Kuwait Real Estate:
Commentary and Analysis

February 2008
Research Highlights:
Examining the trends and developments concerning the real estate sector in Kuwait

MENA Real Estate Team

1. Executive Summary

Kuwait’s real estate sector has experienced significant growth in the last five years, triggered by several structural factors such as economic expansion driven by high oil prices, favorable demographics, and abundant liquidity. Real GDP growth was sustained above 10.0% since 2003, where oil prices grew by 11.3% y-o-y to reach a new high of KD18.8 Bn in 2006. Supported by strong liquidity, total credit facilities granted to the real estate sector has increased at a CAGR of 23.1% over the period 2001-2006. Going forward, we expect rising oil prices and increasing oil production along with government’s diversification program aiming at developing non-oil sectors to sustain GDP growth. Consequently, we expect Kuwait’s real estate and construction sectors to benefit from $8bn worth of private investments and $3bn in government investments over the next five years.

The growth in real estate sector has registered a CAGR of 34.0% for the period from 2002 till 2006. Factors such as a) strong increase in numbers of expatriates; b) young demographic profile; c) increasing disposable incomes; and d) growing private sector participation have supported this growth. Consequently, real estate prices are expected to continue appreciating in the short to medium term across the majority of the segments although this growth in real estate prices in general would be lower, as prices have already increased significantly during the past few years.

Currently, demand is outstripping supply in all aspects of the Kuwait’s real estate sector – Residential, Commercial, Industrial, and Retail. In the private housing sub-segment, a total of 79,894, applications were outstanding and 30,414 individuals were on the waiting list with the Public Authority for Housing and Welfare (PAHW) as of the second half of 2007. On the supply side, according to Ministry of Housing figures, between 1994 and 2005, only 19,000 state private housing units were built. The residential real estate segment will likely face a shortage in supply in the medium term. We expect unmet demand for private housing units to reach approximately 100,000 by 2010.

Similarly, the Istithmari (investment properties) sub-segment also has been witnessing a shortage of units due to the growing influx of expatriates following year 2003, which witnessed the Iraqi war. The growth in demand for private housing units and scarce availability of land in major governorates has been reflected in the prices. Average land price of private housing units in Kuwait grew by 30-35% y-o-y to reach KD550 per sqm in 2007. Furthermore, average Istithmari rentals have expanded at a CAGR of 22.5% over the period 2002-2007, and where in 2006, average Istithmari rentals grew at 9.0% y-o-y to KD2.95 per sqm. We expect growth in Istithmari rentals at moderate levels in the medium term. Going forward, we believe outer city Istithmari properties will provide higher returns compared to inner city areas, as

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well as, high rental growth and lower land value appreciation in outer city areas will lead to compression in cap rates at higher rates when compared to inner city areas.

Rentals for class A office space will increase at lower rates in the medium term (3-4 years) and start decreasing in the long term

In the office segment, Kuwait's strong economic growth has contributed a positive business environment in the country, which has attracted more foreign companies to participate in different sectors of the economy. Due to existing shortage in supply of office space, rents and prices have risen significantly in the office segment. Going forward, we anticipate rentals for class A office space to increase at lower rates in the medium term (3-4 years) and start decreasing in the long term (5 years and above). Further, we expect trends in the outer city office property to mirror those of Istithmari properties, providing higher returns compared to inner city areas.

The retail property is also witnessing growth with the shifting trend towards construction of large malls. Demand for retail space is expected to continue in the short term with many foreign and regional retail brands entering the Kuwait's market in the light of favorable consumer dynamics and regulations. Consequently, we expect retail rentals to witness an upward trend in the short term. As for conventional retail properties, our assessment tends to stay bullish even in the long term.

On the tourism front, Kuwait has been witnessing an increase in the number of tourists driving up hotel occupancy rates. A majority of hotel room supply is expected to come online by the end of 2008 and is bound to create an over-capacity in the market. As a result, we believe that Kuwait may undergo lower occupancy rates and increased pressure on average room rates until the absorption of supply growth.

The industrial segment has benefited from increased activities, primarily in the oil and gas sector. Higher hydrocarbon prices and rich availability of oil reserves has led to the higher expenditure by the government in various industrial infrastructure projects within the oil & gas and energy sector. Furthermore, establishment of FTZs and allowing 100% ownership within the zone is likely is likely to encourage the setting up of new industrial facilities. This, in turn, will boost the demand for industrial properties, leading to increase in prices and rentals of industrial properties, going forward.

Kuwait's real estate sector is expected to sustain the growth On the back of positive economic outlook

Going forward, several structural triggers such as rising expatriates population, growing private sector investments and positive economic outlook, are in place to ensure sustainability of the growth in Kuwait's real estate sector. However, Kuwait's real estate is heavily dependent on the conditions of the economy, and the turbulence in the region. A slump in the economy can evaporate the projected activity in the sector throughout Kuwait. Thus, the positive outlook for Kuwait's real estate sector could be derailed by any unexpected contraction in the country's economy and instability in the region's geopolitical situation.

2. Overview, Commentary, and Analysis

I. Market Performance:

a) Contribution of Construction and Real Estate Sectors to the Economy

Led by high oil price, Kuwait's economy has witnessed significant growth in last five years

Kuwait's economy has experienced significant growth in the last five years, backed by high oil prices and increased oil production levels. Kuwait's oil production has increased by 40% since 2002 to reach in 2007 its full capacity. Furthermore, according to IMF, Kuwait's accumulated reserves from oil are the highest among the GCC countries; it will total 300%-400% of GDP in the next six years. Oil revenues in the last few years have also pushed liquidity in the market up. Money supply, or M2, has been increasing significantly since 2004 where it supply expanded by 21.7% in 2006, as compared to 12.1% and 12.3% in 2004 and 2005, respectively.

Although the real estate sector has grown by 34% from 2002 to 2006, its contribution to Kuwait's GDP declined from 8.4% to 4.4%, as the share of the oil & gas sector increased

Although, the Kuwait's economy is heavily dependent on the oil sector, real estate and construction sectors also play significant roles in the country's economic growth. The real estate sector registered a CAGR of 34.0% for the period from 2002 till 2006. However, growth in both the real estate and construction sectors is not proportional to GDP growth. Abundant liquidity, favorable demographics, economic growth and repatriation of funds have been the major drivers of the boom in real estate sector over the last few years. However, the real estate sector's contribution to GDP decreased to 4.4% in 2006, compared to 8.4% in 2002. Similarly, contribution of the construction sector contracted to 1.6% in 2006 from 2.7% in 2002 (Refer exhibit 1). The combined contribution of the sectors to Kuwait's GDP declined to 6.0% in 2006 from 8.5% and 6.7% in 2004 and 2005, respectively. This decrease can be attributed to the significant increase in the oil & gas sector's share in Kuwait's GDP (55%), due to the steep rise in oil prices in recent years. The growth in Kuwait's real estate and construction sector has come at a cost. Kuwait's inflation rate surged in December 2007 to a record 8.3% compared to 3.9% during the same month of 2006, exacerbated by the steep rise in real estate prices. The cost of housing in Kuwait, which has a 27% weighting in the consumer price index, rose an annual 12.6% in September 2007, compared with 7.1% in August 2007.

Going forward, we expect high oil prices and increasing production to sustain GDP growth. Consequently, we expect Kuwait's economic outlook to remain positive. In addition, Kuwait's diversification program to lower the economy's dependence on oil and gas revenues and its plan of investing $11 Bn over the next five years, further enhances economic outlook. We expect the construction and real estate sectors to continue registering robust growth in Kuwait's non-oil & gas sector. Furthermore, the Central Bank of Kuwait's (CBK) decision to drop the dollar peg in May 2007 and link it to a basket of currencies will enable it to curb inflation. The central bank's move is likely to positively impact the real estate and construction sectors through a stronger Kuwait's Dinar that will make import of construction material cheaper. Added to that, the U.S. is in the midst of a housing market slump, which could result in the Federal Reserve (Fed) slashing interest rates in the medium term. Any rate cut by the Fed in the medium term could lead the Kuwait central bank to do the same, pushing credit off-take higher, thereby benefiting the real estate sector.

Kuwait's economic outlook is expected to remain positive due to high oil prices and growing investments

Exhibit 1: Contribution of real estate sector to GDP (2002-06)

Sector (KD mn)	2002	2003	2004	2005	2006
Mining and Quarrying	4,423.0	5,814.8	7,844.5	12,865.2	16,256.2
Manufacturing excluding refined products	476.7	554.6	660.4	742.7	814.2
Refined Products Industry	430.6	572.4	795.5	970.2	1159.2
Agriculture and Fishing	59.9	64.9	70.9	71.1	74.4
Electricity, Gas and Water	275.3	299.4	306.9	319.1	336.6
Construction	**312.0**	**349.3**	**401.9**	**437.1**	**479.3**
% contribution to GDP (at current price)	**2.7%**	**2.5%**	**2.3%**	**1.8%**	**1.6%**
Trade, Restaurants and Hotels	946.2	1,064.4	1,120.7	1,185.8	1,260.0
Transport, Storage and Communications	590.4	799.9	1,048.0	1,230.7	1,397.4
Financial Institutions	862.7	1,236.6	1,558.6	2,855.4	3,911.1
Real Estate	**969.8**	**1,062.0**	**1,094.8**	**1,208.4**	**1,295.8**
% contribution to GDP (at current price)	**8.4%**	**7.5%**	**6.3%**	**4.9%**	**4.4%**
Business Services	163.7	186.6	227.2	242.3	253.4
Community, Social and Personal Services	2,541.0	2,726.4	2,950.0	3,228.3	3,478.7
Total GDP (at current price)	**11,590.0**	**14,253.5**	**17,516.7**	**24,477.8**	**29,572.8**
% growth	15.2%	23.0%	22.9%	39.7%	20.8%
Total GDP (Real)	**11,945.0**	**13,918.0**	**15,378.2**	**16,910.4**	**18,827.0**
% growth	3.0%	16.5%	10.5%	10.0%	11.3%
	1281.8	1411.3	1496.7	1645.5	1775.1
	11.1%	9.9%	8.5%	6.7%	6.0%

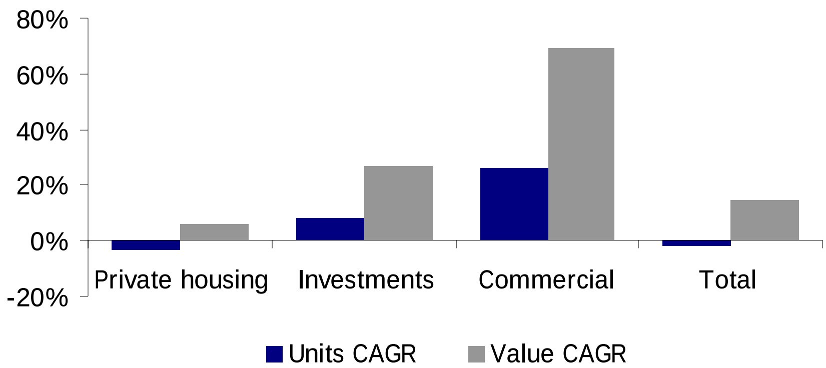
Source: Central Bank of Kuwait

b) Historical and Latest Performance of the Sector

Property sales in value terms increased, at a CAGR of 14.2% over the period 2001-2006

Transaction activity has tremendously surged over the last five years. For the purpose of analysis, the residential segment is divided into: (a) Private Housing (sales of villas and condominiums); and (b) Investment (Istithmari rental properties). The total property sales in value terms increased at a CAGR of 14.2% over the period 2001-2006 to reach KD2,725 Mn in 2006 (Refer exhibit 2). However, the total number of units sold declined at a CAGR of 1.8% over the same period, indicating higher average price realization per unit. The number of units sold in the residential (private housing) segment decreased at a CAGR of 3.4% over the period 2001-2006, while the value of units sold increased at a CAGR of 6.1% over the same period. This indicates a 9.5% increase in average value of units over the period 2001-2006.

Exhibit 2: Property sales CAGR (2001-2006)

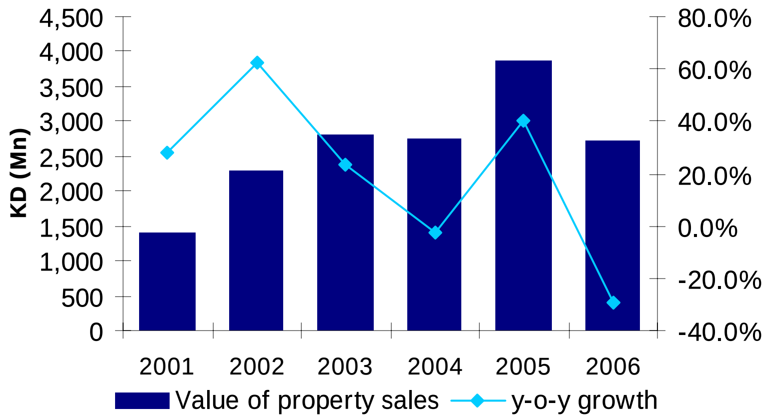


Source: Ministry of Justice

Commercial segment registered the highest CAGR growth during 2001-2006 in terms of both number and value of units sold

In the investment segment (Istithmari rental properties), both the number and value of units sold expanded at a CAGR of 7.8% and 27.1%, respectively, over 2001-2006. The commercial segment registered the highest CAGR growth in terms of both number and value of units sold. While the number of units sold in the commercial segment recorded a CAGR of 69.0%, where the value of units sold posted a CAGR of 25.8% over the period 2001-2006.

Exhibit 3: Total property sales in value terms (2001-2006)



Source: Ministry of Justice

Real estate activity in value terms declined on y-o-y basis during 2006

On a year-on-year (y-o-y) basis, real estate activity in value terms declined across the private housing and investment property segments during 2006 (Refer exhibit 3). The value of property sales in Kuwait's private housing and investment property segments decreased y-o-y by 32.9% and 39.4%, respectively, in 2006. However, the number of units sold increased significantly across all segments in 2006. This indicates that real estate activity increased in the less expensive outer city areas. Units sold in the private housing segment surged 20.2% y-o-y to 8,624 units in 2006. The commercial segment registered the highest y-o-y growth with number of units sold increasing 66.7% in 2006. Similarly, the number of units sold in the investment segment increased 63.8% y-o-y to reach 1,592 units in 2006.

