CUSHMAN & WAKEFIELD | CORE

# DUBAI MARKET UPDATE

Q3 2020

# MARKET SNAPSHOT Q3 2020

As with most global markets, Dubai's economy and real estate market reeled under the impact of COVID-19 since late March 2020 with widespread job losses and salary reductions seen in the private sector. While retail and hospitality sectors continue to face headwinds due to a slowdown in global tourism, residential and office asset classes saw enquiries and transaction activity levels rebound with higher volumes seen in Q3 2020 as buyers, tenants and occupiers adjusted to the new normal. Although this rise in transaction activity may be perceived positively, particularly in the residential market, it is most likely a release of pent-up demand created over Q2 2020. It would be interesting to see if these activity levels will be sustained over the near to mid-term as positive demand drivers such as lower interest rates, increase in loan-to-value ratios, retirement visas and fractional ownership of title deeds are implemented.

Despite a raft of demand drivers and higher transaction volumes, sales prices remain at a cyclical low, with many districts transacting nearly 35% lower than their 2014 peaks. With capital values now nearing the 2011 trough, we continue to see investor buyer interest remaining strong, particularly for competitively priced ready units. Historically, institutional investments have been limited in the UAE primarily due to the scarcity of investment grade stock, despite strong demand. However, we now see institutional interest piquing as many existing developers and corporates are making assets available for dispositions as occupiers look at focusing on core business lines and assets.

While residential supply handovers have slowed compared to initial forecasts, ample existing inventory and contraction in demand is expected to keep a supply overhang in the near to mid-term. This along with the lingering impact of COVID-19 on the overall economy is expected to further delay sales price and rental recovery while sharper rental falls compared to sales prices are resulting in yield contractions. Lower yields coupled with the new regulation on non-payment of service charges ensuing in legal issues and restrictions on new rentals and sales is expected to put further pressure on landlords with limited liquidity.

The office market saw increased relocation activity, particularly from SMEs and regional occupiers as most businesses adapted to market conditions. International corporates on the other hand are mostly continuing to work from home for the remainder of 2020 with their real estate decisions deferred to 2021. We expect a second wave of relocations in 2021 when these large corporates adjust their workplace strategies.

While the initial adoption of widespread work from home arrangement was met with enthusiasm, many enterprises are now witnessing that lack of social connections and no clear separation between personal and professional life is causing loss of productivity and lower levels of engagement. Although we agree that work from home will remain prevalent with hybrid models the largely accepted workplace strategy, the importance of the physical office is unlikely to be diminished as businesses will need common spaces to foster innovation, productivity and teamwork that are hard to sustain through remote working.

The UAE government has been very proactive and agile in navigating through this ongoing situation with unprecedented fiscal stimulus measures and policy reforms deployed to soften the impact on businesses while maintaining the highest standards of public health measures to curtail the spread of COVID-19. As we draw closer to the end of 2020, with signs of gradual revival seen across sectors, we remain cautiously optimistic of a stronger 2021 on the back of ease in global travel, potential availability of vaccinations and undoubtedly the positive impact created by the upcoming Expo.

## This publication

This document was published in October 2020. The data used in the charts and tables is the latest available at the time of going to press. Sources are included for all the charts. We have used a standard set of notes and abbreviations throughout the document.

# Residential Market

# Residential Supply

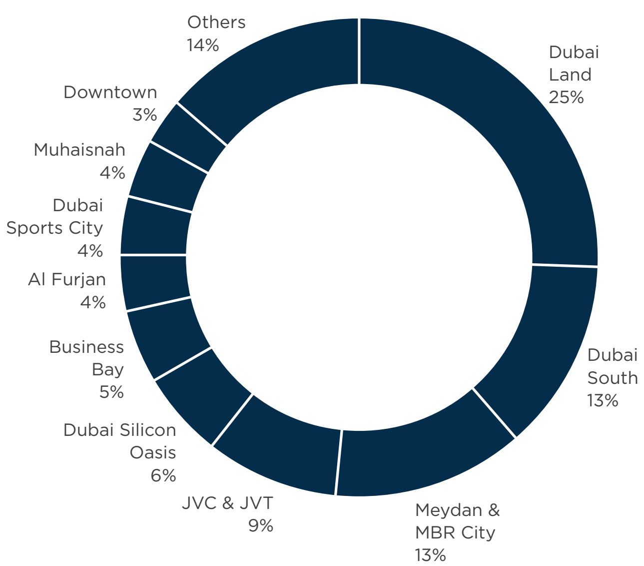
Dubai saw nearly 21,500 units come to market YTD 2020 (January 2020 to September 2020), bringing total residential stock to 571,500 units. Furthermore, there are over 10,500 units expected to be handed over in Q4 2020. Although handover volumes for 2020 are significantly lower than the initial forecast of 49,000 units at the beginning the year, 2020 will still see nearly 32,000 deliveries in total. While there are other factors at play such as lower realization rates over the past several years, we have seen the impact of COVID-19 cause a significant slowdown in handover volumes.

Major YTD 2020 villa deliveries include Noor Townhouses by Nshama in Townsquare, Pacifica by Damac in Akoya Oxygen (Dubailand), Casa Dora (Serena) Villas by Dubai Properties in Dubailand, Maple 3 by Emaar in Dubai Hills Estate and Arabella 2 in Mudon (Dubailand). Prominent apartment handovers this year include Rawda and Hayat Boulevard by Nshama in Townsquare, multiple deliveries by MAG in Dubai South, Merano Towers by Damac in Business Bay, Boulevard Point by Emaar in Downtown Dubai and One JBR by Dubai Properties in Jumeirah Beach Residences.

Dubailand and Dubai South are the leading areas by number of handovers YTD 2020, followed by Meydan and MBR City.

We conservatively forecast nearly 39,000 units for 2021, however, further downward revisions are expected on supply forecasts as they will inherently depend on buyer confidence as developers continue to adjust to ongoing market conditions.

