REVITALISING INDIAN REAL ESTATE:

A NEW ERA OF GROWTH & INVESTMENT

CONTENTS

EXECUTIVE SUMMARY

The real estate sector is on the threshold of changes that have been long overdue. Whilst the investment and commercial office sectors are reviving, the residential sector is still lagging behind. The Central Government has introduced various policy measures to boost the investment environment and regulate the real estate sector, which will power the sector in the long run. We believe that the government, through initiatives such as Real Estate Regulatory Authority, Benami Transactions Act, Income Declaration Scheme 2016, demonetization of currency notes, is committed to increasing transparency in the sector.

This report explores the potential of Indian market across Investments, office, residential and the retail markets, amidst high business confidence. A pro-business government at the center, strong growth in GDP and positive economic outlook have reinstated confidence amongst investors, enabling them to increase their exposure to the real estate sector in India. This report attempts to ascertain the potential of REITs in India and determines trends in key office markets, ascertaining how the demand and supply factors would interplay by 2020. Whilst the real estate sector has seen momentum in investments and the commercial office sector, the residential sector is yet to see a sustained pick-up in demand. This report builds a case for investments into specific segments such as housing for the Low Income Group (LIG) that typically sees a huge gap. We believe that the government has set the building blocks for the economy in ways more than one and that it is now up to the developers, investors and end-users to provide support and take advantage of these to achieve their own objectives.

Foreign Direct Inflows

		Rank in FDI inflow in 2015	Annual Growth	USD billion
DEVELOPING	CHINA	3	6%	135
	BRAZIL	8	-11%	64
	INDIA	10	28%	44
DEVELOPED	USA	1	256%	380
	SINGAPORE	7	-4%	65
	CANADA	9	-17%	48

Source: UNCTAD

GLOBAL ECONOMY

The year 2016 has been a decisive year for the global economy with several crucial events that could potentially alter the balance of the global economy. Watershed events such as Britain's exit from the European Union, Donald Trump winning the US presidential election, refugee crisis in Europe and China's decelerating growth underline this year. The International Monetary Fund (IMF) forecast 2016[1] global growth at 3.1%, before expecting it to inch up to 3.4% in 2017. Slower-than-expected growth in the US, led by weak investment and exports, and wavering growth in Europe and UK are likely to subdue growth this year. The constrained growth is exacerbated by a slowdown in China, a further decline in commodity prices, especially for oil, with sizable redistributive consequences across sectors and countries, as well as geo-political issues in several parts of the world.

On a positive note, growth in advanced economies and emerging economies are both likely to accelerate for the first time since 2010[2]. Although advanced economies would likely grow 1.6%, lower than last year's 2.1% growth, emerging markets and developing economies are expected to grow 4.2% this year.

Despite a gloomy forecast for 2016, global flows of foreign direct investment (FDI) in the year 2015 rose by about 40% to USD 1.8 trillion[3], the highest level since the global economic and financial crisis began in 2008. However, the FDI growth did not convert into an expansion in production capacity in most of the countries, leading to subdued economic growth. Developing economies saw inward FDI reach a new high of USD 765 billion, a 9% increase from 2014 levels.

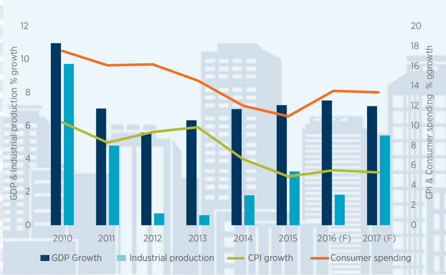
India is ranked 10th in FDI inflows in the year 2015. Various measures by the government such as 'Make in India' mission, liberalization measures such as easing FDI norms across sectors such as civil aviation, defence, food products and pharmaceuticals, have contributed to India maintaining its position.

1. IMF 'World Economic Outlook'
2. IMF estimates
3. 'Global Investment Trends Monitor' United Nations Conference on Trade and Development

INDIAN ECONOMY

India's bright spot in the world economy has been an oft-discussed topic in world forums and discussions. A persuasive central government at the helm has helped improve India's perception by etching a positive image among global investors. The years prior to 2014 in India were marked by a drop in foreign investments, stalled infrastructure projects, rising inflation and a weak currency market. With an investor-friendly government at the helm, the Indian economy has been witnessing a revival in business and consumer confidence. The fastest-growing large economy in the world, India has clocked in GDP growth of 7.6%[4] in 2015. Moreover, a combination of factors such as investor-friendly reforms initiated by the government, increased public expenditure, anticipated increase in rural consumption backed by good monsoons, controlled inflation rate, have renewed confidence of global investors in the Indian economy.

MACRO INDICATORS



Source: Oxford Economics

ECONOMY STIMULANTS:

Government spending - India's recent spurt in growth has been driven by increased government spending over the last two years. In FY 2015-16, public investments grew by 24%, with the government investing across various sectors in the country. Moreover, the Seventh Pay Commission and revised pay for defence personnel has increased government's expenditure. During the 2016-17 budget, the government focus was on rural development, which is likely to incur the maximum expenditure, followed by human resources and roadways sectors.

Subdued inflation - Over the last year, inflation rates have been controlled in India with oil and commodity prices collapsing and food prices witnessing modest increases. The marginal increase in food prices has been led by removing bottlenecks in food supply chains that are leading to higher efficiencies. The moderating inflation, in turn, has been partly responsible for the RBI cutting the benchmark lending rate – the Repo Rate by 150 basis points since January 2015 to 6.5%. This rate cut is vital to provide a much-needed stimulus to private spending in the country and boost the investment cycle.

Urban demand - The average Indian's higher disposable income and the implementation of the Seventh Pay Commission's recommendations would steer urban consumption, going forward. While demand would be led by urban India, rural consumption too is likely to pick up, with hopes from the good monsoon season seen in 2016. Consumer spending in India is likely to grow at a pace of 13.5%[5] in 2016, as against 10.9% last year.

4. Oxford Economics
5. Oxford Economics

IMPACT OF US PRESIDENTIAL ELECTIONS ON INDIA

The election of Donald Trump as the next US President could lead to some short-term volatility for the Indian financial markets, which take their major cues from global financial markets, but may not necessarily impact the broader Indian economy during this period. Investment activity from FIIs and PE funds in the near term may slow down as they will likely go into wait-and-watch mode to assess new policies that Trump will roll out. Once the market calms down, these investors will resume efforts to deploy the record-setting level of capital that has already been raised and allocated for Indian markets.

The Indian IT-BPM sector, which has a strong client base in the US, could be on a wait-and-watch mode for some time. Indian companies would likely experience slight delays in decision-making as companies await new presidential polices on global outsourcing and H1B visas. However, it must be noted that India's large skilled workforce is of high importance to the productivity and growth of American companies.

In terms of real estate, Trump Organization's Indian representation – Tribeca - has four real estate projects in India – in Mumbai, Pune and Gurgaon – across commercial and residential projects. This includes a residential project in Pune with Panchshil Realty and another in Mumbai's Lower Parel with the Lodha Group. Besides, the company is also pursuing a residential and an office project in Gurgaon. These projects make India one of the largest markets for Trump Organization with maximum number of projects after North America. The company has been extremely bullish on its prospects in India and is looking to launch a few projects in 2017.

HEADWINDS:

Manufacturing - The government's 'Make in India' mission attempts to increase the competitiveness of Indian goods in the global market. The government intends to increase the share of manufacturing sector to 25% of GDP by 2022 and create additional 100 million jobs by then. However, India has a long way to achieve this as the sector's share has been marginally declining since 2011. India continues to operate under archaic land and labor laws, with challenges such as power and connectivity in rural areas that leave a lot to be desired. Moreover, India's rank on Ease of doing business[6] moved up only one rank in 2016, signaling that on-ground pace of reforms continues to be slow.

Weak private investment - Private sector investment levels continue to be subdued in India, with the share of private investments in projects under implementation falling from 53% in 2013-14 to 48%[7] in 2015-16. In contrast, during the same period, the government's share of investments increased from 47.2% to 52.3%. Strengthening consumption, lower commodity prices, stable inflation levels have led to some improvement in corporate profitability, but a broad-based recovery is yet to be seen.

6. World Bank's Ease of Doing Business Report
7. Centre for Monitoring Indian Economy

INDIA REAL ESTATE

The Indian real estate sector, while witnessing a tumultuous journey over the last few years, has seen a mixed year. While demand in the commercial office market is undoubtedly strengthening, the residential markets are yet to see a pick-up. Interestingly, private equity investments in real estate (PERE) have been seeing highs, with the year 2016 witnessing one of the best years in terms of PERE inflows. The future course of the Indian real estate sector would largely be dictated by following reforms initiated by the government-

Real Estate (Regulation and Development) Act

The central government has given states the mandate to frame rules for a state level Real Estate Authority, which then would be enforced by April 30, 2017. RERA, which is currently mandated to regulate the housing sector, would be game-changer as it would bring in transparency in the highly fragmented Indian real estate sector.

Real Estate Investment Trusts (REITs)

After bringing in the legislation in 2014 to enable this investment avenue, the government has further eased rules related to the structure, removal of the limit on the number of sponsors and increased the limit of investment in under-construction assets. The government exempted the Dividend Distribution Tax (DDT) for Special Purpose Vehicle (SPV) of REITS in the Union Budget, which was a huge hindrance in the introduction of REITs investments, making them less attractive. Removal of dividend distribution tax too would provide a fillip to REIT structure and attract long-term finance from foreign and domestic investors.

Foreign Direct Investment

Efforts to increase the ease of doing business, easing FDI rules in several sectors including Aviation, Defence, and Pharmaceuticals etc. would simplify the process of foreign investments into the country. Last year, the government eased rules in FDI in Construction and Development sector, which is expected to drive investments into the real estate sector.

As of November 2016

CURRENCY DEMONETIZATION AND REAL ESTATE SECTOR

The Indian real estate market, which is largely fragmented and unorganized, is considered to be a safe haven for black money. Though large and reputed developers do not typically deal with cash transactions, the impact on the investment sales and the secondary market could be higher as the component of cash is high in these transactions. Land transactions too are funded in cash in most markets in India, and in some cases, a very large fraction of the payment is made through cash. Hence, land transactions would be impacted to a certain extent due to the curb on black money. Overall, smaller and unorganized developers could be adversely impacted by this demonetization move as their exposure to cash is far higher. Therefore, there is likely to be some amount of correction in real estate prices in those markets, especially those which have seen substantial speculative investments by individuals through black money. However, the correction is unlikely to be dramatic and immediate. At a time when the sector is looking forward to the setting up of a Real Estate Regulatory Authority in each state, this move of curbing black money is set to bring in increased accountability in the market.

INVESTMENT LANDSCAPE

FOREIGN DIRECT INVESTMENT (FDI) INFLOWS

Cumulative FDI inflows into India amounted to approximately INR 2,159 billion (USD 32.2 billion) during January-September of 2016, a growth of 22% over the corresponding period last year. The services (16%), telecommunication (9%) and (5%) trading sectors garnered the largest share of FDI inflows during 2016. While FDI inflows into India have seen an upward trajectory, FDI inflows into the construction development sector have been declining sharply since 2013 and totaled approximately INR 58 billion (USD 870 million) in the last three years, with FY 2015-16 (April 2015 – March 2016) recording the lowest inflow of annual FDI into the sector. Weak residential demand in the market over the last few years and stretched financials of developers were some of the factors that led to the slowdown in FDI inflows into the sector.

In order to boost overall FDI inflows, the Government of India has been relaxing FDI norms across multiple sectors such as aviation, food processing, defence, pharmaceuticals, etc., over the year. The government has also been actively promoting its investment initiatives such as Make in India, development of new industrial corridors and infrastructure projects, etc. to attract foreign investment in India. Therefore, several countries have already committed significant investment plans in India. Also, the government recently released its plan to identify and build strategic partnerships with prospective foreign investors. Under this initiative, the Department of Industrial Policy and Promotion (DIPP) will meet the top executives of about 150 companies with significant investment potential and develop strategies to help them invest in India. Such initiatives are expected to help drive overall business investments in the country, which in turn will boost demand in the real estate sector.

