project maitree

revolutionising redevelopment

Sample report on developer appraisal
Sample Co-operative Housing Society,
February, 2016

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Background

Sample CHSL floated a tender on 16th September 2015, inviting bids for the redevelopment of their society located at abc location. The society received interest from fourteen developers, out of which only three developers have submitted their offers. During the tender scrutinization only one developer-'Sample Developer' was found to eligible as a contender.

The society has appointed 'Project Maitree' to conduct an appraisal of 'Sample Developer' as a third party evaluator. The parameters of the evolution are defined in the objectives of the assignments.

Objectives of the assignment

1. Evaluate the developer experience of work in last five years from the perspective of 'Domain Experience', 'Overall Experience' and 'Sector (Location) Experience'. The experience will be calculated from the perspective of supply and not the number of years.
2. Conduct the performance evaluation of all the bidder (developer) based upon the construction velocity, sales velocity, delay and future commitments
3. Balance sheet analysis of the bidder to evaluate cash flow conditions, commitments and leverage.
4. Prepare benchmarking analysis and recognize the associate risk to the project.

Report structure

- Part:1: Technical evaluation explained about the developer's supply wise bifurcation in various real estate asset classes, experience of the developer in redevelopment projects and proposed developments.
- Part:2: Performance based evaluation focused on the ongoing projects of the developer's. The analytics explained, whether developer was able to match the construction inflow through the sales of inventories or not, levels of project delay, developer's construction velocity, developer's sales velocity and various relevant aspect to it.
- Part:3: Financial evaluation explained the developer's current liabilities and investment in various asset classes and emerging risk out of it. It also explained the net cash flow of the developers emerging from the operational income and highlights the threat pertaining to it.

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Key findings and report Summary

Sample Developer can be considered as a cash rich developer. Developer's major liability is 0.35 Mn sqft built up area project at Napeasea road stuck since long (at least three years). This primarily resulted into low performance rating, 'D'. Category 'D' rated developer means, developer is neither able to offload its goods, nor construct and hence the delivery is being compromised. This can be validated from the trend of declining revenue in the P&L of balance sheet as well as declining trend in the net cash flow from the operating activities. The developer is over leveraged currently (3.7 – secured loan to net equity), the fund raised were primarily used for purchase of development rights/ lands, investments in mutual funds and short term unsecured lending to related party.

The developer is eying at the market improvement and creating the land banks through mortgage of unyielding properties. The current market research suggest that one can eye on the market improvement during 2018, as the current price is stagnant in residential real estate market and there is also an improvement in end-users' income along with continue reduction/ stability in the lower interest rate for the housing finance. Considering this fact and developers strategy, there is a very less chance of the developer initiating the project in next 1.5 years. In case he kicks off the projects in a positive scenario, the project delays are inevitable. Members' should take an inform decision considering the time line of at least 1.5 years to 2 years.

The developer has shifted from self-funding to debt and hence society should ensure that there is a strict provision of 'no mortgage shall be allowed on the society's land or any premises' in development agreement.

The existing offer for additional area may not fulfil the aspiration of up-gradation from the existing house. In which case, society members are likely to increase their carpet area by paying upfront to the developer. This might end up as zero or minimum investment in the project from the developer. Reduction in the investment may bring down the project priority as the risk is reduced. This shall result in to the delay of project. In given context we recommend that members should link the payment of additional area with the construction progress and society shall not allow anyone to adjust it from the corpus. Society shall take complete corpus from the developer.

1. Technical appraisal

The section evaluates the developer's (Sample Developer's) technical ability to execute the residential redevelopment project in ward K-E of WS-I zone of building proposal department. The key parameters of the appraisal are listed below.

- Developer's experience with reference to,
  - Ongoing and executed projects in various real estate asset classes (Residential, Retail, Commercial, etc)
  - Historical behaviour of the project launch.
  - Experience in dealing with different nature of land tenure/ development (CHSL Redevelopment, Slum Redevelopment, MHADA, Brown field development, etc)
- Domain experience with reference to project approvals in the Zone WS-I of building proposal.
- Location level experience in with reference projects executed in ward K-E.

