SECTOR UPDATE

REAL ESTATE

New DCR regulations: A level playing field

India Equity Research | Real Estate

The Maharashtra government has introduced the amended Development Control Regulations (DCR) for Mumbai city/suburbs. The new regulation creates a level playing field for developers and does away with discretionary exceptions which had led to FSI-free areas accounting for a significantly large chunk of saleable area. We view this as a significant positive since it will spur new launches in Mumbai which have been on hold for over a year. Accordingly, we expect prices to correct and volumes to recover. While we are yet to see the fine print, initial estimates indicate NAV dilution of ~4-7%. However, resumption of the currently-grounded business cycle will be a positive for Mumbai developers' cash flows and stock performance.

Amended DCR largely along expected lines

The amended DCR is largely along expected lines with areas of balcony, flower beds, terraces, voids, niches etc., being counted in the FSI. Further, compensatory fungible FSI will be available to the extent of 35% for residential and 20% for industrial/commercial developments. Accordingly, we believe developers in Mumbai will now be able to construct on the basis of 2.7x FSI against 2.0x FSI, while we do not expect material changes in saleable area for an above-the-board project as areas free of FSI will now be disallowed.

Additional FSI comes at a price

The additional FSI will be allowed at 60%, 80% and 100% of the ready reckoner rates (of applicable land rates) for residential, industrial and commercial projects, respectively. Thus, while there is unlikely to be additional benefit to developers from increase in saleable area, there is likely to be additional outflow of ~5-10% of project realization towards payment of FSI premium, impacting NAVs by ~4-7%.

Transparency, clarity and a level playing field are the dividends

Ceteris paribus, we expect these measures will curb discretionary powers and usher in greater transparency in land bids. Additionally, the long awaited DCR amendments with curtailed discretionary powers are likely to result in greater clarity and transparency in the approval process, which will be a significant long-term positive.

Outlook: Resumption of launches and price correction in the offing

Since November 2010, approvals in Mumbai had slowed down significantly. Subsequently newer launches were deferred, curtailing supply, leading to higher prices and reduced volumes. Going forward, we expect new launches to follow by Q1FY13, resulting in easing of property prices and improvement in volumes. While we are yet to see the fine print, initial estimates indicate NAV dilution of ~4-7%.

Top Picks: Oberoi Realty and Phoenix Mills.

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Key features of the amended DCR

1) Reduction in areas excluded from FSI calculations

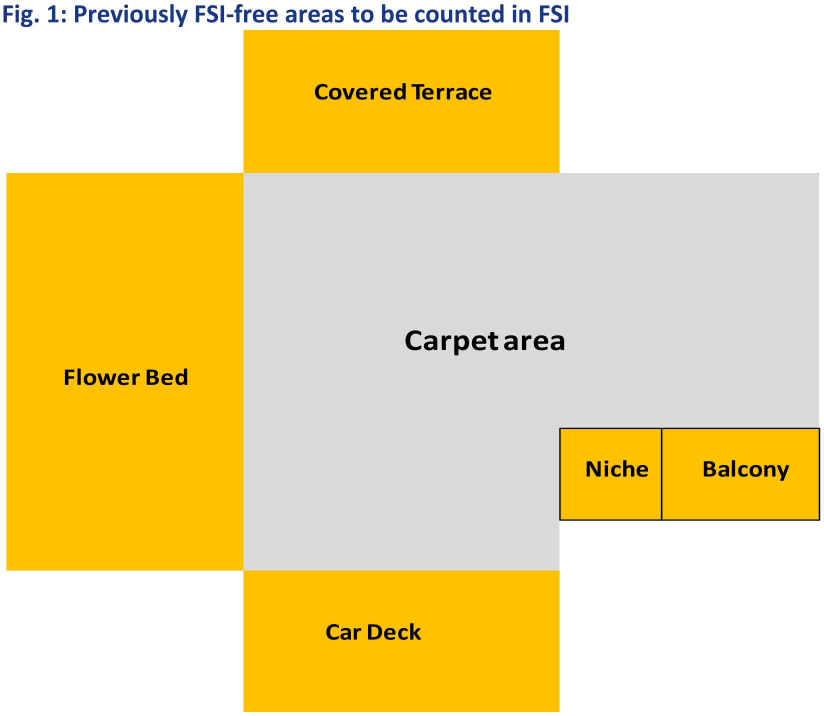
- The amended DCR is largely along expected lines with balcony, flower beds, terraces, voids, and niches etc., being counted in FSI, which were earlier free of FSI.
- However, to compensate for the loss of FSI-free areas, the government has allowed compensatory fungible FSI to the extent of 35% for residential development and 20% for industrial and commercial developments. This is higher than the proposed compensatory fungible FSI of 25% for residential development and 15% for industrial and commercial developments in the earlier draft, which is an incremental positive.
- Fungible FSI is usable like any other FSI i.e., it can be used for making flower beds, voids etc., or can be used for constructing bigger habitable areas.

