SAUDI ARABIA REAL ESTATE MARKET REVIEW

Q2 2020

Office Market Review - Q2 2020

Riyadh

Rents in Riyadh's office market continue to register fragmented performance in the year to Q2 2020, with Grade A rents softening marginally to SAR 1,455 per sqm, whilst Grade B rents declined by 2.8% to SAR 753 per sqm.

Vacancy rates across Grade A office spaces decreased by four percentage points from Q2 2019 to reach 7% in Q2 2020, whilst the Grade B vacancy rate increased by two percentage points to reach 32% over the same period.

In Riyadh, there were no major office completions in Q2 2020, leaving the total office stock unchanged at 3.99 million sqm GLA. Looking ahead, total stock is expected to reach an estimated 5.11 million sqm GLA by end of 2022.

Jeddah

Jeddah's office market performance remained subdued in the year to Q2 2020, with Grade A rents falling by 8.1% to SAR 967 per sqm, whilst Grade B rents declined by 8.9% to SAR 685 per sqm.

The vacancy rate across Grade A office space increased by four percentage points from Q2 2019 to reach 18% in Q2 2020, whilst the Grade B vacancy rate also increased by four percentage points to reach 30% over the same period.

In Jeddah, there were no major office completions in Q2 2020, leaving the total office stock unchanged at 1.23 million sqm GLA. By 2022, this is expected to reach an estimated 1.69 million sqm GLA.

DMA

The Dammam Metropolitan Area's (DMA) office market continued to soften in the year to Q2 2020, with Grade A rents falling by 8.5% to SAR 884 per sqm, whilst Grade B rents declined by 10.9% to SAR 590 per sqm.

The vacancy rates across Grade A office space increased by four percentage points from Q2 2019 to reach 30% in Q2 2020, whilst the Grade B vacancy rate also increased by four percentage points to reach 39% over the same period.

In the DMA, there were no major office completions in Q2 2020, leaving the total office stock unchanged at 1.16 million sqm GLA. By 2022, this is expected to reach an estimated 1.47 million sqm GLA.

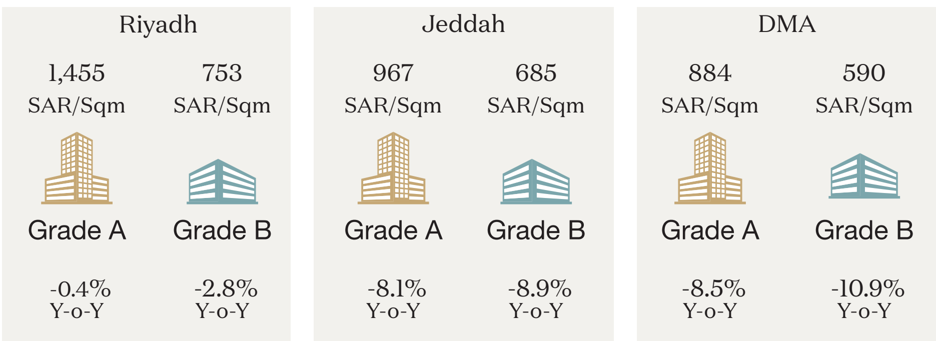
Key trends

The Saudi Arabian Ministry of Investment granted 348 investor licenses in Q1 2020, up 19% from a year earlier. The first quarter of 2020 was reported to be the strongest quarter of investment interest in 10 years. However, we may begin to see interest wane as firms look to scale back expansion plans as a result of the economic fallout caused by the COVID-19 pandemic. With the number of licences issued decreasing from January to March from 126 to 101 respectively, we may already be seeing early signs of this trend.

