Macroeconomic Overview & Outlook

Stronger oil revenues and progress on economic and social reforms have helped drive the Saudi economy in 2018, with GDP growth levels expected to register 2.4% according to Oxford Economics, up from -0.9% in 2017. Inflation rates remained relatively stable at an annual average of 3% following an initial surge on the back of subsidy cuts and the implementation of a 5% VAT at the start of the year. 2019 is expected to see inflationary pressures ease off as the base effect of these measures wears off.

While unemployment rates among Saudi nationals remain high, we are likely to witness growth in the labor market in the medium-to-long term following several reforms aimed at promoting Saudization, particularly in the retail sector, and encouraging more female participation in the labor force. 2019 is expected to witness ongoing activity on the back of strong reform momentum and increased government spending as outlined in the 2019 budget announcement. The expansionary budget is testament to the government’s commitment towards driving economic growth and strengthening the business environment. We expect this to reflect positively on the real estate sector as commercial activity picks up and foreign investment increases. As the biggest economy in the Middle East, we are also likely to see private demand play a large role in the real estate and construction sectors. However, we remain cautious that any event of falling oil prices could soften growth levels over the next 12 months.

A New Era of Hospitality and Entertainment

2018 represented a year of change in Saudi Arabia, driven by Vision 2030’s objective to increase and diversify entertainment in the Kingdom. From announcing a new online visa scheme to hosting the Ad Diyahlah E-Prix and post-race concerts, efforts to promote the entertainment sector are expected to reflect positively on the tourism and hospitality market.

Further announcements in the tourism sector include the launch of Almaala, a new luxury-destination hotel situation on Saudi Arabia’s north-western coast of the Red Sea. The project sits as part of a giga-projects investment portfolio (alongside NEOM and the Red Sea Project) launched by the Public Investment Fund (PIF). In the capital, Riyadh, a new entertainment and sports destination ‘Al Qiddiya’ was also launched by PIF. This project will include a Six Flags theme park, entertainment centres, sports amenities and an array of historical, cultural and educational activities. We view these additions to the entertainment and tourism industry as significant drivers of Saudi Arabia’s non-oil economic growth and expect them to generate more job opportunities. These projects are also likely to trigger large-scale real estate development activity driven by the public and private sectors.

Developing New Industries

December 2018 saw the inauguration of the King Salman Energy Park (Spark) located in the Eastern Province, a project developed by Saudi Aramco in partnership with the Saudi Authority for Industrial Cities and Technology Zones. Spark consists of five main regions focusing on general manufacturing, liquids and chemicals, metal formation and industrial services. With an expected GDP contribution of SAR 22 billion by 2035, we view the inauguration of Spark as a positive step towards developing industries with potential for growth and job creation in the Eastern Province. This in turn is expected to fuel demand for commercial and industrial real estate. The Park’s unique eco-system (consisting of world-class infrastructure and advanced supply chain technologies), is likely to act as a catalyst, attracting foreign investment and encouraging private sector participation.

Cinemas Make a Return

The Development and Entertainment Investment Company (DEIK) in collaboration with AMC Entertainment launched the Kingdom’s first cinema in over three decades in 2018. This move has prompted many local developers to sign agreements with cinema operators from across the region to open cinema multiplexes and offer a diverse selection of entertainment outlets to customers. This paves the way for significant opportunities in the retail sector particularly in the field of shopping-entertainment or “shopertainment”.

Saudi Arabia’s population is expected to reach 39.5 million by 2030 according to Oxford Economics. While recent economic reforms namely the introduction of VAT, subsidy cuts and the expatriate levy have weighed on the purchasing powers of residents, we remain positive on the industry’s long-term growth potential and expect retailers to embrace the shift in shopping habits brought about by Vision 2030.

Promoting Home Ownership

Several initiatives boosting home ownership in Saudi Arabia were introduced in 2018. The Ministry of Housing in partnership with the Real Estate Development Fund (REDF) launched ‘Sakani II’, which aims to deliver 300,000 residential products throughout the Kingdom. Authorities also unveiled a SAR 120 billion mortgage market plan, aimed at raising home ownership among Saudi nationals to 60% by 2020 and 70% by 2030. Highlights of the program include a SAR 18 billion loan-guarantee scheme and SAR 12.5 billion down payment support program.

