

Steady set of numbers; Outlook positive!

Embassy Office Parks REIT delivered a steady set of numbers for Q3FY21; company's Q3FY21 revenue grew by 4% to Rs 565 cr and Net Operating Income (NoI) was reported at Rs 478 cr (up 3% YoY) and has declared a distribution Rs 431.3 cr. which translates into dividend of Rs 4.55 per unit. The rental collections remained robust at 99.5% for 3QFY21 continuing from 99.9% collections in Q2FY21 and 100% for Q1FY21. The company has signed deals for 311,000 sqft in Q3 taking total lease deals signing at 1 mn sq.ft.; company achieved 13% spreads on 203,000 sq. ft leased and 15% rental increase on 1.5 mn sqft in Q3FY21. The company completed acquisition of Embassy Tech Village (ETV) worth Rs 9782 cr in Dec.2020 and successfully raised Rs 3685 cr through institutional placements to fund the acquisition.

Although the office Real Estate markets were badly hit by the pandemic, the portfolio of Embassy Office Parks remains relatively unaffected due to top class clientele comprising Technology companies, MNCs (43% technology and 48% Fortune 500 companies) etc. Moreover, the rentals at Embassy office parks are at discount to the prevailing market rate indicating scope for hike in rentals. The confidence arises from the fact that the company has achieved rental increases of ~13% on 5.3 mnsf YTD and rent collection is more than 99% so far. Company reported Net distributable cash flow (NDCF) of Rs 431 cr (Rs 4.55 per unit) which represented 100% payout ratio at REIT level (break-up: Rs 2.03 as interest, Rs 2.5 as amortization of SPV level debt and Rs 0.02 as dividend). The record date for the distribution would be Feb. 22, 2021. **We recommend HOLD with a DCF based target price of Rs 376 (7% upside).**

Key Highlights

- Company collected 99.5% of Q3FY21 office rentals continuing from 99.9% collections in Q2FY21 and 100% for Q1FY21; maintained healthy occupancy of ~90.6% on enlarged portfolio of 32.3 mnsf operating occupancy portfolio with same store occupancy of 90.5%.
- In this quarter, the company has undertaken organic growth through 5.7 mnsf on campus development out of which 1.9 mnsf is pre-committed to JP Morgan. The company also launched 1.9 mn sf of new on campus development at ETV, integrated 1.1 mnsf JP Morgan built to suit project slated to be completed by Sept.'21 and the construction activities are continuing at good pace on existing 2.7 mnsf development.
- Company signed leases for 311,000 sft across 11 deal during Q3FY21; the company achieved 14% spread on 206,000 sqft re-leased in Q3 and rental increases of 15% on 1.5 mnsqft across 24 office leases with YTD rental increases of 13% on 5.3 mn sqft across 66 office leases.

Outlook and Valuation

REITs are quasi equity instruments distributing minimum 90% of Net distributable cash flows (NDCF) amongst its unit holders. Hence, it should be looked up as more of dividend play in short term and capital appreciation in long run. Despite the uncertainty associated with the office space market, we continue to have positive outlook on the segment with Embassy REIT as a good investment as it is better placed amongst its peers given the quality and sticky nature of its clientele, and location of the properties. The uncertainty associated with Real Estate sector, if any, would benefit the well funded developers like Embassy leading to consolidation in the sector. Despite the turbulence, quality properties both in terms of location and management would be preferred destinations for the long term tenants. **We are of the opinion that Embassy REIT would be in position to ride the current turbulence and hence recommend HOLD on Embassy REIT with a target price of Rs 376 arrived using DCF valuations; at CMP, the dividend yield is at around 7%.**

Key Financials (Consolidated)

(Rs. Cr)	2020	2021E	2022E
Net Sales	2145	2399	3202
NOI	1817	2048	2533
EBITDA	1,666	1,884	2,485
EPS (Rs.)	10	10	11
RoE (%)	3.3	4.2	4.8
D/E	0.4	0.4	0.4
PER (x)	35.1	36.0	33.2
Distribution Yield (%)	7.0%	5.6%	6.9%

Source: Company, Axis Research

(CMP as of Feb. 12, 2021)	
CMP (Rs)	350
Upside /(Downside (%))	7%
High/Low (Rs)	518/301
Market cap (Cr)	33,200
Avg. daily vol. (6m) Shrs.	6,68,180
No. of shares (Cr)	94.0

