

May 24, 2021

CtrlS Datacenters Limited: Ratings upgraded to [ICRA]AA- (Stable) / [ICRA]A1+

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Fund-based Term Loan	456.11	553.57	[ICRA]AA- (Stable); upgraded from [ICRA]A+ (Stable)
Fund-based Working Capital Facilities	25.00	25.00	[ICRA]AA- (Stable); upgraded from [ICRA]A+ (Stable)
Non-fund based Limits	20.00	20.00	[ICRA]AA- (Stable); upgraded from [ICRA]A+ (Stable)
Unallocated Limits	148.89	51.43	[ICRA]AA- (Stable)/[ICRA]A1+; upgraded from [ICRA]A+ (Stable)/[ICRA]A1
Total	650.00	650.00	

*Instrument details are provided in Annexure-1

Rationale

The upgrade in ratings of CtrlS Datacenters Limited (CtrlS/ the company) factors the robust growth in its operating income (OI) - CAGR of ~34% over the last five years to Rs. 760-770 crore (estimated) in FY2021 - on the back of new long-term leases along with rack addition, increase in lease rates and better utilisation of its Mumbai and Hyderabad data centers (DC). The improvement in capacity utilisation led to better absorption of fixed costs. This along with the focus on large accounts with high gross margins, and upward price revision of contracts that were due for renewal in FY2020 has improved CtrlS' operating profitability to 57.1% in FY2020 and 55.0%-58.0% in FY2021 (estimates) from 40.9% in FY2019. Consequently, RoCE improved to 33.0% in FY2020 and 30.0%-33.0% in FY2021 (estimates) from 17.4% in FY2019. The ratings take into account the company's strong financial profile, characterised by comfortable capital structure with TD/TNW¹ of 0.8 times, and healthy debt coverage indicators with TD/OPBIDTA of 1.2 times, debt service coverage of 2.6 times and interest coverage of 9.2 times estimated as on March 31, 2021. Further, the company enjoys high financial flexibility, given that the current borrowings are against one-third of the rental inflows, thereby leaving two-thirds of unencumbered inflows at CtrlS's disposal. For the term debt, the company maintains an escrow account, with liquidity buffer of one month of debt obligation in the form of debt service reserve account (DSRA).

The ratings continue to factor in the company's reputed and diversified customer base across different verticals and the tier-IV nature of the data centers, with 99.995% uptime, which enables the company to command premium pricing than DCs with lower tier structures. The large investments made by customers and the downtime risks associated with shifting ensure high customer stickiness in DC business, evident from CtrlS's long-term relationship with its customers. The ratings draw further strength from the strong track record of management in the IT infrastructure space, with over two decades of experience in the industry. The demand is expected to increase in DC business because of government initiatives such as smart cities, digital India, fiscal incentives to establish data centers along with RBI's regulation dated April 2018 on data localisation and Personal Data Protection Bill 2019 which directed payment system operators to store all data, including full end-to-end transaction details, within India to ensure security of users' information.

The rating is, however, constrained by the company's large capex plans in the medium-term to develop datacenters parks in Mumbai and Hyderabad. Along with this, the company has plans to open small DCs in tier II cities. The ramp-up of Noida DC which started in 2018 is slower than expected and the rack capacity utilisation remained low between 15%-25% in last three

¹ TD means Total Debt, TNW means Tangible Net worth and OPBIDTA means Operating profit before depreciation, interest and taxes

years due to low demand prospects in the region. The ability of the company to ramp-up new DCs while maintaining healthy RoCE remains to be seen. The rating is also constrained by the heightened competition from large DC additions from established players such as Netmagic, STT Global Datacenters and Sify in the co-location business; competition is expected to further intensify with the entry of new players in the segment. While the high uptime of CtrlS DCs and customer stickiness along with the long-standing strategic relationship with its customers provide competitive advantage in case of existing business, the increase in competitive intensity could exert pressure on the operating margin of incremental business. CtrlS faces significant industry risks as data center business models continue to evolve and relatively high capital intensity nature of business. ICRA notes that although the company has adequate insurance cover to handle any liabilities that may arise due to data loss and fire accidents, the company remains exposed to reputation risk. Any significant support extended to group companies will be a key rating monitorable.

