

India Property Sector

Rating: **Positive**

Consultants cautious on residential sector

Construction & real estate: India

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What has changed?

- Property consultants we have met with believe: 1) residential prices in Gurgaon and Mumbai (some areas) are due for corrections, 2) there will be gradual rises in demand for commercial (office) space, and 3) TDR prices will decline.

Impact

- **Residential prices expected to decline in Mumbai.** The consultants we spoke with expected prices in Central Mumbai to decline over the next six-to-12 months due to a combination of oversupply and high prices.
 - 1) **High prices are driving down sales volume.** The prices of some projects in Mumbai are above previous peak prices, due partly to speculation, and this is leading to a decline in sales volume. In Central Mumbai, prices for some projects have risen to Rs20,000-25,000/sq ft, which in some cases is higher than the previous peak.
 - 2) **Oversupply.** According to Knight Frank, about 12,000 apartments are under construction in Central Mumbai. Assuming an average of 1,200 apartments is completed a year, the total supply in the market is about double the average annual demand (500-600 apartments) based on the trend over the past five years. However, in the western suburbs, the decline in prices should be limited due to the scarcity of land.
 - 3) **TDR prices to decline.** With the floor space index due to rise to 1.33x from 1x in Mumbai's suburbs over the next three months, the property consultants expect the demand for transferable development rights (TDR) to decline. This is likely to lead to a decline in TDR prices.
- **Residential prices expected to decline in Gurgaon.** As in Mumbai, the prices of some residential projects in Gurgaon are higher than the previous peaks, due partly to speculation, and this is leading to a decline in sales volume. The prices for some projects have increased to Rs7,000-8,000/sq ft, which in some cases is higher than the previous peak.
- **Commercial rental volumes are increasing gradually.** The commercial rental volumes continue to improve gradually. However, due to high vacancy rates (16-25%), the consultants expect increases in rental rates to have a lag of one-to-two years. They expect the rises in rental rates to be led by Mumbai, but only after 12-18 months.

Valuation

- We maintain our **Positive** rating for the sector. The India property stocks we cover are trading at an average discount of 5% to our 1x FY12 year-end NAV forecast.

Catalysts and action

- We would regard an improvement in demand in the commercial sector as a positive share-price catalyst for the India property companies we cover, and a rise in interest rates as a risk.

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