MEED-Mashreq Business Leaders Club: Real Estate Forum

Outlook for Dubai Real Estate

June 2022

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Foreword

Experts at the Real Estate Forum analysed trends disrupting the property market in the coming year

Despite the multitude of challenges that have faced the market in recent years, Dubai's real estate sector today finds itself in a better position than many of its global counterparts.

Witnessing record-breaking sales in the past 12 months alone, several key segments in the sector have outperformed expectations of stakeholders and analysts alike, even as the market grapples with the impact of issues including the Covid-19 pandemic, fluctuating oil prices, inflation, supply chain crisis and, mostly recently, the Russia-Ukraine war.

The falls in Dubai property prices in 2019 and 2020 provided developers and investors in the emirate with the opportunity to reassess plans, balancing out oversupply as much as possible.

But has much of the recovery in 2020 and 2021 been driven by the success of Expo 2020 Dubai? And how much is the result of underlying factors?

On 22 March 2022, MEED and Mashreq Bank hosted an exclusive closed-door session to discuss the next phase of development in Dubai's burgeoning real estate landscape.

Bringing together leading industry figures, the MEED Mashreq Business Leaders Club: Real Estate forum discussed themes including market drivers, demand for investment-grade stock, and the rise of new asset sub-classes in Dubai.

The challenges are far from over. Investor trust, built by factors including quality of life, regulatory reforms and Dubai's response to the pandemic, is expected to keep the momentum going for some time.

But, looking beyond, the sector must now tap into areas including green finance and new ways to fund projects, to emerge as a globally attractive investment hub.

This report summarises key themes discussed at the event and presents opportunities ahead for the sector.

Dubai property to sustain demand in 2022

The real estate sector is expected to hold its growth trajectory and competitiveness across 2022

Improving demand is expected to hold property prices steady in Dubai in the near term, according to leading real estate experts based in the city.

Real estate experts at the forum note that the Dubai property market is well on its way to recovery in 2022.

A senior financier says that Dubai's real estate sector remains the bellwether for the local economy, underpinned by regulatory reforms, quality of life and most importantly, the successful handling of the Covid-19 pandemic.

Dubai is now seen as a safe haven for investors, reflected in the price improvements recorded since mid-2021.

According to real estate consultant CBRE, average home prices and rents increased by 9.3 percent and 8.3 percent, respectively, during the year. Price and rent improvements are expected to continue in 2022, according to a report by credit ratings agency S&P Global Ratings.

These improvements are being led by the fundamental strengths of the local real estate market rather than external factors, the financier explains.

"The rise in prices is not being caused by banks with cheap loans and loose lending practices, but by cash investors looking for real assets as a store of wealth and a hedge against inflation."

Lending rates have steadily increased in recent months as the UAE Central Bank increases interest rates, but favourable payment plans mean that the market remains affordable for now.

Moreover, the competitiveness of the Dubai real estate market makes it attractive as a borrower.

1.12%

IN PROPERTY VALUES

10%

IN TRANSACTION VOLUMES

Source:
Property Monitor, February 2022

"The interest rates rise in the short-term were pretty much absorbed by re-pricing," he says. "We're in a cycle of margin compression, which is offsetting any increases in interest rates, but that may not continue for too long."

The financier also expects the luxury real estate segment to perform well in the contemporary economic climate, with a strong pipeline of projects ensuring Dubai will comfortably be able to meet the expected demand.

However, the rising costs of new construction materials, supply chain slowdowns and higher fuel prices could dampen the delivery of projects. S&P's report, however, says developers are "somewhat protected" from higher raw material costs in the short term, as these costs will be borne by contractors.

New market segments such as retirement homes and old-age care homes are also expected to grow in relevance in the near future, says the financier, as government reforms make Dubai a more attractive residence for the long term.

"Significant cash is now moving into the UAE's banks, and we expect to see this go into real estate either through direct investments or investment trusts [REITs]."

