DBL Bangalore Nidagatta Highways Private Limited

July 06, 2021

Rating

Facilities	Amount (Rs. crore)	Rating[1]	Rating Action
Long Term Bank Facilities	752.00	CARE A-; Stable (Single A Minus; Outlook: Stable)	Reaffirmed
Total Facilities	752.00 (Rs. Seven Hundred Fifty-Two Crore Only)		

Details of instruments/facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

The rating assigned to the bank facilities of DBL Bangalore Nidagatta Highways Pvt Ltd (DBNHPL) 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 of the stretch and favourable 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 albeit non-linear transmission of bank rate on lending rate is a growing concern for HAM projects. However, unlike the clauses contained in the CA, delay in de-scoping of the unavailable project land has been witnessed in many of the on-going HAM road projects.

The rating further continues to derive strength from the established track record of its sponsor and engineering, procurement and construction (EPC) contractor i.e. Dilip Buildcon Ltd (DBL; rated 'CARE A; Stable/ CARE A1') in executing large sized road projects along with ahead of schedule progress of DBNHPL. The rating continues to remain underpinned by low counterparty risk towards annuity receivables from National Highways Authority of India(NHAI, rated CARE AAA; Stable) post commencement of operations, presence of defined cashflow mechanism by way of escrow arrangement, proposed 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 (BPC) leading to adequate debt coverage indicators along with undertaking extended by the sponsor to fund any shortfall during construction as well as operational period. The rating also takes cognisance of grant of extension of time of 90 days owing to COVID-19.

The above rating strengths are, however, tempered by the inherent construction risk associated with timely completion of the project along with O&M risk and inherent interest rate risk.

Key Rating Sensitivities:

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

- Completion of the project before the scheduled project completion date.
- Establishment of track record of timely receipt of annuities post commencement of operations and creation of stipulated DSRA
- Improvement in debt coverage ratio on account of a significant decline in the interest rate on the borrowed debt.

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

- Significant delay in project progress impacting COD beyond 90 days from revised schedule project completion date (SPCD).
- Deterioration in the credit profile of the sponsor (i.e. DBL) or the counter- party (i.e. NHAI)

Detailed description of the key rating drivers

Key Rating Strengths

Favourable clauses in model CA of HAM projects to address execution challenges; albeit certain instances of delay in actual de-scoping of unavailable project land has emerged as a concern for the industry: The model CA of HAM projects includes favourable clauses such as achievement of atleast 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. However, pending de-scoping of unavailable land despite significant time having lapsed from the appointed date has been affecting the project

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

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. In case of DBNHPL too, the RoW available is 96.26% on 3H basis as on April 30, 2021 while 100% land is available on the 3G basis.

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 advance 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: 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, non-linear transmission of bank rate over lending rate is expected to impact the company's debt coverage indicators to an extent.

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 15 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. DBNHPL has also entered into fixed price EPC contract with DBL for execution of the project. Most of the on-going HAM projects are progressing ahead of schedule which reflects its sound execution capability.

Liquidity Analysis: Adequate

DBNHPL's liquidity is adequate as it has access to timely need-based support from DBL as well as from the fact that as a sponsor, it has extended contractual commitment in the form of unconditional and irrevocable sponsor support undertaking to fund any cost overrun and shortfall in servicing debt obligations of DBNHPL due to non-payment or delayed payment or shortfall in annuity payments for any reason whatsoever, in the event of termination of the CA for any reason or due to escalation in expenses. DBL shall also support to meet any increase in O&M expenses and Major Maintenance (MM) expenses or to meet any shortfall in Major Maintenance Reserve (MMR). 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 in form of fixed deposit receipts (FDR) or Bank Guarantee in respect of the facility which is expected to provide liquidity cushion to DBNHPL.

