

## National Central Cooling Company (Tabreed)

Addition of new customers and higher volumes drive profitability

### 1Q23 Net profit higher than our estimate

National Central Cooling Company's (Tabreed/The Company) net profit more than doubled from AED 88 Mn in 1Q22 to AED 236 Mn in 1Q23, higher than our estimate of AED 142 Mn. Net profit excluding one-time gain stood at AED 117 Mn in 1Q23. The growth in net profit is mainly driven by an increase in revenue due to higher volume and price coupled with strong growth in one-time gain due to revaluation of investment in associates and JVs partially offset by a rise in cost of revenue and higher operating expenses

### P&L highlights

Tabreed's revenue rose 10.4% YOY to AED 464 Mn in 1Q23 driven by an increase in price, addition of new connections, and higher volumes consumed. Tabreed's, total capacity rose from 1.24 Mn refrigeration tones (RT) in 1Q22 to 1.28 Mn RT in 1Q23. UAE capacity rose from 1.03 Mn RT in 1Q22 to 1.07 Mn RT in 1Q23, whereas capacity in Oman increased from 51 thousand RT in 1Q22 to 52 thousand RT in 1Q23, while capacity in Bahrain remains unchanged. Revenue from the chilled water segment rose 10.1% YOY to AED 447 Mn in 1Q23. The Company generated around 96% revenue from the chilled water segment. While the remaining revenue was contributed by the value chain business, which rose 18.7% YOY to AED 17 Mn in 1Q23. Additionally, the Company delivered a total of 1.27 Mn RT in 1Q23 with a utilization rate of 99.5% as compared to 1.24 Mn RT in 1Q22 at a utilization rate of 100.3%. Tabreed's cost of revenue grew 8.7% YOY to AED 224 Mn in 1Q23. Thus, gross profit increased 12.1% YOY to AED 240 Mn in 1Q23 with an increase in gross profit margin by 76 bps YOY to 51.7% in 1Q23. Furthermore, Tabreed's operating expenses rose 12.4% YOY to AED 68 Mn in 1Q23. Tabreed's EBITDA rose marginally 1.7% YOY to AED 268 Mn in 1Q23 with an EBITDA margin of 57.8% in 1Q23 as compared to 62.8% in 1Q22. As a result, operating profit grew 11.9% YOY to AED 172 Mn in 1Q23 with an operating margin of 37.1% in 1Q23 as compared to 36.6% in 1Q22. Finance cost rose marginally 1.9% YOY to AED 74 Mn in 1Q23 while finance income rose significantly from AED 1 Mn in 1Q22 to AED 16 Mn in 1Q23. Other gains and losses stood at AED 119 Mn in 1Q23 as compared to AED 0.3 Mn in 1Q23. The significant growth is mainly due to the issuing of new shares by the Saudi Tabreed at a premium resulting in a gain of AED 49.1 Mn in 1Q23 in addition to a gain of AED 100.6 Mn attributable to the settlement of the term loan before maturity. Share of associates and JVs declined by 14.5% YOY to AED 9 Mn in 1Q23. The share of profit attributable to non-controlling interest holders rose 19.1% YOY to AED 6 Mn in 1Q23.

### Balance sheet & cash flow highlights

Tabreed's cash and cash equivalents stood at AED 1,389 Mn in 1Q23 as compared to AED 1,773 Mn in 4Q22. The decline in cash balance was mainly due to the repayment of interest-bearing loans and borrowings and the repayment of Islamic financing. The Company's net cash flow from operating activities declined to AED 323 Mn in 1Q23 as compared to AED 489 Mn in 1Q22. The Company's debt declined to AED 6,457 Mn in 1Q23 as compared to AED 7,092 Mn in 4Q22. The Company's net debt to LTM EBITDA stood at 4.27x in 1Q23 as compared to 4.49x in 2022. In addition, AED 4.4 Bn debt is maturing in 2025 while AED 2.0 Bn debt is maturing between 2026-31.

**Rating : BUY**

## First Look Note – 1Q23

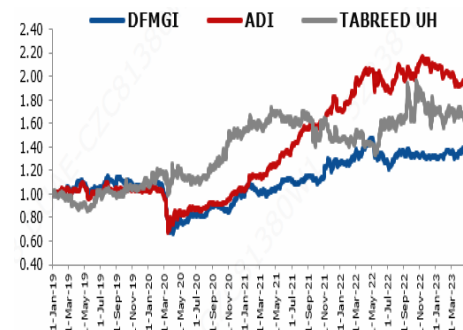
**Sector: Utility**

### Recommendation

Current Price (25-May-23)	2.89
Target Price (AED)	3.50
Upside/Downside (%)	+21%

### Stock Information

Market Cap (mm)	8,251.29
Paid Up Capital (mm)	2,845.27
52 Week High	3.52
52 Week Low	2.40
3M Avg. daily value (AED)	2,081,550



