Unitas Consultancy (A GLOBAL CAPITAL PARTNERS GROUP COMPANY) Q3 2016

Brexit: Much Ado About Nothing

REIDIN Real Estate Information

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GCP GLOBAL CAPITAL PARTNERS

Executive Summary

- UK's vote to leave the European Union sparked an extraordinary period of volatility and panic in global markets, causing the FTSE, S&P, and DFM to fall nearly 5%. After 'Brexit' was declared, some analyst began to compare it to the World Financial Crisis, saying the impact would be catastrophic to the world economy. However as fears receded, market recovered quickly, with the exception of the British sterling.

- British investors have been a significant percentage of buyers of Dubai freehold real estate assets, doubling their exposure from 2012 to 2015 (AED5B to AED10B). The recent fall of the sterling has caused for stress in the real estate markets, as people expect UK investors to evaporate due to the devaluation of the currency. However, a correlation analysis of investment flows against the currency movements over the last 5 years suggests a mildly positive relationship of 0.26, implying that whilst currency moves are a factor, there are a number of other variables that have overwhelmed the systematic depreciation of the GBP during this time frame

- A similar analysis was conducted with Indian Investments flows in the Dubai real estate market against the Indian rupee over the years. It had the same correlation of 0.26 to that of Britain, implying that currency fluctuation is not pivotal in the decision making process for overseas investments.

- The expansive fiscal policy the UAE has adopted is going to be the driving force of the economy. An analysis of bond market issuance within the UAE reveals that in 2016 H1 the private and public sectors had issued bonds of USD11.93 Billion, which is nearly 76% of the full year of 2015 and 72% of 2014. This aggressive strategy to raise funding is inline with the expansive fiscal policy adopted by the government. Dubai, in particular, has increased its budget spend in 2016 by 11%, whilst the rest of region cut back spending due to oil crisis.

- The impact of the 'Brexit' event will be played out over the next few years on a global stage that will continue to push markets in unexpected ways. However, the fear of a weakening currency and its impact on foreign real estate markets is likely exaggerated and in point of fact, there might well be a positive impact on markets such as Dubai as foreign flows continue to gather pace, especially in light of the ensuing uncertainty that has been created as a result of the referendum

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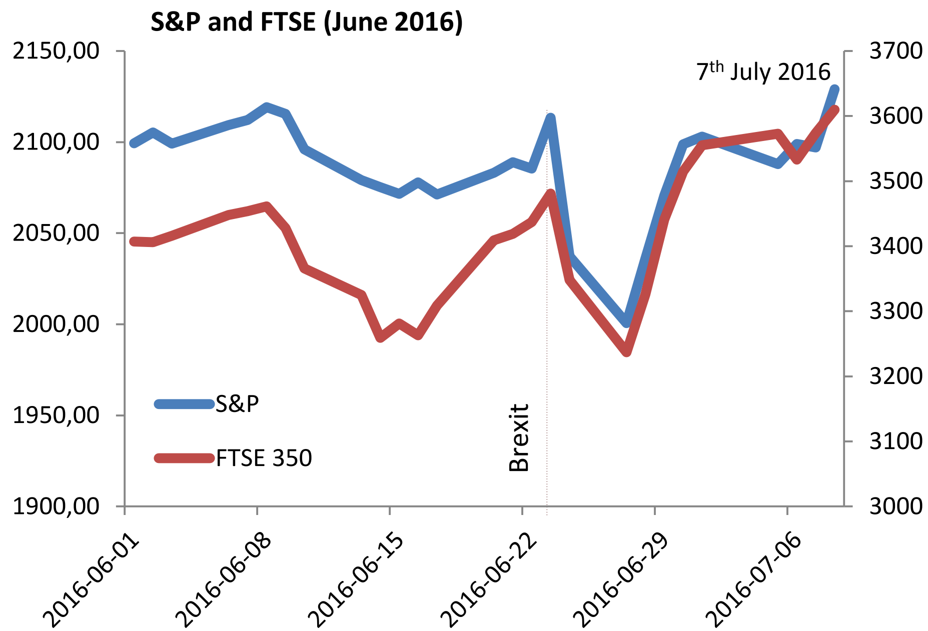
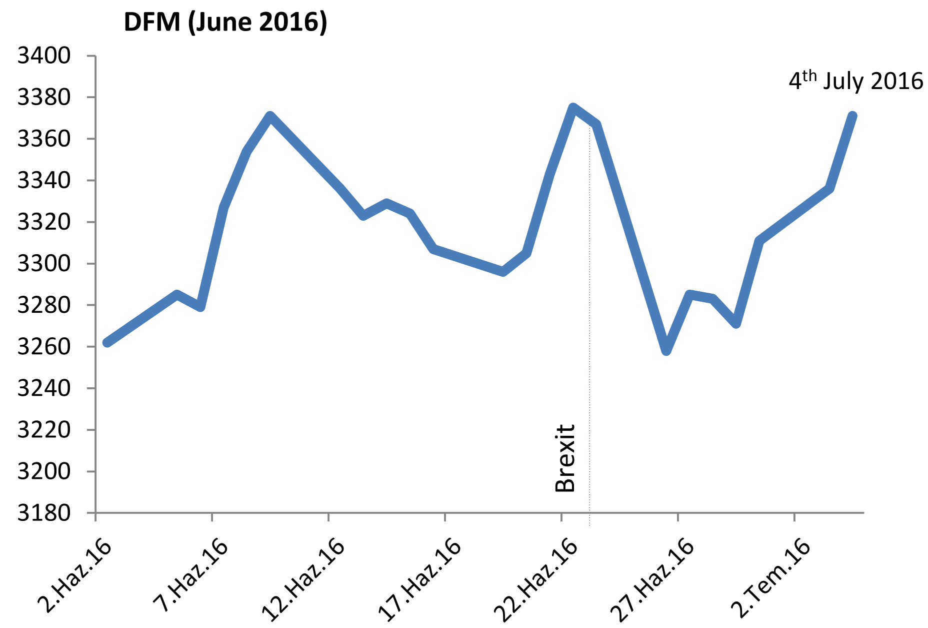
'It's not going to be an amicable divorce - it wasn't exactly a tight love affair anyway:' EU leaders

