



## Rating Rationale

19 Jan 2024

### Lucknow Municipal Corporation

**Brickwork Ratings reaffirms the ratings for the Bonds/NCDs of Rs. 200.00 Crs of Lucknow Municipal Corporation.**

#### Particulars

Instrument**	Amount (Rs. Crs)		Tenure	Rating*	
	Previous	Present		Previous (19 Dec 2022)	Present
Bonds/NCDs	200.00	<b>200.00</b>	<b>Long Term</b>	BWR AA/Stable Reaffirmation	<b>BWR AA/Stable Reaffirmation</b>
<b>Total</b>	200.00	<b>200.00</b>	<b>Rupees Two Hundred Crores Only</b>		

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

\*\* Details of NCD/Bonds are provided in Annexure-I

#### RATING ACTION/OUTLOOK

The reaffirmation of the ratings of the Bonds/NCDs issued by Lucknow Municipal Corporation (LMC or the corporation) derives strength from satisfactory financial performance in FY23 and 6MFY24 (provisional), low debt level and adequate municipal funds, reserves and surplus. The rating continues to be backed by an upfront Debt Service Reserve Amount (DSRA) that covers four semi-annual coupon payments, an escrow mechanism with respect to the cash inflows of tax revenues, and a structured payment mechanism for the timely monitoring of fund availability in the Interest Payment Account (IPA) and Sinking Fund Account (SFA). The rating is further supported by the availability of funds from the Infrastructure Development Fund (IDF) maintained by the Government of Uttar Pradesh (GoUP) with a T-Structure for meeting the shortfall of the Sinking Fund Account (SFA) and replenishment of the DSRA. However, the ratings are constrained by the corporation's moderate achievements against the service level benchmarks in FY23, high receivables from GoUP and moderate tax collection efficiency for the last two years notwithstanding marginal improvement. BWR also takes note of the various continuing observations highlighted by the auditor in the Annual report in FY23.

The Stable outlook reflects the expectation that LMC's performance is likely to remain consistent owing to cash flows from tax revenues and revenue grants. The outlook may be changed to Negative in case of a sustained and significant decline in tax collections, unusual delays in the transfer of grants by the state government, and any breach of bond issue-related covenants.

### **KEY COVENANTS OF THE INSTRUMENT/FACILITY RATED:**

The rated NCDs of Rs.200 Crs have an upfront DSRA of four half-yearly coupon payments and a structured payment mechanism for a mismatch or shortfall in the cash flows for meeting the debt obligations as detailed in the structured payment mechanism. In addition, the rated bonds have implicit support extended by the GoUP for the utilisation of funds available in the Infrastructure Development Fund with a T-Structure for meeting the shortfall of the Sinking Fund and replenishment of the DSRA. Furthermore, the rated bonds are backed by the incentive received of Rs.26.00 Crs from the Government of India (GoI) as part of the AMRUT Scheme, and these cash flows are kept in the form of fixed deposits, and a lien has been created in favour of the debenture trustee throughout the tenor of the debentures.

