COMMERCIAL RESEARCH

DUBAI OFFICE MARKET REVIEW Q1 2018

Key findings

Dubai's GDP grew 2.8% in 2017, down from 3.1% from a year earlier, according to data from Dubai Statistics Centre. A slowdown in the annual percentage growth in three out of five of the largest economic sectors within Dubai has led to the overall growth rate slowing.

The occupier market witnessed a strong start to the year with a clear uptick in demand. Whilst there has been some expansionary activity taking place in the market, the greater level of demand for new space has come from firms consolidating operations.

Despite greater activity levels we have seen rents soften across all segments of the market. Average office rents across Dubai softened by 4.3% year-on-year.

Prime office rents in Q1 2018 registered at AED 250 (sq.ft./p.a.), down 1.4% in the year to Q1 2018.

Grade A rents fell 7.4% year on year to AED 150 (sq.ft./p.a.) on average, this rate is likely to continue to slide.

TAIMUR KHAN
Senior Analyst

"Although we have seen a strong start to the year, we envisage that market activity will begin to slow in Q2, with rents likely to remain under some pressure."

Despite a trend of consolidations in the Dubai market, activity within the occupier sector continues as landlords ease rental terms.

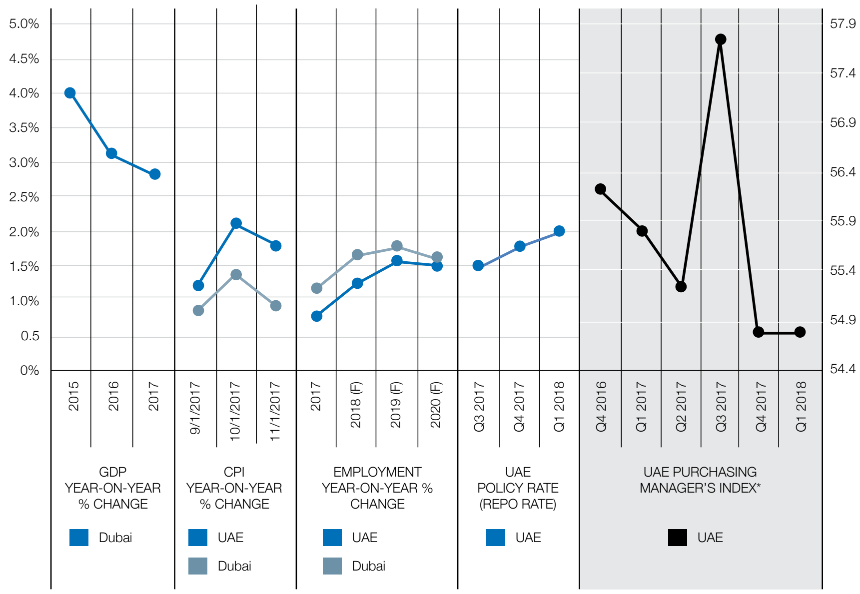
Macroeconomic overview

Dubai's GDP grew 2.8% in 2017, down from 3.1% from a year earlier, according to data from Dubai Statistics Centre. A slowdown in the annual percentage growth in three out of five of the largest economic sectors within Dubai has led to the overall growth rate slowing. On a broader level we have seen that of the 20 broad economic sectors in Dubai, 12 have seen the rate of growth slow in 2017 compared to a year earlier. On a more positive note, all sectors, bar financial and insurance activities which registered a flat growth rate, have recorded positive percentage growth over the year.

The outlook and sentiment for Dubai's GDP in 2018 remains positive on the back of stronger global growth forecasts by the IMF, up 0.2% to 3.9% for both 2018 and 2019. Furthermore, whilst Dubai's GDP is not as sensitive to a slowdown in the hydrocarbon sector compared to its regional peers, due to its diversified economic structure, the slowdown has impacted ancillary businesses which service this sector from Dubai given its regional hub and leading financial centre status. Therefore, the increase in oil prices to US$69.6 as at March 2018, up from US$53.7 a year earlier will help underpin economic growth this year.

Business sentiment somewhat reflects this more positive backdrop, the Emirates NBD Dubai Economy Tracker Index (DET) stood at 55.3 in March 2018 which is well above the neutral 50 level indicating a strong expansion in the non-oil sector. However, despite this the DET shows that employment fell slightly in March. Overall there is cautious optimism for Dubai's economy with GDP growth forecast at 3.5% and employment growth forecast to increase to 1.6% in 2018, up from 0.7% in 2017.

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*

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

Market review

The occupier market witnessed a strong start to the year with a clear uptick in demand for office space which was seen from across a range of business sectors. Whilst there has been some expansionary activity taking place in the market, the greatest level of demand for new space has come from firms consolidating operations. These firms are also using this consolidation as an opportunity to upgrade to higher quality offices, however despite this desire, the firms remain very price sensitive. In reality, this flight to quality becomes more difficult to execute given the lack of prime stock and for larger tenant requirements, this is a further exacerbated issue due to the lack of suitable full floor plate availability in some prime areas.