Complementary factors

A senior spokesperson from a global alternative asset management firm notes that Dubai's handling of the pandemic was a gamechanger for the real estate market.

"Where Expo 2020 helped put Dubai on the map, it was really the way the UAE dealt with Covid-19 that positioned it as a safe and responsible city to live in," says the spokesperson.

This opinion is echoed by a regional mall developer, who adds: "Dubai marketed itself very well both locally and globally. It did well despite the crisis in many parts of the world."

A real estate analyst at the forum notes that demand for residential property has further grown over February 2022 as visitors from Russia and other ex-Soviet Union states flock to Dubai.

A monthly market report from real estate data platform Property Monitor shows that property prices rose by 1.12 per cent in February. Property values now stand at AED1,001 per square feet according to the Property Monitor Dynamic Price Index (DPI), the highest since January 2019.

Transaction volumes in February 2022 stood at 6,346, growing nearly 10 per cent on a monthly basis. Furthermore, a total of 12,119 sales transactions were recorded year-to-date, a 17.7 per cent increase over 2017, the previous best start to a year.

"These visitors are coming here not just to put their money in the market, but also to stay," says the analyst. "Most of the capital is for homes. These people want Dubai to be their first or second home."

In the week ending 25 March, Dubai Land Department (DLD) recorded real estate transactions worth AED6.8bn, while the week prior saw AED13.4bn in transactions.

DLD attributes these transactions to

AED 6.8bn

AED 13.4bn

PROPERTY TRANSACTIONS

Source:
Dubai Land Department, March 2022

"global city status, excellent infrastructure, world-class facilities and easy visa options".

Post-Expo legacy

With Expo 2020 Dubai culminating on 31 March 2022, the site is readying to transition into its legacy phase.

District 2020 is positioned as a 'smart, human-centric community' that will be part of the wider Dubai 2040 masterplan.

The district will repurpose nearly 80 per cent of the expo's self-built structures, including the Al-Wasl Plaza and Dubai Exhibition Centre. It will serve as a mixed-used community for residential and commercial tenants.

"The legacy of Expo 2020 was always on our mind," says a representative from Expo 2020 at the forum. "The infrastructure was built keeping in mind future needs, especially for Dubai South."

Global firms including Siemens and Accenture have already confirmed offices within the legacy project.

Meanwhile, 85 start-ups and small businesses will set up base as part of District 2020's global entrepreneurship programme called Scale2Dubai.

Competition from Saudi

Experts at the panel regard competition from Saudi Arabia in the real estate space with some cynicism.

"For investors, the Saudi real estate market is still immature," says the mall developer. "They are yet to prove if they can execute and deliver. They need to be at a stage where they can attract pure and serious investors."

The real estate analyst shares a similar opinion: "I don't see it as a risk to Dubai.

"Saudi Arabia's 30 million population makes it a critical market to address, but it is still very nascent. Achieving the quality of life an culture similar to Dubai will take a long time."

Dubai investors seek quality real estate stock

Global investors are calling for higher volumes of investment-grade stock in the city

Global alternative investment firms are keen to invest in Dubai's property market but are limited by the lack of institutional-grade opportunities and clear regulations.

Speaking at the forum, one such international investor says that there is a need for more quality stock that can bring more mature types of investments to Dubai in the form of institutional investments, pension funds and REITs.

With a long-term presence in the region with multibillion dollars' worth of exposure in the UAE alone, the investor says they have a view to form partnerships instead of pursuing "one-off" transactions.

"We are opportunistic investors. We don't invest for yield; we invest to do a lot of work. Unlike some of the other investors coming to the region, we take full equity risk here in Dubai. We want to win and lose with the government."

The investor says given the consistency recorded in Dubai over the past three to five years, the city's property market can shed its image of a "risky market".

