

June 11, 2021

Sobha Limited: Ratings reaffirmed; outlook revised to Stable from Negative; rating withdrawn for Rs. 270.0 crore proposed NCD programme

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Fund-based - Term Loan	2485.50	2569.30	[ICRA]A+ reaffirmed; outlook revised to Stable from Negative
Fund-based – Working Capital	970.00	910.00	
Non-fund Based Facilities	717.40	693.60	
Non-convertible Debentures	270.00	0.00	[ICRA]A+ reaffirmed; outlook revised to Stable from Negative; rating withdrawn
Total	4442.90	4172.90	

*Instrument details are provided in Annexure-1

Rationale

The revision in outlook takes into account significant improvement in the net operational cashflows of Sobha in FY2021, which along with curtailment of investments in land have supported reduction in debt levels. Net debt has reduced to Rs. 2852 crore as of March 31, 2021 (estimated) from Rs 3,023 crore as on March 31, 2020. With strong sales performance in the second half of FY2021, improving collections and healthy saleability in ongoing projects, the outlook on the net operational cash flows for FY2022 is favourable, which is expected to support further reduction in debt over FY2022.

The rating reaffirmation continues to take into account Sobha's established position in the Bengaluru real estate market and its strong in-house project execution capabilities in the real estate and contracting sectors. The company has witnessed steady sales volume over the last three years. The company reported sales volume of 4.01 million sqft in FY2021, as compared to 4.07 million sqft sold in FY2020, despite the adverse impact of Covid-19 pandemic in Q1FY2021. Sobha witnessed good recovery in sales from Q2FY2021 onwards, posting all-time high sales during Q4FY2021. The receivables from the sold area in the completed and ongoing projects cover 45% of the pending cost and the debt outstanding as on December 31, 2020. The rating draws comfort from the contracting segment's adequate order-book position and Sobha's ability to win repeat orders from its existing clientele, providing medium-term cash flow visibility. Further, in-house manufacturing division of Sobha, including glazing and metal works, Interiors, and concrete products, augments the real-estate and contracts works operations through benefits arising out of backward integration.

The rating continues to be constrained by the moderately high leverage level (as measured by net debt/FFO), which is estimated to be at around 4.5 times as of March 31, 2021. The debt levels have historically been high compared to the ongoing project portfolio of the company due to the investment in land bank made earlier. However, with substantial project launches planned in the coming quarters, healthy project saleability, and company's intent towards restricting any significant investment outflows in the near-to-medium, net debt levels are expected to reduce in the coming years, backed by improved operational cashflows. The rating is also restricted by the geographical concentration risk as most of the company's projects are located in Bengaluru city. Any slowdown in sales in the Bengaluru market could adversely impact the company's sales and collections. Further, the company remains exposed to external factors such as the inherent cyclicity in the real estate industry and regulatory risks. Any adverse impact of the current lockdown restriction imposed amidst the prevalent pandemic levels, would remain a key monitorable.

The Stable outlook on the [ICRA]A+ rating reflects ICRA's opinion that the credit profile of Sobha will remain supported by the company's established brand recall in the real estate market and healthy saleability across majority of its projects. Further, no substantial land bank investment or any capital expenditure in the medium term, as guided by the company, would help keep

debt levels in check. Despite the Covid-19 pandemic, large real estate developers such as Sobha have benefited from the consolidation of market share among the top developers. This longer-term trend is expected to offset the immediate challenges posed by the second wave of the pandemic on the business operations.

The ratings for the Rs. 270.0 crore proposed NCD programme has been withdrawn at the request of the company, in accordance with ICRA's policy on withdrawal and suspension of credit rating.

Key rating drivers and their description

Credit strengths

Established brand and market position - Sobha has a track record of over 26 years in the Bangalore real estate market. The company has strong in-house project execution capabilities demonstrated through completion of real estate projects with total development measuring 58.75 million sqft, and contractual projects, measuring 52.60 million sqft, as of December 31, 2020.

