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RATING ACTION COMMENTARY

Fitch Affirms Emaar Properties PJSC's IDR at 'BBB-'; Outlook Stable

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Fitch Ratings - London - 04 Jul 2022: Fitch Ratings has affirmed Dubai-based real estate company Emaar Properties PJSC's (EP) Long-Term Issuer Default Rating (IDR) at 'BBB-' with a Stable Outlook.

EP operates a broad conglomerate structure, which generates a diverse revenue stream. About 50% of EBITDA is from recurring revenue-generating businesses led by high-quality shopping centres, helping to offset the inherent volatility of residential development property sales. EP typically develops and sells residential properties, but retains retail, leisure and other assets, which are leased or owned and operated. EP, one of the largest real estate companies in the GCC, benefits from a strong international brand name.

The group is benefiting from Dubai's economic recovery, spurred by high oil prices, increasing international business and tourism and the liberalisation of visa policies, which is attracting new residents. Consolidated revenue grew more than 50% in end-2021, while EBITDA more than doubled. Higher EBITDA has reduced group cash flow leverage to 2.3x (2020: 6.7x).

EP's growing international operations now account for 17% of group revenue, but it remains concentrated in Dubai. The real estate portfolio is significantly concentrated in Dubai Mall, which generates more than 80% of recurring revenue.

KEY RATING DRIVERS

Economic Recovery: GDP growth in 2021 exceeded 3% and is expected to surpass 6% in 2022, spurred by high oil prices and, following a successful Covid-19 vaccination programme, the early reopening of international tourism and business. The government has also initiated several economic reforms, including liberalising residency and visa rules. Dubai's population contracted by about 8% in 2020 as many expatriates (about 90% of the population) had to quickly leave Dubai after losing jobs. Skilled workers are now given more time to find new work before their residency permits expire.

In addition, investors can be eligible for long-term visas after investing above certain thresholds. Official statistics show population growth of almost 2% in 2021.

Strong Sales Growth: Consolidated revenue at end-2021 reached AED28 billion, more than 50% above that at end-2020 and 18% above pre-pandemic levels. EBITDA reached AED8 billion (2020: AED3.3 billion). Residential property sales in UAE were especially strong, resulting in Emaar Development generating a reported revenue of AED15.6 billion (2020: AED9.8, 2019: AED12.7 billion), and property sales more than tripling to AED27 billion (2020: AED6.3 billion).

EMM Recovery: EP, through wholly owned subsidiary Emaar Malls Management LLC (EMM), owns and operates a portfolio of 37 prime retail assets with a gross leasable area (GLA) of about 7 million square feet (sqf). The portfolio is concentrated in the 4.2 million sqf Dubai Mall (one of the largest malls globally), which generates more than 80% of rents. Following the cessation of Covid-19-related rent waivers by 1H21, revenue grew more than 40% at end-2021 to AED4.9 billion, which is 7% above pre-pandemic levels. EBITDA was AED2.6 billion (2020: AED1.4 billion).

Footfall, aided by tourism and consumer confidence, is expected to exceed 2019 levels by end-2022. Occupancy at 1Q22 was 93% (1Q21: 91%). The average lease length is a relatively short at 3.4 years, which allows EP to increase new rents in the current growing market, but also exposes the company in a downturn. In February 2022, EP opened the 1.8 million sqm Dubai Hills Malls, which is expected to reach occupancy of more than 90% by end-2022.

International Development Reduces Concentration: EP is geographically concentrated in Dubai, where more than 80% of 2021 revenue was generated. EP operates in 10 countries through locally managed, largely self-funding subsidiaries that focus on residential property sales. In 2021, EP's international property sales reached AED6.2 billion (2020: AED4.6 billion).

Egypt generated more than 40% of international revenue. The growing international revenue is reducing geographic concentration, but dynamics in countries such as India, Pakistan, Turkey, Egypt and Saudi Arabia differ significantly, which may hinder EP's ability to replicate its business model abroad. Although intended to be self-funding, the international subsidiaries are not ring-fenced from the parent.

Residential Deliveries Funding Working Capital: Emaar Development's backlog at end-2021 was more than AED28 billion, which will be recognised over the next three-four years. The company is building about 25,000 units, 95% of which has been sold. Home buyers provide a deposit of 10% of the purchase price, and then pay instalments on a pre-agreed schedule.

Construction begins once deposits of 25%-30% of a project's the total sales value have been collected, which is used to fund construction costs. Final payments are collected on handover. Under local regulations, all funds must be kept in an escrow account dedicated to each project. Cash is then released to pay building costs and, once a project is complete, remaining cash can be released to Emaar Development as profits.

Land Bank: EP's land bank contains 331 million sqf in the UAE as well as 1.3 billion sqf abroad (mainly in Saudi Arabia for the King Abdullah Economic City project, scheduled to be completed in 2046). Historically, the government, the company's largest shareholder, granted land to EP, but these plots have already been developed. The company now sources land through joint venture partners, which enables EP to acquire land with minimal, if any, upfront cash.

Fitch's Analytical Approach: EP operates a central treasury policy with no ring-fencing in the group structure. We, therefore, rate the company on a consolidated basis. Given EP's range of business activities, Fitch's analytical approach redistributes group debt relative to the primary divisions' EBITDA at levels consistent with an investment grade for their business activities. The remaining group debt is then added to EMM, which generates recurring rents that can support higher levels of debt than development or hospitality companies.