We view these programs as positive steps towards helping citizens own their first home and strengthening the residential real estate market. It remains pivotal however to encourage private sector participation in the development of housing. Already this is being stimulated by the White Land Tax introduced in 2017, which was designed to unlock the private sector land bank and boost construction activity. Further incentives include providing government land for development, conditional off-take guarantees, and amending legislation to allow for increased floor area ratio, thus increasing residential density.

Transport & Infrastructure

The 448 km Al Haramain High Speed Railway connecting Medina, Makkah and Jeddah was inaugurated in 2018, supporting the growing number of Pilgrims to the Makkah region. The Railway also connects to Jeddah Airport and King Abdullah Economic City, thus easing and promoting business travel. Another key development in the transport sector was the soft opening of the new King Abdulaziz International Airport (KAIA) in Jeddah. This forms part of plans to welcome 30 million passengers annually. KAIA features a 28,000 sq m commercial area and an onsite hotel of 175 keys.

These, and other public transport projects in the pipeline such as the Riyadh Metro, are expected to not only facilitate movement, but also tap into the country’s potential as a global transport hub, improve the competitiveness of its infrastructure, and provide opportunities for private and foreign investors.
While all sectors of the Riyadh market remain in the late downturn stage of their cycle, the *residential* market appears closer to the bottom, where marginal rental declines may be experienced over the rest of 2019. The slowdown in economic activity restricted growth levels in the *office* market and increased vacancies in 2018. Growth in the *retail* sector remains constrained across all mall types on the back of a strong supply pipeline. While the *hotel* sector saw occupancy rates remain stable, average daily rates remain under downward pressure, negatively impacting revenues.

* Hotel clock reflects the movement of RevPAR (Revenue per available room: ADR * occupancy rate)

Note: The property clock is a graphical tool developed by JLL to illustrate where a market sits within its individual rental cycle. These positions are not necessarily representative of investment or development market prospects. It is important to recognize that markets move at different speeds depending on their maturity, size and economic conditions. Markets will not always move in a clockwise direction, they might move backwards or remain at the same point in their cycle for extended periods. Source: JLL.
Riyadh - Office

Supply

Construction activity in Riyadh’s office market slowed down in 2018, as a total of 188,000 sq m of office space was delivered; the lowest rate of delivery in 3 years. Q4 2018 saw the delivery of 131,000 sq m of office GLA, bringing the total office stock in Riyadh to 4.3 million sq m as of year-end 2018. The next 12 months are expected to witness the completion of 190,000 sq m of office space, increasing the total office stock to 4.5 million sq m by the end of 2019. The upcoming premium quality supply is expected to result in a “flight to quality” as occupiers move from lower grade office units to higher grade spaces.

Performance

Limited occupier demand and subdued economic activity continued to weigh on the performance of the office market in 2018. Average rents declined 4% Y-o-Y to register SAR 1,248 per sq m. With few businesses looking to expand their operations, vacancy rates remained flat at 8% in Q4 2018. Looking ahead, we expect rents to remain under pressure, particularly for grade B office spaces with poor accessibility and parking limitations. Vacancy rates are set to increase as new supply enters the market.

In the long-run, we expect demand to pick up on the back of increased government spending and the implementation of various strategies to encourage private sector growth in line with the country’s Vision 2030. We are also likely to see the nature of demand changing as a combination of local and global trends, namely flexible office designs, millennials entering the workforce and the growth of Saudi entrepreneurs, change the commercial landscape of Riyadh.

Riyadh - Residential

Supply

A total of 29,000 residential units were delivered during 2018, supported by the government’s initiative to provide more housing for Saudi nationals. Q4 2018 saw the delivery of 7,000 residential units, bringing the total supply of residential apartments and villas in Riyadh to 1.3 million units. An additional 30,000 units per annum are expected to hand over in both 2019 and 2020.

While some developers continued to expand their high-end residential offering, most remain committed to providing affordable residential solutions in line with the government’s initiative. Looking ahead, we expect the affordable housing sector will continue to drive construction activity and the overall real estate market.

With social demographics changing rapidly, and the question of affordability increasingly in the limelight, developers are moving away from the traditional detached villas and spacious apartments that catered to larger families. Instead, future developments are likely to include a mix of unit sizes and layouts to cater to the growing young population.

Performance

The performance of Riyadh’s residential market continued to soften on an annual basis, as average rents for apartments and villas decreased marginally by 1% and 2% respectively in Q4 2018 versus Q4 2017. Meanwhile, sale prices for apartments and villas declined 4% and 3% respectively over the same period. On a quarterly basis, no noticeable declines were recorded in either sale prices or rentals, indicating the market is slowly reaching the bottom of its cycle.