### Supply Delivered by Area YTD 2020

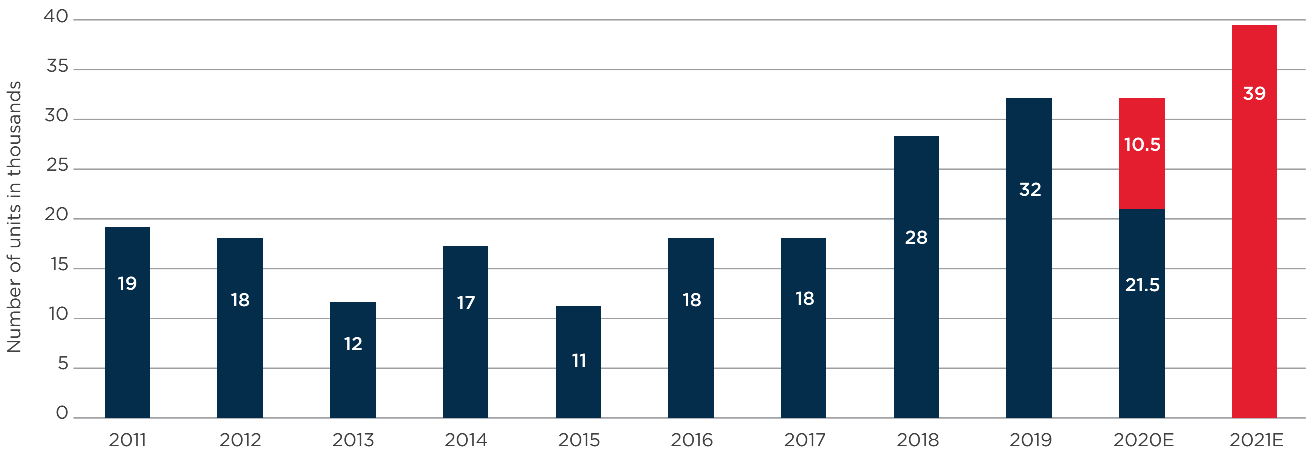



**571,500** units
Total residential stock in Dubai as of Q3 2020

**21,500** units
Delivered YTD 2020 (Jan - Sept 2020)

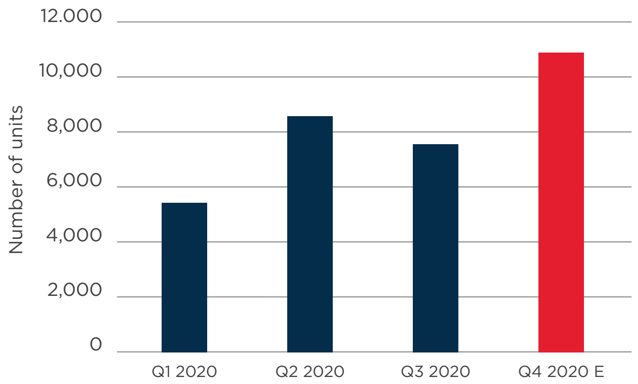
**10,500** units
Estimated to be handed over in Q4 2020

### Residential Deliveries in Dubai 2011 - 2021



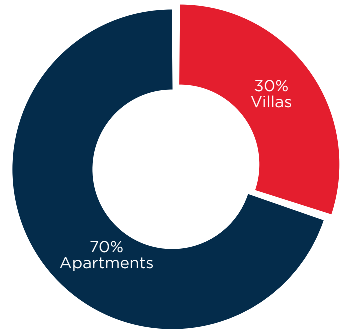

Source: Cushman & Wakefield Core Research

### 32,000 Estimated Residential Deliveries for 2020




Source: Cushman & Wakefield Core Research

### Apartment vs. Villa Deliveries YTD 2020



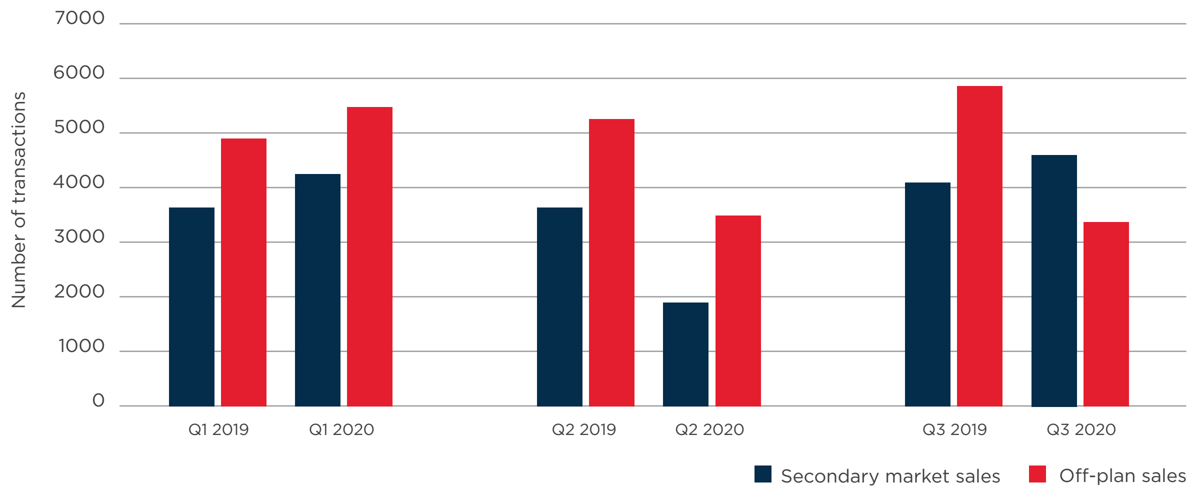

# Transaction Market Trends

Transaction volumes across the secondary market and off-plan market displayed year-on-year growth in Q1 2020, stemming from positive market sentiment with which we entered the year. As expected, due to lockdown restrictions and the overall uncertainty caused due to COVID-19, we saw a sharp decline in transaction activity levels in Q2 2020.

In Q3 2020, secondary market transaction volumes saw a quick rebound and marginally higher transactions than Q1 2020 volumes due to the release of pent up demand. However, off-plan market activity is facing an interim lag as buyers prefer ready units to avoid further uncertainty and delays that may be expected from the off-plan market.