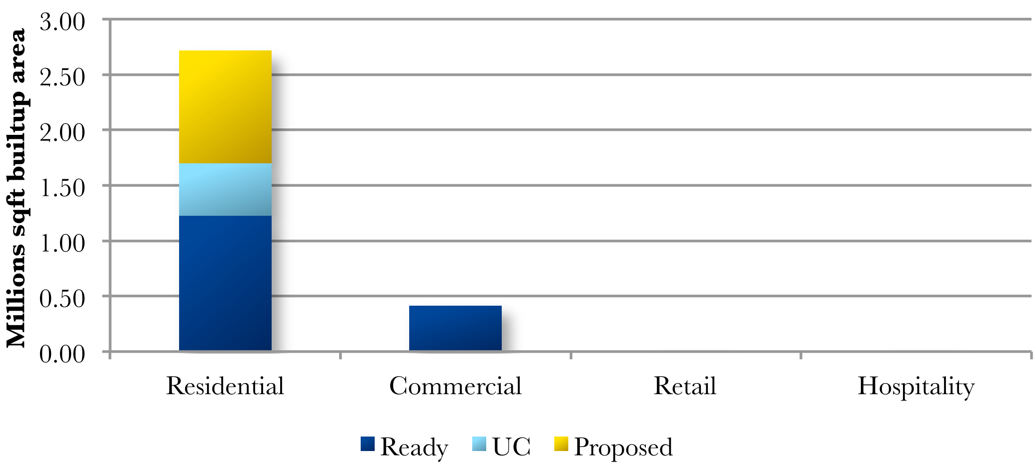
1.1 Developer Experience

The Sample Developer has currently two ongoing projects, a project name 'XYZ-1' in Andheri- East and project 'XYZ-2' on Napeansea road. There are two proposed slum redevelopment, a project at Worli (currently rehab building is under construction) and a project at Goregaon (Annexure-II is awaited). The group has its presence in Mumbai since 1971 and completed 59 projects.

1.1.1 Experience in various real estate asset classes

Sample Developer has presence in the residential as well as commercial real estate asset classes. Based upon the information shared by the developer, the group has executed approximately 1.23Mn sqft of residential built up area since 2003. Residential built up area under construction is 0.47Mn sqft and proposed built up area is approximately 1.0Mn sqft. The developer has also executed the 0.4 Mn sqft of commercial office space in Andheri- East since 1995.

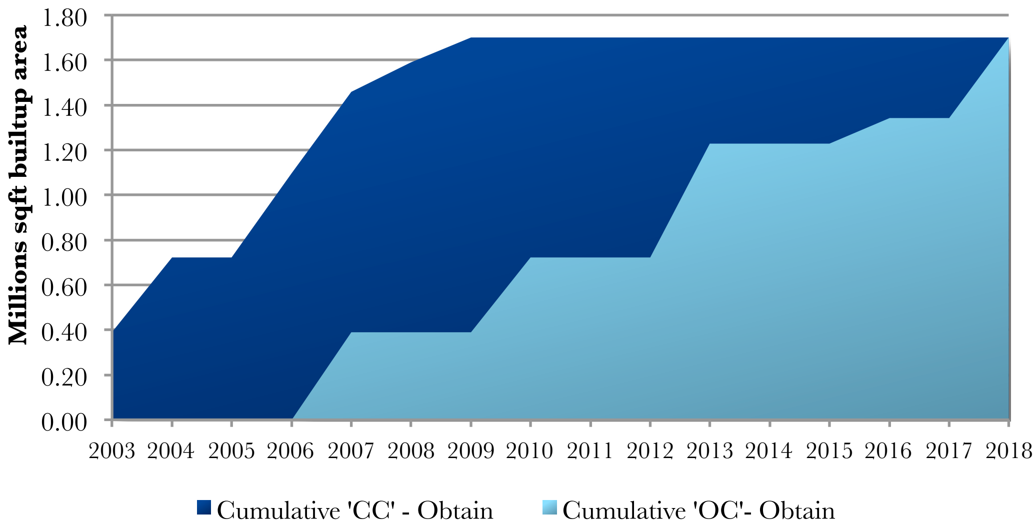
Figure 1 Built up area supply in million sqft against the real estate asset classes



1.1.2 Residential project launch

Sample Developer has cumulatively obtained CC (Commencement Certificate) for 1.70 Mn sqft of residential built up area since 2003. The group has so far OC (Occupancy Certificate) for 1.23 Mn Sqft of residential built up area and proposed to obtain the OC for 0.11 Mn Sqft residential built up area in 2016 and 0.36 Mn sqft residential built up area in 2018. The developer hasn't launch any new residential projects for sale since 2009.

