

Fractional Ownership Platforms

Small and Medium REITs foster growth and transparency in India



Research

India

2024

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Introduction

The Indian real estate sector has been shaped over the past decade by a rapidly evolving regulatory landscape, which in turn has been driven by the need to enhance transparency and ensure consumer safeguards. A more regulated and organized market has borne fruit, as evidenced by the resilience and growth momentum visible across all asset classes. This transformation has further fueled the interest of retail investors who are increasingly recognizing the stability and attractiveness of real estate as an investment option, particularly during periods of economic turbulence.

Traditionally, high entry barriers in terms of the initial cost of ownership, limited market knowledge, and lack of expertise acted as stumbling blocks, especially when it came to evaluating investments in the more lucrative and stable rent-yielding commercial real estate sector.

This restricted the investor class to institutional investors, ultra-high net-worth individuals, and pension and sovereign funds.

However, the emergence of Real Estate Investment Trusts (REITs) and more recently, Fractional Ownership Platforms (FOPs) have democratized access to real estate for retail investors and now provide opportunities for portfolio diversification by enabling access to previously exclusive asset classes.

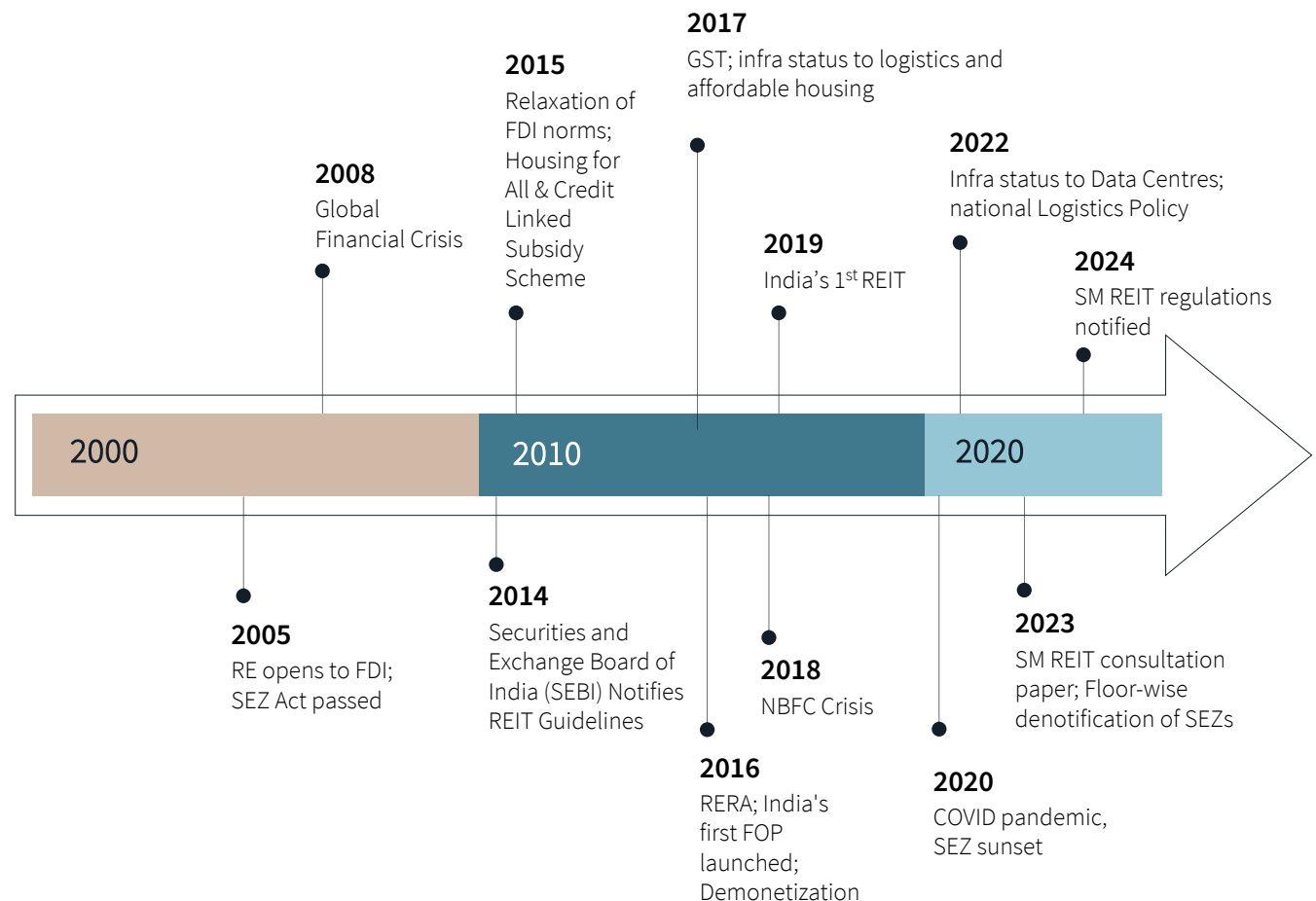
With the Securities and Exchange Board of India's (SEBI) intervention in the fractional ownership market to regulate the sector, this is an appropriate opportunity to delve deeper into the evolving landscape of fractional ownership in India. We explore the challenges and potential of fractional ownership, as well as the necessity for regulatory oversight to ensure organized growth of the market.



