

National Central Cooling Co. - Tabreed

Equity Research Update

Sector – Utilities

Meaningful growth aspirations beyond the UAE

DPO & deleveraging supports valuation until growth outside UAE materializes

Tabreed's capital allocation strategy continues to remain focused towards deleveraging and is evident from the company's partial repurchase (USD 200.7 Mn) of its USD 500 Mn Trust Certificates due in 2025. Our shorter-term thesis shifts towards the company's strategy for the AED 4.285 Bn of debt maturing in 2025, keeping dividend payout (DPO) at roughly 65%-70% and remaining flexible enough for debt-funded acquisitions while maintaining its investment grade (IG) rating. We retain our 'Neutral' rating on Tabreed, as we believe that the company's organic capacity addition forecasts (~300k RT from existing concessions) look mostly priced in at current market prices. Medium term rerating for the stock is expected to come from beyond the UAE - mainly from Saudi Arabia and India, underpinned by strategic partners such as PIF (Saudi Tabreed) and International Finance Corporation (India Ops). Operations from both geographies include services beyond DC O&M contracts, however meaningful revenue recognition should be backend loaded in nature.

UAE organic capacity growth over the medium term to remain moderate

As mentioned in our previous update [Tabreed \(TP: AED 3.55, Neutral\) - Strong FCF generation; but acquisitions missing](#), the acquisition of UAE DC assets remain elusive as developers maintain their strong liquidity on the back of strong cash-based transactions and price momentum, which pushes out any need for monetizing non-core assets in the near term. Tabreed's management now guides for combined organic capacity growth to be moderate at 3%-5% over 2024E-26E across fully consolidated and equity accounted participations. Accordingly, we lower our capacity forecasts for both 2024E/25E and 2025E/2026 to 120k RTs each (previous estimate: 135k RT). We forecast group revenues of AED 2.56 Bn in 2024E, thereafter reaching AED 2.69 Bn by 2026E, driven by our organic capacity growth of 4.4% over 2023-25E. Normalized EBITDA margins should remain healthy at +49% over 2023E-25E, derived from higher non-cyclical capacity-linked revenues. EBITDA-FCF conversion rates would approach ~70% by 2026E (AED 930 Bn) according to our forecasts, which should additionally help in potential acquisitions and deleveraging. Our thesis focus shifts towards the company's strategy for the AED 4.285 Bn of debt maturing in 2025, keeping dividend payout (DPO) at roughly 65%-70% and remaining flexible enough for debt-funded acquisitions while maintaining its investment grade (IG) rating.

International Ops growth mostly backend loaded but required for next rerating

Tabreed continues to pursue brownfield opportunities in the UAE outside their existing concessions, albeit at smaller ticket sizes. Key growth markets outside the UAE remain: 1) Saudi Arabia via equity accounted associate Saudi Tabreed (21% stake), and 2) India from Tabreed's 75% stake partnership with International Finance Corporation. Saudi Tabreed's connected capacity could more than double easily from 124k RTs reported in Q1-2024, driven by strategic partners such as PIF (30% stake) invested in Saudi Tabreed that allows focus on both district cooling and utilities concessions for large multi-use projects, and O&M operator contracts of DC assets similar to the Red Sea project, revenues for which should potentially commence in H2-2024. Growth should be supported by Saudi Tabreed's King Salman Park project with a total concession capacity of 60k RT (Phase 1 - 20k RT). India also represents significant potential for acquisitions albeit backend loaded, and for newer formats of services such as pay-per-service models like CaaS (Cooling as a Service).

Valuation & Risks – Revised TP of AED 3.45 (Previous: AED 3.55)

We revise our TP for Tabreed to AED 3.45/share based on a 70:30 blend between DCF and 2025E EV/EBITDA. **Key upside risks:** 1) Key DC assets acquisitions materialize in the UAE; 2) Faster international DC footprint growth. **Key downside risks:** 1) Lower RE market activity; 2) Delays in the ramp-up of Tabreed's connected capacity. 3) Lower consumption revenues due to lower occupancy rates.

