

BASEL II



Market Discipline: Pillar-III Disclosure under Basel-II

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1. Introduction

In accordance to Pillar III of the revised Framework for International Convergence of Capital Measurement and Capital Standards ('Basel II') and adopted under the Bangladesh Bank rules and regulations on risk based capital adequacy (issued through Revised RBCA Guidelines, dated December 29, 2010), we are now required to make a more in-depth and expanded public disclosure regarding our risk profile (capital structure, capital adequacy, risk management, and risk measurement).

2. Disclosure Policy

The Bank calculates Risk Weighted Assets (RWA) as per Bangladesh Bank's Basel-II guidelines (BRPD circular no.09, dated December 31, 2008) under:

- a) Standardized approach for credit risk,
- b) Standardized approach for market risk, and
- c) Basic indicator approach for operational risk.

3. Scope of Application:

The Risk Based Capital Adequacy framework applies to all banks on Solo and Consolidated basis, where 'Solo' basis refers to all positions of the bank, and its local and overseas branches/offices, and 'Consolidated' basis includes subsidiary companies. Midland Bank Limited applies for "Solo" basis as the bank has no subsidiaries.

4. Disclosure framework:

The following components are the disclosure requirements:

- i. Regulatory capital
- ii. Capital adequacy
- iii. Credit risk in banking book
- iv. Specific provisions
- v. Equities: disclosures for banking book positions
- vi. Interest rate risk in the banking book
- vii. Market risk in trading book
- viii. Operational risk

i. Regulatory Capital

a. Qualitative Disclosures

The terms and conditions of the main features of all capital instruments have been segregated in terms of eligibility criteria (BRPD circular no. 35 dated 29th December 2010 and other instructions given by Bangladesh Bank).

Core Capital (Tier-1) of MDBL is comprised of paid up capital, statutory reserve and retained earnings.

Supplementary Capital (Tier-2) comprises of general provisions (unclassified loans and off-balance sheet exposure), revaluation reserves for securities up to 50%.

The Bank does not have any Tier-3 Capital.

b. Quantitative Disclosures

Particulars	Solo
	(Figures in BDT Crore)
Total Eligible Capital	
The amount of Tier 1 capital, with separate disclosure of:	
Tire-1 Capital:	
Paid up capital	400.00
Statutory reserve	0.22
General reserve	00.00
Retained earnings	0.87
Total Tier-1 Capital	401.09
Tier-2 Capital:	00.00
General Provision	1.76
Revaluation Reserves for Securities up to 50%	0.60
Subordinated debt	00.00
Total Tier-2 Capital	2.36
Tier 3 Capital	00.00
Total eligible capital	403.45

ii. Capital Adequacy

a. Capital Calculation Approach

Assessment of capital adequacy is carried out in conjunction with the capital adequacy reporting to the Bangladesh Bank and the three standardized and basic indicator approaches for risk (credit, market and operational risk).

b. Capital of the Bank

	Figures in BDT Crore
Capital Adequacy Ratio (CAR)	Solo
Total	
MDBL	97.60%
Requirement as per BB	10%
<i>The surplus will act as buffer to support future activities.</i>	
Tier 1	
MDBL	97.03%
Requirement as per BB	5%
<i>Our policy is to maintain a strong capital ratio with high rating.</i>	
Risk Weighted Assets	413.35
<i>We maintain capital levels sufficient to absorb all material risks.</i>	
Capital	
MDBL	403.45
Requirement as per BB	400.00
Surplus	3.45

MDBL ensures compliance with the regulatory requirements, and satisfaction of external rating agencies, and other stakeholders including depositors.

c. Capital Management

Initiatives to ensure adequate capital include the following:

- Consistently encouraging corporate clients to complete external credit rating to assess counterparty Credit Risk status, and to reduce capital requirements.
- Improving and enhancing eligible collateral, by way of collateral optimization.
- Assessment of risk profile and credit rating of new clients.

