Disclosure on **Basel III**

Overview

To strengthen global capital and liquidity rules with the goal of promoting a more resilient banking sector, the Basel Committee on Banking Supervision (BCBS) issued "Basel III: A global regulatory framework for more resilient banks and banking systems" in December 2010. Basel III reforms was to improve the banking sector's ability to absorb shocks arising from financial and economic stress, whatever the source, thus reducing the risk of spillover from the financial sector to the real economy. Through its reform package, BCBS also aims to improve risk management and governance as well as strengthen banks' transparency and disclosures.

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. Besides, the reforms have a macro prudential focus also, addressing system wide risks, which can build up across the banking sector, as well as the procyclical amplification of these risks over time. These new global regulatory and supervisory standards mainly addressed the following areas:

- 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.

To cope up with the international best practices and to make the bank's capital shock absorbent 'Guidelines on Risk Based Capital Adequacy (RBCA) for banks' (Revised Regulatory Capital Framework for banks in line with Basel III) came into force from January 2015.

MBL believes that Basel III is not merely a reporting system rather it is a new risk management technique for the Bank. Therefore, it has put extensive care and attention to implement Basel III inside the Bank. With a view to facilitating the way of implementation, the Bank has formed "Basel Implementation Unit". A supervisory committee includes top management of the Bank overseen the unit. The committee forecast the future; follow up the overall implementation status and way out the probable solution to cope with the international best practices and to make the bank's capital more risk sensitive as well as more shock resilient. The Bank has also formed a Supervisory Review Process (SRP) team to participate the dialogue with the

Supervisory Review Evaluation Process (SREP) team of BB for measuring the adequate capital requirement.

The Basel III principle stands on the following three pillars:

- **Pillar-I: Minimum Capital Requirement**

Banks must hold minimum regulatory capital against Credit, Market and Operational Risk inherent with Banking Business.

- **Pillar-II: Supervisory Review Process (SRP)**

The key principle of SRP is that banks have a process for assessing overall capital adequacy in relation to their risk profile and a strategy for maintaining their capital at an adequate level. The assessment of adequate capital would be the outcome of the dialogue between the bank's SRP and Bangladesh Bank's SREP team.

- **Pillar-III: Market Discipline**

The purpose of Market discipline in the Revised Capital adequacy Framework is to complement the minimum capital requirements and the supervisory review process. The aim of introducing Market discipline in the revised framework is to establish more transparent and more disciplined financial market so that stakeholders can assess the position of a bank regarding holding of assets and to identify the risks relating to the assets and capital adequacy to meet probable loss of assets. For the said purpose, banks will develop a set of disclosure containing the key pieces of information on the assets, risk exposures, risk assessment processes, and hence the capital adequacy to meet the risks.

Disclosure Framework

Bank has a formal disclosure framework approved by the Board of Directors/Chief Executive Officer. The following detailed qualitative and quantitative disclosures of the Bank is furnished to provide our stakeholders with consistent and understandable disclosure framework to assess the Bank's position regarding holding of assets and to identify the risks relating to the assets and capital adequacy to meet probable loss of assets as on December 31, 2015 in line with Bangladesh Bank's Risk Based Capital Adequacy (RBCA) guideline.

a) Scope of application

Qualitative Disclosures		
(a)	The name of the corporate entity in the group to which the guidelines applies.	**Mercantile Bank Limited (MBL)**
(b)	An outline of difference in the basis of consolidation for accounting and regulatory purposes, with a brief description of the entities within the group (a) that are fully consolidated; (b) that are given a deduction treatment; and (c) that are neither consolidated nor deducted (e.g. where the investment is risk-weighted).	MBL, the leading third generation private commercial bank incorporated as a public limited company in Bangladesh on May 20, 1999 and commenced its business on June 02, 1999. It was listed in DSE and CSE on February 16, 2004 and February 26, 2004 respectively. MBL has 109 (One Hundred Nine) branches including 5 (Five) SME/Krishi branches as on reporting date i.e. December 31, 2015. The Bank has 2 (Two) Off-shore Banking Units (OBU) operating at Gulshan and Chittagong EPZ areas. The cardinal activities of the Bank are to serve commercial banking services to its customers. The Bank has 2 (Two) subsidiaries namely "Mercantile Bank Securities Limited' and "Mercantile Exchange House (UK) Limited". **Mercantile Bank Securities Limited** Mercantile Bank Securities Limited (MBSL), a subsidiary company of MBL formed on 27 June 2010 to deal with stock dealing and broking. MBSL has started its commercial operation from 14 September 2011 through obtaining stock dealer and broker license from Bangladesh Securities and Exchange Commission (BSEC). The main operation of the subsidiary is to buy and sell off securities listed with Dhaka and Chittagong stock exchange or approved by BSEC for open market operation for its customer. Margin loan facility is also extended to its customers against their equity for investment in the listed companies. **Mercantile Exchange House (UK) Limited** Mercantile Exchange House (UK) Limited, a fully owned subsidiary company of MBL incorporated as private limited company with companies for England and Wales under registration no. 07456837 dated December 01, 2010. The company commenced its business operation on December 06, 2011. Mercantile Exchange House is committed to provide faster, easier and safer remittance services to the Bangladeshi expatriate living and working in UK.

(c)	Any restriction, or other major impediments, on transfer of funds or regulatory capital within the group.	Not applicable.
Quantitative Disclosures		
(d)	The aggregate amount of surplus capital of insurance subsidiaries (whether deducted or subjected to an alternative method) included in the capital of the consolidated group.	Not applicable.

b) Capital Structure

Qualitative Disclosures

(a) Summary information on the terms and conditions of the main features of all capital instruments, especially in the case of capital instruments eligible for inclusion in CET 1, Additional Tier 1 or Tier 2.