### Financial Ratios

Dividend Yield (12m)	4.66
Dividend Pay-out (%)	63.93
Price-Earnings Ratio (x)	11.00
Price-to-Book Ratio (x)	1.34
Book Value (AED)	2.17
Return-on Equity (%)	12.47
Earning Per Share (AED)	0.26
Beta	0.85

### Stock Performance

5 Days	-0.34%
1 Months	0.35%
3 Months	-2.36%
6 Months	-1.02%
1 Year	17.89%
Month to Date (MTD)	-1.02%
Quarter to Date (QTD)	-3.33%
Year to Date (YTD)	-2.03%

### Target price and rating

We maintain our BUY rating on Tabreed with a target price of AED 3.50. The Company reported substantial growth in revenue due to the addition of new customers and projects during 1Q23 with new customer connection of 12,000 Refrigerated Tons (RT), out of which 11,000 RT in the UAE and 1,000 RT in Oman. The Company further plans to add 120 thousand RT of capacity in 2023-24, of which consolidated entities are expected to contribute 60% while equity-accounted entities contribute the remaining 40%. Tabreed added 12.2k RT capacity in 1Q23, which included 11.3k RT in UAE and the remaining 0.9k RT in Oman. Tabreed incurred a capex of AED 17 Mn in 1Q23 spent towards the ongoing construction of the plant while we further expect the capex to increase during 2023 attributable to the Company's expansion strategy. The Company is working in four countries including a huge network of 86 operating plants and delivered 1.27 Mn RT to its clients in 1Q23 and further aims to expand in India and Egypt. Since 2020, the group's revenue grew at a CAGR of 16%, driven by significant growth in the chilled water segment and supported by the utility business, resulting in a continuous increase in revenue and profitability from existing clients. Furthermore, the company recorded an average EBITDA margin of 61% from 2020 to 2023 and we expect the margins to stay higher due to strong revenue visibility. In addition, out of a total contract, approximately 81% of contracted capacity is locked in for more than 10 years providing strong revenue and cash flow visibility. Furthermore, the Company earns 80% of its revenue from wholly and partially government-owned entities. Moreover, Tabreed signed an agreement with the Saudi Public Investment Fund (PIF) with a 30% stake indicating the Company's ongoing focus on high-potential growth markets. The Company's Board of Directors also announced a cash dividend of 13.5 fils per share in 1Q23 expecting a dividend yield of 4.8% in 2023. Thus, based on the aforementioned factors, we assign a 'BUY' rating to the stock.

### Tabreed - Relative valuation

(at CMP)	2018	2019	2020	2021	2022	2023F
P/E (x)	18.0	16.3	14.0	13.8	13.4	12.3
P/B (x)	1.7	1.6	1.6	1.4	1.2	1.3
EV/EBITDA (x)	15.9	14.1	14.3	14.2	11.4	10.6
Dividend Yield (%)	3.3%	3.7%	2.0%	2.1%	4.7%	4.8%

FABS Estimates & Co Data

### Tabreed - P&L

AED mm	1Q22	4Q22	1Q23	1Q23F	Var.	YOY Ch	QOQ Ch	2022	2023F	Change
Revenue	420	557	464	464	-0.1%	10.4%	-16.7%	2,216	2,465	11.2%
Operating costs	-206	-299	-224	-223	0.6%	8.7%	-25.1%	-1,178	-1,282	8.8%
<b>Gross profit</b>	<b>214</b>	<b>257</b>	<b>240</b>	<b>241</b>	<b>-0.8%</b>	<b>12.1%</b>	<b>-6.9%</b>	<b>1,038</b>	<b>1,183</b>	<b>14.0%</b>
Admin and other exps	-60	-55	-68	-46	45.5%	12.4%	23.6%	-245	-283	15.6%
<b>EBITDA</b>	<b>264</b>	<b>320</b>	<b>268</b>	<b>312</b>	<b>-14.2%</b>	<b>1.7%</b>	<b>-16.3%</b>	<b>1,232</b>	<b>1,354</b>	<b>9.9%</b>
<b>Operating profit/ EBIT</b>	<b>154</b>	<b>203</b>	<b>172</b>	<b>195</b>	<b>-11.8%</b>	<b>11.9%</b>	<b>-15.1%</b>	<b>793</b>	<b>900</b>	<b>13.5%</b>
Finance costs	-72	-73	-74	-84	-11.8%	1.9%	1.3%	-289	-335	15.7%
Finance income	1	13	16	12	31.4%	NM	24.9%	22	49	127.2%
Other gains and losses	0	57	119	10	NM	NM	110.1%	70	40	-42.6%
Share of associates & JV	11	2	9	11	-14.5%	-14.5%	NM	30	30	0.0%
<b>Profit from cont operat</b>	<b>93</b>	<b>210</b>	<b>242</b>	<b>144</b>	<b>68.3%</b>	<b>159.8%</b>	<b>15.5%</b>	<b>633</b>	<b>684</b>	<b>7.9%</b>
Profit from disconti operat	0	0	0	0	NM	NM	NM	0	0	NM
<b>Profit before NCI</b>	<b>93</b>	<b>210</b>	<b>242</b>	<b>144</b>	<b>68.3%</b>	<b>159.8%</b>	<b>15.5%</b>	<b>633</b>	<b>684</b>	<b>7.9%</b>
Non-controlling interest	-5	-9	-6	-2	NM	19.1%	-35.1%	-33	-29	-13.8%
<b>Net Profit</b>	<b>88</b>	<b>201</b>	<b>236</b>	<b>142</b>	<b>66.4%</b>	<b>168.0%</b>	<b>17.8%</b>	<b>600</b>	<b>655</b>	<b>9.1%</b>

