A quarterly review of the residential, office, retail and hospitality markets across Saudi Arabia

Knight Frank

Saudi Arabia Real Estate Market Review

Q2 2021

OFFICE MARKET

RIYADH

Riyadh's office market continues to experience fragmented performance. Average Grade A rents increased by 1.5% over the last 12 months, while Grade B rents experienced declines of 1.1% over the same period. The relative outperformance of Grade A offices can be attributed to a marked increase in the number of licences granted to foreign investors wishing to set up businesses in the Kingdom. Indeed, the number foreign investment licenses issued have almost doubled from about 700 in 2018 to nearly 1300 last year, suggesting that not only is office demand being created, but it is also being sustained.

Furthermore, we have also seen an uptick in office requirements from newly created public sector companies. In general, demand is expected to continue rising as government driven economic reforms spur renewed confidence and hasten business growth.

On the supply front, the completion of a small office development along King Fahad Road added approximately 9,000 sqm to the city's supply. This minor addition left the total office stock relatively unchanged at 4.2 million sqm. Total office space is expected to reach 5.3 million sqm by the end of 2023.

JEDDAH

Jeddah's office market performance remained relatively subdued in the year to Q2 2021, with Grade A rents falling marginally by 0.8%. Grade B rents declined by 1.6% over the same period.

Like in many other markets around the world, the pandemic is driving a rethink in occupational strategies, keeping office demand muted. Indeed, some businesses have begun to shrink their office footprints, not necessarily in response to emerging hybrid working patterns, but more due to the need to contain costs. This cost-conscious behaviour is also manifesting itself in the form of a rise in requests for flexible payment plans and shorter leases.

Supply however continues to grow, with the MASIC Business Centre and Nagy Tower adding 25,000 sqm of new space to the city's stock in Q2, taking the total to 1.3 million sqm. By 2023, this figure is expected to rise to 1.8 million sqm.

DMA

Rental performance in Dammam Metropolitan Area's (DMA) office market continued to soften, with Grade A and Grade B rents declining by 1.7% and 2.5%, respectively, over the last 12 months.

Supply, however, continues to trickle on to the market. Q2 saw the completion of Joaib Tower and Deim Commercial Centre, which added approximately 22,600 sqm of space to the city's supply. These additions bring the total office stock to 1.3 million sqm. By 2023 total stock is expected to grow to 1.5 million sqm.

Over the next 12 months we expect the office market in DMA to remain under pressure. Rents and occupancy rates are likely to soften further as supply outstrips demand. In the long term, however, we see demand for office space picking up as economic reforms drive job creation rates and inward investment, spurring office space demand.

Key trends

Saudi Arabia's unemployment rate has dropped to its lowest level in almost five years. The unemployment rate for Saudi citizens fell to 11.7% in Q1, down from 12.6% at the end of last year.

Several factors have contributed to this; primarily the government's rapid response to COVID-19 and economic reforms stemming from Vision 2030, which have led to an overall improvement in business conditions.

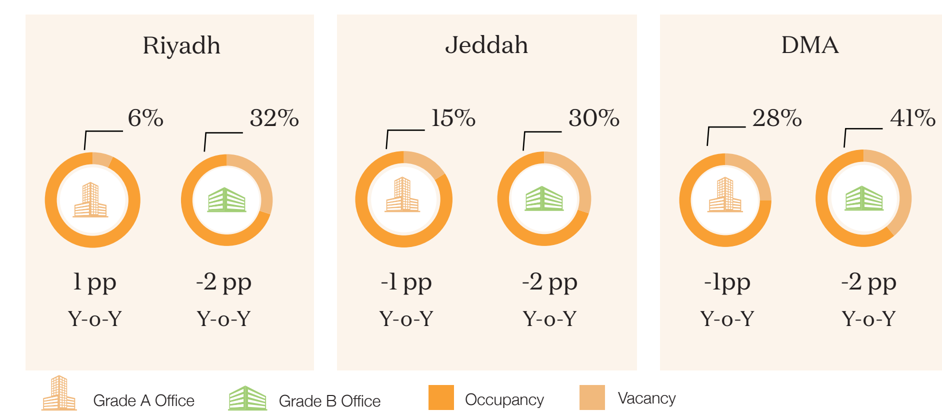
In addition, an increase in female participation in the workforce, which rose to 33.6% from 32.1% in Q1, has helped to lift overall employment levels.

