January 16, 2023

KCC Dhangaon Boregaon Expressway Private Limited: Rating reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term Fund-based – Term loan	270.0	270.0	[ICRA]A-(Stable); reaffirmed
Total	**270.0**	**270.0**	

**Instrument details are provided in Annexure-I*

Rationale

The rating reaffirmation for KCC Dhangaon Boregaon Expressway Private Limited (KDBEPL) continues to reflect the healthy financial profile and track record of its sponsor and engineering, procurement and construction (EPC) contractor for the project – KCC Buildcon Private Limited (KCC, rated [ICRA]A (Positive) / [ICRA] A2+). The rating favourably factors in the inherent benefits of the hybrid-annuity based nature of the project including upfront availability of right of way[1] (RoW), automatic de-scoping of RoW pending beyond 180 days from the appointed date, inflation-linked[2] revisions to the bid project cost during the construction period, and relatively lower equity mobilisation risk with 40% of the bid project cost to be funded by the authority during the construction period in the form of a grant. The rating positively considers the credit support provided by the structural features of the debt, including the presence of escrow, cash flow waterfall mechanism, provision for debt servicing reserve (DSR), provision for creation of major maintenance reserve (MMR), presence of reserves to meet the regular operations and maintenance (O&M) and interest obligations till the next scheduled annuity. Additionally, the cash sweep mechanism and restricted payment clause with a minimum debt servicing coverage ratio (DSCR) of 1.2 times provides comfort. The rating notes the stable revenue stream post commissioning, with 60% of the inflation-adjusted bid project cost being paid out as annuity, along with interest at bank rate plus 300 bps and the inflation-adjusted O&M cost bid over the 15-year operations period by the project owner, National Highways Authority of India [NHAI, rated [ICRA]AAA(Stable)], which is a strong counterparty.

The rating is, however, constrained by the execution risks involved in the under-construction projects including time and cost overruns. However, the risk is mitigated, to an extent, by the fixed-price, fixed-time EPC contract with KCC, which has demonstrated strong project execution capabilities, and availability of majority of RoW (~96.5% was available as of November 2022). The project has received appointed date on August 4, 2021 and is in the intermediate stage of construction, having achieved ~49% financial progress as on November 30, 2022. The company's ability to commission the project in a timely manner and within the budgeted costs would remain important from the credit perspective. KDBEPL is exposed to equity mobilisation risk as ~43% equity is yet to be infused as on December 31, 2022. Nevertheless, KCC's healthy financial risk profile provides comfort. Post commissioning, the company will have to undertake O&M of the project stretch as per the concession agreement to avoid any deductions from annuities. Any significant deductions from annuities or increase in routine and major maintenance (MM) from the budgeted level could impact its DSCR. The rating also factors in the exposure of KDBEPL's cash flows to the spread between the interest earned on the outstanding annuities, which is linked to the Reserve Bank of India's (RBI) Bank Rate, and the interest rate on the project loans, which is linked to lender's MCLR. Further, KDBEPL's cash flows are exposed to inflation risk as O&M receipts, though linked to inflation index (70% WPI and 30% CPI), may not be adequate to compensate for the actual increase in O&M/periodic maintenance expenses.

The Stable outlook on the rating reflects ICRA's opinion that KDBEPL will benefit from the strong execution capabilities and financial profile of the sponsor and EPC contractor—KCC.

Key rating drivers and their description

Credit strengths

Established track record and financial profile of the sponsor and EPC contractor – KDBEPL is a subsidiary of KCC, which has long experience spanning over two decades in the road construction segment and has been executing road projects since 1999. KCC is appointed as the EPC contractor for executing the project, which provides comfort, given its track record of project execution within the budgeted time and cost. The total estimated project cost of Rs. 682.0 crore is planned to be funded by the NHAI's grant of Rs. 332.4 crore, external debt of Rs. 270.0 crore and the promoter's contribution of Rs. 79.6 crore. KDBEPL is exposed to equity mobilisation risk as ~43% of promoter contribution is yet to be infused as on December 31, 2022, which is expected to be infused as the project progresses. While KCC's financial profile is adequate to meet its equity commitment in the project, which is required to be infused over the construction period, it also has sizeable equity commitments towards other under-implementation hybrid annuity model (HAM) projects.

