AUSTRALIA AND NEW ZEALAND BANKING GROUP LIMITED – MUMBAI BRANCH
Basel II: Pillar 3 Disclosures as at 31 March 2013

1. Background

Australia and New Zealand Banking Group Limited – Mumbai Branch ('ANZ India' or 'the Bank') is a branch of Australia and New Zealand Banking Group Limited ('ANZ'), which is incorporated in Australia with Limited Liability.

In October 2010, ANZ received the final approval from the Reserve Bank of India ('RBI') to open a branch in Mumbai to carry out banking business. The Bank commenced its banking business in India from 2 June, 2011. The Bank has only one branch in India as on 31 March 2013.

Disclosures made hereunder are in accordance with Prudential Guidelines on Capital Adequacy and Market Discipline - New Capital Adequacy Framework (NCAF) – Market Discipline (Pillar 3).

2. Key Management Committees, Functions and Frameworks

India Executive Committee ('India EXCO')

India EXCO is the apex committee of the Bank and has the authority to exercise all of the powers and discretions of the Board at the country level. India EXCO takes ownership of the Bank's business in India and fulfils the regulatory responsibility of conducting periodic reviews/ approvals as specified by RBI from time to time. The committee is chaired by Chief Executive Officer India. India EXCO is an in-country committee.

Key responsibilities of the India EXCO are:

- Approving all key business policies.
- Investigating and reviewing policy breaches for credit, operational and market risks; and approving remediation actions.
- Monitoring governance and compliance with Credit, Operational and Market risk management policies, procedures and systems (including risk models) in India and instigating any necessary corrective actions to address deviations.
- Undertaking activities to support the development of new products to be introduced by the Bank.

India Assets and Liabilities Committee ('India ALCO')

India ALCO is a sub-committee of the International and Institutional Banking ALCO ('I&IB ALCO') and is responsible for the oversight and strategic management of the India balance sheet, liquidity and funding positions and capital management activities.

India ALCO's mandate for managing balance sheet, liquidity and funding and capital activities include, but are not limited to:

- Liquidity and funding;
- Capital (book, regulatory and economic);
- Non-traded Interest Rate Risk, including the investment of capital and other non-interest bearing products;

- Balance sheet structure including capital and revenue flows, but excluding traded foreign exchange exposures;
- Approval and oversight of traded market risk;
- Policy, control and compliance activities for all balance sheet, liquidity and funding and capital related risks; and
- Recommendations / noting to I&IB ALCO for any key local decision taken at the ALCO

Risk Management Committee ('India RMC')

India RMC is a sub-committee of regional RMC and acts as a forum to ensure adequate awareness and debate of all significant risk issues that the Bank faces. India RMC has management oversight and presides over credit, operational and market risk within the Bank.

Key responsibilities of the India RMC are:

- Acting as the ultimate point of escalation against agreed Risk/Return standards across division.
- Overseeing Country/Business Level Credit, Operational and Market Risk strategies.
- Recommending country risk strategies.
- Identifying actions and mandating requirements into the resolution of country risk issues.
- Reviewing and approving (for in-country adoption of regionally / globally approved products) country new and amended products/programs, and ensuring that they meet Group Policy parameters.
- Consider key activities across the bank and their risk implications, and action accordingly.

3. Regulatory Framework

The Bank operates as a scheduled commercial bank and is required to maintain capital ratios at par with locally incorporated banks.

Capital Adequacy requirements are outlined in the following circulars:

- Master Circular – Prudential Norms on Capital Adequacy – Basel I Framework;
- Master Circular – Prudential Guidelines on Capital Adequacy and Market Discipline – New Capital Adequacy Framework ('NCAF'), commonly referred as Basel II guidelines.

Presently, banks in India are required to have a parallel run of the revised framework. Banks are required to apply the prudential guidelines on capital adequacy (per both guidelines mentioned above) on an on-going basis and compute their Capital to Risk Weighted Assets Ratio ('CRAR'). Under the parallel run (which continues till 31 March 2013) Banks are required to hold capital sufficient to meet the Basel II minimum capital requirements subject to a prudential floor of 80% of minimum capital requirement computed under the Basel I framework.

