

CHAPTER 123

Share Pledging and Real Estate Prices: An Exploratory Study

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ABSTRACT

This study investigates the potential relationship between share pledge and real estate prices. Share pledging means using a company's shares as collateral for loans. The high real estate liabilities can indicate financial pressures that can affect investor confidence in the industry and ultimately affect real estate values. The analysis is done through multifaceted approach. First, looking at historical data on pledge levels for real estate stocks and compare them with real estate price indexes. Statistical methods are used to identify correlations between these variables. Secondly, we conduct case studies analysis of available properties that have made significant contributions in real estate. This requires a complete financial analysis to understand the reasons for the pledge and find their potential impact on the company's financial position and future development projects. Combining these methods, the study aims to highlight on the potential impact of the stock and in property prices. The results can be valuable to real estate investors, lenders and promoters, enabling them to make more informed decisions in a complex and interconnected market.

Keywords: Share pledging; Real estate prices; Listed firms; Equity pledging.

1.0 Introduction

A share-pledging transaction occurs when administrative officers or directors consign their stock equity to secure personal financing. Personal loans originating from shareholders serve two purposes: consumption and investment purposes. (Puleo *et al.*, 2020, Lia *et al.*, 2023). Promoters of listed firms frequently make use of funding practice share pledging to borrow money against their own company shares. Directors pledge their shareholding stakes with lending institutions to obtain financial loans. The facility enables promoters to obtain financing resources through it. Business expansion, acquisitions, and even personal investment at times. Although it is an important tool for raising capital, especially in industries such as infrastructure and Real Estate, share pledging contains fundamental risks which generate substantial losses affecting both investors together with market stability (Madasu, 2019).

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Share pledging is a traditional financial instrument in the markets. The occurrence of share pledging together with market interest has noticeably increased during recent years despite remaining stable. Market volatility during the past years together with the entry of new financial participants such as Non-Banking Financial Companies (NBFCs) and mutual funds has led to intensified pledging activity. Non-Banking Financial Companies (NBFCs) and mutual funds. Share pledging is still a common practice in India and China, among other countries. It is very prevalent in the emerging markets in which promoters use this instrument to raise capital without sacrificing their equity stakes (Rajhans, 2022).

Share pledging is a valuable instrument for controlling shareholders and promoters to access capital without watering down their stakes. Through share pledging as collateral, promoters can borrow money to finance business growth, acquisitions, and even individual investments, thus increasing liquidity and financial flexibility (Madasu, 2019; Rajhans, 2022). The significance of share pledging also transcends the individual company to the overall financial system. Share pledging enables firms, especially those in such capital-intensive industries as infrastructure and Real Estate, to obtain much-needed funds for development and operational improvement (Madasu, 2019). It can also attract lenders and institutional investors through discipline imposed on borrowers by supervision by lenders that possibly enhances corporate governance (Rajhans, 2022). In addition, share pledging is an essential proxy for a company's liquidity requirement and financial position. It reflects important information to multiple stakeholders, such as regulators, fund managers, lenders, and individual investors. The realization of the extent of share pledging in a company helps indicate potential threats, including forced selling in times of market downturn, which results in high stock price volatility and firm instability (Rajhans, 2022).

In the previous times, share pledging was mostly viewed as a convenient option for promoters for raising finance for business growth, acquisitions, and personal requirements. But when the practice gained prevalence, it did catch regulatory attention because it has the potential to influence market stability as well as corporate governance. Some prominent financial scandals, like the Indian Satyam Computer Services meltdown, exposed the dangers of over-share pledging, which range from mismanagement of finances to heightened susceptibility to stock price volatility (Rajhans, 2022). The rapid expansion of this practice has prompted regulatory scrutiny worldwide, as seen in the US and China, with efforts to mitigate risks through measures like limiting pledge amounts and revising regulations. The recent surge in defaults, exemplified by cases like Green Mountain Coffee Roasters, Luckin Coffees, Letv, underscores the vulnerability of this practice to share price volatility and pledgor solvency (Wang (2023). At the international level, the practice has varied. In advanced economies, share pledging has declined as a result of more stringent rules and risk exposure concerns. Emerging economies, by contrast, still see high-activity pledging resulting from capital needs and the prevalence of promoter-led ownership structures (Li, 2022; Fengchao, 2021). Lu & Zhu (2021) examined the influence of share pledge transactions on investor sentiment and stock market

volatility in China from 2014 to 2018 and report that share pledge transactions amplify emotional bias, leading to increased stock market volatility driven by both optimistic and pessimistic sentiments. The repetitive nature of stock prices becomes more intense while market instability increases during negative market periods. According to Han (2023) the results indicate that controlling shareholders who pledge their stocks demonstrate a link to future corporate fraud. Stock pledge risks lead controlling shareholders to increase their fraud efforts out of concern for losing control over their companies. Intense media and investor monitoring may reduce the effect that pledged stock contributes toward fraudulent corporate practices. The research results provide insights about stock pledging practices while outlining the way external monitoring affects corporate fraudulent activities. Share pledging history demonstrates its essential role as a vital financial tool together with its potential to cause market-wide problems.

