Smartworks Coworking Spaces Private Limited

November 10, 2023

Facilities/Instruments	Amount (₹ crore)	Rating[1]	Rating Action
Long-term bank facilities	395.00 (Enhanced from 72.00)	CARE BBB+; Stable	Reaffirmed

Details of instruments/facilities in Annexure-1.

Rationale and key rating drivers

The rating assigned to the bank facilities of Smartworks Coworking Spaces Private Limited (SCSPL) continues to derive comfort from its strong presence in flexi fully serviced workspace platform marked by PAN India existence, and strong and reputed investors. The rating also derives comfort from diversified tenants' profile leading to low tenant concentration risk, continuous increase in seat availability along with high occupancy levels and presence of escrow mechanism and debt service reserve account (DSRA). The rating also factors in the proposed infusion of equity of around ₹100 crore in FY24 from the existing and new investors.

The rating strengths are, however, restricted by continuous accounting losses in the past resulting in leveraged capital structure, sizeable expansion plans in pipeline leading to market risk, and moderate cash coverage ratio (CCR). The rating strengths are also constrained by the risk of non-renewal of lease after expiry of lock-in-period leading to occupancy risk, exposure to macro-economic scenario and cyclicality associated with competitive real estate industry.

Rating sensitivities: Factors likely to lead to rating actions

Positive factors

- Improvement in the occupancy level above 90% resulting in improvement in CCR and liquidity position on a sustained basis.
- Increase in the rental income over ₹1,100 crore while generating cash profits on a sustained basis.

Negative factors

- Non-renewal of lease contracts leading to decline in the occupancy levels below 70% on a sustained basis resulting in moderation in the liquidity profile.
- Decline in free cash and cash equivalents below ₹30 crore on a sustained basis.
- Un-envisaged debt-laden capex and consequent weakening of CCR on a sustained basis.
- Significant impact on the business risk profile or financial risk profile on account of unforeseen contingent liabilities arising from pending litigations against the promoter/s or the company.

Analytical approach: Standalone

Outlook: Stable

The 'Stable' outlook assigned to the long-term rating is based on the ability of the company to maintain its market position in flexi fully serviced workspace segment and consequent sustenance of high occupancy level coupled with envisaged increase in the scale of operations and improvement in profitability levels.

Detailed description of the key rating drivers

Key strengths

Strong presence in flexi fully serviced workspace platform marked by PAN India existence

SCSPL is one of the largest flexible workspace platforms in India with operational workspace of around 70 lakh square feet (lsf) in 12 cities across 40 centres with over 500 customers. SCSPL offers flexibility to its clients for setting up office spaces

[1]Complete definition of the ratings assigned are available at www.careedge.in and other CARE Ratings Ltd.'s publications

with minimal capex requirement along with quick turnaround time of under 45 to 60 days as compared with 6-9 months for traditional office spaces. SCSPL has the benefit of PAN India presence which helps it to diversify the geographical concentration risk and also adds to the benefits extended to multi city clients. It has sharply scaled up its operations over the last five financial years while establishing a diversified clientele base. Reputed and growing customer base, along with unique product offering, services and facilities are expected to support healthy growth in operating revenues and margins over the medium term.

Strong and reputed investors

The company was promoted by National Capital Region (NCR)-based Neetish Sarda and Harsh Binani. Neetish Sarda, a Purdue University and SIM alumni, has past real estate experience, whereas Harsh Binani, a Shri Ram College of commerce graduate and Kellogg School of Management alumni, has worked for 5 years with McKinsey Chicago Office. They are supported by an experienced team of professionals. Besides this, the promoters have secured funding from Keppel Land (Temasek-backed Singapore-based urban solutions and real estate developer) and Deutsche Bank. Association with reputed investors improves the financial flexibility and market visibility of the company.

Diversified tenants' profile leading to low tenant concentration risk

The operations of the company are spread across 40 centres with over 500 clients, which provides healthy revenue diversity as top-25 tenants contributes only around 32% to the total rental income and thereby minimises business risk. Moreover, the company caters to mid-size and enterprise clients only with an average lock-in period of around two years, which ensures cash flow stability and revenue visibility in the near to medium term. This is further supported by geographical diversity with presence across 12 cities.

