

Analysis of the Real Estate Market in Dubai - A Macro Economic Perspective

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Abstract

Dubai, the most economically active of the seven Emirates of the UAE has grown to be a major investment and trade centre in the Middle East. The foresight and the business-like manner in which the ruler of Dubai, Sheikh Mohammed bin Rashid Al Maktoum invested in infrastructural development of Dubai had indeed attracted the attention of the international investment community, which in turn responded with a steady inflow of FDI into Dubai economy over the years. The real estate sector has been a major beneficiary of this bold economic initiative. Investors from all over the World (Including those from the USA, UK, JAPAN, Saudi Arabia etc.) enjoyed a steady stream of high dividend yielding returns on their investments which was sustained until the economic crises which started immediately from Post George Bush tenure in the USA. According to reports from Dubai Government bureau of Statistics, the real estate sector steadily contributed about 22.5% of the GDP of Dubai Emirate (the biggest of such contribution from a single source). This trend remained constant until year 2008 due to the global economic crises which started in the USA real Estate sector and spread to all other federating components of the Economy.

A major collateral result of this was a strong decline in oil prices and the fall of the US dollar coupled with huge losses in stock markets. Among the after effects was evaporation of savings and liquidity of cash in the global financial sector, hence, investors lacked the capacity to invest and those with capacity were too afraid to invest. Thereupon, Dubai's debt financing rely mainly on sales of properties and real estate assets i.e. meaning urgent needs for cash liquidity by investors who lost their purchasing power due to the crises. This resulted to excessive offers of properties for sale in the market (from the supply side) with unavoidable sharp drops in their prices and also value, but with poor reaction for purchases from the demand side, there by shrinking the profit in the sector in terms of margin and potentials. Consequently, a sharp decline in demand and in returns on investment in the Dubai real estate sector continued until recently.

A combination of factors in the Dubai economic management strategies supported by good public policy initiatives and capital injection from the central Government in Abu Dhabi, have all helped in witnessing an economic re-birth in Dubai again, resulting to an upward increase in the demand for big tickets items especially, real estate assets. This increase in demand had also caused a price increase in the market which had now jolted the sector to the extent that, developers and contractors alike are now scrambling for a piece of the action in the Dubai real estate market again, because of its sales potentials and the inherent profit expectations. Hence, supply is increasing accordingly and much to the joy of the financial sector in the UAE, especially in Dubai.

Keywords: Real Estate, Macro Economic, Dubai

Introduction

Dubai has seen few economically prosperous times and thanks to the rise of oil prices; resulting in increased demand by Gulf investors and international investment community in the real estate sector, Dubai has mastered the art of architecture in terms of building design, engineering and luxury projects, it became the financial center of the region, and was nick named (Singapore of the Arabs). Numerous festivals have been held and so were many more activities that attracted tourists, traders, businessmen, moviegoers and art enthusiasts, making it the Gulf pearl and the bright sunlight for the Arab States

Dubai was able to achieve economic break-through in the region through the efforts and the ambition of the department of housing and urban development of the city, Managed as if it's a private profit making company, the department has a president, a Board of Directors and a team of experts in multiple areas. This reflected in high investment strategy offering a climate of high levels of facilities in all areas, especially, the presence of a strong renaissance in the real estate sector. This fact had contributed to the speed of positive achievement of investors' objectives. Furthermore, the government took a big step in allowing freehold in several projects and the freedom to invest in large projects in wider geographic areas, this in turn generated the ideal relationship between the investor and the government of Dubai in particular, and the UAE in general.

As a starter, Dubai succeeded in minimizing bureaucracy in Government management, and this facilitated the development plans of reconstruction, new construction, credit facility and various investments. Dubai's rulers have managed to sustain it that way without any major problems within the European Union, or with neighbors such as other Gulf countries, Dubai became a model of inspiration for many countries in the region, imitating the same concept in the real estate and financial services and even in the development of tourism.

Dubai Real Estate Market

Real estate has the biggest contributions to the economy of Dubai about 22.5% of Dubai's GDP, arising from various factors. However, Dubai real estate market has experienced a big decline in the fourth quarter of 2008, the decline in the economy occurred from internal and external economic issues which led to a major financial crisis, accompanied by a strong decline in oil prices and the fall of the US dollar coupled with huge losses in stock exchanges. The outcome was the end of liquidity era and its sources; thereupon, Dubai's debt financing rely mainly on sales of properties and real estate assets i.e. meaning urgent needs for liquidity by investors who lost their purchasing power. Therefore, house prices dropped by 25% in the second quarter of the year 2009, and also a sharp drop in rent revenues occurred. Thus, the real estate sector received a hard hit which resulted in a halt in high-cost investments.

