

Air Arabia

Higher load factor and robust passenger traffic boosted profitability

1Q23 Net profit is higher than our estimates

Air Arabia's (The Company/ AIRARABIA PJSC) net profit rose 17.4% YOY to AED 342 Mn in 1Q23, higher than our estimate of AED 313 Mn. The rise in net profit was mainly due to an increase in revenue, finance income and other income partially offset by an increase in cost of sales and operating expenses.

P&L highlights

Air Arabia's revenue rose 26.6% YOY to AED 1,429 Mn in 1Q23 due to a rebound in passenger traffic and the addition of nine routes across its global network. The Company served 3.9 Mn passengers in 1Q23 as compared to 2.4 Mn passengers in 1Q22 whereas the seat load factor rose from 79% in 1Q22 to 85% in 1Q23. On the other hand, Air Arabia's direct cost rose 31.5% YOY to AED 1032 Mn in 1Q23 faster than revenue in 1Q23. Thus, gross profit rose 15.5% YOY to AED 398 Mn in 1Q23 with a gross profit margin of 27.8% in 1Q23 as compared to 30.5% in 1Q22. Furthermore, the company's selling and marketing expenses rose 47.7% YOY to AED 20 Mn in 1Q23 whereas G&A expenses rose significantly 52.4% YOY to AED 112 Mn in 1Q23. While operating profit rose 7.3% YOY to AED 301 Mn in 1Q23. The Company's finance income more than doubled to AED 41 Mn in 1Q23 as compared to AED 15 Mn in 1Q22 due to higher benchmark rates in the economy whereas finance cost declined 5.6% YOY to AED 26 Mn in 1Q23 due to a reduction in lease liabilities and bank borrowings. Air Arabia's other income reported a robust growth and rose to AED 26 Mn in 1Q23 up as compared to AED 12 Mn in 1Q22. Thus, profit before non-controlling interest rose 17.5% YOY to AED 342 Mn in 1Q23.

Balance sheet highlights

Air Arabia's borrowings declined marginally from AED 139 Mn in 4Q22 to AED 136 Mn in 1Q23. Lease liabilities declined 12.6% to AED 2.6 Bn in 1Q23. Air Arabia's cash and bank balance stood strong at AED 5.1 Bn in 1Q23 as compared to AED 3.9 Bn in 1Q22. Similarly, Air Arabia generated a cash flow of AED 657 Mn in 1Q23 from its operation as compared to AED 501 Mn in 1Q22.

Target price and rating

We maintain our BUY rating on Air Arabia with a target price of AED 2.75. The aviation industry continues to see recovery in 1Q23 primarily led by a rebound in the passenger demand and reported a robust growth in the air travel demand. The total number of passengers flying Air Arabia increased to 3.9 Mn in 1Q23 as compared to 2.4 Mn in 1Q22. The Company reported strong growth in seat load factor which rose 8% YOY to 85% in 1Q23. Air Arabia continued to expand its global network and added nine new routes across the world during 1Q23 from its seven strategic hubs including UAE, Morocco, Egypt, Armenia and Pakistan. The Company operated 68 aircraft in service including 59 Airbus A320 and 9 Airbus A321 at the end of 1Q23. Further, Air Arabia ordered 120 Airbus A320 family aircraft whose delivery will start in 2025 which will strengthen its market positioning going forward. Additionally, Air Arabia's management is committed to improving its operational efficiency and taking cost-control measures will enhance the company's performance. The company's management is providing special attention towards active fleet management to ensure healthy growth sup-

Rating : BUY

First Look Note – 1Q23

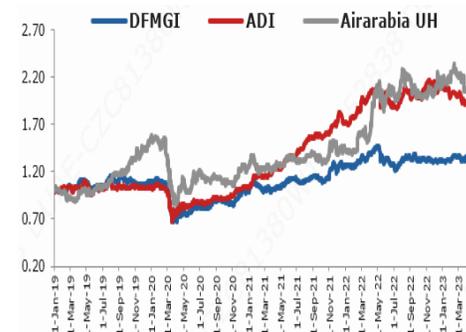
Sector: Transportation

Recommendation

Current Price (12-May-23)	2.33
Target Price (AED)	2.75
Upside/Downside (%)	+20%

Stock Information

Market Cap (mm)	10,733.41
Paid Up Capital (mm)	4,666.70
52 Week High	2.41
52 Week Low	1.82
3M Avg. daily value (AED)	14,209,450



Financial Ratios

Dividend Yield (12m)	6.52
Dividend Pay-out (%)	0.00
Price-Earnings Ratio (x)	8.42
Price-to-Book Ratio (x)	1.64
Book Value (AED)	1.40
Return-on Equity (%)	19.85
Earning Per Share (AED)	0.27
Beta	0.84

Stock Performance

5 Days	0.88%
1 Months	5.50%
3 Months	-1.71%
6 Months	9.00%
1 Year	11.11%
Month to Date (MTD)	5.02%
Quarter to Date (QTD)	8.49%
Year to Date (YTD)	6.98%

ported by the adoption of new technologies. A rise in fuel price affected the company's net profitability in 1Q23 we expect softness in energy prices to drive profitability going forward. Moreover, the company's reported a strong financial position with net cash balance of AED 5.1 Bn 1Q23 supported by a steady free cash flow from its operating activities. Air Arabia's management approved a dividend distribution of 15% cash dividend equivalent to dividend per share of 15 fils in 2022 with a dividend yield of 6.9%. Thus, based on our analysis, we maintain our rating to BUY on the stock.

