August 29, 2022

# CtrlS Datacenters Limited: Ratings reaffirmed

## Summary of rating action

| Instrument* | Previous Rated Amount (Rs. crore) | Current Rated Amount (Rs. crore) | Rating Action |
|---|---|---|---|
| Term Loans | 537.90 | 537.90 | [ICRA]AA- (Stable); reaffirmed |
| Non-fund Based Facilities | 27.50 | 40.00 | [ICRA]AA- (Stable); reaffirmed |
| Unallocated Limits | 167.10 | 172.10 | [ICRA]AA- (Stable)/[ICRA]A1+; reaffirmed |
| Fund-based Facilities | 17.50 | 0.00 | - |
| **Total** | **750.00** | **750.00** | |

**Instrument details are provided in Annexure-I*

## Rationale

The reaffirmation of ratings of CtrlS Datacenters Limited (CtrlS) factors in the robust growth in its operating income (OI) over the last six years to Rs. 933.0 crore in FY2022 on the back of its new long-term leases, rack addition, increase in lease rates and better utilisation of its Mumbai and Hyderabad data centres (DCs). The revenues are expected to grow by 30-35% year-on-year (YoY) in FY2023, backed by ramp-up in utilisation of its existing and new facilities. It enjoys healthy operating margins and return on capital employed (RoCE) due to increase in rack capacity utilisation and better absorption of fixed costs. The ratings note the company's strong financial profile, characterised by comfortable leverage and healthy debt coverage indicators.

Due to its large debt-funded capex in FY2023, the Net Debt/OPBITDA is expected to increase to around 1.4-1.5 times. However, the coverage indicators remained strong with projected DSCR of 4.3-4.4 times in FY2023 owing to the elongated tenure of the debt. Further, the company enjoys high financial flexibility, given that the current borrowings are against 20% of the rental inflows, thereby leaving 80% of the unencumbered inflows to CtrlS. For the term debt, it maintains an escrow account, with liquidity buffer of one month's debt obligation in the form of debt service reserve account (DSRA).

The ratings factor in the company's reputed and diversified customer base across different verticals and the tier-IV nature of the DCs, with 99.995% uptime, which enables CtrlS 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 the DC business, as evident from its long-term relationship with the customers. The ratings draw comfort 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, driven by the Government's initiatives such as Smart Cities, Digital India, fiscal incentives to establish DCs. Further, fiscal incentives by the central and state governments, infrastructure status to the sector will support the growth prospects.

The ratings are, however, constrained by the company's large capex plans in the medium term. During FY2023-FY2025, CtrlS is expected to incur a capex of Rs. 2,000-2,100 crore primarily towards setting up of DCs in Mumbai, Chennai and Hyderabad and solar power project for captive consumption. This capex is expected to be funded by a debt of Rs. 600 crore and the balance through internal accruals. Its ability to ramp-up utilisation in the new DCs, while maintaining healthy profitability and RoCE, remains to be seen. The rating is constrained by the heightened competition from large DC additions from established players such as NTT Global Data Centers, STT Global Datacenters and Sify in the co-location business as well as 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 increased competition could exert pressure on the operating margin of incremental business. CtrlS faces significant industry risks as DC business models continue to evolve and relatively high capital intensity nature of business. ICRA notes that although CtrlS 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 financial support extended to Group companies will be a key rating monitorable.

The Stable outlook on the long-term rating reflects ICRA's belief that the company would benefit from its strong financial profile, healthy demand prospects for the sector and reputed client base.

## Key rating drivers and their description

### Credit strengths

**Healthy growth in scale of operations and robust profitability –** CtrlS witnessed a robust growth in its operating income (OI) (CAGR of 31%) over the last six years to Rs. 933.0 crore in FY2022 on the back of new long-term leases, rack addition, increase in lease rates and better utilisation of its Mumbai and Hyderabad DCs. It enjoys healthy operating margins and RoCE due to an increase in rack capacity utilisation and better absorption of fixed costs. The company's operating margins remained robust at around 57-58% during FY2019-FY2022. The revenues are expected to increase by 30-35% YoY in FY2023, backed by ramp-up in utilisation of its existing and new facilities.

**Strong financial profile –** The company's financial profile is strong, characterised by comfortable leverage with Net Debt/OPBIDTA of 0.9 times and TOL/TNW of 1.0 times, healthy debt coverage indicators with debt service coverage of 2.8 times and interest coverage of 11.5 times as on March 31, 2022. Due to the large debt-funded capex in FY2023, the Net Debt/OPBITDA is expected to increase to around 1.4-1.5 times. However, the coverage indicators are likely to remain strong with projected DSCR of 4.3-4.4 times in FY2023 owing to the elongated tenure of the debt. Further, it enjoys high financial flexibility, given that the current borrowings are against 20% of the rental inflows, thereby leaving 80% of unencumbered inflows to CtrlS. 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 a reputed and diversified customer base across different verticals as on March 31, 2022, the top 10 customers contributed to 64% of revenues in FY2022. It provides tier-IV DCs with 99.995% uptime, which enables CtrlS 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 the long-term relationship with its customers.

**Favourable regulations support long-term prospects of DC –** The demand is expected to increase, driven by the Government's initiatives such as Smart Cities, Digital India, fiscal incentives to establish DCs. Further, fiscal incentives by the central and state governments, infrastructure status to the sector will support the growth prospects.

### Credit challenges

**Large capex plans in medium term –** During FY2023 – FY2025, CtrlS is expected to incur a capex of Rs. 2,000-2,100 crore primarily towards setting up of DCs (in Mumbai, Chennai and Hyderabad), and solar power project for captive consumption. The capex is likely to be funded by a debt of Rs. 600 crore and the balance through internal accruals. The company's ability to ramp-up utilisation of the new DCs, while maintaining healthy profitability and RoCE remains to be seen.