Riyadh’s residential market is expected to continue softening in the next 12 months, albeit at a slower rate, as more supply is handed over. However, with the completion of Riyadh metro the residential landscape is expected to change drastically as the value of properties in close proximity to the transit system is expected to increase.
Riyadh - Retail

Supply
Around 98,000 sq m of retail GLA was completed in 2018, which is below the last 3-year average of 150,000 sq m. Only 14,000 sq m of retail space was handed over in Q4 2018, with the majority of this falling in the neighborhood centre category. This increased the total mall based retail stock in Riyadh to 2.15 million sq m.

Around 470,000 sq m of retail space is scheduled for completion in 2019. Notable upcoming projects include the University Avenue, adjacent to King Saud University, as well as new projects situated in proximity to the airport and in the Northeastern catchment area, namely the Qurtoba Boulevard, Shopping Front, and Granada Centre Extension.

The nature of Riyadh’s retail stock is expected to evolve in response to the growth and change in the city’s workforce. To attract this consumer base, we expect new mall developments to offer more entertainment and F&B concepts, adopt unique designs and interactive technologies, and expand their tenant mix to include international brands.

Performance
Retail rents softened across all mall categories in 2018, with community centers registering the largest declines (10% Y-o-Y). Meanwhile, super-regional and regional mall rents dropped at a slower rate given their limited supply. In turn, vacancy rates across all mall categories increased to 15% by year-end 2018.

Given the level of upcoming supply and increased competition, we expect rents to remain under pressure over the next 12 months.

In the long-run, we expect the expansion of the entertainment sector to strengthen the Riyadh retail market. The increased participation of women in the workforce is also likely to positively impact retail sales and consequently the performance of retail centres, particularly those with a diversified offering.

Riyadh - Hotel

Supply
The hotel market in Riyadh saw the delivery of around 1,700 new hotel keys in Q4 2018, raising the total inventory to 13,700 keys as of year-end 2018. This included the highly anticipated Fairmont Riyadh Business Gate and the Hilton Riyadh Hotel & Residences.

An additional 2,600 and 1,400 keys are expected to complete in 2019 and 2020 respectively. Assuming all projects are delivered within the specified timeframe, the total supply is expected to expand to 17,700 keys by year-end 2020.

While historically Riyadh had been at the forefront of the MICE business, considering its relevance as the capital of the Kingdom, new infrastructure developments and entertainment shows and festivals will help diversify the city’s tourist base, particularly increasing leisure demand. In turn, hoteliers are likely to diversify their offerings and focus on improving their services, modernizing their interiors and incorporating new technologies to meet the demands of more sophisticated travelers.

Performance
Hotel occupancy rates increased 1 bp to reach 55% in the YT November 2018 compared to the same period last year. Meanwhile average daily room rates (ADR’s) declined 10% Y-o-Y to register USD 170. This is largely due to the continued supply growth. This resulted in an 8% decline in revenues per available room (RevPAR’s) to USD 93 over the same period.

Hotel market performance is expected to remain under pressure over the next 12 months as supply continues to increase. However, in the long-run, we expect the hospitality sector (together with the retail market) to lead the recovery of the real estate industry in Riyadh, driven by large-scale investments in leisure and entertainment offerings.

Source: STR Global

Source: JLL
The real estate market in Jeddah continued to witness a slowdown across most asset classes in 2018. In the **residential** sector, rents and sale prices dropped significantly as demand remains sluggish. The **retail** market continues to be constrained by the slowdown in spending, restricting overall growth levels, while the slowdown in commercial activity has limited rental growth in the **office** sector. Meanwhile, Jeddah’s **hotel** market continued to outperform the rest of the country, with room rates (ADR’s) increasing 11% Y-o-Y to November 2018.
Jeddah - Office

Supply

Subdued occupier demand saw developers delay the delivery of office projects in 2018. Q4 2018 saw the completion of one office building, Rovan on Prince Saud Al Faisal Road, adding 8,500 sq m of GLA to the market. This brings the total stock of quality office space to 1.1 million sq m of GLA as of year-end 2018.

The next 12 months are expected to witness the delivery of an additional 106,000 sq m of office space, however we can expect some delays in the handover of these projects. As such, Jeddah’s office market is to remain tenant friendly and is likely to see landlords offer further incentives to attract tenants to their space.

