Research Update:

Dubai-Based Real Estate Developer Emaar Properties Outlook Revised To Stable From Negative On Stronger Demand

June 27, 2021

Rating Action Overview

- The Dubai residential real estate market is gaining momentum as stronger demand drives prices up in some areas of the emirate for the first time since 2015.
- Emaar Properties PJSC has the lion's share of the growth thanks to its leading market position, as indicated by the surge in property presales in the United Arab Emirates (UAE) to UAE dirham (AED) 10.5 billion over the first five months of 2021, compared to AED6.3 billion reported for all of 2020.
- We expect a rebound in the company's earnings and credit metrics in 2021, with EBITDA likely to exceed AED8 billion and funds from operations (FFO) to debt to improve to about 30%.
- We therefore revised our outlook on Emaar Properties to stable from negative and affirmed our 'BB+' long-term issuer credit rating on the company.
- We also revised our outlook on Emaar Malls PJSC, a core Emaar Properties subsidiary, to stable from negative and affirmed our 'BB+' issuer credit rating on the entity, which is aligned with that on Emaar Properties. Our 'bbb-' stand-alone credit profile (SACP) on Emaar Malls is unchanged.
- The stable outlook indicates our expectation that Emaar Properties' adjusted FFO to debt will reach close to 30% at the end of 2021 and will stay above that in the following years.

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Rating Action Rationale

The Dubai real estate market is gaining momentum as the emirate emerges from a COVID-19-induced slowdown. After a tough 2020, data for first-quarter 2021 suggests that the residential real estate market in Dubai has bottomed out and now offers attractive opportunities for developers, especially for premium properties. While sale prices continued to decline at a low-single-digit rate for the residential sector overall in first-quarter 2021, many higher-end properties increased in price. Also, sales volume in Dubai increased 15% overall in the quarter, indicating strong demand. Given that Emaar Properties accounts for more than half of primary sales in Dubai and focuses specifically on premium properties, we think that it will materially benefit from the observed uptick in demand and higher prices. We expect that the company will deliver about 6,000 units in 2021 after delivering 4,800 units in 2020. We also think that handovers will increase to close to 10,000 in 2022, based on the project completion pipeline.

We forecast more than 30% revenue growth in 2021 on supportive market trends for real estate and a gradual recovery in other business segments. A sharp contraction in demand in 2020 due to COVID-19-linked lockdown measures, the slump in international travel, and the waning of consumer confidence resulted in a 57% decline in development property sales in the UAE to AED6.3 billion. In addition, some projects were put on hold and new ones were cancelled. In 2021, Emaar Properties resumed new projects in response to higher demand. It reported AED10.5 billion of sales for the first five months of 2021, and we think that full-year sales will likely outpace the AED14.8 billion recorded in 2019. We expect increasing vaccination rates will provide additional traction to the residential real estate segment in Dubai. We also expect that the company's international operations, which account for 25% of its revenue, will demonstrate solid growth, mainly from Egypt, Turkey, and Pakistan based on the pipeline of project handovers. We further think that the hospitality segment will benefit from higher tourist numbers and the recent authorization for hotels to operate at 100% occupancy. We think revenue from the retail segment will gradually recover because we understand that Emaar Properties is no longer providing rent relief measures to tenants, and footfall and spending are recovering. We foresee a minimal contribution from the new Dubai Hills Mall, set to open in fourth-quarter 2021, with a gradual ramp-up in 2022 and assumed 70%-75% occupancy. Under our revised base-case scenario, we think that revenue in 2021 will exceed AED26 billion.

Increased earnings will lead to improved credit metrics and a stronger financial risk profile. As a result, we revised our financial risk profile assessment to intermediate from significant. With expected EBITDA of AED8.0 billion in 2021, up from AED4.1 billion in 2020, we anticipate that the EBITDA margin will improve to about 30%, after a low 20.8% in the previous year. Consequently, we think that FFO to debt will be close to 30% in 2021-2022, up from 16.8% in 2020. We anticipate that Emaar Properties will continue generating materially negative free operating cash flow (FOCF) in 2020 of about AED3.0 billion, assuming some AED6.0 billion of working capital outflows and AED3.7 billion of capital expenditure (capex; including joint ventures). However, from 2022 onward, we think that working capital will no longer hinder FOCF because handover payments should outpace construction expense based on the current project pipeline. Our assumption, however, depends on the phasing in of new projects, payment collections, and payment delinquencies, so it could vary significantly. Still, we think that the company will generate more than AED3 billion-AED 4 billion of FOCF in 2022, which will reduce leverage.

