COMMERCIAL RESEARCH

ABU DHABI OFFICE MARKET REVIEW Q1 2018

Key findings

Abu Dhabi's GDP decreased by 2.7% in the year to Q3 2017. Despite the weaker performance in the oil sector, the non-oil sector has remained resilient.

Prime office rents in Q1 2018 registered at AED 1,800 on average (sqm/p.a.), down 1.6% from Q1 2017.

Citywide office space witnessed steeper declines in rents of 8.2% and 12.9%, in the year to Q1 2018, respectively.

VAT appears to have had little impact on the commercial occupier market to date and we expect that this is likely to be the case going forward.

TAIMUR KHAN

Senior Analyst

"Over the course of 2018 over 195,000 square metres of stock is pencilled in to be delivered. However, Knight Frank analysis shows that in reality around 70,000 square metres is likely to be delivered with the remainder likely to be pushed into H1 2019."

Please refer to the important notice at the end of this report.

Signs of renewed activity within Abu Dhabi's occupier market as lower rents spur demand.

Macroeconomic overview

Abu Dhabi's GDP decreased by 2.7% in the year to Q3 2017, with the crude and natural gas sector's slowdown of 5.1% continuing to be a drag on the overall growth rate. Despite the weaker performance in the oil sector, the non-oil sector has remained resilient with a near flat annual growth rate in each of the last three quarters. Therefore whilst Abu Dhabi's economic backdrop remains challenged, we are beginning to see some resilience return to the market.

Both the oil and non-oil sector have registered three consecutive quarters of growth in 2017. The oil sector's growth has been driven by the higher oil price which has risen to US$69.6 per barrel as at March 2018, up from US$53.7 a year earlier, the highest price recorded since November 2014.

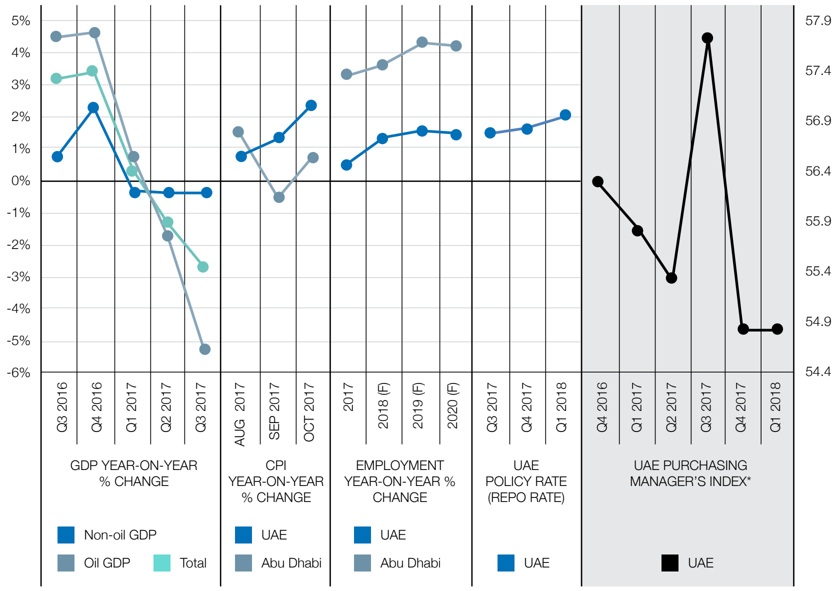
Furthermore firmer global economic activity has underpinned growth in both sectors due to increased demand for oil and increased global demand supporting activity in the non-oil sector.

Stronger global growth forecasts by the IMF, up 0.2% to 3.9% for both 2018 and 2019, indicate that this more positive macroeconomic environment is likely to continue on the back of surprisingly strong growth registered in Asia, Europe and the United States. With the non-oil sector currently accounting for an estimated 53% of Abu Dhabi's GDP, up from 47% in 2012, this level of global growth is required to sustain the recovery and continued diversification of the UAE's largest economy.

