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Realty reforms to boost offshore funds' optimism

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While clouds of uncertainty shroud the real estate sector, our discussions with offshore real estate funds present a rather optimistic picture, even as they remain in wait and watch mode for the next quarter or two. We believe the optimism is based on broadly the following three drivers.

First, the routes for foreign investment in real estate companies have been substantially liberalised. On the one hand, almost all sectoral restrictions for foreign direct investments have been relaxed. On the other hand, substantial relaxations for raising foreign debt have also been provided for. Indian real estate companies that hesitated listing their securities can now raise foreign debt by issuing unlisted debentures to foreign portfolio investors. Offshore funds get tax optimised redeemable instruments with security interests without any coupon restrictions.

Second, SARFAESI benefit which was hitherto available only to banks and financial institutions has now been extended to even offshore funds through the local debenture trustees. This is a huge give away by the government, which affords significant leverage in terms of enforcement of security interests, which has otherwise been criticised as a toothless protection.

Third, the Real Estate Regulation Act, which is scheduled to be effective in most states from March 2017. With 70% of the revenues escrowed for development costs and the requirement to complete the construction in a time bound manner, there is assurance on usage of proceeds and timely delivery. Though standard investor protections like step in rights and enforcement of security interests could now be called into question (since any change in the 'promoter' or developer will require prior approval of 2/3 allottees and the regulator), offshore funds tend to respect the discipline that RERA seeks to bring in.

These regulatory changes are likely to imbibe ethical behaviour and streamline the market to large and serious players - an environment most conducive to offshore funds. It's wait and watch for the next few months, but India is slowly climbing up the ladder of priority in the list of global private equity funds.

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