RESEARCH

INDIA REAL ESTATE OUTLOOK

RESIDENTIAL AND OFFICE

JANUARY – JUNE 2014

BENGALURU | CHENNAI | HYDERABAD | MUMBAI | NCR | PUNE

FOREWORD

A country's economic performance has direct repercussions on how its real estate market behaves. This is especially true for the residential property segment. More prosperity resonates higher financial confidence among home buyers, and this leads to a greater demand for homes. However, over the last two years, India has been battling various economic issues such as rising fiscal deficit, a falling rupee and increasing food inflation which have adversely hit the performance of the real estate sector of the country.

We have already seen overall sales of residential and commercial real estate in India dwindling across major cities. While the residential market did show some signs of recovery in 2012 and H1 2013, there was a sudden drop in new launches and absorption from the second half of 2013 onwards. Factors like rising interest rates by banks, high inflation and the weak rupee, among others, contributed towards building a negative sentiment among home buyers resulting in a substantial drop in investor interest.

All hopes were riding on the General Elections that did make way for a stable government which is expected to do better in reviving the real estate sector as a whole. The incentives announced for the housing sector in the Union Budget and all the subsequent decisions taken by the new government seems to be reflecting their intention towards getting the economy back on the growth path. Sentiments of homebuyers too, seem to have changed for the better as the gap between demand and supply has been narrowing gradually over the last year, and this trend is expected to continue in the next six months on the back of a strong recovery in sales volume.

The office market too, has been recovering over the last two years, with vacancy levels reflecting a steady decline. The recovery has primarily been led by the gradual increase in absorption across the top six metros and is expected to rise even further by the second half of 2014.

Keeping this in view, we are happy to share a comprehensive analysis of the residential and office market performance of 6 major cities – Mumbai, Pune, NCR, Bengaluru, Hyderabad and Chennai for the first six months of 2014 through our first ever half yearly real estate analysis report – The India Real Estate Outlook.

This report will serve as an industry guide for developers, suppliers, financial institutions, consumers and everyone else tracking the sector, to help them make informed choices.

Hope you find the information relevant. I look forward to hearing back for you.

Best Wishes,

Shishir Baijal

Chairman & Managing Director

Knight Frank India

TABLE OF CONTENTS

ALL INDIA 06

BENGALURU

Residential 17

Office 27

CHENNAI

Residential 39

Office 49

HYDERABAD

Residential 59

Office 69

MUMBAI

Residential 79

Office 87

NATIONAL CAPITAL REGION (NCR)

Residential 97

Office 105

PUNE

Residential 115

Office 123

ALL INDIA RESIDENTIAL AND OFFICE MARKET

Residential Market

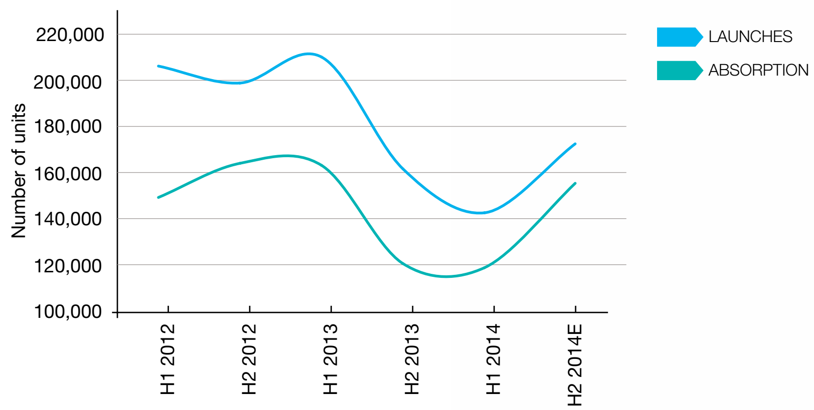
The residential markets of the top six cities in India, namely Mumbai, National Capital Region (NCR), Bengaluru, Pune, Chennai and Hyderabad, have been witnessing extreme volatility in terms of demand and supply over the last two years. While the residential market showed signs of recovery in 2012 and H1 2013, there was a sudden drop in new launches and absorption from H2 2013 onwards. Factors like a slowing economic growth, rising interest rates by banks, high inflation and the weak rupee, among others, contributed towards building a negative sentiment among home buyers and resulting in a dwindling sales volume. While new launches fell by 32% in H1 2014 compared to H1 2013, the sales volume dropped by 27% during the same period. All the cities witnessed a steep fall in absorption, in the range of 14-37% during H1 2014, with the Bengaluru and NCR markets falling by the lowest and highest rates, respectively.

The election results, sops for the housing sector in the Union Budget and all the subsequent decisions taken by the central government in order to revive the economic growth of the country seem to have changed the home buyers' sentiment from negative to positive in the last three months. The sales volume in these six cities is expected to experience a phenomenal growth rate of 26% in H2 2014, compared to H2 2013. Mumbai and Bengaluru are expected to lead in the recovery of sales volume, with 49% and 26% growth respectively, during this period. In contrast to this, the number of new launches is forecasted to report a subdued growth of 5% in the next six months. High unsold inventory and the poor response received by the new projects launched during H2 2013 and H1 2014 are expected to deter the developer community from launching any fresh projects in most of the cities during H2 2014. The only exception to such a trend will be the NCR and Chennai markets that are forecasted to witness a strong growth in new launches, as these markets had observed the sharpest fall during H2 2013, resulting in a low base during that period.

The gap between demand and supply has been narrowing gradually over the last year, and this trend is expected to continue in the next six months on the back of a strong recovery in sales volume. The impact of this can be seen in the weighted average prices, which have been inching upwards since 2012. During H1 2014, prices in Bengaluru have appreciated at the fastest pace of 11%, compared to H1 2013. This was followed by Hyderabad, at 9% during the same period. Prices in Hyderabad seem to be finally catching up with the other cities as the political uncertainty regarding the decision of dividing the state of Andhra Pradesh has ended. Going forward, Mumbai is forecasted to lead in terms of price appreciation during H2 2014, at 10% compared to H2 2013, on the back of a strong revival in absorption.

Pune has emerged as the most affordable city during H1 2014, as 83% of the new

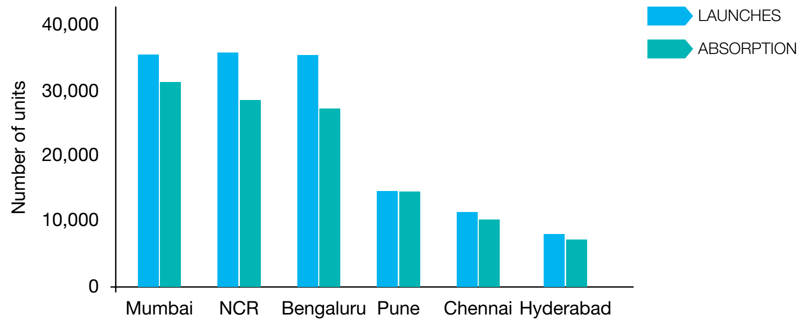
FIGURE 1
Launches and Absorption (Top Six Cities)



Note: The top six cities are Mumbai, NCR, Bengaluru, Pune, Chennai and Hyderabad
Source: Knight Frank Research

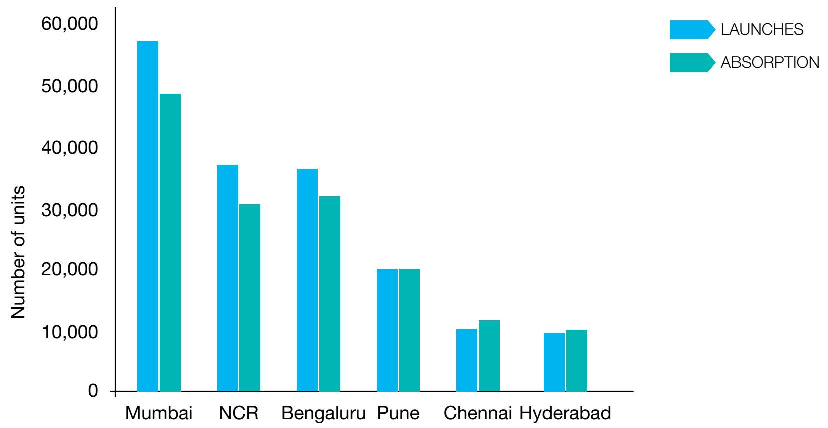
All the cities witnessed a steep fall in absorption, in the range of 14-37% during H1 2014, with the Bengaluru and NCR markets falling by the lowest and highest rates, respectively

FIGURE 2
City-wise New Launches and Absorption during H1 2014



Source: Knight Frank Research

FIGURE 3
City-wise New Launches and Absorption forecasted for H2 2014



Source: Knight Frank Research

Mumbai and Bengaluru are expected to lead in the recovery of sales volume, with 49% and 26% growth respectively from H2 2013 to H2 2014

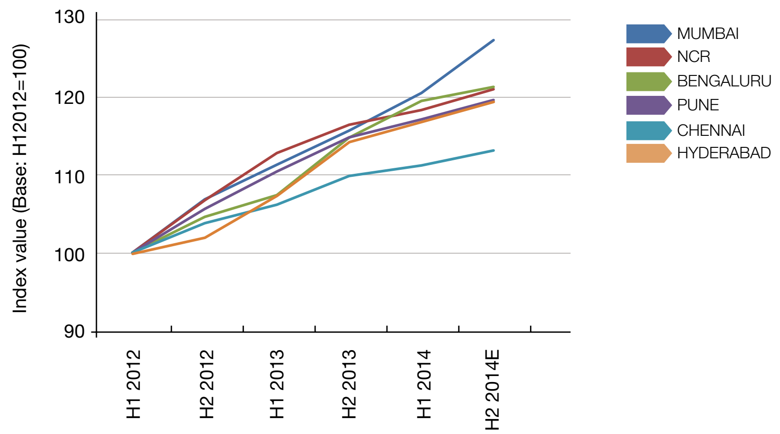
launches were below the ticket size of ₹ 5 mn. Since the majority of the new projects were launched around the periphery of the city, the ticket size of the apartments in these projects has remained small, despite a steady growth in prices. Similarly, 75% and 62% of the new launches in Chennai and NCR respectively were below the ticket size of ₹ 5 mn. Mumbai has emerged as the most premium market, with 34% of the total launches during H1 2014 above the ticket size of ₹ 10 mn. Mumbai was followed by NCR and Hyderabad, at 23% and 20%, respectively. Despite having the lowest weighted average price among the six cities, Hyderabad has a large number of projects above the ticket size of ₹ 10 mn. The primary reason for such a trend is the fact that the apartment sizes in most of the new projects are still on the higher side, compared to the other cities.

Comparing these cities in terms of the number of launches and absorption does not yield a true picture of the health of the market. Hence, we have developed a model that captures the relative health of a city by taking into account demand, supply and the age of unsold inventory. The age of unsold inventory is the number of quarters that have passed since the inventory entered the market. A higher age of unsold inventory indicates that a large number of old projects continue to remain unsold. Demand and supply is represented by the Quarters to Sell Unsold Inventory (QTS) in the model.

QTS can be explained as the number of quarters required to exhaust the existing unsold inventory in the market. The existing unsold inventory is divided by the average sales velocity of the preceding eight quarters in order to arrive at the QTS number for that particular quarter. A lower QTS indicates a healthier market.

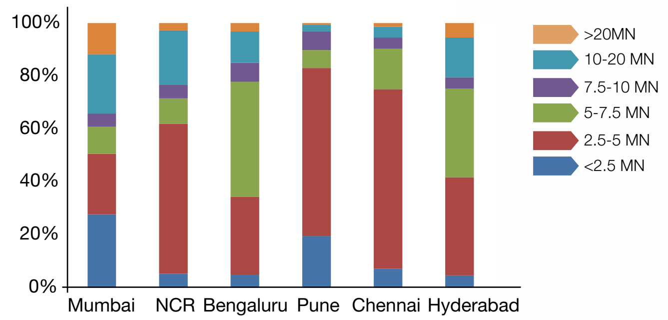
Currently, the Bengaluru residential market is the healthiest market among the six major cities of India. With a low QTS and age of unsold inventory, Bengaluru is the most balanced market, despite a steady drop in sales volume since H1 2013. Developers in Bengaluru have been vigilant with regards to the falling absorption level, and have reacted prudently by deliberately shrinking the number of new project launches in the last year. The health of the Mumbai residential market is the poorest, with the highest QTS and a large number of unsold inventories from previous years. The health of the Mumbai market is expected to improve marginally in the coming six months, on the back of recovery in sales volume and slower growth in new project launches.

FIGURE 4
Weighted Average Price Index



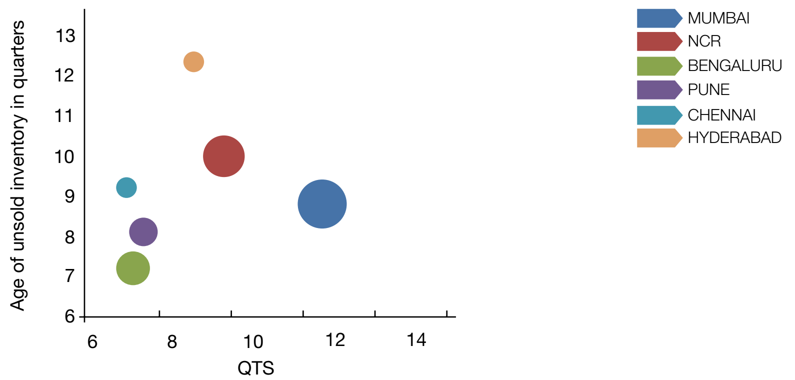
Source: Knight Frank Research

FIGURE 5
Ticket Size Split of Launched Units during H1 2014



Source: Knight Frank Research

FIGURE 4
QTS vs. Age of Inventory across Cities



Note: The size of the bubble indicates the quantum of unsold inventory.
QTS is Quarter to Sell Unsold Inventory

Source: Knight Frank Research

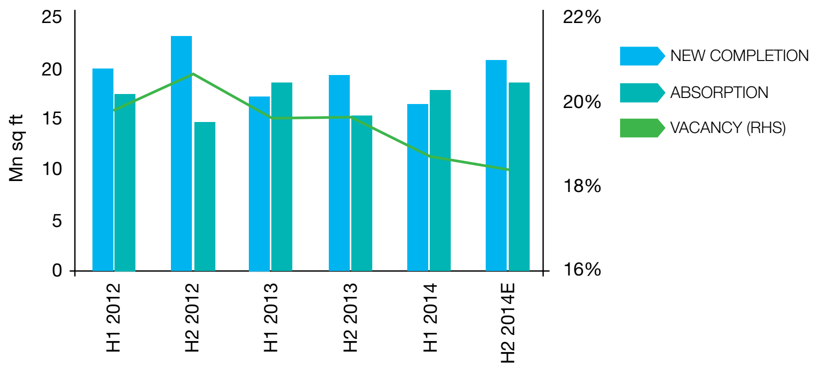
During H1 2014, prices in Bengaluru have appreciated at the fastest pace of 11%, compared to H1 2013. This was followed by Hyderabad, at 9% during the same period

Office Market

The office market of the top six cities have been recovering steadily over the last two years, with vacancy levels falling from 21% in H2 2012 to less than 19% in H1 2014. The recovery has been led primarily by the gradual increase in absorption across the top six cities, namely, Mumbai, NCR, Bengaluru, Pune, Chennai and Hyderabad. The combined absorption of these cities has increased from 14.7 mn sq ft in H2 2012 to 17.9 mn sq ft in H1 2014, and we forecast this to rise even further to 18.7 mn sq ft during H2 2014. For the full year 2014, we expect absorption to touch 36.5 mn sq ft –an 8% jump from the 33.9 mn sq ft reported in 2013. In contrast to this, new completions expected to hit the market will grow by 3%, to 37.4 mn sq ft in 2014, compared to 36.4 mn sq ft in 2013. This will result in the vacancy levels dropping further, to 18.4% by the end of 2014.

Chennai and Bengaluru have led in terms of growth in absorption, at 47% and 29% respectively during H1 2014, compared to H1 2013. However, Hyderabad, Pune and Mumbai are forecasted to post the maximum year-on-year growth in absorption during H2 2014, at 96%, 85% and 76%, respectively. In terms of vacancy, the Bengaluru office market continues to lead, with the lowest vacancy level of 11% during H1 2014, compared to 19-22% reported in the other cities. The steep fall in new

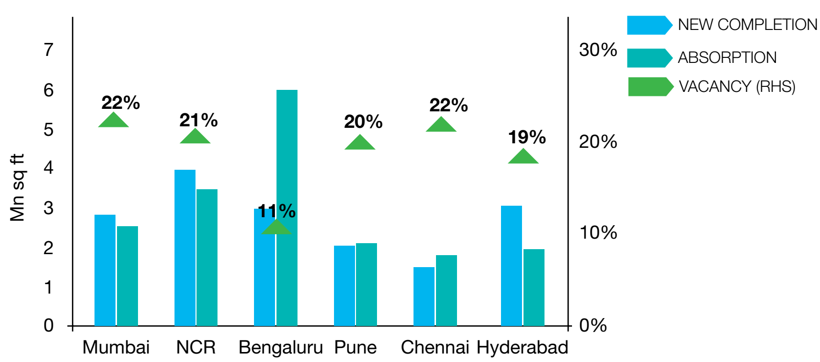
FIGURE 1
New Completion, Absorption and Vacancy (Top Six Cities)



Source: Knight Frank Research

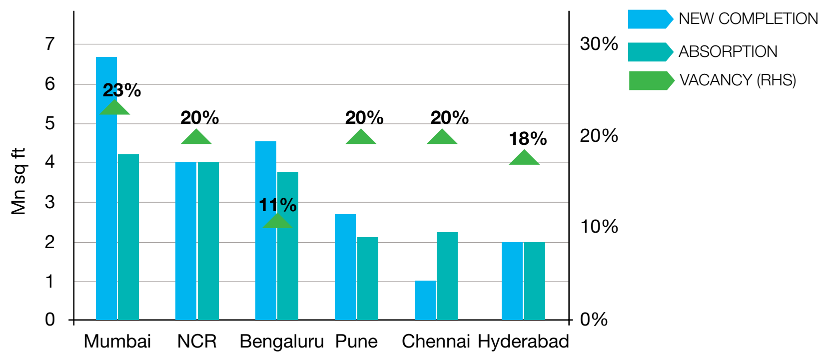
The office market of the top six cities have been recovering steadily over the last two years, with vacancy levels falling from 21% in H2 2012 to less than 19% in H1 2014

FIGURE 2
City-wise New Completion, Absorption and Vacancy During H1 2014



Source: Knight Frank Research

FIGURE 3
City-wise New Completion, Absorption and Vacancy Forecasted for H2 2014



Source: Knight Frank Research

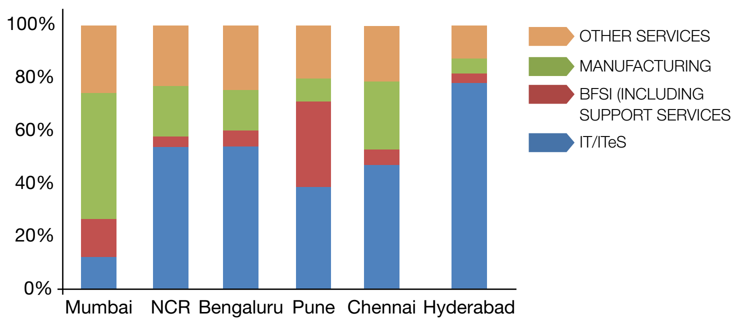
completions, which was reported at 3 mn sq ft during H1 2014, compared to an absorption level of 6 mn sq ft, has helped Bengaluru in attaining its current level of vacancy.

Going forward, vacancy levels across all the six cities are expected to improve marginally during H2 2014, except for Mumbai. A sharp increase in new completions, which is forecasted at 6.6 mn sq ft, compared to just 4.2 mn sq ft of absorption during H2 2014, is bound to push the vacancy levels in Mumbai even higher. Vacancy levels in the Chennai market are expected to improve considerably in the next six months, as absorption in the city is projected to far outstrip new completions. While 2.2 mn sq ft of office space is estimated to be transacted in Chennai during H2 2014, new completions are expected to touch 1.1 mn sq ft.

The IT/ITeS sector continues to lead in terms of share in total absorption across all the cities, except for Mumbai. Demand from the manufacturing sector has dominated the Mumbai office market, followed by the other services sector during H1 2014. Interestingly, the share of the other services sector has been increasing steadily across all the six cities over the last few years. Currently, the other services sector contributes more than one-fifth of the total office space demand in the majority of these cities. The other services sector includes companies from consulting, retail, eCommerce, infrastructure and real

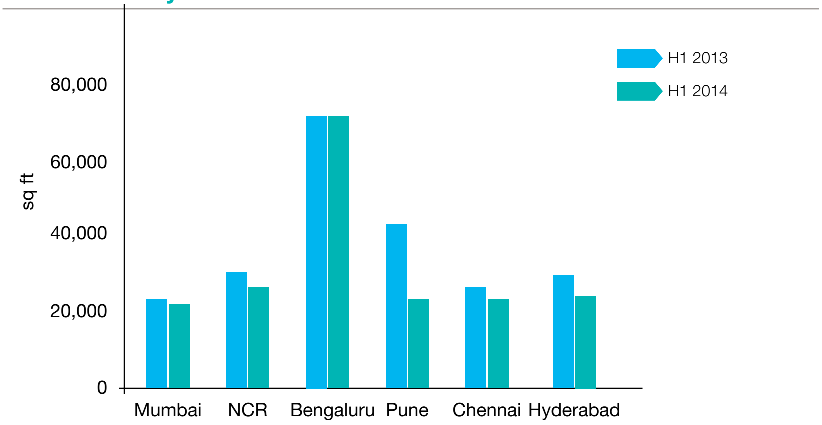
In terms of vacancy, the Bengaluru office market continues to lead, with the lowest vacancy level of 11% during H1 2014, compared to 19-22% reported in the other cities

FIGURE 4
Sector-wise Absorption Split During H1 2014



Source: Knight Frank Research

FIGURE 5
Deal Size Analysis



Source: Knight Frank Research

estate, among others.

During H1 2014, the office space market in each of the six cities has witnessed a substantial jump in the number of deals. The total number of deals has increased from 542 in H1 2013 to 623 in H1 2014. This is a clear sign of improvement in the office space market, as an increase in the number of deals indicates a wider participation in transaction by occupiers. However, the average deal size has reduced marginally in most of the cities during the same period. While Pune has witnessed the steepest drop in the average size of deals during H1 2014, Bengaluru has been able to maintain it, despite a substantial jump in the number of deals. The ticket sizes of transactions have considerable influence on the rental movement during a particular period. While tenants with a requirement for large spaces tend to have the upper hand during rental negotiations, the reverse is true with small-size deals. Hence, a drop in the average size of deals could lead to an upward pressure on rents.

Unlike residential markets, where prices have been increasing sharply over the last three years despite a slowdown in the sales volume, the growth rate

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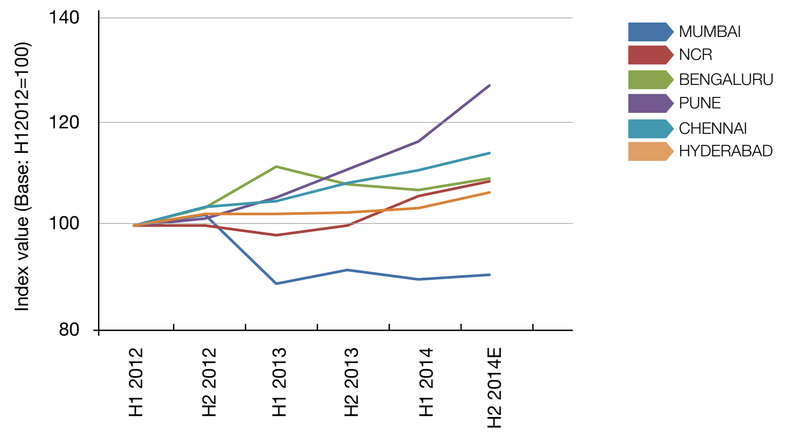
FIGURE 6
Weighted Average Rental Index



Source: Knight Frank Research

achieved in the rental value of office space has been relatively constrained. This is despite the fact that absorption in each of the six cities has been growing steadily since 2012. The primary reason for such an anomaly is that the majority of the transactions are taking place in the peripheral business districts, where rents are considerably lower than those in the central or suburban business districts. This pulls down the weighted average rent of a city. During H1 2014, the weighted average rental growth in these six cities was limited to single digits, except for Pune. Unlike other cities, the Pune office market has witnessed a strong traction in the SBD markets, compared to the PBD markets during H1 2014. This is a clear reversal in trend, wherein the SBD markets have regained their share in total transaction, which they had been losing out to PBD markets over the last few years. Since the rental values in SBD markets are on the higher side, the city's weighted average rent has been observing a faster growth.

The weighted average rental value in Mumbai has been on a downward trajectory since 2012, as the shares of peripheral and suburban business districts have been increasing steadily with each passing year at the cost of the CBD and off-CBD markets. Unaffordable rents, lack of amenities, inadequate parking facilities and smaller floor plates in office buildings located in the CBD and off-CBD markets have caused this exodus, leading to a negative growth in the weighted average rental value of the city.

During H2 2014, we forecast Pune and NCR to lead in terms of growth in the weighted average rental value, compared to the rest of the cities. While rents in Mumbai will continue their downward spiral, cities like Bengaluru, Chennai and Hyderabad are expected to witness a subdued growth, as the peripheral and suburban business districts in each of these cities continue to increase their share in the total transactions.

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BENGALURU

RESIDENTIAL MARKET

Metropolitan Region Analysis

Bengaluru has long been one of the preferred residential destinations in India, thanks to factors like a favourable climate and apt socio-economic conditions. The advent of the IT sector in the region in recent years has brought about great change in the residential landscape of the city, turning it into a veritable property hub.

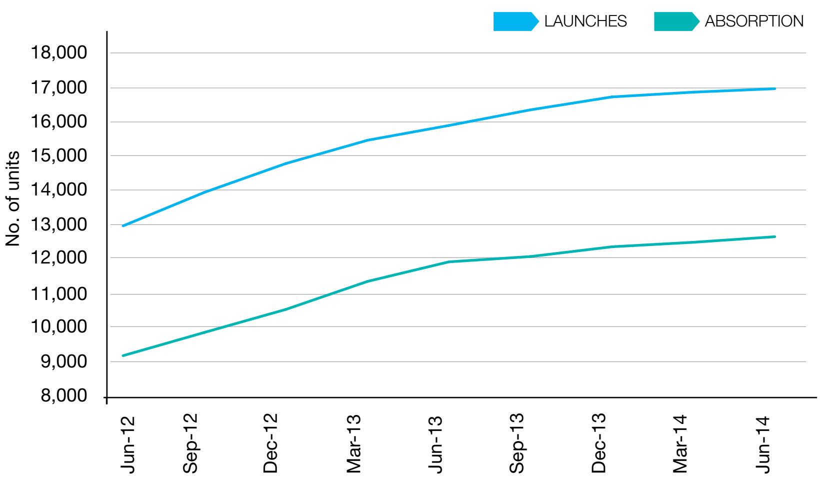
The Bengaluru residential market proved its resilience effectively by maintaining a healthy demand for homes and new project launches in 2013 in a situation wherein most of the prominent residential markets across the country witnessed a witnessed a negative churn. However, the momentum has somewhat slackened in 2014, and while the demand for homes had increased by 13% in 2013 over the demand in 2012, it is expected to increase by just 3% in 2014. The total number of units to be absorbed is expected to increase from 57,366 in 2013 to 59,300 in 2014. This lack of substantial growth in absorption is expected to be accompanied by a drop in the number of new launches during the year. New launches are estimated to decrease by 8% from 78,300 units in 2013 to 72,113 units in 2014.

Since comparing the absolute numbers of absorption and new launches on an annual basis is not adequate to understand the health of a market or its impact on price, hence, with the aim of removing seasonality from the data, we have analysed the long-term moving average (eight quarters) trend in absorption and new launches. It should be understood that demand and supply are influenced by various other independent factors, such as economic growth, market sentiment, interest rate and income growth, among others. An annual rise or fall in demand and supply could be misinterpreted as a sign of a strong or weak market.

The following chart clearly indicates a rather smooth upward progression in both absorption and launches since June 2012. Interestingly, the rate of

The Bengaluru residential market proved its resilience effectively by maintaining a healthy demand for homes and new project launches in 2013. However, the momentum has somewhat slackened in 2014, and while the demand for homes had increased by 13% in 2013 over the demand in 2012, it is expected to increase by just 3% in 2014

FIGURE 1
Long Term (Eight Quarters) Moving Average Trend of Launches and Absorption



Source: Knight Frank Research

increment in new launches has moved in tandem with the growth in absorption since December 2013. This underscores the fact that developers have realised that demand exists for realistically-priced properties that offer quality and transparency in deals. Low volatility in pricing ensures that the sales momentum is maintained and buyers' sentiments are not crossed.

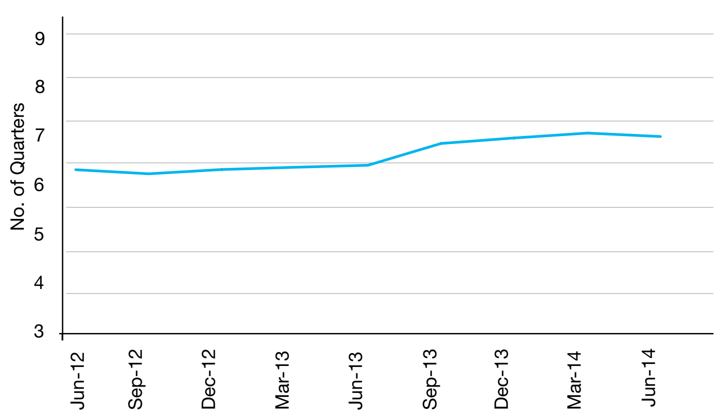
While the analysis of absorption and new launches provides a fair idea about the traction being witnessed in the market, the impact on price can primarily be understood by studying the unsold inventory available in the city. Hence, we have calculated the Quarters to Sell Unsold Inventory (QTS), which can be explained as the number of quarters required to exhaust the existing unsold inventory in the market. The existing unsold inventory is divided by the average sales velocity of the preceding eight quarters in order to arrive at the QTS number for that particular quarter. A lower QTS indicates a healthier market.

The QTS ratio for Bengaluru has inched upwards by one notch since September 2013, signifying a gradual weakening of buyer sentiment in the market. The decline of sales volumes by 20% in H2 2013 as compared to H1 2013 was instrumental in pushing up the QTS from 6 to 7. While the sales volume dropped from 31,844 units in H1 2013 to 25,522 units in H2 2013, new launches declined by 14% from 42,155 units to 36,145 units during the same period. In H1 2014, another 2% decline in new launches was observed, compared to H2 2013. This decline in new launches can be taken as a cognizance of the developer community towards an impending demand-supply imbalance in the market, owing to continuous build-up of unsold units in the city. However, although the sales volume increased slightly, by 7% during H1 2014 to 27,256 units, this has not directly resulted in bringing down the QTS ratio yet.

We expect another six to nine months for the Bengaluru market to offload its excess unsold inventory and cause the QTS ratio to revert to its 2012 level. The election results, revival of manufacturing activity, higher salary growth of IT/ITeS employees and various sops announced in the Union Budget of 2014 seem to have induced a positive change in the home buyer sentiment. The conversion time between a sales inquiry and an actual sale has shortened considerably, indicating a revival in demand. While the sales volume has improved somewhat in H1 2014, we expect it to strengthen even further in H2 2014. Absorption is

The QTS ratio for Bengaluru has inched upwards by one notch since September 2013, signifying a gradual weakening of buyer sentiment in the market. The decline of sales volumes by 20% in H2 2013 as compared to H1 2013 was instrumental in pushing up the QTS from 6 to 7

FIGURE 2
Quarters to Sell Analysis



Source: Knight Frank Research

forecasted to increase by 18% to 32,044 units in H2 2014, compared to H1 2014. This translates into an increase of 26% over the sales volume in H2 2013.

Meanwhile, the variation in demand and supply of residential property notwithstanding, price levels in the city continue to move upwards, albeit at a slower, controlled pace. The weighted average residential price in Bengaluru has increased by 11% from ₹ 4,020/sq ft in H1 2013 to ₹ 4,473/sq ft in H1 2014. This can be attributed to the rising cost of input materials and the relative decline in new launches. Going forward, we forecast the prices to increase nominally, by 1.5% in H2 2014 to ₹ 4540/sq ft, compared to H1 2014, on the back of a moderate recovery in sales volume.

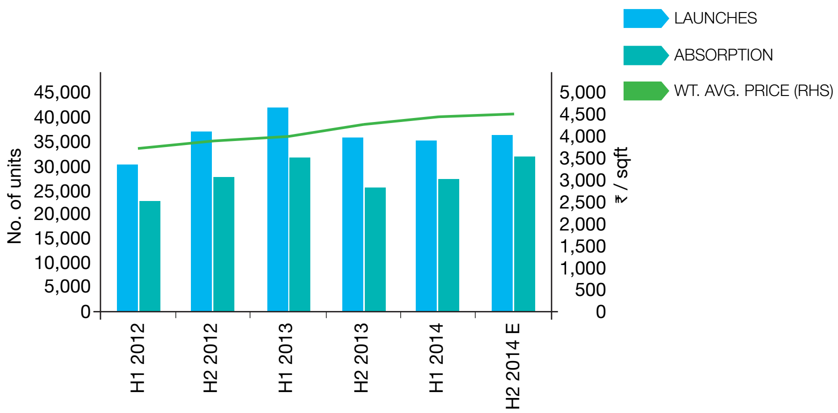
The recent infrastructure projects in Bengaluru have been largely responsible in providing access to newer micro-markets and easing their mobility restrictions, besides decongesting older micro-markets. Good momentum in infrastructure projects has been observed with the initiation of the expansion of the international airport and the elevated expressway on Bellary Road, thereby aiding home prices, as well as the development of the stretch connecting Hebbal and K. R. Puram as a largely signal free-corridor.

This will greatly support the residential developments in these two major markets.

The metro rail is the most ambitious of the projects designed to cover all the corners of the city. Once all the phases of the metro are completed, there will be a considerable impact on the residential prices along the nodes. Meanwhile, the residential micro-markets along the recently commenced Sampige Road–Peenya metro rail stretch towards west Bengaluru are projected to receive an immense amount of interest from home buyers in the forthcoming months. This can be attributed to faster connectivity to their workplaces, facilitated by the metro rail. Vast decongestion of traffic bottlenecks towards the city centre is expected to take place, reducing the travel time by road as well. Moreover, there exists good potential for price appreciation in the residential micro-markets along this stretch, which would attract investors from other regions.

FIGURE 3

Launches, Absorption and Price Trend



Source: Knight Frank Research

The weighted average residential price in Bengaluru has increased by 11% from ₹4,020/sq ft in H1 2013 to ₹4,473/sq ft in H1 2014. This can be attributed to the rising cost of input materials and the relative decline in new launches.

South Bengaluru has consistently witnessed a majority of new launches in both the first halves of 2013 and 2014, although its share decreased slightly from 47% in H1 2013 to 45% in H1 2014, due to the presence of a large number of IT companies in IT/ITeS employment hubs such as Electronics City, Sarjapur Road and Bannerghatta Road

Micro-market Analysis

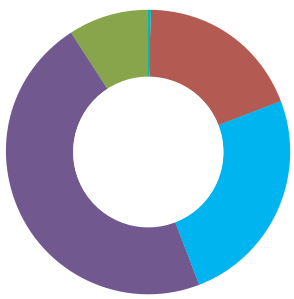
The Bengaluru residential market can be classified broadly into five micro-markets, as presented in the table below:

Micro-markets	Indicative Locations
Central	M.G. Road, Lavelle Road, Langford Town, Vittal Mallya Road, Richmond Road
East	Whitefield, Old Airport Road, Old Madras Road, K.R. Puram, Marathahalli
West	Malleswaram, Rajajinagar, Yeshwanthpur, Tumkur Road, Vijayanagar
North	Hebbal, Bellary Road, Hennur, Thanisandra, Jakkur, Yelahanka, Banaswadi
South	Koramangala, Sarjapur Road, Jayanagar, J.P. Nagar, Electronics City, Kanakapura Road, Bannerghatta Road

The residential market of Bengaluru is divided fairly across the four zones (north, south, east and west) in terms of launches and absorption, with the exception of central Bengaluru. During H1 2014, central Bengaluru accounted for less than 1% of the total new launches, as high prices and unavailability of land parcels deterred developers from launching new projects. A prominent project recently launched in central Bengaluru is Sanyog by Mythreyi Properties at Wilson Garden. Owing to the lack of depth required for our analysis, the focus of our research has been limited primarily to the other four micro-markets of the city.

South Bengaluru has consistently witnessed a majority of new launches in both the first halves of 2013 and 2014, although its share decreased slightly from 47% in H1 2013 to 45% in H1 2014. South Bengaluru has generally been a preferred residential destination for employees of the IT sector due to the presence of a large number of IT companies in IT/ITeS employment hubs such as Electronics City, Sarjapur Road and Bannerghatta Road. Social infrastructure like the availability of quality hospitals and popular retail malls are some of the major reasons for residential demand in this part of Bengaluru. Additionally, property prices are relatively cheaper in the peripheral locations in the south, compared to the other micro-markets. During H1 2014, 71% of the units launched within the price bracket of ₹ 2.5–5.0 mn belonged to south Bengaluru. CityVille by Valmark on

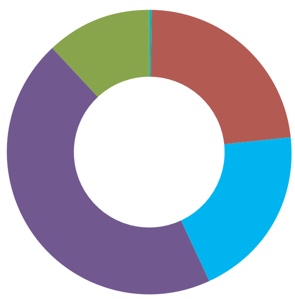
FIGURE 4
Micro-market Split of Launched Units in H1 2013



<1% CENTRAL
19% EAST
25% NORTH
47% SOUTH
9% WEST

Source: Knight Frank Research

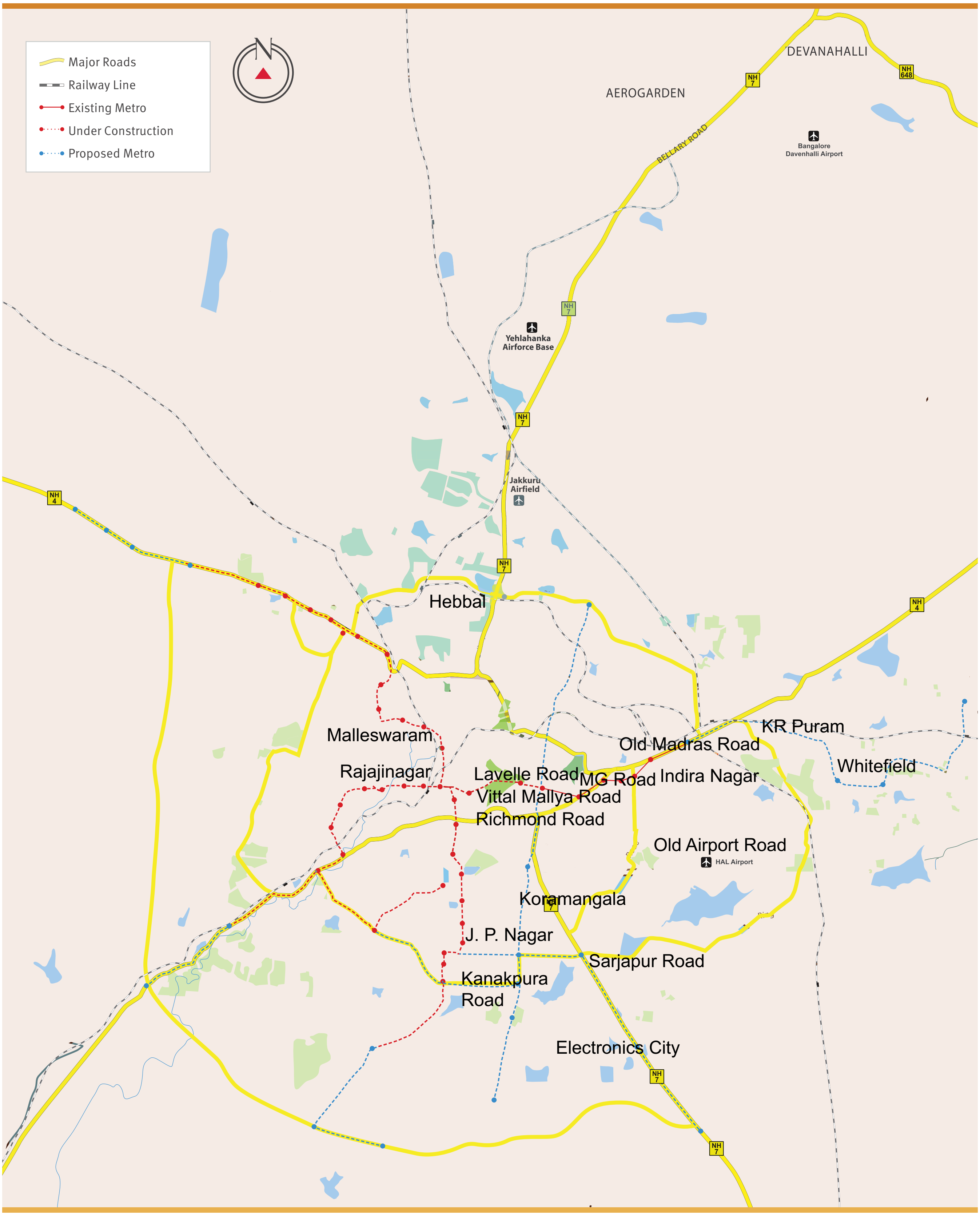
FIGURE 5
Micro-market Split of Launched Units in H1 2014



<1% CENTRAL
23% EAST
20% NORTH
45% SOUTH
12% WEST

Source: Knight Frank Research

BENGALURU METROPOLITAN REGION MAP



The eastern and western parts of the city have been able to increase their share of new launches in H1 2014. While east Bengaluru's share increased by 21% in H1 2014 over the share in H1 2013, west Bengaluru's share increased by an impressive margin of 33%

Bannerghatta Road, Shriram Summit at Electronics City and Shriram Chirping Woods on Haralur Road by Shriram Properties, and BREN EdgeWaters at Sarjapur Road by BREN Corporation are some of the new projects launched in south Bengaluru during H1 2014.

