



# Understanding REITs and InvITs

as an alternate investment  
opportunity



# Basics of real estate

- Huge ticket size
- Indivisible
- Self occupied / leased
- Rent gives regular returns
- Capital appreciation
- Illiquid investment with high transaction costs
- No index



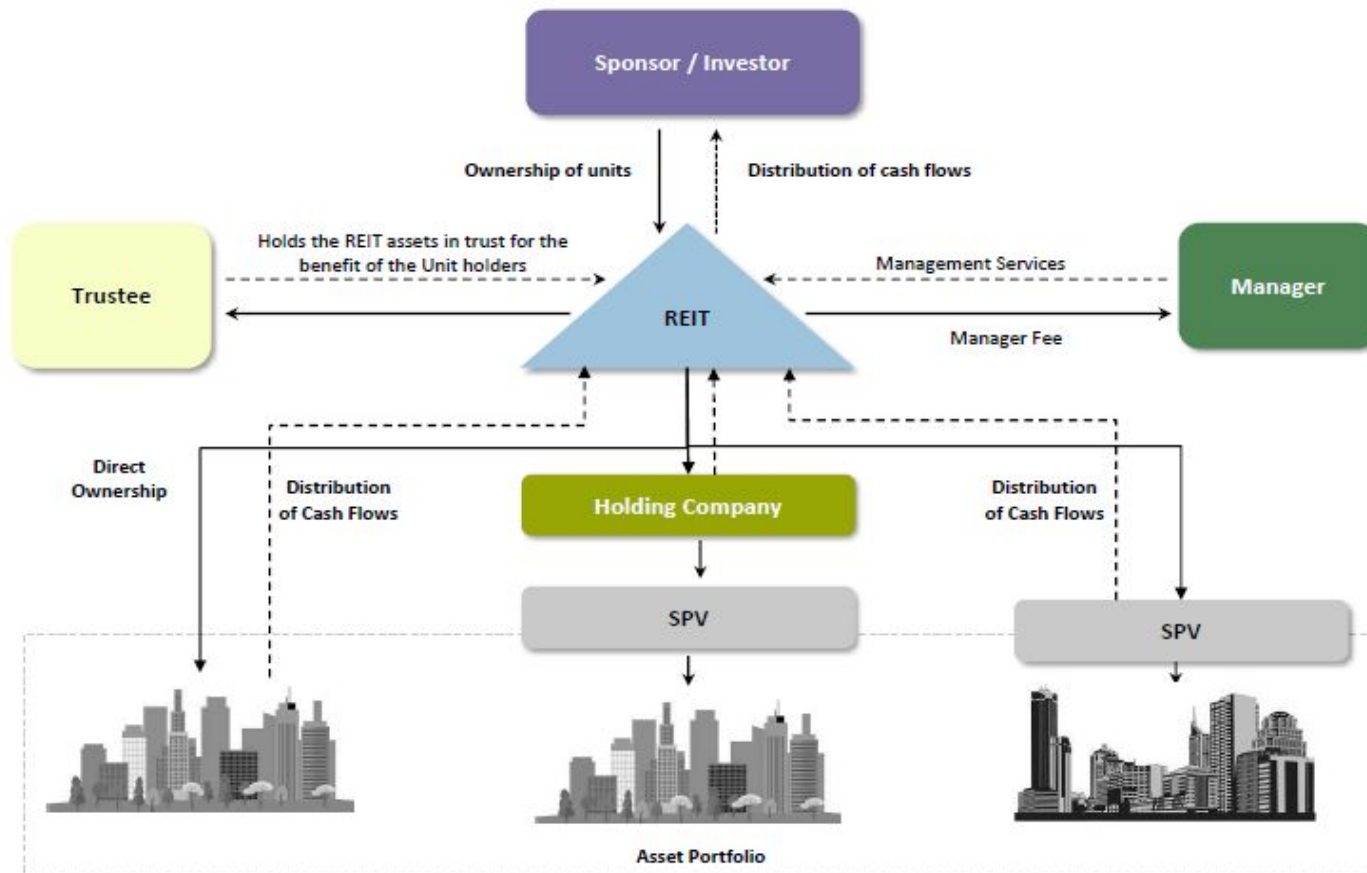
# What is a REIT?

- REIT stands for Real Estate Investment Trust
- Closed end structure but tradable
- More accessible
- Real estate experts make buy/sell decisions
- Can get exposure to malls/business towers
- Cannot invest in vacant land, agricultural land, mortgages other than mortgage backed securities or assets located outside India

# Types of REITs

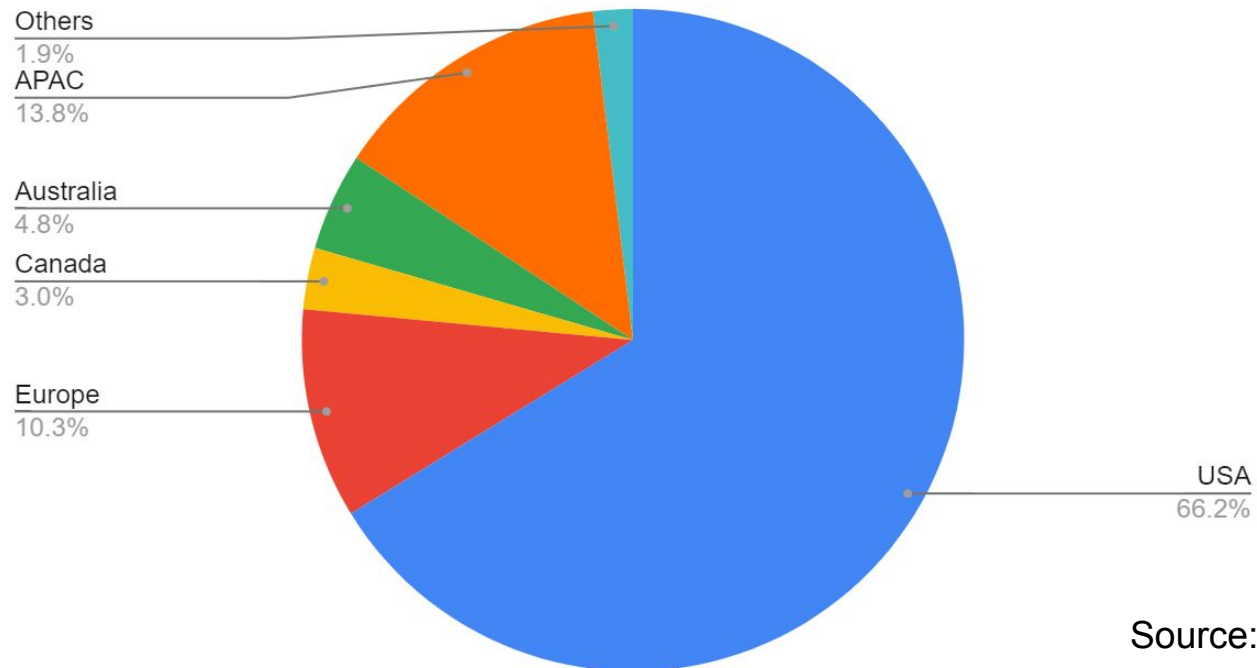
- Commercial REIT
- Residential REIT
- Industrial REIT
- Healthcare REIT
- Mortgage REIT

