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PE Players Switch Focus to Occupied Commercial Assets

Funds expect returns from such investments to jump 18-20% in 5 years

RAVI TEJA SHARMA
NEW DELHI

Occupied commercial buildings are the new favourites for private equity investors in the real estate sector. In a property market where developers are trying to manage cash flows to reduce debt and fund development projects, dedicated rental yield funds like IL&FS Milestone Fund and JM Financial Real Estate Income Fund have bought into such assets, while a few new funds are being raised to focus on this segment.

While the residential real estate market has seen sales slowing down, the commercial office market has been healthy, with many Indian corporates in the IT/ITES, BFSI, pharmaceutical sectors looking to expand.

According to consultant Cushman & Wakefield, in the last one year, Gurgaon has seen rentals go up by 5-10%, Bangalore by 10-15%, Chennai by 4-9%, Kolkata by 10-19% and Mumbai by 10-13%.

"We are looking at investing in AAA-rated properties with AAA-rated tenants, who will carry minimum risk," says Ramesh Jogani, managing director of India-reit Fund Advisors, which will launch a ₹800-crore rental yield fund in August this year. The fund plans to deploy the capital in a year and half to cash in on this opportunity that has opened up. "We believe commercial values are at an all-time low today."

Many Indian developers have a lot of debt on their books and are paying high interest on it. "They want to offload some of their assets," says Jogani. In May, DLF said it plans to sell some of its developed assets, including five IT Parks, to reduce its debt. It is currently in the process of selling its IT SEZ in Pune and an IT Park in Noida.

Sources of funds for developers have dried up in the last one-year as banks have become more cautious while lending to real estate companies and many developers have resorted to private financing at higher interest rates. Most developers though continue to

On A High



Percentage hikes in office rentals

CITY	(%)
Kolkata	10-19
Bangalore	10-15
Gurgaon	5-10
Chennai	4-9

NOTE: Increase in the last one year

hold on to their developed properties unlike in mature markets where they sell and develop new assets and not lock their money in rental assets.

In a recent deal, IL&FS Milestone Fund invested \$20 million in a leased commercial building, Patel Corporate Park, in Mumbai's Jogeshwari area. The building has a single tenant—Pfizer. Last year the fund had bought a 74% stake in HCC's 24x7 Park in Vikhroli for ₹575 crore. In May, another fund JM Financial Real Estate Income Fund bought PVR's Phoenix Mills theatre property for ₹100 crore in a sale and lease-back deal.

"These funds are more for investors who are lower on the risk side," says RK Narayan, director at Infinite India, which is raising a ₹500-crore fund—JM Financial Real Estate Income Fund—from domestic investors to invest in rent generating assets. Investing in such a commercial property will have three-pronged benefits— income from rents, rental appreciation and capital value appreciation. Capital values of such properties could also go up as interest rates come down over the next few years. Over a five-year period, returns from such investments could be in the 18-20% range and there is a fair amount of certainty. "Here, investors will get a regular income as well. In a development asset, you only get capital gain," he adds. Returns in development projects, of course, are higher but so are the risks.

In recent times, a number of corporates too are looking at selling their office buildings.

