

# Real Estate Investment Trusts (REITs) in India: A Capital Market Innovation at Crossroads<sup>1</sup>



**Prof. Venkatesh Panchapagesan**  
*Chairperson*  
IIM Bangalore Real Estate  
Research Initiative



**M. Mareeswaran**  
*Research Fellow*  
IIM Bangalore Real Estate  
Research Initiative

Real Estate Investment Trusts (REITs) are regulated investment vehicles that own, operate, or finance income-producing real estate. Modeled after mutual funds, REITs allow both retail and institutional investors to access the returns of real estate assets without directly owning or managing physical property. For the former, it is also about being able to get exposure to real estate at affordable ticket sizes. Globally, REITs have emerged as an important channel for capital formation in the real estate sector, offering investors a combination of regular income and capital appreciation.

REITs were formally introduced in India in 2014, with the first public listing—Embassy Office Parks REIT—taking place in 2019. As of 2025, India has four listed REITs, primarily focused on commercial office assets, and a growing investor base exceeding 500,000 unit holders. Despite their success in democratizing real estate investments and enabling infrastructure monetization, Indian REITs still face regulatory and structural constraints that limit their broader integration into equity markets.

## REIT as an Asset Class

REITs are designed to serve as income-generating, low-volatility instruments within an investor's portfolio. Their core value proposition lies in:

- **Regular dividends** from rental income, distributed quarterly or semi-annually.
- **Capital appreciation** through rising property valuations and rental escalations.
- **Liquidity**, since listed REIT units trade on stock exchanges.
- **Diversification**, as REIT portfolios typically include multiple properties across geographies and tenants.

Over the last five years, Indian REITs have delivered annualized returns of around 13%, with a relatively stable risk profile compared to traditional real estate or equity assets.<sup>2</sup> Importantly, REITs offer a bridge between real assets and public markets, converting illiquid property investments into liquid, tradable securities.

REITs provide regular, mandated fixed payouts like debt, sourced from real assets that provide security, much like in a debt instrument. But they also have features that make them behave more like equity.

- **Risk exposure:** Similar to a business underlying an equity, REITs are subject to business cycle risks and provide growth options for bearing those risks, like equities.
- **Residual economic interest:** Like equity holders, who have residual equity interest in the underlying business, REITs holders also carry the residual economic interest in the underlying real estate properties.
- **No Repayment obligation:** Unlike debt securities, REITs are not obligated to repay the funds raised. In other words, there is no return on principal that investors can expect like in equities.
- **Unit holding dilutions:** Any additional issuance of units shall dilute the cash flow rights of existing unit holders similar to equity shares.
- **Voting rights:** Unit holders enjoy voting rights similar to equity shares.
- **Liquidity:** REIT holders enjoy the same liquidity rights as equity investors as they are also traded in stock exchanges.

In performance too, REITs behave much like equities. Here is a table that compares their performance with those of real estate companies in the Nifty Realty Index.

Metric	Indian REITs (Average)	Nifty Realty Equities (Average)
Annualized Return (5Y)	~13%	~16%
Dividend Yield	6-7%	<2%
Volatility (Standard Deviation)	~9-11%	~18-22%
Sharpe Ratio (5Y, risk-free =6%)	<b>0.78</b>	<b>0.45</b>

In many ways, REITs actually provide a superior **risk-adjusted performance** than listed real estate equities in India.

As a side experiment, we looked at the largest REIT (Embassy) with similar, but non-real estate, companies in the Nifty 500 index. The market capitalization of Embassy REIT is around Rs. 37,850 crores today. A whopping 280 firms in the Nifty 500 have a lower market capitalization than that of Embassy REIT. To make meaningful comparisons, we created a control group of 30 firms in the Nifty 500 within 10% of Embassy REIT's market capitalization. While these firms provided a dividend payout ratio of 22.8% and carried a leverage of 2.8, Embassy REIT had a much higher dividend payout ratio of 136% and a lower leverage of 2.12.<sup>3</sup> In many dimensions, REITs outperform, not just real estate equities, but many of the equities that are currently included in our equity indices. Then why are they not in any of our equity indices?

Since REITs sit between debt and equity in terms of risk-return characteristics, SEBI has played it safe and classified them as **hybrid** instruments rather than as equity-related instruments.<sup>4</sup> This has led to much of its benefits being locked up and not made accessible to most of retail investors - the investor group that SEBI should really care about. In this, SEBI stands alone, as much of the world around us have gone the other way.

## Global Treatment of REIT

Globally, REITs are treated as equity, both in legal classification and in index inclusion. This consistent treatment has facilitated the growth of large, liquid REIT markets:

- In the United States, the REIT model has flourished since the 1960s, with 162 listed REITs and a total market capitalization exceeding \$1.3 trillion.
- In the United Kingdom, REITs comprise 93% of the listed real estate market.
- In Singapore and Australia, REITs are core components of both retail and institutional portfolios, often included in national and regional equity indices.

REITs in these jurisdictions are embedded within the equity market infrastructure: they are listed on major stock exchanges, eligible for inclusion in equity mutual funds and ETFs, and regularly appear in benchmark indices such as the S&P 500, S&P 1500, Russell 1000 and Russell 2000. In the U.S., REITs have been included in the S&P 500 index as early as in 2001. This has allowed both passive and active index funds and ETFs to include them in their portfolios, making them part of the investment universe for millions of ordinary citizens. No wonder do REITs represent more than 98% of the listed real estate market capitalization in the US as compared to a mere 10% in India.

