

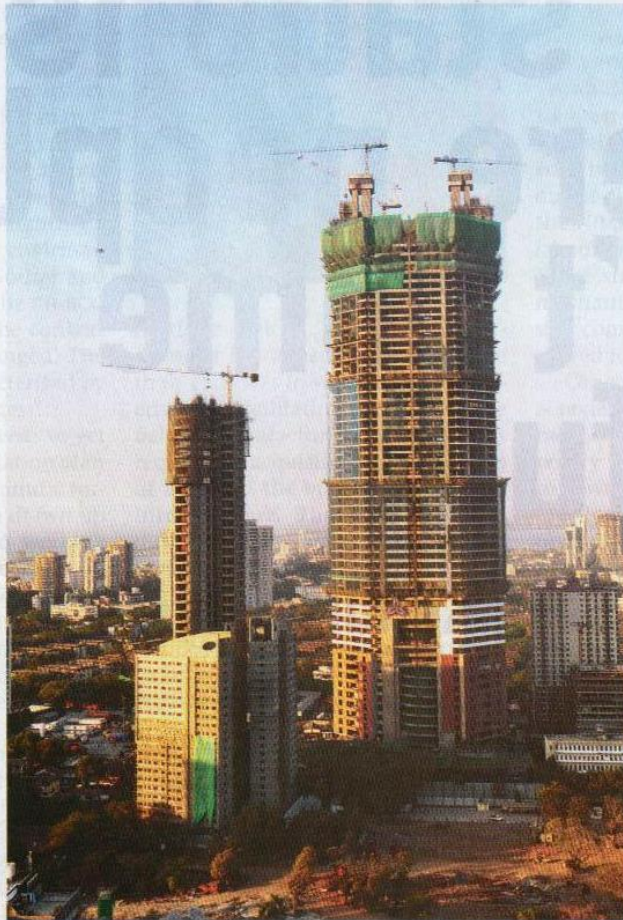
Waiting for a growth trigger

The real estate sector is currently passing through one of its most trying phases. While property sales across cities have slowed down considerably, buyers are cautious in the wake of unfavourable economic condition. Even as developers are struggling with the liquidity crisis due to weakening cash flows, the increasing cost of construction has hit hard on their bottomline. Further, most of the funding options have dried up, making it really tough for the builders faced with high level of debts. Inventory of unsold properties has gone much above the comfort level.

Mumbai, where residential sales volume has fallen by around 40 per cent, is now saddled with an inventory of as high as 48 months, whereas National Capital Region (NCR) is struggling with an unsold stock of over 28 months. Both these prime markets are hard pressed to deal with the oversupply situation.

"Almost all economic indicators are in the negative zone and that has taken its toll on the real estate market as well," says Anshuman Magazine, chairman & managing director, CBRE South Asia. "The sector is at present confronted with multiple challenges. While buyers prefer to wait and watch, developers are trying hard to reduce their inventories in a rough market condition."

"Like any other industry, real estate is also an integral part of our economy and any downturn on that front will have its direct impact on



SANJAY BORADE

The property market is at a crossroads, with economic uncertainties looming large

the real estate sector," argues J.C. Sharma, vice-chairman & managing director, Sobha Developers. "Macroeconomic headwinds have affected both supply and demand side in a major way. Overall outlook in the short term is not so encouraging, even if the industry is trying to cope up with the challenges."

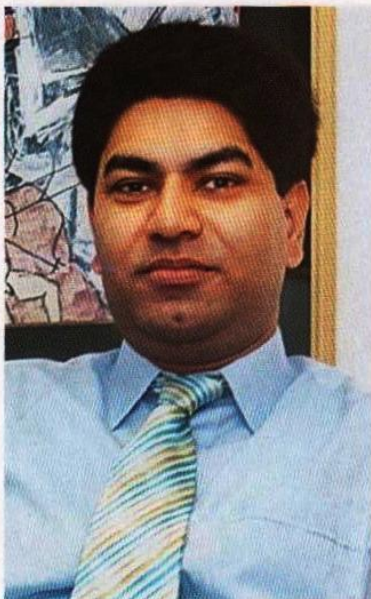
"The condition is definitely complex," explains Sanjay Dutt, executive managing director, south Asia, Cushman & Wakefield. "Economic uncertainties have forced the buyers

to go slow. For developers shrinking cash flows is a matter of big concern. Limited funding avenues and hardening of interest rates have resulted into higher cost of funds for developers. The worst part is that this stressful period is not likely to be over in a hurry." However the market is still not seeing large price cuts by developers – yet.

