COMMENT

# Don't panic

Global inflation and rising oil prices will save the UAE property sector.

words: Peter Cooper*

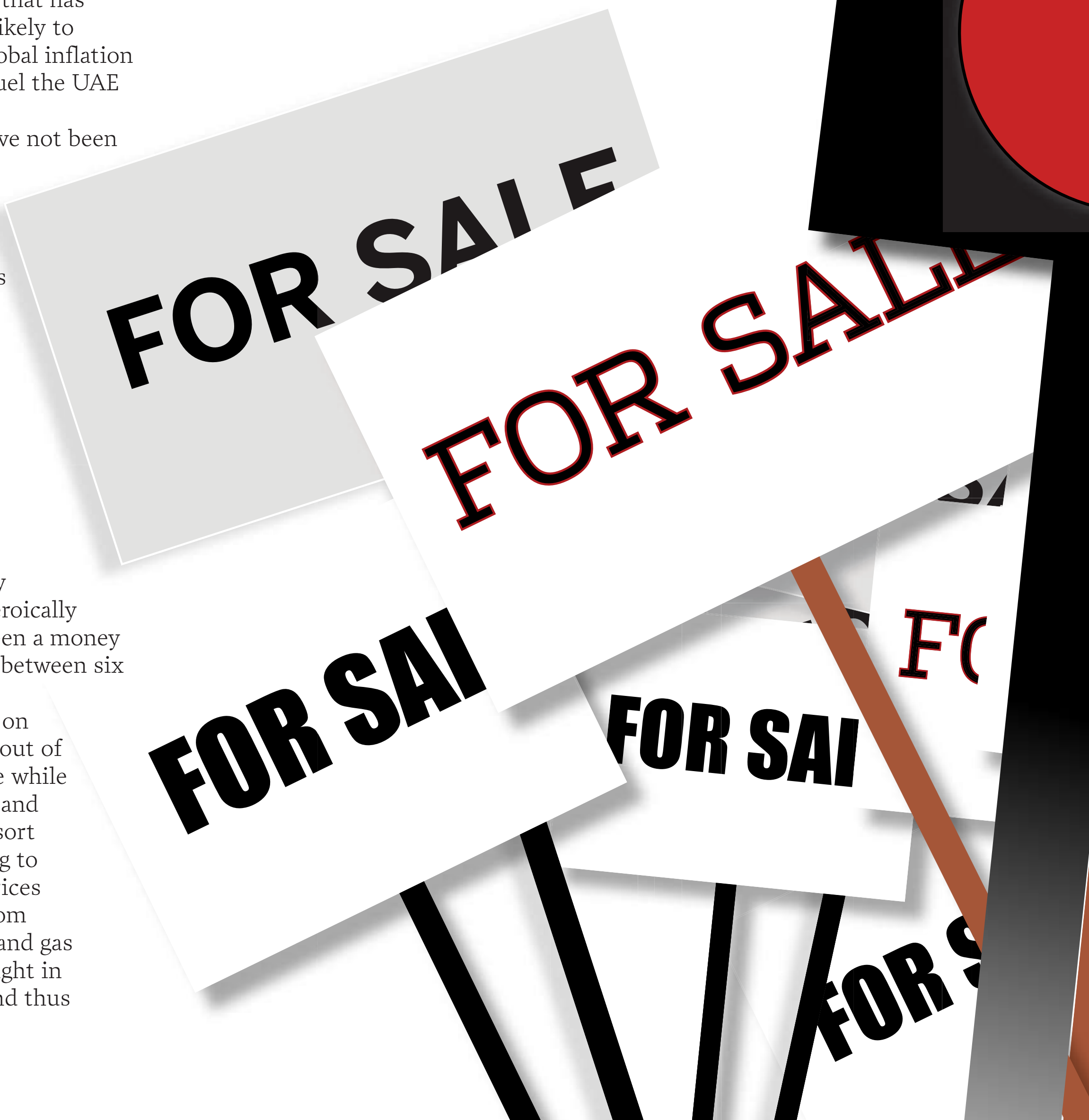
The UAE real estate market has entered a correction phase with new off-plan sales at a virtual standstill, sales in the second hand market much more difficult to achieve and prices now declining from their September all-time peak levels.

