December 21, 2023

Vijayawada Municipal Corporation: Long-term rating upgraded to [ICRA]BBB (Stable) and removed from Issuer Not-Cooperating Category

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term – Fund based – Term Loan	154.00	97.67	[ICRA]BBB (Stable); Rating upgraded from [ICRA]BB+ (Stable) ISSUER NOT COOPERATING and removed from Issuer Not Cooperating category
Long-term – Unallocated	22.00	78.33	[ICRA]BBB (Stable); Rating upgraded from [ICRA]BB+ (Stable) ISSUER NOT COOPERATING and removed from Issuer Not Cooperating category
Total	**176.00**	**176.00**	

**Instrument details are provided in Annexure-I*

Rationale

Vijayawada Municipal Corporation's (VMC) rating has been removed from the Issuer Not Cooperating category and its long-term rating has been upgraded. The rating action follows cooperation from the entity in providing required information for undertaking rating action. The assigned rating derives comfort from the healthy financial profile of VMC, the provider of key municipal services in Vijayawada city and the strategic importance of the city to the Government of Andhra Pradesh (GoAP). The rating also takes into consideration the credit quality of the state government. Vijayawada is one of the largest cities in Andhra Pradesh and the nearest city to Amaravati, which is one of the three proposed capital regions of the state and is likely to attract investment in infrastructure, which augurs well for the development of the city. The assigned rating considers substantial contribution (more than 90%) of VMC's own tax and non-tax revenues to the total revenue receipts of the corporation with low dependence on grants from the state government. The corporation has been generating revenue surplus over the years, enabling it to part fund its capital expenditure requirements from internal sources. ICRA notes that from April 2019, the state government absorbed the permanent employees and consequently their salaries are being paid directly by GoAP, providing significant comfort to VMC's financial health. Further, supported by healthy surplus and reducing debt, the ULB's leverage and coverage indicators as well as liquidity remain comfortable.

The rating is, however, constrained by the limited growth potential of VMC's property tax and other key charges, though the collection efficiency has remained satisfactory. ICRA notes that VMC has changed the computation method of property tax to capital value from rental value in FY2022, which resulted in an increase in current demand and higher collections in FY2023. However, its ability to revise its tax rates and charges on a regular basis would remain a challenge. The corporation's service levels in the areas of solid waste management (SWM), road availability in the service area, water supply availability and sewerage treatment remain satisfactory. However, significant scope of improvement remains in the area related to municipal solid waste (MSW) treatment, metered water supply connections (limited household connections metered at present), upgradation of water supply and sewerage network, and drainage coverage, which would require VMC to undertake large projects to improve the service levels. The rating is also constrained by the risks associated with any large unanticipated expenditure responsibility without any funding support and a delay in transfer of rule-based revenues from the state government, credit quality of which has deteriorated during the recent years. While ICRA notes that several projects are to be undertaken by VMC under the Atal Mission for Rejuvenation and Urban Transformation (AMRUT 2.0) scheme, its ability to execute large and complex projects within the estimated budgets and timely arrangement of funds for the projects are yet to be seen. Nevertheless, ICRA expects that VMC will derive partial support from the Central/state governments for funding the projects and for capacity building of the municipal staff, which are likely to mitigate risks related to execution of large projects to an extent. ICRA notes that the corporation has successfully implemented several reforms in its e-governance system such as online collection of most of the revenues and implementation of Enterprise Resource Planning (ERP) system.

The Stable outlook on VMC's long-term rating reflects ICRA's opinion that VMC will continue to benefit from Vijayawada's strategic importance to the state government for being one of the largest cities as well as economic hub in the state and part of the three proposed capital regions, which would support its growth in its high own tax revenue base and surplus position.

Key rating drivers and their description

Credit strengths

Strategic importance to the state government – Vijayawada is one of the largest cities in Andhra Pradesh and is the nearest city to Amaravati. The city is likely to attract investment in infrastructure, which augurs well for the development of the city. It is also one of the hubs for economic activities in the state, which enhances the revenue potential for VMC.

