“GENERAL RISK MANAGEMENT POLICY”

of

GSB FINANCE LIMITED

1: PURPOSE AND SCOPE OF THE POLICY

The purpose of Risk Management Framework is to establish basic principles and general framework for the control and management of risks which may exist or arise in GSB Finance Limited (hereinafter referred to as GFL). On specific risks faced by GSB, Specific Risk Sub-Policies have been developed which together form the Risk Management Framework.

The underlying premise of GFL risk management is to maximize stakeholders' value. While GFL faces uncertainties and risks, the challenge for the GFL board and management is to determine, as to what extent uncertainty is acceptable to strive to grow stakeholder value. Risk Management is essential as it is required for long-term sustainability of GFL. More specifically, the objectives of risk management at GFL are:

- Enhance shareholders value by minimizing losses and maximizing opportunities.
- Increase knowledge and understanding of exposure to risk.
- A systematic, well-informed and thorough method of decision-making.
- Increase preparedness and reduce uncertainty.
- Minimize disruptions and impact caused.
- Better utilization of resources and capital.
- Strengthen culture of continuous improvement.
- Retain the risk profile of GFL within the approved risk appetite.
- Ensure that risks are correlated with the profitability targets.
- Risks are accurately and timely reflected in GFL's risk reports.

GFL is aware that the key management responsibility is to provide reasonable assurance that GFL's business is being managed sustainably. Rather than focusing on current or historical financial performance, the management of GFL focuses on its ability to identify and manage future risks; this is viewed as being the best predictor of long-term success and sustainability. GFL management has a firm commitment that its products and processes comply with laws and regulations, and are aligned to the best practices of risk management. Increased focus of GFL on risk management reflects a fundamental shift to better anticipate and manage risks, rather than just react to them as and when they occur. This approach emphasises the importance of "self-supervision" and a pro-active approach to risk management by board members and the management team of GFL.

Over the last few years, the microfinance industry has been moving towards the implementation of risk-based and prudential management, as encapsulated in Basel II guidelines and agreement. For GFL, proactive risk management is a means to achieve desired goals. As GFL continues to grow, it plans to strengthen its capacity to identify and anticipate potential risks to avoid unexpected losses and surprises. A comprehensive approach to risk management reduces the risk of loss, builds credibility in the marketplace, and creates new opportunities for growth.

The key to fulfilling the responsibility of providing reasonable assurance to stakeholders that the GFL's business is adequately controlled, is the development of a comprehensive system of management controls, accounting and internal controls, security procedures, and other risk controls.

Risk Management Principles

There are specific core principles with regard to risk management. To suit the context of GFL and its operations, GFL has adopted risk management principles as defined below :

1. Is an integral part of the organizational processes i.e. becoming integral part of governance framework and becomes part of its planning at both operational and strategic level.
2. Create value through continuous review of its process and systems
3. Factor into the overall decision-making processes and help take informed decisions, identify priorities and select the most appropriate action
4. Explicitly address uncertainty by identifying risks and implementing controls to maximize gain while minimizing chances of loss
5. Is systematic, structured and timely so that risk management is consistent across GFL to ensure efficiency, consistency and reliability of results
6. Is based on the best available information relevant to an activity
7. Is based on the risk management framework, factors in the risk profile, and take into consideration internal and external operating environment
8. Take into account human and cultural factors while achieving GFL's objectives
9. Is transparent and all-inclusive so that it engages both internal and external stakeholders
10. Is dynamic and adaptable to change to identify new risks and make allowances for those risks that no longer exist
11. Is continuously monitored and improved upon for continual achievement of organisational objective
12. Is independent from risk taking activities i.e. it is independent from regular day to day operations of GFL
13. Is embedded in the corporate culture so that everyone take responsibility in managing risks