The slowing economy has adversely impacted demand and this has resulted in a much higher level of inventories across all markets. According to international property consultant Knight Frank, in Mumbai, nearly 290,000 residential units are under construction, while unsold inventory levels are close to 130,000 units that include ready as well as under-construction properties. This has happened despite the fact that new launches in the city have plummeted almost 40 per cent in the last two years. The absorption level in the commercial capital during January-September

2013 has dropped to 26 per cent, as against the corresponding period last year and more than 43 per cent from the peak level of 2010.

Though the number of under-construction units in NCR is twice that in Mumbai, the unsold inventory level in case of former is at 26 per cent. In Bangalore, the level at present is about 35 per cent. In the given condition, the stress is so much that Mumbai requires nearly nine quarters to clear its unsold inventory, while Bangalore and NCR need



SURESH SAMINLEY

markets, Bangalore has been quite steady, while Chennai is a dark horse, as it has maintained good momentum," says Rohit Kumar, head, research, DTZ. "This is primarily because both these markets are end-user-driven, unlike NCR and Mumbai, where investors are involved in substantial volume of sales." Adds Samantak Das, chief economist & director, research, Knight Frank India: "In NCR and Mumbai, investors have been playing a big role and, during any downturn, they are the ones who leave the markets first. Currently, these two markets are facing the maximum brunt."

Slowdown continues

The commercial office space, hit harder than residential, has continued to languish even after more than two years of downward trend. According to CBRE, in the first half of 2013, the total net absorption across top eight cities including Mumbai, NCR, Bangalore and Chennai stood at 10.9 million sq ft, implying a decline of 15 per cent over the same period last year. Fresh supply during H1FY13 also fell by 3 per cent and was recorded at 17.6 million sq ft.



Dutt: the condition is complex

Vacancy rates at the end of Q2FY13 were noted at 19.6 per cent – an increase of 1.7 percentage point over the same period last year. "Overall, corporates are cautious and are trying to rationalise their real estate cost due to current situation of lower growth prospects on global as well as domestic front," says Ashok Kumar, managing director, Cresa Partners. "Delay in expansion plans by corporates is clearly visible in most sectors and, hence, the requirement of new space is limited." Ambar Maheshwari, managing director, corporate finance, Jones Lang LaSalle says, "The worrying part is that, after over two years of downturn in commercial sector, the residential market has also been experiencing a distinct contraction for the last six-eight months. In fact, there is hardly any respite for the market," adds he.

Both capital values in the residential segment, as well as rental values for commercial space continue to be under pressure in all major markets. The oversupply situation in the back of weak demand position has put a cap on price appreciation. On the demand side, buyers are postponing their purchases on account of uncertain economic climate. Higher mortgage rates have only added to their

Magazine: in negative zone

around six quarters. Other markets like Chennai, Hyderabad, Kolkata and Pune too are faced with higher inventories. However, experts are of the view that the southern markets are better placed than their counterparts in the north. "Out of all the

Property rates

(Rs/sq feet)	Residential	Commercial
Mumbai		
Grade A	16,000-69,000	18,000-27,000
Grade B	8,500-18,000	7,000-14,000
Bangalore		
Grade A	6,500-16,000	7,000-12,000
Grade B	4,500-6,500	4,000-9,000
Delhi (NCR)		
Grade A	10,000-42,000	13,000-27,000
Grade B	4,000-11,000	4,000-12,000
Chennai		
Grade A	7,000-16,000	6,000-8,500
Grade B	3,500-7,500	3,000-5,500
Hyderabad		
Grade A	4,000-7,000	3,200-5,000
Grade B	2,700-4,200	2,500-3,500
Pune		
Grade A	6,000-14,000	4,000-8,000
Grade B	3,500-6,000	3,000-4,500
Kolkata		
Grade A	5,000-9,000	5,000-9,500
Grade B	2,500-4,500	3,000-5,000



Source: Market



Ashok: corporates are cautious

woes. Developers had huge expectations from the recent festival season, but that has also not able to bring any cheer to the market. In fact, developers feel it was one of the most lacklustre years for the property market.

All this has got a heavy bearing on the cash flow scenario for the developers, who are already saddled with higher levels of debts in their books. Cautious approach adopted by the banking system, coupled with drying up of other funding option like private equity, is only adding to their financial plight. Further, construction cost has spiralled by more than 30 per cent in the last couple of years.