As per NCAF, currently Banks should adopt Standardised Approach (SA) for credit risk and Basic Indicator Approach (BIA) for operational risk. Banks shall continue to apply the Standardised Duration Approach (SDA) for computing capital requirement for market risks.

Basel II guidelines are structured around three ‘Pillars’ which are outlined below:

- Pillar 1 sets out minimum regulatory capital requirements
- Pillar 2 sets out key principles for supervisory review of Bank’s risk management framework and its capital adequacy
- Pillar 3 aims to encourage market discipline by developing set of disclosure requirements by banks that allow market participants to assess key pieces of information on the scope of application, capital, risk exposures, risk assessment processes and hence the capital adequacy of the Bank. Further, providing disclosures that are based on a common framework is an effective means of informing the market about exposure to those risks and provides a consistent and comprehensive disclosure framework that enhances comparability.

4. Scope of Application

In terms of RBI circular dated 12 December, 2006 on Financial Regulation of Systemically Important NBFCs and Banks Relationship with them, NBFCs promoted by the parent / group of a foreign bank having presence in India, which is a subsidiary of the foreign bank’s parent / group or where the parent / group is having management control would be treated as part of that foreign bank’s operations in India and brought under the ambit of consolidated supervision. As at 31 March, 2013 no such group owned NBFC is in operations in India, accordingly framework for consolidated supervision does not apply to the Bank.

The bank does not have any subsidiaries in India and consequently not required to prepare Consolidated Financial Statements. The Bank does not have any interest in insurance entities.

5. Capital Structure

Tier 1 capital mainly comprises of

- Interest free capital funds injected by Head Office
- Statutory Reserves calculated at 25% net profits of each year.

Intangible assets, debit balance in Profit and Loss Account have been deducted from above to arrive at Tier I capital.

Tier 2 capital mainly comprises of

- General provision on Standard Assets
- Provision for Country Exposures

The Capital structure as at 31 March, 2013 is as presented below

(Amount in ₹ '000)

Tier I Capital	
Head Office capital	11,311,074
Statutory Reserves	12,302
Debit balance in Profit and Loss Account (Including losses brought forward from Previous period)	(91,653)
Intangibles	(270,538)
Deferred Tax adjustment	(94,419)
Debit balance with Head office	(524,669)
Total Tier I Capital	**10,342,097**
Tier II Capital	
General Provisions and other eligible provisions	147,511
Total Tier II Capital	**147,511**
Total Eligible Capital (Tier I + II Capital)	**10,489,608**

6. Capital Adequacy

The Bank aims to hold sufficient capital to meet the minimum regulatory requirements at all times. The Bank's capital management strategy is two fold:

- To satisfy the Basel II Regulatory Capital requirements set out by RBI in the Master Circular; and
- To minimise the possibility of the Bank's capital falling below the minimum regulatory requirement by maintaining a capital buffer (in excess of the Basel II minimum requirements) sufficient to cover Pillar 2 risks and the capital impact of a moderate (1 in 7 years) or a severe (1 in 25 years) stress scenario over a 1 year horizon.

The Bank's capital management is mainly guided by current capital position, current and future business needs, regulatory environment and strategic business planning. The bank continuously focuses on effective management of risk and corresponding capital to support the risk. India ALCO and India EXCO emphasises on the growth opportunities supported by cost effective capital.

As at 31 March 2013 CRAR stood at 26.39% as per BASEL II norms and 28.11% as per BASEL I norms. The Bank is adequately capitalised presently. Summary of the Bank's capital requirement for credit, market and operational risk and CRAR as at 31 March 2013 is presented below.