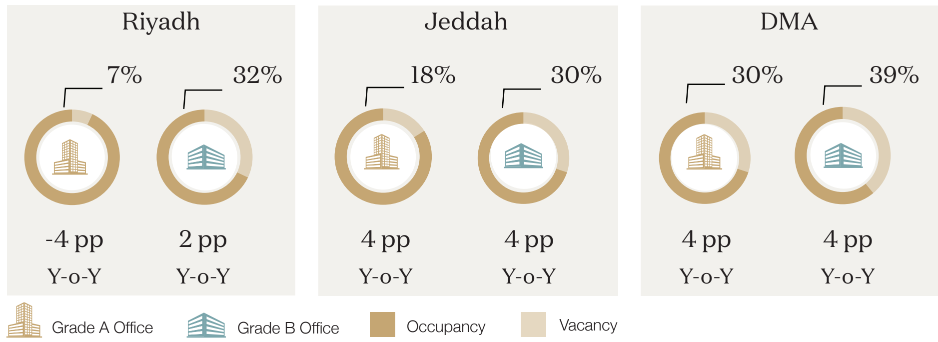
The Kingdom's workspace requirements are shifting from traditional office spaces to a more tech-savvy, elegantly designed and flexible environment. As Saudi Arabia's economy continues to diversify, its workplace needs are shifting where more collaborative and flexible workspaces will be required going forward. In an environment where costs are likely to be much more closely scrutinised, such flexibility is likely to be in even higher demand going forward.

Performance Indicators

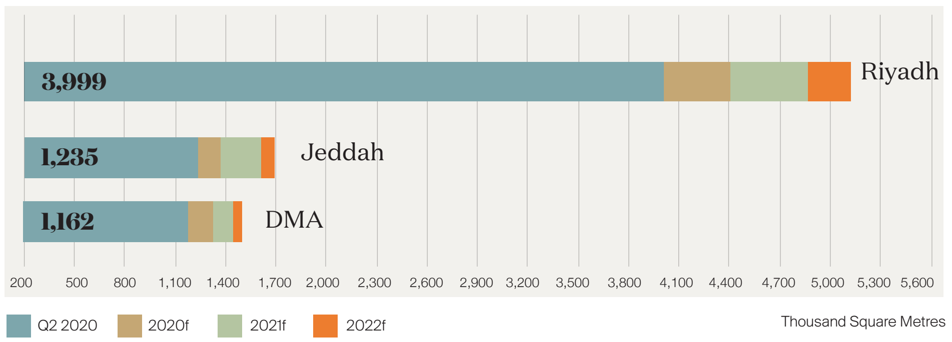
Grade A and B rental rates and YoY % change as at Q2 2020



Grade A and B vacancy as at Q2 2020



Evolution of commercial supply



Source: Knight Frank Research

Residential Market Review - Q2 2020

Riyadh

Residential apartment sales prices in Riyadh fell by 1.2% on average in the year to Q2 2020 to an average of SAR 3,206 per sqm, whilst residential villa prices increased by 3.0% to SAR 3,684 per sqm over the same period.

In the year to Q2 2020, transaction volumes and values fell by 47% and 20% respectively, with lockdown measures enacted to contain the spread of COVID-19 severely impacting transactional activity.

As at Q2 2020, Riyadh's housing stock is estimated to total 1.25 million units and is expected to increase to 1.34 million units by the end of 2022. The majority of this upcoming supply is comprised of apartments and townhouses, a move that matches the changing design and affordability requirements in the capital.

Jeddah

In Jeddah, average residential apartment sales prices increased on average by 2.6% to SAR 3,582 per sqm whereas average villa prices fell by 2.8% to SAR 5,141 per sqm over the same period.

With respect to residential transactions, the total volume and value of residential transactions declined equally by 23% over the same period.

As at Q2 2020, Jeddah's housing stock is estimated to total 840,000 units and is expected to increase to 872,000 units by the end of 2022. The majority of upcoming supply in Jeddah is focused towards middle-income housing, with north Jeddah increasingly seeing the majority of development activity.

DMA

In the year to Q2 2020, residential apartment sales prices in the Dammam Metropolitan Area (DMA) increased on average by 3.7% to SAR 2,900 per sqm whereas average residential villa sales prices fell marginally by 0.5% to SAR 3,405 per sqm.

Over the same period, the volume of residential transactions saw a marginal increase of 1%, whilst the total value of residential transactions rose by 55%.

As at Q2 2020, the DMA's housing stock is estimated to total 328,000 units, this total is expected to increase to 348,000 units by the end of 2022. The majority of this incoming supply comprises high quality apartments and townhouses.

