

ANNEXURE 11: CORPORATE DEBT MARKET DEVELOPMENT FUND (CDMDF)

Annexure 11A - Approach to Purchase Pricing⁴⁷⁹

1. While it may not be possible to pre-empt the events and scenarios prevailing at the point of time when purchase of securities is being undertaken by CDMDF, the investment policy may provide for following indicative factors for determining purchase price of corporate debt securities:
 - 1.1. Valuation policies prescribed for Mutual Funds (based on the principles of fair valuation).
 - 1.2. Previous day's valuation of securities by valuation agencies before the date of Purchase.
 - 1.3. Average 10 days valuation prior to start of market dislocation.
 - 1.4. Mark-up in yield over previous day may be limited to arrive at floor price.
For eg: it may be 25/50/75 bps over AAA/AA/Below AA securities respectively.
 - 1.5. Consideration of Spread over benchmark/ spread over sovereign yields.
 - 1.6. Qualitative factors that may have bearing on arriving at fair price.
2. The investment policy shall be duly approved & reviewed periodically by the Board of Trustee, Investment Committee & Governance Committee. CDMDF shall adhere to investment framework laid down in the investment policy & the fund documents.
3. However, in case the Investment Manager is at variance from the aforesaid factors, they may, after recording reasons in writing and approval from Investment Committee, take such price as deemed fit with an objective of achieving the fair pricing (adjusted for liquidity risk, interest rate risk and credit risk). Such instances shall be apprised to Governance Committee and Board of Trustees on a regular basis.
4. Investment framework of CDMDF:
 - 4.1. CDMDF would buy securities from secondary market of only investment grade, listed and having residual maturity of upto 5 years.
 - 4.2. CDMDF shall not buy any unlisted, below investment grade or defaulted debt securities or securities in respect of which there is a material possibility of default or adverse credit news or views. The rationale for the same shall be documented.
 - 4.3. Purchase of securities to be done as per the above fair pricing guidelines to be adjusted if considered appropriate by the IM for liquidity risk, interest rate risk, and credit risk. Buying/trading to be at fair price but not at distress price.
 - 4.4. Selling at breakeven/profit as market stabilize, to reduce borrowing as soon as possible.

⁴⁷⁹ Inserted by SEBI Circular No. SEBI/HO/IMD/POD2/P/CIR/2023/128 dated July 27, 2023

- 4.5. Valuation of portfolio shall be governed by existing norms on valuation under the Mutual Fund regulatory framework.

Annexure 11B - Loss Waterfall Accounting for CDMDF⁴⁸⁰

Based on deliberations with Mutual Fund industry, the following shall be the approach for reflection of waterfall in the NAV of units of CDMDF

- A. There shall be three classes of units to be allotted by CDMDF, which shall be as follows:
1. Class A1 and Class B units shall be allotted to AMCs and Sponsor/IM respectively (against one time contribution of 0.02% of AUM of specified debt schemes and Sponsor/IM commitment). Class A1 units and Class B units are treated at par and referred as Class A1 units only.
 2. Class A2 units shall be allotted to specified debt schemes (contributing 0.25% of AUM of specified debt schemes)
 3. Class A3 units shall be allotted to Mutual Fund schemes selling debt securities to the Fund (where 10% of the consideration is in the form of units of CDMDF, called A3 units)
- B. Daily NAV should reflect the fair value of each unit class including the effect of differential treatment of A3 unit class. The loss waterfall based on CDMDF Framework is as follows:

Level of loss absorption	Particulars	Hereinafter referred as
1st	Up to 10% by MF schemes selling debt securities to the Fund (i.e., equivalent to the units outstanding of the selling MF schemes issued to them against sale of securities to CDMDF)	Class A3 units
2nd	Contribution of specified debt oriented MF Schemes and AMCs	Class A1 and A2 units
3rd	Government Guarantee	NA

- C. The following process shall be followed:
1. All profits/losses/income/gains/expenses to be apportioned to A1 and A2 unit class in ratio of their AUM during the normal times.
 2. A3 units to be allotted at the same NAV as that of A1 & A2 at the time of opening of market dislocation.
 3. All profits/losses/income/gains/expenses (including cost of leverage) to be apportioned to all the 3 class of units during the market dislocation and

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subsequently till A3 units exits (i.e A1/A2/A3), except that the NAV of A1 and A2 should not drop below their opening NAV (opening NAV at the time of market dislocation). Since A1 and A2 units are to be protected at their opening NAV to that extent the excess/unabsorbed loss/expense would be debited to only A3 unit class. This would mean the NAV of A3 units could drop below the NAV of A1&A2

