A biannual review of the industrial markets in Dubai and Abu Dhabi

Dubai and Abu Dhabi Industrial Markets Review

Spring 2022

RENTAL RECOVERY CONTINUES

Average warehouse lease rates continue to recover rapidly across Dubai, with grade A rents in Al Quoz experiencing the sharpest increase both on a quarterly and annual basis. The central Dubai submarket experienced an 8.6% increase in warehouse rents between Q4 2021 and Q1 2022, pushing rents to AED 38 psf, which equates to a 15.2% increase on this time last year.

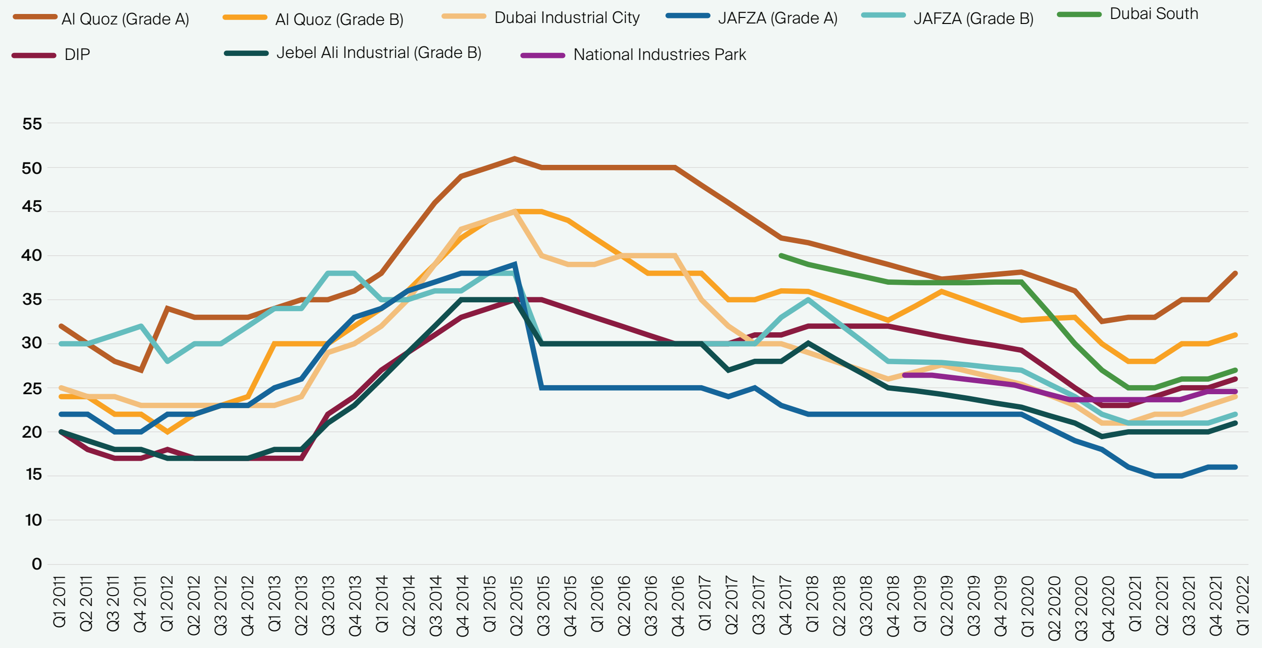
The latest gain marks the fourth consecutive increase in average lease rates and also makes Al Quoz the most expensive location to lease a warehouse in Dubai.

Interestingly, rates in Al Quoz are now just 0.4% shy of pre-pandemic levels, echoing a similar trend across other submarkets. At AED 25 psf, lease rates at National Industries Park are also within touching distance of Q1 2020 levels (AED 26 psf).

Of the nine industrial submarkets we track in Dubai, all but two have experienced rental increases so far in 2022; only Grade B rents in JAFZA (AED 16 psf) and National Industries Park (AED 25 psf) have held steady.