While traditionally the office stock in Jeddah has been characterized by low quality buildings scattered along the main commercial corridors, upcoming supply is likely to be of Grade A quality stock located within business parks and in mixed-use developments.

Performance

Commercial office rents in Jeddah declined 19% in 2018. Rental rates in premium Grade A office spaces saw a decline of 14% to average SAR 1,015 per sq m, as landlords adjusted rents to meet market levels. Meanwhile, rents of Grade B buildings located in secondary locations dropped 22% to average SAR 548 per sq m. Overall vacancy rates increased over the quarter to reach 21%.

In a tenant favourable market, we expect office rents in the next 12 months to soften further while vacancy rates increase on the back of additional supply and strong competition.

In the long-run, efforts to increase the private sector’s participation and contribution to economic activity, in addition to the increasing participation of woman in the workforce, are expected to support commercial activity.

The sector is also expected to benefit from large infrastructure investments such as the newly operational Al Haramain Railway, which links the City of Jeddah to Jeddah Airport and King Abduallah Economic City, and the expansion of King Abdulaziz International Airport, which helps position the city as a regional hub.

Jeddah - Residential

Supply

Around 4,260 residential units were completed in 2018 in Jeddah, which is lower than the 3-year average. Q4 2018 saw the completion of one project, The Golden Tower on Al Corniche Road, adding 71 apartment units to the overall supply. This brings the total stock of available residential apartments and villas to 817,000 units as of year-end 2018.

An additional 7,000 and 16,000 units are expected to handover in 2019 and 2020 respectively. These include Emaar Residences ‘Abraj Al Hilal 3’ within Jeddah Gate and Manazil Al Safa, in addition to the first phase of Salman Bay Housing Project and Al Makarona Community.

Performance

The overall performance of the residential market remained weak with both sale prices and rental rates registering annual declines. Sale prices for both apartments and villas dropped 7% Yo-Y, meanwhile rents fell by 13% for apartments and 12% for villas over the same period.

The soft performance of the residential market is largely due to the slowdown in economic activity and the decreased demand for residential units in Jeddah, as a result of the expat levy which saw many families relocate.

As more supply is expected to materialize, residential vacancies are expected to increase further, resulting in more pressure on both rents and sale prices. This could result in landlords decreasing their asking prices to attract demand. The next 12 months are expected to see homeowners and tenants have more bargaining power when it comes to negotiating their lease and sale terms.
Jeddah - Retail

Supply

A total of 32,000 sq m of retail GLA was delivered in Jeddah throughout 2018, which is a significant decrease from the average retail GLA delivered in the past 3 years. Q4 2018 saw the completion of one neighbourhood centre, Al Marwa Plaza, adding 15,000 sq m of GLA to the retail pipeline. This brings the total retail stock to 1.4 million sq m as of year-end 2018.

The next 2 years are expected to see the delivery of much higher levels of new supply, with 108,000 sq m and 280,000 sq m scheduled to complete in 2019 and 2020 respectively.

With the rapid social and economic changes being introduced in the Kingdom, cinemas, F&B and entertainment options are becoming increasingly vital features of shopping centres and are expected to play a significant role in the mix of upcoming supply as mall operators capitalize on new opportunities.

Performance

Retail rents for regional malls continued to soften in Q4 2018, registering a 5% decline Y-o-Y. Meanwhile, rents in super-regional malls remained relatively stable on the back of limited supply. Vacancy rates were flat Yo-Y at 13%, as landlords continued to offer incentives to retain tenants and maintain healthy occupancy rates.

Performance is expected to remain under pressure as the supply pipeline increases over the next 12 months. This is likely to result in mall operators adjusting their rent expectations in order to retain tenants and ensure healthy footfall levels.

Jeddah - Hotel

Supply

2018 saw the addition of 772 hotel keys in Jeddah, which represents a slight decrease from the 3-year average of stock delivered. There were no notable hotel completions in Q4 2018, leaving the total supply of quality hotel keys in Jeddah at 11,500.

Approximately 2,700 and 1,100 keys are expected to enter the market in 2019 and 2020 respectively, with most of these projects at an advanced stage of construction. Scheduled completions in Q1 2019 include two hotels in the upscale segment: Movenpick Hotel & Apartments Al Taalibah Jeddah (164 keys) and Hyatt House Jeddah Sari Street (112 keys).

