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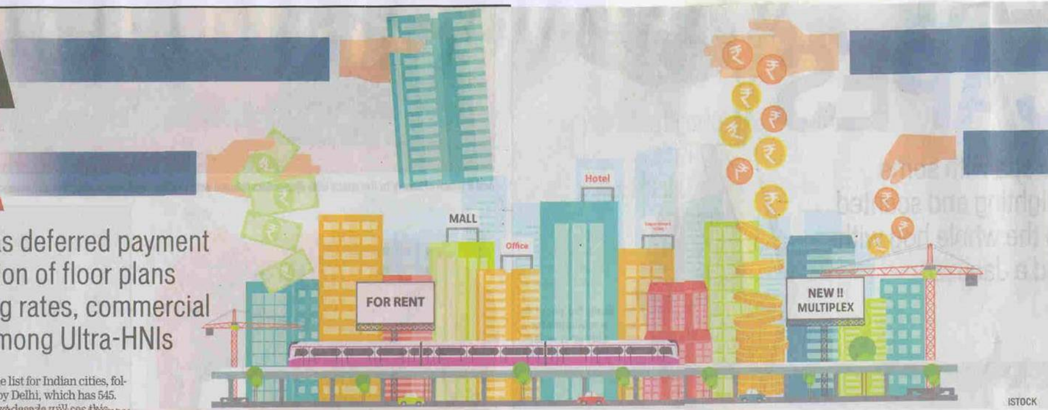
IT'S A DEAL

With benefits such as deferred payment policies, customisation of floor plans and attractive leasing rates, commercial real-estate is a hit among Ultra-HNIs



ISTOCK

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The Kumars and Salujas* live in New York and Toronto respectively. They are just seven hours apart, essentially the time one would take to drive down from Ahmedabad to Mumbai. Unaware of each other, they have one common interest — of investing in commercial properties back home.

In 2015, Sahej Kumar, a 41-year-old technology head in a New York-based multinational company, invested in a commercial space in Bandra. Similarly, earlier this year, 38-year-old entrepreneur Sanjeev Saluja, bought a 4,300-sq-ft office space in Airoli.

They are both planning to invest in more such properties next year.

Kumar and Saluja represent a growing tribe of ultra-high-net-worth-individuals or UHNIs. Realty consultancy Knight Frank defines this category as individuals whose net worth, excluding their primary residence, exceeds $30 million (about Rs 200 crore).

As per data released by Knight Frank, Mumbai is currently home to 1,094 UHNIs, topping the list for Indian cities, followed by Delhi, which has 545. The number rise to 2,243 in Mumbai and 1,128 in Delhi.

And then there are the non-resident Indians like the Kumars and Salujas, also eager to have a stake in the booming realty market back home.

As commercial spaces become more lucrative, many of these investors are beginning to consider investing in these projects too.

Over the past decade, 31% of Indian UHNIs increased their asset allocations to residential real-estate (primary or secondary homes). That number is expected to drop to 22% by 2025, according to a Knight Frank Wealth Report 2016, with more of these investors favouring the faster-moving commercial projects.

"The emerging trend, seen across the UHNIs, is of investing in commercial real-estate," says Samantak Das, chief economist and national director at Knight Frank India. "Over the next decade, we expect to see as much as 41% of wealthy Indian investors buy into commercial spaces, mainly because these spaces have shown year-on-year returns on investment that are higher than those in the residential sector. Commercial spaces are being seen as high-potential, with assured benefits in terms of rental and capital appreciation."

DRIVING THE GROWTH

One of the reasons for the spike in demand for commercial spaces is the unsold inventory in the residential sector. "The residential market was known to be a recession-free asset class until a few years ago, but in the past couple of years it has given in to market realities," says Anuj Puri, chairman and country head of realty consultancy JLL India. "Continuous rise in prices, in many cases faster than rise in incomes and inflation, resulted in homes starting to become unaffordable across major city centres."

In addition to that, 2015 proved to be a good year for key Indian metros in terms of inflows into real-estate by private equity (PE) funds. Total investment in the sector got was approximately Rs 19,500 crore, show data from JLL India. The Mumbai Metropolitan Region (MMR) received a massive chunk — 34% — of this investment, followed by Delhi-NCR (29%) and Chennai (14%). "While investors remain cautious about which cities to invest in, what is interesting to observe is that even for plain equity investments, core commercial assets are preferred over other asset classes," says Shobhit Agarwal, managing director of capital markets at JLL India.