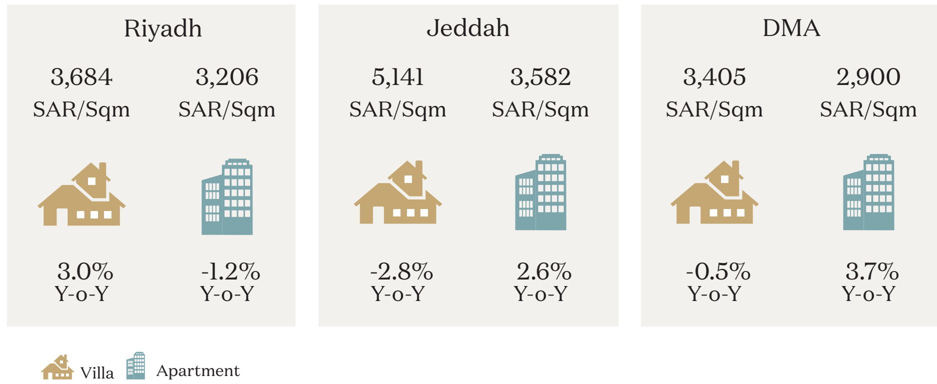
Key trends

The Saudi Real Estate Refinance Company purchased a portfolio of mortgages worth over SAR 3 billion in July 2020. The move aims to provide additional liquidity to the market, allowing for additional loans to be issued in order to increase the home ownership rate across the Kingdom.

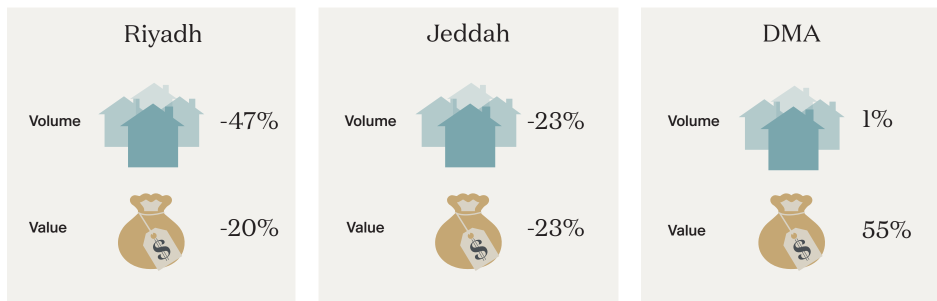
The hike in VAT from 5% to 15% is likely to add to the challenging market conditions that both end-users and developers are facing. From a developers' perspective, we are likely to see this increase in VAT put pressure on cash flows, however, this is likely to be a short term challenge given that eventually this cost will be recoverable. Despite these challenges we anticipate that developers will continue to execute projects, however in an attempt to stimulate demand and recover costs, we may see the introduction of more end-user favourable incentives from developers. To help curtail the impact this will have on affordability, the Ministry of Housing will absorb the increased VAT payment for first time buyers for units worth up to SAR 850,000.

Performance Indicators

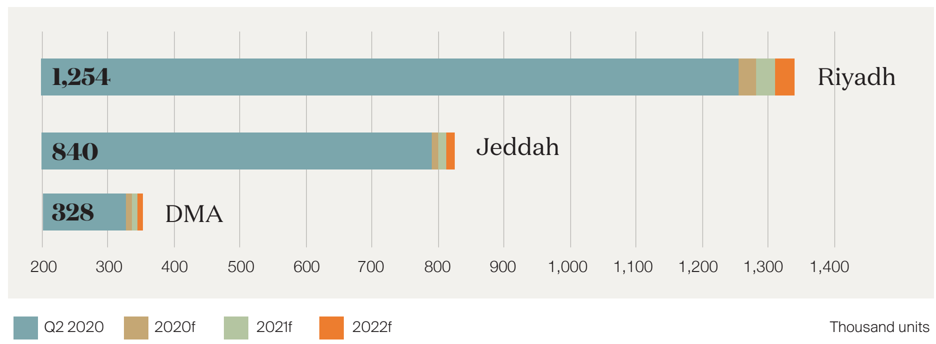
Villas & apartment sales prices and YoY % change as at Q2 2020



YoY % change in the volume and value of residential transactions as at Q2 2020



Evolution of residential supply



Source: Knight Frank Research

Retail Market Review - Q2 2020

Riyadh

Market performance in Riyadh's retail market softened in all segments in the year to Q2 2020, with average regional/ super-regional mall rents falling by 2.6% to reach SAR 2,676 per sqm, whilst average community mall rents fell by 5.4% to reach SAR 1,980 per sqm.