### **KEY RATING DRIVERS**

#### **Credit Strengths:-**

- **Rated bonds are backed by strong structure:** LMC has created a separate escrow account for the receivables revenues (property taxes and fees and user charges) and state grants (which are free from all charges). A structured payment mechanism has been set-up for transferring funds from the escrow account to the IPA and SFA. LMC is also backed by an upfront DSRA for four half-yearly coupon payments. In addition, as per the government incentive related to bonds, LMC has received an incentive of Rs. 26 Crs. from GoI (Government of India) as a part of the AMRUT Scheme, and has been kept in fixed deposits, and a lien has been created in favour of the debenture trustee upto the tenor of the bonds. Furthermore, the rated bonds are also backed by the availability of funds from the IDF maintained by the GoUP (Government of Uttar Pradesh) with a T-Structure for meeting the shortfall of the SFA and the replenishment of the DSRA.
- **Adequate average cash flows available in escrowed taxes and grants:** The corporation's tax revenues and grants from State Finance Corporation (SFC) (which are free from all charges) have been escrowed to the rated bonds for ensuring the funds availability. During FY23 and 6MFY24 (Prov), the average monthly cash flows received from these sources were at Rs. 34.26 Crs. and at Rs. 35.62 Crs., respectively. Approximately, Rs. 3.72 Crs. per month of the escrowed cash flows is required to be transferred to the respective SFA and IPA. Therefore, the cash flows from escrowed receipts are adequate for the scheduled build-up of funds in the IPA and the SFA.
- **Moderate financial risk metrics:** There has been an improvement in total income from Rs. 1329.53 Crs. in FY22 to Rs. 1504.99 Crs. in FY23. The growth in tax and non-tax revenue were at ~35% and ~7%, respectively, over the period. The improvement in tax revenues was on account of addition of 88 new villages in its area along with other measures undertaken. The share of non-tax revenue in total income has gradually improved from ~21% in FY22 to ~25% in FY23. Net surplus has increased from Rs. 17.65 Crs. in FY22 to Rs. 48.48 Crs. in FY23. LMC's total net cash accruals increased from Rs. 141.69 Crs. in FY22 to Rs. 174.29 Crs. in FY23 against yearly obligation of transfer of ~Rs. 37 Crs. to IPA and SFA combined.

LMC's total income, net surplus and net cash accruals in 6MFY24 (Prov) were at Rs. 935.71 Crs., Rs. 315.25 Crs., and Rs. 375.73 Crs., respectively. Till 30 Sep 2023 (Prov), LMC has no meaningful debt apart from the raised bonds. LMC reported Municipal Funds, Reserves and Grants of Rs. 4667.71 Crs. as on 31 Mar 2023 and of Rs. 5192.47 Crs as on 30 Sep 2023 (Prov). The loans to reserves ratio as on 30 Sep 2023 (Prov) was reported at 0.15 time.

#### **Credit Risks:-**

- **Moderate tax collection efficiency and Service Delivery:**

In FY23, property tax collection efficiency improved to 62.67% as against 60.11% reported during FY22 primarily on account of the increase in the number of properties and timely realization of property taxes. Notwithstanding the marginal improvement on YoY basis, the collection efficiency remains at a moderate level and the corporation is utilising Geographic Information System (GIS) based survey along with additional manpower, e-payment services to further improve its own revenue share in the total revenue. Furthermore, LMC has continued to report moderate achievements against the various service level benchmarks pertaining to the delivery of civic amenities. LMC has reported moderate service levels with respect to water supply connections and sewerage network services on account of addition in the municipal area under the Municipal Limits where the services were not effectively implemented. As reported by the Corporation, during FY23, Service level benchmark achieved for Water supply connections stood at 68% (PY 77%; Target 83%), Sewerage Network Services stood at 58% (PY ~69%; Target ~76%) , and Solid Waste Management Collection Services stood at ~67.32% (PY 98%; Target 100%). The corporation's ability to improve the Service delivery benchmarks remains a rating monitorable.

- **Moderate surplus margins and high receivables:**

The corporation's operating and net margins have remained moderate. The operating surplus margins stood at 12.71% (PY: 12.40%) and net surplus margin stood at 3.22% (PY:1.33%) in FY23. However, in H1FY24, the operating surplus margin stood at 41.42% and net margin stood at 33.69% on account of the increase in revenue grants, contribution & subsidies and lower appropriation of expenses. Also, on an average, LMC's outstanding receivables stood at an elevated level of ~Rs. 620 Crs. during the last three years (FY21 to FY23).

- **Auditor's observations:**

BWR also takes note of the various continuing observations highlighted by the auditor in the Annual report in FY23. LMC stated that the issues have already been taken up with the respective authorities and the same would be looked into.

#### **ANALYTICAL APPROACH - Standalone**

To arrive at the ratings, BWR has considered the standalone financials of the corporation, along with the structured payment mechanism, including the IPA which includes a DSRA comprising four half-yearly coupon dues, the build-up of the SFA in the months preceding the due dates and



the replenishment of the DSRA (if utilised) as per the interest payment mechanism. In addition, the rated bonds are backed by availability of funds from IDF maintained by the GoUP with a T-Structure for meeting the shortfall of the SFA and the replenishment of the DSRA.

