

## Residential real estate: How to play the multi-year upcycle?

The residential sector has witnessed a strong, broad-based recovery over the past 12 months. With highly favorable macro conditions, the sector is at the start of a multi-year upcycle.

In our view, investing in to senior secured credit offers the best risk-reward to play this coming upcycle.

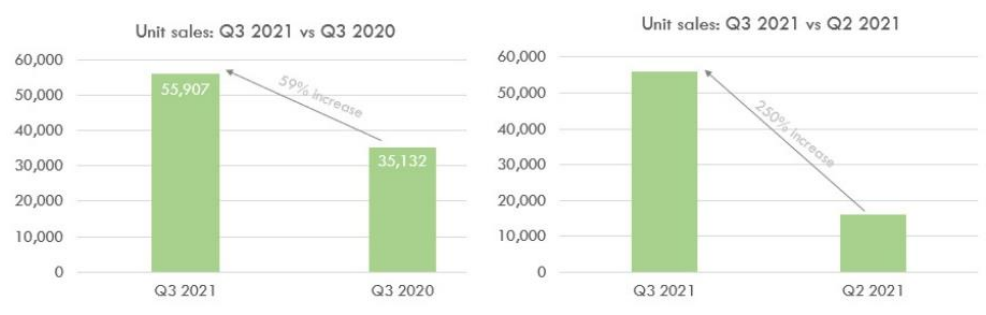
Real estate is a core sector for the Indian economy which is expected to reach a market size of US\$1 trillion by 2030 and contribute ~13% to the country's GDP by 2025(1). Within real estate, the residential segment has the largest contribution of ~80%.

**After a prolonged 6-year down cycle, residential has seen a strong, broad-based recovery in the last 12 months, laying the foundation for an upcycle over next several years.** Further, COVID-19 has provided a positive nudge to the sector already benefiting from a favorable macro setup.

Source: (1) IBEF, Sep 2021

### Strong bounce back in residential sales

Housing sale across tier 1 cities witnessed a sharp rebound in Q3 2021 – up 59% YoY. It also promptly recovered from second lockdown related disruptions in Q1 2021 – up ~250% QoQ.



Source: Proptiger real insights, Economic Times

### Listed players (proxy for performing developers) continue to do exceptionally well

Performing, credible developers continue to gain market share as home buyers increasingly seek quality and assurance of timely delivery.

- Listed developers more than doubled (2.2x) their sales over the last 4 years – growth of 21% p.a. despite a slow market during these years
- Q3 2021 sales were 70%+ higher than the same quarter last year



- Realizations have been increasing steadily – Q3 2021 realization was ~14% higher than same quarter last year and 6% higher than avg. realization in FY21

	FY17	FY18	FY19	FY20	FY21	Sep-21
Avg. INR/sf	6,811	7,104	6,310	6,573	7,028	7,446
% Y-o-Y	-	4%	-11%	4%	7%	6%
CAGR	2%					

Source: Quarterly Investor Presentations

### What is driving this stellar performance?

- Housing affordability is nearly the best it has ever been, driven by:
  - All time low mortgage rates – 400-450 bps reduction in last 5 years
  - Time correction in residential prices i.e. virtually no growth in capital values vs. income growth of ~8% p.a. and inflation of ~5%



Source: Morgan Stanley Research (India Property, 28 Nov 2021), Jefferies India Property: 2021 Outlook - A New Cycle Begins (Report dated 10 January 2021)

- Rising savings and wealth effect from buoyant capital markets
- COVID-19 catalyzing the need for home up-gradation and home ownership
- Supportive government policies – reduction in stamp duty, premium waivers/discounts, higher tax deductions for affordable homes, etc.

## What are market experts / research houses saying?

"In over 50 years of my work life, I have not seen housing affordability better than where it is today in India. I have not seen such easy liquidity conditions and interest rates at such record low levels," HDFC Chairman Deepak Parekh said. "Most importantly, I have not seen such a burning desire to be a homeowner than in these current times." This isn't just feel-good talk, it is real. The Indian real estate market is on the cusp of a new growth cycle and it is important that we make the best of it," Parekh said. "The reason why I am optimistic about the future is that while home sales have been happening, the real shot in the arm has been the recent pipeline of new launches," he said. This is the greatest mark of confidence for the future, he added ([The Indian Express](#), 30 Oct 2021)

"The housing market indeed emerged stronger than before, with speculative buying and selling getting eliminated and end-users emerging as the strongest market drivers in the primary sales segment. Luxury has come back strongly, too. The pandemic caused latent demand to come bubbling to the surface and today, the housing market is firing on all cylinders," said Anuj Puri, Chairman - ANAROCK Group ([Moneycontrol](#), 12 Nov 2021)

"A new residential cycle start should become evident over 2021 as both end-users and investors get back into action. We expect residential sales to cross 2019 levels, inventory to fall to 8-year low by end'21 and prices to rise by 10%+ over next two years." Jefferies Research (India Property: 2021 Outlook - A New Cycle Begins, 10 January 2021)

"Return of residential, after 6 years - The industry has struggled over the last six years, with a 2% CAGR in prices and 25-30% lower average volumes per annum than the preceding five years. The drivers of for the next up-cycle are falling into place - five to six years of pent-up demand, strong affordability, cycle low mortgage rates, higher savings, wealth effect from capital markets and customers need to upgrade. The recovery so far has been broad based across metros, micro-markets and price points. We expect this to continue for next several quarters. There are early signs of pricing power." Morgan Stanley Research (Siding with Fundamentals Over Valuations; Staying Attractive, 28 Nov 2021)

## What is the future outlook and how do you play this residential upcycle?

With the strong fundamentals in-place for the sector and low starting point of residential sale volume (~35-40% below last cycle peak in 2012-2013), we expect volume and price growth to accelerate over the coming years.

In our view, investments in senior secured credit (project finance) to the sector offer the best risk-reward to play this upcycle.

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