

# **Alternative Investments – Introduction To Real Estate Investments**

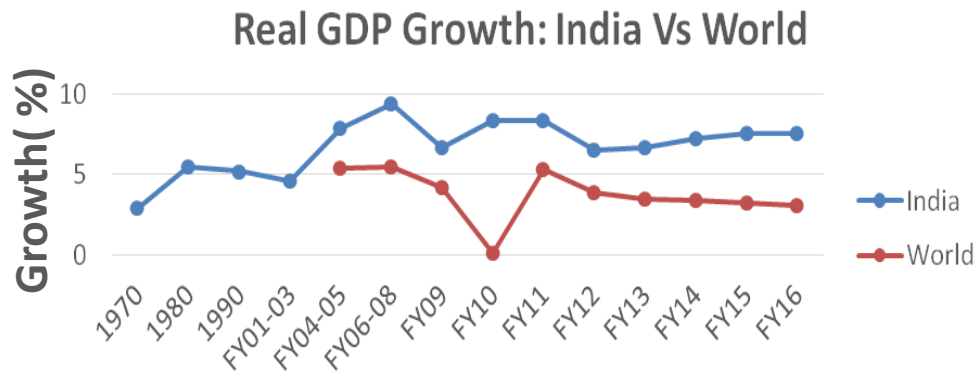
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# India: Growth Engine of the World Economy

- India is the Seventh largest country in the world in terms of GDP and third largest in terms of PPP. (Source : IMF)
- India's real GDP has increased at a CAGR of ~7% during last 5 year (vis-a-vis world GDP growth rate of 3.5%)
- The growth was primarily driven by **service sectors** (~45.4% in FY 16) which is expected to continue to outpace the rest of global economy
- Manufacturing has once again reflected signs of growth due to emergence of Make In India initiative; 7 - 8% economic growth is expected

## 'Make in India' Initiative

- The 'Make In India Initiative' has sharply increased the investment commitment and FDI flow in manufacturing sector
- New labor laws include a "single-window" labor compliance process for companies, simpler Provident Fund procedures
- Skill India initiative to help the development of manufacturing - will train over 500 million young people by 2020 to make them more employable



## Real Estate riding the growth wave

- Indian banks announced sharp cuts to their lending rates raising hopes that lower borrowing costs will help spark credit growth
- Prime Minister announced measures including an interest subsidy of up to 4% on loans taken under the Pradhan Mantri Awaas Yojana
- Real Estate sector expected to grow at a CAGR of ~15% till 2028

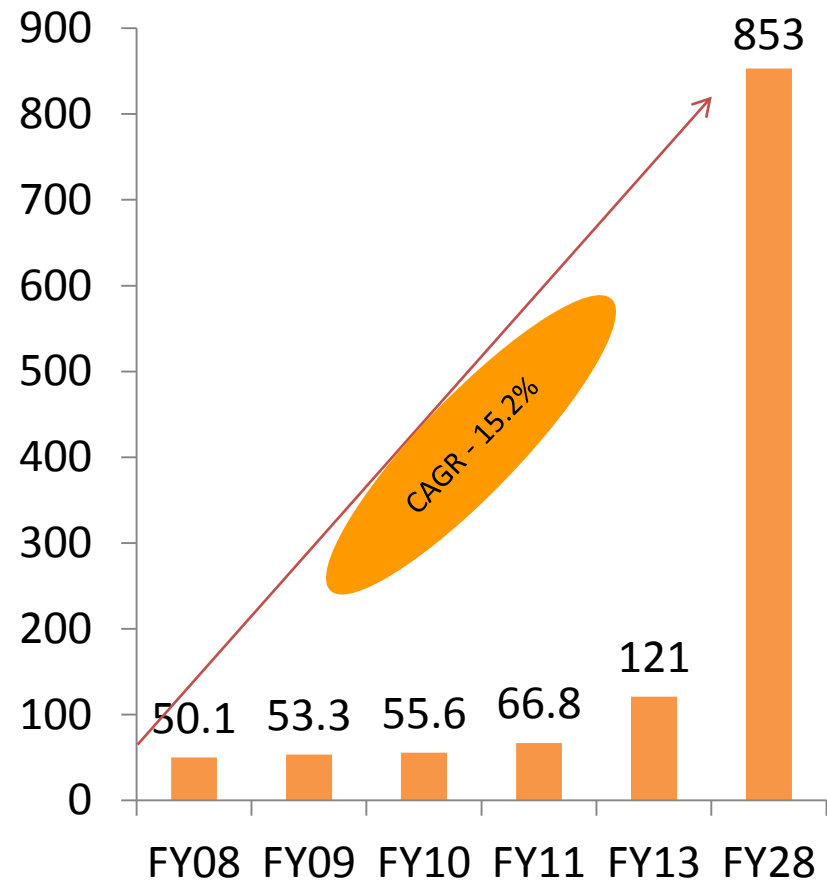
Land area	2,973,193 sq kms
Population	1.3 billion
Urban Population	c. 440 mn (32.8% of population)
GDP (total)	\$ 2.6 trillion
GDP (per capita)	\$ 1760

