EQUITY RESEARCH

Initiating coverage on UAE Real Estate

Headwinds easing, select opportunities emerge

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Equity Research Team

Yugesh Suneja

+971 2 305 0838

yugesh.suneja@adcb.com

Nikhil Poddar, CFA

+971 2 696 6450

nikhil.poddar@adcb.com

We initiate coverage on Emaar Properties, Emaar Malls and Aldar Properties with Buy ratings and on Damac Properties with a Sell rating. Emaar Properties is embarking on next phase of growth with solid development pipeline and expansion in retail/hotels. Emaar Malls' high quality retail assets are positioned to benefit from uptick in Dubai's tourism and emerge fairly resilient from key concerns of oversupply and e-commerce. Aldar Properties is predominantly geared to Abu Dhabi government's pace of fiscal consolidation, which we expect to ease gradually. Damac Properties lacks revenue diversification, offers low visibility and weak earnings outlook.

- **Dubai property market bottoming out, envisaging protracted recovery**
  Dubai residential property market is approaching a bottoming out phase as price declines have moderated and transactions are recovering. Steady oil prices and weakening of US$ has made Dubai less expensive for property buyers in 2017. Whilst headwinds have eased, further catalysts to lift growth are still lacking. Range bound oil prices, expected US$ strengthening and high expectations of forthcoming supply should keep a check on price growth. We therefore expect protracted property market recovery and prices to stabilize in 2018.

- **Pricing pressure to persist in Abu Dhabi, but at moderate pace**
  Abu Dhabi property market is more geared to domestic demand, which is challenged by the government's austerity measures. While constraints are unlikely to wane off in short term, we expect gradual easing of fiscal consolidation aided by steady oil prices. Moderate supply expectations should also be supportive and limit further downside. We expect the pace of decline in residential prices to moderate to -5% y-o-y in 2018E from -10% y-o-y in 2017.

- **UAE developers trading broadly in line with emerging market peers**
  UAE developers trade at a P/BV of 1.0x 2018E, 4% discount to emerging market (EM) peers. Among UAE developers, we expect Emaar Properties (P/BV of 1.1x 2018E) to command premium, powered by its high growth (14% earnings CAGR over 2016-19E). Emaar should also trade above its historical levels, supported by near term catalyst of UAE development business listing and potential for continued value unlocking on listing of other businesses. On the other hand, we see Damac's valuation (P/BV of 1.4x 2018E) as expensive (30% premium to EM peers), especially amid weak earnings outlook.

- **UAE recurring income players trade at discounted valuation**
  UAE recurring income asset owners trade at 2018E EBITDA yield of 10.2%, 310bps discount to EM peers and 480bps discount to global peers. We see current valuation discount as attractive while dividend yield at 5.6% (2018E) is also appealing. For Emaar Malls (9.3% 2018E EBITDA yield), superior earnings growth as well as potential ramp up in dividends (14% CAGR over 2017-19E) should help to narrow the discount to global peers. For Aldar (11% 2018E EBITDA yield), current valuation discount appears excessive. We expect re-rating of the stock as recurring income stabilizes in 2018E and pre-sales is sustained.

  Key risks for the sector are decline in oil prices, US$ strengthening, high upcoming supply and geopolitical uncertainty for the region.

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Fig. 1. UAE Real Estate Valuation Summary

Company	Ticker	Rating	Current price AED	Target price AED	Upside / Downside (%)	M. Cap. US$mn	P/E (x) 2017E	P/E (x) 2018E	EPS CAGR (%) 2016-19E	P/BV (x) 2017E	P/BV (x) 2018E	RoE (%) 2017E	RoE (%) 2018E	EV/EBITDA (x) 2017E	EV/EBITDA (x) 2018E	Dividend yield (%) 2017E	Dividend yield (%) 2018E
Emaar Properties	EMAAR UH	Buy	7.8	10.8	38	15,204	9.1	8.0	14	1.2	1.1	13.9	14.1	7.4	6.2	1.9	2.2
Emaar Malls	EMAARMLS UH	Buy	2.2	2.9	30	7,901	14.6	12.4	11	1.7	1.6	11.8	13.3	12.6	10.7	4.6	5.4
Aldar Properties	ALDAR UH	Buy	2.2	2.9	29	4,795	7.6	8.4	-11	0.8	0.7	10.6	8.7	9.1	9.1	5.4	5.8
Damac Properties	DAMAC UH	Sell	3.6	3.0	(17)	5,913	7.2	7.8	-9	1.5	1.4	22.8	18.8	5.5	6.0	7.0	7.0

Source: Bloomberg, ADCB Securities Equity Research Estimates.

Note: Prices as of market close on 9 November 2017

Fig. 2. Investment thesis

Company	Rating	Investment thesis	Upside case	Downside case
Emaar Properties	**Buy, TP AED10.8**	- Optimum mix of stable cash flows and earnings growth - High growth prospects driven by solid development pipeline, doubling potential of retail GLA and hotel rooms - Near term catalyst of UAE development business listing - Potential listing of other businesses to continue unlocking shareholders' value	- Sustained investor demand to keep up pre-sales momentum - New retail malls in master planned communities - Better than expected performance in international developments - Further disclosures on other unlisted businesses	- Decline in oil prices and strong momentum in US$ strengthening to impact investor demand and lead to slowdown in pre-sales - High upfront capex on new master planned communities
Emaar Malls	**Buy, TP AED2.9**	- Exposure to high quality retail assets and uptick in tourism growth - More resilient to withstand key sector concerns of oversupply and e-commerce - Growth to sustain on planned expansions - Strong dividend increase potential after expected ramp up in EBITDA over 2017-19E	- Growth in tourism spending to boost retail sales and turnover rents - Potential acquisitions of retail developments from parent Emaar Properties	- Decline in oil prices and strong momentum in US$ strengthening to constraint recovery in consumer spending - Inability to increase base rents or negotiate rent escalation on upcoming lease renewals
Aldar Properties	**Buy, TP AED2.9**	- High exposure to stable recurring income generating assets - Gradual easing of government's fiscal consolidation to ease market pressure - Contribution from expansion assets to support recurring income stabilization - Large low cost land bank allows flexibility to meet strong demand for affordable products	- Better than expected recovery in property market rents - Strong pre-sales driven by mid-income focus	- Prolong oil price decline is likely to have a negative impact on property market in Abu Dhabi - Higher upfront capex on new master planned communities or government projects
Damac Properties	**Sell, TP AED3.0**	- Exposed to volatility in earnings due to lack of revenue diversification towards recurring income - Weak earnings outlook - Expensive valuation factoring aggressive pre-sales growth and significant land bank acquisition	- Better than expected recovery in property market driving higher pre-sales and increase in selling prices - Large land acquisitions on favourable payment terms	- Decline in oil prices and strong momentum in US$ strengthening to impact investor demand and lead to slowdown in pre-sales - Lower than expected cash collections from customers

Source: ADCB Securities Equity Research.

Fig. 3. Regional and Global Real Estate Developers' Valuation Comparable

	M. Cap.	EV	P/E (x)			EPS CAGR (%)	P/BV (x)			RoE (%)			EV/EBITDA (x)			Dividend yield (%)		
	US$mn	US$mn	2017E	2018E	2019E	2016-19E	2017E	2018E	2019E	2017E	2018E	2019E	2017E	2018E	2019E	2017E	2018E	2019E
Emaar Properties	15,204	17,415	9.1	8.0	7.1	14	1.2	1.1	0.9	13.9	14.1	14.1	7.4	6.2	5.2	1.9	2.2	2.2
Damac Properties	5,913	5,034	7.2	7.8	7.8	(9)	1.5	1.4	1.3	22.8	18.8	17.2	5.5	6.0	5.9	7.0	7.0	7.0
Aldar Properties	4,795	4,729	7.6	8.4	9.1	(11)	0.8	0.7	0.7	10.6	8.7	7.7	9.1	9.1	10.0	5.4	5.8	6.3
UAE			**7.5**	**7.8**	**7.7**	**(0)**	**1.1**	**1.0**	**0.9**	**13.1**	**13.3**	**13.6**	**7.4**	**7.5**	**6.9**	**5.0**	**5.4**	**6.0**
Saudi Arabia			51.2	32.9	16.4	46	0.9	0.8	NM	1.7	2.4	2.9	39.9	30.6	16.8	NM	NM	NM
Egypt			12.0	9.0	7.1	28	1.4	1.2	1.0	12.1	14.6	14.9	12.6	9.6	8.5	NM	NM	NM
MENA			**11.2**	**9.0**	**7.4**	**23**	**1.2**	**1.1**	**0.9**	**11.4**	**13.3**	**13.8**	**11.9**	**8.5**	**7.8**	**NM**	**NM**	**NM**
Turkey			5.7	4.5	5.0	5	0.8	0.8	0.6	16.9	17.6	18.7	5.8	4.6	4.2	6.9	8.3	9.3
Russia			8.1	6.1	5.5	42	1.4	1.2	1.2	16.9	16.1	16.8	7.2	4.8	4.8	4.6	6.7	9.3
India			29.8	23.7	19.7	30	2.4	2.1	1.9	9.9	11.1	12.2	14.7	12.4	11.2	0.6	0.6	0.7
China & Hong Kong			13.6	13.0	11.8	11	0.7	0.6	0.6	5.6	5.1	5.5	11.4	11.0	10.2	3.3	3.6	4.0
Emerging Markets (EM)			**12.8**	**11.9**	**9.9**	**16**	**1.2**	**1.1**	**0.9**	**11.4**	**13.2**	**13.0**	**11.6**	**10.8**	**9.2**	**2.1**	**2.7**	**3.1**
USA			14.8	12.9	11.3	16	1.6	1.7	1.3	12.0	11.7	11.2	10.8	9.1	9.0	0.2	0.2	0.2
UK & Europe			9.5	9.7	8.7	8	1.8	1.7	1.6	21.3	19.7	19.2	7.0	6.9	6.6	4.5	4.6	5.2
Global			**12.8**	**11.2**	**10.1**	**12**	**1.5**	**1.3**	**1.2**	**13.0**	**14.6**	**14.6**	**10.7**	**9.0**	**8.8**	**1.7**	**2.4**	**2.8**

Source: Bloomberg, ADCB Securities Equity Research.

Note: Market data as of 9 November 2017. Bloomberg consensus estimates have been used for non-covered companies.

Fig. 4. Global Recurring Income Asset Owners' Valuation Comparable

	M. Cap.	EV		P/E (x)		EPS CAGR (%)		P/BV (x)			RoE (%)			EBITDA yield (%)			Dividend yield (%)	
	US$mn	US$mn	2017E	2018E	2019E	2016-19E	2017E	2018E	2019E	2017E	2018E	2019E	2017E	2018E	2019E	2017E	2018E	2019E
Emaar Malls	7,901	9,042	14.6	12.4	11.2	11	1.7	1.6	1.5	11.8	13.3	14.0	7.9	9.3	10.5	4.6	5.4	6.0
Aldar Properties	4,795	4,729	7.6	8.4	9.1	(11)	0.8	0.7	0.7	10.6	8.7	7.7	11.0	11.0	10.0	5.4	5.8	6.3
UAE			**11.1**	**10.4**	**10.2**	**0**	**1.2**	**1.2**	**1.1**	**11.2**	**11.0**	**10.9**	**9.5**	**10.2**	**10.3**	**5.0**	**5.6**	**6.2**
Brazil			34.8	23.0	18.9	36	1.9	1.8	1.7	5.5	7.5	8.6	5.9	6.9	7.6	1.0	1.7	2.6
South Africa			13.1	12.2	11.5	4	1.0	0.9	0.9	8.0	8.2	7.9	6.8	7.2	7.0	7.7	8.2	8.3
Malaysia			19.0	18.2	17.9	(3)	1.2	1.2	1.2	6.6	7.0	7.1	5.0	5.3	5.5	5.2	5.5	5.7
Emerging Markets (EM)			**17.7**	**17.3**	**15.2**	**4**	**1.2**	**1.2**	**1.2**	**7.9**	**8.0**	**7.9**	**6.3**	**7.1**	**6.8**	**4.9**	**5.8**	**6.1**
Singapore			18.6	17.8	17.7	2	1.1	1.1	1.1	6.0	6.0	5.9	4.5	4.6	4.6	5.6	5.7	5.7
Hong Kong			20.1	19.8	20.1	3	0.7	0.7	0.7	3.7	3.7	3.4	4.8	4.9	5.0	3.6	3.9	4.1
USA			37.7	39.1	37.5	(14)	1.8	1.9	2.2	5.7	6.8	8.1	5.9	6.2	6.2	5.2	5.4	5.5
UK & Europe			16.8	16.4	15.9	5	0.7	0.8	0.9	4.1	4.3	4.9	4.9	5.0	5.2	5.0	5.2	5.4
Global			**19.5**	**18.7**	**18.7**	**3**	**1.1**	**1.1**	**1.1**	**5.8**	**6.1**	**6.0**	**5.2**	**5.3**	**5.5**	**5.1**	**5.2**	**5.4**

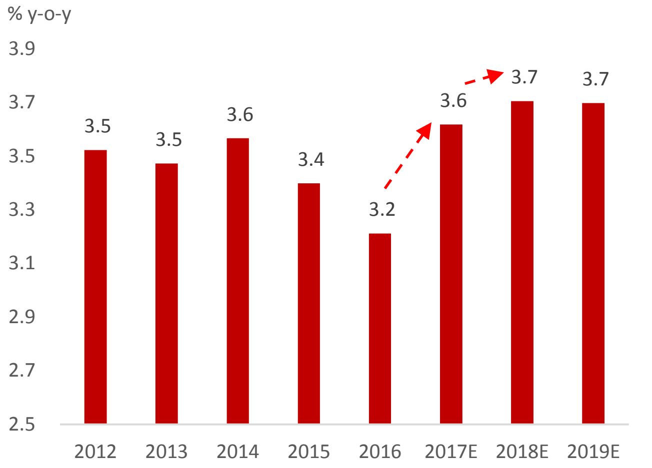
Source: Bloomberg, ADCB Securities Equity Research.

Note: Market data as of 9 November 2017. Bloomberg consensus estimates have been used for non-covered companies.

UAE in a unique position to benefit from global growth

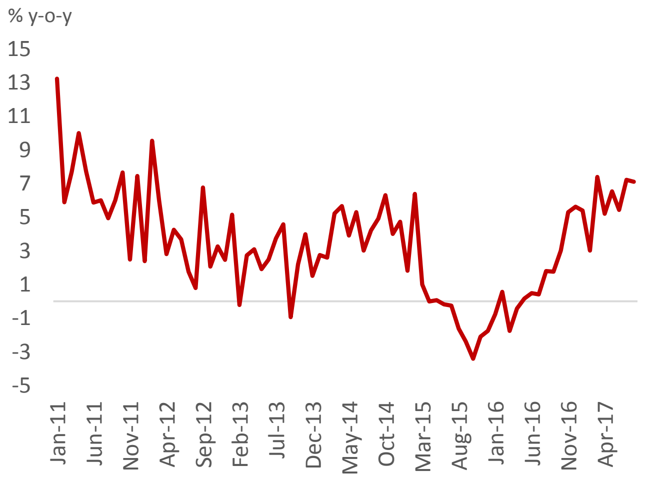
IMF forecasts a broad uptick in the world economy with global growth of 3.6% in 2017E and 3.7% in 2018E, up from 3.2% in 2016. Acceleration of the world economy should result in greater global trade and tourism activity. UAE being a relatively diversified economy and a key trading/tourism hub is expected to benefit from rebound in world trade flows and growth in global tourism.

Fig. 5. World GDP growth picking up



Source: IMF, ADCB Securities Equity Research.

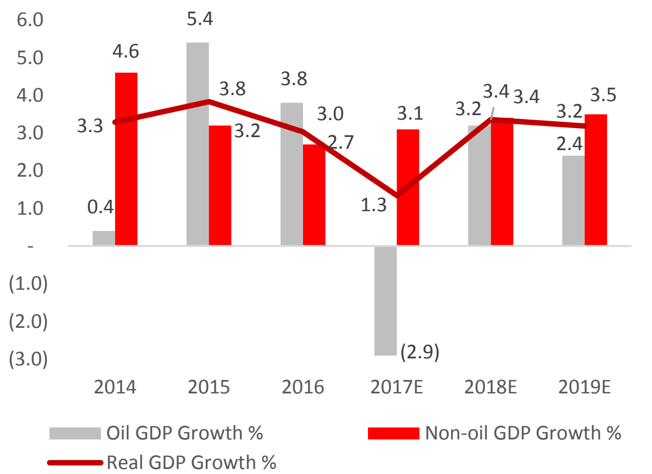
Fig. 6. Global container* growth also on the rise



Source: Institute of Shipping Economics and Logistics, ADCB Securities Equity Research. *Data coverage ~60% of global container throughput

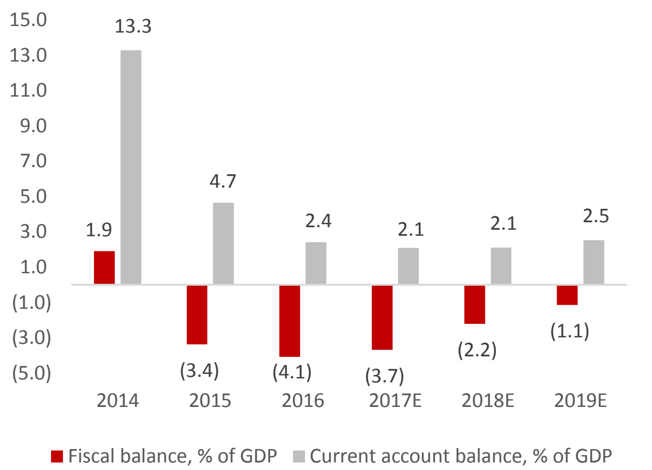
IMF expects UAE real GDP growth to fall to 1.3% in 2017E from 3.0% in 2016. The key reason for lower growth is decline in oil GDP by 2.9%, which is largely due to UAE's commitment to OPEC production cuts. Non-oil GDP is expected to see acceleration to 3.1% in 2017 (from 2.7% in 2016) and then improve further to 3.4% in 2018. Going forward, UAE economy is expected to improve on the back of stable oil prices, increase in Expo 2020 related investments, pick up in global growth and gradual easing of fiscal consolidation.

Fig. 7. UAE GDP growth to suffer from decline in oil GDP in 2017E, Non-oil GDP to strengthen over 2017/18E



Source: IMF, ADCB Securities Equity Research.

Fig. 8. UAE fiscal and current account balance expected to improve moving forward



Source: IMF, ADCB Securities Equity Research.

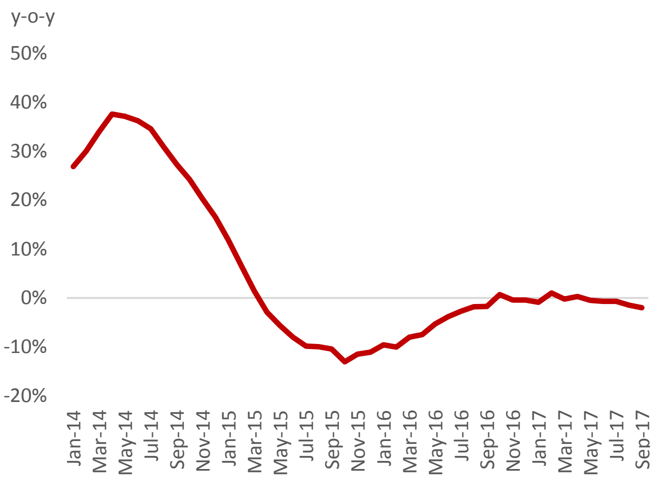
Dubai residential property market: expecting protracted recovery

Dubai residential property market is approaching a bottoming out phase as price declines have moderated, transactions are recovering and supply is kept in check to meet demand growth. Dubai property market is largely geared to foreigners, including GCC and other international buyers. Oil prices and US$ are thus key factors driving sentiment of Dubai property buyers. 2017 has turned out to be favorable for foreign demand as oil prices recovered and US$ weakened against major currencies.

Whilst headwinds have eased, we do not see further catalysts to move prices back to growth trajectory. As per IMF forecast, oil prices are expected to stay near US$55 over next two years. So, sentiment of buyers from UAE/other GCC countries is likely to remain tepid, limiting further uptick in demand. Secondly, US$ is likely to strengthen in medium term as Fed maintains its tightening policy, though at more gradual pace than initial expectations. This should leave limited scope for higher demand from major buyer countries like India, UK, Europe. Thirdly, surging supply risks had been curbed until now, nevertheless supply overhang should keep a check on price growth.

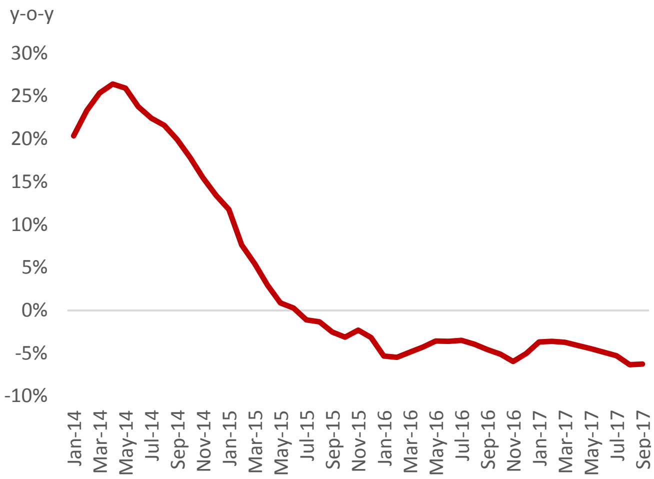
We therefore expect Dubai property market to see a protracted recovery, unlike previous cycles. Price correction in current cycle had been more moderate and y-o-y price decline has been modest since end of 2016. The main reasons we see elongated stabilization phase are: **1/** Dubai's property market is becoming more mature. Regulations have improved with focus on protecting buyers' rights and also discourage flipping. This makes a strong case to attract investors with long term view of capital appreciation or high rental yields. **2/** Sustainability of foreign investors' demand also hinges upon resident population needs of rental housing. Dubai residential rents are continuing to witness declines as job market remains fragile. Pick up in non-oil GDP growth and Expo 2020 related investment should be supportive for the economic growth. But the real impact on the ground could take time to create a more positive sentiment among corporates and their hiring decisions. Hence, improvement in employment prospects and domestic demand are likely to be gradual. We expect Dubai residential prices to stabilize in 2018E after modest decline of 5% y-o-y in 2017.

Fig. 9. Dubai residential selling price change – modest price declines of 1-2% since end of 2016



Source: REIDIN, ADCB Securities Equity Research.

Fig. 10. Dubai residential rent change – rental decline persists at a moderate pace

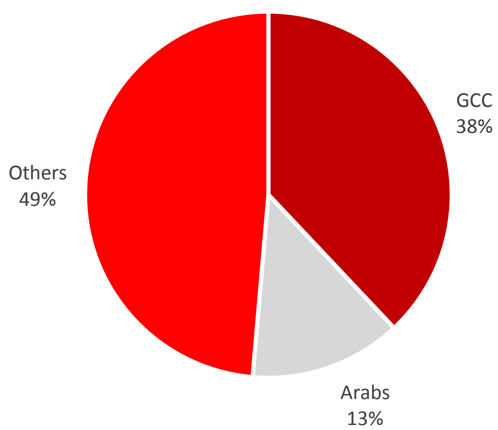


Source: REIDIN, ADCB Securities Equity Research.

Demand drivers for Dubai property: Oil and US$ key factors

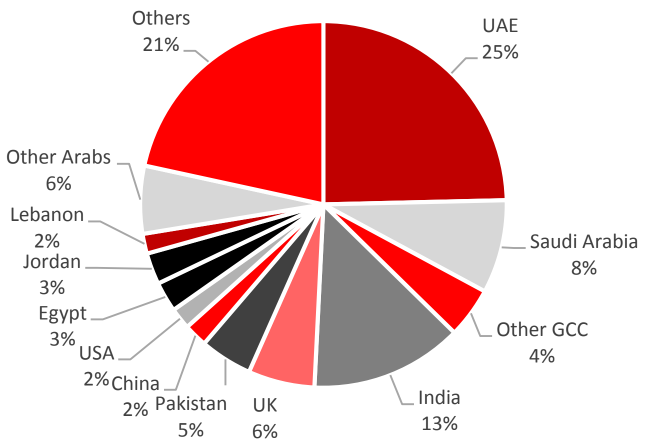
Dubai residential property market is mainly driven by foreigners (75% of Dubai property buyers). The two key categories of foreign buyers are: **1/** oil dependent GCC countries and **2/** Asian/European countries exposed to exchange rate fluctuations against US$. Among foreign buyers, major ones are from India (13%), Saudi (8%), UK (6%) and Pakistan (5%).

Fig. 11. Dubai property buyers by regions: 2016-1H17



Source: Dubai Land Department, ADCB Securities Equity Research.

Fig. 12. Dubai property buyers by nationality: 2016-1H17

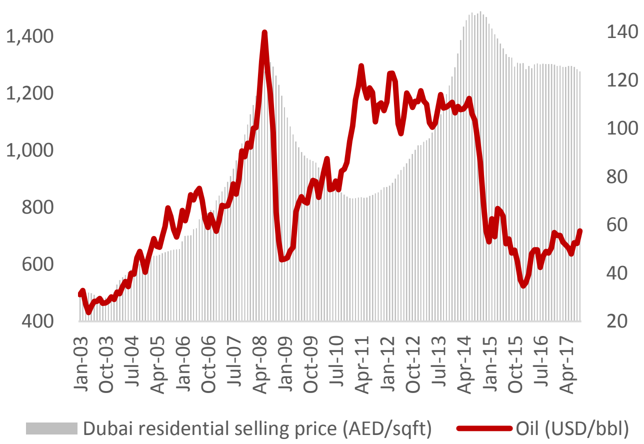


Source: Dubai Land Department, ADCB Securities Equity Research.

Buying demand from GCC countries (38% of total buyers) had been impacted in 2015-16 as lower oil prices curtailed government spending, hampering consumer/investor demand. For another major group of buyers i.e. India, UK, Pakistan, China (27% of total buyers), US$ strengthening against their currencies had made Dubai property more expensive.

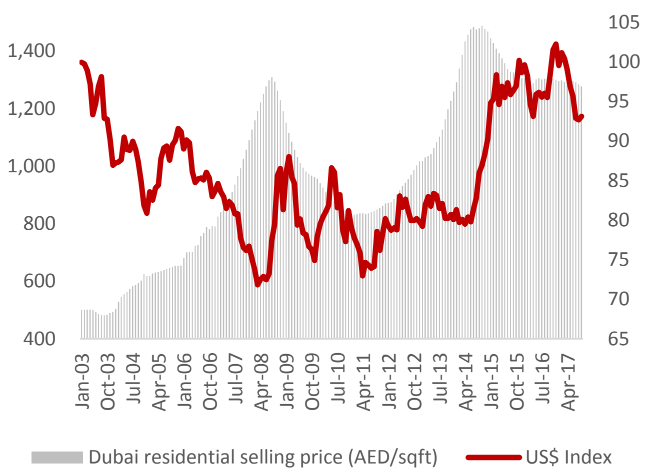
However, YTDSept2017 has seen firming up of oil prices and weakening of US$ by ~10%. This has improved sentiment of foreign buyers towards Dubai property market and supported stabilization in property prices.

Fig. 13. Dubai property prices evolution vs. oil prices – recent firmness in oil supportive of property prices



Source: REIDIN, Bloomberg, ADCB Securities Equity Research.

Fig. 14. Dubai property prices evolution vs. US$ – US$ weakening by ~10% YTD2017 also aided property prices



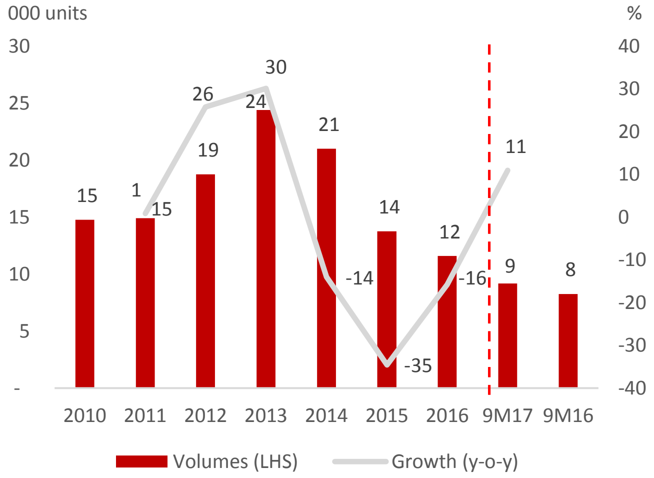
Source: REIDIN, Bloomberg, ADCB Securities Equity Research.

Transactions have recovered in 2017

Secondary market activity has picked up…

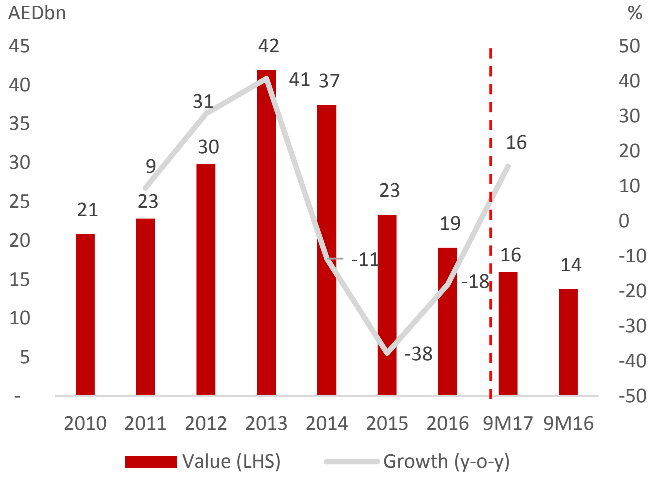
Dubai residential secondary market transactions (completed properties) have recovered in 2017 after three consecutive years of decline over 2014-16. In 9M17, Dubai residential secondary transactions are up 11% y-o-y in volumes and 16% y-o-y in value terms.

Fig. 15. Dubai secondary transactions (completed properties) by volumes



Source: REIDIN, ADCB Securities Equity Research.

Fig. 16. Dubai secondary transactions (completed properties) by value

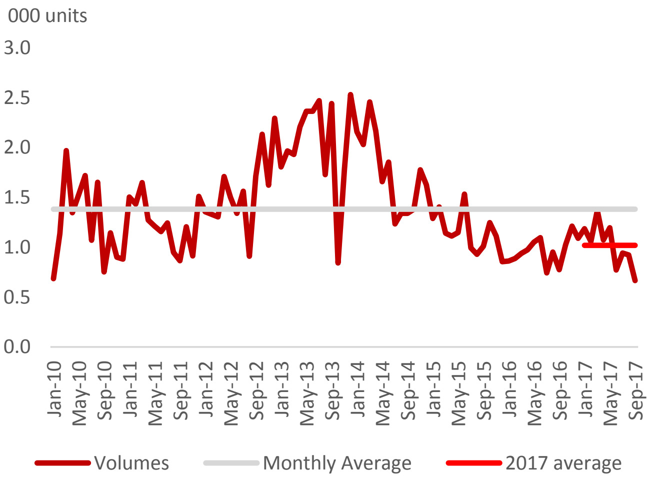


Source: REIDIN, ADCB Securities Equity Research.

…however, it is still below historical levels

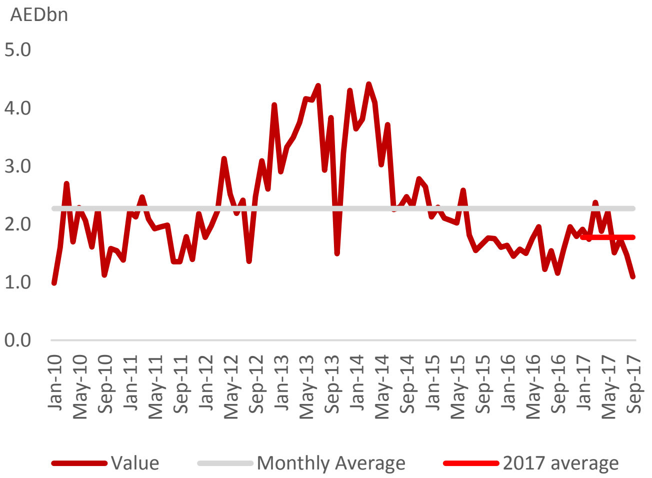
While secondary market transactions are returning to growth, they still remain ~25% below historical average. This indicates investors are still cautious towards Dubai property market.

Fig. 17. Dubai secondary transactions by volumes – 9M17 26% below historical average



Source: REIDIN, ADCB Securities Equity Research.

Fig. 18. Dubai secondary transactions by value – 9M17 22% below historical average

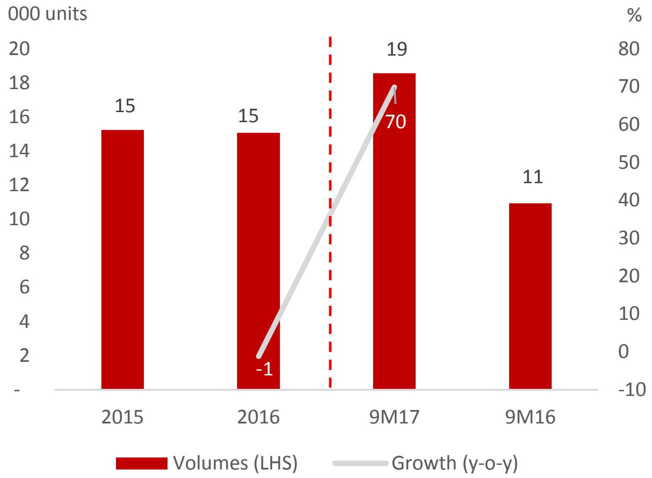


Source: REIDIN, ADCB Securities Equity Research.

Off plan transactions powering the market

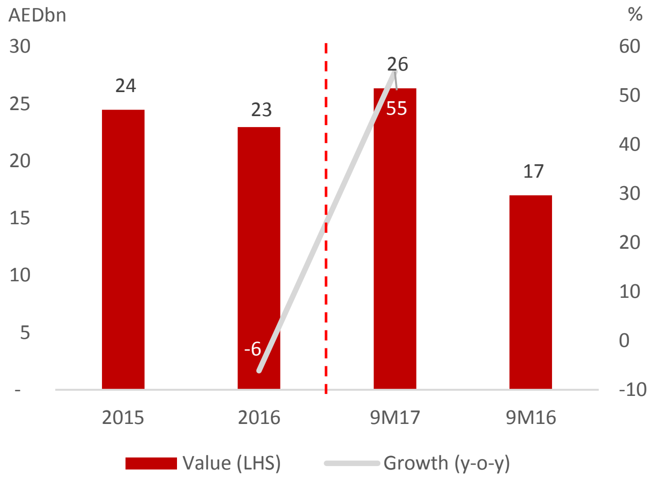
Dubai residential off-plan transactions (under construction properties) have shown a much stronger growth in 9M17 with volumes up 70% y-o-y and value up 55% y-o-y. Off-plan transactions accounted for ~60% of Dubai's total residential transactions in 9M17. Strong pre-sales achieved by leading Dubai developer Emaar Properties played a key role in driving Dubai's off-plan market. As per REIDIN's off-plan transaction data and Emaar's reported pre-sales, Emaar's market share increased to 35% by volumes and 58% by value in Dubai's off-plan market in 9M17 (from estimated 29% in 2016 and 22% in 2015 by volume). Including secondary market transactions, Emaar had a market share of 24% by volumes and 36% by value during 9M17 in Dubai's residential market.

Fig. 19. Dubai off-plan transactions (under construction properties) by volumes



Source: REIDIN, ADCB Securities Equity Research.

Fig. 20. Dubai off-plan transactions (under construction properties) by value



Source: REIDIN, ADCB Securities Equity Research.

Supply expectations rising, likely to be kept in check similar to past

As per Dubai Statistics Centre data, number of households in Dubai have increased at a CAGR of 7.6% over 2011-16. This is higher than 2.9% CAGR in housing stock. Lag in unit deliveries vs. expectations had kept the demand supply dynamics favorable. Deliveries have been delayed in the past due to construction/municipality approvals or developers have prudently kept a check on deliveries to avoid over supply conditions.

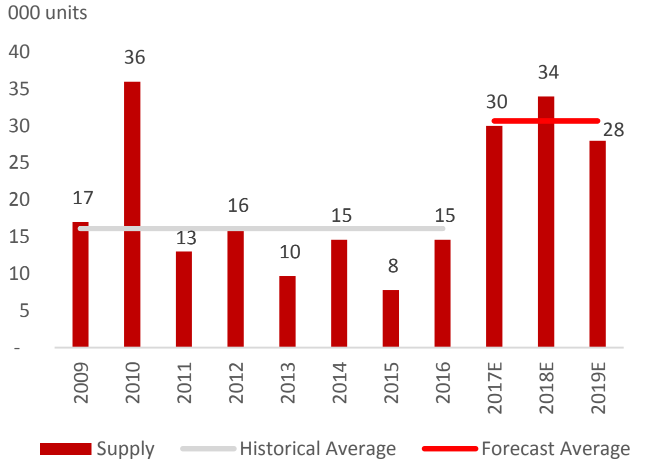
Fig. 21. Dubai housing demand supply dynamics in last five years

	2011	2012	2013	2014	2015	2016	CAGR (2011-16)
Total population (Nos.)	2,003,170	2,105,875	2,213,845	2,327,350	2,446,675	2,698,600	6.1%
Addressable* population (Nos.)	1,355,374	1,458,079	1,566,049	1,624,509	1,724,198	1,933,647	7.4%
Addressable* households (Nos.)	**309,093**	**332,515**	**357,773**	**389,028**	**413,310**	**446,570**	**7.6%**
Annual demand (change in households) – units		23,422	25,258	31,255	24,282	33,260	
Housing stock (units)	**408,300**	**424,300**	**434,000**	**448,600**	**456,400**	**471,000**	**2.9%**
Annual supply (change in housing stock) - units		16,000	9,700	14,600	7,800	14,600	

Source: Dubai Statistics Centre, JLL, ADCB Securities Equity Research.
* Addressable market excludes population living in collective housing, labour camps etc.

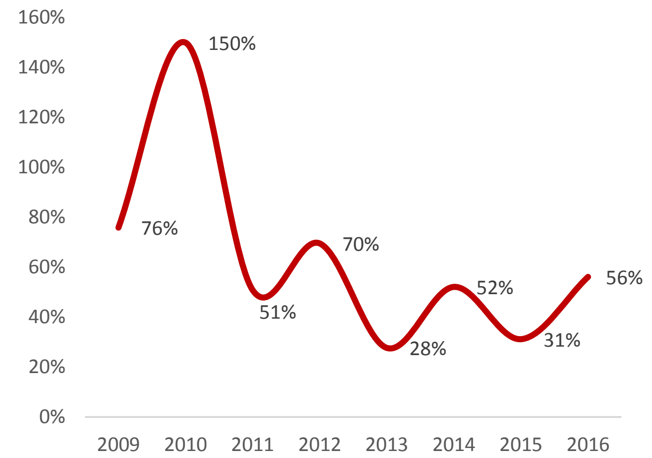
Going forward, JLL supply forecast indicates surge in Dubai unit deliveries over 2017-19E. JLL estimates an increase in Dubai residential stock by 92k units over 2017-19E. This represents an annual increase of ~31k units or 91% higher than historical average supply.

Fig. 22. Dubai annual residential supply – under construction pipeline points to significant increase



Source: : JLL, ADCB Securities Equity Research.

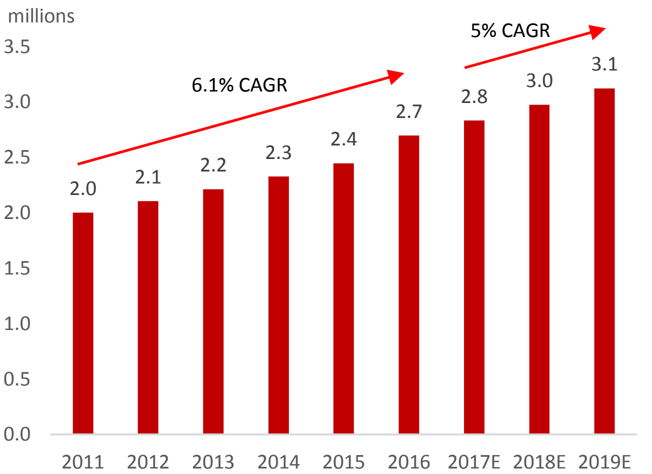
Fig. 23. Actual supply realization had lagged forecast in the past-average realization rate stood at 62% in Dubai



Source: JLL, ADCB Securities Equity Research.

