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# IT-ITES SECTOR TO DRIVE DEMAND

## Summary & Recommendations

Demand in Chennai slowed with year to date (YTD) absorption declining 13% YoY in Q3 2018. However, the year should close at levels similar to 2017 as many leasing deals that we expected to close in Q3 were delayed to Q4 2018.

- > The Tamil Nadu Information Communication Technology (ICT) Policy, released in Q3 2018, is likely to further strengthen the dominance of technology sector investments in Chennai
- > As the city's office leasing outlook remains positive, we advise developers to adhere to their planned timelines for the upcoming Grade A supply to cater to steady occupier demand

		Q3 2018	Full Year 2018	2018-21 Annual Average
 <b>Demand</b>	> We expect gross absorption to remain consistent over 2019-2021 driven by the technology sector expansions and relocations in the city	760,000 sq ft	4,500,000 sq ft	4,800,000 sq ft
	 <b>Supply</b>	> About 17 million sq ft (1.6 million sq m) likely to be added to the inventory over 2018-2021, increasing the total office stock by 30%	150,000 sq ft	2,500,000 sq ft
 <b>Rent</b>		> Rents likely to continue increasing in the OMR pre-toll and OMR post-toll micromarkets; overall city rents to increase at a CAGR of 2.4% over 2018-2021	1.5% INR56.0	1.8% INR56.1
	 <b>Vacancy</b>	> Vacancy rate likely to remain in a 10-11% range over 2019-2021	+0.4pp 11.4%	-0.4pp 11.0%
			End Q3/QOQ	End 2018/YOY

Source: Colliers International India Research

Note: Demand represents gross leasing; 1 sq m = 10.76 sq ft; pp: percentage point

## INCREASED OCCUPIER INTEREST IN ALTERNATIVE LOCATIONS

The third quarter saw leasing of about 760,000 sq feet (70,600 sq metres) leading to YTD 2018 absorption of 2,800,000 sq feet (260,000 sq metres). The YTD gross absorption declined 13% in comparison to the same period in 2017. Though the average deal size has increased in Q3, the fall in number of transactions has brought down the leasing volume. However, we expect the number of deals to increase in Q4 owing to steady enquiries by occupiers.

In line with our earlier forecasts, office demand in the city is moving towards micromarkets such as Old Mahabalipuram Road (OMR) Post-Toll and Mount Poonamalle High (MPH) Road with these micromarkets constituting 41% and 23% of the total office leasing respectively in Q3 2018. The Off Central Business District (Off CBD) and the CBD contributed 20% and 11% of the demand respectively while OMR Pre-Toll accounted for 5%.

The availability of quality contiguous floor plates has led occupiers looking to expand to consider the OMR Post-Toll micromarket. Over the next three years, occupiers looking for proximity to the city's core locations are likely to consider the Off CBD and MPH Road micromarkets owing to the ease of connectivity and upcoming Grade A supply.

In line with our earlier forecasts, companies in the engineering and manufacturing sector started gaining momentum, accounting for 31% of the total demand in Q3 2018. The Information Technology and Information Technology enabled Services (IT-ITeS) sector represented 28% of total demand, the education services 12%, marketing & advertising 10%, banking, financial services and insurance companies 8%, flexible workspace operators 4% and other\* sectors represented 7% of demand.

### Gross effective rental values

	Q3 2018 (INR psf pm)	Q3 2018 (USD psf pm)	QOQ Change (%)	YOY Change (%)
CBD <sup>1</sup>	70 – 90	1.0 – 1.2	0.0	0.0
Off CBD <sup>2</sup>	60 – 75	0.8 – 1.0	0.0	0.0
GST Road <sup>3</sup>	35 – 45	0.5 – 0.6	0.0	0.0
MPH Road <sup>4</sup>	50 – 65	0.7 – 0.9	0.0	0.0
OMR pre-toll <sup>5</sup>	57 – 83	0.8 – 1.1	3.7	5.3
OMR post-toll <sup>6</sup>	32 – 45	0.4 – 0.6	6.9	10.0
Ambattur	30 – 45	0.4 – 0.6	0.0	0.0

Source: Colliers International India Research

Note: Indicative Grade A rentals, includes both Non IT and IT-ITeS buildings; excludes Special Economic Zones (SEZs)  
USD1 = INR72.7 as on 25 September 2018

<sup>1</sup>Nungambakkam, Nandanam, Teynampet, RK Salai, Alwarpet, Egmore, T Nagar, Chetpet

<sup>2</sup>Anna Nagar, Kilpauk, Nelson Manikam Road, Vadapalani, Guindy, MRC Nagar, Adyar