Neutral

CMP 24-May-24: AED 3.18
Target Price (TP): AED 3.45
Upside/Downside: +8.5%


Price Perf.	1M	3M	12M
Absolute	3.3%	-7.8%	8.9%
Relative	6.5%	-1.7%	-4.4%

Stock Data

Bloomberg Ticker	TABREED UH
Last Price (AED)	3.18
MCap (AED Mn)	9,037
MCap (USD Mn)	2,463
EV (AED Mn)	13,072
Stock Performance - YTD (%)	-11.2%
PE - 2024E (x)	13.4
EV/EBITDA - 2024E (x)	10.3
Dividend yield - 2024E (%)	5.2%
52-Week Range (AED)	2.82/3.85

Sources: Kamco Invest Research & Bloomberg

Tabreed Financials	2023	2024E	2025E
Revenue (AED Mn)	2,415	2,563	2,616
EBITDA (AED Mn)	1,198	1,274	1,294
EBITDA margin (%)	49.6%	49.7%	49.4%
EPS* (AED/share)	0.21	0.24	0.26
PE* (x)	16.9	13.4	12.4
EV/EBITDA (x)	12.6	10.3	9.8
Div Yield (%)	4.3%	5.2%	5.7%

Source: Kamco Invest Research, Tabreed, * based on recurring EPS from continuing operations

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Valuation and Risks

Target price raised to AED 3.45/share; retain 'Neutral' rating

Post Q1-24 results, we have revised our TP for Tabreed to AED 3.45/share (Previous AED 3.55/share), based on a blend of DCF (70%), 2025E EV/EBITDA (30%), and our forecasts for connected organic capacity. We retain our 'Neutral' rating on Tabreed as we believe that the company's organic capacity addition forecasts (~300k RT from existing concessions) look mostly priced in at current market prices. Our shorter-term thesis shifts towards the company's strategy for the AED 4.285 Bn of debt maturing in 2025, keeping dividend payout (DPO) at roughly 65%-70% and remaining flexible enough for debt-funded acquisitions while maintaining its investment grade (IG) rating. Medium term rerating for the stock is expected to come from beyond the UAE - mainly from Saudi Arabia and India, underpinned by strategic partners such as PIF (Saudi Tabreed) and International Finance Corporation (India Ops). Operations from both geographies include services beyond DC O&M contracts, however meaningful revenue recognition should be backend loaded in nature.

Tabreed Fair Value	
DCF based value	3.52
EV/EBITDA - 2025E (10x)	3.29
Blended price target	3.45
Current market price (24 May 2024)	3.18
Upside	8.5%

Sources: Kamco Invest Research

Our DCF model reflects the significant visibility of Tabreed's recurring revenues and cashflows, attained from having a majority of revenues locked-in, as per take-or-pay contracts over the next 10 years. Our model incorporates a revenue CAGR of 4.4% over 2023-2026E, driven by a similar growth in percentage terms for total connected capacity, from the 1.303 Mn RT connected in 2023 across the GCC. We expect EBITDA margins to remain strong at an average of ~49% over 2024E-2026E, given the higher proportion of non-cyclical capacity linked revenues. We have assumed a terminal growth rate of 2.0%, revised our average WACC to 7.25% over our forecast period. For the company's terminal value, the sustainable long-term growth rate adequately reflects the risks, competition in the market, and a return on new investment capital (RONIC) that is comparable to the terminal year WACC. For value from associates and JVs, we derive market values based on a target IRR of 10%. Book values of cash, debt and minorities are based on Q1-2024 financials.

Currently, Tabreed trades at a 2025E multiple of 9.8x based on our estimates, which we think is reasonably fair considering market conditions, and bearing in mind that the company trades at a reasonable discount to its larger industry counterpart – Emirates Central Cooling Systems Corporation PJSC (Empower - not rated by Kamco Invest Research) that trades ~10.9x (2025E EV/EBITDA) based on consensus estimates. Moreover, barring any market-wide correction, we feel significant downside risk is protected due to the company's strong defensive profile. Even in the case of an economic slowdown or market-wide correction, declines in Tabreed's share price would make its dividend yields attractive, as the company's operating environment in terms of recurring revenues and hedged debt portfolio should remain largely unaffected.

Risks to our rating & forecasts include:

Upside risks:

- Winning bids for key DC assets acquisitions materialize in the UAE
- Faster international DC footprint growth in India, KSA, Egypt and Kuwait
- Rising number of RE mixed-use projects being announced in the UAE and the GCC
- Higher pass-through of CPI for consumption revenues
- Quicker commercial mainstream adoption of geothermal cooling with ADNOC

Downside risks:

- Lower real estate project market activity, and new project cancellations in Tabreed's target markets
- Delays in ramp-up of Tabreed's connected capacity towards ultimate capacity targets in existing projects
- Lower consumption revenues for the Chilled Water segment due to lower occupancy rates and footfall from existing commercial real estate clients
- FX risks for international operations that erode project IRRs

