Shrenuj & Company Limited

Risk Management Policy

Executive Summary

This Risk Management Policy document provides a framework for the management of Shrenuj & Company Limited (“SCL” or “Shrenuj” or “ the Company”) to manage its foreign exchange and other associated risks. This policy contains a detailed description of the objectives, scope, operation and control framework for management of risks associated with foreign exchange, interest rate, commodity prices etc.

This document constitutes an important part of the process of formalization and documentation of operating risk management policies. It defines overall roles, responsibilities and controls for respective activities and the personnel authorized for the same, and also for the purpose of control and corporate governance.

This policy may be reviewed and amended from time to time to meet the evolving requirements of the business, dynamic risk scenario and any regulatory and statutory requirements or amendments.

1. Objective of the Risk Management Policy

The main objective of the policy is to protect the Company against unfavorable currency movement arising on account of volatility in the forex market and adverse interest rates movements and volatility in commodities. The policy lays down the guidelines of hedging the Company’s receivables, payables, other assets and liabilities to ensure that the possible losses arising out of various market risks are minimized.

The policy also lays down hedging norms and setting up of authorization limits, roles and responsibilities of the treasury dealer, reporting of hedging activities to the Risk Management Committee, accounting treatment and audit compliance relating to such activities.

2. Background & Scope

This Policy is applicable to entire group of Shrenuj which includes Shrenuj & Company Limited and its subsidiaries including step-down subsidiaries/Joint Ventures and Associate Companies. The Company covers entire spectrum of gem and jewellery business, from diamond and jewellery manufacturing to branded jewellery and retail. The Company has sound corporate governance and is represented by highly qualified, eminent and professional Directors of the Board. The Company exports to subsidiaries/associates established overseas and to independent customers abroad. The Company is a DTC sight holder for imports of rough diamonds.

The Company has business across borders which necessitate the dealing in foreign currencies for its receivables and payables. This is fraught with various risks due to volatility in the foreign exchange market. The various risks are explained below:

Exchange Rate Risk:
This risk arises on account of movement in the exchange rates of the foreign currencies where the Company has exposure.

Interest Rate Risk:
This risk arises on account of movement in interest rates in India and in foreign currency market where the Company has borrowing exposure. e.g. if there is upward movement in interest rates in Indian rupee or dollar market, then the Company would be exposed to interest rate risks.

Liquidity risk:
This risk arises on account of the Company's short term need for cash to settle import commitments and local payments. Changing economic conditions affecting global demand for the Company's production and/or delay in realization of receivables may cause mismatches in working capital needs of the Company.

Economic Risk:
The changes in economic policy of the government, inflation levels and trends, GDP growth and also international political and economic conditions and events have an impact on the currency market.

Commodity Risk:
Commodities are subject to market risk. The commodity risk may arise from fluctuations in global commodity prices, exchange rate and supply and demand factors.

In view of the various risk perceived as above and to protect the Company by mitigating the foreign exchange risk, the Company's management has formulated a revised risk policy.
The current policy includes hedging of currencies and interest rates & commodity hedging (mainly gold) which forms an integral part of our jewellery business.

3. Management of exchange risk

3.1. Hedging Norms & Authorization Limits

The foreign exchange dealing is fraught with exchange risk. To protect against adverse movement of exchange rate the Company should hedge its receivables and payables. The Company should at a prudent level hedge its estimated receivables/payables. The Risk Committee shall on the basis of currency and interest rate movements, decide on the hedging ratio which, in any case should not be less than 10% of the estimated receivables and payables for the year. This should also consider

seasonality of the business activity affecting import/export volumes. This flexibility would provide an efficient hedging environment for the forex dealer based on prevailing market conditions at any point of time.

The budgeted exports and imports for the year should be the guideline for booking the hedge positions.

