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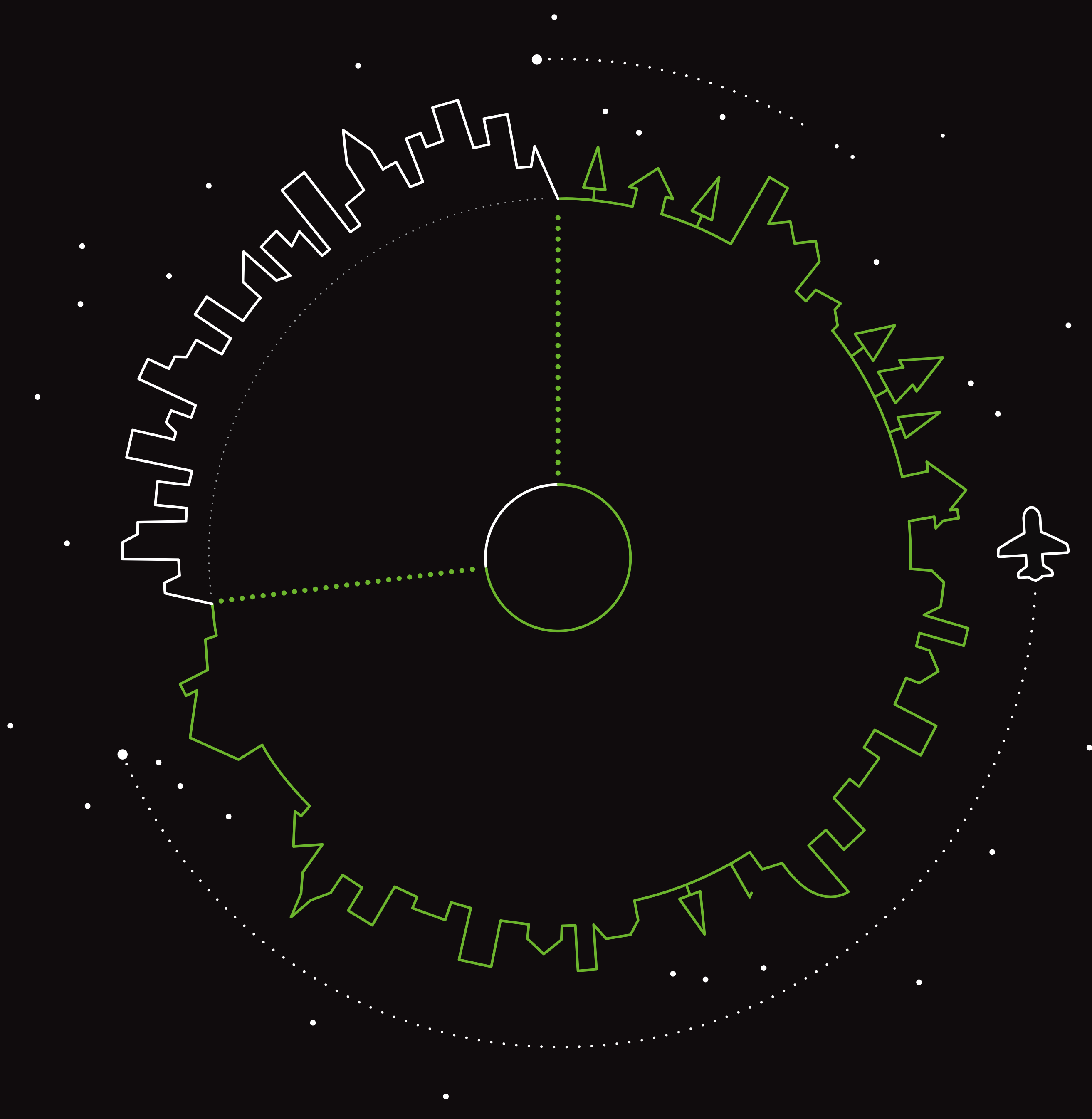

Middle East Real Estate Predictions: Dubai

2018

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A summary of 2017 performance

Dubai's hospitality market

A strong Dirham and slow source market growth have contributed to another challenging year in 2017, but fundamentals are strong and opportunities remain.

A summary of 2017 performance

2017 was another challenging year for Dubai's hospitality market, with slower growth from key source markets compounded by a strong local currency, making Dubai a relatively more expensive destination for many visitors.

Despite the above, tourism demand in Dubai is strong overall. Dubai remains top of the 2017 MasterCard Global Destination Cities Index in terms of visitor spending and has retained its global number four spot in terms of the total number of international overnight visitors.

Increasing supply and competition between operators has pushed down both Average Daily Rates (ADR) and Occupancy, which in turn has led to a market-wide fall in average Revenue Per Available Room (RevPAR) of 6.2% between Q3 2016 and Q3 2017.

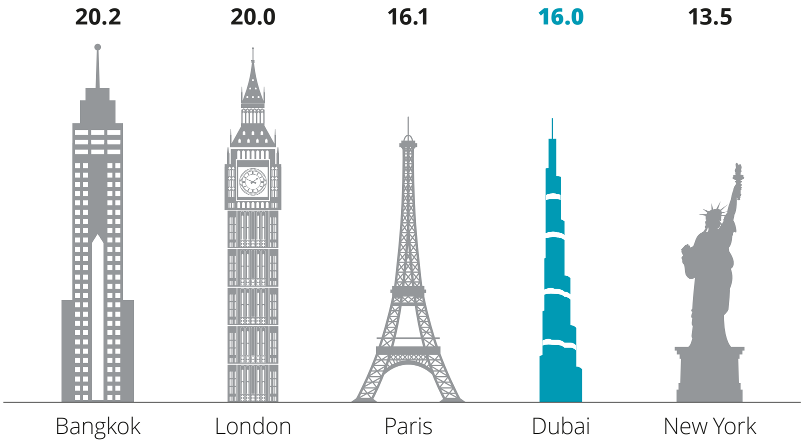
The Luxury, Upper Upscale, Upscale and Upper Midscale segments all experienced a decline in occupancy of between 0.6% and 6.3% between Q3 2016 and Q3 2017.

Over the same period, there was increased occupancy in the Midscale and Economy sectors, from 78% to 82%, an indicator of sustained demand for affordable product across Dubai's hospitality market.