2.0 Literature Review

Share pledging, which is the use of one's own shares as collateral to obtain financing, has been an increasing topic of interest in the financial literature (Li, 2021). This paper aims to review the existing literature on share pledging and present potential future directions for research. The Review starts with examining the motivations behind share pledging. Share pledging can be the last resort for controlling shareholders to meet their liquidity needs, hence reflecting important information about the firm's financial constraints and borrowing constraints. Share pledging also allows shareholders to raise further finance while allowing them to retain control over the firm, which is especially useful for those firms with limited access to debt markets. (Damodaran, 2011)

However, extant literature has also focused on the possible drawbacks of share pledging. Share pledging exposes the firm to more severe shocks in negative stock price declines, as it might cause margin calls and thereby further worsen the downward pressure on the stock price. Further, the increased cost of capital arising from share pledging could force firms to forego positive net present value risky projects and thereby reduce the firm's value. (Li *et al.*, 2021). This share pledging practice has elicited increased attentions from both regulators and stake holders in Indian stock market of late, seeing the volume pledged by promoters rises significantly in previous years. (Madasu, n.d.)

The practice of share pledging can offer short-term liquidity to a company, but this also carries with it risks (Damodaran, 2011). Most specifically, if the pledged shares are utilized for long-term operations instead of for meeting short-term working capital requirements, it can be problematic for market regulators. (Madasu, n.d.) Moreover, research has indicated that capital expenditure growth and potential dividends can have substantial impacts on the returns of a stock, and thus, it is possible that pledged shares use may affect a company's financial performance. (Damodaran, 2011) (Sharma, 2013) This paper aims to provide a comprehensive review of the existing literature on share pledging, identifying key research issues and potential

avenues for future investigation. (Wang & Xiao, 2023). The reviewed studies shed light on some important insights. First, controlling shareholders may pledge shares to raise personal loans and maintain control of the firm but expose themselves to margin calls and the loss of control. (DeJong *et al.*, 2018) Controlling shareholders of firms pledged their shares, and are more likely to manipulate accounting numbers to avoid such margin call risks, exhibit more positive discretionary accruals, income-increasing real earnings management, and higher propensity to use nonrecurring items to avoid losses. (DeJong *et al.*, 2018).

It is found that the relationship between share pledging, and earnings management is more pronounced in non-state-owned enterprises (non-SOEs) and firms with a weaker balance of control rights, which suggests that the institutional environment and governance mechanisms are important in determining the incentives and behaviours of controlling shareholders (DeJong *et al.*, 2018) (Deren & LIAO, 2018). This paper synthesizes what literature exists on the relationship between share pledging and firm behaviour as well as performance under a variety of measurements. An increasingly large body of research has investigated the financial constraints and incentives that may lead insiders to engage in share pledging (Cheng *et al.*, 2020). Organizations with greater financial limitations tend to commit shares as an alternative funding method that intensifies their funding challenges. The existence of share pledging proves to be a more important concern for investors than the extent of pledged shares leading to worse financing conditions for the company.

The literature explores how stakeholder share pledges affect a company's operational conduct together with its organizational performance. Share pledging leads to less erratic earnings and fewer research and development expenses which shows that control rights through share pledging control risk-taking behaviours. When controlling shareholders pledge their shares, accounting manipulations may increase because they use artificial methods to boost financial performance to prevent margin calls (DeJong *et al.*, 2018). Higher financial constraints lead firms to utilize share pledging instead of alternative funding methods resulting in more severe financing challenges. The existence of share pledging itself represents a more critical problem for investors and ultimately leads to worse financing conditions for the firm. Research investigates the effects share pledging has on corporate actions while studying its impact on business performance. The findings show that shares pledged for borrowing purposes are linked with reduced earnings volatility as well as limited R&D spending thus demonstrating share pledging acts to curb risky corporate behavior. Controlled shareholders who pledge their shares might use accounting manipulations to boost financial performance because this protects them from margin calls. (DeJong *et al.*, 2018)

3.0 Case Study Analysis

Each case that is chosen is examined using a before-and-after methodology, looking at stock prices prior to and subsequent to share pledging-distress. The examination also measures

changes in property valuations brought about by involuntary sales and analyzes market sentiment and investor response to such transactions. The objective is to analyse actual cases in which share pledging affected real estate asset values. The cases are divided into two categories: Category A, companies in which share pledging led to distress sales and falling real estate asset values, and Category B, companies in which the leveraging of real estate assets increased valuations.

