

ADNOC Gas PLC

Decline in energy prices impacted profitability

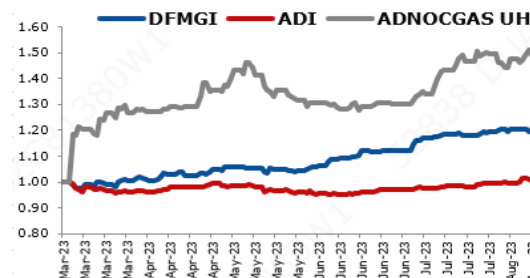
Current Price
AED 3.57

Target Price
AED 3.93

Upside/Downside (%)
+10%

Rating
ACCUMULATE

- To support its growth strategy, the Company awarded contracts worth USD 1.34 Bn to extend the natural gas pipeline, spanning over 3,500 km and catering to the Northern Emirates.
- In July 2023, ADNOC GAS revealed a long-term supply contract worth USD 7-9 Bn with Indian Oil Corporation Ltd that spans over 14 years and involves exporting up to 1.2 MMTA of LNG.
- ADNOC GAS managed to generate EBITDA of USD 1,766 Mn during 2Q23 despite a fall in energy pricing mainly on account of increased efficiency and shift towards high-margin export liquids.
- It recorded a free cash flow of USD 1,035 Mn in 2Q23 as compared to USD 1,509 Mn in 2Q22 due to lower net income and higher capex.



Stock Information

Market Cap (AED, mm)	278,607.66
Paid Up Capital (mm)	19,187.86
52 Week High	3.66
52 Week Low	2.77
3M Avg. daily value (AED)	51,264,220

2Q23 Result Review (USD, mm)

Total Assets	27,379
Total Liabilities	5,932
Total Equity	21,447
EBITDA	1,766
Net Profit	984

Financial Ratios

Dividend Yield (12m)	N/A
Dividend Pay-out (%)	N/A
Est Price-Earnings Ratio(x)	18.07
Price-to-Book Ratio (x)	3.65
Book Value Per share (AED)	0.979
Return-on Equity (%)	N/A

Stock Performance

5 Days	3.18%
1 Months	6.76%
3 Months	12.04%
6 Months	-
1 Year	-
Month to Date (MTD%)	5.20%
Quarter to Date (QTD%)	18.18%
Year to Date (YTD%)	-

2Q23 Net Profit lower than our estimate

ADNOC Gas plc (ADNOC GAS/the Company) net profit declined 28.7% YOY to USD 984 Mn in 2Q23, lower than our estimate of USD 1,275 Mn. The decrease in net profit was primarily due to a decline in revenue owing to a volatile price environment that led to lower prices of Brent Oil, LNG, LPG, and Naphtha prices, partially offset by a decline in feedstock cost and higher gas volume produced across domestic gas and export & traded liquids.

P&L Highlights

ADNOC Gas net revenue declined from USD 7,123 Mn in 2Q22 to USD 5,397 Mn in 2Q23 owing to a drop in Brent oil prices along with a decline in price of LNG, LPG and Naphtha further leading to a decline in gas prices. However, it was partially offset by a growth volume produced. The production volume grew 6.0% YOY in 2Q23. The Company's domestic gas volume grew 8.0% YOY to 582 trillion british thermal units (TBTU) in 2Q23. Exports and Traded liquids volume rose to 256 TBTU in 2Q23 from 247 TBTU in 2Q22. While, LNG production witnessed a decline from 66 TBTU in 2Q22 to 63 TBTU in 2Q23. The Company also maintained a healthy level of reliability across its asset at 99% in 2Q23. ADNOC GAS's direct cost declined to USD 3,078 Mn in 2Q23 mainly due to the benefit from Supply and Payment Agreement (GSPA) with ADNOC Upstream. However, gross profit declined from USD 2,882 Mn in 2Q22 to USD 2,519 Mn in 2Q23 due to decline in revenue. Other operating income stood at USD 283 Mn in 2Q23, while share of profit to equity accounted investee stood at USD 140 Mn in 2Q23. Total operating expenses increased to USD 553 Mn in 2Q23 from USD 468 Mn in 2Q22. Thus, EBIT stood at USD 1,332 Mn in 2Q23. EBITDA also declined from USD 2,414 Mn in 2Q22 to USD 1,766 Mn in 2Q23. Domestic Gas segment delivered at steady performance in the EBITDA which rose 12% to USD 615 Mn owing to favorable contract prices. Export & traded liquids EBITDA impacted by

