RESEARCH

UAE MARKET REVIEW AND FORECAST
2019

THE ANNUAL REVIEW AND FORECAST OF THE UAE REAL ESTATE MARKET

RESEARCH

UAE MARKET REVIEW AND FORECAST 2019

Headlines

The UAE's GDP is expected to grow by 2.8% in 2018, up from the 0.8% registered in 2017.

Residential prices and rents are likely to continue to soften in 2019, however we may see additional demand which helps underpin the market as a result of the recent approval of a range of legislations to ease visa regulations, given that many of the changes are linked to property ownership.

In the short to medium term we expect that market conditions in the UAE's office sector will remain challenging with rental rates continuing to fall.

As a result of the level of incoming retail supply in Abu Dhabi and more so in Dubai, it is likely to mean that operators and retailers are likely to face extreme pressure over the coming five years.

In the UAE's hospitality sector we anticipate that the changing nature of room night demand and sustained development pipeline will result in RevPAR levels weakening over 2019.

TAIMUR KHAN
Research Manager

"Despite the slight downgrade in global growth forecasts, the IMF has revised up the UAE's GDP growth forecasts for both 2018 and 2019."

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

Macroeconomic overview

The United Arab Emirates' GDP increased by 0.8% in 2017, down from 3.0% in 2016. Over the course of 2018, the Central Bank of the UAE's Overall Augmented Economic Composite Indicator, has shown that GDP growth has strengthened throughout the year on the back on higher oil prices, higher levels of production in the hydrocarbon sector and a strengthening non-oil sector. This indicator estimates that the year-on-year GDP percentage change to Q3 2018 stands at 3.1%, with the overall 2018 annual growth rate expected to register at 2.8% and 4.2% in 2019 *(Figure 1).*

Abu Dhabi's GDP grew by 1.5% in the year to Q2 2018 with both oil and non-oil GDP registering year-on-year growth. The oil sector's growth of 1.0%, has been driven by higher levels of production and by the higher oil price. Growth in the oil sector is likely to have underpinned Abu Dhabi's non-oil sector, which in the year to Q2 2018 recorded growth of 2.0%.

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 the five largest economic sectors within Dubai has led to the overall growth rate slowing.

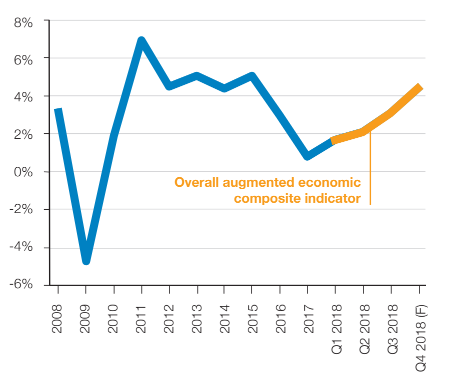
Throughout 2018, the trend of a more tepid economic backdrop has remained fairly constant, with the Emirates NBD Dubai Economy Tracker Index (DET) recording an average, in the year to November 2018, of 55.2, a figure which is slightly lower than the average for the same period a year before. More so, consumer demand remains weak with the selling price in Dubai's private sector declining for the majority of the year, this is despite rising input costs, suggesting firms are having to cut margins in order to support demand. In addition to this, employment has remained broadly unchanged in the first 11 months of the year which has impacted a broad range of sectors in terms of demand.

Outlook

Outlook for the UAE's GDP growth in 2018 and 2019 remains positive on the back of higher oil prices, a range of stimulus packages and easing of business regulations in both Abu Dhabi and Dubai, which are likely to support activity in both the public and private sectors.

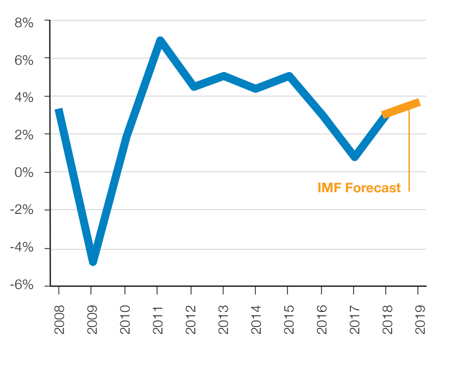
Recent forecasts from the IMF indicate global economic growth is likely to continue its steady expansion with growth forecast at 3.7% in both 2018 and 2019, down only marginally by 0.2% from the previous forecasts. Despite this slight downgrade in global growth forecasts, the IMF has revised up the UAE's GDP growth forecasts for both 2018 and 2019 from 2.0% to 2.9% and 3.0% to 3.7% respectively. The latter estimate is materially lower than the aforementioned estimates by Central Bank of the UAE.