MDBL's CAR is periodically reviewed and assessed by the Risk Management Division (RMD), and reported to senior management.

Capital Adequacy	Solo
	(Figures in BDT Crore)
Capital requirement for Credit Risk	38.03
Capital requirement for Market Risk	0.17
Capital requirement for Operational Risk	3.14
Total and Tier-1 capital ratio:	00.00
- For the consolidated group (%)	00.00
- For standalone Tier 1 capital out of maintained CAR (%)	99.42

iii. Credit Risk in Banking Book

a. Qualitative Disclosure

MDBL manages credit risk through a robust process that enables the bank to proactively manage its loan portfolios in order to minimize losses, and earn an acceptable level of return for shareholders.

b. Credit Risk Management at MDBL

MDBL's Credit Policy Manual (CPM), approved by the Board of Directors, defines organizational structure, roles and responsibilities and processes whereby credit risks can be identified, quantified, and managed. Credit instruction manuals address regulatory issues and establish control points. Product Policy Guidelines (PPG) establish a system of identifying and monitoring problem accounts, at the early stages delinquency, so that timely corrective measures can be taken (for Retail and SME clients as well).

MDBL manages credit risk through continuous measuring and monitoring of risks at obligor (borrower) levels and portfolio level. We follow Bangladesh Bank prescribed Credit Risk Grading Model (CRGM), and have developed a credit appraisal/approval process. The CRGM captures quantitative and qualitative issues related to management risk, business risk, industry risk, financial risk, project risk, and transaction-specific credit features, while assessing the overall grading of a borrower. External credit ratings of our clients, when available, are also taken under consideration. Delegations of credit approval authority are defined for ensuring good governance and better control in credit approval.

c. Loan Classification Criteria

All the loans and advances are grouped into four categories for the purpose of classification: (i) Continuous Loan (ii) Demand Loan (iii) Fixed Term Loan and (iv) Short-term Agricultural and Micro Credit.

Continuous & Demand Loans are classified:

- **Sub-standard** - if past due for 3 months or more, but less than 6 months;
- **Doubtful** - if past due for 6 months or more, but less than 9 months;
- **Bad/Loss** - if past due for 9 months or more.

Fixed Term Loans are classified:

- **Sub-standard** - if the defaulted installment is equal to or more than the amount of installment (s) due within 3(Three) months;
- **Doubtful** - if the defaulted installment is equal to or more than the amount of installment (s) due within 6 (Six) months;
- **Bad/Loss** - if the defaulted installment is equal to or more than the amount of installment (s) due within 9 (Nine) months.

Short-term Agricultural and Micro Credit are classified:

- **Sub-standard** - if the irregular status continues after a period of 12 (twelve) months;
- **Doubtful** - if the irregular status continues after a period of 36 (thirty six) months;
- **Bad/Loss** - if the irregular status continues after a period of 60 (sixty) months.

A continuous credit, time loan or term loan which remains overdue for a period of 60 days or more is classified as a “Special Mention Account (SMA)”.

Credit Risk	(Figures in BDT Crore)
a) Total gross credit risk exposures broken down by major types of credit exposure	178.05
Cash Credit	5.80
Overdraft	42.77
Loans to Stock, Share & Debenture	-
Loans to Brokerage House	-
Loans to Merchant Bank	-
EDF Loan	-
Payment Against Documents (PAD)	0.28
Loan Against Trust Receipt (LTR)	3.44
Packing Credit	-
House Building Loan	0.81
Consumer Loan	0.03
Loan General	-
Hire Purchase	-
Lease Finance	-
Term Loan	109.21