Business sentiment reflects this positive backdrop, with the Purchasing Managers Index showing a strong result in March 2018, albeit moderating from the levels seen at the end of 2017 which benefitted from a pre-VAT boost. For Abu Dhabi these factors have underpinned strong economic and employment growth forecasts of 5.8% and 3.7% respectively in 2018.

FIGURE 1

Economic indicators



Source: Knight Frank Research, Oxford Economics

**Note: A reading of 50 equates to no change, above or below representing growth or decline respectively*

Market review

In the first quarter of 2018 there have been tentative signs of renewed activity within Abu Dhabi's occupier market, with occupiers taking advantage of favourable market conditions. After subdued market performance in 2017, landlords have conceded to lowering rents and offering appealing incentives and as a result leasing rates have exhibited significant falls in the first quarter across all market sectors.

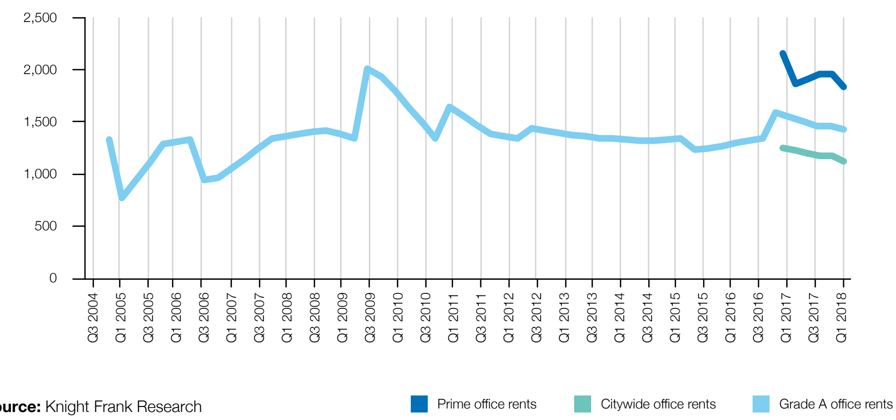
Prime office rents in Q1 2018 registered at AED 1,800 on average (sqm/p.a.), down 1.6% from Q1 2017. Grade A and Citywide office space witnessed steeper declines in rents of 8.2% and 12.9%, over the same time period, respectively. Grade A rents registered on average at AED 1,422 (sq m/p.a.) and Citywide rents at AED 1,083 (sq m/p.a.).

Demand for office space in the first quarter has been witnessed from a broad range of sectors. General trading firms accounted for over 50% of enquiries with professional services, hospitality and other firms, such as education institutes, accounting for just over 10% of new enquiries each. This demand pool represents a clear expansion from the demand pool witnessed in 2017 where enquiries were limited to only a select few sectors.

Over the course of the first quarter we have also seen higher levels of demand for larger floor areas and a healthy level of demand for low to mid-sized office space (Figure 6). In 2017, over 90% of enquiries were for space requirements in the 100 to 500 square metres range, compared to 63% in the first quarter of 2018.

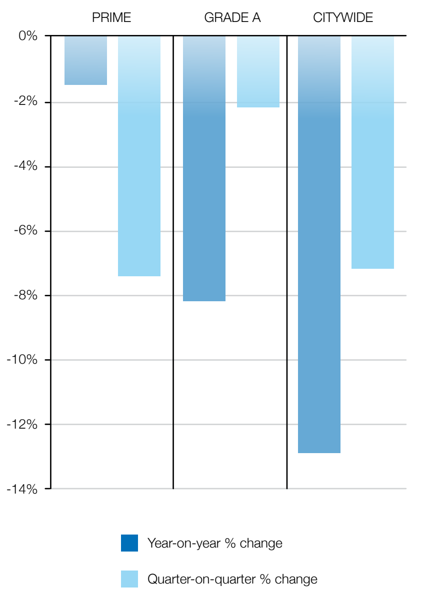
As a result of this renewed activity, led by falling rental rates and improved incentives, the vacancy rate remains relatively stable at 23%.