<sup>3</sup>Grand Southern Trunk Road

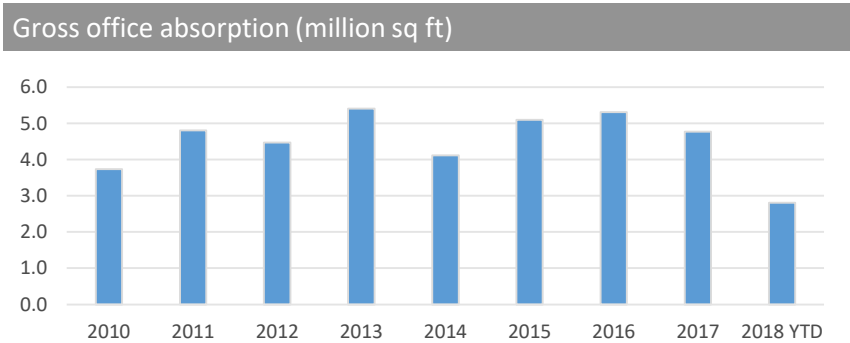
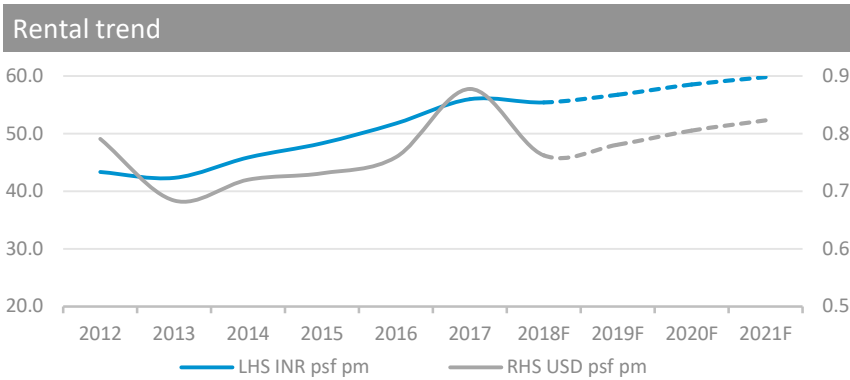
<sup>4</sup>Mount-Poonamallee High Road

<sup>5</sup>Old Mahabalipuram Road Pre-Toll (Madhya Kailash – Perungudi)

<sup>6</sup>Old Mahabalipuram Road Post-Toll (Thoraipakkam to Sholinganallur; Semmencherry to Siruseri; Pallavaram Thoraipakkam Road)

The state government released the Tamil Nadu ICT Policy in Q3 2018 with the objective of encouraging investment as well as increasing software production, exports and employment generation in the IT-ITeS sector. In our opinion, the consistent growth of the IT-ITeS sector coupled with a further policy push by the government including standard fiscal incentives such as capital subsidies, electricity tax exemptions and special incentives for micro, small and medium enterprises, is likely to further support the demand for office space over the next three years.

\*Other sectors include ecommerce, human resources and health care



Source: Colliers International India Research | YTD: Year-to-date - January to September

### Major leasing transactions in Q3 2018

Client	Building Name	Area (sq ft)	Location
Mphasis	DLF Cybercity	141,000	Manapakkam
Paragon Digital Services	Cee Dee Yes - Pallikaranai	77,000	Pallikaranai
Archipelago	SKCL Tech Square	60,500	Guindy
HDFC	MD Towers	47,000	Vadapalani
Ensona	Chennai One SEZ	32,000	Pallavaram Thoraipakkam Road

Source: Colliers International India Research  
Note: All figures are based on market information on 25 September 2018

## 17 MILLION SQ FEET OF NEW SUPPLY OVER 2018-2021

Over the first nine months of 2018, the city has witnessed completions of 1.24 million sq feet (116,000 sq metres) of Grade A office supply. We expect additional supply of 17 million sq feet (1.6 million sq metres) over 2018-2021, increasing the total office stock by 30%. The upcoming supply is distributed across micromarkets with OMR Post-Toll accounting for 52%, OMR Pre-Toll 26%, MPH Road 17%, CBD 3% and Off CBD 2%.

Rents have been on rise in the OMR corridor with a 5.3% YOY rise in OMR Pre-Toll and a 10.0% YOY rise recorded in the Post-Toll micromarket. In our opinion, by end of 2018 rents in these micromarkets are likely to further increase owing to the low vacancy levels in OMR Pre-Toll and rising demand in the OMR Post-Toll micromarket. Over 2018-2021, we also expect average citywide rents to rise by 2.2% annually driven by the rents in upcoming premium buildings.

The construction works of phase II of the metro-rail project, which is planned to cover the OMR corridor, is likely to be initiated by H1 2019 with pre-construction works having been recently initiated. The project is planned to run nearly 108 km along three corridors namely Madhavaram to Siruseri, Madhavaram to Shollinganallur and Koyambedu to Light House.

With enhanced connectivity, we expect that the upcoming phase II of the metro-rail project is likely to have a positive impact on city's real estate market over next ten years.

This is especially true with the proposed elevated corridor along OMR, which is likely to enhance connectivity and further strengthen the rents along the corridor. However, with traffic issues being a key concern in this most active office micromarket, we expect that the project is likely to add more bottlenecks to OMR while it is under construction.

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