Market Tantrums on “Brexit”

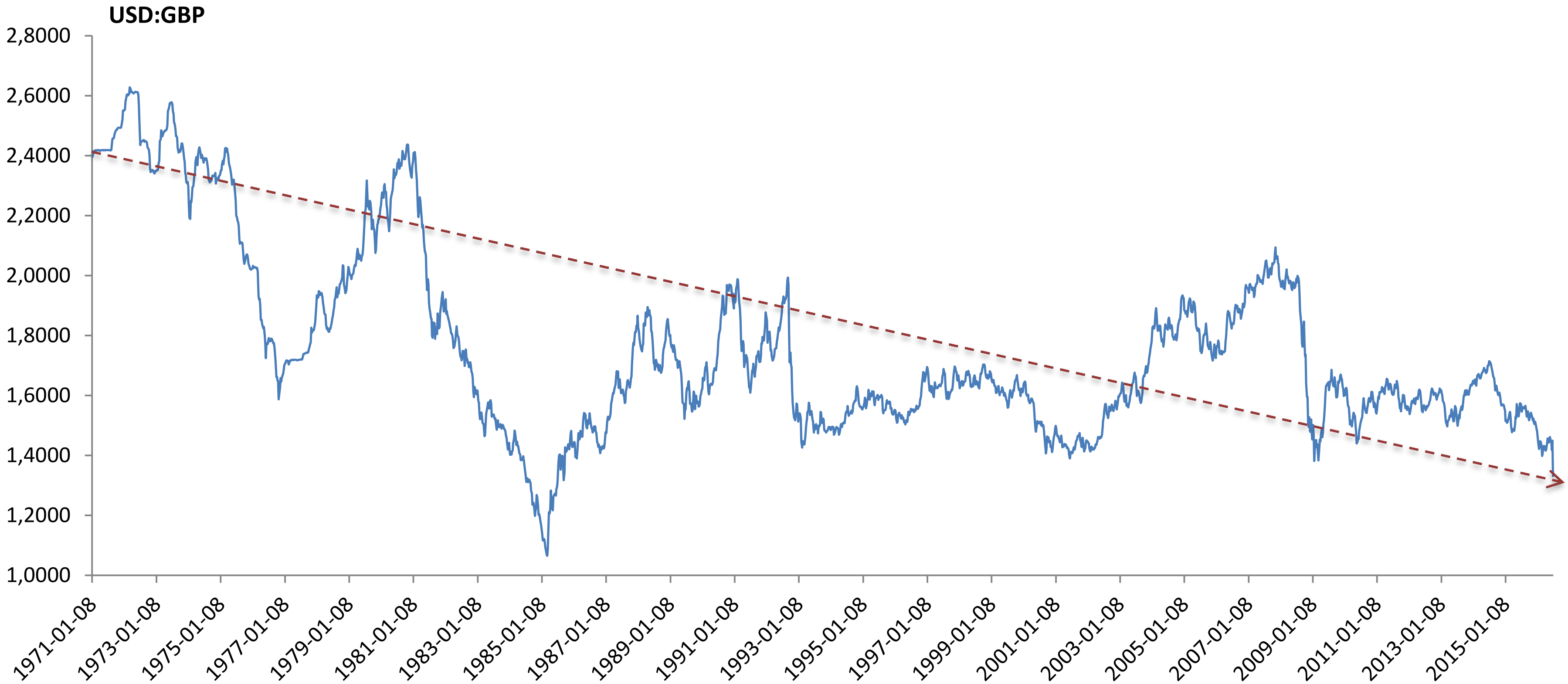




In the weeks after the ‘Brexit’ event global markets fell by nearly 5% as fears of a 2008 redux permeated the ecosystem. However, soon after, concerns began to recede, global markets began to recover, except for the sterling. The above graphs illustrates the prices movements of equity indices during the month of Brexit in various markets.