International overnight visitors

Global top five destinations 2017

Visitors (million)

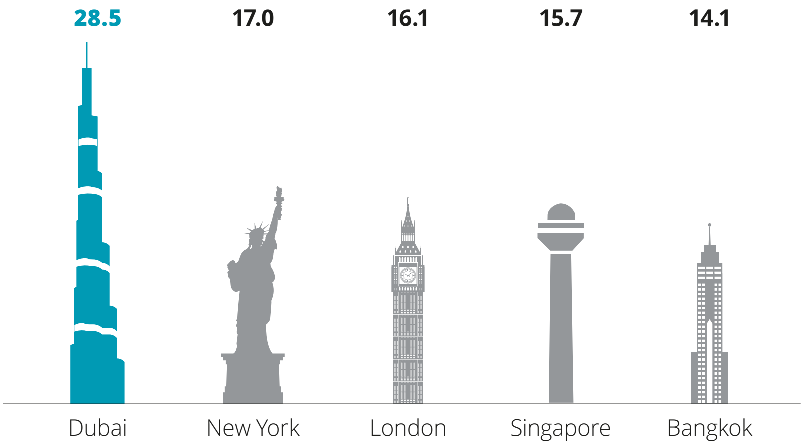


Source: 2017 MasterCard Global Destination Cities Index

International overnight visitor spending

Global top five destinations 2016

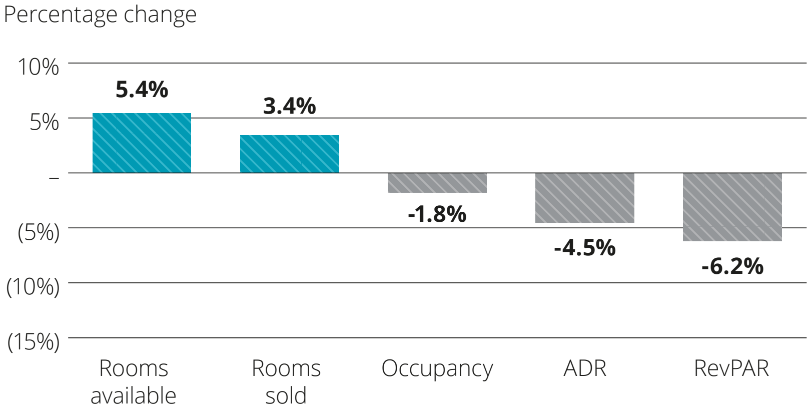
Visitor spend (US$ billion)



Source: 2017 MasterCard Global Destination Cities Index

Dubai hotel performance percentage change

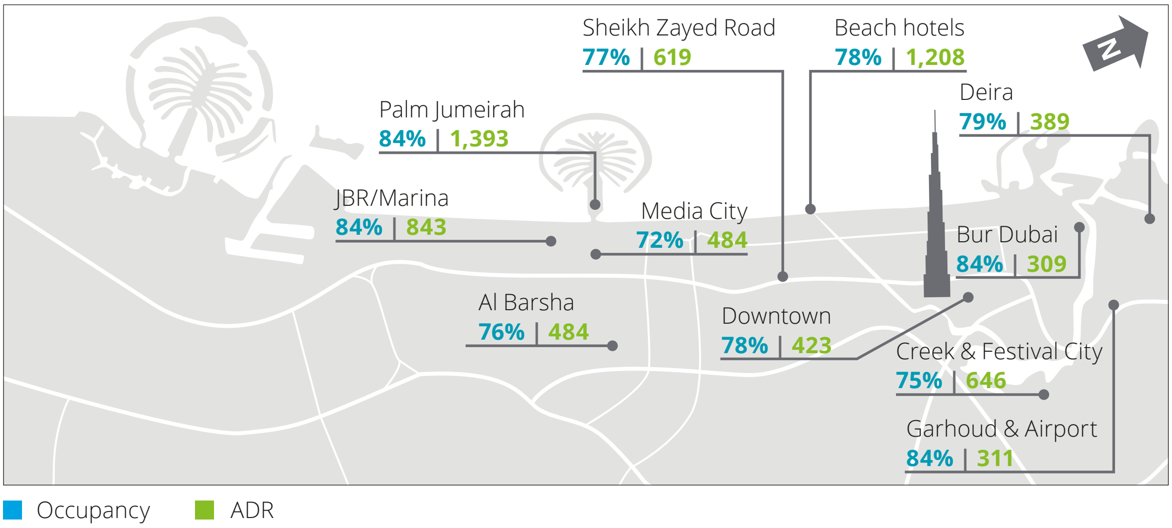
Q3 2016 versus Q3 2017



Source: STR Global

Dubai hotel performance

Year to Date (YTD) Q3 2017



Source: Deloitte, Google Earth

Note: Locations are illustrative

Classification	Luxury	Upper Upscale	Upscale	Upper Midscale	Midscale & Economy
2016 YTD Q3 Occupancy	73.1%	77.8%	77.5%	84.9%	78.4%
Trend	↓	↓	↓	↓	↑
2017 YTD Q3 Occupancy	71.0%	75.3%	76.9%	78.6%	81.8%

Source: STR Global

Note: % refers to average YTD hotel occupancy across all hotels surveyed by STR Global in each submarket

Dubai's residential market

Declining sales prices and rents continued in 2017, whilst new residential supply continued to focus largely on the affordable segment.

A summary of 2017 performance

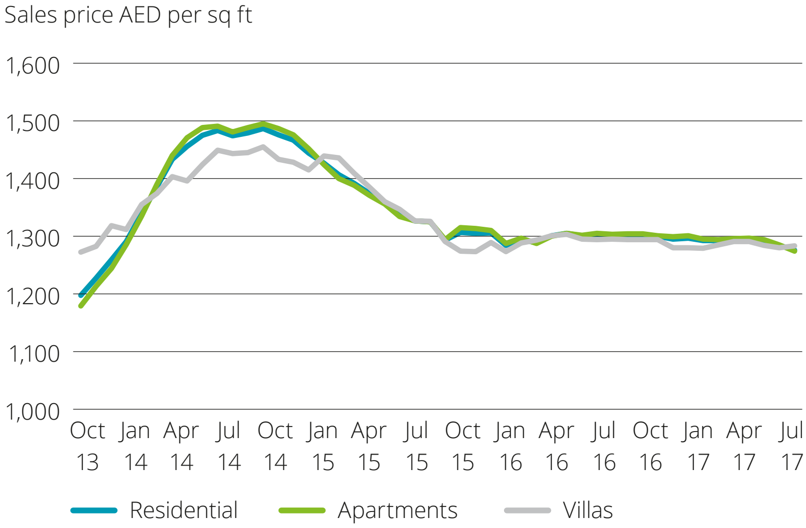
Average sales prices for residential property in Dubai declined by approximately 2% between Q4 2016 and Q3 2017. Average rents declined by approximately 7% over the same period.

These declines were largely a result of low oil prices impacting government spending, and denting investor confidence. This was compounded by a strong local currency reducing the purchasing power of investors from key international source markets, such as India and the UK.

In 2017, much of the new residential supply in Dubai continued to focus on the affordable segment. In addition, certain developers offered multi-year payment plans, with many offering up 60% of the purchase price payable post-completion. This was aimed at capturing demand from the affordable segment and in many cases to turn renters into buyers.

