



SHUAACAPITAL<sub>PSC</sub>

# Emaar Properties

## Equity Research

## H1 06 results update

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|                           |           |                  |                        |
|---------------------------|-----------|------------------|------------------------|
| <b>Current Price:</b>     | AED 12.40 | <b>Country:</b>  | United Arab Emirates   |
| <b>Fair value Target:</b> | AED 18.74 | <b>Sector:</b>   | Real Estate            |
| <b>Recommendation:</b>    | BUY       | <b>Exchange:</b> | Dubai Financial Market |

- We revise our definition of Emaar Properties (Emaar), and reintroduce it as a diversified, regional large-scale real estate developer with growth targets of becoming a fully integrated global property developer as well as a provider of associated social and financial services on a commercial basis.
- We forecast revenues of AED 12.01 bn, gross profits of AED 7.21 bn, EBITDA of AED 6.00 bn and net profits of AED 6.38 bn during FY 06. We forecast consolidated revenues, gross profits, and net income to grow at CAGRs of 22.5%, 15.5%, and 14.5% by 2009, respectively. We find that Emaar's international growth strategy may produce revenue contributions by late 2007, and eventually reach 65% of total revenue by 2010.
- We adopt a sum-of-parts approach on Emaar's diverse range of services, to arrive at a fair value estimate of **AED 18.74/share**. The 10% downward revision of our estimate from AED 20.58/share is primarily due to a higher discount rate on projected cash flows. We upgrade our recommendation from Neutral to **Buy** on the stock, and observe a substantial 50% in upside potential from the stock's most recent closing price of AED 12.40/share.

| Year  | Net profit<br>(AED'000) | BV<br>(AED'000) | EPS<br>(AED) | BVPS<br>(AED) | RoaA<br>(%) | P/E<br>(x) | EV/EBITDA<br>(x) | P/BV<br>(x) |
|-------|-------------------------|-----------------|--------------|---------------|-------------|------------|------------------|-------------|
| 2008E | 8,200,029               | 42,999,440      | 1.35         | 7.05          | 0.24        | 8.70       | 7.68             | 1.66        |
| 2007E | 7,832,051               | 37,540,629      | 1.28         | 6.16          | 0.25        | 9.11       | 8.23             | 1.90        |
| 2006E | 6,381,009               | 31,941,931      | 1.05         | 5.24          | 0.22        | 11.18      | 10.19            | 2.23        |
| 2005  | 4,731,231               | 25,560,922      | 0.78         | 4.19          | 0.19        | 15.07      | 14.46            | 2.79        |

|                         |             |
|-------------------------|-------------|
| 52-week range           | 10.65-28.75 |
| Number of shares ('000) | 6,096,325   |
| Free Float (%)          | 34          |
| Market cap (AED'000)    | 71,022,186  |
| Market cap (USD'000)    | 19,336,288  |
| Div. Yld. 2005 (%)      | 3.4         |

Source: Reuters, SHUAA Capital

Emaar Properties price vs. SC UAE Index



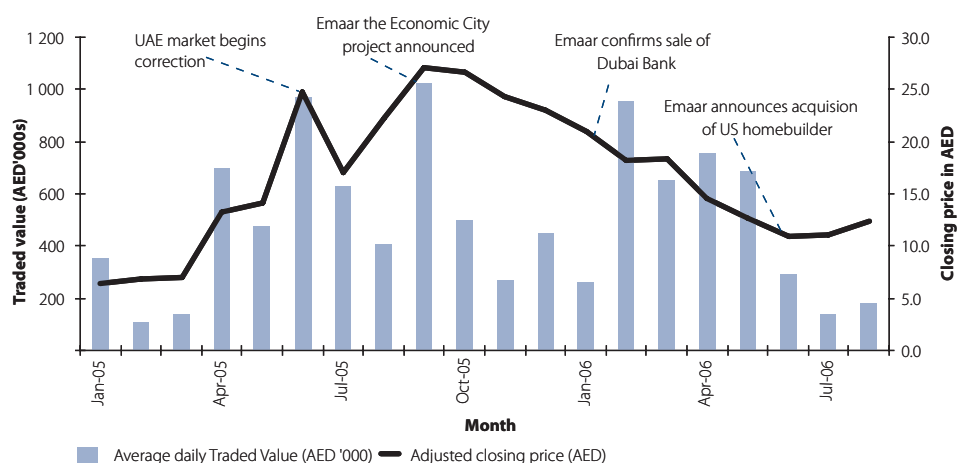
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## Investment highlights

- We revise our definition of Emaar, and reintroduce it as a diversified, regional large-scale real estate developer with growth targets of becoming a fully integrated global property developer as well as a provider of associated social and financial services on a commercial basis.
- We find it plausible that Emaar will develop this strategy further, establishing additional regional entities and ventures and consequently acquiring or establishing supporting functions along the way.
- The Emaar brand remains strong in the UAE, as the developer currently accounts for roughly 20% of all announced residential units to be delivered in Dubai over the next five years. Emaar nevertheless maintains over AED 30 bn (as of December 31st 2005) in available land bank. This may be sufficient to fuel growth (and fund international expansions) on the local front until other entities within the company gather pace.
- During Q2 06, Emaar announced its investment in Turner International ME, in partnership with global contractor The Turner Corporation. Earlier in the quarter, Emaar announced the acquisition of John Laing Homes in the United States, along with Hamptons International, a UK-based realtor, in Q3 06. Emaar also announced the first of its plans to establish a series of international schools across the Middle East, North Africa- (MENA), and India, as well as a similar foray into healthcare services, with announcements of AED 18.35 bn in capital expenditures over the coming 10 years.
- Emaar's strategic objective, in which it leverages its success in Dubai by replicating its most successful features in markets around the region, is now very clear. This encompasses securing sizeable and strategically located land concessions together with strong local partners, and developing fully integrated communities on them. Emaar's transitioning business model is likely to start showing clear results by 2008, whereas management's target of generating 70% of revenues from overseas is expected to be achieved by 2010.
- Q2 06 registered a 27% rise in revenues compared to Q1 06, and a 51% rise from the AED 1.88 bn recorded in Q2 05, making it the most profitable quarter since Emaar's incorporation. Overall, the first half of the year closed up 8% in terms of top-line growth from the AED 4.72 bn registered in H1 05. Both quarters of the current year showed (i) contributions from key portfolio components, such as units at the Arabian Ranches development (ii) robust land sales, and (iii) rising 'take up' rates of sellable units across the board.
- Q2 06 revenues were 14% above our estimate of AED 2.44 bn for the quarter, while bottom-line results fell within 2% of our estimate of AED 1.58 bn. The divergence in top-line figures is due to stronger-than-expected sales recognition of properties, and the consolidation of sales figures pertaining to the newly acquired John Laing Homes, for the month of June 2006, while our net income estimate fell very close to the announced figure due to lower net margins than our estimate.
- Land sales, which Emaar has traditionally made at margins exceeding 70%, totaled more than AED 650 mn in Q1 06, and were concentrated within the Emirates Hills and Dubai Marina developments, of which Emaar still retains a sizable land bank available for further sale or development.
- FY 06 will remain anchored in residential property sales. Rising 'take-up' rates in a number of developments, with emphasis on Emaar's Arabian Ranches properties and Burj Dubai, produced (somewhat) higher unit sales in H1 06 than in H1 05. For the remainder of the year, revenue recognition from the development will continue, along with fresh contributions from Burj Dubai and Dubai Marina.

