RESEARCH

FEBRUARY 2013

RESIDENTIAL TRACTION @ GLANCE

Knight Frank

Mumbai

Market Overview

Mumbai is the financial powerhouse that fuels the Indian economic growth engine and is the most active residential market in the country in terms of transaction density. This city has historically been the strongest residential market in India and has proven its resilience during the economic crisis of 2008 when prices and absorption succumbed to a potential economic catastrophe. Since then, property prices have recovered and risen to highly unaffordable levels, currently quoting more than 25% over their 2007 highs. These unaffordable prices have hit affordability and consequently caused absorption numbers to fall considerably across 2010 and 2011. Increasing inflation and interest rates, liquidity pressures faced by developers and regulatory bottlenecks have also played their part in creating a crisis of confidence in the market, thereby keeping absorption numbers low. However, 2012 saw absorption levels almost equal those in 2011, heralding a potential reversal in the downward trend.

Launches and Absorption

The Mumbai real estate market has stagnated in recent years as buyers have largely kept away from the market expecting an imminent drop in prices in the near future. Consequently, absorption levels in 2011 had dropped over 35% from the previous year. This steep drop in absorption levels should have resulted in a similar correction in prices. However, a regulator imposed supply crunch through delay in approvals ensured that the market price equilibrium was maintained. Thus, an even greater fall in units launched, effectively offset the impact on prices.

2012 SAW ABSORPTION LEVELS ALMOST EQUAL THOSE IN 2011, HERALDING A POTENTIAL REVERSAL IN THE DOWNWARD TREND.

AS COMPARED TO 2011 THEY HAVE DROPPED BY JUST 3% TO 42,200 UNITS. APPROXIMATELY 50,500 UNITS WERE LAUNCHED IN 2012 WHICH WAS AN 8% DROP FROM 2011 LEVELS.

2012 has bucked the downtrend in absorption numbers and seen them match the previous year's levels. This is largely due to the fact that developers who are under pressure to deleverage their balance sheets and create liquidity have been more open to negotiating aggressively by reducing prices. Till very recently, the developer fraternity has been averse to reducing rates upfront but cracks are beginning to show as sporadic cases of price softening have been observed.

Knight Frank Research has analysed the residential market comprising of projects with a sales potential above INR. 300 mn. in the Mumbai Metropolitan Region. Absorption numbers in 2012 are estimated to have dropped by more than 62% from their 2007 heydays. However, as compared to 2011 they have dropped by just 3% to 42,200 units.

Approximately 50,500 units were launched in 2012 which was an 8% drop from 2011 levels. The market which was already carrying close to 75,000 unsold under construction units (unsold inventory) at the end of 2011 saw this number swell further to 83,000 units in December 2012 which is an estimated 39% of the total under construction units in the Mumbai residential market. Increasing inventories coupled with stagnating absorption numbers continued to squeeze the market and put pressure on price levels in 2012.

INCREASING INVENTORIES COUPLED WITH STAGNATING ABSORPTION NUMBERS CONTINUED TO SQUEEZE THE MARKET AND PUT PRESSURE ON PRICE LEVELS IN 2012.

Developers are hard pressed today to maintain their net profit margins as rising interest and other input costs such as land and labour in addition to the ever increasing raw material costs of steel and cement continue to constrain developers from cutting prices. The cost of land is by far the biggest factor that has stopped a developer from reducing prices as the product prices have to be linked to the continuously increasing land prices. Joint development agreements and different forms of redevelopment agreements are the order of the day, as developers look to bypass the mammoth upfront cost that a land acquisition entails.