Market Performance Indicators

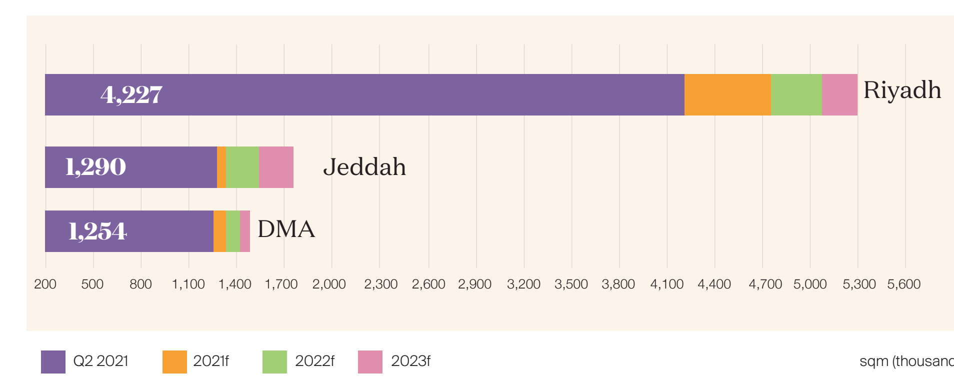
Grade A and B rental rates and YoY % change as at Q2 2021

	Riyadh Grade A	Riyadh Grade B	Jeddah Grade A	Jeddah Grade B	DMA Grade A	DMA Grade B
SAR/sqm	1,475	744	992	694	904	576
Y-o-Y	1.4%	-1.1%	-0.8%	-1.6%	-1.7%	-2.7%

Grade A and B vacancy as at Q2 2021



Evolution of office supply



Source: Knight Frank

RESIDENTIAL MARKET

RIYADH

The residential sector has been a key area of focus for the government in recent years, with attention primarily centred on boosting home ownership levels and providing higher quality housing options and the efforts are paying off. The mortgage market has boomed and the delivery of affordable residential units through the Sakani Program has underpinned the market's buoyancy. Unsurprisingly, apartment and villa sale prices have increased by 7.6 % and 4.7%, respectively, over the last 12 months and demand for housing continues to rise.

On the transactions front, the total number of homes sold has increased by 77% in the 12 months to June, while the total value of transactions has grown by 34% over the same period. The government's continued focus on the sector is also delivering a far more active development market, with 100,000 homes expected to complete by the end of 2023, taking the total housing stock in the capital to 1.4 million units.

JEDDAH

In the Red Sea coastal city of Jeddah, the residential market appears to be a story of two halves: apartment prices have risen by 5.9% over the last 12 months, while villa prices have declined by 2% over the same period. The drop in villa prices highlights the rising affordability issues, with the average income multiplier for villas standing at 12.4, compared to 4.8 for apartments. And this disparity looks set to widen, particularly given the lack of suitable supply aimed at mid-tier buyers, which is fuelling a supply-demand imbalance.

Residential transaction volumes and values in Jeddah increased by 44% and 13% respectively in the year to June; a trend driven by a notable increase in the uptake of mortgages provided by banks and financial institutions.

Jeddah's housing stock is expected to grow by just 35,000 units by the end of 2023, taking the total number of homes to over 890,000.

DMA

Mirroring the trend in Jeddah, average apartment prices in DMA increased by 4.6% in the year to Q2 2021, whereas average villa prices fell by 4.1% over the same period. Like Jeddah, affordability issues are growing in DMA, with average villa prices standing at 6 times annual incomes, compared to 2.8 times annual incomes for apartments.

Unlike elsewhere in the Kingdom, transaction volumes have slipped in DMA, falling by 8% over the last 12 months, while the total value of transactions decreased by 12% over the same period. The rising affordability challenge, combined with a lack of suitable supply for middle and lower tier buyers, is contributing to slowing sales activity.

