

RISK FACTORS IN REAL ESTATE DEVELOPMENT IN THAILAND

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Abstract

Thailand's real estate housing development and related businesses have been blamed as one element that amplified the negative factors in the 1997 economic crisis in Thailand. Unpaid debts from excessive loans from financial institutions before the crisis, became non-performing loans afterwards. Unsold properties became non-performing assets. The majority of real estate companies went bankrupt and left unfinished building constructions. All this destroyed consumer confidence in the real estate business, and reduced or delayed housing purchase and payment. The real estate business was branded as a non-performing business.

However, now in 2003, the real estate development industry is promoted by the Thailand government as a sector which can help boost the country's economy. Many governmental supporting policies and statements have been issued. Consumers are increasingly buying. Many companies that managed to survive the crisis, and many which were resurrected from bankrupt companies, have begun to compete in the business again, although with caution having learnt a hard lesson. But questions have now emerged as to whether this increase in sales will one day lead to a new crisis.

The aim of the paper is to describe and analyze risk factors in real estate development which should be considered to prevent future failure. It focuses on the period 1997 to 2002. It includes: reasons why the real estate business was blamed for its part in the 1997 crisis, and why it is now being promoted to boost the national economy; the effects of mistakes in governmental policies for financial institution practice; and factors that accelerate and worsen the normal downturn of economic and real estate cycles. The paper analyses many factors, and the relationships between them.

The paper shows cause-effect factors at the national level, in financial institutions, in real estate development firms, and at the consumer level. It compares and contrasts the situations in 1997 and 2003 so as to study the risk management issues.

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This paper is concerned with a highly complex situation, intertwined with the wider aspects of finance and politics, with a mixture of international and local forces, with governments and consumers, and with a period from boom to bust and recovery.

1. INTRODUCTION

Real estate business is a high return business, and naturally is therefore a high-risk business. This business was the core of concern during the 1997 economic crisis and the aftermath period, with two very contrasting attitudes: as one of the causes of the 1997 crisis, and as an industry to boost the national economy in 2002. The industry involves about 20 related jobs, and accounts for about 25% of Thailand's GDP. Thus, it is important to learn about the factors and circumstances involved during these bust and boom years.

The paper analyses factors and experiences learnt during this period, and the relationships among these factors, in the real estate business. The research approach is through synthesizing and analyzing information, critiques, and documents concerning this important topic, and through linking the banking crisis and the financial crisis.

2. REASONS REAL ESTATE WAS BLAMED AS A CAUSE OF THE CRISIS

In 1995-1996, the real estate cycle already showed indication of problems, in term of high overbuild of office blocks and condominiums. Many analysts prophesied that the real estate cycle would soon be in its 'bust' phase regardless of the exchange rate crisis (Sayarmwalla 1999, Renaud 1998, Herring 1999). In addition, the exchange rate crisis accelerated, thus exacerbating the down-turn cycle in real estate.

It will be shown how and why real estate was blamed as an important factor in exacerbating the economic crisis which resulted in national problems and real estate industry problems. Using a cause-effect method to capture risk factors, the Appendix shows the Summary of Circumstances and Factors Related to the Economic Crisis and the Recovery Period.

2.1 International Conditions and National Policy Problems

In describing the recent economic crisis in Thailand from 1997 to 2000, the important milestones and conditions, locally and internationally, have to be described for five years prior to the crisis. These milestones and conditions include:

2.1.1 International Conditions at the Time

1. Shortage of attractive investment in the advanced economic countries.
2. Low interest rates dominant in the developed world.
3. Investments in manufacturing capacity brought about by the relocating of industry from East Asia after the depreciation of the yen.