



CIRCULAR

CIR/IMD/DF/03/2015

April 30, 2015

**All Mutual Funds/Asset Management Companies (AMCs)/
Trustee Companies/Boards of Trustees of Mutual Funds**

Sir/ Madam,

Subject: Stress Testing of Liquid Fund and Money Market Mutual Fund Schemes

1. Risk Management framework has been prescribed by SEBI vide circular dated September 30, 2002. As a part of risk management framework, Mutual Funds (MFs) carry out stress testing of their portfolio, particularly for debt schemes. In order to standardize this practice across industry, AMFI came out with Best Practice Guidelines dated September 12, 2014 on stress testing of Liquid Funds and Money Market Mutual Fund Schemes (MMMMFs).
2. In order to further strengthen the risk management practices and to develop a sound framework that would evaluate potential vulnerabilities on account of plausible events and provide early warning on the health of the underlying portfolio of Liquid Fund and MMMF Schemes, it has been decided to stipulate the following guidelines:
 - a. As a part of the extant risk management framework, AMCs should have stress testing policy in place which mandates them to conduct stress test on all Liquid Fund and MMMF Schemes.
 - b. The stress test should be carried out internally at least on a monthly basis, and if the market conditions require so, AMC should conduct more frequent stress test.
 - c. The concerned schemes shall be tested on the following risk parameters, among others deemed necessary by the AMC:
 - i. Interest rate risk
 - ii. Credit risk
 - iii. Liquidity & Redemption risk
 - d. While conducting stress test, it will be required to evaluate impact of the various risk parameters on the scheme and its Net Asset Value (NAV). The parameters used and the methodology adopted for conducting stress test on such type of scheme, should be detailed in the stress testing policy, which is required to be approved by the Board of AMC.



- e. Further, in the event of stress test revealing any vulnerability or early warning signal, it would be required to bring it to the notice of the Trustees and take corrective action as deemed necessary, to reinforce their robustness. Each AMC should also be required to have documented guidelines, to deal with the adverse situation effectively.
- f. Such stress-testing policy shall be reviewed by the Board of AMC and Trustees, at least on an annual basis, in light of the evolving market scenarios and should cover the following aspects:
 - i. Adequacy of the documentation for various elements of the stress testing framework
 - ii. Scope of coverage of the stress testing policy and the levels of stress applied
 - iii. Integration of the stress testing framework in the day-to-day risk management processes
 - iv. Adequacy of the corrective actions and the efficacy of the systems for their activation
- g. Further, Trustees shall be required to report compliance with this circular and steps taken to deal with adverse situations faced, if any, in the Half Yearly Trustee Report submitted to SEBI.

This circular shall be applicable with immediate effect.

This circular is issued in exercise of the powers conferred under Section 11 (1) of the Securities and Exchange Board of India Act, 1992, read with the provision of Regulation 77 of SEBI (Mutual Funds) Regulations, 1996 to protect the interests of investors in securities and to promote the development of, and to regulate the securities market.

Yours faithfully,

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