Source: Bloomberg

A Historical Look in the GBP: USD Relationship (1971-2016)



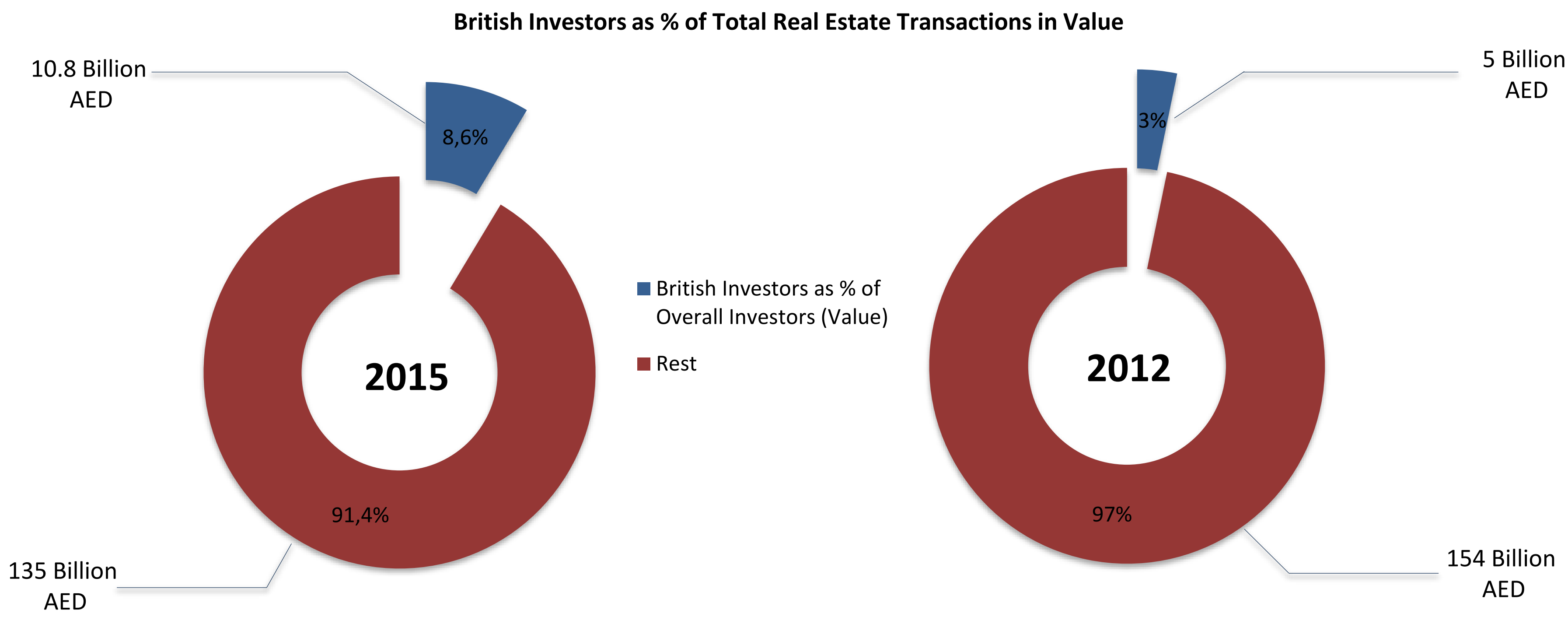
An historical look into the relationship between the GBP and the US dollar, shows a systematic devaluation over the last 35 years. This decline in the currency levels has not hindered the ability of residents to invest in assets abroad, particularly in real estate assets in Dubai.

