

Press Release

A. K. Capital Finance Private Limited (AKCFPL)

22 June, 2017

Rating Assigned and Reaffirmed



Total Instruments Rated*	Rs. 200.00 Cr
Long Term Ratings	SMERA AA (SO#)/Stable (Assigned)

**Refer Annexure for details*

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 converted the provisional rating assigned to the NCD issue aggregating Rs. 200.00 crore of A.K. Capital Finance Private Limited (AKCFPL) to final rating of **SMERA AA (SO) (read as SMERA double A (Structured Obligation))**. The outlook is **'Stable'**. The conversion of the rating from a provisional rating to a final rating reflects the fulfilment of the criteria laid out by SMERA in its press release dated 8th March, 2017.

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 NCD issue aggregating Rs. 200.00 crore 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 a 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, 2017, a significant portion of AKCFPL's earning assets consisted of Central Government Securities, AAA (triple A) and AA (double A) rated debt instruments. The balance constitutes 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 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 - the capital market and CBLO (Collateralised Borrowing and Lending Obligations) segment of the money market. As on 31 March, 2017, 36.71 per cent of total borrowings were from the CBLO market and 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 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 borrowings spread across various tenures and 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 cyclicity 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 and advances and inventory of debt securities) increased to Rs. 1,982.84 crore as on 31 March, 2017 from Rs. 1515.65 crore 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 yield 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. 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 of 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 asset quality. Conversely, the outlook may be revised to 'Negative' in case of significant deterioration in 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 crore in FY2016–17, as compared with net profit of Rs.21.60 crore on operating income of Rs. 118.47 crore 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
Secured Redeemable Non-Convertible Debentures	LT	100.00	SMERA AA (SO)/Stable (Assigned)	-	-	08 Mar, 2017	SMERA Provisional AA (SO)/Stable (Reaffirmed)	01 Mar, 2017	SMERA Provisional AA (SO)/Stable (Assigned)
Secured Redeemable Non-Convertible Debentures	LT	100.00	SMERA AA (SO)/Stable (Assigned)	-	-	08 Mar, 2017	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
Secured Redeemable Non-Convertible Debentures	09/03/2017	9.40	09/09/2021	20.00	SMERA AA (SO)/Stable (Assigned)
Secured Redeemable Non-Convertible Debentures	07/03/2017	9.60	07/03/2024	25.00	SMERA AA (SO)/Stable (Assigned)
Secured Redeemable Non-Convertible Debentures	09/03/2017	9.60	09/03/2024	26.00	SMERA AA (SO)/Stable (Assigned)
Secured Redeemable Non-Convertible Debentures	07/03/2017	9.70	07/03/2027	5.00	SMERA AA (SO)/Stable (Assigned)
Secured Redeemable Non-Convertible Debentures	20/03/2017	9.50	20/03/2022	2.00	SMERA AA (SO)/Stable (Assigned)
Secured Redeemable Non-Convertible Debentures	20/03/2017	9.60	20/03/2024	5.00	SMERA AA (SO)/Stable (Assigned)
Secured Redeemable Non-Convertible Debentures	21/03/2017	9.60	21/03/2024	15.00	SMERA AA (SO)/Stable (Assigned)
Proposed Secured Redeemable Non-Convertible Debentures	N.A	N.A	N.A.	2.00	SMERA AA (SO)/Stable (Assigned)
Proposed Secured Redeemable Non-Convertible Debentures	N.A	N.A	N.A.	100.00	SMERA AA (SO)/Stable (Assigned)

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

Contacts:

Analytical	Rating Desk
Vinayak Nayak, Head – Ratings Operations, Tel: 022-67141190 Email: vinayak.nayak@smera.in Arindam Som, Rating Analyst, Tel: 011-49731321 Email: arindam.som@smera.in	Varsha Bist Manager Tel: 022-67141160 Email: varsha.bist@smera.in

ABOUT SMERA

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