4. Any subsequent profits/gains/income will be first credited to the A3 unit class to an extent that they come back at par with A1 & A2 NAV, and then the balance to be apportioned to all the three unit class.
 5. A3 units will not get any exit till there is an outstanding portfolio from market dislocation and leverage is completely paid.
 6. Any subsequent allotment of A3 units would be at the same NAV as that of the existing A3 units (if they exist), otherwise at opening NAV of A1 and A2. There will be only one class/bucket of A3 units irrespective of whether they were issued in subsequent tranche of purchase during a particular phase of market dislocation or were issued during another phase of market dislocation. Therefore, any adjustment for loss/expense will be carried out to the entire bucket o A3 units irrespective of when they were allotted.
 7. There will not be any segregation of portfolio linking to different phase or tranches of purchase during the market dislocation, entire portfolio will be one common pool, both during the normal times or during the market dislocation including if there is any security that exist from normal times and is continued during the market dislocation
 8. The accounting of A3 and certain adjustments of NAV may require manual workings by the fund accountant and will not be completely system driven. Such manual workings can be subject to second check by the concurrent auditor.
- D. The above is as per various scenarios that have been envisaged currently. There may be a need that may arise with some other scenarios emerging and the same would be dealt with appropriately through relevant committee.

Loss Waterfall accounting for CDMDF

Allocation Mechanism		Investment					System
INR		A1	A2 A3	Total	GSEC/C BLO	MD- INVT A3	Situation
Subscripti on Face		1,000	1,000	-	2,000		
value		10.00	10.00	-			
Number of units		100	100	-			

Part A

Scenario - 1				2,000	2,010		Investment in Government Securities and T-Bills	System driven calculation
MTM Gain		5	5	-	10		MTM Gain is proportionately allocated to all the unit holders (except A3 doesn't exist as of now)	
NAV of the Corpus		1,005	1,005	-	2,01			

Scenario - 2					2,002		Investment in Government Securities and T-Bills	System driven calculation
MTM Loss		-4	-4	-	-8		MTM loss is proportionately allocated to all the unit holders (except A3 doesn't exist as of now)	
NAV of the unit		10.01	10.01	-				
NAV of the corpus		1,001	1,001	-	2,002			

Scenario - 3					2,006		Investment in Government Securities and T-Bills	System driven calculation
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Realised gain NAV of the unit	2 10.03	2 10.03	- -	4			Gain is proportionately allocated to all the unit holders (except A3 doesn't exist as of now)	
NAV of the Corpus	1,003	1,003	-	2,006				

Scenario - 4					2,004		Investment in Government Securities and T-Bills	System driven calculation
Realised loss NAV of the unit	-1 10.02	-1 10.02	- -	-2			loss is proportionately allocated to all the unit holders (except A3 doesn't exist as of now)	
NAV of the corpus	1,002	1,002	-	2,004				

Scenario - 5					204	2,000	Market Dislocation triggered	System driven calculation
Opening NAV of the Corpus Number of opening units Opening NAV of the unit	1,002 100 -	1,002 100 -	- -	2,004				
Additional Capital	-	-	19.96	200			A3 NAV assumed to be same as A1 and A2 while allotting the units. A1 and A2 NAV will be the opening NAV for the market dislocation trigger	
NAV at the which the units to be allotted Number of additional units								

Total corpus (NAV)	1,002	1,002 200	2,204			
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Part B

Scenario - 6			214	2,000	MTM profit	system driven except the FA needs to now start monitoring the NAV of A1 and A2 should not drop below their opening NAV of Rs. 10.02 till A3 NAV is positive
MTM Gain						
NAV of the unit	4.5	4.5 0.9	10		MTM gain gets apportioned to all the unit class	
	10.07	10.07 10.07				
NAV of the Corpus	1,007	1,007 201	2,214			

Scenario - 7				206	2,00,00,000	MTM Loss	system driven except the FA needs to now start monitoring the NAV of A1 and A2 should not drop below their opening NAV of Rs. 10.02 till A3 NAV is positive
MTM Loss NAV of the unit	-3.6 -3.6 0.7 10.03 10.03	- - - 10.03 10.03	-8			MTM gain gets apportioned to all the unit class, however the NAV of A1 and A2 should not drop below opening NAV of 10.02	
NAV of the corpus	1,003	1,003 200	2,206				