Key rating drivers and their description

Credit strengths

Healthy growth in scale of operations, robust profitability along with an improvement in RoCE: CtrlS' operating income (OI) growth has been robust at a CAGR of 34% over the last five years to Rs. 760-770 crore (estimated) in FY2021 on the back of new long-term leases, rack addition, increase in lease rates and better utilisation of its Mumbai and Hyderabad data centers (DC). Improvement in capacity utilisation led to better absorption of fixed costs. This along with focus on large accounts with high gross margins, and upward price revision for the contracts which were due for renewal in FY2020 has improved CtrlS' operating profitability to 57.1% in FY2020 and 55.0%-58.0% in FY2021 (estimates) from 40.9% in FY2019. Consequently, RoCE improved to 33.0% in FY2020 and 30.0%-33.0% in FY2021 (estimates) respectively from 17.4% in FY2019.

Strong financial profile: The financial profile of the company is strong, characterised by comfortable capital structure with TD/TNW of 0.8 times, and healthy debt coverage indicators with TD/OPBIDTA of 1.2 times, debt service coverage of 2.6 times and interest coverage of 9.2 times estimated as on March 31, 2021. Further, the company enjoys high financial flexibility, given that the current borrowings are against one-third of the rental inflows, thereby leaving two-thirds of unencumbered inflows at CtrlS's disposal. For the term debt, the company maintains an escrow account, with liquidity buffer of one month of debt obligation in the form of DSRA.

Reputed and diversified client base with high customer stickiness: The company has reputed and diversified customer base across different verticals as on December 31, 2020, top-10 customers contributed 49% of revenues in 9M FY2021. The company provides tier-IV datacenters with 99.995% uptime, which enables the company to command premium pricing than DCs with lower tier structures. The large investments made by customers and the downtime risks associated with shifting ensure high customer stickiness in DC business, evident from CtrlS's long-term relationship with its customers.

Favourable regulations support long-term prospects of DC: The demand is expected to increase in DC business because of government initiatives such as smart cities, digital India, fiscal incentives to establish data centers along with RBI's regulation dated April 2018 on data localisation and Personal Data Protection Bill 2019 which directed payment system operators to store all data, including full end-to-end transaction details, within India to ensure security of users' information.

Credit challenges

Large capex plans in medium term and under-utilisation of Noida DC - CtrlS has large capex plans in the next two-four years to develop datacenters parks in Mumbai and Hyderabad. Along with this, the company has plans to open small DCS in tier II cities. The ramp-up of Noida DC which started in 2018 is slower than expected, and the rack capacity utilisation remained low between 15% and 25% in the last three years due to low demand prospects in the region. The ability of the company to ramp-up new DCs while maintaining healthy RoCE remains to be seen.

Stiff competition from other players - The company faces heightened competition from large DC additions from established players such as Netmagic, STT Global Datacenters and Sify in the co-location business; competition is expected to further intensify with entry of new players in the segment. While the high uptime of CtrlS DCs and customer stickiness along with the long-standing strategic relationship with its customers provide competitive advantage in existing business; the increase in competitive intensity could exert pressure on the operating margins of incremental business

Exposure to reputation risk - Although the company is adequately covered with insurance to handle any liabilities that may arise due to data loss and fire accidents, the company remains exposed to reputation risk.

Liquidity position: Strong

The liquidity position of the company is strong with unencumbered cash balance of Rs. 115.2 crore as on December 31, 2020 and nil utilisation of Rs. 25 crore fund-based limits. The debt repayment of Rs. 100.6 crore for FY2022 can be comfortably met through estimated cash flow from operations. The capex for FY2022 is estimated to be Rs. 150-200 crore, against which the company has undrawn term loans of 146 crore.

Rating sensitivities

Positive factors – ICRA may upgrade CtrlS Datacenter’s ratings if there is significant increase in revenues while maintaining profitability levels. Specific credit metrics that could lead to a rating upgrade includes TD/EBITDA of less than 0.75 times and DSCR of more than 3.5 times on a sustained basis.

