

Press Release

Karnataka Water and Sanitation Pooled Fund Trust

May 05, 2021

Rating Reaffirmed



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

* Refer Annexure for details

Rating Rationale

Acuite has reaffirmed its long term rating of '**ACUITE AA-(CE)**' (read as **ACUITE double A minus (Credit Enhancement)**) on the Rs. 414.98 Cr bank facilities of Karnataka Water and Sanitation Pooled Fund Trust (KWSPF). The outlook is '**Stable**'.

The rating continues to take into account the strategic role of KWSPF's in urban water supply and sanitation projects in Karnataka and the shortfall undertaking from the Government of Karnataka (GoK) adequately backed by budgetary support and a structured payment mechanism. The rating also factors in the strong fiscal profile of GoK relative to most states in India and the continuing focus on capital expenditure despite the economic disruption brought in by the Covid pandemic in FY21.

Karnataka Water & Sanitation Pooled Fund Trust (KWSPF) was constituted by the GoK (Government of Karnataka) as a fully-owned trust under the Indian Trusts Act, 1882, duly constituted by the Deed of Trust established on 12th Sept. 2003 and is managed by the Karnataka Urban Infrastructure Development & Finance Corporation (KUIDFC). KWSPF aims to mobilize financial resources for urban infrastructure development in Karnataka. KWSPF raised through the 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.

Trust was formed for the purpose of financing infrastructure projects on loan basis in Karnataka. 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 low cost.

About KUIDFC

Karnataka Urban Infrastructure Development and Finance Corporation (KUIDFC) was incorporated as a public limited company under the Companies Act, 1956 on 02.11.1993 with the objective to prepare, formulate and implement projects, schemes and programmes relating to infrastructure development in the urban areas of the state and to provide technical, financial, consultancy and other assistance to urban bodies for development, schemes, including implementation of master plans. Considering its expertise in project formulation, appraisal, management and implementation KUIDFC has been appointed as the Nodal Agency of the State for implementation of various urban infrastructure development projects in the state. KUIDFC has secured the status of State Level Financial Institution (SLFI) from the Government of India.

Standalone (Unsupported) Rating

ACUITE A

Analytical Approach

Acuite has considered the standalone business and financial risk profiles of KWSPF and has factored in support extended by GoK (through an unconditional and irrevocable guarantee) as well as the presence of the Structured Payment Mechanism along with presence of escrow mechanism while arriving at the rating.

Key Rating Drivers

Strengths

• Structured payment mechanism with a shortfall undertaking by 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:

- 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.
- Transfer adequate funds for repayment into the escrow account of the KWSPF Trust at least five working days prior to the due date.
- 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.
- Amount indicated by the Lender / KWSPF shall be final and binding on the GoK.
- 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.
- 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.

• 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 low cost. It acts as a nodal agency on behalf of the central and state government. So far, KWSPF has, raised tax free bond amounting to Rs. 100.00 crore 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. 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. Overall an amount of Rs.3085.80 core Loans has been raised for these schemes up to March 2020.

• Healthy fiscal profile of Government of Karnataka

Karnataka has one of the strongest fiscal profiles among the states of India. Karnataka is the state that leads in social development while simultaneously maintaining a strong fiscal profile. Karnataka is projected to revenue deficit of 0.89 per cent of GSDP in 2021-22 (BE). The state has demonstrated a strong ability to attract investments from foreign as well as domestic companies. In FY21, the GSDP contracted by 2.6 as per budget estimates due to impact of the pandemic. GoK has budgeted increased spending in FY22 for Irrigation and Flood Control (12 per cent), Health and Family Welfare (16 per cent), Rural Development (12 per cent), Law enforcement (11 per cent) and at the same time has reduced spending on certain other segments.

• Tripartite Agreement

A tripartite agreement has been executed between KWSPF, GoK and the lenders in line with the transaction structure. And the Trust has opened an escrow account specifically to fulfil the debt obligations and any withdrawals from the account will require lenders' approvals.

Weaknesses

• Impact of COVID and increased spending associated with the same

Pandemic resulted in increased spending in form of infrastructural and medical spending including setting up temporary health facilities and other expenses. At the same time, the revenue was impacted due to the ongoing pandemic. The governments at central and state level have taken steps to contain the pandemic and revive the economy through public spending. Acuité believes that the ongoing pandemic will negatively impact the state's GSDP on short run and result in higher revenue and fiscal deficits for coming 2-3 years.

Liquidity Position: Adequate

KWSPF has adequate liquidity marked by the comfort it derives from 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 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.

Rating Sensitivities

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

Assessment of Adequacy of Credit Enhancement

KWSPF had established track record and raises resources on a pooled basis and acts as a nodal agency on behalf of the central and state government. KWSPF has adequate liquidity marked by the comfort it derives from support from the Government of Karnataka (GoK) and grants from State Finance Commission (SFC). Acuite believes that the CE will stand adequate in all scenarios and in the event of any requirement, GoK will provide the necessary support.

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 risk profile of GoK and/or impeding its ability for timely budgetary provisions by the state.

About the Rated Entity - Key Financials

| | Unit | FY20 (Actual) | FY19 (Actual) |
|-------------------------------|------------|---------------|---------------|
| Operating Income | Rs. Cr. | 153.61 | 99.39 |
| PAT | Rs. Cr. | 12.21 | 2.13 |
| PAT Margin | (percent) | 7.95 | 2.14 |
| Total Debt/Tangible Net Worth | Times | 56.01 | 68.51 |
| PBDIT/Interest | Times | 1.09 | 1.02 |

Any other information

Not Applicable

Any Material Covenants

None

Applicable Criteria

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

Note on complexity levels of the rated instrument

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

Rating History (Upto last three years)

| Date | Name of Instrument / Facilities | Term | Amount (Rs. Cr.) | Ratings/Outlook |
|-------------|---------------------------------|-----------|------------------|-------------------------------------|
| 31-Jan-2020 | Proposed Term Loan | Long Term | 414.98 | ACUITE AA- (CE) / Stable (Assigned) |

***Annexure – Details of instruments rated**

| Name of the Facilities | Date of Issuance | Coupon Rate | Maturity Date | Size of the Issue (Rs. Cr.) | Ratings/Outlook |
|------------------------|------------------|---------------|---------------|-----------------------------|---------------------------------------|
| Term Loan | Not Available | Not Available | Not Available | 200.00 | ACUITE AA- (CE) / Stable (Reaffirmed) |
| Term Loan | Not Available | Not Available | Not Available | 214.98 | ACUITE AA- (CE)/ Stable (Reaffirmed) |

Contacts

| Analytical | Rating Desk |
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| Aditya Gupta Vice President Tel: 022-49294041 aditya.gupta@acuite.in Hariprasad J Senior Analyst - Rating Operations Tel: 022-49294046 Hariprasad.j@acuite.in | Varsha Bist Senior Manager - Rating Desk Tel: 022-49294011 rating.desk@acuite.in |

About Acuité Ratings & Research:

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