April 15, 2020

Real Estate: Weak quarter…

Commercial segment revenues expected to remain stable

So far, the commercial segment stood as an outlier in the real estate sector with leasing activity touching new highs. As per a CBRE report, leasing activity was robust in CY19 with gross absorption registering 25% YoY growth to 61.6 million sq ft (msf). Bengaluru, followed by Hyderabad, NCR and Mumbai, together accounted for 75% of the office space take up. Against this, office space supply grew robustly by 50% YoY to 52.4 msf albeit lower than overall leasing during CY19. As a result, vacancies have fallen vis-à-vis increase in rental rates for Grade-A assets. Though this trend is positive for our coverage stocks like Brigade Enterprises and Phoenix Mills, we are mindful of the fact that the recent Covid-19 pandemic may disrupt leasing activity in the near term. Nonetheless, we may not see a significant financial impact in Q4FY20 since the nationwide lockdown was implemented from the last week of March. Also, while some impact may be seen on revenues arising from retails spaces leasing, we expect no such impact on office space revenues in Q4FY20.

Housing market to be impacted in near term

The residential real estate sector had set forth a tone of recovery with sales momentum showing an increase for the first time in CY18 after years of consistent decline. This uptrend further continued in CY19 with residential sales rising, albeit at a slower rate of 5% YoY. While the yearly trend seems healthy, the housing market has seen some slowdown since H2CY19 amid liquidity crunch following NBFC crisis & the effects of the ban on subvention schemes. To counter these challenges, the government introduced several revival measures viz. ₹ 25,000 crore Alternate Investment Fund to provide support to ~4.58 lakh stalled housing units. While we were hopeful that the housing market would swing back to recovery path with such measures in place, the impact of lockdown seems to have simply added to the woes of the sector. We not only anticipate a pushback in demand but also a delay in launch of new projects, which would only aggravate challenges for developers across the sector, going ahead. The only positive we see in the current scenario is that in case of a significant slowdown in the housing market, highly leveraged developers and/or those with weaker financials could cease to exist amid cash flow problems, which could lead to massive consolidation, thus benefiting larger, prudent players.

Coverage sales volume to decline 1.9% YoY in Q4FY20E

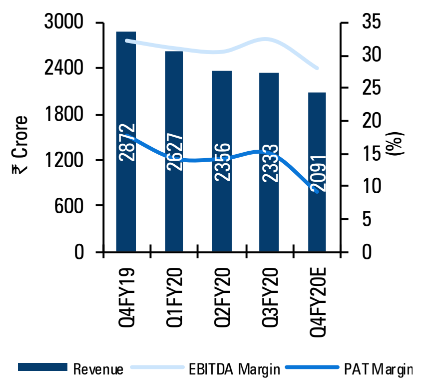
We anticipate Covid-19 led lockdown would impact some deal closures for real estate players leading to lower sales volumes in Q4FY20E. Bengaluru-based players have shown some resilience in sales volumes. Hence, we anticipate relatively lower impact on operational performance of Brigade Enterprises. Overall, we expect sales volumes of our coverage universe to decline 1.9% YoY to 10.8 lakh sq ft (lsf) in Q4FY20E largely on account of 22.4% YoY decline in Oberoi Realty's sales volumes to 1.1 lsf due to the developer having exposure to high-ticket size projects in the MMR region, which could have been the worst hit in the current scenario.

Exhibit 1: Estimates for Q4FY20E: (Real Estate & Building Material) (₹ crore)

Company	Revenue	Change (%)		EBITDA	Change (%)		PAT	Change (%)	
	Q4FY20E	YoY	QoQ	Q4FY20E	YoY	QoQ	Q4FY20E	YoY	QoQ
Oberoi Realty	333.0	-41.9	-36.9	133.3	-36.4	-42.0	81.0	-48.0	-45.3
The Phoenix Mills	404.4	-44.1	-21.0	202.2	-46.4	-22.0	50.8	-77.8	-44.7
Brigade Enterprises	636.5	-16.3	15.2	156.0	-27.6	0.3	14.7	-75.4	-70.2
Kajaria Ceramics	716.5	-12.1	-3.3	94.4	-23.2	-15.2	45.3	-31.4	-26.3
Total	**2,090.4**	**-27.2**	**-10.4**	**585.9**	**-36.7**	**-22.5**	**191.8**	**-62.4**	**-45.4**

Source: Company, ICICI Direct Research

Topline & Profitability (Real Estate Universe)



