

March 30, 2020

## Vijayawada Municipal Corporation: Rating reaffirmed and removed from Issuer not cooperating category

### Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Term loans	75.56	154.0	[ICRA]A- (Stable); Reaffirmed and removed from Issuer not cooperating category
Unallocated limits	100.44	22.0	
<b>Total</b>	<b>176.00</b>	<b>176.00</b>	

\*Instrument details are provided in Annexure-1

### Rationale

The assigned rating continues to derive comfort from the healthy financial profile of the Vijayawada Municipal Corporation (VMC), the provider of key municipal services in Vijayawada city, and the strategic importance of the city to the Government of Andhra Pradesh (GoAP). Vijayawada is one of the three proposed capital regions and is likely to attract investment in infrastructure, which augurs well for the development of the city. The assigned rating considers the substantial contribution (more than 80%) 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 surpluses over the years, enabling it to part fund its capital expenditure requirements from internal sources. Till FY2019, it self-funded salaries for its permanent employees, unlike other ULBs, where the same is funded by the state government. However, from April 2019 onwards, the state government is responsible for paying permanent staff salaries, which augurs well for VMC. Although the revenue surplus was over Rs. 60 crore till FY2018, it moderated to Rs. 13 crore in FY2019 owing to lower revenue grants. Nevertheless, higher capital grants resulted in healthy overall surplus. Further, its leverage and coverage metrics have remained comfortable.

While VMC's current property tax collection efficiency for key tax revenue sources – property tax and user charges – has been satisfactory, its track record of regular revision in property tax rates and user charges (linked to property tax slabs) has remained less than satisfactory. As a result, the growth in its tax revenues and user charges during the recent years has been constrained, thereby limiting its own revenue base. 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 remains satisfactory. However, the service levels with respect to coverage of sewerage, metered water supply connections and road surfacing remain low, limiting VMC's ability to increase its non-tax revenue base. Moreover, the scientific treatment of collected municipal solid waste (MSW) is yet to be taken up. While ICRA notes that several projects are to be undertaken by VMC under the Atal Mission for Rejuvenation and Urban Transformation (AMRUT) scheme, its ability to execute large and complex projects within the estimated budgets and timely arrangement of funds for the projects is yet to be seen. Nevertheless, ICRA expects that VMC will derive support from the state government for funding the projects and for capacity building of the municipal staff, which is likely to mitigate the risks related to execution of large projects to an extent. While the corporation has successfully implemented several reforms in its e-governance system such as online collection of most of the revenues, some instances of inconsistency in data have been observed, which reflect a relatively weak information management system.

ICRA believes that VMC will continue to benefit from Vijayawada's strategic importance to the state government, being a part of three proposed capital regions, which would support growth in its revenue and surplus position.

## Key rating drivers and their description

### Credit strengths

**Strategic importance to state government** – Vijayawada is one of the largest cities in Andhra Pradesh and is in one of the three proposed capital regions. The city is likely to attract investment in infrastructure, which augurs well for the development of the city. It is 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** – VMC has derived more than 80% of its revenue receipts from its own tax and non-tax revenue sources between FY2014 and FY2019, indicating limited reliance on grants and assigned revenue transfers from the state government.

**Healthy financial profile** – VMC generated revenue surpluses during FY2014-FY2019, led primarily by consistent income from its own tax and non-tax revenue receipts. Although the revenue surplus was over Rs. 60 crore till FY2018, it moderated to Rs. 13 crore in FY2019 owing to lower revenue grants. Nevertheless, higher capital grants resulted in healthy overall surplus. Till FY2019, it self-funded salaries for its permanent employees, unlike other ULBs in the state, where the same is funded by the state government. However, from April 2019 onwards, the state government is responsible for paying permanent staff salaries, which would provide significant comfort to VMC's financial position. 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.

