SUMMARY

During the recession in 1985/86, many developers, especially the smaller ones, found themselves in financial difficulties. In 1998, they again faced the same problems. They asked themselves this same set of questions - why did it happen? Is it due to an inappropriate method of feasibility study or is there something that is lacking in the way they manage their finance?

Most of these developers evaluate the viability of a project by first estimating the value of the completed property. The valuation is based on the current prices of similar projects or upon consultation with professional valuers who will give a value based on the market comparison method at the time of project evaluation. As there is a lead-time of one and a half to two years in the construction of a real estate project, such a method of project evaluation has its limitations. This is because the real estate market moves in cycles from boom to bust as seen in Singapore, Malaysia and Thailand during the 1980s and 1990s. A feasibility study on the viability of a project without first studying the real estate cycle of the particular sector may lead to higher risks and result in losses and project failure if the project commences at the wrong time or during the downswing.

The purpose of this dissertation is to understand the financial management method of small developers. Small developers do not have the financial resources of the larger developers, particularly the publicly listed companies who are able to withstand a prolonged downturn in property prices and a recession. The project evaluation technique as well as the impact of timing along the various phases of the real estate cycle and its implications on profitability and the risk of bank loan default will be analysed. It can be seen that the right timing, by commencing a project at the right phase of the real estate cycle, will result in extra profits. Commencing a project at the wrong time may have disastrous consequences resulting in financial losses. It has been seen in the 1985/86 recession and again in
1998 that should the final selling price of the project fall short of the projected selling price by 20% or more, developers will face serious financial difficulties.

In summary, developers, in order to succeed in their developments, need to understand not only the basic methods of financial management but must also possess a clear understanding of the real estate cycle. In the evaluation of development projects, they should factor in the expected prices of the completed properties as dictated by the real estate cycle through trend analysis or other methods of forecasting and not only by the usual market comparison method. The study shows that projects for development should commence during the upswing of the real estate cycle and not at the peak or during the downswing. This is especially important for the small developers who have limited resources.