Delhi-Mumbai Industrial Corridor (DMIC)

It is one of the world's biggest infrastructure projects with an estimated investment of USD 90 billion, and is planned as a hi-tech industrial zone spread across seven states. While Japan has pledged to invest USD 4.5 billion in the industrial corridor, several countries such as Italy, Taiwan, South Korea have also shown interest.

State	Key impact towns
Maharashtra	Nashik, Dhule, Pune
Madhya Pradesh	Pithampur-Dhar-Mhow
Gujarat	Ahmedabad, Dholera
Rajasthan	Jaipur, Neemrana
Haryana	Faridabad, Hissar
Uttar Pradesh	Meerut, Ghaziabad

Bengaluru-Mumbai Economic Corridor

The Bengaluru–Mumbai Economic Corridor project is planned to pass through three industrial nodes spread over 10,000 acres. Master planning of the corridor has been initiated by the Delhi-Mumbai Industrial Corridor Development Corporation Ltd. (DMICDC).

State	Key impact towns
Karnataka	Tumakuru, Chitradurga, Hubballi-Dharwad, Belagavi
Maharashtra	Kolhapur, Solapur, Sangli, Pune, Mumbai

Chennai-Bengaluru Industrial Corridor

The Chennai-Bengaluru Industrial Corridor would enable quicker movement of goods for exports through Chennai and Krishnapatnam ports. The work for the project is expected to begin in 2017.

State	Key impact towns
Tamil Nadu	Ponneri, Sriperumbudur
Andhra Pradesh	Krishnapatnam Port
Karnataka	Hoskote, Tumakuru

MAKE IN INDIA

'Make in India' mission has been launched to project India as a preferred investment destination and a global manufacturing hub. In order to attract companies to invest in India, the government has sought to improve the business environment and increase the ease of doing business. Presented below are key sectors and their hubs-

For **automotive** sector, hubs include Delhi-Gurgaon-Faridabad in the north, Mumbai-Pune-Nashik-Aurangabad in the west, Chennai-Bengaluru-Hosur in the south and Jamshedpur-Kolkata in the east.

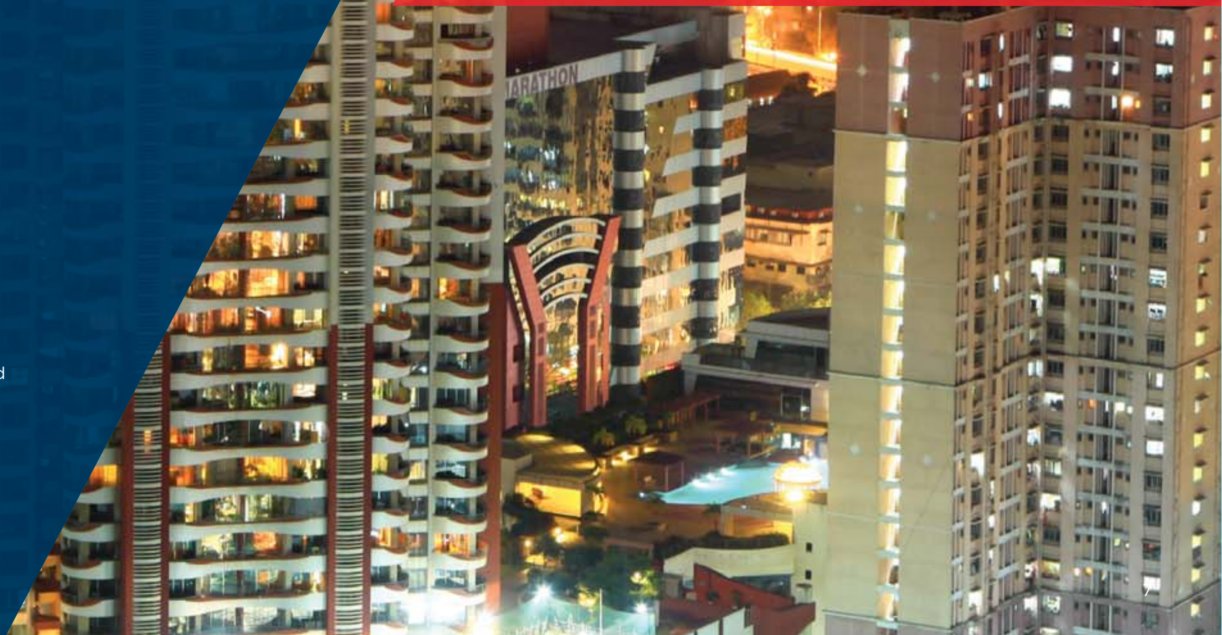
In **chemical** manufacturing, the government has approved Petroleum, Chemical and Petrochemical Investment Regions. Andhra Pradesh's Vishakhapatnam, Dahej in Gujarat, Paradeep in Odisha and Cuddalore and Naghapattinam in Tamil Nadu would witness development in this sphere.

100% FDI in **defence manufacturing** would enable several foreign companies entering on their own or forming JVs with Indian partners. Gujarat's Dholera Smart City on the Delhi-Mumbai Industrial Corridor is expected to become a defence manufacturing hub that would upgrade and overhaul armoured vehicles.

100% FDI in the **aviation sector** can steer further demand for commercial office and industrial spaces in Delhi-NCR, Mumbai and Bengaluru where some of the companies are already located.

74% FDI in existing **pharmaceuticals** companies would increase JVs in the healthcare sector that would in turn, strengthen research and development in the sector. This would not only boost demand for manufacturing and office spaces, but also land for research and development laboratories. Being one of the top pharmaceutical hubs in India, Hyderabad is especially expected to witness high traction in this sector.

These infrastructure initiatives and policies are definitely progressive and will help in driving business investments in the country and also boost demand in the real estate sector. However, the government needs to ensure that it quickly and fully implements and monitors the announced policies, especially the ones that can directly bolster growth in real estate such as infrastructure development, land digitization, Real Estate Regulatory Act, title insurance and Goods & Services Tax (GST).



PRIVATE EQUITY INVESTMENT IN REAL ESTATE IN INDIA

Over the past couple of years, private equity investment in real estate (PERE) in India has been on a sharp growth trajectory. A stable and pro-business government taking charge at the center, strong growth in GDP, positive economic outlook, etc. have reinstated confidence amongst investors, enabling them to increase their exposure to the real estate sector in India. Both domestic and foreign investors have been active and significantly increasing their investments year on year (y-o-y).

The year to date (YTD[8]) PERE in 2016 increased 20% to INR 278 billion (USD 4.2 billion), up from INR 232 billion (USD 3.60 billion) recorded during the same period last year. YTD 2016 investments recorded at INR 193 billion (USD 2.9 billion) by domestic investors have already surpassed those made during the entire calendar year 2015 by 25%. Over the past few years, the structured debt strategy, largely suitable for residential assets, has remained as the most preferred investment mode, especially for the domestic investors as it allows to make stable and secured returns at pre-decided terms. Domestic investment funds therefore, invested about 63% (INR 121 billion, USD 1.8 billion) in residential segment and 20% in office assets, followed by 12% in mixed use developments and remainder 5% being in retail assets.

8. January - September

The cumulative investments from foreign investors during YTD 2016 were INR 72 billion (USD 1.15 billion) about 28% lower than YTD 2015. However, owing to several deals scheduled to close in the fourth quarter (estimated - INR 191 billion, USD 2.9 billion), the investments from foreign investors in 2016 are expected to far exceed those made during calendar 2015. Investments from foreign funds have been comparatively more balanced than domestic fund houses in terms of sector allocation. Foreign investment funds invested 40% in retail assets, 36% in residential, 17% in office and 6% in hospitality assets during YTD 2016. Owing to restrictions on foreign entities offering debt in any form in India, equity investments accounted for 54% of the foreign PE investments during YTD 2016. Special Purpose Vehicle (SPV) level investments have however, been the most preferred for both, foreign and domestic investors. While in 2015 about 81% of the investments were made at the SPV level, YTD 2016 has recorded 97% investments in the category.

PERE - Sectorial analysis

Residential assets

Accounting for 54% of the total investments during YTD 2016, residential assets have remained the most preferred for PERE in India. Over INR 150 billion (USD 2.25 billion) have already been invested in residential assets during YTD 2016. However, most of these investments are being made at project level and largely in projects that have received all necessary approvals and are in the construction phase. In terms of geographic preference, Mumbai has been the top city for investments in residential assets. The city received over 41% (INR 62 billion, USD 930 million) of the total investments in residential assets during YTD 2016. Delhi-NCR accounted for 29% (INR 43.1 billion, USD 644 million) followed by Bengaluru at 19% (INR 28.5 billion, USD 426 million).

Office assets

Owing to continued interest in leased office assets coupled with the potential to list such assets under Real Estate Investment Trusts (REITs), the YTD 2016 investments (INR 57 billion, USD 852 million) are nearly at par with the total investment received during the calendar year 2015 (INR 60 billion, USD 938 million). Moreover, with a few large deals for office portfolios in the closure stages in the fourth quarter, the year 2016 is expected to record the highest annual investments made in this asset class. Mumbai remained the top city for investments in office assets and accounted for about 61% of the investments, Bengaluru accounted for 17% of the investments, while Delhi-NCR accounted for 9% share during YTD 2016.

Retail assets

Investments in retail real estate sector (malls) that had remained subdued over the past few years are now gaining traction. Anticipating a revival in the sector and given the potential to list under REITs, retail real estate assets are now attracting large investments. The YTD investments in retail assets during 2016 increased three-fold to INR 38,000 million (USD 569 million), from INR 10,200 million (USD 156 million) noted during the same period of 2015. Retail assets, especially completed and leased malls with low vacancies, are being preferred by investors. Accounting for about 76% of the total investments in retail assets, foreign investors have been the key drivers of investments in retail assets during 2016. About 65% of the investments in retail asset made during YTD 2016 are concentrated in Mumbai, followed by Delhi-NCR at a distant second with 24% share and the remainder in a mall in Coimbatore.

PERE - Key city analysis

MUMBAI

During 2016, Mumbai's ranking in the top global investment destinations identified by C&W Research, jumped from 110 to 84. The city was also ranked 12th in the top 20 global 'growth' cities[9] with highest annual growth in PERE and is the only Indian city to register in these rankings. With a potential to generate attractive returns, Mumbai accounted for about 44% (INR 121 billion, USD 1.85 billion) of the total investments made in India during YTD 2016, surpassing the total investments made during calendar year 2015. The residential sector accounted for over half of these investments made in the city followed by 29% in the commercial office sector. The remaining 20% investments were in retail assets. Domestic funds have already doubled their investments in residential assets in Mumbai, up from INR 49 billion (USD 747 million) in calendar year 2015 to INR 91 billion (USD 1.4 billion) in YTD 2016. While investments from foreign investment funds recorded a decline of 37% y-o-y, the estimated investments from them in the city are forecasted to double by the end of fourth quarter of 2016, owing to the impending closure of a large commercial office portfolio deal in the city.

9. Top 20 global cities that received investments of over USD 1 billion, excluding development sites, during 2015-16.

DELHI-NCR

Delhi-NCR received about 28% (INR 77 billion, USD 1.16 billion) of the total investment made in India during YTD 2016, of which 56% was made in residential assets followed by mixed-use developments with 26% share. Investments in the commercial office assets in Delhi-NCR have always been low, with YTD 2016 accounting for only about 6.5% of the investments made in the city. Similar to Mumbai, the overall investments made during YTD 2016 in the Delhi-NCR are already 28% higher than those made during calendar year 2015. Over 80% of the investments made in the city during YTD 2016 are by domestic funds and foreign funds accounted for only 13.5%. The remainder was made by joint ventures of domestic and foreign funds. With the last quarter likely to witness the closure of a large commercial office deal, the current year is forecasted to record the second highest annual investment received since 2008. Within Delhi-NCR, Gurgaon accounted for about 44% of the total investments followed by 34% being in Noida-Greater Noida.

BENGALURU

The YTD investments in 2016 in Bengaluru are already the second highest annual investments that the city has received since 2008. Of the INR 38 billion (USD 574 million) that the city has received during YTD 2016, 74% has been in residential assets with the remaining in commercial office assets. Despite being the largest office market in India, Bengaluru received only about 16% of the total investments made in the commercial office assets during the current year as investors continue to prefer residential assets owing to lower gestation period. About 74% of the investments made in the city during YTD 2016 were by domestic funds while the foreign funds accounted for about 16% of the investments and the remaining 10% were by joint ventures of domestic and foreign funds.

