Combined as well as segmented (Overdraft, Term etc.) advance trend for local and foreign currency.
- Loan-deposit ratios.
- Limit status and utilization.

(b) Interest Rate Trend of the Market

Interest rate and yield curve for treasury bills, overnight funds, term money, competitive bank's published customer rates are included in the paper. A yield curve is a graphic representation of the yields for a given financial instrument over a given time period.

(c) Balance Sheet

A summarized or detailed version of the bank's balance sheet for the current and previous month will provide to understand the trend in assets and liabilities. This portion also covers the variance in assets and liabilities against the target of the bank.

(d) Key Management Indicators (Limits & Utilisation)

The management of every bank sets different limits in managing risk and exposures. The current limit of all indicators along with recent utilization will be included for management review. Also trend for last few months are also be included for better understanding of the behaviour of the indicators. Some of the such key management indicators are mentioned in policy statement described earlier.

(e) Liquidity Test for Contingencies

The major risk the bank runs is liquidity risk. Under any circumstances the bank has to honour its commitments. As a result, it has to make sure that enough liquidity is available to meet fund requirements in situations like liquidity crisis in the market, policy changes by Bangladesh Bank. So, the bank's balance sheet should have enough liquid assets for meeting contingencies. Liquid assets can be as follows :

- Reserve assets
- Cash in tills (Balance with Bangladesh Bank)
- Specific Government securities/treasury bills
- Foreign currency in open position
- Specific FDRs

A liquidity contingency plan should be in place to ensure that the bank is prepared to combat any crisis situation.

(f) Interest Rate Profile

Apart from liquidity risk, a bank also runs interest rate risk, which is the exposure of the bank's financial condition to adverse movements in interest rates. Accepting this risk is a normal part of banking and can be an important source of profitability. However, excessive interest rate risk can pose a significant threat to bank's earnings and capital base. To address interest rate risk, an interest rate profile will be in each month prepared, where consolidated yield for assets and liabilities for different maturity buckets are shown for better understanding of interest profile.

12.00 THE ALCO PROCESS

ALCO will review the ALCO paper along with the prescribed agenda. The Chairman of the Committee will raise the issues related to the balance sheet. The Chairman will suggest whether the interest rates need to be repriced, whether the bank needs deposits or advance growth, whether growth of deposits & advances should be on short or longer term, what will be the transfer price of funds among the divisions, what kind of inter-bank dependency the bank should have etc. In short, all issues related to liquidity and market risk will be covered.

Based on the analysis and views of the Chairman, the Committee will take decisions to reduce balance sheet risk while maximising profits.

13.00 ACTION POINTS

The ALCO will take decisions for implementation of any/all of the following issues :

- Need for appropriate deposit mobilisation or asset growth in right buckets to optimise asset liability mismatch.
- Cash flow (Long/short) plan based on market interest rates and liquidity.
- Need for change in Fund Transfer Pricing (FTP) and/or customer rates in line with strategy adapted.
- Address to the limits that are in breach (if any) or are in line of breach and provide detailed plan to bring all limits under control.
- Address to all regulatory issues that are under threat to non-compliance.

14.00 IMPLEMENTATION AND REVIEW OF STRATEGIES

All ALCO members are provided with the minutes of the meeting within the next day. The minute includes :

- The attendees
- The issues addressed
- The recommendations provided by the Chairman
- The action points that were fixed in the meeting

The members will communicate the action points to their respective divisions to implement the strategies undertaken.

15.00 SPECIAL ALCO MEETING

Apart from the regular monthly meeting, ALCO meeting is also called as and when any contingent situations arise. A very good example may be, during the Eid period, changes in SLR/CRR or any other important changes in liquidity imposed by Bangladesh Bank. At those times, market liquidity dries out and overnight rates shoot up. Banks who are net borrowers from the market may be exposed to huge interest expense the high rates in the market. This is an ideal time for a special ALCO meeting, where the committee may take critical decisions.

16.00 MARKET RISK AND ASSET LIABILITY MANAGEMENT

Market risk measures the risk of loss due to adverse movements in market prices or rates such as interest rates, FX rates. Following are the key management indicators for managing market risk :

(a) Value At Risk (VAR)

Value At Risk (VAR) is a technique used by ALM to estimate the losses which could potentially occur on market risk positions as a results of movements in market rate and prices. The following are practical factors relating to VAR :

The estimate is base on a given time horizon and level of confidence. A typical level of confidence may vary from 95% to 99% .