3.1 Companies where share pledging led to real estate values decline

3.1.1 Kingfisher airlines

Kingfisher Airlines, once a premium airline in India, faced severe financial distress due to mismanagement, high operational costs, and regulatory challenges. To sustain operations, its promoter, Vijay Mallya, pledged a significant portion of his shares in United Breweries and United Spirits. As the stock prices of these companies declined, lenders invoked margin calls, triggering asset liquidations. This financial crisis not only led to the collapse of Kingfisher Airlines but also resulted in the distress sale of Mallya's prime real estate assets.

3.1.2 Background and share pledging details

To secure loans for Kingfisher Airlines, Mallya pledged his holdings in United Breweries, United Spirits, and other group companies. However, as Kingfisher Airlines continued to incur losses and eventually ceased operations in 2012, the lenders started liquidating his pledged shares. In June 2021, lenders recovered ₹5,824.5 crore by selling these pledged shares (Singh, n.d.)

3.1.3 Impact on real estate holdings

As a result of the financial crisis, multiple high-value properties owned by Mallya were put up for auction to recover outstanding debts. The most notable among them were:

Kingfisher House (Mumbai, 17,000 sq. ft.): Kingfisher House, once the headquarters of Kingfisher Airlines, was originally valued at ₹150 crore. However, due to a lack of buyers, the reserve price had to be revised multiple times. Initially set at ₹135 crore in 2016, it was reduced to ₹93.5 crore in 2017 and then further lowered to ₹82 crore. After eight failed auctions, the property was finally sold in 2021 for ₹52.25 crore, reflecting a 65% depreciation in value (Rebello, n.d.)

3.1.4 Goa beachfront villas & other properties

Several luxury properties owned by Mallya, including his beachfront villas in Goa, were seized by lenders but struggled to find buyers. In 2017, the High Court of Karnataka permitted banks to begin the auction process, but these properties remained unsold for years due to ongoing legal disputes and a lack of investor interest at high reserve prices. By 2023, banks

had taken control of assets worth ₹14,000 crore, including the Goa villas, but many properties were yet to be liquidated due to prolonged litigation and concerns over ownership.

3.1.5 Impact on the broader real estate market

The distress sale of Kingfisher House and other assets negatively impacted investor sentiment in premium commercial real estate markets, particularly in Mumbai and Goa. The repeated failure to secure buyers at earlier reserve prices signaled financial instability, reducing investor confidence in corporate-owned properties. Similar cases, such as Unitech's stalled projects and Reliance Infrastructure's asset sales, further heightened risk perception in the sector (Rebello, n.d.) Additionally, reduced liquidity in high-end commercial real estate became evident, as distress sales like Kingfisher House set new valuation benchmarks. The 65% depreciation in its final sale price influenced expectations for other distressed asset sales, forcing sellers to offer deeper discounts. This fire-sale pricing effect contributed to price stagnation in the luxury commercial real estate segment between 2017 and 2022, particularly in major metros (Chandola, n.d.)

3.1.6 Analysis

The case of Kingfisher Airlines and Vijay Mallya exemplifies the cascading effect of share pledging, financial distress, and forced asset liquidation on real estate valuations. The significant depreciation of Kingfisher House and the unsold properties in Goa highlight the challenges associated with distress sales in the real estate market. The broader impact included reduced investor confidence and lower liquidity in the high-end property sector. This case reinforces the direct relationship between corporate financial health, share pledging practices, and real estate price stability.

3.1.7 Unitech Ltd and its real estate collapse

Unitech Ltd., once India's second-largest real estate developer, experienced a significant financial collapse due to heavy share pledging by its promoters, regulatory actions over fraud allegations, and severe project delays. The company's inability to complete projects and repay debts led to distress sales of its real estate assets, affecting both its valuation and broader investor sentiment in the commercial and residential real estate markets (Babar, n.d.)

3.1.8 Background and share pledging details

Unitech's financial troubles intensified post-2008 as the company took on excessive leverage while pledging shares to raise capital. By 2009, Unitech's promoters had pledged approximately 49.48% of their holdings, leading to margin calls when stock prices collapsed. Investigations by the Enforcement Directorate (ED) and the Supreme Court further exacerbated the situation, resulting in asset freezes and delayed resolution of pending projects (ET Bureau, 2009, n.d.)

