John Deere Financial India Private Limited

RISK MANAGEMENT POLICY

Policy No.	: JDF044	Amended on	: July 24, 2023
Prepared By	: Finance Department	Approved By	: Board of Directors

1. Scope

This document aims to lay down a broad framework for Risk management at John Deere Financial India Private Limited (referred to as "JDFIPL") as required by the Reserve Bank of India vide notification RBI/2021-22/112 DOR.CRE.REC. No.60/03.10.001/2021-22 - Scale Based Regulation (SBR): A Revised Regulatory Framework for NBFCs

The Finance Department shall be responsible for maintaining this document in consultation with Legal, Treasury, Credit and Secretarial team. The review and updates to this policy shall be done annually and approved by Board of Directors of JDFIPL.

2. References

RBI/2021-22/112 DOR.CRE. REC. No.60/03.10.001/2021-22	Scale Based Regulation (SBR): A Revised Regulatory Framework for NBFCs	October 22, 2021
RBI/2015-16/58 DBR.No. BP.BC.1/21.06.201/2015-16	Master Circular – Basel III Capital Regulations	July 01, 2015
RBI/2013-14/390 DBOD. BP. BC.No. 75 /21.04.103/2013-14	Guidelines on Stress Testing	December 2, 2013

3. Policy

The purpose of this policy is to address unanticipated and unintended losses to the Company. The effective management of risk is vital to the continued growth of the Company since an NBFC is prone to inherent risks while operating in the financial sector. The company has introduced effective risk management systems that address the issues
relating to various risks

3.1. Broad Categories of risks:

The following broad categories of risks have been identified in our risk management framework along with possible mitigation factors:

A. Credit Risk

A risk of loss due to failure of a borrower/counterparty to meet the contractual obligation of repaying his debt as per the agreed terms, is commonly known as risk of default.

Risk Mitigation

- Credit risk shall be managed using a set of credit norms and policies. The Company shall have defined roles and responsibilities for originators and approvers. All credit exposure limits shall be approved by authorized persons.
- Annual review of credit policy is done.
- There shall be a structured and standardized credit approval process to ascertain the credit worthiness of the borrower.
- The Company shall develop internal evaluation team to make credit decisions more robust and in line to manage collateral risk.
- The Company shall follow a process of time-to-time revisiting the credit policy and processes, on the basis of experience and feedback.

Also refer "India Retail Credit Policy" for JDFIPL.

B. Operational Risk

Any eventuality arising from the act relating to people, technology, infrastructure, and external factors, which can give rise to some type of loss in the organization, is termed as Operational Risk. Majorly it is internal and known. Therefore, the persons responsible shall keep continuous watch and shall gather the symptoms/warning signals to manage Operational risk.

There are following types of operational risk that the company is exposed to

i. External frauds
ii. Non compliance with policies
iii. Inaccurate External reporting and communications
iv. Talent management
v. Unstable IT infrastructure
vi. Document availability
vii. Business continuity
viii. Ethics and Compliance.

Risk Mitigation

- Document Storage and Retrieval: The company recognizes need for proper storage of documents as also their retrieval for audit and statutory requirements. The Company is maintaining all the original documents adequately and at safe location. Annual records retention certification is carried out by all employees to ensure retention is in accordance with regulatory and/or company guidelines.
- Whistle Blower Policy: This policy is in place to report any non- compliance to the company policies and procedures noted by the employees.
- Internal audit – Annual internal audit is conducted by an external firm. The scope of this Internal Audit covers all key functions including HR, Operations, Credit, Administration, Finance and Accounts. The firm also audits the company's

adherence to all Statutory and Regulatory Guidelines that have been prescribed for NBFC. The scope of these audits is reviewed periodically and modified as needed. All significant audit observations of Internal Audits and follow-up actions are presented to the Board Audit Committee.

- Technology Infrastructure: An IT security policy is in place. Refer JDF 033 IT Policy and JDF034 Information Security Policy.

