

National Central Cooling Company (Tabreed)

Higher cost base impacted bottom line

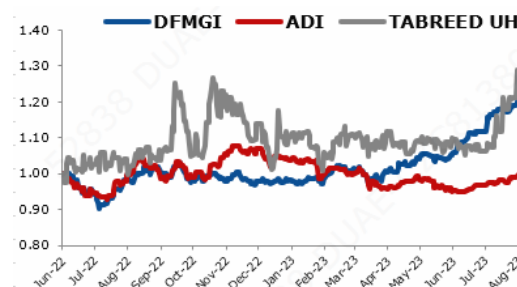
Current Price
AED 3.21

Target Price
AED 3.50

Upside/Downside (%)
+9.0%

Rating
HOLD

- Tabreed continued its geographical diversification with its first successful acquisition in India for AED 44.3 Mn. It acquired cooling infrastructure assets serving Intellion Park, a real estate asset by TATA Realty in Gurugram.
- Added 34k refrigeration tonnes (RT) capacity in 1H23 and plans to 120k RT capacity during 2023 & 2024
- Out of a total addition of 34K RT, 18K RT in UAE, 14k RT in KSA and the remaining 1k RT each in Bahrain and Oman.
- Tabreed's gross and EBITDA margins contracted majorly due to a rise in operating costs.
- Tabreed expands its global portfolio with the commissioning of 3 New Plants in UAE and Saudi Arabia, with a capacity of 17.7k RT.



Stock Information

| | |
|---------------------------|-----------|
| Market Cap (AED, mm) | 9,133.32 |
| Paid Up Capital (mm) | 2,845.27 |
| 52 Week High | 3.52 |
| 52 Week Low | 2.67 |
| 3M Avg. daily value (AED) | 2,944,458 |

2Q23 Net Profit lower than our estimate

National Central Cooling Company (Tabreed/The Company) reported net profit of AED 150 Mn declined marginally 1.4% YOY in 2Q23, lower than our estimate of AED 183 Mn. Net profit excluding other gains and losses stood at AED 162 Mn in 2Q23. The decline in net profit is mainly attributable to outsized increase in cost of sales as compared to revenue partially offset by a rise in topline.

P&L Highlights

Tabreed's revenue rose 8.6% YOY to AED 604 Mn in 2Q23 mainly driven by a growth in revenue of Chilled Water and Value Chain business. Revenue from the chilled water segment rose 7.1% YOY owing to the increase in connection, positive CPI and higher consumption volume. Tabreed's, total capacity rose from 1.24 Mn refrigeration tones (RT) in 2Q22 to 1.30 Mn RT in 2Q23. UAE's capacity rose from 1.04 Mn RT in 2Q22 to 1.08 Mn RT in 2Q23, whereas capacity in Oman increased from 51 thousand RT in 2Q22 to 53 thousand RT in 2Q23, Bahrain increased from 34 kRT in 2Q22 to 35 kRT in 2Q23. Revenue from the chilled water segment rose 7.1% YOY to AED 579 Mn in 2Q23. The Company generated around 96% revenue from the chilled water segment. While the remaining revenue was contributed by the value chain business, which rose 60.7% YOY to AED 24 Mn in 2Q23. Tabreed's cost of revenue grew 18.9% YOY to AED 317 Mn in 2Q23. Thus, gross profit declined marginally 0.8% YOY to AED 287 Mn in 2Q23 with a decline in gross profit margin by 452 bps YOY to 47.5% in 2Q23. Furthermore, Tabreed's operating expenses decreased 2.3% YOY to AED 65 Mn in 2Q23. Tabreed's EBITDA fell marginally 1.1% YOY to AED 322 Mn in 2Q23 with an EBITDA margin of 53.3% in 2Q23 as compared to 58.6% in 2Q22. Operating profit fell 0.4% YOY to AED 222 Mn in 2Q23 with an operating margin of 36.8% in 2Q23 as compared to 40.1% in 2Q22. Finance cost declined 5.1% YOY to AED 69 Mn in 2Q23 while finance