Performance

The hotel market in Jeddah recorded an uplift in performance in the YT November 2018. Average daily rates (ADR) increased 11% to register USD 293 over the same period, driven by an increase in leisure travellers during the summer months. Meanwhile, occupancy rates registered 59%, a 1 bp decrease from YT November 2017 figures. Consequently, revenues per available room (RevPAR) increased 9% to record USD 172 in the YT November 2018.

The next 12 months are expected to witness a slowdown in the overall performance of the hotel market, with ADR’s coming under further pressure as more hotel keys are delivered to the market.

However, in the long run, the expansion of Jeddah’s entertainment and cultural offerings is expected to bode well for the hotel sector as a series of initiatives are paving the way for developers and investors to venture into newly established sectors. These projects aim at diversifying Jeddah’s tourist base, creating further demand for hotel properties and thus boosting overall performance.
Residential rents and sale prices in DMA continued to soften in 2018, with further declines expected on the back of increased supply. Office rents were under pressure given limited occupier demand as DMA’s economy remains reliant on the hydrocarbon sector. While the overall performance of the retail market remained subdued, super-regional and regional centres performed better than community centres. In the hotel market, occupancy levels maintained their stability as DMA remains an attractive destination for local tourists. However, average daily room rates dropped 9% on the back of additional supply.

* Hotel clock reflects the movement of RevPAR (Revenue per available room: ADR * occupancy rate)

Note: The property clock is a graphical tool developed by JLL to illustrate where a market sits within its individual rental cycle. These positions are not necessarily representative of investment or development market prospects. It is important to recognize that markets move at different speeds depending on their maturity, size and economic conditions. Markets will not always move in a clockwise direction, they might move backwards or remain at the same point in their cycle for extended periods. Source: JLL
The second half of 2018 saw the completion of 73,000 sq m of office space in DMA, bringing the total office stock to 921,000 sq m by year-end 2018. The majority of the delivered stock (55%) was standalone high rise administrative towers, while the remaining supply was built within mixed-use developments including retail and residential offerings. More than 40% of the new stock handed over was in Khobar, 35% in Dhahran, and 25% in Dammam.

Looking ahead, DMA’s office market is expected to witness the delivery of 58,000 sq m and 26,000 sq m of office GLA in 2019 and 2020 respectively. Notable expected completions include Taaziz Tower, Abdulhadi Al-Hugayt, and Al-Hairi Tower.

**Performance**

Average rents in DMA’s office market decreased 2% during 2018 to SAR 989 per sq m. Modern buildings offering good quality amenities, adequate parking, and a central location experienced more resilience than the older towers of lower quality. Vacancy rates remained relatively stable, registering 31% at year-end 2018.

With the delivery of over 80,000 sq m of GLA over the next two years we expect rents to remain under pressure, particularly as DMA continues to rely on the hydrocarbon sector. Large scale investments like the King Salman Energy Park (SPARK), are expected to boost demand for office space which in turn will reflect positively on the performance of the office market.

## DMA - Residential

**Supply**

Around 3,000 residential units were handed over in H2 2018 across Dammam, Khobar and Dhahran. This brings the total stock of residential units in DMA’s to around 351,000 as of year-end 2018.

The next two years (2019-2020) are expected to witness ongoing construction activity as 6,000 units per annum are due to complete. Supporting this construction activity is the government’s target of providing housing units to Saudi nationals in an attempt to increase home ownership to 60% by 2020 and 70% by 2030.

**Performance**

In terms of performance, residential sale prices registered marginal declines in H2 2018. Apartment and villa prices dropped 2% and 1% respectively. Similarly, rental rates softened 3% for apartments and 1% for villas over the same period.

Looking ahead, we expect rental rates and sale prices for both apartments and villas to continue softening over the next 12 months. This is particularly the case considering the large amount of supply expected to handover.

In the long-run, we expect the growth of other industries to act as a catalyst for labour growth and consequently residential demand. This is expected to reflect positively on the performance of the residential market.
DMA - Retail

Supply
The total amount of retail stock delivered in 2018 was approximately 36,000 sq m. This is a significant decrease from the 3-year average of 65,000 sq m. The small number of retail projects completed in H2 2018 increased the total stock to 1.1 million sq m of GLA.

Around 45% of this newly completed stock falls within the neighborhood category, 40% within community, and 15% within convenience. 2019 is expected to witness the delivery of an additional 136,000 sq m of retail GLA, with the majority of its supply within the community center category.

