

## Air Transport

**Maintain BUY: 12M TP @ 2.636**

### Valuation Summary (TTM)

Price (AED)	2.320
PER TTM (x)	8.5
P/Book (x)	1.7
P/Sales (x)	2.0
EV/Sales (x)	1.4
Dividend Yield (%)	6.5
Free Float (%)	56%
Shares O/S (mn)	4,667
YTD Return (%)	8%
Beta	0.8

(mn)	AED	USD
Market Cap	10,827	2,948
Total Assets	8,494	2,313

Price performance (%)	1M	3M	12M
Air Arabia PJSC	9%	1%	13%
Dubai Financial Market Gen	5%	4%	-1%

Trading liquidity (,000)	1M	3M	6M
Avg daily turnover (AED ,000)	8,822	13,879	10,445
Avg Daily Volume (,000)	6,103	6,283	4,768

52 week	High	Low	CTL*
Price (AED)	2.41	1.82	27.5

\* CTL is % change in CMP to 52wk low

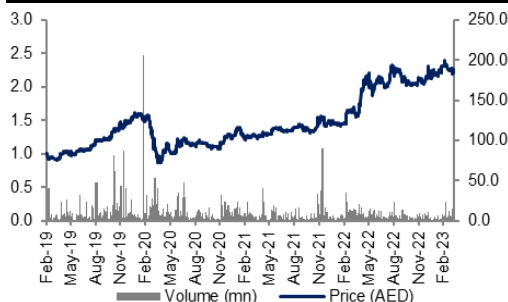
### Major shareholders

Sharjah Asset Manage	19%
EAST & WEST INTERNAT	16.1%
AL Maha Holding Co F	9.2%
Others	56.1%

### Other details

Exchange	DFM
Sector	Airlines
Index weight (%)	6.3%

Key ratios	2020	2021	2022
EPS (AED)	-0.04	0.15	0.26
BVPS (AED)	0.97	1.30	1.50
DPS (AED)	0.00	0.09	0.15
Payout ratio (%)	0%	57%	58%



## Air Arabia – Inline results

Air Arabia reported 1Q23 net income of AED 341.7 million, in line with our estimates and higher by 17.5% y/y. The revenue for the year came in at AED 1.43 bn which was higher by 26.6% as compared to the previous year. Revenue grew as a result of a significant rise in passenger traffic during the quarter. Total passengers carried by Air Arabia rose by 58.8% to 3.94 million out of which 2.5 million passengers were from the Sharjah hub and remaining from other hubs. The airlines added 9 new routes during the quarter. Gross margin witnessed 269bps decline during the 1Q23 compared to 1Q22, primarily on account of oil price volatility and lower yields. The operating profit margin also decreased to 21.1% in 1Q23 compared to 1Q22 level of 24.9% as a result of an increase in administration expenses during the quarter. EBIDTA margins however witnessed a rise to 32.3% during the quarter as depreciation rose significantly in 1Q23. The high cash levels which were parked in the bank as deposits provided a finance income of AED 40 million during the quarter. Cash was also utilized to reduce some component of the debt resulting in a lower finance cost. Due to the lower finance cost and finance income net margins held at 23.9% albeit marginally lower by 189bps compared to the same period the previous year. The company paid out AED 0.15 per share as dividends post our coverage and currently trade at AED 2.27 which is the level we had recommended to BUY. Based on the latest results we remain positive with no change in our forecast, valuation or target price. At current levels the shares trade at FY23e P/E of 7.5x, 1.4x book value, and offers a dividend yield of 6.8%. We maintain our BUY recommendation with target price of RO 2.636, offering potential return of 16.3%.

**Passenger growth robust:** Airline industry has recovered completely from the covid related issues. Passenger growth is in full swing across the industry and visible in all major airlines in the world. Middle east being one of the fastest growing markets for air travel has been a big beneficiary of this upswing. Air Arabia witnessed a stupendous increase in passengers by 58.8% YoY and 7.6% QoQ. Despite the seasonality in passenger traffic and 1Q being the weakest quarter, the company reported a sequential growth in passengers. Air Arabia currently has a fleet size of 68 aircraft and flies to over 260 destinations including the 9 new routes added during 1Q23. The load factor rose to 85%, a level not seen in the past. We are confident that Air Arabia passenger growth will surpass industry and reach our estimate of 18.9million passengers for the full year 2023.

