15th Annual Report 2010-11

PNB GILTS LTD

Board of Directors

Shri K. R. Kamath
Chairman

Shri D.V.S.S.V. Prasad
Managing Director

Shri S.K. Dubey
Non-Executive Director

Dr. O. P. Chawla
Independent Director

Dr. Kamal Gupta
Independent Director

Shri S. K. Soni
Independent Director

Shri A. S. Agarwal
Independent Director

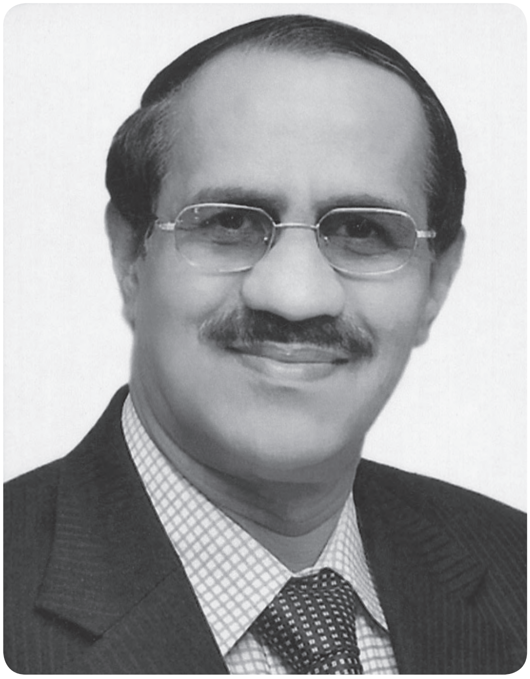
Shri M. S. Aftab
Independent Director

Shri P. P. Pareek
Independent Director

OUR MISSION

To be a leader in the
Primary Dealer Business
and
to be known as a Knowledge Based Research Oriented
&
Quality Conscious company maximising wealth for
Shareholders

CONTENTS



Chairman's Letter to Shareholders

Dear Shareholders,

I take this opportunity to thank you for the confidence reposed in the company over the years. Before presenting the annual results of the company for the year ended March 31, 2011, I would like to apprise you of the developments in the economy under which your company operated.

The year 2010-11 was characterized by consolidation of growth with the Indian economy registering a healthy growth of 8.60%. The growth was led by sharp rebound in agriculture output along with pick up in private consumption. Consolidation in growth gave the government enough room to read the path of fiscal consolidation. Substantial inflows of over a trillion rupees from 3-G and BWA auction along with robust tax revenues helped the government to cut its fiscal deficit to 5.1% from originally estimated 5.5%. However, inflationary pressures persisted throughout the year on account of high food prices despite having good monsoons. Food inflation remained a global phenomenon during the year with prices of essential food items shooting up sharply in many nations. The rise in purchasing power owing to the rapid growth of the economy partly contributed to the upward trend in inflation.

In FY 2010-11, stubbornly high inflation above the comfort level of RBI, together with growth buoyancy, necessitated that the monetary policy focus remains on containing inflation and inflationary expectations. Consequently repo and reverse repo rates were increased seven times during the fiscal by 175 basis points & 225 basis points respectively. The central bank revised its inflation projection for year end thrice during the year from 5.5% to 8% against which the actual inflation for March, 2011 stood at 8.98%.

With regard to the government securities market, heavy primary market supplies, successive policy rate hikes, extremely tight liquidity conditions and inflationary pressures weighed on the market. However factors such as hike in FII investment limit in G-securities & corporate bonds, OMO buyback purchases by the central bank and reduction in fiscal deficit projection for the next fiscal supported the market. 10-yr benchmark paper closed the year at 7.98% after touching a high and low of 8.23% and 7.38% respectively as against 7.85% as on March 31, 2010.

Company's performance during the year under review demonstrates its stability and strength despite operating in a highly uncertain environment. Company's profit stands at Rs. 44.04 crore as on March 31, 2011 as against Rs. 56.03 crore as on March 31, 2010. Company operated in a high cost environment with borrowing cost shooting up by more than 250 basis points during the year Nevertheless, despite company's interest expenses surging by 49% during the year, profit dropped by only 21%. The net worth of the company has risen by 2% to Rs. 568.92 crore as on March 31, 2011. Company traded aggressively during the period under review, which translated in to higher turnover and market share. Company's secondary market turnover jumped significantly to Rs. 68745 crore as against Rs. 48386 crore achieved in FY 2009-10.