The regulatory capital under Basel-III is composed of;

- Tier 1 (going-concern capital) and
- Tier 2 (gone-concern capital)

Tier 1 capital is composed of;

(a) Common Equity Tier 1 (CET-1) and

(b) Additional Tier 1 (AT-1)

Conditions set by BB for maintaining Regulatory Capital are as below;

- Common Equity Tier 1 of at least 4.5% of the total RWA.
- Tier 1 capital will be at least 5.50% of the total RWA.
- Minimum CRAR of 10% of the total RWA.
- Additional Tier 1 capital can be admitted maximum up to 1.5% of the total RWA or 33.33% of CET1, whichever is higher.
- Tier 2 Capital can be admitted maximum up to 4.0% of the total RWA or 88.89% of CET1, whichever is higher.
- In addition to minimum CRAR, Capital Conservation Buffer (CCB) is being introduced which will be maintained in the form of CET1 from year 2016.
- In order to arrive at the eligible regulatory capital for the purpose of calculating CRAR, banks are required to make some regulatory adjustments/ deductions from Tier 1 and Tier 2 Capital.

Quantitative Disclosures

(b) The amount of Regulatory capital, with separate disclosure of:

(BDT in Crore)

	Particulars	Solo	Consolidated
Tier 1 Capital			
A	Common Equity Tier 1 Capital (CET-1)		
	Fully Paid Up Capital	739.16	739.16
	Non-repayable Share Premium account	-	-
	Statutory Reserve	475.18	475.18
	General Reserve	-	-
	Retained Earning	89.25	89.40
	Dividend Equalization Account	4.57	4.57
	Minority Interest in Subsidiaries	-	5.26
	Others (If any item approved by Bangladesh Bank)	-	-
	Sub-Total (A)	1,308.15	1,313.57
	Regulatory Adjustments/Deductions from CET-1	17.30	17.30
	Total Common Equity Tier 1 Capital (CET-1)	1,290.86	1,296.28
B	**Additional Tier-1 Capital (AT-1)**	**0.00**	**0.00**
Total Tier 1 Capital (A+B)		**1,290.86**	**1,296.28**

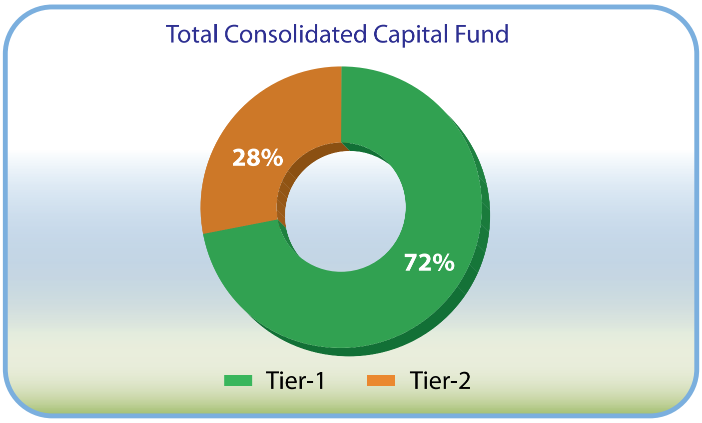
Tier 2 Capital			
	General Provision	162.68	163.02
	Subordinated Debt/Instruments	300.00	300.00
	Revaluation Reserves (as on 31 December, 2014)	54.57	54.57
	Sub-Total	517.25	517.57
	Regulatory Adjustments/Deductions from Tier 2 Capital	10.91	10.91
Total Tier-2 capital		**506.34**	**506.67**
Total Eligible Capital (Tier 1+Tier 2)		**1,797.20**	**1,802.95**

(c) Regulatory Adjustments/Deductions from Capital

Particulars	Solo	Consolidated
Regulatory Adjustments/Deductions from CET-1		
Shortfall in provisions required against investment in Share (Quoted Share excluding director Equity Shares)	17.30	17.30
Regulatory Adjustments/Deductions from Tier 2 Capital		
20% of Revaluation Reserves for Fixed assets, Securities & Equity (phase-in deductions as per Basel III guideline)	10.91	10.91

(d) Total Eligible Capital

Particulars	Solo	Consolidated
Total Tier 1 Capital (CET-1 + AT-1)	1,290.86	1,296.28
Total Tier-2 capital	**506.34**	**506.67**
Total Eligible Capital (Tier 1 + Tier 2)	**1,797.20**	**1,802.95**



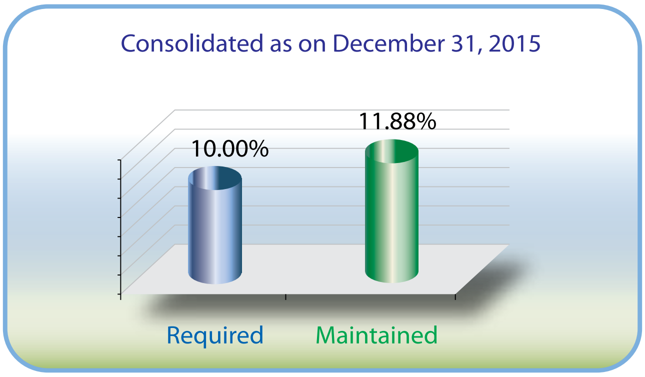
c) Capital Adequacy

Qualitative Disclosures		
(a)	A summary discussion of the Bank's approach to assessing the adequacy of its capital to support current and future activities.	MBL has adopted Standardized Approach for computation of Capital Charge for Credit Risk and Market Risk while Basic Indicator Approach for Operational Risk. Total Risk Weighted Assets(RWA) of the Bank is determined by multiplying the capital charge for market risk and operational risk by the reciprocal of the minimum capital adequacy ratio i.e. 10% as on December 2015 and adding the resulting figures to the sum of risk weighted assets for credit risk. Total RWA is then used as denominator while total Eligible Regulatory Capital as on numerator to derive Capital to Risk weighted assets Ratio (CRAR) i.e. $$\text{CRAR} = \frac{\text{Total Eligible Regulatory Capital}}{\text{Credit RWA} + \text{Market RWA} + \text{Operational RWA}} \times 100$$ The Bank's CRAR on the basis of Consolidated and Solo are 11.88% and 11.87% respectively against minimum requirement of 10% as on December 31, 2015. MBL's policy is to manage and maintain its capital at an adequate level to raise its CRAR well above than minimum requirement in line with Basel III. Ultimate goal of the capital management process of MBL is to ensure that the Bank maintains its capital base at a level to absorb all the material risks. The Bank also ensures that the capital levels comply with all regulatory requirements.

