Investment Strategy & Research

GCC Real Estate Update Dec-2023

Slim pickings & selective focus in 2024

Report Highlights:

This report analyzes GCC real estate fundamentals in 2023. We analyze demand-supply drivers and examine trends in transactions, prices and rents that drive our 2024 outlook for real estate in the region.

Segments covered in the report include:

- *Residential RE*
- *Commercial Office RE*
- *Retail RE*
- *Industrial RE*
- *GCC RE Equities*

Opportunities basket thinner in 2024: Real Estate supply in most segments could quickly get sensitive to market-wide headwinds in 2024, but frontline developers with strong liquidity should be able to calibrate swiftly to bring the right product types to the market. We expect residential developers in Dubai & Riyadh with dominant brand equity, an attractive product mix, and market sensitive payment plans to achieve sell-through of its new launches build-to-sell (BTS) portfolio going forward in Dubai & Riyadh. Separately, office markets in Riyadh and Dubai are expected to remain strong as they compete for their market share of regional headquarters (RHQ) and new Grade-A office space supply from developers remains limited. For retail, best-in-class super regional malls and community-linked malls in key markets should witness strength in typical late-cycle trends, as they should continue to achieve higher occupancy rates and should mitigate tenant portfolio risks adequately. In the industrial warehouse market, specialized warehouses will remain in demand and in short supply in 2024. These spaces should witness stable yields of +8% as owners push up rents, thereby contributing to a widening rental gap for lower quality spaces.

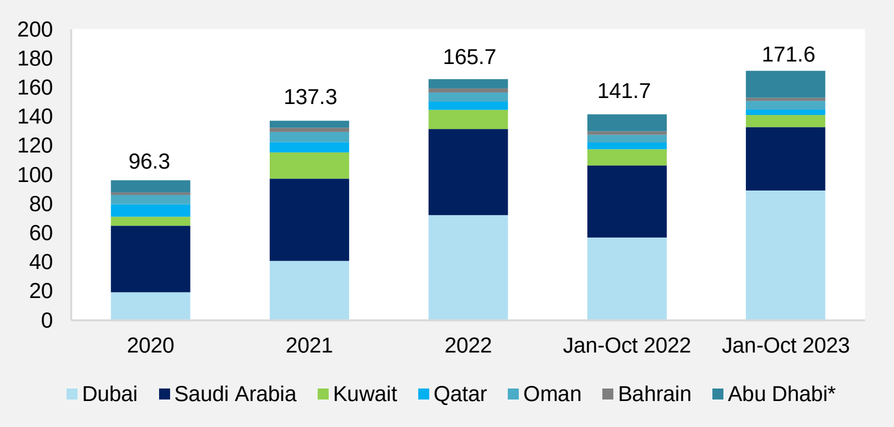
UAE carries GCC RE transacted value over Jan-Oct 2023 beyond full year 2022 estimate: Real estate sale transactions in the GCC over Jan-Oct 2023 reached USD 171.6 Bn and surpassed the full year estimate for 2022 of USD 165.8Bn. Dubai RE transactions contributed 52.1% of the region's total transacted value and was able to offset the decline of the other key markets such as Saudi, Qatar and Kuwait. The average value per transaction achieved over Jan-Oct 2023 for GCC real estate was up by 22.1% y-o-y, as investors continued to see value for market leading real estate products despite the strong pricing demanded by developers. Further, we believe that strong late-cycle pricing outperformance will continue for unique superior-quality assets in GCC's real estate sub-segments in 2024, but this growth is expected to materialize only in specific markets as investors become selective and watch overall economic activity and interest rates. Going forward, we expect a slower pace of price increases across key residential markets in 2024, as typical late-cycle stabilization is witnessed, and supply calibrates to more normalized demand.

Leading developer equities to outperform in 2024: The Refinitiv GCC Real Estate Total Return Index gained by 19.2% outperformed the MSCI GCC index (-2.4%) over the first eleven months of the year, driven by strong performances from Dubai (+32.9%) and Abu Dhabi (+29.0%) and Saudi Arabia's RE Management & Development (+21.4%) indices. The outperformance of the UAE and Saudi RE Management & Development indices is largely restricted to sector leading developers with strong pricing power and pipelines who continue to witness robust demand and sell-through of their projects. In 2024, we expect the rally to continue for select developer names and prefer them over REITs and income generators as strong liquidity on their balance sheets would enable them to maintain market share and achieve higher IRR projects and opportunistic cross-border M&A activity.

