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Economic Recession Challenges and Indian Real Estate Investment Scenario

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ABSTRACT

A golden period in the Indian real estate market has been marked by an out-of-control property boom that is reaching unprecedented heights. Indian real estate, according to industry analysts, has enormous demand and promise in practically every industry, particularly in the commercial, residential, and retail sectors. However, the effects and ramifications of the world recession could not be ignored by Indian real estate. The global credit crisis, which started as a tiny fire in the U.S. housing finance sector in 2007, quickly spread to include not just the United States but also the Western countries and, ultimately, the rest of the globe, including India. Since the Great Depression, no economic crisis has been as severe or as pervasive as the one we are now experiencing. The last quarter of 2018 saw the beginning of the Indian real estate sector's actual effect. Between March 2018 and March 2019, the real estate industry had a 62% reduction in revenues, a 58% decline in PBDIT, and a 78% fall in net profit. The price of real estate in India has significantly decreased along with this reduction. This is further shown by the reduction in demand for all sorts of real estate as well as the sharp decline in building activity. Asian economies like China and India were anticipated to not only stay unaffected by the global downturn but also to play a significant role in containing it. The 'decoupling idea' has been disproven, nevertheless. The real estate industry is undoubtedly being impacted by the global economic slump, both globally and in India. This report makes a modest effort to examine the impact that unfavorable expectations are playing in India's real estate market and to provide potential remedies.

Keywords: *Real estate, property, investment cycle, scenario planning*

Introduction

To begin with let us define the term Recession : _recession is a decline in a country's Gross Domestic Product (GDP), Growth for two or more consecutive quarters of a year. A recession is also preceded by several quarters of slowing down. An economy which grows over a period of time tends to slow down the growth as a part of normal economic cycle. An economy typically expands for 6 to 10 years and tends to go into a recession for about six months to 2 years. A recession normally takes place when customers lose confidence and trust in the chances of growth of the sector and starts not only making less investments and but withdrawing also. This results into a decreased demand for goods and services, decrease in production of related material, layoffs and

Economic slowdowns are regular occurrences around the world. Last two centuries witnessed many slowdowns manifested in banking panics, stock market crashes, currency crisis, bursting of the real estate bubble. In such situations, the supply of money out spaces the demand evaporating the liquidity. The main cause of this financial disaster is unregulated capitalism leading to suboptimal outcome. Unregulated markets adversely affect the macro economic variables resulting in instability of local currency as well as equity and increased uncertainty. This is detrimental to the business confidence and overall economic activities.

Indian Real Estate was a sunrise sector in 2006 passing through a golden era for Indian real estate. It was fascinating to know that the value of commercial property of Delhi and Mumbai is at par with New York and Paris and London. Multinationals have been desperate to invest here. It was moral boosting to hear about the number of mergers, acquisitions and joint ventures taking place with important role of Indian companies in them. In most of them, Indian partners were the initiators. The globalization and liberalization had trickled down an otherwise closed Indian economy. The impact was revolutionary on social, economic, and cultural fabric of India, a country known in the world as tradition bound and always resisting to change. Indian real estate is expected to increase from \$12 billion to \$ 90 billion by 2015. The demand for housing was expected to increase to 80 million with expectation to add new jobs to the value of 4 million by 2015. Investments in the real estate segment are expected to yield 13-16 per cent return. (IBEF 2007). It was expected that it would increase to become top most real estate markets in the world.

Literature Review

Wade Robert in his article –Steering out of the Crisis¹ mentioned that the global financial and economic crisis has discredited many established ideas about how societies should run their economies and the impact of this discrediting will last beyond the recovery.

Thorton Grant in his article, –Sustaining and building businesses during economic slowdown _ has specified that the Real Estate Industry in India witnessed unprecedented growth in a relatively short span of time. With most companies having seen only the upward swing, the economic downturn proved to be a litmus task.

After survival through the recession of 2018, it is striking back more forcefully and confidently with corrected prices and improved product variety. Indian economy has been mostly insulated from global downturns, showing a degree of stability. India’s consumption-driven model is also more people-friendly than other development strategies. (Bandhopadhyaya, Arindam, Basu, Sanjay, Baid.2018, April 01)). There was no direct exposure of India to the US subprime credit market but it did triggered negative sentiments in India. The Bombay Stock Exchange Sensex fell 3.35% or 469 points on September 15. The worst affected was the realty index which dropped 7.6% on the same day. (N.K. Sehgal, 2018).