Elsewhere, the picture in Abu Dhabi is more stable, with rents in the six main markets we monitor remaining unchanged so far this year. Rates in Abu Dhabi Airport Free Zone (AED 550 psm) are still the most expensive in the city and Q1 2022 marks the seventh consecutive quarter rents here have been stable.

Performance of industrial rents in Dubai
AED psf



Source: Knight Frank

GOVERNMENT'S PANDEMIC RESPONSE A CATALYST FOR DEMAND

Average warehouse rental lease rates continue to recover rapidly and can in large part be attributed to the government's decisive response to the pandemic, which has in turn spurred a swift economic rebound.

The authorities' decisive response has meant that Dubai, was only placed into a lockdown once – it lasted 6-weeks. The exponential deployment of vaccines and booster doses has meant the UAE is now the world's most vaccinated nation and as a result, life has, for the most part, returned to normal. This is in stark contrast to many other developed nations.

The swift intervention of the authorities, coupled with Dubai's rapid reopening and hosting of the World Expo has catalysed economic growth. Indeed, GDP growth in 2021 at a national level is expected to have risen by 1.7%, with an even stronger rebound of 6.5% forecast for this year (Oxford Economics).

In Abu Dhabi, growth is forecast to have been sluggish last year (0.5%) due to the initial volatility in oil prices at the start of 2021, but economic expansion this year is expected to mirror Dubai at 6.3%. Dubai meanwhile is likely to see GDP growing by 6.2% this year, following a 5.2% rise last year (Oxford Economics).

The brisk reopening of Dubai's economy has spurred business confidence, which helped to lift the headline non-oil sector PMI reading for the UAE to 55.9 in November 2021, a 29-month high and this remained relatively stable at 55.6 in December.

And it is this heightened confidence amongst businesses across the country that is underpinning the resurgence in demand.

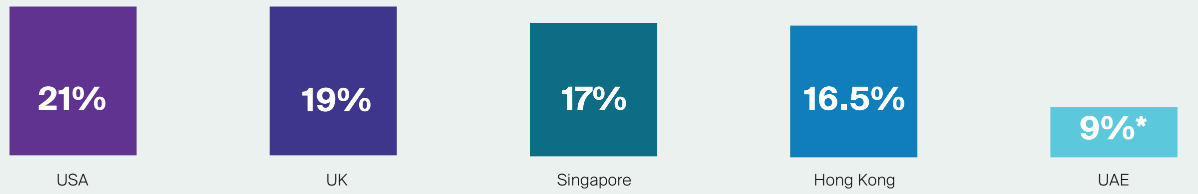
CORPORATION TAX

The recent announcement of the introduction of a Corporation Tax in the UAE from the summer of 2023 is not expected to have a negative impact on the market.

Many countries have tax treaties with the UAE to protect individuals and businesses from dual taxation. While the introduction of Corporation Tax is a first for the GCC, at 9% it is significantly lower than many major global financial centres. Furthermore, the move is part of wider OECD efforts to introduce Corporation Tax across all member states.

Separately worth noting is that businesses located in free zones across the UAE have been historically exempt from any taxation. Should they continue to remain outside any new tax regulations, their popularity is likely to rise amongst local and international businesses.

Global Corporation Tax Rates



*only for businesses with an annual income of over AED 375,000
Source: Knight Frank, various sources

CHANGE IN OWNERSHIP LAWS CONTRIBUTING TO DEMAND

Furthermore, the change in ownership laws announced as part of a raft of economic stimulus measures since the pandemic began, which also include a range of new visas, designed to attract and retain talent, have contributed to increased business confidence, activity and demand.

While the ability for international businesses to fully own and operate businesses in over 1,000 sectors outside the city's well-established free zones without an Emirati partner has not directly translated into an exodus from free zones, it has begun to attract international manufacturers not previously present in Dubai to establish a presence. The elimination of a need for an Emirati sponsor will of course be offset by the introduction of a 9% Corporation Tax from the summer of 2023.