Emerging cities for PERE

HYDERABAD

Hyderabad is fast emerging as a hot-spot for PERE. The bifurcation of the state in 2014 helped in bringing political stability in the state as well as in Hyderabad. Since then the state government has been proactively implementing policies to attract investors and business to setup their offices in city. These factors helped in reinstating faith amongst investors and businesses. The PERE in Hyderabad have grown significantly, up from a mere INR 800 million (USD 12.1 million) in YTD 2015 to about INR 9.1 billion (USD 137 million) in YTD 2016. About 52% of the investments made during 2016 have been by foreign investors. Domestic investors accounted for the remaining share in investments made in Hyderabad during YTD 2016.

Hyderabad has witnessed a steep rise in demand for commercial office spaces and unlike other cities, the commercial office assets in Hyderabad have received the highest investments. Consequently, 73% of the investments, amounting to INR 6.6 billion (USD 99.3 million), were invested in commercial office assets in Hyderabad. Further, the city is expected to witness about 11.4 msf of Grade A supply by the end of 2017, half of which is already pre-committed. This high volume of pre-commitments further reflects the strong demand pipeline in the city. Such demand-supply dynamics is bound to further attract investors to the city. Residential assets received the remaining 27% of the investments made during the current year.

PUNE

Leveraging the presence of several IT-BPM companies in the city, Pune has witnessed rapid growth in real estate especially in locations such as Wagholi, Kharadi, Wakad, Baner, etc, that are in close proximity to the IT-BPM corridors. Moreover, the presence of large developers has attracted the interests of PE firms to Pune. The PERE in Pune has therefore increased 26% y-o-y during 2016 YTD. The investments in current year have also surpassed those made in Pune during the entire calendar year 2015. The residential asset class accounts for the highest investments, taking 64% of the share in total investments made in the city in 2016. The remaining was spread across commercial office (8.2%), retail (9.7%) and mixed-use developments (12%). Domestic funds have been the key driver of investments and account for about 77% of the total investments made during YTD 2016.

While Pune accounts for about 17% of newly launched units in 2016 across the top seven cities, it has also witnessed a 27% y-o-y increase in new unit launches, indicating optimistic sentiments amongst developers. Moreover, with Pune being selected to be developed into a “Smart city” the PERE investments in the city are expected to increase going forward.

Expectations for PERE in the short term

The current year is forecasted to witness record-breaking investments owing to the sale of stakes in large office portfolios by some of the country's most prominent real estate developers being in final stages of closure. Considering these deals, it is estimated that the calendar year 2016 will record cumulative investments of about INR 483 billion (USD 7.2 billion), a growth of 53% y-o-y.

During the next six months India is also likely to witness the launch of its first REIT, as a global private equity firm in JV with a local developer, has already filed its application for approval with the Securities and Exchange Board of India (SEBI). Apart from this, a few other PE firms are also strategizing to launch their own REITs in India.

Private Equity Investment in Real Estate is recorded at USD 4.2 bn in 2016 YTD, annual growth of 20%

Residential asset have remained the most preferred accounting for 54% of the total investments during 2016 YTD

MUMBAI

Highest annual growth in YTD PERE **56%**

Attracted **44%** of total investment in 2016 YTD

Pune

26% annual growth in PERE investment recorded in 2016 YTD

PERE investment in 2016 YTD surpassed investments in 2015 CY

Delhi - NCR

28% higher PERE investment from 2015 CY

Bengaluru

74% of the city's PERE investment in Residential segment in 2016 YTD

2nd

Second highest PERE investment made since 2008

Hyderabad

73% of city's total investment in office asset amounting to USD 99.3 mn in 2016 YTD

More than **10x** annual increase in PERE investment in 2016 YTD

REITS IN INDIA – TURBO CHARGING THE INVESTMENT MARKETS

OPPORTUNITY IN OFFICE ASSETS

With REITs expected to take form next year in India, non-strata sold Grade A projects that are above 100,000 sf would be the most suitable for REIT investments as such projects are usually easier to acquire (single owner), are well maintained, have a good tenant profile with long-term lease contracts and attract higher rental yields. Across the top seven cities[10] of India, ready commercial office stock that is eligible for REIT investments amounts to 277 msf, accounting for less than half (44%) of total commercial office stock in India. In addition to completed stock, approximately 68 msf of additional REIT-eligible stock expected to be completed by 2020. In total, ready and under-construction projects that are REIT-eligible, IT buildings account for the major chunk at approximately 39%, followed by the IT-SEZ projects that account for 35% of the stock and the remainder 26% in commercial office developments.

With gross rental yields currently ranging between 9%-11% for commercial properties in India, the total value of ready REIT-eligible projects are projected at USD 44-53 billion across the seven cities. Of this, ready stock, as of September 2016, account for approximately 82% of the total value, with the rest likely to arise from under-construction projects that would be ready by 2020.

10. Cities include Mumbai, Delhi-NCR, Bengaluru, Chennai, Pune, Hyderabad, Kolkata

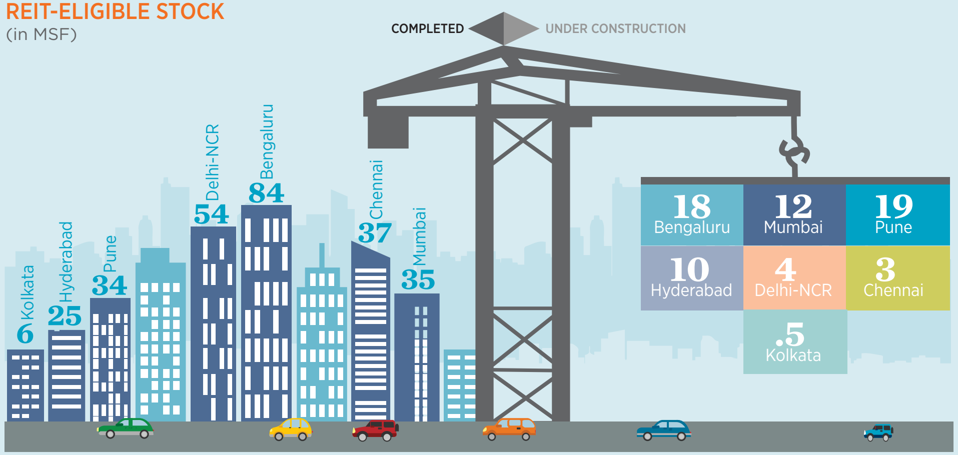
Bengaluru has almost 1.5 times the REIT-eligible stock as that of Delhi-NCR, which ranks second. Bengaluru has a large quantum of existing stock and also a strong pipeline of projects over the next few years which are REIT-eligible. The total (ready and under-construction) value of REIT-eligible projects is likely to be USD 12.3-15.0 billion in Bengaluru, followed by Mumbai (USD 8.9-10.9 billion) and Delhi-NCR (USD 8.7-10.6 billion).

The top three cities of Bengaluru, Delhi-NCR and Mumbai account for 69% of the total value of REIT-eligible ready stock. However, the three cities' share in under-construction projects is likely to taper to 59%, with Pune and Hyderabad expected to witness higher capital values from REIT-eligible under-construction projects (or projects that will be ready by 2020). Delhi-NCR is likely to have comparatively lower under-construction projects between 2016 and 2020, as compared to Bengaluru and Mumbai. With a 20% cap of investment in under-construction assets, projects that are nearing completion are especially ripe for investments. In under-construction assets, Bengaluru accounts for the highest share in the capital value of REIT-eligible developments, followed by Pune and Mumbai. Pune, especially, is likely to account for roughly one-fourth of the total capital value of the REIT-eligible under-construction office assets. Pune is expected to have the highest quantum of under construction REIT-eligible stock that would propel the city's prominence on investors' radar.

Bengaluru's Outer Ring Road (ORR) accounts for the highest capital value of REIT-eligible stock, accounting for roughly 16.4% of the share (existing and under-construction). Owing to a stronghold of the IT-BPM market, the ORR submarket has developed at a rapid pace over the last few years, owing to availability of modern, large buildings at competitive rentals. Pune's SBD East has emerged as a key contender, with REIT-eligible stock valued between USD 3.4-4.2 billion. The submarket, which primarily comprises of Viman Nagar, Hadapsar and Kharadi, has seen strong leasing with several companies requiring large space preferring this submarket. Delhi-NCR's Gurgaon Others submarket (key office hubs in Gurgaon excluding Cyber City, MG Road and Golf Course Road) is expected to have REIT-eligible stock valued between USD 3.2-3.9 billion by 2020.

While Bengaluru's Suburban East submarket has higher REIT-eligible stock, as compared to Gurgaon CBD, lower rentals in the former pushed down the total capital value of REIT-eligible mall spaces of the submarket below Gurgaon CBD.

OFFICE
REIT-ELIGIBLE STOCK
(in MSF)



TOP SUBMARKETS: REIT-ELIGIBLE STOCK

Locations	Value of REIT-eligible stock (In USD billion)	REIT-eligible stock (in msf)	Share in REIT-eligible stock
Outer Ring Road, Bengaluru	7.0-8.5	56.8	16.43%
SBD East, Pune	3.4-4.2	26.3	7.62%
Gurgaon, Delhi-NCR	6.0 - 7.5	39.6	11.5%
Suburban East, Bengaluru	2.7-3.3	17.3	5.03%

SBD East, Pune - Viman Nagar, Kharadi, Nagar Road, Wadgaon Sheri
Suburban East, Bengaluru - Indira Nagar, Old Airport Road, C.V. Raman Nagar

OPPORTUNITY IN RETAIL ASSETS

While investors anticipate a recovery in the segment, retail assets can also be listed as part of the REIT portfolio. Therefore, the retail asset class in India is fast emerging as an attractive investment category for institutional investors. Moreover, the economic factors also indicate a positive growth for the sector. Consumer spending in India has increased by about 14% y-o-y in value terms and is forecasted to grow at 13% CAGR until 2020. The disposable income has also increased in similar proportion, i.e. 12% y-o-y and forecasted to grow at 11% CAGR until 2020[11]. These trends indicate that while disposable incomes have increased, the spending has also increased proportionately. While the e-Commerce segment is gaining increased momentum, the offline retail segment too is set to see growth, resulting from an increase in consumer spending over the next few years. Moreover, the government has significantly relaxed the FDI norms in retail sector in the past few years, especially in single brand retail. Therefore, the FDI in retail trading has increased from USD 184.3 million in 2015 to USD 449.5 million[12] during YTD 2016 as several international brands such as H&M, GAS, Muji, Cath Kidston, GAP, etc. have entered the Indian market in recent times whereas IKEA, Banana Republic, Elevation Burger, MOOYAH Burgers, etc. are in process of opening their first stores in India. Such factors further enhance the investment potential that the retail assets class in India holds.

Currently there are about 112 (52.0 msf) non-strata sold malls above 100,000 sf across the top seven key cities in India. About 78% (41 msf) of these malls are completed and operational while the remaining (11.3 msf) are under construction and scheduled to be completed by 2018. The estimated value of completed malls ranges between USD 16.2 billion and USD 19.8 billion. The malls currently under construction could further add values estimated between USD 3.4-4.2 billion. In the total stock, Mumbai accounts for about 24% (12.5 msf) of the investment-grade malls and has the largest share in value of REIT-eligible malls (31% share, USD 6.1-7.5 billion). Mumbai is followed by Delhi-NCR that has REIT-eligible malls valued at USD 4.6-5.7 billion, further followed by Bengaluru with REIT-eligible malls valued at USD 2.8-3.4 billion. Although Bengaluru has higher REIT-eligible mall stock than Delhi-NCR, the investment value of the REIT-eligible malls is curtailed on account of lower average rentals in the market.

In the under construction stock of malls too, Mumbai has the highest capital value of REIT-eligible mall space ranging between USD 1.2 and 1.5 billion, accounting for 36% of total capital value of REIT-eligible malls under-construction across the seven cities. Chennai emerged as the second-largest market with 27% (3.0 msf) share in upcoming supply. The total capital value of REIT-eligible malls is estimated at USD 750-920 million in Chennai. In under-construction assets, Bengaluru is ranked third with USD 650-800 million worth of REIT-eligible mall spaces. Pune, Chennai and Hyderabad cumulatively account for 52% of the upcoming supply. These three cities also account for 42% of the share in total value of REIT-eligible mall developments. While the top cities are expected to remain as the preferred destination for investments, other tier II and III cities such as Coimbatore, Jaipur, Kochi, Bhubaneswar, etc. are also witnessing increased interest from PE firms in recent years and could be included within REITs over the longer term.