FIGURE 2
Abu Dhabi average office rents (AED / sq m / p.a.)



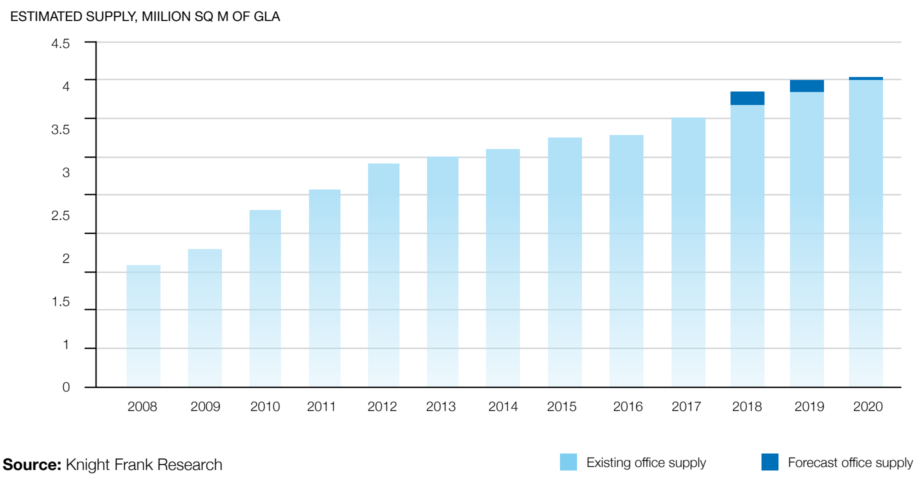
Source: Knight Frank Research

FIGURE 3
Abu Dhabi office market performance



Source: Knight Frank Research

FIGURE 4
Abu Dhabi office supply



Source: Knight Frank Research

Outlook

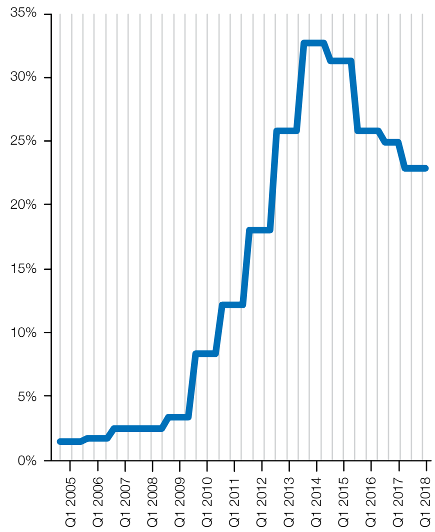
The short to medium term outlook for Abu Dhabi's office market remains negative with further falls in rental rates expected over the coming year. Over the course of 2018 over 195,000 square metres of stock is pencilled in to be delivered. However, Knight Frank analysis shows that in reality around 70,000 square metres is likely to be delivered with the remainder likely to be pushed into H1 2019. More so the vast majority of this new supply is not considered to be prime therefore its impact on the prime market is likely to be limited.

Despite the expectations of a lower level of supply, we are likely to see some pressure on vacancy rates across the city, particularly in the citywide market. This is due to occupiers upgrading to newer stock particularly if rents continue to decline and landlords offer appealing incentives to make such moves.

In terms of demand, we are likely to see similar trends, as discussed above with a possibility of the size of space demanded to be towards the low to mid end of the spectrum. If oil prices stabilise around the US$70 mark this could lead to increased demand from oil related entities and their service providers. Demand from government organisations is likely to remain limited in 2018, while budgets are allocated.

