

Merlin Acropolis Projects Pvt Ltd.

February 27, 2019

Summary of rating action

Instrument*	Current Rated Amount (Rs. crore)	Rating Action
Term Loan	15.00	[ICRA]A (Stable); Assigned
Total	15.00	

*Instrument details are provided in Annexure-1

Rationale

For arriving at Merlin Acropolis Projects Pvt Ltd.'s (MAPPL's) ratings, ICRA has taken a consolidated view of the operational entities in the Merlin Group, having ongoing projects and/or outstanding debt, given the close business, financial and managerial linkages among them.

The rating assignment takes into consideration the established market position of the Merlin Group, of which MAPPL is a part, with a track record of around three decades in the real estate sector, particularly in and around Kolkata area. The Group has demonstrated strong project execution, sales and leasing capabilities, as demonstrated through completion of more than 10 million square feet (msf) of development across residential, commercial and retail segments, as well as successful leasing of around 2.6 msf of commercial space. At present, the Group is undertaking 11 projects amounting to around 4.5 msf of development, of which Merlin Group's share is 3.4 msf. Most of the ongoing projects are at an advanced stage of construction and have achieved healthy booking levels, resulting in execution and market risks being mitigated to an extent. However, ICRA notes that execution risks remain for the few projects that are at an intermediate stage as well as for the planned project pipeline over the medium term. Off-take risks also remain for Merlin Group's share of the unsold inventory of around 0.9 msf, with certain projects having slow-moving inventory. Nonetheless, the consolidated financial profile of the group remains healthy, with comfortable cash flow adequacy indicators on the back of robust collections and high committed receivables in most projects leading to low dependence on debt. The consolidated project gearing is conservative at 0.2 times as on December 31, 2018, and around 47% of the total debt portfolio comprises rental securitization loans, backed by rental income. The low level of leverage, together with a fully paid-up land bank and availability of undrawn bank lines, support the financial flexibility available with the Group. Going forward, ICRA expects the debt levels to remain low, given the high cash flow visibility attributable to healthy collections and stable rental income, the conservative approach of the management towards leverage, and the continued execution of a part of the project portfolio through joint development agreements (JDAs) with landowners, which limits upfront capital costs. The rating is, however, constrained by the high concentration of the Group's operations, which are largely confined in one city, i.e. Kolkata and its surrounding areas, which exposes it to fluctuations in a single market's performance, as well as by the significant expansion plans for the group.

The rating also factors in the favourable location and healthy occupancy levels of MAPPL's single property – Merlin Acropolis Mall. The tenant profile of the mall is diversified and includes reputed anchors such as Shoppers Stop and Cinopolis, and lease renewal risks are low, with no major renewals falling due over the next three years. ICRA notes that the rental securitization loans availed by the Merlin Group have primarily been taken against this property. The cash flow cover on the loans is adequate, and the presence of a debt service reserve account (DSRA) equivalent to one quarter of interest and principal repayment, as well as an escrow structure, provides additional comfort.

Outlook: Stable

ICRA believes that healthy cash flows from the ongoing projects, arising from continued robustness in sales velocity and collections, backed by the high level of committed receivables at present, will support the Group's financial risk profile over the near-to-medium term, and keep the overall debt level of the Group low. Stable rental income is expected to further support the overall cash flow position. The outlook may be revised to Positive if there is a considerable increase in sales velocity, with continued robustness in collection efficiency, resulting in better-than-expected cash flow. The outlook may be revised to Negative in case of any slowdown in project execution/or deterioration in the Group's liquidity position due to inadequate accruals, considerable decline in sales velocity, reduction in occupancy levels in leased properties, large investments in landbank or any other unforeseen downturn in the industry resulting in pressure on the financial profile of the company.

Key rating drivers

Credit strengths

Established real-estate developer with a track record of around three decades and a strong market position in Eastern India, particularly Kolkata - The Merlin Group has an established track record in the real sector in Eastern India, particularly in and around Kolkata, having completed over 10 msf of development till date. It is reputed for providing timely delivery of good quality assets across residential, commercial and retail segments, at an attractive average ticket size of around Rs. 55 lakhs per unit. The Group has also successfully leased commercial space of around 2.6 msf across two properties, with average occupancy levels standing at around 95%.

Healthy booking levels in most ongoing projects reduces market risks, although off-take risks remain for the unsold inventory, with sales for certain projects being slow at present -The group is currently undertaking 11 ongoing projects, having a total saleable area of 4.5 msf, of which Merlin Group's share is 3.4 msf. The aggregate booking level stands at a healthy 73% across the ongoing projects, with the pace of sales remaining in line with the pace of construction, and overall sale velocity remaining healthy. At the current sales velocity, the unsold stock would be liquidated in 1.7 years. The largest ongoing project, 5th Avenue, together with its LIG and MIG components, is performing particularly well, with 90% of the saleable area of 0.8 msf having been sold till December, 2018. However, off-take risks remain for Merlin Group's share of the unsold inventory, which stands at around 0.9 msf, with certain projects having slow-moving inventory. In particular, the sales for Merlin Gangotri and Merlin Regalia have been low. However, ICRA notes that construction is at an advanced stage for Merlin Regalia, and post completion, a considerable portion of the total saleable area is to be handed over to the land-owner, thus reducing the market risks for the project.