Continuous improvement in occupancy level and seat availability

The total seats available for lease have increased by 2.88x in FY23 over FY21. Nonetheless, despite an increase in seats available for leasing, occupancy levels have also improved over the years to 76% in FY23 from 60% in FY21 on the back of brand visibility, good quality of service and efficient marketing strategies which enabled the company to witness quicker tenant acquisition. Moreover, during H1FY24, the occupancy levels further increased to around 80% and are expected to go above 90% by the end of FY24.

Presence of escrow mechanism and DSRA

The company is maintaining escrow accounts for routing the lease rents of specified tenants before transferring the surplus, i.e., after paying equated monthly instalment (EMI), to current account for general usages. Also, the company is maintaining DSRA equal to 3-months EMI in the form of fixed deposits with lenders which provides a cushion to the liquidity position of the company.

Key weaknesses

Continuous accounting losses in the past resulting in leveraged capital structure

The capital structure of the company witnessed moderation over the last three financial years due to erosion of net worth, as the company continued to incur losses (mainly due to accounting treatment of leases as per accounting standards), coupled with increase in the total debt levels to support the enhanced scale of operation. This apart, the increase in total debt was also attributable to the increase in liability on account of finance leases. Nonetheless, the company continued to generate positive cash accruals in the last three financial years. Going forward, the capital structure of the company is expected to improve in the medium term owing to expected book profits, on the back of improved occupancies and revenues, adding to the net worth of the company along with expected infusion of funds by the promoters and investors of around ₹100 crore in FY24.

Sizeable expansion plans in pipeline leading to market risk

The company has proposed to expand its capacity by around 65% over the next five years through a mix of debt and equity/internal accruals. The proposed capex will be funded out of debt of around ₹350 crore and the remaining will be funded from equity/internal accruals. However, the proposed capex is modular in nature and the same can be changed/ shifted with a change in the business environment at minimal cost. Thus, it reduces the business risk to some extent. Nonetheless, the impact of capex on profitability and capital structure will be key rating monitorable.

Moderate cash coverage ratio

The cash coverage of lease rental discounting (LRD) debts of the company is moderate with CCR ranging between 1.5x and 2x as average equated monthly instalment (EMI) to escrowed rental ratio stood at around 55%. Going forward, the same is expected to remain range bound in near to medium term. In addition to the cash coverage through escrowed rentals, the company provides DSRA covering three months of repayment obligations which mitigates the moderate CCR risk to a certain extent.

Risk of non-renewal of lease after lock-in period

The lease agreements with tenants generally have tenure of three to four years with an average minimum lock-in period of two years. Hence, there is a risk pertaining to the tenants exiting out of the agreement after the end of the minimum lock-in period. However, such risk is mitigated to a certain extent as the lessees occupying the space are renowned entities coupled with high retention levels of tenants experienced in the past.
This apart, SCSPL has long-term lease agreement with its landlords of around 5 to 10 years with lock-in period of three years.

Exposed to macro-economic scenario and cyclicality associated with competitive real estate industry

Lease rentals are susceptible to macro-economic scenario like slowdown, high inflation, high interest rate and vulnerability to external events such as the COVID-19 pandemic, which constrains the tenant's business risk profile and therefore might affect the occupancy and rental rates of SCSPL. Also, the arrival of competing capacities in the vicinity could cannibalise tenants or rental rates. The company is also exposed to cyclicality in the commercial real estate sector.

Liquidity: Adequate

The liquidity position of the company is expected to remain adequate over the near to medium term as projected cash inflows are expected to be sufficient to meet the debt repayment obligations in FY24 and FY25, respectively. The liquidity position also draws comfort from escrow mechanism along with DSRA covering three months of repayment obligations; supported by free cash and cash equivalents of around ₹118 crore as on March 31, 2023. Also, the promoters are planning to raise equity of around ₹100 crore through a mix of existing and new investors during FY24, which will add further comfort to the liquidity position of the company and are also expected to remain adequate to meet the equity portion of proposed capex plan apart from debt.