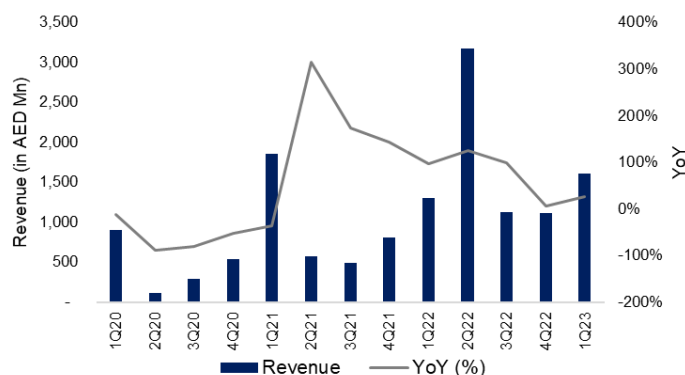
**Revenue in line with estimates:** The rise in passenger growth led to a 26.6% YoY increase in revenue. On a sequential basis as well, the revenue grew by 2.6%. We have been witnessing a decreasing trend in yields since 2Q21. However, we see the decline in yield only as a reversion to mean. Yields had spiked to AED 527/pax in 2Q21 and have declined to AED 362/pax as of 1Q23, in line with the levels of 2019. We believe yields have normalized and will remain in the current range going forward. Competition has also increased in the region with more airlines participating to capture market share. Air Arabia will have to carefully balance the yields and maintain its market share going forward.

**Margins have contracted:** At a gross level margins declined by 269bps compared to the same period the previous year and 300bps compared to 4Q22. This is a result of the volatility in fuel costs which were not effectively passed on to the customers. The decline in margin is visible across the industry and not isolated to Air Arabia. We do not see any further erosion of margins in Air Arabia as oil prices have been partially hedged and the management has effectively managed the margins within a narrow range over the past several quarters. Operating margins were at 21.1%, a decline by 379bps on account of higher admin expenses incurred to manage the rising passenger traffic. At the EBIDTA level margins declined by 420bps on a YoY basis, however they rose by 90bps on QoQ as a result of higher depreciation. The total depreciation charge for the quarter was reported at AED 158 million compared to AED 131 million in 1Q22 and AED 141 million in 4Q22. At the net level, margins for 1Q23 were at 23.9%, lower by 187 bps compared to 1Q22.

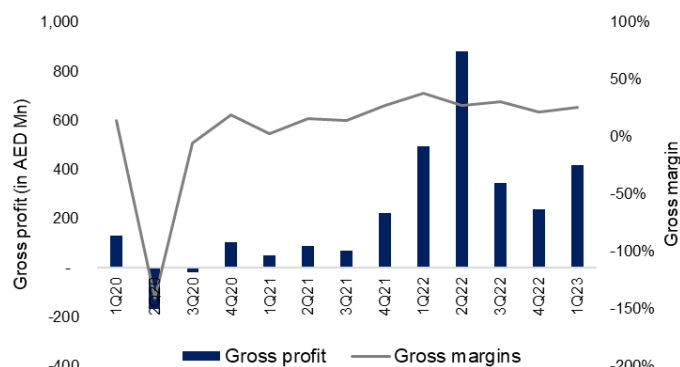
**Cash position stable:** Air Arabia has always been a cash rich company. Despite a dividend payout of AED 700 million during the quarter, and AED 188million as advances for new aircraft during the quarter, the cash levels rose to AED 5billion compared to AED 4.7 billion in 4Q22 and AED 3.9 billion in 1Q22. We find this extremely positive and believe the advance bookings for the next few months have been robust. During the quarter the excess cash deployed in the banks provided interest income of AED 40.8 million, which partially offset the decline in margins at the net level. Net borrowings declined by AED 3.15 million while finance costs reduced to AED 26 million in 1Q23 from AED 30 million in 4Q22.