**Satisfactory current collection efficiency of key revenue contributors** – VMC has witnessed satisfactory current collection efficiency of its key revenue sources – above 90% for the property tax and above 70-50% for water supply charges during FY2014-FY2019.

### Credit challenges

**Limited growth and base of property tax with irregularity in tariff revisions** –Irregular revision in property tax, as depicted by no revision in rates after 2007, has constrained the growth in VMC's user charges income, which are linked to the property tax slabs, impacting its overall growth in revenue receipts. The compounded annual growth rate (CAGR) of property assessments stood at ~5% during FY2013-FY2019. However, the number of property assessments increased by ~8% in FY2019 and is likely to improve with recent efforts undertaken by the ULB through the geographical information system (GIS) survey and the land/building regularisation scheme floated by the state government, which resulted in higher regularisation receipts during FY2017-FY2019.

**Scope of improvement in some services** – The corporation has a significant scope of improvement in municipal solid waste (MSW) treatment (yet to be started), metered water supply connections (only 15% metered at present), sewerage coverage for households (23% of households covered till date) and road surfacing. However, metered connections and sewerage connections witnessed healthy growth in FY2019, which are expected to grow further, going forward. Nevertheless, VMC's service levels in solid waste management (100% MSW collection) with door-to-door collection and segregation, road availability in the service area (more than 20 kms. per sq. km.), water supply availability (~180 litres per capita per day) and street light coverage (~28 street lights per km) remain satisfactory.

**Sizeable capital outlays envisaged** – A large capital contribution by the VMC would be required for the execution of capital- intensive projects under the AMRUT, wherein 30-47% of the total project cost comes under the corporation. This could stretch its cash flows, especially while executing non-revenue generating projects such as housing, etc. Moreover,

given the lack of experience of the municipal staff in handling large and complex projects, its ability to timely execute these projects within the estimated budget and timely funding of the projects would be important.

### Liquidity position: Adequate

VMC's liquidity is **adequate** with annual repayments of Rs. 18 crore, as against a revenue surplus of Rs. 25-35 crore, providing adequate cover for scheduled repayments. The corporation had its own cash and bank balance (excluding funds received towards specific projects) of Rs. 130 crore as of March 2019, which is adequate to meet its share of funding for the AMRUT and housing projects. The corporation's liquidity improved in the current year as the state government has started paying salaries of the permanent staff from April 2019, reducing its establishment expenses. ICRA, however, notes that any major debt-funded capex in the near future, without the support of the government grants may lead to a tight liquidity position in the medium term.

### Rating sensitivities

**Positive triggers** – The rating could be upgraded if VMC demonstrates substantial growth in its revenues, along with an improvement in service indicators such as metered connections, solid waste treatment and sewerage.

**Negative triggers** – ICRA could downgrade the rating if a degrowth in the ULB's surplus position (especially, revenue surplus), or lower cash flows from the state government, adversely impacts its VMC's liquidity, or more-than-estimated-increase in debt levels, result in weakening of its leverage and coverage metrics.

### Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	<a href="#">Rating Methodology for Urban Local Bodies</a> <a href="#">Rating Methodology for State Governments</a>
Parent/Group Support	Not applicable
Consolidation/Standalone	The rating is based on standalone financial statements of the issuer.

### About the entity

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 the municipal services in Vijayawada city, which is part of the Andhra Pradesh Capital Region (area of 8,603 sq km surrounding the new capital of the Andhra Pradesh - Amaravathi). The Vijayawada city is located on the banks of river Krishna in Krishna district of Andhra Pradesh, and is one of the main trading and business centres in the state. The 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 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 head of various departments.