The typical time horizon may be 1 to 10 days.

Specifically, Value At Risk (VAR) is a measure of potential loss from an event in a normal, everyday market environment. VAR is denominated in a currency, say Taka, where it measures the chance of losing Taka for a movement in interest rates for a given balance sheet scenario. For example, if a bank only has 1 month borrowing to fund 1 year customer lending, an increase in 1 month rates would result in incremental expense for the bank. VAR is estimated by assuming a 97.5% confidence level for movement in relevant market risk factors.

Let us construct a very simple example to understand the VaR methodology. In the following table a simple hypothetical balance sheet for a bank is shown, where it has BDT 100 Mio 1 month borrowing to fund same amount of assets :

	1 Month (BDT Mio)	1 Year (BDT Mio)
ASSET	0	100
LIABILITY	100	0
MISMATCH	(100)	100

Say the market interest rate for 1 month is 8% and 1 year is 10%. Now, if we need to square the balance sheet gaps, we need to lend in 1 month at 8% and need to borrow in 1 year tenor at 10%.

Therefore, the expected Value At Risk to square the position will be :
VAR = 100 * (8% *30 days/360 days) - (100* 10% * 360 days/360 days)= BDT (0.67-10) = BDT 9.33 Mio.

PART-C

KEY CONCEPTS

1.00 BALANCE SHEET RISK

Balance sheet risk can be categorised into two major types of significant ri which are liquidity and interest rate risks. Changes in market liquidity and interest rates exposes banks/business to the risk of loss, which may, in extre cases, threaten the survival of institution. As such, it is important that sen management should understand the existence of such risk on the balance sh and they should ensure that the structure of the institutions` business and the le of balance sheet risk it assumes are effectively managed, that appropriate polic and procedures are established to control and limit these risks and that resour are available for evaluating and controlling interest rate risk.

2.00 LIQUIDITY RISK

Liquidity is a bank's ability to ensure the availability of funds to meet all on a off balance sheet commitments as reasonable price at all times. Again liquid risk is the current or prospective risk to earnings and capital arising from a banl in ability to meet its liabilities when they become due, without incurri unacceptable losses as well as from opportunity losses due over liquidity relati to its liabilities.

Banks have ability to meet its liabilities as they become due can reduce tl possibility of an adverse situation developing. Liquidity shortfall in one instituti can have repercussions on the entire system affecting other derivatives inte linked with each other banks should measure not only the liquidity requiremen but also examine how liquidity requirement are likely to evolve under cris period. Banks are using maturity ladder as standard tool for measuring n surplus/deficit of fund at selected maturity dates. The maturity profile is used f measuring future cash flows of banks in different time buckets which are distributed as under :

a. Next day
b. 2 to 7 days
c. 7 days to 1 month
d. 1 to 3 months
e. 3 to 6 months
f. 6 months to 1 year
g. 1 year to 2 years
h. 2 to 3 years
i. 3 to 4 years
j. 4 to 5 years
k. Over 5 years

Within each time bucket there could be mismatches depending on cash inflow/outflow. While mismatch upto one year would be relevant since these provide early warning signal of impending liquidity problems, the main focus would be on the short term mismatches viz. 1 to 14 days and 15 to 28 days. Banks are, however, expected to monitor their cumulative mismatches across all time buckets by establishing internal prudential limits with ALCO. The mismatch (Negative gap) during 1 to 14 days and 15 to 28 days in normal course may not exceed 20 percent of cash outflows in each time-bucket. Big banks with large branch network can afford to have larger tolerance level in mismatches in the long run if their term deposit base is quite high.

An example of Assets Liabilities maturity analysis of "X" Bank is shown in Appendix-1

Banks' traditionally use the statutory liquidity reserve and their borrowing capacity in the volatile inter-bank money market as the source of liquidity. But a conscious approach to measure and monitor the liquidity is somewhat lacking in our market. We can learn and draw immense benefit by sharing the best practices, tools and techniques of liquidity management.

