

## RATING RATIONALE

22 Nov 2024

### Kerala Financial Corporation

**Brickwork Ratings reaffirms the ratings for the Non-Convertible Debentures (Non-SLR bonds) of Rs 378.38 Crores (Reduced from Rs 452.7 Crores) of Kerala Financial Corporation**

#### Particulars:

Instruments**	Amount Rs. Crs.		Tenure	Rating^	
	Previous	Present		Previous (27-Nov-2023)	Present
NCD (Non SLR Bonds)	452.7	<b>378.38</b>	Long Term	BWR AA/Stable (Reaffirmation)	<b>BWR AA/Stable (Reaffirmed)</b>
<b>Total</b>	452.7	<b>378.38</b>	<b>Rupees Three Hundred Seventy Eight Crores and Thirty Eight lakhs Only</b>		

^Please refer to BWR website [www.brickworkratings.com/](http://www.brickworkratings.com/) for the definition of the ratings

\*\* Details of Bonds are provided in Annexure-II

The rating for the aforesaid bonds derives comfort from the built-in structured payment mechanism, cash collateral in the form of fixed deposit/ investment bond equivalent to 20% of the outstanding principal and DSRA for outstanding NCDs of Rs.378.38 Crs.

Please Note- The rated amount stands reduced to Rs 378.38 Crores on account of redemption post the last review. The redeemed NCD details are provided in Annexure-II.

#### RATING ACTION / OUTLOOK: REAFFIRMATION/ STABLE

Brickwork Ratings (BWR) reaffirms the ratings at BWR AA/Stable for the Non-Convertible Debentures (Non-SLR bonds) of Rs 378.38 Crores (Reduced from Rs 452.7 Crores) of Kerala Financial Corporation

The ratings of the company continue to factor in the majority ownership of the Government (Govt) of Kerala (stake of 99.14%) as of 31 Mar 2024 and 30 Sep 2024, Growth in Assets under Management (AUM) from Rs.6529.4 Crores in FY23 to Rs.7368.33 Crores as of FY24 which declined to Rs 7039.41 Crores as of 30 Sep 2024, comfortable capitalization with CRAR of 27.38% as of 30 Sep 2024 and adequate liquidity profile. BWR also continues to derive comfort from the built-in structured payment mechanism, cash collateral in the form of fixed deposit/investment bond equivalent to 20% of the outstanding principal, and DSRA for outstanding NCDs of Rs.378.38 Crores. The rating also factors in the moderate, albeit improving, asset quality. BWR maintains a Stable outlook for the company as the company's standalone performance is improving with focus on recovery and disbursement and expected growth in the AUM in the second half of FY25



**KEY COVENANTS OF THE INSTRUMENT/FACILITY RATED: (For the outstanding NCD issues aggregating to Rs. 378.38 Crores)**

The Corporation shall, prior to the pay-in date, deposit into the DSRA an amount equal to the succeeding coupon payment required to be paid by the corporation in respect of the debentures and shall maintain the same on a rolling basis.

The amount equivalent to the principal amounts repayable in each year shall be brought in by T-7 business days, and the said amount will be invested as detailed in the transaction documents, and the same will always be line-marked to the debenture trustee as explained in transaction documents.

The Corporation shall, prior to the pay-in date, create permitted investments in terms of transaction documents for an amount equivalent to 20% of the outstanding principal amount of the debentures.

At any time, if the Corporation fails to sufficiently fund the NCD interest payment account on T-7 days, the debenture trustee would initiate the liquidation of the DSRA amount to ensure proceeds are available on T-1 day towards the payment due on the NCDs by the due date, i.e. day T.

