A. K. Capital Services Limited

February 13, 2023

Facilities/Instruments	Amount (₹ crore)	Rating[1]	Rating Action
Commercial paper	100.00 (Enhanced from 50.00)	CARE A1+	Reaffirmed

Details of instruments in Annexure-1.

Rationale and key rating drivers

The reaffirmation of the rating assigned to the debt instruments of A. K. Capital Services Limited (AKCSL) factors in the A. K. Capital group's long track record and established presence as a merchant banker in the debt market segment, the experience of the management team, the strong institutional client base, the comfortable capitalisation with moderate gearing level and healthy asset quality.

The rating however, is constrained on account of the inherent volatility in the income profile due to its dependence on the level of activity in debt capital markets; the exposure to market risk with adverse movement in interest, impacting the profitability, mitigated to a large extent by the low average holding period; the high exposure to the corporate segment with a relatively higher client concentration risk; and the competitive merchant banking industry scenario.

Rating sensitivities: Factors likely to lead to rating actions

Positive factors

- Not applicable

Negative factors

- Substantial deterioration in the profitability on a sustained basis.
- Deterioration in the market position in terms of client base.
- Deterioration in the credit quality of major investment in the inventory or liquidity profile.
- Increase in the leverage, with overall gearing beyond 4x on a sustained basis at the AKCSL consolidated level.

Analytical approach

AK Capital Services Limited, the flagship company for AK Capital group owns 100% in most of its subsidiaries and the management/line functions for these businesses is common with significant operational and financial integration among them. Accordingly, CARE Ratings Limited (CARE Ratings) has considered a consolidated view for arriving at the rating.

Key rating strengths

Long track record, established market presence and experienced management team: The company has been providing merchant banking services for over two and a half decades and is a leading player in the corporate debt market segment through the management of private placements as well as public issues. In private debt placement for FY22 (refers to the period from April 01 to March 31), AKCSL managed 121 assignments aggregating to ₹143,172 crore corresponding to a market share of 30.8%, as compared to 177 assignments aggregating to ₹255,228 crore in FY21. On a cumulative basis, AKCSL has managed 1,837 assignments till March 31, 2022, aggregating to ₹16.75 lakh crore (Source: Prime Database). It is also among the largest arrangers of debt for public-sector undertakings (PSUs), including tax-free bonds, private finance initiatives (PFIs), banks, and the private sector, having arranged bonds over ₹13.74 lakh crore over the last decade ended March 31, 2022 (10 years).
The management team of AKCSL is headed by AK Mittal, Managing Director, a first-generation entrepreneur and the promoter of the company, who has more than three decades of experience in the financial services sector and is well networked in the industry. The company has an experienced top and middle-level management team, the majority of whom have been with the group for a long time.

Strong institutional clientele: AKCSL, over the years, has built relationships with a large institutional client base, including leading Indian corporates, banks, non-banking financial institutions (NBFCs), financial institutions (FIs), provident funds, pension funds, insurance companies, mutual funds, alternate investment funds (AIFs), etc. As on September 30, 2022, the company had a client base of over 200 institutions and more than 1,000 provident and retirement funds. AKCSL participates in

[1]Complete definition of the ratings assigned are available at www.careedge.in and other CARE Ratings Ltd.'s publications

primary and secondary debt issuances based on the demand for the securities and holds the securities in its book for a short period (usually for a few days and up to three months) and sells them out to its client base. The majority of income includes merchant banking fees and investment income for the securities held.

Comfortable capitalisation with volatile gearing levels: AKCSL's standalone borrowing is largely in the form of working capital funding in order to participate in debt placement (primary as well as secondary issuances). As a result, AKCSL's standalone gearing levels are prone to volatility depending upon the debt placement volumes, investor appetite, and the quantum of debt underwritten. The overall gearing of AKCSL on a standalone basis stood at 1x as on September 30, 2022 (March 31, 2022: 1.04x).
ACKSL's consolidated reported net worth has been improving steadily due to internal accruals and stood at ₹793 crore as on September 30, 2022 (March 31, 2022: ₹755 crore). AKCSL's overall gearing (debt/tangible net worth) on a consolidated basis as on September 30, 2022, was 1.98x (March 31, 2022: 2.47x). The majority of the borrowings of the group pertain to A. K. Capital Finance Limited (AKCFL), which is an NBFC arm of the group engaged in lending (through loan and investment exposures) to corporate entities (largely NBFCs). The overall gearing of AKCFL on a standalone basis stood at 1.62x as on September 30, 2022 (March 31, 2022: 2.09x). The NBFC has a stated policy to maintain gearing levels of less than 3x. AKCFL reported a capital adequacy ratio (CAR) of 37.25% (March 31, 2022: 32.94%) and Tier-I CAR of 37.04% (March 31, 2022: 32.79%) as on September 30, 2022. AKCSL (the group) has been able to raise debt funds through bank borrowings and from debt capital markets at competitive rates.

