August 30, 2023

Mindspace Business Parks REIT: Rating assigned for proposed NCD Programme and reaffirmed for existing limits

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Issuer rating	-	-	[ICRA]AAA (Stable); reaffirmed
Non-convertible debenture	2,050.00	2,050.00	[ICRA]AAA (Stable); reaffirmed
Proposed non-convertible debenture	0.00	500.00	[ICRA]AAA (Stable); assigned
Commercial paper programme	250.00	250.00	[ICRA]A1+; reaffirmed
Total	**2,300.00**	**2,800.00**	

**Instrument details are provided in Annexure-I*

Rationale

The rating action for Mindspace Business Parks REIT (Mindspace REIT) favourably factors in the healthy committed occupancy of the completed area at 88.8% as of June 2023, which remained at similar levels of 89.0% as of March 2023. The ratings continue to note its large and diversified portfolio of assets with office space, including completed area of 25.9 msf and under-construction/future development potential of 6.2 msf as of June 2023. Mindspace REIT's portfolio is spread across major cities such as Mumbai, Pune, Hyderabad and Chennai, with a reputed and diversified tenant mix comprising leading multi-national and Indian corporates, wherein the top 10 tenants generate 30.9% of the gross contracted rentals.

The ratings draw comfort from the low external borrowings at the consolidated level with net debt at Rs. 5,276.1 crore and comfortable Net debt/NOI at ~2.9 times as of June 2023. The portfolio has a low leverage with loan to asset value (LTV)[1] of 18.8%, which provides financial flexibility to Mindspace REIT to fund its future organic as well as inorganic growth. Based on its current capital expenditure plans, ICRA expects the Net Debt/NOI to remain less than 4.0 times in the near to medium term. Part of Mindspace REIT's debt, at the consolidated level is in the form of Non-Convertible Debentures (NCDs) and Market Linked Debentures (MLDs) with bullet repayments at the end of their maturity period, exposing the REIT to refinancing risk. This risk is mitigated to an extent by the tranche repayment of the issuances and undrawn overdraft/LRD facilities of Rs. 456.2 crore as of June 2023, which are expected to be available to meet any exigencies. ICRA notes that tenant leases contributing to ~7.0% and 3.7% of the gross contracted rentals will be due for expiry in Q2-Q4 FY2024 and FY2025, respectively. The risk is partially mitigated by reputed tenants with strong businesses and lower-than-market rentals, increasing tenant stickiness.

The ratings consider the impact of the future acquisitions that may be undertaken by Mindspace REIT on its leverage metrics. The two assets, Commerzone Raidurg, Hyderabad and The Square Avenue 98 (BKC Annex, Mumbai), which were under evaluation by the REIT for acquisition, have been put on hold in the near term. ICRA will continue to monitor the future asset acquisitions and their consequent impact on the leverage. Comfort, however, continues to be drawn from the proven track record and the experienced management of the REIT sponsor, K Raheja Corp Group (KRC), as well as the REIT manager K Raheja Corp Investment Managers LLP (KRCIML), and the financial flexibility of Mindspace REIT.

ICRA expects that Mindspace REIT's credit profile will be supported by REIT regulations that restrict the extent of under-construction assets in the portfolio to less than 20% of the asset value and the cap on leverage at 49% of the asset value. The

[1] *For the purpose of LTV calculation, Net Debt is post accounting and minority adjustments with market value is as on December 31, 2022, based on the valuation report.*

overall credit profile is expected to remain stable on the back of the large, diversified and stable operational portfolio, the anticipated growth from assets currently under development and the low leverage at the consolidated level.

Key rating drivers and their description

Credit strengths

Well-diversified and large portfolio of assets with strong tenant profile – The asset portfolio under the REIT includes some of the major business parks of Mumbai, Hyderabad, Pune and Chennai, with a reputed and diversified tenant mix comprising leading multi-nationals and Indian corporates, wherein the top 10 tenants generate 30.9% of the gross contracted rentals. The asset portfolio of the REIT includes completed office space area of 25.9 msf, under construction and future development potential of 6.2 msf. The completed area reported a committed occupancy of 88.8% as of June 2023, which remained at similar levels of 89.0% as of March 2023, supported by long-term lease agreements and a good track record of tenant stickiness owing to competitive rentals in most of the assets.