At any point of time the hedged positions should be as under:

	Particulars	Minimum Limit of Hedge positions	Maximum Limit of Hedge positions
1	Receivables/inventories	Nil%	40%
2.	Payables	Nil	20%

The percentage of hedging ratio within the specified limits will be subject to review of the Risk Committee based on the currency and interest rate movements prevalent during the course of the financial year.
The above limits should consider estimated deliverable foreign exchange excluding commitments under pre/post shipment foreign currency finance. The position taken will normally include deliverable foreign currency under the forward contracts/options structure maturing within one year. For the option structure for a longer tenure of over one year, specific approval should be obtained only from the risk committee. The booking beyond the limits specified should be subject to approval of the Risk Committee.

3.2. **Tools of Hedging:**

The hedging of the receivables/inventories and payables will be effected by the forex dealer within the parameters set above. The hedging is normally against USD/INR. However, in addition to this the dealer may book forward foreign exchange transactions as hedge transactions where the currency of hedge is different from the currency of underlying exposure. This will help in managing the risk more dynamically and help in reduction of cost. Further, as USD/INR is affected by global factors and movement of other major currencies, hedging through such major currencies will help in managing both the risk and cost effectively and efficiently.

The forex dealer shall use any one of the following hedging tools for hedging its receivables/inventories/payables:

- Forward contracts

A forward contract will lock in an exchange rate at which the transaction will occur at a future date.

- Options
 An option contract sets a rate at which the Company may choose to exchange currencies with its counter party. If the current exchange rate is favorable then the Company will not exercise the option.

 Option contracts will be effectively used in case of sharp movements in the spot & forward markets to partly offset the impact of such rate movements.

3.3. **Fixation of Limits**

- Hedging Limit
 The forex dealer shall not hedge more than USD 20 mn in case of USD/INR forwards and additional USD 20 mn equivalent in cross currencies on any single occasion. In case of extreme situation wherein a large exposure in excess of the limit prescribed to the forex dealer needs to be hedged, the forex dealer shall obtain the prior approval of the Chief Finance Officer. This action has to be subsequently ratified by the Risk Committee.

- Stop loss limits
 There is need to have a stop loss limit for the forex dealer in case of Intra day/overnight open positions and in case of sudden or sharp movements in spot/forward rates. The stop loss limit will restrict the loss that may arise in the event of adverse movement of currency. The forex dealer should exit the open position immediately after the stop loss limit is triggered.

 In the event of any apparent mismatch in the estimated cash flows after hedge positions are taken or any sharp fluctuations in currency affecting these hedged positions due to mismatches, the dealer may evaluate the potential loss or gain, if any, in consultation with senior management and cancel the hedged position with an option to rebook fresh positions.

 However, if the dealer is of a strong view not to exit the position, then the reasons therefore need to be documented and approval of the Risk Committee has to be obtained.

- Take profit limits
 To take advantage of the favorable movement of currencies, the dealer may book profit and exit the hedged position and rebook at appropriate level depending on the view.

 If the forex dealer is of the view not to book profit then the reasons have to be documented and approval of the Risk Committee has to be obtained.

- Mark to Market (MTM)

  The forward contracts/derivative products should be marked to market on regular basis. The office should prepare a MTM valuation for the information of the top executives and the Board of the Company.

3.4. **Fixation of limits for derivative (option) products**

The Company may enter into derivative products with the following banks with the maximum notional amount as specified below:

ICICI Bank – Rs. 200.0 crores

Citi Bank - Rs 200.0 crores

Standard Chartered Bank – Rs 200.0 crores

The following dealers are authorized to undertake the derivative transactions on behalf of the Company:

Mr. Shridhar Sawant – Group CFO

Mr.Gopi Nair – Manager Exports

The following derivative (plain vanilla & structured) transactions in addition to normal forward contracts can be entered into by the above mentioned dealers:

1. Plain vanilla buy options - To sell an option to reduce the cost of hedging wherever appropriate.

The limits authorized to the dealers designation wise per transaction basis for derivative products (plain vanilla and structured options) are as under:

CFO – Rs 80 crores

AGM Accounts – Rs 60 crores

Manager Exports – Rs. 40 crores

Assistant Manager –Rs.20 crores

The derivative transactions entered into by the Company should be reported to the following personnel:

Mr. Vishal Doshi – Group Executive Director

Mr. Shridhar Sawant – Group CFO

The following personnel are authorized to sign the ISDA and similar agreements on behalf of the Company

Mr.Shreyas Doshi – Chairman & Managing Director

Mr. Vishal Doshi – Group Executive Director

Mr. Shridhar Sawant – Group CFO

4. Interest Rate Risk

4.1. Hedging of interest rate risks

The Company's debt requirement is funded either in Indian rupees or in foreign currency. Depending on the availability of funds at cheaper cost the Company may resort to borrowings in Indian rupees or in foreign currency. The foreign currency borrowing of the Company is generally in US dollars where the interest rates are linked to LIBOR. (London Inter Bank Offer Rate).The upward movement in interest rates due to liquidity or other factors would expose the Company to interest rate risk. The Company should use certain tools of hedging to safeguard itself from interest rate risk.

4.2. Tools of Hedging

The Company may resort to interest rate swaps, interest rate caps, FRAs in USD or in other currencies to protect itself from upward movement of interest rates. This will help the Company to lock in interest expenses. The decision of hedging will be subject to the approval of the Risk Committee. Likewise, the Risk Committee should also decide whether to exit the swap, if the interest rate falls subsequently.

Interest rate swaps are normally combined with cross currency swaps and cash inflow on lower interest rate in swapped currency is available as long as both the currencies move in certain range. The currency risk in principal loan amount starts only when exchange rates move out of this range. Hence any such IRS/FRAs should be only subject to prior approval of the Risk Committee.

In case of higher foreign currency borrowings which provide a natural hedge, the cost of funds is a deciding factor. However, this reduces the Company's ability to deliver dollars/foreign currency

under the dollar/rupee forward contracts and/or option structures. So while stepping up foreign currency borrowings to reduce interest costs, all the dollar rupee hedging positions need to be reviewed carefully. If the Risk Committee is of the view that the forwards/options bought as a hedge for earlier rupee borrowings need to be continued and may yield cash surpluses, the contracts need not be cancelled immediately. In case any potential loss is expected while switching over to foreign currency borrowings, then both the pros/cons of the decision should be weighed and the dealer/forex treasury should be given clear instructions to gradually reduce hedge positions which should also be reviewed on weekly basis.

5. Commodity Risk

5.1. Hedging of commodity risks

Commodities like gold, silver etc. form major component of raw material cost. These commodities are subject to market risk arising from fluctuations in global commodity prices, exchange rate and supply and demand factors. Considering the overall volatility in the commodity market it is important for the Company to adopt proper hedging mechanism to protect its operating margin.

5.2. Tools of Hedging

The Company may resort to hedging of commodities like gold and silver through COMEX/ MCX to safeguard its cost of procurement of gold /silver. The decision of hedging will be subject to the approval of in-charge of gold purchases department and CFO. In case of hedging through MCX, the exchange rate risk may also be hedged as and when appropriate through currency futures/OTC market. The Company should ensure that at least 50% of the total open order position is hedged either through direct purchases or through COMEX/MCX.

5.3. Hedging Procedure

Based on the prevailing gold rates in COMEX, orders are finalized with the buyer. After that based on the view of gold prices, certain quantity of gold is hedged in MCX. The currency leg is then covered in currency futures based on the USDINR view at appropriate levels/time.

6. Receivable/Book Debt Management.

Shrenuj Group is in the business for more than 10 decades and having very conservative and closely monitored systems for taking credit limits calls on every distributors/Traders/Customers globally. The Credit limits is defined on following understanding/rationals.

a. Relationship with Shrenuj Group.
b. Past history of delay/defaults, if any.
c. Payment as committed or not.
d. Onward sales achievement to the end customers.
e. Consistency in taking delivery from Shrenuj Group.
f. Feedback from our regional head/country head about customers quality/issues and their performance.