01

Last couple of decades have witnessed a measured march towards transparency

The transformation of India's real estate sector has been driven by a confluence of factors, with technological advancements, a maturing investment landscape and regulatory reforms like RERA, GST and REITs playing a pivotal role.



02

The proliferation of Fractional Ownership Platforms

Fractional ownership, as the name suggests, empowers investors to own a fraction or share of a physically undivided property, effectively lowering the entry barriers and enabling participation by a diverse investor base. Fractional Ownership Platforms (FOPs) act as process managers, streamlining the process. They form the formal channel that enables retail investors to tap into primarily pre-leased commercial real estate, including office spaces, warehouses, or even shopping malls, at a fraction of the total investment outlay. The cost of asset acquisition is split among several investors who invest in a specific asset-backed scheme under a Special Purpose Vehicle (SPV) established by the FOP. The investors earn returns in the form of rentals as well as long-term value appreciation of the property upon exit, with distributions made after the deduction of management fees and other maintenance expenses.

Over the past few years, the FOP market in India has experienced rapid growth, fueled by technological advancements and increasing investor interest in alternative investment avenues.

Size of the fractional ownership market based on Assets Under Management (AUM) of Fractional Ownership Platforms (FOPs)

USD 500mn

Property share emerged as the first FOP in India in 2016

Property Share and Strata are the two largest players in the fractional ownership space accounting for more than 50% of the market. Other players in the fractional ownership space are HBits, Assetmonk, ALYF, WiseX, YOURS etc. While most of them invest in rent-yielding commercial and warehousing assets, a few also offer residential properties under this model. Currently, office assets account for >90% of the market.

03

SM REIT regulations are a timely intervention

While FOPs proliferated, a critical aspect remained unaddressed – regulatory oversight was mostly ambiguous or absent.

As the market grew in size and retail investor interest rose, investment safeguards came under discussion. There were concerns related to lack of uniformity in disclosure standards, lack of transparency in valuation, management fees, maintenance costs and redressal of investor grievances.

To formalize this growing segment, the Securities and Exchange Board of India (SEBI) notified Small and Medium Real Estate Investment Trusts (SM REITs) through amendments made to the already existing REIT regulations.

The notifications now require every FOP who wishes to operate such investment schemes to be registered as an SM REIT and be licensed under SEBI.

Under the SM REIT regulations, the FOPs will now have higher compliance requirements related to issue size, asset exposure, investment portfolio, number of subscribers and minimum investment size. Also, such offerings now need to be listed on public exchanges and adhere to regular reporting and governance standards

04

Regulations address key aspects to safeguard investor interests

Key aspects of the SM REIT regulations

Investment manager responsible for setting up an SM REIT to have a net worth of at least INR 20 crore and at least two years of experience in the real estate industry or in real estate fund management



In an SM REIT scheme that has opted not to undertake leverage, the investment manager shall always hold at least 5% of the total outstanding units during the first three years. The minimum holding increases to 15% in the case of leveraged schemes



SM REIT schemes are not allowed to invest in under-construction or non-revenue generating real estate assets. At least 95% of the value of the schemes' assets must be invested in completed and revenue generating properties and the remaining 5% can be invested in unencumbered liquid assets



The size of the asset to be acquired in an SM REIT scheme should be at least INR 50 crores and less than INR 500 crores, with units to be issued to a minimum of 200 investors