Negative factors – Negative pressure on the ratings may arise if higher-than-anticipated debt-funded capex or elongation in receivable cycle resulting in weakening of liquidity and coverage indicators. Specific credit metrics that could lead to a downgrade of ratings includes TD/EBITDA of more than 1.5 times and DSCR less than 2.5 times on a sustained basis.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for Entities in the Information Technology Hardware – related Services Industry
Parent/Group Support	Not Applicable
Consolidation/Standalone	Standalone

About the company

CtrlS Datacenters Limited was incorporated in 2008 and the first datacenter was started in Hyderabad in 2009. The company provides infrastructure for dedicated hosting and co-location services to global and domestic customers. The company currently has six operational data centers at four locations - Hyderabad (2), Mumbai (2), Noida and Bangalore. While the Hyderabad (Madhapur), Mumbai (2) and Noida DCs are owned and managed by CtrlS, the Bangalore DC and the Hyderabad (Gachibowli) DCs are managed by CtrlS and are operated on a revenue-sharing model. All the six current DCs of CtrlS are tier IV DCs, ensuring 99.995% availability. The major customer segments of the company are banking, financial service and insurance (BFSI), e-commerce, telecom companies, government bodies, IT companies etc.

Key financial indicators

	FY2019	FY2020	9M FY2021
	Audited	Audited	Provisional
Operating Income (Rs. crore)	449.4	656.3	571.3
PAT (Rs. crore)	53.4	183.4	171.3
OPBDIT/OI (%)	40.9%	57.1%	58.7%
PAT/OI (%)	11.9%	27.9%	30.0%
Total Outside Liabilities/Tangible Net Worth (times)	1.6	1.9	1.3
Total Debt/OPBDIT (times)	2.3	1.5	1.1
Interest Coverage (times)	5.8	7.9	8.8

Source: CtrlS; PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation

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 Mar 31, 2021 (Rs. crore)	Date & Rating in May 24, 2021	Date & Rating in FY2021	Date & Rating in FY2020	Date & Rating in FY2019	
								Oct 11, 2018	Sep 28, 2018
1	Term Loans	Long-term	553.57	553.57	[ICRA]AA-(Stable)	-	Mar 19, 2020	[ICRA]A+(Stable)	[ICRA]A+(Stable)
2	Fund based- Working Capital Facilities	Long-term	25.00	25.00	[ICRA]AA-(Stable)	-	[ICRA]A+(Stable)	[ICRA]A+(Stable)	[ICRA]A+(Stable)
3	Non-fund based Limits	Long-term	20.00	20.00	[ICRA]AA-(Stable)	-	[ICRA]A+(Stable)	-	-
4	Unallocated Limits	Long-term and short term	51.43	51.43	[ICRA]AA-(Stable)/[ICRA]A1+	-	[ICRA]A+(Stable)/[ICRA]A1	[ICRA]A+(Stable)/[ICRA]A1	[ICRA]A+(Stable)/[ICRA]A1

Complexity level of the rated instruments

Instrument	Complexity Indicator
Fund based-Term Loan	Simple
Fund based- Working Capital Facilities	Simple
Non-fund based Working Capital Facility	Very Simple
Unallocated Limits	-

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 Loan	Jun 28, 2012	-	Jan 31, 2022	21.66	[ICRA]AA- (Stable)
NA	Term Loan-II	Nov 14, 2014	-	Aug 1, 2024	20.37	[ICRA]AA- (Stable)
NA	Term Loan-III	Mar 30, 2016	-	Mar 31, 2026	25.00	[ICRA]AA- (Stable)
NA	Term Loan-IV	Dec 1, 2016	-	April 30, 2026	18.88	[ICRA]AA- (Stable)
NA	Term Loan-V	Jun 29, 2017	-	May 31, 2027	59.31	[ICRA]AA- (Stable)
NA	Term Loan-VI	Nov 30, 2018	-	Nov 30, 2028	41.83	[ICRA]AA- (Stable)
NA	Term Loan-VII	Nov 20, 2019	-	Oct 31, 2029	89.94	[ICRA]AA- (Stable)
NA	Term Loan-VIII	Mar 31, 2021	-	Mar 31, 2033	80.01	[ICRA]AA- (Stable)
NA	Term Loan-IX	Mar 8, 2017	-	Aug 31, 2023	12.01	[ICRA]AA- (Stable)
NA	Term Loan-X	Mar 31, 2020	-	Dec 31, 2025	85.64	[ICRA]AA- (Stable)
NA	Term Loan-XI	Jun 30, 2020	-	Jun 30, 2027	98.93	[ICRA]AA- (Stable)
NA	Cash Credit	-	-	-	25.00	[ICRA]AA- (Stable)
NA	Bank Guarantee	-	-	-	20.00	[ICRA]AA- (Stable)
NA	Unallocated Limits	-	-	-	51.43	[ICRA]AA- (Stable)/[ICRA]A1+

