

Rating Rationale

December 28, 2023 | Mumbai

Surat Municipal Corporation

Rating Reaffirmed

Rating Action

Rs.200 Crore Bond	CRISIL AA+/Stable (Reaffirmed)
--------------------------	---------------------------------------

Note: None of the Directors on CRISIL Ratings Limited's Board are members of rating committee and thus do not participate in discussion or assignment of any ratings. The Board of Directors also does not discuss any ratings at its meetings.

1 crore = 10 million

Refer to Annexure for Details of Instruments & Bank Facilities

Detailed Rationale

CRISIL Ratings has reaffirmed its 'CRISIL AA+/Stable' rating on the taxable bonds of Surat Municipal Corporation (SMC).

The rating continues to reflect the strength of trustee-administered escrow account, payment mechanism and adequate liquidity in the form of a debt service reserve account (DSRA) amounting to 12 months of interest servicing (*payment mechanism for coupon and redemption is given in the annexure*).

The rating also reflects the strong creditworthiness and low performance risk of the originator, high debt service coverage ratio (DSCR) leading to low impact of future flow on originators' other obligations, additional security in the form of DSRA created before pay-in, presence of a payment structure and recourse to the originator.

The rating also considers the robust operating performance and strong financial risk profile of the corporation, driven by healthy operating surplus, small debt, superior liquidity, and adequate debt protection metrics. Furthermore, SMC has a sound economic base, adequate service levels, optimal collection efficiency of taxes and charges, and good reform orientation.

These strengths are partially offset by heavy reliance on state government grants and large capital expenditure (capex) requirement.

Analytical Approach

To arrive at its rating, CRISIL Ratings has applied its criteria on future flow securitisation.

Key Rating Drivers & Detailed Description

Strengths:

Strength of the escrow mechanism

The escrow and bond payment mechanism provide adequate strength to the bond issuance. The tax receipts escrowed at collection, trustee-managed escrow mechanism and payment structure with recourse to originator ensure adequate safety for timely debt repayment to investors. The creation of the DSRA before pay-in and maintenance of the same throughout the tenure of the bond further enhance the strength of the structure. The DSCR is also expected to be high throughout the tenure of the bond.

Strong financial performance, reflected in healthy operating surplus

Revenue includes income from collection of property tax, user charges for water and sewerage service, income from other taxes such as professional tax, octroi compensation, other revenue grants, and other non-tax income. Revenue surplus is healthy, backed by strong property tax collection and steady receipt of grants from the state government in lieu of octroi and non-tax income comprising town development income. Fiscal 2023 revenue surplus of Rs 396 crore was in line with the previous fiscal's surplus of Rs 408 crore, given increased establishment expenses. The corporation has revised property tax, other tax and user charges, which increased revenue surplus (before sinking fund contribution) to Rs 485 crore as of November 2023 (vs Rs 436 crore for the full fiscal 2023).

Strong financial risk profile

Healthy operating surplus has helped to fund the increasing capex through internal cash accrual, leading to low reliance on debt. As on March 31, 2023, outstanding debt was Rs 200 crore (on account of municipal bonds raised in March 2019). Robust cash flow generates ample liquidity. Unencumbered cash and cash equivalents stood at over Rs 645 crore as on March 31, 2023, including bank balance and fixed deposits. SMC is expected to maintain its cash balances over the medium term.

The corporation has large capex planned under the Atal Mission for Rejuvenation and Urban Transformation (AMRUT) and Smart City projects, which is being funded through a mix of government grants and own revenue surplus. Despite the debt, debt protection metrics have remained strong and should remain so over the medium term due to no incremental borrowings as on date.

Adequate service levels and healthy collection efficiency of taxes and charges

SMC has strong civic infrastructure and robust delivery systems. This is reflected in good water supply coverage, adequate road and sewerage networks, and improving drainage and solid waste management practices.

Current collection efficiency of property tax has steadily increased after Covid to ~94% from ~91% in FY22. Cost of recovery for essential services is among the highest compared with other corporations in the state. Implementation of AMRUT and

Smart City projects should further drive improvement in service-level arrangements and result in increased collection efficiency of taxes and charges.

Sound economic base

The robust industrial base of Surat, its favourable location, strategic importance in the state, and high per-capita income have led to sound economic base. Industries in Gujarat have flourished due to favourable state government policies, affordable cost of living, surplus labour, and low transportation cost.

Weaknesses:

High dependence on state government grants

Although the share of grants and compensation from the state government has steadily reduced to 25% in fiscal 2023 from 45% in fiscal 2013, it continues to be a major part of total revenue receipts. Since the abolition of octroi in fiscal 2008, the corporation has been consistently receiving compensation from the state government. In fiscal 2023, Rs 774 crore was received as octroi compensation. With rise in property tax rates and non-tax revenue, dependence on government grants is likely to further reduce over the medium term. Additionally, SMC has strong liquidity to partly fund proposed capex in case of any delay in receipt of the grants.

