February 25, 2022

NKC KK Expressway Private Limited: [ICRA]BBB+ (Stable) assigned

Summary of rating action

Instrument*	Current Rated Amount (Rs. crore)	Rating Action
Term Loan	200.00	[ICRA]BBB+ (Stable); assigned
Total	**200.00**	

**Instrument details are provided in Annexure-1*

Rationale

The rating assigned to NKC KK Expressway Private Limited (NKKEPL) takes into account the financial profile and track record of its sponsor– NKC Projects Private Limited (NPPL, rated [ICRA]A- (Stable)/[ICRA]A2+), which is also the engineering, procurement and construction (EPC) contractor for the project being developed by NKKEPL. NPPL has provided sponsor undertakings towards cost overrun during the construction phase, and to meet any shortfall in operations and maintenance (O&M) expenses. The rating favourably factors in the inherent benefits of the hybrid-annuity based nature of the project including upfront availability of right of way (RoW)[1], de-scoping of RoW pending beyond 180 days from the appointed date, inflation-linked[2] revisions to bid for 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 through 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 service reserve (DSR, to be created out of the first two annuities), provision for creation of reserve for major maintenance (MMR), and restricted payment clause with a minimum debt service coverage ratio (DSCR) of 1.15 times. 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 the average of one-year MCLR[3] of the top five scheduled commercial banks (SCBs, to be reset every quarter) plus spread of 1.25%, 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 contract and NPPL's strong project execution capabilities. The company's ability to commission the project in a timely manner and within the budgeted costs would remain important from the credit perspective. NKKEPL is exposed to equity mobilisation risk as equity is yet to be infused. However, NPPL'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 the company's DSCR. NKKEPL'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.

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[1] *At least 80% prior to the appointed date.*

[2] *Based on annual change in price index multiple (PMI) from the base year – PMI is the weighted average of Wholesale Price Index (WPI) and Consumer Price Index (CPI) (IW) in the ratio of 70:30.*

[3] *The authority shall declare the list of top five SCBs on 1st of September every calendar year based on the balance sheet size as declared in their annual reports. The one-year MCLR of the top five SCBs shall be taken at the start of every quarter.*

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

Key rating drivers and their description

Credit strengths

Established track record and financial profile of the sponsor and EPC contractor – NKKEPL is a subsidiary of NPPL, which has vast experience in executing road construction projects. NPPL is 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. 494.22 crore is planned to be funded by NHAI's grant of Rs. 230.0 crore, external debt of Rs. 200.0 crore and promoter contribution/equity of Rs. 64.2 crore. NKKEPL is exposed to equity mobilisation risk as ~50% equity is yet to be infused as of January 2022. While NPPL'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 NHAI – The inherent benefits of hybrid-annuity based nature of the project include upfront availability of RoW, de-scoping of RoW pending beyond 180 days from the appointed date, inflation-linked revisions to bid for 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 through 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 the average of one-year MCLRs of the top five SCBs (to be reset every quarter) plus spread of 1.25%, and the inflation-adjusted O&M cost bid over the 15-year operations period by the NHAI, which is a strong counterparty, provide comfort.

Healthy coverage indicators and presence of structural features – The project is expected to achieve the commercial operations date (COD) within two years from the appointed date. If the overall project cost remains within the budgeted level, once operational, NKKEPL is likely to have healthy debt coverage indicators with a cumulative DSCR of more than 1.3 times. This provides the special purpose vehicle (SPV) adequate cushion to withstand any adverse movement in the interest on annuity and inflation to a major extent. The credit profile is supported by NPPL's undertaking towards cost overrun during the construction phase and any shortfall in O&M expenses. Furthermore, the presence of structural features of the debt, including the presence of escrow, cash flow waterfall mechanism, provision for DSR (to be created out of the first two annuities), provision for creation of MMR and restricted payment clause with a minimum DSCR of 1.15 times provides comfort.

Credit challenges

Execution risk related to project under construction – The project has not yet received the appointed date. 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 fixed-price, fixed-time contract and NPPL's strong project execution capabilities. Its 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 inflation risks – The project's cash flows and returns 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 and MM as per concession requirement – 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

As the project is under construction, the company does not maintain any significant liquidity. However, the liquidity position is supported by an undrawn term loan, grants receivable from NHAI and equity infusion from NPPL. The total estimated project cost of Rs. 494.2 crore is planned to be funded by NHAI's grant of Rs. 230.0 crore, external debt of Rs. 200.0 crore and equity of Rs. 64.22 crore.

Rating sensitivities

Positive factors – The rating could be upgraded if the project achieves PCOD/COD within the expected timelines and budgeted costs or if there is an improvement in the credit profile of the sponsor.

Negative factors – Negative pressure on 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 delayed 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 Roads - Hybrid Annuity Rating Approach - Implicit parent or group support
Parent/Group Support	Parent/Group Company: NKC Projects Private Limited (NPPL) The rating assigned to NKKEPL factors in the likelihood of its parent, NPPL, extending financial support to it because of undertaking provided by NPPL and close operational linkages.
Consolidation/Standalone	Standalone

About the company

NKKEPL is an SPV formed in April 2021 by NPPL for undertaking a road project awarded by the NHAI. The project involves developing the six-lane Karki Kaliagura section of NH130-CD Road from km 226.500 to km 249.000 under Raipur Visakhapatnam Economic Corridor in Odisha under HAM. The construction and operations period for the project is two years and 15 years, respectively. The concession agreement was signed on July 14, 2021 and the appointed date is yet to be received. The total estimated project cost of Rs. 494.2 crore is planned to be funded by NHAI's grant of Rs. 230.0 crore, external debt of Rs. 200.0 crore and equity of Rs. 64.22 crore.

Key financial indicators

The key financial indicators are not applicable as NKKEPL 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 (FY2022)				Chronology of Rating History for the past 3 years		
		Type	Amount Rated (Rs. crore)	Amount Outstanding as of Jan 31, 2022 (Rs. crore)	Date & Rating	Date & Rating in FY2021	Date & Rating in FY2020	Date & Rating in FY2019
					Feb 25, 2022	-	-	-
1	Term Loan	Long-term	200.00	0.00	[ICRA]BBB+(Stable)	-	-	-

Complexity level of the rated instruments

Instrument	Complexity Indicator
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, is available on ICRA's 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 Loan	Oct 2021	-	*	200.00	[ICRA]BBB+(Stable)

Source: *Company, ICRA*

**linked with CoD of the project*

Please click here to view details of lender-wise facilities rated by ICRA

Annexure-2: List of entities considered for consolidated analysis

Not Applicable

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About ICRA Limited:

ICRA Limited was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment Information and Credit Rating Agency.

Today, ICRA and its subsidiaries together form the ICRA Group of Companies (Group ICRA). ICRA is a Public Limited Company, with its shares listed on the Bombay Stock Exchange and the National Stock Exchange. The international Credit Rating Agency Moody's Investors Service is ICRA's largest shareholder.

For more information, visit www.icra.in

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