Performance
DMA's retail sector experienced further rental declines as vacancy rates increased to 6%. Average rents in super regional and regional malls declined 3%, while community centers recorded a 7% decline over the year.

While we expect further declines in rental rates over the next 12-months on the back of significant upcoming retail supply, the retail sector is expected to benefit from many reforms being implemented to diversify the country’s economy away from the hydrocarbon sector.

DMA - Hotel

Supply
No new hotel keys were delivered over the second half of the year in DMA, keeping supply levels stable at 7,800 keys as of year-end 2018. Assuming all projects in the construction pipeline are handed over on time, the market is set to witness the delivery of an additional 1,800 keys by 2020. Some of the notable projects within the pipeline include the Ascot Corniche, Hilton, and Movenpick Residences in Al Khobar.

A key trend observed in the hotel market across DMA is the renovation and upgrade of older properties. This includes the conversion of the Coral Hotel to Voco Al Khobar in 2019, under an agreement between InterContinental Hotels Group (IHG) and Mohammed Abdulaziz Al Rajhi & Sons Investment Company.

Under the same management agreement, refurbishment work is underway on the Holiday Inn Al Khobar Ulaya, which will see it convert from an independently run hotel to the first managed Holiday Inn in Al Khobar.

Performance
Hotel performance remained under pressure as average daily rates (ADR’s) declined 9% in the YT November 2018 to record USD 131, down from USD 145 over the same period last year. In turn, occupancy rates increased marginally to 49% over the same period. As a result, revenues per available room (RevPar’s) declined -7% to reach USD 65.

Looking ahead, the next 12 months are expected to witness further falls in ADR’s as more hotel keys are delivered to the market. Meanwhile, occupancy rates are expected to remain stable as DMA continues to attract a large number of domestic tourists due to its waterfront location. In the long term, the market is well positioned to leverage from the growth opportunities that Saudi Vision 2030 presents.

Source: JLL

Source: STR Global

Source: ATR Global
The real estate market in Makkah witnessed mixed performance in 2018. In the hotel market, while occupancy rates remained stable at 57%, room rates dropped as expansion works in the Grand Mosque only marginally increased the number of Hajj pilgrims in 2018. Elsewhere, the residential market continued to soften on the back of a strong supply pipeline. Competition in the retail market impacted performance particularly in neighborhood and community centres. The office market saw no notable deliveries thus restricting any declines in performance.
Makkah - Office

Supply
There was one small office completion in Makkah during H2 2018, adding 1,500 sq m of GLA to the market. This brings the total supply of office GLA to around 299,000 sq m as of year-end 2018. An additional 25,000 sq m of office GLA is expected to handover in 2019, with no office space currently scheduled for completion in 2020.

Looking further ahead, the quality of office stock in Makkah is expected to improve beyond 2020, as some of the large-scale mixed-use developments such as King Abdulaziz Road, Jawharat Makkah and Rua’a Al Haram are completed.

Makkah’s economic position is expected to strengthen on the back of government initiatives to increase the number of Hajj and Umrah Pilgrims, improve the city’s real estate offering through investing in large-scale developments, and enhance its infrastructure and connectivity.

Performance
The country-wide slowdown in economic activity in 2018 weighed on the performance of Makkah’s office market. Average rents recorded a marginal decline of 1% Y-o-Y to reach SAR 547. Meanwhile, market wide vacancy rates recorded no changes, stabilizing at 13% in the year-end 2018.

Looking forward, we expect office rents to remain relatively stable over the next 12 months on the back of limited future supply. In the long-run, however, performance is likely to improve as large-scale developments are carried out in line with Vision 2030. The opening of Al Haramain Railwaky which runs from Jeddah to Makkah is also likely to boost demand for office space.

Makkah - Residential

Supply
There were no notable residential completions in Makkah during the second half of 2018, leaving the total supply at around 388,000 residential units. Scheduled completions expected throughout 2019 include apartments in the second and third phases of the Jabal Omar Development, and a number of villas in phase 1 of Sumou District within Bawabat Makkah.

Despite expected delays in the handover of units, we remain positive in our outlook for the Makkah residential market. The government’s commitment to delivering a number of mega projects over the next 5-10 years, along with further investments in infrastructure, are expected to boost overall real estate activity.

