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India Ratings Upgrades The Phoenix Mills to 'IND A+'/Stable; Limits Enhanced

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By Mahaveer Jain

India Ratings and Research (Ind-Ra) has upgraded The Phoenix Mills Limited's (PML) Long-Term Issuer Rating to 'IND A+' from 'IND A'. The Outlook is Stable. Instrument-wise rating actions are given below:

Instrument Type	Date of Issuance	Coupon Rate	Maturity Date	Size of Issue (million)	Rating/Outlook	Rating Action
Term loans	-	-	July 2023	INR7,500 (increased from INR 7,182.4)	IND A+/Stable	Upgraded
Fund-based working capital facilities*	-	-	-	INR1,500	IND A+/Stable/IND A1+	Upgraded
Commercial paper (CP)#	-	-	-	INR1,000	IND A1+	Upgraded

* Working capital facilities are sub-limit of term loan
# CP to be carved out from the existing working capital facility

KEY RATING DRIVERS

Reduced Support to SPVs: The upgrade reflects Ind-Ra's expectation of a reduction in support extended by PML to its special purpose vehicles (SPVs)/subsidiaries, given the majority of its SPVs are likely to report positive cash flows, thereby benefitting liquidity and credit metrics at a standalone level. Although PML does not guarantee debt taken at the SPV level, the parent has been consistently providing support to the SPVs over the past few years by extending loans and advances. However, cash generation for the SPVs is expected to improve resulting in a minimal-to-no cash support from the parent.

The better performance of SPVs is attributed to improved occupancy and higher rentals at most malls, refinancing of debt of certain SPVs with long tenor loans at relatively lower interest rates, and completion of a commercial building (Art Guild House, Mumbai) and two residential projects (Crest, Chennai and One Bangalore West Phase 1) leading to increased earnings. Occupancy at Phoenix Market City Malls in Pune, Chennai, Mumbai and Bangalore was 90% or above in FY17. Moreover, post rebranding, average rent per room at St. Regis hotel in Mumbai improved to INR10,594 in FY17 (FY16: INR9,284, FY15: INR8,199).

As of March 2017, PML's combined loans and debentures extended to SPVs declined to INR10,084 million (including INR1,268 million of loans and INR8,816 million of optionally fully convertible debentures) from INR11,159 million as of March 2016 (INR7,377 million and INR3,782 million). The company expects to receive repayments on certain loans from cash surplus SPVs in FY18, and plans to utilise the same to increase equity stakes in partially owned SPVs.

Strong Standalone Operating Performance: The operating performance of High Street Phoenix (HSP) and Palladium mall remained strong in FY17, driven by a healthy growth in consumption (up 5% in FY17) and higher rentals (up 8% yoy to INR311 per sf per month). Standalone revenue grew 6% yoy to INR3,759 million in FY17 and EBITDA margin remained strong at 67.5% (FY16: 67.2%). Occupancy levels at HSP and Palladium malls stood healthy at 92% in FY17 (FY16: 92%) on the back of continued growth in consumption. Consumption and rental growth have been to a large extent supported by a continuous improvement in retailer mix at the mall with large international brands such as H&M, Longchamp, Coach, TOD's, replacing domestic brands. Also, other brands like Massimo Dutti, Mango, GAP, Forever New and TBZ are being added this year.

Robust Operating Cash Flows: PML's operating cash flows have remained strong historically on the back of well-diversified client mix (257 tenants as on June 2017, including under fit-outs), favourable location of the mall in an area where there are no competing malls and strong consumption growth. Standalone fund from operations and cash flow from operations margins in FY17 stood at 47% (FY16: 54.5%) and 40% (58.9%), respectively, although some decline was attributed to lower interest income. Furthermore, strong cash flow visibility is indicated by the average lease tenure of 59 months and average lock-in period of 36 months. About a quarter of the tenants also have revenue sharing agreements with an average share of 8%-10%.