## REIT: Permissible Structure



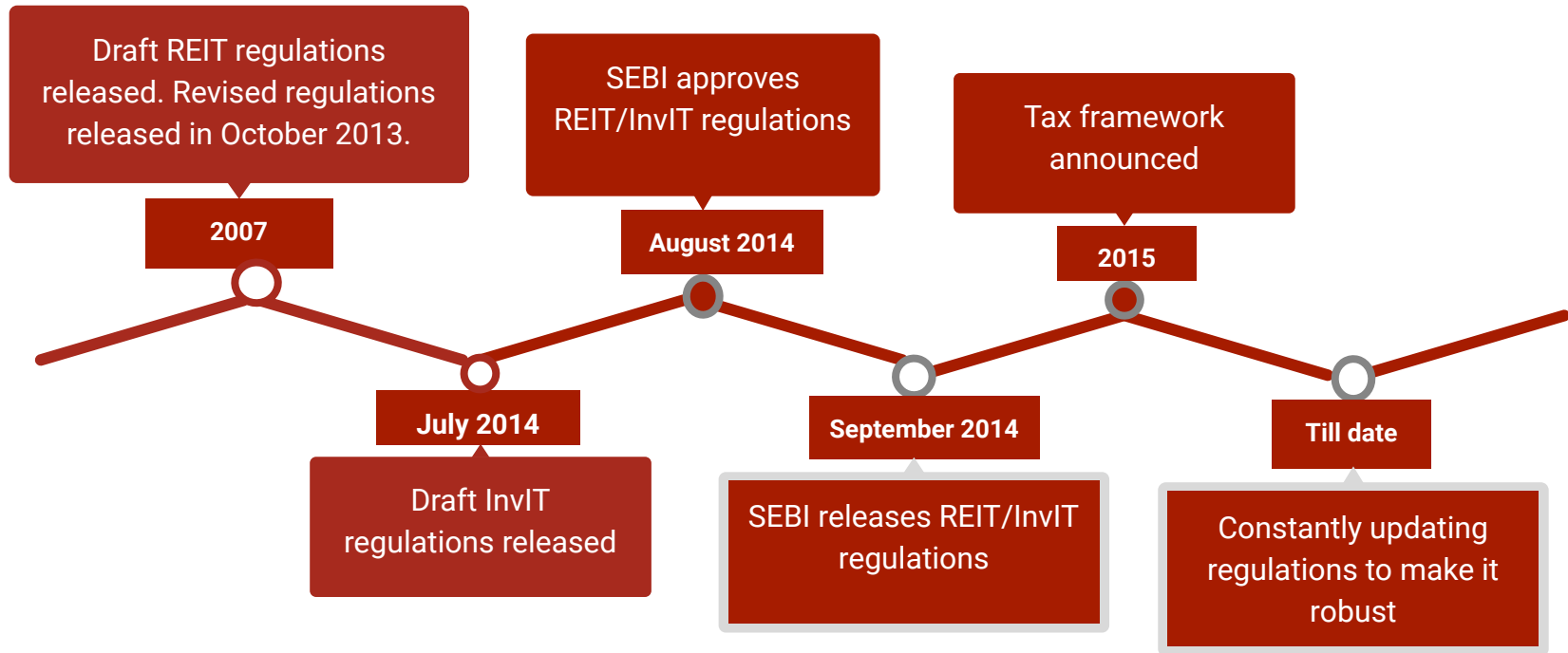
# REITs globally

REIT Market cap (Bn \$)



Source: Bloomberg

# Regulatory timelines in India





# Why now?

- Regulatory clarity
- Clarity around taxation
- Low spread over G-Sec led to the first listing only in 2019.
- Lower interest rates structurally in India
- Residential REITs are some time away

Investment characteristics	<ul style="list-style-type: none"> <li>• Minimum investment of Rs 50,000 with no cap</li> <li>• Freely transferable securities listed on stock exchange</li> <li>• Professionally managed</li> <li>• No entry/exit load</li> </ul>
Diversified portfolio	<ul style="list-style-type: none"> <li>• Grade A assets in prime locations across cities</li> <li>• Multiple tenants across sectors</li> </ul>
Return profile	<ul style="list-style-type: none"> <li>• Driven by regular income distribution and capital appreciation</li> </ul>
Tax treatment	<ul style="list-style-type: none"> <li>• Dividends are tax exempt</li> <li>• 10%-15% tax on sale of listed units (plus applicable surcharge and cess)</li> </ul>
Professionally managed	<ul style="list-style-type: none"> <li>• Experienced team</li> <li>• Good negotiation power with tenants</li> <li>• Ability to grow the portfolio</li> </ul>

