

Press Release

01 March, 2017

A. K. Capital Finance Private Limited

Rating Assigned

Total Instruments Rated*	Rs.100.00 Cr
Long Term Rating	SMERA Provisional** AA (SO#)/Stable (Assigned)

*Refer Annexure for details

** The rating will be converted to a final rating after the:

i. Appointment of a SEBI Registered Trustee

ii. Execution of the Trust Deed with the proposed Structured Payment Mechanism (SPM) duly incorporated

#Credit Enhancement on account of presence first charge of Debenture Trustee over specific identified Investments/Receivables (i.e., Business Assets) of the Company

Rating Rationale

SMERA has assigned a rating of **SMERA Provisional AA (SO) (read as SMERA Provisional double A Structured Obligation)** to the Rs.100.00 crore Proposed Secured, Redeemable, Non-Convertible Debenture (NCD) issue of A. K. Capital Finance Private Limited (AKCFPL). The outlook is '**Stable**'.

AKCFPL is a NBFC-ND-SI engaged in the business of extending advances to high credit quality corporate borrowers and lending against highly rated securities AKCFPL is a subsidiary of A.K. Capital Services Limited (AKCSL) – a SEBI registered Merchant Bank.

List of key rating drivers and their detailed description

Strengths:

Presence of Structured Payment Mechanism (SPM): The rating is driven by the Structured Payment Mechanism (SPM) to be put in place by AKCFPL to ensure timely servicing of the interest and principal obligations. The proposed NCD issue shall be secured throughout its tenure by first Charge in favour of Debenture Trustees over specific identified Investments/Receivables (i.e. Business assets) of the Company ("Primary Security"). Primary Security shall include minimum 25 per cent primary security with credit rating category of AA or above; maximum 15 per cent primary security with credit rating category of A and above issued by central Public Sector Undertakings (PSUs), state PSUs, PSU Banks and urban local bodies including municipal bonds; and maximum 60 per cent of the primary security with credit rating category of A.

AKCFPL would be required to maintain a minimum 1.05x asset cover of principal at all times during the tenure of the NCDs.

The debenture trustee will be authorised to liquidate these 'Business Assets' in case the designated payment account is not funded by T-4 days for the coupon amount due on the forthcoming due date, T. The debenture trustee may invest the above amount temporarily in bank fixed deposits and would be responsible for timely availability of such funds on the due date, T. The rating centrally assumes adherence to the SPM by the debenture trustee and AKCFPL on an ongoing basis.

Healthy asset quality: AKCFPL's major earning assets constitute central government securities, highly rated corporate papers and advances to corporates. As on 31 March, 2016, around 67 per cent of AKCFPL's earning assets comprise Central Government Securities, AAA (triple A) & AA (double A) rated debt instruments. The balance comprised advances to borrowers with high credit quality or investment in their debt instruments.

AKCFPL has demonstrated ability to identify profitable lending opportunities which will help keep its asset quality healthy. AKCFPL reported nil gross non-performing assets over the last three financial years. Its prudent lending policies, robust risk management practices and strong market intelligence derived from its longstanding experience in the debt market will support its ability to scale up its operations while maintaining healthy asset quality.

Diversified funding profile: The rating draws support from AKCFPL's ability to mobilise financial resources from various financial institutions, capital markets and from the CBLO (Collateralized Borrowing and Lending Obligations) segment of the money market. As on 31 March, 2016, 47.78 per cent of the total borrowings were from the CBLO market against 54.00 per cent on 31 March, 2015.

AKCFPL's ability to raise funds from several sources has enabled the company to maintain low weighted average cost of funds (WACF) vis-à-vis its yield on advances/investments. The effective WACF stood at 7.55 per cent in FY2016 as compared to 10.44 per cent in FY2015.

The company avails working capital limits (against securities) and term loans from banks and financial institutions to fund its exposure in various corporates. AKCFPL's borrowing spreads across various tenures are based on the maturity profile of its earning assets. SMERA believes that AKCFPL's diverse funding profile will substantially support its ability to grow its AUM over the medium term.

Comfortable capitalisation and prudent capital structure: AKCFPL reported comfortable Capital Adequacy Ratio (CAR) of 39.98 per cent on 31 March, 2016 as compared to 78.99 per cent on 31 March, 2015. SMERA expects AKCFPL's credit risk profile to continue to be supported by its healthy net worth base of Rs. 353.49 crore on 31 March, 2016 as compared to Rs. 301.90 crore.

The increase in net worth is mainly on account of healthy internal accruals of the company coupled with equity infusion of Rs.30.00 cr by promoters in FY2015-16. Based on existing capitalisation levels, SMERA believes that AKCFPL has adequate flexibility to go in for additional borrowings to support any increase in AUM.

