Pune Municipal Corporation

June 29, 2017

Ratings

Facilities	Amount (Rs. crore)	Ratings[1]	Rating Action
Non-Convertible Debentures (NCDs)	**200 (Rupees Two hundred crore only)**	**CARE AA+; Stable [Double A Plus; Outlook: Stable]**	**Reaffirmed**

Details of instruments/facilities in Annexure-1

NCDs have coupon rate of 7.59% with semi-annual interest payment and bullet repayment of principal after 10 years.

Detailed Rationale & Key Rating Drivers

The rating assigned to the Bond Issue of Pune Municipal Corporation (PMC) factors in the robust income profile with high proportion of own revenue base and a sustained revenue surplus for the period FY12-FY16 (refers to period April 1 to March 31) driven by strong economic base, comfortable liquidity position and capital structure with low dependence on grants or external debt to fund its capital expenditure.

PMC benefits from the strong economic base of Pune city, being known as an evolving business centre hosting various manufacturing and automobile industries, information technology (IT), education, management and training institutes. The rating also positively factors in PMC's self-reliant revenue stream backed by more than 90% of income being generated from its own sources with strong property tax and water tax collections and non-tax revenue, mainly comprising development charges.

PMC's debt service indicators are expected to remain at a comfortable level in the medium term despite the debt funded capital expenditure plan through issuance of bonds. The corporation has undertaken a water supply project with a view to provide 24/7 water to the city. The project is expected to achieve completion in five years and generate additional tax revenue for PMC.

The rating is however tempered by moderation witnessed in tax and user charges collection efficiency during FY16 and shortfalls in utility infrastructure against the set targets by PMC.

The ability of PMC to maintain its revenue surplus while successfully augmenting its infrastructure needs, implementation of key reforms such as Geographical Information System (GIS) based property tax system and improvement in its civic services will be key rating sensitivities. Furthermore, any higher-than-envisaged debt availed by the corporation in future, leading to weakening of debt protection indicators or decline in support from the state government in terms of Local Body Tax compensation, and impact of Goods and Services Tax (GST), if any, on the Corporation when implemented will act as key rating sensitivities.

Detailed description of the key rating drivers

Key Rating Strengths

Robust income profile : The total income (Tax and non-tax revenue) of the corporation has seen a fairly stable growth during the period FY12-FY16, growing at a Compound Annual Growth Rate (CAGR) of 7% aided in large

[1] *Complete definition of the ratings assigned is available at www.careratings.com and other CARE publications.*

part by the strong economic base of the region viz., the favourable growth in various industries mainly IT and auto industries. The revenue receipts of PMC have risen from Rs.3,022 crore in FY12 to Rs.3,862 crore in FY16. Furthermore, more than 90% of the revenue of PMC is earned from its own revenue sources leading to low dependence on government grants.

Tax revenue of PMC accounts for more than 60% of its income, of which local body tax (LBT) contributes around 50%, followed by property tax and water tax. Although the tax revenue of the corporation has seen an increasing trend over the years, the annual growth in the same has been prone to fluctuations. The same can be attributed to induction of Local Body Tax in April 2013 as the replacement of octroi and partial abolition of the LBT during FY16. However, PMC receives compensation from the state government towards abolition of LBT.

Healthy revenue surplus and comfortable liquidity position: PMC has been recording a healthy revenue surplus on a sustained basis for the past five years which is utilised towards capital expenditure by the corporation. For the period FY12 to FY16, PMC has been able to achieve revenue surplus of around 43-49%. Furthermore, excess funds left after meeting the capital expenditure is invested by the corporation in fixed deposit of various nationalized banks. The total investments of the PMC are Rs. 2,097 crore in FY16 comprises of existing fixed deposits with banks, central government securities, debentures and bonds, new fixed deposits with banks and cash & bank balances. CARE believes these investments would provide the corporation a comfortable cushion for any short term contingencies.

