

TECOM Group

High occupancy and rental rates with one-off income drove profitability

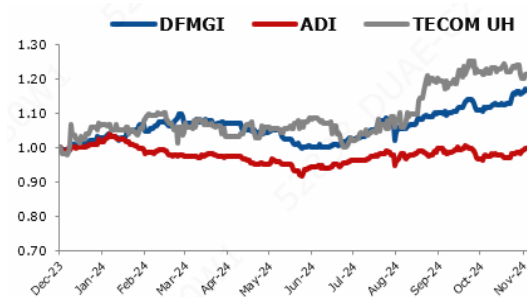
Current Price
AED 3.14

Target Price
AED 3.45

Upside/Downside (%)
+9.9%

Rating
HOLD

- TECOM's client base grew 9% YOY to more than 11,800 in 9M24, with the addition of more than 1,000 new customers including OZON Pharmaceuticals and Hisense
- TECOM experienced a strong occupancy of 90% in the Commercial segment and 98% in the Industrial leasing segment in 3Q24.
- The Company acquired a Grade A office building with a GLA of c. 371K square feet for AED 720 Mn and 73 industrial plots spanning 13.9 Mn square feet for AED 410 Mn in 9M24
- TECOM also plans to develop Innovation Hub Phase 3 with a GLA of c. 167K square feet in Dubai Internet City with a capex of AED 283 Mn
- The Company distributed an interim dividend of AED 400 Mn for 1H24.



Stock Information

Market Cap (AED, mn)	15,650.00
Shares Outstanding (mn)	5,000.00
52 Week High	3.30
52 Week Low	2.53
3M Avg. daily value (AED)	1,211,268

3Q24 Result Review (AED, Mn)

Total Assets	15,511
Total Liabilities	9,120
Total Equity	6,392
EBITDA	500
Net Profit	340

Financial Ratios

Dividend Yield (12m)	5.11
Dividend Pay-out (%)	74.19
Price-Earnings Ratio(x)	12.52
Price-to-Book Ratio (x)	2.45
Book Value (AED)	1.28
Return-on Equity (%)	20.00

Stock Performance

5 Days	-1.57%
1 Months	-1.88%
3 Months	9.82%
6 Months	14.23%
1 Year	20.38%
Month to Date (MTD%)	-2.19%
Quarter to Date (QTD%)	-2.49%
Year to Date (YTD%)	13.82%

3Q24 Net Profit higher than our estimate

TECOM Group PJSC (TECOM/the Company) net profit increased 20.0% YOY to AED 340 Mn in 3Q24 higher than our estimate of AED 312 Mn. The increase in net profit is primarily attributable to healthy revenue growth and one-time earnings from lease termination, partially offset by a rise in direct cost, higher operating & finance expenses, and tax expenses.

P&L Highlights

TECOM's revenue increased by 12.3% YOY to AED 611 Mn in 3Q24, led by new customers, solid occupancy levels, rental rates, and a healthy retention rate coupled with strong demand across all segments. Commercial Leasing segment revenue increased 12.9% YOY to AED 317 Mn in 3Q24, primarily due to new leases, rise in rental rates, and higher retention. Similarly, the Industrial Leasing segment revenue grew 19.3% YOY to AED 91 Mn in 3Q24, owing to increased leasing across warehouses and workers accommodation which pushed the occupancy rates higher. Furthermore, revenue from land leasing climbed 6.2% YOY to AED 130 Mn in 3Q24, primarily from new leases, healthy retention, and higher rental rates. The overall occupancy of the land leasing segment grew 9% YOY excluding new additions. Services income increased 13.0% YOY to AED 73 Mn in 3Q24, mainly due to high AXS sales attributable to new visa from increasing demand for co-working spaces. However, direct costs increased 13.2% YOY to AED 232 Mn in 3Q24. As a result, the Company's gross profit rose 11.8% YOY to AED 379 Mn in 3Q24. TECOM's G&A expenses nearly doubled from AED 28 Mn in 3Q23 to AED 56 Mn in 3Q24, while selling and marketing expenses increased 33.3% YOY to AED 9 Mn. Furthermore, other income grew from AED 8 Mn in 3Q23 to AED 76 Mn in 3Q24 due to repossession of partially constructed structures because of lease termination and reflects value adjustment according to the Company's accounting policy.

Resultantly, operating profit increased 25.0% YOY to AED 391 Mn in 3Q24. Moreover, the Commercial leasing segment EBITDA grew 10.7% YOY to AED 199 Mn in 3Q24, while the Industrial leasing segment EBITDA rose 17.1% YOY to AED 59 Mn. Similarly, Service segment EBITDA improved by 2.3% YOY to AED 57 Mn in 3Q24. Besides, EBITDA from Land Leasing grew 49.0% YOY to AED 184 Mn in 3Q24. The company's overall EBITDA increased by 21.9% YOY to AED 500 Mn, with an EBITDA margin of 81.8% in 3Q24 compared to 75.3% in 3Q23. TECOM's finance income remained at AED 16 Mn in 3Q24, while finance cost rose 19.6% YOY to AED 54 Mn in 3Q24. The Company recorded income tax expense of AED 13 Mn in 3Q24.