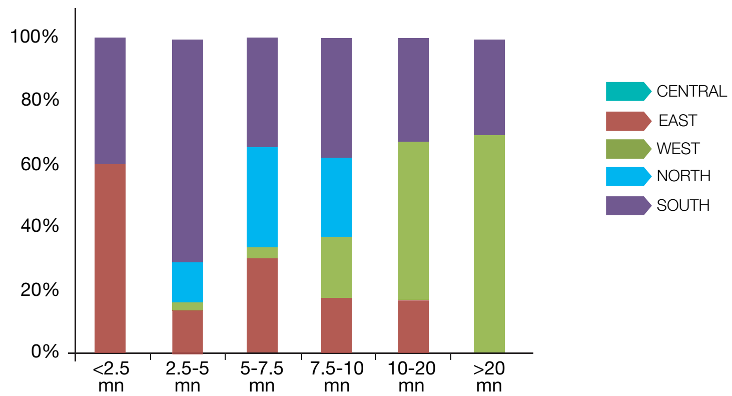
Unlike south Bengaluru, the eastern and western parts of the city have been able to increase their share of new launches in H1 2014. While east Bengaluru's share increased by 21% in H1 2014 over the share in H1 2013, west Bengaluru's share increased by an impressive margin of 33%. On the eastern front, corporates have made large investments in office spaces in locations like Whitefield and ORR East as infrastructure initiatives fructified in tandem. This has increased the attractiveness of east Bengaluru as a residential destination. On the other hand, west Bengaluru has been witnessing a considerable amount of developer interest owing to improving infrastructure. Godrej United by Godrej Properties and Republic of Whitefield by DivyaSree, both located at Whitefield, are a few select projects launched in east Bengaluru, while Presidential Towers by Golden Gate Properties and Aparna Elina by Aparna Constructions and Estates at Yeshwantpur are some of the projects launched in west Bengaluru during H1 2014.

North Bengaluru observed a fall of 20% in new launches during H1 2014 over the share in H1 2013, as developers were deterred from launching fresh projects on the back of lacklustre response received by various projects launched during H2 2013. The micro-market seems to be facing price resistance from home buyers, as a majority of the locations have already breached the psychological price point of ₹ 4,500/sq ft in locations currently lacking social infrastructure. Mirabilis by Kolte Patil Developers at Horamavu and Purva Palm Beach by Puravankara Projects on Hennur Road are some of the new projects launched during H1 2014.

On the absorption front, central Bengaluru has been able to maintain its momentum during H1 2014, although it is insignificant in terms of absolute numbers and share. Locations like Whitefield and Electronics City are witnessing renewed traction since H2 2013, while residential projects along the Outer Ring Road (ORR) continue to do well. This trend is expected to continue even in 2014. The share of north and west Bengaluru has observed the steepest fall in absorption during H1 2014, to the tune of 24% and 30% respectively. This can be attributed to the apprehension among buyers regarding a majority of projects being located beyond the established residential areas, with a dearth of

FIGURE 6

Micro-market Level Ticket Size Split of Launched Units During H1 2014



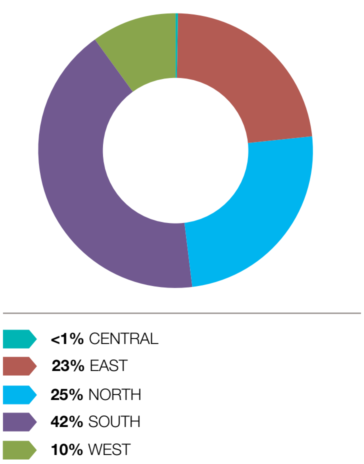
Source: Knight Frank Research

adequate social infrastructure, absence of mass rapid public transportation systems, distance from the city centre and poor access roads. Areas like Devanahalli in north Bengaluru and Mysore Road in west Bengaluru have witnessed dampened sales volumes because of such challenges. The eastern and southern Bengaluru markets have fared relatively better in terms of absorption, compared to the north and west.

However, comparing these micro-markets in terms of the number of launches and absorption does not reflect the true picture of the health of the market. Hence, we have developed a model that captures the relative health of micro-markets by taking into account demand, supply and the age of unsold inventory. The age of unsold inventory is the number of quarters that have passed since the inventory entered the market. A higher age of unsold inventory indicates that a large number of old projects continue to remain unsold.

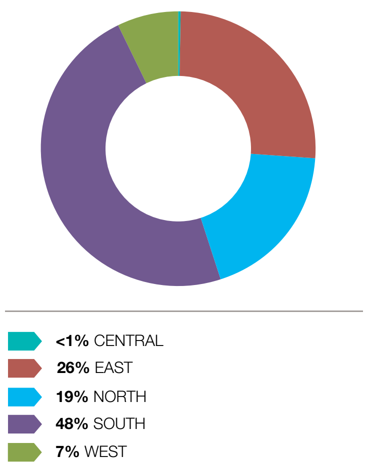
The relative health of each micro-market in Bengaluru can be inferred from the chart below. Currently, east Bengaluru is the healthiest micro-market, as it has one of the lowest QTS and the lowest minimum age of unsold inventory. Hence, despite east Bengaluru witnessing a large unsold inventory, the health of the micro-market is relatively better because the increment in unsold inventory was matched by a similar increase in absorption. South Bengaluru's health is the poorest, as it continues to carry the excess unsold inventory of projects that were launched allmost two years ago. This problem has been compounded by the increase in new launches during H1 2014.

FIGURE 7
Micro-market Split of Absorption in H1 2013



Source: Knight Frank Research

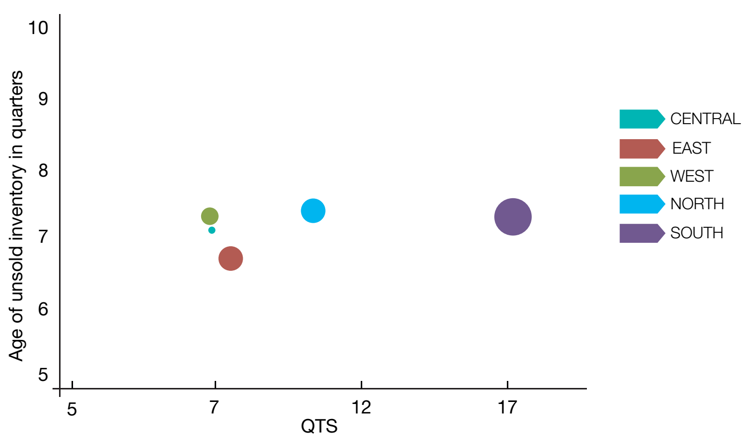
FIGURE 8
Micro-market Split of Absorption in H1 2014



Source: Knight Frank Research

East Bengaluru is the healthiest micro-market, as it has one of the lowest QTS and the lowest minimum age of unsold inventory. Hence, despite east Bengaluru witnessing a large unsold inventory, the health of the micro-market is relatively better because the increment in unsold inventory was matched by a similar increase in absorption

FIGURE 9
QTS vs. Age of Inventory across Micro-Markets



Note: The size of the bubble indicates the quantum of unsold inventory

Source: Knight Frank Research

Key Takeaways

The demand for homes in Bengaluru is expected to rise from 57,366 units in 2013 to 59,300 units in 2014, signifying an increase of 3%. However, this marginal increase in absorption is expected to be accompanied by a drop in the number of new launches by 8% from 78,300 units to 72,113 units during the same period

We expect the sales volume to recover from H2 2014 onwards. It is forecasted to increase by 26% to 32,044 units in H2 2014, compared to H2 2013

The QTS ratio has inched upward, from 6 to 7 since September 2013, signifying a slight weakening of buyer sentiment in the market

South Bengaluru has witnessed the majority of new units launched in H1 2014 due to the presence of a large number of IT companies in IT/ITeS employment hubs such as Electronics City, Sarjapur Road and Bannerghatta Road, as well as good social infrastructure. Additionally, property prices are relatively cheaper in the peripheral locations in the south, compared to the other micro-markets

North Bengaluru observed a fall of 20% in new launches during H1 2014 over the share in H1 2013, as developers deterred from launching fresh projects on the back of lacklustre response received by various projects launched during H2 2013

South Bengaluru's health is the poorest, as it continues to carry the excess unsold inventory of projects that were launched more than two years ago. This problem has been compounded by the increase in new launches during H1 2014

Prices in the majority of the locations across Bengaluru have witnessed a steady, controlled appreciation in the last 12 months. Adequate supply, better infrastructure and the high aspirational quotient attached to the eastern micro-market have pushed prices upwards in the range of 8–15%, coupled with a fair amount of demand. Prices in the other micro-markets of Bengaluru have increased in a similar vein, as compared to H2 2013. The significant build-up in unsold inventory and the availability of a large number of ready-to-move-in apartments have resulted in the constricting price rise in the first half of 2014. However, we expect this to change in the coming months, as signs of revival in demand are already becoming evident in the city, and this could result in prices continuing to move upward H2 2014 onwards.

Price movement in select locations

Location	Micro-market	Price range in H1 2014 (₹/sq ft)	12-month change	6-month change
Langford Town	Central	15,000–18,000	7%	0%
Lavelle Road	Central	21,000–29,000	7%	0%
K.R. Puram	East	4,000–6,000	12%	5%
Whitefield	East	4,500–7,500	15%	6%
Marathahalli	East	4,500–6,800	12%	5%
Indiranagar	East	9,000–12,000	8%	0%
Yeshwanthpur	West	6,500–9,500	12%	5%
Malleswaram	West	9,000–12,000	8%	5%
Rajajinagar	West	8,500–13,500	15%	6%
Tumkur Road	West	3,950–4,500	9%	6%
Yelahanka	North	4,500–7,000	13%	6%
Hebbal	North	5,000–9,000	10%	5%
Hennur	North	4,200–5,500	8%	5%
Thanisandra	North	4,000–7,000	10%	7%
Sarjapur Road	South	4,200–7,000	12%	5%
Electronics City	South	4,000–6,000	8%	2%
Kanakapura Road	South	4,250–5,500	10%	3%
Bannerghatta Road	South	4,200–7,000	12%	4%

*Change in weighted average prices

Source: Knight Frank Research

Notes

OFFICE MARKET

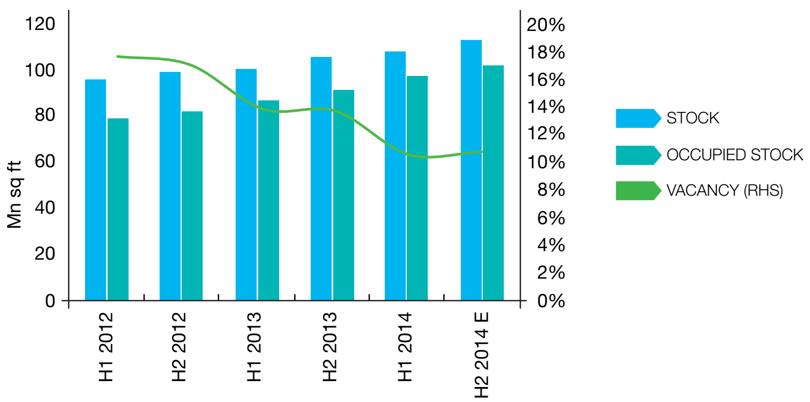
Metropolitan Region Analysis

Bengaluru is one of the key office markets in the southern part of India. Its office market has evolved primarily due to the growth of the IT/ITeS sector in the city. While a number of industries like manufacturing, automobile and biotechnology have their stake in its economy, it is the IT/ITeS sector that has been the predominant driving force. Locations like M.G. Road and Residency Road form the Central Business District (CBD) of the city, while the other important office markets include Koramangala and Old Airport Road in the suburbs. Peripheral locations like Electronics City in the south and Whitefield to the east are the two prime IT/ITeS office markets. Of late, the Outer Ring Road (ORR) has gained prominence as a preferred IT/ITeS office destination in the city.

Known for its vibrant office space market, Bengaluru has consistently topped the absorption charts in the past few years. The IT/ ITeS industry continues to thrive and grow, albeit at a slower pace since the global economic slowdown and the emergence of newer sectors. With an inventory of around 109.5 mn sq ft of office space currently operational, Bengaluru remains one of the most favoured office space destinations in the country. It has seen consistent absorption over the last three years, with vacancy rates dropping steadily every year. This healthy demand in the past years has been responsible for restricting vacancy to 11–18%. The low vacancy levels can also be attributed to the staggered new completions entering the office market each year, although they were significantly outpaced by the absorption in H1 2014. With an occupied stock of 97.9 mn sq ft out of the total office space stock, the vacancy level observed during H1 2014 was 11%, down from 14% in H1 2013.

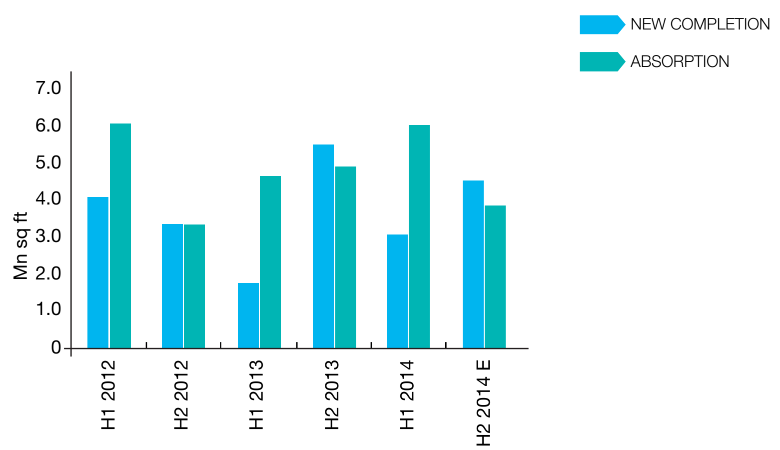
With an inventory of around 109.5 mn sq ft of office space currently operational, Bengaluru remains one of the most favoured office space destinations in the country. It has seen consistent absorption over the last three years, with vacancy rates dropping steadily every year

FIGURE 1
Office Space Stock and Vacancy



Source: Knight Frank Research

FIGURE 2
New Completion and Absorption

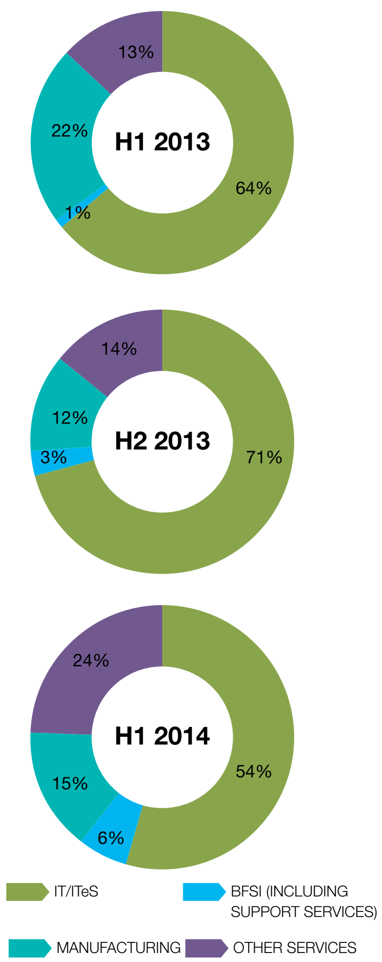


Source: Knight Frank Research

The city's office market clocked a total absorption of around 7.6 mn sq ft during the period January–June 2014, out of which 6.01 mn sq ft were leased transactions, while outright sale deals accounted for the remaining 1.6 mn sq ft

Bengaluru retained the top slot for the highest office space absorption in the country in H1 2014. The city's office market clocked a total absorption of around 7.6 mn sq ft during the period January–June 2014, out of which 6.01 mn sq ft were leased transactions, while outright sale deals accounted for the remaining 1.6 mn sq ft. Significantly, the quantum of outright sale transactions formed a considerable 21% share of the total absorption in H1 2014, more than what had been witnessed in H1 2013. This took place on the back of several large-scale transactions by companies, notable among them being Honeywell, SanDisk and 24X7, which bought office space in the range of 240,000–800,000 sq ft.

FIGURE 3
Sector-wise Absorption Split



Source: Knight Frank Research

The 6.01 mn sq ft of office space leased in the city in H1 2014 matched the absorption witnessed in H1 2012. This reflects a 23% growth over the space leased in the preceding half year (H2 2013), and an increase of 29% over the absorption in H1 2013. The majority of the absorption in the first half of the year 2014 consisted of expansion strategies adopted by companies. The perception of an imminent, stable government at the Center generated hope for growth and structural reforms in the country's economy, causing a number of multinational companies to carry out their expansion plans that were put on hold in 2013.

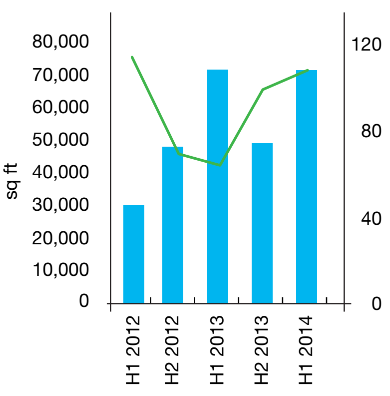
Of the total space absorbed in H1 2014, 54% belonged to the IT/ITeS sector. In the corresponding period of 2013, the share of the sector was more, at 64%, and even higher at 71% in H2 2013. This translates into a downward shift of 24% in H1 2014, compared to the absorption witnessed in the previous six months, though it does not definitively indicate a weakening of the sector. Notwithstanding the relatively less absorption, a number of large transactions took place in H1 2014. Key IT/ITeS occupiers included companies such as Accenture, Honeywell and Altisource.

This waning of the IT/ITeS sector share in the total absorption pie can be attributed partly to the rise in the country's eCommerce sector, categorised under the umbrella of Other Services. Bengaluru saw the advent of several eCommerce firms in the recent past, such as Amazon, Ebay, and national players Flipkart and Myntra, in the office market scenario. This sector has taken up large office spaces in the city and is responsible for taking up the share of the aforementioned category to 24% in H1 2014 from 13% in H1 2013. Besides eCommerce, sectors such as consulting, media and advertising also contributed towards absorption in the Other Services category in H1 2014.

Another key sector in the city's office market—the manufacturing industry—witnessed substantial variations in its share of absorption. While the absorption in H1 2014 increased by 25% over the preceding half year, it lagged behind its corresponding period in 2013 by 32%. On the other hand, the BFSI sector has been struggling to keep its stand in the city's office market. However, it has witnessed considerable improvement since its share of a mere 1% of the total absorption in H1 2013 and 3% in H2 2013. Presently, BFSI is responsible for a 6% share of the total absorption in H1 2014. Some of the prominent companies that took up space during H1 2014 include HSBC Bank and Morgan Stanley.

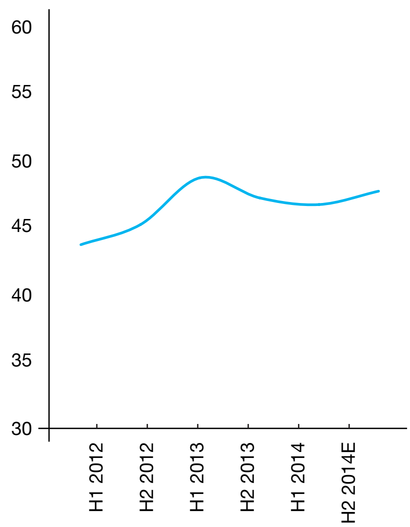
An average deal-side analysis of Bengaluru's office market in the last three years yields some interesting facets. It has been observed that while H1 2013 and H1 2014 experienced similar deal sizes, there was a vast difference between the two corresponding periods regarding the number of deals transacted. H1 2014 had almost matched the high of H1 2012 in terms of the number of deals transacted, whereas H1 2013 saw the lowest number of deals. On the other hand, despite witnessing the highest number of deals, H1 2012 had the lowest average deal size. A large number of small-size deals taking place during a period can be attributed to several factors, such as the proliferation of non-IT sectors looking for small offices, the non-availability of ready large-size office spaces, economic uncertainty impacting the expansion plans of the IT industry, and political ambiguity leading to a wait-and-watch strategy. Significantly, the average size of transactions has increased to 71,500 sq ft in H1 2014 from 30,035 in H1 2012.

FIGURE 4
Deal Size Analysis



Source: Knight Frank Research

FIGURE 5
Weighted Average Rental Movement (₹/sq ft/month)



Source: Knight Frank Research

In H2 2014, we envisage a relatively less active office market as compared to H1 2014, since the majority of the large-scale expansion plans have already been carried out. The absorption in H2 2014 would taper out, and is estimated at around 3.8 mn sq ft, taking the total absorption in leased space in 2014 to 9.81 mn sqft. This would reflect a 3% increase over the total absorption in 2013. However, 2015 has been earmarked as a significant one, based on the new central government's performance.

In H2 2014, we envisage a relatively less active office market as compared to H1 2014, since the majority of the large-scale expansion plans have already been carried out. The absorption in H2 2014 would taper out, and is estimated at around 3.8 mn sq ft, taking the total absorption in leased space in 2014 to 9.81 mn sqft

Weighted average rentals are projected to increase from ₹47/sq ft/month in H1 2014 to ₹48/sq ft/per month in H2 2014, signifying a slight appreciation of 2%

On the supply side, approximately 4.5 mn sq ft of office space is scheduled to be operational by the end of 2014. Weighted average rentals are projected to increase from ₹ 47/sq ft/month in H1 2014 to ₹ 48/sq ft/per month in H2 2014, signifying a slight appreciation of 2%. This rise in rentals is envisaged due to a large quantum of comparativeli higher priced Grade A office space becoming operational in the forthcoming months.

With leasing activity in Bengaluru rising gradually, marginal variations in the weighted average rental have been observed as well. While H1 2014 saw the rental value dip by 4% and 1% compared to H1 2013 and H2 2013 respectively, it is an improvement of 7% over the value in H1 2012. The slight dip in the weighted average rental could be due to a greater number of transactions taking place at non-CBD locations where the rentals are lower. The weighted average rental also depends upon the industry type and the area occupied.

Infrastructure projects in Bengaluru have been largely responsible for giving shape to the city's office markets. Of the current on-going projects in the city, the metro rail is the most ambitious. It has a well-conceptualised plan, designed to cover all corners of the city, ensuring the development of new micro-markets and decongesting older ones. Developers are expected to launch their office projects on the newly-commenced Sampige Road–Peenya stretch in the near future. The full impact of metro rail will be seen only after all its phases are completed, covering peripheral areas like Kanakapura Road in the south and Mysore Road in the west.

The ORR is another significant civic infrastructure project that connects Bengaluru laterally. Its connectivity has improved even further by the signal-free corridor initiative, cutting travel time considerably. Most of the high-traffic junctions now have flyovers or underpasses. This has led to rapid office, residential and mixed-use developments along this belt.

A major infrastructure project on the anvil is the Peripheral Ring Road (PRR). It is aimed at easing congestion on the ORR and connecting the entire peripheral arterial road, linking all the major highways and district roads. The major connecting nodes would be Hosur Road, Tumkur Road, Bellary Road, Old Madras Road and Sarjapur Road. Major office projects are expected along the PRR in the future. Moreover, commercial development is expected to receive an impetus along the metro nodes as well.

Business District Analysis

The Bengaluru office market can be classified broadly into five business districts, with locations within each business district sharing similar characteristics in terms of rent, demand drivers, preference of occupiers, infrastructure development and distance from the city centre.

Business District	Location
Central Business District (CBD) and off-CBD	M.G. Road, Residency Road, Cunningham Road, Lavelle Road, Richmond Road, Infantry Road
Suburban Business District (SBD)	Indiranagar, Koramangala, Old Airport Road, Old Madras Road
Peripheral Business District (PBD) East	Whitefield
Peripheral Business District (PBD) South	Electronics City, Bannerghatta Road
Outer Ring Road (ORR)	Hebbal ORR, Marathahalli ORR, Sarjapur Road ORR

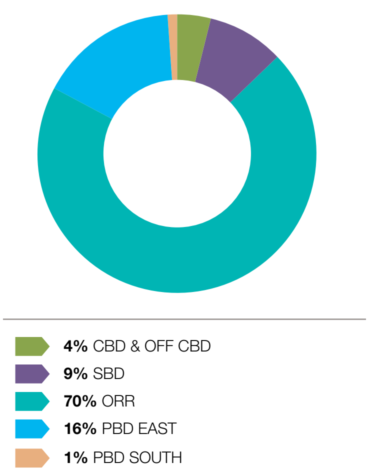
The Bengaluru real estate market observed consistent demand for IT space and for other emerging sectors across all its micro-markets in H1 2014. The dearth of quality office space in the central locations as well as in a few suburban micro-markets of the city caused companies to take up space in peripheral markets like Whitefield and the ORR, which have considerable new office space supply.

Generally, the CBD and off-CBD office markets are preferred by companies, mostly non-IT in nature, looking for smaller office configurations. Around 0.27 mn sq ft was transacted in the CBD and off-CBD locations in H1 2014, while H1 2013 saw approximately 1.91 mn sq ft of office space being leased out in these business districts. Interestingly, the share of office space absorption over these two corresponding periods remained the same at 4%. Some of the key tenants who took up space in these CBD and off-CBD locations in H1 2014 include URS at Pride Elite on Museum Road and Herbalife at RMZ Pinnacle on Commissariat Road.

Like the CBD, the SBD office markets, too, displayed a similar absorption share of 9% in H1 2013 and H1 2014. A majority of the transactions took place in standalone office projects located in Koramangala, which offer small to mid-size office spaces to IT and non-IT companies alike. Indiranagar, Malleswaram and Old Airport Road also saw interest from occupiers in recent months. Some notable transactions in H1 2014 in the suburban business districts include office space taken up by Wildcraft at Suraksha La Classic on the ORR at J P Nagar, and ABB at World Trade Centre at Malleswaram.

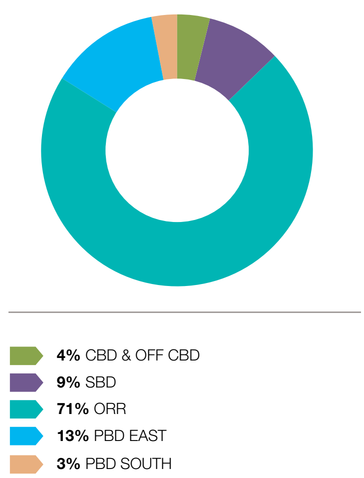
Meanwhile, the peripheral markets that, until a few years back, ruled the roost, boasting of absorbing most of the IT firms entering Bengaluru, have now lost their hold over the IT sector. Although Whitefield in PBD East has still managed to keep its grip fairly, Electronics City in the south has almost been superseded owing to lack of social infrastructure in the region. Although the elevated expressway from Silk Board to Electronics City has brought down the commuting time, the office sector has yet to feel its positive impact. Not surprisingly, the share of PBD South has declined significantly and remains at 3% in H1 2014.

FIGURE 6
Business District-wise Absorption Split in H1 2013



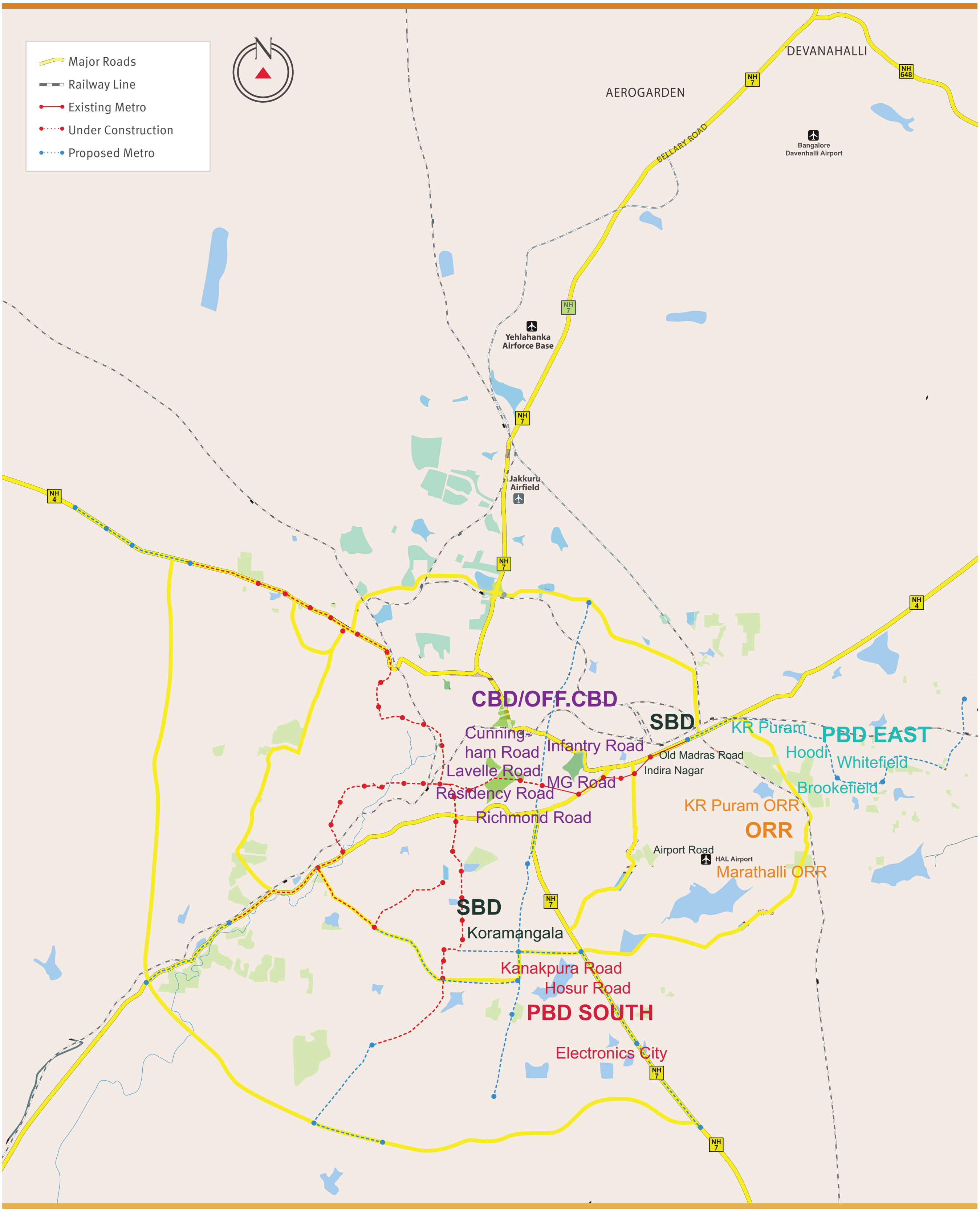
Source: Knight Frank Research

FIGURE 7
Business District-wise Absorption Split in H1 2014



Source: Knight Frank Research

BUSINESS DISTRICTS OF BENGALURU



Despite stiff competition from the ORR office markets, Whitefield garnered 16% of the total office space absorption in Bengaluru in H1 2013. Although the share came down to 13% in H1 2014, it will continue to remain on the occupiers' radar in the forthcoming years owing to attractive lease rentals, the presence of good residential projects and social infrastructure. Key tenants that occupied office space in the PBD East office markets during the H1 2014 include Canadian Standard Association at Beary's Global Research Triangle on Sai Baba Ashram Road, and Unisys at SJR I Park.

The ORR, encompassing the stretch from Hebbal in the north to Silk Board Junction in the south, has emerged as the leading IT growth corridor in the city. The region has increasingly been preferred by corporates due to factors like proximity to the CBD and major residential markets, access to large talent pools, the availability of contiguous land parcels, connectivity to the airport and the presence of hotel and retail projects. Today, it houses most of the big players in the industry, such as Cisco, IBM and Intel. The ORR office market has witnessed considerable activity in 2014, accounting for transactions of over 5 mn sq ft till June. It has surpassed the other office markets of the city and maintained its share at 70% in H1 2013 and 71% in H1 2014. Some of the notable occupiers that took up space in H1 2014 are Symantec in RMZ Ecoworld, and 24X7 in Prestige Tech Park.

Despite stiff competition from the ORR office markets, Whitefield garnered 16% of the total office space absorption in Bengaluru in H1 2013. Although the share came down to 13% in H1 2014, it will continue to remain on the occupiers' radar in the forthcoming years

Select Transactions in the Bengaluru Office Market

Building	Occupier	Location	Approx. Area (sq ft)
RMZ Pinnacle	Herbalife	Commissariat Road	88,000
DivyaSree Techno Park	Capgemini	Whitefield	440,000
Manyata Embassy Business Park	Lowe's	Hebbal Outer Ring Road	70,000
Pritech Park	Altisource	Sarjapur Outer Ring Road	180,000
Global Village Tech Park	Accenture	Off Mysore Road	68,187
Bagmane Tech Park	HSBC	CV Raman Nagar	90,000
Manyata Embassy Business Park	L&T Engineering	Hebbal Outer Ring Road	500,000
Confident Octans	Royal British Hospital	Electronics City	150,000
RMZ Ecoworld	Time Analytics Services	Sarjapur Outer Ring Road	74,877
Prestige Shantiniketan	Caterpillar	Whitefield	80,000

Source: Knight Frank Research

Key Takeaways

The year 2013 witnessed substantial momentum in office market demand, which continued in 2014. Around 6.01 mn sq ft of office space was leased out in H1 2014

While the demand from IT/ITeS sector regained ground in 2013, the first half of 2014 saw demand brought about from several other quarters as well, particularly the eCommerce and manufacturing sectors

The weighted average rental that saw a slight weakening in H1 2014 compared to H1 and H2 2013 is expected to pick up again in H2 2014

The on-going global economic recovery bodes well for the prospects of the IT/ITeS sector, and Bengaluru, being the IT/ITeS exchange of India, stands poised to capitalise on the same

Adequate supply in the pipeline in all the markets will ensure steady rentals and consistent demand over the next six months, and will constrict vacancy to 11% by the end of 2014

The restoration of business confidence by way of healthy absorption in H1 2014 is expected to carry forward a positive, albeit cautious, business outlook. The forthcoming year (2015) has been earmarked as a significant one, based on the performance expected of the new central government

Market sentiment will stay upbeat over the medium term as IT/ITeS sector revenues are expected to stay strong due to signs of recovery in western economies

Business District-wise Rental Movement

Business District	Rental Value Range in H1 2014 (₹/sq ft/month)	12-month change	6-month change
CBD and off-CBD	72–85	-5%	-3%
SBD	47–78	3%	5%
PBD East	30–45	6%	5%
PBD South	30–45	3%	1%
ORR	45–55	9%	8%

Source: Knight Frank Research

The average rental movement across different micro-markets has been relatively marginal over the last year. The rentals remained constant for most part, witnessing changes in the range of 1-8% during the last six months, and 3-9% in one year. The ORR office projects saw the highest appreciation in rentals due to the amount of traction in the market. While all the office markets saw the upward movement of rentals, CBD rentals witnessed a slight decline. This could be attributed to the dearth of quality office space in the region, with transactions taking place in older office developments with lower rental values.

A number of infrastructure projects are going on in the city. In the northern zone, the six-lane Hebbal–Yelahanka Elevated Expressway is expected to cut down the time taken to reach the international airport considerably. As a result, the region will witness more commercial developments, owing to the reduction in commuting time. This will impact the IT/ITeS SEZs under construction on Hennur Road and Bellary Road in particular.

Among the recent infrastructure developments, Bengaluru witnessed the launch of the second metro rail stretch in March 2014, a 9.9-km line of track connecting the city's north-western suburbs in Peenya to Sampige Road in the west. Existing office projects, such as Brigade Gateway at Yeshwanthpur, are expected to strengthen their stand owing to the metro rail, while more commercial projects with office spaces are expected to come up along the Sampige Road–Peenya stretch.

Another important development has been the announcement by global IT major Cisco about its intention to turn Electronics City into a smart city and develop Asia's first Internet of Things (IoT) innovation hub there. The project will help companies in Electronics City innovate and develop products and software applications for deployment in the 100 Smart Cities project that the newly-formed NDA government is planning to set up across the country. This development augurs well for the office market of Electronics City, which has seen considerable waning of occupier interest in the recent months.

Notes

CHENNAI

RESIDENTIAL MARKET

Metropolitan Region Analysis

The Chennai residential market is one of the steadiest markets in India. It proved its resilience during one of the toughest periods in 2008–09, when it remained relatively stable in terms of sales volume and price, as compared to cities like Mumbai, NCR, Bengaluru and Hyderabad. The demand for residential real estate comes predominantly from end users, thereby limiting the scope for erratic price movement in this market. Additionally, the developer community in the city has historically been cautious in its approach towards buyer sentiment, and has time and again resisted the temptation to increase prices sharply, even during buoyant times. Due to this, the Chennai market is recognised as one of the most stable residential markets in the country.

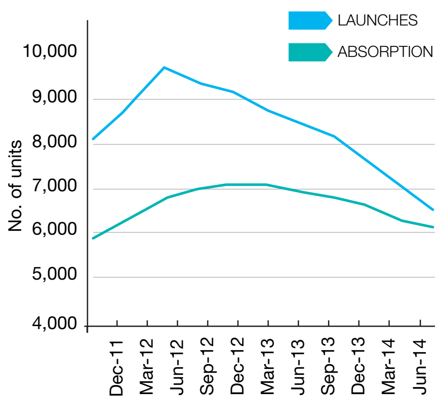
The indigenous demand for residential apartments kept the Chennai residential market afloat till 2013. The world economic turmoil due to the global financial crisis completed its fifth year, but headwinds continued across the global economy. India and the Indian real estate sector were not exceptions. After being resilient to negative global factors till 2013, the Chennai residential market succumbed to the declining trend phenomenon. All major economic parameters, such as bank interest rates, mortgage rates and inflation continued their upward movement, compelling consumers to postpone their discretionary spending, including buying a house.

The cautionary mood of end users is reflected in the volume of the Chennai residential absorption, which reported a 35% decline in H1 2014, as compared to the corresponding period (H1 2013) in the previous year. Taking cognizance of this trend, the Chennai residential developer community has prudently reduced the number of new launches during the last 12 months. This can be observed in Chart 1, where a comparison between the moving average of launches and absorption has been drawn. This analysis has been done on a long term (eight quarters) moving average basis, in order to eliminate any volatility due to seasonal factors.

