

STRICTLY CONFIDENTIAL



## The Curious Case of Payment Plans

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# Executive Summary

- In response to a plethora of exogenous (dollar strength, oil price declines, etc.) as well as endogenous (numerous real estate launches, doubling of transaction fees, Central Bank caps on mortgage etc.) factors, prices and transactional activity has fallen across the freehold markets. In response, Developers in Dubai have offered a variety of incentives to galvanize sales in the form of payment plans that have often stretched to well beyond completion. In a paradigm shift, the number of projects that have offered payment plans skewed towards completion and after has been an astonishing 55% of the overall off plan launches by 2Q 2015, up from 29% just two years earlier.
- Whilst both GREs and PSDs have both moved towards a regime of skewering payment plans towards completion, it has been the latter that has predominantly shifted the payment plan profile; more than 70% of PSDs had started to offer this scheme to investors.
- Whilst primary sales data remains unavailable, secondary off plan market activity indicates that thus far there has been little impact in reversing price declines, and that the purpose of the payment plan (either to entice speculative investors by offering developer leverage or galvanize end user unit sales) has not achieved in offsetting the impact of macro factors such as USD strength and/or Central Bank curbs.
- Deferred payment plans are likely to continue to proliferate in an environment of low interest rates and as long as Central Bank curbs remain; however in the event of a rising interest rate regime, we opine that "developer leverage" will likely translate into the form of lower price offers in the primary market as well as an elongated timeline of supply

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# Macro Shifts and Concerns



“The future will be determined in part by happenings that it is impossible to foresee; it will also be influenced by trends that are now existent and observable” - Emily Greene Balch

# There have been a number of concerns on the horizon lately...

## Exogenous



The strengthening of the US dollar in the last 52 weeks (*Dollar index is up 21%*) has made Dubai real estate that much more expensive for international investors, acting as a deterrent.



Oil prices from its peak to now has fallen a steep 42%, dampening sentiment within the region, and leading to concerns of a slowdown in spending and a contraction in monetary liquidity.



Greek turmoil has added to levels of concern in global sentiments as investors move towards risk aversion



After a prolonged period of near zero interest rates, the Federal Reserve is poised to increase rates this year, sparking concerns of a slowdown in global economic activity as cost of leverage rises.

## Endogenous



The rush of developers trying to capitalize on the 2013 real estate boom of Dubai, has led to a flurry of new launches. New supply entering the market has created fears of a mismatch of the supply/demand dynamics, causing prices to fall further



An analysis of the inflation rate shows that in 2014 Dubai is hovering above a 4%, compared to 2012 where it had a negative rate of 1.71%.



In late 2013 the Central Bank introduced a mortgage cap in order to stop a pre-run of 2008. It set the LTV to 75%, with a limit of multiples of annual salary eligible for a home loan. This has restricted the buying power of end-users, causing home-ownership to become more difficult.



