Dodaballapur Hoskote Highways Private Limited (Revised)

August 05, 2022

Rating

Facilities/Instruments	Amount (₹ crore)	Rating[1]	Rating Action
Long Term Bank Facilities	395.00	CARE A-; Stable (Single A Minus; Outlook: Stable)	Reaffirmed
Total Bank Facilities	**395.00 (₹ Three Hundred Ninety-Five Crore Only)**		

Details of instruments/facilities in Annexure-1.

Detailed rationale and key rating drivers

The rating assigned to the bank facilities of Dodaballapur Hoskote Highways Private Limited (DHHPL) continues to factor in the inherent strengths of hybrid annuity model (HAM) based road projects such as (i) low project funding risk with inflation-indexed annuity to be received for construction and favorable clauses introduced in the concession agreement (CA) to de-bottleneck project execution challenges (ii) lower post implementation risk on account of inflation-indexed annuity to be received for operations and maintenance (O&M) of the road and (iii) receipt of bank rate linked interest annuity. However, unlike the clauses contained in the CA, delay in de-scoping of the unavailable project land has been witnessed in many of the ongoing HAM road projects.

The rating of DHHPL continues to derive comfort from the established track record of its sponsor and engineering, procurement and construction (EPC) contractor i.e., Dilip Buildcon Limited (DBL; rated 'CARE A-; Stable / CARE A2+') in executing large sized road projects which is evident from the ahead of schedule completion for most of its HAM projects. Furthermore, the rating takes into account credit quality of the underlying annuity receivables from National Highways Authority of India (NHAI; rated 'CARE AAA; Stable') post commencement of operations, liquidity support mechanisms such as the envisaged creation of debt service reserve account (DSRA) and major maintenance reserve account (MMRA) post commencement of operations, relatively lower debt levels as against bid project cost leading to adequate debt coverage indicators and shortfall undertaking extended by the sponsor to fund any shortfall during the construction as well as operational period. Furthermore, DBL has also extended irrevocable and unconditional corporate guarantee for the debt availed by DHHPL for the entire tenure of the loan, which provides added comfort.

The above rating strengths are, however, tempered by the inherent construction risk with the interest rate risk and operations and maintenance (O&M) risk.

Rating sensitivities

Positive factors – Factors that could lead to positive rating action/upgrade:

- Completion of project before the scheduled project completion date leading to receipt of bonus.
- Establishment of track record of timely receipt of annuities post commencement of operations.

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

- Significant delay in the project progress due to non-availability of the land within stipulated time frame or significant delay in the descoping of the unavailable land.
- Deterioration in debt service coverage ratio (DSCR) below 1.20 times due to increase in O&M expenses or annuity deductions, if any.
- Deterioration in the credit profile of sponsor - DBL or the counterparty i.e., NHAI.

Detailed description of the key rating drivers

<u>Key rating strengths</u>

Favorable clauses in model CA of HAM projects for addressing execution challenges; albeit certain instances of delay in actual de-scoping of the unavailable project land have emerged as a concern for the sector: The model CA of HAM projects include favorable clauses such as achievement of at least 80% RoW before declaring appointed date for the project and provision for granting deemed completion of the project in case 100% of the work is completed on the RoW which becomes available to it within 180 days of the appointed date. These clauses were expected to address some of the issues which were plaguing the sector primarily on account of delay in land acquisition during construction phase. Besides, stringent

[1]Complete definition of the ratings assigned are available at www.careedge.in and other CARE Ratings Ltd.'s publications

clauses for levy of damages, encashment of performance security as well as requirement of additional performance security in case of delay in execution due to reasons attributed to the concessionaire also exert some pressure on the developer for ensuring timely execution. However, pending de-scoping of unavailable land despite significant time having lapsed from the appointed date has been affecting the project progress in some of the projects awarded under this model which has emerged as a cause of concern from the credit perspective for the industry. Hence, timely de-scoping of unavailable project land within 180 days from appointed date by NHAI as per terms of CA will be a key monitorable for HAM-based road projects. However, during July 2020; NHAI released an SOP pertaining to the approach towards de-scoping whereby, immediately after the expiry of the period of appointed date plus 20% of the construction period, the pending RoW will be removed from the scope of work and the BPC shall be suitably reviewed which expected to ease some concerns. The RoW available for DHHPL is 80.32% on length-wise basis till June 2022.

