Patel KNR Infrastructures Limited

December 09, 2022

Rating

Instruments	Amount (₹ crore)	Rating[1]	Rating Action
Non-convertible debentures	156.34 (Reduced from 181.64)	CARE AA+; Stable (Double A Plus; Outlook: Stable)	Reaffirmed
Total instruments	156.34 (₹ One hundred fifty-six crore and thirty-four lakh only)		

Details of instruments in Annexure-1

Detailed rationale and key rating drivers

The rating assigned to the long-term non-convertible debenture (NCD) issued by Patel KNR Infrastructures Limited (PKIL) continues to derive strength from the long track record of timely receipt of annuity payments and structured payment mechanism, whereby biannual annuity is received from National Highways Authority of India (NHAI, rated 'CARE AAA; Stable') in an escrow account for servicing of the NCDs. The rating also derives strength from the fixed rate of coupon eliminating the interest rate risk, strong credit profile and significant experience of operations and maintenance (O&M) contractor (i.e., KNR Constructions Limited), maintenance of debt-service reserve account (DSRA) as per the terms of the Debenture Trust Deed (DTD) and sponsors undertaking for infusion of funds for any shortfall in meeting major maintenance (MM) expenses over and above the budgeted expenses as well as not to withdraw the surplus cash. The rating also factors in timely receipt of 26th and 27th semi-annuity payments (in March 2022 and September 2022) without any deductions.

PKIL continues to remain exposed to the risks arising out of possibility of lower disbursal of annuity than stipulated due to non-adherence to clauses in Concession Agreement (CA) pertaining to maintenance of project stretch, higher-than-envisaged increase in the O&M expenses and absence of suitable amendments in fixed MM contract in line with the revised MM estimates. Hence, the timely maintenance of the road stretch as per CA to ensure adequate cash flows without any deduction by the Authority would be important from the credit perspective.

Rating sensitivities

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

- Minimum debt-service coverage ratio (DSCR) should be more than 1.10x for every year for the projected period (post factoring all the requisite provisions and excluding interest income).

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

- Non-receipt/significant delayed/reduced receipt of annuities and higher O&M and MM expenses vis-à-vis envisaged
- Withdrawal of any cash balance by the sponsors from the escrow account.

Detailed description of the key rating drivers

Key rating strengths

Timely receipt of annuity from NHAI: PKIL is an annuity project and is not exposed to any traffic risk. The revenue source for PKIL is the bi-annual annuity (i.e., due on March 26th and September 24th of every year) of ₹32.94 crore receivable from NHAI up to March 26, 2027. PKIL has a track record of timely receipt of annuity payments from NHAI and has received 26th and 27th semi-annual payments from the Concessioning Authority without any deduction (except TDS). Furthermore, the project is operating since more than 13 years having final completion certificate, and hence, there is no construction 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

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

country. The outlook on NHAI reflects the outlook on the sovereign, whose direct and indirect support continues to be the key rating driver.

Structured payment mechanism for debt servicing and maintenance of DSRA: PKIL has opened and maintained an 'Escrow account' with the Escrow bank with the first priority assigned towards O&M expenses followed by debt servicing of the NCD and appropriation to DSRA and other relevant expenses, in that order. 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 continues to maintain DSRA as per the terms of the DTD of ₹15 crore as on November 15, 2022, in the form of fixed deposits, which covers about 70% of next six month's debt servicing.

Completion of two MM cycles: PKIL has successfully completed two MM cycles. The second cycle has been completed in FY21 (refers to the period April 1 to March 31) at a cost of ₹50.49 crore, lower than the envisaged cost of ₹52.81 crore.

Significant sponsor experience coupled with strong credit profile of KNRCL: The sponsors have established track record of project execution with O&M of large portfolio of infrastructure assets. KNR Constructions Limited (KNRCL – holding 40% stake in the company) was set up in 1995 and provides engineering, procurement, and construction (EPC) services across sectors, such as roads and highways, irrigation, and urban water infrastructure management. KNRCL had a strong outstanding order book of ₹9,350 crore as on June 30, 2022. The other sponsor, Patel Engineering Limited (PEL – holding 60% stake), has vast experience in the construction segment although the credit profile has relatively moderated over the years.

Fixed interest rate: The NCD repayment and coupon payment are made on semi-annual basis (i.e., due on October 14th and April 14th every year) with a fixed interest rate of 9.57% per annum throughout the tenure of the NCDs, thereby eliminating interest rate risk.