Sales volumes

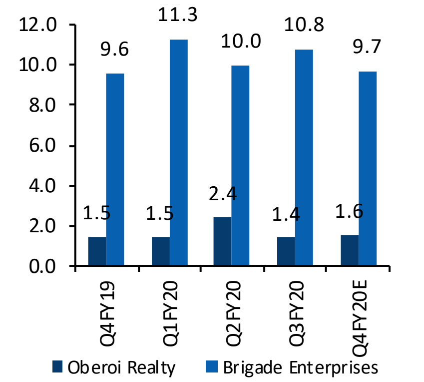


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Exhibit 2: Company Specific Views (Real Estate)

Company	Remarks
Oberoi Realty	Amid the nationwide lockdown, we anticipate sales volumes would have been impacted in Q4FY20E. Thus, we expect Oberoi' (ORL) sales volumes to de-grow 22.4% YoY to 1.12 lakh sq ft (lsf) in Q4FY20E. On the financial front, we expect topline to de-grow 41.8% YoY to ₹ 333.3 crore on account of lower revenue recognition expected in Q4FY20E. Overall, we anticipate ORL net income will decline 48.0% YoY at ₹ 81.0 crore in Q4FY20E. **Key Monitorable:** : Progress on new launches such as Thane & Exquisite-III in Goregaon, progress on annuity portfolio, commentary on sales volumes expected ahead due to impact of lockdown
The Phoenix Mills	We expect The Phoenix Mills' (Phoenix) revenues to de-grow 40.1% YoY to ₹ 433.2 crore mainly on account of lower revenue recognition in the residential real estate segment (₹ 28.8 crore expected to be recognised in Q4FY20E vs. ₹ 307.2 crore recognised in Q4FY19). However, even on the core portfolio front (retail, commercial and hospitality business), we expect revenues to de-grow 2.8% YoY to ₹ 404.4 crore since retail and hospitality segments are expected to be impacted the most amid the complete closure of malls ordered by the government and lower occupancy expected due to travel restrictions imposed during the lockdown. The EBITDA margin is expected to contract 210 bps to 50% in Q4FY20E. Overall, we expect PAT to de-grow 77.8% YoY to ₹ 50.8 crore in Q4FY20E. **Key Monitorable:** Commentary on treatment of contract with retailers due to the lockdown, progress on under construction mall assets
Brigade Enterprises	Some Bengaluru-based real estate players have shown some resilience in residential sales volumes despite the impact of the lockdown. Also, Brigade Enterprises (BEL) remained comfortable on achieving 4 msf overall sales volumes in FY20. We note that the company had already achieved 3.2 msf sales volumes in 9MFY20. Since the company had launched several big ticket projects in the affordable and mid premium category in 9MFY20 we expect its sales volume to be less impacted in Q4FY20E. With this, we expect BEL's sales volumes to grow 1.3% YoY to 9.7 lakh sq ft in Q4FY20E despite challenging environment. On the financial front, we expect the topline to de-grow 16.2% YoY to ₹ 636.5 crore in Q4FY20E. Overall, we expect BEL's net income to decline 75.4% YoY to ₹ 14.7 crore. **Key Monitorable:** Pre-leasing and construction progress on Brigade Tech Garden and WTC, Chennai
Kajaria Ceramics	The overall demand dynamics in the ceramic tiles sector still seems to be subdued following stress in real estate sector. On the other hand, competition intensity continues to remain high in the sector. In this scenario, prudent ceramic players like Kajaria have given due attention to their credit control at the expense of sales to maintain their healthy balance sheet. However, we anticipate Kajaria's sales volumes would have been hit by the nationwide lockdown and lower demand for ceramic due to the discretionary nature of the product. Hence, we anticipate Kajaria's sales volume will de-grow 13.3% YoY to 19.5 MSM in Q4FY20E. On the revenue front, we expect it to de-grow 11.3% YoY to ₹ 723.4 crore mainly led by volume growth. Additionally, with gas prices expected to remain broadly stable in Q4FY20E, we expect EBITDA margins to contract 184 bps QoQ to 13.2%. Overall, we expect the bottomline to post de-growth of 31.4% YoY to ₹ 45.3 crore. **Key Monitorables:** : Management commentary on sector outlook, commentary on gas pricing and product pricing dynamics in the industry

