Real Estate/Property

Industry Overview

Equity | India | Real Estate/Property
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Key takeaways from our meeting with Knight Frank

Amit Agarwal >> +91 22 6632-8654
Research Analyst
DSP Merrill Lynch (India)
amit_a_agarwal@ml.com

Key highlights of our meeting with Knight Frank

We met with property consultants Knight Frank (KF) on September 5. The key highlights of KF's outlook on the property sector are as follows: (1) Long-term growth factors for the industry remain strong, (2) short-term oversupply could lead to price correction, (3) execution is being hampered by a shortage of labor, (4) signs of consolidation in the industry are beginning to emerge, (5) developers' targets for development seem to be stretched and might not be met in the time span stated.

Short-term oversupply could lead to price decline

KF claimed that aggressive development has led to an oversupply situation in many of the towns. This is more acute in the Tier 2 and Tier 3 cities and it expects property prices to be under pressure. KF estimates that approximately 530mn sq ft of mid- to upper-end residential space will be developed in the top seven cities of India over the next three years.

Execution being hampered by labor shortage

Strong growth in development has led to a labor shortage which could hamper the execution of the real estate projects across the country. Anecdotal evidence of import of labor from the Philippines indicates the extent of the labor shortage.

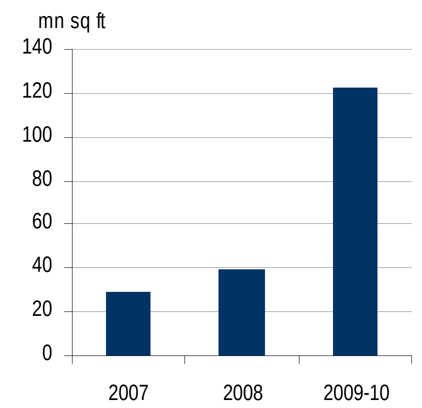
Developers have aggressive targets – may be tough to meet

The current development targets given by the developers are aggressive in KF's view. The main constraint is expected to be the lack of execution capabilities to handle real estate development on such a large scale, together with the labor shortage as mentioned above. The consensus NAV could be challenged due to (1) possible price correction and/or (2) delay in project execution due to labor shortage. In our NAV, we have built in flat prices up to FY10 and a more staggered development schedule than the companies' expectations. For every 1% price decline, our NAV estimate for DLF declines by 1.2% and that for Ansal Properties declines by 1.9%

Beginning of consolidation - beneficial for larger developers

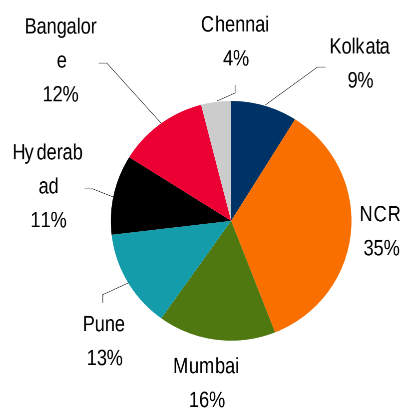
The industry is moving into a consolidation phase with the smaller developers selling land to larger developers instead of developing it themselves. The consolidation is being driven by the inability of the smaller developers to get funds for development due to reduction of lending to the real estate sector by the banks. KF expects that the industry will evolve toward having a few pan-Indian developers complemented by the larger regional developers. We expect the larger developers to benefit since they will be able to access good quality land banks.

Chart 1: New residential supply in NCR



Source: Knight Frank

Chart 2: Distribution of residential supply in top 7 cities in India (Total 530.5mn sq ft in 3 years)



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