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Commercial, warehousing to lead realty investments

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Real estate continues to throw exciting opportunities for investments. As is true for any investment cycle, the leadership of the segment changes hands and in this cycle, we can certainly see commercial, warehousing and logistics segments taking the lead in the current cycle.

Over the last three to five years, we have seen commercial segment performing well with vacancies at a 10-year low. Mainly on account of lack of Grade-A office spaces being developed that has led to a demand-supply mismatch. Going forward, we are seeing increasing demand on account of corporate recovery, which shall continue to sustain the commercial office space market.

Even post the last two year's upward movement in capital prices of office assets, capital appreciation has still not fully played out and I believe corporate sector revival will further fuel the outperformance for this asset class. For 2018 - 2020, the increase in absorption of office spaces is expected to be at a healthy average rate of 7%-10%.

Warehousing is another segment where we are seeing increasing institutional participation. On the policy front, warehousing is a beneficiary of the government's infrastructure push with the largest-ever rail and road budget of Rs 1.48 trillion and Rs 1.21 trillion, respectively in 2018-19. This consistent fund allocation for rail and road infrastructure is importantly being complemented by improved execution capabilities.

With GST also in place, the organized logistics industry will catapult as the demand for integrated logistics services will increase. Warehousing in urban infringes will form a significant portion of the logistics opportunity and institutional and developer participation is set to increase. For funds and institutions with longer investment horizons, warehousing will be an excellent fit with regular yield income over the course of the next 5-6 years along with capital appreciation on account of increase in the underlying land values of these urban infringes.

Additional absorption of more than 200 million sq ft is expected to be generated by 2020. This is being driven by GST and infrastructure push, E-commerce being a key sector, growth in manufacturing and consumption.

Entry strategy is critical for a successfully warehousing investment. Entering at a stage where land acquisition and approvals have been completed and development is ongoing to just about to start is optimal. This will enable a fund to make higher returns as compared to entering at a ready preleased warehouse stage and mitigating risks of acquisition and approvals. To mitigate the leasing risk, forward agreements with logistics and manufacturing companies, e-commerce players can be entered into. With such companies increasingly looking for built-to-suit warehouses, it works out to be an ideal situation for the developer, investor and tenant.

The residential segment has definitely seen a challenging environment over the last 2-3 years where we saw both absorption and launches reducing significantly. Regulatory changes, reduced consumer sentiment, inability of developers to deliver projects have all contributed to the negativity. This has led to price stagnation and demand moderation. During the last four years, the growth in residential prices in most of the top eight cities of India has been below retail inflation growth and the gap has progressively increased since the first half of 2016. This has in fact significantly improved home affordability and average ticket sizes of housing units in most cities.

The long awaited drop in prices is a healthy step toward market recovery as this along with other measures such as reduction

in unit sizes across cities will boost home-buyer affordability and eventually get buyers back to the market. The pace at which developers align themselves to the new regulatory norms and launch new products in the right ticket sizes that appeal to the homebuyer's interests, will determine the trajectory of the market going forward.

What has been a green shoot in the residential segment is the long awaited focus on affordable housing. Through a slew of policies benefiting everyone in the affordable housing spectrum including developers, buyers and fund providers, the government has attracted private developers towards these projects. Granting infrastructure status and home loan sops and interest subsidies under the Pradhan Mantri Awas Yojna has fired up both the supply and the demand for these homes. With these incentives, affordable housing has established a presence in most developer's drawing boards and we shall see much more activity in this space. It is estimated that in the affordable housing segment, the existing supply constitutes just 5% of the overall demand!

What still remains unseen is the execution capability of developers as well as approval timelines. As this also comes under the same approval process, any delays can impact an affordable housing project significantly.

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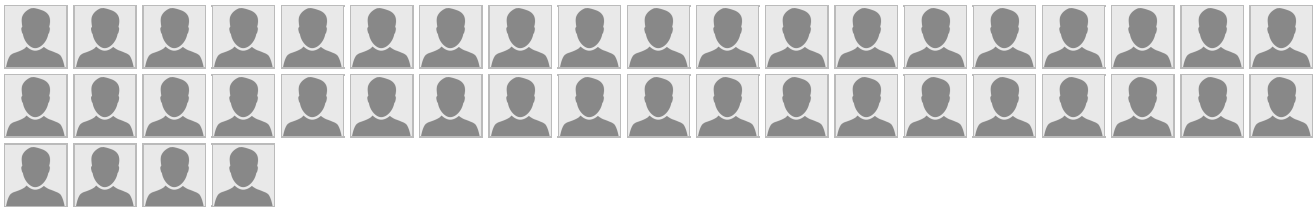
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