As at the end of Q2, DMA's housing stock stood at about 338,000 units. 20,000 units are due to complete by the end of 2023, most of which are expected to be better quality apartments and townhouses.


A view of Riyadh

Key trends

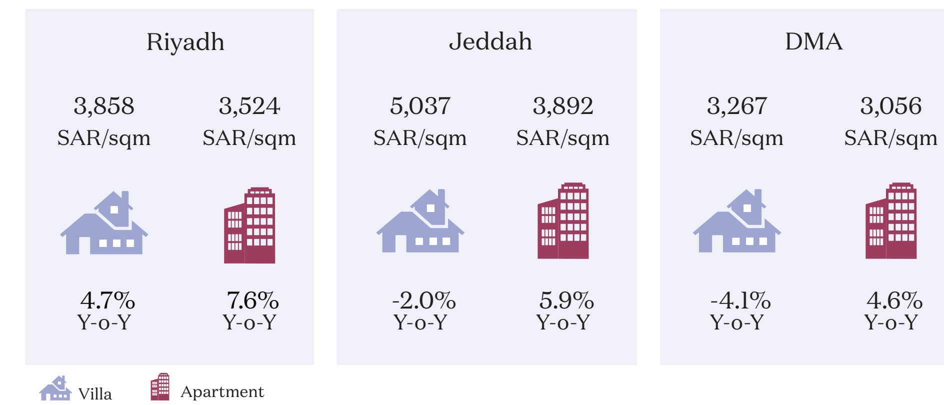
In the year to the end of Q2, residential sales volumes across Saudi Arabia surged by 26%, with the total value of residential transactions increasing by 2% over the same period. Around 58,000 residential transactions were recorded in Q2, compared to 47,000 deals during the same period last year. The government's continued efforts to widen the mortgage market, combined with the delivery of large affordable housing schemes through the Sakani Program have fostered a remarkably resilient residential landscape.

Indeed, the value of real estate loans provided by Saudi banks increased by 10.8% to reach SAR 474.5 billion in Q1, with new mortgage loans for individuals accounting for 75.4% of the total. According to data from the Saudi Central Bank, around 90,000 new mortgage contracts were issued in Q1 2021, with a total value of SAR 46.7 billion, up 50% from Q1 2020.

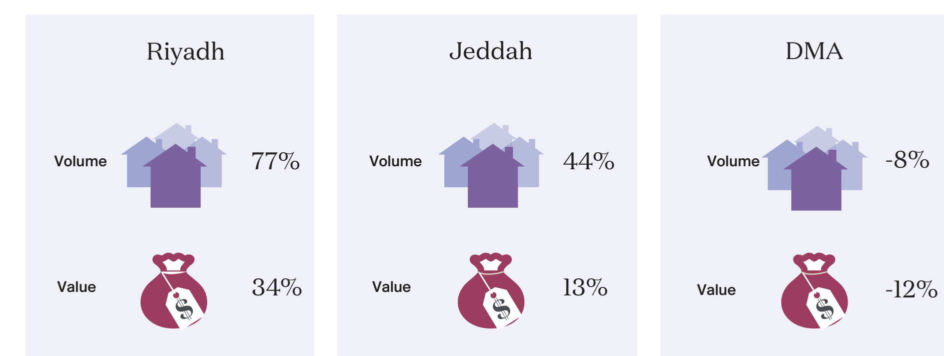
Around 17,500 new mortgages worth SAR 7.5 billion were issued in June alone, up 13.3% from June 2020. 80% were linked to villa or townhouse purchases, with the rest granted to purchase apartments and residential land plots. This is perhaps unsurprising given that villas are, on average, more than three-times as expensive as apartments across the country.