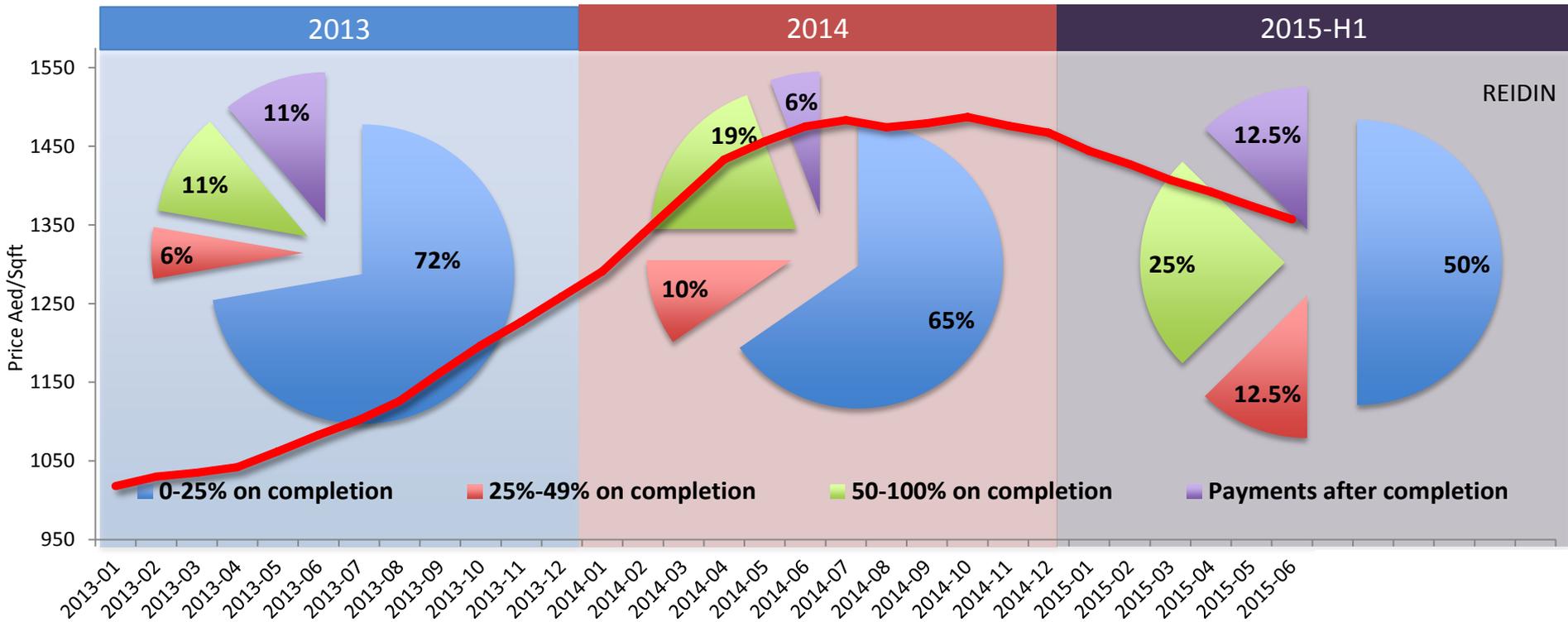
In October 2013, the Dubai Government doubled transaction fees from 2% to 4%, in order to curb speculation and slow down asset price acceleration

