

Air Arabia PJSC

Inflationary pressure and currency fluctuations impacted the bottom line

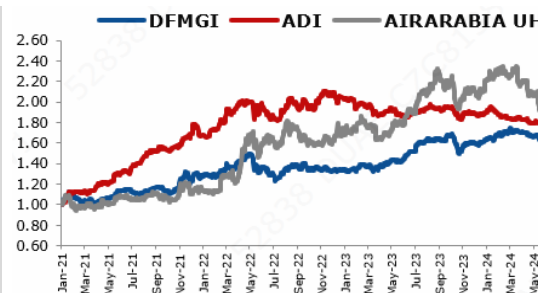
Current Price
AED 2.33

Target Price
AED 3.10

Upside/Downside (%)
+33%

Rating
BUY

- The Company served more than 4.4 Mn passengers in 1Q24 across seven hubs compared to 3.9 Mn passengers in 1Q23
- Seat load factor stood at 85.0% in 1Q24.
- Aviation industry continued to face cost challenges including, engines, spare parts, staffing and other issues, which resulted in higher costs across the industry.
- Air Arabia expanded its network by adding two new routes to its operating hubs in the UAE, Morocco, Egypt and Pakistan.
- AIRARABIA's direct cost rose 18.2% YOY to AED 1,219 Mn in 1Q24 mainly due to an increase in engine costs, spare part costs, and staff costs owing to ongoing supply chain disruptions and higher inflationary pressures.



1Q24 Net Profit lower than our estimate

Air Arabia's (AIRARABIA PJSC/the Company) net profit declined from AED 342 Mn in 1Q23 to AED 241 Mn in 1Q24, lower than our estimate of AED 296 Mn. The decline in the net profit is primarily due to a seasonality shift due to Ramadan, fuel price increase, currency volatility in major markets, and challenges related to the supply chain.

P&L Highlights

Air Arabia's revenue grew 7.8% YOY to AED 1,541 Mn in 1Q24 primarily driven by the robust passenger demand owing to a higher seat load factor. The Company served more than 4.4 Mn passengers in 1Q24 across seven hubs compared to 3.9 Mn passengers in 1Q23. The seat load factor remained unchanged at 85% in 1Q24., whereas the seat load factor stood at 85.0% in 1Q24. Moreover, AIRARABIA's direct cost rose 18.2% YOY to AED 1,219 Mn in 1Q24 mainly due to an increase in engine costs, spare part costs, and staff costs owing to ongoing supply chain disruptions and higher inflationary pressures. Thus, gross profit declined from AED 398 Mn in 1Q23 to AED 322 Mn in 1Q24. Gross profit margin declined from 27.8% in 1Q23 to 20.9% in 1Q24. Air Arabia's selling and marketing expenses rose 21.6% YOY to AED 24 Mn in 1Q24. While, G&A expenses fell 0.9% YOY to AED 76 Mn in 1Q24. The Company's EBITDA declined from AED 461 Mn in 1Q23 to AED 389 Mn in 1Q24 mainly due to higher direct costs and selling and marketing expenses partially offset by a decline in G&A expenses. Moreover, the EBITDA margin dropped from 32.3% in 1Q23 to 25.2% in 1Q24. Thus, the operating profit declined significantly from AED 301 Mn in 1Q23 to AED 222 Mn in 1Q24. The operating profit margin declined significantly from 21.1% in 1Q23 to 14.4% in 1Q24. Air Arabia's finance income grew from AED 41 Mn in 1Q23 to AED 61 Mn in 1Q24 due to higher benchmark rates whereas finance cost declined 6.7% YOY to AED 25 Mn in 1Q24 due to a decline in total debt including leases. Other income fell from AED 26 Mn in 1Q23 to

Stock Information

| | |
|---------------------------|------------|
| Market Cap (AED, mn) | 10,966.75 |
| Paid Up Capital (mn) | 4,666.70 |
| 52 Week High | 3.03 |
| 52 Week Low | 2.31 |
| 3M Avg. daily value (AED) | 10,566,750 |

1Q24 Result Review (AED, mn)

| | |
|-------------------|--------|
| Total Assets | 15,110 |
| Total Liabilities | 8,244 |
| Total Equity | 6,867 |
| EBITDA | 389 |
| Net Profit | 241 |

Financial Ratios

| | |
|-------------------------|-------|
| Dividend Yield (12m) | 8.51 |
| Dividend Pay-out (%) | 0.00 |
| Price-Earnings Ratio(x) | 7.63 |
| Price-to-Book Ratio (x) | 1.60 |
| Book Value (AED) | 1.47 |
| Return-on Equity (%) | 21.58 |