Figure 2 Historical behaviour of new launch and possession

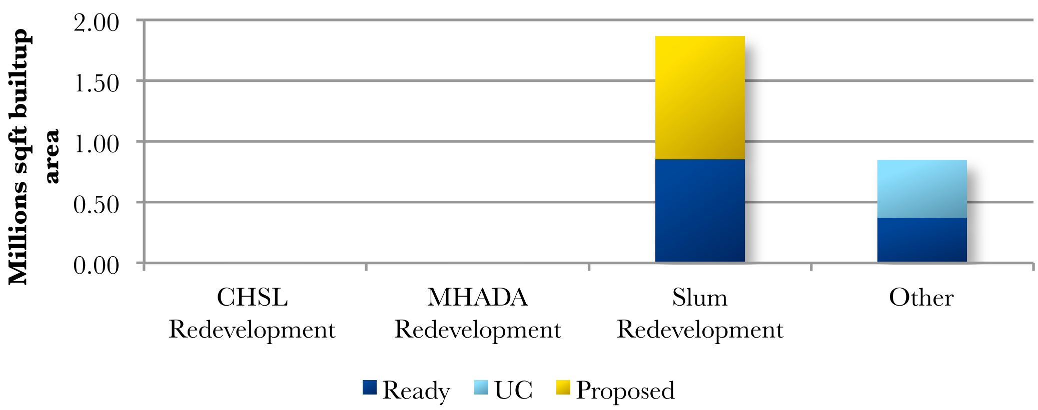


1.1.3 Experience in dealing with different nature of residential development

Sample Developer has been primarily into the slum redevelopment; the group has completed 0.85 Mn sqft of built up area (mainly in Goregaon-East) of slum redevelopment and 1.01 Mn sqft is proposed in Worli and Goregaon.

Under the others category developer has completed 0.37 Mn sqft of built up area of Vandan is the privately owned land (old bungalow) at Walkeshwar, ongoing 0.11 Mn sqft of built up area of 'XYZ-1' is on the freehold (land being purchased from the society) land. The 0.36 Mn sqft of built up area of 'XYZ-2' is unknown but most likely it's on privately owned land only.

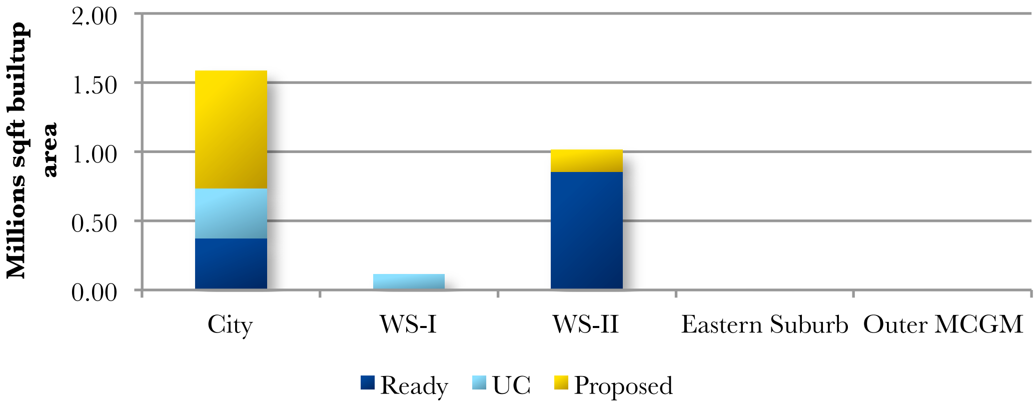
Figure 3 Million sqft built up area bifurcation against the nature of development in ready, under construction and proposed stage



1.2 Domain experience in residential projects

Sample Developer has regulatory exposure in the city as well as in the suburbs. Their completed project supply in terms of built up area is highest in the zone WS-II of building proposal department. They also have an exposure of dealing in the zone WS-I of building proposal department due to their only project in the Andheri- East.