(Amount in ₹ '000)

Minimum Regulatory Capital Requirements	
Capital requirements for Credit risk (a)	**3,001,334**
Portfolios subject to standardised approach	3,001,334
Securitisation exposures.	-
Capital requirements for Market risk (b)	**356,664**
Standardised duration approach	
- Interest rate risk	136,164
- Foreign exchange risk (including gold)	220,500
- Equity risk	-
Capital requirements for Operational risk (c)	**219,380**
Basic indicator approach	219,380
Total Minimum Regulatory Capital (a+b+c)	**3,577,378**
Risk Weighted Assets and Contingents	**39,748,641**
Credit Risk	33,348,154
Market Risk	3,962,930
Operational Risk	2,437,557
Capital Ratios	
Tier - I Capital	26.02%
Tier - II Capital	0.37%
Total Capital	26.39%

7. Credit Risk: General Disclosures for all Banks

Structure and organisation of credit risk management

India RMC is responsible for all aspects of risk management, including credit risk. It approves the credit exposure/ concentration limits, risk management policy (involving risk identification, risk measurement/ grading, risk mitigation and control), credit risk management structure, credit pricing policy, etc. in accordance with extant regulatory guidelines. India EXCO is apprised of key risks affecting the business. It ensures country's risk profile remains within the agreed group risk appetite.

The Bank takes credit risk within a well defined framework that lays out the fundamental principles and guidelines for its management. Primary objective is management of risk concentration within risk appetite and within regulator defined prudential limits. This framework is top down and has four main components:

- Credit principles
- Credit policies
- Line of Business/ Segment Specific Procedures
- Organisation and People.

Key aspects of the Bank's Credit Risk Management Policy are

- Analysis of customer risk
- Approval of limits and transactions

- Managing and monitoring customers
- Working out problem loans

Credit is extended on the basis of the Bank's credit risk assessment and credit approval requirements and is not subject to any influences external to these requirements. All legal entities, with which the Bank has or is considering having, a credit relationship, is assigned a credit rating reflecting the probability of default and each facility is assigned a security indicator reflecting the 'loss given default'. Each country to which the Bank has or is considering having, a credit exposure, is assigned a country rating reflecting the risk of economic or political events detrimentally impacting a country's willingness or capacity to secure foreign exchange to service its external debt obligations.

Risk grade assignment and risk grade reviews are subject to approval by the appropriate independent risk representative. Each assigned risk grade is reviewed at an interval (never greater than 1 year) and whenever new material information relating to the customer or facility is obtained or becomes known. The Bank has an effective credit risk management system and clearly documented credit delegations which define levels of authority for credit approval. The quality of all credit relationships is monitored to provide for timely identification of problem credits and prompt application of remedial actions. Problem credits are managed to minimise losses, maximise recoveries and preserve the Bank's reputation, with attention to measurement of extent of impairment, exposure and security cover, provisioning, remediation, workout & losses. Specialist remediation and workout skills will be applied to the management of all problem credits.

Collateral is a means of mitigating the risk involved in providing credit facilities and will be taken where obtainable and necessary to meet risk appetite requirements. Main types of collateral accepted are property, plant & machinery, current assets, cash and stand-by letters of credit. Reliance on collateral is not a substitute for appropriate credit assessment of a customer or be used to compensate for inadequate understanding of the risks. Collateral arrangements for each facility are reviewed annually to confirm the fair value of collateral and to ensure there is no impediment to realisation. The fair value of collateral will be its realisable value net of realisation costs.

7.1 Total gross credit risk exposures as at 31 March, 2013

(Amount in ₹ '000)

Fund Based	
Claims on Banks	8,617,698
Investments (HTM)	-
Loans and Advances	23,766,789
Other Assets and Fixed Assets	4,189,247
Non Fund Based	
Non Market Related Off Balance sheet items (Contingent Credits and Exposures)	10,429,693
Market Related (Foreign Exchange (Fx) and Derivative contracts)	12,716,976

Notes:

Non Fund Based credit risk exposure has been computed as under:

- In case of exposures other than FX and derivative contracts, credit equivalent is arrived at by multiplying the underlying contract or notional principal amounts with the credit conversion factors prescribed by RBI under the Basel II capital framework.

- In case of Foreign exchange and derivative contracts, credit equivalents are computed using the current exposure method as prescribed by RBI.

