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Emirates Bank

EIS Asset Management

# EMIRATES REAL ESTATE FUND – COMMENTARY AND MARKET OUTLOOK

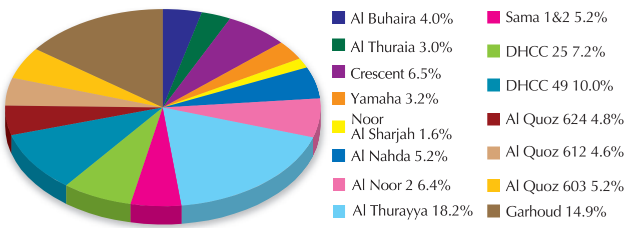
## Background

The Emirates Real Estate Fund is a Jersey-registered open-ended investment fund that seeks to deliver long term returns to investors through investment in direct, physical properties in the UAE and MENA region. The fund has delivered robust and impressive returns since inception in June 2005 as its focus on completed property and undervalued, workable assets has led to consistent revaluations on its portfolio. This performance has been achieved despite a number of market headwinds: the MENA stock crash of 2005/6, rent caps in the UAE and the more recent, and all-encompassing, sub-prime debacle which is a global issue. In this document, we seek to contextualize the strong performance of the fund in 2008 and provide greater levels of insight into current portfolio strategy against the backdrop of a maturing market.

### Portfolio analysis

As at 31st October Emirates Real Estate Fund has more than $610m of assets under management, invested directly across 17 properties, and with an exceptionally low financing ratio of 6:94. The portfolio currently has circa 12.2% in cash pending further property acquisitions, and there is an active pipeline of further acquisitions under negotiation.

The current portfolio split by property value is as follows:




### Portfolio outlook

Our investment philosophy, and consequently choice of properties exhibits the following characteristics;

- completed / close to completion assets
- high occupancy levels
- sound due diligence on the tenants as well as detailed legally binding lease contracts to ensure good covenant strength
- commercially sound tenants who are committed to the region e.g we have names like Boehringer, Sirona Dental, Royal College of Surgeons of Ireland, Costa Coffee and Dnata contracted for significant periods of time at attractive rental rates. Additionally, in our property with TECOM Media Free Zone, our tenant list is commendable with such names as Etisalat, Dubai Press Club, International Cricket Council, MEED and Huawei.
- regular review of the portfolio with a view to disposing any older and management-intensive assets from the portfolio, while being mindful that any disposal is linked as closely as possible with a corresponding re-investment of the sales proceeds to avoid any undue cash drag to performance.
- high standards of maintenance with active property and tenant relationship management. Whilst this may create some additional short-term expenditure, we are already finding that the high levels of tenant satisfaction are ensuring that rents are being paid on time and many tenants are already waitlisted for additional space within our properties. We anticipate implementing these higher standards in some of our older properties, particularly Crescent Tower in Sharjah – a prime office building on the Sharjah Corniche – and effecting key asset management strategies across the entire portfolio in order to drive out additional income and resulting valuation growth for investors.

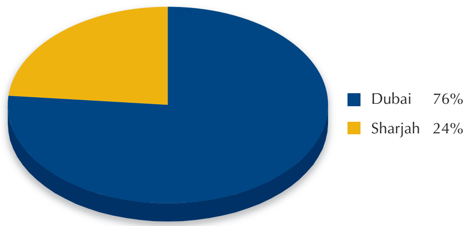
The above steps ensure that the portfolio is positioned to yield attractive and secure income streams. The income streams of the portfolio, after all fees, provide a running yield in excess of 7% per annum, now 600 basis points above the US Fed Funds rate. Where possible, we have been endeavouring to lock in our income streams at key commercial assets offering tenants leases up to 5 years.

## Monthly Performance

| | Jan | Feb | Mar | Apr | May | Jun | Jul | Aug | Sep | Oct | Nov | Dec |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **2005** | – | – | – | – | – | – | 1.00% | 0.99% | 0.98% | 1.17% | 1.25% | 1.33% |
| **2006** | 2.25% | 2.01% | 2.15% | 1.58% | 1.21% | 1.20% | 0.76% | 1.42% | 1.07% | 1.72% | 2.17% | 1.89% |
| **2007** | 0.62% | 0.54% | 0.53% | 0.99% | 0.90% | 0.89% | 0.81% | 0.88% | 1.31% | 0.79% | 0.78% | 1.20% |
| **2008** | 0.70% | 1.59% | 1.36% | 0.81% | 1.67% | 1.25% | 1.62% | 1.78% | 2.19% | 1.53% | – | – |

### Geographical allocation

Our geographic allocation is currently predominantly towards Dubai.




It is our intention to diversify the current geographical exposure by allocating new inflows towards other emirates as additional opportunities present themselves. In particular:

#### Sharjah

While we own a number of residential properties in Sharjah, we currently own only one commercial office property in Sharjah. We would thus like to increase our exposure further to commercial office space and also logistics / warehousing / light industrial. However, further acquisitions of office space in Sharjah are currently challenging, due to a severe lack of office properties, either completed or under development, but we are active in this arena should an opportunity arise.

