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Killing Them Softly: The Impact and Incidence of Off-plan

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Executive Summary

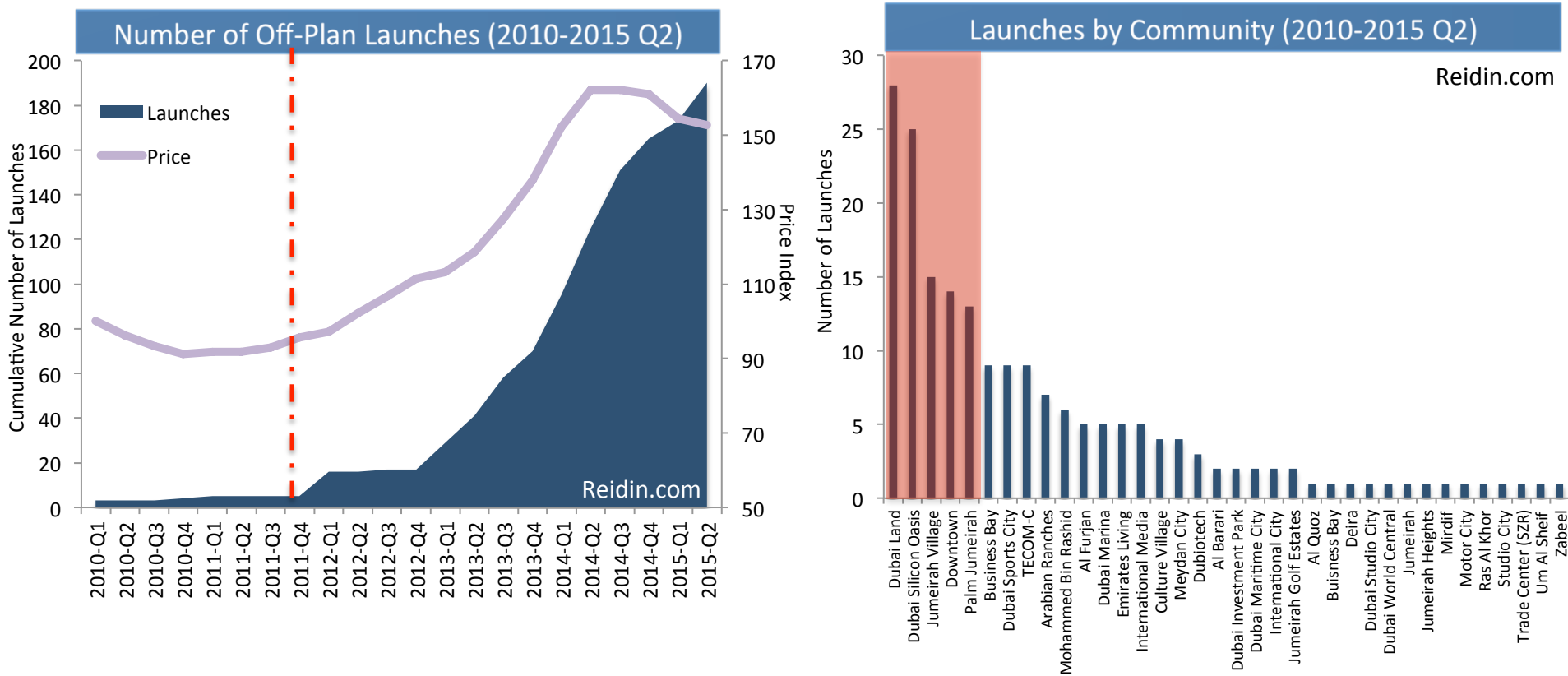
- Since Dubai's price recovery in 2012, a flurry of off-plan units were launched in the market as developers tried to capitalize on the rising prices and strong demand. Initially, the launches were skewed towards prime properties as developers tried to maximize margins. However as the demand and supply mismatch began to widen developers changed course to service the need of the mid-income market.
- As the flurry of off plan launches gathered momentum, liquidity was sucked out from the secondary market, as investors and speculators rushed to the primary market to capitalize upon payment plans. This has resulted in a drop in secondary market activity of 26% on a YoY basis.
- Initially, off plan launches were at prices systematically higher than what was prevailing in the secondary market; this trend has reversed in the last 12 months, where off plan launches have been at levels that have averaged 20% below the secondary market rates; this has caused prices to soften in the secondary market by approximately 15% on a city wise basis. With launches expected to continue post Ramadan, the outlook for capital gains in the medium term remains limited.
- A bivariate analysis of launches between residential and commercial units, shows that only 4% of new launches have been in the office segment. Developers have not yet focused on the commercial domain, due to the lingering effects associated with the boom bust cycle that culminated in 2008. However, since Dubai's asset price revival, office vacancy rates have fallen as company formation gathers momentum, which is reflected in rental rates between both segments in the last 12 months (Offices have outperformed: JLT-Residential: 3%; JLT-Office: 10% and Business Bay-Residential : -2%; Business Bay-Office: 19%)
- We opine as residential prices in the secondary market begin to dip due to the discounted offers in the primary market, developers will shift course towards the office segment in order to cater to the pent up demand. Moreover, until off-plan launches remain below the secondary market prices, an upward trend will be curtailed.