Key Rating Weaknesses:

Inherent execution risk albeit partly offset by ahead of schedule project progress and demonstrated execution capability of DBL: DBNHPL is exposed to inherent construction risk attached to BOT road projects. However, the project is progressing ahead of schedule and has achieved 79.08% physical progress as on April 30, 2021 and it achieved the fourth construction milestone (75% physical progress) on March 6, 2021, which was 119 days ahead of the revised schedule. Owing to spread of COVID-19, DBNHPL, under the Atmanirbhar Bharat financial package of GOI has received an EOT of 90 days from NHAI, thereby shifting the SPCD to February 9, 2022 from earlier November 9, 2021. The company has received four tranches of construction grant till April 30, 2021 including inflation of Rs.33.63 crore. The RoW available is 96.26% on 3H basis and 100% on 3G basis. Further, demonstrated execution capability of DBL as an EPC contractor in executing large sized road projects is expected to mitigate the execution risk to an extent.

The 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 on the project stretch constitutes around 40% of the EPC cost (excluding taxes and inflation).

O&M risk associated with the project; albeit with partial mitigation through proposed signing of fixed price O&M contract with the sponsor: 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. The project stretch consists of flexible (bituminous) pavement which is prone to higher O&M cost compared to rigid pavement. However, DBNHPL shall enter into fixed price and fixed time O&M contract with the sponsor whereby DBL shall be responsible for the maintenance of the stretch, which provides some comfort. Also, DBL has extended undertaking to meet any increase in O&M and MM expenses along with meeting any shortfall in maintaining MMR which mitigates the maintenance risk to an extent.

Inherent interest rate risk: DBNHPL is exposed to inherent interest rate risk since the project debt is sanctioned with a floating rate of interest which is reset periodically. While the risk is partially mitigated on account of receipt of the interest annuity at the applicable bank rate + 300 bps, DBNHPL remains exposed to interest rate risk owing to the timing difference between change in the bank rate & lending rate and non-linear transmission of change in bank rates to lending rates. 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.

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
Criteria on assigning ‘outlook’ and ‘credit watch’ to Credit Ratings
CARE’s Policy on Default Recognition
Financial Ratios – Non-Financial Sector
Liquidity Analysis of Non-Financial Sector Entities
Rating Methodology: Notching by factoring linkages in Ratings
Rating Methodology – Hybrid Annuity Road Projects

About the Company
DBNHPL, a special purpose vehicle (SPV) incorporated and owned by DBL has entered into 17.5 year concession agreement (CA) (including construction period of 910 days from appointed date) with NHAI for the design, build, operate and transfer (DBOT) of 56.2 km road on hybrid annuity basis.
The project under consideration aims at six laning of existing four lane carriageway for the section from Bangalore (Km.18.00) to Nidagatta (Km. 74.20) (approx. length of 56.20 km) including the construction of two new six lane bypasses to towns of Bidadi, Ramanagara & Channapatna on NH-275 in the state of Karnataka. The bid project cost for the project is Rs.2190.00 crore as against NHAI project cost of Rs.1984.00 crore. However, the total cost of completion of the project is Rs.2004.84 crore being funded through construction grant from NHAI of Rs.944.10 crore (including inflation of Rs.68.10 crore), debt of Rs.752 crore and balance through promoter’s contribution. The project achieved financial closure on April 2, 2019 and appointed date on May 14, 2019.

Brief Financials: Not applicable as DBNHPL is a project stage company.

Status of non-cooperation with previous CRA: Not Applicable

Any other information: Not Applicable

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

Complexity level of various instruments rated for this company: Please refer Annexure-3

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	-	-	August 2034	752.00	CARE A-; Stable

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 2021-2022	Date(s) & Rating(s) assigned in 2020-2021	Date(s) & Rating(s) assigned in 2019-2020	Date(s) & Rating(s) assigned in 2018-2019
1.	Fund-based - LT-Term Loan	LT	752.00	CARE A-; Stable	-	1)CARE A-; Stable (03-Jul-20)	1)CARE A-; Stable (25-Jun-19)	1)Provisional CARE A-; Stable (21-Aug-18)

Annexure 3: Complexity level of various instruments rated for this company

Sr. No.	Name of the Instrument	Complexity Level
1.	Fund-based - LT-Term Loan	Simple

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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