7.2 Geographic distribution of exposures, Fund based and Non-fund based separately

Since all the exposures provided under Para 7.1 above are domestic, the disclosures on geographic distribution of exposures, both fund and non-fund based has not been made.

7.3 Industry type distribution of exposures as at 31 March, 2013

(Amount in ₹ '000)

Industry Name	Fund Based	Non Fund Based
Food Processing	2,830,849	-
Petroleum, Coal Products and Nuclear Fuels	977,130	117,734
Chemicals and Chemical Products (Dyes, Paints, etc.)	3,780,272	-
Rubber, Plastic and their Products	687,176	7,552
Glass & Glassware	434,280	-
Basic Metal and Metal Products	1,676,932	63,799
Vehicles, Vehicle Parts and Transport Equipments	200,000	31,694
Infrastructure	2,760,000	462,870
Petro-chemicals	-	25,124
Edible Oils and Vanaspati	-	639,809
Fertilisers	-	35,700
Iron and Steel	-	403,005
Drugs and Pharmaceuticals	-	662,498
Sugar	-	24,374
Residuary Other Advances	10,420,150	579,128
Total Loans & Advances	**23,766,789**	**3,053,287**
Claims on Banks	8,617,698	20,093,382
Investments (HTM)	-	**-**
Other Assets and Fixed Assets	4,189,247	**-**
Total Exposure	**36,573,734**	**23,146,669**

Notes:

Fund Based Exposure comprises of Loans & Advances, Claims on Banks and Investment in HTM & Other Assets (including fixed Assets)

Non Fund Based Exposure comprises of Non Market Related Off-Balance sheet items (Contingent Credits and Exposures)

7.4 Residual contractual maturity breakdown of assets as at 31 March, 2013

(Amount in ₹ '000)

	Cash and Bank balances with RBI	Balances with Banks and money at call and short notice	Investments	Advances	Fixed Assets	Other Assets*	Total Assets
Day 1	328,179	1,093,748	2,356,709	683	-	-	**3,779,319**
2 to 7 days	142,587	1,968,300	819,877	1,816,952	-	4,696	**4,752,412**
8 to 14 days	32,444	-	186,552	313,350	-	422	**532,768**
15 to 28 days	77,809	1,750,000	447,402	1,209,559	-	33,328	**3,518,098**
29days and upto 3 months	349,056	4,070,000	2,007,070	10,382,672	-	283,283	**17,092,081**
Over 3 months and upto 6 months	439,271	100,000	2,525,810	3,298,557	-	19,763	**6,383,401**
Over 6 months and upto 1 year	253,876	90,000	1,459,787	3,619,960	-	3,201,258	**8,624,881**
Over 1 year and upto 3 years	20,763	-	119,389	2,387,556	-	2,912	**2,530,620**
Over 3 years and upto 5 years	18	-	104	737,500	-	6,771	**744,393**
Over 5 years	4,776	-	27,461	-	461,703	542,844	**1,036,784**
Total	**1,648,779**	**9,072,048**	**9,950,161**	**23,766,789**	**461,703**	**4,095,277**	**48,994,757**

* Other assets does not include debit balance in Profit and Loss account

7.5 Details of Non-Performing Assets (NPAs) - Gross and Net

(Amount in ₹ '000)

	As at 31 March 2013
Substandard	-
Doubtful 1	-
Doubtful 2	-
Doubtful 3	280,775
Loss	-
Gross NPAs	280,775
Provisions and Interest in Suspense	280,775
Net NPAs	-

7.6 NPA Ratios

(Amount in ₹ '000)

	As at 31 March 2013
Gross NPAs to gross advances	1.17%
Net NPAs to net advances	-

7.7 Movement of NPAs (Gross)

(Amount in ₹ '000)

	For the year ended 31 March 2013
Opening balance	-
Additions	280,775
Reductions	-
Closing balance	280,775

7.8 Movement of provisions for NPAs

(Amount in ₹ '000)

	For the year ended 31 March 2013
Opening balance	-
Provisions made during the period	280,775
Write-off	-
Write-back of excess provisions	-
Closing balance	280,775

7.9 Amount of Non-Performing Investments

There are no non-performing investments as at 31 March 2013.