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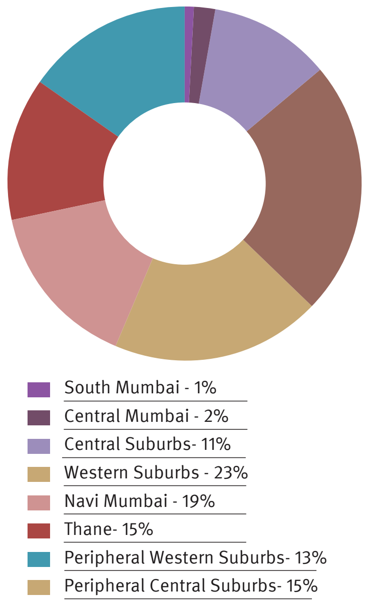
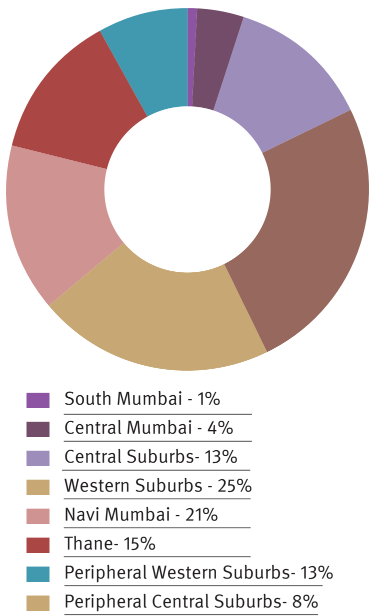
Chart 1: Micro-market Split of Under Construction Units as on December 2012



Source: Knight Frank Research

Chart 2. Micro-market Split of Under Construction Units as on December 2011

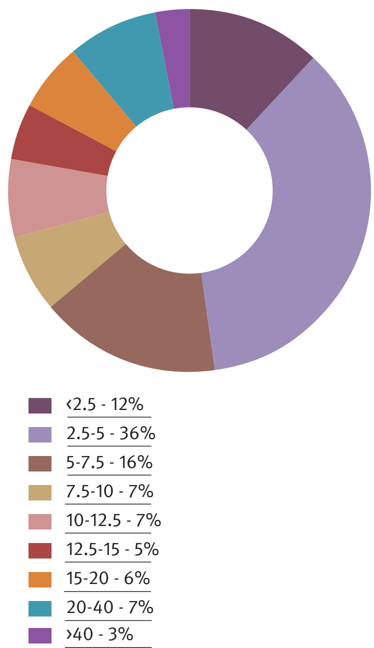


Source: Knight Frank Research

The core of the residential market has been steadily shifting northward of the Mumbai Metropolitan Region over the years as people are prepared to move further away from the Central Business Districts to find an apartment that fits their budget. This has prompted a flurry of construction activity in the peripheral suburbs to accommodate this demographic shift as an estimated 62% of the total units under construction are now concentrated in Thane, Navi Mumbai and the Peripheral Central and Western Suburbs compared to 57% in 2011. The Peripheral Central Suburbs saw a huge spurt in launches in 2012 as its market share jumped from 8% in 2011 to 15% in 2012.

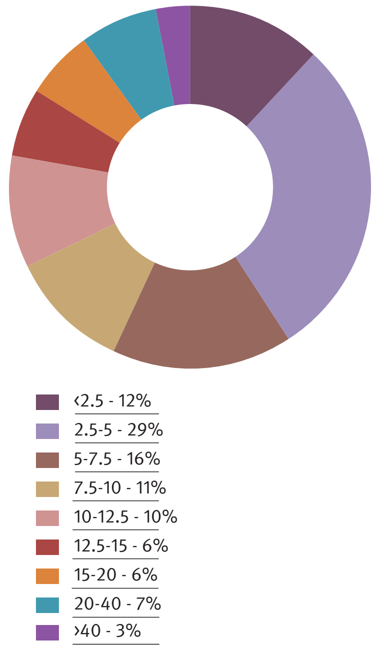
AN ESTIMATED 62% OF THE TOTAL UNITS UNDER CONSTRUCTION ARE NOW CONCENTRATED IN THANE, NAVI MUMBAI AND THE PERIPHERAL CENTRAL AND WESTERN SUBURBS COMPARED TO 57% IN 2011. THE PERIPHERAL CENTRAL SUBURBS SAW A HUGE SPURT IN LAUNCHES IN 2012 AS ITS MARKET SHARE JUMPED FROM 8% IN 2011 TO 15% IN 2012.

Chart 3: Ticket Size Split of Under Construction units as on December 2012 (INR mn.)



Source: Knight Frank Research

Chart 4: Ticket Size Split of Under Construction units as on December 2011 (INR mn.)