Stock Performance

| | |
|------------------------|---------|
| 5 Days | 0.43% |
| 1 Months | -10.98% |
| 3 Months | -18.40% |
| 6 Months | -11.65% |
| 1 Year | -1.67% |
| Month to Date (MTD%) | 1.73% |
| Quarter to Date (QTD%) | -15.77% |
| Year to Date (YTD%) | -16.67% |

AED 18 Mn in 1Q24. Share of loss on investments grew from a nil in 1Q23 to a loss of AED 11 Mn in 1Q24. Thus, profit before tax declined from AED 342 Mn in 1Q23 to AED 266 Mn in 1Q24. The income tax expense amounted to AED 25 Mn in 1Q24 owing to the introduction of corporate tax in the UAE impacting the bottom line.

Balance Sheet Highlights

Air Arabia's borrowings increased from AED 126 Mn in 4Q23 to AED 133 Mn in 1Q24. Lease liabilities fell marginally from AED 2.15 Bn in 4Q23 to AED 2.13 Bn in 1Q24. The Company's cash and bank balance fell to AED 5.0 Bn in 1Q24 compared to AED 5.2 Bn in 4Q23. Moreover, Air Arabia's net cash flow from operations fell from AED 657 Mn in 1Q23 to AED 342 Mn in 1Q24 owing to lower profitability and higher investment in working capital in 1Q24.

Target Price and Rating

We maintain our BUY rating on Air Arabia with a target price of AED 3.10. The Company remains a key beneficiary of a rebound in travel demand post-pandemic. Air Arabia's revenue grew 7.8% YoY to AED 1,541 Mn in 1Q24 due to an increase in the number of passengers from 3.9 Mn in 1Q23 to 4.4 Mn in 1Q24. The seat load factor remains unchanged at 85.0% in 1Q24. Air Arabia remained committed to diversifying and growing its operation, which is evident from the addition of two new routes to its network, including operating hubs in the UAE, Morocco, Egypt and Pakistan. The company operated 74 aircraft in service including 65 Airbus A320 and 9 Airbus A321 during 1Q24. Moreover, the management of AIRARABIA is dedicated to enhancing operational efficiency, lowering costs and increasing its passenger count through their multi-hub business model. The company's management focuses on effective fleet management, and new technologies to facilitate robust growth. In the near term, the aviation industry continues to face challenges including, engines, spare parts, staffing and other issues which result in higher costs across the industry. This continues to impact the Company's operation as well. The Company's board of directors proposed a cash dividend of 20 fils per share with a dividend yield of 8.5% in 2023. Hence, based on our analysis, we recommend a BUY rating on the stock.

Air Arabia - Relative valuation

| (at CMP) | 2019 | 2020 | 2021 | 2022 | 2023 | 2024F |
|----------------|------|------|------|------|------|-------|
| PE | 11.0 | NA | 15.1 | 8.9 | 7.0 | 7.7 |
| PB | 2.0 | 2.4 | 1.8 | 1.6 | 1.4 | 1.3 |
| EV/EBITDA | 5.7 | 20.1 | 5.6 | 3.7 | 3.1 | 3.1 |
| Dividend yield | 3.9% | NA | 3.6% | 6.4% | 8.5% | 8.5% |

FABS Estimates & Co Data

Air Arabia – P&L

| AED mn | 1Q23 | 4Q23 | 1Q24 | 1Q24F | Var. | YOY Ch | QOQ Ch | 2023 | 2024F | Change |
|----------------------------|------------|------------|------------|------------|---------------|---------------|--------------|--------------|--------------|--------------|
| Revenue | 1,429 | 1,545 | 1,541 | 1,501 | 2.7% | 7.8% | -0.3% | 6,000 | 6,450 | 7.5% |
| Direct costs | -1,032 | -1,192 | -1,219 | -1,155 | 5.5% | 18.2% | 2.3% | -4,343 | -4,674 | 7.6% |
| Gross profit | 398 | 353 | 322 | 345 | -6.8% | -19.1% | -8.9% | 1,657 | 1,776 | 7.2% |
| Selling & mkt expense | -20 | -26 | -24 | -23 | 7.2% | 21.6% | -8.0% | -89 | -97 | 9.0% |
| G&A expenses | -76 | -135 | -76 | -83 | -8.4% | -0.9% | -43.9% | -329 | -355 | 7.8% |
| EBITDA | 461 | 361 | 389 | 397 | -2.0% | -15.8% | 7.8% | 1,886 | 1,950 | 3.4% |
| EBIT | 301 | 192 | 222 | 240 | -7.5% | -26.4% | 15.4% | 1,239 | 1,325 | 7.0% |
| Finance income | 41 | 62 | 61 | 58 | 5.7% | 49.4% | -2.1% | 210 | 231 | 9.9% |
| Finance costs | -26 | -25 | -25 | -22 | 14.1% | -6.7% | -0.7% | -102 | -101 | -1.2% |
| Other income | 26 | 25 | 18 | 38 | -51.4% | -29.0% | -27.1% | 113 | 97 | -14.7% |
| Share of profit on eq invt | 0 | -30 | -11 | 12 | NM | NM | NM | 88 | 13 | -85.4% |
| Profit before NCI | 342 | 225 | 266 | 326 | -18.4% | -22.2% | 18.2% | 1,548 | 1,564 | 1.1% |
| Tax | 0 | 0 | -25 | -29 | -15.5% | NM | NM | 0 | -141 | NM |
| Non-controlling int. | 0 | 0 | 0 | 0 | NM | NM | NM | 1 | 0 | NM |
| Net Profit | 342 | 225 | 241 | 296 | -18.7% | -29.4% | 7.2% | 1,547 | 1,423 | -8.0% |

