Marked surge in foreign direct investment

Rising digital dependency in the retail sector

Holistic hospitality, health & well-being on the rise

Saudi Arabia Commercial Market Review

Q4 2021

OFFICE MARKET OVERVIEW

Over the last 12 months, the office market in Saudi Arabia's key markets experienced fragmented performance.

Rental values for Grade A office space in Riyadh and Jeddah have continued to grow amid rising office demand, owing to continued growth in foreign direct investment into Saudi Arabia. In fact, Saudi Arabia's Ministry of Investment granted 1,053 foreign investor licenses during the first half of 2021, up by 108% y/y, which has contributed to increased demand for office space.

Furthermore, the "Program HQ" initiative continues to gain traction. Recently, around 44 multinational companies announced plans to set up their headquarters in the Kingdom.

The decision has also spurred some regional businesses to reassess their Middle East office footprints and begin planning for program HQ's long-term challenges and advantages.

The sustained growth in demand is reflected in rental trends; indeed, Grade A office rents across the capital were up by 3.4%, to SAR 1,500 per sqm in the 12 months to the end of Q4 2021. Likewise, rental values for Grade A office space in Jeddah increased by 1.3% to SAR 1,013 over the same period.

The Dammam Metropolitan Area (DMA) is the only market where Grade A rents fell by 1% during 2021, as demand for office space in DMA remained subdued.

Grade B lease rates across all of Saudi Arabia's key markets remain weak. This trend is mainly underpinned by the desire of tenants to relocate to better quality space, which has forced landlords to offer flexible leasing terms to retain existing occupiers. While not quite a race to the bottom, tenants in Grade B space are firmly in the driving seat. As a result, a two-tiered market is emerging in all major cities where secondary assets with poor access and parking limitations are struggling to hold rents stable. At the same time, buildings situated in better locations, with modern amenities, command premium rents that continue to creep up.

Key trends

Flight to quality

Rising demand for prime assets

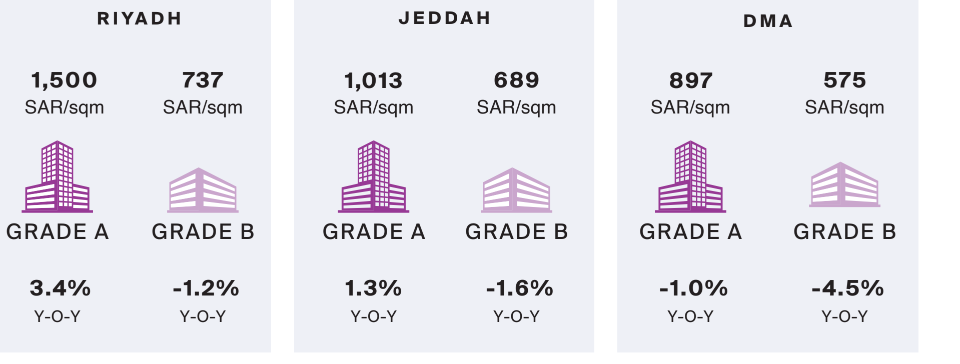
Net foreign direct investment jumped to US$ 13.8 billion in Q2 2021, up by 664% q/q, the highest level in ten years

1,053 foreign investor licenses were issued in the first half of 2021, up by 108% y/y