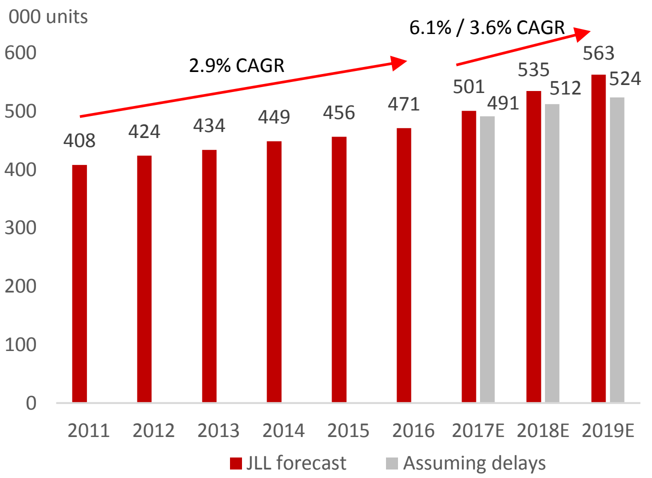
Assuming JLL estimated supply, housing stock in Dubai is likely to increase by 6.1% p.a. over 2016-19E. This increase in supply can be still absorbed if population grows in line with last five years. In the past, actual supply realization had been 62% of forecast. If realization rates are maintained going forward, housing stock is likely to increase at 3.6% CAGR or lower than expected population growth.

Fig. 24. Dubai population – expecting 5% CAGR in next three years vs. 6% in last five years



Source: Dubai Statistics Centre, ADCB Securities Equity Research Estimates.

Fig. 25. Dubai housing stock – base case scenario points to growth broadly in line with population growth



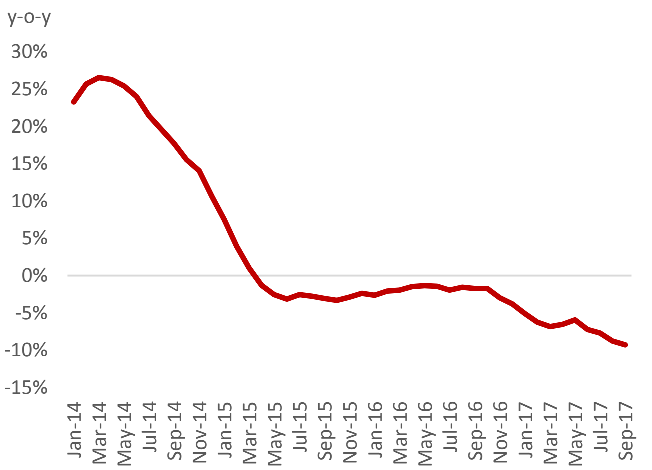
Source: JLL, ADCB Securities Equity Research.

Abu Dhabi residential property market: pricing pressure to persist but at moderate pace

Historically, Abu Dhabi property market lagged Dubai in both recovery and decline phases. Abu Dhabi residential property prices and rent decline accelerated in 2017 while Dubai property market is seeing a moderate drop now.

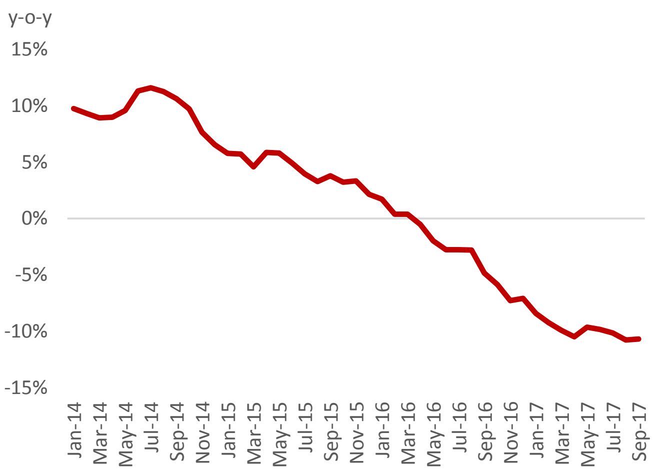
Abu Dhabi property market is less dependent on foreign investors and is more geared to resident population. Given Abu Dhabi's higher exposure to oil, domestic demand was hit by government's spending cuts, lower economic growth, increased job losses/wage pressure and greater uncertainty for residents. Given the constraints are unlikely to wane off in short term, we see its property market to take longer to stabilize in this cycle. We expect Abu Dhabi residential prices to continue to decline in 2018E (-5% y-o-y) but at lower pace than 2017 (-10% y-o-y). Modest residential supply expectations and easing of government's austerity measures should alleviate concerns and limit further downside in 2018E.

Fig. 26. Abu Dhabi residential selling price change – fall accelerated in 2017



Source: REIDIN, ADCB Securities Equity Research.

Fig. 27. Abu Dhabi residential rent change – declining at higher rate in 2017 but pace of decline stabilized

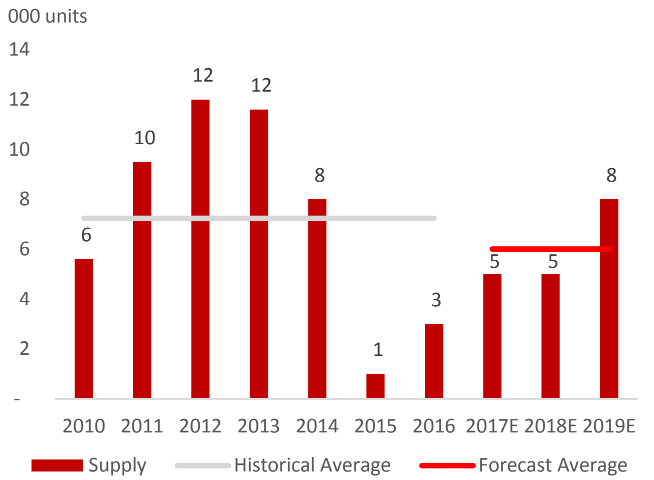


Source: REIDIN, ADCB Securities Equity Research.

Supply expectations picking up but below historical levels

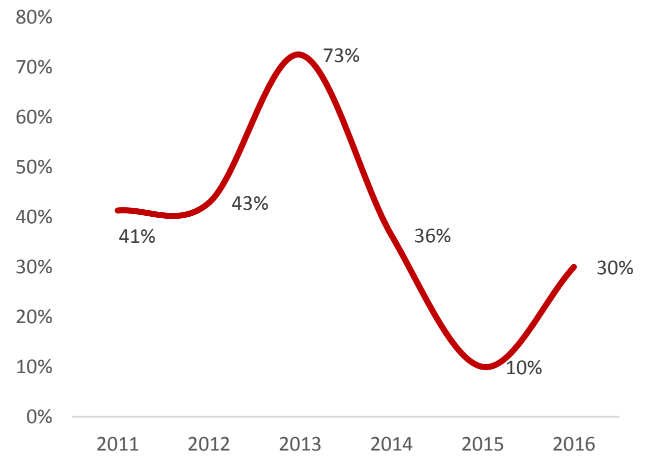
In Abu Dhabi, JLL estimates increase in residential stock by 19k units over 2017-19E. This is a modest increase compared to Dubai and represents an annual increase of ~6.3k units or 12% below historical average supply.

Fig. 28. Abu Dhabi annual residential supply – under construction pipeline below historical levels



Source: JLL, ADCB Securities Equity Research.

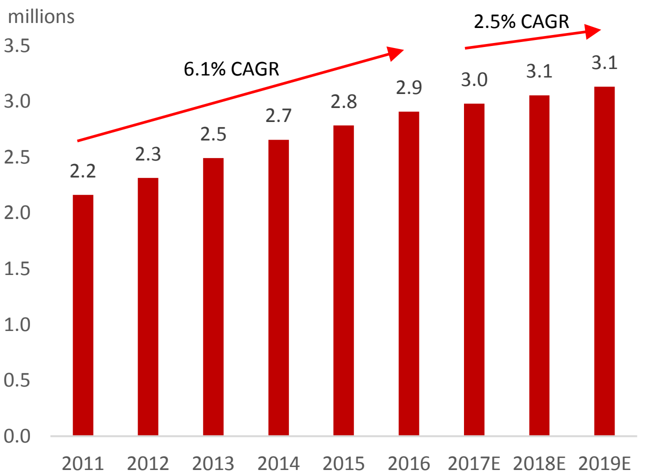
Fig. 29. Actual supply realization had lagged forecast - average realization rate stood at 47% in Abu Dhabi



Source: JLL, ADCB Securities Equity Research.

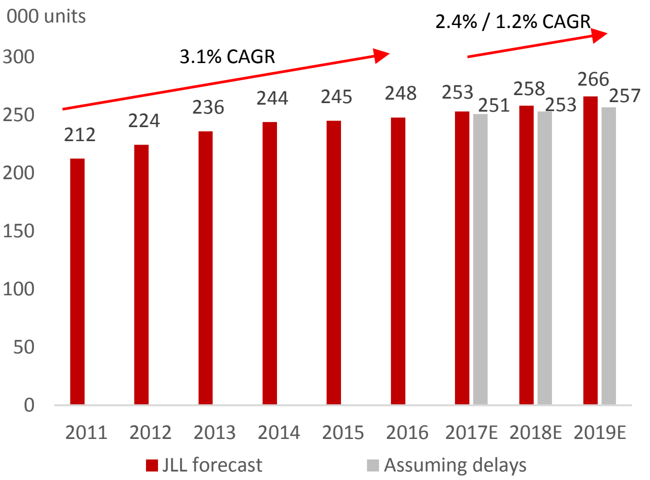
Assuming JLL estimated supply, housing stock in Abu Dhabi is likely to increase by 2.4% p.a. over 2016-19E. This increase in supply can be absorbed even if population growth halves from last five years' level. Moreover, if realization rates are maintained at ~50% as in the past, housing stock is likely to increase at 1.2% CAGR or lower than population growth.

Fig. 30. Abu Dhabi population – expecting 2.5% CAGR in next three years vs. 6.1% in last five years



Source: Statistics Centre Abu Dhabi, ADCB Securities Equity Research Estimates.

Fig. 31. Abu Dhabi housing stock – base case scenario points to growth in line with population growth

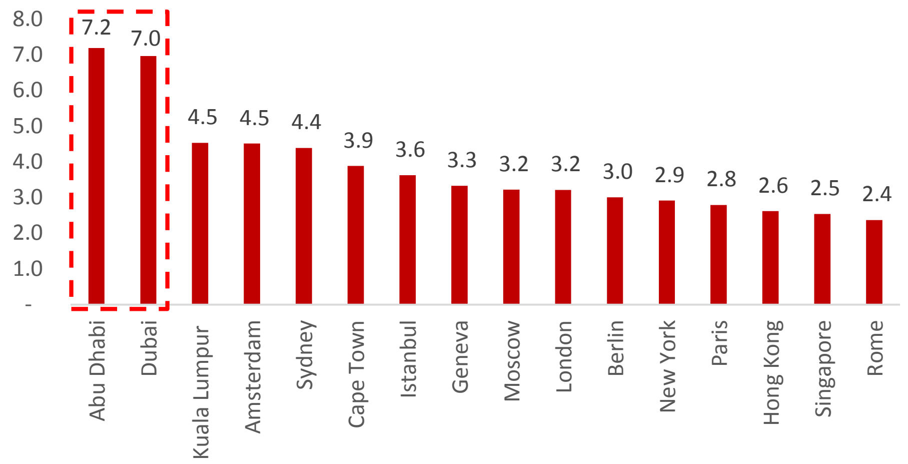


Source: JLL, ADCB Securities Equity Research.

UAE property yields attractive vs. global markets

Dubai and Abu Dhabi offer highest residential yields among key global cities. This makes these property markets attractive to invest in compared to other global cities. Apart from high yields, Dubai's safe haven status, strong tourism proposition, well developed infrastructure, connectivity and currency peg to USD add to the appeal. High yields should support UAE property markets to maintain investors' interest even in absence of capital appreciation expectations.

Fig. 32. Dubai and Abu Dhabi offer highest gross residential yields among global cities

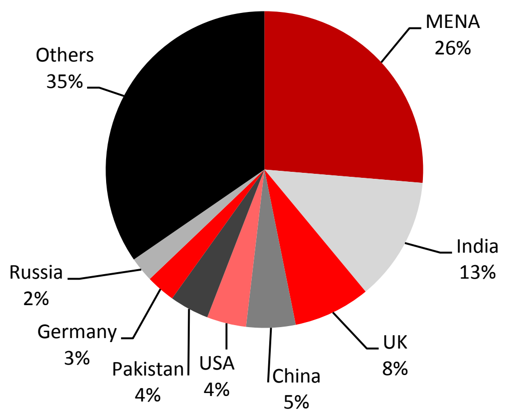


Source: Global Property Guide, ADCB Securities Equity Research.

Retail sector: easing of headwinds

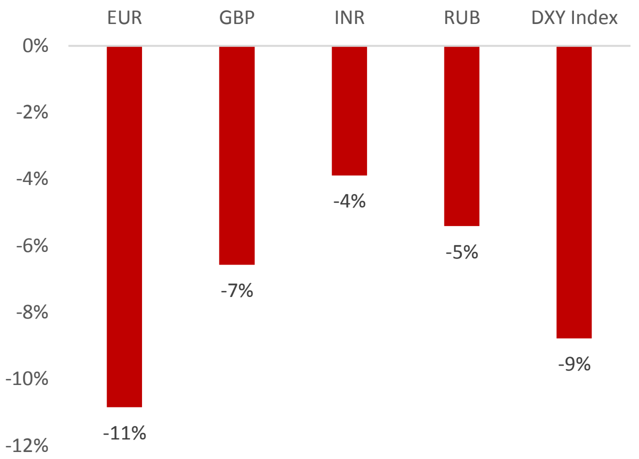
Tourism, in addition to population demand, plays a key role in driving Dubai's retail sector. Tourism growth has picked up in YTDAug2017 to 8.6% y-o-y after slowing down to 4.9% y-o-y in 2016. USD weakening has made Dubai less expensive for tourists from India, UK, Europe etc., which account for top source markets for Dubai tourism. Dubai government's initiative of allowing visa on arrival for Chinese and Russian visitors has boosted growth of visitors from these countries.

Fig. 33. Dubai tourists by nationality – YTDAug2017



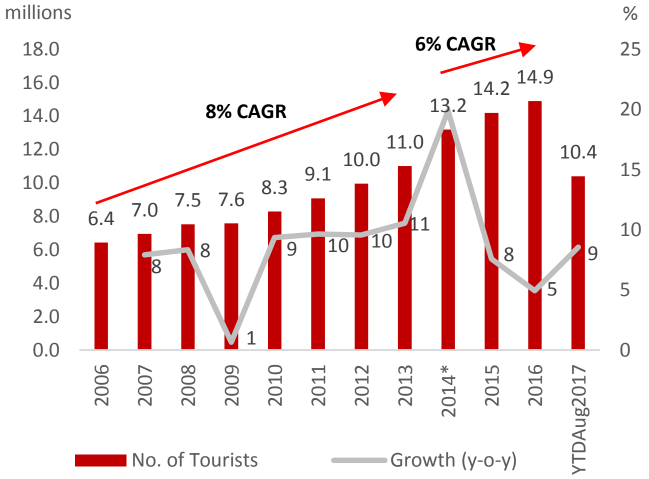
Source: Dubai Department of Tourism and Commerce Marketing.

Fig. 34. YTDSept2017 US$ performance against major currencies



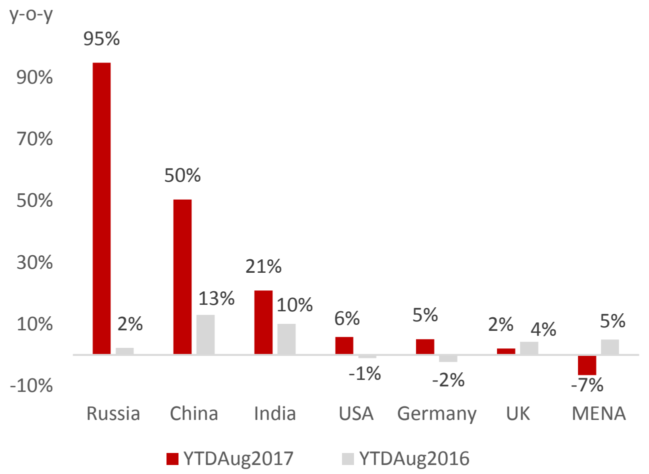
Source: Bloomberg, ADCB Securities Equity Research.

Fig. 35. Dubai tourists growth recovered in YTDAug17 to 8.6%



Source: Dubai Department of Tourism and Commerce Marketing.
* 2014 onwards, tourists numbers include friends and relatives

Fig. 36. YTDAug2017 tourism growth by main countries/region



Source: Dubai Department of Tourism and Commerce Marketing.

Going forward, improving global growth prospects bode well to lift tourism performance. Tourists from MENA region continued to decline YTDAug2017, but stable oil prices and gradual easing of GCC governments' austerity drive should limit further downside. Saudi government has already reinstated bonuses for public sector employees in April 2017. Recently, Saudi Arabia's Finance Minister indicated that the country will slow down on pace of reforms in line with IMF recommendations.

Higher supply and e-commerce key risks to retailers' performance

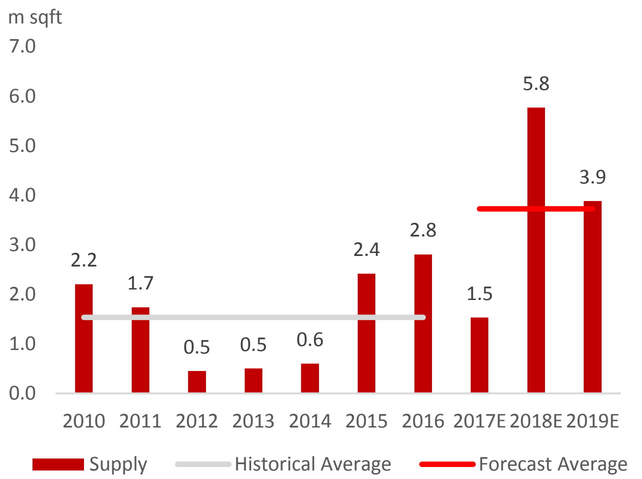
While headwinds have eased for retail sector, resident population consumption and tourism spending are likely to remain challenged by continued low oil price environment and risk of US$ strengthening. We therefore remain cautious on demand growth going forward. Amid subdued demand, higher upcoming supply and rising e-commerce penetration are key risks that could keep a check on recovery in retailers' sales performance.

Retail supply accelerating in Dubai…

As per JLL forecast, retail supply is expected to gather pace in Dubai over 2017-19E. JLL estimates rise in Dubai retail stock by 11.2m sqft in next three years. This represents an annual increase of 3.7m sqft or 2.4x higher than historical average supply of 1.53m sqft p.a. Alternatively, retail supply equivalent to one Dubai Mall will be added every year till 2019E. Unlike residential supply, actual supply realization rate for Dubai's retail sector is higher at 83% of forecast.

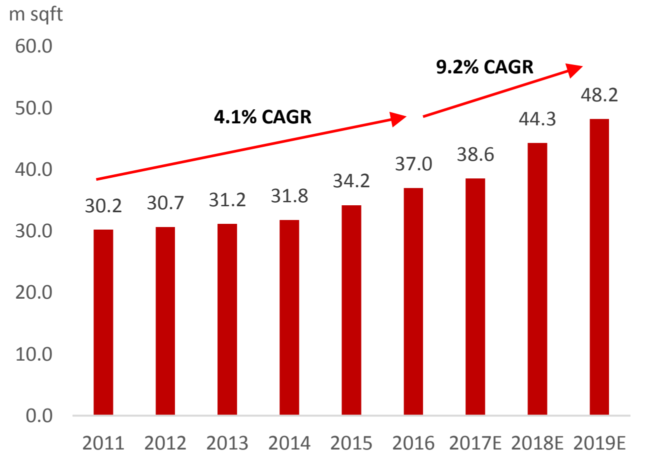
Assuming JLL estimated supply, retail stock in Dubai would increase by 9.2% p.a. over 2016-19E. This is higher than our expectations of population growth of ~5% as well as Dubai government's implied tourist growth of 7.6% p.a. (to reach 20m tourists by 2020).

Fig. 37. Dubai annual retail supply –significant increase expected



Source: JLL, ADCB Securities Equity Research.

Fig. 38. Dubai retail stock – expected increase in retail stock higher than estimated population/tourist growth



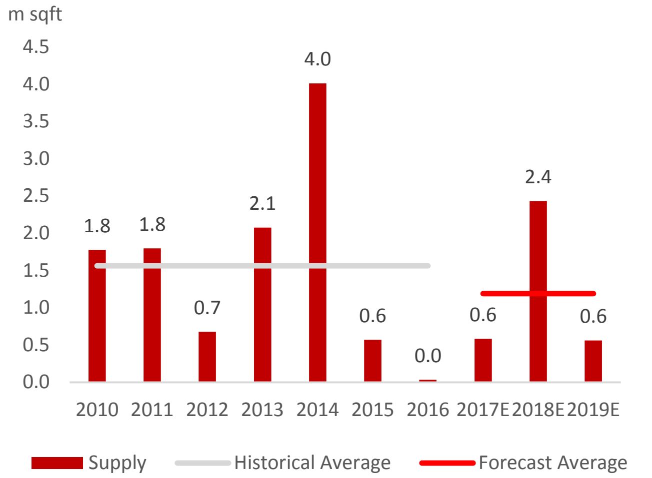
Source: JLL, ADCB Securities Equity Research.

…however, below historical levels in Abu Dhabi

For Abu Dhabi, JLL estimates an increase in retail stock by 3.57m sqft over 2017-19E. This represents an annual increase of 1.2m sqft or 24% below historical average supply of 1.56m sqft p.a. Moreover, actual supply realization rate for Abu Dhabi's retail sector is still low at 53% of forecast.

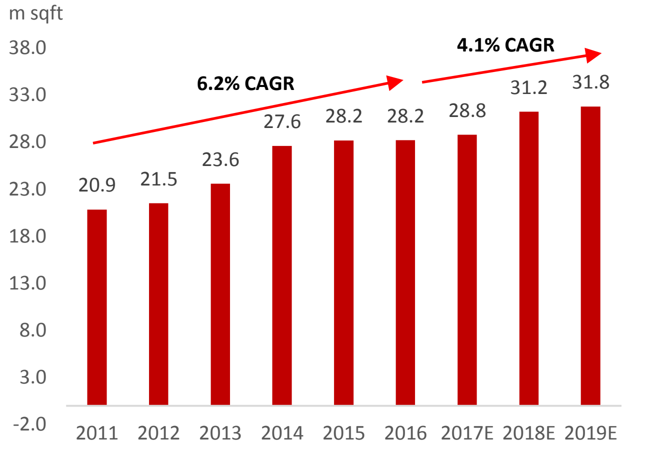
Assuming JLL estimated supply, retail stock in Abu Dhabi would increase by 4.1% p.a. over 2016-19E. This is slightly higher than our expectations of population growth of ~2.5%.

Fig. 39. Abu Dhabi annual retail supply –expected increase in supply below historical levels



Source: JLL, ADCB Securities Equity Research.

Fig. 40. Abu Dhabi retail stock – expected increase in retail stock slightly higher than estimated population growth

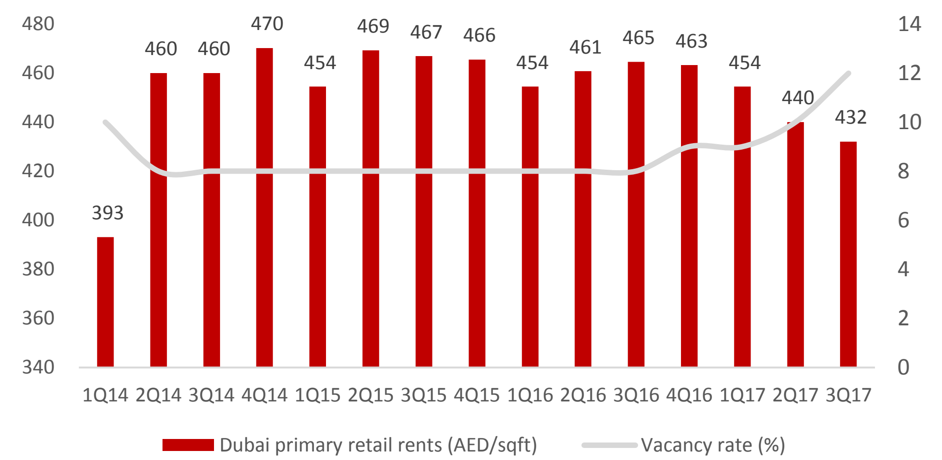


Source: JLL, ADCB Securities Equity Research.

Retail rents begin to fall albeit with a lag

Despite challenging retail market conditions, retail rents remained broadly stable in Dubai and Abu Dhabi over 2015-16. However, latest JLL data indicates correction of 7% in Dubai retail rents in 9M17. Given nature of medium to long term contracts in commercial sector, there appears to be a lag in rental correction. Current data would be better reflection of demand as leases are renewed. Vacancies have also moved up in Dubai, driven by combination of higher supply and retail sector challenges. In Abu Dhabi, retail rents and vacancies have remained firm at AED280/sqft and 2% respectively. However, there is increasing trend of other incentives being offered by landlords of malls like flexible lease terms, early break clause, rent free periods etc.

Fig. 41. Dubai retail rents started to witness correction, vacancy rates also moved up in 9M17

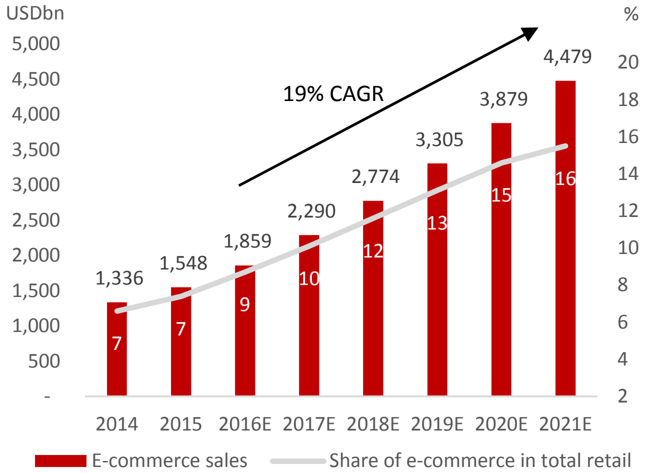


Source: JLL, ADCB Securities Equity Research.

Rising e-commerce penetration key challenge for store based retail sales

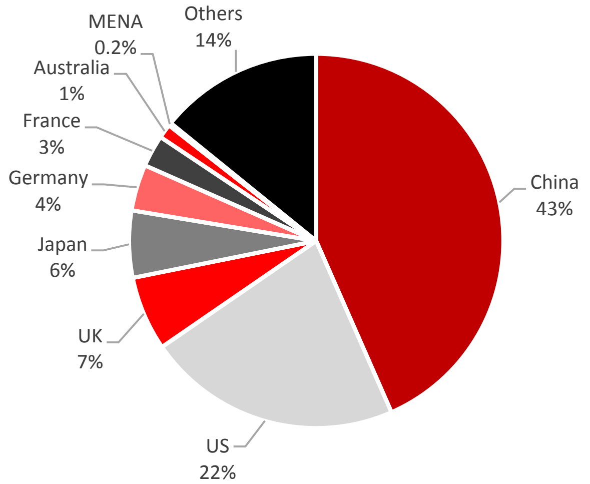
E-commerce is a key emerging theme, which has witnessed increased share of total retail sales across the world. High internet penetration coupled with a generation brought up online and familiar with the digitally connected lifestyle has driven the surge in online shopping. E-commerce penetration has increased from low single digits to low double digits in developed markets of US, Europe and China. As per leading statistics company - statista.com estimates, global e-commerce market is forecasted to grow at 19% CAGR over 2016-21E and reach 16% of total retail sales by 2021. China and USA are currently the largest e-commerce markets with respective size of ~USD672bn and ~USD341bn ending 2015.

Fig. 42. Global e-commerce penetration expected to reach 16% by 2021 as e-commerce sales sustains strong growth



Source: statista.com, ADCB Securities Equity Research.

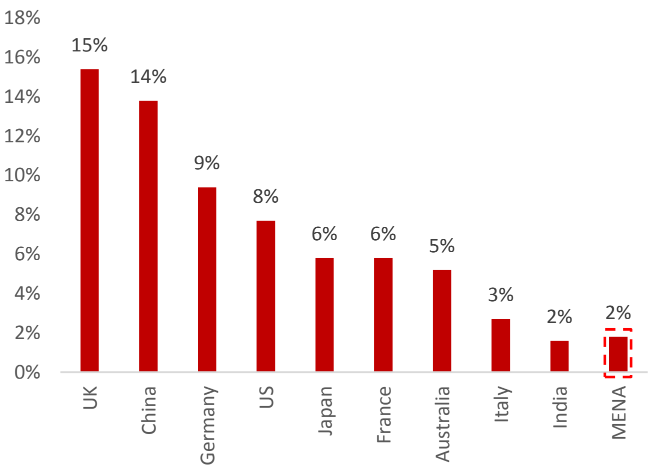
Fig. 43. China and USA are the biggest e-commerce markets, MENA is very small



Source: statista.com, eMarketer, ADCB Securities Equity Research.

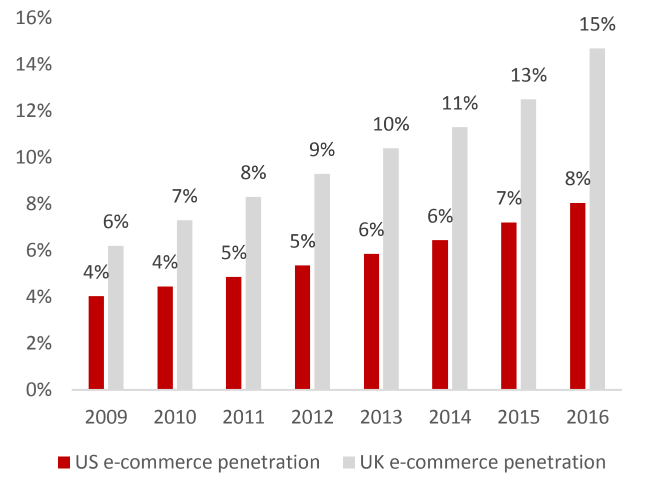
MENA e-commerce market is small compared to other developed markets. Various estimates indicate size of MENA e-commerce market at ~USD5bn. E-commerce penetration in MENA is also low at ~2% versus global average of 9%. However, MENA markets today stand at the same inflection point where developed markets were 8-10 years back. As seen in UK and USA, e-commerce penetration rose from 4% and 6% respectively in 2009 to 8% and 15% in 2016. With entry of Amazon (on acquisition of souq.com) and recent launch of noon.com, MENA e-commerce market is likely to get more dynamic. And it is expected that MENA e-commerce market would follow a similar high growth trajectory (15-20% CAGR) and double in next five years.

Fig. 44. E-commerce penetration highest in UK/China, in MENA penetration is low currently



Source: statista.com, eMarketer, US Census Bureau, UK Office for National Statistics, ADCB Securities Equity Research.

Fig. 45. E-commerce penetration increased at a strong pace in developed markets of US and UK



Source: US Census Bureau, UK Office for National Statistics, ADCB Securities Equity Research.

What is the impact of e-commerce on store based retailing

It is difficult to ignore the dramatic share shift from physical stores to digital commerce or under-estimate the transformative effect of e-commerce on pricing, product availability and shopping convenience which is driving the increasing e-commerce penetration. We tried to analyze few developed markets and understand how rising e-commerce penetration impacted store based retail. Based on our analysis of USA/UK markets, we draw following conclusions for UAE retail market:

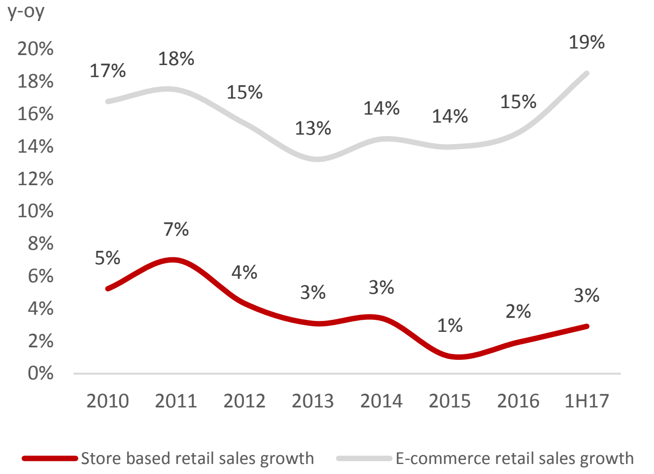
- Store based retail sales is likely to grow at slower rate than seen historically.
- Impact on few categories like electronics, clothing, home furniture/furnishings etc. is likely to be much higher than others. These segments could see sharper slow down than overall store based retail sales.
- We expect retailers to become more selective in store openings and look at selective store closures based on cost structures of individual stores. At the same time, retailers would continue to focus on key stores given store based sales is still a dominant channel (nearly 98% of total retail sales in MENA).
- Food and beverages, supermarkets, luxury fashion and entertainment segments tend to be less affected by the flight to online retail and subsequently remain strong performers. So, right tenant mix becomes more paramount to ensure that shopping malls owners do not face higher risk from growing e-commerce threat.

Based on our conclusions, we are of view that dominant high quality assets with good locations and diversified tenant mix should be more resilient to changing market dynamics. Shopping malls with high footfall and ability to generate high trading density (retail sales per sqft) should continue to get retailers' attention. However, secondary locations would be under higher burden to reduce rents or see higher vacancies.

A case study: How rising e-commerce penetration impacted store based retail

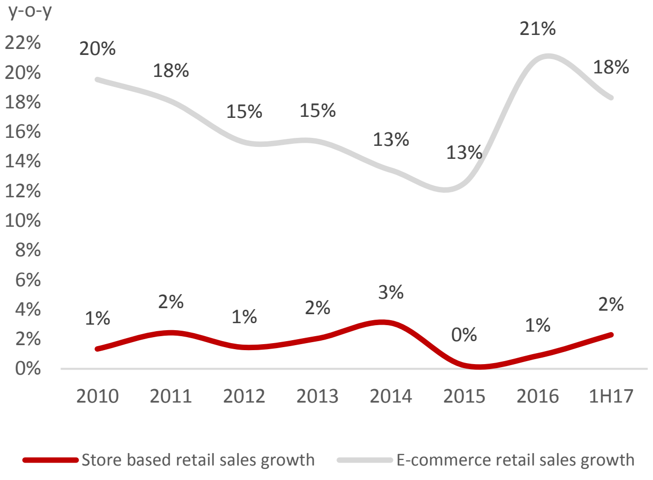
As evident from US and UK experience, rising e-commerce penetration has led to physical brick and mortar stores facing increasing pressure on sales and operating margins. Higher e-commerce share in total retail led to store based retail witnessing slower growth. While store based retail sales suffered slowdown but growth remained in positive territory.

Fig. 46. Store based retail sales performance compared to e-commerce retail sales in US



Source: US Census Bureau, ADCB Securities Equity Research.

Fig. 47. Store based retail sales performance compared to e-commerce retail sales in UK



Source: UK Office for National Statistics, ADCB Securities Equity Research.

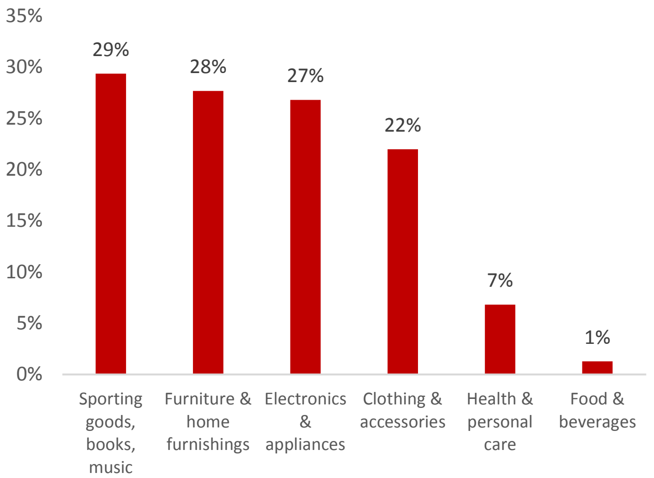
Fig. 48. Conclusion: Store based retail sales witnessed modest growth (2009-16 CAGR) in US and UK as e-commerce gained traction

Source: US Census Bureau, UK Office for National Statistics, ADCB Securities Equity Research.

Clothing, Electronics segments impacted more than other categories

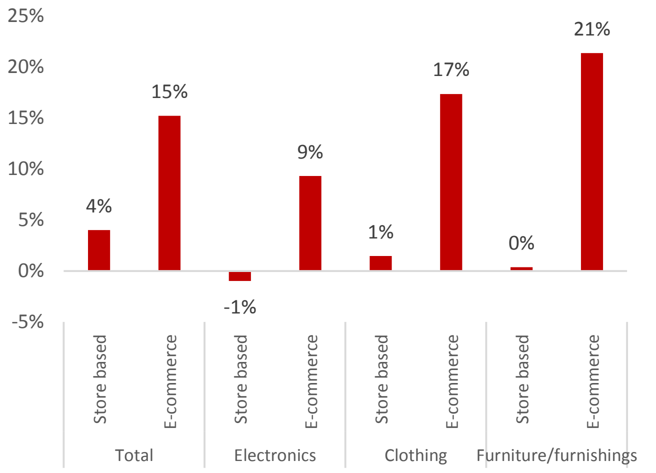
In US/UK markets, few segments like electronics, clothing, furniture/home furnishings etc. witnessed much stronger e-commerce penetration. E-commerce now accounts for major share of retail sales in these segments. Overall store based retail sales still grew modestly at 4% p.a. over 2009-15, but store based retail sales for high prone segments saw sharper slowdown.

Fig. 49. USA e-commerce penetration by segment



Source: US Census Bureau, ADCB Securities Equity Research.

Fig. 50. Growth comparison (2009-15) for US store based and e-commerce retail sales by category



Source: US Census Bureau, ADCB Securities Equity Research.

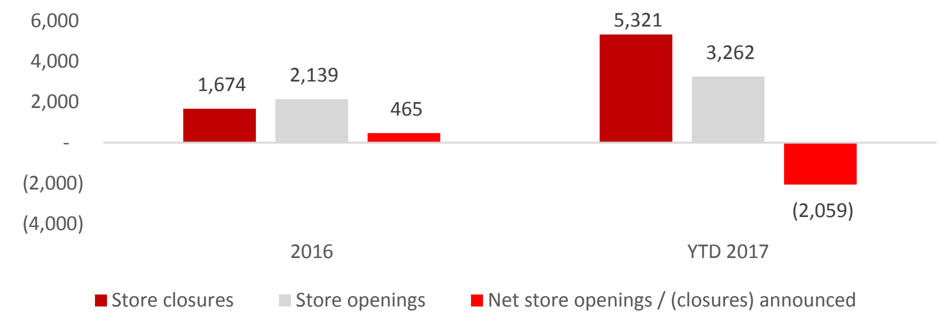
Store consolidation accelerated

Cost cutting measures adopted by retailers to maintain profitability or prevent downward pressure have resulted in many store closures announcements in USA and other developed markets. In order to compete against online players, retailers are focusing on shopping centers that provide the following favorable characteristics:

- High productivity
- Growth potential
- Positive competitive dynamics
- High shopper traffic

In US, 1H17 announcements for store closures have exceeded those of store openings. Store closures were announced mainly due to bankruptcies or to contain losses, while store openings were mainly in value concepts like discount/off-price, fast fashion, beauty and sportswear specialty retailers.

Fig. 51. US store closure announcements exceed store opening announcements in 1H17



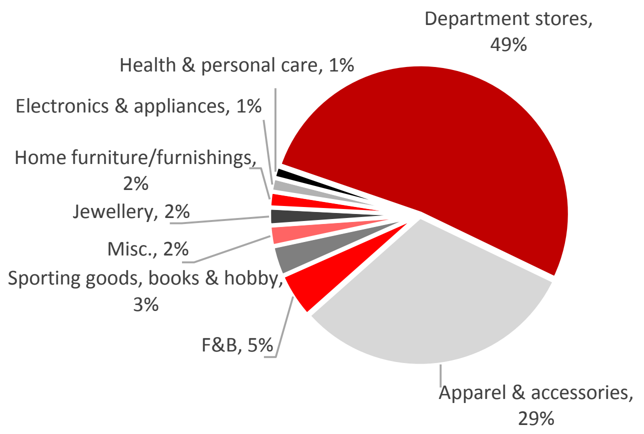
Source: Fung Global Retail & Technology, ADCB Securities Equity Research.

Retail and category mix important

In US, store closure announcements show strikingly worsening retail landscape picture. However, it is partly due to large concentration of categories prone to online retail sales. As per study by leading real estate consultancy - CBRE, about 50% of US shopping malls gross leasable area (GLA) is occupied by department stores with apparel & accessories occupying another 29%. And these two are among slowest growing categories in retail.