"The market is currently faced with multiple challenges and there is not much to be done in the short run," says Gaurav Gupta, director, Omkar Realty. "The economy and the overall sentiment will have to look up in order to provide much needed support to the real estate sector."

On where the market is headed in the short term, experts are of the view that the current impasse will continue at least for the next six-nine months. The market is eagerly waiting for the general elections to get over, after which there could be some clarity in terms of economic progress.

"We need some sort of trigger for our economy to recover and that will have a positive impact on the real estate market, which is anxiously waiting for some positives to take place," states Lalit Kumar Jain, chairman, Confederation of Real Estate Developers Association of India, and CMD, Kumar Builders. "Improved sentiment and lowering of interest rates are required for demand to pick up going forward."

"The market is in a transition phase at present," comments Vikas Oberoi, chairman & managing director, Oberoi Realty. "There is lack of direction. Both demand and supply sides are holding on to their current levels and waiting for some sort of clarity on the political and economic front. Post-election only we can expect things to revive". Oberoi is of the view that, despite this ongoing slowdown, property prices may not see much of a correction, except for some pockets, where prices have gone up significantly high in the past.

Rise in costs

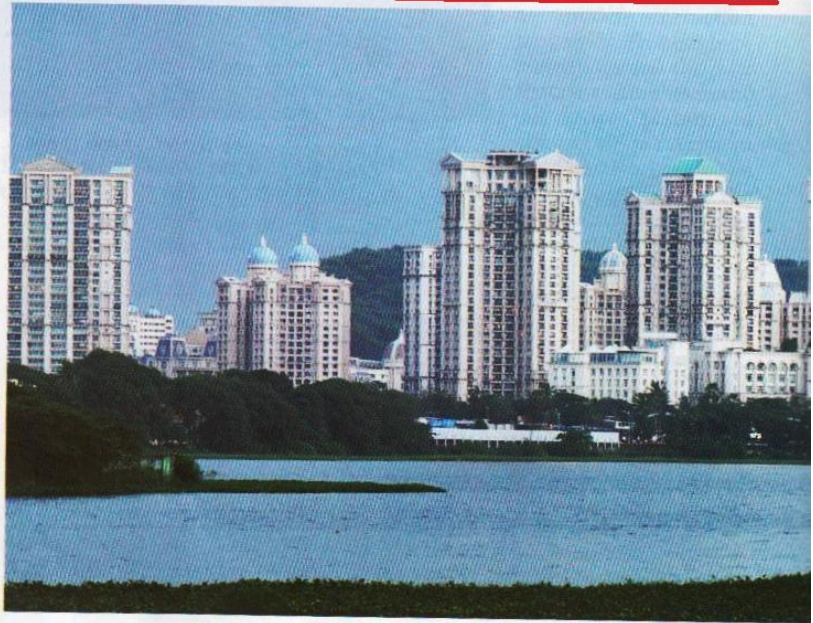
The price correction is likely to vary from 5-15 per cent depending upon the locations. Developers strongly believe that the substantial rise in



Maheshwari: hardly any respite

construction cost, owing to the increase in material and labour cost, has hardly left any scope for price reduction, though there exists an oversupply condition.

Sarang Wadhawan, vice-chairman & managing director, HDIL, however, feels that prices are unlikely to go down. "In fact, there is hardly





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Vakil: industry is learning the hard way

any room left for such correction to take place," he says. "The cost of all inputs from land to labour has gone up exponentially in recent months. Delay in approval process has only aggravated the situation."

"In the last few quarters, prices have not moved up and that itself is a sign of correction in the backdrop

of rising inflation and input cost," concurs Atul Modak, vice-president, Kohinoor Square. "Developers have tried to absorb these hikes without passing them on to the buyers."

On the supply side, builders are holding on to their current prices and trying to encourage sales by offering disguised discounts in terms of free stamp duty and registration as also waiving of floor charges and car-park charges. Additionally, innovative sales strategies, such as rent back and subvention schemes that translate into 5-15 per cent discounts, are being offered by developers in a bid to push sales, even if they have refrained from lowering the base rates, barring a few exceptions.

