

# Dragon-Ukrainian Properties & Development PLC

## Acquisition of a 35% interest in Arricano Trading Ltd

13 September 2010

The Board of Directors of Dragon-Ukrainian Properties & Development Plc (“DUPD”) is pleased to announce the acquisition of a 35% interest in Arricano Trading Ltd (“Arricano” or “the Company” and together with its subsidiaries, the “Arricano Group”), a leading developer of upscale shopping centres in Ukraine, through an issue of new shares by Arricano for \$30 million payable by DUPD in cash (the “Transaction”). The \$30 million investment will be used by Arricano to fund further development of the shopping centre portfolio and also to repay certain existing Arricano debt.

The current owner of Arricano is Expert Capital S.A. (“Expert Capital”), a Luxembourg-based company ultimately owned by an Estonian private investor, Hillar Teder, with extensive experience in real estate development in Eastern Europe. Expert Capital will retain a 65% shareholding in the Company.

### Description of the Arricano Portfolio

Arricano’s portfolio comprises five shopping centre projects with a total building area of over 400,000 sqm and gross leaseable area of 232,000 sqm, of which 128,000 sqm are currently operational with the balance scheduled for delivery during 2011-2013. The portfolio, consisting of international quality shopping malls, is unique for the Ukrainian market where both professional retail space and specialised retail developers are highly scarce. Two of the schemes, representing 60% of the total leaseable space, are located in Kyiv namely “Sky Mall” (114,000 sqm) and “M26” (24,000 sqm). The remaining three projects are located in large regional cities in Ukraine, namely “Sun Gallery” in Kryvyj Rig (34,000 sqm), “City Mall” in Zaporizhzhya (22,000 sqm), and “Inter Mall” in Simferopol (38,000 sqm).

Sky Mall, an upscale shopping mall designed by the award winning and internationally renowned British architects Chapman Taylor, is tenanted by prime retailers including Auchan, Inditex, New Yorker, Top Shop, Marks & Spencer and New Look. The 2<sup>nd</sup> stage of Sky Mall was completed and opened to the public on 27 August 2010. Sky Mall is a landmark retail project in Ukraine, a truly Class-A development being the largest shopping mall in Kyiv with current leaseable space of 67,400 sqm and parking space for over 3,000 cars. Sky Mall’s leaseable space is currently 93% pre-let, of which 90% of the stores are occupied with the remainder due to complete fit-out works by the end of 2010.

The rest of the leaseable space (60,500 sqm) is currently spread across Arricano’s regional schemes, represented by the fully completed Sun Gallery, and the 1<sup>st</sup> stages of InterMall and CityMall shopping centres. The tenant mix in regional schemes comprises key international and Ukrainian retailers, including Auchan, Furshet, Comfy and Intertop.

### Call Option Agreement

Arricano holds a 100% interest in 4 centres and a shareholding of 50% minus 1 share in Sky Mall. In relation to Sky Mall, Arricano has entered into a call option agreement with its local partner in this project, whereby it can acquire the remaining shareholding of 50% plus 1 share at a pre-agreed valuation of \$51-56 million, depending on the timing (the “Sky Mall Call Option”). The Sky Mall Call Option can be exercised during the period of November 2010 - March 2011. Expert Capital and DUPD have agreed to consider a capital increase into Arricano of \$60 million to finance the Sky Mall Call Option, to complete the development of the 2<sup>nd</sup> stage of InterMall and repay certain indebtedness.

DUPD has reserved the right, but not the obligation, through the Shareholders Agreement with Expert Capital in Arricano, to invest additionally up to \$30 million, either by itself or together with co-investors to partially fund the exercise of the Sky Mall Call Option. Expert Capital also has the right, but not the obligation, to fund the remaining \$30 million.

### Future development

The \$30 million capital investment by DUPD into Arricano will be used to:

- (i) finance completion of the 2<sup>nd</sup> stage of the CityMall shopping centre;
- (ii) fund the equity element of the budgets for the M26 project and 2<sup>nd</sup> stage of the InterMall project; and
- (iii) repay \$5 million of outstanding debt.

There is a \$40 million debt facility in place from the European Bank for Reconstruction and Development (“EBRD”) for completion of the M26 and InterMall projects. In addition, Arricano is currently in negotiations with an international

commercial bank to obtain debt finance for the development of Sky Mall's 3<sup>rd</sup> stage, which will add 46,600 sqm of leasable retail space.