SHIFT IN CONSUMER BEHAVIOUR ALSO DRIVING MARKET

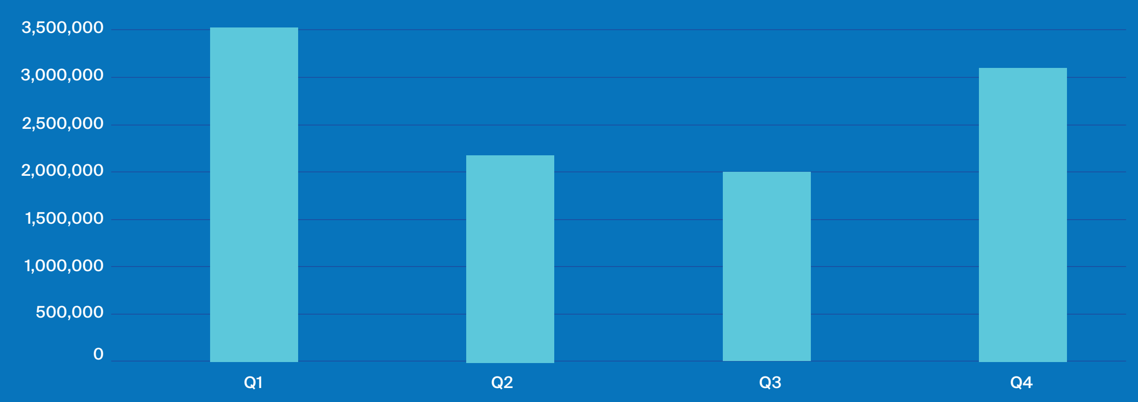
In addition, to the government's response to COVID-19, the pandemic has also driven a seemingly permanent shift in consumer shopping habits, not just in the UAE, but globally, which is fuelling demand for warehousing and distribution facilities.

Indeed, total worldwide e-commerce retail sales increased by 25.7% in 2020 to US$ 4.2 trillion and are anticipated to have increased by a further 16.8% to US$ 4.9 trillion in 2021 (eMarketer).

DEMAND IN DUBAI CLIMBS

Looking more closely at the structure of demand shows that Dubai recorded an increase in space requirements in the final three months of 2021 to almost 3.1m sq ft.
Excluding confidential requirements, the biggest contributor to the surging level of demand was the Manufacturing sector (32.1%), followed by the 3PL & Logistics sector (12.1%) and the Automotive sector (11.9%).
In Abu Dhabi too, of the 141,000 sqm of requirements in the fourth quarter of 2021, just over 50% was linked to demand from the manufacturing sector.

Industrial requirements in Dubai - 2021
sq ft



Source: Knight Frank

> **"Dubai's rapid reopening and hosting of the World Expo has catalysed business confidence and economic growth"**

THREE THEMES FOR THOUGHT

1

SOARING DEMAND FOR ‘LAST MILE’ LOGISTICS FACILITIES

As we outlined in our Summer 2021 Dubai & Abu Dhabi Industrial Markets Review, the pandemic has energised demand for centrally located, ‘last-mile’ logistics facilities, echoing a COVID-induced global trend.

Indeed during 2021, excluding confidential requirements, almost a quarter of all demand in Dubai (23.9%) was from 3PL and logistics operators, which amounted to 1.56m sq ft of space.

The challenge in the market is the severe shortage of warehouses that meet the exacting requirements of occupiers.

Warehouses with adequate height provision and loading access, for instance, are in short supply, but in very high demand.

Current high-profile occupiers on the market for this type of space include several large local and multinational e-commerce businesses.

