

India Ratings Downgrades SP Jammu Udhampur's NCDs Rating to IND AA+/Negative; Off RWN

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India Ratings and Research (Ind-Ra) has downgraded the rating on SP Jammu Udhampur Highway Limited's (SP JUHI) non-convertible debentures (NCD) to 'IND AA+' from 'IND AAA' while resolving the Rating Watch Negative (RWN). The Outlook is Stable. The detailed rating action is as follows:

Instrument	Date of Issuance	Coupon Rate (%)	Maturity Date	Size of Issue (million)	Rating/Outlook	Rating Action
NCDs*	-	-	-	INR26,100 (outstanding INR20,770)	IND AA+/Negative	Downgraded; Off RWN

* Details in annexure

The downgrade reflects the weakening of the sponsor profile and longer-than-expected creation of additional reserve for additional tax liability in full. The company committed to create an additional tax reserve of INR 150 million by end-December 2020. However, the company has created only INR 100 million and the balance is likely to slip beyond December 2020. The delay was attributed to the longer-than-envisaged closure of its divestment. The delay in liquidity creation and the quantum shortfall highlight the underlying liquidity issues in the sponsor group.

The Negative Outlook reflects the continued uncertainty on the sponsor-related risks and its possible impact on the timely completion of the major maintenance. The management has committed to complete the major maintenance activity in or before July 2021. Furthermore, sponsor undertakings are pivotal for the rating and the agency has relied on the sponsor's strength and timely support to meet any shortfall in the project in line with the sponsor undertakings. The sponsor group has applied for a restructuring its debt obligations under the Reserve Bank of India's framework for COVID-19-related cash flow disruptions to ease the liquidity stress. Given the sponsor's credit quality issues are yet to be fully resolved, including the outcome of the restructuring plan by SPCPL, any aspect that exacerbates the project risks will be a rating sensitivity.

Ind-Ra had placed the rating on RWN in September 2020, due to the potential erosion of SP JUHI's debt service coverages over FY21-FY26 due to the continued increased tax post the transition to Indian Accounting Standards (Ind AS 116), delays in undertaking the major maintenance activity and the deteriorating sponsor credit profile. The resolution of the RWN reflects Ind-Ra's receipt of clarity on these aspects. The management has provided the agency with a tax certificate certifying the overall increased tax liability of INR660 million over FY21-FY26. Furthermore, the company has finalised a trustee monitored mechanism to retain the surplus cash until such additional tax liability is funded. The mechanism has been acknowledged by the trustee. The company has started the major maintenance works on the project with nearly 14km of overlaying completed on the left hand side of the road as on November 2020. The annuity payment due on 1 December 2020 has been received in full and in a timely manner.

The rating draws strength from the project's steady project cash inflows, satisfactory performance in FY20 supported by the timely receipt of semi-annual annuities from the National Highways Authority of India (NHAI; IND AAA/Stable), the timely redemption of NCDs and the adequate maintenance of reserves (debt service, major maintenance and major replacement reserve) as stipulated in the financing documents.

KEY RATING DRIVERS

Coverage Ratios Trimmed by Higher Taxes: Under IND-AS 116, annuity projects are considered as service concession agreements. This has increased SP JUHI's tax liability and thereby can impact its coverages. Its tax outgo has increased by INR221 million over the past two years and is likely to be INR660 million higher than the earlier base case plan over FY21-FY26, according to the management. The company has proposed to fund the excess liability through surplus funds in reserves available with the company, sponsor funding and cash trap mechanism. Ind-Ra is in the receipt of the trustee monitored mechanism for trapping surplus cash until the additional liability is being funded. The failure to adhere to the mechanism proposed to build up liquidity could lead to an adverse rating action. On 9 December 2020, the company had an additional INR504 million retained from the past surpluses and infused by the sponsor, which is adequate to cover the next four years of additional tax liability.

Annuity Income from Strong Counterparty: The key credit strength of SP JUHI is demonstrated by the timely receipt of 13 annuities without any major deductions from a highly rated counterparty (NHAI). SP JUHI is eligible to receive fixed and pre-agreed semi-annual annuities (INR2,019 million each), according to the concession agreement.

Final Completion Certificate Issued: The company received the final completion certificate on 7 August 2019 (with effect from 31 May 2018). The project achieved provisional completion effective June 2014. However, due to the acquisition issue of the balance land, the company was unable to complete the punch-list items. Subsequently, the balance portion of the project was descope, resulting in savings of INR11.4 million. In line with the provisions of the concession agreement, the company deposited 80% of the savings with the NHAI. The savings were borne by the sponsor since they were part of the estimated construction cost.