The lines in Chart 1 clearly indicate that the gap between new launches and absorption has reduced gradually since June 2012 and reached a minimum level in June 2014. From their peak in H1 2012, launches and absorption in the Chennai residential market have declined by 47% and 37% respectively in H1 2014. Moreover, the narrowing gap between the two lines in Chart 1 clearly implies that the developer community has reacted promptly and moderated the pace of new launches, in line with the slowdown in absorption. Chart 1 may give an impression of an improving market condition, but the true picture cannot be assessed without understanding the impact of the existing unsold inventory in the market.

The growth in demand for residential units witnessed in 2010–2011 boosted

FIGURE 1
Long Term (Eight Quarters) Moving Average Trend of Launches and Absorption

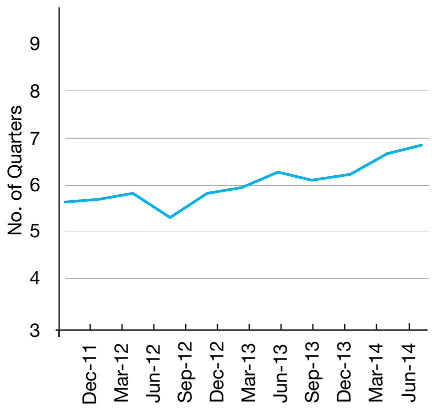


Source: Knight Frank Research

After a slow uptick in the first half of 2014, launches and absorption is estimated to increase by 31% and 14% respectively in H2 2014. Launches for the full year 2014 would witness a relatively higher decline (12%), compared to absorption (9%)

the confidence of Chennai developers and prompted them to launch larger projects. However, in subsequent years, this trend could not sustain itself, and the annual absorption levels returned to their long-term averages of 23,000–25,000 units annually. Absorption was not able to keep pace with the number of new launches. This resulted in a gradual build-up in unsold inventory. For a better understanding of the extent of unsold inventory, we have conducted a Quarters to Sell (QTS) analysis. QTS is the number of quarters required to exhaust the existing unsold inventory in the market. The existing unsold inventory is divided by the average sales velocity of the preceding eight quarters in order to arrive at the QTS number for that particular quarter. A lower QTS indicates a healthier market.

FIGURE 2
Quarters to Sell Analysis



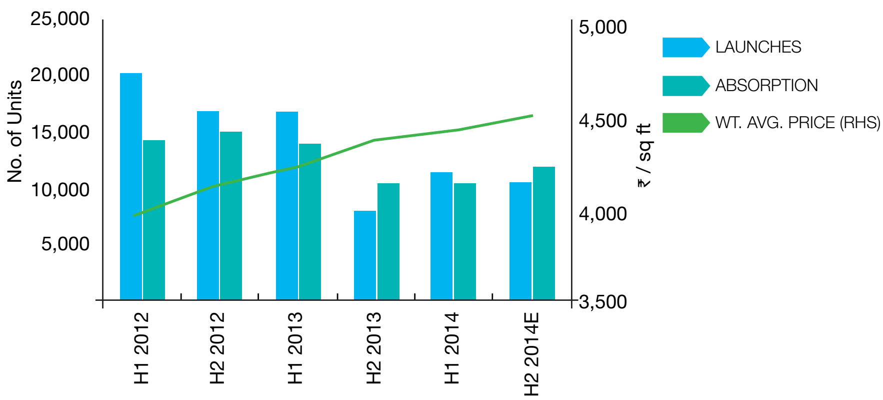
Source: Knight Frank Research

The QTS line in Chart 2 shows how QTS has moved from less than 6 in March 2013 to almost 7 in June 2014. This means that while it would have taken only six quarters (or 18 months) for the market to absorb the unsold inventory in March 2013, it will take seven quarters (or 21 months) for the same to happen in June 2014. This analysis indicates a falling trend in the health of the market, which could have a direct bearing on the prices of residential properties in the city. However, it would be unfair to consider the entire city as a single market and draw conclusions from such an analysis. Since each micro-market is driven by a different set of demand-supply dynamics, the movement in prices could vary across locations. Hence, studying each micro-market is imperative in order to understand their respective demand-supply scenarios and their impact on price movement. This analysis has been done in the subsequent section.

The year 2014 is expected to be good for Chennai infrastructure projects. The second half of the year is expected to

Chennai Metro Rail will significantly benefit locations closer to the metro stations viz. Vadapalani, Ashok Nagar and Alandur

FIGURE 3
Launches, Absorption and Price Trend



Source: Knight Frank Research

witness the successful commissioning of the Outer Ring Road (ORR) Phase I, i.e. the stretch from Vandalur to Nemilichery. The Outer Ring Road connects the northern and southern suburbs of Chennai. It will be a catalyst for the expansion of the city, and will help the growth of industrial hubs in this region through better connectivity. This six-lane highway will ease traffic congestion significantly along the western periphery of Chennai city. It will connect GST Road (NH 45) with the Chennai–Bangalore Highway (NH 4) and NH 205. Residential development in locations like Kuthambakkam, Chembarambakkam and Poonamallee in West Chennai has been observed to be gaining traction due to this new infrastructure.

The commissioning of the Chennai Metro Rail Phase-I is expected to be another milestone in the city's infrastructure development in H2 2014. Trial runs of the Koyambedu and Alandur lines are currently underway. After conducting several trial runs, the route will be opened to the general public in H2 2014. A good demand for residential locations closer to the metro stations is expected. Of the seven metro stations, locations like Vadapalani, Ashok Nagar and Alandur are expected to benefit the most.

The recent collapse of a 12-storey building under construction at Moulivakkam in West Chennai has severely dented the sentiments of home buyers and their trust in real estate developers. The local development authority has become cautious after this event. In order to prevent the recurrence of such events, soil testing has been made compulsory for all under-construction projects. The state government has also directed the approving authority to review all planning and building permit applications more diligently. This stringent approval process is likely to lead to further delay in the already elongated process of receiving approvals. This will affect smaller developers more adversely than larger and more reputed developers who are already adhering to all the processes. The only silver lining is that home buyers will prefer to buy from reputed developers with a strong track record. However, it cannot be denied that there would be fewer new launches in the near future due to changes in the approval process.

Economic sentiment took a big U-turn post the general election, and more so after the first union budget of the newly-elected government. The cash-starved realty sector finally got due attention from the union government as new ways to raise funds were introduced. Moreover, increasing tax sops on the purchase of new homes will benefit the Chennai realty market significantly. The dominant employer in the region – the IT/ITeS sector – has signalled optimism for business in FY 2015. Considering these factors, after a slow uptick in the first half, we estimate new launches and absorption to increase by 31% and 14% respectively in H2 2014, compared to the same period last year. However, despite a steadier second half of 2014, the Chennai residential market would continue its declining trend on an annual basis. On account of the high unsold inventory, new launches in the Chennai realty market would witness a relatively higher decline (12%), compared to absorption (9%). Moreover, new launches are concentrated in the peripheral markets, where prices range between ₹ 4,000 and ₹ 6,500 per sq ft. The weighted average price in the Chennai market is forecasted to increase by 3% for the full year (2014) against the 5% increase witnessed in H1 2014.

Collapse of a under construction building severely dented the sentiments of home buyers across city. Approval process have now being made stringent, this is likely to lead to further delay in the already elongated process of receiving approvals

Micro-market analysis

The Chennai residential market can be classified broadly into four micro-markets, with locations within each micro-market sharing similar characteristics in terms of price, quality of projects, buyer segment, infrastructure development and distance from the city centre, among others.

Micro-market	Location
Central	Nungambakkam, Boat Club, Anna Nagar, Kilpauk, T. Nagar, Mylapore, R.A.Puram, Adyar
West	Sriperumbudur, Ambattur, Poonamallee, Korattur, Mogappair, Porur, Manapakkam
North	Tondiarpet, Madhavaram, Perambur, Ayanavaram, Puzhal
South	Old Mahabalipuram Road (OMR), GST Road, East Coast Road

Since the Bay of Bengal lies to the east of Chennai, real estate development in the city is concentrated in the other three directions. Residential real estate development is non-existent in North Chennai, primarily due to the non-availability of vacant land, the existence of narrow arterial roads and lack of employment opportunities. Central Chennai is the oldest and most premium residential micro-market in the city, and has little potential for further development due to unavailability of land. This has compelled developers to look for greener pastures in the South and West Chennai markets. Affordable prices, abundant vacant land, and proximity to the city centre and employment hubs attracted developers and end users alike to the South and West Chennai micro-markets. Of the 101,212 under-construction units in Chennai city, the South Chennai market has the largest share of under-construction units (66%), followed by West Chennai (26%). The very expensive Central Chennai market and the under-developed North Chennai market account for 4% each.

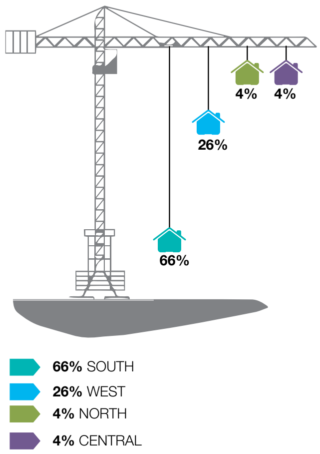
Central Chennai is where the elite reside and work, and is the most sought-after market. Being the state capital, Chennai houses government administrative offices, headquarters of many South India-based corporates, and is home to industrialists, politicians and high net-worth individuals (HNIs). Despite the non-availability of developable land, this micro-market fared well in H1 2014, as it witnessed a 116% increase in new launches. Residential prices in locations like Anna Nagar, Adyar and T. Nagar have increased by 4%, 3% and 1% respectively in H1 2014, as compared to the same period last year. Apartments with a ticket size of less than ₹ 10 mn are not available in this micro-market. High residential prices with bigger unit sizes made owning an apartment in Central Chennai unaffordable, even for the elite. This led to a 23% decline in absorption during H1 2014, as compared to the same period last year. A QTS ratio of 5 implies that the inventory in this micro-market will take five quarters to sell, while the age of inventory, calculated as the time elapsed since launch, is at nine quarters. A healthy micro-market is defined as one with a low QTS ratio and a low age of inventory.

Real estate development mushroomed in South Chennai after it was catalogued as the growth corridor of the city. The focus of the state government over the last decade in promoting Old Mahabalipuram Road (OMR) as an IT/ITeS destination, along with the setting up of Mahindra World City on GST Road, has created immense employment opportunities in

The Central Chennai micro-market is the second best market in Chennai basis QTS and inventory age

CHENNAI METROPOLITAN REGION MAP

FIGURE 4
Micro-market Split of Under-Construction Units as on June 2014



Source: Knight Frank Research

South Chennai. Consequently, OMR, GST Road and various locations between these two roads have emerged as the most favoured locations for office and residential development. Proximity to Chennai International Airport, the presence of arterial roads and the availability of huge vacant land parcels have enabled South Chennai to grow rapidly into an emerging residential market. Moreover, it offers affordable apartment options, as almost 92% of the launched units' ticket sizes are below ₹ 7.5 mn. The weighted average prices in this micro-market have remained subdued, with the price growth ranging between 1-2% as compared to the first half of 2013.

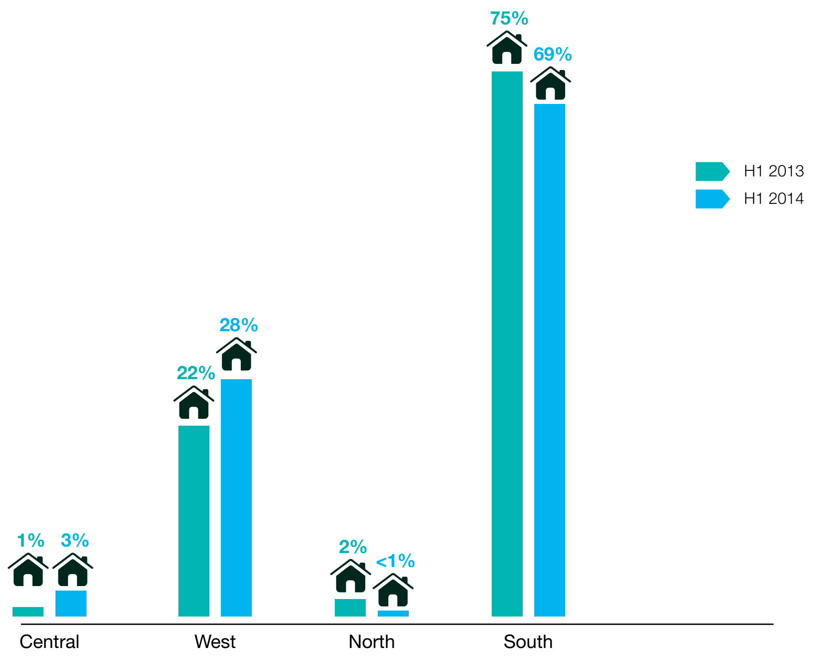
Price movement in select locations

Location	Micro-market	Price range in H1 2014 (₹/ sq ft)	Change since H1 2013*	Change since H2 2013*
Anna Nagar	Central Chennai	9,800-10,100	4%	-1%
Adyar	Central Chennai	16,500-17,500	3%	-1%
Kilpauk	Central Chennai	15,000-15,100	0%	2%
T. Nagar	Central Chennai	18,500-18,700	1%	1%
Alandur	Central Chennai	7,000-7,200	1%	1%
Porur	West Chennai	5,100-5,300	2%	-2%
Ambattur	West Chennai	4,100-4,500	2%	0%
Mogappair	West Chennai	6,100-6,700	2%	0%
Iyappanthangal	West Chennai	3,900-4,300	-2%	2%
Sriperumbudur	West Chennai	2,700-3,000	-2%	-3%
Perumbakkam	South Chennai	4,100-4,300	2%	2%
Chrompet	South Chennai	4,200-4,700	1%	3%
Sholinganallur	South Chennai	4,300-4,800	-1%	-3%
Guduvancheri	South Chennai	3,150-3,300	1%	-2%
Kelambakkam	South Chennai	3,525-3,625	2%	-1%
Tondiarpet	North Chennai	4,200-4,300	1%	-1%
Kolathur	North Chennai	4,300-4,500	2%	2%
Madhavaram	North Chennai	4,500-4,700	2%	2%
Perambur	North Chennai	6,000-6,400	3%	3%
Ponneri	North Chennai	3,500-3,600	1%	1%

* Change in weighted average prices
Source: Knight Frank Research

Of the 101,212 under-construction units in Chennai city, the South Chennai market has the largest share of under-construction units followed by West Chennai

FIGURE 5
Micro-market Split of Launched Units in H1 2013 and H1 2014



Source: Knight Frank Research

South Chennai leads the Chennai residential market in terms of the number of units launched and absorbed. Despite witnessing a 37% decline in new launches during H1 2014 as compared to the same period last year, South Chennai continues to account for the lion's share (69%) in the Chennai residential market. However, a lacklustre economy arrested the absorption momentum in this micro-market, which, in turn, led to an increase in unsold inventory. At a QTS ratio of 7, South Chennai will take a little over two years to clear the inventory that has an average age of nine quarters.

The emergence of the West Chennai micro-market as one of the better residential micro-markets is due to affordable pricing, proximity to the city centre, the presence of employment hubs (IT/ITeS offices) and relatively better developed social infrastructure. Amidst limited opportunity for real estate development in Central Chennai and huge competition in the South Chennai region, developers found greener pastures in the West Chennai micro-market. Increased preference for this market can be substantiated by the growth in the share of new launches, which has increased to 28% in H1 2014, as compared to 22% in the same period last year. West Chennai offers the highest options for affordable apartments. Almost 97% of the units launched in H1 2014 are under ₹ 7.5 mn.

A large number of projects were launched during 2012 and 2013 in locations like Ambattur, Mogappair and Porur, resulting in an oversupply situation. Taking cognizance of such a scenario, developers seem to have deliberately restricted the flow of new launches during the last year. New launches declined by 14% during H1 2014, as compared to the same period in the previous year. The oversupply situation kept residential prices under check, especially in locations like Sriperumbudur and Iyyappanthangal. Weighted average residential prices in locations like Porur, Ambattur and Mogappair increased by 2% in H1 2014, as compared to the same period last year. West Chennai has an

The South Chennai micro-market, with the highest quantum of inventory, is facing problems of high unsold inventory

Key Takeaways

The year 2014 is expected to be good for Chennai infrastructure projects. The second half of the year is expected to witness the successful commissioning of the Outer Ring Road (ORR) Phase I as well as the Chennai Metro Rail Phase-I

ORR is expected to benefit residential development in locations like Kuthambakkam, Chembarambakkam and Poonamallee in West Chennai

Chennai Metro Rail will significantly benefit locations closer to the metro stations viz. Vadapalani, Ashok Nagar and Alandur

Collapse of a under construction building in West Chennai has severely dented the sentiments of home buyers across Chennai residential market. Approval process have now being made stringent, this is likely to lead to further delay in the already elongated process of receiving approvals. The only silver lining is that home buyers will prefer to buy from reputed developers with a strong track record

Positive economic sentiment post the general election, increased tax sops on the purchase of new homes and optimism build for the IT/ITeS sector growth in FY 2015 will benefit the Chennai realty market significantly

After a slow uptick in the first half of 2014, launches and absorption is estimated to increase by 31% and 14% respectively in H2 2014. While on account of the high unsold inventory, launches for the full year 2014 would witness a relatively higher decline (12%), compared to absorption (9%)

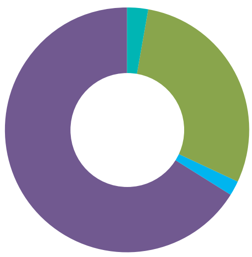
unsold inventory of six quarters with an average age of eight quarters.

The North Chennai population constitutes largely of business communities that have offices in nearby localities and are generally averse to the idea of shifting to other locations within the city. North Chennai has many industrial units, due to which there are limited options for white-collar jobs. Despite the North Chennai micro-market offering the bulk of new launches within the ticket size of ₹ 2.5 mn, migrant as well as local IT/ITeS employees prefer residing in South Chennai, primarily on account of its proximity to business districts and relatively better developed social infrastructure. However, this image of North Chennai is expected to change.

As per the Union Budget 2014-15, Ponneri is one of the hundred planned smart cities announced by the government. This smart city will include industrial parks and commercial buildings, as well as residential development. The announcement augurs well for the entire North Chennai residential market.

In the entire North Chennai zone, Tondiarpet, Madhavaram, Perambur and Ayanavaram were the only locations that witnessed an increase in new launches. These locations also saw an increase in prices primarily due to lack of quality projects elsewhere in this micro-market. The market share for this market dropped significantly in H1 2014, as compared to the same period last year. At a QTS ratio

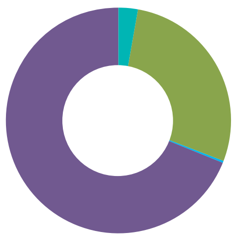
FIGURE 6
Micro-market Split of Absorption in H1 2013



3% CENTRAL
29% WEST
2% NORTH
66% SOUTH

Source: Knight Frank Research

FIGURE 7
Micro-market Split of Absorption in H1 2014

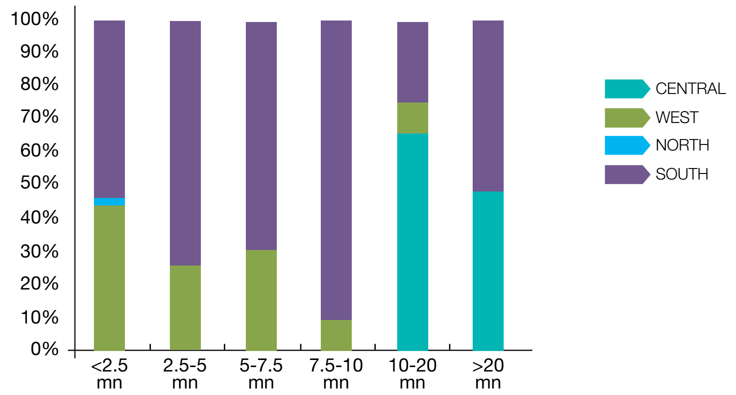


3% CENTRAL
26% WEST
3% NORTH
68% SOUTH

Source: Knight Frank Research

FIGURE 8

Micro-market Level Ticket Size Split of Launched Units During H1 2014



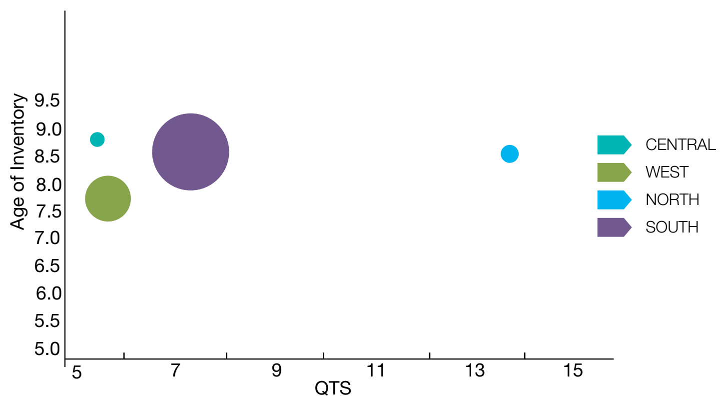
Source: Knight Frank Research

of 14, North Chennai is the worst market, as compared to other micro-markets. It will take almost five years to clear the inventory that has been in the market for 8.5 quarters.

Chart 8 depicts the health of the Chennai residential market. The West Chennai micro-market, with an inventory of six quarters and an inventory age of eight quarters, fares the best in Chennai city. Developers in North Chennai have launched projects ahead of time, as the residential demand in this micro-market is yet to pick up. The North Chennai micro-market, with an inventory of 14 quarters and an inventory age of nine quarters, fares the worst in the city. The Central Chennai micro-market is the second best market in Chennai, with a QTS of 5 and an inventory age of 9. The quantum of inventory, however, is the lowest in this market. The South Chennai micro-market, with the highest quantum of inventory, is facing problems of high unsold inventory. However, this is the third best market in Chennai, based on the parameter of a 7-quarter inventory that was launched 9 quarters ago.

FIGURE 9

QTS vs. Age of Inventory Across Micro Markets



Note: Size of the bubble indicates the quantum of unsold inventory

Source: Knight Frank Research

Key Takeaways

The weighted average price is forecasted to increase by 3% by the end of 2014 against the 5% increase witnessed in H1 2014

Of the 101,212 under-construction units in Chennai city, the South Chennai market has the largest share of under-construction units (66%), followed by West Chennai (26%). The expensive Central Chennai market and the under-developed North Chennai market account for 4% each

In the Union Budget 2014-15, Ponneri in North Chennai has being announced as one of the hundred planned smart cities. The announcement augurs well for the entire North Chennai residential market

The West Chennai micro-market, with an inventory of six quarters and an inventory age of eight quarters, fares the best in Chennai city

Developers in North Chennai have launched projects ahead of time, as the residential demand in this micro-market is yet to pick up. The North Chennai micro-market, with an inventory of 14 quarters and an inventory age of nine quarters, fares the worst in the city

The Central Chennai micro-market is the second best market in Chennai, with a QTS of 5 and an inventory age of 9. The quantum of inventory, however, is the lowest in this market

The South Chennai micro-market, with the highest quantum of inventory, is facing problems of high unsold inventory. However, this is the third best market in Chennai, based on the parameter of a 7-quarter inventory that was launched 9 quarters ago

OFFICE MARKET

Metropolitan Region Analysis

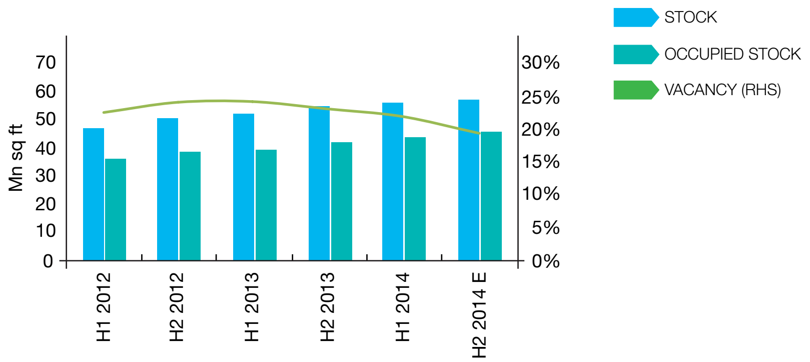
Chennai has always been an industrial hub and is now counted among the most dynamic office markets in the country. Manufacturing industries such as auto and auto ancillary, electronic hardware, apparel and engineering thrived here and promoted the development of an office space market in the city. This has been supported even further by the robust growth of the IT/ITeS sector. Pre-empting the multifaceted potential of the IT/ITeS sector, the state government introduced favourable policies for setting up IT/ITeS companies in Chennai. This, along with exemplary infrastructure and the availability of a talent pool, encouraged a large number of companiesto set up their global delivery centres here. The increasing demand from the IT/ITeS sector led to the emergence of suburban and peripheral business districts (SBDs and PBDs), where the availability of large tracts of land helped in the development of office space.

The IT/ITeS sector, having the lion's share in Chennai's office market in recent years, as well as traditional economic drivers like the manufacturing industry had slowed down expansion activity due to the overall economic turmoil. Additionally, numerous projects launched during 2008–11 have come online between H1 2012 and H1 2014, effectively adding almost 30% to the existing office stock. This huge supply of new office space triggered a glut in the market, as absorption could not keep up with the pace of deliveries. The continuous slowdown in the economy compelled large occupiers to re-strategize their expansion plans. During this demanding time, major corporates sought to consolidate their multiple offices across India to save on the overall cost of operation. In H1 2014, the total office space stock in Chennai stood at 56.2 mn sq ft, while the occupied stock stood at 43.8 mn sq ft. Further, all the above factors resulted in high vacancy levels, which now stand at 22% in the Chennai office market.

The year 2013 ended on an optimistic

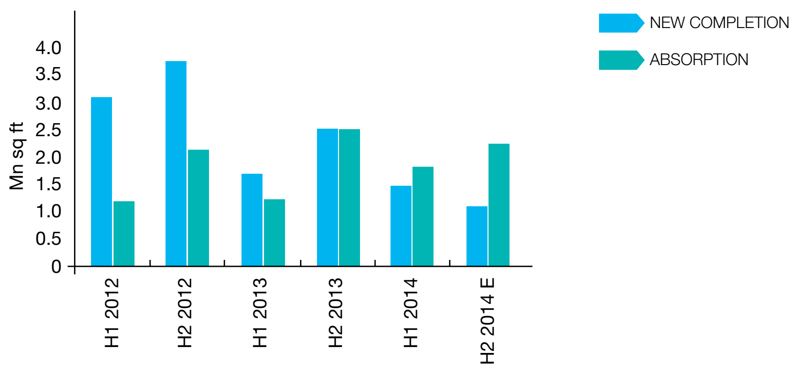
Better-than-expected absorption numbers of over 1.8 mn sq ft were reported during the first half of 2014, registering a growth of 47% over H1 2013

FIGURE 1
Office Space Stock and Vacancy



Source: Knight Frank Research

FIGURE 2
New Completion and Absorption of Office Space



Source: Knight Frank Research

The city's vacancy level is projected to decrease to 20% in H2 2014, as compared to 22% in H1 2014

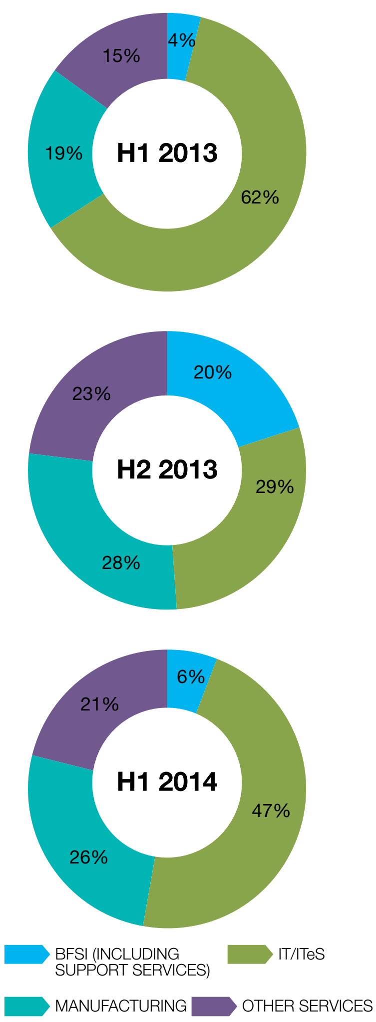
note in terms of the global and domestic economy. Stability in the developed economies of the Western world led to an increase in their discretionary spending. Among others, the IT/ITeS sector benefitted the most from this development. Better-than-expected absorption numbers of over 1.8 mn sq ft were reported during the first half of 2014, registering a growth of 47% from H1 2013.

In H1 2014, the IT/ITeS, manufacturing and other services sectors were the major industries in Chennai and accounted for 47%, 26% and 21% of the total occupied office space respectively. Demand for office space from other service sector companies has been increasing consistently over a period of time. This sector includes a wide range of service industries, such as consulting, telecom, eCommerce, shipping and infrastructure. Office space demand from the BFSI sector has been quite volatile during the last 18 months. After accounting for 20% of the total office space demand in H2 2013, it now stands at only 6%. However, going forward, we expect the IT/ITeS sector to continue to remain the largest occupier of office space in the city. Low rentals, better quality space, the availability of a skilled talent pool, rapid infrastructure development and a favourable business environment are some of the major aspects that will attract companies from this sector.

An analysis of the number of transactions reflects the liquidity condition of the office market. The Chennai market averages 50–55 transactions every six months, and given the present optimistic economic outlook, the steep rise in the number of transactions to 71 in H1 2014 comes as no surprise. The average size of transactions has reduced to 23,600 sq ft in H1 2014, as against 26,800 sq ft in H1 2013. This 12% decline can be substantiated by the fact that, of the total number of transacted deals in H1 2014, approximately 60% had an average size of less than 15,000 sq ft. Ticket sizes of transactions influence the rental movement during a particular period. It has been observed that tenants of small-size deals are often price takers; hence, their deals are executed at relatively higher prices than tenants of large-size deals. The 5.7% increase in the rental rate registered in the preceding six months explains the relationship between deal size and rentals. The average office space rental for the city has risen by approximately 5% every year; it grew from ₹ 43/sq ft/month in H1 2012 to ₹ 48/sq ft/month in H1 2014.

Going forward, we expect 2.23 mn sq ft of office space to be absorbed in the

FIGURE 3
Sector-wise Absorption Split



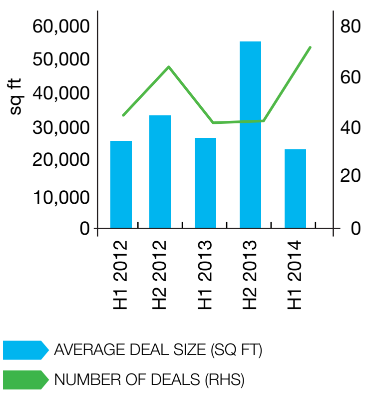
Source: Knight Frank Research

Chennai market during H2 2014, resulting in a 11% decline compared to H2 2013. However, on an annual basis for the year 2014, the total absorption is expected to touch 4.02 mn sq ft, thereby registering an increase of 8% from the 3.74 mn sq ft achieved during 2013. Conversely, 2014 will see only 2.56 mn sq ft of office space attaining completion compared to 4.21 mn sq ft in the previous year. Consequently, overall vacancy level is projected to decrease to 20% in H2 2014 as compared to 22% in H1 2014. Some of the key projects expected to enter the market in the coming months are TRIL at OMR and various smaller projects across PBDs and SBDs.

The rising trend in office rental value is expected to continue on the back of improved global and domestic economic sentiment. However, a robust pipeline of new supply by the end of 2014 is expected to restrict rental growth to single digits. The city's weighted average rental value is forecasted to increase from ₹ 48/sq ft/month in H1 2014 to ₹ 50/sq ft/month in H2 2014.

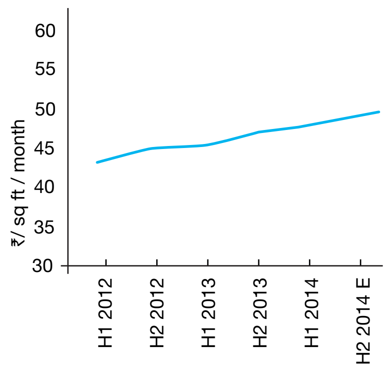
Progress on major infrastructure such as the Chennai Metro Rail and Outer Ring Road (ORR) is quite remarkable. Although marginally behind schedule, both these projects are expected to see the light of day in the second half of the current year. The metro will benefit locations closer to its stations. It is also expected to decongest road traffic and reduce the commuting time between Koyambedu and Alandur. The six-lane ORR stretch from Vandalur to Nemilichery will connect GST Road (NH 45) to the Chennai–Bangalore Highway (NH 4) and NH 205. This will ease traffic congestion significantly along the western periphery of Chennai city.

FIGURE 4
Deal Size Analysis



Source: Knight Frank Research

FIGURE 5
Weighted Average Rental Movement (₹/sq ft/month)



Source: Knight Frank Research

The CBD will continue to remain an important market in terms of value, with non-IT/ITeS sectors contributing to the office space demand here

Business District Analysis

For a better understanding of the city's office market, we have divided it into five business districts. Locations within each business district have been clubbed together, based on similar characteristics in terms of occupier profile, demand drivers, rent and distance from the city centre. The five business districts are CBD and off-CBD, SBD, SBD - OMR, PBD - OMR and GST, and PBD -Ambattur.

Business District	Location
Central Business District (CBD and off-CBD)	Anna Salai, RK Salai, Nungambakkam, Greams Road, Egmore, T. Nagar
Suburban Business District (SBD)	Mount-Poonamallee Road, Porur, Guindy, Nandanam
SBD-OMR	Perungudi, Taramani
Peripheral Business District (PBD) - OMR and GST	OMR beyond Perungudi Toll Plaza, GST Road
PBD - Ambattur	Ambattur

The CBD and off-CBD markets of Chennai comprise locations like Nungambakkam, Anna Salai, T. Nagar and RK Salai. This business district is most preferred by tenants owing to its central location, excellent road connectivity with prime residential areas and well-developed physical and social infrastructure. Occupiers - predominantly small and mid-size IT/ITeS companies and other services sectors – prefer office spaces in the 2,500–10,000 sq ft range. The continuous increase in the share of other services sectors from 15% in H1 2013 to more than 21% in H1 2014 benefitted the CBD and off-CBD business district.

Absorption in the CBD and off-CBD markets has increased during H1 2014, with their share jumping to 19% from 14% during same period in the previous year. Some of the key occupiers in these central office markets include companies such as KBR, which took up space in Prestige Polygon, and Equitas in Spencer Plaza, both located on Anna Salai.

The SBD of the city, offering quality office space as well as larger floor plates, is considered to be an ideal office destination. It is also the most sought after business district by occupiers due to its proximity to the city centre and easy access to the airport. The presence of excellent physical and social infrastructure has also attracted a healthy mix of occupiers from all sectors. The occupiers' preference can be gauged by the increase in the share of absorption of this market, which jumped to 30% in H1 2014 as against 21% in H1 2013.

Limited availability of large land parcels has led to exorbitant land costs in this business district, causing developers to consider residential development instead of office development. This has constricted the supply of new office spaces in this market. The new phenomenon of mixed-use development has been observed in this business district. However, the infusion of new office space through mixed-use development would not be substantial enough to cater for the entire demand. Manapakkam and Guindy are the two major markets primarily responsible for office absorption in the SBD market. During H1 2014, Tata Consultancy Services (TCS) and Delphi have taken up new offices in DLF IT Park.

The lack of larger floor plates and limited amenities in the CBD and off-CBD market fuelled the demand for the SBD market. This has helped the rental value to appreciate by 4%in this market during H1 2014, compared to H1 2013 and H2 2013. We expect the rental value in this

FIGURE 6
Business District-wise Absorption Split in H1 2013

Source: Knight Frank Research

FIGURE 7
Business District-wise Absorption Split in H1 2014

Source: Knight Frank Research

BUSINESS DISTRICTS OF CHENNAI

Key Takeaways

In H1 2014, the total office space stock in Chennai stood at 56.2 mn sq ft, while the occupied stock stood at 43.8 mn sq ft. Vacancy levels in the Chennai office market stood at 22% during this period

Better-than-expected absorption numbers of over 1.8 mn sq ft were reported during the first half of 2014, registering a growth of 47% from H1 2013

Going forward, we expect 2.23 mn sq ft of office space to be absorbed in the Chennai market during H2 2014, resulting in a 11% decline compared to H2 2013. However, on an annual basis for the year 2014, the total absorption is expected to touch 4.02 mn sq ft, thereby registering an increase of 8% from the 3.74 mn sq ft achieved during 2013

While we expect a total of 2.56 mn sq ft of new completions for the year 2014, H2 2014 alone will witness 1.07 mn sq ft of new completions

The city's vacancy level is projected to decrease to 20% in H2 2014, as compared to 22% in H1 2014

The CBD will continue to remain an important market in terms of value, with non-IT/ITeS sectors contributing to the office space demand here

Select Transaction in the Chennai Office Market

Building	Occupier	Location	Approx area (sq ft)
TRIL Infopark	AstraZeneca	Tharamani	110,000
Prestige Polygon	KBR	Mount Road	92,000
DLF IT Park	Tata Consulting Services	Mount Poonamallee Road	73,000
SP Infocity	athenahealth	Perungudi	68,000
SP Infocity	Ford	Perungudi	68,000
RMZ Millenia Business Park	Chrysler	Perungudi	66,764
Prince Infocity II	IBM	Perungudi	54,000
RMZ Millenia Business Park	Schawk	Perungudi	42,000
The Futura	Scope International	Sholinganallur	40,000
Prince Infocity II	Atmel	Perungudi	38,000
Spencer Plaza	Equitas	Anna Salai	37,000
Prince Infocity II	Caliber Point	Perungudi	34,900
Chennai One	Prodapt	Thuraipakkam	33,000
TRIL Infopark	Ascendant Technologies	Tharamani	30,000

Source: Knight Frank Research

business district to continue its growth trajectory, as there is restricted new supply.

We classified the pre-toll region, encompassing Taramani and Perungudi, as the SBD - OMR business district. Over the last decade, this market has evolved as a much-preferred office destination by the IT/ITeS sector. Proximity to the city centre, easy access to the airport, the availability of good quality office buildings, affordable rents and well developed social infrastructure are some of the reasons that have led to the SBD - OMR attracting major IT/ITeS occupiers. This is substantiated by the fact that the region accounted for a remarkable share of 44% of the office space absorption in H1 2014. Prominent IT parks such as TRIL, Prince Infocity, Ascendas IT Park and SP Infocity have been instrumental in garnering absorption in the SBD - OMR region. Some of the key tenants that took up office space in this business district during H1 2014 include AstraZeneca and Ascendant Technologies in TRIL IT Park, and athenahealth and Ford in SP Infocity.

SBD - OMR's strategic location and the IT/ITeS occupiers' interest has helped the rental value to appreciate by 7% and 1% during H1 2014, compared to H1 2013 and H2 2013 respectively. The existing rentals in this business district are quoted in the range of ₹ 45–58/sq ft/month.

The post-toll OMR stretch and GST Road make up the PBD - OMR and GST Road business district. Bigger floor plates offered at competitive rentals attracted large IT/ITeS companies that require large office spaces. Many off-shore companies, including BPOs and KPOs that do not have direct customer interaction, preferred relocating to this market. ELCOT SEZ at Sholinganallur, SIPCOT at Siruseri and Mahindra World City at Singaperumalkoil are the major office hubs in this market. However, distance from the city centre, lack of social infrastructure and traffic bottlenecks continue to plague this business district. Additional costs involved in installing electricity backups and organising transport facilities for employees have caused companies to move away from PBD - OMR and GST Road. This can be substantiated by the decline in the share of office space absorption of this

Business District-wise Rental Movement

Business District	Rental Value Range in H1 2014 (₹/sq ft /month)	12-month change	6-month change
CBD and off-CBD	65–70	1%	11%
PBD - OMR and GST	22–35	0%	2%
SBD	45–58	4%	4%
PBD - Ambattur	18–29	5%	2%
SBD-OMR	45–58	7%	1%

Source: Knight Frank Research

region, which stands at 7% in H1 2014 as against 12% in H1 2013. Some of the notable occupiers in the region include Aricent in ASV Chandilya Prodapt in Chennai One and Scope International in Futura

PBD –Ambattur, on the other hand, has not seen much activity in H1 2014. Factors such as distance from the city centre and the airport, as well as competition from other office markets like the OMR and GST Road, which offer similar rentals, have caused occupiers to overlook this business district. Besides, it is a much smaller office market compared to the other markets of Chennai, with only a handful of quality office projects catering largely to small and mid-size IT/ITeS companies and other services sector industries. PBD - Ambattur's share in absorption has declined sharply from 2% in H1 2013 to less than 1% in H1 2014. The existing rentals in this business district are quoted in the range of ₹ 18–29/sq ft/month.

