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Saudi Arabia:

Infrastructure, Construction & Real Estate

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MAP OF SAUDI ARABIA

Source : PRS Group

EXECUTIVE SUMMARY

Saudi Arabia is facing a serious economic and political crisis at the moment, with low oil prices threatening the very foundations of the Kingdom's system of governance and development. Crown Prince Mohammed bin Salman has taken drastic measures to ensure that the Kingdom is able to move forward with its ambitious development plans, including a plan to offer an IPO of Aramco shares, and, more recently, taking managerial control of Saudi Binladin Group and weighing a possible transfer of some of the giant construction group's assets to the state while its chairman and other family members are in detention. This move follows the Crown Prince's arrest of many of the Kingdom's top businessmen and is indicative of the state's intention to do whatever is necessary to maintain access to funds even in the face of low oil prices.

Indeed, investments have been on the rise. Saudi Arabia allocated US$ 14 bn to infrastructure and transportation in 2017, up from 38 billion riyals in 2016. The investment is aimed at advancing moves to wean the country economy off oil as part of the Vision 2030 plan led by the heir to the Saudi throne, Mohammed bin Salman. Under the 2017 budget, spending on transport and infrastructure developments has increased, rising from SR 37.6 bn (US$ 10 bn) in outlays in 2016 – up from an initial projected expenditure of SR 30.8 bn (US$ 8.2 bn) to SR 52.1 bn (US$ 13.9 bn) earmarked for this year. According to the Ministry of Finance's second quarter update released in mid-August, only 24% of the transport and infrastructure budget was spent in the first half of 2017, leaving SR 39.8 bn (US$ 10.6 bn) still to be spent this year.

Growth in Saudi Arabia contracted by 1.0% in the second quarter of 2017, highlighting the impact of the oil production quotas. The downturn was double the 0.5% contraction in the first quarter and is the first period of negative growth since the start of 2010 when the world was in recession. The Opec-sanctioned cuts in oil output caused the sector to contract by 1.8%. The outturn so far in 2017 will add to fears that the economy will enjoy much lower rates of growth than previously expected over the coming four years in the wake of cuts in oil production. The economy will grow by just 0.1% in 2017, the International Monetary Fund said in its October 2017 world economic outlook, cutting its outlook from the 0.4% it made just six months earlier. That is a further sharp cut from its October 2016 outlook of 2.0% and puts the economy close to stagnation. The fund now expects growth of 1.0% in 2018 rather than 1.3%.

Relative to the rest of the MENA region, Saudi Arabia undoubtedly exhibits lower political risk than its neighbours in North Africa and the Levant; however this does not guarantee that Saudi Arabia is completely insulated from the effects of the Arab Spring or political unrest in general. Recent reports analysing political risk in the MENA region noted that political risk in Saudi Arabia remains higher than in the past few years in light of tensions resulting from the wave of democratisation efforts engulfing the rest of the region, the status of the Shi'a minority, and lingering social tensions related to housing shortages and broader human rights abuses. In response to the first two concerns, the Saudi Arabian government acted swiftly, by drastically increasing public spending on the one hand as a means of quelling discontent related to unemployment and social inequality, while simultaneously suppressing pro-democracy demonstrations throughout the country, in particular in the Eastern provinces that are home to the country's Shi'a population. Furthermore, draconian moves by Crown Prince Mohammad bin Salman pose a wide-ranging threat to industry in Saudi Arabia, with prominent businessmen remaining in prison and the state moving to take control of major assets.

A total of US$ 4.3 tr is expected to be spent on construction in the MENA region over the next decade, representing growth of 80% to 2020. Experts anticipate a particular emphasis on the development of affordable housing. Following the global financial crisis and the Arab Spring, the market suffered throughout most of the region. US$ 1.6 tr worth of projects were cancelled around the region between 2009-2014, and US$ 23 bn worth of North African projects had been put on hold, including many in Libya, as of late 2015. Despite these initial setbacks, the infrastructure and construction sectors are poised for growth in the coming years.

INDUSTRY STRUCTURE

The infrastructure and construction industry encompasses a variety of products and services that together provide for the planning, architectural design, erection and finishing of modern structures. Infrastructure extends beyond the building of structures and into the foundational physical systems that construction is based upon. These systems are often, but not always, provided by the government, and include things like electrical grids, water and sewage systems, airports and telecommunications networks. The real estate industry is based on the sale, ownership, development and marketing of physical space. The real estate sector's activities span the spectrum from land evaluation, surveying and zoning; the sale and purchase of land between buyer and seller, often with the involvement of one or more intermediaries; the development of structures on the land by real estate development companies or individuals with the assistance of architects, engineers and construction professionals and with the use of raw materials such as cement and steel; and the provision of products and public goods to the site.

Saudi Arabia's infrastructure and construction industries are driven largely by state-funded projects, designed to boost the economy and to encourage diversification away from an oil monopoly. While the country's large-scale infrastructure projects are themselves often funded by oil revenues, the demand for improved public infrastructure as citizens become increasingly mobile between metropolitan hubs, improved power and water supplies as cities expand and rural areas develop as well as several plans for improved public transportation all keep industry developments in high demand. Demand is met through a series of state and private contractors, who supply labour and design as the population increases and demand grows. The Saudi Arabian real estate sector has been bolstered by high levels of foreign investment as the market has gained a reputation as a promising investment target. Investments have been largely funnelled into luxury residential compounds and lifestyle venues, leaving a gap in the market for low and medium cost residential properties. While the government has pledged to help close this gap, provision of sufficient units remains a challenge. The market for office and retail space, on the other hand, has become oversaturated, particularly in Jeddah and Riyadh, as foreign and local commercial builders attempt to capitalise on growth in the country's most important cities.

MARKET OVERVIEW

Saudi Arabia is facing a serious economic and political crisis at the moment, with low oil prices threatening the very foundations of the Kingdom's system of governance and development. Crown Prince Mohammed bin Salman has taken drastic measures to ensure that the Kingdom is able to move forward with its ambitious development plans, including a plan to offer an IPO of Aramco shares, and, more recently, taking managerial control of Saudi Binladin Group and weighing a possible transfer of some of the giant construction group's assets to the state while its chairman and other family members are in detention. This move follows the Crown Prince's arrest of many of the Kingdom's top businessmen and is indicative of the state's intention to do whatever is necessary to maintain access to funds even in the face of low oil prices.

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The broader transport sector represents a significant segment of the Kingdom's development pipeline, with a recent estimate suggesting that there are US$ 63 bn worth of sector-related projects in the pre-execution stage. Of the US$ 250 bn in unawarded contracts as of early 2017, transport accounted for 27% of total project volume, trailing only the energy sector (33%) and construction (29%). Although there had been some challenges to the government's development plans due to falls in oil revenue, the country remained the largest market for projects in the region, representing almost 40% of the GCC total. In the twelve months to Q1 2017, construction as a percentage of GDP contracted from 7% to 6.2% as backlogs continued to fall and awards in late 2016 failed to fill the gaps.

The infrastructure and construction industries in Saudi Arabia are among the largest in the Gulf Cooperation Council (GCC) region with high growth rates expected in the short and medium terms. As in most of the region's oil-rich economies, the Saudi Arabian government has played a central role in fuelling infrastructure and building projects through its five-year development plans, and since the 1970s has used its massive fiscal packages to develop highways, increase the country's power generation capacity and expand the country's system of seaports and airports. The 2000s witnessed a renewed emphasis on modernising existing infrastructure and developing new industrial projects, with the total value of construction projects expanding to a staggering average annual rate of 16.8% from 2006-2014.

Initially fuelled by demand associated with the country's booming oil and gas industry, which requires a comprehensive range of industrial structures and infrastructure, the Saudi Arabian government has recently made sizeable investments intended to boost the country's non-oil infrastructure. This includes heavy investments in healthcare, education, and infrastructure projects, including the creation and restoration of rail networks and roadways, in addition to significant construction expenditures in the residential housing sector. The government's current development plan will see over US$ 229 bn allocated for the 2015-2019 period. Despite lagging oil prices, which are expected to continue through 2016, the 2015 budget is Saudi Arabia's largest allocated expenditure to date, with infrastructure development projects scheduled through 2023.

As the government's budget, buoyed by oil revenues, continued to include development packages with massive expenditures on infrastructure and real estate, the country witnessed an unprecedented boom in construction projects, which grew at a combined annual growth rate of 16.8% from 2006-2014. In 2005, the total value of construction projects in Saudi Arabia had not yet reached US$ 200 bn; by 2010, that number had surpassed US$ 600 bn. Currently, the total value of construction projects in the Kingdom is estimated to exceed US$ 1 tr. This trend has been encouraged by the recent political unrest throughout the region, as governments across the Middle East and North Africa responded to the political developments of 2011 by expanding subsidies and development packages in an effort to curb the growing wave of discontent. Saudi Arabia led the way with a 2011 fiscal package amounting to 22% of the country's GDP intended to remedy the country's affordable housing shortage. While the 2011 plan's vision has remained largely unmet, further investments in the infrastructure sector have been effective in placating underlying social unrest within the country. Analysts credit the substantial increase in government investment with the improvement of the construction sector's annual growth rate from 2% in 2008 to a CAGR of 10.9% for the 2015-2019 period.

The government's development plan spanning 2015-2019 outlines investments worth US$ 258 bn in the real estate sector, US$ 126 bn in electricity, gas and water projects, and US$ 41 bn in transport and communications projects. Overall, US$ 1.1 tr is expected to be invested in the country' non-hydrocarbons sector by 2030. Significant development projects in the pipeline include over US$ 16 bn worth of water and agriculture related infrastructure, including US$ 6.1 bn to fund the creation of dams, desalination plants and water treatment networks. Within the infrastructure and transport sector, US$ 8.9 bn has been allocated to fund nearly 2,000 km of new roads, airport upgrades and expansions, railways, seaports and infrastructure projects at Jubail, Yanby and Ras Al-Khair. This is in addition to over US$ 30 bn in transport infrastructure projects currently underway. One of the largest construction projects currently in the pipeline is the Khozam Development in Jeddah. Worth an estimated US$ 13.3 bn, the mixed-use development aims to promote economic development within the area.

Overall, the outlook for the Saudi infrastructure and construction sector remains strong due to the country's 2015-2019 National Development plan that will see significant investments within the country's transport, real estate and basic infrastructure sectors. Although the sustained drop in oil prices has negatively impacted the economy in recent years, the country's significant reserves will ensure that spending on infrastructure and capital projects will continue in order to achieve greater economic diversification. As the largest construction market in both the GCC and greater MENA region, significant growth is expected to continue within the country's infrastructure and construction sectors in the near term.

Major Infrastructure Projects

Project Name	Size (USDbn)
Sudair Industrial City	40.0
Jazan Economic City	27.0
King Abdullah Economic City	27.0
Ras Al Zour Economic City	25.0
Jazan Industrial City	17.0

Project Name	Size (USDbn)
Saudi Landbridge	6.6
Makkah, Madinah Rail Link	6.0
Mina, Arafa Railway	5.3
King Abdulaziz Int. Airport Devp. Project	5.3
Ras Al Zour Port	0.7

Source : Global Research

Transport Infrastructure

Transport infrastructure was identified in both the long-term Vision 2030 for economic and social development and the medium-term National Transformation Programme (NTP) as vital to the broader economic overhaul. The NTP also calls for greater private sector contribution in developing and operating rail projects, targeting a 50% input by 2020, up from 5% currently. Through five-year development plans, the government has sought to allocate its petroleum income to transform its primarily oil-based economy into that of a modern industrial state. The government's first two development plans, spanning much of the 1970s, emphasised infrastructure with impressive results, as the total length of paved highways tripled, power generation increased 28-fold, and the capacity of seaports expanded tenfold. By the end of 1999, Saudi Arabia had built around 150,000 km of roads, which constitute the major arteries providing passage between urban and industrial centres. Jeddah, Mecca, and Medina in the West are linked to Riyadh and to the oil fields located in the Eastern Province by the trans-peninsular highway, while the Tapline road provides a link between the gulf coast and the Jordanian border. While the relative share of government expenditures on infrastructure declined throughout the 1980s as oil revenues abated and spending on education, health, and social services took precedence, the sector still remains a major source of demand for construction activities in the present. In gross terms, the infrastructure sector in Saudi Arabia represents approximately 8.6% of GDP, or around US$ 53 bn a year.