India has not seen a boom and bust cycle of the kind experienced in developed countries. However no liberalized economy can remain unaffected by external factors. (Subramaniam S. & D.Jayraj.2006 October, Nitin A Garg of Garg 2006). It is only after liberalization that the Indian economy has been witnessing several cyclical movements. Economic cycles do impact real estate and there is a relationship between real estate and financial markets (Born and Pyhrr 1994, Mueller 1995). In real estate, most common cycles are considered to be of 8-10 years (Laposa 1995) and there are evidences of such 15 different real estate cycles (Pyhrr and Roulac 1996).

It was realized that the boom/bust of 1920–34 exhibited many similarities to the boom/bust of 1980–93. Both periods were initiated by an unusually high period of inflation and rapidly rising rents. (Ronald W. Kaiser. 1997)

The ripple effect of US financial crisis acted as a double edged sword for India. Firstly, banks, financial institutions, MNC pruned staff. Secondly, the affluent NRI community began to have second thought about purchasing property in India. More so demand for luxury flats declined because of job scenario. Developers finding it difficult to sell high-end apartments began to move towards lower income segments. (Sarthak 2018, City Group Research 2007)

Studies revealed importance of government in moderating boom-bust cycle (Hoyt1993). It was realized that internal policy can be planned in such a way that it minimizes affect from external factors. (Nitin A. Garg of Garg 2006)

It was analyzed that uncertainties can arise for real estate managers in economic growth, political and social development within and outside country (Geert Dewulf and Pity Van der Schaaf, 2004). To overcome the pitfalls scenario building could be used as an important technique to study future property development, investment and management decision (John Ratcliff, 1Jan 1999). In 2006 FHWA office of Real Estate services, Virginia developed four most important predetermined elements possible, probable, preferred, present, strategy.

To overcome the fall in supply, real estate companies explored new investment opportunities. Builders of residential property took to developing commercial space. For example, Raheja moved into constructing special economic zones, Omaxe took to modernizing and maintaining airstrips. DLF, Unitech and Omaxe bidding for road projects being offered by the National Highways Authority of India. Unitech made a foray into telecom.

The second trend was to move abroad to market real estate companies' products, raise funds, source raw materials and launch projects like the one by Sobha Developers opened an office in China and Dubai. Parsvnath Builders has a subsidiary in Singapore. Puravankara Projects too has started operations in Sri Lanka, UAE to build super luxury villas on the outskirts of capital Colombo.

Real estate market in India has been on a high for last decade and as per simple law of gravity or law of economics what goes up must come down. Though market is slowing down but the situation is not one of crashing market because this relatively slower rate of correction is a sign of maturing market (Mangalam 2018) In the long run, given that the Indian growth story is likely to continue, real estate prices will certainly increase. However, they will not see a meteoric rise as they did earlier. The market will eventually consolidate. It will be a more stable market (Prabhakar Sinha, 2018).

Henceforth, the slowdown is unlikely to last beyond the next 2-3 years. In the long term , strong demand for real estate in India will remain intact and will see us through another real estate cycle once the market finds its own level by responding to these short –to mid –term global and domestic factors (Cushman & Wakefield Report 2019).

Objectives of the Research

- *To study the most likely impact of economic recession on Real Estate sector of India.*
- *To study the future of real estate sector of India.*
- *To study the effectiveness of steps taken by government to boost the Real Estate sector of India.*
- *To offer conclusion and suggestion for revival of this sector.*

Research Methodology

Research has its special significance is solving various operational and planning problems of business and industry. Research methodology is a way to systematically analyse the research problem. Market research has been undertaken to to understand marketing problems and prospects in a better way.

