GUJARAT STATE FINANCIAL SERVICES LTD.

CREDIT & INVESTMENT POLICY

Finance Department
Govt. of Gujarat
Sachivalaya, Gandhina

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INTRODUCTION

Gujarat State Financial Services Ltd. (GSFS) is a Government of Gujarat (GoG) undertaking, registered under the Companies Act, and is registered with RBI as a NBFC (Non-Banking Finance Company). Since GSFS does not accept funds from the public, and its asset size is more than Rs.1000 crore, it falls under the (Middle Layer) category of ND-SI (Non Deposit Taking Systemically Important) NBFC. It has been given a mandate by the State Government to manage the funds available with GoG undertakings, offices, entities etc.

The funds received by GSFS from State Government entities are provided to the other state-owned/controlled undertakings, which are in need of funds, at a competitive interest rate as compared to the interest rates provided by banks and financial institutions. This reduces the borrowing of these entities from banks and financial institutions at higher interest rates and provides operational ease to them.

In short, the idea behind formation of GSFS is to manage in-house funds of state-owned/controlled undertakings. This results into the circulation of funds of government entities within the ambit of State Government and its undertakings. Therefore, on one hand, the state-owned/controlled entities earn steady interest on their funds by placing it with GSFS and, on the other hand, these funds are made available to other GoG undertakings at a competitive interest rate.

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BACKGROUND

GSFS was established in November 1992 and started commercial operations in 1993. The company was established to ease and facilitate financial resources to the state-owned/controlled undertakings. To further this objective, the State Government gave a mandate to the company to manage the surplus funds of the state entities, and has issued directions from time to time for effective implementation of the mandate.

State Government departments implement various schemes, programs and projects of the State and Central Government through Government entities (Public Sector Undertakings, Societies and such other vehicles). These entities work as agents of Government and are provided grants for implementing the schemes or projects or procuring goods or services.

Government funds are 'public funds' provisioned to deliver public services and are, therefore, required to be managed in a prudent, risk-free manner. Government has mandated that its entities shall deposit their surplus funds with GSFS till such time as the funds are required by them.

Over a period of time, it was felt that the funds received from state entities be made available to the other state undertakings to meet their financial requirements. This would provide an impetus to state undertakings, reduce their borrowing cost, and would give them better bargaining position when they have to approach Commercial Banks/DFIs for finance.

As a result of the above, the evolution of GSFS's business model took place over a period of time. This has now become a unique and time tested model which other states can emulate.

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NEED FOR A CREDIT & INVESTMENT POLICY

GSFS primarily lends funds received from GoG entities to other GoG undertakings at competitive rates. It also regularly invests in Gujarat State Government Securities (GSGS) to derive advantage of its Sovereign nature, stable interest and zero risk weightage while calculating Capital to Risk-Weighted Assets Ratio (CRAR). As a part of daily funds management exercise and till the availability of new avenues for loans, while maintaining liquidity, GSFS deploys these funds in the Liquid/Debt Schemes of approved Asset Management Companies and MIBOR linked ICDs with Primary Dealers.

Earlier, the business activities of GSFS were carried out within the Credit & Investment norms defined by its Board of Directors. The said norms were last updated during the 98th Board meeting of GSFS held in 2012.

Although GSFS primarily deals with management of its financial resources within the ambit of state entities only, its business activities may still be exposed to certain risks which are inherent to institutions involved in lending and investment activities. The likelihood of such an event, and its consequential impact on depositors, was discussed during a meeting taken by Hon'ble Chief Minister in June 2019 to review the functioning of GSFS. It was desired to devise a Credit and Investment Policy, with specific guidelines, to protect the interest of all the stake holders and to foster financial discipline in the entire process.

Keeping this into consideration, the Credit & Investment Policy was devised to govern the business operations of GSFS and sent for the approval of the State Government. The Credit & Investment Policy was approved by the State Government on 8th October 2020. Presently, GSFS carries out its business

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activities as per the Credit & Investment Policy of the company approved by the State Government.

Looking at the ever evolving business and regulatory requirements, a review of the Credit & Investment Policy of the company was required. In this regard, the Credit & Investment Policy of GSFS has been reviewed and necessary changes/modifications wherever required have been incorporated in this Policy.

CREDIT POLICY

It is the basic objective of GSFS to provide finance to Government of Gujarat (GoG) undertakings. This is generally provided on merit of each case and at a lower rate as compared to banks and financial institutions.

Types of Loans

1. **Short Term/Long Term Loans**

   The loans for less than one year are termed as Short Term Loans, while the loans for one year and above are termed as Long Term Loans. These loans are repayable by way of either bullet repayment or in installments. A moratorium period is provided on loans as per the request of the loanee to suit their repayment schedule.

2. **Line of Credit (LoC) Facility**

   LoC limit is sanctioned for a specific period within which the loanee can draw and repay the funds several times within the sanctioned limit of LoC. Under this facility, interest is charged only on the amount availed and for the period it is availed.

3. **Loan against ICD Facility**

   Loan against ICD is a type of finance facility provided to the depositor entity against the ICDs placed by it with GSFS. Under this facility, the depositor entity can avail loan on ICD which is repayable during its tenure or on its maturity.

