Understanding REITs in India

A MoneyWorks4Me guide to how Real Estate Investment Trusts work, why India's REIT market is set to grow, and what investors should evaluate before investing.

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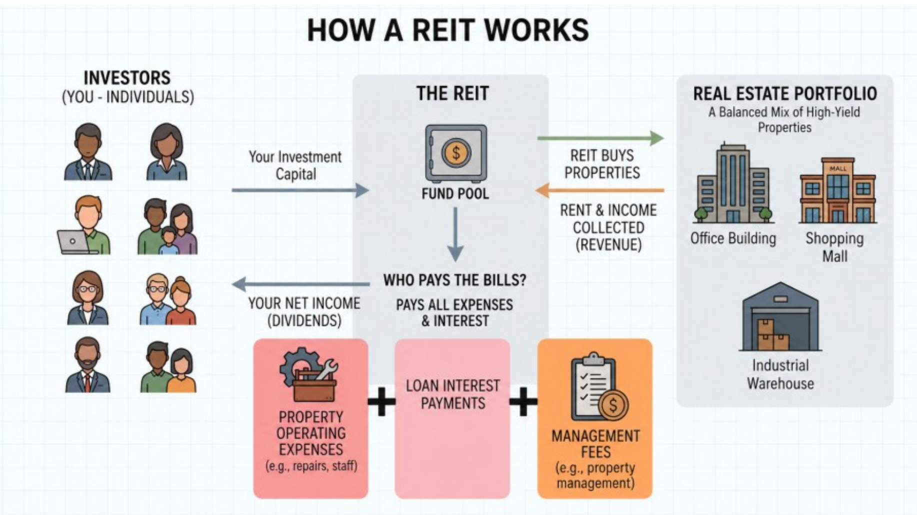
What is REIT?

A Real Estate Investment Trust (REIT) is an investment vehicle that owns income-generating real estate, such as office parks, shopping malls, hotels, and other commercial properties. REITs can be preferred over physical real estate because physical real estate usually requires a large capital investment and is less liquid. In comparison, REITs allow investors to participate in commercial real estate with smaller ticket sizes and can be bought or sold on the stock exchange.

Investors can buy units of a listed REIT on the stock exchange, similar to buying shares of a company. Just as mutual funds pool money from investors and invest it in the shares of listed companies, REITs pool money from investors and invest it in real estate properties. The REIT then collects rental income from these properties, pays operating costs and interest expenses, and distributes 90% of the remaining cash to its unitholders.



✦ KEY TAKEAWAYS

- A REIT is an investment vehicle that owns income-generating commercial real estate such as offices, malls and hotels.
- REITs offer smaller ticket sizes and better liquidity than owning physical real estate directly.
- Like a mutual fund, a REIT pools investor money — but invests it in real estate instead of listed equity.
- REITs are required to distribute 90% of their distributable cash to unitholders.

REIT Structure

There are various parties involved in REIT structure i.e. sponsor, REIT or trust, Manager, trustee, holding company and special purpose vehicle (SPV), unitholders.

Sponsors: The Sponsor is the party that establishes the REIT and is broadly comparable to the promoter of a listed company. It is generally a real estate developer, institutional property owner or investment platform that already owns a portfolio of income-generating properties.

REIT or Trust: The REIT itself is constituted as a trust and registered with the market regulator i.e. SEBI. It is the central investment vehicle through which investors collectively own an interest in the underlying real estate portfolio. The REIT issues units to investors and uses the capital raised to acquire, develop or hold income-generating properties.