Transportation areas such as aviation, railways, roads, seaports, and logistics are expected to see major developments, capacity enhancement and expansion in order to accommodate growing demand across the region. Metro schemes will take the spotlight among other investment projects, as the government awards tenders in Jeddah, Dammam and Mecca. Notwithstanding the aforementioned advances in modernising the country's transport infrastructure, public and private expenditures in this segment continue to expand, with private sector growth exceeding 11% in 2014. In its 2016 budget, the Saudi Arabian government has allocated substantial funds for the creation and renovation of new and existing roadways, rail networks, and road systems. US$ 30 bn has been allocated for the construction of public transport systems in the city centres of Mecca, Jeddah and Taif. In an effort to deal with traffic congestion related to pilgrimage tourism, the city of Mecca will receive an additional US$ 18 bn for the creation of four metro lines, 88 stations and a high-speed bus network for pilgrim transport. Additionally, despite being the country's capital, Riyadh has almost no existing public transport. US$ 22.5 bn has been allocated for the creation of a metro line, 176.5 km of railways, and 85 stations. This project has an expected completion date of 2019. Opportunities for growth also exist in Saudi Arabia's greater rail network, with spending expected to reach US$ 79 bn by 2025. Saudi Arabia plans to significantly improve its rail network by adding 3,900 km of track through three major railway projects. This includes a US$ 13 bn rail line linking Mecca and Medina, while work on a US$ 1.7 bn mass rail transit system for the holy city of Mecca began construction in 2013. Additionally, the country plans to triple the size of King Khalid International Airport in Riyadh over the next three years in order to increase its capacity from 12 mn to 24 mn passengers. Additionally, the first phase in the expansion of the new King Abdulaziz International Airport in Jeddah will be completed in 2016. Phase one of the expansion will bring airport capacity up to 35 mn passengers annually in 2016, while completion of the second phase will bring annual passenger capacity up to 47 mn.

The volume and scope of Saudi Arabia's current transport and infrastructure projects prepare the industry for an expansive future over the next several quarters, with significant growth expected in most areas. Saudi Arabia plans to seek bidders for the construction of a 1,000-mile railroad linking the Red Sea with the Persian Gulf as early as the end of this year, signaling the go ahead for a long-delayed project seen as vital to reducing the economy's dependence on oil. The so-called Land Bridge line will shave around three days off the current five-day journey time for shipping seaborne freight around the Saudi coast, while improving links to Riyadh, and Jeddah, the nation's two biggest cities. Contract tenders will be issued at the end of 2017 or early in 2018 following an encouraging response to an invitation for expressions of interest. In July 2017, the Saudi Railways Organisation (SRO) conducted the first complete trial run of the Haramain High-Speed Rail. The project connects Jeddah to Medina in just 90 minutes, at speeds of up to 330 km per hour. The next stage of the US$ 17 bn Makkah Metro is expected to be put to tender either by the end of this year or in early 2018. The move to speed up the Makkah Metro project, along with proposals to revitalise development of a 149-km metro network for Jeddah, shows that interest in big-ticket transport projects is returning after two years of constraints due to fiscal tightening.

Energy and Water Infrastructure

While the Saudi government has expressed a focus on transport, housing, healthcare, and education for the current funding period, energy and water infrastructure remain important areas of development. The high oil revenue environment has spurred a number of energy development projects in Saudi Arabia. The private sector is poised to invest US$ 79 bn in private-sector energy projects in the Kingdom in coming years geared toward expanding the country's power generation capacity and transmission network over the next 10 years. In 2015 the government allocated an estimated US$ 6.1 bn to increase the Kingdom's water resources, funding new projects such as dams and desalination plants, along with establishing deep aquifer wells and improving water treatment networks. Other anticipated investments in infrastructure projects include a US$ 12.3 bn investment by government-owned National Water Company (NWC). The investment will expand the coverage of water services across major cities of the Kingdom. NWC will also invest in a new sewage treatment capacity in Riyadh for increasing the city's water reuse capacity.

Industrial Infrastructure

While reports suggest that the Saudi Arabian government has recently shifted its focus from investing in big industrial cities to further expanding the country's infrastructure and affordable housing supply, industrial property development still accounts for a sizeable portion of construction activities currently in the pipeline. According to the head of the Saudi Industrial Property Authority (MODON), the government still seeks to increase the number of industrial cities from 22 to 40. Specifically, MODON will oversee the completion of four industrial cities in Sudair, Al-Kharj, Dammam, and Jeddah by 2019. Construction activities at the cities of Al-Kharj and Sudair are well underway and will require total investments of US$ 320 mn and US$ 213.3 mn, respectively. Other large-scale industrial projects include plans for the Jubail 2 City, which will specifically serve the petrochemical production industry and include expansions to the surrounding port and railway network, in addition to the Ras Al-Khair Industrial City for Minerals and Metals, also located in Jubail. While the government has played a central role in spearheading the development of these industrial cities, six of which constitute a mega projects worth approximately US$ 70 bn, the private sector is expected to take the lead in the industry in 2015 as opportunities for public-private partnerships (PPPs) and build-own-operate-transfer (BOOT), as well as different categories of operations and service contracts, proliferate.

Construction Materials

Construction activities have increased significantly since the announcement of the 2010 and 2015 development plans, which put a heavy focus on the renovation and construction of a number of key infrastructure projects. Due to the rapid growth of virtually all sectors within the infrastructure and construction industries, a significant shortage of skilled labourers and building materials has resulted. Large-scale projects in both Saudi Arabia and neighbouring countries have translated into increased material costs, despite the country benefitting from a well-established supply chain. The Kingdom has historically controlled price fluctuations of basic materials such as steel, cement and concrete through legislative action, although strict import measures have resulted in widespread delays and requests by contractors to postpone the Saudisation of the industry until development deadlines are met.

Saudi Arabia currently has the largest construction market in terms of amount and value, with over US$ 30 bn in projects awarded in 2014, while Qatar had US$ 26.2 bn. This has resulted in widespread materials shortages, with limestone, steel, aluminium, tin, and cement experiencing significant shortages. Cement demand rose by an estimated 40% in 2015 to 145.4 mtpa (metric tons per annum), almost double the 81.5 mtpa consumption levels in 2008. This has prompted domestic manufacturers to expand production quotas up to 50% for the 2015-2019 period. Saudi demand for construction materials of all kinds is expected to skyrocket in the short term as the majority of on going projects that started in the 2010-2014 development period have completion dates between 2018 and 2023, with more projects scheduled for the current development period.

Real Estate

Although Saudi Arabia's real estate sector has historically lagged behind its GCC neighbours, today real estate is one of the fastest growing and healthiest industries in the country and among the most competitive in the region. Residential, hospitality, retail, and commercial space are the most prominent segments in the sector, although each segment has developed in different directions and at varying rates. The hospitality segment has experienced sustained growth, reinforced by market potential in budget accommodations and government backing to increase tourism. The residential segment is the strongest and is accelerating at a substantial rate with full backing from the government, due to a booming population and a significant housing shortage, while the retail and commercial sectors continue to benefit from rising demand and sustained government investment, respectively.

As real estate markets in the Gulf continue to feel the pressures of demand dictated by burgeoning populations, recent years have seen a number of major projects developed or added to the pipeline. Saudi Arabia's population has quadrupled to 31.5 mn over the past 40 years, while 60% of its citizens remain under the age of 30. Just 35% of Saudis currently own their own homes due to high land prices and the absence of a developed mortgage financing market. Land prices, particularly in urban areas, are historically inflated, as even middle class citizens tend to invest their savings in land in the absence of a developed treasury market. This has resulted in land costs accounting for up to 60% of total property value, compared to the global average of 25%.

Additionally, there is an extremely high percentage of "white land," particularly in the country's largest urban centres of Riyadh and Jeddah. This "white land," which can account for as much as 65% of total land area in some cities, sits undeveloped as real estate owners hold property as a store of value or trade it for speculative profit rather than perusing development. In response to this trend, the government is in the beginning stages of implementing a tax that would apply to the millions of acres of undeveloped land, thus incentivising landholders to either build on or sell their holdings. Additionally, the recently introduced mortgage law aims to improve the regulatory environment for banks to lend against secured property, making it easier for homebuyers to secure loans. Introduced in 2015, the law was revised in 2016 to loosen credit requirements and reduce the minimum down payment for a home from 30% to 15% of its total value.

According to statements made by the Ministry of Commerce and Industry, in order for the local housing market to satisfy demand over the coming few years, 1.5 mn new housing units would need to be constructed by 2020, which at the current rate, translates to an average annual addition of over 375,000 units per year. The steady rise in demand for housing meanwhile is concentrated in the medium income segment of the population. These demographic pressures combined with the supply gap in affordable housing led to a pledge by King Abdullah bin Abdul Aziz Al-Saud's government in March 2011 to invest in the construction of 500,000 homes by 2015 at a cost of US$ 66.7 bn. Despite this pledge, government failure to secure sufficient land for the project coupled with bureaucratic delays has resulted the construction of less than 350,000 units to date.

Since 2004, the country's office space supply has also been steadily expanding, although industry reports indicate that supply is beginning to outstrip demand in this segment. Saudi Arabia accounted for the highest share of commercial projects completed in 2014 totalling US$ 6.8 bn, although this has created an oversupply within the commercial real estate sector in the short-term, resulting in a drop in rents and an increase in vacancy rates in certain cities. Expansion in the finance, real estate and business services sectors has helped drive office space occupier demand across Jeddah, Riyadh and the Eastern Province, particularly for prime office space, which remains in short supply across the Kingdom as a whole.

In 2014, prime office rents in Jeddah rose by 9%, while rents in Riyadh rose by 5%; this compares favourably with regional neighbours as office rents in Dubai rose also rose by around 5%, while rents in Bahrain fell by 5%. Riyadh continues to develop as the foremost commercial centre of Saudi Arabia as it houses the majority of financial and banking institutions. Future development projects are expected to the raise the standard of commercial offerings as parking and ease of access become increasingly important to occupiers.

As the government embarks on an initiative to increase the number of white-collar jobs available to the local population, a number of new building projects are in the works for both the private and public sectors in an attempt to keep up with future demand. Such projects will see increased collaboration between the Saudi construction sector and leading global technology firms such as US-based DuPont Building Innovations, as the Kingdom seeks to modernise the country's residential and commercial real estate by making its buildings more cost and energy efficient.

In addition to continued expansion within the commercial and residential sectors, heavy investments within the tourism sector coupled with an accelerated population growth have contributed to increased demand within the hospitality and retail sectors. Hotel room supply within the Kingdom is expected to increase by almost 60% by 2020, sustained by projections of increased tourist inflows in the medium-term as the government invests large sums into promoting religious tourism. Supported by increased tourism inflows, the retail sector is slated for continued development as demand for white goods, textiles, footwear and furniture increase behind strong economic indicators, diminishing unemployment, and expansionary fiscal policies.

The Saudi government is increasingly capitalising on growth in the real estate sector by expanding and liberalising economic policies. In April 2010, the government created the Saudi Arabian General Investment Authority (SAGIA) as part of a series of measures designed to liberalise and diversify the economy. SAGIA manages investment opportunities in the country, and is responsible for creating a pro-business, investor-friendly environment in key sectors of the economy, including real estate. In the last five years, 50 new real estate developers have received licenses from SAGIA and regional property firms are entering a real estate market previously centred in Riyadh. SAGIA is also directly responsible for developing the six economic cities, in which over US$ 100 bn has already been invested. SAGIA expects these economic cities to contribute US$ 150 bn to GDP and create more than one million jobs by 2020.

The government has recently taken steps to facilitate foreign investment in real estate, namely through reforms of the investment code that grants foreigners 100% ownership and property rights when purchasing real estate. The exception remains the holy cities of Mecca and Medina, where non-Muslim foreigners can neither invest in nor own property. Saudi real estate firms are invigorated by these reforms, and have publicly announced a desire to partner with companies with foreign expertise.

As the real estate sector continues to grow, its contribution to Saudi Arabia's GDP has increased accordingly. Between 2004 and 2008, the sector's contribution to GDP was a steady 4.5%, climbing to 5.1% in 2013. Analysts anticipate that this figure is poised to increase to almost 10% by 2020. As the government aims to diversify the economy, more of an emphasis will be placed on encouraging even more robust growth in real estate.

Residential Real Estate

The residential sector in Saudi Arabia is driven by a high demand from a young and growing population with increased (albeit limited) purchasing power and a shortage of available and affordable homes. In the past decade, demand has continued to surpass supply driving property prices up by 15% in 2013, with prices expected to increase at a CAGR of 7% through 2018. Present demographic trends are necessitating a shift towards smaller units and more affordable housing. Smaller sized villas (300-400 sqm) and large apartments (135-190 sqm) are the most sought after units for sale at the moment, and these preferences have guided real estate trends across the country.

The Kingdom's residential market is undersupplied as demand across all sectors is continuously increasing, supported by favourable demographics. This supply-demand gap is expected to persist in the medium to long term as population levels continue to climb. The home ownership rates in Riyadh are quite low as compared to other developed cities, with home ownership rates as low as 30% in Riyadh and 40% in other parts of the country. The high land prices and construction costs coupled with lack of financing activities make home ownership difficult for residents, particularly within the Kingdom's main urban centres.

The recent introduction of a new mortgage law that restricted loan-to-value ratios to 70% maximum is expected to play an important role to enhance affordability of housing units. In response to concerns that this initiative would negatively impact new buyers in the mid-low income segment of the population who are either unable to afford a 30% down payment or do not meet financing requirements, the law was amended in 2016 to lower capital requirements to 15% of the homes value. Additionally, in an effort to make home ownership more accessible to the low-income segment of the population, the government has committed to provide affordable housing for all of its nationals, with 65,000 affordable housing units expected for completion in 2016.

