
Rating Rationale for Century Real Estate Holdings Pvt. Ltd's proposed secured Non-Convertible Debentures Issue of ₹ 200 Crores (Two Hundred Crores)

NCD Issue Rating: BWR BBB (SO)

Outlook : Stable

Brickwork Ratings (BWR) has assigned **BWR BBB (SO) [Pronounced BWR Triple B (Structured Obligation)]** for Century Real Estate Holdings Private Limited's proposed Secured Bond issue of ₹ 200 crore, having a tenor of 48 months. 'BWR BBB' stands for an instrument that is considered to offer **MODERATE** credit quality in terms of timely servicing of principal and interest obligations.

The rating has factored, inter alia, the characteristics of the Projects in context, the strong credentials of the Board of Directors and the senior management, the long history of the company, the security and the Escrow mechanism for meeting the NCD obligations. The rating is however constrained by project risk, risk of sustainability of property prices and margins, unavailability of consolidated financial statements, Century's relatively lesser exposure to independent development projects, absence of any significant operating income from the projects in context and the current status of the Real estate industry.

BWR has essentially relied upon the information/ clarification provided by the issuer, Term sheet outlining the structure of the deal, audited financial results of the company as of FY 2010 and its SPVs.

Background

Established in 1973, Century Group ("Century Group") is a renowned real estate group in Bengaluru. Group has over the years evolved itself to become a full service real estate developer. The Group initially focused on acquiring and consolidating land parcels on large scale. Since 2004, Century has transitioned into a full service real estate developer by launching projects under their own brand through undertaking developments under Century Real Estate Holdings Private Limited ("CREH").

Over the past few years, the Company owns approximately 1 million square feet ("mn sft") of completed development and is currently undertaking about 3 mn sft under various stages of development. Also, the company has successfully tied-up with strategic and financial partners to

optimally develop the real estate assets. Currently, Century's portfolio includes over 1,200 acres of free-hold land spread majorly across Bengaluru and a development portfolio of over 21 mn sft comprising residential, commercial, hotels, educational institutions and integrated townships.

Going forward, the Company intends to focus on independent development of properties while also continuing with the model of joint development partnerships. The Company will also continue to form strategic alliances with reputed developers and financial partners in order to unlock better real estate value of existing land banks.

Management Profile

Century is promoted by Dr. P Dayananda Pai (also Founder of VidyaSagar schools and a recipient of Karnataka Udyog Award in 1990) and his brother Mr. P Satish Pai. Century Real Estate Holdings (CREH) is led by Mr. Ravindra Pai who is a post graduate from the prestigious Indian Institute of Management, Bangalore.

Over the last 35 years, Century has grown to have a staff of 317 real estate professionals, each having in-depth industry knowledge and expertise.

Shareholding

As informed by the company, Promoters have aggregate holdings of 76% in CREH and the balance 24% is owned by a private equity firm M/s Drawbridge Century Holdings Ltd., Mauritius, (Fortress Capital).

Projects in Context

The company is raising money for developing two projects – Century Square and Salarpuria Century Towers. Century Square is a 11.26 acres residential cum commercial complex located at Bellary Road, Hebbal. The bookings are about to start for the residential apartments and the project is slated to complete in March 2014. Salarpuria Century Towers is a 9.48 acres Joint Development project with the Kolkata based Salarpuria Group. It is a purely residential project located at Old Airport Road, Bengaluru. The construction will commence in July 2011 and is expected to finish by March 2016.

Revenue Sharing on the Projects

Century will get 79% of revenue from residential sales and 60% of revenue from commercial sales in the Century Square project. In the Salarpuria Century Towers project, Century stands to get nearly 41% of the revenue against its contribution towards land.

The NCD Issue & Its Redemption

CREH plans to issue ₹200 cr secured non-convertible debentures with a tenure of 48 months. The bonds will carry a quarterly coupon of 4.67% to be paid at the end of each quarter. The coupon and the principal repayment shall be made subject to availability of **Free Cash Flows** in any financial quarter. Any unpaid coupon will be compounded at quarterly rate of 4.67% such that the IRR doesn't exceed 20%. The "Free Cash Flows" are summation of "Free Cash Flows A" and "Free Cash Flows B" where

Free Cash Flows A = Sale Proceeds from developer's share of area in Century Square project excluding payments received towards Society Formation Charges, Share Application Money, Maintenance Charges, Taxes and Deposits to Utility Providers – **Cost of Development**

Free Cash Flows B = 41% of sale proceeds from Salarpuria Century Towers project

Free Cash Flows will be calculated on a quarterly basis jointly by Investor and Developer. The NCD holders will be entitled for 60% to 100% of the Free Cash Flows from the projects, till such time that the Investor has made a pre tax IRR of 20% on the NCDs. Thereafter the Investor shall not have any share in the Free Cash Flows.

