Ratings

CRISIL
An S&P Global Company

Rating Rationale

September 21, 2020 | Mumbai

Embassy Office Parks Reit

'CRISIL AAA/Stable' Converted from Provisional Rating to Final Rating for NCD

Rating Action

Rs.1500 Crore Non Convertible Debentures	**CRISIL AAA/Stable (Converted from Provisional Rating to Final Rating)**
Rs.4000 Crore Non Convertible Debentures	**CRISIL AAA/Stable (Reaffirmed)**

1 crore = 10 million
Refer to annexure for Details of Instruments & Bank Facilities

Detailed Rationale

CRISIL has converted the provisional rating assigned to the non-convertible debentures (NCDs) of Rs 1,500 crore of Embassy Office Parks Reit (Embassy REIT) to a final rating of **'CRISIL AAA/Stable'**, while reaffirming the rating on the NCDs of Rs 3,650 crore (outstanding as on June 30, 2020) at **'CRISIL AAA/Stable'**. CRISIL has received the final legal documents executed for the transaction. The executed documents are in line with terms of the transaction, when the provisional rating was assigned on August 26, 2020. Hence, CRISIL has converted the provisional rating to a final rating.

Embassy REIT is sponsored by BRE Mauritius Investments (part of the Blackstone group) and Embassy Property Development Pvt. Ltd (part of the Embassy group). It has 11 commercial assets (office parks and city-centric offices), 4 hotels (of which two are under construction) and a solar plant.

The ratings continue to reflect Embassy REIT's comfortable loan-to-value (LTV) ratio'driven by low debt and strong debt protection metrics, supported by a cap on incremental borrowings'and stable revenue and rent collection from the underlying assets, given the high-quality commercial assets, high occupancy, contracted rent escalations and geographical diversification. These strengths are partially offset by susceptibility to volatility in the real estate sector, resulting in fluctuations in rental rates and occupancy.

CRISIL has considered measures taken by the central and state governments to contain the spread of the Covid-19 pandemic. Subdued economic activity or extended periods of work-from-home adopted by certain corporates may lead to build up of vacancy in the near term. Furthermore, construction activity was impacted during the lockdown, which may lead to delay in project completion. CRISIL will continue to monitor events around the pandemic.

Analytical Approach

CRISIL has combined the business and financial risk profiles of Embassy REIT with its underlying special-purpose vehicles (SPVs). This is because Embassy REIT has direct control over the SPVs and will support them in case of exigencies. Additionally, there is minimal structural subordination of cash flow, wherein the SPVs have to mandatorily distribute 90% of their net distributable cash flow (following servicing of debt) to Embassy REIT, leading to highly fungible cash flow. Also, as per Real Estate Investment Trust Regulations, 2014, of Securities and Exchange Board of India (SEBI), the cap on borrowings by the real estate investment trust (REIT) has been defined at a consolidated level (equivalent to 49% of the value of Embassy REIT's assets).

Please refer Annexure - List of entities consolidated, which captures the list of entities considered and their analytical treatment of consolidation.

Key Rating Drivers & Detailed Description

Strengths:

* **Comfortable LTV ratio protects the ability to refinance:** Consolidated debt was low at Rs 5,876 crore (including redemption premium) as on June 30, 2020. Consequently, Embassy REIT has a comfortable LTV ratio of around 18% (as per external valuation dated March 31, 2020). A low LTV ratio protects investors from the risk of decline in property prices and the consequent impact on refinancing.

The old NCDs (Rs 4,000 crore) are zero coupon and have a bullet repayment (including premium on redemption) at the end of the tenure. The issuer can redeem all or part of the NCDs from the beginning of the last year of the tenure, exercisable every two months until final maturity.

The new NCDs (Rs 1,500 crore) are coupon-bearing (payable quarterly) and have a bullet repayment (at par) at the end of the tenure. The issuer can redeem the NCDs from the beginning of the thirtieth month from allotment, exercisable every three months until final maturity.

These terms provide the trust with sufficient time to arrange for funds or refinance the NCDs prior to the due date.

* **Strong debt protection metrics:** Average consolidated debt service coverage ratio (DSCR) should be comfortable at above 2.0 times throughout the tenure of the debt, including additional financing for construction and working capital requirement in the underlying SPVs. This is primarily because incremental debt to be raised, over and above NCDs of Rs 5,150 crore, will be at about Rs 2,300 crore. Consequently, the LTV and debt-to-EBITDA (earnings before interest, tax, depreciation and amortisation) ratios will remain comfortable at around 30% and 4.0 times, respectively, vis-a-vis 40% and 5.0 times, respectively, as proposed in the NCD term sheet.