The market-wide vacancy rate in Riyadh increased by three percentage points in the year to Q2 2020 to reach 18%. The average vacancy rate in super-regional/ regional malls remained relatively stable, whereas community malls and Grade B retail centres have seen their vacancy rates trend higher.

Riyadh's retail stock stood at 2.78 million sqm GLA as at Q2 2020. By 2022, total stock is expected to reach 3.51 million sqm GLA.

Jeddah

Rents in Jeddah's retail market continued to soften in the year to Q2 2020, with average regional/ super-regional mall rents falling by 3.8% to SAR 2,645 per sqm, whilst average community mall rents fell by 4.1% to reach SAR 1,745 per sqm.

The market-wide vacancy rate in Jeddah increased by four percentage points in the year to Q2 2020 to reach 14%. This increase has primarily been driven by vacation of space by small and medium sized retailers in retail spaces where limited concessions were offered to support such operations through the downturn in demand.

Jeddah's retail stock stood at 1.86 million sqm GLA as at Q2 2020. By 2022, this is expected to reach an estimated 2.77 million sqm GLA. However, given weaker market conditions, we expect some projects may be delayed.

DMA

The DMA's retail market registered softening market performance across all segments in the year to Q2 2020, where average regional/ super-regional mall rental rates fell by 1.3% to reach SAR 2,305 per sqm, whilst average rental rates for community malls dropped by 2.9% to SAR 1,650 per sqm.

The market-wide vacancy rate in the DMA increased by two percentage points in the year to Q2 2020 to reach 8%. Over the last quarter a decrease in vacancy rates has been recorded in those malls where landlords have successfully introduced new retail concepts to attract and retain tenants.

The DMA's retail stock stood at 1.13 million sqm GLA as at Q2 2020. By 2022, this total is expected to reach an estimated 1.54 million sqm GLA.

Key trends

On the back of weaker economic prospects, the increase of the VAT rate from 5% to 15% and the suspension of living allowances, consumer spending in Saudi Arabia is expected to fall by 5.5% in 2020 according to data from Oxford Economics. More so, consumer spending is expected to only surpass 2019 levels by 2022.

Despite the challenge bought about by COVID-19 and the increasing utilisation of e-commerce, the Saudi Arabia retail market's outlook for the long-run remains strong particularly for locations which offer suitable entertainment and leisure demand drivers to help drive retail spending.

To compete with the growing e-commerce market in Saudi Arabia, traditional bricks and mortar retail brands continue to implement omnichannel strategies and are increasingly investing in outlet modernisations. This multi-channel offering will be crucial to the long run success of bricks and mortar retail and may even lead to additional revenue sources for landlords.

Performance Indicators

Retail market lease rates as at Q2 2020

	Riyadh		Jeddah		DMA	
	Regional/Super-Regional mall	Community mall	Regional/Super-Regional mall	Community mall	Regional/Super-Regional mall	Community mall
SAR/Sqm	2,676	1,980	2,645	1,785	2,305	1,650
Y-o-Y	-2.6%	-5.4%	-3.8%	-4.1%	-1.3%	-2.9%

