Embassy REIT

Q3 FY2023 Earnings Call

January 25, 2023

# CORPORATE PARTICIPANTS

Vikaash Khdloya – Chief Executive Officer (CEO)

Abhishek S Agrawal – Interim Chief Financial Officer (CFO)

Ritwik Bhattacharjee – Chief Investment Officer (CIO)

Abhishek Agarwal – Head of Investor Relations

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# MANAGEMENT DISCUSSION SECTION

**Operator:** Good evening everyone. A very warm welcome to all for Embassy REIT's third quarter FY2023 Earnings Conference Call. Currently, all participants are in a listen-only mode. Our speakers will address your questions at the end of the presentation during the question-and-answer session. As a reminder, this conference call is being recorded.

I would now like to introduce your host for today's conference – Mr. Abhishek Agarwal, Head of Investor Relations for Embassy REIT. Sir, you may begin.

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## Abhishek Agarwal

Head of Investor Relations

Thank you, operator. Welcome to the Q3 FY2023 Earnings call for Embassy REIT.

Embassy REIT released its financial results for the quarter and nine month period ended December 31, 2022 a short while back. As is our standard practice, we have placed our financial statements, earnings presentation discussing our performance, and a supplemental financial and operating databook in the Investors section of our website at www.embassyofficeparks.com.

As always, we would like to inform you that management may make certain comments on this call that one could deem forward-looking statements. Please be advised that the REIT's actual results may differ from these statements. Embassy REIT does not guarantee these statements or results and is not obliged to update them at any time. Specifically, the financial guidance and any proforma information that we will provide on this call are management estimates, based on certain assumptions and have not been subjected to any audit, review, or examination procedures. You are cautioned not to place undue reliance on such guidance and information and there can be no assurance that we will be able to achieve the same.

Joining me today are Vikaash Khdloya, the CEO, Abhishek S Agrawal, the Interim CFO and Ritwik Bhattacharjee, the CIO. Vikaash will start off with business and industry overview followed by Ritwik and Abhishek. We will then open the floor to questions.

Over to you, Vikaash.

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**Vikaash Khdloya**

Chief Executive Officer (CEO)

Good evening and thank you for joining us today to review our Q3 results.

We are pleased to report another robust quarter of business performance and a continued positive outlook for India office market. We signed a total of 1 msf leases, improved our same-store occupancy to 88%, generated healthy 13% NOI growth, announced 15th consecutive quarter of 100% distributions and remain on-track with our full year guidance. Additionally, we unlocked further growth in Bangalore at our Embassy TechVillage ('ETV') property by launching a new 410k sf office block at a highly accretive 24% yield. Our active development pipeline now totals 6.6 msf and sets us up to deliver an incremental ₹8 billion annual NOI upon stabilization at an attractive 24% yield. So, another quarter of resilient business activity and a clear pathway towards accelerating growth, which we are well-placed to finance given our low 27% leverage, competitive debt costs and AAA/Stable rated fortress balance sheet.

Even amidst a highly volatile global macro environment, India continues to attract more and more global companies to set up and grow their offshore captive centers. Morgan Stanley, in its recently published report 'Why This is India's Decade', has highlighted offshoring as one of the key megatrends which will continue to fuel India's growth. The dual drivers for this phenomenon are structural, namely India's abundant STEM talent and the cost efficiency offered by India's gateway cities, relative to more expensive and less scalable markets globally. As we have highlighted previously, these global captives continue to pursue premium-quality wellness-focused properties, to attract and retain talent and to grow their presence in India. Our YTD leasing performance, our highly accretive active developments and our resilient distributions demonstrate our continued strong conviction in the long-term growth opportunity offered by India office.

**Let me now update you on our leasing performance**

During Q3, we leased a total of 1 msf across 19 deals and added 7 new occupiers across healthcare, financial services and tech firms. We achieved robust new leasing of 0.5 msf at impressive 5% premium to market rents. Additionally, we renewed another 0.5 msf leases at 21% renewal spreads, including 0.4 msf of early renewals by four large multinationals. We also secured 13% rent escalations on 2.1 msf which further contributes to our NOI growth. Physical attendance in our properties also continued its upward growth trajectory and stood at around 46% last week, a 30% uptick compared to the last quarter, majorly led by banks and global captives.

Bangalore continues to drive demand, with the occupancy of Embassy Manyata now touching 90% and a strong deal pipeline for both Embassy Manyata and ETV, reflecting continued strong demand from global captives. Further, Pune witnessed early signs of demand pick-up with 152k sf new leases in Q3, including by an American healthcare major. With this, our Q3 occupancy stood at 86% and our same-store occupancy rebounded to 88%. Our active deal pipeline of 850k sf sets us on the path to pre-Covid occupancy levels of 90s in the next few quarters.

Our strategy of attracting higher growth occupiers has helped us diversify occupier concentration, deliver above market rents and more importantly, embed growth into our portfolio. For instance, in the last 18 months, we added an impressive 52 new occupiers across sectors such as cloud infrastructure, cybersecurity, fintech, healthcare tech and renewables. These deals were across 1.4 msf and at 4% premium to market rents. Notably, based on our on-ground discussions, around half of these occupiers are already looking to grow their India footprint, which will further aid our new leasing.

On the SEZ front, the industry is currently awaiting further regulatory clarity around the proposed DESH bill. Excluding our 3.3 msf SEZ vacancy, our Q3 same-store occupancy would be at even higher levels of around 97%. An enabling regulatory framework around denotification and flexibility of usage of existing SEZs will boost demand for such spaces and further drive leasing traction.

**Next, an update on our ESG program**

ESG remains a core pillar of our strategy and our sustainability-focused buildings continue to receive recognition from globally renowned organizations. Our operational portfolio was awarded 9 Swords of

Honor by the British Safety Council, acknowledging the best-in-class safety and wellness aspects of our buildings. In addition, we are proud to report that we have been recognized as the world's largest USGBC LEED Platinum-certified office portfolio.

We continue to progress on our 3-year ESG roadmap, supported by our ₹3 billion committed investments. We remain focused on reducing our carbon footprint through green initiatives such as our 20 MW solar rooftop project and we are progressing well on our '75/25 Renewable Program', i.e. our commitment to achieve 75% renewable energy usage across our properties by FY2025. Our team recently launched a dedicated microsite to provide details on our ESG program and we encourage you to visit the same.

**Finally, moving to the outlook for Indian office**

2022 was a resurgent year for India office with total absorption of around 55 msf, closer to pre-pandemic highs. While globally there may be an increased caution around office demand, the long-term fundamentals of India office remain strong as ever. Apart from banks and financial services captives which continue to drive demand, many global retailers, insurers and healthcare majors are now setting up their India offices. Increased focus on costs and efficiencies by global corporates is likely to further accelerate this India offshoring trend, disproportionately to the benefit of institutional landlords like us.

On the other hand, the supply of quality office stock continues to consolidate towards fewer and larger institutional quality landlords who are well-funded to invest in sustainable growth. A combination of cost inflation and rising interest rates is likely to increase the replacement value of properties, thereby impacting supply and driving rent growth in the medium-term.