Looking Forward

In the new fiscal, domestic debt market is expected to be pressurized by inflation and high crude oil prices. Further monetary tightening may be witnessed in continued battle with the persistent inflationary pressures. Nevertheless, likely support from RBI to Govt. borrowing program in form of OMO buyback auctions along with improvement in liquidity conditions may provide fillip to the market. In the new financial year, company would put in place strategies that will address the near term challenges and also look out for opportunities to strengthen its performance further. Company has recently recruited talented and experienced manpower who will assist in improving its performance further. In our pursuit to be at the forefront of the fixed income industry, I solicit your continued patronage and support.

With regards,
Yours Sincerely,

(K. R. Kamath)
Chairman

Date : May 13, 2011

DIRECTORS' REPORT

Your Directors have pleasure in presenting the Fifteenth Annual Report together with the audited accounts of the company for the year ended March 31, 2011.

1. FINANCIAL RESULTS

The financial results for the year ended March 31, 2011 along with comparative figures for the previous year are given below:

(Rs. in lacs)

	For the year ended 31.3.2011	For the year ended 31.3.2010
Total Income	**10321.28**	10172.94
Total Expenditure	**5916.88**	4569.66
Profit/(loss) Before Tax	**4404.40**	5603.28
Less : Provision for Income Tax (including deferred tax)	**1346.55**	1932.83
Profit /(loss) After Tax	**3057.85**	3670.45
Add: Balance in Profit & Loss Account brought forward	**5503.14**	4147.21
Amount available for Appropriation	**8560.99**	7817.66
Proposed Appropriations		
Transfer to Statutory Reserve	**612.00**	735.00
General Reserve	**77.00**	–
Proposed Dividend	**1620.09**	1350.08
Dividend Distribution Tax	**269.08**	229.44
Balance carried forward	**5982.82**	5503.14

The year 2010-11 was marked by the process of exit from the accommodative monetary policy stance with focus on containing inflation and inflationary expectations. As a result, during 2010-11, RBI raised the policy rates seven times, whereby the repo rate under LAF has cumulatively been increased by 175 basis points to 6.75 per cent and the reverse repo rate by 225 basis points to 5.75 per cent. The Cash Reserve Ratio (CRR) was, however, retained at 6 per cent. In tune with the tight monetary policy stance, the money market rates also hovered around the upper bound of the LAF corridor and the borrowing cost of the company accordingly went higher.

In the Govt securities market, monetary policy, inflation concerns and supply issues were the major factors influencing yields on govt securities. Initially, higher than budgeted collections from auctions of 3 G and BWA licences receded the concerns on fiscal deficit with yield on 10-year G-sec touching a low of 7.35 per cent in mid May from 7.85 per cent as on March 31, 2010. Improved sentiments were, however, offset by high inflation and tight monetary policy stance by RBI and the 10 -year yield rose to as high as 8.23 per cent in mid January before closing the year at 7.98 per cent as on March 31, 2011. Moreover, with consistently tight liquidity conditions prevailing almost throughout the year, the short term rates remained high resulting in a flat yield curve with spread between 1 year and 30 year security declining to 102 basis points from 300 basis points in the beginning of the year. Owing to tight liquidity conditions the borrowing cost remained high which hurt the net interest margin considerably.

Against the above backdrop of tight money market rates and firm G-sec yields, the Profit Before Tax of the company stood at Rs. 44.04 crore in 2010-11 as against Rs. 56.03 crore during FY 2009-10. While Profit After

Tax stands at Rs. 30.58 crore during FY 2010-11 as against Rs. 36.70 crore during FY 2009-10. The networth of the company stands at Rs. 568.92 crore as on March 31, 2011.

2. CAPITAL ADEQUACY

Capital adequacy ratio as on March 31, 2011 stood at 94.42 per cent as against the RBI stipulation of 15 per cent.

3. DIVIDEND

Your Board has recommended a final dividend of Rs. 1.20 per share for the financial year 2010-11 amounting to Rs. 1620.09 lakhs. The total outflow on account of said dividend shall be Rs. 1889.17 lakhs (including Dividend Distribution Tax).

4. OTHER MATTERS

4.1. Directors

During the year, the Board of Directors met five times to review strategic, operational, technological and financial matters besides laying down policies and procedures for operational management of the company against the required minimum of 4 meetings in a year. The Audit Committee of the Board met four times; the Share Transfer Committee met twenty four times and Shareholders' / Investors' Grievance Committee met twelve times.

Changes since last Annual General Meeting

The following changes took place in the Board of Directors of the company since last Annual General Meeting :

- **Sh. Nagesh Pydah**, Executive Director - Punjab National Bank, had resigned from Directorship of the company on his elevation as Chairman and Managing Director - Oriental Bank of Commerce.

