RESEARCH

UAE REAL ESTATE

2016 YEAR-END MARKET REVIEW & OUTLOOK

ABU DHABI & DUBAI REAL ESTATE SECTOR REVIEW

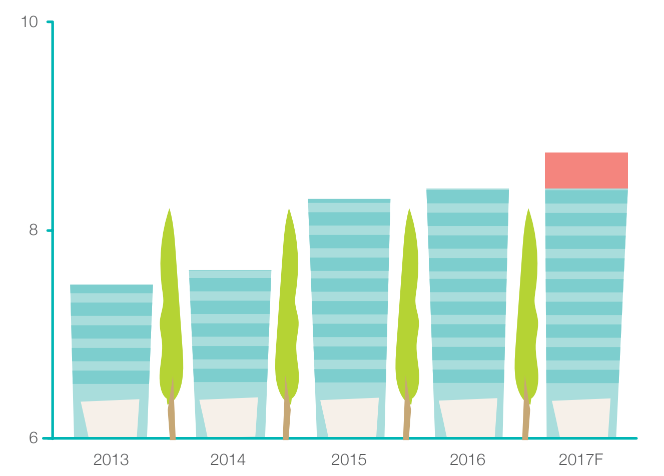
OFFICE MARKET

The slowdown in the UAE economy and subsequent cutbacks in the job market weighed in on the performance of the office market in 2016. In Dubai, while international occupiers remain committed to the region, they have chosen to restructure rather than expand their operations.

As a result, office rents across Grade A spaces in Dubai remained relatively stable. They continue to enjoy high occupancy rates given the limited availability of good quality stock in Freezones and around developed amenities and infrastructure. Meanwhile Grade B rents in secondary locations have dipped as landlords struggle to attract and retain tenants.

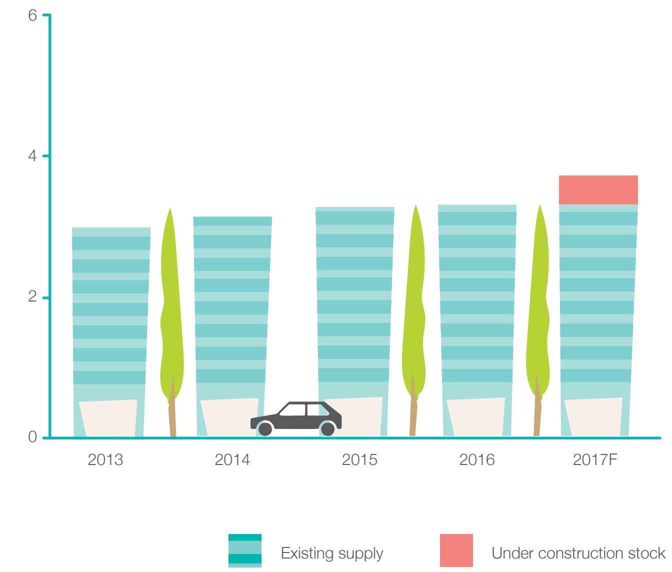
In Abu Dhabi, the drop in oil prices squeezed tenants in the Oil & Gas industry and the public sector who make up the bulk of corporate occupiers. This had a knock on effect on some professional services companies such as law firms and consultancies, who rely on work from government and related entities. Consequently rental rates across the emirate declined as vacancies increased. However the impact has been less profound than expected, given the limited delivery of office space in 2016.

FIGURE 1
Dubai office supply



Source: Knight Frank Research

FIGURE 2
Abu Dhabi office supply



2017 Outlook

The commercial market in Dubai is expected to pick up in 2017 as businesses settle to the new norm in oil prices. We expect blue-chip occupiers (who had put real estate decisions and plans on hold in 2016) to plan for a more active business cycle. However any potential upside in rental values is expected to be offset by the delivery of new Grade A space. Meanwhile rents in Grade B buildings are expected to see marginal declines over the same period. In Abu Dhabi and under the current market conditions, we expect a delay in the delivery of commercial towers which is likely to prevent any further declines in rental rates.