As you may recall, we had given a 5 msf total leasing guidance for FY2023, which was meaningfully above our pre-pandemic 5-year average of 3.3 msf. We are happy to report that year-to-date, we have already leased 4.4 msf, achieving around 90% of our annual guidance, despite Q3 traditionally being a seasonally slow quarter. Notably, we are tracking ahead on both our fresh leasing and pre-leasing guidance and our active deal pipeline remains robust, which will further accelerate our NOI growth.

Let me now handover to Ritwik to expand further on our growth initiatives.

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## Ritwik Bhattacharjee

Chief Investment Officer (CIO)

Thanks Vikaash. Hello everyone. Our key growth initiatives for Q3 include:

- We delivered a new 0.9 msf office block at Embassy TechZone, Pune and launched an additional 410k sf new office building at ETV, Bangalore;
- We accelerated development of our 6.6 msf active growth pipeline, with approximately 90% concentrated in Bangalore, India's best performing office market; and
- We continue working on the non-binding offers to acquire the 7.1 msf of Sponsor assets in Chennai and Bangalore.

**First, an update on our development portfolio**

At Embassy Manyata, we are developing 3.5 msf across five blocks. The 1 msf M3 Block A is nearing completion and we expect to receive the occupancy certificate in Q4. We are seeing good leasing traction with 3 deals in active discussions. Further, there has been encouraging progress on obtaining the Transferable Development Rights ('TDR') and other statutory approvals for the 0.6 msf M3 Block B. This block has already been pre-leased to ANZ bank, and super structure work is underway. Our recently launched new builds across the 0.7 msf L4 block and the 1.2 msf D1 and D2 redevelopment blocks are progressing well, and we are witnessing early traction from global banking, cloud computing and other tech players.

At Embassy TechVillage, we are developing our 1.9 msf Block 8, of which 550k sf has already been pre-leased to JP Morgan. We continue to see surging demand for the balance. We have always been optimistic about the leasing dynamics of ETV in particular and Outer Ring Road ('ORR') micro-market in general. To that end, we are launching a 410k sf block, named Helenium, by unlocking the available FAR potential at ETV. This new block is in addition to ETV's development potential that we underwrote at the time of its acquisition. This project is expected to generate a highly accretive yield on cost of approximately 24%.

Also, in Q3, we received the occupancy certificate for Hudson and Ganges, the 0.9 msf office blocks in Embassy TechZone, Pune; and our 0.7 msf Tower 1 at Embassy Oxygen, Noida is now nearing completion.

To summarize, our total development pipeline now stands at 6.6 msf. Over 90% of this growth pipeline is in Embassy Manyata and ETV in Bangalore. Our reasons for concentrating development in our best parks in Bangalore is simple. Bangalore is the Indian city which leads global occupier demand and the development economics in two of India's best business parks which we own are too attractive to ignore. At ₹30 billion total committed capex, of which ₹21 billion is pending as of Q3, these 6.6 msf projects are expected to deliver ₹8 billion annual NOI upon stabilization. These projects set us up for impressive 24% yields on cost and they validate our strategy to accelerate our growth pipeline.

**Next, an update on our hotels and total business ecosystem**

Our four operating hotels continued their marked rebound in Q3 with 47% occupancy, a 15% QoQ ADR growth and a YTD EBITDA of ₹704 million. This performance is significantly better than what we initially guided to. We have always believed that our hotel business complements our office offering perfectly, and that it will continue to positively reflect in our leasing and rents over the long-term. We expect this to be no different as we develop the 518 key dual-branded Hilton hotels at ETV. The ORR market where ETV is located is underserved, with only 1,400 hotel rooms serving over 50 msf of office space.

Additionally, we continue to provide a 'total-business-ecosystem' experience to our occupiers by constantly upgrading our properties with an eye on occupiers' future needs. Our 200k sf refurbishment of Block K at Embassy Manyata is nearing completion and will enhance the leasable area of this block by 18%. Additionally, we look forward to the upcoming launch of the NXT Retail Plaza at Embassy Manyata. This is an 85k sf F&B hub that will further boost employee experience as well as widen Embassy Manyata's competitive moat.

**Finally, an update on our acquisitions**

We have made significant progress in our discussions with Embassy Sponsor and other stakeholders to acquire the two properties in Bangalore and Chennai, which total 7.1 msf.

This includes the 5 msf Embassy Splendid TechZone business park in Pallavaram, Chennai and the 2.1 msf Embassy Business Hub property in Yelahanka, North Bangalore. Both properties are strategically located in fast-growing micro-markets and are anchored by renowned global occupiers in banking, financial services, healthcare tech and IT services sectors. Of the total 7.1 msf, 2.1 msf is completed or nearing completion with 91% committed occupancy, thereby providing stable cash flow visibility. And of the balance 5 msf, construction is underway for 3 msf, which aids further growth. The potential acquisition will likely account for less than 4% of REIT's current GAV and remains subject to ongoing diligence, negotiations, funding and requisite approvals.

We are also evaluating certain other acquisition opportunities from third parties. We are focused on prudently financing potential acquisitions through an optimal mix of debt-equity and are closely monitoring the challenging financing markets for appropriate transaction windows. We remain committed to ensure that all our growth initiatives deliver value to our Unitholders, as demonstrated by our earlier ETV acquisition which has outperformed our underwriting on numerous metrices.

Over to Abhishek now for our financial updates.

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## Abhishek S Agrawal

Interim Chief Financial Officer (CFO)

Thanks, Ritwik. Good evening everyone. Let me take you through the key financial highlights for Q3.

- We grew Net Operating Income by 13% YoY to ₹7,049 million, with operating margin of 81%;
- We announced distributions of ₹5,033 million or ₹5.31 per unit ('DPU'), with a 100% payout ratio; and
- We continue to maintain our strong balance sheet with 27% low leverage and attractive 7.2% debt cost.

Let me take you through the details.

**First, an update on our Q3 FY2023 income performance**

- **Revenue from Operations** grew by 17% YoY to ₹8,654 million. This was mainly driven by our new lease-up at higher spreads, contractual rent escalations, delivery of our 1.1 msf JP Morgan campus at ETV and ramp-up of our hotel business. This was partially offset by the impact of exits in our office portfolio over the last year.
- **Net Operating Income ('NOI')** and **EBITDA** grew by 13% and 14% YoY, respectively. This was primarily driven by an increase in Revenue from Operations, partially offset by the increased hotel operating expenses corresponding to our hotel business ramp-up. Our overall NOI and EBITDA margins stood at 81% and 80% respectively and continue to be best-in-class. Our NOI margins consistently remain around 86% for the commercial office segment, demonstrating its scale and efficiency.
- **Net Distributable Cash Flows ('NDCF')** stood at ₹5,045 million, up 2% YoY. The YoY increase in our NOI and EBITDA contributed positively to our NDCF, which was primarily offset by an increase in our interest costs. These incremental interest costs mainly related to the debt expense for our recently delivered buildings, as well as the ₹46 billion coupon-bearing debt raised to refinance our earlier Zero-coupon bond.

  Further, earlier today, our Board of Directors declared Q3 distributions of ₹5,033 million or ₹5.31 per unit, representing a 100% payout ratio. This brings our YTD distributions to ₹15.3 billion or ₹16.10 per unit. In the 15 quarters since our listing, we have now cumulatively distributed over ₹73 billion.

