KIFML

KERALA INFRASTRUCTURE FUND MANAGEMENT LIMITED

RISK MANAGEMENT POLICY

JUNE 2023

Policy	Risk Management Policy	Version: 1.0
Reference: **KIFML :**	**Effective date:** **Approved by:**	

Revision History

Base Version	Release date	Rationale for change	Summary of changes	Updated by	Approved by
1.0					
1.1					
1.2					

1. PREAMBLE

KIFML is a, Kerala focused, Asset Management Company primarily engaged in managing multiple Investment funds – both raising and deploying funds in the best interests of the investors and is subject to the regulatory oversight of both ROC and SEBI, in respect of its fundamental role.

The primary objective of the Funds under KIFML is to invest in ESG compliant Infrastructure Projects and in start-ups within the state of Kerala, or projects / start-ups that would have a significant impact or presence in the state of Kerala. The Funds will operate within the framework that is permitted for a Category – II AIF under SEBI (Alternative Investment Fund) Regulations to provide superior, consistent, risk-adjusted returns to its contributors

2. OBJECTIVES OF RISK MANAGEMENT

The fundamental objective of the Risk Management Policy is to "to support the fund in achieving the targeted return while providing adequate guidelines towards management of risk". The accepted level of risk for the Fund would be defined by a comprehensive fund wise 'Risk Appetite Statement' as approved by the Investment Committee. This statement would also set the Risk tolerance level which would enable the Company to operate within the approved risk limits.

The fundamental objectives are further broken down as following:

- Identify and classify the risks and their triggers, their mitigants and tolerance of the Company to draw up a risk profile at project, fund and at company level
- Based on the above risk profile, establish clear risk limits for all the key processes
- Improving decision making, planning and prioritization by comprehensive and structured understanding and proactive management of business activities, volatility and opportunities/ threats. Effective allocation and use of available resources
- Improved incident management and reduction in loss and cost of risk
- Improved stakeholder confidence and trust
- A clear understanding by all staff of their roles, responsibilities and authorities for managing risk
- Better corporate governance
- To enable investment committee/ team to track each of the identified risks through a risk matrix approved by Board and ensure that appropriate management strategies are employed at different levels
- Ensure sustainable business growth with stability and promote a pro-active approach in reporting, evaluating and resolving risks associated with the company
- The development of a more risk aware organizational culture at all levels through enhanced communication and reporting.
- Design an appropriate internal control system to manage the risks

- Design and implement the process of monitoring the internal control system including the Risk Custodian, Risk Management Committee/ the Audit Committee of the BOD and the Internal Audit System and the reporting mechanism thereof.'

3. RISK MANAGEMENT DEFINITION

The processes involved in identifying and understanding the overall risks of an organization and taking informed steps to help achieve organizational goals, strategic objectives, reduced the possibilities of failure, and decrease the uncertainty of overall business performance is termed as Risk Management.

4. RISK MANAGEMENT OVERSIGHT

Board of Directors: The Board of Directors would have the overall responsibility and the requisite authority for governance which includes the governance of the Risk Management function and ensuring that the Company is fulfilling its fiduciary responsibilities. The board will review and set the strategy and risk appetite for the company.

Risk Management Committee / Audit Committee: The BOD would entrust the Audit Committee to carry out the mandate of both Risk Management and Audit functions. At a suitable time, BOD will have the power to appoint a separate Risk Management Committee.

It would be responsibility of the Management to produce compliance reports on the Risk Management framework for review by the Committee. The primary responsibility of Risk Management committee will be to proactively sensitize investment committee and MD/CEO of the risks that the firm / fund / project is facing. Power to take suitable corrective actions will be left to the investment committee / Board / MD/CEO.

