Rating Rationale

05 January 2022

Power Company of Karnataka Limited

Brickwork Ratings reaffirms the ratings for the Bank Loan Facilities of Rs.2944.30 Crs of Power Company of Karnataka Limited.

Particulars

Facilities/ Instrument**	Amount (Rs. Crs)		Tenure	Rating*	
	Previous	Present		Previous (01-Dec-2020)	Present
Fund Based Term Loans	3417.85	**2944.30**	**Long Term**	BWR AA- (CE)/ Stable Reaffirmation	**BWR AA- (CE)/Stable Reaffirmation**
Total	3417.85	**2944.30**	**Rupees Two Thousand and Nine Hundred and Forty Four Crores and Thirty lakhs Only**		

*Please refer to BWR website www.brickworkratings.com for the definition of the ratings
** Details of bank facilities are provided in Annexure
Rating advisory issued on 01 December 2021for a delay in the periodic review

Ratings with the CE symbol are based on a Credit Enhancement (CE) in the form of an unconditional and irrevocable guarantee from the Government of Karnataka (GoK), Energy Department, for the payment of interest and principal until the full repayment of the loan, budgetary provisions for the servicing of the debt and escrow mechanism (securitisation of the receivables of various Gram Panchayats to ESCOMS) to ensure the timely repayment of term obligations and interest servicing.
The Unsupported rating of Power Company of Karnataka Limited as assessed by BWR without considering the CE is BWR BB+/Stable.

RATING ACTION/OUTLOOK

Brickwork Ratings (BWR) reaffirms the rating of Power Company of Karnataka Limited (PCKL or the company) considering the credit enhancement in the form of an unconditional and irrevocable guarantee from the Government of Karnataka (GoK), budgetary allocation (transferred by way of a grants) for the servicing of the debt by the GoK, ownership of ESCOMs and the GoK and its strategic importance to Karnataka. The rating further factors in the moderate fiscal indicators of the Karnataka government, adherence of the state to fiscal norms stated under the Fiscal Responsibility and Budget Management Act (FRBM) and maintenance of zero revenue deficit over the years.
However, the rating is constrained by the company's low income, low net-worth and adverse financial indicators with its high dependence on the timely receipt of grants from the GoK to meet its debt obligations. However, the company does not have operations and facilitates the raising of debt for bringing down the receivables of power distribution companies. The rating is also constrained owing to the impact of the COVID-19 pandemic on the state finances of Karnataka.

The outlook has been kept as Stable, considering the continuous support from the GoK by way of budgetary support of grants to meet its debt obligations.

KEY COVENANTS OF THE INSTRUMENT/FACILITY RATED:

The terms of sanctions include standard covenants normally stipulated for bank loan facilities. The bank facilities are backed by an unconditional and irrevocable, and irreversible guarantee of the GoK, Energy Department. In addition, it is backed by the agreement between lenders and PCKL for an escrow mechanism to ensure the timely repayment of term obligations and interest servicing.

KEY RATING DRIVERS

Credit Strengths-:

- **Ownership and experienced management:** Incorporated in 2007 under the Companies Act, 1956, with an initial authorised capital of Rs. 5 Crs, PCKL commenced its business operations from the investment by five ESCOMs. The management comprises eminent professionals from the GoK and ESCOMs with extensive industry and management experience.
- **Credit enhancement:** The rated facilities of Rs. 2944.30 Crs have an unconditional and irrevocable guarantee from the GoK.
- **Continuous receipt of government grants:** The company regularly receives government grants from the GoK to service its debt obligations. It received Rs. 708.08 Crs and Rs. 367.58 Crs in the form of grants from the GoK during FY21 and 7mFY22 (April 2021 to October 2021), to enable the company to discharge the liability of interest and principal on its term loans.
- **GoK support:** The GoK has provided a guarantee to fund the company's debt obligations, which it had raised to pay ESCOMs the receivables of Rs. 3766.81 Crs as of March 2015, from gram panchayats. The GoK in its order dated 31 March 2017 approved the scheme of the securitisation of receivables from gram panchayats' dues (including interest) of Rs. 3766.81 Crs outstanding as at the end of 31 March 2015, as approved by the State Cabinet on 10 January 2017 and accorded the approval for raising loans from commercial banks and financial institutions. The GoK has appointed PCKL as the nodal agency for implementing the securitisation of gram panchayats' dues, for entering an agreement for borrowings, and the releasing of the borrowed fund to PCKL on behalf of ESCOMs.