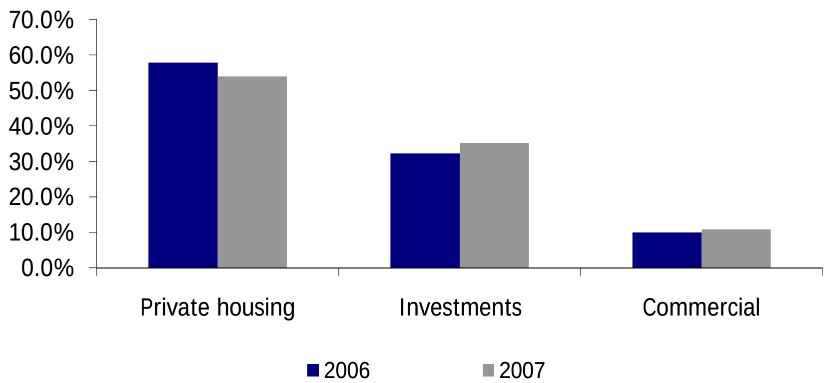
Developments in Real Estate Sector (2007 Vs. 2006)

The first eight months of 2007 saw average real estate sales increase by 67% in value and 41% in number compared with the same period of 2006. Most of the expansion occurred in the investments and commercial sectors. The average price of registered transactions during the eight months rose by 21% for investments and commercial property and 12% for private housing property compared to the same period last year.

The private housing segment's share in terms of value continued to decline during the first eight months of 2007. The segment's share stood at 54.0% during the first eight months of 2007 compared to 57.8% during the corresponding period in 2006 (Refer exhibit 4).

Private housing segment's share in terms of value continued to decline during the first eight months of 2007

Exhibit 4: Segment sales by value as % of total sales (Jan-Aug)



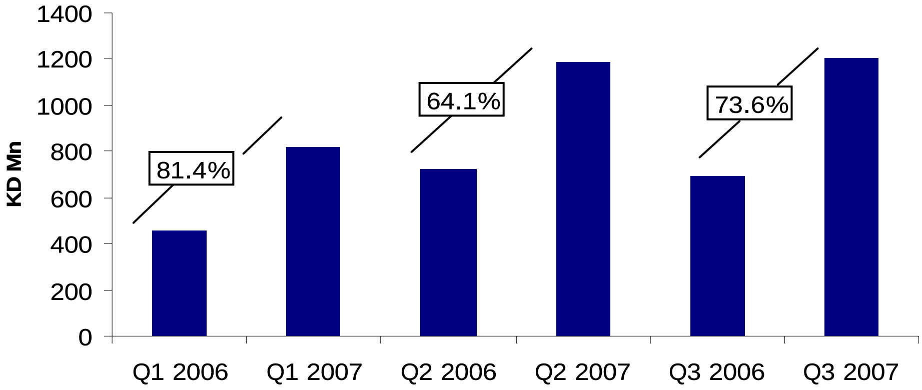
Source: Ministry of Justice

On the other hand, the combined share of the investment and commercial property segments rose to 46% y-o-y during the first eight months of 2007. The investment and commercial property segments continued to witness an upward trend in 2007, led by continued economic expansion and growth in expatriate population driving demand for investment properties.

Real estate sales increased by 72.0% y-o-y and 35.0% y-o-y in terms of value and number of units sold, respectively, during the first nine months of 2007

Activity in the real estate sector rebounded during 2007, led by increase in prices across segments. The value of property sales grew by 81.4% y-o-y during the Q1 2007 and has remained buoyant during Q2 and Q3 2007. The value of property sales rose 64.1% y-o-y in Q2 and 73.6% y-o-y in Q3, respectively (Refer exhibit 5). Total real estate sales increased by 72.0% y-o-y and 35.0% y-o-y in terms of value and number of units sold, respectively, during the first nine months of 2007.

Exhibit 5: Growth in total property sales by value (2006 - 2007)

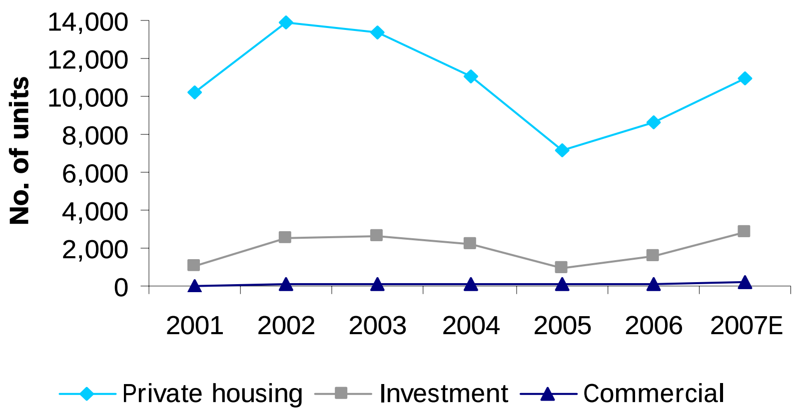


Source: Kuwait Finance House

We have captured the quarterly trend of average real estate sales in terms of value and number of units sold during the last four quarters of 2006 and first three quarters of 2007. Based on this we have forecasted the real estate sales for the fourth quarter and full year 2007. We expect real estate sales to increase by 73.0% y-o-y in terms of value to reach KD4,716 Mn in 2007. On the other hand, total number of units sold is expected to register 16.0% y-o-y growth to reach 12,020 units in 2007.

Exhibit 6: Number of units sold by segment (2001-2007E)

Share of the private housing segment has been declining steadily over the last five years.

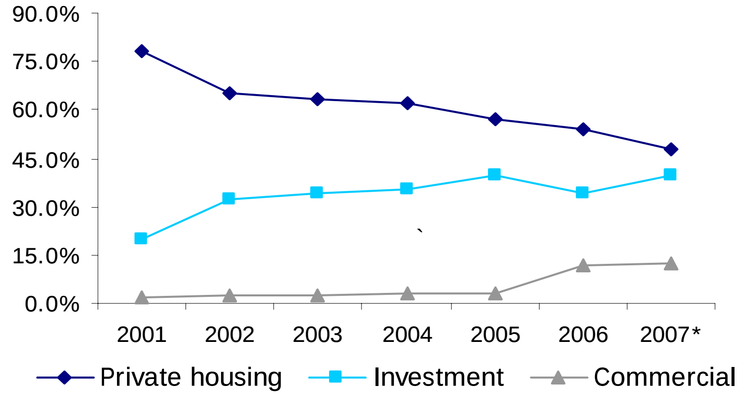


Source: Ministry of Justice, Markaz analysis

Value of private housing sales stood at 47.6% of the total during Q3 2007, compared to 78.4% in 2001

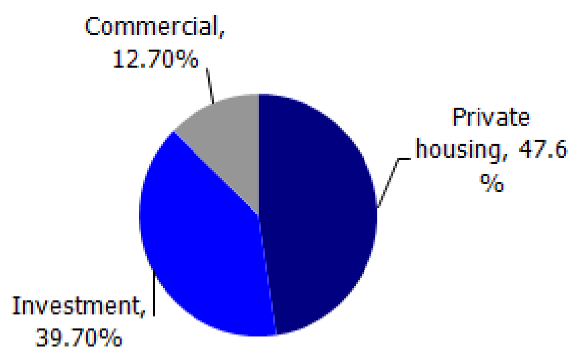
In terms of value of sales by segment, historically, the private housing segment dominated the Kuwait's real estate sector. However, its share has been steadily declining over the last five years. During Q3 2007, the value of private housing sales stood at 47.6% of the total, compared to 78.4% in 2001 (Refer exhibits 7 & 8). On the other hand, shares of the investment property and commercial property segments have been growing steadily. The investment property segment's share increased to 39.7% in Q3 2007 from 20.0% in 2001. This increase can be primarily attributed to the huge influx of expatriates into Kuwait over the same period. Similarly, the Commercial property segment's share surged to 12.7% in Q3 2007 from 1.6% in 2001. This was led by economic expansion and increased consumption as a result of growth in Kuwait's GDP per capita over the same period.

Exhibit 7: Percentage Property Sales by Segment (2001-2007*)



Source: Ministry of Justice, Markaz analysis,* As at Q3 2007

Exhibit 8: Percentage property sales by segment (2007*)



Source: Ministry of Justice Markaz analysis, *As at Q3 2007

II. Municipality Regulations

Relaxation of regulations governing the height of buildings is attracting more developers

The maximum permitted height of a building in Kuwait was 20 floors until the mid 1990s. However, in 2004, the Kuwait municipality changed the law to permit the construction of 30-storey buildings for 1,000 sqm plots and 40-storey ones in downtown areas. Approval of the first 50-storey tower for the Secretariat of Al-Awqaf in 2004 marked the shifting trend towards higher building structures. In 2005, Kuwait Municipality further relaxed the regulations and permitted the construction of buildings with 100 floors in Kuwait City. However, the height of the building should not exceed 400 meters and should have more than

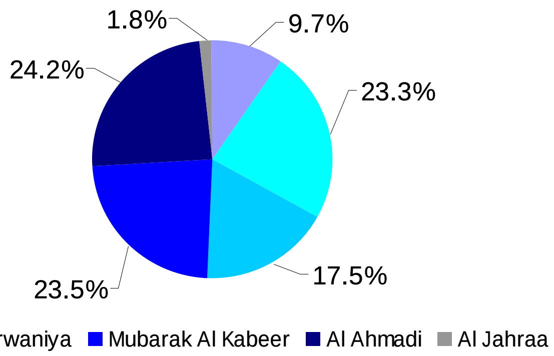
10,000 square meters of area. Relaxations of the regulations governing height of buildings is likely to attract more developers, in favor of building towers as is the trend in several major GCC cities.

Real Estate Activities by Governorate

In terms of number of units sold by governorate, Al Ahmadi, Hawally and Mubarak Al Kabeer dominated the Kuwait's market, together accounting for 71.0% of the total units sold in 2006 (Refer exhibit 9). With respect to the number of private housing units sold, Mubarak Al Kabeer accounted for 28.0% of the market followed by the Al Ahmadi and Hawally governorates at 22.3% and 20.7%, respectively, in 2006.

Al Ahmadi, Hawally and Mubarak Al Kabeer together accounted for 71.0% of the total units sold in 2006

Exhibit 9: Distribution of unit sales across governorates (2006)



Source: Ministry of Justice

Hawally dominated the investment segment accounting for 38.3% of investment units sold in 2006

The governorate of Hawally has dominated the investment segment followed by the Al Ahmadi governorate , accounting for 38.3% and 34.7% of investment units sold, respectively, in 2006 (Refer exhibit 10). Of the total units sold (Total of all three segment) Hawally governorate accounted for 23.3% in 2006. The AL A'SIMA (Capital) governorate accounted for the majority share of commercial sales at 37.2%, followed by Al Ahmadi at 23.4% in 2006. This growth was due to the opening of a number of commercial and entertainment facilities in the governorate.

Kuwait has registered higher cap rates relative to other international countries

Exhibit 10: Property unit sales by governorates (2006)

Governorate	Private housing	Investment	Commercial		
Capital	834	112	54	1000	
% of total	9.7%	7.0%	37.2%		9.7%
Hawally	1,788	609	20	2417	
% of total	20.7%	38.3%	13.8%		23.3%
Farwaniya	1,497	291	26	1814	
% of total	17.4%	18.3%	17.9%		17.5%
Mubarak Al Kabeer	2,419	17	3	2439	
% of total	28.0%	1.1%	2.1%		23.5%
Al Ahmadi	1,924	552	34	2510	
% of total	22.3%	34.7%	23.4%		24.2%
Al Jahraa	162	11	8	181	
% of total	1.9%	0.7%	5.5%		1.7%
Total Units	**8,624**	**1,592**	**145**	10,361	

Source: Ministry of Justice

III. Cap Rate Trend and Analysis

Global real estate markets have provided attractive returns during the last few years. Consequently, the sector has been experiencing increasing liquidity, leading to the trend towards cap rate convergence. Globally, cap rates have followed a decreasing trend over the past five years. However, the cap rate compression in Kuwait was limited due to buoyant stock markets and relatively illiquid real estate sector. Current cap rates in Kuwait are significantly higher than those in other international markets (Refer exhibit 11).

Exhibit 11: Cap rates across different countries/regions

Countries/regions	Cap rates	10-year treasury rates	Spread
United States	6.5%	4.5%	2.0%
United Kingdom	4.2%	3.9%	0.3%
Western Europe	4.6%	4.8%	-0.2%
Japan	4.5%	1.6%	2.9%
India	9.5%	7.5%	2.0%
Kuwait*	9.5%	5.0%	4.5%

Source: Real Capita Analytics, ING Real Estate, Markaz Analysis; * Kuwait's 10 year treasury rate is estimated by adding a 50 basis point over US Treasury bill

Cap rates are expected to compress by approximately 100-150 bps over the next five years

The stock market in Kuwait has remained buoyant between 2001 and 2006. However, since 2006, the market has undergone significant correction and volatility has increased. Consequently, investors are increasingly looking towards other investment assets, such as the real estate sector. The market for income generating real estate properties is becoming increasingly lucrative. As previously mentioned, total property sales in value terms has increased at a CAGR of 14.2% over the period 2001-2006.

We believe that the increasing volatility in the stock market is likely to result in higher asset allocation to the real estate sector in Kuwait. This could lead to increased liquidity and attract more investors to the sector. In the short-term, we expect a price correction as they have already appreciated significantly in the recent past. However as the price picks up in the medium to long term, we expect cap rates in Kuwait to compress by approximately 100-150 bps over the next five years. This would allow investors to record significant capital gains.

IV. Construction Activities in Kuwait

Investment permits issued in 2006 declined 40.2% y-o-y due to an increase in interest rates and the correction of the stock market in 2006.