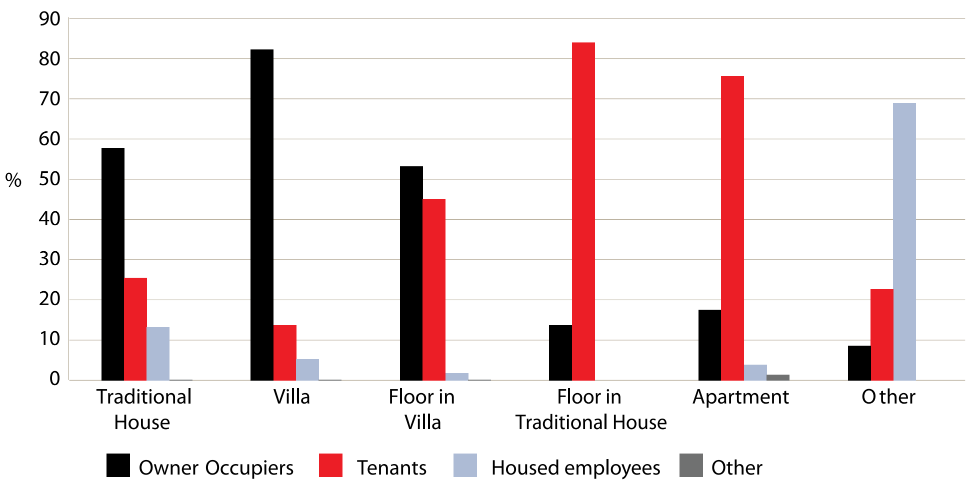
In efforts to further support citizens in need of affordable housing, the Ministry of Housing recently launched the ESKAN housing aid program which will offer Saudi families sate-subsidized home loans or subsidized sales of land

and housing units. Despite these efforts, persistent land and labour shortages coupled with a shortage of key construction materials make bridging the supply gap difficult. The entry of international developers partnering with domestic firms is expected to help in boosting construction activities moving forward, helping to stem the flow of demand for affordable, conventional and luxury housing in the medium term.

Demand for villas in particular has resulted in soaring prices across Saudi Arabia. Small villa sale prices accelerated across the country by a median 5.5% to US$ 888 per sqm, while asking prices for a larger villa (400-700 sqm) grew to reach US$ 1,386 in 2014. Prices for villas of all sizes are persistently high in the capital and Riyadh is currently Saudi Arabia's fastest growing housing market, with a population that has grown at an annual rate averaging 2.2%, and a dearth in supply to meet demand. Riyadh is also home to a quarter of the Saudi population, and as the Kingdom's financial and business capital, is a crucial benchmark for assessing the rest of the country's real estate sector. The rental rates of villas and apartments followed the same upward trend and increased by 6-11% across the Kingdom, depending upon the location and finish quality of the property. Residential units within compounds have the highest rental rates in Riyadh city, where average rental rate of 2-bedroom apartment varies between US$ 29,000 and US$ 40,000 annually.

In Jeddah, the second largest city in Saudi Arabia, the housing sector has also grown in recent years, though not as drastically as in the capital. Jeddah has some of the costliest real estate in the country, however, acting as the Kingdom's main port, commercial centre and gateway for religious tourism. Small villa prices fell in 2009, following flooding that caused massive property damage, but have recovered in recent years to reach 11.9% growth y-o-y in 2014. The city is in need of a vast supply of new housing to meet the demands of a rising population and to improve the quality of living for residents in unplanned settlements. The stock of total available residential units in Jeddah stood at 769,000 in 2014, with the housing supply expected to increase by 4.5%, or 77,000 units by 2018.

Distribution of Housing Supply by Tenant Type



Source : Colliers International

The government is actively attempting to match supply to demand. Over 1.2 mn low-income homes are slated for construction around the country through 2023, with US$ 68 bn currently invested in the project. In spite of government's efforts to stimulate the provision of affordable housing, it is expected that the Kingdoms' residential market, particularly in Riyadh and Jeddah, will remain undersupplied for the next couple of years. Demand for apartments and small villas/duplexes is expected to increase with faster pace due to influx of expatriates and reduced affordability concerns mortgage law) for Saudi nationals due to the new mortgage law. Although rental and ownership prices are increasing for both villas and apartments, this influx of new houses over the next few years is likely to delay many Saudis' plans for purchasing new property in the hopes that prices will stabilise or fall in the medium-term, curbing market growth in the short-term.

Commercial Real Estate

The global recession greatly affected the commercial segment of the GCC real estate market, and most countries have yet to recover. Saudi Arabia, however, has made a spectacular comeback, mostly due to the government's aggressive tactics to re-stabilise this segment. Demand supplies were highest in the capital, where the government and various ministries are the most robust consumers. Government-led initiatives to increase the entry of new market participants, both international and local, coupled with restructured licence and stock agreements aimed at increasing the availability of white-collar jobs for local residents are expected to stabilise diminishing commercial rents in the medium-term.

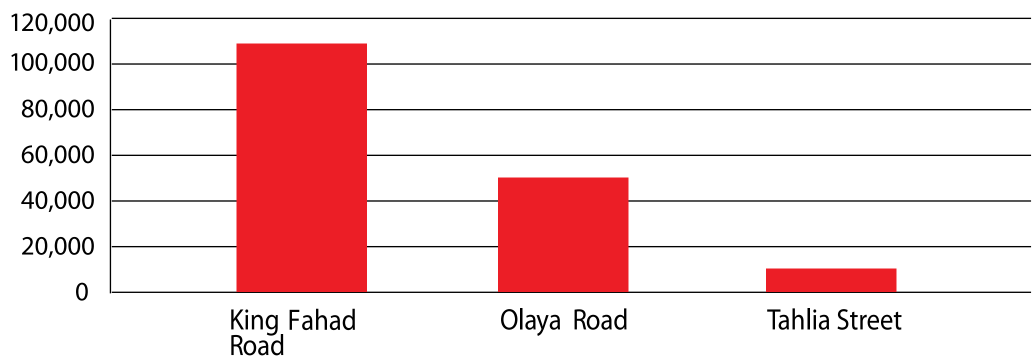
Infrastructure and the new economic cities account for the bulk of commercial projects. The Mecca-Medina railway link, for example, was awarded a contract worth US$ 2.4 bn, while over US$ 100 bn has been invested in the six economic cities. Work is currently underway in four of the cities, with the government heavily overseeing construction, although the private sector will likely take over in 2016. The King Abdullah Economic City (KAEC) is the nearest to completion, having already set up a resale and rental property department in July 2016 that will provide resale and rental services for property already purchased by KAEC investors. A noteworthy perk of this complex is the creation of 1,500 direct jobs and 3,000 indirect jobs. As the Saudi government looks to diversify their economy through commercial real estate, an emphasis will be placed on projects that assist the growing population through both housing opportunities and job creation.

Office Real Estate

The office segment is suffering from an over-supply of space, particularly in the capital. This, coupled with over US$ 6.5 bn worth of commercial projects entering the pipeline in 2014 has resulted in falling rent prices and occupancy rates. As the business capital in the region, Riyadh boasts the largest number of office spaces. There was around 150,000 sqm of new office space completed in 2014, bringing the current office stock in Riyadh to 2.3mn sqm. An expected supply increase of 50% over the next 2-3 years will further exacerbate the current oversupply issues in the short-term as job creation initiatives continue to remain in the beginning stages.

Current demand for commercial and office space is mainly driven by the public and banking sectors, as government initiatives to ease the business environment and diversify the economy are expected to boost office demand in coming years. Traditionally, large local businesses and finance firms occupy grade A space, while small and medium enterprises occupy grade B and C spaces. Median rental rates across all grades remained stable y-o-y in 2014, with Grade A rental rates averaging US$ 339 sqm, while Grade C and B space averaged US$ 231 sqm. Grade A office space continues to lead demand, with vacancy rates in Riyadh hovering around 16% in 2014. In Jeddah, much of it's Grade A commercial stock has yet to meet international standards, although this is being remedied with recent developments such as Jameel Square. Office stock in Jeddah stands at 800,000 sqm, with 135,000 sqm to be added in 2016, meeting demand for both the public and private sectors.

Riyadh Office Supply



Source : Colliers International

Retail Real Estate

Saudi Arabia's demographics and cultural norms are well suited to welcome international brands and well-known labels, boosting demand for expansion within the real estate sector. A young and increasingly globally aware population has turned Saudi Arabia into one of the MENA regions most prosperous shopping destination through its demand for the latest fashions and its strong spending power. Often these international brands are introduced into the Saudi market by corporate partnerships between the brand and a local or regional company acting as a third party. This model is preferable for the foreign investor as the local or regional company will have a better idea of the market, suitable products and customer service norms which are alien to western companies. Saudi Arabia, particularly in the cities of Jeddah and Riyadh, has a healthy mix of high-street retailers and higher-end luxury brands operating outlets throughout the Kingdom.

Unique market conditions provide retailers and developers the opportunity to deliver increasingly creative retail formats to meet consumer demand, such as the development of women-only or family-themed malls that would provide alternative leisure and retail options to current market offerings. Another effective way Saudi retailers have found to increase traffic to stores is the creation of shopping events and festivals. Established in January 2012, the Jeddah Shopping Festival has become one of the country's premiere shopping events, offering a unique and diverse range of retail experiences from street markets and traditional souks to world-class shopping malls. Bonus incentives for attending the event include gift and automobile giveaways. The 30-day festival draws over one million tourists and visitors to Jeddah, further establishing the city as the Kingdom's foremost shopping front.

Due to Jeddah's status as a retail capital, a number of expansion projects are scheduled within the retail sector, the largest being the expansion of the Red Sea Mall. The Red Sea Mall, Jeddah's largest shopping centre, has recently announced plans for a 145,000 sqm expansion containing an additional 30,000 sqm of gross leasable area and 4,000 sqm of outdoor shopping and food retail. The US$ 53.3 mn expansion project has an expected completion date of 2016 year-end.

Riyadh retail mall gross leasable area is dominated by regional malls, accounting for more than 40% of existing supply, followed by community malls. Rising demand has prompted a number of retail projects to enter the pipeline within the past five years, with many nearing completion. Recently opened Nakheel Mall contributed over 1.4 mn sqm of gross leasable retail area to the city, brining total GLA to 3 mn sqm in the first quarter of 2015. Other projects within Riyadh slated for 2016 completion include Al Hamara Mall with a GLA of 51,000 sqm, Al Khaleej Mall with a GLA of 54,000, and The Family Garden in western Riyadh with a total GLA of 20,000. Average vacancy rates in Riyadh malls stood at 12%, while rents increased by an average of 8% in 2014. Many retailers have sited long waiting lists for prime GLA, indicating that further development will be absorbed by a steady demand from luxury and mid-ranger retailers alike.

Hospitality Real Estate

Saudi Arabia led the Middle East and Africa region in the construction of new hotel rooms in August 2017. Saudi Arabia has 40,020 hotel rooms in 89 projects in the construction pipeline, ahead of the UAE, which has 35,050 in 121 projects. Saudi Arabia boasts the second largest hospitality industry in the GCC, with demand only expected to grow in the as the government embarks on ambitious planning to boost tourism across all sectors. In addition to encouraging religious tourism, heavy investments within the healthcare sector are expected to boost the Kingdom's status as a medical tourism hub within the GCC and greater MENA region. The holy cities of Mecca and Medina are key target markets, with more than 10mn Muslim pilgrims from 140 countries visiting the holy cities annually for hajj and umrah, contributing nearly US$ 10 bn in revenue each year. Another key growth area is that of business tourism, as government investments into key infrastructure projects such as King Abdullah Financial District, coupled with economic policies to encourage foreign investment are expected to attract a rising number of investors and business delegates. The cities of Riyadh, Mecca and Medina provide plenty of five-star accommodation, but are sorely lacking in the mid-range and budget department.

In addition to business and religious tourism, medical tourism also represents a growing market, and all GCC countries are attempting to tap into this lucrative field. Inspired by the growth of medical tourism in India and Southeast Asia, Saudi Arabia has begun to attract patients from Western countries and the rest of the Middle East by promoting their low healthcare costs and luxurious accommodations. Medical tourism in the GCC region accounted for US$ 8 bn in 2014.

Total hotel room stock is expected to increase by over 50% within the next 2-3 years as a number of key projects enter completion. Current room inventory stood at 225,000 in 2015, with the rapid expansion expected to be absorbed by increasing tourism inflows. Major developments of international brands across all price sectors such as the Hilton Residence, Hyatt Regency, Crowne Plaza and Fairmont will be delivered throughout the Kingdom's urban centres in 2016. Hilton Worldwide alone has a development pipeline of 18 properties throughout the Kingdom, from luxury developments such as the Waldorf Astoria Hotels and Resorts and Conrad Hotels, to the mid-range and affordable DoubleTree and Hilton Garden Inn brands, with completion dates ranging from 2016 to 2023.

