Practice and Prospect of Islamic Real Estate Investment Trusts (I-REITs) in Malaysian Islamic Capital Market

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Abstract

Over the past three decades, Malaysia has been in the forefront of global initiatives and efforts to establish a viable, sustainable and feasible Islamic Capital Market catering the needs of Muslims and ensuring that its products and services are attractive to all investors and issuers regardless races or religions. The development of a vibrant, efficient and effective Islamic capital market requires the creation of a broad spectrum of innovative Islamic financial instruments and the infrastructure to promote active trading so as to enhance the breadth and depth of the market. One of the most recent investment opportunity introduced in Islamic Capital Market in Malaysia is the Islamic Real Estate Investment Trusts or I-REITs. Islamic REITs funds invest their portfolios in listed real estate securities that own and operate real estate such as residential, commercial, and retail properties, storage facilities, warehouses and car parks. Islamic REITs differ from conventional property funds mainly due to the requirement to strictly observe Islamic investment guidelines and Shariah principles. Thus it provides new investment opportunity for investors who wish to invest in real estate through Shariah-compliant capital market instruments. This paper provides insights into the practice and prospect of Islamic REITs in Malaysia. The application and mechanics of Islamic REITs are examined in the light of Islamic REITs Guidelines issued by Malaysian Securities Commission. As will be evident in this paper, this instrument has its own advantages and value added which would make it the instrument of choice in meeting specific investment interests and needs.

Introduction

Malaysia has always been in the vanguard of global initiatives and efforts to establish a viable, sustainable and feasible Islamic Capital Market catering the needs of Muslims and also ensuring that its products and services are attractive to all investors and issuers regardless races or religions. Malaysia is also poised to be a global Islamic financial and capital hub, as envisaged in the Capital Market Master Plan launched by Malaysian Securities Commission in 2001.

Essentially, the development of a vibrant Islamic capital market requires the creation of a broad spectrum of innovative Islamic financial instruments and the infrastructure to promote active trading so as to enhance the breadth and depth of the market. An efficient capital market is also expected to provide opportunities for constructing well-diversified portfolios and to meet investors' demand in accordance with their risk and return preferences (Iqbal & Mirakhor, 2007).

In order to help propel the expansion of Islamic capital market in Malaysia, Securities Commission has recently introduced a new investment opportunity in the Islamic Real Estate Investment Trusts or I-REITs. To facilitate its development, the Securities Commission has issued the Guidelines on the Issuance of Islamic REIT. This guideline is the first guidelines on Islamic REITs in the global Islamic financial sector, essentially providing Shariah guidance on the investment and business activities on Islamic REITs.

Since the introduction of REITs, the Securities Commission has approved a total of 11 issues with market capitalisation of over three billion ringgit (Yakcop, 2007). Al-'Aqar KPJ REIT was the first Islamic REITs listed on the Main Board of Malaysian Bourse and believed to be the world's first Islamic REITs with a total market value of RM481 million (Idris, 2006).

This paper provides insights into the practice and prospect of Islamic REITs in Malaysia. The application and mechanic of Islamic REITs are examined in the light of Islamic REITs Guidelines issued by Malaysian Securities Commission. As will be evident in this paper, this instrument has its own advantages and value added which would make it the instrument of choice in meeting specific investment interests and needs.

The remainder of the paper proceeds as follows. The next section illuminates the nature and operation of REIT. Section three then delineates the characteristics of Islamic REITs as implemented in Malaysian Islamic Capital Market. Two case studies of Islamic REITs are offered in section four. Section five discusses the prospect of Islamic REITs in Malaysia, whilst the final section contains the concluding remarks.

Nature and Operation of REIT

The Securities Commission of Malaysia defines REIT as "an investment vehicle that proposes to invest at least 50% of its total assets in real estate, whether through direct ownership or through a single purpose company whose principal asset comprise real asset"(Securities Commission, 2005b). Different countries adopt different approach in determining the requirement for a REIT especially with regards to ratio of investing in real estate. In United States for instance, the main requirement for a

REIT is that it must invest at least 75% of company's total assets in real estate. As for Korea and Singapore, 70% is used as the minimum ratio of investing in real estate (Vincent, 1999: 69-104). Thus, REIT is an entity that accumulates a pool of fund from investors, which is then used to buy, manage and sell assets in real estate industry.