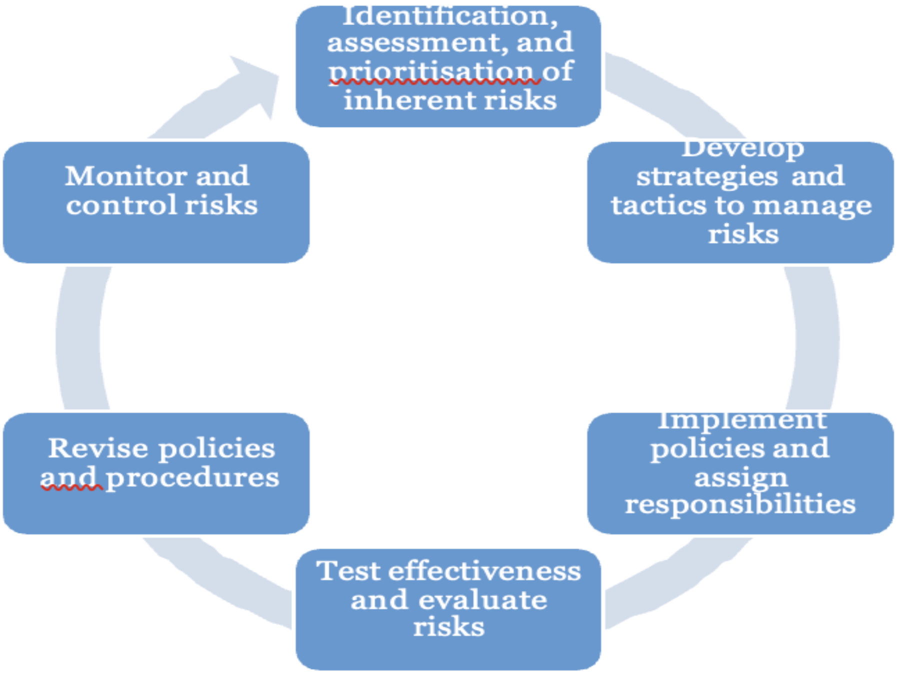
Risk Management Process

At GFL, risk management is a systematic process that comprises well-defined steps:

a) Identification, assessment, and prioritisation and mitigation of inherent risks,
b) Develop strategies and tactics to manage risks,
c) Implement policies and assign responsibilities,
d) Test effectiveness and evaluate risks,
e) Revise policies and procedures,
f) Monitor and control risks

When these steps are taken in sequence, they support better decision making and enable greater insights into risks. However, the risk management process does not end with monitoring and controlling risk; it is an on- going function. Further, it is not a linear process, but rather an on-going iterative process. The steps are part of an interactive and dynamic flow of information from the field to the head office (and management) and back to the field. These steps make a continuous feedback loop that consistently questions whether the assumed risk is reasonable and appropriate, or whether it should be reassessed.

Figure of Risk Management feedback loop



1. Identification, assessment, prioritisation and mitigation of risks

Members of the management including heads of the front-line business/operations and heads of back-end control functions (IT/MIS, HR, Accounts/Finance and Legal and Secretarial Department) shall bear the primary responsibility to identify risks in functional area(s) for which they are responsible (i.e. for which they are Risk Owners[2]). The front-line business/operations are responsible for assessment and control of credit risk whereas back end control functions are responsible for locating, identifying assessment and control of operational, liquidity and market risk. These risk owners/department heads provide the "first line of defence" in the risk governance framework. These risk owners will inform about new risks pertaining to their work area and the consequences if not managed proactively, to the Chief Risk Officer/Advisor. In addition to the first line of defence, the dedicated Chief Risk Officer/Advisor (second line of defence) plays a key role in identifying, assessing and managing the overall risks faced by the institution. The role of the RM is to establishing internal controls by acting as in-house consultant across all risk dimensions and to continuously identify, assess and prioritise the risk independent of the Risk Owners. Besides reporting to the BRMC (Board Risk Management Committee) on Risk Management, he will also apprise them of the new risks identified, their severity and thus priority level. Chief Risk Officer/Advisor, who is not a direct part of the operational command chain, will play a critical role at taking operational exposures by evaluating policies and procedures across different functions from the perspective of risk management. For each new risk area, the BRMC will determine the potential negative impact if the risk is not actively managed. Further, the BRMC will determine the degree of risk that GFL should tolerate and conduct assessments of potential impact from the identified risk, should a risk event actually materialise.

