

IMPACT OF THE RERA ACT, 2016 ON REVENUES OF INDIAN REAL ESTATE DEVELOPERS

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1. ABSTRACT

Real Estate Regulatory Act (RERA) came into force across India on 1st July 2017. The Real Estate Regulatory Authority (RERA) was formed to bring transparency, accountability and efficiency into this sector with the rights and duties of both buyers and developers being clearly defined. Individual states established state level regulatory authorities in a phased manner. RERA covers both existing and new projects under its ambit. This paper envisages to explore the economic impact of RERA on revenue of real estate developers.

The top 10 real estate developers by market capitalisation are considered as the sample for this analysis. Income statements from January 2017 to December 2018 are used to gauge the impact of RERA on revenue of real estate developers. We find that the disruptions caused in the in the real estate industry because of introduction of RERA do not significantly impact the revenue of Indian Real Estate Developers.

KEYWORDS: Financial Performance, Real Estate Developers, Real Estate, RERA, Real Estate (Regulation and Development) Act 2016, Revenue, RERA Act 2016

2. INTRODUCTION

Real estate can be defined generally as space delineated by man, relative to a fixed geography, intended to contain an activity for a specific period of time.

Real estate can be classified as: Residential new houses and existing houses for resale, Commercial shopping centres and offices, Industrial and manufacturing buildings and property and vacant land and farms. In simple words we can say that a person having any one of the above property is called a Real estate owner. Real estate is a property consisting of land and the buildings on it, along with its natural resources such as crops, minerals, or water; immovable property of this nature; an interest vested in this; (also) an item of real property; (more generally) buildings or housing in general.

Real estate sector, which has forward and backward linkages with more than 250 different sectors, is the second largest employment generator in India after agriculture. The sector correlation with GDP is high at 0.78x (every INR1 invested in the sector directly adds INR0.78 to the GDP) and there is significant room for improvement, as real estate sector correlation in other large economies (such as China, the U.S., the U.K., Germany, Spain) is at least 0.9x. According to the Economic Survey 2015-16, the real estate sector constituted 7.4 per cent of India's GDP in 2014-15.

Before the introduction of The Real Estate (Regulation and Development) Act, 2016, Indian real estate customers had little legal recourse and consumer protection was offered to them under various acts such as: The Indian Contract Act, 1872; The Consumer Protection Act, 1986. Indian consumers had to approach various authorities such as, Consumer Courts and Civil courts, to get their grievances addressed. Before the passage of the act, no single regulatory authority existed for regulation of real estate sector and buyers were facing problems like timely delivery of projects, possession not being handed over by the developer, high rate of interest being charged on late payments, multiple bookings for the same property, misselling of projects etc. The developers were facing issues like delay in construction permits, late payments by homeowners and operations in a non-transparent environment.

The Real Estate Regulatory Authority (RERA) was formed to bring transparency, accountability and efficiency into this sector with the rights and duties of both buyers and developers being clearly defined. This research aims to evaluate the short term impact of Real Estate (Regulation and Development) Act, 2016 on the real estate developers.

3. REVIEW OF LITERATURE

(Singh, 2009): In her paper titled "Problems and Prospects of Real Estate in India", she states that the different types of real estate are: Agricultural, Residential and Commercial. She also states that features of real estate market are: Immobility, Heterogeneous, Durability, Bothan investment good and consumption good, long time delays, High transaction costs.

(CRISIL, 2017): In their research report titled “RERA is all about effective implementation “ they state that “CRISIL Research believes with effective implementation of RERA, the sector is expected to see improved transparency, timely delivery, and organized operations. While the ongoing projects have been given a timeline of three months (May-July 2017) to comply with RERA regulations, the Act does not permit developers to launch new projects before registering them with the RERA authority. This will be a major shift from practices followed currently by developers wherein they manage to sell part of the project through soft-launch/ pre-launch activities. RERA is also expected to put an end to fund diversion, and transform the realty sector into a more organized and trustworthy one, re-instilling the confidence of the end-users towards the market.” CRISIL research also states that “During the procedures, documentation and quarterly disclosures. They may also have to opt for joint ventures with big players to survive in the market, which will eventually remove all the unorganized players in the real estate sector. This, along with the registration and approval costs, are expected to increase the compliance cost for realtors.”