The roles and responsibilities of Audit Committee (in interim), Risk Management Committee (when constituted) and Investment Committee with respect to risk management oversight will be as follows:

- Establishment and revision of the Enterprise and fund level risk management policy.
- Status report of annual investment performance and risk management; and
- Other risk management related matters which are required to be submitted to the BOD for deliberation and resolution.
- Recommend long term solutions regarding Risk Management
- The committee shall meet at least once a quarter
- The committee shall have the power to appoint a team as well as a chief risk officer (CRO) to manage risks at a suitable point in future

The committee will have functions at the enterprise level, as well as fund and project level

Key Enterprise Level functions of Risk Management Team when it comes into existence will be
• Establish and communicate the organization's ERM framework and define the appropriate role of risk management in the organization • Work with appropriate executives to establish the control environment that monitors risk across the enterprise and oversees and enforces risk management techniques to mitigate risk • Coordinate the application of risk assessment across the organization to obtain an enterprise-wide view of risk • Implement appropriate risk reporting to Risk Management Committee and the Board of Directors, • Develop measurement methodologies and monitoring methods, which aggregate risk exposures and risk management performance on an enterprise-wide basis
Key Functions of the Risk Management team when it comes into existence at a fund / project level will be
• Establish Risk Management framework methodology for assessment, mitigation, monitoring and reporting of risk, setting up and reviewing risk parameters • Implement appropriate risk reporting to the Board of Directors, Risk Management Committee and senior management • Monitoring various risks at a fund & project level

5. INVESTMENT COMMITTEE

Fund related risk management will be reported to the Investment Committee on a periodic basis. Key responsibilities of Investment committee with respect to risk management of funds will be:

- Review risk appetite for each fund under management and its governance.
- Review risk framework for each fund and any special fund specific provisions on risk policy with respect to investment
- Incorporating assessment, mitigation, and monitoring of risks in the approved Projects.
- Governance of risk management at fund and project level
- Governance of investment and trading related activities
- Review, discuss, set direction, and make decisions in Investment management issues.

6. RISK MANAGEMENT FRAMEWORK

KIFML will use the Enterprise Risk Management (ERM) framework which is designed to view risk in a holistic and portfolio-based manner, rather than addressing individual components which would not take the mutual interplay of such risks and its possible impact. The ERM framework is designed to effectively manage and monitor the entity level portfolio of project level risks. Through this risk management framework, the Company, presents an enterprise-wide approach to ensure that key aspects of risks that have an enterprise-wide impact are considered in its conduct of business. The primary objective of the Risk Management Framework is to ensure that the Company shall operate within the agreed risk tolerance and risk limits. This may be achieved by:

- Effective and efficient continuity of operations.
- Preservation of the reputation of the Company.
- Reliability of internal and external reporting; and
- Compliance with Applicable Laws.

The fundamental processes of the Company where risks have to be identified and managed are as follows:
- Raising funds
- Deploying funds
- Monitoring project execution
- Exit

ERM framework of the Company comprises of the following key components:

I. RISK IDENTIFICATION

Risks are events or conditions that may occur, and whose occurrence, if it does take place, has a harmful or negative impact on the achievement of the organization's business objectives. Risk identification begins with understanding the objectives of the Company. The purpose of identification of risks is to identify the events that have an adverse impact on the achievement of both the commercial and non-commercial objectives of the Company. Due to the dynamic work environment, this will be an ongoing process to ensure that all material risks are knows, understood and proactively managed. This involves learning from past experiences and recognising and managing emerging risks.

Key characteristics by which risks can be identified are:

- Risks are adverse consequences of events or changed conditions
- Their occurrence may be identified by the happening of trigger events
- Their occurrence is uncertain and may have different extents of likelihood

Recognizing the kind of risks that Company is/may be exposed to, risks will be classified broadly into the following categories at enterprise level

- ***Strategic risks:*** Include the range of external events and trends (like Government policy, competition, court rulings or a change in stakeholder requirements) that can adversely impact the Company's strategic growth trajectory and have impact on shareholder value.
- ***Governance Risk:*** The major risk of an Investment Manager is to not deliver on its fundamental task of independently running the fund that it has been tasked to manage, and therefore corporate governance is a key process to manage and mitigate the risk. KIFML views compliance, not as an option, but as law that cannot be violated. The governance risk will occur when regulatory compliance is weak, and the Company interests are compromised in the course of governance. In the case of our Company, it is pointed out that the regulatory environment would be quite strong since the Company

is accountable to both ROC and SEBI. The Company's structure has been built based on the need to ensure timely and total compliance to all the regulatory environments.

