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ECONOMY & REALTY

Knight Frank

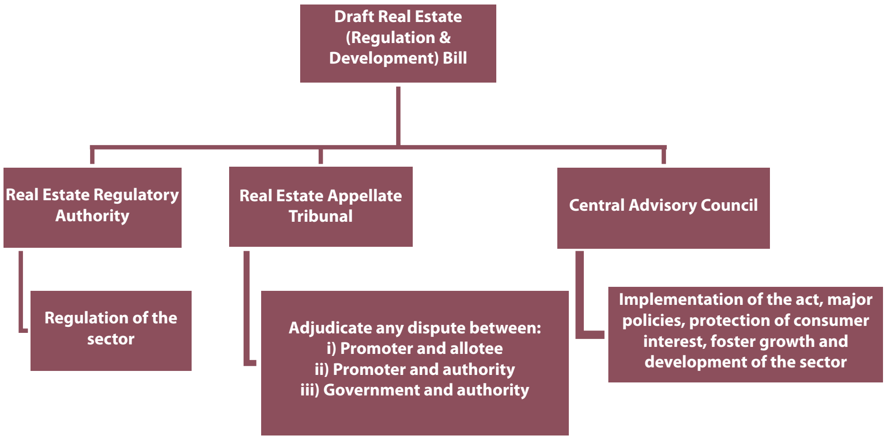
Economic Outlook

The recent economic crisis in countries such as Greece and Italy has played havoc in the global financial market with major lenders staying away from participating in the bond auction of these countries. This has resulted in investors diverting their funds towards safe havens like gold and USD (US Dollar). In the past couple of months, USD has appreciated significantly against most of the currencies including the INR (Indian Rupee). UDS has gained more than 16% against INR since July 2011 and the current exchange rate stands at INR 51.70/USD. Such a steep appreciation in USD has got Indian policymakers worried since it not only increases the import bill but also worsens the debt position of Indian companies which have borrowed in USD.

The timing of such events couldn't have been worse since the corporate sector is already reeling under the pressure of slowing demand and shrinking margin. Additionally, the perception of paralysis in policy framing by the government is making investors jittery in committing new funds. However, the recent move by the government of introducing the Draft Real Estate bill has brought some optimism and hopefully the momentum of reforms will continue going forward.

The draft Real Estate Bill, introduced for public comments earlier this month by the Ministry of Housing and Urban Poverty Alleviation, seeks to regulate all real estate projects being developed in India with land area exceeding 4,000 sq.mtr. This is the first such bill at the central level which will directly regulate the real estate sector and adjudicate any dispute between the buyer, promoter and government authority.

The bill attempts to overcome the shortcomings of the existing system in the real estate market where buyer's interest is



frequently ignored by the promoter as well as the government. The bill tries to identify these problem areas and fix time bound responsibility on the promoters to disclose certain necessary information regarding their projects in order to bring in greater level of transparency.

Promoters will be required to seek registration of their projects from the regulator before advertising, booking or taking any advance from buyers. For registration purpose, promoters will have to submit a declaration stating that the legal title of the land is in their name and the project will be completed within the stipulated time. Additionally, 70% of the amount realized for the project will have to be deposited in a separate bank account which will be used specifically for the purpose of meeting the costs of the aforementioned project. Post registration of the project, details such as layout plan, sanctions received, proforma of agreement, carpet area of each unit, list of bookings, development work, etc will have to be updated on the regulators website. These provisions will ensure that transparency is maintained at every step of the project and buyers are not shortchanged in any way.

The bill aims to protect buyer's interest even after possession is granted. The promoters will be responsible to repair any structural defects in the project within a period of one year from possession. In addition to this, they will be required to take all necessary steps to execute a registered conveyance deed in favour of the allottee.

The recent cases of home buyers being cheated or receiving deficient service from developers has prompted the government to include harsh penalties on promoters to deter them from committing such acts. If any promoter willfully fails to register their project with the regulator, he can be punished with imprisonment of up to 3 years or a penalty up to 10% of the estimated cost of the project. For any other violation, the penalty can go up to 5% of the estimated cost of the project. However, the bill is silent on the wrong doings, if any, committed by a sanctioning or government authority. Punishment of upto 3 years seems too harsh for such an offence and currently no other regulator imposes such a severe penalty for similar offence.

