The Launch of China REITs

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4. REITs in SSE
Introduction To China REITs
1.1 Basic Concepts and Market Capacity

REITs (real estate investment trusts) pool the capital of investors by offering income securities and have specialized investment institutions to carry out real estate investment, operation and management. The investment income will be allocated to investors at a relatively high proportion.

“Quasi-REITs” in China are privately traded and lay the foundation for the launching of C-REITs in China. Since 2014, a total of 90 Quasi-REITs have been issued in China, with total amount of RMB171.5bn. Quasi-REITs invest in real estate properties, including office buildings, logistics and warehouse, commercial complexes, rental housing, roads and hotels.

C-REITs are REITs with infrastructure as the underlying assets instead of commercial or residential real estate. C-REITs convert infrastructure projects with low liquidity into high liquidity shares. Featuring public issuance, medium risks, high liquidity and stable returns, C-REITs are a new investment instrument that is between stocks and bonds.

NDRC: C-REITs have promising future in China, and the market size is at least in trillions of RMB

Experts: It is estimated that the potential market size of C-REITs can be more than RMB 5tn (calculated based on the existing infrastructure assets of >RMB130tn in China and a REITs-rate of 4% in mature markets)

<table>
<thead>
<tr>
<th>Country /Region</th>
<th>Existing REITs: Dec. 31, 2020</th>
<th>REITs Offerings: 2020</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Market Cap ($bn)</td>
<td>Amount</td>
</tr>
<tr>
<td>US</td>
<td>1.268.41</td>
<td>248</td>
</tr>
<tr>
<td>Europe</td>
<td>211.09</td>
<td>261</td>
</tr>
<tr>
<td>Japan</td>
<td>54.84</td>
<td>62</td>
</tr>
<tr>
<td>Australia</td>
<td>110.20</td>
<td>55</td>
</tr>
<tr>
<td>Singapore</td>
<td>73.50</td>
<td>35</td>
</tr>
<tr>
<td>Canada</td>
<td>57.91</td>
<td>38</td>
</tr>
<tr>
<td>Hong Kong</td>
<td>30.68</td>
<td>12</td>
</tr>
<tr>
<td>Thailand</td>
<td>8.66</td>
<td>48</td>
</tr>
<tr>
<td>Others</td>
<td>153.26</td>
<td>143</td>
</tr>
<tr>
<td>Total</td>
<td>1,968.55</td>
<td>902</td>
</tr>
</tbody>
</table>

Domestic Offerings of Quasi-REITs

<table>
<thead>
<tr>
<th>Year</th>
<th>No. of Issuances</th>
<th>RMB100mm</th>
</tr>
</thead>
<tbody>
<tr>
<td>2014</td>
<td>36</td>
<td>2</td>
</tr>
<tr>
<td>2015</td>
<td>131</td>
<td>4</td>
</tr>
<tr>
<td>2016</td>
<td>131</td>
<td>8</td>
</tr>
<tr>
<td>2017</td>
<td>286</td>
<td>26</td>
</tr>
<tr>
<td>2018</td>
<td>278</td>
<td>354</td>
</tr>
<tr>
<td>2019</td>
<td>439</td>
<td>20</td>
</tr>
<tr>
<td>2020</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
1.2 Background

On April 30, 2020, the China Securities Regulatory Commission (CSRC) and the National Development and Reform Commission (NDRC) jointly issued the Notice on Work in Relation to Advancing the Pilot Project for Infrastructure Real Estate Investment Trusts, marking the official launch of China’s pilot program.
Overall arrangement
2.1 Pilot Orientation

- Country policy-based. Focus on qualified assets
- Yield Characteristics and Pricing Model
- Modify policies and Control risk
- Improvement of management
- Steady development of REITs
- Strengthen intermediaries' responsibilities
2.2 Key Elements