VANTAGE POINT

The advantages of commercial real-estate investments is that they are generally secured by leases, which provide a regular income stream, as well as give investors the benefit of capital appreciation, says Shubhika Bilkha, business head at the Real Estate Management Institute (REMI).

"In India, rental yields from Grade A commercial properties are as high as 8% to 10%, which is significantly higher than the rental yields from residential properties," she adds.

Accordingly, the commercial real-estate market has witnessed a surge in demand from about 4 million sq ft in 2000 to 35 million sq ft in 2015. The year 2015 also saw $1 billion worth of leases signed.

"Much of this growth is being driven by the IT-ITeS, BFSI and consulting sectors and the surge in high-potential startups," says Bilkha. "With a gradual change in regulations that now protects landlords, as well as REITS entering the market in India, investors can now take advantage of an additional real-estate asset class."

> The emerging trend, seen across the UHNIs, is of investing in commercial real-estate because it promises rental and capital appreciation. Over the next decade, we expect to see as much as 41% of wealthy Indian investors buying into these spaces.
>
> SAMANTAK DAS, chief economist and national director, Knight Frank India, a real-estate research agency

Developers too are setting out to woo the UHNIs with commercial projects. "Given the existing inventory, builders are trying to attract investors with differed payment plans and customisation of floor plans," says Ravi Gurav, member of the developers' apex body, MCHI-CREDAI. "As a result of which small retail investors are showing a good response in the market and developers are anticipating turnaround in less than a year's time for such projects."

Experts and developers observe that there has been a decent price appreciation too. According to a research report released by auditors KPMG, prices of residential properties in Mumbai city and suburbs saw an appreciation of 3.3% in 2015, down from 7% in 2014. Commercial properties located in Grade A areas, on the other hand, have seen a growth of 8% to 10% with the range of options available to investors ranging from as little as 1,000 sq ft to as much as 20,000 sq ft per unit.

"What has worked for developers is the emergence of new business hubs, and the continuous improvement in infrastructure with the addition of new roads and flyovers that provide better east-west connectivity in Mumbai," says Maulik Sheth, director of construction company Sheth Corp. "An investor can look for a return of 20% to 25% on his investment in commercial projects, particularly in metro cities."

One of the biggest advantages of commercial real-estate are the attractive leasing rates, adds Dharmesh Jain, chairman and managing director of construction company Nirmal Lifestyle. "In areas where the amount of new construction is either limited by land or law, commercial real-estate can offer impressive returns and considerable monthly cash flow," he adds.

DOS AND DON'TS

Investors who are looking to diversify their property holdings by investing in commercial units should ensure that they understand the area and potential of the market in which they plan to invest.

"Commercial property yields are driven by their location in key industrial and commercial hubs," says Bilkha of the Real Estate Management Institute. "Accessibility to public transportation networks, the quality of construction and the underlying infrastructure of the area should be looked into before investing."

One should also consider that the uptake of commercial property is dependent on the overall growth of the economy and could see some impact or volatility in downturns or times of distress.

"The extent of financing is lower for commercial properties than the residential asset class, and the interest charged by financing institutions also varies and is higher for commercial assets," says Ravi Ahuja, managing director of investment sales and office agency at realty consultancy Cushman and Wakefield. "Also the tax benefits that are available for residential developments are not the same for commercial properties, thereby posing a hindrance to investors. Exiting commercial properties may be difficult too, due to fewer suitable buyers."

Das of Knight Frank advises that as a buyer one also check the type of office the space is going to be leased out to. "Rental values differ from an IT-ITeS office to a manufacturing or warehousing space," says Das. One must also consider the tenant profile, and the construction type — green, modern etc, he says.

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TAKING STOCK

- **Mumbai is currently home to 1,094 UHNIs,** topping the list for Indian cities, followed by Delhi, which has 545. The next decade will see this number rise to 2,243 in Mumbai and 1,128 in Delhi.
- **In India, rental yields from** Grade A commercial properties are as high as 8% to 10%, which is significantly higher than the rental yields from residential properties.

SOURCE: KNIGHT FRANK WEALTH REPORT 2016; REMI

It's a deal

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In order to get good rentals, investors should ensure that the property has good amenities such as parking space, backup power supply for lifts, fire safety measures etc. Investors should check the credentials and track record of the developer. "Also overall cost of investment in terms of stamp duty, registration charges etc. and ongoing expenses such as maintenance, property tax and building insurance should be considered closely," says Deep Kantawala, CFO at ICS Group, a real estate and financial services company. "Both have a direct bearing on the overall yield and returns on investment."

(Name changed on request)*