FIGURE 1
UAE GDP, Y-o-Y % change



Source: Knight Frank Research, Macrobond and the Central Bank of the UAE

FIGURE 2
UAE GDP Forecast, Y-o-Y % change



Source: Knight Frank Research, Macrobond and the Central Bank of the UAE

Residential

Dubai

Mainstream residential prices in Dubai fell by 4.1% over the year to November 2018 according to the Property Monitor Index*. Prices for villas continue to fall at a faster pace at 6.1%, compared to prices for apartments which fell by 4.8% over the same time period *(Figure 3)*.

On a community wide basis, data as at November 2018 shows that of the 61 communities and property types tracked in Dubai by Property Monitor, only one area has registered an annual increase in prices, this is down from Q1 2018, where five areas had registered increasing prices in Dubai. The current gap between the top and bottom ranking communities, in terms of annual price performance, currently stands at 9.1%, up from the 7.6% registered in March 2018. These price movements show that we are continuing to see a fragmented market operate in Dubai.

Compared to the mainstream market, the prime market has performed better in relative terms, however there still has been pressure on prices, with prime residential prices in the year to November 2018 falling on average by 3.3%.

Rental rates across Dubai fell on average* by 7.7% in the year to November 2018 with apartment rents falling by 8.4% and villa/townhouse rents by 8.3% over the same time period *(Figure 4)*.

Gross yields in Dubai currently stand at 6.27% as at November 2018, down from 6.45% a year earlier, this is as a result of rents declining at a faster pace than sales prices over this time period.

Total mainstream transaction volumes in the January to November 2018 period fell by 14.9% when compared with the same period a year earlier. The main contributor to this decline has been due to the slowdown in transactions in the off-plan market, where over the same time period, transactions fell by 35%. Whereas, the secondary market has recorded a growth in transaction volumes of 2.2%.

The decline in overall transactions had been particularly severe in the first three months of the year and then again in the summer months from June to September. However since then we have seen the decline in transactions moderate with transactions falling 3% year-on-year to November 2018.

Abu Dhabi

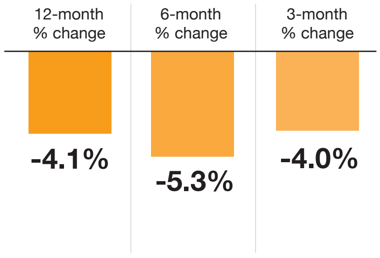
In the year to November 2018 average sales prices in the capital fell by 4.7%, according to the Property Monitor Index*. Annual price declines on average for apartments and villas/townhouses were recorded at 4.4% and 4.9% respectively *(Figure 5)*.

Key-sub submarkets and property types in Abu Dhabi have continued to see prices fall in the year-to November 2018, however the rate at which prices are falling is slowing. Over this time period, the largest declines were witnessed in Al Reem Island's apartment market which fell 5.7% and in Saadiyat Island's and Al Reef's villa/ townhouse markets, which fell by 5.6% each. Whilst, seven of the 10 sales markets tracked by Knight Frank have shown annual price declines of 5.0% or more in the year to November 2018, there have been some areas which have outperformed the market in relative terms, albeit with prices still declining. Apartments on Yas Island recorded the lowest level of annual price falls at 1.4% *(Figure 6)*.

Rental rates across Abu Dhabi fell on average* by 8.7% in the year to November 2018 according to the Property Monitor Index*. On average, apartment rents fell by 7.7% and Villa rents by 8.4% over the same time period *(Figure 7)*.

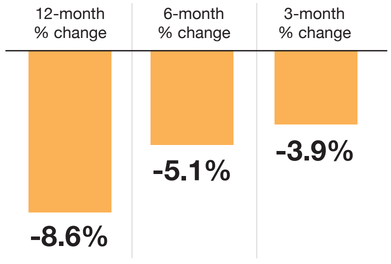
Gross yields in Abu Dhabi currently stand at 6.50% as at November 2018, down from 6.71% a year earlier, once again this is as a result of rents declining at a faster pace than sales prices over this time period.

