

## Bid for Long Term

Issue Details	
Price Band (Rs)	299 - 300
Issue Size(Rs)	4750Cr
Minimum lot	800 units
Minimum Investment	Rs. 2.40Lacs
Issue Opens	March 18, 2019
Issue Closes	March 20, 2019
Instrument Type	Non Convertible Bond
Listing on	NSE, BSE

Other Detail	
Global Coordinator and BRLM	Morgan Stanley India Company Private Limited, Kotak Mahindra Capital Company Limited, J.P. Morgan India Private Limited, DSP Merrill Lynch Limited
BRLM	Axis Capital Limited, Credit Suisse Securities (India) Private Limited, Deutsche Equities India Private Limited, Goldman Sachs (India) Securities Private Limited, HSBC Securities and Capital Markets (India) Private Limited, IIFL Holdings Limited, JM Financial Limited, Nomura Financial Advisory and Securities (India) Private Limited
Registrar to the issue	Karvy Fintech Private Limited

## EMBASSY Office Parks REIT

### Embassy Office Park REIT

The Embassy Office Park REIT (Embassy REIT) was incorporated on March 30, 2017 at Bengaluru as an irrevocable trust under the provisions of the Indian Trusts Act, 1882. It got registered with SEBI on August 3, 2017 as a real estate investment trust under Regulation 3(1) of the REIT Regulations having registration number IN/REIT/17-18/0001. The Embassy Sponsor and the Blackstone Sponsor are the sponsors of the Embassy REIT. Embassy Office Parks Management Services Private Limited (EOPMSPL) has been appointed as the Manager to the Embassy REIT and Axis Trustee Services Limited has been appointed as the Trustee. It is Asia's largest REIT in terms of space to offer as it holds property portfolio of ~33msf leasable area.

### Sponsors Background

**Embassy Office Parks** are Bengaluru based commercial infrastructure developer owning high quality office portfolio across Bengaluru, Mumbai, Pune, and Noida. They have developed over 45msf of area in the commercial and residential segments as of March 2018.

**The Blackstone Real Estate** is the largest real estate investment manager with \$119bn AUM as on June30, 2018. They have investments in North America, Europe, Asia, and Latin America. In 2011, they acquired 36.97% shareholding in Manyata Promoters Private Limited (MPPL), which holds Embassy Manyata. As per REIT Regulations, the Blackstone Sponsor had a net worth of Rs.24.46bn as on December 31, 2017 (minimum requirement is Rs.200mn).

### Issue Detail

The issue offers total 15.83Cr units at a price band of Rs.299-300 per unit aggregating to Rs.4734Cr at lower price band and Rs.4750Cr at the upper price band. The issue would constitute 20.5% of post offer paid-up capital. Net issue excluding part of strategic investor (2.92Cr units) would be of 12.91Cr units. Of the net issue, 75% (9.68Cr units) is reserved for QIBs, and the remaining 25% (3.22Cr units) is reserved for other investors. Minimum bid will be 800 units and in multiples of 400 units thereafter.

### Objectives of the Issue are:

- Proceeds to be utilized for the repayment or prepayment of debt to the extent of Rs.3700Cr
- Purchase an asset worth Rs.460Cr
- Remaining Rs.590Cr will be used for general and corporate purposes

### Outlook

Embassy REIT have strong Sponsors having global expertise in investment and asset management. In the past three years, revenue has grown at a CAGR of 7.5%. It is believed that a classy asset portfolio and marquee clients will help Embassy REIT maintain growth trajectory. According to the management, REIT will offer 8-8.25% yield for FY20, which is assumed to grow further by 8% p.a. It is the first REIT, which would be listed on Indian bourses. We believe it would provide predictable returns to unit holders over a longer term.

