

RATING RATIONALE

21 Oct 2019

Karnataka State Financial Corporation

Brickwork Ratings Reaffirms the ratings for the Non-Convertible Debenture issue of ₹ 100 Crores of Karnataka State Financial Corporation [hereafter referred to as “KSFC” or the ‘Corporation’]

Particulars

Instrument**	Amount (₹ Cr)		Tenure	Rating*	
	Previous	Present		Previous (Oct, 2018)	Present
NCD	100	100	Long Term	BWR AA- (CE) Stable	BWR AA- (CE) Stable
Total	100	100	INR One Hundred Crores Only		

*Please refer to BWR website www.brickworkratings.com/ for definition of the ratings

** Details of NCD is provided in Annexure-I

RATING ACTION / OUTLOOK

The rating reaffirmation has factored, inter alia, strong fiscal profile of Govt of Karnataka (GoK), prudent fiscal discipline and liquidity management by the Karnataka State, credit enhancement in the form of unconditional and irrevocable Guarantee provided by the Government of Karnataka, comfortable capitalisation and adequate liquidity of KSFC. The rating is however constrained by the weak asset quality, low profitability and increasing debt of the state.

Outlook: Stable

BWR believes the **Karnataka State Financial Corporation** business risk profile will be maintained over the medium term considering the strong fiscal profile of Govt of Karnataka and the stable performance of KSFC. The ‘Stable’ outlook indicates a low likelihood of rating change over the medium term.

KEY RATING DRIVERS

Credit Strengths:

- **Strong Fiscal Profile of Govt of Karnataka:** Karnataka witnessed GSDP growth in excess of 10% for last 2 fiscals and continues to report revenue surplus. Total receipts of the state has increased from Rs 1,72,262 Crs in FY18 (Actuals) to Rs 2,12,228 Crs in FY19

(Revised Estimates). This was mainly on account of increase in states own tax revenue, share in central taxes, grants from centre and capital receipts. At the same time, total expenditure of the state has increased from Rs 1,86,510 Crs in FY18 to Rs 2,17,451 Crs in FY19 resulting in a Revenue surplus and Fiscal deficit of Rs 194 Crs and 40,167 Crs respectively when compared to Revenue surplus and Fiscal deficit of Rs 4,517 Crs and Rs 31,101 Crs in FY18.

- **Credit Enhancement:** The outstanding NCD issue has credit enhancement in the form of “Unconditional and Irrevocable guarantee of Govt of Karnataka” for timely repayment of principal and interest.
- **Healthy Capitalisation and adequate liquidity:** Corporation is comfortably capitalised with total CRAR of 28.73% as on 31 Mar 2019 against minimum regulatory requirement of 15%. As per the ALM profile dated 30 June 2019, the liquidity position of the Corporation is comfortable with no cumulative mismatches across various buckets. The corporation also has cash and bank balances and current investments of Rs 75 Crs as on 28 July 2019.

Credit Risks:

- **Weak Asset Quality and low profitability:** Given the objective of KSFC to provides financial support to small and medium enterprises in the state with special focus to the industrially backward areas NPAs have always been high. However in FY19, it has marginally improved with GNPA & NNPA reducing to 11.96% and 6.09% respectively when compared to GNPA of 14.68% and NNPA of 6.56% in FY18. PCR for FY19 stood at 49.06%. Profitability of the corporation remains very low with ROA and ROE of 0.48% and 1.64% respectively for FY19..
- **Increasing debt of GoK:** Total debt outstanding for the state has increased from Rs 2,26,800 Crs in FY18 to Rs 2,64,600 Crs in FY19. The state govt. has also extended support (equity and guarantees) to various weak PSU entities, this has resulted in Debt/guarantees as a percentage of GSDP of 18.54 %. Committed expenses as a percentage of own tax revenues remains moderate at 73.75% for FY19 with interest payments as a percentage of own tax revenues contributing to 16.33%.

ANALYTICAL APPROACH AND APPLICABLE RATING CRITERIA

For arriving at the ratings, BWR has analysed the financial profile of KSFC and derived a standalone rating of BWR BBB. Considering the credit enhancement in the form of “Unconditional and Irrevocable Guarantee” provided by Govt of Karnataka, the rating of BWR AA- (CE) (Stable) has been assigned. BWR has applied its rating methodology as detailed in the Rating Criteria detailed below (hyperlinks provided at the end of this rationale).

