

# Research on Logistics Real Estate Operation Mode under REITs

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**Abstract.** Logistics real estate belongs to the category of industrial real estate, and it is also the basis for the development of the logistics industry. It links with many sectors of the national economy represented by the retail industry. It is an important infrastructure for the national economy and has broad development potential. However, the increase in the cost of land and the long investment recovery period has affected the financing of logistics real estate projects. By studying the financing of REITs and combining the characteristics of logistics real estate, this paper puts forward the business model and specific operation mode of logistics real estate under REITs. It is of great significance to promote the sound development of logistics real estate.

## 1. Introduction

Logistics estate is bearing the weight of the task of running modern logistics facilities, on top of which relevant investors invest in the development of logistics warehouse, transfer center, distribution center and other logistics facilities. Logistics estate, as an important part of industrial estate, is closely connected with the national economic construction and circulation. In recent years, along with growing of e-commerce market and the rapid rise of new retail concepts, logistics property of high standards is needed badly, China's per capita storage is still much smaller than that of developed countries, and the expand of electricity group causes the continuous rise of logistics warehouse rents in first-tier and second-tier cities. Logistics real estate, compared to residential real estate and commercial real estate, has the characteristics of relatively investment, low project construction difficulty, stable lease, and the high return on investment, so it has broad development prospects.

It is not difficult to discover through research that the rapid development of some world-renowned logistics real estate developers (such as GLP, AMB, and Goodman) is inseparable from real estate investment trust funds (REITs). The core profit of logistics real estate comes from the rental business, which is in line with the operation of REITs. Compared with developed countries, China's real estate financial market has yet to be developed. The exploration of REITs is mainly in the fields of commercial real estate, pension real estate, and public rental housing, and there is less practice in the field of logistics real estate. Until now, only the "China CITIC Huaxia Suning Yunxiang Asset Support Special Project" was launched in 2016. It is the the first logistics and warehousing REITs product in the domestic capital market, and is also the first single equity REITs product. The development of logistics real estate in China lacks long-term capital injection, and some bank loans,



trust funds, and private equity funds in the field of logistics real estate also lack mature introduction channels.

Therefore, based on the characteristics of logistics real estate, this article will explore the operational mode of logistics real estate after the introduction of REITs, combined with the current status of the industry, and put forward relevant recommendations.

## **2. The Feasibility of Introducing REITs into Logistics Real Estate**

### *2.1. REITs Overview*

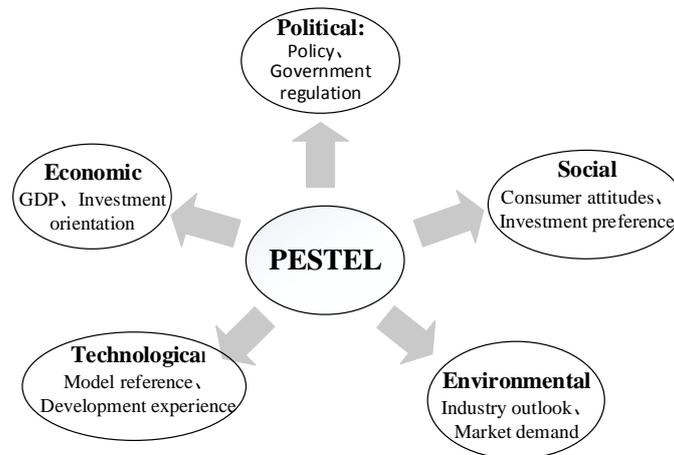
The real estate investment trust fund originated in the United States and is mainly used in a new type of financing model for the real estate industry. It raises investors' funds by issuing proceeds certificates, and then conducts management of real estate investments through professional organizations. The comprehensive income obtained in the whole process is distributed to investors according to a certain proportion.

Through the analysis of the studies and practices in developed countries in Europe and America on REITs and the commonness among different countries, it could be summed up that REITs has the following characteristics: (1) the assets have a steady stream of future earnings. Due to its stable and continuous earnings, it is favored by the investors, and promotes the vigorous development of REITs. (2) The law obliges to regulate its income distribution. In countries where REITs are implemented, strict rules have been imposed on the distribution of profits, and more than 90% of their returns must be regularly distributed to property investors in order to protect the interests of investors and the development of the industry. (3) The extensiveness of investors. REITs lower the investment threshold, so that ordinary investors can also participate in the real estate market. (4) Limited risk. REITs have the advantages of trusts and funds, and do not act as liquid assets when the sponsors go bankrupt, thereby protecting the interests of investors and reducing investment risks.

