RESEARCH

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Knight Frank

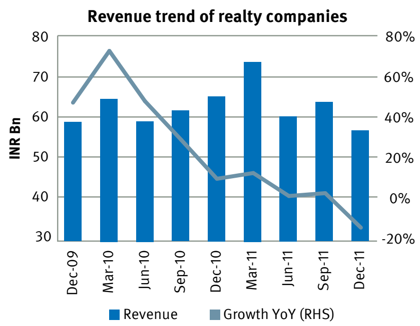
Economic Outlook

The Indian economy finally seems to be cooling off in terms of prices with the latest month's inflation being reported at the lowest level since the last two years. Wholesale Price Index (WPI) growth for the month of January 2012 stands at 6.6%, down from 7.5% in the previous month. Additionally, WPI growth of food articles was reported at -0.5% for the latest month implying that food prices have finally started falling. These numbers bring a great amount of relief to the Reserve Bank of India (RBI) which has been trying to contain inflation since 2010. However, the latest GDP growth number of 6.1% for Q3 2011-12 indicate that the impact of tighter monetary policy has started creeping into the economic growth of the country. With prices under control and GDP growth slowing down, the RBI is expected to ease its monetary policy stance by reducing the policy rates in the coming months. The Cash Reserve Ratios (CRR) cut of 50 basis points from 6% to 5.5% in January 2012 is a clear indication of this.

The impact of monetary policy's easing will be most positively felt on the cash strapped sector of real estate which has been suffering in terms of liquidity since the past few quarters. The financial performance of the real estate companies in the latest quarter is a testimony to the deteriorating condition of the sector. In order to analyze the performance in detail, we have considered the financial results of 22 listed real estate companies in India on a quarterly basis. These 22 companies can be considered as a fair representative of the overall real estate market of India since they not only cover the various sub-segments of real estate but also all the major cities of India.

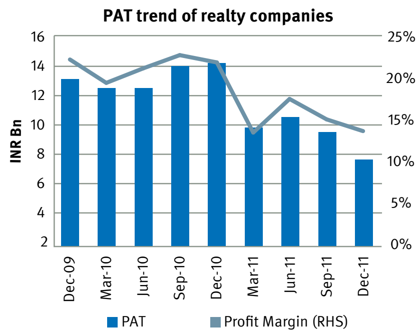
Revenue of these companies has been declining with each passing quarter after peaking in March 2011 quarter at INR 74 bn. The year-on-year growth in revenue has been steadily falling since March 2010 and for the first time in over two years the growth has been negative. Revenues for December 2011 quarter fell by 13% to INR 57 bn as compared to INR 65 bn reported during December 2010. The drop in revenues has been because of the combined effect of falling prices and slowdown in sales volume.

REVENUES FOR DECEMBER 2011 QUARTER FELL BY 13% TO INR 57 BN AS COMPARED TO INR 65 BN REPORTED DURING DECEMBER 2010.



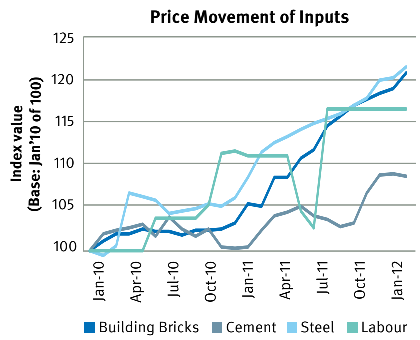
Source: BSE, Knight Frank Research

Performance of realty companies in terms of profit has been even worse in the last few quarters with each passing quarter reporting a lower number. During the December 2011 quarter, the year-on-year growth in profit has been -45% despite revenues falling by only 13%. Profit margins have dropped significantly to 14% during the latest quarter compared to more than 22% reported during December 2010 quarter. Apart from higher cost of borrowing, pressure from rising input costs is eating away into realty companies' profitability and going forward this will not only impact the cash flow position but also the debt repayment capacity of the sector.



Source: BSE, Knight Frank Research

Price of input items such as cement, steel, labour and bricks, which contributes to more than two-third of the total construction cost, has increased substantially in the last two years. While price of steel and bricks have gone up by more than 20% since January 2010, labour cost has increased by close to 16% during the same period. With no legroom to increase the price of properties, developers are left with no other option but to absorb the hike in input costs resulting in lower profit margin. Such a scenario is expected to continue for the next couple of quarters unless there is a significant improvement in either demand or price.