#### Abu Dhabi

We have been actively trying to invest in Abu Dhabi for more than a year now, but the market remains tight in terms of completed or close to completion assets. Completed stock is traditionally still held via individuals who are not keen to sell and, where testing the market, fail to supply adequate information in order to complete even basic levels of due diligence. The broker market also remains wholly unsophisticated and with no regulation in place. That said, we are in the very early stages of discussion on a small residential / commercial asset. With tight supply in Abu Dhabi over at least the coming 3-4 years we are confident of the demand for rentals of both residential and commercial space and remain focused on being invested in Abu Dhabi soon.

It may be that to achieve our aim we will have to invoke the fund's ability to invest a portion of its assets in property under development and look to take exposure to assets still 1-2 years away from completion.

#### Dubai

In the short term, we may add further to our Dubai weighting, before being successful in the wider geographic allocation preferences noted above. However, we envisage that this will typically be in our quest to fulfil an allocation to low cost housing. As such we are closely monitoring such areas as Silicon Oasis, Discovery Gardens, International City and Motor City.

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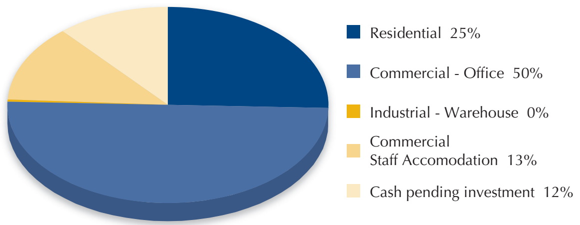
### Asset class allocation

In terms of asset class allocation our weightings are as follows:




### Commercial - Office

With continued delays to the delivery of other commercial assets in Dubai, we currently see little direct competition to most of our commercial assets in terms of rental rates, location and management standards - especially in terms of Al Thurayya TECOM Media City and Dubai Healthcare City 49 and 25.

In the Garhoud area the proximity of our premises to the metro station, the lack of completed assets in such a busy trading area and our active lease management and facilities maintenance will stand us apart from the competition.

TECOM remains an attractive business location and our property is a well known landmark within the zone, overlooking the grassy bowl where many entertainment activities are held. We benefit from a prestigious tenancy roll and are confident of continued opportunity to retain high occupancy rates and increase rental streams on this asset. As part of this process we are working closely with TECOM to encourage further rent reviews within the property over the coming year. Additionally the prospect of a couple of old tenants vacating to owner-occupied space in the coming year presents us with an opportunity to lease to new tenants at higher market rates.

With regards to our DHCC assets, we are widely known to have implemented high standards of management at our properties and benefit from a wait-list of existing tenants wishing to expand and new tenants seeking space. The DHCC area is fast becoming an important part of Dubai and, with the opening of the new City Hospital this month, the fast pace of construction of the Harvard Medical School, and the Dubai Metro line running through the heart of the DHCC zone, this area has considerable attributes.

In terms of Sharjah, the prominent position of Crescent Tower on the Corniche is second to none. As the property has been returned recently from an investment contract, there is an intensive property management and leasing renewal program in the early stages of implementation to raise standards of management at the premises and intensively manage the property on a true asset management basis.

### Commercial – Staff Accommodation

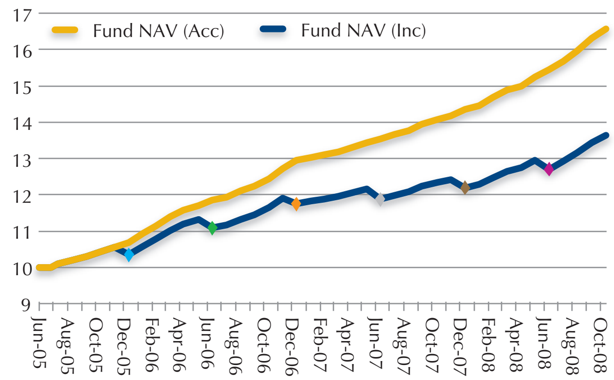
Our allocation to staff accommodation assets of some 13% includes 30 year leasehold investments in Al Quoz. The land lease commences from the start date of the Dubai Metro – 9/9/2009. These assets were purchased at yields in excess of 17%. Typically a single tenant / agent is responsible for each property and as such the fund benefits from a single cheque three to four times per annum for an accommodation of over 300 rooms apiece. While we need to be mindful of continuing to hold these assets long into the land lease term (for fear of reducing capital valuations) the underlying room rentals on these assets continue to increase at a steady pace. We are thus for now satisfied that these continue to be attractive assets to hold in the short to medium term.

