Prime Bank Limited
Head Office, Dhaka

Market Discipline Risk Based Capital Adequacy (Basel-II)

The purpose of Market Discipline in (Basel-II) is to establish more transparent and disciplined financial market so that stakeholders can assess the position of a bank regarding holding of assets and to identify the risks relating to the assets and capital adequacy to meet probable loss of assets. For the said purpose, this "Disclosures on Risk Based Capital (Basel-II)" is made as per Bangladesh Bank's Guideline.

1. Scope of Application

	Quantitative disclosures	
a)	The name of the top corporate entity in the group to which this guidelines applies.	**Prime Bank Limited**
b)	An outline of differences in the basis of consolidation for accounting and regulatory purposes, with a brief description of the entities within the group (a) that are fully consolidated; (b) that are given a deduction treatment; and (c) that are neither consolidated nor deducted (e.g. where the investment is risk-weighted).	Prime Bank Limited has 4 (Four) subsidiaries- (i) Prime Exchange Co. Pte. Limited, Singapore (ii) Prime Bank Investment limited, (iii) PBL Exchange (UK) Limited and (iv) Prime Bank Securities Limited, and **A brief description of the Bank and its subsidiaries are given below:** **Prime Bank Limited** The Prime Bank Limited (PBL) was incorporated as a public limited company in Bangladesh under Companies Act, 1994. It commenced its banking business with one branch from April 17, 1995 under the license issued by Bangladesh Bank. Presently the Bank has 94 (Ninety Four) branches, 14 (Fourteen) SME Branches / Centers all over Bangladesh, and 2 (two) booths located at Dhaka Club, Dhaka and at Chittagong Port, Chittagong. The Bank has 3 (Three) Off-shore Banking Units (OBU) operating at Savar, Chittagong and Adamjee EPZ areas. The Bank went for Initial Public Offering in 1999 and its shares are listed with Dhaka Stock Exchange Limited and Chittagong Stock Exchange Limited as a publicly traded company for its general class of shares. The principal activities of the Bank are to provide all kinds of commercial banking services to its customers through its branches. **There are 4 (Four) Subsidiaries of Prime Bank Limited which are as under:** **i) Prime Exchange Co. Pte. Limited, Singapore** Prime Exchange Co. Pte. Ltd., a fully owned subsidiary company of Prime Bank Limited was incorporated in Singapore on January 06, 2006 and commenced its remittance business from July 08, 2006. The principal activities of the company are to carry on the remittance business and to undertake and participate in transactions, activities and operations commonly carried on or undertaken by remittance and exchange house. **ii) Prime Bank Investment Limited** Prime Bank Investment Limited (PBIL) is a subsidiary company of Prime Bank Limited incorporated as a public limited company on April 27, 2010 with the registrar of Joint Stock Companies, vide certificate of incorporation no.C-84266/2 dated 28 April 2010 which has commenced its business on the same date. The main objectives of the company are to carry out the business of full-fledged merchant banking activities like issue management, portfolio management, underwriting, corporate advisory services etc. **iii) PBL Exchange (UK) Limited**

		PBL Exchange (UK) Limited was incorporated as a private limited company with Companies House of England and Wales on November 19, 2009 and commenced its operation on 02 August 2010 with three Branches located at Brick Lane of London, Coventry Road of Birmingham and North Pldham of Manchester. The company is a wholly owned subsidiary of Prime Bank Limited. **iv) Prime Bank Securities Limited** Prime Bank Securities Limited was incorporated on April 29, 2010 as a private limited company under the Companies Act 1994. The main objectives of the company are to carry on business of stock brokers / dealers in relation to shares and securities dealings and other services as mentioned in the Memorandum and Articles of Association of the Company. The operation of the company yet to start.
c)	Any restrictions, or other major impediments, on transfer of funds or regulatory capital within the group.	Not applicable
d)	The aggregate amount of capital deficiencies in all subsidiaries not included in the consolidation that are deducted and the name(s) of such subsidiaries.	Not applicable

2. Capital Structures

	Qualitative disclosures	
a)	Summary information on the terms and conditions of the main features of all capital instruments, especially in the case of capital instruments eligible for inclusion in **Tier 1** or in **Tier 2**.	As per the guidelines of Bangladesh Bank, **Tier-1 Capital** of PBL consists of (i) Fully Paid-up Capital, (ii) Non-repayable Share Premium Account, (iii) Statutory Reserve, (iv) Retained Earnings and (v) Minority Interest in Subsidiaries. **Tier-2 Capital** consists of applicable amount of (i) General Provision (against unclassified Loans/Investments, Off-Balance Sheet exposure & Off-Shore Banking Units), 50% of Asset Revaluation Reserve, 50% of Revaluation gain/loss on Investment (HFT), 10% of Revaluation Reserve for Equity Instruments, PBL unsecured nonconvertible Sub-ordinate bond as approved by Bangladesh Bank and Exchange Equalization Fund.