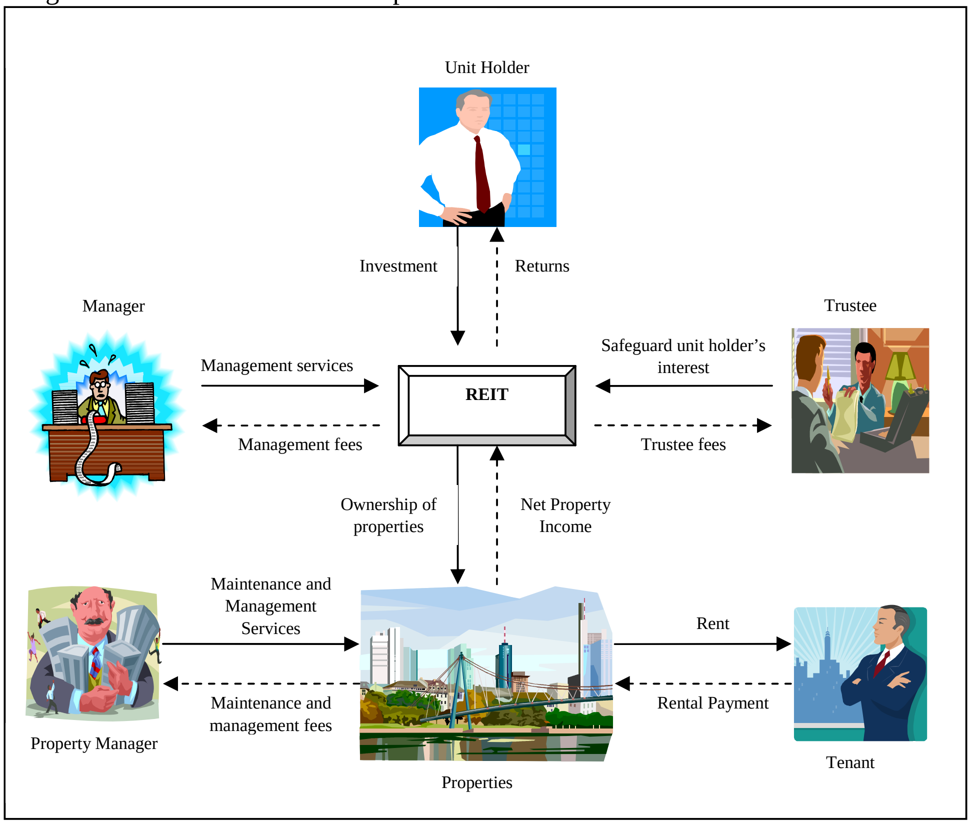
REIT offers investors the opportunity to diversify and invest their portfolios in listed real estate securities that own and operate income generating from real estate such as residential, commercial, retail properties, plantation land, storage facilities, warehouses, car parks and others, which otherwise expensive if they were to invest direct. The owner of one REIT unit is actually buying a portion of a managed pool of real estate. This pool of real estate then generates income through renting, leasing and selling of property and distributes it directly to the REIT on a regular basis. Hence, an investor may receive returns either in the form of dividend or capital gain for the asset holding duration.

In essence, REIT operates like any other trust funds involving stakeholders like Management Company, trustee and unit holders. The relationship of these parties is outlined and governed by a trust deed. The trust deed is essentially a formal document outlining the objectives and principles of REIT, and rights and responsibilities of a management company and a trustee respectively. The REIT must be managed and administered by a management company approved by the Securities Commission. Under the Guidelines on REIT, the management company must be "a subsidiary of either a company involved in the financial services industry in Malaysia; or a property development company; or a property-investment holding company; or any other institution which the Securities Commission may permit" (Securities Commission, 2005b). Among the main functions of REIT manager include setting up the strategic direction of the REIT, recommending to its trustee on the possible acquisitions, divestments or enforcements of assets and ensuring compliance with applicable regulations.

The REIT is also required to have a trustee who acts as the custodian of the assets of the fund and to safeguard the interests of the unit holders. This requires continuous supervision and monitoring of the funds managed by the management company so that it complies with the objectives and the deed of the fund and all related regulatory requirements and guidelines set by laws and the Securities Commission. In Malaysia functions of a trustee can only be assumed by a trust company which registered under the Trust Companies Act, 1989. The trustee earns trustee's fees for its functions in holding the assets for the benefits of the unit holders.