2. Develop strategies and tactics to manage risks

The Board determines the risk appetite as an integral part of choosing a business strategy for GFL. The business strategy needs to be developed and continuously brought in line with the risk appetite. Risk appetite statement of GFL indicates the maximum risk the institution is willing to take. The Board takes care of regulatory limits while determining the risk appetite including capital adequacy norms. The risk appetite statement of GFL should be reassessed regularly-at least once a year-and more often if required-in view of changes in the business environment and as measures of risks. The Board relies on the risk assessment system to identify different types of risk and obtain estimates of their levels. The Board uses quantitative as well as qualitative descriptions of risks.

The Board approves policies for measurement and on-going assessment of risks and monitors GFL's adherence to them. The management team identifies key indicators and ratios that need to be tracked and analysed regularly to assess GFL's exposure to risk in each area. The Board sets the acceptable range for each indicator. The Board also determines the frequency with which each indicator should be monitored and analysed, and lays down the responsibility for tracking. The Board will adopt one or more of the following strategies to manage exposure to risk:

Risk Avoidance	**Risk Transfer**
GFL may choose to avoid risks which have high probability, are beyond its control and can have devastating effect on its functioning	GFL may choose to transfer such risks which have low frequency but can be potentially devastating; examples of tools used for risk transfer are insurance and/or Hedging
Risk Acceptance	**Risk Control**
If the probability of occurrence and the impact of a particular risk are minor and manageable relative to the cost of controlling it, GFL may choose to accept such a risk	If the likelihood of a risk is high and the impact of the risk is low to medium and the costs to manage it in house is also cost effective, GFL may try to control such risks (e.g. risks associated with taking and administering savings services)

3. Implement policies and assign responsibilities

Once suitable control measures are in place line managers will oversee implementation of controls and monitor risks over time. Every staff is responsible for managing and monitoring the identified risk(s) that fall into his/her work area. The Chief Risk Officer/Advisor will support the management in development of cost-effective controls to manage risks and also in the implementation of policies

4. Test effectiveness and evaluate results

The Board of GFL through the BRMC will regularly review the operating results to assess whether the current policies and procedures produce the desired outcome(s)and at the same time adequately manage risks. Some indicators will require weekly or monthly monitoring, while others will require less frequent monitoring. Where results may suggest a need for some changes to policies and procedures and possibly identify new risk exposures, the department heads of GFL will suggest new risk control measures. These measures have to be approved by BRMC to come into effect, however, policy level changes will be approved by the Board of GFL. After the new controls are implemented, Chief Risk Officer/Advisor will test their effectiveness, evaluate the results and report to BRMC

It is the responsibility of the department heads of GFL to determine line staff to be held accountable for implementing changes and monitoring various risks through key indicators. They must also ensure that BRMC receives relevant and useful information in the prescribed format (s) and within timelines.

Department heads, in co-ordination with the Chief Risk Officer/Advisor, regularly check the operating results to assess to what extent:

- Risks are being identified and anticipated sufficiently
- Risk management strategies are indeed minimising risks, as desired
- Operational systems are working appropriately and are having the intended outcomes
- Risks are being managed in the most efficient and cost-effective manner

5. Revise policies and procedures

Based on the summary risk reporting and internal audit findings, BRMC with the assistance of Risk Management department, reviews risk policies for necessary adjustments. While only significant findings are reported to the BRMC, directors should ensure that necessary revisions are quickly made to systems, policies and procedures, as well as to operational workflow to minimize potential loss. The report may make specific recommendations on how to strengthen risk management areas. BRMC is responsible for designing specific changes, and in doing so, should seek inputs from the internal audit team and operations team including field staff. This ensures that the suggested operational changes are appropriate and will not result in unforeseen, negative consequences.

In a nutshell, the risk management feedback loop is an interactive and continuous process to ensure that the management is in-tune with the actual events and that GFL responds in a timely manner to any changes in its internal or external business environment.

