

Heads I buy, Tails I don't

The real estate market is much like the stock market; its peaks and bottoms are always discovered in hindsight. Being a buyer's market, the easy way out is to quote your price and see if developers are willing to sell, says Supriya Verma Mishra

WILL real estate prices fall further? Do builders have the financial muscle to complete ongoing projects? Should I hold my stocks in real estate companies or sell? These are the questions on everybody's minds. And answers are unfortunately hard to come by. As a buyer, one would want to save the last penny. But it is well nigh impossible to catch the market bottom. The real estate market is much like the stock market; its peaks and bottoms are always discovered with hindsight. Being a buyer's market, the easy way out is to quote your price and see if developers are willing to sell.

THE FACTS

Real estate projects are suffering from time and cost overruns as cash-crunched builders are finding it difficult to find buyers. This has put pressure on the prices and terms of trade have shifted in favour of the end user. Nonetheless, some basic facts must be borne in mind before deciding to make the down-payment for your dream home. First and foremost, one must be clear about whether the house is being bought for personal use or investment. Further, one needs to look at one's payment capacity. Going by human nature, one may like a house which is beyond one's budget. Is it advisable to stretch oneself to buy that dream home? If yes, how much should we borrow and what proportion should be funded internally. As a buyer, one should not be lured to buy a home only because the interest rates are low; rightly priced property must be available at a right location.

GET GOING...

Buying property for investment purpose is not really on people's mind in the current economic environment. With job security at stake, it is not advisable to commit any amount, however low the property prices or borrowing costs. For people who want to upgrade to a better location or buy their first home, this is the right time to look for that dream house. One should opt for a builder with a renowned name, so as to minimize the risks associated with project non-completion. Do not attempt to go bottom fishing, irrespective of the negotiating skills that you may possess. The other important thing to keep in mind is that real estate is a long-term asset class. Though selling one's house is the last thing that anyone would do, one must not be bogged down by short-term property price fluctuations. If you've zeroed in on the right location, the ideal strategy is to sit across the table and finalize the

deal. These negotiations may extend upto three-four months for properties that are still beyond affordable levels. Instead of trying to settle at the lowest price points, one must quote a rate based on financial strength. A word of caution: one should not get over leveraged as this would expose oneself to high risk.

DEMAND PULL

There is cautious optimism among the buyers after a drop in prices. After a significant drop in interest rates, a further 10-15% drop (depending on location) in prices is believed to be luring buyers. With the average home loan size hovering at Rs 15 lakh, according to the largest home financing company HDFC, and the ticket size for a 2BHK ranging from Rs 45-80 lakh, there is a big disconnect. The developers have finally realized that neglect of the strong middle class was a big blunder. And their focus has now shifted towards the affordable housing sector. This could bring buyer confidence back into the market.

STOCK MUSINGS

It might be good time for the home buyers, but the situation is not the same for investors of real estate companies. The stock market has taken a beating and the real estate stocks have been hammered beyond recognition. There are no visible signs of recovery, at least in the next 12 months. This has left the investors in a lurch. However, tough times like these call for tough decisions. As we all know, the demand has dried up, be it in the residential segment, retail or commercial. Many companies have committed huge funds towards ambitious projects. The completion of those projects, however, appears to be a bleak possibility. This would affect the companies' cash flows and have a bearing on revenues as well. In fact, some developers are diverting the limited funds to complete the low-margin affordable residential projects. Realising the potential demand in this category, some developers have even launched new projects. Despite the huge demand, this is a volume game with low margins. The business model of companies is therefore shifting from high-margin luxury apartments or villas to thin-margin mid market housing, thereby reducing the overall profit margins of the group company.

It is advisable for investors in real estate stocks to hold on to their investments. It would not be wise to liquidate a portfolio that has already shed 70-80%. There would be recovery in the market in the long term, when the real estate cycle revives.

On the other hand, some investors may be looking at buying real estate stocks as they have given up almost all their gains. Here again, it is not clear how quickly these developers will be able to get over their cash crunch.

Although shares may be available at low prices, it is advisable to wait and see how the real estate cycle turns out.

FUTURE MEASURES

The real estate as an industry has been painted with one large brush of corruption and greed. Some steps need to be taken to give the sector a clear and transparent image. Unlike the developed markets, there is no established housing index (other than the newly launched NHB index) that will help people to benchmark property prices for a certain location. This will not only help prospective buyers to know the prevailing rates in a particular locality, but also instill confidence in times of despondency.

Although the real estate sector has become organized recently, there needs to be clarity on the area (carpet or built-up) at which prices should be quoted. The stamp duty and registration charges have to be rationalized in line with the drop in prices. Multiple state laws, single window clearances and title clearances are other reforms that must be introduced to boost the country's second-largest employment generating sector.

Source: Economic Times dated 16/03/09