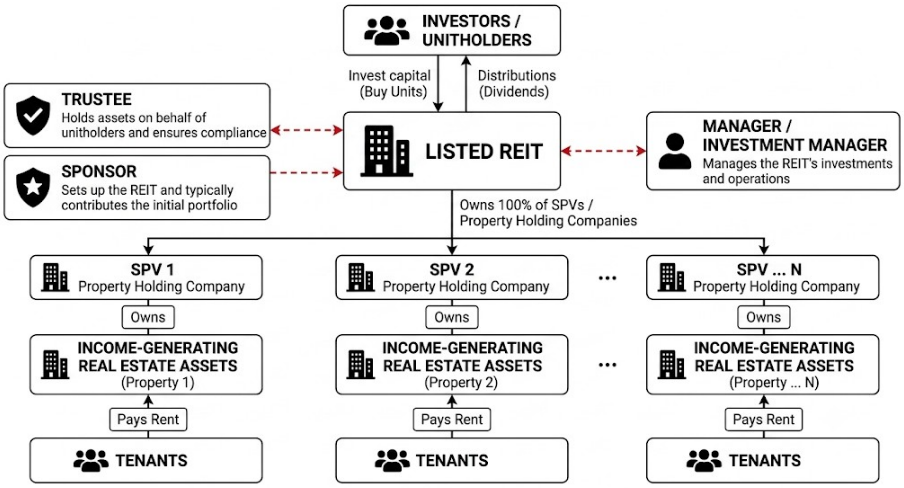
Manager: The Manager is responsible for managing the assets and business operations of the REIT. The Manager formulates the overall strategy of the REIT and makes decisions relating to leasing, tenant renewals, rental negotiations, property operations, acquisitions, disposals, development projects, capital expenditure, debt management and refinancing. It also evaluates opportunities to improve occupancy, increase rental income, undertake redevelopment and expand the portfolio.

Trustee: The Trustee is an independent party that holds the assets of the REIT in trust for the benefit of its unitholders. The Trustee does not generally take commercial decisions relating to leasing, acquisitions or property operations. Instead, its primary responsibility is to supervise the Manager and ensure that the REIT is operated according to applicable regulations and the trust deed.

Holding company or Special Purpose Vehicle (SPV): A REIT may hold its properties through one or more holding companies or SPVs. An SPV is a separate legal entity that owns one or more individual properties. The SPV enters into lease agreements with tenants, collects rental income and pays property-level operating expenses. It may also have debt raised specifically against the property owned by it. After meeting operating costs, interest, taxes and other obligations, the remaining eligible cash is transferred to the REIT.

> *Note: SPV: An SPV is a separate company that legally owns one or more properties on behalf of the REIT.*

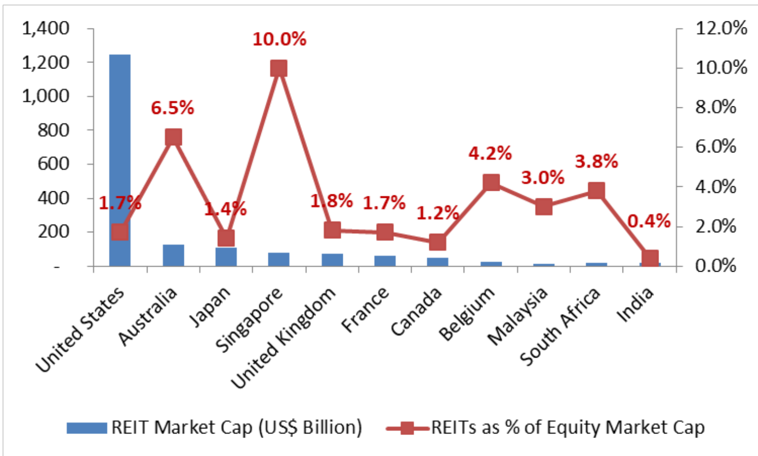
Unitholders: Unitholders are investors who provide capital to REIT by purchasing its units. These investors may include the retail investor, mutual funds, insurance companies, etc. Unitholders are entitled to receive distributions declared by the REIT and may benefit from an increase in market price of the units.



✦ **KEY TAKEAWAYS**

– A REIT's structure has six key parties: Sponsor, Trust, Manager, Trustee, SPVs and Unitholders.
– The Sponsor sets up the REIT — comparable to a promoter of a listed company.
– The Manager runs day-to-day strategy and operations; the Trustee independently supervises the Manager on unitholders' behalf.
– SPVs directly own individual properties, collect rent, and pass eligible cash up to the REIT.

Underpenetrated



The REIT market in India remains underpenetrated. Globally, REIT market capitalisation is generally more than 1% of the total equity market capitalisation, compared with only 0.4% in India. Moreover, the global REIT market is valued at approximately US$2 trillion, while India's REIT market capitalisation is only around US$21 billion. This significant gap indicates considerable growth potential for the Indian REIT market over the coming years.