Large capex requirement

The large capex requirement over the medium term would be for implementing the AMRUT and Smart City schemes, Dumas sea face, Barrage projects and other planned expenditure. The estimated project cost under these schemes is ~Rs 5,000 crore, spread over five fiscals.

A healthy operating surplus is likely to be maintained and no sizeable debt is expected to be contracted. However, any significant increase in capex, leading to substantial incremental debt, could weaken financial risk profile and will remain a key rating monitorable.

Liquidity: Superior

Liquidity is driven by healthy revenue surplus of ~Rs 400 crore annually over the past five fiscals, and unencumbered cash and bank balance of over Rs 645 crore as on March 31, 2023. SMC is likely to maintain unencumbered cash and bank balance and continue to generate healthy operating surplus to meet future debt obligation and part-funded capex.

Outlook: Stable

SMC will continue to generate healthy operating surplus over the medium term while maintaining strong debt protection metrics.

Rating Sensitivity factors

Upward factors

- Significant improvement in service arrangements such as water supply, sewerage, and solid waste management
- Increased collection efficiency in existing own-revenue sources and generation of income from additional sources
- Substantial and sustained increase in operating surplus to over 30%

Downward Factors

- Significant decline in collection of property tax
- Fall in operating surplus to below 15% on a sustainable basis, thereby weakening debt protection metrics
- Reduction in support from the state government in terms of adequacy and timeliness of octroi compensation, and availability of funds under AMRUT and Smart City schemes and other grants
- Any adverse change in the payment structure mechanism

About the Company

SMC is one of the largest municipal corporations in Gujarat and governed by the Bombay Provincial Municipal Corporation Act, 1949, as amended by the Government of Gujarat. It has jurisdiction over 462.15 square kilometres. Services include water supply, sewerage disposal, solid waste management, primary education, public safety, transportation, and slum improvement.

Key Financial Indicators

As on / for the period ended March 31	Units	2023	2022
Revenue receipts	Rs crore	3612	3370
Revenue surplus	Rs crore	396	408
Revenue surplus/ revenue receipts	%	11	12

Any other information:

Broad contours of the escrow structure:

- The tenure is five years with half-yearly coupon payment
- Bullet/full redemption at the end of five years
- Escrow of property tax and user charges collected by and due to SMC-eligible bondholders and lenders shall have first and pari passu charge over the escrow account, debt service account (DSA), and the collection account(s).
- Establishing separate DSA, DSRA, interest payment accounts (IPA), and sinking fund accounts (SFA) with the escrow banker as per the terms of each series. Bondholders/lenders of a particular series have first and pari passu charge over DSA, DSRA, IPA, and SFA for the respective series.
- In case of any shortfall during transfer from the escrow account to DSA, SMC shall compensate with funds from other account(s) to DSA.

Interest payment mechanism

T – Interest payment date

Day	
T-25	The trustees shall check the amount lying to the credit of IPA. In case of any shortfall in amount, the trustees shall intimate SMC
T-15	SMC shall make good the shortfall in the IPA, if applicable

T-14	In case of shortfall, trustees shall trigger the payment mechanism and instruct the bank to transfer the shortfall amount from the DSRA to the IPA
T-10	The bank shall transfer the shortfall amount, if applicable*
T	Interest payment is done

*Any amount drawn from the DSRA should be deposited back in the account

Redemption mechanism

T – Redemption date

Day	
T-25	The trustees shall check the amount lying to the credit of the SFA. In case of any shortfall in amount, the trustees shall intimate SMC
T-15	SMC shall make good the shortfall in the SFA
T	Redemption payment is done

Any other information: Not Applicable

Note on complexity levels of the rated instrument:

CRISIL Ratings` complexity levels are assigned to various types of financial instruments and are included (where applicable) in the 'Annexure - Details of Instrument' in this Rating Rationale.

CRISIL Ratings will disclose complexity level for all securities - including those that are yet to be placed - based on available information. The complexity level for instruments may be updated, where required, in the rating rationale published subsequent to the issuance of the instrument when details on such features are available.

For more details on the CRISIL Ratings` complexity levels please visit www.crisilratings.com. Users may also call the Customer Service Helpdesk with queries on specific instruments.

Annexure - Details of Instrument(s)

ISIN	Type of instrument	Date of allotment	Coupon	Maturity date	Issue size (Rs.Crore)	Complexity Level	Rating assigned with outlook
INE05NX24015	Taxable bonds	01-Mar-2019	8.68%	01-Mar-2024	200	Simple	CRISIL AA+/Stable

Annexure - Rating History for last 3 Years

		Current		2023 (History)		2022		2021		2020		Start of 2020
Instrument	Type	Outstanding Amount	Rating	Date	Rating	Date	Rating	Date	Rating	Date	Rating	Rating
Bond	LT	200.0	CRISIL AA+/Stable	18-01-23	CRISIL AA+/Stable	19-01-22	CRISIL AA+/Stable	26-02-21	CRISIL AA+/Stable	28-02-20	CRISIL AA+/Stable	CRISIL AA+/Stable

All amounts are in Rs.Cr.

