Emerging Trends in the inflow of FDI in Real Estate Sector and Indian Government Policy

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Abstract :

As per the World Investment report 2008, India is the 2nd most attractive location for FDI. At the same time the real estate sector in India has assumed growing importance with the FDI flow. Development in the real estate sector are being influenced by the development in the retail, hospitality, hotels, resorts, IT enabled services and vice-versa. It is also clear from the above that real estate sector is a major employment driver being the 2nd largest employment generator next only to agriculture. Real Estate Sector also giving value addition to apporx. 250 associated industries like Cement, Steel, Logistic, Airports.

***IndexTerms* - Real Estate, FDI, Employment.**

Thriving Inflows

With the advent of globalization, developing economies have been witnessing an intensive rise of foreign direct investment (FDI) inflows during the past two decades. FDI has grown more rapidly than world trade and world output. As explained by the colossal surge in FDI flows crosswise over nations is one of the apparent indications of the globalization of the world economy in the course of twenty years. It has been seen as the prime agent of change for economic growth in developing countries. It influences the economic development by encouraging investment, growing employment opportunities, improving efficiency and by enhancing innovation in the host nations. The political and economic changes occurring in many of the world's emerging market economies have driven much of the increase in FDI. FDI brings in advanced technologies, transmits information, skill-set and grants entree to export market alongside with venture and management know-how. It makes available a large amount of foreign currency to assist in reducing the balance of trade deficit. At the point when overseas venture enters into rivalry with native firm, the local firms are enforced to develop their own technology, skill and management expertise. FDI is a significant means to channelize technology transfer and capital hence alleged to be an important factor encouraging economic growth of emerging economies. Additionally, MNCs regard FDI as an imperative instrument to restructure the manufacture activities crossways boundaries in harmony with their business plans and the competitive edge of host economies. Traditionally, India has pursued a really vigilant attitude however since 1991, with the initiation of economic reforms, India has been more liberal towards its foreign investors and got sequence of actions to draw in FDI. It gradually started gathering up by means of added liberalized policy attitude of other emerging market economies since the early 1990s ahead, etcetera in terms of broader access to diverse regions of the economy, moderation concerning rules for owning equity, comfort of starting business and repatriation of profits and dividends. This rational liberalization, together with substantial improvement regarding macroeconomic fundamentals, revealed in mounting size of FDI inflows to the country showing an increase of closely 5 times through the first decade of present-day millennium.

The emergence of real estate as a lucrative investment option against bonds and equity has led to strong inflows in the sector. We estimate US$7-9bn annual investment through domestic and overseas real estate funds, of which US$4bn is expected through the FDI route. This amount is large enough to finance total cumulative investments required for office and retail construction in India. Further, through the capital markets, developers have raised US$4bn in the past two years and are expected to raise US$4.7bn this year. There is a considerable money flow, which is fuelling further growth by increasing liquidity in the market.

In the past two years, many real estate developers raised substantial funds through various routes (PE/IPO/FCCB/QIP/FPO) at corporate of SPV level. We estimate that real estate developers raised US$4bn in the past two years. By year-end, another US$4.7bn is expected to be raised by DLF, Omaxe and Emaar MGF.

Recent moves by the Reserve Bank of India (RBI) and the central Government to curb overheating in his real estate sector have slowed down the flow of money through traditional channels such as bank loans. However, foreign flow into the Indian realty market is the only funding option that the Government has not been able to block successfully. We expect strict measures by the RBI to curb the flow; some action has already commenced

Table – 1

Funds raised by real estate companies

Companies	Amount (INR mn)	Instrument	Status
Hiranandani	33,750	AIM	Completed
Unitech (Unitech Corporate Park)	31,900	AIM	Completed
K Raheja (Ishaan)	17,100	AIM	Completed
India Bull Real Estate (Dev Property Devlopers)	12,000	AIM	Completed
Parsvnath	10,900	IPO	Completed
Pnsal Properties	10,000	QIP	Completed
Anant Raj	6,840	PE – Morgan Stanley, GIC, Quantum	Completed
Oberoi Constructions	6,750	PE – Morgan Stanley	Completed
Sobha	5,692	IPO	Completed
DSK	5,500	FPO	Completed
Mahindra Gesco	4,725	QIP	Completed
Akruti Nirman	3,600	IPO	Completed
Mantri Developers	3,000	PE – Morgan Stanley	Completed
Lodha Group	2,684	PE – JP Morgan	Completed
Prajay	2,640	FCCB	Completed
RR Industries	1,980	PE – Old Lane	Completed
Peninsula Land	1,700	QIB	Completed
Nitesh Group	1,350	PE	Completed
Orbit	1,000	IPO	Completed
Ansal Housing	1,000	QIP	Completed
Lokhandwala Builders	968	PE-Trinity Capital	Completed
Kapstone Constructions	882	PE-Trinity Capital	Completed
Emaar MGF	90,000	IPO	Expected
DLF	100,000	IPO	Ongoing
Omaxe	6,750	IOO	Ongoing
Total	**362,711**		