With existing investments in office spaces and retail locations, the investor expects segments such as logistics hubs targeting Warehousing 2.0 concepts as well as multi-generational assets emerging as prime investment opportunities.

"Changes are taking place in the market, and institutions are recognising the opportunities that Dubai real estate offers," says the investor.

"Yields and valuations don't reflect the true situation yet, and that might be

> **“Changes are taking place in the market, and institutions are recognising the opportunities that Dubai real estate offers.”**

because people have not spent enough time to understand the market here. But it is changing.”

Delivering quality stock

A Dubai-based real estate analyst at the forum said the city is “reaching a stage where we’re running out of quality office stock”.

He adds: “It is harder and harder to secure Grade A and prime stock in the market for international tenants. A lot of businesses are now opting to set up headquarters in Dubai instead of just having a branch office.”

Stock being built now and in the future, the analyst adds, needs to be of better quality, which could be ensured through regulation. Moreover, the cost of such stock needs to be managed to make it more attractive for investors.

A developer attending the event cites financing and loan-terms, and capitalisation (cap) rates as challenges linked to delivering institutional-grade properties.

“Most loan terms sit around a 10-year mark, which is as comfortable as banks in the region are ready to go,” says the developer. “With counterparts in the US or Europe, we’re seeing 20- to 30-year loan terms, which makes a big difference in what a buyer can pay.”

Cap rates of 7 to 8 per cent are good for a developed market such as Dubai, but the developer notes that it falls well behind global markets.

“It’s a chicken and egg situation,” responds the global investor. “Developers were able to sell institutional-grade products at an attractive cap rate when they had the edge a few years ago. To get higher cap rates now, there needs to be more demand. And for that, you need more quality stock.”

Pension funds and REITs

The investor says attracting pension funds is another lucrative opportunity for Dubai’s market. Globally, investments in real estate serve as a way for pension funds to diversify their asset portfolios and distribute financial risk.

In the GCC, pension funds are the second largest category of institutional investors after sovereign wealth funds, according to the Asset Allocation Insights 2021 report by American asset management firm Mercer.

In response to market declines across 2020, GCC pension funds made investments into areas such as equities, listed infrastructure and real estate.

For instance, Abu Dhabi National Oil Company (Adnoc) signed a real estate partnership with Abu Dhabi Pension Fund in 2021, as part of which the fund will acquire a 31 per cent stake in Adnoc’s Abu Dhabi Energy Real Estate Company for $900m.

"Regional pension funds, like global ones, don't want to take the development risk. Instead, they want to assign their allocation to products with higher yields," says the investor.

"The question is how many assets are primed to attract such funds, or even available for sale?"

A similar challenge deters real estate investment trusts (REITs) in the region. The investor notes that while there is plenty of stock available, it is not always for sale.

"We need to develop an ecosystem that is self-sustaining and allows for mergers and acquisitions with institutional investors. As asset investors and developers, we want to create products for a future investor like government-related entities, pension funds or REITs."

Building trust

A mall developer based in the region notes that while financial institutions are more open to asset-based lending with residential projects, similar practices in the commercial and mall real estate segment are still nascent.

"You do not see the level of commercial transactions here that you might in more developed cities," he said. "Eventually, Dubai will get there because there is huge potential, but institutional investors are simply not there yet. You see them on the residential side, but not as much on commercial projects."

Dubai's current focus is on raising population numbers, which it can do through recently introduced legal reforms, long-term visas and lifestyle incentives, according to the mall developer.

However, the need prevails to build greater trust and transparency to attract more institutional investors.

"Emerging markets such as Dubai know that to be taken seriously, they need to tighten up the regulatory environment," says a senior financier representing a Dubai-based bank. "But frankly, having the environment in a healthier state will make it easier for all of us to do business. It sets out clear rules for everyone."

The financier adds that banks would be keener to support institutional investors with interest-only loans if borrowers are well-regulated.

