

Rising inflation

The impact on Dubai's residential market

Summer 2022



Inflation levels in the UAE and Saudi for that matter, are relatively tame compared to the rest of the world. In the UAE Consumer Price Inflation stood at 2.5% at the end of last year.



There are a number of reasons why we do not expect a significant spike like we're seeing elsewhere in the world:



The UAE has a very **diversified imports strategy** for all its goods, so there is a reduced risk from imported inflation



Then there is the power of the government. **The sustained spike in oil prices** is helping to build up a cash stockpile. In past high inflation environments the government has intervened to cap price rises. And this time appears no different. In April, the UAE's Ministry of Economy introduced a new policy to regulate the price of a wide range of consumer goods. This new policy means retailers must seek prior approval before raising prices on 11,000 commodities, including milk, meat, poultry, eggs and bread, which again should help to contain inflation.



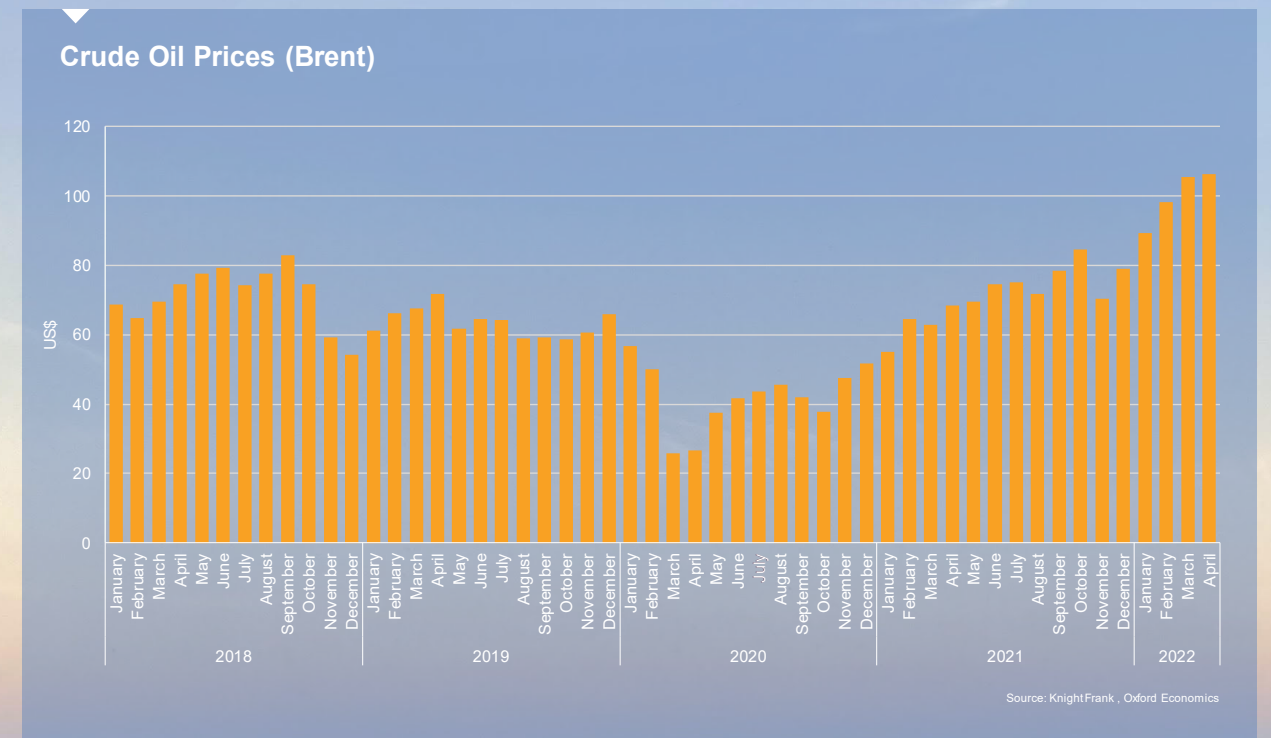
In addition, the UAE maintains a **fixed peg to the US dollar**, which has strengthened significantly in recent weeks, which will, to an extent, offset some of the imported inflation



Furthermore, **the high inflation is not yet impacting business confidence** which has remained in expansion territory and has indeed climbed to a 19-month high during May. The non-oil sector PMI reading indicates that businesses are clearly nervous about rising cost pressures.

