CRISIL Ratings

Rating Rationale

May 11, 2021 | Mumbai

Sobha Limited

Rating outlook revised to 'Stable'; Ratings reaffirmed

Rating Action

Total Bank Loan Facilities Rated	**Rs.3100 Crore**
Long Term Rating	**CRISIL A+/Stable (Outlook revised from 'Negative' and rating reaffirmed)**
Short Term Rating	**CRISIL A1 (Reaffirmed)**

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

Detailed Rationale

CRISIL Ratings has revised its rating outlook on the long term bank facilities of Sobha Limited (Sobha; flagship company of the Sobha group) to **'Stable'** from 'Negative' and has reaffirmed the rating at **'CRISIL A+'.** The short term rating has been reaffirmed at 'CRISIL A1'.

The outlook revision reflects the belief that Sobha will maintain its credit risk profile over the medium term backed by steady saleability and collections, and gradual reduction in debt, supporting improvement in debt protection metrics.

Sobha witnessed significant recovery in sales and collections in the second half of fiscal 2021, with the group achieving sales of 24.71 lakh square feet (sq ft) valued at Rs 1,960 crore. This reflects increase of 38% and 25% year-on-year (y-o-y), respectively, despite the overall industry witnessing a sharp contraction because of the pandemic. Strong sales momentum and upswing in construction resulted in improvement in collections in the third quarter of fiscal 2021; collections from residential real estate business rose to Rs 664 crore, against Rs 336 crore and Rs 502 crore in the first and second quarters, respectively. . The momentum is expected to have continued in the fourth quarter as well. For fiscal 2021, sales volume and value were 4.01 million sq ft and Rs 3137 crores respectively that is an increase of 1% and 13% y-o-y respectively.

The group generated surplus cash flow of Rs 104 crore for the nine months ended December 31, 2020, against negative Rs 660 crore for the corresponding period of the previous fiscal, driven by price increase, cost cutting measures and controlled outflow towards land banking and capital expenditure (capex). Gross debt is estimated at below Rs 3,000 crore as of March 31, 2021, compared with Rs 3,208 crore in December 2019. Net gearing was ~1.23 times as of December 31, 2020, as compared with 1.30 times as of December 31, 2019. The net debt level is expected to continue to reduce going forward as well supported by limited outflows towards land purchases and capital expenditure (capex); net gearing is expected to reduce to 1.1 times in the near term.

CRISIL Ratings expects saleability for the first quarter of fiscal 2022 to be moderately impacted on account of the second wave of the pandemic and resultant curfews/lockdowns by state governments. Nevertheless, demand will be deferred to the remaining quarters of the fiscal, in line with the trend observed in fiscal 2021. Planned launches for fiscal 2022 are unlikely to witness material delay. Furthermore, there have not been any restrictions on construction activity; the group has sufficient labour on site following all Covid-19 protocols.

Given the limited impact on construction, collections from ongoing projects will not be impacted significantly. Receivables stood at Rs 3,127 crore as on December 31, 2020, which covers 79% of the balance project cost to be spent for ongoing projects. Hence, the impact of the current disruptions on cash flow is likely to be limited, unlike the first quarter of the past fiscal when projects had come to a standstill. Having said that, prolonged closures may cause weak saleability, leading to an adverse impact on collections and weakening the credit risk profile of the group. Extent of the second wave, continuation of construction activity without any major disruptions and the ability to maintain operational stability will be closely monitored. The group also has term debt obligation of Rs 778 crore in fiscal 2022, which will be partly refinanced and funded through a mix of unutilised bank lines and cash flow from operations.

The ratings continue to reflect the Sobha group's healthy business risk profile, supported by strong execution capabilities and established brand position, and moderate, but improving, financial risk profile, aided by strong refinancing ability. These strengths are partially offset by high debt level stemming from debt-funded land acquisitions in the past, sizeable debt obligation over the medium term, and exposure to risks and cyclicality in the real estate industry.

Analytical Approach

CRISIL Ratings has fully combined the business and financial risk profiles of all projects in Sobha and its subsidiaries and associate companies, collectively referred to as the Sobha group, because the entities have the same business, common promoters and significant operational, managerial and financial linkages.

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

Key Rating Drivers & Detailed Description

Strengths:

- **Healthy business risk profile, supported by strong execution capabilities and established brand position:**
  The Sobha group is among the leading residential real estate players in Bengaluru. It has developed residential real estate and contractual projects of 1,113.5 lakh sq ft as on December 31, 2020. It has ongoing residential projects of 181.1 lakh sq ft (excluding completed projects, unreleased area and planned launches) and contractual projects of 79.4 lakh sq ft. Strong execution capabilities are reflected in the quality construction and timely completion of projects; the group delivered residential area of 16.3 lakh sq ft in the first nine months of fiscal 2021. The group has expanded to Kozhikode, Chennai, Cochin, Coimbatore, Gurugram, Mysuru, Pune and Thrissur. It has diversified into the contractual business, and manufactures interiors, concrete products, and glazing and metal works. These businesses contributed to 33% of the total collections for the first nine months of fiscal 2021, and the contribution should remain stable over the medium term.