"Majority of the investment grade REITs are already borrowing at around 40 per cent loan to value ratios as a policy," says the financier. "It is a risk-free and efficient way to raise capital and improve yields, but more clarity is required on the regulations front."

The financier notes that the lack of ways to recycle capital if things go wrong is also a major gap in the market.

"It's not about encouraging failure, but about saying that we need that kind of supportive ecosystem, including for banks."

Industry experts gathered at the MEED-Mashreq Business Leaders Club: Real Estate Forum on 22 March

Hyperlocal unlocks new real estate market

New real estate opportunities are emerging on the back of data-driven services

Real estate developers and landlords in Dubai should include space for 'dark kitchens' and 'dark stores' in premium districts, a forum of Dubai real estate developers has been told.

Speaking at the forum, a senior representative from a leading GCC logistics firm said that real estate developments around the world are evolving to meet the growing demand for community-based facilities such as 'cloud kitchens', 'dark supermarkets' and local data centres.

The rise in demand for these community-based services is opening potentially lucrative new investment opportunities for real estate developers and managers.

"There is real estate for people, which includes office, residential and commercial properties," he said. "And there is real estate for the stuff we consume, which includes e-commerce, food delivery, dark kitchens, warehouse. And then there is real estate for data, which is data centres."

The lines between these segments are blurring, he said. E-commerce fulfilment companies, food delivery aggregators, and data-centre operators are now seeking to scoop up locations that in the past would have been taken by traditional real estate development.

"They want to be in [premium] neighbourhoods like Dubai International Financial Centre (DIFC)," he said. "But developers and landlords in these districts

"These options were available before Covid, but no one was really thinking about scaling them."

haven't even begun to think about having a dark kitchen or dark store inside premium, grade A stock."

It is not only in Dubai where these trends are being seen. In mature markets, such as the UK, landlords are witnessing steep rises in industrial rents on the back of 'dark supermarkets' and 'ghost kitchens'.

Real estate consultant Knight Frank reports that for every GBP1bn of online retail sales in the UK, about 320,000 square feet of urban logistic space is required to fulfil the sales. It says that if e-commerce continues to spread at the current projected rates, some 12 million square feet of additional logistics space will be required in the UK by 2025.

The same trends are starting to emerge in the GCC's major cities, with Dubai, as usual, being at the leading edge. As a result, community-based facilities are set to be as an important new category of real estate asset in the region.

Dark hubs

The use of dark stores and dark kitchens in the region rose sharply during the Covid-19 pandemic in 2020 and 2021, when pandemic-led movement restrictions meant that people were limited to purchasing goods online.

"These options were available before Covid, but no one was really thinking about scaling them," says an attendee at the forum. "But now, they are becoming an increasingly important part of the social fabric of societies."

Dark stores are retail distribution hubs that cater only to online shoppers, a blend between a warehouse and a grocery store without in-store shoppers. Dark store staff prepare and pack online orders, which are then collected either by the customer or a last-mile delivery partner.

Although similar in principle to a traditional retail distribution centre, dark stores are located within urban and community centres rather than on the outskirts of towns. Such hyperlocal fulfilment locations make it easier to respond to quick delivery requests.