## Key financial indicators (audited)

	FY2017	FY2018	FY2019*
Revenue income (Rs. crore.)	467.82	421.9	339.6
Revenue expenditure (Rs. crore)	394.21	334.5	326.7
Revenue balance (Rs. crore)	73.62	87.4	13.0
Overall balance (Rs. crore)	26.96	-8.3	100.1
Revenue balance / Revenue income (%)	16%	21%	4%
(Principal + Interest) / Revenue income (%)	4%	4.5%	5.6%
(Revenue balance + Interest) / (Interest + Debt repayment)	3.99	4.85	1.11
Debt / Revenue income (%)	21%	42%	67%

Source: VMC and ICRA research; \*Provisional

## Status of non-cooperation with previous CRA: Not applicable

## Any other information: None

## Rating history for past three years

S. No.	Instrument	Details			Current Rating (FY2020)		Chronology of Rating History for the Past 3 Years			
		Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating		Date & Rating in			
					30- Mar 2020	15- Jan 2020	FY2019		FY2018	FY2017
							27-Jul 2018	13-Jun 2018	-	06-Feb 2017
1	Unallocated	Long Term	22.00	0.00	[ICRA]A-(Stable)	[ICRA]A-(Stable) ISSUER NOT COOPERATING	[ICRA]A-(Stable)	[ICRA]A-(Stable)	-	-
2	Term loans	Long Term	154.0	139.0	[ICRA]A-(Stable)	[ICRA]A-(Stable) ISSUER NOT COOPERATING	[ICRA]A-(Stable)		-	-
3	Issuer rating	Long Term	-	-	-	-	[ICRA] A-(Stable); Withdrawn	-	-	IrA-(Stable)

Amount in Rs. crore

## Complexity level of the rated instrument

ICRA has classified various instruments based on their complexity as "Simple", "Complex" and "Highly Complex". The classification of instruments according to their complexity levels is available on the website [www.icra.in](http://www.icra.in)

## Annexure-1: Instrument details

ISIN No	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Term loans	FY2011	-	FY2028	53.5	[ICRA]A-(Stable)
NA	Term Loans - SBI	FY2019	-	FY2033	100	[ICRA]A-(Stable)
NA	Unallocated limits	NA	NA	NA	22.00	[ICRA]A-(Stable)

Source: VMC

## Analyst Contacts

**Jayanta Roy**

+91 33 7150 1120

[jayanta@icraindia.com](mailto:jayanta@icraindia.com)

**Manish Pathak**

+91 124 4545 397

[manishp@icraindia.com](mailto:manishp@icraindia.com)

**Nithya Debbadi**

+91 44 4067 6515

[nithya.debbadi@icraindia.com](mailto:nithya.debbadi@icraindia.com)

## Relationship Contact

**Jayanta Chatterjee**

+91 80 4332 6401

[jayantac@icraindia.com](mailto:jayantac@icraindia.com)

## MEDIA AND PUBLIC RELATIONS CONTACT

**Ms. Naznin Prodhani**

Tel: +91 124 4545 860

[communications@icraindia.com](mailto:communications@icraindia.com)

## Helpline for business queries:

+91-9354738909 (open Monday to Friday, from 9:30 am to 6 pm)

[info@icraindia.com](mailto:info@icraindia.com)

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## ICRA Limited

### Corporate Office

Building No. 8, 2nd Floor, Tower A; DLF Cyber City, Phase II; Gurgaon 122 002

Tel: +91 124 4545300

Email: [info@icraindia.com](mailto:info@icraindia.com)

Website: [www.icra.in](http://www.icra.in)

### Registered Office

1105, Kailash Building, 11th Floor; 26 Kasturba Gandhi Marg; New Delhi 110001

Tel: +91 11 23357940-50

### Branches

Mumbai + (91 22) 24331046/53/62/74/86/87  
Chennai + (91 44) 2434 0043/9659/8080, 2433 0724/ 3293/3294,  
Kolkata + (91 33) 2287 8839 /2287 6617/ 2283 1411/ 2280 0008,  
Bangalore + (91 80) 2559 7401/4049  
Ahmedabad+ (91 79) 2658 4924/5049/2008  
Hyderabad + (91 40) 2373 5061/7251  
Pune + (91 20) 2556 0194/ 6606 9999

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