Consistent Cash Outflows for Share Purchases: PML incurred significant cash outflows for the purchase of shares in its SPVs from private investors over the last four to five years (INR11 billion until March 2017). Although the company increased its equity investment in subsidiaries by around INR1,171 million in FY17 (FY16: INR 3,424 million), it was largely funded by loan repayments of similar amount from the SPVs. Further, the planned equity purchases of INR2,550 million in FY18 will also be largely funded by inter-company loan repayments by the subsidiaries/SPVs to PML.

Expansion of Retail Portfolio: The company is exploring to acquire lucrative land parcels and existing malls in operations, which are being run sub-optimally. In April 2017, Canada Pension Plan Investment Board signed an agreement with PML to acquire 49% stake in PML's subsidiary, Island Star Mall Developers Private Limited (ISML) for about INR16 billion. The Canada Pension Plan Investment Board has already invested first tranche of INR7.2 billion for a 30% stake in ISML. ISML announced acquisition of a land parcel in Pune for INR1,610 million in August 2017. The acquired land has a development potential of 1.6 million sf, of which approximately 1 million sf is planned as retail development.

Moderate Credit Metrics: Although PML's standalone operating profits have continued to increase, significant investments in the SPVs (INR25 billion, equalling 74% of standalone total assets) in the form of equity, loans and debentures leads to moderate leverage metrics. In FY17, standalone net leverage (total adjusted net debt/operating EBITDA) slightly improved to 2.9x (FY16: 3.1x), and gross interest coverage (EBITDA/gross interest expense) was moderate at 3.1x (3.5x).

RATING SENSITIVITIES

Positive: An improvement in the standalone credit profile and a substantial improvement in the credit profile of the SPVs will lead to a positive rating action.

Negative: Standalone net leverage exceeding 3x on a sustained basis or an increase in support to the SPVs will lead to a negative rating action.

COMPANY PROFILE

PML is a leading retail mall developer and operator in India with a presence across major metros. The group has a portfolio of eight malls, five commercial buildings, two hotels and three residential projects. The standalone entity operates HSP and Palladium malls and Phoenix House commercial building, while the remaining assets are housed in various SPVs/subsidiaries.

FINANCIAL SUMMARY (STANDALONE)

Particulars	FY17	FY16
Revenue (INR million)	3,759	3,558
EBITDA (INR million)	2,538	2,538
EBITDA margin (%)	67.5%	67.2%
Interest coverage (x)	3.1	3.5
Net leverage (x)	2.9	3.1
Source: PML, Ind-Ra		

RATING HISTORY

Instrument Type	Current Rating/Outlook	Historical Rating/Outlook

	Rating Type	Rated Limits (million)	Rating	10 June 2016	8 March 2016	1 December 2014
Issuer rating	Long-term	-	IND A+/Stable	IND A/Stable	IND A/Stable	IND A/Stable
Term loan	Long-term	INR7,500	IND A+/Stable	IND A/Stable	IND A/Stable	IND A
Fund-based working capital facilities	Long-term/Short-term	INR1,500	IND A+/Stable/IND A1+	IND A/Stable/IND A1	IND A/Stable/IND A1	IND A/IND A1
Commercial paper	Short-term	INR1,000	IND A1+	IND A1	IND A1	IND A1

COMPLEXITY LEVEL OF INSTRUMENTS

For details on the complexity level of the instruments, please visit https://www.indiaratings.co.in/complexity-indicators.

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Applicable Criteria

Corporate Rating Methodology

Analyst Names

Primary Analyst

Mahaveer Jain

Associate Director
India Ratings and Research Pvt Ltd Wockhardt Towers, 4th floor, West Wing Plot C-2, G Block. Bandra Kurla Complex Bandra (East), Mumbai 400051
+91 22 40001768

Secondary Analyst

Ashoo Mishra

Associate Director
+91 22 40001772

Committee Chairperson

Abhash Sharma

Director
+91 22 40001778

Media Relation

Mihir Mukherjee

Manager Corporate Communications and Investor Relations
+91 22 40356121