23.9%

Share of demand from 3PL and logistics operators in Dubai during 2021

2

DEMAND BEING SUPPRESSED BY LAND LEASE STRUCTURES

Al Quoz, Umm Ramool and Ras Al Khor, all of which are well-established industrial submarkets in Dubai are yet to achieve their full potential, held back by the prevalence of short-term land lease structures in these areas.

In our experience, 12-month rolling leases often put potential occupiers off and is also preventing the emergence of a vibrant investment market in these locations.

Extending the basic lease structures would help to reinvigorate demand, drive refurbishment, enhance overall activity, secure household-name tenants and above all else, deliver an attractive investment market, particularly as demand remains high for assets with leases in excess of 1-3 years.

All three locations benefit from geographic advantages, not necessarily available in the city’s other industrial areas. Al Quoz, for instance is in central Dubai, while Umm Ramool and Ras Al Khor benefit from their proximity to Dubai International Airport.

The launch of the Al Quoz Creative Zone in April last year is a step in the right direction, and we expect this to spur landlords in the immediate vicinity to redevelop their warehouses as a result.

As an example, a land plot in Al Quoz that was developed into six warehouses was able to command a rent of AED 48 psf when used as a retail unit, compared to a lease rate of c. AED 35-40 psf, when used as a warehouse. This underscores the benefit to landlords of not only upgrading their warehousing, but also considering a change of use to retail, where possible. The dichotomy of course is further erosion of warehouse stock in a high-demand location such as Al Quoz.

3

QUALITY WAREHOUSE SHORTAGE INTENSIFYING

Most of the industrial land in the UAE is held by way of leasehold title. The main implication of the leasehold nature relates to the costs associated with owning and leasing industrial and logistic properties. For the past four to five years, land lease rates across most industrial zones have increased, while occupational rents have compressed, and investment margins have decreased.

Consequently, there has been a slowdown in new developments, especially those in areas where land rents were onerous. This has resulted in a market where most supply consists of dated LIUs and generally tired properties, with poor specifications, such as low eaves, no firefighting systems, poor access, congested location, no temperature control, no circulation areas due to overdevelopment of the plot, etc. There is a hesitancy to demolish and develop better quality assets as occupiers are still taking space in these units.
The market is changing; however, master landlords that hold land directly from the government, such as KIZAD and DI, have the upper hand in industrial and logistics development as land rents are considerably lower than the broader market, making development feasible due to healthier margins.

Newly developed properties that match international specifications are now achieving higher rents, and tenants are willing to sign longer leases, which shows a change in mindset amongst occupiers. In time this shift may lead to some facilities becoming redundant.

There is also a change in occupiers' requirements; many are looking for better quality assets and are open to paying a premium. In addition, more international occupiers are looking for larger spaces.