Quantitative Disclosures

(BDT in Crore)

	Particulars	Solo	Consolidated
(b)	Capital Requirement for Credit Risk	1,301.45	1,304.14
(c)	Capital Requirement for Market Risk	73.89	73.89
(d)	Capital Requirement for Operational Risk	139.05	139.65
(e)	Individual Capital Ratio		
	Capital to Risk Weighted Assets Ratio(CRAR)	11.87%	11.88%
	CET-1 Capital to RWA Ratio	8.53%	8.54%
	Total Tier-1 Capital to RWA Ratio	8.53%	8.54%
	Tier-2 Capital to RWA Ratio	3.34%	3.34%
(f)	Capital Conservation Buffer	-	-
(g)	Available Capital under Pillar 2 Requirement	282.81	285.28



d) Credit Risk

Qualitative Disclosures		
(a)	**The general qualitative disclosure requirement with respect to credit risk, including:**	
	i) Definition of past due and impaired (for accounting purposes);	As per guideline of Bangladesh Bank, All Loans and Advances are grouped into 4 (four) categories namely- Continuous Loan, Demand Loan, Fixed Term Loan and Short-Term Agricultural Credit & Micro Credit for the purpose ofclassification. **Any continuous Loan will be classified as:** **Sub-standard-** if it is past due/overdue for 03 (three) months or beyond but less than 06 (six) months. **Doubtful**-if it is past due/overdue for 06 (six) months or beyond but less than 09 (nine) months **Bad/Loss**- if it is past due/overdue for 09 (nine) months or beyond. **Any Demand Loan will be classified as:** **Sub-standard-** if it remains past due/overdue for 03 (three) months or beyond but not over 06 (six) months from the date of expiry or claim by the bank or from the date of creation of forced loan. **Doubtful**- if it remains past due/overdue for 06 (six) months or beyond but not over 09 (nine) months from the date of expiry or claim by the bank or from the date of creation of forced loan. **Bad/Loss**- if it remains past due/overdue for 09 (nine) months or beyond from the date of expiry or claim by the bank or from the date of creation of forced loan.
		Fixed Term Loan will be classified as: **A. If Fixed Term Loan amounting up to BDT 10 Lacs:** **Sub-standard-** If the amount of past due installment is equal to or more than the amount of installment(s) due within 06 (six) months, the entire loan will be classified as "Sub-Standard". **Doubtful**-If the amount of past due installment is equal to or more than the amount of installment(s) due within 09 (nine) months, the entire loan will be classified as "Doubtful". **Bad/Loss**- If the amount of 'past due installment is equal to or more than the amount of installment(s) due within 12 (twelve) months, the entire loan will be classified as "Bad/Loss". **B. If Fixed Term Loan amounting more than BDT 10 Lacs:** **Sub-standard-** If the amount of past due installment is equal to or more than the amount of installment(s) due within 03 (three) months, the entire loan will be classified as "Sub-Standard". **Doubtful**-If the amount of past due installment is equal to or more than the amount of installment(s) due within 06 (six) months, the entire loan will be classified as "Doubtful". **Bad/Loss**- If the amount of 'past due installment is equal to or more than the amount of installment(s) due within 09 (nine) months, the entire loan will be classified as "Bad/Loss".
		Short-Term Agricultural Credit & Micro Credit: **Sub-standard-** If the irregular status continues, after a period of 12 (twelve) months the credit will be classified as "Sub-standard". **Doubtful**- If the irregular status continues, after a period of 36 (thirty Six) months the credit will be classified as "Doubtful". **Bad/Loss**- If the irregular status continues, after a period of 60 (sixty) months the credit will be classified as "Bad/loss". A Continuous Loan, Demand Loan or a Term Loan which will remain overdue for a period of 02 (two) months or more, will be put into the Special Mention Account (SMA).

	ii) Description of approaches followed for specific and general allowances and statistical methods;	As per Bangladesh Bank's guideline, MBL maintainsGeneral and Specific provision in the following way:

Particulars	Rate (%)
General provision on all unclassified loans/SMA of Small and Medium Enterprise (SME)	0.25%
General provision against all unclassified loans/SMA (other than loans under Consumer Financing, Loans to Brokerage House, Merchant Banks, Stock Dealers etc., Special Mention Account as well as SME Financing.)	1%
General provision on the unclassified/SMA amount for Consumer Financing (other than Housing Finance and Loans for professionals to set up business)	5%
General provision on the unclassified/SMA amount for Housing Finance and Loans for professionals to set up business under consumer financing scheme	2%
General provision on the unclassified/SMA amount for Loans to Brokerage House, Merchant Banks, Stock Dealers, etc.	2%
General provision on the Off-Balance sheet exposures	1%
Specific Provision for classified Continuous, Demand and Fixed Term Loans:	
Substandard	20%
Doubtful	50%
Bad/Loss	100%
Specific Provision for Short-Term Agricultural and Micro-Credits	
All credits except 'Bad/Loss'	5%
Bad/Loss	100%

iii) Discussion of the Bank's credit risk management policy

The Bank bas adopted numerous strategies to manages its credit risk including:

- Creating credit risk awareness culture
- Approved credit policy by the Board of Directors
- Separate credit risk management division
- Formation of law and recovery division
- Formation of Recovery Team with Senior Executives
- Independent internal audit and direct access to Board/Audit committee
- Credit quality and portfolio diversification
- Early warning system
- Provision and suspension of interest
- Scientific lending and credit approval process
- Counterparty credit rating
- Strong NPL management system

Quantitative Disclosures

(b) Total gross credit risk exposures broken down by major types of credit exposure.

