

The Real Estate Sector in Saudi Arabia

Summary

Real estate plays an important role in the Kingdom's non-oil economy. In 2004, the value of real estate transactions including sales of existing units amounted to SR 900 billion. The real estate sector is driven recently by domestic demand fundamentals and not by speculation. A strong economy and demographic fundamentals are the core push factors behind the growth in real estate.

- ◆ Through 2010 we forecast that total new real estate construction in the Kingdom will reach SR 484 billion.
- ◆ In order to meet demand, through 2020 a total of 2.62 million housing units will be built, at an average rate of 163,750 units per annum. Through 2020, total new investment in housing will amount to SR 1.20 trillion.

Real estate demand is sustainable and we expect a strengthening of the current set of favorable circumstances with the likely introduction of mortgage products in the next few years. The housing sector is at the center of the Kingdom's growth in real estate activity.

- ◆ In value terms the housing sector comprises 75 percent of all real estate activity in the Kingdom.
- ◆ SR 75 billion per annum will be required to meet annual housing demand in the Kingdom through 2020.

Real estate growth might be challenged if domestic supply exceeds demand. At the moment there are few indications that this will occur.

- ◆ The real estate market is undersupplied in affordable low-income housing.
- ◆ We believe that the Kingdom's real estate market is at a phase where price appreciation will grow but not exponentially.
- ◆ On average housing prices between 2002-2005 in the Kingdom grew by 13.7 percent per year, land by 16.5 percent and commercial (office) space by 15.2 percent.
- ◆ We believe that large real estate developers will enjoy a stable revenue stream and will grow as real estate in the Kingdom shifts toward large projects.

The Real Estate Sector in Saudi Arabia

The Structure of the Real Estate Market

Since the late 1970s real estate -- raw land, or land developed with commercial or residential buildings -- has widely been perceived as an investment safe-haven in Saudi Arabia. The establishment of the local stock market in 1985 did not dissipate interest in real estate investment throughout the 1980s and 1990s. Since around 2002, real estate investment has been rising as have land prices and rents, predominantly in urban areas.

Land acquisition in Saudi Arabia is a top-to-down process. The government releases large plots of land to a limited pool of investors who either develop the land on their own or sell it to other developers or wholesalers. In turn, wholesalers determine, according to demand and supply conditions, whether to hold on until land prices appreciate or to begin immediately to sell it to consumers. Some opt to develop their own real estate plots into smaller, mainly, residential, projects. We estimate that large developers hold on to land for an average period of 3-4 years.

The government is the distributor of raw land and the private sector is the dominant real estate developer. Individuals and private businesses own most housing and commercial units respectively. Most real estate transactions are conducted through real estate agents, who charge buyers a flat 2.5 percent commission. There are limited direct sales or leasing activities between landlords and tenants and neither is the printed press a popular medium for real estate transactions. Geographically the urban real estate market is divided into three regional centers: Central Region (Riyadh), Eastern Province (Al Khobar and Dammam), and the Western Province (Jeddah, Mecca and Medinah).

By type the real estate market is divided into three groups:

- ◆ Raw land
- ◆ The housing market comprised of apartments, villas, floor in villas (duplex), traditional homes and housing compounds
- ◆ Commercial units, which consists of office buildings, shopping malls, hotels, and industrial facilities including warehouses.

In terms of volume (building permits), the housing market represents over 91 percent of the real estate industry, while our value estimations suggest that this sector comprises 75 percent of all real estate activity.

Recent Developments

Over the past several years, the real estate sector has received much investment attention. After a decade of sluggish growth in the 1990s, a combination of factors have led to the rejuvenation of real estate in the Kingdom, which include:

- ◆ High liquidity
- ◆ Preference to maintain capital within the country and region

- ◆ Low interest rates
- ◆ Expected high return from real estate
- ◆ Increase in bank lending

In the past land was acquired often for a relatively low price by developers and wholesalers as demand and real estate prices rose so did prices of land purchased by the wholesalers. We estimate that over the past three years, wholesalers are paying 175 percent more for raw land than prior to 2002.

Another recent trend in the real estate market has been the development of large-scale housing projects in which middle-income groups have been given investment opportunities. The government, along with large developers, has supported this idea through a vehicle in which developers float affordable shares, based on the estimated total project costs, to small investors. This has been especially popular with residential projects in which small investors may take up a house within the project. Following irregularities with some such projects, the government temporarily halted all such activities for a three-month period in mid-2005. Meanwhile, many investors have also opted to invest their money in the booming local equities market. We anticipate that in the near future investors will regain confidence in these real estate investment partnerships.

Real Estate and the Economy

The real estate and associated sectors, such as construction, have historically been important contributors to the Kingdom's growth. According to government data, service activities related to real estate as well as construction have contributed more than 13 percent toward the country's real GDP over the past few years (see chart). Since 2002, real estate and the stock market have attracted high interest from investors who move back and forth between the two asset classes. In early 2005, as the local equities market rose sharply investors reduced their exposure in real estate. This in part has helped stabilize real estate prices. We anticipate real estate to receive investment reinvigoration in 2006, sustainable for many years to come.

