

# Business Line

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## The well-heeled look ahead

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*The real estate market may be looking stretched in the near term, but smart HNIs understand that realty development is an integral part of the India growth story. Much of the recent HNI interest in real estate is driven by the long term bullish prospects of the sector.*

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Some of the favourite destinations of high net worth individuals are New York, London and Dubai

**Maneesh Kumar**

Recent weakness in both the traded asset markets as well as real estate may have diminished their earlier insatiable appetite, but investing in real estate still remains a viable asset class for the discerning high net worth investor (HNI). Historically, HNIs have always demonstrated proclivity towards acquiring real estate. The difference between then and now is that earlier these HNIs were working more on their gut feel, whereas today they take a relatively more scientific approach towards acquiring real estate.

Wealth management companies, such as ASK Wealth Advisors, recommend that 5 per cent of total assets of a client with an assertive risk profile should be invested in alternative assets such as real estate. For a client with an aggressive risk profile, the proportion can go up to 10 per cent of the total assets.

### More investor friendly

Further, the HNI interest in real estate has been buoyed by the availability of leverage, most often from the developer himself. While leverage benefits investors to the extent that they can obtain marketable title upon a small down payment, it also benefits developers as they can offer supplies that can be developed presently with borrowed money.

Presently, despite the credit squeeze, many developers are not asking for anything more than the down payment until project completion and possession. This may, to some extent, be a reflection of the present tepidness of appetite and a demand-supply imbalance. However, financial institutions are still willing to lend to buyers on viable projects.

What drives investor interest in real estate is that a larger pool of available options between commercial and residential properties has been created in recent years. So in effect, investors are looking at a menu of options, each with a different projected internal rate of return, project completion risk and time frame of completion. Never has the property market in India looked so investor-friendly.

Although the market for real estate is not liquid in the strict sense, the fact that there is a spectrum of risk-reward profile among investors also means that early investors may have an opportunity to resell their investment to later-stage investors.

To take a simple example, a moderate risk-taking HNI with an eye to investing would typically invest in a leased commercial property with regular cash flows. A more aggressive HNI would most likely prefer either buying an under-construction residential dwelling and turning it over for a profit, or investing in land and then either develop it or partake in share of profits once the developer develops and sells the project.

At the other end of the spectrum, are investors who may not wish to participate in deal-making directly, and instead want a professional manager to manage their funds.

### More realistic

In the recent past, HNIs have also shown an inclination to invest in real estate private equity funds. Typically, these funds have a lock-in period and 'project' a IRR (internal rate of return) to their investors. Some PE funds have an objective of investing in income generating properties and then passing on the revenue streams as dividends to the investors. But this is not to say that investment in real estate is a free lunch for everyone.

During the quasi-bubble that we witnessed till the beginning of this year, HNIs were sector, builder and geography-agnostic, as there were profits to be made everywhere. However, as values have come to more realistic levels in 2008, HNIs have become more discerning in terms of their preferences, including geographical preferences.

In earlier times, HNIs were investing in Tier 1, 2 as well as Tier 3 cities. In Tier 1 cities, they were pretty indifferent between city centres and properties in the suburbs. But now the foolhardiness has vanished. At present, HNI behaviour is to tread in shallow rather than in uncharted waters. This means investing more in Tier 1 cities such as Delhi NCR, Mumbai, Bangalore, Chennai and some parts of Kolkata.

Interestingly, there is a pattern witnessed of HNIs purchasing properties abroad. Some favourite destinations are New York, London and Dubai. This has been facilitated by the newly available \$200,000 remittance per year allowed by the RBI. So, a family of four can remit up to \$800,000 each year, and this amount can get you a decent property in any of the above mentioned international cities.

### Sound advice

A significant reason for this trend of increased allocation and geographical preference is that HNIs have the benefit of sound investment advice. It is abundantly clear that over the long term — greater than five years — Indian real estate is still a bullish story. Some of the excesses that had got built into the system have been priced out, so there is some level of sanity. But at the same time, it cannot be denied that India will continue with strong GDP growth. The fundamentals of the economy remain strong, and a growing economy needs to fill gaps in infrastructure, including residential and commercial property.

Real estate is an integral part of the India growth story, and any investor in the India story cannot avoid looking at real estate.

In terms of short to intermediate term downturn, retail may probably be the worst hit followed by commercial and residential. In this process, however, smaller developers who don't have hoards of cash will be the hardest hit. Some large developers sitting with cash raised recently through IPOs and private equity will fare better.

Further the excessive supply of space in certain micro markets will affect all developers irrespective of their size. Within this present downturn in the real estate cycle there is an opportunity for a buyer to pick up great values that weren't available till even a few months ago.

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