Given the relatively nascent nature of the fractional ownership market, the minimum subscription size is kept at INR 10 lac. This is still lower compared to the earlier minimum size of INR 20-25 lac size set by FOPs. Moreover, as the industry matures, SEBI is expected to progressively reduce the ticket size, just like they did with 'big REITs'

05

Regulations to drive transparency & organized growth

The SM REIT regulations have created an enabling environment for active asset management and the potential to bring many income-generating small and medium-sized real estate assets under the purview of REITs. This not only offers a fresh avenue of funding for asset owners but also has the potential to improve transparency and market efficiency. As a result, regulatory oversight is anticipated to inject greater market participation from domestic as well as foreign retail investors, ultimately increasing liquidity in the Indian real estate market.

Investors holding units of SM REIT schemes will be entitled to similar tax benefits and a similar risk-reward spectrum as those investing in 'big REITs'

SM REITs can potentially bring in under-valued 'hidden gem' assets which can create investor value with better asset management

Importantly, the listing of SM REITs on public exchanges will lead to more efficient 'price discovery'. It will offer more flexibility to investors, allowing them to easily participate and exit with relative ease, without relying on FOPs for liquidity



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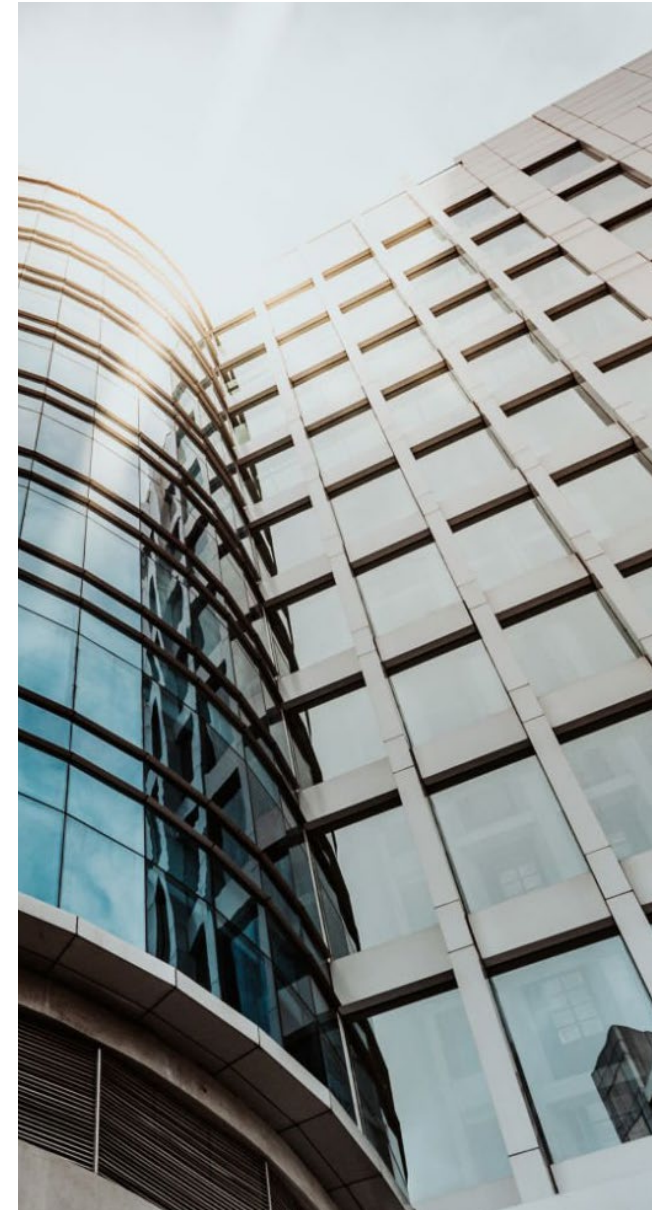
Immense growth potential in the SM REIT market

