

## National Central Cooling Co. - Tabreed

Equity Research Update

Sector – Utilities

### Defensive fortifications

#### Deleveraging & dividend themes payout for now; retain 'Neutral'

We retain our 'Neutral' rating on Tabreed as we believe that the company's organic capacity addition forecasts (~350k RT from existing concessions) look fully priced in at current market prices. However, we feel significant downside risk is protected due to the company's strong defensive capabilities that flow from its deleveraging profile (~99% of its debt portfolio hedged at <4%) which are adequately below IG ratings thresholds. Further, the company's recurring revenues at healthy GP margins, and dividend payout potential which we expect to be comfortably around 65%-70% in the absence of acquisitions of DC assets, should fortify its defensive fundamentals. Separately, we are optimistic on Tabreed's international operations over the longer term, especially with PIF's investment in Saudi Tabreed, which should improve its ability to win DC and O&M utilities concession bids of Saudi's mega projects.

#### Liquidity of RE developers keeps Tabreed's acquisitions landscape dry

In our previous update, we mentioned that RE developers in the UAE are likely to exit non-core assets such as DC assets to fund their expansion plans in a rising interest rate environment, which has not transpired. Developers remain flushed with liquidity on the back of strong cash-based transactions and price momentum in the market, which pushes out any need for monetizing non-core assets in the near term. Tabreed's TAM realization and ROIC maximization will depend on how quickly these transactions come to the market, and acquisitions are executed. For the company's organic growth, we pencil in 130k RT for 2023E/24E and 135k RT for 2024E/25E, as connected capacity picks up the shortfall of management guidance of 120k RT over 2021/22 (95k RT achieved), and while smaller greenfield connections are signed. As a result, we expect Tabreed's group revenues to reach AED 2.33 Bn in 2023E, and thereafter reach AED 2.52 Bn by 2025E, driven by organic capacity growth of 4.3% over 2022-25E. EBITDA margins should remain strong at ~55% over 2023E-25E, derived from higher proportion of non-cyclical capacity-linked revenues. Capacity revenues in 2023E should be aided by contractual CPI pass through (H1-2023E: +4.8% y-o-y), while EBITDA-FCF conversion rates would approach 68% by 2025E according to our forecasts, which should additionally help in generating additional dry powder for acquisitions.

#### International Ops look promising; ongoing evaluation for use case of cash

Tabreed's international operations through Saudi Tabreed represents a significant longer-term opportunity despite the company bringing down its stake from 31.1% to 21.8%, in our view. This is ascribed to having PIF as a strategic shareholder (30% stake) and Saudi Tabreed's focus on both district cooling and utilities concessions such as the 15% share in the PPP utilities concession under BOOT framework with the Red Sea Development Company, which should put the entity in an advantageous position for concession signings of Saudi's mega projects. Tabreed (75%) commenced its India JV participation with IFC (25%) by: 1) Establishing a strategic alliance with TATA Realty and Infrastructure for an investment of AED 44.34 Mn ( INR 100 Cr) in TATA Realty's Intellion Park special economic zone (SEZ) development in Gurugram, with 2k RT of connected capacity and a concession of 6k RT; 2) Being named as the preferred bidder for a long-term DC concession contract for the Hyderabad Pharma City master plan (Phase 1 - 2.5k RT, capex: AED 36.2 Mn). Our thesis for Tabreed going forward will focus on the company's use case for its cash ( H1-2023: AED 1.19 Bn) and undrawn RCF of AED 590 Mn for acquisitions and/or dividends, given its strong deleveraging profile and recurring revenues at healthy GP margins.

#### Valuation & Risks – Revised TP of AED 3.40 (Previous: AED 3.25)

We revised our TP for Tabreed to AED 3.40/share based on a 70:30 blend between DCF and 2024E 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.