Criteria Details

Links to related criteria
Rating Criteria for Municipal and Urban Local Bodies
CRISILs rating methodology for future flow securitisation
The Rating Process
CRISILs Bank Loan Ratings - process, scale and default recognition
CRISILs Approach to Financial Ratios
Understanding CRISILs Ratings and Rating Scales

Media Relations	Analytical Contacts	Customer Service Helpdesk
<p>Aveek Datta Media Relations CRISIL Limited M: +91 99204 93912 B: +91 22 3342 3000 AVEEK.DATTA@crisil.com</p> <p>Prakruti Jani Media Relations CRISIL Limited M: +91 98678 68976 B: +91 22 3342 3000 PRAKRUTI.JANI@crisil.com</p> <p>Rutuja Gaikwad Media Relations CRISIL Limited B: +91 22 3342 3000 Rutuja.Gaikwad@ext-crisil.com</p>	<p>Anuj Sethi Senior Director CRISIL Ratings Limited B: +91 44 6656 3100 anuj.sethi@crisil.com</p> <p>Aditya Jhaver Director CRISIL Ratings Limited B: +91 22 3342 3000 aditya.jhaver@crisil.com</p> <p>Latika Shyam Lala Senior Rating Analyst CRISIL Ratings Limited B: +91 22 3342 3000 Latika.Lala@crisil.com</p>	<p>Timings: 10.00 am to 7.00 pm Toll free Number: 1800 267 1301</p> <p>For a copy of Rationales / Rating Reports: CRISILratingdesk@crisil.com</p> <p>For Analytical queries: ratingsinvestordes@crisil.com</p>

Note for Media:

This rating rationale is transmitted to you for the sole purpose of dissemination through your newspaper/magazine/agency. The rating rationale may be used by you in full or in part without changing the meaning or context thereof but with due credit to CRISIL Ratings. However, CRISIL Ratings alone has the sole right of distribution (whether directly or indirectly) of its rationales for consideration or otherwise through any media including websites and portals.

About CRISIL Ratings Limited (A subsidiary of CRISIL Limited, an S&P Global Company)

CRISIL Ratings pioneered the concept of credit rating in India in 1987. With a tradition of independence, analytical rigour and innovation, we set the standards in the credit rating business. We rate the entire range of debt instruments, such as bank loans, certificates of deposit, commercial paper, non-convertible/convertible/partially convertible bonds and debentures, perpetual bonds, bank hybrid capital instruments, asset-backed and mortgage-backed securities, partial guarantees and other structured debt instruments. We have rated over 33,000 large and mid-scale corporates and financial institutions. We have also instituted several innovations in India in the rating business, including ratings for municipal bonds, partially guaranteed instruments and infrastructure investment trusts (InvITs).

CRISIL Ratings Limited ('CRISIL Ratings') is a wholly-owned subsidiary of CRISIL Limited ('CRISIL'). CRISIL Ratings Limited is registered in India as a credit rating agency with the Securities and Exchange Board of India ("SEBI").

For more information, visit www.crisilratings.com

About CRISIL Limited

CRISIL is a leading, agile and innovative global analytics company driven by its mission of making markets function better.

It is India's foremost provider of ratings, data, research, analytics and solutions with a strong track record of growth, culture of innovation, and global footprint.

It has delivered independent opinions, actionable insights, and efficient solutions to over 100,000 customers through businesses that operate from India, the US, the UK, Argentina, Poland, China, Hong Kong and Singapore.

It is majority owned by S&P Global Inc, a leading provider of transparent and independent ratings, benchmarks, analytics and data to the capital and commodity markets worldwide.

For more information, visit www.crisil.com

Connect with us: [TWITTER](#) | [LINKEDIN](#) | [YOUTUBE](#) | [FACEBOOK](#)

CRISIL PRIVACY NOTICE

CRISIL respects your privacy. We may use your contact information, such as your name, address and email id to fulfil your request and service your account and to provide you with additional information from CRISIL. For further information on CRISIL's privacy policy please visit www.crisil.com.

DISCLAIMER

This disclaimer is part of and applies to each credit rating report and/or credit rating rationale ('report') that is provided by CRISIL Ratings Limited ('CRISIL Ratings'). To avoid doubt, the term 'report' includes the information, ratings and other content forming part of the report. The report is intended for the jurisdiction of India only. This report does not constitute an offer of services. Without limiting the generality of the foregoing, nothing in the report is to be construed as CRISIL Ratings providing or intending to provide any services in jurisdictions where CRISIL Ratings does not have the necessary licenses and/or registration to carry out its business activities referred to above. Access or use of this report does not create a client relationship between CRISIL Ratings and the user.