<table>
<thead>
<tr>
<th>Same Control</th>
</tr>
</thead>
<tbody>
<tr>
<td>• The fund manager and the ABS manager must have an actual controlling relationship or both are controlled by the same entity</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>ABS</th>
</tr>
</thead>
<tbody>
<tr>
<td>• More than 80% of the fund assets shall be invested in the ABS and hold 100% of the ABS securities. In addition to invest in ABS, the rest of the fund assets shall be legally invested in interest rate bonds, AAA-rated credit bonds or money market instruments</td>
</tr>
<tr>
<td>• The fund can invest in various ABS, which will further invest in project companies, thus enlarging the raising capital</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Fully Control</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Ownership of SPV: The fund is required to hold all interests of the SPV through ABS</td>
</tr>
<tr>
<td>• Ownership of infrastructure assets: The fund is required to obtain the full ownership or operation rights of the infrastructure assets through structures such as ABS and the SPV, and to have full control and disposal rights of the special purpose vehicles and the infrastructure project</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Close-end Fund</th>
</tr>
</thead>
<tbody>
<tr>
<td>• The fund shall be close-end fund and can be traded publicly once meeting the statutory conditions and approved by the Exchanges in accordance with the law</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>90%</th>
</tr>
</thead>
<tbody>
<tr>
<td>• The fund shall allocate more than 90% of the annual distributable amount of the consolidated fund to the investors in cash, which shall not be less than once a year if the allocation conditions are met</td>
</tr>
</tbody>
</table>
2.3 Transaction Structure

ABS and the SPV are collectively referred to as special purpose vehicles (SPV).

“Part of the operation and management duties shall be fulfilled by subsidiaries of the fund manager or a third-party management provider.”
2.4 Division of REITs Pilot

- Setting assets selection standards
- Pilot projects promotion
- Pilot projects selection
- Making rules
- Verification and registration
- Supervising REITs operation
- Cultivating investors
2.5 Related Policies

Introduction of Policies for China REITs

On April 30, 2020, the CRSC and the NDRC jointly issued the *Notice on Promoting the Pilot Program of Infrastructure Real Estate Investment Trust Funds (REITs)*

On August 3, 2020, the NDRC issued the *Notice on Effectively Performing Infrastructure REITs Pilot Project Application Work*

On August 7, 2020, the CSRC issued the *Guidelines on Publicly-traded Infrastructure Securities Investment Funds (for Trial Implementation)*

On January 13, 2021, the NDRC issued the *Notice on the Establishment of a National Infrastructure Real Estate Investment Trust (REITs) Pilot Project Tank*

On January 29, 2021, the SSE and the SZSE issued the *Business Rules for Publicly-traded C-REITs*

On February 8, 2021, the AMAC issued the *Guidelines on Due Diligence of Publicly-traded Infrastructure Securities Investment Funds (for Trial Implementation)* and the *Operational Guidelines on Publicly-traded Infrastructure Securities Investment Funds (for Trial Implementation)*
2.6 Filing Path for Pilot Projects

- For pre-approved pilot projects, the provincial development and reform commission (DRC) for where the assets are located is required to issue a special no-objection opinion to the NDRC.
- **Sponsor can not submit the filing materials to both the CSRC and the exchanges until recommendation letter from the NDRC are obtained.**
- While CSRC is primarily responsible for approving the offerings of public funds, while the exchanges are responsible for reviewing and issuing no-objection letters for ABS, sponsor shall simultaneously submit listing applications to the exchanges.

Note*: If the sponsor is foreign-funded, it may entrust and authorize the sponsor to take the provincial DRC for one of the assets for filing.
2.7 Pilot Assets Categories

Key Industries for REITs: 7 Industries/24 Sub-industries + Qualified Park Infrastructure Assets

- Logistics: Warehousing and logistics
- Transportation: Tollways, railways, airports and ports
- Environmental Protection: Environmental treatment related estate
- Public Works: Urban water, power, gas and heat supply
- Manufacturing: Data center, AI and intelligent computing center
- TMT: 5G, Network Tower, Internet of Things, Industrial Internet, Broadband Network, Cable TV Network, Smart Transportation, Energy and City
- Others

Special Requirements for Park Infrastructure Assets:

- National strategic emerging industrial clusters: Beijing, Shanghai, Wuhan, Shenzhen and Hefei
- Hi-tech/Characteristic Industrial Parks: Located in 2,543 development zones in the "Catalogue of Review Announcements of Development Zones in China (2018 Edition)". Among which, there are 552 development zones approved by the State Council and 1,991 local development zones.
  - Business requirements: R&D, innovative design and pilotsale experiment platforms, industrial plants, business incubator and industrial accelerator, etc.
  - Land use requirements: The land used for the projects is non-commercial and non-residential land.

