Kingdom of Bahrain

Quick Stats

Change from

Lease Rates	Q1 10	Q4 10
Office	↘	↘
Residential	↘	↘
Sale Prices	**Q1 10**	**Q4 10**
Residential	↘	↘

Hot Topics

- "Domino Effect" sweeping region amplified the demands of the regular opposition protests in Bahrain to a higher and more serious level.
- GCC announces aid package of $10 billion likely to be used for housing and infrastructure projects.
- Government confident that Bahrain remains on target to achieve 4.5% growth in 2011.
- State of National Safety appears to have calmed daily activity, with most of Bahrain back to 'business as usual'.

OVERVIEW

From being ranked third for "best expatriate experience in the world" in a recent HSBC survey, the Kingdom of Bahrain's image has swung 180 degrees, with recent political unrest attracting global media coverage.

Despite this, few expatriates have left the Kingdom on a long term basis and emergency flights arranged by the UK FCO in March left virtually empty.

Throughout February and March a number of national reforms were initiated in a bid to appease growing political unrest including a payout of BD1,000 per family, reshuffling of cabinet ministers, the creation of 20,000 new jobs by the Interior Ministry, and the announcement of plans to build 50,000 social housing units over a five year period at a cost of BD2.5 billion.

Mindful of the need to ease tensions in Bahrain, the GCC, led by Saudi Arabia, also announced a $10 billion aid package for both Bahrain and Oman, two of the six GCC states currently struggling with turbulent domestic politics.

While details of the GCC aid package remain to be specified, the funds in Bahrain are likely to be allocated to housing and infrastructure initiatives.

However, with Formula One "called off", low levels of visitation by Saudi and Kuwaiti nationals and business travel curtailed, the hospitality and leisure industry has experienced a substantial setback so far this year.

After being ranked second in the region for its tourism and travel competitiveness, according to the Travel and Tourism Competitiveness Report released by the World Economic Forum, hotels in Bahrain are currently achieving occupancy rates of between 5% and 10%.

It is hoped that this will be just a temporary setback, but several hotels previously rushing to meet the Formula One opening deadline in March have put back their formal openings until after the summer period.

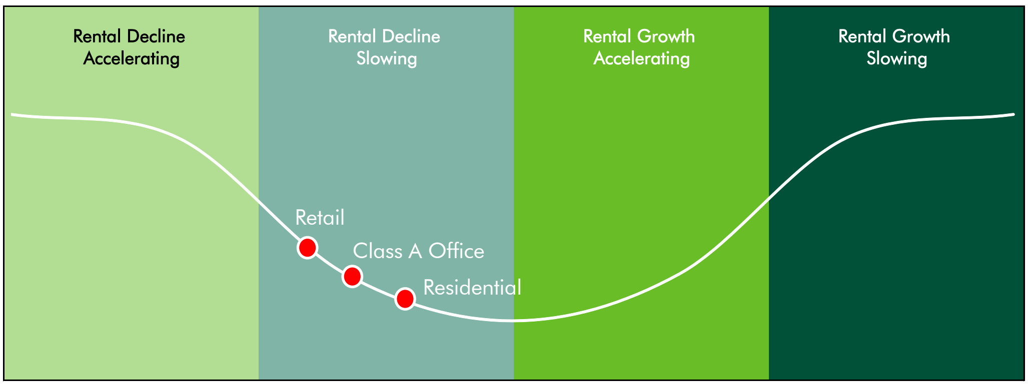
Retail malls have also been quiet but activity levels have improved as curfew hours in Seef District have been relaxed and retailers have reported a significant upturn in business.

Moving forward, the Government remains confident that Bahrain's economy is still on target to achieve the 4.5% growth projected for 2011, despite the recent unrest and is committed to supporting all sectors of the economy to this end.

Banks have been asked to help small and medium enterprises (SMEs) affected by the troubles, and they have been relaxing loan conditions as a result.

The extent of permanent outward movement from Bahrain by staff and businesses has been only very limited to date. However, it is very possible that some foreign companies will be considering their options, although the full extent to which FDI and residential and commercial space demand will be affected is not likely to be fully apparent until after the summer period.

