Evolving Dynamics
Makkah Retail Overview
Kingdom of Saudi Arabia
Summary

The holy city of Makkah is currently going through a major strategic development phase to improve connectivity, increase capacity, and enhance the experience of Umrah and Hajj pilgrims throughout their stay.

This is reflected in the execution of several strategic infrastructure and transportation projects, which have a clear focus on increasing pilgrim capacity and improving connectivity with key projects, including the Holy Haram Expansion, Haramain High-Speed Railway, and King Abdulaziz International Airport.

These projects, alongside Vision 2030, are shaping the city’s real estate landscape and stimulating the development of several large real estate projects in their surrounding areas, including King Abdulaziz Road (KAAR), Jabal Omar, Thakher City and Ru’a Al Haram. These projects are creating opportunities for the development of various retail formats that target pilgrims.

Makkah has the lowest retail density relative to other primary cities; Riyadh, Jeddah, Dammam Al Khobar and Madinah. With a retail density of c.140 sqm / 1,000 population this is 32% below Madinah which shares the same demographics profile.

Upon completion of major transport infrastructure and real estate projects the number of pilgrims is projected to grow by almost 223% from 12.1 million in 2017 up to 39.1 million in 2030 in line with Vision 2030 targets.

Importantly the majority of international Pilgrims originate from countries with low purchasing power. Approximately 59% of Hajj and Umrah pilgrims come from countries with GDP/capita below USD 5,000 (equivalent to SAR 18,750). This translates directly into the central area tenant mix which comprises value to mid-range brands concentrated in jewellery & accessories and apparel collectively accounting for c. 57% of the central area mall GLA.

Outside of the central area the City lacks regional/super regional malls with the existing supply mainly comprised of traditional retail centres averaging 16,000 sqm. Tenant mix in the resident malls is mainly focused on fashion (51%), health & beauty (8%), and entertainment (12%). Limited new brand exposure combined with the aging quality of existing entertainment and experience offerings in these malls is one of the draws motivating Makkah’s residents to shop and dine in Jeddah.

It’s important to note that the magnitude and the scale of retail opportunities are subject to developers/retailers ability to balance the formula of both pilgrims and residents. New developments must also compete with mixed used projects in the neighboring cities: Jeddah, King Abdullah Economic City (KAEC), and Madinah.

In this paper, we will shed light on the evolving market dynamics of Makkah’s retail sector, which covers changes in the structure of the retail landscape, supply and demand dynamics, potential opportunities and challenges ahead, and the outlook of the sector.
Retail Landscape

Makkah’s local economy is highly dependent on seasonal pilgrim visitations and modest local industries. Therefore, retail demand is generated from two distinct segments:

1) Makkah residents
2) Hajj and Umrah pilgrims

This has shaped the retail landscape of the city into the following:

- **Shopping centers** mainly serving pilgrims concentrated in the vicinity of the Holy Haram (between the First and Second Ring Roads) and Masqaer Al Muqadassah (Mina and Jamarat) along Al Masjid Al Haram Road.
- **Retail centers** serving Makkah’s residents are mostly scattered outside Third Ring Road, in northwest and south Makkah, and close to well-established residential areas.

Introduction
Makkah has a shopping mall supply of 140 sqm per 1,000 persons. This is significantly lower than other primary cities considering that the holy city received c.8.5 million international pilgrims in 2017 (c.6.8 million Umrah pilgrims and 1.7 Hajj pilgrims).

The city has considerably lower shopping mall density than Madinah (-32%), even though Makkah has a larger population base (43%), a higher number of international pilgrim visitations, and shares similar demographic and income level structure.

Makkah’s market is nascent and lagging behind, suggesting that there is either untapped potential for the development of shopping centers or market conditions are challenging to support supply growth.

Makkah’s mall density is 32% lower than that of Madinah, despite sharing the same demographic profile.
**Supply Structure**

77% of Makkah’s retail supply is fragmented, comprising traditional souqs and line shops, whereas showrooms and organized retail (i.e. shopping malls) account for the remaining 23%.

**Ownership Structure**

Makkah’s top 5 developers account for 49% of the city’s total mall-based supply. We expect to see more consolidation in the future (akin to the potential merger between Jabal Omar and Umm Al Qura), and large-scale developers will likely continue to develop a sizable portion of the future supply.

**Shopping Mall Breakdown by Category**

The majority of Makkah’s small shopping malls comprise mostly community centers, ranging in size between 10,000 and 30,000 sqm. Regional malls represent only 15% of Makkah’s total organized retail supply, while the remaining 85% is provided by community centers. Riyadh, Jeddah, and Dammam / Al Khobar’s retail supply is weighted more toward larger centers.

**Key Challenges**

Mainly attributed to the following factors:

1. Shortage of suitable land plots for mall developments,
2. High land prices relative to other cities; hence less commercial viability of horizontal regional and super-regional malls,
3. High infrastructure cost given Makkah’s mountainous topography, and
4. Residents’ preference towards shopping in Jeddah.

