

# HOT PROPERTY: Is the Indian real estate market too hot for comfort?



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The tranquil, if not sleepy district of Ernakulam in Kerala is witnessing a furious real estate boom. Almost 70 per cent of the district is already counted in realty circles as Kochi, where hardly any space is available to build on. With mega projects coming up at Kochi attracting professionals in droves, demand for living space exceeds supply. The port-based SEZ along with an international container terminal, Petronet's LNG terminal and the Smart City IT project are expected to create 200,000+ high-paid jobs. Roughly 5,000 flats are under construction, against expected demand for 30,000+ apartments over three years. Even little known builders are able to sell 50 per cent of the flats within a month of announcement of a project. Hopes of revival of Kochi's fortunes to the pre-independence Travancore-Cochin days have led to the announcement of a number of giant hotel projects. Projections indicate mushrooming of 100,000+ apartments around Kochi by 2015.

Well, this is the situation in an obscure town of Kerala State – whose all-powerful labour unions have the dubious reputation of driving away any enterprise and where even ordinary people have to put up with porters through vendors, who are anything but friendly. The real estate scenario in amiable towns of India can just be imagined and is no less rosy. The action at Pune (see page 11) is being repeated in most tier-II and tier-III towns, where hotels, malls and hospital projects are attracting mega investments.

The torrent of global business into sectors like IT, ITeS, automobiles and pharmaceuticals have given a terrific boost to realty in India. When SEZs under implementation become fully operational, a double-digit growth is not unlikely to be sustained for several years. The phenomenal economic growth, after almost 50 years of stagnancy, has created a strong need for multi-storied industrial and IT complexes. Additionally, a working class with unprecedented spending fuels demand in the retail and banking sectors. All these have a great appetite for premium space. The new working class desires to and can afford to lease or buy premium residential properties, crowd malls and book up hotels.

Statistics from growth centres in South India reveal that IT and ITeS firms alone in 2006 absorbed 25 million sq feet of land. The size of the Indian real estate market,

hovering around USD 16 billion currently, according to a CII study, will touch the USD 60-billion mark by 2010. CII predicts that foreign investments in the sector will be around USD 28 billion.

The last few years have witnessed several policy initiatives from the Centre to sustain the level of growth that was unheard of until the last decade. Allowing 100 per cent FDI in the construction sector under the automatic route, encouraging venture capitalists and a revolutionary SEZ policy in the face of stiff opposition from entrenched interests have ushered in a paradigm shift.

However, only a die-hard optimist can expect growth in real estate to continue at the same tempo, when privatisation and development of other sectors lag behind. Most experts aver that growth is almost certain to slow down, particularly in the light of RBI's objective of checking the danger of runaway inflation. The latest World Economic Outlook says that India's 2006 GDP growth will slow down from 9.2 per cent to 8.4 per cent in 2007, and further to 7.8 per cent in 2008. Robert Prior-Wandesforde, HSBC economist based in Singapore, predicts 7.8 per cent growth in 2007-08, to further slide to 6.3 per cent in 2008-09. He maintains, "Cumulative effects of the monetary tightening will eventually come to bear on the economy. Also, after a period of above-trend growth, one should presumably expect a period of sub-trend growth."

Irfan Razack, Vice-President (South) of Confederation of Real Estate Developers' Association of India agrees, "Real estate prices have seen all-time high. We should expect them to stabilize now." Moreover, he identifies lack of infrastructure in the regions of high growth as a major bottleneck. After all, it does not make much sense to erect ultramodern structures when reliable facilities like water and electricity for the residents cannot be provided for. Also, it is important to make enough

investments in the social sector to let the residents live in peace.

Star developer Niranjan Hiranandani however feels that funds of the order of USD 10 billion per year in FDI will amount to nothing when the gigantic scale of the demand-supply gap is factored in. "It is untrue that there are too much funds in the real estate industry. We need USD 5 billion for just one project of Dharavi development. For real development to take place, we must think of how to make USD 100 billion happen." In a high profile pre-budget conclave in February, he was vociferous in condemning the RBI move to increase interest on home loans to individual buyers. "The only social security for a person in India is a home, a shelter of his own. In reality, we must encourage the poor and the middle class individual to buy a home." He ridiculed the

tendency of the banker to lavishly fund purchase of automobiles, which make far greater demands on infrastructure, while making home purchase prohibitive. On the other side of the scale, professional bankers are quite keen to prevent the overheating of economy, raising the risk of a meltdown. Said Rajeev Sabharwal of ICICI Home Finance in the conclave, "Although funds are flowing into the economy, developing infrastructure has been somewhat starved of investment. When we talk about increasing FSI to augment supply, the big question to be asked is "Can the infrastructure really support it?"

Leave alone new townships facing infrastructure constraints *after* they come up, sceptics suspect that the boom is artificial. They fear being left to grapple with yet another crop of vanishing companies, once the bubble bursts. It is not that there is no basis for the pessimism of dismissing the talk of booming real estate scenario as lot of hot air and hype.

