



# Report and Recommendation of the President to the Board of Directors

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Project Number: 48341-001  
June 2015

## Proposed Investment Drashti Developers Private Limited Shapoorji Affordable Housing Project (India)

This is an abbreviated version of the document approved by ADB's Board of Directors that excludes information that is subject to exceptions to disclosure set forth in ADB's Public Communications Policy 2011.

**Asian Development Bank**

## CURRENCY EQUIVALENTS

(as of 15 May 2015)

Currency unit	–	Indian rupee/s (Re/Rs)
Re1.00	=	\$ 0.0166
\$1.00	=	Rs60

## ABBREVIATIONS

ADB	–	Asian Development Bank
CCD	–	compulsory convertible debenture
DDPL	–	Drashti Developers Private Limited
ESMS	–	environmental and social management system
IFC	–	International Finance Corporation
IRR	–	internal rate of return
NCD	–	nonconvertible debenture
SCB	–	Standard Chartered Bank
SPCPL	–	Shapoorji Pallonji and Company Private Limited
SPG	–	Shapoorji Pallonji Group

## NOTES

- (i) The fiscal year (FY) of Drashti Developers Private Limited and Shapoorji Pallonji and Company Private Limited ends on 31 March. “FY” before a calendar year denotes the year in which the fiscal year ends, e.g., FY2014 ends on 31 March 2014.
- (ii) In this report, "\$" refers to US dollars.

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## I. THE PROPOSAL

1. I submit for your approval the following report and recommendation on a proposed investment of up to Rs 2,170,000,000 in Drashti Developers Private Limited (DDPL) for the Shapoorji Affordable Housing Project in India.

## II. THE PROJECT

### A. Project Identification and Description

#### 1. Project Identification

2. India suffers from an acute national shortage of housing, estimated at 76 million dwelling units in 2009<sup>1</sup> including all income segments. The urban shortage was about 18.8 million dwelling units at the end of 2012.<sup>2</sup> Due to the lack of housing in urban areas, many people live in inadequate conditions and slums have proliferated across the country. In Mumbai, for instance, about 53% of the population lives in slums; however, officially, only 15% are identified as the real poor. This led industry experts to comment that even the middle class is having difficulty finding housing that is not in slums or substandard conditions.<sup>3</sup> Increasing urbanization from 28% in 2001 to 40% by 2030,<sup>4</sup> nuclearization of families, positive demographics (more than 50% of the population is under 25 years of age), and rising incomes will increase demand for urban housing. Increased infrastructure development is improving connectivity within cities, allowing workers to live further away from their jobs at more suburban locations. The combination of high demand and relatively low organized supply, as well as new policy initiatives allowing foreign direct investment in real estate are contributing to the interest of reputed developers to enter the lower price segment.

3. Shapoorji Pallonji and Company Private Limited (SPCPL or the sponsor) approached the Asian Development Bank (ADB) to invest in a housing platform to develop a portfolio of affordable housing projects. The project is considered to be one of the best opportunities for ADB to support affordable housing in India because of its high development impact and its strong and experienced sponsor. SPCPL is one of the first large, well-reputed developers to move into the affordable housing market with a structured approach.

#### 2. Project Design

4. The sponsor, SPCPL, has incorporated DDPL as the entity under which all future affordable housing projects under the Shapoorji brand will be developed. The proposed transaction will make an equity investment in DDPL, which is expected to construct approximately 20,000 affordable housing units. The project will provide affordable housing for families in the upper part of the lower income group and the middle-income group segment—targeting working class, salaried, service sector households. These households are expected to be able to obtain a long-term mortgage from commercial banks and housing finance institutions that will partner with SPCPL ahead of project launch.

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<sup>1</sup> Credit Rating Information Services of India Limited Research. 2009. *Housing Annual Review: Affordable Housing in India*. Mumbai.

<sup>2</sup> KPMG. 2012. *Bridging the Urban Housing Shortage in India*. Mumbai.

<sup>3</sup> J. Cochrane. 2010. Urban Planning Laboratory. *Development Asia*. 3 (6). pp. 9–12.

<sup>4</sup> McKinsey Global Institute. 2010. *India's Urban Awakening: Building Inclusive Cities, Sustaining Economic Growth*. Mumbai.