7.10 Amount of provisions held for Non-Performing Investments

There are no provisions held for non-performing investments as at 31 March 2013 as there are no non performing investments.

7.11 Movement of provisions for depreciation on investments

(Amount in ₹ '000)

	For the year ended 31 March 2013
Opening balance	-
Provisions made during the period	445
Write-off	-
Write-back of excess provisions	-
Closing balance	445

8. Credit Risk: Disclosures for Portfolios Subject to the Standardised Approach

The Bank uses short term / long term issuer rating instruments of the accredited rating agencies viz, CARE, CRISIL, ICRA and Fitch to assign risk weights as per RBI guidelines. For Non resident corporate and foreign banks ratings issued by the international rating agencies like S&P, Moody's and Fitch are used for assigning risk weights.

For assets having a contractual maturity of more than a year long term credit ratings assigned by the above mentioned rating agencies are used.As at 31 March 2013 all of the Bank's exposures were un-rated. Below attached is the summary as at 31 March 2013.

(Amount in ₹ '000)

Nature Of exposure	Gross Credit Exposure	Credit Risk Mitigation	Net Exposure (Before Provision)	Credit Risk weight bucket summary			Deduction from Capital
				< 100%	100%	>100 %	
Fund Based							
Claims on Banks	8,617,698	-	8,617,698	8,617,698	-	-	-
Investments (HTM)	-	-	-	-	-	-	-
Loans and Advances	23,766,789	-	23,766,789	354,607	23,412,181	-	-
Other Assets and Fixed Assets	4,189,247	-	4,189,247	3,449,036	740,211	-	-
Non Fund Based							
Non Market Related Off Balance sheet items (Contingent Credits and Exposures)	10,429,693	-	10,429,693	9,675,208	754,485	-	-
Market Related (Foreign Exchange (FX) and derivative contracts)	12,716,976	-	12,716,976	10,418,174	2,298,802	-	-

9. Credit Risk Mitigation: Disclosures for Standardised Approaches

RBI Basel II guidelines allow following credit risk mitigants to be recognized for regulatory capital purposes under the comprehensive approach

- Eligible financial collateral which included cash (deposited with the Bank), gold, securities issued by Central and State governments, Kisan Vikas Patra, National Savings Certificate, life insurance policies, certain debt securities rated by a recognised credit rating agencies, mutual fund units.
- On balance sheet netting, which is confined to loans and advances and deposits where banks have legally enforceable netting arrangements, involving specific lien with proof of documentation.
- Guarantees where these are direct, explicit, irrevocable and unconditional. Further, the eligible guarantors would comprise :
    - Sovereigns, sovereign entities stipulated as per Basel II guidelines, banks and primary dealers with a lower risk weight than the counterparty;
    - other entities rated AA (-) or better

These credit risk mitigation techniques are subject to specific conditions given in Basel II guidelines.

Main types of collateral accepted by the Bank are property, plant & machinery, current assets, cash and stand-by letters of credit. Collateral arrangements for each facility are reviewed annually to confirm the fair value of collateral and to ensure there is no impediment to realisation. The fair value of collateral will be its realisable value net of realisation costs.

Credit Risk Mitigation details as at 31 March 2013 are as below

(Amount in ₹ '000)

Exposure covered by eligible financial collateral after application of haircuts	NIL
Exposure covered by guarantees	NIL

10. Securitisation Exposures: Disclosure for Standardised Approach

The Bank has not securitised any asset for the year under review hence no disclosures have been made.

11. Market Risk

Market risk is the risk to the Bank's earnings arising from changes in interest rates, currency exchange rates or from fluctuations in bond prices. Market risk arises when changes in market rates, prices and volatilities lead to a decline in the value of assets and liabilities, including financial derivatives. Market risk is generated through both trading and banking book activities.