Figure 4 Building proposal zone wise supply of million sqft built up area

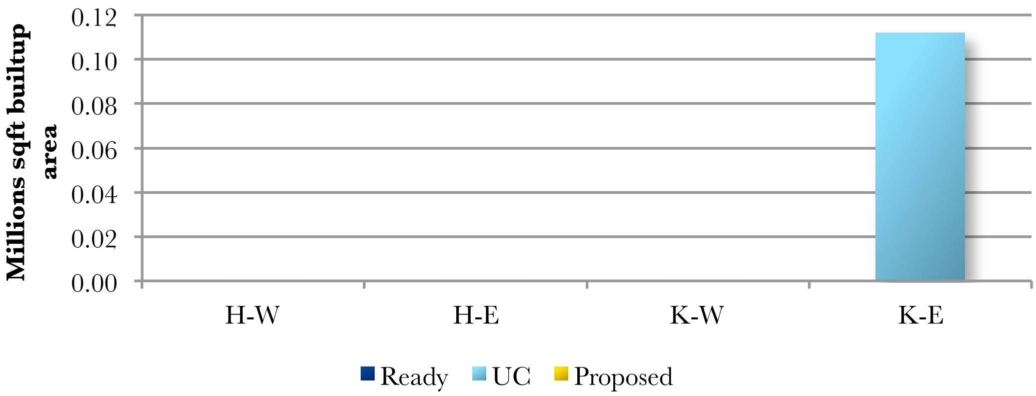


As the developer is not having any project under the CHSL redevelopment category further bifurcation analysis of building proposal and zone wise redevelopment projects is not done.

1.3 Location level experience in residential development

Zone WS-I of building proposal is composed of four wards, H-W, H-E, K-E and K-W. The site falls under the ward K-E of zone WS-I, and as a result, there are likely chances that developer is familiar with the local condition pertaining to the aviation related issues. Apart from the residential development, the developer has also accomplished two commercial projects of 0.41 Mn sqft built up area in the ward K-E. This exposure in the local condition may work in favour of the society.

Figure 5 Ward wise bifurcation of million sqft built up area in zone WS-I of building proposal department in ready, under construction and proposed category



Note: There was no documented evidence found in the developer's profile regarding environmental clearance. But, the developer had already completed the buildings above 2lac sqft of constructed area. Thus, we have presumed that he must be aware about the challenges related to environmental clearance.

2. Performance appraisal

The section discusses associated project risks through the performance evaluation of various ongoing projects of the developer. High performance project represents the balance of sales velocity, construction velocity and commitment towards the delivery. Deficiency in any of the parameters will lead to an impact on the cash flows, i.e. higher velocity of construction against low sales velocity will impact the cash flow negatively and in such situation normally projects are put on hold which eventually impact delay of the delivery. Performance appraisal represents, at what level developer is stuck in the maze of realty.

The Sample Developer has two ongoing projects, 'XYZ-1' at Andheri East and 'XYZ-2' at Napeansea road. The performance evaluation is based upon these two projects only.

2.1 Delivery efficiency

Delivery efficiency is inversely proportionate to the estimated project delay, lesser the project delay higher the delivery efficiency. In the current market situation we have considered upto six (6) months of delay, if the delay increases more than six (6) months it will start impacting the delivery efficiency.

Project delay are calculated through two methods, method one is based upon the difference in commitment, i.e. during the project survey in Q1 FY 13-14 developer committed the possession in July 2015 but survey in Q3 FY 13-14 developer changes his commitment to Dec 2015. This means the project is on running on a delay of 5 months. Second method is based upon the estimation of the project time line and identification of delay, i.e. a stand alone tower of seven story in MCGM should not take more then 30 Months to complete, any additional time taken from 30th month onwards shall be counted in delay.

Table 1 Delivery efficiency of ongoing projects

	'XYZ-1' (1)	**'XYZ-2' (2)**
Built up area in sqft (a)	1,11,999	3,59,378
Date of CC (b)	Sep- 2009	Nov- 2007
Ideal duration required to complete the project (c)	30 Months	60 Months
Estimated date of completion (d=b+c)	Mar-2012	Nov- 2012
Proposed date of completion (e)	Oct-2016	Dec-2018
Delay in months (f=e-d)	55 Months	73 Months
Weighted Average Delay ($g=(\Sigma a_i f_i/\Sigma f_i$)	68 Months	
Delivery Efficiency (h=6/g)	**8.73%**	

2.2 Construction efficiency

Construction efficiency is the ratio of achieved construction velocity and desired construction velocity. Construction velocity is derived from monthly builtup area constructed divided by total built up area where by monthly built up area constructed is calculated through division of constructed built up area and months passed by. Desired construction velocity is derived from desired monthly built up area to be constructed divided by total builtup area, where by desired monthly built up area to be constructed is calculated through division of total built up area to be constructed and desired project duration. Construction efficiency indicates the influence of the construction delay on the project delivery.

