The real estate and financial crisis: Causes, effects and impacts on development

Seminar organized by the UNECE Secretariat and Real Estate Market Advisory Group (REM), with the support of the International Real Estate Federation (FIABCI)

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Conference Room 8, 3:00 – 6:00 p.m.

CONCEPT NOTE

The overriding message of the seminar is that the real estate sector, if well regulated and based on a transparent real estate and financial market could be a driving force for development, producing social, economic and environmental benefits to member States. It could indeed drive a recovery towards more sustainable economic systems and stronger and healthier production and consumption patterns in emerging markets.

The current global financial crisis is the result of inadequate regulation of real estate and financial markets. Real estate bubbles were allowed to improperly inflate, mortgage lending was improperly supervised, financial markets were allowed to develop complex financial instruments that few understood, credit risk was inadequately modelled, and credit ranking agencies failed to carry out their fundamental role. Investors also failed to properly understand the instruments they were buying and consumers failed to evaluate the risks they were undertaking in buying inflated property with innovative mortgages.

The crisis developed despite the fact that methods and regulations of managing credit risk existed, such as those incorporated in the Basel 2 regulations. These regulations and methods simply failed to properly consider the true level of risks that were involved in issuing sub-prime mortgages and their securitization. The inadequacy of these tools has now become very widely publicized.

The financial crisis is having repercussions on economies throughout the world and is likely to be the most severe global crisis since the Great Depression of the 1930s. As it is becoming a global challenge, the United Nations through a number of different initiatives is trying to understand its root causes, as well as the effects and impacts of the crisis on development. In addition to providing advice on addressing the current crisis, there is a need to discuss institutional changes and ways to operate that will help world markets to avoid similar shocks in the future and make the real estate sector more stable and sustainable.

Since the financial crisis was generated by turmoil in the real estate market and triggered initially by the sub-prime mortgage crisis in the United States, this sector needs special attention. Every developed country’s economy is underpinned by their real estate and property market, thus addressing this specific issue would assist the recovery towards more sustainable economic systems. More generally, there is evidence that property values are particularly “bubbled” in a number of emerging European markets. This raises questions about whether there will also be behavioural consequences in such markets.
Indeed, the perception of ever-upward land and property values in most markets has been materially responsible for this current financial crisis. Individuals have been encouraged to borrow excessively against the perceived value of their property and the resulting upward pressure on values caused speculative bubbles. In turn, easy access to cheap credit exacerbated the situation by abnormally increasing the demand. The crisis would not have been so acute and serious if housing prices had remained anchored to fundamentals; but instead, demand was driven by the expectations of further price increases.

Any solution to the current financial crisis will also be dependent on returning stability to the real estate and property market. More generally, this is both a real estate and financial crisis.

The overall purpose of this panel discussion is to initiate dialogue within the United Nations, not only on the financial aspects of the current crisis but also on the real estate market as a sector. There is an obvious need for improved regulation of both the real estate and financial markets, and for greater collaboration between private sector advisory professionals and public sector regulators turned rescuers. With Governments seeking long-term paybacks of bail-out funding and thus taking more embedded and deep-rooted positions in distressed real estate markets, the success of effective public-private partnerships will underlie work-out strategies in many markets. In this context, the discussion will identify a need for organizations such as the United Nations to provide better advice to Governments regarding regulatory practices in the real estate sector. The panel should attempt to address the following issues:

- The effects of the real estate and financial crisis on overall development in specific regions and worldwide, and identifying sectors and areas for priority action;
- The roles played so far by the United Nations in discussing the issue, including reports on the interactive discussion on the financial crisis held at United Nations Headquarters in New York on 30 October and the Financing for Development conference held in Doha from 29 November to 2 December 2008;
- The existing and possible roles for the United Nations to provide a forum for addressing additional financial and real estate issues and advising countries on the matter, including existing good practices;
- The need for targeted responses that Governments could develop to limit the damage of the current financial crisis and re-establish a healthy real estate market;
- Post-crisis policy guidelines for both the real estate and financial sectors that will promote stability and sustainability;
- More specifically, the characteristics that a new real estate market and credit system should have, including collaborative standard setting for increased informational transparency, limitations on the use of complex financial tools, better capital risk allocation models, and policies and actions to sustain investors’ confidence and increase citizens’ trust;
- Given that the real estate sector seems susceptible to recurring boom-bust cycles, what policies can be implemented to reduce the volatility of investment and employment in this sector, and stabilize the asset value of housing for family finance.
The seminar will also discuss the need for more comprehensive policies and action in the housing and land management sector to be developed at the regional and global levels which should be directed towards a healthier real estate market. Additionally to be addressed is the need to look at the possible complementarities between increasing the financial stability of the real estate sector with attempts also to make this market more environmentally sustainable and more socially responsive to the need to provide adequate housing for all.