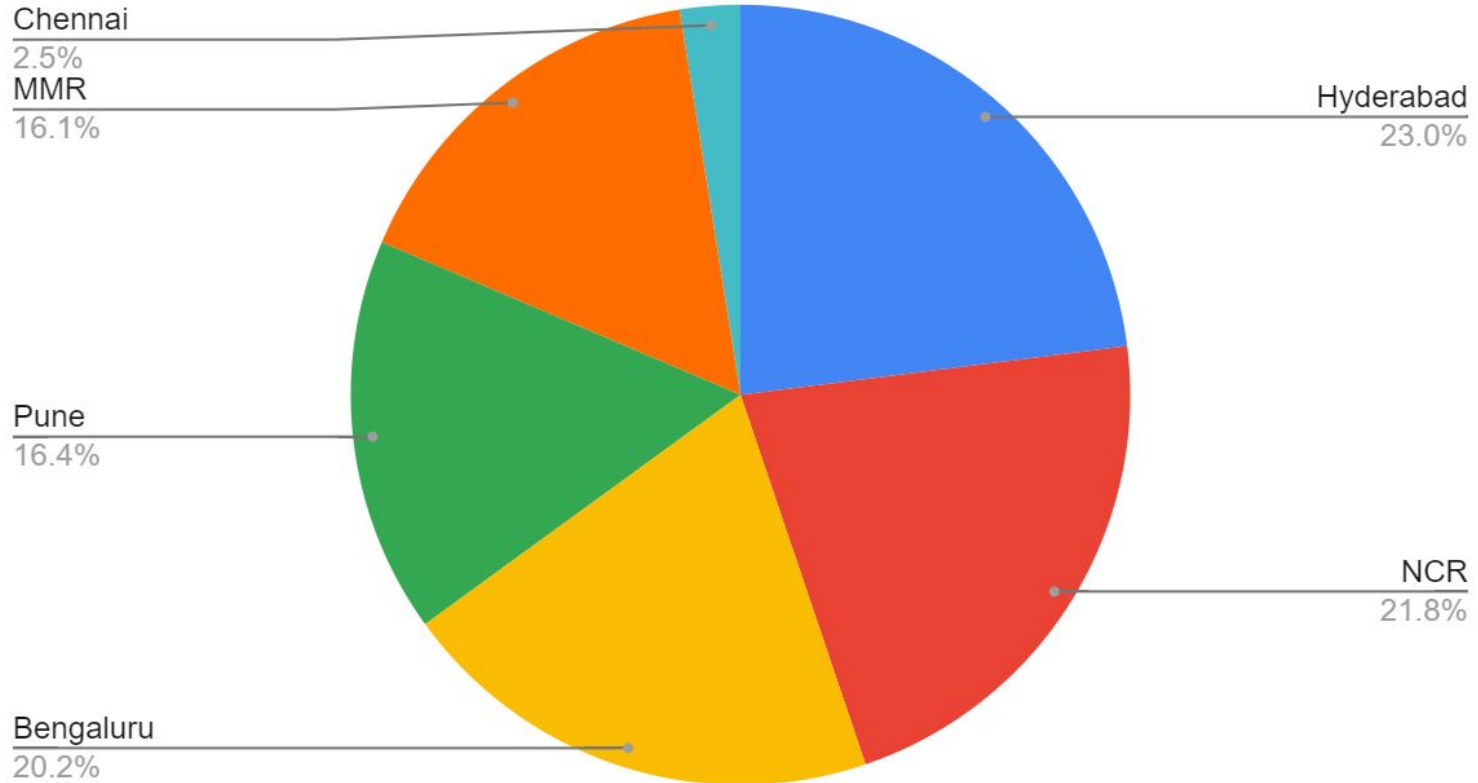
Asset	<ul style="list-style-type: none"> <li>• At least 80% of total value must be comprised of completed and income generating properties</li> <li>• Restrictions on speculative land acquisition</li> <li>• Minimum 90% of distributable cash flows to be distributed semi annually</li> </ul>
Debt	<ul style="list-style-type: none"> <li>• Majority unitholder approval required if debt exceeds 25% of asset value</li> <li>• Debt cannot exceed 49% of asset value</li> </ul>
Manager	<ul style="list-style-type: none"> <li>• 50% independent directors on the Board</li> <li>• REIT Manager can be removed with 60% approval of unrelated unitholders</li> <li>• Alignment with unitholder interests due to a performance linked management fees structure</li> </ul>
Related party transactions	<ul style="list-style-type: none"> <li>• Sponsors are prohibited from voting on certain related party transactions, subject to a threshold</li> <li>• Majority unitholder approval required for acquisition or disposal of asset which exceeds 10% of REIT value</li> <li>• Acquisition or sale price of new asset cannot deviate from average valuation of two independent valuers by +/- 10%</li> <li>• Fairness opinion from independent valuer required if related party leases exceed 20% of the total REIT area</li> </ul>

# Advantages from a Developer perspective

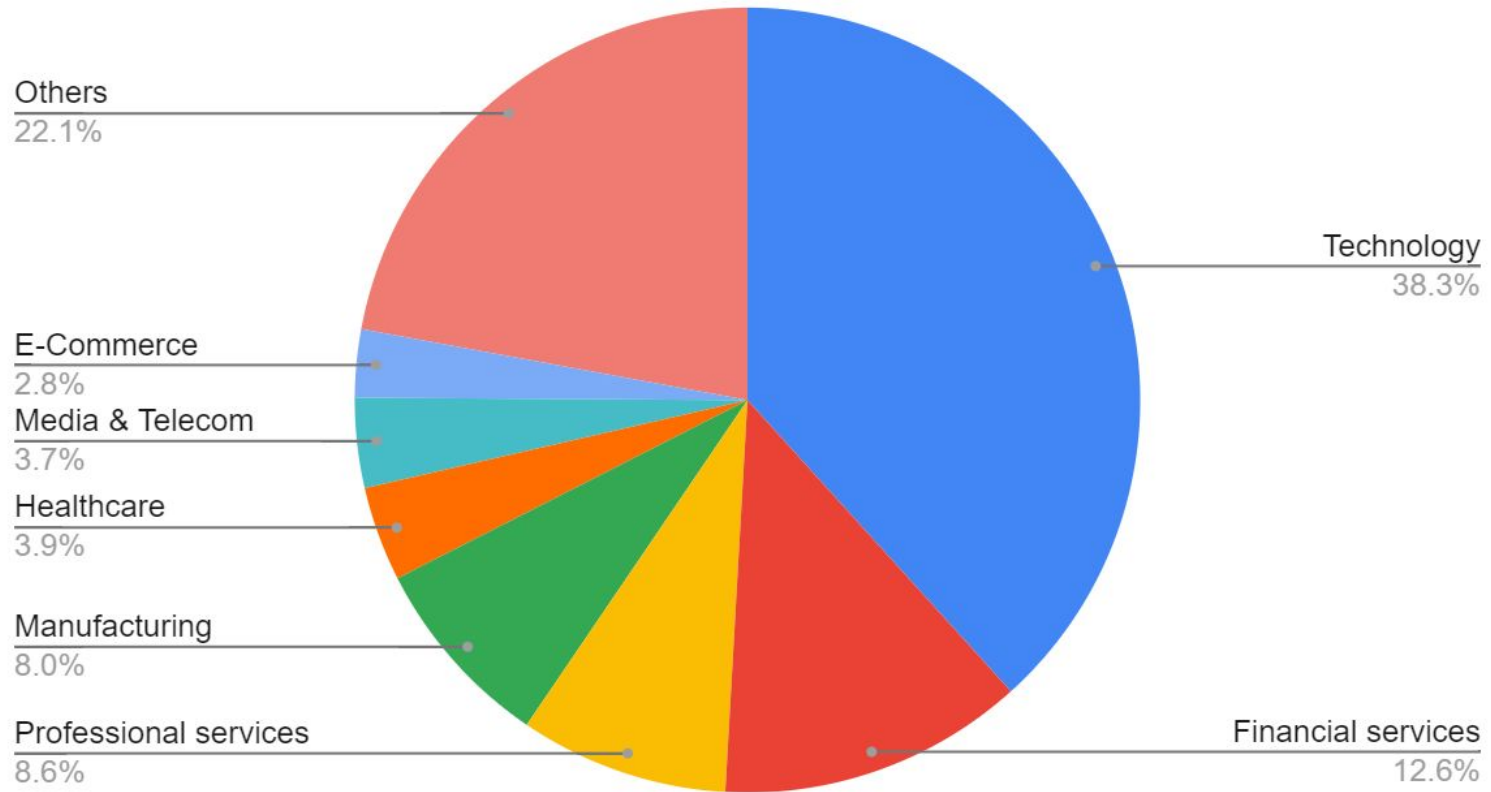
- Raise money
- Deleverage
- To increase market value
- Acquisitions
- Retain employees
- Provide liquidity to shareholders