Conservative Financial Position: FFO gross leverage is expected to average about 3.0x by end-2022-2023, a significant improvement from 6x in 2020. Similarly, interest coverage improved to 10.4x at end-2021, but is expected to remain at about 8x for the forecast period. Under the debt allocation approach, EMM's net debt/EBITDA is forecast to be 7.7x at end-2022(2021: 6x) and expected to remain below 7x going forward supported by strong malls EBITDA generation

DERIVATION SUMMARY

EP is a conglomerate structure, akin to Dubai-based Majid Al Futtaim Holding LLC (MAF; BBB/Stable), which has two primary companies that generate nearly all cash flow. Majid Al Futtaim Properties (MAFP), which owns and operates a portfolio of 29 shopping centres and 13 hotels, generates more than 60% of group EBITDA, while Majid Al Futtaim Retail (MAFR) operates 423 Carrefour franchises in 17 countries and generates about 40% of EBITDA.

Both companies generate stable recurring revenue from a portfolio of shopping mall and hotels. Like EP, MAF's shopping malls are mainly high-quality assets in prime locations. Both companies have single-asset concentration - EP owns Dubai Mall, which generates about 85% of recurring EBITDA, while MAF owns and operates the 2.6-million-sqf Mall of the Emirates, which generates more than half of MAF's EBITDA.

EP's focus on home development sets it apart from MAF. EP, through Emaar Development, mainly develops high-end master plan communities, typically selling the residential assets and retaining other assets to lease or to own and operate. Assets sales generate about 50% of group EBITDA. Homebuilding is inherently volatile and capital-intensive. With about two-thirds of EBITDA generated by recurring rents, MAF's cash flow is generally less volatile than EP's.

EP's position as a master-builder locally and regionally, and in conglomerate structure, means it operates a different business model than peer homebuilders, such as UK-based Miller Homes Group Holdings plc (BB-/Stable; withdrawn in April 2022), Spain-based Neinor Homes, S.A. (BB-/Stable) and London-focused Berkeley Group Holdings plc (BBB-/Stable).

KEY ASSUMPTIONS

Fitch's Key Assumptions Within Our Rating Case for the Issuer

- Revenue rebounds in 2023 following slight decrease in 2022

- EBITDA margin 28% for 2022-2026

- Low capex intensity ratio at 8% over the forecast period

- Dividend pay-out ratio similar to pre-pandemic levels at 85% of share capital

- High average occupancy ratio at 95% for EMM

RATING SENSITIVITIES

Factors that could, individually or collectively, lead to positive rating action/upgrade:

-Overall improvement in domestic property real estate, lowering the oversupply of units and reducing EP's business risk.

-With the current mix of group activities, consolidated EBITDA gross leverage consistently below 3.5x.

-Decrease in existing asset concentration contributions to group EBITDA.

Factors that could, individually or collectively, lead to negative rating action/downgrade:

-Under Fitch's analytical approach, the group's remaining gross debt/recurring rental income-derived EBITDA leverage increasing above 9.0x.

-With the current mix of group activities, consolidated EBITDA gross leverage increasing beyond 4.5x

-Liquidity Score below 1x.

-Material deterioration in property market adversely affecting Emaar Development's working capital and business profile.

-Volatility in international property development causing EP to increase borrowings to finance international projects.

-Material decrease in occupancy rates at EMM leading to a material reduction in profits.

BEST/WORST CASE RATING SCENARIO

International scale credit ratings of Non-Financial Corporate issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of four notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit https://www.fitchratings.com/site/re/10111579.

LIQUIDITY AND DEBT STRUCTURE

Ample Liquidity: EP had reported cash of AED8.6 billion at end-2021, including AED5.9 billion in escrow accounts, which are subject to RERA regulations and which hold advances received from customers against property sales and unclaimed dividends. We have restricted this cash, along with AED126 million under lien. Restricted cash will be released to EP from escrow accounts as projects reach completion. The company had about AED9 billion available under committed revolver facilities (RCF) with a limit of AED12.8 billion. One RCF, a USD1 billion facility, matures in December 2022.

The company has a smooth debt maturity profile, although there is close to AED4.5 billion due in 2022, mainly short-to-medium term working capital facilities that are typically rolled over. Short-term debt and undrawn facilities comfortably cover short-term debt. Despite significant working capital outflows from development, and planned capital expenditures and dividends push, liquidity coverage is expected to remain above 3.0x on average.

Debt is mainly senior unsecured, apart from a small amount of low-cost secured debt over five hotels to Emirates NBD Bank PJSC in the ROVE joint venture (with Dubai Holding), which is largely a legacy debt.

ISSUER PROFILE

EP is a Dubai-based real estate company operating principally through two entities: the parent EP and the subsidiary Emaar Development, a build-to-sell property business in UAE. After delisting Emaar Malls PJSC in November 2021, the lease-based retail assets now sit with 100%-owned EP subsidiary EMM.

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

ESG CONSIDERATIONS

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of '3'. This means ESG issues are credit neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg

RATING ACTIONS

ENTITY / DEBT ⬍	RATING ⬍	PRIOR ⬍

Emaar Properties PJSC	LT IDR	BBB- Rating Outlook Stable Affirmed	BBB- Rating Outlook Stable

VIEW ADDITIONAL RATING DETAILS

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APPLICABLE CRITERIA

Corporate Rating Criteria (pub. 15 Oct 2021) (including rating assumption sensitivity)

Sector Navigators - Addendum to the Corporate Rating Criteria (pub. 15 Oct 2021)

APPLICABLE MODELS

Numbers in parentheses accompanying applicable model(s) contain hyperlinks to criteria providing description of model(s).

Corporate Monitoring & Forecasting Model (COMFORT Model), v8.0.3 (1)

ADDITIONAL DISCLOSURES

Dodd-Frank Rating Information Disclosure Form

Solicitation Status

Endorsement Policy

ENDORSEMENT STATUS

Emaar Properties PJSC	UK Issued, EU Endorsed

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