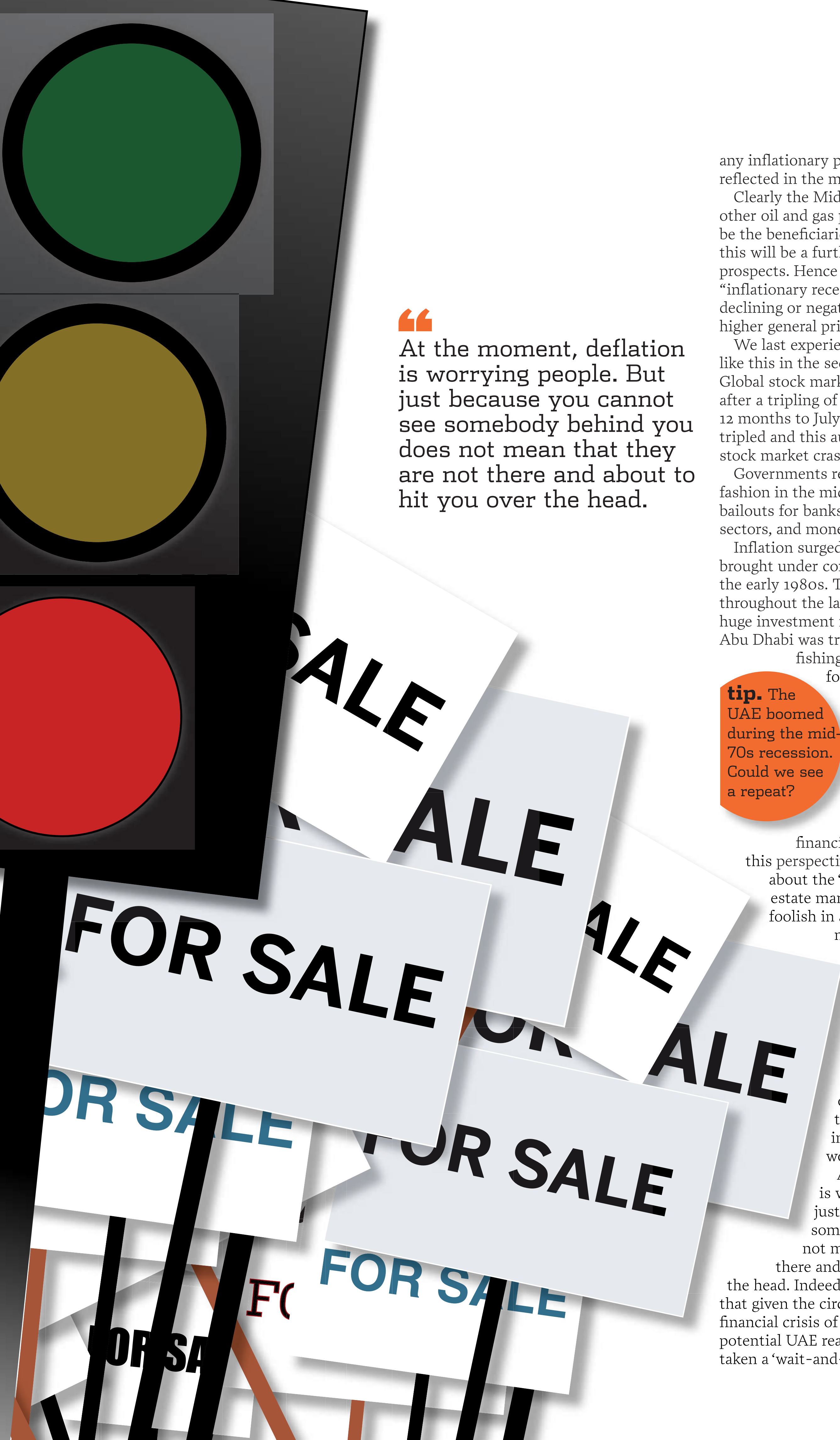
But the global financial crisis that has brought this correction is also likely to provide its salvation: surging global inflation that will raise oil prices and refuel the UAE real estate boom.

