"Brookfield India Real Estate Trust Q3 FY23 Earnings Conference Call"

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MANAGEMENT: **MR. ANKUR GUPTA – MANAGING PARTNER, BROOKFIELD ASSET MANAGEMENT & DIRECTOR, BROOKPROP MANAGEMENT SERVICES PRIVATE LIMITED**
MR. ALOK AGGARWAL – CHIEF EXECUTIVE OFFICER, BROOKPROP MANAGEMENT SERVICES PRIVATE LIMITED
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MR. SHAILENDRA SABHNANI – BROOKFIELD ASSET MANAGEMENT

Moderator: Ladies and gentlemen, good day, and welcome to Brookfield India Real Estate Trust Earnings Call for Q3 FY '23.

As a reminder, all participants' lines will be in the listen-only mode until the floor is open for questions. Should you need assistance during the conference call, please signal an operator by pressing '*' then '0' on your touchtone phone. Please note that this conference is being recorded. On the call, we have the following persons:

Mr. Ankur Gupta – Managing Partner, Brookfield Asset Management and Director, Brookprop Management Services Private Limited; Mr. Alok Aggarwal – Chief Executive Officer, Brookprop Management Services Private Limited; Mr. Sanjeev Kumar Sharma – Chief Financial Officer, Brookprop Management Services Private Limited; and Mr. Shailendra Sabhnani from Brookfield.

I now hand the conference over to the management. Thank you and over to you, sir.

Shailendra Sabhnani: Thank you. Good afternoon everyone and welcome to the Third Quarter FY '23 Earnings Call for Brookfield India REIT. We continue to deliver robust performance with around 1 million square foot of leasing year-to-date with around two-thirds being contributed from new leasing and the balance from renewals.

We have also achieved a 10% average escalation on 3.5 million square feet of leased area to date. Our occupancy has remained stable while achieving 9% NOI run rate growth over FY '22. And our NOI run rate as of December 22 which stood at 961 crores has a further embedded growth potential of 18% through a mix of new leasing, releasing and MTM potential that is well supported by a robust 2.2 million square feet leasing pipeline.

We also continue to evaluate select sponsor assets which will further grow the REIT portfolio inorganically. The balance sheet continues to remain robust with a 32% LTV AAA rating, which has enabled us to achieve highly competitive pricing. On the recent budgetary announcement, we are putting together a representation along with industry participants which my colleague Sanjeev will further elaborate upon.

With this, I will hand it over to Alok for a deep dive into the business updates. Thank you.

Alok Aggarwal: Thank you, Shailendra. A very good afternoon to everyone. I am pleased to announce that we have delivered another quarter of stable performance for our unit holders.

We have seen a consistent improvement in the physical occupancy at our assets in the quarter ending December comprising the holiday season in many organizations. Our assets have continued to witness physical occupancies of over 50%. This increase in physical occupancy is driving increased leasing inquiries. We continue to attract new tenants to our world class portfolio, and many of our existing high-quality tenants are looking to expand their footprint in our portfolio assets. Our leasing remains on track, and we have a healthy leasing pipeline.

During the last quarter, we leased 3,32,000 square feet comprising 2,41,000 square feet of new leasing, and 91,000 square feet of renewals. Additionally, we signed expansion options of about 40,000 square feet. The total leased area of the portfolio has remained stable at 11.9 million square feet, and we have maintained our Committed Occupancy at 83% and Effective Economic Occupancy at 88%. Our existing leases have delivered robust embedded growth with a 12% average escalation on 1.5 million square feet during the quarter.

In the last nine months, we have achieved gross leasing of 9,49,000 square feet with a healthy mix of existing and new tenants taking up space. Additionally, we have signed expansion options of 1,17,000 square feet and have a robust leasing pipeline with 2.2 million square feet of ongoing discussions. This should provide a further fillip to our leasing recovery. We have added many new office tenants into our portfolio in the year till date including Aristocrat Technologies, LTI Mindtree, and McGraw Hill.

Backed by robust cash flows from our underlying assets, the Board has approved a distribution of Rs. 5 per unit this quarter. We remain on track to achieve our H2 FY '23 and this year's guidance.