The current market is very much a tenant-favoured market, as a result some landlords are having to become more proactive in ensuring the longer term performance of their asset. The manner in which this has been carried out is similar across both fully fitted and shell and core products where incentives such as rent free periods, delayed rent escalations and free parking are being offered to entice tenants. Due to the unsettled nature of the market we will continue to see landlords having to work harder to attract and retain tenants. Shell and core landlords will have to be willing to provide capital expenditure incentives and start to consider active asset management and lease re-gears to retain key tenants.

Despite greater activity levels we have seen rents soften across all segments of the market. Average office rents across Dubai softened by 4.3% year-on-year.

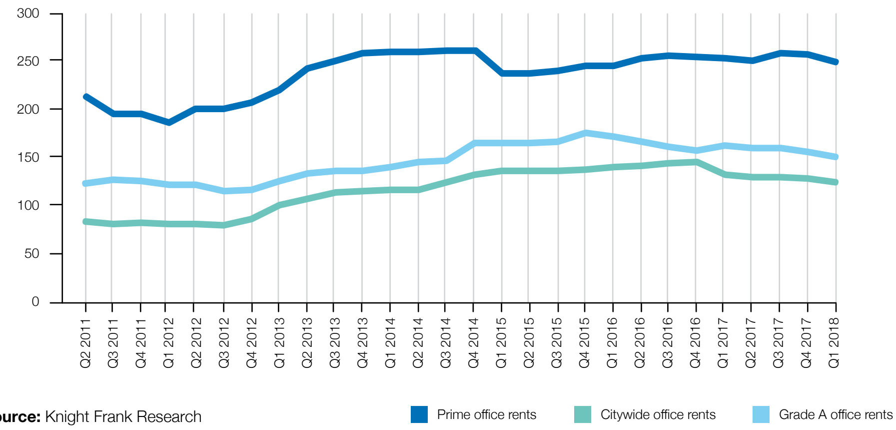
Prime office rents in Q1 2018 registered at AED 250 (sq.ft./p.a.), down 1.4% in the year to Q1 2018. Vacancy in core prime assets remains as low as 1%, however as you move towards the outskirts of these prime areas we are seeing this rate shift higher. As the Gate Avenue project nears completion, in the DIFC, we are likely to see the “core” expand and therefore this spread in vacancies fall.

Grade A rents fell 7.4% year on year to AED 150 (sq.ft./p.a.) on average, this rate is likely to continue to slide given that there is a range of Grade A office supply due to enter the market.

Citywide office rents fell 6.2% in the year to Q1 2018 to AED 123 (sq.ft./p.a.), however in the citywide office market we are seeing fragmented market performance continue. Single-ownership

FIGURE 2

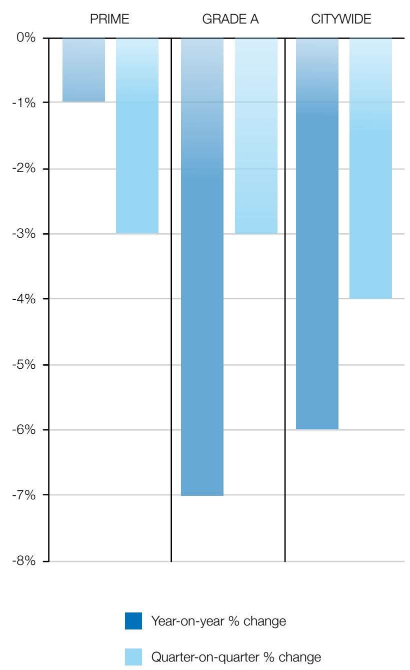
Dubai average office rents (AED / sq ft / p.a.)



Source: Knight Frank Research

FIGURE 3

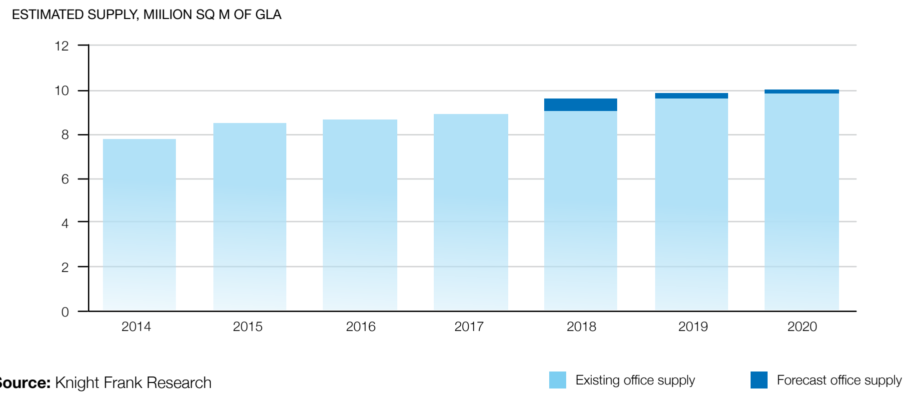
Dubai office market performance



Source: Knight Frank Research

FIGURE 4

Dubai office supply



Source: Knight Frank Research

assets continue to outperform the market whereas strata owned stock has underperformed, due not only to lack of quality, but lack of demand for this type of stock due to its long term disadvantages as businesses grow.