Source: Knight Frank Research

Developers are looking to tap into the largest chunk of buyers looking for apartments priced up to INR 7.5 mn. as an estimated 64% of units under construction today are targeted at this price bracket. The fact that the share of the Peripheral Suburbs has jumped from 21% in 2011 to 28% in 2012 has resulted in a proportionate spurt in the number of units launched in the INR. 2.5 mn. - INR. 5.0 mn. category that has grown from 29% to 36% in 2012.

DEVELOPERS ARE LOOKING TO TAP INTO THE LARGEST CHUNK OF BUYERS LOOKING FOR APARTMENTS PRICED UP TO INR 7.5 MN. AS AN ESTIMATED 64% OF UNITS UNDER CONSTRUCTION TODAY ARE TARGETED AT THIS PRICE BRACKET.

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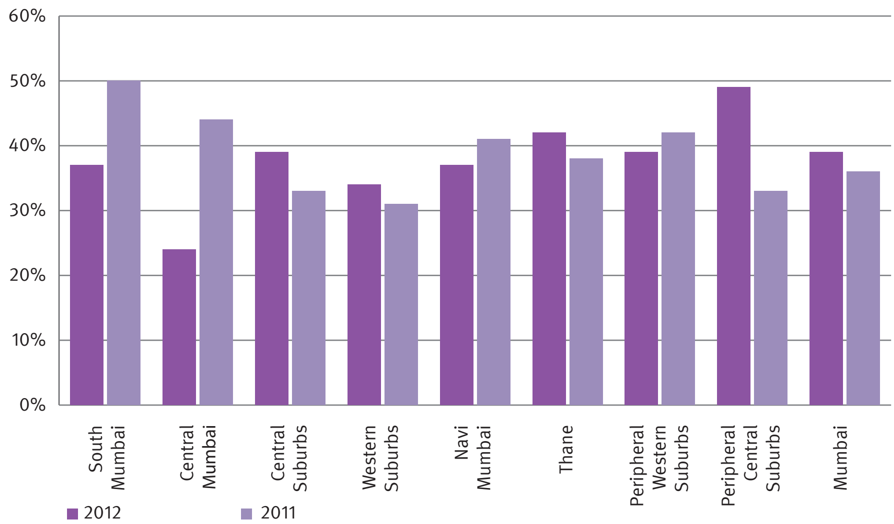
Chart 5: Unsold Stock as a % of Launched Units



Source: Knight Frank Research

If one analyses the unsold inventory levels across ticket sizes in the Mumbai market, it is observed that they are as high as 49% for units launched in the INR 20 mn. and above price bracket vis-a-vis 39% for the overall Mumbai market.

THE MUMBAI MARKET CURRENTLY HAS AN ESTIMATED 83,000 UNITS OF UNSOLD INVENTORY WHICH IS APPROXIMATELY 39% OF THE UNITS UNDER CONSTRUCTION. GOING BY THE AVERAGE ABSORPTION RATE OF THE PRECEDING EIGHT QUARTERS, THIS TRANSLATES TO APPROXIMATELY SIX QUARTERS WORTH OF UNSOLD INVENTORY AT THE END OF 2012 COMPARED TO FIVE QUARTERS FOR THE PREVIOUS YEAR.

The Mumbai market currently has an estimated 83,000 units of unsold inventory which is approximately 39% of the units under construction. Going by the average absorption rate of the preceding eight quarters, this translates to approximately six quarters worth of unsold inventory at the end of 2012 compared to five quarters for the previous year.

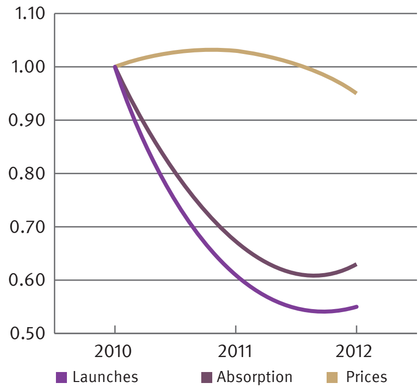
The central suburban corridor from Sion in the Central Suburbs upto Badlapur in the Peripheral Central Suburbs experienced the maximum number of launches in 2012 and consequently had the highest unsold inventory levels in the market. Approximately 35% of the planned launches in 2013 will be in these micro-markets which is likely to put further pressure on unsold inventory levels and prices prevailing there. Also, the peripheral markets attract a lot of investor interest due to the lower ticket sizes and the promise of superior returns. The investors' segment which makes up approximately 25% - 30% of the market demand has been observed to be actively offloading its real estate holdings, thereby adding significant shadow supply into these micro-markets.