As pent-up demand activity gradually stabilizes over Q4 2020, it would be interesting to see how transaction volumes perform as economic sentiment recovers on the back of a host of demand drivers initiated by the government to spur demand.

### Residential Transaction Market Trends




Source: REIDIN, Cushman & Wakefield Core Research

# Residential Market Performance

## Sales Market

Despite the rise in secondary transaction volumes, residential sales prices continue to follow a downward trajectory with almost all areas showing sharp double-digit year-on-year drops.

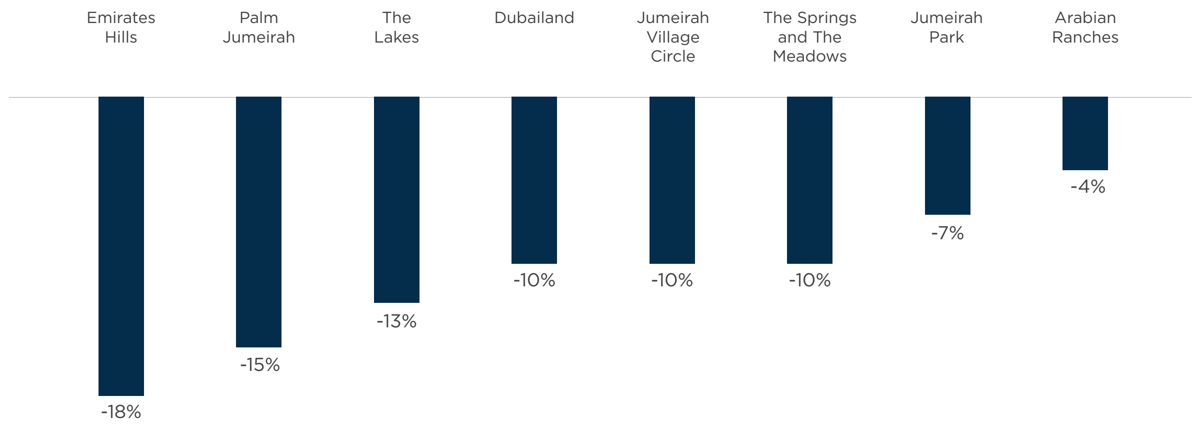
The government is implementing many demand drivers to spur recovery including attractive interest rates and the favourable loan-to-value ratio with an increase of five percentage points for first-time buyers which is expected to improve affordability in the secondary sales mortgage market. While this is a good initiative, contraction in disposable income, concerns of oversupply and caution is making some end-user buyers, who were otherwise primed to buy, wary of investing in current market conditions.

Other positive measures include fractional ownership of title deeds for hotel or serviced apartments. A fractional title deed refers to the division of the same unit into two or four fractional shares, each having its own title deed that may be sold, mortgaged, or transferred as would any other property. This is a good step to drive demand, with the launch expected to increase interest and cater to a wider base of investors with smaller entry ticket sizes while offering access to premium secondary home options. With tourism gradually opening up, this model bodes well for Dubai due to its historically large tourist base with buyers being incentivized to visit and stay for a longer duration as well as rent units as holiday homes.

The most important recent announcement is undoubtedly the retirement visa regulations which is expected to create long-term demand as more resident expats and international buyers choose the UAE to settle down, thus contributing to sustained population growth. In the mid to long-term, we expect this regulation to open new real estate asset classes such as retirement communities with integrated healthcare that are prevalent in other mature economies while retirees can also benefit from UAE's tax free environment for their retirement funds. With a warmer climate compared to most European markets, world class infrastructure, excellent air connectivity and proximity to countries with a higher population of aging residents, we expect strong demand from this demographic.

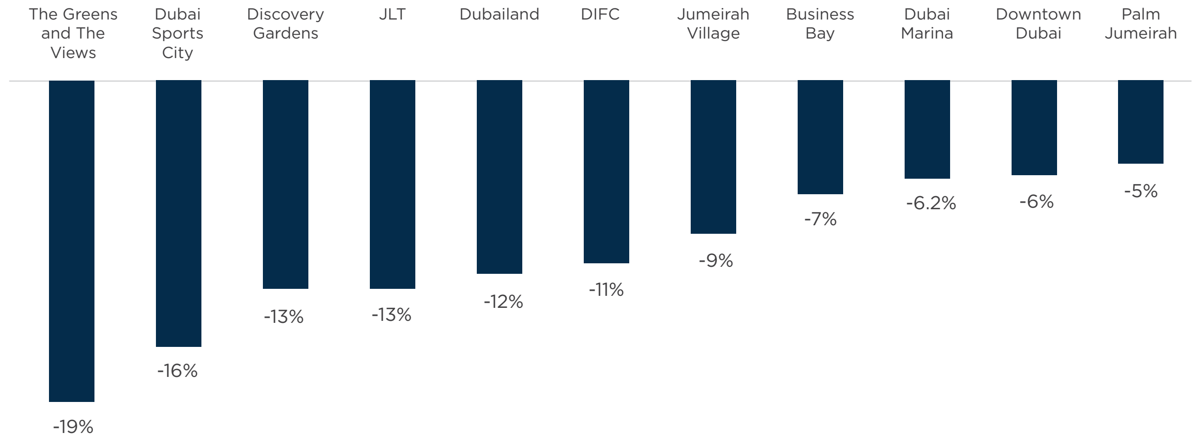
Sustained price drops have also piqued the interest of opportunistic buyers who are expected to take advantage of ongoing market conditions in this period of reduced liquidity. We are also witnessing some tenants who have a long term view, making a shift from renting to owning as a form of savings plan due to attractive entry points and easy access to finance. Therefore, we forecast continued market movement and steady transaction volumes, particularly in secondary homes, as many local and international investors are actively looking for competitively priced assets in the market.

**Villa Sales Prices Q3 2019 vs. Q3 2020**




Source: Cushman & Wakefield Core Research

**Apartment Sales Prices Q3 2019 vs. Q3 2020**




Source: Cushman & Wakefield Core Research

## New Service Charge Regulations

Dubai's Real Estate Regulatory Authority, as part of a series of regulatory reviews and improvements, has recently announced that all owners need to clear outstanding dues by October 2020. Non-compliance shall result in restrictions being imposed on renting and selling the property while legal action shall commence via the Dubai Land Department and associated channels.