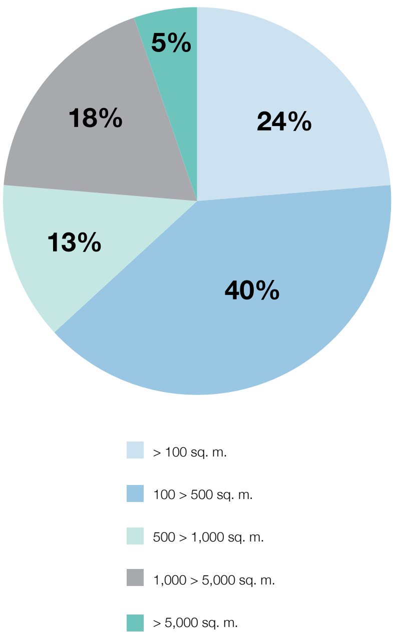
Finally, VAT appears to have had little impact on the commercial occupier market to date and we expect that this is likely to be the case going forward.

FIGURE 5
Abu Dhabi vacancy rate



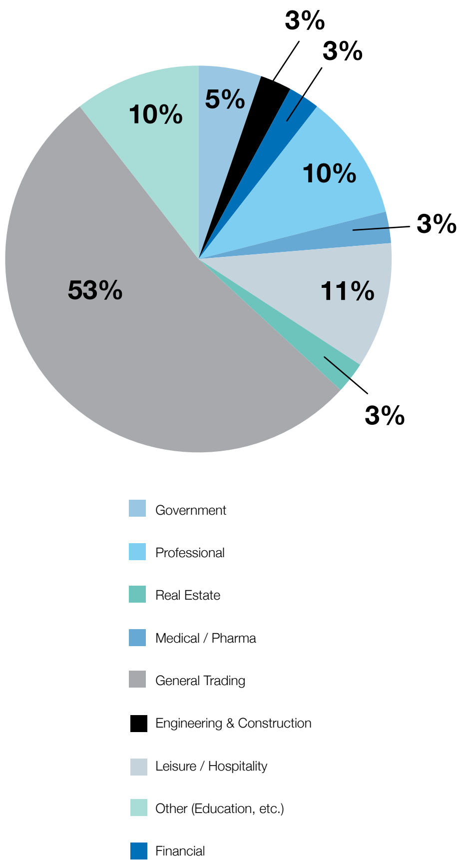
Source: Knight Frank Research

FIGURE 6
Proportion of enquiries by size (%), Q1 2018



Source: Knight Frank Research

FIGURE 7
Demand by sector (%), Q1 2018



Source: Knight Frank Research

MATTHEW DADD
Partner, Commercial Leasing & Agency

"Abu Dhabi reported foreign direct investment of over US$29 billion in 2017. As this investment enters the economy, we hope to see further stability and improvement in occupier demand."

Definitions *(With guidance from the Best Practice Standards for Office Developments (2015 V2.0) by the Middle East Council for Offices (MECO):*

Prime: The Prime segment represents the average rent of the top 5% of all lettings in the market

Grade A: This segment of the market represents offices which are adjacent to the city centre, with rents on average higher than those in the citywide market

Citywide: This segment represents the broader city offices market, outside the 'core city', where usually a significant of office buildings are grouped

Composite: The composite data represents is an average of all aforementioned markets

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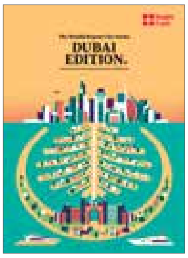

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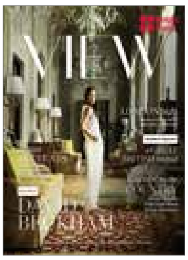

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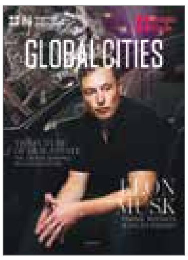

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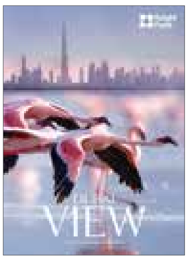
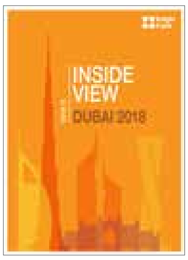


Dubai View 2017/2018



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