- **Moderate, though improving, financial risk profile:**
  Financial risk profile is characterised by moderate operating cash inflow. Healthy sales and collections in the second half of fiscal 2021 enabled the group to slightly lower debt and improve gearing. The group has an intent to lower its net gearing levels to 1.1 times in the near term, and is continuing to focus on keeping debt levels under check.

  CRISIL Ratings expects the group to generate operating cash inflows (including contracts business) of over Rs 2,500 crore per annum in the three fiscals through March 2024. Furthermore, while annual debt obligation is sizeable, financial flexibility is supplemented by the group's demonstrated refinancing ability, access to unutilised bank limit of Rs 1,289 crore, unsold inventory of Rs 5,566 crore (excluding area not released for sale) and 2,120 lakh sq ft of developable area across major micro markets in the country as on December 31, 2020. The group can also utilise part of its non-fund based limits (up to Rs 200 crore) for payments to suppliers, limiting the pressure on fund-based bank lines. CRISIL Ratings does not expect additional land purchases by the Sobha group under current market conditions, obviating the need to add debt over the medium term.

Weakness:

- **High debt because of historical debt-funded land acquisitions:**
  The group had undertaken debt-funded land purchases historically, with a large portion of debt being used for purchase of land. Though collections have grown in recent years, debt had been increasing till fiscal 2020 owing to continued land acquisitions and ongoing construction. Nevertheless, land acquisition spend significantly fell in fiscal 2021 given subdued market sentiment on account of the pandemic. Consequently, gross debt and net gearing decreased to Rs 3,134 crore and 1.23 times as on December 31, 2020, from Rs 3,208 crore and 1.30 times, respectively, as on December 31, 2019. The group is expected to focus on reducing debt and maintain net gearing at 1-1.1 times over the medium term. Material increase in debt, resulting in net gearing exceeding 1.5 times, will be a key monitorable. Purchase of large land parcels, if any, is likely to be undertaken through the special purpose vehicle in joint venture with private equity partners.

- **Exposure to risks and cyclicality inherent in the real estate sector:**
  Cyclicality in the real estate sector may result in volatility in cash inflow and sales. In contrast, cash outflow, such as for debt servicing, is fixed. Any decline in demand may adversely impact sales and collections, disrupting the debt improvement trajectory. Sobha generates over two-thirds of its revenue from Bengaluru, and a sizeable chunk of its customers are from information technology/banking and financial services sectors, where salaries are stable and hence unlikely to affect collections of ongoing projects.

Liquidity: Adequate

Liquidity will remain supported by adequate saleability and collections in ongoing projects and expectation of sustenance with new launches, though there may be temporary disruptions owing to the second wave of Covid-19. The company has unsold inventory of Rs 5,566 crore in ongoing and completed projects (excluding area not released for sale) along with almost fully paid-up land bank, with development potential of 2,120 lakh sq ft, against which additional debt can be raised, if required.

Term debt obligation is expected at Rs 778-1,056 crore over the three fiscals through March 2024. The group has strong relationships with the lending community, and is likely to refinance part of the obligation in advance besides servicing it through cash flows and unutilised bank lines. Undrawn bank limit stood at Rs 1,289 crore and cash and equivalent at Rs 159 crore as on December 31, 2020. Besides, the Rs 200 crore non-fund based lines can also be used as supplier credit, adding to liquidity. In the first half of fiscal 2021, the group had availed the moratorium on bank loan payments as per Reserve Bank of India's Covid-19 Regulatory Package. Going forward, refinancing of term debt obligation with longer maturity loans can help obviate need for material refinancing during cyclical downturns.

Outlook: Stable

CRISIL Ratings believes the Sobha group will continue to benefit from its strong position in Bengaluru's real estate market, sound operating capabilities and sizeable projects under implementation. The financial risk profile will remain moderate over the medium term, supported by reduction of debt.