This is a massive step forward in regulation after nearly a decade of Jointly Owned Property operations in the Emirate and one that will develop the industry moving forward. This announcement by the Land Department is a welcome step for Associations to have a clear pathway and regulatory support to pursue delinquent service charges which will improve confidence in the market and collections to protect assets and Associations.

Management companies will need to provide transparency on where the money has been spent and allocated in the communities and engage in communication with the owners to prevent legal cases. Legal cases need to be a minority and not the standard operating procedure as the Dubai Owners Association Market continues to mature.

We still believe that the best course of collections is transparency and communication with owners to ensure sufficient cash flow management of the Jointly Owned Property. Management companies will need to continue working with our communities and the regulator at Dubai Land Department to further develop the industry and the government's objectives for the future of Dubai.

## Rental Market

With many facing salary adjustments in the wake of COVID-19, we have seen household income contraction in almost all income brackets. This has resulted in considerable movement in the rental market with high enquiry levels witnessed in Q3 2020. This rise in interest is also partially attributed to the pent-up demand built over Q2 due to movement restrictions.

Faced with a new financial reality, tenants are either looking to find the current (albeit corrected) rental value of their property to help them negotiate rent reductions with their landlords or relocate and reduce their rental outflow.

While landlords may not completely agree with increasing tenant demands, most landlords are now willing to negotiate lower rents and flexible lease terms upon renewals to retain tenants. This has led many tenants to remain in their current premises as they have been able to achieve rental savings upon negotiations while avoiding uncertainty and additional moving costs.

However, depending upon landlord flexibility and a tenants' financial capability, many have relocated to achieve significant savings as rents have softened markedly over the last 12 to 24 months, with a particularly sharp drop seen over the last few months. Tenants can now find newer build and occasionally bigger units at similar or lower rents than what they were previously paying.

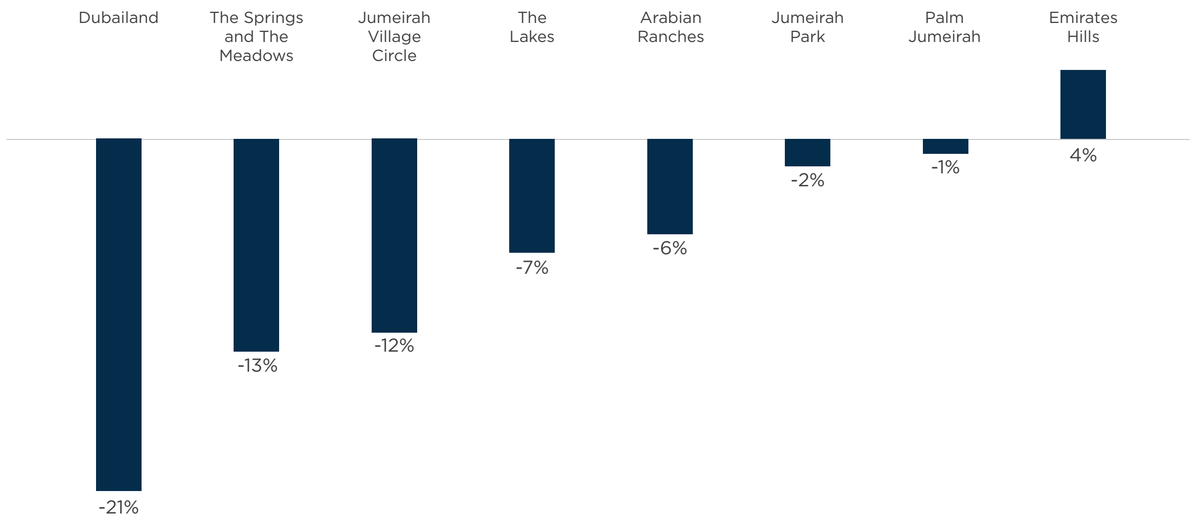
We have seen some tenants upgrade to bigger units or move from apartments to villas as the aftermath of COVID-19 has created the need for larger living and outdoor spaces, particularly for families with children, as they accommodate current e-learning and work from home arrangements. That said, most of these upgraders are actually paying lower than previous rents with very few going above their previous rental outflows. It is also interesting to note that moving from apartments to villas may at the outset offer lower rents, however, villas may involve hidden costs such as higher DEWA and maintenance charges which offset savings - something tenants should account for during relocation.

Some tenants on the other hand have downgraded or moved to outward locations which have seen new stock deliveries such as Jumeriah Village Circle, Dubai Sports City and projects in Dubailand to achieve major savings as tenants look to manage finances in the backdrop of widespread salary reductions.

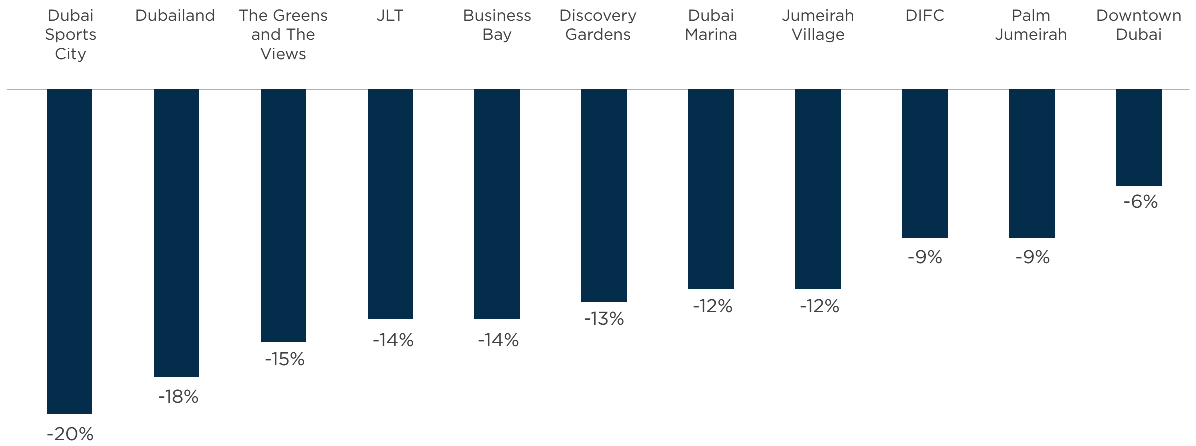
Rents in apartment districts in general have fallen sharper than villa districts with a higher share of apartment districts witnessing double-digit drops. The weakest performing apartment areas are Dubai Sports City (-20%), Dubailand (-18%), The Greens and The Views (-15%), and JLT (-14%). Villa communities witnessing the sharpest year-on-year declines are Reem-Mira and The Villa in Dubailand (-21%) followed by The Springs and The Meadows (-13%) and Jumeirah Village Circle (-12%).