Risk types managed under the policy

As a finance institution, GFL faces different types of risks. The general risk management policy covers five broad categories of risks:

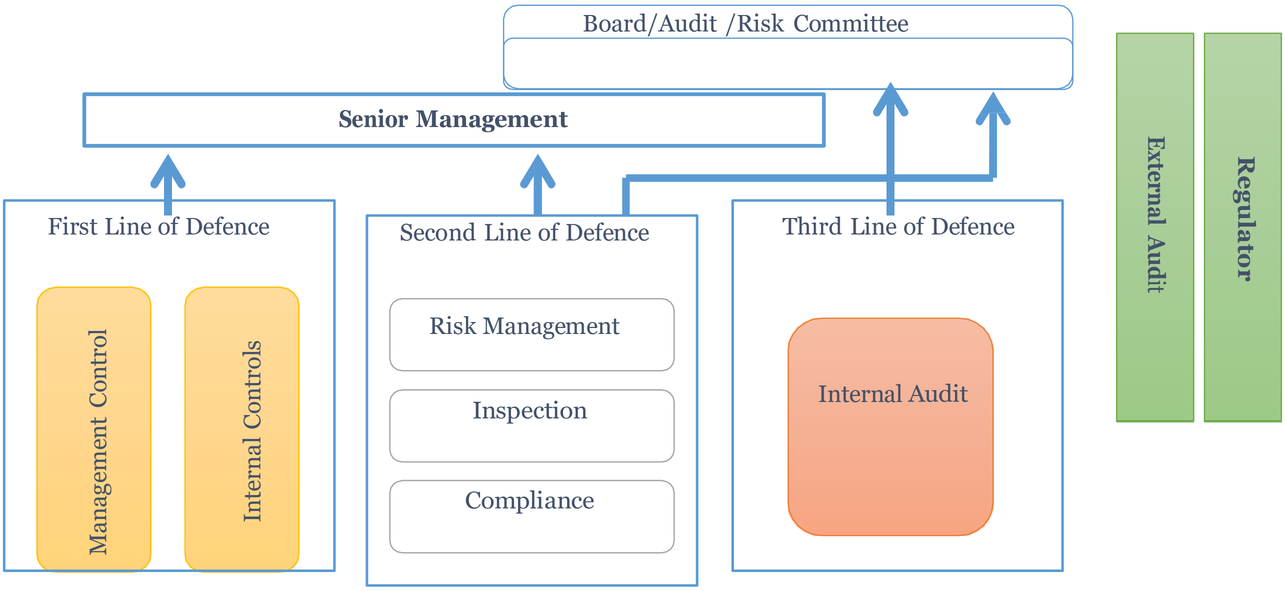
Operational Risk – these include risks related to areas like Information Technology, Human Resources, Administration and Information and Communication, and Legal
Credit Risk – these include risks related to the Lending activity
Market Risks – these include risks related to Foreign Exchange and Interest Rate

Liquidity Risk- including Funding risk
Foreign Exchange Risk –GFL is exposed to funds in foreign currency and the likelihood of raising foreign currency loans in future also.

2: RISK MANAGEMENT GOVERNANCE

The risk governance model of GFL is adapted from three lines of defence model as suggested by Bank for International Settlement. Figure 3 describes the risk governance model for GFL in detail.

Figure 2: Three lines of Defense for Risk Governance at GFL



At the organization level, the Board of GFL is responsible for overall risk management and it does so through the **Board Risk Management Committee (BRMC).** The Board defines the overall risk appetite of GFL by setting limits and standards.

In the context of GFL, the three lines of defense[3] are explained as below:

First line of defense - As the first line of defense, department heads (including frontline business and control functions) own and manage risks. They also are responsible for implementing corrective actions to address process and control deficiencies. These department heads are responsible for maintaining effective internal controls and for executing risk and control procedures on a day-to-day basis. The first line of defense identifies, assesses, controls, and mitigates risks, guiding the development and implementation of internal policies and procedures and ensuring that activities are consistent with goals and objectives. Through a cascading responsibility structure, the heads of different departments design and implement detailed procedures that serve as controls and supervise execution of those procedures by other staff. There should be adequate managerial and supervisory controls in place to ensure compliance and to highlight control breakdown, inadequate processes, and unexpected events. The first line of defense provides management with the assurance that robust internal controls are in place and being executed to avoid loss to the organisation.

