

16/04/2002

Something new

LATELY, there has been some buzz surrounding real estate investment trusts (REITs). For example, on March 8, the Securities Commission (SC) issued a consultation paper on the subject to seek the public's response to issues and concerns raised in the document.

Eleven days later, the Association of Valuers and Property Consultants in Private Practice Malaysia (PEPS) held a two-day seminar to discuss the revitalisation of the property trust industry as a solution to the commercial property overhang.

The heightened level of interest is understandable. In his Budget 2002 speech, Prime Minister Datuk Seri Dr Mahathir Mohamad (who is also Finance Minister) advocated the establishment of REITs to facilitate corporate restructuring efforts.

It is clear that the wheels have been set in motion to make this happen.

The SC's consultation paper is meant to help the authorities formulate the relevant policies and strategies. The game plan has to be a good one because this is a matter whose impact will be felt on several fronts.

But first, it would be helpful if there is a consensus on the definitions of REITs and property trust funds. Many people treat these terms as interchangeable, and this has caused some confusion.

In a paper presented at the PEPS seminar, PEPS president Elvin Fernandez and ING Barings senior investment analyst Uday Jayaram say REITs and property trusts are 'essentially the same'. They define these as 'the pooling of investment funds in a company to invest in property investments, thus resulting in the equity securitisation of real estate'.

They point out that the current Malaysian regulatory framework uses only the term 'property trust'. They believe more and more people prefer to use 'REIT' because of the success of REITs in the United States.

On the other hand, the SC's consultation paper talks about both REITs and property trust funds, making it clear that they have different structures and legal statuses, without actually explaining how so. It is apparent, though, that the REITs that the SC is referring to do not exist in Malaysia, and the government intends to introduce them here.

When this happens, the property market will obviously be the first to experience changes. The hope is that the REITs will help shrink the property overhang, particularly commercial properties, and revive the sector.

PEPS says the REIT industry can be a white knight. 'The property trust industry has the capability to deepen the property market with its potential bond-like yields,' says Fernandez.

It is also likely that the REITs will somewhat alter the property business. As assets change hands, new players and new ways of doing things will emerge.

With REITs set to play a role in corporate restructuring (via acquisition of collateralised properties), the banking system's exposure to non-performing loans will lower.

Many participants in the local capital market are also closely following the initiatives to encourage the setting up of REITs. The introduction of these vehicles will lead to opportunities and options for investors and investment professionals.

For this to happen, there is much groundwork to do, starting with education. People should understand exactly what they are getting into

when they invest in REITs. The experience of the Malaysian property trust fund industry, which certainly needs a boost, is a good lesson. In fact, given this history, it may be hard to convince prospective investors to go for REITs.

A key factor is the tax treatment for the REITs. Because real estate investments are burdened by real property gains tax and stamp duty, REITs ought to be given appropriate tax reliefs so that they have more income to distribute. This way, it will be more attractive to invest in REITs.

(END)