Source: Company, ICICI Direct Research

Exhibit 3: Real Estate Coverage Universe

Sector / Company	CMP (₹)	TP(₹)	Rating	M Cap (₹ Cr)	EPS (₹) FY19	EPS (₹) FY20E	EPS (₹) FY21E	P/E (x) FY19	P/E (x) FY20E	P/E (x) FY21E	EV/EBITDA (x) FY19	EV/EBITDA (x) FY20E	EV/EBITDA (x) FY21E	P/B (x) FY19	P/B (x) FY20E	P/B (x) FY21E	RoE (%) FY19	RoE (%) FY20E	RoE (%) FY21E
Oberoi Realty (OBEREA)	297	450	Buy	10,799	22.5	14.5	21.2	13.2	20.5	14.0	7.8	11.6	9.4	1.3	1.3	1.2	10.1	6.1	6.8
The Phoenix Mills (PHOMIL)	488	740	Buy	7,473	27.5	20.0	16.3	17.8	24.4	30.0	11.3	11.5	12.2	2.2	2.0	1.8	10.7	7.9	6.1
Brigade Enterprises (BRIENT)	138	160	Buy	2,817	11.7	8.7	-0.2	11.7	15.9	NA	8.0	8.6	10.2	0.9	0.9	1.2	11.1	8.1	NM
Kajaria Ceramics (KAJCER)	352	420	Hold	5,593	14.2	16.1	16.0	24.7	21.8	22.0	12.1	12.7	12.0	1.9	1.9	1.9	14.4	14.5	13.0

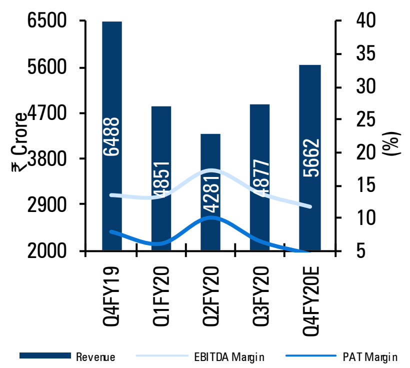
Source: Company, Bloomberg, ICICI Direct Research

Infrastructure: Pain in the offing

Expect tendering & awarding activity to get delayed

Overall tendering has continued to remain muted with ₹ 4,71,954 crore worth tenders floated in 11MFY20 vs. ₹ 8,74,375 crore YoY. The overall tendering seems to have gathered some pace post August, 2019 with average tender value increased to ~₹ 42,000 crore in 11MFY20 vs. ~₹ 27,000 crore in April-July, 2019 due to impact of central elections. Over the long term, this could further pick up as the Finance Minister has announced a roadmap for infrastructure investment in FY20-25 under the National Infrastructure Pipeline (NIP). According to this, capital expenditure in the infrastructure sector in FY20-25 is projected at ₹ 102 lakh crore, which could lead to strong ramp up of tendering activity, going ahead. However, in the interim, there could be some setback in the project tendering and awarding could now be deferred by at least three to six months since most government executives/offices are working at minimum workforce due to lockdown amid the Covid-19 impact.

Topline & Profitability (Infra Universe)



Near term pain expected for road based players

Total road tendering in 11MFY20 was at just ₹ 1,67,167 crore vs. ₹ 3,18,935 crore YoY. Also, only ₹ 27,697 crore worth road projects were awarded in 11MFY20 vs. ₹ 72, 944 crore YoY. NHAI had awarded only 3,200 km road projects have been awarded in 10MFY20 against target of 10,000 km in FY20 on account of issues like land availability. However, as of February, 2020, it had floated bids for 40 HAM and 50 EPC projects, which were expected to be awarded in the rest of Q4FY20. However, we have not observed project awarding. Road projects worth only ₹ 3,099 crore were awarded in February, 2020. While this was expected to show some improvement with the government making efforts mainly on land acquisition front, the Covid-19 impact could only add further to delays since it could take some time for economic activity to get back on track post lifting of the lockdown. On the toll collection front, media reports indicate that NHAI has ordered BOT/TOT toll operators to stop collecting toll fees from users on national highways during the lockdown period. Consequently, BOT toll assets are bound to witness pressure in near term toll collection as well as debt servicing.

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Universe expected to show sharp PAT de-growth in Q4FY20E

We expect our road & construction universe to post revenue de-growth by 12.7% YoY to ₹ 5,661.8 crore mainly on account of 25.0% YoY de-growth in NCC's revenues to ₹ 2,540.4 crore in Q4FY20E. The EBITDA margin of our universe is expected to contract 180 bps YoY to 11.7% in Q4FY20E. Overall, we expect our universe PAT to de-grow 50.4% YoY to ₹ 253.5 crore in Q4FY20E.

