

TREASURY & INVESTMENT POLICY

Table of Contents

<u>S.No.</u>	<u>Contents</u>	<u>Page</u>
1.	Fundamental Principles	1
2.	Sources & Uses of Funds	3
3.	Operation Sustainability	5
4.	Avenues of Investment	7
5.	Gap Analysis	9
6.	Sovereign Risk	12
7.	Bank Risk	14
8.	Project Risk	16
9.	Segregation of Duties	18
10.	Portfolio Review	20

TREASURY & INVESTMENT POLICY NO 1: FUNDAMENTAL PRINCIPLES

POLICY STATEMENT

Safety, Liquidity and Return shall be three fundamental principles of treasury and investment policy of Hydropower Investment and Development Company Ltd. (HIDCL).

JUSTIFICATION

Funds available at HIDCL at various points of time require to be managed prudently. Prudent management of funds require that funds are safely invested; are available when need arises; and that it fetches best return. Therefore it is essential that management of available funds must be done in the priority order of safety, liquidity and return.

OBJECTIVE

To ensure that investments are safe, liquid and provide best return.

ACTION

1. All the treasury investment and fund management decisions will strictly follow the protocol of Safety, Liquidity, and Return. No deviation on this priority will be permitted.
2. All the investment and fund management decisions must take 'SAFETY' of the fund as the first and foremost consideration.
3. Such investments must fulfill the characteristics of 'LIQUIDITY' so that funds are available on the required time bucket.
4. Having fulfilled the test of safety and liquidity, investment decisions must take careful comparative assessment of best 'RETURN' for HIDCL.

5. Officials involved in treasury management must have or develop the knowledge continuously and keep updated with market conditions and investment options vis-à-vis risks in a continuous manner.

RESULT

HIDCL will have prudent management of available funds.

TREASURY & INVESTMENT POLICY NO 2: SOURCES & USES OF FUNDS

POLICY STATEMENT

HIDCL will plan the investment and use of its funds matching to the tenure and purpose of such funds.

JUSTIFICATION

At various times, HIDCL will have funds available for the purpose of investment. Such availability arises due to various circumstances. At times collection of resources is at hand but disbursement of funds for projects have some time lag because hydropower investment takes a lot of time for planning and preparation. Certain funds are also maintained for liquid assets for contingency purpose or for the purpose of running its day to day activity.

The source of such funds could be the equity funds or other funds collected from various instruments in local or international market. HIDCL will have to categorize such funds as per the requirement of liquidity in various time frames.

OBJECTIVE

To make prudent planning and management of funds.

ACTION

1. A substantial portion of the funds raised from equity will be segregated as funds for lending to hydropower projects. Such funds will be available for investments only for interim period till disbursement in hydropower projects takes place.
2. A portion of the funds raised from equity will be allocated for the purpose of investment in sovereign instruments and term deposits in banks. Such

funds will be available for investment in medium and longer term. The earning from these investments will be the sources for day to day business operations.

3. Small portion of the funds raised from equity will be allocated for contingency purpose. Such funds will be available for investment in shorter term and will be placed in saving, call or checking accounts at banks.
4. HIDCL will be raising funds in the form of deposit or debt instruments from the market for various hydropower projects. Until such funds are invested in the specific hydropower projects, HIDCL requires making best use of such funds. These funds will be for relatively shorter period and therefore cannot be invested for long term instruments.
5. Taking consideration of above, HIDCL will prepare time bucket analysis which may be called as “gap analysis” so that there are no mismatch of assets and liabilities.

RESULT

HIDCL takes into account of various types of funds for investment and plans its allocation for designated purposes to ensure safety, liquidity and return.

**TREASURY & INVESTMENT POLICY NO 3:
OPERATIONAL SUSTAINABILITY**

POLICY STATEMENT

HIDCL identifies a clear and definite source of cash revenue to maintain office overheads and operational expenditures.

JUSTIFICATION

HIDCL will be lending most of its funds in hydropower projects which will have long gestation period. Incomes from such lending will be recognized on accrual basis. There will be no cash revenue whereas HIDCL will require regular cash outflow for meeting its operational overheads and expenditures.