Time Loan	7.51
Bridge Finance	-
Agricultural Credit	-
Others	-
Staff Loan	8.20
Bills purchased and discounted	
Payable in Bangladesh	5.09
Payable outside Bangladesh	00.00
	5.09
b) Geographical distribution of exposures, broken down in significant areas by major types of credit exposure.	
Dhaka Division	164.54
Chittagong Division	18.60
	183.14
c) Industry or counterparty type distribution of exposures, broken down by major types of credit exposure.	
Agriculture	-
RMG	18.59
Textile	-
Ship Building	-
Ship Breaking	-
Other Manufacturing Industry	20.42
SME Loan	21.12
Construction	0.26
Power, Gas	-
Transport, Storage and Communication	25.97
Trade Service	5.65
Commercial Real estate financing	-
Residential Real estate financing	0.81
Consumer Credit	-
Capital Market (loan provided for brokerage or merchant banking, to stock dealer or any kind of capital market activities	-
Non- Banking financial institutions	73.93
Others	16.39
	183.14
d) Residual contractual maturity breakdown of the whole portfolio, broken down by major types of credit exposure	
Up to 1(one) Month	0.28
Over 1(one) Month but not more than 3 (three) Months	16.32
Over 3 (three) Months but not more than 1 (one) Year	53.51
Over 1 (one) Year but not more than 5 (five) Years	87.53
Over 5 (five) Years	25.50
	183.14

iv. **Specific Provisions - Guidelines for Loan Loss Provisions**

The Bank follows Bangladesh Bank guidelines regarding loan classifications, provisioning, and any other issues related to Non-performing Loan (NPL). Internal credit guidelines direct loan provisioning review procedure, debt write-off, facility grading, reporting requirement and interest recognition.

Particulars	Rate
General Provision	
Against all unclassified loans of Small and Medium Enterprise (SME)	0.25%
Against all unclassified loans and off-balance sheet exposures (other than loans under Consumer Financing, Loans to Brokerage House, Merchant Banks, Stock dealers etc., Special Mention Account as well as SME Financing.)	1%
On the unclassified amount for (i) Housing Finance and (ii) Loans for Professionals to set up business under Consumer Financing Scheme, Brokerage House, Merchant Banks, Stock dealers, etc.	2%
On the unclassified amount for Consumer Financing other than Housing Finance, Loans for Professionals and Loans to share business	5%
On the outstanding amount of loans kept in the 'Special Mention Account'.	5%
Specific Provision	
Specific provision on Substandard Loans and advances:	20%
Specific provision on Doubtful Loans and advances:	50%
Specific provision on Bad & Loss Loans and advances:	100%

Throughout the year, we reviewed loans and advances to assess whether objective evidence of impairment had arisen.

<i>(Figures in BDT Crore)</i>	
a) Gross Non Performing Assets (NPAs)	
Non Performing Assets (NPAs) to Outstanding Loans & advances	0.00
Movement of Non Performing Assets (NPAs)	
Opening balance	0.00
Additions	0.00
Reductions	-
Closing Balance	0.00
Movement of specific provisions for NPAs	
Opening balance	0.00
Provisions made during the period	0.00
Write-off	0.00
Write-back of excess provisions	0.00
Closing Balance	0.00

Amount of Impaired Loans

The amount of classified loans and advances/investments are given below as per Regulatory body's instruction:

Particulars	Figures in BDT Crore
Continuous Loans	0.00
Demand Loans	0.00
Term Loans	0.00
Short Term Agro Credit and Macro Credit	0.00
Total	0.00

Specific and General Provisions

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 of the Bank.

Particulars	Figures in BDT Crore
Provision on classified loans and advances/ investments	0.00
Provision on unclassified loans and advances/ investments	1.60
Provision on Off-balance sheet exposure	0.16
Provision for Off-shore Banking Unit	0.00
Total	1.76

v. Interest Rate Risk In The Banking Book

Interest rate risk is occurs when changes in market interest rates might adversely affect a bank's financial condition, affecting both current earnings (earnings perspective) and net worth of the bank (economic value perspective).