With household incomes expected to remain under pressure, we foresee relocations to continue with a majority of tenants remaining price sensitive.

**Villa Rents Q3 2019 vs. Q3 2020**




**Apartment Rents Q3 2019 vs. Q3 2020**




Source: Cushman & Wakefield Core Research

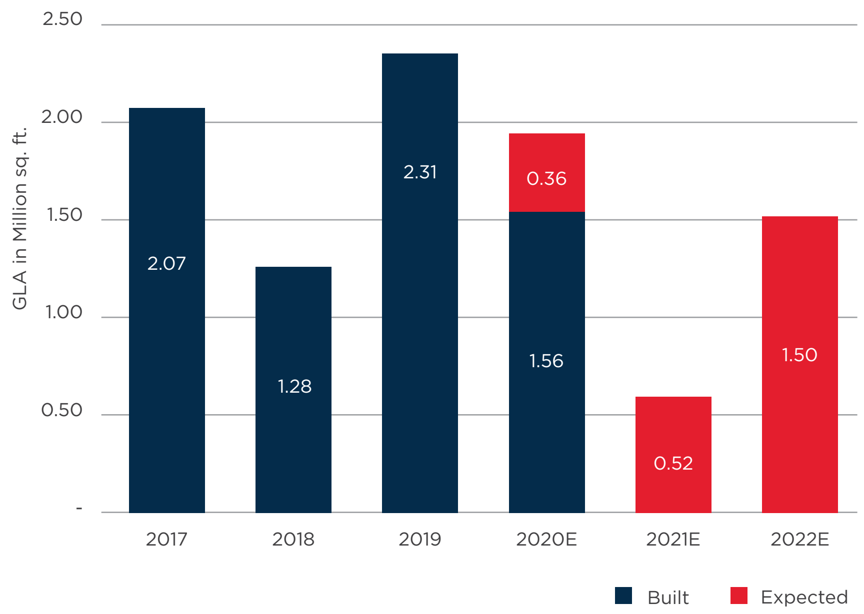
# Commercial Market

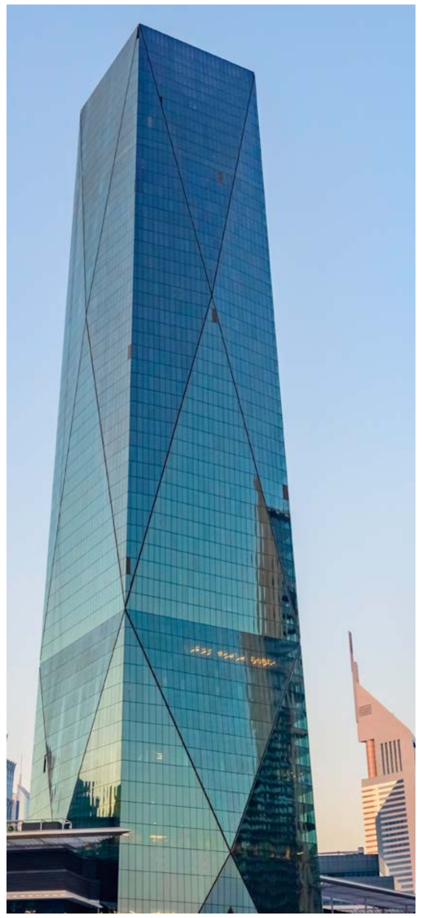
# Office Market Overview

## Office Supply

ICD Brookfield Place was the most prominent handover of the year, adding nearly 1 million sq. ft. of Grade A office space and bringing the total Dubai office stock to 104.9 million sq. ft as of Q3 2020. It is reportedly 41% occupied (preleased and under offer) with Ernst and Young being the first major anchor tenant occupying nearly 100,000 sq. ft. across 5 floors. While arguably the most premium Grade A building in Dubai, the handover of ICD Brookfield Place brings total Dubai office Grade A stock to nearly 34.3 million sq. ft. There haven't been any prominent Grade B and C deliveries over 2020 keeping the sector's stock at 70.6 million sq. ft.