Second line of defense – This line of defense provides assurance through oversight that internal controls are being properly designed and enforced for effective risk management. The oversight is guaranteed through inspection of whether the internal controls are effectively being implemented and there is compliance to risk management policies, procedures, and regulatory requirement. Risk management function facilitates and monitors the implementation of effective risk management practices by the operational management and assists Department Heads in defining target risk exposure and reporting risk- related information throughout the organisation. Risk Management function ensures completeness/accuracy of risk assessment, reporting, and adequacy of mitigation plan. Risk management function also defines and reviews risk policies and thresholds and provides guidance and directions for implementing the policies and for monitoring their proper execution.

Third line of defense – This represents internal audit that offers independent challenge to organisational operations and oversight function and lends additional assurance to risk management at GFL. Besides internal audit, external audit and compliance to regulation forms an additional line of defense in risk management for GFL.

In light of the three lines of defense, day-to-day management and monitoring of risks takes place by respective department. The Chief Risk Officer/Advisor who reports back on risks to BRMC further supports this function. RM also inspects and checks compliance of risk management actions, by respective departments, are in line with organisation risk management policies.

BRMC, with support from the Chief Risk Officer/Advisor, provide assurance to stakeholders through its oversight of risk management and by ensuring compliance to organisational risk management policies. Further, it also helps in defining and developing risk management policies and processes and defines GFL's risk appetite/profile.

Additional assurance to compliance is provided through internal and external audit of GFL BRMC, as a committee of the Board, has access to all audit reports for cross comparison and for trend analysis.

Individual business functions of GFL are responsible for monitoring different types of risk and share the monitoring reports with the Chief Risk Officer/Advisor. The following table defines which business unit/support unit monitors and manages risk at GFL.

Role of Board

The role of the board in risk management is the following

1. The board will approve and oversee implementation of the Risk Management framework of GFL and approve risk management polices

2. Ensure that resources allocated for risk management are adequate given the size, nature and volume of GFL's business
3. Approve GFL's contingency and business continuity plans
4. Require comprehensive and independent internal audit by well trained, competent auditors, who are independent of the risk management function, and who are responsible for periodically validating adherence to internal controls.

Role of Board Risk Management Committee

The role of BRMC with respect to risk management at GFL is :

1. To assist the Board in formulating risk management strategy and policies coordination with management and in discharge of its duties relating to corporate accountability and associated risk in terms of management assurance and reporting.
2. To review and assess the quality, integrity and effectiveness of the risk management systems and ensure that the risk policies and strategies are effectively managed;
3. To review and assess the nature, role, responsibility and authority of the risk management function within the Company and outline the scope of risk management work
4. To review processes and procedures to ensure the effectiveness of internal systems of control so that decision-making capability and accuracy of reporting and financial results are always maintained at an optimal level;
5. To monitor external developments relating to the practice of corporate accountability and the reporting of specifically associated risk, including emerging and prospective impacts;
6. To provide an independent and objective oversight and view of the information presented by management on corporate accountability and specifically associated risk, also taking account of reports by the Audit Committee to the Board on all categories of identified risks
7. To review the risk bearing capacity of the Company in light of its reserves, insurance coverage, guarantee funds or other such financial structures.
8. The Chairman of the RMC shall report to the Board of Directors regularly on the deliberations of the Committee.

To carry out any other function as may be specified from time to time as per the regulatory amendments/ requirements.

Role of Management Oversight (the Risk Owners)

Management that comprises Departmental/ Functional Heads, has the collective responsibility of implementing the business strategies approved by GFL's Board of Directors and developing policies and procedures for effective management of risks. The management team at GFL shall ensure the following:

1) Develop written procedures including responsibilities of the various functions for executing internal controls
2) Ensure compliance with internal exposure limits, prudential limits and regulatory requirements

3) Ensure that risk management policies, procedures, indicators and thresholds are communicated throughout GFL and implemented, monitored and revised periodically to address changes in environment and/or operating procedures
4) Ensuring GFL has robust management information systems for risk reporting