11. Oxford Economics
12. Department of Industrial Policy & Promotion (DIPP)

REITS ACROSS THE WORLD – A COMPARATIVE ANALYSIS

Several developed economies have taken the lead in the implementation of REITs decades ago. The United States' (US) REIT market dates back to the 1960s and is the largest REIT market in the world, followed by Australia. In Asia, Japan was the first country to adopt the REIT system (2001), with Singapore following closely on the Japan's footsteps by enacting REITs in 2002. India's first REIT listing is expected in early to mid-2017.

When REITs were first introduced in the 1960s, they were viewed as a dull investment option due to their nature of fixed dividend akin to bonds and mutual funds. For example, in the US, REITs were considered to be largely unprofitable till the late 1980s, exacerbated by various economic events such as high inflation, tax shields in private property, etc. Over a period of time, significant demand for real estate and upward trend in capital values and rentals powered REITs in the US. This year has been a watershed year for REITs in the US with the market capitalization crossing the USD 1 trillion-threshold led by stable returns in a low-interest rate scenario. Dow Jones U.S. Real Estate Investment Trusts Index has witnessed 5-year annualized returns of 14.85% as of October 2016, slightly higher than the Realty Index's returns[13] of 14.72% during the same period. The soaring rental market since 2008 and the expansion of REITs into various sectors such as telecom towers, healthcare trusts, etc. have further strengthened the REITs market in the US.

The table below provides a brief comparison of the current REIT's regime in the most prominent countries.

COMPARISON OF REITs REGIME IN VARIOUS COUNTRIES

Country	India	Singapore	Japan	Australia	U.S.A
1st REIT listing	2017 expected	2002	2001	1971	1965
No. of listings	2 (estimated)	32	53	18	222
Asset class	Commercial office and retail properties	Commercial office, residential, retail and industrial properties;	Office, residential, and logistics facilities. Some J-REITs invest in hotels, housing for the elderly and infrastructure facilities.	Commercial, retail, office, diversified (some residential) and industrial. Some REITs also invest in healthcare assets, retirement properties, storage facilities and childcare centres	Retail, residential, office, healthcare assets
Non-resident investors	Non-resident investors permitted, subject to conditions	No restrictions on non-resident investors	Non-resident investors permitted, with some conditions	No restrictions on non-resident investors	No restrictions on non-resident investors
Investment criteria	At least 80% should be in completed and revenue-generating real estate, excluding residential assets.	At least 75% of the property fund should be invested in income-generating real estate	Can invest in foreign assets; Cannot hold 50% or more of the total issued shares of another company	Can invest offshore	Must invest at least 75% of its total assets in real estate assets and cash
Income Tax criteria	Not less than 90% of net distributable cash flows of the REIT shall be distributed to the unit holders once in 6 months	If REITs pay out at least 90% of its income as dividends, they are exempt from paying any Income Tax	REITs are required to distribute more than 90% of their profits as a condition for dividend deductibility, but a majority of J-REITs have a payout ratio close to 100%.	Trustee of trust is taxable if unit holders are not entitled to 100% of the income of the trust at year end	Must distribute at least 90% of its taxable income to shareholders annually in the form of dividends.

Source: Country Indices, KPMG, FTSE, S&P

13. Five-year returns have been considered due to lower fluctuations in the medium-term

CITY SNAPSHOT

Office | Retail | IT-BPM | Manufacturing | Pharma | BFSI | Consulting

BENGALURU

READY REITABLE STOCK

Office: 84.3 | Retail: 7.0

KEY OFFICE SUBMARKETS

	Outer Ring Road	Suburban East	Peripheral East
Demand Drivers			
Share in net absorption	57%	7%	7%

DELHI - NCR

READY REITABLE STOCK

Office: 54.6 | Retail: 8.3

KEY OFFICE SUBMARKETS

	Gurgaon Others	Gurgaon CBD	Noida
Demand Drivers			
Share in net absorption	46%	10%	26%

MUMBAI

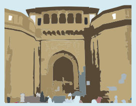
READY REITABLE STOCK

Office: 35.1 | Retail: 10.0

KEY OFFICE SUBMARKETS

	Western Suburbs	SBD	Peripheral
Demand Drivers			
Share in net absorption	33%	8%	25%

PUNE



READY REITABLE STOCK

Office: 34.9 | Retail: 6.0

KEY OFFICE SUBMARKETS

	SBD East	PBD West
Demand Drivers		
Share in net absorption	61%	19%

KOLKATA

READY REITABLE STOCK

Office: 5.8 | Retail: 2.6

KEY OFFICE SUBMARKETS

	Rajarhat	Salt Lake
Demand Drivers		
Share in net absorption	3%	74%

HYDERABAD

READY REITABLE STOCK

Office: 25.9 | Retail: 2.4

KEY OFFICE SUBMARKETS

	Madhapur	Gachibowli
Demand Drivers		
Share in net absorption	67%	18%

CHENNAI

READY REITABLE STOCK

Office: 36.7 | Retail: 4.0

KEY OFFICE SUBMARKETS

	Suburban South	South-West
Demand Drivers		
Share in net absorption	29%	NA

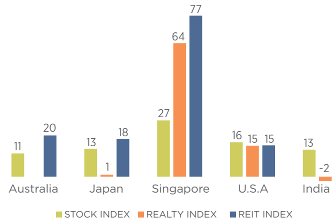
Notes:
Ready REITABLE Stock in MSF as of September 2016
Share in Net Absorption during Jan-Sept 2016
Share in city's total office net absorption

REIT INDICES

Among the four countries compared here, the highest annualized 5-year returns in the REITs index is seen in Singapore. As of October 2016, the FTSE S-REIT Index gave 5-year annualized returns of 76.63%, outperforming the FTSE Realty Index, which gave returns of 63.54%. On the other hand, the country's broader Strait Times Index's annualized 5-year returns were seen at 26.72% as of October 2016. Strengthening office space and industrial demand over the years, as well as Singapore's ability to attract foreign investments have further led to strong fundamentals of the Singapore REIT market.

Australia too has seen the REIT index outperforming the broader XAO Index. The REITs index gave returns of 19.59% on a 5-year annualized basis, while that of the country-level broader AOX index's returns is lower at 11.04%. Japan joins the league of the REITs index outperforming the broader indices with FTSE J-REIT reaping 5-year annualized returns of 17.89%, partly due to negative interest rates in Japan.

Return on Investments across Indices



Australia (XAO, A-REIT)
Japan (NIKKEI, TOPIX-17 REALTY INDEX, J-REIT)
Singapore (STI, FTSE REALTY INDEX, FTSE S-REIT)
US (DJ STOCK MARKET, DJ REALTY INDEX, DJ REITS INDEX)
India (BSE Sensex, BSE Realty Index)

Source: S&P, FTSE, Nikkei, Bloomberg

In India, the S&P BSE Sensex Index's gave 5-year annualized returns of 12.84%, while the S&P BSE Realty gave negative returns of 2.18% owing to sluggish demand in the residential sector affecting the listed companies' financials. The Realty Index reached its peak in December 2007 and thereafter lost 88% of its value by November 2016. However, since January this year, the Realty Index has recouped 10% of its value, helped by increased regulatory clarity and improved economic environment. Going ahead, REITs would help attract funds into the sector and help developers resolve their fund-raising issues and allow them to focus on completing their projects in a timely manner.

KEY TAKEAWAYS FOR REITS IN INDIA

A study of REIT regimes across countries shows that the first few years of the REITs regime have been tumultuous as the market and investors take time to adapt to the new regime. The returns after the initial teething stage has been strong enough in most markets to keep investors attracted to this investment avenue and further develop the real estate markets in those countries. Below is a brief overview of a key event in the REIT market of each country, its implication and the learning for India to avoid similar pitfalls.

JAPAN

In Japan, REIT regulations were formulated in 2000, with two swift listings the very next year. However, the first two listings saw slumping of price due to deterioration in the office market conditions in Japan, arising from a glut in supply, as well as lack of trust in these new investment vehicles (REITs). This led to a mismatch in the demand-supply scenario in the market, resulting in a high vacancy levels. The price-to-book ratio[14] hovered above 1[15], after the first year of anxiety around REITs when the price-to-book ratio slumped below 1. However, after the initial two years, investors garnered confidence to pump funds into REITs. Moreover, in 2003, the tax rate for REITs was lowered, which led to better performance and higher prices of REIT. By now, the REIT market gave higher dividends than expected, with an upward trajectory. The success of REITs led to nearly 14 listings by the end of August 2004.

Following the global financial crisis in 2008, several REITs merged and one REIT even went bankrupt due to plummeting property prices. The market took several years to recover from the crisis, with REIT prices reviving only in 2012. As of 2016, Japan has over 53 REIT listings and with a total market capitalization of USD 110 billion[16].

14. Price-to-book ratio examines the market capitalization of the stock, relative to the book value on the balance sheet
15. The Association for Real Estate Securitization
16. The Association for Real Estate Securitization

KEY TAKEAWAYS

In the initial stage, the Japanese REIT market went through a downturn led by relatively higher vacancy levels in the realty market as supply exceeded demand. Currently, India's vacancy levels for Grade A office development as of September 30th 2016 is seen at 17%. Moreover, with improving economic visibility and strong demand for office space by occupiers, going ahead, the commercial market is likely to witness an upswing in rentals and demand. For perspective, approximately 20.3 msf of space has been pre-committed by occupiers during the years 2015 and YTD 2016, signaling strong demand pipeline going ahead.

KEY CITIES	VACANCY RATE (GRADE A)
Bengaluru	7.2%
Chennai	9.8%
Delhi-NCR	27.4%
Mumbai	19%
Pune	11%
Hyderabad	7.4%

Additionally, in India, existing REIT policies are conservative and do not allow investments in foreign assets, as compared to other countries wherein REITs can invest in overseas assets. Such regulations in India would help safe guard investments against risks such as exchange rate fluctuations, dependency on economic growth and real estate market performance of other countries, etc., especially in present economic conditions wherein several developed countries are undergoing economic slowdown. Overall, the time is opportune for REITs to be launched in India as the Indian commercial office market fundamentals are strong with low-to-moderate vacancy levels in top cities of India.

SINGAPORE

While REIT regulations were floated in 1999, the Singapore market witnessed the launch of some REITs in 2002. Until 2005, REITs were faced with under-subscription largely due to the under-performing economy and lack of tax incentives. In an effort to make REITs attractive, the Singapore government introduced tax incentives such as remission of Stamp Duty in 2005 that helped in the rapid expansion of REITs in the country and also made Singapore's REIT market competitive against other Asian countries. As of 2014, REITs comprised 34%[17] of the total real estate market in Singapore. Singapore was the first country in Asia to allow overseas investments. It currently has 32 REIT listings with a market capitalization of USD 48 billion[18].

The learnings from the initial years of the REITs market in Singapore and Japan show that India is now well-placed to witness the listing of REITS. Under-construction assets may hold maximum potential for Indian investors, as existing office portfolio of most large developers are in the process of being divested. Since REITs are permitted to invest up to 20% of their fund value into under-construction assets, investors may have to wait until delivery of projects to build a portfolio of completed projects.

Strengthening demand in the commercial office sector, and various government incentives such as relaxed FDI norms across multiple sectors would spur demand for office space, thereby aiding the growth of REITs.

Moreover, the government's 'Make in India' scheme, and commencement of several infrastructure projects across cities would augment economic growth and improve business confidence, thereby bolstering demand for office space. This would likely be a huge catalyst for the growth of REITs in India, going ahead.

KEY TAKEAWAYS

One of the major challenges in implementing REITs in India has been the taxation structure, which made REITs less attractive for investors. However, over the last year, the government has cleared the deck in not only easing taxation policy, but also easing regulations. Measures such as increasing the number of sponsors (five sponsors, from three allowed earlier), easing the investment cap in under-construction assets (allowing up to 20% of the investment fund in under-construction assets, from 10% earlier), removal of dividend distribution taxes, etc. have warmed up investors to REITs in India.

