

Real estate

Sector Update

BKC auction indicates realty slowdown

As per media reports, the Mumbai Metropolitan Region Development Authority (MMRDA) had recently put five plots on auctions in the G-Block of the Bandra-Kurla Complex, comprising two commercial, two residential and a clubhouse. Out of these five plots, the authority only managed to sell three plots for Rs1,322 crore. Of these three plots, the authority sold one commercial plot, spanning 24,000 square metre, to Jet Airways for Rs826 crore. This implies a selling price of approximately Rs32,000 per square feet (Rs314,467 per square metre) for the commercial plot. This selling price is at a 31.7% discount to the Wadhwa Builders' bid of Rs46,806 per square feet (or Rs503,636 per square metre). It is also interesting to note that Jet Airways was the sole bidder for the commercial plot in the recent auction.

Price correction—most likely

Such a lukewarm response from the corporate houses and developers to the recent MMRDA auction indicates there is a lack of demand across verticals from the end users in the Mumbai region. This, in turn, shows that there is a possibility of a correction in the property prices in the Mumbai region.

We had also highlighted in our last Sector Update report dated March 12, 2008 that the outlook for the information technology (IT)/IT enabled services (ITES) sector, a major demand driver for the real estate sector, remains hazy. Since the IT/ITES sector alone drives almost 75.0% to 80.0% of the demand for the commercial space and about 30% to 40% demand for the residential space, we believe the slowdown in the IT/ITES sector would lead to the deferring of commercial space requirement by the corporates and of residential space requirement by the employees in the IT/ITES sector.

Although the developers have maintained the selling price for their projects, there has been a significant slowdown in the sales volume in the recent past. There has been approximately a 50.0% year-on-year slowdown in the sales volume in the National Capital Region. Besides, a slowdown has also been witnessed in the Tier II and Tier III cities. The lukewarm response to the recent MMRDA auction also indicates that there is a lack of demand in the Mumbai

Metropolitan Region. Hence, we believe that the developers will find it difficult to maintain the current prices owing to the recent drop in the sales volume and the slowdown in the IT/ITES sector. Therefore the developers could reduce prices to boost sales volume.

Price targets and earnings estimates revised downward

In view of the recent decline in the sales volume and the poor response to the MMRDA auction, we believe property prices could soften in the near term. Hence, we are revising our assumptions for valuing the realty stocks under our coverage. We are factoring a 5.0% property price correction in FY2009, stable prices in FY2010 and a 5.0% growth rate for selling prices thereafter for the stocks under coverage.

Orbit Corporation

To factor in the property price correction expected in FY2009 and FY2010, we are revising our earnings estimates downward by 25.2% for FY2009 and by 22.4% for FY2010. We have also fine-tuned our FY2008 earnings estimate. Given its unique business model, we continue to value the stock using price to earning multiple and are rolling over our target multiple to the FY2010 earnings estimate. We have revised our price target to Rs852. We maintain our Buy recommendation on the stock.

Key financial

Particular	FY2007	FY2008E	FY2009E	FY2010E
Net profit (Rs cr)	57.3	224.2	261.0	351.8
No of shares (cr)	2.7	4.5	4.5	4.5
EPS (Rs)	21.1	49.4	57.5	77.5
<i>y-o-y growth rate</i>		134.5	16.4	34.8
PER(x)	33.5	14.3	12.3	9.1
Price/BV(x)	6.3	5.9	4.5	3.0
EV/EBITDA(x)	30.7	6.9	6.4	4.5
RoCE(%)	25.1	39.9	30.2	32.7
RoNW(%)	28.2	51.4	36.9	33.2

Mahindra Lifespace

To factor in the property price correction in FY2009 and FY2010, we are revising our earnings estimates downward by 18.6% for FY2009 and by 26.9% for FY2010. We continue to value the stock using the sum-of-parts-valuation method.

After factoring the property price correction, we value Mahindra Lifespace's Chennai and Jaipur SEZs and the other planned developments at 1.0x of the revised net asset value of Rs805 per share. The remaining land on which the company does not have any development plans in the short to medium term is valued at Rs30 per share. We maintain Buy recommendation on the stock with a revised price target of Rs835.

Key financial

Particular	FY2007	FY2008E	FY2009E	FY2010E
Adj net profit (Rs cr)	17.9	38.8	113.5	282.9
No of shares (crore)	4.1	4.1	4.1	4.1
EPS (Rs)	4.4	9.5	27.8	69.2
<i>y-o-y growth rate</i>		116.3	192.9	149.2
PER(x)	87.3	40.4	13.8	5.5
Price/BV(x)	20.0	1.9	1.6	1.3
EV/EBITDA(x)	56.8	26.8	8.3	2.4
RoCE(%)	3.0	4.5	11.7	24.1
RoNW(%)	2.3	4.6	11.8	22.8

The author doesn't hold any investment in any of the companies mentioned in the article.