We continue to factor in prudent financial policy focused on debt reduction. We assume that Emaar Properties will use excess cash for debt reduction rather than exceptional dividend distributions, because it remains committed to deleveraging its balance sheet. Also, management took actions over the past couple of years that helped moderate weaker credit metrics in a challenging pandemic year. The company generated close to AED6 billion in cash proceeds from disposals in 2019-2020, partly offsetting negative discretionary cash flow of about AED8 billion. Furthermore, in 2020, dividends were cancelled (except for the minority dividends at subsidiaries), capex was reduced, and cost reduction efforts were deployed across the board. While management could be considering further disposals of noncore assets, we don't factor this into our base-case scenario due to the uncertainty from completion timing and value. Furthermore, we no longer provide an uplift to the company's SACP for potential strategic actions through our financial policy adjustment, because we believe it has already taken most of those actions.

Outlook

The stable outlook reflects our expectation that Emaar Properties will achieve close to 30% FFO to debt by the end of 2021 and above that in the following year. It also reflects our view of the improving residential real estate market trend in Dubai especially for higher-end properties despite the structural oversupply. We believe that Emaar Properties is well positioned to capture the bulk of the growth in this segment. The stable outlook also factors in that the company will continue to focus on deleveraging, including debt reduction, using its available liquid assets or disposals proceeds.

Downside scenario

We could lower the rating on Emaar Properties in the next 12 months if the company's credit metrics weaken, including FFO to debt declining below 30% without near term prospects of recovery. This could be triggered, in our view, by:

- Protracted negative COVID-19-related ramifications that could weigh on Dubai's economic recovery and tourist volumes in the second half of 2021 or in 2022, and, as a result, on the recovery of the emirate's retail and hospitality sectors. We think further travel restriction measures globally could hinder demand for real estate from foreign investors; or
- A sharp rise in new supply of residential units from other developers that could further exacerbate market oversupply and pressure prices.

Upside scenario

We view the probability of a positive rating action as remote because it would largely depend on a notable improvement in credit conditions affecting Dubai, generally. However, our views could change if we see a more robust economic recovery than we expect.

We think that upward pressure on Emaar Properties' SACP could materialize if its FFO to debt were to improve to 40%, alongside stronger cash flow that is used by management for debt repayment, as well as additional management actions such as disposals, which could also help improve credit ratios.

Company Description

Emaar Properties is the largest listed property developer in the UAE. It reported revenue of AED19.7 billion in 2020, of which close to 75% represented domestic activities. the company also has activities in Egypt, Turkey, Saudi Arabia, and India. The company develops masterplan communities, including residential and commercial property, such as shopping centers, offices, recreational facilities, and hotels. The residential properties are typically divested, whereas Emaar Properties has retained a significant portfolio of high-end retail developments and hotels in Dubai as rental and operating assets. Established in 1997, Emaar Properties has been listed on the Dubai Financial Market since 2000. Key operating subsidiaries Emaar Malls and Emaar

Development (not rated) were listed in 2014 and 2017, respectively. Emaar Properties' market capitalization is close to AED29 billion.

Our Base-Case Scenario

Assumptions

- We expect Dubai's GDP to rebound about 3.5% in 2021, followed by growth of 2.5% in 2022.
- We think that Emaar Properties will continue to derive the bulk of its revenue from Dubai, which we estimate will account for about 75% in 2021. At the same time, we positively note that the company's presence outside of Dubai increased to about 25% of revenue in 2020, from 12% in 2019, fueled by strong international operations in the development segment.
- While we think that structural oversupply in Dubai's residential real estate sector will linger, we think that demand for good-quality, premium assets will support sales in 2021.
- We expect 30%-35% revenue growth in 2021, from high demand for residential real estate in Dubai and recovery in other business segments, namely the retail and hospitality sectors.
- Operating cash flow will remain positive, in our view, despite likely high working capital requirements of about AED6 billion, because we expect the company to continue to launch new projects in 2021.
- Capex estimated at AED3.7 billion in 2021 and AED2.7 billion in 2022, including for joint ventures.
- Dividend distributions will be in line with historical levels, but subject to available liquidity and market conditions.

Key metrics

- S&P Global Ratings-adjusted FFO to debt of close to 30% in 2021 and 30%-32%% in 2022.
- Debt to EBITDA of about 2.8x in 2021 and 2.7x in 2022.
- Negative FOCF of about AED3 billion in 2021, but with significantly reduced working capital requirements in 2022 leading to materially positive FOCF.

