

Real Estate Development and Financial Markets (August 2005)

The UAE is in the midst of a construction boom. This has not only helped the performance of cement companies on the local financial markets, but activity has spilled over into real estate sector stocks.

The UAE stock markets, mainly Dubai Financial Market, witnessed heightening trends in the past couple of months. In fact UAE indices notched strong gains over the previous year, particularly in the real estate development and financing sectors.

This is mainly attributed to the anticipation of another round of strong macroeconomic performance in the wake of high oil revenues, strong liquidity as a result of the diversion of funds from the western capital markets to the maturing markets in the GCC after the September 11 events, and the outstanding performance of leading real estate developers such as Emaar Properties.

Furthermore, positive economic developments in Dubai and the UAE have boosted forecasts for 2005 to reflect the expansionary climate Dubai currently enjoys. In fact Dubai has become a leading destination for business and investment for numerous considerations, mainly its geographical proximity to the markets of the Middle East, Africa and Asia, combined with its tax free environment, sophisticated infrastructure and internationally acclaimed free zones.

In brief, strong corporate results, coupled with increased business and consumer confidence in Dubai and the UAE are sending the markets and indices to their all-time high. The strong first and second quarter results of listed companies operating in the real estate market seem to have reaffirmed the confidence of the investors in the ever expanding Dubai and UAE economy and have acted as trigger for investors to take further positions in the markets. Listed companies operating in the real estate market are already among the major players which are implementing multimillion dollar projects across the region.

The market capitalization would further expand as new listings grow and the IPO market would experience substantial growth in late 2005.

Therefore, there should be clearly elaborated regulations in place to protect shareholders, investors and companies alike.

Shedding the light on the regulatory framework governing the financial markets in the UAE may help us identify the much needed improvements to the system.

Federal Law No. 4 of 2000 established the Emirates Securities and Commodities Authority “ESCA”, and authorized the establishment of securities and commodities markets in the UAE.

The Law empowered the Authority to issue regulations, regulate the securities and commodities markets, and receive reports and complaints relevant to the activities of the markets.

Following the issuance of Law No. 4 of 2000 and pursuant to its terms and conditions, two financial markets were established in the Emirates of Abu Dhabi and Dubai. Abu Dhabi Securities Market was established pursuant to Abu Dhabi Local Law No. 3 of 2000 (“ADSM”), and Dubai Financial Market was established pursuant to Dubai Local Decree No. 14 of 2000 (“DFM”). Both markets were duly licensed by the Authority.

Pursuant to Law No. 3 of 2000, ADSM is managed by a board of directors, in which Article (6) vested the power to oblige listed companies to disclose information and any material developments occurring in any such companies.

ADSM applies the regulations issued by the Authority in relation to membership in the market, listing, licensing of brokers, transparency and disclosure and other effective regulations and instructions in addition to any future rules and regulations that may be issued by the Authority.

Disclosure rules are contained in Articles 33 to 35 of Federal Law No. 4 of 2000. Essentially, Article 33 gives the Authority permission to require disclosure “.. of any material developments which may affect the price of listed securities such as The issue of new securities”, and empowers the Authority to publish any such information as it may deem necessary.

However, although Articles 33 and 34 broadly require publication of “any clarifying information relating to (listed company) circumstances, activities or anything that would guarantee the integrity of the transactions and confidence of the investors whenever requested to do so”, Article 35 provides that such publication may not be made if the management of the listed company considers that the said publication may cause extreme prejudice to its interests.

Although the financial markets have made headway on a number of the aforementioned objectives in relation to the protection of investors, there is a great deal of room for improvement and establishing best practices to maintain fairness to all investors in the markets and protect minority shareholders. The regulation of the primary market needs development. In fact, more must be done to develop the markets, pushing them into an era of international recognition and compliance in standards.

The abuse of disclosure rules is a cause of serious concerns to the extent that certain cautious commentators are claiming that financial markets are merely driven by speculation and describe the phenomenon of growth as a bubble ready to burst. But the facts are that the real estate market is booming at present and its success is unparalleled.

Therefore the elaboration and proper application of disclosure rules by the Authority is essential to curb speculation and ensure smooth transactions and price behavior. Also, to curb speculation and rationalize market behavior, the development and regulation of new real estate investment vehicles such as real estate funds and real estate trusts is essential.

It is high time that the investors called for a more ambitious pace of change at the financial markets and in the structure of the market supervision, as a change is a must to help protect, support and lead the local financial markets into a better regulated, organized and legislated future.

Tony Maalouli
LLM in Private Law
Managing Director,
ProConsult Advocates & Legal Consultants