

## Press Release

### Kerala Financial Corporation

January 06, 2023



### Rating Assigned and Reaffirmed

Product	Quantum (Rs. Cr)	Long Term Rating	Short Term Rating
Bank Loan Ratings	5050.00	ACUITE A+   Stable   Reaffirmed	-
Non-Convertible Debentures (NCD)	750.00	ACUITE AA   Stable   Assigned	-
Non-Convertible Debentures (NCD)	1000.00	ACUITE AA   Stable   Reaffirmed	-
Bank Loan Ratings	950.00	-	ACUITE A1   Reaffirmed
Total Outstanding Quantum (Rs. Cr)	7750.00	-	-
Total Withdrawn Quantum (Rs. Cr)	0.00	-	-

### Rating Rationale

Acuite has assigned the long term rating of '**ACUITE AA**' (read as **ACUITE double A**) on the Rs. 750.00 Cr Non-convertible Debentures of Kerala Financial Corporation (KFC). The outlook is '**Stable**'.

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

Acuite has reaffirmed 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 remains '**Stable**'.

Acuite has reaffirmed 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).

### Rationale for the rating

The rating factors in the majority ownership of the Government of Kerala (98.54 percent) in KFC and its strategic importance as a 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 in to 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 4621.13 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 a competitive cost and maintains comfortable liquidity buffers. Also for NCD, the rating takes the additional support from the Debt Service Reserve Account (DSRA) and

the Structured Payment Mechanism.

The rating is however constrained on account of KFC's portfolio 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, apart from the fiscal profile of Kerala state and KFC's systematic importance, KFC's ability to maintain asset quality and profitability would be the key rating monitorables.

### 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.

### Standalone (Unsupported) Rating

ACUITE A+

### 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. KFCs 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 Rs. 1000.00 Cr. NCDs considers the presence of Structured Payment Mechanism wherein amount equivalent to principal repayment of respective year shall be brought in by T-7 (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 on the Rs. 750.00 Cr. NCDs considers the presence of Structured Payment Mechanism wherein starting from the 1st day of each quarterly servicing cycle, remit on every

working day an amount equivalent to 2.00% of the aggregate servicing requirement for such quarterly servicing cycle to the bond servicing account. The Debenture Trustee shall monitor the same on T-15 day (T is the due date) and any shortfall persisting on T-9th day shall be met through transfer of requisite funds from the DSRA.

The SPM is also stipulates that KFC would be required to maintain in DSRA an amount equivalent to total servicing obligation (principal plus interest) for the next two quarters on a rolling basis. KFC would also be required to maintain a cash collateral for an amount equivalent to 10% of the outstanding amount of debentures. Both, the Cash Collateral and DSRA would be in the form of cash and cash equivalent, invested in permitted instruments and would remain charged in favour of the debenture trustee.

In case of any erosion from the DSRA due to transfer of funds in bond servicing account, the same shall be required to be cured within 30 days (T+30). If not the same shall be made good by transferring necessary amount of funds / investment to the DSRA from cash collateral and the Debenture Trustee should immediately inform the issuer to replenish the cash collateral amount to the stipulated level within the next 30 days (T+60).

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 A1+ rating or AA or higher 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

### **Moderate asset quality**

KFC has moderate asset quality as the GNPA as on September, 2022 stood at 4.41% from 3.27% as on March 31, 2022. Further the company also has restructured accounts amounting to Rs.~394.84 Cr which reduced from ~Rs. 734 Cr. as on March 31, 2022. KFC also has high borrower concentration as the top three borrowers, all Kerala state PSUs, amounted to ~Rs. 2374 Cr. as on June 30, 2022.