Another important stakeholder of REIT is property manager who provides property management services and in return, earns property management fees. The main functions of property manager include managing and controlling the assets of the REIT, preparing budgets and maintaining financial records for the properties and advising on sale and purchase decisions. Figure 1 summarises and illustrates the roles and functions of various parties involve in REIT operation.

Diagram 1: Stakeholder in REIT Operation



Literature has generally categorised REITs into three types, namely Equity REITs, Mortgage REITs and Hybrid REITs (Allen, Madura, & Springer, 2000: 141-152; Obaidullah, 2005; Park, Mullineaux, & Chew, 1990: 91-103) . A brief description of each type is discussed below:

Equity REITs

Equity REITs owns and operates income-generating real estate which involves a wide range of activities including leasing, development of real properties and tenant services. A distinctive feature of equity REITs is that it acquires and develops the real estate properties with the intention to manage them as part of its portfolio rather than resell them once they are developed.

Mortgage REITs

Mortgage REITs primarily hold long-term mortgages, but many also engage in short-term construction financing (Park et al., 1990: 91-103).This type of REITs offers interest-based loans to real estate owners, operators or developers. It involves greater risk since mortgage REITs tend to be more sensitive to volatility in market interest rates. This is due to the fact that mortgage REITs hold mortgages whose prices move in the opposite direction of interest rates.

Hybrid REITs

As the name implies, hybrid REITs are a combination of equity and mortgage REITs. In other words they own and operate real estate at the same time extend loans to real estate owners and operators.

Out of these three types of REITs, equity REITs is the most common type of REITs traded in the securities market. It also has the acceptable features which are more compliant with Shariah since its basic structure does not involve in the prohibited elements such as riba. The Shariah issues shall be discussed further in the sections to follow.

Characteristics of Shariah-Compliant REITs

The introduction of Islamic REITs is viewed as one of the most significant initiatives to broaden and deepen the product base of Islamic capital market in Malaysia. It can also help to enhance competitiveness of Malaysian Islamic capital market by attracting global Islamic investors who wish to diversify their investment portfolio which are Shariah compliant. This section provides an overview of Shariah rules and principles used in determining the Islamicity of REITs as outlined in the Guidelines for Islamic REITs issued on 21st November 2005 by Securities Commission (Securities Commission, 2005a).

Compliance Assessment Process

The Shariah-compliant assessment is undertaken by Shariah committee or advisor. This Shariah committee is responsible to oversee the operation of Islamic REITs so that it complies with every aspect of Shariah principles including investment, deposit and financing decision for Islamic REITs, acquisition and disposal of real estate and rental earnings and activities. The Shariah committee is also required to supervise and ensure that all funds are managed and administered according to the Shariah principles decreed and outlined by the Securities Commission.

There are several specific aspects of Shariah-compliant assessment process that Securities Commission has outlined in the Guidelines for Islamic REITs. The following highlights the salient aspects that need to be scrutinised when conducting Shariah-compliant assessment.

Non-Permissible Rental Activities

Since rental constitutes the main income stream for investors, it is pertinent to ensure that this rental derived from halal or permissible sources. Accordingly, the Shariah Advisory Council of Securities Commission delineates the following rental activities that are classified as non-permissible. The list includes financial services based on interest (riba); gambling/gaming; manufacture of sale of non-halal products or related products; conventional insurance; entertainment activities that are non-permissible according to the Shariah; manufacture or sale of tobacco-based products or related products; stockbroking or share trading in Shariah non-compliant securities; and hotels and resorts. Apart from these activities, the Shariah committee or advisors are allowed to use their own discretion based on ijtihad[1] to determine other activities that are deemed non-permissible to be included as a criterion in assessing the rental income for the Islamic REIT.

Rental from Tenant who Operates Mixed Activities

When there is a case of tenant who operates mixed activities i.e. one where its core activities are permitted by Shariah, although there are some other activities that may contain a small extent of prohibited elements, the Shariah advisors must perform compliance assessment with additional consideration. One of the most important considerations is that the rental from non-permissible activities must not exceed 20% of total turnover of the Islamic REIT (based on the latest financial year). To that effect, Shariah advisors need to advise the Islamic REIT fund manager not to invest in the real estate involving non-permissible activities that clearly exceed the benchmark.