Market Cycle, Bahrain Q1 2011



Source: CB Richard Ellis

Quick Stats

Lease Rates	Q1 10	Q4 10
Office	↘	↘
Sale Prices	**Q1 10**	**Q4 10**
Office	N/A	N/A

Change from

Hot Topics

- Office market continues to be faced by large quantities of available office space met by limited demand.
- Rental rates continue to decline in order to sustain occupancy rates.
- Fitch and S&P drop Bahrain's credit ratings by two notches to BBB.
- Moodys still rates Bahrain at A3 but with a review for possible downgrade.

OFFICE MARKET

While many businesses are contemplating their current and future presence in Bahrain, strategic business decisions are not made overnight, and it will likely be several months before the full impact of the current crisis on the office rental market will be fully understood.

Faced by significant oversupply, the result of somewhat irrational exuberance in 2007 and 2008 which led to significant numbers of building starts, subsequently unmatched by demand growth, the office market is likely to have high levels of vacancy at least in the short and medium term.

As a consequence, rental rates have fallen by circa 30% since 2008, with the result that Bahrain has become an extremely competitive location from which to do business. Purpose built prime office accommodation in the Kingdom's CBD is now available at around BD6/sqm/pm, making Bahrain one of the cheapest places in the GCC from which to do business.

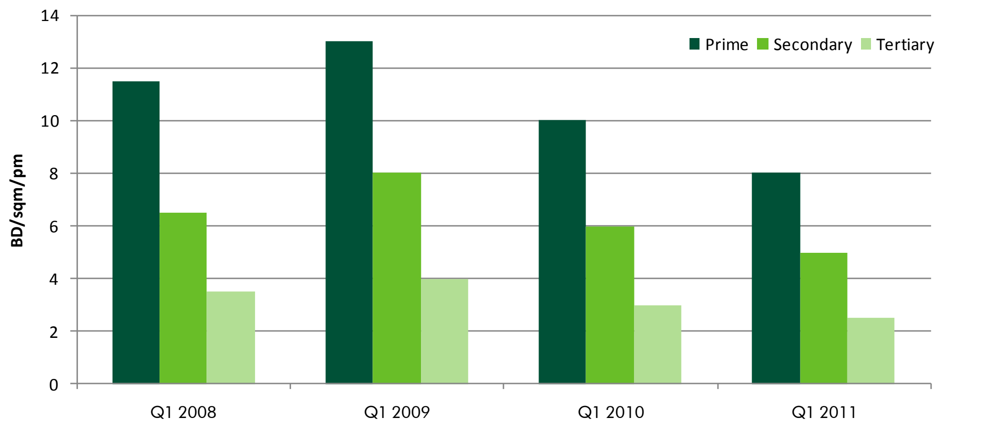
Despite the political tensions in the Kingdom, the banking sector remains the best regulated in the GCC and is still home to well over 400 financial institutions. Operating as a banking sector is not just about shiny new office space, the key remains the regulatory environment, an issue which Dubai and Doha in particular, have never fully embraced.

However, the key advantages that Bahrain has always treasured have been the well regulated financial environment and political stability. With one of these cornerstones of the economy removed, at least in the short term, it remains to be seen what impact recent events will have on FDI and corporate appetite to do business in the Kingdom.

Office space rental rates have come under the most severe pressure in the last two years in the CBD (Diplomatic Area), where parking and circulation issues have become so chronic that new business is being drawn to secondary locations such as Seef District and even existing tenants are being lured out of Diplomatic Area by more convenient accommodation, albeit at higher rates.

With prime office space rental rates in decline, there has been something of a "ripple effect" into the Class B category as office occupiers in Class B have been able to upgrade and consolidate their accommodation requirements by moving to prime space at similar or in some cases lower rents. This is especially true where owners of Class B space and their management have not been quick to spot such potential movement taking place.

Office Market Rental Rates, Bahrain – Q1 2008 to Q1 2011



Source: CB Richard Ellis

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Quick Stats

Change from

Lease Rates	Q1 10	Q4 10
Residential	↘	→
Sale Prices	**Q1 10**	**Q4 10**
Residential	↘	↘

Hot Topics

- Popularity of key expatriate residential areas such as Saar/ Budaiya, and Janabiya likely to be impacted negatively in the short term.
- Housing Ministry has been allocated a budget of over BD2 billion to build 50,000 'social housing' units over the next five years.
- Subsidised housing loans from the Government have been raised to BD60,000 with repayment terms extended to 30 years.