KEY PLAYERS

Saudi Oger Limited

Incorporated in 1978, Saudi Oger has grown to become one of the leading construction, facilities management, and infrastructure development companies in Saudi Arabia. Most recently, the company signed a US$ 1.5 bn contract with Saudi Arabia's General Authority of Civil Aviation (GACA) to increase the capacity of Prince Mohammad Bin Addulaziz International Airport. Saudi Oger and SBG are considered to be two of the biggest players in the Saudi construction and infrastructure industry, with some analysts suggesting that their hold on the market borders on a monopoly.

Saudi Binladin Group (SBG)

Established in 1931 by Mohamed bin Laden, the Binladin Group has benefitted from its founder's solid relationship with the country's ruling class and since its inception has consistently been awarded contracts for the biggest government projects in Saudi Arabia. With annual revenue estimated at US$ 5 bn, the Binladin Group has worked on both residential and non-residential building projects, the most recent of which include a large complex near the Kaaba in Mecca, a US$ 1.23 bn contract to construct the Kingdom Tower in Jeddah, as well as a leading share of the US$ 26.6 bn contract to build King Abdullah Economic City awarded to a consortium of Saudi and Emirati companies in December 2005. The group is also currently involved in the design and construction of the Jeddah Kingdom City. In January 2018 it was reported that the Saudi state would seize managerial control of the company while its chairman remains in detention.

Bechtel Corporation

Established in 1898, Bechtel Corporation is the largest construction and civil engineering company and the fourth largest privately owned company in the United States. The company's operational activities are global and wide-ranging and include civil infrastructure, government services, mining and metals, energy and oil, gas, and petrochemicals. The company is currently overseeing a number of key projects within the Kingdom, including the expansion of Jubail Industrial City, which the company has managed since the 1970s. Additionally, Bechtel recently won a US$ 10 bn contract to design and build two rail lines of the Riyadh Metro Network.

Arabtec

Dubai-based Arabtec was founded in 1976 and is one of the leading construction contractors in the United Arab Emirates, although the country's largest market is Saudi Arabia, home to almost 40% of the company's active backlog in 2010. Arabtec currently has US$ 4.1 bn worth of projects in its backlog, US$ 1.3 bn of which are located in Saudi Arabia.

Samama Holdings

Established in 1980, Samama is a rapidly expanding group with a diversity of operations. With a focus on the development and utilisation of resources in order to yield sustainable growth and benefit the community, the company has a number of business lines that include operation and management, contracting, services, real estate development and investment. Samama boasts over 10,000 skilled employees and handles over 200 projects annually. The company has headed a number of key residential and commercial development projects within the Kingdom including the Al Jazzera Mall and Suhoob Sea Resort in Jeddah.

Saudi Diyar Consultants

Diyar Consultants is one of the leading multidiscipline design firms in the Middle East with a diverse portfolio of commercial, institutional, residential, hospitality, healthcare and urban design projects. Founded in 1985, Diyar has offices located in Jeddah, Cairo, Beirut, Riyadh, Mecca, and Medina. The firm has been involved in the design and construction of a number of key projects such as the Jeddah Gate, King Abdullah Medical City, and the Lamar Towers.

Al Khodari Sons Company (AKS)

Established in 1966, AKS is a multi-faceted contracting company providing construction, engineering and other related services to clients engaged in a variety of economic sectors including hydrocarbons, infrastructure, transportation, manufacturing, and utilities. The majority of the company's equity is currently held by the Abdullah A. M. Al-Khodari Sons Investment Holding Company, in addition to another 10% held by the Al-Khodari family directly, leaving a free float of approximately 30%. Analysts generally hold a favourable view of AKS considering the company's strong history of securing government contracts, consistent order book growth, and management's focus on high-margin sustainability. The company's backlog grew at a CAGR of 19.6% from 2010-2014. Because it is a well-diversified player in infrastructure and can bid for an unlimited amount of contracts by virtue of its status as an A Grade contractor, AKS enjoys higher profit margins than its peers.

El Seif Engineering Contracting Company

Established in 1975, El Seif Engineering Contracting Company is a member of El Seif Group, a conglomerate of companies that has operated in Saudi Arabia since 1951 in the fields of construction, healthcare, defence, and transport. Among the company's most well known projects are the Kingdom Tower in Jeddah, the Kingdom Hospital, the King Khalid International Airport, and the King Faisal Airbase, in addition to several power plants in Riyadh and other cities. The company's website reports over US$ 710 mn in annual revenues.

Emaar the Economic City (EEC)

EEC is a consortium led by Emaar Properties in collaboration with numerous high-profile Saudi investors. The company is based in Jeddah, and was incorporated to plan and develop the King Abdullah Economic City (KAEC), a new economic zone, spread over 168 mn square metres. EEC's core activities include property development, real estate investment, and property-related services. Despite the economic importance of KAEC to the Kingdom, the company is prone to operational challenges, and had to put several residential, office, and commercial units on hold after banks restricted lending in Saudi Arabia.

Mohammad Al-Mojil Group

Al-Mojil Group is one of the leading oil and gas construction contractors in Saudi Arabia with over 50 years of experience and approximately US$ 13.3 bn worth of projects completed since its establishment. The company's core activity is the construction of onshore and offshore hydrocarbons facilities for key clients such as Aramco, Sabic and Maaden. Aramco's projects alone contributed 63% to the company's top line in 2010, in addition to US$ 453.3 mn of Al-Mojil's US$ 746.6 mn worth of new contracts obtained in 2011. Al-Mojil's top line then increased by over 36% to reach US$ 630.4 mn in 2011, and was estimated to exceed US$ 1 bn in 2015. Meanwhile the company's profits are expected to increase from US$ 33.5 mn in 2011 to US$ 43.1 mn over the same period.

Taiba Holding Company

Taiba is Saudi Arabia's largest real estate company by market capitalisation. Through its subsidiaries, Taiba is engaged in the management, ownership and investment of commercial, tourism and residential properties. The company also directly and through subsidiaries undertakes industrial and architectural projects. Currently, their largest revenue source comes from renting residential properties, a sector that may be edged out within the next few years if the government is able to rapidly build low-income housing to satiate demand. The company is increasingly turning towards tourism and residential projects, and will subsequently capitalise on the government's effort to boost both of these segments in Saudi Arabia.

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Makkah Construction & Development Company (MCDC)

MCDC is Saudi Arabia's fourth largest real estate company by market capitalisation. The company engages in investment, property development, ownership and management of hotels and shopping malls. The majority of MCDC's properties and projects are located in the holy city of Mecca, therefore shielded from downturns that affect the rest of the country. MCDC owns most of the property around the Grand Mosque, and well benefit greatly from the large-scale government-backed development currently in the pipeline, including a central transport station.

Hilton Worldwide Inc.

Hilton Worldwide Inc. is a global American hospitality company. As of 2014 the Hilton brand encompasses over 4,000 hotels with 680,000 rooms in 91 countries. The company owns, manages and franchises a portfolio of brands including Hilton Hotels and Resorts, DoubleTree by Hilton, Embassy Suites Hotels, Hilton Grand Vacations, and Waldorf Astoria Hotels and Resorts. The Hilton brand has a strong presence in the MENA region including locations in Dubai and Egypt, along with a number of planned developments throughout the Kingdom and greater GCC region.

Majid Al Futtaim Group (MAF)

A Dubai-based conglomerate, MAF covers a large spectrum of sectors across the Middle East, including real estate, mall development and retail. Established in the 1930's as a trading company, today the group has diversified to represent some of the world's biggest retail brands in the UAE including Ikea, Raymond, Marks & Spencer, Panasonic and Toys 'R' Us. The property development section of the group is currently developing Dubai Festival City, a flagship property that will combine business, residential and retail districts, the latter of which will include over 600 retail stores. The company has also partnered with French hypermarket brand Carrefour across the Middle East, with over 13 branches in the UAE alone. In August 2017 the company acquired Retail Arabia, the franchise owner of 26 Geant stores across the region as well as four Gulfmart supermarkets in Bahrain. In August 2017 the company also announced its first real foray into Abu Dhabi with plans for the AED 1.4 bn City Centre Al Jazira. Construction is scheduled to begin in October 2017 and the project is due to be completed in early 2021. The mall will consist of 153 retail and service stores across its 80,500 square metre total leasable area, whilst it will also include a Carrefour Hypermarket, a 15-screen Vox Cinema, a Magic Planet games centre, a medical clinic and a number of indoor and outdoor dining options. This latest announcement is in line with the company's plans to invest AED 30 bn in the UAE by 2026.

Alshaya Retail

Founded in 1890, Kuwait-based Alshaya is a trading and commerce company that operates global retail franchises in the MENA region as well as in Eastern Europe. In the UAE, the group owns and manages FMCG and retail outlets for American Eagle, BHS, Boots, Claire's, Coast, Debenhams, Dorothy Perkins, Evans, Express, Foot Locker, H&M, Jo Malone, Justice, M.A.C, Milano, Miss Selfridge, Mothercare, Next, Oasis, Office Depot, Payless, Peacocks, Pottery Barn, River Island, Solaris, Topshop, VaVaVoom, Vision Express, Victoria's Secret, Wallis and Warehouse. With over 200 stores in operation, Alshaya is one of the biggest retail companies in the UAE.

Saudi Real Estate Company (Al Akaria)

Al Akaria is a leading Saudi real estate development company founded in 1976 that develops and manages residential and commercial real estate properties. Historically, the company has focused on rentals, but has increasingly been purchasing and building commercial properties. Nearly 70% of Al Akaria is owned by the Saudi Arabian government, with the Public Investment Fund owning 64.5% and the Pension Fund owning 4.7%. Al Akaria has several large-scale projects in the pipeline, including the King Saudi University Science Park and units in the diplomatic quarter of Riyadh.

Dar Al Arkan Real Estate Development Company

Established in 1994, Dar Al Arkan is a one of Saudi Arabia's leading real estate development companies, specializing in the development of master-planned residential communities. The company was publicly listed on the Saudi Stock Exchange in 2007. With expertise concentrated in the development of high-end residential communities, Dar Al Arkan has become intricately involved in the development and modernisation of Saudi Arabia's numerous industrial centers, most recently clinching a US$ 1.06 bn facility to finance Qasr Khozam, a US$ 3.19 bn project that will span an area of 4 mn sqm, one of the company's biggest projects in recent history.

ECONOMIC OVERVIEW

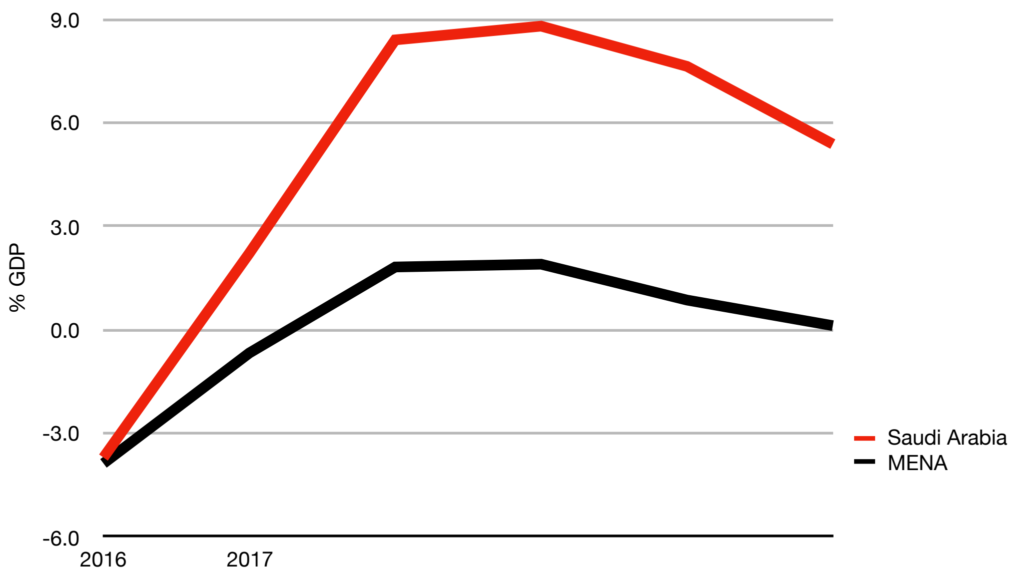
Economic Forecasts

Subject Descriptor	Units	2016	2017	2018	2019	2020	202
GDP, constant prices	% change	1.7	-0.9	2.2	2.4	1.9	2.1
GDP, current prices	US dollars	644.9	686.7	769.9	795.6	815.3	835.2
GDP per capita, current prices	US dollars	20,317	21,096	23,186	23,491	23,601	23,703
Total investment	%, GDP	30.3	27.9	26.6	26.5	26.9	26.9
Inflation, average consumer prices	% change	2.0	-0.9	2.6	2.0	2.3	2.2
Volume of imports of goods and services	% change	-16.3	-4.0	4.9	2.8	3.1	3.5
Volume of Imports of goods	% change	-16.2	-9.5	6.3	3.3	4.0	4.23
Volume of exports of goods and services	% change	5.9	-0.5	3.9	2.2	1.1	1.2
Volume of exports of goods	% change	4.3	-1.0	3.9	2.0	0.7	0.9
Unemployment rate	%, total labour force	5.6	n/a	n/a	n/a	n/a	n/a
Population	Millions	31.7	32.6	33.20	33.9	34.6	35.2
General government net lending	%, GDP	-17.2	-9.3	-4.6	-1.7	-1.3	-1.7
General government gross debt	%, GDP	13.1	17.2	19.4	20.4	21.2	22.5
Current account balance	%, GDP	-3.7	2.2	8.4	8.8	7.6	5.4