3.00 INTEREST RATE RISK

Interest rate risk is the risk that bank earnings and/or net worth will be influence adversely by unanticipated changes in interest rates, i.e., it is the risk wher changes in market interest rates adversely affect a bank's financial positio having impact on interest income and on bank's market value of equity or ne worth. To monitor the interest rate risk bank should prepare gap analysis whic measure mismatch between the rate sensitive liabilities and rate sensitive assets All investments, advances, deposits, borrowings etc., that mature/repriced withi a specified time frame are interest rate sensitive.

The gap may be identified in the following time buckets :

a. Next day
b. 2 to 7 days
c. 7 days to 1 month
d. 1 to 3 months
e. 3 to 6 months
f. 6 months to 1 year
g. 1 year to 2 years
h. 2 to 3 years
i. 3 to 4 years
j. 4 to 5 years
k. Over 5 years

An example of the above is shown

	Variable/1D		2D-1M		1-6M		6-12M		1-5Y		5Y+	
Total Assets	950	10%	2,200	11%	6,50	10%	150	12%	1,800	14%	500	14.5%
Total Liabilities	- 2,200	5%	- 3,250	5.5%	- 150	7%	- 250	10%	- 400	0%	- 0	0%
Fwd. Contracts	0		150		100		0		0		0	
Net Mismatch	- 1,250		-900		600		- 100		1400		500	

The gap is the difference between the rate sensitive assets and rate sensitive liabilities for each time bucket.

The positive gap indicates that it has more RSAs than RSLs whereas negative gap indicates that it has more RSLs than RSAs. The institution in position in positive gap position may be benefited from rising interest rate of assets or in negative gap position may be benefited from declining interest rates of liabilities.

Excessive interest rate risk can pose a significant threat to a bank's earnings and capital base. 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. Changes in interest rates also affect the underlying value of the bank's assets, liabilities and off-balance sheet instruments because the present value of future cash flows (And in some cases, the cash flows themselves) change when interest rates change. Accordingly an effective risk management process that maintains interest rate risk within prudent levels is essential to the safety and soundness of banks.

4.00 CAPITAL ADEQUACY

The need to adopt the best international practices, given the globalisation of economies and businesses. As you are aware of "Basel Committee on Banking Supervision" and the emphasis on maintaining the capital adequacy commensurate to exposure or risk on balance sheet. The new "Basel Capital Accord" stipulates that "Banks must hold capital commensurate with the level of interest rate risk they undertake".

As mentioned earlier, changes in interest rates expose banks to the risk of loss which may, in extreme cases, threaten the survival of the institution. In addition to adequate systems and controls, capital has an important role to play in mitigating and supporting this risk. As part of sound management, banks translate the level of interest rate risk they undertake, whether as part of their trading or non-trading activities, into their over all evaluation of capital adequacy, although there is no general agreement on the methodologies to be used in this process. In cases where banks undertake significant interest rate risk in the course of their business strategy, a substantial amount of capital should be allocated specifically to support this risk.

APPENDIX-I

Asset Liability Maturity Analysis of "X" Bank as on 31 December-2003

(Taka in crore)

Particulars	Upto 01 month	01 to 03 months	03 to 12 months	01 to 05 years	More than 05 years	Total
Assets:						
Cash in hand	928	-	-	-	-	928
Balance with Other Banks and Financial Institutions	157	40	52	74	-	323
Money at call and short notice	440	-	-	-	-	440
Investment	32	264	157	1608	219	2280
Loans and Advances	1277	2445	3844	1454	1123	10143
Fixed Assets including Premises	0	-	-	18	72	90
Other Assets	253	245	50	72	800	1420
Total Assets	3087	2994	4103	3226	2214	15624
Liabilities :						
Borrowing from Bangladesh Bank, Other Banks, Financial Institutions & Agents.	(220)	-	-	-	-	(220)
Deposits :	(3920)	(2644)	(3927)	(1102)	(1489)	(13082)
Other Accounts	(474)	(85)	-	(214)	-	(773)
Provision and Other Liabilities	-	(11)	(175)	(351)	(700)	(1237)
Total Liabilities:	(4614)	(2740)	(4102)	(1667)	(2189)	(15312)
Customer's commitments		(300)	00	00	00	(300)
Net Mismatch	(1527)	(46)	1	1559	25	12
Cumulative Net Mismatch	(1527)	(1573)	(1572)	(13)	12	12

This Cumulative Net Mismatch that is surplus liquidity can be managed through short term investment (upto one month bucket) reducing long term investm ents of increasing inflow in upto one month bucket.