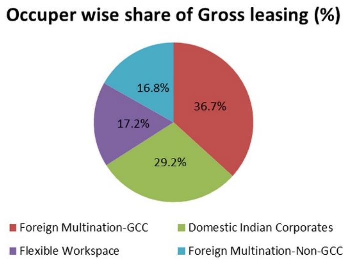
Source: S&P Global, NSE

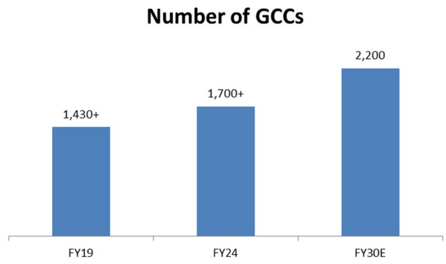
✦ **KEY TAKEAWAYS**

– India's REIT market cap is only 0.4% of total equity market cap, versus over 1% in most global markets.
– India's REIT market (~US$21 billion) is a small fraction of the ~US$2 trillion global REIT market.
– This gap points to considerable long-term growth potential for REITs in India.

Growth Drivers

GCC Growth Engine

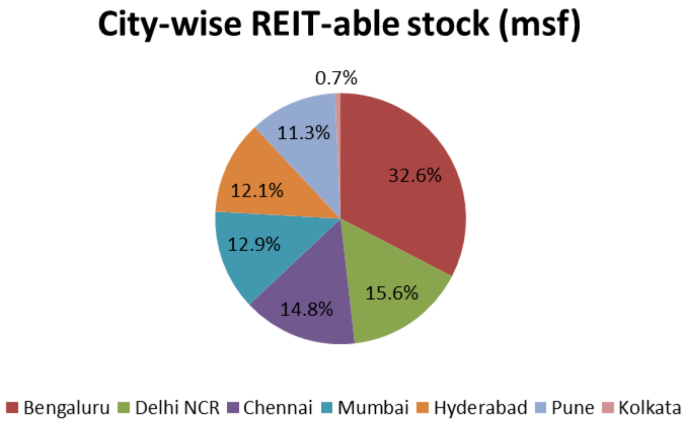




More global companies are establishing offices in India. These companies typically enter into long-term leases, which provide stable rental income for REITs. India currently has more than 1,700 Global Capability Centres (GCCs), and this number is expected to exceed 2,200 by FY30. Further, between CY21 and H1CY25, GCCs accounted for 37.5% of total office leasing activity.

Source: Embassy Quarterly Presentation; Bagmane Prime office REIT DRHP

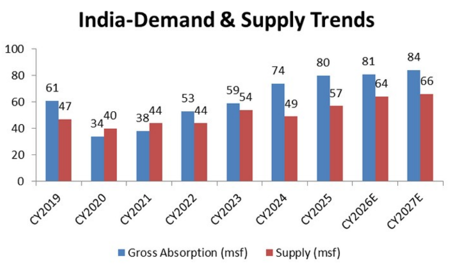
Healthy REIT-able potential

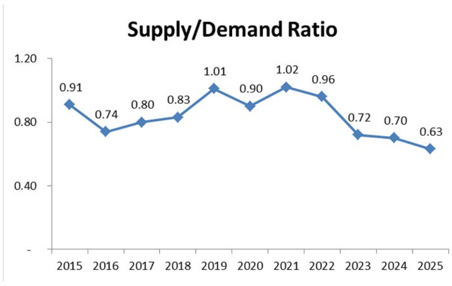


India's four major office led REITs cumulatively account for 132.2 msf, which equates 15% of the total operational grade A office stock across the top seven cities as of June 25. As per the estimates current REIT-able potential across top seven cities stands at 415 msf of operational projects that are currently not under REITs. Bengaluru has the highest office stock of REIT-able assets with a share of ~32.6%.