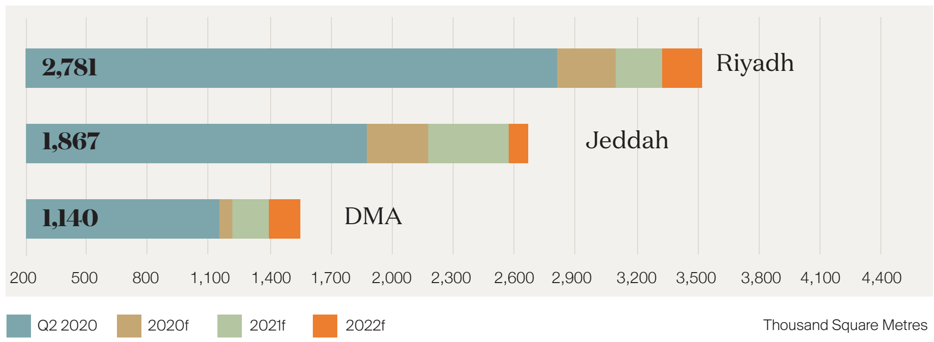
Regional/Super-Regional mall   Community mall

Retail occupancy rates

	Riyadh		Jeddah		DMA	
	Q2 2019	Q2 2020	Q2 2019	Q2 2020	Q2 2019	Q2 2020
Vacancy	15%	18%	11%	14%	6%	8%
Y-o-Y	3 pp		4 pp		2 pp	

Occupancy   Vacancy

Evolution of retail supply



Source: Knight Frank Research

Hospitality Market Review – Q2 2020

Riyadh

Whilst RevPAR levels in Riyadh softened y-o-y by 5.0% in the year to June 2020, the capital's hospitality market has witnessed a significant relative outperformance in comparison the broader Saudi Arabian hospitality market. This relative outperformance over this period has been underpinned by the extension of the Riyadh Season initiative as well as a slight variance in school holiday periods in early 2020. Further declines are expected in the coming months, where only the resumption of international travel is likely to act as a catalyst for any potential recovery.

Total quality hotel supply in Riyadh stood at 16,674 rooms as at June 2020. Taking into consideration only projects that have broken ground, supply is expected to increase by 33% by the end of 2022.

Jeddah

ADRs in Jeddah fell y-o-y by 37.0% in the year to date June 2020, whilst occupancy decreased by 17.7 percentage points. As a result, marketwide RevPAR levels decreased y-o-y by 56.9%. Over and above the challenges of attracting inbound corporate tourism seen in Riyadh, hotel owners in Jeddah have faced the additional challenge of religious visitation restrictions. In the month of June alone RevPAR levels fell by 78.9%.

Jeddah's total quality hotel supply stood at 11,171 rooms as at June 2020. The supply of quality hotel rooms is expected to increase by 46% considering only projects that are currently under construction and due for completion by the end of 2022, assuming that they complete as planned.

DMA

In the year to date June 2020, ADRs in the DMA fell y-o-y by 2.1%, whilst occupancy decreased by 2.4 percentage points. In turn, RevPAR decreased y-o-y by 6.5%. The DMA is a traditionally a popular destination for domestic visitation and has benefited from sustained visitation over the summer period, as Saudi Nationals who are unable to travel abroad instead holiday within the Kingdom. As a result, the DMA has been more reliant than other major cities with RevPAR only falling by 2.5%.

The DMA's total quality hotel supply stood at 8,231 rooms as at June 2020. Taking into consideration only projects that have broken ground, supply is expected to increase by 24% by the end of 2022.

Key trends

The Saudi Arabian government has launched a SAR 15 billion tourism fund as part of the first phase of its National Tourism Strategy, which aims to develop 38 sites across seven destinations by 2022. As part of Vision 2030, the Saudi Arabia government is aiming for the tourism industry to make-up at least 10% of its total GDP, up from 3% currently.

With the international arrivals being curtailed across the Kingdom corporate, leisure and religious tourism has come to all but a standstill since the 15th March 2020.

Given the current challenges associated with inbound corporate visitation, cities that have historically been centres of business activity have faced challenges attracting hotel guests. Areas which have traditionally received religious visitation have fared no better given that Hajj and Umrah have been reduced in scale significantly this year. Looking forward, it is reasonable to expect a rise in leisure visitation on a domestic level not only to traditional destinations but also to secondary cities such as Abha, Baha and Al Ahsa.