5. The definition of affordable housing differs around the world, although a commonly accepted guideline is that cost of housing should not exceed 40% of a household's gross income. Income, size of dwelling, and affordability are three key parameters used to define affordable housing. KPMG and Knight Frank, an international property consultant, have outlined a useful affordable housing definition in India (Table 1).<sup>5</sup> Affordable housing is distinct from the Indian high-end real estate market, which recently experienced a boom. Affordable housing is a low-margin (but stable), mass-market business with an estimated market size of Rs3 trillion (\$50 billion) in India's seven largest cities alone (footnote 5). A key factor that determines financial success of the affordable housing segment is low overall cost, which includes (i) low cost of land, (ii) low construction cost, (iii) efficient implementation of construction, (iv) access to low-cost capital, (v) innovative marketing skills, (vi) dedicated organizational focus, and (vii) good government relations to obtain all required licenses in a timely manner.

**Table 1: Defining Affordable Housing**

	Income Level	Size of Dwelling Unit	Affordability
EWS	<INR 150,000 per annum (< \$ 2,444 per annum)	Up to 300 ft <sup>2</sup>	
LIG	INR 150,000 to 300,000 per annum (\$2,444 - \$4,889 per annum)	300 to 600 ft <sup>2</sup>	Monthly Installment to Monthly Income • 30 to 40 percent House Price to Annual Income Ratio • Less than 5.1
MIG	INR 300,000 to 1,000,000 per annum (\$4,889 - \$16,287 per annum)	600 to 1200 ft <sup>2</sup>	

EWS = economically weaker section, LIG = low income group, MIG = middle income group  
Source: KPMG advisory 2010.

6. The project will draw on the extensive construction experience of SPCPL and other Shapoorji Pallonji Group (SPG) companies, which have a presence across the construction value chain. The projects will be located in suburban locations of preselected cities, have clear growth potential, and are carefully selected based on a well-defined geographic strategy. Amenities will include standard sanitation, adequate water and power supply, and provision of community spaces. They could include amenities such as parks, schools, and health-care facilities, where applicable.

### 3. The Sponsor

7. Established in 1865, SPG is one of the oldest and most reputable conglomerates in India with presence across construction, real estate, infrastructure, and water, with a total annual turnover of \$2.5 billion. As part of SPG, SPCPL is one of the leading real estate companies in India with a pan-India portfolio of residential and commercial developments, and experience in affordable housing. SPCPL has constructed landmark buildings, such as the Reserve Bank of India (1952), the Taj Mahal Palace Hotel (1903), and the Imperial Towers in Mumbai (2010), which are the tallest buildings in India to date. SPCPL has also constructed international landmark buildings in the Middle East and Africa, such as the Palace of the Sultan in Oman and the Seat of Government in Ghana. SPCPL is the developer and contractor of the Shukhobrishti project in Kolkata, which is one of the largest mass, affordable housing projects in India to date and is being developed for the government of West Bengal based on a Public Private Partnership. Spread over 61 hectares, about 20,000 units are being constructed in one single location for lower, middle, and upper-middle-income households.

<sup>5</sup> KPMG. 2010. *Affordable Housing—A Key Growth Driver in the Real Estate Sector?* Mumbai.

## **B. Development Impact, Outcome, and Outputs**

### **1. Impact**

8. The direct impact of the project is to increase private sector investment in affordable housing. It supports poverty reduction and inclusive growth by generating employment and improves housing availability and quality. Access to adequate housing improves health conditions, but also reduces stress and improves security, especially for children and women. At the same time, housing provides a place of employment for micro and small businesses and can be used as collateral to secure a loan.<sup>6</sup>

### **2. Outcome**

9. The outcome of the project is improved access to affordable, available and quality housing for target households in urban India. The shortage of housing in urban centers will be partially addressed by the construction of additional units. This will be measured through the number of units sold to end consumers and ownership deeds transferred.

### **3. Outputs**

10. The project's outputs will be the construction of approximately 20,000 affordable residential housing units, to be built to the extent possible according to green building principles.<sup>7</sup> The project is expected to create approximately 9,000 temporary unskilled and semiskilled direct jobs during project construction. Locally purchased goods and services are expected to contribute approximately \$640 million to the local economy. Construction is a large contributor to employment, particularly in the form of semiskilled and unskilled jobs for lower income groups. According to an ADB study, Rs1 million invested in construction creates (direct and indirectly) 22,000 unskilled, 23,000 skilled and semiskilled, and 9,000 managerial and technical person-days of employment in India (footnote 6). Environmental and social standards of the developer will be implemented at each subproject.