# The Evolution of Payment Plans



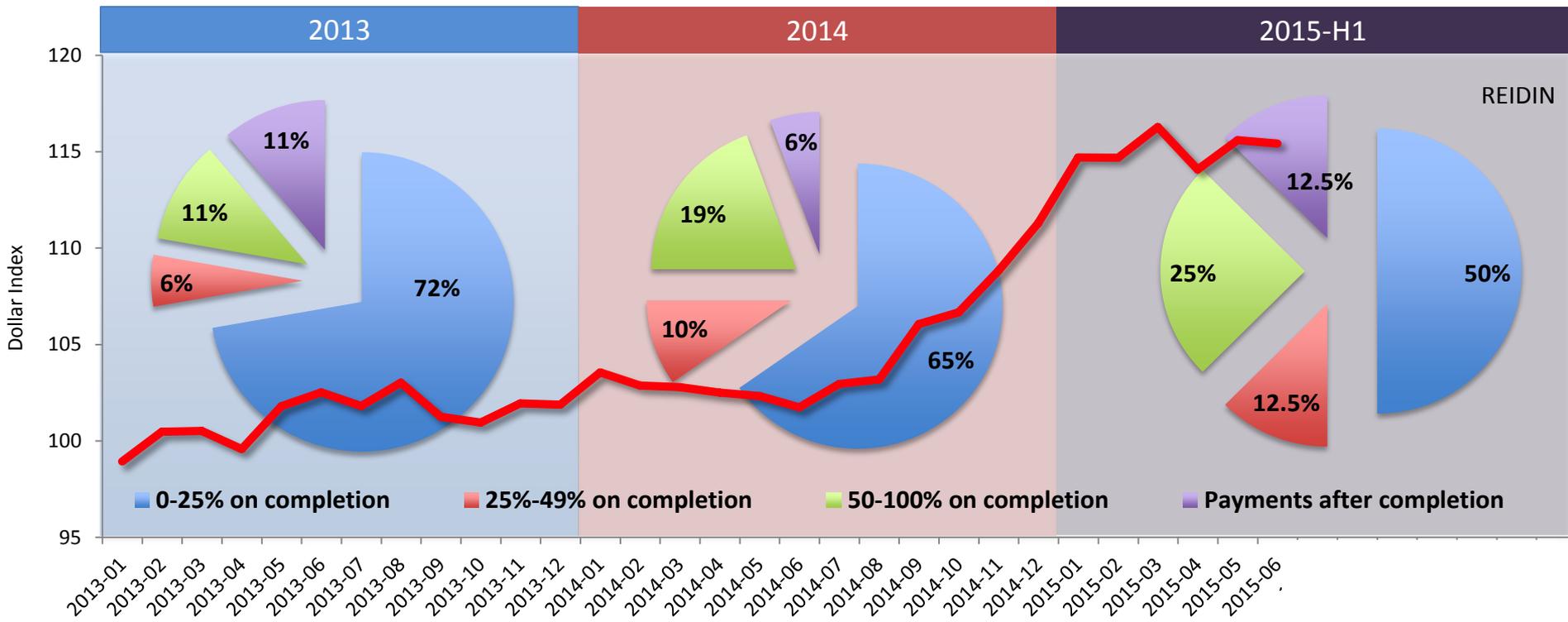
“Intelligence is the ability to adapt to change” - Stephen Hawking

# Paradigm Shift: Payment Plans Versus Price Action



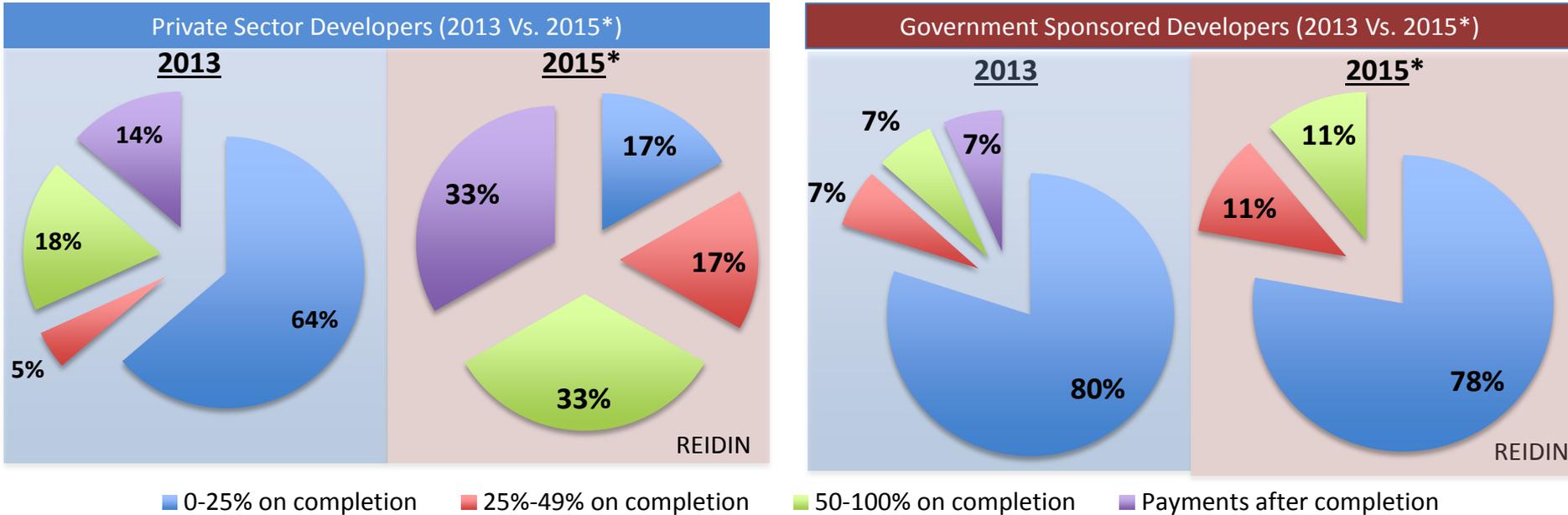
The above chart clearly depicts the evolution of payment plans; during times of exuberance in 2013 and the first half of 2014, payment plans were conventional in nature; 7 in 10 launches had payment installments of 25% or less on completion. However, as prices started to fall, developers started to incentivize buyers in an attempt to galvanize sales. By mid 2015, 50 % of launches had “back ended” payment plans; mirroring the decline in city wide prices.