Governments of the world have not been standing idle over the past six weeks as the worst financial crisis since the 1930s Great Depression has spread around the globe. Bank bailout packages now total more than $4 trillion – about twice the annual GDP of Great Britain – and over the past six weeks US money supply has risen by 35%, a historically unprecedented increase in the money supply.

Almost all economists agree that an increase in the money supply on this epic scale and after a long period of flat money supply growth, is going to be heroically inflationary. The time lag between a money supply increase and inflation is between six months and a year.

This inflation is a kind of tax on consumption to pay for the bailout of the banks. Goods will cost more while salaries are unlikely to increase and job losses mounting. Still, this sort of inflationary recession is going to be good news for commodity prices which should recover rapidly from their current deflation. The oil and gas markets are known to be very tight in terms of supply and demand, and thus






“At the moment, deflation is worrying people. But just because you cannot see somebody behind you does not mean that they are not there and about to hit you over the head.

any inflationary pressure should be quickly reflected in the marketplace.

Clearly the Middle East, Russia, Brazil and other oil and gas producing countries will be the beneficiaries. For consumer nations, this will be a further blow to their recovery prospects. Hence the coining of the phrase “inflationary recession” — that means declining or negative growth patterns with higher general price levels.

We last experienced a “stagflation” period like this in the second half of the 1970s. Global stock markets also crashed in 1974 after a tripling of oil prices in 1973. In the 12 months to July this year oil prices had tripled and this autumn we have massive stock market crashes all over the world.

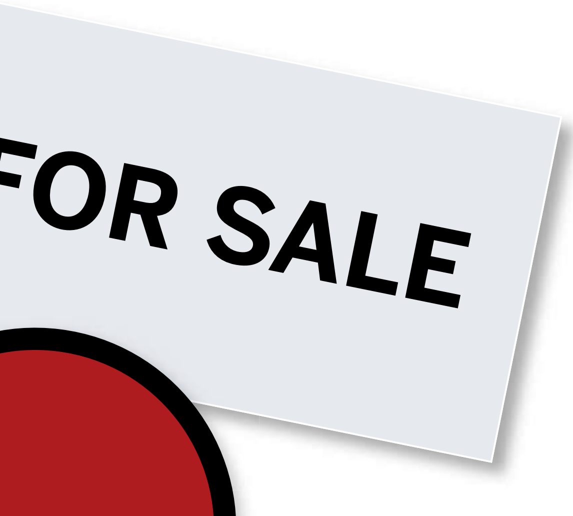
Governments responded in a similar fashion in the mid-70s, with big state bailouts for banks and key industrial sectors, and money supply went haywire.

Inflation surged and was not really brought under control until the recession of the early 1980s. The Middle East boomed throughout the late 1970s and there was huge investment in domestic infrastructure. Abu Dhabi was transformed from a small fishing village into a modern city for 500,000 people. Dubai made key investments like the Jebel Ali Port, Trade Center Tower and its famous dry docks, able to handle ships of one million tons that have never actually been built.

**tip.** The UAE boomed during the mid-70s recession. Could we see a repeat?

If you look at the global financial crisis of 2008 from this perspective, then those panicking about the “standstill” in the UAE real estate market might well look very foolish in a year’s time. Far from marking the end of the local real estate boom, this could well speed up the process — albeit a painful shakeout for speculative buyers and under-financed property companies in the short term. It really all depends on how long it takes for the anticipated wave of inflation to arrive in the world economy.