**Neutral**

**CMP 01-Sept-23: AED 3.69**

**Target Price (TP): AED 3.40**

**Upside/Downside: -7.7%**



Price Perf.	1M	3M	12M
Absolute	9.5%	25.5%	29.5%
Relative	9.3%	12.0%	9.0%

#### Stock Data

Bloomberg Ticker	TABREED UH		
Last Price (AED)	3.69		
MCap (AED Mn)	10,487		
MCap (USD Mn)	2,857		
EV (AED Mn)	15,326		
Stock Performance - YTD (%)	24.7%		
PE - 2023E (x)	15.6		
EV/EBITDA - 2023E (x)	11.9		
Dividend yield - 2023E (%)	4.2%		
52-Week Range (AED)	2.70/3.85		

Sources: Kamco Invest Research & Bloomberg

Tabreed Financials	2022	2023E	2024E
Revenue (AED Mn)	2,216	2,326	2,416
EBITDA (AED Mn)	1,232	1,290	1,333
EBITDA margin (%)	55.6%	55.5%	55.2%
EPS* (AED/share)	0.21	0.24	0.23
PE* (x)	14.0	15.6	16.1
EV/EBITDA (x)	11.3	11.9	11.3
Div Yield (%)	4.6%	4.2%	4.0%

Source: Kamco Invest Research, Tabreed, \* from continuing operations

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## Valuation and Risks

### Target price raised to AED 3.40/share; retain 'Neutral' rating

We updated and rolled over our forecasts since our previous update '[Tabreed \(TP: AED 3.25, Neutral\): Valuation gap closes amid smaller-ticket signings](#)'. We revise our TP for Tabreed to AED 3.40/share, based on a blend of DCF (70%), 2024E EV/EBITDA (30%), and our forecasts for connected organic capacity. Tabreed's share price rallied almost 24.7% YTD in 2023, and we retain our 'Neutral' rating on the company as we feel that revised organic capacity addition forecasts (~350k RT from existing concessions) look fully priced in at these levels. Our thesis for Tabreed going forward will focus on the company's use case for its cash (H1-2023: AED 1.19 Bn) and undrawn RCF of AED 590 Mn for acquisitions and/or dividends, given its strong deleveraging profile and recurring revenues at high GP margins.

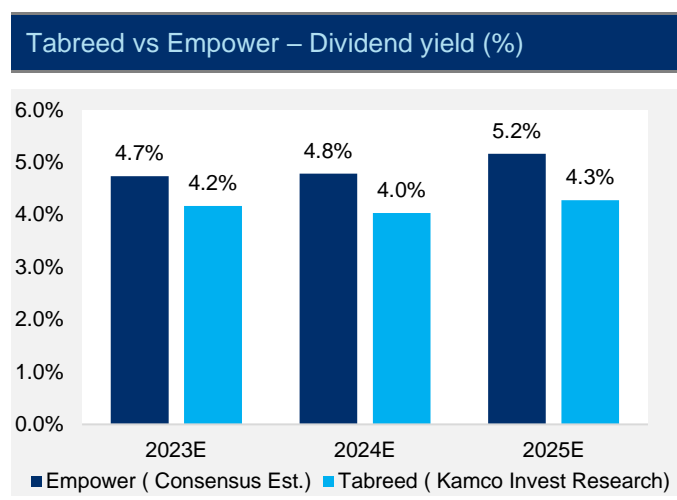
Tabreed Fair Value	
DCF based value	3.28
EV/EBITDA - 2024E (11.5x)	3.69
<b>Blended price target</b>	<b>3.40</b>
Current market price (01 Sept 2023)	3.69
<b>Downside</b>	<b>-7.7%</b>

Sources: Kamco Invest Research

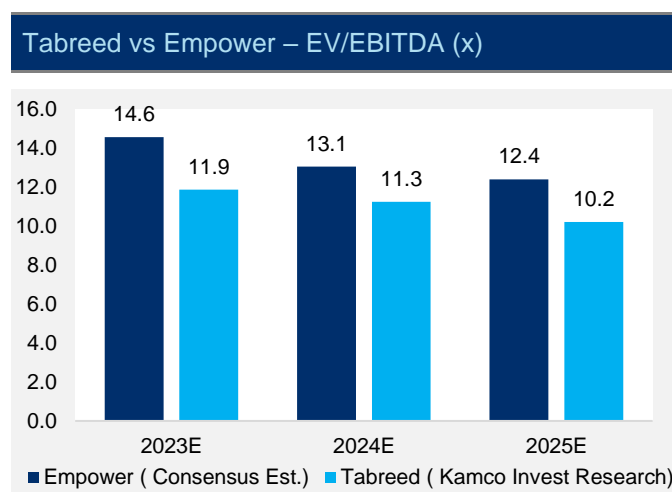
Our DCF model reflects the significant visibility of Tabreed's recurring revenues and cashflows, attained from having a majority of revenues locked-in, as per take-or-pay contracts over the next 10 years. Our model incorporates a revenue CAGR of 4.4% over 2022-2025E, driven by a similar growth in percentage terms for total connected capacity, from the 1.27 Mn RT connected in 2022 across the GCC. We expect EBITDA margins to remain strong at an average ~55% over 2023E-2025E, 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 7.1% over our forecast period, and have adjusted our after-tax cashflows for the introduction of UAE's corporate income tax of 9% starting from 2024E. 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 H1-2023 financials.