The Bank conducts trading operations in interest rates, foreign exchange and securities.

The Bank has a detailed risk management and control framework to support its trading and balance sheet activities. The framework incorporates a risk measurement approach to quantify the magnitude of market risk within trading and balance sheet portfolios.

The management of Risk Management is supported by a comprehensive limit and policy framework to control the amount of risk that the Group will accept. Market risk limits are allocated at various levels and are reported and monitored by Market Risk on a daily basis. The detailed limit framework allocates individual limits to manage and control asset classes, risk factors and profit and loss limits (to monitor and manage the performance of the trading portfolios)

To facilitate the management, measurement and reporting of market risk, the Bank has grouped market risk into two broad categories:

- Traded market risk

  This is the risk of loss from changes in the value of financial instruments due to movements in price factors for both physical and derivative trading positions. Trading positions arise from transactions where the Bank acts as principal with customers, financial exchanges or interbank counterparties.

- Non-traded market risk (or balance sheet risk)

  This comprises the management of non-traded interest rate risk and liquidity risk.

Measurement of market risk

A key measure of market risk is Value at Risk (VaR). VaR is a statistical estimate of the possible daily loss and is based on historical market movements.

The Bank measures VaR at a 99% confidence interval. The Group's standard VaR approach for both traded and non-traded risk is historical simulation. The Group calculates VaR using historical changes in market rates, prices and volatilities over the previous 500 business days. Traded and non-traded VaR is calculated using a one-day holding period.

It should be noted that because VaR is driven by actual historical observations, it is not an estimate of the maximum loss that the Bank could experience from an extreme market event. As a result of this limitation, the Bank utilises a number of other risk measures (e.g. stress testing) and risk sensitivity limits to measure and manage market risk.

ANZ also undertakes a wide range of stress tests to the individual trading portfolios. Standard stress tests are applied daily and measure the potential loss impact arising from applying the largest market movements during the previous seven years over specific holding periods. The worst stress losses during the month are reported to the RMC on a monthly basis.

VaR and stress tests are also supplemented by cumulative loss limits and detailed control limits. Cumulative loss limits ensure that in the event of continued losses from a trading activity, the trading activity is stopped and senior management reviews before trading is resumed. Where necessary, detailed control limits such as sensitivity or position limits are also in place to ensure appropriate control is exercised over a specific risk or product.

Back-Testing

Back testing involves the comparison of calculated VaR exposures with profit and loss data to identify the frequency of instances when trading losses exceed the calculated VaR. The Bank uses actual and hypothetical profit and loss data. Back testing is conducted daily, and outliers are analysed to understand if the issues are the result of trading decisions, systemic changes in market conditions or issues related to the VaR model i.e. historical data or model calibration.

12. Liquidity Risk

Liquidity risk is the risk that the Bank is unable to meet its payment obligations as they fall due, including repaying depositors or maturing debt, or that the Bank has insufficient capacity to fund increases in assets. The timing mismatch of cash flows and the related liquidity risk is inherent in all banking operations and is closely monitored by the Bank.

The Bank maintains a portfolio of liquid assets to manage potential stresses in funding sources. The minimum level of liquidity portfolio assets to hold is based on a range of the Bank specific and general market liquidity stress scenarios such that potential cash flow obligations can be met over the short to medium term.

The bank's liquidity and funding risks are governed by a set of principles which have been fixed by the Group. The core objective of the overall framework is to ensure that the bank has sufficient liquidity to meet obligations as they fall due, without incurring unacceptable losses.

Key principles of the Bank's approach to liquidity risk management include:

- Maintaining the ability to meet all payment obligations in the immediate term. Ensuring that the bank has the ability to meet 'survival horizons' under a range of the Bank specific and general market liquidity stress scenarios to meet cash flow obligations over the short to medium term.
- Maintaining strength in the bank's balance sheet structure to ensure long term resilience in the liquidity and funding risk profile.
- Limiting the potential earnings at risk implications associated with unexpected increases in funding costs or the liquidation of assets under stress.
- Ensuring the liquidity management framework is compatible with local regulatory requirements.
- Preparation of daily liquidity reports and scenario analysis, quantifying the bank's positions.
- Targeting a diversified funding base, avoiding undue concentrations by investor type, maturity, market source and currency.
- Holding a portfolio of high quality liquid assets to protect against adverse funding conditions and to support day-to-day operations.
- Establishing detailed contingency plan to cover liquidity crisis events.