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## Investment Rationale

### • Real Estate Investment Trust

REIT (Real Estate Investment Trust) are long-term investment vehicles for real estates and own, operate, and manage a portfolio of income generating properties. These properties are mostly commercial assets such as office space, malls, industrial parks, hotels, hospitals, convention centres, SEZs, etc which are leased out for regular returns. Listed REIT are like mutual funds converting illiquid assets to liquid assets where small investors can also buy units of REIT getting ownership of commercial estate without actually buying any asset. These financial instruments are like bonds in nature and provide returns in form of dividend, interest, and appreciation in unit price. REIT provide better liquidity, transparency, returns, and risk mitigation compared with investments in real estates. REIT have Sponsor-Manager-Trustee structure. For Embassy REIT, Embassy Property Developments Pvt Limited and Blackstone are the Sponsors, Embassy Office Parks Management Services Private Limited is the asset Manager, and Axis Trustee Services Limited is the REIT Trustee. The Embassy REIT has been given a long-term rating of AAA by ICRA with Stable outlook.

### REIT compared with InvITs

In REIT, minimum 80% of assets have to be income generating properties with long-term rental contracts, which guarantees stable income and certain yield whereas in InvITs cash flows are uncertain. Underlying assets in REIT are self-owned whose value grows over time, and they usually have higher terminal value whereas in InvITs there is a concession period post which projects are returned or rebid for. REIT are better regulated with lesser political and regulatory risk. REIT are also required to pay-off at least 90% of the net distributable income at least twice a year.

### • Strong property portfolio

Embassy REIT asset portfolio is of 32.6 msf leasable areas comprising 7 office parks and 4 prime city-center office buildings having well-developed infrastructure such as food courts, gymnasium, amphitheater, sports facilities, childcare facilities, and public transportation. Overall, there are 75 high quality office buildings across 11 commercial locations. The portfolio also includes four hotels with total 1096 keys of which two are complete and the other two are under construction. They have 95% space leased to marquee tenants with built in contractual rent escalations of 10-15% in every 3-5 years. Moving ahead, the management expects at least 36% of revenue to come from contractual escalations for FY20 and FY21.

Asset Portfolio			
Particulars	Leasable Area (msf)	Market Value (INR mn)	% of Total Market Value
<b>Commercial Office</b>			
Bengaluru	14.5	138707	45%
Mumbai	2.1	50887	16%
Pune	8.9	45429	14%
Noida	4.7	27947	9%
<b>Investment Portfolio</b>			
Bengaluru	2.5	26067	8%
<b>Hotels</b>	1096 keys	14952	5%
Embassy Energy	100 MW	10820	3%
<b>Total Portfolio</b>	<b>32.7msf</b>	<b>314809</b>	<b>100%</b>

Source: Offer Document, ACMIL

### • Marquee Tenants

Embassy's high scale asset and quality service makes it a preferred choice for office space in premier locations. They have a tenant base of 160 + MNC of which ~43% are Fortune 500 companies. Average lease rent period is of seven years providing stable cash inflows. In the last 45 months, they have leased 6.8 msf of total office space with average re-leasing spreads of 48.0% on approximately 2.7 msf of re-leased space. Tenant retention has been maintained at 80.9% as 7.7msf of office space was renewed. Same Store Rental (SSR) CAGR during FY16-18 was 7.1% with high quality tenants.

Tenants				
Fortune 500 Tenants		Other Tenants		
Google	Microsoft	TCS	Yahoo	ATOS
IBM	Cognizant	L&T Infotech	Warbug Pincus	Blackstone
Goldman Sachs	JP Morgan	Tech Mahindra	Indian Hotels	Fiserv
Wells Fargo	PWC	Mercedes Benz	Shradul Amarchand	KPIT Technologies
Volkswagen	Accenture	Cisco	McKinsey	Crisil
NOKIA	Rolls Royce	Cognizant	DBS Bank	L&T Technology
Maersk	Legato	Access Healthcare	DHL Logistics	JBF Industries
Target	Lowe's	eClerx Services	Future Retail	Lintas India

Source: Offer Document, ACMIL

#### • Leading high barrier industry with sustainable initiatives

Embassy REIT have assets located in top office markets of Bengaluru, Pune, Mumbai, and Noida, which have strong market dynamics with highest absorption rate of 30%. These markets forecast healthy demand with increase in MNCs presence in India as they get ~85% lower cost structure compared to an average tier 2 city of USA. Embassy's high-class assets have created a high entry barrier for other developers as now acquiring and developing such scale of land property is not feasible. The management expects high demand from sectors such as IT, finance, E-Commerce, and services sector, which currently forms 72% of its tenant base.