Shareholding (%)

	Jun-20	Sept.-20	Dec.-20
Promoter	61.57	61.57	61.57
FII/FPIs	26.00	26.00	26.00
MFs / UTI	1.58	1.58	1.58
Banks / FIs	0.11	0.11	0.11
Public	10.74	10.74	10.74

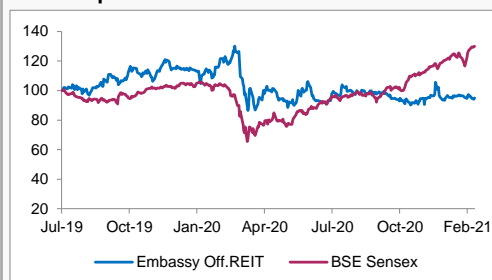
Financial & Valuations

Y/E Mar (Rs. Cr)	FY20	FY21E	FY22E
Net Sales	2145	2399	3202
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Change in Estimates (%)

Y/E Mar	FY21E	FY22E
NOI	5.5	15.9
EBITDA	4.4	24.6
Ad. Profit	(3.9)	(2.0)

Relative performance



Source: Capitaline, Axis Securities

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Key Highlights:

- **Outlook:** Near and medium term challenges to commercial real estate industry do persists; but Emabssy REIT has delivered so far. The Embassy REIT management expects its business to be little impacted in the medium term on account of strong occupier portfolio which include 43% technology and 48% Fortune 500 companies while the businesses affected by pandemic contribute roughly 5% of the revenue pool. Given the brand image, property location and promoter pedigree, the company would be able to sail through the turbulent waters and emerge winner.
- **Acquisition:** Company has successfully undertaken acquisition of Embassy Tech village assets for Rs 9782.4 cr. located at ORR, Bengaluru. The deal has been financed through institutional placements (11.134 cr units ate Rs 331 per unit) thereby raising Rs 3685 cr, preferential allotment of 6.489 cr units at Rs 356.7 per unit to third party raising Rs 2315 cr., Rs 2600 cr through listed debt at coupon rate of 6.4% paid quarterly and roll-over of Rs 1200 cr (approx.) in-place debt.
- **Hotel:** Though the 477 key hotels has reopened in mid June 2020, it attracts low occupancy on account of covid-19 related travel restrictions. The company has instituted significant cost saving measures to reduce fixed/ variable costs and global safety protocols have been implemented for guests which would help ramping up occupancy as and when travel restrictions are lifted. Hospitality demand is expected to remain muted till FY22 given COVID-19 related travel disruptions. Slowdown in hospitality segment would have limited impact on company's financials as it contributed <1% of pre-covid Nol in FY20.
- **Demand side dynamics:** CBRE has noted considerable shrinkage of over 23% in supply of office space in CY20 and expect it to recover modestly in as the demand rebounds on H2CY21. With vaccine roll-out and return to work by occupiers, the demand is expected to rebound by H2CY21. Grade A stock, which includes Embassy, to remain resilient given occupier and asset quality coupled with robust rent collections. Quality properties like Embassy REIT could benefit from the supply shrinkage along with increased offshoring and technology spends and preference to high quality, wellness oriented properties supported by adequate maintenance services. Moreover, office demand in India is well placed for 2021 and beyond given the talent pool, cost advantages and depreciating INR.
- **Supply side dynamics:** CBRE's 2-year forward supply estimate has decreased from 119 mnsf in Jan'20 to 92 mnsf in Jan'21, a 23% decline in 4 quarters. Supply is likely to recover modestly when demand rebounds in H2 CY2021; Institutional landlords to deliver smarter buildings in sync with changing market dynamics

Result Update (Consolidated)
(Rs Cr)