RATING SENSITIVITIES

Positive: Improvement in the fiscal profile of Govt of Karnataka resulting in substantial reduction in fiscal deficit, reduction in overall debt levels, committed expenses as a percentage of own tax revenues and improved profitability and asset quality of the corporation will be key rating positives..

Negative: Substantial deterioration in the fiscal profile of Govt of Karnataka, substantial increase in debt+guarantees as a percentage of GSDP and committed expenses as a percentage of own tax revenues and further deterioration in asset quality and profitability of the corporation will be key rating sensitivities.

LIQUIDITY POSITION: Adequate

As per the ALM profile dated 30 June 2019, the liquidity position of the Corporation is comfortable with no cumulative mismatches across various buckets. The corporation also had cash and bank balances and current investments of Rs 75 Crs as on 28 July 2019.

Corporation PROFILE

KSFC was incorporated in the year 1959, under the State Financial Corporations Act 1951. Since inception, KSFC has been playing a major role in the development and industrialization of Karnataka. It has a network of offices all over Karnataka with 4 Circle offices and 32 branch offices. The main objective of KSFC is to assist small and medium enterprises in the state with a special focus on the industrially backward areas. Government of Karnataka (GoK) is the majority shareholder (91.90%) in the Corporation whereas SIDBI holds 8.05% as on March 31, 2019.

FINANCIAL INDICATORS - Karnataka State Financial Corporation (Issuer)

Key Parameters	Units	2017	2018	2019
Result Type		Audited	Audited	Audited
Loan Portfolio	₹ Cr	1809	1825	1949
Net Interest Income	₹ Cr	107	107	123
PAT	₹ Cr	30	26	10
Tangible Net worth	₹ Cr	1039	989	606
Total Debt	Times	1494	1399	1289
CRAR	%	35.81	37.81	28.73
GNPA	%	12.04	14.68	11.96
NNPA	%	5.77	6.56	6.09

FINANCIAL INDICATORS – Government of Karnataka (Credit Enhancement Provider)

Key Parameters	Units	2018	2019
		Actuals	Revised Estimates
Total Receipts	Rs in Crs	1,72,262	2,12,228
States Own Tax Revenue	Rs in Crs	87,130	95,512
Total Expenditure	Rs in Crs	1,86,510	2,17,451
Revenue Surplus	Rs in Crs	4,517	194
Fiscal Deficit	Rs in Crs	31,101	40,167
Debt Outstanding	Rs in Crs	2,26,800	2,64,600
Fiscal Deficit/GSDP	%	2.35	2.66
Committed expenses/Own tax revenue	%	65.44	73.75
Debt+Guarantees/GSDP	%	18.27	18.54

KEY COVENANTS OF THE INSTRUMENT/FACILITY RATED: Nil
NON-COOPERATION WITH PREVIOUS RATING AGENCY IF ANY: Nil

RATING HISTORY

S.No	Instrument	Current Rating (Oct, 2019)			Rating History			
		Long Term/ Short Term	Amount (₹ Crs)	Rating	Jun 2018	Oct 2018	Oct 2017	Sep 2016
1	NCD	Long Term	-	Withdrawn	BWR AA- (CE) Stable Withdrawn	BWR AA- (CE) Stable	BWR AA- (CE) Stable	BWR AA- (CE) Stable
2	NCD		100	BWR AA- (CE) Stable	BWR AA- (CE) Stable	BWR AA- (CE) Stable	BWR AA- (CE) Stable	BWR AA- (CE) Stable
	Total		100	₹ One Hundred Crores Only				

COMPLEXITY LEVELS OF THE INSTRUMENTS: Simple

For more information, visit www.brickworkratings.com/download/ComplexityLevels.pdf

Hyperlink/Reference to applicable Criteria

- [General Criteria](#)
- [Banks and Financial Institutions](#)
- [Credit Enhancement](#)



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Karnataka State Financial Corporation

**ANNEXURE I
INSTRUMENT (NCD/Bonds) DETAILS**

Instrument	Issue Date	Amount in ₹ Cr.	Coupon Rate	Maturity Date	ISIN Particulars
NCD	02/01/2013	100	9.49%	02/01/2023	INE549Fo8491