

## Press Release

### Karnataka Water And Sanitation Pooled Fund Trust

January 31, 2020

#### Rating Assigned



<b>Total Bank Facilities Rated*</b>	Rs.414.98 Cr.
<b>Long Term Rating</b>	ACUITE AA- (CE)/ Outlook: Stable

\* Refer Annexure for details

#### Rating Rationale

Acuité has assigned its long-term rating of '**ACUITE AA-(CE)**' (read as **ACUITE double A minus (Credit Enhancement)**) on the Rs.414.98 Cr proposed bank facilities of KARNATAKA WATER AND SANITATION POOLED FUND TRUST (KWSPF). The outlook is '**Stable**'.

KWSPF was constituted by the GoK (Government of Karnataka) as a trust under the Indian Trusts Act, 1882, through a Deed of Trust executed on 12th Sept. 2003 and is managed by the Karnataka Urban Infrastructure Development & Finance Corporation (KUIDFC), a GoK entity. KWSPF aims to mobilize financial resources for urban infrastructure development in Karnataka. It raises funds through tax-free municipal bonds and bank loans under the Chief Minister's Small and Medium Towns Development Programme (CMSMTDP) and Nagarothana Programme for lending to urban local bodies (ULBs) through the Directorate of Municipal Administration (DMA) for implementation of urban infrastructure projects.

KWSPF lends to projects undertaken by ULBs, statutory bodies and public sector undertakings. It raises funds on a pooled basis and provides credit enhancement to reduce the funding cost.

#### Standalone (Unsupported) Rating: '**ACUITE A**'

#### Analytical Approach

Acuité has considered the standalone business and financial risk profiles of KWSPF and has in addition, factored in support extended by GoK (through an unconditional and irrevocable guarantee) as well as the presence of a Structured Payment Mechanism facilitated via an escrow account while arriving at the rating.

#### Key Rating Drivers

##### Strengths

##### • Structured payment mechanism with a shortfall undertaking by Government of Karnataka (GoK)

The State Finance Commission (SFC) Grants are allocated in the Budget every financial year to each ULB. These grants get released quarterly as Tied and Untied Grants. Tied Grants are released directly by GoK for committed payments like repayment of loans, salaries, rent, utility, bills, etc. The Untied Grants are released through DMA/Deputy Commissioners of Districts for their respective planned expenses. The GoK unconditionally and irrevocably undertaken to:

- I. Make a budgetary allocation on an annual basis for timely and full repayment of principal and interest with respect to the servicing of the loan during the entire tenure under the Global Protection component of the SFC devolutions.
- II. Transfer adequate funds for repayment into the escrow account of the KWSPF Trust at least five working days prior to the due date.
- III. Upon receipt of an intimation from the Lender/KWSPF, the GoK will without demur make good any shortfall in the escrow account (for repayment) at least one working day prior to the due date.
- IV. Amount indicated by the Lender / KWSPF shall be final and binding on the GoK.
- V. The obligation of the GoK under the GO will rank pari-passu to any other commitment of the GoK, which relates to the deduction by the GoK from the SFC devolution. The commitment of the GoK is valid till any amount is outstanding under the term loans.
- VI. The government order shall form part of the documentation related to the term loans.

Acuité believes that the shortfall undertaking is backed by budgetary support and a well-defined structured obligation from the GoK is similar to a guarantee. The adherence to the structured payment mechanism, however will be a key rating sensitivity factor.

#### • **Tripartite Agreement**

A tripartite agreement would be executed between KWSPF, GoK and the lenders in line with the transaction structure. The Trust will open an escrow account before the disbursal of term loan specifically to fulfil the debt obligations and any withdrawals from the account will require lenders' approvals. KWSPF proposes to avail disbursement of the term loan of Rs. 414.98 Cr in two tranches; first tranche to be availed in FY2019-20 of Rs.200 Cr and second tranche of Rs.214.98 Cr is likely to be availed in FY 2020-21.

#### • **Strategic role of KWSPF for GoK**

KWSPF lends to projects undertaken by ULBs, statutory bodies and public sector undertakings. It raises resources on a pooled basis and provides new credit enhancement to avail debt at a lower cost. It also acts as a nodal agency on behalf of the central and state government. KWSPF in the past has, raised tax free bond amounting to Rs. 100.00 Cr to provide Water Supply and Drainage to surrounding 8 ULBs around under Greater Bangalore Water and Sanitation Project (GBWASP) scheme, Bengaluru through Bangalore Water Supply and Sewerage Board. KWSPF has also raised resources for Government of Karnataka to implement schemes such as Chief Minister's Small and Medium Town Development Programme (CMSMTDP) Phase-I and Phase-II and Chief Minister's Special Grants of Rs.100 Cr each to City Corporations under Nagarothana Scheme in Phase-II and Phase-III. KWSPF in total has raised an amount of Rs.2,766.80 Cr through loans for these schemes up to December 2019. All these debts are supported by GoK. Acuite therefore believes that KWSPF is of strategic importance to GoK given its objective to avail low cost funds by mobilizing resources for Urban Infrastructure Projects besides acting as a Nodal Agency on behalf of the central and state government.