Arricano is planning to complete the development of its existing portfolio projects during 2011-2013, with the opening of the 2<sup>nd</sup> stage of City Mall, scheduled for 1H2011.

### **Operational and Financial Highlights**

The Shareholders Agreement provides that DUPD and Expert Capital shall jointly decide on key matters of the Arricano business, while Expert Capital shall be predominately responsible for managing the day-to-day operations.

Following the recent opening of Sky Mall's 2<sup>nd</sup> stage, the annualised Net Operating Income ("NOI") of Arricano is \$13.5 million and DUPD's investment manager believes that NOI could grow to \$18.5 million in 2011 and \$29 million in 2012, driven by the openings of the completed developments and a modest recovery of rental rates from their currently depressed levels. Should Arricano exercise the Sky Mall Call Option, DUPD's investment manager believes the combined NOI of all five projects could increase to \$29.3 million in 2011, and \$41.5 million in 2012.

The unaudited profit before tax for the Arricano Group for 1HY 2010 is \$5.6 million which has benefitted from the substantially stronger anchor tenant base including a major lease agreement with anchor tenant Auchan. In addition, the 1HY 2010 results do not include the rental income from the opening on 27 August 2010 of the 2<sup>nd</sup> stage of the Sky Mall shopping centre and the expiry of initial rent free periods that will be reflected in FY 2010 results. The total assets of Arricano were \$309 million as per audited consolidated financial statements for the period ending 31 December 2009.

The Arricano Group's bank debt currently stands at c. \$90 million, comprised predominantly by loans from commercial banks and the EBRD. The Arricano Group has already successfully restructured \$39 million of this debt with a further \$16 million in the final stage of restructuring.

### **Strategic Plan**

As a part of its development strategy, Arricano aims to conduct an IPO on a reputable foreign stock exchange during 2012 in order to finance further growth through acquisition and the development of new commercial real estate projects. Post IPO, Arricano intends to maintain its focus on the retail property sector, capitalising on its development expertise and knowledge of the local retail market, but may also consider mixed-use developments in proper locations in Kyiv.

Although Arricano's portfolio is expected to generate substantial cash flow, Arricano will selectively consider divestments of shopping centres post completion and stabilisation of rental income, should yield compression deliver strong financial returns for Arricano's shareholders, retaining part of the sales proceeds (after any debt repayments) for new developments, while distributing the balance to its shareholders.

Aloysius van der Heijden, DUPD Chairman, commented:

"I am very satisfied with our investment into Arricano, as I am convinced that assets of this type are most capable of long-term value creation, and maximising returns to DUPD shareholders. Arricano projects, in particular Sky Mall, which by all means, represents a landmark shopping mall in Kyiv, are professional shopping centres of international quality, a sector still nearly non-existent in Ukraine. Such retail centres possess all the right features to withstand competition, generate stable rent-roll, and maximize the investor's upside in the long-run. I am also happy with the timing of the Transaction, which is taking place a year after the Ukrainian retail market bottomed-out in 2H2009, allowing the Company to promptly capitalise on the ongoing recovery of the sector."

Chris Kamtsios, Senior Manager and Managing Director of Dragon Capital Partners (the Investment Manager of DUPD), commented:

"This acquisition falls right within our investment priorities, announced by the Company during 2009 upon the burst-out of the crisis in Ukraine. We commenced negotiations on this Transaction one year ago and are very happy to see them come to fruition. We see operational or close to completion retail schemes as the most attractive investment segment in the current Ukrainian market, given the recovery of the sector, weak competition, delayed deliveries, and still attractive pricing due to low levels of foreign investment. With vacancies across shopping centres in Ukraine narrowing to 1-2% on average and rents increasing in 1H2010, we are convinced in the strong growth prospects of Arricano."

DUPD is excited to develop Arricano together with our new partner, Expert Capital, which is one of very few foreign retail developers in Ukraine and one that shares the same values, investment priorities and commitment to quality as us."

Hillar Teder, principal owner of Expert Capital, commented:

“We have been looking for a strong long-term co-investor after the financial crisis started here in Ukraine, and are very pleased to have Dragon-Ukrainian Properties & Development as our partner. DUPD is a large foreign investment fund with strong local presence and expertise, making it well suitable for our strategic development goals. Together with a trustworthy and financially strong investment partner, we plan to develop our portfolio much faster and gain better access to international capital markets, as we prepare Arricano for an IPO.”

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