(Rs.Cr.)	Quarterly Performance				
	Q3FY21	Q3FY20	% Change (YoY)	Q2FY21	% Change (QoQ)
Revenue from Operations	565	546	4	540	5
Other Income	0.0	0.0	NA	0.0	NA
Total Income	565	546	4	540	5
Total Expenditure					
Maintaining and Operating Expense	62	49	27	34	84
Employee Expenses	6	10	(45)	5	9
Various Fees and Valuation charges	17	33	(49)	26	
Other Expenses	29	30	(6)	25	
Total Expenditure	113	122	(7)	90	25
EBIDTA	452	424	7	450	1
EBITDA Margin	80%	78%		83%	
Other Income (Includes MI)	57	47	22	48	20
Interest	136	94	44	144	NA
Depreciation	136	118	15	119	14
Exceptional Item	0	0	NA	0	NA
PBT	238	258	(8)	234	1
Tax	23	5	377	2	1095
PAT	215	253	(15)	233	(8)

Source: Company, Axis Securities

Financials (CONSOLIDATED)
Profit & Loss

(Rs Cr)

Y/E March	FY20	FY21E	FY22E
Revenue	2,145	2,399	3,202
Total income	2,145	2,399	3,202
Operating Expenses	479	516	717
EBITDA	1,666	1,884	2,485
EBITDA Margin (%)	77.7%	78.5%	77.6%
Depreciation	528	526	557
Interest & Fin Chg.	380	613	588
Other Income	99	88	-62
Exceptional Income	-178	0	0
Pre-tax profit	679	833	1,279
Tax provision	30	50	196
Associates	117	132	-93
Other Comprehensive Income	0.0	0.0	0.0
PAT	766	915	990

Source: Company, Axis Securities

Balance Sheet

(Rs Cr)

Y/E March	FY20	FY21E	FY22E
Total Assets	33,490	36,584	36,316
Net Block	21,477.5	27,809.4	27,514.7
CWIP	233.4	64.0	132.0
Investments	1,824.9	1,451.6	1,117.3
Cash / Bank balance	324.9	(2,699.3)	(2,574.5)
LT L&A	185.7	185.7	185.7
Other Current and Non Current Assets	9,443.7	9,772.2	9,940.4
Total Liabilities & Equity	33,490	36,584	36,316
Equity capital	22,912.1	22,912.1	22,912.1
Reserves	-594	-1,522	-2,811
Pref. Share Capital	0.0	0.0	0.0
Current Liabilities	1,164	1,169	1,535
Borrowings	5,968	8,832	9,392
Def tax Liabilities	4,040.7	5,192.2	5,287.2

Source: Company, Axis Securities

Cash Flow		(Rs Cr)		
Y/E March	FY20	FY21E	FY22E	
Profit before income tax	679	965	1,186	
Depreciation and amortisation expense	528	526	557	
Net change in Working Capital	154	336	545	
Income taxes paid, net	(142.9)	(49.9)	(195.7)	
Cash flows from operating activities	1,691.5	2,258.2	2,772.3	
Capex	-2,056	-5,690	-340	
Cash flow from investing activities	-2,144	-5,690	-340	
Equity Issued/(Bought back)	-238	0	0	
Debt Raised/(Repaid)	-2,452	2,864	560	
Dividends Paid	(1,352.7)	(1,842.9)	(2,279.8)	
Cash flow from financing activities	(4,197.4)	407.9	(2,307.2)	
Net increase/ (decrease) in cash and cash equivalents	(4,650.1)	(3,024.2)	124.8	

Source: Company, Axis Securities

Ratio Analysis		(%)		
Y/E March	FY20	FY21E	FY22E	
Revenue Growth	14.3	11.9	33.5	
OPM	77.7	78.5	77.6	
Oper. profit growth	22.5	13.1	31.9	
Operating Expenses / Net sales	22.3	21.5	22.4	
Depreciation / G. block	2.5	1.9	2.0	
Effective interest rate	6.0	8.7	6.7	
EBITDA Margin (%)	77.7	78.5	77.6	
Debt/Equity (x)	0.37	0.37	0.39	
Interest Coverage (x)	4.4	3.1	4.2	
Debt / equity (x)	0.37	0.37	0.39	
Effective tax rate	3.8	5.2	16.5	
Distribution Per Share (Rs.)	17.7	19.6	24.3	

Source: Company, Axis Securities

About the analyst**Analyst:** Pankaj Bobade**Contact Details:** pankaj.bobade@axissecurities.in**Sector:** Metals, Auto, Auto ancillary**Analyst Bio:** BE (Met.), CFA (ICFAI) with 12 years of Research Experience in Metals, Auto, Auto ancillary**Disclosures:**

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