Access previous reports:

- *Pockets of late-cycle opportunities remain – July 2023*
- *Late-cycle disparities emerge – Dec 2022*
- *Divergent cap rate narratives in 2022 – Mar 2022*
- *Pinning hopes on a 'Resi'lient recovery - Aug 2021*
- *Cyclical or Structural Conundrum – Dec 2020*
- *Déjà vu or Different this time? – May 2020*

GCC RE Transactions Breakdown – USD Bn



*Source: Kamco Invest Research, Govt Sources, DXB Interact, *9M-2023 only available*

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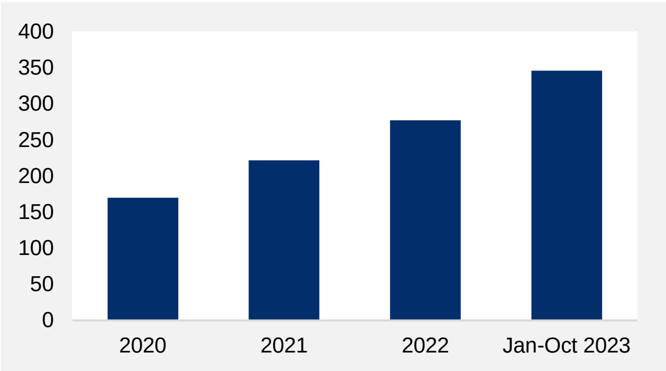
Investment Strategy & Research

UAE carries GCC RE transactions in 2023

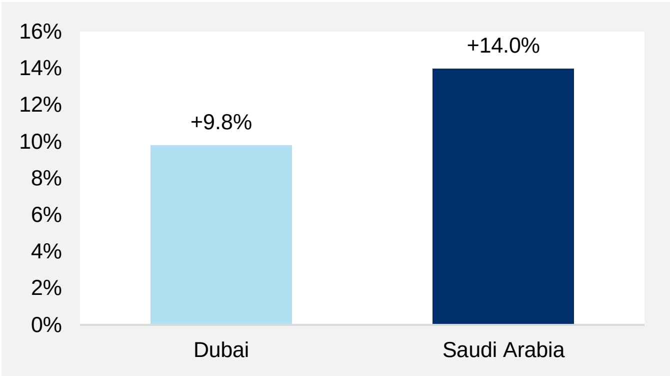
Real estate sale transactions in the GCC over Jan-Oct 2023 reached USD 171.6 Bn, up 21.1% y-o-y from USD 141.7 Bn over the same period in 2022, based on our analysis of available official estimates. Dubai's transactions contributed 52.1% of the region's total transacted value and was able to offset the decline of the other key markets such as Saudi, Qatar and Kuwait. RE value transacted in Dubai increased almost 57% y-o-y over Jan- Oct 2023 based on data from DXB Interact, mainly driven by strong pricing for leading developers and off-plan demand of luxury properties and single-family, multi-family homes of above AED 5 Mn. While data for Abu Dhabi was only available until 9M-2023, transacted value of Abu Dhabi real estate also reportedly jumped by 56% over 9M-2023. Both UAE markets pushed the aggregate value transacted in the GCC over Jan-Oct 2023 beyond the full year estimate for 2022 of USD 165.8Bn. The number of transactions in the GCC however remained broadly stable y-o-y (-0.8%) over the first ten months of 2023 and reached 495,872 deals, despite a jump of over 43% and 36% witnessed in Dubai & Abu Dhabi's RE transactions.