**Recommendation:** Air Arabia has been a consistent performer in the past. The management has maintained a measured approach towards expansion after due consideration of the scalability. Operational costs and cash position have remained consistent throughout the past. The load factor reaching 85% is a testament to the fact that the choices of routes have been well received. The increasing contribution to passenger traffic from hubs other than Sharjah is also a vindication of successful selection of locations. We believe the airline is on track to report another record year in revenue and profit. The fleet size is expected to rise significantly post 2025 as the company takes delivery of 120 new aircraft. We remain positive on the company and maintain our forecast, valuation, and target price, this will be reviewed post the 2Q23 results. At the current price the stock trades attractively at 7.5x 2023e PE with a dividend yield of 6.8%. We recommend BUYING the stock with a target price of AED 2.636.

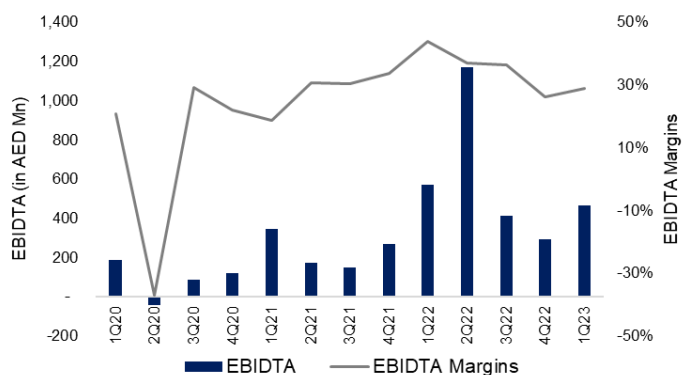
1Q23 Revenue growth in line with expectations



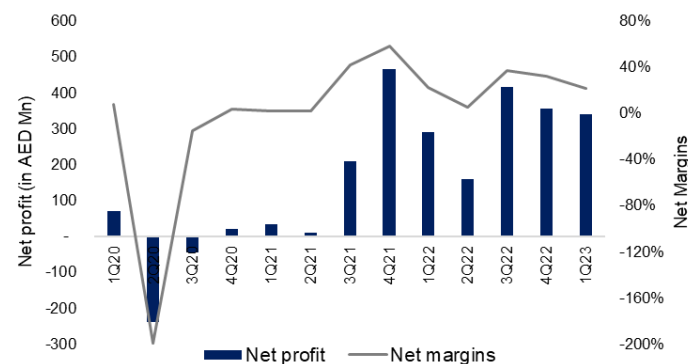
Gross margins remain stable despite fuel price volatility



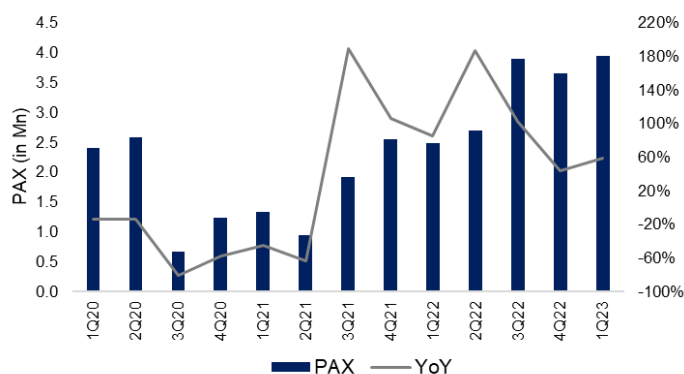
EBIDTA margins inches upwards on higher depreciation