**Plenty of Space in the Pipeline**

Increasing pilgrim visitations coupled with the completion of major infrastructure projects are expected to drive the development of shopping malls in Makkah city, mainly within close proximity to the Holy Haram. We expect this trend to intensify in the medium to long-term, as key retail projects in the planning stages are scheduled for construction in the coming years. Shopping mall supply is expected to increase from approximately 280,000 sqm to 338,000 sqm in 2020, to reach 804,000 sqm by 2025. Major projects accounting for a significant share of this future supply include the remaining phases of Jabal Omar, shopping malls within KAAR project, Muzdifah Mall by ACCL (Al-Hokair Group), and Abraj Kudai.
Top ten market feeders for international Hajj and Umrah visitation in 2017 was c. 6.1 million, equating 72% of total international visitation (c. 8.5 million in 2017) and 47% of total domestic and international pilgrims (c. 12.1 million).

The majority of international pilgrims originate from countries with low purchasing power. 66% of international Hajj & Umrah pilgrims come from countries with GDP/capita below USD 10,000 (equivalent to SAR 37,500) and 59% with GDP/capita below USD 5,000 (equivalent to SAR 18,750).

**Consumer Focus**

Shopping behavior and income profile of international visitors have greatly influenced the tenant mix in the central area. It is strongly focused on traditional offerings comprises value to mid-range brands concentrated on jewelry & accessories and apparel, which collectively account for 57% of the central area mall GLA.

On the other hand, domestic and GCC visitors accounted for 30% of the total visiting pilgrims in 2017. These pilgrims have stronger purchasing power compared to their international peers and have an average GDP/Capita of c. USD 23,773 (SAR 89,147). Brands with higher positioning (premium and luxury) are within the affordability range of domestic and GCC pilgrims. However, luring this pilgrim group to shop in Makkah is challenging as they prefer their home countries/cities, which has more diverse and innovative retail offerings.

Domestic and GCC pilgrims spend more on gifts, souvenirs, and F&B. The latter is underserved in Makkah and mainly focuses on moderately priced express F&B concepts and expensive hotel restaurants with a lack of casual dining concepts.

**Looking Forward**

Significant increase in pilgrim visitation is expected to fuel growth in pilgrim spending, therefore creating opportunities for retailers and developers. However, developers and retailers need to be aware of the increasing competition from alternative options in destinations such as Jeddah, Madinah, and potentially KAEC, which also offer retail components targeted toward pilgrims. Regional competition is expected to intensify when the Haramain High-Speed Railway becomes fully operational.
Consumer Profile – Resident Segment

Lowest Shopping Mall Density Relative to Primary Cities & Madinah

With the Holy City’s smaller population, worker base and spending power, its residents’ retail spending is lower than that of other major cities (Riyadh, Jeddah, and DAK (Damam Al Khobar). Makkah’s lower retail density suggests that the city is underserved and has not realized its full potential. However, it could also be an indication of the lack of retail choice driving consumer spend elsewhere.

Retail Mix

Fashion accounts for approximately 51% of the total merchandise mix in shopping malls, followed by indoor family entertainment (12%) and health & beauty (8%). Fashion stores in Makkah are mainly positioned around value to mid-range brands, with the later mostly available in well-established malls such as Makkah Mall and Hijaz Mall.

Additionally, there’s a limited presence of local emerging brands as well as fresh concepts that are starting to build a strong client base in major cities such as Jeddah and Riyadh. However, Makkah’s market is dominated by mainstream brands which often do not fully cater to the aspirations and needs of the younger generation.

Makkah has a lack of large and modern retail shopping centers that offer a balanced mix of retail categories. The city’s existing supply primarily comprises traditional retail centers with an average size of c. 16,000 sqm. Entertainment offerings in the existing malls lack fresh and unique entertainment experience which could strongly motivate residents to shop and dine in Jeddah.

Looking Ahead

The number of pilgrims is expected to rise over the next few years, reflecting the Saudi Vision 2030’s goal to increase the contribution of non-oil sectors to GDP. The completion of key infrastructure and masterplan projects, coupled with the expected increase in pilgrim visitations, will likely act as a catalyst in driving job growth in Makkah, translating into higher retail spending and future demand by residents. Furthermore, resident population is set to grow by 25% over the coming 15 years which will further support retail spending and demand in the future.

However, to compete with existing regional destinations developers will need to offer a shopping destination with fresh tenant mix and exciting entertainment concepts that addresses the needs and aspirations of young and dynamic shoppers.

“Makkah’s residents prefer to shop in Jeddah due to the city’s retail quality and diversity. However, the city’s shoppers could be retained if their needs are fulfilled.”

“Key infrastructure and masterplan projects in the construction pipeline are expected to give a substantial boost to the local economy upon completion, which will in turn strengthen the purchasing power of Makkah’s residents.”

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The devaluation of currencies in major feeder markets shrunk the purchasing power of pilgrims from those markets (such as Egypt and Turkey), resulting in lower retail spending. The fall has affected the performance of shopping malls situated within the Central Area, leading to a modest decrease in rental rates in the last year.