**Stiff competition from other players –** The company faces heightened competition from large DC additions from established players such as NTT Global Data Centers, STT Global Datacenters and Sify in the co-location business. The 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 competition could exert pressure on the operating margins of incremental business.

**Exposure to reputation risk –** Although CtrlS 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 company's liquidity position is strong with unencumbered cash balance of Rs. 163.3 crore as on March 31, 2022. The debt repayment of Rs. 52.7 crore for FY2023 can be comfortably met through estimated cash flow from operations. The capex for FY2023 is estimated to be ~Rs. 1,000 crore (against which it has undrawn term loans of Rs. 200 crore), which is expected to be funded by a debt of Rs. 600 crore and the balance through internal accruals.

## Rating sensitivities

**Positive factors –** ICRA may upgrade the ratings if there is significant increase in revenues while maintaining profitability levels. Specific credit metrics that could lead to a rating upgrade includes Net Debt/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 there is steep decline in revenues and profitability or any 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 Net Debt/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<br>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 (CtrlS) was incorporated in 2008 and the first DC started in Hyderabad in 2009. The company provides infrastructure for dedicated hosting and co-location services to global and domestic customers. At present, it has nine operational DCs at four locations – Mumbai (5), Hyderabad (2), Noida and Bangalore. While the Hyderabad (Madhapur), Mumbai (5) and Noida DCs are owned and managed by CtrlS Group, the Bangalore DC and the Hyderabad (Gachibowli) DCs are managed by CtrlS and are operated on a revenue-sharing model. All the nine current DCs of CtrlS are tier IV DCs, ensuring 99.995% availability. Its major customer segments are banking, financial service and insurance (BFSI), e-commerce, telecom companies, government bodies, IT companies, etc.

### Key financial indicators

| | FY2021 | FY2022 |
|---|---|---|
| | Audited | Provisional |
| **Operating income** | 780.2 | 932.9 |
| **PAT** | 234.4 | 289.1 |
| **OPBDIT/OI** | 58.6% | 57.2% |
| **PAT/OI** | 30.0% | 31.0% |
| **Total outside liabilities/Tangible net worth (times)** | 1.1 | 1.0 |
| **Total debt/OPBDIT (times)** | 1.1 | 1.2 |
| **Interest coverage (times)** | 9.1 | 11.5 |

*PAT: Profit after tax; OPBDIT: Operating profit before depreciation, interest, taxes and amortisation; Amount in Rs crore*

*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 (FY2023) | | | | Chronology of Rating History for the Past 3 Years | | | |
|---|---|---|---|---|---|---|---|---|---|
| | | Type | Amount Rated (Rs. crore) | Amount Outstanding as on Mar 31, 2022 (Rs. crore) | Date & Rating | Date & Rating in FY2022 | | Date & Rating in FY2021 | Date & Rating in FY2020 |
| | | | | | Aug 29, 2022 | June 18, 2021 | May 24, 2021 | - | Mar 19, 2020 |
| 1 | Term Loans | Long-term | 537.9 | 581.60 | [ICRA]AA- (Stable) | [ICRA]AA- (Stable) | [ICRA]AA- (Stable) | - | [ICRA]A+ (Stable) |
| 2 | Non-fund based Limits | Long-term | 40.00 | 40.00 | [ICRA]AA- (Stable) | [ICRA]AA- (Stable) | [ICRA]AA- (Stable) | - | [ICRA]A+ (Stable) |
| 3 | Unallocated Limits | Long-term and Short term | 172.10 | - | [ICRA]AA- (Stable)/ [ICRA]A1+ | [ICRA]AA- (Stable)/ [ICRA]A1+ | [ICRA]AA- (Stable)/ [ICRA]A1+ | - | [ICRA]A+ (Stable)/[ICRA]A1 |
| 4 | Fund based- Working Capital Facilities | Long-term | - | - | - | [ICRA]AA- (Stable) | [ICRA]AA- (Stable) | - | [ICRA]A+ (Stable) |

## Complexity level of the rated instruments

| Instrument | Complexity Indicator |
|---|---|
| Term Loans | Simple |
| Non-fund Based Facilities | Very Simple |
| Unallocated Limits | Not applicable |

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 analysing 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 are available on ICRA's website: www.icra.in

## Annexure I: Instrument details

| ISIN | Instrument Name | Date of Issuance | Coupon Rate | Maturity | Amount Rated (Rs. crore) | Current Rating and Outlook |
|---|---|---|---|---|---|---|
| NA | **Term Loans** | Mar 2020 | NA | Dec 2036 | 537.90 | [ICRA]AA-(Stable) |
| NA | **Non-fund Based Facilities** | NA | NA | NA | 40.00 | [ICRA]AA-(Stable) |
| NA | **Unallocated Limits** | NA | NA | NA | 172.10 | [ICRA]AA-(Stable)/[ICRA]A1+ |

*Source: Company*

*Please click here to view details of lender-wise facilities rated by ICRA*

### Annexure II: List of entities considered for consolidated analysis

Not applicable

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## About ICRA Limited:

ICRA Limited was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment Information and Credit Rating Agency.

Today, ICRA and its subsidiaries together form the ICRA Group of Companies (Group ICRA). ICRA is a Public Limited Company, with its shares listed on the Bombay Stock Exchange and the National Stock Exchange. The international Credit Rating Agency Moody's Investors Service is ICRA's largest shareholder.

For more information, visit www.icra.in

## ICRA Limited

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