Substantial contribution of own tax and non-tax revenue receipts reduces dependence on the state government –VMC derives more than 90% of its revenue receipts from its own tax and non-tax revenue sources in FY2023, indicating limited reliance on grants and assigned revenue transfers from the state government. Moreover, the collection efficiency of property tax and water supply user charges has remained satisfactory.

Healthy financial profile –VMC generated healthy revenue balance (more than Rs. 100.0 crore) over the years, led primarily by consistent and healthy income from its own tax and non-tax revenue receipts and relatively restricted revenue expenditure. ICRA notes that from April 2019, the state government absorbed the permanent employees and consequently their salaries are being paid directly by the GoAP, providing significant comfort to VMC's financial health. The revenue surplus position has enabled it to fund a part of its capital expenditure from internal resources, while maintaining a healthy closing cash balance position. Consequently, with reducing debt and healthy surplus, VMC's debt coverage metrics and liquidity remain comfortable.

Credit challenges

Limited growth potential of property tax and other key revenue base – The area covered by the ULB is limited and therefore it limits the growth potential for property tax and other key charges. Further, the property tax tariff revision has been irregular, limiting the ULB's ability to grow its property tax base. While the property tax rates have not been revised since a long time, upward revision in water supply user charges has been regular, though its base remains small. ICRA notes that VMC has changed the computation method of property tax to capital value from rental value in FY2022, which resulted in an increase in current demand and higher collections in FY2023. However, regular revision in the revised property tax base would be a key credit challenge, going forward.

Scope of improvement in some services will require significant capex – The corporation has significant scope of improvement in MSW treatment, metered water supply connections (limited household connections metered at present), upgradation of water supply and sewerage network, and drainage coverage. Nevertheless, service levels of VMC in the areas of solid waste management (100% MSW collection) with door-to-door collection and segregation, water supply availability (~215 litres per capita per day), and street light coverage (~32 street lights poles per km) remain satisfactory. A significant capex would be needed in the required areas to improve the service levels, for which the ULB will have to mobiles funds.

Risk associated with any unanticipated large expenditure and delay in timely release of rule-based transfers from the state government – During the recent years, the credit quality of the state government has deteriorated due to which the ULB is exposed to the risk of being burdened with additional large expenditure such as large projects, payment to staff etc. without any funding support, considering VMC's healthy financial position. Consequently, the revenue balances and liquidity of the ULB could be impacted to that extent. Further, any delay in timely release of rule-based transfers such as stamp duty share could also impact VMC's liquidity.

Sizeable capital outlays envisaged – A large capital contribution by VMC would be required for the execution of capital-intensive projects under AMRUT 2.0 for execution of water supply and sewerage development projects. This could stretch the cash flows of the corporation, especially while executing long-term capital intensive projects. Moreover, given the limited experience of the municipal staff in handling such large and complex projects, the ability of the corporation to timely execute these projects within the estimated budget and timely funding of the projects by VMC would be important.

Liquidity position: Adequate

VMC's liquidity is adequate with an estimated revenue balance of Rs. 100-110 crore in FY2024 against annual repayments of around Rs. 18.0 crore. Further, the corporation had its own cash and bank balance (excluding balance funds earmarked towards specific projects) of more than Rs. 150 crore as of March 2023, which is adequate to meet its share of funding for various projects as well as any urgent need. The corporation's liquidity derives significant comfort from the absorption of its permanent employees by the state government since FY2020. The salary and other related payments of such employees are made directly by the state government from its own treasury, which significantly reduces VMC's establishment expenses. Any adverse change in this arrangement by the state government, leading to pressure on the VMC's healthy revenue balance position and liquidity, would be key rating sensitivity.

Rating sensitivities

Positive factors – The rating could be upgraded if VMC demonstrates substantial growth in its revenues on a sustained basis, along with an improvement in its service indicators in the areas related to MSW treatment, metered water supply connections, upgradation of water supply and sewerage network, and drainage coverage.