Thereafter; signs of indebtedness emerged from the inability of investors to sell the high valued premium assets.

Demand factors in real estate markets

Population

Population size, distribution and demographic development are all encouraging consistent migration to this part of the world. Population fluctuations have a major impact in the market value, market demand and market fluctuations which occur also due to stable job opportunities. Therefore, Dubai is expecting a population increase by 0.421 million people in the next few years, which means an annual increase of 0.1068 million within 3 years

GDP, population and per capita GDP

	2000	2001	2002	2003	2004	2005
GDP	62,335	65,669	77,091	88,766	104,772	116,879
Population	0.862	0.910	0.961	1.014	1.071	1.321
GDP per capita	72,282	72,137	80,223	87,508	97,847	88,447

Income and Availability of financing

Simply put, the more the income the more the purchasing power, this in turn means more demand for real estate assets. The less the income, the less the purchasing power i.e. less demand for high priced items such as real estate. Steady Increase in income leads to steady increase in Commercial activities and business transactions, which when combined increases number of activities that grows the Economy and expand businesses, meaning more demand for private and commercial properties. Most property purchases are via financing due to affordability factor; consequently, demand is related to both prices and availability of financing. In other words, if lending costs increases, less people will be able to afford property purchases. Therefore, there will be less demand for properties.

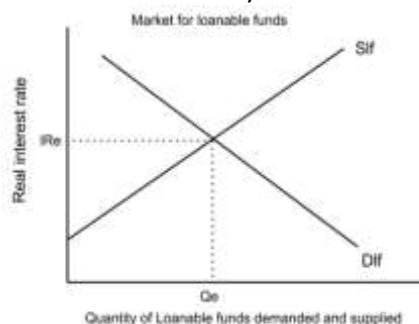
Supply factors in real estate markets

Costs of production inputs

When the cost of land, labor and construction materials rises, the quantity supply will decrease at a given price. Land prices play a significant role in rising real estate costs in Dubai. Prices could increase due to the location of the land and/ or the availability of infrastructure.

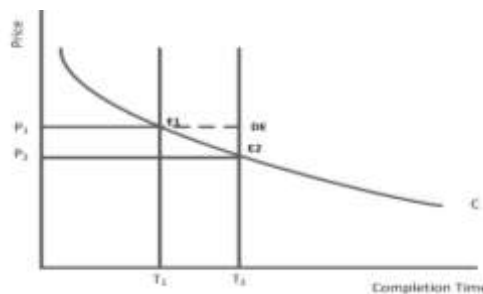
Cost of financing

Just like on the demand side, supply of properties require availability of cash liquidity and or financing. (See the graphical illustrations below).



Technological know-how

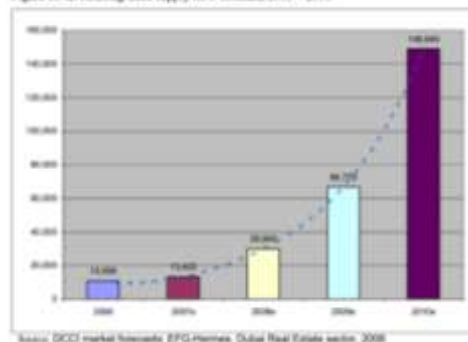
The levels of inputs and technical know-how changes the cost of production, i.e. advance technology reduces the cost of production (construction) and increases the output (number of units produced). Production (construction) efficiency and quality also receives a boost in terms of rate of completion and quality of the products. In these regards, Dubai has witnessed fast growth



Expectations of Developers

This is a very important factor in that, If developers demand expectations about national, regional, and local economic activity are positive, number of units to be produced will increase. If on the other hands the expectations of developers on the performance of the Economy are low or unfavorable, then, expected unit output will also decrease. The graph below illustrates housing units supply flow forecast from 2006 until 2010 which forecasted

Figure 1.9.2: Housing units supply flow forecast, 2006 - 2010



270,000.00

Market trends in Dubai Real Estate

Dubai experienced a slight growth in 2013 in the real estate sector. There have been increases in rents rates and sales prices have also increased. While the study of investment advisors shows that Dubai market is at recovery stage. Reports also show that property rentals are also growing in 2013. A major reason for this is the increase in Dubai’s population. As the price and rental performance improved, it has increased the interest and demand by people (investors) in the sector; this has played a big role in decreasing the hitherto existing surplus in the market. Reports show that recently, there are many projects that are being launched in Dubai, and at the moment, the UAE is at the peak of the construction cycle. However, we should know that not all the projects are going to benefit from this recovery stage. Successful projects will be ones with good financial backing and quick equity potentials. However, as we experienced in the last global financial crises, over supply of construction projects could also occur. It is expected that sales and rental rates of real estate will shift upward but not as fast as comparing to last years. According to multiples reports, the real estate protection law is also going to be released soon. Also, the UAE Central Bank has restricted property loans – to

– value ratio; so that, other local banks cannot be too exposed to property sector investment risks, so as to avoid the kinds of pitfalls witnessed in the last economic crisis.