Low funding risk and permitted price escalation: HAM model entails lower sponsor contribution during construction period considering 40% construction support from NHAI and availability of 10% mobilization advances on bid project cost (BPC) at bank rate. Nevertheless, instances of delay in issuance of bank guarantee for availing mobilization advances and term loan disbursement due to challenging funding environment can hinder the project progress. Further, BPC and O&M cost shall be inflation indexed [through a Price Index Multiple (PIM)], which is the weighted average of Wholesale Price Index (WPI) and Consumer Price Index (CPI) in the ratio of 70:30. Inflation indexed BPC protects the developers against price escalation to an extent.

Assured cash flow due to annuity nature of the revenue stream linked to inflation indexed O&M annuity and bank rate linked interest annuity: Besides the construction milestone payments during construction, during operational phase, cash flow is assured in the form of annuity payments from NHAI on semi-annual basis covering 60% of the project completion cost along with interest at bank rate plus 3% on reducing balance and inflation indexed O&M annuity. However, the above feature may get diluted in cases where there exists a lag between reduction in bank rate and lending rate exposing the company to the interest rate risk.

Low counterparty credit risk: Incorporated by the Government of India (GoI) under an Act of the Parliament as a statutory body, NHAI functions as the nodal agency for development, maintenance, and management of the national highways in the country. The outlook on NHAI reflects the outlook on the sovereign, whose direct and indirect support continues to be the key rating driver.

Demonstrated track record of DBL in executing road projects: DBL has demonstrated track record of successfully operating and maintaining build-operate and transfer (BOT) projects for more than a decade. DBL has pan India presence in more than 14 states with diversified execution capabilities in roads & bridges, mining, water sanitation, sewage, dams, irrigation, industrial, commercial, and residential buildings. Further, larger fleet of construction equipment as compared to its peers enables it to complete most of the projects ahead of schedule and consequently earn early completion bonus. RHPL is also expected to enter into fixed price EPC contract with DBL for execution of the project. DBL as a promoter has infused ~56% of the equity commitment till May 25, 2022. DHHPL has also entered fixed price EPC contract with DBL for the execution of project.
Further, DBL as a sponsor, has also extended unconditional and irrevocable undertaking in favor of DHHPL to fund cost overrun over and above budgeted cost and shortfall in debt servicing in case of non-payment/delayed payment/shortfall in payment of annuity or termination of the CA. DBL has also extended Corporate Guarantee for the debt availed by DHHPL valid for the entire tenure of the debt, which provides added comfort.

Key rating weaknesses

Inherent execution risk; albeit partly offset by execution capability of DBL: DHHPL is exposed to inherent construction risk attached with BOT road projects. The appointed date for the project is received and company has also achieved financial closure. DHHPL currently has 80.56% right of way (ROW) on 3H basis, which further elevates the project execution risk. Timely handover of the balance ROW shall remain crucial for the overall project progress. Project stretch is to be constructed with flexible pavement for the main carriageway as well as service road while rigid pavement for toll plaza. Total structural work of the project stretch constitutes around 36% of the EPC cost (excluding inflation), indicating relatively moderate complexity in the project.
DHHPL has achieved physical progress of 57.45% and financial progress of 67% till May 2022 and the project is progressing on schedule. The project has received three milestone payments from NHAI based on achieving 50% physical progress till May 2022, which is as per schedule.

Inherent O&M risk associated with the project: Although inflation indexed O&M annuity partly mitigates O&M risk, developers would still face the risk of sharp increase in the O&M cost due to more than envisaged wear and tear and aggressive bidding in O&M cost. Flexible pavement is prone to more wear and tear than rigid pavement. However, DHHPL is expected to enter into fixed price O&M contract and MM contract with the sponsor DBL which is expected to mitigate the O&M risk to an extent. Furthermore, the sponsor has extended undertaking to infuse funds in case of higher than envisaged O&M and Major Maintenance (MM) expense which also provides additional comfort. Also, as per the sanction conditions, DHHPL is required to maintain a Major Maintenance Reserve Account (MMRA) out of the project cash flow to conduct their major maintenance on the project stretch.