Absorption grew by almost 50% in H1 2014 on the back of improved sentiments that brought the demand for office space back in the Chennai market. Based on this, we expect the IT/ITeS sector to continue to drive demand, and the Small and Medium Enterprises (SME) sector, with requirements of smaller office spaces, to show increased activity, providing an opportunity for developers to tap this demand. The manufacturing and other services sectors, including consulting, telecom and eCommerce industries are expected to gain momentum in the forthcoming year.

The CBD will continue to remain an important market in terms of value, with non-IT/ITeS sectors contributing to the office space demand here. On the rental front, the values are expected to remain stable in most micro-markets, although marginal appreciation is envisaged in projects witnessing occupier interest.

Going forward, we believe that the maximum absorption will happen in the SBD - OMR business district. Office projects in Mount Poonamallee Road, Taramani and Perungudi within this area will garner traction due to the district's strategic location, the availability of good quality office buildings at affordable rents and well developed social infrastructure. Meanwhile, with the situation of considerable oversupply in the PBD - OMR and GST business district, transactions have almost dried up. We expect this business district to remain stagnant over next 12–15 months before witnessing any traction.

The commissioning of the Chennai Metro Rail Phase-I between Koyambedu and Alandur in H2 2014 will benefit the SBD business district the most. This will attract occupiers who require smaller office spaces closer to the CBD market. Guindy is poised to emerge as the best alternative to the CBD and off-CBD markets, as it offers quality office buildings with all the amenities, including parking space within the premises at reasonable rentals. PBD - OMR and GST Road will generate interest in occupiers having large floor plate requirements at lower rentals. The IT/ITeS sector will be the driving force for the office space demand here.

Key Takeaways

We expect maximum absorption will happen in the SBD - OMR business district. Office projects in Mount Poonamallee Road, Taramani and Perungudi within this area will garner traction due to the district's strategic location, the availability of good quality office buildings at affordable rents and well developed social infrastructure

The commissioning of the Chennai Metro Rail Phase-I between Koyambedu and Alandur in H2 2014 will benefit the SBD business district the most. This will attract occupiers who require smaller office spaces closer to the CBD market

Guindy is poised to emerge as the best alternative to the CBD and off-CBD markets, as it offers quality office buildings with all the amenities, including parking space within the premises at reasonable rentals

PBD - OMR and GST Road will generate interest in occupiers having large floor plate requirements at lower rentals

HYDERABAD

RESIDENTIAL MARKET

Metropolitan Region Analysis

2014 has been a landmark year for Hyderabad, as the prevailing political deadlock was finally broken and the state of Telangana was formed on 2 June 2014. The Hyderabad real estate market has been in the eye of this political storm that caused it to be left out of the broad-based recovery in residential prices all Indian markets experienced after the Global Financial Crisis. Telangana now shares the dubious distinction of being the joint capital of two states, along with Chandigarh. However, the welcome closure of the Telangana issue, coupled with the fact that Hyderabad is the most affordable residential market among the country's top seven cities of NCR, Mumbai, Bengaluru, Chennai, Pune and Kolkata, makes a convincing case for a significant and sustained increase in market traction.

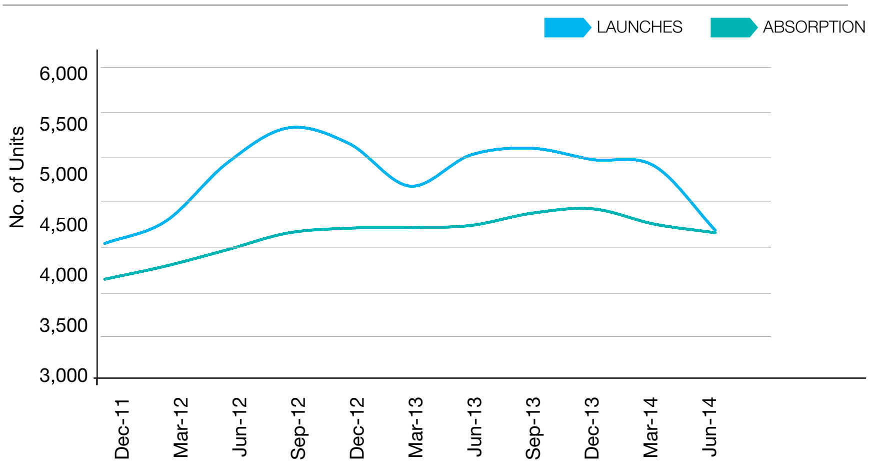
Market action on the ground, however, narrates a bleak story thus far. While the demand from homes dropped by over 4% in 2013, depressed absorption numbers in the first half of 2014 suggest a more pronounced fall this year. This can be attributed in no small measure to the fact that buyers who have roots in Andhra Pradesh have felt more secure investing in their home state rather than in Telangana. The aggressive political posturing by the now ruling party in Telangana also seems to have had a spillover effect on buyers belonging to other states that make up an estimated 70% of the demand base.

That being said, comparing absolute numbers of absorption and new launches on an annual basis is not sufficient to understand the health of a market or its impact on price. Since demand and supply are influenced by various other independent factors such as economic growth, market sentiment, interest rate and income growth, among others, an annual rise or fall in demand and supply could be misinterpreted as signs of a strong or weak market. Hence, with the aim of removing seasonality from the data, we have analysed the long-term (eight quarters) moving average trend of absorption and new launches.

The following chart depicts a story of steady absorption levels built on a

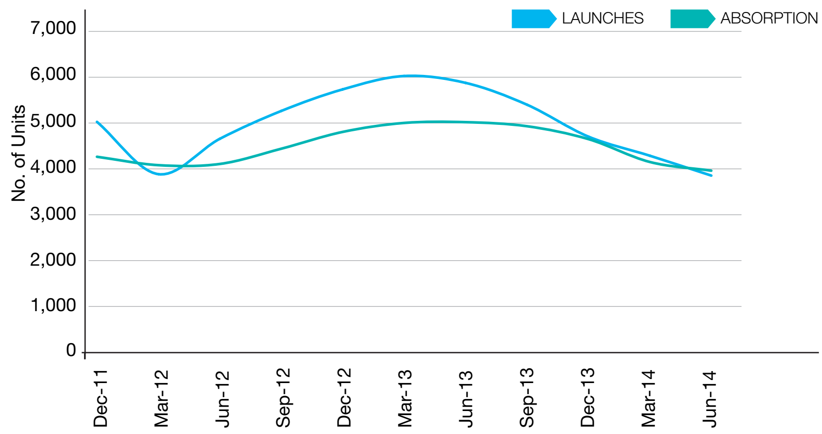
Residential sales volumes have plunged over 27% to 7,300 units during H1 2014, compared to the previous reference period. The alarming fall in demand during the first six months of 2014 show just how big an impact the final tumultuous months leading up to the effective formation of Telangana have had

FIGURE 1
Long Term (Eight Quarters) Moving Average Trend of Launches and Absorption



Source: Knight Frank Research

FIGURE 2
Short Term (Four Quarters) Moving Average Trend of Launches and Absorption



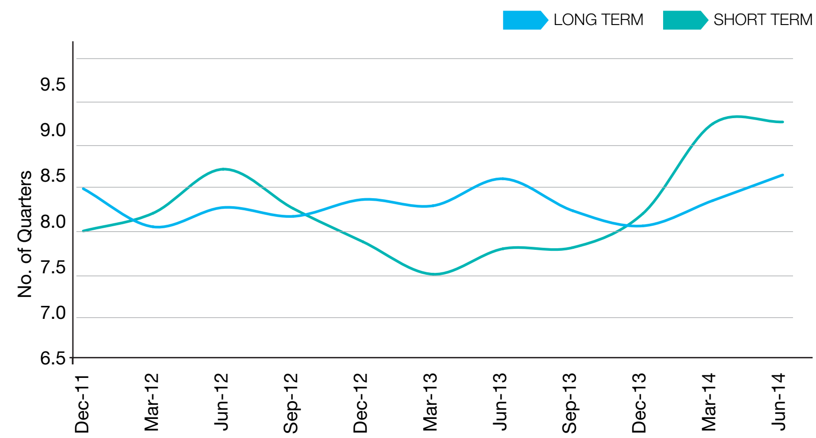
Source: Knight Frank Research

Notwithstanding the fact that the absorption numbers in H1 2014 have plummeted over 27% Y-o-Y, we believe that demand will pick up in the second half of the year as the festive season kicks in and the full effect of the easing out of the political and economic situation is felt

bedrock of discerning end users. The Hyderabad residential market is unique, as it is virtually bereft of an investors' community that participates actively at the project launch stage. This tends to keep absorption levels stagnant and range-bound as risk-averse end users take up ready-to-occupy units with little regard to launches. Thus, the current lull in the market is not alarming, as demand is expected to pick up in the months to come.

The fact that the drop in market traction is more pronounced since 2013 can be observed in the short-term moving average trend of launches and absorption, as well as the short and long term Quarters to Sell (QTS) analysis. As can be observed from the following chart, the four-quarter moving average of launches and absorption reached peak levels just after the end of 2012 and has been plummeting ever since. It is heartening to note that the rate of launches or supply has fallen more than absorption. This should see the demand-supply equation support price growth, going forward.

FIGURE 3
Quarters to Sell Analysis



Source: Knight Frank Research

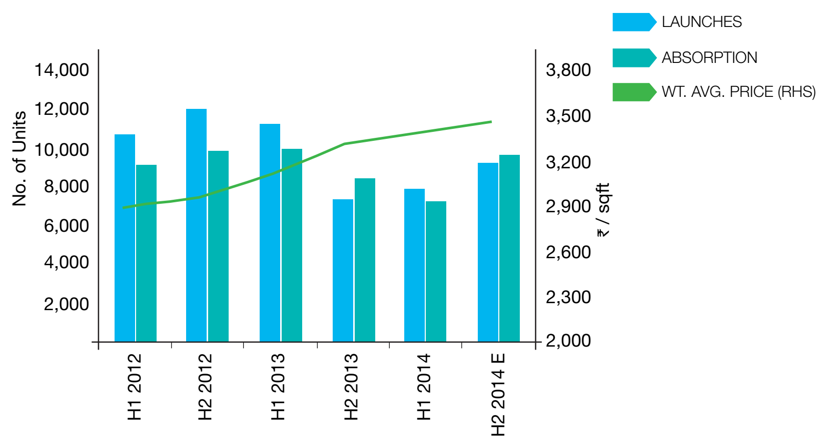
The QTS analysis refers to the number of quarters required to exhaust the existing unsold inventory in the city. While the eight-quarter trend ranges between 8–8.5 quarters, the short-term trend has crossed the nine-quarter level, further emphasising the drop in market traction.

We expect the on-going skittishness in the market to play itself out over the second half of 2014 as the election results, revival in economic activity, salary growth of IT/ITeS employees and the various sops announced in the Union Budget of 2014 make their weight felt on home buyer sentiment. Developers have already started seeing an increase in enquiries in June, which bodes well for the remainder of 2014. Hence, notwithstanding the fact that the absorption numbers in H1 2014 have plummeted over 27% Y-o-Y, we believe that demand will pick up in the second half of the year as the festive season kicks in and the full effect of the easing out of the political and economic situation is felt. We estimate that launches and absorption levels will increase by 25% and 15% in H2 2014 Y-o-Y respectively, and will end the year at a much more reasonable 8% deficit in terms of launches and absorption, compared to the previous year.

Nearly 18 months of decreasing market activity has had no discernable impact on the weighted average asking prices of available units, as developers have continued to up the ante by floating new offerings at higher prices, citing higher input costs and improved amenities. This has further discouraged the price-sensitive buyer segment from entering into the market. However, it is important to note that the developers have made a concerted effort to bring the ticket sizes of apartments down by reducing unit sizes. 75% of the units launched in H1 2014 were launched under the ticket size of ₹ 7.5 mn, compared to 58% in the preceding period of H2 2013.

In order to understand the market dynamics further, it is important to study the city in parts. The Hyderabad residential market can be classified broadly into five micro-markets, each of which has different characteristics, price points and buyer profiles.

FIGURE 4
Launches, Absorption and Price Trend



Source: Knight Frank Research

We estimate that launches and absorption levels will increase by 25% and 15% in H2 2014 Y-o-Y respectively, and will end the year at a much more reasonable 8% deficit in terms of launches and absorption, compared to the previous year

Micro-market Analysis

Micro-market	Location
HMR-Central	Begumpet, Banjara Hills, Jubilee Hills, Panjagutta, Somajiguda
HMR-West	Kukatpally, Madhapur, Kondapur, Gachibowli, Raidurgam
HMR-East	Uppal, Malkajgiri, L.B. Nagar
HMR-North	Kompally, Medchal, Alwal, Qutubullapur
HMR-South	Rajendra Nagar, Shamshabad

HMR refers to Hyderabad Metropolitan Region

The western zone, comprising locations like Kukatpally, Madhapur, Kondapur, Gachibowli, Miyapur, HITEC City and Gopannapalli, is the largest contributor to the residential supply in Hyderabad. It accounts for approximately 60% of the total units under construction. Demand in this region is end user-driven, the majority of which caters to the employees of IT firms in and around HITEC City and Gachibowli. The supply in this micro-market has seen a boost due to its proximity to workplaces, the upcoming retail development and supporting infrastructure in the form of connecting railway stations, the National Highway and Express Highway that connect to the airport. Development in this region is moving southwards, with developers showing interest in locations like Narsingi and Appa Junction. These locations

HYDERABAD METROPOLITAN REGION MAP

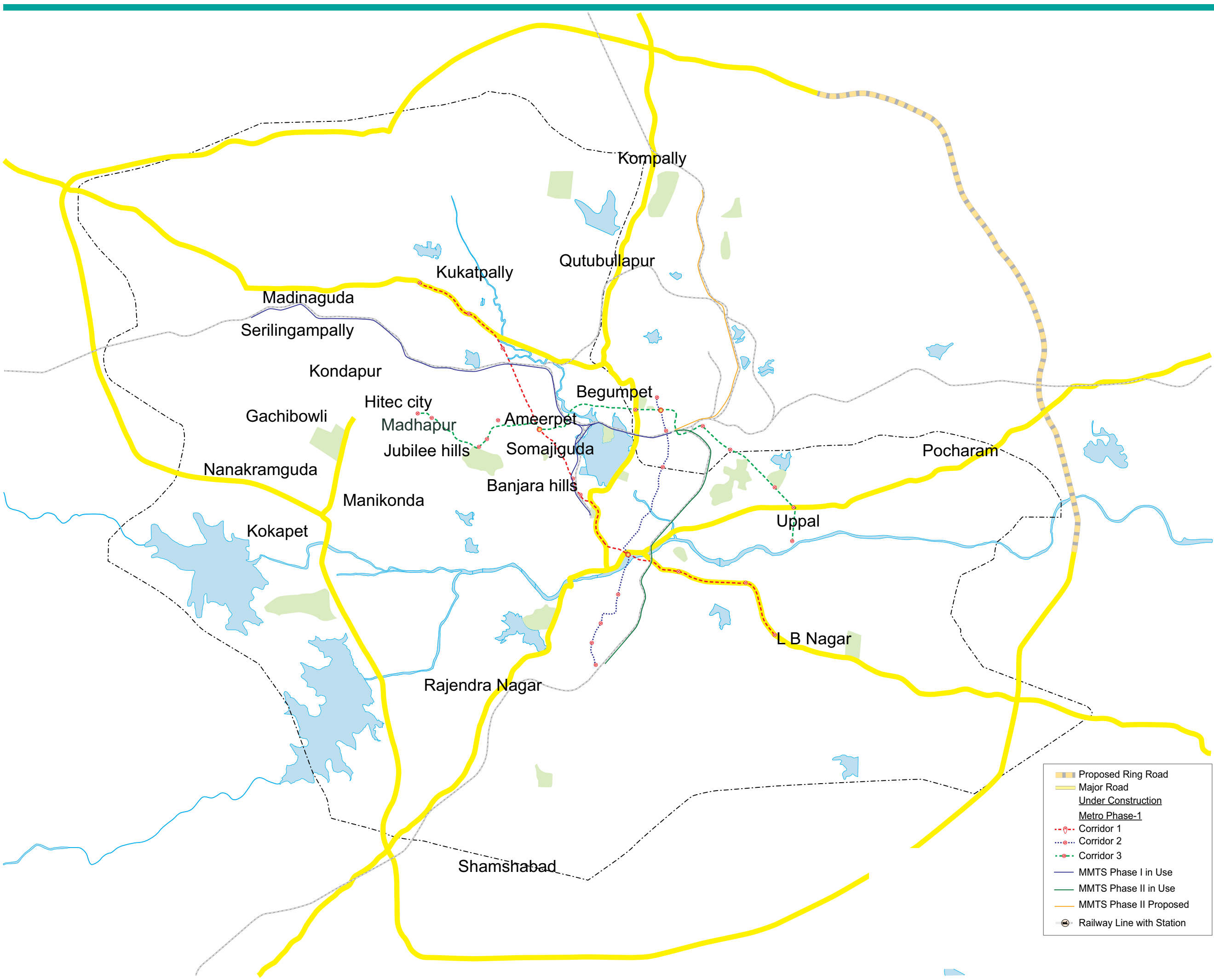
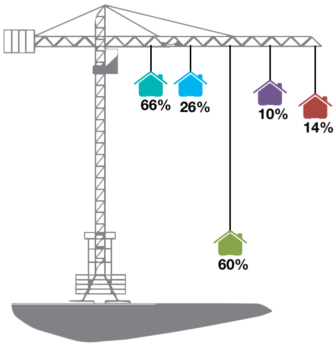


FIGURE 5
Micro-market split of under-construction units as on June 2014



- **8%** HMR CENTRAL
- **8%** HMR EAST
- **60%** HMR WEST
- **10%** HMR NORTH
- **14%** HMR SOUTH

Source: Knight Frank

are now perceived as the next growth corridors, and are expected to gain traction in the coming years.

Malakpet, Upparpally, Saidabad, Santosh Nagar, Rajendranagar and Shamshabad fall under the southern zone. With the development of the Rajiv Gandhi International Airport at Shamshabad, and other developments like SEZs, Hardware Park and Fab City, this zone has been growing as a residential location and has the second largest number of units under construction today. However, its distance from the city and lack of social infrastructure are still deterrents to demand, causing nearly 60% of its units to remain unsold at the end of H1 2014.

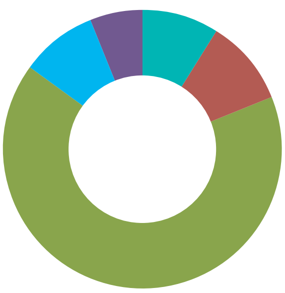
The northern zone is the third most preferred residential micro-market, and is driven due to good infrastructure facilities and proximity to the cantonment area. This region constitutes nearly 10% of the total under-construction units in the Hyderabad market. Most of the supply in the north zone has come up in Kompally, Qutubullapur, Nagpur Highway, Yarpal and Shamirpet.

The eastern zone comprises locations such as Uppal, Nacharam, Mallapur, Kapra, Cherlapalle, Pocharam, Kuntloor, Rampally and Ghatkesar. Nearly 8% of the total units under construction fall in this zone. Uppal remains one of the favoured destinations in this micro-market. Phase II of the ORR, which is under construction, will improve the traffic situation and connectivity in the eastern zone.

Residential demand in the central zone, comprising areas like Begumpet, Marredpally, Somajiguda, Himayatnagar,

Being the largest and most preferred micro-market in Hyderabad, the west zone has product offerings in all ticket sizes, be it affordable, mid-segment or high-end housing, making it a favourable residential destination for home buyers

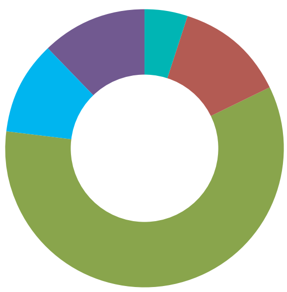
FIGURE 6
Micro-market split of launched units in H1 2013



- **9%** HMR CENTRAL
- **10%** HMR EAST
- **66%** HMR WEST
- **9%** HMR NORTH
- **6%** HMR SOUTH

Source: Knight Frank Research

FIGURE 7
Micro-market split of launched units in H1 2014

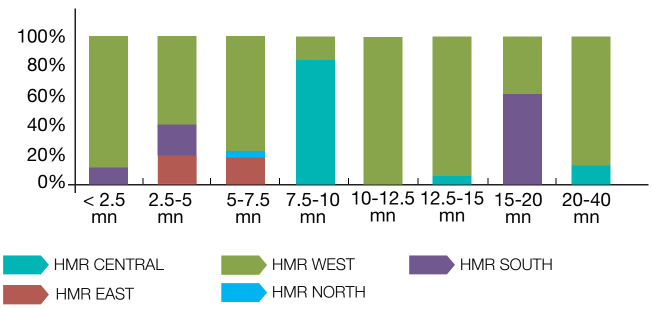


- **5%** HMR CENTRAL
- **13%** HMR EAST
- **59%** HMR WEST
- **11%** HMR NORTH
- **12%** HMR SOUTH

Source: Knight Frank Research

FIGURE 8

Micro-market Level Ticket Size Split of Launched Units During H1 2014



Source: Knight Frank Research

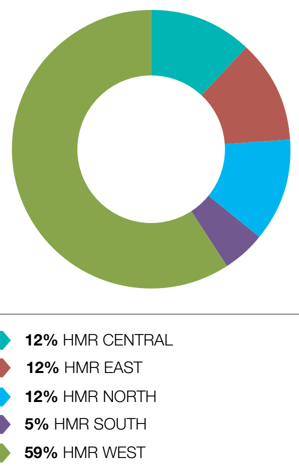
Chikkadpally, Banjara Hills and Jubilee Hills, is primarily driven by government officials, businessmen, corporate office employees and NRIs. These locations cater to higher income groups, as well as the upper middle income segment.

West Hyderabad has been contributing the largest share of new launches in the last five years, as its residential appeal has been increasing with time. However, its share has dropped since H1 2013, as the overall number of unit launches in the market has shrunk by 30% in H1 2014, and the other micro-markets did not experience a significant drop in the absolute number of units launched. A total of 4,700 residential units were launched in this micro-market during H1 2014, constituting 59% of the new launches. Developers have started exploring locations like Gopanpally, Chanda Nagar and Miyapur, further west of Gachibowli, where it is possible to offer comparatively lower-priced apartments to the cost-conscious buyer. Gachibowli, Kukatpally and Manikonda continue to remain preferred locations for fresh development within this zone. These locations cater to the demand from the IT/ITeS sector, wherein employees prefer

We estimate that launches and absorption levels will increase by 25% and 15% in H2 2014 Y-o-Y respectively, and will end the year at a much more reasonable 8% deficit in terms of launches and absorption, compared to the previous year

FIGURE 9

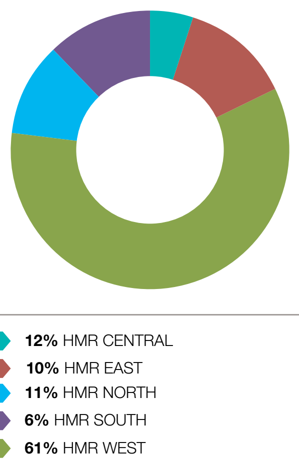
Micro-market split of absorption in H1 2013



Source: Knight Frank Research

FIGURE 10

Micro-market split of absorption in H1 2014



Source: Knight Frank Research

to buy a house instead of renting an apartment. Being the largest and most preferred micro-market in Hyderabad, the west zone has product offerings in all ticket sizes, be it affordable, mid-segment or high-end housing, making it a favourable residential destination for home buyers.

East Hyderabad's share in the new launches has also shown improvement in H1 2014. This region has a lot of potential to grow further, as land prices are still low compared to other developed parts of the city, despite the run-up in prices since 2012. Once Phase II of the ORR is operational, the connectivity issue will also be resolved. The majority of the launches took place in Nagole, Pocharam, Shamirpet and Uppal in the price range of ₹ 2,000–2,600 per sq ft Green Terraces, launched by Mahanagar Homes in Nagole, and Serene Hills County by Avani Infra Developers were among the prominent projects launched in H1 2014.

North Hyderabad's share in the overall number of new launches has shown improvement in H1 2014. Medchal Alwal and Kompally continue to feature prominently in this micro-market in terms of project launches. Kompally is predominantly witnessing the development of villa projects in the price range of ₹ 5–10.25 mn/unit. Alwal, on the other hand, has a number of stand-alone projects in the price range of ₹ 2,500–2,800 per sq ft.

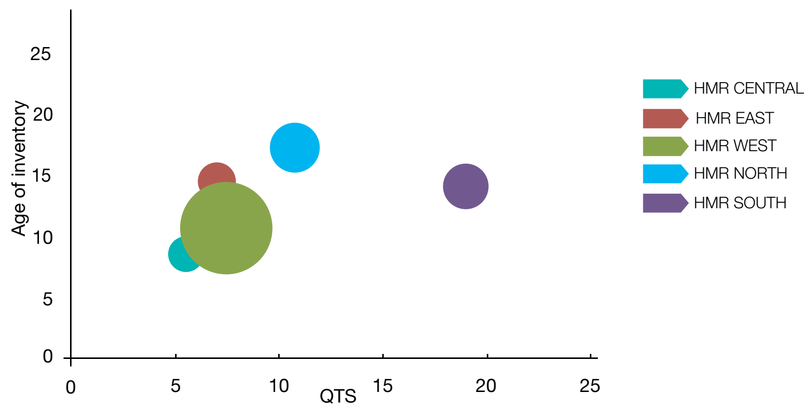
South and Central Hyderabad have had contrasting fortunes in H1 2014, clearly depicting the surge in apartment launches in lower ticket sizes. Abundant land parcels and low prices of apartments in the South Hyderabad micro-market have encouraged development activity in this region, while the converse is true in Central Hyderabad. South Hyderabad has also seen a lot of villa development activity in recent years – Tranquillas by Ramky Real Estates was among the more prominent villa projects launched during H1 2014. Central Hyderabad should see increased traction once the market picks up momentum again and developers look to enter into joint ventures with bungalow plot owners wanting to cash in on the uptrend.

Residential sales volumes have plunged over 27% to 7,300 units during H1 2014, compared to the previous reference period. The year 2013 had also seen a slight drop in sales volume, but the alarming fall in demand during the first six months of 2014 show just how big an impact the final tumultuous months leading up to the effective formation of Telangana have had.

East and Central Hyderabad experienced the steepest decline in absorption

In spite of the fact that the absorption levels were 25% less than those recorded in H1 2013, West Hyderabad still fared better than the overall Hyderabad residential market. Nearly 4,500 residential units were absorbed in this micro-market during H1 2014 and most of the buyers' interest was observed to be in the ₹ 2.5–7.5 mn ticket size range

FIGURE 11
QTS vs. Age of Inventory across Micro-Markets



Note: The size of the bubble indicates the quantum of unsold inventory
Source: Knight Frank Research

The Hyderabad residential market could well be at a turning point in its evolution, and could see the price discount that it has, as compared to other frontline IT/ITeS-driven cities like Bengaluru, Pune and Chennai, diminish progressively in the coming years. We expect that a revival in demand in H2 2014 should sustain the current period's growth rate of 2.2%

numbers, at 39% and 29% respectively, while the demand in the other micro-markets did not decline as much as the overall market. The health of the residential market in East Hyderabad hinges largely on the completion of the ORR and the proposed and under-construction metro lines ending at Nagole and L.B. Nagar. Political insecurity, the likes of which Hyderabad has seen, invariably puts the best laid development plans under a cloud of uncertainty and has a direct impact on the real estate market. East Hyderabad was the biggest casualty during the first six months of 2014, but should see a recovery in market traction in H2 2014.

The western micro-market has shown the highest absorption in terms of volume, which can be attributed to the variety and volume of inventory available in this market. In spite of the fact that the absorption levels were 25% less than those recorded in H1 2013, West Hyderabad still fared better than the overall Hyderabad residential market. Nearly 4,500 residential units were absorbed in this micro-market during H1 2014 and most of the buyers' interest was observed to be in the ₹ 2.5–7.5 mn ticket size range, which, incidentally, also constitutes over two-third of the under-construction inventory in this micro-market.

Comparing these micro-markets in terms of the number of launches and absorption does not show the complete picture regarding the health of the market or the impact on prices. Hence, we have developed a model that captures the relative health of a micro-market by taking into account the impact of demand, supply and the age of unsold inventory. The age of unsold inventory is the number of quarters that have passed since the inventory entered into the market. A higher age of unsold inventory indicates that a large number of old projects continue to remain unsold. Currently, based on the average sales velocity, the overall Hyderabad market holds approximately 8.5 quarters of unsold inventory at an average age of 12.4 quarters.

The relative health of each micro-market in Hyderabad can be inferred from the adjoining chart. For example, Central Hyderabad has approximately the same amount of under-construction inventory as East Hyderabad, but as seen from the chart, it can be concluded that it is the healthier of the two micro-markets because it has a lower average age of inventory and QTS as well.

Central Hyderabad is the healthiest micro-market in the city, while North Hyderabad carries the oldest inventory. South Hyderabad has the lowest sales velocity, and will thus take the most time to liquidate the current inventory. Even though West Hyderabad has the most unsold inventory in the market by far, it is second only to Central Hyderabad in terms of market health, as its average sales velocity is sufficient to liquidate the current unsold inventory in 7.5 quarters even in this depressed market.

Steady absorption levels and already low prices in the Hyderabad residential market have ensured a steady growth in prices over the last two years. Growing at a compounded annual growth rate of 4.9% since 2010, the Hyderabad market has underperformed significantly as compared to other IT/ITeS sector-driven markets; yet, it is the most affordable by far. However, the last year saw some volatility, with price growth in most-micro markets falling by the end of 2013 and then trending up again in the following six months. The weighted average asking prices in the Hyderabad market grew by approximately 2.2% in H1 2014, compared to H2 2013. The central and western micro-markets showed the most appreciation, growing by 2.9% each, while the other micro-markets grew between 1% and 2% respectively.

The established residential locations in the central and western micro-markets saw above-average price appreciation even as absorption levels dropped in 2014. Restricted supply, better

Price movement in select locations

Location	Micro-market	Price range in H1 2014 (₹ /sq ft)	Change since H1 2013*	Change since H2 2013*
Begumpet	Central	4,500– 5,800	3%	8%
Banjara Hills	Central	7,000–9,000	8%	3%
Jubilee Hills	Central	4,500–6,200	2%	-1%
Madhapur	Central	5,800–7,800	5%	3%
Uppal	East	2,600–2,800	5%	3%
L. B. Nagar	East	2,400–2,900	4%	2%
Nacharam	East	2,200–2,800	-1%	-5%
Kompally	North	2,200–3,100	6%	8%
Quthbullapur	North	2,100–2,600	3%	6%
Shamirpet	North	2,000–2,400	-1%	3%
Shamshabad	South	2,300–3,000	7%	-2%
Bandlaguda	South	2,200–3,100	-2%	4%
Rajendra Nagar	South	2,100-3,100	2%	1%
Kondapur	West	4,000 - 5,200	2%	8%
Gachibowli	West	3,800 - 4,500	4%	7%
Manikonda	West	3,400 - 4,500	5%	3%
Kukatpally	West	2,800 - 3,900	4%	3%
Madeenaguda	West	2,600 - 3,100	2%	4%

* Change in weighted average prices

Source: Knight Frank Research

infrastructure and high aspirational quotient attached to Central Hyderabad will continue to push prices upward in the various locations of this micro-market, despite sluggish demand. Banjara Hills showed maximum appreciation, while the price growth in Jubilee Hills was more subdued. While the price growth in central locations was more concentrated, the western zone saw prices appreciate across all locations and Kondapur and Gachibowli appreciated the most, by 8% and 7% respectively.

The Hyderabad residential market could well be at a turning point in its evolution, and could see the price discount that it has, as compared to other frontline IT/ITeS-driven cities like Bengaluru, Pune and Chennai, diminish progressively in the coming years. We expect that a revival in demand in H2 2014 should sustain the current period's growth rate of 2.2%.

Key Takeaways

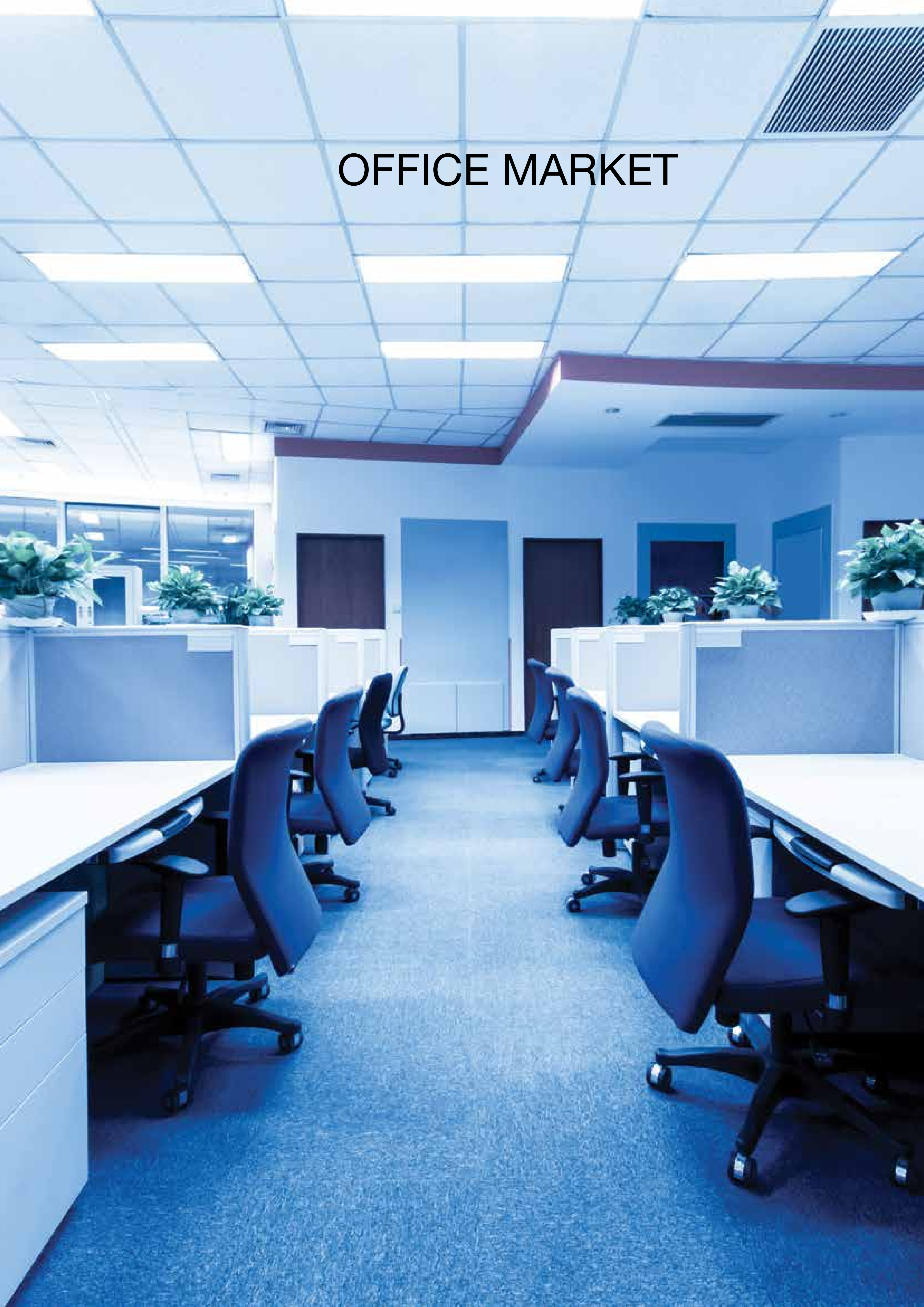
Residential sales volumes have plunged over 27% to 7,300 units during H1 2014, compared to the previous reference period. The year 2013 had also seen a slight drop in sales volume, but the alarming fall in demand during the first six months of 2014 show just how big an impact the final tumultuous months leading up to the effective formation of Telangana have had

Notwithstanding the steep drop in absorption numbers during H1 2014, we believe that demand will pick up in the second half of the year as the festive season kicks in and the full effect of the easing out of the political and economic situation is felt

We estimate that launches and absorption levels will increase by 25% and 15% in H2 2014 Y-o-Y respectively and end the year at a much more reasonable 8% deficit in terms of launches and absorption, compared to the previous year

The Hyderabad residential market could well be at a turning point in its evolution, and could see the price discount that it has, as compared to other frontline IT/ITeS-driven cities like Bengaluru, Pune and Chennai, diminish progressively in the coming years. We expect that a revival in demand in H2 2014 should sustain the current period's growth rate of 2.2%

OFFICE MARKET



Metropolitan Region Analysis

Hyderabad is the administrative, financial and economic capital of Andhra Pradesh and the newly-formed state of Telangana. This city, whose commercial landscape was predominantly made up of engineering-based industries and trading companies, has seen a dramatic change over the last few decades. With the Internet boom, global IT/ITeS leaders like Google, IBM, CA, HP, GE and Convergys set up offices in Hyderabad, thus emphasising the large-scale development of infrastructure facilities and the rapid growth of contiguous locations surrounding the HITEC City area, which is at the centre of the IT boom in Hyderabad.

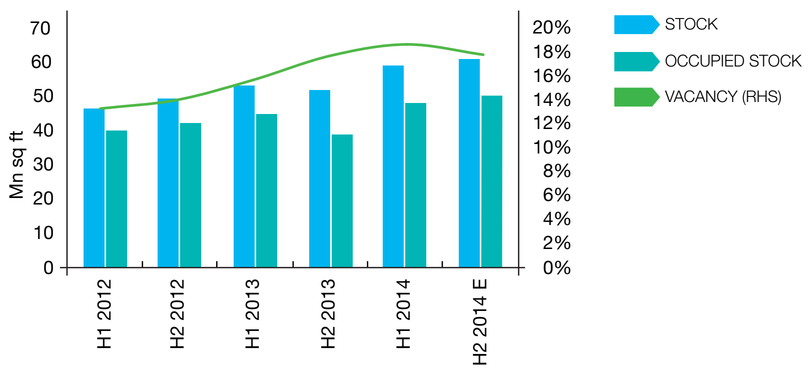
Despite having all the elements that would enable the growth of a vibrant office market, Hyderabad has been lagging behind other IT/ITeS sector-driven markets. The political uncertainty caused by the Telangana issue had effectively discouraged long-term capital from entering the city. The formation of the state of Telangana on 2 June 2014 has put this long-standing issue to rest and set the stage for Hyderabad to take its place alongside frontline IT/ITeS sector-driven markets like Bengaluru. We believe that H1 2014 marks an inflection point in the evolution of the Hyderabad office market, and that the effect of the political situation easing out, along with improving macroeconomic indicators, will see sustained growth in demand, going forward.

The Hyderabad office market currently has an office stock of approximately 59 mn sq ft, and has been experiencing steadily-increasing vacancy levels since 2012. Symptomatic of an ailing office market, the vacancy rate has increased from 13% in H1 2012 to nearly 19% in H1 2014.

The annual absorption numbers have been declining over the past four years, and if the H1 2014 numbers are anything to go by, this trend should continue in the current year as well. Down 25% YoY, the absorption levels, at 1.94 mn sq ft in H1 2014, paint a bleak picture about the year ahead. However, the massive change in market dynamics due to the closure of the Telangana issue leads us to believe that absorption numbers in the second half of the year will be high enough to ensure that 2014 sees a total of approximately 4.2 mn sq ft of space transacted, exceeding the previous year's tally by 12%.

