

Evidence of speculative bubbles and regime switch in real estate market and crude oil price: Insight from Saudi Arabia

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INTERNATIONAL JOURNAL OF FINANCE & ECONOMICS

DOI: 10.1002/ijfe.1971

Early Access: AUG 2020

Document Type: Article; Early Access

[View Journal Impact](#)

Abstract

The sector performances of many economies especially the oil-producing ones, are consistently linked with the volatility of the international crude oil prices. Considering the significance of the international crude oil price to the economy of the Saudi Arabia, the current study investigates the dynamics of the crude oil price and the country's real estate market. This is achieved by investigating the evidence of both speculative bubbles and regime switching in the crude oil and real estate market from October 3, 2005, to March 29, 2018. As such, the Supremum Augmented Dickey-Fuller (SADF) and Markov switching regression model were employed. Although there is no significant evidence of speculative bubbles in the Saudi Arabia's real estate market, the result reveals statistical significant evidence of price bubbles in the Brent crude oil price especially between the period of 2007 to 2008, which coincides with the Global Financial Crisis period. However, the Markov switching investigation reveal that there is evidence of significant and positive impact of crude oil price return on the real estate market in the regimes. Importantly, empirical evidence shows that the impact is higher in Regime 2 even as the global factor (proxy volatility index) is evidently significant. Although the regimes are persistent, the expected regime duration of the stable regime is of the higher quarter. This investigation is statistically significant and robust, especially when Organization of the Petroleum Exporting Countries (OPEC) price of crude oil is used in lieu of the European Brent price. The estimation result encourages more strict energy policies that tackle the Saudi Arabia's energy and the real estate challenges.

Keywords

Author Keywords: [crude oil](#); [Markov switching](#); [real estate market](#); [speculative bubbles](#); [Saudi Arabia](#)

KeyWords Plus: [ECONOMIC-POLICY UNCERTAINTY](#); [TIME-SERIES](#); [HOUSING RETURNS](#); [UNIT-ROOT](#); [VOLATILITY](#)

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Publisher

WILEY, 111 RIVER ST, HOBOKEN 07030-5774, NJ USA

Categories / Classification

Research Areas: Business & Economics

Web of Science Categories: Business, Finance

Document Information

Language: English

Accession Number: WOS:000554501000001

ISSN: 1076-9307

eISSN: 1099-1158