**Moving to our balance sheet updates**

We continue to maintain our fortress balance sheet with 27% low leverage, attractive 7.2% debt cost, AAA/Stable credit rating and a ₹108 billion proforma debt headroom to finance growth. Our debt strategy remains focused on active capital management and interest cost optimization by locking-in fixed rates given the inflationary environment.

Over the last 3 quarters, we have cumulatively refinanced or renegotiated over ₹42 billion debt at 120 bps positive spreads. As a result of this and our earlier refinancings, 65% of our ₹139 billion debt book carries a fixed rate of 6.7% for an average maturity of 2 years. Additionally, 27% of our debt carries a yearly reset date and the interest rate is fixed for the next 7 months on an average. Further, we are in advanced discussions for refinancing an additional ₹16 billion floating rate debt and are targeting around 45 bps positive spreads. Given our access to various debt capital pools across mutual funds, insurers, FPIs, banks and NBFCs, we are well-placed to refinance any upcoming debt maturities at best-in-class industry rates.

Further, in line with our ESG commitments, I am happy to report that our sustainable finance portfolio has now grown to ₹39 billion, representing 28% of our total debt book, which is one of the best in the industry.

**Lastly, an update on our FY2023 guidance**

As a recap, during April 2022, we had provided our full year guidance with a mid-point NOI of ₹27,030 million and a mid-point DPU of ₹21.70 per unit, both within a range of +/-5%. This guidance implies a YoY increase of 9% in NOI and an in-line DPU, considering the mid-point guidance. On a like-to-like basis, post factoring the impact of our Nov'21 ZCB refinancing, this DPU guidance was also 9% higher YoY, reflecting the efficient flow through of our NOI to distributions.

Based on our YTD performance, I am pleased to reconfirm this guidance. There has been a clear positive rebound in office leasing as well as hotel business, both of which are currently tracking at or ahead of our estimates. On the other hand, we expect interest costs to be higher than our initial assumptions, given the rapid rise in rates over the last 3 quarters. While rising interest rates have severely impacted global REIT distributions and resulted in widespread guidance downgrades, we are happy to report that the positive operational levers of our NOI have been able to largely mitigate the increase in interest costs.

Looking beyond FY2023, our new lease-up, contractual rent escalations, mark-to-market rent growth, and scheduled deliveries will act as significant growth levers, thereby accelerating our growth to the benefit of our Unitholders.

Over to Vikaash for his concluding remarks.

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**Vikaash Khdloya**

Chief Executive Officer (CEO)

Thank you, Abhishek.

So, we continue to deliver consistently and are moving forward on our growth trajectory.

On the business front, Q3 was another strong quarter with 1 msf leasing and uptick in our same-store occupancy to 88%. With 4.4 msf leases already signed year-to-date and a promising 850k sf pipeline, we are well-positioned to deliver on our annual guidance. We continue to unlock value, as demonstrated by the FAR enhancement projects across Embassy Manyata and ETV which will add 1.2 msf to our total leasable area at highly accretive 22% yield. And we remain focused on our 6.6 msf development growth investments, estimated to add around ₹8 billion to our NOI upon stabilization.

On the capital markets front, amidst significant declines in global REIT stocks, Indian office REITs have been resilient and infact significantly outshined their global peers. This was largely driven by the continued offshoring demand, impressive leasing spreads, development growth at attractive yields and low leverage of Indian REITs. Given wider understanding of the yield plus growth total return story combined with our consistent 15 quarters of business delivery, Embassy REIT provides one of the best risk-to-reward profile. Our Unitholder register continues to expand, with our retail base increasing around 18x since listing to over 70k investors.

We continue to focus on growing our NOI and distributions by developing and acquiring quality properties and delivering long-term value to our Unitholders.

With this, let's now move to Q&A please.

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# QUESTION & ANSWERS SESSION

*(Note: The Q&A has been edited for clarity)*

**Moderator:** Thank you very much. We will now begin the question and answer session. The first question is from the line of Kunal Tayal from Bank of America.

**Kunal Tayal:** My first question was around the leasing intensity for corporates. There has been this news flow around layoffs in the tech sector. And I very well understand that the direct impact on India or the plans for direct layoffs in India could be quite less and there's the long-term offshoring trend as well. But I was just wondering if this kind of news flow might be enough for corporates to start thinking about pushing out new lease plans for 6 to 12 months. Is that something that you have seen or does it continue to be unchanged versus three, six months back?

And then the second question is around the DESH policy. Any clarity as to when that could get done? We've seen it get pushed twice over. And I was just thinking about the 97% occupancy ex of your SEZ spaces. I'm wondering if policy clarity would become a bottleneck to losing next year?

**Vikaash Khdloya:** Thank you, Kunal. Let me take the first question on leasing. There are a couple of interesting things that's happening right now. One, obviously, we are hearing the overall macro commentary globally and a bit in India as well, on layoffs. But I would just like to state that employment or recession trends are cyclical, whereas the talent and cost advantage that India has is structural. So, that's a huge advantage we have. What we have seen is that the layoffs in India are comparatively limited and concentrated to a few pockets. The elimination of roles is happening in fewer areas, but companies continue to hire in other strategic areas, including R&D, and we are seeing a lot of that.

In general, I would say that we have seen a couple of things. One, demand continues to be led by global captives. We do think that on large deals, i.e., 800k sf to 1 msf plus, we will see increased caution, and hence, decision-making may be slow over the next two quarters. But we continue to see robust deal pipeline and momentum. If you also look at our advanced leasing pipeline that we've indicated of 850k sf for Q4, you'll see that on the smaller and mid-sized requirements, we continue to see the momentum ongoing. We do think that large deals will slow down for the next two quarters, but then pick up in the second half of this calendar year. And the reason is simply that the global corporates right now are revaluating their strategy, and they are firming up the decision on overall cost optimization measures given the macro uncertainty. But once they arrive at a decision, the India cost advantage will stand in stark contrast and more work will come to India. We are firm believers of that. We have seen that in the past, we continue to believe in that.

We are well positioned to continue to focus on the smaller and mid-sized requirements until we see the momentum on the large requirements. Interestingly, even within the deals that we are seeing, we are seeing that the geographical mix is expanding. So, besides just US banks and US captives, we are now seeing many European and Australian banks setting up and expanding offices in India. We have done a couple of such deals in this quarter and the previous quarters.

We are also seeing global captives from newer sectors setting up shops or expanding. For example, apart from banks and financial services, we are now seeing a lot of retailers, insurers and healthcare majors setting up their R&D centres, and a lot of those examples as well. The key is to be nimble and flexible in the solutions, and we think that we'll continue to see the demand momentum, albeit for the larger deals, we'll see that pick up only in the second half of this calendar year. So, that's on the leasing trends.

Coming to the DESH policy. There are two things here. One, the industry as a whole is awaiting clarity on the DESH policy where the ask simply is to provide flexibility especially on the strata floor-by-floor de-notification. I think it's an industry-wide issue. Kunal, my personal view is that we may see one or two quarters before there's a final resolution to this. Of course, there's been a lot of advocacy by the industry participants on this. But in the meantime, the way we have approached this, given it's an external factor, is in a two- or three-pronged strategy.