**Dubai Office Supply 2017 - 2022**



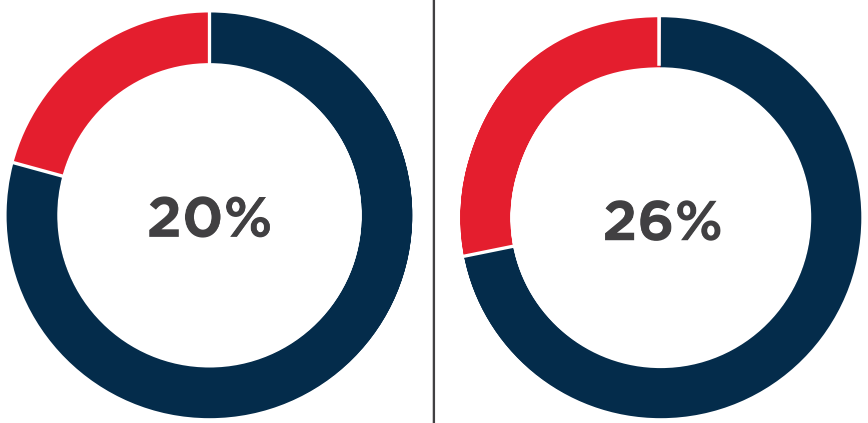



**Dubai Office Market in Numbers**

**104.9 million sq. ft.**
Total office stock

**34.3 million sq. ft.**
Prime office stock

**70.6 million sq. ft.**
Grade B & C office stock




Average prime office vacancy levels

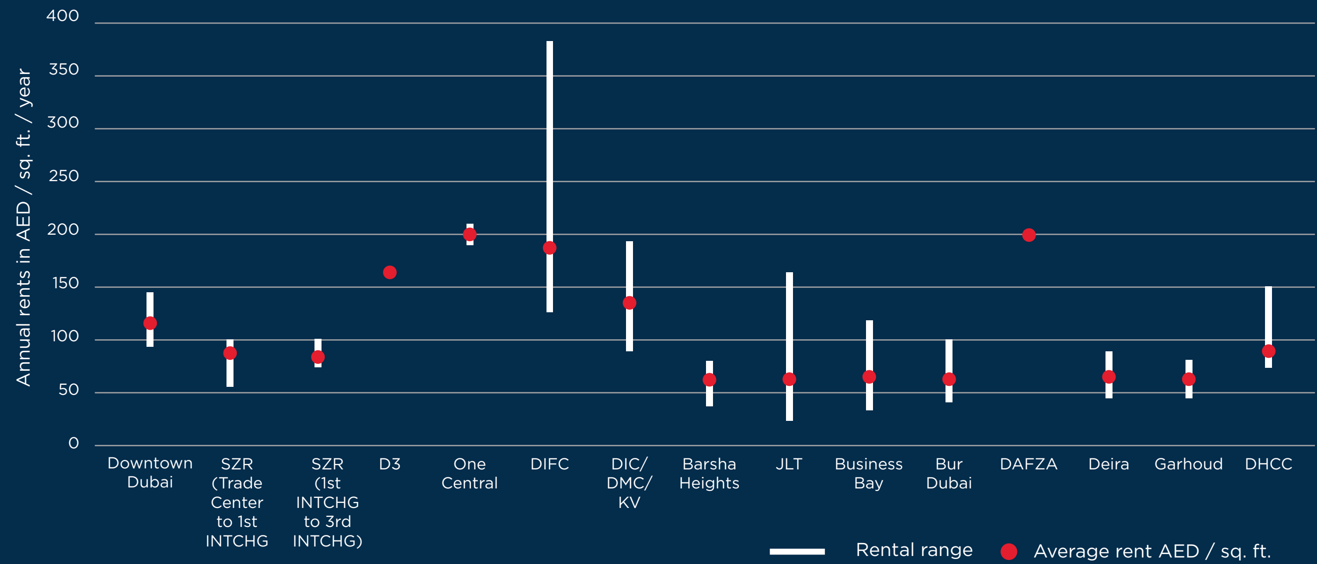
Grade B & C vacancy levels

Source: Cushman & Wakefield Core Research

# Office Rental Market Performance

Rents have been under pressure across all the fifteen districts we track. However, freezones with predominantly single owned office assets that are at relatively higher occupancy levels such as DIFC, Dubai Internet City and Media City, DWTC, DAFZA and D3 have shown resilience with nominal rental drops. Old Dubai locations such as Deira, Bur Dubai, Garhoud and Sheikh Zayed Road (Trade Centre to third interchange) have seen average rents fall in the range of 5 - 10% year-on-year. The weakest performing areas are the strata districts of Busines Bay and JLT displaying a steep 20% year-on-year drop in average rentals.