Two immediate pressure release valves are a reduction in the pace of new hires and passing on costs to consumers. The latter is often seen as a last resort, but there are signs to suggest a slight slowdown in the pace of recruitment.

With these reasons in mind, our expectation is for inflation to remain relatively stable, at least for the next 12 months, hovering around the 2%-2.5% mark in the UAE for the remainder of 2022.



The residential real estate market

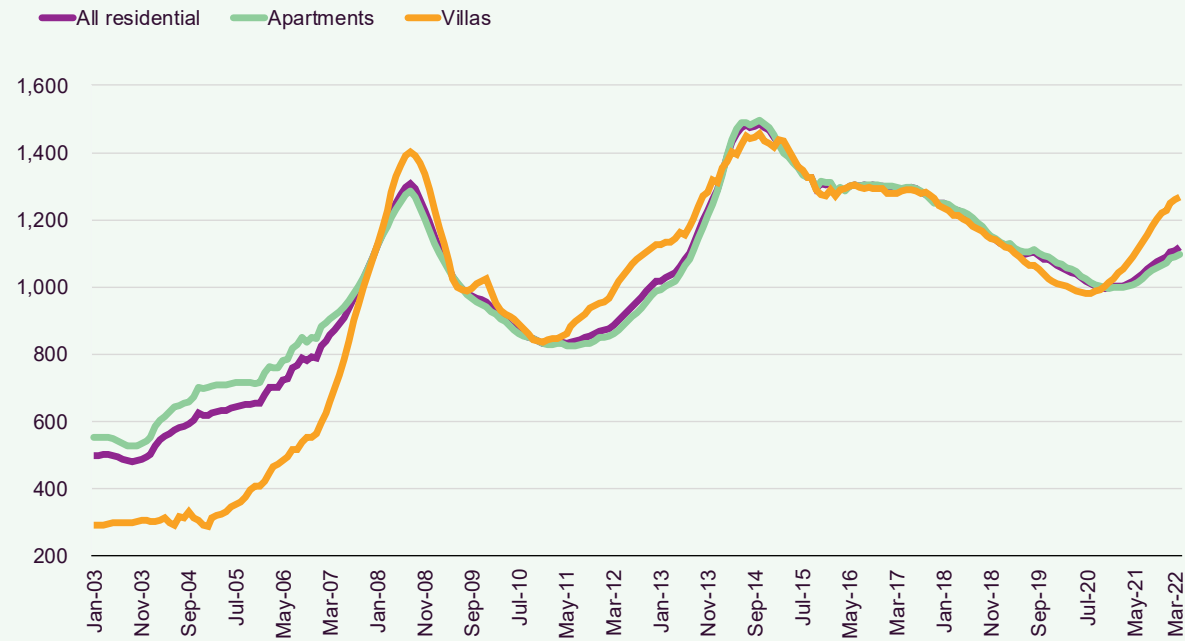
So, what does all of this mean for Dubai's residential real estate market? First, let's recap on current performance. Prices in Dubai's residential market continue to expand, with Prime residential prices, encompassing the Palm Jumeirah, Emirates Hills and Jumeirah Bay Island, surging by 58.9% over the last 12 months.

Overall, house prices in Dubai grew by 10.6% last year and rose by a further 2.6% during the first three months of 2022. The latest increase leaves values 11.3% higher than Q1 2021; the highest rate of annual growth since January 2015.

Despite the sharp turnaround in prices, values are still, on average, about 25% below their 2014 peak, but villas are now just 12.9% below the last market high in 2014.

Residential price performance in Dubai

AED psf



Source: KnightFrank

Affordable luxury

The positive market sentiment, driven by the government's world-leading response to the pandemic, coupled with the successful hosting of the World Expo, the reopening of travel corridors and Dubai's global safe-haven status continues to underpin the residential market.

This, alongside the world-leading response to the pandemic and the softer factors that make Dubai such an attractive place to live and work, are boosting the city's appeal amongst the international elite as evidenced by the record spike in ultra-prime (US\$ 10m+) home sales in the last 12-months. This has also included the most expensive villa ever sold in Dubai – a US\$ 76 million villa on the Palm Jumeirah.

In addition, Dubai remains relatively affordable when compared to other global locations. US\$ 1 million, for instance, secures approximately 1,330 sqft of prime residential real estate in Dubai – this is about four times more than you would be able to purchase in London or New York's prime residential markets.