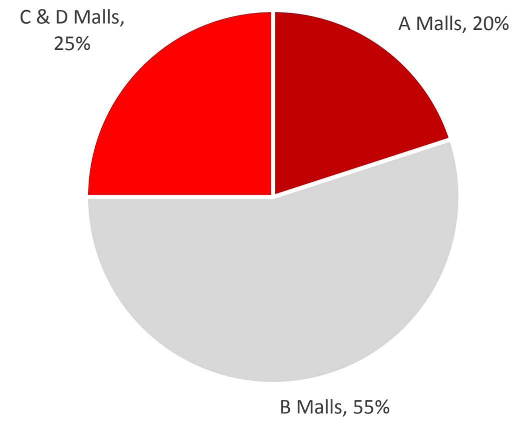
Moreover, A class malls in US constitute only 20% of the market, but they account for nearly 70% of all mall sales. High concentration of GLA is in class B & C malls with large space allocated to low performing department stores. The wide divergence between performance of A and other class of malls explains the high number of bankruptcy and store closure announcements in US.

Fig. 52. US shopping malls GLA by segments



Source: CBRE, ADCB Securities Equity Research.

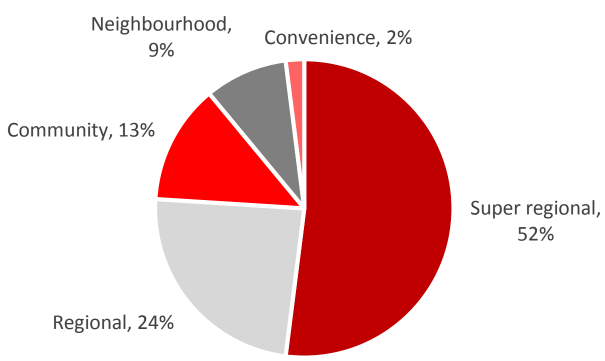
Fig. 53. US shopping malls GLA by category



Source: Fung Global Retail & Technology, ADCB Securities Equity Research.

For Dubai retail sector, higher concentration of super-regional malls should prove to be supportive to maintain better performance than seen in USA retail sector. Super-regional malls tend to draw higher footfall and thus have increased ability to generate high trading density (retail sales per sqft).

Fig. 54. Super regional malls dominate Dubai retail GLA

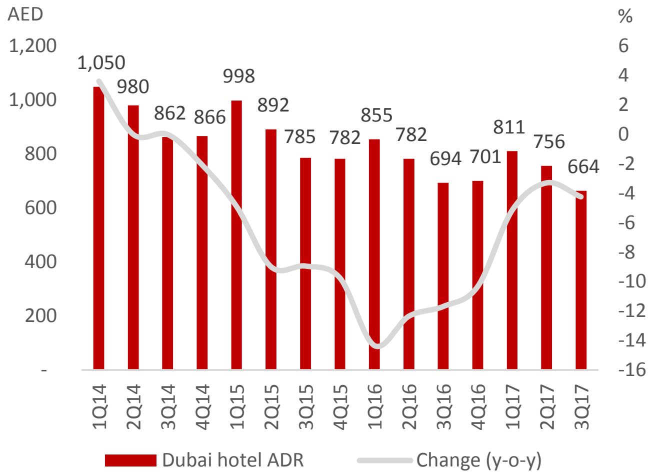


Source: Knight Frank, ADCB Securities Equity Research.

Hospitality sector: high supply key risk to ADRs

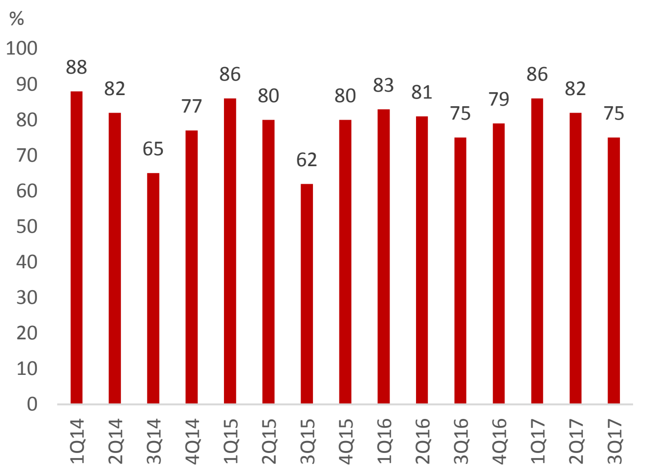
Occupancy at UAE hotels has remained broadly stable despite slowdown in tourism growth seen in 2016. Hotels have resorted to discounting on daily room rates to push occupancy levels. In line with recovery seen in tourism, decline in average daily rates (ADRs) has moderated in 9M17. Dubai hotel ADRs have declined at 4.2% y-o-y in 9M17 after suffering -10% y-o-y in 2016.

Fig. 55. Dubai hotel ADRs - gradual easing of pressure



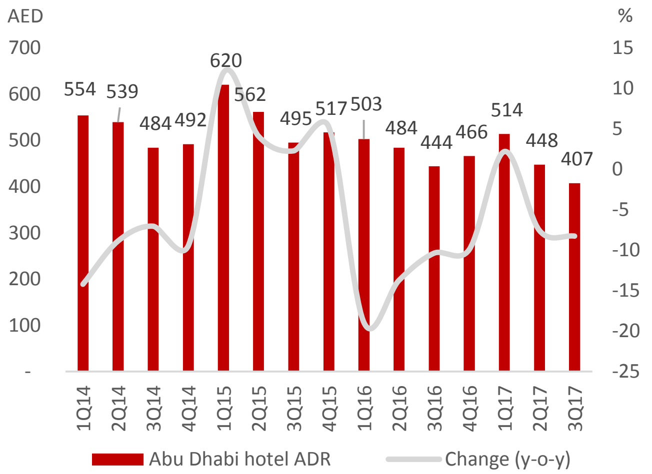
Source: JLL, ADCB Securities Equity Research.

Fig. 56. Dubai hotel occupancy remains stable



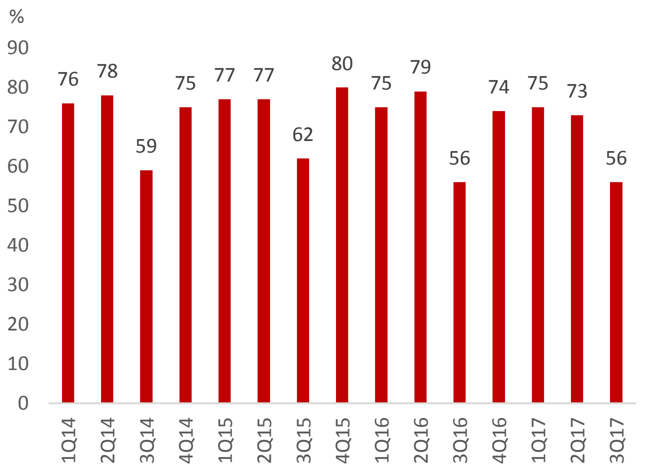
Source: JLL, ADCB Securities Equity Research.

Fig. 57. Abu Dhabi hotel ADRs - moderating pace of decline



Source: JLL, ADCB Securities Equity Research.

Fig. 58. Abu Dhabi hotels occupancy also stable



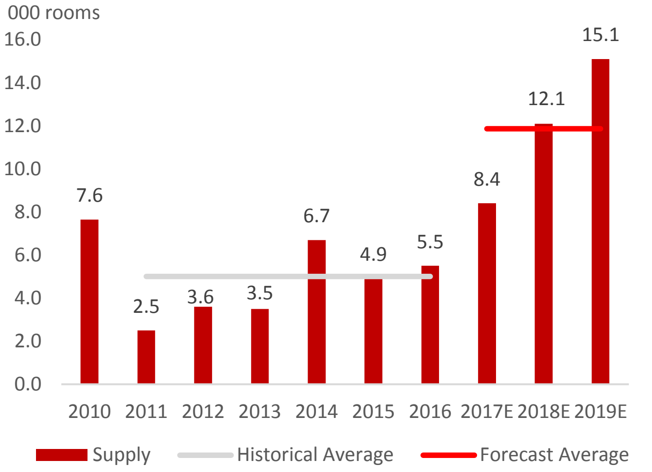
Source: JLL, ADCB Securities Equity Research.

Forthcoming supply exceeds demand growth

Hospitality players are pressing ahead with aggressive pipeline of hotel rooms in anticipation of strong demand from Dubai's Expo 2020 event. JLL estimates an increase in Dubai hotel rooms by 35.6k over 2017-19E. This represents an annual increase of 11.8k rooms or 2.4x higher than historical average supply of 4.9k rooms p.a. Similar to retail, actual supply realization rate for Dubai's hotel sector is also higher at 78% of forecast.

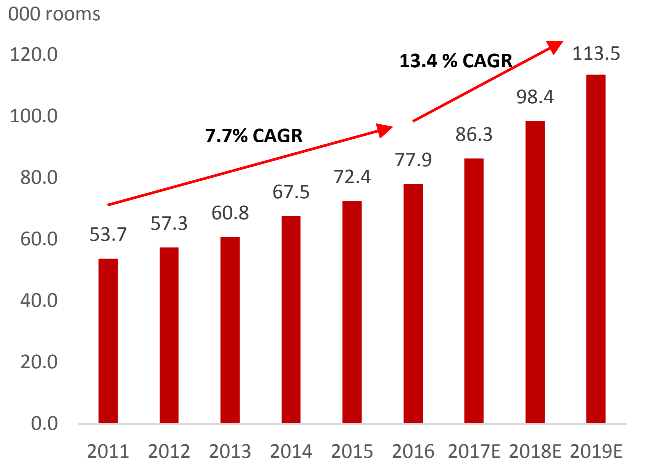
Assuming JLL estimated supply, hotel rooms in Dubai are likely to increase by 13.4% p.a. over 2016-19E. This is higher than expected tourism growth of 7.6% p.a.

Fig. 59. Dubai annual hotel supply –expected increase in supply is 2.4x historical levels



Source: JLL, ADCB Securities Equity Research.

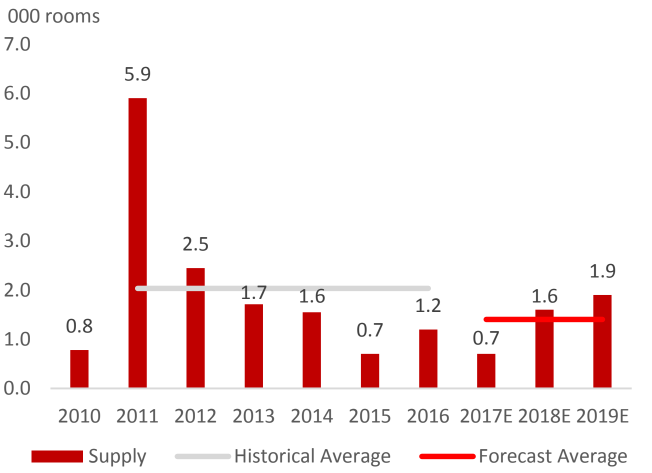
Fig. 60. Dubai hotel rooms – expected increase in hotel rooms is twice the estimated tourism growth



Source: JLL, ADCB Securities Equity Research.

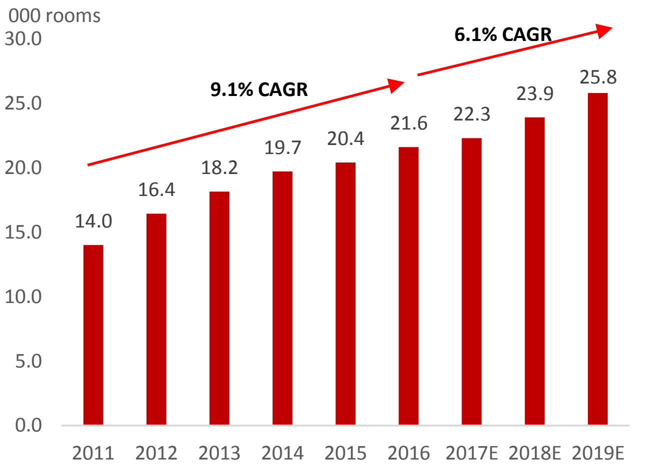
For Abu Dhabi, JLL estimates an increase in hotel rooms by 4.2k over 2017-19E. This represents an annual increase of 1.4k rooms or 31% below historical average supply of 2.2k rooms p.a. Actual supply realization rate for Abu Dhabi's hotel sector is high at 83% of forecast. Assuming JLL estimated supply, hotel rooms in Abu Dhabi are likely to increase by 6.1% p.a. over 2016-19E. This is broadly in line with tourism growth.

Fig. 61. Abu Dhabi annual hotel supply –expected increase in supply 31% below historical levels



Source: JLL, ADCB Securities Equity Research.

Fig. 62. Abu Dhabi hotel rooms – expected increase in hotel rooms broadly in line with tourism growth

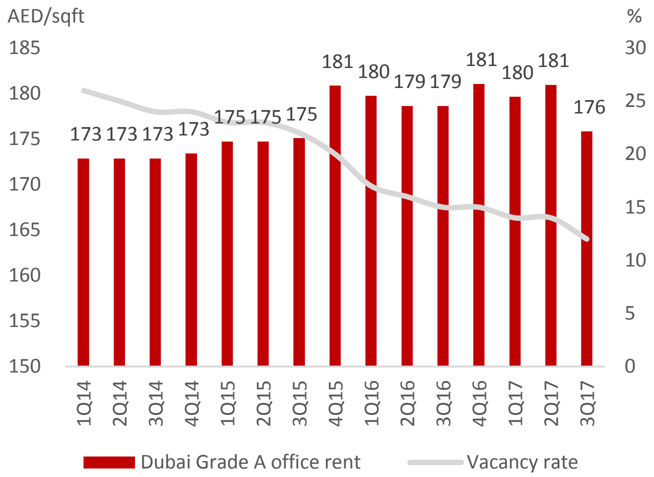


Source: JLL, ADCB Securities Equity Research.

Office sector: Dubai more resilient than Abu Dhabi

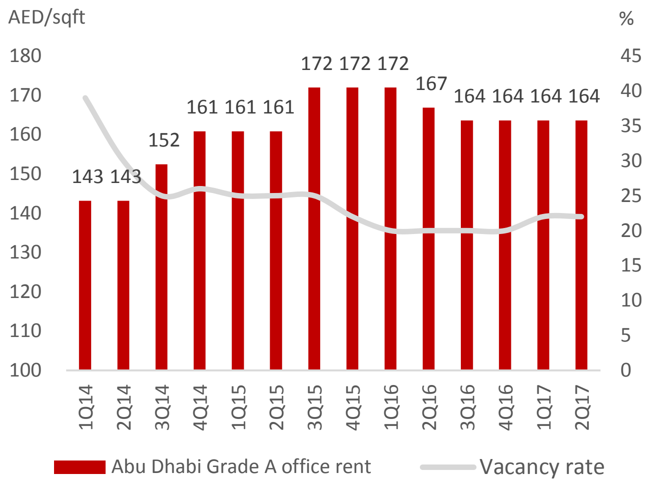
Dubai office sector had been relatively resilient to economic slowdown, with stable rents and reducing vacancy rates. However, Grade A offices at central business locations started to see soft demand recently with moderate decline in rents. Upcoming high quality space at ICD Brookfield / One Central are adding to competition for existing locations. In Abu Dhabi, corporate demand is largely driven by government related entities, which has seen a slowdown as a result of government's fiscal consolidation. Current rents or vacancy rates in Abu Dhabi show stable trend, but this is likely due to long term rent agreements in place. We expect the impact to become visible with lag as leases fall due for renewal (similar to trend seen in Dubai office segment).

Fig. 63. Dubai office rents and vacancy rate



Source: : JLL, ADCB Securities Equity Research.

Fig. 64. Abu Dhabi office rents and vacancy rate

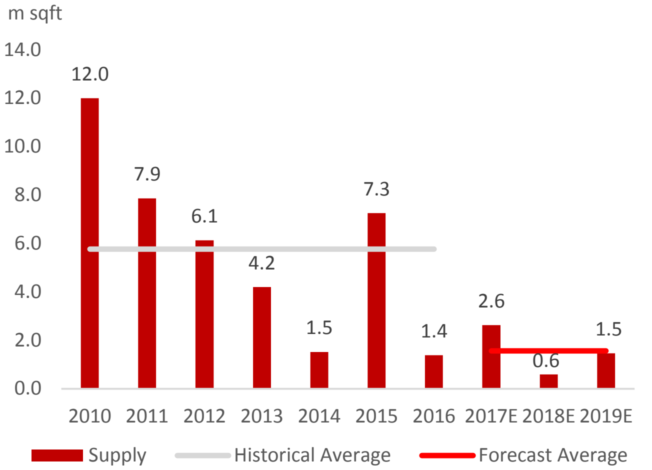


Source: JLL, ADCB Securities Equity Research.

Supply expectations remain muted

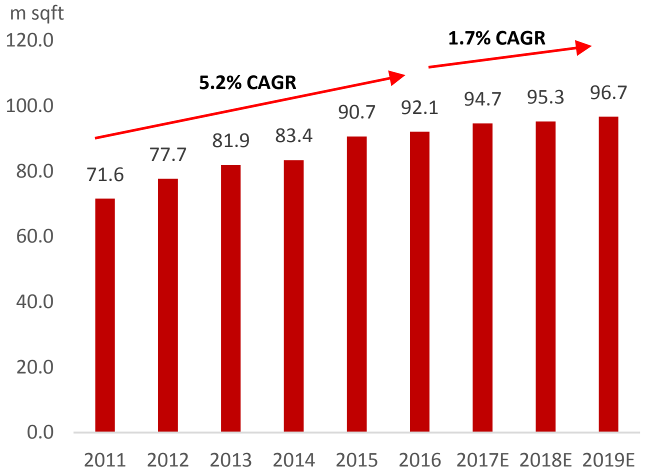
JLL estimates an increase in Dubai office stock by 4.7m sqft over 2017-19E. This is an annual increase of 1.6m sqft or 73% below historical average supply of 5.7m sqft p.a. Actual supply realization rate for Dubai's office sector has been low at 48% of forecast. Assuming JLL estimated supply, office stock in Dubai is likely to increase by 1.7% p.a. over 2016-19E. This is lower than expected UAE GDP growth of ~3.5%.

Fig. 65. Dubai annual office supply –expected increase in supply below historical levels



Source: JLL, ADCB Securities Equity Research.

Fig. 66. Dubai office stock – expected increase in stock below GDP growth forecast

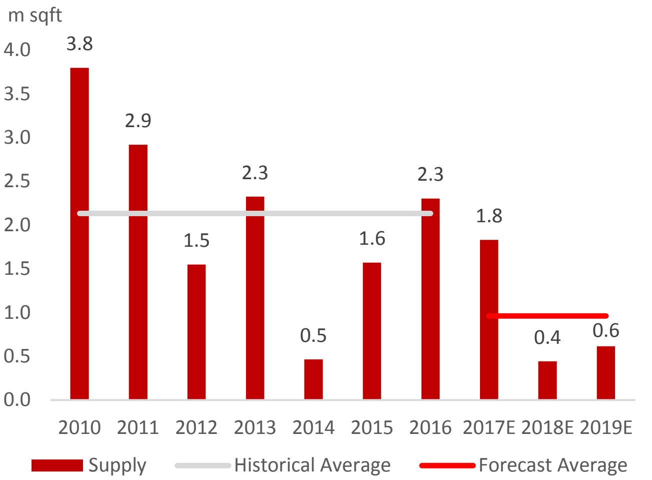


Source: JLL, ADCB Securities Equity Research.

For Abu Dhabi, JLL estimates an increase in office stock by 2.9m sqft over 2017-19E. This represents an annual increase of 0.96m sqft or 55% below historical average supply of 2.1m sqft p.a. Actual supply realization rate for Abu Dhabi's office sector had also been low at 37% of forecast.

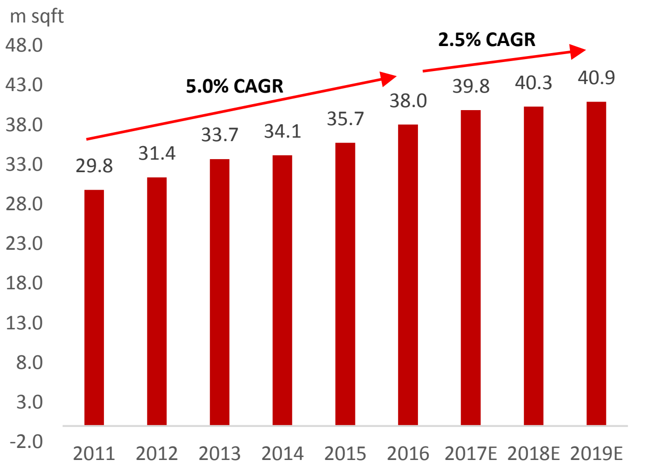
Assuming JLL estimated supply, office stock in Abu Dhabi is likely to increase by 2.5% p.a. over 2016-19E or lower than UAE GDP growth of ~3.5%.

Fig. 67. Abu Dhabi annual office supply –modest increase in supply compared to historical levels



Source: JLL, ADCB Securities Equity Research.

Fig. 68. Abu Dhabi office stock – expected increase in stock below GDP growth forecast



Source: JLL, ADCB Securities Equity Research.

EMAAR PROPERTIES
Firing on all cylinders

Initiate coverage with a Buy

Real Estate | UAE | 12 November 2017

We initiate coverage on Emaar Properties with a Buy rating and a target price of AED10.8, offering an upside of 38%. Emaar offers exposure to mix of stable recurring income (50% of gross profit) and high earnings growth. Its development property (DP) business is largely driven by Dubai, which is embarking on a next phase of growth through joint venture (JV) deals with government developers. Dubai DP business' solid pipeline (enhanced mainly by JVs) ensures strong visibility and sustainability of pre-sales. Listing of UAE development business should help to crystallize value of this business, which has been undervalued by the market despite superior pre-sales performance. Implied market discount for other unlisted businesses is likely to increase significantly post listing of UAE development business. As one of the strategic goal, Emaar's management could look at listing other businesses over next few years, offering opportunity for further value unlocking.

Solid development pipeline for next 20 years, boosted by JV projects

Emaar's development property business is largely driven by Dubai (80% of pre-sales on average). Emaar's own land parcels in Dubai are expected to be sold over next five years. Emaar has partnered with government developers to expand its land bank and embark upon next phase of growth. New JV projects offer attractive location and add significant scale and visibility. Recently acquired Dubai Harbour plot near Dubai Marina should further augment its pipeline. We estimate its UAE development pipeline of 120k units (excl. Lusaily) to offer development visibility for next 20 years.

Mgmt. confident to sustain peak Dubai pre-sales, we are cautious

Emaar has outperformed Dubai property market and recorded strong pre-sales in 2016/9M17. We expect Dubai pre-sales of AED19.4bn in 2017 (35% y-o-y) i.e. at historical highs. Aggressive new launches with attractive payment plans has lifted its pre-sales performance. Emaar's management expects to sell its pipeline in next 12 years, implying an annual sales of ~10k units over 2018-29E (~8.3k in 2017E). We factor pre-sales of AED282bn over 2017-38E, implying an average pre-sales of AED12.8bn p.a. or 34% lower than 2017E. Our pre-sales estimates are ~55% above historical average (2001-16) and includes Emaar's JV partners share in pre-sales.

Earnings catalysts ahead: all segments on high growth path

Emaar's earnings (14% CAGR over 2016-19E) are expected to sustain growth momentum as all major businesses are positioned to grow strongly. UAE development business should maintain high growth driven by acceleration in deliveries. Retail segment should benefit from start of fashion avenue expansion by 2017 end and doubling of retail GLA by 2021/22 with new malls in JV projects. Hotel business is likely to see a new growth trajectory after doubling of rooms in last one year and further planned expansion.

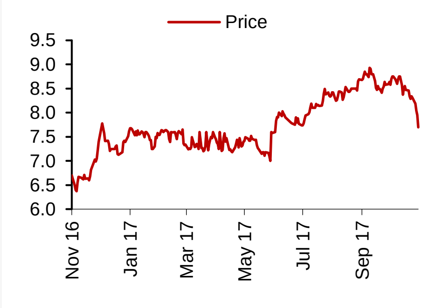
New listings key to unlock value and sustain premium valuation

Emaar is trading at a P/BV of 1.1x 2018E, in line with EM peers. On P/NAV, it trades at 0.52x (10% above historical average). Discount to NAV has narrowed since announcement of UAE development listing. Post UAE development listing, market implied discount for other unlisted businesses would increase substantially. Management strategy to independently list each business in future would ensure that further value unlocking continues. This coupled with its strong growth profile should sustain Emaar's valuation above historical levels and peers multiple.

Fundamentals

Recommendation	Buy
Target Price	AED 10.8
Price	AED 7.8
Price 12m High/Low	AED 8.93/6.37
Market Cap.	AED55,799mn
Bloomberg/Reuters	EMAAR UH / EMAR.DU

Price Performance Chart



Source: Bloomberg

Equity Research Team

Yugesh Suneja (+971 2 3050838)
yugesh.suneja@adcb.com

Nikhil Poddar, CFA (+971 2 696 6450)
nikhil.poddar@adcb.com

Financials

Income Statement (AEDmn)	2016	2017E	2018E	2019E
Revenue	15,540	18,544	21,200	23,519
EBITDA	6,257	7,431	8,749	9,891
Depreciation and amortization	955	1,025	1,132	1,254
EBIT	5,302	6,406	7,617	8,638
Other income	551	582	463	620
Net Finance Cost	(42)	69	67	(6)
Profit before tax	5,895	6,919	8,014	9,264
Taxes	79	35	41	47
Minority interest	583	840	1,082	1,485
Net profit	5,233	6,044	6,891	7,732

Source: ADCB Securities Equity Research

Balance Sheet (AEDmn)	2016	2017E	2018E	2019E
Cash and cash equivalents	17,289	17,594	17,291	16,610
Other current assets	49,246	52,620	55,473	56,451
Total non-current asset	16,015	16,590	16,988	17,434
Total assets	96,334	102,803	107,581	110,056
Total current liabilities	31,168	32,229	31,419	29,820
Borrowings	17,350	17,149	16,204	12,536
Other non-current liabilities	149	149	149	149
Total liabilities	48,667	49,526	47,771	42,505
Minority interest	6,663	7,303	8,185	9,435
Shareholders` equity	41,004	45,974	51,625	58,116
Total net debt	62	(445)	(1,087)	(4,073)

Source: ADCB Securities Equity Research

Cash flow statement (AEDmn)	2016	2017E	2018E	2019E
Cash flow from operations	2,403	5,546	5,385	7,620
Net capex	3,581	3,821	3,361	3,289
Free cash flow	(1,177)	1,725	2,024	4,331
Net financing	2,346	(874)	(1,612)	(4,257)
Change in cash	(630)	306	(303)	(682)

Source: ADCB Securities Equity Research

Valuation and leverage metrics	2016	2017E	2018E	2019E
P/E (x)	10.5	9.1	8.0	7.1
P/BV (x)	1.3	1.2	1.1	0.9
P/FFO (x)	8.9	7.8	6.9	6.1
FCF yield (%)	(2.1)	3.1	3.7	7.9
Dividend Yield (%)	1.9	1.9	2.2	2.2
EV/EBITDA (x)	8.8	7.4	6.2	5.2
Interest coverage (x)	8.9	9.5	11.4	14.7
Net debt/equity (x)	0.00	(0.01)	(0.02)	(0.06)
Net debt/EBITDA (x)	0.0	(0.1)	(0.1)	(0.4)

Source: ADCB Securities Equity Research

Key Ratios (%)	2016	2017E	2018E	2019E
ROAIC	14.4	14.8	15.6	16.5
RoAE	13.2	13.9	14.1	14.1
Revenue growth	13.8	19.3	14.3	10.9
EBITDA growth	14.9	18.8	17.7	13.1
EPS growth	31.7	15.5	14.0	12.2
EBITDA margin	40.3	40.1	41.3	42.1

Source: ADCB Securities Equity Research

Per-share data (AED)	2016	2017E	2018E	2019E
EPS	0.73	0.84	0.96	1.08
DPS	0.15	0.15	0.17	0.17
BVPS	5.73	6.42	7.21	8.12
Total no. of outstanding shares (mn)	7,160	7,160	7,160	7,160

Source: ADCB Securities Equity Research

Investment case

Emaar Properties offers exposure to mix of stable recurring income and high earnings growth. Its Dubai development property business is embarking on a next phase of growth with solid pipeline. Emaar Malls and hotels, the other key businesses, are also on high growth trajectory driven by expansions. Listing of UAE development business by Nov2017 should crystalize its value. We see potential listing of other businesses, as aimed by management, to continue unlocking value for shareholders.

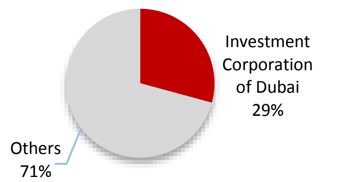
Upside case AED11.8

Better than envisaged consumer and tourist spending to lift growth in retail sales and thus rents. Emaar could also sustain current pre-sales momentum in such a scenario. Emaar would trade at 2018E P/NAV of 0.8x under such scenario.

Downside case AED7.7

Decline in oil prices and strong momentum in US$ strengthening will further constraint spending from tourists and population. This could restrict ability to increase retail base rents and also slowdown its pre-sales. Investors are likely to apply higher discount to value Emaar Malls, other retail and hotels, as well as take a more cautious view on pre-sales. Emaar would trade at 2018E P/NAV of 0.5x under such scenario.

Fig. 1. Shareholding pattern



Source: DFM, ADCB Securities Equity Research

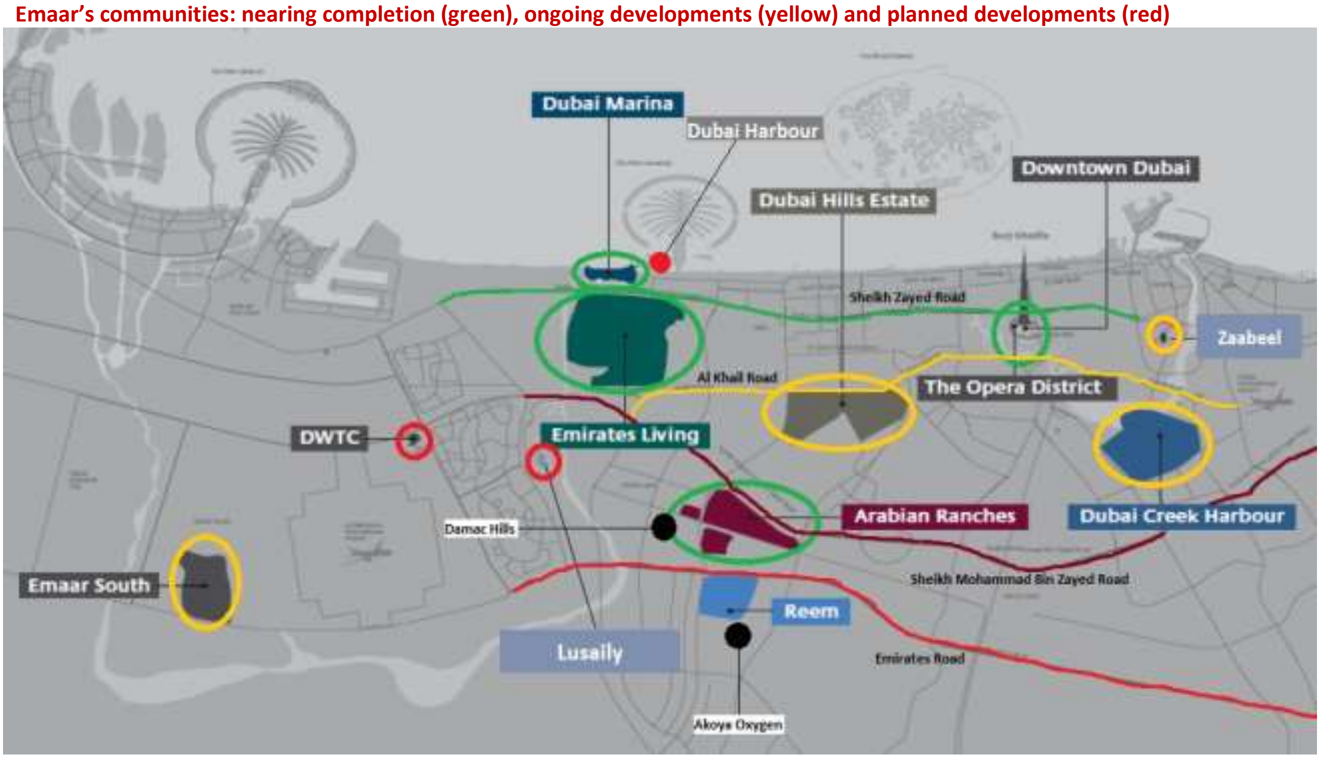
Embarking on next phase of Dubai's development cycle

Solid UAE development pipeline boosted by JV projects

Dubai's freehold development started in 2000 is distributed along key road corridors of Sheikh Zayed Road, Al Khail Road, Mohammed Bin Zayed Road and Emirates Road (highlighted in below figure). Emaar has played an instrumental role in Dubai's property market with the development of prime corridor along the Sheikh Zayed Road (Downtown Dubai, Dubai Marina, Emirates Living) as well as secondary development (Arabian Ranches) between Sheikh Mohammad Bin Zayed Road and Emirates Road. Master planned communities developed by Emaar enjoy strong traction from residents and have now turned into mature developments.

Next big developments along Al Khail Road were conceptualized in the past but were delayed by financial crisis and thus were put on hold. Meanwhile, developers continued their focus on relatively affordable developments along Mohammed Bin Zayed Road. Emaar in partnership with government developers now has embarked on next phase of growth with development of communities at Dubai Creek Harbour, Dubai Hills Estate and key secondary location at Dubai South.

Emaar's communities: nearing completion (green), ongoing developments (yellow) and planned developments (red)

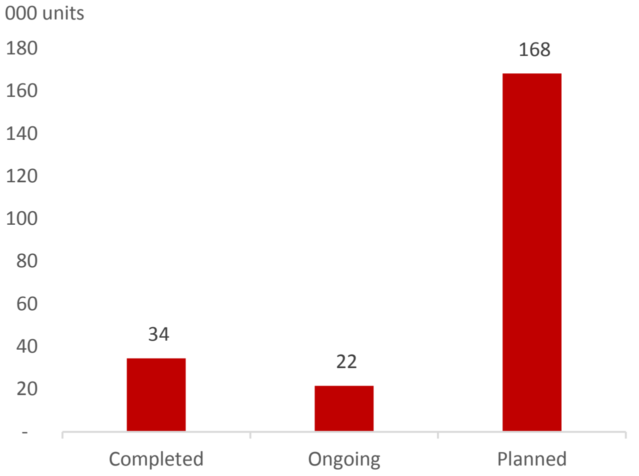


Source: Company, ADCB Securities Equity Research.

Emaar has undertaken development of ~56k units in last 16 years. Its current development pipeline remains solid and we estimate it to offer visibility for next 20 years. Scale of development pipeline (168k units, active pipeline of 120k units excluding projects in design phase) is more than Emaar has undertaken historically in Dubai (34k units completed plus 22k units under construction). Emaar's own major land parcels in UAE (Downtown Dubai, Emirates Living, Dubai Marina, Arabian Ranches) are near completion and should be fully sold in next five years. However, its

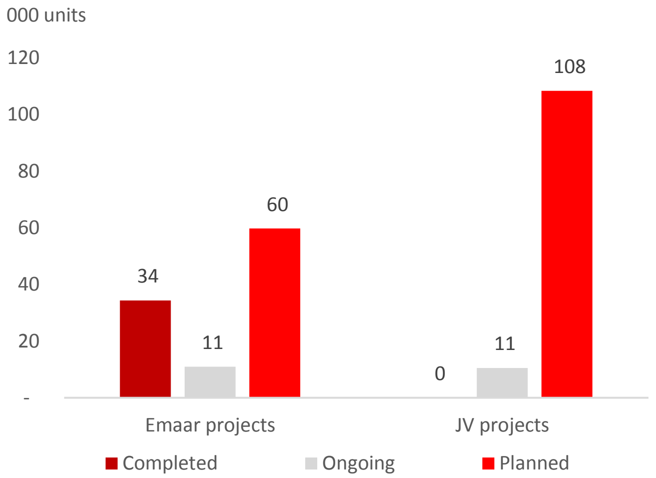
50:50 joint venture (JV) projects at Dubai Hills Estate (Meraas as partner), Dubai Creek Harbour (Dubai Holding as partner) and Emaar South (Dubai World Central as partner) have boosted its pipeline. JV projects account for 90% of its active pipeline and 64% of its total planned unit pipeline.

Fig. 69. Planned UAE development pipeline is 3x higher than historical (completed + ongoing)



Source: Company, ADCB Securities Equity Research.

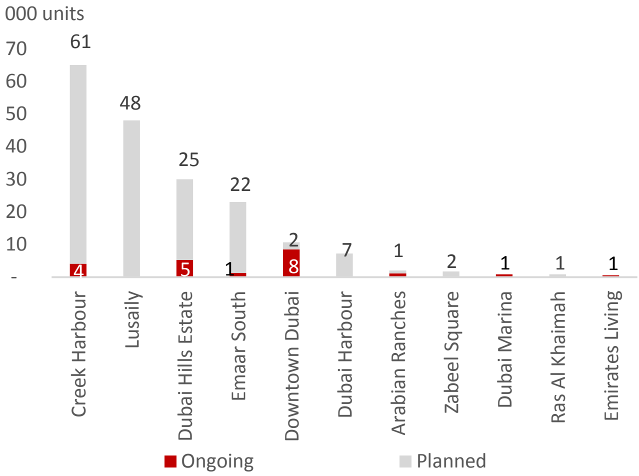
Fig. 70. Development pipeline boosted mainly by JV projects



Source: Company, ADCB Securities Equity Research.

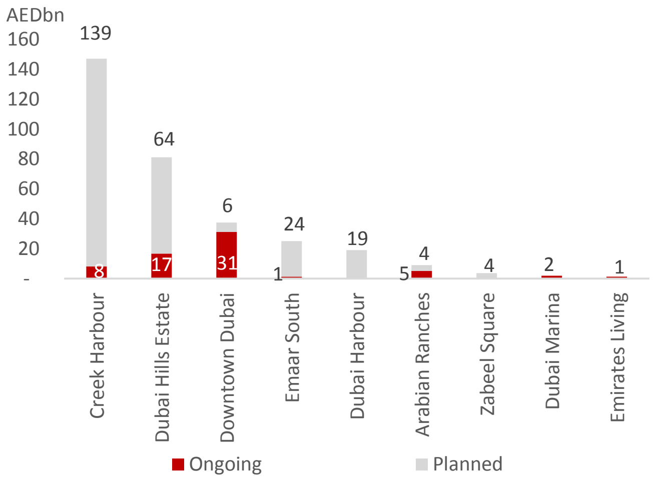
In terms of size, Creek Harbour represents highest visibility followed by Dubai Hills Estate and Emaar South. Emaar's recently acquired Dubai Harbour land plot near Dubai Marina is also noteworthy addition to its pipeline given prime location. Emaar's Lusaily land hold sizeable potential but it is still in design stage. We have excluded it along with Ras Al Khaimah plot from our pre-sales forecast and valuation, given lack of development timeframe and other details.

Fig. 71. Development pipeline by projects



Source: Company, ADCB Securities Equity Research.

Fig. 72. Estimated development pipeline by value (AEDbn)

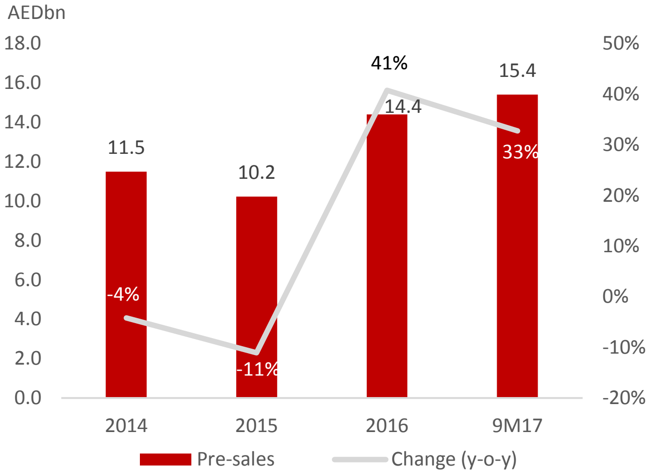


Source: Company, ADCB Securities Equity Research Estimates.

Strong Dubai pre-sales ahead of IPO

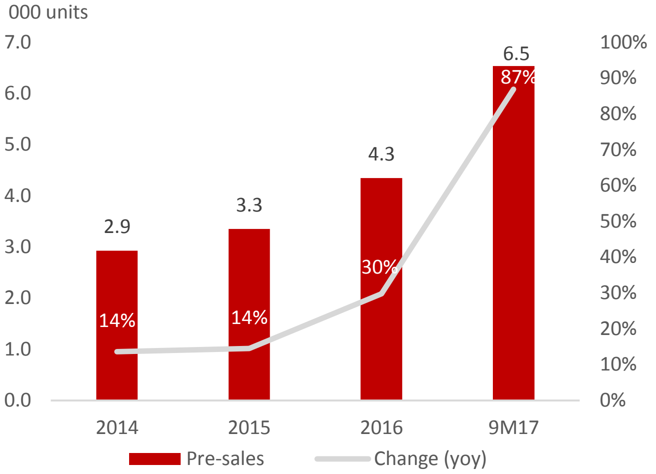
Emaar Properties' Dubai pre-sales surged 33% y-o-y to AED15.4bn in 9M17, following on from solid growth of 41% y-o-y in 2016. Emaar has already sold 6.5k units in 9M17 and we expect pre-sales of ~8.3k units in 2017. In value terms, we expect Emaar's 2017 Dubai pre-sales to reach AED19.4bn (35% y-o-y), at historical highs. In our view, significant pre-sales increase has been driven by: **1/** aggressive new launches (8.4k units launched in 9M17 after 4.6k units in FY2016), **2/** flexible payment plans, **3/** mix of low ticket sized and high end units launched, and **4/** three large Dubai developers (Emaar, Dubai Holding, Meraas) joining hands to sell JV projects.

