

Guidance Notes on Management of Credit Risk and Market Risk

DBOD. No. BP. 520 /21.04.103/2002-03

October 12, 2002

All Scheduled Commercial Banks (Excluding RRBs and LABs)

Dear Sir,

Guidance Notes on Management of Credit Risk and Market Risk

As you are aware, guidelines on Risk Management Systems were issued vide our circular DBOD.No.BP.(SC).BC.98/ 21.04.103/99 dated October 7, 1999. These guidelines, together with the Asset-Liability Management (ALM) guidelines issued vide our circular DBOD.BP.BC.8/21.04.098/98-99 dated February 10, 1999 are intended to serve as a benchmark to the banks, which are yet to establish integrated risk management systems.

2. As a step towards enhancing and fine-tuning the existing risk management practices in banks, draft Guidance Notes on Credit Risk Management and Market Risk Management were issued to banks vide our letters DBOD.BP.BC.26/21.04.103/2001 dated September 20, 2001 and DBOD.BP.1913/21.04.103/2001 dated March 26, 2002, respectively. These Guidance Notes were placed on our website for wider discussion by banks, financial institutions and other market participants. The Guidance Notes were based on the recommendations of two Working Groups constituted in Reserve Bank of India drawing experts from select banks and FIs.

3. Comments on these Guidance Notes were received from a wide spectrum of banks, financial and academic institutions, rating agencies and other market participants. The draft Guidance Notes on Management of Credit Risk and Market risk have been revised in the light of the feedback received and the revised Guidance Notes are now placed on the website of RBI (<http://www.rbi.org.in>), which banks may download from the said website.

4. Banks may use these Guidance Notes for upgrading their risk management systems. The design of risk management framework should be oriented towards the banks' own

requirements dictated by the size and complexity of business, risk philosophy, market perception and the expected level of capital. The systems, procedures and tools prescribed in the Guidance Notes for effective Management of Credit Risk and Market Risk may, therefore, be treated as indicative. The risk management systems in banks should, however, be adaptable to changes in business size, the market dynamics and the introduction of innovative products by banks in future.

Yours faithfully,

Sd/-

(M.R. Srinivasan)

Chief General Manager-in-Charge