C. Market risk

This is majorly external market dynamics, which gives rise to Risks like Liquidity risk, Interest Rate risk and Funding risk. Liquidity risk is the inability to meet financial obligations in a timely manner and without stress. The Company shall resort to proper ways to manage such risks.

Risk Mitigation

As a contingency plan the Company shall maintain sufficient approved but un- drawn credit lines on a continuous basis as buffer to manage eventuality of liquidity constraints.

D. Financial Risk

The financial risk includes interest rate risk, liquidity risk. Interest rate risk is the risk where changes in market interest rates might adversely affect an NBFC's financial condition. Liquidity Risk arises largely due to maturity mismatch associated with assets and liabilities of the company. Liquidity risk stems from the inability of the company to fund increase in assets, manage unplanned changes in funding sources and meet financial commitments when required.

Risk Mitigation

The company has the following policies in place to mitigate the financial risks- JDF 038 Liquidity Risk Management Framework Policy and JDF035 Resource planning policy.

E. Regulatory Risks

The Company shall be compliant in terms of regulatory norms and therefore shall effectively manage regulatory risk. Effective Customer redressal mechanism and fair practices shall keep legal risk under control. The Company shall have processes in place, to manage the risk of fraud and the suspected frauds are reported, wherever necessary.

Risk Mitigation

The company has a Customer Charter Committee in place monitoring customer grievances and issues and meets on a periodic basis. The company tracks regulatory updates in the monthly legislative compliance review meeting. Periodic checks are done by Risk and Compliance team to identify frauds. Process is in place for escalation and reporting of fraudulent incidents.

3.2. Capital Adequacy framework

As per changes made under Scale based regulations, SBR, issued on Oct 22, 2021 NBFCs are required to make a thorough internal assessment of the need for capital. The assessment will be similar to ICAAP prescribed for commercial banks under Pillar 2 (Master Circular – Basel III Capital Regulations dated July 01, 2015). The SBR mentions that Pillar 2 will not be insisted upon but NBFCs are required to make a realistic assessment of risks. Internal capital assessment shall factor in credit risk, market risk, operational risk and all other residual risks.

(Master Circular – Basel III Capital Regulations dated July 01, 2015) provides a link "Master Circular" which contains detailed information.

1. Part A – Contains Minimum Capital Requirement (Pillar 1)
2. Part B – Supervisory Review and Evaluation Process (Pillar 2)
3. Part C - Market Discipline (Pillar 3)

Reserve Bank issued Guidelines based on the Basel III reforms on capital regulation on May 2, 2012, to the extent applicable to banks operating in India. Basel III reforms strengthen the bank-level i.e. micro prudential regulation, with the intention to raise the resilience of individual banking institutions in periods of stress. These new global regulatory and supervisory standards mainly seek to raise the quality and level of capital to ensure banks are better able to absorb losses on both a going concern and a gone concern basis, increase the risk coverage of the capital framework, introduce leverage ratio to serve as a backstop to the risk-based capital measure, raise the standards for the supervisory review process (Pillar 2) and public disclosures (Pillar 3) etc.

3.2.1 Scope of application of capital adequacy framework:

JDFIPL is required to do the standalone ("Solo") level capital adequacy ratio requirements, which measure the capital adequacy of a unit based on its standalone capital strength and risk profile.

JDFIPL will annually evaluate of capital adequacy and consider different business case scenarios to see minimum threshold capital requirement maintained even at worst case scenario.

3.2.2 Three pillars of capital adequacy

The Capital Adequacy Framework rests on three components or three Pillars. Pillar 1 is the Minimum Capital Ratio while Pillar 2 and Pillar 3 are the Supervisory Review Process (SRP) and Market Discipline, respectively.

- Pillar 1: Minimum Capital Requirements - which prescribes a risk-sensitive calculation of capital requirements that, for the first time, explicitly includes operational risk in addition to market and credit risk. As mentioned in Chapter IV of Master Directions for NBFC-ND-SI dated Sept 1 2016 as updated from time to time, as applicable to JDFIPL
    1. Every Applicable NBFC shall maintain a minimum capital ratio consisting of Tier I and Tier II capital which shall not be less than 15 per cent of its aggregate risk weighted assets on-balance sheet and of risk adjusted value of off-balance sheet items.
    2. The Tier I capital in respect of applicable NBFCs (other than NBFC-MFI and IDF- NBFC), at any point of time, shall not be less than 10 per cent.