Fig. 73. Strong growth in Emaar's Dubai pre-sales in 2016 and 9M17, despite challenging property market



Source: Company, ADCB Securities Equity Research.

Fig. 74. Unit pre-sales increased at much higher pace as low priced units are launched this year

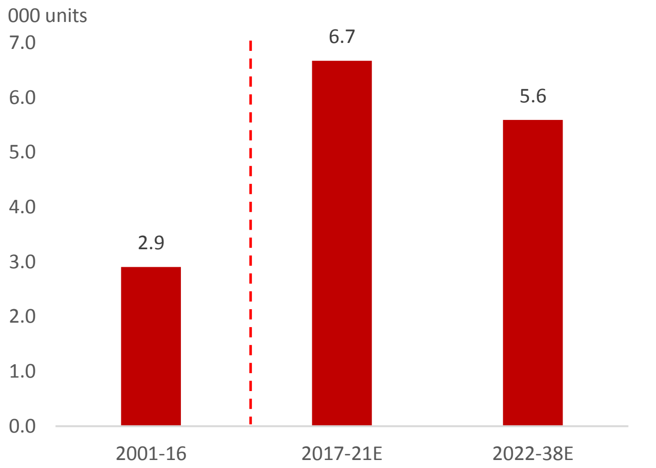


Source: Company, ADCB Securities Equity Research.

Is current pre-sales sustainable?

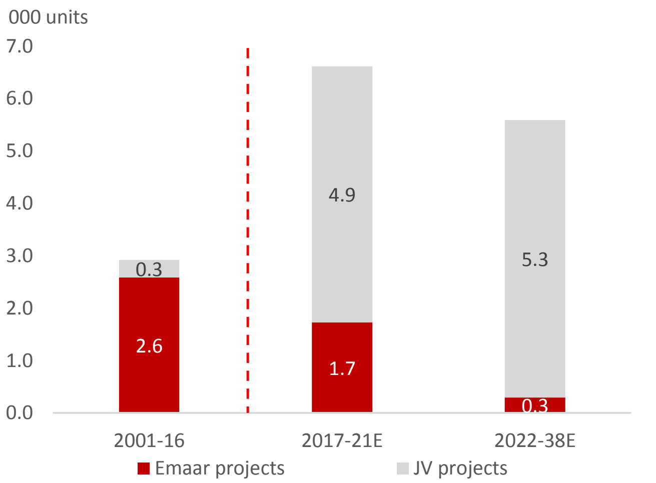
Emaar's management expects to sell its pipeline in next 12 years, implying an annual sales of ~10k units over 2018-29E (~8.3k in 2017E). This would imply future pre-sales to increase 3x historical levels (2.9k units sold per annum over 2001-16). Also this would mean pre-sales to sustain at cyclical peak levels for next 12 years, which we believe is aggressive.

Fig. 75. Our estimated pre-sales



Source: Company, ADCB Securities Equity Research Estimates.

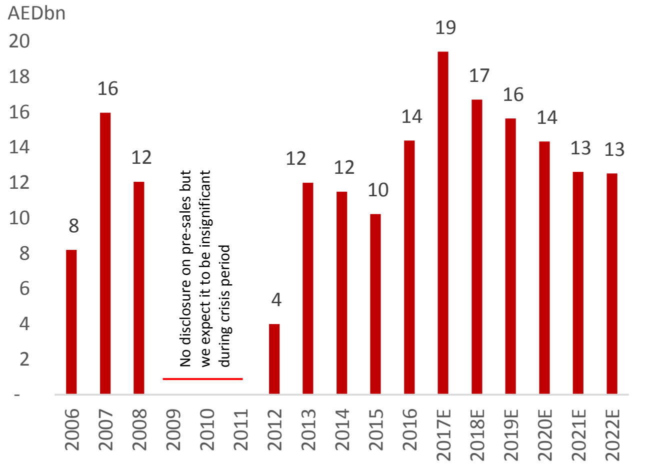
Fig. 76. Future pre-sales mainly driven by JV projects



Source: Company, ADCB Securities Equity Research Estimates.

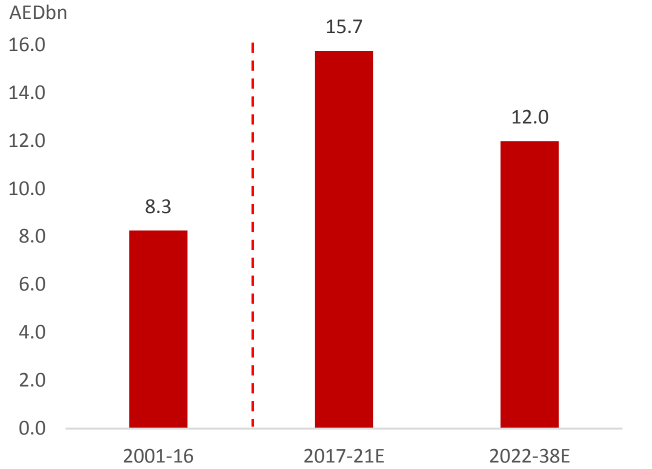
We expect that pre-sales should start to normalize as company's own land bank gets sold by 2021E. Our average pre-sales of AED12.8bn p.a. over 2017-38E is 55% above historical levels (average AED8.3bn p.a. over 2001-16). Higher than historical pre-sales would be supported by Emaar and other two large developers (Meraas and Dubai Holding) joining hands in developing next primary destinations in Dubai.

Fig. 77. Dubai pre-sales expected to peak in 2017 and normalize gradually



Source: Company, ADCB Securities Equity Research Estimates.

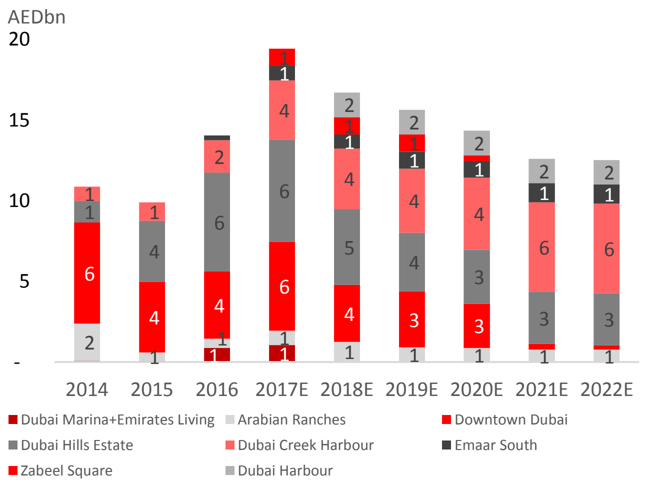
Fig. 78. Dubai pre-sales expected to stay above historical average



Source: Company, ADCB Securities Equity Research Estimates.

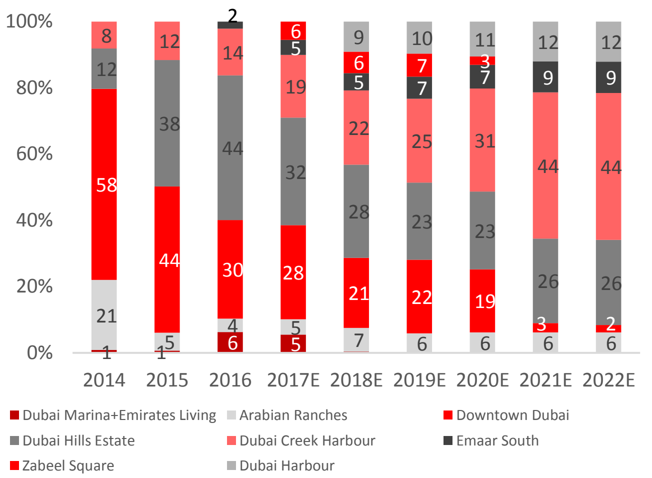
JV projects accounted for half of Dubai pre-sales (on an average in 2015-16). We expect JV projects contribution to increase to 62% over 2017-20E and 80% in 2021-22E.

Fig. 79. Dubai pre-sales contribution by projects



Source: Company, ADCB Securities Equity Research Estimates.

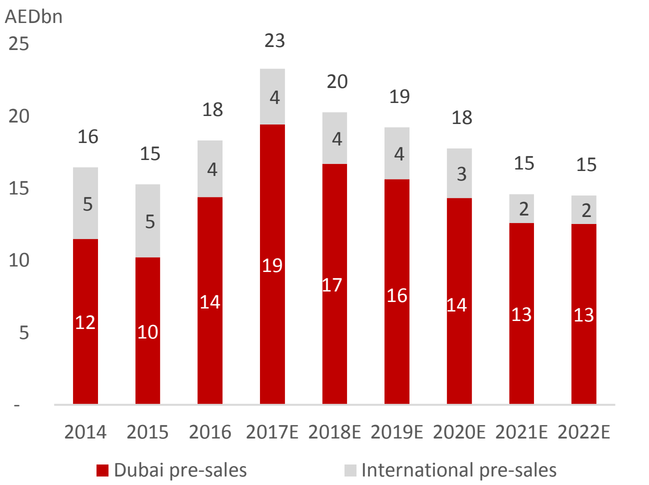
Fig. 80. JV projects contribution increasing in Dubai pre-sales



Source: Company, ADCB Securities Equity Research Estimates.

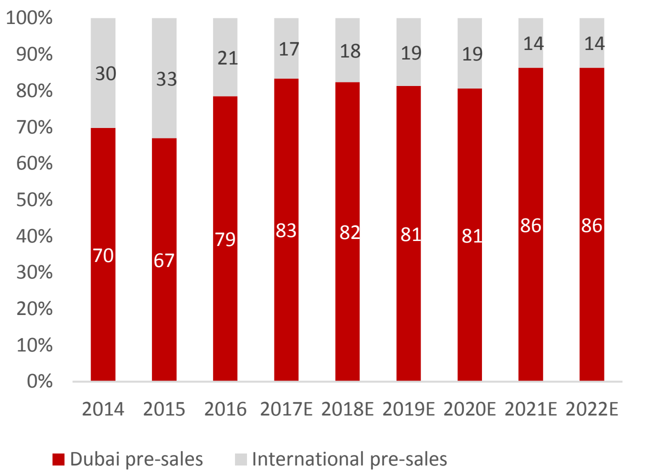
Emaar's group pre-sales (Dubai + International) is largely driven by Dubai and we expect this trend to continue.

Fig. 81. Emaar's group pre-sales expected to decline, in line with Dubai pre-sales



Source: Company, ADCB Securities Equity Research Estimates.

Fig. 82. Dubai development business to contribute around 80% to group's pre-sales over 2017-20E



Source: Company, ADCB Securities Equity Research Estimates.

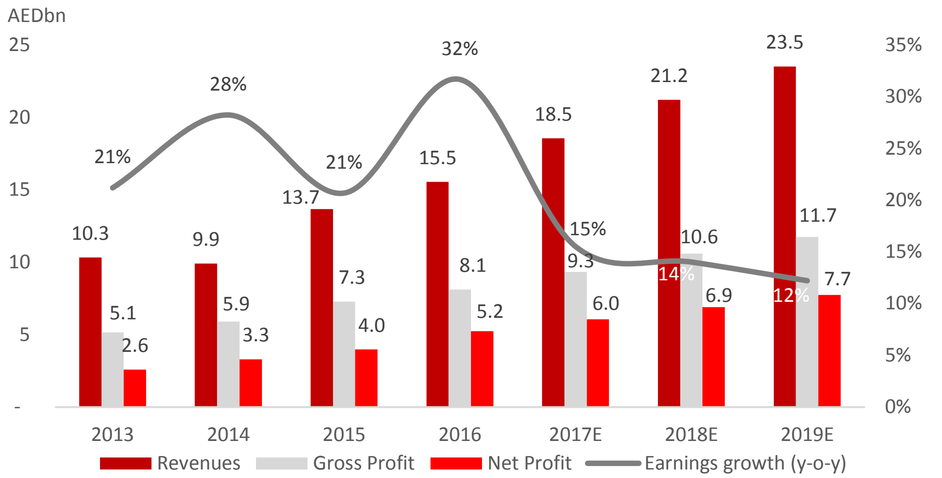
Increase in selling prices offer upside risk to pre-sales

Our estimated pre-sales is based on company's indicated gross floor area (GFA) in each project and our estimated selling prices. We have not factored increase in selling prices over next 20 years. The company expects selling prices to increase as these communities mature. There is a scope for increase in selling prices as infrastructure is developed, residents start to move in post-handover and new attractions are delivered (tallest tower at Creek Harbour, golf course at Dubai Hills Estate, new malls etc.), similar to the trend seen in Downtown Dubai.

All business segments on high growth trajectory

Emaar Properties earnings growth is expected to sustain momentum as all major businesses are positioned to grow strongly, driven by high growth in past years' pre-sales and contribution of expansion assets. We expect earnings CAGR of 14% over 2016-19E.

Fig. 83. Emaar offers strong earnings growth

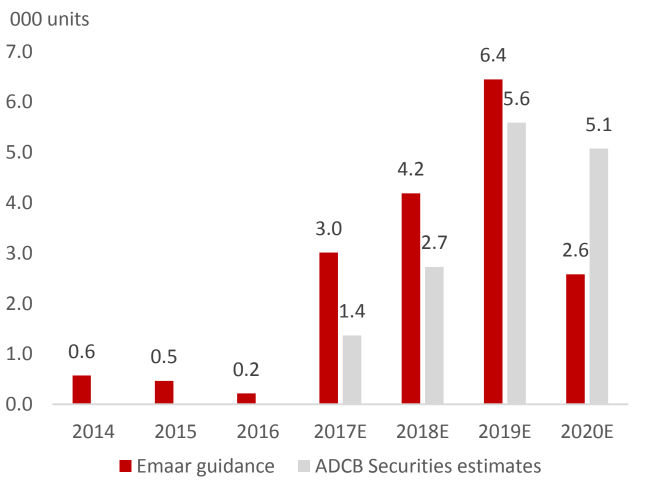


Source: Company, ADCB Securities Equity Research Estimates.

Development business earnings driven by Dubai backlog

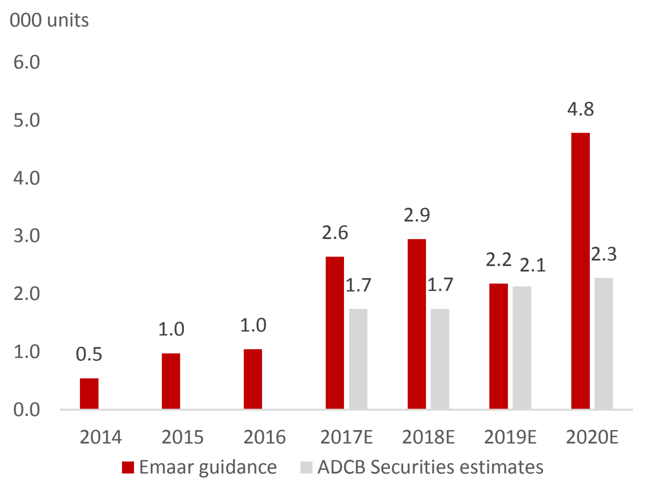
Emaar's development business' (50% of 2017E gross profit) backlog stood at AED50bn as on 1H17, which is expected to be recognized over next four-five years. Backlog is largely driven by UAE (80% of backlog) after solid pre-sales growth seen in last two years. UAE development business' unit deliveries are expected to accelerate in next few years as past pre-sales is delivered, contributing to strong revenue growth. We expect 17% CAGR in UAE development business gross profit over 2016-19E.

Fig. 84. UAE development business: expecting acceleration in unit deliveries



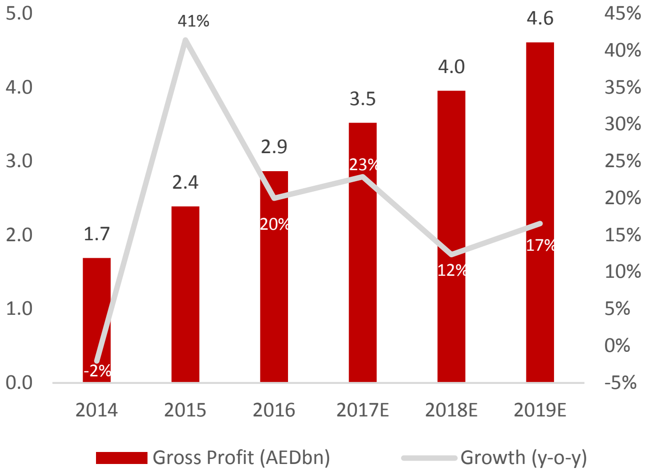
Source: Company, ADCB Securities Equity Research Estimates.

Fig. 85. International development business: co. expecting sharp pick up in deliveries but we are more cautious



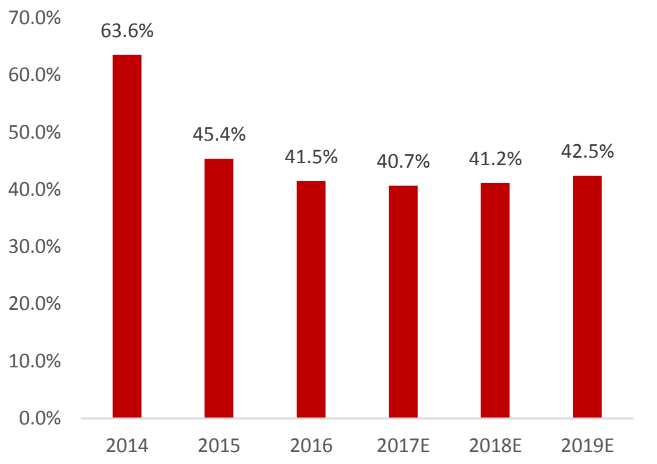
Source: Company, ADCB Securities Equity Research Estimates.

Fig. 86. UAE development business gross profit expected to grow at a 18% CAGR over 2016-19E



Source: Company, ADCB Securities Equity Research Estimates.

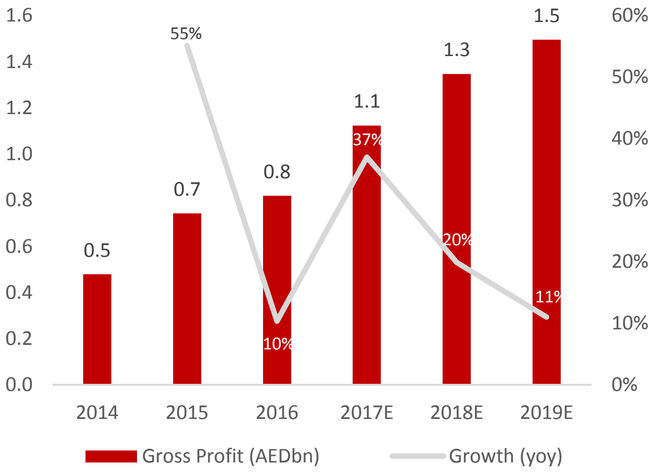
Fig. 87. UAE development business gross profit margin expected to remain stable



Source: Company, ADCB Securities Equity Research Estimates.

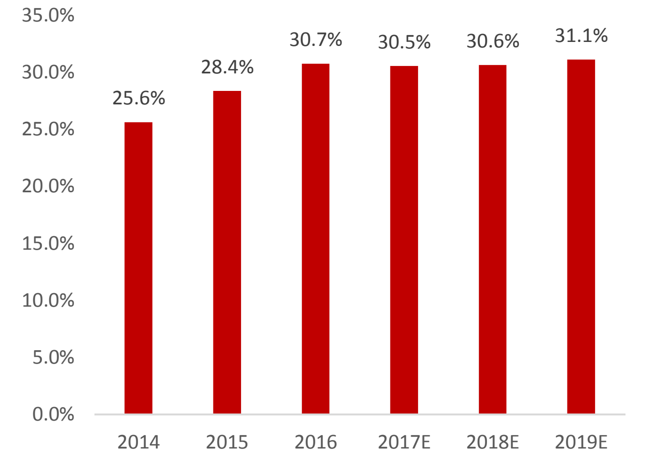
For international development business, we expect gross profit to grow at a CAGR of 22% over 2016-19E driven by higher revenue growth. Higher growth is driven by consolidation of Emaar MGF (Indian development subsidiary consolidated since end of 4Q16). International development business margins are expected to remain stable.

Fig. 88. International development business gross profit expected to grow at a 22% CAGR over 2016-19E



Source: Company, ADCB Securities Equity Research Estimates.

Fig. 89. International development business gross profit margin expected to decline

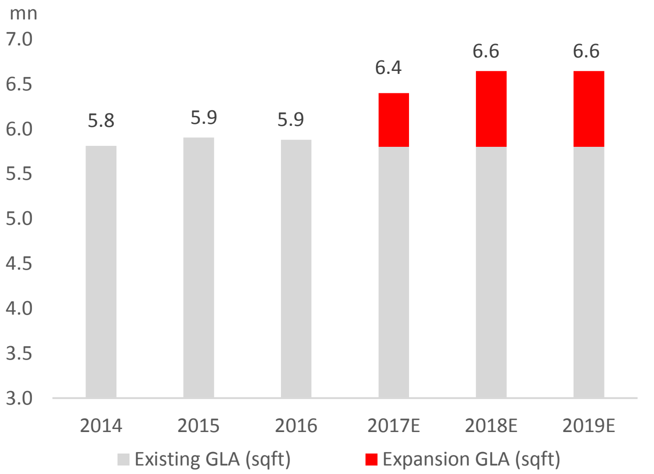


Source: Company, ADCB Securities Equity Research Estimates.

The Dubai Mall expansion to drive growth in retail business

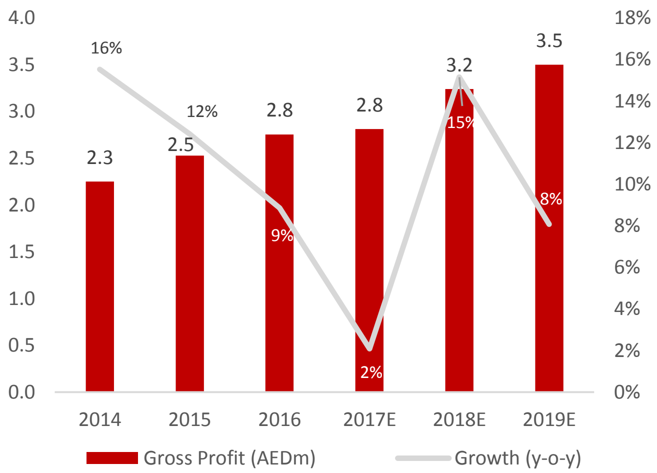
Emaar Malls (31% of 2017E gross profit) should see growth rebound in 2018/19E as The Dubai Mall (TDM) expansion starts to contribute fully to earnings. Emaar Malls witnessed growth slowdown over 2015-17E as tenant sales suffered from lower consumer/tourism spending (resulting from low oil prices and USD strengthening). Going forward, we expect organic rental growth to remain subdued, as rent increase on upcoming lease renewals (nearly 80% of leases to expire over 2017-19E) drops to reasonable levels (5% from +25% in 2015-16). However, overall growth is likely to be buoyant, as revenues from Fashion Avenue expansion kicks in.

Fig. 90. Expansion assets key trigger for Emaar Malls growth, organic growth potential limited



Source: Company, ADCB Securities Equity Research Estimates.

Fig. 91. Emaar Malls profit growth to pick up in 2018E after slowdown seen in last two years



Source: Company, ADCB Securities Equity Research Estimates.

Retail growth to sustain on doubling potential of GLA by 2021/22

After completion of fashion avenue expansion and springs village by 2018E, Emaar Malls plans to further expand TDM through Boulevard expansion, Zabeel expansion and Fountain View expansion. We have not yet included these expansions in our forecast given lack of full details. Our analysis indicate that planned extensions could add around 10% to GLA by 2019 and 6% to rental income.

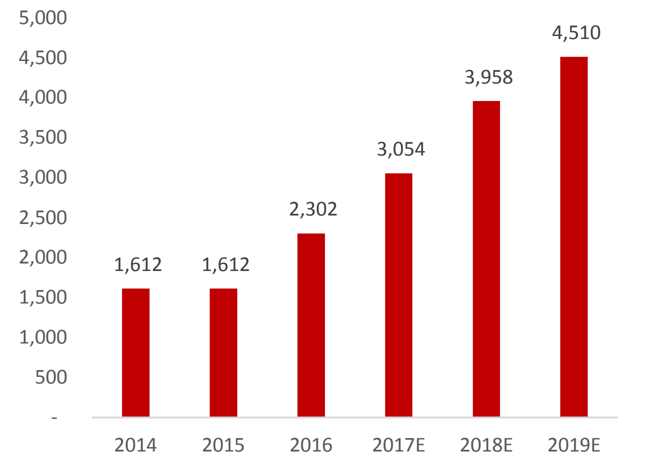
Emaar Properties has recently unveiled 2.0m sqft Dubai Hills Mall in its master planned community Dubai Hills Estate (JV with Meraas). Also various media articles have highlighted that new mall in Emaar's Dubai Creek project (JV with Dubai Holding) would be bigger than TDM, though no details have been confirmed yet. Looking at size of the two malls (~6m sqft), we see it as strong growth driver in long term (potentially near 2020). These two assets could double retail GLA and add ~25% to retail rental income (assuming 50% share in JV malls).

Aggressive expansion in hotel business continues

Total hotel rooms managed by Emaar's hospitality group saw 90% increase from 1,612 rooms in 3Q16 to 3,054 rooms in 2Q17, driven by addition of Rove brand hotels in Dubai (Emaar has 50^ share in Rove hotels). Emaar has opened four Rove brand hotels (1,246 rooms) and Address The BLVD (196 rooms) in last one year or almost doubling the rooms under management. The expansion in hotels is expected to continue at strong pace with expected addition of 904 rooms in 2018, followed by further addition of 2,651 rooms by 2021.

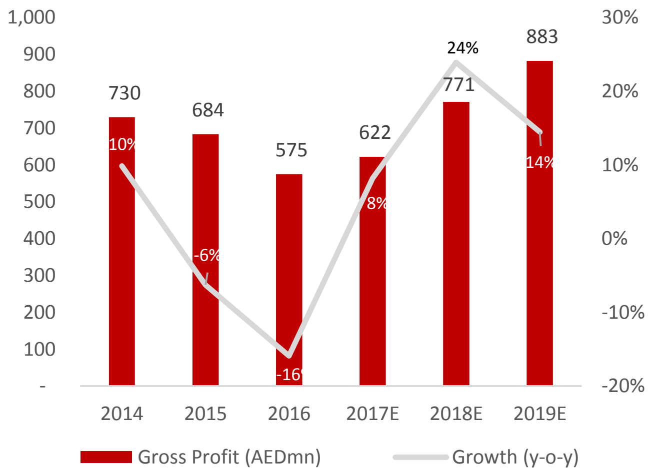
Despite factoring 5% decline in ADRs in 2017E, we expect hotel business gross profit to increase 8% y-o-y in 2017E and growth to jump 24% y-o-y in 2018E and 15% y-o-y in 2019E, mainly led by new hotels rooms.

Fig. 92. Number of hotel rooms to double by 2019E driven by Rove hotels



Source: Company, ADCB Securities Equity Research Estimates.

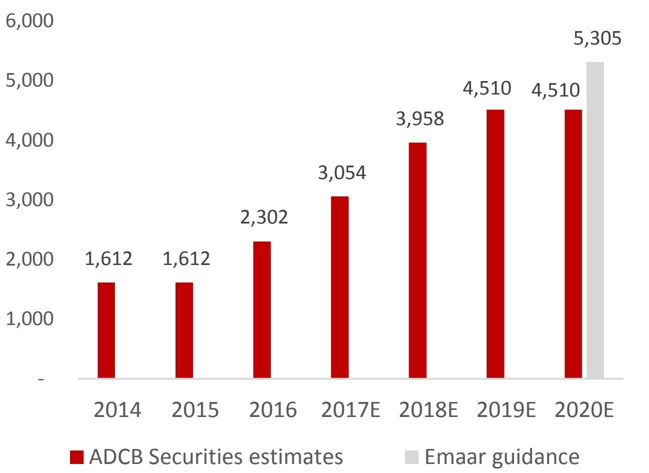
Fig. 93. Gross profit from hotel division expected to record strong growth despite pressure on market ADRs



Source: Company, ADCB Securities Equity Research Estimates.

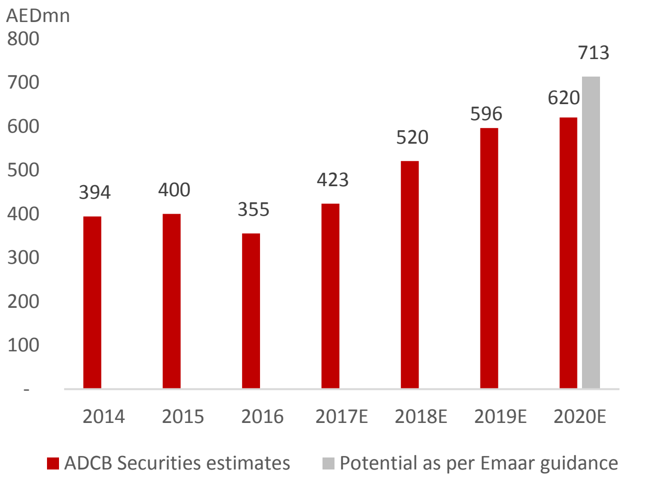
Aggressive expansion in hotels business is likely to continue beyond next two years. Emaar has recently announced addition of new hotels in master planned communities of Dubai Hills Estate, Dubai Creek Harbor and Emaar South, which will drive further growth.

Fig. 94. Hotel rooms expansion to continue beyond 2019E…



Source: Company, ADCB Securities Equity Research Estimates.

Fig. 95. …driving further upside to our EBITDA



Source: Company, ADCB Securities Equity Research Estimates.

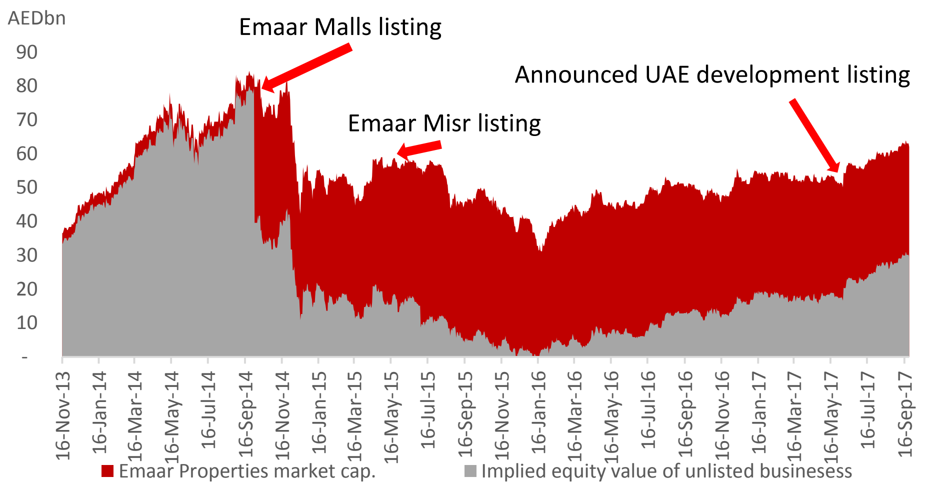
IPOs of unlisted businesses key to unlock value

Before IPO of Emaar Malls, shopping malls business used to trade at high cap rate discount. Since listing of Emaar Malls and Emaar Misr, implied discount for UAE development business (second largest contributor to valuation) has been significant. Emaar Properties management has identified listing of different business units as one of the strategic goal to unlock shareholder value. After listing Emaar Malls in 2014 and Emaar Misr in 2015, the company is pressing ahead with IPO of UAE development business.

UAE development listing acts as a strong catalyst

Emaar's UAE development business is second biggest contributor to its valuation after Emaar Malls. Its gross profit contribution of 38% is expected to be higher than Emaar Malls (31%) in 2017E. Thus, IPO of UAE development business was key awaited catalyst for stock, as market was heavily discounting its value despite strong business performance. Emaar Properties share price has reacted positively since announcement of UAE development listing.

Fig. 96. Emaar market cap and market implied equity value for residual unlisted businesses



Source: Bloomberg, ADCB Securities Equity Research.

We see continued potential for value unlocking on listing of other businesses

Listing announcement of UAE development business has triggered narrowing of its discount to fair value. Implied market cap. of unlisted businesses has since improved from AED17bn (AED2.4/share) to AED25bn (AED3.5/share). Post its listing, market implied discount for other unlisted businesses like hotels, entertainment, leisure and international development businesses would increase substantially. Netting off listed entities market cap. and JLL's 9M17 net asset value of AED24.1bn for UAE development, implied equity value for other unlisted businesses would be AED132mn. In other words, market is not recognizing value of remaining unlisted businesses, despite 31% contribution to 2017 expected gross profit. We value these businesses at AED16.2bn (AED2.3/share). We believe that listing of other businesses over next few years will be key to unlock value for Emaar shareholders and thus act as further triggers.

Fig. 97. Market implied discount for unlisted businesses

AEDmn	Current market cap.	AED/Emaar share
Emaar Properties	**55,846**	**7.8**
Less:		
Emaar Malls	24,561	3.4
Emaar Misr	3,184	0.4
Emaar Economic City	3,148	0.4
Amlak Finance	721	0.1
Implied equity value of unlisted business	**24,232**	**3.4**
Less: UAE development business net asset value (JLL)	**24,100**	**3.4**
Implied equity value of residual unlisted businesses	**132**	**0.0**
ADCB Securities estimated fair value of residual unlisted businesses	16,171	2.3
Market implied discount for residual unlisted businesses	**-99%**	

Source: Bloomberg, ADCB Securities Equity Research Estimates.

Hotel business listing could be next on the cards

Emaar Management has already hinted at listing or spinning off hotels/entertainment business at right time. Media articles have also indicated in the past about potential stake sale in its entertainment division to private equity firms. Post listing UAE development business, we expect management to focus on potential of hotel business listing in next 2 years as the business gains critical size. Hotel business should see strong growth cycle ahead and similar to other listings, we expect Emaar to consider listing of this business at right time offering a new catalyst for the stock performance.

New catalysts to support valuation above historical levels

We use sum-of-the-parts (SOTP) approach to value Emaar Properties' different businesses. Our target price for Emaar Properties stands at AED10.8/share, offering upside potential of 38% from current share price.

For development business (build to sell assets), we use DCF to value cash flows from pre-sales of projects. We use WACC of 11.4% for UAE development and 15% for international developments. We assume pre-sales till 2038 for UAE development (i.e. till current land bank is completely developed) and till 2022 for international developments. We do not use pre-sales beyond 2022 for international developments given lack of full disclosures. We do not factor any selling price increase over our forecast period.

For recurring income assets (build to lease), we use cap rate methodology by applying 7.1% yield on 2018E EBITDA for Emaar Malls and 10% yield on 2018E EBITDA for hotels, entertainment and other leasing.

For associates/JVs (excluding UAE development JVs), we use 2018E book value of investments and apply appropriate discount.

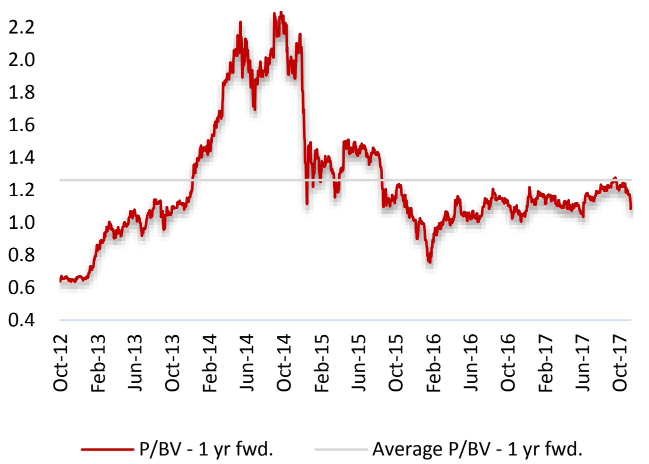
Fig. 98. Emaar Properties sum-of-the-parts (SOTP) valuation

AEDmn	Value	Value/ Share (AED)	% of assets	Valuation methodology
Investment Properties	**48,852**	**6.8**	**66%**	
Emaar Malls (84.6% stake)	34,133	4.8	46%	Cap rate of 7.1% applied on 2018E EBITDA
Emaar Entertainment and other leasing	9,913	1.4	13%	Cap rate of 10% applied on 2018E EBITDA
Emaar Hotels	4,805	0.7	6%	Cap rate of 10% applied on 2018E EBITDA
Development Properties	**22,877**	**3.2**	**31%**	
Emaar UAE Development	17,785	2.5	24%	DCF @ WACC of 11.4%, Pre-sales assumed till 2038
Emaar International Development	2,508	0.4	3%	DCF @ WACC of 15%, Pre-sales assumed till 2022, no value for residual land
Emaar, The Economic City (30.6% stake)	2,584	0.4	3%	At book value, implying 20% discount to market cap.
Associates & JVs	**2,159**	**0.3**	**3%**	
Amlak Finance PJSC (48.1% stake)	707	0.1	1%	At book value, implying 0% discount to market cap.
Emaar Industries & Investment (40% stake)	114	0.02	0%	At 20% discount to book value
Dead Sea Company (29.3% stake)	93	0.01	0%	At 20% discount to book value
Emaar Bawadi LLC (50% stake)	375	0.05	1%	At 20% discount to book value
Turner International Middle East (65% stake)	265	0.04	0%	At 20% discount book value
Mirage Leisure & Development (65% stake)	107	0.02	0%	At 20% discount to book value
Other Associates (50% stake)	497	0.07	1%	At 20% discount to book value
Total Enterprise Value	**73,888**	**10.3**	**100%**	
Add: Financial Investments	1,620	0.2		At 2018E BV
Add: Cash & cash Equivalents	16,564	2.3		At 2018E BV, adjusted for minority stakes in Emaar Malls, Emaar Misr
Less: Total Debt	(15,099)	(2.1)		At 2018E BV, adjusted for minority stakes in Emaar Malls, Emaar Misr
Equity value	**76,973**	**10.8**		
No. of outstanding shares (mn)	7,160			
Target price per share (AED)	**10.8**			
Current share price (AED)	7.8			
Upside / downside (%)	38%			

Source: ADCB Securities Equity Research Estimates.

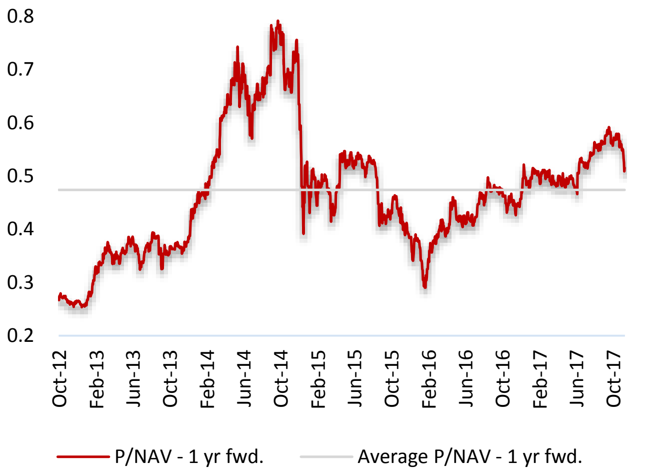
The stock is trading at a P/BV of 1.1x 2018E, in line with emerging market peers and 13% discount to historical average. Emaar trades at 2018E P/NAV of 0.52x or 10% above historical average. At our target price, the stock would trade at 1 year fwd. P/BV of 1.5x and P/NAV of 0.7x. High growth profile, listing of UAE development business and potential listing of other businesses should continue to unlock value for shareholders, supporting higher than historical valuation.

Fig. 99. Emaar Properties trading at a 1 yr. fwd. P/BV of 1.1x, 13% discount to historical levels



Source: Bloomberg, ADCB Securities Equity Research Estimates.

Fig. 100. And 1 yr. fwd. P/NAV of 0.52x or 10% above historical levels



Source: Bloomberg, ADCB Securities Equity Research Estimates.

Potential valuation of UAE development business

We value this business at an enterprise value (EV) of AED17.8bn. 9M17 proforma net cash of UAE development business (adjusting for new borrowings and upstream of AED4.0bn dividend to parent company) stood at AED6.2bn. This results in an equity value of AED23.9bn or AED3.3/share (31% of our target price). Note that our valuation of UAE development business reflects value for Emaar Properties shareholders and not Emaar Development shareholders. Emaar Development would additionally benefit from management fee earned on built to lease (BTL) / built to operate (BTO) assets, as well as on management of certain JV projects (Emaar South and Zabeel Square). Emaar Development also benefits from funding provided by Emaar Properties for infrastructure development in Dubai Creek Harbour project, as well as lower general & administration expenses related to shared services. As per 2016 results presentation, Gross Profit and EBITDA of UAE development business stood at AED2.9bn and AED2.0bn respectively. This implies SG&A of AED826mn. However, as per Emaar Development's financials, 2016 SG&A expenses stood at AED577mn or 30% lower than Emaar's UAE development business.