Air Arabia—Relative Valuation

(at CMP)	2018	2019	2020	2021	2022	2023F
PE	-17.8	11.0	-56.6	15.1	8.9	7.9
PB	2.4	2.0	2.4	1.8	1.6	1.4
EV/EBITDA	9.1	5.7	20.1	5.6	3.5	3.0
Dividend yield	NA	3.9%	NA	3.6%	6.4%	6.9%

FABS estimate & Co Data

Air Arabia - P&L

AED mm	1Q22	4Q22	1Q23	1Q23F	Var.	YOY Ch	QOQ Ch	2022	2023F	Change
Revenue	1,129	1,393	1,429	1,310	9.1%	26.6%	2.6%	5,242	5,927	13.1%
Direct costs	-784	-964	-1,032	-943	9.4%	31.5%	7.0%	-3,810	-4,262	11.9%
Gross profit	344	429	398	367	8.4%	15.5%	-7.3%	1,432	1,665	16.3%
Selling & Marketing exp.	-13	-21	-20	-18	8.2%	47.7%	-7.0%	-68	-95	39.4%
G&A expenses	-50	-112	-76	-52	45.6%	52.4%	-31.8%	-286	-284	-0.7%
EBITDA	435	459	461	419	10.1%	6.0%	0.6%	1,710	1,992	16.5%
EBIT	281	296	301	296	1.8%	7.3%	1.9%	1,077	1,285	19.3%
Finance income	15	33	41	22	83.4%	175.2%	24.3%	89	107	20.1%
Finance costs	-28	-31	-26	-31	-16.2%	-5.6%	-14.3%	-115	-127	10.3%
Other income	12	66	26	26	-1.9%	108.9%	-61.3%	136	119	-12.6%
Share of profit on JVs	11	-9	0	0	NM	NM	NM	36	0	NM
Profit before NCI	291	356	342	313	9.2%	17.5%	-3.9%	1,222	1,383	13.2%
Non-controlling int.	0	1	0	0	NM	NM	NM	1	0	NM
Net Profit	291	355	342	313	9.1%	17.4%	-3.8%	1,222	1,383	13.2%

FABS Estimates & Co Data

Air Arabia - Margins

	1Q22	4Q22	1Q23	YOY Ch	QOQ Ch	2022	2023	Change
GPM	30.5%	30.8%	27.8%	-269	-297	27.3%	28.1%	78
EBITDA Margin	38.6%	32.9%	32.3%	-628	-62	32.6%	33.6%	99
OPM	24.9%	21.2%	21.1%	-379	-13	20.5%	21.7%	114
Net margin	25.8%	25.5%	23.9%	-187	-159	23.3%	23.3%	3

FABS estimate & Co Data

Valuation:

We use Discounted Free Cash flow (DCF) and Relative Valuation (RV) to value Air Arabia. We have assigned 70% weight to DCF and 30% to RV.

Valuation Method	Target	Weight	Weighted Value
DCF	2.72	70.0%	1.91
Relative	2.83	30.0%	0.85
Weighted Average Valuation (AED)			2.75
Current market price (AED)			2.33
Upside/Downside (%)			18.03%

1) DCF Method:

Air Arabia is valued using free cash flow to equity since the Company is nearly debt free. We have discounted the cash flow using the cost of equity of 8.9%. Cost of equity is calculated by using 10-year government bond yield of 4.7%, beta of 1.0 and equity risk premium of 4.2%. Government bond yield is calculated after adding Dubai 10-year spread over 10-year US risk free rate. Also, assumed a terminal growth rate of 2.0%.

Sum of PV (AED, Mn)	3,748
Terminal value (AED, Mn)	8,956
FV to Common shareholders (AED, Mn)	12,704
No. of share (Mn)	4,667
Current Market Price (AED)	2.33
Fair Value per share (AED)	2.72

DCF method

(All Figures in AED Mn)	FY 2023E	FY 2024E	FY 2025E	FY 2026E	FY 2027E
Net Income	1,383	1,404	1,454	1,407	1,332
D&A	707	791	885	994	1,111
Capex	-1,003	-1,196	-1,275	-1,273	-1,239
Net change in working capital	-263	-57	-83	-92	-298
Free Cash Flow to Equity (FCFE)	823	942	980	1,036	907
Discounting Factor	0.95	0.87	0.80	0.73	0.67
Discounted FCFE	779	819	782	759	609

2) Relative Valuation:

We have used local and international peers to value Air Arabia and it is valued using the EV/EBITDA multiple. It is valued at EV/EBITDA of multiple of 5.5x in line with peers.

Company	Market (USD Mn)	EV/EBITDA (x)		PE (x)	
		2023	2024	2023	2024
Gol Linhas Aereas inteligentes SA	571	6.2	4.7	17.7	3.1
Jazeera Airways	1,357	8.6	8.9	13.7	14.1
Pegasus Hava Tasimacigli anonim sirketi	2,758	5.5	4.6	7.9	6.1
Jetblue Airways corporation	2,066	4.5	4.0	11.5	4.4
Easy Jet PLC	3,094	3.0	2.7	10.5	7.0
Average		5.6x	5.0x	12.3x	6.9x
Median		5.5x	4.6x	11.5x	6.1x
Max		6.2x	4.7x	13.7x	7.0x
Min		4.5x	4.0x	10.5x	4.4x

FAB Securities Awards



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Best New Mobile Application
in UAE 2016
by "IFA"



Best Equity Finance Company
in UAE 2016
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