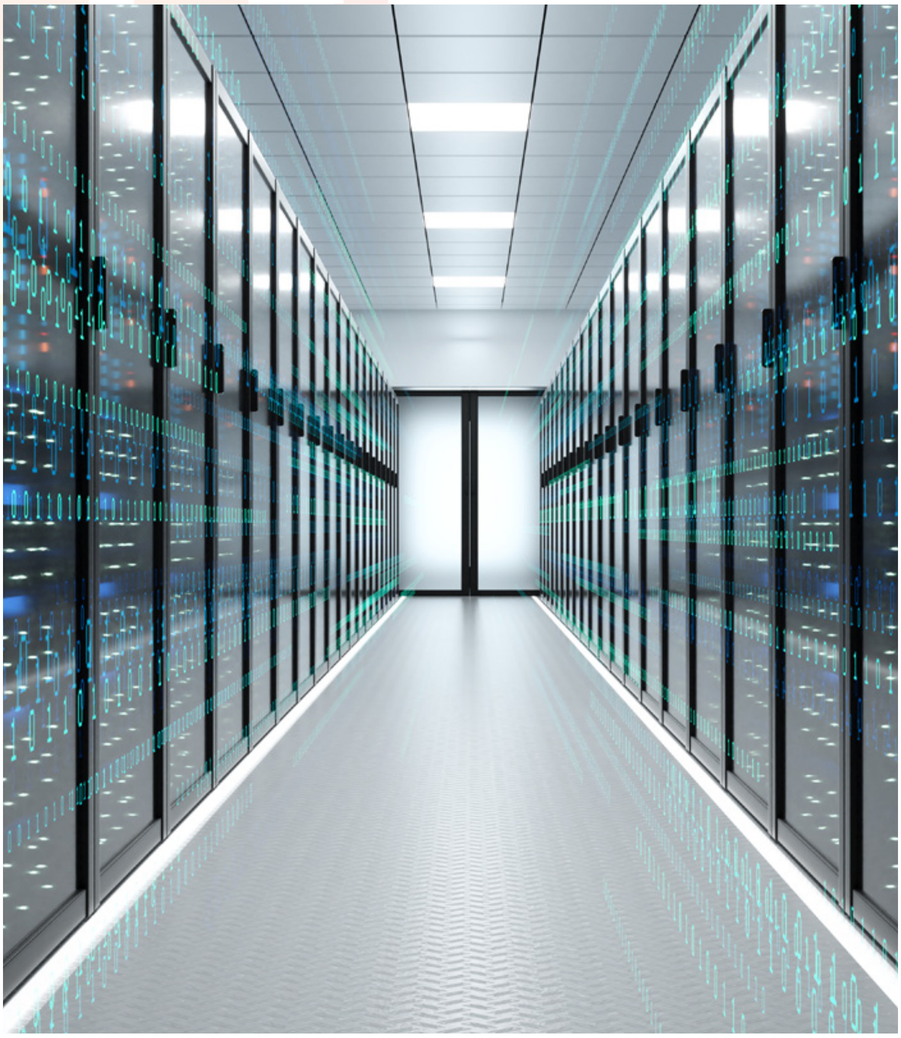
Dark stores also tend to be smaller in size compared to a large fulfilment hub and are often stocked to meet the needs of a particular locality.

In December 2021, UAE-based Careem

“Large-scale data centres can’t really be located in the city due to their size and the rents within urban hubs.”

GLOBAL MARKET FOR EDGE DATA CENTRES

Source: PwC



announced it was adding dark stores to support its grocery delivery arm, with the aim of having a 100 stores across Middle East within 2022.

Careem Quik is pushing to deliver grocery and household items in 15 minutes or less in select areas in Dubai, made possible through a dense network of hyperlocal dark stores and high-tech fulfilment management systems.

Dark kitchens or cloud kitchens operate in a similar fashion, with food prepared on behalf of several restaurants within a single space, for delivery apps only.

A Dubai-based analyst at the forum says that while developers have been looking at catering to these new players, it has been difficult to pin down operating models and to forecast returns when compared to a traditional commercial tenant.

Data centres

The rapid increase in demand for data and data-led services, has led to a surge in investment in data centres in the region over the past two years. Much of the demand for data centres is being driven by government directives to build smart cities.

In March 2022, Emirati property developer and founder of Damac Properties, Hussain Sajwani said he would invest over $1bn into building a data centres network across Europe, Asia, Africa and the Middle East, through Dubai-based digital infrastructure provider Edgnex.

The data centre market in the UAE is dominated by government-related entities, and operators such as Microsoft are looking to diversify their suppliers to reduce their risk.