FIGURE 3
Dubai mainstream price performance



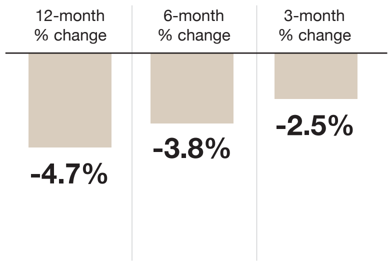
Note: Data to November 2018
Source: Knight Frank Research, Property Monitor

FIGURE 4
Dubai mainstream rental performance



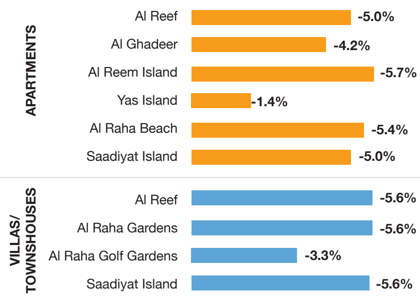
Note: Data to November 2018
Source: Knight Frank Research, Property Monitor

FIGURE 5
Abu Dhabi mainstream price performance



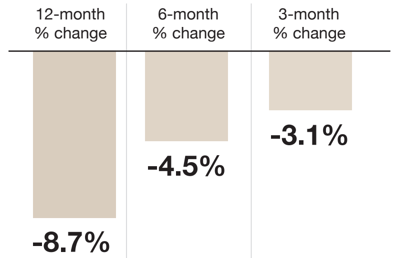
Note: Data to November 2018
Source: Knight Frank Research, Property Monitor

FIGURE 6
Abu Dhabi, sub-markets, y-o-y % price change to November 2018



Source: Knight Frank Research

FIGURE 7
Abu Dhabi mainstream rental performance



Note: Data to November 2018
Source: Knight Frank Research, Property Monitor

** The Property Monitor Index methodology is based on a basket of properties where the property value is estimated using a range of sources compared to the price changes for apartments and townhouses/villas which is based on DLD transfers which may result in the average price changes not tallying with one another.*

Outlook

Whilst the stimulus packages and easing of business regulations are positive and will provide some support to the residential markets, there is likely to be a time delay in these resulting in increased demand in the UAE's residential sector. Currently businesses are looking for short to medium term stability before committing to any expansion plans. In the short run, this hesitation impacts consumer confidence, which in turn impacts residential market activity in both the sales and rental markets. Therefore, until the expected increase in business confidence feeds through to consumer confidence, we are likely to see continued pressure on real estate prices and rents.

In Abu Dhabi, at the start of 2018, Knight Frank estimated that total 8,121 units would be delivered, however, to date initial estimates show that only 3,346 units have been delivered. In the capital, the lack of demand is the single largest contributor to the pressure exerted on prices and rents, therefore until we see a notable improvement in the economic backdrop, we are unlikely to see any significant improvement in performance.

In Dubai, whilst demand had eased in 2018, prices falls are more due to the considerable level of supply which has been delivered in 2018 and that which is expected to be delivered in 2019. In 2018, Knight Frank forecast 32,727 units to be completed in Dubai, initial estimates indicate that to date we have seen 22,476 units delivered. This increase in supply, in addition to the unabsorbed supply from previous years has led to the extended pressure on prices and rents which we are witnessing, this trend is expected to continue throughout 2019.

Whilst there are clear challenges facing the residential market, the recent approval of a range of legislations to ease visa and foreign business ownership by the UAE Cabinet are likely to drive addition demand to the UAE's property market, given that many of the changes in visa regulations are linked to property ownership. The new visa legislations - which are expected to take effect towards the end of Q1 2019 and where all investments must be cash which is not loaned - include five year retirement visas for those over 55 years old, in return for investing AED 5 million or more in the property market or those with incomes of 20,000 per month or more or those with more than AED 1 million in capital. There are also options to be made available for non-retiree investors, where investors who invest over AED 5 million in property are able obtain a five year visa.

In addition to these property related visas there are a range of business investment visas have also been approved. Investors who invest over AED 10 million in enterprise can obtain a 10-year visa, where up to 40% of the investment can be related to property purchases. Entrepreneurs in the UAE with previous business investments worth over AED 500,000 or those with a business which is accredited by a business incubator will be able to obtain a 5-year visa with the possibility of obtaining the aforementioned business investor visa, should they eventually meet the criteria. Finally, the approved legislation also allows for a10-year visa for high value talent in selected fields, as well as 5-year visa for students and their families, who are studying in the UAE.