- ***Environmental risks:*** The environmental risk in the field of infrastructure finance cannot be overstated given the long investment horizon, regulatory developments and possibility of economic cycles. The Company is aware of these challenges and address these risks with proactive measures.
- ***Process Risk:*** Risk associated with the processes would be monitored by the CRO
- ***Financial risks:*** The risk that a Company will not have adequate cash flow to meet financial obligations.
- ***Reputation risks:*** It is type of risk related to the trustworthiness of business. Damage to Company's reputation can result in loss of revenue or destruction of shareholder value, even if the Company is not found guilty. Reputation risk can be a matter of corporate trust, but serves also as a tool in crisis prevention
- ***Compliance risk:*** Compliance risk is the current and prospective risk to earnings or capital arising from violations of, or nonconformance with, laws, rules, regulations, prescribed practices, internal policies, and procedures, or ethical standards

Recognizing the kind of risks that fund is/may be exposed to, risks are classified broadly into the following categories at fund level

- ***Investment risks:*** Probability or likelihood of occurrence of losses relative to the expected return on any particular investment. To put it simply, it is a measure of the level of uncertainty of achieving returns as per the expectations of the investor
- ***Operational risks:*** The risk of loss resulting from inadequate or failed business processes, people and systems or from external events
- ***Compliance risk:*** Compliance risk is the current and prospective risk to earnings or capital arising from violations of, or nonconformance with, laws, rules, regulations, prescribed practices, internal policies, and procedures, or ethical standards. It is the failure to meet statutory or regulatory obligations and may result in investigations, fines, financial forfeiture, regulatory sanctions, and/or material loss to investors and organisation
- ***Market risks:*** Market risk arises from changes in economic situation such as interest rate shifts, price volatility
- ***Credit risks:*** Credit risk is the risk that results in change in the credit quality of a counterparty will affect the value of a lender's position (default or credit downgrade). Credit risk is only an issue when the position is an asset (positive replacement value).
- ***Exit risks: Exit*** risk refers to the possibility that it may be difficult or impossible to exit an investment. Though all investments made will have well defined liquidity/exit options, at the outset, there could be environmental or regulatory changes which constrains the exit strategy thereby exposing the investment to risks.

II. RISK ASSESSMENT

Risk assessment will be performed based on inputs from the Senior Management of the Company and the Investment Committee. Following steps will be adopted for the purpose of risk assessment:

- ***Objective setting:*** The senior management has set organisational objectives under broad categories of risk categories defined in section above.
- ***Identification of risk events and assessment:*** An event is defined as an incident or occurrence, from sources internal or external to an entity that affects achievement of objectives. Risk is defined as the probability that an event will occur and adversely affect the achievement of objectives. For each of the risks identified in section before , risk events will be identified at entity level which will be further percolated down to project level risks which will be monitored by the management and investment committee.
- ***Assessment of inherent likelihood and impact:*** A Risk Assessment pertaining to the identified objectives and risks will be carried out. It is the primary responsibility of the individual process owner to identify the key risk impacting the individual process along with the relevant risk triggers, the likely effects, probability of occurrence, impact of occurrence and controls available for prevention and detection. Scores need to be assigned from 1-10 for probability of occurrence, impact (Severity), controls effectiveness. The product of the 3 scores which will be called the Risk Priority Number (RPN) which will represent the level of residual risks given the existing controls. The RPN scores will help in identifying the high-risk events which require to be addressed. Based on the RPN scores, Risk Register will be updated by the process owner. There would be a formal custodian for maintaining the Risk, who would be responsible for all activities concerned with the stewardship and management of risk. Sector studies are to be undertaken in order to determine the sectors that have a higher risk component. This shall be used to determine the likely impacts and explore if said sector could deliver the promised return. This investment committee shall use these sector assessments to make relevant investment decisions based on cost-benefit analysis.

Definitions of probability of occurrence (High, Medium, Low) and Impact (measured in terms of potential financial loss) are defined below.

Probability description	Indicators	Ratings
High (Probable)	Potential of it occurring several times within the time period and has occurred recently	7-9
Medium (possible)	Could occur more than once within the time period. Could be difficult to control due to some external influences	4-6
Low (remote)	Has not occurred and is unlikely to occur	0-3

Impact (financial loss per occurrence)	For the Company	For the fund / project	Rating
Low			0-3
Moderate			4-6
High			7-9

Detection	Ratings
Cannot detect or detection with very low probability	9
Remote or low chance of detection	6-8
Moderate detection probability	3-5
Almost certain detection	0-2

III. RISK MITIGATION

On completion of risk assessment, key risks that matter to the Company will be documented in the risk register along with the mitigation plan and ownership by the Custodian. Currently Company has documented the key risk events across the investment life cycle. Refer Appendix A for risk register. While risks cannot be eliminated, having a good risk mitigation strategy can:

a. Reduce risks, by having good periodic internal controls and continuous monitoring.
b. Mitigate risks, by adhering to the investment policy of the Fund
c. Help retain investments to avoid higher cost of trying to reduce risk.
d. Share risks, by following a middle path between retaining, monitoring and mitigating risk.