17. 'Overview of REITs' Morgan Stanley
18. Bloomberg (as on March 2016)

OTHER CHALLENGES POSING REITS IN INDIA

Whilst we have identified some of the learnings that India can take away from other countries, the following factors could pose as major challenges to the evolution and success of a REITs market in India.

High interest rates in India

Term-deposit rates in other countries are significantly lower than those of India, where they hover between 4-7.5%. These low term-deposit rates in other countries have played a major role in steering investments into their REITs as they gave higher returns. In India, higher term-rates deposit rates and several other instruments offer high returns, e.gs. Public Provident Fund offer 8.1% and Non-Convertible Debentures (NCDs) 9-12%. These instruments with comparatively higher interest rates may pose as major deterrents for retail investors ploughing in funds into the Indian REITs market.

Term-deposit rates

	LOW	HIGH
INDIA	4.00%	7.50%
AUSTRALIA	1.50%	3.20%
SINGAPORE	0.05%	1.20%
JAPAN	0.01%	0.24%
USA	0.01%	0.55%

Risk-averse household investment trend

While India's stock market has been growing at a rapid pace, majority of India's retail investors still prefer to park money with banks or in gold as they typically offer stable returns and directly in real estate. The high risk associated with the equity market has typically deterred households from investing in stocks and debentures. In FY 2015-16, savings in equities and debentures accounted for only 6% of the total household savings during the year. This risk-averse attitude could also make investors cautious of investing in REITs. However, the silver lining is that investments in equity markets and debentures are the fastest-growing investment products. Investment in shares and debentures has seen a consistent rise over the last five years, with investment jumping 72% in FY2015-16 from that of the preceding year. Going ahead, the growing quantum of investments in equities and debentures could usher greater acceptance of REITs.

Tax structure of REITs

Taxation norms are extremely critical to the success of REITs in any country. While the Indian government has taken strides in relaxing taxes for REITS (such as exemption of Dividend Distribution Tax for business trusts), there are several other taxes that would hamper the profitability of the trusts. Under the current regulations Capital Gains Tax is applicable to REITs, apart from Stamp Duty charges at the state level. Moreover, Value Added Tax (VAT) and Service Tax or the uniform Goods and Services Tax (GST), once it is implemented, are applicable on under-construction properties. Such taxes could therefore increase the total acquisition costs for any under construction assets. Therefore, the existing tax structure that is applicable on REITs in India may contribute in lower overall returns that the REITs can potentially offer. Most countries with REIT framework provide exemptions and discounts to REITs, which help in improving their profitability and the returns to investors.

Highly unorganized market

Despite over 6% contribution to the GDP, the real estate sector in India has been highly unorganized, until now. Therefore, only about 45% of the office stock and 56% of the retail stock is eligible for REIT investments. Moreover, the policies and procedures vary for every State across India where governing and regulatory bodies are further decentralized, which could make functioning of REITs a challenging process, especially if a REIT has a portfolio that is spread across multiple cities and states.

Sectorial dependency for growth

The IT-BPM sector accounts for more than half of the commercial office leasing in the top cities. The growth of the sector, is dependent on several external factors such as the growth of the US economy, changing outsourcing policies of various countries, changes in technology and needs of clients, etc. which could make the sector more susceptible to external risks. With over 75% of the REIT eligible stock (ready and under construction) being concentrated in the IT and IT-SEZ developments, the growth of REITs in India would largely hinge upon the roadmap of IT-BPM companies.

Geographical concentration & lack of availability of investable stock

The top 3 cities (Bengaluru, Delhi-NCR and Mumbai) account for about 63% of the total REIT eligible stock. Moreover, a large proportion of the office stock is already divested or in process of being divested and may not be offered in a REIT. Owing to the limited availability of eligible preferred stock, the overall REIT investments may remain undersized.

SECTOR OVERVIEW AND PROJECTIONS

OFFICE SECTOR

In the backdrop of improving economic performance and business confidence, the commercial office leasing activity sustained momentum from last year whilst the investment activity saw increasing interest resulting in some landmark deals. Though the net absorption activity in Grade A developments across the top eight Indian cities[19] during January – September period was subdued at 16.7 million square feet (msf), it is likely gather pace and end the year at 29 to 30 msf, similar to last year. The construction pipeline is also robust and we expect the total new supply in 2016 to be around 35 msf across the top eight cities.

OFFICE STOCK DOUBLES IN LAST SEVEN YEARS; ROBUST PIPELINE EXPECTED

The commercial office construction activity across the top eight cities has been robust with Grade A inventory as of September 2016 doubling in last seven years at 434 msf. The top three cities of Bengaluru, Delhi-NCR and Mumbai now contribute 65% of the total Grade A stock[20], indicating that despite other cities such as Pune and Hyderabad seeing a spurt in developer activity, the pace of activity in the top cities maintained momentum. Over the years, developers have identified newer growth locations in these cities for new and existing businesses to expand and establish their presence.

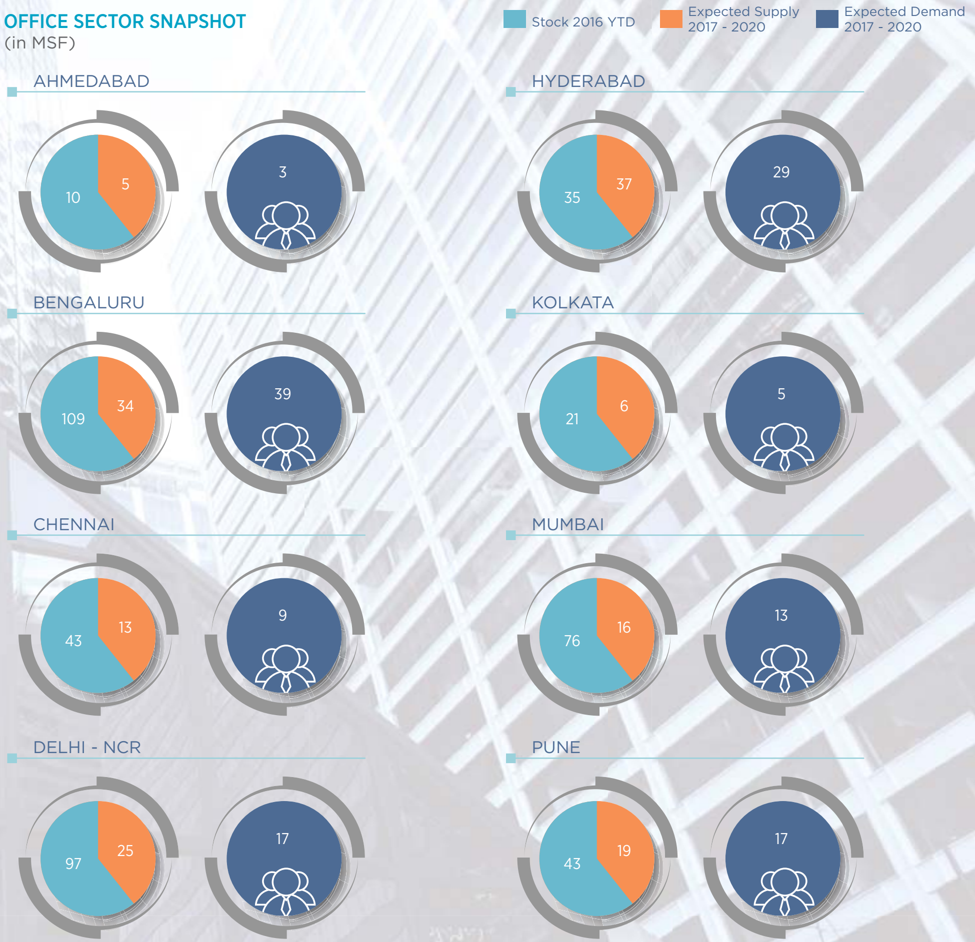
During the January-September 2016 period, supply declined by 7% compared to same period last year owing to delays in building completions. Grade A new developments across eight cities were noted at 22.3 msf in the said period with highest infusion of 5.5 msf recorded in Bengaluru, followed by Mumbai and Delhi-NCR. Supply in Bengaluru was impacted by the municipal authority's reassessment of building sanctions, despite which, the IT city's supply was seen to be the highest amongst all cities during the first three quarters of 2016. While overall supply moderated this year, the next four years (2017-2020) will see a compounded annual growth rate of 8 to 10% in Grade A inventory across eight cities, with approximately 156 to 190 msf of fresh supply expected. This indicates the bullish stance of developers as office leasing is expected to steadily grow ahead, whilst the industry institutionalizes further.

Hyderabad, touted as the next big growth-city, is expected to witness the highest Grade A supply of 37 to 40 msf over 2017-2020 as developers bet on the IT-BPM sector's expansion to steer future demand. In 2018, supply in Hyderabad is expected to overtake that of Bengaluru. The state government has planned and implemented several infrastructure and commercial development projects across the city such as the Transit-oriented growth corridor, Information Technology Investment Region (ITIR), Strategic Road Development Plan and the Hyderabad metro. These initiatives are expected to give Hyderabad a competitive edge over other cities in the medium term. Hence, in light of such measures, grade A inventory is expected to double going forward in next 4-5 years, majority (almost 60%) of it catering to the IT sector.

Meanwhile, construction activity in Bengaluru too is likely to be robust with 34-38 msf of supply likely to be delivered in next 4-5 years, with majority comprising of commercial office developments. The IT-BPM sector will continue to be the major demand driver in Bengaluru, apart from continued demand from the consulting and BFSI sectors. Delhi-NCR[21] is expected to witness 25-30 msf of new office space between 2017 and 2020, with majority of the space expected to come up in Gurgaon.

19. Ahmedabad, Bengaluru, Chennai, Delhi-NCR, Hyderabad, Kolkata, Mumbai and Pune
20. As of September 2016
21. Delhi, Gurgaon and Noida

OFFICE SECTOR SNAPSHOT
(in MSF)



EXPECTED SUPPLY & DEMAND - YEAR WISE

Note: Figures for Grade A developments

STEADY DEMAND TO TAPER VACANCY LEVELS

The delays in completion of buildings in preferred submarkets in cities such as Bengaluru, Hyderabad and Delhi-NCR led the plunge in net absorption during the January-September period this year. The net absorption in Grade A developments was recorded at 16.7 msf, lower by 20% compared to same period last year. Except Delhi-NCR, Hyderabad and Ahmedabad, all the remaining cities saw negative annual growth during the said period. Some part of the lower net absorption can be attributed to lack of quality supply.

Bengaluru continues to account for the highest net absorption with 32% share in YTD 2016 followed by 19% of Delhi-NCR and 15% of Hyderabad.

The year 2016 is expected to end at around 30 msf, similar to that of the previous year, although demand is likely to gather pace in subsequent years owing to strengthening business confidence and optimistic economic outlook. Net absorption compounded annual growth is anticipated at 3% until 2020 which is higher than the growth seen in the last five years.

Bengaluru will continue to account for the majority share (30%) of the projected net absorption during 2017-2020. Hyderabad is expected to follow Bengaluru with 29.5 msf of cumulative net absorption during 2017-2020 representing a 22% share owing to increased traction of occupiers as the state offers supportive policy measures for the IT-BPM industry. Factors such as competitive rentals in Hyderabad, availability of land parcels and a proactive policy stance by the Telangana government have been instrumental in not only attracting existing IT-BPM companies to expand in the city, but also inviting other companies to foray into the city.

Pune and Delhi-NCR are expected to see similar contributions to net absorption of around 17.2 msf each during 2017-2020 due to sustained leasing from IT-BPM sector, which has and will continue to be the primary demand driver. Pune's share in overall net absorption is likely to rise to 16% during 2017-2020, from a 12% share in net absorption between 2012-2014, owing to availability of quality talent graduating from the city's robust educational system. Also, proximity to Mumbai and lower operating costs have added to the lure of Pune.

SECTORIAL LEASING

While the IT-BPM sector continues to be the prominent demand driver in majority of the cities, the share of IT-BPM sector fell from 50% in 2015 to 48% as of September 2016. In turn, other sectors such as consulting, e-Commerce and engineering & manufacturing witnessed a surge in their respective shares. The consulting sector's share grew to 8%, from 6% last year. When compared over a five-year period, the consulting sector's share grew from a mere 5% in 2012. The e-Commerce sector, which has negligible share of 1% in 2012, has seen its share grow to 6% in 2016. Incidentally, while the share of engineering and manufacturing has risen year-on-year, the share has declined from 10% in 2012 to 6% last year, despite the government's emphasis on the manufacturing sector.

