

National Central Cooling Company (Tabreed)

Global expansion strategy and healthy cash flow to drive profitability

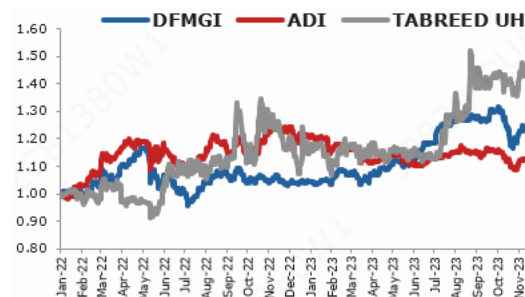
Current Price
AED 3.64

Target Price
AED 3.95

Upside/Downside (%)
+8.5%

Rating
HOLD

- Tabreed expanded its regional footprint in India as the preferred bidder for Hyderabad Pharma City project with a total concession capacity of 125k RT to be implemented in various phases with Ph. 1 of 2.5k RT
- Added 41k refrigeration tonnes (RT) capacity in 9M23 and plans to 120k RT capacity during 2023 & 2024
- Out of total addition of 41K RT, 24K RT in UAE, 14k RT in KSA and the remaining 1k RT each in Bahrain, Oman and India
- Tabreed generated a healthy and predictable free cash flow of AED 903 Mn in 9M23
- Tabreed expands its global portfolio with the commissioning of 4 new plants in UAE and Saudi Arabia, and India contributing to c.45% to incremental capacity



3Q23 Net Profit lower than our estimate

National Central Cooling Company (Tabreed/The Company) reported a net loss of AED 101 Mn in 3Q23, lower than our estimate of AED 176 Mn. The decline in net profit is mainly attributable to other gains of AED 54.4 Mn and a non-cash deferred tax liability provision of AED 359 Mn in 3Q23 related to intangible assets arising from customer contracts and goodwill from business combinations prior to the enactment of UAE CT Law. The normalised net profit rose 13.9% YOY to AED 442 in 9M23 from AED 388 in 9M22 mainly driven by a robust EBITDA performance and a decline in the net finance cost.

P&L Highlights

Tabreed's revenue grew 10.5% YOY to AED 755 Mn in 3Q23 mainly driven by a growth in revenue from the Chilled Water. Revenue from the chilled water segment rose 11.4% YOY owing to the higher consumption volumes, positive CPI, and increase in new business connections. Tabreed's, total capacity rose from 1.24 Mn refrigeration tonnes (RT) in 3Q22 to 1.30 Mn RT in 3Q23. UAE's capacity rose from 1.06 Mn RT in FY2022 to 1.09 Mn RT in 3Q23, whereas capacity in Oman increased from 52 thousand RT in FY2022 to 53 thousand RT in 3Q23, Bahrain increased from 34 kRT in FY2022 to 35 kRT in 3Q23. Revenue from the chilled water segment grew 11.4% YOY to AED 736 Mn in 3Q23. The Company generated around 97% revenue from the chilled water segment. The remaining 3% of revenue is contributed by the value chain business, which declined 16.4% YOY to AED 19 Mn in 3Q23. Tabreed's cost of revenue grew 17.7% YOY to AED 478 Mn in 3Q23. Thus, gross profit declined 0.1% YOY to AED 278 Mn in 3Q23 with a decline in gross profit margin by 389 bps YOY to 36.7% in 3Q23. Moreover, Tabreed's operating expenses decreased 4.6% YOY to AED 61 Mn in 3Q23. Tabreed's EBITDA rose marginally 0.4% YOY to AED 324 Mn in 3Q23 with an EBITDA margin of 42.9% in 3Q23 compared to 47.2% in 3Q22. Operating profit rose 1.3% YOY to

Stock Information

Market Cap (AED, mm)	10,356.79
Paid Up Capital (mm)	2,845.27
52 Week High	3.93
52 Week Low	2.67
3M Avg. daily value (AED)	2,270,580

3Q23 Result Review (AED, mm)

Total Assets	14,927
Total Liabilities	8,085
Total Equity	6,841
EBITDA	324
Net Profit/Loss	-101

Financial Ratios

Dividend Yield (12m)	3.71
Dividend Pay-out (%)	63.93
Price-Earnings Ratio(x)	12.25
Price-to-Book Ratio (x)	1.66
Book Value (AED)	2.19
Return-on Equity (%)	7.77