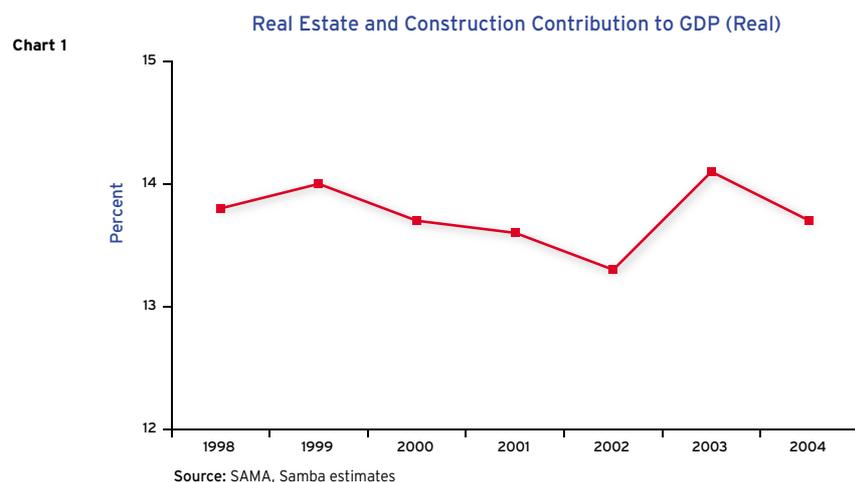
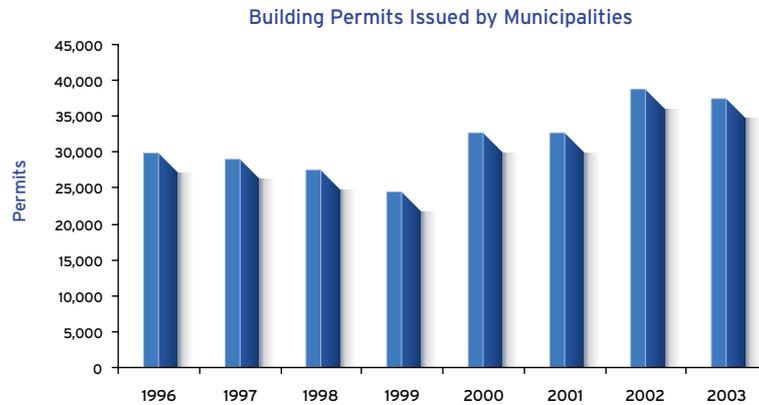


Chart 2



Source: Ministry of Municipality and Rural Affairs

Real estate is an important sector in the economy. We believe that building permits (a measure of real estate activity) will continue to exceed 37,000 per annum through 2010. We estimate that real estate, predominantly a private sector activity, employed more than 50,000 people in 2004 compared to nearly 23,000 thousand in 1995. Construction, an associated sector, employed some 550,000 people in 2004 compared to nearly 392,000 people in 1995. There is very little employment effect on the labor market for Saudi workers as construction predominately hires expatriates. We expect that as real estate grows in the coming years, construction activity will enjoy a sustained boom in the Kingdom. We estimate that there are more than 15,000 licensed and unlicensed real estate offices in Saudi Arabia.

Real estate and construction are more cyclical in Saudi Arabia than in many other countries because of the economy's overall connection to oil prices. When the economy accelerates so does real estate and construction and when it decelerates, both sectors slow in parallel, albeit at a slower rate than the rest of the economy. Over the past several years, construction and real estate combined have tended to grow faster than overall real GDP. In 2004, real estate and construction combined grew by 7.5 percent, while the economy grew at rate of 5.2 percent. In 2002, real GDP grew by 0.74 percent, while construction and real estate grew by 3.1 percent. We explain this resilience in growth due to the demand driven nature of real estate activities and construction.