New building permits, another indicator of real estate and construction sector activity, increased at a CAGR of 5.3% over the period 2000-2005. However, the total number of new construction permits issued in 2006 declined 13.2% y-o-y to 3,391 (Refer exhibit 12). This was mainly due to the fewer number of private housing permits issued during 2006. The investment segment registered the highest growth in construction permits issued, registering a CAGR of 34.8% over the period 2000-2006. However, the number of investment permits issued reported a significant 40.2% y-o-y decline in 2006. This decrease could be primarily attributed to an increase in interest rates and the correction of the stock market in 2006.

Exhibit 12: New construction permits 2000-2006

	2000	2001	2002	2003	2004	2005	2006
Commercial	15	25	46	178	55	52	87
Investment	71	220	524	712	912	712	426
Industrial	45	63	103	198	62	85	140
Private housing	2,882	2,926	4,887	4,518	2,618	3,058	2,738
Total	3,013	3,234	5,560	5,606	3,647	3,907	3,391

Source: Kuwait Ministry of Planning

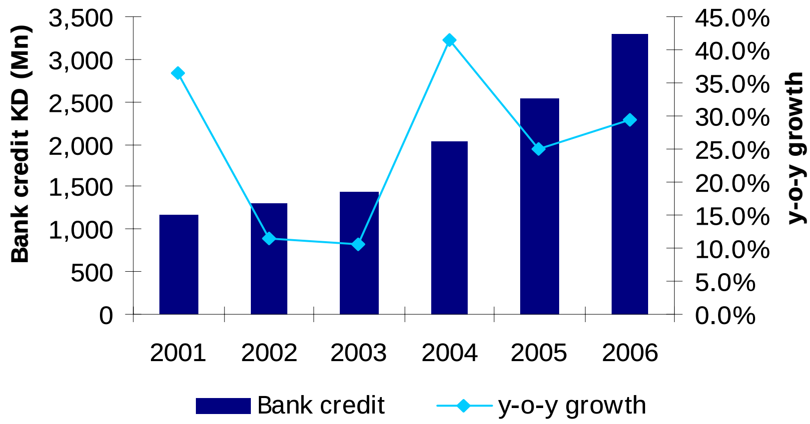
New private housing construction permits issued declined 10.5% y-o-y in 2006. On the other hand, new commercial permits grew significantly by 67.3% y-o-y to 87 in 2006, indicating the buoyant activity in the commercial segment of Kuwait's real estate sector.

V. Financing

a) Commercial Bank Credit Facilities to Real Estate Sector in Kuwait

Increased liquidity and steep demand in the real estate sector have ensured high credit growth rates in the last five years. Total credit facilities granted to the real estate sector has increased at a CAGR of 23.1% over the period 2001-2006. During 2006, credit facilities extended to the real estate sector grew 29.5% y-o-y to KD3,288 Mn (Refer exhibit 13). This accounted for 22.0% of the total bank credit extended in 2006, compared to 19.3% in 2001. The construction sector also saw high credit growth rates over the period 2001-2006. Credit to the construction sector increased at a CAGR of 24.6% over the period 2001-2006 to reach KD1,069 Mn. Consequently, the share of construction sector to total bank credit increased to 7.2% in 2006 from 5.9% in 2001. Furthermore, credit facilities to the retail segment (which includes residential loans) also recorded a CAGR of 24.4% over the period 2001-2006, indicating strong demand in the Kuwait's residential segment.

Exhibit 13: Bank credit to real estate sector (2001-2006)



Source: Central Bank of Kuwait

b) Islamic Financing

Islamic financing positively evolved as a popular mean for real estate investment and financing

Islamic financing involves financing in accordance with Islamic law (Sharia). Islamic financing has emerged as one of the popular means of financing real estate sector in Kuwait. This is primarily due to its relatively simple structure and other inherent benefits such as potential for securitization. Islamic financing has benefited Kuwait's real estate sector, given the flexibility that it offers. The number of Investment companies operating in accordance with the provisions of Islamic sharia in Kuwait had reached 33, managing assets over KD5 Bn in the first quarter of 2007. Various modes of Islamic financing and investment structures have been developed, benefiting Kuwait's real estate sector.

VI. Drivers of Real Estate and Construction Sector

Favorable population demographics will likely drive demand for new housing units

Demand Driver	Signal	Justification
Population and demographics	Positive	Kuwait exhibited strong population growth over the past five years with a CAGR of 6.4% up to 2006. According to the UN's population division, Kuwait's population is expected to

			grow at a CAGR of 2.6% over the next five years, compared to 2.1% for the Middle East (Refer exhibit 14), thus sustaining housing demand, going forward. Furthermore, Kuwait has a young population—approximately 64% is below the age of 35 (Refer appendix 1). Hence, we believe that the percentage of population buying houses will increase, as Kuwait's young population will grow older and move into homes of their own.
Growing employment in Kuwait has been attracting inflow of expatriates and driving up demand for housing	Employment growth and influx of expatriates	Positive	Expatriates account for approximately 68% of Kuwait's total population. Influx of expatriates into Kuwait has grown significantly since 2001. In 2006, the expatriate population surged to 2.16 Mn individuals, representing 8.0% growth over the previous year. Furthermore, employment in Kuwait exhibited a CAGR of 9.5% over the past five years (Refer appendix 2). This growth in employment in Kuwait has boosted the demand for housing and thus for investment properties.
	Renewed confidence and political stability	Positive	We expect the political scenario in Kuwait to remain stable, with the Emir Sheikh Sabah retaining the ultimate executive authority. A stable political framework will uphold investor sentiment and increase foreign investment in Kuwait's real estate sector.
	Growing private sector participation and liquidity	Positive	Government has been encouraging private sector participation to cater to the strong demand and growing infrastructure development needs of Kuwait. The private sector is expected to invest approximately $8 Bn in Kuwait's construction sector over the next five years. This coupled with increasing liquidity due to high oil prices are likely to fuel investment within the real estate and construction sectors.
Mega projects worth $232 Bn are planned for the next five years	Increasing number of mega projects	Positive	Approximately $232 Bn worth of mega projects are planned to be executed in Kuwait over the next five years. These projects will span different sectors, including construction, infrastructure, oil and gas, and industry. Mega projects are expected to create more jobs, both temporary and permanent. This, in turn, could attract more expatriates into the country, propelling demand in the real estate sector.

Expected cut in discount rate in medium term could boost credit off-take

Political standoff between government and members of parliament could create an unfavorable environment for investors

Interest rate environment	Positive	Interest rates in Kuwait closely follow those in the U.S. Since July 2006, Central Bank Of Kuwait (CBK) has maintained its discount rate at 6.25%. However, the central bank cut its repurchase rate by 75 basis points to 4.5% in September 2007. This made yields from income generating real estate properties more attractive than bank deposits. Going forward, we expect CBK to maintain its discount rates in the short-term, lending stability to the market. However, we believe the U.S., in the wake of a crunch in the housing market could further slash interest rates in the medium term. The Kuwait central bank could also cut rates in the medium term, which will push credit off-take higher, benefiting the country's real estate sector.
High per capita income	Positive	Kuwait is one of the wealthiest countries in the world. Per capita GDP increased 8.0% y-o-y to reach $28,100 compared to an average per capita GDP of $17,425 for the entire GCC region in 2006. We believe that Kuwait will be able to sustain per capita income growth, given the expectations of oil prices remaining firm. This is likely to fuel the demand for high-end housing in Kuwait.
High level of land prices	Negative	Average residential price in Kuwait grew by 9.3% y-o-y to KD277 per sqm in 2006. The residential land prices continued to witness upward trend in 2007, growing by more than 30-35%. High land prices curbs development as it negatively impacts demand and renders new projects financially unviable.
Political standoff	Negative	Recently, Kuwait has been witnessing a political standoff between the government and members of parliament (MP). The MPs have been opposing the new government over allegations of misuse of power. This could create an unfavorable environment for investors.

Slow reforms of existing laws and regulations	Negative	In order to enhance the role of private sector in the real estate and construction sectors, Government has been considering the use of B.O.T (Build-Operate-Transfer) system. This system allows private sector companies to develop and invest in plots that are owned by the government. However, B.O.T. regulation has been under deliberation for a long time and is yet to be ratified. These delays and half-hearted attempts by the government are limiting private sector participation in development projects.
Expected shortage of power and water and slow development of infrastructure	Negative	Kuwait is expected to face acute shortages of power and water, going forward. Kuwait has five power stations which produce around 9,100 megawatts for the national grid, while consumption has been rising by 20% annually. This coupled with slow development of infrastructure, such as ports and airports, could act as a hindrance to expansion of industrial activities and the setting up of new residential communities, going forward.
Instability in the regional Geopolitical scene	Negative	Rising conflict between Iran and US over Iran's nuclear policies and Iraq's current turmoil could negatively impact the investor's confidence in the GCC region, including Kuwait.

Instability in the regional geopolitical scene could negatively impact the investor's confidence

Exhibit 14: Kuwait population (2001-2006)

Year	2001	2002	2003	2004	2005	2006
Kuwait population (000's)	870	898	928	956	992	1,023
% growth	3.3%	3.2%	3.3%	3.0%	3.8%	3.1%
Expatriate population (000's)	1,439	1,522	1,619	1,797	1,999	2,160
% growth	4.7%	5.8%	6.4%	11.0%	11.2%	8.1%
Total (000's)	2,309	2,420	2,547	2,753	2,991	3,183
% growth	4.1%	4.8%	5.2%	8.1%	8.6%	6.4%

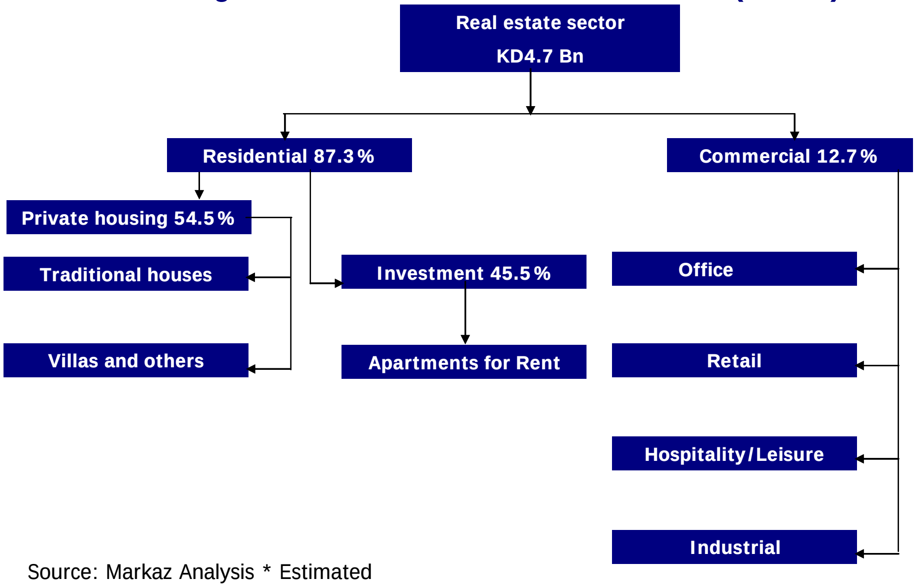
Source: Ministry of planning/UN population division

3. Components of the real estate sector in Kuwait

Structure of Real Estate Sector

Exhibit 15: Segments of real estate sector in Kuwait (2007*)

Residential market accounts for 87.3% of the total real estate market in Kuwait



Source: Markaz Analysis * Estimated

The real estate sector in Kuwait can be broadly classified into: (a) Residential and (b) Commercial. Residential market dominates the Kuwait's real estate sector accounting for 87.3% of the total market. Kuwait's residential market can be further classified in to private housing and Istithmari (investment properties). While, private housing market accounts for 54.5% of the total residential market, Istithmari (investment sub-segment) forms 45.5% of the market. Commercial real estate market in Kuwait consists of office, retail, hospitality/leisure and industrial property market.

I. Residential segment:

Size of private housing segment is estimated at KD2.2 Bn

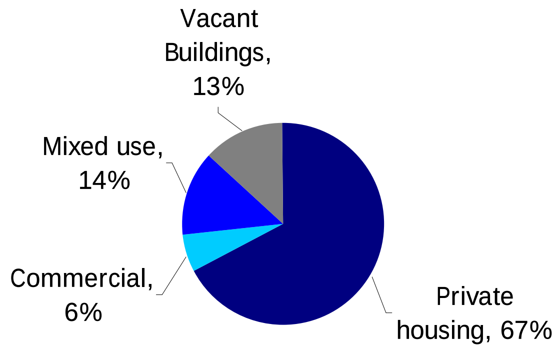
The size of Kuwait's private housing market is estimated at approximately KD2.2 Bn in 2007. The private housing segment has been the most important segment of the real estate sector in Kuwait. As mentioned above, although the private housing segment's share has been declining steadily since the last five years, it still accounts for 47.6% of the value of total real estate sales. Furthermore, it accounts for 67% of the total building mix in Kuwait (Refer exhibit 16). The private housing segment primarily comprises the freehold villas and condominiums. Since expatriates are not allowed to own residential properties in Kuwait, the freehold market is exclusively dominated by Kuwait's nationals. The government sponsored private housing development in Kuwait primarily deals with providing housing to Kuwait's nationals under its "housing for Kuwait's nationals" program. The program is administered through Public Authority for Housing Welfare (PAHW), the largest real estate development entity in Kuwait. It is primarily engaged in the distribution of housing units and formulation and implementation of national housing policies in Kuwait. However, with growing demand for housing units in Kuwait, government has been encouraging private sector participation in the sector (Refer role of private sector section).

Rental market is dominated by expatriates

The rental market in Kuwait is mainly in the form of residential Istithmari (investment properties) and is dominated by expatriates. The rental market is concentrated in the inner city areas such as Bneid Al-Gar, Sha'ab, Salmiya, Sharq and Hawally. However, the rental market in

Kuwait has been witnessing a major shift towards outer city areas such as Fahaheel, Jahra, Farwanieh, Kheitan, Mahboola, and Mangaf. This is primarily due to the increasing demand for rented units in these areas from the expatriate population.