## **C. Alignment with ADB Strategy and Operations**

### **1. Consistency with Strategy 2020 and Country Strategy**

11. The project will promote private sector development, one of the pillars of Strategy 2020 and its midterm review, in the affordable housing segment.<sup>8</sup> The government has traditionally supported this part of the real estate sector, which has historically not seen much interest from the private sector. The Midterm Review of Strategy 2020 also calls for sharpening the focus of ADB operations on inclusive economic growth, which is addressed through the spin-off effects of construction.<sup>9</sup> ADB's country partnership strategy for India, 2013–2017 notes that housing finance, and physical and social infrastructure development will be supported.<sup>10</sup> The project

<sup>6</sup> ADB. 2013. Housing and Housing Finance—A Review of the Links to Economic Development and Poverty Reduction. *ADB Economics Working Paper Series, No. 362*. Manila.

<sup>7</sup> Green building initiatives include maximizing green spaces within the development area, usage of efficient water and energy management techniques, ventilation design to maximize ambient air where possible, and water recycling for irrigation and gardening requirements.

<sup>8</sup> ADB. 2008. *Strategy 2020: The Long-Term Strategic Framework of the Asian Development Bank, 2008–2020*. Manila.

<sup>9</sup> ADB. 2014. *Midterm Review of Strategy 2020: Meeting the Challenges of a Transforming Asia and Pacific*. Manila.

<sup>10</sup> ADB. 2013. *Country Partnership Strategy: India, 2013–2017*. Manila.

supports the government's priority of promoting affordable housing, which was identified in the country's Twelfth Five Year Plan, 2012–2017 as a particularly critical concern for low-income groups.<sup>11</sup> The plan calls for private sector involvement in housing, and encourages city authorities to enable this by offering improved governance and services (e.g., in land management).<sup>12</sup>

## 2. Consistency with Sector Strategy and Relevant ADB Operations

12. The project is in line with ADB's Urban Operational Plan to increase private sector involvement in the urban sector.<sup>13</sup> By constructing affordable housing units that provide better living conditions, the project will help to improve urban quality of life, which is the main objective of ADB's urban sector operations in India.

### D. Implementation Arrangements

13. Table 3 summarizes the implementation arrangements.

**Table 3: Summary of Implementation Arrangements**

Aspects	Arrangements
Regulatory framework	Projects will be designed as per requirements of the National Building Code of India 2005 and prevailing local or regional statutory authority guidelines such as the development control regulations in Mumbai and Chennai. SPCPL will prepare subproject designs in accordance with the applicable municipal development regulations that specify site and building by-laws.
Management	SPCPL
Contractor	SPCPL will be the construction contractor for all projects.
Operations arrangements	
Revenue structure	Revenue will occur from sales of residential housing units, which will be sold directly to the end-users.
Operation and maintenance	Housing societies, to be formed by the unit owners after completion, will be responsible for the operation and maintenance of the common areas of the buildings.
Performance monitoring	DDPL will report on key performance indicators, including output and outcome indicators. An independent external consultant will monitor compliance with ADB's Safeguard Policy Statement (2009) during construction.

ADB = Asian Development Bank, DDPL = Drashti Developers Private Limited, DMMA = development, management and marketing agreement, SPCPL = Shapoorji Pallonji and Company Private Limited.

Source: Asian Development Bank.

## III. THE PROPOSED ADB ASSISTANCE

### A. The Assistance

14. The investors propose to co-invest along with SPCPL in DDPL by making equity investments in DDPL. ADB proposes to invest Rs 2,170 million in total. Drawdown of ADB funds, which will be staggered against different project development timelines.

<sup>11</sup> Government of India, Planning Commission. 2012. *Approach to the 12th Plan. The Challenges of Urbanization in India*. Delhi.

<sup>12</sup> Government of India, Planning Commission. 2012. *Twelfth Five Year Plan (2012–2017): Faster, More Inclusive and Sustainable Growth*. Delhi.

<sup>13</sup> ADB. 2013. *Urban Operational Plan, 2012–2020*. Manila.

## B. Value Added by ADB Assistance

15. Long-term funding for the real estate sector, particularly for the affordable housing segment, is not readily available in the Indian market due to limited risk appetite and commercial bank's limits to the sector which have been largely used for the high-end real estate market. ADB's investment will be catalytic as it allows SPCPL to launch a sizeable and sustainable housing platform for affordable housing, an area that needs quality sponsors to build low-cost, good quality housing stock. To date this segment is largely characterized by small unorganized participants with limited capacity. The construction of housing supply affordable to the middle class will free up housing stock for people who currently live in substandard conditions but are unable to move out due to a lack of available options. The project will play a pioneering role in demonstrating the commercial viability of affordable housing projects undertaken without government subsidies.