Prioritized Regions for the Pilot of REITs

- The Greater Bay Area includes: Guangzhou, Shenzhen, Zhuhai, Foshan, Huizhou, Dongguan, Zhongshan, Jiangmen, Zhaoqing, Hong Kong and Macau
- Beijing-Tianjin-Hebei region
- Xiongan New Area
- Yangtze River Economic Belt
- Yangtze River Delta Region
- Hainan Duty Free Port
2.8 Focus on Qualified Assets

**Qualified Assets of REITs**

- **Infrastructure Real Estate**: The property shall be infrastructure real estate assets, “assets heavy” instead of “assets light”

- **Mature Assets**: REITs shall invest in mature assets in operation rather than under-developing assets

- **High Dividends**: REITs must allocate a high proportion of cash instead of rely solely on the expected appreciation of assets

- **Between Stocks and Bonds**: The feature of REITs are between stocks and bonds with medium risk, medium return, and medium liquidity

**Major Requirements**

- Consecutive operation duration > 3 years, generally
- **The sources of cash flows shall be reasonably diversified.** It should mainly come from operational revenue rather than depending on non-recurring income such as subsidies from third parties
- **Maintaining profitability or positive operational net cash flows for the past 3 years**
- **The expected net cash flow distribution rate for the next 3 years (estimated annual distributable cash flows/ target net appraisal value of real estate) is in principle not less than 4%**
2.9 Asset Selection Criteria

- **Pilot scope**: qualified types of asset that located in the pre-approved pilot regions
- **Ownership**: self-owned assets; legally entitled to project ownership, franchise rights or operation fee rights
- **Operation duration**: not less than 3 years in principle, and for some asset types, the duration can be determined based on the actual conditions when the operation and cash flow are stable
- **Cash flow**: the sources of cash flows shall be reasonably diversified, and the assets shall maintain profitability or positive operational net cash flows for the past 3 years

**Basic Requirement**

- **Investment procedures for fixed assets**: completion of project approval or filing procedures; completion of planning, land use, environmental impact assessment and construction permit procedures; completion of project inspection and acceptance
- **Other procedures**: completion of other permitting procedures necessary for special assets (e.g. energy conservation review, value-added telecommunications business license, etc.)
- **PPP Projects**: meeting the regulatory requirements and the franchise operation requirements, and the revenue source should mainly comes from user-based payments

**Compliance Requirement**

- **Project return rate requirements**: The expected net cash flow distribution rate for the next 3 years (estimated annual free cash flows/ net assets value) **shall not less than 4% in general**
2.10 Responsibilities of Fund Managers and Property Managers

**Fund Managers**

- Fund managers shall fulfill the qualifications in six aspects: establishment period, financial status, corporate experience, professional experience, institution regulation and compliance. In addition, fund managers should also meet other requirements stipulated by the CSRC.

**Due Diligence & Offering**
- Responsibilities similar to those of investment banks

**Valuation & Income Allocation**
- Responsibilities of publicly-traded fund managers

**Information Disclosure**
- Responsibilities similar to those of board offices of listed companies

**Proactive Operation**
- Responsibilities of operating and managing property

**Property Managers**

- **Responsibilities:** daily operation and management of infrastructure projects. When a third-party management institution accepts the entrusted management, the property manager shall not delegate the principal responsibilities of the entrusted operation and management of infrastructure to other institutions.
Offering and Trading Issues
3.1 Investors

**Strategic Investors**
1) sponsor or connected party under common control
2) Special government funds, industrial investment funds
3) Upstream and downstream industrial investors...

**Institutional investors**
1) Securities companies, 2) fund management companies, 3) trust companies, 4) finance companies, 5) insurance companies, 5) QFIs, 6) commercial banks and their wealth management subsidiaries, 7) eligible PE fund managers, 8) other professional institutional investors accredited by the CSRC, 9) NSSF, basic pension funds, annuity funds, etc.