Exhibit 16: Building mix in Kuwait (2006)



Source: Ministry of Planning

a) Private housing sub-segment

On an average 7,000 applicants per year have been added with PAHW

The demand for private housing properties in Kuwait has been witnessing a significant growth in the last few years while supply has failed to keep pace. Consequently, the demand/supply dynamics in the private housing segment indicate an undersupply situation. Demand has been fuelled by increasing population. According to PAHW, a total of 79,894 applications were outstanding, with 30,414 individuals on the waiting list as of the second half of 2007. On average, around 7,000 applicants per year have been added over the period 2000-2006. On the supply side, according to Ministry of Housing figures, between 1994 and 2005 only 19,000 state private housing units were built. Furthermore, the waiting list rate with PAHW increased to 81.7% in 2006, compared to 33.5% and 47.8% in 2004 and 2005, respectively.

Demand for private housing units is expected to reach 100,000 units by 2010

Kuwait's residential private housing market would continue to experience an undersupply situation in the medium term. We expect demand for private housing units to reach approximately 100,000 in 2010. On the other hand, according to ministry of Public Works, over 70,000 units are expected to enter the market in the medium-term. In spite of this, the private housing market in Kuwait would continue to experience a shortfall in the medium term due to pile up of unmet demand over the last few years. We believe that the majority of the future demand in residential segment will be concentrated towards low and middle income Istithmari (rental apartments) in the outer city areas. This is primarily due to expected growth in expatriate population.

Activities in the private housing sub-segment

Average private housing prices in Kuwait increased at a CAGR of 24.0% between 2001-2007

The number of units sold in the private housing sub-segment declined at a CAGR of 3.4% over the period 2001-2006. However, value of units sold increased at a CAGR of 6.1% over the same period. This indicates a 9.5% increase in average value of units over the period 2001-2006. Real estate activities in the private housing segment strengthened during the first nine months of 2007, led by continued economic growth. The value and number of units sold in the private housing segment increased 50.2% and 32.8%, respectively, during the first nine months of 2007, compared to the same period of 2006. In terms of number of units sold by governorate, Mubarak Al Kabeer dominates the private housing segment with 28.0% followed by Al Ahmadi with 22.3% of the total units sold in 2006.

Bayan registered the highest growth of 30% in Q3 2007 within the Hawally governorate

Prices in private housing sub-segment

The growth in demand for private housing units along the scarce availability of land in major governorates has been reflected in the prices. Average private housing price in Kuwait grew at a CAGR of 24.0% between 2001-2007. The private housing prices continued to witness upward trend in 2007 averaging KD 550 per sqm, growing by more than 30-35% y-o-y in 2007. During Q3 07, average private housing land prices increased by 12.7% over Q2 07.The Capital governorate registered an average rate of KD 700 per sqm in 3Q 07. Rates in the Shuwaikh area and Abdulla Al-Salem suburb at KD1,050-1,100 per sqm, continued to be the highest in the Capital governorate. Average private housing land price in the Farwaniya Governorate increased 22.0% to KD366 per sqm in Q3 2007.In the Hawally Governorate, land price per sqm grew by 22.2% in Q3 2007 over Q2 2007. Average private housing land rates touched KD363 per sqm in the Ahmadi governorate; within the governorate, the Kheiran residential area recorded the highest increase in growth rate of 74.2% in Q3 2007 to KD144 per sqm. The Jahra governorate registered an average of KD268 per sqm in Q3 2007. The Mubarak Al-Kabir governorate registered an average rate of KD495 per sqm in Q3 2007. Within the Mubarak Al-Kabir governorate, the Al Messilah area registered the highest growth of 35.3% in Q3 2007 (Refer Exhibit 17).

Exhibit 17: Private housing land prices across Governorates

Area	Private housing Land Prices (Average Q1 & Q2 2007 (KD/Sqm))	Private housing Land Prices Q3 2007 (KD/Sqm)
Capital Governorate	593.0	700.0
Shuwaikh Residential	745.0	1050.0
Suburb of Abdulla Al-Salem	900.0	1100.0
Farwaniya Governorate	292.0	366.0
Kheitan	256.7	334.0
Jaleeb Al-Shoyoukh	340.0	527.0
Hawalli Governorate	525.5	643.0
Bayan	380.0	420.0
Al Sha'ab	600.0	675.0
Al Rumeithiyah	360.0	367.0
Ahmadi Governorate	271.0	363.0
Al Kheiran	83.0	144.0
Jahra Governorate	256.0	268.0
Al-Qasir	163.3	170.0
al waha	266.7	272.0
Mubarak Al-Kabir Governoı	406.0	495.0
Al Qurain	281.0	294.0
Al Messilah	378.2	575.0

Source: Kuwait Finance House

Average price per private housing unit also followed an increasing trend, recording a CAGR of 4.3% over the period 2003-2006. Average private housing price per unit increased from KD152,470 during 2003 to KD172,980 in 2006.

b) Istithmari (Apartment) sub-segment

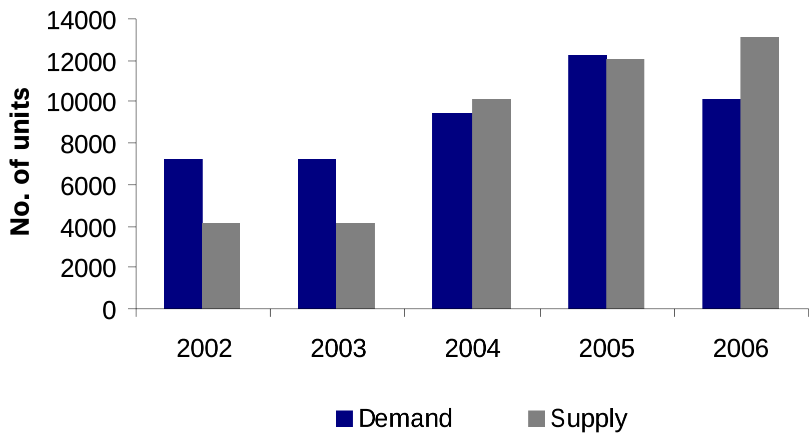
Rapid growth in population and significant influx of expatriates into Kuwait has led to the shortage of quality Istithmari space. The expatriate population in Kuwait has increased significantly at a CAGR of 8.5% over the period 2001-2006. Among the Istithmari, middle and low quality Istithmari units have witnessed more demand. Majority of the high quality Istithmari are occupied by expatriates occupying professional and high level managerial positions. With the growth in

Growth in expatriate population has led to the shortage of quality space for Istithmari

expatriate population and existing expatriate population shifting to outer city areas, high-rise Istithmari have also become an important segment of Kuwait's Istithmari sub-segment.

Demand for Istithmari units in Kuwait has been increasing since 2002. On the other hand, supply of new Istithmari was limited and did not meet demand (Refer exhibit 18). However, with accelerated construction activities, 2006 witnessed a slight oversupply situation. The demand for new Istithmari was approximately 10,125 units, while supply stood at 13,100. Majority of the supply was absorbed due to the pile-up of unmet demand over the period 2002-2005. We expect Istithmari supply to increase over the next two-three years. In addition, increasing private sector participation will further boost new developments in the Istithmari sub-segment. At the same time, we expect these Istithmari supplies will be absorbed by the expanding expatriate population.

Exhibit 18: Istithmari demand-supply 2002-2006



Source: Public Authority for Civil Information

Average Istithmari rentals have recorded a CAGR of 22.5% over 2002-2007

Istithmari rentals

The scenario of demand outstripping supply over the last five years has pushed rentals higher. Average Istithmari rentals have gone up at a CAGR of 22.5% over the period 2002-2007. In 2006, Istithmari rentals continued to rise, albeit at a lower rate. This was primarily due to new supply in Istithmari buildings, especially in the Salmiya, Hawally, Khaitan and Farwania regions. In 2006, average Istithmari rentals grew at 9.0% y-o-y to KD2.95 per sqm. Majority of the governorates continued to witness increasing rentals in 2007. Bneed Al Gaar and Hawally witnessed the highest y-o-y increases in rentals at 9.1% and 9.6%, respectively, in 2007. Salmiya and Messilah reported the lowest y-o-y growth of 3.0% and 1.9%, respectively, in 2007 (Refer exhibit 19).

Exhibit 19: Average Istithmari rentals 2006-2007 (KD/sqm)

Area	2006	2007*	% change
Messilah	2.70	2.75	1.9%
Bneid Al-Gaar	3.67	4.00	9.1%
Al Jabriya	3.20	3.40	6.3%
Salmiya	3.30	3.40	3.0%
Hawalli	2.97	3.25	9.6%
Fahaheel	2.80	2.80	0.0%
Jahra	2.50	2.60	4.0%

Source: Kuwait International Bank, As at the end of Q3 07

Outlook in the Istithmari sub-segment

We expect the majority of the Istithmari supply to enter the market over the next two-three years. This, will keep the growth in rentals at moderate levels in the medium term. However, because of the time lag which is involved before new supply comes to the market, rentals are likely to increase at higher rates in the long term. We expect operating expenses to grow in line with inflation rate of 2%-3%. Considering that the rentals are likely to grow only at a moderate rate in the medium term, we foresee net operating income to grow at a declining rate over the next two-three years. Going forward, we believe that Istithmari properties in the outer city areas of Kuwait (such as Fahaheel, Jahra, Salmiya, Mahboola, and Mangaf), offer greater potential for returns. This is primarily due to:

I) High population and rental growth

High Population growth in the outer city areas is one of the major factors that would drive the demand for Istithmari units, going forward. Population growth in outer city areas has been higher compared to inner city areas. Cumulative population growth between 1995 and 2005 was 47% in the outer city areas compared to 30% in the inner city areas. We believe that outer city locations hold a high potential for population growth. Furthermore, the growth in Istithmari rentals has been highest in the outer city areas. This is evident from the fact that the cumulative rent growth over the past 10 years in the outer city areas stood at 39% compared to 25% in the inner cities (Refer exhibit 20). In addition, the upcoming mega projects, especially in the oil and gas sector, are expected to generate additional employment around these areas. This is expected to lend a further boost to Istithmari demand in these regions.

Exhibit 20: 10 year Istithmari rent growth in outer cities

Area	10 year growth
Jleeb Al Shuyoukh	73.3%
Mangaf	41.2%
Farwaniya	40.0%
Kheitan	38.5%
Fahaheel	31.6%

Source: Kuwait International Bank

II) Low land price appreciation and high cap rates

The outer city areas have been witnessing lower growth in land value appreciation compared to inner cities. Cumulative growth in (Istithmari) land values in inner city areas has exceeded 216% over the past 10 years compared to 167% for outer land areas. Due to the high rental growth and lower land value appreciation, Istithmari cap rates are higher in outer city locations, compared to inner city ones. The spread between cap rates in outer city locations and inner city locations is between 100 and 200 basis points (Refer exhibit 21). We expect outer city Istithmari properties to provide stable return, going forward. This is primarily led by higher potential for rental growth and attractive land valuations compared to inner city areas. This, in turn, would drive cap rates downwards in the coming years to levels close to those of inner city areas.

Exhibit 21: Cap Rates in inner city and outer city Areas

Inner City	Cap rate	Outer City	Cap rate
Kuwait	8.0%	Fahaheel	10.0%
Sharq	8.5%	Jleeb Al Shuyoukh	10.5%
Bneid Al Gar	8.5%	Jahra	10.5%
Salmiya	9.0%	Mahboola	11.0%
Hawalli	9.5%	Mangaf	11.0%

Source: Al-Jal Real Estate

Summary of Istithmari sub-segment

We expect moderate growth in Istithmari properties in medium term

Istithmari segment in Kuwait has been witnessing strong demand in the last five years primarily led by influx of expatriates, in the light of economic boom the country is experiencing. The scenario of demand outstripping supply over the last five years has pushed rentals higher. Average Istithmari rentals have gone up at a CAGR of 22.5% over the period 2002-2007. However, with accelerated construction activities, 2006 witnessed a slight oversupply situation. Going forward, majority of the Istithmari supply is expected to enter the market over the next two-three years. This, in our view, will keep the growth in rentals at moderate levels in the medium term. Furthermore, Istithmari properties in the outer city areas of Kuwait (such as Fahaheel, Jahra, Salmiya, Mahboola, and Mangaf offers greater potential in our view. This is driven by the fact that outer city areas have been witnessing lower growth in land value appreciation compared to inner cities. Consequently, we expect investors to benefit from cap rate compression in the outer city areas.

c) Government financing in residential segment (Savings & Credit Bank (SCB))

SCB loans approved increased 16.1% y-o-y during first nine months of 2007

Though, commercial banks' participation in the real estate finance is fairly high in Kuwait, government also plays an important role by providing subsidized real estate credit. For instance, the Kuwait government established Savings & Credit Bank (SCB) in 1965, to facilitate subsidized real estate and social credit to eligible citizens. SCB provides loans for buying, constructing and/or renovating a house (both government and private). The number of approved SCB loans declined by 14.7% in 2006 over 2003. This was due to a 38.6% fall in loans for the construction of new homes over the same period. However, the number of SCB loans approved during the first nine months of 2007 increased 16.1% over the same period of 2006, as loans for the construction of new homes increased 35.1% y-o-y during the period (Refer exhibit 22). In terms of value, total SCB loans have declined by 24.2% to KD214.8 Mn in 2006 compared to 2003. The total value of SCB loans disbursed during the first nine month of 2007 decreased 5.6% y-o-y to reach KD142.4 Mn. This was led by a 17.4% y-o-y decline in the value of loans disbursed for the construction of new homes over the same period.