Method of Calculating the Ratio of Rental of Non-Permissible Activities

There are several approved methods that can be used for calculating the ratio of rental of non-permissible activities from a tenant operating mixed activities. The

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[1] Ijtihad is the process of reasoning by Islamic jurists to obtain legal rulings from the sources of Shariah. Refer to (Mohammad Hashim Kamali, 1989a; Muhammad Hashim Kamali, 1989b: 215-235).

methods include the usage of space, hours of service and other methods deemed appropriate by the Shariah advisors using their own ijtihad. In the case of a supermarket for instance, the rental of non-permissible activities such as selling of alcohol can be based on the ratio of area occupied for non-permissible activities to the total area occupied. For example, if the total area rented out is 10,000 square feet and the area allocated for the sale of alcoholic beverages is 1000 square feet, then the ratio of area used for non-halal activities is 10%. Thus, the rental from non-permissible activities is 10% of the total rental paid by the supermarket. In this case the 10% rental income is deemed to be permissible as it is still within the acceptable benchmark of 20% of total turnover of the Islamic REITs.

Acquisition of Real Estate

Shariah-compliant assessments must be carried out by the appointed Shariah advisor. It is not permitted to acquire real estates in which all tenants operate non-permissible activities, even if the percentage of rental from the said real estate is within the accepted benchmark i.e. below 20% of the total turnover of the Islamic REITs.

Renting out to new tenant

The 20% benchmark in determining the status of mixed rental income need not be applied in case of renting out to a new tenant. This is because the exact rental receipt from non-permissible activities is still unknown. However in an obvious case whereby the new tenant involves in activities which are deemed impermissible then it is not allowed for Islamic REIT fund manager to accept such tenant. For example, a well-known casino operator who plans to rent the real estate of the Islamic REIT must not be accepted as a new tenant.

Instruments used in investment, deposit and financing for Islamic REITs

An Islamic REIT must also ensure that all forms of investment, deposit and financing instruments comply with the Shariah principles. For example, in financing the acquisition of real estate, Islamic REIT fund manager must not engage in riba-based instrument which would have an effect on the Islamicity of the Islamic REIT operation and transaction.

Takaful Coverage

The Guideline issued by the Securities Commission also stipulates that an Islamic REIT must use Takaful schemes to insure its real estate. However in case that Takaful schemes are unable to provide the insurance coverage, then the Islamic REIT is permitted to use conventional schemes (Securities Commission, 2005a).

Risk Management Issues

Islamic REIT is permitted to participate in forward sales or purchases of currency, and is encouraged to deal with Islamic financial institutions. If the Islamic REIT deals with Islamic financial institutions, then it will be bound by the concept of wa'd (a unilateral promise where only one party is obligated to fulfil his promise or responsibility). The party that is bound is the party that initiates the promise. However, if the Islamic REIT deals with conventional financial institutions, it is permitted to participate in the conventional forward sales or purchase of currency.

In a nutshell the preceding features of Islamic REIT as described and outlined in the Guidelines for Islamic REITs reflect fundamental differences between Islamic REIT and conventional REIT. The key difference between the two lies in how the incomes from REIT are earned and how the fund is supposed to be managed. For Islamic REIT, these two aspects need to be based on the principles of Shariah.

Besides the distinctive nature of Shariah-compliant investment which may appeal to Muslim investors, the Islamic REITs has the potential to attract investors due to their unique characteristics such as high dividend yields, low correlation with common stocks and a potential hedge against inflation (Lin & Yung, 2006: 275-291).

According to Forest (1994) and Lin and Yung (2006) the high dividend yield of REITs is a major reason investors move into REIT market. The high dividend yield also relates to the higher certainty of income as the fund manager is required to distribute its income in the form of dividend in order to enjoy tax incentives (Chang, 2006). In Malaysia, REITs are required to pay out a minimum amount to qualify for tax transparency, which in most cases is at least 90% of their income as distribution (Treasury Malaysia, 2006). This provides investors with a regular income as compared to the dividend payout of a listed company's shares equity which is at the discretion of the company. With a stable flow of income coupled with the REIT's low risk, appeal to certain types of investors, such as pension funds and retirees (Ghosh, Nag, & Sirmans, 1999: 175-192; Lin & Yung, 2006: 275-291). Furthermore, the ability of REITs to offer steady flow of income is attributed to its relatively stable cash flow since almost all of its revenue is generated by rentals under the terms of tenancy agreements, which are typically for specific durations.