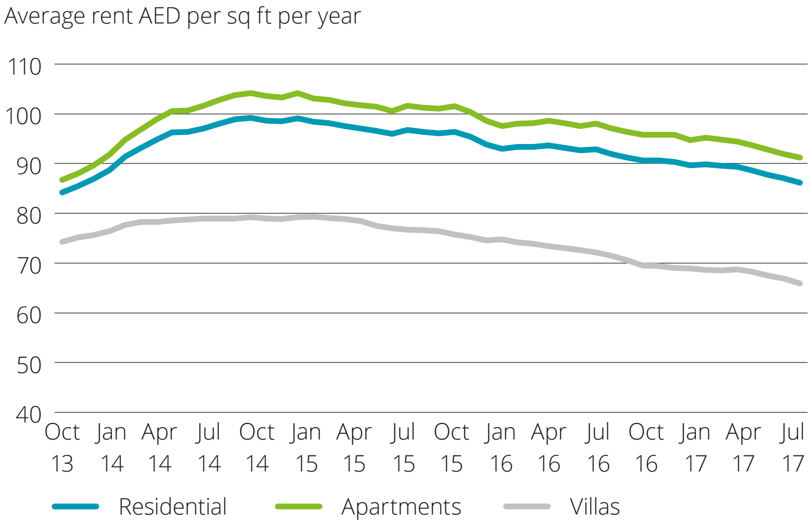
Based on consultations with key industry stakeholders, it is estimated that the total number of residential units delivered in Dubai in 2017 was approximately 15,000, representing an increase in total stock of 3.5% since the previous year.

Dubai residential sales prices
Q4 2013 to Q3 2017



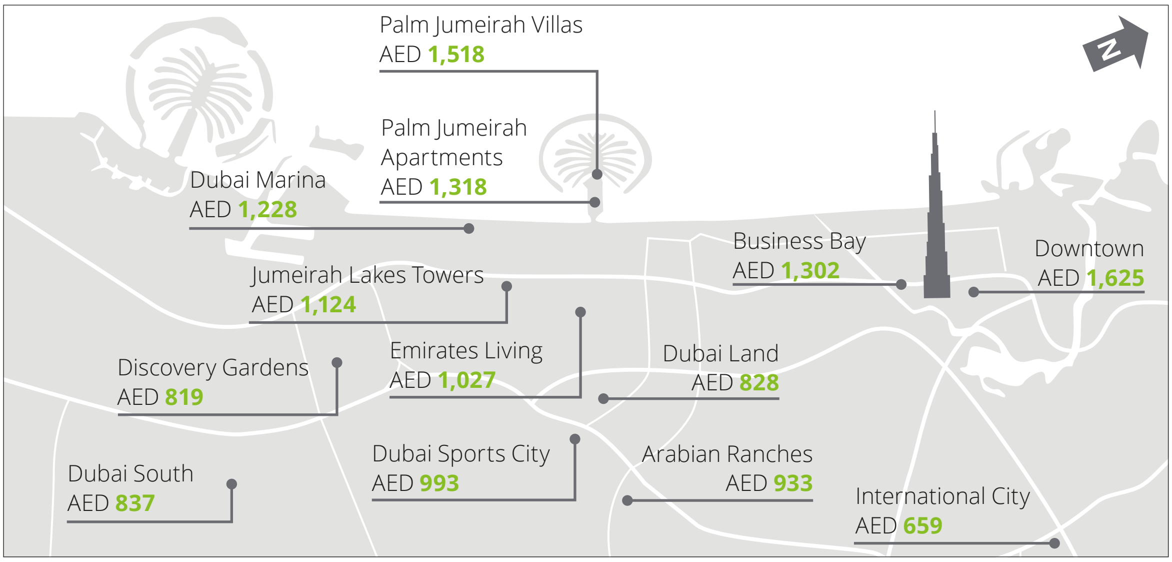
Source: REIDIN

Dubai residential rents
Q4 2013 to Q3 2017



Source: REIDIN

Dubai residential sales prices by location
Q3 2017



Source: Deloitte, Google Earth

Note: Locations are illustrative

Metric	Average apartment rents	Average apartment sales prices	Average villa rents	Average villa sales prices	Dubai average rents	Dubai average sales prices
Q3 2016	AED 71 per sq ft per year	AED 1,303 per sq ft	AED 99 per sq ft per year	AED 1,295 per sq ft	AED 92 per sq ft per year	AED 1,302 per sq ft
Trend	↓ 7%	↓ 2%	↓ 11%	↓ 1%	↓ 7%	↓ 2%
Q3 2017	AED 66 per sq ft per year	AED 1,274 per sq ft	AED 88 per sq ft per year	AED 1,283 per sq ft	AED 86 per sq ft per year	AED 1,276 per sq ft

Source: REIDIN

Dubai's retail market

Increasing competition between retailers as supply increases and retail sales decline.

A summary of 2017 performance

Data from the Economist Intelligence Unit (EIU) suggests that total UAE retail sales volume was down by 2.8% in 2017. This has been largely driven by declining disposable incomes (as inflation has outstripped wage growth) as well as a strong local currency making purchases more expensive for foreign visitors.

Domestic retail demand in Dubai is being constrained by a squeeze on disposable incomes. In 2017, 71% of Dubai residents expected to have the same or less disposable income in 2018, while only 29% expected to have more.

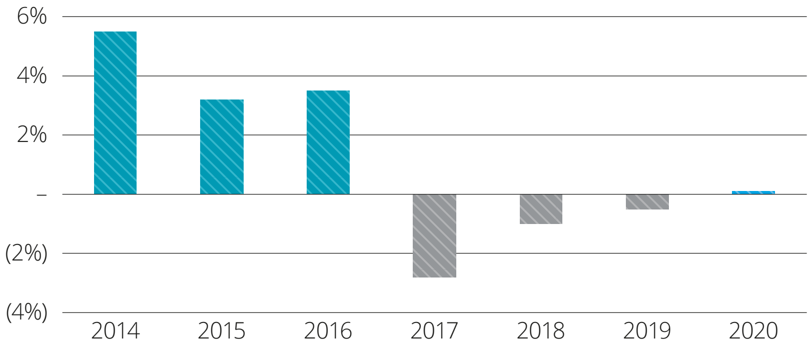
Notably, VAT was introduced in Dubai from 1 January 2018, which is expected to raise the overall cost of living in Dubai by between 2.7% and 3.7%, according to forecasts produced by the IMF.

The Dubai Mall and Mall of the Emirates consolidated their positions as the most popular malls with tourists in Dubai in 2017, collectively capturing 52% of total tourist retail demand.

For residents, 'Other Malls' (including smaller community centres and convenience retail) have increased in popularity, capturing 32% of resident retail demand in 2017.

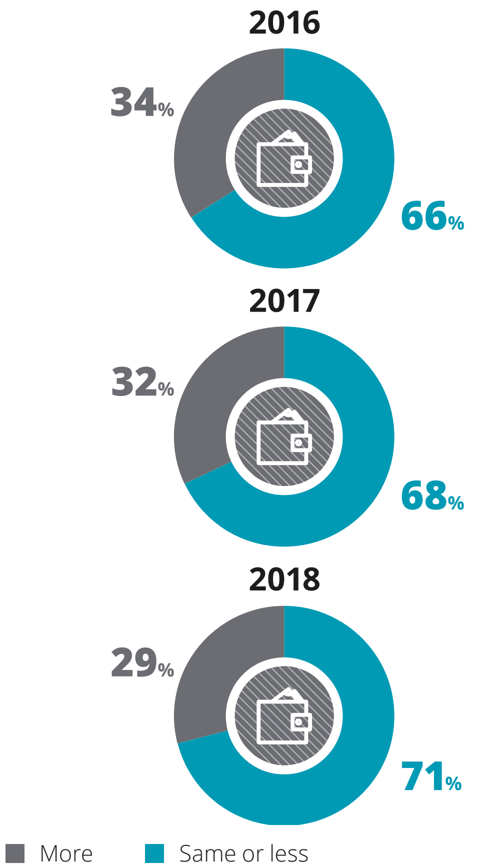
The number of visitors to Dubai from the GCC, traditionally a high spending retail source market, declined by 3% in 2017. Conversely, visitors to Dubai from South Asia increased by 1.5% in 2017.