Exhibit 22: Saving and Credit Bank disbursals (2003-2007*)

Number of Approved loans	2003	2004	2005	2006	2007*
New Construction	2796	2628	2652	1716	1447
Purchase of Existing Homes	1632	1320	1116	1404	1098
Additions & Renovations	1128	888	900	1620	1006
Total	5556	4836	4668	4740	3551
Value of Disbursed Loans (Mn KD)	2003	2004	2005	2006	2007*
New Construction	174.0	169.2	166.8	134.4	79.8
Purchase of Existing Homes	91.2	76.8	58.8	60	46.8
Additions & Renovations	18.0	19.2	16.8	20.4	15.8
Total	283.2	265.2	242.4	214.8	142.4

Source: National Bank of Kuwait, *As of September 2007

In 2005, SCB changed its regulation to allow eligible citizens to purchase a 280 sqm plot, compared to the earlier 360 sqm. This is likely to boost the demand for SCB housing loans and positively impact the residential market.

d) Regulations governing investments in residential sector

Currently, only Kuwait's citizens are allowed to own residential property in the country. However, the government is considering allowing non-Kuwait'ss to invest and own freehold residential property. Government has indicated its plans to change regulations governing foreign ownership in the designated residential areas. This is primarily due to the growing expatriate population in Kuwait who desire to own residential property in the country. In this regard, a law has been under deliberation which would allow expatriates to own up to 1,000 sqm of residential property with no right to re-sale. Furthermore, the deal would require a) approval of the ministerial cabinet; and b) a Kuwait's national to hold some stake in the property.

II Commercial segment

A. Office

Demand for office space is on the rise since the Iraqi war

The office market in Kuwait has been experiencing significant increase in demand for quality space since the Iraq war in 2003. Furthermore, strong growth of the Kuwait economy and improved performance of the corporate sector, led to the formation of several new companies and the expansion of existing ones. In addition, opening of the banking sector saw the entry of many foreign and regional banks (such as HSBC Bank, BNP Paribas, Citibank, and National Bank of Abu Dhabi). Consequently, Kuwait is experiencing strong demand for office space.

It is estimated that a total of 70,640 sqm of prime office space came on stream between 2003 and 2006. All of this office space was absorbed, indicating an annual absorption rate in excess of 23,000 sqm. Supply of office space has failed to keep pace with growing demand, leading to the shortage of office space in Kuwait. Currently, office occupancy rates in Kuwait are at all times high approaching the 100% level.

The office market in Kuwait is characterized by lack of prime quality space. Prime buildings are generally reserved for the public sector while large domestic corporations such as banks, occupy their own office space.

Status of office space in Kuwait

For the purpose of analysis, the office market in Kuwait can be divided into the following areas or sub-markets: (a) Kuwait city; (b) Salmiya and Hawally; (c) Shuwaikh; (d) Al-Rai; (e) Ahmadi; and (f) Free Trade Zone and other outer areas such as Farwaniya, Kheitan, Jleeb Al shouyuokh, and Fahaheel.

Companies in the oil and gas sector prefer offices in the Ahmadi region

These areas cover majority of the office space in Kuwait. It is observed that companies in the oil and gas sector prefer to have their office and commercial operations in the Ahmadi region. While investment and financial service based companies prefer Kuwait city, Engineering and Automobiles based companies prefer Shuwaikh and Al- Rai. Retail and service sector companies opt for Salmiya. In addition, local small companies prefer to rent office space close to their customers and clients in areas such as Farwaniya, Kheitan, Jleeb Al shuyuokh, and Fahaheel.

A favorable change in regulations by Kuwait Municipality is encouraging the construction of high rise office towers in Kuwait City

Total office space in Kuwait was estimated at 819,775 sqm in 2006. Majority of this office space was located in Kuwait city. The current supply of the office space in Kuwait is characterized by number of towers, buildings and office space in shopping complexes. In 2005, Kuwait Municipality allowed the height of new buildings in Kuwait city to be increased to 100 floors from 40 floors, provided the height did not exceed 400 meters conditional on a certain minimum for the area of the land. The change in regulation has resulted in the construction of a number of high rise office towers in Kuwait city. According to Colliers International, approximately 500,000 sqm of office space is in the construction/planning phase and expected to go live by 2010. Majority of this office space will be ready for occupation in 2009, most in line with international standards. Consequently, we expect the office market in Kuwait to witness an oversupply situation in the medium term (3-4 years).

Prices and rentals

Due to the shortage in supply of office space, rents and prices have risen significantly in the office segment. The average office land rates in Kuwait expanded at a CAGR of 17% over the period 2001-2006. Office land rates continued to soar during the second and third quarter of 2007, primarily due to increasing demand from local companies (Refer exhibit 23).

Exhibit 23: Commercial land prices in different areas (2007*)

Governorates/Areas	Prices (KD/Sqm)	Average prices (KD/Sqm)
Capital Governorate	-	10,750
Downtown (Al-Mubarakiya Souq)	3,000-5,000	4,000
Downtown (Ahmad Al-Jaber Str.)	9,500-12,000	10,750
Downtown (Mubarak Al-Kabir Str.)	10,000-11,000	10,500
Downtown (Fahd Al-Salem Str.)	10,500-12,000	11,250
Downtown		
(Ali Al-Salem Str.) (FAR 300)	4,400-6,000	5,200
(Ali Al-Salem Str.) (FAR 520)	8,000-9,000	8,500
Governorates/Areas	**Prices (KD/Sqm)**	**Average prices (KD/Sqm)**
Farwaniya	-	4,500
Kheitan	2,800-3,300	3,050
Dajeej	650-750	700
farwaniya munawir st	4,000-4,500	4,250
farwaniya matafi st	3,000-3,500	3,250
Governorates/Areas	**Prices (KD/Sqm)**	**Average prices (KD/Sqm)**
Hawalli	-	3,750
Salem Al mubarak street (Salmiya)	4,000-4,500	4,250
Bahrain street (Salmiya)	2,500-2,800	2,650
Beirut Street (Hawalli)	3,500-4,000	3,750
Tunis st (Hawalli)	3,500-4,000	3,750
Al-Othman st	2,800-3,200	3,000
Governorates/Areas	**Prices (KD/Sqm)**	**Average prices (KD/Sqm)**
Jahra		2,900

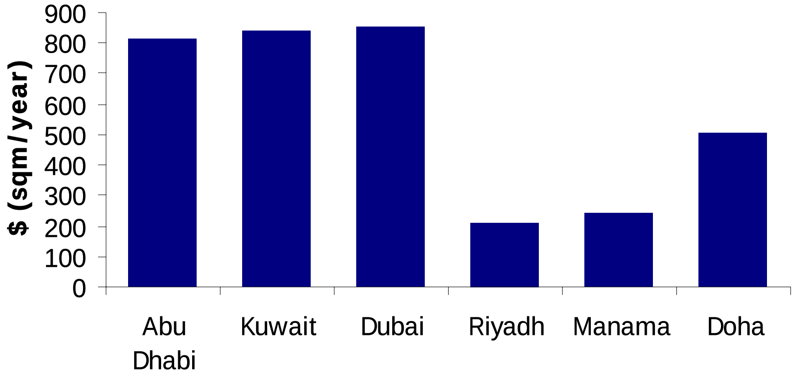
Source: Kuwait Finance House, * As on third quarter of 2007.

Office rents in Kuwait has increased by 100% since 2003

According to Colliers International, office rents in Kuwait have risen by close to 100% since 2003. In 2006, Kuwait registered the second highest y-o-y growth in office rentals among GCC countries after Abu Dhabi. Average annual office rentals in Kuwait increased 41% y-o-y to reach $844 per sqm (Refer exhibit 24) in 2006. Kuwait also stood second in terms of rental value after Dubai. The gap between Dubai and Kuwait City narrowed significantly to just $13 per sqm per year.

Among GCC countries, Kuwait registered the second highest y-o-y growth in office rentals in 2006

Exhibit 24: Office rentals across major cities in GCC (2006)



Source: Colliers International

Cumulative rental growth in Jahra and Jleeb Al Shuyoukh stood at 69.4% and 61.6%, respectively, over the past five years

In the past few years, rental growth was higher in the outer city areas compared to the inner city areas. This can be explained from the fact that cumulative rental growth in Jahra and Jleeb Al Shuyoukh (outer city areas) stood at 69.4% and 61.6%, respectively, over the past five years. On the other hand, cumulative rental growth in Salmiya and Kuwait City (inner city areas) stood at 37.0% and 32.1%, respectively, over the past five years.

Future opportunities

Outer City office properties are expected to provide higher returns, going forward

We believe that the office segment in Kuwait exhibits similar trends as Istithmari segment (investment) with respect to future potential opportunities. As mentioned above, the rent growth is higher in the outer city areas compared to the inner city areas. Furthermore, land price appreciation for office properties is lower in the outer city areas than inner city areas. Due to the high rental growth and lower land value appreciation, office cap rates are higher in outer city locations (Refer exhibit 25). Therefore, we expect cap rates of outer city office properties to compress at a faster pace when compared to those of inner city area's cap rates and hence provide higher returns, going forward.

Exhibit 25: Office cap rates in inner city and outer city areas

Inner City	Cap rate	Outer City	Cap rate
Kuwait	6.5%	Farwaniya	8.5%
Sharq	6.5%	Kheitan	8.8%
Hawalli	8.0%	Jahra	9.0%
Salmiya	8.0%	Fahaheel	9.5%

Source: Al-Jal Real Estate

Drivers of the office segment

Demand Driver	Signal	Justification
Strong growth of	Positive	Kuwait has been experiencing strong

the Kuwait economy		economic growth primarily due to increasing oil prices. Kuwait's current account surplus increased by 47.7% y-o-y to reach KD14.8 Bn ($53.6 Bn) in 2006. Kuwait has been a key beneficiary of the oil boom with current oil reserves accounting for 10% of the world's reserves. The government is expected to invest a significant part of the oil gains in developing oil and gas facilities, infrastructure, and other sectors of the economy. We believe that this has helped create a strong business environment, which is attracting more foreign companies to participate in different sectors of the country.
Government support	Positive	The Kuwait's government has been attempting to liberalize foreign investment regulations. In line with this, the government has renewed long-standing legislative proposals to reduce foreign corporate tax from 55% to 25% in order to attract foreign investment. Furthermore, government allows 100% investment in certain sectors of the economy. Favorable foreign investment regulations are likely to see entry of more foreign multinationals in Kuwait.

Outlook of the office market

The growing demand for class A office space is expected to continue in the short term. However, majority of the office supply is likely to come into the market in the next 2-3 years. This, in our view, will keep the growth in rentals at moderate levels in the short-term (1-2 years). However, as the entire supply of new units gets absorbed, rentals are likely to increase at lower rates in the medium term (3-4 years) and start decreasing in the long term (5 years and above). As for class B and C office space, our assessment tends to stay bullish for this sub-segment of the office market in the foreseeable future.

B. Retail

Kuwait is one of the most established retail markets in the Gulf region. After a relatively stagnant performance up to 2001, retail real estate has seen increased activity. Rising number of expatriates and growing purchasing power are fuelling retail consumption, thereby transforming the retail real estate market in Kuwait.

Although the proportion of street-facing retail stores remains high, a number of comparatively small malls [from 5,000 - 8,000 sqm Gross Leasable Area (GLA)] have been constructed during 1993-1998. The trend has now shifted towards development of large malls. Tamdeen which has a firm grip on Kuwait's retail market also opened AlKout mall in 2005 as a part of its Waterfront Project in Fahaheel. The development encompasses in excess of 17,000 sqm of retail and rentable area. However, construction of "Souk Sharq" mall by "National Real Estate Company" in 1998 actually marked the switch towards construction of large malls. "Souk Sharq" is one of the most popular malls in Kuwait located on the seafront of Safat with total GLA of 28,384 sqm (Refer exhibit 26).

There has been shifting trends towards development of large malls

Going forward, several mega malls are planned to be developed by Tamdeen such as the Mall of Kuwait (130,000 sqm GLA, opening 2008), and '360˚ Kuwait' (60,000 sqm GLA, in 2008) mall among the others. Salhiya Real Estate Company also plans to develop an integrated multi use development named "Al-Asemeh" which will feature a 70 storey tower and a mall with a total development cost exceeding $250 Mn. Avenues Mall phase I of Mabanee has opened in April 2007 (160,000 sqm GLA) and it is expected to finish phase II in 2008 (340,000 sqm GLA) to reach in total 500,000 sqm and thus is expected to be the biggest mall in the region (Refer exhibit 27). Furthermore, the Kuwait's retail property market is witnessing trend towards construction of air-conditioned shopping centers both in up-market suburbs such as Salmiya and in the Kuwait City.

Exhibit 26: Existing major malls in Kuwait

Mall	Location	GLA sqm	Rent/month KD/Sqm	Year
Avenues Mall phase I	Al Rai	160,000	30 - 45	2007
AlKout mall	Fahaheel	17,000	25 - 35	2005
Al Raya shopping mall	Sharq	20,000	35 - 45	2003
Marina mall	Salmiya.	31,000	30 - 45	2002
Al Thuraya	Salmiya	5,400	25 - 35	1999
Souk Sharq	Kuwait City	28,384	25 - 35	1998
Al Bustan	Salmiya	12,000	20 - 30	1998
Al Fanar	Salmiya	17,000	25 - 35	1997
Laila Gallery	Salmiya	6,407	20 - 30	1993
Salhia Complex	Kuwait City	14,000	30 - 45	1978

Source: Markaz Research

Occupancy rates in up-market malls, such as Marina mall and Al Fanar, stood at 100%

Furthermore, the increasing entrance of regional and international retail brand names (such as Carrefour, IKEA, and Abu Dhabi based Emke Group) to the market has created strong demand for retail space. The average vacancy rates in shopping centers and malls in Salmiya and Kuwait City stood less than 2%. Occupancy rates in up-market malls, such as Marina Mall and Al Fanar, stood at 100%.

Status of the retail space in Kuwait

Total retail space in Kuwait was estimated at 345,000 sqm at the end of 2006. Approximately 349,000 sqm of retail space is in the construction /planning phase and expected to be delivered by 2008.