# Real estate market in India

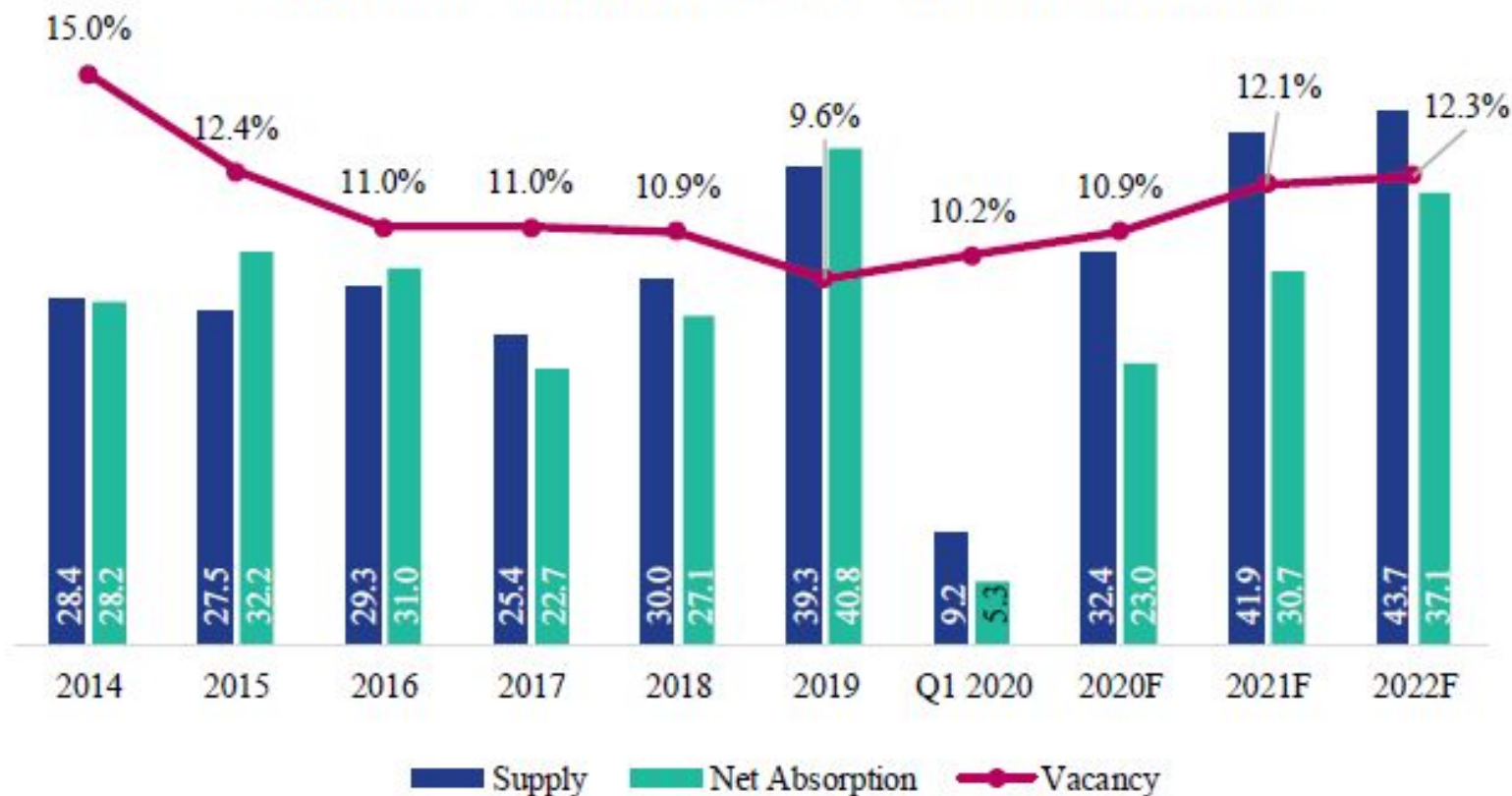
## Market share by net absorption (FY20)



## Market share by sectoral absorption (Top 6 cities)



## Supply, Net Absorption & Vacancy - Top Six Indian Markets



(Source: C&W Report)



## Current & Potential REIT listings

REIT	Stock (mn sq ft)	Markets
Embassy (listed)	26	Bengaluru, Mumbai
Mindspace (listed)	23	Hyderabad, Mumbai
Brookfield	22	NCR, Mumbai
DLF-GIC	30	NCR
Prestige Office	10	Bengaluru
Panchshil Realty	20	Pune
RMZ Corp	32	Bengaluru

	Embassy	Mindspace
<b>Asset Overview</b>		
Operating (mn sq ft)	26.2	23.0
Committed occupancy (%)	92.8%	92.0%
Under construction (mn sq ft)	2.6	2.8
Future development (mn sq ft)	4.5	3.6
Total (mn sq ft)	<b>33.3</b>	<b>29.4</b>
% of construction completed	90.4%	91.50%

	Embassy	Mindspace
Geography		
Bengaluru	55%	NA
Hyderabad	NA	38%
Mumbai	15%	39%
Pune	13%	18%
NCR	9%	NA
Chennai	NA	3%
Others	8%	2%

	Embassy	Mindspace
<b>Tenants quality</b>		
MNC	78.0%	84.9%
Top 10 tenants	42.0%	41.6%
<b>Sector</b>		
Technology	50.0%	44.4%
Financial Services	12.0%	22.0%
Healthcare	6.0%	6.5%
Others	32.0%	27.1%
<b>Shareholding</b>		
Blackstone	47.0%	10.0%
Permanent sponsor	15.0%	65.0%
Others	38.0%	20.0%

# Taxation

Dividend distributed by REIT	<p>Exempt u/s 10(23FD)*</p> <p>*Subject to the SPV not opting for a concessional tax rate u/s 115 BBA or else it is subject with withholding tax of 10%</p>
Interest distributed by REIT	<p>Taxable u/s 115 UA(3)</p> <p>→ Resident - applicable slab rate</p> <p>→ Non resident - 5%</p>
Capital gains & other income taxed in hands of REIT and distributed by REIT	<p>Exempt u/s 10(23FD)</p>
Capital Gains on sale of REIT units through stock exchange	<p>Taxable u/s 111A/112A</p> <p>LT CG (&gt;3 years) - 10% on gains &gt; Rs 1 lakh</p> <p>STCG - 15%</p>

# Valuation of a REIT

- NAV of a REIT is declared quarterly
- $\text{NAV} = \text{Market value of properties} - \text{debt of REIT}$
- Market price can be at a discount/premium to the NAV
- Akin to discounting rate in DCF of a company
- Net operating income is discounted by the cap rate for 10 years
- 11th year NOI is considered for terminal value