Stock Performance

5 Days	-1.62%
1 Months	4.00%
3 Months	1.39%
6 Months	24.66%
1 Year	23.81%
Month to Date (MTD%)	4.00%
Quarter to Date (QTD%)	1.11%
Year to Date (YTD%)	22.97%

AED 216 Mn in 3Q23 with an operating margin of 28.7% in 3Q23 compared to 31.3% in 3Q22. Finance cost declined 7.7% YOY to AED 65 Mn in 3Q23 while finance income rose significantly from AED 5 Mn in 3Q22 to AED 15 Mn in 3Q23. Tabreed sold 50% stake in Tabreed Park Investments in 3Q23 and earned a gain of AED 84 Mn including a disposal of 50% interest and gain on 50% retained interest. Other gain and losses stood at AED 54 Mn in 3Q23 compared to AED 12 Mn in 3Q22. Share of associates and JVs grew by 14.0% YOY to AED 10 Mn in 3Q23. However, the share of profit attributable to noncontrolling interest holders rose to AED 27 Mn in 3Q23.

Balance Sheet Highlights

Tabreed's cash and cash equivalents stood at AED 1.4 Bn in 3Q23 as compared to AED 1.2 Bn in 2Q23. The decline in cash balance was mainly attributed 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 250 Mn in 3Q23 as compared to AED 269 Mn in 3Q22. The Company's gross debt declined from AED 6.5 Bn in 2Q23 to AED 6.3 Bn in 3Q23. Net debt to LTM EBITDA declined from 4.49x in FY2022 to 4.18x in 9M23. In addition, debt of AED 4.4 Bn debt is maturing in 2025 and AED 2.0 Bn debt is maturing between 2026-31.

Target Price and Rating

We maintain our HOLD rating on Tabreed with a target price of AED 3.95. The Company share price rose 13.8% since our last rating. Tabreed reported healthy growth in revenue due to new business connections and higher consumption during 3Q23. The Company expanded its regional presence outside GCC with an acquisition of a new plant from Tata Reality in India. Further, Tabreed attracted new customers and commissioned four new plants with one new plant in UAE, two new plants in KSA and the one brownfield acquisition in India. Meanwhile, Tabreed added a new capacity of 41,319 Refrigerated Tons (RT), in UAE, Bahrain, Saudi Arabia and Oman and increased the total connected capacity to 1.30 Mn RT. The Company is progressing as planned to add 120 thousand RT of capacity in 2023-24 period. The expansion is supported by initiation of new projects and new connections within existing concessions. Out of which 41k RT has already been delivered in 9M23, with 60% is expected to be contributed by consolidated entities and the remaining 40% by equity-accounted entities. During 3Q23, the Company incurred a total capex of AED 53.9 Mn, in line with balanced capital allocation strategy and 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 with a strong regional network and delivered 1.30 Mn RT to its customers in 3Q23 and further aims to expand its new geographies outside GCC. The Company continued its geographical footprints ahead in India as the preferred bidder for the Hyderabad Pharma City project with a total concession capacity of 125k RT. It is implemented in various phases with Ph.1 capacity of 2.5k RT. The Company further extends its presence in Saudi with King Salman Park project of total concession capacity of 60k RT and Ph. 1 of 20k RT. Moreover, Tabreed contracted 81% of its capacity being locked into long-term contracts for more than 25 years providing strong revenue visibility by ensuring stability and continuity. Furthermore, the Company earns around 80% of chilled water 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 4.18x in 3Q23. Thus, based on the aforementioned factors, we assign a 'HOLD' rating to the stock.

Tabreed - Relative valuation

(at CMP)	2018	2019	2020	2021	2022	2023F
PE	23.5	21.3	18.3	18.0	17.6	23.1
PB	2.3	2.1	2.0	1.8	1.6	1.5
EV/EBITDA	19.5	17.3	16.9	16.6	13.4	12.7
Dividend yield	2.6%	2.8%	1.5%	1.6%	3.6%	3.8%