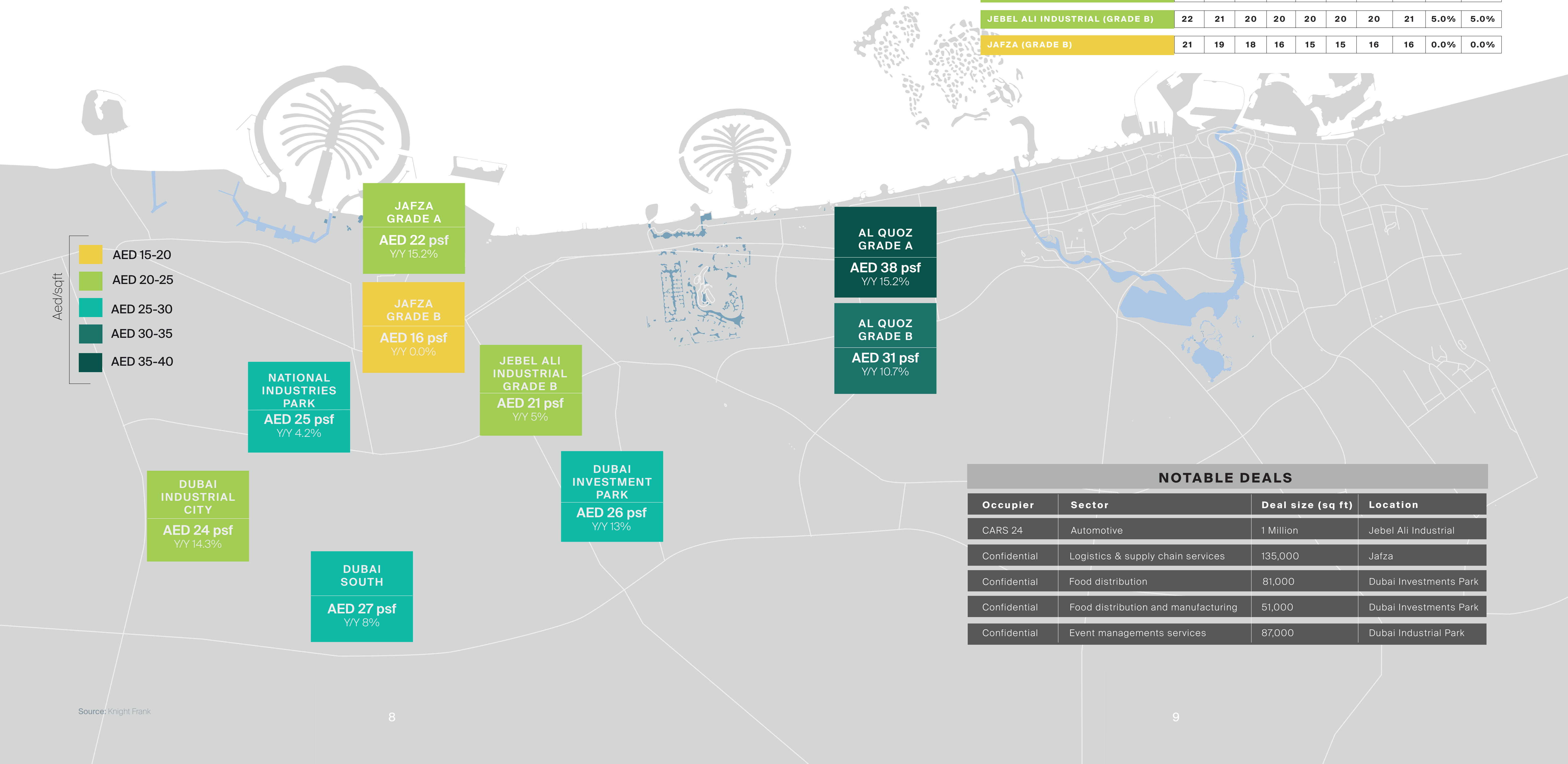
The developers/landlords who have built the best assets have maintained good occupancy and pre-lease due to this change in the market dynamic, underpinned by growth sectors, including e-commerce, dark kitchens/dark stores, data centres, last-mile delivery, vertical farms, recycling facilities, sports facilities (particularly paddle tennis) and drive through F&B (such as the Last Exit developments by Meraas).

This structural shift in the nature and type of demand now means the market, particularly in Dubai, is experiencing a severe shortage of high-quality warehousing, especially larger units in excess of 200,000 sq ft.

“There is a hesitancy to demolish and develop better quality assets as occupiers are still taking space in these units.”