Approximately 3 mn sq ft of office space came online in H1 2014, and

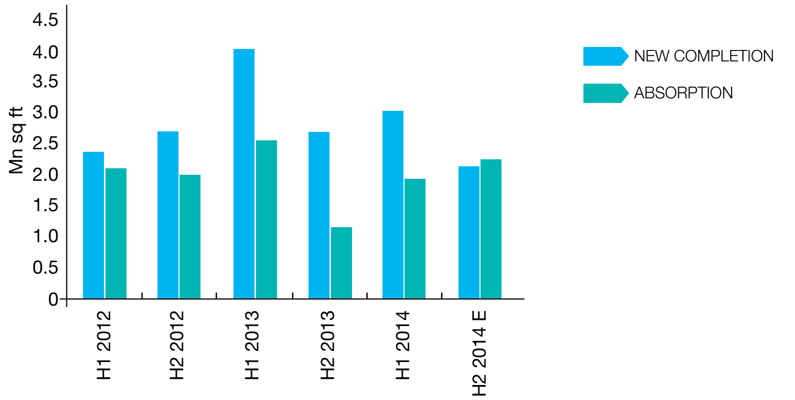
FIGURE 1
Office Space Stock and Vacancy



Source: Knight Frank Research

We believe that H1 2014 marks an inflection point in the evolution of the Hyderabad office market, and that the effect of the political situation easing out, along with improving macroeconomic indicators, will see sustained growth in demand, going forward

FIGURE 2
New Completion and Absorption



Source: Knight Frank Research

an additional 2.2 mn sq ft is expected to achieve completion in the following period. This annual tally of 5.2 mn sq ft is approximately 23% less than the area delivered in the previous year. This reduced supply, coupled with the expected increase in demand, should effectively pull down the vacancy rate to an estimated 18% by the end of 2014.

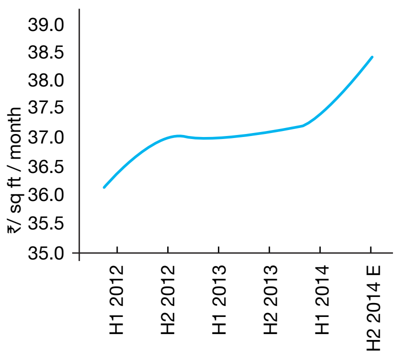
The weighted average rental levels in the Hyderabad office market have stagnated between ₹ 36–37.5/sq ft/month during the analysis period, and have grown marginally by 1% YoY in H1 2014. Currently estimated at ₹ 37.5/sq ft/month, these low rentals reiterate that Hyderabad is the probably the most affordable office market in India today. With the promise of increased market traction and the demand-supply equation poised to promote rental growth, the second half of the year is expected to see rental levels reach approximately ₹ 38.5/sq ft/month – a 2.7% increase over the previous year.

The IT/ITeS sector has been the primary driver of the office space market in Hyderabad, and accounted for approximately 1 mn sq ft of absorption in H1 2014. This sector forms the backbone of the Hyderabad office space market, and consistently takes up the lion's share of the transactions pie. The fact that its share has been falling does not bode well for the market, but other services sector companies have made up for the deficit amply. IT/ITeS sector companies like Pegasystems, Google and IBM were among the companies that took up large format office spaces during H1 2014. A 0.18-mn-sq-ft lease in Raheja Mindspace at HITEC City inked by IT/ITeS major Pegasystems was the largest transaction by an IT/ITeS sector company during this period.

The market share of other services sector-companies has shown prolific growth during the analysis period, as healthcare, eCommerce and consulting companies have consolidated and expanded their commercial footprint in Hyderabad in a big way. Healthcare companies were especially active during H1 2014, with UnitedHealth Group and

IT/ITeS sector companies like Pegasystems, Google and IBM were among the companies that took up large format office spaces during H1 2014. A 0.18-mn-sq-ft lease in Raheja Mindspace at HITEC City inked by IT/ITeS major Pegasystems was the largest transaction by an IT/ITeS sector company during this period

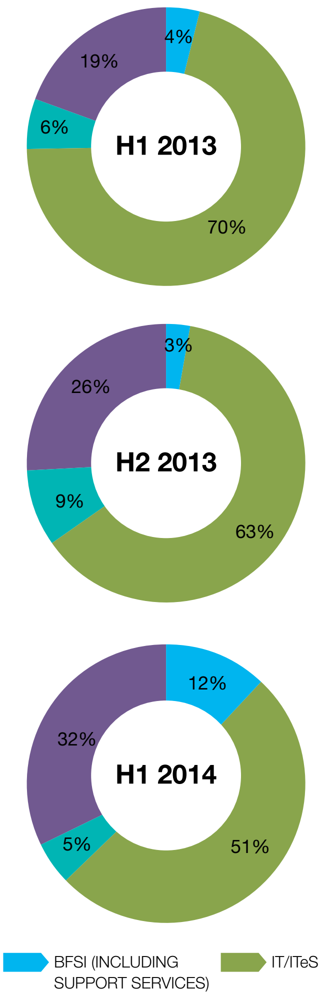
FIGURE 3
Weighted Average Rental Movement (₹/sq ft/month)



Source: Knight Frank Research

Sunshine Hospitals taking up 0.25 and 0.18 mn sq ft, respectively, in HITEC City. Accenture and Mindtree were among the prominent consulting companies active during this period.

FIGURE 4
Sector-wise Absorption Split



Source: Knight Frank Research

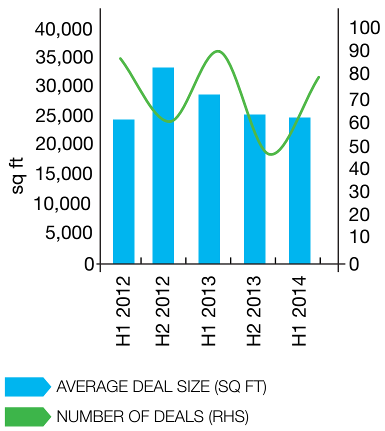
BFSI sector companies tripled their market share in H1 2014 compared to the previous reference period. This can be attributed largely to two large deals signed by the Karvy Group and HSBC, which constituted almost 90% of the total transacted volume. The manufacturing sector maintained its market share in H1 2014 and could see its share increasing in times to come, as the recently-announced intention of the government to implement an industrial and investment policy encourages investments by the companies belonging to this sector.

The average size of deals in the Hyderabad office market has declined continuously since 2012, as the share in transactions of the IT/ITeS sector has been reducing. An analysis of the number of transacted deals provides a measure of market traction and reflects the liquidity and depth of the market. The Hyderabad market averages 65–75 transactions in every six-month period, and the number of transactions seems to peak in the first half of every year. A better-than-average number of transactions enables more efficient price discovery and helps support rental levels. This is largely because occupiers in lower-size ranges are in a relatively weaker negotiating position compared to their larger counterparts. The number of transactions in the Hyderabad office market has dropped over 12% YoY in H1 2014, but still shows a marked improvement over the preceding period. Consequently, even as YoY rental growth has largely been flat, most of the growth has taken place in the first six months of 2014. The average office space rentals in the city grew by 1% YoY in H1 2014 and 0.8% from the preceding period.

Phase I of the Hyderabad Metro Rail and the Outer Ring Road (ORR) are two major infrastructure projects that will impact the real estate landscape in the city in the next two years. Phase I of the metro project is scheduled for completion by H2 2017. However, of the six stages that this project is divided into, three are scheduled for completion by H2 2015. The three stages of Nagole to Mettuguda, Miyapur to SR Nagar, and Jubilee Bus Station to Falaknuma that are set to become operational by the end of next year will efficiently connect the eastern, northern and southern extremities of Hyderabad to CBD and off-CBD locations. Additionally, the Shamirpet–Pedda Amberpet stretch of the ORR in the east is expected to become operational in H2 2014, completing the ORR and providing complete radial connectivity in the city. This improvement in connectivity, coupled with the recent announcement of a Hyderabad–Warangal industrial corridor passing through East Hyderabad, will enhance the prospects of real estate development immensely in that area.

Besides these infrastructure initiatives, the Telangana government has also undertaken to put into effect an industrial and investment policy that will be benchmarked alongside those in leading economies like Singapore. These initiatives will go a long way in attracting investments and nurturing the growth of a robust office market.

FIGURE 5
Deal Size Analysis



Source: Knight Frank Research

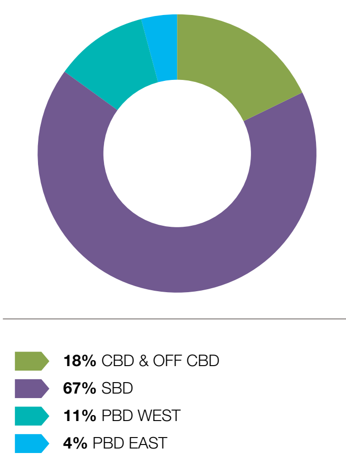
Business District Analysis

The Hyderabad office market is classified into different business districts. Locations like Begumpet, Ameerpet, Somajiguda, Banjara Hills and Jubilee Hills form the CBD and off-CBD office markets. Other key locations like Madhapur, Kondapur and HITEC City form the suburban business district (SBD) and primarily comprise the IT/ITeS strength of the region. Gachibowli, another key IT/ITeS hub, forms a part of the Peripheral Business District - West (PBD W) micro-market. Locations like Uppal and Pocharam towards the east, which have the lowest rents in Hyderabad, constitute the Peripheral Business District – East (PBD E) micro-market. Extensive infrastructure developments like the ORR and radial roads have led to further office space development in peripheral locations like Shamshabad, Pocharam and other HMDA localities.

Business District	Location
CBD and off-CBD	Banjara Hills, Jubilee Hills, Begumpet, Ameerpet, Somajiguda, Himayatnagar, Raj Bhavan Road, Punjagutta
SBD	HITEC City, Kondapur, Madhapur, Manikonda, Kukatpally, Raidurgam
PBD - West	Gachibowli, Kokapet, Madinaguda, Nanakramguda, Serilingampally
PBD - East	Uppal, Pocharam

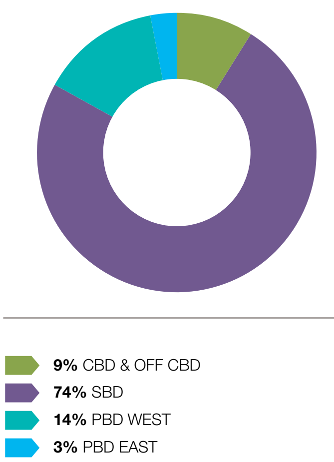
The SBD accounts for well over half of the office stock in Hyderabad and easily dominates the absorption pie, as it is by far the most preferred business district in Hyderabad. The office stock in this business district is built to suit the requirements of the dominant IT/ITeS sector, and is well connected to the city's residential hubs via road and rail. Office occupiers have shown a marked preference toward SBD locations, as its share of transactions has jumped from 67% in H1 2013 to 74 % in H1 2014. IT/ITeS and other services sector companies accounted for over 92% of the space taken up in this business district. It is notable that nearly 87% of the space taken up by other services sector companies during H1 2014 was transacted in this area. This is largely due to the fact that even front offices of consulting and legal firms are slowly moving west. The top three largest transactions during H1 2014 took place in the SBD and accounted for over 40% of the 1.46 mn sq ft transacted there. HITEC City alone accounted for over 70% of the space transacted in this business district. Raidurgam, Madhapur and Kondapur also saw significant market activity during H1 2014, while DivyaSree Orion in Raidurgam attracted big ticket occupiers like IBM, Accenture and Mindtree. Strong absorption numbers enabled this business district to achieve a rental growth of 1.5% YoY in H1 2014 and 1% compared to the preceding period.

FIGURE 6
Business District-wise Absorption Split in H1 2013



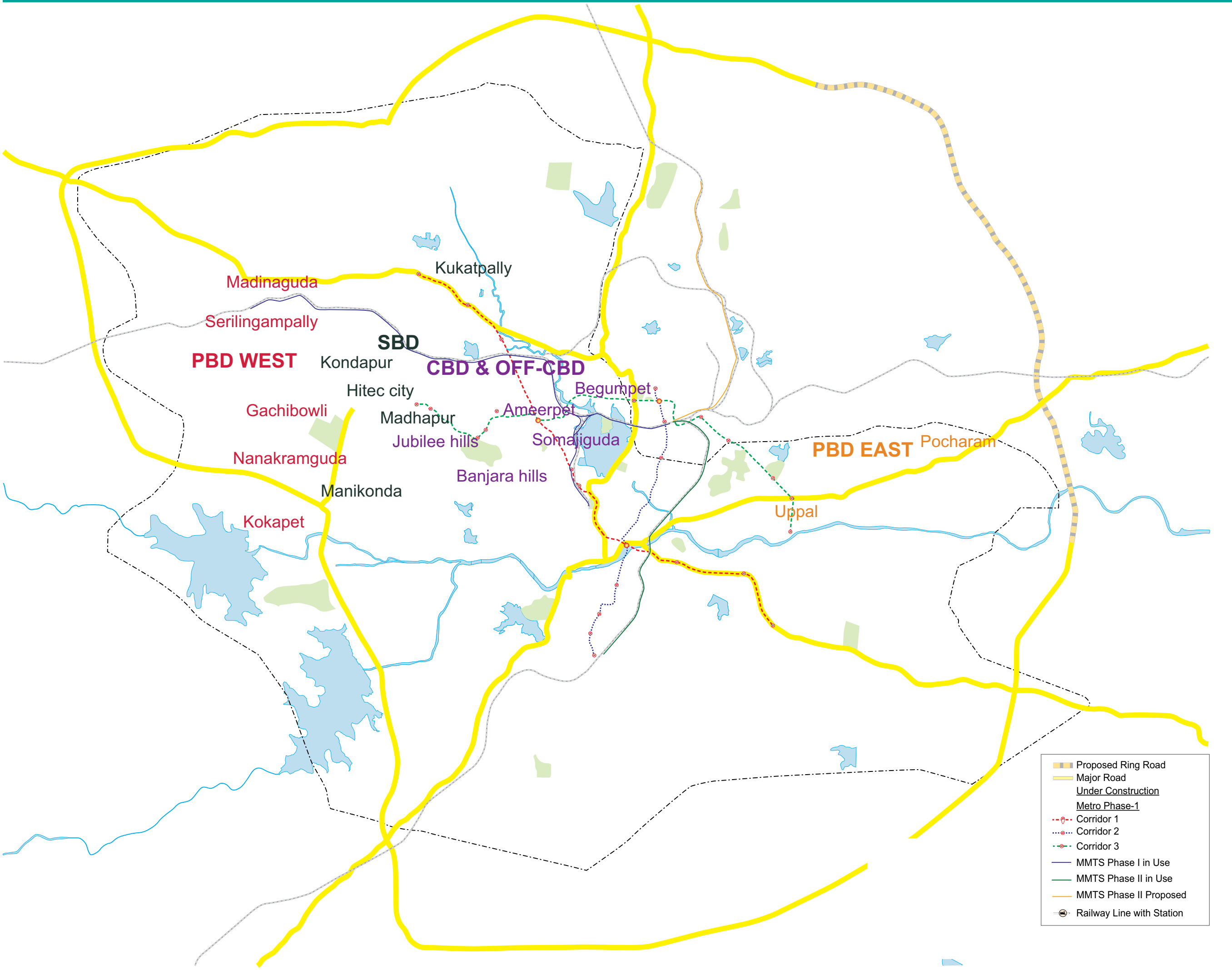
Source: Knight Frank Research

FIGURE 7
Business District-wise Absorption Split in H1 2014



Source: Knight Frank Research

BUSINESS DISTRICTS OF HYDERABAD



Select Transactions in the Hyderabad Office Market

Building	Occupier	Location	Approx. Area (sq ft)
Raheja SEZ 12 B	UnitedHealth Group	HITEC City	250,000
Raheja Mindspace	Pegasystems	HITEC City	183,000
Divyasree Omega	Google	HITEC City	180,000
Ramky	Karvy	Nanakramguda	140,000
TSI	Antheleo	Nanakramguda	25,000
DLF	Genpact	Gachiboli	21,000
Sarvotham Building	B/E Aerospace	Jubilee Hills	49,088
Cyber Spazio	USM Business Systems	Banjara Hills	18,536
White House	WizIQ	Begumpet	7,000
NSL Arena	GVK Biosciences	Uppal	30,000
TSI	Sunera Technologies	Uppal	20,000

Source: Knight Frank Research

Key Takeaways

Down 25% YoY, the absorption levels in H1 2014, at 1.94 mn sq ft, paint a bleak picture about the year ahead

The massive change in market dynamics due to the closure of the Telangana issue leads us to believe that absorption numbers in the second half of the year will be high enough to ensure that 2014 sees a total of approximately 4.2 mn sq ft of space transacted, exceeding the previous year's tally by 12%

With the promise of increased market traction and the demand-supply equation poised to promote rental growth, the second half of the year is expected to see rental levels reach approximately ₹ 38.5/sq ft/month – a 2.7% increase over the previous year

We believe that H1 2014 marks an inflection point in the evolution of the Hyderabad office market, and the effect of the political situation easing out, along with improving macroeconomic indicators, will see sustained growth in demand, going forward

The fact that the IT/ITeS sector share has been falling consistently since H1 2013 does not bode well for the market, but other services sector companies have made up for the deficit

IT/ITeS sector companies such as Pegasystems, Google and IBM were among the companies that took up large format office spaces during H1 2014. A 0.18-mn-sq-ft lease in Raheja Mindspace at HITEC City inked by IT/ITeS major Pegasystems was the largest transaction by an IT/ITeS sector company during this period

The PBD - West business district of Hyderabad lies further west of the SBD and is fast gaining prominence, as it offers significant price arbitrage and a greater choice to the office occupier without compromising on overall project quality. It is the second largest business district of the city, and the only other zone besides the SBD to experience a YoY increase in the market share of the transacted area. It claimed approximately 0.26 mn sq ft of the space absorbed during H1 2014. The IT/ITeS sector usually takes up the bulk of the space transacted in this business district, but H1 2014 saw the BFSI sector account for over half of the space transacted here, thanks to a 0.14 mn sq ft lease inked by the Karvy Group at Nanakramaguda. The IT/ITeS and other services sector companies accounted for 31% and 16% of the area transacted in this business district. Practically all of the space transacted in this business district was accounted for by Nanakramguda and Gachibowli, and properties owned by DLF and Ramky featured prominently during H1 2014. Rentals grew by a marginal 1% YoY during H1 2014 due to significant vacancy in the business district and a drop in overall market activity.

The share of the CBD and off-CBD business district has fallen consistently, as its desirability as a premium office space destination has reduced considerably over time. Occupiers have shifted to comparatively lower-priced options in the SBD that currently offer similar market dynamics as the erstwhile CBD and off-CBD. The H1 2014 absorption numbers have stayed true to the trend and fell 63% YoY, clocking approximately 0.17 mn sq ft in the first six months of 2014. This drop in transacted volumes, coupled with the increasing desirability of SBD locations, has caused rentals to fall by 1% in H1 2014, compared to the previous reference period. Transaction activity was well dispersed among all sectors, with the manufacturing sector taking up 37% of the total volume accounted for by the business district. Manufacturing major B/E Aerospace accounted for the largest lease signed in the business district, in Sarvottam Building at Jubilee Hills. Transactions in Jubilee Hills, Banjara Hills and Begumpet constituted nearly 95% of the total area accounted for by the CBD. Rentals showed a negative bias, dropping 2% in H1 2014, compared to the previous period.

The PBD - East business district experienced approximately 0.05 mn sq ft of absorption during H1 2014, with GVK Bioscences and Sunera Technologies taking up over 95% of the transacted space in Uppal. Although occupiers evinced interest for locations such as Uppal and Pocharam, they did not convert to transactions during the year despite offering the lowest rents in the Hyderabad office space market. This business district saw no new office space completions during the year, and occupancy levels here continue to be the highest in the market. Rentals have stagnated in PBD - East locations, as there has been no significant traction in this business district.

Business District-wise Rental Movement

Business District	Rental Value Range in H1 2014 (₹/Sq ft/month)	12-month change	6-month change
CBD and off-CBD	40–45	-2.0%	0.4%
SBD	38–41	1.5%	1.0%
PBD - West	30–35	1.1%	0.8%
PBD - East	26–31	0.5%	0.5%

Source: Knight Frank Research

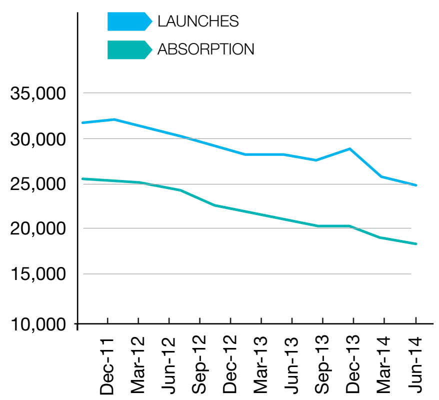
Notes

MUMBAI

RESIDENTIAL MARKET

FIGURE 1

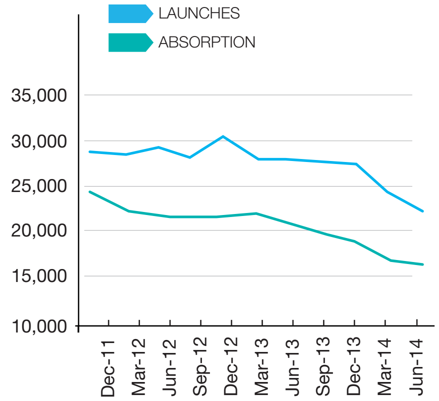
Long Term (Eight Quarters) Moving Average Trend of Launches and Absorption



Source: Knight Frank Research

FIGURE 2

Short Term (Four Quarters) Moving Average Trend of Launches and Absorption



Source: Knight Frank Research

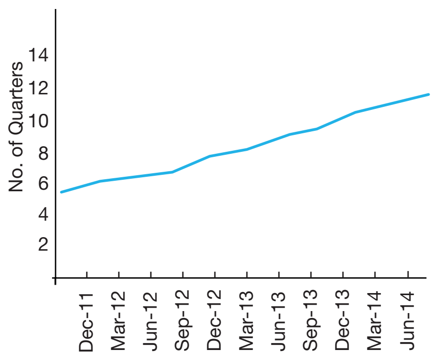
Metropolitan Region Analysis

Over the last 2–3 years, India's economic health had deteriorated, and the situation of the Mumbai Metropolitan Region (MMR) residential property market was no different. The shrinking size of the market in terms of demand and supply in this segment confirms the misfortune of the region's residential market. After a decline of 14% in demand last year, the latest half yearly numbers for H1 2014 showed a demand slowdown by 25% in comparison with the same period last year. While a policy hiatus by the union government slowed the economic engine and impacted buyer sentiment in 2013, buyers continued to sit on the fence for the most part of H1 2014 in anticipation that the new and stable leadership at the Centre would revive the ailing economy. Taking cognizance of the weak consumer appetite, developers adopted several measures, ranging from the 20:80 financing scheme and rent back scheme to waivers on stamp duty and registration, in a bid to revive sales. Eventually, the developers attuned their strategy to the changed market scenario. The resultant impact on the launch of new housing units was a decline of 10% in 2013, followed by a staggering 38% decline in H1 2014. The assessment over a longer period, depicted by the smooth moving average trend lines in the charts below, highlight the contraction of the MMR residential property market. The long-term (8-quarter) trend line captures the declining momentum; the decline is sharper in the short-term (4-quarter) trend line that captures the four most recent quarters. In the case of new launches, the long-term trend indicates a contraction of 22% in the quarterly absorption rate between Q4 2011 and Q2 2014, whereas the short-term trend has shrunk by 24%. In the case of absorption, the size of the market has dwindled by 28% in the long-term trend and a steeper 34% in the short-term trend during this period.

The unabated demand-supply gap in the MMR residential market has created a pile-up of unsold inventory, which now stands at 2,13,742 dwelling units. The MMR is a growing urban agglomeration and the second largest residential market in the country. Hence, the assessment of the health of this market has to be done by comparing the inventory level with the rate of sale. Accordingly, we calculate the quarters-to-sell (QTS) ratio for the region. The QTS ratio indicates the time period required to clear the inventory. The QTS ratio for the MMR has more than doubled in the last ten quarters, from being 5 in December 2011 to 12 in June 2014, implying that the unsold inventory will take almost three years to sell at the average absorption rate of the preceding eight quarters. A sharper decline in demand as compared to supply has resulted in such a precarious inventory pile-up. While the inventory two years ago was mainly on account of under-construction projects, the share of ready-possession projects is rising this time around. Opportunistic investors, including some private equity fund firms, have started to exploit this new investment avenue presented by the residential market.

While the state of affairs of the region's real estate market continued to remain in the doldrums in H1 2014, this period has seen significant completion of transit infrastructure that has the potential to alter the dynamics of the region's property market, the most significant being the completion of the Versova-Andheri-Ghatkopar corridor of the city's first metro rail. Covering a distance of 11.4 km, this efficient and comfortable urban transport system has boosted the west-east connectivity in the city

FIGURE 3
Quarters to Sell Analysis



Source: Knight Frank Research

considerably by reducing the travel time from 1–1.5 hours to 21 minutes. Another significant project that has reached completion is the Chembur-Wadala corridor of the city's first monorail. An efficient and convenient form of transport, the monorail is suited to operate in crowded and narrow roads where the metro cannot be implemented. The benefit of this first phase, which covers a distance of 8.9 km, is limited at present because it does not connect any employment hubs. However, once the second phase of 11.2 km connecting Wadala and Jacob Circle is operational by 2016, this monorail link will become an important transit corridor from the perspective of the realty market.

The Eastern Freeway, a 16.8 km controlled-access highway connecting the Ghatkopar-Mankhurd Link Road to P D'Mello Road, also became operational in H1 2014. The first of its kind, this transit project has enhanced the connectivity of the Central Suburbs with South Mumbai significantly. Improving connectivity with the employment hubs of Nariman Point, Colaba and Cuffe Parade, this infrastructure development has increased the north-south connectivity of the region.

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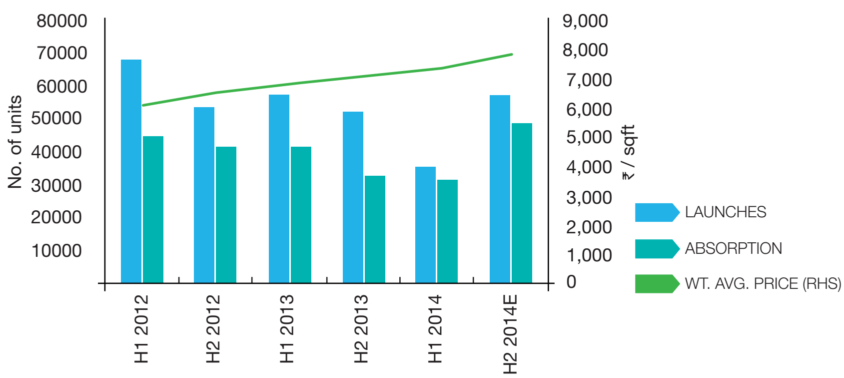
While these four important projects have come up within the Mumbai city limits, they are redefining the property market dynamics of the entire metropolitan region. On account of high residential property prices in and around office markets, a large section of the region's populace travels from the suburbs and peripheral suburbs to their workplaces. The travel time in most cases ranges from 30–60 minutes for road travel and 60–120 minutes in the case of suburban train travel. These new infrastructure projects have shrunk the travel time for people who stay in the affordable peripheral suburbs and commute to work in the city. In effect, they have increased the acceptability of residential markets in the peripheral suburbs. Another critical factor that has contributed to the acceptability of the peripheral suburbs is the development of new office projects towards the north of the city, mainly in the Western and Central Suburbs. Hence, these two dominant factors of infrastructure development and access to employment opportunities will determine the fate of the residential property market in the foreseeable future.

With a new, stable government at the Centre, stakeholder sentiment has witnessed remarkable improvement. The first budget under the leadership of Mr Narendra Modi offered several positive surprises to the realty sector, with special focus on housing. Expanding the avenues of fund flow to the sector and cementing the position of house buyers will benefit the Mumbai realty market, with peripheral markets being the biggest beneficiaries. The BFSI and IT/ITeS sectors – dominant employers in the region – have indicated their increasing optimism for business in FY 2015. Considering these factors, after a dull first half, we forecast new launches and absorption to increase by 10% and 49% respectively in H2 2014, compared to the same period last year. As a result, although 2014 would witness a decline of 15% in new launches to 92,845 housing units, it would be a trend reversal year for absorption, which will increase by 8% to 80,022 units. On the residential price front, while the weighted average price in the MMR increased by 4.2% in H1 2014, the forecasted increase for the entire year (2014) is 10.1%.

FIGURE 4
Launches, Absorption and Price Trend



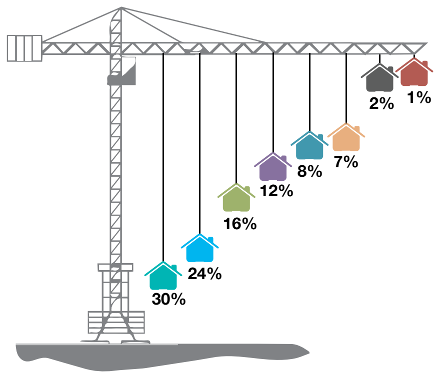
Source: Knight Frank Research

Micro-market Analysis

The performance of various micro-markets within the MMR will vary according to the respective demand drivers, i.e. its occupation profile, connectivity with employment hubs, physical and social infrastructure development and cost of its real estate. From the perspective of the residential real estate market, the MMR is divided into eight micro-markets, as given in the table below:

Micro-markets	Location
Central Mumbai	Dadar, Lower Parel, Mahalakshmi, Worli, Prabhadevi
Central Suburbs	Sion, Chembur, Wadala, Kurla, Ghatkopar, Vikhroli, Bhandup, Mulund
Navi Mumbai	Vashi, Nerul, Belapur, Kharghar, Airoli, Panvel, Ulwe, Sanpada
Peripheral Central Suburbs	Kalyan, Kalwa, Dombivli, Ambernath, Bhiwandi, Mumbra, Karjat
Peripheral Western Suburbs	Vasai, Virar, Boisar, Palghar, Bhayandar, Nallasopara
South Mumbai	Malabar Hill, Napean Sea Road, Walkeshwar, Altamount Road, Colaba
Thane	Naupada, Ghodbunder Road, Pokhran Road, Majiwada, Khopat, Panchpakhadi
Western Suburbs	Bandra, Andheri, Goregaon, Kandivali, Borivali, Santacruz, Vile Parle

FIGURE 5
Micro-market Split of Under-Construction Units as on June 2014



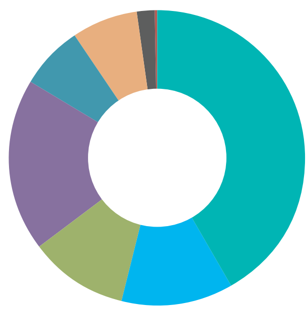
PERIPHERAL CENTRAL SUBURBS
PERIPHERAL WESTERN SUBURBS
NAVI MUMBAI
WESTERN SUBURBS
CENTRAL SUBURBS
THANE
CENTRAL MUMBAI
SOUTH MUMBAI

Source: Knight Frank Research

The most expensive South Mumbai micro-market accounts for less than 1% of the 4,47,294 under-construction units in these eight micro-markets. The South Mumbai micro-market is home to industrialists and high net-worth individuals (HNIs), and pricing is not bound by the affordability benchmark in projects offering snob value. However, despite land scarcity, which has restricted new launches in the recent period, this micro-market's fortunes have suffered. A comparison with all other micro-markets in the MMR indicates that the inventory level in the South Mumbai market will take the maximum time of 18 quarters (4.5 years) to sell. The age of inventory, calculated as the time elapsed since launch, is also the longest, at 15 quarters. A weak business environment, coupled with the northward movement of prominent corporate office occupiers, has impacted the fortunes of this micro-market adversely.

Central Mumbai, emerging as a prominent residential market on the back of premium residential and social infrastructure developments, has around 2% of the under-construction units in the MMR. This micro-market has also emerged as a premium office market for occupiers from the Banking Financial Services and Insurance (BFSI) front office

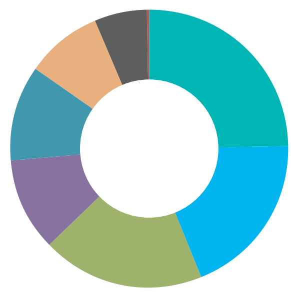
FIGURE 6
Micro-market Split of Launched Units in H1 2013



42% PERIPHERAL CENTRAL SUBURBS
12% WESTERN SUBURBS
11% PERIPHERAL WESTERN SUBURBS
19% NAVI MUMBAI
7% CENTRAL SUBURBS
7% THANE
2% CENTRAL MUMBAI
<1% SOUTH MUMBAI

Source: Knight Frank Research

FIGURE 7
Micro-market Split of Launched Units in H1 2014



25% PERIPHERAL CENTRAL SUBURBS
19% WESTERN SUBURBS
19% PERIPHERAL WESTERN SUBURBS
11% NAVI MUMBAI
11% CENTRAL SUBURBS
9% THANE
6% CENTRAL MUMBAI
<1% SOUTH MUMBAI

Source: Knight Frank Research

Mumbai Metropolitan Region Map

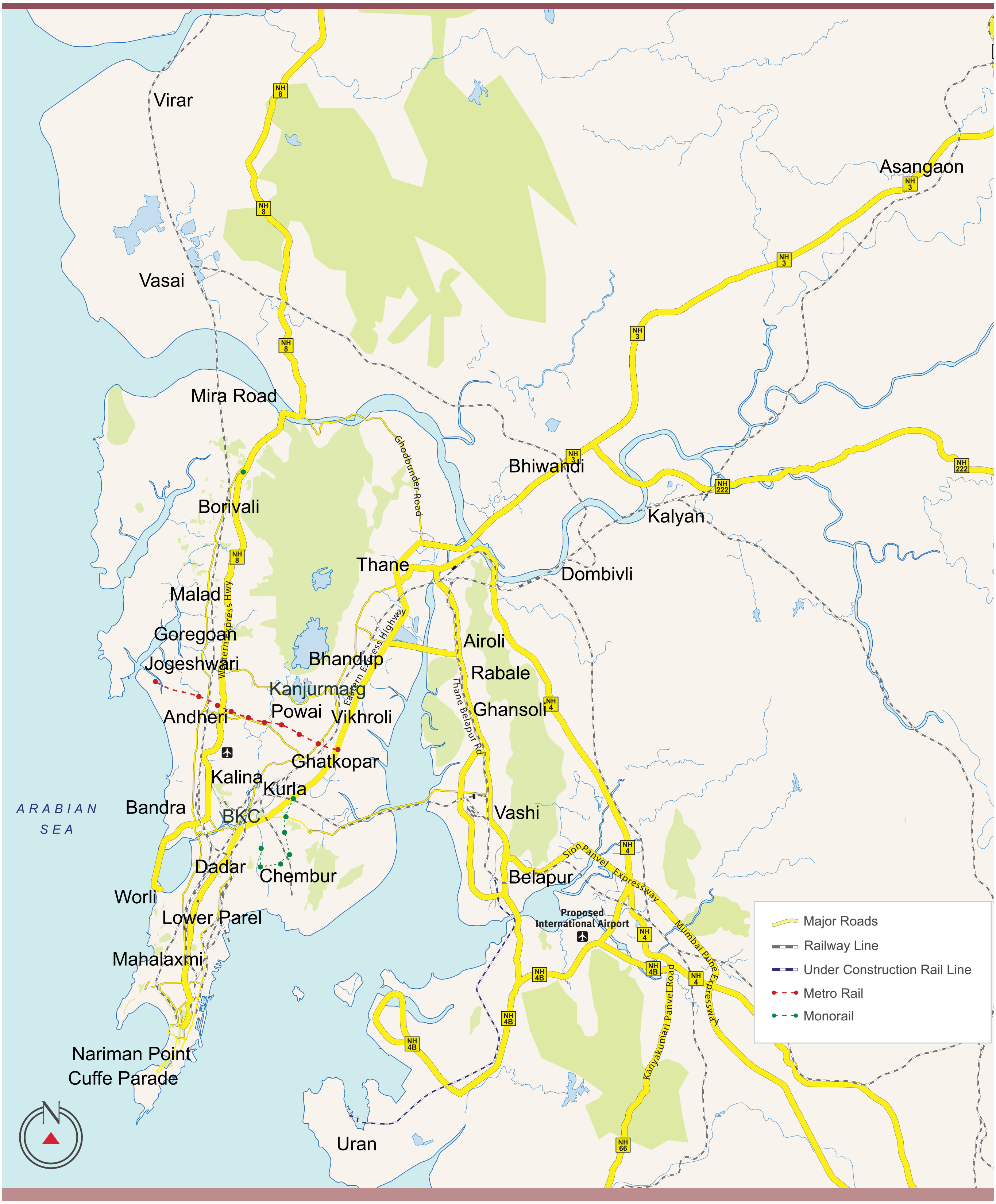
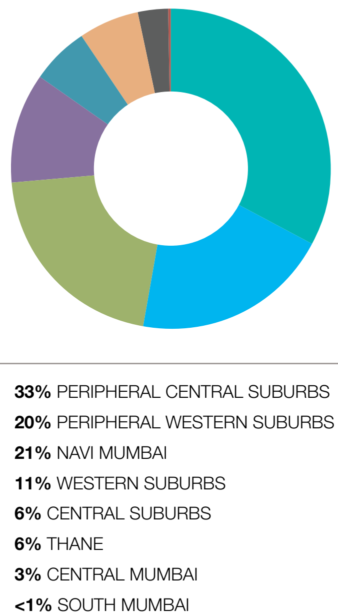
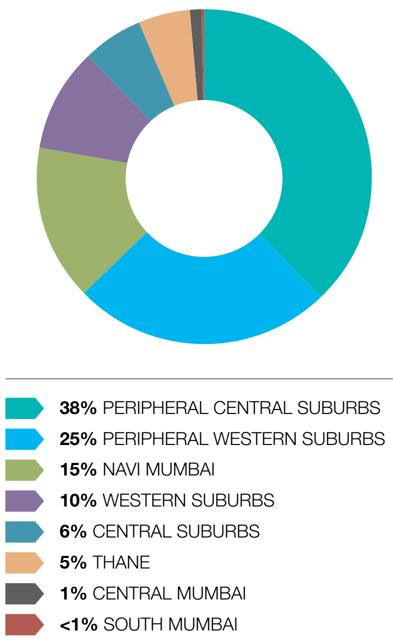


FIGURE 8
Micro-market Split of Absorption in H1 2013



Source: Knight Frank Research

FIGURE 9
Micro-market Split of Absorption in H1 2014



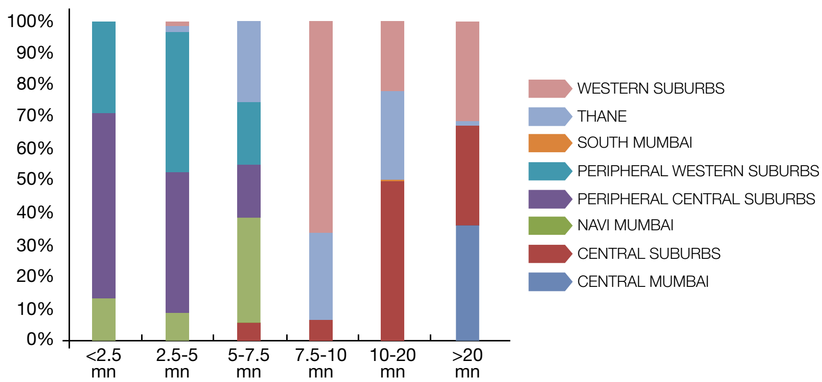
Source: Knight Frank Research

segment and corporate headquarters of corporations from the manufacturing, media and consulting sectors. The Mumbai Monorail will pass through this micro-market once the second phase of 11.2 km, connecting Wadala and Jacob Circle, is operational by 2016. This will increase the attractiveness of this market and ease the burdened traffic conditions in the densely-populated locations of Dadar, Parel and Lower Parel. At a QTS ratio of 16, Central Mumbai will take almost four years to clear the inventory that has been in the market for nine quarters.