The Launches of Off-Plan properties



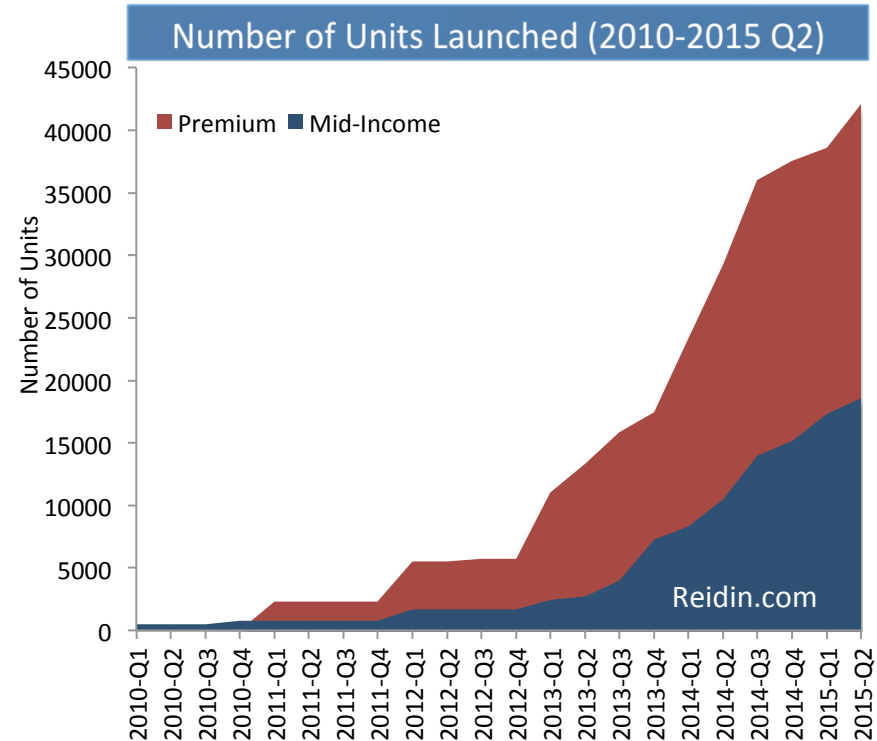
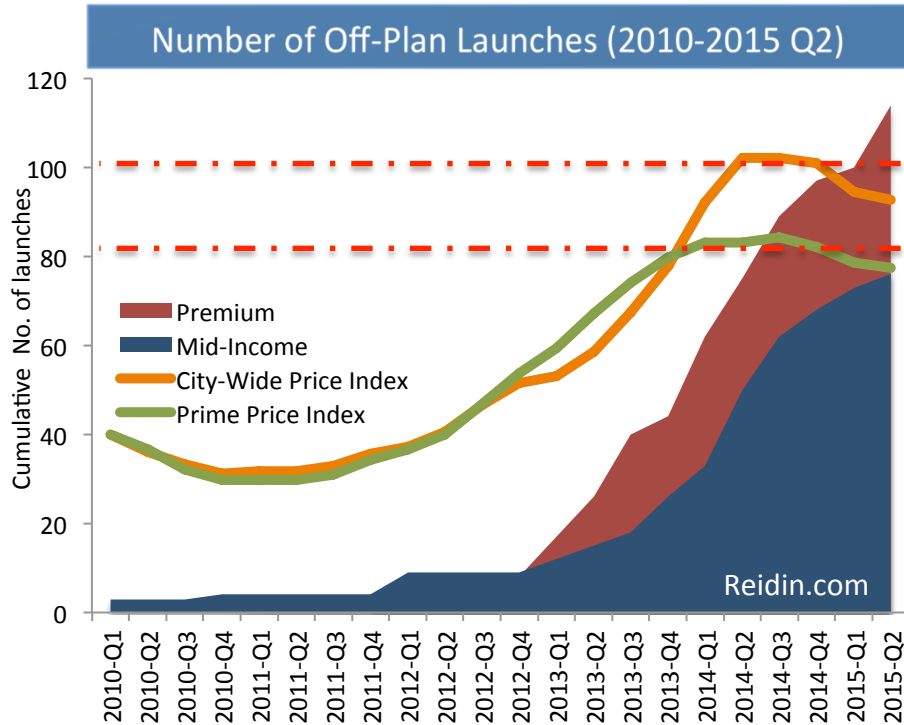
“You never change things by fighting the existing reality. To change something, build a new model that makes the existing model obsolete.” — R. Buckminster Fuller