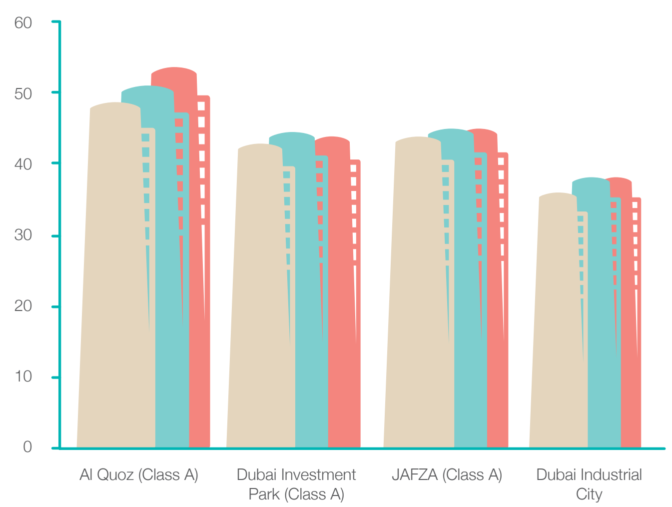
INDUSTRIAL MARKET

Despite economic headwinds the overall performance of the UAE's industrial sector displayed relative stability in 2016. In Dubai, whilst falling oil prices weakened investor and consumer confidence, industrial rents remained flat on an annual basis. The emirate's diversified economy and the sector's reliance on trading activity have acted as a buffer against economic uncertainties.

Expectations of the emirate's industrial growth potential and the government's diversification strategy have resulted in an increasing number of private sector players committing to the market. Unilever, (one of the leading FMCG companies), built a AED 1 billion factory in Dubai Industrial Park. The facility will export locally made products to 80 countries in the Middle East, North Africa and Europe. Similarly, retailer Majid Al Futtaim (MAF) is expected to set up a new logistics facility at the National Industries Park (NIP), which it will use as a distribution hub for its Carrefour hypermarket chain.

In Abu Dhabi, the dominance of the hydrocarbon sector impacted demand for industrial space in 2016. However the lack of sufficient high quality warehousing space constrained occupier movement and kept rents flat throughout the year. Occupancy rates in well-established industrial zones such as Abu Dhabi Airport Free Zone continue to be strong. In turn, Khalifa Industrial Zone (KIZAD) has gained traction, while rates in older industrial locations such as Musaffah have declined.

Figure 3
Dubai industrial rents



Source: Knight Frank Research

Figure 4
Abu Dhabi industrial rents

2017 Outlook

Our short and long term view of the industrial market is positive, as the sector remains an integral component of the country's development and diversification strategy. Looking beyond oil price volatility and geopolitical tensions, it is apparent that both government and private players are committed to expanding industrial activity over the next couple of years.

June 2016 saw the launch of Dubai's Industrial Strategy which aims to 'transform the UAE into a global platform for innovative industries and a destination of choice for international companies'. The strategy prioritises key development areas including aerospace and maritime, aluminium and fabricated metals, pharmaceuticals, food and beverages, and machinery and equipment. To this end we expect investments into these sectors to increase exponentially, thus driving the performance of the industrial sector further.

HOSPITALITY MARKET

The UAE's hospitality market remained subdued in 2016 on the back of weaker macroeconomic conditions, further strengthening of the USD, and a strong supply pipeline. In Dubai, hotel occupancy rates maintained their stability on an annual basis registering 77% YTD Nov 2016; the highest rate amongst its regional peers. Meanwhile, average daily rates (ADR) dropped 12% YTD Nov 2016 compared to the same period last year. This resulted in a 12% decline in revenue per available room (RevPAR).

In Abu Dhabi occupancy rates dropped 4% on an annual basis recording 71% YTD Nov 2016. Given the emirate's dependence on corporate tourism, the sector suffered from low demand on the back of softening global economic conditions. In turn ADR and RevPAR declined 11% and 14% respectively over the same period.

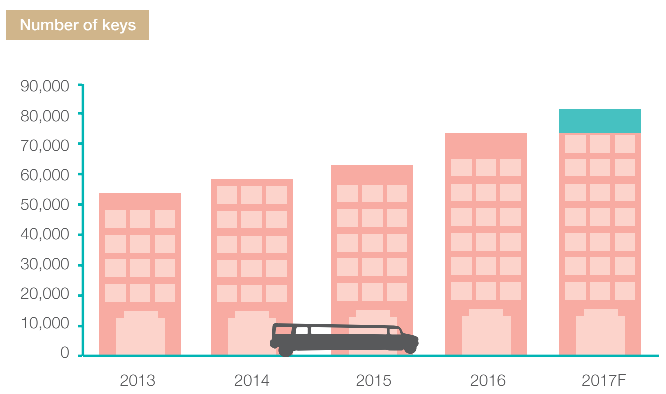
Figure 5
Key performance indicators (average)