FABS Estimates & Co Data

Tabreed – P&L

AED mm	3Q22	2Q23	3Q23	3Q23F	Var.	YOY Ch	QOQ Ch	2022	2023F	Change
Revenue	684	604	755	728	3.8%	10.5%	25.1%	2,216	2,400	8.3%
Operating costs	-406	-317	-478	-429	11.3%	17.7%	50.8%	-1,178	-1,272	8.0%
Gross profit	278	287	278	298	-6.9%	-0.1%	-3.3%	1,038	1,128	8.7%
Admin and other expenses	-64	-65	-61	-68	-10.6%	-4.6%	-5.7%	-245	-259	5.7%
EBITDA	323	322	324	330	-1.7%	0.4%	0.6%	1,232	1,268	2.9%
Operating profit/EBIT	214	222	216	230	-5.9%	1.3%	-2.6%	793	869	9.6%
Finance costs	-71	-69	-65	-71	-8.2%	-7.7%	-5.8%	-289	-285	-1.6%
Finance income	5	11	15	18	-14.0%	NM	39.2%	22	60	NM
Other gains and losses	12	-12	54	0	NM	NM	NM	70	161	NM
Share of associates & JV	9	8	10	9	14.0%	14.0%	24.8%	30	30	0.0%
Profit from cont operation	169	159	231	185	24.6%	36.7%	44.9%	633	835	31.8%
Income tax expense	0	0	-359	0	NM	NM	NM	0	-359	NM
Profit before NCI	169	159	-128	185	NM	NM	NM	633	476	-24.9%
Non-controlling interest	-10	-9	-27	-9	NM	NM	NM	-33	-20	-40.0%
Net Profit	159	150	-101	176	NM	NM	NM	600	456	-24.0%

FABS estimate & Co Data

Tabreed - Margins

	3Q22	2Q23	3Q23	YOY Ch	QOQ Ch	2022	2023F	Change
Gross margin	40.6%	47.5%	36.7%	-389	-1,077	46.8%	47.0%	15
EBITDA margin	47.2%	53.3%	42.9%	-431	-1,047	55.6%	52.8%	-277
Operating margin	31.3%	36.8%	28.7%	-261	-813	35.8%	36.2%	41
Net profit margin	23.3%	24.8%	-13.4%	-3,669	-3,825	27.1%	19.0%	-809

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	3.93	70.0%	2.75
EV/EBITDA	3.99	30.0%	1.20
Weighted Average Valuation (AED)			3.95
Current market price (AED)			3.64
Upside/Downside (%)			+8.5%

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 7.7%. It is arrived after using cost of equity of 8.8% and cost of debt of 6.0% with debt-to-equity ratio of 60.2%. Cost of equity is calculated by using 10-year government bond yield of 5.7%, beta of 0.90 and equity risk premium of 3.4%. 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 2.0%.

Sum of PV (AED, Mn)	3,317
Terminal value (AED, Mn)	13,614
FV to Common shareholders (AED, Mn)	11,157
No. of share (Mn)	2,842
Current Market Price (AED)	3.64
Fair Value per share (AED)	3.93

DCF Method

(All Figures in AED Mn)	FY 2023E	FY 2024E	FY 2025E	FY 2026E	FY 2027E
NOPAT	869	907	967	1,019	1,055
D&A	311	308	309	308	309
Change in working capital	-123	-40	-50	-36	-42
(-) Capex	-240	-283	-251	-267	-281
Free Cash Flow to Firm (FCFF)	816	892	975	1,023	1,041
Discounting Factor	0.99	0.92	0.85	0.79	0.74
Discounted FCFF	84	821	833	812	766

Source: FAB Securities

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 of 13.5x in line with its peers.

Company	Market (USD Mn)	EV/EBITDA (x)		P/E (x)	
		2023F	2024F	2023F	2024F
Essential Utilities, Inc.	9,550	14.7	13.7	18.7	17.4
SJW Group	2,071	14.9	14.2	24.6	23.7
Abu Dhabi National Energy Company PJSC	99,810	13.0	19.3	20.4	41.8
ESSENTIAL UTILITIES, INC.	9,550	14.7	13.7	18.7	17.4
Emirates Central Cooling Systems Corporation	4,711	14.0	12.6	18.3	17.7
Exelon Corporation	38,680	10.8	10.3	16.6	15.4
Dubai Electricity and Water Authority	34,310	10.5	10.4	15.8	17.3
Saudi Electricity Company	20,760	12.8	9.0	17.0	19.0
Average		13.2x	12.9x	18.8x	21.2x
Median		13.5x	13.2x	18.5x	17.6x
Max		14.7x	13.8x	19.1x	20.2x
Min		12.3x	10.4x	16.9x	17.4x

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%

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