One, we are full up on our occupancy, as we mentioned, 97%, excluding the SEZ vacancy. On all the new developments that we are doing, we have converted or planned them as non-SEZ, including all the developments that are coming up in later half of this year. So, we deliver about 1.7 msf in the next two quarters, all of that is planned as non-SEZ, so we can offer that to the market.

Two, for about 1.3 msf of the existing SEZ vacancy, we are exploring and have already initiated conversion to non-SEZ by exploring moving some of the SEZ tenants to other buildings and de-notifying the entire building. So, 1.3 msf is in process under that route. And then finally, the advocacy efforts continue.

Given that we have more supply coming up in terms of new product and we are focused on the precommitments on the 6.6 msf, we think that we will be reasonably fine in terms of the leasing momentum for the full next year. We will obviously lay out a guidance next quarter. But for the first two quarters, the applicability or announcement of the DESH or SEZ policy may hamper or slow down the ability to lease up our strata SEZ vacancy.

Just in terms of numbers. Today, we have about 4.8 msf of total vacancy as of December. Of that, 4 msf is SEZ, and as I mentioned, 1.3 msf of that we are converting to non-SEZ, which we have the ability to do through the existing framework. And another 0.7 msf of non-SEZ vacancy.

So yes, it means that for the next two quarters, there will be a little bit of a challenge given the conversion. At the same time, given we have a massive under-construction and about-to-be-delivered pipeline, I think, we will be reasonably better off compared to the market.

**Ritwik B:** Can I just add one small piece to that, Kunal? We can't understate the efforts of the advocacy program here. I think the ministry and the government has been lobbying really hard to make sure that this happens. This is a big year for India. At the end of the day, we have differentiated ourselves and the markets have held up well relative to where China is. And yes, China is opening up, but India has done very well. This is a year that we host the infrastructure, the G20, there's a lot of focus from tenants as well, who are clearly looking for non-SEZ spaces. As we said, the demand for that's off the charts. And my sense is, thinking a couple of quarters down from now, is when you'll probably see a sort of resolution start to kick in. But they're all focused on it, the government is aware of that, and it's something that I think we will be able to get some clarity on.

**Kunal Tayal:** Sure. I understand that. And it seems like new addition is very timely. If I can push in a follow-up here. I wanted to understand these 1.3 msf of conversion. Is that expected to be operationally and financially smooth or what might that involve?

**Vikaash Khdloya:** Kunal, one of the recent 0.9 msf deliveries in Pune gets converted and we expect that to happen anytime in the next month or so. And then for one of the earlier buildings in Manyata where we had a legacy IT services occupier vacate, we also relocated few smaller tenants within this SEZ building to ensure that the whole building is vacant and available for de-notification under the existing regulations. We expect that to happen in the next two or three months, and we are already in discussions to backfill the space. So, I think the 1.3 msf is very near term.

**Moderator:** The next question is from the line of Puneet from HSBC.

**Puneet Gulati:** Thank you so much for the opportunity and very happy to see you making extra efforts here on converting into non-SEZ. My question again is on Manyata. So, the 0.36 msf which will be expiring next year, is that also SEZ? And is there any visibility on that getting re-leased?

**Vikaash Khdloya:** For the next year, about 30% of the expiries in our overall portfolio is SEZ and 70% non-SEZ. We expect 0.9 msf of expiries next year, but in the business of this size, we may always have an extra 100-200k sf. We think a large majority of that will be renewed. We don't think extra SEZ space will be added to the stock at end of March 2024. I think it will be about 100-200k sf additional SEZ space, which will not be renewed at the end of FY2024, as per estimates as of today.

**Puneet Gulati:** So, you're saying out of 0.3-0.4 msf, you will still be able to renew at least half of it?

**Vikaash Khdloya:** Yes, we think a little higher than that.

**Puneet Gulati:** The second question is on the NDCF for ETV. That seems to be lower on a QoQ basis from ₹208 crores to ₹172 crores. Anything to highlight there?

**Vikaash Khdloya:** Abhishek, would you want to take that?

**Abhishek Agrawal:** So, if you look at quarter-on-quarter, the NDCF is lower largely because during the current quarter, we have received lower security deposits as compared to the previous quarter.

**Vikaash Khdloya:** Just wanted to mention that while we appreciate a quarterly comparison, but in general, we look at it more from a year-to-date or full year perspective because there will always be some movements on security deposits and working capital quarter-to-quarter.

**Puneet Gulati:** Lastly, just on the hotel. From industry commentary, we seem to be hearing that occupancies are much higher, but all your hotels are still sub-50%. What should we read into that?

**Vikaash Khdloya:** Puneet, if I can speak to the Slide 34 of our earnings deck. At Hilton GolfLinks, the occupancy was low this quarter, one, for seasonal reasons; and two, given the holiday season, the back to work was lower during the month of November, December. But we are seeing pre-pandemic levels, both on ADR and this quarter is looking pretty strong.

On Four Seasons, if you may recollect, this was the hotel where we had pretty low ADRs to start with. So, we have re-strategized and have changed the entire team at the hotel on the operating level, and we have raised the ADRs now to over ₹15,000. So, you will see a nice uptick in EBITDA even though the occupancy still remains low at around 31%. The target is to take it up to 50% in the next two quarters.

And Hilton Manyata is actually a good success story because within the first year of operations, it is throwing a positive EBITDA for a hotel of this scale, 619 keys. And as of today, the occupancy is 50%. While we have not shared the occupancy numbers between Hilton Garden Inn and Hilton in our materials, Hilton Garden Inn is doing pretty well. There, the objective is to hike the ADRs. But Hilton, the larger hotel which was launched later and at a more premium offering, the occupancy level is at about 40%, and we are trying to move the occupancy levels higher there. That's the segment which depends on business travel from senior executives. And that's where in November, December, we saw some amount of slowdown.

Overall, I would say we are well on track. And in fact, we expect the EBITDA on our hotels to be more than double than our underwriting. So, I think our hotel business is on a good trajectory. We will continue to see quarter-on-quarter improvement. Q3 has slowed a little bit for two reasons, one, the holiday season; two, some of the festive

season that's happening. And most of the Bangalore hotels and our hotels in particular are more positioned to corporate travel than leisure travel.

**Moderator:** The next question is from the line of Mohit Agarwal from IIFL.

**Mohit Agarwal:** My first question is on the new supply. So, you mentioned that the 0.9 msf in Pune that you are now getting converted into non-SEZ. So, what is the kind of demand that you are seeing there? Considering in earlier calls, you have mentioned that Pune has been slow and you have mentioned today that you are seeing some recovery. So, if you could give some colour on that? And also on the 1.7 msf that is going to come up in the next 6 months between M3 and Oxygen?

**Vikaash Khdloya:** Sure. So, on Pune ETZ, where we have delivered the 0.9 msf, we are converting to non-SEZ and expect it to go through in the next 1 or 2 months. So far, what we have seen is that Pune as a market is recovering, but the traction is more on the east side through the banks and financial services client base. For West Pune, demand still remains muted. While we have done some deals, but mainly it is awaiting clarity on the DESH bill, although we have seen some early signs of pick-up.