Role of Chief Risk Officer (Advisor)

1) Development and update the GFL's Risk Management policies and procedures. Though final approval on the policies will be by the Board and final approval on the procedures will be by BRMC.
2) Ensure compliance with the rules/ processes set in the risk manual and independent reporting in case of any deviation to the BRMC
3) Independent reporting to BRMC of the risk reports as per the defined frequency
4) Coordinate risk management training programmes for GFL staff
5) Identification, assessment and prioritisation of risk independently.
6) Monitoring positions against approved risk tolerance limits and initiate responses in case of warnings
7) Initiate specific risk reviews as requested by the BRMC
8) Identification of stress situations and preparation of contingency plans
9) Oversee risk analysis for new product development
10) Annually update the RAS of GFL
11) Prepare annual risk plans
12) Advise Risk Owners on all matters pertaining to Risk Management

Role of Internal Audit

The Internal audit unit and the internal audit committee of the Board will be responsible for the following:

1) Review adherence to Board's policies and procedures
2) Provide assurance regarding control systems and risk management process
3) Evaluate risk management measures for their appropriateness in relation to exposures
4) Test all aspects of risk activities and positions

3: Risk Appetite

GFL recognizes the need to define risk appetite so that it serves as a guide for managing risks. Risk appetite is defined as the amount / quantum and type of risk that GFL regards as appropriate and acceptable in pursuit of strategy.

The board regularly reviews and sets this in the form of risk appetite statements / threshold limits, which it sets in the context of GFL strategy and the requirements of various stakeholders, including the regulatory framework in which it operates. The risk appetite statements provide the benchmark against which GFL's risk profile is reported, monitored and managed by the board and relevant committees. Risk appetite also forms the basis for the calibration and setting of delegated authorities and financial limits for all aspects of market, credit, liquidity and operational risk. The risk appetite statements address both quantitative and qualitative aspects of risk taking.

Quantitative Risk Appetite Statements

1. GFL will ensure compliance to the organisation's vision, mission and organisational objectives and avoid situations/actions that could have negative impact on its reputation and brand
2. GFL will ensure full compliance with regulatory requirements
3. GFL will ensure compliance with operational risks in the execution of business plan
4. GFL will implement effective lending operating policies, and procedures, with appropriate internal controls
5. GFL will ensure development and adherence to Board approved concentration limits, and credit risk indicators
6. GFL will ensure that annual or multi-year business plans and business objectives, such as loan portfolio growth, are to be consistent with the credit risk management policy including risk strategy and risk appetite.

Credit Risk

Credit risk is the most important risk category for GFL. Credit risk for GFL refers to the possibility of its borrowers or another contractual counterparty not being able to honour their loan obligations. It includes risk arising from borrower's late repayment or non-repayment of the loan obligations. Such defaults lead to loss of income for finance institutions as they fail to collect interest and outright losses in case the principal amount given as a loan is not repaid. GFL needs to identify and manage credit risk arising out of individual transactions as well as losses of a significant portion of the loan portfolio.

The credit risk management policy requires sound practices for the management of credit risk and applies to all lending and related activities that may lead to credit risk.

GFL's credit risk management process is designed to cover the entire credit cycle starting from the origination of the credit in the books to the point the credit is paid off and cleared from the books, providing for sound practices in:

- Client selection
- Credit processing/appraisal,

- Credit approval/sanction
  - Credit documentation
  - Credit administration
  - Disbursement
  - Monitoring and control of individual credits
- Monitoring the overall credit portfolio
- Credit classification and
- Problem credit management and recovery

Regulatory Requirements

GFL must incorporate regulatory and legal requirements, including:

- The Companies Act, 2013
- Master Direction - Non-Banking Financial Company - Systemically Important Non-Deposit taking Company and Deposit taking Company (Reserve Bank) Directions, 2016 as amended from time to time
- RBI (Regulatory Framework for Microfinance Loans) Directions, 2022

Liquidity and Interest Rate Risk

Definition of Liquidity Risk Management

This may be caused by GFL's inability to liquidate assets or to obtain funding to meet its liquidity needs.

