

India International Clearing Corporation (IFSC) Limited

July 05, 2021

Ratings

Type of Rating	Rating ¹	Rating Action
Issuer Rating *	CARE AAA (Is); Stable [Triple A (Issuer Rating); Outlook: Stable]	Reaffirmed

*The rating is subject to the company maintaining overall gearing not exceeding 2.00 times

Detailed Rationale & Key Rating Drivers

The rating assigned to India International Clearing Corporation (IFSC) Ltd. (India ICC) continues to draw strength from its strong parentage, being a subsidiary of BSE Ltd. (BSE), strategic importance of India ICC to BSE, technological and managerial linkages of India ICC with BSE, its experienced Board and Management team, adequate operational risk management systems which are in line with international standards. The ratings also derive strength from well-defined default waterfall along with presence of adequate default fund and strong liquidity.

The rating takes cognisance of setting up of the new unified regulator, International Financial Services Centres Authority (IFSCA) which would provide a single window regulatory institution and accelerate development of efficient markets, enable strong regulatory supervision and boost investor confidence. Further, the rating continues to factor in various incentives & tax benefits provided to the exchange i.e. India International Exchange (IFSC) Ltd. (India INX) along with its extended period of trading operations (22 hours per day) and its strong solvency. The rating also factors in exponential increase in trading turnover at India INX in FY21 driven by growth in volumes of index derivatives.

The rating, however, continues to be tempered by its low revenue due to no clearing fees levied on members as trading volumes are still evolving at India INX due to its initial stage of operations in comparison to other established domestic and global exchanges and various inherent business & operational risks associated with India ICC.

Rating Sensitivities:

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

- Inability to replenish the actual default fund above minimum default fund requirements in case of utilization of default fund
- Any deterioration in credit profile of BSE going forward
- Any further weakening of linkages due to any significant reduction in shareholding of BSE below 51%

Detailed description of the key rating drivers

Key Rating Strengths

Strong parentage of BSE Ltd., a leading stock exchange with strong financial risk profile

India ICC is a subsidiary of BSE, Asia's oldest stock exchange, and it holds 78.88% equity in India ICC and 84.14% equity in India INX as on May 14, 2021 and remains integrated with the parent in terms of managerial, technological and other infrastructure.

Established in 1875, BSE Ltd. (formerly known as Bombay Stock Exchange Ltd.), is Asia's first and one of the fastest stock exchanges in the world. It is also the world's largest stock exchange in terms of number of companies listed and derives its income from diversified sources such as income from trading members / security services, income from services to corporates, data dissemination fees and income from investment and deposits. India INX and India ICC are expected to be a major growth driver for BSE going forward.

BSE's financial performance largely remained stable in FY21 with healthy profitability, strong liquidity and network base and nil outstanding debt.

Technological and managerial linkages of India ICC with BSE

India ICC adopts the risk management systems and latest technology which are implemented at the clearing corporation of BSE i.e. ICCL, which has a long and successful track record of operations. The systems are constantly monitored on real time basis with automated processes. Further, the entire information technology and cyber security systems are audited annually and more frequently, if required. India ICC also has a Disaster Recovery (DR) site, located at Hyderabad (alongside BSE's DR site), a city in a different seismic zone from its primary site at the IFSC, GIFT City, Gandhinagar.

Some of the key management officials of India ICC are also from BSE's clearing corporation. The Chairman of India ICC, Mr. Ashishkumar Chauhan, is the MD and CEO of BSE and was one of the founders of NSE and has also been instrumental in setting up of India INX. Mr. Arup Mukherjee (MD and CEO of India ICC) has an experience of over three decades and has previously worked with ICCL. The other board members have diverse and vast experience and are instrumental in development and functioning of India ICC. They are ably supported by a professional and experienced team, having knowledgeable personnel. Further, the Board of India ICC comprises of five directors out of which one is an independent director and to avoid conflict of interest, trading and clearing members are not allowed to be part of the Board, reflecting good corporate governance.

Hence, CARE derives comfort with India ICC being a subsidiary of BSE and BSE's management articulation for providing technological, marketing and need based financial support to India ICC, given its strategic importance to parent, BSE.

New unified regulator enables single window clearances and strong regulatory supervision

Government of India has setup a new unified regulator IFSCA for regulating all financial services entities in IFSC replacing multiple regulators earlier which would bring about more ease of doing operations by providing single window clearance and increase the pace of approvals. India ICC operations are regulated by IFSCA from October 1, 2020. India ICC has to seek regulators approval before extending its services to any segment of a recognized stock exchange and before admitting any securities for clearing and settlement. Regulator also prescribes margins to be collected from the members for positions taken by them as part of its broad guidelines for operations of the clearing corporation. IFSCA has issued the IFSCA (Market Infrastructure Institutions) Regulations, 2021, which lays down the framework under which MIIs can operate at IFSC and would help IFSC clearing corporations substantially to compete with other clearing corporations established at international jurisdictions. Further, IFSCA has also taken several steps for ease of doing business at IFSC such as permission for foreign brokers to operate at IFSC by opening a branch office at IFSC and not a separate company, allowing alternate investment funds to be setup in IFSC, relaxation in minimum networth requirements for exchanges and clearing corporation and increase in maximum single shareholding by individuals/institutions etc. As per new regulations, the minimum networth requirement is USD 3 Million against which India ICC has networth of USD 10.99 Million as on March 31, 2021.