Therefore, HIDCL allocates certain component of the equity fund to invest on longer term sovereign instruments or term deposits at banks. The interest earned from these investments will constitute a source of cash revenue for HIDCL to meet the operating expenses.

OBJECTIVE

To invest a portion of the capital fund to generate cash income.

ACTION

1. HIDCL will allocate 5% of its capital fund for investment in long term high yield sovereign instruments and/or term deposits at banks.
2. HIDCL shall review the level of revenue realized on cash basis and the requirement of cash expenditures at various points of time and may adjust the level of allocated fund.

RESULT

The operating expenditure of HIDCL will be met by cash revenue.

TREASURY & INVESTMENT POLICY NO 4: AVENUES OF INVESTMENT

POLICY STATEMENT

HIDCL identifies various avenues of investments taking into account the policy of safety, liquidity and return.

JUSTIFICATION

HIDCL will choose its decision of investment of available funds from various options available in the market at that point of time. The options of investment will range from fully secured sovereign risk instruments like Saving Bonds, Development Bonds, Treasury Bills etc; placement of funds in various banks and financial institutions to investments in tradable equity.

The decision makers at HIDCL will have available options from short term money market instruments like call deposits, short term treasury bills etc to longer term development bonds and term deposits at banks. The decision will have to be made taking into consideration of liquidity requirements at various time buckets vis-à-vis the yield in such investments.

OBJECTIVE

To choose the most desirable options for investment amongst various available instruments in the market.

ACTION

1. HIDCL will make its decision of choice of investment among various sovereign risk instruments ranging for various time frames. Such instruments will be:
 - (a) Short Term Treasury Bills
 - (b) Saving Bonds

(c) Development Bonds

(d) Other Instruments

2. HIDCL will also have options to choose from placement and deposits for various time frames on 'A' class banks only:

(a) Fixed/Term Deposits

(b) Call and Current Deposits

(c) Placements/Lending

(d) Any other forms of Deposits

3. HIDCL can consider to make investments on following type of instruments issued by hydropower projects:

(a) Equity/Preference Shares

(b) Bonds and Debentures

(c) Commercial Papers

4. HIDCL can also consider making investments on the secondary market of shares/debentures of listed blue-chip companies and mutual funds. A separate guideline will have to be made to avoid speculative risks.

RESULT

HIDCL will be able to make a conscious choice of investment decisions among a range of various options to maximize yield by enhancing security and liquidity.

TREASURY & INVESTMENT POLICY NO 5: GAP ANALYSIS

POLICY STATEMENT

HIDCL will allocate limits for various time-buckets against various instruments to ensure safety, liquidity and best return of its funds available for investment.

JUSTIFICATION

Availability of funds on the future period of requirement is crucial. HIDCL runs the risk of default to its creditors, depositors and lenders if planning of fund is not done meticulously and accurately.

Similarly, if funds are kept idle or if not invested for the appropriate time bucket, HIDCL will earn low return and causes a loss situation. HIDCL requires accurate planning about which of the funds will be required at which predictable time frame in the future period. Such prudent prediction of time bucket will enhance security, liquidity and yield.

OBJECTIVE

To make accurate prediction of available funds for various time-buckets helping prudent investment decision.

ACTION

1. HIDCL will plan its available funds for investment in various time-buckets. The breakdown for the period till 31 Dec 2012 is projected as below: (The figure shown in table is only sample.)

HIDCL: Treasury and Investment Policy

Rs in millions

S. No.	Description	1 - 30 Days	31 - 90 Days	91 - 180 Days	181 - 365 Days	1 - 5 Years	5 - 10 Years	Max Limit
	<u>Assets</u>							
1	Cash Balance	5.00						5.00
2	Bank deposits at A class banks	-			-			7,500.00
2.1	Fixed deposits				5,000.00	5,000.00		7,500.00
2.2	Interest bearing overnight	1,000.00						1,000.00
2.3	Call deposits		1,000.00	1,000.00				1,000.00
2.4	Call Money	500.00						500.00
3	Sovereign Securities							
3.1	Bonds and debentures			100.00	2,500.00	7,500.00	500.00	7,500.00
3.2	Treasury Bills							
4	Loan to Hydropower Projects and Banks							
5	Equity, Bonds and Debentures of hydro power projects					1250	2,500.00	2,500.00
6	Secondary market stocks		100.00	100.00	50.00			250.00
	<u>Total Assets</u>							10,000.00

2. HIDCL will review such projection in quarterly basis and present to Board of Directors for due approval.
3. HIDCL will also make projection of its various liabilities e.g. deposits and debt instruments etc as per above format of time bucket to identify the accurate dates of maturing obligations and plan the sources of funds accordingly on those dates of maturity.