- We forecast revenues of AED 12.01 bn, gross profits of AED 7.21 bn, EBITDA of AED 6.00 bn and net profits of AED 6.38 bn during FY 06. We forecast consolidated revenues, gross profits, and net income to grow at CAGRs of 22.5%, 15.5%, and 14.5% by 2009, respectively. We find that Emaar's international growth strategy may produce revenue contributions by late 2007, and eventually reach 65% of total revenue by 2010.
- We forecast consolidated gross and net margins to experience downward pressure, as a result of higher development costs going forward, in both of its local and international portfolios. We project gross margins of 52% in FY 07, and 45% in FY 09. We also project a similar contraction in net margins to 47% and 41% by FY 07 and 09 respectively.
- We adopt a sum-of-parts perspective on Emaar's diverse range of services, to arrive at a fair value estimate of AED 18.74/share. The 10% downward revision of our estimate from AED 20.58/share is primarily due to a higher discount rate on projected cash flows. However, we incorporate value-enhancing developments on the international front, and evidence of progress in a number of markets and business lines, particularly in India and Saudi Arabia, as well as acquisitions and joint ventures in Dubai and abroad. We upgrade our recommendation from Neutral to Buy on the stock, and observe a substantial 50% in upside potential from the stock's most recent closing price of AED 12.40/share.



Source: Reuters, SHUAA Capital

## Redefining Emaar

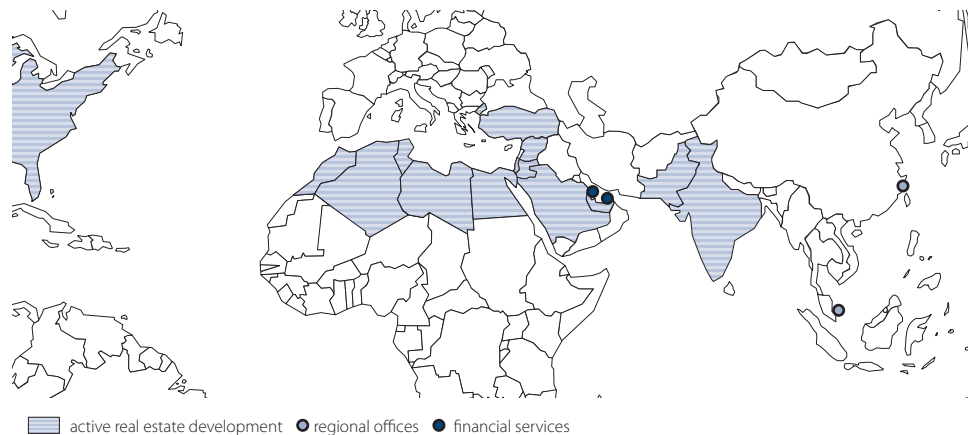
### *A diversified regional property developer*

We previously viewed Emaar as a real estate developer operating out of Dubai, UAE. We then expended that definition to one which includes some regional joint ventures relating to real estate development. From the company's new mission statement of becoming "one of the world's most valuable companies" and "becoming an international brand name by 2010", we can draw little more than the conclusion that growth is high on the agenda, to say the least. The full statement made by management at an AGM in Q1 06 is:

*"Vision 2010' sees Emaar as not only the number 1 real estate company, but one of the most valuable companies in the world beyond property development and irrespective of business activity. Emaar's mission is to deliver world-class products and services...in every chosen business activity, from real estate, hospitality, leisure, retail, education, healthcare and finance."*

We readdress Emaar from this point forth as a diversified regional property developer. We maintain some conservatism in our definition, since our task is to identify and quantify value, not to perceive it. Any expansions by Emaar into ancillary fields will be the subject of future updates.

### *Regional footprint*



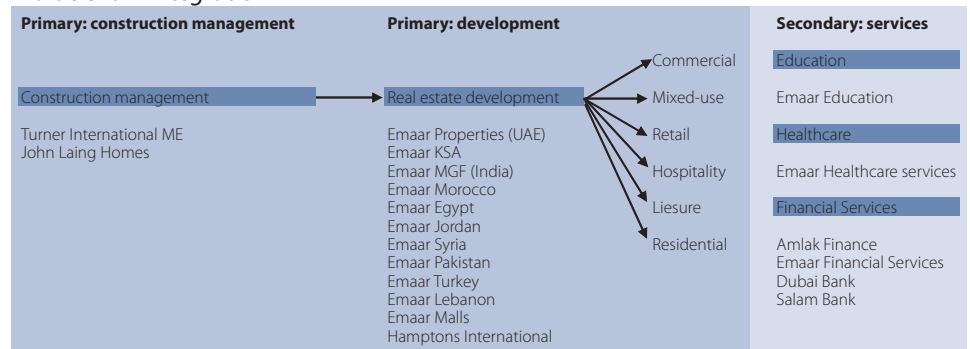
Source: SHUAA Capital

**Integration of value chain elements**

**What is Emaar?**

Our definition: A diversified, regional large-scale real estate developer with growth targets of becoming a fully integrated property developer as well as a provider of associated social and financial services on a commercial basis. This is an articulation of Emaar's announced forays into construction management, hospitality and leisure services, education, and healthcare during the past 18 months and in turn what Emaar is earmarking its capital expenditures into over the coming five years. Beginning as a local property developer and expanding into the region, Emaar has since pursued the integration broadly related elements under its umbrella. We find it plausible that Emaar will continue along this trajectory; establishing regional entities and ventures and consequently acquiring or establishing supporting functions along the way.

**Value chain integration**



Source: SHUAA Capital

The end result is summed up in greater exposure to all phases of a property-based value chain. Whether such an approach can create substantially more value is the question to address.

**Primary: Real estate development and construction management**

**Emaar still holds a sizable land bank**

**Real Estate Development:**

This is and will likely continue to be the value anchor of Emaar Properties. The Emaar brand remains strong in the UAE, as the developer currently accounts for roughly 20% of all announced residential units to be delivered in Dubai over the next five years. Due to the eventual erosion of its local land bank, Emaar may shift its focus from a high-margin sales-based model towards higher exposure to rental income. Management targets the expansion of rental income contributions to over 7% in FY 06, and between 20-25% of overall income (excluding international operations), within the next five years. Emaar nevertheless maintains over AED 30 bn (at market value as of December 31st, 2005) in available land bank. This may be sufficient to fuel growth (and fund international expansions) on the local front until other entities within the company gather pace.