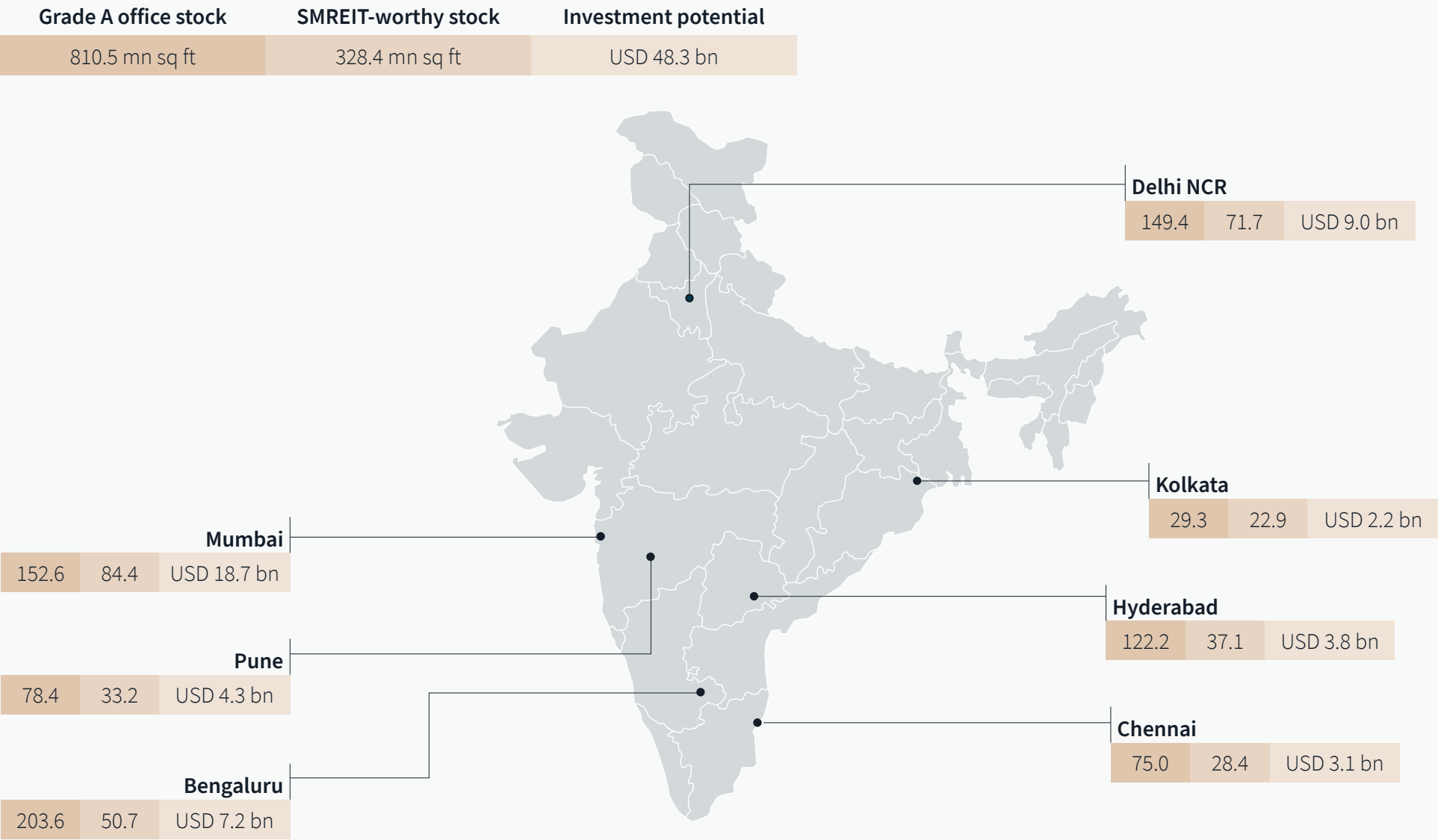
More than 40% of the overall Grade A office stock in the top seven cities of India, currently valued at ~USD 48 billion is SM REIT-worthy. This illuminates the promise and potential of this sector's burgeoning future. Markets like Mumbai and Delhi NCR offer the biggest opportunities for asset acquisition under the SM REIT umbrella, given the proliferation of smaller and mid-sized projects. Even the tech markets offer sizeable growth opportunities where well-leased but mid-sized assets are potential investment opportunities under SM REITs.