Inherent interest rate risk: DHHPL is exposed to inherent interest rate risk since the project debt is sanctioned with a floating rate of interest which is reset periodically. The interest rate risk is partially mitigated on account of receipt of the interest annuity at the applicable bank rate +300 bps. However, DHHPL remains exposed to interest rate risk due to non-linear transmission of bank rate and time lag between reduction in the bank rate and lending rate. However, steep impact on debt coverage indicators is precluded due to higher gap expected between inflation indexed completion cost and cost of project considered for financial closure.

Liquidity: Adequate
DHHPL's liquidity is underpinned from the fact that it has access to timely need-based support from DBL as well as from the fact that DBL has extended undertaking to fund any short fall, cost overrun over and above the budgeted cost along with O&M and major maintenance expenses. Also, as per the terms of sanction of the project debt, the company shall maintain DSRA, of an amount equivalent to ensuing six months of interest and principal repayment apart from creation of major maintenance reserve account during operation phase which is expected to provide financial cushion to DHHPL.

Analytical approach
Standalone while factoring execution track record of EPC contractor along with sponsor support undertaking to meet any shortfall in debt servicing during construction as well as operational phase.

Applicable criteria
Policy on default recognition
Factoring Linkages Parent Sub JV Group
Financial Ratios – Non financial Sector
Liquidity Analysis of Non-financial sector entities
Rating Outlook and Credit Watch
Project stage companies
Construction
Hybrid Annuity Model based road projects
Policy on Withdrawal of ratings

About the company
DHHPL, a special purpose vehicle (SPV) incorporated and owned by Dilip Buildcon Limited (DBL; rated 'CARE A-; Stable / CARE A2+'); has entered into 17-year concession agreement (including construction period of 730 days from appointed date) with National Highways Authority of India (NHAI, rated 'CARE AAA; Stable') for the design, build, operate and transfer (DBOT) of 38 km road on hybrid annuity model basis (HAM). The project under consideration aims at four laning of existing two-lane carriageway for the section from Dodaballapur Bypass (Km.42.00) on NH 648 (Old NH-207) to Hoskote Section (Km. 80.00) (approx. length of 38.00 km) in the state of Karnataka under Bharatamala Pariyojana. The bid project cost for the project is Rs.1278.00 crore while the total estimated project cost is Rs.1007.18 crore to be funded through construction grant from NHAI of Rs.511.20 crore (excluding inflation), debt of Rs.395 crore and balance through promoter's contribution. The project received Appointed Date on February 22, 2021.

Brief Financials:

Brief Financials (₹ crore)	FY21 (A)	FY22 (A)	Q1 FY23 (UA)
Total operating income	NA	NA	NA
PBILDT	NA	NA	NA
PAT	NA	NA	NA
Overall gearing (times)	NA	NA	NA
Interest coverage (times)	NA	NA	NA

NA: Not Applicable as the company is a project stage entity

Status of non-cooperation with previous CRA: Not Applicable

Any other information: Not Applicable

Rating history for the last three years: Please refer Annexure-2

Covenants of the rated instruments/facilities: Detailed explanation of covenants of the rated instruments/facilities is given in Annexure-3

Complexity level of various instruments rated for this company: Annexure-4

Annexure-1: Details of instruments/facilities

Name of the Instrument	ISIN	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (₹ crore)	Rating Assigned along with Rating Outlook
Term Loan-Long Term		-	-	March 2036	395.00	CARE A-; Stable

Annexure-2: Rating history for the last three years

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating History			
		Type	Amount Outstanding (₹ crore)	Rating	Date(s) and Rating(s) assigned in 2022-2023	Date(s) and Rating(s) assigned in 2021-2022	Date(s) and Rating(s) assigned in 2020-2021	Date(s) and Rating(s) assigned in 2019-2020
1	Term Loan-Long Term	LT	395.00	CARE A-; Stable	-	1)CARE A-; Stable (06-Jan-22) 2)CARE A-; Stable (16-Apr-21)	-	-

Annexure-3: Detailed explanation of the covenants of the rated instruments/facilities: Not Applicable

Annexure-4: Complexity level of various instruments rated for this company

Sr. No.	Name of Instrument	Complexity Level
1	Fund-based-Long Term	Simple

Annexure-5: Bank lender details for this company

To view the lender wise details of bank facilities please click here

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

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About us:
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