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Tuesday 15 June 2010

## Session 2 - Investing in Real Estate Development

The panel was moderated by **Richard Banks (RB)**, Director, Middle East, Euromoney Conferences, with panelists: **Hesham Shoukri (HS)**, Chairman & Managing Director, Rooya; **Hazem Ashry (HA)**, General Manager, Emaar Misr; **Khaled Sedky (KS)**, Chief Portfolio Officer, Palm Hills Developments Co.; **Mohamed Abdalla (MA)**, President, Coldwell Banker Egypt; **Ahmed Demerdash Badrawi (ADB)**, Chief Business Development Officer, SODIC; **Chris Jolly (CJ)**, CEO, Cadena.

Below are excerpts from the session.

This panel will look at the supply and demand for financing in the wholesale sector. The particular focus will be on developer finance and how the financial markets might change the way they approach the development of real estate projects across all market segments. We will consider the impact of regulatory changes, the availability of bank capital, why institutional investment capital is reluctant to enter the market in a meaningful way. We will hear from the financiers about their concerns about lending to real estate and their plans for risk management in the like of the global real estate crash. And we will hear how real estate developers are raising the funding for their projects: bank lending; capital markets; off plan financing.

**RB:** Ahmed, SODIC is a big company, it's publicly listed, how have you gotten a funding base for your developments? What's the difference between development and investment?

(Order as seated on panel: HA, HS, KS, MA, ADB, CJ)

**ADB:** Investment is quite a new concept in Egypt. It's only in the last 5-7yrs that the market has become more sophisticated, where companies rely on something other than off-plan sales. Since then, bigger companies have come in with access to capital markets and more diverse portfolios. These new options allow us to bring a new view into market and create longer term projects. We have more options now as developers and investors; we can do mixed-use space, offices and shopping malls on top of residential and hold onto it as whole and lease the commercial space or sell it off in packages or sell completely and move on.

**RB:** Again, let's focus on answering; what is the difference between an investor and a developer?

**HA:** Developers use hard hats and we dirty our boots, we focus on lifestyle and the people. We aren't looking so much at the numbers and yields.

**RB:** Emaar is an investor and developer, right?

**HA:** Yes, but we look to developing communities and maintain ownership of those assets.

**RB:** You're a developer, and an architect, if there was an institution that was investment based, at what stage would they come to you and why would they come?

**HS:** First, the difference between developers and investors in my opinion is that development is the know-how and investment is the financing. Developers have more ideas than money and investors have more money than ideas. If a developer is alone, as it is in Egypt now, you cannot take big steps. We would see large growth if the two existed together. But we can only use sales to generate funds and so this needs to be solved.

**RB:** Khaled, are you looking at using your own debt and equity with Palm Hills?

**KS:** Yes, we have one of the lowest debt-to-equity ratios in the sector.

**RB:** Do you see benefits of bringing in retail space? Or would you rather just look at the balance sheet?

**KS:** I see massive investment and movement from trends in the UAE for office and commercial space. So, there are great benefits in developing for-lease space. The problem is obtaining the initial investment to carry such projects through the initial stages.

**RB:** Chris, as a foreign investor, what are the first things you look for in opportunities abroad? How do you judge the reality of an opportunity?

**CJ:** You have to be comfortable with the investment through the people, the level of classes, and number of young people in the population. You need to see stability through things in the economy remaining in growth also a bubble that, in Egypt, is rightly under leveraged.

It needs to be clear that the number of commercial registrations is currently low and that you'll be bringing a large investment into the market. The way things are priced here hasn't gotten to the point where it's that reflective of the market. A constraint in Egypt is liquidity and funding and once investment comes in, then you'll get more money and liquidity and the whole segment gains momentum, but it's still early for Egypt.

**RB:** As for asset class, what does it provide the end investor? What motivates them to choose real estate as opposed to other areas?

**CJ:** Stability against inflation and continued growth.

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**RB:** SODIC is a publicly traded company, people have access to shares; When you talk to investors, do they express interest or just want the security of a publicly traded company?

**ADB:** There are some, the ones who want capital appreciation look to real estate; a lot want a ready-made product. There is risk and their appetite is finite and they would rather come in towards the last few years, so as to see their investment realize. Until now, there hasn't been the portfolio for them to come into the market (investors).

**RB:** Are you seeing the beginning of change in the way people are seeing real estate as asset class?

**MA:** The idea of assets as real estate has been at the core in Egypt forever. Even when Egyptians go abroad, they put their money into real estate. Now, it has changed. It is more sophisticated, the way of thinking and the market has changed in the past 5-7 years. The ideology has always been there though.

**RB:** Do you see institutional clients who are starting to look at Egypt?

**MA:** We have seen foreign funds before the crisis and now they are starting to come back. Some are just watching. The vehicles for foreign investment are not here. Foreign investment has to be through real estate or development companies, but this is too big of a risk for the investors.