Moving forward KFC's ability to reduce the concentration of top borrowers and its ability to maintain NPA and restructured accounts below 5% will be key monitorables

### **ESG Factors Relevant for Rating**

Not Applicable

### **Rating Sensitivity**

- Credit Profile of Kerala Government and timely support to KFC.
- Movement in Asset Quality and NPA + restructured assets <5 %
- Sustained improvement in AUM and Profitability metrics.
- Movement in gearing and further capital infusion; Gearing <8 %

### **Material Covenants**

None

## 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 (Gearing)	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):

None

## Any other information

None

## 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>
- Explicit Credit Enhancements: <https://www.acuite.in/view-rating-criteria-49.htm>
- Non-Banking Financing Entities: <https://www.acuite.in/view-rating-criteria-44.htm>

### Note on complexity levels of the rated instrument

In order to inform the investors about complexity of instruments, Acuite has categorized such instruments in three levels: Simple, Complex and Highly Complex. Acuite's categorisation of the instruments across the three categories is based on factors like variability of the returns to the investors, uncertainty in cash flow patterns, number of counterparties and general understanding of the instrument by the market. It has to be understood that complexity is different from credit risk and even an instrument categorized as 'Simple' can carry high levels of risk. For more details, please refer Rating Criteria "Complexity Level Of Financial Instruments" on [www.acuite.in](http://www.acuite.in).

### Rating History

Date	Name of Instruments/Facilities	Term	Amount (Rs. Cr)	Rating/Outlook
07 Sep 2022	Term Loan	Long Term	841.00	ACUITE A+   Stable (Assigned)
	Term Loan	Long Term	900.00	ACUITE A+   Stable (Assigned)
	Proposed Long Term Loan	Long Term	1075.00	ACUITE A+   Stable (Assigned)
	Proposed Non Convertible Debentures	Long Term	406.00	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	62.50	ACUITE AA   Stable (Reaffirmed)
	Non Convertible Debentures	Long Term	31.50	ACUITE AA   Stable (Reaffirmed)
	Proposed Short Term Loan	Short Term	174.00	ACUITE A1 (Assigned)
	Short Term Loan	Short Term	491.00	ACUITE A1 (Assigned)
	Short Term Loan	Short Term	175.00	ACUITE A1 (Assigned)
	Short Term Loan	Short Term	60.00	ACUITE A1 (Assigned)
	Short Term Loan	Short Term	50.00	ACUITE A1 (Assigned)
	Term Loan	Long Term	212.00	ACUITE A+   Stable (Assigned)
	Term Loan	Long Term	200.00	ACUITE A+   Stable (Assigned)
	Term Loan	Long Term	489.00	ACUITE A+   Stable (Assigned)
	Term Loan	Long Term	200.00	ACUITE A+   Stable (Assigned)
	Term Loan	Long Term	829.00	ACUITE A+   Stable (Assigned)
	Term Loan	Long Term	304.00	ACUITE A+   Stable (Assigned)

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)
		Long		
	Non Convertible Debentures	Term	250.00	ACUITE AA   Stable (Reaffirmed)
18 Aug 2020	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 (Reaffirmed)