	Quantitative disclosures		
b)	**The amount of Tier-1 capital, with separate disclosure of**		
	Particulars	**Solo**	**Consolidated**
		Taka in Million	
	I. Fully Paid up capital	5,776.37	5,776.37
	II. Non repayable share premium account	2,241.23	2,241.23
	III. Statutory reserve	4,391.63	4,391.63
	IV. General reserve	-	-
	V. Retained earnings	2,691.26	3,383.90
	VI. Minority interest in subsidiaries	-	0.00
	VII. Non-cumulative irredeemable preference shares	-	-
	VIII. Dividend equalization account	-	-
	Sub-Total (A)	**15,100.49**	**15,793.13**
c)	**The total amount of Tier 2 and Tier 3 capital (B)**	**Solo**	**Consolidated**

		Taka in Million	
	i) Amount of Tier 2 capital	5,671.61	5,691.71
	ii) Amount of Tier 3 capital	-	-
	Total amount of Tier 2 and Tier 3 capital (B)	**5,671.61**	**5,691.71**
d)	**Other deductions from capital**	**-**	**-**
e)	**Total eligible capital (A+B)**	**20,772.10**	**21,484.84**

3. Capital Adequacy

	Qualitative disclosures	
a)	A summary discussion of the bank's approach to assessing the adequacy of its capital to support current and future activities.	a) The Bank has adopted Standardized Approach (SA) for computation of capital charge for credit risk and market risk, and Basic Indicator Approach (BIA) for operational risk. Assessment of capital adequacy is carried out in conjunction with the capital adequacy reporting to the Bangladesh Bank. The Bank has consolidated capital adequacy ratio of **11.69%** as against the minimum regulatory requirement of **9%.** Tier-I capital adequacy ratio is **8.60%** against the minimum regulatory requirement of **5%.** The Bank's policy is to manage and maintain its capital with the objective of maintaining strong capital ratio and high rating. The Bank maintains capital levels that are sufficient to absorb all material risks. The Bank also ensures that the capital levels comply with regulatory requirements and satisfy the external rating agencies and other stakeholders including depositors. The whole objective of the capital management process in the Bank is to ensure that the Bank remains adequately capitalized at all times.

	Quantitative disclosures		
	Particulars	**Solo**	**Consolidated**
		Taka in Million	
b)	Capital requirement for credit risk	14,543.87	14,336.52
c)	Capital requirement for market risk	687.27	906.64
d)	Capital requirement for operational risk	1,232.85	1,294.06
e)	Total and Tier 1 capital ratio	72.70%	73.51%
	Minimum capital requirement	16,464.00	16,537.20
	Total Risk Weighted Assets (RWA)	182,933.20	183,746.90
	Total and Tier-1 Capital Ratio:		
	Total CAR	11.36%	11.69%
	Tier-1 CAR	8.25%	8.60%
	Tier-2 CAR	3.10	3.10%

4. <u>Credit Risk:</u>

<table>
<tr><td rowspan="3">a)</td><td colspan="2">Qualitative disclosures</td></tr>
<tr><td colspan="2">The general qualitative disclosure requirement with respect to credit risk, including:</td></tr>
<tr><td>i) Definitions of past due and impaired (for accounting purposes);</td><td>With a view to strengthening credit discipline and bring classification and provisioning regulation in the line with international standard, a phase wise program for classification and provisioning was undertaken by the Bank as per Bangladesh Bank circulars issued from time to time. In this regard, all the loans and advances are grouped into four (4) categories for the purpose of classification, namely (i) Continuous Loan, (ii) Demand Loan, (iii) Fixed Term Loan and (iv) Short-term Agricultural and Micro Credit. The above loans are classified as follows:

Continuous & Demand Loan are classified as under:

➢ Sub-standard- if it is past due/over due for 6 months or beyond but less than 9 months;
➢ Doubtful- if it is past due/overdue for 9 months or beyond but less than 12 months;
➢ Bad/Loss- if it is past due/overdue for 12 months or beyond.

Fixed Term Loan (repayable within maximum 5 years of time) are classified as:

➢ Sub-standard- if the defaulted installment is equal to or more than the amount of installment (s) due within 6 (six) months, the entire loans are classified as “Sub-standard”.
➢ Doubtful- if the defaulted installment is equal to or more than the amount of installment (s) due within 12 (twelve) months, the entire loans are classified as “Doubtful.
➢ Bad/Loss- if the defaulted installment is equal to or more than the amount of installment (s) due within 18 (eighteen) months, the entire loans are classified as “Bad/Los”.

Fixed Term Loan (repayable more than 5 years of time) are classified as:

➢ Sub-standard- if the defaulted installment is equal to or more than the amount of installment (s) due within 12 (twelve) months, the entire loans are classified as “Sub-standard”.
➢ Doubtful- if the defaulted installment is equal to or more than the amount of installment (s) due within 18 (eighteen) months, the entire loans are classified as “Doubtful.
➢ Bad/Loss- if the defaulted installment is equal to or more than the amount of installment (s) due within 24 (twenty four) months, the entire loans are classified as “Bad/Los”.

Short-term Agricultural and Micro Credit are classified as:

➢ Sub-standard- if the irregular status continue after a period of 12 (twelve) months, the credits are classified as “Sub-standard”.
➢ Doubtful- if the irregular status continue after a period of 36 (thirty six) months, the credits are classified as “Doubtful”.
➢ Bad/Loss- if the irregular status continue after a period of 60 (sixty) months, the credits are classified as “Bad/Loss”.