Healthy asset quality: AKCSL is in the business of dealing of various fixed-income securities/instruments, ie, non-convertible debentures (NCDs), market-linked debentures (MLDs), pass through certificates (PTCs) and such other fixed-income securities. These securities are marketable and can be liquidated within a short span of time. Furthermore, the company deals in fixed-income securities with the minimum investment-grade rating category. The investments in AKCSL are liquidated within days to a few months, depending upon the demand for the securities and the company's ability to sell down.
AKCFL, on a standalone basis has a lending portfolio that comprises loans given to borrowers as well as investments in NCDs and other debt instruments. The company has maintained a healthy asset quality with nil non-performing assets (NPAs) over the last three years. As on September 30, 2022, around 88% (March 31, 2022: 87% and March 31, 2021: 93%) of the assets under management (AUM) of AKCFL on a standalone basis were in the government securities (G-Sec)/ 'A' category and above-rated papers, which provide reasonable strong liquidity as the company has the flexibility to sell down such assets.
Furthermore, of the total AUM of AKCFL on a standalone basis, which includes term loans, loans in the form of NCDs and other debt instruments, investments in G-Sec and other highly rated papers, around 18% of the total AUM exposure as on September 30, 2022 (March 31, 2022: 40% and March 31, 2021: 43%), is towards treasury book (G-Sec plus highly rated papers), which has low risk. AKCFL has sound risk management practices and is benefitted from the group's experience in the debt market in the assessment of the credit quality of the borrowers, which has helped it maintain good asset quality over the years.

Key weaknesses

Volatility in profitability parameters: AKCSL on a standalone basis derives the majority of its income by subscribing to debt instruments from the primary market and retailing them out to its client base. The transaction volumes depend upon the overall buoyancy in debt capital markets, which can exhibit periodic volatility and impact AKCSL's income. AKCSL's consolidated income profile consists of fee-based income earned from its merchant banking, brokerage, advisory, and syndication activities, which contributed 31.06% of its total income for H1FY23 (FY22: 24.73%) and fund-based income earned from its loan portfolio and investment book, which contributed 68.10% of its total income for H1FY23 (FY22: 74.21%).
For H1FY23, AKCSL's consolidated total income was ₹185.71 crore (FY22: ₹322.89 crore) and consolidated PAT was ₹41.51 crore (FY22: ₹83.01 crore). On a standalone basis, AKCSL reported a PAT of ₹14.59 crore (FY22: ₹26.32 crore) on a total income of ₹57.03 crore (FY22: ₹86.89 crore) for H1FY23.

Exposure to market risk with adverse movement in interest, impacting the profitability: The company is also exposed to market risks arising out of the adverse movement of prices of the securities, which are influenced by the level and changes in interest rates in the economy and developments in other markets, including credit and capital markets, international bond markets, and policy actions by the Reserve Bank of India (RBI). This may result into adverse price volatility on mark-to-market basis. In addition, the company may also face risks on account of its inability to liquidate holdings due to the non-availability of buyers for the securities. Due to the illiquidity, the company may need to sell at adverse prices.
The company manages the market risk through back-to-back sell down of majority of its securities and the remaining portion is generally sold within one to three months. AKCSL, being in the fixed-income industry for over two and a half decades, has built expertise and has been able to manage the interest rate risk quite effectively by tweaking its positions and maintaining its

profitability in volatile interest rate scenarios; however, managing profitability with the higher-than-expected movement in interest rates continues to be a key rating sensitivity.

High exposure to the corporate segment with relatively higher borrower concentration risk: The group has, over the years, maintained good asset quality. However, due to the nature of its exposures (in AKFCL), the company remains vulnerable to a high concentration in exposure, as it focuses on large ticket-size corporate lending to mainly financial services entities, a sector that has been under considerable stress for the past three years but has started to see improvement from FY22 onwards. The group continues to report nil NPAs and based on the historical track record of its AUM performance, the collection of contractual cash flow provides only the minimum provisions as per applicable regulatory guidelines. As the exposures of AKCFL are relatively large for its size, any slippages in its portfolio will require higher provisioning, which may impact its profitability and the group as a whole. AKCFL's top 10 borrowers on standalone basis in the lending segment (term loans plus loans in the form of NCDs) constituted around 35% (March 31, 2022: 27%) of the total AUM (lending segment plus treasury book) and 0.90x (March 31, 2022: 0.82x) of the tangible net worth, as on September 30, 2022. AKCFL is selective in taking exposures and investing in NCDs or lending to companies (mostly to NBFCs) with a minimum rating of BBB category. AKCSL's top five clients accounted for approximately 49% of the merchant banking income in FY22, thus resulting in a high concentration risk of revenue on a standalone basis (FY21: 36%).