Speculation is rampant in the sector, with or without the promoters ganging up with stock market manipulators, fuelled by pliable elements in the media. Even as SEBI has tried to curb unrealistic projections, many realty promoters advertise their valuable "land banks" in subtle ways. Little known "Groups" promote mega issues at monstrous premium, driving cold chill of recall of earlier crashes in the CCI era. Take for example, the front page story in a local edition of a national newspaper that previews a 100+ storeyed complex supposed to be in place by 2010 in a tier-II town! This, while there are no takers for many of the 110 units in presently the tallest building of India, five years after it was completed. In addition, vehement resistance on the part of real estate agents and other players for the proposed compulsory registration and licensing has only further undermined the credibility.

In balance, there can be no denying the fact that the realty sector in the country is piping hot. After all, when you have a lot of catching up to do even with fellow BRICs nations and entities like Malaysia, leave alone matching developed countries like the US, EU and Japan (purchasing power parity-compensated GDP of India that contains 17.5 per cent of world population is 6.3 per



cent, compared to China's 15.4 per cent from 20 per cent world population, 2.5 per cent PPP-GDP of Brazil's 2.8 per cent people), things do tend to get hot. But, not hot enough to drop it like a hot potato and go back to old times!

### DECONSTRUCTING REAL ESTATE - REALTY AND THE REALITY

Strange, but true, there is no such thing as real estate or real property in Civil Law jurisdictions anywhere in the world. The Civil Law reckons only two categories of property, immovable and movable. Personal property like clothing, car, jewels or money, also called chattels, is distinct from real property. The word **real**, Latin **res**, refers to a relation with **matter or thing** as distinguished from a **person**. In Common Law, real **estate** denotes the land and the things that are permanently affixed to the land, such as structures. Real **property**, shortened as **realty**, is not the same as real estate. It refers to the ownership **rights**, which are essentially intangible, rather than the physical **things**.

Moreover, the reference to "real" in both cases is a misnomer; originally the term was derived from "royal" (Latin *rex-regis*), meaning the king. In all civilizations, all land and structures erected thereon belonged to the King or the State. Distinction between "ownership" and "possession" of property prevails even in nations fanatically committed to private enterprise. The State does play an important role in realty market.

The advent of private ownership of property, as distinct from the old socialist notion, has created several branches of the business of real estate and realty. The modern day Realtor is service provider catering various categories of customers on different aspects of real estate and realty, both residential and commercial.

#### Realty services include:

- **RELOCATION SERVICES:**  
Assisting people to relocate business, which may include shifting belongings and arranging for services over and above looking for a home



- **PROPERTY MANAGEMENT:**  
Managing properties for the owner for short/long term, including leasing and renting as well as providing maintenance and security
- **SITE DEVELOPMENT:**  
Improvement to virgin or reclaimed land, including dredging and levelling to add or replace buildings
- **FINANCIAL SERVICES:**  
Channelling funds of individual and institutional investors to the sector, including Real Estate Funds and mortgage funds
- **CONSTRUCTION BUSINESS:**  
Erecting structures like housings, commercial complexes, hotels and hospitals
- **BROKING:**  
Bridging the needs of the customers through Estate Marketing
- **LEGAL:**  
Due diligence exercise, including registration and recordation of property rights
- **APPRAISAL:**  
Professional valuation services

Since transactions in real estate involve items, particularly land, of great value, it becomes important to reflect the distinction between contract and conveyance – rights of a third person, including the civil society, have to be factored in – and complex systems of registration and recordation exist. Broadly classified, the English and German systems stress on land registration, where transfer of title does not take place unless and until the

transfer is registered in the system. On the other hand, the systems prevailing in France and the US stress on recordation in order to protect innocent third parties. The onus is on the new owner to record the transaction. The legal system in India, as well as in China, is one of utter confusion. Muscle power and mob action abound *Vis a Vis* property rights. This is the case in many developing countries. If India is to attract investments in the sector, it will need to align its laws to countries where investors exist. The government has reckoned the need for a credible regulatory framework that can help attract investors by allaying their fears of being taken for a ride.

Investors and banks will be willing to make massive funds available at favourable rates only if they have a foreclosure option in case the borrower defaults in repayments. Mortgaging of a property will be meaningful only if a court action could be secured to let the lenders take back the property promptly and sell it to get their money back. Mortgage loan industry, however, either does not exist at all or is only available to members of privileged social classes in underdeveloped countries. Mortgaging is one realty instrument that has been responsible for the phenomenal real estate wealth in advanced countries. The potential can be gauged by comparing USD 16 billion worth of property in India with the value of property in the developed world – USD 62,000 billion, of which 75+ per cent comprises of residential

property. The government is currently working on ways to develop the industry in India. A beginning has been made in Budget 2007-08 with the introduction of reverse mortgage scheme. This addresses concerns of the real estate sector, while allowing senior citizens owning property to avail a monthly stream of income against mortgage of the house. After the owner's death, in case the heir fails repay the complete amount, the property will go back to the bank.