Despite the economic slowdown, the Bangalore market has attempted to buck the trend, backed by the demand revival in the IT/ITES sector. Prices in the residential segment have in fact escalated by 8-13 per cent in the last one year. Northern and southern micro markets in the city, however, have moved in a narrow range. Whitefield in the east and Rajajinagar in the west have witnessed price appreciation of 10-13 per cent. Other western locations like Tumkur Road and Magadi Road have also seen prices move by



PRAKASH JADHAV

Jain: waiting for some positives

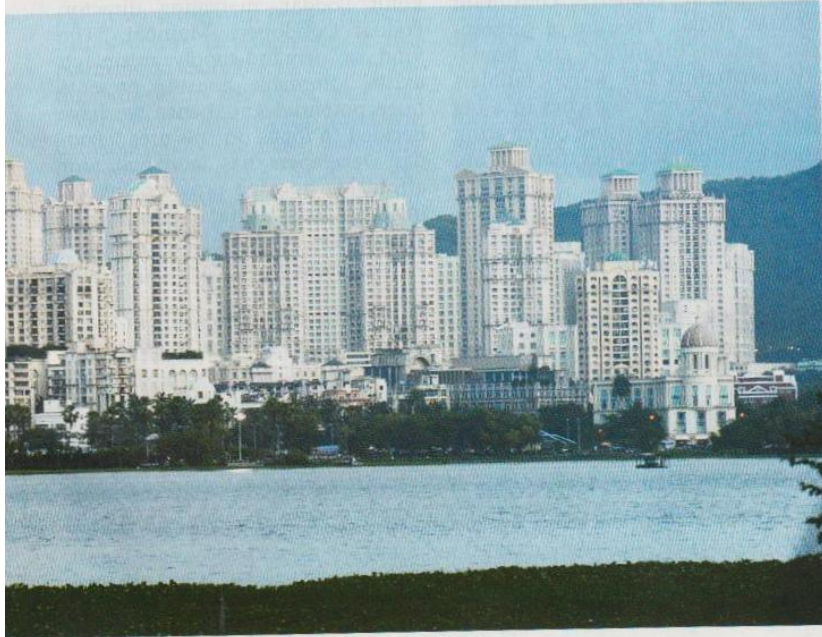
about 12 per cent, due to upcoming infrastructure projects.

"Showing resilience, the Bangalore market has exhibited a steady trend," says Ashwini Kumar, executive director & COO, Nitesh Estates. "Builders have been quick to respond to the condition and proactively revamping their offering as per market requirements. This has resulted in better absorption level for the city and its peripheral areas."

Feeling the heat

Jackbastian Nazareth, chief executive officer, Puravankara Projects, tries to explain the trend. "Bangalore is primarily an actual buyer-driven market," he says. "Unlike other cities, prices here have risen in a steady manner and, hence, property prices are reasonably priced at this juncture as well. Going forward also, we expect the market to maintain its momentum."

Within NCR and Mumbai, there are micro markets, where prices in the past went up very high and some such locations are currently feeling the heat. Both these markets in the past saw launching of a good number of high-end projects and these are the ones where developers are struggling to find buyers. In Mumbai, areas like



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Oberoi: in a transition phase

Parel, Lower Parel and Mahalaxmi are facing an oversupply situation in both commercial and residential segments. Developers are now open to negotiation. However, prices in Navi Mumbai, Thane and the peripheral suburbs of central and western Mumbai have been stable. "Peripheral locations in most cities with lower income housing," according to Abhay Kumar, managing director, Griha Pravesh Buildtech, a Navi Mumbai-based developer, "are doing relatively well and will continue to do so in future as well. Many of these locations are getting the desired support from upcoming infrastructure developments."

"Builders have so far sailed through. But in places like Mumbai, NCR and Pune, we may see in coming months some concrete efforts on

the part of developers to reduce their inventories. This will be more obvious in case of high-end projects. This may apply also to some of the upper mid segment projects also," says Kumar.

"On the residential front, the rise in interest cost and decline in net profits during 2013 will compel developers to lighten inventory load and deleverage their balance sheets," says Shishir Baijal, CMD, Knight Frank. "Demand, however, is likely to remain subdued over the initial part of 2014, as the market continues to bottom out against the backdrop of a sluggish economy."

To cope up with the slowdown, developers are changing their strategy and initiating multiple measures to ward off the difficult period. Across cities, developers have restrained themselves from launching new projects and thus are trying to contract the supply. In Mumbai, some 47,488 units were launched during January-September 2013 – a sharp 28 per cent drop from a year ago. The difference is even greater, at 42 per cent and 46 per cent, when compared with the same period in 2011 and 2010, respectively.

Huge potential

According to Sam Chopra, chairman, global property consultant RE/MAX India, "Pressure of substantial unsold inventory and liquidity constraints has forced builders to slowdown new launches in a big way. They are focussing on clearing their existing properties than adding new ones."

Besides, developers are also trying to reposition themselves in the market by realigning their portfolio.