Management of liquidity and funding risks are locally overseen by India ALCO

Scenario modelling

A key component of the Group's liquidity management framework is scenario modelling. The Bank mainly assesses liquidity under different scenarios, including the 'going-concern' and 'name-crisis'. Liquidity scenario modelling stresses cash flow projections against multiple 'survival horizons' over which the Bank is required to remain cash flow positive.

Capital requirement for Market Risk is provided in section 6 above.

13. Operational Risk

The Bank understands and manages operational risk efficiently and effectively, allocating appropriate capital to cover expected and unexpected losses to protect depositors, customers and shareholders. Further, ANZ Group has introduced a revised Operational Risk Measurement and Management Framework (ORMMF), including new policies and procedures, which will enable globally consistent and comparable management of operational risk. The framework sets out the minimum requirements to identify, assess, measure, monitor, control and manage operational risk. ANZ India has reached a matured stage of implementation for ORMMF and is expected to be compliant with the revised framework by 30-June-2013.

An effective and embedded governance structure is also built for managing operational risk in line with the bank's values, culture, strategy and appetite. The oversight of operational risk management is conducted via three clearly articulated layers of risk management – Three lines of defence:

- The area where the risk originates is responsible for managing the risk. This is defined as 'the First Line of Defence'.
- To ensure appropriate challenge and oversight, there is a dedicated and independent operational risk management function. This is 'the Second Line of Defence'.

  The first and second lines of defence have defined roles, responsibilities and escalation paths to support effective two way communication and management of operational risk. There are also on-going review mechanisms in place to ensure the framework continues to meet organisational needs and regulatory requirements.
- 'The Third Line of Defence' has an independent oversight role within the governance structure and is performed by Internal Audit. Internal Audit provides independent and objective assurance to management that the first and second lines of defence are functioning as intended.

The Bank periodically identifies and assesses its exposure to material operational risk within all existing and new products, processes, projects and systems, and assesses the key controls in place to manage these risks. Compliance to the operational risk measurement and management framework is monitored using one or more of the following mechanisms, but is not limited to:

- Half yearly Risk Certification
- Periodic Control Testing
- Internal Audit Reviews
- Periodic External Reviews
- Compliance Monitoring

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

The objective of balance sheet interest rate risk management is to secure stable and optimal net interest income over both the short (next 12 months) and long term. Non-traded interest rate risk relates to the potential adverse impact of changes in market interest rates on the bank's future net interest income. This risk arises from two principal sources: mismatches between the re-pricing dates of interest bearing assets and liabilities; and the investment of capital and other non-interest bearing liabilities in interest bearing assets.

Interest rate risk is monitored using VaR. The Bank also uses Earnings at Risk (EaR) as an estimate of the amount of the next 12 months' income that is at risk from interest rate movements over a 1 month holding period, expressed to a 97.5% level of statistical confidence. It is calculated by applying a statistically derived interest rate shock to static repricing gaps over the first 12 months.

Impact in earnings for upward and downward shocks of 200 bps broken down by currency are:

As at 31 March 2013 :

(Amount in ₹ '000)

Currency	**Interest Rate Risk Shocks**	
	200bp up	**200bp down**
Rupees	23,064	(22,484)
USD	1,028	(142)

The Bank uses Duration Gap approach to measure the impact of Market Value of Equity (MVE) for upward and downward rate shocks. This measures the potential change in MVE of the Bank for a 200 bps change in interest rates. The change in MVE due to 200 bps change in interest rate are:

Change in MVE due to 200 bps change in interest rate	Amount in ₹ '000
31 March 2013	(241,705)