

Press Release

Federal Operations and Services Limited

June 14, 2022



Rating Reaffirmed

Product	Quantum (Rs. Cr)	Long Term Rating	Short Term Rating
Non-Convertible Preference Shares	5.00	ACUITE A+ Stable Reaffirmed	-
Total Outstanding Quantum (Rs. Cr)	5.00	-	-
Total Withdrawn Quantum (Rs. Cr)	0.00	-	-

Rating Rationale

Acuite has reaffirmed the long-term rating of '**ACUITE A+**' (read as **ACUITE A plus**) on the Rs. 5.00 Cr. Non-Convertible Preference Shares of Federal Operations And Services Limited (FOSL). The outlook is 'Stable'.

The rating reaffirmation is on the account of continuous improvement in the operating metrics marked by FOSL's operating income which has increased to Rs. 42.67 Cr in FY2022 as against Rs.26.38 Cr. in FY2021 and Rs.18.95 Cr. in FY2020. This improvement was driven by FOSL's performance in migration of certain identified processes from The Federal Bank Limited (FBL) to FOSL. As on March 31, 2022, FOSL has taken over 109 activities as against 87 activities as on March 31, 2021 and 78 activities as on June 30, 2020, out of 150 activities identified from the 8 major heads of activities approved by RBI. The rating also derives strength from FOSL's strong parentage (Federal Bank Limited., FBL, holds 99.99% stake in FOSL), demonstrated capital support and expectations of continued support going forward.

About the company

FOSL was incorporated in October, 2018 as a wholly owned subsidiary of Kerala based private sector bank, The Federal Bank Limited (FBL). FOSL was established with intent to streamline the operational and technology driven services of FBL, in line with best global practices. It works as a back office processing unit for FBL. Currently, FOSL is handling 109 activities out of the total 150 approved activities. FOSL's operating facilities located at Kochi (Kerala) and Vizag (Andhra Pradesh).

About the Group

FBL is a Kerala based private sector bank founded in 1931. The bank has a network of 1282 branches in India and abroad and 1945 ATMs and cash recyclers as on March 31, 2022. It has a networth of Rs. 19, 255.52 Cr. as on March 31, 2022. The bank has aggregate deposits of Rs. 1.82 trillion and advances of Rs. 1.45 trillion as on March 31, 2022 as against Rs. 1.73 trillion and advances of Rs. 1.35 trillion as on March 31, 2021. FBL registered a net profit of Rs. 1.965.40 Cr. on a total income of Rs. 16,502.47 Cr. in FY2022 as compared to Rs. 1647 Cr. on a total income of Rs. 16,272 Cr. in FY2021. The bank is listed on BSE and NSE with a Market capitalization of Rs. 19.315 Cr as on June 02, 2022.

Analytical Approach

Acuité has considered the standalone business and financial risk profile of FOSL and has notched-up the standalone rating to factor in the expectation of support from The Federal Bank Limited (FBL). The rating of FBL is central to the rating of FOSL and will remain a key monitorable.

Standalone Unsupported Rating

ACUITE BB+/Stable

Key Rating Drivers

Strength

- **Improving financial performance along with benefits emanating from parentage of Federal Bank**

FOSL was incorporated in October 2018 as a wholly owned subsidiary of FBL. FOSL is strategically important to FBL and is significantly aligned to FBL's banking operations. Around 150 activities identified from the 8 major heads of activities approved by FBL which can be outsourced to FOSL. These activities include Contact Center, Account opening and Trade Finance activities. As on March 31, 2022, FOSL is handling 109 activities as against 87 activities as on March 31, 2021 and 78 activities as on June 30, 2020. It operates as a captive vehicle for FBL and is required to maintain exclusivity with FBL. It operates from its two offices located in Kochi and Vizag. The financial performance of FOSL witnessed improvement in terms of increase in revenue by 62% to Rs. 42.67 Cr in FY2022 over Rs. 26.38 Cr in FY2021. Net profitability margin has also increased to 8.10 percent in FY2022 against 6.96 percent in FY2021. Increase in the financial performance is on the account of acquiring more and more activities from FOSL in every year. FOSL has target to acquire all remaining activities by FY2023. In line with the increase in its scale of operations FOSL is also gradually increasing its workforce. As per the arrangement with FBL, FOSL carries out several activities which are considered important from a customer service standpoint. Since the operational risks in banking are significantly high, FBL maintains considerable oversight on the operations of FOSL. FOSL has integrated with the bank's tech platform and aids the bank in improving its operating efficiency through lower costs of operations and better productivity. The Board of Directors of FOSL comprises nominees from FBL and experienced professionals. Mr. A P Hota, Independent Director of FBL, is the Chairman and Director of FOSL. Besides the managerial support, FBL has infused funds by way of equity and preference shares to support the business operation of FOSL. The company's operations are managed by Mr Prashant Preman, President and Whole time Executive Director. He has been associated with FedServ since August 2019. He has been appointed as Whole Time Director (as Key Managerial Personnel) of FedServ w.e.f. 16th April 2021. Mr. Prashant has been key to FedServ in setting up and rolling out successful Long term & short-term Strategic programs and successfully reengineering of various operations including consumer asset products including ATM's, Debit Cards, Contact center operations, CASA & KYC operations, Trade Finance Operations, and various other activities. FOSL has also support from other key employees of FBL who are assisting in smooth migration of systems to FOSL. Acuité believes that FOSL shall continue to derive significant benefits from FBL and augment its scale of operations through gradual migration of the processes as envisaged under their mutual arrangement. The continued support and ownership of FOSL by FBL will be central to the rating.