**Key acquisitions in Q2 06**

In August 2006, Emaar announced the 100% acquisition of Hamptons International via an all-cash deal worth AED 562.5 mn. Hamptons International was purchased from former parent Wheelock Properties. The Hamptons brand and management team are expected to remain unchanged post-acquisition. Hamptons' 130 year track record in international property transactions will serve to establish a valuable transaction pipeline and an extensive client pool for Emaar, in our view.

**Construction management**

During Q2 06, Emaar announced its investment in Turner International ME, in partnership with global contractor The Turner Corporation. The venture aims to tap into regional opportunities in construction management and building services, starting with Emaar's own. Turner International is in fact the construction manager at the Burj Dubai main structure, as well as the Dubai Mall. The move can generate substantial value, as Emaar can effectively mitigate construction management risk across its international portfolio. Earlier in the quarter, Emaar announced the acquisition of John Laing Homes in the United States.

John Laing Homes is the second largest privately held homebuilder in the USA, with revenues of US\$1.6 billion and 2,891 residential closings in 2005. The company finished 2005 with revenues of more than US\$1.6 billion on 2,891 residential closings. Based in Newport Beach, California, John Laing Homes operates mainly in the states of California and Colorado. The company indicated that the acquisition will likely draw on the target's broad experience in building large residential communities, and leverage that experience in the regions that Emaar is active in.

**AED 15.0 bn CAPEX earmarked  
for retail space development**

### Retail

In September 2005, Emaar announces plans to develop about 100 malls in the emerging markets of the Middle East, North Africa, and the Indian subcontinent, via investments of over AED 15.0 bn. Emaar announced the incorporation of a fully owned subsidiary, Emaar Malls, which is expected to set up operations in the UAE, Saudi Arabia, Jordan, Syria, Lebanon, Algeria, Morocco, India and Pakistan. Development work on the 12 mn square foot Dubai Mall, at Emaar's existing Burj Dubai development, will fall under Emaar Malls' management.

| Retail                               | Gross leasable area, sq-ft |
|--------------------------------------|----------------------------|
| Dubai Mall                           | 12,000,000                 |
| Gold & Diamond Park, phases I and II | 354,184                    |
| Marina Walk                          | 60,000*                    |
| Emaar Towers                         | 11,465                     |
| Emirates Living, Town Centre         | 60,000                     |
| Arabian Ranches, Community Center    |                            |
| Meadows, Community Center            |                            |
| Greens Centre, phases I and II       |                            |
| Lakes Centre                         |                            |
| Springs Community Center             |                            |
| <b>Total</b>                         | <b>12,425,649</b>          |

\*Including outdoor landscaping

\*\*Approximate

Source: Emaar Properties, SHUAA Capital

### Secondary: Services

#### Hotels

Emaar Hotels and Resorts is a subsidiary of Emaar Properties, and was initially established as a joint venture with Giorgio Armani SPA. Its objective is to develop and operate a branded five-star hotel chain on a global level, with an initial phase of ten hotel facilities. The first property will occupy a number of floors at the Burj Dubai development in Dubai, while future properties are expected to be released as part of the deal with Armani SPA, once the primary facility is launched in 2008.

#### Education

In Q1 06, Emaar announced the first of its expansion plans outside of the real estate development arena, in which it plans to establish a series of international schools across the Middle East, North Africa- (MENA), and India. Emaar announced strategic partnerships with education specialists, as well as announcing that it had already finalized acquisition transactions with existing institutions. Although the move is a departure from traditional real estate development, it makes, in our view, sense given that (i) Emaar plans to establish its educational facilities within its upcoming regional residential and community-level developments, securing a 'captive market', and (ii) general consensus about the relative shortage of quality educational facilities in some of the core markets Emaar Properties is involved in. Emaar has announced total capital expenditures of AED 2.50 bn towards the initiative over the coming five years. We forecast substantial further cash injections into expanding this arm of its business across the MENA region and India.

**New business line:  
educational services**

**AED 18.35 bn  
investments in  
healthcare services  
over 10 years**

#### **Healthcare**

The first quarter of the year also saw Emaar announce a similar foray into healthcare services, with announcements of AED 18.35 bn in capital expenditures over the coming 10 years, to be used in developing hospitals, clinics, and medical centers throughout the MENA and South Asia regions. Emaar targets the development of 100 hospitals over the period, at a combined capacity of 20,000 beds and equipped with extensive medical infrastructure. Similarly, this is likely to mainly target communities that Emaar develops, and represents another angle through which Emaar can secure a captive market for its services.

**Growing exposure to  
regional financial services  
industry: Salam Bank**

#### **Financial Services**

Emaar still retains a 30% stake in Dubai Bank, a previously fully-owned subsidiary that was partially sold to Dubai Holding in Q4 05 for approximately AED 800 mn. Apart from broad commercial banking services, Dubai Bank has introduced new business lines such as Islamic Banking, Asset Management and Investment Banking. Interestingly, the company has since participated along with its mortgage finance subsidiary, Amlak Finance, as the main founder of Al Salam Bank in Bahrain, a newly set up Sharia-compliant bank.

Emaar has had exposure to the mortgage finance industry of the UAE via its subsidiary Amlak Finance, which was initially established to exclusively facilitate property transactions involving Emaar, but which later expanded its business to finance properties sold by other developers. Amlak has since ventured into a number of non-core businesses, including securities brokerage, industrial manufacturing, and auto finance, and has established an office in Abu Dhabi, as part of its strategy of growing beyond Dubai and eventually, into a regional presence. Furthermore, Amlak Investment, its AED 500 mn independent investment arm, is effectively a hedge-fund model with the purpose of exploiting any proprietary investment opportunities in the region. Emaar has retained a 48.02% stake in Amlak Finance since its initial public offering in 2004.

Furthermore, and presumably as a move to gain exposure to capital market gains and trading activity in FY 05, Emaar established its subsidiary Emaar Financial Services (paid-in capital base of AED 5.0 mn), in which it holds a sizable stake along with joint venture partners Amlak Finance and Global Investment House of Kuwait.

#### **Other elements:**

Emaar Industries and Investments, a joint stock entity set up in Q1 05 with a paid-in capital base of AED 250.0 mn, was established to undertake investments in industrial projects both in and outside of the UAE. Emaar retains a 40% stake, along with Amlak Finance (a 10% partner), and various UAE investors, who collectively hold 50% of equity claims on the company. The company intends to invest in existing manufacturers in the UAE, in addition to pursuing joint ventures with leading industrial establishments and a focus on technology-related industries in the UAE and abroad.

***KSA, India & Morocco  
are Emaar's main  
international markets***

**Going forward- international joint ventures**

Emaar's strategic objective, in which it leverages its success in Dubai by replicating its most successful features in markets around the region, is now very clear. This encompasses securing sizeable and strategically located land concessions together with strong local partners, and developing fully integrated communities on them. Demand for such developments has proven to be high, as it successfully overcomes much of the problems presented by old urban infrastructure in many of the locations Emaar is currently targeting.

