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SAGA Views and News

Welcome to this edition of SAGA Strategies' newsletter! In this issue, an important brief on trends shaping real estate in the region along with some relevant news links for you to browse through.

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Investing in Real Estate – Trends Shaping the Industry

For better or worse, real estate is the asset class of choice for investors in the GCC, particularly Saudi Arabia. It has its charms. It's a real asset - values and prices have a long-term upward trend, assets can be passed down generations, and investing can be done through a host of efficient vehicles.

Contrary to popular belief, most of the wealth held by GCC citizens is in their home country and most of that wealth is in real estate. So let's look at a few trends that should be noted when considering investment in real estate (with a view to the region):

Amenitization. Over the past decade, there has been marked shift toward mixed-use development. Gone are the days where distinct segregation between work, leisure, accommodation, health services, etc. were the norm. Nowadays, people (especially the millennial generation) prefer to have integrated communities that allow for all services within close proximity.

Redefinition of Retail. Retail property is moving from merchandise driven marketplaces to programmed experiences integrating lifestyle, socializing, and dining pursuits with shopping. Placemaking, differentiation and curating are the order of the day for landlords and developers. Traditional shopping centers (managed by developer behemoths such as Simon Properties) are ditching department stores and metamorphosing into mixed-use destinations offering entertainment and technology-enhanced shopping.

Transformation of Logistics. Rapid change is happening in the warehouse and logistics sectors as more commerce is fulfilled away from stores and as warehouses evolve into 'fulfillment centers' for e-commerce. Supply chains are being restructured and location drivers are more critical and also require 'last mile' and 'last minute' delivery capabilities.

Within industrial buildings, the use of automation has grown. Adoption will continue to rise as technology improves, although the nature of distribution—with its picking complexity, variability, and seasonality—limits the investment return for robotics in this region with inexpensive unskilled labor. We also note that artificial intelligence and predictive analytics will have a big impact on how retailers and distributors optimize inventories.

Additional automation is being considered in the form of drones as deliverers. A startup company in the UK is even looking at making take-off and landing hubs for drones on rooftops in densely populated areas.

Co-Working Comes to the Middle East. WeWork is now deploying in the GCC, on the back of generous funding from Softbank and its PIF-backed Vision Fund. While in the UK and North America they have loaded up their balance sheet with 10-20 year lease liabilities, in this region WeWork is looking to expand on the back of landlord-funded management deals which replace the lease liabilities with long term management income. A big question is how dense, open-plan workplaces will work in car dependent cities and where local culture has a tendency to use

more space.

Core and Core+ Have Become Expensive. With huge amounts of mainstream and peripheral capital chasing yields from income-generating assets, the less risky end of the spectrum of real assets have gone up in prices and cap rates have gone down. Put another way, for the same amount of risk, investors are getting less returns.

High Supply. All across the world markets have been absorbing a wave of capital from institutional and cross-border investors which is being reallocated from equity and fixed-income assets. As a result every city has seen ambitious new urban development projects. The corollary of all this supply is that locations and buildings that might have been considered Class 'A' ten years ago might be approaching relative secondary positioning, especially when the impact of new 'millennial' preferences are factored in. Sensitive readings of the local landscape remains an essential discipline for investors.

PPP. Public Private Partnerships come in to vogue as both governments and private sector stakeholders realize the more diversified and managed way to investment returns is to have different (even antagonistic) parties. PPP investment projects also provide salient benefits such as tax exemption, long-term yields and succession planning.

A wide range of real estate and infrastructure PPP opportunities are being discussed and promoted in the GCC. In the past regional governments have not always been able to structure these to be attractive for investors. Still, the scale of opportunities from transport, urban development and new economic cities has a number of global investors and operators watching with interest.

Investing in real estate can be achieved via a variety of vehicles – direct, managed account, fund, REIT, club, etc. – and, in fact, a well-balanced portfolio should have strategic allocation exposure to these different vehicles. The aforementioned trends, however, highlight how important it is to be involved in selecting the right sub-asset classes to achieve appropriate risk-adjusted returns.

Interesting News

- [\(Forbes\) What is a Virtual Family Office](#) - A brief description of a trend many family offices are increasingly following - the Virtual Family Office.
- [\(Barrons\) Family Offices Continue to Favor Private Equity for High Returns](#) - Private equity funds will continue to appeal to family offices for their potentially high returns, with the average allocation projected to rise 73% next year from 2017. Family offices' increasing investment in private equity is primarily driven by the consistent, oversized return of this asset class.
- [How Asia's new money is driving boom in 'family offices'](#) - The family office is a relatively new concept in Asia, with less than 500 such entities, compared to thousands in the West. But more and more people are realizing they offer a comprehensive solution to managing wealth, including investments, charitable giving, taxation and wealth transfer.