**DBOD BP.BC. 8/21.04.098/99**

**February 10, 1999**

**To**

**All Scheduled Commercial Banks**
(excluding RRBs)

Dear Sir,

**Asset - Liability Management ( ALM ) System**

Please refer to our circular DBOD No. BP. BC. 94/ 21. 04. 098/ 98 dated September 10, 1998 forwarding therewith draft Guidelines for putting in place Asset-Liability Management (ALM) System in banks. The draft Guidelines have been reviewed by us in the light of the issues raised/suggestions made by banks in the seminars held at Bankers Training College and also at the Review Meeting of the Chairmen/Chief Executive Officers of banks. The final Guidelines revised on the basis of the feedback received from banks are enclosed, for implementation by banks, effective **April 1, 1999.** In this connection, we have to advise as under:

2. Banks should give adequate attention to putting in place an effective ALM System. Banks should set up an internal Asset-Liability Committee (ALCO), headed by the CEO/CMD or the ED. The Management Committee or any specific Committee of the Board should oversee the implementation of the system and review its functioning periodically.

3. Keeping in view the level of computerisation and the current MIS in banks, adoption of a **uniform ALM System** for all banks may not be feasible. The final guidelines have been formulated to serve as a benchmark for those banks which lack a formal ALM System. Banks which have already adopted more sophisticated systems may continue their existing systems but they should ensure to fine-tune their current information and reporting system so as to be in line with the ALM System suggested in the Guidelines. Other banks should examine their existing MIS and arrange to have an information system to meet the prescriptions of the new ALM System. To begin with, banks should ensure coverage of **at least 60%** of their liabilities and assets. As for the remaining 40% of their assets and liabilities, banks may include the position based on their estimates. It is necessary that banks set targets in the interim, for covering 100 per cent of their business by **April 1, 2000**. The MIS would need to ensure that such minimum information/data consistent in quality and coverage is captured and once the ALM System stabilises and banks gain experience, they must be in a position to switch over to more sophisticated techniques like Duration Gap Analysis, Simulation and Value at Risk for interest rate risk management.

4. In order to capture the maturity structure of the cash inflows and outflows, the Statement of Structural Liquidity (Annexure-I) should be prepared, to start with, as on the last reporting Friday of March/June/ September/December and put up to ALCO/Top Management within a month from the close of the last reporting Friday. It is the intention to make the reporting system on a fortnightly basis by **April 1, 2000.** The Statement of Structural Liquidity should be placed before the bank's Board in the next meeting. It would also be necessary to take into account the rupee inflows and outflows on account of previously contracted forex transactions (swaps, forwards, etc). Tolerance levels for various maturities may be fixed by the bank's Top Management depending on the bank's asset - liability profile, extent of stable deposit base, the nature of cash flows, etc. In respect of mismatches in cash flows for the 1-14 days bucket and 15-28 days bucket, it should be the endeavour of the bank's management to keep the cash flow mismatches at the minimum levels. To start with, the mismatches (**negative gap**) during 1-14 days and 15-28 days in normal course may not exceed 20% each of the cash outflows during these time buckets. If a bank in view of its structural mismatches needs higher limit, it could operate with higher limit with the approval of its Board/Management Committee, giving specific reasons on the need for such higher limit. **The objective of RBI is to enforce the tolerance levels strictly by April 1, 2000.**

5. In order to enable the banks to monitor their liquidity on a dynamic basis over a time horizon spanning from 1-90 days, an indicative format (Annexure III) is enclosed. The statement of Short-term Dynamic Liquidity should be prepared as on each reporting Friday and put up to the ALCO/Top Management within 2/3 days from the close of the reporting Friday.

6. We advise that in the Statement of Interest Rate Sensitivity (Annexure - II) only rupee assets, liabilities and off-balance sheet positions should be reported. The statement should be prepared as on the last reporting Friday of March/June/September/December and submitted to the ALCO / Top Management within a month from the last reporting Friday. It should also be placed before the bank's Board in the next meeting. The banks are expected to move over to monthly reporting system by **April 1, 2000**. The information collected in the statement would provide useful feedback on the interest rate risk faced by the bank and the Top Management/Board would have to formulate corrective measures and devise suitable strategies wherever needed.

7. The guidelines for ALM cover the banks' operations in **domestic currency**. In regard to foreign currency risk, banks should follow the instructions contained in Circular AD (MA Series) No.52 dated December 27, 1997 issued by the Exchange Control Department.

8. As regards furnishing of data to RBI, a separate communication will follow from the Department of Banking Supervision.

9. This circular may please be placed before the Board of Directors at its next meeting

10. Please acknowledge receipt.

Yours faithfully,

(**A . Ghosh**)
Chief General Manager