Steady pre-sales in FY2020 and FY2021; good recovery witnessed following adverse impact of Covid pandemic in Q1FY2021 - Sobha has witnessed steady sales volume over the last three years. The company reported sales volume of 4.01 million sqft in FY2021, as compared to 4.07 million sqft sold in FY2020, despite the adverse impact of Covid-19 pandemic in Q1FY2021. Sobha witnessed good recovery in sales from Q2FY2021 onwards, posting all-time high sales during Q4FY2021. The company continues to maintain low completed inventory stock, which coupled with healthy pre-sales in majority of the projects, demonstrates healthy saleability. As of December 31, 2020, cover of cash inflows from sold area over balance project cost and net debt outstanding, stands comfortable at 45%. This is supported by strong sales bookings of 59% of the launched area as on December 31, 2020.

Adequate contractual order book provides steady cash flow; repeat orders from existing clientele provides comfort - During 9MFY2021, inflows from the contractual and manufacturing business reduced by about 36% on a Y-o-Y basis, impacted largely by the disruption caused by the pandemic. For the full year of FY2021, inflows from the segment are expected to recover to levels of 65-70% of that witnessed during FY2020. Nevertheless, margins from the segment are expected to remain stable, leading to steady net cashflows. As of December 31, 2020, the company reported orders in-hand worth Rs. 2,126 crore, which is 1.4 times of the FY2020 revenues from the segment, lending adequate revenue visibility for the medium term.

Credit challenges

Moderate leverage levels; however, expected to reduce in the medium term - During FY2021, Sobha's net operational cashflows have improved significantly vis-à-vis FY2020. This coupled with reduced investment outflows have resulted in reduction in debt levels during the year to Rs. 2852 crore as of March 31, 2021 (estimated) from Rs. 3023 crore as of March 31, 2020. Leverage levels (as measured by net debt/FFO) is estimated at around 4.5 times as of March 31, 2021. The debt levels have historically been high compared to the ongoing project portfolio of the company due to the investment in land bank made earlier. High scheduled debt repayment obligations expose Sobha to refinancing risks. However, with substantial project launches planned in the coming quarters, healthy project saleability, and company's intent towards restricting any significant investment outflows in the near-to-medium, net debt levels are expected to reduce in the coming years, backed by improved operational cashflows.

Geographical and project concentration risks - The company has high geographical concentration as around 67% of the sales by volume came from the Bengaluru real estate market in FY2021. Any slowdown in sales in Bengaluru market could adversely impact the company's sales and collections. However, presence of significant inventory in projects across cities like Cochin, Gurgaon and Pune along with future plans of 14.4 million sqft of residential launches and 0.32 million sqft of commercial launches (as of December 31, 2020) in the coming quarters across geographies such as Hyderabad, Delhi, Hosur and Trivandrum, the risk is mitigated to an extent.

Sensitive to external market factors – Currently, the lockdown restrictions amidst the prevalent pandemic levels are expected to impact site visits affecting demand levels to some extent. However, the impact is expected to be less severe as compared to similar situation last year. Further, the company remains exposed to other external factors such as the inherent cyclicality in the real estate industry and regulatory risks, which could have an impact on the cash inflows of the company.

Liquidity position: Adequate

Sobha's liquidity is adequate. The company has witnessed significant improvement in terms of cashflow from operations during FY2021 vis-à-vis FY2020. Operational cashflows are expected to steadily improve in the coming quarters and would comfortably meet the finance costs and investing cash outflows of the company in FY2022-FY2023. The company remains reliant on refinancing or drawdown of new project loans to some extent, as substantial scheduled debt repayments of around Rs. 752 crore and Rs. 831 crore fall due in FY2022 and FY2023 respectively. Undrawn debt limits of Rs. 1289 crore and liquid investments and bank balances of Rs. 159 crore, as on December 31, 2020, provides further support to the liquidity profile.

Rating sensitivities

Positive factors – Improvement in net operational cash flows from the real estate and contracting division resulting in meaningful reduction in debt levels. Specific credit metrics that could lead to an upgrade include net debt/FFO remaining below 3.0 times on a sustained basis.