# USD strength appears to be the predominant factor for the change..



When the evolution of payment plans is compared with the Dollar index, an even clearer pattern emerges; the single largest contributor to the softening of prices and therefore the easement of payment plans has been the strength of the US dollar against all currencies. The response of developers to lure overseas buyers has been in direct response to this trend (been observed for the first time since the launch of freehold in 2002).

# Private Sector more willing to offer developer finance



A developer-wise analysis of payment plans, shows the degree of flexibility has been significantly higher in private sector compared to government sponsored projects, with Government sponsored developers not following suit thus far. This has typically been because the latter have managed to move inventory even as prices have moved lower. However, as the incidence of negative premiums in the secondary market proliferate, we opine that GSDs will start offering increasingly flexible payment plans as well, mirroring their counterparts in the private sector.

# The Economics of Developer Leverage



“When you combine ignorance and leverage, you get some pretty interesting results” – Warren Buffet

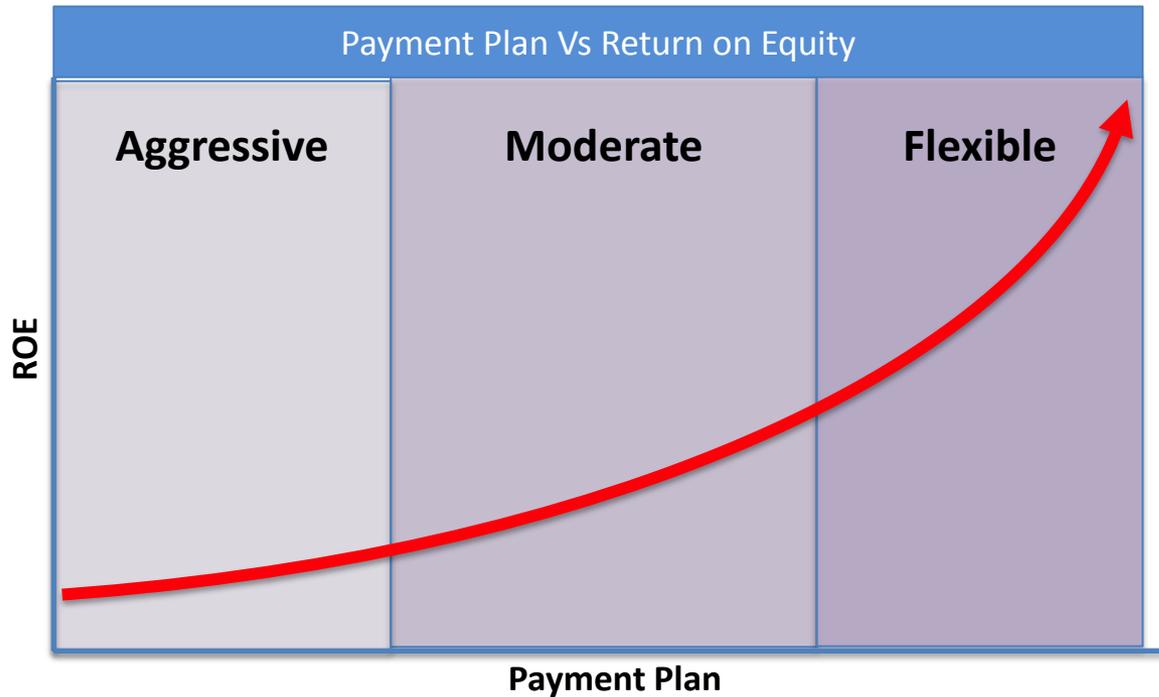
# The Economics of Developer Leverage for Investors