This concurrent trend should ease in the coming years, as the number of religious visitors is expected to increase from c.12 million in 2017 to 16 million in 2020, ultimately reaching c.30 million by 2030. As such, existing participants may benefit of demand growth potential in the short-term and retailers may be willing to pay escalating rents given that over the short term, only limited supply will enter the market within the Central Area.

However the dynamics could change with the arrival of new supply which is expected to enter the market by 2025 leading to intensified competition.

Makkah’s resident mall market is facing several headwinds, including rising inflationary pressure and increased competition from Jeddah, translating into downward pressure on rents and occupancy. However, regional shopping centers are in short supply, and their demand outstrips supply, and have maintained a leading position with stable rents and occupancy.

In the medium to long term even larger exiting malls may be susceptible to changing dynamics as new malls will likely induce demand from existing old malls, creating downward pressure on rents and occupancy level.

The strength of the Saudi Riyal against other currencies, a drop in the number of pilgrims, and ensuing reduction in retail spending combined to play a central role in modest drop in rates within the Central Area.
Major Trends & Opportunities

Emergence of New Pockets Suitable for Mall Developments

Upcoming masterplans in the Central Area, such as KAAR and Thakher City, are currently in the infrastructure stage and expected to unlock new land supply. Upon completion, they will be well connected to the Holy Haram and major transportation projects, including the HHSR (Haramain High Speed Railway) and the proposed metro network (currently in planning). This is expected to create an opportunity for the development of shopping malls that cater to on-site residents and pilgrims.

Expansion Toward the Edges of the City

The Saudi Government plans to reduce pressure on the Central Area by relocating residential districts to the Bawabat Makkah Grand Masterplan (in western Makkah), which has stimulated the development of new masterplans in the area. Furthermore, several new masterplans in the west and south have been recently completed. These projects are expected to offer large and reasonably priced lands suitable for mall developments.

However, these masterplans are still vacant and are not expected to witness any major development activity in the short-term, as such this opportunity will become more relevant once the critical mass is built over the medium to long-term.
Strong Preference for Horizontal Malls

The majority of Makkah’s shopping malls are vertical structures comprised of three to five floors, with small floor plates given the city’s mountainous nature and high land prices, which have always been a setback for horizontal malls. However, shoppers and tenants alike are drawn to malls with horizontal layouts, large floor plates and wide corridors, with easy circulation and enhanced shopping experience. Shopping mall’s horizontal configurations can also differentiate their offerings from the competition. Therefore, with the emergence of reasonably priced lands introduced by upcoming masterplans, there will be strong opportunities in the development of horizontal malls.

A Wider Variety of Offerings

Given the varying shopping patterns between pilgrims and residents, strong emphasis is recommended to be placed on positioning to cultivate a tenant mix that caters to the needs of the target market. Pilgrims mostly prefer local brands with unique product offerings, including health & beauty (e.g. oud), gold & jewellery, and souvenirs. Meanwhile, residents favor contemporary offerings by prominent international retailers in fashion, electronics and technology. Therefore, shopping malls are advised to have a combination of traditional and contemporary offerings alongside local and international brands to cater to both segments. The mix, however, will vary depending on the mall location to their target market.

Entertainment & Leisure a New Differentiation Strategy

The majority of Makkah’s shopping malls feature food court space, but only a few malls feature casual dining restaurants. Additionally, the market lacks fresh F&B concepts that are gaining popularity in Jeddah. Furthermore, indoor family entertainment areas generally have a homogenous feel with little innovation.

Given the government’s emphasis on promoting leisure and entertainment activities as part of the Saudi Vision 2030, more space could be dedicated to express F&B outlets, casual dining restaurants, and unique family-oriented entertainment concepts. The combination of these factors is essential to differentiate new shopping malls from traditional centers, to fend off competition from Jeddah, and to retain Makkah’s resident shoppers.
Outlook

Short-term Outlook

- Makkah’s elevated pilgrim capacity and completion of major infrastructure projects will likely stimulate retail spending.
- Existing developers will likely reap the benefit from easing of visa quotas as major retail projects in the pipeline are expected to take a number of years to enter the market, which will likely translate into higher sales density in properties near the Holy Haram and Mashar Al Muqaddasa.
- Jeddah, however, will continue to capture a significant portion of Makkah’s resident retail spending, given the diversity and scale of its offering. Still, rental rates of prominent resident shopping malls in Makkah are expected to hold up and to increase modestly in the short-term.

Medium to Long-term Outlook

- Competition will likely intensify as a large supply of shopping malls is expected to enter the pilgrim market, thus developers/landlords are expected to reduce rental rates.
- Several large-scale projects, including regional/super regional malls, are planned to enter the market. These developments are expected to feature retail offerings that focus on creating a destination for shopping and family entertainment, where people not only shop but also dine, socialize and have fun in a way that responds to the needs of the local community while respecting its culture and values.
- However, projects of this scale and magnitude in Makkah remain untested. As such, they are expected to be released over phases to gauge market capacity.
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