Exhibit 27: Upcoming major malls in Kuwait

Name of the Mall	Location	Developer	Total GLA (sqm)	Year of operation
360 degree Kuwait Mall	South Surra	Tamdeen	60,000	2008
Mall of Kuwait	Sabahiya	Tamdeen	130,000	2008
Symphony Mall	Salmiya	Commercial Real Estate Co.	N/A	2008
The Avenues-Phase II &III	Al Rai	Mabanee Company	340,000	2008
Al-Asemeh mall	Sharq	Salhiya Real Estate Co.	N/A	2011

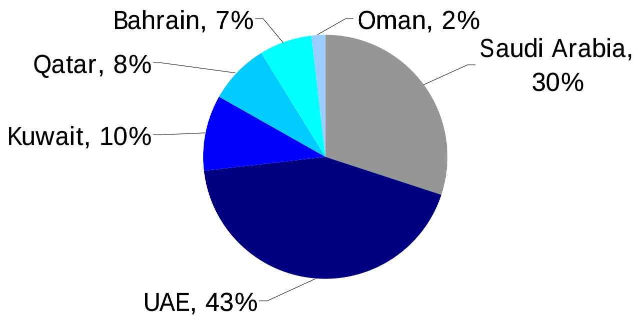
Source: Markaz Research

According to Colliers International, total offering of retail space in Kuwait is expected to reach 1.15 Mn sqm of GLA by the end of 2010, representing an increase of 233% over 2006. Kuwait will be the third largest provider of retail space, accounting for 10% of the total supply coming online by 2010 in the GCC region (Refer exhibit 28).

Furthermore, the retail space per capita in Kuwait is expected to increase to 0.32 sqm compared to 0.66 sqm for the GCC region by 2010 which will act as a positive driver for retail development in Kuwait. Consequently, we expect the retail market in Kuwait to remain strong in the short to medium term (1-4 years) and stabilize in the long term (beyond 4 years).

Kuwait will be the third largest provider of the retail space in GCC by 2010

Exhibit 28: Expected spread of retail supply in the GCC in 2010



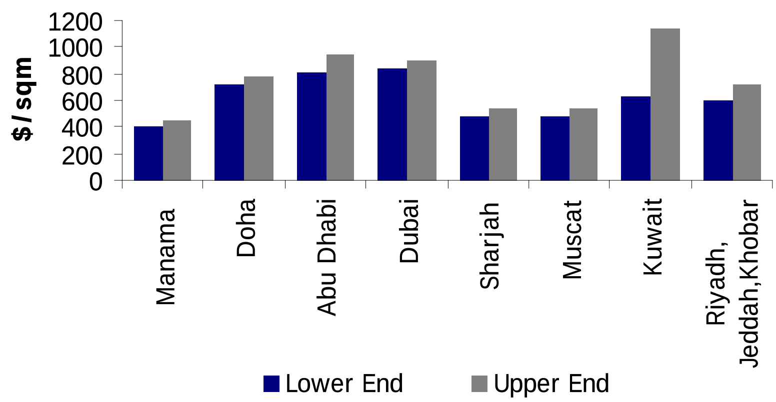
Source: Retail International

Prices and rentals

The boom in Kuwait's retail segment has also pushed prices and rentals higher. According to Kuwait International Bank, commercial segment average land rates grew rapidly at a CAGR of 18.8% over the period 2000-2006. Furthermore, average retail rental rates in Kuwait increased by approximately 17% y-o-y in 2006. Kuwait features the highest level of retail rentals in the GCC region. The average yearly retail rental in the prime shopping malls in Kuwait stood at $900-$2,000 per sqm in 2006 (Refer exhibit 29).

Kuwait features the highest level of retail rentals in the GCC region.

Exhibit 29: Rentals in the malls across GCC 2006



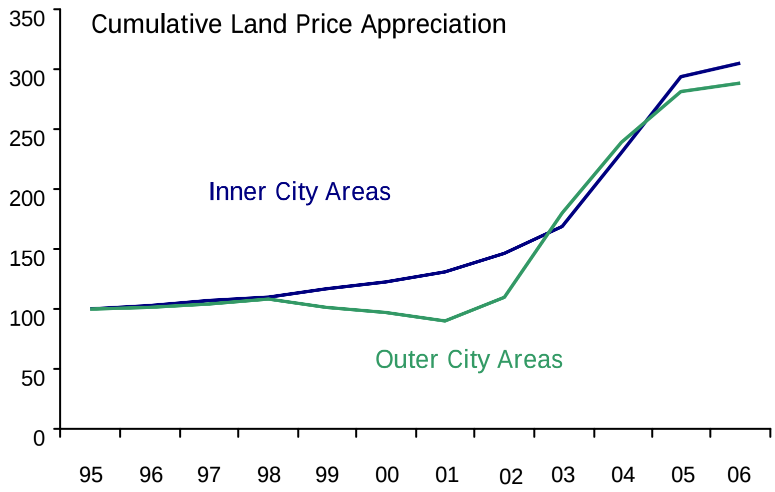
Source: Retail International, CB Richard Ellis

Future opportunities and outlook

The conventional sub-segment of retail in Kuwait depicts similar opportunity trends as Istithmari and class B and C office real estate. We expect rental growth in outer city areas to be higher than inner city areas due to high growth in population and demand from unskilled and semi-skilled labor residing in these areas. However, in spite of strong demand driven by increasing purchasing power, we expect the high end retail sub-segment in the inner city areas to exhibit a slight oversupply in the long term (5 years and above). Furthermore, in the past few years, land price appreciation for retail property was lower in the outer city areas than inner city areas (Refer exhibit 30). Due to the expected high rental growth and the current lower cost of land value appreciation, future cap rates compression is expected to be higher in outer city locations. Consequently, in general we expect outer city retail properties to provide higher returns, going forward.

Going forward, outer City retail properties are expected to provide higher returns

Exhibit 30: Commercial land price appreciation



Source: Markaz Assessment

Cap rates compression is expected to be higher in outer city locations

Drivers of the retail segment

Demand Driver	Signal	Justification
Consumer dynamics	Positive	Economic boom in Kuwait has led to growth in per capita income, and hence, purchasing power of consumers. As mentioned earlier, the country's per capita GDP increased 8.0% y-o-y to reach $28,100 compared to an average per capita GDP of $17,425 for the entire GCC region in 2006. Added to that, the influx of expatriates coupled with increasing brand awareness has fueled retail consumption and contributed to shifting trends toward buying high-end retail products from malls. Consequently, investments in construction of shopping centers and malls are on the rise, driving demand in the retail real estate sector.
Favorable regulations	Positive	Kuwait government's increasing thrust towards liberalization of foreign investment regulation has encouraged many regional and foreign players in the country. For instance, Carrefour has recently, opened an outlet in the 'The Avenues' mall, which is set to be Kuwait's largest commercial development when completed in 2010. Furthermore, Emke Group opened its first hypermarket in Kuwait at the beginning of 2007.

Growing per capita income led to the shift in trend towards buying high-end products

Increasing presence of foreign retail brands is likely to push demand for quality retail space

Demographics	Positive	Kuwait has a young population with approximately 64% of the population below the age of 35. The high proportion of young population is likely to drive retail consumption. Hence, investments in retail property, such as shopping centers and malls, may also get a strong boost.
Population of semi skilled labor	Positive	Kuwait has a high proportion (36% in 2006) of semiskilled labor. This factor is likely to fuel the consumption of mid-low end consumer products such as electronics and clothing manufactured in China and other low-cost countries.

Rentals for conventional retail properties are expected to remain bullish in the long term

Outlook of the retail market

Demand for retail space is expected to persist in the short term. Consequently, we expect retail rentals to witness an upward trend in the short term. However, as majority of the retail supply is likely to go live in the next three-four years, retail rentals for malls (high-end) will stabilize or slightly decline in the long term. For conventional retail properties, our assessment tends to stay bullish even in the long term.

Government has embarked upon a master plan aiming at attracting higher number of tourists

C. Hospitality/Tourism & Leisure

Kuwait's Tourism and Leisure industry is characterized by sluggish growth owed to limited tourist facilities. This is largely due to the delay in enacting the B.O.T law, which is limiting private sector participation. Consequently, there has been delay in the execution of strategic tourist and leisure projects such as Failaka and Boubyan Islands.
However, the government appears to have realized the shortcomings and has increased its focus on reviving tourism where Kuwait has recently seen an increase in tourist arrivals. According to World Tourism Organization (WTO), the total number of tourists visiting Kuwait increased at a CAGR of 5.7% to 120,000 during 2002- 2006. Furthermore, the number of tourist nights spent rose 25.0% y-o-y to 1.9 Mn in 2006. However, still the majority of tourists visiting Kuwait comprises of business travelers.

The hospitality industry in Kuwait is dominated by business travelers as they account for 90% of hotel occupancy in the country. The hospitality industry has shown signs of recovery since 2003, with 90 hotel licenses being granted since then. After the war in Iraq, Kuwait's hospitality sector has emerged as one of the fastest expanding segments. The growth is being driven by the positive business environment created by Kuwait's improved economic fundamentals.

Government's efforts: 20 year master plan

Delay in the ratification of B.O.T law has led to the development of limited tourism facilities

In 2004, the Kuwait's government launched a 20-year tourism master plan, developed in tandem with the World Tourism Organization and the United Nations. The goal of the master plan is to transform Kuwait into a world class tourism and business destination. In line with this objective, the government is working on the Failaka Island project. The project aims to transform the historic island, located 20 km northeast of Kuwait City, into a major tourist attraction. Under the project, the government plans to develop hotels, shops, residential complexes, a media center and restaurants at an estimated cost of $3.3 Bn. The government has also been investing heavily in developing and upgrading transport infrastructure. To that end, the government has outlined a master plan for the expansion of the Kuwait International Airport. The plan includes the construction of a second terminal on a build-operate-transfer (B.O.T) basis. It also involves the development of eight air bridges and more aircraft parking space for an estimated cost of $350 Mn. The expansion plan will enable Kuwait International Airport to handle 15 Mn passengers per year by 2015. Furthermore, to attract foreign investments within the tourism sector, the government has introduced a new foreign investment law. The new law allows foreign companies to operate in Kuwait with 100% foreign ownership in most of the sectors, including tourism.

Demand and Supply in Hospitality/lodging market

Supply of rooms in 5 star and 4 star hotel categories is expected to double by the end of 2008

The hotel industry has been a direct beneficiary of the increasing number of business travelers visiting Kuwait. The total number of incoming tourists increased 17.0% y-o-y to 120,000 in 2006. Furthermore, the number of occupants in Kuwait's hotels reached 175,000 between January and July 2007, a 47% increase over the corresponding year-ago period. Business travelers accounted for majority of the hotel occupants representing 90% of the total hotel occupancy. With tourist arrivals increasing, Kuwait has witnessed strong growth in demand for hotel rooms. Average hotel occupancy rates have increased to 65% in 2006 from 45% in 2000. However, this average was below the 68.7% for the Middle East region. Average revenue per available room (Revpar) in Kuwait stood at $155 in 2006, compared to $143 for the Middle East region. On the supply front, supply of room inventory remained almost stagnant until 2002, where supply of room inventory has been rising steadily. This can be primarily attributed to the government's effort to encourage more investments within the hospitality and tourism sector. The Ministry of Commerce and Industry received 128 applications for new hotels with more than 15,000 rooms. Of those, approvals were granted to 100 new hotels during early 2006. Currently, there are 45 hotels in Kuwait with approximately 4,500 rooms. Supply of rooms in 5-star and 4-star hotel categories stood at 2,957 in 2006.

With increasing number of tourists expected to visit Kuwait, there has been thrust toward investing in hotel infrastructure since the last couple of years. Majority of the new hotel room supply is expected to come on stream by 2008 (Refer exhibit 31). The number of hotel rooms in 5-star and 4-star hotel categories is expected to increase by approximately 2,200 rooms to reach about 5,157 rooms by the end of 2008. Future hotel developments will be primarily concentrated in locations such as Salmiya, Sharq and Hawally.

Expected oversupply of hotel rooms is likely to put pressure on average room rates

Exhibit 31: Expected future supply of hotel rooms in 2008

Development	Rooms	Grade	Opeartor	Year of opening
The Monarch	400	5	Refad	2008
Cerruti	350	5	Cerruti	2008
Refad Resort and Spa	325	5	Refad	2008
The hotel (Not named)	280	5	Intercontinental	2008
Four Seasons	225	5	Four Seasons	2008
Safir Renovation	N/A	5	Safir	2008
The square Capital Tower	N/A	4	Refad	2008

Source: Zawya, MEED projects

As the government plans to attract 1 Mn tourists with 650,000 hotel occupants by 2010, we believe that the slow and unsuccessful enactment of the B.O.T law coupled with delay in the execution of strategic tourist and leisure projects could adversely impact the government's plans to attract more tourists.

Drivers of the hospitality and tourism segment

Demand Driver	Signal	Justification
Foreign ownership regulation	Positive	In order to attract private investment within the tourism and hospitality sector, the government has been encouraging foreign companies to operate in Kuwait with 100% foreign ownership in the tourism sector. This is likely to attract more foreign investment, fuelling further growth in the real estate and construction sector of Kuwait.
Unsuccessful enactment of B.O.T law	Negative	Government has been considering the use of the B.O.T mechanism. This system allows private sector companies to develop and invest in plots that are owned by the government. However, the B.O.T. mechanism has been under deliberation for a long time and is yet to be ratified.
Unsuccessful government efforts	Negative	The Kuwait's government has been attempting to revitalize the tourism industry through the development of strategic tourist and leisure projects such as Failaka and Boubyan Islands. However, development of these projects has been frozen. This has led to investors doubting the Kuwait government's ability to implement anchor tourist projects.

Outlook for the hospitality and tourism sub-segment

A large part of the hotel room supply is expected to come online by the end of 2008. The increase in room supply is bound to create an over-capacity situation in the market. Consequently, we believe that Kuwait may see lower occupancy rates and increased pressure on average room rates until the absorption of supply growth. This factor could restrict the growth of fresh investments in hotel infrastructure in the future.

"Silk City" project:

Government has formed a committee to oversee the execution of Silk City project

Kuwait's government is planning to develop the Silk City project in the Subbiya region on the northern shore of the Kuwait bay. The government has recently formed a committee to oversee the execution of the Silk City project. The project is a mixed use of business, commerce, culture, residence, and entertainment to be built over 250 Mn sqm. The city will include a resort, a 2 Mn sqm desert preserve, and will be linked to Kuwait City by the Sheikh Jaber Al-Ahmad Al-Sabah Bridge. The city will also hold a free zone near a new international airport, a business city, and an area for forums and exhibitions, sports, culture, environment, media, industry, education and health. Furthermore, it will include tourism centers, hotels, resorts, public gardens, spacious residential areas, and a tall and distinctive tower.