# Indian Real Estate Overview



- Real estate sector is one of the major pillar of Indian Economy with contribution of ~6.8% to the GDP. (Source : Census of India, 2011).
- The sector is the second largest provider of employment post agriculture and support 250 ancillary industries (Source : KPMG)
- The sector is the forth largest in terms of Foreign Direct Investment (FDI) inflows (Source : DIPP)
- The market size of real estate in India is expected to increase at a CAGR of 15.2 per cent during FY2008 - 2028 and is estimated to be worth USD853 billion by 2028.
- Increasing share of real estate in the GDP would be supported by increasing industrial activity, improving income level, and urbanisation .

Market Size of Real Estate in (USD billion)



# India Real Estate – Growth Drivers



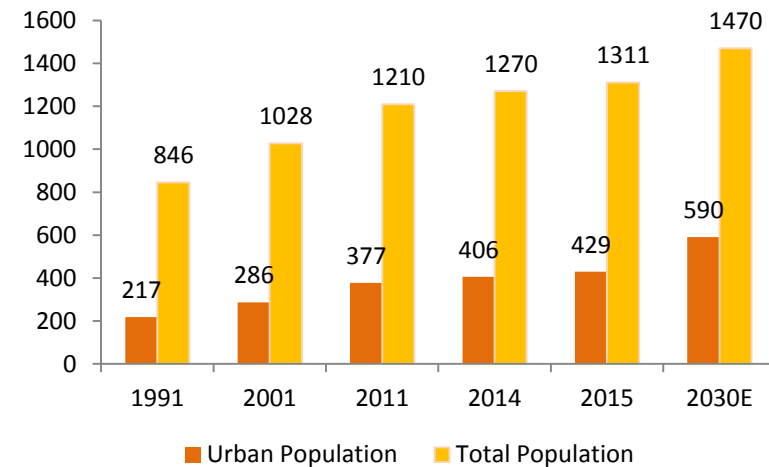
## Demographic Dividend

- India has population of 1.3 billion with median age of 27 years compared to 36 years in China, 46.1 years in Japan and 37.6 years in USA.
- Indian population has a young profile with ~45% of the population below 25 years of age.
- This demographic dividend will help India to have large educated and earning workforce and Increase in India's saving rate, thus helping India's urban population as a percentage of total population was around 32.7 per cent in 2015 and is expected to rise to 40.0 per cent by 2030.

## Rapid Urbanization

- Better wages and better standard of living is expected to result in an increase in urban population in India to above 600 million by 2031 from 429 million in 2015.
- Government initiatives such as various urban development policies and programmes are expected to contribute to enhanced urbanisation.
- Urbanisation and growing household income are driving demand for residential real estate and growth in the retail sector .
- In 2015, more than 429 million people were staying in cities, which is more than the population of the US.

Population breakdown of India (Mn)



Indian Census, World Bank, Mckinsey estimates, Cushman & Wakefield, TechSci Research

# India Real Estate – Growth Drivers



## Growing nuclear Family Culture

- Average household size is expected to decrease from 4.8 currently to just above 4.4 adding demand for 10 million new homes.

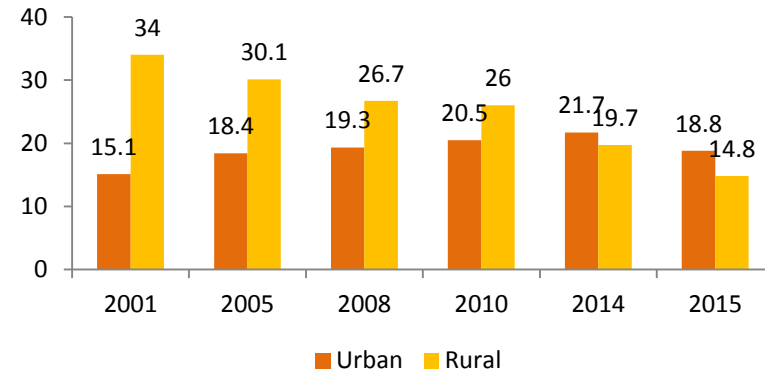
## Housing Shortage

- The current urban housing shortage is approximate 18.8 million units.
- Government plans to build 100 metro and Satellite cities.