“The bulk of deals at the top end of the residential market are cash purchases, in large part due to the unrelenting influx of ultra-high net worth capital targeting Dubai's most expensive homes”

The impact of rising base rates

In any case, rising base rates are a question of when, not if in the UAE. The UAE's fiscal policy correlates with that of the US Fed, due to the Dirham's fixed exchange rate – indeed the headline base rate was recently raised by 50 bps to 2.25% by the UAE Central Bank.

However, despite this, the threat to the stability of the residential market appears low. During the first five months of 2022, just 17.9% of the residential market, by value of deals, was made up of mortgaged buyers, compared to 40% last year and 52% in 2007.

While there appears to be a decrease in residential mortgage lending, as at the end of May there had been almost AED 38 billion of financing extended across all real estate asset classes. Extrapolating the number of transactions, we have seen so far this year, 2022 could be on course to see the second highest level of mortgaged deals in the last five years for the whole market. The main challenge is for banks to keep pace with the current growth of the market and the subsequent demand for mortgages.

Right now, the bulk of deals at the top end of the residential market are cash purchases, in large part due to the unrelenting influx of ultra-high net worth capital targeting Dubai's most expensive homes. A persistent and intensifying wave of UHNWI capital from markets as varied as Monaco, Singapore, Hong Kong, Austria, Switzerland and even mainland China continues to zero in on the emirate's residential real estate market.

Real estate still an excellent hedge against inflation

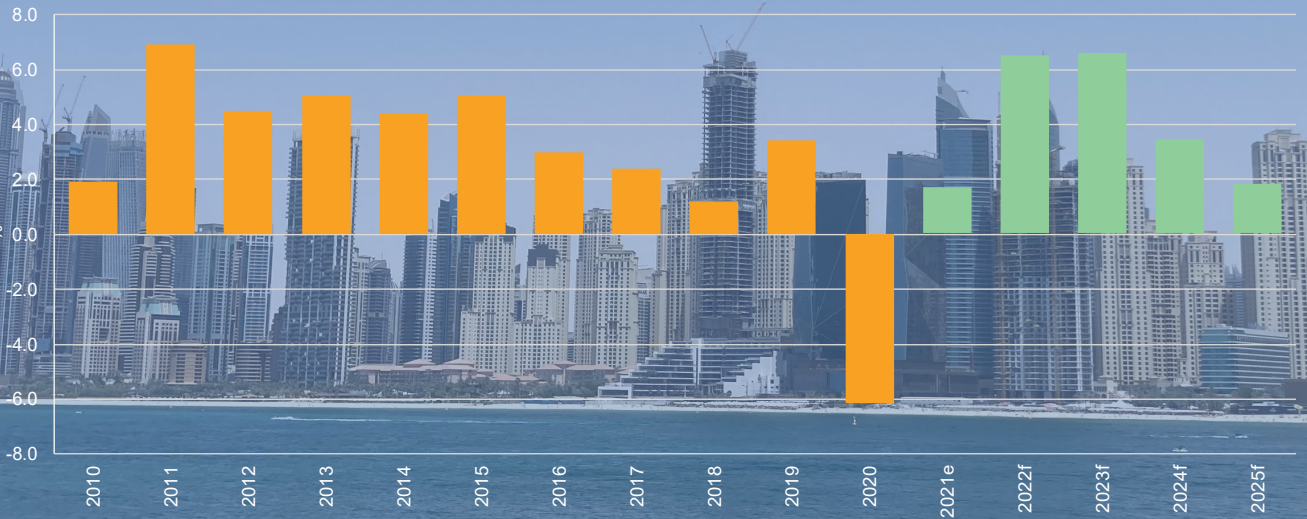
The other big factor to consider is future house price growth. With our forecasts for values expected to remain well ahead of inflation, residential real estate still offers an excellent hedge against inflation. Clearly it is unlikely prime values will rise by another 59% this year – it is unsustainable and unhealthy for the market, so price increases will undoubtedly be less vigorous.

However, with international UHNWI demand showing no sign of weakening, coupled with the dearth of high-end homes, means we do expect the top end of the villa market to continue outperforming the mainstream market.

Last year, the mainstream residential market saw prices increase by about 11%. Our forecast for the mainstream market for 2022 is 5-7%, so nearer the long-term average (5.5%).

For Dubai's prime residential market however, we expect prices to increase by 12%-15%.

UAE GDP growth y/y change



Source: KnightFrank, Oxford Economics

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