Exhibit 4: Estimates for Q3FY20E: (Roads & Construction) (₹ crore)

Company	Revenue	Change (%)		EBITDA	Change (%)		PAT	Change (%)	
	Q4FY20E	YoY	QoQ	Q4FY20E	YoY	QoQ	Q4FY20E	YoY	QoQ
Ashoka Buildcon	1,349.1	3.2	37.2	148.4	-18.1	19.4	91.9	-12.6	7.5
PNC Infratech	1,092.5	1.6	-10.3	142.5	-5.8	-16.8	58.5	-58.2	-24.2
NCC	2,540.4	-25.0	20.0	266.7	-32.9	6.7	72.6	-58.4	-34.2
KNR Construction	679.8	-5.0	21.8	105.0	-27.1	-15.6	30.5	-66.9	-24.1
Total	**5,661.8**	**-12.7**	**16.1**	**662.6**	**-24.2**	**-1.1**	**253.5**	**-50.4**	**-19.1**

Source: Company, ICICI Direct Research

Exhibit 5: Exhibit 2: Company Specific Views (Roads & Construction)

Company	Remarks
Ashoka Buildcon	All seven HAM projects are under execution, which should support revenues in Q4FY20E. However, we build in one week of revenue loss on account of nationwide lockdown. Hence, we expect revenues to grow 3.2% YoY to ₹ 1,349.1 crore in Q4FY20E. EBITDA margins are expected to contract 287 bps YoY to 11.0%, on account of higher fixed costs due to a week of revenue loss. On the profitability front, we expect PAT to de-grow 12.5% YoY to ₹ 91.9 crore on account of lower topline growth and EBITDA margin contraction expected in Q4FY20E. **Key monitorable:** Management commentary on execution ahead and status on monetisation of Ashoka Concessions
NCC Ltd	Deriving comfort from the several major executable projects in NCC's order book, the management was confident of clocking revenues worth ~₹ 3,000 crore in Q4FY20E. However, we anticipate revenues may have not met this guidance due to blanket halt on construction activity for a week amid nationwide lockdown. Hence, we expect NCC's topline to de-grow 25.0% YoY to ₹ 2,540.4 crore in Q4FY20E. EBITDA margin is expected to contract 124 bps YoY to 10.5% due to lower operational leverage. Overall, NCC's bottomline is expected to decline 58.4% YoY to ₹ 72.6 crore. **Key Monitorable**: Management commentary on order inflows, execution, status on Andhra Pradesh orders, receivables and net debt
PNC Infratech	With execution in six out of seven HAM projects in full swing, PNC's execution is expected to be strong in Q4FY20E. However, we take into account the impact of lockdown, which could restrict higher YoY revenue growth for the company during the quarter. Hence, we expect PNC Infratech's to report flattish topline growth to ₹ 1,078.5 crore in Q4FY20E. The EBITDA margins are expected at 13.5%, broadly in-line with management guidance of 13.5-14.0%. Overall, PNC's bottomline is expected to de-grow 58.2% YoY to ₹ 58.5 crore in Q4FY20E since it received one-time net tax rebate worth ₹ 24.1 crore in Q4FY19. **Key Monitorable**: Management commentary on order inflows, progress on HAM projects
KNR Constructions	Execution in three out of five HAM projects and large fast track irrigation orders in Q4FY20E are expected to support revenues. However, like any other construction company in our coverage universe, we take into account one week of revenue loss due to the nationwide lockdown. Hence, we expect revenues to de-grow 5.0% YoY to ₹ 679.8 crore. EBITDA margin is expected to contract 469 bps YoY to 15.4%. Overall, we expect bottomline to grow 66.9% YoY to ₹ 30.5 crore due to EBITDA margin contraction, higher interest expenses, higher depreciation and higher tax rate expected in Q4FY20E **Key Monitorable:** Land acquisition status on balance HAM projects

Source: Company, ICICI Direct Research

Exhibit 6: Road Coverage Universe

Sector / Company	CMP			M Cap	EPS (₹)			P/E (x)			/EBITDA (x)			P/B (x)			RoE (%)		
	(₹)	TP(₹)	Rating	(₹ Cr)	FY19	FY20E	FY21E	FY19	FY20E	FY21E	FY19	FY20E	FY21E	FY19	FY20E	FY21E	FY19	FY20E	FY21E
KNR Constructions (KNRCON)	186	240	Buy	2,615	18.7	14.6	15.0	9.9	12.7	12.4	6.7	6.1	5.3	1.8	1.6	1.4	18.6	12.7	11.6
PNC Infratech (PNCINF)	112	125	Buy	2,868	11.9	15.9	12.7	9.4	7.0	8.8	6.4	4.4	5.0	1.4	1.2	1.0	14.4	16.4	11.7
Ashoka Buildcon (ASHBUI)	49	UR	UR	1,628	-1.4	-1.5	0.0	NA	NA	NA	5.0	5.0	4.3	5.7	6.6	6.6	6.9	-17.1	0.3
NCC (NAGCON)	24	UR	UR	1,433	9.4	5.8	4.9	2.6	4.1	4.9	2.2	3.1	3.3	0.3	0.3	0.3	11.9	7.0	5.6

Source: Company, ICICI Direct Research, Reuters

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