NCC Bank

नेपाल क्रेडिट एण्ड कमर्स बैंक लि

Nepal Credit & Commerce Bank Ltd.

Your Business Bank

Framework for Implementation of Branch Credit Risk Scoring Model

Nepal Credit And Commerce Bank Ltd

Bagbazar, Kathmandu

Approval Sheet

	Name	Designation	Signature
Prepared and Submitted by:	Ashim Bhatta	Credit Risk Management Department	22-3-2018
Reviewed & Supported By:	Sameer Acharya	Head- Credit Risk Management Department	
Reviewed & Supported By:	Mukunda Subedi	Chief Risk Officer	23.3.018
Reviewed & Supported By:	Rewant Kumar Dahal	Deputy Chief Executive Officer	
Reviewed & Supported By:	Bandana Pathak	Deputy Chief Executive Officer	
Approved By:	Ramesh Raj Aryal	Chief Executive Officer	

Table of Content

NCC Bank

नेपाल क्रेडिट एण्ड कमर्स बैंक लि.

Nepal Credit & Commerce Bank Ltd.

Your Business Bank

1. Introduction

Branch Risk Assessment is the identification and measurement of quantitative and qualitative risk related to a well-defined situation. Risk Grading of the branches according to their associated risk is the basic tool of credit risk management. Credit Risk scoring model will be regarded as the basic module for developing a credit Risk Management system. According to Risk Management Guidelines, Credit risk is the likelihood that a debtor or financial instrument issuer is unwilling or unable to pay interest or repay the principal according to the terms specified in a credit agreement resulting in economic loss to the bank. Credit risk also refers the risk of negative effects on the financial result and capital of the bank caused by borrower's default on its obligations to the bank.

Periodic risk assessment and profiling of branch and overall bank using various quantitative and qualitative measures and implementing risk mitigating tools according to identified risk areas and profile can only ensure the effective risk management of the overall bank. Hence, this document is prepared for the assessment of credit risk of branches to determine the Credit risk profile of the Branches using quantitative method and risk indicators.

In line with the NRB's Risk Management Guidelines, Bank's Risk Management Guidelines 2072, bank shall adopt policy and procedures to enable to identify, measure, monitor, management, control the credit risk and report to senior management and Board of Directors. The Branch Credit Risk Profiling Indicator Framework has been developed to identify the risk associated with branches through well-defined risk parameters, measure it through well-defined risk severity and weight, monitor it through continuous review, manage & control it through using various mitigating tools and report it to senior management and Board through monthly report. This framework shall come into immediate effect from the date of approval by CEO.

2. Key Principles

Followings are the key principles of this framework:

- Credit Risk assessment of the branch shall be conducted on individual basis.
- Risk Assessment of the branches shall be conducted on a Monthly basis and according to the level of quantified risk branch shall be categorized accordingly.
- Branches having high risk will require more oversight from management and frequency of offsite & onsite audit/monitoring should be increased.
- Credit Risk Management Department will be responsible for assessing the risk profile of the branches.
- Communication of major findings with recommendation to the senior management and board level risk management committee.

- Concerned corporate departments take the risk report for mitigating the risk identified and develop the strategic and make follow ups to bring the branches up to the low level of credit risk.

3. Objectives

The main objective of the framework is to guide the management to identify, measure, monitor, control and report the credit risk positioning of the branches. Some of the objectives of this framework are as follows:

- To provide the procedural guidelines to management to assess credit risk of the branches through well-defined risk indicators
- To identify and classify potential problem in the branches on a timely basis
- To ensure that the bank understands the current risk status of the branches. This is an important starting point towards encouraging a culture of responsible branches and credit activity.
- To take corrective measure to manage and mitigate the identified credit risk before occurring further financial losses
- To prepare risk avoiding and mitigating plan and procedures by management before occurring such risk events
- To ensure adequate, prioritized and focused attention from the board and senior management level on significant credit risk exposures and measures of mitigations of such risk.
- To implement the adequate control measures in order to ensure the quality of risk assets.