Credit Risks-:

- **Limited financial ability to fund debt obligations:** PCKL's main income source is advisory services and interest earned on the short-term deposits of surplus funds. There are no operations in the company. As per FY21 data, the company has reported nil revenues and a net loss of Rs. 0.04 Crs. PCKL's total debt stood at Rs. 3238.66 Crs, against a TNW of Rs. 2.68 Crs. The repayments are met timely through the payment

mechanism for the servicing of debt obligations through annual budgetary support from the GoK.

- **COVID-19 impact on state finances:** The impact of COVID-19 will be felt on the state's financial profile, on account of disruptions in the operations of several of the state's revenue generating sectors, with likely reductions in the devolution of central taxes to Karnataka, resulting from the prolonged nationwide lockdown implemented to curb the spread of the virus in the country. However, the expected moderation in the state's budgeted revenues from tax collections, coupled with the requirement of additional spending, would pose a challenge for the state in adhering to the fiscal consolidation norms.

ANALYTICAL APPROACH AND APPLICABLE RATING CRITERIA

To arrive at its ratings, BWR has considered the company's standalone financials. Furthermore, BWR has assessed the Karnataka state finances for determining the CE. 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 company's ability to ensure the timely receipt of grants from GoK and ensure the adequate allocation of the grants in the government's budget would be key rating sensitivities. The ability of the state to maintain the socio demographic indicator levels, ensure fiscal discipline and economic stability, improve its financial risk profile and improve the state revenue surplus, would also be key rating sensitivities.

- **Upward:** The ratings can move upward if the state government's performance improves on account of an improvement in the revenue surplus and socio-economic policies, along with an optimum increase in revenues and debt indicators and any upward revision in the credit rating of the guarantor (GoK).
- **Downward:** The ratings can move downward if there is a delay in the receipt of adequate government grants for debt servicing, deterioration in the fiscal profile of the state and downward revision in the credit rating of the guarantor (GoK).

LIQUIDITY: ADEQUATE

The company is not generating adequate cash accruals to meet its debt obligations. However, the company's liquidity is assessed as adequate as the company is being supported by the GoK by way of grants to meet its repayment obligation. The company received Rs. 708.08 Crs in the form of grants from the GoK during FY21, to enable the company to discharge liability of principal and interest on term loans. PCKL reported a cash balance of Rs. 28.92 Crs and term deposits with banks of Rs. 3.05 Crs as of 31 March 2021. The GoK has provided grants through the budgetary allocation of Rs. 367.58 Crs till October 2021 during FY22.

ABOUT THE COMPANY

Power Company of Karnataka Limited (PCKL) was incorporated in August 2007 by the GoK as a Special Purpose Vehicle (SPV) to supplement the efforts of KPCL in capacity addition by way of setting-up new power projects through a bidding process, under Case-II bidding guidelines issued by the Ministry of Power, GOI, and the long-term procurement of power under Case-I bidding guidelines of the MoP, GoI. Presently, PCKL acts as the nodal agency for implementing the securitisation of various gram panchayat dues to ESCOMs. The company will be working on a no-profit–no-loss basis till FY28. It is acting as a facilitator between all the discoms of Karnataka (BESCOM, CESC, MESCOM, HESCOM and GESCOM) and the GoK, wherein the GoK will fund the debt repayment.

PCKL has raised Rs. 3766.81 Crs through bank loans by securitising the receivables of various gram panchayats to ESCOMS during FY18 and FY19. These bank loans are backed by an unconditional and irrevocable guarantee from the GoK.