2Q23 Result Review (AED, mm)

| | |
|-------------------|--------|
| Total Assets | 14,696 |
| Total Liabilities | 7,689 |
| Total Equity | 7,007 |
| EBITDA | 322 |
| Net Profit | 150 |

Financial Ratios

| | |
|-------------------------|-------|
| Dividend Yield (12m) | 4.21 |
| Dividend Pay-out (%) | 63.93 |
| Price-Earnings Ratio(x) | 12.23 |
| Price-to-Book Ratio (x) | 1.44 |
| Book Value (AED) | 2.23 |
| Return-on Equity (%) | 12.06 |

Stock Performance

| | |
|------------------------|--------|
| 5 Days | -4.75% |
| 1 Months | 8.45% |
| 3 Months | 9.18% |
| 6 Months | 9.93% |
| 1 Year | 14.23% |
| Month to Date (MTD%) | -6.96% |
| Quarter to Date (QTD%) | 12.63% |
| Year to Date (YTD%) | 8.45% |

income rose significantly from AED 2 Mn in 2Q22 to AED 12 Mn in 2Q23. Other gains and losses stood at a loss of AED 12 Mn in 2Q23 as compared to income of AED 1 Mn in 2Q22. Share of associates and JVs declined by 1.1% YOY to AED 8 Mn in 2Q23. However, the share of profit attributable to non-controlling interest holders rose 4.1% YOY to AED 9 Mn in 2Q23.

Balance Sheet Highlights

Tabreed's cash and cash equivalents stood at AED 1,192 Mn in 2Q23 as compared to AED 1,389 Mn in 1Q23. 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 grew to AED 386 Mn in 2Q23 as compared to AED 206 Mn in 2Q22. The Company's gross debt stood at AED 6,457 Mn in 2Q23 unchanged as compared to 1Q23. The Company's net debt to LTM EBITDA stood at 4.43 in 1H23 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.

Target Price and Rating

We revise our rating from BUY to HOLD on Tabreed with an unchanged target price of AED 3.50. The Company share price rose 12.7% since our last rating on 24 May 2023. The Company reported healthy growth in revenue due to the increased connection and higher consumption during 2Q23. Further, Tabreed attracted new customers and commissioned one new plant in UAE and two new plants in KSA with total capacity of 17.7k RT. Meanwhile, Tabreed added a new capacity of 33,483 Refrigerated Tons (RT), in UAE, Bahrain, Saudi Arabia and Oman and increased the total connected capacity to 1.30 Mn RT. The Company further plans to add 120 thousand RT of capacity in 2023-24 out of 34k RT has already been delivered in 1H23, of which consolidated entities are expected to contribute 60% while equity-accounted entities contribute the remaining 40%. Further, Tabreed added 22k RT capacity in 2Q23. During 2Q23, the Company incurred a total capex of AED 59.6 Mn, 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. Moreover, Tabreed is working in five countries including a network of 89 operating plants and delivered 1.30 Mn RT to its clients in 2Q23 and further aims to expand in new geographies of Egypt. Tabreed continued its geographical diversification with its first successful acquisition in India for AED 44.3 Mn. It acquired cooling infrastructure assets serving Intellion Park, a real estate asset by TATA Realty in Gurugram. The move reflects Tabreed's commitment to expanding its international portfolio and underscores its dedication to fostering growth and excellence in its ventures. In addition, Tabreed contracted approximately 81% of its capacity is locked into long-term contracts for more than 10 years providing strong revenue and cash flow visibility. Furthermore, the Company earns around 80% of its revenue from wholly and partially government-owned entities. High level of debt in a rising interest rate environment makes us turn cautious on the name with net debt-to-EBITDA ratio of 4.4x in 2Q23. Thus, based on the aforementioned factors, we assign a 'HOLD' rating to the stock.

