New realty norms to worsen developers' debt woes

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The Real Estate (Regulation & Development) Act (RERA) would push up debt levels of developers and lead to continued negative cash flows, said property developers and analysts.

Companies in the BSE Realty Index had a total debt of ₹52,598 crore in September 2016, 7.3 per cent higher than a year ago. The companies had an average 0.8 times debt to their total equity.

Debts of top developers are expected to rise by 15-20 per cent in the current financial year, according to industry estimates.

"The RERA will definitely pose challenges for many developers in terms of cash flows. Many were launching projects without approvals and some level of stress will come in," said Anita Arjundas, managing director and chief executive at Mahindra Lifespace Developers, part of the Mahindra group.

The RERA makes it mandatory for developers to keep 70 per cent of the proceeds from a project in an escrow account, thereby restricting their ability to dip into project sales. It also makes it mandatory for developers to obtain all approvals before launching a project, thus prohibiting pre-launches, a favourite method to raise funds.

Ajay Jain, executive director, investment banking, and head, real estate group, at Centrum Investment Banking, said most developers would have to borrow project by project with the RERA.

"Earlier, they were able to complete any project with 50 per cent of the sale proceeds. Now it has come down to 20-30 per cent. The RERA will make matters worse," Jain said.

Home sales have halved in Gurgaon, Noida, Mumbai and Bengaluru in January-March from a year ago, says property data analytics firm PropEquity.

"The slump in sale of residential units will result in continued negative cash flows and push up already high debt levels, resulting in the weakening of the sector's credit profile. The implementation of the RERA will further impact liquidity," said India Ratings and Research in a recent report.

Rajeev Talwar, chief executive at DLF, said property developers would need to become accustomed to a new style of working. "Earlier, they were launching projects even without land. Now they have to buy land, secure all approvals and then launch projects," he said.

Talwar said DLF had worked out its cash flow planning. "We will launch only after completion," he added.

DLF had debts of ₹24,098 crore in September 2016.

"There has to be a financial recalibration as there will be a gap between fund requirement and availability. Since nationalised banks do not fund for all purposes, property developers have to go to non-banking finance companies and private equity funds," said Sandeep Runwal, director at the Runwal group.

Developers do not have room to increase prices, given the slowdown in sales and unsold stock. Arjundas said developers would not be able to increase prices in the next six months due to high inventory levels and a gradual pick-up in demand.

"Prices will remain steady or go up marginally in the near term," she said.

STICKY SITUATION

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