

In September 2008, Government of Gujarat directed all profit making state PSUs to contribute 30% of the pre-tax profits to newly formed Gujarat Socio-Economic Development Society (GSEDS) for welfare activities.

In spite of opposition from some, the heads of state PSUs have been ordered to get the approval from their board as well as shareholders for going ahead with the plan.

The approval of shareholders was necessary because of Section 293 (1) (e) of the Companies Act. Under this provision "a public company cannot, except with the consent of its members, contribute to charitable and other funds not directly relating to the business of the company or the welfare of its employees, any amounts the aggregate of which will, in any financial year, exceed Rs 50,000/- (Rupees Fifty Thousand only) or 5 percent of the company's average net profit, determined in accordance with Sections 349 and 350 during the three financial years immediately preceding, whichever is greater."

If all PSUs were to follow the government directive, then the six listed PSUs would have to cough up a total of over Rs 550 crore. The move could severely hit the dividend amount to be paid to shareholders.

All the contributions will be exempted under Section 35 AC of the IT Act and hence the actual impact would be much less than 30%. For example, under this approval, GMDC can contribute upto Rs 122.52 crore to GSEDS for projects approved by Central Board Of Direct Taxes. All the contributions will be exempted under Section 35 AC of the IT Act which would mean around Rs 40 crore benefits for GMDC. This means the actual impact is 20%.

It is pertinent to note that this was an "enabling" and not a binding proposal.

The Gujarat Mineral Development Corporation, or GMDC has approved it in spite of minority shareholders' disapproval, as Government of Gujarat controls 75% of the shareholding. Other PSUs where the government controls less than 50%, are likely to reject the move.

Gujarat Alkalies Ltd. and GNFC AGMs have already rejected the proposal.

Even, in case of GMDC, unhappy minority shareholders have appealed to the High Court against the move. All eyes are set on the outcome of the postal ballot issued by another Gujarat State Petronet Ltd (GSPL) where the state government controls close to 40% shareholding.

Stocks of these 5 PSUs fell like a nine pin on the back of these dictats. The timing of these announcements coupled with a broad market correction in the month of October, led to a larger than warranted decline in these stocks. We feel investors can relook at these stocks as the fall seems overdone. Government of Gujarat would be wary of forcing the company to make large contributions even if the boards pass the resolution, as it would be a sore example of bad corporate governance.

Name	GNFC	GSFC	GSPL	GACL	GMDC	GIPCL
Govt Holding	41.18	37.84	37.78	36.72	74	58.21
PBT	576.21	358.3	149.15	275.51	408.39	140.25
30% of PBT	172.863	107.49	44.745	82.653	122.517	42.075

GMDC – Already approved.

GNFC, GACL – Rejected the proposal.

GSFC, GSPL - Likely to reject.

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RATING INTERPRETATION

Buy Expected to appreciate more than 20% over a 12-month period

Accumulate Expected to appreciate up to 20% over a 12-month period

Hold Expected to remain in a narrow range

Avoid Expected to depreciate up to 10% over a 12-month period

Exit Expected to depreciate more than 10% over a 12-month period