Tabreed - Relative valuation

| (at CMP) | 2,018 | 2,019 | 2,020 | 2,021 | 2,022 | 2023F |
|----------------|-------|-------|-------|-------|-------|-------|
| PE | 20.6 | 18.7 | 16.0 | 15.8 | 15.4 | 12.0 |
| PB | 2.0 | 1.9 | 1.8 | 1.6 | 1.4 | 1.5 |
| EV/EBITDA | 17.6 | 15.6 | 15.5 | 15.3 | 12.4 | 11.7 |
| Dividend yield | 2.9% | 3.2% | 1.8% | 1.8% | 4.2% | 4.3% |

FABS Estimates & Co Data

Tabreed – P&L

| AED mm | 2Q22 | 1Q23 | 2Q23 | 2Q23F | Var. | YOY Ch | QOQ Ch | 2022 | 2023F | Change |
|-----------------------------------|------------|------------|------------|------------|---------------|--------------|---------------|--------------|--------------|--------------|
| Revenue | 556 | 464 | 604 | 598 | 1% | 8.6% | 30.2% | 2,216 | 2,465 | 11.2% |
| Operating costs | -267 | -224 | -317 | -281 | 13% | 18.9% | 41.4% | -1,178 | -1,282 | 8.8% |
| Gross profit | 289 | 240 | 287 | 317 | -10% | -0.8% | 19.8% | 1,038 | 1,183 | 14.0% |
| Admin and other expenses | -66 | -68 | -65 | -75 | -13% | -2.3% | -4.1% | -245 | -283 | 15.6% |
| EBITDA | 326 | 268 | 322 | 342 | -6% | -1.1% | 20.1% | 1,232 | 1,299 | 5.4% |
| Operating profit/EBIT | 223 | 172 | 222 | 242 | -8% | -0.4% | 29.1% | 793 | 900 | 13.5% |
| Finance costs | -73 | -74 | -69 | -74 | -7% | -5.1% | -6.0% | -289 | -297 | 2.8% |
| Finance income | 2 | 16 | 11 | 17 | -35% | 393.9% | -32.7% | 22 | 62 | 183.9% |
| Other gains and losses | 1 | 119 | -12 | 0 | NM | NM | -110.4% | 70 | 107 | 53.2% |
| Share of associates & JV | 8 | 9 | 8 | 8 | -1% | -1.1% | -8.1% | 30 | 30 | 0.0% |
| Profit from cont operation | 161 | 242 | 159 | 193 | -17% | -1.1% | -34.3% | 633 | 800 | 26.3% |
| Profit from discount. operation | 0 | 0 | 0 | 0 | NM | NM | NM | 0 | 0 | NM |
| Profit before NCI | 161 | 242 | 159 | 193 | -17% | -1.1% | -34.3% | 633 | 800 | 26.3% |
| Non-controlling interest | -9 | -6 | -9 | -10 | -6% | 4.1% | 53.8% | -33 | -34 | 0.9% |
| Net Profit | 152 | 236 | 150 | 183 | -18.0% | -1.4% | -36.5% | 600 | 767 | 27.8% |

FABS estimate & Co Data

Tabreed - Margins

| | 2Q22 | 1Q23 | 2Q23 | YOY Ch | QOQ Ch | 2022 | 2023F | Change |
|-------------------|-------|-------|-------|--------|--------|-------|-------|--------|
| Gross margin | 43.3% | 43.2% | 48.9% | 563 | 568 | 43.6% | 44.5% | 90 |
| EBITDA margin | 40.4% | 39.7% | 45.3% | 495 | 563 | 40.3% | 41.3% | 103 |
| Operating margin | 24.0% | 24.8% | 27.6% | 355 | 277 | 23.7% | 25.5% | 174 |
| Net profit margin | 9.7% | 10.8% | 11.9% | 222 | 110 | 9.6% | 11.0% | 142 |