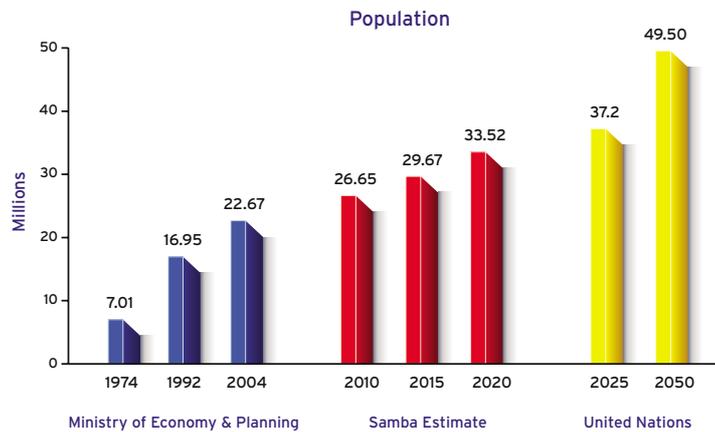
Demand Factors of Real Estate

Demographic Dynamics

According to census figures in the past 30 years, the total population in the Kingdom rose from 7.01 million in 1974, to 16.95 million in 1992, and 22.674 million by the third quarter of 2004. Saudi Arabia's population increased in absolute terms by 5.7 million between 1992 and 2004. The total population growth averaged 2.45 percent from 1992 to 2004, including foreigners, and 2.49 percent for Saudis only. While this is lower than the widely perceived growth rate of above 3 percent, it remains above the global average growth rate of 1.5 percent during the same period. The proportion of Saudis in the total population slightly rose from 72.63 percent in 1992 to 72.90 percent in 2004 (see chart).

The Kingdom’s fertility rate is high at 4.3 births per woman, while the replacement fertility rate (number of births per woman required to maintain the population with no growth) is around 2.1 births per woman. According to the Ministry of Health, life expectancy at birth has improved substantially from 61 years in 1980 to 72.1 years in 2004. Increased family planning and an increase in women’s participation in the workforce is likely to lower population growth over time. We estimate that the Kingdom’s population will reach 25.77 million in 2010, 28.95 million in 2015 and 32.52 million in 2020. Due to socio-economic trends in the Kingdom, such as urbanization, we believe that population growth through 2020 will continue its decline below the 2.45 percent mark witnessed between 1992 and 2004. According to the 2004 United Nations report on World Population Prospects, Saudi Arabia’s population will grow to 37.2 million in 2025 and 49.5 million in 2050.

Chart 3



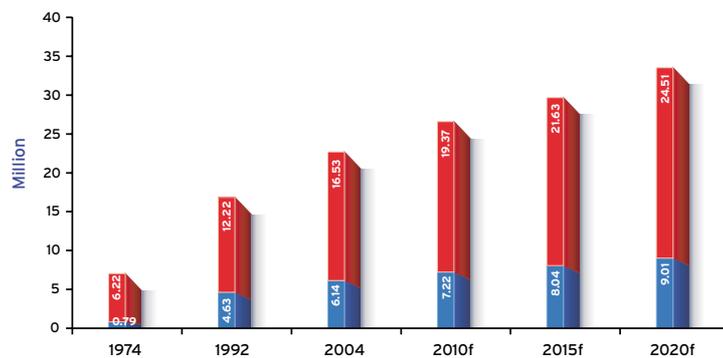
Saudi Arabia is a country of the young, the natural outcome of relatively high birth rates over the last 30 years. Around 70 percent of the population is made up of people under 30 years of age. Around 45 percent of the population is under 15 years old.

These demographic forces lay the groundwork for sustainable real estate demand, especially residential demand, for many years to come. The demand for housing will grow in the coming decade and a half, as many reach marriageable age.

Disposable income is the single most important factor determining housing demand and size. Higher income leads to additional demand and greater preference for larger housing units. According to the Ministry of Economy and Planning, the average monthly income for nationals was SR 7,043 in 2000 (most recent official data). Monthly incomes are often supplemented by additional income from secondary employment or private business. We estimate that average monthly incomes may be about SR 10,360 in 2006. Thus we foresee that the largest demand for permanent accommodation will be for affordable middle-income housing. Certainly, not all of that income will be directed toward purchasing/renting a house. We estimate that around 40-45 percent of a person’s monthly salary in Saudi Arabia is apportioned toward housing needs. In addition, the absence of widespread mortgage availability, discussed below, also limits Saudis’ ability to purchase housing. We estimate that 65 percent of Saudi households currently own their primary residence.

Shifts in the non-Saudi population can also affect demand in the real estate market. In absolute terms, the total expatriate population rose from 4.63 million in 1992 to 6.14 million in 2004. Males comprised 69.5 percent of the total expatriate population. We estimate that the share of expatriates of the total population will remain stable for the next fifteen years. The push toward Saudization will keep the expatriate population from rising while at the same time the expansion of the non-oil private sector will pull expatriate labor into the country (see chart). We think these two forces will roughly offset each other.

Chart 4 Total Saudi & Expatriate Population (1974-2020f)



Source: Central Department of Statistics (CDS), Samba Estimates

According to the Ministry of Economy and Planning, the average monthly salary for expatriates stood at SR 2,354 in 2000. The majority of the expatriate labor force falls into the low-income category. Most of these laborers are male and share low-income accommodation with other male workers. Only a minority of the expatriate labor force falls into the high-income salary bracket and opt for high-end compound accommodations. We estimate that around 90 percent of expatriates find accommodation outside compounds and most opt for renting apartments. We do not foresee significant demand growth for additional high-end compounds in the Kingdom. We foresee a continuation in the current demand for smaller housing units for expatriate singles.

