

Quick Stats

Lease Rates	Change from	
	Q4 09	Q3 10
Office	↘	↘
Residential	↘	↘
Sale Prices	Q4 09	Q3 10
	Residential	↘

Hot Topics

- Bahrain on target to meet 4% annual GDP growth.
- Ratings agency Fitch and S&P both reaffirm Bahrain's 'A' rating for sovereign debt with a 'stable' outlook buoyed by the rebound in oil prices.
- BD240m budgeted by Government for social housing projects in 2011 and 2012.
- In the wake of Qatar's selection as hosts of the FIFA World Cup 2022, the development of the Bahrain-Qatar 'Friendship Bridge' gains new momentum.
- Land prices in prime areas such as Seef and Juffair fell considerably between Q4 2009 and Q4 2010 with current land prices now well below 2008 prices.

OVERVIEW

According to a report from the IMF released by the Economic Development Board, Bahrain's economy grew by 4% in 2010 buoyed principally by a rebound in oil prices and fiscal stimulus. The best performing sectors were hospitality and manufacturing followed by finance, transport and communications.

With the ratings agencies Fitch and S&P both reaffirming the country's 'A' rating with a 'stable' outlook for sovereign debt in early December 2010, the IMF has declared Bahrain's near-term outlook as 'favourable'.

Though Bahrain is faced with a budget deficit of \$988.5m in 2011, the good news is that this is well below the \$3.4bn deficit originally forecast for 2010. The higher figure was based on oil price estimates of \$80 which have now proved somewhat conservative.

In a bid to expand on key social infrastructure such as housing and to cater to the growing waiting list which remains at 50,000 plus homes, the Government's budget for the next two years has revealed a significant increase in infrastructure projects.

The Government plans to spend BD240m on housing projects and BD116m on housing services and low-cost housing will remain a hot topic for the public as well as the private sector well into 2011.

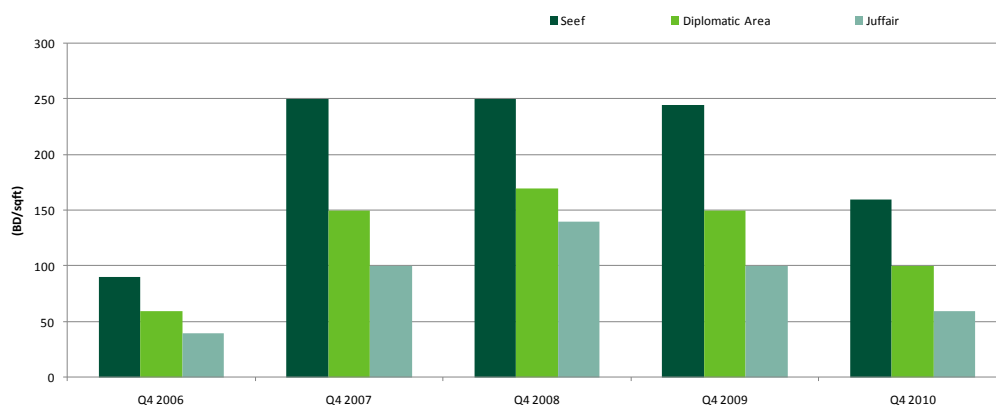
Q4 2010 also saw the surprise victory of Qatar as the hosts for the 2022 FIFA World Cup, bringing Qatar into the spotlight for its pioneering ideology and vision as the first hosts in the Middle East.

Now more than ever, the significance and impact of the long-planned 40 km 'Friendship Bridge' between Qatar and Bahrain is being considered, as the bridge is likely to impact both economies positively. Qatar's efficiency in managing heavy traffic during the World Cup will be greatly increased while Bahrain may benefit from the mass tourist inflow and will have links to both of the region's powerhouse economies via causeways to the east and west, when the causeway is completed in 2017.

Bahrain's improved linkage with Qatar and Saudi Arabia is likely to stimulate business development and investment for firms based in the Kingdom who will, in future, be able to access all three economies with relative ease.

With a shortage of liquidity in the market, short-term land speculation or 'flipping' has diminished with few transactions undertaken in 2010. Significant areas of land have been 'banked' and are unlikely to be offered back to the market until prices have returned significantly, or they have been written down sufficiently by corporates and financial institutions.

