IRCON Ludhiana Rupnagar Highway Limited

March 23, 2023

Facilities/Instruments	Amount (₹ crore)	Rating[1]	Rating Action
Long-term bank facilities	570.82	CARE AA (CE); Stable*	Assigned

Details of instruments/facilities in Annexure-1.
*Backed by an unconditional and irrevocable corporate guarantee of Ircon International Limited valid until 180 days from the commercial operations date or the receipt of the first full annuity, whichever is later.

Unsupported rating	CARE A-

Note: Unsupported rating does not factor in the explicit credit enhancement.

Rationale and key rating drivers for the credit-enhanced debt

The rating assigned to the bank facilities of IRCON Ludhiana Rupnagar Highway Limited (ILRHL) primarily factors in the unconditional and irrevocable corporate guarantee (CG) of Ircon International Limited (IRCON; rated 'CARE AAA; Stable/CARE A1+'), a Government of India (GoI) enterprise and a Miniratna Category-I public sector undertaking (PSU), which will be valid until 180 days from the commercial operations date (COD) or the receipt of the first full annuity, whichever is later, thereby covering the risks associated with the project during the entire construction period.

The rating is underpinned by the inherent strengths of the hybrid annuity model (HAM)-based road projects, such as (i) lower project funding risk with 40% of the bid project cost (BPC) available as a grant from the National Highways Authority of India (NHAI; rated 'CARE AAA; Stable') during the construction period, inflation-indexed annuity to be received for construction and favourable clauses introduced in the concession agreement (CA) to mitigate challenges to project execution, (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 the marginal cost of lending rate (MCLR)-linked interest annuity.

Furthermore, the rating of ILRHL also derives strength from the fixed-price engineering, procurement, and construction (EPC) contract with the sponsor – IRCON, which has an established track record of constructing roads and highways. The rating also favourably factors in the credit quality of the underlying annuity receivables from the NHAI subsequent to the commencement of the operations. Furthermore, the comfortable debt coverage indicators, the liquidity support mechanism, such as upfront creation of a debt service reserve account (DSRA) on achievement of the COD, the proposed major maintenance reserve (MMR) and the sponsor undertaking to arrange additional amounts and funds to mitigate any liability arising due to the change in the base-case business plan or the assumptions made in the base case business plan are some of the other credit positives.

The above rating strengths are, however, tempered by the inherent construction risk associated with the project execution. Furthermore, the absence of cushion between the annuity due date and the repayment date, resulting in ad-hoc support from the sponsor to address possible cash flow mismatches if any, and susceptibility to changes in operations and maintenance (O&M) cost and interest rate, are other credit deterrents.

Key rating drivers of Ircon International Limited

The detailed rationale of the CG provider, IRCON, is available at the link: Ircon International Limited.

Key rating drivers of ILRHL

The unsupported rating assigned to the bank facilities of ILRHL takes into account the inherent strengths of the HAM-based road projects, including the credit quality of the underlying annuities to be received post-implementation. The liquidity support mechanism, such as the upfront creation of a DSRA on the COD, the proposed MMR, and the undertaking extended by the sponsor to arrange additional amounts and funds to mitigate any liability arising due to the change in the base case business plan or the assumptions made in the base case business plan, including any deficit in annuity payment on account of non-compliance of the maintenance obligations for the entire debt tenure, lends additional comfort.

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

The above rating strengths are, however, tempered by the construction risk associated with the project. Furthermore, susceptibility to changes in O&M risk and interest rate risk are other credit deterrents.

Rating sensitivities

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

- Completion of project on or before the scheduled COD.
- Track record of the timely receipt of annuities.

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

- Deterioration in the credit profile of the sponsor, IRCON, or counterparty, ie, NHAI.
- Delay in project progress including the achievement of project milestones, leading to levy of penalty by the NHAI, thereby affecting the financial risk profile.

Analytical approach

Credit enhancement in the form of an unconditional and irrevocable CG by IRCON, which is valid until the receipt of the first full annuity or 180 days from the COD, whichever is later. Post the validity period of the CG, CARE Ratings Limited (CARE Ratings) has analysed the project on a standalone basis while factoring in the sponsor's undertaking and the strong linkages with IRCON.

Unsupported rating: Standalone, while factoring in the sponsor's undertaking and the track record of the EPC contractor.

Outlook: Stable

The Stable outlook assigned to the bank loan facilities of ILRHL takes into account the inherent strengths of the HAM-based road projects, including the credit quality of the underlying annuities, upfront creation of a DSRA on the COD, and the undertaking extended by the sponsor to arrange additional amounts and funds to mitigate any liability arising due to the change in the base-case business plan including any deficit in annuity payment on account of non-compliance of the maintenance obligations for the entire debt tenure.