Gupta: facing multiple challenges

After reducing their exposure to commercial properties in the last two years, now most of the developers are concentrating on mid and affordable housing where the demand continues to be intact. Further, the government is also encouraging affordable housing projects in the wake of the massive shortage.

"As a developer one has to see where the actual demand lies," says Rohit Poddar, managing director, Poddar Developers, Mumbai. "The kind of demand-supply mismatch exists, affordable housing presents huge potential and hence we have decided to focus on this area." Poddar Developers has launched four affordable housing projects, involving more than 20,000 flats in peripheral areas of Mumbai. Enthused by the response, the builder is also

Heading for the big league

The Securities and Exchange Board of India (SEBI) has recently issued draft guidelines to set up real estate investment trusts (REITs). REITs, often listed entities, on one hand present investment avenues for investors and institutions to invest in the real estate

market with much greater liquidity and transparency, and on the other hand help developers get an opportunity to monetise their revenue-generating assets. The introduction of REITs in the long term would propel the sector, spurring capital inflows and

bringing institutional credibility. SEBI's move to put in place a framework for REITs will go a long way in reviving substantial interest among domestic and global investors in India's currently subdued real estate market as it moves towards a more organised set-up. Global

investors who are risk or development averse in the Indian condition may find leased assets with least risk and better exits through REITs.

The SEBI draft regulations envisage REITs as a trust, set up under the provisions of the Indian Trusts Act 1882, even as it will not be allowed to launch any schemes. A REIT will have trustees, sponsors, managers



Sharma: downturn impact

planning to launch four more such projects in coming months.

Mumbai-based Shapoorji Pallonji, with a pan-India presence, is also changing its strategy and looking to bring down its exposure to commercial developments and focus on residential and affordable housing. The company, which is undertaking an ₹2,700-crore mega township project (20,000 apartments) in Kolkata jointly with the West Bengal Housing Infrastructure Development, is also planning to launch a series of housing projects in Bangalore, NCR and other cities. "Keeping in mind the demand-supply mismatch prevailing in the housing sector, we as a company have decided to increase our building construction portfolio in the residential segment and there too trying to build houses that can match to

and a principal valuer. A trust, once formed, will initially apply for SEBI registration and once the market regulator grants the approval, it will be allowed to offer units to the public and get the units listed, similar to an initial public offering of equity shares, albeit in a different structure. Once listed, a REIT may subsequently raise funds through follow-on

common man's affordability," states Raymond Dastur, executive vice-president, Shapoorji Pallonji.

Further, in place like Mumbai, where prices have skyrocketed and gone beyond the affordable levels, builders are now coming up with projects where flats are being offered with smaller ticket sizes. In other words, if earlier 2 BHK apartments had areas ranging 1,000-1,200 sq ft, the same are now being offered with smaller areas of 900-1,000 sq ft. "Builders are using all ways and means to push up sales with flats that can suit to buyer's affordability. This is certainly an apt move on the part of developers in the given situation," states Das.

Experts believe that the ongoing market condition is proving to be a learning curve for the industry which is now more receptive to the market changes than before. Builders are in the process of mending their ways and trying to come up with projects that can move quickly. Unlike in the past, their actions are much measured now and they are selective in terms of products as well as locations.

Corrective phase

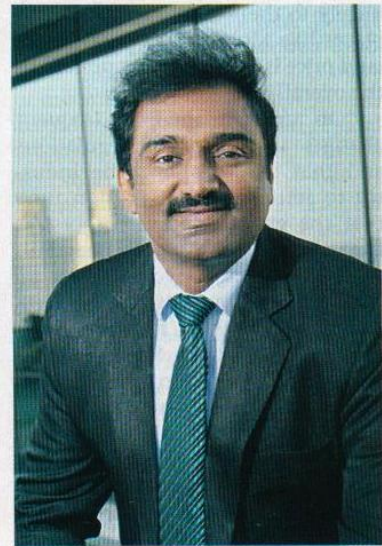
"The industry is learning the hard way," feels Pranay Vakil, chairman, Praron Consultancy and former chairman of Knight Frank. "There are now concerted efforts to focus on right kind of products and selection of appropriate locations. Further, pricing is also finding due significance in the whole strategy."

"The market," according to Maheshwari, "is undergoing a corrective phase. Developers are tweaking their portfolio and trying to build more properties for actual users." He

offers. Listing of units will be mandatory for all REITs.