A Continuous Credit, Demand loan or Term Loan which will remain over due for a period of 90 days or more, are treated “Special Mention Account (SMA)”.</td></tr>
</table>

<table>
<tr><td></td><td>ii) Description of approaches followed for specific and general allowances and statistical methods;</td><td>

The Bank is following the general and specific provision for loans and advances / investments on the basis of Bangladesh Bank guidelines issued from time to time. The provision rates are given below:

<table>
<tr><th>Particulars</th><th>Rate</th></tr>
<tr><td>General provision on unclassified general loans and advances / investments.</td><td>1%</td></tr>
<tr><td>General provision on unclassified small enterprise financing.</td><td>1%</td></tr>
<tr><td>General provision on unclassified loans / investments for housing.</td><td>2%</td></tr>
<tr><td>General provision on unclassified consumer financing other than housing finance, loan for professionals and loans to share business.</td><td>5%</td></tr>
<tr><td>General provision on special mention account.</td><td>5%</td></tr>
<tr><td>Specific provision on substandard loans and advances / investments.</td><td>20%</td></tr>
<tr><td>Specific provision on doubtful loans and advances / investments.</td><td>50%</td></tr>
<tr><td>Specific provision on bad / loss loans and advances / investments.</td><td>100%</td></tr>
</table>
</td></tr>
<tr><td>b)</td><td>Total gross credit risk exposures broken down by major types of credit exposure.</td><td>

Total gross credit risk exposures broken down by major types of credit exposure of the Bank:

<table>
<tr><th>Particulars</th><th>Taka in Million</th></tr>
<tr><td>Secured Overdraft/Quard Against TDR</td><td>23,052.86</td></tr>
<tr><td>Cash Credit/Mudaraba</td><td>14,915.77</td></tr>
<tr><td>Loan (General)</td><td>18,426.70</td></tr>
<tr><td>House Building Loan</td><td>3,435.34</td></tr>
<tr><td>Loan Against Trust Receipts (LTR)</td><td>19,014.81</td></tr>
<tr><td>Payment Against Documents (PAD)</td><td>733.76</td></tr>
<tr><td>Retail Loan</td><td>9,290.65</td></tr>
<tr><td>Lease Finance/Izara</td><td>6,037.07</td></tr>
<tr><td>Credit Card</td><td>517.06</td></tr>
<tr><td>SME Loan</td><td>1,086.98</td></tr>
<tr><td>Hire Purchase</td><td>4,710.73</td></tr>
<tr><td>Other Loans & Advances</td><td>2,969.34</td></tr>
<tr><td>Bill purchased/discounted-Inland</td><td>5,958.77</td></tr>
<tr><td>Bill purchased/discounted-Foreign</td><td>1,017.55</td></tr>
<tr><td>Total</td><td>111,167.39</td></tr>
</table>
</td></tr>
<tr><td>c)</td><td>Geographica1 distribution of exposures, broken down in significant areas by major types of credit exposure.</td><td>

Geographical distribution of exposures, broken down in significant areas by major types of credit exposure of the Bank:

<table>
<tr><th>Particulars</th><th>Taka in Million</th></tr>
<tr><td>Urban:</td><td></td></tr>
<tr><td>Dhaka Zone</td><td>80,606.15</td></tr>
<tr><td>Chittagong Zone</td><td>17,265.64</td></tr>
<tr><td>Khulna Zone</td><td>4,388.36</td></tr>
<tr><td>Rajshahi Zone</td><td>1,482.86</td></tr>
<tr><td>Barishal Zone</td><td>178.74</td></tr>
<tr><td>Sylhet Zone</td><td>4,210.68</td></tr>
<tr><td>Sub-Total</td><td>108,132.43</td></tr>
<tr><td>Rural:</td><td></td></tr>
<tr><td>Dhaka Zone</td><td>1,858.98</td></tr>
<tr><td>Chittagong Zone</td><td>519.70</td></tr>
<tr><td>Khulna Zone</td><td>-</td></tr>
<tr><td>Rajshahi Zone</td><td>57.54</td></tr>
<tr><td>Barishal Zone</td><td>-</td></tr>
<tr><td>Sylhet Zone</td><td>598.74</td></tr>
<tr><td>Sub-Total</td><td>3,034.96</td></tr>
<tr><td>Grand Total (Urban and Rural)</td><td>111,167.39</td></tr>
</table>
</td></tr>
</table>

d)	Industry or counterparty type distribution of exposures, broken down by major types of credit exposure.	**Industry or counterparty type distribution of exposures, broken down by major types of credit exposure of the Bank:**

Particulars	Taka in Million
Commercial Lending	19,564.27
Export Financing	9,363.16
House Building Loan	3,435.34
Retail Loan	9,290.65
Small & Medium Enterprises (SME)	5,757.28
Special Program Loan	-
Other Loans & Advances (SOD)	17,204.59
Staff Loan	13.78
Loans, Advances & Lease/Investments to Managing Director / CEO and other senior executives	1,246.55
Industrial Loans/Investments **(Details are given below)**	45,291.77
Total	**111,167.39**