What we have done in Pune is we have done 2 or 3 leases of about 150k sf in the new building. Our pipeline currently is about 400k sf for Pune, 120k sf of that is in advanced discussion and that's included in our 850k sf overall leasing pipeline for Q4 that we indicated. And most of the enquiries are for non-SEZ.

Of the entire vacancy that we have in Pune, half of it is SEZ. That has been a marketing challenge. We have seen existing occupiers expanding, we have seen some of the European captives in automobile and renewals. We are speaking to them, and that's included in the pipeline. We are also seeing some new tech players across healthcare looking at space. And maybe 2 or 3 quarters down the lane, while it is including the 400k sf pipeline, we have some large Fortune 500 American corporates who are looking to set up centers in Pune.

I would say that Pune is expected to be slow for the next 2 quarters, awaiting both clarity on DESH bill and on the SEZ side. And the back to office on Pune has been slower than what we have seen overall in our portfolio as well as in Bangalore and ETV especially. So, I think we'll have to just be patient on Pune.

The good thing about our portfolio, with the scale that we are operating is, we can play the patient game in markets where there is muted demand. We think it will come back. But as of now, next 1 or 2 quarters, we expect the traction to be at similar levels with what we have seen.

**Ritwik B:** Our entire strategy of building is building to where we foresee demand in the future. Given that it takes 3 years from putting a shovel in the ground to actually getting a building up and running, I think we never want to be in a situation where we are caught offside, and particularly in these kinds of volatile markets where interest rates have been rising or the cost of construction has been swirling around a bit.

We just want to make sure that we have the two buildings ready and for us to put that into a market where there is obviously demand from automotive, from renewables, from people looking to do EV. Over time, we feel pretty good about the project and the prospects.

**Vikaash Khdloya:** And, Mohit, if I can just add on the 1 msf in Manyata that we deliver next quarter, there, we are seeing pretty robust pipeline. So, we have about 400k sf of advanced discussions, which is included in our 850k sf pipeline number. And just to give you a flavour of the occupiers we are talking to, we are talking to an IT infra services occupier and we are talking to a global engineering and consulting occupier there. We are looking to convert 400k sf by the time the building is delivered next quarter, in line with our usual target of having 50% of the building pre-committed by the time

it is delivered.

And on Oxygen, which is the 0.7 msf tower in Noida. Again, Noida, given that most of the buildings are SEZ, this is also an SEZ building and is in the process of being converted. The delivery comes up sometime in June or July of 2023. We are talking to one Fortune 500 big tech company, and we will see how it goes. So, that's in intermediate discussions. But I would reiterate that Bangalore continues to see a lot of strong traction. Pune, Noida, we think it will take a little bit more time to lease up.

**Mohit Agarwal:** And how much time does it take to de-notify from the time you start the process?

**Vikaash Khdloya:** Usually, it takes about three months. But in certain states like Noida, it is the first time that it is being done in the state itself. So, that takes a little bit more time for the regulators to just figure out the processes internally. But typically, in Bangalore, we see it happening in 3 months.

**Mohit Agarwal:** And my second question is on the rental growth. So, in an inflationary environment, one would want to believe that you would be able to push higher rentals to account for the overall inflation and higher interest rates. So, I wanted to get your thoughts, have we been able to do that? Or are the market forces not allowing that?

**Vikaash Khdloya:** So Mohit, the short answer to that is, yes, we are seeing rental growth. In fact, a Knight Frank office report earlier this month had mentioned that Bangalore has seen a year-on-year increase of 11% in rents for the market overall. We continue to lease at a premium to the rent that CBRE expects for our properties. This quarter, for our overall leasing, we have leased at 5% premium to market rents. And obviously, the spreads are much higher if you take into account the renewals and in-place rents.

So, you are absolutely right, in an inflationary environment and especially with interest costs rising, we will see the replacement values of the properties go up, which would mean two things. One, it will mean that supply will decline, and we have already seen that last year, as announced supply which the IPCs expected to be delivered versus what was actually delivered was lower. We continue to believe that the supply will be constrained. And two, we will also see rental growth. We are already seeing that in Bangalore. Many of our discussions in Bangalore are not centred around rent, it's just centred around solutions, timing and flexibility to the occupiers and quality and wellness. And we think over time, that will flow through to Noida, Pune as well. So yes, rental inflation is likely. We have already seen that in Bangalore, and we are trying to see how best we can convert that into NOI growth in our portfolio.

If you see our in-place rent versus market rent and the gap, over the last 4 to 6 quarters, we have narrowed that gap considerably. That's obviously because of the renewals happening at mark-to-market at higher spreads. Plus, as we see better back-to-work ramp-up, which we have already seen a good uptick this quarter, we will also start seeing even healthier rental growth, not just in Bangalore, but in other cities over the next 2 or 3 quarters. And that will also mean that the portfolio will start catching up to those newer rents as leases expire or come up for renewal or new leases come in. So yes, rental inflation is something we are seeing, and we believe it will be demonstrated in the leasing as we move forward.

**Moderator:** The next question is from the line of Kunal Lakhan from CLSA.

**Kunal Lakhan:** Vikaash, you mentioned that your physical attendance has been ramping up and you were at 46% last week. Just wanted to understand, in your discussion with your occupiers, say, at what level of physical attendance do you think occupiers will be compelled to look at new office options?

**Vikaash Khdloya:** Sure, Kunal. We have a slide in the deck, which I can point to, but let me give a flavour of what's happening in the portfolio. It's really interesting that the trends that we are seeing are not similar for all the cities, for all the kind of occupiers as well as for all

properties. If you see Slide 30, let me walk you through that and what we believe would be a trigger point.

So overall, we saw that our physical attendance was 46% for our properties earlier this month in January. Mumbai is already at pre-pandemic levels of 75%. Bangalore has shown a nice uptick, and it is now at around 45%. In fact, ETV is already at 60%, and that is why we see a lot of precommitment activity and pipeline at ETV. ETV again, if you recollect, has a very high proportion of global captives.

In Pune and Noida, back-to-work has been slow. It is around 40% or slightly lower. And that is simply because the IT services back-to-work has been slower overall compared to the captives and compared to the big tech. We believe that at around 50-55%, occupiers will be compelled to just look at their space strategies, and to firm up with decisions, both on medium-term, as well as on long-term. We are already seeing that happening for banks, healthcare and retail captives. We think that will also translate and trickle down to the big tech and the product tech companies that we speak of. And I think the IT services companies will be the last to come in. The back-to-work is slower in IT services, although we have seen very positive commentary by the CEOs who are trying to push and nudge people back to work.

So, I think at 50-55%, we'll see a trigger. We are already seeing that in certain segments. If you see, we have early renewed with a healthy uptick, although we had contracted for a much later timeline, with a global retail captive and leased-up additional space to them in Manyata. Also, banks continue to feature in our pipeline.

And a 50%-55% overall physical attendance will require the companies to look at their plans because I think it will never be 100%. It was never 100% pre-pandemic. I think somewhere around 70-75% is what is being expected. And at 50-55% level, they will need to start factoring in more space.