Scope of Liquidity Risk Management Policy

The liquidity risk management policy details the asset and liability risks, daily strategy and long-term plans to identify and measure risks, strategies to effectively control risks, report and monitor risks and contingency plan.

For effective liquidity management both static and dynamic measures need to be applied. Static measures are based on published balance sheet on a certain date, it provides a simple, point in time liquidity index, which is based on a static balance sheet condition. The dynamic measures are based on a more detailed breakdown of inflows and outflows based on projected business.

Static Liquidity Management based on the Balance Sheet

The conventional place to start in measuring liquidity is on the balance sheet, by looking at certain ratios between liquid or illiquid assets and liabilities, and at the contractual maturity structure of the balance sheet in the form of a maturity gap report.

Dynamic Liquidity Management based on Cash Flows

Cash flow planning is essential for liquidity management as balance sheet ratios can only give a quick sense of the liquidity risk of an institution but assurance that GFL will always be able to meet its payment obligations can only come from a detailed forecast of expected future business and its attendant cash flows.

Scenario analysis and Liquidity Stress testing

Liquidity stress testing plays a critical role in assessing the potential impact of a range of low probability and high impact severity circumstances on GFL's liquidity risk profile.

Liquidity stress test is designed to:

- Capture the impact of exceptional but plausible events, including the change in behaviour of borrowers and the impact on GFL's balance sheet and Liquidity Report under stress conditions,
- Understand GFL's liquidity risk profile and potential action plans that could be implemented even if the Disaster Recovery Plan had to be invoked,
- Confirm the adequacy of risk limits and risk appetite, and
- Evaluate strategic risk that may be sensitive to liquidity risk.

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The stress tests consist of a country-specific scenario and a GFL -specific crisis scenario. Each scenario represents a change in the measurement methodologies and assumptions governing the Liquidity Report.

Crisis Type	Causes	Impacts
GFL-specific	Major earnings or loan losses, deterioration of key financial ratios, reputation issues, management turmoil.	Negative public reports, loss of confidence expressed by key donors and sponsors, increased supervisory oversight, client or staff fraud and salary hike because of increased competition.
India- specific	National economic and political issues, natural disaster, financial turmoil.	Clients' inability to repay loans, negative sentiment about the microfinance industry, political hazards etc.

Operational Risks

Operational Risk is defined as the possibility of “losses resulting from inadequate or failed internal processes, people and systems or from external events[9]. This definition includes legal risk, but excludes strategic and reputational risk.
Legal risks includes, but is not limited to, exposure to fines, penalties, or punitive damages resulting from supervisory actions, as well as private settlements.

S. N	Operational Risks	Examples
1.	Internal fraud	Intentional misreporting of positions, employee theft, ghost loans to non-existing clients siphoned off by business executives
2.	External fraud	Robbery, forgery, cheque kiting, damage through computer hacking, clients misrepresenting their situation and obtaining a loan that they have no intention of paying back.
3.	Employment practices and workplace safety	Staff compensation claims, violation of employee health and safety rules, discrimination and sexual harassment claims and general liability for damages incurred by staff.
4.	Clients, products and business practices	Misuse of confidential customer information, marketing of unauthorised or inappropriate products, omission or incorrect disclosure of effective rates, abusive collection practices
5.	Damage due to physical activities	Fires, floods, vandalism, earthquakes, terrorism
6.	Business Disruption and System Failures	Hardware and software failure, utility failures, telecommunication problems, massive staff absence due to epidemic or political unrest.
7.	Execution, Delivery and Process Management	Data entry errors, collateral management failures, incomplete legal documentation, unapproved access granted to client accounts and vendor disputes.
8.	IT platform and procedure related risk	Disaster Recovery & business continuity plan failure, AMC deficiency, software upgrade, user credential reset , IS audit compliance etc.

Type of Operational Risk Events Relevant to GFL

Chief Risk Officer/Advisor will be reporting to the Board Risk Management Committee on a regular interval. Wherever possible, the Chief Risk Officer/Advisor will include industry benchmarks/peer institution benchmarks on KRIs and operational risk losses. The Risk Management policy will be reviewed annually or as and when required.