    Tier I and Tier II capital are defined in Chapter II of Master Directions Master Directions for NBFC-ND-SI dated Sept 1 2016.

- Pillar 2: Supervisory Review Process (SRP) - which envisages the establishment of suitable risk management systems in banks and their review by the supervisory authority.

- Pillar 3: Market Discipline - which seeks to achieve increased transparency through expanded disclosure requirements for banks.

Under Pillar 2 the main aspects to be addressed under the SRP, and therefore, under the ICAAP, would include:

(a) the risks that are not fully captured by the minimum capital ratio prescribed under Pillar 1;
(b) the risks that are not at all taken into account by the Pillar 1; and
(c) the factors external to the bank/NBFC.

Since the capital adequacy ratio prescribed by the RBI under the Pillar 1 of the Framework is only the regulatory minimum level, addressing only the three specified risks (viz., credit, market and operational risks), holding additional capital might be necessary, on account of both – the possibility of some under-estimation of risks under the Pillar 1 and the actual risk exposure vis-à-vis the quality of its risk management architecture. Some risks which the Regulated Entity is exposed to but not captured or fully captured in the regulatory CRAR would include:

i. Interest Rate Risk
ii. Credit Concentration Risk
iii. Reputational Risk
iv. Strategic Risk
v. Underestimation of Credit Risk

vi. Risk of weakness in credit mitigations
vii. Exchange Rate Risks

3.3 Internal Capital Adequacy Assessment Process (ICAAP):

Pillar 2 requires banks/financial institutions to implement an internal process, called the Internal Capital Adequacy Assessment Process (ICAAP) for assessing their capital adequacy in relation to their risk profiles as well as a strategy for maintaining their capital levels.
The ICAAP comprises a financial institution's procedures and measures designed to ensure the following:

a. An appropriate identification and measurement of risks;
b. An appropriate level of internal capital in relation to the financial instituion's risk profile; and
c. Application and further development of suitable risk management systems in the Company.

Four key principles are laid out by the Basel Committee with regard to SREP (Supervisory Review and Evaluation Process)

1. Company should have a process for assessing their overall capital adequacy in relation to their risk profile and a strategy for maintaining their capital levels.
2. Supervisors would review the Internal Capital Adequacy Assessments.
3. Company is expected to operate above the minimum regulatory capital ratios
4. Supervisors would intervene at an early stage to prevent capital from falling below minimum threshold.
   Thus, the ICAAP and SREP are the two important components of Pillar 2.

Detail process of ICAAP as suggested in BASELIII has been considered and forms as part of this policy.

Based on the outcome of the ICAAP as submitted to and approved by the Board, the ICAAP Document, in the format furnished at Annex 15 to the guidelines, should be furnished to the RBI (i.e., to the CGM-in-Charge, Department of Banking Supervision, Central Office, Reserve Bank of India, World Trade Centre, Centre I, Colaba, Cuffe Parade, Mumbai – 400 005). The document should reach the RBI latest by end of the first quarter (i.e. April-June) of the relevant financial year subject to some further communication in this regard

<u>Board of Directors Meeting and Review</u>

The Board of Directors, in their board meetings, will oversee the implementation of the system and review its functioning at least once in a year.

The ultimate responsibility for designing and implementation of the ICAAP lies with the Company's board of directors of the financial institution and with the Chief Executive Officer/Managing Director.

4. Risk Management Framework

The Risk Management Framework provides an overall structure to ensure that the assessment to monitoring of risks are done. A robust framework would enable the company to have proper mitigations in place to address risks associated with business.

Identification and Risk Assessment:

As part of strategic planning process and day to day management of business, functional leaders identify internal and external risks that effect business. The Risk Management function helps assess the risks and do an assessment.

Risk Response:

A response is determined based on overall risk exposure and root cause analysis and control activities are in place to provide assurance that objectives would be achieved.