Source: FRED

Currencies and Foreign Real Estate

“The first panacea for a mismanaged nation is inflation of the currency; the second is war. Both bring a temporary prosperity; both bring a permanent ruin. But both are the refuge of political and economic opportunists” - Ernest Hemingway

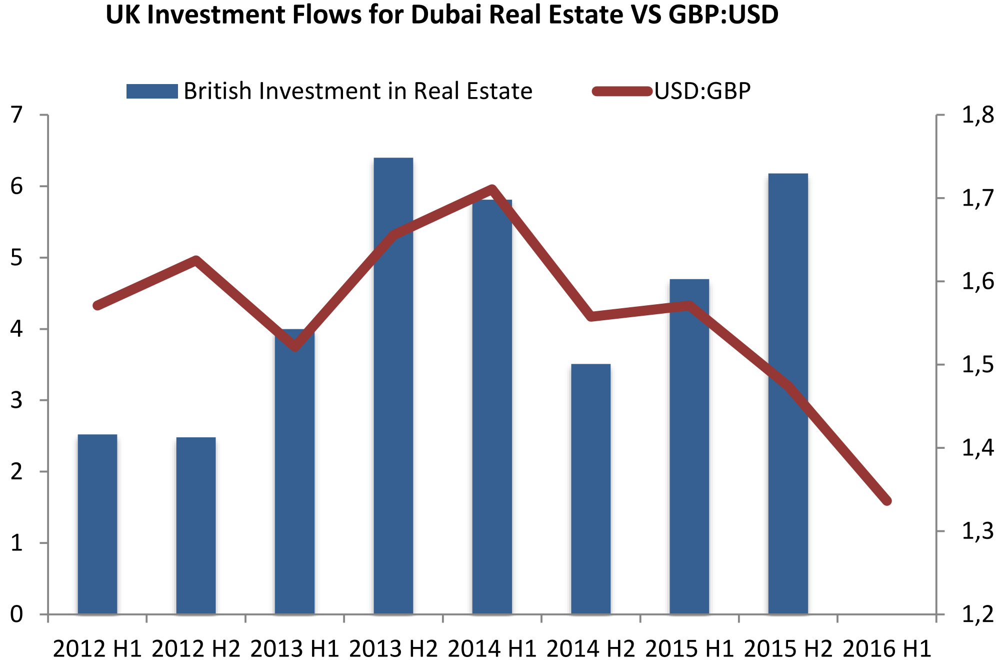
British Investment Flows in Dubai Real Estate have doubled in absolute Quantum over 4 years

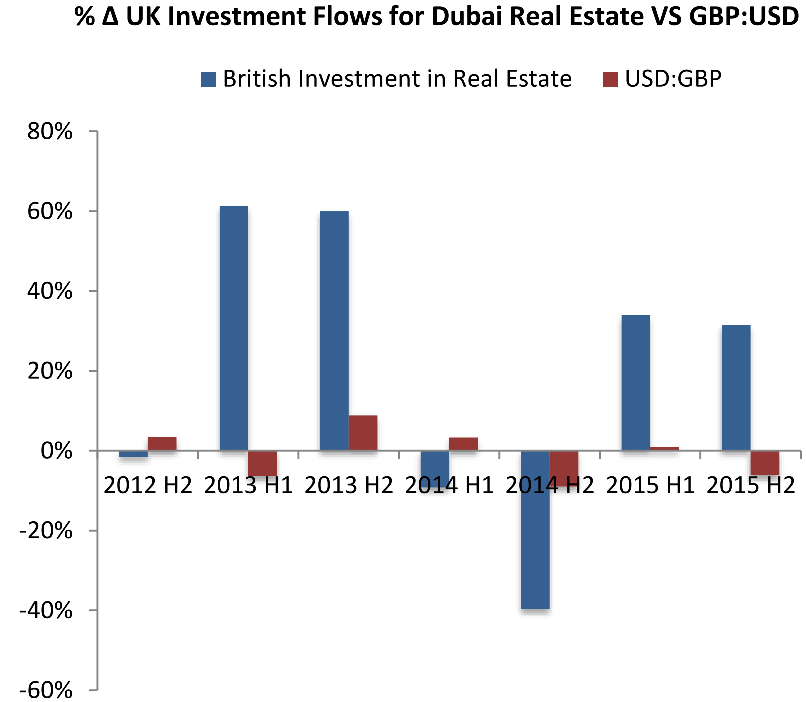


The above graph reveals the growth of British Investors in the Dubai real estate market in the last four years. In terms of the absolute quantum the investment levels have doubled, but as a percentage of the overall value of transactions it has nearly tripled. In 2007, the level of British Investments in Dubai real estate totaled AED 2.1 Billion, marking a near 5x increase in the last 9 years.

