

Press Release

Kerala Financial Corporation

September 07, 2022



Rating Assigned and Reaffirmed

Product	Quantum (Rs. Cr)	Long Term Rating	Short Term Rating
Bank Loan Ratings	5050.00	ACUITE A+ Stable Assigned	-
Bank Loan Ratings	950.00	-	ACUITE A1 Assigned
Non-Convertible Debentures (NCD)	1000.00	ACUITE AA Stable Reaffirmed	-
Total Outstanding Quantum (Rs. Cr)	7000.00	-	-
Total Withdrawn Quantum (Rs. Cr)	0.00	-	-

Rating Rationale

Acuite has reaffirmed the long term rating of 'ACUITE AA' (read as ACUITE double A) on the Rs. 1000.00 Cr Secured Non-convertible Debentures of Kerala Financial Corporation (KFC). The outlook remains 'Stable'.

Acuite has assigned the long term rating of 'ACUITE A+' (read as ACUITE A plus) on the Rs. 5050.00 Cr Long Term Bank Loan Facilities of Kerala Financial Corporation (KFC). The outlook is 'Stable'.

Acuite has assigned the Short term rating of 'ACUITE A1' (read as ACUITE A one) on the Rs. 950.00 Cr Short Term Bank Loan Facilities of Kerala Financial Corporation (KFC).

The rating factors in the majority ownership of the Government of Kerala (98.54 percent) and KFC's strategic importance as financial institution for assistance of Micro, Small and Medium Enterprises (MSME) sector in the state. The rating takes into account the regular support from Government of Kerala and its experienced management. The rating also takes into consideration the fiscal constraints faced by the Government of Kerala. KFC's capitalization levels remained moderate at 22.41 percent as on March 31, 2022. The rating also takes into account KFC's portfolio growth (Rs 4750.71 Cr. as on March 31, 2022 as against Rs 4612.13 Cr. as on March 31, 2021) driven by disbursements of Rs 2175.20 Cr during FY2022. By virtue of state government ownership and support, the corporation enjoys strong resource raising ability at lower cost of funds thereby maintaining comfortable liquidity buffers to meet its funding requirements. Also for NCD, the rating takes the support of the presence of internal credit enhancement proposed in the form of Debt Service Reserve Account (DSRA) and the Structured Payment Mechanism.

The rating is however constrained on account of concentration in MSME Sector comprising of 93.74 percent as on March 31, 2022, and moderate profitability. While ontime portfolio has

improved to 84.78 percent as on June 2022 as against 68.70 percent on June 2021, KFC reported GNPA (90+DPD) at 3.27 percent as on March 2022 as against 3.58 percent as on March 2021. Going forward, credit profile of Kerala state and KFC's systematic importance, KFC's ability to maintain asset quality and profitability would remain key monitorable.

About the company

Kerala Financial Corporation was incorporated in 1953, under the State Finance Corporations Act, 1951 by Government of Kerala, with an objective of rapid industrialization of the state by extending financial assistance to Micro, Small and Medium Enterprises in manufacturing and service sector.

The corporation was originally established as the Travancore Cochin Financial Corporation in 1953 and consequent to reorganization of states on linguistic basis in November 1956, Kerala State was formed and the Travancore Cochin Financial Corporation was renamed as Kerala Financial Corporation.

Government of Kerala is the majority stakeholder with 98.54 percent holding and the balance is headed by domestic banks and other institutions. As on March 31, 2022, the corporation operates in 14 districts of Kerala with a network of 16 branches. Shri Sanjay Kaul IAS is the current Chairman and Managing Director of KFC.

Analytical Approach

Acuité has considered the standalone approach while assessing the business and financial risk profile of KFC and has factored in the financial, operational and managerial support it receives from Kerala Government by virtue of being a State Financial Corporation. The rating factors in the high degree of Government holding in KFC along with the systematically important role played by the corporation in implementing the key financial and developmental objectives of the state. Further for NCD, the rating also takes the support of the presence of internal credit enhancement proposed in the form of Debt Service Reserve Account (DSRA) and the Structured Payment Mechanism.