Adequate operational risk management in adherence to global benchmarks and adequate counterparty

India ICC undertakes to act as the central counterparty to all the trades executed on the India INX. India ICC has adopted a collateral management system (CLASS) which keeps track of collateral deposited by clearing members on real-time basis and accepts only high-quality collateral, with low credit risk and high liquidity; which are legally enforceable and easily realizable. India ICC employs a robust real-time risk management system (RTRMS) which calculates the margin at client level on a real-time basis, blocks it in CLASS, generates various alerts according to utilization levels and places the terminal of member in risk reduction mode when collateral utilization exceeds 90%. India ICC's margining framework which is designed keeping in mind best practices globally, uses SPAN for computing initial margin and margin provision for Intra-day crystallized losses on parameters defined by regulator. The various margins are computed at a client level portfolio and grossed across all clients at the member level.

India ICC's risk management policy is in accordance with the Principles for Financial Market Infrastructures (PFMI) published by the Committee on Payments and Market Infrastructures (CPMI) and the Technical Committee of the International Organization of Securities Commissions (IOSCO) and is similar with risk management systems of other global exchanges who also follow PFMI and IOSCO guidelines. These principles are also broadly adopted by risk management systems of leading domestic clearing corporations like Indian Clearing Corporation Limited (ICCL; rated CARE AAA (Is); Stable), Clearing Corporation of India Limited (CCIL; rated CARE AAA (RPS); Stable) etc.

Further, India ICC has an established framework for the selection of members and clearing banks which ensures high quality selection. India ICC inducts three categories of members with a stipulated minimum tangible net-worth requirement. The clearing banks are empaneled based on criteria such as net-worth, infrastructure, etc. Currently, India ICC conducts its fund settlement through nine clearing banks.

Well defined default waterfall and adequate Default Fund

India ICC has created a dedicated Default Fund which is readily and unconditionally available to meet settlement obligations of India ICC in case of Clearing / Custodian members failing to honour the settlement obligation. IFSCA has also made it obligatory to conduct daily stress test (to check the adequacy of the default fund). The default fund shall be at least the minimum required corpus as arrived at from the monthly stress test value or USD 1 million, whichever is higher. For the month of April 2021, the value of default fund was 1.23 Million USD as against the minimum required value of 0.57 Million USD as per the stress testing mechanism.

Incentives and tax benefits provided to promote trading volumes at India INX

India INX is located in the International Financial Service Centre (IFSC) zone at Gift City - Gandhinagar, which is a SEZ and hence provides various tax benefits and incentives. The same have been provided to incentivize trading activity and attract investors from across the globe by making it cost competitive.

Extended period of trading operations at India INX resulting in access for multiple markets across the globe

India INX operates for 22 hours a day which allows FPIs to trade from multiple locations across the globe. The trading is done in 2 sessions: the first session operates from 4:30 am to 5:00 pm and second session operates from 5:00 pm to 2:30 am, wherein the settlement is done from 8:00 am to 8:15 am and 4:30 pm to 4:45 pm respectively for the said sessions on T+1 day.

Exponential growth in turnover led by volumes in index derivatives

The operations of India ICC are a function of the trading turnover of its exchange i.e. India INX. The trading turnover at India INX is still evolving due to initial years of operation; however, it has witnessed exponential increase in the trading turnover

in past two years. During FY21, India INX notional trading turnover almost doubled with increase in trading volume by almost 3x. Although the trading turnover of India INX has improved, it is still evolving in comparison to its global peers and hence results in low trade settlement volumes for India ICC.

Key Rating Weaknesses

Various inherent business and operational risks

India ICC undertakes to act as the central counterparty to all the trades executed on India INX for which it clears trades and provides full novation. India ICC remains the counterparty to trades from the time of the execution of the trade until settlement/expiry/delivery. Hence, India ICC is exposed to various business and operational risks viz. Participant Exposure and Settlement Default Risk, Credit Risk, Liquidity Risk, Legal Risk, Operational Risk, Cyber Security risk, Custody and Investment Risk, Technology Risk, etc. India ICC has various risk mitigation policies which are in accordance with IFSCA and PFMI guidelines published by the CPMI and IOSCO. However, the effectiveness of the same needs to be tested over a period of time.