Table 2 Construction efficiency of ongoing projects

	'XYZ-1' (1)	'XYZ-2' (2)
Built up area in sqft (a)	1,11,999	3,59,378
Date of CC (b)	Sep- 2009	Nov- 2007
Construction completed in percentage as on Q3 2015 -16 (c)	75%	60%
Months passed by (d)	75 Months	97 Months
Construction velocity achieved (e= (((a*c)/d)/a)	1.00%	0.62%
Desire project time line (f)	30 Months	60 Months
Desire construction velocity (g=((a/f)/a)	3.33%	1.67%
Construction efficiency (h=e/g)	30.03%	37.20%
Weighted average construction efficiency ($i=(\Sigma a_i h_i/\Sigma h_i)$	**35.42%**	

2.3 Sales efficiency

Sales in the projects are representation of the company's cash flow and performance. Sales efficiency is derived from the ratio of achieved sales velocity and desired sales velocity. Achieved sales velocity is derived from monthly built up area sales divided by total built up area where by monthly built up area sales is calculated through division of built up area sales and months passed till then. Desired sales velocity is derived from desire monthly sales of built up area divided by total built up area, where by desire monthly sales of built up area is calculated through division of total built up area to be sold and desire project duration.

Table 3 Sales efficiency of ongoing projects

	'XYZ-1' (1)	'XYZ-2' (2)
Built up area in sqft (a)	1,11,999	3,59,378
Date of CC (b)	Sep- 2009	Nov- 2007
Sales in percentage as on Q3 2015 -16 (c)	65%	10%
Months passed by (d)	75 Months	97 Months
Sales velocity achieved (e= (((a*c)/d)/a)	0.87%	0.10%
Desire project time line (f)	30 Months	60 Months
Desire sales velocity (g=((a/f)/a)	3.33%	1.67%
Sales efficiency (h=e/g)	26.00%	6.19%
Weighted average sales efficiency ($i=(\Sigma a_i h_i/\Sigma h_i)$	**10.89%**	

2.4 Performance rating

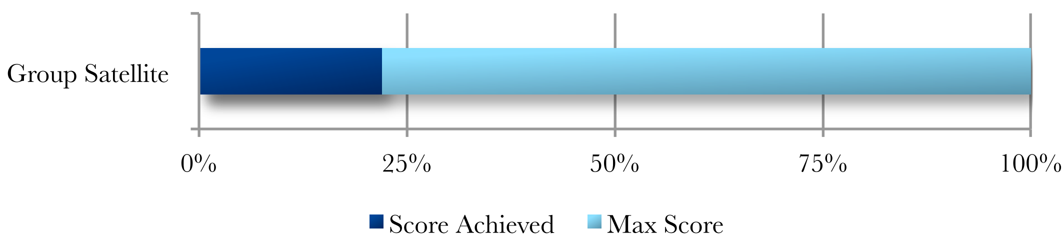
Developers attending the score greater than 75% are 'A' category developers with balance of sales, construction and delivery. Developers falling in the range of 50.01% to 75% are 'B' category developers; developers falling in the range of 25.01% to 50% are 'C' category developers; developers score less than 25% are 'D' category developers.

Table 4 Overall performance rating

	Max Efficiency (1)	Score Efficiency (2)
Delivery efficiency (a)	100%	8.73%
Construction efficiency (b)	100%	35.42%
Sales efficiency (c)	100%	10.89%
Weighted average sales efficiency $(d=(a2^2+b2^2+c2^2)^{1/2} / (a1^2+b1^2+c1^2)^{1/2}$	22%	

The achieved performance score suggest that developer performance rating is 'D'.

Figure 6 Performance rating



3. Financial appraisal

Financial appraisal is discussed in two parts. Part one discusses the changes in liabilities and assets and part two discusses the changes in profit and loss.

3.1 Changes in liabilities and assets

The long term borrowing of the developers between from 2014 to 2015 increased by Rs. 517.61 cr are primarily diverted towards the investments, inventories (land/development rights) and short-term loans and advance. Following section provide the detail descriptions.