Source: IMF, World Economic Outlook database, October 2018

Growth in Saudi Arabia contracted by 1.0% in the second quarter of 2017, highlighting the impact of the oil production quotas. The downturn was double the 0.5% contraction in the first quarter and is the first period of negative growth since the start of 2010 when the world was in recession. The Opec-sanctioned cuts in oil output caused the sector to contract by 1.8%. The outturn so far in 2017 will add to fears that the economy will enjoy much lower rates of growth than previously expected over the coming four years in the wake of cuts in oil production. The economy will grow by just 0.1% in 2017, the International Monetary Fund said in its October 2017 world economic outlook, cutting its outlook from the 0.4% it made just six months earlier. That is a further sharp cut from its October 2016 outlook of 2.0% and puts the economy close to stagnation. The fund now expects growth of 1.0% in 2018 rather than 1.3%. It then forecasts 1.6%, and 1.8% for 2019, and 2020 respectively. However Standard Chartered bank is forecasting a 0.5% contraction. The non-oil private sector maintained its expansion path in September 2017. The snapshot survey of managers in the Emirates NBD purchasing managers index edged up to 55.5 from 55.8 in August on a scale where a number above 50 signifies expansion. Although still robust, the rate of expansion remained slower than the historical average. Panellists that reported a rise in output commonly noted strong underlying demand. Growth in new orders softened slightly during September, but remained steep overall. In line with the trend for overall new business, new export order growth eased in the latest survey. Oil supply slipped in September as lower domestic consumption more than offset slightly higher crude shipments to world markets. It pumped 9.94m barrels per day (bpd) down from 9.96m and in excess of its agreed 0.5m bpd cut. This represents a 640,000 bpd reduction on its baseline output.

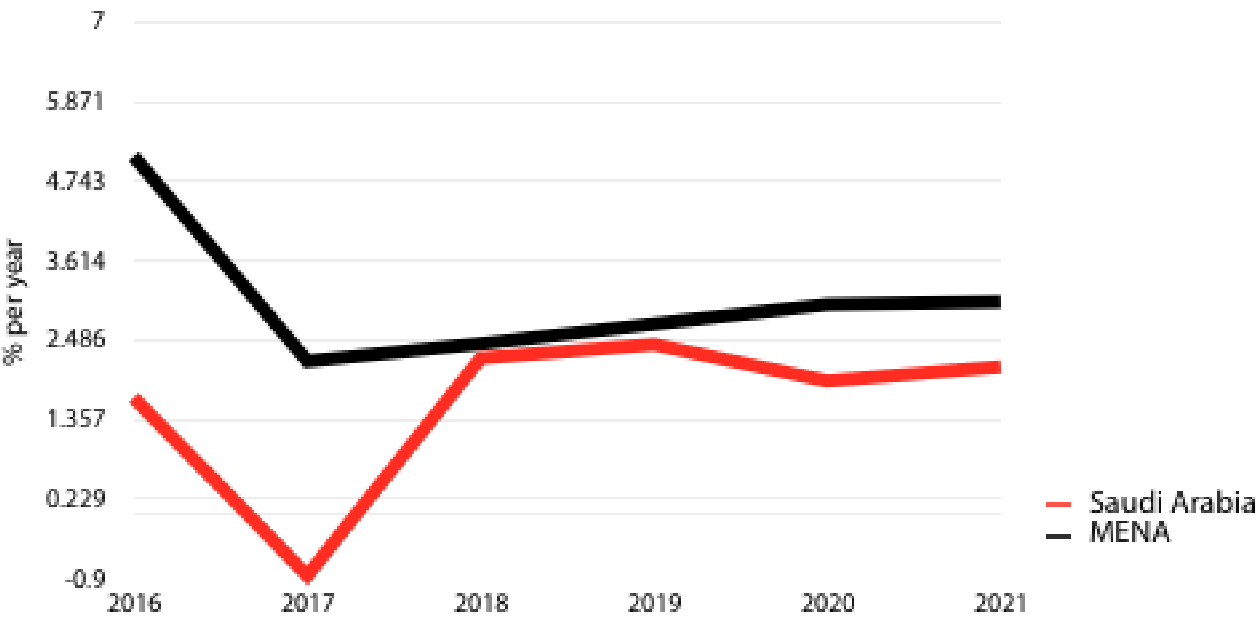
Current account deficit



Source: IMF, World Economic Outlook database, October 2018

The forecast slowdown in the Saudi economy masks a split between the oil and non-oil sectors. The hydrocarbon industry is expected to contract in 2017 because of the cut in output to meet the Opec quotas. This may push the overall growth measure in negative territory throughout 2017 rather than the marginal growth that the IMF expects. In its latest Article IV assessment of the economy published in July 2017, the IMF expects non-oil growth to pick up to 1.7%, while overall real GDP growth is expected to be close to zero as oil GDP declines in line with Saudi Arabia's commitments under the Opec agreement. It will be important to see how the slowdown in the Emirates NBD indicators in September feeds through to estimates for third quarter growth. There are signs that non-oil growth may be slipping with ATM cash withdrawals and point-of-sale retail transactions slowing. Occupancy rates of hotels in Saudi Arabia fell by 5.2 percentage points to 48% in July 2017 compared with a year earlier. Analysts STR said average daily rates (ADR) plummeted by nearly a third (31.6%) to SAR 625.78 while revenue per available room (RevPAR) fell even further — by 35.2% to SAR 300.14 Its preliminary data showed that Riyadh hotels' occupancy rates drop to 68.5% from 82.2% and RevPAR dropped 6.6% to SAR 850.3 although the ADR rose 8.2% to SAR 1,240.65. Indications that the government is slowing down the planned pace of its National Transformation Program may have undermined confidence. The NTP is central to the country's Vision 2030 economic plan. If achieved it will lead to Saudi Arabia moving from an oil-dependent economy towards one based on flourishing industry and services. The vision would involve restructuring the kingdom's oil-dependent economy, involving diversification, privatisation of major state assets including the energy giant Aramco, tax increases and spending and subsidy cuts. Goals include increasing non-oil government revenue from SARv163vbn (US$ 43 bn) to SAR 1 tr by 2030 and raising the share of the private sector from 40% to 65% of GDP. Other targets include reducing unemployment from 11.6% to 7% by 2030, and increasing women's participation in the labour force from 22% to 30% and creating an additional million jobs for Saudis in the retail sector by 2020. However according to reports in September 2017, Crown Prince Mohammed bin Salman has started to redraft the NTP to change existing initiatives and add new ones that the NTP covers up to 2020 and which lays out 178 strategic objectives with more than 340 indicators and benchmarks for 24 ministries. It aims to reduce the share of wages in the budget from 45% to 40% while creating 450,000 private sector jobs. The plan indicates a target to increase net revenues by SAR 321bn (US$ 86 bn) by 2020. Meanwhile rumours that Saudi Arabia is exploring a private sale of a stake in Aramco, the state oil group, rather than a stock market flotation has raised doubts over the kingdom's commitment. Riyadh has denied any change to its plan for an international listing that has seen London and New York compete to be the host exchange. One explanation may be concern that current volatile conditions would lead to Aramco attracting a valuation below the estimated US$ 2 bn — something that would be concealed by a private sale. GDP per capita will remain higher than the MENA average but will show only gentle growth over the coming four years.

GDP growth

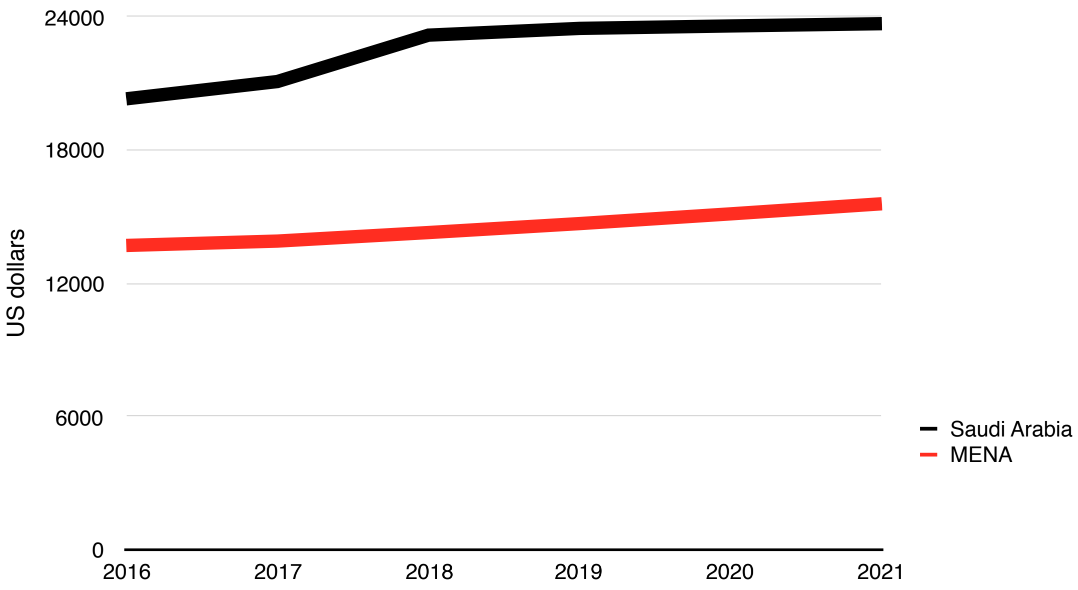


Source: IMF, World Economic Outlook database, October 2018

Saudi Arabia posted its second successive current account surplus in the second quarter of 2017, putting it on track to record its first annual surplus since 2014. The current account balance is expected to move into a small surplus in 2017 as oil export revenues increase and import growth and remittance outflows remain relatively subdued, the IMF said in October 2017. The kingdom posted a surplus of US$ 1.1 bn down from a surplus of US$6.7 bn in the previous quarter. It recorded a current account deficit of US$ 2.2 bn in the fourth quarter of 2016, which was the lowest since the final quarter of 2015 other than a surplus of US$ 2.3 bn in the third quarter of 2016. The IMF expects the external balance to move into a surplus of 0.7% of GDP in 2017 rather than the 6.6% deficit it forecast in October 2016 but smaller than the 1.5% surplus it had forecast in April 2017. It will then build up surpluses of 0.4%, 1.2%, and

1.2% over the subsequent three years although smaller than previously expected. One unexpected boost may come from the decision to allow women to drive. According to Standard Chartered bank, households employ 1.38 million non-Saudi male drivers, accounting for close to 60% of the total non-Saudi domestic workers. Assuming an average monthly salary of US$ 600 per driver, these drivers are paid around US$ 10 bn by Saudi households annually. Most of which is then remitted abroad. These sums accounted for 26% of the total remittances from Saudi Arabia in 2016. Assuming that a significant number of these foreign drivers are no longer employed in Saudi Arabia, this would reduce the number of foreign workers in the labour force and the amount of foreign currency being remitted abroad, both of which would help the Saudi economy to adjust to the terms-of-trade shock it currently faces. The current account position deteriorated at the start of 2016 thanks to lower oil prices. 2017's current account surplus has left observers surprised, given a sharp decline in foreign exchange reserves over the course of 2016. Between the start of 2017 and the end of May, the foreign exchange reserves of the Saudi Arabian Monetary Authority, the central bank, fell by US$ 19.3 bn. This was probably to finance the current account deficit and offset capital outflows. Following a peak of US$ 731 bn August 2014, foreign exchange reserves have dropped by more than US$ 2 tr to around US$ 493 bn as of May 2017, their lowest level since December 2011 and the first time since then they have dropped below US$ 500 mn.

