

# Analysis of the Influencing Factors of Housing Price in Saudi Arabia

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## Abstract

An analysis of key factors that determine the housing price in Saudi Arabia has been presented. The analysed studies have indicated that the cause for the high housing price is the high-interest rates of mortgages, high cost of land acquisition, high construction cost due to materials and labour as well as the oil boom that gave rise to inflation. However, there have been efforts to curb the high cost of housing. These efforts are the ambitious project of smart cities, the rise of microfinance sector that offers affordable interest rates on mortgages, the practice of crowd funding, the incorporation of sustainability practices whose effect is the innovation that leads to reduced housing cost as well as the government commitment to upgrade slums areas to accommodate more people. These initiatives would lead to a balance of demand and supply thereby stabilization of housing prices.

**Keywords:** High-interest rates • High construction costs • Sustainability practices • Policies

## Introduction

According to Fereidouni et al., the house prices in Middle East and especially Saudi Arabia has been on the rise [1]. The effect of this increase in house prices has been that the middle and the low income citizens in find difficulties in affording a house [2]. This presents a contradiction to the Saudi Arabia Vision 2030 and the United Nations Sustainability principles of affordable housing [3,4]. The analysis aims to identify the causes of the rise in housing prices in Saudi Arabia. Further, efforts to curb the rise in house prices through provision of affordable houses are identified.

The high prices of houses in Saudi Arabia can be associated with several factors such as the surplus of oil production that leads to increased money in circulation, policy failure by the government to spur the housing sector as well as the high mortgage rates by the financial institutions. However, there have been measures put in place to address this issue of high housing prices. Such measures include the smart cities program and the transformation of the building sector to embrace new innovative technologies that have been demonstrated to lower the cost of construction [5].

The aspect of infrastructure development due to the economic growth would lead to opening up of new areas that can be utilized for housing projects. Roads and rail are important in ensuring the effective transportation of construction materials. Additionally, affordable housing requires the incorporation of Islamic teachings of waqf to spur the much important microfinance sector and crowd funding initiatives to help low-income earners access financial products for homeownership.

## Factors that Influence House Prices

### High interest rates on mortgages

There are a number of factors that contribute to high house prices in Saudi Arabia. To start with, there is high interest rates on mortgages hence the non-affordability. According to research by Alqahtany and Mohannafinancial institutions offer mortgages at high interests thus increasing the house prices [6]. The low-income earners may face challenges in the accumulation of savings to purchase the highly-priced land. Also, servicing such mortgages becomes unbearable to the middle and low income earners. This renders the available houses to be highly-priced hence only affordable to the high-income residents.

### Costly technicalities of construction

A study by Assaf et al. linked the unavailability of affordable houses in Saudi Arabia to costly technical aspects of construction [7]. The study found out that the construction sector faces lack of appropriate material standards in as far as technical aspects of construction is concerned. This implies that the houses build may not withstand the climatic and natural circumstances in the region. The effect is pushing housing costs due to regular maintenance costs hence the unaffordability. The study further highlighted the technical aspects of the unavailability of design professionals. This implies that sourcing these professionals would translate into increased construction costs. Again, this would have an impact on house prices.

### Costly construction procedures

Costly construction procedures especially the use of capital intensive methods in design and construction in Saudi Arabia end up soaring house

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prices. Research by Shaawat et al. showed that the costly procedures utilized in the sector translate to high costs of houses [8]. The procedures are capital intensive hence cannot accommodate the low-income population. The study proposes that there is a need to phase out the capital intensive procedures by adopting innovative green building technologies. This will reduce the construction costs to a level that low-income earners can afford.

### **Socio-economic considerations of the Saudi Arabian population**

Socio-economic considerations of the Saudi Arabian population also affects house prices. A study found out that the majority of urban dwellers have a preference for buying a house than renting arrangements. Also, the study demonstrated that residents had a feeling that owning a house was a sign of success [9]. This implies that the rush to own a house would increase the demand. A situation where the demand outweighs the number of housing units in the market would result to increase in house prices. Additionally, the research showed that the house price would be high due to social economic consideration of privacy considerations, and aesthetics in the locality.

### **High demand and preference**

High demand and preference among Saudis of owning a house is a major factor that pushes the house prices up. There is an approximate shortfall of 1.6 million residents of Saudi Arabia who are yet to benefit from the social support of owning a house [10]. This implies that the 1.6 million number exerts pressure on the housing demand. The available houses are therefore highly-priced due to the natural economic principle of scarcity.