* **Stable revenue of SPVs proposed to be part of REIT:** Around 90% of the revenue comes from 11 established and high-quality commercial assets and one solar park, with stable operations and track record of at least five years of rental collection. Consolidated revenue was Rs 2,340 crore for fiscal 2020. The commercial assets have robust occupancy, averaging 92% as on June 30, 2020, with a multinational occupier base, of which Fortune 500 companies account for 48%. The top 10 tenants contribute 42%, while the technology sector contributes 50% of rentals. Rentals have upside potential given the superior asset and service quality; favourable locations in prime areas of Mumbai, Pune, Bengaluru and National Capital Region; healthy demand in the respective markets; and competitive rental rates.

Weakness:
* **Susceptibility to volatility in the real estate sector:** Rental collection (key source of revenue) is susceptible to economic downturns, which constrains the tenant's business risk profile and, therefore, occupancy and rental rates. Emergence of competing facilities in the vicinity could also have the potential to cannibalise tenants or rental rates.

Liquidity Superior
Liquidity is likely to remain supported by healthy average consolidated DSCR of above 2.0 times throughout the tenure of the NCDs, including for permitted additional financing. The NCDs are non-amortising, exposing the debenture-holders to refinancing risk. However, the conditions around redemption provide the REIT with sufficient time to arrange for refinancing. Furthermore, consolidated debt at the REIT level is not expected to exceed LTV ratio of 40%, protecting investors from the risk of decline in property prices and the consequent impact on refinancing.

Outlook: Stable
CRISIL believes Embassy REIT will continue to benefit from the quality of its underlying assets over the medium term.

Rating Sensitivity factors
Downward factors:
* Depreciation in the value of the underlying assets, resulting in LTV ratio of over 40%
* Higher-than-expected incremental borrowings
* Increase in overall vacancy for already operational assets by more than 5% from the current level
* Significant delay in the completion and leasing of under construction assets
* Any non-adherence to the structural features of the transaction

About the Trust
Embassy REIT is registered as an irrevocable trust under the Indian Trust Act, 1882, and as a REIT with SEBI's Real Estate Investment Trust Regulations, 2014, as amended. Embassy REIT's portfolio assets are held through the following SPVs:

Indian Express Newspapers (Mumbai) Pvt. Ltd (IENMPL) owns and operates a commercial property, Express Towers, in Nariman Point, Mumbai. The property has been operational for over four decades and has a total leasable area of 4.7 lakh square feet (sq. ft), of which 93.5% was occupied as on June 30, 2020.

Quadron Business Park Pvt. Ltd (QBPL) owns and operates a commercial information technology (IT) park, Embassy Quadron, in Hinjewadi, Pune. The property has been operational since 2010 and has a total leasable area of 18.9 lakh sq. ft, of which 77.0% was occupied as on June 30, 2020. It also owns and operates mixed-use development, consisting of office and retail space and a hotel in North Bengaluru. The property has a total leasable area of 2.5 lakh sq. ft, of which majority is yet to be leased. The hotel, consisting of 230 rooms, is run under the Four Seasons brand.

Qubix Business Park Pvt. Ltd (QBPPL) owns and operates a commercial IT park, Embassy Qubix, in Hinjewadi. The company has a track record of seven years in lease rental collection. Of the total leasable area of 14.5 lakh sq. ft, 97.6% was leased as on June 30, 2020.

Earnest Towers Pvt. Ltd (ETPL) owns and operates 3.6 lakh sq. ft of First International Finance Centre (FIFC) in Bandra Kurla Complex, Mumbai, of which 77.8% was occupied as on June 30, 2020.

Vikhroli Corporate Park Pvt. Ltd (VCPPL) owns a commercial property, Embassy 247, in Vikhroli, Mumbai. It has been operational for eight years and has total leasable area of 11.9 lakh sq. ft, of which 91.6% was leased as on June 30, 2020.

Galaxy Square Pvt. Ltd (GSPL) owns and operates an IT park, Embassy Galaxy, in Sector 62, Noida. The company has a track record of seven years in lease rental collection, and 98.9% of the entire leasable area of 13.6 lakh sq. ft was leased as on June 30, 2020.

Oxygen Business Park Pvt. Ltd (OBPPL) owns and operates a commercial IT park, Embassy Oxygen, in Sector 144, Greater Noida. The property is part of the Oxygen Boulevard IT Special Economic Zone and has been operational for six years. The property has total leasable area of 25.2 lakh sq. ft, of which 77.7% was leased as on June 30, 2020, while around 7.0 lakh sq. ft is under development.

Manyata Promoters Pvt. Ltd (MPPL) owns and operates Embassy Manyata Business Park, Bengaluru. The commercial complex is spread over 120 acre. The company has developed around 117.5 lakh sq. ft, of which 97.4% was leased as on June 30, 2020, while around 17.0 lakh sq. ft is under development and 14.0 lakh sq. ft is proposed to be developed. The company is also developing a five-star and a three-star hotel with 266 rooms and 353 rooms, respectively, to be operated under the Hilton brand.