Industrial Loans/Investments

Agriculture	1,871.46
Textile Industries	11,676.55
Food and allied industries	2,014.45
Pharmaceutical Industries	1,446.40
Leather , Chemical, Cosmetics, etc.	1,278.59
Tobacco Industries	45.58
Cement and Ceramic Industries	2,140.14
Service Industries	2,915.10
Transport & Communication Industries	3,678.26
Other Industries including bills purchased and discounted	18,225.24
Total	**45,291.77**

e)	Residual contractual maturity breakdown of the whole portfolio, broken down by major types of credit exposure.	**Residual contractual maturity break down of the whole portfolios, broken down by major types of credit exposure of the Bank:**

Particulars	Taka in Million
Repayable on Demand	-
Up to 1 month	23,942.56
Over 1 month but not more than 3 months	21,204.14
Over 3 months but not more than 1 year	38,206.61
Over 1 year but not more than 5 years	25,680.57
Over 5 years	2,133.51
Total	**111,167.39**

f)	**By major industry or counterparty type:**	
	i) Amount of impaired loans and if available, past due loans, provided separately;	**The amount of classified and unclassified loans and advances/investments are given below as per Bangladesh Bank guidelines:**

Particulars	Taka in Million
Continuous Loan	208.14
Demand Loans	369.48
Term Loans up to 5 years	745.20
Term Loans over 5 years	44.87
Short Term Agro Credit and Micro Credit	-
Total	**1,367.69**

<table>
<tr><td></td><td>ii) Specific and general provisions; and</td><td colspan="2">Specific and general provisions were made on the amount of classified and unclassified loans and advances/investments, off-balance sheet exposures and off-shore banking units as per Bangladesh Bank guidelines:</td></tr>
<tr><td></td><td></td><td>Particulars</td><td>Taka in Million</td></tr>
<tr><td></td><td></td><td>Provision on classified loans and advances/investments</td><td>642.14</td></tr>
<tr><td></td><td></td><td>Provision on unclassified loans and advances/investments</td><td>1,462.56</td></tr>
<tr><td></td><td></td><td>Provision on Off-balance sheet exposures</td><td>810.00</td></tr>
<tr><td></td><td></td><td>Provision for Off-shore Banking Units</td><td>60.50</td></tr>
<tr><td></td><td></td><td>Total</td><td>2,975.20</td></tr>
<tr><td></td><td>iii) Charges for specific allowances and charge-offs during the period.</td><td colspan="2">During the year the specific and general provisions were made on the amount of classified and unclassified of loans and advances/investments, off-balance sheet exposure and off-shore banking units as per Bangladesh Bank guidelines:</td></tr>
<tr><td></td><td></td><td>Particulars</td><td>Taka in Million</td></tr>
<tr><td></td><td></td><td>Provision on classified loans and advances/investments</td><td>120.00</td></tr>
<tr><td></td><td></td><td>Provision on unclassified loans and advances/investments</td><td>120.00</td></tr>
<tr><td></td><td></td><td>Provision on Off-balance sheet exposures</td><td>270.00</td></tr>
<tr><td></td><td></td><td>Provision for Off-shore Banking Units</td><td>30.00</td></tr>
<tr><td></td><td></td><td>Total</td><td>540.00</td></tr>
</table>

<table>
<tr><td>g)</td><td colspan="3">Gross Non Performing Assets (NPAs)</td></tr>
<tr><td></td><td colspan="3">Non Performing Assets (NPAs) to Outstanding loans and advances</td></tr>
<tr><td></td><td>Movement of Non Performing Assets (NPAs).</td><td>Particulars</td><td>Taka in Million</td></tr>
<tr><td></td><td></td><td>Opening balance</td><td>1,149.10</td></tr>
<tr><td></td><td></td><td>Additions</td><td>218.59</td></tr>
<tr><td></td><td></td><td>Reductions</td><td>-</td></tr>
<tr><td></td><td></td><td>Closing balance</td><td>1,367.69</td></tr>
<tr><td></td><td colspan="3"></td></tr>
<tr><td></td><td>Movement of specific provisions for NPAs.</td><td>Opening balance</td><td>631.14</td></tr>
<tr><td></td><td></td><td>Provisions made during the period</td><td>120.00</td></tr>
<tr><td></td><td></td><td>Write-off</td><td>(257.23)</td></tr>
<tr><td></td><td></td><td>Write-back of excess provisions</td><td>298.23</td></tr>
<tr><td></td><td></td><td>Provision no longer required</td><td>(150.00)</td></tr>
<tr><td></td><td></td><td>Closing Balance</td><td>642.14</td></tr>
</table>

5. Equities: Disclosures for Banking Book Position

<table>
<tr><td>a)</td><td colspan="2">Qualitative disclosures</td></tr>
<tr><td></td><td colspan="2">The general qualitative disclosures requirement with respect to equity risk, including</td></tr>
<tr><td></td><td>• Differentiation between holdings on which capital gains are expected and those taken under other objectives including for relationship and strategic reasons; and</td><td>Investment in equity securities are broadly categorized into two parts:

i) Quoted Securities (Common or Preference Shares & Mutual Fund) that are traded in the secondary market (Trading Book Assets).

