



# Indian Real Estate Sector – Small and Medium REITs

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**SM REIT regulations could create  
monetisation opportunity of Rs.  
68,000-71,000 crore for small office  
spaces**

**APRIL 2024**





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*Small and medium REIT-ready office spaces are estimated at ~52-53 million square feet, indicating a healthy potential for SM REIT listings in the commercial office space.*



SEBI has announced that it will regulate fractional ownership platforms (FOPs) offering real estate assets through small and medium REITs (SM REIT). Registration of existing FOPs and new ones is mandatory under SEBI. FOPs allow investors to participate in real estate ownership with fractional shares and minimum investment ranging from Rs. 10-25 lakh. Given the increasing value of investments with such FOPs and the growing number of investors, SEBI has introduced regulatory oversight in the form of SM REIT regulations.



SM REITs will provide an opportunity for small Grade A and most of the Grade B office developers to monetise their investments. Also, fractional ownership platforms are expected to be formalised, leading to wider market acceptance. At present, it is estimated that the assets under management (AUMs) for various FOPs stand at Rs. 5,000 crore. However, the minimum unitholding requirement for SM REITs could act as a deterrent from a scalability perspective.



As of December 2023, the total Grade A office supply stood at 980 msf and Grade B office at 115 msf across the top seven cities. ICRA estimates SM REIT-ready office space at ~52-53 msf (3% of Grade A supply and 20% of grade B supply), indicating a healthy potential for SM REIT listings in the commercial office space. At a cap rate of 8-8.5%, SM REIT-ready office space provides monetisation opportunity of Rs. 67,000 – 71,000 crore across top seven cities.



ICRA has maintained a Stable outlook on India's commercial office sector. With healthy demand from global capability centres (GCCs), non-IT MNCs and domestic corporates, the net absorption across the top six cities is expected to grow by 4-5% in FY2025, after a decline of 19-20% to 47-48 million square feet (msf) in FY2024. With the influx of a huge supply of around 60-62 msf in FY2025, the vacancy levels are expected to remain at around 16.0-16.2% (largely similar to the previous year).

## 1 Small and Medium REITs



## 2 Outlook on Commercial Office – Stable



## 3 Rating Actions in Commercial Real Estate





## Small and Medium REITs

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# Sponsor, Investment Manager and Investment Conditions of REIT and SM REIT

Parameter	For current REITs	For small and medium REITs
<b>Sponsor</b>	The sponsor(s), on a collective basis, must have a net worth of not less than Rs. 100 crore, provided that each sponsor individually has a net worth of not less than Rs. 20 crore.	<ul style="list-style-type: none"> <li>▪ ‘Sponsor’ or ‘Manager’ shall be construed as a reference to an ‘Investment Manager’ of the SM REIT</li> <li>▪ Investment manager means a company incorporated in India, which sets up SM REIT and manages assets and investments of the SM REIT and undertakes operational activities of the SM REIT</li> <li>▪ Should have a net worth of at least Rs. 20 crore provided that at least Rs. 10 crore of net worth of the investment manager is in the form of liquid net worth</li> <li>▪ Should have at least 2 years of experience either in the real estate industry, real estate fund management or it shall employ at least 2 key managerial personnel, having not less than 5 years of experience in the real estate industry or real estate fund management.</li> </ul>
	The sponsor or its associate(s) should not have less than 5 years of experience in real estate development or fund management in the industry. If the sponsor is a developer, at least 2 projects of the sponsor should be completed.	
<b>Investment manager (IM)</b>	Manager to have a minimum net worth of Rs. 10 crore, if it is a body corporate or a company. If LLP, minimum net tangible assets of value should be Rs. 10 crore	
	The manager or its associate should have at least 5 years of experience in either fund management, advisory services, property management in the real estate industry or in real estate development	
<b>Investment conditions</b>	The manager has atleast 2 key personnel, having at least 5 years of experience in either fund management, advisory services, property management in the real estate industry or in real estate development.	
	REIT’s ultimate holding interest in the underlying SPV(s) should not be less than 26%	The SPV shall directly and solely own all assets that are acquired or proposed to be acquired by the scheme of the SM REIT, of which SPV is the wholly owned subsidiary.
	At least 80% of the REIT’s asset values shall be invested in completed and rent - generating assets. A maximum of 20% of the value of the REIT assets shall be invested in under-construction properties, which shall be held by the REIT for not less than 3 years after completion.	The scheme of the SM REIT shall invest at least 95% of the value of the schemes’ assets for each of its schemes <ul style="list-style-type: none"> <li>▪ in completed and revenue-generating properties and shall not invest in</li> <li>▪ under-construction or non-revenue generating real estate assets.</li> </ul>
	REIT shall not invest in vacant land, agricultural land or mortgages other than mortgage-backed securities.	Provided that up to 5% of the value of the schemes’ assets may be invested in liquid assets, which are unencumbered
	REITs shall not invest in units of other REITs. No schemes shall be launched under the REIT.	The scheme of SM REIT shall not be permitted to lend to any entity other than lending to its own SPV. The SPV shall not be permitted to lend to any entity