APPENDIX-II

A Demo ALCO Minutes

ACTION POINTS ("X" Bank) ALCO MEETING (Mar-03.2003)			**Attendees :** CEO (Name) Head of Corporate Banking (Name) Head of Consumer Banking (Name) Head of Treasury (Name) Head of Operations (Name) Head of Credit (Name) Head of Finance (Name)	
Date	Item No.	Section	Issue and proposed action	To be Action by (initials) (Date)
03-03-03	I	PREVIOUS MINUTES	I. Revision to customer interest rates were to be discussed & new rates to be established. Deposit growth to be reviewed.	
	2	ECONOMY MARKET	I. No significant change in macro-economic factors other than inflationary growth. 2. Inflation rose to 4.57% in November 2002 highest since FY 1999. 3. Foreign Exchange Reserve stands at US$ 1.78 bio in February, 2003 4. Board Money (M2) recorded an increase of 5.29% during July-Dec., 2002 period compared to same period last year. 5. ADP is expected to cut to BDT 16.5 bio from BDT 19.0 bio for FY 2003 6. Overnight rates in the downtrend after Eid. 7. Treasury Bill yield curve is expected to be stable with no major change in sight. 8. Secondary Market for Treasury Bills is emphasised the BBK.	
	3	LIQUIDITY	1. AD ratio has increased since the last meeting in February, 2003 2. Lcy Deposits has no major change in February. 3. Assets have grown by approx BDT 250 mio in February. 4. Inter-bank borrowing is approx BDT 1.000 mio. 5. AD ratio still within limits but there is clearly a need to grow our core deposit base and reduce reliance on inter-bank. 6. Medium Term Funding Ratio has improved due to growth in longer term deposits.	
	4	PRICING	1. Need to mobilise deposits on an urgent basis to reduce inter-bank dependency 2. Growth of Advance and Deposits should be synchronised.	
	5	ACTION	1. Introduce new (increased) customer rates to encourage deposit accretion and emphasize need to focus on account profitabiliity for assets w.e.f 1st March. 2. Finance to determine impact of new rates on avg. CB and C & I Balance Sheet of Jan`03 and advised ALCO 3. Contingency action plan to manage stressed liquidity discussed & agreed.	

APPENDIX-III

LIQUIDITY CONTINGENCY PLAN

"X" BANK

CONTINGENCY ACTION PLAN TO MANAGE STRESSED LIQUIDITY

SCOPE

To establish an action plan to manage a stressed liquidity situation created by a name problem in the market.

PURPOSE OF THE PLAN

To provide a framework within which an effective response to a liquidity crisis can be managed.

N. B. : Stressed liquidity is defined as a condition that arises from a sudden deterioration of the perceived safety and credibility of the bank, resulting in substantial withdrawal of funds by depositors.

TRIGGER POINTS

Plan to be activated when two or more of the following conditions exist :

1. Bangladesh Bank has declined to open the Rediscount/Repo window at our request.
2. Call money market rates have exceeded 25% for more than 7 consecutive days.
3. Call facilities have been declined by the market or a premium over market rates has been imposed on our borrowing.
4. Consolidated AD ratio has exceeded 100% for more than 15 days.

Version Date : February, 2003 Approved at ALCO Meeting, March 03, 2003

"X" Bank
CONTINGENCY ACTION PLAN TO MANAGE STRESSED LIQUIDITY

PHASE 1 - IMPENDING CRISIS	
1. Phase 1-Team	
* Deputy Managing Director-1 : Chairman * General Manager, Fund Management Division : Member * General Manager, Overseas Banking Division : Member * General Manager, Local Office : Member * Deputy General Manager, Overseas Banking Division (OBD) : Member * Deputy General Manager, Fund Management Division : Member-Secretary	
2. Action Points	**Responsibility**
2.1 Investigate the underlying cause of the crisis to establish : * Extend and timing of the crisis * Duration of the crisis * Remedial action to avoid the crisis, agree any external / internal communications statement etc.	ALM Desk
2.2 Advise all Divisional Heads of the crisis and cancel leave commitments of key personnel.	DMD-1
2.3 Review liquid and market assets portfolio by maturity and prepare a liquidation strategy.	GM, FMD
2.4 Liquidate any long forex positions and reduce forex open position to a minimum.	GM, Overseas Banking Division

