

August 14, 2020

North Eastern Karnataka Road Transport Corporation: Rating Reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Fund-based Term Loans	230.00	230.00	[ICRA]B+ (Stable); reaffirmed
Total	230.00	230.00	

*Instrument details are provided in Annexure-1

Rationale

The rating continues to take into consideration the importance of the North Eastern Karnataka Road Transport Corporation (NEKRTC) to the Government of Karnataka (GoK), as illustrated by the continuous financial support received over the years and during the current pandemic, with the corporation playing a critical role in providing transport services to the north eastern districts of the state. ICRA also notes that the NEKRTC enjoys the flexibility of holding the payment of the Motor Vehicles Tax (MVT) to the Government of Karnataka, with prior approval of the GoK, in the event of any cash flow mismatch, particularly on account of the repayment of the external borrowings. The rating also derives comfort from the fact that the traffic fares have been revised upwards by 12% for the NEKRTC, the first in a span of six years, w.e.f. February 26, 2020. Although ICRA believes that due to the increasing social distancing measures in the public transport system and lower passenger load on account of the Covid-19 pandemic, the favourable impact of the fare hike is likely to be limited, at least in the medium term.

The rating, however, remains constrained by the deterioration in the NEKRTCs operational profile, owing to the complete shutdown of operations due to the Covid-19 pandemic, which has resulted in a sharp decline in its revenues and operating profits during FY2020, based on the provisional estimates. ICRA notes that the uncertainty over the resumption of regular operations in the medium term, given the restrictions imposed by the state government for plying passenger buses in districts, will further impact its revenues and lead to operating losses during FY2021, which will adversely impact its liquidity too. Moreover, the lower-than-expected earnings during the current year (FY2021) is likely to increase the NEKRTC's dependence on grants from the state government to meet critical revenue expenditures like salaries to employees and payment of statutory liabilities like provident fund. ICRA notes that, although the NEKRTC's fixed costs have been funded in a timely manner during the nationwide lockdown amidst the Covid-19 pandemic, its financial profile is likely to be adversely impacted in the medium term, given the high employee costs and lower traffic revenues.

Key rating drivers and their description

Credit strengths

Strategic importance to the GoK; financial flexibility derived from being a state-owned entity – The NEKRTC is wholly-owned by the GoK and is responsible for providing transport infrastructure and services to passengers in the north-eastern districts of the state. Its operations are supervised by its Board of Directors (BoDs) appointed by the GoK, which also extends financial support, with grants funding a considerable portion of its capital expenditure programme. Further, the GoK has allowed the corporation to retain the Motor Vehicle Tax till NEKRTC reaches break even, providing a liquidity cushion. The NEKRTC also enjoys financial flexibility with the banks through regular availability of credit for capital expenditure requirements at competitive rates.

Timely and continuous revenue support by the GoK during the pandemic and debt moratorium up to August 2020, support the financial profile of NEKRTC to a large extent – During FY2021, given the liquidity concerns on account of the lack of revenues, the NEKRTC may have to defer the payment of MV Tax to the GoK. Revenue expenditure requirements like payment of salaries/pensions etc. to employees for the month of April, May and June 2020 has been met by timely revenue support received from the GoK. Moreover, the debt moratorium up to August 2020 (for a period of five months from April 2020) has also helped it manage its stretched liquidity position - a result of the restricted traffic and non-traffic revenues during the Covid-19 pandemic. This is likely to keep the debt and interest coverage indicators at a moderate level in the medium term.

Credit challenges

Complete shutdown of traffic operations owing to the pandemic severely impacted revenues and liquidity – Due to the Covid-19 pandemic, a nationwide lockdown was announced by the Government of India in March 2020, which has been continuing till now with periodic relaxations, thus impacting the traffic revenues of the NEKRTC. With almost no operations for around two-and-a-half months and high employee costs, the NEKRTC's liquidity position remains stretched. Nevertheless, support from the GoK in the form of one-time revenue support grant (~ Rs. 175-crore) to meet critical fixed expenses (salaries and pension to employees) has provided significant comfort. However, despite continuation of such a timely support from the GoK in future, the NEKRTC's liquidity position is likely to remain stretched in the near term on account of the high fixed costs and weak traffic revenues.