The Embassy has established a 100MW solar plant at Bengaluru to supply green energy to its Bengaluru based properties. They also received Environmental, Health, and Safety Certifications such as ISO / OHSAS for select assets.

#### • Financials

During FY16-18, Embassy REIT's revenue and Net Profit grew at a CAGR of 6% and 66% respectively to Rs.17,663mn and Rs.2569mn respectively in FY18, maintaining double-digit margin. For 9MFY19, total revenue was Rs.14932mn with profit of Rs.2851mn (19% margin). Of the total gross rental revenue, ~81.4% comes from leading MNCs while 43.4% is from Fortune 500 companies. In the past six years, Embassy REIT rents have grown at a CAGR of 6.9% compared with market rent CAGR of 4.2% indicating the premium enjoyed by the REIT and is believed to continue with demand escalation. Embassy REIT has a debt of Rs.85,065mn as on December 31, 2018 providing a debt-to-GAV of 11%, which would improve as they will repay part of the debt from the issue proceedings.

### Taxation Benefits of investing in RITEs

#### Income received by REIT

Any income received by REIT in the form of dividends & interest from SPVs and rental & lease income from the properties held would be exempt from tax under Section 10(23FC)(a) of The Income Tax Act, 1961.

#### Income received by Unit holders of REIT

- Any income received by unit holders, in nature of **interest and/or rent** as per Section 115UA(1) of the act would attract TDS as per the below rates:
  - In case unit holder is a resident, 10%
  - In case unit holder is nonresident, 5% (plus applicable surcharge and cess). If the non-resident unit holder is entitled to a lower tax rate on interest under the relevant DTAA, the REIT may withhold tax at such lower rate.
  - For nonresident holders, rent income would be taxed at the rates in force as per section 194LBA(3) of the Act. If the non-resident unit holder is entitled to a lower tax rate on interest under the relevant DTAA, the REIT may withhold tax at such lower rate.
- Any distributions by the REIT **other than those referred above** (i.e., interest and/or rent) will not attract any withholding tax.
- Any distributions made by the REIT to the following unit holders should not be subject to any withholding tax:
  - Category I and Category II Alternative Investment Funds as per Notification No 51 / 2015 issued by Central Board of Direct Taxes
  - Mutual funds referred to in section 10(23D) of the Act.