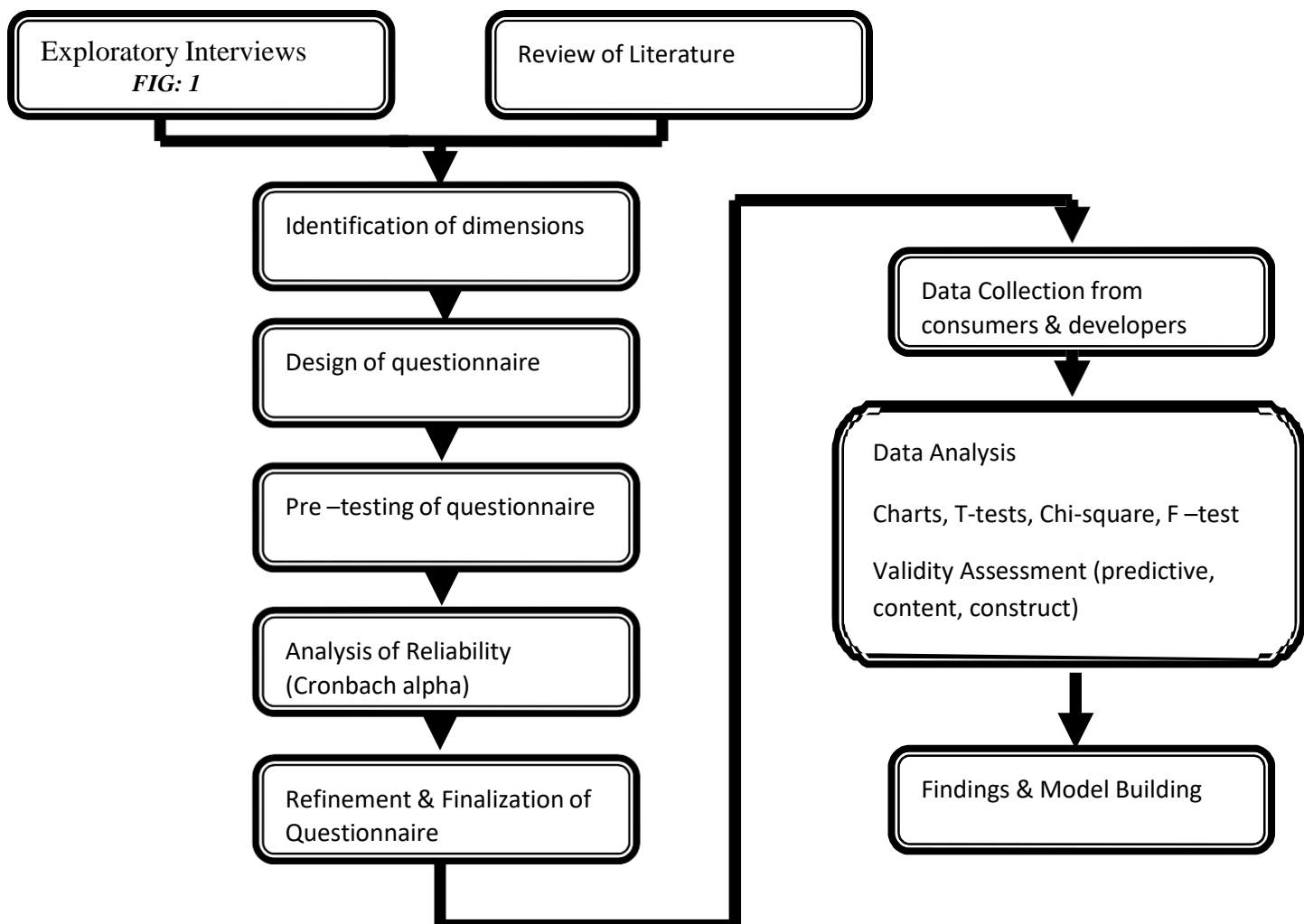
Primary data has been collected from the direct source that is by direct contact with the consumers and developers. The required information was gathered from them by questionnaire and by making discussions.

Secondary data has been collected through books, research articles, news papers, internet and various reports on real estate.

Analysis and Discussion

Primary Data

Questionnaire development involves the stages shown in the following chart:



Hypotheses

Null Hypothesis 1: There is no significant variance between impacts of economic recession on real estate of India reflected in terms of various factors.

Null Hypothesis 2: There is no significant variance between the future of real estate of India in three times period (1-2years, 2-3years, 3-4 years) reflected in terms of decline, growth and stability.

