GUJARAT STATE FINANCIAL SERVICES LTD.

(CIN: U65910GJ1992SGC018602)

ASSET- LIABILITY MANAGEMENT POLICY

Background

GSFS was established to ease and facilitate financial resources to the state-owned undertakings. To further this objective, the State Government has given mandate to the Company to manage the surplus funds of the state entities, and has issued directions from time to time to GoG entities for placing their funds with GSFS, in order to effectively implement the mandate. GSFS primarily provides these funds as loans to GoG entities only and hence acts as an in-house fund manager to the GoG entities. Thus, the idea of formation of GSFS is to manage funds of GoG entities which results into the circulation of funds within the State Government ambit. With respect to this mandate, it is prudent for GSFS to manage its assets and liabilities in a manner such that it is able to repay its obligations in a timely manner. This is also a statutory obligation as RBI, the regulating agency for NBFCs, has stipulated that NBFCs should have an effective Asset-Liability Management (ALM) system as part of their overall system for effective risk management.

Business Model of GSFS

GSFS has a unique business model in India which creates a win-win situation for GoG entities placing their funds with GSFS, GoG entities taking loans from GSFS and Government of Gujarat. The basic objective of the Company is to manage the surplus funds of GoG entities as per the mandate of State Government. The funds received are primarily provided as loans to other GoG entities at a lower rate as compared to banks/FIs. The business model of GSFS is a unique time-tested model in India which has been in operation since last more than two decades and continues to be so. Some of the salient features of the simple but highly effective business model are as under:

i. GSFS accepts funds from GoG entities as per the mandate of Government of Gujarat, at interest rates which are higher than banks.

ii. The funds received by GSFS from GoG entities are provided as loans to GoG entities on merit, at interest rates which are lower than Banks/FIs thereby lowering their borrowing costs.

iii. In the event of immediate unavailability of new avenue for loans and to maintain adequate liquidity, GSFS invests these funds in the Liquid/Debt Schemes of approved Mutual Funds and MIBOR linked ICDs with Primary Dealers (PDs) till such time it gets the opportunity to cater the loan requirement of any GoG entity.

iv. GSFS carries out all its functions through a small setup located at a single location with limited number of employees.

v. GSFS does not accept deposits from public nor does it provide any loan to individuals or any private Company. Hence, as the Company operates within the ambit of GoG entities only, its business model does not transmit any risks to the financial market.

The major assets and liabilities of GSFS consist of the following:

A. Liabilities – Deposits in the form of Inter Corporate Deposits (ICDs) received from GoG entities with tenors ranging from 15 days to 3 years and Liquid Deposit Scheme (LDS) received from GoG entities having tenor less than 15 days.

B. Assets – Deployment of funds as Loans to GoG entities and Money Market Investments.

Objective and Scope

The objective of this policy is to create an institutional mechanism to monitor the maturity pattern of the various liabilities and assets of the company from time to time to:

(a) Ascertain the nature and extent of mismatch, if any, in different maturity buckets, especially the 1-30/31days bucket, which would indicate the structural liquidity.

(b) The extent and nature of cumulative mismatch, if any, in different buckets indicative of short term dynamic liquidity.

An efficient ALM in context of GSFS needs (a) a good information system (b) a Committee of Senior functionaries for ensuring that ALM is carried out within the framework of State Government mandate and the norms approved by the Board of Directors and (c) a well defined process.

Asset - Liability Management Committee (ALCO)

Asset- Liability Management will be overseen by a Committee consisting of the following officials:

Managing Director – Chairman of the Committee

Nominee Director – Member

Independent Director – Member

Quorum: Any two of the above committee members will constitute the quorum.

ALM Support Group: consisting of senior officials who will be analyzing and monitoring liquidity position of the company and in case of any adverse situation, will report to ALCO.

Process:

ALCO will review various MIS reports submitted to it. Further, Reserve Bank of India has stipulated templates for reporting Dynamic Liquidity (DNBS04A), Structural liquidity (DNBS04B), and Interest Rate Sensitivity (DNBS04B). If required, ALCO will also use these templates for reviewing the liquidity and interest rate risk.

Periodicity of Meeting:

The ALCO will meet as and when needed depending upon the requirement but atleast once in a financial year. The agenda covering the following areas will be deliberated by ALCO namely:

- Position of Liabilities in terms of ICD and LDS received by GSFS
- Position of Assets in terms of deployment of funds as loans and investments
- Liquidity risk management

Minutes of the ALCO meeting will be prepared and preserved

Liquidity Risk Management

Measuring and managing liquidity needs are vital for effective operation of company. The importance of liquidity transcends individual institutions, as liquidity shortfall in one institution can have repercussions on the entire system. The ALM Support Group will be analyzing and monitoring liquidity position of the company and in case of any adverse situation, will report to ALCO.