Source: Bagmane Prime office REIT DRHP

Demand Supply





Across India's top eight markets, demand for commercial office space has continued to outpace supply. The supply-to-demand ratio compares the amount of new office space entering the market with the amount of office space occupied or absorbed by tenants during the same period. For example, a supply-to-demand ratio of 1.25x means that 1.25 million sq. ft. of new office space was added for every 1 million sq. ft. absorbed by tenants. Similarly, a ratio of 0.8x means that only 0.8 million sq. ft. of new office space was supplied for every 1 million sq. ft. of demand. Over the past 10 years, the supply-to-demand ratio has remained below 1.0x in most years, indicating that demand has been higher than supply in the market.

Source: Knight Frank Research; Embassy Office Park REIT Annual Report

✦ **KEY TAKEAWAYS**

- GCCs are a major demand driver — expected to grow from 1,700+ to over 2,200 by FY30, and already 37.5% of office leasing (CY21–H1CY25).
- India's four listed office REITs hold 132.2 msf (15% of Grade A office stock); 415 msf of REIT-able assets remain outside REITs.
- Bengaluru leads REIT-able office stock with a ~32.6% share.
- Office demand has outpaced supply in most years over the last decade, supporting rental growth.

Key parameters to analyze REITs

Investing in a REIT is different from investing in a traditional company. Instead of focusing mainly on product sales or profits, investors should evaluate how efficiently the REIT's properties generate stable rental income and cash flows, as these ultimately drive returns to unitholders.

Occupancy Rate: The first thing to look at is the occupancy rate, which indicates how much of the REIT's leasable area is currently occupied by tenants and generating rent. A higher occupancy rate generally translates into stable rental income, stronger cash flows, and greater visibility of future distributions. For office REITs, an occupancy rate of more than 90% is generally considered healthy.

Rent Escalation & MTM: Occupancy alone, however, does not tell the complete story. Investors should also understand how rental income grows over time. Most commercial leases include rent escalation clauses, where rentals typically increase by around 5% every year or about 15% every three years. This means the REIT can generate higher rental income from existing tenants even without acquiring new properties. In addition, investors should monitor the mark-to-market (MTM) opportunity. When an existing lease expires, the REIT may be able to renew it at prevailing market rents. If market rentals have increased since the original lease was signed, the renewed lease can generate significantly higher rental income, providing another important source of organic growth.

Weighted Average Lease Expiry (WALE): Another important parameter is the Weighted Average Lease Expiry (WALE). It shows, on average, how many years are left before the REIT's existing leases expire. It helps investors understand how secure the REIT's future rental income is. A longer WALE means tenants are committed to staying for a longer period, making cash flows more predictable and reducing the risk of sudden vacancies. On the other hand, a shorter WALE indicates that a larger portion of leases will come up for renewal in the near future, increasing uncertainty regarding occupancy rates. However, a shorter WALE is not always negative. If market rents are higher than the existing rents, lease expiries can provide an opportunity for the REIT to re-lease the space at higher market rents, creating a mark-to-market (MTM) opportunity.

Debt Profile: Since REITs are required to distribute at least 90% of their Net Distributable Cash Flow (NDCF) to unitholders, they retain very little cash for expansion. As a result, growth is usually financed through borrowings or equity issuance, such as Qualified Institution Placement (QIPs). This makes the debt profile an important aspect of REIT analysis. Investors should evaluate the leverage ratio, cost of debt, proportion of fixed versus floating-rate borrowings, and the debt maturity schedule. A well-managed debt profile helps protect profitability, especially during periods of rising interest rates.

Development Pipeline: Growth is not driven only by acquisitions. Many REITs also own under-construction projects or future development land parcels that are expected to become income-generating over time. This is known as the development pipeline. Investors should track the under-construction and future development area as a percentage of the REIT's total portfolio, as it indicates the potential for future growth. Once these projects are completed and leased, they start generating additional rental income.

Net Distributable Cash Flow: Finally, one of the most important metrics for a REIT is NDCF, as REITs are primarily cash-flow distribution vehicles. NDCF represents the cash available for distribution after deducting expenses, interest, taxes, and other adjustments. A stable and growing NDCF supports sustainable growth in Distribution per Unit (DPU) over the long term.