Balance Sheet Highlights

TECOM's borrowings remained at AED 4.6 Bn in 3Q24 compared to 2Q24, excluding AED 2.9 Bn in committed undrawn floating rate bank borrowing. The Company's funds from operations rose by 20% YOY to AED 1,265 Mn in 9M24 excluding restricted cash of AED 270 Mn from visa deposits and EOSB, supported by improved service conditions, healthy collections, and improvement in customer quality. Furthermore, TECOM's recurring free cash flow grew 22.3% YOY to AED 1,080 Mn in 9M24 due to lower capex investment and improved collections. The Company incurred AED 185 Mn in maintenance capex and AED 854 Mn in growth expenditure during 9M24 due to rise in acquisitions and completion of development projects.

Target Price and Rating

We maintain our HOLD rating on TECOM with a revised target price of AED 3.45. TECOM's performance is being driven by strong demand and increasing rental rates in both commercial and residential properties. Dubai is emerging as a global business hub, with companies worldwide setting up production units and offices in the emirate, drawn by supportive government policies. As a result, the Company anticipates increased demand for office spaces in the near future, driven by limited supply and a growing number of businesses. Such a positive outlook for commercial real estate underpins strong growth momentum. The favorable market conditions are expected to maintain demand and high occupancy levels across the Company's portfolio. Additionally, strong property price growth and high rental rates have contributed to significant appreciation in TECOM's portfolio. TECOM's customer base increased 9% YOY to more than 11,800 in 9M24, with the addition of more than 1,000 new customers including global industry leaders such as OZON Pharmaceuticals and Hisense. To capitalize on the positive business environment and increasing demand, TECOM Investment FZ LLC, a TECOM Group subsidiary, acquired a Grade A office building with a GLA of c. 371K square feet in the Dubai Internet City for AED 720 Mn. The acquisition will have an immediate impact on revenue in 4Q24. Besides, TECOM also plans to develop Innovation Hub Phase 3 with a GLA of c. 167K square feet in Dubai Internet City with a capex of AED 283 Mn, since Phase 1 is fully occupied and Phase 2 will be completed in the short term which is expected to be 100% leased after handover. Additionally, the Company has started the development of a new warehouse with a GLA of c. 200k square feet in Dubai Science Park with a capex of AED 75 Mn, since existing warehouses are fully occupied. TECOM Investment FZ LLC, a TECOM Group subsidiary, also acquired two Grade A office buildings with GLA of c. 334K square feet in the Dubai Internet City for a consideration of AED 420 Mn. Moreover, the Company also acquired 73 plots across Dubai Industrial City spanning 13.9 Mn square feet for a consideration of AED 410 Mn. The acquisitions are expected to positively benefit the Group's financial performance and strengthen its commercial asset portfolio. TECOM also announced Phase 2 of Dubai Design District (d3, Design Quarter) with commercial and residential components. For the d3 project, the Company acquired the volumetric GFA for commercial components for AED 136 Mn and plans to invest AED 690 Mn in the d3 project, which is planned to be completed in FY2027. The Company distributed an interim cash dividend of AED 400 Mn for 1H24. Thus, considering the abovementioned factors, we maintained our HOLD rating on the stock.

TECOM - Relative valuation

(at CMP)	2019	2020	2021	2022	2023	2024F
PE	24.78	27.11	20.87	16.36	14.56	12.61
PB	0.96	1.08	0.80	0.78	1.00	1.03
EV/EBITDA	16.33	16.93	13.68	12.46	12.29	10.92
Dividend yield	9.4%	4.1%	11.8%	11.0%	5.1%	5.1%

FABS Estimates & Co Data

TECOM – P&L

AED Mn	3Q23	2Q24	3Q24	3Q24F	Var	YOY Ch	QOQ Ch	2023	2024F	Change
Sales	544	584	611	586	4.2%	12.3%	4.7%	2,169	2,375	9.5%
Direct cost	-205	-191	-232	-189	23.0%	13.2%	21.6%	-760	-812	6.7%
Gross profit	339	393	379	398	-4.7%	11.8%	-3.6%	1,409	1,563	11.0%
G&A expenses	-28	-51	-56	-34	65.6%	99.6%	8.5%	-154	-205	32.8%
Marketing & selling exp.	-7	-11	-9	-11	-18.8%	33.3%	-20.5%	-43	-40	-6.4%
Other income	8	23	76	12	NM	NM	NM	47	125	164.9%
Other expenses	0	0	0	-6	NM	NM	NM	0	-7	NM
Operating profit	313	354	391	359	8.8%	25.0%	10.5%	1,259	1,436	14.1%
Depr. & Amort	97	103	109	107	1.9%	11.9%	5.7%	395	416	5.6%
EBITDA	410	457	500	466	7.2%	21.9%	9.4%	1,654	1,853	12.1%
Finance income	16	19	16	20	-18.4%	3.8%	-14.2%	82	72	-11.8%
Finance cost	-45	-56	-54	-55	-1.2%	19.6%	-3.7%	-262	-220	-16.2%
Profit before zakat	283	316	353	324	8.8%	24.7%	11.5%	1,078	1,289	19.5%
Income Tax	0	-6	-13	-12	7.7%	NM	124.8%	0	-44	NM
Net Profit	283	311	340	312	8.9%	20.0%	9.4%	1,078	1,245	15.4%