### Fairly priced until acquisitions are executed; strong defensive fundamentals

We expect Tabreed's dividend payout potential to be comfortably around 65%-70% over 2023E-25E, in the absence of acquisitions of DC assets which fortifies its defensive fundamentals.



Source: Kamco Invest Research, Bloomberg



Source: Bloomberg, Kamco Invest Research

Currently, Tabreed trades at a 2024E multiple of 11.5x, which we think is 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). 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

<b>Tabreed Financials</b>						
<b>Balance Sheet (AED Mn)</b>	<b>2020</b>	<b>2021</b>	<b>2022</b>	<b>2023E</b>	<b>2024E</b>	<b>2025E</b>
<b>Assets</b>						
Cash and cash equivalents	1,313	1,197	1,773	1,709	1,907	2,657
Receivables	1,214	1,015	1,233	1,279	1,315	1,359
Other current assets	42	51	60	63	65	68
<b>Total current assets</b>	<b>2,569</b>	<b>2,263</b>	<b>3,066</b>	<b>3,051</b>	<b>3,288</b>	<b>4,084</b>
Net PPE including capital WIP	4,437	4,813	4,753	5,008	5,009	5,025
Other assets	6,306	7,758	7,632	7,126	6,881	6,628
<b>Total assets</b>	<b>13,313</b>	<b>14,833</b>	<b>15,451</b>	<b>15,186</b>	<b>15,178</b>	<b>15,737</b>
<b>Liabilities</b>						
Current Liabilities	662	859	819	785	815	851
Total debt	6,623	7,272	7,217	6,548	6,423	6,328
Other Liabilities	153	256	261	273	48	297
<b>Total liabilities</b>	<b>7,438</b>	<b>8,387</b>	<b>8,297</b>	<b>7,606</b>	<b>7,286</b>	<b>7,476</b>
<b>Shareholders' Equity</b>						
Share capital	2,716	2,776	2,845	2,845	2,845	2,845
Retained earnings	2,134	2,460	2,757	3,072	3,286	3,553
Minority Interest	710	700	679	712	746	779
Other Equity	315	510	872	950	1,015	1,084
<b>Total Equity</b>	<b>5,875</b>	<b>6,446</b>	<b>7,154</b>	<b>7,580</b>	<b>7,892</b>	<b>8,261</b>
<b>Total liabilities and equity</b>	<b>13,313</b>	<b>14,833</b>	<b>15,451</b>	<b>15,186</b>	<b>15,178</b>	<b>15,737</b>
<b>Income Statement (AED Mn)</b>	<b>2020</b>	<b>2021</b>	<b>2022</b>	<b>2023E</b>	<b>2024E</b>	<b>2025E</b>
Revenue	1,741	1,955	2,216	2,326	2,416	2,521
Cost of goods sold	-683	-829	-875	-904	-940	-980
<b>Adjusted gross profit</b>	<b>1,058</b>	<b>1,126</b>	<b>1,341</b>	<b>1,422</b>	<b>1,476</b>	<b>1,541</b>
General and administrative expenses	-88	-93	-109	-132	-143	-156
<b>EBITDA</b>	<b>970</b>	<b>1,033</b>	<b>1,232</b>	<b>1,290</b>	<b>1,333</b>	<b>1,385</b>
Depreciation and amortization	-340	-410	-430	-456	-458	-458
<b>EBIT</b>	<b>630</b>	<b>623</b>	<b>802</b>	<b>834</b>	<b>875</b>	<b>927</b>
Finance costs	-222	-258	-289	-287	-285	-296
Interest/investment income	3	3	22	59	58	58
Other Income/Loss	130	166	99	205	100	102
<b>Net profit before income taxes</b>	<b>542</b>	<b>534</b>	<b>633</b>	<b>811</b>	<b>748</b>	<b>791</b>
Income taxes					-65	-68
<b>Net profit after tax</b>	<b>542</b>	<b>534</b>	<b>633</b>	<b>811</b>	<b>684</b>	<b>723</b>
Discontinued operations & one-offs	32	77	0	107	0	0
<b>Net profit from continuing operations</b>	<b>573</b>	<b>611</b>	<b>633</b>	<b>705</b>	<b>684</b>	<b>723</b>
Minority interest	-23	-26	-33	-33	-33	-33
<b>Net profit attributable to parent</b>	<b>550</b>	<b>585</b>	<b>600</b>	<b>778</b>	<b>650</b>	<b>690</b>
<b>Net profit attributable to parent- continuing operations</b>	<b>518</b>	<b>508</b>	<b>600</b>	<b>671</b>	<b>650</b>	<b>690</b>
<b>EPS (AED)</b>	<b>0.19</b>	<b>0.21</b>	<b>0.21</b>	<b>0.27</b>	<b>0.23</b>	<b>0.24</b>
<b>EPS from continuing operations (AED)</b>	<b>0.18</b>	<b>0.18</b>	<b>0.21</b>	<b>0.24</b>	<b>0.23</b>	<b>0.24</b>
<b>Cash Flow (AED Mn)</b>	<b>2020</b>	<b>2021</b>	<b>2022</b>	<b>2023E</b>	<b>2024E</b>	<b>2025E</b>
Net cash from operating activities	629	1,316	1,355	1,299	1,243	1,290
Net cash (used in) from investing activities	(2,595)	(977)	(214)	(101)	(292)	176
Net cash from (used in) financing activities	3,051	(455)	(565)	(1,262)	(754)	(716)
Change in cash and cash equivalents	1,086	(116)	576	(64)	198	750
FX and other adjustments	0	0	0			
<b>Cash at the end of the year</b>	<b>1,313</b>	<b>1,197</b>	<b>1,773</b>	<b>1,709</b>	<b>1,907</b>	<b>2,657</b>