DUBAI INDUSTRIAL MARKET IN NUMBERS

	Q2 2020	Q3 2020	Q4 2020	Q1 2021	Q2 2021	Q3 2021	Q4 2021	Q1 2022	Q\Q	Y/Y
AL QUOZ (GRADE A)	37	36	33	33	33	35	35	38	8.6%	15.2%
AL QUOZ (GRADE B)	33	33	30	28	28	30	30	31	3.3%	10.7%
DUBAI SOUTH	34	30	27	25	25	26	26	27	3.8%	8.0%
DIP	27	25	23	23	24	25	25	26	4.0%	13.0%
NATIONAL INDUSTRIES PARK	25	24	24	24	24	24	25	25	0.0%	4.2%
DUBAI INDUSTRIAL CITY	24	23	21	21	22	22	23	24	4.3%	14.3%
JAFZA (GRADE A)	26	24	22	21	21	21	21	22	5.0%	4.8%
JEBEL ALI INDUSTRIAL (GRADE B)	22	21	20	20	20	20	20	21	5.0%	5.0%
JAFZA (GRADE B)	21	19	18	16	15	15	16	16	0.0%	0.0%



NOTABLE DEALS

Occupier	Sector	Deal size (sq ft)	Location
CARS 24	Automotive	1 Million	Jebel Ali Industrial
Confidential	Logistics & supply chain services	135,000	Jafza
Confidential	Food distribution	81,000	Dubai Investments Park
Confidential	Food distribution and manufacturing	51,000	Dubai Investments Park
Confidential	Event managements services	87,000	Dubai Industrial Park

Source: Knight Frank

ABU DHABI INDUSTRIAL MARKET IN NUMBERS

	Q2 2020	Q3 2020	Q4 2020	Q1 2021	Q2 2021	Q3 2021	Q4 2021	Q1 2022	Q\Q	Y/Y
MUSSAFAH	291	280	250	250	250	280	300	300	0.0%	0.0%
ICAD	331	320	310	300	300	300	300	300	0.0%	0.0%
ALMARKAZ	300	300	300	300	300	300	300	300	0.0%	0.0%
KIZAD	333	333	333	333	333	333	333	333	0.0%	0.0%
ABU DHABI AIRPORT FREE ZONE	575	550	550	550	550	550	550	550	0.0%	0.0%

Aed/sqft

AED 0-300

AED 300-500

AED 500+

Source: Knight Frank

OUTLOOK

We expect the industrial and logistics market to evolve in various ways for different asset classes. Well-maintained or newly developed properties that benefit from higher specifications are expected to experience an increase in achievable rents and capital values. Conversely, more dated and properties in poorer condition and specification are likely to see rents remain stable, or at best, record marginal rent rises.

The investment appetite for the sector is high; however, the majority of properties are leased on short terms (1-3 years), which doesn't match the requirements of most institutional investors. We are now seeing this trend change, and many local and international occupiers are happy to sign longer leases with no breaks. This is being achieved through the use of incentives such as extended rent-free periods. If this trend continues, we can expect a compression of yields in the industrial and logistics sector, which could slip to c.8%, from about 8.75% currently.

Central industrial areas such as Al Quoz in Dubai and Mussaffah in Abu Dhabi may face significant changes in land uses, moving away from the industrial sector to more commercial/retail warehousing. The redevelopment in central industrial areas may also be driven by the unprecedented demand from occupiers with new business models, such as dark kitchens, entertainment and sports facilities, and fulfilment centres. Stringent requirements of local authorities with respect to development quality and specification of the newly developed warehousing stock will likely widen the gap in rents between new and older supply. We also expect local authorities to introduce certain restrictions, such as limitations on permitted activities for properties that don't match minimum fire-fighting requirements, or civil defence systems, for instance.

Over the longer term, it is our expectation that most industrial and logistics businesses will be relocated to out-of-town industrial zones. We expect that the newly developed stock, built to international specifications, in conjunction with various government initiatives targeted towards improving the sector will eventually lead to more international firms moving to the UAE, further eroding the available supply.

> **"The market is experiencing unprecedented demand for dark kitchens and 'last-mile' logistics facilities"**

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2021 INDUSTRY NEWS HIGHLIGHTS

Al Quoz Creative Zone opens

New district launched in April 2021 for artists and designers to live and work in the industrial submarket of Al Quoz.
The launch coincided with the launch of Dubai's Creative Economy Strategy, which aims to double the number of creative companies in the city to 15,000 in the next five-years, while doubling the creative workforce to 70,000 over the same period. The goal is to grow the creative industries' contribution to GDP to 5% by 2025, from c. 2.5% today.