IV. RISK MONITORING

The Risk Management Committee will collect and collate evidence of effectiveness of mitigation plan, for risks that matter from the operations and other teams and report to the Risk Management Committee for its review on a quarterly basis. Periodic reporting on risks is required to determine whether the impact or likelihood of the risk is increasing or decreasing and to ensure continuing alignment of organizational resources to priorities. The reporting of key risks and risk handling measures is necessary to:

- Improve the quality of and support timely decision making.
- Determine priorities for action and improvement.
- Enable the Board and Risk Management Committee to satisfy themselves that the key risks are being identified and managed to an acceptable level

Risk reporting may include:

- Risk Appetite Profile: monitor the performance of the risk appetite matrix against board approved limits
- Top and Emerging Risk Profile: provide forward looking analysis of risk themes such as internal and external circumstances or events which are beyond the organisations control.

7. INTERNAL CONTROLS

Other than loans and advances that may be granted to Directors who are working as whole-time employee of the Company and at par with other employees as per the Company's human resource policy / rules, no other loan/credit facility shall be extended to the Directors of the Company and their relatives

8. REVIEW

The policy will be the guiding document for risk management in the Company and will be reviewed as and when required due to the changes in the risk management regulations/ standards/ best practices as appropriate. In any case, the policy will be regularly reviewed annually.

ANNEXURE A

I. RISK REGISTER

Register for Risk that emerges at each stage of project (Need update on the control effectiveness categorisation). Based on the control effectiveness categorisation, RPN can be applied to arrive at the residual risk

Risks to Raising Funds

S. No.	Risk	Enterprise / Fund	Likelihood	Impact	Risk Response
1.	Compliance risk: Withdrawal of SEBI License	Enterprise	Low	High	SEBI closely monitors compliance with the regulatory framework. To ensure quality compliance, all operating functions of our Company like Investor services, Fund Accounting, Financial Accounting, Legal & Secretarial and Fund Audit have been outsourced to reputed parties. The company Secretary as the compliance officer will co-ordinate with such agencies and ensure compliance. The Internal Controls for Compliance have been designed and manualized to address this risk in conjunction with the outsourced vendors
2.	Environmental risk - Economic Downturn	Enterprise	Moderate	High	The risk of Economic downturn affecting our portfolio undertakings will be addressed by judicious Asset-Liability Management initially and in the long term by diversification across multiple dimensions in our portfolio.

S. No.	Risk	Enterprise / Fund	Likelihood	Impact	Risk Response
3.	Governance risk and Reputation risk - Credibility of Pipeline	Enterprise	Low	Moderate	Our Pipeline tracking mechanisms should be subject to strict quality control and compliance to the internal controls specified in the Investment manual to retain only qualified prospects in the pipeline.
4	Credit risk - Draw Down Defaults	Fund	Low	High	Sourcing more from large institutional investors subject to AIF regulations
5	Investment risk - Sector Risk	Fund	Moderate	High	; While the risk is accepted, would be offset by robust appraisals of individual projects and startups the funds are investing into
6	Strategic risk-Key personnel attrition	Enterprise	Moderate	High	The creation of a modern "flat" organization and an informal and participative work environment and financial alignment of interests of personnel & Company will reduce scope for attrition. A well-considered Succession plan that creates a good "bench-strength" would all be used to mitigate this risk.
7	Strategic risk-Event risk	Both	Moderate	High	Impact of political and regulatory changes would remain significant unknown for the investor. To some extent event risk is mitigated in Kerala by institutional mechanisms like the KIIFB, the sponsor, which carries out the conception and implementation of

S. No.	Risk	Enterprise / Fund	Likelihood	Impact	Risk Response
					infrastructure projects across the SPVs sponsored by government departments and PSUs. Secondly, given the critical nature of this sector, successive Governments have demonstrably maintained continuity. Thirdly, incremental costs in PPP and Government sponsored projects tend to get absorbed by the budget and not passed on to the investors. Our contracts with portfolio undertakings shall try to use this as a mitigation route. A major KIFML specific mitigant, is to ensure diversified ownership.