**Dubai Office Rents Q3 2020**




Source: Cushman & Wakefield Core Research

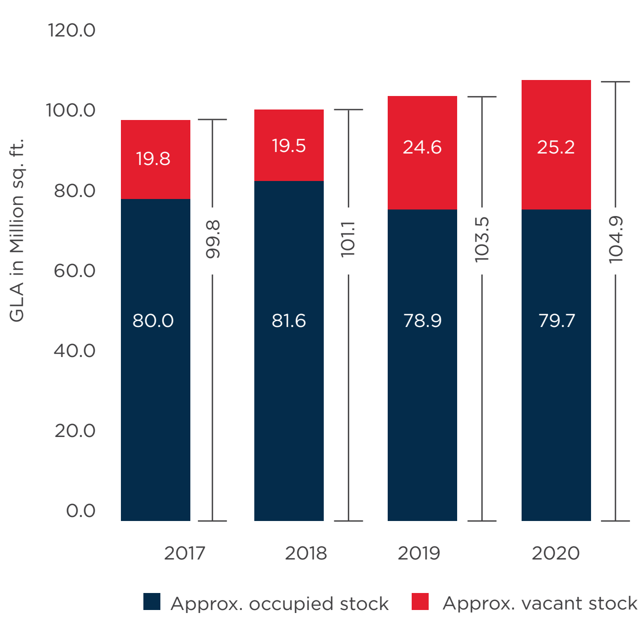
# Office Market Outlook

## Office Occupancy

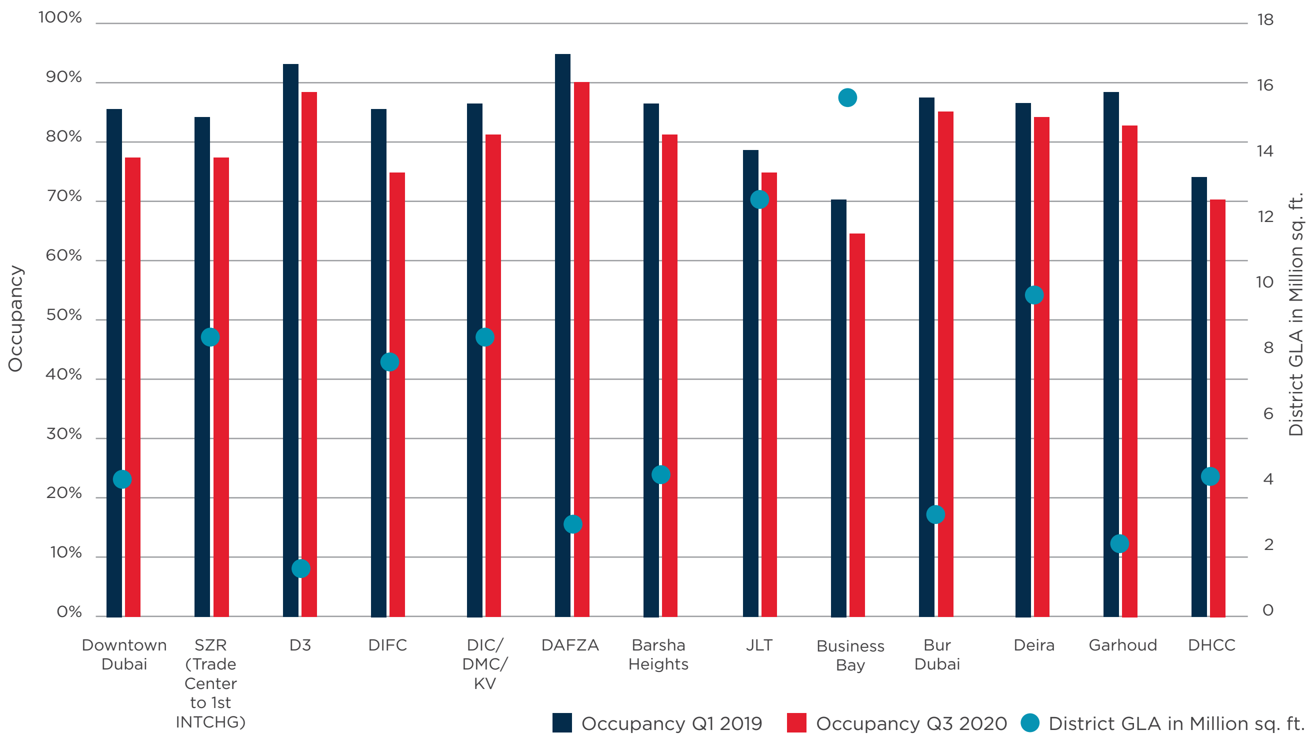
Occupancy levels contracted across the board as first phase expansions remain limited and most new demand stems from downsizing or relocation activity, keeping the net absorption negative. Downtown and DIFC both saw the sharpest decline in occupancy levels (10% year-on-year drop) as significant new stock was handed over, coupled with secondary stock brought to market as occupiers relocated within the district. Properties on Sheikh Zayed Road (Trade centre to first interchange) also saw their occupancy drop on an average of 8% year-on-year while the remaining districts in Dubai saw below 5% drops.

Of the total 104.9 million sq. ft. of office stock, nearly 25.2 million sq. ft. of stock is vacant, with the volume of vacant stock gradually increasing over the last five years. That said, we have seen a polarizing performance amongst Grade A and Grade B areas with most of the market witnessing a flight to quality with Grade A areas typically witnessing resilience in both occupancy and rental drops.

**Total Office Occupied vs. Vacant Stock**




**Office Occupancy Q3 2019 vs. Q3 2020**



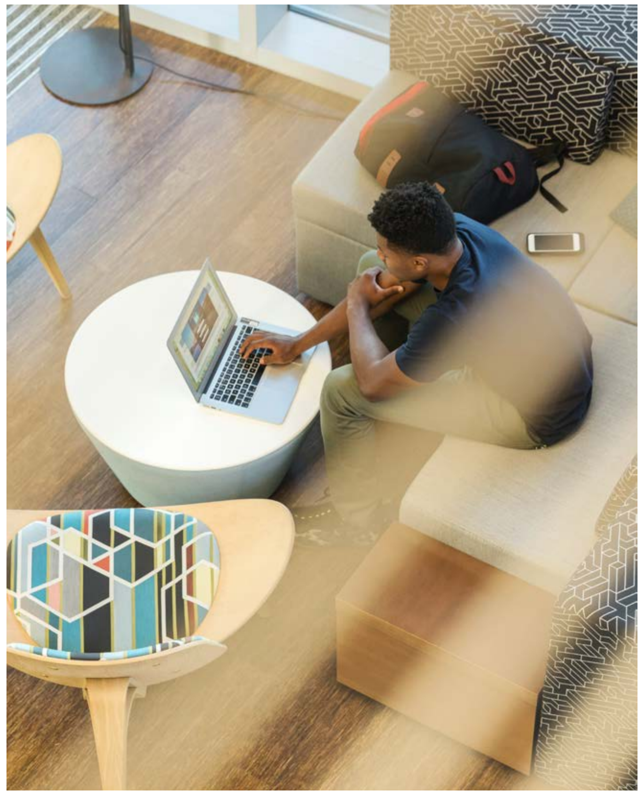

Source: Cushman & Wakefield Core Research

## Office Demand

In the wake of COVID-19, we are seeing two types of office market behavior emerge. A large section of demand is stemming from the SME sector which has seen the immediate business impact of COVID-19 and has been agile in restructuring staff and adjusting to market conditions. This reduction of staff coupled with the need to lower office rents to reduce capital expenditure is leading to a significant rise in office enquiry levels from this tenant segment. Most small businesses are looking to renegotiate with current landlords (some irrespective of lease term) or looking to move depending upon the scale of their staff and spatial contraction. This segment has constituted the majority of enquiries in the last few months with demand focused in the sub 2,000 sq. ft. area requirements.

Over the last few weeks, we are starting to see leasing enquiries from large local or regional occupiers as they gradually phase back into physical offices.