Lower inherent risks in HAM projects from the NHAI – The inherent benefits of hybrid-annuity based nature of the project include upfront availability of RoW, automatic de-scoping of RoW pending beyond 180 days from the appointed date, inflation-linked revisions to the bid project cost during the construction period. Moreover, it faces relatively lower equity mobilisation risk with 40% of the bid project cost to be funded by the authority during the construction period in the form of a grant. Stable revenue stream post commissioning, with 60% of the inflation-adjusted bid project cost being paid out as annuity, along with interest at bank rate plus 300 bps and the inflation-adjusted O&M cost bid over the 15-year operations period by the NHAI, which is a strong counterparty, provides comfort.

Healthy coverage indicators and presence of structural features – Once operational, KDBEPL is expected to have healthy debt coverage indicators. This provides the special purpose vehicle (SPV) adequate cushion to withstand any adverse movement in the bank rate and inflation to a major extent. The credit profile is supported by undertaking towards cost overrun during the construction phase, any shortfall in O&M expenses and corporate guarantee to meet any shortfall in debt servicing until the receipt of the first two annuities. Further, the presence of structural features of the debt, including the presence of escrow, cash flow waterfall mechanism, provision for DSR (worth three months' interest to be created upfront and the remaining to be created out of the first two annuities), provision for creation of MMR, presence of reserves to meet the regular O&M and interest obligations till the next scheduled annuity, cash sweep and restricted payment clause with a minimum DSCR of 1.2 times provides comfort.

Credit challenges

Execution risk related to under-construction project – The project has received appointed date on August 4, 2021 and is in the intermediate stages of construction with ~49% completion achieved as on November 30, 2022. Thus, the company is exposed to project execution risks including risks of delays and cost overruns. However, the risk is mitigated, to an extent, by the availability of majority of RoW (96.5% available till November 2022), and the fixed-price, fixed-time contract and strong project execution capabilities of KCC. The company's ability to commission the project in a timely manner and within the budgeted costs would remain important from the credit perspective.

Project cash flows and returns exposed to interest rate and inflation risks – The project's cash flows and returns are exposed to interest rate risk and are dependent on the spread between the RBI's Bank Rate and the interest rate charged by lenders. The interest on the outstanding annuities from the NHAI is linked to the RBI's Bank Rate, while the interest rate charged by lenders is linked to their respective MCLR. Further, KDBEPL's cash flows are exposed to inflation risk as O&M receipts, though linked to inflation (70% WPI and 30% CPI), may not be adequate to compensate for the increase in O&M/periodic maintenance expenses.

Undertaking O&M as per concession requirement and risk of deductions from annuity – Post commissioning, the company will have to undertake O&M of the project stretch as per the concession agreement to avoid any deductions from annuities. Any significant deductions from annuities or increase in routine and MM expenses from the budgeted level could impact its DSCR.

Liquidity position: Adequate

The total estimated project cost of Rs. 682.0 crore is planned to be funded by the NHAI's grant of Rs. 332.4 crore, external debt of Rs. 270.0 crore and equity of Rs. 79.6 crore.

Rating sensitivities

Positive factors – The rating could be upgraded if the project is completed within the expected timelines and budgeted costs.

Negative factors – Negative pressure on the rating could arise if the project progress is delayed, leading to significant time and cost overruns, or if there is a deterioration in the credit profile of the sponsor, or if delays in receipt of grant or equity infusion results in increased funding risks for the project.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Corporate Credit Rating Methodology Rating Methodology for ROADS–HYBRID ANNUITY
Parent/Group support	Not Applicable
Consolidation/Standalone	Standalone

About the company

KDBEPL is an SPV formed in December 2020 by KCC for undertaking a road project awarded by the NHAI. The project involves four-laning of Dhangaon–Boregaon section of NH-347BG and 753L (Indore to Boregaon- Pkg IV) Design Ch. 81.000 to 139.000 (Length 58.000 Km) in Madhya Pradesh on HAM basis. The concession agreement was signed on January 11, 2021 and the appointed date was received on August 4, 2021. The construction period for the project is two years from the appointed date, and the operations period is 15 years from the commercial operations date (COD). The total estimated project cost of Rs. 682.0 crore is planned to be funded by the NHAI's grant of Rs. 332.4 crore, external debt of Rs. 270.0 crore and promoter contribution (equity) of Rs. 79.6 crore.