Rating Sensitivity factors

Upward Factors:

- Higher-than-expected sales in the ongoing and upcoming residential projects, leading to substantial improvement in operating cash flow
- Sharp reduction in debt level, including through equity infusions, leading to net gearing of below 1.0 time

Downward Factors:

- Sharp decline in operating cash flow, triggered by slackened saleability of existing and proposed projects or delays in project execution
- Weakening of financial risk profile, due to weak performance or large land purchases and capex, leading to substantial increase in borrowings, and resultant increase in net gearing to over 1.5 times

About the Company
Sobha was founded by Mr PNC Menon in August 1995. The Bengaluru-based group has been engaged in the construction and development of real estate for the past 23 years. As on December 31, 2020, it had developed 1,113.5 lakh sq ft, of which around 75% is in Bengaluru. The group also has presence in Thrissur, Chennai, Pune, Gurugram, Coimbatore, Calicut, Mysuru and Cochin. The promoter held 51.99% stake in Sobha as on March 31, 2021.

The company's net profit was Rs 44.4 crore on net revenue of Rs 1,556 crore in the nine months ended December 31, 2020, compared with Rs 230.8 crore on Rs 2,844 crore, respectively, during the corresponding period of the previous fiscal. Revenue and profit were impacted by lower sales in the first quarter of fiscal 2021.

Key Financial Indicators (Consolidated)

Particulars	Unit	2020	2019
Revenue	Rs.Crore	3,787	3,478
Profit After Tax (PAT)	Rs.Crore	282	297
PAT Margin	%	7.4	8.5
Adjusted gearing	Times	1.29	1.17
Interest coverage	Times	1.74	2.81

Any other information: Not applicable

Note on complexity levels of the rated instrument:
CRISIL complexity levels are assigned to various types of financial instruments. The CRISIL complexity levels are available on www.crisil.com/complexity-levels. Users are advised to refer to the CRISIL complexity levels for instruments that they consider for investment. Users may also call the Customer Service Helpdesk with queries on specific instruments.

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
NA	Term loan	NA	NA	Apr-24	681.9	NA	CRISIL A+/Stable
NA	Term loan	NA	NA	Feb-33	239.3	NA	CRISIL A+/Stable
NA	Term loan	NA	NA	Sep-24	120.0	NA	CRISIL A+/Stable
NA	Term loan	NA	NA	Sep-23	120.0	NA	CRISIL A+/Stable
NA	Term loan	NA	NA	Jun-24	110.0	NA	CRISIL A+/Stable
NA	Term loan	NA	NA	Jan-24	89.2	NA	CRISIL A+/Stable
NA	Term loan	NA	NA	Feb-23	79.1	NA	CRISIL A+/Stable
NA	Term loan	NA	NA	Apr-23	45.0	NA	CRISIL A+/Stable
NA	Term loan	NA	NA	Dec-21	18.9	NA	CRISIL A+/Stable
NA	Term loan	NA	NA	Nov-23	13.0	NA	CRISIL A+/Stable
NA	Cash credit	NA	NA	On demand	890.0	NA	CRISIL A+/Stable
NA	Bank guarantee	NA	NA	NA	693.6	NA	CRISIL A1

Annexure - List of Entities Consolidated*

Names of Entities Consolidated	Extent of Consolidation	Rationale for Consolidation
Sobha City [partnership firm]	Full	Subsidiary/associate
Sobha Contracting Pvt Ltd	Full	Subsidiary/associate
Sobha Developers (Pune) Ltd	Full	Subsidiary/associate
Sobha Assets Pvt Ltd	Full	Subsidiary/associate
Sobha Highrise Ventures Pvt Ltd	Full	Subsidiary/associate
Sobha Interiors Pvt Ltd	Full	Subsidiary/associate
Sobha Nandambakkam Developers Ltd	Full	Subsidiary/associate
Sobha Tambaram Developers Ltd	Full	Subsidiary/associate
Sobha Construction Products Pvt Ltd	Full	Subsidiary/associate
Kilai Builders Pvt Ltd	Full	Subsidiary/associate
Kondhwa Projects LLP [partnership firm]	Full	Subsidiary/associate
Kuthavakkam Builders Pvt Ltd	Full	Subsidiary/associate
Kuthavakkam Realtors Pvt Ltd	Full	Subsidiary/associate
Vayaloor Properties Pvt Ltd	Full	Subsidiary/associate
Vayaloor Builders Pvt Ltd	Full	Subsidiary/associate
Vayaloor Developers Pvt Ltd	Full	Subsidiary/associate
Vayaloor Real Estate Pvt Ltd	Full	Subsidiary/associate
Vayaloor Realtors Pvt Ltd	Full	Subsidiary/associate
Valasai Vettikadu Realtors Pvt Ltd	Full	Subsidiary/associate
**Details as on March 31, 2020*		

Annexure - Rating History for last 3 Years

	Current			2021 (History)		2020		2019		2018		Start of 2018
Instrument	Type	Outstanding Amount	Rating	Date	Rating	Date	Rating	Date	Rating	Date	Rating	Rating
Fund Based Facilities	LT	2406.4	CRISIL A+/Stable		--	31-03-20	CRISIL A+/Negative		--	31-12-18	CRISIL A+/Stable / CRISIL A1	CRISIL A+/Stable
Non-Fund Based Facilities	ST	693.6	CRISIL A1		--	31-03-20	CRISIL A1		--	31-12-18	CRISIL A1	CRISIL A1

All amounts are in Rs.Cr.