Applicable criteria

Policy on default recognition
Financial Ratios – Non-financial Sector
Liquidity Analysis of Non-financial sector entities
Rating Outlook and Credit Watch
Rating methodology for Debt backed by lease rentals
Policy on Withdrawal of Ratings

About the company and industry

Industry classification

Macro-economic Indicator	Sector	Industry	Basic Industry
Consumer discretionary	Realty	Realty	Real estate related services

SCSPL was started in 2016 by NCR-based Neetish Sarda (promoter) and Harsh Binani (promoter). The company is engaged in flexi-fully serviced workspace leasing business, with PAN India presence having total leasable areas of around 70 lsf. The day-to-day operations of the company are managed by Harsh Binani and Neetish Sarda, supported by a team of experienced professionals.

Other notable investors include Keppel Land (Temasek-backed Singapore urban solutions and real estate developer) and Deutsche Bank.

Brief Financials (₹ crore)	March 31, 2022 (A)	March 31, 2023 (A)
Total operating income	360.24	709.95
PBILDT	211.54	431.28
PAT	-69.74	-99.79
Overall gearing (times)	NM	NM
Interest coverage (times)	1.73	1.82

A: Audited; NM: Not meaningful; Note: 'the above results are latest financial results available'

Status of non-cooperation with previous CRA: Not applicable

Any other information: Not applicable

Rating history for last three years: Please refer Annexure-2

Covenants of rated instrument / facility: Detailed explanation of covenants of the rated instruments/facilities is given in Annexure-3

Complexity level of various instruments rated: Annexure-4

Lender details: Annexure-5

Annexure-1: Details of instruments/facilities

Name of the Instrument	ISIN	Date of Issuance (DD-MM-YYYY)	Coupon Rate (%)	Maturity Date (DD-MM-YYYY)	Size of the Issue (₹ crore)	Rating Assigned along with Rating Outlook
Fund-based - LT-Term loan	-	-	-	July, 2030	395.00	CARE BBB+; Stable

Annexure-2: Rating history for the last three years

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating History			
		Type	Amount Outstanding (₹ crore)	Rating	Date(s) and Rating(s) assigned in 2023-2024	Date(s) and Rating(s) assigned in 2022-2023	Date(s) and Rating(s) assigned in 2021-2022	Date(s) and Rating(s) assigned in 2020-2021
1	Fund-based - LT-Term Loan	LT*	395.00	CARE BBB+; Stable	1)CARE BBB+; Stable (20-Oct-23)	-	-	-

*Long term

Annexure-3: Detailed explanation of the covenants of the rated instruments/facilities: Not applicable

Annexure-4: Complexity level of the various instruments rated

Sr. No.	Name of the Instrument	Complexity Level
1	Fund-based - LT-Term Loan	Simple

Annexure-5: Lender details

To view the lender wise details of bank facilities please click here

Note on the complexity levels of the rated instruments: CARE Ratings has classified instruments rated by it on the basis of complexity. Investors/market intermediaries/regulators or others are welcome to write to care@careedge.in for any clarifications.

Contact us

Media Contact	**Analytical Contacts**
Mradul Mishra Director **CARE Ratings Limited** Phone: +91-22-6754 3596 E-mail: mradul.mishra@careedge.in	Arindam Saha Director **CARE Ratings Limited** Phone: + 91-033- 40181631 E-mail: arindam.saha@careedge.in
Relationship Contact Pradeep Kumar V Senior Director **CARE Ratings Limited** Phone: 91 44 2850 1001 E-mail: pradeep.kumar@careedge.in	Gopal Pansari Assistant Director **CARE Ratings Limited** Phone: + 91-033- 40181647 E-mail: gopal.pansari@careedge.in Vikash Kumar Rai Lead Analyst **CARE Ratings Limited** E-mail: vikashkumar.rai@careedge.in

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