A. K. Capital Services Limited

February 07, 2024

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

Details of instruments/facilities in Annexure-1

Rationale and key rating drivers

The rating assigned to the debt instrument 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; AKCSL being the flagship holding company of the group. The rating further factors in experience of the promoter and the management team, strong institutional client base, comfortable capitalisation with moderate gearing level and healthy asset quality.

The rating 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 – Factors that could lead to positive rating action/upgrade:

- Not applicable

Negative factors – Factors that could lead to negative rating action/downgrade:

- Substantial deterioration in 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 AKCSL's consolidated level.

Analytical approach

Consolidated. List of companies consolidated given in Annexure-6

Outlook: Not Applicable

Detailed description of the key rating drivers

Key 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. On a cumulative basis, AKCSL has managed 1,945 assignments till March 31, 2023, aggregating to approx. ₹19 lakh crore (Source: Prime Database).

In private debt placement for FY23 (refers to the period from April 01 to March 31), AKCSL managed 204 assignments aggregating to ₹275,531 crore corresponding to a market share of 42.90%, as compared to 121 assignments aggregating to ₹143,172 crore in FY22.

For H1FY24, AKCSL managed 107 assignments aggregating to ₹159,716 crore. It is also among the largest arrangers of debt for public sector undertaking (PSUs), including tax-free bonds, private finance institutions (PFIs), banks and the private sector having arranged bonds over assignments of private placement of debt, having arranged bonds over ₹15.67 lakh crore over the last decade ended March 31, 2023 (10 years).

The management team of AKCSL is headed by Mr. A.K. 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

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

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 participates in 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. Over the years, AKCSL 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, 2023, the company had a client base of over 200 institutions and more than 1,000 provident and retirement funds which helps in faster down-selling of securities.

Comfortable capitalisation and moderate but 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 1.34x as on September 30, 2023 (March 31, 2023: 1.08x).
AKCSL's consolidated net worth has been improving steadily due to internal accruals and stood at ₹871 crore as on September 30, 2023 (March 31, 2023: ₹835 crore). AKCSL's overall gearing (debt/tangible net worth) on a consolidated basis as on September 30, 2023, was 3.07x (March 31, 2023: 2.60x).

The majority of the borrowings of the group pertain to A. K. Capital Finance Limited (AKCFL), which is an non-banking finance company (NBFC) arm of the group engaged in lending (through loan and investment exposures) to corporate entities (largely NBFCs). AKCFL reported a capital adequacy ratio (CAR) of 30.99% (March 31, 2023: 33.56%) and a Tier-I CAR of 30.92% (March 31, 2023: 33.40%) as on September 30, 2023, with moderate overall gearing at 2.67x (March 31, 2023: 2.27x) as on September 30, 2023. 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, i.e. non-convertible debentures (NCDs), market-linked debentures (MLDs), pass through certificates (PTCs) and such other fixed-income securities with the minimum investment-grade rating category. These securities are marketable and can be liquidated within a short span of time ranging from a few days to a few months, depending upon the demand for the securities and the company's ability to sell down.
AKCFL's assets under management (AUM) on a standalone basis consists of lending book and treasury assets, each comprising 50% of the AUM as on September 30, 2023. The lending book comprises term loans and fixed-income securities/instruments given to companies in the banking and financial services segment, including NBFCs that are typically rated investment grade and above. The treasury book includes G-Sec plus highly rated papers that are more liquid and have relatively lower risk.

The company has maintained healthy asset quality over the last three and half years. As on September 30, 2023, around 84% (March 31, 2023: 83%) of the AUM was in G-Sec or 'A' category and above rated papers. AKCFL reported a gross non-performing assets (GNPA) ratio of 0.63% (March 31, 2023: 0.02%) and net non-performing assets (NNPA) of 0.38% (March 31, 2023: Nil) as on September 30, 2023 on loans and advances, with the company seeing delinquency in one account and minor slippages in the direct assignment (DA) retail portfolio bought out. AKCFL has sound risk management practices and has 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 28% of its total

income for H1FY24 (FY23: 26%) and fund-based income earned from its loan portfolio and investment book (including trading income), which contributed 72% of its total income for H1FY24 (FY23: 74%).

For H1FY24, AKCSL reported consolidated PAT of ₹42 crore (FY23: ₹88 crore) on total income of ₹241 crore (FY23: ₹407 crore). On a standalone basis, AKCSL reported a PAT of ₹15 crore (FY23: ₹31 crore) on a total income of ₹60 crore (FY23: ₹115 crore) for H1FY24.

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 in 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. CARE Ratings notes that in recent years, the volatility has increased in fixed-income markets with many fluctuations observed led by various domestic and international events.
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. AKCSL through AKCFL takes exposure through the lending book, where it lends by way of loans as well as investments in debt securities. It has a treasury book, which invests in G-Secs as well as high-rated securities, which provides the company with the flexibility to sell down and has helped it maintain good asset quality. However, due to the nature of its exposures, AKCFL remains vulnerable to a high concentration in exposure as it focuses on large ticket-size corporate lending to mainly financial service entities. 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.