FABS estimate & Co Data

TECOM - Margins

	3Q23	2Q24	3Q24	YOY Ch	QOQ Ch	2023	2024F	Change
Gross margin	62.3%	67.3%	62.0%	-28	-529	64.9%	65.8%	88
EBITDA margin	75.3%	78.2%	81.8%	643	355	76.2%	78.0%	179
Operating margin	57.5%	60.6%	63.9%	650	337	58.0%	60.5%	244
Net profit margin	52.0%	53.2%	55.6%	356	240	49.7%	52.4%	270

FABS estimate & Co Data

Valuation:

We use Discounted Free Cash flow (DCF), Dividend Discount Method (DDM), and Price/Funds From Operations (FFO) method to value TECOM. We have assigned 70% weight to DCF, and 15% each to DDM and Price/FFO method.

Valuation Method	Target	Weight	Weighted Value
DCF Method	3.23	70.0%	2.26
Dividend Discount Method (RV)	2.73	15.0%	0.41
Price/ FFO	5.17	15.0%	0.78
Weighted Average Valuation (AED)			3.45
Current market price (AED)			3.14
Upside/Downside (%)			+9.9%

1) DCF Method:

TECOM is valued using free cash flow to the firm. We have discounted the cash flow using the weighted average cost of capital of 8.5%. It is arrived after using the cost of equity of 9.3% and after-tax cost of debt of 6.5% with a debt-to-equity ratio of 34.8%. The cost of equity is calculated by using a 10-year government bond yield of 5.3%, beta of 1.00 and equity risk premium of 4.0%. Government bond yield is calculated after adding Dubai 10-year spread over a 10-year US risk-free rate. The cost of debt is calculated using the cost of 6.7% after adjusting a tax rate arriving at after-tax cost of debt of 6.5%. Also, it assumed a terminal growth rate of 2.0%.

Sum of PV (AED, Mn)	4,822
Terminal value (AED, Mn)	15,693
FV to Common shareholders (AED, Mn)	20,515
No. of share (Mn)	5,000
Current Market Price (AED)	3.14
Fair Value per share (AED)	3.23

DCF Method

(All Figures in AED Mn)	FY 2024E	FY 2025E	FY 2026E	FY 2027E	FY 2028E
NOPAT	1,402	1,342	1,387	1,457	1,509
D&A	407	452	465	471	480
(-) Capex	-1,673	-334	-280	-481	-583
Change in working capital	-139	40	8	7	7
Free Cash Flow to Firm (FCFF)	(4)	1,500	1,579	1,453	1,413
Discounting Factor	0.99	0.91	0.84	0.77	0.71
Discounted FCFF	(1)¹	1,367	1,326	1,124	1,007

Source: FAB Securities, ¹Adjusted for partial year

2) DDM Method:

TECOM dividend grew in line with its policy and pays regular dividend to its shareholders. Strong cash flow generation of the Company enables continuous dividend payments. Thus, we have valued TECOM using DDM method. The dividend is discounted at the cost of equity of 9.3%

Sum of PV (AED, Mn)	3,885
Terminal value (AED, Mn)	9,762
FV to Common shareholders (AED, Mn)	13,648
No. of share (Mn)	5,000
Current Market Price (AED)	3.14
Fair Value per share (AED)	2.73

DDM Method

(All Figures in AED Mn)	FY 2024E	FY 2025E	FY 2026E	FY 2027E	FY 2028E
Dividend paid -					
H1	400	400	500	500	500
H2	400	500	500	500	500
Total dividend	800	900	1,000	1,000	1,000
Discounting Factor	0.99	0.90	0.83	0.76	0.69
Present Value of dividend	791	814	828	758	694

Source: FAB Securities

3) Price/FFO:

We have used local peers to value TECOM and it is valued using the Price/FFO multiple. It is valued at Price/FFO multiple of 15.0x in line with peers.

Company	Market (USD Mn)	EV/EBITDA (x) Current	PE (x) ¹ Current	Price/FFO (x)
Jadwa REIT Saudi Fund	551	12.2	14.5	18.6
Riyad REIT Fund	298	NA	20.3	42.9
Al Rajhi REIT	616	16.2	19.5	15.5
Bonyan REIT	400	13.5	11.3	11.3
Alahli REIT Fund 1	261	29.2	18.7	17.7
Derayah REIT	177	16.5	15.5	28.2
Mulkia Gulf Real Estate REIT	152	43.3	20.1	42.3
Taleem REIT	148	15.6	15.3	14.4
Al Maather REIT Fund	154	13.0	14.8	12.8
Average		19.9x	16.7x	22.6x
Median		15.9x	15.5x	17.7x
Max		19.6x	19.5x	28.2x
Min		13.4x	14.8x	14.4x

Source: FAB Securities, ¹Based on 9M24 Results

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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