fell from USD 1,282 Mn in 2Q22 to USD 853 Mn in 2Q23 due to unfavourable price environment. ADNOC Gas's LNG EBITDA fell from USD 403 Mn in 2Q22 to USD 270 Mn in 2Q23 due to a decline in pricing. The Company finance cost stood at USD 73 Mn in 2Q23.

Balance Sheet Highlights

ADNOCGAS's cash from operating activities declined from USD 3,171 Mn in 1H22 to USD 2,509 Mn in 1H23. The Company's investment in capex increased from USD 289 Mn in 1H22 to USD 399 Mn in 1H23 primarily due to growth projects such as ESTIDAMA and the construction of an extra greenfield gas processing plant. Furthermore, the Company plans to allocate USD 14 Bn towards growth capex between 2023-28, along with an additional USD 1 Bn for maintenance capex over the next three years. ADNOCGAS's free cash flow experienced a decline from USD 2,882 Mn in 1H22 to USD 2,109 Mn in 1H23, primarily due to investments in capex and a reduction in net income partially offset by lower taxes. As of 2Q23, the Company held cash and cash equivalents of USD 3,688 Mn, while its gross debt amounted to USD 1,350 Mn.

Target Price and Rating

We revise our rating from BUY to ACCUMULATE on ADNOCGAS with a revised target price of AED 3.93. The Company's share price went up 16.7% since our last rating on 24 April 2023. ADNOCGAS reported a decline in net profit owing to a decline in net revenue and EBITDA on account of a fall in energy prices. The Company's net revenue was impacted mainly due to the reduction in the Brent crude oil prices which led to a further decline in gas prices. While the EBITDA declined to USD 1,766 Mn in 2Q23. The Company managed to maintain stable margins as it focused on increased efficiency and shifted towards high-margin export liquids. ADNOCGAS currently owns a total gross capacity of 10+ BSCFD of gas processing facilities and 29 MTPA of liquid processing capacity. While it further anticipates increasing its gas processing by 3 BSCFD and liquid processing by 6 MTPA over the next five years. ADNOCGAS's asset utilization and availability improved to 86.8% and 97.8% respectively in 2Q23 mainly due to lower shutdowns as compared to 1Q23. The Company projects its production volume to range between 2,150 and 2,250 TBTU for the Domestic Gas segment, between 900 and 950 TBTU for Exports & Traded Liquid, and between 200 and 250 TBTU for ALNG JV products in 2023. Recently, ADNOCGAS authorized contracts worth USD 1.34 Bn to extend the natural gas pipeline, spanning over 3,500 km and catering to the Northern Emirates, to support its growth strategy. The milestone is a significant step within the ESTIDAMA program, focused on enhancing the sales gas pipeline network. The strategic extension of the pipeline will drive additional expansion for ADNOCGAS ensuring a consistent supply of sustainable gas to customers and contributing to the UAE's goal of achieving gas self-sufficiency. The Company is also actively capitalizing on the increasing global demand for natural gas while expanding its presence. In July 2023, it signed a long-term supply contract with Indian Oil Corporation Ltd which is valued at USD 7-9 Bn. The agreement spans 14 years and involves exporting up to 1.2 MTPA of LNG. ADNOCGAS is also planning to gradually increase leverage to fund its capex requirement. It has earmarked a Capex of USD 14 Bn over 2023-28. The Company aims to achieve a 5.0% annual dividend payment increase from 2024 to 2027, while it plans to pay a dividend of USD 3.25 Bn in 2023 in two instalments. The aforementioned factors lead us to maintain an ACCUMULATE rating on the stock.