Fig. 101. Emaar's estimated UAE development business valuation

	AEDmn	AED/share
Enterprise value	17,785	2.5
Net cash / (debt)	6,153	0.9
Equity value	**23,938**	**3.3**

Source: ADCB Securities Research Estimates.

Sensitivity of UAE development business valuation to pre-sales

In our forecast (as shown in Figure 77), we estimate pre-sales to decline from peak 2017 levels. If pre-sales is sustained at current run-rate (as expected by management), we see an upside of 20% to our valuation of UAE development business and 6% upside to Emaar Properties target price. Following table shows sensitivity of UAE development business valuation and Emaar's target price at different levels of annual pre-sales.

Fig. 102. UAE development business valuation and Emaar's target price sensitivity to pre-sales

	Historical 2000-16	Forecast 2017-38E						
Pre-sales p.a. (AEDmn)	**8,312**	**9,179**	**11,221**	**12,833**	**14,117**	**15,685**	**17,646**	**20,167**
No. of years of pre-sales		28	25	22	20	18	16	14
Equity Value (AEDmn)		**20,312**	**22,165**	**23,938**	**25,482**	**26,812**	**27,945**	**28,911**
Equity Value (AED/share)		**2.8**	**3.1**	**3.3**	**3.6**	**3.7**	**3.9**	**4.0**
Emaar target price (AED/share)		**10.2**	**10.5**	**10.8**	**11.0**	**11.2**	**11.3**	**11.4**

Source: ADCB Securities Equity Research Estimates.

Sensitivity of UAE development business valuation to margin

In our forecast, we estimate gross profit margin of 37% on development pipeline. Following table shows sensitivity of UAE development business valuation and Emaar's target price at different levels of gross profit margin.

Fig. 103. UAE development business valuation and Emaar's target price sensitivity to gross margin

Development pipeline gross profit margin	**33%**	**34%**	**36%**	**37%**	**39%**	**41%**	**42%**
Equity Value (AEDmn)	**21,594**	**22,376**	**23,157**	**23,938**	**24,719**	**25,500**	**26,282**
Equity Value (AED/share)	**3.0**	**3.1**	**3.2**	**3.3**	**3.5**	**3.6**	**3.7**
Emaar target price (AED/share)	**10.4**	**10.5**	**10.6**	**10.8**	**10.9**	**11.0**	**11.1**

Source: ADCB Securities Equity Research Estimates.

Key risks

Decline in oil prices and US$ strengthening could delay recovery in Dubai property market. This would dampen the prospects of stability in tenant sales at its retail portfolio and daily rooms rates for its hotel business, slowing down earnings growth. Emaar's ability to sustain pre-sales at high levels or achieve desired margins in its new master developments would also be restricted amid continued tough market conditions. Lastly, higher than expected upfront infrastructure/other capex on new master developments would impact its cash flows.

EMAAR MALLS

Quality retail exposure

Initiate coverage with a Buy

Real Estate | UAE | 12 November 2017

We initiate coverage on Emaar Malls with a Buy rating and a target price of AED2.9, an upside of 30%. Emaar Malls is a pure play on Dubai's retail story, which is driven by population and tourism growth. YTDSept2017, tourism growth has picked up supported by US$ weakening, allowing visa on arrival for Russian/Chinese visitors and improvement in global growth prospects. Steady oil prices should limit further downside on spending by resident population and GCC tourists. Moreover, we expect Emaar Malls' high quality asset - The Dubai Mall (84% of Emaar Malls' rent) to emerge fairly resilient to key sector concerns of potential over supply and rising e-commerce penetration. Emaar Malls entry into e-commerce through Namshi should also help to offset slowdown in store based retail sales. The stock is trading at discounted valuation to peers and its historical levels, which we view unwarranted amid near term earnings catalyst and dividend growth potential.

Uniquely positioned to benefit from tourism uptick

Dubai tourism activity has picked up in YTDSept2017 with a growth of 8.6% after 4.9% in 2016. US$ depreciation against major currencies coupled with increasing retail discounts/lower hotel room rates have made Dubai less expensive for tourists. Dubai government's initiative to allow visa on arrival for Russian/Chinese visitors and improving global growth prospects also aided tourism performance. Emaar Malls' relatively higher gearing to tourism helped it to record footfall growth of 7% in 1H17 (after no growth in 2016) and stability in tenant sales (after mid-single digit decline in 2016).

Rising supply and e-commerce penetration are key sector risks

Retail supply in Dubai is expected to accelerate with upcoming supply 2.4x higher than historical average. Retail stock could increase by 9.2% p.a. over 2016-19E, much higher than 4.1% p.a. over 2011-16. Adding to supply risk is increasing e-commerce penetration, a key emerging theme likely to impact retail industry. Globally, store based retail sales suffered slowdown as e-commerce gained traction. Few segments like electronics, apparel and home furniture/furnishings face risk of sharper slowdown than others. We expect similar effect to be seen in UAE retail sector as e-commerce momentum sustains. This could weigh on retail rents and occupancies.

The Dubai Mall likely to be more resilient than secondary malls

In light of e-commerce threat, retailers are likely to consolidate stores to sustain profitability. However, they would continue to focus on prime locations with high trading density (sales/sqft) and footfall. The Dubai Mall enjoys all the advantages, retailers are looking to compete with online. Thus, we see it to be more resilient to e-commerce threat than secondary malls, which could bear greater burden of reduction in rents or higher vacancies.

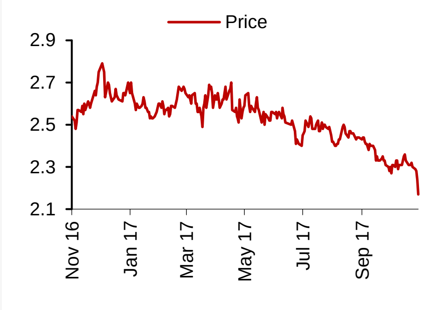
Strong earnings growth ahead, valuation discount unwarranted

The stock is trading at 2018E P/NAV of 0.6x, discount of 43% to global peers and 23% to its historical average. 2018E implied EBITDA yield is 9.3%, discount of 400bps to global peers. We see its discount to narrow given superior earnings profile (11% CAGR over 2016-19E vs. 3% for global peers), driven by completion of Fashion Avenue expansion. In long term, Emaar Malls is likely to maintain its high growth status owing to option to acquire retail assets from parent Emaar Properties. Lastly, we see dividends increasing by 14% CAGR over 2017-19E (yielding 5.4% in 2018E / 6% in 2019E) on higher EBITDA generation post expansion.

Fundamentals

Recommendation	Buy
Target Price	AED 2.9
Price	AED 2.23
Price 12m High/Low	AED 2.79/2.17
Market Cap.	AED28,241mn
Bloomberg/Reuters	EMAARMLS UH / EMAA.DU

Price Performance Chart



Source: Bloomberg

Equity Research Team

Yugesh Suneja (+971 2 3050838)
yugesh.suneja@adcb.com

Nikhil Poddar, CFA (+971 2 696 6450)
nikhil.poddar@adcb.com

Financials

Income Statement (AEDmn)	2016	2017E	2018E	2019E
Revenue	3,228	3,278	3,789	4,094
EBITDA	2,444	2,512	2,880	3,113
Depreciation and amortization	372	386	426	428
EBIT	2,072	2,126	2,454	2,685
Other income	0	0	0	0
Net Finance Cost	197	191	175	153
Profit before tax	1,874	1,935	2,278	2,532
Taxes	0	0	0	0
Minority interest	0	0	0	0
Net profit	1,874	1,935	2,278	2,532

Source: ADCB Securities Equity Research

Balance Sheet (AEDmn)	2016	2017E	2018E	2019E
Cash and cash equivalents	3,551	3,843	4,804	5,962
Other current assets	435	425	446	468
Total non-current asset	204	174	150	131
Total assets	25,408	25,944	26,955	28,002
Total current liabilities	2,031	1,934	1,968	2,016
Borrowings	7,296	7,296	7,296	7,296
Other non-current liabilities	61	61	61	61
Total liabilities	9,389	9,291	9,326	9,374
Minority interest	0	0	0	0
Shareholders` equity	16,019	16,652	17,629	18,629
Total net debt	3,746	3,453	2,492	1,334

Source: ADCB Securities Equity Research

Cash flow statement (AEDmn)	2016	2017E	2018E	2019E
Cash flow from operations	2,626	2,425	2,893	3,139
Net capex	749	640	455	295
Free cash flow	1,877	1,785	2,438	2,844
Net financing	(266)	(280)	(280)	(280)
Change in cash	381	293	961	1,158

Source: ADCB Securities Equity Research

Valuation and leverage metrics	2016	2017E	2018E	2019E
P/E (x)	15.1	14.6	12.4	11.2
P/BV (x)	1.8	1.7	1.6	1.5
P/FFO (x)	12.6	12.2	10.4	9.5
FCF yield (%)	6.6	6.3	8.6	10.1
Dividend Yield (%)	4.6	4.6	5.4	6.0
EV/EBITDA (x)	13.1	12.6	10.7	9.5
Interest coverage (x)	7.5	7.6	8.8	9.6
Net debt/equity (x)	0.23	0.21	0.14	0.07
Net debt/EBITDA (x)	1.5	1.4	0.9	0.4

Source: ADCB Securities Equity Research

Key Ratios (%)	2016	2017E	2018E	2019E
ROAIC	9.3	9.4	10.5	11.1
RoAE	11.9	11.8	13.3	14.0
Revenue growth	7.9	1.6	15.6	8.1
EBITDA growth	9.1	2.8	14.6	8.1
EPS growth	13.2	3.2	17.8	11.1
EBITDA margin	75.7	76.6	76.0	76.0

Source: ADCB Securities Equity Research

Per-share data (AED)	2016	2017E	2018E	2019E
EPS	0.14	0.15	0.18	0.19
DPS	0.10	0.10	0.12	0.13
BVPS	1.23	1.28	1.35	1.43
Total no. of outstanding shares (mn)	13,014	13,014	13,014	13,014

Source: ADCB Securities Equity Research, Emaar Malls financials does not reflect consolidation of its 51% stake in Namshi pending full disclosures

Investment case

Emaar Malls is a pure play on Dubai's retail story, which is driven by Dubai's attractive tourism proposition and population growth. YTDSept2017 saw easing of headwinds as tourism growth picked up, supported by US$ weakening, easing of visa restrictions and improvement in global growth outlook. Steady oil prices should limit further downside in spending by resident population and GCC tourists. The Dubai Mall should also be more resilient to supply and e-commerce risks, underpinned by its prime location, strong footfall and high trading density.

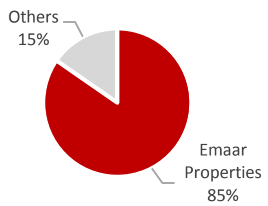
Upside case — AED3.2

Improvement in tourist and domestic spending driven by firm oil prices and continued weakness in US$. In such a scenario, Emaar Malls could see higher tenant sales and rise in turnover rent, leading to better earnings growth than currently envisaged. The stock would trade at 2018E EBITDA yield of 7% in this case.

Downside case — AED2.1

US$ strengthening and lower oil prices will further constraint spending from tourists and population, denting prospects of recovery or stabilization in tenant sales. This would restrict its ability to increase base rents or could even push base rents lower. In such a scenario, market implied discount to cap rate is also likely to sustain. The stock would trade at 2018E EBITDA yield of 9.5% in this case.

Fig. 2. Shareholding pattern



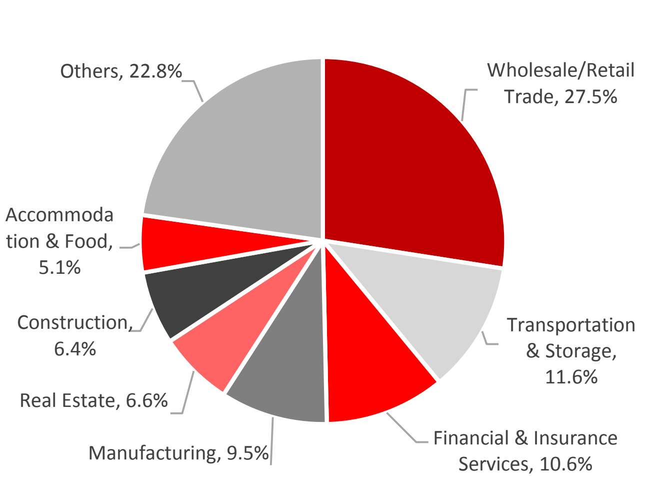
Source: DFM, ADCB Securities Equity Research

A unique exposure to Dubai's retail story

Dubai offers attractive tourism proposition…

Emaar Malls is a pure play on Dubai's retail story, which is driven by Dubai's attractive tourism proposition and population growth. Tourism is one of the key pillars of Dubai government's strategy to boost its economic growth. Dubai is a key tourism hub in the Middle East and Indian sub-continent. One third of the world's population lives within a four hour flight radius and two-thirds within an eight hour flight radius, thereby attracting large tourists from catchment areas of GCC, India, China and Africa.

Fig. 104. Retail/wholesale trade accounts for 28% of Dubai's GDP - 2016



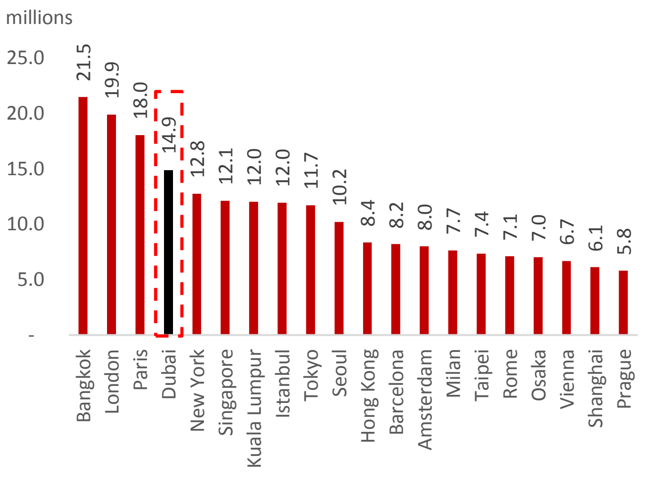
Source: Dubai Statistics Centre, ADCB Securities Equity Research.

Fig. 105. Dubai's air connectivity – 1/3rd of world's population in 4 hour flight radius and 2/3rd within 8 hour flight radius

Source: Dubai Airports, ADCB Securities Equity Research.

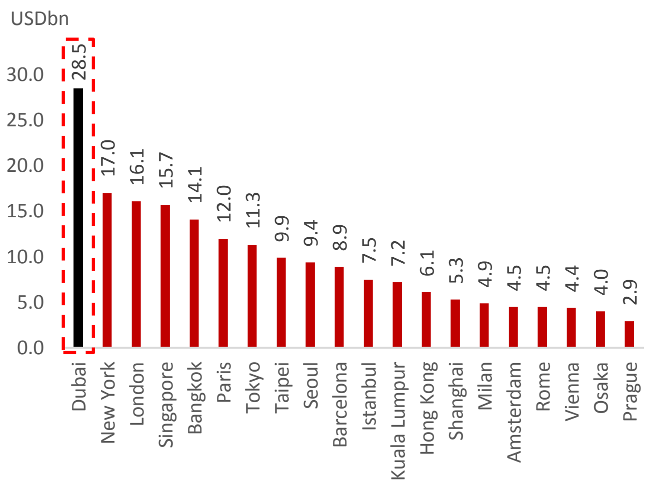
As per Mastercard, Dubai is ranked no. 4 among all global destination cities in terms of number of visitors while ranked no. 1 in terms of total tourist spending. Dubai has one of the highest spending per tourist. Dubai's tourism success has been primarily driven by its well-equipped infrastructure, increasing number of tourist destinations, retail offerings and a "safe haven" status. Also, higher disposable income amongst Emirati's and expatriates, compared to other retail destination, has helped the emirate to develop a buoyant retail sector.

Fig. 106. Global cities by number of tourists - Dubai ranked 4th in 2016



Source: Master Card Worldwide, ADCB Securities Equity Research.

Fig. 107. Global cities by tourist spending - Dubai ranked at the top in 2016



Source: Master Card Worldwide, ADCB Securities Equity Research.

… new initiatives to support tourism growth

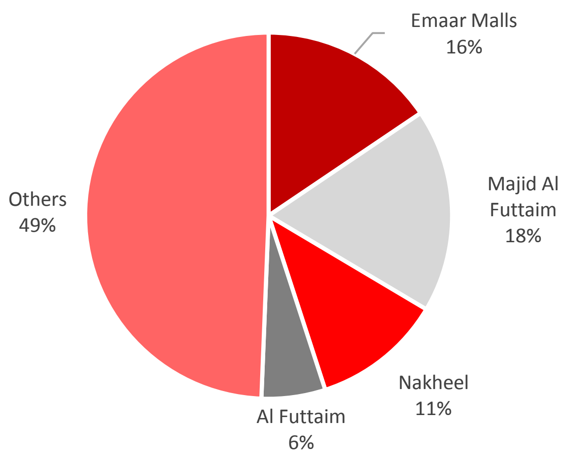
Dubai has successfully pioneered the concept of retail tourism through its retail offerings, hotels, beaches, and unique experiences such as Burj Khalifa, Dubai Fountain, Desert safaris, old fashioned souks and most recently Dubai Parks and Dubai Opera. Dubai government remains firmly committed to support leisure tourism (c.80% of total tourism GDP, 20% is business travel). It has planned large-scale public and private investments into tourism enablers – airports, hotels, transport infrastructure, new attractions (theme parks/safari, cultural avenues). Moreover, government is working to make Dubai more affordable tourist destination. Government is targeting to increase mid-market hotels in pipeline to attract more visitors from mass markets like India and China.

The Dubai Mall: a key destination mall

Emaar Malls portfolio comprises of two major shopping malls (The Dubai Mall and Dubai Marina Mall), specialty retail (Souk Al Bahar and Gold and Diamond Park) and community retail. Emaar Malls represent 16% of Dubai's retail GLA and retail sales across its portfolio contribute ~5% to Dubai's GDP. The Dubai Mall accounts for 50% of luxury goods sold in Dubai, highlighting its prominence among shoppers.

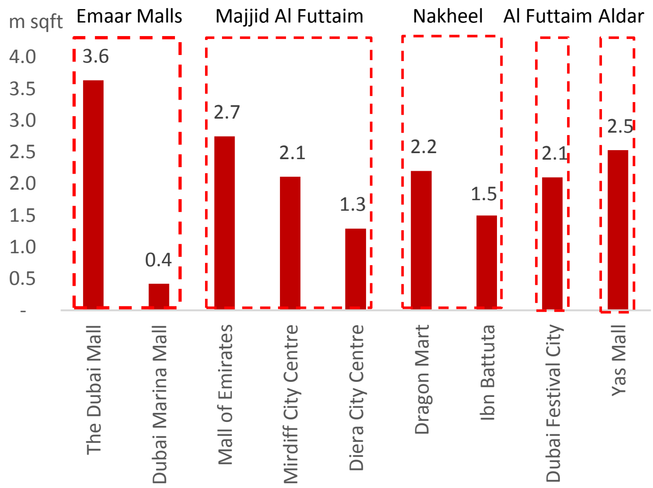
Its flagship asset 'The Dubai Mall (TDM)' is a key destination mall located centrally in Dubai. TDM accounts for 62% of Emaar Malls' total gross leasable area but 84% of its rental income owing to higher rent/sqft it generates. TDM is a gateway to visit the world's tallest building 'Burj Khalifa' and The Dubai Fountain. TDM also includes other key tourist attractions - Underwater Zoo and Aquarium, Ice Rink, Kidzania, thereby attracting strong footfalls. TDM draws its strength by offering tourists (contributing to nearly 40% of retail sales at mall) the first choice for luxury shopping. It is also well positioned to attract strong interest from population given optimum mix of retailers across fashion, jewellery & watches, apparel, electronics, leisure & entertainment segments.

Fig. 108. Emaar Malls represents 16% of Dubai's retail GLA



Source: Company, ADCB Securities Equity Research Estimates.

Fig. 109. The Dubai Mall is largest shopping mall in MENA region



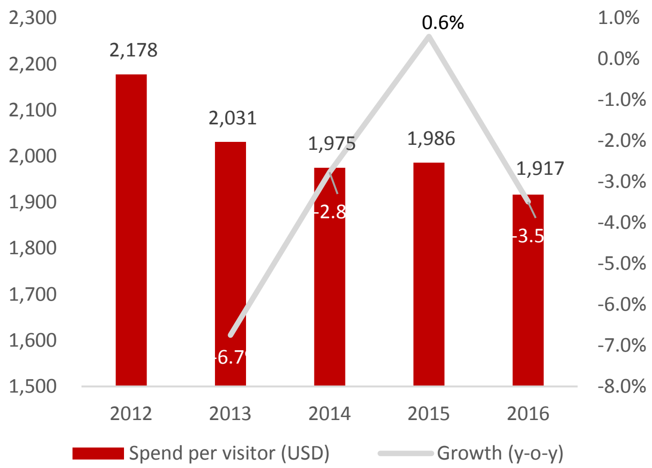
Source: Company, ADCB Securities Equity Research Estimates.

Tourism growth has picked up driven by USD weakening and improving global growth

Tourism, in addition to population demand, plays a key role in driving Dubai's retail sector. Dubai tourism has picked up in YTDSept2017 with number of tourists increasing by 8.6% y-o-y (after 4.9% in 2016). USD weakening has made Dubai less expensive for tourists from India, UK, Europe etc., which account for top source markets for Dubai tourism. Dubai government's initiative of allowing visa on arrival for Chinese and Russian visitors has boosted growth of visitors from these countries.

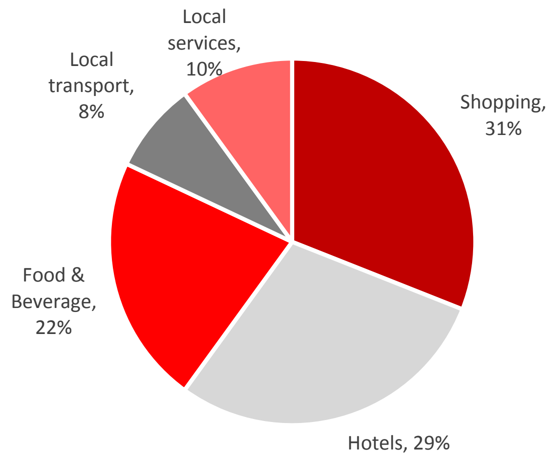
In 2015-16, retail sector saw increasing pressure, impacted by slowdown in consumer and tourist spending. Low oil prices curtailed economic growth in GCC countries, impacting spending by resident population as well as GCC tourists. US$ strengthening also affected international tourists spending adding to regional pressure.

Fig. 110. Spend per tourist in Dubai – low oil prices and US$ strengthening impacted spending in 2016



Source: Master Card Worldwide, ADCB Securities Equity Research.

Fig. 111. Shopping and hotels are two largest buckets of spending by visitors and thus likely to have impacted most



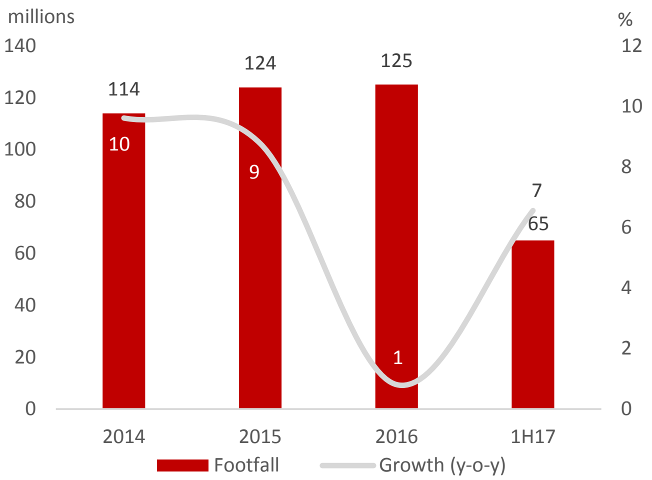
Source: Master Card Worldwide, ADCB Securities Equity Research.

Going forward, improving global growth prospects bode well to lift tourism performance. Tourists from MENA region continued to decline YTDAug2017, but stable oil prices and gradual easing of GCC governments' austerity drive should limit further downside. Saudi government has already reinstated bonuses for public sector employees in April 2017. Recently, Saudi Arabia's Finance Minister indicated that the country will slow down on pace of reforms in line with IMF recommendations.

Emaar Malls benefitted from pick up in tourism

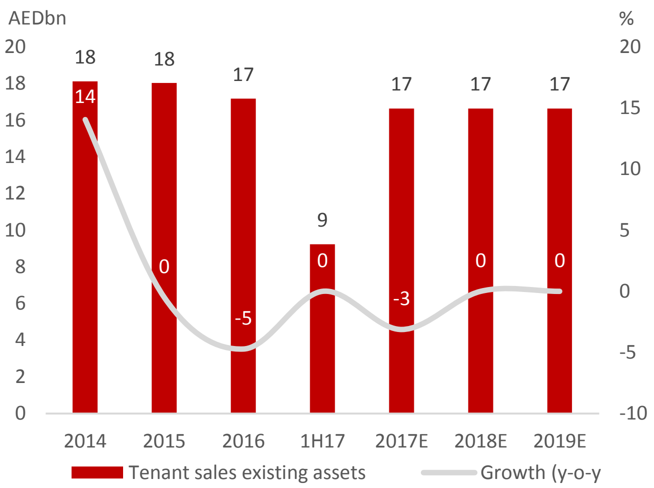
Emaar Malls being highly geared to tourism also benefitted from positive tourism growth. Footfall at Emaar Malls' portfolio has strengthened by 7% in 1H17 after no growth in 2016. Tenant sales at Emaar Malls' portfolio has stabilized after witnessing mid-single digit decline in 2016. We are still cautious on tenant sales for 2017 and expect it to decline by 3% y-o-y. However, we expect tenant sales to stabilize in 2018 and factor no growth thereafter.

Fig. 112. Emaar Malls footfall – growth returns in 1H17



Source: Company, ADCB Securities Equity Research.

Fig. 113. Emaar Malls tenant sales – stabilized in 1H17



Source: Company, ADCB Securities Equity Research.

Retail outlook cautious, TDM to be more resilient

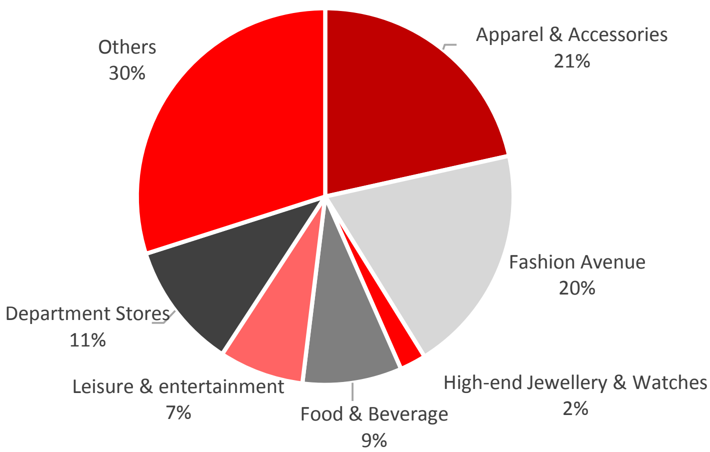
While headwinds have eased for retail sector, domestic consumption and tourism spending are likely to remain challenged by continued low oil price environment and risk of US$ strengthening. We therefore remain cautious on demand growth going forward. Amid subdued demand, higher upcoming supply and rising e-commerce penetration could keep a check on recovery in retailers' sales performance (detailed analysis on retail sector outlook, P-17 and P-19).

TDM stands to benefit from changing market dynamics, secondary locations more at risk

In light of e-commerce threat, retailers are likely to consolidate stores to sustain profitability. However, they would continue to focus on prime locations with high trading density (sales/sqft) and footfalls.

Among key primary malls, TDM enjoys a strong attraction for retailers. TDM has highest mall footfalls in the world and offers strong exposure to tourism. Moreover, tenant mix at TDM is more balanced that makes it less prone to e-commerce threat. Thus, we see TDM to be more resilient than secondary malls, which could bear greater burden of reduction in rents or higher vacancies.

Fig. 114. The Dubai Mall retail mix is more balanced



Source: Company, ADCB Securities Equity Research.

Emaar Malls entry into e-commerce to cushion slowdown in store based retailing

With online sales continuing to increase at solid pace and expected to double in next five years, retailers are adapting to the challenges in order to survive. The retail response appears to be investment in developing multiple channels. The multi-channel approach means that retailers are ideally indifferent to where a purchase occurs, in person or online.

The growth of the online retail market may also have an impact on the relationship between landlords and tenants. The bargaining power of tenants in negotiating with landlords will increase. Mall owners across developed world in USA or Europe have adopted digital strategy to engage more with consumers and provide further convenience of shopping like apps that help customers find what they are looking for, parking guidance systems etc. to differentiate their assets.

In May 2017, Emaar Malls acquired 51% stake in Namshi at AED554mn. With Namshi's acquisition, Emaar Malls aims to offer alternative digital platform to tenants across its portfolio. This is to leverage on changing market dynamics and growth in online sales. In our view, this strategy is also likely to protect the downside from lower growth in tenants sales at stores.

Namshi acquisition expected to be earnings accretive, no significant capex expected to expand platform

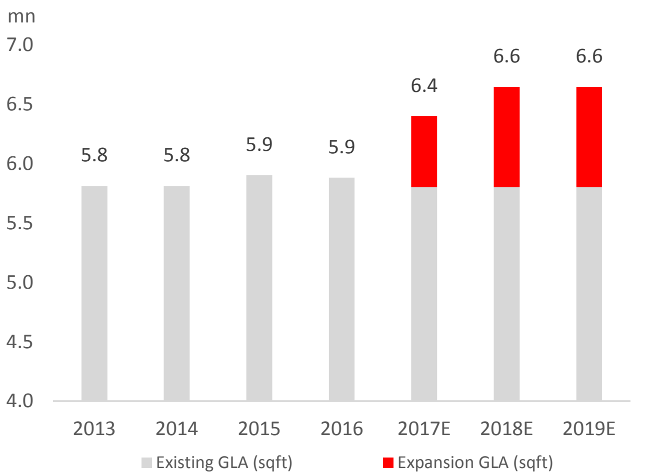
As per disclosures made by Emaar Malls, Namshi recorded revenues of AED555mn in 2016 and also turned profitable for the first time. More disclosures on Namshi's recent performance (consolidated from 16th August 2017) will be available on release of 3Q17 full financial statements (expected by next week). Based on preliminary 3Q17 result disclosures, we expect this acquisition to be earnings accretive for Emaar Malls, unlike other e-commerce players which are estimated to be running in losses. As per our discussion with the management, acquisition cost includes investment in the company for its future growth and there is no significant capex planned for Namshi.

Emaar Malls to record superior earnings growth

Earnings growth mainly driven by fashion avenue expansion

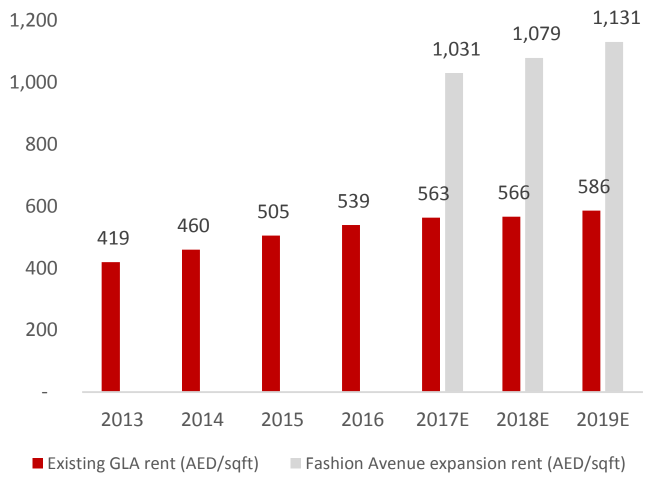
Emaar Malls' earnings grew at a solid rate of 31% CAGR over 2012-15, but momentum slowed down in 2016 (+13%) and 2017E (+5%). However, Emaar Malls' growth should see strong rebound in 2018E as Fashion Avenue expansion (+10% to GLA) starts by 2017 end. While Fashion Avenues' contribution to GLA is 10%, its contribution to rental income is expected to be 20% given its rents are almost double the existing portfolio.

Fig. 115. Fashion Avenue expansion to add 10% GLA by 4Q17 and Springs Village will add another 4% by 2Q18



Source: Company, ADCB Securities Equity Research Estimates.

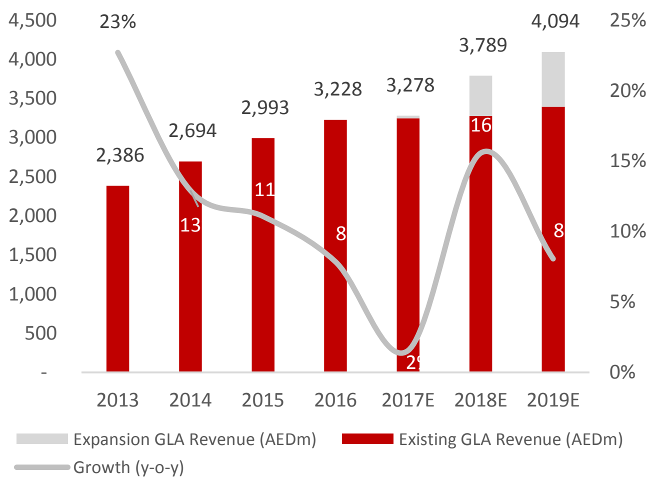
Fig. 116. Fashion Avenue expansion rents almost double the existing portfolio rent



Source: Company, ADCB Securities Equity Research Estimates.

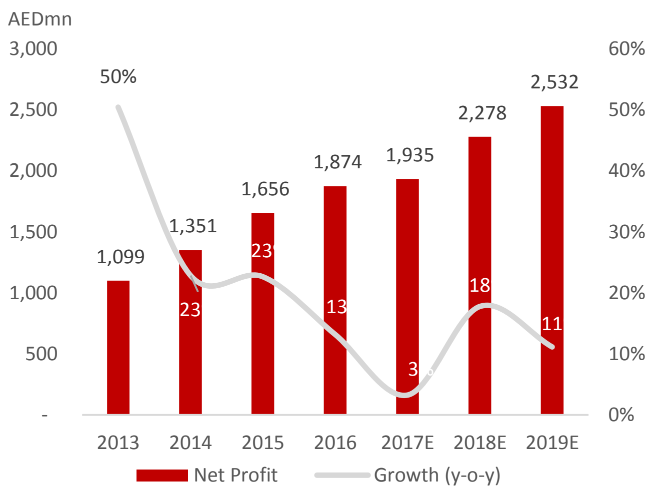
We expect Emaar Malls' net profit to grow at 11% CAGR over 2016-2019E, higher than 3% CAGR expected for global peers.

Fig. 117. Rental growth to return as Fashion Avenue expansion starts to contribute in 2018/19E



Source: Company, ADCB Securities Equity Research Estimates.

Fig. 118. Earnings to rebound in 2018/19E on the back of rental contribution from Fashion Avenue expansion

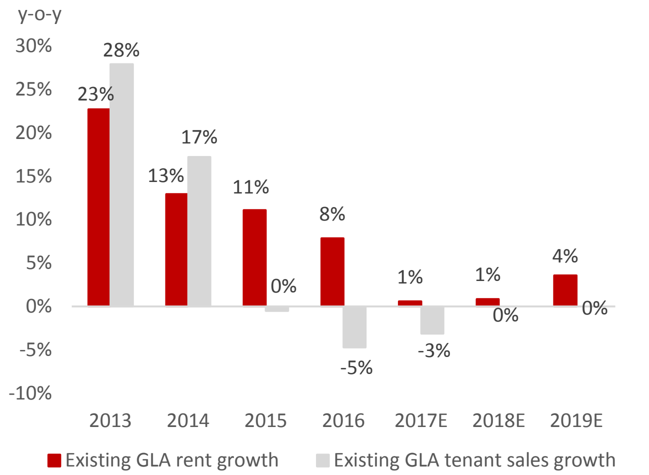


Source: Company, ADCB Securities Equity Research Estimates.

Base rents escalation could continue, occupancy cost not a real threat

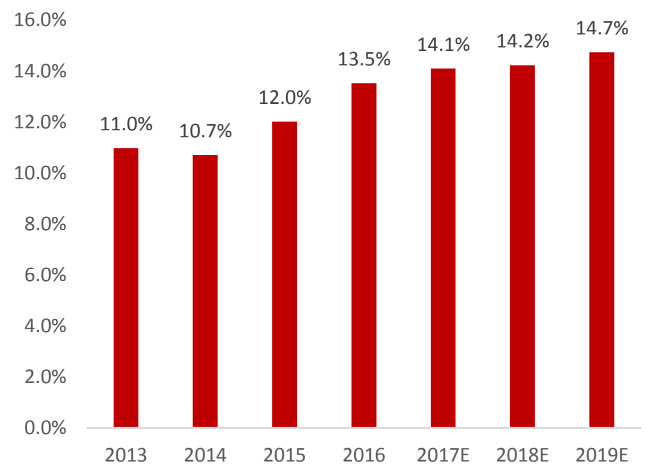
Emaar Malls' occupancy cost ratio increased from 11% in 2013 to 13.5% in 2016 as rental growth (+16% p.a. over 2011-16) outpaced tenants' sales (+11% CAGR). However, it is still broadly in line with global malls (~13%). We expect base rent escalation of 5% in 2017/18/19E. Despite increase in base rent, total rental income should remain same in 2017/18E as turnover rent (7% of total rent in 2016) would be converted to base rent as per rental structure. If base rent continues to grow in 2019E and tenant sales remain flat, overall rent is likely to increase modestly in 2019E. However, increase in occupancy cost would still be manageable. Emaar Malls' main asset, the Dubai Mall, is a high quality asset generating solid footfall (most visited mall in the world), higher trading density (retail sales per sqft) than other global locations and a key channel for retailers to capture high tourist spending in Dubai. Thus, we see retailers willing to bear slightly higher occupancy cost than global locations. Thus, we do not see any threat to minimum base rent escalations and expect it to continue supporting total rental income despite reduced turnover rents.

Fig. 119. Rentals outpaced tenant sales since 2015, we expect flat rent in 2017/18E and moderate increase in 2019E



Source: Company, ADCB Securities Equity Research Estimates.

Fig. 120. Occupancy cost increased since 2015, expected to remain manageable with 5% p.a. base rent increase



Source: Company, ADCB Securities Equity Research Estimates.

We also highlight here that occupancy cost derived from headline rental and tenant sales does not accurately reflect true occupancy cost of retailers. Headline sales does not include tenants like banks, currency exchanges, temporary kiosks, medical clinics and community facilities (laundry etc.), although all these tenants contribute to rents. Our analysis reveals that there is a ~25% variation in true occupancy cost and headline occupancy cost, which investors should consider to gauge ability of Emaar Malls to increase base rents.

Fig. 121. How reported occupancy cost is different from calculated – example from last reported data as of 9M15

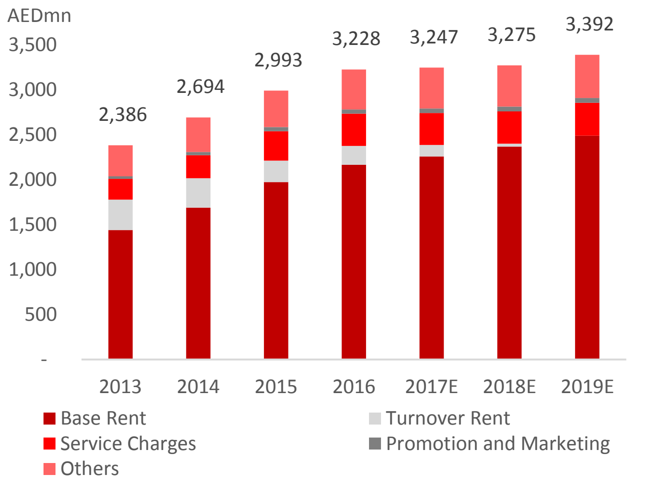
Retail Sales (AEDmn) - 9M15	13,500	Rental Income (AEDmn) - 9M15	2,172		
Net leasable GLA (sqft)	5,683,200	Net leasable GLA (sqft)	5,683,200		
Annualized Retail sales (AED/sqft) - calculated (A)	3,167	**Annualized Rent (AED/sqft) - calculated (C)**	509	**Occupancy cost - calculated (C / A)**	16%
Annualized Retail sales (AED/sqft) - reported (B)	4,216	**Annualized Rent (AED/sqft) - reported (D)**	491	**Occupancy cost - reported (D / B)**	12%
% difference (reported vs. calculated)	**33%**	**% difference**	**-4%**	**% difference**	**-28%**

Source: Company, ADCB Securities Equity Research.