GCC average value per transaction



Sources: DLD, Kamco Invest Research

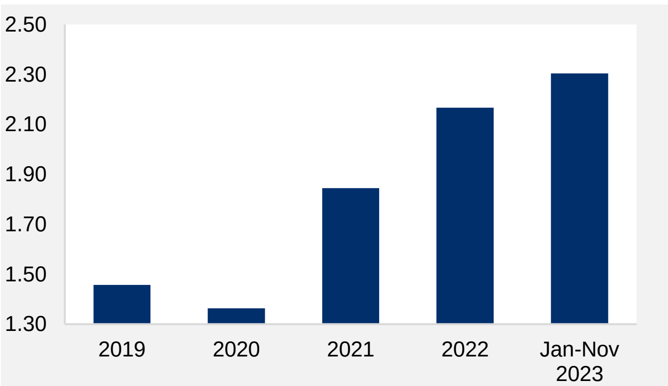
Average value per transaction y-o-y over Jan-Oct 2023



Sources: MOJ, Kamco Invest Research

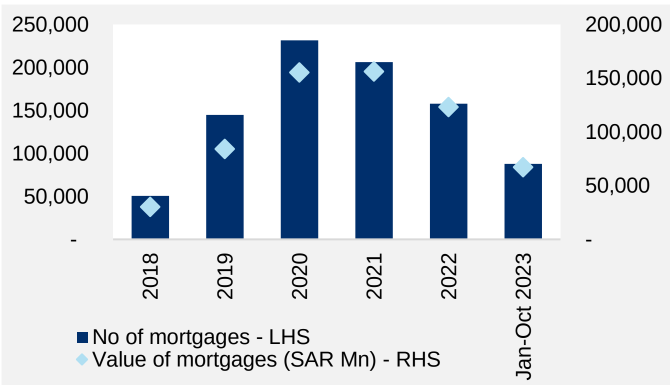
Nevertheless, the average value per transaction achieved over Jan-Oct 2023 for GCC real estate was up by 22.1% y-o-y, as investors continued to see value for market leading real estate products despite the strong pricing demanded by developers. In Dubai, off-plan transactions continued their strong momentum with off-plan volumes jumping by over 40% over Jan-Nov 2023 when compared to full year 2022 estimates, while registering a healthy 9.8% increase in average off-plan value per transaction from end -2022.

Dubai off-plan value per transaction average (AED Mn)



Sources: DXB Interact, Kamco Invest Research

Total Saudi residential new mortgages from banks & finance companies



Sources: SAMA, Kamco Invest Research

Separately in Saudi Arabia, mortgage activity continued to trend downwards over Jan-Oct 2023 due to higher mortgage rates and higher pricing of residential products. Going forward, we expect a slower pace of price increases across key residential markets in 2024, as typical late-cycle stabilization is witnessed, and supply calibrates to more normalized demand. Mortgage rates and rental affordability should impact end user ownership trends especially in markets such as UAE & Saudi Arabia and determine the future course of residential transaction activity, in our view.

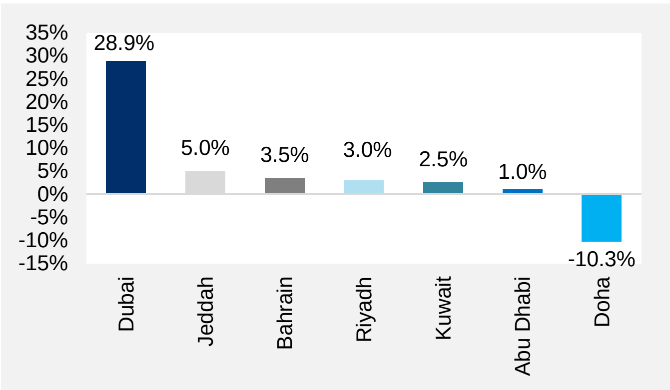
Selective focus from investors to combine with slim pickings in 2024

Real Estate supply in most segments could quickly get sensitive to market wide headwinds in 2024, but frontline developers with strong liquidity should be able to calibrate swiftly to bring the right product types to the market. Further, we believe that strong late-cycle pricing outperformance will continue for unique superior-quality assets in GCC's real estate sub-segments in 2024, but this growth is expected to materialize only in specific markets as investors become selective and watch overall economic activity and interest rates. Moreover, ESG considerations are expected to become a more integral part of commercial supply in terms of design elements and ratings such as LEED, BREEAM and occupier demand. We believe residential developers in Dubai & Riyadh who possess dominant brand equity, an attractive product mix, and market sensitive payment plans can achieve sell-through of its new launches build-to-sell (BTS) portfolio going forward. Separately, office markets in Riyadh and Dubai are expected to remain strong as they compete for their market share of regional headquarters (RHQ) and new Grade-A office space supply from developers remains limited. For retail, best-in-class super regional malls and community linked malls in key markets should witness strength in typical late-cycle trends, as they should continue to achieve higher occupancy rates and should mitigate tenant portfolio risks adequately. In the industrial warehouse market, specialized warehouse spaces will remain in demand and in short supply in 2024, pushing up rents for such spaces and widening the rental gap with lower quality spaces.