DUBAI	ADR	Occupancy	RevPAR
YT NOV 2016	189	77%	149
YT NOV 2015	215	77%	170

ABU DHABI	ADR	Occupancy	RevPAR
YT NOV 2016	124	71%	90
YT NOV 2015	139	74%	105

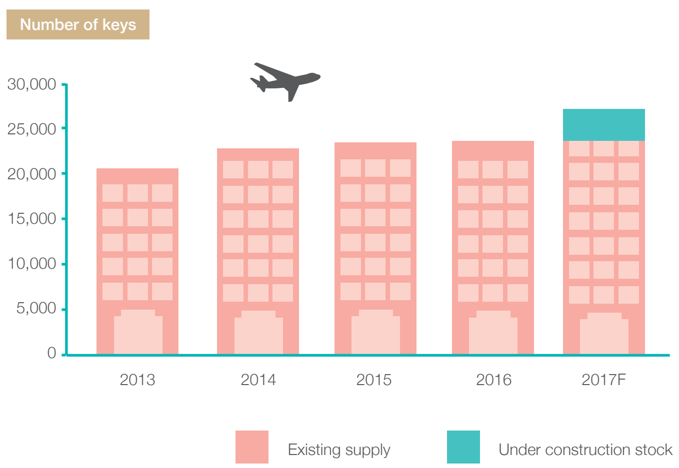
Source: STR Global

Figure 6
Dubai hotel supply



Source: Knight Frank Research

Figure 7
Abu Dhabi hotel supply



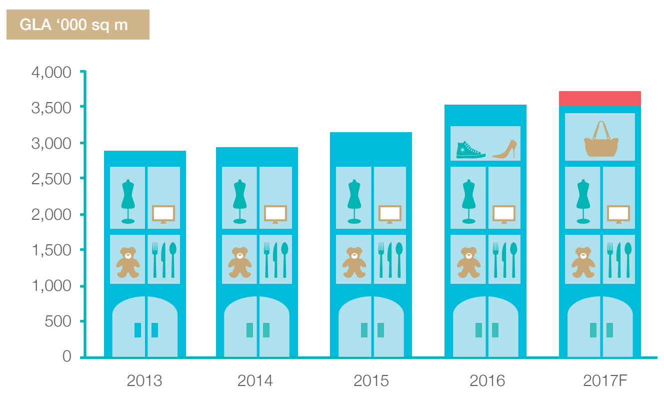
RETAIL MARKET

The retail market in Abu Dhabi and Dubai experienced further softening in 2016 as the strong dirham continued to dent retail sales. This in turn exerted pressure on retailers' ability to meet the high rental rates imposed. Consequently, a number of landlords have introduced flexible lease terms such as longer rent-free periods in order to retain their occupiers.

Well-established malls with higher footfall maintained healthy occupancy rates throughout 2016, indicating continued demand for units in prime locations. However the delivery of additional retail supply in 2016 is expected to put pressure on overall occupancy rates. Meanwhile, the performance of smaller community and neighbourhood centres remained flat with marginal growth witnessed in select locations. These centres cater to the local resident population and are therefore able to ensure continuous revenue streams.

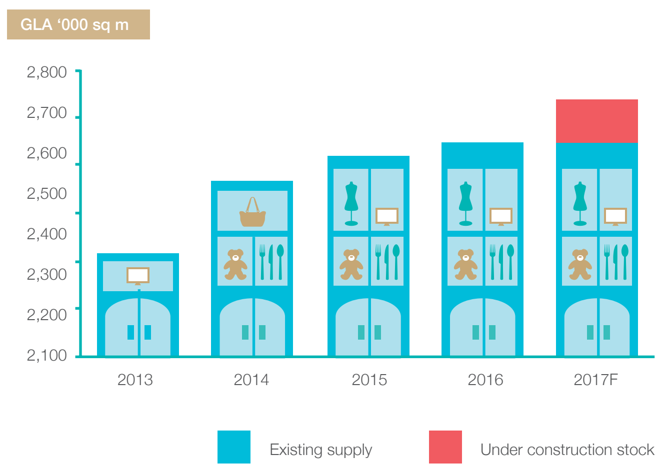
To ensure their permanence amid uncertainty and weaker sentiment, 2016 saw both mall operators and retailers diversify their product offerings and introduce new technologies as a means of reaching out to customers, with e-commerce being on the forefront of this evolution. This trend manifested itself in November 2016 when Mohammed Alabbar, Chairman of Emaar Properties, announced plans to launch Noon.com, an online retailer the size of Amazon. Similarly, luxury retailer Al Tayer launched its first online retail business called Ounass, serving the UAE, Saudi Arabia and Qatar.