Rental income from existing assets is expected to stay flat in 2017/18E as increase in base rents is offset by reduction in turnover tent. Moderate increase in existing assets rental income is expected in 2019E, as base rents continue to increase.

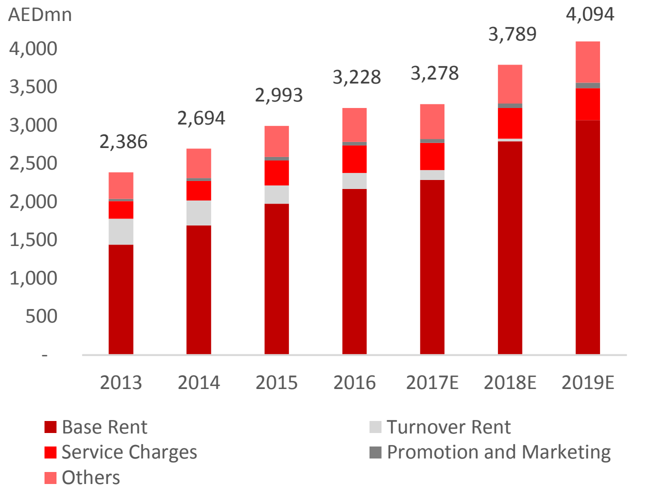
Total rental income growth should be mainly supported by base rent contribution of expansions assets (Fashion Avenue expansion and Springs Village).

Fig. 122. Rental income from existing assets – flat in 2017/18E, modest growth expected in 2019E



Source: Company, ADCB Securities Equity Research Estimates.

Fig. 123. Total rental income expected to grow mainly due to base rent contribution of expansion assets

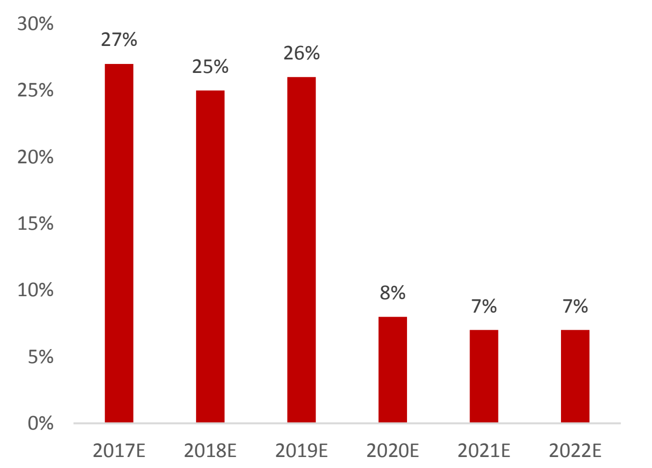


Source: Company, ADCB Securities Equity Research Estimates.

Rent increase on lease renewals expected to moderate

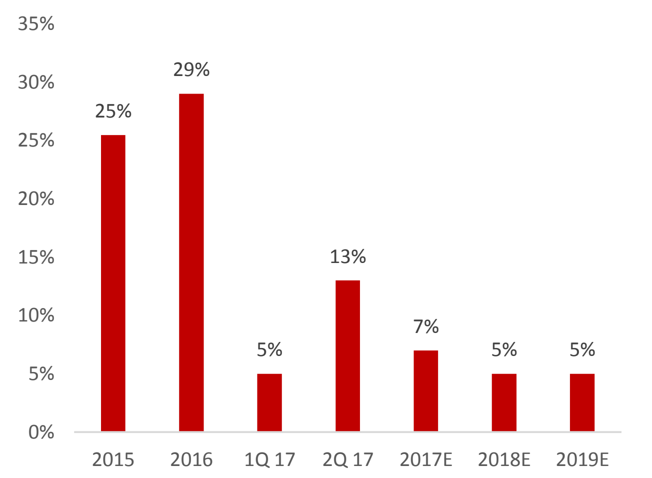
Over 2017-19E, 78% of GLA is due for renewal. In 2015/16, Emaar Malls had been able to increase rentals by more than 25% on lease renewals. However, we believe that rent increase on upcoming renewals is likely to fall to more reasonable levels (already reached 10% in 1H17) given more challenging retail conditions. We factor 5% increase in rentals on upcoming lease renewals. This should result in relatively modest growth in rental income over next few years.

Fig. 124. 78% of GLA is due for renewal over 2017-19 (as of Dec 2016)



Source: Company, ADCB Securities Equity Research.

Fig. 125. Rent increase on lease renewals expected to fall to more reasonable levels



Source: Company, ADCB Securities Equity Research.

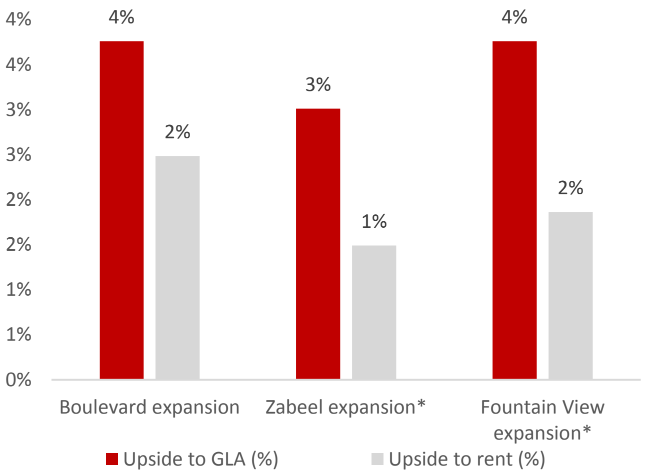
Strong relationship with parent could facilitate further acquisitions

- **Planned expansions offer limited growth…**

After completion of fashion avenue expansion and springs village by 2018E, Emaar Malls plans to further expand TDM through Boulevard expansion, Zabeel expansion and Fountain View expansion. Boulevard expansion will be directly undertaken by Emaar Malls, while other extensions would be funded by Emaar Properties. As per arrangement between Emaar Malls and Emaar Properties, Emaar Malls will have the first right of refusal on any retail project that the parent company undertakes. Once retail projects undertaken by Emaar Properties are 70% pre-leased, Emaar Malls can opt to buy these assets from parent company at an average of fair value arrived by two independent valuation companies.

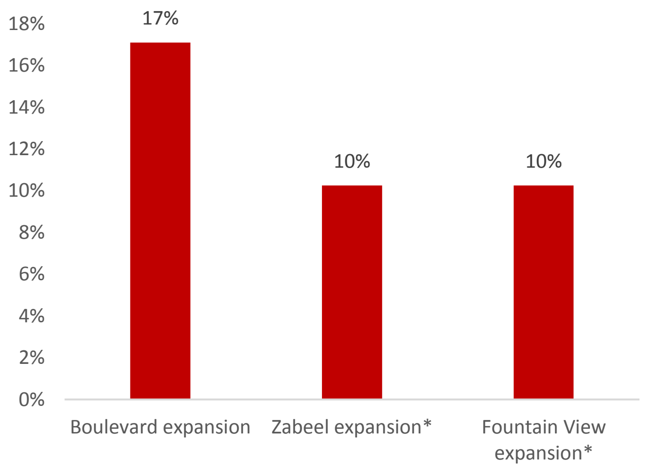
We have not yet included these expansions in our forecast given lack of full details. Our analysis indicates that planned extensions could add around 10% to GLA by 2019 and 6% to rental income. We expect yield on acquisitions from parent company to be lower than company's own developments. For calculation of yield, we assume acquisition cost at 25% development margin for Emaar Properties and a construction cost of AED1,600/sqft.

Fig. 126. Potential upside to GLA and rental income from planned expansions



Source: Company, ADCB Securities Equity Research Estimates.
* Potential acquisitions from Emaar Properties

Fig. 127. Expected yield on acquisitions lower than own developments



Source: Company, ADCB Securities Equity Research Estimates.
* Potential acquisitions from Emaar Properties

Fig. 128. Limited growth potential from planned expansions

Potential expansions	GLA (sqft)	Rent (AED/sqft)	Acquisition cost (AEDmn)	Rental Income (AEDmn)	Upside to GLA (%)	Upside to rent (%)	Expected completion	Expected Yield
Boulevard expansion	250,000	400	400	95	5%	2%	2019/20	17%
Zabeel expansion	200,000	300	400	57	3%	1%	2019/20	10%
Fountain View expansion	250,000	300	500	71	4%	2%	2019/20	10%

Source: Company, ADCB Securities Equity Research Estimates.

…however, potential from parent company's JV projects significant

Emaar Properties has recently unveiled 2.0m sqft Dubai Hills Mall in its master planned community Dubai Hills Estate (JV with Meraas)). Also various media articles have highlighted that new mall in Emaar's Dubai Creek project (JV with Dubai Holding) would be bigger than TDM, though no details have been confirmed yet. While it is uncertain if Emaar Malls can acquire these assets given involvement of JV partners, but chairman of Emaar Malls Mr. Mohamed Alabbar had mentioned in the past about potential growth opportunity for Emaar Malls coming from new master planned communities. Looking at size of the two malls, if Emaar Malls acquire these assets, we see it as strong growth driver in long term (potentially near 2021/22). These two assets could double its GLA and add ~25% to rental income of Emaar Malls (assuming 50% stake acquisition equivalent to parent company share in JVs). It would involve significant capex to acquire these assets, which in our view is likely to be funded by internal cash accruals and debt.

Fig. 129. Potential growth opportunities from Emaar Properties' JV projects is sizeable

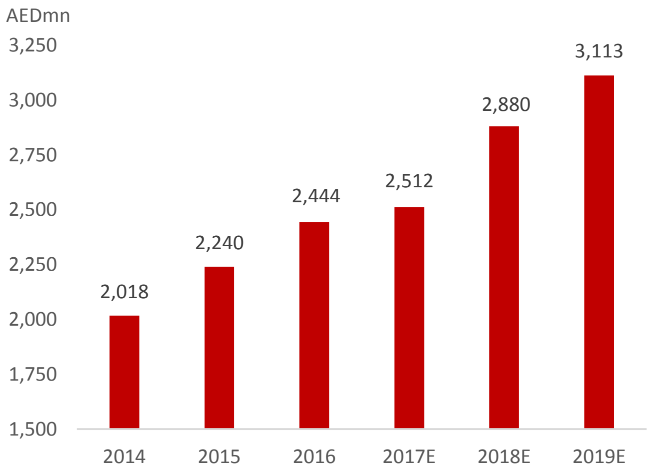
Potential expansions	GLA (sqft)	Rent (AED/sqft)	Acquisition cost* (AEDmn)	Rental Income* (AEDmn)	Upside to GLA (%)	Upside to rent* (%)	Expected completion	Yield
Dubai Hills Mall	2,000,000	350	2,000	333	30%	9%	2021/22	12%
Dubai Creek Mall	4,000,000	350	4,000	665	60%	17%	2021/22	12%

Source: Company, ADCB Securities Equity Research Estimates.
* Assuming 50% stake acquisition equivalent to Emaar Properties share in JVs

Upside to current dividends, likely in 2018/19E

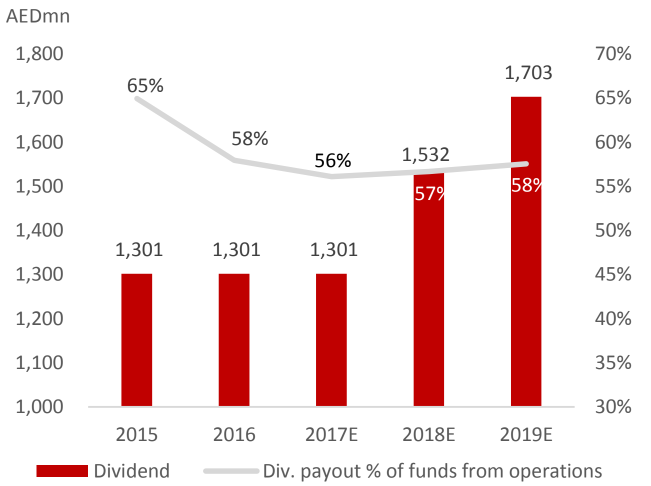
Post completion of Fashion Avenue, we expect strong ramp up in EBITDA in 2018/19E as rental income grows. The company's dividend policy at the time of IPO states distribution of 50-70% of funds from operations (EBITDA less net finance expenses). The company distributed 2016 dividend at mid-point of this range (58%) and we expect 2017E dividends to remain same (implying 55% payout). If we assume 2018/19E dividend payout similar to 2016/17E, dividend per share could increase at a CAGR of 14% over 2017-19E, offering dividend yield of 5.4% in 2018E and 6% in 2019E.

Fig. 130. Expecting strong ramp up in EBITDA in 2018/19E



Source: Company, ADCB Securities Equity Research Estimates.

Fig. 131. Dividend expected to jump assuming similar pay out



Source: Company, ADCB Securities Equity Research Estimates.

Valuation discount unwarranted, near term growth key trigger

We value Emaar Malls using cap rate methodology and apply yield of 7% for The Dubai Mall and 8% for other assets on 2018E EBITDA. Our yield assumes discount of 170-270bps over global peers EBITDA yield of 5.3%. Our target price of AED2.9/share offers an upside of 30% from current share price.

Fig. 132. Emaar Malls sum-of-the-parts (SOTP) valuation

AEDmn	Value	Value /share (AED)	% of assets	Valuation methodology
The Dubai Mall	31,721	2.4	79%	Cap rate of 7% applied on 2018E EBITDA
The Dubai Mall expansion	5,738	0.4	14%	Cap rate of 7% applied on 2018E EBITDA
Dubai Marina Mall	1,692	0.1	4%	Cap rate of 8% applied on 2018E EBITDA
Community Retail	2,544	0.2	6%	Cap rate of 8% applied on 2018E EBITDA
Speciality Retail	1,452	0.1	4%	Cap rate of 8% applied on 2018E EBITDA
Others	(2,814)	(0.2)	-7%	Cap rate of 7% applied on 2018E Corporate G&A expenses
Total Enterprise Value	**40,332**	**3.1**	**100%**	**Implied 2018E EBITDA yield of 7.1% and NOI yield of 7.8%**
Less: Gross Debt	7,296	0.6		2018E Gross Debt
Add: Cash & cash equivalents	4,804	0.4		2018E Cash
Equity Value	**37,841**	**2.9**		
No. of outstanding shares (mn)	13,014			
Target Price per share (AED)	**2.9**			
Current share price (AED)	2.2			
Upside / (downside) %	30%			

Source: ADCB Securities Equity Research Estimates.

Fig. 133. Sensitivity of target price to cap rate

2018E EBITDA yield	5.0%	6.0%	7.0%	8.0%	9.0%	10.0%
Target Price (AED)	**4.1**	**3.4**	**2.9**	**2.5**	**2.2**	**2.0**
% change	21%	17%	0%	-13%	-12%	-11%

Source: ADCB Securities Equity Research Estimates.

Fig. 134. Sensitivity of target price (AED) to retail sales and base rent growth

		Retail sales growth (2017-19E)				
		-10%	-5%	0%	5%	10%
Base rent growth (2017-19E)	-5%	2.7	2.7	2.9	3.0	3.1
	0%	2.8	2.8	2.9	3.0	3.1
	5%	2.9	2.9	**2.9**	3.0	3.2
	10%	3.0	3.0	3.0	3.1	3.2
	15%	3.1	3.1	3.1	3.1	3.2

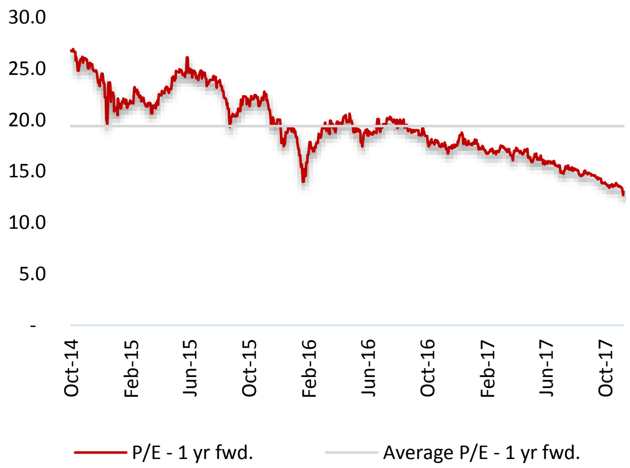
Source: ADCB Securities Equity Research Estimates.

The stock is trading at 2018E P/NAV of 0.6x, a discount of 43% to global peers and 23% to its historical average. At our target price, the stock would trade at 2018E P/NAV of 0.8x 2018E, still discount of 30% vs. peers. We expect earnings CAGR of 11% over 2016-19E (vs. 3% for global peers). In long term, Emaar Malls is likely to maintain its high growth status owing to option to acquire retail assets from parent Emaar Properties. Despite strong growth prospects, the stock is trading at discount to peers, which we see as unwarranted.

As per our analysis, current share price of Emaar Malls is either not factoring Dubai Mall expansion (AED0.4/sh. in our target price) or implying an EBITDA yield of 9.3% (400bps discount to global peers).

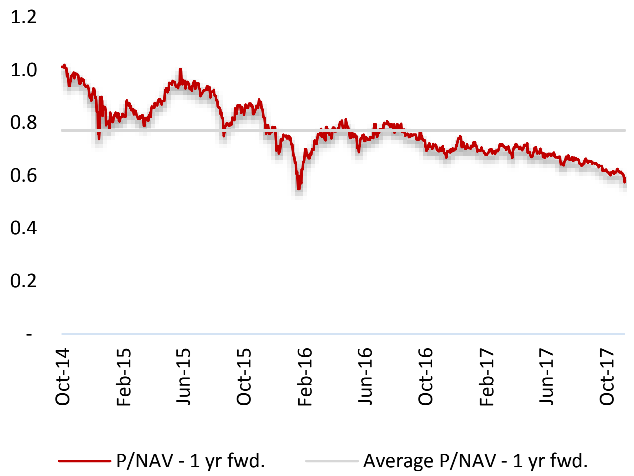
Challenging retail outlook and slowdown in earnings growth had dented investors sentiment for the stock over last two years. We believe that headwinds have eased now while concerns over supply or e-commerce threats are overdone for quality of Emaar Malls' assets. Moreover, with expansion coming on stream by 2017 end, earnings growth should start to rebound in 2018 driving re-rating of the stock.

Fig. 135. Emaar Malls trading at a 1 yr. fwd. P/E of 12.4x or 33% below historical average



Source: Bloomberg, ADCB Securities Equity Research.

Fig. 136. And 1 yr. fwd. P/NAV of 0.6x or 23% below historical average



Source: Bloomberg, ADCB Securities Equity Research.

Key Risks

We see US$ strengthening and decline in oil prices as key downside risks for Emaar Malls. Emaar Malls is highly geared to Dubai's tourism growth. US$ strengthening and lower oil prices will further constraint spending from tourists and resident population, denting prospects of recovery or stabilization. Slowdown in tenant sales at its retail assets could drive up occupancy costs for retailers. This will limit Emaar Malls' ability to increase base rents (70% of total rental income). This would also impact negotiations on upcoming lease renewals and could push down rents.

ALDAR PROPERTIES
A value play

Initiate coverage with a Buy

Real Estate | UAE | 12 November 2017

We initiate coverage on Aldar Properties with a Buy rating and a target price of AED2.9, an upside potential of 29%. Our target price is largely driven by recurring income assets, which offer stable cash flows. We expect Aldar's recurring income to stabilize in 2018 after modest decline of 5% y-o-y in 2017. Relatively muted supply expectations, slowdown in pace of government's austerity measures, contractual lease escalations and expansion assets coming on stream should be supportive to stabilize the income. Aldar's development property business should sustain pre-sales owing to mid income focus that witnessed strong demand. However, market seems to take a more bearish view on Aldar's outlook as seen by high valuation discount. We expect the implied discount to narrow down as market starts to see stability in recurring income, as well as pre-sales.

Stability in recurring income key catalyst

We expect Aldar's recurring income to stabilize in 2018E and post modest growth in 2019E. Retail assets, largest among its recurring portfolio, have remained broadly stable and should continue to see modest growth given contractual lease escalations. Aldar's residential portfolio is more exposed to market volatility given higher proportion of short term leases. Residential rents should continue to see downward pressure in 2017 given lack of short term catalyst to lift job market and consumer sentiment. That said, we expect gradual easing of conditions in 2018 as expected improvement in government's fiscal balance should slowdown the pace of austerity measures. Office rents/hotel ADRs continue to see decline but rate of decline has moderated in 9M17 and we expect this trend to continue in 2018. Finally, we expect contribution from Aldar's expansion assets to lift its performance as they come on stream over 2017-20. However, we expect ~15% downside to management's target of AED2.2bn net operating income by 2020. Mgt. implied rental growth and occupancy uplift appear aggressive, especially after headwinds of 2016/17.

Pre-sales to sustain owing to mid income focus

Company's large low cost land bank is one of its key competitive advantages. It allows flexibility to offer different products as per market conditions. Recently, Aldar has been focusing on mid income/low ticket size products, which saw strong market demand. Overall, the three key infrastructure enabled land parcels of Yas Island, Al Raha and Shams Abu Dhabi offer pre-sales potential of AED37bn. However, in our valuation, we only factor 40% of this potential to be realized by 2022. We have not yet captured upside from Aldar's large unutilized land bank beyond 2022 given lack of management guidance on development plans. We expect pre-sales of AED2.1bn in 2017, down 15% y-o-y, which is then assumed to sustain till 2022E.

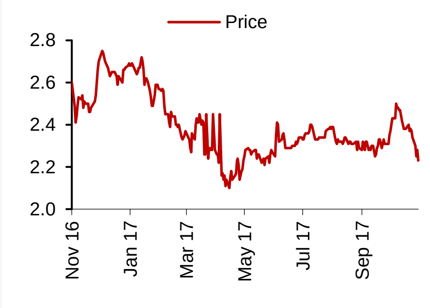
Market heavily discounting recurring assets, unwarranted in our view

Aldar is trading at a 2018 P/BV of 0.7x, 31% below historical average and 33% below global recurring income asset owners. In our target price, we conservatively assume no value for Aldar's unutilized land bank. We also apply 270bps discount to peers' cap. rate to value its recurring income assets (8% 2018E EBITDA yield vs. 5.3% for global peers). Discount to peers is warranted, given low growth prospects (flat 2016-19E recurring EBITDA vs. +3% CAGR for peers). However, current share price implies cap rate of 13% on 2018E recurring EBITDA i.e. 770bps discount to peers (assuming other assets at our valuation). This appears excessive to us. Market is likely to re-rate as recurring income stabilizes and pre-sales is sustained.

Fundamentals

Recommendation	Buy
Target Price	AED 2.9
Price	AED 2.24
Price 12m High/Low	AED 2.75/2.10
Market Cap.	AED17,533mn
Bloomberg/Reuters	ALDAR UH / ALDR.AD

Price Performance Chart



Source: Bloomberg

Equity Research Team

Yugesh Suneja (+971 2 3050838)
yugesh.suneja@adcb.com

Nikhil Poddar, CFA (+971 2 696 6450)
nikhil.poddar@adcb.com

Financials

Income Statement (AEDmn)	2016	2017E	2018E	2019E
Revenue	6,237	5,734	5,847	6,110
EBITDA	3,007	2,514	2,254	2,007
Depreciation and amortisation	199	201	203	209
EBIT	2,808	2,313	2,051	1,798
Other income	65	124	185	185
Net Finance Cost	121	105	124	29
Profit before tax	2,752	2,332	2,112	1,955
Taxes	0	0	0	0
Minority interest	30	30	30	30
Net profit	2,722	2,302	2,082	1,925

Source: ADCB Securities Equity Research

Balance Sheet (AEDmn)	2016	2017E	2018E	2019E
Cash and cash equivalents	6,696	7,714	5,753	5,543
Other current assets	8,284	7,906	7,202	7,173
Total non-current asset	4,808	4,219	4,291	4,311
Total assets	35,561	35,776	33,680	33,917
Total current liabilities	7,602	6,486	5,694	5,355
Borrowings	5,564	5,428	2,956	2,600
Other non-current liabilities	308	308	308	308
Total liabilities	13,475	12,223	8,959	8,263
Minority interest	203	233	263	293
Shareholders` equity	21,883	23,320	24,458	25,361
Total net debt	5,564	5,428	2,956	2,600

Source: ADCB Securities Equity Research

Cash flow statement (AEDmn)	2016	2017E	2018E	2019E
Cash flow from operations	2,058	2,310	2,284	1,817
Net capex	311	186	706	619
Free cash flow	1,748	2,124	1,578	1,198
Net financing	(600)	(371)	(2,710)	(473)
Change in cash	437	1,018	(1,961)	(210)

Source: ADCB Securities Equity Research

Valuation and leverage metrics	2016	2017E	2018E	2019E
P/E (x)	6.4	7.6	8.4	9.1
P/BV (x)	0.8	0.8	0.7	0.7
P/FFO (x)	5.7	6.8	7.7	8.2
FCF yield (%)	10.0	12.1	9.0	6.8
Dividend Yield (%)	4.9	5.4	5.8	6.3
EV/EBITDA (x)	7.7	9.1	9.1	10.0
Interest coverage (x)	11.6	9.9	8.6	15.4
Net debt/equity (x)	(0.05)	(0.10)	(0.11)	(0.12)
Net debt/EBITDA (x)	(0.4)	(0.9)	(1.2)	(1.5)

Source: ADCB Securities Equity Research

Key Ratios (%)	2016	2017E	2018E	2019E
ROAIC	11.8	9.4	8.3	7.4
RoAE	13.9	10.6	8.7	7.7
Revenue growth	36.1	(8.1)	2.0	4.5
EBITDA growth	22.9	(16.4)	(10.4)	(10.9)
EPS growth	7.4	(15.4)	(9.6)	(7.5)
EBITDA margin	48.2	43.8	38.5	32.9

Source: ADCB Securities Equity Research

Per-share data (AED)	2016	2017E	2018E	2019E
EPS	0.35	0.29	0.26	0.24
DPS	0.11	0.12	0.13	0.14
BVPS	2.78	2.97	3.11	3.23
Total no. of outstanding shares (mn)	7,863	7,863	7,863	7,863

Source: ADCB Securities Equity Research

Investment case

Aldar Properties is the largest developer in Abu Dhabi with significant land bank. Its recurring income assets (~65% of gross profit) offer stability in income and consistent cash flows. After modest decline in 2017E, we expect its recurring income to stabilize in 2018E and return to growth in 2019E, helped by contribution of expansion assets. Meanwhile, its development property business should sustain pre-sales owing to mid-income focus.

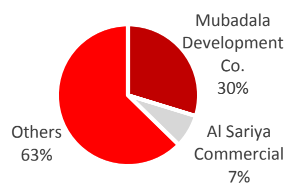
Upside case AED3.2

Higher than expected property market recovery would lift Aldar's recurring income growth prospects and pre-sales outlook. In such a scenario, rental CAGR over 2017-22E could increase to 3% vs. 1% estimated by us. Aldar would trade at 2018E P/BV of 1.0 in this case.

Downside case AED2.2

Decline in oil prices could prolong downward trend in property market. In such a scenario, Aldar's rental decline could continue at 3% p.a. and market implied EBITDA yield for recurring income assets is likely to sustain at current levels. Aldar would trade at 2018E P/BV of 0.7x in this case.

Fig. 3. Shareholding pattern

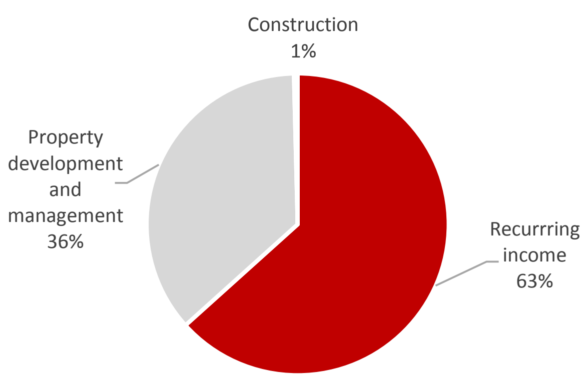


Source: ADX, ADCB Securities Equity Research

Large exposure to stable recurring income assets

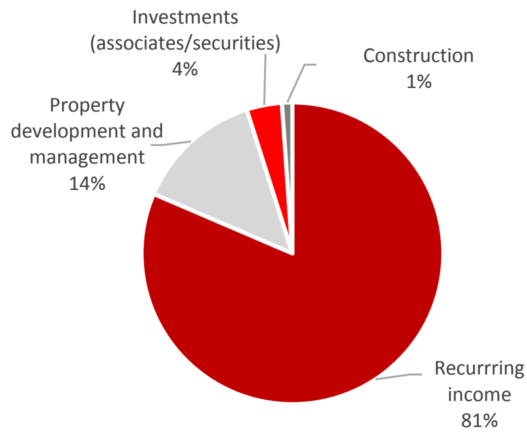
Aldar Properties is the largest developer in Abu Dhabi with significant land bank. Despite large land bank, Aldar's development property business remains small contributor to our valuation. Its recurring income assets account for 63% of gross profit and 81% of our valuation. Its business mix thus offers stability in income and consistent cash flows.

Fig. 137. Gross profit contribution by segments – 2017E



Source: Company, ADCB Securities Equity Research Estimates.

Fig. 138. Estimated enterprise value by segments

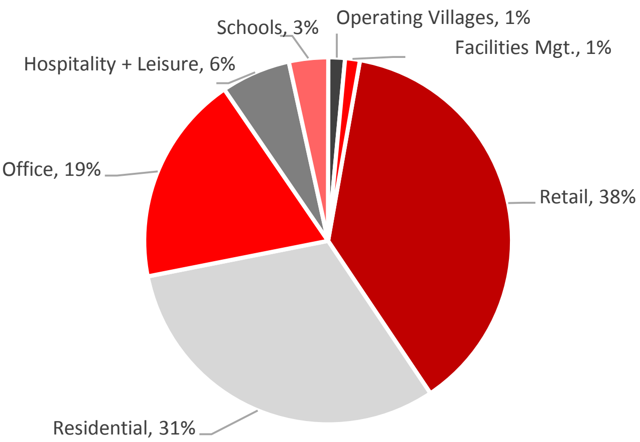


Source: Company, ADCB Securities Equity Research Estimates.

Easing of headwinds for recurring income

Aldar's recurring assets are diversified across different segments, but largely exposed to retail, residential and office segments of Abu Dhabi.

Fig. 139. Aldar's recurring income gross profit by segments – AED1.5bn in 2017E

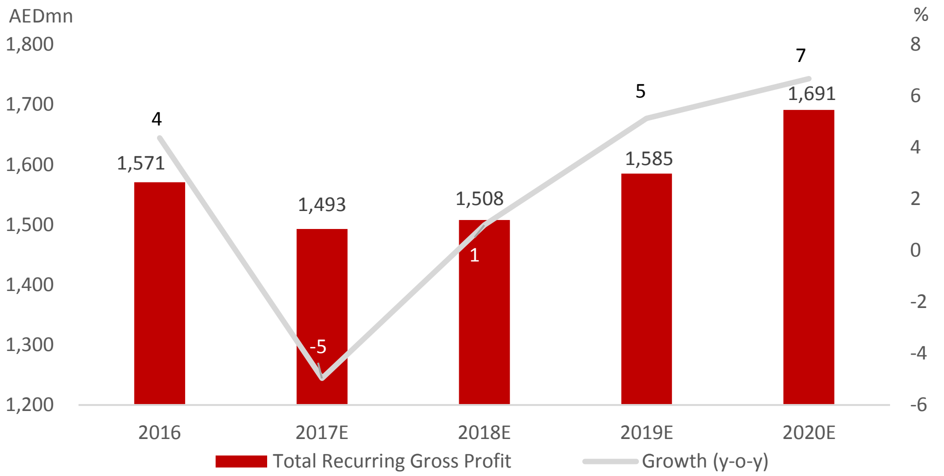


Source: Company, ADCB Securities Equity Research Estimates.

Recurring income likely to stabilize starting 2018

We expect 2017 recurring income of AED1.5bn or a modest decline of 5% y-o-y. However, we expect Aldar's recurring income to stabilize in 2018E (+1% y-o-y) and growth to return in 2019-20E.

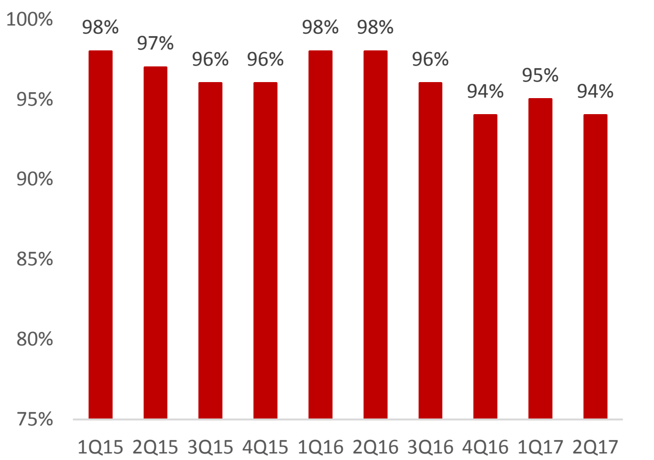
Fig. 140. Aldar's recurring income gross profit and growth



Source: Company, ADCB Securities Equity Research Estimates.

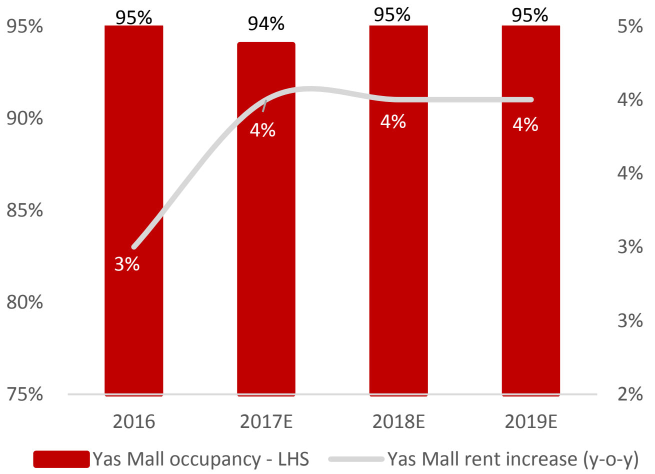
Retail assets are largest contributor to Aldar's recurring income. Retail assets have broadly remained stable in Abu Dhabi, both in terms of rents and occupancy. Aldar should continue to see a modest growth given contractual lease escalations build in rent agreements. Yas Mall is Aldar's key retail asset (~70% of retail revenues) and is still in ramp up phase. Despite offering strong retail proposition to Abu Dhabi residents, its rents are already 40% below main Abu Dhabi Island malls. We therefore do not expect its retail tenants to negotiate major revisions in lease terms on upcoming renewals.

Fig. 141. Yas Mall (70% of retail rents) occupancy broadly stable



Source: Company, ADCB Securities Equity Research.

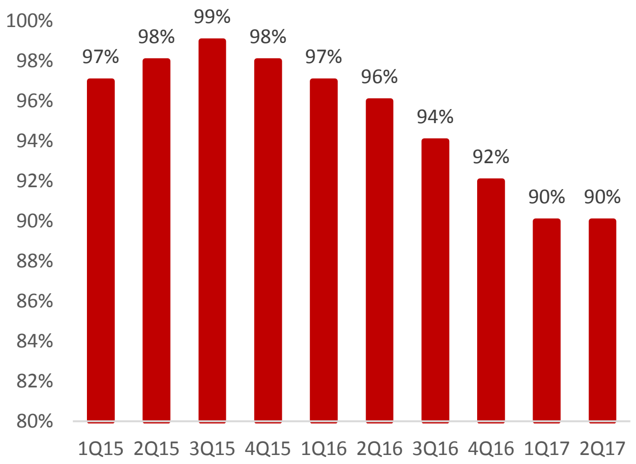
Fig. 142. We expect occupancy for Yas Mall to sustain at current levels and rents to escalate at 4% p.a.



Source: Company, ADCB Securities Equity Research Estimates.

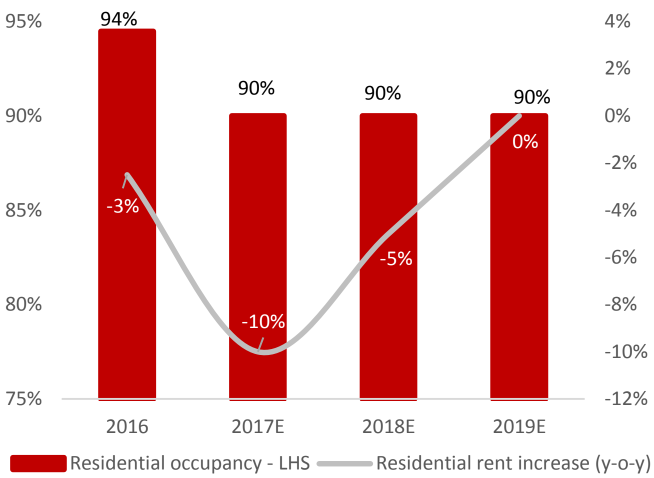
Aldar's residential portfolio (second largest contribution to recurring income) has higher proportion of short term leases (~70%) and is more exposed to market movement in rents. We assume residential occupancy levels to stabilize at current levels (already started to stabilize in 1H17). We are likely to see continued rental drops in remainder of 2017E and 2018E, though expect gradual easing of conditions with slowdown in pace of governments' tightening measures.

Fig. 143. Residential portfolio suffered higher decline in occupancy but started to stabilize in 1H17



Source: Company, ADCB Securities Equity Research.

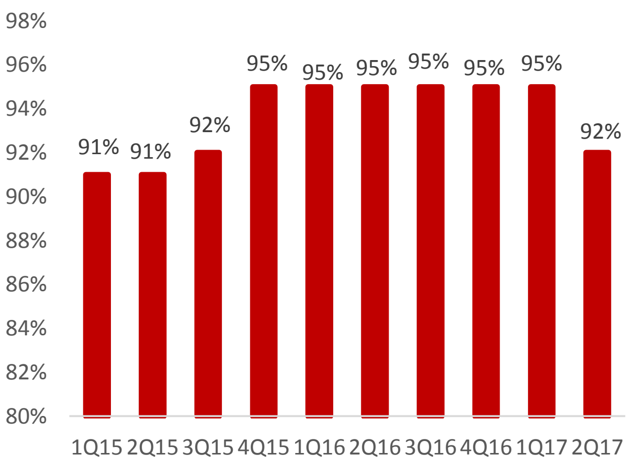
Fig. 144. Expecting residential occupancy to stabilize from hereon and rental pressure to ease after sharp decline in 2017E



Source: Company, ADCB Securities Equity Research Estimates.

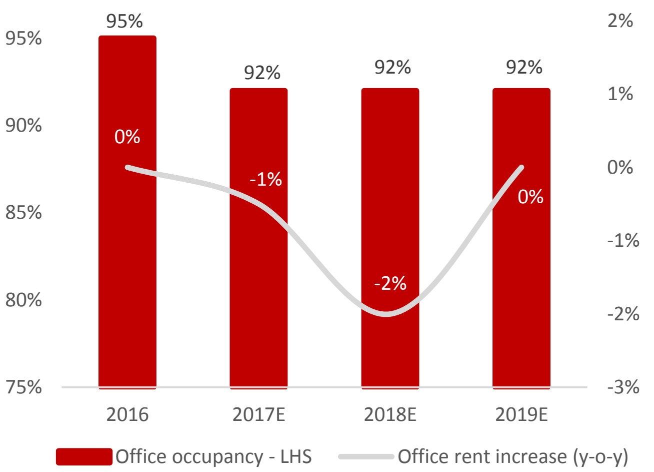
Aldar's office assets have seen stable occupancy over last two years. Moderate dip in 2Q17 occupancy is likely to have come from non-renewal of some of the leases expired in the quarter. Going forward, we expect occupancy levels to sustain at current levels as Abu Dhabi government slows down on spending cuts (Government and government related entities represent 77% of Aldar's office tenants). But upcoming lease renewals are likely to take place at lower rents as Aldar's current rents appear to be around 10% higher than prevailing market rents.

Fig. 145. Office portfolio occupancy stable, moderate dip in 2Q17 likely from non-renewal of expired leases



Source: Company, ADCB Securities Equity Research.

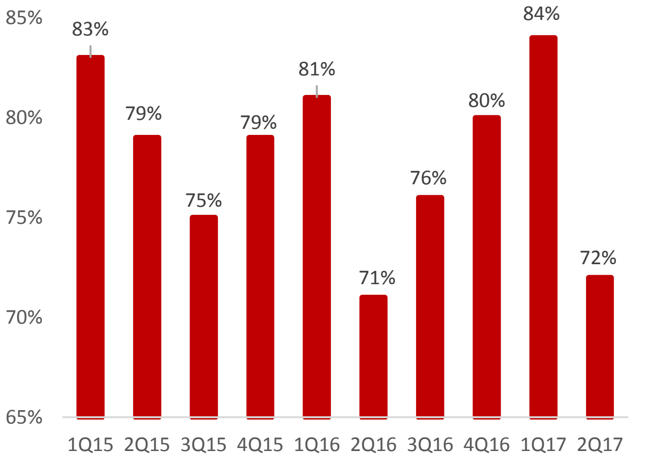
Fig. 146. Expecting office occupancy to stabilize at current levels, but rents to decline at modest pace



Source: Company, ADCB Securities Equity Research Estimates.