The Western Suburbs have witnessed an increase in their share of new launches to 19% in H1 2014 compared to 12% in the same period last year. The presence of employment opportunities and social infrastructure, along with decent road and suburban train connectivity with other parts of the city, has immensely benefitted this market. With the completion of the Versova-Ghatkopar corridor of the Mumbai Metro in H1 2014, the connectivity of the Western Suburbs with the Central Suburbs has improved significantly. The merits of this enhanced connectivity through an efficient Mass Rapid Transit System (MRTS) will benefit residential and office projects in and around Andheri, as eight out of the ten metro stations are within this micro-market. Another transit project of significance that will benefit this micro-market immensely is the Santacruz–Chembur Link Road (SCLR) that became operational in H1 2014. This 6.5-km arterial road enhances the connectivity of this micro-market with the Central Suburbs by reducing the travel time from an hour to 20 minutes. The Western Suburbs have an unsold inventory of 13 quarters, with an average age of nine quarters.

The Central Suburbs, which currently account for 8% of the under-construction units in the MMR, witnessed their share in new launches almost double, from 6% in H1 2013 to 11% in H1 2014. Not long ago, this micro-market was perceived as a cheaper cousin of the Western Suburbs. However, improved east-west connectivity through the Jogeshwari–Vikhroli Link Road and the recently-completed SCLR and metro corridor have increased the appeal of this market. Further, the recently-completed Eastern Freeway has benefited commuters of this market the most on account of improved connectivity with the South Mumbai office markets. Quality retail developments and office spaces along LBS Road, parallel to the arterial Eastern Express Highway, have added to the appeal of its residential developments. A QTS ratio of 15 implies that the inventory in this micro-market will take 15 quarters to sell. However, at nine quarters, the age of inventory in this market is similar to most micro-markets in the region.

FIGURE 10
Micro-market Level Ticket Size Split of Launched Units During H1 2014



Source: Knight Frank Research

Price Movement in Select Locations

Location	Micro-market Location	Price range in H1 2014 (₹/sq ft)	Change since H1 2013*	Change since H2 2013*
Lower Parel	Central Mumbai	24,000–36,000	6%	1%
Worli	Central Mumbai	31,000–50,000	-3%	-13%
Ghatkopar	Central Suburbs	12,000–22,000	24%	18%
Mulund	Central Suburbs	10,000–14,000	-4%	-5%
Powai	Central Suburbs	13,000–20,000	20%	9%
Panvel	Navi Mumbai	4,500–6,500	6%	4%
Kharghar	Navi Mumbai	6,500–9,500	15%	6%
Vashi	Navi Mumbai	10,000–15,000	-7%	1%
Badlapur	Peripheral Central Suburbs	2,800–3,500	6%	2%
Dombivali	Peripheral Central Suburbs	4,500–6,000	8%	2%
Mira Road	Peripheral Western Suburbs	5,500–7,500	0%	1%
Virar	Peripheral Western Suburbs	4,500–5,500	0%	2%
Tardeo	South Mumbai	40,000–60,000	8%	4%
Ghodbunder Road	Thane	6,000–10,000	5%	2%
Naupada	Thane	13,000–18,000	14%	4%
Andheri	Western Suburbs	14,000–20,000	9%	1%
Bandra (W)	Western Suburbs	40,000–60,000	16%	0%
Borivali	Western Suburbs	11,000–15,000	4%	1%
Dahisar	Western Suburbs	8,000–10,000	13%	3%
Goregaon	Western Suburbs	13,000–15,000	4%	2%

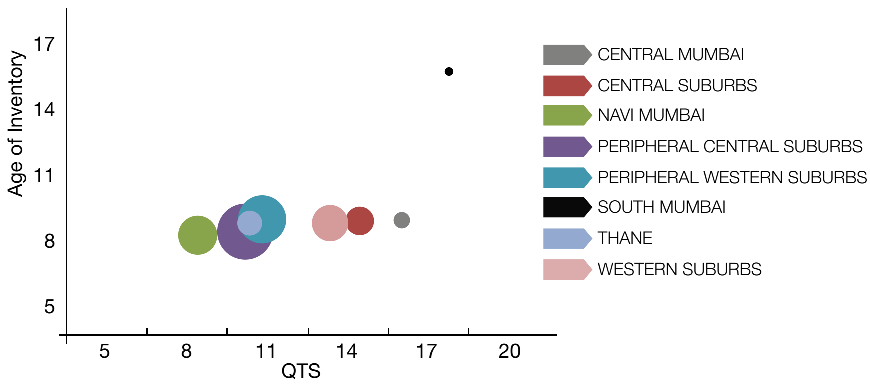
*Change in weighted average prices

Source: Knight Frank Research

Thane, a micro-market with a 7% contribution to the under-construction units in the MMR, witnessed its share in new launches inch up marginally from 7% in H1 2013 to 8% in H1 2014. A city of lakes, Thane has been developing rapidly over the last decade on account of its proximity to both, Mumbai and Navi Mumbai. The arterial Ghodbunder Road has witnessed frenetic residential development over the last decade.
To address the increasing density of vehicular traffic on this crucial connector to the Western Suburbs, the government has developed multiple flyovers along the stretch. With quality mall developments and other social infrastructure for education and health developing rapidly, the appeal of this market has increased significantly. At a QTS ratio of 11, the situation is better than the overall MMR region ratio, which stands at 12.

Navi Mumbai, developed as a satellite city of Mumbai and also its affordable residential alternative, is the third largest market in terms of residential development in the MMR. However, its share of launches and absorption in the MMR has declined from 19% to 11% and from 22% to 15% respectively in H1 2014, compared to the same period last year. On the back of employment opportunities within Navi Mumbai, quality housing developments and corollary social infrastructure, prices in the Navi Mumbai micro-market have climbed fast. During H1 2014, the price growth in Kharghar and Panvel, the most active markets, was 6% and 4% respectively. New projects are coming up mainly in localities like Kharghar, Taloja, Kalamboli and Panvel, where prices are relatively low in comparison with dense locations on the Thane–Belapur Road and the picturesque Palm Beach Road. As a result, all new housing units launched during H1 2014 were under the ₹7.5 mn ticket size. A favoured residential market on account of improving connectivity with South Mumbai through the Sion–Panvel Highway, Navi Mumbai has the lowest QTS ratio and age of inventory in the MMR, implying better near-term prospects compared to others.

FIGURE 11
QTS vs. Age of Inventory across Micro-Markets



*Size of the bubble indicates the quantum of unsold inventory

Source: Knight Frank Research

The Peripheral Central Suburbs continue to be the biggest micro-market, both in terms of launches and absorption in H1 2014. The dominance of this market stems from the fact that it has emerged as an affordable housing market with good suburban train connectivity with employment hubs in Mumbai. Locations like Kalyan and Dombivli, on account of their decent road connectivity with the IT/ITeS hub of Navi Mumbai through the Kalyan–Shilphata Road, are witnessing increasing interest from house buyers. Many prominent Mumbai developers have responded to the increasing consumer interest by offering projects with lifestyle-enhancing amenities in this micro-market. Yet, contributing more than half of all new launches in the MMR in the under-₹ 5 mn ticket size in H1 2014, it continues to remain a market for the middle class. Not surprisingly, despite being a large market, it fares among the top two markets in the MMR in terms of QTS ratio. This market will take 10 months to liquidate its unsold inventory, which has been standing in the market for nine quarters now.

At 24%, the Peripheral Western Suburbs is the second largest micro-market in terms of the quantum of under-construction activity in the MMR. Good connectivity with Mumbai's office markets through the suburban train network was the primary reason for the initial wave of housing market growth in this market. With the northward shift of office occupiers to locations like Andheri, Malad and Goregaon, the acceptability of the Western Suburbs among house buyers increased tremendously. Residential localities like Dahisar, Bhayander and Mira Road have benefitted on account of acceptability from road commuters. However, locations like Vasai and Virar are largely dependent on the suburban train connectivity. While the proposal for the ambitious elevated rail corridor has increased the hope of stakeholders in this micro-market, it continues to remain a distant dream for consideration of any impact on the realty market in the near term. The micro-market has an unsold inventory aged nine quarters, which will take 11 quarters to sell.

Clearly, within the MMR, the most expensive South Mumbai market fares the worst, with an 18-quarter inventory that has remained in the market for 15 quarters. The quantum of inventory, however, is the lowest in this market. Navi Mumbai, with an unsold inventory of nine quarters, fares the best among all the residential markets of the MMR. Its age of inventory, at eight quarters, is also the lowest in comparison with all the other markets. The quantum of unsold inventory is the largest in the Peripheral Central Suburbs. However, this is the second best market in the MMR, based on the parameter of a 10-quarter inventory that was launched nine quarters ago.

Key Takeaways

After a decline of 14% in demand last year, the latest half yearly numbers for H1 2014 showed a demand slowdown by 25% in comparison with the same period last year. While a policy hiatus by the union government slowed the economic engine and impacted buyer sentiment in 2013, buyers continued to sit on the fence for the most part of H1 2014 in anticipation that the new and stable leadership at the Centre would revive the ailing economy

The unabated demand-supply gap in the MMR residential market has created a pile-up of unsold inventory, which now stands at 2,13,742 dwelling units. While the inventory two years ago was mainly on account of under-construction projects, the share of ready-possession projects is rising this time around. Opportunistic investors, including some private equity fund firms, have started to exploit this new investment avenue presented by the residential market

While four important transit infrastructure projects have come up within the Mumbai city limits, they are redefining the property market dynamics of the entire metropolitan region

Although 2014 would witness a decline of 15% in new launches to 92,845 housing units, it would be a trend reversal year for absorption, which will increase by 8% to 80,022 units

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OFFICE MARKET

Metropolitan Region Analysis

The recognition of being the financial capital of the country puts Mumbai at the forefront of the economic landscape of India, and Asia as well. This distinction also makes Mumbai an important city from the global economic perspective. Besides being the state capital, the city also serves as the headquarters for the political and administrative machinery of the state government of Maharashtra.

There are several reasons for which national and multinational corporates vie to have a base in Mumbai. The availability of talent, a favourable business environment, international air connectivity and quality office developments are primary factors. Additionally, there are specific factors that have attracted the financial industry: for instance, the presence of prominent stock and commodity exchanges, and regulators and headquarters of several banks has helped in making Mumbai the most preferred location for occupiers from the Banking Financial Services and Insurance (BFSI) sector. Collectively, these features have made the city a preferred destination for corporate headquarters of national and multinational companies. An analysis of driver industries for the Mumbai Metropolitan Region (MMR) office market indicates that the BFSI sector led the office space demand, contributing 32% to the absorption in H1 2013. This was followed by the other services sector, which takes in to account companies from industries like media, consulting and eCommerce. However, between H1 2013 and H1 2014, there has been a remarkable shift in the demand dynamics of the city's office market. The manufacturing sector has emerged as the largest demand driver, with a contribution of 48% in H1 2014, leaving behind the BFSI and IT/ITeS sectors at 15% and 12% respectively. Companies like Clariant Chemicals, Pfizer, HPCL and Firestar Diamond from the manufacturing sector have taken up space during this period. With the increasing presence of companies from the manufacturing and other services sectors, the Mumbai office market has reduced its dependence on the BFSI sector.

Besides the changing occupier profile, another important shift during H1 2014 has been brought about by the completion of major transit infrastructure projects, the most significant being the Versova–Andheri–Ghatkopar corridor of the city's first metro rail. Covering a distance of 11.4 km, this efficient and comfortable urban transport system has boosted the west–east connectivity in the city considerably, by reducing the travel time from 1–1.5 hours to 21 minutes. Another significant project that has reached completion is the Chembur–Wadala corridor of the city's first monorail. An efficient and convenient form of transport, the monorail is suited to operate in crowded and narrow roads where the metro cannot be implemented. The benefit of this first phase, which covers a distance of 8.9 km, is currently limited because it does not connect any employment hubs. However, once the second phase of 11.2 km, connecting Wadala and Jacob Circle, is operational by 2016, this monorail link will become an important transit corridor from the perspective of the realty market.

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The Santacruz–Chembur Link Road (SCLR), a 6.5-km arterial road connecting the crucial Western Express Highway (WEH) and Eastern Express Highway (EEH) at Santacruz and Chembur respectively, is another milestone project that became operational in H1 2014. The SCLR has improved the west–east connectivity significantly by cutting the

FIGURE 1
Sector-wise Absorption Split

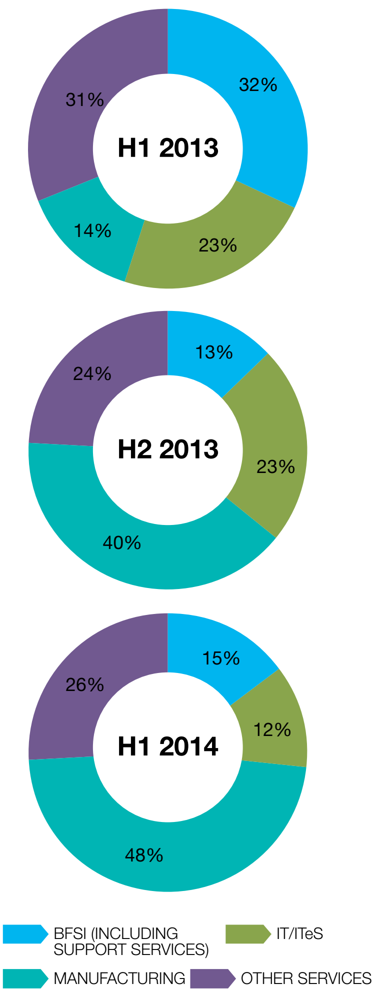
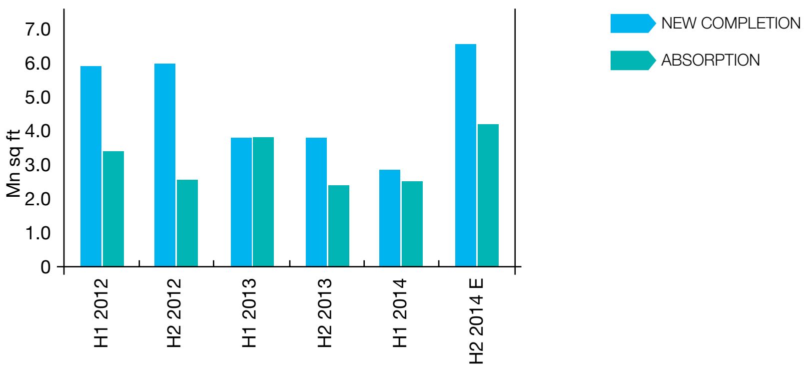


FIGURE 2
New Completion and Absorption



Source: Knight Frank Research

travel time between Santacruz and Chembur from an hour to 20 minutes.

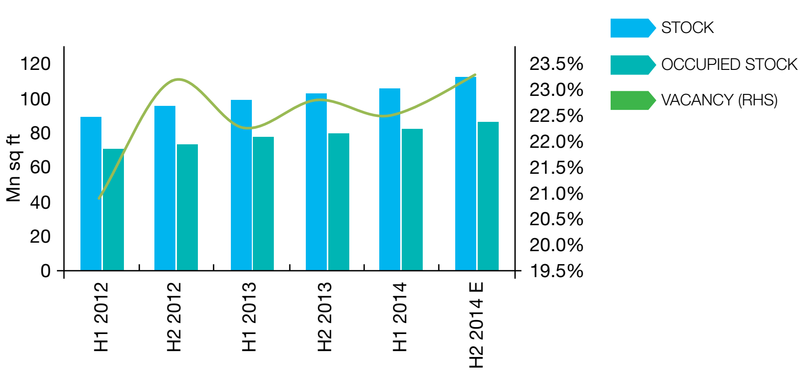
These infrastructure projects have translated into better connectivity between employees and office hubs, especially the east–west connectivity – a critical factor that was lagging in the city. With a slew of transit-oriented projects addressing this factor, occupiers will now consider the same while deciding the location of their offices. The impact on business districts, however, would vary, depending on several other factors like rent, driver industry and appropriate space availability.

Overall, the MMR office market witnessed a lacklustre trend in absorption as well as new project completions in H1 2014. The uncertain economic and political environment in the wake of the 2014 general elections resulted in corporates adopting a noncommittal attitude towards taking up office space during the first half. As a result, the absorption of office space, at 2.5 mn sq ft, declined by 34% in H1 2014 over H1 2013. In comparison with H2 2013, it recorded a marginal 5% growth. With developers deferring project completions to attune their offering to the changed market circumstances, new project completions to the tune of 2.9 mn sq ft were recorded in H1 2014, which is a 25% decline in comparison with the same period last year, as well as in H2 2013. Though the hesitation among developers as well as occupiers hurt market growth, it ensured that the vacancy levels in completed projects did not jump significantly. In comparison wioth H1 2013, when the market vacancy stood at 22.3%, the vacancy in H1 2014 increased marginally to 22.5%. As a result, the rents moved in a narrow range during this period. The weighted average rent in the MMR increased from ₹ 111/sq ft/month to ₹ 112/sq ft/month, recording a growth of 1% between H1 2013 and H1 2014.

The office transaction analysis indicates that the number of deals has improved by 46% to 118 deals in H1 2014, compared to H2 2013, when the markets witnessed a drastic fall in transaction activity on account of the worsening business scenario. Not surprisingly, even after this revival, the number of deals stands at 28% lower compared to H1 2013.

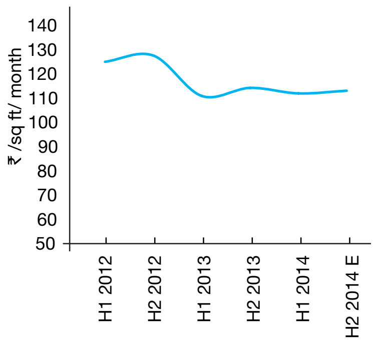
The deal size analysis indicates that the average deal size in H1 2014 declined by 28% to 21,430 sq ft from 29,695 sq ft in H2 2013. The primary reason for this change is the declining IT/ITeS industry dominance, which witnessed its share in absorption decline from 23% in H2 2013 to 12% in H1 2014.

FIGURE 3
Office Space Stock and Vacancy



Source: Knight Frank Research

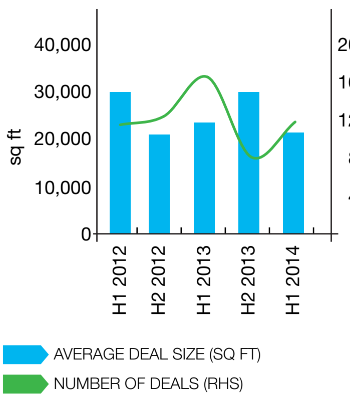
FIGURE 4
Weighted Average Rental Movement (₹/sq ft/month)



Source: Knight Frank Research

The newly-elected stable government has infused hope among households and businesses alike. The government initiatives for improving business sentiments, along with impetus on real estate FDI and REITs, will bode well for the country's financial capital. As a result, the absorption in office space in the MMR is estimated to revive in H2 2014. The absorption, at 4.2 mn sq ft in H2 2014, would be a 67% growth over H1 2014. In contrast, new project completions, at 6.6 mn sq ft, would be a 131% growth over H1 2014. The weighted average rent is estimated to increase only marginally, by 1%, during this period. Such market dynamics would translate into a market expansion during 2014 over 2013. The absorption of 6.8 mn sq ft in 2014 would be an increment of 8% over last year. In the case of new completions, at 9.5 mn sq ft in 2014, the growth would be 24%.

FIGURE 5
Deal Size Analysis



Source: Knight Frank Research

Business District Analysis

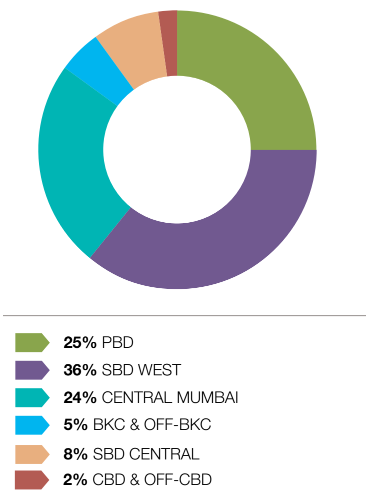
The MMR office market has been divided in to six business districts, in accordance with the homogeneity of parameters like rent, driver industry and infrastructure.

Business District	Location
CBD and off-CBD	Nariman Point, Cuffe Parade, Ballard Estate, Fort, Mahalaxmi, Worli
BKC and off-BKC	BKC, Bandra (E), Kalina, Kalanagar
Central Mumbai	Parel, Lower Parel, Dadar, Prabhadevi
SBD West	Andheri, Jogeshwari, Goregaon, Malad
SBD Central	Kurla, Ghatkopar, Vikhroli, Kanjurmarg, Powai, Bhandup, Chembur
PBD	Thane, Airoli, Vashi, Ghansoli, Rabale, Belapur

The CBD and off-CBD business district comprises locations like Nariman Point, Fort, Cuffe Parade and Worli. The origin of business in the country's financial capital can be traced to this business district, where office space development began as early as the 1970s. However, high rent, coupled with the northward growth of the city, has reduced the dominance of this business district. In H1 2014, it accounted for just 2% of the absorption. Though the lack of land availability restricts new supply in this market, the demand of office space is also limited, mainly emanating from the requirement of offices for the senior management of top corporate houses. The rent in this market witnessed a 6% decline during the last twelve months.

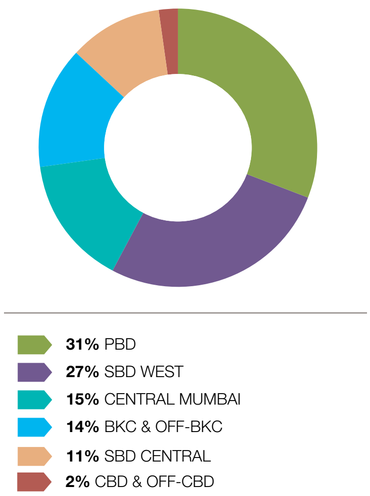
In terms of infrastructure projects, the Eastern Freeway, a 16.8-km controlled-access highway connecting the Ghatkopar–Mankhurd Link Road to P D'Mello Road became operational in H1 2014. The first of its kind, this transit project has enhanced the connectivity of CBD locations like Nariman Point,

FIGURE 6
Business District-wise Absorption Split in H1 2013



Source: Knight Frank Research

FIGURE 7
Business District-wise Absorption Split in H1 2014



Source: Knight Frank Research

Colaba and Cuffe Parade. However, with occupiers preferring to move to Central Mumbai and BKC, this market will have an uneventful future.

Central Mumbai, with markets like Parel, Lower Parel and Dadar, is located centrally within the city. With defunct textile mills giving way to swanky office and retail developments, Central Mumbai witnessed a massive transformation during the last decade. Coupled with relatively lower rentals compared to the CBD and BKC, occupiers typically intending to set up front offices of multinational banks and financial institutions in the case of the BFSI sector have evinced strong interest in this business district. As a result, the share of this business district in office space absorption reached 24% in H1 2013. However, a receding supply pipeline, coupled with muted demand from the BFSI sector, has resulted in a decline in the share of absorption to 15% or 3,64,121 sq ft in H1 2014. The Chembur–Wadala corridor of the city's first monorail, covering a distance of 8.9 km, has become operational in H1 2014. Going forward, the Central Mumbai business district would witness improved connectivity once the 11.2-km second phase of the monorail, connecting Wadala and Jacob Circle, is operational in 2016. With Central Mumbai witnessing a rent growth of 6% during the last 12 months, such prospects, coupled with an encouraging occupancy scenario, would translate in to an even better fortune.

The BKC and off-BKC business district comprises the micro-markets of Bandra Kurla Complex (BKC), Bandra (East), Kalina and Kalanagar. This business district saw its share in absorption increase from 5% in H1 2013 to 14% in H1 2014. A premium office market, it commands a rent of ₹ 190–290/sq ft/month, which is 5% lower than the level of H1 2013. BKC and off-BKC command a premium because of the profile of the occupiers here: typically front offices of multinational banks and financial institutions in the case of the BFSI sector. In the manufacturing sector, the profile includes corporate headquarters of established domestic and international companies. Additionally, occupiers from consulting and media industries and foreign consulates have evinced a strong interest to set up offices here. Among other prominent names, Pfizer, the American pharmaceutical major, took up space in this business district in H1 2014. Going forward, in H2 2014, a limited supply pipeline, coupled with steady absorption, would bode well for this business district.

Besides the changing occupier profile, another important shift during H1 2014 has been brought about by the completion of major transit infrastructure projects, the most significant being the Versova–Andheri–Ghatkopar corridor of the city's first metro rail

BUSINESS DISTRICTS OF MUMBAI METROPOLITAN REGION

Business District-wise Rental Movement

Business District	Rental Value Range in H1 2014 (₹/sq ft/month)	12-month change	6-month change
BKC and off-BKC	190–290	-5%	-2%
CBD and off-CBD	180–270	-6%	-1%
Central Mumbai	140–190	6%	5%
PBD	40–70	-1%	-3%
SBD Central	80–120	-6%	-7%
SBD West	90–130	4%	-1%

Source: Knight Frank Research

With developers deferring project completions to attune their offering to the changed market circumstances, new project completions to the tune of 2.9 mn sq ft were recorded in H1 2014, which is a 25% decline in comparison with the same period last year, as well as in H2 2013

The SBD West business district consists of markets like Vile Parle, Andheri, Jogeshwari, Malad and Goregaon. At 1.4 mn sq ft, it was the largest office market, with a share of 36% of absorption in H1 2013. However, the share stands at 27% in H1 2014 on the back of an absorption of 0.7 mn sq ft. Besides the IT/ITeS industry that had a presence in the region, a large number of occupiers from the BFSI industry have preferred to operate their backend support functions here because of lower rentals. Even as this business district remained a favourite among corporate occupiers on account of the Mumbai international airport and a strong residential catchment, the east–west connectivity through an MRTS was lacking. However, in H1 2014, the Versova–Andheri–Ghatkopar corridor of the city's first metro rail became operational. Covering a distance of 11.4 km, this efficient and comfortable urban transport system has boosted the west–east connectivity by reducing the travel time considerably, from 1–1.5 hours to 21 minutes.

The Santacruz–Chembur Link Road (SCLR), a 6.5-km arterial road connecting the crucial Western Express Highway (WEH) and Eastern Express Highway (EEH) at Santacruz and Chembur respectively, is another milestone project that became operational in H1 2014. The SCLR has improved west–east connectivity significantly by cutting the travel time between Santacruz and Chembur from an hour to 20 minutes.

Together, both these projects have increased the appeal of the SBD West market, as the residential catchment has been enlarged on account of better connectivity with the Central Suburbs. As a result, office rent in this market now stands at ₹ 90–130/sq ft/month, higher by 4% since H1 2013.

The SBD Central business district, comprising the micro-markets of Kurla, Chembur, Vikhroli, Kanjurmarg, Bhandup and Powai, increased its share in absorption during the last 12 months. At an absorption of 0.27 mn sq ft, the share in absorption stands at 11% in H1 2014, in comparison with 8% in H1 2013. The enhanced east–west connectivity on account of the completion of the Mumbai Metro Phase I and the SCLR in H1 2014 has benefitted this market as well. On account of relatively lower rent at ₹ 80–120/sq ft/month, this market will continue to garner occupier interest. However, a strong supply pipeline will restrict rent growth in the immediate future.

The PBD business district, comprising the office markets of Navi Mumbai and Thane, attracts occupiers mainly from the IT/ITeS sector on account of the lowest rent of ₹40–70/sq ft/month that it offers. Its increasing dominance in the MMR office market is evident by its share in absorption, which stood at 31% in H1 2014 – the largest in the metropolitan region, and up from 25% in H1 2013. The increasing share in this predominantly IT/ITeS-driven market has come at a time

Select Transactions in the MMR Office Market During H1 2014

Building	Occupier	Location	Approx. Area (sq ft)
Reliable Tech Park	Clariant Chemicals	Airoli	140,000
The Capital	Pfizer	BKC	110,000
Silver Utopia	DHL	Andheri	100,000
Lighthall	Merck Pharma	Andheri	70,000
Nesco	Morgan Stanley	Goregaon	60,000
Vishwaroop IT Park	ICICI Lombard	Vashi	55,000
Marathon Futurex	HPCL	Lower Parel	51,000
One Indiabulls	CNBC	Lower Parel	50,000
Mindspace	Convergys	Airoli	50,000
Kohinoor City	Firestar Diamond	Kurla	45,000

Source: Knight Frank Research

when the share of the IT/ITeS industry in the MMR has come down from 23% in H1 2013 to 12% in H1 2014. This has happened on account of increasing interest from manufacturing sector companies like Clariant Chemicals, BASF and Bombardier. Our market assessment is that the acceptability of the manufacturing and other services sector companies, including some eCommerce companies, to set up an office here would lead to steady absorption in this business district. However, strong project completions, coupled with a high vacancy in existing projects, will prevent significant rent growth.

Key Takeaways

Between H1 2013 and H1 2014, there has been a remarkable shift in the demand dynamics of the city's office market. The manufacturing sector has emerged as the largest demand driver, with a contribution of 48% in H1 2014, leaving behind the BFSI and IT/ITeS sectors at 15% and 12% respectively

Besides the changing occupier profile, another important shift during H1 2014 has been brought about by the completion of major transit infrastructure projects, the most significant being the Versova–Andheri–Ghatkopar corridor of the city's first metro rail

Overall, the MMR office market witnessed a lacklustre trend in absorption as well as new project completions in H1 2014. An uncertain economic and political environment in the wake of the 2014 general elections resulted in corporates adopting a noncommittal attitude towards taking up office space during the first half. As a result, the absorption of office space, at 2.5 mn sq ft, declined by 34% in H1 2014 over H1 2013. It recorded a marginal 5% growth, compared to H2 2013

With developers deferring project completions to attune their offering to the changed market circumstances, new project completions to the tune of 2.9 mn sq ft were recorded in H1 2014, which is a 25% decline in comparison with the same period last year, as well as in H2 2013

The absorption of 6.8 mn sq ft in 2014 would be an increment of 8% over last year. In the case of new completions, at 9.5 mn sq ft in 2014, the growth would be 24%

NATIONAL CAPITAL REGION (NCR)

RESIDENTIAL MARKET

National Capital Region (NCR) Analysis

The National Capital Region (NCR) witnessed a slowdown during 2013, and this downward trend continues in 2014 as well. Pressures of substantial unsold inventory and liquidity constraints have compelled developers to keep new launches in check. Similarly, on the demand side, consumer sentiment was weakened by the uncertain economic fundamentals and impending elections. The analysis of the long-term moving average (eight quarters) of launches and absorption exhibits a plummeting trend since the last three years.

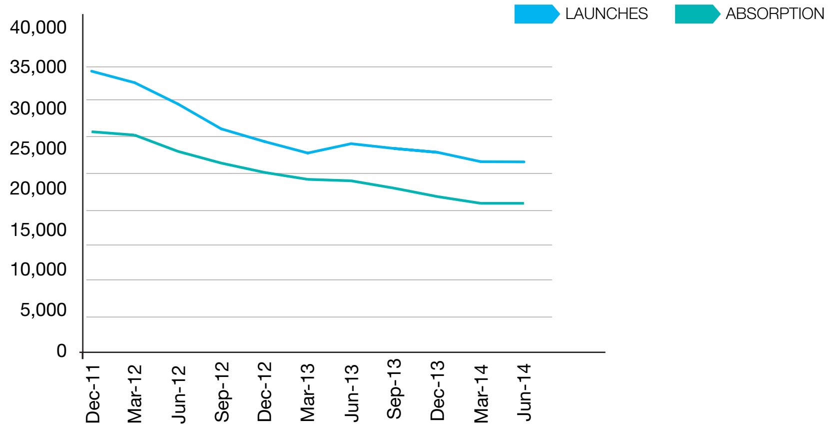
Both new launches and absorption nearly halved during 2013 compared to the peak levels of 2010. A further decline was observed in the first half of the year 2014. New launches shrunk by nearly 43% in H1 2014 compared to H1 2013, and stood at 35,500 units. Quite evidently, developers are focussing on project execution by deferring new launches. The absorption level also witnessed a 37% drop during the same period. Nearly 28,500 residential units were sold in H1 2014, which is a tad higher than the lowest-ever half yearly sales volume (26,000 in H2 2013) since the year 2010. Nevertheless, the rate of decline of new launches is higher than that of sales, indicating that the NCR market is striving to reach a better equilibrium.

While the analysis of absorption and new launches could provide a fair idea about the traction being witnessed in the market, the impact on price cannot be understood without studying the unsold inventory available in the city. A deep dive into the unsold inventory levels of the NCR is essential in order to comprehend the health of the market. In June 2014, nearly 167,000 residential units remained unsold in the NCR market, growing at a CAGR of 15% since the last three years. We have calculated the Quarters to Sell Unsold Inventory (QTS), which can be explained as the number of quarters required to exhaust the existing unsold inventory in the market. For the purpose of calculation, the eight-quarter sales velocity has been considered. A lower QTS indicates a healthier market. In June 2014, the QTS for the NCR market stood at 9, implying that the current unsold inventory would take more than two years to be fully absorbed. This is undeniably high and has been inching upwards every two quarters, indicating a weakening market. In fact, the QTS of the NCR market has risen significantly from 5 in June 2012 to 9 in June 2014. The recent slowdown in project launches was needed to control further inventory pileup.

Although the NCR market is reeling under the immense pressure of unsold inventory, we expect it to gain some momentum in H2 2014. Market sentiment has already seen some improvement post the elections. According to our recent survey, supply-side stakeholders are quite bullish about the residential sector and expect better launches and sales volumes by the end of the year. Sales inquiries have gone up in the past month, indicating some sort of revival. The Union Budget of 2014 has also proposed constructive measures that are likely to have a positive impact on home buyer sentiment and give a fillip to developer activities. As per our forecasts, new launches will increase by 10% to 37,000 units in H2 2014, compared to H2 2013. Absorption is forecasted to increase by 17% to 30,500 units in H2 2014, compared to the same period in 2013. A lower growth in project launches compared to the sales volume is likely to have a positive impact on the mounting unsold inventory levels and QTS ratio. Even with a recovery in H2 2014, the overall yearly numbers will be slightly below those of 2013. New launches and absorption for the year 2014 will stand at 72,700 units and 59,000 units, showing a decline of 24% and 17% respectively.

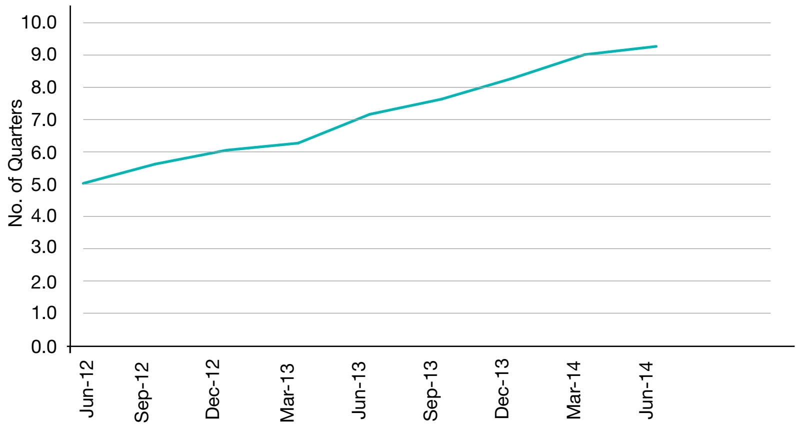
Despite showing signs of weakening, the NCR market has been able to hold residential prices. However, the growth

FIGURE 1
Long term (eight quarters) moving average trend of launches and absorption



Source: Knight Frank Research

FIGURE 2
Quarters to Sell Unsold Inventory (QTS)



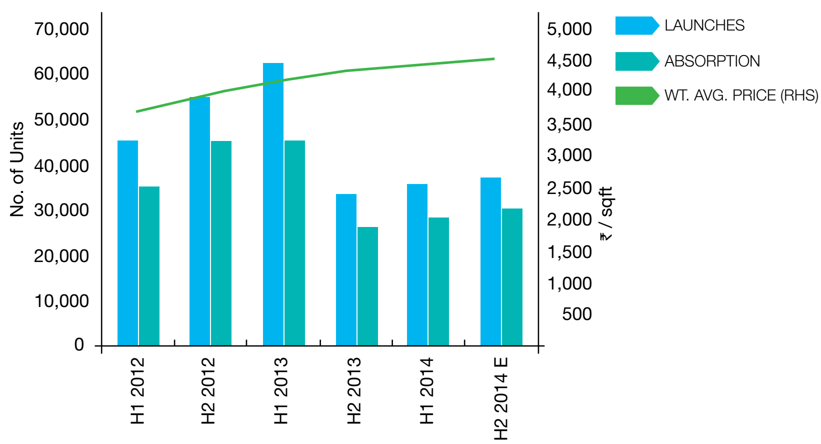
Source: Knight Frank Research

in weighted average prices has dwindled significantly in the last couple of quarters. The weighted average residential asking prices in the NCR have increased by 5%, from ₹ 4,195 per sq ft in H1 2013 to 4,400 per sq ft in H1 2014. Developers are persistent and continue to launch projects at higher prices, claiming increased input costs and higher borrowing costs. However, they have taken cues from the weakened consumer sentiment and have been offering EMI sharing schemes and freebies .Going forward, we forecast that prices will increase by 2% in H2 2014 to ₹ 4,500 per sq ft, in view of the recovery in sales volume.

The majority of the recent residential development has taken place in the peripheral micro-markets of Noida, Gurgaon, Ghaziabad and Greater Noida. No new supply has been infused into the Delhi market since the last two years. The Delhi Development Authority's recent approval of the land pooling policy is expected to unlock nearly 40,000 acres of land in the Delhi market. As per the policy, developers may acquire land directly from farmers who are willing to participate in the process, wherein they get back 40–60% of the developed land. This is likely to act as a cooling measure for property prices in the region.

A deep dive into the unsold inventory levels of the NCR is essential in order to comprehend the health of the market. In June 2014, nearly 167,000 residential units remained unsold in the NCR market, growing at a CAGR of 15% since the last three years

FIGURE 3
Launches, Absorption and Price Trend



Source: Knight Frank Research

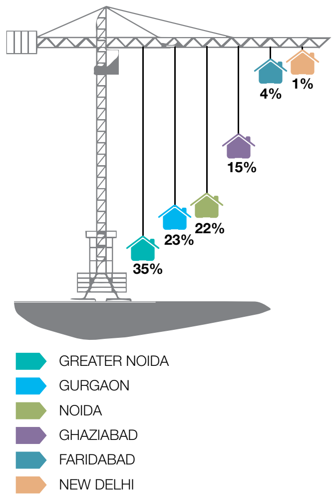
Micro-market-level analysis

Greater Noida and Noida contain more than half of the under-construction units in the NCR market. Both these micro-markets are backed by the on-going robust infrastructure developments. Noida is perceived to be a prime end user market in Uttar Pradesh due to the presence of good physical and social infrastructure, along with proximity to South Delhi and abundant job opportunities. Greater Noida, on the other hand, enjoys the presence of large contiguous land parcels that are ideal for group housing projects. However, as compared to Gurgaon and Noida, the residential market in Greater Noida has been somewhat cautious because of the lack of commercial presence to support the residential supply.

Greater Noida is a planned industrial location, an educational hub and also an affordable housing option. Even though it was primarily developed as an extension of Noida, it is fast evolving as a self-sufficient market. Most of the residential options here are in the affordable segment, thus attracting a lot of buyers. Residential development has come up along the Yamuna Expressway and other locations like Sector Alpha, Gamma, Beta, Chi, Phi and Delta. Greater Noida contributed to about 40% of the units launched in H1 2014, showing a slight de –growth in share as compared to H1 2013. The availability of huge land parcels and reasonable land prices enabled developers to launch projects in the affordable and mid-segment range with a ticket size of less than ₹ 5 million. It is currently positioned as the most affordable residential market in the NCR. Preferred locations for project launches in H1 2014 were along the Yamuna Expressway and Tech Zone IV, in the price range of ₹ 3500–5000 per sq ft.