✦ **KEY TAKEAWAYS**

- Occupancy above 90% is generally considered healthy for office REITs.
- Rent escalations (~5%/year) and mark-to-market lease renewals drive organic rental growth.
- WALE shows how secure future rental income is — longer WALE means more predictable cash flows.
- Debt profile and Net Distributable Cash Flow (NDCF) are critical to assess the sustainability of distributions.

Capital raising

As per regulatory requirements, REITs are required to distribute at least 90% of their Net Distributable Cash Flow (NDCF) to their unitholders. As a result, REITs generally retain limited cash within the structure and need to raise capital separately for acquisitions, development funding. This capital can be raised either through debt or through the issuance of new units, such as through a Qualified Institutional Placement (QIP).

> *Note: Net Distributable Cash Flow (NDCF) is the cash available for distribution to REIT unitholders after adjusting rental income for operating expenses, interest costs, taxes, maintenance capex and other permitted items.*

Currently, listed REITs in India are able to borrow from banks and financial institutions at a rate of around 7.3% to 7.5%. However, REIT leverage is regulated, and the net debt to Gross Asset Value ratio is capped at 49%. This ensures that REITs do not take excessive leverage while pursuing growth.

This structure also creates a capital recycling opportunity for developers. Once a developer builds and stabilises a commercial asset, it can sell the asset to a REIT. The developer then receives capital from the sale and can use it to develop new assets. In this way, REITs provide developers with an efficient route to monetise completed assets, while investors get access to income-generating commercial real estate.

✦ **KEY TAKEAWAYS**

- Since REITs distribute 90%+ of NDCF, growth capital comes from debt or fresh unit issuance (e.g. QIPs).
- Indian REITs currently borrow at approximately 7.3–7.5%, with leverage capped at 49% of Gross Asset Value.
- REITs enable “capital recycling” — developers sell stabilised assets to REITs and redeploy the capital into new projects.

Regulatory Landscape of REITs in India

Minimum 90% of Net Distributable Cash Flow (NDCF) distribution: A REIT must distribute at least 90% of NDCF to unitholders. The same 90% distribution logic also applies at the SPV level, so cash moves upwards from SPV to REIT and then from REIT to shareholder.

Minimum 80% in completed rent-generating assets: At least 80% of the value of REIT assets should be invested in completed and rent-generating producing real estate. This protects investors from buying a disguised real estate developer. A REIT should mainly own mature lease assets.

Leverage cap 49%: REITs consolidated borrowings are capped at 49% of the value of REIT assets/ Gross asset value (GAV). If leverage crosses prescribe thresholds, additional safeguards may apply.

Note: Leverage ratio = Gross debt/GAV.

Minimum rental/leasing income requirement: REITs must derive a minimum portion of consolidated revenues from rental/leasing income. At least 50% of consolidated revenue should come from rental income, ensuring that the REIT remains primarily backed by income-generating real estate assets.

Independent valuation and NAV disclosure: REIT asset must be valued half yearly by an independent valuer, and NAV must disclose to unitholders on half yearly basis. Valuation is typically based on rental cash flows, occupancy, lease terms, cap rates and discount rates.

Tax structure of Distributions: REITs distribute income in different forms, such as dividend, interest and capital repayment. Of these, some components are tax-free in the hands of unitholders, while others are taxable. SPVs pay corporate tax on their taxable profits like normal companies. Once eligible income is passed from the SPV to the REIT and then to unit holders, it is generally not taxed again at the REIT level. This pass-through structure helps avoid double taxation of the same income before it reaches investors.

Distribution type	Tax treatment
Interest Income	Tax at slab rate
Dividend Income	Exempt only if SPV has not opted for Section 115BAA; otherwise taxable
Capital Repayment	Reduces cost of acquisition

Tax implications: Section 115BAA allows an SPV to opt for a concessional corporate tax rate; if the SPV has opted for this regime, dividend distributions from the REIT become taxable in the hands of unit holders.

Capital repayment is not taxed immediately, but it reduces the cost of acquisition of REIT units and will attract capital gains tax at the time of sale.