From the legal perspective, the Real Estate Regulatory Authority shall have the same powers as are vested in a civil court under

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the Code of Civil Procedure, 1908. No civil court shall have jurisdiction in respect of any matter which the regulatory authority or the appellate tribunal is empowered under this act to determine. Also, no court inferior to that of a Metropolitan Magistrate or a Judicial Magistrate of first class shall try any offence punishable under this act.

THE BILL SEEMS TO FOCUS MORE ON REGULATION OF THE REAL ESTATE SECTOR RATHER THAN DEVELOPMENT, WHICH IS THE NEED OF THE HOUR

There are certain shortcomings in the bill despite the best efforts of the government authorities in drafting it. The bill seems to focus more on regulation of the real estate sector rather than development, which is the need of the hour. Additionally, many important stakeholders of the real estate market such as brokers, sanctioning authorities, registrars, landlords and others are kept out of the ambit of the bill. Even secondary market transactions including lease agreements and landlord-tenant relationship has been kept out.

For the development of a healthy real estate market, it is important that interest of all stakeholders is taken care by the bill. This bill is definitely a welcome move from the government and will give the much needed relief to millions of home buyers in India.

Mumbai Residential Market Summary–Q2FY12

Market Overview

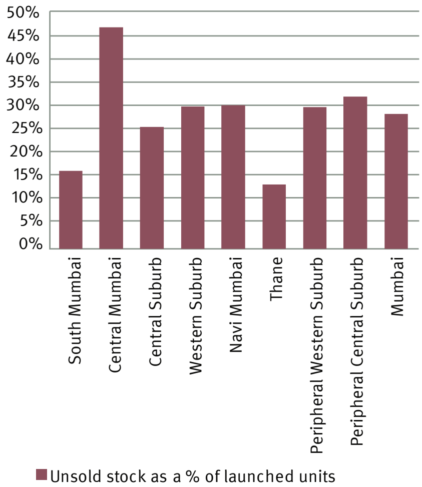
Mumbai has historically been the strongest residential market in India and has proved its resilience during the economic crisis of 2008. Since then, property prices have risen to highly unaffordable levels and are currently quoting more than 20% over their 2007 highs. The Maharashtra State stamp and registration department data has shown a consistently declining trend in the number of property sales registrations over the past 24 months. The trend has continued as even the festive season failed to stimulate the market. These astronomical prices, increasing interest rates and liquidity pressures have hurt market sentiment and caused transaction volumes to plummet. Price levels have however proven to be more resilient with new project launches virtually coming to a standstill as the BMC has withheld approvals to new projects since late 2010 in an endeavour to restructure and rationalize FSI guidelines in the city.

Supply and Demand

The Mumbai real estate market has stagnated over the previous three quarters with buyers largely keeping away from the market with the expectation of an imminent drop in prices in the near future. This coupled with a regulator imposed supply crunch has resulted in residential market transaction volumes plummeting more than 70% since its 2007 heydays. Unsold inventory levels are currently estimated to be approximately 27% of the under construction stock. Also, the investors' segment which makes up approximately 20% of the market demand has been observed to be actively reducing its real estate portfolio, thereby adding significant shadow supply into the market.

APPROXIMATELY 63% OF THE TOTAL UNSOLD INVENTORY IS CONCENTRATED IN THE PERIPHERAL CENTRAL SUBURBS, THANE, NAVI MUMBAI AND THE WESTERN SUBURBS BEYOND BORIVALI

Unsold stock as a % of launched units



Source: RBI, Knight Frank Research

The core of the residential market has been steadily shifting northward over the years as people are prepared to move further and further away from the CBDs to find an apartment which fits their budget. This had prompted a flurry of construction activity in the peripheral suburbs to accommodate this demographic shift. A bulk of the supply is concentrated on the northern fringes of the Mumbai market as developers tap