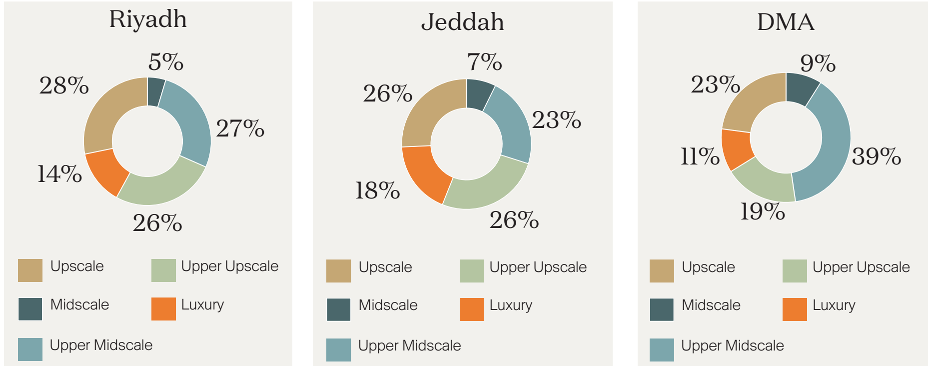
In response to declining revenues, owners are looking to cut costs universally at an unprecedented scale, this trend is likely to continue into next year.

Performance Indicators

KPIs - ADR, Occupancy and RevPAR - Y-o-Y % change YTD June 2020

	Riyadh	Jeddah	DMA
ADR	-2.5%	-37.0%	-2.1%
Occupancy	-1.4 PP	-17.7 PP	-2.4% PP
RevPAR	-5.0%	-56.9%	-6.5%

Existing quality hotel supply market segmentation YTD June 2020



Existing and upcoming quality hotel supply

	Riyadh	Jeddah	DMA
Existing supply June 2020	16,674 keys	11,171 keys	8,231 keys
Increase in supply until 2022	+33%	+46%	+24%

Source: Knight Frank Research and STR Global

KSA Real Estate Market Outlook

Macroeconomic Outlook

Looking ahead, forecasts from Oxford Economics show that Saudi Arabia's GDP is expected to contract by 7.5% in 2020. This trend is set to be underpinned by contractions in both the oil and non-oil sectors.

For the prior, as global lockdowns came into effect, demand for oil plummeted and oil prices followed soon after. In an attempt to support oil prices, OPEC+ agreed to reduce production from May 2020, these cuts have since been extended to July 2020. This reduction in production is expected to have a material impact on Saudi Arabia's GDP, particularly given that its oil sector accounts for 40.2% of GDP.

For the latter, Saudi Arabia's Purchasing Managers' Index (PMI), which tracks the country's private non-oil economy, is a timely indicator as to the impact of lockdown measures had on the Kingdom's private sector. Saudi Arabia's PMI recorded a reading of 47.7 in June 2020, indicating that economic activity continued to contract for the fourth straight month. With restrictions on mobility only gradually lifted from late May, we are only likely to see economic activity begin to normalise over the coming months. This slowdown in activity in the non-oil private sector, which accounts for 41.0% of Saudi Arabia's GDP will also have a material impact on GDP over the course of 2020.

As economic activity contracts, employment in Saudi Arabia is expected to follow suit with a 9.0% contraction forecast in 2020. Total employment in Saudi Arabia is expected to return to 2019 levels by 2022.

Overall, the depth of the contraction and the rate of recovery will be dependent on the rate at which the global economy and global mobility returns to some form of normality. These factors will underpin demand and activity in the hydrocarbon, travel and tourism and wholesale and retail trade sectors, all of which form significant parts of Saudi Arabia's economy.

The COVID-19 pandemic is forecast to have a material impact on Saudi Arabia's economy, with GDP and employment forecast to decline in 2020 by 7.5% and 9.0% respectively.

KEY CONTACTS

Stefan Burch, *MRICS*
General Manager & Partner
+966 53 0893 297
Stefan.Burch@me.knightfrank.com

Stephen Flanagan, *MRICS*
Partner – Valuation & Advisory
+966 55 8866 480
Stephen.Flanagan@me.knightfrank.com

Amar Hussain
Data Manager
+966 55 2323 036
Amar.Hussain@me.knightfrank.com

Abdullah M Alsayegh
Senior Analyst
+966 55 2323 660
Abdullah.Alsayegh@me.knightfrank.com

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