

TOPICS

- [RBI Restricts FII Subscription to Real Estate IPOs](#)
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» RBI Restricts FII Subscription to Real Estate IPOs

The central bank, Reserve Bank of India (RBI) has planted road blocks for foreign institutional investors (FIIs) in public equity offerings by real estate companies. The RBI has taken a view that FIIs can subscribe to shares of real estate IPOs only if the project is compliant with foreign direct investment (FDI) regulations in real estate. Currently, this appears to be a representation made by the RBI and a possible change in policy would be announced by way of a notification or regulations would be framed/amended to reflect the same.

The RBI has sought to restrict FIIs from investing in initial public offerings (IPOs) of real estate firms if the proposed venture is not in conformity with FDI conditions. The Union Government had issued Press Note 5 in 2005 which stipulated guidelines for FDI in townships, housing, built-up infrastructure and construction-development projects. By virtue of the said guidelines, FDI is permitted in real estate projects subject to meeting certain development criteria, investment conditions, ban on sale of underdeveloped plots etc.

If a project satisfies these conditions, the concerned company can invite foreign participation upto 24% equity and later revise it towards the FDI sector cap (being 100% in construction development companies) However, a registered FII would still be allowed to invest in real estate companies via the portfolio investment route, or in other words, through a registered broker once the company is listed.

In recent times, real estate companies are seen to form an ubiquitous part of the IPO scenario. However, this RBI stance has issuer companies adopting different methodology to bypass the restriction or refrain from marketing to FIIs altogether. Also, it would appear that although a real estate IPO (non FDI complaint) would be inaccessible to an FII, a foreign venture capital investor can invest in a domestic venture capital undertaking which in turn could invest in such projects. Whether this would be permissible and other related issues remain to be clarified whence and if the RBI announces the relevant notification.

For further details please contact the Real Estate Team.

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