Buyers preference, taste and Life Style

Since UAE accommodate more than 200 nationalities and various ethnic races, consumer's choice is apparent by favoring Dubai life as a place to live and have a job, besides, business, Tourism and other visiting forms. The number of People choosing to have a taste of Dubai life has increased and boosted with opportunities that Dubai offers. Some places in Dubai are actually better in quality of living. Educational institutions, day care and other community facilities and building features are extras that developers like Emaar Properties and Al Nakheel pay very much attention to, in order to ensure buyers and residents alike prefer buying and or living in their properties (buildings). Some areas are affordable and some have embraced the luxury life like Palm Jumeriah, the famous luxurious island in Dubai.

Knight Frank, a global consulting company prepared a World Development Study report (2013). The report mentioned cities such as Dubai, Miami, Nairobi and London as the places that are increasingly considered as investment destinations for the very wealthy investors. In addition, Dubai being in the midst of the Arab Nations has become a safe destination for property buyers and investors from the Middle East and beyond.

The report pointed out that the Dubai Real Estate market remained quiet between the years 2008-2010, but, with the emergence of strong indications of the beginning of a recovery in 2011, over the last year, residential real estate prices began to recover, and several new projects were launched. Now, there is a significant demand for luxury real estate assets in Dubai, while the volume of transactions increased significantly during the year 2012.

Part of the signs of appetite for luxury homes in the market emerged from the prices of villas in excellent locations, which rose nearly 20% in 2012. Apartment prices have also increased gradually last year, although to a lesser extent.

The most popular projects were sea view areas such as Dubai Marina and Palm Jumeirah, other areas such as downtown Dubai and Business bay district became more established, attracting the attention of global buyers, while villas and apartment complexes attract end users.

Conclusion:

The supply side has been steady in changing the demand side in the real estate business in Dubai. This is a shift from what obtains elsewhere around the globe especially, in other high ticket items. However; the high profit potential for Dubai Real estate properties has made it a sellers' market with ease. This trend continued until the Financial melt down which slowed down the sales of big ticket items in the UAE by shrinking the profit in terms of margin and potential. Consequently, a sharp decline in demand was prevalent until recently. The upward increase in demand had also caused a price increase which jolted the sector and now making developers and contractors more active cause of sales potentials and the inherent profit expectations. Hence, supply is increasing accordingly. The market forces of demand and supply described above have reconfirmed the importance of the third component of the package, i.e. the financial sector.

The relationship between the real estate sector and the financial sector had always been Important and had always been duly recognized in the macroeconomic literature. This explains why real estate prices are often used as real indicators of how healthy an economy is, and or how sound the financial system is. The combinations of these factors normally play

a major role in making monetary and public policy decisions. The peculiar nature of real estate market causes real estate prices to behave differently from the prices of other big ticket properties such as shares; equipment etc. all over the World and Dubai is by no means an exception. Therefore, it is Common that the short run real estate prices diverge from their long-term trends and this is evident in what obtains in the sector now as compared to what obtained few years back

Hence, it is even possible that the fluctuations in real estate prices may be experienced not only because of cyclical shifts in the economy, but also, as a result of the peculiar nature and features of the real estate market and real estate products.

At the macroeconomic level of Dubai, it has been determined that there is a major correlation Between the performance of the real estate sector and that of the financial sector in general For example, in the Dubai Financial Market, a major relationship has been confirmed between the share prices of the real estate Organizations and those of Commercials banks. This phenomenon gives a far-reaching implications of how viable the real estate sector is to the

Financial stability of the City of Dubai and perhaps, the entire UAE, the volume of the real estate prices and banks' lending for residential and commercial real estate properties is also a major factor that should be included in the list of other indicators of the financial system stability in the entire Emirate.

Be these as they are; there are a couple of major issues that should be properly investigated by other researchers in the future. (a) The separation of residential real estate ventures from the hardcore commercial real estate projects. This is necessary given the importance and the relevance of the two divisions (individually) on the Economy at large (b) Secondly, the issue of Construction and facility project implementation price factor and price indices, which are very important as consideration as to how well, healthy and stable a financial system is really is

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