Overall vacancy level across the top eight cities, which was seen at 17.3% at the end of September 2016, is likely to taper to 16.6% by the end of 2020 given the reducing growth rate of new supply infusion and steady absorption activity. Among the top cities, Bengaluru, Kolkata and Pune are expected to see a drop in vacancy levels by the end of 2020, as compared to September 2016. Given the present known supply pipeline, Bengaluru is likely to see a steep fall in vacancy levels from 7.2% as of September 2016 to 1.6% by the end of 2020. However, we do expect some more supply to come online and the vacancy rate to be around 5% around 2020. The current vacancy levels and future projected supply is expected to meet the anticipated demand, even as occupiers continue to make a beeline for the city.

The rental values across most cities will see a compounded annual average growth upto 5% compared with 2016. The steepest rental increases are noted to be in Bengaluru and Hyderabad, wherein stong demand would drive rentals in key submarkets.

IMPACT ON REAL ESTATE

The increase in office demand in the coming years is likely to be substaintiated by increase in stock, abeit at a lower pace and is likely to be landlord favorable in a few markets. Cities such as Bengaluru and Pune are expected to be landlord favorable as the vacancy levels will be in single digits by 2020. Occupiers should plan their real estate strategy keeping in mind the supply and availability constraints as landlord/ownership profile of office spaces will continue to undergo a change as institutional investments increase further and REITs make their mark in the coming years.

Among the new and growing trends is that of 'co-working spaces,' which is gaining popularity with a number of providers signing up for large spaces foreseeing the potential demand from mid-scale and start-up occupiers. Co-working spaces not only provide modern work places, but also enable flexible staffing option to occupiers at relatively lower cost compared to a full-term lease to tide over sudden or small term needs for office spaces. The demand for co-working spaces is expected to co-exist with regular leases as many companies may also opt for a hybrid approach to keep costs under control.

Sectorial Leasing

	2014	2015	2016 YTD
IT-BPM	53%	50%	48%
BFSI	13%	9%	9%
Consulting	4%	6%	8%
E-commerce	1%	4%	6%
Engineering & Manufacturing	6%	5%	6%
Pharma & Healthcare	4%	5%	3%
Others	18%	21%	20%

Others includes sector such as Energy & Chemicals, Media, Logistics, Automobile, FMCG, Telecom, etc

RETAIL SECTOR

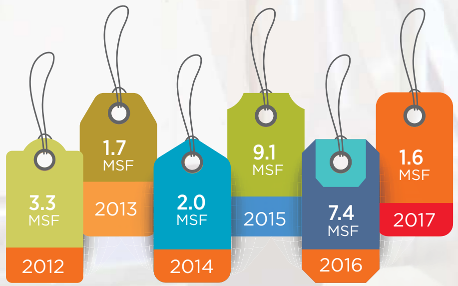
The Indian retail sector is undergoing an exciting period as it straddles the world of home-grown brands, kirana stores, a plethora of foreign brands and the burgeoning e-Commerce sector. Although unorganized retail forms a major chunk of the retail sector in India, organized retail (comprising 8% of total retail) has been expanding over the last decade-and-a-half, along with the exploding growth of the e-Commerce market. The Indian consumer is riding the wave of rising income, coupled with exposure to global trends and higher aspirations, providing a huge opportunity to retailers in India.

While foreign retailers have shown interest in India over the years, mall supply in Indian cities has grown at a slow pace over the past few years, exacerbated by the economic slowdown, delays in building completions due to lack of investors' interest. However, the year 2016 has emerged as a game-changer for the retail sector. The organized retail space that was witnessing a slack for the past few years, has shifted gears and is attracting retailers as well as investors. Higher investors' interest and anticipation of a revival of the retail sector is steering developers to focus on completing their under-construction malls.

As a result, during the first three quarters of 2016, the top eight Indian cities witnessed 10 malls becoming operational – amounting to 5.31 msf of mall space. This year marks the highest number of malls becoming operational since 2012. Delhi-NCR accounted for the highest supply during YTD 2016, followed by Mumbai and Pune. The new mall spaces are expected to provide quality spaces to retailers, and wider options for expansion across multiple cities. Delhi-NCR accounted for 58% of the share in new supply during YTD 2016 on account of the completion of Mall of India (one of the largest malls in India). Mumbai witnessed two malls becoming operational, spanning a total of 850,000 sf during the same period, while Pune also witnessed 840,000 sf of mall space (3 malls became operational) coming into supply.

With these supply additions, operational retail mall stock for the top eight Indian cities has increased to approximately 75 msf as of September 2016. Delhi-NCR and Mumbai remain the largest retail markets, accounting for 35% and 21% respectively of the mall stock across the top 8 cities in India. Bengaluru is the third largest market, accounting for about 11% of the total stock closely followed by Pune. Hyderabad, on the other hand, continues to remain the least penetrated market with operational space of only 2.9 msf.

Mall Supply



STRONG MALL PIPELINE

Going ahead, the mall pipeline is likely to remain strong. According to Cushman & Wakefield Research, approximately 12.75 msf of retail space spread across 31 malls is expected to become operational by 2018-19 in the top eight cities. Chennai is expected to account for the maximum share accounting for 24% of the upcoming supply. Mumbai, Hyderabad and Bengaluru are expected to witness 18-20% each of the expected mall space over the next 2-3 years. Interestingly, the southern cities of Chennai, Bengaluru and Hyderabad are expected to witness the opening up of nearly 19 malls over the next 2-3 years. In terms of number of malls, Hyderabad is expected to get 7 malls by 2018 - the maximum number of malls - which would give a thrust to the city's unpenetrated organized retail market. Hyderabad will be followed by Bengaluru and Chennai, which would each see 6 malls getting operational over the next 2 years.

Overall mall vacancy level for the top eight cities has largely remained stable at 15.6% as of September 2016 led by revival in demand amidst higher supply additions. Despite vacancy levels declined by 2%, Ahmedabad continues to witness the highest mall vacancy levels of 31.1%, as of September 2016 as the city continues to reel under sluggish retailer activity. Delhi-NCR's vacancy rates were seen to be the second highest vacancy rate (17.1%), owing to over-supply of mall spaces. Mumbai's mall vacancy levels dropped by 1.2 percentage points from last year to 16.3% at the end of September as retailers picked up space at a fast pace. Retailers across food and beverages (F&B) and apparels segments continued to expand their footprint across select malls and main streets in the city. At the same time, as of September 2016, mall vacancies in Chennai, Hyderabad and Pune largely remained range-bound from last year.

RENTAL TREND

Mall rentals remained largely range-bound across key markets in the top 8 cities, except for select submarkets in Delhi, Mumbai and Pune. Mall rentals in South Delhi witnessed an appreciation of 20% on a y-o-y to INR 600/sf/month. In Mumbai, the average mall rentals in the Goregaon rose by 8% on a y-o-y basis on the back of sustained demand from F&B and apparels retailers.

Rentals in high streets saw a mixed trend across the top eight cities. At the end of September, the submarket of Cathedral Road – RK Salai Main Street in Chennai witnessed the highest increase, with rentals increasing by 14%, compared to the year-ago quarter. This was closely followed by the main streets of Rajouri Garden and Connaught Place in Delhi-NCR and Fort / Fountain in Mumbai, where rentals increased by 10-13% at the end of September 2016.

At the same time, the steepest rental value decline was noticed in Greater Kailash I where rentals fell by 16% on a y-o-y basis, as the market saw a huge churn with advent of restaurants and a few fashion stores exiting. Sector 18, Noida also saw decline in rentals by 11% on a y-o-y basis to INR 200/sf/month owing to available spaces in mall in the vicinity with better parking and other facilities. Delhi's Khan Market with rentals of INR 1250/sf/month continued to be the costliest main street in India. In most of the other main streets across the top 8 cities, rentals largely remained stable or witnessed marginal variations from those prevailing in the last year.

OUTLOOK

At a time when the brick and mortars retail market is witnessing the onslaught of fierce competition from the e-Commerce segment, malls owners are gearing up in their own way to attract footfalls. Over the last two years, developers have been promoting their malls as destination centers that create experiences through various entertainment and dining options, movies, and various activities for all age-groups, apart from shopping. Moreover, as foreign players descend into India, malls are undergoing significant churn in tenant mix to accommodate such brands, especially in the apparels segment.

Going ahead, the omni-channel retailing approach could be the biggest game-changer for the sector as retailers integrate online and offline models of retailing with much more vigour. Physical retailers have already recognized the wide reach of e-Commerce and are now keen to build their online reach to increase their touch-points. On the other hand, e-Commerce players are keen to expand into main streets and malls. Such a transition would enable retailers to cater to a wider range of customers, who are provided with a better shopping experience wherein they can touch and feel the products. Over the last three years, online retailers such as Lenskart, PepperFry, Firstcry have opened their stores in high streets across cities such as Bengaluru, Hyderabad and Delhi-NCR. Amazon India too has entered into a few partnerships to expand the e-commerce giant's rural presence. Over the next few years, a larger number of retailers are likely to adopt such a viable retail model that will require them to be present across various channels, driving consumption through physical stores, websites, apps, tablets and social media.

Another facet that would change the face of the retail sector is the implementation of the central Goods & Services Tax (GST) as it will help to rationalize product prices across the country, making them more appealing to customers and also help retailers in streamlining their supply-chain processes in an efficient manner. With the removal of hurdles of state boundaries post GST, retailers will mostly have large, centralized or regional warehouses instead of small, local warehouses in each city and / or state. This would remove supply-chain bottlenecks that retailers currently face and lead to better distribution channels in a seamless manner. As a result, retailers would experience lower logistics costs and see lower wastage of products, especially in the perishable goods commodity. With leaner supply chains, retailers can take advantage of economies of scale and reduce their operating costs.

RESIDENTIAL SECTOR

The Indian residential real estate sector has remained sluggish with unsold inventory levels remaining high in key markets in the last couple of years. The end-user demand has remained a sticky point with the residential sector grappling with a perceptible inventory overhang that is forcing developers to control new supply and focus on completing their existing projects. The top eight cities[22] saw a 28% decline (y-o-y basis) in unit launches as a result of subdued demand during 2015.

After witnessing a slowdown in launches in 2015, 2016 YTD saw the launch of approximately 90,000 units across the top eight cities in India (recording an increase of 16% year-on-year). This was fueled by a two-fold rise in launches in the affordable housing segment which constituted nearly 30% of the total unit launches during the period as developers foresee greater pent-up demand in this segment. On the other hand, mid-segment continued to be the mainstay of developers although unit launches dropped by merely 2% in YTD 2016. Launches in the residential sector has been a mixed bag this year with some cities witnessing a revival in launch units, while others still seeing low activity levels. Overall sales velocity are still low and consequently, the total launches have been low compared to the highs seen in previous years.

It is pertinent to note that prolonged lower sales volume can be attributed mainly to the price mismatch between the available supply and buyers' expectations especially in the affordable and mid segments. Besides the low sales velocity, another important reason for the relatively lower launches is that developers have started gearing up for the Real Estate Regulatory Authority (RERA) Act that is to be enforced from next year. Further, the recent currency demonetization move by the Indian Government is expected to have an adverse impact on new launches and sales volumes, both in the primary and secondary markets. We expect developers to hold back on their launch plans as they wait and assess the full impact of this move.

Delhi-NCR, which accounted for the highest share of unit launches in YTD 2015, saw its share down to 10% during YTD 2016 as developers remain wary due to mounting unsold inventory and sluggish sales. Delhi-NCR has witnessed a marked drop (37% from the corresponding period last year) in unit launches as developers are on a wait-and-watch mode until the market improves. On the other hand, Mumbai, which had a share of 14% last year, has the highest share of 21% this year. Mumbai was closely followed by Bengaluru with a share of 18%. Launches in Mumbai were buoyed by a three-fold increase in the affordable segment and formed nearly 15% of the unit launches during YTD 2016 (compared to 8% in the corresponding period last year).