Deteriorating operating profile and sharp decline in operating profits during FY2020; to report operating losses during FY2021 – The NEKRTC's operating performance has been adversely impacted over the years, owing to the limited addition to its fleet strength, a decline in the number of profitable schedules operated and the rising cost of operations amidst lower-than-optimal vehicle utilisation rates. These factors, along with the lack of upward revision in tariffs (till February 2020), have constrained revenue growth, resulting in a deterioration in operating margins. The operating profits declined sharply during FY2020 due to closure of operations for the better part of March 2020, owing to Covid-19 restrictions imposed by the state government. The deterioration in the NEKRTC's operating performance is likely to continue in FY2021 owing to the limited operations with modified routes in specific zones within the state and interstate routes during the current year, which is likely to lead to operating losses in the medium term.

Increasing dependence on the GoK grants for both revenue and capital purposes – The NEKRTC's dependence on discretionary grants from the GoK to meet its revenue and capital expenditure requirements has increased over the years. Although the liquidity position, till now, has been supported by the timely transfer of grants and subsidies by the GoK, the debt-servicing coverage indicators have started showing signs of stress due to weakening operational performance.

Liquidity position: Stretched

The corporation has substantial annual debt repayments amounting to Rs. 31.24 crore (considering moratorium benefit availed amounting to Rs. 10.41 crore) during FY2021. The retained cash flow estimated during FY2021 would be negative by around Rs. 267 crore, which would be inadequate to cover for scheduled repayments. However, a special grant from the GoK to meet the NEKRTC's high establishment costs and the moratorium extended by the bankers for a period of six months up to August 2020 (only 3-month moratorium availed by the NEKRTC) would be adequate to cover any potential cash flow mismatches. Further, the cushion to defer the transfer of the Motor Vehicle Tax to the GoK (around Rs. 53.84-crore in FY2021) will provide the additional headroom. ICRA notes that any further deviation in the operational cash flows would lead to a tight liquidity position for the NEKRTC in the medium term.

Rating Sensitivities

Positive triggers – ICRA could upgrade the rating if the NEKRTC is able to achieve operating profits after traffic operations are normalised completely.

Negative triggers – ICRA could downgrade the rating if there is a delay in receiving adequate support from the GoK to meet any shortfalls and a higher-than-expected deterioration in NEKRTC’s operating performance during FY2021.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Rating Methodology for Passenger Road Transport Entities Rating Methodology for State Governments
Parent/Group Support	The assigned rating factors in the importance that the NEKRTC holds for the state government as an institution for providing public transportation services in the state, which has induced it to extend timely financial support to the rated entity.
Consolidation / Standalone	Standalone

About the company

The NEKRTC was established in August 2000 as an independent entity under the provisions of the Road Transport Corporation (RTC) Act, 1950, to provide passenger road transport services in the north-eastern districts of Karnataka. As on March 31, 2020, with a fleet strength of 4,678 buses, the NEKRTC operates close to 4,252 schedules daily through 52 depots with around 20,300 personnel on its payroll.

In FY2020, on a provisional basis, the entity reported a net loss of Rs. 106.2 crore on an operating income of Rs. 1828.3 crore compared to a net loss of Rs. 65.7 crore on an operating income of Rs. 1790.7 crore in FY2019.

Key financial indicators

	FY2018	FY2019	FY2020*
Operating Income (Rs. crore)	1635.4	1,790.7	1,828.3
OPBDITA	50.0	53.5	20.4
PAT (Rs. crore)	-31.7	-65.7	-106.2
OPBDIT/ OI (%)	3.1%	3.0%	1.1%
RoCE (%)	-33.6%	-56.9%	-147.0%
Total Debt/ TNW (times)	0.7	7.1	-1.5
Total Debt/ OPBDIT (times)	1.4	2.6	4.6
Interest coverage (times)	10.3	6.0	2.0
NWC/ OI (%)	-36.5%	-40%	-45%

Source: NEKRTC data, ICRA research; *FY2020 numbers are provisional

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years

	Instrument	Current Rating (FY2021)				Chronology of Rating History for the past 3 years				
		Type	Amount Rated	Amount Outstanding [^]	Date Rating &	Date (month/year) & Rating in				
						14-Aug-20	FY2020	FY2019	FY2018	
					26-Aug-19		06-Jul-18	05-Feb-18	15-Nov-17	27-Jul-17
1	Term Loans	Long-term	230	93.3	[ICRA]B+ (Stable)	[ICRA]B+ (Stable)	[ICRA]B+ (Stable)	-	-	-
2	Issuer Rating	Long-term	Nil	-	-	-	[ICRA]B+ (Stable) Withdrawn	[ICRA]B+ (Stable)	[ICRA]B+ (Stable) 'ISSUER NOT CO-OPERATING'	[ICRA]B+ (Stable)

[^]As on March 31, 2020

[^]As on March 31, 2020

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

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	FY2019	~8.7%	Upto FY2026	230.00	[ICRA]B+ (Stable)

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