Source: Dubai Land Department

Pound and British Buying Real Estate : 0.26% Correlation

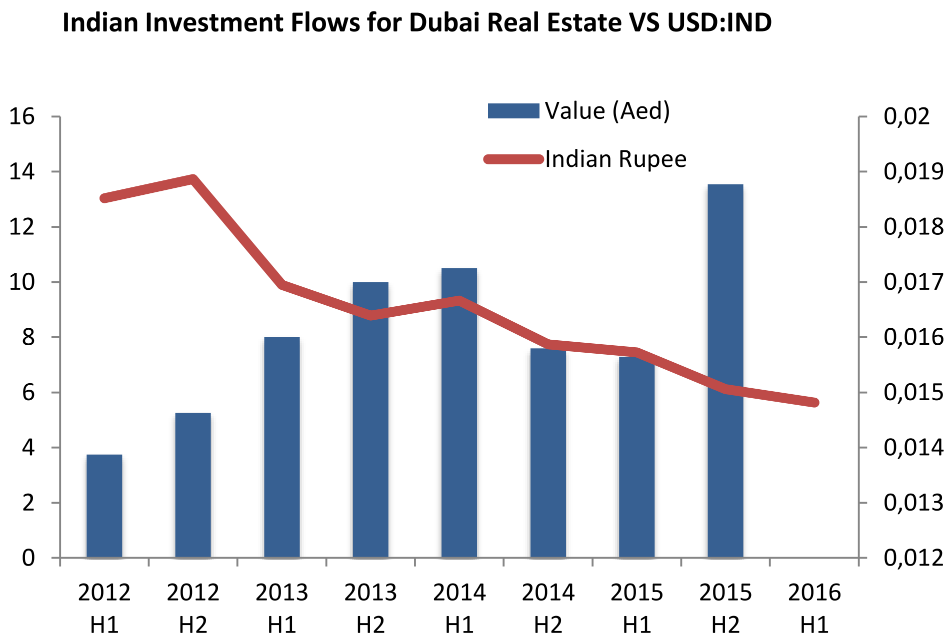


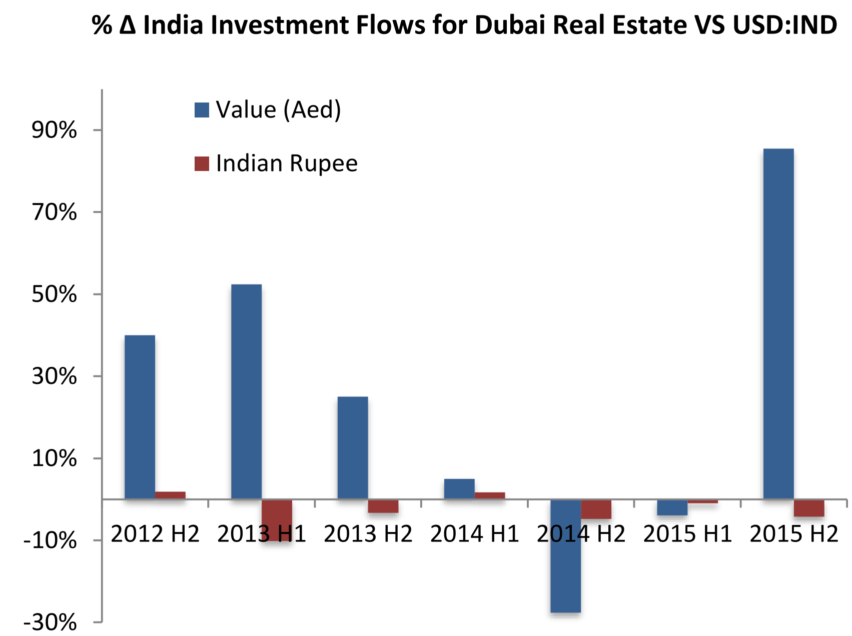


The devaluation of the sterling after the 'Brexit' has sparked fears of reduced investment flows into the real estate market in Dubai. However we witness that over the last 18 months the sterling has devalued by 5%, but investment flows have continued to increase. Over a four year horizon, investment flows of UK investors in Dubai real estate assets against the sterling has a mildly positive correlation (0.26). This implies that the currency fluctuation is not a predominant factor in purchasing overseas assets. In point of fact, data reveals that even as the value of the GBP has declined over the last 9 years, money flows into Dubai's real estate sector has steadily ratcheted higher.

Source: Dubai Land Department

Indian Investors and Dubai Real Estate Assets (+0.27)