## C. Risks

16. **Sponsor risk.** The real estate sector in India is plagued by delays and underperformance due to the limited financial and operating capacity of developers. SPCPL has ample experience as a real estate developer and construction contractor, having delivered multiple landmark buildings. SPCPL is the developer and engineering, procurement, and construction contractor of the Shukhobrishti project in Kolkata, which is one of the largest mass housing projects in India to date.

17. **Project implementation risk.** Real estate projects are prone to construction delays and cost overruns. Construction of the subprojects will be done by SPCPL, one of India's most reputable and leading construction companies. Projects will be undertaken in a phased manner and are scalable, as the project will comprise multiple independent towers. If market demand dictates a smaller development, fewer towers can be constructed, reducing the capital outlay and the risk of cost overruns. Increased construction costs are generally absorbed by sales price escalations for units sold in later stages of the development.

18. **Market risk.** The transaction is exposed to underlying real estate risk of the projects (in terms of cost, schedule, unit sales, and financing) which, if materialized would result in lower sales proceeds than planned. By providing financing at a corporate level, ADB is able to invest in affordable housing on a portfolio basis, mitigating the geographic real estate concentration risk of a single project location.

19. **Government support.** Reliance on government for provision of basic infrastructure and public transport creates a risk that project sites might not be sufficiently connected or will encounter connection delays. Sites will be carefully selected on the (near) availability of such trunk infrastructure and connectivity services in order to mitigate against connection delays.

20. **Permitting risk.** The real estate sector has seen significant delays over the past few years due to the increased number of permits required and the lengthy processes involved, which can contribute to high cost overruns. Several Indian cities have started implementing an automated system for approving building plans. SPCPL's proven track record, good reputation, and ongoing relationship with authorities should mitigate permitting delays.



## IV. POLICY COMPLIANCE

### A. Safeguards and Social Dimensions

21. In compliance with ADB's Safeguard Policy Statement (2009), the project is classified category B for environment and category C for involuntary resettlement and indigenous peoples impacts. The potential environmental and social impacts were identified and effective measures to avoid, minimize, mitigate, and compensate for the adverse impacts are incorporated in the safeguard reports and plans. To assess compliance with the safeguard requirements for individual projects, DDPL will establish and maintain an environmental and social management system (ESMS), to screen, assess, and address environmental and social impacts and risks. The institutional capacity and commitment of DDPL to manage the project's social and environmental impacts are deemed adequate.

22. Sites within the municipal boundaries of the metropolitan areas, subject to a development control plan and zoned for residential development, will be considered for development of housing projects by DDPL. No significant environmental disturbances are anticipated as the screening criteria for site selection will avoid areas in the vicinity of environmentally sensitive areas. Typical construction impacts such as vegetation clearance, storm-water management, dust, noise, and solid and liquid waste generation will occur apart from an increase in local traffic due to operation of construction vehicles and equipment on site. No involuntary resettlement impacts are expected as DDPL will acquire already aggregated lands, free of land disputes or encumbrances, from (i) lands already owned by SPG in the metropolitan cities, (ii) a network of reputed land aggregators and realtors with access to suitable lands, and (iii) international property consultants and reputed brokers. DDPL will perform due diligence of the process for all land procurement, and address any residual impacts on affected persons in line with ADB safeguard requirements. Impacts on indigenous peoples are not expected as there is no likelihood of concentrations of scheduled tribes occupying or utilizing the sites within the metropolitan cities. Each project will undergo an initial environmental examination and a social safeguards compliance due diligence as per the DDPL ESMS.

23. A corporate audit was conducted on SPCPL's existing environment and social policy and procedures. The audit identified corrective actions required to ensure compliance of the procedures with Safeguard Policy Statement requirements. The corrective actions were discussed and agreed upon with SPCPL. DDPL commits to implement the corrective actions proposed and to have in place a Safeguard Policy Statement compliant ESMS, which is satisfactory to ADB, prior to first disbursement. DDPL will submit annual monitoring reports on the implementation of its ESMS and the subprojects.

24. The project gender category is some gender elements. Measures to benefit women or facilitate their involvement in construction and operation of the project are incorporated in the project design in accordance with ADB's Policy on Gender and Development (1998). DDPL will comply with national labor laws and, pursuant to ADB's Social Protection Strategy (2001), will take measures to comply with the internationally recognized core labor standards.<sup>14</sup> The client will report regularly to ADB on (i) its (and its contractors') compliance with such laws and (ii) the measures taken. Information disclosure and consultations with affected people will be conducted in accordance with ADB requirements.

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<sup>14</sup> ADB. 2003. *Social Protection*. Manila (adopted in 2001).