Growing in relevance now are edge data centres, which are smaller-scale, local data hubs that can reduce latency and store data closer to the end user. A report by global consultant PwC notes that the global market for edge data centres is expected to nearly triple to $13.5bn in 2024 from $4bn in 2017.

“Large-scale data centres can’t really be located in the city due to their size and the rents within urban hubs,” he says a forum attendee from a global asset management firm. “Economics may not sustain them, unless there is a willing payer.”

Unlocking green funding options

Lack of incentivisation is limiting the growth of green financial instruments for real estate

While environmental, social and governance (ESG) considerations are a priority for many investors today, real estate developers in Dubai are not able to effectively tap into 'green' funds to finance their projects, according to leading real estate financier.

"Even as the world prioritises companies that are environmentally-focused, green lending remains nascent in Dubai," said Cyril Lincoln, executive vice president and global head of real estate finance & advisory at Mashreq Bank.

Speaking at the forum, Lincoln said that "part of the reason for that is the lack of tangible incentives for an investor or a lender to label their loans as green. Structurally, there is no pricing benefit".

The banker told leading figures from Dubai's real estate sector that while financial institutions are keen to drive green lending initiatives, there remains a lack of incentivisation and clarity when it comes to green regulations.

"Green finance is a theme that will only grow in relevance," said Lincoln. "But it is yet to be fully defined in Dubai and other markets in the region."

The global drive to tackle climate change is creating a surge in demand for green investment opportunities around the world, particularly in the property market where corporate buyers as well as individuals are

EUROPEAN EXEMPLAR

Serving as an example are efforts underway in Europe, where the European Commission is pushing banks and other financial institutions to promote ESG and sustainability through green finance as part of its climate neutrality strategy.

In order to streamline green lending, the EU Green Taxonomy came into force in July 2020, which helps define what activities and projects are classified as environmentally sustainable.

For banks specifically, the taxonomy can help:
• Increase transparency, consistency and comparability
• Strengthen risk management processes and support due-diligence practices
• Provide common language for banks and clients to communicate
• Provide reputational enhancement and increase business opportunities
• Build coherence with national and international standards

seeking energy-efficient, carbon-neutral properties. This is creating demand for green finance and ESG lending.

Recent reports from the UN and the World Bank said that green lending will play an essential role in reducing carbon emissions and tackling climate change with banks enabling this transformation through their role as "as investors, capital providers and capital intermediaries".

Enabling regulation

Green lending can offer benefits to both lenders and borrowers, especially from a reputational point of view. But it also comes with challenges, as transparency and continuous assessment are a core part of the process.

Appropriate regulations along with the standardisation of carbon footprint certification are needed to enable effective green lending.

"Debt providers recognise the role they have to play in enabling this change," said Lincoln. "But as is the case with conventional lending, we would benefit from having a framework that addresses aspects such as standardisation, risk assessment and monitoring practices. One way to do this could be a green license, for example, awarded to green lenders."

"It is equally important for banks to be actively thinking about their green finance strategy and to prepared for the regulations that are certain to come," said Lincoln.

Developing the relevant structures and mechanisms to support green finance in the GCC could unlock nearly $2tn in economic growth and more than 1 million jobs by 2030, according to consultancy Strategy&.

Strategy& advises governments in the GCC to focus on four priorities:

• Enact sustainability policies;
• Create a new green investment body;
• Strengthen capital markets; and
• Establish, or join, standard and transparent reporting mechanisms for environmental performance.

Efforts are underway in the UAE to exploring incentive mechanisms for financial institutions to develop and market sustainable products and services such as green deposits, green mortgages, green bonds or sukuk, green loans and green insurance or takaful, as highlighted by the UAE Sustainable Finance Framework for 2021-2031.

In November 2021, a statement was issued by the UAE Sustainable Finance Working Group (SWFG) on the sidelines of COP 26, emphasising that work was underway on building regulations relating to green finance in the UAE.