Liquidity

We view Emaar Properties' liquidity as strong because we see liquidity sources exceeding uses by more than 1.5x as of March 31, 2021, and more than 1.0x over the next 12 months.

Currently, the company has more than AED10 billion of undrawn credit lines. However, the $1.5 billion revolving credit facility (RCF) at Emaar Properties and the $2 billion RCF at Emaar Malls will mature in September and December 2021, respectively. Since these maturities are in less than 12 months, we don't include them as sources. Nevertheless, we expect that the company will roll them over, because we believe that it has a good standing in credit markets and solid bank relationships. Based on the company's track record and prudent financial policy, we think that in case of liquidity shortages, Emaar Properties could cancel dividend distributions and materially curtail capex.

Liquidity sources for the next 12 months include:

- Cash of AED10.2 billion, of which AED3.8 billion is cash held in escrow accounts with the Real Estate Regulatory Agency, Dubai's real estate regulator.
- AED3.1 billion of short-term liquid investments, of which AED1.9 billion is treasury bills in Egypt.
- Cash flow from operations of AED6.5 billion-AED7.0 billion for the next 12 months.

Liquidity uses for the same period include:

- Short-term debt of AED4.5 billion.
- About AED3.7 billion in capex on investment properties, including joint, ventures in 2021 and AED2.7 billion in 2022.
- Significant working capital outflows of above AED6 billion for 2021.
- Dividend distributions in line with historical levels, but subject to available liquidity and market conditions.

Covenants

We understand that Emaar Properties is not subject to maintenance covenants. The company is subject to incurrence covenants under its sukuk and RCFs. At the end of 2020, there was ample headroom under these covenants, and we expect this to continue in 2021.

Issue Ratings - Subordination Risk Analysis

Capital structure

At March 31, 2021, Emaar Properties' capital structure comprised $2 billion (AED7.3 billion) of senior unsecured sukuk certificates, AED10.7 billion of unsecured bank loans, and AED3.4 billion of secured bank loans.

Analytical conclusions

We rate debt issued by Emaar Properties 'BB+', the same as our long-term foreign currency issuer credit rating on the company. This reflects the absence of significant subordination risk.

Ratings Score Snapshot

Issuer Credit Rating: BB+/Stable/--

Business risk: Fair

- Country risk: Moderately high
- Industry risk: Intermediate
- Competitive position: Fair

Financial risk: Intermediate

- Cash flow/leverage: Intermediate

Anchor: bb+

Modifiers

- Diversification/portfolio effect: Neutral (no impact)
- Capital structure: Neutral (no impact)
- Financial policy: Neutral (no impact)
- Liquidity: Strong (no impact)
- Management and governance: Satisfactory (no impact)
- Comparable rating analysis: Neutral (no impact)

Stand-alone credit profile : bb+

- Likelihood of government support: Low (no impact)

Related Criteria

- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Corporates | General: Corporate Methodology: Ratios And Adjustments, April 1, 2019
- Criteria | Corporates | General: Reflecting Subordination Risk In Corporate Issue Ratings, March 28, 2018
- General Criteria: Rating Government-Related Entities: Methodology And Assumptions, March 25, 2015
- General Criteria: Methodology For Rating Sukuk, Jan. 19, 2015
- Criteria | Corporates | General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- Criteria | Corporates | Industrials: Key Credit Factors For The Homebuilder And Real Estate Developer Industry, Feb. 3, 2014
- Criteria | Corporates | General: Corporate Methodology, Nov. 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities, Nov. 13, 2012
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Ratings List

Ratings Affirmed; Outlook Action

	To	From
Emaar Properties PJSC		
Emaar Malls PJSC		
Issuer Credit Rating	BB+/Stable/--	BB+/Negative/--
Emaar Properties PJSC		
Emaar Malls PJSC		
EMG Sukuk Ltd.		
Senior Unsecured	BB+	

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. A description of each of S&P Global Ratings' rating categories is contained in "S&P Global Ratings Definitions" at https://www.standardandpoors.com/en_US/web/guest/article/-/view/sourceId/504352 Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column. Alternatively, call one of the following S&P Global Ratings numbers: Client Support Europe (44) 20-7176-7176; London Press Office (44) 20-7176-3605; Paris (33) 1-4420-6708; Frankfurt (49) 69-33-999-225; Stockholm (46) 8-440-5914; or Moscow 7 (495) 783-4009.