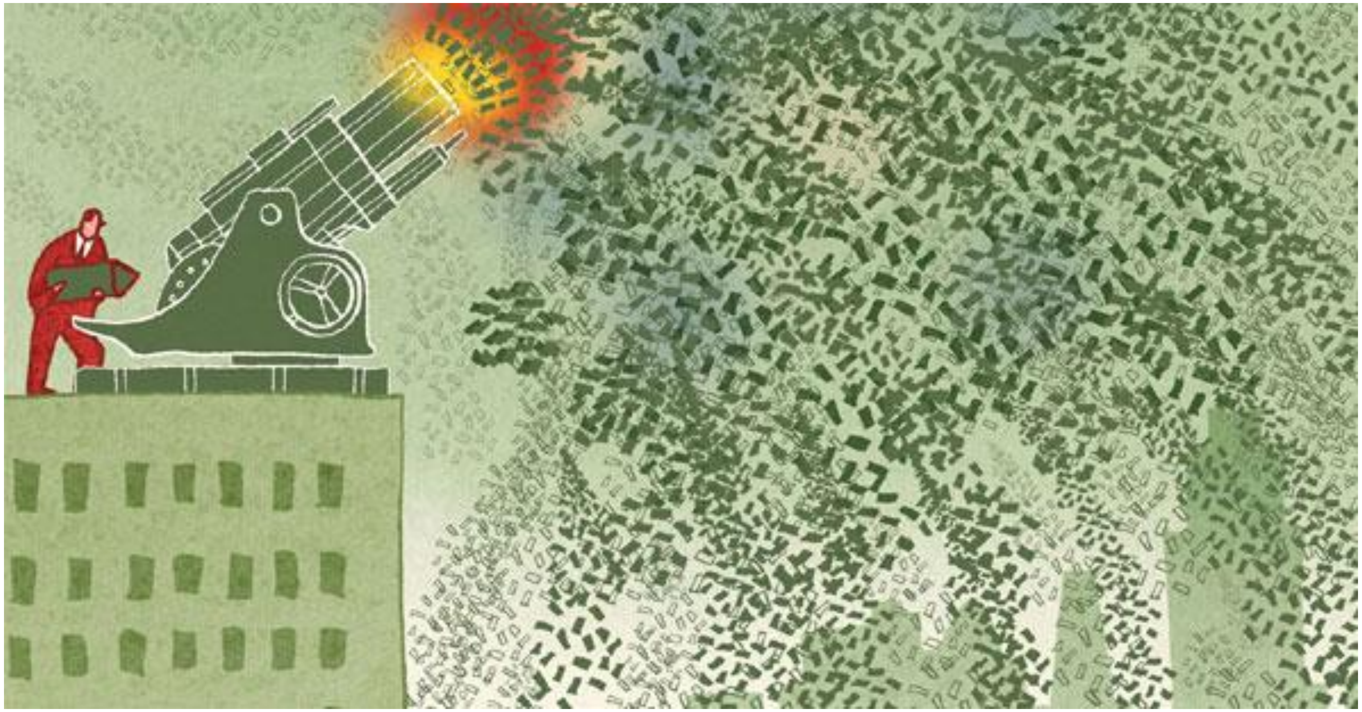




The above graph illustrates the devaluation of the Indian currency against the investment flow from Indian nationals into Dubai real estate assets. Similarly to the UK, there was a low moderate correlation implying that currency fluctuation has a minor role in this investment decision.