Adnoc Gas - Relative valuation

(at CMP in USD)	2018	2023F
PE	NA	16.1
PB	NA	3.3
EV/EBITDA	NA	10.6
Dividend yield	NA	4.4%

FABS Estimates & Co Data

ADNOCGAS share started trading on 13th of March 2023; hence previous-year multiples are not provided.

Adnoc Gas – P&L

USD mm	2Q22	1Q23	2Q23	2Q23F	Var.	YOY Ch	QOQ Ch	2022	2023F	Change
Revenue	7,123	5,226	5,397	5,230	3.2%	-24.2%	3.3%	21,200	19,279	-9.1%
Direct Cost	4,241	2,938	3,078	3,022	1.8%	-27.4%	4.8%	NA	11,580	NA
Gross Profit	2,882	2,288	2,319	2,208	5.0%	-19.5%	1.4%	NA	7,699	NA
G&A Expenses	468	-514	-553	-510	8.4%	-218.2%	7.6%	NA	2,605	NA
EBITDA	2,414	1,774	1,766	2,118	-16.6%	-26.8%	-0.5%	7,300	6,689	-8.4%
Net Profit	1,380	1,275	984	1,275	-22.8%	-28.7%	-22.8%	4,900	4,570	-6.7%

FABS estimate & Co Data

Adnoc Gas - Margins

	2Q22	1Q23	2Q23	YOY Ch	QOQ Ch	2022	2023F	Change
Gross Profit	40.5%	43.8%	43.0%	251	-81	NA	41.4%	NA
EBITDA	33.9%	33.9%	32.7%	-117	-122	34.4%	34.7%	26
Net Profit	19.4%	24.4%	18.2%	-114	-616	23.1%	23.7%	59

FABS estimate & Co Data

Valuation:

We have used Discounted Free Cash Flow (DCF), Relative Valuation (RV) and Dividend Yield to value ADNOC Gas. We have assigned 70% weight to DCF, 15% to RV and 15% to Dividend Yield. In addition, we have also valued ADNOC LNG JV using the Discounted Free Cash Flow (DCF) and Relative Valuation (RV) method. We excluded the profit of ADNOC LNG JV while valuing ADNOC GAS; as a result, it is valued as a standalone business.

Valuation Method	Target	Weight	Weighted Value
DCF Method	4.12	70.0%	2.88
Relative Valuation (RV)	3.57	15.0%	0.53
Dividend Yield	3.42	15.0%	0.51
Weighted Average Valuation (AED)			3.93
Current market price (AED)			3.57
Upside/Downside (%)			+10%

1) ADNOC Gas DCF Method:

Adnoc Gas is valued using free cash flow to Equity. We have discounted the cash flow using weighted average cost of equity of 8.2%. The cost of equity is calculated using a 10-year government bond yield of 4.5%, a beta of 0.97, and an equity risk premium of 3.8%. Government bond yield is calculated after adding Abu Dhabi 10-year spread over 10-year US risk-free rate. Also, assumed a terminal growth rate of 2.0%.

Sum of PV (USD, Mn)	22,429
Terminal value (USD, Mn)	55,256
FV to Common shareholders (USD, Mn)	77,685
No. of share (Mn)	76,751
Current Market Price (AED)	3.57
Fair Value per share (AED)	3.72