Table 1: Compensatory FSI under amended DCR is higher than under draft DCR

Segment	Amended DCR (%)	Draft DCR (%)
Residential	35.0	25.0
Industrial	20.0	15.0
Commercial	20.0	15.0

Source: BMC, Edelweiss research

Fig. 1: Previously FSI-free areas to be counted in FSI



Source: Edelweiss research

2) Proposed premium for compensatory FSI

- The compensatory fungible FSI will be charged at 60%, 80% and 100% of ready reckoner rates for developed land for residential, industrial and commercial developments, respectively. This is lower than the proposed premium of 100% of ready reckoner rate for residential development, 125% for industrial development and 200% for commercial developments in the earlier draft, which is an incremental positive.

- As per our estimates, there is likely to be additional outflow of ~5-10% of project realization towards payment of FSI premium for developers (illustrated in table 3 below).

Table 2: FSI premium under amended DCR is lower than under draft DCR

Segment	Amended DCR (%)	Draft DCR (%)
Residential	60.0	100.0
Industrial	80.0	125.0
Commercial	100.0	200.0

Source: Edelweiss research

Table 3: FSI cost calculation under new DCR

Micro-Market	CY12E - Ready reckoner rate for developer land (INR/sf)	FSI cost at 60% of CY12 ready reckoner rate (INR/sf)	FSI premium (INR/sf)	Residential Sale price (INR/sf)	FSI premium/sale price (%)
Napean Sea Road	32,062	19,237	5,002	50,000	10.0
Worli	14,760	8,856	2,303	40,000	5.8
Bandra	7,581	4,548	1,183	20,000	5.9
Andheri	7,213	4,328	1,125	14,000	8.0
Goregaon	6,009	3,605	937	11,000	8.5
Ghatkopar	5,474	3,284	854	10,000	8.5
Mulund	5,184	3,110	809	9,000	9.0
Chembur	6,399	3,839	998	10,000	10.0

Source: Edelweiss research estimates

3) Relaxations given for redevelopment schemes

- No premium will be charged for fungible FSI to be used in rehabilitation component under redevelopment of cessed buildings under 33(7) and 33(9) etc. In suburbs where buildings are not cessed, the fungible FSI on the FSI already consumed in existing buildings will be available free of premium. This will help MHADA developments as also regular proposals for redevelopment of existing buildings using TDR in suburbs.

- Open space requirements for development of small plots under 33(7) i.e., redevelopment of cessed buildings has been relaxed. The requirement under the new rules will be only 1.5 metre open space on all sides of plots measuring 600 sq.m. or less. This relaxation will also be available for small plots' development under 33 (10).

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Coverage group(s) of stocks by primary analyst(s): Real Estate

Brigade Enterprises, DLF, Jaypee Infratech, Mahindra Lifespace Developers, Oberoi Realty, Orbit corporation, The Phoenix Mills

Recent Research

Date	Company	Title	Price (INR)	Recos
03-Jan-12	**Real Estate**	Mumbai: 20% reservation for LIG housing on cards; *EdelFlash*		
28-Dec-11	**DLF**	Pune SEZ stake sale along expected lines; *EdelFlash*	193	Hold
21-Dec-11	**Real Estate**	USD3bn of PE exits on cards in CY12; *Sector Update*		

Distribution of Ratings / Market Cap

Edelweiss Research Coverage Universe

	Buy	Hold	Reduce	Total
Rating Distribution* * 3 stocks under review	119	47	15	184

	> 50bn	Between 10bn and 50 bn	< 10bn
Market Cap (INR)	111	57	16

Rating Interpretation

Rating	Expected to
Buy	appreciate more than 15% over a 12-month period
Hold	appreciate up to 15% over a 12-month period
Reduce	depreciate more than 5% over a 12-month period

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