Weakness

• Initial stage of operations; Susceptible to operational and regulatory risks

Since FOSL was incorporated in 2018, it is in its initial stage of operations. Though the plan of activities migration is going as planned. The gradual take-over of activities by FOSL is done in close co-ordination with the employees of FOSL. Around 150 activities identified from the 8 major heads of activities approved by RBI, out of which 109 activities have been migrated as of 31 March 2022 from FBL to FOSL. The operations of FOSL are dependent on FBL's systems and data bases, which exposes FOSL to operational risks. The risks are expected to multiply once additional processes get added in FOSL's portfolio. Hence, continuous management of operational risks is crucial for smooth running of this arrangement. Besides operational risks the growth trajectory of FOSL will also depend on the regulatory environment. Any changes in the regulatory framework restricting/curtailing banks from outsourcing their activities will impinge on the performance of FOSL. Acuité believes that the success of FOSL's business model will depend on its ability to manage the various operational and enhance its linkages with FBL within the regulatory paradigm.

Rating Sensitivity

- Support and ownership of FBL
- Regulatory framework in respect of outsourcing of activities
- Event risks in respect of Operational risks

Material Covenants

None

Liquidity Position

Adequate

As on March 31, 2022, FOSL had no external borrowings. The company is expected to be adequately supported by FBL for its working capital requirements as and when necessary.

Outlook:

Acuité believes that FOSL will maintain 'Stable' outlook over the medium term owing to its strong association and linkages with FBL. The outlook may be revised to 'Positive' if the company scales up operations by taking over more operations thereby increasing its linkage to FBL. Conversely, the outlook may be revised to 'Negative' if FOSL faces significant challenges in scaling up of operations or in case of sharp adverse changes in the credit profile of FBL.

Key Financials - Standalone / Originator

Particulars	Unit	FY22 (Actual)	FY21 (Actual)
Operating Income	Rs. Cr.	42.67	26.38
PAT	Rs. Cr.	3.46	1.84
PAT Margin	%	8.1	6.96
Total Debt/Tangible Net Worth	Times	0.45	0.65
PBDIT/Interest	Times	-	-

Status of non-cooperation with previous CRA (if applicable):

Not Applicable

Any other information

Not Applicable

Applicable Criteria

- Application Of Financial Ratios And Adjustments: <https://www.acuite.in/view-rating-criteria-53.htm>
- Default Recognition: <https://www.acuite.in/view-rating-criteria-52.htm>
- Group And Parent Support: <https://www.acuite.in/view-rating-criteria-47.htm>
- Service Sector: <https://www.acuite.in/view-rating-criteria-50.htm>

Note on complexity levels of the rated instrument

<https://www.acuite.in/view-rating-criteria-55.htm>

Rating History

Date	Name of Instruments/Facilities	Term	Amount (Rs. Cr)	Rating/Outlook
18 Jun 2021	Preference Shares	Long Term	5.00	ACUITE A+ Stable (Reaffirmed)
09 Jul 2020	Preference Shares	Long Term	5.00	ACUITE A+ Stable (Upgraded from ACUITE A Stable)
31 Jul 2019	Preference Shares	Long Term	5.00	ACUITE A Stable (Assigned)

Annexure - Details of instruments rated

Lender's Name	ISIN	Facilities	Date Of Issuance	Coupon Rate	Maturity Date	Quantum (Rs. Cr.)	Rating
Not Applicable	Not Applicable	Non-Convertible Preference Shares	14-11-2019	8.5	13-11-2029	5.00	ACUITE A+ Stable Reaffirmed

Contacts

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About Acuité Ratings & Research

Acuité is a full-service Credit Rating Agency registered with the Securities & Exchange Board of India (SEBI). The company received RBI Accreditation as an External Credit Assessment Institution (ECAI) for Bank Loan Ratings under BASEL-II norms in the year 2012. Acuité has assigned ratings to various securities, debt instruments and bank facilities of entities spread across the country and across a wide cross section of industries. It has its Registered and Head Office in Kanjurmarg, Mumbai.

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