Off-Plan Launches Takes off Exponentially



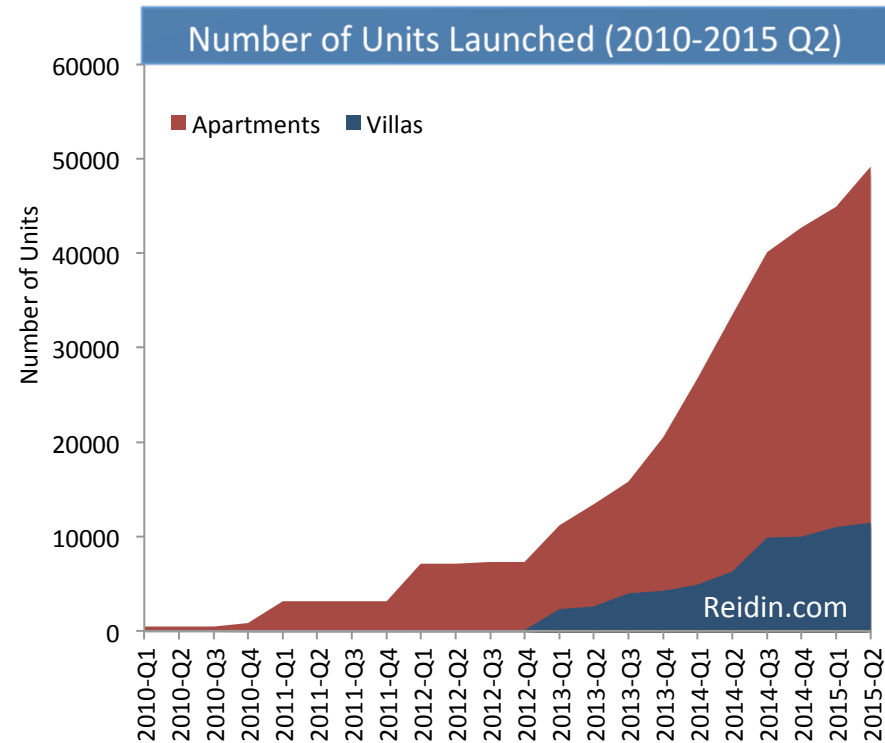
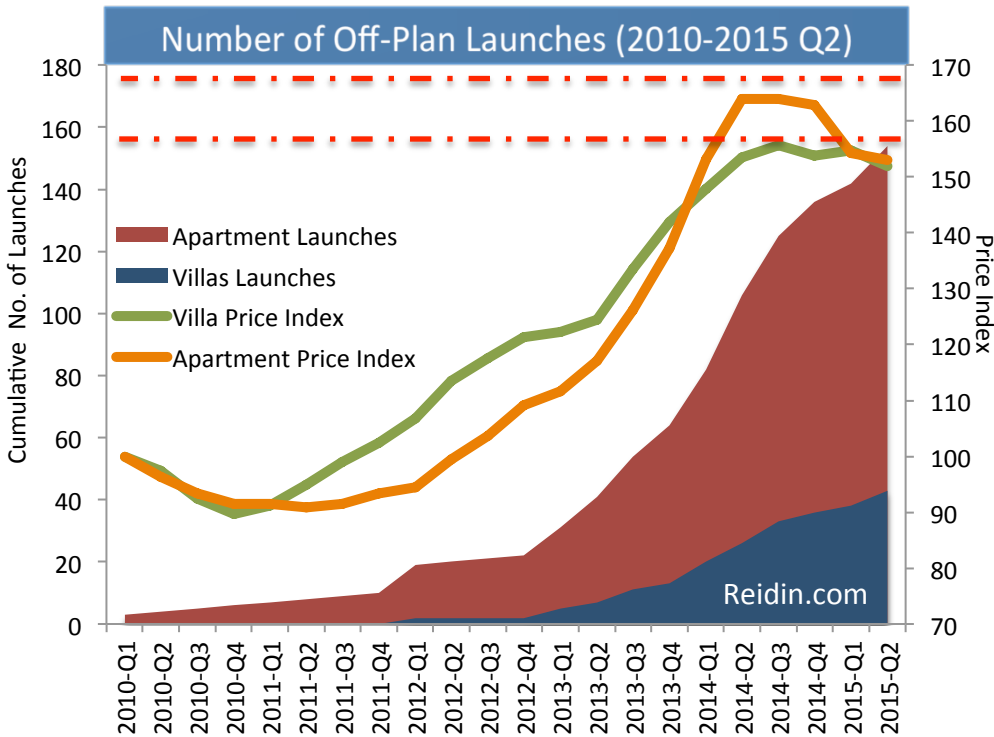
A time series analysis of off-plan activity in the real estate market shows an exponential increase of launches in 2012, which is about the same time as asset prices began to rise after the crash of 2008. A community-wise bifurcation shows that the most number of launches has been witnessed in Dubai Land and DSO, followed JVC and Downtown.

Swap between Premium and Mid-income Property Launches Transpire



The highest margins for developers have historically been in premium projects as it has the largest spread between replacement value and selling price. As developers rush to capitalize on the asset boom of 2012, a flurry of prime project started to launch. As prices at the high end began to taper off in 2014, developers switched course, starting to offer a plethora of choices in the mid market segment in the last 12 months.