SWFG's roadmap includes three key actions: strengthening sustainability disclosure; fostering sustainability focused corporate governance; and developing a UAE taxonomy of sustainable activities.

"Progress is headed in the right direction, but will take time to fully bloom," said Lincoln. "But we are glad to be at the heart

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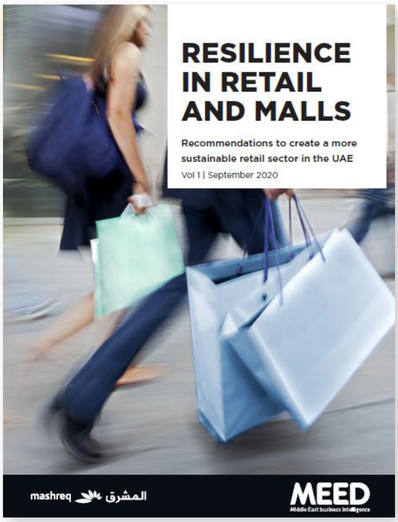

September 2020
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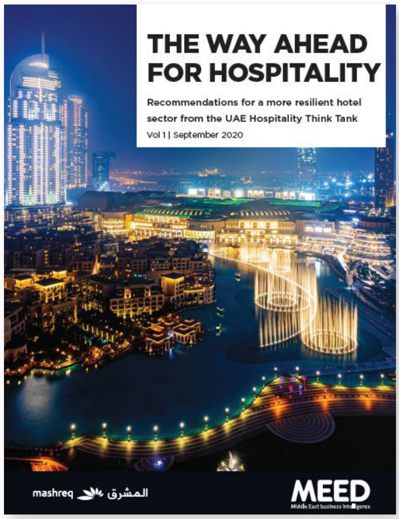
Resilience in Retail and Malls



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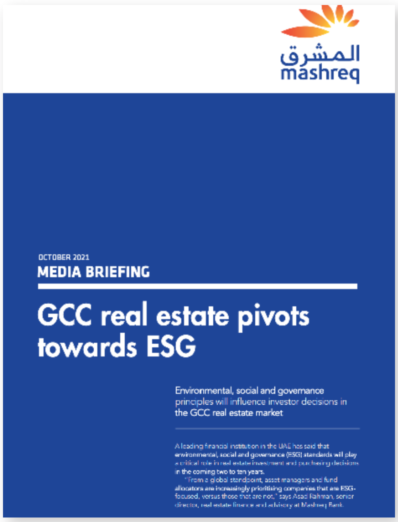

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Cyril Lincoln
EVP, Global Head of Real Estate Finance and Advisory at Mashreq Bank

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Established in 1967, Mashreq is the oldest bank in the UAE, with award-winning financial solutions and services. Throughout its 50 years' history, Mashreq has differentiated itself through innovative financial solutions, making it possible for its customers to achieve their aspirations.

Today, Mashreq has a significant presence in 11 countries outside the UAE, with 21 overseas branches and offices across Europe, the US, Asia and Africa. Mashreq launched its new Vision and Mission recently, outlining its commitment towards its clients, colleagues and the community.

In line with its vision to be the region's most progressive bank, Mashreq leverages its leadership position in the banking industry to enable innovative possibilities and solutions for its customers across corporate, retail, international, treasury and Islamic banking.

Mashreq is proud to be the first financial institution in the UAE to be awarded the Gallup Great Workplace Award for four consecutive years from 2014-17. Mashreq also continues to invest in recruiting, training and developing future generations of UAE national bankers.

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About MEED

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Attracting a key senior management audience through its content and activities, MEED is a media brand, publication and data business that covers a spectrum of services which inform, engage, connect and ultimately support our subscribers and partners in their business development and strategic growth.

Acquired by GlobalData Plc in 2017, MEED is now part of one of the largest data and insights solution providers in the world with the capacity to build global communities for our clients.

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