Press Release

A. K. Capital Finance Private Limited (AKCFPL)

21 June, 2017

Rating Assigned

Total Instruments Rated*	Rs. 250.00 Cr
Long Term Ratings	SMERA Provisional** AA (SO$)/Stable (Assigned and Reaffirmed)

**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 of a Debt Service Reserve Account (DSRA) equivalent to a minimum of 15 per cent of the principal amount outstanding on the NCD in the form of Bank Fixed Deposits, "AAA" Rated Liquid Bonds, bank guarantee, in any combination

Rating Rationale

SMERA has assigned 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 Issue of AKCFPL. The outlook is **'Stable'**.

SMERA has also reaffirmed the rating of **SMERA Provisional AA (SO) (read as SMERA Provisional Double A (Structured Obligation))** assigned to the Rs. 150.00 cr Proposed Secured Redeemable Non-Convertible Debenture Issue by AKCFPL. The outlook is **'Stable'.**

SMERA also has an outstanding rating of **SMERA AA (SO) (read as SMERA double A (Structured Obligation))** on the Rs. 200.00 cr Secured Redeemable Non-Convertible Debenture Issue by AKCFPL. The outlook is **'Stable'**.

AKCFPL is a (Non-Banking Financial Company - Systemically Important Non-Deposit) NBFC-ND-SI engaged in the business of extending advances to corporate borrowers with high credit quality 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 interest and principal obligations.

The proposed NCD issue aggregating Rs. 250.00 crore shall be secured throughout its tenure by the presence of a Debt Service Reserve Account (DSRA) equivalent to 15 per cent of the principal amount outstanding of the NCDs in the form of Bank Fixed Deposits, "AAA" Rated Liquid Bonds, bank guarantee, in any combination. AKCFPL will also be required to maintain a minimum asset cover of 1.05 times at all times during the currency of the NCD.

The debenture trustee will be authorised to liquidate the DSRA or invoke the bank guarantee in case the designated payment account is not funded by T-1 days for the coupon amount due on the forthcoming due date, T in case of a bank fixed deposit; T-2 days in case of a bank guarantee and T-3 days in case of

'AAA' rated liquid bonds. 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.

In case the DSRA is utilised in full or part or the value of the DSRA is diminished below the minimum required, AKCFPL will be required to replenish the same within seven days of the occurrence of such an event. 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, 2017, a significant portion of AKCFPL's earning assets comprised 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 (Collateralised Borrowing and Lending Obligations) segment of the money market. As on 31 March, 2017, 36.71 per cent of the total borrowings were from the CBLO market and from Repo Transactions against 47.78 per cent on 31 March, 2016.

AKCFPL's ability to raise funds from several sources has enabled the company to maintain a low weighted average cost of funds (WACF) vis-à-vis its yield on advances/investments. The effective WACF stood at 5.84 per cent in FY2017 as compared to 7.55 per cent in FY2016.

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 34.24 per cent as compared to 39.98 per cent on 31 March, 2016. SMERA expects AKCFPL's credit risk profile to continue to be supported by its healthy net worth base of Rs. 406.08 crore as against Rs. 353.49 crore on 31 March, 2016.

The increase in networth is mainly on account of healthy internal accruals of the company coupled with equity infusion of approximately Rs.20.00 crore by promoters in FY2016-17. Based on existing capitalisation levels, SMERA believes that AKCFPL has adequate flexibility to go in for additional borrowings to support increase in AUM. SMERA expects AKCFPL's net debt to networth ratio to remain comfortable at under four times for the year ended 31 March, 2018.

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 cyclicality 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. 1,982.84 cr on 31 March, 2017 from Rs. 1515.65 cr as on 31 March, 2016.

AKCFPL has traditionally focused on low risk segments such as lending against highly rated corporate papers, government securities and fully collateralised loans. Since the yields 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 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. It's top 20 clients accounted for 30 per cent of its exposure as on 31 March, 2017. 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 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. The standalone rating has been notched up on account of the credit enhancement in the form a DSRA equivalent to 15 per cent of the principal amount outstanding on the NCD.

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 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.31.09 crore on operating income of Rs.153.62 cr in FY2016–17, as compared with net profit of Rs.21.60 crore on an Operating income of Rs. 118.47 cr in FY2015–16.

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

Any other information: NA

Rating History for the last three years:

Name of Instrument /Facilities	FY2018 (Current)			FY2018		FY2017		FY2016	
	Scale	Amount (Rs. Crore)	Rating with Outlook	Date	Rating	Date	Rating	Date	Rating
Proposed Secured Redeemable Non-Convertible Debentures	LT	150.00	SMERA Provisional AA (SO)/Stable (Reaffirmed)	31 May, 2017	SMERA Provisional AA (SO)/Stable (Assigned)	-	-	-	-
Proposed Secured Redeemable Non-Convertible Debentures	LT	100.00	SMERA Provisional AA (SO)/Stable (Assigned)	-	-	-	-	-	-

***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.	150.00	SMERA Provisional AA (SO)/Stable (Reaffirmed)
Proposed Secured Redeemable Non-Convertible Debentures	N.A	N.A	N.A.	100.00	SMERA Provisional AA (SO)/Stable (Assigned)

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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