Emaar released its planned cash commitments towards international operations in Q1 06. The largest portion of initial capital injections lies in Saudi Arabia, as part of Emaar's equity contribution towards the establishment of a joint venture named 'Emaar the Economic City'. The company had recently undergone an IPO on the Saudi Arabian exchange. Emaar MGF Land Private Ltd, a joint venture with an Indian counterpart, will receive 15% of Emaar's planned investment funds during the year. A number of other ventures were announced, as summarized below:

| Market   | % FY 06 equity investments | Emaar estimated ROI | % of FY 10 revenues |
|----------|----------------------------|---------------------|---------------------|
| KSA      | 31%                        | 25-30%              | 22%                 |
| India    | 15%                        | 30-40%              | 11%                 |
| Morocco  | 8%                         | 30-35%              | 6%                  |
| Egypt    | 7%                         | 20-30%              | 5%                  |
| Jordan   | 4%                         | 20-30%              | 3%                  |
| Syria    | 3%                         | 20-30%              | 2%                  |
| Pakistan | 3%                         | 25-30%              | 2%                  |
| Turkey   | 2%                         | 25-30%              | 2%                  |
| Lebanon  | 2%                         | 20-30%              | 2%                  |
| Other    | 24%                        | 20-30%              | 17%                 |
| Total    |                            |                     | 72%                 |

Source: Emaar Properties, SHUAA Capital

Emaar's transitioning business model is likely to start showing clear results by 2008, whereas management's target of generating 70% of revenues from overseas is expected to be achieved by 2010. We provide an overview of announced international ventures, as per Emaar management's planned investments over the coming three years:

***Saudi Arabia***

Since its launch in Q4 05, the King Abdullah Economic City development in Saudi Arabia has received its initial site works as well as excavations for the town center marina and canal. The development totals AED 100 bn in value, in which Emaar is a joint venture partner with a Saudi counterpart. The venture resulted in the establishment of Emaar the Economic City (EEC), which is currently being floated on the Saudi Arabia market through an IPO. Emaar (through itself and five subsidiaries) will retain 30.58% of EEC post-floatation.

***India***

Emaar's joint venture in India, Emaar MGF Land Private Ltd has acquired prime land plots during 2005, for the development of luxury hotels in Delhi and Kolkata. The joint venture is expected to announce further plans for investments in the Indian residential, commercial, and mixed-use property sectors. The venture is also likely to disclose details of further hospitality facilities, which are expected to cover a range of luxury and budget hotels to be built over the coming 3-5 years.

Emaar's Hyderabad International Convention Centre-HICC, among the largest and most highly equipped convention facilities in India, became operational in Q1 06, and is, according to management, receiving extensive advance bookings for the coming year.

***Extensive mixed-use  
developments in Egypt***

***Morocco***

Emaar's announced property development schemes in Morocco include an AED 19.8 bn Memorandum of Understanding with the Moroccan government for three community-style developments along the Atlantic coast, including world class golf and ski resorts, luxury accommodations and spas. The developments are in addition to Emaar's Amelkis II and Amelkis III and Bahia Bay developments announced earlier last year (in which joint venture partner ONA, the country's largest conglomerate, has been a participant). The total development value of Emaar's projects in Morocco currently stand at AED 25.3 bn, making the country one of Emaar's largest investment commitments outside of the UAE, and a potential expansion gateway to other markets.

***Egypt***

Emaar's Cairo-based joint venture with the Artoc Group for Investment and Development- (AGID), known as Emaar Misr for Development- (EMD), announced the signing of a Memorandum of Understanding in May 2006 with the Alexandria Library for a waterfront redevelopment project. The project is intended to provide a range of facilities along a portion of the Alexandrian coast, including extensive hotel facilities. The project was Emaar's fifth announcement concerning property development deals in Egypt. Previously, the 4.0 mn square foot residential development 'Cairo Heights' was announced, as well as a 280 acre integrated community development at Egypt's Smart Village, consisting of a convention centre, serviced apartments, a hotel, and commercial, retail and residential space. Later, in Q3 06, Emaar won an auction for 625 hectares of prime land along the Egyptian Mediterranean coast, via a bid worth AED 642.3 mn. The seven-kilometer strip is to be developed into a tourism project, including a 5-star hotel facility, golf courses, a marina, and shopping and sporting facilities. Emaar is expected to incur AED 6.38 bn in development costs over the project's five-year lifespan. Emaar is likely to expand its Egypt portfolio further over the coming five years.

***Syria***

In a joint venture with IGO, an offshore investment and property development company, Emaar announced plans for a mixed-use development in the Yafour area of Syria, a short distance from the Damascus. The AED 1.84 bn project will be based on the stylistic features of Emaar's Dubai-based developments. Again, this is an example of Emaar's strategy of 'exporting' business competencies developed at home. Named 'The Eighth Gate', the development is segmented into three zones, including a commercial centre, which consists of a 35 storey office tower, a number of commercial buildings, and 450,000 square feet of retail space. The remaining two segments include a low-rise residential district named the Waterfront, and a residential 'community' zone.

***Applying the Dubai model  
on an international level***

***Pakistan***

Emaar signed a Memorandum of Understanding with Pakistan's Port Qasim Authority during Q2 06, for a mixed-use land development in Karachi, along with three master-planned communities in Islamabad and Karachi. The combined development value of the projects is around AED 8.80 bn. The developments are an extension of Emaar's business model in Dubai, centered around long-term agreements with municipal and governmental entities for the development of community-scale mixed-use projects. The benefits of such a model are significant; (i) long-term property management deals can be effected, generating recurring income streams, (ii) opportunities for the development of education, healthcare, and retail space become immediately available, for which Emaar has established specialized subsidiaries, and (iii) strategic alliances with local governments will likely be a valuable source of future ventures.

***Turkey***

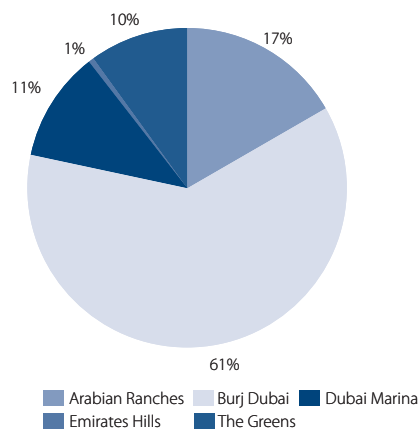
Emaar announced a development project at a total value of AED 2.57 bn in Turkey in Q1 06. A joint venture named the Lakeside Project will involve Emaar Properties and Atasay, the largest gold jewelry exporter in Turkey. A total of 600 luxury residential units with supplementary recreational space will be built during the initial phase. Emaar expects to follow up its initial development with further phases worth AED 18-37 bn over the coming few years.