ii) Unquoted securities are categorized as banking book equity exposures which are further sub-divided into two groups: unquoted securities which are invested without any expectation that these will be quoted in near future i.e. held for maturity (HFM). And securities those are acquired under private placement or IPO and are going to be traded in the secondary market after completing required formalities. Unquoted securities are valued at cost.</td></tr>
</table>

	• Discussion of important policies covering the valuation and accounting of equity holdings in the banking book. This includes the accounting techniques and valuation methodologies used, including key assumptions and practices affecting valuation as well as significant changes in these practices.	The primary aim is to investment in these equity securities for the purpose of capital gain by selling them in future or held for dividend income. Dividends received from these equity securities are accounted for as and when received. Both Quoted and Un-Quoted equity securities are valued at cost and necessary provisions are maintained if the prices fall below the cost price. As per to Bangladesh Bank guidelines, the HFT equity securities are revaluated once in each week using marking to market concept and HTM equity securities are amortized once a year according to Bangladesh Bank guideline. The HTM equity securities are also revaluated if any, are reclassified to HFT category with the approval of Board of Directors.

	Quantitative disclosures		
	Particulars	**Solo**	**Consolidated**
		Taka in Million	
b)	Value disclosed in the balance sheet of investments, as well as the fair value of those investments; for quoted securities, a comparison to publicly quoted share values where the share price is materially different from fair value.	-	1,038.27
c)	The cumulative realized gains (losses) arising from sales and liquidations in the reporting period.	24.78	86.35
d)	• Total unrealized gains (losses).	-	180.48
	• Total latent revaluation gains (losses)	-	-
	• Any amounts of the above included in Tier 2 capital.	-	18.05
e)	**Capital requirements broken down by appropriate equity groupings, consistent with the bank's methodology, as well as the aggregate amounts and the type of equity investments subject to any supervisory provisions regarding regulatory capital requirements:**		
	• Specific Market Risk	-	109.69
	• General Market Risk	-	109.69

6. Interest Rate Risk in the Banking Book (IRRBB)

	Qualitative disclosures	
a)	The general qualitative disclosure requirement including the nature of IRRBB and key assumptions, including assumptions regarding loan prepayments and behavior of non-maturity deposits, and frequency of IRRBB measurement.	Interest rate risk is the risk where changes in market interest rates might adversely affect a bank's financial condition. Changes in interest rates affect both the current earnings (earnings perspective) as well as the net worth of the bank (economic value perspective). Re-pricing risk is often the most apparent source of interest rate risk for a bank and is often gauged by comparing the volume of a bank's assets that mature or re-price within a given time period with the volume of liabilities that do so. The short term impact of changes in interest rates is on the bank's Net Interest Income (NII). In a longer term, changes in interest rates impact the cash flows on the assets, liabilities and off-balance sheet items, giving rise to a risk to the net worth of the bank arising out of all re-pricing mismatches and other interest rate sensitive position. Maturity grouping of rate sensitive assets and liabilities of the bank shows significant positive gap in the first quarter and moderate gap during the rest three quarters. If market rates shifts upward by one percent the bank will enjoy a positive earning to the tune of Tk 61.87 million and vice versa. The impact is very insignificant compared to total revenue of the bank and also within the acceptable limit as stipulated by Bangladesh Bank.

<table>
<tr><td rowspan="10">b)</td><td rowspan="10">Quantitative disclosures

The increase (decline) in earnings or economic value (or relevant measure used by management) for upward and downward rate shocks according to management’s method for measuring IRRBB, broken down by currency (as relevant).</td><td>Particulars</td><td>1-90 days</td><td>Over 3 months to upto 6 months</td><td>Over 6 months to upto 9 months</td><td>Over 9 months to upto 1 year</td></tr>
<tr><td></td><td colspan="4">Taka in Million</td></tr>
<tr><td>Rate Sensitive Assets</td><td>39,611</td><td>15,632</td><td>12,375</td><td>9,121</td></tr>
<tr><td>Rate Sensitive Liabilities</td><td>29,356</td><td>11,926</td><td>5,854</td><td>4,513</td></tr>
<tr><td>GAP</td><td>10,255</td><td>3,707</td><td>6,521</td><td>4,608</td></tr>
<tr><td>Cumulative GAP</td><td>10,255</td><td>13,961</td><td>20,482</td><td>25,091</td></tr>
<tr><td>Adjusted Interest Rate Changes (IRC)</td><td>1.00%</td><td>1.00%</td><td>1.00%</td><td>1.00%</td></tr>
<tr><td>Quarterly earnings impact (Cum. GAP * IRC)</td><td>25.29</td><td>9.14</td><td>16.08</td><td>11.36</td></tr>
<tr><td>Accumulated earning impact to date</td><td>25.29</td><td>34.43</td><td>50.50</td><td>61.87</td></tr>
<tr><td>Earning Impact/ Avg. Quarterly Net Profit</td><td>1.83%</td><td>2.49%</td><td>3.65%</td><td>4.47%</td></tr>
</table>