Key Rating Drivers

Strength

Ownership and Support from Government of Kerala (GoK):

KFC is a State finance corporation established under the SFC Act, 1951. The board of KFC includes representation from Government of Kerala. The Board of Directors comprise 3 bureaucrats appointed by the Government of Kerala and the others representing SIDBI, LIC of India, Bank of India and State Bank of India (erstwhile State bank of Travancore).

The Government of Kerala is the 98.54 percent stakeholder in the corporation and is expected to support the corporation given its systemic importance to the state. KFC's capitalization levels remained adequate at 22.41 percent as on March 31, 2022 as against 22.85 percent as on March 31, 2021.

By virtue of state government ownership and support, the corporation enjoys strong resourcing raising ability at lower cost of funds thereby maintaining comfortable liquidity buffers to meet its funding requirements. KFC's funding profile is supported by the State Government's moral obligation to support the capitalization levels both on an ongoing basis and in the event of distress. KFC's funding mix comprises equity contribution from its shareholders primarily GoK, NCDs and borrowings from banks. Of the overall outstanding borrowings of Rs 4308.87 Cr. as on March 31, 2022, NCDs comprise ~16.98 percent and remaining ~77 percent is bank borrowings and foreign currency loans.

KFC is a Nodal Agency for several policy initiatives by the State Government of Kerala and is responsible to implement the states policy initiatives announced in the annual state budget. The corporation in the past has operationalized various policy initiatives by GoK such as

Kerala State Entrepreneur Development Mission and Interest Subvention for Innovative Projects. The corporation is presently promoting schemes such as Startup Support Scheme, receivable financing scheme to support various business while extending working capital loans and term loans as its own products. KFC reported loan portfolio of Rs. 4750.71Cr as on March 31, 2022 as against Rs. 4621.12 Cr. as on March 31, 2021.

Since the support from GoK is critical to the rating, the credit profile of Kerala state is of key importance. The state's fiscal headroom has been further impacted by the recent COVID outbreak. While this is expected to put some pressure on Kerala's fiscal metrics over the near term, the overall fiscal health of the state over the medium term is expected to stay satisfactory. Movement in the state's key fiscal metrics i.e. fiscal deficit to GSDP and Debt to GSDP will remain key monitorable.

Acuité believes that the corporation will continue to benefit from strong financial and managerial support from the State Government on an ongoing basis over the medium term.

Maintenance of principal cash collateral, DSRA along with presence of Structured Payment Mechanism (SPM) for NCD:

The rating factors in the Structured Payment Mechanism (SPM) put in place by KFC to ensure timely availability of funds for servicing of debt obligations. The rating on the NCDs is secured by presence of Structured Payment Mechanism wherein amount equivalent to principal repayment of respective year shall be brought in by T-7 days (T is the due date) and the said amount will be invested in permitted investments. The maturity proceeds of the said investment will be credited directly to the designated escrow account and will be utilized for principal redemption process.

In case the principal amount is not invested and made sufficient, the principal servicing is additionally secured by way of cash collateral of 20 percent of outstanding principal being maintained at any point of time.

The SPM is also in place for semi-annual servicing of interest obligations wherein semi-annual interest will be divided into two portions and each interest portion at the beginning of the third and fifth month will be invested in permitted investments and both will mature on the T-1 day of the coupon payment date and the proceeds will be credited directly to the designated escrow account from where the coupon amount will be paid.

In case the interest amount is not invested and made sufficient, the interest servicing is additionally secured by way of DSRA wherein amount equivalent to one semi-annual interest obligation of the outstanding bonds will be maintained by the issuer on rolling basis.

The cash collateral and DSRA will be lien marked to the debenture trustee and in the event of principal or interest is not invested and made sufficient, the trustee will mandatorily liquidate the principal cash collateral and DSRA in order to make the proceeds available for the principal payment and interest payment respectively.

The cash collateral, DSRA, investment as per structured payment mechanism, and funds in the escrow account till such time being utilized would be permitted to remain invested in Fixed deposits with Scheduled commercial banks with preferably AAA rating or AA rating, Central or State Government securities (G Sec/T- Bills /SDL) or AAA/AA paper rated by two SEBI/RBI approved rating agency. These investments will be pledged in favour of debenture trustee.