GDP per capita, current prices

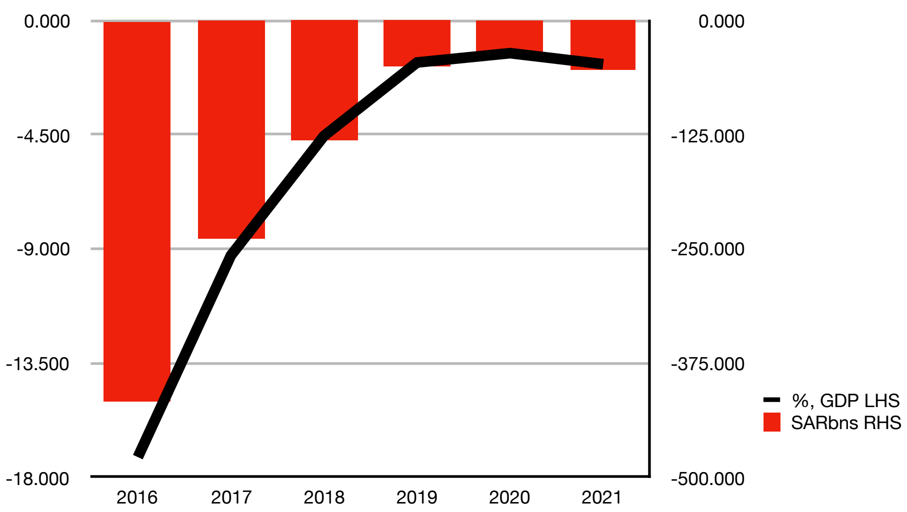


Source: IMF, World Economic Outlook database, October 2018

Saudi Arabia's budget deficit shrank by a fifth from a year earlier in the second quarter of 2017 as revenues rose moderately and spending fell marginally. Revenues increased by 6% in the three months to June 2017 from a year ago to SAR 163.9 bn (US$ 43.7 bn) while spending dropped 1.3% to SAR 210.4 bn in the second quarter, leaving a deficit of SAR 46.5 bn compared with about SAR 58.4 bn a year earlier. The deficit had fallen by 71% in the first quarter, after the kingdom made sweeping spending cuts. The positive news follows the blow of the downgrade to the credit rating of its sovereign debt in late March 2017. Fitch Ratings said its decision to cut its rating from A+ to AA- was based on the significantly wider than expected fiscal deficit in 2016 and continued doubts about the extent to which the government's ambitious reform programme can be implemented. It followed a previous cut in September 2016. The government budget for 2017 published in December 2016 showed that ministers had decided to increase spending rather than repeat the austerity of 2016 in light of the sharp growth slowdown. In its 2017 budget plan, Riyadh said it would increase spending by 8% to SAR 890 bn (US$ 236 bn) from the SAR 840 bn (US$ 223 bn) originally projected for 2016. However this will be offset by a 31% increase in revenues that will leave a budget deficit of SAR198bn (7.7% of GDP) compared with SAR 416bn or 17.3% in 2016 (compared with a target of SAR 326bn).

In April 2017 Mohammed al-Tuwaijri, deputy economy minister, said the first quarter deficit was SAR 26 bn (US$ 7 bn), compared with SAR 54 bn projected at the beginning of the year. Spending allocations include SAR 42 bn for projects related to the NTP, as part of the goal of diversifying the economy away from oil. The budget deficit narrowed to US$ 79 bn in 2016. That was below a record US$ 98 bn in 2015, and less than the government's projection in its original 2016 budget plan of a deficit of US$ 87 bn. Fitch expects the deficit to fall to 9.2% of GDP in 2017 and 7.1% in 2018, which will be financed by some further run-down in deposits as well domestic and international issuance. The finance ministry said it would issue new debt to fund the deficit. In July 2017 Saudi Arabia raised SAR 17 bn (US$ 4.5 bn) from its first local Islamic bond sale of the year. In October 2016 Saudi Arabia launched a US$ 17.5 bn sale of international bonds to fund around a third of 2017's budget. The NTP aims to raise government non-oil revenue by US$ 98 bn by 2020 through measures such as a unified income tax, an income tax on residents, a value-added tax, and an income tax on expatriate workers. The government cut spending by 15% in 2016 having reduced it by the same amount in the previous year. However in April 2017 King Salman bin Abdulaziz reversed one of Saudi Arabia's most contentious austerity measures on Saturday, reinstating benefits to civil servants and military personnel. The removal of these benefits in October 2016, affected the take-home pay of two-thirds of working Saudi nationals. At a meeting of Opec countries the cartel agreed to impose oil output cuts. The goal is to cut production to a range of 32.5-33. million barrels per day (bpd). The October 2017 forecasts by the IMF envisage a budget shortfall narrowing from 8.6% of GDP to 1.6% between 2017 and 2019, rather than the deeper deficits of 9.8%-1.4% path expected in April. The latest budget assumes an average oil price of around $50 a barrel. In September 2015 the IMF calculated that the fiscal breakeven point was closer to US$ 106 a barrel compared with US$69 in 2014. Nevertheless, government debt is very low and was 7% of GDP at end of 2015.

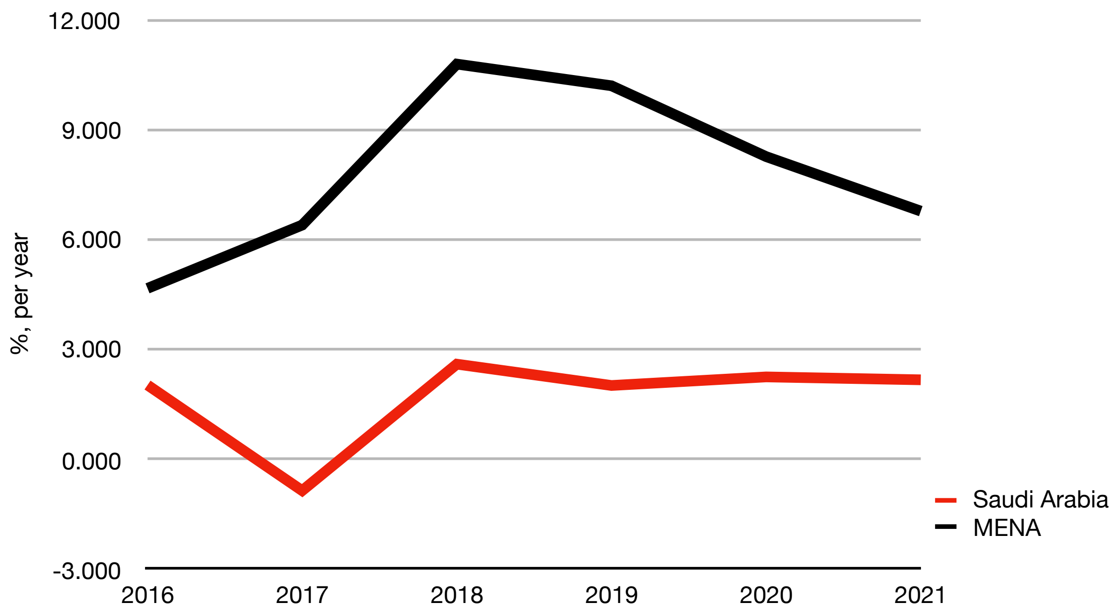
Government budget balance



Source: IMF, World Economic Outlook database, October 2018

Inflation was virtually unchanged for the second month in a row in September 2017, raising hopes that the nine months of mild deflation may be nearing an end. However the annual rate remained in negative territory as prices continued to fall. The annual rate was unchanged at minus 0.1% following minus 0.3% in July and minus 0.4% in June. Food inflation, which accounts for around a fifth of the inflation basket, stood at minus 1.4% down from minus 1.8% in August. Housing and utilities inflation eased to minus 0.3% from minus 0.5% while transport was unchanged at minus 1.6%. There are growing hopes that the deflation is not likely to become ingrained as the government is pushing ahead with subsidy cuts while a new VAT will come into force in 2018. The authorities have increased the price of petrol by 50% and diesel by 81% as part of their fiscal consolidation programme. Inflation is forecast by the IMF to reach 3.8% in 2017 but recede to 2.2% by 2020. The government is determined to stick with the riyal's US dollar peg. In July 2017 the IMF said the peg remained appropriate given the structure of the Saudi economy but said it "saw merit" in reviewing the peg periodically to ensure it remains appropriate. The Saudis are almost certain not to alter the peg of SAR 3.75 to the US dollar. SAMA has responded to the tightening of liquidity by relaxing the loan to deposit ratio for banks. In June 2017 the bank left its benchmark repo rate steady at 2% but raised the reverse repo rate by 25 basis points to 1.25%, saying the decision was made in line with domestic and international financial market conditions. The move was made after the Federal Reserve raised rates for the second time this year.

CPI inflation

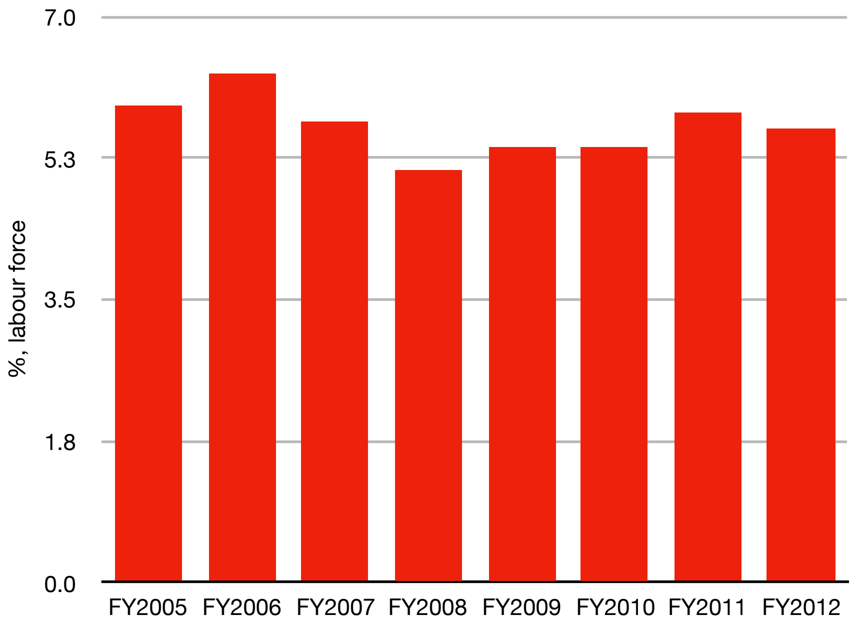


Source: IMF, World Economic Outlook database, October 2018

Saudi Arabia's unemployment rate rose to 6.0% in the second quarter of 2017 from 5.8% and 5.6% in the previous two three-month periods. However that official figure masks a higher unemployment rate, excluding migrant and expatriate workers, according to other estimates. On that measure unemployment rose to 12.8% from 12.7% in the first quarter of 2017, marking a four-year high. According to the Saudi Press Agency, the latest statistics show that the total number of Saudis seeking jobs is 1.075 million of whom 216,352 are men and 859,581 women. The total number of employees was 13.84 million, down slightly from 13.89 million in the first quarter of 2017. The Vision 2030 aims to cut the native unemployment rate to 7% by 2030. The highest percentage of Saudi job-seekers was in the age group 25-29 years, at 34.2%. Half of Saudi job-seekers are university graduates. Overall unemployment had been stable at 5%-6% over the previous decade according to official figures. Some two thirds of working Saudi nationals are employed in the public sector. Saudi Arabia unveiled a plan in March 2016 to guarantee jobs for its citizens over foreigners living in the country — by legally forcing firms to have 100% Saudi employees within six months.

In April 2017 the government reinstated benefits and bonuses for civil servants that had been cancelled in October 2016 as part of the austerity drive. Ministers' salaries had been reduced by 20%, and housing and car allowances for members of the advisory Shura Council cut by 15%. Lower-ranking civil servants would have seen wage increases suspended, and overtime payments and annual leave capped. Some 40% of Saudi Arabians under the age of 30, or 13m, are unemployed. In its July 2017 annual Article IV assessment the IMF said creating more jobs for Saudi nationals in the private sector was essential. Over the past decade, the number of graduates with tertiary education has more than doubled, but leaving them without the skills that the private sector needs. The government is making changes to wage subsidies, incentives, working hours, unemployment insurance and social benefits to encourage more nationals into work. Employment grew by 3.2% in 2014, with Saudi employment growing by 4.4% and non-Saudi by 2.2%.

