

FEDEX FINANCE PRIVATE LIMITED

Risk Management Policy

Fedex Finance Private Limited

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Risk Management Policy

Risk Management Framework:

The Risk Management Framework or the Risk Appetite Framework is the overall approach, including policies, processes, controls and systems, through which risk appetite is established, communicated as well as monitored. The chief components of a Risk Management Framework are:

- A. Mission, Strategy and Operating Model
- B. Risk Appetite Statement
- C. Risk Governance Model
- D. Risk Identification, Classification and Policies managing these Risks
- E. Key Risk Appetite Indicators / Thresholds
- F. Monitoring of the Risk Management Framework.

A. Mission, Strategy and Operating Model

Vision Statement:

Reaching the unreached through suitable credit solutions

Mission Statement:

Fedex Finance Private Limited (“the Company/FFPL”) provides funds predominantly to the unreached section of the business population of India. The Company adds value by providing medium to long term loans and supports its clients as a formal complementary source of financing. It endeavors to take care of the interests of all its stakeholders and at the same time ensuring that it respects the law of the land and remain compliant to its rules and regulations.

The Company’s strategy and operating model is to:

- Identify and do a preliminary evaluation of its potential customers through its own network and then underwrite those proposals for credit decision making.
- To reach out to those customers who are predominantly in non-metro areas and are willing to enter into formal organised lending channel to fund their business/personal requirements.

In order to support its lending operations, the Company finances its activities through equity, borrowing from Financial Institutions. The main objective is to ensure that the Company is able to operate and continue its core activities even during stressed market conditions. The composition and the maturity profile of the liquidity portfolio are aligned with this objective.

B. Risk Appetite Statement

The Company, being a NBFC, is governed by the regulations laid down by the Reserve Bank of India (RBI). Risk management systems and procedures are reviewed and refined on an ongoing basis in order to comply with what the company identifies as the relevant market standards, recommendations and practices. The key elements of the Risk Appetite Statement are as follows:

1. Risk Culture

The Company follows sound corporate governance and business practices. We abide by the various policies and regulations issued by the regulators and the various governing agencies of our country and would follow them in letter and spirit. All individuals in our company are expected to contribute and promote a sound risk culture.

2. Capital

The Company will strive to maintain a strong capital position with respect to the total risk exposure. We would use risk-based approach to assess our capital needs and would hold capital buffers on top of the regulatory stipulated minimum capital requirement.

3. Lending

The Company provides medium to long term financing to customers predominantly to support them in their business development activities. We strive to maintain a high quality of the loan portfolio by following our unique underwriting practices and at the same time securing our loan exposure by availing a collateral from our customer, wherever possible. We would diversify risk by ensuring that we disburse small, medium and large ticket sized loans and ensure geographical spread of our customers.

4. Treasury

FFPL, through its treasury activities, will enable and support the company's lending operations by acquiring optimal cost funding from diversified sources and by maintaining a strong liquidity position. We are cognizant of liquidity risk arising out of maturity mismatches between borrowing and lending tenures and would aim it keep it within the defined threshold levels.

C. Risk Governance Structure:

In order to manage the risks in The Company effectively and efficiently, the risk governance structure will be both at Board Level and Management Level.

1. Key Principles of Risk Governance Structure:

The Board of Directors will be responsible for overall governance and oversight of the core risk management activities.

Risk Framework & Policy is approved by the Board on an annual basis and is defined based on the company risk appetite which helps to align risk, capital and performance targets. All major risk classes, viz. Credit risk, Liquidity Risk and Other Risks, are managed through focused and specific risk management processes.

2. Risk Management Committee:

2.1 Composition of RMC:

The Reserve Bank of India, vide circular DNBS (PD) CC NO. 288/03.10.001/2012-13 dated July 2, 2012, has envisaged the creation of a Risk Management Committee by all NBFs. This Committee will be responsible for the identification and measurement of risks and also taking suitable measures to prevent the occurrence of such risks.

RMC is empowered by the Board of Directors to manage the risks in the Company and it manages the same through oversight of the risk management function and laying down risk measurements and mitigants.

2.2 Frequency of Meeting:

RMC shall meet at least twice in a financial year and its findings shall be presented to the Board in the subsequent Board meeting.