Figure 8
Dubai retail supply



Source: Knight Frank Research

Figure 9
Abu Dhabi retail supply



2017 Outlook

The short term outlook for the hospitality market in the UAE remains clouded by the continued appreciation of the USD and prevalent economic uncertainties. However, the delivery of Dubai's theme park complex along with the Opera District and other demand generators is expected to drive demand for Dubai's hospitality market in the next 12 months. Meanwhile in Abu Dhabi, the delivery of more cultural and entertainment facilities is expected to stimulate visitation.

Looking ahead, and amid a strong supply pipeline, hotel operators need to diversify their products to offer more budget accommodation to cater for diverse travellers. This is particularly true as 2016 year-end figures reveal a growing percentage of visitation from non-traditional source markets. Introducing more affordable options will not only balance the hotel supply, which is currently skewed towards the luxury market, but will continue to broaden the country's tourist base and ensure the UAE remains a competitive tourist destination.

2017 Outlook

The general sentiment amongst retailers and mall operators is expected to remain cautionary in 2017, as consumer confidence is low amid job insecurities, and the higher cost of living has impacted residents' purchasing powers. In addition, the strengthening of the USD is showing little respite, particularly in light of further potential interest rate hikes in 2017. This will ultimately push the UAE Dirham even further, making the country an expensive retail destination.

UAE shopping malls are also expected to experience further competitive pressures from online rivals, as more consumers embrace e-shopping. In Dubai, the strong supply pipeline is likely to weaken rents and potentially result in a market correction. Meanwhile in Abu Dhabi, the short-term supply pipeline remains limited, which will keep the emirate's retail market relatively stable over the next 12 months.

RESIDENTIAL MARKET

The residential market in Dubai continued to soften in 2016, albeit at a slower rate. Sale prices in the mainstream market dropped 5% in 2016 versus 7% in 2015, whilst prices in the prime residential market declined 4% in 2016 versus 5% in 2015. Despite the annual dip in prices however, the General and Prime REIDIN sale price indices remained flat on a monthly basis since August 2016. This leads us to believe the residential market is reaching its cyclical trough.

Over the next 5 years and as Dubai prepares to host the Expo 2020, further government spending is expected to boost the market and thus provide positive sentiment to investors. In addition, international corporates are expected to expand their commercial activity, utilising Dubai as a regional hub, thus prompting demand for office space and more residential properties.

In Abu Dhabi the General REIDIN sale price index registered no increase in 2016. While there has been a slowdown in demand on the back of job cuts and corporate restructuring, sale prices remained flat given the limited availability of investment grade quality product. Similarly, rental values remained flat throughout the year following a 1% increase in 2015.

Figure 10
Dubai prime vs. Dubai general residential sales index

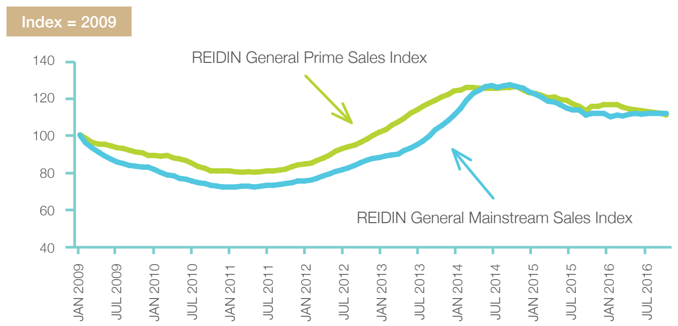
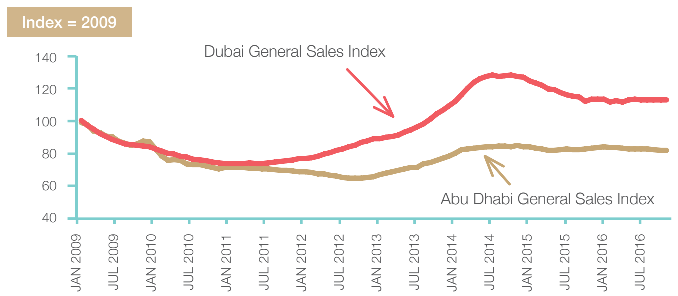
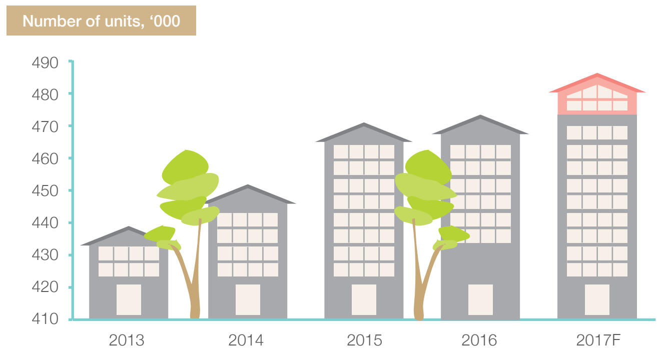