Villas and Apartments



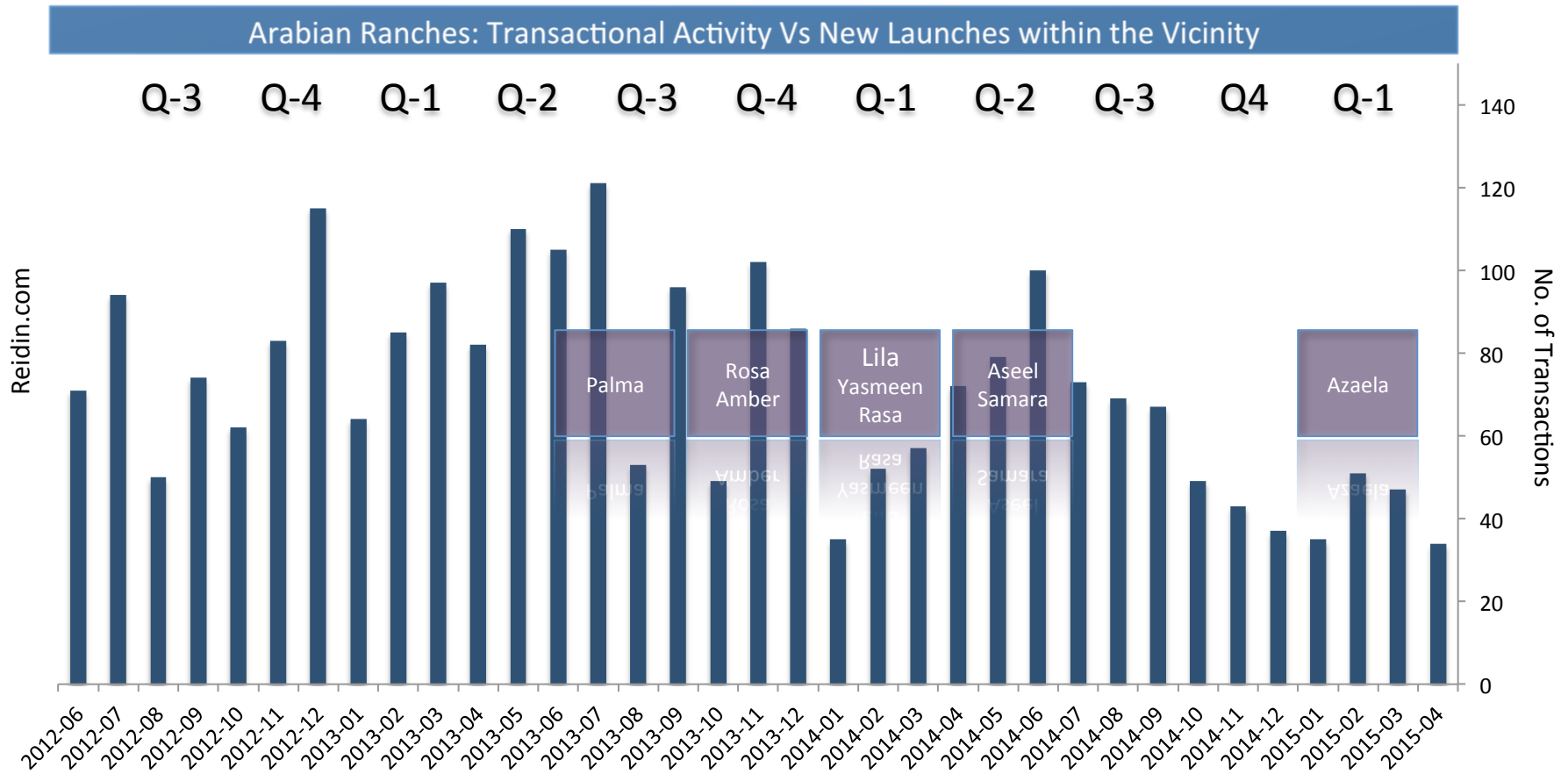
A largely similar trend appears to have been witnessed between apartments and villas. The exuberance in villa prices in 2012/13 lead to a flurry of launches in this space, and in 2014, the ratio of apartments to villa launches was slightly less than 3:1. However, as markets adjusted to the rising relative supply of horizontal developments causing prices to stagnate, developers quickly altered course; as of 2015, the ratio of launches was at 5:1 which is at or near the long term city average.