Deploying Funds / Project Selection

S No	Risk	Enterprise / Fund	Likelihood	Impact	Mitigation
1.	Investment risk: DPR validity	Fund	High to Moderate	High	While DPRs in the past have a certain amateurish quality, since 2016 (setting up of KIIFB and a Project Preparation Fund) this has seen a significant improvement. Mitigation shall include rigorous filtration of deals; challenge & authentication of all material assumptions; 3rd party valuations if required
2.	Governance risk - Inadequate information	Enterprise	Moderate	High	Adequate monitoring & information dissemination system

S No	Risk	Enterprise / Fund	Likelihood	Impact	Mitigation
					will be developed to ensure adequate flow of information
3.	Governance and reputation risk - Appraisal Expertise	Enterprise	Low	High	To hire the best of breed and pay as per market to obtain and retain best talent; compensation aligned to the Company's objectives
4.	Operational risk- Midstream Changes	Fund	Moderate	High	To build mitigation into contracts including exit; Force majeure clauses
5.	Market risk - Valuation risk	Fund	Moderate	Moderate	Given the nature of asset-class, creating accurate (realizable) valuation may be difficult. The deal team will have competent valuers and also can engage reputed 3rd party agencies on a case-to-case basis for the valuation. This will drive the investment-mix. Ill-liquidity discounting will be part of the process. Independence of the deal team and Investment Committee is the most important mitigant. In an innovation fund context, valuation risk can be mitigated by taking strategic exits at suitable opportunities.
6.	Investment risks -Risks of Investments in Unlisted, Illiquid undertakings,	Fund	Moderate	High	Adequate level of diligence and monitoring of assets will be done to ensure that the realization of investments will be sufficiently in advance of the term of the Fund, or intended date of distribution of

S No	Risk	Enterprise / Fund	Likelihood	Impact	Mitigation
	Long-Gestation Projects and, Greenfields				assets, return of assets or redemption of any capital to investors. The intended investment period will be during the upfront stage of the Fund's life while the subsequent years would be devoted to preparing for exits. Further, as a policy, all debt instruments that are invested will only have a term that is co-terminus with the life of the Fund. Upfront care would be taken to assess the refinancing risk of the project SPV if the payback period for the project is longer than the fund duration The fund manager will endeavour to build a robust exit clause in the contract using such devises as listing, creation of a sinking fund, buy-back clauses and permission to divest to secondary buyers. From an innovation fund perspective, fund manager will proactively identify suitable secondary stake sale opportunities regularly so that liquidity challenge is mitigated

Project Execution

S. No	Risk	Enterprise / Fund	Likelihood	Impact	Mitigation
1	Operational risks- Time overrun	Both	High	High	The evaluation of the DPR will include understanding the Critical Path and its known vulnerabilities. No project would be funded where the investee

S. No	Risk	Enterprise / Fund	Likelihood	Impact	Mitigation
					company is not in possession of the land and all necessary statutory clearances. The RM team once formed will be responsible for concurrent monitoring of milestones and its approach shall include obtaining/building expertise on project tracking, creating monitoring dashboards. One of the objectives of creating a "dual discipline" team is to mitigate this risk.
2.	Operational risk- Cost Overrun	Both	High	High	Financial Close of projects after addressing all known vulnerabilities and recourse to Sensitivity Analysis and simulation to assess tolerance at various possible scenarios. As above, the early warning and ability to intervene are crucial risk mitigants.
3.	Operational risk - Project Complexity risk	Fund	Moderate	Moderate	Most infrastructure projects tend to be complex and require careful appraisals, but are prone to execution gaps leading to risk exposure. Robust SPV design and concurrent PMO led monitoring to address this risk
4.	Operational risk - Project Reporting Risks	Fund	High	Low	All project reports to be vetted by the monitoring team for proactive action to address vulnerabilities. Use of third party PMO with strict reporting mandates.
5	Governance risk - Risks Associated with Non-Controlling Interests	Enterprise	High	Low	The Fund expects to have Board representation and also ensure that its interests are aligned with the other shareholders and promoters. The fund will ordinarily not invest below 5% of the equity ownership of the