Source: Gulf Business

Dubai CommerCity launches

Spread across 2.1 million sq ft, the first e-commerce free zone in the Middle East, Africa, and South Asia region opened in April 2021 in Dubai's Umm Ramool.
The AED 3.2 billion development's first phase includes 320,000 sq ft of offices and 145,000 sq ft of logistics units. The warehouses will be managed by DHL and Hellman Worldwide Logistics.
The government estimates that the UAE has the second fastest growing e-commerce market in the GCC and has the fifth largest e-commerce sales market in the Middle East, Africa and South Asia, estimated to be worth US$ 4 billion.

Source: Government of Dubai

WenChao Group plans Dubai food hub

WenChao Group announced plans to invest US$ 200 million to build a new 950,000 sq ft food manufacturing and distribution facility in Dubai Industrial City. The first phase of WenChao Logistics Hub is scheduled to open in H1 2022.

Source: ZAWYA

France's CMA CGM Group plans terminal at Khalifa Port

In September last year, France's CMA CGM Group signed a joint venture with Abu Dhabi Ports to establish a new terminal at Khalifa Port.
The project, which is expected to open in 2024, will see investments of US$ 154 million and will have an initial capacity of 1.8 million TEU's. The development will also see the development of 700,000 sqm of terminal yard space, 1,200m of quay walls and a 3,800m breakwater.

Source: The National

Region's first tyre hub to open in KIZAD

At the end of last year, KIZAD signed an agreement with China's Shandong Port Group to create the Middle East's first tyre storage and distribution facility in Khalifa Industrial Zone Abu Dhabi (KIZAD).
The agreement also coincides with a the signing of a 'sister-ports' agreement, aimed at boosting cross border trade between the two ports of KIZAD and Shandong.

Source: AD Ports Group

Al Barakah Dates expands

Dubai-based Al Barakah Dates announced plans to double its date production facility at Dubai Industrial City early last year.
The plan is to boost its production capacity to 100,000 tonnes annually, representing almost 50% of the UAE's annual date harvest and making it the single largest facility to process dates globally.
The new factory will cover an area of 600,000 sq ft and will allow the facility to ship 7,000 shipping containers worth of dates every year.

Source: Government of Dubai

CONTACTS

Andrew Love
Partner
Head of ME Capital Markets and OSCA
+971 50 7779 595
Andrew.Love@me.knightfrank.com

Adam Wynne, MRICS
Associate Partner
Co-Head of Industrial and Logistics UAE
+971 56 4741 921
Adam.Wynne@me.knightfrank.com

Maxim Talmatchi, MRICS
Manager
Co-Head of Industrial & Logistics UAE
+971 50 5169 965
Maxim.Talmatchi@me.knightfrank.com

Mikhail Vereshchagin
Commercial Agent
Industrial & Logistics
+971 56 454 2978
Mikhail.Vereshchagin@me.knightfrank.com

Dumitru Mamaliga
Surveyor
Industrial & Logistics
+971 50 8189 846
Dumitru.Mamaliga@me.knightfrank.com

Faisal Durrani
Partner
Head of Middle East Research
+971 4 4267 698
Faisal.Durrani@me.knightfrank.com

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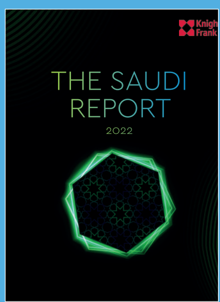

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Knight Frank, 1st floor, Building WH01, Al Raidah Digital City, Riyadh, Kingdom of Saudi Arabia

Knight Frank, 9th floor, Jameel Square, Prince Mohammad Bin Abdulaziz Street, Jeddah, Kingdom of Saudi Arabia

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