Effect Off-Plan Launches on Ready Units



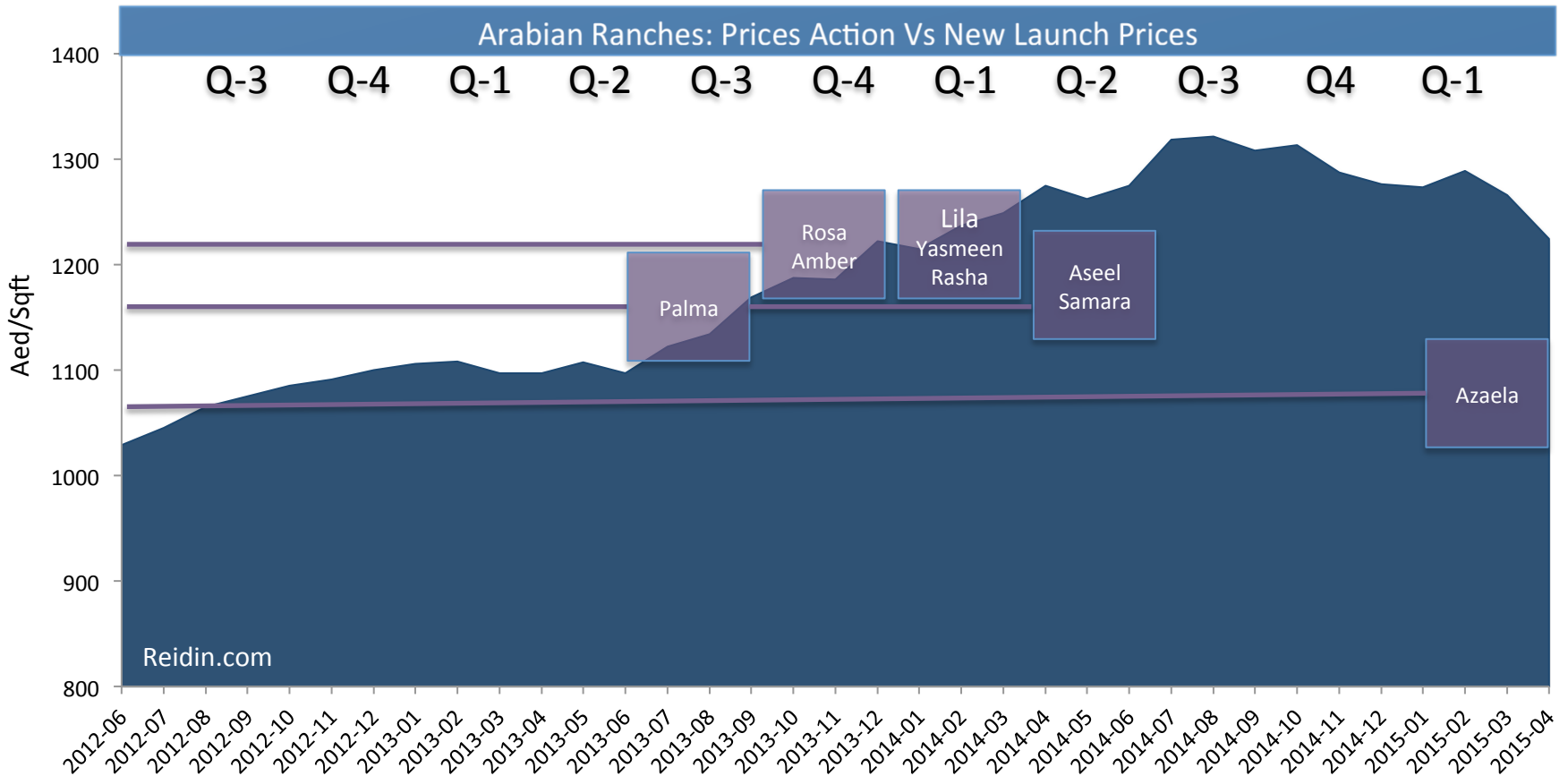
“Supply always comes on the heels of demand” - Robert Collier

Ranches: Transactional Slow Down Coincide with Off-plan Launches



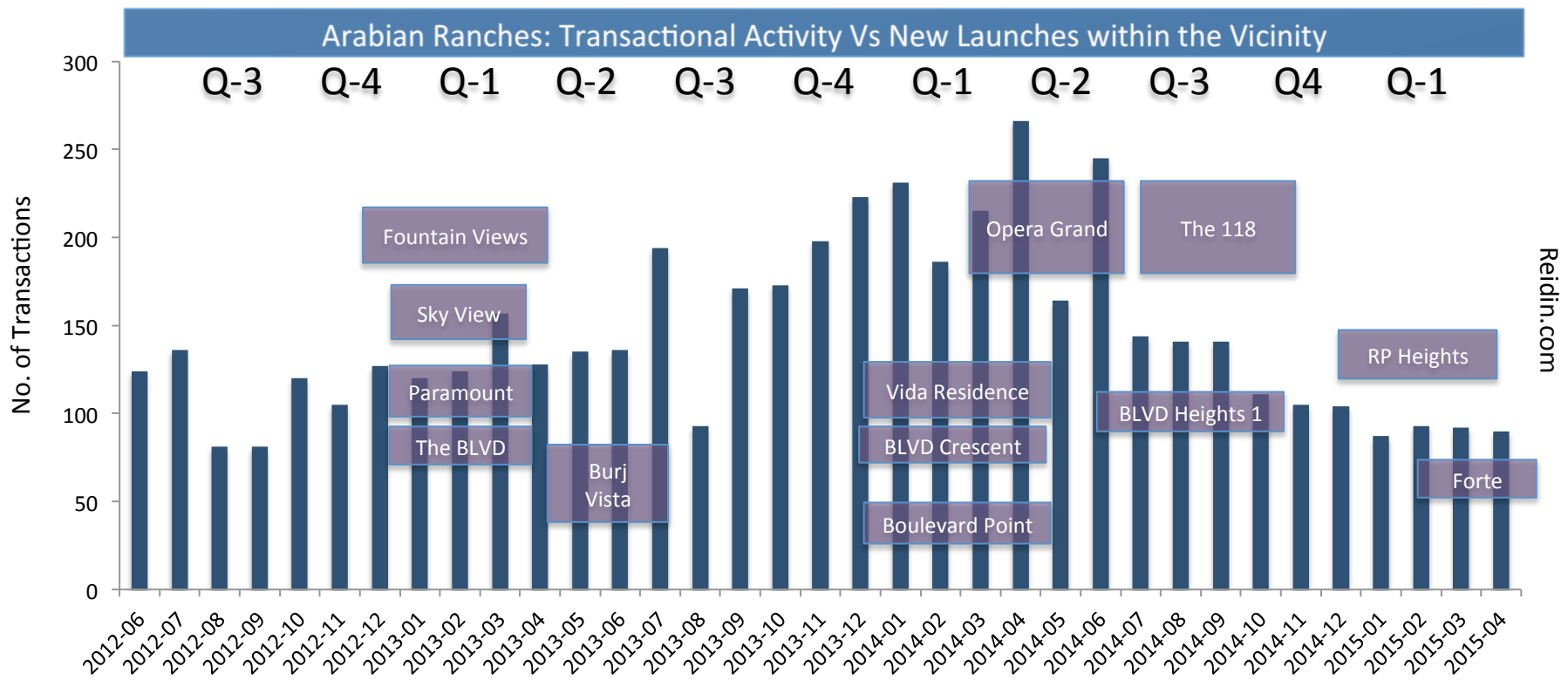
A transactional activity analysis of Arabian Ranches, plotted against the new launches within the Ranches extension shows an obvious decline of activity in the secondary market. This coincided with exogenous factors such as the strengthening of the US Dollar as well as the decline in oil prices, but it is apparent that the number of launches played a significant role in the tapering off of transactions in the secondary market.