REITs can be divided into trust type and company type according to the different forms of organization; according to different investment targets, they can be divided into equity type, mortgage type, and hybrid type; depending on the mode of operation, they can be divided into open type and closed type; according to the way of raising funds The differences can be divided into public offerings and private placements.

### *2.2. Feasibility Analysis of Introducing REITs into Logistics Real Estate*

At present, China's logistics real estate has ushered in a new period of development while also face many challenges. The introduction of REITs that are in line with China's national conditions is conducive to widening the financing channels for logistics real estate. Therefore, the feasibility of introducing REITs is analyzed by using the PESTEL model below. This model is mainly divided into five aspects: political, economic, social, technological, environmental and legislative.



**Fig. 1** PESTEL feasibility analysis

**Political factors:** The product model of the securitization of logistics real estate in developed countries has already matured. It is supported by the government's perfect legal system, and it has rapidly developed and occupied the mainstream position. In order to protect the interests of investors, REITs have set up a diversification plan to make investors to earn profits. Government regulators have made strict regulations on the distribution of profits of investors. Under certain conditions, the introduction of REITs into logistics real estate can also avoid double taxation.

**Economic factors:** With the growth of the national economy and the increase in per capita GDP, the per capita storage of urban and rural residents in China has gradually increased, and per capita disposable income has risen. However, the diversity of investment channels is lacked and the investment method is simple. The introduction of REITs in logistics real estate has broadened investors' investment channels. Investors tend to invest more in low-risk, high-yield products. REITs are lower in risk than stocks, and their returns are higher than bonds, which is in line with investors' investment value.

**Social factors:** In recent years, with the popularization of e-commerce in most parts of the country, and the rise of "new retail", investors have had a new understanding of smart logistics. Logistics real estate as the foundation for the development of logistics has also attracted the attention of investors. Usually, investors need to invest in real estate through the direct purchase of property assets, which requires a lot of capital investment and high barriers to entry. However, if REITs are introduced into logistics real estate, investors can indirectly own logistics assets through asset securitization and enjoy other stable incomes such as rental income and value-added income. This method is more liquid and can be withdrawn at any time, which is more in line with the preferences of investors.

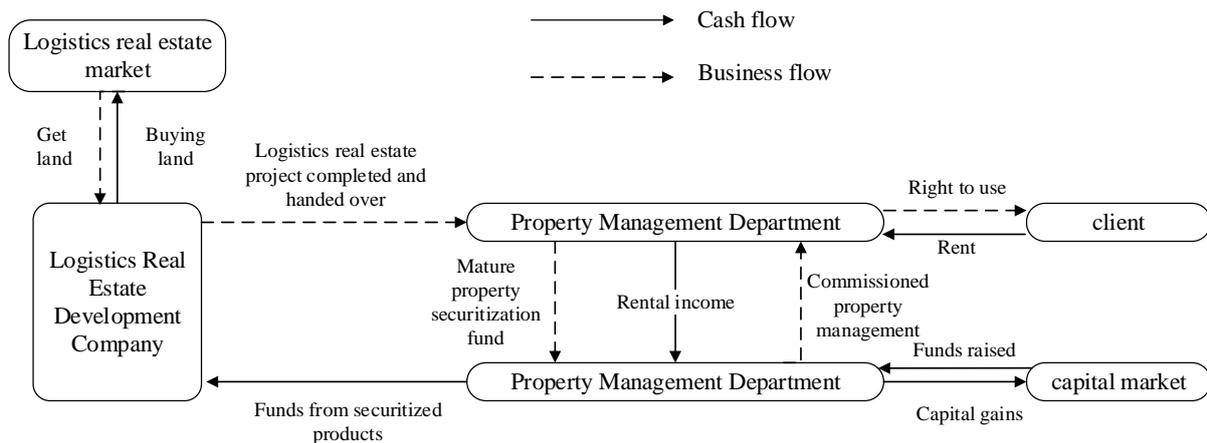
**Technical factors:** GLP entered the Chinese market in 2003 and quickly launched logistics real estate business through financing methods such as REITs. It quickly occupied the Chinese market, perfected the regional layout and became the overlord of the logistics industry. In January 2018, GLP officially withdrew from the Singapore Stock Exchange, representing the full completion of its privatization process. The development of GLP in China is worthy of being fully learned by local logistics real estate developers. The development of the REITs market in the United States and other countries has been relatively mature.