Market Performance Indicators

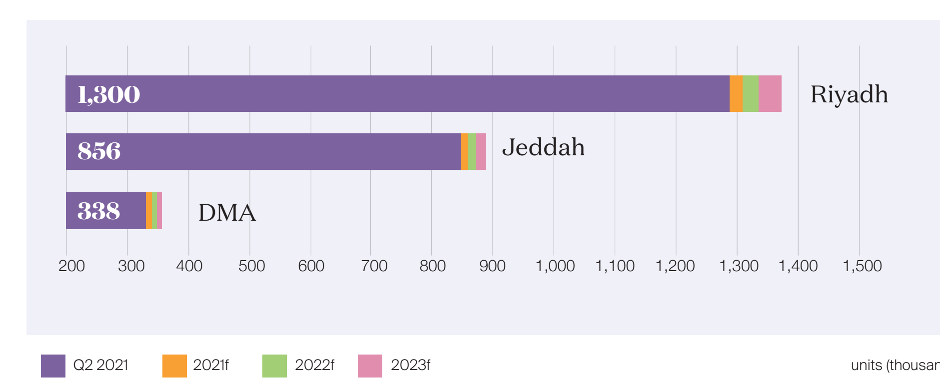
Villa & apartment sales prices and YoY % change as at Q2 2021



YoY % change in the volume and value of residential transactions as at Q2 2021



Evolution of residential supply



Source: Knight Frank

RETAIL MARKET

RIYADH

Average regional and super-regional mall lease rates registered a decline of 1% across the Saudi capital in the 12 months to the end of June. Community malls (-1.5%) too have seen rents softening. Repeated lockdowns and border closures have taken their toll on footfall and retailers' appetite to expand or take new space has remained subdued as a result.

Furthermore, new supply continues to be delivered to the market, further dampening the prospects for a return to growth in rents. The most noteworthy completions this quarter were Park Avenue and the extension of Nakheel Mall, which together added approximately 100,000 sqm to the city's retail stock, taking the total to 3 million sqm.

While demand for new space from retailers has been mute, developers have taken note of changing attitudes and expectations from consumers, with the majority of new supply focussing on lifestyle or experience-based retail developments, where placemaking is central. In general, we expect rents to remain supressed, particularly as new completions look set to accelerate. In fact, some 700,000 sqm of retail space is due to complete by 2023.

JEDDAH

Like Riyadh, rents in Jeddah's retail market faltered during Q2, with average regional and super-regional mall rents falling by 1.5% in the 12 months to the end of Q2. Community mall rents fell by 2.8% over the same period.

The market-wide vacancy rate in Jeddah rose to 15% in the year to Q2. The rising vacancy rate was in large part driven by the completion of Wow Square and Crystal Mall, which together added around 23,000 sqm of new space, taking the total formal retail stock to almost 2 million sqm.

By the end of 2023, this is expected to rise by almost 30% to 2.7 million sqm, which is likely to keep rental growth suppressed.

DMA

Mirroring other markets elsewhere in the Kingdom, DMA's retail market experienced rental declines of 2.7% and 1.7% in community malls and regional and super-regional malls, respectively, over the last 12 months.

Despite there being no major new additions of stock, the vacancy rate across DMA crept up by 2% as retailers continue to right size operations to match the much-reduced footfall as a result of the pandemic. Total retail stock currently stands at about 1.2 million sqm. By 2023, this figure is expected to reach 1.6 million sqm.

In the short term, we expect lease rates and occupancy levels of regional and super-regional malls to demonstrate greater stability as no major schemes are due to be delivered over the next 12 months.

Key trends

According to the Saudi Central Bank (SAMA), consumer spending in Saudi Arabia increased by 2.1%, to around SAR 261 billion in Q1, compared to SAR 256 billion over the same period last year.

The food & beverages sector has enjoyed the most significant boost, with spending surging by 35% to SAR 17.4 billion, while spending in restaurants and cafes alone rose by 59% over the same period.

This relative outperformance is linked in part to the slight easing of lockdown restrictions, which boosted footfall across the Kingdom's food and beverage outlets.

Online retailing continues to boom in Saudi Arabia, chipping away at demand for new bricks and mortar stores. Across the country, e-commerce sales increased by 28% to reach a record SAR 22.5 billion in 2020. Saudi Arabia's e-commerce market is forecast to grow at a CAGR of 7% between 2020-2024 (Statista).