DCF Method

(All Figures in USD Mn)	FY2023E	FY2024E	FY2025E	FY2026E	FY2027E	FY2028E	FY2029E	FY2030E
Net Income	4,131	4,234	4,256	4,503	4,710	4,426	4,706	5,032
D&A	1,156	1,211	1,355	1,523	1,666	1,813	1,888	1,925
(-) Capex	-1,900	-3,500	-3,500	-3,000	-3,100	-3,200	-1,628	-800
Change in working capital	-54	-89	-71	-75	-76	-87	-91	-98
Net change in debt	0	500	1,000	1,000	1,000	500	0	0
Free Cash Flow to Equity (FCFE)	3,333	2,356	3,040	3,952	4,200	3,452	4,876	6,059
Discounting Factor	0.97	0.90	0.83	0.77	0.71	0.65	0.60	0.56
Discounted FCFE	3,233	2,112	2,518	3,023	2,969	2,255	2,942	3,378

Source: FAB Securities

1) ADNOC Gas LNG JV DCF Method:

Adnoc Gas LNG JV is valued using free cash flow to Equity. It is discounted using the similar WACC used to discount ADNOC GAS. We have discounted the cash flow using weighted average cost of equity of 8.2%. The cost of equity is calculated using a 10-year government bond yield of 4.5%, a beta of 0.97, and an equity risk premium of 3.8%. Government bond yield is calculated after adding Abu Dhabi 10-year spread over 10-year US risk-free rate. Also, assumed a terminal growth rate of 2.0%.

Sum of PV (USD, Mn)	3,904
Terminal value (USD, Mn)	8,040
FV to Common shareholders (USD, Mn)	11,944

DCF Method

(All Figures in USD Mn)	FY2023E	FY2024E	FY2025E	FY2026E	FY2027E	FY2028E	FY2029E	FY2030E
Net Income	627	523	524	591	672	689	722	757
D&A	143	143	143	143	143	293	293	293
(-) Capex	-135	-324	-334	-371	-389	-432	-202	-210
Change in working capital	-81	-36	-37	-42	-48	-53	-56	-58
Net change in debt	0	250	250	300	300	200	100	100
Free Cash Flow to Equity (FCFE)	554	555	545	621	678	697	857	882
Discounting Factor	0.97	0.90	0.83	0.77	0.71	0.65	0.60	0.56
Discounted FCFE	538	497	452	475	479	455	517	491

Source: FAB Securities

2) Relative Valuation: (EV/ EBITDA) & (Dividend Yield)

We have used regional and global peers to value ADNOC GAS PLC, which is valued using the EV/EBITDA and Dividend Yield multiple. It is valued at a 2024 EV/EBITDA multiple of 8.5x in line with its peers. In the dividend yield, we have used a dividend Yield of 4.8% to value ADNOC GAS.

Company	Market (USD Mn)	EV/EBITDA (x)		P/E (x)		Dividend Yield (%)	
		2023F	2024F	2023F	2024F	2023F	2024F
Saudi Basic Industries Corp	17,924	9.4	7.1	34.2	18.9	4.3	4.7
Saudi Arabian Oil Co	2,228,775	8.4	8.0	17.4	16.6	4.2	4.6
Borouge	22,504	11.9	9.8	25.0	16.3	5.6	5.5
Petronas Gas Bhd	7,297	9.4	9.0	17.9	17.4	4.7	4.8
Kinder Morgan Inc	39,617	9.3	9.0	15.5	14.4	6.4	6.5
Valero Energy Corp	49,107	3.8	5.6	6.0	9.2	2.9	3.0
Marathon Petroleum Corp	59,877	4.7	6.5	6.9	10.2	2.1	2.2
Oneok Inc	29,654	9.1	10.1	11.7	14.0	5.8	5.9
Targa Resources Corp	19,002	8.7	8.0	19.6	12.8	2.4	2.7
Williams Cos Inc	43,037	10.1	10.0	18.4	19.3	5.1	5.3
Average		8.5x	8.3x	17.3x	14.9x	4.3x	4.5x
Median		9.2x	8.5x	17.7x	15.4x	4.5x	4.8x
Max		9.4x	9.6x	19.3x	17.2x	5.5x	5.4x
Min		8.4x	7.3x	12.7x	13.1x	3.3x	3.4x

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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