We have not seen conversations around desk sharing, that's the conversation that's not happening. There will be flexibility and so there will be a certain amount of work from home. But majority of the time, the business leaders want people to come back to office, and there's a lot of requirement of space to be re-modelled. That discussion is happening, both on creating more social spaces and a larger per person seat space.

**Kunal Lakhan:** So, 50-55%. Going by the traction that you are seeing, say, about 1 or 2 quarters, we should be there?

**Vikaash Khdloya:** Yes. We think so too as well, Kunal. And that's why we said the second half of this year, we believe that we will see traction on the larger leases. And by that time, global corporates will also firm up their long-term plans. Because if they come to India, they have to think of a 5 or 10-year commitment, if they are offshoring an R&D process or any other centre. And I think by that time, they will also be able to get internal approvals on the capex requirements to set up or offshore more to India.

**Kunal Lakhan:** My second question was on the financials. So, on a 9-month basis YTD, we have seen a 12% growth in the NOI. But on NDCF basis, we've seen a decline, and understand it is so because of the conversion of the zero-coupon bond and so on and so forth. But going into next year, can we expect the NOI growth to also reflect into NDCF growth? Or there could be a disconnect there?

**Vikaash Khdloya:** Kunal, while I will request my colleague Abhishek to answer, but we will refrain from commenting on the next year. In general, given the leasing momentum for next year, we are targeting to deliver double-digit NOI growth, and there are a couple of factors which will determine the DPU trajectory – interest rates and DESH will be 2 of them. But certainly, we will give more flavour in the coming quarter when we lay out our annual guidance. Abhishek, do you want to speak through what you are seeing for FY2023 this year?

**Abhishek Agrawal:** Yes. So, Kunal, on a YTD basis for this current year, it is the zero-coupon refinancing and also the interest cost on the loan for the deliveries that we have done during this year, both have come and hit the NDCF this year. Going forward, you will see all the leasing that has happened during the current year will definitely go to the NOI and will flow through because of our efficient flow through from NOI to NDCF. However, the interest rates have risen, and we will have to refi certain loans. So, all of those factors will also play into it, and we will give a guidance the way we are giving every year.

**Ritwik B:** Kunal, if you just lay out the picture right now, for the longest time, we have actually hit guidance in the past. We are very cautious about this. You have to understand that our distribution flow through, unfortunately, is also dependent on absolute interest rate environment, which isn't really conducive to financing. If you think about global REITs, people who were financing at 2-3% historically, they have obviously moved into a volatile financing scenario, where now, effectively, they go from 2% to 4%, that's sort of doubling their interest cost and their cost of capital. We moved from, call it, 7% to somewhere in the 8%, and we are still the best credit in the industry.

Overall, what we try is to make sure that we don't overpromise something on a distribution basis that then is very hard for us to sit there and manage. At the end of the day, we build growth through the scale that we have in the portfolio, and we try and buy growth from outside, and then to the extent we can manage the drop downs efficiently, we do that.

And in this kind of an environment, I think the biggest risk which we have already kind of managed is the interest rate risk. It is baked into our stock. It is baked into our ability to get the financing that we do and we are getting some very, very attractive offers as well. So, with that in mind, we just don't want to overstep and tell you that we are going to be able to deliver some kind of growth, which clearly, in a volatile environment, would be a bit imprudent.

**Vikaash Khdloya:** If I can just conclude that. We, as management, are focused on NOI growth because NOI growth in the long term, will deliver value and will flow through into the NDCF or our distributions. For example, if you are seeing new buildings being built and delivered, of course till the time the building gets stabilized, let's say 1 year, the interest costs will be a drag to the NDCF. But if you look at it from a three-year horizon, from a unitholder perspective, what we need to be doing is keep delivering newer buildings and start trying to stabilize them as soon as possible.

So, NOI growth is our focus. Given that 100% of our debt is coupon bearing, there will be efficient flow through as and when the buildings start getting stabilized and the rents start flowing in. And given the levers that we have both on mark-to-market, lease-up, which we have already seen a rebound on the same-store basis, as well as escalations on the new deliveries and their revenues, we think we are well placed to target a double-digit NOI growth in this coming year.

**Moderator:** The next question is from the line of Karan Khanna from Ambit Capital.

**Karan Khanna:** Just a couple of clarifications. So, on the mark-to-market side, while Bangalore opportunity remains strong. Mumbai and Pune have seen a downward mark-to-market of the expiries in FY2024 to FY2026. So, can you help elaborate this further, as in case of FIFC, which is in BKC, we are seeing new leasing being done in excess of ₹300 per square feet, while your mark-to-market report is only ₹275?

**Vikaash Khdloya:** Karan, the market rent assessment is a third-party assessment of CBRE and they have been kind of more conservative on Pune given that Pune market has been sluggish. Some of the leases that come up for expiry and renewal next year in Pune as well as in Mumbai, in Mumbai, it is very typical, but in Pune as well, given the contracted escalations that these are 8-10-12 year leases, there may be a slight mark-to-market downward. But I think that is not material, it is a judgment thing,

whether it is a ₹48-50-52 market in Pune. So, we are not overly worried about that.

In FIFC, of course, we are trying to see if we can push the rents higher. Given Mumbai contributes a small portion, and the fact that this building has a co-owner, I think the valuers have been conservative. But we have consistently tried to lease at about ₹285 to ₹290 per square feet or higher.

**Karan Khanna:** And secondly, on your hotel portfolio, while we have seen the physical occupancy increasing, the hotel occupancies have stagnated or perhaps were declining in the last quarter. Just wanted to understand what office or park level of physical occupancy do you see the hotels starting to benefit as well?

**Vikaash Khdloya:** There are a couple of things here. While the hotel occupancy in Q3 has declined, let me break this down into 2 or 3 pieces as I mentioned it earlier during the call. GolfLinks' hotel occupancy was obviously linked to two factors; one, the GolfLinks' back to work in November, December given the holiday season and given all our hotels cater to corporate clients, there is very minimal leisure travel involved. So, it is all corporate and, hence, Q3 generally has been a slower quarter comparatively, still much better than the pandemic period. GolfLinks has been slightly impacted, but at about 40-50% levels of back-to-work, we think the hotel can reach pre-pandemic occupancy levels of 70-72%.

Coming to Four Seasons. As I said, here, we are focused on repositioning the hotel, given that it contributes negligibly to our NOI, and we have raised the ADR substantially from earlier so what we are adhering to the standard of what a Four Seasons hotel should be charging. So, that's second.

And third, on Manyata Hilton, given that it is a large hotel and is still stabilizing, and I mentioned the larger Hilton format was launched later and the senior level business travel is still picking up, we saw occupancy levels of 49%, which I think, for a 619-key hotel, within the first year of its launch, is still fantastic.

So overall, I would say, hotels will see a consistent overall growth trajectory. For example, if I were to give you a forward-looking flavour, there are citywide events such as G20, Aero Show, Petro Conference, which are expected to generate additional demand, especially in Embassy Manyata Hilton in Q4. So, we think hotels will continue to stabilize and continue to deliver incremental NOI quarter-on-quarter. We are well placed for that.