UAE retail sales volume growth
2014 to 2020



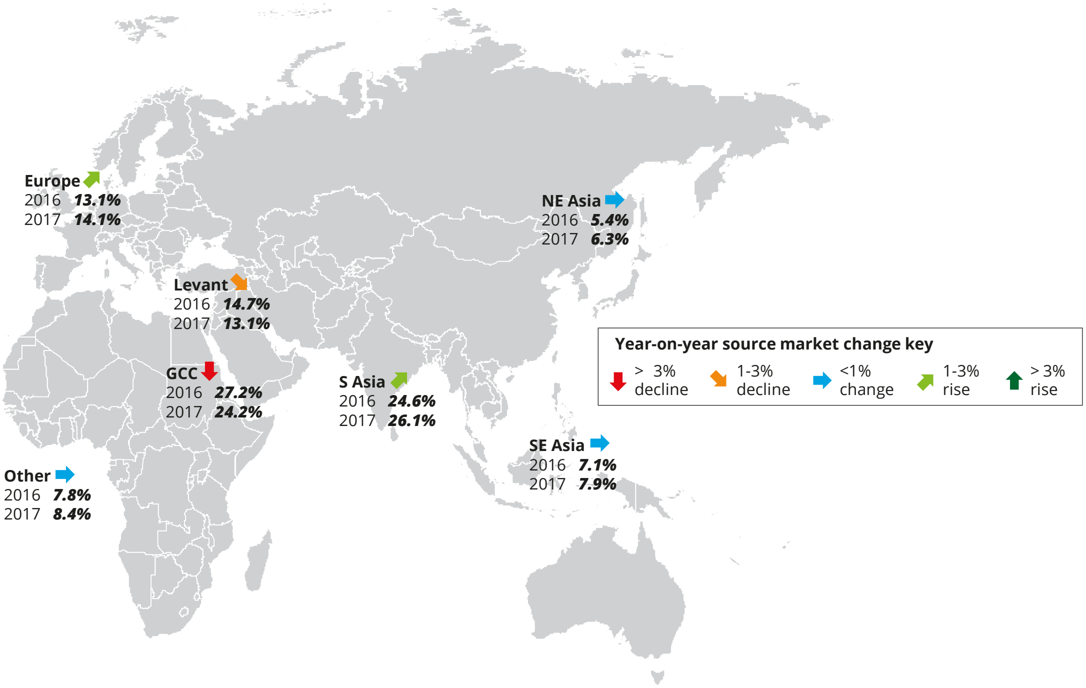
Source: EIU

Dubai expectations on disposable income
2016 to 2018



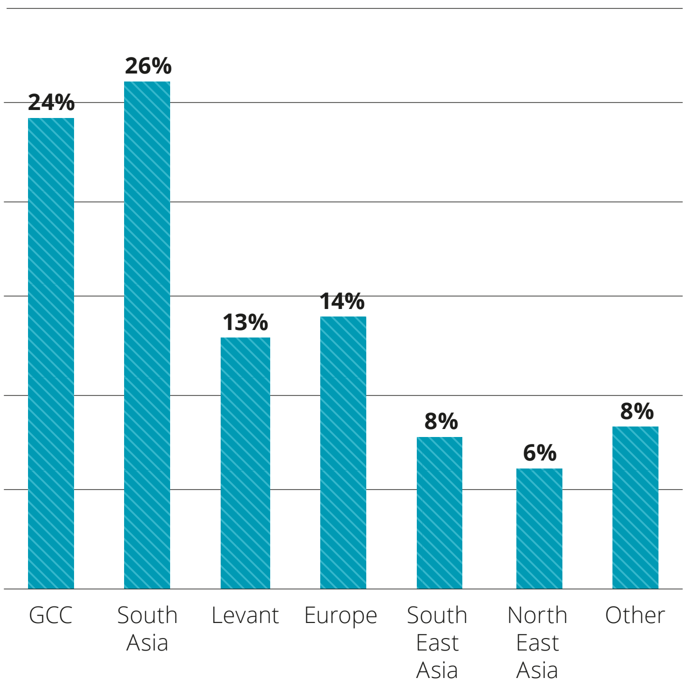
Source: grmc

Dubai retail mall source markets
2016 to 2017



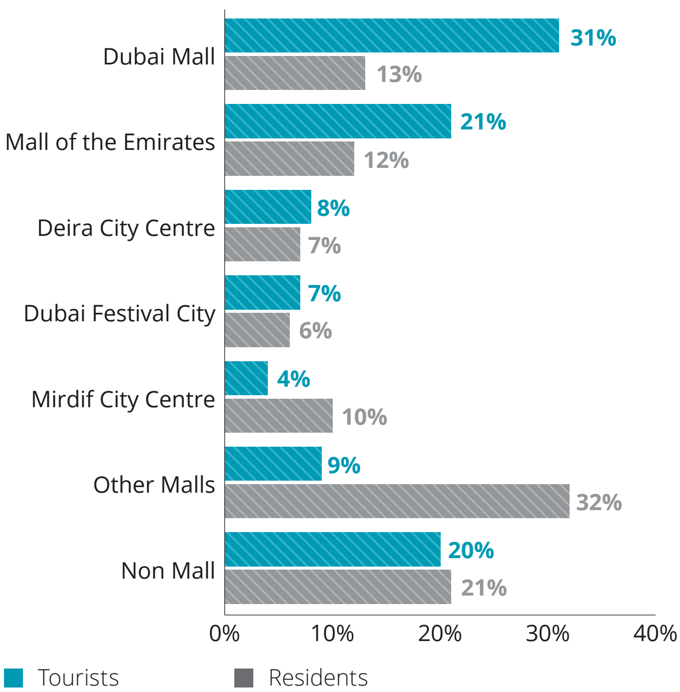
Source: grmc

2017 retail mall source markets



Source: grmc

Dubai tourist and resident mall preferences 2017



Source: grmc

Dubai's office market

Slowing occupier demand led to a 3% decline in office rents in 2017, although four submarkets registered positive rental growth.

A summary of 2017 performance

2017 was a challenging year for Dubai's office market. Slowing demand from new occupiers, combined with some existing occupiers looking to consolidate their office footprint, has led to landlords increasing incentives to attract and retain tenants.