## Mortgage Finance Penetration

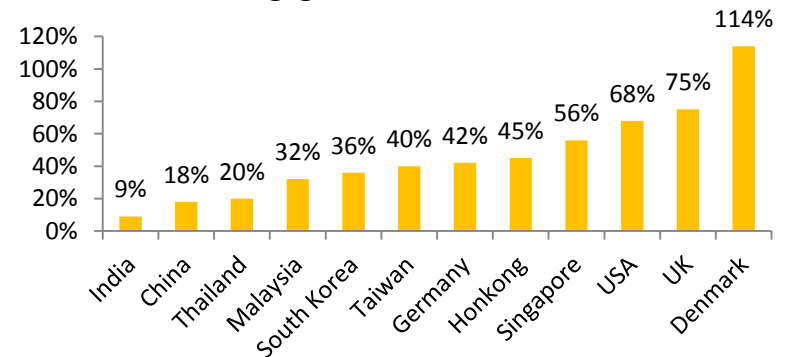
- The mortgage penetration in India is at 9% of Nominal GDP which is much lower than that of other emerging/developed countries.
- The mortgage finance industry is pegged at a size of INR 9 trillion and has grown at 15% CAGR over last 5 years.
- Availability of mortgage finance provides tremendous impact on the real estate housing demand.

Urban- Rural Housing Shortage(Mn)



Indian Census, World Bank, Mckinsey estimates, Cushman & Wakefield, TechSci Research

Mortgages as % of Nominal GDP



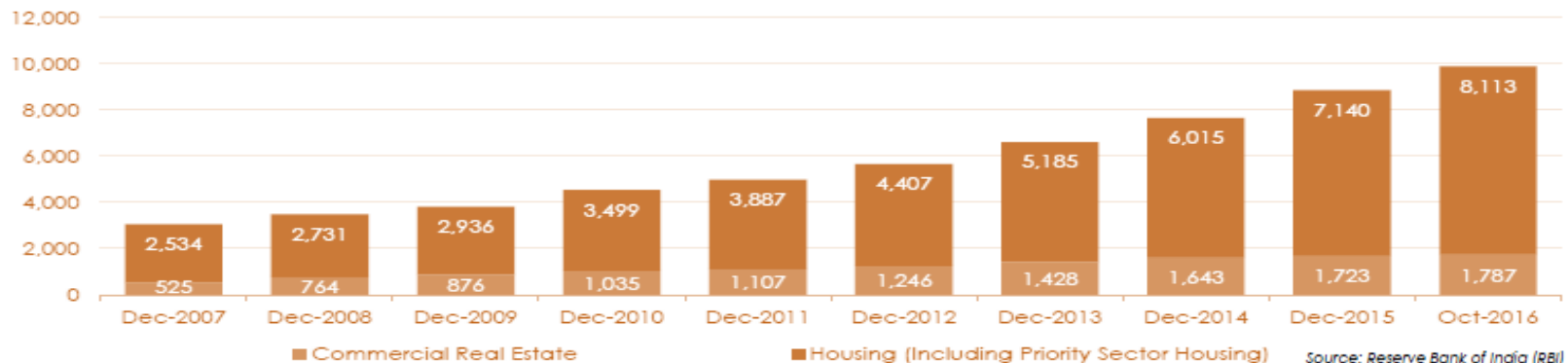
# India Real Estate – Growth Drivers



## Investment In Indian Real Estate

- USD 52.2 billion of offshore institutional capital and onshore institutional capital has been raised and deployed in the Indian Real Estate Sector (Source : Brookfield)
- In last year, USD 5.1 billion of institutional capital was committed for Indian real estate (Source : Brookfield)
- Of the total institutional private equity capital deployed till March 2014, nearly one-fifth, amounting to USD 6.9 billion, has been exited (Source : Brookfield)
- The total credit to housing sector by Indian banks is pegged above USD 27 billion

(Bank Credit to CRE  
in INR Bn)



# Real Estate Growth drivers continue to remain robust



Favourable Demographics

66% of India's population is below 35 years of age, hence large potential for housing demand