Commercial

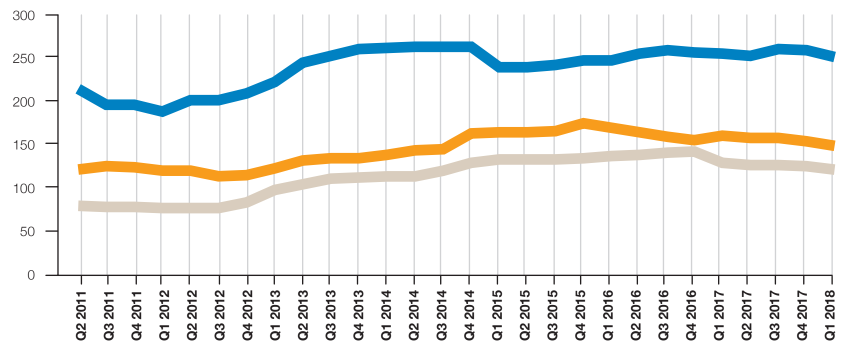
Dubai

Dubai's office market continues to see performance softening as a result of subdued market activity which has led to the market remaining tenant favourable. In Q3 2018, we have seen limited activity from new corporate occupiers, with new licence issuances falling 9% year-on-year in the year to Q2 2018 according to data from Dubai Statistics Centre. The primary source of activity has come from firms looking to consolidate their commercial real estate portfolios or occupiers looking to downsize. On a positive note, these market conditions do provide opportunity for occupiers looking to take advantage of softer market conditions and as a result of this activity, landlords who actively manage their assets have fared better.

More so, given this subdued market activity, we have seen rents soften across all segments of the market. Average office rents across Dubai softened by 5.8% year-on-year to Q3 2018, up from the 4.3% decline witnessed in Q1 2018.

FIGURE 8

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

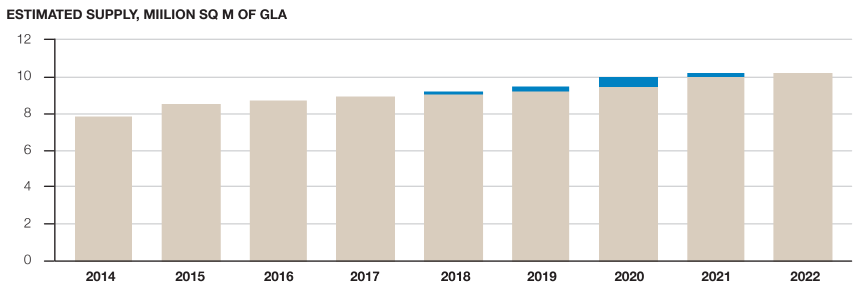


Source: Knight Frank Research

Prime office rents · Grade A office rents · Citywide office rents

FIGURE 9

Dubai office supply



Source: Knight Frank Research

Existing office supply · Forecast office supply

Prime office rents in Q3 2018 registered at AED 246 (sq ft/p.a.), down 4.9% in the year to Q3 2018. Vacancy in core prime assets remains as low as 1%, however as you move towards the outskirts of these projects we are seeing this rate shift higher. As the Gate Avenue project nears completion we are likely to see the "core DIFC" expand and therefore this spread in vacancies fall.

Grade A rents fell 8.9% in the year to Q3 and now stand at AED 145 (sq ft/p.a.) on average. This rate is likely to continue to slide given a range of Grade A office supply due to enter the market and existing vacancy.

Citywide office rents fell 4.9% in the year to Q3 2018 to AED 123 (sq ft/p.a.), however in the citywide office market we are seeing fragmented market performance continue. Single-ownership assets continue to outperform strata owned stock which has underperformed, due not only to lack of quality but lack of demand for this type of space due to its long term disadvantages as businesses grow.

Outlook

The short to medium term outlook for Dubai's commercial market remains negative with rents expected to continue to decline across all market segments. This trend is likely to be primarily driven by the delivery of additional supply which we expect to total at over 400,000 square metres by the end of 2019. However, the vast majority of this supply is concentrated in the Grade A and Citywide office market. As a result we expect that prime market rents are likely to be less impacted by the influx of new supply in the medium term.