# Capitalisation rates

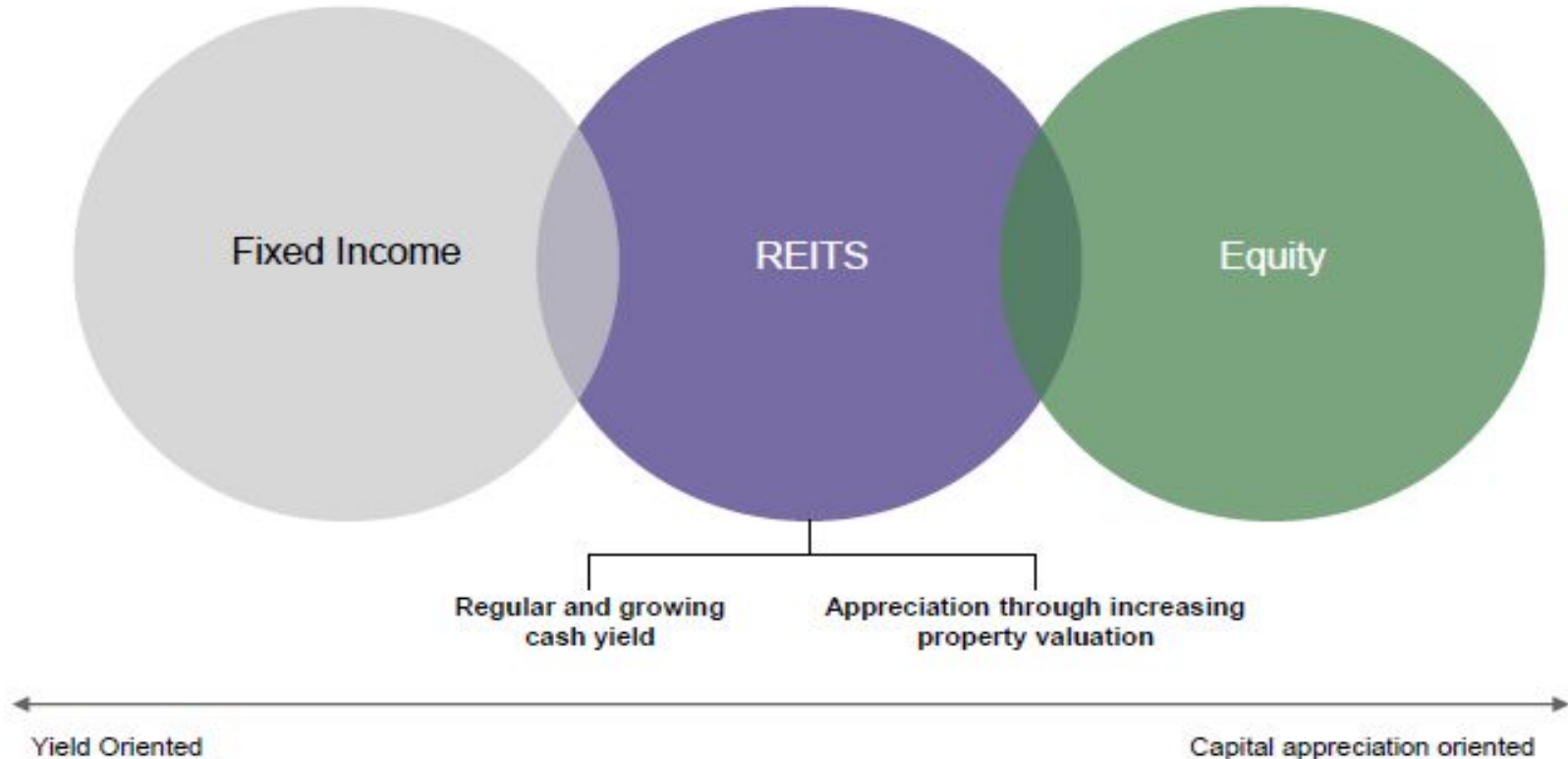
- Office cap rates in India are ~7.5-8%
- Cap rates are a function of interest rates and supply demand of office spaces
- Over the last decade, cap rates have steadily come down offering improved valuation to landlords
- Cap rates unlikely to go up in medium/long term; although near term uncertainty expected due to weak demand.

# Key metrics to track

- Weighted average lease expiry (WALE)
- Committed occupancy/vacancy rate
- Concentration of Top 10 tenants
- Sector and asset concentration