Investment in the city has been estimated at KD 25 Bn. We believe that the project will serve to create investment opportunities and attract both local and foreign investors, while creating an effective strategic partnership between the public and private sectors. While the first phase of the project is expected to be completed within the next five years, the full project is scheduled for completion in the next 25 years.

D. Industrial segment

Industrial segment has benefited from governments effort to diversify

The Industrial segment in Kuwait can be primarily divided into: (a) sector covering logistics, warehousing, storage, manufacturing and other conventional facilities. Areas covering these activities are located in Sulaibieh, Sabhan, and Shua'aibah; (b) another in Shuwaikh and Rai area that covers retail, car repair, and office space; and (c) the oil and gas sector which occupies areas such as Al-Hmadi, and Mina Abdulah. In the Shuwaikh and Rai area, the government retains the land and enters into lease contracts with tenants. Tenants, in turn, buy and sell properties based on these contracts with prices close to other retail and office areas outside Kuwait city.

The oil and gas sector in Kuwait has primarily benefited from higher hydrocarbon prices and rich availability of oil reserves. This led to the higher expenditure by the government in various industrial infrastructure projects within the oil & gas and energy sector. Kuwait is planning to invest nearly $64 Bn in its hydrocarbon sector over the next 15 years as it seeks to ramp up both oil production and refining capacity. Approximately $26 Bn will be invested in upstream operations as the country aims to achieve its goal of producing 4 Mn barrels a day (b/d) of crude by 2020, while $17 Bn will be invested in downstream projects. This is likely to fuel the demand for industrial property of type (c) mentioned above.

Establishment of FTZs likely to attract the setting up of new industrial facilities

Kuwait has also benefited from the government's efforts to diversify the economy and increase investments in other sectors. Power has been identified as a key growth area. The Public Authority for Industry (PAI) has also allocated KD7 Mn to establish new power generators for industrial areas in Al-Shuaiba. Furthermore, the Ministry of Electricity & Water plans to build a $1.8 Bn, 1500 MW gas-fired combined cycle power plant at Subiya. The plant will serve both Kuwait City and Subiya. The project is expected to be completed by the end of 2011. The government also provides infrastructure and other support facilities to national industries by allowing the private sector to develop industrial areas on state-owned properties. Consequently, Kuwait has been witnessing flurry of industrial activity in the heavy industrial sector in recent years. A recent example is the launch of a $255 Mn facility by United Steel Industrial Company for its reinforced bars factory. The factory will be built on a total area of 100,000 sqm. The government of Kuwait is also encouraging the setting up of light and medium industries, According to UHY, (a leading business advisory and consulting firm), the Ministry of Energy plans to develop loading and exporting facilities over three years at an estimated $1 Bn. Consequently, rates of industrial plots (warehousing and storage) rose from 4.3%-13.8% during the 3rd quarter of 2007, compared to the 2nd quarter. Shuwaikh Industrial Area and Al Raii witnessed a notable increase that reached 16.5% on average.

a- Kuwait Free Trade Zone (KFTZ)

The Kuwait government established the Free Trade Zone in 1995 to boost activities in the industrial segment. Since 1995, KFTZ offers several benefits such as guaranteed tax exemptions, no restrictions on repatriation of capital and profits, and no customs or other import duties or taxes on imports into or exports out of the KFTZ. The free trade zone has also reserved around 700,000 square meters for such industries. In addition, Kuwait's FTZ located in Shuwaikh allows 100% foreign ownership of businesses within the zone. This is likely to encourage the setting up of industrial facilities in the KFTZ, increasing the demand for industrial property.

Industrial land prices in Shuwaikh area are highest among other industrial areas

We expect demand for industrial space in Kuwait to pick up as the government continues to open up for foreign investments, and provide several incentives to the sector. This, in turn, will boost the demand for industrial properties, leading to increase in prices and rentals of industrial land.

Industrial Zones in Kuwait

The major Industrial zones in Kuwait are located in areas such as Shuaiba, Shuwaikh, Subhan, Ahmadi and Mina Abdullah. Shuaiba is considered as the largest industrial area and contains most of the country's heavy industries, many of which are based on raw materials derived from oil. Shuwaikh and Al-Rai are the largest non-oil industrial areas and contains many small workshops, several large plants producing construction materials, as well as various wholesale and retail businesses. The light industries are primarily located in Sabhan with mainly assembly-type plants, printing presses, food and beverages factories and warehousing. Several smaller industrial areas are located in Sulaibikhat, Jahra and Ahmadi.

The Shuaiba industrial area (SIA)

SIA is the first industrial complex in Kuwait and is considered the largest industrial area (according to Kuwait Publishing House) in Kuwait It accommodates most of the large-scale industries in Kuwait. Presently, there are 12 major industries including two petrochemical companies, three refineries, two power plants and an industrial gas corporation. Currently, 30% of the land in the SIA's eastern sector and 70% of land in the SIA's western sector is available for future expansion. The major upcoming project in the SIA includes, development of 235,000 sqm calcined coke plant by Petroleum Coke Industries Company (PCIC).

b- Shuwaikh and Rai industrial area

Shuwaikh industrial area is the largest non-oil related industry and warehousing area in Kuwait. Shuwaikh industrial area has been witnessing a rise in the industrial activities. This is driven by its close proximity to Kuwait City and its easy access to Shuwaikh Port and the free trade zone. Land prices in Shuwaikh Industrial Area are considered the highest among other industrial areas in Kuwait as it is used for retail, show rooms, office space, as well as light manufacturing and car repair shops. Prices of industrial plots in Shuwaikh increased by 16.5% in Q3 2007 compared to Q2 2007. Prices range between KD 300 to KD 1,500 per sqm in industrial Shuwaikh.

4. Role of private sector

Government is considering opening up to the private sector through B.O.T contracts

With growing demand for housing units and infrastructure development in Kuwait, the government has been encouraging greater private sector participation. The government has been following the B.O.T (Build-Operate-Transfer) mechanism to allow the private sector to play a more dynamic role in the real estate and construction sectors. Furthermore, due to high land prices in Kuwait, investors are increasingly turning towards B.O.T mechanism. B.O.T has become an important tool for financing government's infrastructure projects. Under the B.O.T mechanism, private sector companies are permitted to develop plots owned by the government and to operate and benefit from the venture for a period of 20 years from the end of construction, after which the projects revert to the Municipality. "Souk Al-Kuwait" developed in 1970's and operated by Kuwait real estate company, was the first retail and car park project on B.O.T. basis in Kuwait. The Sharq Development on the Waterfront of Kuwait City in 1998 was the first modern shopping mall carried out on a B.O.T basis in Kuwait. The private sector is expected to invest approximately $8 Bn in the Kuwait's construction sector over the next five years. Furthermore, Ministry of Public Works has announced to undertake 500 large scale infrastructure projects in the next few years. Majority of these projects are expected to be executed on B.O.T basis. The government also intends to coordinate several other B.O.T projects, such as Failaka islands, Bubiyan islands, and the Silk City.

Prolonged delay in approval of B.O.T. could act as hindrance for private sector participation

Kuwait's government has been allowing projects on B.O.T basis since early seventies. These projects continue to be plagued by cumbersome government procedures. However, the government is working towards making procedures and regulations more flexible. To promote co-operation between the public and private sectors in infrastructure, the government had put forward new draft legislation to the Kuwait's parliament in recent months. This legislation outlines more flexible procedures for B.O.T and Public-Private-Partnerships (PPP). Growing private sector participation through the B.O.T route is likely to fuel the investment within Kuwait's real estate and construction sectors, going forward. On the other hand, a prolonged delay in approval of this legislation could hinder private sector participation in infrastructure projects.

5. Stock market performance

Real estate sector in Kuwait has significant representation in the country's stock market.

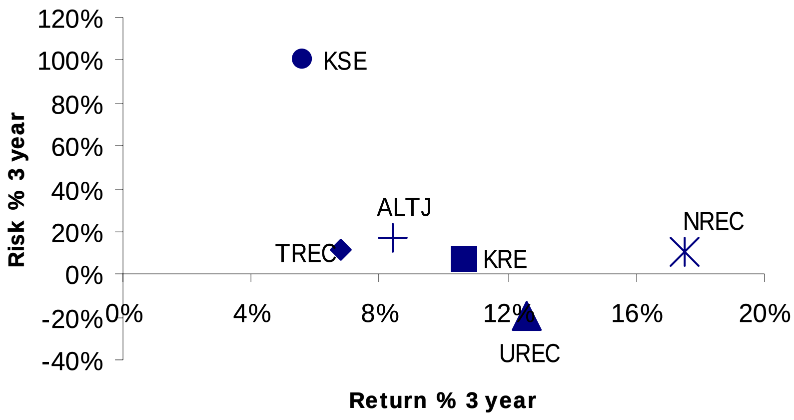
There were 198 companies listed on Kuwait Stock Exchange (KSE) with a total market capitalization of KD 51.0 Bn ($184.0 Bn) as at November 2007. The real estate sector in Kuwait has significant representation in the country's stock market. The sector's market capitalization accounted for 7.0% of the total market cap of Kuwait Stock Exchange Price Index (KSEP) as at November 2007. Furthermore, 34 real estate companies are listed, accounting for 17% of the total listed companies in the Kuwait Stock Exchange. In addition, 29 Kuwait's real estate companies feature among the top 40 real estate stocks (in terms of market cap) in the GCC region (Refer appendix 4). These companies accounted for 20.4% of the of the total market cap of the real estate stocks in the GCC region.

On the performance front, all sectors have provided positive return in the last three years (November 2004-November 2007). Banking sector and service sector generated the highest return of 127.2% and 116.6% respectively in the last three years. The real estate sector provided the lowest return of 14.3% during the last three years. This can be attributed to the limited growth in profitability of the real estate companies listed on the KSE over the last three years compared to companies listed in other sectors. However, the real estate sector rebounded during the first nine months of 2007, as improved profitability and positive macroeconomic fundamentals lifted investor sentiment in the sector.

For the purpose of analyzing the stock market performance of the real estate sector during the last three years, we have considered the top five real estate companies in terms revenue: Kuwait Real Estate Co. (KRE), United Real Estate Co. (UREC), National Real Estate Co. (NREC), Tamdeen Real Estate Co. (TREC), and Altijaria (ALTJ). These companies accounted for 40.0% of the real estate sector's total market cap at November 2007. Real estate stocks have underperformed the broad market index (KSEP) during the last three years (Refer exhibit 32). While UREC provided the lowest return (-19.7%), ALTJ yielded the highest return (16.7%) during the last three years. Furthermore, the real estate stocks also proved to be riskier than the benchmark index during the last three years.

Exhibit 32: Risk & Return chart for Kuwait Real Estate stocks

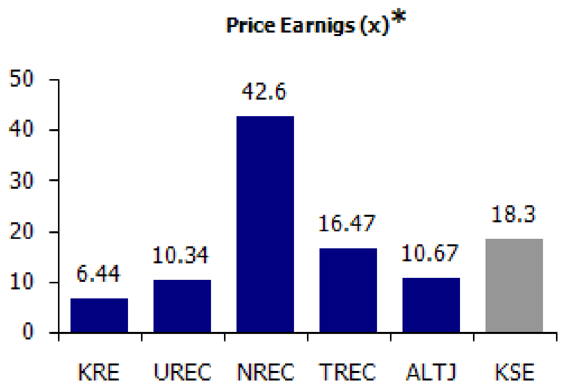
Real Estate stocks and Benchmark performance (Nov. 2004-Nov. 2007)

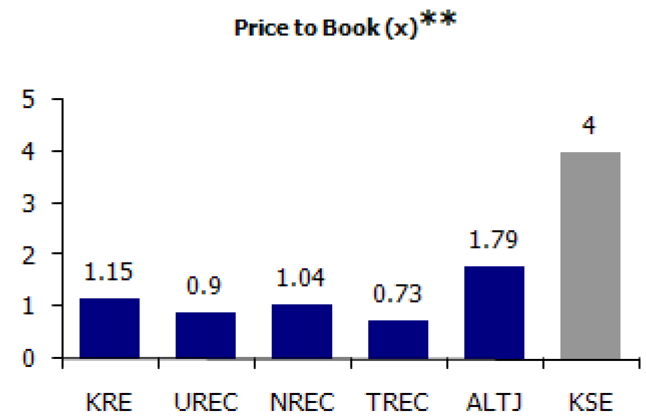


Source: Bloomberg, Markaz analysis

NREC proved to be the riskiest stock, while TREC remained less risky. The price of the majority of real estate stocks moved higher during the last three years, depicting positive investor sentiment. In spite of the increase in price, UREC, TREC, and ALTJ continue to trade at discount to the historical (November 2004 to November 2007) average in terms of price-to-earnings ratio. On the other hand, KRE and NREC trade at premium to the historical average in terms of price-to-earnings ratio. However, all the five real estate stock continue to trade at discount to the historical average in terms of price-to-book ratio (Refer exhibit 33).

Exhibit 33: Valuation landscape of real estate stocks





Source: Reuters, SICO, Bloomberg

6. Conclusion

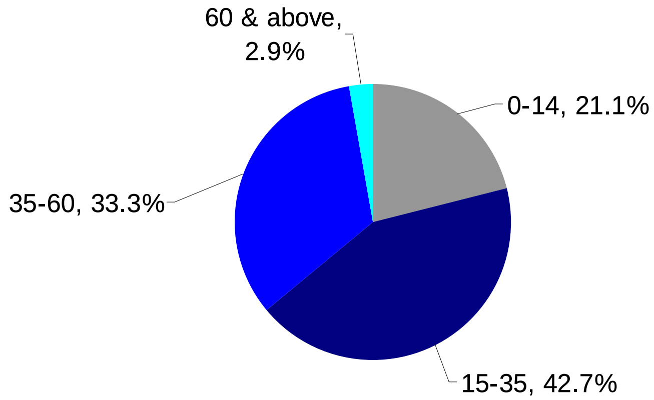
Kuwait's real estate and construction sectors are currently experiencing unprecedented growth, led by strong economic growth triggered by high oil prices. The growth in Kuwait 's real estate sector can be attributed to the fact that currently demand is outstripping supply in all segments of Kuwait's real estate, except for the hospitality and tourism segment. We expect Kuwait's construction and real estate sectors to sustain strong growth, going forward. This would be driven by expected robust economic conditions in the light of high oil prices. In addition, Kuwait's diversification program aiming at lowering the economy's dependence on oil and gas revenues and the $11 Bn worth of investment over the next five years, further enhances the country's economic outlook.