Low leverage and strong debt coverage – The ratings draw comfort from the low external borrowings at the consolidated level with net debt at Rs. 5,276.1 crore and comfortable Net debt/NOI at ~2.9 times as of June 2023, which is in similar lines as of March 2023. Thus, the portfolio has a low leverage with LTV of 18.8%, which provides financial flexibility to Mindspace REIT to fund its future organic as well as inorganic growth. The incremental debt drawdown for the under-construction assets will increase the debt to some extent in FY2024. Based on its current capital expenditure plans, ICRA expects the Net Debt/NOI to remain less than 4.0 times in the near to medium term. Low leverage provides financial flexibility to fund the future construction and acquisition.

Track record of sponsor and REIT manager – The REIT manager and sponsor are a part of KRC, which has considerable experience in developing and managing commercial real estate projects. KRC is one of India's leading groups in the real estate development and retail business, with experience of over four decades in developing and operating assets across commercial, hospitality, retail, and residential segments.

Credit challenges

Exposure to refinance risk – Part of the Mindspace REIT's debt is in the form of NCDs and MLDs with bullet repayments at the end of their maturity exposing the REIT to refinancing risk. However, this refinancing risk is mitigated to an extent by the tranche repayment of the issuances (multiple NCDs) and the undrawn overdraft/LRD facilities of Rs. 456.2 crore as of June 2023, which are expected to be available to meet any exigencies.

Expected increase in leverage levels – The two assets, Commerzone Raidurg, Hyderabad and The Square Avenue 98 (BKC Annex, Mumbai), which were under evaluation by the REIT for acquisition has been put on hold in the near term. ICRA expects the incremental capex to be funded by additional borrowings. The planned capex and acquisition plans are expected to increase the leverage, thus impacting the consolidated debt coverage indicators. However, the high financial flexibility from unencumbered assets provides some comfort. ICRA will continue to monitor the future asset acquisitions and their consequent impact on the leverage.

Vulnerability of commercial real estate sector to cyclicality – The company remains exposed to the inherent cyclicality in the real estate industry and vulnerability to external factors. ICRA notes that tenant leases contributing to ~7.0% and 3.7% of the gross contracted rentals will be due for expiry in Q2-Q4 FY2024 and FY2025, respectively. However, the risk is partially mitigated by the reputed tenants with strong businesses and the lower-than-market rentals, which increase the tenant stickiness.

Environmental and social risks

Environmental considerations – The real estate segment is exposed to risks of increasing environmental norms impacting operating costs, including higher costs of raw materials such as building materials and cost of compliance with pollution control regulations. Environmental clearances are required for commencement of projects and lack of timely approvals can impact its business operations. Impact of changing environmental regulations on licenses for property development could also create credit risks.

Social considerations – The downside social risks faced by REITs like Mindspace could be said to be low. The demand for commercial office space, particularly those with good ancillary infrastructure and connectivity has been growing in India as the service economy expands. While there could be societal trends like preference for work-from-home, which could weigh on demand, on balance, the tailwinds for commercial real estate remain reasonably strong. Further, rapid urbanisation and a large working age population will support demand for commercial real estate in India and in turn benefit REITs like Mindspace.

Liquidity position: Strong

The liquidity position of the REIT is supported by stable rental income from the underlying assets and low operational expenditure in the leasing business. Healthy fund flow from operations will be adequate to cover the debt servicing obligations. Additionally, the REIT had cash and bank balances of Rs. 351.7 crore as on June 30, 2023. Further, the REIT had unutilised overdraft/LRD facilities of Rs. 456.2 crore as of June 2023, which supports the liquidity profile.

Rating sensitivities

Positive factors – Not Applicable

Negative factors –

- Higher-than-anticipated borrowing that increases the LTV higher than 40% on a sustained basis
- Decline in the committed occupancy to lower than 80% on a sustained basis
- Any non-adherence to the debt structure
- Significant time and cost overruns in the under-construction assets, as well as any considerable delay in incremental lease tie-ups, may result in downward rating revision

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Corporate Credit Rating Methodology Rating Methodology for Real Estate Investment Trusts
Parent/Group support	Not Applicable
Consolidation/Standalone	For arriving at the ratings, ICRA has consolidated the financials of Mindspace REIT and its subsidiaries (as mentioned in Annexure II)

About the company

Mindspace REIT is a Real Estate Investment Trust (REIT) listed in India under the SEBI Real Estate Investment Trust Regulations, 2014. It is incorporated as a registered trust and listed through a public issue of units. The sponsor of Mindspace REIT is the K Raheja Corp Group, which has contributed shares in eight special purpose vehicles (SPVs) to the REIT in lieu of units in the latter. Mindspace REIT primarily holds interests in rental yielding of commercial real estate assets (Grade-A office portfolio). The REIT houses a facility management division in one of the SPVs. The asset portfolio of the REIT has a total completed area of 25.9 msf, and under-construction area and area for future development of 6.2 msf. The REIT may also acquire additional assets in future as per its investment criteria to grow the portfolio inorganically.