As a result of this, commercial office rents in Dubai experienced a decline in 2017 with average rents for shell and core accommodation declining by 3% city-wide. In contrast, four office sub-markets registered rental growth in 2017: Al Barsha, Al Garhoud, Downtown and TECOM.

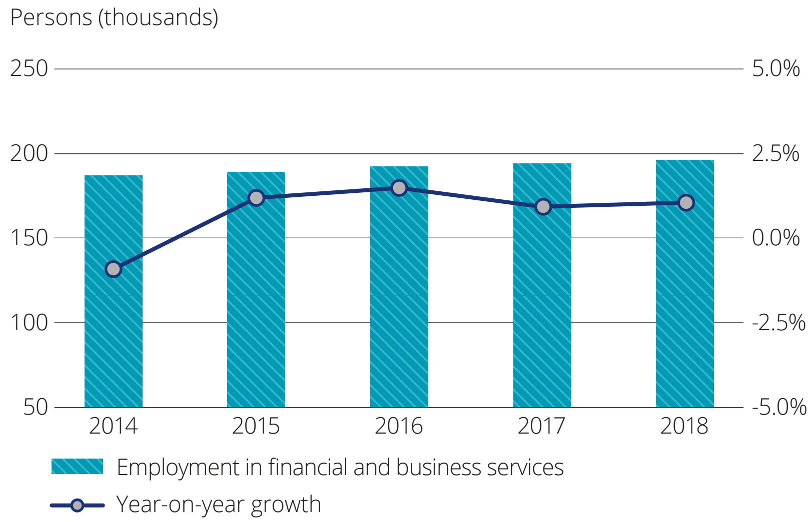
It should be noted that whilst overall rental levels in prime office locations such as DIFC have fallen slightly, this is largely due to the discounting of stock in the south of this free zone, whilst the north has remained stable.

Offices in Dubai that are specified to international Grade A standards with single, institutional ownership have remained broadly stable in terms of rents and occupancy. This is due to the sustained under-supply of quality product in the market.

Dubai's office market is likely to come under further pressure as a number of large scale completions significantly increase the volume of International Grade A office space. These include ICD Brookfield Place, One World Trade Centre and Emirates Towers Business Park.

Dubai employment in financial and business services

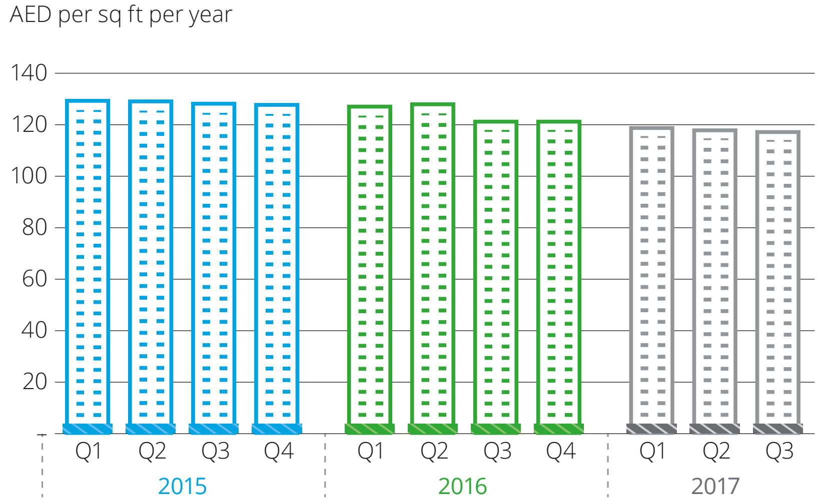
Q1 2014 to Q3 2018



Source: Oxford Economics

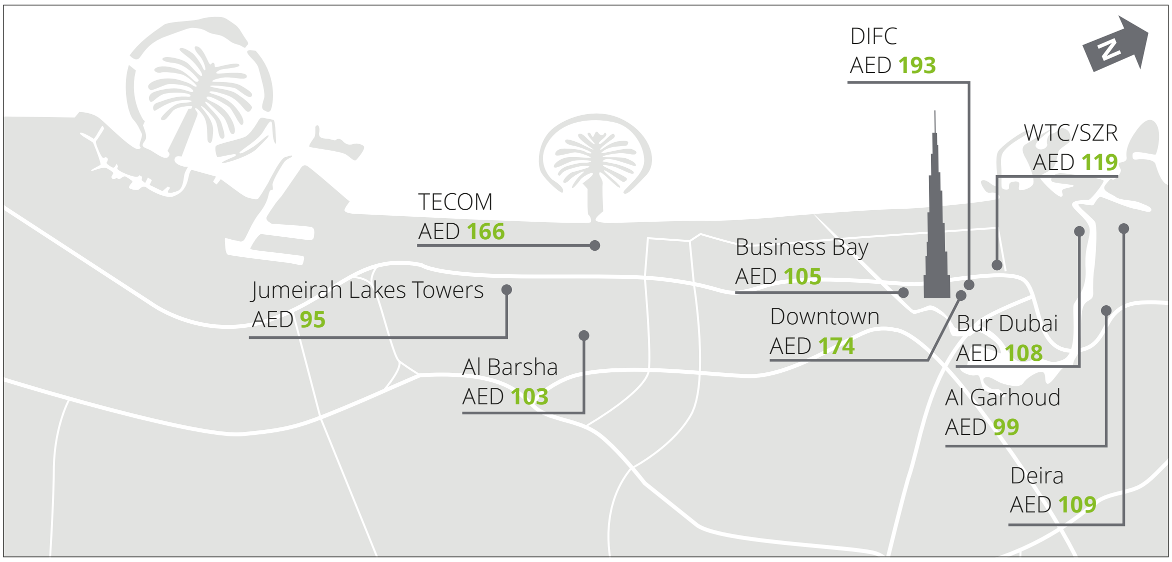
Dubai average office rents

Q1 2015 to Q3 2017



Source: REIDIN, Deloitte

Dubai average office rents
Q3 2017



Source: Deloitte, Google Earth

Note: Locations are illustrative

Area	DIFC	Bur Dubai	Al Garhoud	Deira	WTC/ SZR	Barsha Heights	Business Bay	Down-town	TECOM	JLT	Dubai average
Q3 2016	198	109	98	113	126	102	109	171	160	102	121
Trend	-2%	0%	1%	-4%	-6%	1%	-4%	2%	4%	-6%	-3%
Q3 2017	193	108	99	109	119	103	105	174	166	95	116

Source: REIDIN, Deloitte

Note: Rents are quoted AED per sq ft per year

Note: Rents are average achieved rents for shell and core offices exclusive of service charges

Dubai's industrial and logistics market

Strong fundamentals and a high level of infrastructure investment have enabled Dubai to capitalise on its strategic position to become a global transhipment hub.