Negative factors – The ratings could be downgraded in case if lower-than-expected pre-sales and collections enhances the refinancing requirement for the maturing debt obligations or higher than anticipated land investments result in further increase in debt levels.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for Real Estate Entities Rating Methodology for Construction Entities
Parent/Group Support	Not Applicable
Consolidation/Standalone	ICRA has taken a consolidated view of Sobha Limited and its seven subsidiaries, based on the strong operational and financial linkages between the group entities and their common management group.

About the company

Incorporated in August 1995, as a private limited company, and subsequently converted into a public limited company in June 2006, Sobha Limited is an established player in real estate development and contract construction in Bengaluru. Sobha is promoted by its chairman emeritus Mr. P. N. C. Menon, who started his India operations after successfully running interior decoration firms in Muscat. Along with his family members, he holds around 51.99% of equity shares in the company. As on December 31, 2020, Sobha executed real estate projects with an overall development of 58.75 million sqft of built-up area, with a major presence in Bengaluru. It has also diversified to other cities such as Gurgaon, Chennai, Pune, Thrissur, Coimbatore, Kochi, Calicut, Mysore and Gujarat. In the contracting segment, Sobha has completed projects in several states in India, covering a total built-up area of 52.60 million sqft.

Key financial indicators (audited)

Standalone	FY2019	FY2020
Operating Income (Rs. crore)	3442.1	3753.8
PAT (Rs. crore)	297.0	281.4
OPBDIT/OI (%)	19.6%	29.7%
PAT/OI (%)	8.6%	7.5%
Total Outside Liabilities/Tangible Net Worth (times)	3.8	3.5
Total Debt/OPBDIT (times)	3.9	2.8
Interest Coverage (times)	2.9	1.6

PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation; n.m.: not meaningful

Source: Company, ICRA research

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2022)				Chronology of Rating History for the past 3 years			
		Type	Amount Rated (Rs. crore)	Amount Outstanding as of Dec 31, 2020 (Rs. crore)	Date & Rating in	Date & Rating in FY2021	Date & Rating in FY2020		Date & Rating in FY2019
							11-Jun-2021	14-Sep-2020	
1	Long-term Term Loan	Long Term	2569.30	3134.00	[ICRA]A+ (Stable)	[ICRA]A+ (Negative)	[ICRA]A+ (Negative)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)
2	Long-term Fund Based	Long Term	910.00		[ICRA]A+ (Stable)	[ICRA]A+ (Negative)	[ICRA]A+ (Negative)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)
3	Long-term Non-fund Based	Long Term	693.60	NA	[ICRA]A+ (Stable)	[ICRA]A+ (Negative)	[ICRA]A+ (Negative)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)
4	Proposed Non-convertible Debentures	Long Term	270.00	-	[ICRA]A+ (Stable); withdrawn	[ICRA]A+ (Negative)	[ICRA]A+ (Negative)	-	-

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long-term Term Loan	Simple
Long-term Fund Based	Simple
Long-term Non-fund Based	Very Simple
Proposed Non-convertible Debentures	Very Simple

The Complexity Indicator refers to the ease with which the returns associated with the rated instrument could be estimated. It does not indicate the risk related to the timely payments on the instrument, which is rather indicated by the instrument's credit rating. It also does not indicate the complexity associated with analyzing an entity's financial, business, industry risks or complexity related to the structural, transactional, or legal aspects. Details on the complexity levels of the instruments, is available on ICRA's website: www.icra.in

Annexure-1: Instrument details

ISIN No	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. Crore)	Current Rating and Outlook
NA	Term loans	FY2014-FY2021	-	FY2022-FY2034	2569.30	[ICRA]A+ (Stable)
NA	Fund Based - Working capital	-	-	-	910.00	[ICRA]A+ (Stable)
NA	Non-fund based - Working capital	-	-	-	693.60	[ICRA]A+ (Stable)
NA	Proposed NCD	-	-	-	270.00	[ICRA]A+(Stable); withdrawn