At the moment, deflation is worrying people. But just because you cannot see somebody behind you does not mean that they are not there and about to hit you over the head. Indeed, it is hardly surprising that given the circumstances of the global financial crisis of the past few weeks, potential UAE real estate buyers have taken a ‘wait-and-see’ approach rather




than rushing into long-term financial commitments during a period of considerable uncertainty in the market.

Meanwhile, secondary property sales are dogged by several factors: prices inflated over the summer months to perhaps over-optimistic levels; the difficulty in obtaining anything more than 65% mortgages; as well as the obvious concerns about the outlook for the global and local economy with oil prices sliding.

Agents say the shortage of property in favourite locations should limit the downsize in prices for completed property. They say the market has frozen rather than entered a panic mode, as the maintenance of price levels by sellers still indicates confidence in the future.

Factors that could stabilise the market in advance of a worldwide inflationary surge include: government action to provide low-cost mortgage finance; incoming funds from overseas markets in a repeat of the flow after 9/11 which financed the first Dubai real estate boom; former local stock market investors turning to property for high yields; and the lack of alternative investment opportunities overseas during a turbulent financial period.

It's hard to see foreign money flowing back quickly into UAE real estate as the revaluation of the US dollar is making property here much more expensive for buyers from the UK, Europe and Russia. However, foreign money flows should resume as global capital markets unfreeze and money is attracted by the prospect of higher returns.

Real estate is also a traditional hedge against inflation, and that will become a force in the UAE market as GCC rents head upwards again making real estate ownership the only way to beat surging rents. It is a resumption of the investment circle favouring property investment, and will be compounded by lower global interest rates to counter the recession (which are again inflationary). This will make it cheaper to buy property in the UAE.

**9/11**
**was followed by a flow of international capital into the UAE.**

That's why taking advantage of the depressed UAE property markets at this time might prove a good idea. Completed property, particularly villas which are in short supply, look by far the best option. The off-plan market is going to be the focus for any market shake out as speculators try to pull out and developers are forced to reconsider projects.

All the same, this could prove to be no more than a short bull market correction for UAE property. But that's not going to prevent it from being painful and terminal for some off-plan investors and weaker property developers. fw

## Mortgage vs mortgage

Provided by Independent Finance (04 398 1886)

| Bank | LTV (loan-to-value) | DBR (debt burden ratio) | Interest rate | Loan term | Min salary | Processing fees (% of loan amount) | Early repayment fee |
|---|---|---|---|---|---|---|---|
| ADCB | 85% with ST*<br>80% no ST* | 60% salary <25k<br>65% salary >25k | 7.25% (LTV <49.99%)<br>8.5% (LTV 85%) | 25yrs | Dh8,000/m | 1% | 2% after 6 months<br>1% after 3-5 yrs |
| HSBC | 70% | 60%<br>(less 0.15% with ST*) | 8.25% | 25yrs | Dh10,000/m | 1% min Dh5,000 | 2% for life of loan |
| LLOYDS | 70% owner<br>65% investor | 40% | 8.5% variable | None | Dh2,000m | 1% | None |
| BARCLAYS | 80% | 55% salary >25k<br>50% salary <25k | 8.55% max | 25yrs | Dh10,000/m | 1% max Dh30,000 | 3% up to 2yrs<br>2% after 2-3yrs<br>1% for life of loan |
| CBD | 85% | up to 55%<br>5% more with ST* | min 6.5% | 2-25 yrs<br>2-25yrs | Dh20,000/m | 1% max Dh30,000 | 3% after <1yrs<br>2% after 1-2yrs<br>1% after 2-5yrs<br>Free after >5yrs |
| AMLAK | 90% | 60% | 8% case by case | 25yrs expat<br>30yrs uae nat | Dh7,500/m | pre-approval Dh6,000<br>0.75% | 2% for life of loan |
| MASHREQ | 80% | 55% | Eibor + 4% | 25yrs | Dh9,000/m | 1% max Dh25,000 | 1% after >2yrs<br>Free after 2yrs |

* With salary transfer

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