Null Hypothesis 3: There is no difference of opinion between consumers and developers regarding methods adopted to handle the harmful impact of economic recession on real estate of India according to developers.

Null Hypothesis 4: There is no difference of opinion between consumers and developers regarding methods adopted to handle the harmful impact of economic recession on real estate of India according to consumers.

Null Hypothesis 5: There is no association of income with the steps followed by government to handle harmful impact of economic recession on real estate.

Null Hypothesis 6: There is no association of occupation with the steps followed by government to handle harmful impact of economic recession on real estate.

Null Hypothesis 7: There is no association of education with the steps followed by government to handle harmful impact of economic recession on real estate.

Null Hypothesis 8: There is no association of gender with the steps followed by government to handle harmful impact of economic recession on real estate.

Table 1: Summary of Hypotheses Testing

Hypothesis	Significant/Not Significant	Statistical Test
NH 1	Significant	F-test
NH 2	Significant	F-test
NH 3	Significant	One Sample T-test
NH 4	Significant	One Sample T-test
NH 5	Significant association between income and reduction in price of steel and cement and changes in price for purchase of property.	Chi-Square

NH 6	Not significant	Chi-Square
NH 7	Not Significant	Chi-Square
NH 8	Not Significant	Chi-Square

Model Building

The role of government is very important in strategic decision making in Real Estate Sector. During the period of growth, stability and boom, government of a country plays different roles. On the basis of findings of this study, the model has taken two major dimensions namely *strategies and scenarios* (Geert Dewulf and Pity van der Schaaf 2004). Strategies dimension has three variants: *growth, stable, decline* and scenario have been developed for *1-2 years, 2-3 years, and 3-4 years* starting with economic recession 2018. Future has been developed for the various factors mentioned in the model.




From the analysis, it has been observed that the *role of government had remained* pro-active. The policy makers felt that the support of the government is very crucial for improving the condition of real estate during the initial 1-2 years immediately after the recession in 2018. At that point of time the government was playing the role of an *initiator (I)*. By next year that is around 2019 end and beginning of 2010 situation began to stabilize and not so strong role of Government was required. Here, the Government played the role of *controller (C)*. After March 2010 the situation improved a lot and the real estate market showed sign of strong survival and growth changing the role of government to be of a *moderator (M)*. This phenomenon is indicated with the help of changing shades of blue color. The model is being named as *ICM Real Estate Model (Initiator Controller Moderator Model)*.

Several strategies adopted by the government reveal that for initial 1-2 years there will be growth in sales promotions (g) to attract consumers to buy property. Competition (e) is expected to stabilize in the initial 1-2 years. The remaining demand for real estate (a), price of property (b), profit of builders and developers (c), launch of new products will decline (d), rate of home loans (f) will decline.

Whereas in 2-3 years bracket, the competition (e) will grow as situation improves, demand for property (a), launch of new products will decline (d), rate of home loans (f) will stabilize and price of property b), and profit of builders will decline (c).

Finally, in the category of coming 3-4 years sales promotion (g) methods will decline because of increase in demand, price of property (b) and profit of builders will stabilize (c), and demand for property (a), launch of new products (d), rate of home loans (f) and competition will increase (e).

Table 2 : Scenario

		1-2 Years	2-3 Years	3-4 Years
Strategies	Grow	g	e	a e d f
	Stable	e	a f d	b c
		Government as INITIATOR		
	Decline		b	g
		Government as CONTROLLER		
	Government as MODERATOR			

- a) Demand for real estate
- b) Price of property
- c) Profit of builders and developers
- d) Launch of new projects
- e) Competition
- f) Rate of home loans
- g) Sales promotions