### Residential

Our residential assets represent just 25% of the portfolio today and are largely focused in Sharjah, with two assets in Dubai. The majority of these properties are now undergoing review via our administration and leasing teams as many tenants are becoming due for renewal and thus due rent reviews. We anticipate as a result some upwards valuation improvements in a number of these assets.

It is our intention to add further to our residential component of the portfolio but our asset selection will likely be skewed towards medium to low cost accommodation as we believe there is still continued growth in this sector. We already have a number of corporate tenants that would like to rent whole buildings from us should we make appropriate vacant possession acquisitions. We find this an attractive proposition as we could lock in rentals for a number of years from high quality corporate and even quasi Government tenants. Our biggest challenge on residential currently is achieving meaningful rental yields, as despite high rental values most sellers are pricing this into sales prices leaving only 4-5% rental yield opportunities for any acquirer.

## Performance history




Income Share Class NAV after Dividend Distribution of

- $0.35 per share Dec 05
- $0.37 per share Jun 06
- $0.38 per share Dec 06
- $0.40 per share Jun 07
- $0.39 per share Dec 07
- $0.41 per share Jun 08

### Performance Data (based on accumulation shares)

| | |
|---|---|
| Current NAV (USD) Accumulation shares | 16.57 |
| Current NAV (USD) Income shares** | 13.65 |
| Current NAV (AED) shares | 10.72 |
| 1 Month performance (USD) | 1.53% |
| Performance since launch (USD) | 65.70% |
| Average Annualised (USD)* | 16.32% |

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## General market outlook

We are of course mindful of the wider global picture, as well as the current negative sentiment in local equity markets and, more directly, the speculative and off plan local real estate market.

We have long since commented that the front-running on pricing of the off plan / under construction market by such a huge margin to the completed / close to completion market was irrational. Measures should have been taken earlier by developers, or relevant authorities, to curb such wild speculation and tighten measures of ownership at an early stage ensuring true long term investors could participate at sensible pricing levels. In mature markets, completed / close to completion stock usually trades at a premium to off plan sales with long lead times. We believe there will be some pain in the short term for the off plan market as many speculators have to offload assets at a discount or fail to meet 2nd payments with assets simply being returned to developers. This is not however a market into which EREF invests. We remain hopeful that any negative sentiment driven from this short term pain does not spill over into the completed market.

While this repositioning of the speculative cycle will offer some short term pain, we believe the knock on effect will be that true investors and end users will take their place for the medium to long term (and also some speculators are already seen converting their own strategy to that of long term investor). The fundamentals for the UAE and the region as a whole remain strong, and particularly so for completed property stock. The current liquidity crisis and short term pain in the off plan market should also add further delays to delivery, reducing the volume and speed of future supply. This will in time provide added upward pricing pressure to those assets into which EREF invests – completed / close to completion assets.

One factor we should keep an eye to is the tightening credit crunch and the ability of the true investor and end-user to gain adequate mortgage financing. Loan to value ratios have tightened significantly due to tighter credit controls at banks and finance houses. If this continues, or even increases, this could choke even the true investor market. However, we are confident at this stage of measures currently being taken by the UAE Government to loosen liquidity in the region.

## Future prospects for EREF

In summary, we remain active acquirers of completed / close to completion assets and hope to add another 2-3 assets to the portfolio before year end. We continue to be cautious of the assets in which we invest and must be clear on their redeeming factors and potential contribution to performance over the short, medium and long-term prior to investing. We must also be able to complete adequate levels of due diligence prior to acquisition in order to minimize risk and surprises for ourselves and of course to investor returns.

In terms of the existing assets we continue to manage them actively to drive out further income generation, reduction of expenses and consequent improvements in value. We are also raising standards of property management and tenant relationship management to ensure that, when tenants do have a wider choice, through oncoming supply, we remain a landlord of choice. We may also be a little more cautious in terms of tenant selection in the coming months.

We remain confident in the Dubai, Sharjah, and Abu Dhabi real estate markets and believe most of the fundamentals currently remain intact - high GDP, growing businesses, continued population growth – and thus the demand for accommodation across most sectors remains high. We believe that the global picture and the tightening credit conditions could actually be positive for EREF in terms of less supply coming to the market within the previously targeted timeframes. As an investor and landlord of predominantly completed and ready to occupy assets, this should ensure that the demand for our properties remains high, and in turn positive for the outlook for EREF and resulting performance for investors.

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** Figures based on period 30th June 2005 to 31st October 2008. Performance stated on accumulation share class, annualised on a day count basis. Launch bid price held to 15th July 2005 at $10, prevailing bid thereafter. ** The following dividends for income shares were declared - $0.35 per share as at 31st December 2005, $0.375 as at 30th June 2006, $0.38 as at 29th December 2006, $0.40 as at 29th June 2007, $0.39 as at 31st December 2007, and $0.41 as at 30th June 2008". The published price for income shares is the ex-dividend price and share valuations are based on this ex-dividend price from 31st Dec 2005 onwards.*