Parameter	For current REITs	For small and medium REITs															
<b>Lock-in requirements for unitholding</b>	<p>The sponsor(s) and sponsor group(s) shall collectively <b>hold a minimum of 15%</b> of the total units of the REIT for a period of <b>at least three years</b> from the date of listing</p> <p>Provided that any holding of the sponsor(s) and sponsor group(s) exceeding the minimum holding, shall be held for a period of at least one year from the date of listing of such units</p>	<p>Minimum unit holding requirement applicable to the investment manager for the period of the first 3 years commencing from the date of listing of units in the initial offer till the end of the third year, shall be :</p> <ul style="list-style-type: none"> <li>in a scheme which has opted <b>not</b> to undertake leverage, the investment manager will have to <b>always hold at least 5% of the total outstanding units</b>.</li> <li>in a scheme which has opted to undertake leverage, the investment manager will have to <b>always hold at least 15% of the total outstanding units</b>.</li> </ul> <p>Provided that <b>any holding more than 15% or 5%</b>, will be held by the investment manager for <b>at least one year from the date of listing of units</b>.</p> <p>Minimum unit holding by investment managers in each scheme of SM REIT:</p> <table border="1" data-bbox="1081 631 1866 838"> <thead> <tr> <th>Minimum unit holding of SM REIT in each scheme</th> <th>Duration of holding</th> <th>Years from date of listing of initial offer</th> </tr> </thead> <tbody> <tr> <td>5%</td> <td>2 years</td> <td>Year 4 and Year 5</td> </tr> <tr> <td>3%</td> <td>5 years</td> <td>Year 6 to Year 10</td> </tr> <tr> <td>2%</td> <td>10 years</td> <td>Year 10 to Year 20</td> </tr> <tr> <td>1%</td> <td>Perpetual</td> <td>From Year 20</td> </tr> </tbody> </table> <p>The units in which holding is required to be maintained shall be <b>unencumbered and locked-in</b>.</p>	Minimum unit holding of SM REIT in each scheme	Duration of holding	Years from date of listing of initial offer	5%	2 years	Year 4 and Year 5	3%	5 years	Year 6 to Year 10	2%	10 years	Year 10 to Year 20	1%	Perpetual	From Year 20
Minimum unit holding of SM REIT in each scheme	Duration of holding	Years from date of listing of initial offer															
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# Investments, Distribution and Leverage of REIT and SM REIT

