

# Identifying Stock with Best Investment Value – A Case Study of Brigade Enterprises, Bangalore



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## 1. Real Estate Industry in India- An Overview

The real estate sector in India is one of the most important sectors for India's GDP growth. It contributes to around 6.3% to the total GDP. The Indian real estate market is currently one of the fastest growing markets in the world. This has led to increased keenness among many foreign investors that are investing in many big projects. The estimated market size was USD 78 billion in 2012 which is expected to almost double and become USD 140 billion by 2017. Changing demographics, rising income level and rapid urbanization would be the key factors in fuelling this significant growth. As per CREDAI estimates, the real estate sector alone would have generated close to 7.6 million jobs during the year 2013. CREDAI has also projected that the real estate sector would generate more than 17 million employment opportunities for India by 2025.

The real estate sector in India is largely fragmented and is highly unorganised. However with increased foreign investment, entry of International real estate players and a number of corporate entering this sector, the industry is getting more organised. The phenomenal growth in India's real estate sector in the past decade can be credited to factors like opening of the sector for Foreign Direct Investment (FDI), rapid urbanization and rising income levels of the people. From being a supplier of residential and commercial space; new age concepts like luxury homes, senior citizen homes, student housing and education Institute are fast catching pace.

## 2. Bright Prospects of Real Estate Industry in Bangalore

The State government has launched the Information and communications Technology policy and the Karnataka Electronics policy for the growth of industry in the state. Karnataka is the leading state in electronics and computer software exports, accounting for 38.76% of India's total exports in 2011-12. With the flourishing IT sector, there has been a phenomenal growth in the real estate sector where Bangalore and Mysore are two important real estate markets.

In 2013, Bangalore turned out to be the second largest real estate market with the launch of 1.23 Lakh new units, a figure which was less than the 1.25 Lakh units launched in the Mumbai Metropolitan Region (MMR). Despite a deluge of supply, inventory levels in Bangalore at 80,000 units are much lower compared to 1.1 Lakh in MMR, signifying an inherent demand. Unlike other national markets, prices in Bangalore are stable and affordable in the range of 4,300 per sq ft. All this is good news for investors and home buyers in Bangalore as they get ample affordable options to choose from.

IT hub **Bangalore** is expected to witness the second highest demand for office space in the Asia Pacific region during 2014 in a list topped by Tokyo, according to property consultant Cushman and Wakefield (C&W).

" Bangalore is expected to see the second highest absorption in the APAC region and the highest demand in the country owing to expansion of the IT, ITeS and multi-national companies," C&W said in a statement. Tokyo is forecast to see the highest office absorption among the 30 cities in Asia in 2014 at 7.6 million sq ft, followed by Bangalore at 2nd position and Manila at 3rd, with expected absorption of 6.3 million sq ft and 6 million sq ft, respectively, during 2014. "The office demand is likely to reach 60 million sq ft in all 30 major cities tracked within Asia Pacific," C&W said. The National Capital Region (NCR) is projected to witness the sixth highest net absorption of offices space in the region, at 3.7 million sq ft representing a rise of approximately 10 per cent over 2013. "The demand for commercial office space will strengthen going forward in 2014 and 2015. The oversupply situation, which most cities across the country are witnessing, will ease from 2014 onwards as economic conditions improve domestically and globally," C&W Executive Managing Director, South Asia, Sanjay Dutt said. He said that the growth of IT/ITeS sector has been greatly affected by the global economic scenario. "With a more favourable dollar to rupee exchange rate and the improvement in global economic scenario, we expect the industry to benefit in terms of increase in exports of IT services from India," Dutt said.

An expected improvement in overall economic condition in the second half of 2014 would result in companies undertaking more expansion activities, which will propel the demand for office space. Net absorption is likely to increase by 31 per cent over 2013 at 29.5 million sq ft. The cities to record majority of the net absorption will be similar to 2013, with Bangalore, Mumbai, Delhi NCR and Pune leading the pack. There is increased interest by private equity players for projects with strong fundamentals and Bangalore remains a bright spot in India for foreign investors as indicated by the trends from last 2 years. Property buyers know that location matters the most. This also holds true when one buys the stocks of listed builders. In 2013, Mumbai based developers such as Oberoi Realty and HDIL saw their revenues drop 30 percent, while sales increased 40 percent for Bangalore-based developers Prestige Estates, Sobha Developers and Brigade Enterprises. The Continuing robustness in the Bangalore real Estate Market lends strength to Brigade Enterprises which develops both Residential and

Commercial Property. The Company's established brand name in the local markets diversified revenue mix from property sale, lease rentals and hospitality, a strong pipeline of projects and expansions in allied segments such as retirement homes should aid earnings growth prospects. Investors can buy the Brigade stock as its share is attractively priced. The current share price of Rs.77 is far more than its low PE level of 12 times. Brigade's main line of Business is developing integrated enclaves, homes, Commercial space, retail outlets, hospitality property and Infrastructure such as schools. Revenues from the sale of residential and commercial property form the main stay of the company accounting for over 60% of its total revenues. While most of the development is in Bangalore, Brigade has also expanded its operations to Mysore, Chennai, Chikmagalur and Kochi. Revenue and earnings have grown at an average rate of 15% annually in the last five years. The company earns 20 percent of its revenue from rents on its commercial properties in Bangalore. These include office space in the world Trade centre, retail properties such as Orion Mall and Outlets such as Solitair. Leasing is a high margin business, commanding operating margin of over 85%. From this view point it is come to know that Brigade's Primary market of Bangalore is quite robust with demand growth expected in both the residential and commercial segments helped by IT segment. Residential sales growth has averaged 30 percent since 2010 according to data from Vestian, a Bangalore based real estate advisory.