## Financial Analysis and Forecasts

### **Q2 06: the most profitable quarter in Emaar's history**

Q2 06 registered a 27% rise in revenues compared to Q1 06, and a 51% rise from the AED 1.88 bn recorded in Q2 05, making it the most profitable quarter since Emaar's incorporation. Overall, the first half of the year closed up 8% in terms of top-line growth from the AED 4.72 bn registered in H1 05. This does not necessarily imply, however, that operational growth was flat. Q1 05 was an exceptionally strong quarter, skewing Emaar's performance in light of spikes in property prices, abnormally high sales figures, and disproportionately strong land sales. Both quarters of the current year showed (i) contributions from key portfolio components, such as units at the Arabian Ranches and Dubai Marina developments, (ii) robust land sales, and (iii) rising 'take up' rates of sellable units across the board. Robust sales of units at the Burj Dubai development, Emaar's largest portfolio component, were particularly strong during the period. Sales of units within the main tower structure however, have as of yet had no impact on reported sales figures, due to Emaar's revenue recognition policy.

### **Emaar Properties- portfolio composition**



Source: SHUAA Capital

### **Stronger property sales at lower margins than expected**

- Q2 06 revenues were 14% above our estimate of AED 2.44 bn for the quarter, while bottom-line results fell within 2% of our estimate of AED 1.58 bn. The divergence in top-line figures is due to stronger-than-expected sales of properties, and the consolidation of sales figures pertaining to the newly acquired John Laing Homes, for the month of June 2006, while our net income estimate fell very close to the announced figure due to lower margins than we expected. We had expected larger sales volumes of high-margin land units, which did not occur during Q2 06. We also anticipated a mild decline in net margins, but not to the extent to which it occurred during the quarter (an estimate of 65%, versus 68% in Q1 and a surprise 54% in Q2).

### **Margins**

| Emaar Properties- margins |       |       |       |       |       |       |
|---------------------------|-------|-------|-------|-------|-------|-------|
| Margins                   | Q2 06 | Q1 06 | Q4 05 | FY 05 | 9M 05 | Q1 05 |
| Gross                     | 59%   | 66%   | 59%   | 57%   | 57%   | 51%   |
| EBITDA                    | *50%  | 62%   | 56%   | 54%   | 53%   | 46%   |
| Net                       | 54%   | 68%   | 63%   | 57%   | 55%   | 47%   |

\*Approximate

Source: Company financial statements, SHUAA Capital

### **Q206 margins impacted by land sales**

- Q2 06 marked a reversal in a trend that has been clear since the boom in Dubai's property market began in 2004. A broad-based contraction in margins, despite the 27% rise in sales, curtailed quarterly gross, EBITDA, and net income growth rates to 13%, 2.5%, and 2% respectively. We attribute this to a possible decline in land sales, which as discussed later on, buoyed Q1 06 results and produced the highest gross margins in Emaar's history. We view this development positively: the decline in high-margin land sales and the substitution of which by value-added real estate development activity

## A 27% Q-o-Q expansion in sales volumes

is a solid indicator of operational growth. We are much more comfortable with Emaar generating value by delivering residential and commercial units, rather than by eroding further its land bank.

Land sales, which Emaar has traditionally made at margins exceeding 70%, totaled more than AED 650 mn in Q1 06, and were concentrated within the Emirates Hills and Dubai Marina developments, of which Emaar still retains a sizable land bank available for further sale or development.

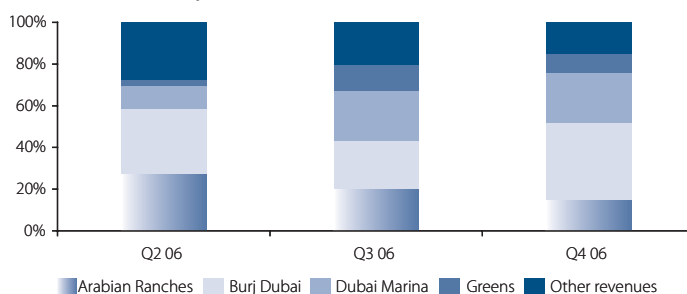
- A counter-effect to the impact of declining unit sales during the quarter had been (i) Emaar's continuous re-pricing strategy, geared at capturing value created by controlling supply of residential space, and therefore property prices, and (ii) the cost inelasticity of fixed-rate construction contracts with Emaar's contractors. Material prices and labor costs remain a core driver of rising construction costs, which are borne by contractor in fixed-rate contracts with Emaar.

## The rest of the year...

- FY 06 will remain anchored in residential property sales. Rising 'take-up' rates in a number of developments, with emphasis on Emaar's Arabian Ranches and Burj Dubai properties, produced (somewhat) higher unit sales in H1 06 than in H1 05. With practically all units of Emaar's Arabian Ranches sold in H1 06, revenue contributions from the development will continue to feature in FY 06 results, due to Emaar's revenue recognition policy.

## H2 06 to remain concentrated in Burj Dubai and Dubai Marina unit sales

## Revenue composition, FY 06



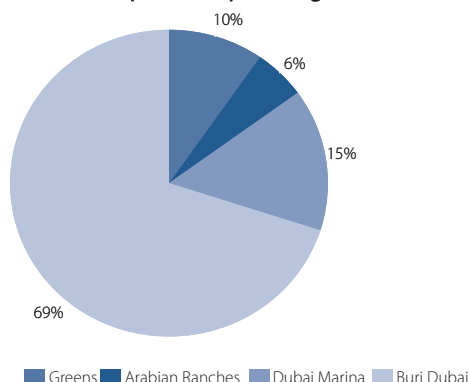
Source: SHUAA Capital

- Burj Dubai, Emaar's largest portfolio component in terms of sellable value, will command the bulk of revenue contributions during the year. We estimate, that as of the date of publication of this report, the main lower structure remains below the 20% completion mark. We project that Emaar can reach this threshold by the closing quarter of the year. At least 20% of the construction work associated with a structure, along with 20% cash receipts in lieu of sold properties must be accrued before Emaar can begin recognizing and booking revenues on its property sales (according to its revenue recognition policy). Q2 06 saw the handover of the first phase of residential units, 'The Residences', to buyers, as well as the release of new towers for development.

## Retail space to feature in FY 06 contributions

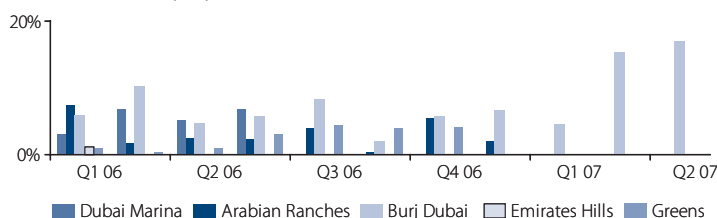
Rental income from retail space at the Gold & Diamond Park will feature in FY 06 contributions. Outlets will be operational during the year, generating recurring income contributions starting at AED 250 mn in FY 06. Further retail space contributions are expected starting FY 07.