Sustained capital expenditure: The capital expenditure of the corporation, which is mainly incurred towards development of civic amenities and infrastructure projects, has been fairly steady over the years. During the last five years (FY12-FY16), PMC has incurred capex in the range of Rs.1,200 crore – Rs.1,500 crore per annum. Majority of the capital expenditure undertaken by the municipal corporation is sourced from its internal accruals with low dependence on the state/central government grants or debt. Pune has also been selected under the Smart City project of the government of India as per which it will receive Rs. 200 crore every year for a period of five years. Apart from the annual outlay towards the development projects such as road and sewages, PMC has also embarked on augmenting its water supply infrastructure with universal metering of the water consumption.

Comfortable debt coverage indicators: Reliance on external debt by PMC is minimal. It has cleared all its outstanding debt as of 24th April, 2017 and there has not been any incremental borrowing. The debt to revenue receipt ratio of PMC is 3.03% in FY16. Going forward, the debt coverage indicators of PMC are expected to remain at a comfortable level in the medium term despite the debt funded capital expenditure plan through issuance of bonds. Furthermore, the bonds will be issued in tranches and have a long moratorium period with repayment at end of 10th year.

Key Rating Weaknesses

Fluctuations in collection efficiency: The collection efficiency of the corporation has indicated fluctuations over the years. While there has been an improvement in the collection of property tax (since FY09), water & sewerage charge collection has been recording fluctuations.

Shortfalls in civic amenities: There are shortfalls in the coverage of civic amenities provided by the corporation. The coverage of the civic infrastructure is below the target set by the corporation. The coverage of sewerage and sanitation is marginally lower. The coverage however has declined from 97.6% in 2012 to 96% in 2015. The waste water recycles and reuse percentage is 5.38% and treatment capacity however has gone down from 71% in 2012 to 64% in 2015. As of September 2015, the supply of water reached to 219 lpcd along with the coverage of 93%. Storm water drainage coverage for 2015 is recorded at 93%. The household level coverage of solid waste management improved from 56% in FY13 to 60% in FY14 and further to 70% in FY15.

Structured Payment Mechanism

PMC has put in place a Structured Payment Mechanism to provide a liquidity support towards the principal and interest repayments of the NCDs. Under the structured payment mechanism, property tax collected and due to PMC will be deposited every month in a separate no-lien escrow account for servicing of the bonds. Firstly, a Debt Service Reserve Account (DSRA) account is funded one day before the pay-in date with an amount equal to two interest payments.

The salient features of the Structure Payment Mechanism are as follows:

1. At the beginning of every month, the funds lying/ deposited in escrow account shall be used in the following priority:

    a) Firstly, transfer to Debt Service Reserve Account (DSRA) to make good any shortfall in DSRA. At all times the DSRA is maintained at 2 interest payments.

    b) Secondly, transfer to Interest Payment Account on monthly basis the stipulated amount, and any shortfall in earlier contributions.

    c) Thirdly, transfer to the Sinking Fund Account on monthly basis the stipulated amount, and any shortfall in earlier contributions.

2. Any surplus funds in the account thereafter shall be transferred out of the escrow account to account of PMC.

The debenture trustee shall have the lien on the Interest Payment account, DSRA and Sinking Fund accounts. The Amount deposited in Interest Payment Account, DSRA and Sinking Fund shall be used solely for meeting the dues to the bondholders. Any surplus in the escrow account after meeting the dues to the bondholders can be transferred to the PMC. No amount can be withdrawn from these accounts without the approval of Trustees to the bond holders. The Funds lying credited in the Interest Payment Account and DSRA can be kept in Fixed Deposits with any scheduled commercial bank with a dual rating of AA or above. However, the conditions of the fixed deposits shall not restrict premature withdrawal from the Fixed Deposit. The funds lying to the credit of Sinking Fund Account can be deposited in Fixed Deposit with any scheduled commercial bank with a dual rating of AA and above and/or in Government Securities and Treasury Bills. The lien shall be created in favour of debenture trustee on all the investments made above. Any actual interest income earned and received on the investments made from the funds in the interest payment account and DSRA account can be utilized towards the next instalment of the interest in the interest payment account or to cover any shortfall in the DSRA account.