FABS estimate & Co Data

Air Arabia - Margins

| | 1Q23 | 4Q23 | 1Q24 | YOY Ch | QOQ Ch | 2023 | 2024F | Change |
|------------------|-------|-------|-------|--------|--------|-------|-------|--------|
| Gross Profit | 27.8% | 22.9% | 20.9% | -694 | -199 | 27.6% | 27.5% | -7 |
| EBITDA | 32.3% | 23.3% | 25.2% | -707 | 188 | 31.4% | 30.2% | -119 |
| Operating Profit | 21.1% | 12.5% | 14.4% | -668 | 195 | 20.6% | 20.5% | -10 |
| Net Profit | 23.9% | 14.6% | 15.6% | -826 | 109 | 25.8% | 22.1% | -372 |

FABS estimate & Co Data

Valuation:

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

| Valuation Method | Target | Weight | Weighted Value |
|---|--------|--------|----------------|
| DCF Method | 3.11 | 70.0% | 2.18 |
| Relative Valuation (RV) | 3.08 | 30.0% | 0.92 |
| Weighted Average Valuation (AED) | | | 3.10 |
| Current market price (AED) | | | 2.33 |
| Upside/Downside (%) | | | +33% |

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 9.5%. The cost of equity is calculated using 10-year government bond yield of 5.7%, beta of 1.00 and equity risk premium of 3.7%. 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) | 4,879 |
| Terminal value (AED, Mn) | 9,612 |
| FV to Common shareholders (AED, Mn) | 14,491 |
| No. of share (Mn) | 4,667 |
| Current Market Price (AED) | 2.33 |
| Fair Value per share (AED) | 3.11 |

DCF Method

| (All Figures in AED Mn) | FY 2024E | FY 2025E | FY 2026E | FY 2027E | FY 2028E |
|--|--------------|--------------|--------------|--------------|--------------|
| Net profit | 1,417 | 1,357 | 1,441 | 1,420 | 1,425 |
| D&A | 513 | 518 | 503 | 509 | 485 |
| Capex | -703 | -699 | -683 | -679 | -671 |
| Net change in working capital | -3 | 156 | -29 | -29 | -178 |
| Free Cash Flow to Equity (FCFE) | 1,224 | 1,332 | 1,231 | 1,221 | 1,061 |
| Discounting Factor | 0.95 | 0.87 | 0.79 | 0.72 | 0.66 |
| Discounted FCFE | 1,163 | 1,155 | 976 | 884 | 702 |

Source: FAB Securities

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 a 2024 EV/EBITDA multiple of 6.2x in line with peers.

| Company | Market cap (USD Mn) | EV/EBITDA (x) | | P/E (x) | |
|---|------------------------|---------------|-------------|--------------|-------------|
| | | 2024F | 2025F | 2024F | 2025F |
| Pegasus Hava Tasimacigli anonim sirketi | 3,134 | 6.2 | 4.5 | 11.8 | 7.4 |
| Jetblue Airways corporation | 1,900 | 12.2 | 7.2 | NA | NA |
| Capital A Berhad | 760 | 5.1 | 3.9 | 7.4 | 5.0 |
| Chorus Aviation Inc. | 330 | 4.4 | 4.2 | 7.8 | 6.0 |
| Allegiant Travel Company | 938 | 6.8 | 4.8 | 25.7 | 8.1 |
| Average | | 7.0x | 4.9x | 13.2x | 6.6x |
| Median | | 6.2x | 4.5x | 9.8x | 6.7x |
| Max | | 6.8x | 4.8x | 15.3x | 7.6x |
| Min | | 5.1x | 4.2x | 7.7x | 5.7x |

Source: FAB Securities