Source: BSE, Knight Frank Research

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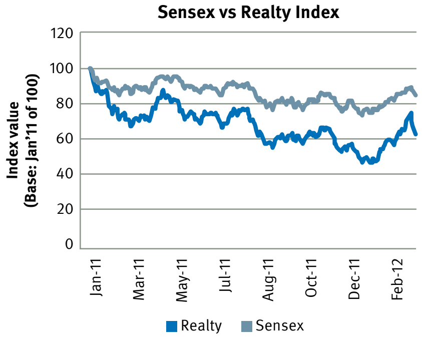
WHILE PRICE OF STEEL AND BRICKS HAVE GONE UP BY MORE THAN 20% SINCE JANUARY 2010, LABOUR COST HAS INCREASED BY CLOSE TO 16% DURING THE SAME PERIOD.

Poor performance by realty companies is being reflected in their share price indicating the lack of interest by investor community towards the sector. The Realty Index on Bombay Stock Exchange (BSE) has dropped by more than 36% in the last one year compared to a 15% fall in the Sensex. In order to bring back the enthusiasm of the investor community into the sector, real estate companies will have to focus on factors such as improving cash flow position, lowering inventory, reducing debt and increasing profit margins.

Sensex vs Realty Index



Source: BSE, Knight Frank Research

Bangalore Residential Market

Market Overview

Bangalore residential market has been represented by both positive sentiments as well as cautiousness on the part of the buyers during the year 2011. The city has typically been preferred by home buyers due to its favourable socio-economic conditions and a salubrious climate. In the recent years, Bangalore has attracted a large influx of population engaged with the thriving IT sector. Consequently, the city has been expanding to meet the residential demand of the increasing populace. The Bangalore residential market can be divided based on its geographical pattern into central, north, south, east and west. Table 1 depicts the market classification in Bangalore.

Table 1: Residential Micro-markets in Bangalore

Central	
Prime	MG Road, Richmond Road, Lavelle Road, Cunningham Road, Brunton Road, Residency Road, St.Mark's Road
Others	Frazer Town, Cox Town, Indiranagar, Sadashivnagar, Ulsoor, Jayamahal
Suburban	
East	Airport Road, Old Madras Road, KR Puram, Whitefield, Marathahalli, Varthur Road, Brookefield
North	RT Nagar, Hebbal, Bellary Road, Yelahanka, Banaswadi, HRBR Layout, Doddaballapur Road, Jakkur
South	Koramangala, Sarjapur Road, HSR Layout, Jayanagar, JP Nagar, Banashankari, Bannerghatta Road, Outer Ring Road, Kanakapura Road, Hosur Road, Mysore Road
West	Malleswaram, Rajajinagar, Vijaynagar, Magadi Road, Yeshwanthpur, Tumkur Road, Jalahalli

Source: Knight Frank Research

The city had witnessed considerable decline in residential demand during the slowdown in the country with developers and buyers both maintaining a negative outlook on the real estate market. However, with the economy back on track in 2010, the first quarter of 2011 was characterized by optimism on both the developer and the buyer's side, leading to enhanced activity across various micro-markets of the city. A number of new projects were launched while sales and enquiries on projects under construction picked up momentum.

With the city undergoing expansion and transformation to a fast growing metropolitan, considerable investor interest has also been observed in the past few years. There has been a growing demand from individuals looking at buying premium properties in Bangalore. These may be in the form of villas or luxury apartments with world class interiors and facilities. Most of the demand for high-end residences has emanated from MNC executives, businessmen and NRIs who want to invest in India due to global economic uncertainties and a dearth of feasible investment opportunities elsewhere. Besides, high-end residential properties in Bangalore are relatively lower-priced as compared to the NCR or Mumbai markets. Thus, along with the interest shown by these investors, the year 2011 began with enthusiasm shown by property buyers who had delayed their purchases in the past.

Bangalore has typically been an end-user driven market with moderate price appreciation. Stability in the market in early 2011, as well as minimal speculation, had instilled confidence in the end-users to proceed with their purchase decisions. Demand was more evident in the mid-end category, primarily towards the South and the North micro-markets where majority of the affordable projects are located. This led a number of developers to hike up their prices by around 5-8% in the suburbs while the price appreciation was higher in the CBD areas. However, unfavourable global economic conditions and a higher rate of interest in the second and the third quarter of the year dampened the optimism in the market and slackened the sales figures. Both end-users and investors exhibited some amount of reluctance owing to these factors, which also affected their affordability. Despite the subdued buyer interest, the developers have gone ahead with their plans and several large scale projects have been announced in the last quarter of 2011, thus establishing a strong supply pipeline in the next 2-3 years.

Supply and Development

The Bangalore residential market saw the launch of around 90 projects in the first three quarters of 2011-12, translating to an incremental supply of over 30,000 units. Majority of these projects are located towards the southern part of the city, encompassing micro-markets such as Sarjapur Road, Bannerghatta Road, Kanakapura Road and Electronic City. The northern region of the city witnessed the second highest number of project launches, primarily in locations like Yelahanka, Jalahalli and Hebbal Ring Road.