Rapid Urbanisation

Currently 32% of the Indian population reside in cities; estimated to be 40% by 2030

Households

Rise in the number of households with a shift towards nuclear families

Improved Affordability

Improved affordability through rising disposable incomes and affordable interest rates on home loans

Mortgage penetration

The mortgage penetration in India is at 9% of Nominal GDP which is much lower than that of other emerging/developed countries

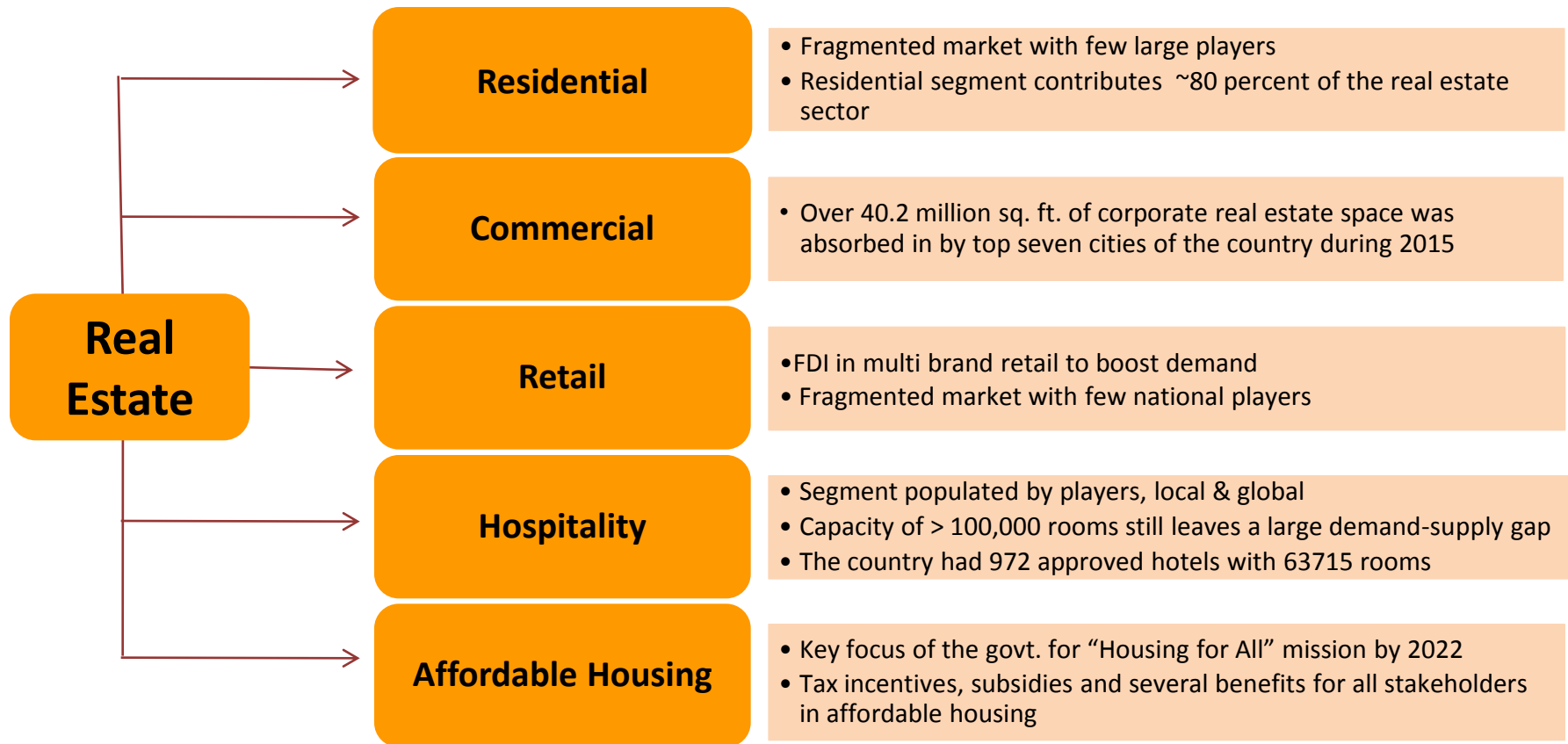
RERA

Real Estate (Regulatory & Development) Act, 2016 to bring greater transparency and discipline in the sector