Key rating strengths

CG from IRCON until the receipt of first annuity

The detailed rationale of the CG provider, IRCON, is available at the link: Ircon International Limited. As per the CG, until the receipt of the first full annuity or 180 days from the COD, whichever is later, IRCON unconditionally and irrevocably guarantees to cover any event of default on the part of ILRHL towards debt servicing or compliance with any of the terms, conditions, and covenants contained in the facility agreements.

The guarantee stipulates that in the event of default by the borrower in repayment of the obligations, for the time being due and payable to the lender in respect of the facilities, the lender will invoke the guarantee immediately subsequent to the lapse of the cure period (if any) after the occurrence of an event of default at any time during the validity period. As per the facility agreement, the 'cure period' with respect to all the events of default is 60 days, except in case of a payment default on interest or principal, wherein no cure period is to be provided to the borrower. Subsequent to the invocation, the guarantor will pay the amount of guaranteed obligations to the lender forthwith immediately upon invocation of the guarantee by the lender, failing which, the lender will be entitled to approach the court of law for legal recourse and to file a recovery suit against the guarantor, after serving them 15 days legal notice to pay or repay the guaranteed obligations.

With this limited-period guarantee, construction and other risks that might materialise until the commissioning of the project are supported by the guarantor, which is viewed as a comforting factor.

Favourable clauses of hybrid annuity concession

The CA – in line with the model CA for HAM projects – includes clauses that serve to partially secure the project and its lenders against construction risks, including delays in land acquisition. Such clauses include stipulating the achievement of at least 80% right of way (RoW) as a precedent condition for declaring the appointed date for the project. Besides, there is a provision for granting deemed completion of the project in case 100% of the work is completed on the RoW, which becomes available to the concessionaire within 180 days of the appointed date. In addition, stringent clauses for levy of damages, encashment of performance security, as well as the requirement of additional performance security in case of delay in execution due to reasons attributed to the concessionaire, act as significant disincentives against slippages in execution.

Low funding risk and permitted price escalation
The HAM model entails lower sponsor contribution during the construction period considering 40% construction support from the NHAI and the availability of 10% mobilisation advances on the BPC. The BPC and O&M cost will be inflation-indexed (through a price index multiple [PIM]), which is the weighted average of the wholesale price index (WPI) and consumer price index (CPI) in the ratio of 70:30. The inflation-indexed BPC protects the developers against price escalation to an extent.

Cash flow visibility
During the operational phase, the cash flow is assured in the form of annuity payments from the NHAI on a semi-annual basis covering 60% of the project completion cost along with interest at an 'average of one-year MCLR of the top five scheduled commercial banks plus 1.25%' on the reducing balance and inflation-indexed O&M annuity.

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

Demonstrated track record of IRCON in executing road projects
The company has entered into a fixed-price EPC contract with IRCON, which has executed nation-building infrastructure projects in the roads, buildings, electrical substation and distribution, airport construction, commercial complexes, metro, and railway segments. IRCON has successfully commissioned four road projects in the public-private partnership (PPP) mode and has over four decades of experience in the construction and infrastructure sector. It is ably supported by a team of qualified engineers with significant expertise in road and highway construction.

Undertakings for meeting exigencies and proposed DSRA/MMRA
IRCON, as a sponsor, has extended an undertaking to the lenders to fund cost overruns beyond the budgeted cost and to arrange additional amounts and funds to mitigate any liability arising due to a change in the base case business plan or the assumptions made in the base case business plan, including any deficit in annuity payment on account of non-compliance of the maintenance obligations for the entire debt tenure.

Furthermore, as per the terms of the facility agreement, the company proposes to create and maintain a DSRA equivalent to the debt servicing requirement of three months of interest and one ensuing principal repayment upfront on the COD of the project. The facility agreement also stipulated the maintenance of an MMRA as per the base case business plan.

Key rating weaknesses

Inherent project execution risk
Notwithstanding the availability of about 82% of RoW and the demonstrated track record of IRCON as an EPC contractor in executing similar road projects, ILRHL is exposed to inherent construction risk attached to road projects. Nevertheless, the demonstrated track record of IRCON as an EPC contractor in executing large-sized road projects mitigates the execution risk to an extent.

Inherent O&M risk associated with the project
While the inflation-indexed O&M annuity partly mitigates O&M risk, the disparate movement in the inflation index (70% WPI; 30% CPI) and the O&M cost poses a risk. Besides, the company can face the risk of a sharp increase in the O&M cost in the event of the wear and tear on the road or road facilities being more than the extent envisaged during the bidding and aggressive bidding in O&M cost. However, the presence of a sponsor undertaking to fund any deficit in annuity payment on account of non-compliance with the maintenance obligations by the borrower mitigates the O&M risk to an extent.

Inherent interest rate risk
ILRHL is exposed to the inherent interest rate risk considering the floating rate of interest with a reset clause linked to the reset of spread every month. Although, the reimbursement of the interest cost in the form of interest annuity payable by the NHAI biannually at an interest rate equal to the average of one-year MCLR of the top five scheduled commercial banks plus the spread of 125 bps on 60% of the project completion cost (on the reducing balance) mitigates the risk arising in the earlier case due to the lag effect between the bank rate and the MCLR.