Ranches: Ready Units Fall to Off-Plan Prices



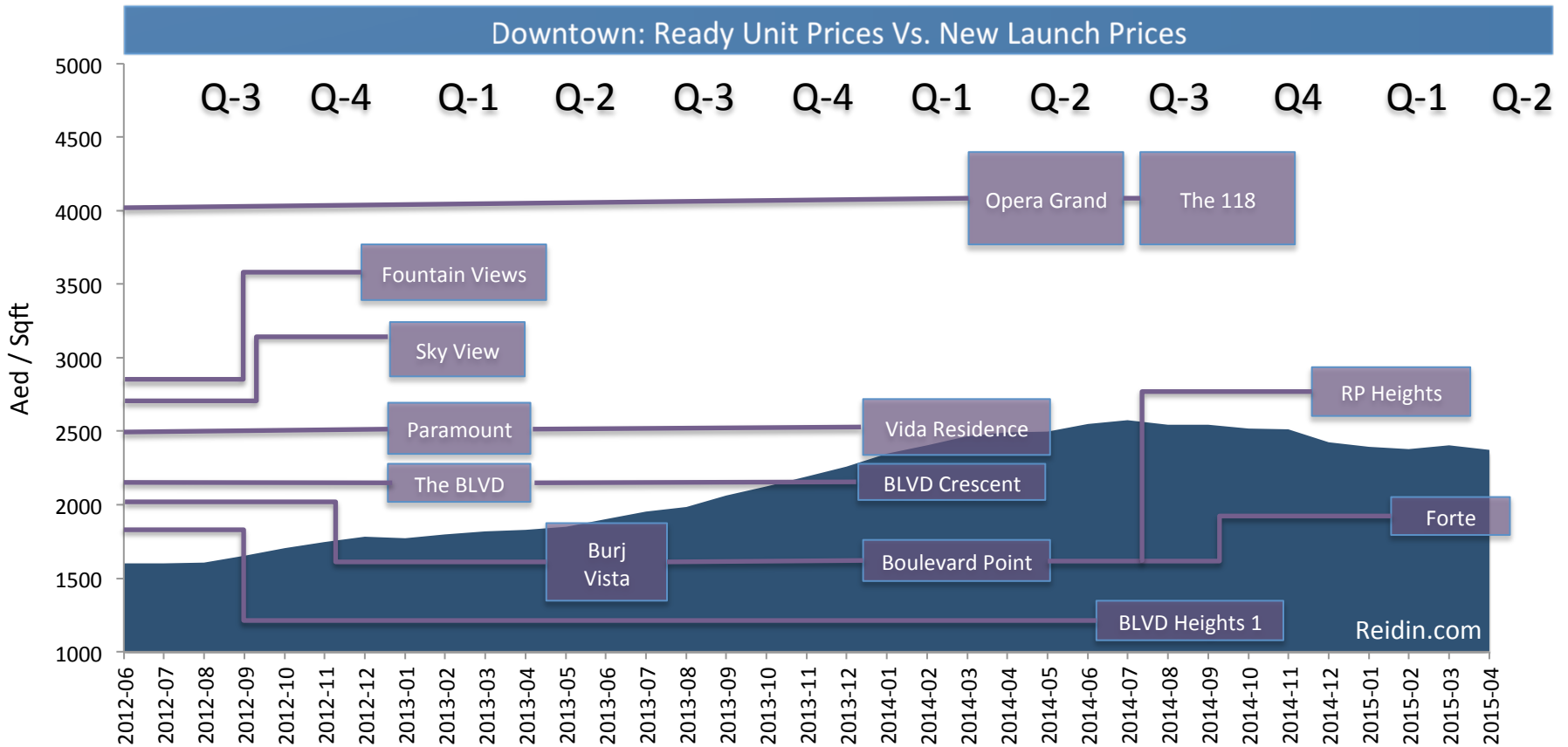
An analysis of Arabian Ranches shows that prices have begun to trend downwards as new launches within the same vicinity begin to start offering similar products at lower prices. Although there was locational differences, investors responded to the new lower priced launches by “switching” from the ready to off plan market causing prices to start declining in Q3 2014.