O&M Contractor's Strong Track Record: Maintaining the project according to the requirements of the concession agreement could pose a challenge owing to the topography of the location. Project maintenance is the key for continued and timely receipt of semi-annual annuities from the NHAI.

The operating performance-related risks are mitigated by the fact that SP JUHI has entered into a fixed-rate operations and maintenance (O&M) contract and periodic maintenance contract with SP Cement (Gujarat) Private Limited Company (SP Cement) – a Shapoorji Pallonji group company. The contract has pass-through provisions for non-performance/under performance of any conditions delineated in the concession agreement. The project's O&M costs are significantly higher than those of its peers on account of the tough terrain of its location.

Timely Major Maintenance Critical for Future Annuities: According to the concession agreement, the company needs to undertake major maintenance when the roughness indicator value reaches 2,500mm/km. Based on the test conducted by the company in December 2019, around 32% of the overall project length exceeded the stipulated roughness indicator. The company intended to start the major maintenance activity in March 2020; however, due to the COVID-19-led disruptions, the activity was delayed and only could be started in October 2020. At end-November 2020, the company had nearly completed 14km of overlaying (one way) while expending around INR150 million. Furthermore, an additional INR100 million of mobilisation advance has been provided to the contractor. The company has entered into a fixed-price contract with SP Cement for undertaking the major maintenance work for INR1,076 million, in line with the base case plan and adequate according to the lender's independent engineer's report. The company has maintained a major maintenance reserve as stipulated in the financing agreements.

Sponsor Support Undertakings: The company is sponsored by Shapoorji Pallonji Roads Pvt. Ltd. (74%) and SPCPL (26%). SPCPL is the flagship company of Shapoorji Pallonji group with presence across various segments such as engineering and construction, infrastructure development for roads, solar, ports, etc. The rating is supported by the undertakings from the sponsors for meeting any shortfall in annuity for the deductions made by the NHAI due to lane non-availability according to the terms of the concession agreement, funding any damages for the non-compliance of requirements under the concession agreement, meeting O&M cost (including major maintenance) overruns, and covering any shortfall between the termination payments and the total debt outstanding. Notwithstanding the lower debt service coverage, the sponsor undertakings and its credit quality provided salutary effect on the rating. However, continued weakening of sponsor group profile will exert pressure on the promptness of support undertakings.

SPCPL is planning to deleverage its balance sheet through equity infusion, promoter funding and asset monetisation. Subsequently, SPCPL has invoked a one-time restructuring and is planning to propose to lenders for a one-year moratorium for interest payment and two years of moratorium for principal repayment. SPCPL had outstanding debt of INR109.33 billion at 1QFY21 with a repayment obligation of INR60.83 billion until March 2021. Given the importance of the undertaking to the project, any further deterioration in the credit profile of sponsor group, including SP Cement, could pose a risk to the project's rating.

Strong Structural Features: The debt structure risk is mitigated as the debt amortisation schedule is structured to suit the calculated cash flows. A debt service reserve equivalent to succeeding six months' debt service obligations has been created in the form of a bank guarantee of INR1,550 million and INR189.4 million in form of cash. This guarantee, valid until July 2021, is likely to be extended prior to its expiry. A gap of 30 days between the annuity receipt date and the NCD redemption date provides cushion against any potential administrative delays in the receipt of the annuities. The project has a tail period of six months. Furthermore, the company has formulated an additional reserve for the increased tax liability.

Liquidity Indicator - Adequate: Although the overall coverages of the company may be impacted due to increased tax liability, the company maintains adequate liquidity and plans to augment by additional sponsor infusion and restricting surplus generation until such additional liability for FY21 to FY26 is fully funded.

The overall liquidity of the company as on 9 December 2020 was INR4,556 million of which INR3,221 million is against stipulated reserves, INR830 million against balance ongoing major maintenance and the balance surplus of INR 504 million is towards additional tax liability. Of this INR4,556 million, INR1,830 million is non-fund-based and INR2,726 million is fund-based limits. The management has asserted its intention to maintain the additional INR504 million surplus available with the company. The company may use this reserve towards any additional tax liability. The company has not availed any moratorium.

Of the overall non-fund-based limit, INR1,550 million of bank guarantee is towards debt service reserve (DSRA). The DSRA bank guarantee expires on 31 July 2021. Basis the debenture trust deed, if the DSRA bank guarantee is not renewed 10 days prior to its expiry, the debenture trustee will invoke the same.

The company has a working capital limit worth INR200 million that is used for meeting O&M obligations in between the two annuity payments; it had a peak utilisation of INR123 million over the 12 months ended November 2020. Furthermore, a steady stream of annuities from the NHAI enables the company to generate adequate cash accruals for meeting its scheduled debt obligation.