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Table 2. Select Upcoming Projects in Bangalore

Project Name	Developer	Location	Number of Units	Possession
Adarsh Serenity	Adarsh Developers	Whitefield	171	Dec-2013
Century Renata	Century Group	Richmond Road	36	Dec-2014
HM Tropical Tree	HM Group	RT Nagar	85	Dec-2012
Mantri Glades	Mantri Developers	Sarjapur Road	165	Nov-2013
Purva Midtown	Puravankara Projects	Whitefield	117	Aug-2013
Ramky One North	Ramky Estates	Yelahanka	312	Dec-2013
Skylark Esta	Skylark Group	Hoodi Junction	200	Jan-2014
Sobha Pristine	Sobha Developers	Off Sarjapur Road	44	Dec-2014

Source: Eyestate

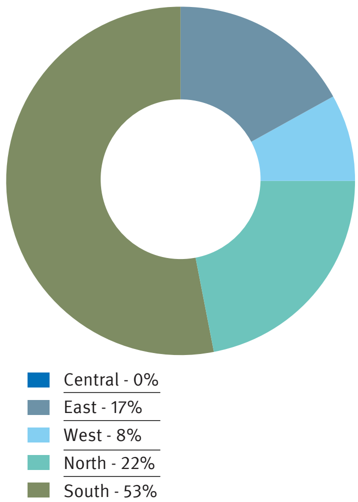
THE BANGALORE RESIDENTIAL MARKET SAW THE LAUNCH OF AROUND 90 PROJECTS IN THE FIRST THREE QUARTERS OF 2011-12, TRANSLATING TO AN INCREMENTAL SUPPLY OF OVER 30,000 UNITS.

Bangalore east saw several new residential developments being commenced in Whitefield and Hoody Junction, while the western and central parts of the city witnessed relatively lesser number of new project launches.

During the next 3 years, an aggregate of 82,000 units will be entering the market with majority of it concentrated in the southern, northern and eastern region of the city. With the launch of a large number of projects in the last few quarters, southern region now accounts for more than 50% of the total upcoming supply. However, the prime central location has no significant upcoming supply due to a dearth of developable land.

DURING THE NEXT 3 YEARS, AN AGGREGATE OF 82,000 UNITS WILL BE ENTERING THE MARKET WITH MAJORITY OF IT CONCENTRATED IN THE SOUTHERN, NORTHERN AND EASTERN REGION OF THE CITY

No. of Units Under Construction (Region-wise)



Source: Eyestate

Significantly, the projects under construction have met with encouraging absorption, all the regions witnessing more than 50% of their units having been sold. The northern and eastern regions each witnessed 57% of the total number of units as sold, while 95% of the projects in central Bangalore are sold out. This positive trend has made the city occupy the top spot in residential absorption in the country.

Table 3: Micro-market wise Absorption

Micro-market	Percentage
Central	95%
East	57%
West	52%
North	57%
South	55%

Source: Eyestate

Price Trend

Bangalore residential market has seen favourable sales traction which may be primarily attributed towards stable pricing during the year. High inventory levels and availability of large tracts of developable land in the suburban and peripheral locations have aided in maintaining consistency in the residential prices in those regions. Price appreciation in most micro-markets was observed to have been in the range of 5-12% during the year.

Table 4: Residential Capital Values (INR/Sq.ft) in Dec 2011

Micro-markets	Minimum	Maximum
MG Road	16000	23000
Koramangala	7000	10000
Indiranagar	8000	11000
Malleshwaram	7500	12000
Banaswadi	4200	6000
Bellary Road	3500	5500
Whitefield	3000	4500
BTM Layout	5000	8000

Source: Knight Frank Research

Outlook

Bangalore residential market had a positive run in 2011, which has extended to early 2012 as well. The first two months of 2012 have witnessed several project launches by reputed developers and this momentum is expected to remain in the coming months. These projects offer a balanced mix of both high-end and mid-end developments. Post recession, developers in the city have realized that demand exists for those properties which offer quality, value for money and transparency in deals.

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Thus, majority of the upcoming supply will be concentrated in the suburban and peripheral locations with gated sustainable communities offering various amenities and facilities.

Another major trend expected is the emergence of the resale market in the city. Delayed deliverables in the past have led home buyers to explore the ready to move in properties at a higher cost than the under construction ones.

On the price front, capital values of properties are not expected to increase considerably due to slowing down of the economy, though marginal appreciation is expected in a few micro-markets like Hebbal and Sarjapura Road.

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