Healthy financial profile, with comfortable cash flow adequacy indicators and low dependence on debt; fully paid-up land bank, undrawn bank lines and low leveraging in ongoing projects provide financial flexibility - The adequacy of committed receivables¹ on an aggregate basis as in December, 2018 stood at a high 107%, on the back of considerable committed receivables from the sold area and low pending cost for ongoing projects, given the advanced stage of construction for most projects. Collections have also been healthy thus far, leading to low dependence on debt. The group takes a conservative approach towards debt for the projects, resulting in the consolidated project gearing being conservative at 0.2 times as in December, 2018. Several projects have been undertaken through joint development agreements with landowners, which has limited upfront capital costs and debt requirements as well. The Group also has a considerable fully paid up land bank, which, in addition to providing visibility on future projects, also serves as a source of financial flexibility. Moreover, with the Group maintaining a low level of leverage in its ongoing projects, and keeping sufficient undrawn bank lines in hand, the overall liquidity position remains comfortable.

¹ Defined as $(\text{committed receivables} + \text{undrawn debt}) / (\text{pending cost} + \text{debt outstanding} + \text{undrawn debt})$

Stable rental income from favourably located retail property with high occupancy further supports cash flows; rental securitization loans availed against the same carry a DSRA and an escrow mechanism – MAPPL currently owns a single property - Merlin Acropolis Mall, with 0.28 msf of leasable area, located on Rajdanga Main Road in Kolkata. The mall is favourably located in an upcoming commercial hub, and thus benefits from a populous catchment area, which, in turn, has resulted in occupancy levels being high at 95%. The tenant profile of the mall is diversified and includes reputed anchors such as Shoppers Stop and Cinopolis, and lease renewal risks are low, with no major renewals falling due over the next three years. The stable rental income being generated by the mall has been leveraged to obtain rental securitization loans, which comprise around 45% of the total debt portfolio of the Merlin group. The cash flow cover on the loans is adequate, and the presence of a debt service reserve account (DSRA) equivalent to one quarter of interest and principal repayment, as well as an escrow structure, provides additional comfort.

Credit challenges

Moderate scale and high concentration of operations in the Kolkata market, which exposes the entity to fluctuations in a single market's performance - Of the ~4.5 msf being constructed by the Merlin Group at present, around 89% is being developed in and around Kolkata, thereby exposing the group to geographical concentration risks, although ICRA notes that the projects are diverse in the end-user segments that they are targeting. Moreover, the group is slowly expanding into other geographies, and has some, albeit limited, presence in Odisha, Chennai, Chhattisgarh and Ahmedabad as well. Overall scale of operations, however, remains moderate.

While 74% of construction project cost has been incurred on an aggregate basis, certain projects are at intermediate stage of development, which, together with projects in the pipeline, results in exposure to execution risks – On an aggregate basis, 74% of the total project cost had been incurred till December, 2018. However, certain projects are at an intermediate stage, thus exposing the Group to execution risks for the concerned area. Construction progress in the Group's largest project, 5th Avenue, stands at 62% as in December, 2018. The 1, Verve and Gangotri are also at intermediate stages, with just over 50% of the project cost having been incurred for each of the three projects. Moreover, the Group also has a significant project pipeline, with a planned constructed area of around 4.9 msf to be developed over the medium to long term, which exacerbates the execution risks, although ICRA notes that the Group intends to launch the same in a phased manner. The cost and funding pattern of the upcoming projects is yet to be determined.

Susceptibility of the real-estate sector to economic cycles– Real-estate developers, including the Merlin group, remain exposed to the inherent cyclicity of the real-estate sector, which can result in volatility in cash flows.

Liquidity Position:

The Group's liquidity profile is supported by high committed receivables of Rs. 493 crore from the sold area (Merlin Group's share) as well as undrawn bank limits. Moreover, MAPPL maintains a DSRA equivalent to one quarter of principal and interest servicing on its rental securitization loan, which accounts for almost 45% of the total debt outstanding as in December, 2018.

Analytical approach:

Analytical Approach	Comments
Applicable Rating Methodologies	Rating Methodology for Real Estate Entities
Parent/Group Support	Not Applicable
Consolidation / Standalone	For arriving at the ratings, ICRA has taken a consolidated view of MAPPL along with its operational group entities having ongoing projects and/or outstanding debt (as mentioned in Annexure-2), given the close business, financial and managerial linkages among them. In line with its methodology for rating real estate entities, Merlin Group's share of the cash flows across various group companies have been consolidated.