Whilst demand has been subdued in 2018, after a strong start to the year, we believe that due to the easing of regulations, freezing of government fees, economic stimulus packages, and continued introduction of dual-licencing in Free Zones, demand is likely to tick up over the short term to medium term from both existing and new market entrants. However, there will naturally be a lag between the implementation and pick-up from corporate occupiers.

Abu Dhabi

After a relatively strong start to the year in Abu Dhabi's office market, we have witnessed activity become muted once again over the course of Q2 and Q3 2018. Whilst there is increased activity from certain sectors in the market, there has been a notable slowdown in demand from the general trading and professional sectors. Abu Dhabi's fragile economic backdrop is a likely contributor to this slowdown, as firms are likely to hold off executing many corporate decisions until there is a clearer understanding and implementation of 100% foreign ownership laws and the outcome of proposed mergers in the banking sector.

Prime office rents in Q3 2018 registered at AED 1,720 on average (sq m/p.a.), down 11.5% from Q3 2017. Over the same time period we have seen Grade A rents register the steepest declines with rents falling by 15.8%, with a significant reduction in rents from Q2 to Q3 contributing to the large annual decline. Citywide rents have also softened, with year-on-year rents to Q3 2018 falling by 10.0%. Grade A rents registered on average at AED 1,225 (sq m / p.a.) and Citywide rents at AED 1,050 (sq m / p.a.).

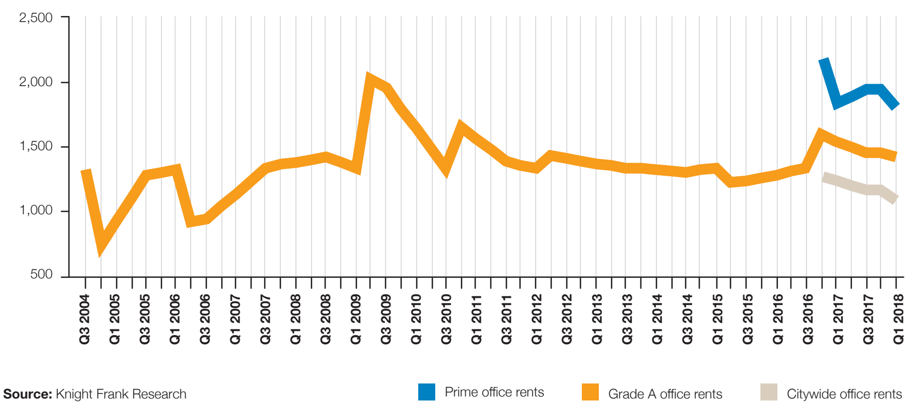
Outlook

In the short to medium term we expect that market conditions in Abu Dhabi's office sector will remain challenging with rental rates continuing to fall. However we expect that the rate of decline is likely to start to moderate, particularly in the Prime and Grade A segments.

Knight Frank's view is based on limited levels of supply due to enter the market in the Grade A and Prime segments, with the vast majority of the 165,000 square metres of additional supply expected by 2020 being classed as Citywide stock in non-core locations.

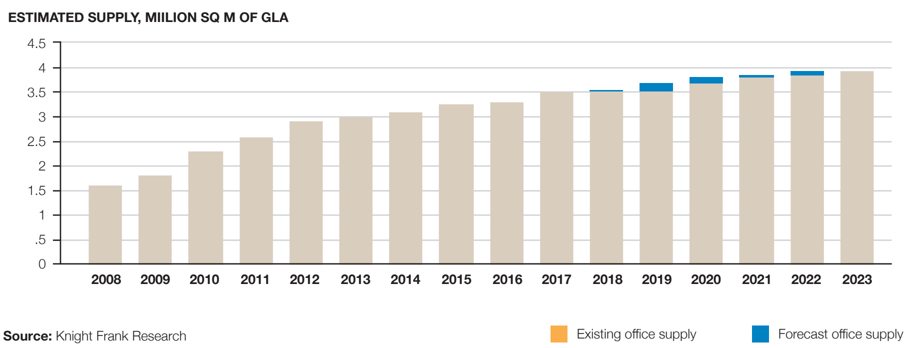
More so, a result of renewed activity in the oil sector and the expected benefits of the AED 50bn stimulus packages as well as the easing of regulation, we expect demand to tick up from early 2019.

FIGURE 10
Abu Dhabi average office rents (AED/ sq m/ p.a.)