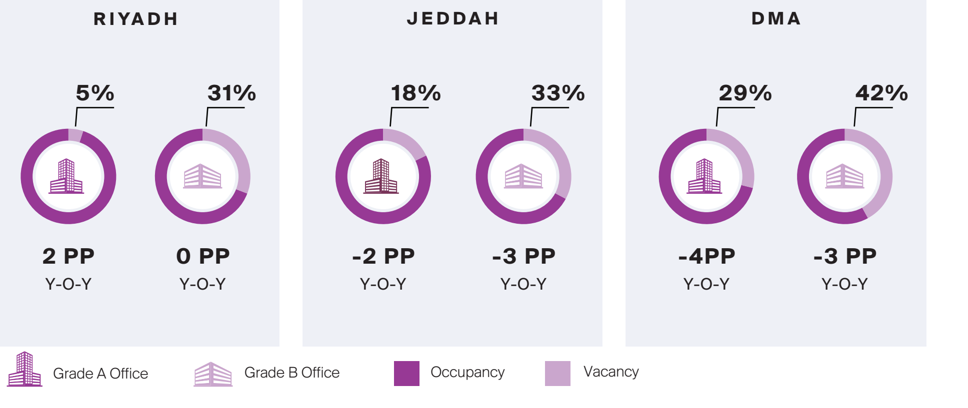
Premium rents for the best space

Market Performance Indicators

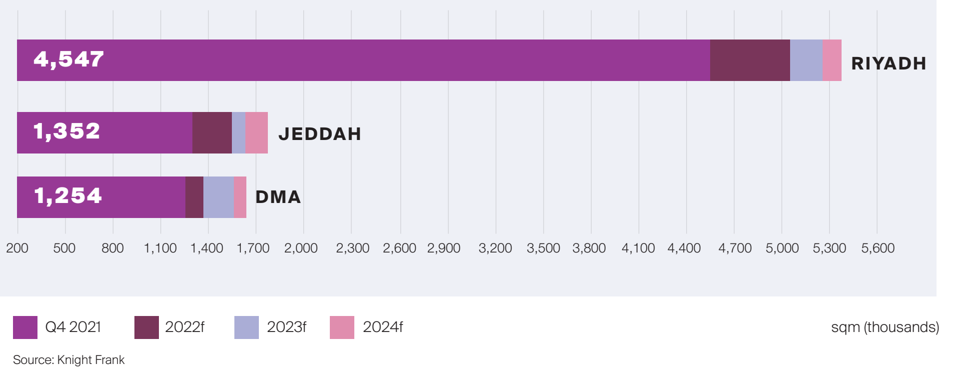
Grade A and B rental rates and YoY % change as at Q4 2021



Grade A and B vacancy as at Q4 2021



Forecast office supply



Source: Knight Frank

INSIGHT

Currency Advantage for International Occupiers

Looking ahead, as Saudi Arabia begins to implement its "Program HQ," demand from international corporations is expected to increase sharply. For international businesses, currency fluctuations may heavily influence the decision to establish a presence in the capital.

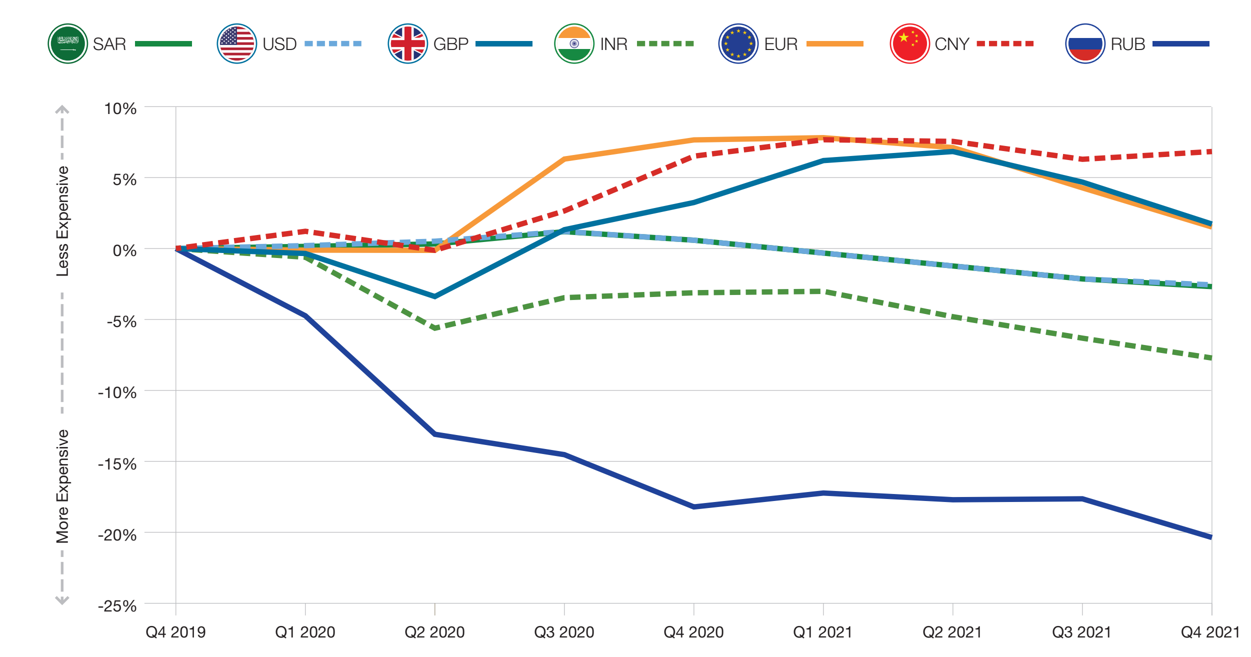
Compared to pre-pandemic exchange rates, it is now less expensive for European, British, and Chinese companies to set up a base in Riyadh, although this window appears to be closing.