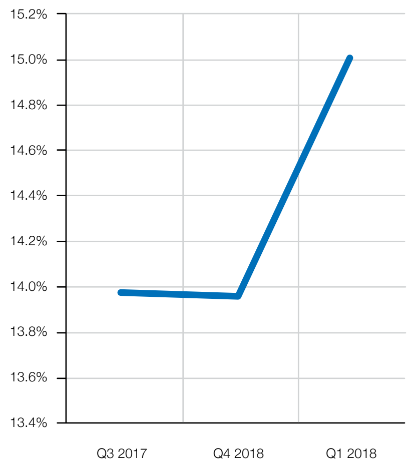
IT/ Technology and Professional Services were the joint largest source of total enquiries with each sector making up 14% of the total. Design, education, healthcare and investment businesses accounted for 9% apiece. Even with such a broad range of demand 65%, of space requirements were below 5,000 square feet.

Market wide vacancy over the course of the last quarter has seen a small uptick to 15% given the availability of new stock and consolidation by firms.

Although we have seen a strong start to the year, we envisage that market activity will begin to slow in Q2, with rents likely to remain under some pressure. Grade A rents are likely to soften further, given that the majority of stock which is due to enter the market this year falls within this category.

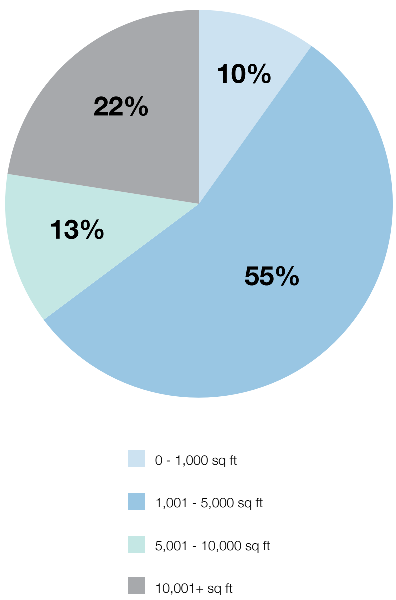
Looking at the supply side, of the total level of supply originally scheduled to enter the market in 2018, we believe that at least 25% of this is likely to be delayed.

FIGURE 5
Dubai vacancy rate



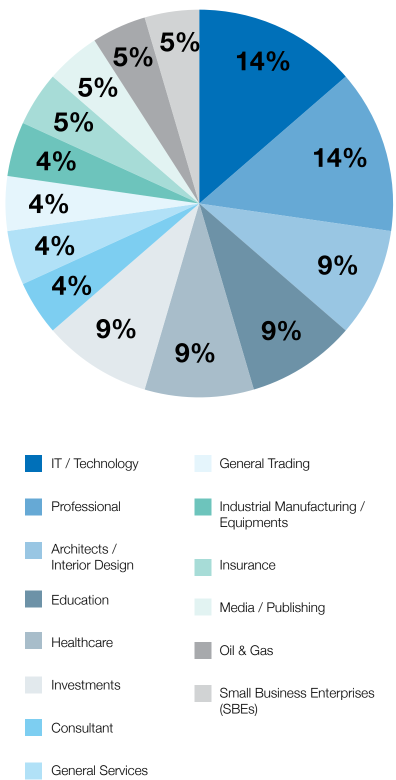
Source: Knight Frank Research

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

"The current market is very much a tenant-favoured market, as a result some landlords are having to become more proactive in ensuring the longer term performance of their asset."

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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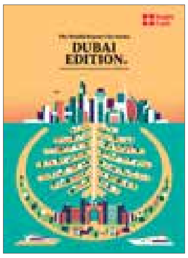

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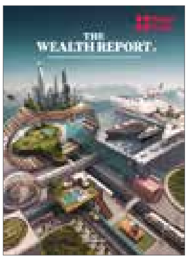

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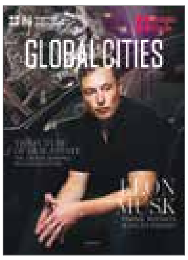

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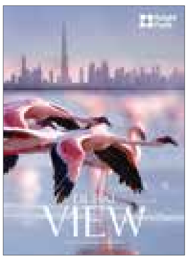
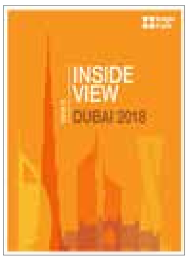


Dubai View 2017/2018



Dubai Inside View 2018

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