High liquidity, per capita income, low cost borrowing and financing

The availability of financing is a bottleneck to real estate growth in Saudi Arabia, but not as severe as in other developing countries, as there is certain level of government lending for housing and relatively high wealth and income levels.

Availability of low cost financing has been another factor aiding real estate demand. From its founding in 1974 through 2003, the government's Real Estate Development Fund (REDF) provided some SR 123.2 billion worth of interest-free credit to build more than 560,000 housing units. However, demand for REDF loans far surpasses availability. Based on REDF data in 2002, only one out of every 4.7 applications was approved. Anecdotal evidence suggests that the credit applications backlog could extend for more than a decade. Around 8 percent of all housing units built in a year are REDF funded. We estimate that around 86 percent of all purchased homes are paid for in cash and the remaining 6 percent funded from

banks and financial companies. In August 2005, the REDF received an additional SR 9 billion in capital to grow its lending activities, but the fund's financial means to meeting the growing housing demand in the country will remain limited. Riyadh tends to receive around 30 percent of all REDF loans, followed by the Eastern Province and the Mecca region at 25 percent and 22 percent, respectively.

The majority of housing units are mainly funded by private savings in the Kingdom, as the legal infrastructure does not yet support commercial bank mortgage lending. A commercial mortgage law to rectify this shortcoming is in draft. We are beginning to observe the emergence of private sector financing companies, which give loans to those wishing to own plots of land and housing units. Some of these finance companies are autonomous but the rising trend will consist of real estate developers, who will establish parallel financing institutions, similar to automobile agents who established car financing operations along with their car dealerships.

Incomes could support mortgage lending. Strong GDP growth as well as further decline in population growth will most likely help per capita income increase to over \$15,000 by 2010.

Within the next few years, we expect the approval of the commercial mortgage law, which will add impetus to real estate growth. The availability of debt financing will unleash significant pent up demand for residential real estate. Over the past several years, interest rates have remained low in Saudi Arabia. Due to the currency peg, interest rates in the Kingdom follow US interest rates. In due course, higher dependence on mortgages will link real estate prices and activity to interest rate movements, which is currently not the case. The types of mortgage products will affect the housing market and the economy as a whole. Research shows that countries with mortgage loans have better-behaved housing prices and fewer negative effects on their economies from house price changes than economies where no mortgage is available.

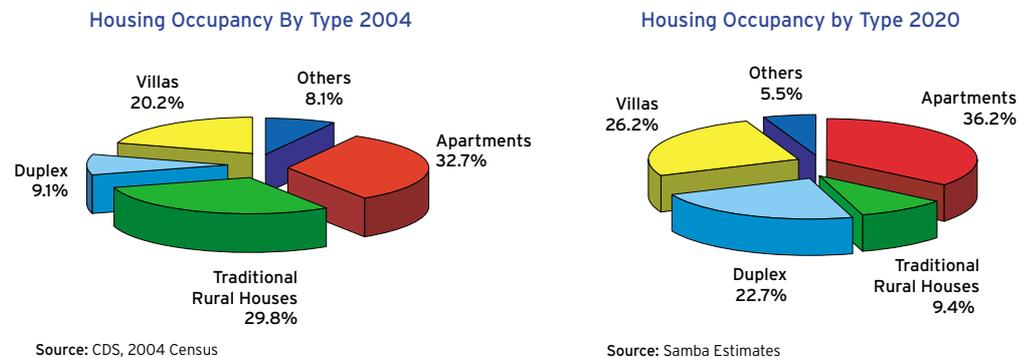
The Housing Market

Most Saudis, in both urban and rural areas, have a preference for villas. Nearly 45 percent of all housing units are villas and duplexes (see chart below). This is due to a large family size (an average of around six in the Kingdom), availability of land, access to capital and affordable labor. Another widespread tendency in the Kingdom is prospective house owners getting involved in the entire construction process of their houses. This starts with choosing the land, goes on to designing and hiring the contractors, often negotiating the building materials prices and finally finishing and decorating most of the interiors. In many ways, this changes the dynamics of the house-building sector, as there are many intermediaries involved in every building process and this limits the advent of large overall building contractors. Medium-sized contractors construct most housing units, especially luxury housing units.

As the housing market matures further, we expect housing quality will also improve. The average lifespan of a housing unit in the Kingdom is around 30 years compared to an average of 90 years in Germany.

Gradually, apartments are gaining popularity in the Kingdom. According to the most recent data, apartments form 32 percent of all housing in the Kingdom. Small families, expatriates, and newly-married Saudis (without children) usually choose this housing type. Both Saudis and expatriates rent most apartments, as owning condominiums are not common in Saudi Arabia. In the next two decades, preference for apartments will rise throughout the Kingdom as younger Saudis enter the job market and income sensitivity will lead this segment of the population to opt for more affordable housing. A change in the height of buildings will provide incentives to raise multi-storied apartment buildings in Riyadh as well as the Eastern Province. Jeddah is currently seeing strong growth in apartment buildings.

