Serial No.	CHAPTER 6 : CREDIT RISK MEASUREMENT AND MANAGEMENT	ICAI Study Material Page No.	Extra Reference In ICAI Material	Past Paper /Mock Paper (Book 1)	Book 2
1	UNDERSTANDING CREDIT RISK	6.1			
1.1	Two Way Risk	6.2			
1.2	Risk – Return Trade Off	6.2			
	Credit Risk calls (4 decisions)	6.2			
1.3	Credit Risk in Capital Market (retail and wholesale)	6.2			
2	COMPONENTS OF CREDIT RISK	6.2			
	(i) Default Risk	6.2			
	(ii) Exposure Risk	6.3			
	(iii) Recovery Risk	6.3			
	(a) Collateral Risk	6.3			
	(b) Third Party Guarantee Risk	6.3			
3	MEASUREMENT OF CREDIT RISK IN BANKING TRANSACTIONS AND	6.3			
	FACTORS AFFECTING THE CREDIT RISK				
3.1	Measurement of Credit Risk in Banking Transactions (formula)	6.3			
3.2	Factors Affecting the Credit Risk	6.4			
	(i) Internal Factors (ii) External Factors	6.4			
4	TYPES OF CREDIT FACILITIES	6.4			
	(a) Retail Financing (b) Wholesale Financing	6.4			
4.1	Fund Based Facilities	6.5			
	(a) Personal Loan	6.5			
	(b) Mortgage loan / Home Loan	6.5			
	(c) Working Capital loans	6.5			
	Maximum Permissible Banking finance (MPBF)	6.5			
	Tandon Committee	6.5			
	3 Method	6.5			
	Various types of working capital loans include	6.5			
	(i) Overdraft	6.5			
	(ii) Cash Credit	6.6			
	(iii) Bill Discounting- Bills purchased / discounted facility	6.6			
	(iv) Packing Credit	6.6			
	Pre-shipment and post shipment	6.6			
	(v) Factoring	6.6			

Serial No.	CHAPTER 6 : CREDIT RISK MEASUREMENT AND MANAGEMENT	ICAI Study Material Page No.	Extra Reference In ICAI Material	Past Paper /Mock Paper (Book 1)	Book 2
	(d) Demand Loan	6.6			
	(e) Term Loans	6.6			
	(f) Project / Infrastructure Loans	6.6			
	(g) Micro finance loans	6.7			
	(h) Real Estate Construction Loans	6.7			
	(i) Agriculture and Allied Services Loans	6.7			
4.2	Non Fund Facilities	6.7			
	(a) Bank Guarantee	6.7			
	(b) Letter of Credit	6.7			
5	CLASSIFICATION OF ASSETS	6.7			
	Standard Assets Sub Doubtful assets Loss Assets	6.8			
6	EVALUATING CREDIT RISK	6.8			
	(1) Understand the reality	6.8			
	(2) Check the credibility	6.8			
	(3) Ask and Check the references	6.9			
	(4) Due Diligence	6.9			
	(5) Recovery	6.9			
	(6) Nature of business	6.9			
7	MITIGATING CREDIT RISK	6.9			
7.1	Identification of Credit Risks (Historical and traditional)	6.9			
7.2	How Credit risk is Mitigated	6.10			
	different types of funded credit risk mitigation methods	6.10			
	(a) On Balance Sheet Netting	6.10			
	(b) Collateral (typical example)	6.10			
	credit protection is only "eligible"	6.11			
	Method of calculating credit charge of credit risk under Basel II	6.11			
	Standardize approach	6.11			
	Internal rating based approach	6.11			
	Credit risk mitigation	6.11			
	Other techniques or methods of credit risk mitigation	6.12			
	(a) Risk-based pricing	6.12			
	(b) Credit insurance	6.12			