Total Gross Credit Risk exposures broken down by major types of credit exposure as on December, 2015 is as under:

Particulars	BDT in Crore
Term Loan	3,418.20
Time Loan	1,107.09
Packing Credit	142.71
Loan against Trust Receipt (LTR)	397.43
Lease Finance	104.64
EDF Loan	581.57
Loan General	80.56
House Building Loan	290.39
Hire Purchase	658.08
Payment Against Documents (PAD)	45.83
Cash Credit (Hypo)	1,097.98
Overdraft	2,223.35
Home Loan Scheme Refinance	0.64
Personal Loan	28.52
Consumer Credit Scheme	1.78
Consumer Finance	104.77
Other Credit Scheme	0.24
Staff Loan	69.65
Credit Card	28.66
Small and Medium Enterprise (SME) Loan	1,165.69
Agricultural Credit	220.22
Bill Purchased and Discounted-Inland	656.29
Bill Purchased and Discounted-Foreign	209.59
Total	**12,633.88**

(c) Geographical distribution of exposure, broken down in significant areas by major types of credit exposure

Geographical Distribution of total exposure as on December, 2015 is as under:

Particulars	BDT in Crore
Urban:	
Dhaka	8,479.69
Chittagong	2,102.59
Rajshahi	851.86
Sylhet	92.35
Khulna	98.26
Rangpur	94.25
Barisal	114.32
Sub-Total (A)	**11,833.32**
Rural	
Dhaka	350.51
Chittagong	345.87
Rajshahi	89.99
Sylhet	6.73
Rangpur	6.00
Barisal	1.46
Sub-Total (A)	**800.56**
Grand Total (A+B)	**12,633.88**

(d)	Industry or counterparty type distribution of exposures, broken down by major types of credit exposure	Industry or counterparty type distribution of exposures, broken down by major types of credit exposure.	
		Particulars	**BDT in Crore**
		Garments	1,916.31
		Trading	1,745.77
		Engineering	1,550.82
		Contractor Finance	105.86
		Leasing Company	178.48
		Housing	690.80
		Food, Food product, Beverage, Edible oil etc	1,008.60
		Pharmaceuticals	198.80
		Tele-communication	49.74
		Transport	221.78
		Leather & Leather Product	85.52
		Jute Industries	190.26
		Textile	370.79
		Information Technology	17.78
		Hospital & Medical Service	82.93
		Paper, Paper Production & Publication	273.12
		Plastic & Plastic Materials	132.64
		Storage	39.59
		Glass & Glass Product	0.00
		Agriculture	220.22
		SME Loan	1,165.69
		Credit Card	28.66
		Consumer Loan	164.66
		Loans to Brokerage House	475.10
		Others	1,719.96
		Total	**12,633.88**
(e)	Residual contractual maturity breakdown of the whole portfolio, broken down by major types of credit exposure	Residual contractual maturity breakdown of total exposure as on December, 2015 is as under:	BDT in Crore
		Up to 1 (one) month	2,495.32
		Over 1 (one) month but not more than 3 (three) months	1,472.81
		Over 3 (one) months but not more than 1 (one) year	4,243.46
		Over 1 (one) year but not more than 5 (five) years	2,766.73
		Over 5 (five) years	1,655.56
		Total	**12,633.88**
(f)	**By major industry and counter party type:**		
	i) Amount of impaired loans and if available, past due loans, provided separately	**Impaired Loan under 4 (four) broad categories as on December 31, 2015 is as under**	
		Particulars	**BDT in Crore**
		Continuous Loan	128.49
		Demand Loan	97.62
		Term Loan	398.53
		Short Term Agro Credit and Micro Credit	0.43
		Total	**625.07**
	ii) Specific and general provisions; and	**According to Bangladesh Bank's guideline, Specific and general provisions made as on December 31, 2015 is as under**	
		Particulars	BDT in Crore
		General Provision (including SMA & OBU)	370.38
		Specific Provision (SS, DF, Bad/Loss)	255.10
		Provision for Off-balance Sheet Exposure	61.64

	iii) Charges for specific allowances and charge-offs during the periods	**During the year 2015 following provisions were made on un classified, classified and off-balance sheet exposure as per Bangladesh Bank's guideline**	
		Particulars	**BDT in Crore**
		Provision against Un Classified Loans	116.10
		Provision against Classified Loans	9.80
		Other Provision (Off Balance Sheet Items)	3.34

(g)	Gross non-performing assets (NPAs):	**Gross non-performing assets as on December 31, 2015 is as under**	
		Particulars	**BDT in Crore**
		Gross non-performing assets (NPAs):	
		Non-performing Assets (NPAs) to Outstanding Loans & Advances	4.95%
		Movement of Non Performing Assets	
		Opening balance	606.46
		Additions	75.92
		Reductions	57.31
		Closing Balance	625.07
		Movement of specific provisions for NPAs	
		Opening balance	240.48
		Recoveries of amount from pre-written off	4.32
		Provisions made during the period	19.25
		Write-off	0.32
		Write-back of excess provisions	-
		Closing Balance	255.09