Residential RE prices price growth to moderate, yields to stabilize in 2024

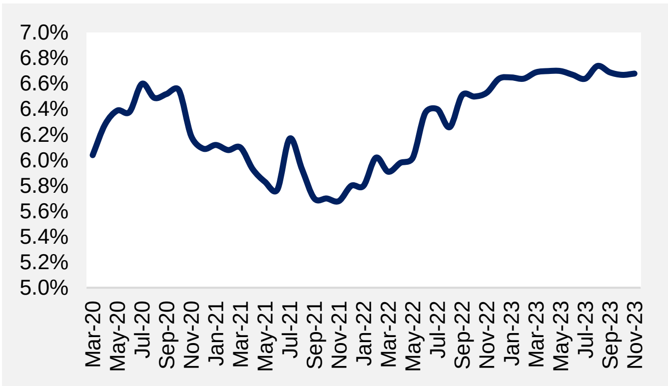
Growth in residential real estate prices in key markets continued into Q3-2023, driven by investment demand and slower completion of the supply pipeline. In Dubai, prices rose 18.4% by Nov-2023 y-o-y as per ValuStrat, driven mainly by higher demand for single-family homes and luxury villas, while incremental supply for those products continues to be limited as compared to supply. As a result, villas reportedly witnessed price gains of 23.3% y-o-y, while apartment price gained by 14.1% as on Nov-2023, according to data from ValuStrat. Developers in Dubai continue to monetize improved specifications and continue to tweak post-completion plans of their new launches to keep price momentum going. In Abu Dhabi, residential price growth was muted at 3% y-o-y at the end of Q3-2023 as per JLL, as demand was reportedly strong for new developments, especially within the investment zones, with a particular emphasis on townhouse and villa projects. In Riyadh sales prices gained by 7% y-o-y at the end of Q3-2023 as per JLL, as Riyadh regional business hub ambitions led to an increased demand for residential units. Jeddah also witnessed a similar price growth of 7% y-o-y, as per JLL. Nevertheless, rising prices and interest rates are increasing affordability concerns in Saudi residential markets and contributing to a decrease in sales activity as per consultants.

Residential rents performance: Q3-2023 (y-o-y%)



Source: Kamco Invest Research, ValuStrat, REMI, JLL

Dubai apartment yields performance



Source: Property Monitor, Kamco Invest Research

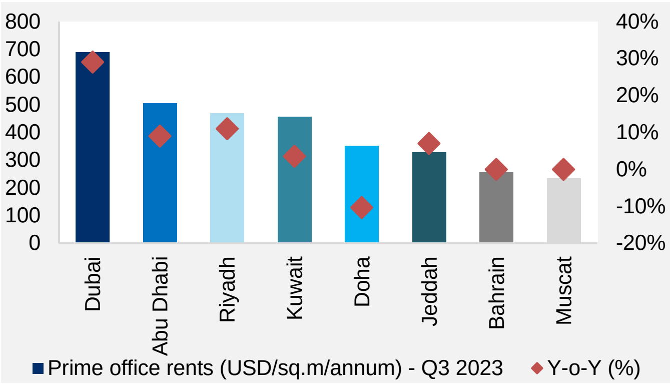
In terms of rents, Dubai reportedly witnessed a 28.9% y-o-y jump in average residential rents as per ValuStrat, as investors continued to raise rents to maintain gross yields which are around 6.5%. Other rental markets such as Riyadh (+3%), Kuwait (+2.5%) and Abu Dhabi (+1%) also witnessed marginal increases y-o-y, based on trends from JLL, ValuStrat and REMI respectively. In 2024, we expect the pace of price and rental growth across key markets to moderate barring unique market-leading residential projects from developers who possess strong brand equity and pricing power. For the broader market, we expect typical late-cycle stabilization to be witnessed and as supply calibrates to more normalized demand, while investors and end users should remain cautious about higher interest rates and affordability.

