REALTY MELTDOWN

PEs buy in as realtors face a cash crunch

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Realty index of the BSE has fallen by 56% since January when it touched its record 52-week high of 13,848.09.

Source: BSE

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Experts predict realty firms will turn to debt as PE turns expensive and these players focus on specific projects

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BANGALORE

A downturn in demand for housing and the shortage of debt and investor capital in the real estate business may be bad news for realtors. But, it comes as a huge investment opportunity for private equity (PE) players. Such firms say it is a good time for them to strike deals with developers facing a cash crunch for completing their projects and fund expansion.

"India is a land of scarcity and due to the downturn, more opportunistic distress investments will be made now," says Aashish Kalra, co-founder and managing director, Trikona Capital, a real estate fund management firm.

Real estate firms have seen a blip this year as high inflation, put at 12.1% by latest government estimates, a 13-year high, and rising interest rates as well as steep property prices have turned away buyers. With companies reporting at least a 50% fall in the cash on their books, debt being both scarce and expensive, and the option of going public looking difficult at the moment with the realty index of the Bombay Stock Exchange (BSE) fallen by 56% since January when it touched its record 52-week high of 13,848.09, developers hardly have any options than raise money from PE firms, says Prakash Gurbaxani, founder and chief executive, **QVC Realty**, a Bangalore-based real estate firm.

Investors say the current market situation and mellowed sentiments have made deals more feasible for them. "What we have on hand now are saner valuations, more willing partners (both promoters and investors)," says Kuldip Chawlla, director, Red Fort Capital Advisors, a real estate PE firm. Chawlla says valuations, depending on cities and locations, are down between 10% and 40%.

In the first six months of this year, PE firms invested around $5.8 billion or Rs24,360 crore across 56 real estate companies or special purpose vehicles (SPVs) built around projects, compared with $4.5 billion in 48 companies or SPVs in the year-ago period, according to Venture Intelligence, a firm that tracks venture capital and PE activity in India. Some of the prominent deals this year include: **Standard Chartered Plc.**'s $830 million investment in **DLF Assets Ltd**, a firm owned by the promoters of **DLF Ltd**, and steel tycoon L.N. Mittal and San Francisco-based Farallon Capital's investment of $399 million in **Indiabulls Real Estate Ltd**.

> PE firms have invested around $5.8 billion in real estate cos in the first half of 2008

Experts say that despite the recent slump they continue to be bullish on realty as fundamentals of demand egged on by growing incomes and supply remain unchanged. "There is a definite increase in the number people approaching (us) for deals. It hasn't gone up from one to 10, but quite substantial, actually," says Chetan Dave, chief executive and managing director, SUN-Apollo Real Estate Advisors. Dave says that besides getting more realistic valuations now, the quality of deals has improved with realistic market viability and an assurance that the developer can deliver on time.

Still, some realtors charge PE players with playing Shylock. "Developers, who have expansion plans or unfinished projects, are in a desperate state. In such a situation, when they approach private equity firms, they (PE players) will take advantage," says J.C. Sharma, managing director, **Sobha Developers Ltd**.

Some experts say investors ask for a higher return due to risks involved in India realty. "Compared with a country like the US, the transparency is not very high in real estate development in India. For PEs it means taking a huge risk, so they will ask for a bigger returns," says an analyst from a Mumbai-based brokerage, who requested anonymity.

With the PE option turning expensive, there are some firms such as Bangalore-based **Puravankara Projects Ltd** that plan to raise money through debt and not equity.

"Private equity funding has become extremely expensive, we would rather go for debt," says Ravi Ramu, director, finance, Puravankara Projects. Developers are hopeful that the situation will improve for them once inflation rates come down and interest rates follow.

Industry insiders predict the emphasis will shift to funding individual projects as returns are perceived to be fairly safe in them. Also, with demand for commercial space (used by offices, retailers and software or back office firms) and budget hotels expected to increase, developers in these segments are expected to have an easier run with investors interested in funding projects in niches such as these.

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