**RB:** Int'l investors aren't the only solution, there's a need for domestic investors as well. Are there really no domestic investors?

**HA:** There is a huge gap between complete and incomplete assets, things aren't finished. The gap needs to be funded by domestic investment first. Foreigners want ready-made assets and until things are completed, it is difficult for developers to pay the bills without them.

**HS:** Problem is we don't know how to market ourselves (Egypt). An example is that, in Egypt, no one knows the ratio of class A offices but abroad and in other developing countries there are numbers and not the kind of shortage we have. It's about .04sq meters/person in Egypt. There is a huge demand for office space and people abroad aren't aware. We have to market this so investors are interested in funding.

## Q&A

**Q:** If you are a foreign fund, you are not allowed to own local property without owning a local company in order to ensure you are paying taxes. If you want to come in and invest, there is no tangible ownership because the title is only for 7 years. Do we have the environment for foreigners to lease, like China? Most people think they can't afford to spend 3 years waiting for returns on investments.

**CJ:** Taxes are a problem but we have to provide post tax income numbers to our investors and it depends on what amount you are willing to put in. Nothing can be done until some of the regulations are relaxed and the market becomes friendlier for foreign investors.

**Q:** The domestic market should be getting bank financing. What is the difference between commercial and real estate financing? People are more trusting with real estate and it still comes down to personal financing. Commercially, for example, Smart Village was built and sold one at a time. Institutions will want to see something finished before funding. We will have to see two markets converge, local and international. The supply will come and the market will have to step up.

**KS:** I agree. There is a market where pioneers need to go in and start to show how investors and developers can work hand in hand in different types of projects.

**HS:** The investors don't want the risk, they want to see something first and then come to invest, but this will shrink the market. We all need to collaborate on the risk or the market will slow. We have huge demand on real estate and are far behind on office space.

**Q:** What about using specialized funds? This has been recently seen in infrastructure, as joint ventures, what about these? Use un-used liquidity, which is stagnant, from retail savings and use it for commercial space.

**CJ:** Typically in mature markets, developers take risk in other, outside markets because they know they have an outlet and process, and institutions to buy assets, etc. If they know they are producing high quality, then they will take that risk. Domestic investors need to start the trend and then institutional investors and foreign investors will be more willing to take the risk. If they see domestic institutional investors aren't taking risk, why would they want to?

**Q:** If you're investing, you want to have an exit route. How are you going to overcome the issue of poor quality, which is stopping investors?

**HA:** Quality codes must be committed to actual quality. We only develop quality and invest here because we know the future of Egypt is in the hands of foreign investments and they need to meet the standards. We always use international codes and standards.

**KS:** I think it takes two to tango. We need both developers to work on that and also provide training to improve workmanship. We are doing CSR initiatives to do this on all levels of our work.

**HS:** If we see foreigners investing in something, they'll bring high the quality. We have to have foreign investment and then the quality will improve.

**Q:** Foreign contractors should be looked at as a solution. In regards to the marketing issue, maybe part of the problem is that we don't have credible market research in Egypt. Figures are skewed from one company to another. We need to create a credible research standard.

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**HS:** I agree on the poor data point. We need to market with true data. As for the foreign contractors, I have no experience. There are some companies searching for opportunities from abroad. They are trying to come to emerging markets, where there is more work. They have higher prices than local ones, so that is the problem.

**HA:** Developers have to market real estate opportunities abroad. We are a great market and need to show it all together. The companies alone cannot do it, the government needs to help and show people the statistics that make Egypt so lucrative.

**Q:** We are focused on A&B commercial space sectors, but there is huge potential for B&C sectors. We need to work on research and learning from best practices abroad for quality but affordable units for this segment.

**Q:** Why don't we collaborate together and be one umbrella for marketing Egypt as investment destination?

**HA:** Banks need to bridge and fuel this sector; they need to relax conditions such as capital on the real estate market, so the fuel can flow into the investment sector. No one in Egypt has lost money recently in the real estate market; this needs to be utilized. The issue is: relax regulations; there must be trust in the industry. We have outperformed, the proof is there.

**HS:** The banks won't change. The important thing is that the outside world sees the numbers.

**KS:** Developers and investors should orchestrate value chain to attract foreigners. It will take a couple of brave people with deep pockets to pave the way, just like in the retail market; they are now making a lot of money.

**MA:** We have to look first internationally. The residential developing is no problem other than mortgaging; now it's the commercial space's time. The domestic market can try to improve the current climate and when we have a good story, the investors will come. Fix domestic problems first.

**CJ:** I see an engine that's not running on all cylinders. Banks need to operate more loosely, not too much but some. They need to bring in ideas about types of debt banks could supply. Whatever the reasons are that domestic investors have not already invested here, they need to be worked out in order to convince international investors.