Table 5 Changes in equities and liabilities

I. Equity and Liabilities	2014 Rs. Cr	2015 Rs. Cr	YoY Change
Shareholders' Capital			
Share Capital	53.40	53.40	0%
Reserve and Surplus	136.16	138.56	2%
Subtotal-Shareholders' Capital	189.56	191.95	1%
Non-current liabilities			
Long term borrowings	174.77	692.38	296%
Other long term liabilities	2.28	2.29	0%
Subtotal-Non-current liabilities	177.05	694.67	292%
Current liabilities			
Short term borrowing	132.28	35.24	-73%
Trade Payables	14.93	7.84	-47%
Other current liabilities	771.53	645.83	-16%
Short term provisions	13.11	8.21	-37%
Subtotal-Current liabilities	931.85	697.13	-25%
Total	1298.45	1583.76	22%

Table 6 Changes in assets

II. Assets	2014 Rs. Cr	2015 Rs. Cr	YoY Change
Non-Current Assets			
Fixed Assets	28.13	29.94	6%
Tangible assets	5.90	29.79	
Intangible assets	0.14	0.15	
Capital work in progress	22.09	0.00	
Non-current investments	36.75	36.64	0%
Deferred tax assets (net)	0.43	0.07	-83%

Long term loans and advances	88.42	94.11	6%
Other non-current assets	0.35	0.09	-73%
Subtotal-non current assets	154.08	160.86	4%
Current assets			
Current investments	0.00	3.74	428203%
Inventories	642.76	822.88	28%
Trade receivables	37.67	33.67	-11%
Cash and bank balances	34.66	10.03	-71%
Short term loans and advances	421.18	545.84	30%
Other current assets	8.10	6.73	-17%
Sub total current assets	1144.37	1422.90	24%
Total	1298.45	1583.76	22%

3.1.1 Change in the long-term borrowings

The developer has raised approximately Rs 517 cr from various means. Debt to Net Equity ratio of the developer is 3.70, this means the developer is over leveraged and further funding for the projects would be difficult. This also indicates that developer had moved from self-funding to debt for project executions. Society should ensure going forward that no mortgage of the premise shall be allowed in development agreement.

Table 7 Historical reviews of long term borrowings

Notes:4: Long Term Borrowings	2012 Rs. Cr	2013 Rs. Cr	2014 Rs. Cr	2015 Rs. Cr
Secured				
Non-Interest optionally convertible debentures secured by second charge on specified duplex under construction project and first charge on a residential premises				45.00
Secured- Term loans				
From Bank				
Secured by Mortgage of specified premises and ongoing construction at Andheri (E) and Goregaon (E) and personal guarantee of Two directors	22.37			
Secured by Mortgage of premise at Andheri (E) and personal guarantee of two directors and charge in property of associate company	23.83	19.01	13.49	7.12

Secured by mortgage of property at Andheri (E) and personal guarantee of two directors	35.00			
Secured by hypothecation of vehicle	0.18	0.13	1.59	1.09
Secured by hypothecation of vehicle		1.90	0.00	0.00
Secured by mortgage of premises at Worli, hypothecation of lease rent receivables and personal guarantee of two directors		10.00	8.89	7.78
Secured by mortgage of property and ongoing construction at Andheri (E) and personal guarantee of two directors		30.00	37.00	37.32
From other parties				
Secured by Mortgage of specified duplex in "XYZ-2" project Napean Sea road and personal guarantee of a director	130.00			
Secured by hypothecation of vehicle	0.76	0.67	0.57	0.45
Secured by charge on property of associate company and personal guarantee of two directors		32.00	32.00	5.30
Secured by charge on office property at worli and andheri and personal guarantee of two directors		20.00	20.00	8.31
Secured by Mortgage of specified duplex in "XYZ-2" project at Napeansea road and personal guarantee of a director		150.00	99.90	
Secured by Mortgage of specified duplex in under construction project, hypothecation of receivable and personal guarantee of a director				350.59

Secured by mortgage of plot of land				72.00
	212.14	**263.71**	**213.43**	**489.97**
Less: Current maturities	192.31	82.24	154.55	22.45
Sub total secured from bank	**19.83**	**181.46**	**58.88**	**467.52**
	Unsecured			
Deposits	47.73	44.55	60.97	22.83
Bodies Corporate	26.60	26.79	25.20	125.45
Loans and advances from related parties	9.32			
Optionally fully convertible debentures			29.71	25.88
Compulsory convertible debentures				5.71
Sub total unsecured	**83.65**	**71.34**	**115.89**	**179.86**
Long term borrowing	**103.48**	**252.81**	**174.77**	**692.38**

3.1.2 Change in current investments

During the fiscal year 2014-15 developer's has significantly increase the investment in the mutual funds. There was approximate Rs 3.74 cr invested in the mutual funds.