S. No	Risk	Enterprise / Fund	Likelihood	Impact	Mitigation
					undertaking and the average holding will usually allow it to participate in the Board. Please refer to Investment Manual.
6	Governance risk-Counterparty risk	Enterprise	High	High	The change in operating environment on account of policy change or non-implementation or change in rules and regulations mid-stream is a vulnerability in the sector. However, In the case of the Kerala Infrastructure Fund, this is mitigated by the fact that the counterparty in most cases for the asset would be the SPVs promoted by the Government of Kerala or an almost oligopoly if not monopoly in servicing the consumer base. Whilst the default risk is typically quite remote given the often-high credit quality of the typical counterparty, the counterparty (credit) exposure does exist. The fund would seek additional mitigating mechanisms like judicious use of Force Majeure and collateral measures like gap funding commitments and escrow accounts which are specified in the Investment Manual in detail.
7	Governance risk-Reliance on Portfolio Undertaking Management	Enterprise	Moderate	Moderate	The Fund will have adequate representation on the Board and Management Committees of the portfolio companies in order to ensure that their performance is monitored very closely. Further, the Investment Agreement will ensure that the Fund will not be excluded from key decisions

S. No	Risk	Enterprise / Fund	Likelihood	Impact	Mitigation
8	Governance risk-Board participation risk	Enterprise	Moderate	Moderate	The Investment Agreements and the terms of compensation of the Investment Manager will consider such risks and provide for their impact during the process of evaluating and executing the investment documents. In general, the Fund will have to indemnify the Investment Manager from such claims.

Exit Strategy

S. No.	Risk	Enterprise / Fund	Likelihood	Impact	Mitigation
1.	Exit risks-Changes in operating, financial or regulatory environment before exit. Loss of exit opportunities	Fund	Moderate	High	The investment policy manual would have strong process safeguards to address this risk including but not limited to addressing such investments which have a defined exit, considering options for phased exit and by managing to write floors for investments. The strategy is to monitor continually and look for opportunistic exits. Risk mitigant is to create "fallback" exit opportunities prior to investment. From the infrastructure fund perspective, fund manager will periodically monitor the refinancing capability of the project so that exit opportunities are evaluated continuously For the innovation fund, a milestone-based approach could be employed to monitor the growth of start-ups

S. No.	Risk	Enterprise / Fund	Likelihood	Impact	Mitigation
					invested. Concurrent to achieving these milestones, partial stake sale could be evaluated .
3.	Environmental risk and exit risk - Economic risk	Both	Moderate	High	Commonly, India has a large growing appetite for critical infrastructure, and it is on a trajectory of high growth rates. Also, Kerala has witnessed secular growth in investments, economic development. The ability of consumers to spend on essential utilities and pay-for-use of infrastructure is likely to increase in an aspirational economy. As most private infrastructure investors have started allocating to the asset class in recent years, they have directly or indirectly deployed most of their capital in periods of high valuations while they are lacking exposure to the years where discount rates were at much more attractive levels. Infrastructure sector is relatively inelastic to downturns in economic cycle, but the downturn may affect the valuations rather than the cash flow. The mitigating measures used in the case of other exit risks like phased exits and negotiated floor values would also be helpful, and the detailed mitigation through internal controls is part of the investment manual. From an innovation fund perspective, valuations fluctuate a lot during economic cycles. The mitigation factor would be to spread the investments over a period of time and seek

S. No.	Risk	Enterprise / Fund	Likelihood	Impact	Mitigation
					phased exits via secondary sale /IPO's from invested start-ups
3	Exit risk-Liquidity Risk	Fund	Low	Low	The tenor of any debt instrument will be co-terminus with the Fund's life. hence, the repayment of such investments is aligned with the Fund's life. From an innovation fund perspective, this will be mitigated by continuously exploring secondary sale opportunities in invested start-ups on achieving major valuation jumps Regarding equity investments as well as periodic distributions of realized investments, the Board of Directors will ensure that the Fund is sufficiently diversified with regard to the lifecycle of the investment in order to service investors in accordance with their expectation and to re-invest earnings based on the investment horizon of the investors. Please see investment manual for details.

End of document