Crucially, REITs in these markets are not viewed as hybrid or debt-like instruments. Instead, they are treated as specialized equities with high payout ratios, making them especially attractive in a low-interest environment. Moreover, the lower volatility of REITs—thanks to their income visibility and stable tenancy structures—makes them attractive to conservative or income-seeking investors like retirees and pension funds.

At the macro level, several global research studies have shown that inclusion of REITs improves portfolio performance across a wide set of metrics.<sup>5</sup> An Oxford Economics study in 2019 demonstrated that including REITs broadens the efficient frontier (higher return with lower risk) of optimal portfolios made with just traditional assets like stocks, bonds and commodities.<sup>6</sup> Their low correlations with stocks and bonds make them appealing for investors seeking diversification and hedging in financial markets.

## Unintended Consequences of Classifying REIT as Hybrid

The hybrid classification of REITs in India has led to several unintended consequences.

### a. Exclusion from Equity Indices

As mentioned before, REITs are not included in Indian equity indices because SEBI does not consider them as equity. This means that there is no participation from index funds and ETFs that track these index funds. Like everywhere else in the world, passive investing is growing in India and is almost a fifth of all mutual fund assets now.<sup>7</sup> This means that a substantial group of investors are simply shut off from this value enhancing instrument because of our regulatory outlook. Moreover, long-term regulated investors like EPFO cannot invest in REITs as they are not part of the equity ETFs, even though they could benefit immensely from REITs' superior risk-adjusted returns.

Ironically, Indian REITs are included in global sectoral equity indices such as FTSE, MSCI and S&P making them accessible to international passive investors seeking Indian realty exposure while our own passive investors do not have access to them.

### b. Low Mutual Fund Participation

SEBI periodically mandates the extent of investment in REITs (and in InvITs) by active mutual funds. Currently, debt, equity and hybrid mutual funds can invest up to 10% of their AUM in REITs/InvITs, and not more than 5% in a single REIT. A recent consultation paper of SEBI suggests increasing this limit to 20% and 10% respectively.

While this seems like a good move, it hides the fact that active funds invest far less in REITs than what their current limit allows them to. Active funds invest a fifth of their allowable limit (around 2%) in REITs today.<sup>8</sup> Active funds are free to choose where to invest as they seek to maximize the risk-adjusted returns for their investors. If they are investing less in REITs, then it must mean that REITs are less attractive to their other investable options. Increasing the limit in such circumstances would be useless as the current limit itself is not binding. Interestingly, the average active allocation in S&P 500 benchmarked funds in the US, a country with no regulatory cap on REIT exposure, is also about 2.5% of AUM, much like their Indian counterparts.<sup>9</sup>

If SEBI is keen to increase the attractiveness of REITs for active funds, it should allow them to be included in the equity indices. Once passive investor flows are assured, issues such as poor liquidity and price-to-NAV discounts will recede for REITs, making them attractive to active funds for their risk-return characteristics, like how it is in global markets.<sup>10</sup> Regulatory caps would not be necessary then as the funds' mandate, diversification rules, and the tax strategy, would dictate their actual allocations.

## Conclusion

REITs represent a powerful tool to mobilize long-term capital into India's real estate sector while offering investors access to high-quality, income-generating assets. However, their regulatory classification as hybrid instruments has constrained their integration into mainstream capital markets.

Global experience demonstrates that REITs, when classified as equity instruments, can thrive as core components of investment portfolios and major contributors to financial markets. SEBI's recent consultation paper asking public views for considering them under equity-related instruments is a welcome step in the right direction. This change, if implemented, will unlock broader participation, deepen market liquidity, and align Indian REITs with global best practices—paving the way for REITs to fulfill their true potential in India's growth story. Our country can immensely benefit from redirecting speculative investments in physical real estate into the more productive, financial real estate products like REITs.<sup>11</sup>

<sup>1</sup> Though the article focuses on REITs, all the key issues discussed here equally apply to Infrastructure Investment Trusts, or InvITs, as well.

<sup>2</sup> <https://www.reitspro.com/historicalreturns#:~:text=REITs%20and%20InvITs%20are%20capable,per%20annum%2C%20on%20an%20average.>

<sup>3</sup> Leverage is Total Liabilities over Shareholder's Equity.

<sup>4</sup> Equity related instruments include convertible debentures, convertible preference shares, warrants carrying the right to obtain equity shares, equity derivatives, under the SEBI (Mutual Funds) Regulations, 1996.

<sup>5</sup> <https://www.nature.com/articles/s41599-025-04715-0>

<sup>6</sup> <https://www.oxfordeconomics.com/resource/listed-real-estate-in-a-multi-asset-portfolio-a-europeanperspective/>

<sup>7</sup> <https://economictimes.indiatimes.com/mf/mf-news/passive-investing-booms-mutual-funds-cross-rs-10-lakhcrore-aum/articleshow/112687323.cms?from=mdr>

<sup>8</sup> [https://www.sebi.gov.in/reports-and-statistics/reports/apr-2025/consultation-paper-on-investment-by-mutual-funds-in-reits-and-invits\\_93488.html](https://www.sebi.gov.in/reports-and-statistics/reports/apr-2025/consultation-paper-on-investment-by-mutual-funds-in-reits-and-invits_93488.html)

<sup>9</sup> <https://www.reit.com/news/blog/market-commentary/real-estate-and-reit-allocations-generalist-funds-trendinghigher>

<sup>10</sup> <https://www.avendus.com/india/avendus-eye/reits-tapping-into-india-s-real-estate-potential>

<sup>11</sup> Speculation in physical real estate leads to vacant land and apartments, which, in turn, leads to higher prices and reducing affordability for most Indians.