Annexure - Details of various bank facilities

Current facilities			Previous facilities		
Facility	Amount (Rs.Crore)	Rating	Facility	Amount (Rs.Crore)	Rating
Bank Guarantee	693.6	CRISIL A1	Bank Guarantee	172.5	CRISIL A1
Cash Credit	890	CRISIL A+/Stable	Cash Credit	853.2	CRISIL A+/Negative
Term Loan	1516.4	CRISIL A+/Stable	Term Loan	2074.3	CRISIL A+/Negative
Total	3100	-	Total	3100	-

Criteria Details

Links to related criteria
CRISILs Bank Loan Ratings - process, scale and default recognition
CRISILs Rating criteria for Real Estate Developers
CRISILs Criteria for Consolidation

Media Relations	Analytical Contacts	Customer Service Helpdesk
Saman Khan Media Relations **CRISIL Limited** D: +91 22 3342 3895 B: +91 22 3342 3000 saman.khan@crisil.com **Naireen Ahmed** Media Relations **CRISIL Limited** D: +91 22 3342 1818 B: +91 22 3342 3000 naireen.ahmed@crisil.com	Anuj Sethi Senior Director **CRISIL Ratings Limited** B:+91 44 6656 3100 anuj.sethi@crisil.com Anand Kulkarni Director **CRISIL Ratings Limited** B:+91 22 3342 3000 Anand.Kulkarni@crisil.com Parth Luthra Senior Rating Analyst **CRISIL Ratings Limited** B:+91 22 3342 3000 Parth.Luthra@crisil.com	Timings: 10.00 am to 7.00 pm Toll free Number:1800 267 1301 For a copy of Rationales / Rating Reports: CRISILratingdesk@crisil.com For Analytical queries: ratingsinvestordesk@crisil.com

Note for Media:
This rating rationale is transmitted to you for the sole purpose of dissemination through your newspaper / magazine / agency. The rating rationale may be used by you in full or in part without changing the meaning or context thereof but with due credit to CRISIL Ratings. However, CRISIL Ratings alone has the sole right of distribution (whether directly or indirectly) of its rationales for consideration or otherwise through any media including websites, portals etc.

About CRISIL Ratings Limited

CRISIL Ratings pioneered the concept of credit rating in India in 1987. With a tradition of independence, analytical rigour and innovation, we set the standards in the credit rating business. We rate the entire range of debt instruments, such as, bank loans, certificates of deposit, commercial paper, non-convertible / convertible / partially convertible bonds and debentures, perpetual bonds, bank hybrid capital instruments, asset-backed and mortgage-backed securities, partial guarantees and other structured debt instruments. We have rated over 33,000 large and mid-scale corporates and financial institutions. We have also instituted several innovations in India in the rating business, including rating municipal bonds, partially guaranteed instruments and infrastructure investment trusts (InvITs).

CRISIL Ratings Limited ("CRISIL Ratings") is a wholly-owned subsidiary of CRISIL Limited ("CRISIL"). CRISIL Ratings Limited is registered in India as a credit rating agency with the Securities and Exchange Board of India ("SEBI").

For more information, visit www.crisil.com/ratings

About CRISIL Limited

CRISIL is a global analytical company providing ratings, research, and risk and policy advisory services. We are India's leading ratings agency. We are also the foremost provider of high-end research to the world's largest banks and leading corporations.

CRISIL is majority owned by S&P Global Inc., a leading provider of transparent and independent ratings, benchmarks, analytics and data to the capital and commodity markets worldwide

For more information, visit www.crisil.com

Connect with us: TWITTER | LINKEDIN | YOUTUBE | FACEBOOK

CRISIL Ratings uses the prefix 'PP-MLD' for the ratings of principal-protected market-linked debentures (PPMLD) with effect from November 1, 2011 to comply with the SEBI circular, "Guidelines for Issue and Listing of Structured Products/Market Linked Debentures". The revision in rating symbols for PPMLDs should not be construed as a change in the rating of the subject instrument. For details on CRISIL Ratiings' use of 'PP-MLD' please refer to the notes to Rating scale for Debt Instruments and Structured Finance Instruments at the following link: www.crisil.com/ratings/credit-rating-scale.html