Key rating weaknesses

Higher expenditure on MM on account of revised estimates: KNRCL is the O&M contractor for the project and Patel-KNR joint venture (JV) (Patel: KNR in the ratio 60: 40) is undertaking the periodic maintenance. The special purpose vehicle (SPV) has incurred higher MM expenses than envisaged despite having a fixed price contract for MM, due to instructions from NHAI for overlaying the renewal coat on the road with 40 mm bituminous concrete (BC) as against 30 mm BC overlay as per the agreement. Accordingly, the company had revised estimates for the MM activity, which is higher than the initial estimates by more than 75% for the third MM cycle. Post revision in the estimates of the MM expenditure, the company has not amended the fixed price contract entered with the contractor for execution of MM though payment thereof is being made as per the revised estimates instead of fixed price. As the promoters have provided undertaking to cover the cash shortfall over the revised estimates instead of fixed price contract, the cost of additional MM expense is borne by the company. Higher MM expense over and above the fixed price contract already executed has led to moderation in debt service coverage indicators of the company. The receipt of annuity from NHAI is fixed and is not linked to the toll revenue on the project road. However, the receipt thereof in full is linked to the maintenance of road in line with the clauses stipulated in concession agreement. Hence, the same would remain important from the credit perspective. Furthermore, during FY22, owing to cyclone and heavier than normal rainfall in the area, despite completion of second MM activity recently last year, additional maintenance expense was required to be incurred. The same was met out of project cash accruals despite presence of sponsor undertaking.

Inherent maintenance risk associated with road projects: In order to mitigate 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 contractor in carrying out routine and Major Maintenance Activity (MMA) might translate into reduction in annuity receivables. Such shortfall in annuity will have a direct bearing on the envisaged debt servicing capability of PKIL.

No tail period: The last principal instalment of ₹16.94 crore and coupon payment of NCD is due on April 14, 2027, whereas the concession end date is March 25, 2027. The last annuity of ₹32.94 crore will be received during the month of March 2027 and

DSRA of ₹15 crore is maintained till the tenor of the NCD, which together would be sufficient to repay the last principal instalments and coupon payments. In addition, the surplus liquid reserves as maintained till April 2027 is also expected to be available.

Liquidity: Strong

The liquidity position of PKIL continues to remain strong with cash flow receivable from NHAI in the form of annuity of ₹65.88 crore as against the repayment obligations of ₹42.08 crore in FY23 with a T+20 repayment. PKIL has already repaid the debt obligation for FY23 and had liquid investments of ₹15 crore for DSRA (covers 70% of next six month's interest and principal), lien marked to lender and ₹37.16 crore towards MM and other exigencies as on November 15, 2022.

Analytical approach: Standalone

Applicable criteria

Rating Outlook and Credit Watch
CARE's Policy on Default Recognition
Rating Methodology – Annuity-based Road Projects
Rating Methodology - Infrastructure Sector Ratings (ISR)
Liquidity Analysis of Non-Financial Sector Entities
Financial ratios – Non-Financial Sector

About the company

Patel-KNR Infrastructures Limited (PKIL) is a special purpose vehicle (SPV) incorporated on June 26, 2006, for developing four-laning of national highways section "Km 463.6 (AP/Karnataka border) to Km 524.0 (Avathi Village), covering 60.42 Kms" on NH-7 in the state of Karnataka on build-operate-transfer (BOT) annuity basis. The concession was awarded to the consortium, Patel-KNR JV based on its quote for lowest semi-annual annuity of ₹32.94 crore. The concession agreement (CA) between PKIL and National Highways Authority of India (Authority) was signed on September 28, 2006. The concession is for a period of 20 years including construction period of 24 months.

The company is jointly promoted by Patel Engineering Limited with 60% shareholding and KNR Constructions Limited with 40% shareholding. The completion certificate for the project was received on March 31, 2017; however, post grant of PCOD in December 2009, the company has been receiving annuity since March 2010 from NHAI.

Brief financials:

Brief Financials (₹ crore)	31-03-2021 (A)	31-03-2022 (A)	H1FY23 (U/A)
Total operating income	37.42	43.08	16.73
PBILDT	27.85	16.24	5.95
PAT	5.67	(2.32)	(2.41)
Overall gearing (times)	3.92	3.63	NA
Interest coverage (times)	1.38	0.90	0.73

A: Audited, U/A: Unaudited, NA: Not available

Status of non-cooperation with previous CRA: Not applicable

Any other information: Not applicable

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

Covenants of 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

Name of the Instrument	ISIN	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (₹ crore)	Rating Assigned along with Rating Outlook
Non-convertible debentures	INE057L07016	October 23, 2010	9.57	April 14, 2027	156.34	CARE AA+; Stable

Annexure-2: Rating history of 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	Debentures-Non-convertible debentures	LT	156.34	CARE AA+; Stable	-	1)CARE AA+; Stable (05-Jan-22)	1)CARE AA+; Stable (06-Jan-21)	1)CARE AA+; Stable (24-Mar-20)

Annexure-3: Detailed explanation of covenants of the rated instrument/facilities:

Name of the Instrument	Detailed explanation
A. Financial covenants	
I. Debt-service coverage ratio (DSCR)	Maintain at all times a DSCR of 1.11x of all annuity payments

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

Sr. No	Name of instrument	Complexity level
1	Debentures-Non-convertible debentures	Simple

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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