Increasing competition in the merchant banking business: The number of lead arrangers has increased over a period of time, which has impacted the fees earned from debt placement as well as the transaction volume managed. Intensive competition in the merchant banking space, coupled with the high dependence on capital market conditions, may impact the company's earnings profile and profitability.

Liquidity: Adequate

AKCSL's standalone debt profile includes term loans of around ₹37.49 crore (outstanding as on September 30, 2022) and sanctioned working capital limits of ₹650 crore as on September 30, 2022. The company utilises the working capital facility in case of participation in debt issuances in the primary as well as secondary markets, a large proportion of which is typically down sold by the company to investors within a short period, post which the facilities are repaid. The average utilisation of the working capital was 34% for the last 12 months ended September 30, 2022. On a standalone basis, AKCSL has term debt repayments of ₹13.60 crore over the next year. The company has a stock of investment-grade debt securities of ₹504 crore as on September 30, 2022 (on a provisional basis), which are fairly liquid and provides comfort.

Applicable criteria

Policy on default recognition
Consolidation
Financial Ratios - Financial Sector
Short Term Instruments
Service Sector Companies
Non Banking Financial Companies

About the company – AKCSL

AKCSL is a SEBI-registered Category-I merchant banker. The company has been providing merchant banking services for over two and a half decades and is a leading player in the corporate debt market segment through the management of private placements as well as public issues. AKCSL is primarily involved in merchant banking activity and dealing in the fixed-income market, ie, buying and selling of rated debt securities (ie corporate bonds, G-Secs) and advisory activities. The merchant banking activities conducted by AKCSL involve corporate debt raising through private placement of bonds and debentures, initial public issue of bonds and debentures, project financing, working capital financing, financial advisors, etc.

AKCSL (Consolidated)

Brief Financials (₹ crore)	March 31, 2021 (A)	March 31, 2022 (A)	H1FY23 (UA)
Total income	289.15	322.89	185.71
PAT	75.05	83.01	41.51
Total assets	2,156.66	2,708.37	2,443.65
Net NPA (%)	Nil	Nil	Nil
ROTA (%)	4.02	3.41	3.22*

A: Audited; UA: Unaudited

* On Annualized Basis

AKCSL (Standalone)

Brief Financials (₹ crore)	March 31, 2021 (A)	March 31, 2022 (A)	H1FY23 (UA)
Total income	73.34	86.89	57.03
PAT	25.42	26.32	14.59
Total assets	541.50	917.77	920.64
ROTA (%)	5.10	3.61	3.18*
PAT Margin (%)	34.66	30.29	25.58

A: Audited; UA: Unaudited
* On Annualized Basis

Status of non-cooperation with previous CRA: Not applicable

Any other information: Not applicable

Rating history for the last three years: Please refer Annexure-2

Covenants of the rated instruments/facilities: Detailed explanation of covenants of the rated instruments/facilities is given in Annexure-3

Complexity level of the various instruments rated for this company: Annexure-4

Annexure-1: Details of instruments

Name of the Instrument	ISIN	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (₹ crore)	Rating Assigned along with Rating Outlook
Commercial paper (Standalone)	-	-	-	7-365 days	100.00	CARE A1+

Annexure-2: Rating history for the last three years

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating History			
		Type	Amount Outstanding (₹ crore)	Rating	Date(s) and Rating(s) assigned in 2022-2023	Date(s) and Rating(s) assigned in 2021-2022	Date(s) and Rating(s) assigned in 2020-2021	Date(s) and Rating(s) assigned in 2019-2020
1	Fund-based - LT-Bank overdraft	LT	-	-	-	-	-	1)Withdrawn (01-Apr-19)
2	Commercial paper-Commercial paper (Standalone)	ST	100.00	CARE A1+	1)CARE A1+ (19-Jul-22)	-	-	-

*Long term/short term.

Annexure-3: Detailed explanation of the covenants of the rated instruments

Not applicable

Annexure-4: Complexity level of the various instruments rated for this company

Sr. No.	Name of Instrument	Complexity Level
1.	Commercial paper (Standalone)	Simple

Annexure-5: Entities considered for consolidation

Sr. No.	Subsidiary	Extent of Consolidation (%)	Rationale for consolidation
1.	A.K. Capital Finance Limited (AKCFL)	98.73%	Subsidiary
2.	A.K. Stockmart Private Limited (AKSPL)	100.00%	Subsidiary
3.	A.K. Wealth Management Private Limited (AKWMPL)	100.00%	Subsidiary
4.	A.K. Capital Corporation Private Limited (AKCCPL)	100.00%	Subsidiary
5.	A.K. Capital (Singapore) PTE Limited (AK Singapore)	100.00%	Subsidiary
6.	Family Home Finance Private Limited	98.73%	Step Down Subsidiary

Note on complexity levels of the rated instruments: CARE Ratings has classified instruments rated by it on the basis of complexity. Investors/market intermediaries/regulators or others are welcome to write to care@careedge.in for any clarifications.

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About us:
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