Unemployment rate



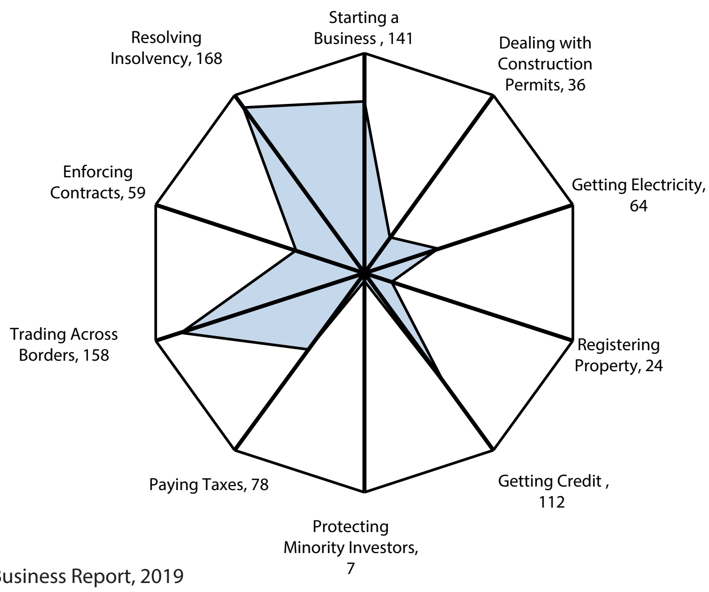
Source: IMF, World Economic Outlook database, October 2018

The Saudi economy is adjusting to the effects of lower oil prices and fiscal consolidation, but that non-oil growth is expected to pick up this year and overall growth is expected to strengthen over the medium term as structural reforms are implemented. However proper calibration and sequencing of reforms will be crucial to their success. Non-oil growth is forecast to accelerate from 1.3% in 2018 to 3.0% in 2022 while hydrocarbon growth will stabilise at around 1.0%. The authorities have taken bold steps towards tackling the impact on economic growth and the public finances from the fall in oil prices. The fiscal deficit is projected to narrow substantially in the coming years. Given Saudi Arabia's dependence on oil and gas for economic growth and its fiscal and external position, the plunge in global prices will put pressure on GDP growth and the current account balance over the coming years. The decline in oil prices has increased the importance of the goal of the Vision 2030 programme and the National Transformation Plan to push through structural reforms to switch the focus of growth away from the public sector and toward the private sector. It also aims to diversify the economy, increase the number of jobs for Saudis in the private sector, and adjust fiscal policy to ensure macroeconomic stability. The elevation of Prince Mohammed bin Rashed to the title of Crown Prince will be seen as a validation of the policies that have been implemented. The authorities are beginning to make good progress in identifying and reducing obstacles to private sector growth. The decision to launch a technology-based fund with Softbank indicates that the Saudi authorities are prepared to support their pledged with money. The agreement by Opec to cut production quotas, which Saudi Arabia was instrumental in pushing through, will cause short-term pain as output falls, but should deliver medium-term benefits in the form of higher prices. Together with the ambitious fiscal consolidation this should help it reduce its budget deficits over time. Oil export revenues account for almost half of GDP, 80% of tax revenues and 90% of export earnings. In any event the kingdom will continue to have the foreign reserves needed to sustain both current account and fiscal deficits and to tide it over. Its efforts to diversify into non-hydrocarbon growth in sectors such as construction, manufacturing, transportation, trade and tourism, have so far proved successful and the details of the National Transformation Plan will be pored over.

There are still obstacles to doing business in Saudi Arabia although it is one of the less bureaucratic countries in the MENA region. The country is ranked at 94 out of 190 countries in the World Bank's 2017 Doing Business report. However this is a slight rise from its revised rank of 96 in the 2016 assessment. The improvement was due to the fact that made property transfers faster by introducing a new computerised system at the land registry, which raised it 18 places in the property registration sub-index. Bribery is illegal in Saudi Arabia, and is prosecuted with increasing vigour. The UK government notes that the late King Abdullah had "done much to tackle the market distorting effects of patronage and compel prominent individuals to play by the rules". The NTP aims to raise direct foreign investment to SAR 70 bn from SAR 30 bn currently as part of the Vision 2030 plans to open up the private sector. The 2017 Budget indicated there were no plans to impose taxes on nationals and residents or to tax Saudi companies. Saudi businesses benefited from an estimated US$ 350 bn of deals with the US announced during the 2017 visit by President Donald Trump that also saw US companies investing in the kingdom. In July 2017 the IMF noted that good progress was being made in identifying and removing obstacles to private sector growth, and welcomed the intensive consultation with the business community. The decision in September 2017 to allow women to drive is being seen as a milestone on the path to further reform. Saudi Arabia ranked 62 out of 176 countries in Transparency International's 2016 Corruption Perceptions Index, a deterioration from its 52 out of 168 ranking in 2015. There are still delays for entrepreneurs wishing to obtain official approvals (with ranking of the best-performing nation, New Zealand, in brackets):

• Start a business: 15 days (0.5)
• Obtain construction permits 106 days (93)
• Gain electricity supply 61 days (58)

Doing business in Saudi Arabia



Source: World Bank, Doing Business Report, 2019
Rank 190 bottom, Rank 1 top of scale

CHALLENGES TO INDUSTRY

Relative to the rest of the MENA region, Saudi Arabia undoubtedly exhibits lower political risk than its neighbours in North Africa and the Levant; however this does not guarantee that Saudi Arabia is completely insulated from the effects of the Arab Spring or political unrest in general. Recent reports analysing political risk in the MENA region noted that political risk in Saudi Arabia remains higher than in the past few years in light of tensions resulting from the wave of democratisation efforts engulfing the rest of the region, the status of the Shi'a minority, and lingering social tensions related to housing shortages and broader human rights abuses. In response to the first two concerns, the Saudi Arabian government acted swiftly, by drastically increasing public spending on the one hand as a means of quelling discontent related to unemployment and social inequality, while simultaneously suppressing pro-democracy demonstrations throughout the country, in particular in the Eastern provinces that are home to the country's Shi'a population. Furthermore, draconian moves by Crown Prince Mohammad bin Salman pose a wide-ranging threat to industry in Saudi Arabia, with prominent businessmen remaining in prison and the state moving to take control of major assets.

Still, Saudi Arabia faces little to no risk of regime change or of a civil uprising in the foreseeable future as the government possesses the means of appeasing its population through generous fiscal programs. However, the government does face legitimate security threats from terrorist networks within its borders, particularly in light of the recent merger between the Yemeni and Saudi branches of Al-Qaeda, now known collectively as Al-Qaeda in the Arabian Peninsula (AQAP). In addition to home grown terrorist threats, the regime also views instability in neighbouring Bahrain and Yemen with trepidation, and has intervened in both countries in support of the existing regimes. Continued political unrest in neighbouring countries Bahrain, and Egypt, combined with the conflict in Yemen, has the potential to shake investor confidence in Saudi markets and negatively affect FDI levels.

While the outlook is generally favourable for the real estate sector, there are several persistent problems that could potentially devalue the sector. Although Saudi Arabia boasts a high GDP, and has increasingly been introducing social stimulus packages, a large portion of the population has yet to see the benefits, particularly in terms of employment and housing. The majority of Saudis earn less than US$ 2,200 a month and are thus unable to afford the housing currently offered on the market. Over 50% of the population is under the age of 24, and population is expected to grow yearly by 2.2%.

The Saudi government has taken noteworthy steps to introducing low- and middle-income housing to the market, by pledging US$ 68 bn to such projects, and is in the process of implementing a new mortgage law to facilitate home ownership. However, this law has negatively impacted the Kingdom's low-mid income segment who are unable to afford a 30% down payment, prompting the government to push through further legislature that gives low-income Saudi's loan subsidies in order to purchase residential property and reduces capital requirements to 15% of the homes total value.

Despite government efforts, demand continues to vastly surpass supply, and the government is increasingly turning to the private sector to assist in funding. This will require an overhaul of the public sector to provide improved policies, incentives and regulations that will attract potential investors. Currently, few aspects of the government's regulatory system are transparent, and there is a dearth of reliable data. Tax, labour laws, and policies tend to favour high-tech transfers and the mandatory employment of Saudi citizens, as opposed to allowing open competition between all candidates, which can be problematic for foreign investors. Bureaucratic procedures are cumbersome, and the red tape can take a significant amount of time to overcome. Furthermore, corruption continues to pose a significant problem to the commercial climate. The Kingdom ranked 55th out of 175 surveyed countries by Transparency International in 2015.

Challenges in the bank lending system further hinder the ability of the private sector to enter the real estate market. Saudi's current Islamic banking system does not adequately support the whole real estate sector, and since the financial crisis of 2008 most banks have become increasingly cautious when it comes to providing loans and mortgages. In the wake of 2008, banks have also tightened their lending policy and refrained from lending to companies based solely on the borrower's name and reputation.

Finally, an issue which relates to the Saudi Arabian economy as a whole, but with particular effect on government revenues, fiscal policy and therefore infrastructure spending, is the economy's reliance on the hydrocarbon industry and vulnerability to oil prices. Despite lagging oil prices the government has been persistent with its development initiatives, resulting in a US$ 98 bn deficit in 2015, doubling analysts projections. Historically, and particularly during the past decade, Saudi Arabia has routinely overspent budget projections by more than 20%. This marks the highest projected deficit in the Kingdom's history and given the most recent projections on the price of oil futures and government reluctance to increase production levels, the Saudi government has reason to fear a tight fiscal situation moving forward in the short term.

SWOT CHART

Strengths

• Efforts to boost religious tourism have translated into higher budget allocations towards the hospitality and infrastructure sectors. This is expected to result in a further increase in construction activities in the short and medium terms.

• State expenditures in virtually all infrastructure sectors are booming; projected investments include US$ 67 bn worth of housing projects and over US$ 80 bn worth of transport infrastructure.

• Strong government support for the real estate sector, particularly as a means to diversify the economy and create jobs and homes, as represented by the efforts of King Salman, the Saudi Arabian General Investment Authority, and the Real Estate Development Fund.

• Easing of restrictions previously placed on foreigners in the real estate market, namely through property laws that now grant foreigners 100% ownership on purchased property.

• Largest real estate market in the GCC, with more commercial floor space than all of the other GCC countries put together.

Weaknesses

• Large amounts of undeveloped "white land" within the country's major urban centres have resulted in housing shortages, artificially high land prices and a stagnant residential and commercial development market.

• The country remains reluctant to invest in renewable energy sources in the short-term, leaving the country heavily reliant on oil in the long-term.

• Only about 35% of Saudis are homeowners, and average land costs account for around 60% of total property value in many of the countries major cities. The government needs to address both land and housing shortages in the short-term to simulate further development.

• Saudi favouritism for a collection of major domestic and US-based contractors has rendered entry into the market for construction and infrastructure projects difficult for medium-sized contractors.

• Real estate developers looking to incorporate sustainability (site design, solar energy, natural light, etc.) into their designs could meet with a lack of public and governmental understanding and support.

• A severe housing shortage, particularly within the affordable housing segment, leaves market demand unmet.

Opportunities

• The Saudi government plans to make significant investments in the country's infrastructure through 2025, with tenders and project opportunities across virtually all sectors of the infrastructure and construction industries.

• A recently proposed law that would tax undeveloped "white land" aims to incentivise developers to build on these plots, offering opportunities for development projects while further expanding the construction and real estate industries.

• Over the years Saudi Arabia has emerged as an international tourist hub for leisure travellers, international shoppers, and pilgrims. Growth in the tourism sector is expected to spur further growth in the country's infrastructure and construction sectors.

• A recently approved mortgage law will improve the regulatory environment for banks to lend, making it easier for homebuyers so secure loans. This will result in an increased demand for residential real estate and construction services.

• 375,000 homes need to be built annually through 2020 to meet demand in the under-supplied middle- and low-income residential segment.

Threats

• Government policies are not always predictable, as demonstrated by the recent shift in focus from developing big industrial cities to developing the country's infrastructure and affordable housing supply.

• Volatility of world oil prices could put pressure on Saudi oil revenues, affecting fiscal policy and sector investments.

• The Kingdom has a significant shortage of affordable housing, with shortages estimated between 1.5 and 5 million units. This has already prompted many citizens to air their frustrations on social media, with further social unrest imminent if the problem is not remedied.

• The country needs to secure a reliable supply of key building materials such as cement or face shortages and susceptibility to price shocks.

• A severe shortage of residential units coupled with the new mortgage law adversely affecting the Kingdom's poorest citizens could translate into rising unrest among the country's large low-income segment.

PROJECTIONS

Economic Projections

	2019	2020	2021	2022	2023
Country GDP (US$ bn)	703.2	721.5	742.4	760.0	775.6
GDP Growth (%)	2.6	2.9	3.3	3.5	3.1
GDP per Capita (US$)	25,637	26,303	27,066	29,050	29,544
Population (mn)	33.9	34.6	35.2	35.7	36.3

Source: Noozz

Industry Projections

	2019	2020	2021	2022	2023
Construction Sector Value (US$ bn)	68.7	76.7	80.2	81.3	82.4
Construction Sector Growth (%)	7.7	8.3	8.4	6.7	7.1
Construction Industry Value to GDP (%)	6.5	6.6	6.9	7.0	7.1
Real Estate Industry Value (US$ bn)	142.5	148.2	151.0	155.4	161.3

Source: Noozz

NEEDS ASSESSMENT

• The government needs to open up the playing field to bids from a wider range of sector players. The government's preference for a handful of domestic and US-based contracting firms has effectively closed the market to competition. In order to promote competition and attract new investments the government will need to open its project and tender markets to qualified regional and international firms.

• A growing population and economy means that sustained investments in infrastructure will be needed in both the short and medium terms. Significant investments in housing, transport, and water infrastructure are needed to keep up with growing population demand

• A supply gap in the affordable housing segment and artificially high land prices signal a need for reform within the commercial and residential real estate sector. Owners of vast amounts of undeveloped "white land" need to be incentivised to build on or sell the land rather than keeping it as a store of value.

• The government needs to continue to develop its mortgage and treasury market. The lack of a developed treasury market has prompted the country's middle class to invest in land, resulting in high land prices and a stagnant construction market. Additionally, the lack of a unified mortgage-lending framework has resulted in low levels of homeownership.

• Continued progress towards economic diversification should continue to reduce the economy's reliance on hydrocarbons. The government should continue pumping investment into industrial cities and other projects to create jobs and promote new industries.

• Countries throughout the MENA region have embarked on ambitious infrastructure development programmes. This has resulted in price spikes and shortages for key building materials such as cement, steel and aluminium. Saudi Arabia needs to ensure maximum domestic production levels of these materials or face susceptibility to price shocks.