RATING SENSITIVITIES

The outlook would be revised to stable, if the agency believes the major maintenance-related-risks are fully addressed with no cost escalation, at least receipt of one full annuity without any deductions, and stability in the sponsor group profile

Negative: Future developments that could, individually or collectively, lead to a negative rating action are:

- An increase in potential tax liabilities
- Any increase in O&M cost or deduction in annuity
- Further delay in completion the major maintenance activity beyond August 2021
- Any negative rating action on NHAI

- Deterioration in credit profile of the sponsor
- Any dip into the cash reserve and/or
- Any significant dip in the contingency reserve for the current major maintenance cycle

COMPANY PROFILE

SP JUHI is a special purpose vehicle promoted by Shapoorji Pallonji Roads and SPCPL for the expansion of the 64.58km of the Jammu-Udhampur section in Jammu and Kashmir to four lanes on a build, operate and transfer annuity basis. The concession period is 20 years from 17 June 2011. The provisional certificate was issued on 1 July 2014 and the commercial operation date was 1 June 2014, 14 days prior to the scheduled commercial operation date.

FINANCIAL SUMMARY

Particulars (INR million)	FY20	FY19
Revenue from operations	2,952	3,219
Other income	251	205
Total income	3,203	3,424
EBITDA	2853	2,873
Profit after tax	821	765
Source: Company, Ind Ra		

RATING HISTORY

Instrument Type	Current Rating/Outlook			Historical Rating/Outlook/Rating Watch				
	Rating Type	Rated Limits (million)	Rating	18 September 2020	16 September 2019	13 September 2019	30 July 2018	22 May 2017
NCDs	Long-term	INR26,100	IND AA+/Negative	IND AAA/RWN	IND AAA/Negative	IND AAA(SO)/Negative	IND AAA(SO)/Stable	IND AAA(SO)/Stable

ANNEXURE

S. No.	Instrument	ISIN	Date of Issuance	Coupon Rate (%)	Maturity Date	Size of Issue (million)	Rating/Outlook
1	NCD	INE923L07373	6 August 2015	7.82	30 December 2020	INR610	IND AA+/Negative
2	NCD	INE923L07381	6 August 2015	7.82	30 June 2021	INR700	IND AA+/Negative
3	NCD	INE923L07399	6 August 2015	7.82	30 December 2021	INR710	IND AA+/Negative
4	NCD	INE923L07407	6 August 2015	7.82	30 June 2022	INR760	IND AA+/Negative
5	NCD	INE923L07415	6 August 2015	7.82	30 December 2022	INR770	IND AA+/Negative
6	NCD	INE923L07167	6 August 2015	9.15	30 June 2023	INR780	IND AA+/Negative
7	NCD	INE923L07175	6 August 2015	9.15	30 December 2023	INR790	IND AA+/Negative
8	NCD	INE923L07183	6 August 2015	9.15	30 June 2024	INR850	IND AA+/Negative
9	NCD	INE923L07191	6 August 2015	9.15	30 December 2024	INR880	IND AA+/Negative
10	NCD	INE923L07209	6 August 2015	9.15	30 June 2025	INR910	IND AA+/Negative
11	NCD	INE923L07217	6 August 2015	9.15	30 December 2025	INR930	IND AA+/Negative
12	NCD	INE923L07225	6 August 2015	9.15	30 June 2026	INR1,020	IND AA+/Negative
13	NCD	INE923L07233	6 August 2015	9.15	30 December 2026	INR1,050	IND AA+/Negative
14	NCD	INE923L07241	6 August 2015	9.15	30 June 2027	INR1,100	IND AA+/Negative
15	NCD	INE923L07258	6 August 2015	9.15	30 December 2027	INR1,130	IND AA+/Negative
16	NCD	INE923L07266	6 August 2015	9.15	30 June 2028	INR1,250	IND AA+/Negative
17	NCD	INE923L07274	6 August 2015	9.15	30 December 2028	INR1,290	IND AA+/Negative
18	NCD	INE923L07282	6 August 2015	9.15	30 June 2029	INR1,340	IND AA+/Negative
19	NCD	INE923L07290	6 August 2015	9.15	30 December 2029	INR1,250	IND AA+/Negative
20	NCD	INE923L07308	6 August 2015	9.15	30 June 2030	INR1,400	IND AA+/Negative
21	NCD	INE923L07316	6 August 2015	9.15	30 December 2030	INR1,250	IND AA+/Negative
	Total					INR 20,770	

COMPLEXITY LEVEL OF INSTRUMENTS

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Applicable Criteria

[Rating Criteria for Infrastructure and Project Finance](#)

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