Negative factors – ICRA could downgrade the rating if a decline in the ULB's revenue balance, or lower/delayed cash flows from the state government adversely impacts VMC's liquidity on a sustained basis. Also, higher-than-estimated increase in debt levels, weakening its leverage and coverage metrics, would be a key credit negative.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	[Corporate Credit Rating Methodology](#) [Rating Methodology for Urban Local Bodies](#)
Parent/Group support	The assigned rating factors in VMC's importance to GoAP as a provider of urban infrastructure and basic services within the city, as well as its strong operational and financial linkages with the GoAP
Consolidation/Standalone	Standalone

About the company

VMC was upgraded to a municipal corporation in 1981 from a selection grade municipality and is governed by the Andhra Pradesh Municipal Corporations Act 1994 (Act). It manages municipal services in Vijayawada city in the Andhra Pradesh Capital Region (area of 8,603 square kilometre (sq. km.) surrounding the new capital, Amaravati). The Vijayawada city is situated on the banks of River Krishna in Krishna district of Andhra Pradesh, which is one of the main trading and business centres in the state. VMC covers an area of 61.88 sq. km. and serves a population of 10.4 lakh (as per Census 2011). Its major functions include water supply, solid waste management and construction, repair and maintenance of roads and streetlights in its area. The Council, which governs the ULB, comprises 64 Ward Councillors and is headed by a Mayor, who is elected by the Ward Councillors. The regular operations of the corporation are supervised by the Commissioner, who is appointed by the state government and is supported by the heads of various departments.

Key financial indicators (audited)

Standalone (Actuals)	FY2022	FY2023*
Revenue income (Rs. crore.)	298.66	389.05
Revenue expenditure (Rs. crore)	192.18	196.81
Revenue balance (Rs. crore)	106.48	192.24
Closing cash balance (Rs. crore)	260.79	426.45
Revenue balance / Revenue income (%)	35.7%	49.4%
(Principal + Interest) / Revenue income (%)	9.8%	7.9%
(Revenue balance + Interest)/ (Interest + debt repayment)	4.0	6.6
Debt/ Revenue income (%)	41.6%	25.1%

*Source: VMC; ICRA Research; *Provisional figures*

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2024)				Chronology of Rating History for the past 3 years		
		Type	Amount Rated (Rs. crore)	Amount Outstanding as on Nov 30, 2023 (Rs. crore)	Date & rating in FY2024	Date & rating in FY2023	Date & rating in FY2022	Date & rating in FY2021
					Dec 21, 2023	Oct 31, 2022	July 16, 2021	-
1	Fund-based – Term Loan	Long-term	97.67	88.60	[ICRA]BBB (Stable)	[ICRA]BB+ (Stable) ISSUER NOT COOPERATING	[ICRA]BB+ (Stable) ISSUER NOT COOPERATING	-
2	Unallocated limits	Long-term	78.33	-	[ICRA]BBB (Stable)	[ICRA]BB+ (Stable) ISSUER NOT COOPERATING	[ICRA]BB+ (Stable) ISSUER NOT COOPERATING	-

Source: VMC

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long-term fund-based – Term Loan	Simple
Long-term – Unallocated	Not Applicable

The Complexity Indicator refers to the ease with which the returns associated with the rated instrument could be estimated. It does not indicate the risk related to the timely payments on the instrument, which is rather indicated by the instrument's credit rating. It also does not indicate the complexity associated with analysing an entity's financial, business, industry risks or complexity related to the structural, transactional or legal aspects. Details on the complexity levels of the instruments are available on ICRA's website: Click Here

Annexure I: Instrument details

ISIN	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	**Long-term fund-based – Term Loan**	FY2011	NA	FY2028	20.98	[ICRA]BBB (Stable)
NA	**Long-term fund-based – Term Loan**	FY2019	NA	FY2033	76.69	[ICRA]BBB (Stable)
NA	**Long-term – Unallocated**	NA	NA	NA	78.33	[ICRA]BBB (Stable)

Source: VMC

Please click here to view details of lender-wise facilities rated by ICRA

Annexure II: List of entities considered for consolidated analysis: Not Applicable

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About ICRA Limited:

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