4. Branch Risk Assessment

Branch risk assessment begins with identifying major credit risk parameters set for this purpose. Risk assessment on the major areas will be determined by measuring materiality of that parameters and severity of that parameter to the bank while achieving business objectives and strategies. At present, all the parameters are given the equal weight which will be gradually changed on need basis. Risk Assessment of the Branches shall be conducted on following broad category:

- Non-performing Assets
- Interest overdue
- Past due accounts
- Account Expired
- Insurance expired
- Drawing Power Expired/Business Inspection Due
- Accounts with Margin Call (*incase of Margin lending*)
- Revaluation Pending Account/ Revolving Account %

Credit Risk Management shall calculate the risk level of the branch on the basis of data provided by the concerned departments as well as from core banking software.

Following methodologies have been applied to calculate the total risk of the branch:

Total Credit Risk = Total Risk Score / 8

The risk weight given to each parameter and calculation method used in this module is as follows:

		SCORE					
S. No	Parameters	0	1	2	3	4	5
1	NPA %	0	=<0.5	< = 1.0	< = 1.5	< = 2	> 2
2	Interest overdue to Total Loan %	0	=<0.5	< = 1.0	< = 1.5	< = 2	>2
3	Past due Account to Total Account %	0	< = 7	< = 10	< = 13	< = 15	< 15
4	Expired Accounts to Total loan Account%	0	< = 2	< = 4	< = 7	< = 10	> 10
5	No of Insurance Expired	0					> 0
6	Drawing Power Expired/Business Inspection Due	0			< = 10		> 10
7	Margin Call A/c to Total Margin Loan Account %	0			< = 20		> 20
8	Revaluation Pending Account/ Revolving Account %	0	<=5	<=10	<=15	<=20	<20

According to the risk assessment and total calculated risk scores, branches will be categorized in to following category according to the following risk weighted exposures:

S.N.	Risk Weight Exposures	Risk Category
1	0	No Risk
2	Up to 1.0	Inherent Risk
3	1.0 to 2	Low Risk
4	2.0 to 3.5	Medium Risk
5	3.5 to 4.5	High Risk
6	Above 4.5	Very High Risk

5. Risk Categorization

Credit risk is the major risk that banks are exposed during the normal course of lending and credit underwriting. Credit risk arises from non-performance by a borrower. For most banks, loans are the largest and most obvious source of credit risk; however, credit risk could stem from activities both on and off balance sheet. It may arise from either an inability or an unwillingness to perform in the pre-committed contracted manner. In a bank's portfolio, losses arise from outright default due to inability or unwillingness of a customer or counter party to meet commitments in relation to lending, trading, settlement and other financial transactions. Alternatively losses may result from reduction in portfolio value due to actual or perceived deterioration in credit quality.

Management of above mentioned risk through branch categorization on the basis of risk exposure is the major motive of this framework.

6. Implementation Guidelines

Credit Risk Management Department shall prepare the risk score report on monthly basis within 15 days after completion of each month.

There are 8 parameters in this Branch credit risk profiling model which incorporate major credit risk indicator of the branch. Additional parameters may be added after obtaining the approval of the management on need basis.

- According to the score of the credit risk level, branch shall be categorized into 5 categories as No Risk, Inherent Risk, Low Risk, Medium Risk, High Risk and Very High Risk.
- All the concerned departments shall provide the required information on timely basis in order to calculate the risk grade.
- After preparation of Branch risk profile, report should be submitted to senior management through Chief Risk Officer. Higher authority will review the report and instruct the branch as required to mitigate the credit risk issue.

7. Update and Review of Risk Indicator, Weight and Risk Calculation Methods

The Risk parameter defined in this model for calculation of credit risk shall be reviewed on timely manner and update accordingly. The risk parameter can be increased or removed according to the development in banking business, internal control system and other factors as well as timely availability of data. Further, weight and severity of risk given to each risk parameter shall also be reviewed and revised on need basis. Risk calculation method shall be revised to more scientific and realistic method incorporating development in internal and external environment.