Liquidity: Adequate

For ILRHL: The company has received appointed date on February 16, 2023; following this mobilization of resources have begun. Furthermore, the various undertakings/CGs to fund any cost overruns for the project completion and O&M have been executed by the sponsor.

For IRCON: The detailed rationale of the CG provider, IRCON, is available at the link: Ircon International Limited.

Assumptions/Covenants: Not applicable

Environment, social, and governance (ESG) risks: Not Applicable

Applicable criteria

Policy on default recognition
Financial Ratios – Non financial Sector
Liquidity Analysis of Non-financial sector entities
Rating Credit Enhanced Debt
Rating Outlook and Credit Watch
Hybrid Annuity Model based road projects

About the Credit Enhancement Provider

IRCON was incorporated in April 1976 as Indian Railway Construction Company Limited, mainly for the construction of railway projects in India and abroad. IRCON is a Miniratna Category-I PSU since 1998. It is a Central Government company under Section 617 of the Companies Act, 1956, with a 73.18% shareholding held by the GoI as on February 28, 2023. The company has diversified into roads, buildings, electrical substation and distribution, airport construction, commercial complexes, and metro segments, but mainly earns its revenue from the railway segment. It raised funds through an initial public offering (IPO) in September 2018 through an offer for sale and was listed on the Bombay Stock Exchange (BSE) and the National Stock Exchange (NSE) on September 28, 2018.

Brief Financials (₹ crore)	March 31, 2021 (A)	March 31, 2022 (A)	9M FY23 (UA)
TOI	4,955.42	6,909.53	6487.66
PBILDT	350.43	361.28	626.57
PAT	404.56	544.33	538.65
Overall gearing (times)	0.94	0.97	NA
Interest coverage (times)	25.96	34.81	83.54

A: Audited; UA: Unaudited; NA: Not available.
Note:
1.Financials classified as per CARE Ratings' internal benchmarks.
2.The above results are latest financial results available

About the company and industry

Industry classification

Macro Economic Indicator	Sector	Industry	Basic Industry
Services	Services	Transport Infrastructure	Road Assets–Toll, Annuity, Hybrid-Annuity

ILRHL, a special purpose vehicle (SPV) promoted by IRCON, has entered into a 15-year CA (excluding a construction period of 730 days from the appointed date) with the NHAI for the construction of construction of four/six lane greenfield Ludhiana-Rupnagar NH-205K from junction with NE-5 village near Manewal (Ludhiana) to junction with NH-205 near Bheora Village

(Rupnagar) including spur to Kharar with Ludhiana bypass under Bharatmala Pariyojana in the State of Punjab on hybrid annuity mode: Package-3. The BPC of the project excluding goods and services tax (GST) is ₹1,107 crore.

Brief financials

ILRHL: Not applicable, as the project is under the implementation phase.

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

Lender details: Annexure-5

Annexure-1: Details of instruments/facilities

Name of the Instrument	ISIN	Date of Issuance (DD-MM-YYYY)	Coupon Rate (%)	Maturity Date (DD-MM-YYYY)	Size of the Issue (₹ crore)	Rating Assigned along with Rating Outlook
Fund-based - LT-Term Loan	NA	-	-	01-11-2035*	570.82	CARE AA (CE); Stable
Un Supported Rating-Un Supported Rating (Long Term)	NA	-	-	-	0.00	CARE A-

NA: Not applicable.
*Subject to company achieving the COD as per the base case financial plan.

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	Fund-based - LT-Term Loan	LT	570.82	CARE AA (CE); Stable				
2	Un Supported Rating-Un Supported Rating (Long Term)	LT	0.00	CARE A-				

*Long term/Short term.

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

Name of the Instrument	Detailed Explanation
A. Financial covenants	
Debt to equity ratio	Debt-to-equity ratio will not exceed 4:1
DSCR	DSCR will not be less than 1.00x (except for the first year of the COD) and the average DSCR will be 1.10x during the tenure of the facility
B. Non-financial covenants	Not applicable

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

Sr. No.	Name of Instrument	Complexity Level
1.	Fund-based - LT-Term loan	Simple
2.	Unsupported rating-Unsupported rating (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 the 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:

Established in 1993, CARE Ratings is one of the leading credit rating agencies in India. Registered under the Securities and Exchange Board of India, it has been acknowledged as an External Credit Assessment Institution by the RBI. With an equitable position in the Indian capital market, CARE Ratings provides a wide array of credit rating services that help corporates raise capital and enable investors to make informed decisions. With an established track record of rating companies over almost three decades, CARE Ratings follows a robust and transparent rating process that leverages its domain and analytical expertise, backed by the methodologies congruent with the international best practices. CARE Ratings has played a pivotal role in developing bank debt and capital market instruments, including commercial papers, corporate bonds and debentures, and structured credit.

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