Chart 6

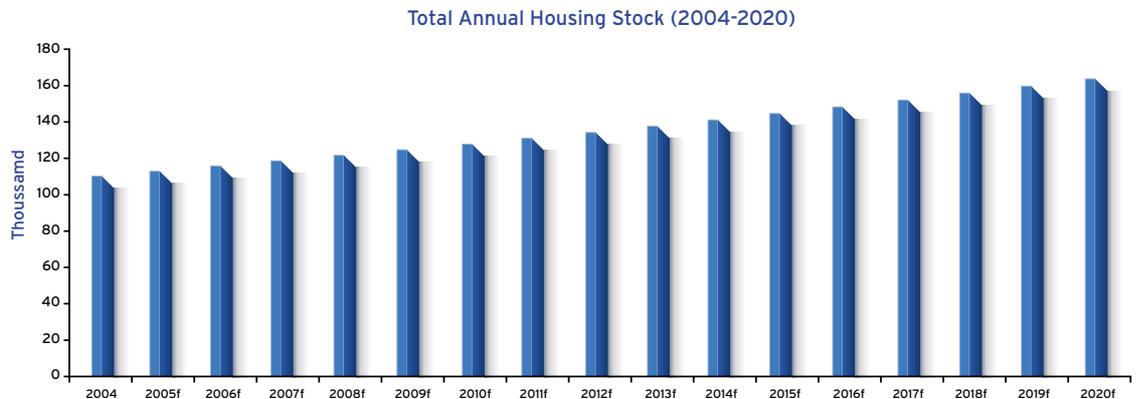


Housing Demand

According to the 2004 census, the housing occupancy rate (the proportion of total housing units that are occupied) between 1992 and 2004 grew annually by 3 percent while population grew at an annual rate of 2.45 percent. In 1992, the total number of occupied houses amounted to 2.89 million units, whereas by 2004, it reached 3.99 million units. Over this 12-year period, some 100,000 units were occupied every year. Average household size in the Kingdom fell to 5.6 persons in 2004, from 6 persons in 1992. This could be mainly attributed to the trend away from the extended family concept (parents, children and grandchildren living together). As society evolves, we expect that this trend will continue. We estimate that the average household size will shrink to 5.1 persons per household by 2020.

Several factors affect the housing market. Population growth, cost of capital, per capita income, cost of living, rental prices, availability of house financing instruments such as mortgages, occupancy rates, and supply of housing units all affect this sector. We estimate that the total housing stock in the Kingdom was 4.39 million units in 2004. Around 10 percent of the total housing stock in Saudi Arabia remains unoccupied. This percentage includes units that remain uninhabited for various reasons including due to people moving from one place to another. We estimate that the total housing stock will reach 7.01 million units through 2020. During the same period, a total of 2.62 million housing units will be built, at an average rate of 163,750 units per annum (see chart).

Chart 5



We estimate that 2.62 million housing units will require a SR 1.20 trillion of total investment in order to meet demand, not adjusted for inflation, through 2020. The cost and types of building materials, as well as the construction methods will affect the final price of housing units, which we have not included in our model. On a total housing stock basis, we estimate that SR 75 billion per annum will be required to construct an average of 163,750 housing units per annum.

Mortgage products will give Saudis the ability to purchase villas and duplexes and gradually shift away from their current propensity for renting apartments (among younger people) and traditional houses (mostly in rural areas - see tables). Also, mortgage products will alter the rental market, as the majority of newly married couples, who opt for rental units due to their affordability, will find it easier to purchase an apartment or house. The introduction of mortgage products will allow the Kingdom's real estate market to develop characteristics of other mortgage-driven markets in terms of rising real estate prices.

Demand-Driven Growth or Speculation?

We believe that the real estate market is mostly demand-driven, rather than speculative. This is not to say that speculative spurts have not been visible over the past few years, especially on plots of raw land. The rise in housing prices is still mainly driven by demand factors and as a result are not generally volatile. An important indicator of real estate speculation is the ratio of prices to rents, otherwise known as rental yield rates. The price of a house as an investment should reflect the financial benefits of ownership from rental income and compare favorably with other asset classes with similar risks. The lower the rental yield the greater the likelihood of speculative overvaluation in a given market. Yields in Riyadh for housing units range between 6.5 percent and for commercial space 8.3 percent (see table). These yields are at the mid to high point of the range for rental yields in several markets, suggesting the market is not in general, overpriced by international standards. Rental contracts favor the landlord, with a minimum duration of one year and rent paid in advance.

For many years, raw land speculation in the secondary high-end raw land market areas has been prominent in the Kingdom. This type of speculation is less prevalent in the housing and commercial space market.