Key financial indicators

Key financial indicators are not applicable as KDBEPL is a project-stage company.

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current rating (FY2023)				Chronology of rating history for the past 3 years		
		Type	Amount rated (Rs. crore)	Amount outstanding as on Dec 31, 2022 (Rs. crore)	Date & rating in FY2023	Date & rating in FY2022	Date & rating in FY2021	Date & rating in FY2020
					Jan 16, 2023	Dec 07, 2021		
1	**Term loans**	Long term	270.0	93.55	**[ICRA]A-(Stable)**	**[ICRA]A-(Stable)**	-	-

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long-term Fund-based – Term loan	Simple

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	**Term loan-I**	March 2021	NA	FY2037*	140.0	[ICRA]A-(Stable)
NA	**Term loan-II**	May 2021	NA	FY2037*	130.0	[ICRA]A-(Stable)

*Source: Company; *linked with CoD of the project*

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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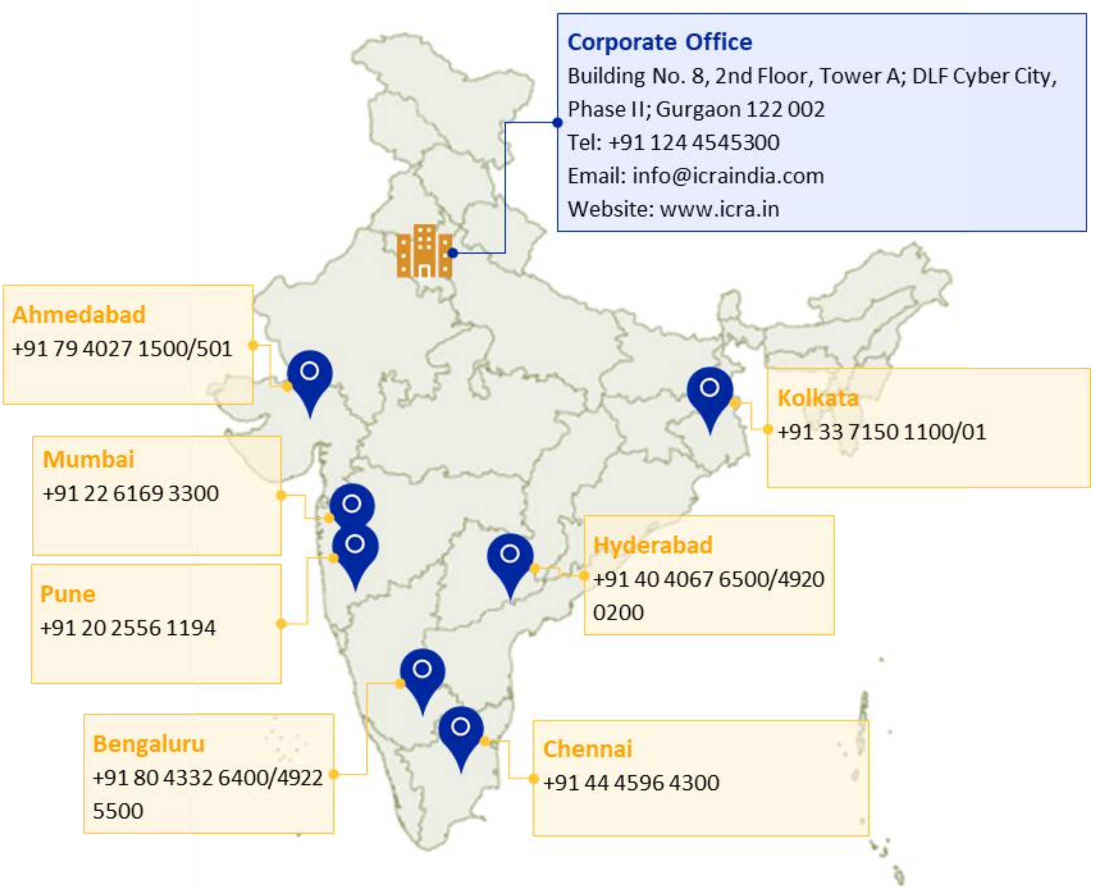

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