DSRA, Interest Payment Account and Sinking Fund Account shall be maintained with Bank of Maharashtra or the scheduled commercial bank rated at least A by two rating agencies through the tenor of the instrument. In case, at any point of time the rating of senior debt of the Bank falls below A, the PMC has to move the funds to other bank satisfying the previous condition.

Interest Payment and Principal Repayment Mechanism
(T = Bond payment date)

Date	Event/ employed	Measures if shortfall occurs
Interest Payment Account		
T-25	Trustees will check amount in Interest Payment Account	Intimate PMC to make good for the shortfall in interest payment account 15 days prior to interest payment date.
T-14	Trustees shall re-check amount in interest Payment	Trustees will trigger the payment mechanism and bank will be instructed to transfer the shortfall amount from DSRA to interest payment account 10 days prior to interest payment date. Withdrawal from

		DSRA should be deposited back in the account.
T	PMC shall pay the interest on due date	
Sinking fund		
T-25	Trustees shall check credit in the sinking fund	Intimate PMC of the shortfall and PMC shall make good the shortfall 15 days prior to redemption date
T	PMC shall repay the principal	

Restrictions on the total borrowing

(A) Debt Service Coverage Ratio ("DSCR") for the PMC will not be less than 1.5 times of operating surplus
(B) The total amount collected in escrow account shall be atleast 1.25 times of the Debt Service Amount on an annual basis. In case, the ratio falls below 1.25 times, PMC shall not, without the previous approval of the Trustees to the Debenture Holders, borrow any further amount against the cash flow of the escrow account.

Analytical Approach: Standalone
CARE has relied on the unaudited financial statement for FY12 and audited financial statements for FY13-FY16 provided by PMC.

Applicable Criteria
Criteria on assigning Outlook to Credit Ratings
CARE's Policy on Default Recognition
Financial ratios – Non-Financial Sector
CARE's Methodology for Urban Infrastructure Projects

About the Corporation
Established on February 15, 1950, PMC is the second-largest corporation in the state of Maharashtra. The corporation is governed by The Maharashtra Municipal Corporations Act, 1949 (amended from time to time). PMC is mainly responsible for the administration of the city, maintaining infrastructure facilities, and providing various civic services such as water supply, solid waste management, sewerage, education, health and others to its citizens. Pune's proximity to Mumbai, good climate, and availability of talent made it a destination for large firms. Pune has been the hub of the engineering industry for over five decades and one of the evolving business centres as it hosts various Information Technology (IT) and automotive companies.

Status of non-cooperation with previous CRA: Not Applicable

Any other information: N.A

Rating History (Last three years): Refer Annexure 2

Note on complexity levels of the rated instrument: CARE has classified instruments rated by it on the basis of complexity. This classification is available at www.careratings.com. Investors/market intermediaries/regulators or others are welcome to write to care@careratings.com for any clarifications.

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About CARE Ratings:

CARE Ratings commenced operations in April 1993 and over nearly two decades, it has established itself as one of the leading credit rating agencies in India. CARE is registered with the Securities and Exchange Board of India (SEBI) and also recognized as an External Credit Assessment Institution (ECAI) by the Reserve Bank of India (RBI). CARE Ratings is proud of its rightful place in the Indian capital market built around investor confidence. CARE Ratings provides the entire spectrum of credit rating that helps the corporates to raise capital for their various requirements and assists the investors to form an informed investment decision based on the credit risk and their own risk-return expectations. Our rating and grading service offerings leverage our domain and analytical expertise backed by the methodologies congruent with the international best practices.

Annexure-1: Details of Instruments/Facilities

Name of the Instrument	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. crore)	Rating assigned along with Rating Outlook
Non-Convertible Debentures	-	-	June, 2027	200.00	CARE AA+; Stable

Annexure-2: Rating History of last three years

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating history			
		Type	Amount Outstanding (Rs. crore)	Rating	Date & Rating assigned in 2016-2017	Date & Rating assigned in 2015-2016	Date & Rating assigned in 2014-2015	Date & Rating assigned in 2013-2014
1.	Non-Convertible Debentures	LT	200.00	CARE AA+; Stable	-	-	-	-

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