Buy a Ready Unit	
Buying Amount	1,000,000
Payment	100%
Fees Paid	6%
Gross Buying Price	1,060,000
Outflow	1,060,000
Sell the Unit	
Market Rises	15%
Profit	90,000
<b>ROI</b>	<b>8%</b>
<b>Rent (Per Annum)</b>	<b>7%</b>

Buy an Off-Plan Unit	
Buying Amount	1,000,000
Payment	20%
Fees Paid	6%
Gross Buying Price	1,060,000
Outflow	260,000
Sell the Unit	
Market Rises	15%
Profit	150,000
<b>ROI</b>	<b>58%</b>
<b>Rent (Per Annum)</b>	<b>0%</b>

A relative analysis between purchasing off plan and ready units reveals that off-plan yields higher returns if executed within the necessary parameters. Although, off-plan can yield almost 5 times the returns to that off-ready with less capital, they have their own set of risks.

# Payment Plans and ROE for Investors



There is a direct correlation between the flexibility of the payment plan and the return on investment. The higher the degree of the flexibility translates into higher ROI as depicted by the above chart. A detailed example of the ROI's for different payment plans can be seen in Appendix A.

# Conclusions

*The negative impact of exogenous and endogenous factors on the Dubai real estate market has led developers to change the flexibility of payment terms*

*A developer-wise analysis of payment plans, shows the degree of flexibility has been significantly higher in private sector compared to government sponsored projects.*

## Macro Shifts and Concerns

A plethora of exogenous (dollar strengthening, oil prices falling, etc.) and endogenous factors (doubling of transaction fees, mortgage fees, etc.) have translated into a fall of transactional activity in the real estate market, consequently leading to a city-wide fall in prices

This circumstance has led to developers to ease payment terms for off-plan properties in order to entice investors and end-users.

## Economics of Developer Leverage

In the last year, investment activity has gravitated towards the primary end of the market; this has been due to a number of factors, namely being the reduced prices on offer relative to the secondary market and the implicit developer leverage that increases return for investors and encourages “flipping”.

However, reduced activity in the secondary market has reduced the pay off for such investors and in many cases has also acted as a double edged sword, in the form of higher possibility of losses

## Evolution of Off-plan Payment Plans

An analysis of the evolution of off-plan payment plans reveals that the price trend has a direct impact on the degree of flexibility offered by developers.

As prices began to rise in 2013, developers offered aggressive payment plans to buyers. However, as prices began to dip towards the end of 2014, payment terms begin to get skewed towards the end of completion.

A developer-wise analysis shows the degree of flexibility is higher in private sector developers

## Conclusion

USD Strength appears to have been the predominant reason in a long list for the markets slowing down and has led to developers to offer payment plans.

We opine that these payment plans will continue to proliferate as developers continue to their attempts to galvanize sales, and that GREs which have thus far largely resisted the move, will increasingly resort to similar plans should the price lull continue.