In the residential segment, we expect the private housing sub-segment to continue witnessing undersupply in the medium term. This is primarily due to pile up of unmet demand over the last few years. We expect demand for private housing units to reach approximately 100,000 in 2010. In the Istithmari segment, we expect properties in the outer city areas of Kuwait (such as Fahaheel, Jahra, Salmiya, Mahboola, and Mangaf) to offer greater potential for returns. This is due to the higher potential for rental growth and attractive land valuations compared to inner city areas. This, in turn, would drive cap rates downwards in the coming years to levels close to those of inner city areas.

In the commercial segment, majority of office space under construction and development will be ready for renting in 2009. Consequently, we expect the office market in Kuwait to witness an oversupply situation in the long term. Rentals for class A office space is expected to increase at lower rates in the medium term and start decreasing in the long term. However, for class B and C office space, our forecast tends to stay bullish in the foreseeable future. As for retail segment, demand for retail space is expected to continue in the short term with entry of major foreign and regional brand in the light of Kuwait's positive economic outlook. Consequently, we expect retail rentals to witness an upward trend in the short term. However, for conventional retail properties, our assessment tends to stay bullish even in the long term. In hospitality segment, increase in room supply is likely to create an over-capacity situation in the market. Consequently, we believe that Kuwait may see lower occupancy rates, restricting new investments in the hospitality sector. However, in the industrial segment government's several industrial infrastructure projects within the oil & gas and energy sector coupled with establishment of FTZs would drive the demand for industrial properties in the short to medium term.

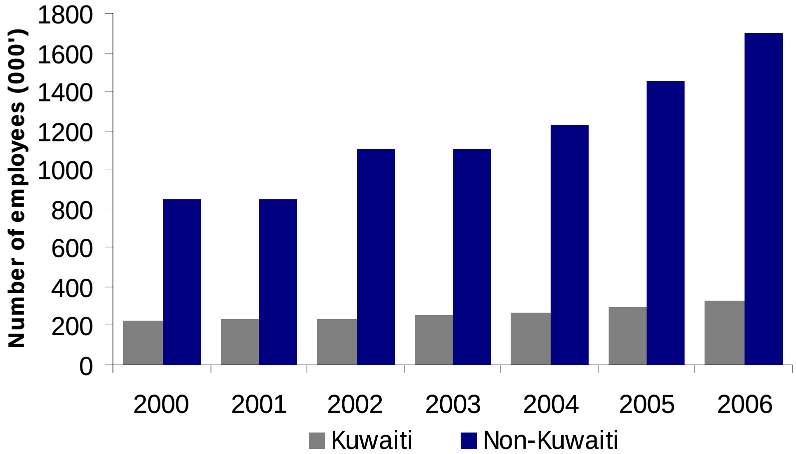
The growth in the Kuwait's real estate sector would be further supported by increasing private sector investment backed by strong government support. However, slow reforms of existing laws and half-hearted attempts by the government are restricting the private sector participation in development projects. In addition, high land prices in Kuwait further curbs development as it negatively impacts demand and render new projects financially unviable. Going forward, we believe Kuwait's economy is heavily dependent on the oil & gas sector. A sudden drop in the oil price could negatively impact country's economic outlook. This coupled with instability in the region's geopolitical situation could pose threat to Kuwait's real estate sector.

Appendix: 1 Kuwait population by age group (2006)



Source: Ministry of planning/UN population division

Appendix: 2 Employment growth (2000-2006)



Source: Ministry of Planning

Appendix: 3 Major real estate, infrastructure, and industrial project

Sr No.	Project Name	Type	Company name	Project completion date	Value	Sqm (000')
1	Silk City project	Residential/Commercial	Tamdeen Real Estate and Ajiyal Real Estate Co.	2012 (Phase I)	$86 Bn	N/A
2	The Failaka Island	Mixed use	Ministry of Public Works	2014	$3.3 Bn	N/A
3	Bubiyan Island (Including construction of largest seaport in Kuwait)	Tourism	Ministry of Public Works	2016	$6 Bn	N/A
4	Khairan Residential City	Residential	Public Authority for Housing Welfare	N/A	$27 Bn	N/A
5	Project Kuwait	Industrial	Kuwait Petroleum Corporation (KPC)	2010	$8.5 Bn	N/A
6	Mina Al-Ahmadi Gas Fractionation Train 4	Industrial	Kuwait National Petroleum Company	2011	$800 Mn	N/A
7	Kuwait City 1st Ring-Road Extension (Phase III)	Commercial	Ministry of Public Works (MPW)	2013	$100 Mn	N/A
8	Al Asima High-Rise Tower	Mixed use	Salhiya Real Estate Company	2011	$310 Mn	150
9	Kuwait Airport Expansion (Phase I)	Commercial	Directorate General of Civil Aviation	2011	$1.8 Bn	N/A
10	Al-Sour Tower	Residential/Retail	Al-Shaya Group	2011	$90 Mn	N/A
11	Subiya Seafront Resort	Tourism	Kipco Asset Management Company	2011	$250 Mn	100
12	Mutlaa Township	Residential	Public Authority for Housing & Welfare	2013	$10 Bn	N/A
13	Al Hamra Tower	Mixed use	Ajial Real Estate	2009	$372 Mn	180
14	Kuwait Busines Town	Commercial	Al Mazaya/Global Investment House	N/A	$241 Mn	11
15	Business City Tower	Mixed use	United Real Estate Co.	2008	$120 Mn	49.5
	Total				$144.9 Bn	

Source: MEED projects

Appendix: 4 Comparative matrix of real estate companies

Name	Country	Market Cap (Mn Dollars)	Close (Lc)	% Price Chg 1Y (As on Nov.07)	PE (x)	P/B (X)	Price to sales (x)	Divid end yield (%)
Large Real Estate Companies in GCC								
EMAAR PROPERTIES	UAE	20558	12.40	5.08	14.12	2.71	5.29	N.A.
EMAAR ECON CITY	Saudi	4729	20.75	15.28	N.A	1.53	N.A	N.A.
ALDAR PROPERTIES	UAE	4446	9.47	115.72	14.74	4.62	135.35	0.65
SOROUH REAL EST	UAE	4675	6.87	141.05	16.78	5.86	12.68	1.16
UNION PROP	UAE	3158	4.17	76.69	18.32	2.94	5.12	N.A.
NATL REAL EST	**Kuwait**	**1182**	**0.48**	**-18.64**	**11.92**	**1.56**	**6.98**	**6.55**
MAKKAH CONSTRUCT	Saudi	1845	41.75	-3.47	46.01	2.51	29.59	2.53
MABANEE CO	**Kuwait**	**1571**	**1.24**	**63.16**	**24.22**	**5.44**	**38.80**	**N.A.**
COMMERCIAL R.E.	**Kuwait**	**1323**	**0.27**	**1.71**	**11.07**	**1.86**	**9.39**	**4.03**
Medium size Real Estate Companies in GCC								
ARAB TECH CONST	UAE	1354	8.32	92.42	15.84	4.57	1.27	2.17
SAUDI REAL EST	Saudi	1383	43.0	13.16	41.75	2.09	32.63	1.41
RAK PROPERTIES	UAE	1051	1.96	42.03	11.96	1.76	N.A.	3.13
TAMDEEN REAL EST	**Kuwait**	**525**	**0.44**	**4.76**	**16.27**	**0.72**	**4.72**	**2.89**
QA REAL EST CO	Qatar	949	48	67.95	14.17	2.45	7.96	N.A.
SALHIAH REAL EST	**Kuwait**	**685**	**0.56**	**-8.20**	**3.09**	**1.38**	**4.70**	**8.38**
KWT REAL EST	**Kuwait**	**684**	**0.24**	**51.90**	**6.00**	**1.07**	**21.45**	**N.A.**
THEMAR	**Kuwait**	**449**	**0.13**	**22.64**	**5.85**	**0.86**	**54.35**	**N.A.**
RED SEA HOUSING	Saudi	561	69.75	7.31	16.78	4.35	3.21	2.06
GRAND REAL EST	**Kuwait**	**409**	**0.32**	**-34.69**	**7.92**	**1.18**	**6.02**	**2.69**
UNITED REAL EST	**Kuwait**	**421**	**0.17**	**-29.17**	**11.20**	**0.98**	**9.08**	**6.27**
INTL INVEST PROJ	**Kuwait**	**510**	**0.24**	**81.82**	**12.54**	**1.88**	**8.63**	**N.A.**
INJAZZAT RE EST	**Kuwait**	**307**	**0.33**	**24.53**	**5.29**	**1.50**	**4.01**	**4.84**
AAYAN REAL EST	**Kuwait**	**331**	**0.29**	**-1.75**	**11.22**	**2.65**	**4.27**	**4.93**
GRND RE TOUR DEV	**Kuwait**	**486**	**0.14**	**-24.73**	**7.57**	**1.17**	**70.30**	**N.A.**
Small size Real Estate Companies in GCC								
AJIAL REAL EST	**Kuwait**	**247**	**0.42**	**25.37**	**7.88**	**0.86**	**52.44**	**4.42**
TIJARA& REAL EST	**Kuwait**	**214**	**0.16**	**-21.57**	**8.30**	**1.19**	**29.75**	**7.23**
ARAB REAL EST CO	**Kuwait**	**232**	**0.14**	**2.94**	**8.39**	**1.42**	**11.28**	**N.A.**
KWT R.E.HOLDING	**Kuwait**	**222**	**0.21**	**34.62**	**16.83**	**1.42**	**9.73**	**N.A.**
JEEZAN REAL EST	**Kuwait**	**223**	**0.28**	**59.09**	**8.68**	**1.22**	**7.71**	**N.A.**
AL ENMAA REA EST	**Kuwait**	**258**	**0.19**	**-7.77**	**1.88**	**1.27**	**2.34**	**5.56**
UNION REAL EST	**Kuwait**	**135**	**0.22**	**12.24**	**7.16**	**0.94**	**6.53**	**4.75**
PEARL REAL EST	**Kuwait**	**144**	**0.18**	**21.62**	**7.44**	**1.30**	**13.41**	**N.A.**
AL-MASSALEH R.E.	**Kuwait**	**131**	**0.19**	**11.76**	**14.39**	**0.94**	**9.08**	**2.64**
ARKAN ALKWT R.E.	**Kuwait**	**141**	**0.19**	**1.06**	**11.79**	**1.58**	**100.68**	**N.A.**
AL KHALEEJ DEV	**Kuwait**	**128**	**0.28**	**-15.15**	**6.60**	**1.87**	**4.61**	**3.43**
UNITED PROJ CO	**Kuwait**	**120**	**0.42**	**6.33**	**3.80**	**1.01**	**4.66**	**2.40**
TAMEER R.E. INV	**Kuwait**	**109**	**0.13**	**3.17**	**19.68**	**0.91**	**22.86**	**3.76**
AQAR REAL EST	**Kuwait**	**98**	**0.13**	**6.56**	**19.75**	**1.32**	**14.64**	**N.A.**
SANAM REAL EST	**Kuwait**	**106**	**0.28**	**17.65**	**15.89**	**1.73**	**13.29**	**N.A.**
AL MOWASAT HLDG	**Kuwait**	**62**	**0.22**	**-13.73**	**16.36**	**1.18**	**1.43**	**N.A.**

Source: Reuters as on November 2007

Markaz Research Offerings

Strategic research

Title	Release Date	Research Highlights
GCC Equity Funds: The Asset Allocation Challenge	Sep-06	Issues behind asset allocation for GCC equity funds. The report examines the asset allocation pattern among GCC equity fund managers.
GCC Leverage Risk: How real it is?	Nov-06	Examining the risk behind increased exposure of the GCC financial system to stock market.
GCC for fundamentalists: A top-down framework	Dec-06	Establishing a framework involving fundamental variables affecting GCC stock markets.
Managing GCC Volatility: Strategies and Tactics	Feb-07	Devising risk-based portfolio strategy.
Derivatives Market in GCC: Cutting a (very) long market short	Mar-07	Examining the need for derivatives market in GCC.
To Leap or To Lag: Choices before GCC Regulators	Apr-07	Examining the evolution and progress of GCC capital market structures.
A Gulf Emerging Portfolio: And Why Not?	Jun-07	A Study on Saudi, Kuwait, and UAE for Portfolio Enhancement.
A Potential USD 140 Bn Industry Review of Asset Management Industry in Kuwait	Sep-07	Examining the status of Kuwait investment industry, both managed accounts and mutual funds.
China and India: Too much	Oct-07	Examining the sharp run ups in

Sector Research

Title	Release Date	Research Highlights
Real Estate Report - Syria	Apr-07	Examining the sector trends in the Arab Republic of Syria.
Saudi Arabia Real Estate	Jul-07	Examining the sector trends in Saudi Arabia.
Qatar Real Estate	Sep-07	Examining the Sector trends in Qatar

Quantitative Research

Title	Release Date	Research Highlights
GCC Asset Allocation	Since May - 07 (Monthly)	Presenting asset allocation strategy for GCC stock markets using an in-house proprietary model. The report also analyses the performance of GCC equity funds.
Markaz Volatility Indices (MVX)	Since Jul – 07 (Monthly)	Launch of Volatility Indices for the six GCC markets, EM and S&P.

Too Fast	emerging markets especially India and China. The report suggests inclusion of GCC inclusion of GCC may soothe the process from an asset allocation perspective.

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