(Das, 2017): In his research report titled “RERA through a magnifying glass “he states that “The implementation of the Act, in its entirety, will have a far-reaching impact on the real estate sector. The Act will be a game changer for the entire sector and will transform the entire paradigm in which the sector operates and the manner in which different stakeholders interact with each other. Implementation of the provisions of the Act will cause some teething troubles in the short term but in the long run, the sector will stand to gain. The Act will require developers to recalibrate their business model so that it complies with the various provisions of the Act. Participation from homebuyers will galvanise the fortunes of the sector and help the cash-strapped developers. The confidence flowing into the sector, from the provisions of the Act, will also rub off on institutional funds and banks, thus enabling them to lend to the sector. The access to funds at competitive rates, which in the present day are pretty high, could lead to rationalisation of prices within the sector thereby making it a win-win situation for all the stakeholders. Most importantly, the Act will ensure that only serious and strong players remain within the sector. Therefore, going forward, a consolidation among players within the sector cannot be ruled out. The success of the new rules of the game will however, lie in having the necessary systems and processes across states so that the act can be implemented in full letter and spirit without causing much distress among the relevant stakeholders.”

(Housing News Desk, 2017): In their article titled “Real estate sentiments turn negative on RERA, GST implementation: FICCI-NAREDCO-Knight Frank India’s sentiment index” they state that “The short-term uncertainty over new policies such as RERA and the GST, have turned

real estate sentiments negative for the first time since Q4 2015, according to FICCI-NAREDCO-Knight Frank India's sentiment index”

(**Sharma. N. 2018**): In his article titled: “Developers to focus on ramping up systems for RERA compliance” he states that “Over the years, real estate sector has been characterised by myriad unstructured practices, which has given a very different perception of the sector to the larger stakeholders of the economy. These practices have led to increase in the number of litigations, marked with worsening customer sentiments as seen in the recent times.”

(**Sharma A., 2018**): In his article titled “Over 40% developers have no formal process in place to comply with RERA: Survey” he states that “About 45 per cent developers across India have no formal process in place to manage compliance mechanism of RERA while 44 per cent have made some modifications to their MIS (Management Information System), a recent survey by FICCI and Grant Thornton Advisory has revealed.”

(**Housing News Desk, 2018**): In their article titled “What is RERA and how will it impact the real estate industry and home buyers?” they state that “Impact of RERA on real estate industry will be Initial backlog, Increased project cost, Tight liquidity, Rise in cost of capital, Consolidation, Increase in project launch time.”

(**Shenoy, 2018**): In his article titled “RERA's conciliation tool brings hope to common man”, he states “Before the Real Estate (Regulation And Development) Act, 2016 (RERA) came into effect the affected buyers of real estates could only approach the civil courts, criminal courts or consumer forums under the provisions of the Maharashtra Ownership of Flats Act (MOFA) or the Consumer Protection Act, 1986.”

4. OBJECTIVE OF THE STUDY

To study the impact of RERA on revenue of Indian Real estate developers.

5. HYPOTHESIS

Null Hypothesis **H₀**: RERA has no impact on revenue of real estate developers $\mu=0$

Alternate Hypothesis **H_a**: RERA has a positive impact on revenue of real estate developers $\mu>0$

Where μ =mean of change in revenue of population

6. IMPORTANCE OF STUDY

The study shall be useful in determining the impact of RERA on revenue of real estate developers.

