November 03, 2023

ESR Pune Industrial Park Private Limited: Rating upgraded to [ICRA]A-(Stable)

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term – Fund-based – Term loan	183.0	119.72	[ICRA]A-(Stable) upgraded from [ICRA]BBB+(Stable)
Long-term – Unallocated	17.00	80.28	
Total	**200.00**	**200.00**	

**Instrument details are provided in Annexure-I*

Rationale

The rating upgrade for ESR Pune Industrial Park Private Limited (EPPL) factors in the increase in its leasing levels to 100% as of September 2023 from 74% as of September 2022. The rating notes the expected completion of the project in Q4 FY2024, resulting in improved cash flow visibility and debt protection metrics. EPPL has incurred 85% of the project cost as of June 2023. The rentals for 80% of the leasable area have already commenced, while those for the balance 20% area is scheduled to commence in H2 FY2024. With incremental leasing, the outstanding construction finance (CF) loan (38% of total CF loan) is anticipated to be converted to lease rental discounting (LRD) loan in H2 FY2024, thereby mitigating the refinancing risk. The leverage is likely to be moderate, with total debt to net operating income (NOI) at around 7.4 times (PY: 8.2 times) as of March 2024 and adequate debt coverage metrics, with five-year average DSCR at around 1.2 times for FY2024-FY2028.

The rating continues to consider the EPPL's strong sponsor profile, backed by the ESR Group, which has a long and established track record in developing and leasing logistics and industrial parks globally and the presence of a debt service reserve account (DSRA) and escrow mechanism for the debt. The rating factors in the favourable asset location, which offers good connectivity. The asset is situated in an industrial belt that has evolved into a mature manufacturing and industrial hub.

The rating, however, continues to be constrained by the high tenant concentration risk, with top two tenants occupying around 75% of the total area, exposing EPPL to vacancy risks. However, long-term lease agreements with adequate lock-in period mitigates the risk to an extent. The company is also exposed to high geographical and asset concentration risks, which are inherent in single asset special purpose vehicle (SPV). The rating notes the vulnerability of debt coverage ratios to factors such as changes in interest rate or reduction in occupancy levels. Further, the increase in competition in the industrial warehousing segment may put pressure on the occupancy or the rental rates over the medium to long term.

The Stable outlook on the rating reflects ICRA's opinion that the company will benefit from the favourable location of the asset, generate steady rental revenues, backed by healthy occupancy levels with adequate debt coverage metrics.

Key rating drivers and their description

Credit strengths

Experienced promoters with long track record globally – The ESR Group is one of Asia's largest developers and operators in the logistics and warehousing segment with an established track record of developing and leasing logistics and industrial parks globally. The Group's Indian operations are focused towards developing and leasing logistics and industrial parks in the country.

Attractive location of property with increase in leasing levels – The project site is in Chakan area, Pune, around 35 km away from the Central Business District, in Pune. The favourable asset location offers good connectivity. The asset is situated in an industrial belt that has evolved into a mature manufacturing and industrial hub. The rating factors in the increase in leasing levels to 100% as of September 2023 from 74% as of September 2022 and expected completion of the project in Q4 FY2024, resulting in improved cash flow visibility and debt protection metrics. The leverage is likely to be moderate, with total debt to NOI at around 7.4 times (PY: 8.2 times) as of March 2024 and adequate debt coverage metrics, with five-year average DSCR at around 1.2 times for FY2024-FY2028. Additionally, there is a presence of debt service reserve account (DSRA) to the tune of Rs. 14 crore, which is equivalent to around three months' debt servicing for the entity.

Conversion of partial CF loan to LRD; expected full conversion in near term provides comfort – EPPL has incurred 85% of the project cost as of June 2023. The rentals for 80% of the leasable area have already commenced, while those for the balance 20% area is scheduled to commence in H2 FY2024. With incremental leasing, the outstanding CF loan (38% of total CF loan) is likely to be converted to lease LRD loan in H2 FY2024, thereby mitigating the refinancing risk.