It has been one year since we completed the acquisition of Candor TechSpace N2. We are pleased with the leasing success we have achieved in this asset with the last new lease signed at a rental 15% higher than the income support rental of Rs. 60 per square feet. The newly completed tower at the asset - Tower 11A - has been 77% leased to Aristocrat, a leading mobile game developer. The balance 23% is available with them as an expansion option making the tower fully committed within seven months of completion.

ESG continues to be a key component of our overall strategy, and we continue to work towards a sustainable future with our target to achieve net zero by 2040. The scores we have received such as GRESB 5-star rating and the prestigious Golden Peacock Award bolster our faith that we are making meaningful progress and invigorates us to increase our efforts to create sustainable campuses. We remain closely connected with the community that we operate in. We recently launched the “Trees of Hope” campaign with the objective of providing education to children, which has seen a fantastic response from all our stakeholders.

The REIT has an attractive acquisition pipeline and is evaluating 6.5 million square feet across two assets: Candor TechSpace G1 in Gurugram and Downtown Powai in Mumbai. These acquisitions, if materialized, would help broad base the REIT and diversify our offering to our tenants.

Backed by our high-quality portfolio, we continue to remain focused on the path of value creation for our unit holders, and we continue our effort to deliver long-term value to our partners and communities.

Now I would like to invite Sanjeev to provide the financial updates. Thank you.

Sanjeev Kumar Sharma: Thank you, Alok. Good evening everyone. I am pleased to announce that we have achieved an NDCF of Rs. 168 crore or Rs. 5.01 per unit in quarter three of the financial year 2023 and are on track to achieve our full year guidance of Rs. 20.25 per unit. For the nine months of the financial year '23, we have already achieved an NDCF of Rs. 15.26 per unit.

The Board has approved the distribution of Rs. 168 crore or Rs. 5 per unit this quarter. With this, we have distributed Rs. 509 crores or Rs. 15.20 per unit for the nine months of the financial year 2023.

There were recent budgetary announcements regarding taxation of a component of distribution that accounts for around 50% of our current distributions. It is pertinent to note that apart from distribution, REITs provide capital appreciation driven by embedded growth drivers in the underlying assets, and the taxation on capital gains of REIT remains unchanged. We are examining the impact of the budget announcements, and along with industry participants, are evaluating next steps including making appropriate representation.

Our operating lease rentals for the quarter are Rs. 207 crore, which is 43% higher than the same period last year. The adjusted NOI for the quarter including income support from the sponsor group is Rs. 240 crore, which is 60% higher than quarter three of financial year 2022.

For the nine months of the financial year 2023, we achieved a 33% growth in our operating lease rentals at Rs. 616 crore and a 48% growth in our adjusted NOI at Rs. 716 crore, which is primarily driven by the addition of Candor TechSpace N2 into the portfolio and a significant improvement in our CAM margins over financial year 2022. The improvement in our CAM margins was driven primarily by some occupier moving to the higher hours of operation, and because of the higher physical attendance we have seen at our assets.

We continue to maintain a strong balance sheet with a 32% loan to value, and robust cash flows generated by our high-quality assets have ensured that our debt is rated AAA Stable, by CRISIL. This has enabled us to see a limited increase in the average interest rate to 7.95% as on 31st December 2022, which is 119 basis point increase in the interest rate during nine months of financial year 2023, as compared to a 225-basis point increase in the repo rate during the same period. With the highest credit quality and minimal refinancing risk, we have witnessed only a partial pass-through of the increase in benchmark rates to our borrowing costs.

Thanks everyone. With this, I would request the moderator to open the floor for Q&A.

Moderator: Thank you very much, sir. Ladies and gentlemen, we will now begin the question-and-answer session. The first question is from the line of Puneet Gulati from HSBC. Please go ahead.

Puneet Gulati: My first question is obviously with respect to the tax. So, you know, based on your assessment, what is the implication if the budget proposals go through? And secondly, what is the industry and you trying to do about it? And related to that, how does it impact the ROFO proposition?