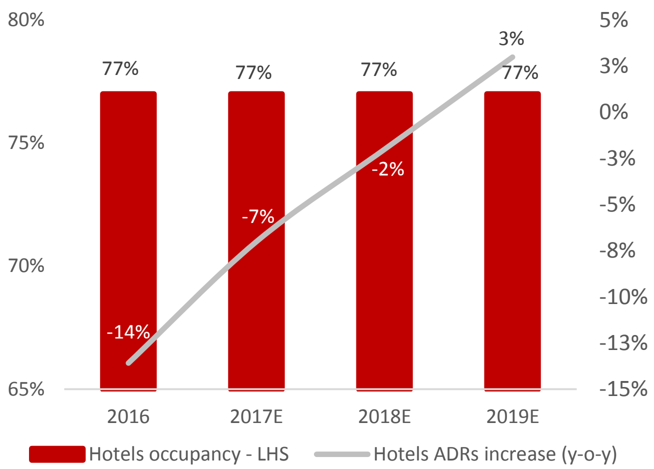
Aldar's hotels assets have seen uptick in occupancy in 1H17. We expect occupancy levels to be maintained broadly at similar levels as seen in 2016. After slight easing of market pressure on ADRs in 9M17 (-8% y-o-y after -14% y-o-y in 2016), we expect this trend to continue in 4Q17 and 2018. We therefore factor ADRs to drop 7% y-o-y in 2017E and 2% y-o-y in 2018E, and then start to pick gradually.

Fig. 147. Aldar's hotels assets saw slight uptick in 1H17 occupancy



Source: Company, ADCB Securities Equity Research.

Fig. 148. We expect occupancy to stay at 2016 levels and ADRs to recover gradually, in line with 1H17 trend



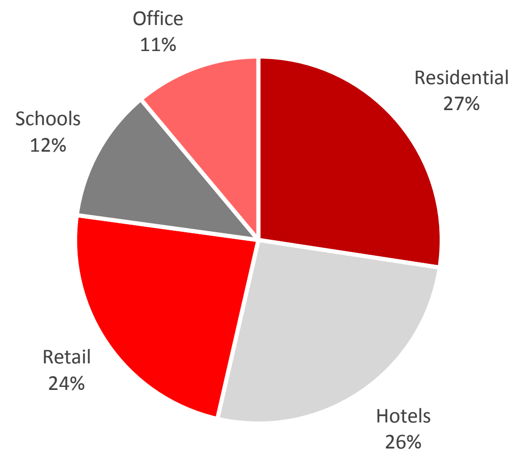
Source: Company, ADCB Securities Equity Research Estimates.

Expansion assets to support growth

Aldar had set aside AED3bn for expansion of recurring income assets. While AED1.1bn of investments were unveiled till 2016, additional AED1.9bn of investment plan was announced in 1H17. Aldar expects to complete its expansion plan by 2020 to generate incremental NOI of AED300mn. As per company guidance, this should drive an increase of 20% in existing NOI by 2020.

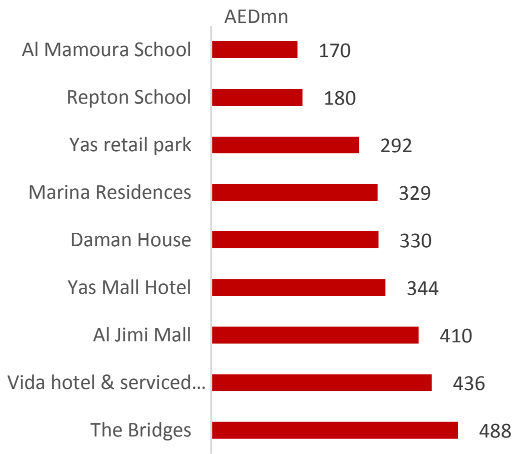
Aldar has already completed AED680m capex (Daman House, Al Mamoura school and Repton school), while remaining is expected to be completed over 2017-20E.

Fig. 149. Expansion capex of AED3bn by segments



Source: Company, ADCB Securities Equity Research Estimates.

Fig. 150. Expansion capex of AED3bn by assets



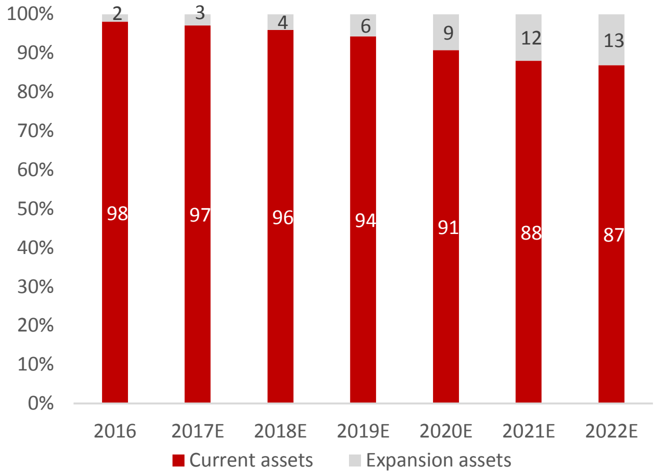
Source: Company, ADCB Securities Equity Research Estimates.

Increasing contribution of expansion assets should support recovery in recurring income. By 2022E, we expect expansion assets to account for 13% of total recurring income.

Fig. 151. Recurring income gross profit - supported by increasing contribution from expansion assets

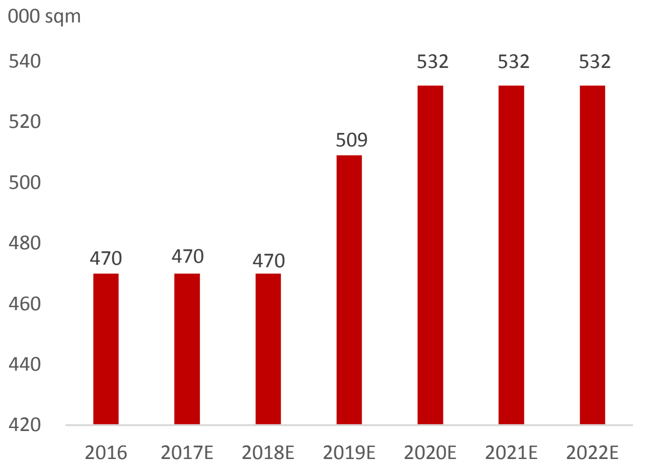
Source: Company, ADCB Securities Equity Research Estimates.

Fig. 152. Contribution to recurring income gross profit - expansion assets expected to account for 13% by 2022E



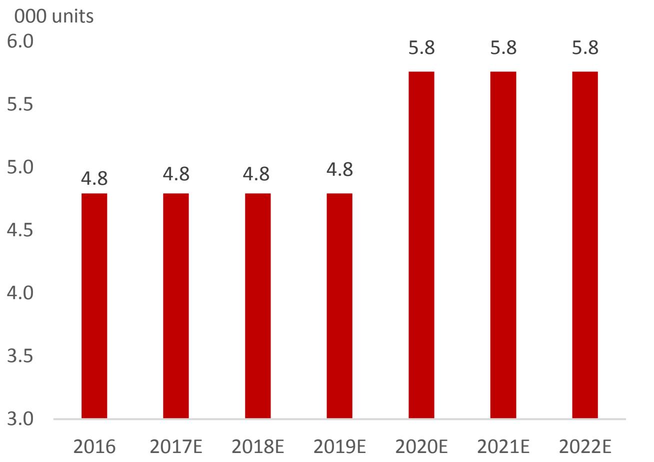
Source: Company, ADCB Securities Equity Research Estimates.

Fig. 153. Retail GLA to increase by 13% after completion of Al Jimmi Mall extension in 2018E / Yas retail park by 2020E



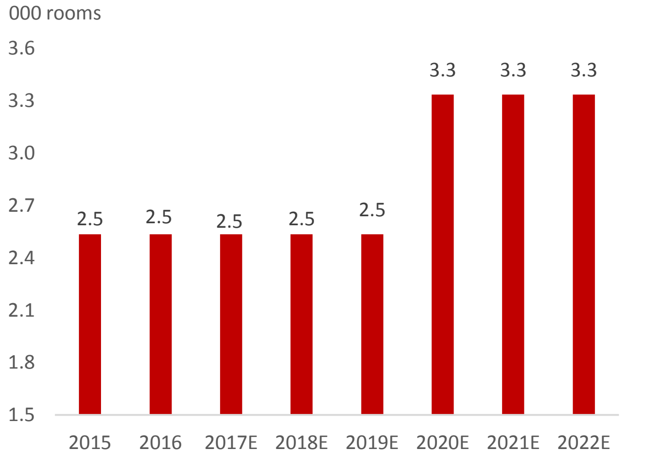
Source: Company, ADCB Securities Equity Research Estimates.

Fig. 154. Residential leasable units to increase by 20% after completion of The Bridges/Marina Residences by 2020E



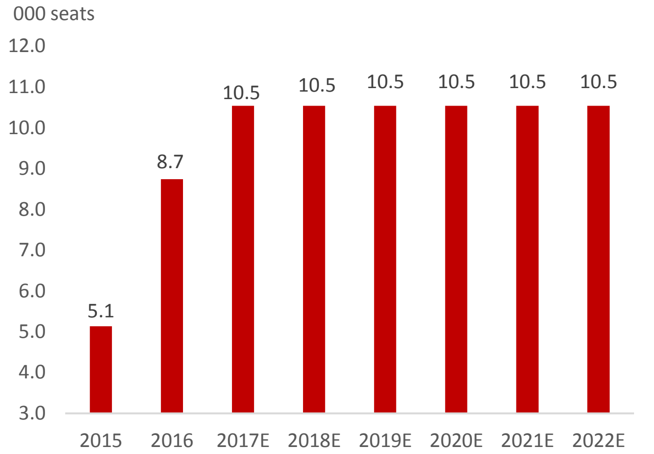
Source: Company, ADCB Securities Equity Research Estimates.

Fig. 155. No. of hotel rooms to increase by 32% after completion of Yas Mall hotel and Vida hotel/serviced apartments



Source: Company, ADCB Securities Equity Research Estimates.

Fig. 156. No. of school seats to increase by 21% on completion of Repton school in 2017

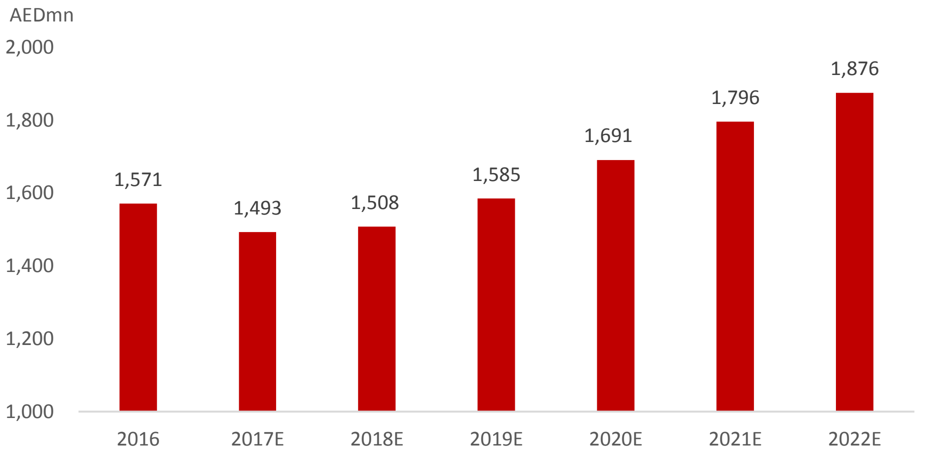


Source: Company, ADCB Securities Equity Research Estimates.

Downside risks to management guidance

Aldar management aims to reach recurring net operating income (NOI) of AED2.2bn by 2020 (from AED1.6bn in 2016) driven by organic and expansion growth. However, we expect recurring income NOI to reach AED1.9bn in 2022E. Our estimates imply NOI CAGR of 3% p.a. over 2016-22E vs. management implied guidance of 9% p.a. over 2016-20E.

Fig. 157. Our recurring income gross profit of AED1.9bn by 2022 is 15% below management guidance of AED2.2bn

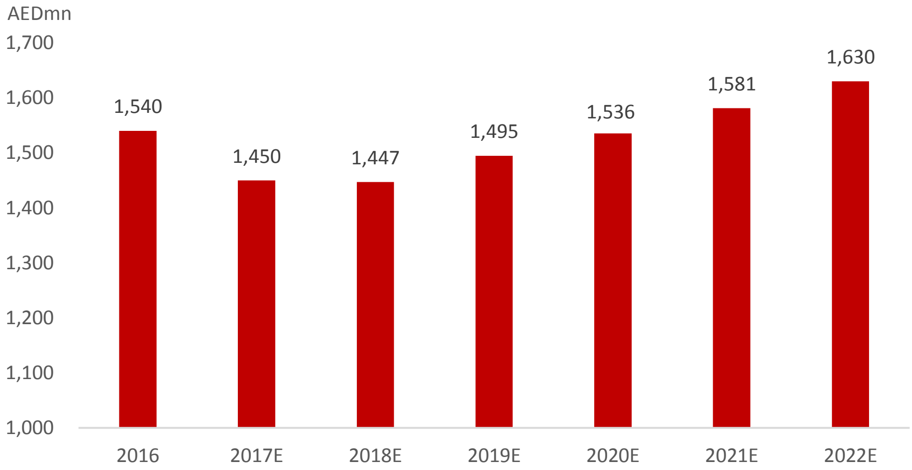


Source: Company, ADCB Securities Equity Research Estimates.

Our organic rental growth assumes no CAGR over 2016-20E, mainly due to slowdown in 2017/18E

As per management guidance, half of the incremental NOI (i.e. AED300mn) should come from organic growth. This implies an organic rental growth of 5% p.a. over 2016-20E. This is aggressive and seems challenging to achieve in current environment. We only expect recovery in organic rental growth starting 2019E (~3% p.a.). However, our estimated CAGR over 2016-20E is 0%, mainly due to decline of 6% in 2017E and no growth in 2018E.

Fig. 158. We expect organic recurring income gross profit to reach AED1.6bn by 2022

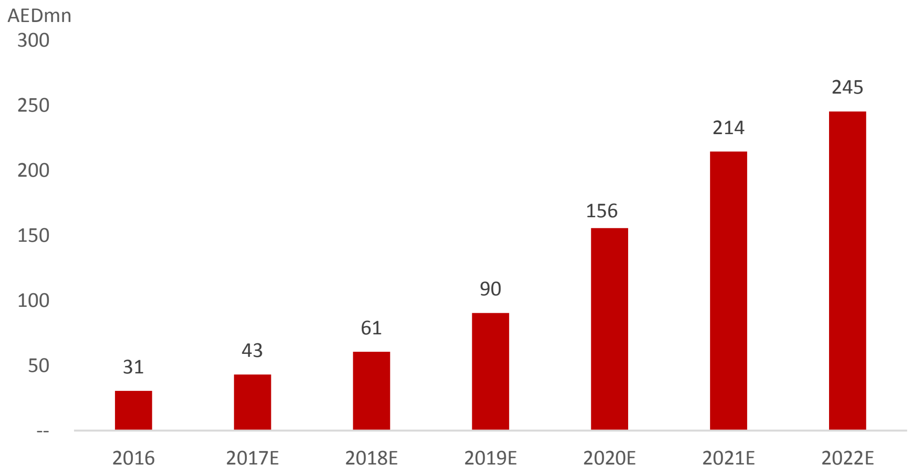


Source: Company, ADCB Securities Equity Research Estimates.

In absence of stronger rental recovery, expansion assets also unlikely to achieve expected yield

Aldar management expects expansion assets to yield AED300mn NOI by 2020 (10% net yield). In absence of stronger rental escalation, we see downside risks to incremental NOI target from expansion assets as well. Moreover, these new assets should be completed by 2020 and thus start their full contribution by 2022 as the occupancy ramps up. We see expansion assets to generate incremental NOI of AED245mn by 2022 or net yield of ~8%.

Fig. 159. We expect expansion recurring income gross profit of AED246mn by 2022



Source: Company, ADCB Securities Equity Research Estimates.

Land bank allows flexibility to weather market cycles

Large, low cost and infrastructure enabled land bank

Aldar has large, fully paid land bank of 75m sqm across Abu Dhabi. We estimate that major land parcels (Al Raha, Shams, Nareel, other land acquired from Sorouh) in Aldar's books is at cost of AED5-5.5bn. This implies an average cost of AED10/sqft and cost of AED35/sqft excluding Seih Sdeirah. Although infrastructure development costs are higher for Aldar, it being a master developer, but low cost of land should still be a key advantage for Aldar.

In our view, company's large low cost land bank (either granted free of cost from government or at low price) is a key competitive advantage that allows flexibility to offer different products as per market conditions.

Fig. 160. Aldar's land bank

Land bank*	Land (m sqm)	Land (m sqft)	Type	GFA** (m sqm)	GFA (m sqft)	Sellable*** (m sqft)
Yas Island	**7.41**	**79.8**	**Mixed Use**	**3.8**	**40.9**	**20.4**
Al Raha Beach	**3.64**	**39.1**	**Mixed Use**	**1.2**	**12.9**	**6.5**
Shams Abu Dhabi	**0.13**	**1.4**	**Mixed Use**	**0.9**	**9.7**	**4.8**
Motor World (Ph. 2)	2.71	29.2	Mixed Use	NA	NA	NA
Al Falah	2.15	23.1	Mixed Use	NA	NA	NA
Nareel Island	0.71	7.6	Mixed Use	NA	NA	NA
Al Gurm (Ph. 2)	0.70	7.5	Residential	NA	NA	NA
Al Merief	0.69	7.4	Mixed Use	NA	NA	NA
Sheibat Al Watah	0.48	5.1	Mixed Use	NA	NA	NA
Shabhat	0.25	2.7	Mixed Use	NA	NA	NA
Eastern Mangroves	0.22	2.4	Residential	NA	NA	NA
Noor Al Ain	0.09	0.9	Retail	NA	NA	NA
Capital District	0.05	0.5	Commercial	NA	NA	NA
Al Mutarad	0.02	0.3	Hotel	NA	NA	NA
Seih Sdeirah	52.26	562.3	Mixed Use	NA	NA	NA
Lulu Island	5.03	54.1	Mixed Use	NA	NA	NA
Al Naqlah	0.52	5.6	Mixed Use	NA	NA	NA
Al Mashtal	0.14	1.5	Mixed Use	NA	NA	NA
Al Ajban	0.03	0.3	Farm Land	NA	NA	NA
Saraya	0.02	0.2	Land	NA	NA	NA
Total	**77.25**	**831.2**		**5.9**	**63.5**	**31.7**

Source: Company, ADCB Securities Equity Research.

*Land size as of 2013 (Aldar Sorouh Merger presentation)
** GFA is Gross Floor Area
*** Sellable area is as per our estimates

Strong Pre-sales visibility, but we factor only 40% of potential to be realized over next five years

Of total land bank, infrastructure enabled land parcels in Yas Island, Shams Abu Dhabi and Al Raha represent sellable area of 32m sqft or development potential of nearly 18,000 units (3,500 units already launched). These three key land parcels offer sufficient pre-sales visibility for next 10 years, though other land parcels hold additional potential to further enhance the pipeline.

In terms of value, we estimate pre-sales value of AED37bn for these three developments. Of this, AED8.2bn is already launched. In our valuation, we factor total pre-sales of AED14.7bn from these three land parcels or only 40% of total potential. Residual pre-sales potential of AED22bn offers pre-sales visibility of additional 10 years.

Fig. 161. Aldar's three main land parcels holds strong visibility of which we factor only 40% in our valuation

m sqft	Pre-sales potential	Used in DCF	Residual	% Used
Yas Island	20.4	10.7	9.8	52%
Al Raha Beach	6.5	1.0	5.5	15%
Shams Abu Dhabi	4.8	1.5	3.3	31%
Total	**31.7**	**13.2**	**18.6**	**41%**

Units	Pre-sales potential	Used in DCF	Residual	% Used
Yas Island	8,380	4,380	4,000	52%
Al Raha Beach	4,782	730	4,052	15%
Shams Abu Dhabi	4,725	1,460	3,265	31%
Total	**17,887**	**6,570**	**11,317**	**37%**

AEDmn	Pre-sales potential	Used in DCF	Residual	% Used
Yas Island	22,308	11,659	10,648	52%
Al Raha Beach	9,412	1,437	7,975	15%
Shams Abu Dhabi	5,274	1,630	3,644	31%
Total	**36,994**	**14,726**	**22,268**	**40%**

Source: Company, ADCB Securities Equity Research Estimates.

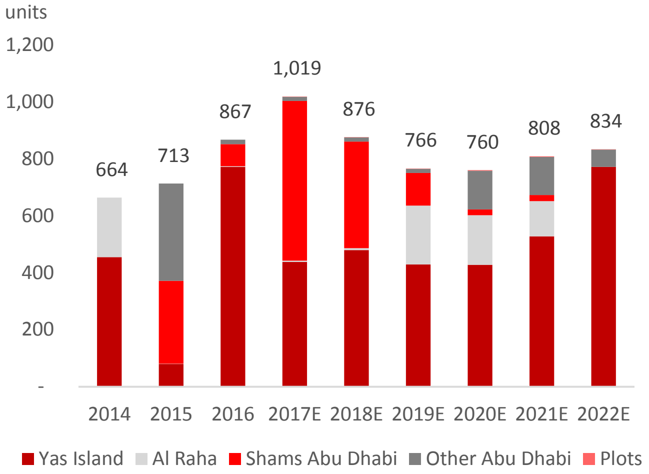
Focus on mid-income segment and attractive payment plan supportive of pre-sales

After factoring a decline of 15% in 2017 pre-sales to AED2.1bn, we expect it to sustain at these levels. Pre-sales should be supported by:

- **Strategy to focus on mid-income/low ticket size products**
  Aldar's adapted its development strategy to focus more on mid-income market products or low ticket size units to encourage end users demand. Strong response to Yas Acres (smaller 2-3 BR townhouses offered in the market) and The Bridges (mid-income product) launches point to potential for untapped market. While weak job market conditions would continue to impact overall activity in the market, we expect Aldar to leverage upon its infrastructure enabled low cost land bank to sustain pre-sales owing to new focus and leading market position.

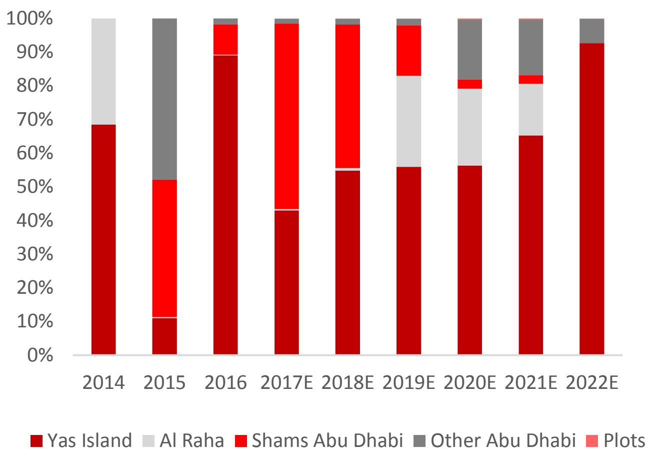
- **Attractive back ended payment plans**
  Aldar has been offering attractive payment plans with 50% or 70% payment on handover. Although this would increase working capital requirement in interim but Aldar has sufficient balance sheet strength to fund the construction spend. Default risk should be manageable unless market corrects by more than 20-30% i.e. by the upfront payment already received on the sales.

Fig. 162. Higher pre-sales in 2017 supported by mid income 'The Bridges' sales in Shams Abu Dhabi



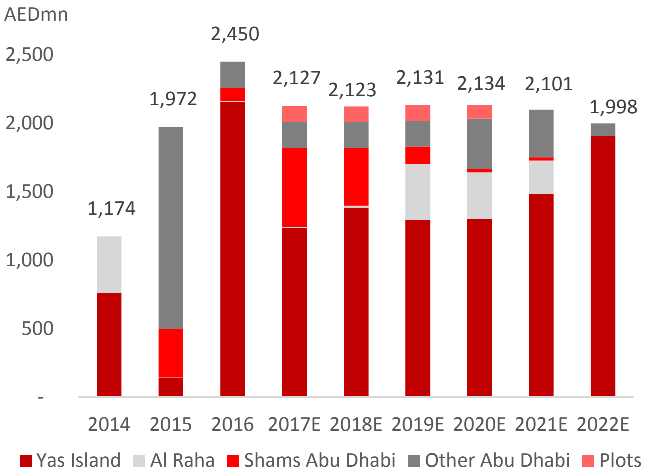
Source: Company, ADCB Securities Equity Research Estimates.

Fig. 163. We expect Yas Island to be main contributor to unit pre-sales as new apartment products are also launched



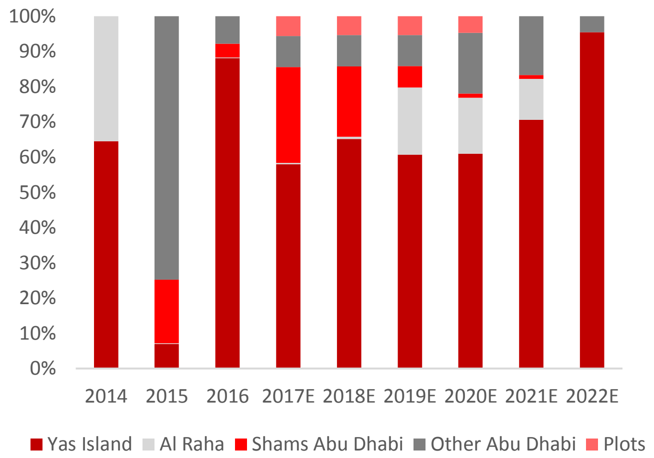
Source: Company, ADCB Securities Equity Research Estimates.

Fig. 164. We expect pre-sales to sustain at AED2.1bn p.a. over 2017-22E..



Source: Company, ADCB Securities Equity Research Estimates.

Fig. 165. …with Yas Island key contributor. Mid income Shams Abu Dhabi to support pre-sales in short term



Source: Company, ADCB Securities Equity Research Estimates.

Market pricing significant discount for recurring income assets

We use sum-of-the-parts (SOTP) approach to value Aldar Properties' different businesses. Our target price for Aldar Properties stands at AED2.9/share, offering upside potential of 29% from current share price.

For development business (build to sell assets), we use DCF to value cash flows from pre-sales of projects. We use WACC of 10.7% for development business. We assume pre-sales till 2022. We have not yet captured upside from Aldar's large unutilized land bank beyond 2022 given lack of management guidance on development plans. We do not factor any selling price increase over our forecast period.

For recurring income assets (build to lease), we value cash flows till 2022 on DCF basis using WACC of 10.7%. We apply cap rate on 2022E recurring EBITDA to derive terminal value. We have used 2022 EBITDA for terminal value given expansion assets will reach mature occupancy levels by that period. Our valuation of recurring income assets imply 2018E EBITDA yield of 8.0% (vs. 5.3% for global peers).

For construction business (Pivot), we use DCF to value cash flows till 2022E and terminal value at the end of 2022, assuming no terminal growth.

For associates/JVs (excluding UAE development JVs), we use 2018E book value of investments and apply discount of 20%.

Fig. 166. Aldar's sum-of-the-parts (SOTP) valuation

AEDmn	Value	Value/ Share	% of assets	Methodology
Investment Properties	**16,500**	**2.1**	**81%**	**Implied 2018E EBITDA yield of 8% and NOI yield of 9.1%**
Residential	4,914	0.6	24%	
Retail	7,361	0.9	36%	DCF of cash flows till 2022, Terminal Value at EBITDA yield of 8.25%
Office	2,810	0.4	14%	
Schools	682	0.1	3%	
Facility Management (Khidmah)	127	0.0	1%	
Operating Villages	214	0.0	1%	DCF of cash flows till 2022, Terminal Value at EBITDA yield of 10.25%
Hospitality & Leisure	391	0.1	2%	
Development Properties	**2,833**	**0.4**	**14%**	
Development & development management	2,845	0.4		DCF @ WACC of 10.7%, Pre-sales of AED2.1bn p.a. till 2022
Construction	**230**	**0.0**	**1%**	
Pivot	230	0.0		DCF @ WACC of 10.7%, Terminal growth of 0%
Associates & JVs	**788**	**0.1**	**4%**	
Associates & JVs	788	0.1		At 20% discount to 2018E BV
Total Enterprise Value	**20,350**	**2.6**	**100%**	
Add: Financial Investments	126	0.0		At 2018E BV
Add: Cash & cash Equivalents	5,753	0.7		At 2018E BV
Less: Total Debt	(2,956)	(0.4)		At 2018E BV
Less: Minority Interest	(263)	(0.0)		At 2018E BV
Equity value	**23,010**			
No. of outstanding shares (mn)	7,863			
Target Price per share (AED)	**2.9**			
Current share price (AED)	2.2			
Upside / downside (%)	29%			

Source: ADCB Securities Equity Research Estimates.

Aldar is currently trading at a P/BV of 0.7x 2018E, a discount of 31% compared to historical average and 33% discount to global recurring income asset owners P/BV of 1.1x. At our target price of AED2.9/share, Aldar would trade at 0.9x i.e. 10% below historical average. We expect the discount to narrow as recurring income stabilizes and pre-sales is sustained.

Fig. 167. Aldar is trading at 31% discount to its historical average P/BV

Source: Bloomberg, ADCB Securities Equity Research Estimates.

If we assume our calculated fair value of development property and other assets, current share price would imply a 2018E EBITDA yield of 13% for recurring assets (770bps discount to peers cap rate of 5.3%), which we see as excessive for stable cash flow generating assets.

Valuation sensitivity to cap rate

Recurring income assets account for 81% of Aldar's valuation. Thus, any change in expectations of cap rate would significantly influence the stock price performance. We believe that market would start to re-rate as recurring income stabilizes by next year. With every 100bps change in cap rate expectations, our target price changes by 7%.

Fig. 168. Aldar's target price sensitivity to recurring income cap. rate

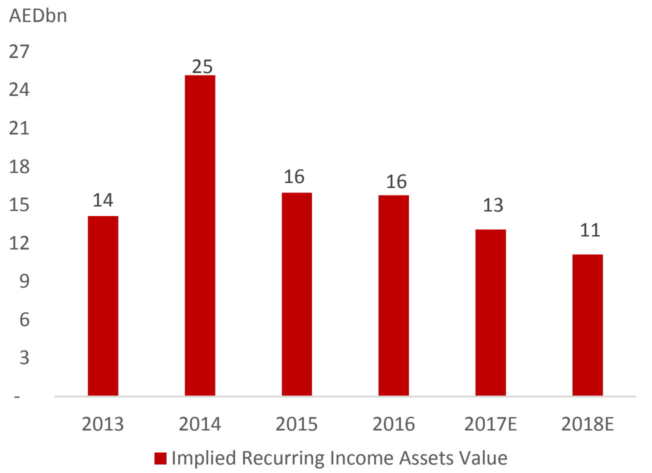
Target Price (AED/share)		Annual rental escalation (2016-22E)					
		-3.0%	-1.0%	0.9%	3.0%	5.0%	7.0%
Implied Cap. Rate on 2018E recurring EBITDA	6.0%	2.8	3.1	3.5	3.9	4.3	4.8
	7.0%	2.6	2.9	3.2	3.5	3.9	4.3
	8.8%	2.4	2.7	**2.9**	3.3	3.6	4.0
	9.0%	2.3	2.5	2.8	3.1	3.4	3.7
	10.0%	2.2	2.4	2.6	2.9	3.2	3.5
	11.0%	2.1	2.3	2.5	2.8	3.0	3.3
	12.0%	2.0	2.2	2.4	2.6	2.9	3.2

Source: ADCB Securities Equity Research Estimates.

Why cap rate should re-rate?

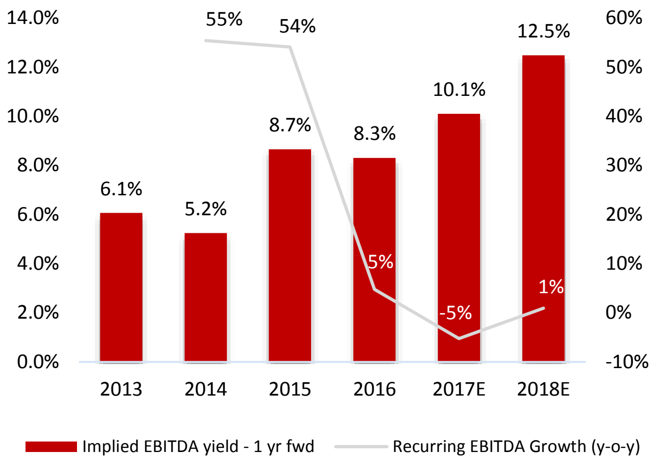
Historically, market implied cap rate for Aldar's recurring income assets had been a function of growth prospects of rental income. As seen in charts below, if we exclude other assets (at our fair valuation) from market cap., implied value of recurring income assets has fallen in 2017 (and implied EBITDA yield has increased). However, we see pressure on recurring income easing next year (stabilization phase) and rentals to recover starting 2019. We therefore see potential for EBITDA yield to reduce as market starts to see stability in recurring assets.

Fig. 169. Market implied value of recurring income assets has come down as growth slowed down



Source: Company, ADCB Securities Equity Research Estimates.

Fig. 170. Market implied EBITDA yield becoming more attractive as recurring income starts to stabilize by 2018



Source: Company, ADCB Securities Equity Research Estimates.

Key risks

We see decline in oil prices as key downside risk for Aldar. Continued pace of austerity measures by Abu Dhabi government in low oil price environment would create further uncertainty in job markets, pulling down consumer and corporate demand. This would depress the prospects of recovery in property prices and rents, thereby impacting Aldar's rental income and pre-sales. Large upfront infrastructure capex (for own or government development projects) could also negatively impact its cash flows.

DAMAC PROPERTIES
Market pricing aggressive pre-sales

Initiate coverage with a Sell

Real Estate | UAE | 12 November 2017

We initiate coverage on Damac Properties with a Sell rating and a target price of AED3.0/share, a downside of 17%. Damac is a Dubai centric developer with sales mainly driven by foreigners. Stable oil prices and USD weakening YTD 2017 have positively impacted sentiment of foreign buyers for Dubai property. This has been reflected in Damac's pre-sales recovery, as well as its share price performance, which outperformed benchmark DFM Index by 45% this year. Following this rally, we believe the stock is expensive at 1.4x 2018E P/BV and already factors significantly higher pre-sales growth. Current valuations imply: 1/ annual pre-sales over 2017-20E to jump 28% above 2017E, and 2/ the company would acquire land bank similar to its second largest project Damac Hills to support higher pre-sales till 2020 and beyond. Lastly, lack of revenue diversification (unlike higher recurring income contribution for Emaar and Aldar) and weak earnings outlook are other constraints to sustain premium valuation.

Pre-sales recovering, but market factoring aggressive growth

Stable oil prices and USD weakening has made Dubai property less expensive YTD 2017. Damac benefitted from positive sentiment and saw pre-sales starting to grow in 1Q17, after nine consecutive quarters of decline. Recovery firmed up in 3Q17 with growth of 17% y-o-y. We expect its 2017 pre-sales to grow 11% y-o-y to at AED7.8bn, and sustain at these levels till current land bank gets exhausted by 2020E. However, Damac's share price implies aggressive pre-sales of AED10bn p.a. over 2017-20E (28% above 2017E) and AED2bn p.a. over 2021-25E. To achieve such an increase in pre-sales, Damac needs to acquire land bank with potential value of AED19bn, similar to Damac Hills (second largest project undertaken by Damac).

Revenues lack diversification, earnings outlook is weak

Damac is highly exposed to cyclical nature of development business with insignificant recurring income contribution (vs. 50% of Emaar's and 63% of Aldar' 2017E gross profit). This is reflected in sharp slowdown in cash collection in 2016, resulting in negative free cash flows of AED57mn (after +AED2.4bn in 2015 / +AED3.2bn in 2014). Its earnings also declined by 18% y-o-y in 2016. Though Damac plans to increase its recurring income portfolio, we do not expect major ramp up over next five years. Moreover, we see its weak earnings performance to continue (-9% CAGR over 2016-19E), impacted by lower margins and absence of unit cancellation income.

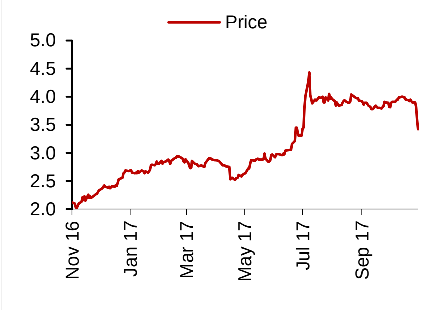
Valuation expensive despite supportive dividend yield

Damac is trading at a P/BV of 1.4x 2018E or 12% above historical average and 30% above EM peers. Damac's current market cap. is only 10% below our valuation of Emaar's Dubai development business. This is despite significantly higher visibility offered by Emaar's Dubai land bank vs. Damac. We expect Damac's 2017-20E pre-sales of AED31.5bn, ~30% lower than Emaar's Dubai pre-sales of AED45.4bn (Emaar's share only). While Damac management is looking to acquire land bank to enhance visibility, but market is already factoring aggressive ramp up in pre-sales and large new project additions. Damac's expected dividend yield at 7% in 2017/18E is supportive, but it is below 7.5% dividend yield expected for Emaar Development (at upper end of IPO price range). We therefore see Damac's current valuation demanding, particularly amid weak earnings outlook, less visibility and lack of revenue diversification.

Fundamentals

Recommendation	Sell
Target Price	AED 3.0
Price	AED 3.59
Price 12m High/Low	AED 4.43/2.02
Market Cap.	AED21,700mn
Bloomberg/Reuters	DAMAC UH / DAMAC.DU

Price Performance Chart



Source: Bloomberg

Equity Research Team

Yugesh Suneja (+971 2 3050838)
yugesh.suneja@adcb.com

Nikhil Poddar, CFA (+971 2 696 6450)
nikhil.poddar@adcb.com

Financials

Income Statement (AEDmn)	2016	2017E	2018E	2019E
Revenue	7,156	7,779	7,777	7,939
EBITDA	3,732	3,163	2,901	2,802
Depreciation and amortisation	15	24	27	30
EBIT	3,717	3,139	2,874	2,772
Other income	45	48	51	53
Net Finance Cost	67	141	144	70
Profit before tax	3,695	3,045	2,781	2,756
Taxes	0	0	0	0
Minority interest	0	0	0	0
Net profit	3,695	3,045	2,781	2,756

Source: ADCB Securities Equity Research

Balance Sheet (AEDmn)	2016	2017E	2018E	2019E
Cash and cash equivalents	8,316	7,851	6,793	5,866
Other current assets	16,066	17,215	17,870	18,024
Total non-current asset	244	234	227	218
Total assets	24,626	25,504	25,093	24,311
Total current liabilities	8,191	6,714	6,185	5,811
Borrowings	3,816	4,639	3,489	1,838
Other non-current liabilities	0	0	0	0
Total liabilities	12,008	11,353	9,674	7,649
Minority interest	0	0	0	0
Shareholders` equity	12,618	14,151	15,419	16,662
Total net debt	(4,500)	(3,212)	(3,303)	(4,027)

Source: ADCB Securities Equity Research

Cash flow statement (AEDmn)	2016	2017E	2018E	2019E
Cash flow from operations	(47)	381	1,768	2,326
Net capex	10	15	20	20
Free cash flow	(57)	366	1,748	2,306
Net financing	46	823	(1,150)	(1,651)
Change in cash	(1,185)	(465)	(1,059)	(927)

Source: ADCB Securities Equity Research

Valuation and leverage metrics	2016	2017E	2018E	2019E
P/E (x)	5.6	7.2	7.8	7.8
P/BV (x)	1.6	1.5	1.4	1.3
P/FFO (x)	5.6	6.7	7.4	7.4
FCF yield (%)	(0.3)	1.8	8.4	11.1
Dividend Yield (%)	7.3	7.0	7.0	7.0
EV/EBITDA (x)	4.3	5.5	6.0	5.9
Interest coverage (x)	20.4	11.4	10.9	16.0
Net debt/equity (x)	(0.36)	(0.23)	(0.21)	(0.24)
Net debt/EBITDA (x)	(1.2)	(1.0)	(1.1)	(1.4)

Source: ADCB Securities Equity Research

Key Ratios (%)	2016	2017E	2018E	2019E
ROAIC	25.8	18.9	16.2	15.7
RoAE	32.9	22.8	18.8	17.2
Revenue growth	(16.2)	8.7	0.0	2.1
EBITDA growth	(18.1)	(15.2)	(8.3)	(3.4)
EPS growth	(18.2)	(17.6)	(8.7)	(0.9)
EBITDA margin	52.1	40.7	37.3	35.3

Source: ADCB Securities Equity Research

Per-share data (AED)	2016	2017E	2018E	2019E
EPS	0.61	0.50	0.46	0.46
DPS	0.25	0.25	0.25	0.25
BVPS	2.09	2.34	2.55	2.75
Total no. of outstanding shares (mn)	6,050	6,050	6,050	6,050

Source: ADCB Securities Equity Research

Investment case

Damac is a Dubai centric developer with its sales mainly driven by foreign nationals. Steady oil prices and US$ weakening has supported its pre-sales recovery in 2017. However, after strong YTD2017 share price outperformance, market is already factoring aggressive pre-sales growth over medium term and significant land acquisitions. We see its valuation expensive, particularly amid weak earnings outlook, lower visibility and lack of revenue diversification towards recurring income.