### **High number of retirees with a sole intention to purchase a house**

Housing prices have been demonstrated to be affected by the number of retirees at a particular time [11]. There exist social expectations of retirees owning a home on or after retirement. This can be associated with the need to have an uninterrupted retirement. Retirees may not have an additional revenue source to aid in paying rent expenses. This means that a situation where more retirees are searching for homes to purchase would most likely lead to soaring of house prices and vice versa.

### **Challenges faced by private developers**

Private developers are engaging in affordable housing particularly in Jeddah city. Despite the novel work of complimenting government efforts to upset the high demand for affordable houses, the private developers face a myriad of challenges. A study carried out in Jeddah indicated that the private developers are grappling with frustrations from the institutions charged with housing regulations. Also, the government institutions have failed to improve the infrastructure to open up potential areas for housing development. This further adds on to the frustrations of private developers [12]. These challenges have the effect of the supply of a few quantities of houses hence the price increase.

### **Failed government policies**

The problem of failed government policies that ought to support affordable housing is a key hurdle to efficient housing pricing in Saudi Arabia [13]. This has pushed house prices in major cities of Riyadh and Jeddah. The study by Abed et al. showed that there is a problem of weak policy implementation in as far as affordable housing was concerned [14]. The study points out that there have been cases of complete failure of policies that would otherwise have supported affordable housing. The result has been a few supplies of houses hence the rise in prices. The study advocates for a solid policy that incorporates planning frameworks as provided for in the urban development provisions.

### **Lack of conformity of customer preferences with those of property developers**

Another significant factor that may be associated with high house prices in Saudi Arabia is the lack of conformity of customer preferences with those of property developers [15]. This gives rise to a situation where the property developers supply houses that do not meet customer needs. The resultant effect is a property market with houses that can only be afforded by a few. This leads to unsuccessful housing projects. There have been propositions that the housing sector needs to supply more low-cost houses that align with customer preferences.

### **Inflation**

Saudi Arabia's inflation is driven by the over surplus production of oil leading to more money in circulation. The immediate effect of inflation is the general increase in prices including those of houses [16]. The consumer price index is affected that leads to more spending on consumer goods on investments [17]. It is therefore important that government checks and balances are implemented to curb inflation.

## **Addressing the Problem of Rising House**

### **Adoption of sustainability concepts and technology**

Despite the factors highlighted above that cause a rise in house prices, there has been efforts to provide solutions that would lead to affordable housing in the country. To start with, there has been adoption of sustainability concepts in the Saudi Arabia construction industry. Research by Taleb and Sharpless showed that most existing houses were associated with high consumption of energy and water [18]. This rendered them unsustainable [19]. Thus, going by the need to incorporate sustainability in the building sector, the research demonstrated that there was a need to design houses in a manner that it will lead to saving water and energy [20]. The proposed designs would be ultimately lead to the increased initial house purchase price. However, the high cost of purchasing the house would be compensated, in the long run, by savings in water and energy expenses.

A related study recommended that the building sector in Saudi Arabia ought to incorporate technologies that would lead to energy-saving [21]. This would work towards achieving sustainability practices that are widely accepted. The realization that the building sector contributes substantially to greenhouse emissions informed the adoption of sustainability. The research notes that the existing energy policy in Saudi Arabia provides a platform for progressive reforming in the building sector. Such policies would aid in the construction of houses that are environmentally friendly and would cost less in the long-run. The research advocates for more reforms in the building sector including the need to explore the available best practices from other parts of the world that would save energy.

Further to the study of Al-Tamimianother study emphasizes the need for the building sector to adopt energy-efficient designs to comply with sustainability practices [22]. The study specifically addressed the question of building performance simulation practice in the design stages of the construction [23]. This practice ensures that houses constructed shall save energy and water usage. Though the study found out that the practice is being used sparingly, it would aid in designing houses that would be affordable in terms of costs for energy and water. The adoption of the practice would potentially lead to innovations of the reduced cost of construction. This would translate into reduced housing costs.