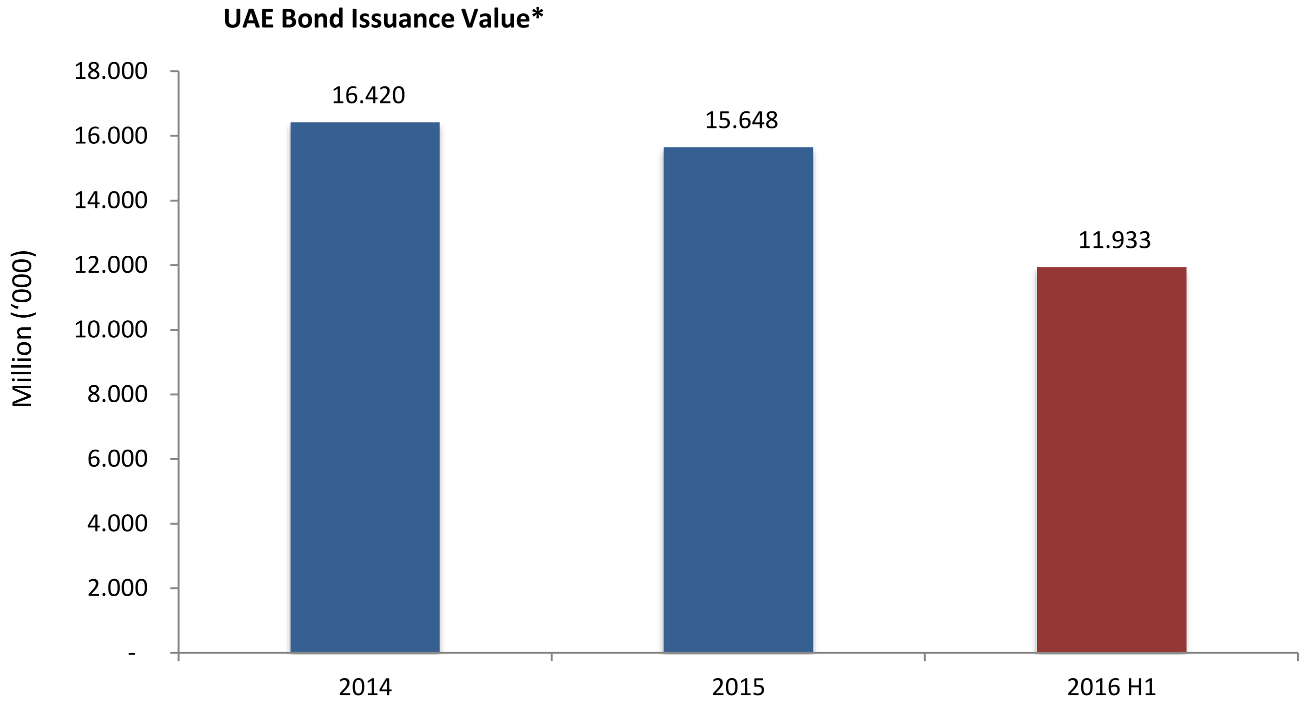
Source: Dubai Land Department

Fiscal Stimulus on the way



"The basic prescription for preventing deflation is straightforward, at least in principle: Use monetary and fiscal policy as needed to support aggregate spending, in a manner as nearly consistent as possible with full utilization of economic resources and low and stable inflation. In other words, the best way to get out of trouble is not to get into it in the first place."
Ben Bernanke

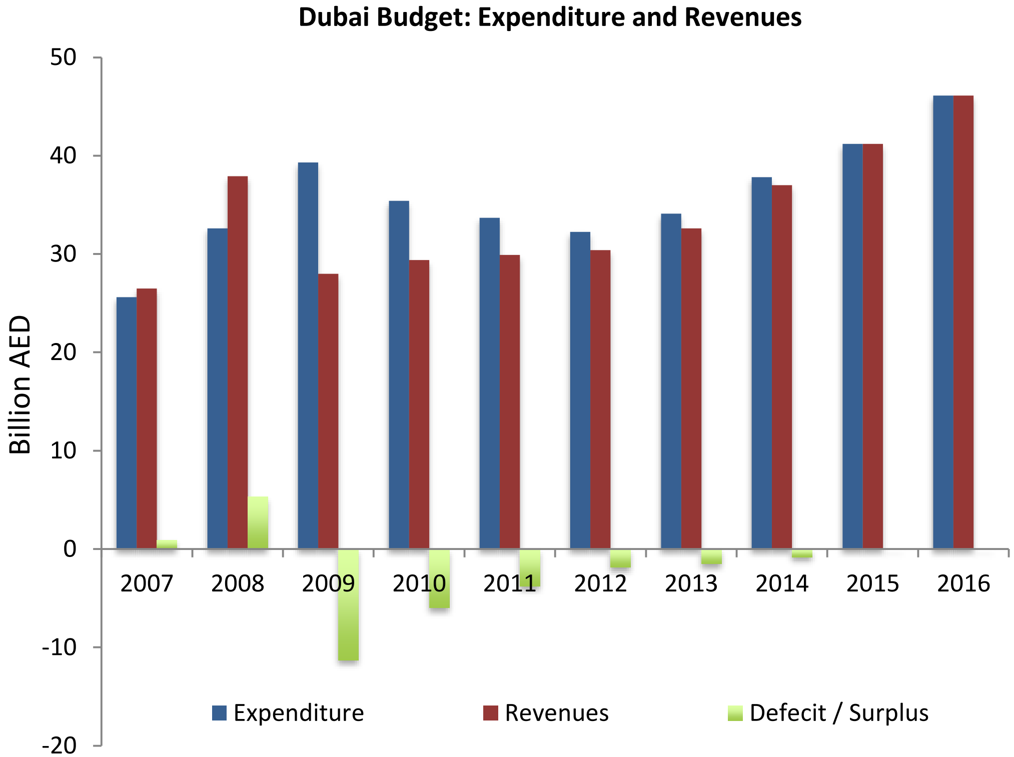
Bond Issuance within the UAE ratchets Higher