# Provides good diversification



# Provides good diversification

Source: NAREIT REITwatch, July 2020

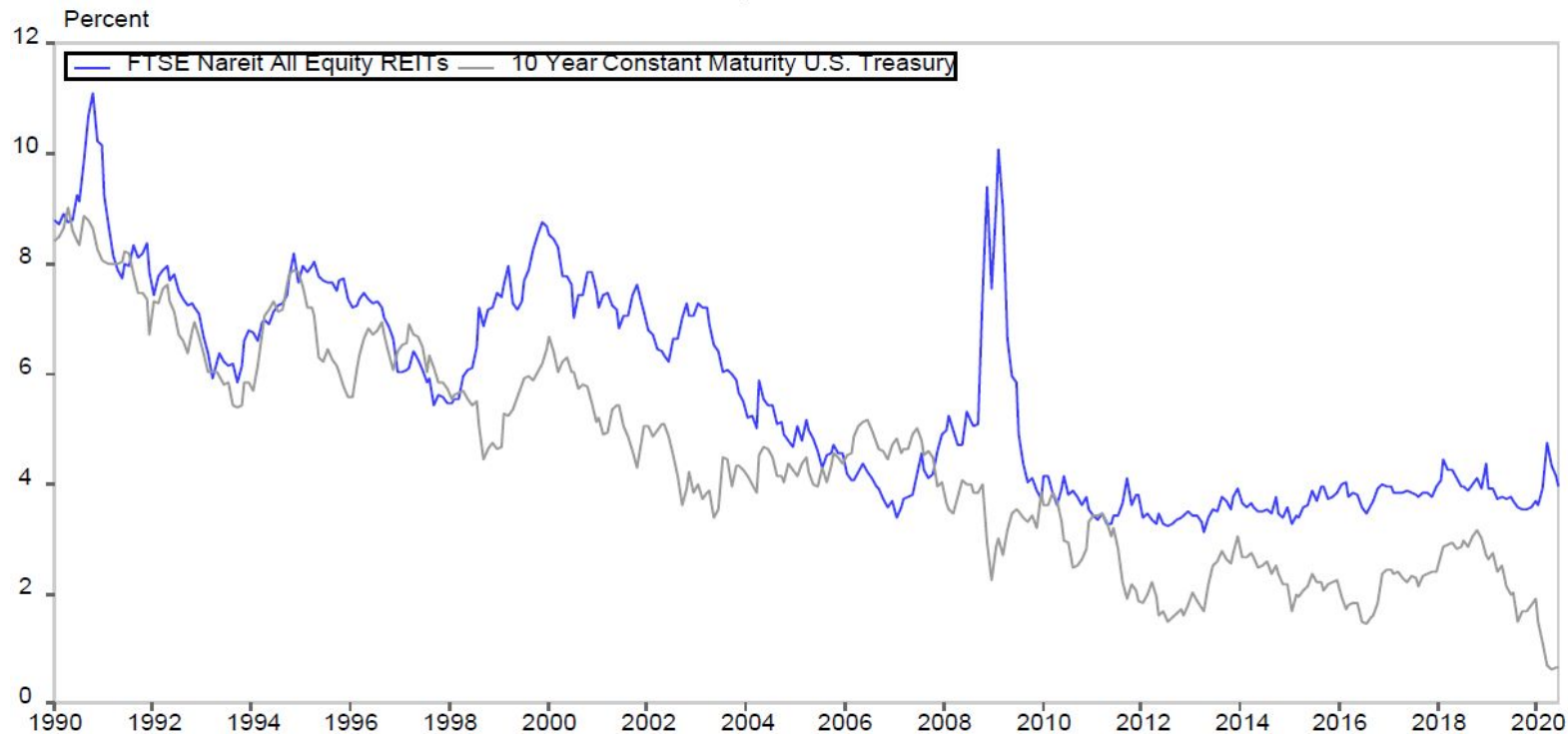
	<u>FTSE Nareit</u>		S&P 500	Russell 2000	Nasdaq Composite	Dow Jones
	All REITs	All Equity REITs				Industrial Average
2020: YTD	-15.01	-13.30	-3.08	-12.98	<b>12.67</b>	-8.43
1-Year	-8.36	-6.47	7.51	-6.63	<b>26.94</b>	-0.54
3-Year	2.65	3.51	10.73	2.01	<b>19.14</b>	9.08
5-Year	6.11	6.56	10.73	4.29	<b>16.36</b>	10.62
10-Year	10.05	10.39	13.99	10.50	<b>18.25</b>	12.99
15-Year	6.31	6.89	8.83	7.01	<b>11.16</b>	9.08
20-Year	9.74	<b>10.13</b>	5.91	6.69	4.76	7.18
25-Year	9.54	<b>10.02</b>	9.27	8.16	9.98	7.18
30-Year	9.87	10.40	9.74	8.93	<b>10.81</b>	7.58
35-Year	8.50	9.89	<b>10.79</b>	9.02	10.60	8.83
40-Year	10.01	11.38	<b>11.49</b>	10.22	10.95	8.85
1972 - 2020	9.30	<b>11.37</b>	10.48	-	8.93	7.19

# Provides good diversification

Source: NAREIT REITwatch, July 2020

## REIT Dividend Yield vs. 10-Year Constant Maturity Treasury Yield

January 1990 - June 2020



Source: Nareit®, FactSet.

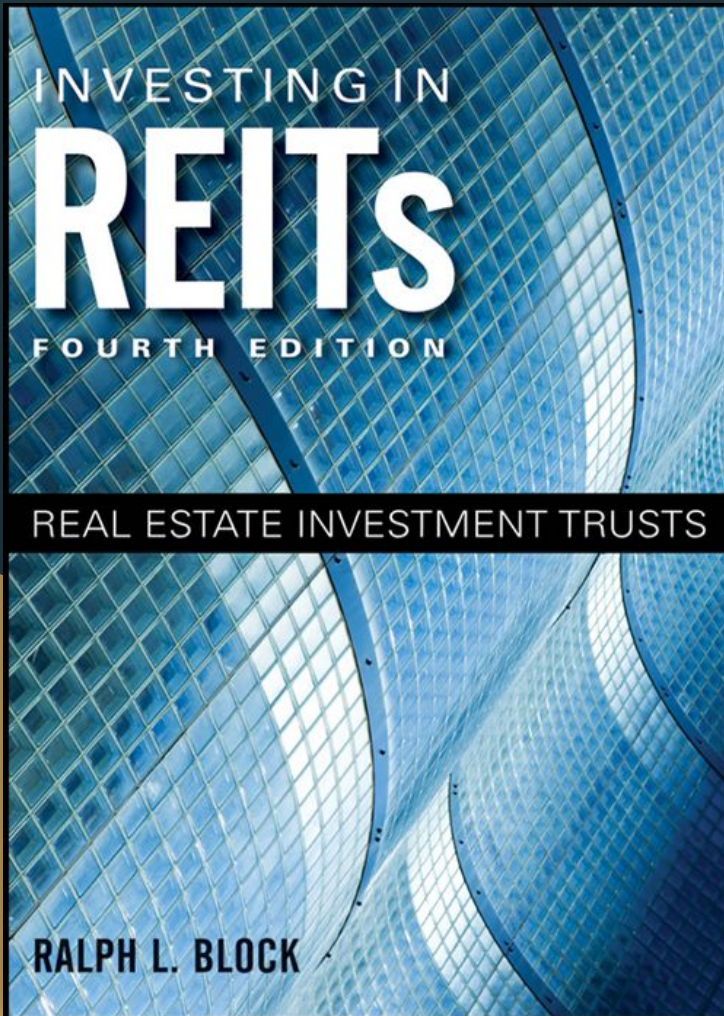
# Provides good diversification

Source: NAREIT REITwatch, Jan 2010

## Comparative Total Return Investment Correlation

	FTSE NAREIT Equity	S&P 500	NASDAQ Composite	S&P Utilities	Dow Jones Industrials	ML Corp/Govt Bond Index
FTSE NAREIT Equity	1.00	0.66	0.53	0.38	0.61	0.10
S&P 500		1.00	0.91	0.56	0.96	-0.10
NASDAQ Composite			1.00	0.40	0.83	-0.17
S&P Utilities				1.00	0.55	0.14
Dow Jones Industrials					1.00	-0.12
ML Corp/Govt Bond Index						1.00

December 2000 through December 2010



<https://www.reit.com/>



**EMBASSY OFFICE PARKS**

# Risks

- Slowdown in demand for commercial space
- Oversupply
- Changing trends/location preferences
- Work from home trend picking up leading to more vacancies
- Renegotiation of existing contracts at lower rates
- Interest rate cycle





**Uday Kotak** 

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Tech hub San Francisco reports a 96% increase in empty homes - Higher cost of living, taxes and virus risk. Remote work allows productivity without these downsides.

Cities need to be competitive and cannot take success for granted. This applies to cities in India too.