## Emaar Properties- upcoming units, 07-09



Source: SHUAA Capital

## Product mix, %, FY 06-07



Source: SHUAA Capital

## The big picture

### International transition to take effect by 2008

Emaar management has indicated that it is targeting a 70:30 mix in its sales figures between international and Dubai-based activities, by 2010. It expects initial contributions from international subsidiaries and joint ventures by 2008. We opt to forecast a more gradual transition, as we feel that the company has less control over the progress of projects in other countries than in does in Dubai, as well as the higher risk associated with developments in some of these countries, as the recent unfortunate events in Lebanon have demonstrated. We forecast a 65% contribution from international sources by 2010, composed mainly of unit sales in Saudi Arabia, India, Egypt and Morocco.

### A number of hotel facilities to operate in 2007/08

- With all land acquisition costs pertaining to Emaar KSA and Emaar MGF already incurred in FY 05, and pre-sales of residential and commercial units already in place, the developments (which are proportionately consolidated as associate entities) will contribute a pipeline of income (we project AED 2.31 bn in contributions during 2010), without further CAPEX expectations.
- Rental income on retail space is expected to make a more effective contribution to FY 06 results, and to rise in line with the delivery of retail space throughout the forecast period.
- Hospitality services, whereby Emaar will develop hotel properties and later outsource the management to third parties, are expected to generate a stable income stream as of FY 08. We restrict this component to a number of Dubai-based facilities, until solid announcements are made regarding the next series of branded international hotel properties.

***Gross, EBITDA, and net  
margins to contract  
significantly by 2010***

**Putting it all together**

- We forecast revenues of AED 12.01 bn, gross profits of AED 7.21 bn, EBITDA of AED 6.00 bn and net profits of AED 6.38 bn during FY 06. We forecast consolidated revenues, gross profits, and net income to grow at CAGRs of 22.5%, 15.5%, and 14.5% by 2009, respectively. We find that Emaar's international growth strategy may produce revenue contributions by late 2007, and eventually reach 65% by 2010. Emaar's aggressive growth targets are likely to impact consolidated cash flows well into 2009 due to high capital expenditures. This is stated keeping in mind that the bulk of CAPEX associated with international joint ventures rests in land acquisition costs. Land acquisitions associated with Emaar's two largest projects, the King Abdullah Economic City in Saudi Arabia and components of its Indian portfolio have already been incurred in 2005. This mitigates the cash flow impact of acquisition CAPEX going forward.

We forecast consolidated gross and net margins to experience downward pressure, as a result of higher development costs going forward, in both of its local and international portfolios. We project gross margins of 52% in FY 07, and 45% in FY 09. We also project a similar contraction in net margins to 47% and 41% by FY 07 and 09 respectively.

## Valuation

| Emaar Properties                      |                  |              |
|---------------------------------------|------------------|--------------|
| Sum of parts valuation- AED           |                  |              |
| Activity                              | Entity           | Value/share  |
| Dubai real estate development         | Emaar Properties | 8.02         |
| International real estate development | Various          | 7.91         |
| Other                                 | Various          | 2.81         |
| <b>Total</b>                          |                  | <b>18.74</b> |

Source: SHUAA Capital

**A sum-of-parts target  
of AED 18.65/share**

We maintain our approach set forth in previous reports in valuing Emaar's operations. We adopt a sum-of-parts perspective on Emaar's diverse range of services, to arrive at a fair value estimate of **AED 18.74/share**. The 11% downward revision of our estimate from AED 20.58/share is primarily due to a higher discount rate on projected cash flows. However, we incorporate value-enhancing developments on the international front, and evidence of progress in a number of markets and business lines, particularly in India and Saudi Arabia, as well as acquisitions and joint ventures in Dubai and abroad.

### Emaar Properties

| Sum of parts valuation- AED |                          |               |                                              |                     |
|-----------------------------|--------------------------|---------------|----------------------------------------------|---------------------|
| Segment                     | Entity                   | Country       | Method                                       | Fair value estimate |
| Manufacturing               | Emaar Industries         | UAE           | Book value                                   | 0.04                |
| Construction management     | Turner International ME  | UAE           | 20% premium to acquisition value             | 0.59                |
|                             | John Laing Homes         | USA           | 20% premium to acquisition value             | 0.76                |
| Real estate development     | Emaar Properties         | UAE           | Discounted cash flows                        | 8.02                |
|                             | Emaar The Economic City  | KSA           | Discounted cash flows                        | 1.32                |
|                             | Emaar MGF                | India         | Discounted cash flows, rental capitalization | 6.48                |
|                             | Emaar Morocco            | Morocco       |                                              |                     |
|                             | Emaar Egypt              | Egypt         |                                              |                     |
|                             | Emaar Jordan             | Jordan        |                                              |                     |
|                             | Emaar Syria              | Syria         |                                              |                     |
|                             | Emaar Pakistan           | Pakistan      |                                              |                     |
|                             | Emaar Turkey             | Turkey        |                                              |                     |
|                             | Emaar Lebanon            | Lebanon       |                                              |                     |
|                             | Emaar Algeria            | Algeria       |                                              |                     |
|                             | Various                  | Other         |                                              |                     |
|                             | Emaar Malls              | International |                                              |                     |
|                             | Emaar Hotels             | International |                                              |                     |
|                             | Hamptons International   | UK            | 20% premium to acquisition value             | 0.11                |
| Services                    | Emaar Education          | UAE           | Discounted cash flows                        | 0.36                |
|                             | Emaar Healthcare         | UAE           | Discounted cash flows                        | 0.24                |
|                             | Amlak Finance            | UAE           | Market value of equity stake                 | 0.75                |
|                             | Emaar Financial Services | UAE           | Book Value                                   | 0.01                |
|                             | Dubai Bank               | UAE           | At sale value                                | 0.056               |
| <b>Total</b>                |                          |               |                                              | <b>18.74</b>        |

Source: SHUAA Capital

The change in our value target is a result of several other factors, as summarized below:

- Operational factors and forecast revisions: We have revamped our estimates for FY 06 and the remainder of the explicit forecast period, revising our revenues, gross profit, EBITDA, and net income estimates by 3%, -2%, -4% and -11% respectively. We expect a less aggressive and more consistent delivery schedule of Dubai-based properties, and little in the way of earnings surprises going forward. We also expect gross and EBITDA margins to remain strong on core properties, and the recognition of the first 20% (if not more) tranche of Burj Dubai during the year.
- Valuation parameters: We incorporate a single discount rate across all discounted cash flows, regardless of country or business segment. We adopt a risk-free rate of 6.00%, in-line with our process of estimating the yield of a simulated UAE 10-year bond, based on an existing set of Qatari sovereign bonds and yields on US Treasuries. We adopt a beta of 1.0 going forward, due partly to a broadening of activities across business lines as well as the fact that Emaar remains a broad proxy for the Dubai Financial Market.