About the Group:

The Merlin group, which has more than three decades of experience in the realty sector, has developed over 100 residential and commercial complexes and 150 independent bungalows, with a total constructed area in excess of 10 million square feet (msf), mostly in and around Kolkata. The Group also has some presence in other parts of India with various residential and commercial projects at Chennai, Chhattisgarh and Ahmedabad as well. Merlin Projects Limited (MPL) is the flagship entity of the Merlin Group, and was established in 1976 as a partnership firm, before being converted to a public limited company in 1992.

About the company:

Merlin Acropolis Projects Pvt Ltd. was established in 2009 for development of a stadium and a commercial complex under a Public Private Partnership (PPP) model with the Kolkata Metropolitan Development Authority (KMDA). The company developed Acropolis Mall, which comprises 3B+G+18 floors and is located on Rajdanga Main Road in Kolkata. 3B+G+4 are dedicated to the mall and floors 5th to 18th are for commercial office space. The mall and 5th floor of the commercial office space lies under MAPPL, with the remaining office space from 6th to 18th floor is in a group company, Merlin Projects Limited (MPL). Total leasable area available with MAPPL as on date stands at around 0.28 msf.

In FY2018, the company reported a net profit of Rs. 9.7 crore on an operating income of Rs. 33.7 crore compared to a net profit of Rs. 9.7 crore on an operating income of Rs. 29.3 crore in the previous year.

Key financial indicators (stand-alone)

	FY2017	FY2018
Operating Income (Rs. crore)	29.33	33.75
PAT (Rs. crore)	9.7	9.7
OPBDIT/OI (%)	98.9%	98.8%
RoCE (%)	11.5%	14.3%
Total Debt/TNW (times)	3.7	2.7
Total Debt/OPBDIT (times)	4.9	3.9
Interest coverage (times)	2.6	3.6

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years:

		Current Rating (FY2019)			Chronology of Rating History for the Past 3 Years		
Instrument	Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating Feb 2019	Date & Rating in FY2018	Date & Rating in FY2017	Date & Rating in FY2016
1	Term Loans	15.00	15.00	[ICRA]A (Stable)	-	-	-
Total		15.00					

Complexity level of the rated instrument:

ICRA has classified various instruments based on their complexity as "Simple", "Complex" and "Highly Complex". The classification of instruments according to their complexity levels is available on the 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	Jan-18	NA	FY2026	15.00	[ICRA]A (Stable)

Source: Company

Annexure-2: List of entities considered for consolidated analysis

Company Name	Economic Interest	Consolidation Approach
Merlin Acropolis Projects Private Limited	100%	Full Consolidation
Merlin Projects Limited	100%	Full Consolidation
Bengal Merlin Housing Limited	100%	Full Consolidation
PS Merlin Developers LLP	100%	Full Consolidation
Merlin Developers Private Limited	100%	Full Consolidation
Merlin Real Estate LLP	100%	Full Consolidation
Elita Garden Vista Project Private Limited	37.5%	Proportional Consolidation
Sureka Merlin Promoters Private Limited	48%	Proportional Consolidation

ANALYST CONTACTS

Shubham Jain

+91 1244545 306

shubhamj@icraindia.com

Mahi Agarwal

+91 337150 1106

mahi.agarwal@icraindia.com

RELATIONSHIP CONTACT

Jayanta Chatterjee

+91 80 4332 6401

jayantac@icraindia.com

MEDIA AND PUBLIC RELATIONS CONTACT

Ms. Naznin Prodhani

Tel: +91 124 4545 860

communications@icraindia.com

Helpline for business queries:

+91-9354738909 (open Monday to Friday, from 9:30 am to 6 pm)

info@icraindia.com

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For more information, visit www.icra.in

ICRA Limited

Corporate Office

Building No. 8, 2nd Floor, Tower A; DLF Cyber City, Phase II; Gurgaon 122 002

Tel: +91 124 4545300

Email: info@icraindia.com

Website: www.icra.in

Registered Office

1105, Kailash Building, 11th Floor; 26 Kasturba Gandhi Marg; New Delhi 110001

Tel: +91 11 23357940-50

Branches

Mumbai + (91 22) 24331046/53/62/74/86/87

Chennai + (91 44) 2434 0043/9659/8080, 2433 0724/ 3293/3294,

Kolkata + (91 33) 2287 8839 /2287 6617/ 2283 1411/ 2280 0008,

Bangalore + (91 80) 2559 7401/4049

Ahmedabad+ (91 79) 2658 4924/5049/2008

Hyderabad + (91 40) 2373 5061/7251

Pune + (91 20) 2556 0194/ 6606 9999

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