#### **RATING SENSITIVITIES:**

The ability of the Corporation to improve the tax revenues, collection efficiency, ensuring adequate timely availability of cash flows, continued support from the State Government and ensuring timely transfer of funds from the Infrastructure Development Fund in case of any shortfalls in sinking fund/DSRA replenishment will remain the key rating sensitivities.

- **Upward:**
  - Substantial improvement in the tax collection efficiency and service delivery achievements
  - Substantial reduction in the receivables position.
- **Downward:**
  - Sustained reduction in the tax collection, sustained deterioration in service delivery level, a sharp reduction in the available Municipal Funds, Reserves and Grants position,
  - A breach of bond issue-related covenants or a delay in meeting the shortfall in the DSRA / SFA from IDF as per the tripartite agreement with GoUP.

#### **LIQUIDITY: Adequate**

The liquidity position is considered adequate keeping in view that the corporation doesn't have any principal debt obligation upto Nov'24. Also, the corporation doesn't have any outstanding term loans from banks apart from unsecured loans of Rs 589 Crs for FY23 which are interest free loans and does not have any fixed repayment obligation on LMC. As confirmed by the corporation, the same may only be adjusted/deducted by the State Government from the grants/transfers to LMC. During FY23, the average monthly cash flows received with respect to property taxes and fees and user charges were Rs. 34.26 Crs. as compared to Rs. 29.02 Crs corresponding period which is adequate for building up the funds in the Interest Payment account and for the Sinking Fund account for meeting the debt obligations. The liquidity is further supported by maintenance of upfront DSRA (Equivalent of 4 Semi annual coupon payments), sinking fund (have ~2x coverage for the principal obligation falling due in Nov'24) and has a cash and bank balances of Rs. 1191.47 Crs. as on 30 Sep 2023 (PY: Rs 985.31 Crs).

#### **About the Corporation**

Lucknow Municipal Corporation (LMC) is administered under the Uttar Pradesh Municipal Corporation Adhiniyam, 1959. Till the year 1884, Lucknow was known as Municipal Committee however in the same year it was given the name of Municipal Board and continued till 1959. Lucknow Nagar Mahapalika was constituted in the year 1959 under Uttar Pradesh Nagar Mahapalika Act 1959. Under 74th Constitution amendment act Lucknow Nagar Mahapalika was again reconstituted on 31.05.94 and given the status of Municipal Corporation. The area under LMC is divided into eight zones and further subdivided into 110 municipal wards. It has a coverage area of 568 sq. kms, and serves a population of 28.17 lakh as per 2011 census and

density of 4959 person/Sq. Km. At the time of constitution, total area under its jurisdiction was 48 Sq Km which is now 510 Sq Km as on 31 Mar 2023.

## KEY FINANCIAL INDICATORS

Key Parameters	Units	FY22	FY23	6MFY24
Result Type		Audited	Audited	Provisional
Total Income	Rs. Crs	1329.53	1504.99	935.71
Total Expenditure	Rs.Crs	1164.63	1313.70	548.14
Cash Surplus before depreciation and interest	Rs. Crs	164.89	191.29	387.56
Net Surplus	Rs. Crs	17.65	48.48	315.25
Municipal Fund and Reserves	Rs. Crs	4487.86	4667.71	5192.47
Loans to Reserve Ratio	In Times	0.17	0.16	0.15

### Terms of the NCDs/Bonds

The tenor of the NCD/bonds is 10 years, and the redemption starts from FY25. LMC has created an interest payment account and a sinking fund. Additionally, an escrow account has been created, and the cash flows received from the property tax, and fees and user charges will be transferred to this escrow account.