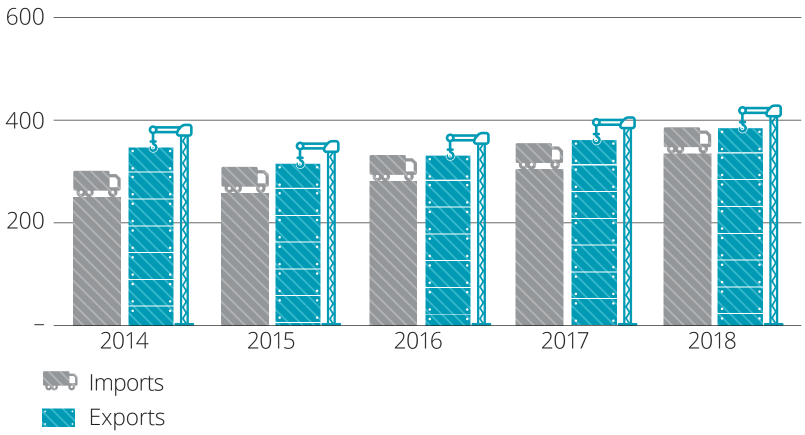
A summary of 2017 performance

Dubai has invested heavily in developing world class industrial and logistics infrastructure. Dubai World Central (DWC), Jebel Ali Free Zone and Jebel Ali Port have all capitalised on Dubai's strategic location and provide sea-air connectivity to global markets.

Sustained growth in UAE imports and exports has driven demand for industrial and logistics warehouses in Dubai. Key demand drivers, including airport cargo throughput, port throughput and road freight, have all increased between the first half of 2016 and the first half of 2017.

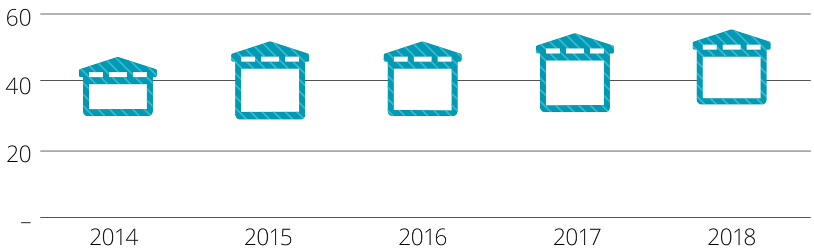
As a result of this sustained demand, rents for warehouses in Dubai have increased in 2017 by between 3% and 5%. Properties located near to key transport infrastructure have leased at a premium, whilst a broad shift in demand toward Dubai South has been evident in some segments, where connectivity to Jebel Ali Port and Jebel Ali Free Zone, via a bonded corridor, has attracted occupiers.

UAE imports and exports
2014 to 2018
US$ billion



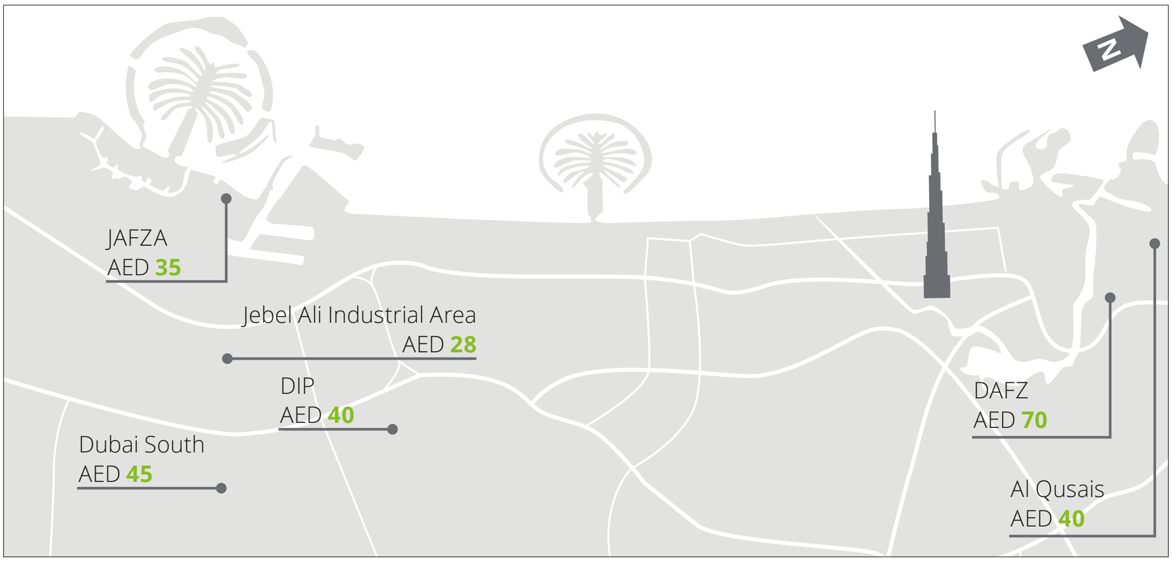
Source: BMI

Dubai average warehouse rents
2014 to 2018
AED per sq ft per year



Source: Deloitte

Dubai average warehouse rents
Q3 2017



Source: Deloitte, Google Earth

Note: Locations are illustrative

Period	DWC cargo throughput	DXB cargo throughput
H1 2016	430,132	1,282,074
Trend	↑ 3%	↑ 2%
H1 2017	443,835	1,302,911

Year	Jebel Ali container throughput	Jebel Ali tonnage throughput	Road freight tonnes
2016	15.7m	16.0m	29.0m
Trend	↑ 4%	↑ 2%	↑ 1%
2017	16.4m	16.3m	29.4m

Source: BMI

Note: Rents are quoted AED per sq ft per year

Note: Rents are average achieved rents for purpose built warehouses exclusive of service charges

Predictions for 2018

Dubai will become more connected than ever to the global economy

Dubai has established its position as a global city through various initiatives including the development of world-class infrastructure and a business-friendly legal and regulatory environment.

Dubai has developed world-class infrastructure. Dubai International Airport (DXB) handled 80.4 million passengers over the period January to November 2017, a year-on-year increase of 5.8%. This makes DXB the largest airport in the world in terms of international passenger numbers. Al Maktoum International Airport, being developed at Dubai South, will have the capacity to handle up to 200 million passengers annually. Other world-class infrastructure in Dubai includes Jebel Ali Port, the largest marine terminal in the Middle East and the ninth largest container port in the world.

Dubai has developed a business-friendly legal and regulatory environment. The Heritage Foundation's 2017 Index of Economic Freedom ranked the United Arab Emirates as the eighth most free economy in the world, citing efforts to strengthen the business climate, boost investment, and foster the emergence of a more vibrant and diverse private sector. Dubai has developed globally competitive sectors including finance, logistics, maritime and tourism. Taking the tourism sector as an example, data from the 2017 MasterCard Global Destination Cities Index shows that visitors to Dubai made a bigger relative contribution per resident than any other city in the world.