Case Studies of Islamic REITs in Malaysia

Whilst the discussion in the preceding sections mainly aim to illuminate the understanding about the nature and characteristics of Islamic REITs operation, the subject of interest in this section sheds some light on the actual issuance of Islamic REITs in Malaysia based on two case studies namely, Al-'Aqar KPJ REIT and Al-Hadharah Bousted REIT.

Al-'Aqar KPJ REIT

Al-'Aqar KPJ REIT is claimed as the world's first Islamic REIT. It was established as a Malaysian-based unit trust on 28 June 2006 with the investment objective of owning and investing in Shariah-compliant real estate. When it was launched, Al-'Aqar KPJ REIT owned and invested in six hospitals which were first acquired from KPJ Healthcare Bhd and its subsidiaries. These properties were endorsed and approved as Shariah-compliant real estate by the appointed Shariah committee[2]. The properties which worth a total market value of RM481 million include Ampang Puteri Specialist Hospital Building, Damansara Specialist Hospital Building, Johor Specialist Hospital Building, Ipoh Specialist Hospital Building, Puteri Specialist Hospital Building and Selangor Medical Centre Building (Idris, 2006).

These acquired properties are then leased back to KPJ Healthcare Bhd and its subsidiaries. In other words, Al-'Aqar KPJ REIT is wholly dependant on the performance and operation of the KPJ Group for its revenue. KPJ and is subsidiary companies is a healthcare focused group and its portfolio of businesses include hospital management, healthcare technical services, hospital development and commissioning, nursing and healthcare professional continuous education, pathology services, central procurement and retail pharmacy (KPJ REIT, 2006) It is expected that being the single tenant of the properties and long term player in the healthcare industry, KPJ Group is able provide stable rental income to the Al-'Aqar KPJ REIT.

To protect the unit holder's interests, Amanah Raya Berhad was appointed as the trustee. As required by the Securities Commission Guidelines, the trustee shall actively monitor the administration of the fund by the management company to ensure that the interests of unit holders are upheld at all times. The trustee will ensure that the fund is managed and administered by Damansara REIT Manager in accordance with the objective of the fund, the deed, REIT Guidelines and acceptance and efficacious business practices within the real estate investment trust industry. Amanah Raya is also responsible to avoid any potential conflict of interests arising from future acquisition of Shariah-compliant properties especially with regards to the fact that the tenants are subsidiaries of KPJ and both the sponsor (KPJ Healthcare

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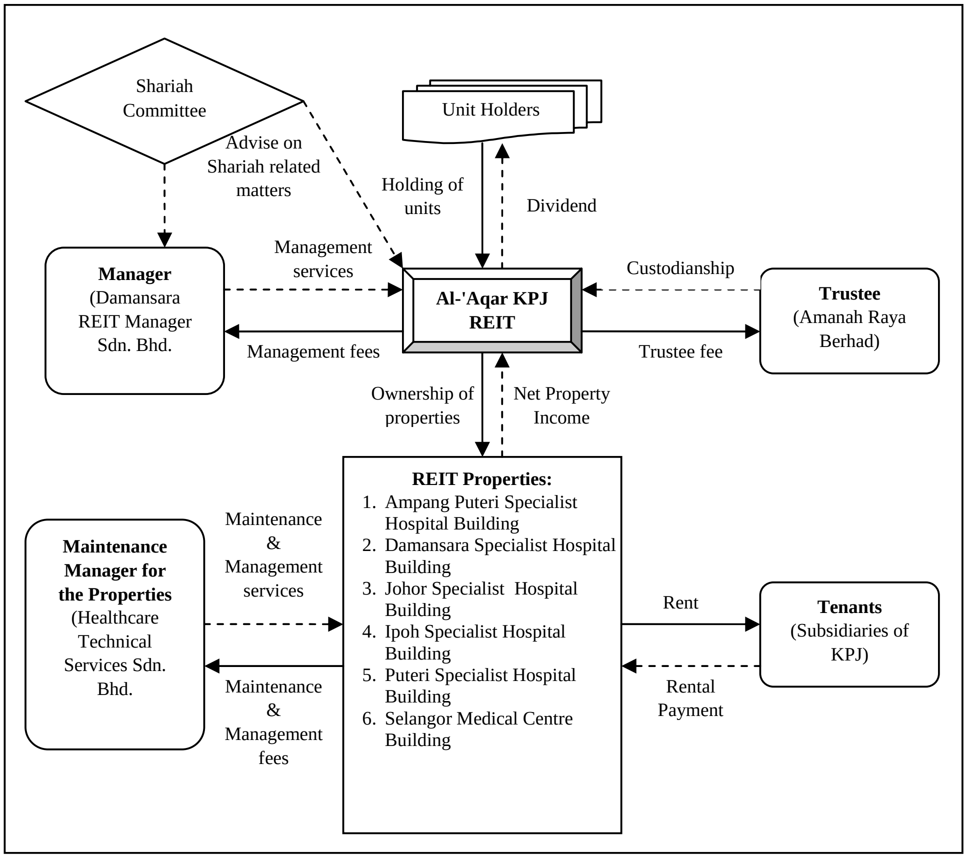
[2] The Shariah committee members include the Mufti of Johor Dato' Haji Nooh bin Gadut, former Mufti of Wilayah Persekutuan, Dato' Hj Md Hashim Yahaya and Prof. Madya Dr. Abdul Halim bin Muhammad.