2.3 Roles and Responsibilities of RMC:

The key roles and responsibilities of RMC include:

- a) Approve / recommend to the Board for its approval / review of the policies, strategies and associated frameworks for the management of risk
- b) To identify areas of risks as also various types of risks involved in the business.
- c) To suggest methodologies to measure / quantify the risks.
- d) To control and mitigate various types of risks involved.
- e) To specify the risk bearing capacity/risk appetite of the Company.
- f) Sub-delegate its powers and discretions to executives of The Company or management committee of Fedex Finance Private Limited, with or without power to delegate further
- g) To monitor and review non-compliance, limit breaches, audit/regulatory findings and policy exceptions with respect to Risk Management
- h) To ensure regulatory compliance on risk management and prudential norms set by RBI/ Govt. / Other regulatory agencies
- i) To improve the assets quality of the Company by using the risk management techniques.
- j) To maximize the returns to all the stakeholders, with an acceptable level of risk, for the purpose of protecting, preserving and increasing the worth of the Company.

3. Risk Management Structure:

The Company has adopted the “2 LINES OF DEFENCE MODEL” for management of its risks.

- The 1st Line of Defence will be the Business and Support Units that will own the risks and manage the same, as per laid down risk management guidelines. The primary responsibility for managing risks on a day to day basis will continue to lie with the respective business units of the Company.
- The 2nd Line of Defense will be the Audit Functions – primarily the Audit functions that are supported by External Audits. The 2nd Line of Defense focuses on providing the assurance that the risk management principles/policies and processes well entrenched in the organisation and are achieving the objective of managing the risks of the organization.

D. Risk Identification, Classification and Policies managing these Risks:

The Company has identified and classified the primary risks that it faces under the following:

1. Credit Risk

The key risk for NBFC or any other institutions involved in lending business is Credit risk. According to RBI, credit risk is defined as

- Possibility of losses associated with decline in the credit quality of borrowers or counterparties

- Default due to inability or unwillingness of a customer or counterparty to meet commitments in relation to lending, trading, settlement and other financial transactions
- Loss from reduction in portfolio value (actual or perceived)

Hence it is imperative that the company should have a robust credit risk management system to address the above risk. The effective management of credit risk is a critical component of comprehensive risk management and is essential for the long-term success of any lending organisation.

Credit risk management should encompass identification, measurement, monitoring and control of the credit risk exposures. The objective of the same should be to minimize the risk and maximize company's risk adjusted rate of return by assuming and maintaining credit exposure within the acceptable parameters. The credit risk management shall include credit norms and policies approved by Board. The credit policy shall include:

- Target segments

The segments targeted by the company will largely comprise of Services segment. This is based on the company's past experience over 25 years that this segment is least impacted by cyclical issues. The company would also largely not focus on seasonal and speculative sectors/activities.

Credit Underwriting Process

There shall be a structured and standardized credit underwriting / approval process to ascertain the credit worthiness of the borrower.

The Company shall follow a process of revisiting the credit policy and processes from time to time, based on experience and feedback. The latest Credit Policy of The Company covers in detail as to the various policies and procedures to address this risk.

The Company ensures that sufficient training is given to its employees on the credit and KYC procedures for onboarding and evaluation of its customers. The Company has constituted a KYC policy in line with the RBI requirements.

2. Liquidity Risk

The third risk that is very specific to NBFCs or other institutions involved in the activity of lending is liquidity risk or the risk of inadequate liquidity to further the business.

The Company is also dependent on banks and financial institutions and other funding structures for its funding and hence the liquidity risk needs to be managed efficiently in order to ensure smooth functioning. Availability of liquidity alone is not sufficient but managing the cost of funds is a very important indicator to ensure company profitability. The cost of funds charged by the banks and financial institutions to a NBFC depends on a multitude of factors (listed below) and the ALCO is tasked to keep a track of these factors and ensure that they stay in favor of the Company at all times.

- ✓ Company size – the larger the company size, the lower the cost of funds
- ✓ Portfolio quality – Demonstration of a strong portfolio quality over long periods of time would help the company get cheaper funds
- ✓ Capital adequacy and Leverage – the higher the capital adequacy and lower the leverage, the company will be able to attract lower cost funds for its operations
- ✓ Credit rating – the better the credit rating of the company, the lower would be its cost of funds
- ✓ Multiple sources of funds – A company which has access to multiple sources of funds will be able to rationalize its costs better than a company which is dependent predominantly on a single source of funds

One of primary activities for a NBFC is to raise financial resources to fund the operations of the company. These resources can be raised through a multitude of channels and through various financial instruments. The company can raise resources vide Bank/FI Borrowings, CP, NCD, Securitisation, ECBs etc.

Another aspect to the liquidity risk is matching the asset-liability profile such that there is no negative asset-liability mismatch, at least in the short to medium term. While this risk needs to be monitored and managed by the Risk Management Committee, given the sophisticated nature of the risk, this is typically managed by the ALCO (Asset-liability Committee).