By virtue of the unique business model of GSFS, the supply of funds from GoG entities in the form of ICD and LDS is unanticipated as well as unregulated but continuous in nature (fresh as well as renewals) on account of budgetary allocations from State Government to GoG entities on year to year basis. Moreover, the emphasis of GSFS is to primarily provide loans to GoG entities on merit.

As a matter of fact, it has been the experience of the company that major portion of deposits placed with the company are renewed on maturity by GoG entities as per the trend of deposits placed by GoG entities. For measuring and managing liquidity requirements, ALCO will take into consideration the MIS reports of the company submitted to it considering the tenor buckets of GSFS. ALCO may also take a reference to the templates DNBS04A and DNBS04B of RBI and will use the tenor buckets suggested by RBI (shown below) for measuring the liquidity.

i) 1 day to 7 days
ii) 8 days to 14 days
iii) 15 days to 30/31 days (One month)
iv) Over one month and upto 2 months
v) Over two months and upto 3 months
vi) Over 3 months and upto 6 months
vii) Over 6 months and upto 1 year
viii) Over 1 year and upto 3 years
ix) Over 3 years and upto 5 years
x) Over 5 years

Based on its business model, GSFS has segregated the 1-30 days time bucket in the RBI's Statement of Structural Liquidity into granular buckets of 1-7 days, 8-14 days and 15-30 days for measuring liquidity. The company shall strive that the net cumulative negative mismatches in the Statement of Structural Liquidity in the maturity buckets 1-7 days, 8-14 days and 15-30 days shall not exceed 10%, 10% and 20% respectively. The cumulative net cash outflows across all other time buckets upto 1 year shall not exceed 30%.

It is worthwhile to mention that although there may be a mismatch in the asset to liability schedule in some of the tenor buckets of the said templates, the company can use on hand balance, its investments in open-ended liquid/debt schemes of AMCs or can also utilise likely fresh inflow of ICDs to repay its obligations across tenors in a timely manner.

In the backdrop of these facts, ALM Support Group will evaluate the ability of GSFS to meet its maturing liabilities as they become due. In case of any adverse situation arising, ALM Support Group will report to ALCO to review this position and ALCO will take appropriate action, if required.

Interest Rate Risk

Interest rate risk is the risk where changes in market interest rates might adversely or favorably affect an NBFC's financial condition. The immediate impact of changes in interest rates is on company’s earnings.

The liabilities of GSFS majorly constitute of funds received under ICD and LDS from Government of Gujarat entities. Assets constitute of loans provided to other Government of Gujarat entities and funds invested in the Liquid/Debt Schemes of approved Mutual Funds and MIBOR linked ICDs with Primary Dealers (PDs).

The interest rate on the ICD, LDS and loans are decided by the Finance Committee from time to time. The interest rate revision of ICDs is applicable on renewals / fresh placement of ICDs while in case of LDS, such revision is applicable on entire LDS funds from the date of revision itself. The interest rate on loans are kept floating in nature and its revision is also applicable from the date of revision. Hence, after the interest rate revision by Finance Committee is put into effect, the loan asset and LDS liability gets repriced immediately while the repricing of ICD liabilities happens over a period of time.

The funds deployed in the Liquid/Debt Schemes of approved Mutual Funds constitute usually more than 50% of the total asset size of the company. The returns from Liquid/Debt schemes are primarily based on interest rate movement in the financial market which are dependent on various parameters such as liquidity position in the financial market, fiscal and monetary policies of Government and RBI and various other economic and geo-political factors, domestic as well as global, and hence are varying in nature.

ALCO will take into consideration the MIS reports of the company submitted to it considering the tenor buckets of GSFS for ascertaining the Gap in individual buckets and the cumulative Gap of the interest sensitive assets and liabilities. ALCO may also take a reference to the Reporting Format DNBS04B of RBI for ascertaining the Gap in individual buckets and the cumulative Gap as per the following buckets.

i) 1 day to 7 days
ii) 8 days to 14 days
iii) 15 days -30/31 days (One month)
iv) Over one month to 2 months
v) Over two months to 3 months
vi) Over 3 months to 6 months
vii) Over 6 months to 1 year
viii) Over 1 year to 3 years
ix) Over 3 years to 5 years
x) Over 5 years
xi) Non-sensitive

In order to meet with the situation of a negative mismatch in certain tenor buckets of the said format of RBI, the Company shall maintain adequate investments in open-ended liquid/debt schemes of AMCs or even use fresh inflow of ICDs to be able to turn it into a positive gap. However, the ALM Support Group will be analyzing and monitoring interest rate movement and in case of any adverse situation, ALM Support Group will report to ALCO to review this position and ALCO will take appropriate action, if required.