• As the Saudi population continues to rise, the need for affordable housing will increase accordingly. The Saudi government must continue building low- and middle-income housing for its growing youth population and will have to include the private sector in construction in order to quickly and efficiently build 375,000 units annually through 2020.

• Saudi Arabia must make a more concerted effort to aid the low-income segment after the passing of the new mortgage legislation law, as the country's poorest citizens remain unable to secure housing loans and rental rates continue to climb.

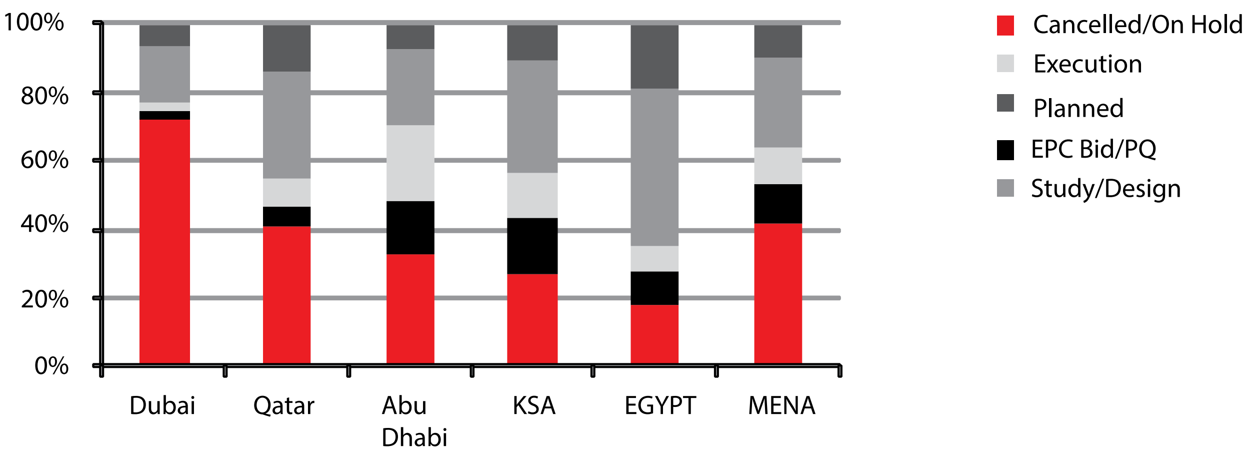
• Demand for retail space continues to rise as the country's large and growing consumer base continues to attract international and regional brands. There is also a need for new and novel retail concepts that reflect country's cultural sensitivities as shopping and retail remains the Kingdom's premiere leisure activity.

• In terms of planning for commercial space, the government will need to take into account the current oversupply of office space coupled with the fact that commercial space is expected to increase by almost 50% over the next 2-3 years. The country will need to continue to attract regional and international businesses if it is expected to absorb its commercial supply overhang in the medium term.

MENA-WIDE OVERVIEW

A total of US$ 4.3 tr is expected to be spent on construction in the MENA region over the next decade, representing growth of 80% to 2020. Experts anticipate a particular emphasis on the development of affordable housing. Following the global financial crisis and the Arab Spring, the market suffered throughout most of the region. US$ 1.6 tr worth of projects were cancelled around the region between 2009-2014, and US$ 23 bn worth of North African projects had been put on hold, including many in Libya, as of late 2015. Despite these initial setbacks, the infrastructure and construction sectors are poised for growth in the coming years.

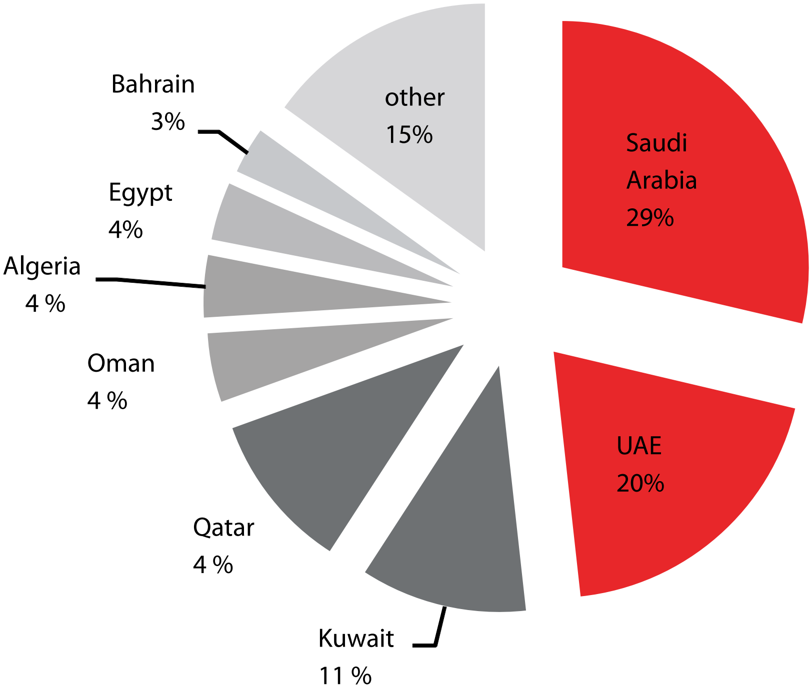
MENA Projects by Location



Source : Global Research

Infrastructure in the MENA region is not as developed as the construction or real estate sectors. At the 2010 World Economic Forum, government and business leaders noted that the region must overcome its infrastructure deficit if it is to boost its competitiveness and attract much-needed foreign investment. According to the World Bank, the MENA region needs to invest between US$ 75 and US$ 100 bn in infrastructure annually to sustain growth rates achieved in recent years and boost economic competitiveness. Saudi Arabia's contribution to regional expenditures in the sector remains the one of the highest in both the MENA and GCC region. In 2014, the UAE surpassed Saudi Arabia as the largest regional construction market with an estimated US$ 16.2 bn worth of projects in the pipeline. Although small by comparison, Bahrain's construction market has been steadily increasing in recent years with over US$ 4.7 bn worth of development projects in the pipeline in 2014.

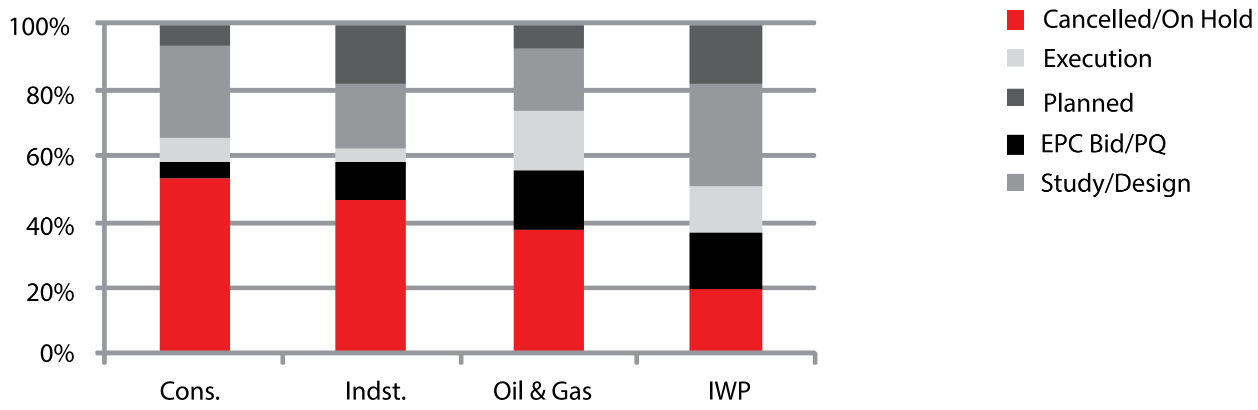
Backlog Market Share



Source : Global Investment House

As a whole, the GCC countries account for over US$ 1.6 tr worth of construction projects to be completed over the next decade, equal to over three-quarters of the region's project pipeline. The construction market is currently undergoing a comeback after a period of economic volatility. The collapse of the Dubai real estate market momentarily brought the construction industry to its knees, as projects were abandoned, investors pulled out, and companies suffered high losses. However, government interest in construction projects following regional unrest in 2011 has helped revive the sector, particularly in countries like Bahrain, where the potential for political unrest is imminent. Demographic factors, economic growth and state pursuits of a diversified economy are all propelling growth. A considerable wave of projects across the Middle East has turned the region into the world's biggest market for construction machinery, vehicles and equipment.

MENA Projects by Segment



Source : Global Research

Regional cement and steel production have also followed a similar upward trend, as massive investments in construction projects have fuelled demand for building materials. With regional demand for steel expected to grow between 8-10% per year, many countries have boosted domestic production, with Saudi Arabia notably expanding capacity by at least 50% within the coming three years. To stave off the wave socio-economic discontent engulfing its neighbours, the government has attempted to pre-empt the forces of political unrest by launching development plans aimed at stimulating employment, in some cases adding to the volume of expenditures proceeding to the region's construction markets. As instability persists across the region, Egypt and its neighbours will continue to devote large sums to investment in infrastructure, fuelling the construction sector demand for building materials region-wide.

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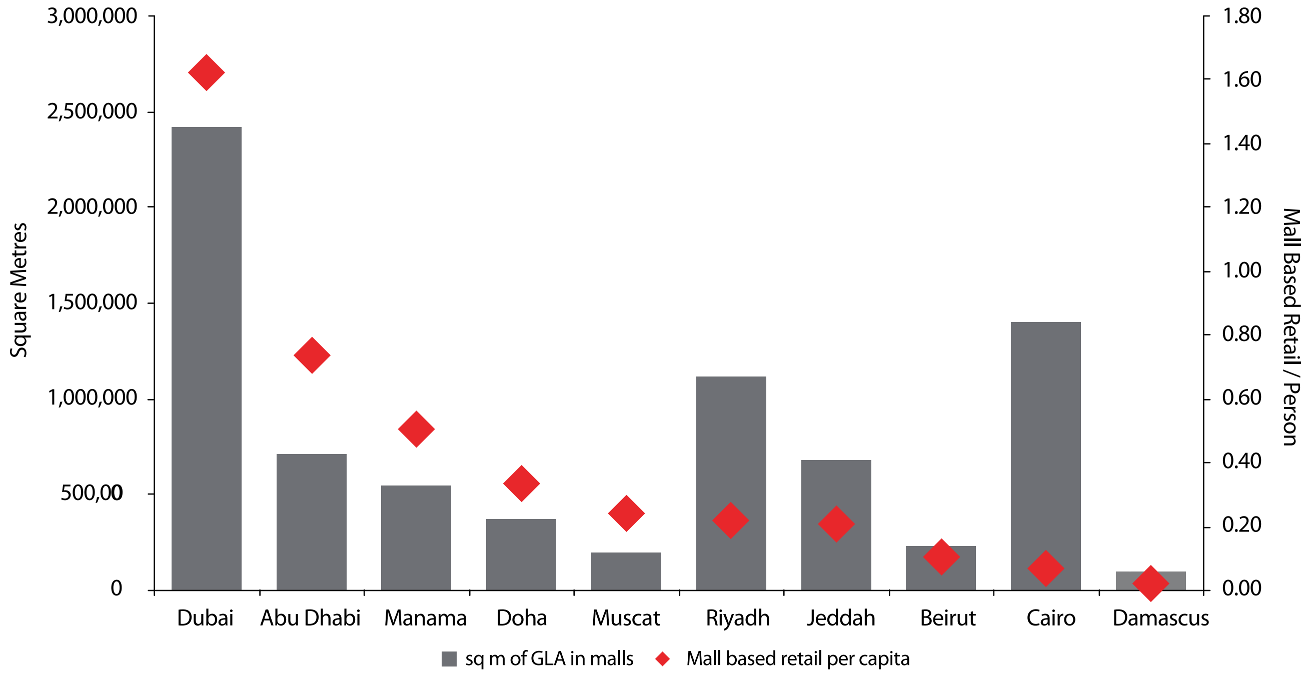
Shortage of Affordable Housing in MENA

Country	Total Supply	Total Demand	Shortage
Egypt	15,400,000	16,900,000	1,500,000
Iraq	1,900,000	2,900,000	1,000,000
Morocco	2,800,000	3,400,000	600,000
KSA	2,300,000	2,700,000	400,000
Bahrain	190,000	230,000	40,000
UAE	370,000	390,000	20,000
Oman	285,000	300,000	15,000
Total	23,245,000	26,820,000	3,575,000

Source : Jones Lang LaSalle

Retail Space Supply (Egypt vs. MENA)



Source : Jones Lang LaSalle

Saudi Arabia offers relatively attractive opportunities for investors, although the government has historically demonstrated a reluctance to partner with private sector enterprises to carry out ambitious development plans. The range of projects in the pipeline, from desalination plants to railways, and clean energy initiatives, presents an array of opportunities that will require the involvement of specialised investors, contractors and consultants to be successful. While Saudi Arabia's business environment remains an obstacle, the country's push for development in infrastructure, tourism and residential housing will make the domestic construction sector one of the most promising region-wide in the near and medium terms.