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 Method | 3.61 | 70.0% | 2.53 |
| EV/EBITDA | 3.26 | 30.0% | 0.98 |
| Weighted Average Valuation (AED) | | | 3.50 |
| Current market price (AED) | | | 3.21 |
| Upside/Downside (%) | | | +9.0% |

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 69.9%. Cost of equity is calculated by using 10-year government bond yield of 5.1%, beta of 1.00 and equity risk premium of 3.1%. 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) | 3,901 |
| Terminal value (AED, Mn) | 12,486 |
| FV to Common shareholders (AED, Mn) | 10,251 |
| No. of share (Mn) | 2,842 |
| Current Market Price (AED) | 3.21 |
| Fair Value per share (AED) | 3.61 |

DCF Method

| (All Figures in AED Mn) | FY 2023E | FY 2024E | FY 2025E | FY 2026E | FY 2027E |
|--------------------------------------|------------|------------|------------|------------|------------|
| NOPAT | 900 | 938 | 1,000 | 1,054 | 1,091 |
| D&A | 311 | 309 | 310 | 310 | 314 |
| Change in working capital | -144 | -25 | -52 | -38 | -44 |
| (-) Capex | -247 | -293 | -317 | -369 | -388 |
| Free Cash Flow to Firm (FCFF) | 819 | 929 | 941 | 958 | 974 |
| Discounting Factor | 0.97 | 0.91 | 0.84 | 0.79 | 0.73 |
| Discounted FCFF | 797 | 841 | 795 | 754 | 714 |

Source: FAB Securities

2) Relative Valuation:

We have used Utilities Companies multiple to value Tabreed as there is only one pure-play company is listed in the region. It is valued at EV/EBITDA multiple by applying a discount of 25% to get a valuation in line. It is valued at EV/EBITDA of 11.9x.

| Company | Market (USD Mn) | EV/EBITDA (x) | | P/E (x) | |
|--|--------------------|---------------|--------------|--------------|--------------|
| | | 2023F | 2024F | 2023F | 2024F |
| Qatar Electricity and Water Company QPSC | 5,482 | 20.8 | 18.9 | 12.7 | 12.4 |
| Essential Utilities, Inc. | 11,141 | 16.2 | 14.6 | 22.6 | 20.8 |
| SJW Group | 2,220 | 15.7 | 14.9 | 28.6 | 26.0 |
| Abu Dhabi National Energy Company PJSC | 99,488 | 12.9 | 19.3 | - | 37.8 |
| SHENZHEN ENVICOOL | 2,254 | 32.5 | 23.6 | 40.1 | 30.2 |
| Engie | 39,990 | 4.7 | 5.2 | 8.3 | 8.5 |
| Veolia | 23,045 | 6.2 | 5.8 | 19.3 | 15.9 |
| Drax | 2,993 | 3.1 | 2.3 | 5.6 | 4.4 |
| ESSENTIAL UTILITIES, INC. | 11,141 | 16.2 | 14.6 | 22.6 | 20.8 |
| American Water Works Company | 28,605 | 18.7 | 17.5 | 30.6 | 28.6 |
| Emirates Central Cooling Systems Corporation | 5,146 | 15.8 | 14.1 | 20.4 | 20.2 |
| Average | | 14.8x | 13.7x | 21.1x | 20.5x |
| Median | | 15.8x | 14.6x | 21.5x | 20.8x |
| Max | | 17.5x | 18.2x | 27.1x | 27.3x |
| Min | | 9.5x | 10.0x | 14.4x | 14.2x |

Source: FAB Securities

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% |

FAB Securities Contacts:

Research Analyst

Ahmad Banihani +971-2-6161629 ahmad.banihani@Bankfab.com

Sales & Execution

Abu Dhabi Head Office

Trading Desk +971-2-6161700/1 Online Trading Link

+971-2-6161777

Institutional Desk +971-4-4245765

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