optional and non-convertible preference shares have been classified as external commercial borrowings (ECBs). Further, norms for investments through the ECB route have been tightened. This has significantly impacted developers' capital raising plans; other such stringent norms are likely to follow. Reduction of foreign capital flow into the Indian real estate market would affect the overall health of the sector and jeopardize many large development plans.

Table – 2

Proposed Investments in Indian Realty Sector

Overseas Investments	Investments (US$ mn)	Country	Project
Macquire Bank	25,000	Australia	Modern Integrated township Spread Over 65,000 acres in Andhra Pradesh; JV with three Partners
Al Nakheel LLC	20,000	Dubai	Two townships spread over 20,000 acres; JV with DLF
Royal Indian Raj	2,900	US	Royal Garden City, Bangalore, over 10 years
Tishman Speyer Properties	2,000	US	Township spread over 400 acres near Hyderabad; JV with ICICI and nagajuna Constructions
Carlyle	1,000	US	Multiple/commercial
Blackstone Group	1,000	US	Multiple
Emmar Properties	800	Dubai	Township Hyderabad & commercial
HDFC	720	India	Unknown
Sun Apollo Ventures	630	US-India	Unknown
ILFS	525	India	Unknown
Trikona Capital	450	AIM	Unknown
Peninsula Realty Fund	200	India	Unknown
IDFC	345	India	Unknown
Hines and Maia	250	US	Unknown
Ascendas Fund	230	Singapore	Commercial Project
IREO	180	US	Pune– Office & Residential
Pegasus Realty	150	US	Unknown
Citigroup Property Investors	125	US	Unknown
Lee Kim Tah Holdings	115	Singapore	Township Chennai
Kotak Mahindra Realty Fund	115	India	Unknown
Morgan Stanley	70	US	Housing Bangalore
Dewan Housing	69	India	Unknown
GE Commercial Finance Real Estate	63	US	Unknown
Kshitij	57	India	Unknown
Fire Capital	50	India	Unknown
Edelweiss Capital	35	India	Unknown

Keepel Land	Unknown	Singapore	Condominium – Bangalore
Universal Success Enterprise	Unknown	Indonesia	Housing Kolkata
Capitaland	Unknown	Singapore	Housing Mumbai
Evan Lee & Co Pvt. Ltd.	Unknown	Singapore	Township Vizag
Salim Group	Unknown	Dubai	Township Kolkata
Merrill Lynch	Unknown	US	Unknown
Tata, Kotak, ICICI, UTI and others	Unknown	India	Unknown

FDI in the Indian real estate market has grown significantly in the past four years. This is largely attributable to Government's initiatives of opening up the sector to FDI in February '05 and to the strong fundamentals driving the sector. We estimate FDI in the Indian real estate market at US$4-5bn annually for the next five years. A recent AT Kearney report rated India as the second best destination for FDI investments after China.

