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Saudi King's \$15 Billion Housing Grant Won't End Shortage

March 2 (Bloomberg) -- Saudi King Abdullah's pledge to increase spending on housing by 55 billion riyals (\$15 billion) probably will do little to relieve the country's home shortage unless it's coupled with long-delayed changes in mortgage financing laws.

"This is largely symbolic," said Jarmo Kotilaine, chief economist at National Commercial Bank, Saudi Arabia's largest lender by assets. "We have a significant structural issue that can never be solved through government spending alone."

Saudi Arabia, the world's largest oil exporter, needs 2 million homes by 2014 to keep up with the demands of a population that quadrupled over 40 years, Credit Suisse Group AG estimates. A planned mortgage law aimed at bringing private lenders into the market by creating a clearer set of rules is still being debated a decade after it was proposed.

The 86-year-old monarch last week announced plans to spend about 110 billion riyals on programs aimed at boosting housing, education and social welfare. Governments from Jordan to Yemen have offered concessions to quell public discontent after popular uprisings toppled leaders in Tunisia and Egypt last month and led to protests across the Middle East and North Africa.

Interest-Free Loans

Saudi Arabia's Real Estate Development Fund, which provides interest-free loans, will get 40 billion riyals. Another 15 billion riyals will be added to the housing budget to build affordable homes for state employees.

The money will help the real-estate fund provide an additional 133,000 loans, Saudi finance minister Ibrahim al- Assaf said on Al Arabiya TV Feb. 27. The fund has granted about 600,000 loans since it started in 1975, he said.

Saudi Arabia's Tadawul All Share Index dropped 3.9 percent to its lowest in almost two years. The measure's banking index, which includes 11 stocks, was among the day's worst performers after sliding 6.4 percent. Builders lost 4.6 percent, while property developers fell 4 percent in Riyadh trading.

While the government's plan is a step in the right direction, much more would be achieved by passing laws that allow a private mortgage lending market to thrive, according to Naveed Siddiqui, chief executive officer of Capitas Group International. Capitas, a Saudi Arabia-based holding company focused on Islamic financing, estimates that the mortgage law could spark a lending market worth \$32 billion a year.

"Risk and credit approval measures need to be put in place so money goes to the people who deserve and there is clear-cut monitoring of its effectiveness," he said.

Selective Investments

Kotilaine of Jeddah-based NCB said much of the property investment in recent years has gone toward the upper end of the market or on commercial real estate without addressing the housing needs of the wider population.

Banks have shied away from mortgage lending in Saudi Arabia because of unclear regulation that could lead to lengthy court disputes in cases of default, leaving the country's real estate fund unable to meet the demands of a growing population. Less than 1 percent of all Saudi home purchases are financed by mortgages. That compares with 7 percent in the neighboring United Arab Emirates and 66 percent in the U.S., Deutsche Bank estimated in November.

"To say this is scratching the surface is perhaps too derogatory, but it's very partial solution," Kotilaine said of the increased spending on housing. "The kinds of numbers that we are seeing in Saudi Arabia are going to require a solution of a completely different magnitude."

Cash Transactions

Currently, most buyers pay cash or get interest-free loans from the real-estate fund. Some use money provided by the fund to buy land before tapping into consumer loans, end-of-service pay or pensions to fund homebuilding. Others rely on cash from their families combined with personal loans.

If lending "continues to be done the way it was before, as a direct lending program and non-recourse money giveaway, it will go fast and we'll never know what the true effect of it will be," Siddiqui said.

Predictions that the mortgage law would be passed last year weren't met as the government and the Shura Council, a body that advises the king, worked out differences. The remaining disagreements "should be ironed out soon," Saleh Al-Shoaibi, head of the council's economic affairs and Energy Committee, said by telephone. He said King Abdullah's three-month absence for medical treatment also delayed approval.

"This is not a law you can get out and then start amending later," Al-Shoaibi said. "They want to get it right the first time."

--Editors: Ross Larsen, Andrew Blackman.