e) Equities: Disclosure for Banking Book Positions

Qualitative Disclosures		
(a)	**The general qualitative disclosure requirement with respect to equity risk, including:**	
	Differentiation between holdings on which capital gains are expected and those taken under other objectives including for relationship and strategic reasons.	MBL's total equity share holding comprises of two purposes i.e. capital gain and other strategic reason like equity participation and investment diversification. MBL is the director of IDLC finances Ltd. and sole purpose of such investment is not capital gain, rather maintain relationship as well as diversify its investment portfolio. Investment in equity securities are broadly fall under 2 categories: • Quoted Securities (traded in the secondary market; trading book assets) & • Unquoted Securities (not traded in secondary market; banking book assets)
	Discussion of important policies covering the valuation and accounting of equity holdings in the banking book. This includes the accounting techniques and valuation methodologies used, including key assumptions and practices affecting valuation as well as significant changes in the practices.	Quoted shares are recorded at cost prices and after every quarter end if the total cost of entire portfolio is higher than the market value, provision is maintained to the extent of differential amount of cost and market value of the portfolio as per terms and condition of regulatory authority. On the other hand, unquoted share is valued at cost price or book value as per latest audited accounts.

Quantitative Disclosures

(BDT in Crore)

	Particulars	Solo	Consolidate
(b)	Value disclosed in the balance sheet of investment, as well as the fair value of those investments; for quoted securities, a comparison to publicly quoted share values where the share price is materially different from fair value.		
	• Quoted shares	58.70	58.70
	• Un Quoted shares	442.50	442.50
(c)	The cumulative realized gain (losses) arising from sales and liquidations in the reporting periods.		
	· Realized gain (losses) from equity investments	1.29	1.29
(d)	Total unrealized gains (losses)	88.92	88.92
	Total latent revaluation gains (losses)	-	-
	Any amount of the above included in tier 2 Capital	-	-
(e)	Market value of investment in equities as on December 31, 2015	147.62	147.62
	Specific Risk- Capital Requirement is 10% of the said value	14.76	14.76
	Market value of investment in equities as on December 31, 2015	147.62	147.62
	General Risk- Capital Requirement is 10% of the said value	14.76	14.76

f) : Interest rate risk in the banking book (IRRBB)

Qualitative Disclosures

(a)	The general qualitative disclosure requirement including the nature of IRRBB and key assumptions, including assumptions regarding loan prepayments and behavior of non-maturity deposits, and frequency of IRRBB measurement.	Interest rate risk in the banking book arises from mismatches between the future yield of an assets and their funding cost. Assets Liability Committee (ALCO) monitors the interest rate movement on a regular basis.MBL measure the Interest Rate Risk by calculating Duration Gap i.e. positive Duration Gap affects bank's profitability adversely with the increment of interest rate and negative Duration Gap increase the bank's profitability with the reduction of interest rate.

Quantitative Disclosures

(b) The increase (decline) in earnings or economic value (or relevant measure used by management) for upward and downward rate shocks according to management's method for measuring IRRBB, broken down by currency (as relevant)

Increase of Interest Rate will affect the Bank in the following ways:

Particulars	Minor Shock	Moderate Shock	Major Shock
Magnitude of Shock	1%	2%	3%
Duration Gap (Years)	0.75	0.75	0.75
Total Regulatory Capital (BDT in Cr)	1,797.20	1,797.20	1,797.20
Risk Weighted Assets (BDT in Cr)	15,143.87	15,143.87	15,143.87
CRAR	11.87%	11.87%	11.87%
Revised Capital (After Shock)	1,660.52	1,523.83	1,387.15
Revised RWA	14,674.74	14,674.74	14674.74
Revised CRAR (%)	11.32%	10.38%	9.45%

g) : Market Risk

Qualitative Disclosures

(a) Views of BOD on trading/ investment activities

Market Risk is the possibility of losing assets in balance sheet and off-balance sheet positions arising out of volatility in market variables i.e. interest rate, exchange rate and price. Total capital requirement for MBL against its market risk is the sum of the following

i) Interest Rate risk
ii) Equity position risk
iii) Foreign Exchange risk
iv) Commodity risk

All the Market Risk related policies/guidelines are duly approved by BOD. The BOD sets limit, review and update the compliance on regular basis aiming to mitigate the Market risk.

	Methods used to measure Market risk	In order to calculate the market risk for trading book purposes the Bank uses Standardized (rule based) Approach where capital charge for interest rate risk, price and foreign exchange risk is determined separately. For instance, MBL's total market risk is calculated as below: i) Capital Charge for interest Rate Risk = Capital Charge for Specific Risk + Capital Charge for General Market Risk. ii) Capital Charge for Equity Position Risk = Capital Charge for Specific Risk + Capital Charge for General Market Risk. iii) Capital Charge for Foreign Exchange Risk = Capital Charge for General Market Risk. iv) Capital Charge for Commodity Position Risk = Capital Charge for General Market Risk.
	Market Risk Management system	Treasury Division and International Division manage the Market Risk with the help of Asset Liability Committee (ALCO) and Asset Liability Management (ALM) Desk.
	Policies and Processes for mitigating market risk	Policy for managing Market Risk has been set out by the Board of Directors of the Bank where clear instructions has been given on Loan Deposit Ratio, Whole Sale Borrowing Guidelines, Medium Term Funding, Maximum Cumulative Outflow, Liquidity Contingency Plan, Local Regulatory Compliance, Recommendation / Action Plan etc. Furthermore, special emphasis has been put on the following issues for mitigating market risk: • **Interest Rate Risk Management** Treasury Division reviews the risks of changes in income of the Bank as a result of movements in market interest rates. In the normal course of business, the Bank tries to minimize the mismatches between the duration of interest rate sensitive assets and liabilities. Effective Interest Rate Risk Management is done as under: • **Market Analysis** Market analysis over interest rate movements are reviewed by the Treasury Division of the Bank. The type and level of mismatch interest rate risk of the Bank is managed and monitored from two perspectives, being an economic value perspective and an earning perspective.
		• **Gap Analysis** ALCO has established guidelines in line with central Bank's policy for the management of assets and liabilities, monitoring and minimizing interest rate risks at an acceptable level. ALCO in its regular monthly meeting analyzes Interest Rate Sensitivity by computing GAP i.e. the difference between Rate Sensitive Assets and Rate Sensitive Liability and take decision of enhancing or reducing the GAP according to prevailing market situation aiming to mitigate interest rate risk. • **Foreign Exchange Risk Management** Risk arising from potential change in earnings resulted from exchange rate fluctuations, adverse exchange positioning or change in the market prices are considered as Foreign Exchange Risk. Treasury and International Division manage this risk in the following fashion: • **Continuous Supervision** Bank's Treasury Division manages and controls day-to-day trading activities under the supervision of ALCO that ensures continuous monitoring of the level of assumed risks. Treasury Division monitors the foreign exchange price changes and Back Office of the Treasury Division verifies the deals and passes the entries in the books of account.
		• **Equity Risk Management** Equity Risk is the risk of loss due to adverse change in market price of equities held by the Bank. Equity Risk is managed by the following fashion:

- **Treasury Back Office separated from Treasury Front Office**

  Treasury Back Office is conducting its operation in separate locations apart from the Treasury Front Office. Treasury Back Office is responsible for currency transactions, deal verification, limit monitoring and settlement of transactions independently. Treasury Back Office gathers the market rates from an independent source other than dealers of the same organization, which helps to avoid any conflict of interest.

- **Mark-to-Market Method for Approved Securities and Foreign Exchange Revaluation**

  All foreign exchange reserves and balances along with approved securities are revalued at Mark-to-Market method according to Bangladesh Bank's guidelines. Such valuations are made after specific time interval as prescribed by Bangladesh bank.

- **Nostro Accounts**

  Nostro accounts are maintained by the Bank with various currencies and countries. These Accounts are operated by the International Division of the Bank. All Nostro accounts are reconciled on monthly basis. The management reviews outstanding entry beyond 30 days for settlement purpose.

- **Investment Portfolio Valuation**

  Mark-to-Market valuations of the share investment portfolio is followed in measuring and identifying risk. Mark-to-Market valuation is done against a predetermined cut loss limit.

- **Diversified Investment to minimize Equity Risk**

  MBL minimizes the Equity Risks by Portfolio diversification as per investment policy of the Bank.

- **Margin Accounts are monitored very closely**

  Where Margin loan is allowed, security of investment, liquidity of securities, reliability of earnings and risk factors are considered and handled professionally.

Quantitative Disclosures (BDT in Crore)

Particulars	Solo	Consolidate
Interest Rate Risk	30.45	30.45
Equity Position Risk	29.52	29.52
Foreign Exchange Risk	13.91	13.91
Commodity Risk	-	-
Total Capital Requirement for Market Risk	**73.88**	**73.88**

h) : Operational Risk

Qualitative Disclosures

(a)	Views of BOD on system to reduce Operational Risk	All the policies/guidelines including Internal Control and Compliances and Board audit are duly approved by BOD. Audit Committee of the Board directly oversees the activities of internal control and compliances aiming to check all types of lapses and irregularities inherent with operational activities of the Bank and thereby may create a notable downfall risk for the Bank. Operational risk includes legal risk, but excludes strategic and reputation risk. Operational Risk includes: • Transaction processing • Operation control • Technology and systems • Risks of physical and logical security • Unique risk arises due to outsourcing

	Performance gap of executives and staffs	The BOD of the Bank is always keen to provide a competitive, attractive and handsome remuneration package for its employees. Besides, the recruitment policy of the Bank always emphasizes on sorting out fresh graduate from the reputed universities and nurture them until transformation to a 'Human Capital' of highest quality. Besides, the Bank's name and fame as top tier Bank of the country acts as moral boosting factor for the employees. An accommodating, welcoming, co-operative and congenial work atmosphere motivates its employees to act as a family towards achievement of goal. As such, there exists no performance gap in the Bank.
	Potential external events	No potential external events have been detected yet at the time of reporting of the capital accord.
	Policies and processes for mitigating operational risk	Operational Risks results from inadequate or failed internal process, people and systems or from external events. Within the Bank, Operational Risk may arise from negligence and dishonesty of the employees, lack of management supervision, inadequate operational control, lack of physical security, poor technology, lack of automation, non- compliance of regulatory requirements, internal and external fraud etc. Operational Risk Management Framework has been designed to provide a sound and well-controlled operational environment and thereby mitigate the degree of operational risk.
	Approach for calculating capital charge for operational risk	Operational Risk is defined as the risk of loss resulting from inadequate or failed internal processes, people and system or from external events. The Bank use Basic Indicator Approach for calculating capital charge against operational risk i.e. 15% of average positive annual gross income of the Bank over the last three years.

Quantitative Disclosure

(b)	**particulars**	**Solo**	**Consolidate**
		BDT in Crore	
	Capital requirements for	**139.05**	**139.65**

i) : Liquidity Ratio

Qualitative Disclosures

(a)	Views of BOD on system to reduce Liquidity Risk	Board of Directors of the Bank always has been giving utmost importance to minimize the liquidity risk of the bank. In order to reduce liquidity risk strict maintenance of Cash Reserve Ratio (CRR) and Statutory Liquidity Reserve (SLR) are also being emphasized on a regular basis. Apart from these as a part of Basel-III requirement Liquidity Coverage Ratio (LCR) and Net Stable Funding Ratio (NSFR) are also maintained under the guidance and sharp insight of our honorable Board of Directors.
	Methods used to measure Liquidity Risk	
	Liquidity Risk Management System	As a part of liquidity risk management system we have board approved liquidity contingency plan. In this liquidity contingency plan we have incorporated all the strategic decision to tackle any sort of liquidity crisis. As per the Bangladesh Bank ALM guideline this liquidity contingency plan is reviewed annually which is approved by the Board of Directors.
	Policies and processes for mitigating Liquidity Risk	We have board approved policies for mitigating liquidity risk. This policy is reviewed annually and placed before the Board of Directors for their kind approval.