- **Interest Payment Account:**

- The interest payment account is an account from which interest payments on the debentures will be serviced and the required DSRA will also be maintained. For ensuring the maintenance of the required DSRA, the four succeeding coupon payments amount has been reserved.
- Furthermore, on each of the first five transfer dates occurring in each 12-month block, an amount equivalent to 20% (twenty percent) of the coupon payment is to be made on the first coupon payment date in such a 12-month block and any further interest payable as per the terms of the issuance and any shortfall in the earlier contribution is to be transferred to the interest payment account.
- On each of the 6th to 10th transfer dates occurring in each 12-month block, an amount equivalent to 20% (twenty percent) of the coupon payment is to be made on the 2nd coupon payment date in such a 12-month block and any further interest payable as per the terms of the issuance and any shortfall in earlier contribution is to be transferred to the interest payment account.
- Any shortfall in the funds available in the escrow account to complete the aforesaid transfers to the above account(s) shall be made good by LMC by transfer from the other account(s) of LMC.

- **Sinking Fund Account:**
  - On each of the first 10 (ten) transfer dates occurring in each 12-month block, an amount equivalent to 1/10th of 10% (ten percent) of the issue size and any shortfall in the earlier contribution is to be transferred to the sinking fund account.
  - Any shortfall in the funds available in the escrow account to complete the aforesaid transfers to the above account(s) shall be made good by the LMC by transfer from the other account(s) of LMC.
- **Infrastructure Development Fund:** The replenishment of the required DSRA, as well as funding of the shortfall in the sinking fund account (created for principal repayment) a tripartite agreement has been executed among the GoUP/state government, the debenture trustee and LMC. The GoUP has issued a Governmental Order (GO) dated 30 July 2019, wherein it has created a policy for the utilisation of the funds in the Infrastructure Development Fund to promote/incentivise the issuance of municipal bonds. Pursuant to the GO, a tripartite agreement with the GoUP, debenture trustee and LMC has been executed on for agreeing and covenanting to make the payment of funds from the Infrastructure Development Fund in terms of such an agreement
  - into the interest payment account for the creation of the upfront required DSRA,
  - into the interest payment account on the occurrence of a DSRA shortfall
  - and into the sinking fund account on the occurrence of a sinking fund mismatch
- **GoI incentive:** LMC has received an incentive from the GoI as part of the AMRUT incentive during June 2021. This incentive amount of Rs. 26.00 Crs has been deposited in the form of fixed deposits, and a lien has been created in the favour of the debenture trustee over such fixed deposits throughout the tenor of the debentures. Interest amounts earned on such fixed deposits shall be utilisable by the issuer, in accordance with the terms set out in the transaction documents.
- **Interest Payment Mechanism- Structured Payment Mechanism**
  - The debenture trustee shall check the amount lying to the credit of the interest payment account (which is over and above the required DSRA) at 25 (twenty five) days prior to the coupon payment date (T-25 days). In the case of any shortfall in the amount required to make the payment of the coupon on the coupon payment date in the interest payment account (calculated on the basis of the amounts available in addition to the required DSRA), the debenture trustee shall intimate the issuer of the shortfall, and the issuer shall make good the shortfall in the interest payment account prior to the date falling 10 (ten) days prior to the coupon payment date (T-10 days).
  - In the case of a shortfall in the amount required to make the payment of coupon on the coupon payment date in the interest payment account (calculated on the basis of the amounts available in addition to the required DSRA) at nine days prior to the coupon payment date (T-9 days), the debenture trustee shall trigger the payment mechanism and instruct the bank to utilise the DSRA to the extent of the shortfall in the amount required to make the payment of the coupon on the coupon payment date on or prior to the date falling eight days prior to the interest payment date (T-8 days).
  - The coupon shall be paid by the issuer on the coupon payment date (T).
  - In case the DSRA (or part thereof) is utilised to fund the shortfall in the amount required to make payment of the coupon in respect of any coupon payment date,

immediately after the debenture trustee has instructed the bank to utilise the DSRA as above and in any event prior to seven days prior to the relevant coupon payment date (T-7), the debenture trustee would issue a notice in writing to the issuer (and the GoUP shall be informed of the same, by the debenture trustee, marking a copy of such a notice to the GoUP).