12:26 · 17 Aug 20 · [Twitter for iPhone](#)

# Track record - Embassy

- Issue price - Rs 300
- Listing date - April 01,2019
- CMP - Rs 360
- Dividend - Rs 24.39 per unit for FY 20
- XIRR - 13.82%



InvITs

# What is a InvIT?

- InvIT stands for Infrastructure Investment Trust
- Modified version of REIT
- Complicated
- Each InvIT will be unique
- Very contrasting returns

# Sectors covered for InvIT

- Transport and logistics - roads, bridges, ports, airports, inland waterways, logistics infra etc
- Energy - electricity generation/transmission/distribution, gas and oil storage facility
- Water and sanitation - solid waste management, water treatment plants, irrigation
- Communication - Telecommunications fixed network, towers and services
- Social and commercial infra - affordable housing, educational institutions, sports infra, hospitals, hotels, storage for horticulture/agri produce etc

# Categories of InvIT's

## 1. Publicly offered InvIT's

Will hold > 80% in completed and revenue generating projects

Minimum 20 investors

Listing mandatory in India

## 2. Privately placed InvIT's

Will hold >80% in **Eligible infrastructure projects**

Min 5 and max 1000 investors

Listing mandatory in India

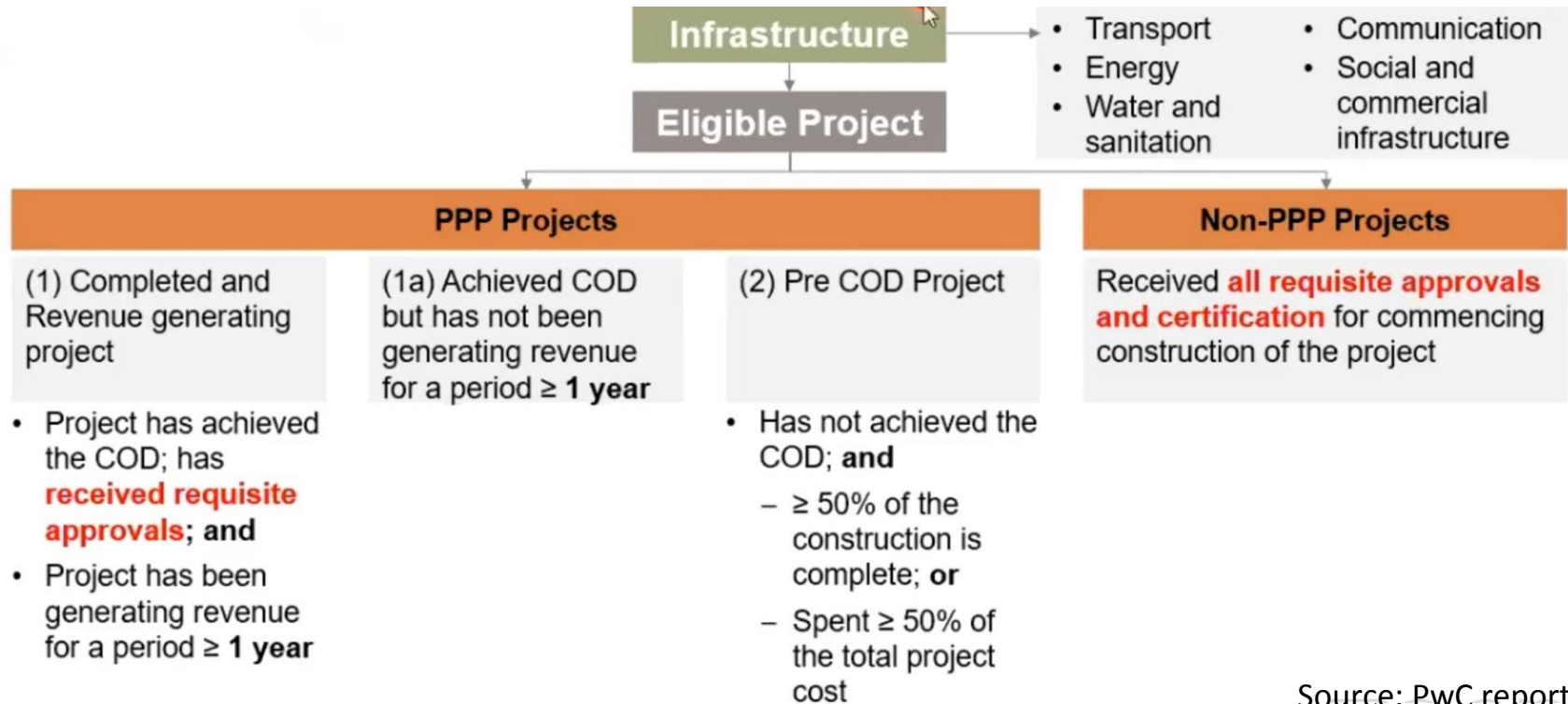
## 3. Privately placed unlisted InvIT's

Will hold >80% in **Eligible infrastructure projects**

Max 20 investors

Listing not mandatory

# Eligible infrastructure projects



# Current & Potential InvIT listings

Name	Parties	Type	Asset	Offer document	Listing status
India Grid Trust	Sterlite	Public	Power transmission	Final offer doc filed	Listed
IRB InvIT Trust	IRB Infra	Public	Road assets	Final offer doc filed	Listed
India Infrastructure Trust	Brookfield - Reliance	Private	Gas pipeline	Final placement memo	Listed
Indinfravit Trust	L&T and IDPL	Private	Road assets	Final placement memo	Listed
Oriental Infra Trust	Oriental Tollways	Private	Road assets	Final placement memo	Listed
Reliance Infra InvIT Trust	Reliance Infra	Public	Road assets	Draft offer doc filed	NO
IRB Infra Trust	GIC-IRB Infra	Private	Road assets	Draft placement memo filed	NO
Tower Infra Trust	Brookfield - Reliance	Private	Towers assets	Draft placement memo filed	NO