Key financial indicators (audited)

Consolidated	FY2021*	FY2022	FY2023
Operating income	1138.1	1750.1	2282.1
PAT	334.9	447.3	308.5
OPBDIT/OI	74.4%	78.0%	67.4%
PAT/OI	29.4%	25.6%	13.5%
Total outside liabilities/Tangible net worth (times)	0.3	0.4	0.5
Total debt/OPBDIT (times)	4.5	3.3	3.6
Interest coverage (times)	4.9	5.2	4.5

**Audited results for 8 months (August-March)*

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

Source: Annual Report and Company, ICRA Research

Status of non-cooperation with previous CRA: Not applicable

Any other information:

The company also faces prepayment risk, given the possibility of debt acceleration upon the breach of covenants, including financial covenants, operating covenants and rating linked covenants. Upon failure to meet the covenants, if the company is unable to get waivers from the lenders/investors or the lenders/investors do not provide it with adequate time to arrange for alternative funding to pay off the accelerated loans, the rating would face pressure.

Rating history for past three years

	Instrument	Current Rating (FY2024)					Chronology of Rating History for the Past 3 Years					
		Type	Amount Rated (Rs. crore)	Amount outstanding as on Mar 31, 2023 (Rs. crore)	Date & Rating in FY2024		Date & Rating in FY2023	Date & Rating in FY2023	Date & Rating in FY2023	Date & Rating in FY2022	Date & Rating in FY2021	
					Aug 30, 2023	May 23, 2023	Feb 20, 2023	Jan 6, 2023	Jun 16, 2022	Sep 16, 2021	Aug 28, 2020	Jul 25, 2020
1	Issuer rating	Long-term	-	-	[ICRA] AAA (Stable)	[ICRA] AAA (Stable)	[ICRA] AAA (Stable)	[ICRA] AAA (Stable)	[ICRA] AAA (Stable)	[ICRA] AAA (Stable)	[ICRA] AAA (Stable)	Provisional [ICRA]AAA (Stable)
2	Non-convertible debenture	Long-term	2050.0	2050.0	[ICRA] AAA (Stable)	[ICRA] AAA (Stable)	[ICRA] AAA (Stable)	[ICRA] AAA (Stable)	[ICRA] AAA (Stable)	-	-	-
3	Proposed non-convertible debenture	Long-term	500.00	-	[ICRA] AAA (Stable)	-	-	-	-	-	-	-
4	Commercial paper	Short - term	250.00	0.0	[ICRA] A1+	[ICRA] A1+	[ICRA] A1+	-	-	-	-	-

Complexity level of the rated instruments

Instrument	Complexity Indicator
Issuer rating	NA
Proposed non-convertible debenture	Simple

Commercial paper	Very Simple
Non-convertible debenture	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 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: Click Here

Annexure I: Instrument details

ISIN	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (Rs. crore)	Current Rating and Outlook
INE0CCU07058	Non-convertible debenture	Feb- 2022	6.35%	Dec - 2024	500.00	[ICRA]AAA (Stable)
INE0CCU07066	Non-convertible debenture	July- 2022	7.9%	FY2028	500.00	[ICRA]AAA (Stable)
INE0CCU07074	Non-convertible debenture	Mar- 2023	8.0%	FY2027	550.00	[ICRA]AAA (Stable)
INE0CCU07082	Non-convertible debenture	Jun- 2023	7.75%	Jun- 2026	500.00	[ICRA]AAA (Stable)
-	Issuer ratings	-	-	-	-	[ICRA]AAA (Stable)
-	Proposed non-convertible debenture*	-	-	-	500.00	[ICRA]AAA (Stable)
-	Commercial paper*	-	-	-	250.00	[ICRA]A1+

*Source: Company; *Proposed to be listed*

Annexure II: List of entities considered for consolidated analysis

Company Name	Ownership	Consolidation Approach
Intime Properties Limited	89%	Full Consolidation
Sundew Properties Limited	89%	Full Consolidation
K. Raheja IT Park (Hyderabad) Limited	89%	Full Consolidation
Mindspace Business Parks Private Limited	100%	Full Consolidation
Gigaplex Estates Private Limited	100%	Full Consolidation
Avacado Properties & Trading (India) Private Limited	100%	Full Consolidation
KRC Infrastructure and Projects Private Limited	100%	Full Consolidation
Horizonview Properties Private Limited	100%	Full Consolidation

Source: Company

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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.

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