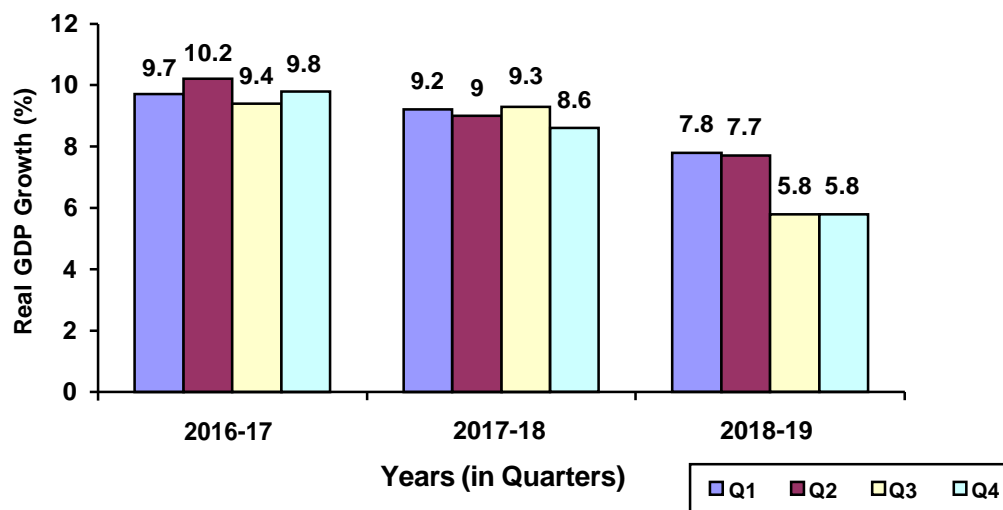
Strategic Implications

This research emphasizes on the studies done in the past and checks its validity against Indian real estate. There have been boom and bust cycles in the past in Indian real estate also but not to the extent as experienced in the western countries of the world. The Government of India has played a very important role in controlling the recession in real estate sector, which is second largest contributor to GDP. During this type of situations, only commitment can win the support of consumers and developers alike which is very important in the tough time of recession. Studies reveal that in spite of economic recession demand for lower income group is still robust. There is a lot of potential to study the scope of new age construction like Green Construction, fire safety, earthquake resistance housing, etc. These should be used effectively during the period of recession.

Secondary Data :

The major issues that plague this industry is tremendous shortfall of middle class housing as majority of the developers are involved in developing high class housing. So, there is a dearth of low cost affordable units. Recession in US economy has caused great impact on Indian real estate business. The real estate industry was a booming industry in pace with information technology (IT) industry. Demand for it space and from high net worth individuals had created opportunities for the this sector

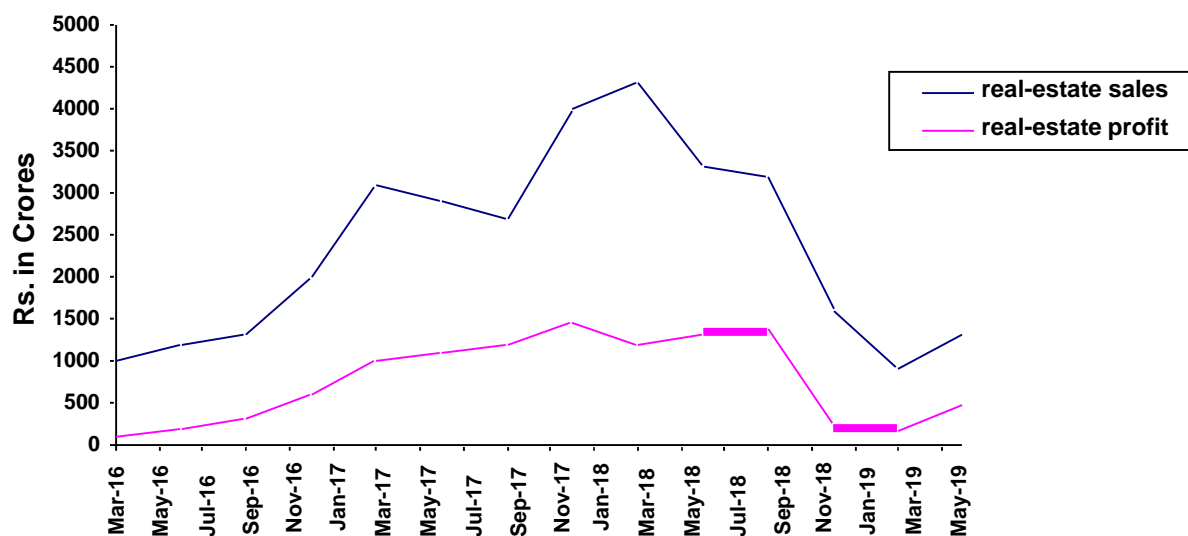
Table 3: Quarterly Estimates of GDP at Constant (1999-00) Prices-Growth Rates



