

India International Clearing Corporation (IFSC) Ltd.

October 01, 2019

Rating

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 [India ICC being a subsidiary of BSE Ltd. (BSE)], strategic importance of India ICC from the perspective of BSE, its experienced board of directors & management team, good corporate governance framework, its robust collateral & risk management systems & margining framework, sound system & technology infrastructure, established framework for selection of members & clearing banks and presence of adequate default fund. The rating of India ICC further factors in strong regulatory supervision of SEBI on its operations, 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 nil overall gearing.

The rating, however, continues to be tempered by its low revenue on the back of still evolving trading volumes at India INX due to its initial stage of operations and various inherent business & operational risks associated with India ICC.

Continued parentage along-with need-based technical, system and financial support (including meeting its regulatory net worth levels) from BSE, effective implementation and monitoring of the various risk management systems along-with growth in the trading volumes of India INX are the key rating sensitivities.

Detailed description of the key rating drivers

Key Rating Strengths:

Strong parentage of BSE Ltd. along with being strategically important for BSE: BSE, Asia's oldest stock exchange, holds 90.10% equity in India ICC and 92.29% equity in India INX. India INX and India ICC are expected to be a major growth driver for BSE going forward. As per SEBI regulations, India ICC is required to attain a minimum net-worth of Rs.100 crore within a period of 3 years from the date of commencement of operations, irrespective of settlement volumes of India ICC, towards which BSE has committed to invest further capital, if required, reflecting the importance of India ICC to BSE. Further, on request of the company, SEBI has granted a relaxation for a further period of one year and the company is now required to attain the Rs.100 crores net-worth by January 16, 2021. Also, some of the key management officials of India ICC are from BSE's clearing corporation. The MD and CEO of BSE is the Chairman of India ICC. India ICC derives support from BSE and its clearing corporation in terms of technology, risk management system and process development. Being a subsidiary of BSE, which has a net worth of ~Rs.2,593 crore (on a standalone basis) as on March 31, 2019, India ICC derives comfort from the available need based financial support of its parent, given its strategic importance.

Parent a leading stock exchange with strong financial risk profile: 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 which stood at 5,262 as on March 31, 2019. Also, as on FY19 end, BSE is ranked no. 2 in currency options traded, no. 2 in currency futures traded and no. 8 by market capitalization among the global stock exchanges. Over the past 143 years, BSE has facilitated the growth of the Indian corporate sector by providing it an efficient capital-raising platform. In 2017 BSE became the 1st listed stock exchange in India.

The management team of BSE is led by Mr. Ashishkumar Chauhan who is the MD & CEO. He is well supported by other experienced team members looking after regulations, finance, information, business, trading and secretarial aspects.

BSE derives its income from diversified sources such as income from trading members / security services (Rs.171 crore for FY19), income from services to corporates (Rs.214 crore), data dissemination fees (Rs.30 crore) and income from investment and deposit (Rs.202 crore). Total operating income of BSE remained largely stable in FY19. Further, PBILDT for FY19 stood at Rs.276 crore translating into PBILDT margin of around 45% which was also stable as compared to FY18. BSE has strong capital structure as indicated by negligible debt level as on March 31, 2019. BSE had free cash balance of around Rs.1,493 crore as on March 31, 2019 owing to its strong cash accruals. Equity in BSE is held by public to the extent of 67.80% and remaining 32.20% by trading members and their associates.

Experienced board of directors and management: The board of directors of India INX / India ICC consists of highly qualified personnel who have vast experience of working in exchanges and clearing corporation. The Chairman of India ICC, Mr. Ashishkumar Chauhan is the current MD and CEO of BSE Ltd. He was one of the founders of NSE and has also been instrumental in setting up of India INX. The other board members have diverse and vast experience and are instrumental in development and functioning of India ICC. Mr. Arup Mukherjee (MD and CEO of India ICC) has an experience of over three

decades and has previously worked with the clearing corporation of BSE i.e. Indian Clearing Corporation Limited (ICCL). The top management of India ICC also has experience of working with ICCL. They are supported by a professional and experienced team, having knowledgeable personnel with respect to various aspects of the business (such as clearing, settlement and risk management).

Good corporate governance framework: India ICC follows best practices with regard to corporate governance, which is reflected through its Board structure, management team, various policies, rules, regulations and bye-laws. The board of India ICC comprises of five directors out of which two are independent directors. To avoid conflict of interest, trading and clearing members are not allowed to be part of the Board.

Strong regulatory supervision by SEBI

India ICC's operations are closely regulated by SEBI. India ICC needs to seek approval of SEBI before extending its services to any segment of a recognized stock exchange and before admitting any securities for clearing and settlement. SEBI also prescribes margins to be collected from the members for the positions taken by them. SEBI directs India ICC towards mandatory maintenance of a default fund to ensure settlement of transactions in case of failure on the part of the clearing members to fulfil their obligations. It also requires that the adequacy of the fund should be tested by regular stress tests.