## BOOM TOWN PUNE

### Preview of things to expect in India's tier-II cities:

A pioneer in engineering activity, Pune was instrumental in putting India on the world's manufacturing map, wooing engineering giants like Sandvik, Wimco, Atlas Copco, SKF, KSB and Buckau-Wolf to set shop. It then attracted Bajaj, Firodias, Bharat Forge and lured Tata Motors to get away from Jamshedpur. Yet, Pune remained relatively a laggard on the real estate front compared to other towns with lesser development. The entry of IT and ITeS sector players in a big way has changed the story. With high value R&D outsourcing work from global majors finding its way into the labs and centres situated in the town, Pune is witnessing unprecedented spurt in property development in all segments – commercial, residential, hospitality and retail.

Residential and commercial properties have been appreciating rapidly since the last few years. Cushman & Wakefield reports 14 upcoming malls under construction or in the planning stages. The Hotel segment too is undergoing sea change. There are 30-odd hotels on the anvil, against the count of just 3 big hotels operating currently. Hyatt Regency, Radisson, Novotel, Traders Hotel, Royal Orchid and Lemon Tree are scheduled to come in, chasing 3 Marriott properties.

Naturally, real estate developers are queuing up to make a fortune in the boom town. National level biggies DLF, Unitech, Reliance, Raheja are being given a tough fight by 300+ local builders. Sustained business over several years have added financial muscle to local realty players like Panchshil Realty, Gera Developments,

Paranjape Schemes, Kumar Builders, Kolte Patil and DS Kulkarni Developers, who all have their hands full with mega projects.

Pune is the first city to get a satellite township developed in full conformance with the new Township Development Policy of the government. Fully self-sustaining for all civic amenities, such townships are envisaged to have their own governing structure on the lines of municipal corporations. The 400-acre Amanora Park City, promoted by Future Group's retail-focussed fund Horizon Realty LLC and the City Group of Pune, is expected to be worth Rs. 3000 crore soon after it is completed in 2010. The "city government" is even negotiating with Indian Railways to run its own rail connectivity for its "citizens". A 30-storey commercial building **Signature Towers**, Maharashtra's tallest building outside Mumbai, will be Amanora Park's hallmark.

The changing skylines of Pune, many realtors predict, presages the state of affairs 5-10 years hence in most tier-II and tier-III cities. Brainstorming exercises, on how infrastructure for IT-BPOs can be created and expanded in Tier II cities in a phased manner, are already under way. In fact, the Prime Minister's Office has issued a directive to put integrated modern townships for sunrise industries on the fast track. Representatives of Information Technology Ministry, Urban Development Ministry, NASSCOM and the IT industry are participating in the exercise. Creation of such townships will take the pressure off large cities, which are unable to cope up with growing infrastructure demands. The PMO takes it as a tool for decentralizing economic activity.

## HOTELS, HOTELS EVERYWHERE

Whatever others think about India being a hot investment destination, global hospitality majors appear to be betting heavily on the country's fortunes. Who's who of the prestigious hotel chains predict that a lot of global business is going to be done out of Indian cities and towns. They are readying to have – or increase – their presence in the country, by setting up

of modern hotels. This is happening even in locations that only had guest houses and roadside inns earlier.

The biggest gainer in the ongoing hotel boom is the real estate industry. Unitech Ltd is currently creating 28 hotel properties, which will put 7,000 rooms in the marketplace by 2010. It has already tied up with big names for managing 10 of them. Marriott International will partner it for 4 hotels in the 4-5 star categories. Another 3 five-plus star hotels will be managed by Carlson. Ritz Carlton has entered into a deal for such a property at Kolkatta. One property each in Gurgaon and Bangalore in the 3-4 star category is to be managed by Country Inn. Other realty players too have entered the hotel foray. DLF is teaming up with Hilton Hotels Corporation in a JV. Atie-up with Accor for its budget hotel chain has been announced by Emaar MGF.

Budget hotels target the swelling incomes and bank balance of the country's middle class, which is spending huge amounts on tour and travel. Big players, including the state-run ITDC, Tata's Taj Group and Welcome Group-ITC have entered the segment, realizing the phenomenal business potential. Growth in business and leisure travel, aided by low-cost airlines and better rail/road connectivity, guarantees growth in the sector. It is predicted to skyrocket with more new economic centres like SEZs. Taj Group arm Roots Corporation has emerged as an aggressive player, exploiting the Smart Basic concept to the hilt. In a matter of under two years, its chain Ginger is already 8-strong, with 3.6 lakh sq feet space under its belt. The Ginger chain will be 37-strong by 2010, with the company pumping in Rs. 350 crore in the properties. Kotak Realty Fund is extending investment support to Lemon Tree Hotels with its USD 7 million Red Fox brand. London-based Dawnay Day is just one of the smaller chains, keen to establish footprint in India.

Overall demand is predicted to witness a growth of 55,000 room-month between March 2007 and March 2008. Only 37,000 rooms across categories are coming up during 2007-08. With an existing demand-supply gap of 50,000, there is unlikely to be let up in demand for real estate from this premium sector for a long time to come. 