Quantitative Disclosure	
	(BDT in Crore)
Liquidity Coverage Ratio (LCR)	166.57%
Net Stable Funding Ratio (NSFR)	109.18%
Stock of High quality liquid assets	4,131.90
Total net cash outflows over the next 30 calendar days	2,480.58
Available amount of stable funding	16,273.42
Required amount of stable funding	14,905.48

j) : Leverage Ratio

Qualitative Disclosures		
(a)	Views of BOD on system to reduce excessive leverage	Leverage is an inherent and essential part of modern banking business. In other words, banks are highly leveraged organizations which facilitate leverage for others. Leverage, in simple terms, it is the extent to which a bank funds its assets with borrowings rather than capital. More debt relative to capital means a higher level of leverage. Banks have a range of financial incentives to operate with high leverage. But it creates risk when it crosses a certain point. Therefore, the board views that sound prudential controls are needed to ensure that the organization maintains a balance between its debt and equity. The board also believes that the bank should maintain its leverage ratio on and above the regulatory requirements which will eventually increase the public confidence on the organization.
	Policies and processes for mitigating excessive on and off balance sheet leverage	The leverage ratio is a non risk based approach to the measurement of leverage. The ratio acts as a 'backstop' against the risk-based capital requirements and is also designed to constrain excess leverage. The leverage ratio is intended to achieve the following objectives: a) Constrain the build-up of leverage in the bank b) Reinforce the risk based requirements with an easy to understand and a non-risk based measure. Under Basel III, the Bank has to maintain a minimum Tier 1 Leverage ratio of 3% is being prescribed both at solo and consolidated level. To manage excessive leverage, the bank follows all regulatory requirements for capital, liquidity, commitment, Advance Deposit Ratio (ADR), Maximum Cumulative Outflow (MCO), large exposures as well as risk management which are eventually reinforcing standards set by Bangladesh Bank. The aim is to ensure that the high leverage inherent in banking business models is carefully and prudently managed.
	Approach for Calculating exposure	Leverage ratio refers to the ratio between Bank's Tier 1 capital (as numerator) and total exposure (as denominator). Total exposure includes both balance sheet exposures and off-balance sheet exposures after related deductions.
		$\text{Leverage Ratio}=\dfrac{\text{Tier 1 Capital (after related deductions)}}{\text{Total Exposure (after related deductions)}}$ The capital measure for the leverage ratio is based on the Tier 1 capital after related deductions. The exposure measure for the leverage ratio follows the accounting measure of exposure. In order to measure the exposure consistently with financial accounts, the followings are applied by the bank:

		• On balance sheet, non-derivative exposures will be net of specific provisions and valuation adjustments. • Physical or financial collateral, guarantee or credit risk mitigation purchased is not considered to reduce on-balance sheet exposure. • Netting of loans and deposits is not considered. • Off-balance sheet (OBS) items are calculated by applying a uniform 100% credit conversion factor (CCF). For any commitments that are unconditionally cancellable at any time by the bank without prior notice, a CCF of 10% is applied.

Quantitative Disclosure

(BDT in Crore)

Particulars	Solo	Consolidated
Leverage Ratio	6.36%	6.36%
On balance sheet exposure	17,654.54	17,752.64
Off balance sheet exposure	2,655.23	2,655.23
Total exposure (After deduction from On and Off balance sheet exposure)	20,292.48	20,390.58

k) : Remuneration

Qualitative Disclosures

(a)	Information relating to the bodies that oversee remuneration.	Human Resources Division (HRD), Head Office of the Bank oversees the remuneration. The Human Resources Division comprises of 9 officials (2-executives and 7 officers) including Divisional Head. At present, the Division is directly supervising by the Managing Director of the Bank. The Board/Executive Committee of the Bank approves remuneration policy time to time. The Bank does not take any external consultants in preparing remuneration policy. The remuneration policy shall apply to all regular employees of the Bank and ensures its Scales of Pay equal grade benefit of the employees of their respective grade. Remuneration Committee of Bank also oversees its two subsidiaries i.e. MBL Exchange House (UK) Limited and MBSL.
		The senior management or employees who can take, or influence the taking of, material risk for Bank or for a material business unit are considered as material risk takers, such as;

Designation No of Employee	No. of Employee
Managing Director & CEO	1
Additional Managing Director	3
Deputy Managing Director	3
Senior Executive Vice President	9
Executive Vice President	10
Senior Vice President	22