Robust collateral management, risk management systems and margining framework

India ICC undertakes to act as the central counterparty to all the trades executed on the India INX. India ICC uses various real time systems for collateral management, risk management and margining frameworks. India ICC has a sound framework for the comprehensive management of all material risks and established documented policies, procedures, systems and controls to identify, measure, monitor and manage risks. 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).

For collateral management, India ICC has adopted CLASS system which keeps a track of the collateral deposited by the clearing members with India ICC on a real-time basis. The system is also enabled to give instructions to clearing banks and members with respect to settlement functions. India ICC 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 and blocks it in the collateral system (CLASS). The RTRMS also generates various alerts at different collateral utilization levels (70%, 80% and 90%) and places the trading terminal of the member in risk reduction mode when the collateral utilization exceeds 90%.

India ICC carries out on-line margining through RTRMS using SPAN, which is used for the purpose of computation of initial margins and margin provisions for Intra-day crystallised losses, based on the parameters defined by SEBI. The margining framework is designed keeping in mind best practices prevalent globally. SPAN computes various margins on a real time basis for various scenarios of price changes wherein the scenario contract values are updated at the start of the business day, then every 1.5 hours and finally at the end of the business day. The various margins are computed at a client level portfolio and grossed across all clients at the member level. All the above said risk management systems are subject to various SEBI inspections.

Sound systems and technology infrastructure

India ICC has established a secure and reliable information technology system from basic infrastructure to the application level. The systems are constantly monitored on real time basis with automated processes. Being a subsidiary of BSE, it benefits India ICC as it adopts the latest systems and technology being implemented at the clearing corporation of BSE i.e. ICCL, which has a long and successful track record of operations. Further, India INX has an advanced trading platform with a response time of 4 micro seconds.

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.

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. SEBI 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 10% of the net-worth of the India ICC. For the month of September 2019, the value of default fund is USD 1,135,970 as against the minimum required value of USD 570,740 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 FPI's 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.

Well established framework for selection of members and clearing banks

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

Liquidity analysis: Strong

India ICC's liquidity remained comfortable as marked by strong cash accruals against no repayment obligations and presence of free cash and bank balance of Rs.78.84 crore (including default fund of Rs.7.44 crore) as on March 31, 2019. The overall gearing of India ICC was NIL as on March 31, 2019. 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 September 2019, the value of default fund is USD 1,135,970 as against the minimum required value of USD 570,740 as per the stress testing mechanism. Furthermore, India ICC has available sanctioned bank facility of USD 1 million in the form of overdraft against fixed deposit; however the same has never been utilized.

Key Rating Weaknesses

Trading volumes at India INX is still evolving: 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 gradual increase in the trading turnover in last few months. The monthly average trading turnover for 10 months ended Oct-18 was USD 11.46 billion which has increased to USD 32.83 billion for 10 months ended Aug-19. Although the trading turnover of India INX has improved, it is still evolving in comparison to its global peers and hence there is low clearing volumes at India ICC. It is envisaged that various tax benefits and incentives offered at India INX would further lead to increase in the trading turnover and in-turn lead to improved financial performance of India ICC.

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 SEBI guidelines and PFMI guidelines published by the CPMI and IOSCO. However, the effectiveness of the same needs to be tested over a period of time.

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, accordingly India ICC works as an extended arm of BSE with BSE holding 90.10% 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 to Credit Ratings](#)

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

[Financial ratios - Non- Financial Sector](#)

[Rating Methodology: Factoring Linkages in Rating](#)

[CARE's Issuer Rating](#)

About the Company

India ICC was incorporated in September 2016 as a clearing corporation providing clearing & settlement and risk management services to India INX. Initially, the said clearing corporation was named BSE International Clearing Corporation (IFSC) Ltd. and subsequently in November 2016 its name was changed to India International Clearing Corporation (IFSC) Ltd. India ICC was earlier a wholly owned subsidiary of the BSE Ltd. During Aug-19, ICICI Bank Ltd acquired 9.90% stake in India ICC thereby revising BSE's shareholding in India ICC to 90.10%. 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 intends to develop itself into a world class clearing corporation to clear and settle a wide range of global benchmark products across all major asset classes including securities, equity derivatives, precious metals, base metals, energy, interest rates, currencies etc. (subject to necessary approvals and operating guidelines from regulators). 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.

Brief Financials (Rs. crore)	FY18 (A)	FY19 (A)
Total Income	0.74	2.04
PBILDT	-2.30	-1.55
PAT	-2.98	-2.49
Overall gearing (times)	0.00	0.00
Interest coverage (times)	NM	NM

A: Audited; NM – Not Meaningful

Status of non-cooperation with previous CRA: Not Applicable

Any other information: Not Applicable

Rating History for last three years: Please refer Annexure-2

Annexure-1: Details of 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 2019-2020	Date(s) & Rating(s) assigned in 2018-2019	Date(s) & Rating(s) assigned in 2017-2018	Date(s) & Rating(s) assigned in 2016-2017
1.	Issuer Rating-Issuer Ratings	Issuer rating	0.00	CARE AAA (Is); Stable	-	1)CARE AAA (Is); Stable (20-Dec-18) 2)CARE AAA (Is); Stable (05-Apr-18)	-	-

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

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