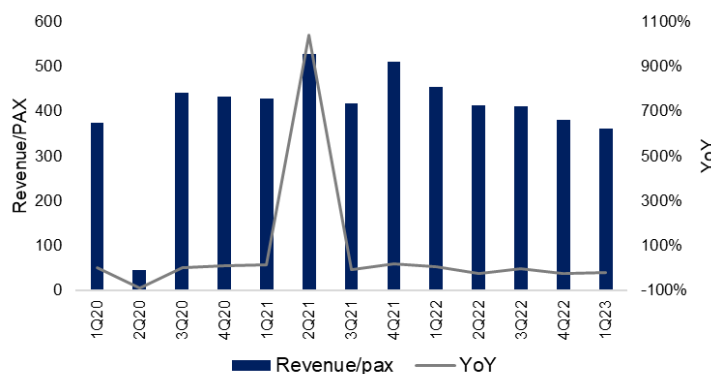
Net margins decline marginally, YoY growth robust



Highest number of PAX in a single quarter



PAX yields are reverting to mean post a spike during covid



Income Statement (in AED Mn)	2019	2020	2021	2022	2023e	2024e	2025e	2026e
Revenue	4,758	1,851	3,174	5,242	6,136	7,239	8,347	9,548
Direct Costs	3,509	1,800	2,291	3,810	4,418	5,249	6,093	6,970
<b>Gross Profit</b>	<b>1,249</b>	<b>51</b>	<b>883</b>	<b>1,432</b>	<b>1,718</b>	<b>1,991</b>	<b>2,254</b>	<b>2,578</b>
Admin and general expenses	233	196	198	286	337	398	459	525
Selling and marketing expenses	83	34	41	68	92	109	125	143
Operating profit	933	-180	643	1,077	1,289	1,484	1,669	1,910
<b>EBIDTA</b>	<b>1,461</b>	<b>347</b>	<b>1,171</b>	<b>1,609</b>	<b>1,821</b>	<b>2,082</b>	<b>2,335</b>	<b>2,642</b>
EBIT	933	-180	643	1,077	1,289	1,484	1,669	1,910
Finance income	96	102	63	89	90	101	104	113
Finance costs	129	138	138	115	102	98	105	119
Share of profit / (loss) of associates	32	-16	90	36	37	36	34	33
Other income / (expense) -net	76	40	62	136	90	101	104	113
PBT	1,008	-192	720	1,222	1,404	1,625	1,806	2,048
Tax	-	-	-	-	-	146	163	184
<b>PAT</b>	<b>1,008</b>	<b>-192</b>	<b>720</b>	<b>1,222</b>	<b>1,404</b>	<b>1,478</b>	<b>1,644</b>	<b>1,864</b>
Balance Sheet (in AED Mn)	2019	2020	2021	2022	2023e	2024e	2025e	2026e
Property, plant and equipment	6,866	6,367	5,868	5,403	4,955	5,617	6,246	6,808
Right-of-use assets	369	575	624	645	689	807	856	929
Intangible assets	1,312	1,324	1,332	1,338	1,338	1,338	1,338	1,338
Other non-current assets	652	635	840	1,419	1,569	1,800	2,042	2,312
<b>Total non-current assets</b>	<b>9,199</b>	<b>8,902</b>	<b>8,665</b>	<b>8,805</b>	<b>8,551</b>	<b>9,562</b>	<b>10,482</b>	<b>11,387</b>
Current inventories	23	26	24	33	44	39	30	42
Trade and current receivables	617	527	739	863	1,350	1,632	1,928	2,258
Cash and bank balances	2,806	3,149	3,878	4,736	5,000	5,222	5,992	7,193
Other current assets	168	50	-	-	-	-	-	-
<b>Total current assets</b>	<b>3,615</b>	<b>3,751</b>	<b>4,641</b>	<b>5,632</b>	<b>6,395</b>	<b>6,894</b>	<b>7,951</b>	<b>9,493</b>
<b>Total Assets</b>	<b>12,814</b>	<b>12,653</b>	<b>13,306</b>	<b>14,437</b>	<b>14,945</b>	<b>16,456</b>	<b>18,433</b>	<b>20,880</b>
Share capital	4,667	4,667	4,667	4,667	4,667	4,667	4,667	4,667
Reserves	549	33	1,003	1,320	1,320	1,320	1,320	1,320
Retained earnings	342	-192	405	1,008	1,712	2,491	3,434	4,598
Total Equity to shareholders	5,558	4,508	6,075	6,995	7,699	8,477	9,421	10,585
Non controlling interests	-	-	-	1	1	1	1	1
<b>Total equity</b>	<b>5,558</b>	<b>4,508</b>	<b>6,075</b>	<b>6,996</b>	<b>7,700</b>	<b>8,478</b>	<b>9,421</b>	<b>10,585</b>
Provision for staff benefits	145	131	145	170	202	239	275	315
Trade and other payables	1,061	1,766	1,350	1,407	1,590	1,863	2,130	2,398
Bank Borrowings	-	-	-	31	-	-	-	-
Finance Lease liabilities	3,165	3,073	2,584	2,126	2,003	1,919	2,053	2,347
<b>Total non-current liabilities</b>	<b>4,371</b>	<b>4,970</b>	<b>4,079</b>	<b>3,734</b>	<b>3,796</b>	<b>4,021</b>	<b>4,459</b>	<b>5,061</b>
Deferred income	352	301	492	514	514	514	514	514
Trade and other payables	1,654	1,662	1,970	2,462	2,386	2,914	3,476	4,084
Bank Borrowings	352	552	38	109	50	50	50	50
Current lease liabilities	528	660	652	622	501	480	513	587
<b>Total current liabilities</b>	<b>2,885</b>	<b>3,175</b>	<b>3,153</b>	<b>3,707</b>	<b>3,450</b>	<b>3,957</b>	<b>4,553</b>	<b>5,234</b>
<b>Total equity and liabilities</b>	<b>12,814</b>	<b>12,653</b>	<b>13,306</b>	<b>14,437</b>	<b>14,945</b>	<b>16,456</b>	<b>18,433</b>	<b>20,880</b>