We believe residential developers in Dubai & Riyadh who possess dominant brand equity, an attractive product mix, and market sensitive payment plans can achieve sell-through of its new launches build-to-sell (BTS) portfolio going forward. Having said that aggregate supply and launches in most residential markets could quickly get sensitive to market wide headwinds in 2024, but frontline developers with strong liquidity should be able to calibrate swiftly to bring the right product types and volumes to the market. Mortgage rates and rental affordability should impact end user ownership trends especially in markets such as UAE & Saudi Arabia and determine the future course of residential transaction activity, in our view. Nevertheless, over the long term national programs should such as Saudi Arabia's Vision 2030's vision of increasing homeownership from 60.6% in 2022 to 70% by 2030, and the strategic roadmaps set through initiatives such as the Dubai 2040 Urban Master Plan and D33 agenda should increase demand for residential developments.

RHQ markets remain hot on limited supply

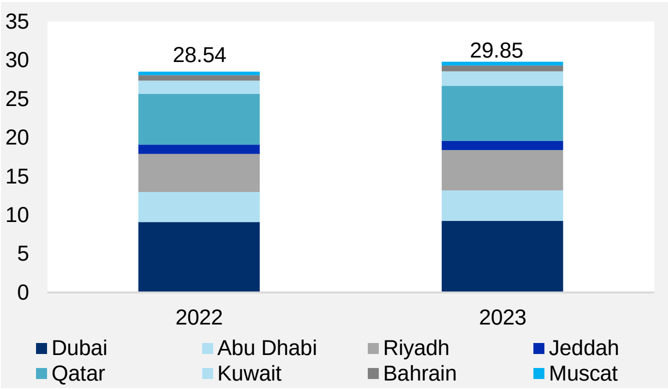
Prime office spaces in Dubai (+29%) and Riyadh (+11%) witnessed significant rental increases as demand continued for superior quality office premises, and as certain industries continued to expand their footprint in these markets. Both markets also represent aspirations of becoming the regional headquarters for corporates. Saudi Arabia launched the regional headquarters program (RHQ Program) and announced tax incentives for foreign companies that locate their regional headquarters in the kingdom, including a 30-year exemption for corporate income tax. In Dubai, Asteco reported that there was increased demand, strong rents and waiting lists for well-managed and superior fully fitted office spaces from companies looking to expand their existing footprint.

GCC prime office rents & y-o-y declines: Q3-2023



Source: Kamco Invest Research, Asteco JLL, Savills, REMI, ValuStrat

GCC key office markets office supply (Mn sq.m)



Source: JLL, ValuStrat, REMI, Savills, Kamco Invest Research

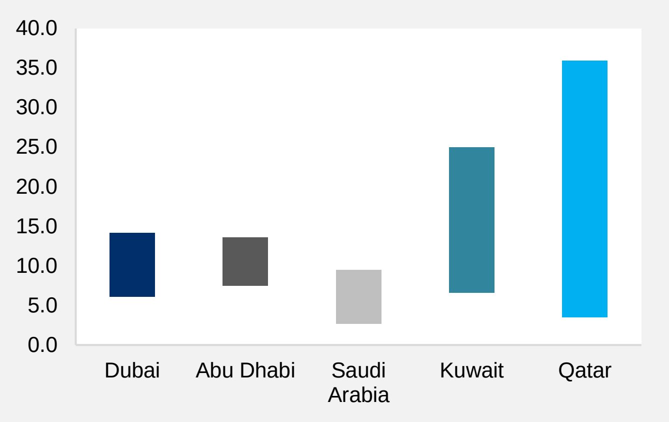
Office space developers in the region continue to hold supply tight due to the time-lag between conceptualization of design and completion due to potential risks of supply entering weak economic conditions. Aggregate office space in GCC's key markets is expected to reach 29.85 Mn sq.m by the end of 2023, from 28.54 Mn sq.m in 2022, based on our analysis of consultant data. As a result of the lower supply of quality spaces, prime office spaces in Abu Dhabi (+9%), Jeddah (+11%) and Kuwait (+3.5%) also witnessed gains in rents y-o-y at the end of Q3-2023. BFSI (banking, financial services and insurance) and O&G (oil & gas) and newer sources of demand such as TMT (Technology, Media & Telecom) remain primary drivers of additional take-up of quality spaces. BFSI re-established itself as the key sector driving office space demand within key office markets such Riyadh, Dubai, and Abu Dhabi in 2023, while we expect TMT, AI, Robotics, Healthcare/Pharm and Legal corporates to remain active occupiers, on a continuation of a trend which emerged since 2020. Moreover, certain multi-national corporates will continue to prefer sustainable and energy-efficient office spaces that are LEED certified, with allocation towards wellness components and better infrastructure connectivity.