7. Market Risk:

<table>
<tr><td rowspan="3">a)</td><td colspan="2">Qualitative disclosures</td></tr>
<tr><td>i) Views of Board of Directors (BOD) on trading/ investment activities.</td><td>Market risk is the possibility of losses of assets in balance sheet and off-balance sheet positions arising out of volatility in market variables i.e., interest rate, exchange rate and price. Allocation of capital is required in respect of the exposure to risks deriving from changes in interest rates and equity prices in the bank’s trading book, in respect of exposure to risks deriving from changes in foreign exchange rates and commodity price in the overall banking activity. The total capital requirement for banks against their market risk shall be the sum of capital charges against:

i. Interest rate risk
ii. Equity position risk
iii. Foreign exchange (including gold) position risk throughout the bank’s balance sheet and
iv. Commodity risk.</td></tr>
<tr><td>ii) Methods used to measure Market risk.</td><td>Measurement Methodology

As banks in Bangladesh are now in a stage of developing risk management models, Bangladesh Bank suggested the banks for using Standardized Approach for credit risk capital requirement for banking book and Standardized (rule based) Approach for market risk capital charge in their trading book.

Maturity Method has been prescribed by Bangladesh Bank in determining capital against market risk. In the maturity method, long or short positions in debt securities and other sources of interest rate exposures, including derivative instruments, are slotted into a maturity ladder comprising 13 time-bands (or 15 time-bands in case of low coupon instruments). Fixed-rate instruments are allocated according to the residual term to maturity and floating-rate instruments according to the residual term to the next repricing date.
In Standardized (rule based) Approach the capital requirement for various market risks (interest rate risk, price, and foreign exchange risk) are determined separately.

The total capital requirement in respect of market risk is the sum of capital requirement calculated for each of these market risk sub-categories. e.g.:

a) Capital Charge for Interest Rate Risk = Capital Charge for Specific Risk + Capital Charge for General Market Risk;
b) Capital Charge for Equity Position Risk = Capital Charge for Specific Risk + Capital Charge for General Market Risk;
c) Capital Charge for Foreign Exchange Risk = Capital Charge for General Market Risk;
d) Capital Charge for Commodity Position Risk = Capital charge for general market risk.</td></tr>
</table>

<table>
<tr><td></td><td>iii) Market Risk Management system.</td><td>Treasury Division manages the market risk and ALCO monitors the activities of treasury Division in managing such risk.</td></tr>
<tr><td></td><td>iv) Policies and processes for mitigating market risk.</td><td>To mitigate the several market risks the bank formed Asset Liability Management Committee (ALCO) who monitors the Treasury Division's activities to minimize the market risk. ALCO is primarily responsible for establishing the market risk management and asset liability management of the Bank, procedures thereof, implementing core risk management framework issued by the regulator, best risk management practices followed by globally and ensuring that internal parameters, procedures, practices/polices and risk management prudential limits are adhere to.
The Treasury Division are taking following measures to minimize the several market risks:

i) Foreign exchange risk management:

it is the risk that the bank may suffer losses as a result of adverse exchange rate movement during a period in which it has an open position in an individual foreign currency. This risk measured and monitored by the Treasury Division. To evaluate the extent of foreign exchange risk, a liquidity Gap report prepare for each currency.

ii) Equity Risk

Equity risk is defined as losses due to changes in market price of the equity held. To measure and identify the risk, mark to market valuation to the share investment portfolios are done. Mark to market valuation is done against a predetermined limit. At the time of investment, following factors are taken into consideration:

a) Security of Investment
b) Fundamentals of securities
c) Liquidity of securities
d) Reliability of securities
e) Capital appreciation
f) Risk factors and
g) Implication of taxes etc.</td></tr>
</table>

<table>
<tr><td rowspan="7">b)</td><td colspan="3">Quantitative disclosures</td></tr>
<tr><td colspan="3">The capital requirements for</td></tr>
<tr><td rowspan="2">Particulars</td><td>Solo</td><td>Consolidated</td></tr>
<tr><td colspan="2">Taka in Million</td></tr>
<tr><td>• Interest rate risk</td><td>624.60</td><td>624.60</td></tr>
<tr><td>• Equity position risk</td><td>-</td><td>219.40</td></tr>
<tr><td>• Foreign exchange risk and</td><td>62.70</td><td>62.70</td></tr>
<tr><td></td><td>• Commodity risk</td><td>-</td><td>-</td></tr>
<tr><td></td><td>Total Capital Requirement</td><td>687.30</td><td>906.70</td></tr>
</table>

