



14th August 2020

Sent by Email and by Post

The Securities and Futures Commission
35/F Cheung Kong Center
2 Queen's Road Central
Hong Kong

Dear Sirs/Madams,

Re: Consultation Paper on Proposed Amendments to the Code on Real Estate Investment Trusts

Raising the standard of practice in the financial services industry is one of the missions of our Society. Regarding the captioned subject matter, we understand that a fine balance should be maintained between facilitating REITs market development and competitiveness on the one hand and ensuring the protection of investors' interests and market integrity on the other. The Society have received both written comments and verbal comments. The latter were collected in a meeting convened for the purpose of this consulting paper.

All views are expressed as members of the Society and we are not aware that the views expressed represent corporate interests.

The Society has consolidated various views from members coming from different background. Some of them may conflict with each other. We do not aim to present a unified view in all circumstances.

For the captioned consultation, our specific answers are as stated in the appendix attached.

Thanks for your attention.

Yours sincerely,
For and on behalf of
CFA Society Hong Kong

Ashley Khoo, CFA
Co-chair, Industry Relations Committee

Alvin Ho, CFA
Co-chair, Industry Relations Committee

Appendix

1. Do you agree with the proposal to allow flexibility for REITs to invest in Minority owned Properties? Please explain your view.

Answer:

We are generally agreeable to the direction in this regard. Some of our members have cited reasons such as the potential for a broadened investment universe, diversification of the portfolio, opportunity for improved returns, and more room to grow. Some members maintain that a balance between the need to grow the business and the associated risks is important.

2. Do you consider that the proposed overarching principles and specific conditions for Qualified Minority-owned Properties are appropriate? Do you have any comments on the principles and conditions proposed? Please explain your view.

Answer:

Some of us are concerned with the possibility of an over-exposure to qualified minority-owned properties (QMOP). Hence, it is suggested that within the 75% band, a specific percentage cap should be set for QMOP. Another possibility is that because investors invest in REITs using equity value (or net asset value) as a baseline reference, the measurement of QMOP (and MOP) should also incorporate equity value (in addition to GAV). This could be especially important in highly leveraged transactions where equity value could be vulnerable.

3. Do you have any comment on the proposed requirements for Non-qualified Minority-owned Properties? Please explain your view.

Answer:

There are concerns such as while capped within the 25% limit, an over-exposure to non-qualified minority-owned properties (NQMOP) would still open REIT operators to risks that investors cannot fully appreciate. In particular, it would be very tricky to assess the risks associated with the unconsolidated debts and other features buried deep inside the special purpose vehicles in which the REIT operators only hold minority interests. To mitigate such risks, some members have put forward a percentage cap of such NQMOP within the 25% band, or the requirement of minimum income level for those minority positions. See the next paragraph for points relating to disclosure.

4. Do you have any comment on the proposed disclosure and other requirements for investments in Minority-owned Properties?

Answer:

Members are very keen to receive transparent disclosure of the minority-owned properties, including details of the financial performance and balance sheet impacts. Also, the disclosure obligation should continue on an ongoing basis (for example, interim and annual reports).

Some members are sceptical in that they do not expect such investments to achieve the said objectives. As such, a lower % threshold, such as 20% (instead of 25%), is suggested.

5. Do you agree with our proposal to align the diversification limit on the REIT's holdings of Relevant Investments issued by any single group of companies with the Single Investment Cap on Non-qualified Minority-owned Properties of 10% of GAV? Please explain your view.

Answer:

Some members suggest that a ratio of 5% (diversification limit) / 25% (cap on non-core investment) may be more reasonable and effective (for the purpose of diversification) than the ratio at 10% / 25%. However,

some other members reckon that such a 5/25 ratio may reduce the opportunity set available to the REIT operators, particularly those with smaller equity base.

6. Do you have any comment on the proposal to adjust the 10% GAV Cap and the safeguards imposed? Please explain your view.

Answer:

We agree that having unitholders' approval would be necessary for the situation where the 10% threshold may be exceeded. Full disclosures, both qualitative and quantitative, are critical as REIT investors invest in such vehicles for low risk and developmental projects present very different (higher) risk profile. Some members also raise the concerns about "other auxiliary investments" as REIT investors may not have the necessary skills to evaluate all the intricacy embedded in, say, FX hedging.

7. Do you have any comments on the proposed increase of the borrowing limit from 45% to 50%? Do you think a higher borrowing limit above 50% should be allowed? Please explain your view. If you think a higher borrowing limit should be allowed, what should be the appropriate limit and what other conditions or safeguards (if any) should be imposed?

Answer:

We note that HK's REIT operators have generally been conservative in managing leverage. Therefore, we are agreeable to the 50% limit. Caution, however, should be maintained as some members cite that the global peers tend to have lower gearing ratio than the limit proposed.

8. Do you have any comments on the proposed amendments to the definition of "connected persons"? Please explain your view.

Answer: We do not have comments.

9. Do you agree with the proposal to align the connected party transactions and notifiable transactions requirements for REITs with the Listing Rules? Please set out your reasons.

Answer: We do not have comments.

10. Do you have any comments on the other proposed amendments to Chapter 8 and Chapter 10 of the REIT Code?

Answer: We do not have comments.

11. Do you have any comments on the proposed miscellaneous amendments? Please explain your view.

Answer: We do not have comments.

12. Do you have any comments on the proposed implementation timeline?

Answer: We do not have comments.

The answers above are based on the feedback from the members from Advocacy Committee, Industry Relations Committee and Research Challenge Committee.