Ankur Gupta: One, this is not applicable uniformly for everybody. So, let's just make that distinction to say that there is impact won't be a holistic answer. Second, we have heard a lot of commentary around that principal repayment to the REIT relates to not paying taxes. That repayment of principal, the way we have all learnt, happens from post-tax income, as applicable to the SPV. So, I think, there is a little bit of commentary that is required and there is confusion that needs to be plugged in. As Sanjeev mentioned, we are making representations to make sure the point is well established just like dividends are paid from post-tax income, that debt repayment on the principal side also happens from net operating profit after tax.

And then finally, the capital nature of suitable capital adjustment as it relates to principal payment are already in the code right now. So, on all three counts I would say that this needs clarification, and we have, as Sanjeev said, made representation or are going to make representations, because clarity is required.

Puneet Gulati: So, what does it do to the ROFO proposition, right? In case there is no change in the budget proposal, and it does get passed through, how does it impact the ROFO proposition?

Ankur Gupta: These are long term assets. You know, this is the product which has dividends; it has capital appreciation etc. So, I don't think fundamentally things change. Of course, it's not great if tax codes are tinkered with too frequently. India has a very robust REIT environment. We have learnt our regulations from the best places in the world. And I think clarification will come through is my understanding or at least my hope. To grow the REIT through acquisitions remains our strategy.

Puneet Gulati: So, just related to that, if I may, Ankur, since you are there, on the news article which related that Brookfield ROFO portfolio might get sold to GIC. Is that something that you would even evaluate or should we think that everything that Brookfield holds will ultimately flow into the REIT?

Ankur Gupta: I don't think it's fair for me to comment upon a media article here. But even in the presentation we put out and in the speaking notes that Alok just mentioned, Downtown Powai is being considered as part of the ROFO portfolio.

Puneet Gulati: My other two questions are just a bit on financial side. There was a positive impact of almost 309 million for this quarter. Are we likely to see more of this in the remaining year or all those reforms are done with now?

Sanjeev Kumar Sharma: So, Puneet, Sanjeev here. As you know how our tax regime works, the withholding tax gets deducted every quarter, and then in some quarters refunds come. So, over a period of time, it's tax neutral I will say, because in some quarters you will see negative where withholding tax is deducted. In some quarters, you will see refunds. So, it's a continuing process which will happen till perpetuity.

Puneet Gulati: For this year, is there more to come or are we done with fiscal 23?

Sanjeev Kumar Sharma: So, there are certain refunds in the balance sheet outstanding. We can't exactly comment on the timing whether we will be able to get those refunds in the current quarter, because we are only one quarter away from the year end or in the coming quarters.

Puneet Gulati: Can you also clarify how much of your unoccupied portfolio is SEZ now?

Alok Aggarwal: I would say, most of our vacancy right now is in the SEZ portfolio.

Puneet Gulati: And last, if I may squeeze in, there are some big expiries due in FY '24, especially from Kensington. Any update or color you want to give there?

Alok Aggarwal: I think we have mentioned in past, discussions have progressed well, and it's just a question of time, you know, we should be able to get confirmation from the tenant for further renewal and confirmation. We are advanced stage of discussions, a very advanced stage.

Moderator: Thank you. The next question is from the line of Kunal from Bank of America. Please go ahead.

Kunal: I just wanted to follow up on, you know, the developments that came through as part of the budget. Ankur, on the repayment of debt, is that representation about trying to get reversed or see what workarounds might be possible, you know, if you could clarify that one?

Ankur Gupta: The industry is making a joint representation. So, it's probably not fair for me to make my assessment, but as I said that there are clarifications rather than reversals that are required right now. Because, as I said, one is, there was, again, there is lot of chatter around that this was a channel or a "loophole" around taxation. That's not the case. So, that's the clarification required. And the existing code provide for dealing with such repayment of debt leading to distribution. So, I would say, it's a matter of the tax code of the country to be interpreted properly and clarifications required from the announcement made during the budget. But we have to wait and see how this plays out.

Kunal: And then on the SEZ part of it or the DESH Bill Mindspace was of the view that, again, the industry would start of talk about trying to make adjustments to the existing policy itself. So, do you have any thoughts there as to how fast could we see progress on this particular fact et cetera?