Location	Price (Q2 FY12) in INR./sq.ft	Price (Q2 FY11) in INR./sq.ft
Cuffe Parade	32500-65000	37000-62000
Malabar Hills	60000-75000	58000-66000
Nepeansea Road	55000-80000	55000-70000
Mahalaxmi	23000-40000	25000-46000
Worli	25000-60000	25000-50000
Lower Parel	22000-30000	22000-37000
Prabhadevi	20000-45000	20000-42000
Dadar	18000-30000	19000-31000
Bandra West	20500-35000	22000-42000
Andheri	8500-17000	11000-17000
Goregoan	6500-11500	9500-11500
Kandivali	7000-9000	8500-11000
Borivali	7500-9000	8500-13000
Mira Road	3000-4500	4400-5400
Virar	2200-3200	3200-4500
Naigaon East	2200-3000	2900-3300
Vasai	2500-3200	3100-3500
Chembur	9000-14000	9000-15000
Bhandup	5800-8500	7500-9000
Mulund	6000-8500	7500-9500
Thane	5300-8700	5500-8700
Dombivali	2400-4000	3000-4000
Kalyan	2900-3800	3000-4200
Ambernath	2000-3500	2500-3800
Vashi	6000-8000	7000-10000
Airoli	4000-5000	6500-7200
Kopar Khairane	4500-6000	6000-7500
Kharghar	3500-4500	4500-7100
Panvel	2200-3600	3200-6500

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into the largest chunk of buyers looking for apartments priced upto INR 7.5 mn. Nearly 75% of the unsold inventory in the Mumbai market caters to this category. Approximately 63% of the total unsold inventory is concentrated in the Peripheral Central Suburbs, Thane, Navi Mumbai and the Western Suburbs beyond Borivali due to the advent of mass housing projects in these micro-markets. South and Central Mumbai account for 3% while Central Suburbs and the Western Suburbs account for 10% and 23% respectively of the unsold inventory in the Mumbai market.

UNSOLD INVENTORY HAS ALSO DOUBLED IN THE WESTERN SUBURBS, NAVI MUMBAI AND THE PERIPHERAL WESTERN SUBURBS SINCE Q2 FY11 TO APPROXIMATELY 30% LEVELS

A drop in transaction volumes coupled with a significant number of deal cancellations has hit the Central Mumbai market the hardest as the quantum of unsold inventory has gone up to more than 45% of the units launched. Unsold Inventory has also doubled in the Western Suburbs, Navi Mumbai and the Peripheral Western Suburbs since Q2 FY11 to approximately 30% levels for the same reasons.

Prices

Prices have been moving in a narrow range in the past four quarters as developers have held on and buyers have been playing a waiting game. It has been observed that prices in premium micro-markets tend to be much more volatile compared to the peripheral suburban micro-markets. Thus prices in some South and Central Mumbai locations like Parel, Lower Parel and Mahalaxmi, have declined between 5-15% over the previous three quarters while prices in Navi Mumbai, Thane and the peripheral suburbs of Central & Western Mumbai have either been stable or have trended marginally upwards.

Developers have been more open to negotiation in the premium segment reducing prices by as much as 25% in favour of a sizeable up-front payment. The increasing number of cancellations is symptomatic of a wary investors' segment which is fast losing faith in the current scenario where developers are hard pressed to even service their debt obligations.

Outlook

The stagnant real estate prices today suggest a stalemate between buyers and sellers but market indicators strongly hint at an imminent inflection point. Tight liquidity conditions, increasing inventories, rising interest rates, increasing construction costs, proposed incremental 33% FSI and subsequent reduction in TDR prices will eventually tip the scales in the buyers' favour. However, developers might be able to hold their ground if the current credit crunch eases which is unlikely as the banking fraternity curtails lending to the real estate sector. Rental yields are expected to rise as residential prices correct and owners compensate by increasing rentals.

RENTAL YIELDS ARE EXPECTED TO RISE AS RESIDENTIAL PRICES CORRECT AND OWNERS COMPENSATE BY INCREASING RENTAL RATES

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