Source: Knight Frank Research

FIGURE 11
Abu Dhabi office supply



Source: Knight Frank Research

Retail

Given the weaker economic climate, a stronger US Dollar and therefore a stronger Dirham (given the Dirham's US$ peg), lower levels of consumer confidence, the increasing impact of e-commerce and the impact of the introduction of VAT in 2018, the UAE's retail sector, particularly its bricks and mortar retail sector is continuing to face strong headwinds.

The impact of e-commerce on the physical retail sector has been particularly evident over the course of 2018. E-commerce firms such as Noon, Souq, Ounass and Nashimi have enacted a range of initiatives, aside from only discounting prices, to improve the range of products offered and also delivery options, particularly same-day and next-day delivery. The impact of e-commerce has not been limited to non-perishable goods only, with grocery giants such as Carrefour now offering one-hour delivery for everyday basics and same day delivery on their hypermarket range.

Whilst the traditional retail sector has battled back primarily through participation in sales festivals as a result of the continued growth in tourism levels, but despite this the impact of market conditions on profitability has been clear. This in turn has impacted retail real estate performance across the board. Rental rates have witnessed double digit declines on an annual basis on average in both Abu Dhabi and Dubai. Despite declining rents we are also witnessing occupancy rates fall, particularly in speciality retail and community retail locations.

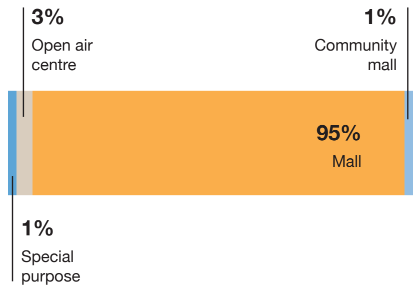
Outlook

Although the emergence and increasing utilisation of e-commerce will be of concern to operators, physical retail, particularly destination and entertainment focused retail developments, will continue to attract demand given the extreme weather conditions witnessed over summer months in the UAE. However, the level of incoming supply in Abu Dhabi and more so Dubai is likely to mean that operators and retailers are likely to face extreme pressure over the coming five years.

In Abu Dhabi, Knight Frank estimate that by 2022 we are likely to see the delivery of over 650,000 square metres of retail space, the vast majority of which will be in the form of super regional or regional malls. Many of these new offerings will be destination and entertainment focused so are likely to attract significant demand, as currently existing offerings lack this element, therefore these developments are likely to be most adversely impacted in the long term *(Figures 14 and 15)*.

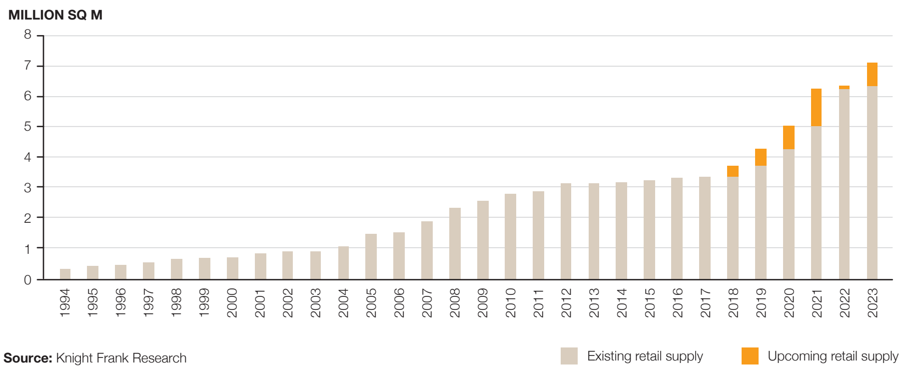
Dubai's retail market is set to change drastically over the next five year with over 3.7 million square metres of retail space set to be delivered by 2024. If the delivery of this supply come to fruition, we expect Dubai's total retail stock to be almost 7.1 million square metres, a 111% increase on current levels. Retail destinations within developed residential communities and good transport links are least likely to be impacted by this influx of supply *(Figures 12 and 13)*.