RESULT

HIDCL will be able to plan its funds in various timeframe so that the concern of safety, liquidity and yield is addressed in a logical manner.

TREASURY & INVESTMENT POLICY NO 6: SOVEREIGN RISK

POLICY STATEMENT

Investment in Government of Nepal instruments like Treasury Bills, Government bonds, debentures etc is defined as “Sovereign risk”, a fully secured investment, and investible funds in these instruments will be decided by the liquidity and return factor.

JUSTIFICATION

Treasury bills, saving bonds, debentures, development bonds issued by Government of Nepal are classified as sovereign risks and are considered secured investment. Investible funds within the set time-bucket limit is encouraged to be placed in the Sovereign Risk instruments to the extent that such investments are attractive in terms of yield and is suitable to the liquidity profile of HIDCL.

OBJECTIVE

To classify investment in Nepal Government sovereign risk instruments as the Secured Investment.

ACTION

1. HIDCL classifies investment on different securities issued by Government of Nepal and NRB as sovereign risk and therefore “secured” investment.
2. Investment up to the limit allocated in time-bucket for sovereign risk can be made with the approval of CEO upon recommendation of Finance/Treasury Department. Finance/Treasury Department shall evaluate its recommendation from liquidity and yield perspective.

3. Till such allocation limit is finalized in time bucket for various types and tenures of securities; investment up to 50% of the net worth of HIDCL will be permitted to invest on Sovereign risk instruments with the approval of CEO upon recommendation of Finance/Treasury department.
4. Management could contain exposure in sovereign risk instruments less than this limit set above depending upon the liquidity and yield considerations.

RESULT

HIDCL will make optimum level of investment in sovereign risk instruments ensuring adequate liquidity and return.

TREASURY & INVESTMENT POLICY NO 7: BANK RISK

POLICY STATEMENT

All deposits or placements in various banks are classified as “Bank Risk”. Counterparty risk assessment and exposure limit for each bank must be predetermined.

JUSTIFICATION

HIDCL will require to keep deposits of various tenures and types in the course of day to day business. Term deposits, call deposits and overnight deposits are good source of investments and yield.

There are chances that if banks get into financial distress, HIDCL’s funds placed in such bank can be lost or in difficulty with potential legal problems. Therefore to minimize such potential risk, HIDCL will make a procedure of “counterparty risk assessment” of each bank and set limits of deposits which HIDCL can place in each of these banks.

OBJECTIVE

To set bank limits before placing funds in banks.

ACTION

1. HIDCL will place its funds only on NRB licensed “A” class banks.
2. Risk analysis for each “A” class bank requires to be completed taking into account of the key financial indicators like capital adequacy, NPA, liquidity etc; financial reports of last three years; market reputation; quality of management; governance practice etc.

3. Limit for each bank will not be allowed to exceed more than 25% of the concerned bank's core capital.
4. Total investment on Bank Risk will be as set in various time buckets for various types of deposits.
5. To determine best yield and to establish transparency while placing deposits in banks, HIDCL may take the route of public bid announcement and offer to the highest bidder provided that such banks enjoy exposure limit with HIDCL.

RESULT

HIDCL's investment in various banks will remain within acceptable risk.

TREASURY & INVESTMENT POLICY NO 8: PROJECT RISK

POLICY STATEMENT

Any kind of investment made by HIDCL in the bonds, debentures, and any form of participation in equity or venture capital of a hydropower project is classified as “Project Risk”.