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Eligible Entities

The company shall provide loans or credit only to the entities falling under atleast ONE of the below conditions:

i) A listed/unlisted Government of Gujarat (GoG) undertaking wherein the audit is carried out by CAG and whose name is mentioned in CAG report.

ii) Any listed/unlisted Public Sector Undertaking (PSU) or any entity, wherein the State Government as a shareholder has administrative control and it has a #sound financial position.

iii) Municipal Corporations of the state having #sound financial position.

* Administrative control shall mean the entities where Chairman or Managing Director or both are appointed by Government of Gujarat.

Sound financial position shall mean entities which are having regular operations and generating revenue OR revenue model OR Government support that enables the repayment of its loan obligations in time.

The eligible entities, as above, are further categorized as under:

a) Commercial and self-sustaining in nature
b) Entities availing 100% budgetary support from GoG
c) Entities which rely on both, i.e., budgetary as well as non budgetary resources.

In case of the category (c) above, GSFS may take necessary assurance from the borrowing entity that the loan sought from GSFS shall be utilized to fund its non budgetary requirements.

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Amount of Loan

The amount of loan shall be sanctioned keeping into consideration the requirement of loanee entity.

With respect to the single party/group exposure norms of Reserve Bank of India, GSFS has been given exemption by Reserve Bank of India from concentration of credit norms to the extent of exposure to the Government of Gujarat entities.

Interest on Loan

The rate of interest on loan shall be kept competitive as compared to banks and financial institutions and shall be floating in nature. The rate of interest shall be determined keeping in view GSFS's cost of borrowing, administrative and other expenditures, risk of interest rate volatility in future and nominal savings.

Tenure of Loan

The tenure of loan shall be considered for sanction on case to case basis, considering the requirement of loanee entity and liquidity position of GSFS. However, in any case, the loans provided by GSFS shall not be more than 15 years.

Purpose of loan

Loans shall be provided to the loanee entities for their financial requirement purposes requested by them in their request letter except for any purpose which is not permitted under law.

The company shall obtain End use certificates from loanee entities on quarterly basis post disbursement, to verify the end use of loans with the purpose for which the loan was availed.

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Other Features of Loan

The following shall be the policy of GSFS while sanctioning loans or line of credit:

1. GSFS shall not take any mortgage on assets/any collateral from the loanee against the sanctioned loan and hence shall not create any charge on the assets of loanee entity.
2. GSFS shall not take any processing fee for sanctioning of the loan.
3. GSFS shall not take any commitment charges for non-availing of any portion of the sanctioned loan.
4. In case of pre-payment by the loanee, GSFS shall not take any pre-payment charges.

Exclusions in case of credit

1. GSFS shall not provide loans for capital expenditure to newly formed/established companies with no operations and revenue undertaking new projects. Such companies can be provided loans for capital expenditure, only if they are wholly owned by GoG or its subsidiary company wholly owned by it and/or by GoG OR to an Eligible Entity for which a specific approval from GoG is taken for funding such capital expenditure from GSFS.

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INVESTMENT POLICY

Eligible Instruments

A. Long Term Instruments

i) Government of India Securities (G-Sec)

G-Secs are securities issued generally for a tenor ranging from 5 years to 10 years. These borrowings form the crux of the Central Government's borrowing program aimed at financing the shortfall in fiscal balances. Since these are sovereign issuances, they carry no risk and, hence, are also referred to as risk-free gilt-edged instruments.

G-Secs qualify as SLR instruments and carry a coupon rate which is paid half-yearly and are redeemed at maturity at par value. G-Secs issuances are managed by RBI, which, on behalf of the Centre, regularly conducts G-Sec auctions.

Commercial banks, Scheduled UCBs, Primary Dealers, Insurance Companies and Provident Funds, who maintain funds and securities account with RBI, are members of the electronic platform used for issuance of G-Secs.

ii) Gujarat State Government Securities (GSGS):

State Government Securities (SGS), earlier named as State Development Loans (SDLs), are issuances of the respective states in order to manage their

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Generally, as SGS have the backing and sovereign guarantee of the respective State Governments, depending on the fiscal health of the states and the consequent risk associated with such investments, SGS are traded at a spread above the benchmark G-Sec security. Investment in SGS is a good option for investors seeking to earn higher interest.

GSFS shall invest in SGS of Gujarat State only.

iii) Bonds of eligible entities

Bonds refer to securities issued by public/private sector corporates for a variety of business purposes. These securities are issued by Public Sector Enterprises, Public Sector Banks, All India Financial Institutions, Private Sector Companies, Municipal Bodies etc. for their business activities. The tenor of such securities is generally in the range of 1-15 years. However, the tenor may vary depending upon the funding requirement of the issuer. Bonds are not sovereign and are serviced by the entity issuing them.

Bonds are non-SLR instruments and are priced at a spread over the corresponding government security, depending on the level of perceived risk. Frequency of interest payments could be yearly/ half-yearly/ quarterly/ monthly, etc. Also, the face value of the security is specific to each issue.

