

Real Estate & Hospitality Sector

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Residential Realty Market To Remain Subdued; Positive On Rental Portfolio

We expect 3QFY19 earnings of NESCO and Phoenix Mills to decline by 21% and 6%, respectively, QoQ. The earnings of Prestige Estates Projects, Sobha, Brigade Enterprises and Lemon Tree Hotels are expected to increase by 3.6%, 2.3%, 10.5% and 221.4%, respectively, QoQ. The earnings of NESCO are likely to decline QoQ because of its Building 1 being vacated on account of planned IT park restructuring. We have assigned Sell rating to Sobha with a target price of Rs376, Buy rating to NESCO with a target price of Rs764, Buy rating to Prestige Estates Projects with a target price of Rs256, Buy rating to Phoenix Mills with a target price of Rs791 and also Buy rating to Brigade Enterprises with a target price of Rs290. We are also bullish on Lemon Tree Hotels and have Buy rating on it with a target price of Rs92.

We expect overall sales of realty companies to improve: Sales of Sobha, Prestige Estates Projects, Brigade Enterprises and Phoenix Mills are likely to increase by 5%, 5%, 5.0% and 4.0%, respectively, QoQ. However, NESCO's sales are expected to decline 12% QoQ because of the ongoing restructuring of its IT park (Building 1 vacated). Sales in case of Phoenix Mills are expected to increase by 4% YoY supported by: 1) Rise in rental rates. 2) Increase in the occupancy rate of PMC (Phoenix Market City) located at Kurla, Mumbai.

EBITDA margin to improve on the back of write-backs: EBITDA margins of Sobha and Prestige Estates Projects are expected to improve to 21% and 28%, respectively, in 3QFY19. We expect revenue recognition of completed projects in the coming four to six quarters, which were earlier recognised based on POCM (reversed recognition of revenues in 1QFY19) leading to improved EBITDA margin. However, the residential real estate market continues to remain subdued, resulting in pricing pressure. EBITDA margin of NESCO is expected at 62% in 3QFY19, a decline on YoY basis because of the hospitality segment getting reported as a part of consolidated results.

Change in accounting methodology of revenue recognition to impact earnings positively: Earnings of Sobha are expected at Rs628mn in 3QFY19. The earnings growth is because of revenue recognition of completed projects which were earlier accounted using POCM. However, Prestige Estates Projects is expected to report earnings of Rs1,060mn in 3QFY19, an increase of 3.6% QoQ. We expect NESCO to report earnings of Rs385mn in 3QFY19, which represents a 21.8% decline on QoQ basis. Despite its Building 1 getting vacated, strong performance of BEC (Bombay Exhibition Centre) and hospitality segment is expected to support earnings.

Residential prices expected to fall further in next two years: Compared to peak sales in FY12, residential sales volume declined 35% in Mumbai, 60% in Gurugram and 20% in Bengaluru. The price decline has been the sharpest in Gurugram at 20%-25% (in some localities it has been 35%-40%). Prices in Mumbai also continue to be under pressure. Going forward, the combined impact of a slowing economy and regulatory changes in residential real estate segment could lead to prices declining by 10%-15% in Mumbai and by 20% in Bengaluru.

We maintain our negative view on residential segment, but rental portfolio to outperform: Weak sales together with rising cost pressure are expected to be compounded by negative news flow arising from the implementation of Real Estate (Regulatory and Development) Act or RERA and Insolvency & Bankruptcy Code. Likely further decline in residential real estate prices together with rising costs will add to the pressure on valuation. However, high demand and lower additions in commercial and retail space have led to tightening of vacancy rate and increase in lease rentals. We have a negative view on the residential segment, but positive view on rental portfolios of Prestige Estates Projects, NESCO, Brigade Enterprises and Phoenix Mills.

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(Rsmn)	Rating	TP	CMP	Sales			EBITDA			EBITDA margin (%)			PAT		
Company		(Rs)	(Rs)	3QFY19E	YoY (%)	QoQ (%)	3QFY19E	YoY (%)	QoQ (%)	3QFY19E	2QFY19	3QFY18	3QFY19E	YoY (%)	QoQ (%)
Sobha	Sell	376	458	6,930	0.2	5.2	1,466	6.7	4.6	21.2	21.3	19.9	628	17.6	2.3
NESCO	Buy	764	446	879	9.0	(12.2)	545	(6.9)	(17.5)	62.0	66.0	72.6	385	(12.0)	(21.8)
Prestige Estates	Buy	256	236	13,886	9.1	5.0	3,843	51.1	5.0	27.7	27.7	20.0	1,060	6.8	3.6
Brigade Enterprises	Buy	290	220	8,662	104.3	4.9	2,307	44.8	5.4	26.6	26.5	37.6	956	112.0	10.5
Lemon Tree Hotels	Buy	92	76	1,436	8.5	0.6	449	5.0	3.5	31.3	28.0	32.3	120	17.1	221.4
Phoenix Mills	Buy	791	578	4,209	1.0	4.0	2,025	0.6	4.9	49.4	49.0	49.6	552	(9.8)	(5.6)
Grand total/avg.				36,002	22.0	1.3	10,635	16.9	(0.9)	36.3	36.4	38.7	3,701	21.9	35.1

Source: Nirmal Bang Institutional Equities Research

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BUY > 15%

ACCUMULATE -5% to 15%

SELL < -5%

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