#### • **Healthy fiscal profile of Government of Karnataka**

The state of Karnataka has one of the healthiest fiscal profiles amongst all other states of India. Karnataka leads in social development while simultaneously maintaining a strong fiscal profile. This is notwithstanding the Rs. 8,165 Cr farm-loan waivers announced in the 2018-19 State budget. Karnataka's entrepreneurial private sector particularly in information technology and the commitment of successive governments to adhere to fiscal prudence despite being prone to agrarian crisis have resulted in the State being the preferred destination for private sector investments in India. It has demonstrated a strong ability to attract investments from foreign as well as domestic companies. With an overall GDP growth of 56.2 per cent and a per capita GDP growth of 43.9 per cent in the last decade, Karnataka surpassed all other states in India, pushing Karnataka's per capita income in Indian Rupee terms to sixth place. Acuite believes that Government of Karnataka will maintain its fiscal position in near to medium term given its fairly diversified revenue streams and its economic infrastructure as compared to other states of India.

### **Weaknesses**

#### • **Subject to changes in fiscal profile of Karnataka**

KWSPF's rating is driven by continued support from GoK. Hence the fiscal profile of Karnataka will be a key rating sensitivity factor. Any significant changes in the rating of GoK due to factors such as prolonged slowdown in the industrial or services sector or challenges faced by Karnataka for factors such as socio-economic changes or other such events can have impact in its fiscal indicators. The trust is however, solely dependent on the SFC devolution, which limits the resources available for its own revenue apart from nominal interest earnings on deposits. This leads to high reliance on GoK for timely servicing of the debt obligations. Further, timely budget allocation and timely receipt of revenue and capital grants from GoK for servicing the debt obligations is another rating sensitivity factor.

#### **Rating Sensitivities**

- Fiscal profile of GoK
- Structured payment mechanism and shortfall undertaking by GoK

#### **Material Covenants**

None

#### **Liquidity: Adequate**

KWSPF has adequate liquidity drawn from the support from the Government of Karnataka (GoK) and grants from State Finance Commission (SFC). The SFC devolution would be deducted from source and deposited in the respective escrow accounts at least 5 days prior to the due date of payments with respect to the structured payment mechanism of the term loan. Moreover, all withdrawals from the respective escrow accounts would exclusively be limited only to payment of principal and interest to the lender and for making investments. Moreover, GoK will transfer the required amount in the escrow account one day prior to the due date, in case of any shortage in the adjustment from SFC devolution from the budgetary allocation for

the debt servicing of the term loan. Given such a structure, Acuite expects that adequate balances will be maintained in the designated escrow account at all points in time to service the rated debt in a timely manner.

#### Outlook: Stable

Acuite believes that the outlook on KWSPF will remain 'Stable' on account of strong support from GoK driven by both strategic importance and moral obligation. The outlook may be revised to 'Positive' in case of any improvement in the fiscal profile of the state government. Conversely, the outlook may be revised to 'Negative' in case of any deterioration in the fiscal position of GoK and/or any weakness in the performance of the structured payment mechanism.

#### About the Rated Entity - Key Financials

	Unit	FY19 (Actual)	FY18 (Actual)
Operating Income	Rs. Cr.	99.39	95.32
PAT	Rs. Cr.	2.13	0.74
PAT Margin	(%)	2.14	0.78
Total Debt/Tangible Net Worth	Times	68.51	51.96
PBDIT/Interest	Times	1.02	1.01

#### Government of Karnataka Financials:

	Unit	FY2018-19 (RE)	FY2017-18 (Actual)
Total Receipts	Rs. Cr.	213,734	172,262
Total Expenditure	Rs. Cr.	218,488	186,510
Revenue Deficit	Rs. Cr.	-181	-4,518
Fiscal Deficit	Rs. Cr.	40,753	31,101
Debt/GSDP	%	2.89	2.37

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

None

#### Any other information

None

#### Applicable Criteria

- Default Recognition - <https://www.acuite.in/view-rating-criteria-52.htm>
- Financial Ratios and Adjustments - <https://www.acuite.in/view-rating-criteria-53.htm>
- Service Entities - <https://www.acuite.in/view-rating-criteria-50.htm>
- Infrastructure Entities - <https://www.acuite.in/view-rating-criteria-51.htm>
- State Government Support - <https://www.acuite.in/view-rating-criteria-26.htm>
- Credit Enhancement - <https://www.acuite.in/view-rating-criteria-49.htm>

#### Note on complexity levels of the rated instrument

<https://www.acuite.in/criteria-complexity-levels.htm>

#### Rating History (Upto last three years)

Not Applicable

#### \*Annexure – Details of instruments rated

Name of the Facilities	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. Cr.)	Ratings/Outlook
Proposed Term Loan	Not Applicable	Not Applicable	Not Applicable	414.98	ACUITE AA-(CE) /Stable

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### About Acuite Ratings & Research:

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