Bhd) and the manager (Damansara REIT Manager Sdn. Bhd.) are 71.09% owned and 100% owned subsidiary of Johor Corporation (JCorp).

Diagram 2: the structure of Al-'Aqar KPJ REIT.



Al-Hadharah Bousted REIT

Al-Hadharah Bousted REIT is the second Islamic REIT listed on Bursa Malaysia (formerly known as Kuala Lumpur Stock Exchange). It was officially launched on 15 January 2007. Al-Hadharah Bousted REIT is the first Islamic REIT made up of plantation assets, particularly oil palm plantation. Similar to Al-'Aqar KPJ REIT, the initial transaction involves sale and lease back mechanism based on the contracts of al-bay` and al-ijarah.

Al-Hadharah Bousted REIT acquires plantation assets from Bousted Group involving eight oil palm estates and two palm oil mills, all located within Peninsula Malysia.

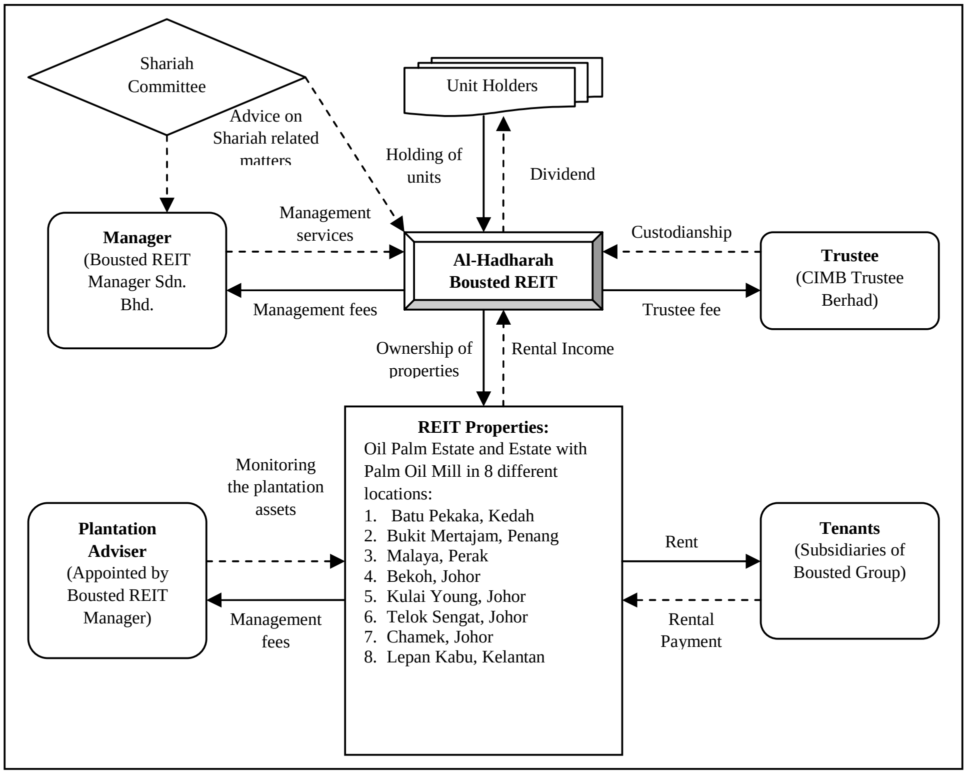
Total purchase consideration for these plantation assets, which forms the basis of this Al-Hadharah Bousted REIT fund is RM472 million. To fund the purchase consideration of the plantation assets, Al-Hadharah Bousted REIT issues units (the undivided interest in Al-Hadharah Bousted REIT as constituted by the Deed) to the vendors (namely the subsidiaries of Bousted Group, which include Bousted Properties, Bousted Plantations Berhad and Bousted Heah Joo Seang Sdn. Bhd.) as well as through public offering. These assets are subsequently leased back to the subsidiaries of the Bousted Group, who then become tenants based on Ijarah agreement (Bousted REIT, 2007) Similar to Al-'Aqar KPJ REIT, whereby the maintenance and management of REIT properties are done by the maintenance manager, Al-Hadharah Bousted REIT appointed a plantation adviser to monitor the overall state and condition of all aspects of the plantation assets.