During YTD 2016, affordable housing sector has seen a massive surge of more than 100% in new unit launches as against the same period last year. The remarkable rise in the launch of affordable housing units can be attributed to a steady demand for this segment of housing in key cities of Bengaluru, Delhi-NCR and Mumbai. The government, in recent times, has taken a number of steps to spur affordable housing, such as 100% deduction on profits to housing projects building homes up to a certain limit, and Service Tax exemption for construction of affordable homes measuring up to 60 sq. m. under state and central housing schemes. However, while these tax concessions coupled with relaxation in development norms (e.g. higher Floor Space Index) will make development of affordable projects somewhat financially attractive and viable from developers' perspective, it will be critical to provide a supportive regulatory approval framework to ensure that delivery timelines can be shortened so that more units can be completed within time-frames.

22. Ahmedabad, Bengaluru, Chennai, Delhi-NCR, Hyderabad, Kolkata, Mumbai, Pune

Key Market Movers[23]

Capital values showed a mixed trend across cities based on local market forces. As of 30th September, capital values in Delhi-NCR declined by 2-4% in three submarkets, namely South-West, South-East and South-Central Delhi in the high-end segment, while mid-segments in most submarkets (except Noida) saw stable values since September last year. Bengaluru, on the other hand, witnessed appreciation in two of its submarkets by 10-11%, namely, North and West Bengaluru within the mid segment driven by steady end-user demand. Hyderabad also witnessed a rise in capital values across most of the submarkets in the mid-segment. In case of Mumbai, quoted capital values continued to remain range bound in the last one year. While the quoted values of existing under construction and completed stock have largely remained stable over the last 1-2 years, developers have rationalised prices of newly launched units (with focus on specific segments) in select submarkets to improve their affordability.

23. The values for affordable housing are for units typically priced in the range of INR 2-5 million; values for mid segment are for units in the range of INR 5-10 million except Delhi-NCR and Mumbai, where the range in mid segment housing is typically between INR 5-17 million (20 million for Mumbai). High-end segment values are for units typically priced above INR 10 million except for Delhi and Mumbai (where it is more than 17 million in Delhi and 20 million for Mumbai)

Key Market Movers

CITY	SUBMARKET	KEY LOCATIONS	SEGMENT	% CHANGE IN CAPITAL VALUES (Y-O-Y)
Delhi-NCR	South-west	Shanti Niketan, Westend, Anand Niketan, Vasant Vihar	High-end	-3%
Delhi-NCR	South-east	Friends Colony East, Friends Colony West, Maharani Bagh, Greater Kailash – I, Greater Kailash – II,	High-end	-4%
Delhi-NCR	Noida		Mid	-4%
Bengaluru	North	Hebbal, Bellary Road, Yelahanka, Doddaballapur Road, Hennur Road, Thanisandara Road	Mid	11%
Bengaluru	West	Mysore Road, Uttarahalli Main Road, Magadi Road	Mid	13%
Chennai	Velachery		Mid	11%
Chennai	Suburban (South)	Alandur, Ekkatuthangal, Adambakkam, Nanganallur, Medavakkam, Perumbakkam, Pallavaram, 200 ft. Road, Vandalur-Kelambakkam Road	Mid	18%

Note: The change in capital values have been calculated as of September 2016

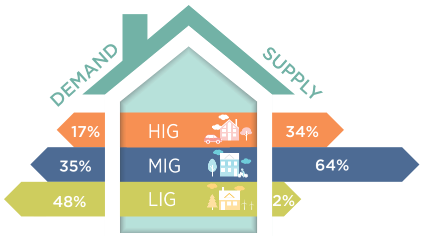
Demand scenario

The levels of urbanization is expected to accelerate from 31% in 2011 to nearly 40% by 2030 with urban population anticipated to increase from 377 million to 590 million[23] during the same period. The government's 'Make in India' initiative is expected to fuel a tremendous demographic shift by reducing the dependence on agriculture and providing higher employment to the rural poor, leading to a burgeoning urban population. Thus, rapid migration, increasing income levels and changing urban demographics, will place increasing pressure on the cities to provide housing for the growing population.

As per Cushman & Wakefield Research estimates, total demand for urban housing is expected to reach 4.2 million units during the period 2016-2020 across the top eight cities. Delhi-NCR (NCT, Ghaziabad, Faridabad, Gurgaon and Noida) continues to garner the highest proportion of demand (24%) at around 1.0 million units by the end of 2020. Key industrial initiatives such as the Delhi-Mumbai Industrial Corridor, continuous improvement in infrastructure, and smart city developments are some of the major initiatives that are expected to generate higher employment opportunities and continue to attract migrants from the adjoining districts. Mumbai and Bengaluru will follow Delhi-NCR and will be generating housing demand of about 711,000 and 686,000 units respectively over the next five years. The improving political environment has triggered investment activity in Hyderabad, which has been reflected in terms of heightened activity in commercial office leasing over the last few quarters. This momentum is likely to continue and augur well for the residential demand in the city over the next 4-5 years and thus account for about 12% (518,000 units) of the housing demand.

The Lower Income Group (LIG) accounts for majority of the urban housing demand at 48%, translating into a total demand of 1.98 million units by the end of 2020. The Mid Income Group (MIG) continues to occupy a sizeable proportion and is expected to generate demand of about 1.46 million units by the end of 2020 - accounting for 35% of total demand. Factors such as higher disposable income, easy availability of credit, improving regulatory scenario leading to greater transparency and expectations of the interest rates for mortgages reducing in the short to medium terms are expected to boost the aspirations of first time home-buyers. On the other hand, the High Income Group (HIG) – a category that is already well-catered to - is expected to generate demand of around 717,000 units across the top eight cities between 2016 and 2020.

Cumulative Demand- Supply analysis 2016 - 2020



23. Report on Trend and Progress of Housing in India, National Housing Bank

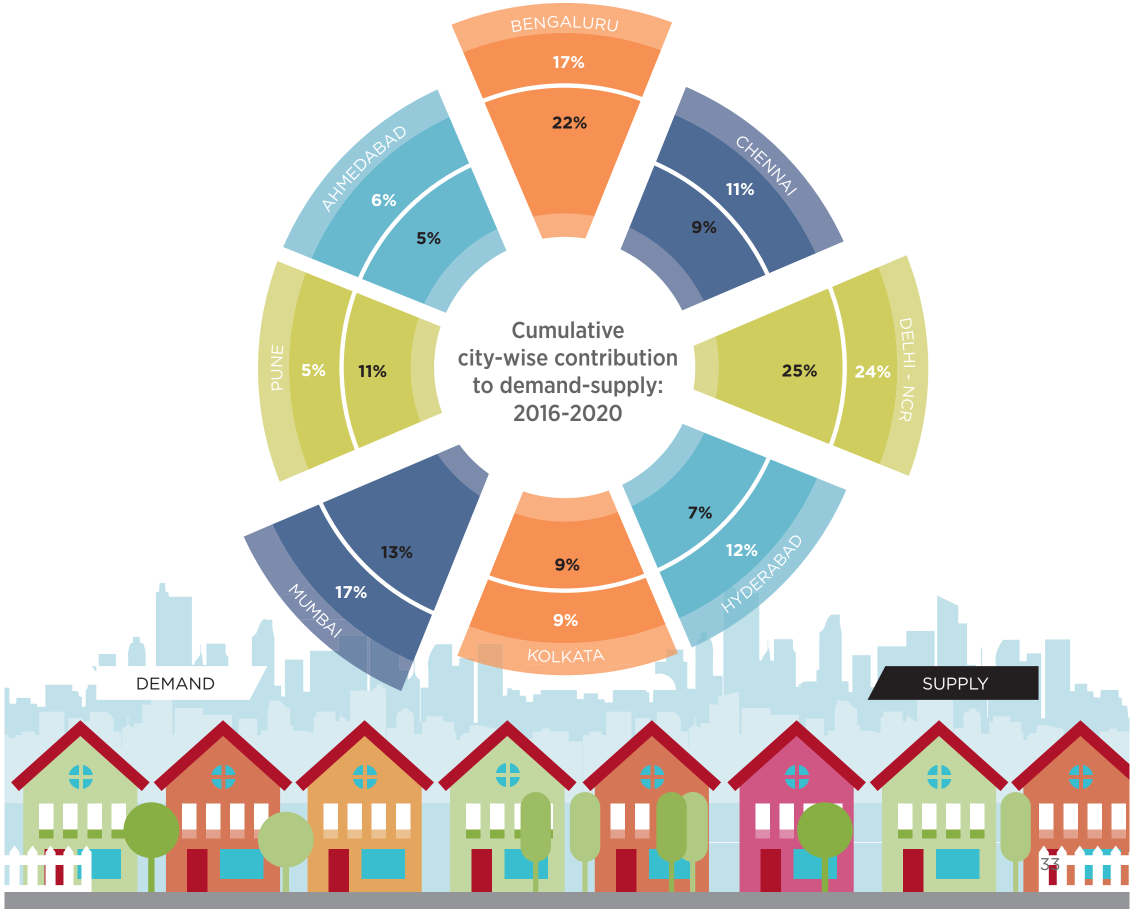
Supply scenario*

During YTD 2016, residential asset class continued to be the preferred investment avenue and accounted for about 54% of the overall PERE investments. Thus, anticipated higher investments coupled with implementation of RERA are expected to accelerate projects completions over the next few years. Accordingly, existing under-construction and planned supply of 1.0 million housing units by private developers is expected to be delivered across top eight cities between 2016 and 2020. However, there exists a huge demand-supply mismatch, given that estimated demand is roughly 4.1 times more than the supply expected across the top eight cities. On the lines of demand, by the end of 2020, Delhi-NCR is expected to witness the supply of approximately 253,000 units by private developers, followed by Bengaluru at around 220,000 units over the same period.

Over the last couple of years, developers have been realigning their project portfolios to tap the hugely under-served and growing demand from the LIG and MIG segments. However, present supply pipelines suggest that only 2% of the supply that is expected to be completed by 2020 will cater to LIG segment, while 63% of the supply will cater to MIG and the balance 35% to HIG.

CATEGORY	DEMAND	SUPPLY
LIG	Households earning up to INR 200,000 per annum and above poverty line	Units priced below INR 1.5 mn
MIG	Households earning INR 200,001 to INR 1mn per annum	Units priced in the range of INR 1.5 to 7.0 mn
HIG	Households earning above INR 1mn per annum	Units priced above INR 7.0 mn

*Private developers led



Demand-supply gap analysis

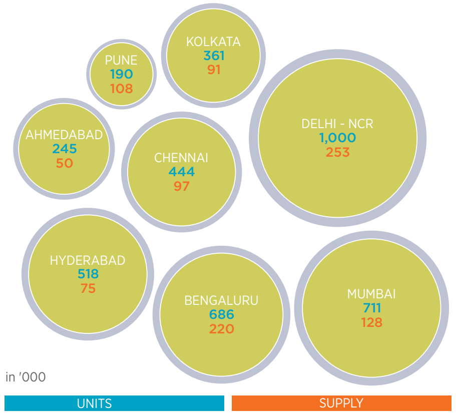
Our analysis indicate that LIG continues to be highly under-penetrated in most of the cities covered as a part of our study. There exists a huge gap that remains untapped and is estimated at about 1.96 million units. To provide a perspective, LIG, that is likely to generate demand of about 1.98 million units (nearly 2.8 times the demand in the HIG segment), is expected to witness supply of barely 25,000 units. LIG continues to be a neglected segment amongst private developers and constitutes a miniscule proportion of the expected supply over the next 4-5 years. While private developers are slowly recognizing the huge mismatch in demand for housing units and supply in the LIG segment only a handful are designing their product portfolios accordingly. Hence, the segment warrants significantly higher supply traction in the coming years.

While MIG accounts for 63% of the total housing supply across eight cities between 2016 and 2020, the segment's housing shortfall has been estimated at 56%. However, the narrowest gap at 51% would likely be witnessed in the HIG segment. Developers in major cities are already catering to this segment that typically sees high margins. Owing to high land prices in the major cities and the opportunities for higher profits, developers launched a sizeable portfolio in the high-end and luxury categories, thus resulting in mounting pent-up demand for LIG and MIG segments. However, though there is a still some gap in the demand-supply dynamics for this segment, a number of issues such as poor location, quality, high prices, low to nil growth in capital values leading to poor investor sentiments, amongst others have resulted in creating high unsold inventories in many pockets of the major cities of Delhi NCR and Mumbai.