Weaknesses:

Susceptibility of performance to the debt segment of capital markets: AKCFPL has an established track record in the debt capital market. Its performance is linked to the demand for credit by corporates which in turn is dependent on the level of economic activity. Hence, AKCFPL's performance is largely influenced by economic cyclical and other macroeconomic factors like GDP growth rate, inflation and expected movement in interest rates. Adverse events such as sharp spike in inflationary pressures or hardening of interest rates could translate into muted credit offtake, thereby translating into lower transaction volumes for AKCFPL.

AKCFPL's Assets Under Management (AUM) (including current investments, non-current investment, loans & advances and inventory of debt securities) increased to Rs. 1515.65 cr on 31 March, 2016 from Rs. 914.96 cr on 31 March, 2015. However, most of the increase in AUM was in the second half of FY2016 primarily due to subdued corporate debt offtake on account of volatility in debt markets. This translated into a decline in Return on Average Assets (RoAA) to 1.72 per cent in FY2016 from 2.47 per cent in FY2015. For the six months ended 30th September, 2016, AKCFPL reported a RoAA of 2.23 per cent.

AKCFPL has traditionally focused on safe lending segments such as lending against highly rated corporate papers and government securities and fully collateralised loans. Since the yield on advances against high rated debt instruments are typically lower for the company, going forward, AKCFPL plans to increase its focus on providing financial assistance to corporates by investing in their NCDs and extending advances against other tangible securities. While the risk involved in such transactions is

relatively higher, this is expected to result in higher yields and lower dependence of AKCFPL on lending against debt instruments for its earnings.

The government has been focusing on deepening of corporate debt markets and reducing the dependence of corporate borrowers on the banking system. The deepening of the corporate debt market is expected to augur well for players like AKCFPL – who are primarily focused on the debt market segment.

Risks inherent in the wholesale lending business: AKCFPL has been lending mainly to high quality corporates against highly rated securities. Top 20 clients accounted for 95 per cent of its exposure as on 31 March, 2016. While AKCFPL has been following prudent risk management practices with respect to lending, collateral events like deterioration in credit quality of borrowers and decline in security prices can impact its performance with regard to its asset quality and earnings profile.

SMERA believes that AKCFPL will continue to be influenced by the risks emanating from the high degree of concentration in its portfolio. Its ability to diversify its exposure across borrowers while maintaining asset quality shall be a key rating sensitivity factor.

Analytical approach: SMERA has taken a standalone view of the above entity.

Applicable Criteria

- Non-Banking Finance Entities: <https://www.smera.in/criteria-nbfc.htm>
- Default Recognition: <https://www.smera.in/criteria-default.htm>
- Policy on Provisional Ratings: <https://www.smera.in/provisional-ratings.htm>

Outlook: Stable

SMERA believes that AKCFPL will maintain a stable outlook owing to the structured payment mechanism, healthy asset quality, comfortable earnings and capitalisation level. The outlook may be revised to 'Positive' in case of significant and higher than expected growth in its earnings assets and margins while maintaining its asset quality. Conversely, the outlook may be revised to 'Negative' in case of significant deterioration in its profitability margins or increased exposure to high assets risk segments.

About the Rated Entity

AKCFPL – a Mumbai based NBFC-ND-SI, formerly known as Girdhar Vanijya Private Limited, was incorporated in 2006 and was acquired by A.K. Capital Services Limited (AKCSL) in 2008. AKCFPL was promoted by Mr. A.K. Mittal. The company is engaged in the financing of corporates through NCDs, direct advances and lending against high quality paper. It is a subsidiary of AKCSL – a SEBI registered Merchant Bank.

The company reported net profit of Rs.21.60 cr on operating income of Rs.118.48 cr in FY2015-16, as compared with net profit of Rs.21.07 crore on an Operating income of Rs.104.06 cr in FY2014-15.

Status of non-cooperation with previous CRA (if applicable): Not Applicable

Any other information: N.A.

Rating History for the last three years:

Name of Instruments	FY2017			FY2016		FY2015		FY2014	
	Scale	Amount (Rs. Crore)	Rating with Outlook	Date	Rating	Date	Rating	Date	Rating
Proposed Secured, Redeemable Non-Convertible Debentures	LT	100.00	SMERA Provisional** AA (SO#)/Stable	-	-	-	-	-	-

***Annexure – Details of instruments rated:**

Name of the Facilities	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. Crore)	Ratings/Outlook
Proposed Secured, Redeemable Non-Convertible Debentures	N.A	N.A	N.A	100.00	SMERA Provisional** AA (SO#)/Stable

Note on complexity levels of the rated instrument:
<https://www.smera.in/criteria-complexity-levels.htm>
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ABOUT SMERA

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