Commercial Absorption

Robust office space absorption shall fuel demand dynamics for residential RE

# India Real Estate - Sectors





# Reforms

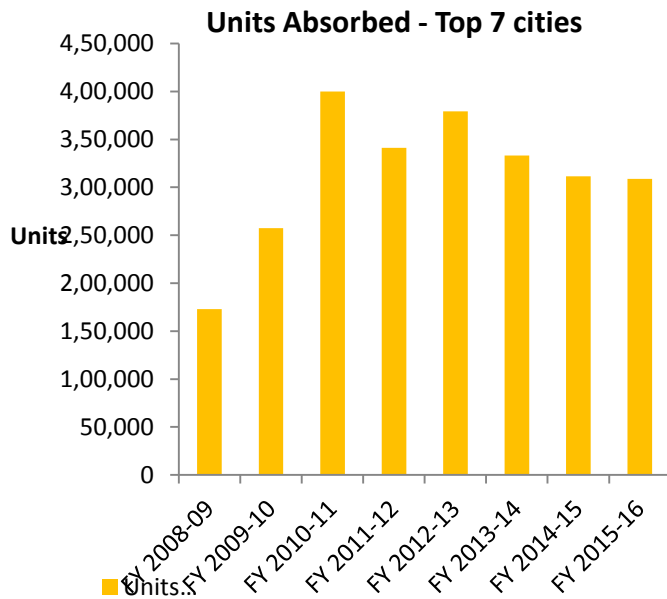
Ease of doing business	RERA
<ul style="list-style-type: none"> <li>▪ The Modi government since it assumed its term in 2014 have emphasised on Ease of doing business and taken steps in the same direction</li> <li>▪ As a result, India is one of the fastest growing economies of the world at the backdrop of strong domestic consumptions and global investments</li> </ul>	<ul style="list-style-type: none"> <li>▪ The Real Estate (Regulation and Development) Act, 2016 is enacted to provide greater transparency to customers of real estate in India</li> <li>▪ The endeavour of the Law is to organise the much unorganised real estate sector with uniformity across projects in the country Provisions include : Consent of buyers incase project changes, using buyer needs for project purposes, registration of project with govt. Authorities, Marketing guidelines etc</li> </ul>
<ul style="list-style-type: none"> <li>• Construction - Development projects - 100% FDI through automatic route is permitted.</li> <li>• No minimum land area requirement in case of development of serviced plots.</li> <li>• In case of construction-development projects, minimum floor area of 20,000 sq. mts.</li> <li>• Minimum investment of only USD 5 Million</li> <li>• Exit permitted on completion of the project or after the development of trunk infrastructure</li> </ul>	<ul style="list-style-type: none"> <li>• Uniform Indirect Tax regime through enactment of GST (Goods and Service Tax)</li> <li>• Bankruptcy Code, 2016</li> <li>• SARFAESI (Central Registry) Rules</li> <li>• Housing for All mission by 2022</li> <li>• Smart City Project of PM Modi</li> <li>• Make in India Initiative to push manufacturing</li> </ul>



# Indian Real Estate – Current Scenario

## Real Estate

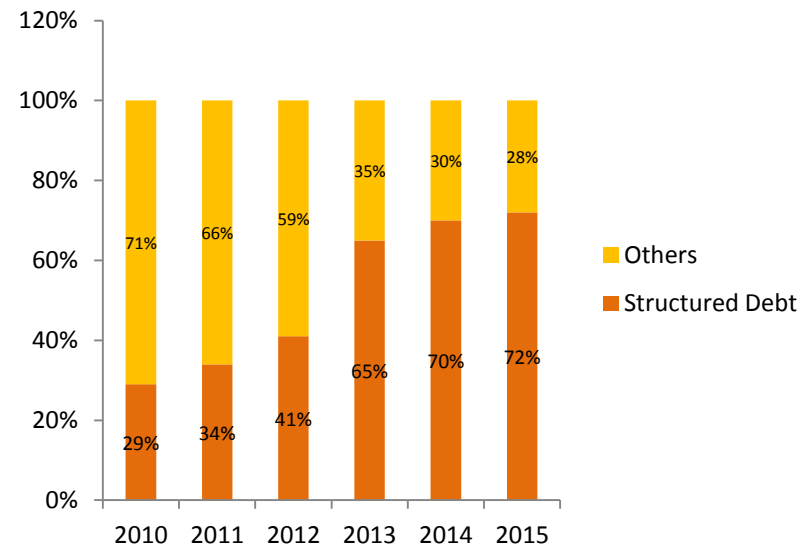
- **Current Scenario** : Sales velocity has dipped by ~20% from its peak in 2010 – 11.