The short term impact of changes in interest rates is on the bank's Net Interest Income (NII). Longer term, changes in interest rates impact asset cash flows, liabilities, and off-balance sheet items. This poses a risk to the net worth of the bank, arising out of all re-pricing mismatches, and other interest rate sensitive positions. MDBL assesses the economic value at risk due to interest rate shock on a quarterly basis.

Interest Rate Risk in the banking book:

<i>(Figures in BDT Crore)</i>				
Total Risk Sensitive Assets	:	576.63		
Total Risk Sensitive Liabilities	:	276.86		
Cumulative Gap	:			
< 3months		95.51		
3-6 months		215.21		
6-12 months		299.77		
CAR before Shock (%)	:	97.60		
Assumed Change in Interest Rate	:	1.00%	2.00%	3.00%
Net Interest Income Impact				
Capital after Shock		406.45	409.45	412.44
CAR after shock (%)		98.26	98.91	99.56

vi. Market Risk

Market risk is the risk that the fair value of future cash flows of financial instruments will fluctuate due to changes in different market variables, namely:

- Interest rate movements
- Currency - foreign exchange rate movements
- Equity - stock price movements
- Commodity - commodity price movements

MDBL's Market Risk Policy, approved by the Board, covers assessment, monitoring, and management of the above market risks. The Board sets limits and reviews compliance on a regular basis, in order to provide cost effective funding to finance asset growth, and trade related transactions.

a. Methods Used to Measure Market Risk

Our standardized approach to measure market risk calculates the minimum capital requirement, for each risk sub-category, in terms of two separately calculated capital charges for "specific risk" and "general market risk".

b. Market Risk Management System

The Treasury Division manages market risk covering liquidity, interest rate, and foreign exchange risks, with oversight from Asset Liability Management Committee (ALCO), comprising of senior executives of the bank. ALCO is chaired by the Managing Director and CEO. ALCO meetings are held at least once in a month.

c. Policies and Process for Managing Market Risk

There are approved limits for credit deposit ratio, liquid asset to total asset ratio, maturity mismatch, commitments for both on-balance sheet and off-balance sheet items and borrowing from money market and foreign exchange position. The limits are monitored and enforced on a regular basis to protect against market risks. The Treasury Division of the bank reviews the prevailing market conditions, exchange rates, foreign exchange position, and transaction to mitigate foreign exchange risks on a daily basis. Foreign exchange risk is computed on the sum of net short positions, or net long positions, whichever is higher of the foreign currency positions held by the bank. The bank adopts the maturity method in measuring interest rate risk in respect of securities in trading book.

Quantitative Disclosure of Market Risk		<i>(Figures in BDT Crore)</i>
The Capital Requirement for:		
Interest Rate related instruments		0.020
Equities		0.000
Foreign Exchange Position		0.144
Commodity Risk		0.000
Total		0.165

vii. Operational Risk

Operational risk is arises from inadequate or failed internal processes, people and systems, or from external causes, whether deliberate, accidental or natural - inherent in all of the Bank's activities. The policy for operational risks including internal control and compliance risk is approved by the Board, taking in to account relevant guidelines of Bangladesh Bank. The Audit Committee of the Board directly oversees the activities of the Internal Control and Compliance Division (ICCD) to protect against all operational risk.

a. Policies and Processes for Managing Operational Risk

The preparation of policy guidelines on risk-based internal audit system is under process. According to the guideline, the activities of branches will be rated in terms of their risk status. It is the policy of the bank to conduct audit on all the branches at least once a year. ICCD directly reports to the Audit Committee of the Board. In addition there is a vigilance team (RMD) which was established in 2013 to identify, assess, monitor, control and managing operational risk, rectify risk events, and implement any additional procedures required for compliance. The Human Resource Division of MDBL has also introduced a vigorous Performance Management system (PMS) to evaluate human resources in terms of performance, and instill a performance-based culture within the organization.

Quantitative Disclosure of Operational Risk		<i>(Figures in BDT Crore)</i>
The Capital requirement for :		
Operational Risk		3.14

