Patel KNR Infrastructures Limited

February 14, 2017

Ratings

Facilities	Amount (Rs. crore)	Rating[1]	Rating Action
Non Convertible Debentures (NCD)	295.81 (334.14) (Rs. Two hundred ninety five crore and eighty one lakh only)	**CARE AAA (SO); (Triple A (Structured Obligation); (credit watch with developing implications)**	Placed on Credit Watch with Developing Implications
Total Facilities	**295.81** **(Rs. Two hundred ninety five crore and eighty one lakh only)**		

Details of instruments in Annexure-1

Detailed Rationale

The rating assigned to the NCDs of Patel KNR Infrastructures Limited (PKIL) has been put under credit watch with developing implications on account of the proposed sale of the entire equity stake in PKIL by Patel Engineering Limited (PEL) and KNR Constructions Limited (KNRCL) to Express Way Developer Limited, step-down subsidiary of Essel Infraprojects Limited (rated CARE BBB+; Stable/ A3+ in January 2017). This may impact the credit enhancement measures (CEMs) and structured payment mechanism (SPM), in view of the increase in major maintenance expenses incurred in FY16 and slight delay in completion of major maintenance, resulting in deduction of annuity towards damages by NHAI. CARE is not in a position to evaluate the exact impact of these developments on the credit profile of PKIL as various agreements and undertakings providing comfort to the rating including promoter support undertaking and undertakings related to Operations & Maintenance (O&M) expenses would now be required to be executed by the new sponsor. CARE will closely monitor the impact of the same on the CEMs and SPM and resolve the credit watch thereafter.

The rating continues to take into account the current structured payment mechanism for servicing the NCDs, in the form of escrow of semi-annual annuity receivables from National Highways Authority of India (NHAI - rated 'CARE AAA' for its bonds), fixed price Operation and Maintenance (O&M) contract, creation of Major Maintenance Reserve Account (MMRA) and Debt Service Reserve Account (DSRA). The rating also derives comfort from the timely receipt of annuity payments, good condition of the road reflected by a lower roughness index vis-à-vis the requirement, completion of the first major maintenance cycle and comfortable liquidity position maintained by the company.

Furthermore, any deterioration in the credit profile of the promoters, timely completion of major maintenance work in future, thereby ensuring timely receipt of full annuity due, deterioration in the credit profile of the annuity provider – NHAI and occurrence of any force majeure event are the key rating sensitivities.

Detailed description of the key rating drivers

The revenue source for PKIL is the bi-annual annuity of Rs.32.94 crore receivable from NHAI till March, 2027. A 'T+20' structure has been provided for NCD repayment with 'T' being the NHAI annuity receipt date to take care of any operational delay in receipt of annuity from NHAI. PKIL has an established track record of receipt of 14 annuities from NHAI.

PKIL has opened and maintained an 'Escrow account' with the bank with the first priority assigned towards O&M expenses followed by debt servicing of the NCDs and appropriation to Major Maintenance Reserve Account (MMRA) and other relevant expenses, in that order. PKIL has created a fund-based DSRA of Rs.15 crore to address any cash-flow mismatch for payment to O&M contractor and/or debt servicing, invested in approved securities yielding at least 6% annually. The post-tax returns on the DSRA of Rs.15 crore shall always be retained in the escrow account till the maturity of the NCDs.

In order to mitigate Operation & Management (O&M) risk and avoid any fluctuation in O&M and major maintenance expenses (MME), PKIL has entered into a fixed-price O&M contract with KNRCL. Besides, non-performance of O&M

[1] *Complete definition of the ratings assigned are available at www.careratings.com and other CARE publications*

contractor in carrying out routine and Major Maintenance Activity (MMA) may translate into reduction in annuity receivables. Such shortfall in annuity will have a direct bearing on the envisaged debt servicing capability of PKIL.

The road has been in a good condition and the roughness index at present is well within the the stipulated limit of less than 2000 mm/km. The company initiated the process of major maintenance work in March 2015 and the work was to be completed by February 2016. However the work was completed in February 2016 and the expenses increased substantially compared to envisaged expenses, predominantly due to an unexpected increase in the overlay thickness to 40 mm from earlier envisaged 25 mm. The company had to pay damages to NHAI for the delay in completion of major maintenance. The company funded the higher major maintenance through MMRA reserves and cash reserves.

As on March 31, 2016 PKIL had a cash and bank balance of Rs.60.16 crore, which comprised of DSRA of Rs.15 crore, MMRA of Rs.6.44 crore, fixed deposits of Rs.8.38 crore and free cash and bank balance of Rs.35.29 crore signifying a comfortable liquidity position after the completion of the periodic major maintenance.