At any time, if the State Govt of Kerala ceases to own 51% of the Corporation or ceases to control the Corporation without obtaining the prior written consent of the debenture trustee (acting upon the instructions of each of the debenture holders), the debenture trustee shall be entitled to exercise any and all remedies set out in the transaction documents, in accordance with the terms and conditions in the transaction documents including, without limitation, accelerating the redemption of the debentures

**Key Rating Drivers**

**Credit Strengths:-**

- **Strong support from the Government of Kerala:** Kerala Financial Corporation, incorporated under the State Financial Corporations Act of 1951, benefits from the strong support received from the Govt of Kerala. The primary objective of KFC is to promote industrialization in Kerala by extending financial assistance to micro, small and medium enterprises in the manufacturing and service sectors. As of 31 March 2024, the Govt of Kerala had a majority shareholding of 99.14%, followed by Small Industries Development Bank of India (SIDBI) at 0.844%, Life Insurance Corporation (LIC) at 0.010%, State Bank of India (SBI) at 0.003% and others at 0.001%, respectively. Moreover, KFC is a nodal agency for several policy initiatives by the State Govt of Kerala and is responsible for implementing the state's policy initiatives announced in the annual state budget. BWR takes comfort from the Corporation's strategic importance to the state of Kerala.
- **Structured Payment Mechanism and Additional Comfort from Cash collateral:** BWR also continues to derive comfort from the built-in structured payment mechanism, cash collateral in the form of fixed deposit/investment bond equivalent to 20% of the outstanding principal and DSRA for outstanding NCDs of Rs.378.38 Cr (Reduced from Rs 452.7 Cr).
- **Comfortable capitalization:** The company's capital to risk-weighted assets ratio (CRAR) stood at 27.38% as of 30 Sep 2024 (improved from 25.52% as of FY24) The company

maintained CRAR well above the minimum regulatory requirement of 15%. Improvement in net worth to Rs 1063.53 Crores as of FY24 due to capital infusion of Rs 100 Crores and continued improvement as of 30 Sep 2024 to Rs 1127.76 Crores also contributed to comfortable capitalization.

### **Credit Risks:-**

#### **Improving but modest Asset Quality:**

- Asset quality of the company continued to improve as of FY24 as compared to FY23 as Gross NPA (%) reduced from 3.11% in FY23 to 2.88% in FY24. Net NPA (%) improved from 0.74% in FY23 to 0.68% in FY24. As of FY24, the Standard assets stood at 97.12% of the loan portfolio. The Provision Coverage Ratio is maintained at a comfortable level of 85.92%.(increase from 84.89% as of FY23) which indicates the Company has sufficient provisions to withstand losses. The Company has a well-built monitoring mechanism for recovery of loans which resulted in increase in collections by 67.26% to Rs 3901.2 Crores as of FY24 compared to Rs 2332.41 Crores as of FY23.
- GNPA however increased to 4.52% as of 30 Sep 2024 from 3.74% as of 30 June 2024.. NNPA ratio stood at 2.15% , higher than 1.41% as of 30 June 2024. As per the company, while preparing the interim financials, the company provide only the minimum NPA provision required as per RBI norms (15% for S2- Sub Standard and 25% for D1- Doubtful debts 1) as against the higher provision given on 31 March 2024 (77% for S2 and D1 is fully written off technically). The company does not technically write off any bad debts while preparing the quarterly financials. Hence the Gross and net NPA as of 30 Sep 2024 is before the technical write off of bad debts and incremental NPA provisioning and hence it is on the higher side when compared to 31 March 2024. The Company expects the gross NPA and net NPA to be below FY24 levels (GNPA 2.88% and NNPA 0.68%) by FY25.
- However, going forward, the company's ability to manage the asset quality while increasing its loan book will be a key rating monitorable.

#### **Moderate Profitability:**

- Net profit improved to Rs. 74 Crores in FY24 as compared to Rs. 50 Crores in FY23 primarily due to 25.11% increase in total income to Rs 869 Crores in FY24 from Rs 694 Crores in FY23. The Significant Reduction In Provisions to Rs 1.35 Crores in FY24 as against Rs 49.99 Crores in FY23 boosted the net profits. Net interest income however declined by 16.43% to Rs 110.35 Crores in FY24 as compared to Rs 132.05 Crores due to 38.85% increase in interest expenses to Rs 571.5 Crores owing to an increase in borrowings. Other income increased by 64.37% to Rs 64.95 Crores in FY24 as compared to Rs 39.51 Crores in FY23. The majority of other income is interest on bank deposits which increased to Rs 55.21 Crores in FY24 (Rs 24.21 Crores in FY23). ROE and ROA both improved to 6.96% and 0.85% respectively in FY24 from 5.42% and 0.67% respectively in FY23. The improvement was primarily due to an increase in Net profit and net worth in FY24 from FY23. During FY25, the Net profits declined by 15.94% y-o-y to Rs 25.31 Crores from Rs 30.11 Crores in Q2FY25 due to increase in total expenses by 11.87% to Rs 168.25 crores in Q2FY25 from Rs 150.40 Crores in Q2FY24 owing to 12.12% increase in interest expenses to