KEY FINANCIAL INDICATORS

Key Parameters	Units	2021	2020
Result Type		**Audited**	**Audited**
Total Income*	Rs. Crs	0.68	0.80
EBITDA	Rs.Crs	(0.68)	(1.47)
Net profit	Rs. Crs	(0.04)	(0.84)
Tangible Net worth	Rs. Crs	2.68	2.72
Total Debt/Tangible Net worth	In Times	1209.33	1349.06
Current Ratio	In Times	0.08	0.06

*Total income includes operating and non operating income

KEY FINANCIAL INDICATORS – STATE FINANCES KARNATAKA

The revenue expenditure for 2021-22 is budgeted at Rs. 1,87,405 Crs, which is an annual increase of 4% over 2019-20. The capital expenditure for 2021-22 is budgeted to be at Rs 58,802 Crs, which is an annual increase of 9% over the actual expenditure in 2019-20. The state expects a revenue deficit of Rs. 15,134 Crs in 2021-22 (0.89% of the Gross State Domestic Product ((GSDP)). In 2020-21, as per revised estimates, the revenue deficit was at Rs. 19,486 Crs as compared to the revenue surplus of Rs. 143 Crs budgeted for 2021. The fiscal deficit for 2021-22 as per revised estimates is to be at Rs. 59,240 Crs (3.48% of the GSDP). Given the situation due to COVID-19, the central government permitted states to increase their fiscal deficit up to 5% of the GSDP in 2020-21. All the states were allowed to increase their fiscal deficit up to 4% of the GSDP. As per the revised estimates of 2021, Karnataka's fiscal deficit was reported at 3.23%, which is within this increased limit.

State Financials	Units	2020	2021	2022
Result Type		**Actuals**	**R.E.**	**B.E.**
Revenue Receipts	Rs. Crs	1,75,443	1,59,709	1,72,271
Revenue Expenditure	Rs. Crs	1,74,257	1,79,195	1,87,405
Capital Receipts	Rs. Crs	50,707	70,672	71,463
Capital Expenditure	Rs. Crs	49,779	50,730	58,802
Revenue Surplus/GSDP	**%**	0.07	(1.08)	(0.89)
Fiscal Deficit/GSDP	**%**	(2.25)	(3.23)	(3.48)
Debt+Guarantees/GSDP	**%**	21.45	23.57	28.48

R.E. Revised Estimates B.E. Budget Estimates

NON COOPERATION WITH PREVIOUS CREDIT RATING AGENCY IF ANY: NIL

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

S. No	Instrument /Facility	Current Rating (2022)			Chronology of Rating History for the past 3 years (Rating assigned and press release date) along with outlook/watch, if applicable		
		Type (Long Term/ Short Term)	Amount (Rs. Crs)	Rating	**Date(s) & Rating(s) assigned in 2021**	**Date(s) & Rating(s) assigned in 2020**	**Date(s) & Rating(s) assigned in 2019**
1	**Fund Based** Term Loans	Long Term	2944.30	BWR AA- (CE) / Stable Reaffirmed	NA	BWR AA- (CE) / Stable Reaffirmed (01-Dec-2020)	BWR AA- (CE) / Stable Reaffirmed (25-Nov-2019)
Total			**2944.30**	**Rupees Two Thousand and Nine Hundred and Forty Four Crores and Thirty lakhs Only**			

COMPLEXITY LEVELS OF THE INSTRUMENTS: Simple

BWR complexity levels are meant for educating investors. The BWR complexity levels are available at www.brickworkratings.com / download / ComplexityLevels.pdf. Investors' queries can be sent to info@brickworkratings.com.

Hyperlink/Reference to applicable Criteria

- General Criteria
- Approach to Financial Ratios
- Ratings based on government support
- Ratings based on credit enhancement
- Infrastructure Sector

For any other criteria obtain hyperlinks from website.

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Power Company of Karnataka Limited
Annexure
Details of Bank Loan Facilities rated by BWR

S.No	Name of the Bank/Lender	Type of Facilities	Long Term (Rs. Crs)	Short Term (Rs. Crs)	Total (Rs. Crs)
1	State Bank of India	Term Loan	1348.78	--	1348.78
2	Punjab National Bank	Term Loan	359.00	--	359.00
3	Bank of India	Term Loan	1236.52	--	1236.52
		Total	**2944.30**	**--**	**2944.30**
Total Rupees Two Thousand and Nine Hundred and Forty Four Crores and Thirty lakhs Only.					

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