# Appendix A: ROI for different Degrees of Payment Plans

Premium 15%

Aggressive	Registration	15-Sep-15	15-Jan-16	15-Jun-16	15-Jul-17	15-Dec-17	15-Jun-18	Completion
Payment Plan	20%	10%	10%	10%	10%	10%	10%	20%
ROI		42%	33%	27%	23%	20%	17%	14%

Moderate	Registration	15-Sep-15	15-Jan-16	15-Jun-16	15-Jul-17	15-Dec-17	15-Jun-18	Completion
Payment Plan	20%	0%	0%	0%	0%	0%	0%	80%
ROI		58%	58%	58%	58%	58%	58%	14%

Flexible	Registration	15-Sep-15	15-Jan-16	15-Jun-16	15-Jul-17	15-Dec-17	15-Jun-18	Completion	3 years After Hand Over
Payment Plan	5%	5%	5%	5%	5%	5%	5%	5%	60%
ROI		94%	71%	58%	48%	42%	37%	33%	30%-14%



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## Research Database

Title	Report	Date
Dubai: The Signal and the Noise	REIDIN - UNITAS Real Estate Market Reports	5-Jul-15
Killing Them Softly: The incidence and impact of Off-Plan	REIDIN - UNITAS Real Estate Market Reports	15-Jun-15
Dubai: The Ramadan Phenomena	REIDIN - UNITAS Real Estate Market Reports	2-Jun-15
Dubai: Sell in May and Go Away	REIDIN - UNITAS Real Estate Market Reports	11-May-15
Dubai: The Metro Effect	REIDIN - UNITAS Real Estate Market Reports	28-Apr-15
Renter's Ball: The Dynamics of the Tenancy Market in Dubai	REIDIN - UNITAS Real Estate Market Reports	14-Apr-15
Dubai: The Path of Symbiosis	REIDIN - UNITAS Real Estate Market Reports	22-Mar-15
Dubai: Boom-Bust-ology	REIDIN - UNITAS Real Estate Market Reports	8-Mar-15
Dubai: Is Commercial Realty Commercially Viable?	REIDIN - UNITAS Real Estate Market Reports	2-Feb-15
Dubai: Shocks, Shifts & a Return to First Principles	REIDIN - UNITAS Real Estate Market Reports	19-Dec-14
Dubai: The Hunt for Yields	REIDIN - UNITAS Real Estate Market Reports	15-Dec-14
Dubai: Amidst a Slowdown, Underlying Strength	REIDIN - UNITAS Real Estate Market Reports	15-Nov-14
Dubai: Where to build?	REIDIN - UNITAS Real Estate Market Reports	22-Oct-14
The Cityscape Effect	REIDIN - UNITAS Real Estate Market Reports	18-Sep-14
Dubai: The Real Estate Value Guide	REIDIN - UNITAS Real Estate Market Reports	3-Sep-14
Dubai: The "New Normal"	REIDIN - UNITAS Real Estate Market Reports	8-Aug-14
Dubai: The Paradox of Affordable Housing	REIDIN - UNITAS Real Estate Market Reports	21-Jul-14
Dubai: A Tale of Two Markets	REIDIN - UNITAS Real Estate Market Reports	17-Jun-14
Dubai: The Trophy Buying Phenomena	REIDIN - UNITAS Real Estate Market Reports	22-May-14

## Research Database

Title	Report	Date
Dubai: The Road Ahead	REIDIN - UNITAS Real Estate Market Reports	5-May-14
Dubai: Buy Land Where the City Ends	REIDIN - UNITAS Real Estate Market Reports	7-Apr-14
Dubai: A Closer Look into 2013	REIDIN - UNITAS Real Estate Market Reports	13-Feb-14
Dubai: What Now?	REIDIN - UNITAS Real Estate Market Reports	28-Nov-13
Dubai: If You Build It They Will Come	REIDIN - UNITAS Real Estate Market Reports	30-Sep-13
Dubai: The City is Built Upon it's Commerce	REIDIN - UNITAS Real Estate Market Reports	11-Apr-13
Home Ownership: Dubai's Road to Prosperity	REIDIN - UNITAS Real Estate Market Reports	12-Mar-13

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HH General Sheikh Mohammed Bin Rashid Al Maktoum  
The Ruler of Dubai and Prime Minister of UAE



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