**Environmental factors:** With the rapid development of e-commerce, the logistics rents in major cities have continued to rise. The per capita logistics warehousing area is still far behind that of developed countries, and there is ample room for the development of logistics real estate. However, In previous years, the convergence of logistics real estate has occurred. Compared to residential and commercial real estate, logistics real estate has a low contribution to taxation and low land use, which leads to a decline in urban logistics Land use index and an increase in the cost of land acquisition. And its investment recovery cycle is usually over 15 years, so it is necessary to introduce REITs. With the

shift of e-commerce and third-party logistics to second and third-tier cities, the traditional non-standard extensive storage can no longer meet the demand. The international high standard warehousing has a large gap and requires a large amount of capital investment, which also causes financial pressure on logistics companies.

### 3. The Operation Mode of Logistics Real Estate REITs

#### 3.1. The Business Model of Logistics Real Estate REITs



**Fig. 2** Logistics Real Estate Introduces REITs Business Model Diagram

The purpose of REITs is to help logistics real estate companies raise funds for development and construction. It is a system in which various entities such as the logistics real estate development company, property management department, REITs management department, and investors participate together.

The main participants:

1. Property real estate development company: It obtains land for logistics real estate projects, conduct feasibility analysis and plan development for project investment and construction. And formulates REITs financing plan. The progress of the development of the project is supervised. After the project is completed, it is handed over to the property management department and is entrusted it to operate and manage the property.

2. Property management department: It is responsible for the management of logistics real estate projects and the daily maintenance of supporting facilities, sharing management income for gains.

3. REITs management department: It is responsible for the approval of the application plan and the day-to-day management of the fund, conducting REITs financing work in the capital market, raising funds for social investors, and helping development companies to achieve fund recovery and business expansion.

4. Investors: Ordinary investors who are optimistic about the prospects for the development of logistics real estate use revenue certificates to share revenue in accordance with relevant regulations. It has high flexibility and perfect exit mechanism.

5. Customer: The commerce company or the third-party logistics company leases logistics real estate to carry out related warehousing, distribution and other business. It pays a certain rent, and obtain the right to use the related supporting facilities.

Operation flow:

1. Establish a contractual organizational structure. Enterprises can choose companies with high correlation to form investors and look for professional logistics real estate developers as trustees.

2. At the stage of development of logistics real estate, real estate companies, joint venture subsidiaries and investment funds will develop logistics real estate and related ancillary facilities, reduce the occupation of self-owned funds, and realize the company's strategic goals.

3. After the property is completed, the project will be transferred to the property management department and the property will be sold to REITs for fund recovery. The recovered funds are used for the development of new projects. For the entrusted management and self-sustained REITs, they share revenue and obtain management fees.

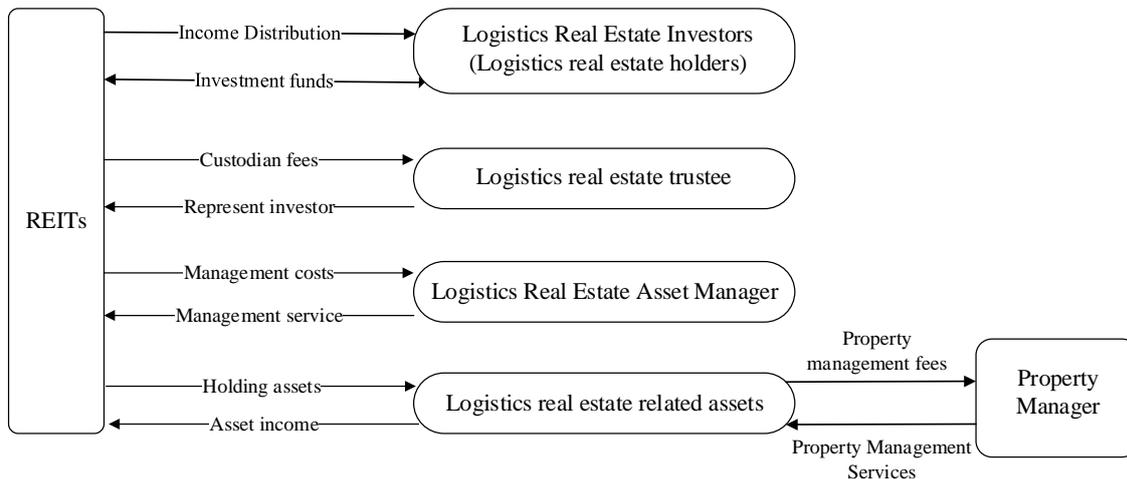
4. The REITs management department applied for the issuance of funds, established the REITs contract, raised funds through the capital market, and invested in the expansion of new projects for developing company. The capital proceeds were distributed to investors in accordance with relevant regulations.

The introduction of REITs in the logistics real estate model can not only increase revenue and reduce risk, but also enable companies to have more funds to develop properties, achieve rapid business expansion, and increase market share. Large-scale properties also represent sustained and stable capital income and more management benefits. Foreign capital shares risks and promotes sound and steady business operations.