RESIDENTIAL SECTOR

Following the strong upward pressure on occupancy and rates that took place up to the end of 2008, rental rates declined across all categories of accommodation in the following two years to the end of 2010.

Rental rates in compounds and private villas appear to have stabilised but the sheer volume of new privately held apartment units that have entered the market in the last two years, continues to exert downward pressure on rental rates in this particular sector especially in central Manama and Juffair.

Historically, the most popular area of Bahrain for upper-income expatriates with families has been in the north-west, in and around numerous Shia dominated villages such as Saar and Budaiya. Many expatriates, especially those with families, have found the recent problems, which were very audible in this area, to be deeply troubling, and as a result there is likely to be some movement to quieter locations not so visibly or audibly affected by political differences.

These include Riffa Views and Amwaj Islands in particular, both relatively new development areas with no history of trouble and/or disruption. Both areas remained untroubled during the crisis and there has been a noticeable pick-up in rental demand in both locations during the first quarter.

Naturally, the appetite for freehold properties for sale in the current political climate has fallen sharply although this means that rental yields are extremely healthy in the villa sector, less so for apartments. The market is not sufficiently stable at present to be precise regarding the impact that recent events have had on sale prices, rental rates, yields and occupancy by type of accommodation and location, because these all need to be played out over the next three to six months.

Social and Affordable Housing

As ever, the key housing topics in Bahrain remain 'social' and 'affordable' housing. The Government simply does not have the resources to meet the housing demands of a rapidly growing , relatively low-income population of nationals. The waiting list for social housing now extends to well over 50,000 units and in some cases applicants have been waiting for 17 years.

The biggest problem in this sector comes from the Government's own regulations which prohibit Bahrainis from selling their social housing unit during the repayment term of 25 years. This means that the first unit they move into will be the one in which they will probably spend the rest of their life. Given the propensity of low-income Bahrainis to have large families this is extremely problematic in the apartment sector and understandably is causing significant dissatisfaction amongst this group.

The Housing Ministry has recently been allocated a budget of over BD2 billion to address this issue with the stated aim of building 50,000 social housing units over the next five years. However, it should be pointed out that the waiting list is growing by three or four thousand per annum and by the end of the five year period the number of applicants will have grown by a further 15,000 to 20,000.

With the regulation prohibiting movement within the social housing sector in place, it will still be difficult to satisfy existing applicants if the focus continues to fall on apartments. For obvious reasons this 'solution' will still be largely unacceptable.

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Social and Affordable Housing *(continued)*

In the affordable housing sector, which applies mainly to those Bahrainis just above the income bracket that enables them to apply for social housing, there is also a significant mismatch in demand and supply. Properties offered by the private sector to this category of Bahrainis are simply not 'affordable' to the majority of potential buyers due to constraints created by the mismatch between unit cost and the availability of subsidised finance.

The private sector has been trying to address the opportunity presented by this mismatch for some time but the problem lies principally with the price of land which moved significantly out of line with economic values as a result of the rampant land speculation that took place in the period up to the end of 2008.

Although the maximum mortgage available under Government subsidised housing loan regulations has been raised from BD40,000 to BD60,000, to be paid in 30 years instead of the current 25 years, there are few developments that can be constructed to meet these requirements at current land prices, and this issue will present a challenge if the private sector is to be harnessed to meet housing needs.

OUTLOOK

Although oil prices have risen sharply as a result of political uprisings across the Middle East, the economic windfall from this will be offset by uncertainty particularly from international businesses. It will take time for confidence to be fully restored although improved economic circumstances form oil and the GCC handout may help the Government of Bahrain to address financial and social reforms more quickly than might otherwise have been the case.

It remains to be seen how the political situation will play out, and this will be key to the Kingdom's ability to recover and grow in the near term. It was hoped that the real estate sector in particular, might start to turn a corner during 2011, but it is likely that any major recovery will be put on hold as the market adopts a 'wait and see' approach.

The number of businesses that leave the Kingdom is likely to be small, but nevertheless damaging if it does take place, new investment and growth are likely to be stunted by such uncertainty and in the short term the market is likely to be characterised by low levels of transaction activity, some consolidation activity, falling rental rates in the office sector and retail malls and weaker performance in the hospitality sector than previously hoped.

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