DBL Poondiyankuppam Highways Limited

December 26, 2022

Rating

Facilities/Instruments	Amount (₹ crore)	Rating[1]	Rating Action
Long Term Bank Facilities	477.69	CARE A-; Stable (Single A Minus; Outlook: Stable)	Reaffirmed
Total Bank Facilities	**477.69 (₹ Four Hundred Seventy-Seven Crore and Sixty-Nine Lakhs Only)**		

Details of instruments/facilities in Annexure-1.

Detailed rationale and key rating drivers

The reaffirmation in the rating assigned to the bank facilities of DBL Poondiyankuppam Highways Private Limited (DPHPL) continues to factors 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 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 marginal cost of funds-based lending rate (MCLR) linked interest annuity. However, unlike the clauses contained in the construction agreement (CA), delay in de-scoping of the unavailable project land has been witnessed in some of the ongoing HAM road projects.

The rating continues to derive strength 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 along with satisfactory project progress in DPHPL.

Furthermore, the rating continues to remain underpinned by low counterparty risk towards annuity receivables from NHAI post commencement of operations, liquidity support mechanisms such as the envisaged creation of debt service reserve account (DSRA), 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 the operational period.

The above rating strengths are, however, constrained by inherent construction risk and the O&M risk associated with the project.

CARE Ratings notes the trigger of one of the previous negative rating sensitivities (as mentioned in press release dated December 23, 2021) related to deterioration in the sponsor i.e DBL's credit profile. Yet on time project progress, availability of right of way (RoW), relatively lower complexity of the project scope, equity infusion to the extent of 50% of the required contribution by the sponsor along with DBL's strong execution capability have partially supported DPHPL's credit profile.

Rating sensitivities

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

- Completion of project within scheduled project completion date
- 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
- Non-receipt of timely need-based support from the sponsor during construction and operational period.
- Deterioration in the credit profile of sponsor- DBL or 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 the unavailable project land have emerged as a concern for the industry: The model CA of HAM projects includes favorable clauses such as achievement of at least 80% Right of Way (RoW) before declaring an 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 the construction phase. Besides, 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 also exert some pressure on the developer for ensuring timely execution. However, pending de-scoping of unavailable land

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

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. However, during July 2020, NHAI released a standard operating process (SOP) pertaining to the approach towards de-scoping whereby, immediately after the expiry of the period of the 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 has eased out some issues. In case of DPHPL, the RoW available is 92.11% as on October 31, 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 MCLR-linked interest rate. Furthermore, the BPC and O&M costs 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, which 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 the operational phase of the project, cash flow is largely assured in the form of annuity to be received from NHAI on semi-annual basis covering 60% of the project completion cost along with interest at '1-year MCLR of top five scheduled commercial banks plus 1.25%' on reducing balance and inflation-indexed O&M annuity.

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. NHAI is vested with executive powers for developing national highways in India by the Ministry of Road Transport & Highways (MoRTH). 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. The order book position of DBL stood healthy at Rs.26,338 crore as on September 30, 2022. Furthermore, 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. DPHPL has entered into fixed-price EPC contract with DBL for execution of the project.

Interest annuities linked to MCLR, mitigating the interest rate risk to a large extent
Both the interest annuities and the interest on debt are linked to MCLR. Interest annuities are linked to 1-year average MCLR of top five scheduled commercial banks plus 1.25% and interest on term loan is also linked to the MCLR which mitigates the interest rate risk to a large extent.
Moreover, as per the proposed sanction terms, DPHPL shall be required to create and maintain DSRA till the tenor of the debt to meet any shortfall in the debt service requirements. DSRA shall be created in funded, equivalent to the ensuing six months principal and six months interest obligations after meeting the debt service obligations during the operational phase which provides cushion for the debt servicing.

Key Rating Weaknesses
Inherent execution risk: DPHPL is exposed to inherent construction risk attached to BOT road projects. The company has received appointed date on November 15, 2021 and has 92.11% land available on 3H basis. Project stretch is to be constructed with rigid pavement. Total structural work constitutes around 46% of the EPC cost which indicates a moderately complex nature of the project stretch. The project is adequately bid with bid project cost (BPC) being 17.46% above NHAI cost. DPHPL has achieved physical progress of 34% as on October 31, 2022. Furthermore, 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.

Inherent O&M risk: Although, receipt of inflation-indexed O&M annuity partly mitigates O&M risk, developers would still face the risk of a sharp increase in the O&M cost due to more than envisaged wear and tear and aggressive bidding in O&M cost. Also, as per the sanctioned terms, DPHPL is not required to maintain any major maintenance reserve account (MMRA) out of the project cash flow to conduct major maintenance of the project stretch. However, DPHPL plans to enter into fixed price and fixed time O&M contract with the sponsor prior to the achievement of COD, thereby mitigating the O&M risk to an extent. Furthermore, the project stretch is to be constructed on a rigid pavement basis which is prone to less wear and tear resulting in lower O&M cost.

Liquidity Analysis: Adequate

DPHPL's liquidity is underpinned from the fact that it has access to timely need-based support from DBL. Furthermore, DBL has extended undertaking to fund any cost overrun, funding of shortfall in the debt servicing of DPHPL in case of delayed payment or non-payment or shortfall in annuity payments for any reason whatsoever. Also, as per the terms of sanction of the project debt, DPHPL shall create and maintain DSRA equivalent to the ensuing six months principal and six months interest obligations after meeting the debt service obligations during the operational phase which provides cushion for the debt servicing.

Analytical approach

Standalone while factoring execution track record of EPC contractor i.e. DBL 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
Factor Linkages Parent Sub JV Group
Financial Ratios – Non financial Sector
Liquidity Analysis of Non-financial sector entities
Rating Outlook and Credit Watch
Hybrid Annuity Model based road projects
Policy on Withdrawal of Ratings

About the company

DPHPL is a special purpose vehicle (SPV) incorporated by DBL to undertake four laning of Puducherry – Poondiyankuppam Section of NH – 45A (New NH – 32) from ch.km 29+000 to ch.km 67+000 (design chainage) under Bharatmala Pariyojana Phase I (Residual NHDP-IV works) on HAM in the State of Tamil Nadu and Union Territory of Puducherry. DPHPL has entered into 17-year concession agreement (CA) (including construction period of 730 days from appointed date) with NHAI.
The bid project cost for the project is Rs.1,228.00 crore as against NHAI project cost of Rs.1,045.47 crore. However, the financial closure is achieved at project cost of Rs.1,088.61 crore to be funded through construction grant from NHAI of Rs.491.20 crore, debt of Rs.477.69 crore and balance through promoter's contribution. The project has received appointed date as November 15, 2021.

Brief Financials (₹ crore)	March 31, 2021 (A)	March 31, 2022 (A)	H1FY2023 (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

A: Audited; UA: Unaudited; NA: Not Applicable as it 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
Fund-based-Long Term	-	-	-	30-11-2036	477.69	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	Fund-based-Long Term	LT	477.69	CARE A-; Stable	-	1)CARE A-; Stable (23-Dec-21)	-	-

*Long term

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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