DUBAI RESIDENTIAL MARKET UPDATE
Core Savills Research | Q2 2017

Sales and rental market performance ● Ramadan and seasonal effect on sales ● Growing off-plan market and its effects
Foreword
Dubai’s residential market performance and its future course is something that cannot be generalised in a sweeping statement: it requires a granular analysis as it is not functioning as a single entity and continues to fragment further. In a market where a significant section of occupiers are transient, we see several factors having impacts on the submarket dynamics – such as seasonality, change in regulations, developers’ strategies, and of course, launch and delivery of new stock. With this variety of drivers, a clear direction on recovery is yet to emerge, with only a few locations consistently marking an upward creep.

Furthermore, sales and rental market trajectories have been diverging as sale prices were recovering and rentals falling, causing yields to contract. Through this publication, we assess the performance of Dubai’s residential submarkets in a fast changing environment.

Supply
Over 3,500 units were delivered in Q2 2017, slightly more than the 3,100 units brought to market during Q1. The delivery of Warsan Village in International City in Q2 contributed to a relatively higher ratio of 30% villas (including townhouses) compared to 70% apartments. Other deliveries were distributed across DubaiLand, Dubai Silicon Oasis, Downtown Dubai, Jumeirah Village Circle and Palm Jumeirah, notably Five Palm Jumeirah (previously Viceroys), Belgravia phase 1 in Jumeirah Village Circle and Volante in Business Bay.

We expect deliveries to slow down in Q3 and pick up pace again during and after Cityscape in September. Our conservative forecast for the remainder of the year now stands at 11,200 units.

Sales Market
The number of transactions in Q2 across Dubai was 6% higher when compared to the same period last year, while the total value remained almost equal, albeit lower than Q1.

On the desirability scale for buyers, the core apartment districts of Dubai Marina, JLT, The Views and The Greens continue to witness a steady transaction activity. Nevertheless, outer areas are seeing the most number of supply deliveries and only a few buildings in Jumeirah Village, Dubailand and Al Furjan gained traction from price conscious buyers. We observe higher movement in the villa districts across the low to mid-market segment of Jumeirah Village and Mira, while the centrally located villa districts of The Springs and The Meadows to have seen steady demand over the last few quarters.
Prime Market

Most prime villa markets witnessed a positive second quarter performance, with Emirates Hills and Palm Jumeirah marking an uptick for the first time in 2 years. This upward movement in markets that fundamentally lack liquidity was mainly due to a few large transactions having a significant statistical effect on the district average.

Similar statistical bias was witnessed in the apartments on Palm Jumeirah with the overall average increasing, as hotel apartments and upscale buildings saw a few big-ticket transactions. The rest of the prime districts continue to soften in secondary sales performance although the off-plan sales remain steady, particularly for Downtown Dubai and Dubai Marina.

Mainstream Market

The mainstream market displayed disparity with a few areas marking a rise, while others observed a ‘double dip’. The outer areas of Dubailand and Dubai Sports City maintained a relatively stable upward momentum. Discovery Gardens displayed a classic case of double dipping, with newer developments by Aziz being delivered in close proximity to the submarket at very competitive prices. These new projects benefit from the social infrastructure available within Discovery Gardens, therefore causing a migration of buyers out of this district, adding downward pressure on prices.

The Views, The Greens and JLT have shown negligible variance in sale prices, displaying maturity in these established apartment submarkets on the back of higher transaction volumes. Both apartments and villas in Jumeirah Village Circle have started to show marginal appreciation as the district nears completion and achieves higher occupancy levels, leading us to mildly adjust our previous forecast for Jumeirah Village to a more positive outlook.

Interestingly, after leading the recovery trend for the villa districts, The Springs and The Meadows marked a slowdown due to the trickle-down effect of Mira’s delivery in Reem. Both communities are managed by Emaar but Mira is considerably newer and relatively cheaper, enticing a section of potential buyers away from The Springs and Arabian Ranches’ smaller units. Long-term investors and occupiers who are keen on central locations are the ones holding interest for these core markets.
Ramadan and seasonal effect on sales

With the prevailing sentiment that property sales slow down during Ramadan, we investigated transaction volumes in detail to gauge whether it does cause a detrimental effect on sales. We looked into data from 2010 to date and calculated transaction volumes to analyse monthly peaks and troughs throughout the years.

Our findings show that over the past 8 years, peak transactional numbers have consistently concentrated in March, June and December – marking the end of Quarters 1, 2 and 4 respectively. Performance in March and December have an amplified effect due to financial year closures, while June’s peak is attributed to sellers and buyers attempting to finalise transactions before the summer lull.

The onset of summer is undoubtedly the biggest factor affecting the sales market, evidenced by August being the slowest month of the year followed by September; notably not coinciding with Ramadan. This trend is further intensified by the summer break in the academic calendar when a majority of families travel. As expected, sales activity tends to increase on their return.