Alok Aggarwal: So, we had multiple discussions with the government and regulatory bodies. I think there is sufficient progress that has been made here, and that's the indication we have. Difficult to commit timelines, but there is sufficient progress that has been made. At the same time, you would have seen the lease of Aristocrat that we have done. We are re-pitching all our properties, and we see sufficient attractiveness for SEZ properties also. So, sufficient progress is being made with government, while it is difficult to commit timelines. I think it could take a few months more. At the same time, we are seeing interest also there for SEZ, and we continue to work with tenants for leasing of SEZ properties.

Kunal: And then the last one from me, your average rentals at Rs. 64, it basically feels unchanged over a span of 8 quarters I was wondering as to why should that be because you have been getting the escalations, is that mainly because of any sort of a mix change may be caused by N2 or anything else going on there?

Alok Aggarwal: So, we can look at the details, but of course we have seen lot of leasing in N1 and of course leasing in N1 we have kind of now gone from almost Rs. 52 to Rs. 63 so that is one reason where and when the leasing rental is lower.

Kunal: This should all be mix led is your guess correct?

Alok Aggarwal: Absolutely.

Moderator: Thank you. We will take our next question from the line of Srikarthik Velamakanni from Investec. Please go ahead.

Srikarthik Velamakanni: Just a quick clarification on the taxation changes in the budget in the current form will there be any benefit to the cost basis on the capital gains?

Ankur Gupta: If you could just clarify your question. We tried to clarify our position on the tax and as you would appreciate that we all have the same information, but if you could just clarify your questions then we will try to see what best we can do to answer that.

Srikarthik Velamakanni: If the principal repayment instead of being classified as principal repayment are classified as income. Earlier the cost basis would have been lower because now the capital gain component at least would be adjusted upwards. So, there will be lower capital gains and hence lower capital gains tax is that the right understanding?

Ankur Gupta: When we stated that there is existing law or tax framework to deal with the entire process means, and you are right that both cannot coexist. So, we would not be in a position to answer what part of it is the right answer because there is a little bit of confusion there and that is the clarification the industry has sought.

Srikarthik Velamakanni: So, just to clarify this effectively the outcomes are if they sort of roll this back then effectively our capital gains increase and if they do not then you get a benefit there, is that the right understanding?

Ankur Gupta: Your first part is probably the right understanding as it relates to the treatment before the recent announcement came in. So, I do not think anything changes on that front.

Srikarthik Velamakanni: The second question is what percentage of our operating assets are classified as SEZ and could you also quantify what percentage of that area is vacant currently?

Alok Aggarwal: So, out of portfolio, N1 is non SEZ other assets are SEZ and as we have mentioned that 90% of the vacant area is in SEZ.

Srikarthik Velamakanni: And are you also looking to selectively de-notify some of this depending on obvious approvals there?

Alok Aggarwal: Yes subject to approvals we can look at it if it is accretive for us we can look at it, but right now you can de-notify new buildings, but not the old or occupied building that probability is not there.

Srikarthik Velamakanni: And lastly the way you have mentioned your NOI growth over a Q4 base the way to interpret this is of course that 9% absolute growth so far is effectively annualizing to 12% to 13% on a full year basis, is that the right interpretation out here?

Ankur Gupta: I do not think that is the right interpretation it is comparing run rate to run rate. So, the right interpretation is if we extend that to 18% potential this portfolio has a stabilized potential of more than 1,100 crores of income per year.

Moderator: Thank you. We just have a question from Sameer Baisiwala from Morgan Stanley. Please go ahead.

Sameer Baisiwala: Couple of questions one is if you can just talk about what does 18% embedded NOI growth over a period of time can translate into DPU growth?

Shailendra Sabhnani: Sameer we have just talked about the NOI growth that we see from here on a run rate basis to stabilization. I think DPU will be a factor of some other aspects as well as financing etc., you may probably make assumptions with respect to other factors, but otherwise this is broadly how we think NOI shaping up as we continue to look at the portfolio stabilizing.

Ankur Gupta: In other words, Sameer, this requires almost little capital investment all of this should ultimately flow to the DPU.

Sameer Baisiwala: So, what you are suggesting is that your DPU growth should broadly track NOI growth going forward?

Ankur Gupta: Yes there is about 15% to 20% embedded growth in DPU potential of the existing operating portfolio.