Figure 11
Abu Dhabi vs. Dubai general residential sales index



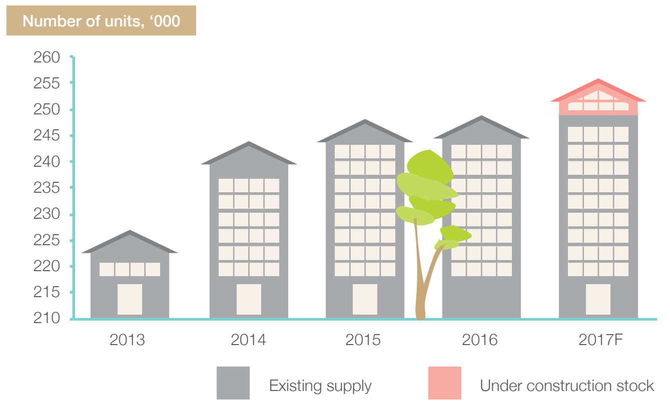
Source: REIDIN

Figure 12
Dubai residential supply



Source: Knight Frank Research

Figure 13
Abu Dhabi residential supply



2017 Outlook

We expect the residential property market in Dubai to gradually recover in 2017 with a potential uptick in sale prices and rents from mid-2017 onwards. Government commitment to spending on infrastructure and facilities, along with the realisation among developers for the need to phase out projects in line with demand, lead us to believe the real estate market in Dubai has become more mature and resilient.

In Abu Dhabi, the reinstatement of a 5% rental cap is unlikely to impact the market given rents are expected to decline further. Similarly, sale prices are likely to drop amid continued cost cutting and corporate restructuring. Meanwhile, the introduction of a 3% housing fee on annual rent is expected to increase cost pressures on households, which would further aggravate demand for property.

OVERVIEW

The UAE in 2017

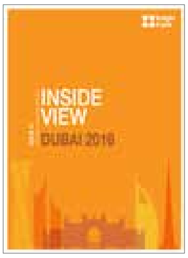
Our outlook for the UAE remains positive in 2017 as oil prices are expected to regain some of the losses recorded. This is expected to boost government revenues and increase spending, particularly on infrastructure and development projects. In light of this, preparations for the Expo 2020 are likely to go ahead in full steam, with investments focused on the expansion of the metro, airport and roads network along with tourism facilities and real estate. Investments in these sectors are expected to support the overall growth of the economy.

However given the UAE's position as a regional hub, we remain cautious of external challenges which may hinder economic growth. Any decision by the US Federal Reserve to increase the interest rates further will strengthen the USD and consequently the UAE Dirham. This will likely put pressure on the cost of living and challenge the competitiveness of the UAE as an international tourist and retail destination.

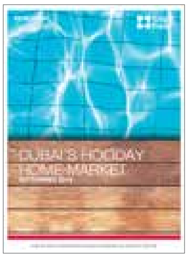
In addition, on-going political uncertainties are likely to impact the performance of financial markets, which in turn will dent investor sentiment and appetite. Among these are the new US administration and any potential protectionist measures, Brexit and the expected trigger of article 50 in March, and a stream of elections across many EU countries (France in May, Germany in September).

RECENT MARKET-LEADING RESEARCH PUBLICATIONS

Abu Dhabi Hospitality Spring 2016



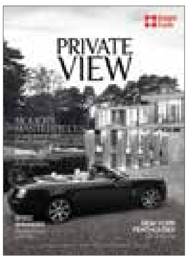
Dubai Inside View 2016



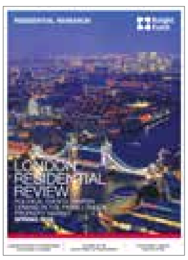
Dubai's Holiday Home Market September 2016

International View 2016

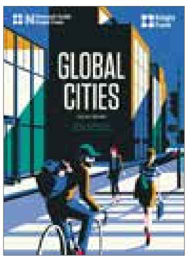
The Wealth Report 2016



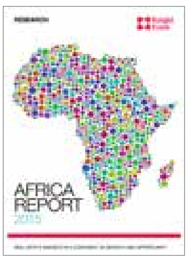
Private View 2016



London Residential Review Spring 2016



Global Cities 2017



Africa Report 2015

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