Retirement of Directors by Rotation

As per Article 99 of the Articles of Association of the company, Dr. O. P. Chawla & Sh. P. P. Pareek shall retire by rotation in the forthcoming Annual General Meeting and are eligible for reappointment.

Corporate Governance

Corporate Governance for the company means achieving high level of accountability, efficiency, responsibility and fairness in all areas of operations. Our workforce is committed towards the protection of the interest of the stakeholders including shareholders, creditors, investors, customers, employees, etc. Our policies consistently undergo improvements keeping in mind our goal i.e. maximization of value of all the stakeholders. The Corporate Governance practices followed by the company are given in the Annual Report. A certificate from M/s S. Mohan & Co., Statutory Auditors of the company regarding compliance of conditions of corporate governance stipulated by stock exchanges is enclosed with the 'Report on Corporate Governance'.

4.2. Directors' Responsibility Statement

Pursuant to Section 217(2AA) of the Companies (Amendment) Act 2000, the Directors confirm that in the preparation of the annual accounts:

- The applicable accounting standards have been followed.

- Appropriate accounting policies have been selected and applied consistently, judgements and estimates made are reasonable and prudent so as to give true and fair view of the state of affairs of the company at the end of the financial year ended March 31, 2011 and the profit and loss account for the year ended March 31, 2011.
- Proper and sufficient care has been taken for the maintenance of adequate accounting records in accordance with the provisions of the Companies Act, 1956, for safeguarding the assets of the company and for preventing and detecting fraud and other irregularities.
- The annual accounts have been prepared on a going concern basis.

4.3. Audit, Internal Control Systems & their adequacy

M/s S. Mohan & Co., Chartered Accountants, Delhi were appointed as the Statutory Auditors of the company by the Comptroller & Auditor General of India for the financial year ended March 31, 2011. The report of the auditors is self-explanatory.

The company considers Internal Audit to be a very significant part of its corporate governance practices. For the year 2010-11, the Board appointed M/s Deloitte Haskins & Sells as the Internal Auditors of the company. The scope of Internal Audit included audit of treasury transactions on a monthly basis and reporting to the Audit Committee of the Board that the company has operated within the limits of various risk parameters laid down by the Board, Reserve Bank of India and other statutory authorities. Besides, they also audited and reviewed key business processes, including IT systems of the company, on quarterly basis. All the reports of the Internal Auditors were submitted to the Audit Committee and the monthly audit reports were submitted to Reserve Bank of India as well.

4.4. Human Resources

Total number of employees of the company as on March 31, 2011 was 36 (including 5 employees on deputation from parent bank). The company has maintained peaceful and harmonious relations with its employees.

The information required under Section 217 of the Companies Act, 1956 read with the Companies (Particulars of Employees) (Amendment) Rules, 2011 be treated as NIL as none of the employees of the company draws remuneration in excess of Rs 5,00,000 /- p.m. No employee is related to any Director of the company.

4.5. Particulars required to be furnished by the Companies (Disclosure of particulars in the report of the Board of Directors) Rules, 1988.

a) Part A pertaining to the conservation of energy are not applicable to the company.

With regard to Part B pertaining to technology absorption, the company has installed the integrated treasury management software and RBI's Negotiated Dealing System with the help of IDRBT and reputed IT companies. The company recognizes the growing importance of Information Technology in the emerging business environment. The company has also implemented Business Continuity Plan (BCP) and Disaster Recovery Plan (DRP) with the help of IDRBT (consultants for implementation of BCP and DRP) to identify and reduce risk exposures and proactively manage any contingencies.

b) Foreign Exchange earnings and outgoing:

The company has neither used nor earned any foreign exchange during the year under review.

4.6. Public Deposits

During the year ended March 31, 2011, the company has not accepted any deposits from the public within the meaning of the provisions of the Non- Banking Financial Companies (Reserve Bank) Directions, 1977 and RBI's notification no. DFC.118DG/(SPT)-98 dated 31st January 1998.

4.7. Acknowledgement

Your Directors thank Government of India, Reserve Bank of India, Securities and Exchange Board of India, National Stock Exchange Ltd., Bombay Stock Exchange Ltd., Punjab National Bank, Commercial, Cooperative & Regional Rural Banks, Financial Institutions, PF Trusts, Public Sector Undertakings and Private Sector Corporate Bodies and other valued clients for their whole-hearted support. We acknowledge the sincere and dedicated efforts put in by employees of the company at all levels.