Market Performance Indicators

Retail market lease rates as at Q2 2021

	Riyadh		Jeddah		DMA	
	Regional/Super-Regional mall	Community mall	Regional/Super-Regional mall	Community mall	Regional/Super-Regional mall	Community mall
Rate	2,670 SAR/sqm	1,950 SAR/sqm	2,685 SAR/sqm	1,740 SAR/sqm	2,295 SAR/sqm	1,635 SAR/sqm
Change	-1.0% Y-o-Y	-1.5% Y-o-Y	-1.5% Y-o-Y	-2.8% Y-o-Y	-1.7% Y-o-Y	-2.7% Y-o-Y

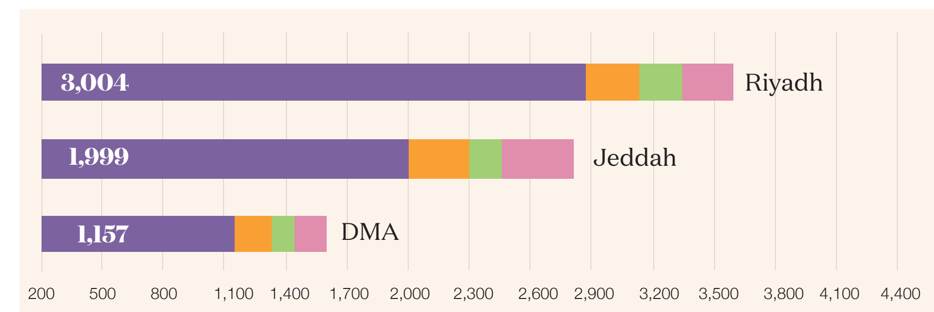
Regional/Super-Regional mall Community mall

Retail occupancy rates

	Riyadh	Jeddah	DMA
Q2 2020 (vacancy)	17%	13%	8%
Q2 2021 (vacancy)	18%	15%	10%
Change	-1 pp Y-o-Y	-2pp Y-o-Y	-2 pp Y-o-Y

Occupancy Vacancy

Evolution of retail supply



Q2 2021 2021f 2022f 2023f sqm (thousands)

Source: Knight Frank

HOSPITALITY MARKET

RIYADH

Average daily rates (ADR) and average occupancy levels have continued to slip, dropping by 3.3% and 18.4%, respectively, in the year to May 2021. As a result, market-wide RevPAR levels fell by 21% over this period to SAR 254. The faltering performance is largely due to the significant reduction in corporate tourism in Riyadh due to Covid-linked travel restrictions.

In the short term corporate demand for hospitality in Riyadh is expected to remain subdued. In addition, with supply due to increase by 27%, or 4,800 rooms, by 2023, we expect sustained downward pressure on both occupancy and ADR. Total quality hotel supply in Riyadh currently stands at about 17,700 rooms.

JEDDAH

Jeddah's hospitality market has outperformed the rest of the country for a number of reasons. The principal driver has been the resumption of the Umrah pilgrimage, the recent Eid holidays and increased summer domestic tourism, stemming from various international travel restrictions. As a result, in the year to May 2021, ADR grew y-o-y by 32.5% to SAR 722, while occupancy increased by a fifth to nearly 49%. Over this period, RevPAR grew by a substantive 60% to SAR 352.

Total quality hotel supply in Jeddah stood at 13,230 rooms as at the end of May 2021. Taking into consideration only projects that have broken ground, supply is expected to increase by 64% by the end of 2023 to 20,600 rooms, higher than Riyadh and DMA combined.

DMA

In the year to May 2021, average occupancy in DMA remained relatively stable at c.50%, while ADR grew y-o-y by 8.3%. Over this period, RevPAR increased by 7.4%. Performance in DMA has been driven by Al Khobar, where RevPAR increased by 16.7% y-o-y, whereas in Dammam, over the same period, we have seen RevPAR fall by 33.7%. Al Khobar's performance has been underpinned by the appeal of its beach resorts to domestic tourists who have sought out staycation options in the Kingdom due to Covid-linked international travel restrictions.

DMA currently has 11,800 quality hotel rooms. This figure is expected to increase by almost a fifth (18%) by the end of 2023 to 13,800 rooms.