Tabreed Financials

Balance Sheet (AED Mn)	2022	2023	2024E	2025E	2026E
Assets					
Cash and cash equivalents	1,773	1,510	1,630	1,933	2,322
Receivables	1,233	1,024	1,027	1,041	1,062
Other current assets	60	70	74	75	78
Total current assets	3,066	2,604	2,731	3,050	3,462
Net PPE including capital WIP	4,753	4,472	4,966	4,973	4,982
Other assets	7,632	7,738	7,182	7,054	6,916
Total assets	15,451	14,814	14,880	15,077	15,361
Liabilities					
Current Liabilities	819	873	743	680	700
Total debt	7,217	6,325	5,665	5,529	5,434
Other Liabilities	261	673	995	1,048	1,059
Total liabilities	8,297	7,870	7,403	7,257	7,193
Shareholders' Equity					
Share capital	2,845	2,845	2,845	2,845	2,845
Retained earnings	2,757	2,762	3,266	3,525	3,786
Minority Interest	679	626	636	646	656
Other Equity	872	710	731	804	881
Total Equity	7,154	6,943	7,477	7,819	8,168
Total liabilities and equity	15,451	14,814	14,880	15,077	15,361
Income Statement (AED Mn)	2022	2023	2024E	2025E	2026E
Revenue	2,216	2,415	2,563	2,616	2,693
Cost of goods sold	-875	-1,013	-1,074	-1,101	-1,134
Adjusted gross profit	1,341	1,402	1,490	1,515	1,559
General and administrative expenses	-109	-204	-216	-221	-229
EBITDA	1,232	1,198	1,274	1,294	1,330
Depreciation and amortization	-430	-392	-388	-394	-398
EBIT	802	806	886	899	931
Finance costs	-289	-265	-259	-232	-236
Interest/investment income	22	61	84	104	119
Other Income/Loss	99	184	38	40	42
Net profit before income taxes	633	785	749	811	856
Income taxes & deferred tax adjustments	0	359	-64	-70	-74
Net profit after tax	633	427	685	741	783
Minority interest	-33	5	-10	-10	-10
Net profit attributable to parent	600	431	675	731	773
One-offs & Deferred tax liability adjustments	-70	-172	0	0	0
Normalized net profit attributable to parent	530	603	675	731	773
EPS (AED)	0.21	0.15	0.24	0.26	0.27
Normalized EPS from continuing operations (AED)	0.19	0.21	0.24	0.26	0.27
Cash Flow (AED Mn)	2022	2023	2024E	2025E	2026E
Net cash from operating activities	1,355	1,312	1,101	1,133	1,242
Net cash (used in) from investing activities	(214)	(54)	278	(86)	(110)
Net cash from (used in) financing activities	(565)	(1,521)	(1,258)	(745)	(743)
Change in cash and cash equivalents	576	(263)	120	303	389
FX and other adjustments	0	0			
Cash at the end of the year	1,773	1,510	1,630	1,933	2,322

Source: Kamco Invest Research and Tabreed

Valuation & Financial Ratios					
Ratios	2022	2023	2024E	2025E	2026E
Leverage Ratios					
Total Debt / Total Assets (x)	0.47	0.43	0.38	0.37	0.35
Total Debt / Equity (x)	1.01	0.91	0.76	0.71	0.67
Net Debt/Equity (x)	0.76	0.69	0.54	0.46	0.38
Operating Efficiency & Liquidity Ratios					
Receivables Turnover Ratio (%)	2.8	3.1	3.2	3.7	3.8
Payables Turnover Ratio (%)	3.0	3.4	3.4	3.8	3.8
Cash conversion cycle	8.6	8.3	7.4	2.7	2.2
Total Assets Turnover Ratio (x)	0.15	0.16	0.17	0.17	0.18
Current Ratio (x)	3.75	2.98	3.67	4.48	4.94
Margins & Profitability Ratios					
Adjusted Gross profit margin (%)	60.5%	58.0%	58.1%	57.9%	57.9%
EBITDA margin (%)	55.6%	49.6%	49.7%	49.4%	49.4%
EBIT margin (%)	36.2%	33.4%	34.6%	34.4%	34.6%
Net profit margin (%)	23.9%	25.0%	26.3%	27.9%	28.7%
Return on Assets (%)	3.4%	4.1%	4.5%	4.8%	5.0%
Return on Equity (%)	7.4%	8.7%	9.0%	9.4%	9.5%
ROIC (%)	5.6%	6.1%	6.3%	6.2%	6.3%
Per Share Data and Valuation Ratios					
Earnings Per Share (AED)*	0.19	0.21	0.24	0.26	0.27
Book Value Per Share (AED)	2.52	2.44	2.63	2.75	2.87
Dividend Per Share (AED)	0.14	0.16	0.17	0.18	0.19
PE (x)*	15.9	16.9	13.4	12.4	11.7
EV/EBITDA (x)	11.3	12.6	10.3	9.8	9.1
PB (x)	1.2	1.5	1.2	1.2	1.1
Dividend Yield (%)	4.6%	4.3%	5.2%	5.7%	6.0%

Source: Kamco Invest Research and Tabreed, * recurring EPS

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