On behalf of Board of Directors

Date : May 11, 2011
Place : New Delhi

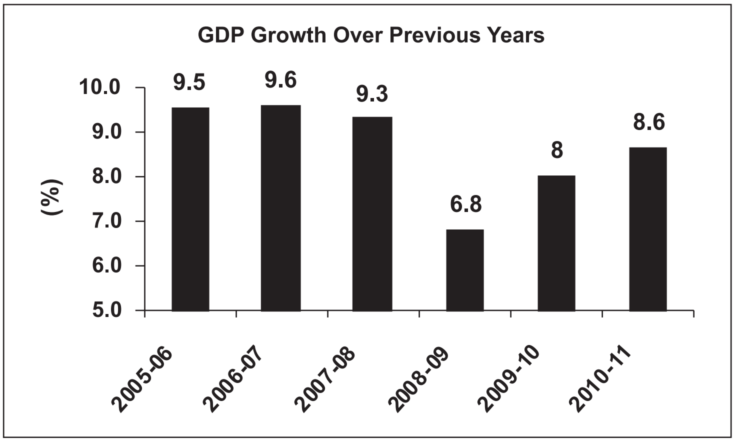
(K.R.Kamath)
Chairman

MANAGEMENT DISCUSSION AND ANALYSIS

MACROECONOMIC REVIEW

Gross Domestic Product

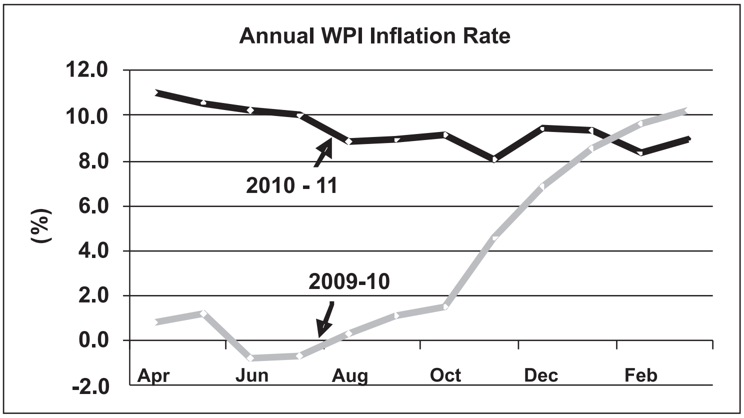
Robust growth and steady fiscal consolidation have been the hallmark of the Indian economy in the year 2010-11. GDP growth for FY 2010- 11 has been estimated at 8.6 per cent as against 8.0 per cent in the previous year. The growth is mainly driven by the rebound in agriculture and pick up in private consumption as employment prospects have improved and disposable income continues to rise. The growth has been broad based with a rebound in the agriculture sector which is expected to grow around 5.4 per cent. Manufacturing and Services sector too have registered impressive gains. However food inflation, higher commodity prices and volatility in global commodity markets have been a cause of concern underscoring the need of fiscal consolidation and stronger reserves.



On the demand side, a rise in savings and investments and pickup in private consumption have resulted in strong growth of GDP at constant market prices at 9.7 per cent in 2010-11. Good kharif output and higher rabi sowings suggest stronger contribution of the agriculture sector to overall GDP growth in 2010-11. The agriculture sector growth in the first four years of the 11th Plan (2007-12) is estimated at 2.87 per cent. The food grain production went up to 235.88 million tones from 218.1 million tones in 2009-10. The rising food inflation and the critical role of agriculture underline the need for a larger investment in agriculture enroute to the second green revolution. The industrial output growth rate was 8.6 per cent while the manufacturing sector registered a growth rate of 9.1 per cent in 2010-11.

International Trade and Debt

The exports during April-March 2011 went up by 37.5 per cent in dollar terms while the imports during the same period registered a growth rate of 21 per cent in dollar terms. Oil imports during April to March, 2011 were valued at USD 101.70 billion which was 16.7 per cent higher than oil imports of USD 87.14 billion in the corresponding period last fiscal. On the other hand non oil imports during similar period were valued at USD 249 billion which is 23.7 per cent higher than USD 201.24 billion in corresponding period last year. The trade deficit shrunk to USD 104.83 billion during April to March, 2011 from USD 109.62 billion during corresponding period of last fiscal.



Inflation

The year 2010-11 started off with headline inflation of 11.0 per cent in April 2010 in terms of Wholesale Price Index on the revised base year. After remaining in double digits till June 2010, inflation moderated to reach 8.93 per cent in September, 2010. In terms of consumer price