In terms of housing shortfall in cities, Mumbai, Delhi-NCR, Ahmedabad and Hyderabad are likely to witness the maximum gap in the demand and supply ratio within MIG segment. Within the HIG segment, Mumbai and Pune are expected to witness the lowest deficit as the segment is expected to be adequately catered by developers in relation to demand.

Thus, it is important for the developers to seize the opportunity in the LIG and MIG segments, which together constitute nearly 90% of the housing shortfall in the top 8 cities covered as a part of our study.

Cumulative city-wise gap: 2016-2020



Note: Size of the bubble indicates the size of housing shortfall in terms of number of units

Outlook

The residential real estate sector has been reeling under tremendous pressure on the back of prolonged low sales velocity and the resultant inventory overhang. While the extent of impact has been different across cities with Delhi-NCR hit hardest, markets such as Bengaluru and Hyderabad have been relatively resilient owing to strong end-user demand. Majority of the prospective home buyers are currently fence-sitters, who are in a wait-and-watch mode in anticipation of a correction in property prices. At the same time, developers need to focus on offering the right mix of products (higher focus on LIG and MIG segments) at appropriate price points. Thus, any uptick in property demand will result only from a change in consumers' expectations of economic growth, income growth and rationalization of property prices.

There is a definitive mandate from the government to improve the transparency and accountability in the sector which is expected to go a long way in streamlining this largely unorganized sector. Measures such as the Real Estate Regulatory Act that would be enforced next year would definitely improve accountability in the market, thereby improving consumer confidence. The latest demonetization move of the government is expected to have far reaching impact on the flow of unaccounted money into the sector. In the short to medium term, the sector is expected to be adversely impacted in terms delay of ongoing projects owing to funding crunch, slower off take of units especially in investor-driven markets, etc, the long term impact is likely to be positive and sustainable. In terms of prices, cities with relatively higher investor demand and inventory overhang are likely to witness moderation in the short to medium term.

The combined impact of these measures will help boost consumer confidence, thereby resulting in an uptick of demand in the long term. Further, absorption in the office sector is likely to gain momentum over the next 4-5 years and will also have a trickle-down effect on the residential sector. Thus, demand side factors are expected to pan out positively aided by an anticipated reduction in interest rates. At the same time, the proactive government measures will help the residential sector to attract higher investments enabling developers to fulfil their supply commitments.

OUTLOOK

India is on track to further enhance its position as a key market in the global economy as expectations of high economic growth during the next few years will propel it ahead of most large global economies. The Indian real estate sector is on the threshold of transforming into a much larger, more transparent, better organized and mature sector that could truly be comparable to the well developed and mature markets such as Australia, China (including Hong Kong), Japan and Singapore in the Asia Pacific region. The past few years have seen the government move towards bringing in enabling infrastructure and regulatory frame-works that ease business operations, simplify the country's taxation system, boost demand, promote transparency and protect seller and buyer/investor rights. Against this backdrop, we expect that the real estate sector's growth across all parameters (demand, supply, returns on investment, etc.) will take on new meaning – perhaps similar to what we have seen take place in the country's telecommunication sector where market valuations for efficient operators grew multifold even as prices dropped drastically and inefficient operators were forced to shut shop or merge with other stronger operators.

The residential sector, which has been impacted by negative sentiments and poor sales in the past couple of years, could take some more time to come out of the woods due to the short-term impact of demonetization that is likely to hurt some markets. However, as our demand-supply analysis has shown, there is still a huge gap between the two and the government has already signaled its support to meeting the housing gap through its 'Housing for All – 2022' initiative. Hence, there is still a huge business opportunity for private developers, but they need to change their approach and bring in better strategies, systems, technology and funding options. International developers are already actively scouting the various local markets to identify the right opportunities for themselves; Indian developers will need to gear up to meet their onslaught and remain relevant and profitable. The formation of a Real Estate Regulatory Authority in each of the states next year would enable higher accountability, thereby providing an impetus to investors' and end-user demand whilst ensuring that developers, sellers and intermediaries become transparent and accountable.

The Indian commercial office sector, while driven by the cities of Bengaluru, Delhi-NCR and Mumbai, is likely to see increased momentum from cities such as Hyderabad and Pune by 2020. These two cities, which are already established IT-BPM hubs, would be witnessing traction from companies from other sectors too. Concerns over global occupiers' strategies in the face of uncertainty over the results of the US Presidential election, BREXIT, possible slowdown or recession in many parts of the world are not expected to have a long lasting or adverse impact on the Indian economy. By and large, most global occupiers are committed to growing and expanding their Indian operations and/or looking at new business avenues. Indian IT-BPM companies are also consciously transforming their own operations and strategies to move up the value chain and maintain their stranglehold on global outsourcing businesses despite increasing competition from other emerging economies like the Philippines, Vietnam, Indonesia or those from Latin America or Eastern Europe. Hence, we have conservatively forecasted that net absorption (incremental demand) will grow on an average of 10% over the next few years.

The Indian retail sector, on the other hand, is going through a dynamic period with heightened private-equity interest, fast-paced expansion of foreign fashion brands and aggressive e-commerce companies. We expect the fierce competition between e-Commerce players and physical retailers to play out through the multi-channel approach as retailers look to have higher number of touch-points. The government's thrust on boosting economic growth by growing the contribution of manufacturing to GDP and the streamlining of the tax structure through the GST is likely to increase operational efficiencies in the manufacturing and warehousing sectors. Increased demand from e-Commerce companies and organized retailers, is already giving a thrust to the warehousing sector's standing as an attractive asset class for investors. Similarly, industrial townships and large industrial projects may also see sizeable investments in the next few years as many local and international developers and funds have started evaluating the potential quite seriously. Overall, the next few years hold promise for the entire gamut of asset classes, as the sector gets regulated in a bid to become more transparent.

Finally, riding on the wave of increased investments into the realty sector, we expect REITs to emerge as an important driver of the commercial office and retail real estate sector investments in the medium to long term. While the initial few years may face see some hiccups arising from the new regime of REITs, they have the potential to improve liquidity in the both these sectors and bring in more transparent and globally acceptable practices ensuring the maturity of India's real estate markets.

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VCCIRCLE

DEFINITIONS AND NOTES

APAC: Asia-Pacific

BFSI: Banking Financial Services and Insurance

bn: billion

CAD: Current Account Deficit

CAGR: Compounded Annual Growth Rate

Capital values: Quoted base price per square feet for category of residential property under consideration. It does not include other charges such as Preferential Location Charges, External Development Charges, Internal Development Charges, etc.

CBD: Central Business District

CII: Confederation of Indian Industry

Construction Development: Townships, housing, built-up infrastructure and construction-development projects (which would include, but not be restricted to, housing, commercial premises, hotels, resorts, hospitals, educational institutions, recreational facilities, city and regional level infrastructure)

CPI: Consumer Price Index

Deferred Supply: under construction projects whose delivery timelines have been postponed to

DMIC: Delhi-Mumbai Industrial Corridor

EWS: Economically Weaker Section

F&B: Food & Beverage

FDI: Foreign Direct Investment

FX: Foreign Exchange

CY: Calendar Year

GDP: Gross Domestic Product

GIC: Government of Singapore Investment Corporation

GMV: Gross Merchandise Value

GST: Goods and Services Tax

H1 or H2: first or second half of a year

HIG: High Income Group

IIP: Index of Industrial Production

INR: Indian rupee

Inventory / Stock: The total available constructed space in a micro market / city in square feet

InvITs: Infrastructure Investment Trusts

IT-BPM: Information Technology and Business Process Management

JV: Joint Venture

LIG: Low Income Group

MIG: Mid Income Group

mn: million

MNC: Multinational Corporation

msf: million square feet

NDA: National Democratic Alliance

Net absorption: Incremental new space take-up of commercial office spaces

PBD: Peripheral Business District

PE: Private Equity

Q1, Q2, Q3 or Q4: first, second, third or fourth quarter of a year

QE: Quantitative Easing

RBI: Reserve Bank of India

REITs: Real Estate Investment Trusts

R&R: rehabilitation and resettlement

SBD: Secondary Business District

SEBI: Security and Exchange Board of India

SEZs: Special Economic Zones

sf: square feet

SPV: Special Purpose Vehicle

sq. m.: square metres

Top 8 Indian cities: Ahmedabad, Bengaluru, Chennai, Delhi-NCR, Hyderabad, Kolkata, Mumbai and Pune

TNC: Transnational Corporations

USD: United States Dollars

Vacancy Rate: The total availability of space as a proportion of the existing inventory

Weighted average rentals: Quoted rentals of commercial office spaces, calculated as a proportion of availabilities/ vacancies in these buildings

y-o-y: year-on-year

YTD: Year-to-date

KEY TO OFFICE SUBMARKETS:

BENGALURU

CBD/Off-CBD –M.G. Road, Millers Road, Vittal Mallya Road, Residency Road, etc.

Peripheral South –Electronic City, Hosur Road, Mysore Road

Outer Ring Road –Sarjapur, KR Puram, Hebbal

Suburban East –Indira Nagar, Old Airport Road, C.V. Raman Nagar

Peripheral East –Whitefield

Suburban South –Koramangala, Bannerghatta Road, Jayanagar

Peripheral North –Bellary Road, Thanisandara Road, Tumkur Road

CHENNAI

CBD – Anna Salai, Nungambakkam, R.K. Salai

Off-CBD – T.Nagar, Alwarpet, Kilpauk, Egmore, Chetpet, Royapettah, Kotturpuram

South-west – Guindy, Ashok Nagar, Vadapalani, Manapakkam, Ekkaduthangal

North-west – Ambattur, Padi, Anna Nagar, Koyambedu, Arumbakkam

Suburban South – Perungudi, Taramani, Thiruvanmiyur, Velachery

Peripheral South – Sholinganallur, Thoraipakkam, Navalur, Siruseri, Padur

Peripheral South-west – Singaperumalkoil, Tambaram, Guduvanchery, Perungalathur, Pallavaram

DELHI-NCR

Delhi CBD - Connaught Place

South - East Delhi -Rohini, Shalimar Bagh, Jasola, Munirka, Saket & Nehru Place

Gurgaon CBD - Cyber City and M. G. Road

Gurgaon Others - rest of the city (excludes Manesar); Noida -excludes Greater Noida

HYDERABAD

CBD –Banjara Hills Road No. 1, 2, 10 & 12

Off-CBD –Begumpet, Somajiguda, Raj Bhavan Road, S.P Road, Himayath Nagar

Suburban (Madhapur) –Madhapur, Kondapur, Raidurg

Suburban (Gachibowli) –Gachibowli-Nanakramguda, Manikonda;

Suburban (Others) –Kukatpally, Shaikpet

Prime Suburban –Rest of BanjaraHills, Jubilee Hills

Peripheral East –Pocharam and Uppal

MUMBAI

CBD –Ballard Estate, Colaba, Churchgate, Fort & Nariman Point

SBD –Bandra-Kurla Complex, Bandra East, Kalina

Lower Parel - Lower Parel, Parel and Dadar

Western Suburbs – Andheri – Kurla, Malad Goregaon

Peripheral – Thane, Thane-Belapur, Vashi

PUNE

CBD: Laxmi Road, Camp, Bund Garden, Boat Club, Koregaon Park, Dhole Patil Road, Pune Station, Shivaji Nagar, FC Road, JM Road, Wakdewadi, SB Road, Model Colony, Ganeshkhind Road

SBD East: Kalyani Nagar, Kharadi, Mundhwa, Yerwada, Nagar Road, Viman Nagar, Hadapsar, Kondhwa

SBD West: Aundh, Baner, Pashan, Kothrud, Karve Nagar, Khadki, Paud Road

PBD East: Phursungi, Wagholi, Charoli, Solapur Road, Saswad Road, Katraj

PBD West: Hinjewadi, Wakad, Pimpri, Bhosari, Chinchwad, Bavdhan, Mulshi, Talawade, Tathawade, Nanded, Pimple Saudagar

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GRI is a global club of leading investors, developers and lenders active in Real Estate.

Its mission is to help its members build personal relationships and work together in creating rewarding opportunities, great places and a better world.

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GRI runs its activities through a collection of annual meetings focussed on different regions of the world.

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