Commercial Land Prices in Key Areas, Bahrain – Q4 2007 to Q4 2010



Source: Arabian Homes - prime commercial plots

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		Change from	
Lease Rates		Q4 09	Q4 10
Office		↘	↘
Sale Prices		Q4 09	Q3 10
Office		N/A	N/A

Hot Topics

- During Q4, office space rates and occupancy struggled to keep pace with the volume of new supply entering the market, particularly in Seef District.
- Existing Class B tenants and those occupying apartment conversions are taking the opportunity to consolidate into discounted 'local prime' purpose-built office space.
- There is some evidence of a gradual migration of tenants from the increasingly inaccessible Diplomatic Area to Seef District.
- Landlords are increasingly incentivising tenants through extended rent-free periods and professional property management.

OFFICE SECTOR

As more and more purpose-built office buildings are completed, many occupiers are taking the opportunity to move away from awkward office space in residential buildings or ill-planned commercial buildings with insufficient parking ratios. This trend has resulted in many of the older, less efficient buildings in the 'secondary' category of office space facing fierce competition from newer, 'local prime' properties.

The volume of new office space entering the market during 2010 and further into 2011 is forecast to be significant, and the impacts are already being felt in almost all categories of space, both in terms of occupancy and rate.

In Q4 2010, the market continued to juggle with the dynamics of new space in Seef District, unpopular space in Diplomatic Area and Class A space in the Kingdom's two iconic projects, Bahrain Financial Harbour and World Trade Centre.

Rental rates have fallen sharply in Diplomatic Area for all standards of space due to long-standing chronic parking shortages and access problems. Many tenants are exiting Diplomatic Area in favour of new space in Seef District. This dynamic in Diplomatic Area looks set to continue in the short term and little will change unless these traffic management issues are resolved.

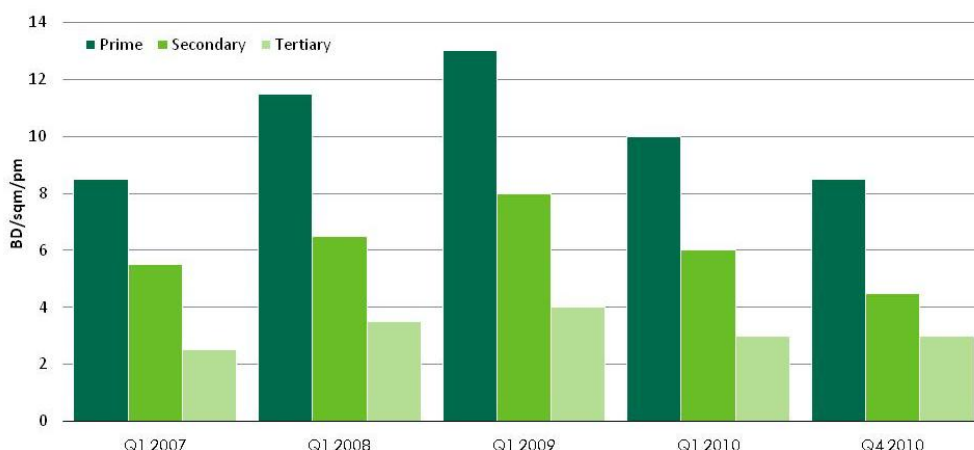
However, during Q4, new space in Seef District outstripped both local demand growth and the transferred demand from Diplomatic Area, with the result that both rental rates and occupancy continued to fall.

Recognising that the office space sector is now a tenant's market, landlords are increasingly incentivising tenants with rent-free periods of up to five months and turning to international property management firms to enhance the appeal of each property.

The Bahrain office market continues to be largely price-sensitive, consequently international quality 'prime' office space buildings such as Bahrain Financial Harbour and the World Trade Centre continue to struggle to achieve full occupancy despite having been on the market for a number of years. With a mere 10% premium over 'local prime' space, occupancy issues continue to loom in both properties.

As the investor market in Bahrain has become more selective, the strata title office sales market has slowed and with the well-documented problems being faced by strata title properties in Dubai, it is unlikely that this particular form of property investment will be resuscitated in the medium term.

Office Lease Rate Movements – (Q1, 2007 to Q4, 2010)



Source: CB Richard Ellis

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Hot Topics

- The apartment sector in general has experienced steeper falls in rents than the villa/compound sector.
- Faced by a depressed rental market and a limited resale market, Q4 saw many investors in masterplanned projects turn into owner-occupiers.
- This will provide a significant boost to these projects which previously faced the prospect of large numbers of vacant units.
- Social and affordable housing continues to be a thorny issue, with the cost of the anticipated PPP solution exceeding the expectations of the Government .
- Private developers continue to struggle to meet 'affordable' demand due to the cost of land which has been inflated by rampant land speculation in recent years.