Information and Communication:

Channels are in place to make everyone aware of the risks associated with their area of responsibility and actions to mitigate negative outcomes.

Monitoring:

Management testing, auditing, assessment procedures are in place to ensure risks are effectively identified and preventive controls are in place.

5. RISK APPETITE

JDFIPL encounters risks every day as it pursues its objectives. Effective risk management increases the probability of successful outcomes while at the same time protecting the reputation and sustainability of JDFIPL. A necessary pre-requisite of effective risk management requires a distinction of the specific levels of risk we are willing to incur in pursuit of the expected rewards associated with our actions. That is the role served by a Risk Appetite statement.

This Risk Appetite Statement will serve:
- To link existing strategies and objectives with specific risk tolerances
- To provide effective communication throughout the enterprise to drive the implementation of enterprise risk management and the establishment of risk limits

- To provide a basis for further discussion of Risk Appetite as strategies and objectives change

Low	This reflects an appetite which allows risks/activities that may lead to insignificant impacts. Very little variance in actual versus expected performance is allowed
Medium	This reflects an appetite which allows risks/activities that may lead to minor to moderate impacts. Some variance in actual versus expected performance is allowed,
High	This reflects an appetite which allows risks/activities that may lead to major impacts to maximize company value. Greater variance in actual versus expected performance exists

Type of Risk and Risk Tolerance Metric

Risk	Type of Risk	Risk Appetite	Risk Tolerance Metric
Credit Risk	GNPA	Medium	6 %
Credit Risk	Concentration Risk	Medium	Within allowed % - single 15%, group-30%
Strategic Risk	Competitive position	Medium	Volume number – 1500cr
Liquidity Risk	Capital Risk – Capital Adequacy	Low	17%
Market Rate Risk	Interest Rate Risk	Medium	Net Interest Income > 8%
Liquidity Risk	Funding lines	Low	Funding lines for6 months debt repayment
Regulatory Risk	Compliance with laws	Low	Compliance with regulations, Number of customer complaints>15% from last March year end.
Operational Risk	External Fraud	Low	FMR reporting – 50 lakhs annually
Operational Risk	Non Compliance with Policy	Low	NA, Incidences count reported in quarterly ICQ meeting.
Operational Risk	External Reporting	Low	Timely reporting to RBI
Operational Risk	Ethics and Compliance	Low	NA
Operational Risk	Talent Management	Medium	FTE attrition rate >15% on R12.
Operational Risk	Unstable IT Infrastructure	Low	Uptime of system> 98%
Operational Risk	Document availability	Low	NA
Operational Risk	Business Continuity Plan	Low	BCP meetings quarterly

6. RISK GOVERNANCE STRUCTURE

JDF India has the below committees to govern and monitor the various requirements to operate the business. Overall, the Board of Directors have an overarching responsibility.

1. Board of Directors

2. Committees
   a. Audit Committee
   b. Asset Liability Committee
   c. Risk Management Committee (Credit & Risk)
   d. Stakeholder Relationship Committee
   e. IT Committee
   f. Customer Charter Committee
   g. Pricing sub committee
   h. Fraud Management sub committee

Purpose & Scope of Committees

The purpose and scope of each committee is defined in the Business Structure Policy (Internal Guidelines on Corporate Governance) of JDFIPL.

The Risk Management Framework structure is also aligned to enterprise framework available at [JDF Enterprise Risk Management - JDF Enterprise Risk Management (sharepoint.com)].

Records Management and Retention

Record Management and Retention: This document shall be kept in compliance with JDF record retention policy.

Document Change Records

Document Change Records				
Sr. No.	**Revision no./ date**	**Section Revised/ Page No.**	**Reason For change**	**Change Description**
1				

Need to know departments				
Finance	**Operations**	**IT**	**Legal**	**Credit**
Yes	**Yes**	**Yes**	**Yes**	**Yes**

Sales	Collection	HR	Wholesale	Risk and Compliance
Yes	**Yes**	**Yes**	**No**	**Yes**
Bank Relationship				
No				