Rental Yield Rates (2005)

City	Housing	Commercial
Beijing	8.30%	9.60%
Delhi	5.50%	8.50%
Dublin	2.95%	3.60%
Hong Kong	3.75%	3.95%
London	5.30%	6.45%
Madrid	4.10%	5.20%
Riyadh	6.50%	8.30%

Source: Property Investing, Colliers, Economist, Financial Times, Samba Estimates

The single most important factor that makes the Saudi real estate market differ, for example, from Dubai is the lack of expatriate ownership. Since 2000, non-Saudi residents have been entitled to own real estate for their private residence with the permission of the Ministry of Interior. Ownership of real estate by foreign investors to conduct their business activities and house their employees is also permitted. Non-Saudis may not own real estate in Mecca or Madinah. We do not, however, anticipate non-Saudis to invest heavily in real estate.

The Players

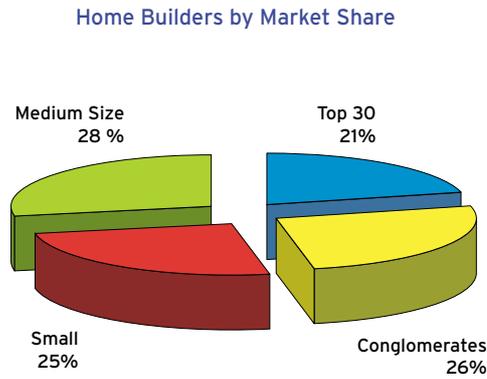
The real estate market's growth over the years has attracted a multitude of new entrants. There are approximately 3,500 companies involved in real estate development in the Kingdom. We estimate that around 37 percent are located in the Central region, 34 percent in the Western region and 29 percent in the Eastern region. In terms of market players, there is fragmentation due to the presence of many small real estate developers. We estimate that more than 80 percent of the real estate companies in the Kingdom are small, and often unregistered, entities. The rest of the market is divided into 30 big players, who specialize in real estate development, diversified conglomerates with interests in real estate, and medium-size private companies, who also have interests in real estate development. In the housing market, the very small firms possess around a 25 percent market share. The top 30 housing construction companies have a 20 percent market share, followed by the diversified conglomerates at around 30 percent and medium-sized companies at 25 percent (see chart).

In the commercial real estate sector the top construction companies along with the diversified conglomerates dominate the market. Due to the capital intensity, small players have little presence in the commercial real estate construction sector.

Unlike government-backed developers, such as Emar and Nakheel in Dubai, the state does not play an important role as a real estate developer in the Kingdom. Compared to the private real estate entities, there is little involvement from the Ministry of Public Works and Housing and various other government departments and municipalities in real estate. Small developers dominate the housing market, mainly due to low entry barriers. This is set to change in the coming years, as large developers increasingly build large housing complexes.

Supply

Chart 7



Source: Samba Estimates

We believe that the real estate market is undersupplied in affordable low and middle-income housing. Low-income housing units tend to have less than 150 square meters of floor space, which is less than half the average size of a housing unit in the Kingdom. Still spacious by international standards, these low-income units house large families. There is also a need for middle-income housing at a cost per unit of around SR 400,000. Middle-income apartment units, which vary between 180 square meters and 250 square meters, are in short supply. The Kingdom has a good supply of upper-middle income and high-income housing units, which are larger than 250 square meters, due to most of them being custom built. These upmarket units are mostly custom-built.

The Kingdom-wide Real Estate Market

We estimate that through 2010, total new real estate construction activity will reach SR 484 billion in value (see table). The majority of the activity will arise out of the housing segment, followed by commercial office space units and retail shopping centers. Real estate prices have increased over the last four years, but not at a level that dissuades both developers and consumers. Real estate prices in the Kingdom are very difficult to track since there is no price registry. Certain areas, for example Riyadh and Mecca, have witnessed higher prices. However, prices vary tremendously within a city. Between 2002-2005, average housing prices in the Kingdom have increased by 13.7 percent per year, while average land and commercial (office) space prices have increased by 16.5 and 15.2 percent respectively (see price table), according to our estimates.

Following we examine developments in the three major metropolitan areas. However, there are strong real estate developments elsewhere, especially the industrial areas of Jubail, Jubail II and Yanbu. In addition the recently announced planned development of the King Abdullah Economic City at Rabigh, north of Jeddah, at a planned cost of nearly SR 100 billion will add more impetus.