The South and Central Mumbai micro-markets which experienced few new launches in 2012 saw unsold inventory levels fall the most during the year.

Prices

Prices had stayed steady all through 2011 and the initial part of 2012 in the face of weak demand only due to an even weaker supply scenario. This equilibrium is however shifting as the increasing rate of units launched makes it harder for the market to maintain the same price levels.

Chart 6: Index of Real Estate indicators



Source: Knight Frank Research

That said, prices have been moving in a narrow range in the past four quarters as the market slowly adjusts to the increasing launches. As prices in premium micro-markets tend to be much more volatile compared to the peripheral suburban micro-markets, prices in some South and Central Mumbai locations like Parel, Lower Parel and Mahalaxmi, have declined close to 10% 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 upward. This can be explained by the lower ticket sizes of apartments on offer in these micro-markets which find much more takers than their more premium counterparts.

Developers in a bid to liquidate their higher priced inventory have been more open to negotiation in the premium segment, reducing prices substantially in favour of a sizeable up-front payment. We have also observed the number of cancellations increasing over the past few quarters. This 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.

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Location	Price (Q4 2012) in INR./sq.ft	Price (Q4 2011) in INR./sq.ft
Cuffe Parade	35000-71000	34000-73000
Malabar Hill	60000-76000	60000-76000
Nepean Sea Road	47000-74000	55000-75000
Mahalaxmi	21000-42000	20000-44000
Worli	25000-48000	25000-55000
Lower Parel	21000-38000	22000-38500
Prabhadevi	22000-45000	20000-45000
Dadar	20000-31000	18000-30000
Bandra West	26000-42000	21000-41000
Andheri	14000-18500	11000-17000
Goregoan	11000-12500	9500-11500
Kandivali	8900-13000	8500-13000
Borivali	9500-13500	9400-13000
Mira Road	5200-6500	5000-6300
Virar	3700-4500	3500-4300
Naigaon East	3400-3800	3200-3500
Vasai	4100-4500	4000-4400
Chembur	9500-16000	9000-15000
Bhandup	8000-9500	7500-9000
Mulund	8000-10000	7500-9500
Thane	6000-8700	5500-8700
Dombivali	3500-5000	3000-4000
Kalyan	3400-4300	3100-4200
Ambernath	2500-3800	2500-3800
Vashi	7000-10000	7000-9500
Airoli	6500-7200	6500-7200
Kopar Khairane	6000-7500	6000-7500
Kharghar	4500-7500	4500-7100
Panvel	3300-6500	3000-6500

Source: Knight Frank Research

On the flipside, government efforts to usher in the next generation of reforms and get us closer to fiscal consolidation will help improve the investment climate. Also, a drop in interest rates following reduction in policy rates by RBI in a phased manner as inflation has seemingly topped out, should aid demand and help keep prices buoyant. In the short term however, demand is likely to remain subdued as the market continues to bottom out in the backdrop of a sluggish economy. Hence, we believe that a more pronounced rationalisation of prices is warranted in 2013.

DEMAND IS LIKELY TO REMAIN SUBDUED AS THE MARKET CONTINUES TO BOTTOM OUT IN THE BACKDROP OF A SLUGGISH ECONOMY. HENCE, WE BELIEVE THAT A MORE PRONOUNCED RATIONALISATION OF PRICES IS WARRANTED IN 2013.

Outlook

The fact that real estate prices are showing signs of weakening suggests that the long standing stalemate between buyers and builders is finally turning in the buyers' favour. The increase in inventories coupled with stagnating absorption levels are bound to put further pressure on prices. The rise in interest costs for the realty sector and decline in net profits during 2012 compared to the previous period is likely to compel developers to lighten unsold inventory levels and deleverage their balance sheets.

THE FACT THAT REAL ESTATE PRICES ARE SHOWING SIGNS OF WEAKENING SUGGESTS THAT THE LONG STANDING STALEMATE BETWEEN BUYERS AND BUILDERS IS FINALLY TURNING IN THE BUYERS' FAVOUR.

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