JUSTIFICATION

HIDCL may require investing in the bonds, debentures and equity or may acquire a stake as a venture capital of hydropower projects. Such investments could be in addition to the loan extended to the project. All such investments have to be regarded as project risk exposure because HIDCL’s investment can be at risk in the project’s difficulties. Therefore such investments have to be evaluated in the same spirit and risk like extending a loan to a hydropower project.

OBJECTIVE

To clarify bonds, debentures and equity investments made in hydropower projects as “project risk”.

ACTION

1. Any investment in bonds, debentures, and equity will be evaluated as extending a loan to a project and the parameters of sound risk assessment has to be completed.
2. Total exposure to the project is calculated by adding the loan component plus investments in debt, bonds and equity.
3. Such total exposure will not exceed 25% of capital fund of HIDCL.

4. Investments in projects' bonds, debt and equity will be carefully evaluated in terms of security, liquidity and return.
5. Exposure on these instruments also needs to be within the limit set by the time bucket.
6. As these exposures are "project risk", a due care has to be adopted to assure that it is an acceptable risk. Risk mitigation measures have to be followed.
7. All bonds, debentures and equity including venture capital investment require to be approved by the Board of Directors of HIDCL upon the recommendation of the Risk Management Committee.

RESULT

HIDCL's investment in various bonds, debentures and equity or venture capital of hydropower project will be considered after due risk analysis to ensure that it is an acceptable risk.

TREASURY & INVESTMENT POLICY NO 9: SEGREGATION OF DUTIES

POLICY STATEMENT

The responsibilities and authorities of business deal makers, settlement process and accounting are clearly segregated.

JUSTIFICATION

HIDCL shall put in place appropriate controls and procedures in respect of the handling and management of various types of investments and instruments. This is important to control any kind of potential frauds, mishandling of instruments and loss of funds. The decisions of investment will be taken by the front office upon compliance of due approval process. All the document controls and instrument controls will be handled by back office and/or accounting department.

OBJECTIVE

To establish separation of front office and back office accounting functions so that there are enough check and control on all investment activities.

ACTION

1. Investment decisions will be made by front desk of Treasury department with due approval process.
2. Once the approval of the deal is done, it will be forwarded to Back Office in accounts department who will do the reconfirmation, record updates and keep the documents and instrument in appropriate safe keeping with dual control in a fireproof cabinet or in the vault room.

3. The fundamental principle of maintenance of internal controls is the functional segregation of the front office and back office and settlement functions.
4. The ideal segregation of the duties will be as follows:

Front office : Dealing/Approval/Contract/Agreement

Mid-Office : Risk management, accounting and management information

Back office : Confirmations, settlement and reconciliation
5. In all circumstances, personnel in back office functions and mid-office functions should be functionally segregated from those in the front office. Persons who conclude deals/transaction must not be involved in the confirmation or settlement of deals/transaction.
6. Deals recorded by the trader are confirmed independently by the back-office.
7. The effectiveness of the segregation of duties and internal control is annually reviewed by the internal auditor.
8. The adequacy of filing and instrument security and accuracy has to be assured by internal auditor in half yearly basis to the Audit Committee and Risk Management Committee.
9. Until the front office, mid office and back office is set-up, an appropriate mechanism could be applied with maker, checker and approver process to ensure the effective control over treasury operation.

RESULT

There will be appropriate control mechanism at place avoiding risks that may cause loss of value, loss of instruments or misplacement of documents.

TREASURY & INVESTMENT POLICY NO 10: PORTFOLIO REVIEW

POLICY STATEMENT

HIDCL shall establish the review mechanism of its portfolio periodically by senior management and Board of Directors.

JUSTIFICATION

The assets portfolio has several risk associated with it. Risks like interest rate risk, currency risk, and concentration risk should be understood and controlled properly. Risk may result into loss. The portfolio should be controlled, well managed and justified all the time.

OBJECTIVE

To ensure safety, liquidity and good return from the portfolio.

ACTION

1. Find out the average yield in investments.
2. Scrutinize if the portfolio assets are as per the desired and approved plan.
3. Compare against set targets for portfolio growth and diversification.
4. Confirm if established benchmark mix and yield have been followed.
5. The Risk Management Committee shall review the portfolio mix and return at least on half yearly basis and provide guidance accordingly.

RESULT

Safe and secure portfolio with good rate of return.