Sameer Baisiwala: And the second question I had was taking from your press release that you have achieved 10% average escalation on 3.5 million square feet of leased area 9 months if you can just talk about it I mean normally it would be 15%, but is there any one-third of the leases being on annual escalation is that driving it if you can just talk about this?

Sarthak Patel: Our escalation in the Kensington Asset are typically an annual escalation of 4.5% to 5% and the Candor Assets typically have a 15% escalation every 36 months. So, a blended average of that in the last 9 months is the 10% figure which you see.

Sameer Baisiwala: That is very clear so there is no change to 5% and 15% it is just a mix thing and sir the page on the inorganic options so G1 rentals are Rs. 75 is curious, is this the market rate in that neighborhood or is it very highly under indexed?

Alok Aggarwal: So, you are talking about G1 so this is the in-place rent and of course some of the leases have been signed earlier. Of course, today when we look at leases could be happening at about 15% to 20% than more rental than what is in-place rent.

Sameer Baisiwala: Which means if and when this assets comes in we will come with a fair bit of mark-to-market up selling so that is what I was trying to get?

Alok Aggarwal: Yes absolutely.

Sameer Baisiwala: Sir one final question from my side is on the CAM recovery how does this work and is there now at 50% physical occupancy are you pretty much there or you think there is some more scope for CAM to go up?

Sanjeev Kumar Sharma: Normally our CAM is cost plus margin basis. So, whatever we incur in the expenditure the margin is added and recovered. With the physical occupancy of 50% there is reasonably good headroom for CAM income to increase. If you just go to our slide number 13 where we have shown the organic growth potential where we are talking of increase of 18% in our NOI, 30% to 35% potential of increase is in the CAM margin itself is there in our portfolio when we will get stabilized NOI.

Sameer Baisiwala: I think you just talked a fair bit about the budget announcement, but just one more this is going to be if it goes through it is going to be applicable from 1st April 2024 so you would have say five quarters, is there anything that you can do to mitigate the impact?

Ankur Gupta: We are not sure that is the right understanding.

Shailendra Sabhnani: Sameer this is applicable from AY 24 which means it would be next FY so applicable from 1st of April next year.

Moderator: Thank you. Our next question is a follow up from Puneet Gulati from HSBC. Please go ahead.

Puneet Gulati: So, this is effective for FY24 if it goes through for your FY24 income will be subject to this taxation or FY24 distribution?

Ankur Gupta: Distribution mainly.

Puneet Gulati: Can you give some chance of what is the achievable rents for all of your four locations currently?

Ankur Gupta: Is there a specific question on a particular asset because we have stated the market trend versus in place et cetera, but happy to answer any particular question.

Puneet Gulati: So, like-to-like for each of the five assets that you have if you can give some sense of where those leasing rents are moving currently?

Alok Aggarwal: Let me talk about what the leases we have signed in last 6 months so let us take N1. Today, in N1 we are crossing 62, 63 or even touching 65, 68 for smaller spaces that is the kind of a number we are achieving. N2 now we have closed something at 70, but I think 65 is the rent that we have got in last 3 to 4 months. When we talk about G2 it can be around 90; for smaller space could be 90 plus, for larger space could be slightly lower than 90 so that is where we are on G2. On Kolkata what we are hoping is to sign something maybe in mid 40s anything between 43 to 45 and Mumbai can vary between 120 to 125.

Puneet Gulati: So, there has not been any meaningful increase in the market rentals per se over last quarter that is the message I should give?

Alok Aggarwal: I think if you really look at Noida which were mid-50s to 60s now we are crossing 62, 63 which is N1. N2 we were signing around 60 we have crossed 65 there, Gurgaon we continue to range between 90 to 95, Kolkata now we are around mid-40s again increased of course something has to materialize in short time and Mumbai is around 120, 125 which we have indicated earlier.

Moderator: Thank you. So, that was the last question. Over to you, Mr. Ankur Gupta for closing comments.

Ankur Gupta: Thank you everybody for your participation today and we look forward to getting back in touch with you shortly. Thank you, have a good evening.

Moderator: Thank you members of the management. On behalf of Brookfield India Real Estate Trust that concludes this conference. Thank you for joining us and you may now disconnect your lines.