Looking at above parameters the centralized credit department in India decide the credit limits for the each customers/ group, but limit the exposure to the tune of USD 5 Millions for a large group and restrict credit exposure of USD 1-2 Millions for a small group. Any deviation on credit limits has been approved by the risk committee which consist of Mr. Shreyas Doshi – Chairman and Managing Director , Mr. Vishal Doshi- Group Executive Director, Mr. S.S. Thakur – Director and Mr. Shridhar Sawant – Group Chief Financial Officer.

Apart from above, the group is having Audit Committee and Internal Auditors where at regular intervals the credit process/Credit monitoring/Collection progress and outstanding more than 180 days has been assessed/monitored an the report has been presented to the Board for necessary action.

7. Roles and Responsibility of the Forex Dealer

- The dealer should ensure that limits set up with the bankers are properly utilized for the purpose they are sanctioned and should monitor MTM regularly.
- The dealer should continuously monitor the currency movement and based on the market views initiate hedging transaction for receivables/inventories/payables as the case may be.
- The dealer should execute the trades within the limits set for him.
- The dealer should keep a track of the important data and accordingly devise hedging strategies.
- In case of extreme situations where a transaction is in excess of the limits set to the dealer is to

be hedged, the dealer should obtain prior approval of Chief Finance Officer.

- The dealer should monitor on daily basis the positions hedged and give the necessary feedback in the Risk Review report submitted to the Board every quarter and to identify any potential losses/mismatches to modify the hedging strategy.

8. Process Flow

- Once the deal is initiated for hedging receivables/inventories/payables, the dealer should enter the same in the deal slip .The deal slip should spell out the value in foreign currency, the rate, the name of the bank, the contract date and the maturity date. The deal slip should be authorized by /CFO.

- The dealing activities undertaken by the dealers need to be reported to the CFO/Group Executive Director by email on the same day. The following reports should be generated:

- Deal Slip:

  The slip would give the details of the deal undertaken during the day.

- Forex report:

  This report containing details of outstanding positions bankwise, profit/loss for particular date as well as amount receivable/payable from/to various banks/MTM should be available as and when required to /CFO/Group Executive Director/Chairman & Managing Director.

- Monitoring

  In addition to the above the concerned officials should monitor :

  1. The total outstanding hedged positions as on the end of the month
  2. The gains/loss arising from hedged positions.
  3. Monitoring of hedged positions and MTM arising out of the hedged positions booked by way of Forward contracts and options.
  4. Ratification of deals if any

9. Risk Management Committee

9.1. Composition

The Risk Management Committee will comprise of:

1. Shri S. S. Thakur – Chairman (Independent Director)

1. Shri Shreyas K Doshi - Member (Chairman & Managing Director)
2. Shri Vishal S Doshi - Member (Group Executive Director)
3. Shri Shridhar Sawant – Member (Group Chief Finance Officer)

9.2. **Meetings**

The Risk Management Committee shall meet at least once in a year to discuss and review:

- The current outstanding hedged positions.
- The current market situation and outlook in terms of the currencies directly or indirectly affect the Company's business operations overseas.
- The review of the MTM of hedged positions.
- The review of the potential gain/loss and direct the dealer to cut positions to reduce risk.
- The current exposure of the Company and the risks involved
- Ratification of deals if any.

9.3. **Reporting to the Board**

The risk review report should be placed before the Board on quarterly basis giving explicitly

- The forward/option contracts booked in USD/INR and in other cross currencies where one leg is US dollar.
- Assessment of risk identification and assignment of risk of foreign exchange and interest rate risks.
- Assessment and assignment of financial risk.

10. Accounting And Audit Compliance

The Accounts Department should ensure that proper accounting entries are made in respect of all the deals undertaken by the dealer. It shall be ensured that proper accounting norms are followed for all derivative transactions. Proper accounting norms should be followed for revaluation and reporting of MTM positions.

The audit should be undertaken at periodic intervals. The areas to be tested during this audit shall include:

- Reconciliation of forex position between the dealer's records and the accounting system
- Review of deal confirmations

- Functional separation of mid office back office and dealing room
- Completeness, correctness and timeliness of internal reporting system
- Any other matter which would help in strengthening the reporting function