The study by Dawood and Vukovic showed that the practice of incorporation energy-saving technologies in residential areas was important in as far as saving the cost of energy used for cooling [24]. The climatic conditions of most parts of Saudi Arabia are usually hot. This necessitates the use of electricity to cool houses, a practice that leads to increased

household expenses. The study showed that incorporating thermal insulation during the construction of houses would lead to saving energy. Though insulation would increase the cost of the house, the long term benefits of the reduced expense of cooling appliances and energy consumption far outweigh the initial cost.

## Idle Land Tax

The second solution to affordable houses have been the proposition of taxing idle land. This is due to the realization that there exists undeveloped land whose owners are unable to secure bank financing to construct. The tax introduced is meant to make hoarding such idle land uneconomical. The owner of such land is therefore forced to sell it [25]. With more of such lands being put in the property market, the high cost of land that translates into high housing costs is addressed.

## Crowd funding

Growing culture of crowd funding where a group of persons with a common interest of owning homes pools resources can help address the unaffordability of financing options to own a house by banks [26]. Pooled resources are used to buy land for housing. This is a new form of homeownership that is becoming more prominent. The government needs to support such initiatives by enacting legislation to streamline crowd funding. This will help address the problem of low-income residents failing to secure homeownership due to discrimination from the conventional banking system that prefers dealing with high-income earners.

## Flourishing economy

The other solution is that of the rapid expansion being witnessed in Saudi Arabia in terms of economic growth and development presents a promising future for the housing sector [27]. The flourishing economy provides opportunities for well-enumerated jobs. This translates into more people with purchasing power of land and/or houses. Economic growth would also translate into infrastructure developments that would open up new frontiers for housing development. This ensures that there is more supply of houses hence affordability.

## Growth of the micro-finance sector

Growth of the micro-finance sector in Saudi Arabia to boost the affordability of houses to low and middle-income residents can also help to address the housing price challenge in the country. The micro-finances are accommodative as compared to the conventional banks in as far as access to loan products is concerned. The micro-finances provide loans financing to purchase houses that banks could find risky. They anchor the loans on use Islamic religion and beliefs of for example waqf (trust) [28]. This aids the low-income population to own houses hence contributing towards affordable housing policies of the government.

## Slums upgrade

A project to upgrade slums in Jeddah and other urban areas can help to create affordable houses. This project exposed one of the underlying challenges of the property market in Saudi Arabia [29]. There is a disconnection when it comes to property compensation systems that aids in the acquisition of land for housing development. The slum dwellers reluctance to cede land to the government is due to unclear procedures for compensation and relocation. The effect has been that land that can accommodate a good number of housing units is left undeveloped. This creates shortages of houses in the economy thus the high house prices in these urban areas.

## Government projects

There is also the solution of government undertaking ambitious projects to bridge the shortage. Key among these projects is the King Abdullah Economic City. The city is aimed at addressing the housing shortfall that has been facing the residents over the years. Improved infrastructure in the proposed city coupled with the innovation in building cost-friendly houses, the housing deficit shall ease [30]. This project among others that the government is implementing is important in appeasing the residents through employment opportunities especially the youth who have previously participated in the Arab Springs that topples the Arab government.

The development by the government of smart cities across five cities in Saudi Arabia shall lead to increased opening up of new areas for the housing sector. The ambitious smart cities program shall include the improvement of roads and rail transport networks [31]. This will open up new areas for housing. The government intends to provide incentives to private property developers of reduced taxes would spur the housing sector. The resultant effect is the increased supply of houses that would cause the stabilization of house prices. The low-income population will benefit leading to the high uptake of house ownership in the country.

## Conclusion

In conclusion, there is need for a strong policy framework of affordable housing in the country. This shall provide a platform to strengthen the efforts curbing high house prices hence affordability. Implementation of the policy needs to be both effective and efficient. The interests' stakeholders in the housing sector need to be accommodated in the policy framework. Further, the cost aspects of policy implementation need to be efficient. This shall address the past pitfalls of weak implementation of policies that relate to housing.

The existing research on housing in Saudi Arabia has achieved in demonstrating the policy failures of the government. The government may be said to have not provided the enabling environment for the housing stakeholders to deliver affordable houses hence lower the house prices. However, there is little research on the successes of government driven initiatives such as the smart cities to deliver affordable housing. Additionally, there is need for further research on the causes of expensive technicalities of construction industry in the country. The current research trend is on the need to incorporate sustainability practices in the construction industry. This has been informed by the high costs associated with energy and water consumption.

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