✦ **KEY TAKEAWAYS**

- REITs must distribute ≥90% of NDCF and hold ≥80% of assets in completed, rent-generating properties.
- Leverage is capped at 49% of Gross Asset Value; independent valuations are required half-yearly.
- Interest income is taxed at slab rate; dividends may be exempt or taxable depending on Section 115BAA; capital repayment reduces cost of acquisition and is taxed as capital gains on sale.

Who Should Invest in REITs?

REITs are suitable for investors seeking regular income along with moderate capital appreciation, especially retirees and conservative investors. They are also useful for investors who want exposure to real estate but do not want the hassles of directly buying, owning, maintaining and managing physical property. Through REITs, investors can participate in income-generating commercial real estate with smaller ticket sizes and better liquidity. REITs can also act as a good diversification tool, as their returns are driven by rental income and commercial real estate fundamentals, which are different from traditional equity investments.

✦ KEY TAKEAWAYS

- REITs suit income-seeking investors, retirees and conservative investors wanting real estate exposure with liquidity.
- They remove the hassle of directly owning, maintaining and managing physical property.
- REITs can aid portfolio diversification, as returns depend on rental income and real estate fundamentals rather than equity market moves.

Conclusion

REITs offer investors a convenient way to participate in income-generating commercial real estate without directly owning physical property. In India, the REIT market is still underpenetrated, while growth drivers such as rising GCC demand, healthy office leasing and a large pool of REIT-able assets provide long-term potential. However, REITs are not risk-free fixed-income products, as returns depend on occupancy, rental growth, interest rates, and cost of debt, leverage, asset quality and future capital raising. Overall, REITs are listed real estate investments that mainly provide regular income.

Frequently Asked Questions (FAQs)

What is a REIT?

A REIT (Real Estate Investment Trust) is an investment vehicle that owns income-generating commercial real estate, such as offices, malls and hotels. Investors buy REIT units on the stock exchange, and the REIT distributes at least 90% of its distributable cash to unitholders.

How does a REIT make money for investors?

A REIT collects rental income from its properties, pays operating costs, interest and taxes, and distributes at least 90% of the remaining Net Distributable Cash Flow (NDCF) to unitholders. Investors can also gain from any appreciation in the market price of REIT units.

How big is the REIT market in India compared to the world?

India's REIT market capitalisation is around US$21 billion, about 0.4% of India's total equity market capitalisation. Globally, REITs are worth approximately US$2 trillion and typically represent over 1% of equity market capitalisation, indicating significant room for growth in India.

What is WALE in a REIT?

WALE (Weighted Average Lease Expiry) shows, on average, how many years remain before a REIT's existing leases expire. A longer WALE means more predictable cash flows, while a shorter WALE can create mark-to-market opportunities if market rents have risen.

What is Net Distributable Cash Flow (NDCF)?

NDCF is the cash a REIT has available for distribution to unitholders after adjusting rental income for operating expenses, interest costs, taxes, maintenance capex and other permitted items. A stable, growing NDCF supports sustainable Distribution per Unit (DPU).

How much can an Indian REIT borrow?

REIT leverage is regulated: consolidated borrowings are capped at 49% of Gross Asset Value (GAV). Listed Indian REITs currently borrow from banks and financial institutions at approximately 7.3% to 7.5%.

Are REIT distributions taxable in India?

It depends on the component. Interest income distributed by a REIT is taxed at the investor's slab rate. Dividend income is exempt unless the underlying SPV has opted for the Section 115BAA concessional tax regime, in which case it becomes taxable. Capital repayment is not taxed immediately but reduces the cost of acquisition, attracting capital gains tax on eventual sale.

What occupancy rate is considered healthy for a REIT?

For office REITs, an occupancy rate above 90% is generally considered healthy, as it indicates stable rental income, stronger cash flows and greater visibility on future distributions.

What is the REIT-able potential in India?

India's four major office-led REITs together hold 132.2 msf, about 15% of Grade A office stock across the top seven cities. An estimated 415 msf of operational, REIT-able office space currently sits outside REITs, with Bengaluru holding the largest share at ~32.6%.

Who should invest in REITs?

REITs suit investors seeking regular income and moderate capital appreciation, including retirees and conservative investors, as well as anyone who wants commercial real estate exposure without the hassle of directly owning and managing physical property.