**Karan Khanna:** And lastly, if you could give us some ballpark understanding in terms of having seen the entire commercial real-estate space over the last couple of decades, by when do you expect the occupancies to perhaps touch your pre-COVID levels of 95%? And if you think that the same is achievable even without the SEZ benefits?

**Vikaash Khdloya:** That's a very interesting question, Karan. Let me put it this way. By the end of this year, we are looking to go back to the early to mid-90s and we have a path towards that. If you see the expiry profile next year of 0.9 msf and even factoring for additional vacancies or expiries that usually come up as a normal part of business, we expect a large proportion of next year's expiries to be renewed. Plus, we have seen uptick and positive momentum in net leasing given the large occupier who had legacy leases and was vacating on a staggered basis, that has ended in September. We think we have a path to occupancy levels of early 90s in the next 2 to 3 quarters on a same-store basis.

Again, I would like to impress what I mentioned earlier that we would like to emphasize and focus on NOI growth, simply because we think leasing, let's say, at a Manyata or ETV and achieving premium rents at a faster velocity, contributes higher to NOI growth than, let's say, at a Pune or a Noida. It is not to say that the efforts are not being made at Pune or Noida. So, NOI growth is purely what we would like to guide you and to request you to focus on.

Occupancy levels can be misleading because we would not do deals just for the optics purposes. We are very selective on our occupier profile who will continue to grow. As I mentioned earlier, we have a path towards early to mid-90s in the next 3 to 4 quarters on a same-store basis. We have already seen an uptick.

If you see our guidance on the leasing pipeline of 850k sf, roughly half of that is fresh leasing and half of that is under-construction pipeline. And if you see our exit profile for Q4, it is negligible. So, if you just do the math, we will be close to 90% on a same-store basis by next quarter itself. Obviously, it all depends on if we can execute and get the leases signed. And on the NOI trend, as I mentioned already earlier, we are targeting a healthy double-digit NOI growth next year, and that is our core focus.

**Moderator:** The next question is from the line of Ravi Agarwal from Mirae Asset Investment Managers.

**Ravi Agarwal:** My question is largely a clarification. On the CF loan taken by the Embassy Property Developments and there was a delay in the servicing of the repayment, citing some regulatory issues. So, I would just like to have an update on the status of that and would like to also confirm if there any liquidity issues or delays which have been still going on?

**Vikaash Khdloya:** Ravi, thank you for the question. Let me take this and Ritwik or Abhishek, please feel free to add in. So, a couple of things. One, it's more appropriate for this question to be directed to the Embassy Sponsor. As a principle, we don't want to comment on market speculation and news, especially around our Sponsors.

As we have highlighted in our Q3 results and as Abhishek spoke, our operational and financial position remains strong and we are on track to deliver on our guidance and we have AAA/Stable rating, both from CRISIL and CARE on our balance sheet. We have very conservative leverage, best-in-class interest rates and negligible debt maturities this fiscal. We have access to a wide investor debt pool across mutual funds, insurers, FPIs, banks, NBFCs and corporate treasuries. And we do not see any impact on the REIT itself and we do not want to comment on market speculation.

**Moderator:** The next question is from the line of Arun Kumar from Unifi Capital.

**Arun Kumar:** Hearty congratulations on the leasing traction. Two questions. One, over the last three years, the NOI margin has been, on an average, around 85%. But in this financial year, over the last three quarters, it is somewhere between 81% to 82%. And as it has been explained in the presentation, it is due to the product mix between the commercial office space and the hotels. So, is the 81% to 82% the new range or is there any scope for improvement in the NOI margins?

**Vikaash Khdloya:** Thank you, Arun. And why don't I ask my colleague, Abhishek, to take this question?

**Abhishek Agrawal:** Thank you for the question. Actually, you have put it rightly. Earlier, the NOI margin was around 85-86%. Now, the NOI margin has gone down to 81%. This is because of the product mix and what has happened is during the current quarter and the just previous quarter, the revenue from office has not increased so much, but the revenue from hotel business has increased a lot. So, the product mix has changed. But having said that, we have done so many leasing during the current 9 months, the revenue from that will start flowing in from the next quarter or the quarter next. So, the mix can again go back to almost a similar range. So, you can expect anything between 81% to 85% to come back.

**Vikaash Khdloya:** There is a little bit more flavour on the segment mix and segment-wise margins in Page 13 of our supplemental data book. But the way we look at it is, we will have more hotels come up. And as hotel revenues increase, with ETV hotel and all coming up, the overall consolidated ratio of NOI margin will be misleading. That is why we have segregated for office and other segment. Office, we consistently have been at

around 86%, if you see the year-on-year and the quarter-on-quarter trend in that Slide 13 of the supplemental data book. So, you will have to just factor for the segment mix and see the segregated ratios. Office remains best-in-class. Hotel margins, obviously, the nature of the business is different than office.

**Arun Kumar:** And my second question, with the 6.6 msf that we are planning to add and the ROFO assets, do we need additional equity to fund them? And we have also approved raising of debt by another ₹5,000 crores. So, what is the level of leverage that you would be comfortable with? And does AAA rating warrant you to maintain some specific level of leverage?

**Ritwik B:** Firstly, we have got to break down the square footage. So, you have got 6.6 msf of development that is in-house, that we typically fund through debt – bonds at the REIT level, term loans, LRD at the SPV level. So, for that we do not think about any other source of financing beyond what we have laid out in our supplemental deck, and we are very comfortable with that.

Now, an acquisition is something that is a little different. That is obviously a function of the financial markets, where it could be debt, a mix of debt, mix of equity depending on the market conditions. Take ETV, for example. When we did Embassy TechVillage acquisition, we did a placement for that. Market conditions obviously played a big role in the way we looked to finance that transaction. So again, typically, for the in-house construction and development, we wouldn't be looking to go out there and raise equity in these kinds of markets.

**Vikaash Khdloya:** Arun, just to add to what Ritwik said, the ₹5,100 crores that you referred to, in terms of approval for debt raise, that's just a provision. It is not the intent that we go ahead and raise it right now. We do not have a use of proceeds. We have never raised that unless we have a clear sight of where we are using it for. That is an enabling resolution because there are maturities that are coming up.

Let me break down the thought process of ₹5,100 crores. ₹1,000 crores of that, today, as we speak, we have refinanced some of the existing loans close to ₹950 crores at sub-8% rate. So, we have used ₹1,000 crores of that limit to refinance existing debt, again, to manage and optimize on interest cost, that's one. The balance ₹4,100 crores is towards an enabling resolution as we have, in the second half starting October and February as we have included in the deck, we have expiries coming off existing bonds. And we have the data in our presentation on Slide 37.

So, it's an enabling resolution to ensure that we have flexibility to refi the existing debt. So, there's no intent to borrow additionally. The only borrowing, as Ritwik mentioned, we will do is for new construction and if and when we go ahead with an acquisition. Again, if we were to do the entire 6.6 msf development, even assuming that the value of the building does not increase, which means the denominator for the leverage ratio does not increase, we will still not reach the 30% leverage. And we, as management, are very comfortable with debt levels of around 30% on net debt to GAV.