FIGURE 12
Existing Dubai retail supply, by type



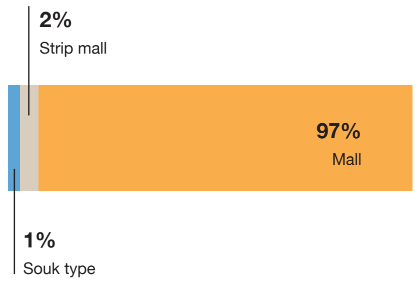
Source: Knight Frank Research

FIGURE 13
Dubai retail supply



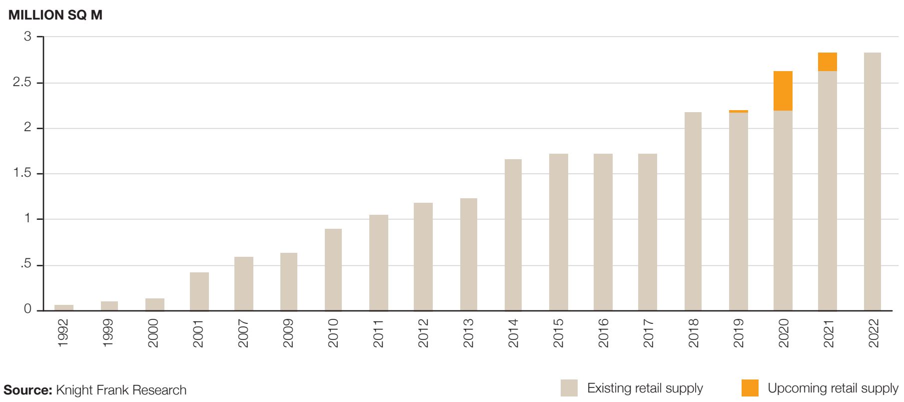
Source: Knight Frank Research

FIGURE 14
Existing Abu Dhabi retail supply, by type



Source: Knight Frank Research

FIGURE 15
Abu Dhabi retail supply



Source: Knight Frank Research

Hospitality

Market performance has continued to deteriorate in the UAE's hospitality sector with occupancy falling by 2.0%, ADR by 5.8% and RevPAR by 7.7% in the year to date to November 2018, compared to the same period a year earlier.

This is despite, visitation to the UAE continuing to increase, but in light of a more cash-constrained guest profile, hotels have had to price more competitively in order to maintain market share. This indicates that weaker KPIs are not related to occupancy issues but due to the changing nature of source markets visiting the UAE.

From an operational perspective, in a market of softening performance, we are seeing an increasing number of hotel owners scrutinise operators more critically than ever, and this has most often come in the form of operational reviews, enforced headcount reduction, or even termination.

Over the past year we have seen developers increasingly moving away from traditional management contracts, instead choosing to explore franchise agreements as a means to drive profitability. In some instances we have even seen operators willing to convert management agreements to franchise agreements regardless of contractual obligations if the necessary prerequisites are met.

Outlook

Looking ahead, we anticipate that the changing nature of room night demand and sustained development pipeline will result in RevPAR levels weakening over 2019. We anticipate that this RevPAR decline will continue to be attributable to a falling ADR rather than declining occupancy levels. Nonetheless development opportunities still exist in certain micro markets, but these tend to be in secondary areas rather than in the more established areas of Dubai *(Figure 16)*.

"Whilst there are clear challenges facing the market, a trend we expect to continue in 2019, the recent approval of a range of legislations to ease visa and foreign business ownership by the UAE Cabinet are likely to drive addition demand in the UAE's property market. Looking ahead we expect that the prime segments of the market are likely to continue to outperform the mainstream market overall."

TAIMUR KHAN
Research Manager

FIGURE 16
UAE Hospitality Key Performance Indicators, Year to date, Nov 2018 vs Nov 2017

	OCC	ADR	RevPAR	Room Revenue	Room Availability	Room Sold
United Arab Emirates	-2%	-5.8%	-7.7%	-2.8%	5.3%	3.2%
Abu Dhabi	0%	-4.6%	-4.6%	-0.3%	4.5%	4.5%
Dubai	-2.5%	-6.4%	-8.7%	-3.1%	6.2%	3.6%
Ras Al-Khaimah	-3.4%	-0.3%	-3.7%	1.0%	4.8%	1.3%
Sharjah	-4.0%	-2.5%	-6.4%	-7.5%	-1.2%	-5.2%
Fujairah	-3.6%	0.1%	-3.5%	0.1%	3.7%	-0.1%

Source: Knight Frank Research

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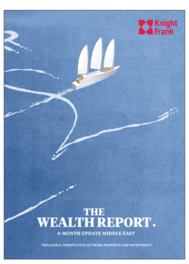

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