SM REIT Opportunity

328 mn sq ft

USD 48 bn





Note: Institutionally owned assets and assets under REITs were excluded. Of the remaining basket, those with a value of up to INR 700 crores and occupancy of >=95% were included; Average cap rate of 8% assumed to calculate investment potential

07

Fractional market to grow at an accelerated pace

SM REITs are expected to pave the way for a thriving fractional ownership market in India. The regulatory aspects will allow investors to approach this segment with greater confidence, given higher levels of disclosures and accountability. Additionally, technological advancements, improved transparency, smaller capital outlay requirements and growing investor interest for participation in a rapidly appreciating real estate market are expected to drive growth.

There are likely to be some initial compliance issues that the industry is expected to face during the initial phase of implementation of SM REIT regulations. Despite these teething issues, the market is poised to grow and potentially surpass USD 5.0 billion of AUM by 2030.

Today, U.S. public REITs own ~USD 2.5 tn of gross assets. Moreover, the REIT market in India grew from around USD 3.6 bn to USD 15.6 bn in Gross Asset Value within a span of five years. As the sector evolves on the regulatory framework backbone, we expect the fractional market to experience even faster growth

Size of the fractional ownership market

2023

USD 0.5bn

10x increase

2030

USD 5bn+

Looking ahead

Fractional ownership is still a relatively nascent market in India, driven by PropTech-enabled startup firms that offer retail investors a technology-driven investment solution for private investments in rent-yielding assets. However, a critical aspect remained unaddressed – regulatory oversight. While SEBI has addressed this aspect, challenges related to scalability and fostering investor trust remain, especially for newer SM REITs lacking a proven track record.

Despite these challenges, fractional ownership, with its inherent advantages of affordability, diversification, and opportunities for appreciation, is poised to become a mainstream investment option in India.

To support its growth, efforts should be focused on educating investors and stakeholders about

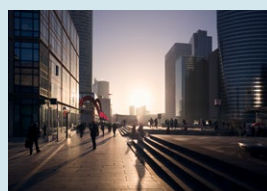
this investment model, enhancing digital infrastructure, and fostering collaboration between fractional ownership platforms, developers, and regulatory bodies.

Moreover, regulatory oversight will ensure a well-defined and secure environment, empowering individuals with varying investment capacities to participate in the institutionalized real estate market. Complementing ‘big REITs’, SM REITs or ‘micro-REITs’ are expected to expedite the journey of India’s real estate sector towards becoming more organized and institutionalized. This development will fuel the growth and advancement of the real estate sector, creating a win-win situation for investors, asset owners, and the economy as a whole.

As the market for SM REIT products evolves we are likely to see increasing share of other

asset segments. While office assets currently dominate, warehousing/logistics assets are finding increasing favour given the inherent rent stability associated with such assets. Going forward, there is possibility of SM INVIT regulations hitting the market to enable FOP ownership of regulated “infrastructure status” assets including logistics and warehousing. There are also platforms offering residential investment options – second homes, luxury villa/resort investment opportunities, given the rent as the potential for rent and capital appreciation. Income-generating assets across varying real estate segments are likely to be part of SM REITs going forward, further adding depth to the market while unlocking asset value accretion.

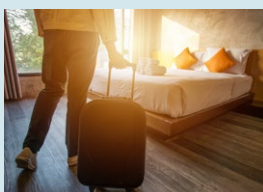
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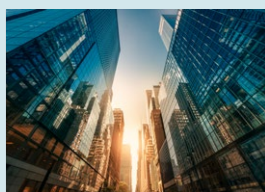
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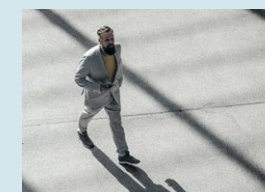
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About Property Share

Established in 2016, Property Share is India's first and largest technology driven real estate investment platform that allows sophisticated investors access to institutional grade assets with 8-10% in-place rental yields and 17-20% returns. The platform assumes complete responsibility of sourcing, due diligence, property management and sale on behalf of users making owning, managing and exiting commercial real estate simple and transparent.

Property Share was founded by Kunal Moktan and Hashim Khan. Kunal holds an MBA from the Indian Institute of Management (Ahmedabad) and as one of the founding members of Blackstone Real Estate Fund in India helped invest and manage c.\$1 billion of equity into Indian real estate. Hashim headed tech in a multi-billion-dollar middle eastern conglomerate and comes with >15 years of experience in managing and implementing complex technologies and processes. Hashim holds a B. Tech from IIT, Kanpur and an MBA from IIM Ahmedabad.