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**Focus of the study:** This study is apart from numerical and analytical aspects and it teaches new investors that whether Real estate industry is suitable or not for the Investment. Besides this study justifies the selection of Brigade enterprises that investment in this company is the viable option.

### Growth Prospects

The Company is now constructing 11.7million Sq.ft(msf) in Devanahalli and Whitefield sub urban of Bangalore, its share in the joint development is 8.7msf. Brigade is also developing retirement homes as part of its Devanahalli project. A foray in to this growing market should aid its revenue and margins. Commercial space totaling 0.86 msf is also being developed in multiple cities. Office and retail projects in Bangalore and an IT park in Kochi account for 40 per cent each of the ongoing development. Sale price in both its residential and commercial segments improved last year.

### Stable Financials

Brigade's revenues in 2013-14 increased from 16 percent from 2012-13 toRs.916 crore and its profits grew 40 percent year on year to Rs.90 crore. The company's net margin increased from 8 percent last year to 10 percent now. The company's total debt as on March2014 is Rs. 843 crore down from Rs.985 crore a year ago.Nearly half the debt is utilized in the leased properties. Leverage levels are at a comfortable 0.7times.The company's cost of borrowing also dropped to around 12.2 percent, from over 13 percent last year, lowering the interest expense.

Brigade's credit rating was upgraded in January to A minus from BBB plus by ICRA, which should help it avail itself of debt at a lower cost. Thanks to its rental income of around Rs.40 crore a quarter, Brigade has positive cash flows from its operations. Cash Collection from residential sales has also been robust, with 1370 crore collected in 2013-14, on a sale of nearly the same amount. The company is the regular dividend payer. For 2013-14, the company has announced a dividend of Rs.2 per share, up from Rs. 1.5 a share paid last year.

## 3. On the back of Bright and Stable Financials

### Exhibit-1 Outlook on Asset and Liability Matching

(Rs. In Crores)

S.No.	Details	FY14	FY13	FY12	FY11	Trend	Score
1	Reserves and Surplus	115.96	109.59	89.02	76.08	Positive	1
2	Long term Loans Provisions	22.5	42	67	69	Positive	1
3	Long term Borrowing	634.91	779.58	872.04	923.89	Positive	1
4	Short term Borrowing	163.9	297.4	324	365	Positive	1
5	Trade Receivables	350.1	155.7	126.68	112	Positive	1

6	Cash and Cash Equivalents	405.3	350.7	156.07	134.56	Positive	1
7	Profit or Loss for the year	898	642.5	577	427.89	Positive	1
8	Rent Received in Advance	4.00	1.67	0.83	0.56	Positive	1
9	Other Non Operating Income	14.23	7.47	6.23	5.34	Positive	1
	Total						9

It had been proved that Asset and Liability employment and positioning aspects were absolutely on the positive side. Out of nine variables none was found to be negative. These variables were the key indicators to the investors.

#### Exhibit-2 Key Result Areas of Brigade Enterprises

S.No.	Particulars	FY14	FY13	FY12	FY11	FY10	Trend	Score
1	Net Sales	962.70	834.60	651	491.10	391.40	Positive	1
2	EBITDA	291.50	220.80	180.90	168.90	84.70	Positive	1
3	Interest Expenses	68.8	82.88	89.70	93.42	97.40	Positive	1
4	PBT	123.50	53.70	67.30	123.90	47.00	Positive	1
5	Net worth	1268.00	1213.90	1156.90	1130.20	1008.20	Positive	1
6	Debt	932.20	1048.10	693.50	923.20	766.60	Negative	0
7	Net Fixed Assets	1477.80	1441.70	2326.40	1223.90	1084.90	Negative	0
8	Inventory	1132.00	909.90	668.90	793.90	629.60	Negative	0
10	EPS	8	5.5	5.1	4.70	4.2	Positive	1
11	ROE	9.5	4.90	4.9	10.70	4.70	Positive	1
12	ROCE	9.5	6.30	6.90	6.90	3.20	Positive	1
13	Interest Coverage	6.20	3.40	2.10	2.4	1.6	Positive	1
	Total							10

In tune with Asset and liability matching out of above mentioned 13 profitability variables, 10 variables were found to be positive. Brigade stocks are lands and apartments, highly illiquid in nature. Due to that, debt, net fixed assets and Inventory were piling up. However, the firm was able to ensure its steady growth in term of sales, the positive sales effect was reflected in Net worth, EBITDA, ROC, ROCE and EPS. There was the positive sign on the part of operating expenses as well and it has been that Interest expenses were totally under control.

#### 4. Questions

1. Explain the outlook of Real Estate Industry in India
2. Why would investors have to prefer Bangalore real estate companies over all other companies located in various parts of India?
3. Give reasons for the Best Buy stock from the outlook of Brigade.
4. Explain the outcome of containing Interest Expenses and increasing Interest coverage effect.