Ritz Carlton, Riyadh

SAUDI ARABIA REAL ESTATE REVIEW I Q2 2021

Key trends

According to World Travel and Tourism Council, Saudi Arabia advanced to 16th place in the global ranking of the largest Travel and Tourism Economies in 2020, from 17th place a year earlier. Saudi Arabia's progress in the ranking of top 20 countries comes from the government's ambitious strategy to transform the tourism sector and establish a vibrant entertainment and tourism industry. This is expected to be realised through mega tourism projects in Qiddiya, along the Red Sea coast, Amaala, NEOM, AlUla and Diriyah Gate. Together, these schemes will add around 70,000 hotel rooms to the Kingdom, spread across developments worth USD545 billion, all to be completed by 2030.

Separately, the Saudi Cruise Company, launched in January 2021 by the Public Investment Fund (PIF), has recently inaugurated its first cruise ship terminal at Jeddah Islamic Port, with a capacity of 2,500 passengers. The Saudi Cruise Company expects to create 50,000 jobs in the sector by 2025, with 1.5 million cruise visitors annually forecast by 2028.

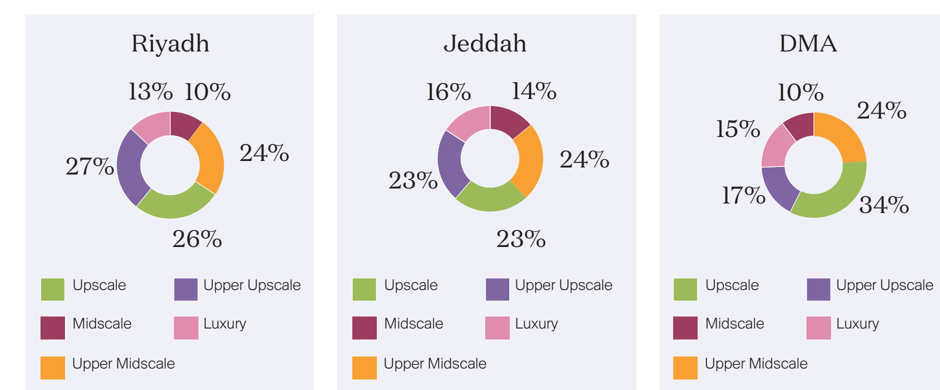
In early August, the government announced the reopening of the country's borders to fully vaccinated tourists from 49 countries (mainly the EU, US and UK), after a 17-month closure. Clearly, this change will go some way in aiding the recovery of the tourism sector.

Market Performance Indicators

KPIs - ADR, Occupancy and RevPAR - Y-o-Y % change YTD May 2021

	Riyadh	Jeddah	DMA
ADR	-3.3%	32.5%	8.3%
Occupancy	-18.4%	20.8%	-0.8%
RevPAR	-21.1%	60.1%	7.4%

Existing quality hotel supply market segmentation YTD May 2021



Existing and upcoming quality hotel supply

	Riyadh	Jeddah	DMA
Existing Supply	17,708 keys	13,230 keys	11,820 keys
Increase in supply until 2023	+27%	+64%	+18%

Source: Knight Frank, STR Global

MACROECONOMIC OUTLOOK

According to the General Authority for Statistics, Saudi Arabia's real GDP contracted by 3.3% year-on-year as at the end of Q1. This sharp decline was underpinned by a substantial fall in hydrocarbon sector activity, which fell by 12% due to crude oil production cuts agreed by OPEC+ in May 2020. However, the non-oil sector registered growth of 3.3% over the same period.

The non-oil and private sectors are at the centre of Saudi Arabia's Vision 2030 and the reforms launched to bolster these sectors are already being felt widely across the economy. Indeed, the latest private sector PMI reading for the Kingdom stood at 55.8 in July, representing the 11th month of expansion and business growth. According to the General Department of Statistics, the private sector's contribution to GDP rose to over 44% in Q1, compared to 41% at the same time last year. The Q1 reading of private sector contribution to Saudi GDP is now at the highest level in over 10 years.

Looking ahead, the IMF forecasts a return to growth for the Kingdom's economy. The region's largest economy is expected to see GDP growth of 2.1% in 2021, down from the 2.9% predicted in April 2021 due to the lingering global impact of the pandemic.

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