Riyadh

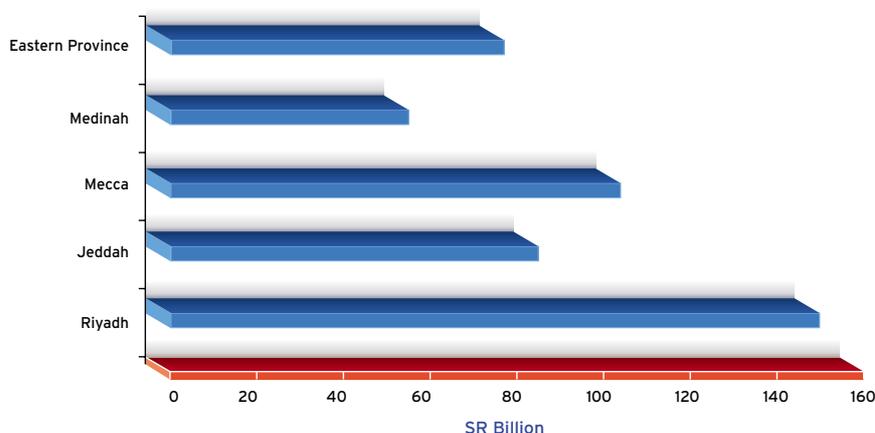
Riyadh is a growing city, both in terms of size and population. We estimate that through 2010 SR 150 billion will be invested in new construction. According to a study conducted by the Riyadh Development Authority (RDA), the city's population reached 4.2 million in 2004. Riyadh is growing, but not at an exponential rate. Its population growth has declined to 4.2 percent between 1996-2004 from 8.1 percent between 1990-1996. Due to a slowdown of internal migration and a slowdown in the city's growth, we estimate that Riyadh will be an 8-million strong city by 2023. At current growth levels, we see no compelling evidence of a huge

Average Real Estate Annual Price Increase By Region (2002 - 2005)

	Housing	Land	Commercial
Riyadh	9.1%	14.7%	11.8%
Jeddah	7.7%	7.1%	10.5%
Mecca	11.8%	13.9%	11.8%
Medinah	9.1%	11.8%	10.5%
Eastern Province	9.1%	10.5%	9.1%

Source: Samba Estimates

Chart 8 Real Estate Activity by Select Regions (2005-2010)



Source: Samba Estimates

rise in demand leading to a supply shortage. Families in Riyadh grew by 50 percent between 1987 and 1991 and 41 percent between 1991-1997, while the supply of new housing units grew by 14 percent and 29 percent respectively during the same periods. However, housing supply rose by 55 percent between 1997 and 2004, outstripping population growth and bringing the housing market into balance. We estimate that the housing occupancy rate in Riyadh is at 92 percent and for commercial (office) space at 94 percent.

We believe the following dynamics are part of the Riyadh market:

- ◆ Riyadh is facing a shortage in affordable middle and low-income housing.
- ◆ There is a shortage in rental apartment in various areas of Riyadh.
- ◆ There is a shortage in affordable office space units in the town's central area.

Currently, various areas of northern Riyadh (toward King Khaled International Airport) and northwest (in close proximity to the diplomatic quarter) are witnessing a housing boom. Most of these areas cater to a high-income clientele, who opt for customized housing units. The west and southern parts of Riyadh are not experiencing a housing boom. New office space is being created in the central part of the town, next to the traditional commercial/office centers near Olaya Street and King Fahad Road. Our estimates foresee private sector GDP growing by more than 5 percent per year in the next five years. This growth will fuel demand for high quality office space that is currently available in limited supply. However, the city's commercial center will grow as

the city spreads, particularly in the north. We expect that these areas will see strong growth in office buildings, as prices and space in the traditional central area crowds out prospective developers. Overall, we expect that Riyadh's attraction to business and capital will increase in the next few years, boosting demand for housing and commercial space in and around the city.

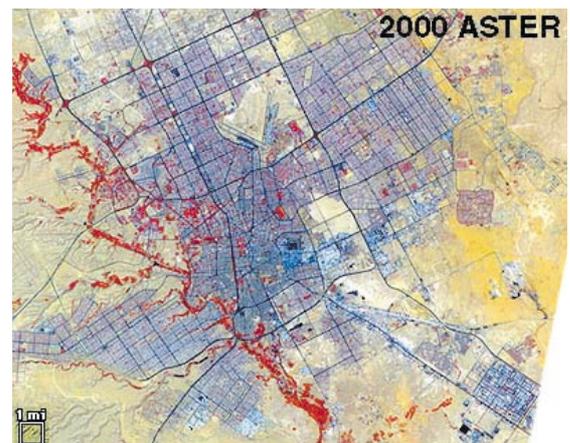
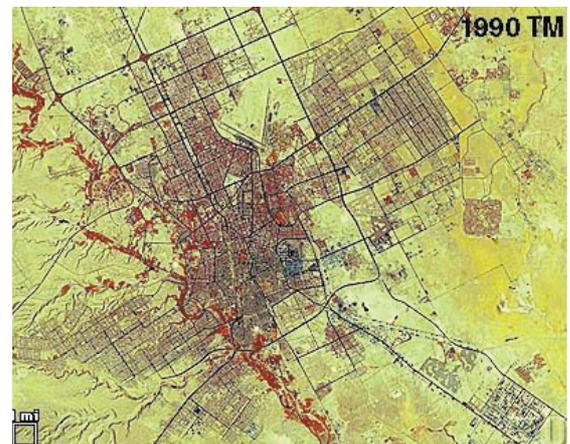
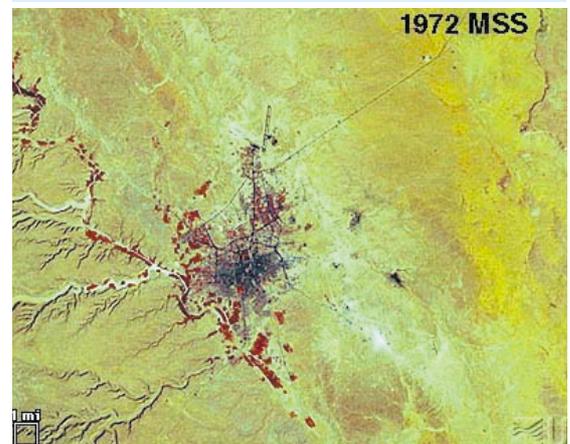
Jeddah