Scenario - 8				710	1,50,00,000	Realised Gain	system driven except the FA needs to now start monitoring the NAV of A1 and A2 should not drop below their opening NAV of Rs. 10.02 till A3 NAV is positive
Realised gain NAV of the unit	1.8 10.05 10.05	1.8 0.4 10.05 10.05	4			Realised gain gets apportioned to all the unit class	
NAV of the Corpus	1,005	1,005 201	2,210				

Scenario - 9				908	1,30,00,000	Realised Loss	system driven except the FA needs to now start monitoring the NAV of A1 and A2 should not drop below their opening NAV of Rs. 10.02 till A3 NAV is positive
Realised loss NAV of the unit	-0.9 -0.9 0.2 10.04 10.04	- - - 10.04 10.04	-2			Realised Loss	
NAV of the corpus	1,004	1,004 200	2,208			Realised Loss gets apportioned to all the unit class	

Scenario - 10	888			1,300	Significant MTM loss	Manual working and intervention required
MTM loss	-9.1 1.8	-9.1 -	-20			
NAV of the unit	9.95	9.95			with the loss getting apportioned to all the 3 unit classes, the NAV of A1 and A2 is falling below their opening NAV of 10.020	
NAV of the corpus	995	995 199	2,188			

Manual working and adjustment to be carried out	888			1,300		
Less: Protection to opening NAV Surplus to absorb the w/off	10.02	10.02				
Number of units	0.02	0.02				
	100	10				
	0					
NAV post the loss absorption	10.02	10.02			which is same as the opening NAV	
Unabsorbed loss entirely to A3		-16.36	16.36			
Corpus NAV of A3 units post absorbing the waterfall loss		184			Now A3 unit NAV drops below the NAV of A1 and A2. this is manual adjustment to be done in the system where there should be transfer of value between the unit class based on such workings	
A3 class unit NAV post absorbing the waterfall loss		9.22				
Closing corpus(NAV)	1,002	1,002 184	2,188			

Cash loss	-13.7 2.5	-13.7	-	-30			
NAV of the corpus	988	988	181	2,158			

Manual working and adjustment to be carried out

Less: Protection to opening NAV Surplus to absorb the w.off	10.02	10.02	10.0				
Number of units	-	-	-				
Loss to be absorbed by A1 and A2	-	-	-	-			
NAV post the loss absorption	10.02	10.02					which is same as the opening NAV
Unabsorbed loss entirely to A3			-30	-30			
Corpus NAV of A3 units post absorbing the waterfall loss			154				Now A3 unit NAV drops below the NAV of A1 and A2. this is manual adjustment to be done in the system where there should be transfer of value between the unit class based on such workings
A3 class unit NAV post absorbing the waterfall loss			7.72				
Closing corpus(NAV)	1,002	1,002	154	2,158			

							Additional Security of Rs 1000 purchased and
Current NAV of units	10.02	10.02	7.72				
Number of units	100	100	19.96				
			12.96				
Balance Cash profit to be distributed	1.77	1.77		4.13			
				4.13			

Scenario -13			1,313	1,000	1,00A3 portfolio sold of Rs 300 at Realised loss of Rs 40 & MTM of Rs 15	Manual working and intervention required
MTM Gain	-	-	15			
Cash Loss		-	-40			
Current NAV of units	10.04	10.04				
Less: Protection to opening NAV Surplus	10.02	10.02				
to absorb the w/off	0.02	0.02				
Number of units	100	100				
NAV post the loss absorption	10.02	10.02				
Unabsorbed loss entirely to A3		-21.45	-21.45			
A3 class unit NAV post absorbing the waterfall loss		9.39	9.39			

Scenario -14			1,343	1,000	MTM gain gets apportioned to A3 until the Opening NAV and then to all remaining unit holders	Manual working and intervention required
MTM Gain						
NAV of the unit	10.02	10.02	30			
Corpus NAV post bridging the gap	1,002.00	1,002.00 329.87	2,334			
Balance Cash profit to be distributed			9.13		Post gains apportioned to A3 balance MTM gain gets apportioned to all the unit class	
Distribution of balance profits	3.92	3.92	9.13			
Corpus AUM post bridging the gap	1,005.92	1,005.92 331.16	2,343			

NAV after distribution	10.06	10.06	10.06	10.06	10.06	10.06	10.06	10.06	10.06	10.06
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1. Post achieving parity in NAV again the normal accounting would sta