**Public Investors**
- On-exchange offering
- Maximize the scope of retail investors

**Offering price determined through Bookbuilding**
- Signing the placement agreement in advance
- Fund manager direct sales counter
- Subscribe

**Mutual Fund (Close-end)**
- On-Exchange trading
- Listed shares
- Custody transfer
- OTC shares

**Public Investors**
- Securities companies
- Banks and the 3rd party channels

**Strategic Investors**
- Maximize the scope of retail investors

**Public Investors**
- OTC offering
3.2 Offering Arrangements

- **Offering**: The valuation of underlying assets is converted in ¥1 par value for each unit. The fund unit is priced via bookbuilding, following the practice in stock offerings, and issued in accordance with that in LOF offerings.
- **Pricing**: Bookbuilding (via the exchange’s electronic platform for placement) with institutional investors (ex. strategic investors).
- **Pricing process**: Roadshow → Bookbuilding → offering price determination.
- **Offering method**: Strategic placement + bookbuilding based placement + public offering.
- **Organizer**: Fund manager and financial adviser (if any, which is entrusted with roadshow, bookbuilding, pricing, placement, etc.).
- **Type of institutional investors**: Securities companies, mutual fund, trust, finance company, insurance company, private equity, commercial bank’s wealth management subsidiaries, social security fund and other professional institutional investors.

**Investor Structure**

- Strategic placement to sponsor
- **Not less than 20% of total shares issued, with 5 years lock-up period**
- **Lock up period for portion > 20%**: 3 years

- Percentage of strategic placement to professional institutional investors should be determined by fund manager and financial advisor through negotiation and the **shall be locked up for at least 1 year**.

- Size of placement, after deducting placement to strategic investors, **shall not be less than 70% of the public offering size**.

- Public investors may subscribe for shares through fund sales agencies at a price determined through price inquiry, with **at most 24% of individual investors allowed to invest in the offering**.
3.3 Offering Process

- After registration with CSRC, the subscription price of fund units are determined via offline price inquiry. The roadshow, price inquiry, pricing, placement and other relevant activities are carried out by the fund manager or the financial advisor engaged by it.

1. Public investors subscribe for fund units
2. Institutional investors submit subscription application through price inquiry platform and complete payment to fund manager
3. Investors in strategic placement subscribe for fund units as they have undertaken

Fund manager submits offering application to exchange

Fund manager discloses offering plan, price inquiry announcement, fund contract, prospectus, overview of fund product information and other legal documents

1 trading day is arranged for offline price inquiry. Qualified institutional investors bid for the offering

Offering announcement is disclosed 3 days prior to public offering, and the announcement shall contain subscription price and process of its determination, starting and ending dates of offering period, subscription method, subscription fee, etc.

CSDC sends subscription applications made in and outside the exchange to fund manager for confirmation

Fund manager confirms clawback result and final allocations, and CSDC completes registration of shares
3.4 Trading Platforms

- **Auto-match transaction by price bidding**
  Similar to on-exchange funds trading

- **Block trade**
  Minimum 1,000 RMB, minimum distance 1,000 RMB

- **B2B/B2C**, support bonds, bilateral bond repos and REITs Trading
  Quotation transactions and price inquiry –based transactions
3.5 Other Details

**Market-maker**

The market-making mechanism is introduced semi-compulsively. Fund managers shall, in principle, select no less than one liquidity service provider to provide services such as bilateral quotations for infrastructure funds. The market-making mechanism is under improvement.

**Margin Trading**

Include securities margin trading: Security rights can be included, and whether it can be used as the underlying securities for margin trading is under talking.

**Price Range**

Price fluctuation limit on the first day of listing is increase to 30%, and price fluctuation limit on other trading days is 10%.

**LOF**

Settlement: T+1. Follow LOF to conduct depository, clearing and settlement.
REITs in SSE
4.1 Exchange Duties

- Rules Setting
- Verification
- Listing
- Disclosure
- Trading and Supervisory
- Market Development
4.2 Information Displayed

SSE website Regarding REITs

http://www.sse.com.cn/reits/home/
Access to verification process, listing and trading information, disclosure, investors education
4.3 Latest Updates

1. Oral Defense for Key Projects
   - NDRC, together with CIECC, organized formal presentation for more than 20 key projects.

2. NDRC Notice
   - NDRC issued a formal notice for materials to the qualified pilot projects that have gone through the pre-screening.