### 3.2. The choice of specific operating modes for logistics real estate REITs

#### 1. The choice of organizational form

REITs have two choices in organization form: trust type and company type. For the long-term development of logistics real estate, the trust type is more appropriate than the company type. The information asymmetry between the company's shareholders and fund managers is prone to harming shareholders' interests. The rights and interests of shareholders cannot be guaranteed. The trust-type REITs has more symmetric information, separated ownership and income, relatively independent property. In addition, company-type companies are required to pay corporate income tax, and shareholders must also pay individual income tax when they receive proceeds. Trust companies can avoid such double taxation and protect the interests of investors.



**Fig. 3** the Organization Chart of REITs Introduced in Logistics Real Estate

#### 2. The choice of product form

For logistics real estate, equity-based REITs mainly hold some real estate industry. The revenue comes from the cost of property rental and asset appreciation, which is in line with the development model of logistics real estate. Mortgage refers to the purchase of Real Estate Mortgage Securities REITs. The main source of income is interest. Hybrid is the hybrid mode of the two. Following the

logistics real estate's developing and profiting model and drawing on the advanced experience of the United States and other countries, China should adopt equity REITs.

### 3. The choice of mode of operation

The process of the development of logistics real estate is a relatively long process, and it takes a long time for funds to be used. The issuance of funds should be combined with the years of completion and lease of logistics real estate. With open REITs, due to the characteristics of small changes in logistics real estate transactions, it is difficult to obtain real-time price information, and it is necessary to rely on assessment to determine prices, which is a huge project. Therefore, in accordance with the purpose of long-term stable income of REITs, China should adopt closed REITs. The issuance period of funds should be determined before issuance, generally based on the project recovery period of 5-10 years. After purchasing the fund, the investor may not redeem the investment capital according to the certificate of fund income within the prescribed period of time, but may trade in the financial market.

### 4. The choice of fundraising method

The public offer method is recommended on the specific way of raising funds. With the development of the national economy, per capita GDP has risen, and the amount of savings for residents in China has increased year by year. But there are fewer suitable investment products and investment channels need to be broadened. According to the investment of the majority of investors, it is more likely to continue to REITs with stable returns and lower risks. The long investment cycle of logistics real estate requires a large amount of funds. The public offering method mobilizes long-term investors for investment, which is conducive to the financing of logistics real estate.

## 4. Summary

### 1. The build of REITs legal norms

At present, China's existing legal provisions on investment trust funds are still not perfect, and the entire capital market is not mature enough. Especially after the introduction of REITs in logistics real estate, as a kind of trust product, the entire investment market is not fair and open enough to provide adequate legal protection. China should improve the "Trust Law" and the "Company Law," clarify the REITs investment regulations and capital structure, regulate the balance of assets and liabilities, and expand the size of investors. The profit portion should be distributed to investors in accordance with regulations. The existing legal system of real estate property rights in China is not perfect. This hinders the operation of highly liquid REITs so the investment portfolios and investment targets should be regulated.

### 2. Establish risk control and early warning mechanisms

REITs should establish a set of fund risk warning indicators based on logistics real estate and set corresponding thresholds. Through dynamic analysis, different risks are clearly divided according to the extent of the degree. According to the characteristics of REITs under logistics real estate, the source of market risk is evaluated, and these possible risks are quantified. The numerical values and risk values of subsystem indicators are calculated and predicted. When the value of risk exceeds the acceptable range, it must be handled promptly to protect the interests of investors.

### 3. The improvement of REITs supervision system

The government must legislate to clarify the rights and obligations of REITs and related regulations. At the same time, they should exercise their supervisory functions and supervise whether each entity's operations in the market comply with legal norms and maintain the normal operation of the entire capital market. For the phenomenon of REITs management departments sacrificing the interests of investors in specific operations caused by the objectively existing information asymmetry, it is necessary to improve industry norms, establish industry organizations, and regulate the development of logistics real estate REITs market.

### 4. The cultivation of market factors

The development of trust is restricted because it cannot be circulated, when developing REITs logistics real estate, by learning from the development experience of the United States and other

countries, we should cultivate the secondary market for trust product transactions and improve the rating system through standardized processes and risk indicators. In addition, in order to link the logistics real estate market with the financial market closely, relevant intermediaries must be nurtured. It is a diversified investment service system which includes the operation by financial institutions, such as logistics real estate trust and investment companies, the trusteeship by professional bank, the guarantee of the project by insurance companies, and the conduct valuations by logistics real estate appraisal agencies.

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