## Annexure - Details of instruments rated

Lender's Name	ISIN	Facilities	Date Of Issuance	Coupon Rate	Maturity Date	Complexity Level	Quantum (Rs. Cr.)	Rating
Not Applicable	INE818F07104	Non-Convertible Debentures (NCD)	Sep 14 2020	7.70	Sep 14 2026	Simple / Complex	50.00	ACUITE AA   Stable   Reaffirmed
Not Applicable	INE818F07112	Non-Convertible Debentures (NCD)	Sep 14 2020	7.70	Sep 14 2027	Simple / Complex	50.00	ACUITE AA   Stable   Reaffirmed
Not Applicable	INE818F07120	Non-Convertible Debentures (NCD)	Sep 14 2020	7.70	Sep 14 2028	Simple / Complex	50.00	ACUITE AA   Stable   Reaffirmed
Not Applicable	INE818F07138	Non-Convertible Debentures (NCD)	Sep 14 2020	7.70	Sep 14 2029	Simple / Complex	50.00	ACUITE AA   Stable   Reaffirmed
Not Applicable	INE818F07146	Non-Convertible Debentures (NCD)	Sep 14 2020	7.70	Sep 14 2030	Simple / Complex	50.00	ACUITE AA   Stable   Reaffirmed
Not Applicable	INE818F07096	Non-Convertible Debentures (NCD)	Jul 9 2019	8.99	Jun 9 2023	Simple / Complex	62.50	ACUITE AA   Stable   Reaffirmed
Not Applicable	INE818F07070	Non-Convertible Debentures (NCD)	Jul 9 2019	8.99	Jun 9 2024	Simple / Complex	62.50	ACUITE AA   Stable   Reaffirmed
Not Applicable	INE818F07062	Non-Convertible Debentures (NCD)	Jul 9 2019	8.99	Jun 9 2025	Simple / Complex	62.50	ACUITE AA   Stable   Reaffirmed
Not Applicable	INE818F07088	Non-Convertible Debentures (NCD)	Jul 9 2019	8.99	Jun 9 2026	Simple / Complex	62.50	ACUITE AA   Stable   Reaffirmed
Not Applicable	INE818F07039	Non-Convertible Debentures (NCD)	Apr 9 2018	8.69	Apr 4 2023	Simple / Complex	16.30	ACUITE AA   Stable   Reaffirmed
Not Applicable	INE818F07047	Non-Convertible Debentures (NCD)	Apr 9 2018	8.69	Apr 4 2024	Simple / Complex	10.45	ACUITE AA   Stable   Reaffirmed
Not Applicable	INE818F07054	Non-Convertible Debentures (NCD)	Apr 9 2018	8.69	Apr 4 2025	Simple / Complex	4.75	ACUITE AA   Stable   Reaffirmed
Not Applicable	INE818F07013	Non-Convertible Debentures (NCD)	May 9 2016	8.90	May 9 2023	Simple / Complex	62.50	ACUITE AA   Stable   Reaffirmed



Not Applicable	Not Applicable	Proposed Long Term Loan	Not Applicable	Not Applicable	Not Applicable	Simple	618.00	ACUITE A+   Stable   Reaffirmed
Not Applicable	Not Applicable	Proposed Non Convertible Debentures	Not Applicable	Not Applicable	Not Applicable	Simple / Complex	406.00	ACUITE AA   Stable   Reaffirmed
Not Applicable	Not Applicable	Proposed Non Convertible Debentures	Not Applicable	Not Applicable	Not Applicable	Simple / Complex	750.00	ACUITE AA   Stable   Assigned
Federal Bank	Not Applicable	Short-term Loan	Not Applicable	Not Applicable	Not Applicable	Simple	250.00	ACUITE A1   Reaffirmed
Union Bank of India	Not Applicable	Short-term Loan	Not Applicable	Not Applicable	Not Applicable	Simple	100.00	ACUITE A1   Reaffirmed
State Bank of India	Not Applicable	Short-term Loan	Not Applicable	Not Applicable	Not Applicable	Simple	500.00	ACUITE A1   Reaffirmed
South Indian Bank	Not Applicable	Short-term Loan	Not Applicable	Not Applicable	Not Applicable	Simple	100.00	ACUITE A1   Reaffirmed
Canara Bank	Not Applicable	Term Loan	Not available	Not available	Not available	Simple	763.00	ACUITE A+   Stable   Reaffirmed
Union Bank of India	Not Applicable	Term Loan	Not available	Not available	Not available	Simple	304.00	ACUITE A+   Stable   Reaffirmed
State Bank of India	Not Applicable	Term Loan	Not available	Not available	Not available	Simple	1292.00	ACUITE A+   Stable   Reaffirmed
Bank of Maharashtra	Not Applicable	Term Loan	Not available	Not available	Not available	Simple	1000.00	ACUITE A+   Stable   Reaffirmed
Bank of Baroda	Not Applicable	Term Loan	Not available	Not available	Not available	Simple	212.00	ACUITE A+   Stable   Reaffirmed
Indian Bank	Not Applicable	Term Loan	Not available	Not available	Not available	Simple	488.00	ACUITE A+   Stable   Reaffirmed
India Infrastructure Finance Company Ltd.	Not Applicable	Term Loan	Not available	Not available	Not available	Simple	173.00	ACUITE A+   Stable   Reaffirmed
South Indian Bank	Not Applicable	Term Loan	Not available	Not available	Not available	Simple	200.00	ACUITE A+   Stable   Reaffirmed

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### About Acuité Ratings & Research

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