Downtown Dubai shows a Similar Trend



Downtown Dubai witnessed a similar trend, where transactional activity started declining in response to the wide number of new launches being offered in the district.

Ready Unit Prices in Downtown Trend Closer to the Off-Plan Launch Prices



A price analysis of Downtown plotted against the off-plan launches shows the impact of the primary market. Off-plan properties till mid 2013 were launched above the price of the secondary market, pushing it upwards. However, since then (with few exceptions), the new launches have been systematically lower than the secondary market, causing prices to trend lower.

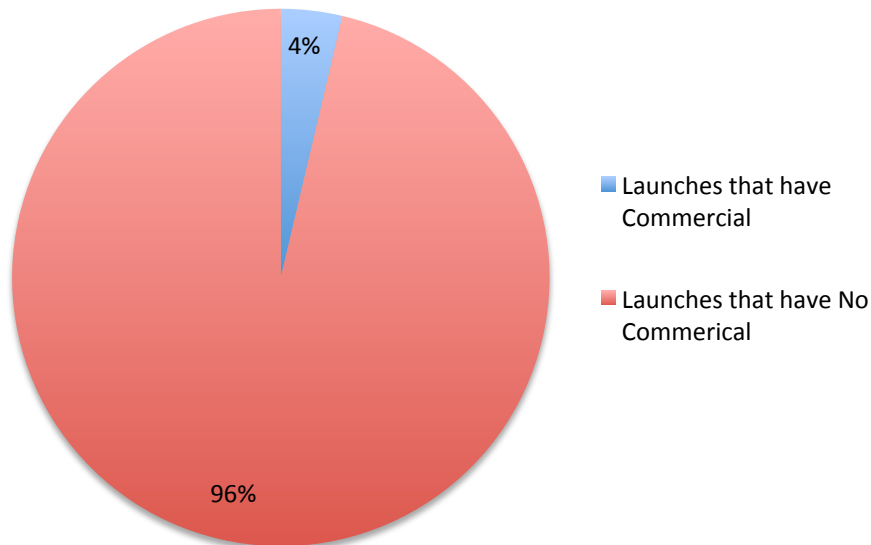
Where are the Customer's Offices?



“To be truly rational, you can’t hold a conviction without significant empirical evidence” – Alan Greenspan

Commercial Realty Launches Virtually Non-existent!

Number of Off-Plan Launches (2010-2015 Q2)



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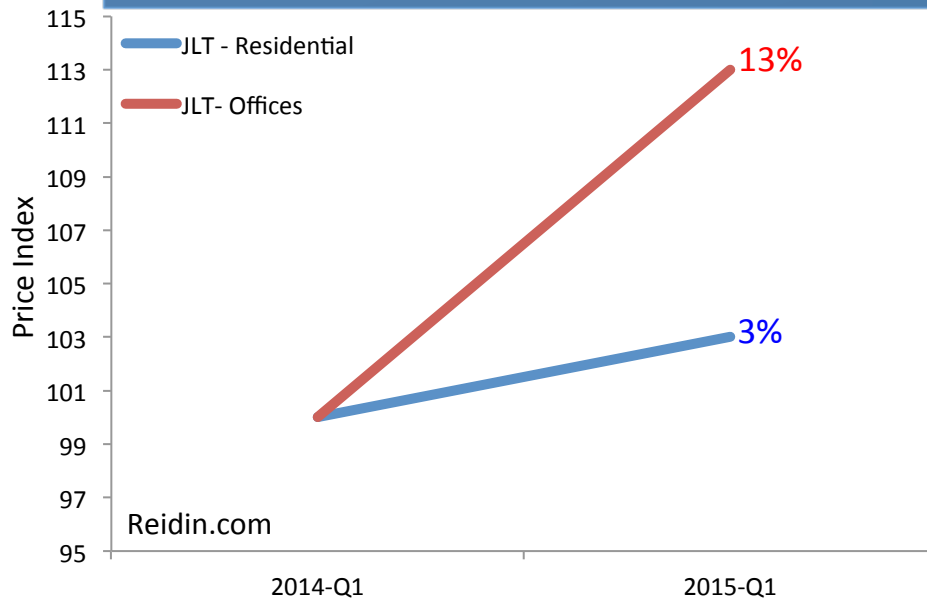
List of Commercial Launches