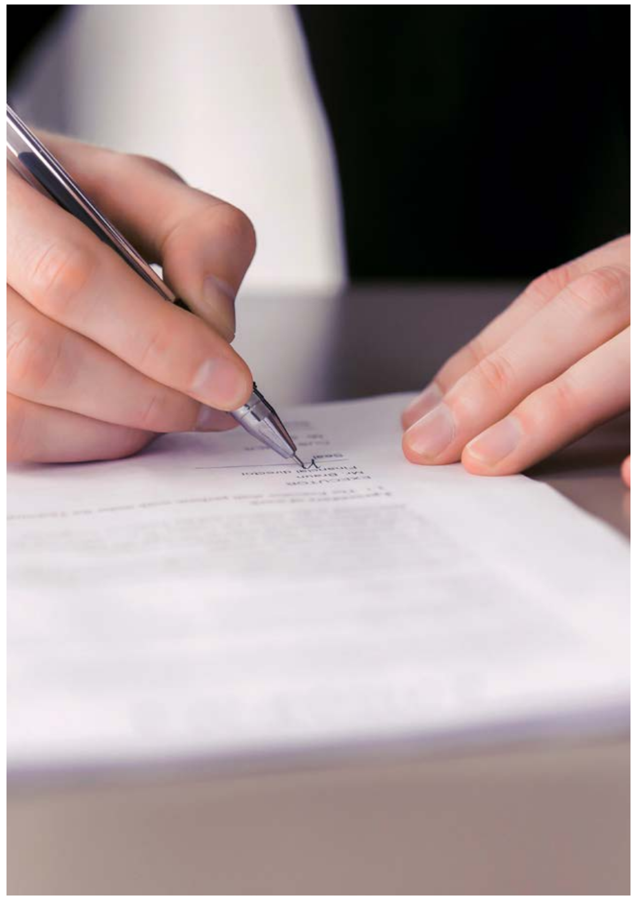
On the other hand, larger corporates and blue-chip occupiers are continuing to work from home or deploying hybrid models of work from home and phased office occupancy. These large occupiers are yet to finalise their workplace strategy and current and future spatial requirements, with many deferring real estate decisions to 2021 and taking a wait and see approach on business performance and growth.



## Office Trends

- First phase expansion is almost entirely limited with most demand coming from downsizing or consolidation activity where tenants are looking for economical options possible and immediate occupation. Most transaction activity is focused in the sub 2,000 sq. ft. size.
- We continue to see a strong trend of old Dubai occupiers migrating to properties located in Business Bay and Sheikh Zayed Road
- A few tenants are looking to upsize, mostly in media, healthcare, IT and technology sectors which have been relatively resistant to the impact of COVID-19 - albeit exploring upsizing options only if there are significant discounts on offer. Of the multinational clients that are looking to move, we have seen their global headquarters directing strict budget constraints on new leases.
- We have seen nearly 60% of small spatial occupiers (sub 2,000 sq. ft.) enquire and analyse the market and use this data to renegotiate with current landlords and remain in their present units. Most of these renegotiations are for a one-year term as tenants are deferring decision-making and not wanting to commit to longer terms due to business uncertainty. In other instances where landlords were unable to meet tenants' expectations resulted in tenants moving out to more economical units.
- We have also seen tenants prefer relocating within the same building or adjoining buildings where possible as they want to minimize the impact on staff. We have seen this trend in both single owned and strata assets within DIFC, Tecom(DIC/ DMC) and JLT.
- It is interesting to note that while landlords are becoming increasingly flexible, some are only being so if the company is financially strong. This has resulted in some landlords being cautious to offer discounts and a few have asked for credit checks or tenant qualifications on prospective tenants to safeguard themselves.

## Tenant Preferences



Most tenants are preferring 1 - 3 year terms with the option to renew, with smaller firms looking mostly at a one year term. This trend is also attributed to the change in international accounting regulations with lease terms over one year now viewed as a liability on a firm's balance sheet as per IFRS-16 (starting in January 2019, IFRS 16 introduced a single lessee accounting model and requires a lessee to recognize assets and liabilities for all leases with a term of more than 12 months)

We have witnessed a higher preference for fully fitted and partitioned offices or CAT-A finishes (finished ceiling and raised flooring) while shell and core stock has seen limited movement as potential tenants are hesitant to invest in fit-outs and want immediate occupancy. This decision driver has led well priced, maintained, fully fitted units to witness good absorption, particularly in strata markets such as Business Bay and JLT.

While proximity to the metro has always been a draw for potential tenants, we have seen this preference be of increased importance recently with most occupiers preferring units within a 10-minute walking distance from the metro. Thus, projects further away from the metro have seen challenges in take-up.

## Landlord Decision Drivers

Tenant retention remains the most critical issue for all landlords as many tenants are coming forward for rental negotiations irrespective of their lease term. Some landlords who were until now not aligned with market conditions are playing catchup and struggling to close transactions and witnessing long void periods.

We have seen strata landlords, particularly those with mortgaged units be very flexible and willing to undercut the market while single landlords are being relatively resilient. This is because most strata buildings have lower occupancy levels, making landlords eager to attract and retain tenants whereas single landlord buildings have typically witnessed higher occupancy levels and attracted bigger corporates, a distinction they wish to maintain. Single landlords, therefore, are unwilling to drop rents drastically while also wanting to minimize the impact on their valuations.

Single landlords also have standard lease terms that are largely uniform across their assets and thus are not flexible in providing offers or creative incentives compared to strata landlords. However, with ample new grade A stock available in the market, we have seen newer single owned developments be more flexible to increase initial critical occupancy.

In terms of typical lease terms, fitted options with 1 year lease term are now being offered with 1 month rent free while for 3 year lease terms for large spatial requirements rent-free periods range between 3 - 6 months and are dependent on tenant profile, condition of the fit-out and landlord flexibility. Landlords are providing attractive overall terms for long leases of 5 years, although very few tenants are going for such long leases with flexibility remaining key, with most tenants asking for early break clauses with limited penalties.

Office landlords have typically taken single check payments but are now flexible for up to four cheques while capital contribution to fit-outs are being offered in case of longer lease terms of 5 - 7 years for prominent or anchor tenants.

**HEAD OFFICE**
Ground Floor, Building 6,
Emaar Square, Downtown Dubai,
Dubai, UAE

+971 4 245 2100

**DMCC OFFICE**
Ground Floor, Indigo Tower
Jumeirah Lakes Towers,
Dubai, UAE

+971 4 245 2100

**ABU DHABI OFFICE**
Office No. RU 04, Abu Dhabi National
Exhibition Centre (ADNEC), Al Khaleej
Al Arabi Street, Abu Dhabi, UAE

+971 2 556 7778