

The Housing Opportunity in India

This article is authored by MOI Global instructor Rahul Saraogi, managing director of Atyant Capital Advisors, based in Chennai, India.

That homeownership is a big driver of economic activity is a well-established fact in modern economics. Homeownership is directly correlated to several factors including but not limited to purchasing power or affordability, employment, availability of mortgages, interest rates on mortgages, physical and social infrastructure, taxation and property rights etc.

Housing in major Indian cities has traditionally been unaffordable for the average middle-class buyer. In the past housing demand was concentrated in city centers due to limited physical infrastructure that resulted in long commute times from peripheral areas. Social infrastructure like schools and hospitals were limited in quantity and in quality and as a result those who chose to live in peripheral areas had a much lower quality of life than their peers who lived inside cities.

The trifecta of dysfunctional capital markets, illicit cash in the economy and high interest rates on mortgages played their role in making housing further inaccessible and unaffordable for the average buyer. Dysfunctional capital markets resulted in concentration of capital and a tendency among homebuilders with access to capital to hoard land. This was further accentuated by illicit cash in the economy which fueled purchases of land as a store of value. High headline inflation of between 4% to 6% resulted in high nominal mortgage rates of between 8% and 10% for mortgages that extended for a maximum duration of 15 years. This made it difficult for an average home buyer to make monthly mortgage payments for homes with the needed standard of living.

The entire housing and real estate industry in India was therefore an overleveraged, capital appreciation game where lenders, developers, so called investors and wealthy buyers were all in a nexus of convenience to the detriment and exclusion of the average homebuyer. It is no wonder then that according to a KPMG-NAREDCO study, India has an urban housing shortage of 18 million units while tens of thousands of completed homes remain unsold in major Indian cities.

The scenario has changed materially in India in the previous few years. Urban infrastructure, though far below what would be desirable, has improved steadily with the construction of metro rail systems, rapid bus transit systems, bypass roads, ring-roads and in-city overpasses. Significant investments have been made in expansion of water, sewage and waste management infrastructure. Social infrastructure like schools and hospitals has improved in both quality and quantity. As a result, the quality of life in peripheral areas of cities has improved.

The curbing of illicit cash in the economy has had a deflationary impact on the real estate sector. Land as a store of value has been steadily losing sheen and capital allocated to the real estate sector has been moving to productive and yield generating assets like offices, warehouses and housing. This has upset the erstwhile capital appreciation business model of real estate developers. Equity in a real estate project is less valuable than before and only marginally more remunerative than high cost debt. This has disincentivized over leveraging

by developers. Real Estate development is gradually becoming a volume throughput game. Developers who can efficiently utilize capital and deliver value are able to scale rapidly with external capital (equity and debt) and in the process are able to earn high returns on their own capital.

The government's thrust on housing for all through the PMAY scheme has been a game changer for home ownership. Under this scheme, housing loans under LIG (Low income group), for homes below 650 sq.ft. in size and for loans below USD 8,700 in value, receive 6.5% interest subsidy per year. Housing loans under MIG-1 (Middle income group), for homes below 1,725 sq.ft. in size and for loans below USD 13,000 in value, receive 4.00% interest subsidy per year. Housing loans under MIG-2, for homes below 2,150 sq.ft. in size and for loans below USD 17,400 in value, receive 3.00% interest subsidy per year. With unsubsidized mortgage rates on 15-year loans at 8.5%, the interest subsidy under the PMAY scheme has had a catalytic impact on housing demand.

The Real Estate Regulation Act (RERA), the Goods & Services Tax (GST) and the Insolvency & Bankruptcy Code (IBC) have empowered home buyers of under-construction properties and have caused weaker developers to close shop. This has expanded the market opportunity for strong and scrupulous developers. With reforms in place and a reset from the sins of the past, housing is likely to be a big driver of economic growth in India and it presents a large opportunity for allocators of capital looking to invest in India.

Rahul Saraogi is the founder and managing director of Atyant Capital Advisors, advisor to the Atyant Capital family of funds. In the last two decades he has focused on the Indian markets. His mission is to consistently identify the best 10-15 investment ideas from among the thousands of publicly-traded Indian corporations.

Rahul's value-based philosophy stands apart due to his belief in the paramount importance of corporate governance, specifically how management operates with minority shareholders in mind. Rahul is the author of [Investing in India](#), a definitive guide to navigating the Indian markets, published by John Wiley & Sons.

Rahul graduated from the Wharton School of the University of Pennsylvania with a degree in Economics. Outside of Atyant, he practices Vipassana, a 2,500 year-old meditation technique that helps people see things as they really are. Rahul splits time between Chennai and Miami.