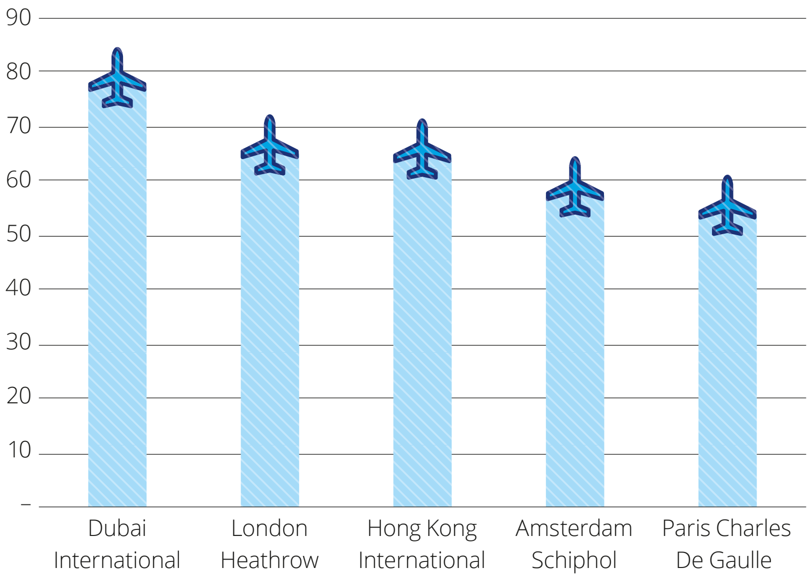
Dubai is an established global event hub. Dubai World Trade Centre hosts more than 300 events per year, which attract more than three million global visitors. Dubai Expo 2020 is forecast to attract millions of visitors to Dubai from approximately 180 countries.

2018 Prediction

This year will see Dubai more connected than ever to the global economy. Although this presents a number of opportunities for Dubai, there are also risks that will need to be managed in 2018. According to the World Bank, risks to the global economy include increasing economic protectionism, heightened geopolitical uncertainty and the possibility of financial market turbulence.

Top five airports by international passenger throughput 2016

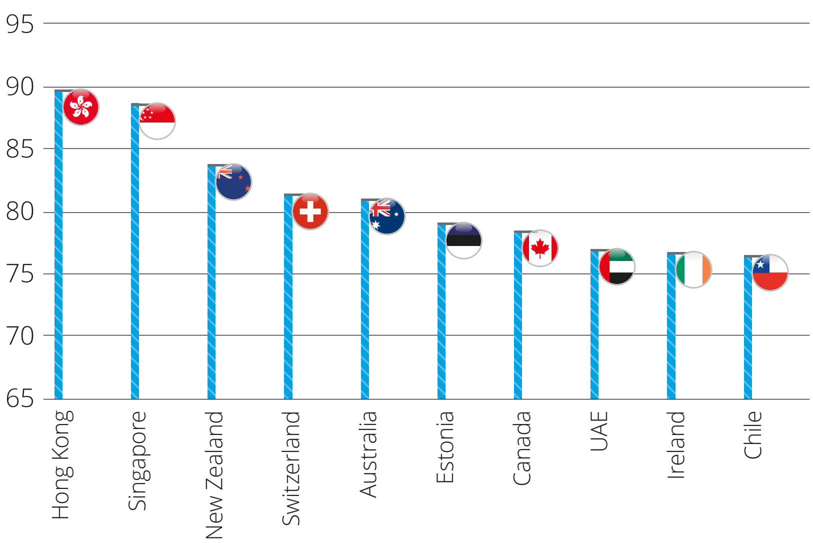
Passengers (million)



Source: Airports Council International

Top ten countries by economic freedom 2017

Index of economic freedom score



Source: The Heritage Foundation

Dubai's development finance market is evolving and becoming more diverse

Development finance via bank debt remains available in Dubai for qualifying real estate developers and projects. Other sources of finance, such as Export Credit Agencies (ECAs) and direct private debt funds, represent a diversified real estate finance market in Dubai.

Bank debt remains available in Dubai for qualifying developers and projects. Finance for real estate projects remains available in Dubai. This is generally for qualifying developers who have a proven track record and alternative sources of free cash that can be used to service project debt during construction. A typical finance structure for a real estate project in Dubai includes a loan to construction value ratio of 60% to 70% on hard construction costs at a rate of approximately 5.5% to 6% (EIBOR + margin). Loan tenures are typically between two to three years of construction plus seven to eight years of amortization, with a 20% to 30% balloon payment.

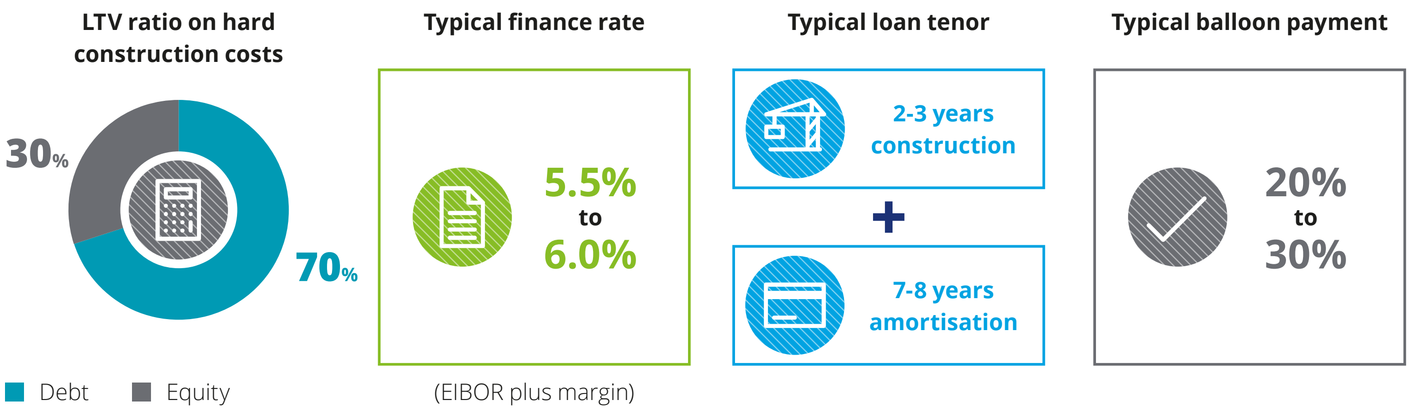
Sources of non-bank finance are starting to emerge in Dubai. In addition to senior bank debt, ECA supported debt and mezzanine debt has generally been available in Dubai. There has also been increased appetite by credit funds to lend to the real estate sector in Dubai. Such private credit is priced between senior bank debt and mezzanine debt, which is available to both new development projects and existing income-producing assets. As with mezzanine debt, direct private debt funds increase borrowing costs but provide flexibility in repayment terms and can also reduce equity investment burdens.

Residential developers in Dubai are increasingly taking on finance risk from unit buyers through phased payment plans. Certain residential developers in Dubai have started to offer three to five year phased payment plans in an attempt to access Dubai's mid-market segment and to turn renters into buyers. This represents a future finance risk, as sales booked on low down payments may not always lead to converted transactions.

2018 Prediction

Dubai's development finance market is evolving and becoming more diverse, as alternative sources of finance become increasingly available. This will mean that real estate finance is likely to remain available, on competitive terms, for qualifying developers who have a proven track record and alternative sources of free cash that can be used to service project debt during construction. Looking to consumer finance, phased payment terms in Dubai's residential market mean that developers will be taking on more finance risk in 2018.