3. List of First Pilot Projects
   - NDRC issued recommendations to CSRC on the first pilot projects.
   - The Exchanges conducted pre-review on the first draft of pilot project materials.

4. CRSC and SSE&SZSE working on regulation and rules development
   - CRSC issued the final version of the Guidelines on Funds, and the Exchanges issued the supporting business rules.
   - The Exchanges formulated business procedures. In the mean time, issuance supporting system was upgraded.

5. Listing of First Projects
   - The first pilot projects finished formal application and review process in the Exchanges and CSRC.
   - CSRC issued a formal reply and the Exchanges issued a no-objection letter.
   - Registration, issuance and listing of the first projects.
### 4.4 First REITs to be Listed in SSE

<table>
<thead>
<tr>
<th>Name</th>
<th>Segment</th>
<th>Location</th>
<th>Underlying Assets</th>
<th>Net Cash Distribute Ratio (2021,2022)</th>
<th>Issue amount (Billion RMB)</th>
<th>Period (Years)</th>
<th>Price (RMB)</th>
<th>Fixed Fee</th>
<th>Floating Fee</th>
</tr>
</thead>
<tbody>
<tr>
<td>DongWu- Suzhou Industrial Park Close-End Infrastructure Fund</td>
<td>Industrial Park</td>
<td>Suzhou</td>
<td>International Science 5th project, Block B; 2.5 Industrial Park 1st and 2nd project</td>
<td>4.50% 4.54%</td>
<td>3.492</td>
<td>40</td>
<td>3.88</td>
<td>NAV<em>0.15 %+Distributable Amount</em>1.05%</td>
<td>Sum of all parks` (net revenue-target net revenue)*40%</td>
</tr>
<tr>
<td>HuaAn-Zhangjiang-GuangDa Park Close-End Infrastructure Fund</td>
<td>Industrial Park</td>
<td>Shanghai</td>
<td>Zhangjiang-GuangDa Park</td>
<td>4.74% 4.11%</td>
<td>1.495</td>
<td>20</td>
<td>2.99</td>
<td>NAV*0.55 %</td>
<td>Floating Fee=(previous year’s net operating revenue-target revenue)*10%+(previous year’s gross operating revenue <em>4%-NAV</em>0.2%)</td>
</tr>
<tr>
<td>CICC-GLP Logistics Close-End Infrastructure Fund</td>
<td>Logistics</td>
<td>Beijing, Guangzhou, Foshan, Suzhou, Kunshan</td>
<td>Logistics Parks in Beijing, Tongzhou, Guangzhou,Zengcheng, Shunde, Suzhou-Wangting and Dianshan Lake</td>
<td>4.45% 4.48%</td>
<td>5.835</td>
<td>50</td>
<td>3.89</td>
<td>Issue Amount*0.7%</td>
<td>Logistics rental revenue *floating rate</td>
</tr>
<tr>
<td>ZheShang-Shanghai-Hangzhou-Ningbo Expressway Close-End Infrastructure Fund</td>
<td>Toll Roads</td>
<td>Zhejiang Province</td>
<td>Hangzhou-Anhui Expressway (Zhejiang Parts)</td>
<td>12.40% 10.50%</td>
<td>4.36</td>
<td>20</td>
<td>8.72</td>
<td>NAV*0.12 5%</td>
<td>Year Revenue *(1.2%,1%,0.8%) with accordance to cash distribute ratio (&gt;=10%,9-10%,&lt;9%)</td>
</tr>
<tr>
<td>FuGuo-Beijing Capital Sewage Treatment Close-End Infrastructure Fund</td>
<td>Sewage treatment</td>
<td>Shenzhen, Hefei</td>
<td>375,000 tons/day capacity –sewage treatment BOT franchise project in Shenzhen, PPP project of Shiwuli River Sewage Treatment Plant with a Treatment capacity of 300,000 tons/day in Hefei</td>
<td>8.74% 9.15%</td>
<td>1.85</td>
<td>26</td>
<td>3.7</td>
<td>NAV<em>0.1% +Operating Revenue</em>0.86%</td>
<td>Based on the result of EBITDA of the property company(6 ranges)</td>
</tr>
</tbody>
</table>