The rating centrally assumes complete adherence to the SPM by the debenture trustee and KFC on an ongoing basis.

Weakness

Moderate profitability albeit improving.

The profitability in FY2022 stood at Rs. 13.20 Cr. (Rs 6.58 Cr for FY2021 as against Rs 18.37 Cr for FY2020). The corporation reported Net Interest margin of 4.74 percent in FY2022 as against 3.01 percent in FY2021 and 3.24 percent in FY2019. The profitability continues to be supported by lower operating expenses to earning assets of 1.04 percent for FY2022 as against 0.82 percent in FY2021 along with low average cost of borrowing of 6.67 percent in FY2022. The

corporation's return on average assets stands at 0.24 percent as on March 31, 2022 (0.14 percent for FY 2021).

Acuité believes, given the challenges, the company's ability to manage the additional slippages while maintaining the profitability will be crucial

ESG Factors Relevant for Rating

Not applicable

Rating Sensitivity

- Credit Profile of Kerala Government and timely support to KFC.
- Movement in Asset Quality and Profitability metrics.

Material Covenants

Kerala Financial Corporation is subject to covenants stipulated by its lenders/investors in respect of various parameter.

Liquidity Position

Adequate

KFC's overall liquidity profile remains well matched with no negative cumulative mis-matches in near to medium term as per ALM dated March 31, 2022. The company is in talks with various lenders to raise long term debt. The company's liquidity position is supported by unencumbered Cash and Bank Balance of Rs 240 Cr as on March 31, 2022. The support from GoK should help KFC for any refinancing, if needed.

Outlook : Stable

Acuité believes that KFC will maintain a 'Stable' outlook over the medium term mainly supported by presence of SPM along with continued support from the GoK. The outlook may be revised to positive in case of significant improvement in the operating performance of KFC backed by improved asset quality. The outlook may be revised to negative in case of nonadherence to the SPM or in case of events which may impinge on GoK's ability to provide financial and operational support to KFC.

Other Factors affecting Rating

None

Key Financials - Standalone / Originator

Particulars	Unit	FY22 (Actual)	FY21 (Actual)
Total Assets	Rs. Cr.	5662.26	5340.88
Total Income*	Rs. Cr.	231.89	137.75
PAT	Rs. Cr.	13.20	6.58
Net Worth	Rs. Cr.	690.45	678.35
Return on Average Assets (RoAA)	(%)	0.24	0.14
Return on Average Net Worth (RoNW)	(%)	1.93	1.04
Total Debt/Tangible Net worth (Geraing)	Times	6.24	6.29
Gross NPA	(%)	3.27	3.58
Net NPA	(%)	1.28	1.48

*Total income equals to Net Interest Income plus other income.

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>
- Non-Banking Financing Entities: <https://www.acuite.in/view-rating-criteria-44.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
06 Oct 2021	Non Convertible Debentures	Long Term	250.00	ACUITE AA Stable (Reaffirmed)
	Non Convertible Debentures	Long Term	250.00	ACUITE AA Stable (Reaffirmed)
	Non Convertible Debentures	Long Term	250.00	ACUITE AA Stable (Reaffirmed)
	Non Convertible Debentures	Long Term	250.00	ACUITE AA Stable (Reaffirmed)
01 Oct 2020	Non Convertible Debentures	Long Term	250.00	ACUITE AA Stable (Assigned)
	Non Convertible Debentures	Long Term	250.00	ACUITE AA Stable (Reaffirmed)
	Non Convertible Debentures	Long Term	250.00	ACUITE AA Stable (Reaffirmed)
	Non Convertible Debentures	Long Term	250.00	ACUITE AA Stable (Reaffirmed)
18 Aug 2020	Non Convertible Debentures	Long Term	250.00	ACUITE AA Stable (Reaffirmed)
	Proposed Non Convertible Debentures	Long Term	250.00	ACUITE Provisional AA Stable (Reaffirmed)
	Non Convertible Debentures	Long Term	250.00	ACUITE AA Stable (Reaffirmed)
	Non Convertible Debentures	Long Term	250.00	ACUITE AA Stable (Reaffirmed)
04 Nov 2019	Non Convertible Debentures	Long Term	250.00	ACUITE AA Stable (Reaffirmed)
	Non Convertible Debentures	Long Term	250.00	ACUITE AA Stable (Reaffirmed)
	Non Convertible Debentures	Long Term	250.00	ACUITE AA Stable (Reaffirmed)
	Proposed Non Convertible Debentures	Long Term	250.00	ACUITE Provisional AA Stable (Assigned)
	Proposed Non Convertible Debentures	Long Term	250.00	ACUITE Provisional AA (SO) Stable (Assigned)