Rs 155.03 Crores (Rs 138.27 Crores in Q2FY24). Operating Expenses growth outpaced total income growth resulting in drop in Net Profit in Q2FY25. Net interest income declined by 41.46% to Rs 31.97 Crores in Q2FY25 as compared to Rs 54.61 Crores in Q2FY24 owing to a decline in interest income to Rs 187 Crores (Rs 192.88 Crores in Q2FY24). This resulted in a decline in Net Interest Margin to 1.82% in Q2FY25 as compared to 2.52%. However, in H1FY25, Net profit improved by 12.72% in H1FY25 to Rs 64.05 Crores from Rs 56.82 Crores in H1FY24 due to an increase in total income by 11.84% to Rs 419.06 Crores supported by growth in interest income by 5.22% to Rs 383.49 Crores (Rs 364.48 Crores in H1FY24). Net interest income however declined by 10.30% to Rs 77.38 Crores in H1FY25 as compared to Rs 86.27 Crores in H1FY24 due to an increase in interest expenses by 10.03% in H1FY25 to Rs 306.11 Crores (Rs 278.21 Crores in H1FY24).

### **ANALYTICAL APPROACH - STANDALONE**

For arrive at its ratings, BWR has evaluated the risk profile of KFC on a standalone basis and factored in the financial, operational and managerial support that KFC continues to receive from the Government of Kerala. As a State Financial Corporation, KFC is a strategically important financial institution in Kerala, contributing towards the economic, industrial and social development of the state. For NCDs aggregating to Rs.378.38 Crores rated 'BWR AA/Stable', BWR has drawn comfort from the structured payment mechanism and cash collateral of 20% of the NCDs outstanding. BWR has applied its rating methodology as detailed in the rating criteria (hyperlinks provided at the end of this rationale).

### **RATING SENSITIVITIES**

Going forward, the corporation's ability to improve the earnings profile and asset quality while maintaining portfolio growth will be key rating sensitivities. Positive: The corporation's ability to improve the earnings profile, Gearing levels and asset quality while maintaining portfolio growth is a key rating positive. Negative: The weakening of the asset quality and earnings profile and/or a deterioration in capitalisation are key rating negatives.

### **LIQUIDITY POSITION - ADEQUATE**

As per the ALM statement shared by the company as of 30 Sep 2024, the liquidity position of the company is adequate with no negative cumulative mismatches across the buckets. The company's repayment obligations are NCDs falling due between June 2025 to September 2030, amounting to Rs. 378.38 Crores, against which it had cash and bank balance of Rs. 498.68 Crs as of 30 Sep 2024. Given the aforesaid, the liquidity is adequate. The company also had short-term deposits with banks Rs 601.62 Crores, Rs 855 Crores of unutilised bank limits as of 30 Sep 2024. It has average monthly collections of around Rs.325 Crores in FY23-24 with annual collections of Rs.3901 Crores for FY24. Further, the company collected Rs 2717.34 Crores with an average monthly collection of Rs 452.89 Crores during the H1FY25 (April 2024 to September 2024).

Further, the rated bonds have a cash collateral in the form of Fixed Deposit equivalent to 20% of the outstanding principal. Also, the company shall, prior to the pay-in date, deposit into the DSRA an amount equal to the succeeding coupon/ principal payment, and shall maintain the same on a rolling basis. At any time, if the company fails to fund the NCD interest / principal

payment account on T-7 days, the debenture trustee would initiate the liquidation of the DSRA amount to ensure proceeds are available on T-1 day Hence liquidity is considered to be adequate

## COMPANY PROFILE

**Kerala Financial Corporation**, incorporated under the State Financial Corporations Act of 1951, is a public sector enterprise under the administrative control of the Govt of Kerala with the objective of promoting the industrialisation of the state by extending financial assistance to micro, small and medium enterprises in the manufacturing and service sectors. The financial assistance is provided in the form of term loans, working capital loans and special schemes. A Jayathilak IAS, is the present chairman and managing director of KFC. The board of directors of the corporation consists of seven members, including representatives from the state government, and other stakeholders. KFC now has 22 branch offices with its headquarters in Thiruvananthapuram. 99.14% of the shares of the Corporation are owned by the Government of Kerala. The main objective of the Corporation is to boost industrial growth in the state by strengthening the MSME industrial sector.