Suitability still underserved in industrial warehouses

Quality and specialized industrial warehouse spaces remained in demand throughout the GCC and in short supply. Rents for such spaces moved higher, widening the rental gap with lower quality spaces, while underserved markets such as Riyadh witnessed YTD rental gains of +30% at the end of Q3-2023 as per CBRE. Demand for warehouses with international specifications remains strong, and owners who can retrofit older assets are able to command a premium, based on consultant data across the GCC.

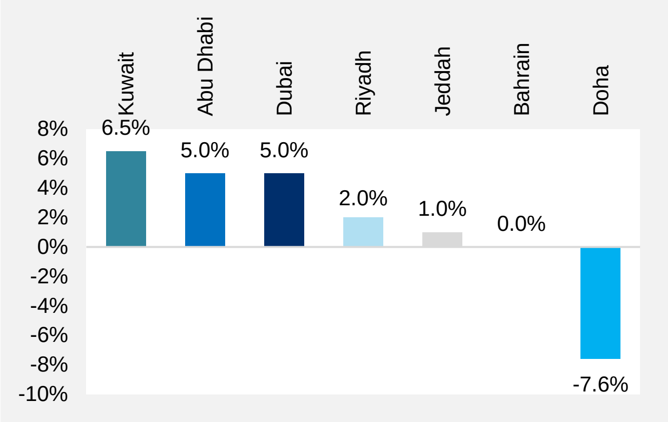
Saudi Arabia introduced the Logisti platform - a transport and logistics initiative under the National Industrial Development and Logistics Program (NIDLP) that targets to provide 59 logistics centers of over 100 Mn sq.m across Saudi Arabia by 2030. Vacancy rates in Riyadh and Jeddah have reportedly reached low single digit percentages. Demand continues from ecommerce, as Modon has signed a deal to build 14 new high-tech warehouses that will be operated based on a public-private sector partnership model. In the UAE, industrial warehouse activity reportedly remained relatively subdued, due to the lack of available stock, as per CBRE. They mentioned that this resulted in a market, where tenants are pushed to comply with landlords' terms with lower incentives. Knight Frank mentioned that international funds and investors were drawn towards the 8.50-8.75% yield in H1-2023 and estimate demand to compress yields by 50bps by the end of 2023. They further expect the yield compression to potentially lower investor demand for industrial assets going forward if interest rates remain high causing yield compression to slow or even reverse.

GCC industrial warehouse rents (USD/sq.m/month)



Source: CBRE, Knight Frank, Valustrat, REMI, Kamco Invest Research

GCC retail space rents: Q3 2023 (y-o-y%)



*Source: JLL, Valustrat, REMI, Kamco Invest Research, * Kuwait and Bahrain are as of Dec - 2023*

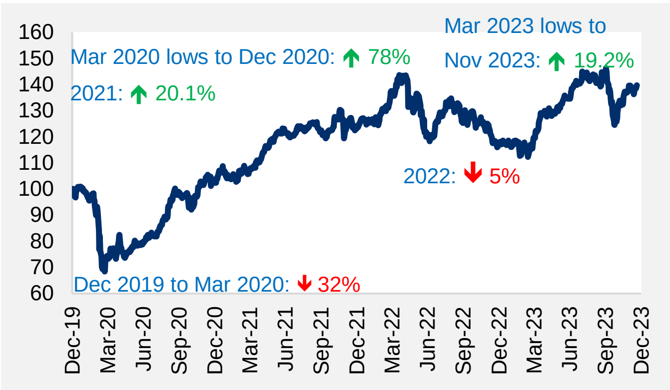
Super-regional malls comeback strong in 2023