Building	Launch Date	Location
Jewel Of The Creek	2011-Q1	Deira
Yass Tower	2012-Q3	Culture Village
Tayyeb Mohammad Ibrahim Towers	2013-Q1	TECOM-C
Palazzo Venezia	2014-Q1	Majan
The Onyx	2013-Q4	Emirates Living
Royal Estates	2014-Q3	Dubai Investment Park
RP One	2015-Q1	Downtown

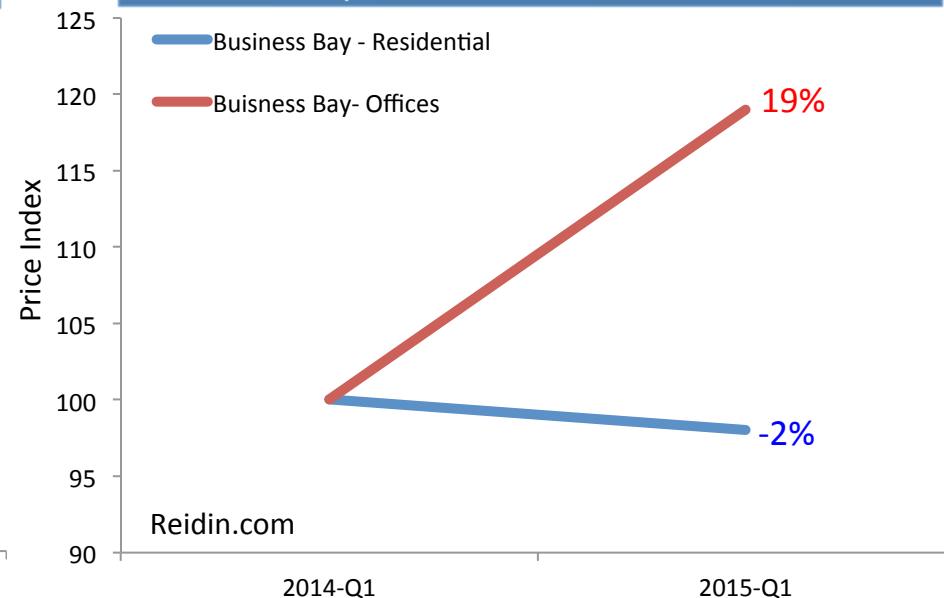
A sector-wise analysis of off-plan launches in the last 5 years reveals that, commercial properties only account for 4% of all launches. This was largely due to the overhang of supply in this segment from the last boom bust cycle of 2008.

Pent Up Demand for Office Witnessed in Rental Rates

JLT Rental Index: Offices Vs Residential



Business Bay Rental Index: Offices Vs Residential



This shortfall for office supply can be seen in the rental rates between both segments. In the last 12 months office in JLT and Business Bay have outperformed their residential counterparts, which has not been the case historically. However, as this demand continues to rise within this segment we opine that a flurry of off-plan projects will be launched as developer try to take advantage of the high margins.

Conclusions

A time series analysis of off-plan activity in the real estate market shows an exponential increase of launches in 2012

Developers have not yet focused on the commercial domain, due to the lingering effects associated with the boom bust cycle that culminated in 2008

Dubai's Off-Plan Launches

Since the second real estate boom cycle (2011-2014) of Dubai, a plethora of new off-plan units have entered the market.

As developers rush to capitalize on the asset boom, they had primarily focused on premium products as it had the highest margins. However due to supply and demand mismatch they have shifted course towards mid-income housing.

A similar trend appears to have transpired between apartments and villas. As markets adjusted to the rising relative supply of horizontal developments causing prices to stagnate, developers quickly altered course

Offices Vs Residential Launches

A sector-wise analysis of off-plan launches in the last 5 years reveals that, commercial properties only account for 4% of all launches. This low number is a reflection of the overhang of supply that existed after the crash of 2008.

As Dubai's economy rebounded in 2012 it diversified out of the real-estate sector; company formation is escalated in various other domains (i.e. tourism, financial services).

This rapid increase in company formations has caused a stealth rally in the office segment, which is reflected in the rental growth rate.

Impact of Off-plan launches on Ready Units

As new launches within certain communities roll out (i.e. Ranches and Downtown) an obvious decline of activity in the secondary market is witnessed. This phenomena has coincided with exogenous factors such as the strengthening of the US Dollar as well as the decline in oil prices.

Towards mid 2014 developers switched price points for launches from above the secondary market trend line to below, pushing prices for ready units lower

Conclusion

We opine that a flurry of new off-plan units in the commercial segment will be launched as residential prices in the secondary market begin to fall.

Developers will begin to change course again towards the commercial segment in order to cater to the pent up demand, and as well as maximize margins in their developments

Moreover in the residential segment, until off-plan launches remain below the secondary market prices, capital gains prospects will be limited



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Research Database

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Home Ownership: Dubai's Road to Prosperity	REIDIN - UNITAS Real Estate Market Reports	12-Mar-13

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“No barrier can withstand the strength of purpose”

HH General Sheikh Mohammed Bin Rashid Al Maktoum
The Ruler of Dubai and Prime Minister of UAE