Performance
The residential market continued to soften in H2 2018 with rents and sale prices declining on both a 6-month and annual basis. Apartment sale prices dropped 6% in H2 2018. On an annual basis, the decline was more significant, registering 10%. In turn, villa sale prices declined 2% in H2 2018, but remained relatively stable Y-o-Y.

Average apartment rents softened 1% and 3% on a 6-month and annual basis respectively. Villa rents declined further, recording falls of 2% and 5% on a 6-month and annual basis. The next 12 months are expected to see further declines in rents and sale prices of both apartments and villas, as supply continues to increase.
Makkah - Retail

Supply
2018 saw the delivery of 20,000 sq m of retail GLA with the majority of stock handed over in H2 2018. This brings the total stock of retail space to 1.3 million sq m by year-end 2018. An additional 67,000 and 20,000 sq m of GLA is scheduled for completion in 2019 and 2020 respectively.

The city of Makkah is currently undergoing major changes to improve its connectivity and increase its capacity to accommodate an expected 6.7 million Hajj pilgrims and 30 million Umrah pilgrims by 2030. This creates opportunities for the development of supporting retail facilities that target pilgrims from various countries.

Major projects accounting for a significant share of the future supply include the remaining phases of Jabal Omar and Maad Mall. These large-scale retail projects are likely to offer more in terms of shopping and appropriate entertainment, in line with expanding and diversifying the retail sector in the Kingdom.

Performance
Makkah’s retail sector exhibited mixed performance in H2 2018. Average retail rents in both the Markazia area and community shopping centres outside of the Markazia dropped 5% in 2018. This decrease in rental rates can be attributed to the increase in competition coupled with a slowdown in demand. As such, retailers are offering temporary incentives in the form of decreased lease rates and more flexible terms to retain tenants.

Rent in regional shopping centres rose marginally by 2% Y-o-Y in 2018. The stock of regional centres remains limited and so landlords continue to have the upper hand when it comes to charging higher rents.

As additional supply is expected to enter the market over the next 2 years, competition is set to intensify, thus exerting further pressure on rents particularly in neighborhood and community centers. Meanwhile, rents are expected to remain stable within regional centres and in the Markazia area.

Makkah - Hotel

Supply
There was one internationally branded hotel completed in Makkah in H2 2018, Four Points by Sheraton Makkah Al Naseem, adding 1,140 keys to the current stock. This brings the total supply of quality hotel rooms to 37,800 by year-end 2018.

An additional 12,300 keys are expected to hand over in 2019, dominated mostly by high-end hotel brands. 2020 is expected to witness the significant delivery of 34,700 keys, with more diversified stock being planned. With visitor demographics changing, hotels are expected to adapt their offerings to new types of travelers, including budget conscious millennials.

Makkah remains a key city for hotel operators, with many looking to enter the market for the first time. This is driven by Vision 2030’s target of attracting 3.7 million Hajj pilgrims by 2020, increasing to 6.7 million by 2030. The increasing pilgrim numbers provide significant opportunities for expanding the number of hotel keys as the sector benefits from increasing demand.

Performance
2018 was a challenging year for hotels in Makkah. With a marginal increase of 0.8% in Hajj pilgrims during 2018, the overall performance of the hotel sector softened in the YT November 2018 compared to the same period in 2017. This is largely due to restrictions on visas on the back of ongoing expansion works of the Grand Mosque.

While occupancy rates remained relatively unchanged at 57%, average daily room rates (ADR) dropped 9% Y-o-Y, registering USD 183 in YT November 2018. In turn revenues per available room (RevPAR) declined 9% to USD 104 over the same period.

Looking ahead, we maintain our positive outlook for the Makkah hospitality market supported by Vision 2030’s target of increasing the number of pilgrims and investing in the supporting infrastructure.
**12 O’clock**
Indicates a turning point towards a market consolidation/slowdown. At this position, the market has no further rental growth potential left in the current cycle, with the next move likely to be downward.

**9 O’clock**
Indicates the market has reached the rental growth peak. While rents may continue to increase over coming quarters, the market is heading towards a period of rental stabilisation.

**3 O’clock**
Indicates the market has reached its point of fastest decline. While rents may continue to decline for some time, the rate of decrease is expected to slow as the market moves towards a period of rental stabilisation.

**6 O’clock**
Indicates a turning point towards rental growth. At this position, we believe the market has reached its lowest point and the next movement in rents is likely to be upwards.
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