(b)	Information relating to the design and structure of remuneration processes.	Mercantile Bank always considers employee benefits to make them feel good and get their commitment. We target a fair human resources management by using a performance based system. Our remuneration policy is the same in all branches and head office level. There is no incident of discrimination has been occurred in terms of remuneration provided to male and female employees. We believe that competitive remuneration creates opportunity to maintain and retain the performing and brilliant officers and executives in the Bank. The overall objective of the Bank's remuneration policy is to establish a framework for attracting, retaining and motivating employees, and creating incentives for delivering long-term performance. During the past year, the Bank did not review its remuneration policy.
(c)	Description of the ways in which current and future risks are taken into account in the remuneration processes.	The following key risks have been taken into account when implementing remuneration measures; Keep morale high of the employees and posting better result, reduce turnover, retain the experienced and productive officials, free from corruption etc.
(d)	Description of the ways in which the bank seeks to link performance during a performance measure-ment period with levels of remuneration.	Now Banking industries becomes very competitive. In the Banking sector performance plays a very vital role on determining someone's remuneration. Performance appraisal is closely linked to other HR processes like helps to identify the training and development needs, promotions, incentives etc. The focus of the performance assessment is measuring and improving the actual performance of the employee and also the future potential of the employee. Its aim is to measure what an employee does. The Bank has one set of Performance Appraisal Form (PAF) to evaluate the all categories officials of the Bank. The PAF has 3 (three) parts; **Part-A:** Basic information & Business development performance **Part-B:** Measurable Performance Rating & PAF Rating **Part-C:** Comments of Reporting Officer & Score sheet Yearly increment, promotions, incentives bonus all had now been linked up with individual performance. On the basis of grade of an individual of the Performance Appraisal Report, the Bank takes decision in allowing yearly benefits. At present the Bank does not consider such type of adjustment.
(e)	Description of the ways in which the bank seek to adjust remuneration to take account of longer-term performance.	The Bank has various schemes in regards to deferred and vested variable remuneration which are as under; **<u>Provident Fund (PF)</u>** Provident Fund is created to provide long term benefit to the employees of the Bank as per Deed of Trust executed between the company and the trustees of the Provident Fund. Entitlement to employer's contribution happens on completion of 05 (three) years of regular service and the Bank contributes equal amounvt of contribution as contributed by the employee. **<u>Gratuity</u>** Entitlement to employer's contribution happens on completion of 5 (five) years of regular service in the Bank @ one basic pay for each completed year of service.This increases depending on years of service if completed 11 years. **<u>Welfare Fund</u>** These rules called the Mercantile Bank Limited Employees' Welfare Fund Rules. This benefits Provides to the employees of the Bank on their death, disability or retirement at any time or for any other cause that may be deemed fit as per approved policy.

(f)	Description of the different forms of variable remuneration that the bank utilizes and the rationale for using these different forms.	MBL's compensation and benefits strategy has been devised to foster high performance culture keeping market competitiveness in mind. Our management strategy is a multi-pronged one; that includes compelling employee value proposition with a competitive reward package. Our total rewards strategy has evolved with our business transformation and basic pay is benchmarked against the market to ensure competitiveness. The Bank offers satisfactory financial and nonfinancial benefits for the employees of the Bank to ensure a better life style. Such as- • Attractive compensation package • Festival and incentive bonus • Fair promotion • Annual increment • Provident fund • Gratuity fund • Disability benefit • Leave fare assistance • Career growth opportunities • Training and workshop (home and abroad) • Favorable work environment • Health care facilities • Loan facilities at a privileged rate etc. Besides the above, we have platforms which provide recognition for outstanding performance, we offer career development opportunities, and we are dedicated to our employees' well-being. To boost motivation, we recognize and reward top performers, long service employees, best managers,
		executives and officers. Bank is maintaining a welfare fund taking contribution from both employees and the bank to support the employees and their families on the ground of medical, maternity, retirement, disability and death claim. The Fund has been established to provide coverage in the event of accidental death or permanent disabilities, a portion of retirement benefit & stipend to the employees' children. The Bank also extended the maternity leave from 03 months to 06 months for its female employees. Variable pay, as the term denotes usually does not defer between the employees of the same rank. Depending on experience, jobs performed and other traits new hire in the same rank the individuals are offered remuneration that varies from each other. While in the service on recommendation and according to performance extra increment or bonus may be awarded to the employees.

<table>
<tr><th colspan="3">Quantitative Disclosures</th></tr>
<tr><td>(g)</td><td>Number of meetings held by the main body overseeing remuneration during the financial year and remuneration paid to its member.</td><td>Meeting regarding overseeing the remuneration was held on need basis.</td></tr>
<tr><td>(h)</td><td>Number of employees having received a variable remuneration award during the financial year.</td><td>19 employees having received variable remuneration award during the financial year.</td></tr>
<tr><td></td><td>Number and total amount of guaranteed bonuses awarded during the financial year.</td><td>There are 2 incentive bonuses and 2 festival bonuses are awarded during the financial year.</td></tr>
<tr><td></td><td>Number and total amount of sign-on awards made during the financial year.</td><td>Nil</td></tr>
<tr><td></td><td>Number and total amount of severance payments made during the financial year.</td><td>Nil</td></tr>
<tr><td>(i)</td><td>Total amount of outstanding deferred remuneration, split into cash, shares and share-linked instruments and other forms.</td><td>Nil</td></tr>
<tr><td></td><td>Total amount of deferred remuneration paid out in the financial year.</td><td>Nil</td></tr>
<tr><td>(j)</td><td>Breakdown of amount of remuneration awards for the financial year to show:
- fixed and variable.
- deferred and non-deferred.
- different forms used (cash, shares and share linked instruments, other forms).</td><td>Breakdown of amount of remuneration awards for the financial year 2015;<table><tr><td>Basic salary</td><td>78.21</td></tr><tr><td>Allowances</td><td>66.61</td></tr><tr><td>Bonus</td><td>27.79</td></tr><tr><td>Provision for Gratuity</td><td>3.00</td></tr><tr><td>Provident fund contribution</td><td>7.54</td></tr></table>Nil
All the remunerations are provided in the form of cash</td></tr>
<tr><td>(k)</td><td colspan="2">Quantitative information about employees' exposure to implicit (eg fluctuations in the value of shares or performance units) and explicit adjustments (eg clawbacks or similar reversals or downward revaluations of awards) of deferred remuneration and retained remuneration:</td></tr>
<tr><td></td><td>Total amount of outstanding deferred remuneration and retained remuneration exposed to ex post explicit and/or implicit adjustments.</td><td>Nil</td></tr>
<tr><td></td><td>Total amount of reductions during the financial year due to ex post explicit adjustments.</td><td>Nil</td></tr>
<tr><td></td><td>Total amount of reductions during the financial year due to ex post implicit adjustments.</td><td>Nil</td></tr>
</table>