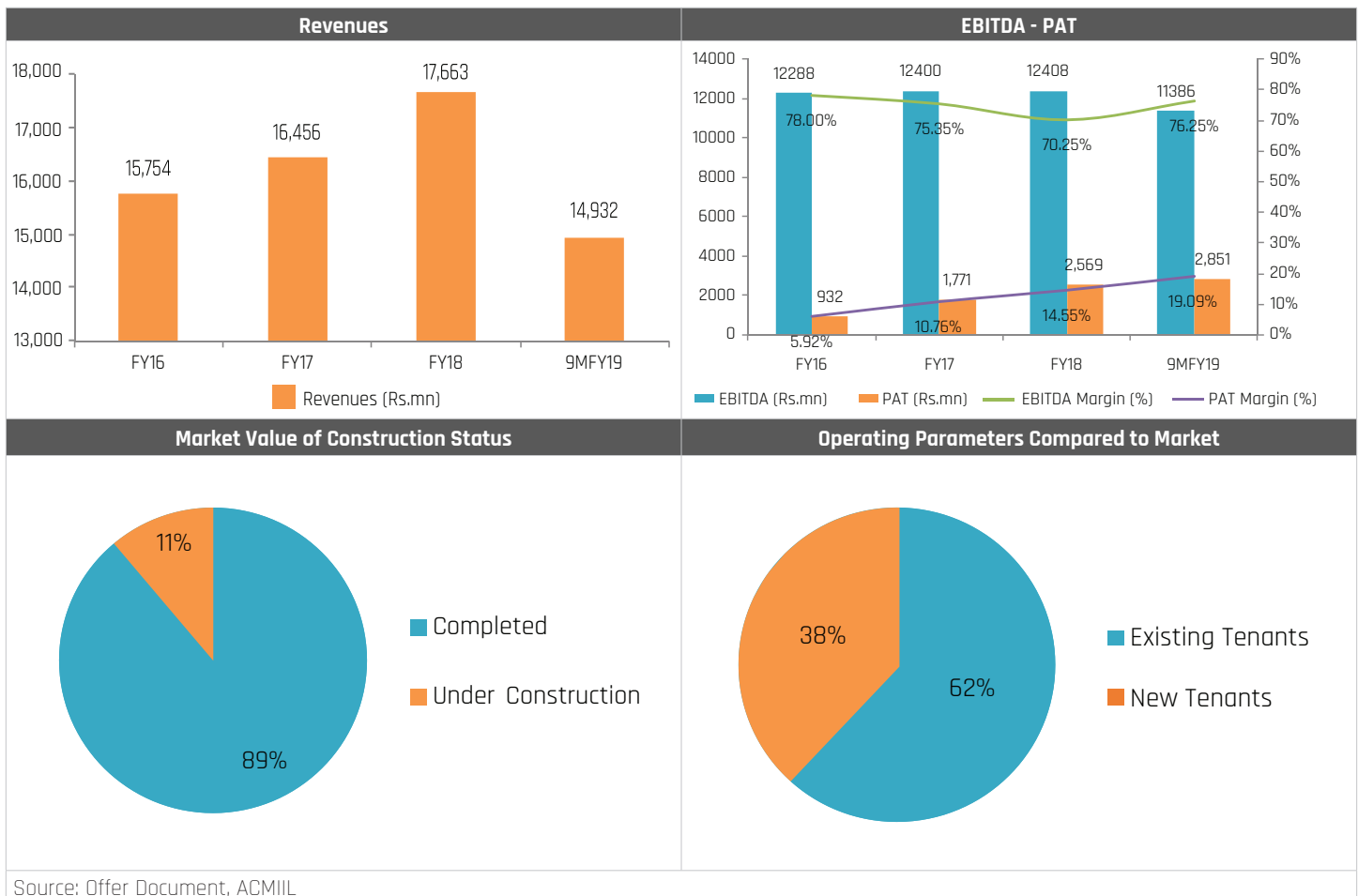
## Sale of units by the unit holders

After listing of units, further transactions (buying/selling) can be done of the units amounting to minimum Rs.1lac. Taxation while selling the units would be accordingly:

- No withholding tax would be applied in respect of capital gains arising from transfer of units to a resident or a nonresident which is a Foreign Portfolio Investor ('FPI') registered with the SEBI.
- Withholding tax may apply on capital gains arising to a non-resident who is not a FPI. Where such nonresident is entitled to benefits, including capital gains tax exemptions, under the applicable DTAA, it will have to furnish all the relevant documents / information to demonstrate his claim of taking DTAA benefits.

## Risks and Concerns

- **Economic Risk:** Any slowdown in the real estate sector might impact Embassy REIT space demand and rental income flow.
- **Dividend Yield Risk:** If they are unable to pay the said dividend, it will affect the unit holders' returns.
- **Business Risk:** Any slowdown or deviation in expansion plan would affect the top-line growth.



## Financials

### Income statement

Particulars (Rs.mn)	FY16	FY17	FY18	9MFY19
<b>Revenue from operations</b>	13,970	14,849	16,118	13,760
Other income	1,784	1,607	1,545	1,172
<b>Total Income</b>	<b>15,754</b>	<b>16,456</b>	<b>17,663</b>	<b>14,932</b>
<b>Expenses</b>				
Cost of materials consumed	42	49	55	42
Employee benefits expense	181	208	215	220
Operating and maintenance expenses	2072	2333	2069	1730
Other expenses	1171	1467	1720	1168
Impairment loss on property, plant and equipment	0	0	1195	386
<b>Total Expenses</b>	<b>3466</b>	<b>4057</b>	<b>5254</b>	<b>3546</b>
<b>EBITDA</b>	<b>12288</b>	<b>12400</b>	<b>12408</b>	<b>11386</b>
EBITDA Margin %	78.00%	75.35%	70.25%	76.25%
Finance costs	7083	6938	6312	5174
Depreciation and amortization expense	3158	3244	3228	2687
Profit before share of profit of investees and income tax	2046	2218	2868	3525
Share of profit of equity accounted investees	241	579	960	875
<b>Profit before income tax</b>	<b>2288</b>	<b>2798</b>	<b>3828</b>	<b>4400</b>
<b>Tax expense</b>				
Current tax	716	917	1,298	1,327
Deferred tax charge	1,163	716	745	320
MAT credit entitlement	-523	-606	-784	-98
<b>Total Tax Expense</b>	<b>1,356</b>	<b>1,027</b>	<b>1,259</b>	<b>1,549</b>
<b>Net Profit</b>	<b>932</b>	<b>1,771</b>	<b>2,569</b>	<b>2,851</b>
Net Profit Margin %	5.92%	10.76%	14.55%	19.09%