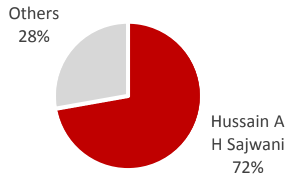
Upside case AED4.0

Rebound in 2017-20E annual pre-sales to 2014 peak of AED11.5bn (+45% from 2017E) and 2021-25E annual pre-sales of AED3bn, driven by property market recovery and new land bank acquisition with pre-sales value equivalent to combined Akoya Oxygen and Aykon City. In this case, Damac would trade at 2018E P/BV of 1.6x.

Downside case AED2.6

Decline in oil prices and strong momentum in US$ strengthening would lower demand and pre-sales. As a result, cash collection would slowdown. We assume 20% lower cash collection than our current estimates for a downside case. In this case, Damac would trade at 2018E P/BV of 1.0x.

Fig. 4. Shareholding pattern



Source: DFM, ADCB Securities Equity Research.

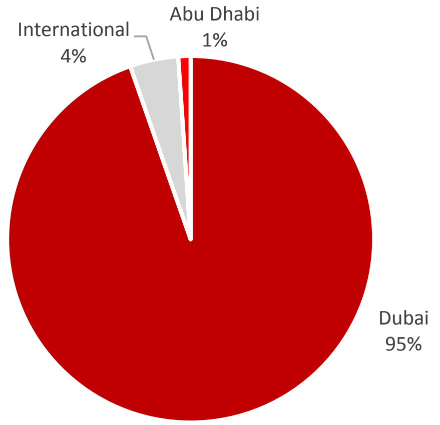
Dubai focused developer

Damac Properties (Damac) is a Dubai centric developer (95% of its project pipeline) primarily operating in build to sell residential segment. The company ventured as a master developer in 2013 with the launch of mixed use community Damac Hills (Akoya) and later Akoya Oxygen in 2015. Damac's strategy is to acquire land bank at competitive prices, maintain tight cost control to ensure higher margins, fund construction using customer payments and sell majority of project before completion. The company manages its launches in a phased manner to ensure the project is de-risked first (sold to a level to cover full construction cost). Then new releases aim to maximize selling prices till completion. Damac has also used co-branding strategy with premium brands of FENDI Casa, Versace Home, Bugatti, Paramount and the Trump Organization to increase international buyers' interest and higher selling prices compared to unbranded apartments.

The company also develops and operates hospitality units comprising of serviced apartments and hotels. Serviced apartments account for 20% of its development pipeline and hotel rooms (including build to sell) represent 5% of pipeline.

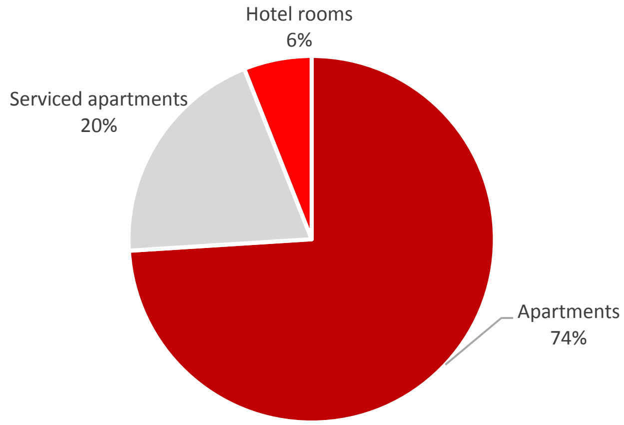
Currently, recurring income contribution is insignificant. The company plans to develop its investment property segment, which will involve leasing of retail, residential and office units.

Fig. 171. Damac's development pipeline by regions (~41k units)



Source: Company, ADCB Securities Equity Research.

Fig. 172. Damac's development pipeline by type

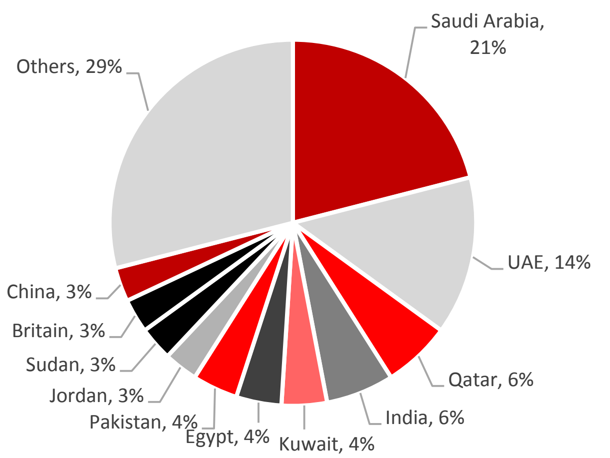


Source: Company, ADCB Securities Equity Research.

Geared to foreign buyers' purchasing power

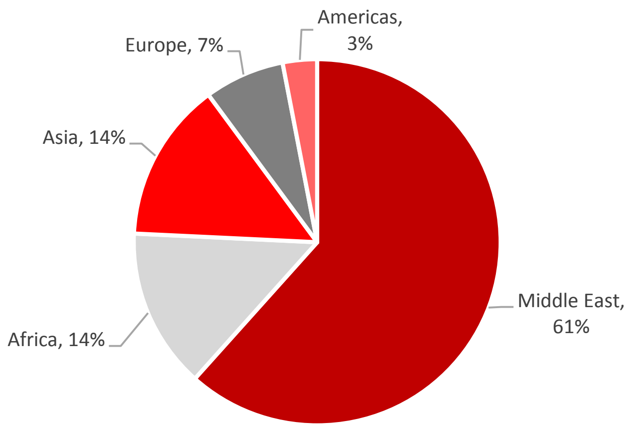
Damac's sales is mainly driven by foreign nationals, which typically fund the purchase by cash rather than mortgage. As per 2014-16 sales, 86% of its buyers were from outside UAE. Buyers from Saudi Arabia formed the major chunk at 21% of total. In terms of region, Middle East accounted for 61% of its buyers, followed by Africa and Asia at 14% each.

Fig. 173. Damac's buyers by nationality as per 2014-16 pre-sales



Source: Company, ADCB Securities Equity Research.

Fig. 174. Damac's buyers by region as per 2014-16 pre-sales

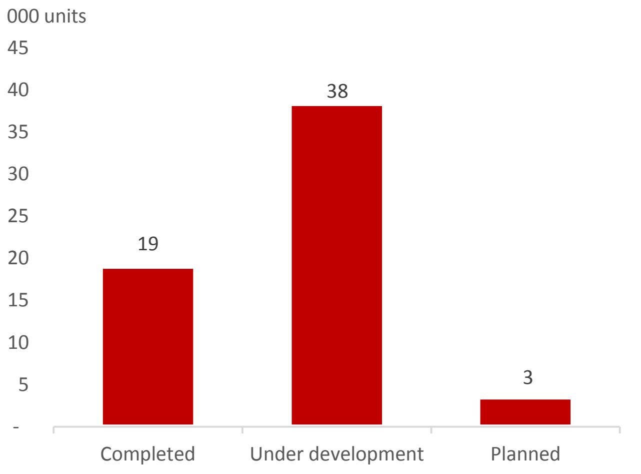


Source: Company, ADCB Securities Equity Research.

Damac's pipeline offer visibility for next three years

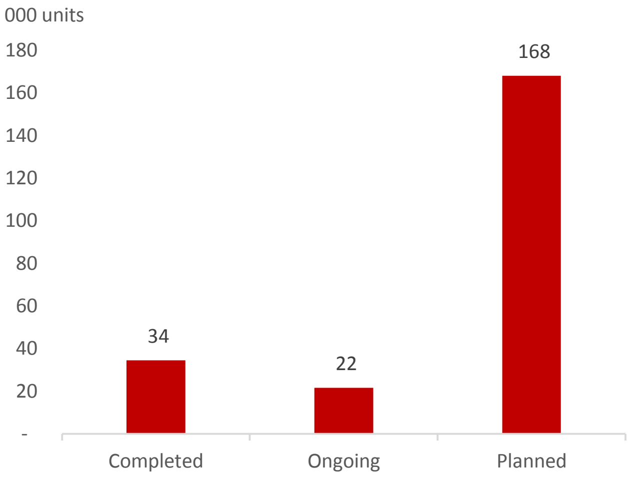
Damac's pipeline consists of ~41k units, which we expect to be largely sold by 2020. To put this into context, Emaar Properties' Dubai development pipeline consists of 190k units and is expected to offer visibility for next twenty years.

Fig. 175. Damac's development pipeline



Source: Company, ADCB Securities Equity Research Estimates.

Fig. 176. Emaar's Dubai development pipeline



Source: Company, ADCB Securities Equity Research Estimates.

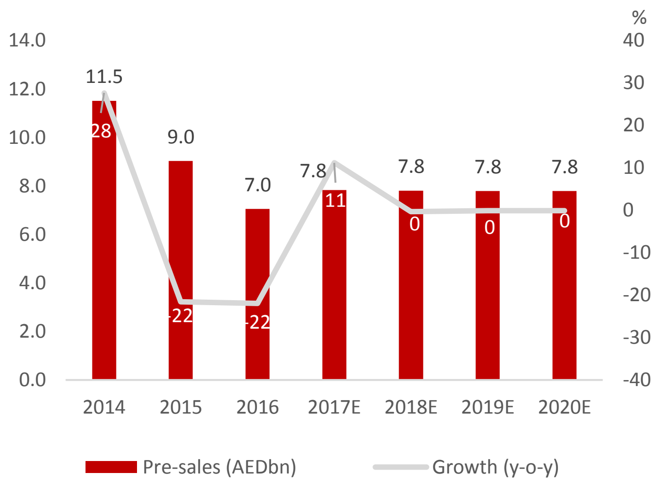
Pre-sales starting to recover, market pricing aggressive growth

Stable oil prices and USD weakening have positively impacted sentiment of foreign buyers for Dubai property. Damac has also benefitted from change in sentiment. It saw growth in pre-sales in 1Q17 (+11% YoY) after nine consecutive quarters of drop. Pre-sales growth sustained in 2Q17 (+10% YoY) and firmed up in 3Q17 (+17% y-o-y). We expect 2017E pre-sales at AED7.8bn (up 11% y-o-y, management guidance of AED7bn) after -22% p.a. in 2015/16. We estimate that Damac's current land bank offers pre-sales potential of AED31.5bn and its pre-sales can sustain at 2017E levels till 2020E.

Fig. 177. Pre-sales growth returns in 2017 after nine consecutive quarters of decline

Source: Company, ADCB Securities Equity Research.

Fig. 178. We expect pre-sales to grow 11% y-o-y in 2017E and sustain at these levels till 2020E

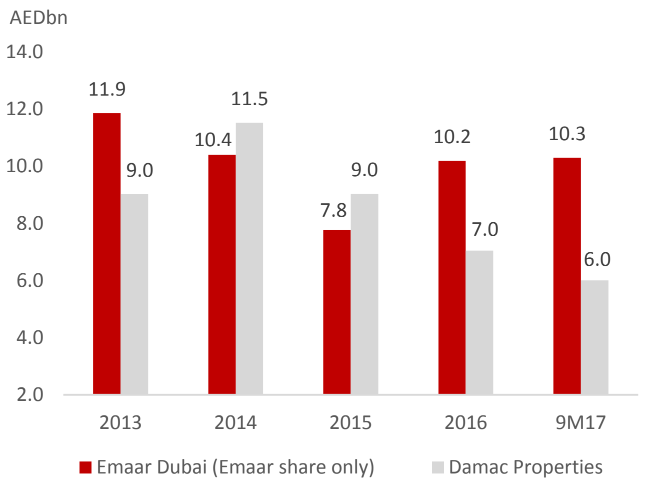


Source: Company, ADCB Securities Equity Research Estimates.

Management looking to acquire land bank to enhance visibility

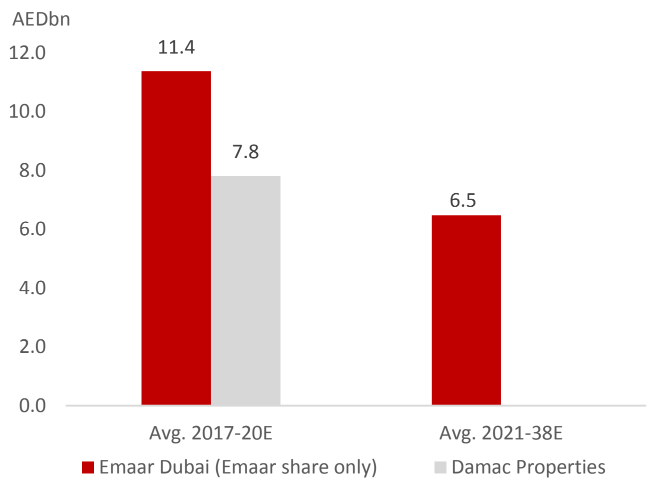
Damac's 2017-20E pre-sales is expected to be 31% below Emaar Properties' Dubai pre-sales (100% owned projects + 50% share in JV projects). Beyond next five years, Emaar continues to offer visibility for additional 18 years but Damac's lacks further visibility.

Fig. 179. Damac exceeded Emaar's Dubai pre-sales in 2014/15 but lost its edge since 2016



Source: Company, ADCB Securities Equity Research.

Fig. 180. We expect Damac's 2017-20E pre-sales to be 31% below Emaar

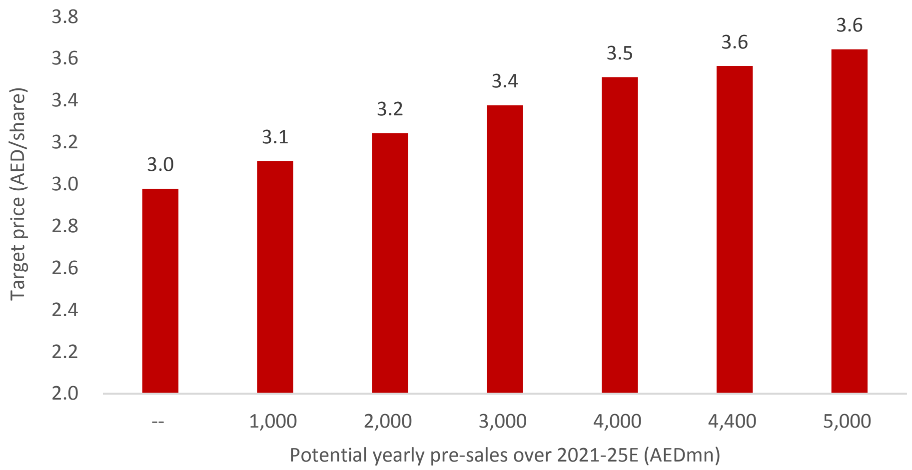


Source: Company, ADCB Securities Equity Research Estimates.

Damac's management is looking to acquire land bank to enhance pre-sales visibility. In last five years, Damac had been able to add land bank with favorable payment terms (spread over four to five years) and avoid upfront large land liability. While it is expected that the company would be able to add more land bank, it is difficult to predict the size, pricing or payment terms, which will be key drivers of incremental valuation addition for shareholders.

We have tried to do scenario analysis and gauge potential upside risks to pre-sales beyond 2020E. We assume two scenarios for potential land acquisition: **1/** Pre-sales value similar to Aykon City (AED5bn) i.e. lower end of major land acquisitions done by Damac in last five years, and **2/** Pre-sales value similar to Akoya Oxygen (AED22bn) i.e. higher end of major land acquisitions done in last five years. Based on average development timeframe of five years, first scenario would add pre-sales visibility of AED1bn p.a. over 2021-25E while second scenario would add pre-sales visibility of AED4.4bn p.a. over 2021-25E. Assuming gross profit margin of 45% and SG&A of 7.5% of pre-sales, we see upside potential of AED0.1/share to AED0.6/share to our target price on above two scenarios respectively.

Fig. 181. Potential upside to target price assuming pre-sales visibility beyond 2020E



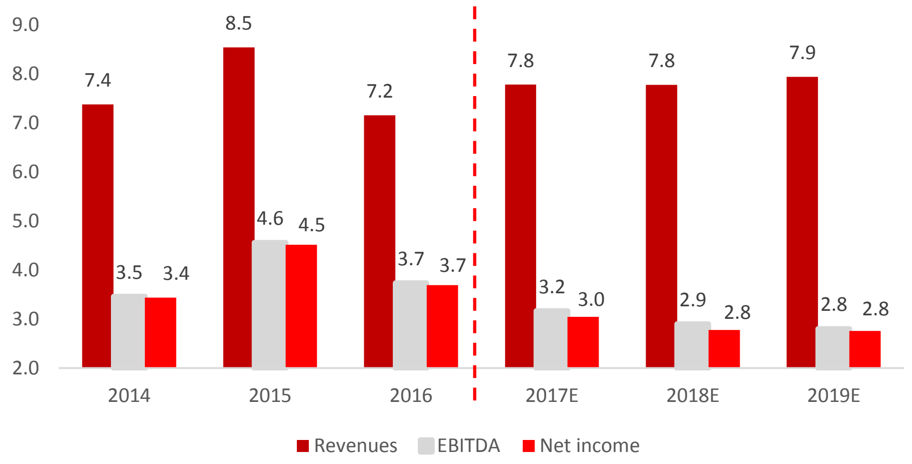
Source: ADCB Securities Equity Research Estimates.

Earnings outlook weak, revenues lack diversification

Earnings expected to decline in 2016-19E

We expect Damac's net profit to decline at a CAGR of 9% over 2016-19E despite stable revenues profile.

Fig. 182. Damac's earnings expected to decline - AEDbn



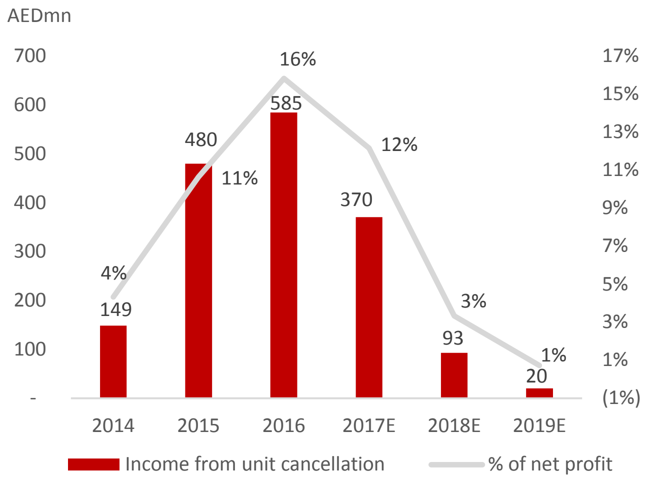
Source: Company, ADCB Securities Equity Research Estimates

The key reason for decline in earnings estimates are:

- **Phasing out of unit cancellation income**
  In 2017, we expect unit cancellation income to account for 12% of net profit. However, we expect its contribution to decline significantly in 2018. Damac witnessed increase in other income starting 2015, driven by cancellation of units sold in crisis period. On cancellation, Damac forfeits customer payments received against unit and recognizes it as other income. Unit cancellation income accounted for 10% of 2015 net profit and 16% of 2016 net profit. Management had indicated in the previous results conference call that unit cancellation income can continue for 2-3 more quarters. We therefore expect phasing out of this income as main reason for decline in earnings.

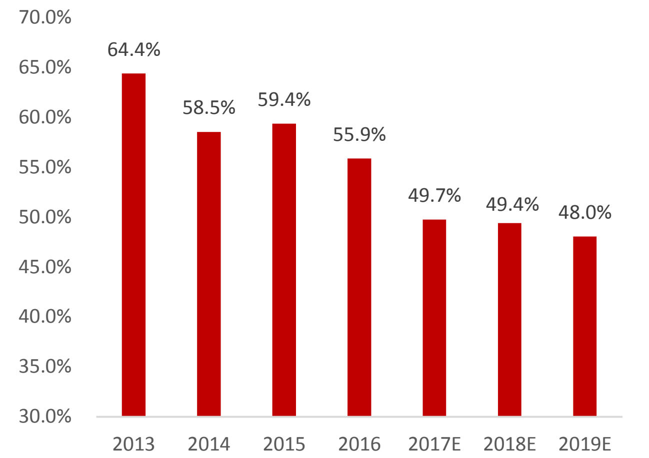
- **Lower margins**
  We expect Damac's gross profit margin to decline gradually over next few years as contribution of low margin construction revenues increase. As per its accounting policy, Damac recognizes land part of villas immediately after collection of down payment. Revenues pertaining to built-up-area (BUA) are recognized on percentage completion basis. Historically, Damac saw higher gross profit margins as high margin land recognition lifted the performance. However, as Damac starts to deliver projects and execution increases, contribution of low margin construction revenues should increase, thereby impacting its margins.

Fig. 183. Income from unit cancellation is likely to drop



Source: Company, ADCB Securities Equity Research Estimates.

Fig. 184. Gross profit margin also expected to decline



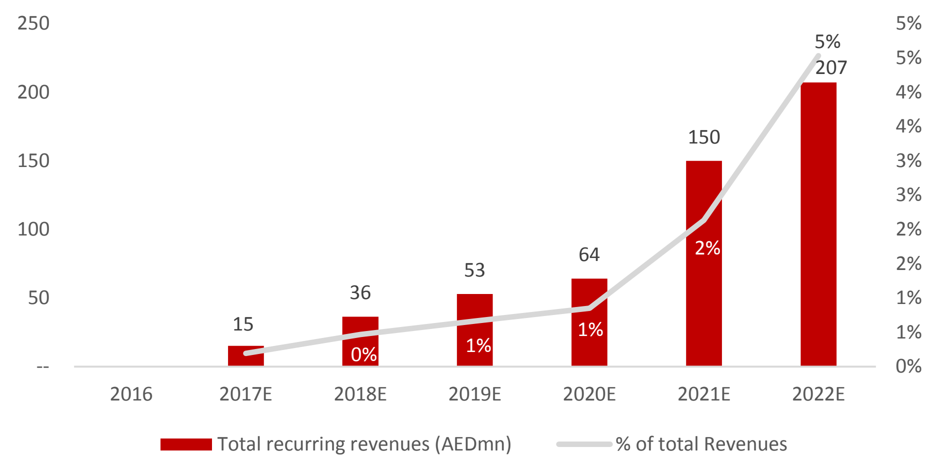
Source: Company, ADCB Securities Equity Research Estimates.

Recurring income contribution likely to remain insignificant

Damac is a pure play real estate developer with earnings largely driven by development business. It is exposed to recurring income through management of serviced apartments in hotel pool, but we estimate its contribution to be insignificant. Damac aims to grow its recurring income to AED367mn (US$100mn) by 2020. Key drivers of recurring income as targeted by management are: **1/** Leasing of residential units at Damac Hills. Damac has allocated ~20% of its apartment pipeline at Damac Hills for leasing rather than selling, **2/** Damac plans to allocate one tower (with planned BUA of 700k sqft) out of six towers at Aykon City for office, and **3/** community and other retail at its master planned developments of Damac Hills and Akoya Oxygen.

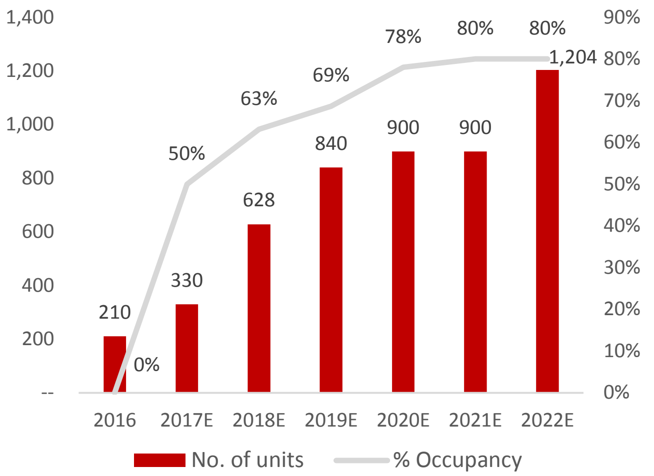
We have only factored residential and office leasing income in our estimates. We have excluded retail due to lack of details on planned retail developments. We expect recurring income of AED207mn by 2022E. Our estimates imply recurring income to contribute 5% to 2022E revenues.

Fig. 185. Damac's recurring income revenues and its contribution



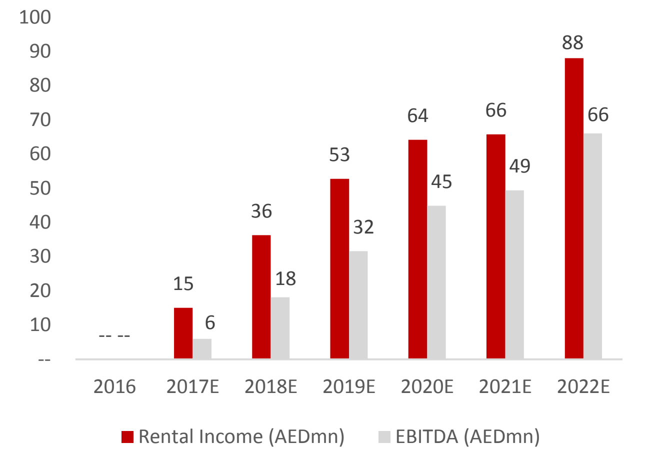
Source: Company, ADCB Securities Equity Research Estimates.

Fig. 186. Estimated residential units for leasing



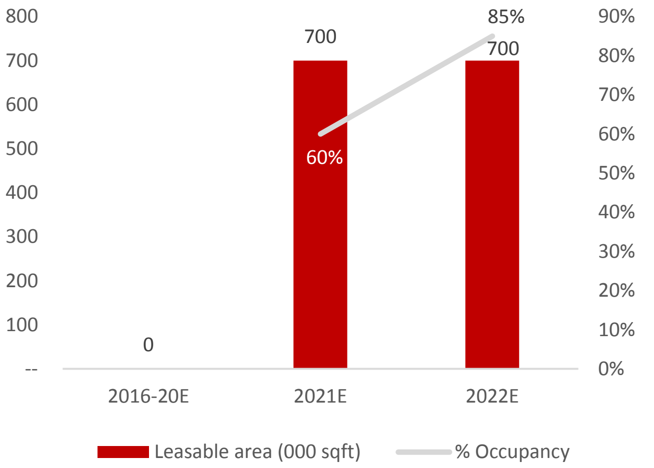
Source: Company, ADCB Securities Equity Research Estimates.

Fig. 187. Evolution of residential leasing revenues and EBITDA



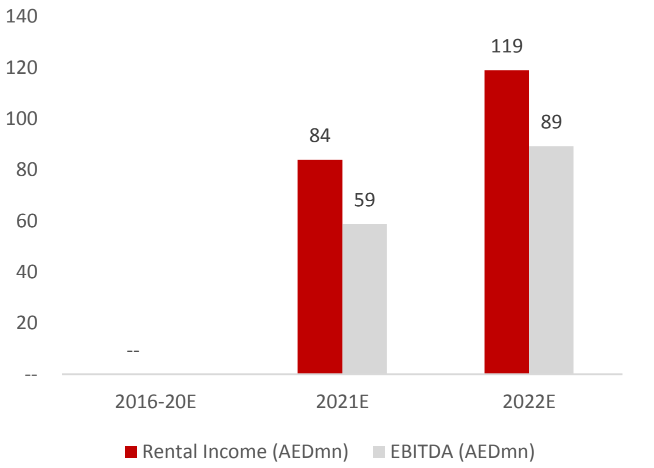
Source: Company, ADCB Securities Equity Research Estimates.

Fig. 188. Office leasable area – likely to kick in post 2020



Source: Company, ADCB Securities Equity Research Estimates.

Fig. 189. Evolution of office leasing revenues and EBITDA



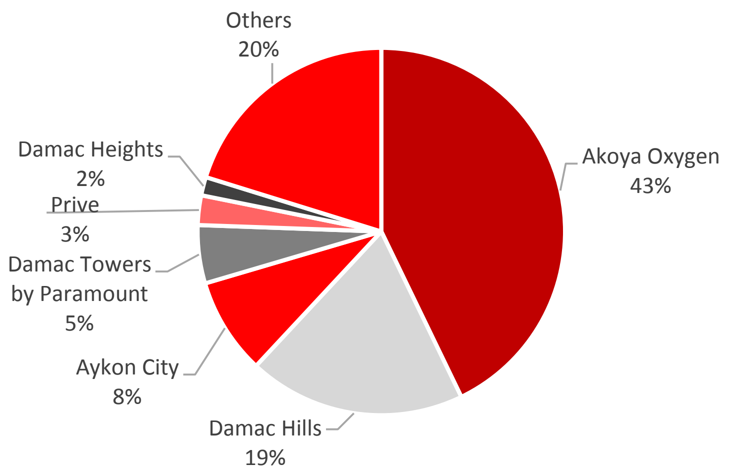
Source: Company, ADCB Securities Equity Research Estimates.

Project de-risking to support execution but earnings volatility unlikely to wane off

Damac's management has focused on de-risking its portfolio by targeting to sell each project at least equivalent to cost of the project (typically 50%). This strategy is well reflected in its marketing efforts, which are largely geared towards two major projects of Damac Hills and Akoya Oxygen (62% of development pipeline and 60% of our valuation). We estimate that these two projects accounted for ~65% of total pre-sales in 2016 and we expect this trend to continue in next four years. We believe that these two projects are close to being de-risked.

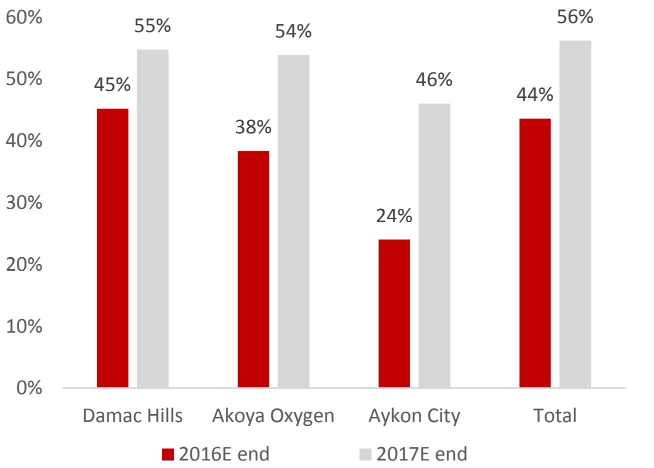
Focus on de-risking should reduce the execution risk, unlike 2009-10 crisis, where many projects were put on hold due to lack of funding. Having said that, Damac is likely to see continued volatility in cash flows given cyclical nature of development business and insignificant recurring income contribution.

Fig. 190. Damac's development pipeline by projects – Akoya Oxygen and Damac Hills account for 62% of pipeline



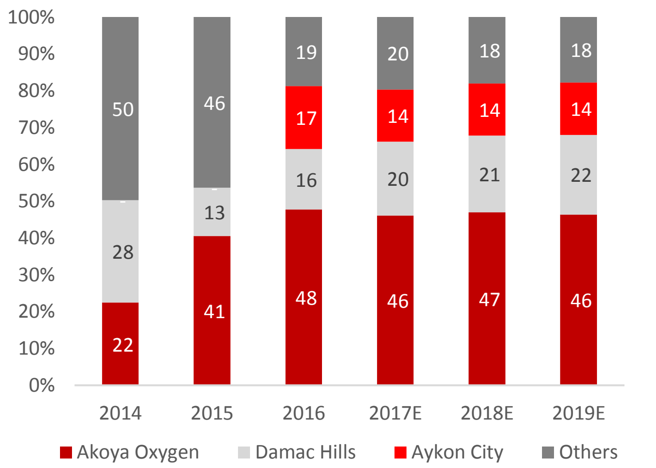
Source: Company, ADCB Securities Equity Research Estimates.

Fig. 191. Percentage sold by projects – expecting major portfolio to be de-risked by 2017



Source: Company, ADCB Securities Equity Research Estimates.

Fig. 192. Damac's pre-sales by projects –Akoya Oxygen key focus given its size and company's strategy to de-risk

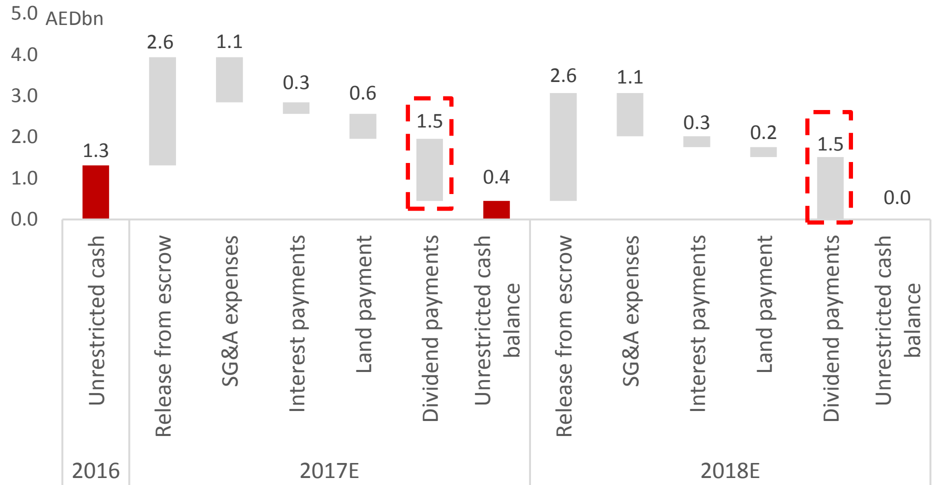


Source: Company, ADCB Securities Equity Research Estimates.

Escrow releases to support dividend payments

Damac's cash flows from operations turned negative in 2016 post slowdown in cash collection. Despite this, Damac was able to pay its committed dividend of AED0.25 per share. We highlight here that Damac's future dividend paying ability depends on release of cash profit from escrow account. As per real estate laws, all customer payments are deposited in escrow balance and can be utilized only for construction purpose. On project completion and handover, gross profit of project is released and becomes freely available to use by the company. In 2016, Damac was able to release ~AED2.4bn (US$650mn) from escrow and the management expects ~AED2.6bn (US$700mn) to be released this year. Along with the last year's free cash balance (AED1.3bn), this should be sufficient to meet operating/financial expenses, land commitments, as well as maintain last year dividends. While management has not disclosed dividend policy for this year, it has been indicated that they would like to retain Damac as high dividend payout stock. In our assumption for dividend paying ability, we only factor existing land commitments. If Damac acquires more land bank this year, we would expect shortfall in cash flows to maintain dividend payment. This needs to be funded by debt.

Fig. 193. Damac's free cash balance sufficient to maintain dividend payments



Source: Company, ADCB Securities Equity Research Estimates.

Valuation is expensive

We use DCF methodology to value cash flows from pre-sales of units. We completely exhaust its land bank by 2020 and assume no increase in selling prices given cyclical nature of development business. For expected recurring income, we use a cap rate of 8% on fully mature recurring EBITDA (2022E) and discount it to 2018E. We derive a target price of AED3.0/share, offering downside of 17% from current share price.

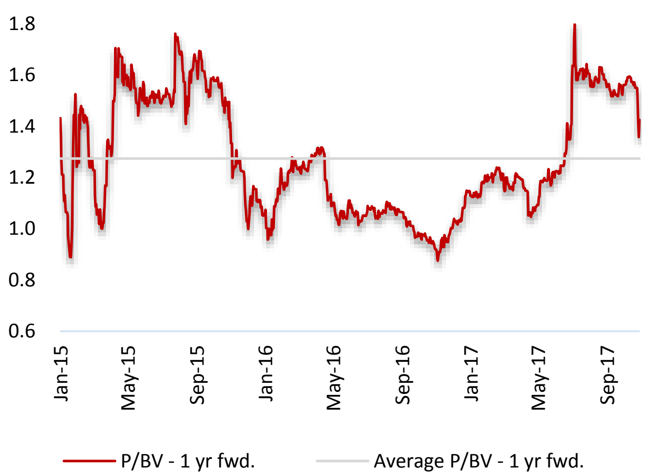
Fig. 194. Damac's sum-of-the-parts valuation

AEDmn	Value	Value/ Share (AED)	% of assets	Methodology
Development properties	12,789	2.1	93%	DCF @ WACC of 11.2%
Investment properties	912	0.2	7%	DCF of cash flows till 2022 and cap rate of 8% applied on 2022E EBITDA (discounted to 2018E)
Enterprise Value	**13,701**	**2.3**	**100%**	
Add: Financial Investments	1,017	0.2		At 2018E BV
Add: Cash & cash Equivalents	6,793	1.1		At 2018E BV
Less: Total Debt	(3,489)	(0.6)		At 2018E BV
Equity value	**18,021**	**3.0**		
No. of outstanding shares (mn)	6,050			
Target price per share (AED)	**3.0**			
Current share price (AED)	3.6			
Upside / downside (%)	(17%)			

Source: ADCB Securities Equity Research Estimates.

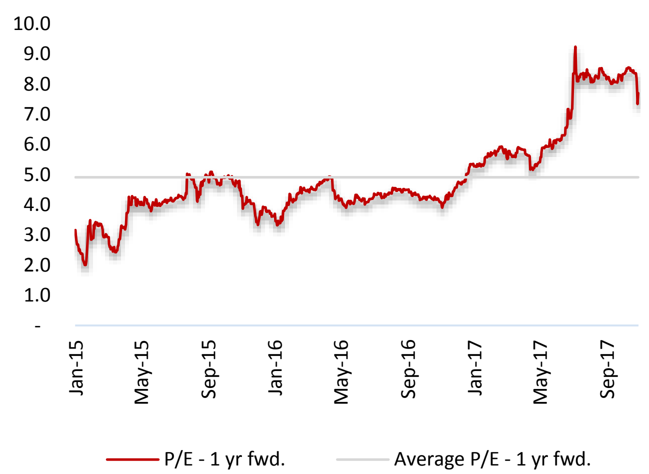
The stock is trading at a 2018E P/BV of 1.4x or 12% premium to historical average and 30% above emerging markets (EM) peers. At our valuation, the stock would trade at 2018E P/BV of 1.2x. We believe given Damac's weak earnings outlook (CAGR of -9% over 2016-19E), lack of recurring income contribution and less visibility, it is likely to trade at a discount to peers.

Fig. 195. Damac trades at 1.4x 1 yr. fwd book, 12% above its historical average



Source: Bloomberg, ADCB Securities Equity Research Estimates.

Fig. 196. And at 7.7x 1 yr. fwd earnings, 57% above its historical average



Source: Bloomberg, ADCB Securities Equity Research Estimates.

Market implying aggressive pre-sales growth for Damac

Damac's current market cap. is only 10% below our valuation of Emaar's Dubai development business. This is despite significantly higher visibility offered by Emaar's Dubai land bank vs. Damac. In our view, Damac's current valuation already captures significantly higher pre-sales than offered by its current land bank. Its current share price implies that average yearly pre-sales will increase to AED10bn p.a. over 2017-20E (28% above AED7.8bn expected in 2017E) and additional AED2.0bn p.a. over 2021-25E. To increase pre-sales to such a level, the company would be required to buy land bank with potential sales value of AED19bn, similar to value of its second largest project Damac Hills.

Fig. 197. Sensitivity of Damac's target price to different pre-sales scenarios

Target price (AED/share)		Annual pre-sales over 2017-20E (AEDmn)					
		7,800	8,000	9,000	10,000	11,000	12,000
Annual pre-sales over 2021-25E (AEDmn)	--	3.0	3.0	3.1	3.3	3.4	3.6
	1,000	3.1	3.1	3.3	3.4	3.6	3.7
	2,000	3.2	3.3	3.4	3.6	3.7	3.8
	3,000	3.4	3.4	3.5	3.7	3.8	4.0
	4,000	3.5	3.5	3.7	3.8	4.0	4.1
	4,400	3.6	3.6	3.7	3.9	4.0	4.2
	5,000	3.7	3.7	3.8	4.0	4.1	4.2

Source: Company, ADCB Securities Equity Research Estimates.

Key risks

Better than expected recovery in Dubai property market would drive higher pre-sales and increase in selling prices. This would result in higher cash flows. Also, significant land acquisition would increase pre-sales visibility, which is not yet captured in our target price.

Recommendation history

Rating	Coverage Universe %

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Rating	Potential upside / (downside) %
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Hold	(10%) – 15%
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SALES CONTACTS

Call Center
800 3325 (within UAE)
+971 2 621 1608 (outside UAE)
adcbsecurities@adcb.com

Head of Institutional Desk
Chahir Hosni
+971 2 696 2700
Chahir.Hosni@adcb.com