

SDL Valuation

Methodology

Background:

CRISIL Funds and Fixed Income Research provide valuation for all State Development Loans (SDL) securities to subscribers on a daily basis. These prices are used by various market participants such as AMCs, Insurance Companies, Custodians/ Fund accountants to value their portfolio. State Development Loans (SDL) is a bond issued by state governments to fund their fiscal deficit. SDLs service their interest at half-yearly intervals and repay the principal amount on the maturity date. RBI coordinates the actual process of selling these securities.

Valuation Methodology

Step 1: Same ISIN secondary trade VWAY of last 1 hour subject to outlier validation

- VWAY of Trades reported on RBI Negotiated Dealing System – Order Matching segment (NDS – OM) & RBI Negotiated Dealing System (NDS) for last one hour are considered for valuation over full day VWAY for Same ISIN
- Trades reported on NDS OM & NDS with minimum trade volume of 5 crore including regular market trades and odd lot are considered
- If trade is outside our threshold, we will poll from market participants for fair level for valuation for that particular ISIN

Step 2: Same ISIN secondary market trade VWAY for the day subject to outlier validation

- In absence of same ISIN trade in the last one hour, VWAY of Trades reported on RBI Negotiated Dealing System – Order Matching segment (NDS – OM) & RBI Negotiated Dealing System (NDS) for full day are considered for valuation
- Trades reported on NDS OM & NDS with minimum trade volume of 5 crore including regular market trades and odd lot are considered
- If trade is outside our threshold, we will poll from market participants for fair level for valuation for that particular ISIN

Step 3: VWAY of Primary issuances (auction yield)

- In case of no secondary market trade for reissuance/new auction papers, VWAY of Primary trade (Newly auctioned paper/ Re-issuance) will be considered for valuation (SDLs are re-issued or auctioned once a week mostly on Tuesdays)
- If trade is outside our threshold, we will poll from market participants for fair level for valuation for that particular ISIN

Step 4: VWAY of same issuer similar maturity secondary market trade of last one hour & full day subject to outlier validation

- VWAY of traded levels in any state in a year to be given to all papers of same state, similar maturity, similar coupon and same type (Special or Normal). In the case of multiple papers in the same year having trades, VWAY of those levels to be given to the remaining papers.
- Due to high volatility in papers in some tenors, papers are divided into multiple buckets in that year. The number of buckets in each year and tenor of each bucket is decided based on feedback from market participants(on

recorded line) and discussion internally. VWAY traded levels in any paper in a bucket to be given to all papers in that bucket only.

Step 5: Two-way quote not wider than 5 bps on NDS OM, subject to outlier validation

- Two-way quotes (bid and ask both are available) reported on NDS – OM are taken as valuation input with minimum quantity for the quotes of 5 crore each. Mid-point of two-way quote is given to that same ISIN
- In case of no trade in same state of the same year, mid-point of two-way quote is given to all papers of same state, similar maturity/bucket, similar coupon and same type (Special or Normal). Other similar issuers will be given movement based on the two-way for the benchmark security.
- If mid-point of two way is outside our threshold, we will poll from market participants for fair level for valuation for that particular ISIN

Step 6: Carry forward of spreads over the benchmark

- If there are no trades or no primary issuances for any state (other than benchmark) in any tenor, we would carry forward yesterday's spread over the benchmark states for the securities
- If there are no trades, no primary issuances for any benchmark state in any tenor, we would give movement of Benchmark G-sec for the tenor to all the SDL securities in that tenor.

Step 7: Polling

Market participants are polled in case:

- Trade is identified as outlier
- Spread review/ Client query

Polls are also taken into consideration on exceptional days including:

- Monetary Policies
- Annual Budget
- Quarter end days
- Policy announcements
- Macro-Economic data release days

Trades that qualify as per volume criteria

- Trades reported on NDS OM & NDS with minimum of one trade of volume 5 crore and above including odd lot and market lot qualify for daily G-sec valuations and
- Two-way quotes not wider than 5 bps considered for valuations and satisfies the volume criteria mentioned earlier (minimum bid and ask quantity of 5 crore and above) are considered. Mid-point of two-way quote is considered for valuation.

Special Papers:

- The Special papers are issued by state governments under the Ujwal Discom Assurance Yojana (UDAY) scheme to revive loss-making power distribution companies (discoms)
- Same waterfall steps are followed for valuation of Special Papers.
 - Spread between Special papers and Normal SDLs are reviewed at regular intervals.

Identification of SDL benchmark securities

Criteria used to determine SDL benchmarks:

- States are ranked based on liquidity.
- Total volume of trades (secondary market traded volume) is considered to rank states.

The states that obtain highest ranks (maximum secondary market volume) are taken into consideration for Benchmark selection. The final selection of benchmark states is done post obtaining feedback from market participants.

Quality check

- Review of valuations is done by secondary analyst. All changes over the previous day are reviewed.

Action taken in case of outlier trades

- Outlier definition +/- 5 bps Deviation in yield of traded security over and above the yield of the benchmark movement is classified as an outlier. Such trades shall be included in valuations post validation through polls.
- Outlier is checked on VWAY considering all transactions.

Governance mechanism

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- **Criteria Committee:** Valuation policy and any changes to such policies are discussed with the committee and are incorporated post approval by the committee.
- **Valuation Committee:** Matters pertaining to exceptions are discussed with valuation committee and acted upon based on its feedback. Exceptions may include any methodology changes, regulatory changes, market events impacting yields, etc.

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