Since Ramadan has fallen during the summer months over the last few years, there is a perception that sales slow down as a direct consequence of the Holy month, which (as explained above) is not supported by facts. Contrary evidence suggests that people travel less during Ramadan and have more time to conduct property searches due to the reduced working hours.

According to findings of a 2016 YouGov survey of 1,523 people in the UAE, Saudi Arabia and Egypt, 72% of respondents had no plans to travel during Ramadan, with most preferring to stay in their country of residence.

Another key factor affecting sales seasonality has been the changes in regulations: for example, the transfer fee regulatory amendment in October 2013 (when fees were doubled) caused that month to record the slowest activity since 2011.

Sales performance during Ramadan 2017, with respect to the rest of the year, is yet to be quantified although we have seen many big-ticket transactions conclude across prime locations. Transaction volumes in the mid-market segment remained steady with deal-seeking buyers keeping the market considerably active. We expect the number of transactions to have fallen early July, due to the above reasons, with the usual recovery starting mid-September onwards.

As Ramadan moves away from summer in the coming years, we do not foresee the holy month to be a significant factor to negatively impact transaction activity.
Rental Market

In line with our previous forecast, rentals have continued to soften across the board with only one exception marked in Dubailand, possibly due to low entry level rents. Tenants are increasingly conscious of current market conditions and many have successfully renegotiated contracts while others have shifted homes, either upgrading to a better unit at a similar or lower rent or downsizing, depending on how their housing allowances/income is affected by the ongoing economic conditions.

We also note there is a statistical bias in calculating rental drops, as the market is largely transacting at the lower end of the spectrum bringing the area average down. This has let some market commentators to over-report the amplitude of the actual rental softening. Nonetheless, rental contractions of varying degrees are felt across the 18 of the 19 submarkets we track.

As in other parts of the world, rentals tend to lag behind the sales market performance by some time, which is particularly the case in Dubai due to longer lease terms as rents are often paid a year in advance. This lag was prominent two years ago as landlords were resistant to adjust rents in line with overall market softening and drop in sales prices. This resulted in ‘negative potential energy’ building up as tenants usually don’t consider relocating for around 5% rental differential due to the inconvenience and additional costs involved in the move.

As the market dropped further and rents lost momentum by 15-20%, this accumulated friction has now resulted in a seismic shift causing a delayed and amplified downward adjustment in rents. Furthermore, with lease terms generally ending between March to September (when new tenants arrive in the country while many existing tenants shift during the school break), we expect a larger movement of tenants during this period. As a result, we are now finding landlords to be susceptible to negotiations by compromising on yields to retain or attract tenants, sometimes even over-adjusting to their detriment. Multiple cheques are becoming more common to incentive tenants, as landlords aim to keep their headline rents steady.

Nonetheless, few districts continue to notice an active rental market in core locations such as Dubai Marina, JLT, The Greens and The Views, where well-maintained units advertised at competitive rents are easily absorbed within 2 to 3 weeks.

Lastly, looking at the overall market, a major factor affecting the widespread rental drops is the contracting pool of renters in the last 2 years due to macroeconomic employment deterrents while new expat demand has not fully covered the gap. Of this decreased occupier demand, a segment of tenants who could afford to shift to ownership in the backdrop of lower sales prices and favourable payment plans have done so – further reducing the existing pool of renters. While rental yields have seen compression, they remain relatively high, with the cost of renting vs owning still comparatively more expensive than other global cities.
Outlook

We stand by on our previous forecast of further rental drops throughout the summer months, but expect rents to start stabilising in core locations by next year while predicting potential room for softening in the secondary locations.

Rental depreciation witnessed in the last 12 - 18 months is yet to have a significant negative influence on the sales market, however it does slow the recovery of sale prices. Although yields have contracted, they are still northwards of 7.5% for most apartment districts and 5.5 - 6% for mid segment villa districts – relatively higher than other forms of investments in the region. This led us to run a simulation on 20 prominent properties across Dubai to gauge at what rental level would the yield cease to be attractive to investors.

Our findings reflected that rents would have to be between 25-40% (depending on the location) lower than the present level to start having a notable negative impact on the investor market and prices – even with the present subdued rental market this is an unlikely probability over the next 24 months.

With other aspects of demand such as relatively positive economic outlook, a marginal uptick in job creation and adjustment to stagnant oil prices at around $50 per barrel, we are cautiously optimistic on mid-market sale prices while expecting further room for softening in the prime segment. We remain watchful over growing off-plan sales and lucrative payment plans which continue to undercut both low and mid segment sale prices as well as adding systemic risk to the overall market – something which might require further regulatory strengthening.
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