This nature of the research will be descriptive. Quarterly income statements of Indian real estate developers is used. Convenience sampling will be used in this study. 10 listed developers ranked by market capitalisation will be considered as sample. Ratio data is the type of data being collected. The population is assumed to be normally distributed i.e. the revenues of all real estate developers follow a normal distribution. Since the type of data and normal population, one tailed paired T-test has been used to evaluate the impact of RERA on sales of real estate developers.

7. DATA ANALYSIS AND INTERPRETATION

The calculation of revenue for six monthly periods has been done in table 1 as per the following formula: Revenue for i^{th} month period = Revenue for current quarter + Revenue for previous quarter

Where i = Quarter ending month in consideration

Table 1

Revenue (in Crores)				
		Time period		
RANK	By market cap	Company	Jan-Jun 2017	Jul-Dec 2017
1		DLF	4272.88	3281.43
2		Godrej Prop	679.93	1119.35
3		Oberoi Realty	550.24	659.72
4		Prestige Estate	2723.33	2370.40
5		Indiabulls	1513.85	2821.71
6		Sunteck	271.29	548.23
7		Sobha	1238.40	1316.00
8		Omaxe	581.02	628.54
9		Brigade	1108.78	908.62
10		Puravankara	661.60	686.15

Table 2

		Revenue (crores)			
		Time period			
RANK By market cap	Company	Jan-Jun 2017	Jul-Dec 2017	Difference (xi)	(m-xi)^2
1	DLF	4272.88	3281.43	-991.45	1134934.40
2	Godrej Prop	679.93	1119.35	439.42	133617.29
3	Oberoi Realty	550.24	659.72	109.48	1267.14
4	Prestige Estate	2723.33	2370.40	-352.93	182169.33
5	Indiabulls Real	1513.85	2821.71	1307.86	1522699.23
6	Suntech Realty	271.29	548.23	276.94	41232.14
7	Sobha	1238.40	1316.00	77.60	13.81
8	Omaxe	581.02	628.54	47.52	695.007
9	Brigade Ent	1108.78	908.62	-200.16	75099.56
10	Puravankara	661.60	686.15	24.55	2433.74

Table 3

Sample mean	m	73.88
Sample Standard Deviation	s	586.34
Standard Error	S	185.41
No of samples	n	10
Degree of freedom	df	9
Critical value	c	0
Test Statistic	ts	0.3985

$$t_s = (m - c) / S \quad df = n - 1$$

One tailed paired T-test is applied on the revenues across both time periods for respective developers from the above calculations and tables. We find from standard one tailed t distribution table that $t_{0.05}$ for df of 9 is $t_{0.05} = 1.833$.

RESULT

Since $t_s < t_{0.05}$ i.e. $.3985 < 1.833$, we **fail to reject** the null hypothesis **H₀** at a level of significance of **5%**. Hence we can say with 95% confidence that **RERA does not have a significant impact on revenue of real estate developers.**

8. ASSUMPTIONS

- Profit margin on sales for population (real estate developers) follows a normal distribution
- All developers are in compliance with provisions of RERA
- Sample real estate developers derive most of their revenue from products covered under RERA
- Sample size of 10 is large enough to have good power of paired t test
- Only short term effects of RERA are considered.
- Other external shocks to the real estate industry have been ignored
- Only income from normal operations has been considered.
- Revenue from exceptional items like selling of assets to repay debt has been ignored.

9. LIMITATIONS OF STUDY

This study is able to gauge only the short term impact of RERA on real estate developers due to non-availability of data. Also, data shall be collected from listed public real estate developers since their accounting methods are most transparent and they will comply to the maximum extent with the provisions of RERA. Impact of inflation on income statements has been ignored.

10. CONCLUSION

The null hypothesis is failed to reject at a level of significance of 5% and thus RERA does not have a significant positive impact on revenue of real estate developers. Thus disruption caused by introduction of regulation in the real estate industry has impacted the revenue of Indian Real Estate developers non-significantly in the short term. Also, the medium/ long term impact of RERA can be gauged once enough time passes post implementation of RERA.

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