All retail real estate markets in the GCC barring Doha (ValuStrat:-7.6%) witnessed rental growth y-o-y at the end of Q3-2023, as per consultant data. Kuwait's retail malls witnessed rental growth of 6%-7% y-o-y by Dec-2023 as per REMI, while JLL mentioned that UAE retail mall owners continued to optimize their spaces to attract footfall and tenant demand which has pushed rents higher by 5% y-o-y in Dubai and Abu Dhabi. Mall space owners across markets continue their focus on increasing their Family Entertainment (FEC) footprint to attract footfalls. On the demand side retailers are constantly evaluating their mall space expansion plans and the potential impact from increasing omnichannel strategies such Click & Collect, and influencer-driven marketing campaigns to maintain profitability and market share. Nevertheless, we believe that brick-and-mortar retail has established its place in the overall retail market in 2023, and the risk of retail ecommerce largely pinning hopes of achieving continuous market share gains has clearly stabilized. Further, mall space owners of best-in-class super regional malls and community-linked retail spaces should keep natural vacancy rates of 4%-5% and witness rental growth as retail returns as late-cycle favorites. In such landmark mall spaces, retailers would continue to look for more strategic locations for their outlets and will be willing to pay a premium for better visibility. Mall owners of such spaces should be able to mitigate tenant portfolio risks by monitoring KPIs such as footfalls, tenant sales and occupancy cost ratios (OCRs), that should be enable them to achieve contract renewals or tenant rollover at favorable rental rates. In markets such as Dubai, mall operators have reportedly been able to repurpose spaces that witness lower footfall into vibrant service hubs that offer a range of amenities such as clinics and gyms.

Developer RE equities to end 2023 as outperformers

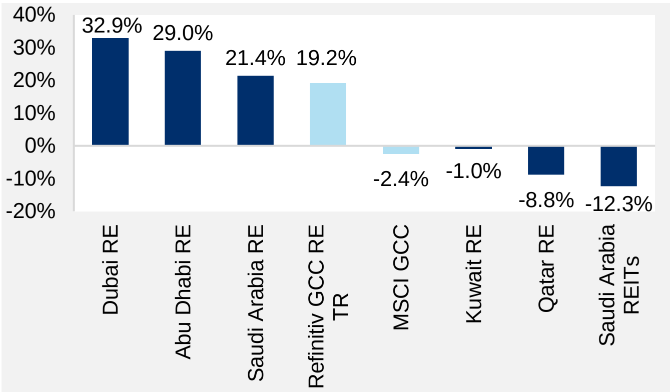
Real estate equity indices in the UAE and Saudi Arabia's RE Management & Development index continued their outperformance and witnessed strong gains over Jan-Nov 2023. The Refinitiv GCC Real Estate Total Return Index gained by 19.2% outperformed the MSCI GCC index (-2.4%) over the first eleven months of the year, driven by strong performances from Dubai (+32.9%) and Abu Dhabi (+29.0%) and Saudi Arabia's RE Management & Development (+21.4%) indices. The Saudi REITs index (-12.3%) and Qatar (-8.8%) were major decliners in the regional real estate listed space.

Refinitiv GCC Real Estate Total Return Index (Rebased) – Jan-Nov 2023



Sources: Kamco Invest Research, Refinitiv

GCC RE equity indices: Jan-Nov 2023 returns (%)



Sources: Kamco Invest Research, Bloomberg, Refinitiv

The outperformance of the UAE and Saudi RE Management & Development index is largely restricted to developers who are sector leaders with strong pricing growth and pipelines, who continue to witness robust demand and sell-through of their projects. In 2024, we expect the rally to continue for select developer names and prefer them over REITs and income generators as strong liquidity on their balance sheets would enable them to maintain market share and achieve higher IRR projects and opportunistic cross-border M&A activity. Further, share price sensitivity to potential interest rate cuts and fluctuation of occupancy rates could potentially impact secondary income generating properties more in our view.

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