Q&A with Sharon Lau and Cathy Yeung

The Future of Trust IPOs in Asia

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With developed and active real estate investment trust (REIT) markets and expanding business trust (BT) markets, trust IPOs have earned themselves a solid place in the Asian financial marketplace. “Trust IPOs are no longer a trend in Asia,” said Sharon Lau, a partner in Latham & Watkins’ Singapore office. “They are certainly a product and structure that is here to stay.”

Lau participated in a panel on Asian trust IPOs at the International Financial Law Review (IFLR) Capital Markets Forum in Hong Kong. The panel was moderated by Cathy Yeung, a Hong Kong-based partner at Latham & Watkins. Representatives from Morgan Stanley, New Century REIT and Ping An Trust participated in the panel.

In this Q&A interview, Lau and Yeung discuss the current state of the trust IPO markets in Asia, particularly Hong Kong and Singapore, and what businesses and investors can expect in the future.

What are the differences between REITs and BTs?

Lau: REITs have been around for a long time, and BTs have somewhat modeled themselves on REITs. BTs are set up as trusts as well and invest in yield generating assets. Many BTs do invest in real estate but they do not fulfill the requirements of a REIT. With REITs there are quite a lot of belts and braces in terms of what the trust can and cannot invest in. For example, there is a limit on the investment a REIT can make into development properties. There are also many restrictions in terms of the amount of gearing and leverage a REIT is allowed to take on, which is similar whether under Singapore or Hong Kong rules – there are slight differences but the principles are pretty much the same.

The focus is slightly different for business trusts. Investors typically want to invest in a particular asset class and/or a particular business – it might be that the trust owns not only assets but also operating companies, so these structures contain much more flexibility. There is also a lot more flexibility in terms of the types of assets these trusts can invest in. For example, they are not legally tied to gearing limits. From a marketing or investor protections perspective, there will certain be limits imposed, but it is certainly not as tight as what you would find in REITs.

How do the BT markets in Singapore and Hong Kong differ?

Lau: The Singapore market compared to the Hong Kong market is much more developed in terms of BTs. It is now one of two markets in Asia, but for the longest time it was the only market in Asia that had a statutory regime for business trusts. Hong Kong still doesn't have a statutory regime for BTs. There has been a lot of discussion on new rules that would change this, but it still hasn't taken place. Interestingly, if one wanted to list a business trust type structure in Hong Kong, there are ways to do it within the existing regime. This basically entails listing both a company as well as a trust separately.

Yeung: Although Hong Kong has no statutory regime for BTs, in order to facilitate the application of the Securities and Futures Ordinance and other regulatory requirements, the Hong Kong Stock Exchange and Securities and Futures Commission approved a hybrid structure called the share stapled unit structure, which means that the units in the trust, the shares in the operating company as well as beneficial interest in the shares legally bound, transferred and traded together. Both the BT and the operating company are all listed on the stock exchange.

With the introduction of this hybrid structure, are BTs becoming more popular in Hong Kong?

Lau: The benefit of doing a business trust over a REIT in Hong Kong is that the regulatory process for clearance of the structure is more straightforward and relatively quicker compared to REITs. Certainly one of the takeaways that the panelists had was that they would expect more and more of these structures in the coming years, culminating, hopefully, in the legislation actually being passed.

Yeung: Notwithstanding this, we are still seeing people choosing between REITs and BTs—it is not just all BTs. People should assess the pros and cons of both and decide which one is more suitable for their business. Even though BTs are less restrictive compared to REITs, some feel they are more risky because there are fewer regulations. So it really depends on the investors and whether they would like to have a more restrictive investment structure rather than a more relaxed one. Real estate investors are more used to the REIT structure, so many prefer to stick with it. But for other businesses, other than real estate, BT is a flexible structure for them.

Is Hong Kong expected to usurp Singapore as the Asian center for REITs and BTs?

Lau: This question was certainly one focus of the panel – what can Hong Kong learn from Singapore and what are the trends that Singapore is seeing that they might expect in Hong Kong, especially for BTs?

Hong Kong has a very developed REIT market as does Singapore and frankly, between the two markets, the market with greater liquidity and trading volumes is Hong Kong. A key advantage for Singapore is of course the statutory BT regime which has been in place for many years. As such. we have seen the BT structure used initially for real estate assets, then shipping, infrastructure and other asset classes. Trust structures in Hong Kong have typically been focused more on real estate.

Yeung: In terms of the number of REITs and the market cap of the REIT market, Hong Kong has been lagging behind. However, as one of the most vibrant real estate markets in the world, we do expect the Hong Kong REIT market to become a center in Asia, and the world especially for Greater China. Some real estate developers actually expected China to establish a REIT market during the past few years, but they were disappointed because it has been so long and there hasn't been any progress and they can't continue to wait for the REIT market to open in China, so Hong Kong has become attractive venue for them to list their real estate assets. They are always comparing Singapore and Hong Kong, but because Hong Kong is closer to China and more familiar with the investors and more familiar with the Chinese market it has become an attractive venue for listings. That said, Singapore has a very mature REIT market as well as a BT market and it also has an attractiveness to investors. Singapore and Hong Kong are both attractive markets at this point.

In response to the market criticism on certain more stringent restrictions on REITs, the Securities and Futures Commission has published a consultation paper on amendments to the Hong Kong REIT code, with proposals for introducing flexibility in respect of instructs in properties under development or engagement in property development activities, as well as flexibility in respect of instructs in financial instruments. The consultation paper has been welcome by the market and I believe with the changes, Hong Kong REITs market will certainly thrive and become more attractive in the future.

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