RESIDENTIAL SECTOR

As housing allowances are curtailed by employers as part of ongoing cost-cutting measures post-global credit crunch, tenants remained extremely price-sensitive in Q4.

In prime residential areas such as Saar/Budaiya, the new supply of rental villas on compounds has taken some of the pressure out of the market with the result that most compounds now have some vacancy and rental rates have continued to 'soften' during 2010.

This is also true of higher density residential areas such as Juffair and Hooraa where supply growth has created modest vacancy levels and downward movement in rental rates in most residential apartment buildings.

Further project completions in Q4 2010 led to a rental rate fall of approximately 8% in Juffair while villa compound rentals in the Saar area fell by around 5%. Rental rates have now fallen back to pre-2008 levels when the market peaked through record employment growth which outstripped supply growth.

The lack of rental market pressure for tenants has important implications for masterplanned projects seeking to sell units. As rental rates grew between 2006 and 2008 and occupancies reached near capacity levels, there were strong drivers for expatriates in particular, to buy their own property.

Buying a house or apartment up to 2008 had the dual comfort of enabling expatriates to gain control of their future housing costs whilst also presenting an attractive investment prospect.

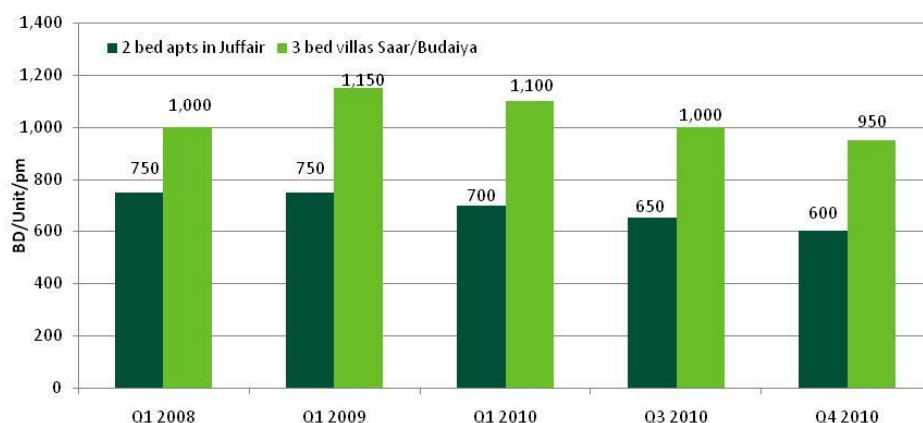
However, this is no longer the case. With housing demand now falling behind supply in the middle and upper income sectors, and large numbers of rental and investment units circulating in the market, the pressure is off, for now.

Allied to high finance costs and modest investor confidence, transactions for luxury properties have dried up and many investors in masterplanned projects have now become owner-occupiers.

Social and affordable housing shortages continue to dominate the press in Bahrain. There is strong political will to resolve this issue at all levels but the waiting list for Government homes continues to grow and continues to outstrip completions.

The attempt to form a Public Private Partnership has not provided the immediate solution hoped for by all parties and negotiations continue. In the meantime, the private sector remains constrained by the high cost of land which is the result of rampant land speculation, and Government assistance in zoning and infrastructure will increasingly be required.

Residential Rental Rates in Key Locations – Bahrain (BD/per month)



Source: CB Richard Ellis

OUTLOOK

Bahrain continues to face significant challenges in 2011 as the Kingdom absorbs the new stock of residential units and office and retail space recently delivered to the market. Despite numerous project postponements there remains a significant delivery 'pipeline' of projects, which in the context of relatively slow employment growth in the wake of the global economic crisis, continues to be a drag on market performance.

However, the wider Bahrain economy continues to perform well, showing strong GDP growth and this, allied with the continuing rebound in oil prices and the sheer scale of neighbouring Qatar's infrastructure projects is thought likely to continue to stimulate investment and business growth throughout all sectors in the Kingdom.

Very few transactions took place in 2009 and 2010 as investors sought 'distressed' sales that simply did not materialise. This is likely to be the case in 2011 as buyers continue to seek bargains while sellers await the return of improved market conditions. However, given the historic volatility of the Middle East's economies, rapid decline and growth are not uncommon and we see recovery, when it does come, being relatively swift.

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