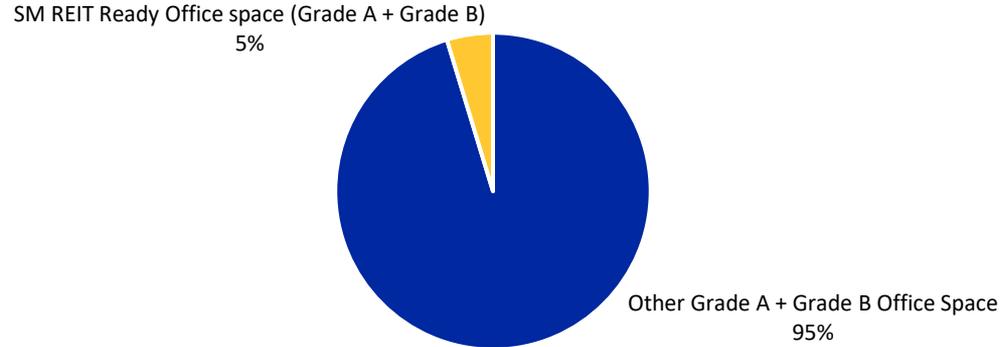
Parameter	For current REITs	For small and medium REITs
Investments	The value of the REIT assets <b>should be at least Rs. 500 crore.</b>	The proposed asset size to be acquired within the SM REIT scheme is <b>at least Rs. 50 crore and less than Rs. 500 crore.</b>
	The minimum number of unit holders other than sponsor(s), its related parties and its associates forming part of the public, shall be not less than 200 investors.	The minimum number of unit holders of the SM REIT scheme other than the investment manager, its related parties and associates of the SM REIT should not be less than 200 investors.
	Maximum subscription from any investor other than sponsor(s), its related parties and its associates, shall not be more than 25% of the total unit capital.	The minimum subscription amount from any investor in any offer shall be <b>Rs. 10 lakhs</b> or such amount as may be specified by the Board from time to time.
	The <b>offer size is at least Rs. 250 crore</b>	The minimum offer and allotment to the public shall be <b>at least 25% of the total outstanding units</b> of each scheme
Distribution	Not less than <b>90% of net distributable cash flows (NDCF)</b> of the SPV shall be distributed to the REIT in proportion of its holding in the SPV. <b>not less than 90% of the net NDCF of the REIT</b> shall be distributed to the unit holders.	<b>Not less than 95% of NDCF</b> of the SPV are distributed to the scheme of SM REIT <b>100% of the NDCF of the SM REIT scheme</b> shall be distributed to the unit holders.
	Such distributions shall be declared and made not less than <b>once every six months</b> for each financial year and not later than fifteen days from the date of such declaration.	The distributions are declared <b>at least once in every quarter</b> of the financial year and not later than fifteen working days from the end of the quarter.
	If the distributions are not made <b>within fifteen days of declaration</b> , then the manager shall be liable to pay interest to the unit holders at the rate of 15% per annum until the distribution is made.	If the distributions are not made <b>within seven days of declaration</b> , then the manager shall be liable to pay interest to the unit holders at the rate of 15% per annum till the distribution is made
Leverage	The aggregate consolidated borrowings and deferred payments of the REIT [holdco and/or the SPV(s),] net cash and cash equivalents shall <b>never exceed 49%</b> of the value of the REIT assets. <b>If the same exceeds 25%</b> , for any further borrowing - <b>credit rating shall be obtained</b> from a credit rating agency registered with the Board	The scheme offer document shall state whether the SM REIT scheme is with or without leverage. SM REIT schemes that choose to leverage their assets will be subject to borrowing limitations. The total debt minus readily available cash (loan-to-value ratio) <b>at the scheme level cannot exceed 49% of the value of the scheme's assets.</b> However, if the <b>loan-to-value ratio surpasses 25%</b> , any <b>further borrowing will require a credit rating</b> from a credit rating agency registered with the Board.

# Valuation Requirements for REIT and SM REIT

Parameter	For current REITs	For small and medium REITs
Valuation	<p>A full valuation shall be conducted by the valuer at least once in every financial year, provided that such valuations are conducted at the end of the financial year, ending March 31st, <b>within three months</b> from the end of such year.</p> <p>A <b>half-yearly valuation</b> of the REIT assets shall be conducted by the valuer for the half-year ending on September 30 for incorporating any key changes in the previous six months and such half-yearly valuation report shall be prepared <b>within forty-five days</b> from the date of end of such half year.</p>	<p>The investment manager shall ensure that the valuer shall carry out the full comprehensive valuation of the assets of each scheme of the SM REIT on an annual basis and submit its report to the investment manager <b>within two months</b> from the end of the financial year.</p> <p><b>Half-yearly valuation is not required for SM REIT</b></p>
	<p>The valuer shall not be an associate of the sponsor(s) or manager or trustee and shall have <b>not less than five years of experience</b> in the valuation of real estate.</p>	<p>The investment manager shall ensure that the valuer is not an associate of the investment manager or trustee of the SM REIT and that the signatory to the valuation reports <b>has at least five years of experience</b> in the valuation of real estate.</p>
	<p>The net asset value of the REIT is based on the valuation done by the valuer and is declared no later than fifteen days from the date of valuation to the stock exchange(s) and such computation shall be done and declared not less than <b>once every six months</b>.</p>	<p>The net asset value of each scheme shall be required to be declared and disclosed to the recognized stock exchanges based on the latest valuation report as on March 31st (<b>once every year</b>) and upon the occurrence of any material development.</p>
	<p>Valuation reports received by the manager shall be submitted to the designated stock exchange and unit holders <b>within fifteen days</b> from the receipt of such valuation reports.</p>	<p>The investment manager shall submit the valuation reports to designated stock exchanges and unit holders <b>within one working day</b> from the receipt of such valuation reports.</p>
	<p>The investment manager shall ensure that no valuer undertakes valuation of the properties of the schemes of the SM REIT for <b>more than four years</b> consecutively.</p>	<p>The investment manager shall ensure that no valuer undertakes valuation of the properties of the schemes of the SM REIT for <b>more than four years</b> consecutively</p>
	<p>With respect to the purchase or sale of properties after the initial offer - <b>two valuation reports</b> from two different valuers, independent of each other, shall be obtained.</p>	<p>For any purchase of a new property or sale of an existing property, the investment manager shall require the <b>valuer</b> to undertake a full comprehensive valuation of that property.</p>