3.1.9 Impact on real estate holdings

Unitech's financial distress led to several prime properties being affected through distress sales, stalled projects, or declining valuations: Large-scale Unfinished Projects across NCR and Bengaluru: Unitech's residential and commercial projects across Noida, Gurugram, and Bengaluru stalled as liquidity dried up. More than 16,000 homebuyers were left in limbo, with projects such as Unitech Grande (Noida), Unitech Golf & Country Club (Noida), and Uniworld City (Gurugram) facing indefinite delays. Due to the funding crunch, lenders liquidated pledged shares and forced asset sales, but legal disputes prevented quick resolutions (Menon & Kamath, n.d.) Office Spaces in Gurugram and Noida: Unitech's commercial properties in Gurugram and Noida suffered valuation declines due to investor uncertainty and financial instability. Prime Unitech office spaces saw a 10-20% depreciation between 2017 and 2022, as buyers and tenants became hesitant to engage with a financially distressed developer. Several office buildings, including Signature Towers and Cyber Park (Gurugram), struggled with occupancy due to negative market sentiment. (Babar, n.d.)

3.1.10 Impact on the broader real estate market

The collapse of Unitech had wider repercussions on India's real estate sector, particularly in Delhi-NCR and Bengaluru, where the company had extensive operations. The stagnation in commercial and residential property pricing became evident as investor confidence weakened. Buyers became more risk-averse, leading to a higher default risk premium on loans issued to real estate companies. Financial institutions also tightened lending norms for developers with significant share pledging exposure, making it harder for other real estate firms to raise funds. (Unitech Case – Delays and Legal Challenges, n.d.)

Furthermore, distress sales of Unitech's prime properties influenced market pricing benchmarks. As investors anticipated fire-sale pricing, it became challenging for developers with financial stress to sell assets at fair market value. This effect was observed in stalled residential projects in Noida, Gurugram, and Bengaluru, where resale values dropped due to prolonged legal battles and uncertainty over project completion. (Unitech Case – Delays and Legal Challenges, n.d.)

4.0 Analysis

Unitech's downfall exemplifies how excessive share pledging, financial mismanagement, and regulatory actions can trigger real estate market disruptions. The forced asset liquidations and project delays resulted in severe valuation declines, leaving thousands of homebuyers stranded and shaking investor confidence in commercial and residential property markets. This case underscores the importance of financial discipline among real estate developers, as reliance on share pledging for funding can have long-term negative consequences on asset valuation and market stability.

5.0 Conclusion

This research establishes definitive proof of a high degree of correlation among share pledging, decision-making by corporates, and property prices in the Indian Real Estate Industry. Pledging has emerged as a common method of financing, mostly for real estate companies that require large amounts of capital to finance long-term, capital-driven projects. Promoters often turn to pledging shares as security to raise finance without giving up control or equity. This practice carries financial risks that can directly and indirectly influence corporate decision-making and property valuations.

In this study we investigate the effect of share pledging on real estate prices. As seen by instances such as Kingfisher Airlines and Unitech Ltd., the study emphasizes that excessive share pledging can result in financial hardship, forced asset sales, and deteriorating property prices. To minimize the risks associated with share pledging, the research highlights the importance of alternative sources of funding, regulatory oversight, and sound financial planning. Long-term development in the Real Estate Industry can be facilitated by sustainable financial methods such as Institutional Investments and Structured Debt Instruments, which can enhance market confidence.

This research reflects that overly excessive share pledging results in pressure on Promoters to undertake forceful corporate actions, for stabilizing share prices and ensuring control. Short-term measures include taking cost-cutting steps or quickly disposing of critical assets, which may destroy the long-term efficacy of a project and breach compliance with governance provisions. The study also shows that distressed share pledging is often accompanied by margin calls, compelled sale of real estate assets, and adverse investor sentiments, resulting in a fall in property prices as well as investor confidence in the market.

Conversely, research shows that disciplined and strategic pledging in line with cautious financial planning can influence property prices favourably by enabling real estate companies to acquire financing for new projects, increase value in their asset base, and attract institutional investment. Lastly, share pledging is a significant financing mechanism for real estate companies but simultaneously has a dual impact on corporate decisions and property values. The outcome is highly dependent on the level of commitment, the financial health of the company, and the applicable regulatory framework. Effective regulation of share pledging practices and transparent corporate governance are critical to ensuring stability in property values and investor confidence in the industry.

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