**B. Anticorruption Policy**

25. DDPL was advised of ADB's policy of implementing best international practice relating to combating corruption, money laundering, and the financing of terrorism. ADB will ensure that the investment documentation includes appropriate provisions prohibiting corruption, money laundering, and the financing of terrorism, and remedies for ADB in the event of noncompliance.

**C. Investment Limitations**

26. The proposed equity investment is within the medium-term, country, industry, group, and single-project exposure limits for nonsovereign investments.

**D. Assurances**

27. Consistent with the Agreement Establishing the Asian Development Bank (the Charter),<sup>15</sup> ADB will proceed with the proposed assistance upon establishing that the Government of India has no objection to the proposed assistance to DDPL. ADB will enter into suitable finance documentation, in form and substance satisfactory to ADB, following approval of the proposed assistance by the Board of Directors.

**V. RECOMMENDATION**

28. I am satisfied that the proposed investment would comply with the Articles of Agreement of the Asian Development Bank (ADB) and recommend that the Board approve the investment of up to Rs 2,170,000,000 from ADB's ordinary capital resources in Drashti Developers Private Limited for the Shapoorji Affordable Housing Project in India, with such terms and conditions as are substantially in accordance with those set forth in this report, and as may be reported to the Board.

Takehiko Nakao  
President

11 June 2015

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<sup>15</sup> ADB. 1966. *Agreement Establishing the Asian Development Bank*. Manila.

## DESIGN AND MONITORING FRAMEWORK

<p><b>Impacts the Project is aligned with:</b></p> <p>Private sector investments in affordable housing increased (12th Five Year Plan) Enhanced inclusive and sustainable growth (12th Five Year Plan)</p>
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Results Chain	Performance Indicators with Targets and Baselines	Data Sources and Reporting	Risks
<p><b>Outcome</b> Improved access to affordable, available and quality housing for target households in urban India<sup>a</sup></p>	<p>a. By 2025, at least 20,000 additional households hold ownership deeds for their houses (2014 baseline: n/a)</p>	<p>a. Sponsor's annual financial statement</p>	<p>Housing ownership transfers are delayed. Mortgage finance is not available to the relevant market segment. Ancillary infrastructure connecting potential affordable housing sites to industrial hubs is delayed.</p>
<p><b>Outputs</b> 1. Residential housing increased</p>	<p>1a. Construction of at least 20,000 residential units by 2023 (2014 baseline: n/a)</p> <p>1b. Gender responsive physical design features designed and built in DDPL subprojects by 2023 (2014 baseline: n/a)</p> <p>1c. Number of unskilled and/or semiskilled workers employed on project construction total approximately 9,000 by 2023 (2014 baseline: n/a)</p> <p>1d. Locally purchased goods and services amount to \$640 million by 2023 (2014 baseline: n/a)</p>	<p>1a-d. Sponsor's annual financial statement</p>	<p>Construction execution is slower than expected. Market uptake is lower than expected. Adherence to the ESMS is not sufficient.</p>
<p>2. Environmental and social standards of the developer implemented</p>	<p>2a. An ESMS document satisfactory to ADB established prior to first disbursement (2014 baseline: n/a)</p> <p>2b. Adequate worker facilities provided, including special facilities for women (e.g., child care and education facilities at construction sites) by 2023 (2014 baseline: n/a)</p>	<p>2a. DDPL board of directors approval of ESMS</p> <p>2b. Annual environmental and social performance reports</p>	
<p><b>Key Activities with Milestones</b></p> <p><b>Output 1. Residential housing increased</b> 1.1 ADB executes finance agreements by 2016.</p>			

**Output 2. Environmental and social standards of the developer improved.**

2.1 DDPL establishes an ESMS consistent with ADB's Safeguard Policy Statement by Q4 2015

2.2 Environment and social safeguards integrated in all DDPL affordable housing projects, in line with DDPL ESMS, by 2016

2.3 Qualified, trained staff assigned to implement the ESMS within DDPL by Q4 2015

2.4 Monitoring and reporting on satisfactory implementation of ESMS to ADB annually

**Inputs**

ADB: provides of up to Rs2,170 million (\$35 million equivalent) in nonconvertible debentures, compulsory convertible debentures, and equity.

**Assumptions for Partner Financing**

Not applicable

ADB = Asian Development Bank, DDPL = Drashti Developers Private Limited, ESMS = environmental and social management system, IFC = International Finance Corporation, n/a = not applicable, SCB = Standard Chartered Bank.

<sup>a</sup> Target households are in the upper part of the low-income group and the middle-income group.

Source: Asian Development Bank.