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Shrinivas Rao, CEO-APAC, Vestian shares his insight with Sandeep Sharma about the latest real estate trends, prospects of rental and affordable housing in the near term, reforms and sops expected in the upcoming budget, project finance, green building development, impact of GST and Real Estate Regulatory Act, 2016 (RERA) and solution to solving India's burgeoning housing problem. Edited excerpts...

Could you share with us insights about the latest real estate trends?

Indian real estate sector witnessed one of the most trying periods of all time in 2017. Demonetization, Real Estate (Regulation and Development) Act 2016 (RERA) and Goods and Services Act (GST) Act were major reform milestones that impacted the business environment. The primary issue concerning these policy reforms was the lack of clarity on how they would impact the country's real estate sector and the buyers/investors thereof. This has had a direct bearing on the stakeholders as property markets are largely sentiment-driven. Consequently, residential markets were severely hit with new launches restricted to dismal numbers; and the market witnessing a depleting sale in housing units. The luxury market was affected the most, and the drop in the number of launches was significantly steeper in this segment.

Prices of properties remained largely stagnant across markets in 2017, although a few locations holding a large quantum of unsold inventory did witness a slight decline, as developers vied to offload their inventory. Despite the adversities that obstructed residential real estate growth in 2017, there were developments that brought cheer to the sector as well. Office space absorption continued to remain robust across the country and Bangalore maintained its position as the city with the highest office space absorption. Affordable Housing was another segment that received much fillip from the Central Government.

On retrospection, the year 2017 has turned out to be a period of inflection for the Real Estate sector, with the industry observing a comprehensive shake down. It has been compelled to take cognizance of the fact that it can no longer work as an unorganized sector or on unscrupulous terms. In 2018, industry stakeholders are of the opinion that the heartburn that was witnessed in the sector in 2017 as a result of various policy reforms would eventually fade away, the reforms strengthening its foundations and transforming it into a robust, transparent and prosperous industry.

Do you expect Rental housing and Affordable housing to take off in a big way in FY2018-19?

'Housing for all' is a buzz word in the Central Government as well as Real Estate circles. With the Union Budget 2017-18 having emphasised on the importance of affordable housing, according infrastructure status to this sector, things are expected to change for the better. Given the benefits offered in the budget last year, the clearer definition of affordable housing in terms of area, relaxation of construction timelines for affordable housing projects, and tax incentives; the country's demand for housing has a fair shot at meeting its corresponding supply in the near future. Meanwhile, the nationwide scheme of Pradhan Mantri Awas Yojana (PMAY), launched in 2015 with an ambitious vision of providing affordable housing solutions for all Indian citizens, approved an increase in the carpet area of houses for the two-middle-income group (MIG) categories, in November 2017. We believe Affordable Housing will grow in the next 12-24 months, though Rental Housing would require careful planning in terms of regulatory environment (the National Urban Rental Housing Policy 2017 would need to be finalised).

Do you see newer reforms and sops for the real estate sector in the upcoming budget?

The real estate sector would ideally look forward to the following reforms/sops in the budget:

i. Reduction in the long -term capital gains holding period for REITs from three years to one year.

ii. Long-standing issues like taxability of sale of Floor Space Index (FSIs)/ Transfer of Development Rights (TDRs) as well as taxability of barter transactions in the form of giving away flats in lieu of development rights needs to be clarified. Further clarification is still awaited regarding inclusion of leasehold rights and tenancy rights in the definition of 'land and building' for the purpose of availing benefit of reduced holding period.

iii. Affordable housing segment has regulations which have a lot of exclusions, with its full potential yet to be realized. The rules need to be simplified with focus only on first house purchase (to prevent speculative buys) and quantum of the loan. Other conditions, including those related to the size of houses should be done away with.

iv. The premium/high end housing segment is under a lot of stress. The robust growth that Indian real estate sector saw was supported by purchases in all categories of houses. Lower taxes and extension of interest subsidy for larger loans over the next one or two years for a limited period, subject to Tier I cities, would help the segment. Premium houses, while smaller in numbers, may have the potential of providing a larger multiplier to the economy and can provide the required stimulus to sector.

v. The real estate sector would also benefit from a cut in corporate tax rates in order to make Indian companies competitive on a global level.

More incentives for Home Loan principal & interest exemption in personal income tax could indirectly help the real estate sector.

Could you comment on the changing dynamics as far as real estate project finance is concerned?