In terms of absorption, Greater Noida's share in the overall pie remained the same in H1 2014, as compared to the same period last year. However, sales in absolute terms have been showing a downward trend with each passing quarter since Q1 2013. Greater Noida has an unsold inventory of 10 quarters, with an average age of 10 quarters, making it the unhealthiest micro-market compared to the others. Developers have been touting the metro connectivity from Noida City Centre to Greater Noida. However, there has been substantial delay in project clearance, which has impacted buyer sentiment as well. Connectivity with a mass transit public transportation system is crucial for further development of locations like the Yamuna Expressway and other sectors of Greater Noida. Moreover, this slowdown in the market is driven majorly by the high number of project launches and subdued

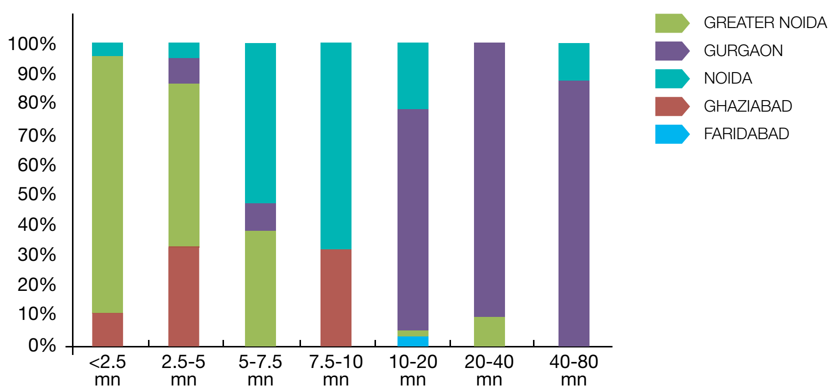
FIGURE 4
Micro-market Split of Under-Construction Units as on June 2014



Source: Knight Frank Research

Greater Noida contributed to about 40% of the units launched in H1 2014, showing a slight de –growth in share as compared to H1 2013

FIGURE 5
Micro-market Level Ticket Size Split of Launched Units During H1 2014



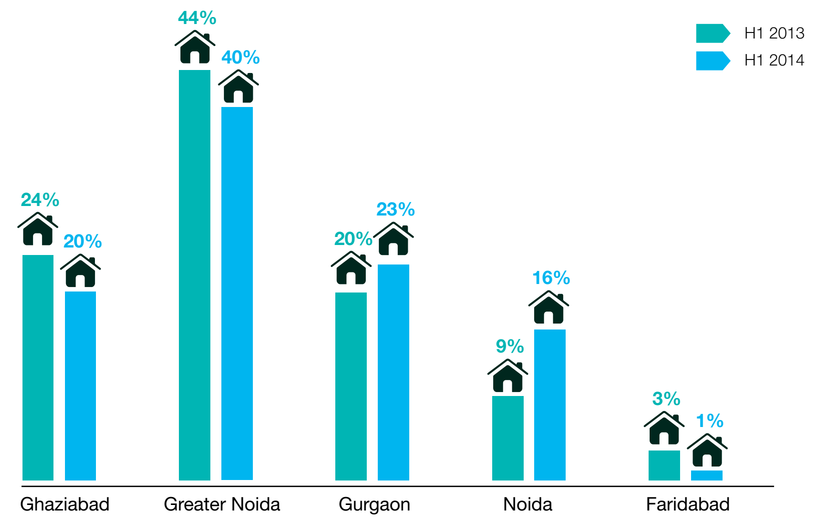
Source: Knight Frank Research

NATIONAL CAPITAL REGION MAP

demand due to the land acquisition row of 2011–12. The resolution of this issue in the latter half of 2012 normalised the market, and demand has picked up substantially. We expect the market to reach a better equilibrium in the next year, with improving sales volumes. Yamuna Expressway is a major hotspot in this particular market, and is attracting a lot of developers. With land availability in Noida becoming limited, this location is touted as the next hub for logistics, warehousing and integrated township development.

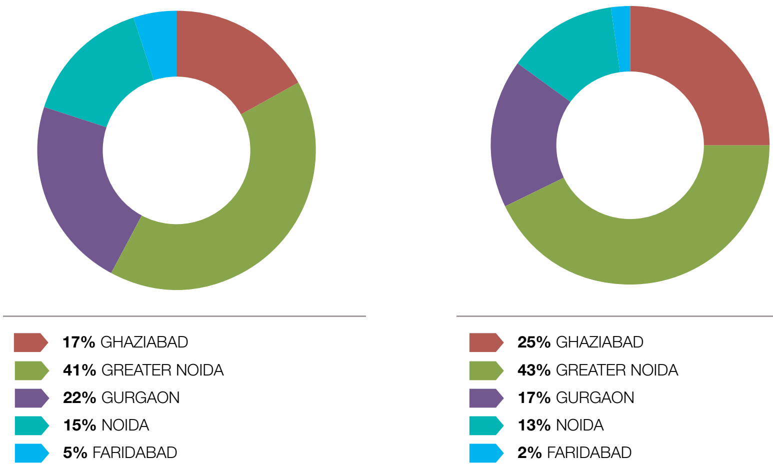
Noida is an outsourcing hub within the NCR. A large number of IT/ITeS companies have set up their bases here. It has also witnessed sufficient traction from the automobile ancillary industry. Most of the residential projects launched in this satellite town are

FIGURE 6
Micro-market split of units launched in H1 2013 and HI 2014



Source: Knight Frank Research

FIGURE 7
Micro-market Split of Absorption in H1 2013 and H1 2014



Source: Knight Frank Research

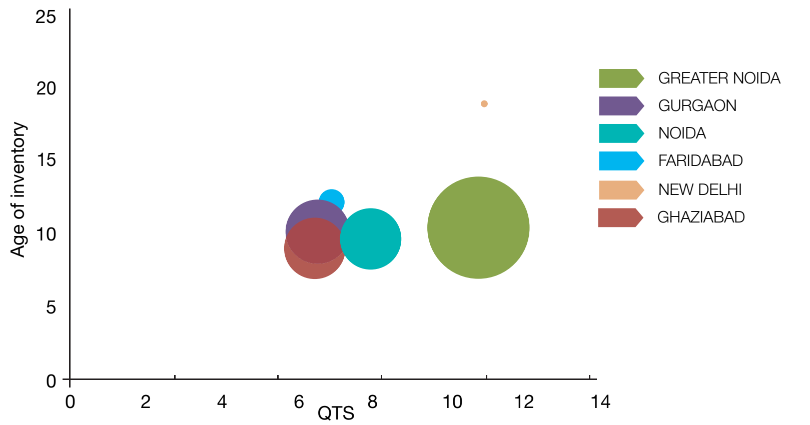
in the mid-segment housing range. Locations like the Noida–Greater Noida Expressway have seen tremendous growth in residential projects, owing to the high demand from commercial and IT/ITeS developments in the vicinity. The presence of employment opportunities, social infrastructure and decent road and mass transit connectivity with other parts of the city has benefitted this market immensely. The fact that this is the only micro-market within the NCR region that offers an array of products across all ticket sizes works in favour of this location. Noida observed its share of new launches increase to 16% in H1 2014, compared to 9% in the same period last year. The majority of the project launches in this micro-market were along the Noida–Greater Noida Expressway, in the price range of ₹ 5,500–7,500 per sq ft. Despite showing an improvement in percentage share, the number of new launches has remained constant in absolute terms. Project launches had bottomed out in H1 2013, primarily due to the limited availability of land parcels for group housing projects. Moreover, the allotment rates of group housing have been raised by 15% in Noida, thus weakening the feasibility of affordable housing options. This, along with the litigation between developers and buyers, consumer agitations and regulatory bottlenecks, has contributed to the reduction in launches in Noida.

Noida's share in the absorption pie has not changed much in H1 2014 compared to H1 2013. However, in terms of absolute volume, there is a steep fall of 45% during the same period. The fact that housing sales took a hit across all micro-markets during H1 2014 because of the weakened sentiment and uncertainty on election outcome confirms that the situation is not exclusive to Noida. The micro-market has an unsold inventory aged 10 quarters, which will take eight quarters to be absorbed.

At 23%, Gurgaon is the second largest micro-market in terms of the quantum of under-construction units in the NCR. The primary developing areas in Gurgaon are Golf Course Extension Road, Southern Peripheral Road, Dwarka Expressway, Manesar and Jaipur Highway. Neemrana, Bhiwadi and Dharuhera are the upcoming residential hubs catering to the affordable housing demand that has been created by the continual industrial development in these locations. Along with being affordable, these projects are offering good infrastructure, public amenities

Noida observed its share of new launches increase to 16% in H1 2014, compared to 9% in the same period last year. The majority of the project launches in this micro-market were along the Noida–Greater Noida Expressway, in the price range of ₹5,500–7,500 per sq ft

FIGURE 8
QTS vs. Age of Inventory across Micro-Markets



Note: The size of the bubble indicates the quantum of unsold inventory

Source: Knight Frank Research

Gurgaon accounted for 23% of the launches in H1 2014, showing a slight increase compared to H1 2013. It is interesting to note that the only premium projects launched in the NCR in H1 2014 have been in Gurgaon, within the price range of ₹ 11,000–14,000 per sq ft, indicating the dominance and demand for the luxury segment

and connectivity options to lure buyers. New infrastructure developments and the presence of prominent builders like DLF, TATA, Unitech, IREO, M3M, Rahejas and Emaar have made Gurgaon one of the favoured residential markets in the NCR, with primarily mid to high-segment projects.

Gurgaon accounted for 23% of the launches in H1 2014, showing a slight increase compared to H1 2013. It is interesting to note that the only premium projects launched in the NCR in H1 2014 have been in Gurgaon, within the price range of ₹ 11,000–14,000 per sq ft, indicating the dominance and demand for the luxury segment. More than 75% of the new launches are above the ticket size of ₹ 10 mn, clearly positioning Gurgaon as a premium market. Sohna is the only location that witnessed project launches in the affordable and mid-segment range within Gurgaon. Unaffordable land prices have pushed developers to consider new locations like Sohna for project launches. More than 20 new sectors are proposed in the master plan of Sohna 2031, one-fourth of which is set aside for residential development. Connectivity with Gurgaon is a major advantage for this upcoming hotspot. This market is expected to emerge as an affordable alternative to Gurgaon, with projects priced at ₹ 4,000–5,500 per sq ft. Home sales in Gurgaon witnessed a drop of 49% in H1 2014, compared to the same period in 2013, largely due to the increasing unaffordability of housing options available in this market. This slowdown in demand has pushed the QTS ratio from 4 to 7 within a span of four quarters. At 28,000 units, Gurgaon market's unsold inventory levels are comparable to those of Noida and Ghaziabad. An analysis of market health based on the QTS and age of inventory suggests that its performance is better than Noida, but worse than the affordable micro-market of Ghaziabad.

Ghaziabad constitutes nearly 15% of the units under construction in the NCR market. Indirapuram, NH 24, Crossings Republic and Raj Nagar Extension are some of the preferred locations for project launches in this micro-market. Ghaziabad accounted for 20% of the new launches in H1 2014, showing a minor dip compared to H1 2013. However, in absolute terms, a steep fall of 54% was observed in residential unit launches during the same period. Primarily an end user market, Ghaziabad has seen consistent demand from home buyers looking for affordable options. Yet, home sales observed a substantial fall in H1 2014, despite a large number of new projects being launched at an affordable ticket size range of ₹ 2.5–5 mn. Since a majority of these projects are located beyond the established residential areas within this micro-market, there is apprehension among home buyers to explore them. Lack of social infrastructure, the absence of mass rapid public transportation systems, distance from work centres and poor access roads are some of the reasons for such trepidation towards these locations. Areas like Lal Kuan, Pratap Vihar and NH 24 Bypass are faced with such challenges and fail to attract buyers.

Although it is a small market in terms of the number of residential units under construction, Faridabad holds an important position. Development in this micro-market is backed by industrial growth. Most of the residential demand is driven by end users. Locations like Old Faridabad, sectors on NH2, Neharpar and Surajkund Road have seen ample residential project launches during the last few years. However, the Faridabad residential market witnessed the steepest drop in both project launches and absorption during H1 2014, compared to H1 2013. The unsold inventory levels are the lowest in the NCR market, but the age of inventory is the highest compared to other micro-markets, clearly indicating a mismatch between the demand and products offered. Developers were over-enthusiastic in launching projects in Faridabad, and demand has been subdued due to lack of drivers. Unlike Noida and Greater Noida, this market observed little demand from corporates with only 3 mn sq ft of operational office space. Project delays have also influenced the negative sentiment for this market, since this is an end user market.

Steady price appreciation is observed across all micro-markets in the NCR in the last 12 months. On the other hand, the preceding six months hardly show any movement in prices due to the sluggish demand. The prices in all the micro-markets of the NCR have increased only marginally, in the range of 1–3% during H1 2014, as compared to H2 2013, with the exception of Raj Nagar Extension. Consistently increasing unsold inventory levels have resulted in such a limited price rise in the first half of 2014. As per our forecasts, the sales volume is expected show some revival in H2 2014. This will aid the upward price movement in H2 2014.

Price Movement in Select Locations

Location	Micro-market	Price Range in H1 2014 (₹/sq ft)	Change since H1 2013*	Change since H2 2013*
Tech Zone IV	Greater Noida	3,300 - 3,500	8%	1%
Yamuna Expressway	Greater Noida	2,800–3,000	3%	1%
Sector Pi	Greater Noida	3,500–3,650	1%	0%
Sector 16B	Greater Noida	3,500–3,650	4%	1%
Sector 93 A	Noida	5,650–5,800	0%	0%
Sector 74	Noida	6,500–6,600	1%	1%
Sector 143 B	Noida	5,600–5,800	2%	1%
Sector 128	Noida	9,000–9,100	2%	0%
Sector 66	Gurgaon	11,000–12,000	1%	0%
Sector 49	Gurgaon	11,000–12,000	5%	0%
Sector 37D	Gurgaon	6,350–6,400	0%	0%
Sohna (Sector 5)	Gurgaon	4,000–4,1000	0%	0%
Indirapuram	Ghaziabad	3,600–4,200	2%	1%
NH 24	Ghaziabad	3,050–3,200	8%	0%
Raj Nagar Extension	Ghaziabad	2,800–3,000	10%	6%
Mathura Road	Faridabad	6,600–6,800	3%	0%
Suraj Kund	Faridabad	8,000–8,500	1%	0%
Sector 82	Faridabad	4,250–4,400	1%	0%

*Change in weighted average prices

Source: Knight Frank Research

Key Takeaways

New launches shrunk by nearly 43% in H1 2014, compared to H1 2013, and stood at 35,500 units. However, absorption levels also witnessed a 37% drop during the same period, thus preventing the QTS ratio from going down

As per our forecasts, new launches will increase by 10% to 37,000 units in H2 2014, compared to H2 2013. Absorption is forecasted to increase by 17% to 30,500 units in H2 2014, compared to the same period in 2013

In June 2014, nearly 167,000 residential units remained unsold in the NCR market, growing at a CAGR of 15% since the last three years

Going forward, we forecast the prices to increase by 2% in H2 2014 to ₹ 4,500 per sq ft, in view of the recovery in sales volume

Greater Noida has an unsold inventory of 10 quarters, with an average age of 10 quarters, making it the unhealthiest micro-market compared to the others

At 28,000 units, Gurgaon market's unsold inventory levels are comparable to those of Noida and Ghaziabad. An analysis of market health based on the QTS and age of inventory suggests that its performance is better than Noida, but worse than the affordable micro-market of Ghaziabad

OFFICE MARKET

National Capital Region (NCR) Analysis

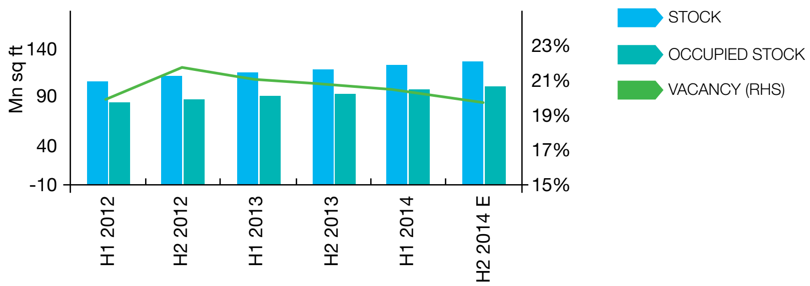
Improved global economy, conclusive election results and a clear appetite for office space prepares the NCR office market for an eventful 2014

The office market of the National Capital Region (NCR) is a unique agglomeration comprising Delhi, Gurgaon, Noida, Greater Noida, Faridabad, Ghaziabad and other adjoining peripheral urban areas. While the Delhi market has evolved gradually over the years, the peripheral markets of Gurgaon and Noida have grown rapidly in a relatively short span of time to accommodate the domestic and international office demand. Being the seat of political power, Delhi is undoubtedly the nucleus of the national capital, and riding on the luxury of the Greenfield land at its disposal, the city's

peripheral business districts (PBDs) are offering occupiers a range of options to set up base in this prime office market of India.

NCR currently has a total office stock of 122 mn sq ft, of which 96.5 mn sq ft is occupied. Past analysis shows that vacancy levels in the national capital peaked in 2011 due to an addition of 12 mn sq ft of newly-completed projects, which caused them to spike at 21%, from 18% in 2010. Moving in close range ever since, the vacancy levels continued this trend and settled at 20.5% in the first half of 2014. Going forward, limited new completions and an increase in demand for office space are likely to push the vacancy levels down to 20% in H2 2014.

FIGURE 1
Office Space Stock and Vacancy

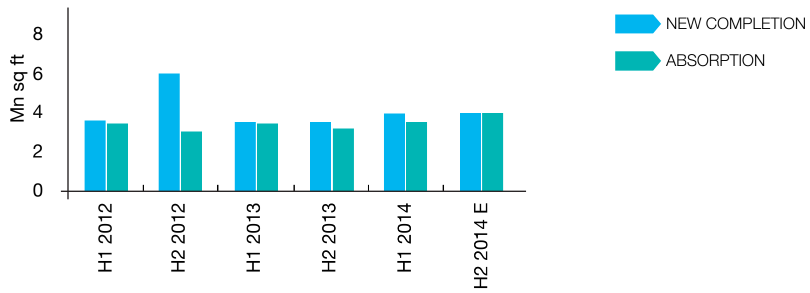


Source: Knight Frank Research

Micro-markets	Location
Central Business District (CBD), Delhi	Connaught Place, Barakhamba Road, Kasturba Gandhi Marg, Minto Road
Secondary Business District (SBD), Delhi	Nehru Place, Saket, Jasola, Bhikaji Kama Place, Mohan Cooperative area, Aerocity
Peripheral Business District (PBD), Gurgaon	DLF Cyber City, MG Road, Sohna Road, Golf Course Road, Dundahera, Manesar, NH 8, Udyog Vihar
Peripheral Business District (PBD), Noida	Sector 16, 18, 62, 63, Greater Noida Expressway
Peripheral Business District (PBD), Faridabad	Mathura Road

Improved global economy, conclusive election results and a clear appetite for office space prepares the NCR office market for an eventful 2014

FIGURE 2
New Completion and Absorption



Source: Knight Frank Research

Having already indexed 3.5 Mn sq ft of office space in H1 2014, Knight Frank estimates the overall absorption levels in 2014 to plug at 7.5 Mn sq ft, hitting a high of four years

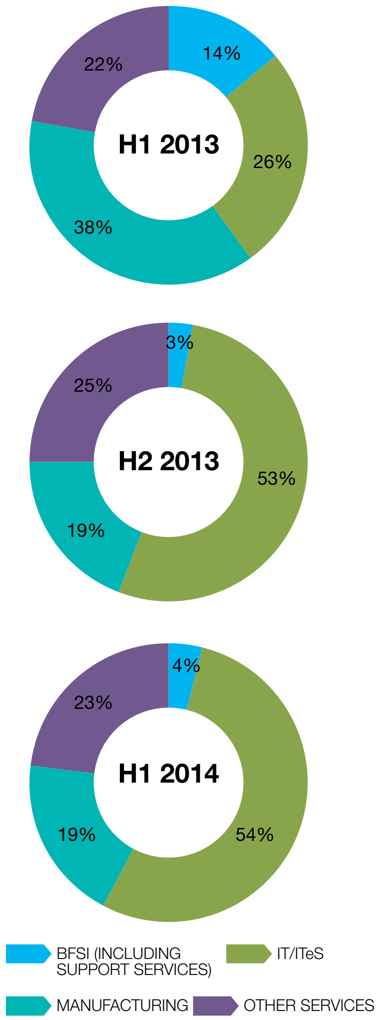
Having already indexed 3.5 Mn sq ft of office space in H1 2014, Knight Frank estimates the overall absorption levels in 2014 to plug at 7.5 Mn sq ft, hitting a high of four years.

The tone for a good business market was set in the second half of 2013, when the world watched India gear up for the general elections. Riding on the optimism of a reviving macro-economic scenario and hopes of a decisive new government, 2 mn sq ft of office space was absorbed in Q1 2014, followed by another 1.5 mn sq ft in Q2 2014, tallying the NCR absorption levels at 3.5 mn sq ft at the end of June 2014. In terms of new completions, approximately 4 mn sq ft of new office space entered into the market in H1 2014, all of which was centred in Gurgaon, whereas projects in the Delhi SBD and Noida PBD failed to keep their respective timelines. The year ahead looks bright, with the markets riding high on post-election and budget sentiments. As per our forecast, we see approximately 4 mn sq ft of office space demand in the second half of 2014 compared to 3.3 mn sq ft in H2 2013.

Of the total absorption in H1 2014, IT/ITeS, the primary driver of the NCR office space, shows an absorption of 1.8 mn sq ft, which is 54% of the overall NCR market. Trends suggest that the IT/ITeS sector monopolises absorption levels in the NCR office market on a year-on-year (Y-O-Y) basis, indicating sound occupier sentiments for the region. Except for the dampener in H1 2013, when the percentage share of the IT/ITeS sector dropped to 26%, the sector has been improving gradually from the preceding quarters. This improvement in the IT/ITeS absorption trends comes in the wake of the gradual economic revival in the United States, along with the fact that European companies are moving towards the offshoring model, thus creating opportunities for the expansion of IT companies. The availability of large floor plates, good infrastructure and affordable housing options has made NCR a favourite for IT/ITeS companies. The year so far has not only proved well for the sector in terms of transacted space but also in the number of deals, which registered a 36% jump from 22 closures in H1 2013 to 30 in H1 2014, with 63% of the deals being below 25,000 sq ft. Some of the major companies taking up sizable spaces include Aricent, TCS, Accenture and Oracle. The sector has set the tone for a prolific 2014, and is expected to perform even better with an anticipated increase in global technology spending and with IT/ITeS companies projecting revenue growth in the coming quarters of 2014.

Unlike IT/ITeS, the manufacturing sector share in NCR has shown erratic trends. During January –June 2014, the sector had leased 0.6 mn sq ft of office space, which is 19% of the overall NCR absorption. The percentage share of manufacturing sector in H1 2014 matched that of H2 2013, but saw a visible drop from the sector's best of a 38% share in H1 2013. Sluggish domestic demand, coupled with project lags due to government policies like the land acquisition issues, has hampered the confidence levels of the industry. Probing further, 90% of the deals in the manufacturing sector involved office space under 25,000 sq ft, with an average transaction size of 15,000 sq ft, which is a significant drop from the average deal size of 30,000 sq ft in H1 2013 and 2012. However, though the maximum demand in H1 2014 was for office space less than 25,000 sq ft, the sector did

FIGURE 3
Sector-wise Absorption Split



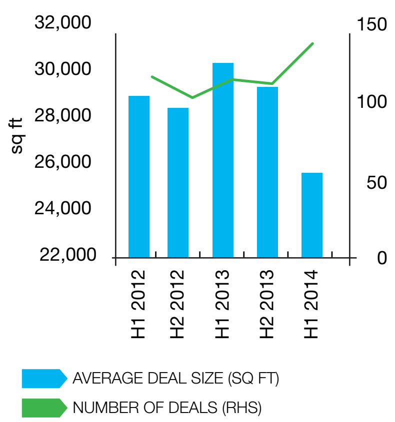
see heavyweights like, Media Tek taking up substantial space. In the second half of 2014, the sector is expected to pick up from the current discouraging levels, given the government's budgetary intentions to revive the industry and increase domestic demand through investment and policy interventions.

Maintaining a steady pace, the other services sector absorbed 0.8 mn sq ft in H1 2014 or 23% of the overall NCR pie – a slight increase from the 22% share in H1 2013. It is interesting to note that even though this sector is dominated by conventional media, consulting and advertising companies, the emergence of the start-up and e-Commerce culture in India is making its presence felt by the growth of this sector. H1 2014 saw a rise in the number of deals, from 43 closures in H1 2013 to 57 in H1 2014, with 87% of the deals settling for less than 25,000 sq ft. The control of conventional domains continued to manifest itself with significant floor plates being taken up by companies like Copal Partners, Gurgaon, JWT and News Nation, while eCommerce made its presence felt in the absorption tally by leasing from companies like Snapdeal, Zomato, Myntra, Yepme and Shopclues.

BFSI has been the worst performer in office leasing during H1 2014. The share of the banking sector in terms of transacted space has dropped to 4% compared to the same period in 2013 and 2012, with only RDB Insurance absorbing 1 lakh sq ft. The current share could see a rise in the coming quarters if the opinions on new licenses and expansion plans for various financial institutions take shape.

On further analysis of the NCR absorption levels, it is noted that though the demand for office space of less than 25,000 sq ft continued to dominate the market like the preceding quarters of 2013, there was a drop in the average deal size, from 30,000 sq ft in H1 2013 to 25,000 sq ft in H1 2014. However, it is seen that the sheer number of transactions have substantially gone up to 137 in H1 2014 compared to 114 in H1 2013. A few large-size transactions like Aricent, TCS, and Oracle added to the absorption tally by taking up sizable spaces in Gurgaon and Noida.

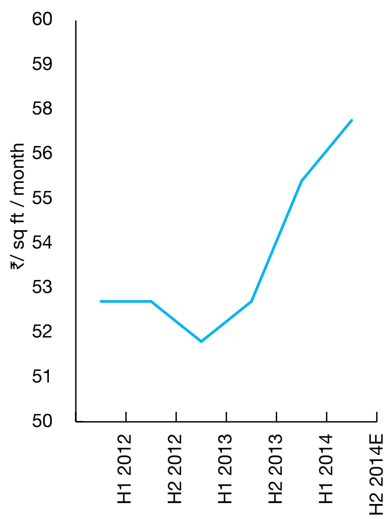
FIGURE 4
Deal Size Analysis



Source: Knight Frank Research

The weighted average rentals in the first half of 2014 peaked at ₹ 56 per sq ft, surpassing the preceding quarters of 2013 and 2012. A rental appreciation of 8% was caused by limited influx of new completions in 2013, H1 2014, and high-asking rentals in old prime markets like CBD Delhi and Cyber City, Gurgaon. Riding on these factors, the market will continue to show an uptick in rents, and will appreciate to ₹ 57.5 per sq ft in H2 2014. The current spike in rent has caused occupiers to consider options in the peripheral markets that not only offer competitive rentals but also promising infrastructure and matched quality standards.

FIGURE 5
Weighted Average Rental Movement (₹/sq ft/month)



Source: Knight Frank Research

Cashing in on this sentiment, the PBDs of Gurgaon and Noida are extending their infrastructure plans to their respective sub-markets, and we even foresee a city like Faridabad increasing its share in the NCR office pie two years from now.

BUSINESS DISTRICTS OF NCR

Business District Analysis

The NCR office market can be classified broadly into five business districts that possess their distinctive occupier and supply profiles.

Business District-wise Rental Movement

Business District	Rental Value Range in H1 2014 (₹/sq ft /month)	12-month change	6-month change
CBD - Delhi	200 - 350	2%	1%
SBD - Delhi	90 - 140	5%	1%
PBD Gurgaon Zone A	90 - 130	6%	2%
PBD - Gurgaon Zone B	55 -80	4%	1%
PBD - Gurgaon Zone C	25 - 35	-	-
PBD - Noida	40 - 60	4%	1%
PBD - Faridabad	45 - 55	-	-

Source: Knight Frank Research

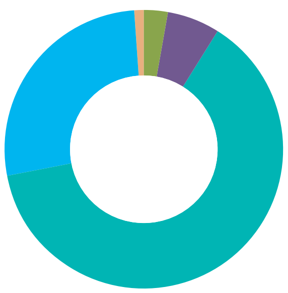
CBD - Delhi is the oldest and prime office market in NCR as well as the whole country, and encompasses an office stock of 7 mn sq ft. In H1 2014, the percentage share of office space absorption in the CBD dropped, to a dismal 1% from 3% in H1 2013. Limited new completions, small floor plates have pushed the rentals in the range of ₹ 200 - 350 per sq ft and are encouraging occupiers to look for alternate markets. However, despite the steep rentals, companies that give more weightage to location and presence would still prefer an office in the CBD. Some companies have their front offices in the CBD, while their back offices are located in the SBD due to the availability of a range of floor plate options that command comparatively low rentals. As mentioned earlier, CBD Delhi is a mature office market, characterised by old construction buildings, leaving limited scope for new developments. In H1 2014, most transactions were seen in the newly constructed DLF Capitol Point, with companies like JP Morgan, Hannover Re and Ratnakar Bank taking up small office spaces.

The SBD of Delhi, comprising Jasola, Saket, Mohan Cooperative, Nehru Place, Saket and Vasant Kunj, has 17 mn sq ft of operational office stock. Due to its proximity to Delhi, the SBD saw rapid growth in terms of infrastructure development, making it the second most popular option for occupiers scouting to set base in the capital. The percentage share of the SBD in the overall NCR market has shown an increase with a 8% market share in H1 2014 compared to 6% in the same period of 2013. This absorption of 0.3 mn sq ft in this half of 2014 is a marked 33% increase from the same period in 2013, including transactions with companies like LG, Rostfrei, Triumph Bikes, Moser Baer and Snapdeal. The other services sector saw tenant leasing from companies like DEN Networks and Publicis, among others. Rental trends showed a 5% increase from the same period in 2013, moving in the range of ₹ 90 - 140 per sq ft. This rent appreciation is seen to stabilise around the same level by the end of 2014

Stylish office buildings, upscale condos and steady infrastructure developments characterise Gurgaon as the hub for white-collar managers. Coming a long way from 1997, Gurgaon is the first choice for global companies wanting to set up operations in India. It saw an

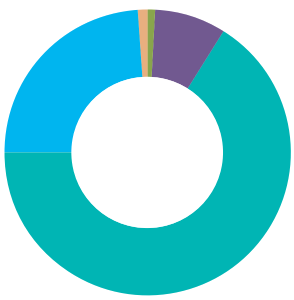
Gurgaon is the first choice for global companies wanting to set up operations in India. It saw an absorption of 2.3 mn sq ft in the first half of 2014, and took up a 66% share in the overall NCR office pie

FIGURE 6
Business District-wise Absorption Split in H1 2013



Source: Knight Frank Research

FIGURE 7
Business District-wise Absorption Split in H1 2014



Source: Knight Frank Research

PBD Gurgaon Zones	Location
PBD - Gurgaon Zone A	MG Road, NH 8, Golf Course Road, Golf Course Extn. Road
PBD - Gurgaon Zone B	Cyber City, Sohna Road, Udyog Vihar, Gwal Pahari
PBD - Gurgaon Zone C	Manesar

absorption of 2.3 mn sq ft in the first half of 2014, and took up a 66% share in the overall NCR office pie. This 7% increase in transacted space from the same period in 2013 was complemented by an increase in the number of deal closures from 74 in H1 2013 to 86 in H2 2014. The increased deals in this half has pushed down absorption levels but also compressed the average deal size from 29,000 sq ft in H1 2013 to 27,000 sq ft in H1 2014. The occupier profile was dominated by the IT/ITeS sector yet again, which took up 58% of Gurgaon's total transaction volume. Currently, this PBD of NCR has a ready stock of 68 mn sq ft, making it vital to discuss it in detail. Based on the dominance of commercial office spaces, Gurgaon's PBD has been sub-divided into three broad zones, as follows:

Zone A comprises MG Road, Golf Course Road and Golf Course Extension Road, and predominantly has commercial office spaces suited for corporates. MG Road, the oldest office space zone in Gurgaon, now has negligible new supply. Hence, the rentals in the existing stock range between ₹ 90–130 per sq ft and continue to spike with every new transaction. On the other hand, with the advantage of good connectivity and abundant residential options, Golf Course Road has seen the maximum number of transactions in Zone A in the current half. The construction work of various infrastructure projects like the metro extension are giving further impetus to this office zone, which, coupled with the budding Golf Course Extension, is attracting occupiers from various sectors. However, Zone B, comprising Cyber City, Udyog Vihar and Sohna Road, has a different story to tell. The occupier profile of this zone is dominated by the IT/ITeS sector due to the availability of large floor plates. According to insights several companies in Cyber City are up for lease renewal in 2014, and occupiers who had started with a rent of ₹ 35–45 per sq ft nine years ago are now reluctant to pay the current market rents of ₹ 75–80 per sq ft. The current asking rentals in Cyber City are particularly driving IT/ITeS companies that are seeking large floor plates to seek locations like Sohna Road and Golf Course Extension Road. Sensing this movement, rents in Sohna Road saw an average 3 - 4% appreciation on a Y-O-Y basis. In the coming quarters, though there will be moderate tenant reshuffling in Cyber City, it will continue to uphold its prominence as an important office address and be patronised by consulting, media and corporate heavyweights. On the other hand, key considerations like connectivity, low rents, matched quality office spaces and congestion-free transit for employees will drive transaction movement towards other sub-markets in Zone B. No traction was seen in Zone C in the current half of 2014.

Noida did not see much leasing activity in H1 2014. The total absorption levels stood at 0.8 mn sq ft, coming close to the demand in the same period in 2013, but then registering a decline in the market share that dropped to 24% in 2014 from 27% in 2013. Noida currently has a 22 mn sq ft of operative office stock, with rentals moving in the range of ₹ 40–60 per sq ft. IT/ITeS sector saw a 70% increase in its share of office space absorption with companies like TCS, Adobe and NEC Technologies at the forefront. Apart from IT/ITeS companies, other companies that transacted space in Noida are Media Tek, RDB Insurance, News Nation and Yamaha.

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Faridabad, a relatively new entrant into the NCR office space, is creating a buzz with infrastructure developments like the 4.4-km Badarpur Skyway, the under-construction Delhi Metro and the six-laning of the Delhi–Faridabad–Agra Highway, making it important to discuss this market. Presently, Faridabad is perceived as an industrial town, with only 3 mn sq ft of office stock. This picture is slowly set to change, with reputed developers and brands like Vatika, Crown Group, Piyush Group and Radisson Blu planning office and hospitality projects along Mathura Road. The trends hint that the market, though not overly bullish, is positive about the future of this peripheral town, which is reinforced by recent land deals. However, it is maintained that the actual turnaround of Faridabad as an office market will be dependent largely on the performance of Gurgaon and Noida, which not only dominate the existing office market but also boast of a robust office pipeline for NCR.

Select Transactions in NCR Office Market

Building	Occupier	Business District	Area leased (sq ft)
DLF IT Park	TCS	PBD - Noida	420,000
Plot 112	ShopClues	PBD - Gurgaon	25,000
DLF Capitol Point	JP Morgan	CBD - Delhi	1,900
Enkay Centre	JWT	PBD - Gurgaon	40,400
DLF Silokhera	WNS	PBD - Gurgaon	150,000
A-31	RDB Insurance	PBD - Noida	108,000
Plot 139	Zomato	PBD - Gurgaon	45,200
ABW Towers	Myntra	PBD - Gurgaon	13,770
Gys Universal	Adobe	PBD - Noida	25,000
DLF Silokhera	Edifecs	PBD - Gurgaon	27,000
S B Tower	Media Tek	PBD - Noida	30,000
DLF Capitol Point	Hannover re	CBD - Delhi	3,000
Okhla Ph-3	Snapdeal	SBD - Delhi	50,000
Plot 267	Copal Partners	PBD - Gurgaon	120,000
DLF World Tech Park	Edifecs	PBD - Gurgaon	120,000
Hines One Horizon	Oracle	PBD - Gurgaon	100,000

Source: Knight Frank Research

Key Takeaways

Encouraging global and domestic trends, coupled with limited new completions, drove NCR absorption levels to 3.5 mn sq ft, in H1 2014

We forecast H2 2014 to absorb 4 mn sq ft, of office space, plugging 2014 absorption levels at 7.5 mn sq ft

Rental appreciation of 8% in H1 2014 moves office rents to ₹ 56 per sq ft from ₹ 52 per sq ft in 2013

A preference for small and mid-size office space was observed in H1 2014. More than three fourth of the deals were less than 25,000 sq ft

PBD - Gurgaon improved its share in the NCR office market, taking up 66% of the total absorption in H1 2014 compared to 63% in 2013

IT/ITeS outperformed other sectors, taking up 54% of the total transaction volume in the NCR in H1 2014

Riding on the eCommerce and start-up boom in India, eRetail companies saw significant transactions from occupiers like Myntra, Snapdeal and Zomato

PUNE

RESIDENTIAL MARKET

Metropolitan Region Analysis

The Pune residential market has been witnessing a downward trend in terms of demand for homes since the beginning of 2013, and this momentum seems to have continued in 2014 as well. While the demand for homes dropped by over 19% in 2013, it is expected to fall by 11% in 2014. The total number of units to be absorbed is expected to fall from 38,800 in 2013 to 34,500 in 2014. However, a fall in absorption is expected to be complemented by a sharper drop in the number of new launches during the year. New launches are estimated to decrease by 21% from 45,370 units in 2013 to 35,840 units in 2014.

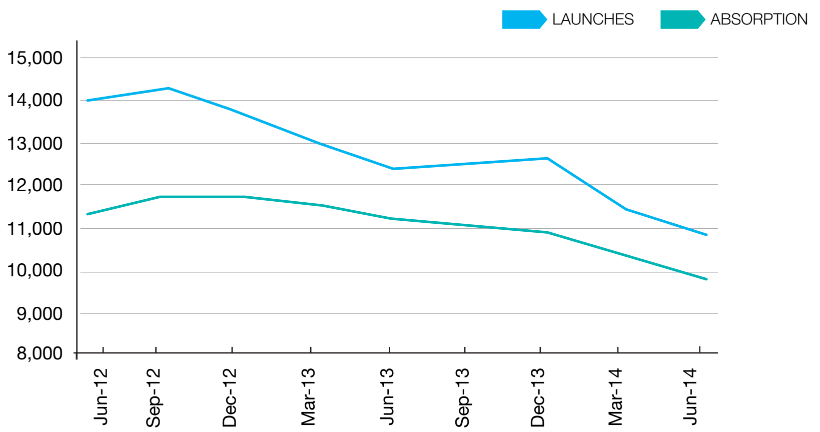
Comparing the absolute numbers of absorption and new launches on an annual basis is not sufficient to understand the health of a market or its impact on price. Since demand and supply are influenced by various other independent factors, such as economic growth, market sentiment, interest rate and income growth, among others, an annual rise or fall in demand and supply could be misinterpreted as a sign of a strong or weak market. Hence, with the aim of removing seasonality from the data, we have analysed the long-term moving average (eight quarters) trend in absorption and new launches. The following chart clearly indicates a falling trend in both absorption and launches since June 2012. Interestingly, the rate of fall in new launches is far greater than the fall in absorption since December 2013. The correction in the market has been led primarily by developers who have refrained from launching new projects during the last six months after witnessing a decelerating trend in sales volumes for over two years in a row.

While the analysis of absorption and new launches could provide a fair idea with respect to the traction being witnessed in the market, the impact on price cannot be understood without studying the unsold inventory available in the city. Hence, we have calculated the Quarters to Sell Unsold Inventory (QTS), which can be explained as the number of quarters required to exhaust the existing unsold inventory in the market. The existing unsold inventory is divided by the average sales velocity of the preceding eight quarters in order to arrive at the QTS number for that particular quarter. A lower QTS indicates a healthier market.