Source: Kamco Invest Research and Tabreed

<b>Valuation &amp; Financial Ratios</b>						
<b>Ratios</b>	<b>2020</b>	<b>2021</b>	<b>2022</b>	<b>2023E</b>	<b>2024E</b>	<b>2025E</b>
<b>Leverage Ratios</b>						
Total Debt / Total Assets (x)	0.50	0.49	0.47	0.43	0.42	0.40
Total Debt / Equity (x)	1.13	1.13	1.01	0.86	0.81	0.77
Net Debt/Equity (x)	0.90	0.94	0.76	0.64	0.57	0.44
<b>Operating Efficiency &amp; Liquidity Ratios</b>						
Receivables Turnover Ratio (%)	2.3	2.5	2.8	2.5	2.5	2.5
Payables Turnover Ratio (%)	2.9	2.9	3.0	3.0	3.0	3.0
Cash conversion cycle	29.2	21.2	8.6	22.2	23.7	23.4
Total Assets Turnover Ratio (x)	0.13	0.14	0.15	0.15	0.16	0.16
Current Ratio (x)	3.88	2.63	3.75	3.89	4.03	4.80
<b>Margins &amp; Profitability Ratios</b>						
Adjusted Gross profit margin (%)	60.8%	57.6%	60.5%	61.1%	61.1%	61.1%
EBITDA margin (%)	55.7%	52.8%	55.6%	55.5%	55.2%	54.9%
EBIT margin (%)	36.2%	31.9%	36.2%	35.9%	36.2%	36.8%
Net profit margin (%)	29.8%	26.0%	27.1%	28.9%	26.9%	27.4%
Return on Assets (%)	4.1%	3.9%	3.9%	5.1%	4.3%	4.4%
Return on Equity (%)	9.4%	9.1%	8.4%	10.3%	8.2%	8.4%
ROIC (%)	6.2%	6.1%	6.2%	7.5%	6.5%	6.8%
<b>Per Share Data and Valuation Ratios</b>						
Earnings Per Share (AED)	0.18	0.18	0.21	0.24	0.23	0.24
Book Value Per Share (AED)	2.12	2.27	2.52	2.67	2.78	2.91
Dividend Per Share (AED)	0.06	0.06	0.13	0.15	0.15	0.16
PE (x)	13.9	13.8	14.0	15.6	16.1	15.2
EV/EBITDA (x)	12.8	12.7	11.3	11.9	11.3	10.2
PB (x)	1.2	1.1	1.2	1.4	1.3	1.3
Dividend Yield (%)	2.3%	2.4%	4.6%	4.2%	4.0%	4.3%

Source: Kamco Invest Research and Tabreed

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