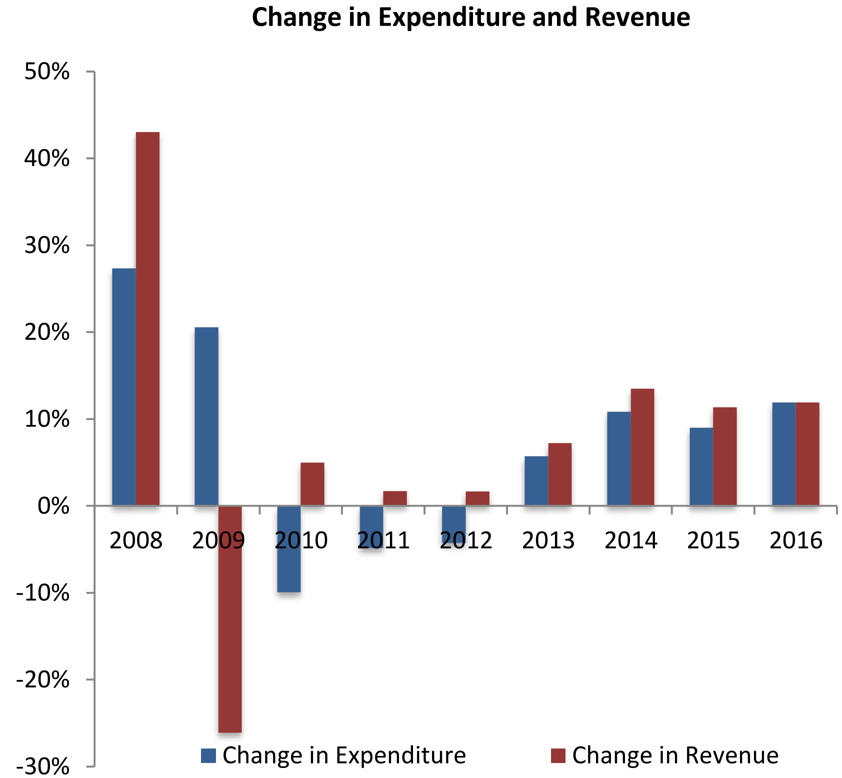


The above graph highlight the UAE bond issuance by value of both private and public sector entities. In the first half of 2016, the value is already 72% of 2015, implying the liquidity within the system will continue to ratchet higher in order to pursue the ambitious infrastructure expansion program in place.

***The Gulf Bond and Sukuk Association**

Dubai: The Lion in Winter (A look into the Budget Spending of Dubai)





After the 2008 global financial bust, Dubai (along with the rest of the world) responded by cutting budgetary expenditures, which amplified the contractionary impact on the economy. However, it is apparent from the chart above, that starting from 2010, the government adopted a policy of sustained fiscal expansion, leading to constant increases in budgetary spending on a year over year basis. This has been true for 2016 as well, where Dubai has bucked the regional trend, announcing an increase in budgetary spending of 12%. This continued expansionary stance has and will continue to percolate throughout the economy, making this cycle dramatically different from the 2008 episode.

Source: Unitas Consultancy / Reidin – “Dubai: The Lion in Winter”

Conclusions

British Investors in the Dubai real estate market in the last four years have doubled in absolute quantum

A correlation analysis of UK investment flows against the currency movements over the last 5 years suggests a mildly positive relationship of 0.26

Brexit and Dubai Markets

The recent panic of 'Brexit' caused global markets to fall by 5%, which included the S&P, FTSE, and the DFM. As fear receded, the markets made a quick recovery, regaining the losses.

The sterling, which fell 10% on the day remained at 30 year lows. Over the last 35 years the pound has systematically devalued against the US dollar. However this decline in the currency levels has not hindered the ability of residents to invest in assets abroad, particularly in real estate assets in Dubai.

Currency Movements and Foreign Investments

An analysis of the correlation between the UK currency strength against investment flows shows that there is a mildly positive relationship. This Implies that whilst currency moves are a factor, there are a number of other variables that have overwhelmed the systematic depreciation of the GBP during this time frame. A similar relationship can be witnessed in Indian investors against their home currency.

British investors have continued to increase exposure in Dubai real estate assets (increasing from AED 5B to AED 10B in 5 years).

Fiscal Stimulus on the Way

The UAE has adopted an expansive fiscal policy, which is reflected in their bond issuance in H1 2016. They have issued a total amount of USD 11.9 B, which is equivalent to 74% of the full year before.

The raising of liquidity by both the private and public sector is inline with funding their ambitious project.

Dubai has been the only city in the region that has increased its budget spend by 12%, whereas other places were cutting budgets.

Conclusions

The 'Brexit' event will continue to play out over next few years, creating uncertainty and instability in the UK and global markets.

However, it is clear that currency fluctuation don't influence overseas buyers to the degree that will drastically effect buying patterns.

The uncertainty in the UK markets could be beneficial to Dubai real estate assets, as investors decide to reallocate portfolios out of fragile market and depreciating currency and towards markets that have an expansionary fiscal bent.

GCP believes in in-depth planning and discipline as a mechanism to identify and exploit market discrepancy and capitalize on diversified revenue streams.

Our purpose is to manage, direct, and create wealth for our clients.

GCP is the author for these research reports

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