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Mumbai

CRISIL Research assigns IPO grade 2/5 to Nitesh Estates Limited

CRISIL has assigned a CRISIL IPO Grade "2/5" (pronounced "two on five") to the proposed initial public offer (IPO) of Nitesh Estates Limited (NEL). This grade indicates that the fundamentals of the IPO are below average relative to other listed equity securities in India. However, this grade is not an opinion on whether the issue price is appropriate in relation to the issue fundamentals. The grade is not a recommendation to buy/sell or hold the graded instrument, or a comment on the graded instrument's future market price or its suitability for a particular investor.

The IPO grade for NEL reflects the company's entry into the highly competitive mid-income housing segment, and development of retail, commercial and hospitality projects, in which the company has a limited track record. These plans also present significant funding and execution risk. Further, in the past, the management's strategies have not been very successful, with NEL registering very low margins. The company had also defaulted on its debt and interest payments in 2008-09, which has been subsequently restructured/repaid. In addition, the second-rung management is fairly new and highly dependent on the promoter, Mr Nitesh Shetty, and the executive director, Mr L.S. Vaidyanathan. Our grading also takes into account that NEL's second line of management has limited experience in the real estate sector, a limitation in the context of the company's large development plans over the next few years.

The grading, however, gets its support from the group's strong brand name in the high-end luxury housing segment and the presence of experienced independent directors on the board of the company. The promoters have a number of group companies, some of which are in the same line of business. However, the company has confirmed to CRISIL Research that there will be a board resolution to execute a formal non-compete agreement to avoid any issues of conflict of interest.

NEL's operating (OPBDIT) and net margin in FY09 were low at 7.6 per cent and 3.2 per cent, respectively, due to low-margin contractual income and high corporate expenses compared to its revenue. In the first half of 2009-10, operating margin was negative 19.1 per cent and net margin was positive at 11.7 per cent, due to a one-time gain of Rs174 mn from sale of investments in subsidiary company, Nitesh Housing Developers Private Limited.

About the company and the issue

Nitesh Estates Ltd. (NEL) is a Bengaluru-based real estate development company. It was incorporated as Nitesh Estates Pvt Ltd on February 20, 2004, and became a public limited company on November 3, 2009. NEL conducts business under the joint development model. Since 2004, NEL has developed three housing projects in the niche high-end luxury market, totaling 0.55 mn sq ft of saleable area.

The promoters, Mr Nitesh Shetty and Mrs Pushpalatha V Shetty, and their group company currently own 84.1 per cent of NEL's shares. AMIF I Ltd (a PE fund of Och-Ziff Capital Management Group) holds a 14.4 per cent stake in the company.

NEL recently ventured into the mid-income housing segment. In the residential segment, the company has four ongoing projects, having a total saleable area of 3.0 mn sq ft (NEL's share is 49 per cent), five forthcoming projects of 2.3 mn sq ft (NEL's share is 71 per cent) and five planned projects of 6.5 mn sq ft (NEL's share is 65 per cent). On the commercial and retail fronts, the company has four planned projects of a total developable area of 3.0 mn sq ft (NEL's share is 65 per cent). These projects (except one residential project) are being developed on the joint development model.

Out of the Rs 4.5 billion that NEL plans to raise via the IPO, Rs 905 million is expected to fund the

acquisition of joint development rights of 2 residential and one retail project, Rs 884 million would be used to fund the construction of a residential project, Rs 460 million will be invested in equity of Nitesh Residency for construction of the 'Ritz Carlton' hotel, Rs 1,357 million will be used to repay debt and the balance will be utilised for general corporate use.

About CRISIL IPO Grading

CRISIL IPO (Initial Public Offering) Grading is an opinion on the fundamentals of the graded issue that reflects CRISIL's independence and expertise. This opinion is expressed as a relative assessment in relation to other listed equity securities in India. The assessment is based on a grading exercise carried out by industry specialists from CRISIL Research. A CRISIL IPO Grade 5/5 indicates strong fundamentals and a CRISIL IPO Grade 1/5 indicates poor fundamentals. CRISIL IPO Grading reflects its assessment of the graded company's equity fundamentals as distinct from an assessment of debt fundamentals. A CRISIL IPO Grade should not be construed to mean a comment on the price of the graded security, nor is it a recommendation to invest or not to invest in the graded security.

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