Liquidity: Strong

India ICC's liquidity remained comfortable marked by no repayment obligations and presence of free cash and bank balance of Rs.76.98 crore (including default fund of Rs.8.70 crore) as on March 31, 2021. The overall gearing of India ICC was NIL as on March 31, 2021. India ICC has also created a dedicated Default Fund which is readily and unconditionally available to meet settlement obligations of India ICC in case of Clearing / Custodian members failing to honour the settlement obligation; the adequacy of the same is stress tested on a daily basis. For the month of April 2021, the value of default fund is USD 1.23 million as against the minimum regulatory requirement of USD 1 million or value as determined by monthly stress test, whichever is higher, as per new regulations introduced by IFSCA. Furthermore, India ICC has available sanctioned bank facility of USD 3 million in the form of overdraft against fixed deposit; however, it is rarely utilized.

Analytical approach: Standalone along with factoring strong linkages which India ICC has with its parent viz. BSE. Statutorily, exchanges are not allowed to carry out the function of 'trade clearing & settlement' within the same entity and hence it required formation of a separate legal entity which led to incorporation of India ICC, with BSE holding 78.88% equity in it. India ICC derives significant support in terms of technology, system & process development and capital infusion from BSE. Reputation of BSE will be at stake if the clearing and settlement operations at India ICC get disrupted as it is a matter of trust and accordingly, it shall ensure that India ICC remains as one of the critical subsidiaries of BSE.

Applicable Criteria

[Criteria on assigning 'outlook' and 'credit watch' to Credit Ratings](#)

[CARE's Policy on Default Recognition](#)

[Rating Methodology: Notching by factoring linkages in Ratings](#)

[CARE's Issuer Rating](#)

[Financial ratios - Financial Sector](#)

About the Company

India ICC is the first clearing corporation to be established at the International Financial Services Centre (IFSC), GIFT City-Gandhinagar, Gujarat. India ICC commenced operations from January 16, 2017 and clears and settles a wide range of global benchmark products across all major asset classes including equity derivatives, commodity derivatives, currency derivatives, debt securities. India ICC maintains world class standards in its operations and competes with other international clearing corporations. India ICC provides clearing & settlement, risk management and collateral management services to the India INX which is also a wholly owned subsidiary of the BSE Ltd. and is also operating at IFSC, Gift City, Gandhinagar.

India ICC has gradually diversified its investor base with induction of ICICI Bank, DCB Bank and other individual shareholders and BSE now holds 78.88% as on May 2021.

(Rs. Crore)

Brief Financials of India ICC (Standalone)	FY20 (A)	FY21 (A)
Total income	2.28	1.80
PAT	-1.74	-3.00
Total Assets*	100.64	105.92
ROTA (%)	NM	NM
Interest coverage (times)	NM	NM

A: Audited; NM: Not meaningful; * Total Assets are net of intangible assets

(Rs. Crore)

Brief Financials of Parent, BSE (Consolidated)	FY20 (A)	FY21 (*)
Total income	630.00	654.65
PAT	120.61	141.70
Total Assets*	4,281	4,412
ROTA (%)	2.80	3.26
Interest coverage (times)	VL	VL

A: Audited; *as per published results; VL – Very Large

ROTA is calculated as ratio of PAT to average of annual opening and closing balance of Total Assets, calculated as Net of Deferred Tax Assets, Intangible Assets and Goodwill.

Status of non-cooperation with previous CRA: Not Applicable

Any other information: Not Applicable

Rating History (Last three years): Please refer Annexure-2

Covenants of rated instrument: Not Applicable

Complexity level of various instruments rated for this company: Not Applicable

Annexure-1: Details of Instruments/Facilities

Name of the Instrument	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. Cr.)	Rating assigned along with Rating Outlook
Issuer Rating	NA	NA	NA	NA	CARE AAA (Is); Stable

NA: Not Applicable

Annexure-2: Rating History of last three years

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating history			
		Type	Amount Outstanding (Rs. crore)	Rating	Date(s) & Rating(s) assigned in 2021-2022	Date(s) & Rating(s) assigned in 2020-2021	Date(s) & Rating(s) assigned in 2019-2020	Date(s) & Rating(s) assigned in 2018-2019
1.	Issuer Rating-Issuer Ratings	Issuer rating	0.00	CARE AAA (Is); Stable	-	1)CARE AAA (Is); Stable (06-Jul-20)	1)CARE AAA (Is); Stable (01-Oct-19)	1)CARE AAA (Is); Stable (20-Dec-18) 2)CARE AAA (Is); Stable (05-Apr-18)

Annexure-3: Complexity level of various instruments rated for this company

Sr. No.	Name of the Instrument	Complexity Level
1.	Issuer Rating-Issuer Ratings	Simple

Note on complexity levels of the rated instrument: CARE has classified instruments rated by it on the basis of complexity. Investors/market intermediaries/regulators or others are welcome to write to care@careratings.com for any clarifications.

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