GSFS shall invest in Bonds of entities eligible for credit.

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B. Short Term Instruments

i) Treasury Bills

Treasury Bills are money market instruments offered to finance short term debt obligation of the Government of India. These short term instruments aid in plugging in the short term liquidity mismatches of the Central Government. In simple words, it acts as the working capital of the Central Government.

Treasury Bills (T-Bills) are generally issued for a tenor of 91 days, 182 days and 364 days. These are discounted instruments i.e. they are issued at a discount to par value. On maturity, they are redeemed at par value, with the difference between the discounted rate (at the time of issuance) and maturity value being the return earned on such investments.

ii) MIBOR linked ICDs with Primary Dealers

Primary Dealers (PDs) are NBFCs registered with RBI. Their core activities comprise underwriting, bidding, market making and trading in Government Securities, Treasury Bills and other fixed income securities. PDs are governed by Prudential Norms for Primary Dealers issued by RBI. It also permits PDs to access its Subsidiary General Ledger Account (maintained only with RBI for Government Securities), Current Account facility, favored access to OMOs and other privileged access to facilitate participation of nonbank entities (like GSFS) and develop liquid market for Government Securities.

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An Inter Corporate Deposit (ICD) is an unsecured borrowing by one corporate entity from another corporate entity registered under the Companies Act. The corporate having surplus funds would lend to another corporate that is in need of funds. This lending would be on uncollateralized basis and, hence, a higher rate of interest is demanded by the lender. The tenor of ICD may range from 1 day to 1 year, but the most common tenor is for 90 days.

Primary Dealers are permitted to borrow in the ICD market. GSFS lends to PDs under ICDs which are linked with MIBOR (Mumbai Inter Bank Offer Rate). The lock-in period for these ICDs is of 7 days, while the tenor is generally up to 91 days.

GSFS shall invest only with approved Primary Dealers.

iii) Overnight & Liquid/Debt Schemes of Approved Asset Management Companies (Mutual Funds)

A mutual fund is a pool of money managed by a professional Fund Manager. It is a trust that collects money from a number of investors who share a common investment objective and invests the same in equities, bonds, money market instruments and/or other securities. The income / gains generated from this collective investment is distributed proportionately amongst the investors after deducting applicable expenses and levies, by calculating the scheme's 'Net Asset Value' or NAV. Simply put, the money pooled in by a large number of investors is what makes up a Mutual Fund.

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Just like an equity share which has a traded price, a mutual fund unit has Net Asset Value per Unit. The NAV is the combined market value of the shares, bonds and securities held by a Fund on any particular day (as reduced by permitted expenses and charges). NAV per Unit represents the market value of all the Units in a mutual fund scheme on a given day, net of all expenses and liabilities plus income accrued, divided by the outstanding number of Units in the scheme.

GSFS shall invest its surplus funds only in Overnight & Liquid/Debt Schemes of empanelled Asset Management Companies, considering various parameters like scheme size, scheme duration, interest rate movement, debt market condition, company's fund position, liquidity requirements etc. All the investment shall be done with the Asset Management Companies directly without involving any broker or intermediary.

Daily funds management

The company receives funds under LDS and ICD from various GoG entities on an ongoing basis which ranges from less than 15 days to 3 years. Hence, in order to manage the liquidity and enable timely repayment of its liabilities, the company shall undertake daily funds management activity by way of deployment of surplus funds in the Overnight & Liquid/Debt Schemes of empaneled Mutual Funds while redemptions shall be done from these schemes for repayment of liabilities on an ongoing basis as these avenues provide high liquidity and reasonable returns.

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Exclusions in case of investments

1. GSFS shall not invest in equity shares. However, in the event of a written directive from the State Government as a part of its strategic requirement, investment in equity shares may be considered to that extent.

2. In case of investments in Asset Management Companies (Mutual Funds), GSFS shall not-

   i) Invest in the Equity Funds;
   ii) Invest in the Hybrid Funds;
   iii) Invest in the Credit-Risk Funds of the Debt Category;
   iv) Invest through any broker or intermediary. All the deployment shall be done under the Direct Code only.

3. GSFS shall not invest in State Government Securities of any state or Union Territory except Gujarat.

4. GSFS shall not invest in Bonds and Debt instruments of Private Sector Corporates.

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LIST OF ABBREVIATIONS

1	GoG – Government of Gujarat
2	GOI – Government of India
3	GSGS – Gujarat State Government Securities
4	G-Sec – Government of India Security
5	GSFS – Gujarat State Financial Services Limited
6	ICD – Inter Corporate Deposit
7	LDS – Liquid Deposit Scheme
8	LoC – Line of Credit
9	MIBOR – Mumbai Inter Bank Offer Rate
10	NAV – Net Asset Value
11	NBFC – Non Banking Finance Company
12	ND-SI – Non Deposit Taking Systemically Important
13	OMO – Open Market Operation
14	PD – Primary Dealer
15	PSU – Public Sector Undertaking
16	RBI – Reserve Bank of India
17	SGS – State Government Securities
18	SLR – Statutory Liquidity Ratio
19	T-Bill – Treasury Bill

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