Table 8 Historical changes in the current investments

Note:15: Current investments (at cost)	**2012**		**2013**		**2014**		**2015**	
In mutual funds (unquoted)	No of unit	Rupees	No of unit	Rupees	No of unit	Rupees	No of unit	Rupees
IDFC Money manager fund- treasury plan inst plan- B Daily Dividend	631	6,355	2,373	23,894				
IDFC Money Manager -treasury plan- plan A daily dividend reinvestment			148	1,494				
Sundaram ultra st fund- inst div reinvest weekly			8,911	97,383	811	7,383	811	8,858
Sundaramulta short term fund regular weekly dividend			199	2,190	120	1,344	164	1,879
Franklin Templetion- Daily Dividend							36,853	3,68,79,132
IDFC Money Manager Fund- Treasury plan inst							48,474	4,88,131

3.1.3 change in inventories

Significant portion (~Rs 50 Cr) of the loan is also diverted towards the land/ development right purchases. This means instead of investing in the project construction developer has exploited the funding for creation of land bank or diverted it to associate companies. This signifies that, there is not much scope of improvement in the future from the perspective of project performance as well as cash flow at current market behaviour.

Table 9 Historical review of change in inventory

Notes:16: Inventories (as valued certified by the management)	2012 Rs. Cr	2013 Rs. Cr	2014 Rs. Cr	2015 Rs. Cr
Property development				
Land and Development rights- unamortised	331.03	385.15	430.63	533.89
Development cost and borrowing cost (including amortised land and development rights)	114.89	150.69	208.23	289.00
Sub total Property development	445.92	535.84	638.86	822.88
Premises	7.79	22.14	3.91	
Total	453.71	557.98	642.76	822.88

3.1.4 Short term loans and advances

During the fiscal year 2014-15 second significant change was observed in short term loans. The developer has given approximately Rs. 100.15 cr unsecured loans and advances to the related parties. Similar trends are observed in balance sheet when promoters are looking for cash exits from the company.

Table 10 Historical review of changes in short term loans and advances

Note: 19: Short term loans and advances (Unsecured considered good)	2012 Rs. Cr	2013 Rs. Cr	2014 Rs. Cr	2015 Rs. Cr
Loan and advances to related parties	100.92	96.34	169.38	269.91
Other loans and advances	119.33	162.14	215.65	218.29
Income tax payment	17.36	21.97	19.97	21.29
Employee loans and advances	0.41	0.24	0.10	0.10
Security deposits	0.29	0.26	3.52	0.50
Advance recoverable in cash	8.54	7.67	12.56	35.76
Total	246.85	288.61	421.18	545.84

The assessment suggest that developer is highly leveraged, and increasing the burden by investing in land banks as against focusing on the construction. In different words developer is capitalizing on the untradeable goods an envisioning the market improvement.

3.2 Changes in Profit and Loss

Revenue from the operation has declined by 11%, however due to the heavy investment activities; income from other sources has increased by 50%. This leads to the increase of the revenue by 11%, but due to high level of borrowings; finance cost is also increased by the 47%. The profit declined from Rs 3.18 cr to Rs 2.40cr. Looking at ongoing projects sales momentum and the borrowing, there are very limited chances of improvement in the profit margins from operation activity.

Table 11 Changes in profit and loss from FY 2013-14 to FY 2014-15

Profit and Loss statement for a year	2014 Rs. Cr	2015 Rs. Cr	YoY Change
Revenue			
Revenue from the operations	74.29	66.11	-11%
Other Income	42.85	64.29	50%
Total Revenue	117.13	130.40	11%
Expanses			
Cost of land, plots, development rights, construction expanse and borrowing costs	142.37	207.46	46%
Change in inventories of premises and property development	-103.21	-183.42	78%
Employee Benefits	6.59	5.44	-17%
Finance cost	55.70	81.89	47%
Depreciation and amortisation	1.41	2.79	98%
Other expanse	9.27	12.56	35%
Total Expanse	112.13	126.72	13%
Profit Before Tax	5.01	3.68	-26%
Tax expense	0.00	0.00	
Current tax	2.00	0.74	-63%
Deferred tax	-0.24	0.36	-249%
Taxation adjustment of earlier years	0.06	0.19	202%
Profit for the period	3.18	2.40	-25%
Earning per equity shares			
Basic and diluted	0.6	0.45	