The company's top 10 borrowers in the lending segment (term loans plus loans in the form of NCDs) constituted around 22% (March 31, 2023: 22%) of the total AUM (lending segment plus treasury book) and around 0.80x (March 31, 2023: 0.72x) of the total net worth (TNW) as on as on September 30, 2023. AKCFL is selective in taking exposures and investing in NCDs or lending to companies (mostly to NBFCs) with a minimum rating of BBB category.

On a standalone basis, AKCSL's top five clients accounted for approximately 69% of the merchant banking income in FY23 and 47% in H1FY24, thus resulting in a high concentration risk of revenue on a standalone basis (FY22: 49%).

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 ₹23.90 crore (outstanding as on September 30, 2023) and sanctioned working capital limits of ₹775 crore as on September 30, 2023. 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 47% for the last 12 months ended October 2023. On a standalone basis, AKCSL has term debt repayments of ₹6.53 crore up to March 2024. AKCSL had ₹254 crore worth of AAA rated (₹530 crore worth of AA & above) investments as on September 30, 2023, which can be readily liquidated.

Environment, social, and governance (ESG) risks:

AKCSL's board comprises of a total of eight directors out of which three are independent directors and one is woman director. The operations of the company are not energy intensive. However, adequate measures for conservation of energy, usage of alternate sources of energy and investments for energy conservation, wherever required have been taken. The company makes all efforts towards conservation of energy, protection of environment and ensuring safety.

The company recognizes the significance of robust IT infrastructure in the current era, where it is crucial to offer clients faster and more efficient services. Towards this end, the company makes investment each year to ensure adoption of best technologies that can streamline operations, brings in efficiency and enable to provide better customer service to make it more competitive in the market.

Applicable criteria

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

About the company and industry

Industry classification

Macro-economic Indicator	Sector	Industry	Basic Industry
Financial services	Financial services	Capital markets	Other capital market-related services

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, among others.

AKCSL (Consolidated)

Brief Financials (₹ crore)	March 31, 2022 (A) 12 M	March 31, 2023 (A) 12 M	September 30, 2023 (UA) 6M
Total income	322.89	406.81	240.96
PAT	83.01	88.42	42.31
Total assets	2,708.36	3,113.26	3,650.62
Net NPA (%)	Nil	Nil	Nil
ROTA (%)	3.41	3.04	2.50*

A: Audited; UA: Unaudited. Note: The above results are the latest financial results considered.
*On an annualised basis

AKCSL (Standalone)

Brief Financials (₹ crore)	March 31, 2022 (A) 12 M	March 31, 2023 (A) 12 M	September 30, 2023 (UA) 6M
Total income	86.89	115.35	59.79
PAT	26.32	30.71	14.87
Total assets	917.65	938.38	1,135.91
ROTA (%)	3.61	3.23	2.81*
PAT Margin (%)	30.29	26.63	24.87

A: Audited; UA: Unaudited. Note: The above results are the latest financial results considered.
*On an annualised 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 the covenants of the rated instruments/facilities is given in Annexure-3

Complexity level of the various instruments rated: Annexure-4

Lender details: Annexure-5

Annexure-1: Details of instruments/facilities

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-Commercial paper (Standalone)	INE701G14148	13-Oct-23	8.75%	19-Apr-24	50.00	CARE A1+
Commercial paper-Commercial paper (Standalone)	INE701G14155	12-Jan-24	8.75%	10-Jul-24	1.00	CARE A1+
Commercial paper-Commercial paper (Standalone)	INE701G14155	12-Jan-24	9.00%	10-Jul-24	49.00	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 2023-2024	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
1	Commercial paper-Commercial paper (Standalone)	ST	100.00	CARE A1+	-	1)CARE A1+ (13-Feb-23) 2)CARE A1+ (19-Jul-22)	-	-

*Long term/Short term.

Annexure-3: Detailed explanation of the covenants of the rated instruments/facilities: Not Applicable

Annexure-4: Complexity level of the various instruments rated

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

Annexure-5: Lender details: Not Applicable

Annexure-6: Entities considered for consolidation as on September 30, 2023

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	100.00%	Subsidiary
3.	A.K. Wealth Management Private Limited	100.00%	Subsidiary
4.	A.K. Capital Corporation Private Limited	100.00%	Subsidiary
5.	A.K. Capital (Singapore) PTE Limited	100.00%	Subsidiary
6.	Family Home Finance Private Limited	98.73%	Step Down Subsidiary
7.	A. K. Alternative Asset Managers Private Limited	100.00%	Step Down Subsidiary

Note on the 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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