8. Operational Risk:

	Qualitative disclosures	
a)	i) Views of BOD on system to reduce Operational Risk	Operational risk is defined as the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events. This definition includes legal risk but excludes strategic and reputation risk. It is inherent in every business organization and covers a wide spectrum of issues. The Board of Director (BOD) of the Bank and its Management firmly believe that this risk through a control based environment in which processes see documented, authorization as independent and transactions are reconciled and monitored. This is supported by an independent program of periodic reviews undertaken by internal audit, and by monitoring external operational risk events, which ensure that the group stays in line which industry best practice and takes account or lessons learned from publicized operational failures within the financial services industry. The BOD has also modified its operational risk management process by issuing a high level standard like SOP, supplemented by more detailed formal guidance. This explains how the bank manages operational risk by identifying, assessing, monitoring, controlling and mitigating the risk, rectifying operational risk events, and implementing any additional procedures required for compliance with local regulatory requirements. The Bank maintains and tests contingency facilities to support operations in the event of disasters. Additional reviews and tests are conducted in the event that any branch of the bank is affected by a business disruption event, to incorporate lessons learned in the operational recovery from those circumstances. Plans have been prepared for the continued operation of the bank's business, with reduced staffing levels.
	ii) Performance gap of executives and staffs.	Prime Bank Limited (PBL) considers its employees as a resource, an asset that provides competitive advantage to the organization and on whom organizational success is leveraged as the bank is always prepared and committed to play strategic HR Management. To establish the perfect strategic HR, PBL has developed the linking human resources to strategic goals and objectives in order to improve business performance and develop organizational culture that foster innovation, flexibility and competitive advantage. Here, HR Division functions as a strategic partner in the formulation and implementation of the company's strategies through HR activities such as recruiting, selecting, training, counseling and rewarding personnel. Side by side, this division does research on the future, and offers proactive solutions and strategic advices. HR Division is molding the employees of the future today. To survive and excel in the future, it acquires or develops employees who are multi-skilled, cross-functional, empowered, team players who should be capable not only of improving their work, but reengineering or reinventing it if necessary. This division is working relentlessly to meet the need and desire of the Bank as it believes in service excellence. In the year 2010, HR Division successfully developed and rolled out "Employee Code of Ethics and Business Conduct" throughout the organization as a tool of ensuring good corporate governance. Keeping this in mind and emphasizing on the issue of a constantly changing commercial environment, this year, PBL brought some changes in HR policy level as well. Major activities/achievements include:

		• Developed and made amendment to a few HR policies upon taking approval from the Board of Directors to meet the business need as well as motivating the employees to perform better. • Successfully restructured the hierarchy of Management Trainees as Senior Officers with re-defined career progression and promoting the deserving employees from the Executive Officers (Old) grade to Senior Executive Officer grade based on certain criteria set by the management which mitigated their dissatisfaction; • Formed "Female Employee's Welfare and Grievance Handling Committee" to ensure 'Equal Employment Opportunity'; • Rationalization of manpower by considering the future expansion of business, time series data and trend analysis of manpower. Accordingly, a Table of Establishment (TOE) was prepared consisting of the manpower forecast for three years (2010-2012) for which approval was taken from the Board of Directors; • Provided right quantity of manpower supports at the right time is opening branches; • Formed 'HR Policies, Research and Development Section' which is responsible for updating policies, conducting surveys and provide feedback on employee's motivation, employees Grievances, Conducting Exit Interviews. **HR Future Plan** The HR Division envisages engaging in the following areas: • Implementation of Revised Human Resource Policies; • Substantial review of few existing policies for providing more benefit to employees with a view to introducing superior level of job satisfaction; • Successfully run the activities of "Female employee's Welfare and Grievance Handling Committee" to ensure 'Equal Employment Opportunity'; • Continuous Research and Development (R&D) is important for an organization to gain and maintain the competitive advantage. Research and development reveals the change in lifestyle, social life, price, parity and it also assists in the environmental scanning where both the external and internal environmental factors play a big role. As research seeks to make basic discoveries and uncover new principles or facts so far unknown or unrecognized, Human Resources Training & Development Center of PBL would like to arrange a comprehensive training program on "Applied Marketing Research Methodology".
	iii) Potential external events	**Risk factors/Potential external events:** It is needless to say that there are certain risk factors which are external in nature and can affect the business of the Bank. The factors discussed below can significantly affect the business: • **General business and political condition** PBL's performance greatly depends on the general economic conditions of the country. The effect of recession is still unfolding which may result to slow down in business environment. Political stability is must for growth in business activities.

- **Changes in credit quality of borrowers**

  Risk of deterioration of credit quality of borrowers is inherent in banking business. This could result due to global economic crisis and supply side distortion. The changes in the import prices affected the commodity sectors and ship breaking industry. Deterioration in credit quality requires provisioning.

- **Changes in policies and practices of regulatory bodies to revise practices, pricing and responsibilities of the financial institutions**

  PBL is subject to regulations and compliance of regulation is must. Changes in policies with regard to interest rates, pricing have significant effect on the performance of the Bank. Bangladesh Bank is expected to continue its persuasion to reduce the spread and charges further which is likely to affect the performance. Changes in provisioning requirement will also affect the performance of the bank.

- **Implementation of Basel-II**

  Basel-II is fully effective from 2010 and PBL needs to be complied with respect to credit risk management, its supervision and establishment of effective internal control. The grading of the borrowers and its link with capital requirement may slow down the credit expansion. The establishment of effective control requires more investment in technology and operating expenses are likely to increase.

- **Volatility in equity market**

  Securities and Exchange Commission and the stock exchanges improved their supervisory role but the equity market is still volatile. The recession fear also added to the volatility. If volatility continues it is likely to affect the performance of the bank.

- **Changes in market conditions**

  Changes in market conditions particularly interest rates on deposits and volatility in FX market is likely to affect the performance of the bank. Depositors are becoming increasingly price sensitive and any unilateral upward change by a bank will exert pressure on interest rate structure of the banking sector. It is feared that wage earners remittances may decline due to fall in job opportunity in international market. Unless offset by export performances, there may be pressure in the FX market.

- **The risk of litigation**

  In the ordinary course of business, legal actions, claims by and against the bank may arise. The outcome of such litigation may affect the financial performance of the bank.