#### Assumptions

| AED '000 unless otherwise stated       | Old        | New        | Change (% or bps) | Reason                                           |
|----------------------------------------|------------|------------|-------------------|--------------------------------------------------|
| Revenue FY 06 (Dubai operations)       | 11,676,868 | 12,009,928 | 3%                | Revised delivery schedule                        |
| Revenue CAGR FY 06-10 (consolidated)   | 33%        | 18%        | (15)              |                                                  |
| Gross profits FY 06 (Dubai operations) | 7,321,289  | 7,205,957  | -2%               |                                                  |
| Gross margin (consolidated)            | 63%        | 60%        | -3                |                                                  |
| EBITDA FY 06 (Dubai operations)        | 6,270,978  | 6,003,515  | -4%               | Weaker blended margins; lower land sales         |
| EBITDA margin (consolidated)           | 54%        | 50%        | -4                |                                                  |
| Net profit (Dubai operations)          | 7,185,207  | 6,381,009  | -11%              | Revised delivery schedule                        |
| Net margin (consolidated)              | 62%        | 53%        | -8                | Weaker blended margins; lower land sales         |
| Fair value estimate (AED/share)        | 20.53      | 18.65      | -9%               | Operational assumptions and valuation parameters |
| Discount rate                          | 9.81%      | 11.00%     | 12%               | Interest rates, risk                             |
| risk-free rate                         | 5.66%      | 6.00%      |                   | Interest rate hikes                              |
| Equity risk premium                    | 5.00%      | 5.00%      |                   | Unchanged                                        |
| Beta                                   | 0.83       | 1.00       |                   | Broader correlation to regional economy          |
| Terminal growth rate                   | 3.50%      | 2.50%      |                   | Shift to international profile                   |

Source: SHUAA Capital

We upgrade our recommendation from Neutral to **Buy** on the stock, as we revise our earnings estimates and readdress the value of the company's international ventures. Our target price of **AED 18.74/share** represents a substantial 51% in upside potential from the stock's most recent closing price of AED 12.40/share.

## Financials

### Consolidated Balance Sheet (AED'000)

| Year to December                                              | 2004              | 2005              | 2006E             | 2007E             | 2008E             | 2009E             |
|---------------------------------------------------------------|-------------------|-------------------|-------------------|-------------------|-------------------|-------------------|
| <b>Assets</b>                                                 |                   |                   |                   |                   |                   |                   |
| <b>Current assets</b>                                         |                   |                   |                   |                   |                   |                   |
| Cash and banks                                                | 1,834,965         | 10,368,009        | 13,001,636        | 12,234,936        | 18,345,959        | 20,233,462        |
| Trade receivables                                             | 756,181           | 717,533           | 3,602,979         | 6,651,653         | 8,046,399         | 8,918,092         |
| Loans and advances                                            | 758,316           | 658,313           | 987,470           | 1,382,457         | 1,866,317         | 2,426,213         |
| Other receivables, deposits, and prepayments                  | 240,588           | 1,928,369         | 2,041,688         | 3,325,826         | 3,786,541         | 4,196,749         |
| Securities                                                    | 1,847,611         | 3,602,868         |                   |                   |                   |                   |
| Total current assets                                          | 5,437,661         | 17,275,092        | 19,633,772        | 23,594,872        | 32,045,217        | 35,774,517        |
| Growth %                                                      | -16.35%           | 217.69%           | 13.65%            | 20.17%            | 35.81%            | 11.64%            |
| <b>Long term assets</b>                                       |                   |                   |                   |                   |                   |                   |
| Investments in associates                                     | 388,324           | 3,103,825         | 3,476,284         | 3,736,485         | 4,549,801         | 5,957,124         |
| Fixed Assets, net                                             | 273,114           | 737,711           | 951,502           | 1,499,211         | 1,826,709         | 2,145,173         |
| Investment properties                                         | 2,456,802         | 8,062,354         | 10,077,943        | 13,101,325        | 14,411,458        | 15,132,031        |
| Development properties                                        | 2,232,805         | 3,025,750         | 4,031,177         | 7,860,795         | 7,205,729         | 7,566,015         |
| Other assets                                                  | 2,425,677         |                   |                   |                   |                   |                   |
| Total long term assets                                        | 7,776,722         | 14,929,640        | 18,536,906        | 26,197,816        | 27,993,697        | 30,800,343        |
| Growth %                                                      | 187.49%           | 91.98%            | 24.16%            | 41.33%            | 6.86%             | 10.03%            |
| <b>Total assets</b>                                           | <b>13,214,383</b> | <b>32,204,732</b> | <b>38,170,678</b> | <b>49,792,688</b> | <b>60,038,913</b> | <b>66,574,859</b> |
| Growth %                                                      | 43.55%            | 143.71%           | 18.53%            | 30.45%            | 20.58%            | 10.89%            |
| <b>Liabilities</b>                                            |                   |                   |                   |                   |                   |                   |
| <b>Current liabilities</b>                                    |                   |                   |                   |                   |                   |                   |
| Accounts payable and accruals                                 | 2,325,510         | 5,527,575         | 4,733,807         | 7,746,344         | 10,593,131        | 13,165,993        |
| Other liabilities                                             | 1,569,534         |                   |                   |                   |                   |                   |
| Current portion of long term contract payables and retentions | 329,975           | 470,657           | 468,819           | 733,702           | 993,415           | 1,172,604         |
| Short term loans from Financial Institutions                  | 400,000           |                   |                   |                   |                   |                   |
| Total current liabilities                                     | 4,625,019         | 5,998,232         | 5,202,626         | 8,480,046         | 11,586,546        | 14,338,596        |
| Growth %                                                      | 106.49%           | 29.69%            | -13.26%           | 63.00%            | 36.63%            | 23.75%            |
| <b>Long term liabilities</b>                                  |                   |                   |                   |                   |                   |                   |
| Long term contract payables and retentions                    | 288,565           | 262,464           | 468,819           | 698,763           | 946,110           | 1,066,003         |
| Provisions for end of service benefits                        | 7,486             | 9,035             | 12,010            | 16,629            | 18,933            | 20,984            |
| Long term loans from financial institutions                   | 238,693           | 238,693           | 305,093           | 2,724,038         | 3,541,249         | 1,362,019         |
| Total long term liabilities                                   | 534,744           | 510,192           | 785,922           | 3,439,430         | 4,506,291         | 2,449,006         |
| Growth %                                                      | 76.01%            | -4.59%            | 54.04%            | 337.63%           | 31.02%            | -45.65%           |
| Total liabilities                                             | 5,159,763         | 6,508,424         | 5,988,548         | 11,919,476        | 16,092,838        | 16,787,602        |
| Growth %                                                      | 102.85%           | 26.14%            | -7.99%            | 99.04%            | 35.01%            | 4.32%             |
| Minority interest                                             | 2,685             | 135,386           | 240,199           | 332,583           | 946,635           | 1,049,187         |
| <b>Shareholders' equity</b>                                   |                   |                   |                   |                   |                   |                   |
| Share capital                                                 | 2,650,000         | 5,780,176         | 5,780,176         | 5,780,176         | 5,780,176         | 5,780,176         |
| Statutory reserve                                             | 2,875,400         | 13,922,653        | 13,922,653        | 13,922,653        | 13,922,653        | 13,922,653        |
| General reserves                                              |                   |                   | 638,101           | 783,205           | 820,003           | 860,864           |
| Retained earnings                                             | 2,532,498         | 5,862,479         | 9,372,034         | 14,317,763        | 19,610,984        | 25,165,739        |
| Employee's performance share program                          | (5,963)           | (4,386)           | (4,386)           | (4,386)           | (4,386)           | (4,386)           |
| Dividends                                                     |                   |                   | 2,233,353         | 2,741,218         | 2,870,010         | 3,013,024         |
| Total shareholders' equity                                    | 8,051,935         | 25,560,922        | 31,941,931        | 37,540,629        | 42,999,440        | 48,738,070        |
| Growth %                                                      | 20.89%            | 217.45%           | 24.96%            | 17.53%            | 14.54%            | 13.35%            |
| <b>Total liabilities and shareholders' equity</b>             | <b>13,214,383</b> | <b>32,204,732</b> | <b>38,170,677</b> | <b>49,792,687</b> | <b>60,038,913</b> | <b>66,574,860</b> |
| Growth %                                                      | 43.55%            | 143.71%           | 18.53%            | 30.45%            | 20.58%            | 10.89%            |