For instance, Chinese companies looking to open an office in Riyadh can now expect 6.9% lower lease rates compared to pre-pandemic levels. European companies can also benefit from a 1.6% decrease in office rents per square meter, compared to pre-pandemic rates, making it an appealing time to open an office in Riyadh. Similarly, British businesses can enjoy 1.9% lower lease rates compared to pre-pandemic levels.

Indian and Russian businesses on the other hand are currently disadvantaged due to the speed of their currencies falling against the Saudi Riyal. Compared to pre-pandemic levels, it is 7.8% more expensive for Indian corporations and 20.4% more expensive for Russians to acquire office space in Riyadh.

Currency Performance Indicators

Currency Advantage available to international businesses looking to open in the Kingdom (%)



Source: Knight Frank, OANDA

Office lease rates in international currencies per sqm - against the SAR (gain/loss)

	Q4 2019 (Pre-Pandemic)	Q4 2021
British Pound	302	296 (1.9%)
Indian Rupee	27,609	29,772 (-7.8%)
Euro	351	346 (1.6%)
Chinese Renminbi	2,739	2,549 (6.9%)
Russian Ruble	24,752	29,800 (-20.4%)

RETAIL SECTOR OVERVIEW

Lease rates across super-regional, regional, and community malls have remained under pressure in all of Saudi Arabia's key markets over the last 12 months.

A significant supply of regional malls, community, and neighbourhood centres entered the market in 2021 (265,000 sqm). When coupled with continued e-commerce growth and changing consumer behaviour, spurred by the COVID-19 pandemic, landlords still face an uphill battle in attracting and retaining retailers. Retailers themselves are locked in their own battles, trying to curate retail experiences to drive footfall and profits. This was a key theme in our recently launched 2022 Saudi Report

Repeated lockdowns forced many consumers, particularly the slow digital adopters, to switch to online shopping. And this change is not limited to younger consumers. Globally, a sizable proportion of customers over 65 claim that their buying habits have permanently changed (NPD Group). Because of the increased reliance on digital touchpoints, businesses are being driven to reinvent their products and strategies to satisfy consumers' new expectations.

The nature of physical stores is expected to continue evolving rapidly, as consumers demand a more digitally centric journey.

Despite these challenges, the longer-term retail real estate forecast in Saudi Arabia is positive. Increasing urbanisation, expanding tourism, and significant growth in the Kingdom's entertainment industry is expected to increase retail spending and demand for retail premises.

Key trends

- Rising digital dependency
- Rebalancing physical retail
- Supply chain disruptions
- Profitability protection
- Emergence of omni-channels

Market Performance Indicators

Retail market lease rates as at Q4 2021

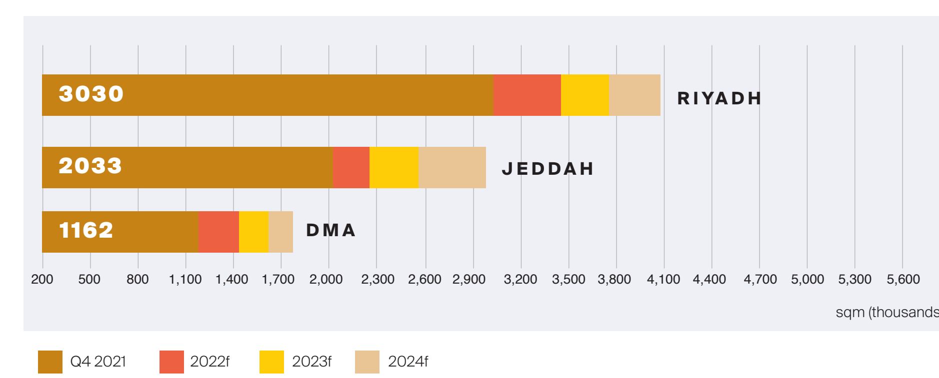
	RIYADH		JEDDAH		DMA	
	Regional/Super-Regional mall	Community mall	Regional/Super-Regional mall	Community mall	Regional/Super-Regional mall	Community mall
Rate	2,660 SAR/sqm	1,940 SAR/sqm	2,680 SAR/sqm	1,730 SAR/sqm	2,294 SAR/sqm	1,638 SAR/sqm
Y-O-Y	-1.5%	-3.0%	0.0%	-1.4%	-1.0%	-2.0%