Source: Offer Document, ACMIIL

## Balance sheet

Particulars (Rs.mn)	FY16	FY17	FY18	9MFY19
<b>ASSETS</b>				
<b>Non-Current Assets</b>				
Property, plant and equipment	4,345	4,157	10,398	10,109
Capital work-in-progress	2,140	3,586	4,970	7,578
Investment property	63,951	62,731	66,611	67,653
Investment property under development	853	2,920	4,600	4,945
Goodwill on consolidation	8,105	8,119	8,119	8,119
Other intangible assets	2,860	2,838	2,912	2,846
Equity accounted investee	4,014	4,599	5,559	6,434
Investments	6,314	355	390	471
Loans	1,501	1,573	829	649
Other financial assets	1,804	1,904	2,048	2,754
Deferred tax assets (net)	201	343	542	566
Non-current tax assets (net)	872	894	923	1,246
Other non-current assets	959	3,908	8,103	8,455
<b>Total Non-Current Assets</b>	<b>97,919</b>	<b>97,927</b>	<b>1,16,003</b>	<b>1,21,825</b>
<b>Current Assets</b>				
Inventories	2,384	2,926	9	5
Investments	1,292	1,351	2,518	2,254
Trade receivables	400	363	378	371
Loans	595	1,276	9,278	8,084
Cash and cash equivalents	1,434	2,664	1,483	2,353
Other bank balances	280	1,062	696	260
Other financial assets	896	4,024	4,496	1,854
Other current assets	289	377	293	784
<b>Total Current Assets</b>	<b>7,571</b>	<b>14,042</b>	<b>19,153</b>	<b>15,966</b>
<b>Total Assets</b>	<b>1,05,490</b>	<b>1,11,969</b>	<b>1,35,155</b>	<b>1,37,791</b>
<b>Equity and Liabilities</b>				
Equity Capital	3,871	4,279	4,482	3,608
Instruments entirely equity in nature	8	8	9	0
Other equity	27,838	29,673	30,299	34,066
<b>Total Equity</b>	<b>31,717</b>	<b>33,960</b>	<b>34,789</b>	<b>37,674</b>
<b>Non-Current Liabilities</b>				
Borrowings	49,235	58,224	75,909	76,512
Other financial liabilities	2,778	3,081	2,813	2,794
Provisions	4	5	5	8
Deferred tax liabilities (net)	2,108	2,360	2,520	2,830
Other non current liabilities	650	711	648	696
<b>Total Non-Current Liabilities</b>	<b>54,775</b>	<b>64,381</b>	<b>81,894</b>	<b>82,841</b>
<b>Current Liabilities</b>				
Borrowings	1,450	29	3,551	3,249
Trade payables	469	289	417	173
Other financial liabilities	16,210	12,481	13,712	13,067
Provisions	0.21	0.25	0.33	2
Other current liabilities	792	814	765	652
Current tax liabilities (net)	77	14	27	132
<b>Total Current Liabilities</b>	<b>18,998</b>	<b>13,628</b>	<b>18,472</b>	<b>17,276</b>
<b>Total Equity and Liabilities</b>	<b>1,05,490</b>	<b>1,11,969</b>	<b>1,35,155</b>	<b>1,37,791</b>

Source: Company RHP, ACMIL

# Asit C. Mehta

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