- **Impact** : Cashflow mismatches for levered projects
- **Result** : Significant financing opportunities for PE funds

## Private Equity

- **Type for transaction in Indian PE** : Structured Debt has emerged as winner



- **Reason** :
  - Private equity funds are nearing the end of the fund life
  - The Promoters are obliged to provide such exits

- **Outcome** : Medium term debt capital is the preferred route of deal making for both, PE Funds and Developers

# Opportunities

## Real Estate Funding

### Banks

- Highly regulated with significant end use restrictions and capital adequacy norms
- No funding to private builders for acquisition and development of land

### NBFC

- Strict norms in terms of servicing the interest on funding at a regular periodicity
- Cash flow mis-match makes making interest servicing to NBFC's difficult for developers

### Equity Capital Markets

- Available to only top 5% percentile of the Industry; Valuation mis-match

### Private Equity Funds

- Global and domestic private equity funds active post 2008 to participate mainly at project level through equity, debt and Mezzanine transactions

***Developers keen on alternative sources of funds, as funds from conventional sources have dried up, leading to an increase in opportunity***

## High Yield Debt Opportunity

- End use restriction free capital for acquisitions, approvals, equity working capital, restructuring bank debts etc through high yield fixed return transactions
- To structure debt deals that generate high yields (18 – 20% IRR)
- The funds can allow Developers to structure the repayment schedule in line with underlying project cash flows

# Opportunities for International Capital



## Fixed Return

- Model : Fixed return portfolio with residential real estate assets with developers across geographies
- Returns : 18% - 20% IRR
- Security : 1.5X – 2X
- Mode : Listed NCD's / CCD's

## Equity

- Model : Structured equity participation with developers across geographies
- Returns : 20% - 24% IRR
- Partners : Top 20 developers in Tier I cities
- Asset class : Residential

## Income Yielding Funds//REITS

- Model : Acquisition of completed commercial assets
- Returns : 15% - 18% IRR
- Distribution : Quarterly
- Security : 100% buy outs

## Platform Level Deals

- Model : Equity platform participation with a marquee developer in India
- Tenure : 5 – 7 years
- Returns : 17% - 24% IRR

# AIF – Key Considerations



## Key considerations for set-up and managing an AIF

- AIF to be formed as a pooling vehicle for making investment in securities
  - AIF could be set-up as either a Trust, Company or LLP; typically set-up as Trust for flexibility in operations
  - AIF would need to be registered with SEBI, if the objective is to invest in securities of companies in real estate sector
  - Minimum corpus requirement of INR 20 crores; maximum of 1000 investors; minimum contribution of INR 1 crore per investor
  - Investment objective, target investors, proposed corpus etc to be disclosed to SEBI at the time of seeking registration
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# AIF – Pros..

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## Pros

- AIF can hold securities in its own name or in the name of trustee
  - AIF can invest into LLPs
  - Administratively convenient to manage a AIF vehicle
  - No restriction on charge of management fees; Possible to structure carried interest as return on investment vs. performance fee
  - AIF can be listed; affords flexibility in operation to handle multiple investors
  - No distribution tax on income paid / distributed by AIFs
  - Foreign Investments in Alternate Investment Funds allowed
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# AIF – Pros..

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## Pros

### Tax Impact

- AIF Category I and II eligible for pass-through on all income other than business income
  - Capital gains and interest income eligible for pass-through
  - Fund exempt, investors taxable
  - Income taxable in investors' hands, deemed to be of the same nature and proportion as in the AIF's hands

# AIF – Cons..

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## Cons

- Minimum contribution per investor is INR 1 crores
  - Sponsor commitment required of 2.5% of the corpus or 5 crores whichever is lower
  - Not more than 25% of the investible funds can be invested in one company
  - SEBI approval can be time consuming affair and adequate time needs to be budgeted for launching any product under an AIF.
  - Timelines for setting up an AIF is 2-3 months; significant documentation required
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# AIF – Cons..

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## Cons

### Tax Impact

- Business income taxable at AIF level
  - Correspondingly such income exempt for investors
  - AIF to withhold tax at the rate of 10 per cent on income credited / paid to resident investors and for non resident it will be deducted as per the applicable rate of tax .
  - Issue is whether withholding tax would also be applicable on exempt income
  - Loss to be carried forward at AIF level for set off in future years
  - Losses not to be passed on to investors
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**Thank You !**

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