- On the issuance of such a notice, the issuer shall make good the DSRA shortfall prior to the date falling on the relevant coupon payment date (T). In the event that the shortfall is not made good by the issuer on the relevant coupon payment date (T), the debenture trustee shall issue a notice to the issuer (and GoUP shall be informed by marking a copy to GoUP) on the date immediately succeeding the relevant coupon payment date (T+1).
- On the issuance of such a notice, the GoUP shall remit funds required to replenish the required DSRA (such that the amount in the interest payment account (calculated on the basis of the amounts available in addition to the minimum balance) is atleast equivalent to the required DSRA) within 15 (Fifteen) days from the relevant coupon payment date (T+15) by depositing such amounts into the interest payment account.
- **Principal Repayment (Sinking Fund) Mechanism:**
  - The debenture trustee shall check the balance in the sinking fund account prior to the end of each 12-month block, and in the case of any shortfall in the sinking fund account, i.e., a sinking fund mismatch, it shall be replenished as per the following mechanism.
  - The debenture trustee shall check the amount lying to the credit of the sinking fund account at 25 (twenty five) days prior to the end of each 12-month block (T-25 days). In the case of any shortfall in the amount, the debenture trustee shall intimate LMC of the shortfall (and the GoUP shall be informed by marking a copy to the GoUP), and LMC shall make good the shortfall in the sinking fund account prior to the date falling 15 (fifteen) days prior to end of each 12-month block (T-15 days).
  - In case a shortfall in any amount still persists in the sinking fund account at 14 (fourteen) days prior to the end of each 12-month block (T-14 days), the debenture trustee shall trigger the payment mechanism and issue a notice to the issuer (and the GoUP shall be informed by marking a copy to the GoUP). On the issuance of such a notice, the state government shall remit funds to fund the shortfall into the sinking fund account prior to the end of each 12-month block (T).
  - The redemption shall be made by LMC on relevant redemption dates.

**NON-COOPERATION WITH PREVIOUS CREDIT RATING AGENCY IF ANY:**

There is no non-cooperation with other CRAs.

**Rating History for the previous three years (Including withdrawal and suspended)**

S.No	Instrument /Facility	Current Rating (January 2024)			Rating History					
		Type	Amount (Rs. Crs)	Rating	2023		2022		2021	
					Date	Rating	Date	Rating	Date	Rating
1	NCDs / Bonds	Long Term	200.00	BWR AA / Stable (Reaffirmation)	NA	NA	19 Dec 2022	BWR AA / Stable (Reaffirmation)	30 Nov 2021	BWR AA/ Stable (Reaffirmation)
<b>Total</b>			<b>200.00</b>	<b>Rupees Two Hundred Crores Only</b>						

**COMPLEXITY LEVELS OF THE INSTRUMENTS - Simple**

The BWR complexity levels are available at

<https://www.brickworkratings.com/download/ComplexityLevels.pdf>

**Hyperlink/Reference to applicable Criteria**

- [General Criteria](#)
- [Approach to Financial Ratios](#)
- [Public Finance- Municipal and Urban Local Bodies](#)

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**Lucknow Municipal Corporation  
Annexure-II  
Instrument Details**

<b>Instrument@</b>	<b>Issue Date</b>	<b>Amount (Rs. Crs)</b>	<b>Coupon Rate#</b>	<b>Maturity Date</b>	<b>ISIN Particulars</b>
NCD/Bonds	18 Nov 2020	28.58	8.50%	18 Nov 2024	INE05OC24017
NCD/Bonds	18 Nov 2020	28.58	8.50%	18 Nov 2025	INE05OC24025
NCD/Bonds	18 Nov 2020	28.58	8.50%	18 Nov 2026	INE05OC24033
NCD/Bonds	18 Nov 2020	28.58	8.50%	18 Nov 2027	INE05OC24041
NCD/Bonds	18 Nov 2020	28.58	8.50%	18 Nov 2028	INE05OC24058
NCD/Bonds	18 Nov 2020	28.58	8.50%	18 Nov 2029	INE05OC24066
NCD/Bonds	18 Nov 2020	28.52	8.50%	18 Nov 2030	INE05OC24074
<b>Grand Total</b>		<b>200.00</b>		<b>Rupees Two Hundred Crores Only</b>	

@ These bonds are listed in BSE and NSE ;

#The interest payment is made every year on 18-May and 18-Nov commencing from 18-May-2021.

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