We are not aware that any user intends to rely on the report or of the manner in which a user intends to use the report. In preparing our report we have not taken into consideration the objectives or particular needs of any particular user. It is made abundantly clear that the report is not intended to and does not constitute an investment advice. The report is not an offer to sell or an offer to purchase or subscribe for any investment in any securities, instruments, facilities or solicitation of any kind to enter into any deal or transaction with the entity to which the report pertains. The report should not be the sole or primary basis for any investment decision within the meaning of any law or regulation (including the laws and regulations applicable in the US).

Ratings from CRISIL Ratings are statements of opinion as of the date they are expressed and not statements of fact or recommendations to purchase, hold or sell any securities/instruments or to make any investment decisions. Any opinions expressed here are in good faith, are subject to change without notice, and are only current as of the stated date of their issue. CRISIL Ratings assumes no obligation to update its opinions following publication in any form or format although CRISIL Ratings may disseminate its opinions and analysis. The rating contained in the report is not a substitute for the skill, judgment and experience of the user, its management, employees, advisors and/or clients when making investment or other business decisions. The recipients of the report should rely on their own judgment and take their own professional advice before acting on the report in any way. CRISIL Ratings or its associates may have other commercial transactions with the entity to which the report pertains.

Neither CRISIL Ratings nor its affiliates, third-party providers, as well as their directors, officers, shareholders, employees or agents (collectively, 'CRISIL Ratings Parties') guarantee the accuracy, completeness or adequacy of the report, and no CRISIL

Ratings Party shall have any liability for any errors, omissions or interruptions therein, regardless of the cause, or for the results obtained from the use of any part of the report. EACH CRISIL RATINGS PARTY DISCLAIMS ANY AND ALL EXPRESS OR IMPLIED WARRANTIES, INCLUDING BUT NOT LIMITED TO ANY WARRANTIES OF MERCHANTABILITY, SUITABILITY OR FITNESS FOR A PARTICULAR PURPOSE OR USE. In no event shall any CRISIL Ratings Party be liable to any party for any direct, indirect, incidental, exemplary, compensatory, punitive, special or consequential damages, costs, expenses, legal fees or losses (including, without limitation, lost income or lost profits and opportunity costs) in connection with any use of any part of the report even if advised of the possibility of such damages.

CRISIL Ratings may receive compensation for its ratings and certain credit-related analyses, normally from issuers or underwriters of the instruments, facilities, securities or from obligors. Public ratings and analysis by CRISIL Ratings, as are required to be disclosed under the regulations of the Securities and Exchange Board of India (and other applicable regulations, if any), are made available on its website, www.crisilratings.com (free of charge). Reports with more detail and additional information may be available for subscription at a fee - more details about ratings by CRISIL Ratings are available here: www.crisilratings.com.

CRISIL Ratings and its affiliates do not act as a fiduciary. While CRISIL Ratings has obtained information from sources it believes to be reliable, CRISIL Ratings does not perform an audit and undertakes no duty of due diligence or independent verification of any information it receives and/or relies on in its reports. CRISIL Ratings has established policies and procedures to maintain the confidentiality of certain non-public information received in connection with each analytical process. CRISIL Ratings has in place a ratings code of conduct and policies for managing conflict of interest. For details please refer to: <https://www.crisil.com/en/home/our-businesses/ratings/regulatory-disclosures/highlighted-policies.html>.

Rating criteria by CRISIL Ratings are generally available without charge to the public on the CRISIL Ratings public website, www.crisilratings.com. For latest rating information on any instrument of any company rated by CRISIL Ratings, you may contact the CRISIL Ratings desk at crisilratingdesk@crisil.com, or at (0091) 1800 267 1301.

This report should not be reproduced or redistributed to any other person or in any form without prior written consent from CRISIL Ratings.

All rights reserved @ CRISIL Ratings Limited. CRISIL Ratings is a wholly owned subsidiary of CRISIL Limited.

CRISIL Ratings uses the prefix 'PP-MLD' for the ratings of principal-protected market-linked debentures (PPMLD) with effect from November 1, 2011, to comply with the SEBI circular, "Guidelines for Issue and Listing of Structured Products/Market Linked Debentures". The revision in rating symbols for PPMLDs should not be construed as a change in the rating of the subject instrument. For details on CRISIL Ratings' use of 'PP-MLD' please refer to the notes to Rating scale for Debt Instruments and Structured Finance Instruments at the following link: <https://www.crisil.com/en/home/our-businesses/ratings/credit-ratings-scale.html>