Retail occupancy rates

	RIYADH		JEDDAH		DMA	
	Q4 2020	Q4 2021	Q4 2020	Q4 2021	Q4 2020	Q4 2021
Vacancy	17%	19%	15%	16%	11%	11%
Y-O-Y	-2 PP		-1 PP		0 PP	

Occupancy | Vacancy

Forecast retail supply



Source: Knight Frank

HOSPITALITY SECTOR OVERVIEW

The Saudi hospitality sector has continued to recover. The resumption of corporate and business travel and the successful return of Riyadh Season, which saw a record 11 million visitors, including over 1 million international tourists, has underpinned the bounce-back in Riyadh's hospitality sector.

Occupancy levels in Riyadh climbed by 18% in 2021 to 58%, while ADRs (SAR 551) and RevPAR (SAR 320) increased by 1.4% and 19.7%, respectively, over the same period.

Elsewhere, Jeddah's hospitality market continued to outperform the rest of the country. In addition to the resumption of Umrah, several events took place in Jeddah in the fourth quarter of 2021. The most notable was the Jeddah Grand Prix, held in December 2021, which attracted many local and international visitors. Indeed, Jeddah's ADRs rose by 10.9% to SAR 670 during 2021. Occupancy levels meanwhile also increased by 32% to 50.5%. At the same time, the RevPAR levels increased by 46.4% to SAR 338 over the same period.

In contrast, the hospitality sector in the Dammam Metropolitan Area (DMA) has experienced a mixed performance. Average ADRs fell slightly by 2% to SAR 417, while occupancy rates increased by 7.8% over the same period to stand at 56.8%. Unsurprisingly, the higher occupancy levels resulted in a 5.6% increase in market wide RevPAR levels.

It is evident that the events staged in Riyadh and Jeddah drew the bulk of domestic and international visitors, resulting in a lower number of visitors to DMA during the last quarter of 2021. As a result, the DMA hospitality sector didn't enjoy the same uptick in performance as seen in Jeddah and Riyadh.

Key trends

Holistic hospitality, health & well-being on the rise

Digitalised guest experiences

Safety & hygiene focus

Contactless payments

Virtual reality tours

Return of international tourists

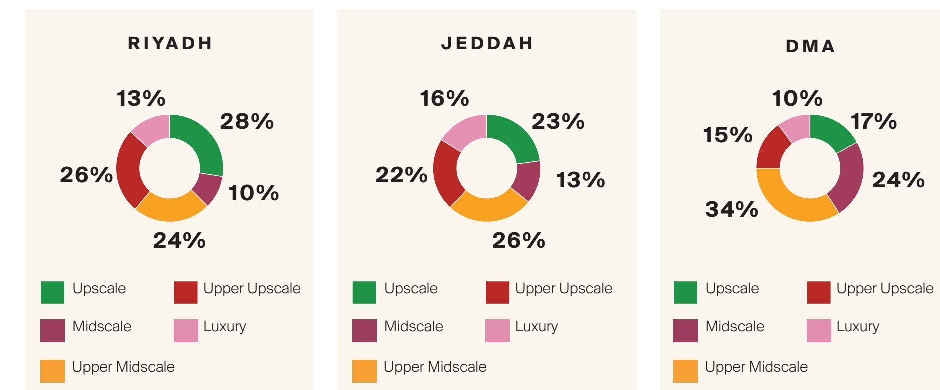
Market Performance Indicators

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

	RIYADH	JEDDAH	DMA
ADR	1.4%	10.9%	-2.0%
OCCUPANCY	18.0%	32.0%	7.8%
REVPAR	19.7%	46.4%	5.6%

Occupancy Vacancy

Existing quality hotel supply market segmentation YTD Dec 2021



Existing and upcoming quality hotel supply

	RIYADH	JEDDAH	DMA
EXISTING SUPPLY	18,554 KEYS	13,547 KEYS	11,970 KEYS
INCREASE IN SUPPLY UNTIL 2024	+30%	+46%	+24%

Source: Knight Frank, STR Global

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