Table – 3

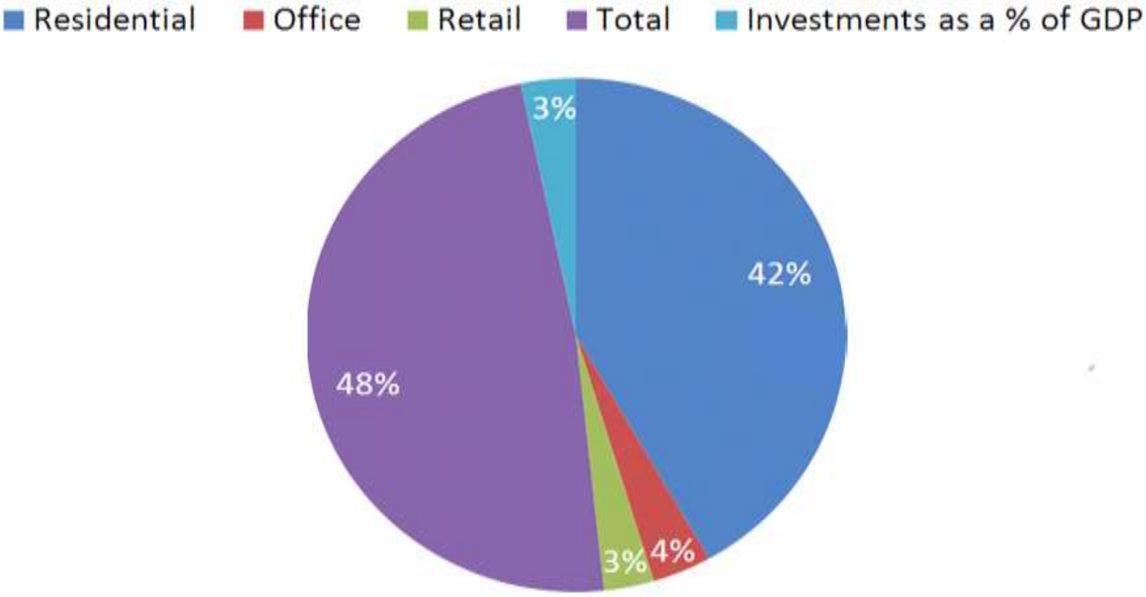
FDI in India

Year	US$ bn	Share of Real Estate	
		%	US$ bn
2003-2004	4.3	4.5	0.2
2004-2005	6.1	10.6	0.6
2005-2006	7.7	16.0	1.2
2006-2007E	15.0	26.0	3.9

Indian Real Estate Pie

We estimate the current size of Indian real estate market at US$57bn or 6.2% of India's GDP. In terms of value the real estate market would likely grow at 12.8% CAGR in the next five years to US$105bn or 7.1% GDP by FY12E. In the next five years, the average annual investments required in the real estate sector are US$.85bn. These are based on requirements of investments in land and construction cost to meet the intrinsic real estate demand in India and no on sales as the mark up on costs could vary with market conditions of which the residential

Demand in FY12E



Graph – 6.1

Demand forecast (US$ bn)

Sectors	Demand in FY07	Demand in FY12E	Average Demand In next five years	CAGR (%)
Residential	51.7	90.6	74.1	11.9
Office	3.0	7.7	5.7	20.9
Retail	2.7	6.5	4.8	19.5
Total	57.3	104.9	84.7	12.8
Investments as a % of GDP	6.2	7.1	6.8	

segment constitutes 88% at US$74bn. We estimate annual investments for office space at US$5.7bn and retail segment at US$4.8bn.

FDI inflows to India witnessed significant moderation in 2010-11. This raised worries in the wake of flaring current account deficit in India far beyond the professed sustainable level of 3 per cent of GDP through April-December 2010. FDI inflows fell in the year 2012; reason could be traced to the government‘s decision taken in 2010 to prohibit FDI in manufacturing of 'Cigars, cheroots, cigarillos and cigarettes, of tobacco or of tobacco substitutes'. It seems that initially FDI inflow in India was less, grew significantly up to 2009 then slightly came down, this is due to sub-prime crisis of 2008. But in terms of amount, the

FDI inflow in India grew significantly. Various FDI reforms and favorable measures have been adopted by the Indian government in the last ten years (discussed in the next section) in order to entice foreign investors to invest in India and which has certainly helped India in receiving FDI amounting US$ 34416.8 in the year 2014.

Conclusion

The results indicate that the probability value of t-statistics to be near to 5 percent level of significance. Henceforth, with 90 percent confidence level; it can be concluded that there exists significant long term positive trend in FDI inflows in India. The results indicate that on an average FDI of 2173.684 million of US$ comes in India every year. The slope coefficient is positive, which indicates the presence of positive trend of FDI inflows in India. The F-statistics is found to be 4.778 with probability value of 0.056; this indicates the statistical significance of the model at 90 percent confidence level. The R- squared of 0.3467 indicates that there exist significant and positive upward trend in the behavior of FDI inflows in India and 34.67 percent of the variance in FDI inflows in India can be explained with the help of trend analysis as estimated by bivariate regression model. Liberalized FDI reforms adopted by the government have been able to create an investor friendly environment and thus have played a major role in attracting FDI inflows.

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