Serial No.	CHAPTER 6 : CREDIT RISK MEASUREMENT AND MANAGEMENT	ICAI Study Material Page No.	Extra Reference In ICAI Material	Past Paper /Mock Paper (Book 1)	Book 2
	(c) Tightening	6.12			
	(d) Diversification	6.12			
	(e) Covenants	6.12			
8	QUALITATIVE TECHNIQUES OF CREDIT RISK MANAGEMENT	6.12			
	Transaction risk management	6.12			
	Portfolio risk management	6.12			
	Policies/processes (credit risk governance)	6.12			
8.1	Borrower / Transaction specific risk management	6.13			
	five C's of Credit viz; Capacity, Capital, Character, Collateral and Conditions.	6.13			
8.1.1	Credit Due Diligence for Retail Financing	6.14	6.4, 6.17		
8.1.2	Credit Due Diligence for Wholesale Financing	6.14			
	wholesale credits, the detailed appraisal would inter alia cover	6.14			
8.2	Credit Rating Scales	6.15			
	Few leading credit rating agencies	6.15			
	Rating Scale for Long term instruments is as follows	6.16			
	AAA (Highest Safety), AA (High Safety), A (Adequate Safety), BBB (Moderate	6.16			
	Safety), BB (Moderate Risk), B (High Risk), C (Very High Risk), D (Default)				
	A1, A2, A3, A4, D (Table)	6.16			
8.3	Portfolio Risk Management	6.17			
	Retail Financing,	6.17			
	Wholesale Financing	6.17			
	Special Mention Account classification (SMA accounts)	6.18			
	SMA – 0, SMA-1, SMA-2 (Table)	6.18			
	"Concentration Risk Management"	6.18			
8.4	Credit Risk Rating Process	6.18			
	Probability of Default (PD), Loss Given Default (LGD)	6.18			
8.5	Credit Loss Estimation	6.19			
	Expected Loss Unexpected Loss	6.19			
	3 integral components (known as risk components)	6.19			
	I. Probability of Default (PD)	6.19			
	II. Loss Given Default (LGD)	6.19			
	III. Exposure at Default (EAD)	6.20			

Serial No.	CHAPTER 6 : CREDIT RISK MEASUREMENT AND MANAGEMENT	ICAI Study Material Page No.	Extra Reference In ICAI Material	Past Paper /Mock Paper (Book 1)	Book 2
	*Default definition as per Bank for International Settlement (BIS)	6.20			
8.5.1	Estimation of Probability of Default (PD)	6.20			
	Types of PD Estimation	6.20			
	1. Pooling Method	6.20			
	2. Statistical Method (logistic regression)	6.20			
	3. Structural Method (applicable for listed corporate)	6.20			
8.5.2	Estimation of Loss Given Default	6.21			
	Value of LGD varies with the economic cycle	6.21			
	Cyclical LGD (Point-in-Time LGD)	6.21			
	Long-run LGD (Through-the-Cycle LGD)	6.21			
	Downturn LGD	6.21			
8.6	Credit Default Swaps	6.21			
	"naked" CDSs	6.21 (2nd			
		para in			
		section 8.6)			
	two kinds of settlement (Physical settlement and cash settlement)	6.22			
	Key features of RBI guidelines on CDS	6.22			
8.7	Credit Insurance	6.24			
8.8	Difference between Credit Insurance and Credit Default Swaps	6.24			
8.9	Other Qualitative Techniques of Credit Risk Management	6.25			
8.9.1	Stipulation of Covenants	6.25			
8.9.2	Collateral / Security	6.25			
	Various types of securities depending upon the nature of facilities	6.25			
8.9.3	Structuring of the transaction	6.25			
	examples of good structuring	6.25			
8.9.4	Sell Down / syndication / Co- participating / Securitization	6.26			
9	QUANTITATIVE TECHNIQUES OF CREDIT RISK MANAGEMENT	6.26			
9.1	Altman Z Score	6.26			
	Z-score formula	6.27			
	the Merton Model)	6.27			
	privately held companies (the Altman Z'-Score) and non- manufacturing companies (the Altman Z"-Score)	6.27			

Serial No.	CHAPTER 6 : CREDIT RISK MEASUREMENT AND MANAGEMENT	ICAI Study Material Page No.	Extra Reference In ICAI Material	Past Paper /Mock Paper (Book 1)	Book 2
9.2	Risk Adjusted Returns / Capital	6.28			
	Alpha, Beta, Sharpe Ratio, R Squared,	6.28			
9.2.1	Return on Risk Adjusted Capital (RORAC)	6.29	6.30		
9.2.2	Economic Capital	6.29			
9.2.3	Value at Risk (VaR)	6.30			
9.2.4	Risk – adjusted Return on Capital (RAROC)	6.30	6.29		
	RAROC system allocates capital for two basic reasons	6.30			
9.3	Ratios and Financial Assessment	6.31			
9.3.1	Financial Statement analysis	6.31			
9.3.2	Cash Flow analysis	6.32			
	(a) Operating Cash flow	6.32			
	(b) Investment cash flow	6.32			
	(c) Financing cash flow	6.32			
9.3.3	Working capital analysis	6.32			
	(a) Account receivable days (formula)	6.32			
	(b) Inventory days (formula)	6.33			
	(c) Payable days (formula)	6.33			
	(d) Current Ratio and Quick ratio (formula)	6.33			
10	CREDIT SCORING MODELS	6.33			
10.1	What is a Credit Scoring Model?	6.33			
	usage of credit models	6.34			
10.2	Types of Credit Scoring Model	6.34			
	FICO Score	6.34			
	Vantage Score	6.35			
	PLUS Score	6.35			
	Experian National Equivalency Score (ENES), (also called FAKO), FICO	6.36			
	Equifax	6.36			
	The advantages of Equifax	6.36			