On the acquisition front, as Ritwik indicated, the size of the acquisition is expected to be less than 4% of the GAV of the company. So, the acquisition is strategic as we are looking at it and if we were to negotiate and announce, but it is less than ₹2,000 crores. It will typically be funded by a mix of debt and equity. Overall, I would say that we are not looking at reaching the 30% figure on the leverage that we as management are comfortable. However, in the medium term, if there is a transformative acquisition like an ETV, we are comfortable at around 35% overall. We would not like to breach 35% in the next 3 to 5 years.

**Arun Kumar:** Yes. And to your last point, on the AAA rating, what is required?

**Vikaash Khdloya:** Yes, they are typical covenants. And being able to access a ₹1,000 crores debt at

sub-8% in today's market just speaks to how we have managed and maintained the balance sheet. Yes, there are couple of covenants typical to AAA rating, including EBITDA coverage. And we are very comfortable with those leverage ratios, including for factoring for any potential organic or inorganic growth. We always factor what it means to our debt covenants when we undertake additional growth.

**Arun Kumar:** One final question. We are targeting a double-digit NOI growth next year. So, would the same double-digit target into DPU as well?

**Vikaash Khdloya:** So, Arun, again, we didn't want to give a guidance or an indication for next year. What we were alluding to is that given the levers that we have, we should be back to the double digit. We have always stated that we would like to target a mid-teens NOI growth as a business given the four levers that we have of mark-to-market, lease-up, escalations and new delivery. We would not want to layout our guidance on NOI and DPU today. We will come out with the guidance next quarter.

But again, I would want to impress and request everybody on the call that our focus is on NOI growth, simply because NOI growth will eventually translate and flow through into distributions. The DESH bill as well as the rising interest rates will have a bearing on the distributions. But we are looking at growth, and we think that if we can deliver the growth at those 24% yield on the construction, having a fantastic spread given our cost of financing is at around 8% handle, and yields that we are doing on new development is 24%, we think we will be able to deliver DPU growth in the medium term if we can focus on NOI and grow that. So I will leave it at that. But yes, our focus is to enhance the overall value. We are not overly focused on distributions. Distributions will come in and it will flow through. We are also not focused on occupancy. We are focused on NOI growth.

**Moderator:** Ladies and gentlemen, due to time constraint, we will take one last question, which is from the line of Samar Sarda from Axis Capital.

**Samar Sarda:** I had a follow-up question with respect to SEZs and the de-notification. While we have seen a lot of landlords who de-notified vacant lands and in a couple of instances also under-construction buildings. If you could help us, if there is any precedent of the number of months or how much time does it take for any other buildings, which are ready, occupied, and then vacant, which have been de-notified in the past?

**Vikaash Khdloya:** Samar, thank you for the question. Typically, assuming that the building complies with the requirements of de-notification, which specifically mean that the entire building needs to be vacant, and also that the support infrastructure needs to be segregated, it typically takes around three months in states which have done it previously. In Noida, we have experienced that it is taking longer, but it is very typical in Bangalore to get it de-notified within three months of application. Abhishek, would you want to add something?

**Abhishek Agrawal:** Yes, there are other conditions also like contiguity etc., all of those conditions need to be met for these timelines to be basically adhered to.

**Samar Sarda:** But do we have precedents of that happening in Karnataka?

**Vikaash Khdloya:** Yes. We have done de-notifications, not post acquisition, but pre-acquisition, it has happened at ETV a couple of times and similarly at Manyata as well. So, de-notification of a full building block is a procedural routine business as usual, we would say. The challenge we are facing today, and the first question by Kunal on the DESH policy, is what do we do of buildings which are half vacant and half occupied in SEZ. The law today does not provide for de-notification of strata or floor-by-floor, and that's the challenge. So, if the entire building is vacant, and we comply with other conditions of contiguity and infrastructure segregation from non-SEZ, it is pretty procedural, three months is a fair timeline, and it has been done in the past.

**Samar Sarda:** Which we believe they're trying to change in the DESH bill with respect to the floors?

**Vikaash Khdloya:** Absolutely, you're right. The request from the industry as a whole is that the government allows floor-by-floor and also does it in a single window clearance on a self-declaration basis, so that they can just speed up the conversion process and the verification happens post facto. So, even that three months, we can bring it down to 7 days. So, that is the request from the industry.

Just to give you a context of SEZ space. In India, today we have about 180 msf of SEZ space, of which around 30 msf is vacant, and I am talking about Grade A spaces. Roughly, this is based on some published reports. And that is why this is a critical component of regulation that needs to be addressed. And that is why the industry has been in advocacy with the government.

**Samar Sarda:** And just a small follow-up on this, again, a little more operational. The DESH bill might come in over the next three months or over the next six months, it is a government-driven procedure. We have seen some other landlord peers who have been leasing space in their SEZs because most of the SEZs are campus-style developments and for expandability options etc. Obviously, it's not 100 out of 100, activity might probably be 20-25 out of 100. Are you guys also still evaluating options where tenants do come here? Or that's a complete loner until and unless the DESH bill clears?

**Vikaash Khdloya:** Samar, that's a good question. Let me break it to two things. One, what we have done and what is happening in the portfolio is where India is headed. In general, it would be fair to say that given the tax holiday has been phased out in SEZ, the demand has moved disproportionately to non-SEZ. That also reflects the fact that Indian occupiers and office demand has moved up the value chain, because the larger occupiers are in India not to save on rent cost, they are in India to access talent at scale.

So, we have seen global captives, they are just not bothered about the tax incentives. They want non-SEZ spaces because they want flexibility of operations and flexibility to grow their business. In SEZ, there are a bunch of conditions that need to be complied with. So, India office in general, has moved towards that, which is a great sign because it shows that the market is maturing and the propensity to pay higher rents by the occupiers has increased. We are moving more and more towards global captives and big tech, whereas, in the past, IT services would have been a large component of the new demand. So, that's one. So directionally, India has moved there. For the demand that we see in the market and the pipeline, it is safe to say over 90% of that would be non-SEZ enquiries and demand today.

Having said that, we do see SEZ demand. For example, year-to-date, we have done 2 msf of SEZ leasing, both pre-leases where we did a large pre-lease with a banking occupier in Manyata that was SEZ, and a large SEZ renewal. So, we are seeing SEZ renewals and new leasing. Even in Q3 alone, we did about 230k sf of SEZ leasing. These are mostly existing occupiers who are expanding with their existing SEZ benefits going on, but we have seen any new global captive or large, big tech taking up space or growing, it's all non-SEZ. So yes, we are being opportunistic where we can do SEZ leasing. We have done that in Q3 as well as year-to-date, 2 msf, including precommitments on new buildings. But the more usual enquiries we get is of non-SEZ.

**Moderator:** Thank you. I will now hand it over to Mr. Abhishek Agarwal for closing comments.

**Abhishek Agarwal:** Thank you so much for joining us on today's call and for your great questions. Most of the data points covered today can be found on our website and in the published materials, and we are always happy to engage further if any additional clarifications are required. Thanks again.

**Moderator:** Thank you very much. On behalf of Embassy Office Parks REIT, that concludes this conference. Thank you for joining us, and you may now disconnect your lines.