The QTS ratio for Pune has been

The demand for homes is expected to decrease from 38,800 units in 2013 to 34,500 units in 2014 resulting in a fall of 11%. However, a fall in absorption is expected to be complemented by a sharper drop in the number of new launches that are estimated to decrease by 21% from 45,370 units to 35,840 units during the same period

FIGURE 1
Long-term (Eight Quarters) Moving Average Trend of Launches and Absorption



Source: Knight Frank Research

The QTS ratio for Pune has been inching upwards since September 2013, signifying weakness in the market. The large number of new launches during H2 2013, despite slowing sales volumes in H1 & H2 2013, pushed the QTS to a higher level

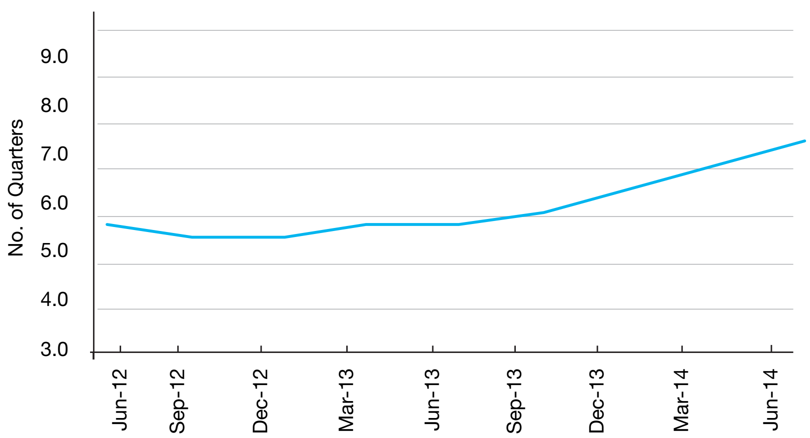
inching upwards since September 2013, signifying weakness in the market. The large number of new launches during H2 2013, despite slowing sales volumes in H1 & H2 2013, pushed the QTS to a higher level. While the sales volume dropped by 15% from 20,940 units in H1 2013 to 17,860 units in H2 2013, new launches increased by 19% from 20,720 units to 24,650 units during the same period. This led to a surge in unsold units in the city, resulting in an imbalance between the demand and supply equilibrium. The developer community seems to have taken cognizance of such an imbalance and reduced new launches drastically by 32% during H1 2014, compared to H2 2013. However, such a course correction has not directly resulted in bringing down the QTS ratio, as the sales volume declined further by 18% during H1 2014 to 14,720 units.

We expect another six to nine months for the Pune market to offload its excess unsold inventory and the QTS ratio to fall back to its 2013 level. The election results, revival of manufacturing activity, higher salary growth of IT/ITeS employees and various sops announced in the Union Budget of 2014 seem to have induced a positive change in the home buyer sentiment. The conversion time between a sales inquiry and an actual sale has reduced drastically in the past month, indicating some sort of revival in demand. We expect the sales volume to recover from H2 2014 onwards, after a lull of more than two years. Absorption is forecasted to increase by 35% to 19,800 units in H2 2014, compared to H1 2014. Similarly, it is estimated to increase by 11% from H2 2013 or the preceding twelve-month period.

The bumpy ride in demand and supply does not seem to have any significant impact on price levels in the city as prices continue to move upwards, albeit at a slower pace. The weighted average residential price in Pune has increased by 6% from ₹ 4,350/sq ft. in H1 2013 to ₹ 4,600/sq ft. in H1 2014. The rising cost of input materials and the sharp fall in new launches have aided in maintaining such a trajectory in prices. Going forward, we forecast the prices to increase by 4% in H2 2014 to ₹ 4,700/sq ft. on the back of a moderate recovery in sales volume.

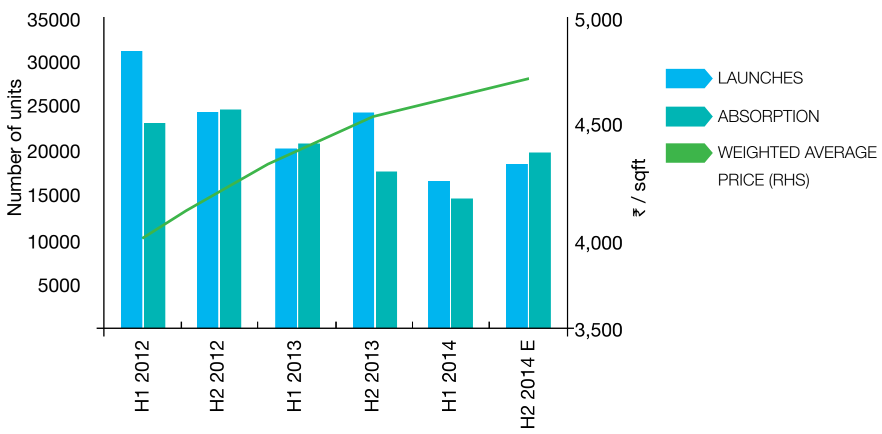
The progress on all the major infrastructure projects in the city, such as the Pune Metro, Pune International Airport and Pune Outer Ring Road, has been lacklustre. Although the metro rail project has witnessed some traction in the past few months with the proposal to form a Special Purpose Vehicle (SPV), tangible progress at the ground level is still missing. The airport and outer ring road projects are still at the pre-feasibility study level and hence, we do not expect any concrete benefits arriving out of these projects during 2014.

FIGURE 2
Quarters to Sell Analysis



Source: Knight Frank Research

FIGURE 3
Launches, Absorption and Price Trend



Source: Knight Frank Research

Micro-market Analysis

The Pune residential market can be broadly classified into five micro-markets, with locations within each micro-market sharing similar characteristics in terms of price, quality of projects, buyer segment, infrastructure development and distance from the city centre.

Micro-markets	Locations
Central	Koregaon Park, Boat Club Road, Erandwane, Deccan, Kothrud, Model Colony
East	Viman Nagar, Kharadi, Wagholi, Hadapsar, Dhanori
West	Aundh, Baner, Wakad, Hinjewadi, Bavdhan, Pashan
North	Pimpri, Chinchwad, Moshi, Chikhali, Chakan, Talegaon
South	Kondhwa, Ambegaon, Undri, Dhayari, Warje, Sinhgad Road

The residential market of Pune is fairly divided across the four zones (north, south, east and west) in terms of launches and absorption, with the exception of central Pune. During H1 2014, central Pune accounted for only 1% of the total new launches, as unaffordable prices, high unsold inventory and unavailability of vacant land deterred developers from launching new projects. Therefore, the focus of our analysis has been limited primarily to the other four micro-markets of the city. Some of the prominent projects recently launched in central Pune are Devkunj by Pandit Javdekar Developers on Prabhat Road and Anant Rukmini by Dajikaka Gadgil Developers in Kothrud.

South Pune has witnessed a phenomenal jump in terms of new launches during H1 2014, with its share increasing from

We expect the sales volume to recover from H2 2014 onwards, after a lull of more than two years. It is forecasted to increase by 35% to 19,800 units in H2 2014, compared to H1 2014. Similarly, it is estimated to increase by 11% from H2 2013

PUNE METROPOLITAN REGION MAP

21% to 36%. South Pune is slowly emerging as a preferred destination for home buyers in Pune due to its strategic location between the two major IT/ITeS employment hubs of Hinjewadi in the west and Kharadi in the east, with areas like Kondhwa, Ambegaon, Undri and Dhayari equidistance from both. Additionally, property prices are relatively cheaper in the south, compared to the west and east. During H1 2014, 96% of the new units launched in south Pune were below the ticket size of ₹ 5 mn compared to 66% and 73% in west Pune and east Pune respectively. These factors have attracted the attention of developers towards the south, since they are facing sluggish sales volumes in the other micro-markets of the city. The Leaf by Kothari Brothers at Kondhwa, Godrej Prana by Godrej Properties at Undri and Vertical Alcinia by Vertical Infra at Mohammadwadi are some of the new projects launched during H1 2014 in south Pune.

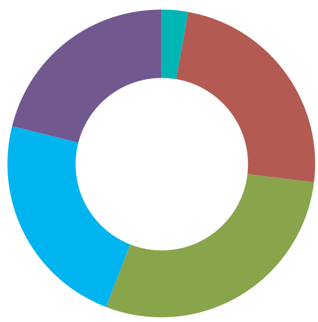
West Pune observed the sharpest fall in new launches during H1 2014, as developers curtailed launching fresh projects on the back of lacklustre demand and poor response received by the various projects launched during H2 2013. The micro-market seems to be facing price resistance from home buyers, as a majority of the locations have already breached the psychological price point of ₹ 5,000/sq ft. Wish Towers by Aditya Builders at Baner and Siyona by Pethkar Projects at Punawale are some of the new projects launched during H1 2014. East and north Pune have been able to maintain their share in the new launches during the last six months. Nyati Elan by Nyati Group at Wagholi and Song of Joy by Gera Developers at Kharadi are a few select projects launched in east Pune, while Kesar Kingdom by Kesar Group at Dighi and Padmanabh by Darode Jog Properties at Moshi are some of the projects launched in north Pune during H1 2014.

On the absorption front, central Pune has been able to maintain its momentum during H1 2014, although it is insignificant in terms of absolute numbers. Locations like Kothrud, Deccan and Erandwane are witnessing renewed traction since H2 2013, and such a trend is expected to continue even in 2014. West and east Pune have observed the steepest fall in absorption during H1 2014, despite a large number of new projects being launched at a relatively affordable ticket size range of ₹ 2.5 – 5 mn. Since a majority of these projects are located beyond the established residential areas, there is apprehension among home buyers to explore them. Lack of social infrastructure, absence of mass rapid public transportation systems, distance from the city centre and poor access roads are some of the reasons for such apathy towards these locations. Areas like Pirangut and Bavdhan in west Pune, and Wagholi, Dhanori, Phursungi and Handewadi in east Pune have witnessed dampened sales volumes because of such challenges. The north and south Pune markets have fared relatively better in terms of absorption, compared to the west and east.

Comparing these micro-markets in

South pune is slowly emerging as a preferred destination for home buyers in Pune due to its strategic location between the two major IT/ITeS employment hubs of Hinjewadi in the west and Kharadi in the east, with areas like Kondhwa, Ambegaon, Undri and Dhayari equidistance from both

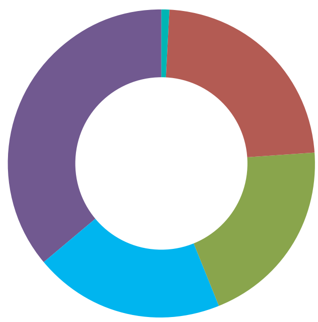
FIGURE 4
Micro-market Split of Units Launched in H1 2013



3% CENTRAL
24% EAST
29% WEST
23% NORTH
21% SOUTH

Source: Knight Frank Research

FIGURE 5
Micro-market Split of Units Launched in H1 2014

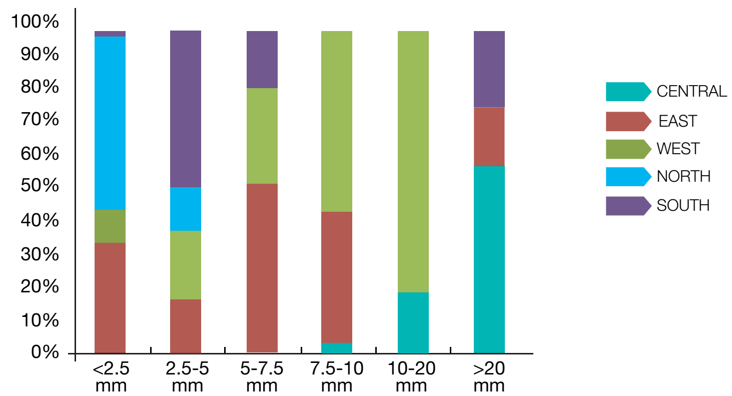


1% CENTRAL
23% EAST
20% WEST
20% NORTH
36% SOUTH

Source: Knight Frank Research

FIGURE 6

Micro-market Level Ticket Size Split of Launched Units During H1 2014



Source: Knight Frank Research

terms of the number of launches and absorption does not reflect the true picture pertaining to the health of the market. Hence, we have developed a model that captures the relative health of micro-markets by taking into account demand, supply and the age of unsold inventory. The age of unsold inventory is the number of quarters that have passed since the inventory entered the market. A higher age of unsold inventory indicates that a large number of old projects continue to remain unsold.

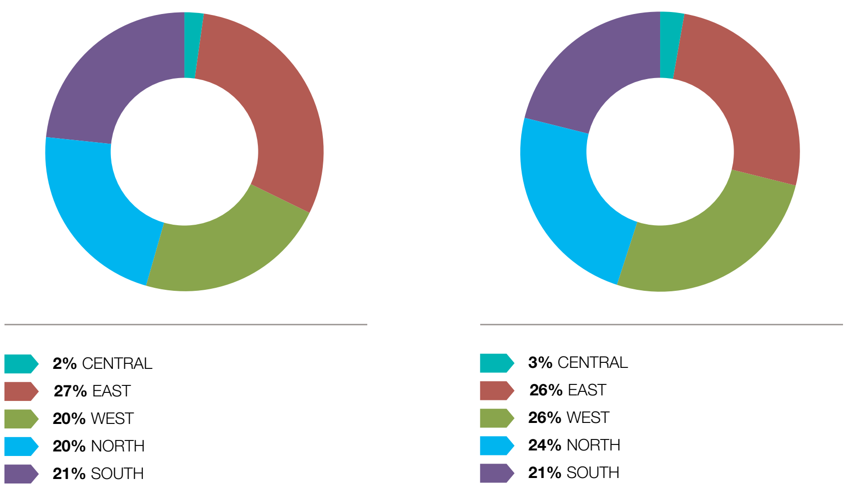
The relative health of each micro-market in Pune can be inferred from the figure 8. Currently, west Pune is the healthiest micro-market, as it has the lowest QTS and minimum age of unsold inventory. Hence, despite west Pune witnessing the sharpest fall in absorption, the health of the micro-market is relatively better because the drop in absorption was matched by a similar fall in new launches. Moreover, the age of unsold inventory is considerably less in this micro-market, as compared to the others. South Pune's health is the poorest, as it continues to carry the excess unsold inventory of projects that were launched more than two years ago. This problem has been compounded by the sharp increase in new launches during H1 2014.

Prices in the majority of the locations across Pune have witnessed a steady

West Pune observed the sharpest fall in new launches during H1 2014, as developers curtailed launching fresh projects on the back of lacklustre demand and poor response received by the various projects launched during H2 2013

FIGURE 7

Micro-market Split of Absorption in H1 2013 and H1 2014

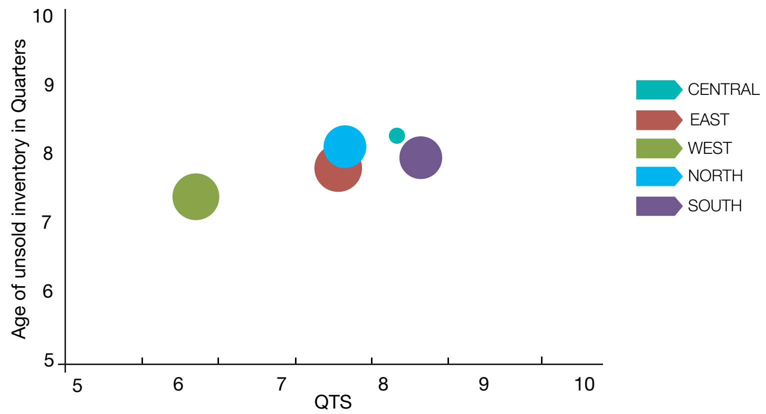


Source: Knight Frank Research

appreciation in the last 12 months. But the momentum seems to have been broken in the preceding six months, except for certain locations in central Pune. Restricted supply, better infrastructure and the high aspirational quotient attached to this micro-market will continue to push prices upwards in various locations across central Pune, despite sluggish demand. Prices in the other four micro-markets of Pune have increased only marginally, in the range of 1-3% during H1 2014, as compared to H2 2013. The significant build-up in unsold inventory and the availability of a large number of ready possession apartments have resulted in such a limited price rise in the first half of 2014. However, we expect this to change in the coming months, as green shoots of revival in demand are already being observed in the city, and this could result in prices continuing to move upward from H2 2014 onwards.

FIGURE 8

QTS vs. Age of Inventory Across Micro Markets



Note: The size of the bubble indicates the quantum of unsold inventory

Source: Knight Frank Research

Price Movement in Select Locations

Location	Micro-market	Price range in H1 2014 (₹/sq ft)	Change since H1 2013*	Change since H2 2013*
Koregaon Park	Central	13,000 - 17,000	8%	5%
Boat Club Road	Central	14,000 - 19,000	1%	0%
Wagholi	East	3,400 - 4,500	4%	2%
Hadapsar	East	4,500 - 5,800	10%	3%
Aundh	West	7,500 - 9,500	14%	1%
Hinjewadi	West	4,800 - 5,800	9%	1%
Chikhali	North	3,400 - 4,000	4%	3%
Chakan	North	2,800 - 3,200	8%	2%
Ambegaon	South	4,200 - 5,200	7%	2%
Undri	South	3,800 - 4,800	12%	3%

* Change in weighted average prices

Source: Knight Frank Research

Key Takeaways

The demand for homes in Pune is expected to decrease from 38,800 units in 2013 to 34,500 units in 2014 resulting in a fall of 11%. However, a fall in absorption is expected to be complemented by a sharper drop in the number of new launches that are estimated to decrease by 21% from 45,370 units to 35,840 units during the same period

We expect the sales volume to recover from H2 2014 onwards, after a lull of more than two years. It is forecasted to increase by 11% to 19,800 units in H2 2014, compared to H2 2013

The QTS ratio has been inching upwards since September 2013, signifying weakness in the market

South Pune is slowly emerging as a preferred destination for home buyers in Pune due to its strategic location between the two major IT/ITeS employment hubs of Hinjewadi in the west and Kharadi in the east, with areas like Kondhwa, Ambegaon, Undri and Dhayari equidistance from both

West Pune observed the sharpest fall in new launches during H1 2014, as developers curtailed launching fresh projects on the back of lacklustre demand and poor response received by the various projects launched during H2 2013

South Pune's health is the poorest, as it continues to carry the excess unsold inventory of projects that were launched more than two years ago. This problem has been compounded by the sharp increase in new launches during H1 2014

The bumpy ride in demand and supply does not seem to have any significant impact on price levels

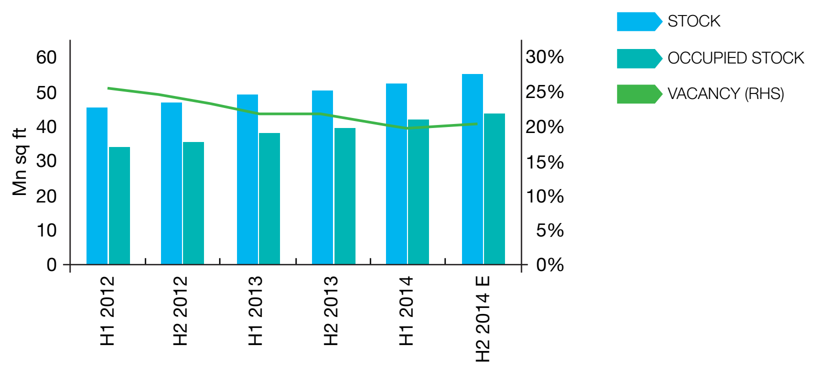
OFFICE MARKET

Metropolitan Region Analysis

Pune city is one of the leading software exporters in India. The pace at which the IT/ITeS industry grew in the city led to a flurry of construction activity in the office space market over the last decade. The manufacturing sector, primarily from this sector led to the emergence of suburban and peripheral business districts, where the availability of large tracts of land helped in the development of office space.

The Pune office market has been witnessing falling vacancy levels since 2012 on the back of a steady rise in absorption and a slower pace of

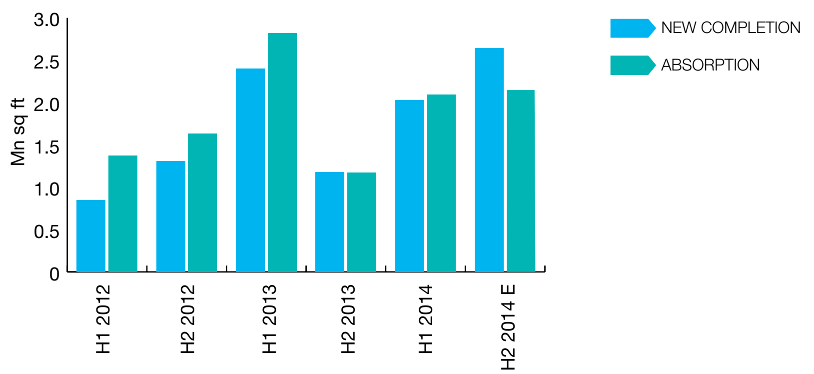
FIGURE 1
Office Space Stock and Vacancy



Source: Knight Frank Research

driven by the auto and auto ancillary and engineering industries, remained at the forefront of office space absorption in the city for many years, till the IT/ITeS boom fuelled the need for quality office space in a large quantum. The growing demand completion of new project. With an occupied stock of 43.4 mn sq ft out of the total office space stock of 54.3 mn sq ft, the vacancy level observed during H1 2014 was 20%, down from 22% in H1 2013. The absorption numbers during the first half of 2014 were better than

FIGURE 2
New Completion and Absorption of Office Space



Source: Knight Frank Research

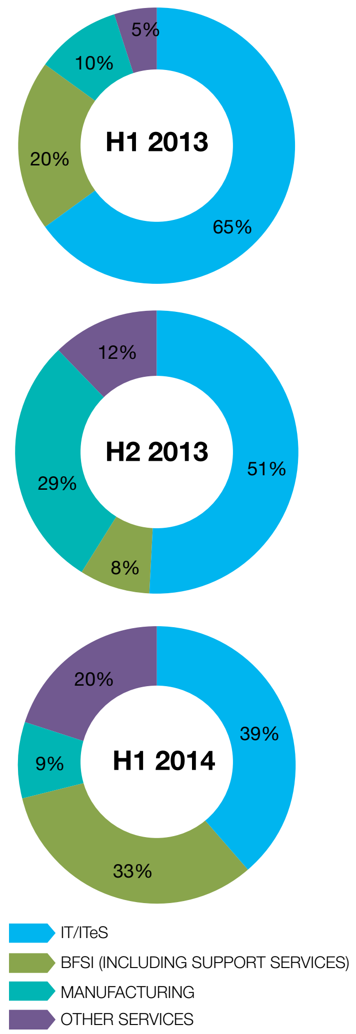
The absorption numbers during the first half of 2014 were better than expected due to improved sentiment in the IT/ITeS and BFSI sectors, which helped in pulling down the vacancy levels from 22% in H1 2013 to 20% in H1 2014 expected due to improved sentiment in the IT/ITeS and Banking, Financial Services and Insurance (BFSI) sectors, which helped in pulling down the vacancy levels. Additionally, new completions were outpaced significantly by absorption during this period. While more than 2.1 mn sq ft of office space was transacted in H1 2014, only 2 mn sq ft of new supply entered into the market.

Office space transactions in Pune have historically been dominated by the IT/ITeS and manufacturing sectors. However, this trend seems to be changing, with the share of the IT/ITeS sector in total absorption falling drastically. The BFSI sector has garnered second place in terms of shares during H1 2014. A few big-ticket deals by banking majors including support services like HSBC, Barclays and Citibank have skewed the share towards the BFSI sector during this period.

The share of the other services sector has increased to 20% of the total transaction volume from less than 5% a year ago because of the strong demand for space from consulting, media, healthcare and retail companies. The high cost of real estate in metro cities has compelled a large number of service-sector companies to explore alternative locations like Pune and Hyderabad, where the rentals are relatively cheaper. Additionally, numerous start-up ventures that cater to the Mumbai market in the consulting and media sector prefer to operate out of Pune due to lower operational costs. These factors seem to have aided in a steady rise in absorption in this segment in the last two years, and we expect such a trend to continue.

During H1 2014, the Pune office market witnessed a substantial jump in the number of deals. However, the average deal size has reduced considerably during the same period. Since the majority of the deals in the other services sector are below 12,000 sq ft, the average deal size tends to be pulled down whenever the share of this segment in total absorption increases. Alternatively, the bulk of the deals in the IT/ITeS and BFSI sectors are in the ticket size of 30,000 sq ft and 60,000 sq ft respectively. Hence, the average size of transactions has reduced to 21,400 sq ft in H1 2014 from 42,700 in H1 2013.

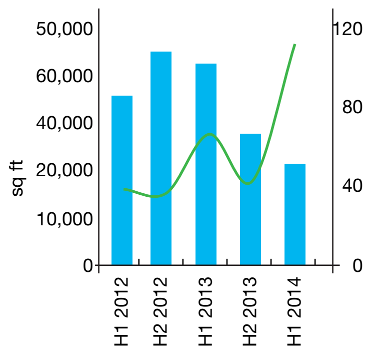
FIGURE 5
Sector-wise Absorption



The ticket sizes of transactions have a considerable influence on the rental movement during a particular period. While tenants with a requirement for large spaces tend to have the upper hand during rental negotiations, the reverse is true with small-size deals. Since the average deal size in Pune has been

The share of the other services sector has increased to 20% of the total transaction volume from less than 5% a year ago due to strong demand for space from consulting, media, healthcare and retail companies

FIGURE 3
Deal Size Analysis



Source: Knight Frank Research

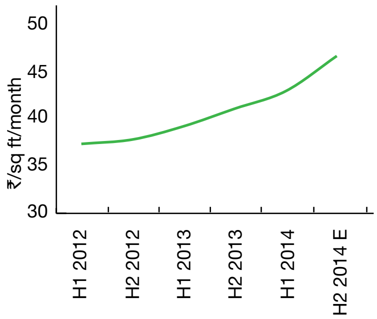
shrinking, the resultant impact has been observed on the rental value, which has increased by 5% in the preceding six months. Moreover, the downward trend in vacancy levels seems to have encouraged the landlord community to demand a higher rent.

Going forward, we expect 2.16 mn sq ft of office space to be absorbed in the Pune market during H2 2014, resulting in a 85% increase compared to H2 2013. For the year 2014, the total absorption is expected to touch 4.26 mn sq ft - an increase of 7% from the 4 mn sq ft that was achieved during 2013. This will be matched by a higher increase in new completions of 4.68 mn sq ft by the end of 2014, as new projects amounting to 2.64 mn sq ft are expected to be completed in the remaining six months of the year. One of the prominent projects expected to enter into the market in the coming months is Blue Ridge Phase 2 by Paranjape Schemes at Hinjewadi.

Rental value is expected to continue its upward stride in H2 2014 at a pace of 9% compared to H1 2014 on the back of improved sentiment. A strong pipeline of new supply is expected to restrict the upside movement of rentals to single digits. The city's weighted average rental value is forecasted to increase from ₹ 43/sq ft/month in H1 2014 to ₹ 47/sq ft/month in H2 2014.

Progress on all the major infrastructure projects in the city, such as the Pune Metro, Pune International Airport and Pune Outer Ring Road, has been slow. Although the metro rail project has gained some traction in the last few months with the proposal to form a Special Purpose Vehicle (SPV), tangible progress at the ground level is still missing. The airport and outer ring road projects are still at the pre-feasibility study level, and we do not expect any concrete benefits arriving out of these projects during 2014.

FIGURE 4
Weighted Average Rental Movement (₹/sq ft/month)



Source: Knight Frank Research

Since the average deal size in Pune has been shrinking, the resultant impact has been observed on the rental value, which has increased by 5% in the preceding six months

Business District Analysis

The Pune office market can be classified broadly into six business districts, with locations within each business district sharing similar characteristics in terms of rent, demand drivers, preference of occupiers, infrastructure development and distance from the city centre.

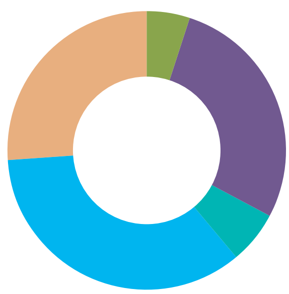
Business District	Micro-markets
CBD and off-CBD	Bund Garden Road, S B Road, Camp, Deccan
SBD East	Kalyani Nagar, Airport Road, Yerwada, Nagar Road
PBD East	Hadapsar, Kharadi, Phursungi, Wanowrie
SBD West	Pashan, Aundh, Baner, Kothrud
PBD West	Hinjewadi, Bavdhan, Wakad, Balewadi
SBD North and South	Pimpri, Chinchwad, Bhosari, Bibvewadi, Satara Road

The CBD and off-CBD markets of Pune consist of locations that are perceived to be the most sought after by tenants due to their strategic location within the city, excellent connectivity to prime residential areas and the presence of developed physical and social infrastructure. Historically, Bund Garden Road, Camp and Deccan were considered to be prime office locations, with S B Road emerging as an addition in recent years.

The CBD and off-CBD markets have observed an increase in traction during H1 2014, with their share jumping to 8% from 5% a year ago. The manufacturing and other services sectors are the primary demand drivers in this business district. Compared to the IT/ITeS sector, demand for space from the tenants of these two sectors is on the lower side, with the bulk of the requirement falling in the range of 4,000-12,000 sq ft. As this results in a lower deal size (value of transaction), the affordability level of occupiers increases despite higher rentals prevailing here. Additionally, the preference to locate within the city centre for these sectors is very high because their employees have to make their own travel arrangements, in contrast to the majority of the IT/ITeS sector companies that provide transportation facilities. As the city has witnessed an increase in the combined share of absorption from the manufacturing and other services sectors, from 15% in H1 2013 to more than 29% in H1 2014, the resultant benefit has accrued to the CBD and off-CBD markets.

The renewed interest in the CBD and off-CBD markets, especially in locations like S B Road and Bund Garden Road have impacted the rental levels positively after a lull of more than five years. Rents have increased marginally by 6% in the last twelve months, with S B Road leading in terms of appreciation. Going forward, we expect a muted growth in rental value, as most of the occupiers continue to prefer locating within the SBD markets due to relatively cheaper rentals.

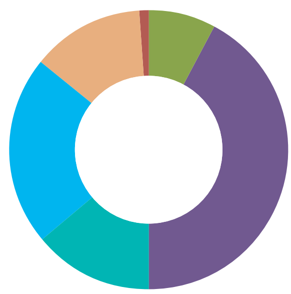
FIGURE 6
Business District-wise Absorption Split in H1 2013



- **5%** CBD & OFF- CBD
- **28%** SBD EAST
- **6%** SBD WEST
- **35%** PBD EAST
- **26%** PBD WEST

Source: Knight Frank Research

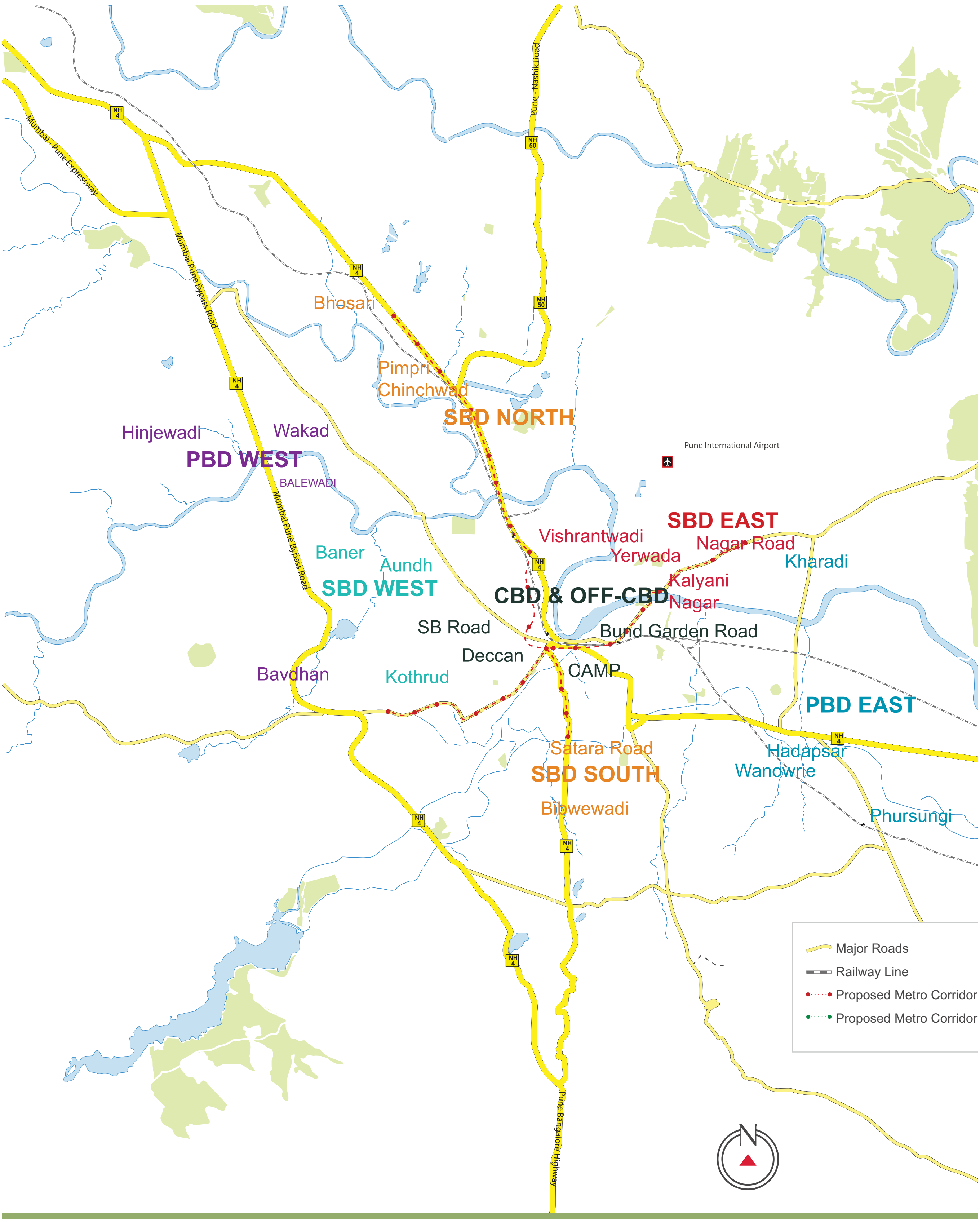
FIGURE 7
Business District-wise Absorption Split in H1 2014



- **8%** CBD & OFF- CBD
- **42%** SBD EAST
- **14%** SBD WEST
- **22%** PBD EAST
- **13%** PBD WEST
- **1%** SBD NORTH & SOUTH

Source: Knight Frank Research

BUSINESS DISTRICTS OF PUNE



Select Transactions in the Pune Office Market

Building	Occupier	Location	Approx. Area (sq ft)
Business Bay	HSBC	Yerwada	500,000
Elbee House	Times of India	Bund Garden Road	12,000
EON	Barclays Technology	Kharadi	180,000
Embassy Techzone	Volkswagen	Hinjewadi	50,000
Commerzone	ADP	Yerwada	50,000
Marvel edge	Quick Heal	Viman Nagar	62,000
Commerzone	Schlumberger	Yerwada	25,000
Matrix Towers	Yardi	Wakdewadi	47,000
Amer Paradigm	Xoriant	Baner	17,500
Amar Apex	Siemens	Baner	47,000
Sai Hera	DFPCL	Mundwa	73,000
S P Infocity	CSI Compucom	Fursungi	45,000
EON	Citi Bank	Kharadi	35,000
Embassy Techzone	Flextronics	Hinjewadi	108,000
Commerzone	Nuance	Yerwada	52,000

Source: Knight Frank Research

SBD east has emerged as the most preferred market during H1 2014 as its share in absorption has increased from 28% in H1 2013 to 42%

SBD east has emerged as the most preferred market during H1 2014, as its share in absorption has increased to 42% from 28% in H1 2013. Connectivity to Pune airport, easy access to the city centre and the presence of excellent physical and social infrastructure have attracted a healthy mix of occupiers from all sectors towards this business district. The construction of good quality office projects like Commerzone by K Raheja Corp at Yerwada and Business Bay by Panchshil Realty on Airport Road have diverted a large number of occupiers from CBD and off-CBD locations towards this market. Smaller floor-plates, limited amenities and inadequate parking facilities in the office buildings located in the CBD and off-CBD markets have caused this exodus. This trend has helped the rental value appreciate by more than 12% and 6% during H1 2014, compared to H1 2013 and H2 2013 respectively. The upswing in rental value is expected to continue, as the pipeline of new supply is shrinking with each passing quarter.

SBD west, which had a miniscule share of 6% in total absorption during H1 2013, has attracted significant interest from occupiers during H1 2014, as its share has jumped to 14%. SBD west is similar to SBD east in many ways. It is well connected with the city centre and has excellent physical and social infrastructure that has helped it attract occupiers from all sectors. However, its distance from the airport and railway station has limited the potential of this market as compared to SBD east. During H1 2014, IT/ITeS sector companies led in terms of absorption in this business district, with Aundh and Baner emerging as the most preferred locations. A limited number of new project completions, low supply pipeline and steady demand have helped the rental levels soar by 14% over the last year. We expect absorption to remain healthy in the coming months, as occupiers who have a high preference to locate close to the city centre but are restricted by limited budgets will continue to drive the demand in this business district.

Business District-wise Rental Movement

Business District	Rental Value Range in H1 2014 (₹/Sq ft/month)	12-month change	6-month change
CBD and off-CBD	55 - 85	6%	2%
SBD East	40 - 60	12%	6%
SBD West	40 - 55	14%	4%
PBD East	35 - 60	13%	5%
PBD West	32 - 45	9%	3%

Source: Knight Frank Research

Strong traction in the SBD markets seems to have undermined the transaction activities in the PBD markets during H1 2014. This is a clear reversal in trend, wherein the SBD markets have regained their share in total transaction, which they had been losing out to PBD markets over the last few years. The key reason for such a trend reversal in H1 2014 is due to a higher share of non-IT/ITeS sector companies in total absorption, as these occupiers prefer locating closer to the city centre. EON Free Zone and World Trade Center by Panchshil Realty at Kharadi, along with SP Infocity by Shapoorji Pallonji at Phursungi have witnessed the highest traction within PBD east during H1 2014. Similarly, the maximum traction in PBD west has been observed in Blue Ridge by Paranjape Schemes and Embassy Techzone by Embassy Group, both located at Hinjewadi.

Rising rental values and non-availability of large vacant space in the SBD markets will continue to drive the demand for office space in the PBD markets. While there is little difference in the characteristics of the east and west PBD markets, the share in absorption of PBD east has consistently remained higher than PBD west. Proximity to the Pune airport and the presence of a developed retail infrastructure have continued to work in favour of east Pune. This has helped in faster rental growth in PBD east compared to PBD west over the last year, and we expect this trend to continue.

Traction within the SBD north and south markets continue to remain insignificant because the rapid development of office markets in East and West Pune has restricted the growth of these markets. Hence, despite their proximity to the city centre, real estate development in these markets has been restricted mainly to residential. While a large number of industrial units are located in the Pimpri-Chinchwad region of SBD north, it has achieved limited success in attracting office space occupiers. Similarly, the SBD south market has been unsuccessful in attracting occupiers, and we expect this to continue.

Key Takeaways

For the year 2014, the total absorption is expected to touch 4.26 mn sq ft - an increase of 7% from the 4 mn sq ft that was achieved during 2013

Absorption numbers during the first-half of 2014 were better than expected, due to improved sentiment in the IT/ITeS and BFSI sectors, which helped in pulling down the vacancy levels from 22% in H1 2013 to 20% in H1 2014

Since the average deal size in Pune has been shrinking, the resultant impact has been observed on the rental value, which has increased by 5% in the preceding six months

The share of the other services sector has increased to 20% of the total transaction volume from less than 5% a year ago on the back of strong demand for space from consulting, media, healthcare and retail companies

SBD east has emerged as the most preferred market during H1 2014 as its share in absorption has increased to 42% from 28% in H1 2013

Proximity to the Pune airport and the presence of a developed retail infrastructure have continued to work in favour of east Pune. This has helped in faster rental growth in PBD east compared to PBD west over the last year

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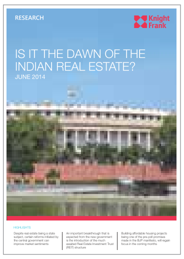

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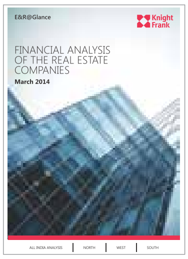

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