- **Success of strategies**

  PBL is proceeding with its strategic plan and its successful implementation is very important for its financial performance. Major deviation due to external and internal factors will affect the performance of the bank.

	iv) Policies and processes for mitigating operational risk.	Prime Bank limited (PBL) has formed a separate 'Risk Management Unit' under Chief Risk Officer to ensure following things:
		• Designing of organizational structure by clearly defining roles and responsibilities of individuals involved in risk taking as well as managing it;
		
		• Formulation of overall risk assessment and management policies, methodologies, guidelines and procedures for risk identification, risk measurement, risk monitoring, defining an acceptable level of risk, mitigation of all the core risks in line with their respective guidelines provided by Bangladesh Bank;
		
		• Reviewing and updating all risks on systematic basis as necessary at least annually, preferably twice a year, ensuring that adequate controls exist and that the related returns reflect these risks and the capital allocated to support them. The main risk areas will be (i) Balance sheet Risk Management, (ii) Credit Risk, (iii) Foreign Exchange Risk, (iv) Internal Control and Compliance Risk, (v) Money Laundering Risk and (vi) IT Risk. The following risks have also to be reviewed:
		  • Operational Risk
		  • Market Risk
		  • Liquidity Risk
		  • Reputation risk
		  • Insurance Risk
		  • Sustainability Risk
		
		• Setting the portfolio objectives and tolerance limits/parameters for each of the risks;
		• Formulation of strategies and different models in consistency with risk management policy based on IT Policy and in house IT support which can measure, monitor and maintain acceptable risk levels of the bank;
		• Development of information systems/MIS inflow and data management capabilities to support the risk management functions of the bank.
		• Ensure compliance with the core risks management guidelines at the department level, and at the desk level;
		• The unit will work under bank's organizational structure and suggest to the CEO to take appropriate measures to overcome any existing and potential financial crisis;
		• Analysis of self resilience capability of the bank;
		• Initiation to measure different market conditions, vulnerability in investing in different sectors;
		• The unit will also work for substantiality of capital to absorb the associated risk in banking operation.
		
		Activities undertaken by "Risk Management Unit" since inception and recent approaches
		
		• Risk Management Unit of PBL is currently arranging monthly meeting on various issues to determine strategies in consistency with risk management policy, which can measure, monitor, and maintain acceptable risk level of the bank. Minutes of each meeting is submitted to Bangladesh Bank on monthly basis;
		• Besides, Risk Management Paper has also been prepared on the basis of 03 months' monthly minutes addressing different areas of risk and their mitigating tools & techniques guided by the members of Risk Management Unit;
		• In order to perform the risk management function smoothly, RMU had invited all the Operational Divisions vide letter to the Head of respective Divisions to form an internal committee along with defined duties of concerned officials. It is to be noted here that due to continuous and successful persuasion, all the Operational Divisions have formulated and established internal risk management committees.

		Stress Testing in PBL: Risk Management Unit (RMU) of PBL has already prepared a stress testing model in line with the Bangladesh Bank's guideline which initially focused on "Simple Sensitivity and Scenario Analysis" on the following five risk factors: • Interest rate; • Forced sale value of collateral; • Non-performing loans (NPLs); • Share prices; and • Foreign exchange rate. The first phase of stress testing based on the financial performance of the bank as of June 30, 2010 has already been furnished and presented to the regulatory authority i.e., Bangladesh Bank and also to the Board of Directors. The result of Stress Testing reflects the strength of this bank to absorb the shocks against all the risk factors. It has been observed that at any level of shocks, the bank will be able to maintain the capital adequacy ratio at the level which is in line with the standard set by Bangladesh Bank. The next phase of stress testing based on the financial performance of the bank as on December 31, 2010 has also been completed which shows that the bank has adequate capital to absorb minor, moderate and major level of shocks. However, in case of cumulative shocks, some additional capital may be required.
	v) Approach for calculating capital charge for operational risk.	The Banks operating in Bangladesh shall compute the capital requirements for operational risk under the Basic Indicator Approach (BIA). Under BIA, the capital charge for operational risk is a fixed percentage, denoted by · (alpha) of average positive annual gross income of the bank over the past three years. Figures for any year in which annual gross income is negative or zero, should be excluded from both the numerator and denominator when calculating the average. The capital charge may be expressed as follows: $K = [(GI\ 1 + GI2 + GI3)\ \alpha]/n$ Where- K = the capital charge under the Basic Indicator Approach GI = only positive annual gross income over the previous three years (i.e., negative or zero gross income if any shall be excluded) α = 15 percent n = number of the previous three years for which gross income is positive. Gross income: Gross Income (GI) is defined as "Net Interest Income" plus "Net non-Interest Income". It is intended that this measure should: i). be gross of any provisions; ii). be gross of operating expenses, including fees paid to outsourcing service providers; iii). exclude realized profits/losses from the sale of securities held to maturity in the banking book; iv). exclude extraordinary or irregular items; v.) exclude income derived from insurance.

	Quantitative disclosures		
	Particulars	**Solo Basis**	**Consolidated**
		Taka in Million	
b)	The capital requirement for operational risk	1,232.85	1,294.06