All the sale proceeds for the projects will be deposited in an Escrow Account. A SEBI registered Debenture Trustee will be appointed by the Issuer.

Security

- NCDs shall carry a first charge on the unsold Saleable Area in the Projects, Receivables and Escrow Account
- Also offered as security are the Post Dated Cheques of ₹414 cr, Promoter guarantee and Corporate Guarantee of the developer

Financial Analysis

Based on the projections provided to us, the company is expected to record ₹105 cr of sales by March FY2011. The SPVs, Century Shelters, a partnership firm (formed in 2007) & Suruchi Properties Pvt. Ltd. (recently acquired from Salarpuria) would be implementing the two projects and would subsequently record revenues from Fy12.

Century gained about ₹6.27 cr of rental/revenue share between March 2010 and December 2010 from its completed projects. This annuity income, along with the sale of land, is a predictive revenue source for the company.

There are 11 ongoing projects of which almost 50% are joint development (JD) / joint venture(JV) in nature. The JD/JVs typically yield 35%-40% revenue share for Century. Between Mar 2010 to Dec 2010, Century recorded about ₹86 cr of sales value from these ongoing projects. This revenue source doesn't involve any major Project Risk to Century.

There are another 21 upcoming projects in which Century owns the land and will undertake independent development except for a few, where it has identified the JD/JV Partner. The Financial Closure is yet to happen on these set of projects.

Century expects to see 5x revenue in FY12 as against FY11. This is mainly on account of customer advances /rentals from the new launches and higher proportion of Independent Development projects which leads to higher margins for the company.

About 70% of the current development portfolio of Century is in Residential segment. Lesser exposure to Commercial segment means lesser portfolio risk but consequently the bottom-line margins are relatively lower as well.

The total debt outstanding for CREH is around ₹562 cr (including ₹200 cr of the proposed NCD) out of which around ₹450 cr are borrowings from current FY. As a result, we see the debt-equity ratio for current FY at a consolidated level at 1.21, which is slightly on the higher side. But with new project launches and improved equity position, we see D/E falling to a comfortable 0.18 by FY2014. For the two projects in context here, the D/E is at 3.4 for current FY and it falls to 0.11 by Fy2014. Debt servicing has not yet started for around 88% of the total outstanding debt. By the time, the debt servicing on this portion starts, CREH expects decent bookings on the launched projects.

On a consolidated level, Debt Service Coverage Ratio stands at 1.19 and 3.33 for FY11 and FY14 respectively. Looking at the SPV level, DSCR is -ve for current FY (absence of any income) but it improves to 3.20 by FY14.

Century has assumed a base selling rate per square feet for residential portion at ₹6250/= (for Century Square) and ₹6500/= (for Salarpuria Century Towers) keeping in view the location of the projects. A sensitivity analysis (for the two projects) assuming a fall in sales realizations by over 30% still yields a comfortable DSCR except for FY2015 (owing to debt repayment).

Risk Factors

As per the term sheet, ₹50 cr will be used towards the development of two projects while the balance fund will be used for general corporate purposes. The unavailability of Consolidated Book of Accounts has been a constraining factor for the given rating.

Both the projects have a long gestation period of 4-5 years. Additionally, unlike the project Salarpuria Century Towers which is a JD project, the Century Square will be developed as an independent project by Century on its own which exposes the company to Construction Risk as well.

Century is involved in arbitration with one of its Joint Development partners in a completed project where the dispute is on the portion of rental income. While we have captured the downside scenario, if the award is in Century's favour, the topline will increase by another ₹25-30cr.

The prescription of higher risk weight for real estate industry by the RBI and the current market outlook on this industry adds up to the risk factors governing this rating.

Rating Outlook

We believe the rating is sensitive to sustainability of the current property price levels and margins and timely completion of ongoing projects. Century has a huge land bank in and around Bengaluru and the company is basically trying to unlock value and grow. Even though the proportion of Joint Development /Joint Venture projects is slated to go down in the years to come, the ability of the company to manage the JD/JV relationships remains one of the key factors towards the stability of its income.

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