Consequently, fixed rental is the main source of income for Al-Hadharah Bousted REIT. Tenants pay a cumulative fixed rental of RM41.3 million per annum on a bimonthly basis for the first tenancy term of three years. The rental is reviewed at the end of every three years and the new rental is determined based on historical crude palm oil prices, prevailing and expected future crude palm oil prices, cost of production, extraction rates and yield per hectare (Bousted REIT, 2007). All the leasing matters are clearly outlined under the Ijarah agreement between Al-Hadharah Bousted REIT and the vendors.

In addition to the fixed rental, other sources of income for Al-Hadharah Bousted REIT include performance-based profit sharing and capital gains. The former refers to an annual profit sharing of net incremental income based on a formula pegged to crude palm oil prices and fresh fruit bunch prices. The profit will be shared on an equal basis (50:50) between the tenants and the fund. It was claimed that this profit sharing payment is the first of its kind in the REIT market and may translate into more handsome dividend yields for investors. As for the capital gain, the fund shall distribute any gains realised from the sale proceeds of selected plantation assets in form of bonus dividends (Bousted REIT, 2007). There are also fees, charges and expenses involved in the administration of the fund, including manager's fees, plantation adviser's fees and trustee's fee.

As noted earlier all the plantation assets are rented back to the vendors who are effectively the subsidiaries of Bousted Group. In other words, the entire rental income of Al-Hadharah Bousted REIT under the Ijarah agreement is derived from only three parties that are within the Bousted Group. Hence, there is a risk of overdependence on single tenant and related party tenants. This is particularly true since the tenants' ability to pay rental very much dependent on their performance in the global commodity market. Fluctuations in crude palm oil and palm kernel prices coupled with volatility of foreign exchange currency rates could adversely affect the ability of the tenants to pay rental which make up a material proportion of the operating income of the fund.

Diagram 3: The structure of Al-Hadharah Bousted REIT.



Prospect of Islamic REITs in Malaysia

The future prospect of Islamic REITs in Malaysia looks very encouraging. It is envisaged that the growth of Islamic REITs in Malaysia to be further boosted following the recent tax transparency and incentives from the Malaysian government. Perhaps, as part of the Malaysian government's effort to promote Malaysia as an Islamic financial centre and capitalise on the influx of liquidity, particularly from the Middle East, various incentives were introduced via 2007 Budget proposals announced by the Prime Minister and Minister of Finance on 1 September 2006 (Treasury Malaysia, 2006). This has partly resolved the uncompetitive business environment due to high taxation regime which had discouraged foreign investors from entering the Malaysian capital market before.