Real Estate project finance dynamics has been re-written post the implementation of the Real Estate (Regulation and Development) Act. The previous practice of pre-launch schemes which adversely affected home buyers is done away with and hence RERA aims to prevent malpractices, restore consumer faith in the real estate sector, regulate the real estate sector and promote transparency. One of the major implications of RERA is that the developer will now have to deposit 70% of the proceeds received from a project in a separate account, which can only be used for the earmarked project. This greatly affects the short-term liquidity of the developer. Further, developer is not allowed to sell any units without compliance to the mandated requirements and registration with the regulating authority, as a direct result the developers cannot raise capital for the initial stages of a project and have to rely on other avenues to raise the initial capital for their projects. The developer can avail of either debt financing or equity financing or a mix of debt and equity financing to raise the initial capital for their project. The cash flow generated from the project subsequently can be used to help repay the same. Funding of real estate projects can be obtained through multiple routes such as banks, non-banking financial institutions, or via external commercial borrowings.

Stringent provisions of RERA such as declaration of carpet area, display of all project information on the website, display of all approvals etc. may make investments more attractive to financial institutions. Financial institutions shall find it easier to carry out their due diligence before investing in a project. The project financiers shall find it easier to gather documents and adjudge the financial viability of a project. While top tier large scale builders with a substantial project portfolio, a stellar land bank and a good reputation shall find it easier to raise capital by means of funding, relatively smaller players in the real estate field shall find it difficult to get financial institutions to invest in them. A direct result of this shall be that the number of developers in the field shall reduce and only those developers with a sound business plan shall be able to carry on their business in the real estate sector. A number of projects being undertaken by developers who are facing liquidity issues shall be taken over by others having the means to raise such funding. A major concern for financial institutions shall be the provision under RERA which states that the developer shall not transfer or assign his majority rights and liabilities in respect of a project to a third party without obtaining prior written consent from two-thirds of the buyers, and without the prior written approval of the Regulatory Authority.

Ultimately, the introduction of RERA has increased project financing opportunities. Cautious financial institutions investing in projects after completion of legal due diligence and exhaustive market research have a lot of scope under the changing landscape of the real estate market in India.

What's your take on making green building development mandatory for all the projects?

Green building development may only be viable for larger integrated residential projects and commercial buildings, that too for sizes larger than a certain minimum square-footage. In current market conditions, we don't think this can be made mandatory for all projects. The first stage should be incentivizing use of renewal energy and proper waste management, whose scope can be broadened over a period of time to reduce overall carbon footprint of buildings.

What's the impact of GST and Real Estate Regulatory Act, 2016 (RERA) on the real estate companies and the buyers at large?

The primary issue concerning policy reforms like RERA & GST was the lack of clarity on how they would impact the country's real estate sector and the buyers/investors thereof. This has had a profound bearing on the stakeholders, as property markets are largely sentiment-driven. Consequently, residential markets were severely hit with new launches restricted to dismal numbers and the market witnessed depleting sale in housing units. The luxury market was affected the most, and the number of launches dropped considerably in this segment. Post a massive cash crunch due to demonetization and resultant project completion delays, the RERA compliance exercise turned complicated for many. The tax reform of GST, too, led to new launches drying up further in the market while increasing the number of fence-sitters who awaited a clear verdict on GST in real estate – whether it would aid the home buyers by bringing down prices, or lead to an escalation in prices. Hence, prices of properties remained largely stagnant across the markets in 2017, although a few locations with large quantum of unsold inventory did witness a slight decline, as developers vied to offload their inventory.

What's the solution to solving India's burgeoning housing problem?

With an estimated housing shortfall of more than 20 million units as per NHB in the country, the Housing problem requires a long-term action plan which the government is trying to address through the 'Housing for all' scheme. The Union Budget 2017-18 has accorded infrastructure status to the affordable housing sector, thus facilitating easier access to low cost funding. Given the benefits offered in the budget last year, clearer definition of affordable housing in terms of area, relaxation of construction timelines for affordable housing projects, and tax incentives, the country's demand for housing has a fair shot at being met by its corresponding supply in the next 4-5 years. Meanwhile, the nationwide scheme of Pradhan Mantri Awas Yojana (PMAY), launched in 2015 with an ambitious vision of providing affordable housing solutions for all Indian citizens, approved an increase in the carpet area of houses for the two-middle-income group (MIG) categories, in November 2017, thus expanding the scope of affordable housing. In addition to these steps, a more proactive approach, coupled with continuous monitoring needs to be adopted to ensure that the government and the industry are able to handle this concern.

About Shrinivas Rao

Shrinivas Rao, a founding member of Vestian Global Workplace Services, is responsible for Vestian's growth and expansion in Asia Pacific. With over 23 years of experience in global real estate industry, Shrinivas has assisted various multinational corporations with portfolio planning, strategic consulting, expansion/ relocation and project delivery in order to achieve their real estate goals in key Asian markets.

About Vestian

Vestian is an occupier-focused workplace solutions firm specializing in commercial, residential, industrial, retail and hospitality sectors. Headquartered at Chicago, Vestian has offices across US, India, China, Sri Lanka and the Middle East.

Photo Courtesy: Casagrand Builder Pvt Ltd | Project: Casagrand Miro, Manivakkam in Chennai