In addition to raise of funds, another important aspect of liquidity is also how these funds are safely held till they are disbursed to potential customers of the company. This is addressed in the Investment policy, which clearly lays down the permissible forms of investments, thresholds for different forms of investments, and so on. The Company can place their investments predominantly in FDs (rated A1+ or equivalent rating by a SEBI accredited credit rating agency) or in MFs (Liquid funds of top 10 MF based on AUM).

The Liquidity Risk Management & ALM Policy and Investment Policy covers in detail the aspects mentioned above.

3. Other Risks

3.1 Financial Risk

Every Company, especially financial institutions, which is in the process of lending needs to manage its financial risk in a prudent fashion. Financial risk could take the following forms:

- ✓ Compliance with Accounting Standards – this is essential to ensure that the company’s financials including the balance sheet and profit & loss account reflect the true and correct picture of the company’s position and all the errors of Omission and Commission are avoided
- ✓ Adequacy of Internal Financial Controls – every company needs to develop its own set of Internal Financial Controls, which will serve as the check and balance to ensure the orderly and efficient conduct of its business
- ✓ Clearly documented and consistent accounting policies – it is essential for every company to develop its set of accounting policies in line with applicable Accounting Standards and also maintain consistency in the adoption of such accounting policies over the course of financial years.

The Accounting Policy of The Company has been compiled to ensure that the relevant accounting principles are adhered to.

3.2 Operational Risk

Another risk that is prevalent to many institutions is the inadequacy of processes to maintain checks and balances in the conduct of its operations. Necessary controls are essential to ensure that there are no intentional or unintentional errors that creep into the process.

The operations staff shall independently carry out or check the various processes like data entry, preparation and verification of MODs, necessary checks before disbursements, scrutiny of documents at each stage as required, ensure safe custody of the property documents and the like. With such independent checks, it is envisaged that the errors would decrease significantly.

3.3 Technology Risk

In this digital era, as organizations use automated information technology (IT) systems to process their information, risk management plays a critical role in protecting an organization’s information assets,

from IT-related risks.

An effective risk management process is an important component of a successful IT security program. The principal goal of an organization's risk management process should be to protect the organization in its entirety and its ability to perform their mission, and not restricted to its IT assets.

To address these key risk areas, The Company has framed comprehensive IT Policies and Procedures with the help of an external consultant.

3.4 Compliance Risk

- The Company is a NBFC coming under the regulatory purview of the Reserve Bank of India and Ministry of Corporate Affairs. In addition, it is also required to comply with various central, state and commercial laws applicable in the conduct of the various activities of the business.
- The Company recognizes that the regulatory landscape is under periodical review and this requires the company to be proactively prepared, as best as possible, to meet with the challenges posed by the changes. The company shall respond effectively and competitively to regulatory changes, maintain appropriate relationship with the regulators / authorities strengthen the reliance on capital and improve the quality of in-house compliance. All reports, returns and disclosures stemming from regulations are submitted promptly and accurately to reflect the correct position.
- Business processes shall be defined in a manner to ensure comprehensive regulatory compliance considering the multitude of regulatory agencies the company has to deal with. Competent and knowledgeable specialist officers shall be recruited to ensure compliance.
- The responsibility for ensuring compliance with regulatory requirements and directives on a day to day basis rests with the Business Heads, who will comply with the Compliance requirement of the Company. Relevant Committees of the board provide oversight for management of these compliances.

3.5 Human Resources Risk:

The success of any institution lies in the strength of its people. It is essential for a company to attract and recruit the right set of people, manage their monetary and non-monetary expectations so that they are able to contribute towards the growth of the Company.

The latest HR Policy of the company has been compiled to address all the facets of HR requirements of the company.

3.6 Reputational Risk:

Reputation risk is the loss caused to the Company due to its image or standing being tarnished by certain incidents or actions arising from its business operations. Such incidents or actions may be attributable to the Company or any employee(s) or executive(s) committed either consciously or otherwise. Reputation risk could result in loss of revenues, diminished shareholder value and could even result in fines being levied by the relevant regulators.

The Company realizes that its goodwill depends on its reputation, which has been built over years, and hence, protecting its reputation assumes paramount importance. The company has framed required policies, which shall ensure that its customers and its employees are treated fairly and in a transparent manner, while achieving its business objectives thereby not giving any scope for the reputation to get tarnished in any manner.

The latest FPC Policy, Grievance Redressal Policy and Sexual Harassment Policy has been documented keeping in mind the requirement to protect the reputation of the company.

E. Monitoring the Risk Management Framework:

Having established a framework to manage risk; it is imperative that it be monitored religiously. The Company would monitor the same by conducting adequate risk reporting to its various committees and the Board. The reporting would be done to these committees in the relevant forums in the form of relevant dashboards/reports.