# India Grid Trust (IndiGrid)

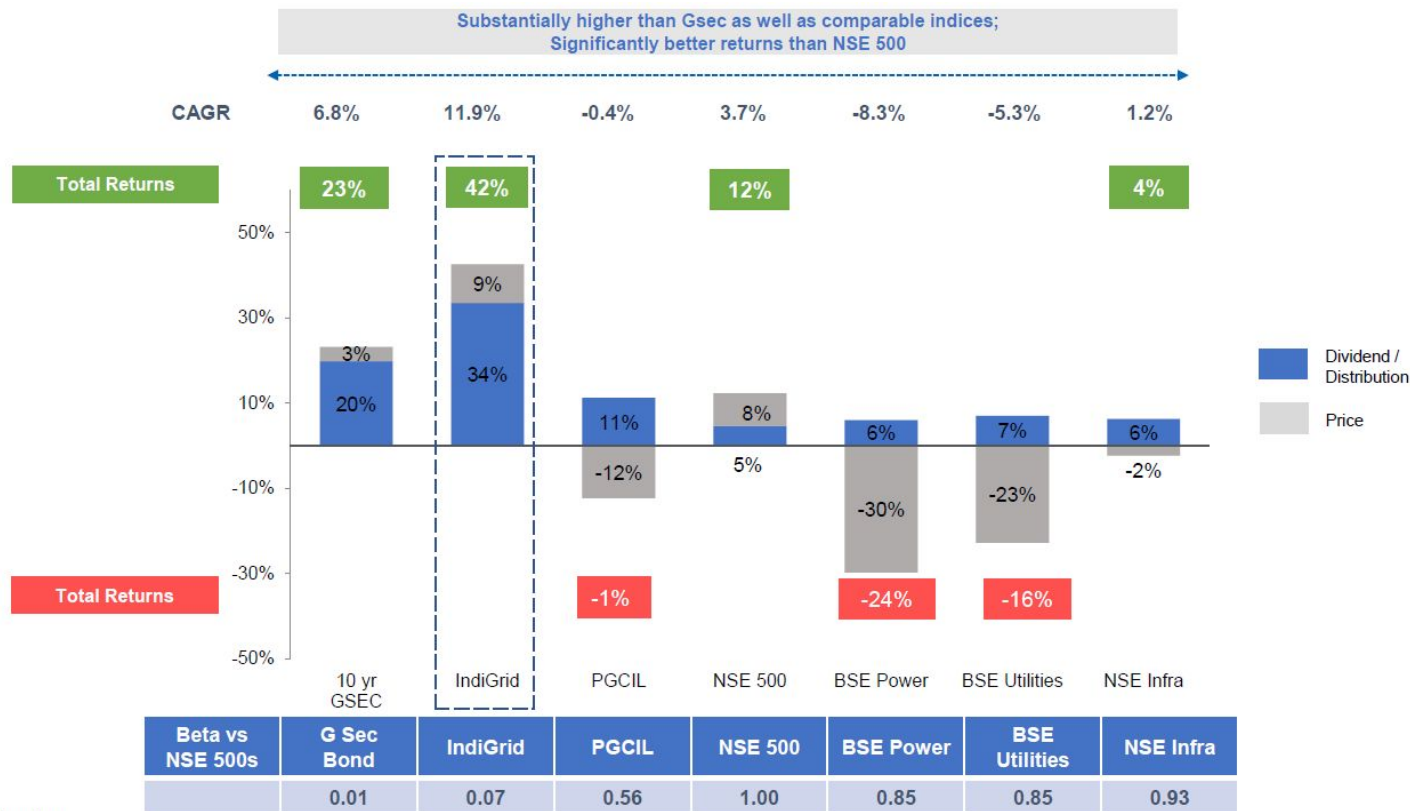
- Owns inter state power transmission assets in India
- Established in October 2016
- Sponsor - Sterlite Power Grid Ventures (SPGV)
- Currently owns 6 operational assets and 7 others that can be bought from the sponsor on Right of First offer
- Trading at 11-13% IRR

# Issues at the sponsor level

- May 2019 - preferential allotment to KKR & GIC for 42% stake at INR 83.89 per unit
- KKR planned to buy another 15% at the same price from SPGV
- Conflict of interest - Sterlite was the sponsor as well as controlled the investment arm
- KKR bought 60% in the investment arm and continues to hold it



# Track record - IndiGrid



Source: Bloomberg

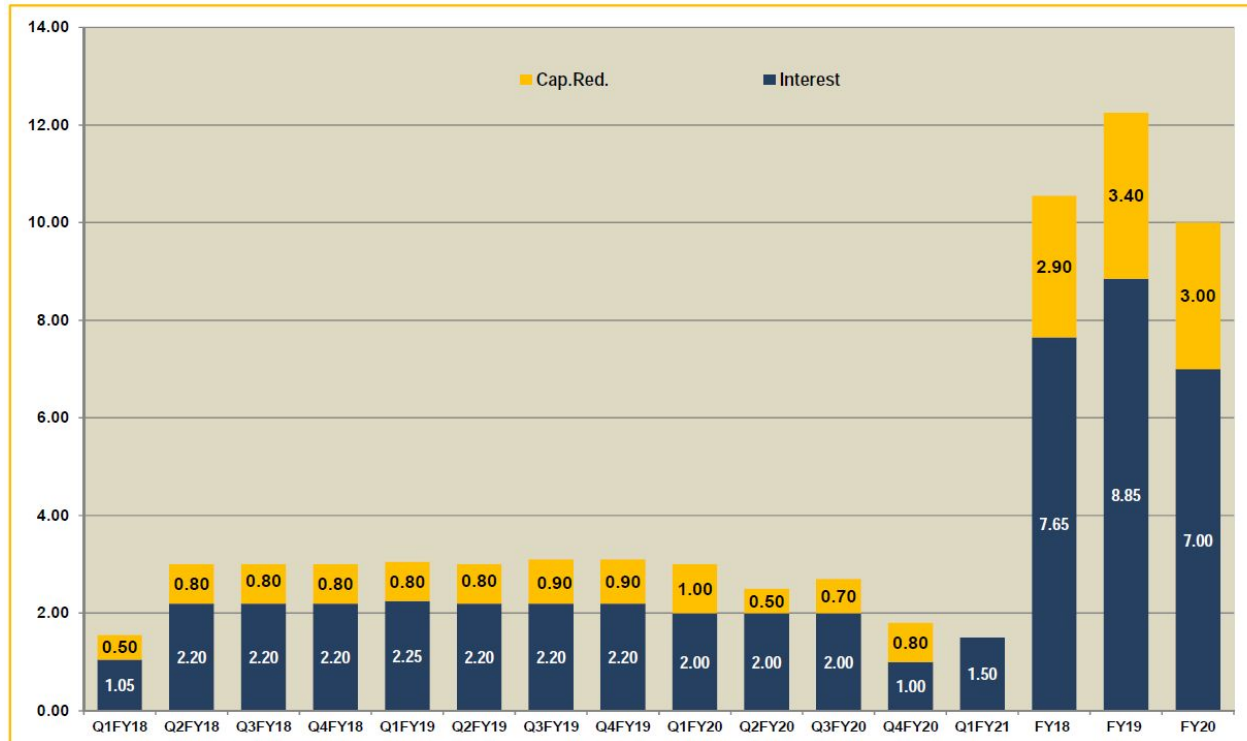
Note: Total Return chart is since listing of IndiGrid till July 31, 2020

# IRB InvIT

- Own 7 toll road assets
- Toll collections are not predictable and can change drastically
- Cannot rely on management estimates
- Evaluate each asset separately
- Listed in May 2017

# Track Record - IRB InvIT

## Distribution till date



# Track record - IRB InvIT

- Issue price - Rs 100-102
- Listing date - May 2019
- CMP - Rs 38
- Dividend - Rs 10 per unit for FY 20
- Indicative IRR - 12-12.75% on original issue price

# Conclusion

- REITs are easier to understand than InvITs
- Diversify through a portfolio of REITs
- Spread over G-sec yields
- InvITs may have some sector specific or asset specific issues
- Regulatory updates
- At par with global standards for REIT/InvIT regulations