The city of Jeddah is going through its own high growth. Some SR 85 billion will be invested in new real estate construction through 2010. Census data does not provide a gauge of the city's demand potential since it lumps together Mecca and Jeddah. According to the 2004 census, the Mecca/Jeddah region has 5.8 million people, the largest regional population in the Kingdom.

Housing units, mainly high-end residences, are being developed in the northern parts of the city. Larger housing projects are spreading in the southern limits of the city and beyond. The Corniche is witnessing a combination of developments, which include a small trend in high-rise apartments and commercial space growth closer to the city's traditional commercial center. Overall, a change in building codes has led to the phenomenon of high-rise development in this area.

The municipality's decision to permit construction of three-story buildings in the eastern parts of Jeddah has renewed appetite for new low-to-medium income housing units in the area. An example is the state's project in Abraa, which involves the government spending SR 320 million for a low-income housing development project. We expect that eastern parts of the city will become more accessible with the construction of additional roads, which in turn will create further interest in the area.

Growth of Riyadh



Source: NASA/GSFC/METI/ERSDAC/JAROS, and US/Japan ASTER Science Team

Mecca and Medinah

Mecca's real estate investment will be greater than Jeddah, amounting to SR 104 billion through 2010. In the last few years, real estate development has gotten a boost from government-initiated infrastructure projects, which have made parts of the city more accessible and, in turn, opened up land availability. Private realtors anticipate greater influx of visitors as the government increases its focus on religious tourism. Mecca's real estate development has been characterized by a surge in luxury residential units in the town center. Medinah is seeing a build-up in residential, as well as commercial, space.

The government's infrastructure projects in Mecca have boosted the private sector's desire to build within the city center. Plans are underway to construct residential towers in Jabal Omar, a mountainous area close to the Grand Mosque, at an estimated cost of SR 12 billion. Within the city's center, a five-star hotel, shopping mall and four residential towers, known as the Al Balt Towers, is moving toward completion and the project value is estimated at SR 6 billion. Another project under construction is the SR 1 billion, 22-story Meridian Towers. Soaring land prices in this area have forced small shopkeepers to operate on diminishing margins or relocate elsewhere.

Over the past few years, Medinah has been witnessing its own real estate boom, albeit smaller in size and total investment, when compared with that of Mecca. We estimate Medinah will see investment of around SR 68 billion in real estate development through 2010. Real estate development is mainly taking place in the eastern area from the Prophet's Mosque. More than 50 projects, valued at SR 25 billion, have been approved and are expected to be completed through 2015. The most promising is the Al Haram Commercial and Residential Center. The SR 2 billion project would include nine inter-connected towers, a shopping mall, and a five-story car park. Real estate development in Medinah's central area has also led many small retail outlets to leave, given rising rental prices over the past two years.

Eastern Province (Al Khobar and Dammam)

A considerable amount of real estate development is also taking place in many parts of the Eastern Province, valued at SR 77 billion through 2010. The attractiveness of the region hinges on the region's commercial/industrial importance, in addition to its coastal exposure. Aramco plays a central role as the region's industrialist. The expected capital expenditure that the region will witness in the coming years will impact the real estate market in the region. The region has aspirations to attract Gulf Cooperation Council (GCC) property owners. According to 2004 data from the Ministry of Economy and Planning, a limited number of GCC citizens are real estate owners in Saudi Arabia. Only 2,640 GCC citizens own real estate in Saudi Arabia, while 7,922 GCC citizens own property in the United Arab Emirates (UAE) and 7,346 GCC citizens own property in Bahrain (around 33 percent of all GCC owned-real estate in Bahrain is in Saudi hands). Opening the Eastern Province to foreign/GCC ownership will add modestly to what is likely to be a strong real estate market for several years.

Outlook

Real estate is in a growth phase that will continue through at least 2010. The Saudi real estate market is driven by demand fundamentals that are not set to change in the foreseeable future. The demographic fundamentals, combined with the strong performance of the economy, will sustain the growth in real estate. We do believe that a supply shortage in affordable low-income housing is a challenge. We also believe that the market will eventually become more sensitive to quality as real estate development becomes more structured and organized. The introduction of mortgage products in the next few years will add impetus to an already high growth sector.

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