# SM REIT-ready office space provides monetisation opportunity of Rs. 67,000 – 71,000 crore

Exhibit 1: 3% of India's Grade A and 20% of Grade B office space is SM REIT-ready (December 2023)



Source: Propequity, ICRA Research; To arrive at SM REIT-ready office spaces, ICRA has included Grade A office space with less than 2 lakh sft and total Grade B office spaces across top 7 cities with a minimum occupancy of 80% as of December 31, 2023. To arrive at the monetisation opportunity for SM REIT-ready office spaces, ICRA has used a cap rate of 8-8.5%.

- As of December 2023, the total Grade A office supply stood at 980 msf and Grade B office at ~115 msf across the top seven cities. ICRA estimates SM REIT-ready office at ~52-53 msf (3% of Grade A supply and 20% of grade B supply) of the total office supply, indicating a healthy potential for SM REIT listings in the commercial office space.
- At a cap rate of 8-8.5%, SM REIT-ready office space provides monetisation opportunity of Rs. 67,000 – 71,000 crore across the top seven cities.



## Outlook on Commercial Office – Stable

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*Global macroeconomic headwinds loom over office leasing*



## Outlook – FY2025

### OCCUPANCY



#### Occupancy to decline marginally

Occupancy to remain at around 83.8-84.0% during FY2024 and FY2025

### RENTALS and NOI



#### Contracted rent escalations & new tie-ups to support rentals & NOI

Rental inflow and net operating income (NOI) expected to improve by 11-12% in FY2025

### LEVERAGE



#### Leverage to ease in FY2025

Debt-to-NOI ratio expected to improve to 4.5-4.6x in FY2025 from estimated levels of 5.2-5.3x in FY2024, supported by higher NOI

### COVERAGE



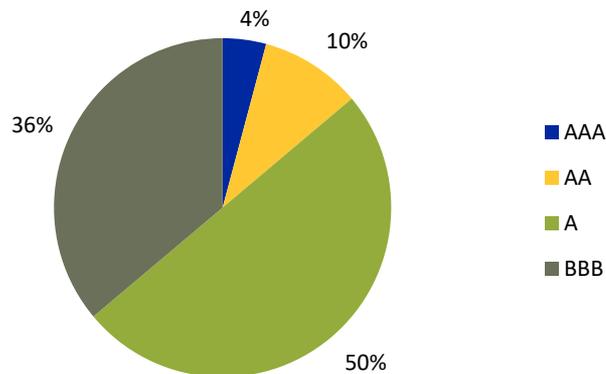
#### Coverage to improve on the back of increase in NOI

DSCR expected to improve and remain healthy at 1.35x in FY2025, over 1.25x in FY2024



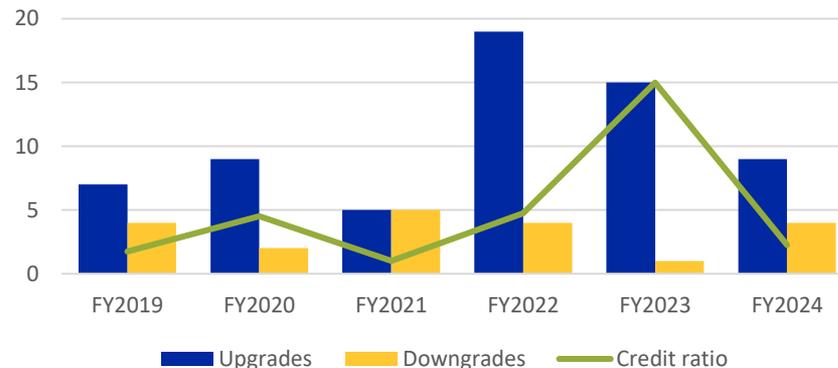
# ICRA's Rating Actions in Commercial Office Leasing

Exhibit 2: Rating distribution of ICRA-rated entities



Source: ICRA Research; Note: Excludes rating actions due to issuer non-cooperation