Credit challenges

Exposure to high tenant concentration risk – EPPL continues to be constrained by the high tenant concentration risk, with top two tenants occupying around 75% of the total area, exposing them to vacancy risks. However, long-term lease agreements with adequate lock-in period mitigates the risk to an extent. It is exposed to high geographical and asset concentration risks, which are inherent in single asset SPVs.

Vulnerable to cyclicality and interest rate scenario – The rating notes the vulnerability of debt coverage ratios to factors such as changes in interest rate or reduction in occupancy levels. Further, the increase in competition in the industrial warehousing segment may put pressure on the occupancy or rental rates over the medium to long term.

Liquidity position: Adequate

The company's liquidity position is adequate with free cash and liquid investments of Rs. 31 crore as on March 31, 2023. The repayment obligation of Rs. 7.0 crore in FY2024 can be comfortably serviced through its estimated cash flow from operations.

Rating sensitivities

Positive factors – The rating may be upgraded if there is a significant improvement in rental rates or a material reduction in debt levels, resulting in improvement in coverage metrics. Specific metric for an upgrade would be five-year average DSCR above 1.3 times and Debt/NOI less than 6.5 times on a sustained basis.

Negative factors – The pressure on the rating could arise if there is any material decline in occupancy levels/rental rates or a significant increase in indebtedness, resulting in weakening of debt coverage and leverage metrics or the liquidity position on a sustained basis. Specific metric for a downgrade would be five-year average DSCR sustaining below 1.15 times.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Corporate Credit Rating Methodology Rating Methodology for Debt Backed by Lease Rentals
Parent/Group support	Not Applicable
Consolidation/Standalone	Standalone

About the company

EPPL, a part of the ESR Group, was incorporated on November 13, 2017, to develop and lease industrial park/logistics facilities. It is undertaking a single project located in Chakan MIDC Phase-II, Pune. The project is spread over 53 acres with a potential leasable area of 14 lakh square feet.

The ESR Group is one of Asia's largest developers and operators in the logistics and warehousing segment. The Group is backed by strong investors including Warburg Pincus, APG, CPPIB, Goldman Sachs, Morgan Stanley AIP, PGGM, Allianz, Ping An and SK Holdings.

Key financial indicators

Standalone	FY2022	FY2023
	Audited	Provisional
Operating income	9.6	25.0
PAT	(7.7)	(38.9)
OPBDIT/OI	263.7%	78.8%
PAT/OI	-80.3%	-155.3%
Total outside liabilities/Tangible net worth (times)	(55.4)	(10.3)
Total debt/OPBDIT (times)	14.3	23.1
Interest coverage (times)	0.9	0.5

Source: Company; ICRA Research; PAT: Profit after tax; OPBDIT: Operating profit before depreciation, interest, taxes and amortisation; Amount in Rs. crore

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

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 Sep 30, 2023 (Rs. crore)	Date & rating in FY2024	Date & rating in FY2023	Date & rating in FY2022	Date & rating in FY2021
					Nov 03, 2023	Oct 31, 2022	Jul 30, 2021	Apr 07, 2020
1	**Term loan**	Long Term	119.72	68.39^	**[ICRA]A- (Stable)**	**[ICRA]BBB+ (Stable)**	**[ICRA]BBB (Stable)**	**[ICRA]BBB (Stable)**
2	**Unallocated**	Long Term	80.28	-	**[ICRA]A- (Stable)**	**[ICRA]BBB+ (Stable)**	**[ICRA]BBB (Stable)**	-

^Undrawn limit of Rs. 51.33 crore

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long-term Fund-based – Term loan	Simple
Long-term – Unallocated	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: [Click Here.]

Annexure I: Instrument details

ISIN	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	**Term loan**	FY2021	-	FY2025	119.72	**[ICRA]A-(Stable)**
NA	**Unallocated**	-	-	-	80.28	**[ICRA]A-(Stable)**

Source: Company, ICRA Research

Annexure II: List of entities considered for consolidated analysis – Not Applicable

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About ICRA Limited:

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