Embassy Energy Pvt. Ltd (EEPL) owns and operates a solar project, with installed capacity of 100 MW. The park is spread over 465 acre across multiple villages in Karnataka. It has executed power purchase agreements for over 85% of the total capacity for supplying electricity to office parks/hotels of the Embassy group in Bengaluru.

Umbel Properties Pvt. Ltd (UPPL) owns and operates the Hilton hotel at Embassy Golflinks, along Intermediate Ring Road (IRR), Bengaluru. The hotel, consisting of 247 rooms, has been operational since 2014 and had an occupancy rate of 11% for the quarter ended June 30, 2020. The hotel was temporarily closed in accordance with state government guidelines following the lockdown and subsequently reopened by mid-June 2020.

Embassy Office Parks Pvt. Ltd (EOPPL), on a standalone basis, owns an office space, Embassy Techzone, in Hinjewadi. Of the total area of 21.6 lakh sq. ft, 90.6% was leased as on June 30, 2020, while 9.0 lakh sq. ft is under development and 24.0 lakh sq. ft is proposed to be developed.

Golflinks Software Park Pvt. Ltd (GLSP) was incorporated in 2000 for developing a software technology park, Embassy Golflinks, on IRR. The company has developed around 27.4 lakh sq. ft, of which 98.6% was leased as on June 30, 2020.

As on June 30, 2020, Embassy REIT's profit after tax (PAT) was Rs 223 crore on revenue of Rs 565 crore, against Rs 261 crore and Rs 583 crore, respectively, during the corresponding period of fiscal 2019.

Key Financial Indicators*

For fiscal	Unit	2020	2019
Revenue	Rs crore	2,340	NA
PAT	Rs crore	896	NA
PAT margin	%	38.3	NA
Adjusted gearing	Times	0.25	NA
Interest coverage	Times	4.78	NA

**REIT was listed on April 1, 2019, and asset acquisition took place simultaneously. Hence, previous financials are not relevant.*

Any other information: Not applicable

Note on complexity levels of the rated instrument:
CRISIL complexity levels are assigned to various types of financial instruments and are included (where applicable) in the Annexure -- Details of Instrument in this Rating Rationale. For more details on the CRISIL complexity levels, please visit www.crisil.com/complexity-levels.

Annexure - Details of Instrument(s)

ISIN	Name of instrument	Date of allotment	Coupon rate (%)	Maturity date	Issue size (Rs crore)	Complexity level	Rating assigned with outlook
INE041007019	Non-convertible debentures	03-May-19	0%	03-Jun-22	3,000	Complex	CRISIL AAA/Stable
INE041007027	Non-convertible debentures	22-Nov-19	0%	03-Jun-22	650	Complex	CRISIL AAA/Stable
NA	Non-convertible debentures*	NA	NA	NA	350	NA	CRISIL AAA/Stable
INE041007035	Non-convertible debentures	09-Sep-20	7.25%	09-Oct-23	750	Complex	CRISIL AAA/Stable
NA	Non-convertible debentures*	NA	NA	NA	750	NA	CRISIL AAA/Stable

**Not yet placed*

Annexure - List of entities consolidated with Embassy REIT

Names of entities consolidated	Extent of consolidation	Rationale for consolidation
IENMPL	Full	100% subsidiary
QBPL	Full	100% subsidiary
QBPPL	Full	100% subsidiary
ETPL	Full	100% subsidiary
VCPPL	Full	100% subsidiary
GSPL	Full	100% subsidiary
OBPPL	Full	100% subsidiary
MPPL	Full	100% subsidiary
EEPL	Full	100% subsidiary
UPPL	Full	100% subsidiary
EOPPL	Full	100% subsidiary
GLSP	Partial	Investment entity consolidated to the extent of 50%

Annexure - Rating History for last 3 Years

		Current		2020 (History)		2019		2018		2017		Start of 2017
Instrument	**Type**	**Outstanding Amount**	**Rating**	**Date**	**Rating**	**Date**	**Rating**	**Date**	**Rating**	**Date**	**Rating**	**Rating**
Non Convertible Debentures	LT	4400.00 21-09-20	CRISIL AAA/Stable	26-08-20	CRISIL AAA/Stable| Provisional CRISIL AAA/Stable	09-05-19	CRISIL AAA/Stable	24-09-18	Provisional CRISIL AAA/Stable		--	--
				05-08-20	CRISIL AAA/Stable	22-04-19	Provisional CRISIL AAA/Stable					
				16-05-20	CRISIL AAA/Stable	06-03-19	Provisional CRISIL AAA/Stable					
						18-01-19	Provisional CRISIL AAA/Stable					

All amounts are in Rs.Cr.

Links to related criteria
CRISILs criteria for rating debt backed by lease rentals of commercial real estate properties
CRISILs rating criteria for REITs and InVITs
CRISILs Criteria for Consolidation

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