Analytical approach:

CARE has analyzed PKIL's credit profile by considering the structured payment mechanism [biannual annuity is received from the National Highways Authority of India (NHAI) (rated 'CARE AAA' for bonds) in an escrow account for servicing of the NCD] and adequate built-in liquidity cushions with favourable credit protection mechanisms..

Applicable Criteria

Criteria on assigning Outlook to Credit Ratings
CARE's Policy on Default Recognition
Rating Methodology - Infrastructure Sector Ratings
Financial ratios – Non-Financial Sector

About the Company

PKIL is a special purpose vehicle (SPV) incorporated on June 26, 2006, as a private limited company and thereafter converted into a public limited company on February 04, 2010. PKIL is promoted by Patel Engineering Limited (PEL), KNR Constructions Limited (KNRCL) and Enpro Limited (EL) in the ratio 42:40:18, to undertake 4-laning of the AP/Karnataka Border-Avathi village section from Km 463/0 to Km 524/0 on NH-7 under North-South Corridor (NHDP Phase–II) on BOT basis. The Concession was awarded to the Patel-KNR consortium based on its quote for lowest semi-annuity of Rs.32.94 crore.

The Concession Agreement (CA) was signed on September 28, 2006, with a concession period of 20 years including a 24-month implementation period ending on March 25, 2027. The project cost was initially estimated at Rs.496.56 crore to be financed in a Debt/Equity ratio of 3:1. However, the delay in handing over of RoW resulted in cost overrun to the tune of Rs.26.90 crore and the incremental cost was funded by the promoters by way of unsecured loans. The company achieved Commercial Operations Date (COD) as on December 21, 2009. PKIL has been receiving timely annuities since March 2010 (due in March and September every year) from NHAI.

KNRCL has entered into a number of Joint Ventures (JVs) with various reputed construction companies since its inception. On a total income of Rs.934 crore in FY16, KNRCL earned a PAT of Rs.161 crore (standalone). PEL has over 67 years of operations; however there has been deterioration in credit profile of PEL. PEL reported a Loss of Rs. 18.69 crore on total operating income of Rs.2,161.50 crore during FY16. EIL (prospective promoter) is an infrastructure arm of Essel Group with interest in road projects, urban infrastructure, power, water management and solid waste management. The company has been developing urban recreational infrastructure in the form of theme parks in India like Essel World and Water Kingdom. As on March 31, 2016, EIL has 45 subsidiaries and 5 associates. During FY16, EIL's profit after tax (PAT) stood at Rs.17 crore on a total operating income of Rs.500 crore vis-à-vis PAT of Rs.29 crore on a total operating income of Rs.506 crore in FY15.

On November 12,2016 , PEL and KNRCL signed definitive agreements for sale of 100% stake in PKIL and Patel KNR Heavy Infrastructures Ltd. (PKHIL), another SPV of the same promoters, to Express Way Developer Ltd. (Step down subsidiary of Essel Highways Ltd. which in turn is a step down subsidiary of Essel Infraprojects Ltd. (EIL)). The transaction is expected to be executed after the completion of certain precendented conditions by end of March 2017.

Status of non-cooperation with previous CRA: Not Applicable

Any other information: Not Applicable

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

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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****For detailed Rationale Report and subscription information, please contact us at www.careratings.com**

About CARE Ratings:

CARE Ratings commenced operations in April 1993 and over two decades, it has established itself as one of the leading credit rating agencies in India. CARE is registered with the Securities and Exchange Board of India (SEBI) and also recognized as an External Credit Assessment Institution (ECAI) by the Reserve Bank of India (RBI). CARE Ratings is proud of its rightful place in the Indian capital market built around investor confidence. CARE Ratings provides the entire spectrum of credit rating that helps the corporates to raise capital for their various requirements and assists the investors to form an informed investment decision based on the credit risk and their own risk-return expectations. Our rating and grading service offerings leverage our domain and analytical expertise backed by the methodologies congruent with the international best practices.

Annexure-1: Details of Instruments/Facilities

Name of the Instrument	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. crore)	Rating assigned along with Rating Outlook
Fund Based - LT-Term Loan	April 21, 2010	9.57% p.a.	April 14, 2027	295.81	CARE AAA (SO) (Under Credit watch with Developing Implications)

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 2016-2017	Date(s) & Rating(s) assigned in 2015-2016	Date(s) & Rating(s) assigned in 2014-2015	Date(s) & Rating(s) assigned in 2013-2014
1.	Debentures-Non Convertible Debentures	LT	295.81	CARE AAA (SO) (Under Credit watch with Developing Implications)	-	1)CARE AAA (SO) (15-Jan-16)	1)CARE AAA (SO) (02-Feb-15)	1)CARE AAA (SO) (08-Jan-14)

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