To float an initial offer, it has been specified that the size of assets under the REIT will have to be at least ₹1,000 crore. This, according to SEBI, would ensure that initially only large assets and established entities enter the market. Further, the minimum initial offer size has to be ₹250 crore, in which

the public float has to be at least 25 per cent. Towards this end, SEBI has also proposed that though a REIT may raise funds from any type of investors, resident or foreign, initially till the market develops, the units of the REITs would be offered only to high networth individuals and institutions. The minimum subscription size would be ₹2 lakh and the



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Shah: getting approval is a big issue

feels that all these changes will hold the market in a good stead in the long run. In markets like Mumbai, Pune and NCR, the portion of speculative element has been on the higher side and, hence, these markets are more adversely impacted and showing signs of aberrations. However, as the end users consolidate their position gradually, things may fall in place in due course.

While developers are trying to deal with the immediate issues, the industry has been battling with the perennial problem of delays in getting approval for their projects. Developers unanimously view that the inordinate delay in obtaining approvals is the biggest challenge that the industry has been facing for long. A typical approval process can take as long as 12-24 months, adding

unit size will be ₹1 lakh. REITs have been allowed to invest in properties directly or through a special purpose vehicle (SPV) if such an SPV holds at least 90 per cent of the REIT asset. However, in such cases, it has been mandated that the REIT should have control over the SPV so that the interest of the investors are not adversely affected. ♦

hugely to the overall project cost in places like Mumbai and NCR, where land price is the major component in the overall property price.

"On top of it, there are frequent changes in rules and regulations and that hardly allows the industry to settle down. It is high time that the entire approval process is streamlined," says Diipesh Bhagtani, executive director, Jaycee Homes.

"Getting approvals for projects is the biggest issue for any developer," states Mayur Shah, managing director, Marathon group. "Apart from having contingency in place, it becomes often difficult for a developer to complete a project on time. Working in such an uncertain situation is one of the biggest challenges for the industry."

Regulatory measures

On the flip side, the government has recently initiated certain measures to streamline the domestic real estate sector. The introduction of draft Real Estate Regulation and Development Bill is a move in the right direction to bring about the desired transparency in the system.

However, the developer community believes that the bill is skewed in favour of buyers, even as the problems faced by builders have not been taken into consideration. There is a provision for a regulator but there is no attempt to regulate all the stakeholders. It does not hold government agencies accountable for delays in construction activities and, hence, they feel that such a regulation will only create greater discrepancy in the system.

"Though the intent is right, in its present form the bill may not serve the desired purpose. There is need to broaden its scope to include all stakeholders," says Jain.

The draft guidelines issued by the Securities and Exchange Board of India recently for setting up real estate investment trusts (REITs) has been hailed whole-heartedly by the



Ashwini: Bangalore holds steady

industry. In fact, it is being seen as a move that can redefine the Indian real estate landscape by bringing about the much-required liquidity as also infusing much greater level of transparency in the market. "The introduction of REITs in the long term would propel the sector, spurring capital inflows and bringing institutional credibility," says Magazine.

"It is an attempt that can revolutionise the Indian real estate industry. REITs will attract the much-needed institutional money into the sector which has often struggled on the liquidity front," states Maheshwari.

With all these initiatives in place, the domestic real estate sector may head for a better future in the

long run, even as it is faced with a set of headwinds in the immediate term. The market will have to sail through the present impasse, which is expected to continue till the general elections. The industry is eagerly expecting for some clarity on political and economic front. The uncertainties are still looming large and there is need for some concrete policy measures to bring the economy back on track. Any macro or micro trigger on the economic front will go a long way in reviving the overall sentiment and, therefore, the real estate sector, where the fundamentals continue to be intact. Softening of interest rates will also play a big role in the revival of demand in the industry.

In the short run, the market will be range-bound, with property prices remaining under pressure. Some of the locations may see some degree of correction in prices. Rental values for commercial properties will continue to be subdued, even as the demand-supply equilibrium is gradually getting restored with constraint being adopted on the supply side. Once the economy looks up, the corporates, which have been going slow for some time now, may start implementing their expansion plans.

In the long term, the sector is expecting certain structural changes. The proposed real estate regulation bill, if implemented in true spirit, may go a long way in setting up an organised and transparent set-up. This, along with investment instruments like REITs, will attract the much-desired liquidity in the system

and thus help increase the supply. Despite now more than two decades of economic liberalisation, real estate is still not got its due industry status and grappled with several policy-related anomalies. It is high time the state governments and the Centre work in tandem to streamline the sector which contributed heavily to the overall GDP.

• ARBIND GUPTA