Based on the 2007 Budget Proposals, the tax incentives can be generally categorised into two main areas, namely the enhancement of tax transparency system and reduction of investor's tax. Under the enhanced tax transparency system, REIT is fully exempted from paying its income tax on its taxable income if it distributes at least 90% of income to investors. In other words, the undistributed income from REITs is exempted from tax provided that the REITs distribute at least 90% of their income. On the other hand, where the 90% distribution is not complied with, the indistributed chargeable income of the REITs will be subject to income tax at the prevailing tax rates (Treasury Malaysia, 2006).This particular incentive encourages REITs manager to distribute at least 90% of income to investors thus not only providing investors more certainty of income but also ensuring higher yields from their investments in REITs.

The National Budget 2007 also provides tax incentives to entice specific investors to the Malaysia REIT market through the reduction of tax on the investors. According to the new tax proposal, dividends received by local and foreign individual investors and local unit trusts from listed REITs subject to a withholding tax of 15%, while foreign institutional investors (include a pension fund, collective investment scheme or such a person approved by the Minister of Finance) be reduced to 20% from the previous 28% for five years (Badawi, 2006; Treasury Malaysia, 2006). Undoubtedly, the tax incentives proposed in the National Budget 2007 would enhance the competitiveness of Malaysian REIT market.

In addition to various tax incentives, Islamic REITs are also expected to operate in a more transparent and well regulated environment. The issuance of two important documents by Securities Commission, namely Guidelines on REITs and Guidelines on Islamic REITs essentially provide a more transparent regulatory approach in Islamic capital market. The Guidelines delineates the roles and responsibilities of all stakeholders in the REIT structure. It clearly states the structure of the fund, restrictions, investment powers, fees and expenses, valuation requirements and procedures as well as reporting and disclosure requirements. Furthermore, the introduction of the Guidelines on Islamic REITs as guidance on Shariah-compliance criteria and requirement for managing Islamic REITs facilitates the development of a wider range of Islamic collective investment schemes for global Islamic funds. In a sense, the new guideline on Islamic REIT can be considered a supplement to the existing guidelines which are general rules on all aspects of investments in REIT in Malaysia. It also sets a global benchmark for the development of Islamic REITs. Undoubtedly, these two guidelines attest sound and tight regulatory framework, which promotes transparency and predictability in regard of business strategies and financial standing.

Finally, the Islamic REITs as offered in Malaysia demonstrate high-quality assets which can generate a stable stream of cash flow backed by a steady portfolio of tenants. For example, in the case of Al-'Aqar KPJ REITs, with a portfolio of hospital buildings and 100% guaranteed occupancy rate, it may certainly appeal to investors since subscribers are to receive consistent return from stable rental income. Moreover, according to Rating Agency of Malaysia (RAM), good quality assets are more likely to command sustainable resale values through economic cycles, hence ensuring timely repayment of financial obligations through refinancing and/or disposal of assets. Assessment of asset quality according to RAM entails the type of assets involved (e.g. retail, hotel or office) as well as their location (e.g. city centre or suburb), accessibility, age and condition (Ean, 2007).

Conclusion

This paper sheds some light on the practice and mechanics of Islamic REITs as implemented in Malaysian Islamic Capital Market. The introduction of Islamic REITs is viewed as one of the most significant initiatives to broaden and deepen the product base of Islamic capital market in Malaysia. It can also help to enhance competitiveness of Malaysian Islamic capital market by attracting global Islamic investors who wish to diversify their investment portfolio which are Shariah compliant.

Undoubtedly, Islamic REITs, with their relatively stable returns, provide investors with a new Shariah-compliant investment options. As evident from the above discussion, Islamic REITs is an investment instrument not only potential in providing investors with a 'piece of mind' in terms of complying with God's law but equally important the benefits of participating in the steady rental yields of real estates and other properties. Islamic REITs typically have relatively stable cash flow since almost all of its revenue is generated by rental payments. Islamic REITs also offer the benefit of diversification arising from their holding of a portfolio of high quality real estates with different tenancy lengths and geographical locations, rather than a single real estate or building. More importantly it promotes financial inclusion by providing investors an entry into the real estate market via participation and investment in units of the Islamic REITs, which requires a smaller capital outlay relative to purchasing similar real estate on their own.

Indeed, the emergence of Islamic REITs should help to propel the expansion of Islamic capital market in Malaysia. For Malaysian Islamic REITs to be truly successful, they also have to appeal to the vast international investing community. In this regard, the various tax incentives and regulatory framework introduced by the Malaysian authorities are perceived as a move in a right direction towards realising the noble vision of becoming the world’s Islamic financial and capital hub.

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