31 Jan 2019	Non Convertible Debentures	Long Term	250.00	ACUITE AA (SO) Stable (Reaffirmed)
	Non Convertible Debentures	Long Term	62.50	ACUITE AA (SO) Stable (Assigned)
	Non Convertible Debentures	Long Term	62.50	ACUITE AA (SO) Stable (Assigned)
	Non Convertible Debentures	Long Term	62.50	ACUITE AA (SO) Stable (Assigned)
	Non Convertible Debentures	Long Term	62.50	ACUITE AA (SO) Stable (Assigned)
16 Nov 2016	Non Convertible Debentures	Long Term	250.00	ACUITE AA (SO) Stable (Assigned)
05 May 2016	Proposed Non Convertible Debentures	Long Term	250.00	ACUITE Provisional AA (SO) 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 Debentures (NCD)	Not Applicable	Not Applicable	Not Applicable	31.50	ACUITE AA Stable Reaffirmed
Not Applicable	Not Applicable	Non-Convertible Debentures (NCD)	Not Applicable	Not Applicable	Not Applicable	62.50	ACUITE AA Stable Reaffirmed
Not Applicable	Not Applicable	Non-Convertible Debentures (NCD)	Not Applicable	Not Applicable	Not Applicable	250.00	ACUITE AA Stable Reaffirmed
Not Applicable	Not Applicable	Non-Convertible Debentures (NCD)	Not Applicable	Not Applicable	Not Applicable	250.00	ACUITE AA Stable Reaffirmed
Not Applicable	Not Applicable	Proposed Long Term Loan	Not Applicable	Not Applicable	Not Applicable	1075.00	ACUITE A+ Stable Assigned
Not Applicable	Not Applicable	Proposed Non Convertible Debentures	Not Applicable	Not Applicable	Not Applicable	406.00	ACUITE AA Stable Reaffirmed
Not Applicable	Not Applicable	Proposed Short Term Loan	Not Applicable	Not Applicable	Not Applicable	174.00	ACUITE A1 Assigned
Federal Bank	Not Applicable	Short-term Loan	Not Applicable	Not Applicable	Not Applicable	175.00	ACUITE A1 Assigned
Union Bank of India	Not Applicable	Short-term Loan	Not Applicable	Not Applicable	Not Applicable	60.00	ACUITE A1 Assigned
State Bank of India	Not Applicable	Short-term Loan	Not Applicable	Not Applicable	Not Applicable	491.00	ACUITE A1 Assigned
South Indian Bank	Not Applicable	Short-term Loan	Not Applicable	Not Applicable	Not Applicable	50.00	ACUITE A1 Assigned
Canara Bank	Not Applicable	Term Loan	Not available	Not available	Not available	829.00	ACUITE A+ Stable Assigned
Union Bank of India	Not Applicable	Term Loan	Not available	Not available	Not available	304.00	ACUITE A+ Stable Assigned
State Bank of India	Not Applicable	Term Loan	Not available	Not available	Not available	841.00	ACUITE A+ Stable Assigned
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Bank of Maharashtra	Not Applicable	Term Loan	Not available	Not available	Not available	900.00	A+ Stable Assigned
Bank of Baroda	Not Applicable	Term Loan	Not available	Not available	Not available	212.00	ACUITE A+ Stable Assigned
Indian Bank	Not Applicable	Term Loan	Not available	Not available	Not available	489.00	ACUITE A+ Stable Assigned
India Infrastructure Finance Company Ltd.	Not Applicable	Term Loan	Not available	Not available	Not available	200.00	ACUITE A+ Stable Assigned
South Indian Bank	Not Applicable	Term Loan	Not available	Not available	Not available	200.00	ACUITE A+ Stable Assigned

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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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