"X" Bank
CONTINGENCY ACTION PLAN TO MANAGE STRESSED LIQUIDITY

PHASE 2 - CRISIS SITUATION

1. Phase 1-Team

✳ Deputy Managing Director-1	: Chairman
✳ General Manager, Fund Management Division	: Member
✳ General Manager, Overseas Banking Division	: Member
✳ General Manager, Local Office	: Member
✳ Deputy General Manager, Overseas Banking Division (OBD)	: Member
✳ Deputy General Manager, Fund Management Division	: Member-Secretary

2. Action Points	Responsibility
2.1 Communication	
2.1.1 Convene Emergency ALCO Meeting to review the crisis, agree content of any external / internal messages and delegate tasks..	DMD-1
2.1.2 Inform Bangladesh Bank of crisis and proposed remedial action, if deemed necessary.	DMD-1
2.1.3 Brief Relationship Managers and Branch Managers.	GM, FMD
2.1.4 Brief Dealers	DGM, Overseas Banking Division

"X" Bank
CONTINGENCY ACTION PLAN TO MANAGE STRESSED LIQUIDITY

PHASE 2 - CRISIS SITUATION (Cont.)	
2.2 Assessment and Action	**Responsibility**
2.2.1 Confirm the liquid and market asset portfolio for initial selective liquidation	GM- FMD/ DGM- FMD
2.2.2 Assess the level of inter-bank borrowing capacity and raise funds to meet liquidity .	GM- FMD/ DGM- FMD
2.2.3 Approach Bangladesh Bank for Repo.	DGM- FMD
2.2.4 Selling Fcy from forex open position limit to generate Lcy liquidity.	DGM, Overseas Banking Div.
2.2.5 Approach Bangladesh Bank for extended use of the rediscount window.	GM- FMD
2.2.6 Monitor closely withdrawal patterns, under report to Head of Treasury.	DGM- FMD
2.2.7 Do not approve early redemption of deposits without specific approval of DMD/GM, FMD	DGM- FMD
2.2.8 Assess overall level of loans/OD and ensure no incremental draw down. No excess to be allowed.	DGM- FMD
2.2.9 Assess overall Advances portfolio and activate plan contract/recall/seek repayment from customers.	DGM- FMD

"X" Bank
CONTINGENCY ACTION PLAN TO MANAGE STRESSED LIQUIDITY

Government and/or Central Bank Statutory Holdings Liquidity Requirements

Regulation	Parameter/Formula	Comprising
Cash Reserve	4.5% of Liabilities	Lcy Cash at Central Bank
Liquidity Reserve	11.5% of Liabilities	Treasury Bills Cash in Tills Fcy balance with Central Bank Lcy balance with Central Bank Selected Govt. Bonds

Money Market Instruments Comprising Marketable Securities and Reserve Liquidity

Instrument	Features/Restrictions	Included in Marketable Or Reserve
Treasury Bills	Issued by Central Bank weekly auction at discount Tenors are 28, 91, 182, 364 days & 2 years.	M & R

Amount of Contingency Fund for liquidity required from specific sources.

"X" Bank **CONTINGENCY ACTION PLAN TO MANAGE STRESSED LIQUIDITY**

QUANTIFICATION OF AMOUNT OF CONTINGENCY FUNDS - LOCAL CURRENCY

BDT IN MILLION

Source of contingency funds during stressed liquidity	Estimated Maximum Available Funds	Cost to "X"
Money Market • Term Deposit	Amount as and when required	Acceptable Interest rate in Market
Central Bank (Marketable Securities and Reserve Portfolio)	do	do
• Repo facility for Treasury Bills	do	do
• Rediscounting window	do	do
• Balance with CB (Excess of CRR)	do	do
Others • Lcy Cash in hand		