Source: Reserve Bank of India Bulletin

The Indian industry has dealt with economic slowdowns in the past also but this one is in the nature of contagion effect of the western recession. The full spectrum of the shades of the contagion is not evident in the GDP growth trend. Numbers alone would indicate that economic slowdown, so far, has been barely a two-quarter phenomenon. In figure 1, the real slowdown was seen only in the last two quarters of 2018-09. Sales growth respectively dropped to 9.5 per cent and 1.9 per cent in Q3 and Q4 with much worse impact on the net profits that respectively fell by 53.3 per cent and 19.9 per cent.

Table 2: Sales and Profit After Tax Trend of India Real Estate Sector

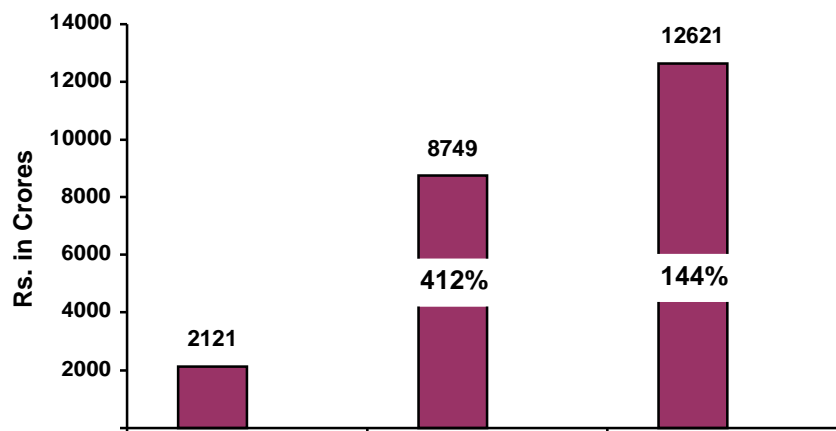


The trend in sales and net profit of -worst affected|| Real Estate is given in figure 2. The Real Estate has shown decline by 62 per cent in revenues, 58 per cent decline in PBDIT, and 78 per cent decline in net profit, between March 2018 and March 2019. This decline has been accompanied by a significant fall in the property prices in India. However, this sector has shown a moderate recovery in the quarter after March 2019.

Table 3: Rate of Growth at Factor Cost at 1999-2000 Prices (Per Cent)

	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19
Agriculture, forestry & fishing	10	0	508	4	4.9	1.6
Mining & quarrying	3.1	8.2	4.9	8.8	3.3	3.6
Manufacturing	6.6	8.7	9.1	11.8	8.2	2.4
Electricity, gas & water supply	4.8	7.9	5.1	5.3	5.3	3.4
Construction	12	16.1	16.2	11.8	10.1	7.2
Trade, hotels & restaurants	10.1	7.7	10.3	10.4	10.1	9
Transport & communication	15.3	15.6	14.9	16.3	15.5	9
Real estate & Financing	5.6	8.7	11.4	13.8	11.7	7.8
Community, social & personal services	5.4	6.8	7.1	5.7	6.8	13.1
Total GDP at factor cost	8.5	7.5	9.5	9.7	9	6.7

(Source: Central Statistical Organization)

Figure 4 : FDI Equity In Indian Real Estate Business

Source: RBI's Bulletin August 2019 (Table No. 46 – Foreign Investment Inflows)

The above table reflects how the steady growth rate of real estate sector had slowed down in year during 2018-19 because of the recessionary trend prevalent in the economy. This proves our hypothesis (Ha) that recessionary effects were responsible for downtrend in the real estate sector and null hypothesis is rejected from the observations made. In figure 4, it can be that FDI equity in Indian Real Estate Business is increasing but in reality it is not so happening. In the year 2007-08 it has increased by 412 per cent and in 2018-19 the increase is only by 144 per cent. Therefore, the growth has not happened in the Real Estate Sector.