Source: CtrlS

Annexure-2: List of entities considered for consolidated analysis

Not applicable

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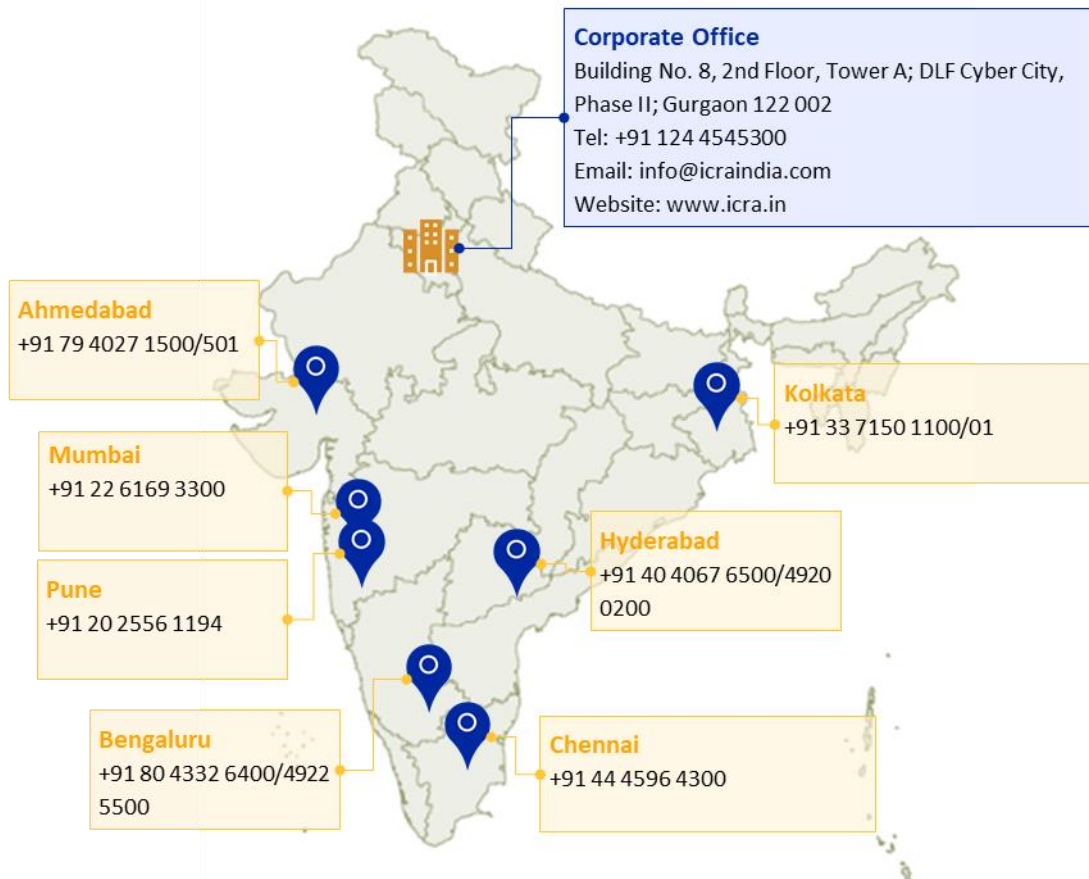
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