Source: Emaar properties, SHUAA Capital

**Consolidated Income statement , (AED '000)**

| Year to December                   | 2004             | 2005             | 2006E            | 2007E            | 2008E            | 2009E            |
|------------------------------------|------------------|------------------|------------------|------------------|------------------|------------------|
| Revenues                           | 5,246,264        | 8,361,362        | 12,009,928       | 16,629,132       | 18,932,704       | 20,983,747       |
| Growth %                           | 40.98%           | 59.38%           | 43.64%           | 38.46%           | 13.85%           | 10.83%           |
| Cost of sales                      | -3,037,774       | -3,585,686       | -4,803,971       | -7,981,983       | -9,939,670       | -11,541,061      |
| <b>Gross profit</b>                | <b>2,208,490</b> | <b>4,775,676</b> | <b>7,205,957</b> | <b>8,647,148</b> | <b>8,993,034</b> | <b>9,442,686</b> |
| Growth %                           | 115.22%          | 116.24%          | 50.89%           | 20.00%           | 4.00%            | 5.00%            |
| Gross margin                       | 42.10%           | 57.12%           | 60.00%           | 52.00%           | 47.50%           | 45.00%           |
| Other income                       | 172,063          | 493,411          | 170,647          | 288,305          | 663,102          | 994,653          |
| SG & A                             | -707,599         | -1,021,752       | -1,307,685       | -1,389,528       | -1,621,680       | -1,907,997       |
| Management fees and others         | -110,209         | (92,300)         | -54,280          | -43,244          | -25,338          | -32,465          |
| Total operating expenses           | -817,808         | -1,114,052       | -1,361,965       | -1,432,771       | -1,647,019       | -1,940,461       |
| <b>Operating income</b>            | <b>1,562,745</b> | <b>4,155,035</b> | <b>6,014,639</b> | <b>7,502,682</b> | <b>8,009,118</b> | <b>8,496,878</b> |
| Operating margin                   | 30%              | 50%              | 50%              | 45%              | 42%              | 40%              |
| Net Interest income                | 81,443           | 352,386          | -1,428           | 16,722           | 19,230           | 22,114           |
| Share of results from an associate | 20,810           | 99,145           | 62,500           | 260,201          | 813,317          | 1,407,322        |
| Other income                       | 26,914           | 122,486          | 389,796          | 292,347          | 97,868           | 106,598          |
| Minority interest                  | -1,355           | 2,179            | -3,291           | -77,486          | -559,043         | -948,105         |
| Taxes on EBIT                      |                  |                  | (81,207)         | (162,415)        | (180,461)        | (476,168)        |
| <b>Net profit</b>                  | <b>1,690,557</b> | <b>4,731,231</b> | <b>6,381,009</b> | <b>7,832,051</b> | <b>8,200,029</b> | <b>8,608,640</b> |
| Profit margin                      | 32%              | 57%              | 53%              | 47%              | 43%              | 41%              |
| Growth %                           | 149.96%          | 179.86%          | 34.87%           | 22.74%           | 4.70%            | 4.98%            |

*Real estate development and construction*  
Source: Emaar properties, SHUAA Capital

**Key Ratios and Figures**

| Year to December                   | 2004        | 2005         | 2006E        | 2007E       | 2008E        | 2009E        |
|------------------------------------|-------------|--------------|--------------|-------------|--------------|--------------|
| <b>Growth</b>                      |             |              |              |             |              |              |
| Revenues                           | 41%         | 59%          | 44%          | 38%         | 14%          | 11%          |
| EBITDA                             | 163%        | 160%         | 42%          | 24%         | 7%           | 3%           |
| Net income                         | 150%        | 180%         | 35%          | 23%         | 5%           | 5%           |
| Equity                             | 21%         | 217%         | 25%          | 18%         | 15%          | 13%          |
| Assets                             | 44%         | 144%         | 19%          | 30%         | 21%          | 11%          |
| <b>Margins &amp; profitability</b> |             |              |              |             |              |              |
| EBITDA margin                      | 31%         | 51%          | 50%          | 45%         | 42%          | 39%          |
| Net margin                         | 32%         | 57%          | 53%          | 47%         | 43%          | 41%          |
| RoAE                               | 21%         | 28%          | 22%          | 23%         | 20%          | 19%          |
| RoAA                               | 13%         | 21%          | 18%          | 18%         | 15%          | 14%          |
| <b>Leverage</b>                    |             |              |              |             |              |              |
| Net debt (cash)                    | (1,196,272) | (10,129,316) | (12,696,543) | (9,510,898) | (14,804,711) | (18,871,443) |
| Net debt to equity                 | -           | -            | -            | -           | -            | -            |
| <b>Valuation</b>                   |             |              |              |             |              |              |
| Number of ordinary shares ('000)   | 2,650,000   | 6,096,325    | 6,096,325    | 6,096,325   | 6,096,325    | 6,096,325    |
| EPS (USD)                          | 0.64        | 0.78         | 1.05         | 1.28        | 1.35         | 1.41         |
| BVPS (USD)                         | 3.04        | 4.19         | 5.24         | 6.16        | 7.05         | 8.00         |
| P/E (x)                            | 42.19       | 15.07        | 11.18        | 9.11        | 8.70         | 8.28         |
| P/BV (x)                           | 3.85        | 2.79         | 2.23         | 1.90        | 1.66         | 1.46         |
| EV/EBITDA (x)                      | 37.67       | 14.46        | 14.46        | 10.19       | 8.23         | 7.68         |

Source: Emaar Properties, SHUAA Capital

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