#### Tabreed - Margins

	1Q22	4Q22	1Q23	YOY Ch	QOQ Ch	2022	2023F	Change
GPM	50.9%	46.2%	51.7%	76	543	46.8%	48.0%	115
EBITDA	62.8%	57.5%	57.8%	-498	31	55.6%	52.7%	-291
OPM	36.6%	36.4%	37.1%	50	68	35.8%	36.5%	71
Net margin	21.0%	36.0%	51.0%	2,997	1,494	27.1%	26.6%	-51

FABS estimate & Co Data

## Valuation:

We use Discounted Cash Flow (DCF) and Relative Valuation (RV) method to value Tabreed. We have assigned 70% weight to DCF and 30% weight to RV method.

Valuation Method	Target	Weight	Weighted Value
DCF	3.53	70.0%	2.47
Relative Valuation	3.44	30.0%	1.03
<b>Weighted Average Valuation (AED)</b>			<b>3.50</b>
<b>Current market price (AED)</b>			<b>2.89</b>
<b>Upside/Downside (%)</b>			<b>+21.1%</b>

### 1) DCF Method:

Tabreed is valued using free cash flow to firm. We have discounted the cash flow using the weighted average cost of capital of 7.3%. It is arrived after using cost of equity of 8.2% and cost of debt of 6.0% with debt to equity ratio of 78.3%. Cost of equity is calculated by using 10-year government bond yield of 4.7%, beta of 1.00 and equity risk premium of 3.5%. Government bond yield is calculated after adding Dubai 10-year spread over 10-year US risk free rate. Cost of debt is calculated using cost of 6.0% without adjusting tax rate. Also, assumed a terminal growth rate of 1.5%.

Sum of PV (AED, Mn)	3,830
Terminal value (AED, Mn)	12,317
<b>FV to Common shareholders (AED, Mn)</b>	<b>10,034</b>
No. of share (Mn)	2,842
Current Market Price (AED)	2.89
<b>Fair Value per share (AED)</b>	<b>3.53</b>

#### DCF method

(All Figures in AED Mn)	FY 2023E	FY 2024E	FY 2025E	FY 2026E	FY 2027E
NOPAT	900	933	995	1,045	1,082
D&A	311	309	310	310	314
Change in Working Capital	-144	-22	-52	-36	-43
(-) Capex	-247	-293	-317	-369	-388
<b>Free Cash Flow to Firm (FCFF)</b>	<b>819</b>	<b>927</b>	<b>936</b>	<b>951</b>	<b>964</b>
Discounting Factor	0.96	0.89	0.83	0.78	0.72
<b>Discounted FCFF</b>	<b>785</b>	<b>828</b>	<b>780</b>	<b>738</b>	<b>698</b>

## 2) Relative Valuation:

We have used Utilities Companies multiple to value Tabreed as there is only one pure-play company listed in the region. It is valued at EV/EBITDA multiple in line with Emirates Cooling Company. It is valued at EV/EBITDA of 12.2x.

Company	Market (USD Mn)	EV/EBITDA (x)		PE (x)	
		2023	2024	2023	2024
Qatar Electricity and Water Company QPSC	5,333	20.1	-	14.0	13.7
Essential Utilities, Inc.	12,519	17.3	16.3	25.1	23.3
SJW Group	2,462	16.4	15.7	32.3	29.6
Abu Dhabi National Energy Company PJSC	107,000	-	20.4	31.3	29.6
SHENZHEN ENVICOOL	2,099	-	24.3	41.4	29.8
Engie	34,994	4.5	4.5	8.2	8.0
Veolia	18,938	5.4	5.2	12.6	12.6
Drax	3,394	3.1	2.1	6.6	5.2
ESSENTIAL UTILITIES, INC.	12,519	17.3	16.3	25.1	23.3
American Water Works Company	27,714	-	17.2	31.9	29.5
Emirates Central Cooling Systems Corporation	15,500	12.4	11.5	-	-
<b>Average</b>		12.1x	13.4x	22.8x	20.5x
<b>Median</b>		14.4x	16.0x	25.1x	23.3x
<b>Max</b>		17.3x	17.0x	31.8x	29.6x
<b>Min</b>		5.2x	6.8x	13.0x	12.9x

**Research Rating Methodology:**

Rating	Upside/Downside potential
BUY	Higher than +15%
ACCUMULATE	Between +10% to +15%
HOLD	Lower than +10% to -5%
REDUCE	Between -5% to -15%
SELL	Lower than -15%

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