Strategies to Cope Up with the above Situation

Challenging times present an opportunity for Companies to capture market share by outperforming competitors. A quick analysis of the market conditions and quicker response to mitigate existing risks differentiates companies. There can be multiple reasons why some companies continue to tread well while some other companies falter badly in their operations, when countered by some serious challenges. But, invariably, the most significant role at this crucial stage is played by the strategic decisions taken by the company. When the global economic crisis, compounded by the local economy issues, started hitting real estate demand in India, different companies reacted in different ways as presented below.

a) Financial Decisions

At the Initial stage, developers were reluctant to reduce real estate prices so that demand in this sector may get boost. However, with no immediate visible respite and growing pressure to cut down the increasing losses, a gradual slash down in prices had to be introduced. The day by day worsening situation of credit availability in the market also forced the real estate developers into liquidity crunch. Many developers were forced to arrange finance from the market at a very high rate and ultimately succumbed to this pressure.

b) Diversification of Business

As they were facing financial crunch and recognizing the need of developing multiple streams of revenues with the opening of the Indian economy, some cash-rich developers vertically diversified their business activities into telecommunications, financial services, insurance, etc. The horizontal diversification also took place into the services related to property management and leasing. This also surfaced as a preferred strategy for dealing with the situation of economic downturn. Due to the increased competition in metropolitan cities, developers opted to diversify their business geographically also. Tier II and Tier III cities also surfaced in their scheme of things. As part of their long term strategy and encashing on many opportunities available due to globalization factor, instead of selling off properties, developers in India began to enter onto lease agreements with the larger

companies for commercial space. The long term rental arrangement, though at reduced rates, guaranteed a steady stream of income, which was very important for their survival.

c) Cost Control

Indian Real Estate companies also embarked upon various cost cutting strategies, like other sectors. Capital intensive projects which had no impact on the revenues of the organization in the short run were either put on hold or scaled down, and some even were cancelled. A number of companies also downsized their extra manpower to cut their cost. However, in many cases, this was not done, thereby putting companies on the risk of losing essential talent in exchange of short term cost savings. A number of real estate companies in developed countries like US and U.K did not hesitate in outsourcing their marketing activities but of course after carrying out the necessary due diligence exercise. This helped in infusing efficiency and cutting the unnecessary costs involved.

d) Focus on Customer Satisfaction

The focus on customer service was the call of the situation. The ongoing situation of economic contraction has also resulted in improved services to the customer. In order to shed off an image of being non-transparent and unorganised, a number of developers increased their focus on customer satisfaction. A customer was provided with the facility of checking the status of construction of his property by logging on to a website. Earlier, this was possible only after visiting the site and following up with the concerned officials. With such initiatives, the real estate developers are changing their image very fast as professionally managed corporate houses, committed for meeting customer expectations and empathetic in resolving the concerned issues. Business development with customer satisfaction became the logo of all concerned.

Conclusion

The Economic Slowdown has been the offshoot of poor under writing standards and weak Regulatory Mechanism, particularly in the mortgage lending. Consequent outburst of the housing bubble and resultant financial mayhem gripped the major economies around the globe. The resultant sub optimal outcome had far reaching effects on production and unemployment, particularly in construction and Real Estate Sector of India.

However, there is a saying that success is not about how high you rise but about how high you bounce back when you hit rock bottom. Real Estate Companies of India today are at that strategic inflation point, when they must define new imperatives to be successful once again. Building the gap between the customers and themselves taking a harder look at resource – sapping processes and above all gaining agility and flexibility as organizations will be the stepping stone to success.

The results of this study reveals that though the picture of Indian real estate is not so rosy but it is temporary and the prospects for future are good. A long overdue adjustment in real estate market is needed. In the long term, strong demand for real estate in India will remain intact. With the economy showing signs of revival, the real estate sector will once again take a giant leap forward.

Suggestions

Following lessons and suggestions are worth noting:

- ❖ Sound credit policies should not be violated while sanctioning housing loans.
- ❖ There is a need to set up a centralized Real Estate Regulatory Authority in line with existing authorities such as SEBI, IRDA, TRAI and RBI.
- ❖ Fiscal stimulus package should be implemented for key areas such as housing to overcome the crisis

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