Dubai typical real estate debt terms, 2018



Source: Deloitte

Note: subject to application

Disruptive technologies, such as 3D printing, will become more mainstream

Dubai is leading the world in a number of technologies that are likely to disrupt the real estate market, including 3D printing and peer-to-peer technologies. Meanwhile, Dubai is playing catch-up with other mature markets on some disruptive technologies, most notably online retail.

Dubai has set the target that all new buildings will be 25% 3D printed by 2025. Dubai's 3D printing target, set by the Dubai Future Foundation's Dubai 3D Printing Strategy, aims to substantively reduce the cost of both construction materials and labour, in addition to reducing the amount of time taken to construct buildings. Dubai's 3D printing target, administered by the Dubai Municipality, will be introduced on a sliding scale basis, beginning in 2019 with a requirement that all new buildings are 2% 3D printed.

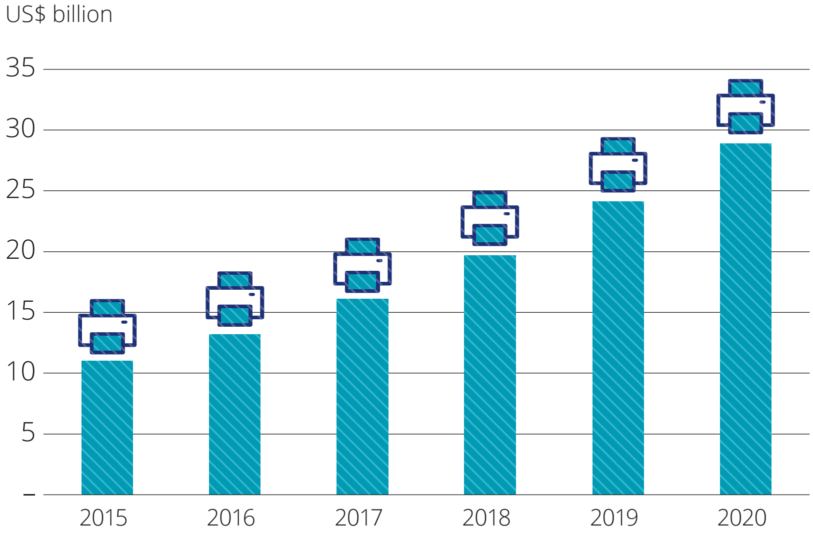
Dubai is exploring peer-to-peer technologies. The Dubai Land Department, in cooperation with Smart Dubai, is looking at how to adopt Blockchain technology within its electronic real estate platform. Although this initiative is still in its early stages, it has the potential for multiple applications that include property purchases, property mortgages, utilities payments and property and facilities management.

Dubai has been a late adopter of online retail, but this is about to change. Online retail sales in the Middle East account for approximately 2% of all retail activity, a figure well below mature markets in America and Western Europe. Recent announcements suggest that this is about to change. In 2017, Amazon closed the purchase of Middle East online retailer Souq.com. Also in 2017, Mohamed Alabbar, founder and Chairman of Emaar Properties, announced the launch of Noon, a Middle East online retailer that has secured substantial funding.

2018 Prediction

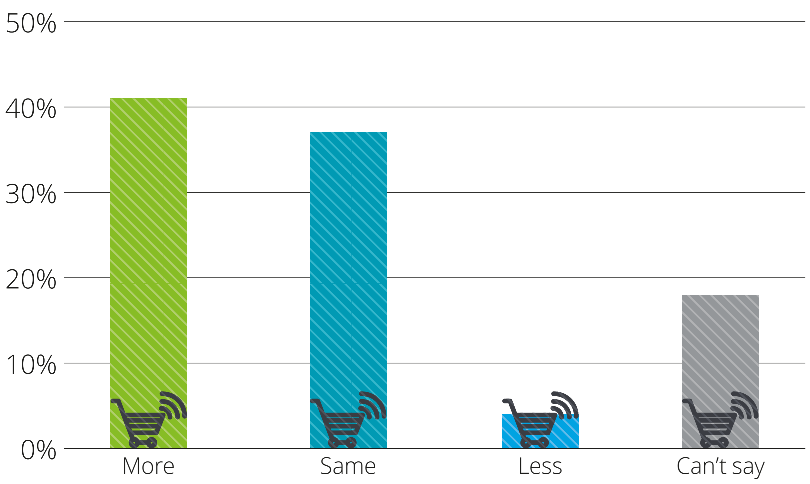
This year will see disruptive technologies becoming more mainstream in Dubai's real estate market. There will be no absolute winners or losers, as disruptive technologies represent both threats and opportunities. Taking online retail as an example, it is not a case of "in store" versus "online" but the adoption of multiple channels to market. Online retail, as a disruptive technology, will most likely impact each asset class differently and to varying degrees.

Global 3D printing market size
2015 to 2020



Source: statista

Dubai residents' expectations for online shopping
2018



Source: grmc

The introduction of VAT will be one of the biggest challenges for Dubai's real estate industry

The construction and supply of commercial, industrial and retail properties, as well as the provision of infrastructure, is now subject to VAT at a rate of 5% from 1 January 2018. This poses a challenge for many stakeholders in Dubai's real estate industry.

Lease incentives may become more complicated. It has become more common in Dubai for landlords to offer rent free periods and other incentives to both attract and retain office, industrial and retail tenants. As from the 1 January 2018, lease incentives could trigger a VAT liability if they are deemed to have been offered in return for an inducement, such as a contribution towards capital fit out works.

VAT may represent a cash flow concern for some developers. Margins are typically low in the real estate industry. The introduction of VAT on the purchase of construction materials and professional services may cause cash flow pressures and impact working capital for some of Dubai's developers.

Dubai's hotel operators may face a complex process to establish VAT across multiple revenue streams. For invoice and accounting purposes, hotel operators in Dubai will need to treat the VAT implications of each revenue stream separately. These revenue streams typically comprise room revenue, F&B revenue, telecommunications revenue and conference and events revenue.

2018 Prediction

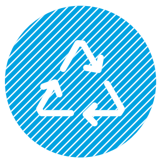
The introduction of VAT represents one of the biggest challenges to Dubai's real estate industry in 2018. The introduction of VAT in Dubai will drive wide ranging changes, from the revision of accounting systems and processes to cash flow and working capital pressures for some developers.

VAT treatment of land transactions in Dubai

Bare land (greenfield)

0%

Used land (brownfield)



5%

Source: Deloitte

VAT treatment of commercial and residential property in Dubai

Scenario	VAT treatment	Impact and outcome
Sales and rents for commercial property	5%	Treated as subject to VAT at standard rate of 5%.
First sale/rent of residential property	0%	VAT incurred during construction will be recoverable, with no impact on the costs of construction.
Subsequent sale/rent of residential property	0%	Developers will not be able to recover any VAT incurred during construction, but seek to recover this on top of normal profit margins when the property is sold or leased.

Source: Deloitte

Get in touch

We bring together teams with global knowledge and local experience to provide customised solutions for clients across the full spectrum of the real estate community.

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