Source: Company

Annexure-2: List of entities considered for consolidated analysis

Company Name	Ownership	Consolidation Approach
Sobha City ['Partnership firm']	100.00%	Full Consolidation
Sobha Construction Products Pvt Ltd	100.00%	Full Consolidation
Sobha Developers (Pune) Limited	100.00%	Full Consolidation
Sobha Assets Private Limited	100.00%	Full Consolidation
Sobha Highrise Ventures Private Limited	100.00%	Full Consolidation
Sobha Nandambakkam Developers Limited	100.00%	Full Consolidation
Sobha Tambaram Developers Limited	100.00%	Full Consolidation
Kondhwa Projects LLP	50.00%	Equity method

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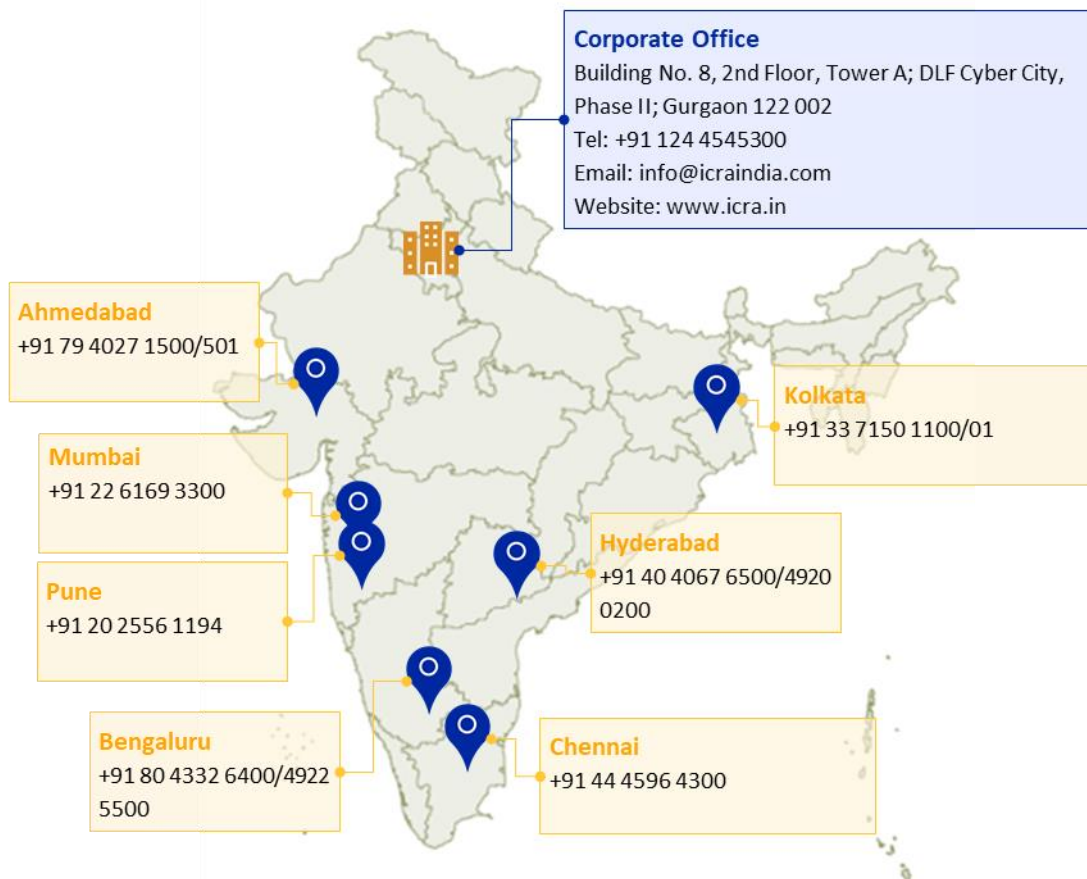


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