Exhibit 3: Count of upgrades and downgrades

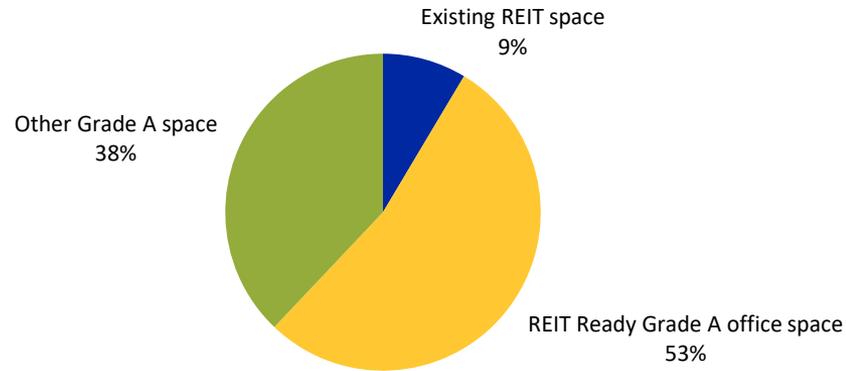


Source: ICRA Research; Note: Excludes rating actions due to issuer non-cooperation

- The rating distribution of entities in the office leasing segment is skewed towards higher rating categories, with the median rating falling within the A category. This reflects the industry's high degree of consolidation, where larger developers benefit from their established market position and access to capital.
- In FY2024, there were nine upgrades and four downgrades (of which three are part of the same group). A healthy increase in pre-leasing, mitigating refinancing risk for under-construction assets and improvement in occupancy levels for the operational portfolio. This resulted in enhanced debt protection metrics, which is one of the major reasons for the upgrades in FY2024. For the three entities in the same group, a delay in the ramp-up of occupancy levels and an increase in indebtedness adversely impacted the debt protection metrics and resulted in a rating downgrade. Additionally, space rationalisation from a major tenant and the resultant moderation in debt protection metrics were the other reasons for the downgrade.

# Annexure 1: REIT-ready office supply stands at 6-6.5 times of current REITs' operational area

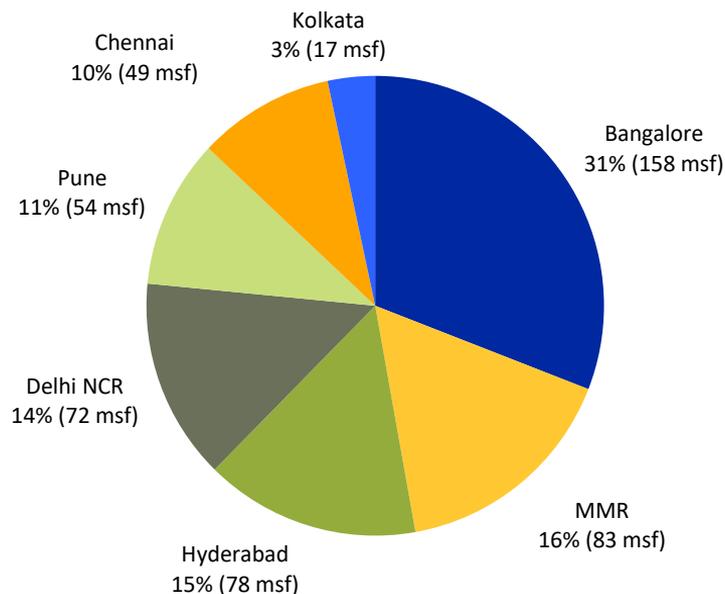
Exhibit 4: Around 53-54% of India's Grade A office space is REIT-ready (December 2023)



Source: Propequity, ICRA Research; To arrive at REIT-ready office spaces, ICRA has included developers with at least 1 million sft of Grade A office space across top 7 cities with a minimum occupancy of 75% as of December 31, 2023.

- As of December 2023, total Grade A office supply stood at 979.7 msf across the top seven cities. Of this around 82.4 msf (9%) made up the existing REIT supply. REIT-ready office space is estimated at 510 msf (53-54%) of total office supply, indicating a significant potential for further REIT listings in the commercial office space.
- REIT-ready office supply has the potential to increase the market by 6.0-6.5 times.

**Exhibit 5: City-wise distribution of REIT-ready office space**



**Exhibit 6: Investment for REIT-ready office space**

City	REIT-ready Investment in Rs. '000 crore
Bangalore	184 - 196
MMR	136 - 144
Hyderabad	71 - 76
Delhi NCR	72 - 77
Pune	59 - 63
Chennai	47 - 50
Kolkata	12 - 13
<b>Total</b>	<b>583 - 619</b>

- Bangalore, which already leads in total office supply in India, also has the highest REIT-ready office space with 158 msf, followed by MMR (83 msf) and Hyderabad (78 msf).
- Though Hyderabad leads marginally in REIT-ready space, due to higher weighted average rental rates in Delhi NCR, the investment opportunity requirement is greater in Delhi NCR.

Source: Propequity, ICRA Research

To arrive at the investment opportunity for REIT-ready office spaces, ICRA has used a cap rate of 8–8.5%.



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