## KEY FINANCIAL INDICATORS – Standalone

Key Parameters	Units	FY 23 Audited	FY 24 Audited	6MFY25 Unaudited (Reviewed)
Asset Under Management	Rs in Crores	6529.4	7368.33	7039.41
PAT	Rs in Crores	50.18	74.04	64.05
CRAR	%	25.58	25.32	27.38
Gross NPA ratio	%	3.11	2.88	4.52
Net NPA ratio	%	0.74	0.68	2.15
NIM	%	2.02	1.50	1.82

## NON-COOPERATION WITH PREVIOUS RATING AGENCY IF ANY:

No outstanding non-cooperation rating with other Credit Rating Agencies.

# **RATING HISTORY FOR THE PREVIOUS THREE YEARS [including withdrawal and suspended]**

S. No	Facilities	Current Rating (22 Nov 2024)			Rating History		
		Type	Amount Outstanding (Rs in Cr)	Rating	2023 27 Nov 2023	2022 7 Sep 2022	2021 06 Aug 2021
1	NCR (Non SLR bonds)	Long Term	378.38	BWR AA / Stable (Reaffirmation)	BWR AA / Stable (Reaffirmation)	BWR AA/ Stable (Reaffirmed)	BWR AA/Stable (Reassigned)
2	Bank Facilities	Long Term	-	-	BWR A / Stable (Reaffirmation and simultaneous Withdrawn)	BWR A/Stable (Reaffirmed)	BWR A/Stable (Reaffirmed)
	<b>Total</b>		<b>378.38</b>		<b>Rupees Three Hundred Seventy Eight Crores and Thirty Eight lakhs Only</b>		

## **Hyperlink/Reference to applicable Criteria:**

- [General Criteria](#)
- [Approach to Financial Ratios](#)
- [Banks and Financial Institutions](#)
- [Capital Instruments issued by Banks and Financial Institutions](#)

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## Kerala Financial Corporation

### ANNEXURE I

#### Details of Bank Loan Facilities rated by BWR: NA

Lender Name	Type of Facility	Long Term (Rs. Crs.)	Short Term (Rs. Crs.)	Total (Rs. Crs.)	Total (Rs. Crs.)	Complexity Level
NIL	NIL	NIL	NIL	NIL	NIL	NIL

### ANNEXURE II

#### (NCD/Bonds/CP/FDs) DETAILS

Instrument	Issuance date	Amount (Rs Crs)	Coupon Rate	Maturity Date	ISIN number	Complexity Level
NON SLR BOND (ISSUE SERIES 1/2018)	4 April 2018	NIL*	8.69%	4 April 2024	INE818F07047	Simple
	4 April 2018	3.38	8.69%	4 April 2025	INE818F07054	Simple
NON SLR BOND (ISSUE SERIES 1/2019)	9 July 2019	NIL*	8.99%	9 July 2024	INE818F07070	Simple
		62.5	8.99%	9 July 2025	INE818F07062	Simple
		62.5	8.99%	9 July 2026	INE818F07088	Simple
NON SLR BOND (ISSUE SERIES 1/2020)	14 Sep 2020	50	7.70%	14 Sep 2026	INE818F07104	Simple
		50		14 Sep 2027	INE818F07112	Simple
		50		14 Sep 2028	INE818F07120	Simple
		50		14 Sep 2029	INE818F07138	Simple
		50		14 Sep 2030	INE818F07146	Simple
Total		378.38		Rupees Three Hundred Seventy Eight Crores and Thirty Eight lakhs Only		

\*Redeemed

#### COMPLEXITY LEVELS OF THE INSTRUMENTS: Simple

For more information, visit [www.brickworkratings.com/download/ComplexityLevels.pdf](http://www.brickworkratings.com/download/ComplexityLevels.pdf)

### ANNEXURE-III

#### List of Entities Consolidated - None



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