Ratio Analysis	2019	2020	2021	2022	2023e	2024e	2025e	2026e
<b>Per Share</b>								
EPS (AED)	0.212	-0.041	0.154	0.262	0.301	0.317	0.352	0.399
BVPS (AED)	1.191	0.966	1.302	1.499	1.650	1.817	2.019	2.268
DPS (AED)	0.000	0.090	0.085	0.150	0.150	0.150	0.150	0.150
FCF per share (AED)	0.073	0.229	0.360	0.217	-0.051	0.231	0.279	0.339
<b>Valuation</b>								
Marketcap (AED Mn)	7,373	5,973	6,767	10,033	10,267	10,267	10,267	10,267
EV (AED Mn)	8,612	7,109	6,163	8,185	7,820	7,494	6,891	6,058
EBITDA (Mn)	1,461	347	1,171	1,609	1,821	2,082	2,335	2,642
P/E (x)	7.45	-31.08	9.40	8.21	7.32	6.95	6.25	5.51
EV/EBITDA (x)	5.89	20.50	5.26	5.09	4.29	3.60	2.95	2.29
Price/Book (x)	1.33	1.33	1.11	1.43	1.33	1.21	1.09	0.97
Dividend Yield (%)	0.0%	7.0%	5.9%	7.0%	6.8%	6.8%	6.8%	6.8%
Price to sales (x)	1.55	3.23	2.13	1.91	1.67	1.42	1.23	1.08
EV to sales (x)	1.81	3.84	1.94	1.56	1.27	1.04	0.83	0.63
<b>Liquidity</b>								
Cash Ratio (x)	0.97	0.99	1.23	1.28	1.45	1.32	1.32	1.37
Current Ratio (x)	1.25	1.18	1.47	1.52	1.85	1.74	1.75	1.81
Quick Ratio (x)	1.24	1.17	1.46	1.51	1.84	1.73	1.74	1.81
<b>Returns Ratio</b>								
ROA (%)	7.9%	-1.5%	5.4%	8.5%	9.4%	9.0%	8.9%	8.9%
ROE (%)	18.1%	-4.3%	11.9%	17.5%	18.2%	17.4%	17.4%	17.6%
ROCE (%)	10.2%	-2.0%	7.1%	11.4%	12.2%	11.8%	11.8%	11.9%
<b>Cash Cycle</b>								
Inventory turnover (x)	149.4	70.4	97.5	116.4	100.0	133.3	200.0	166.7
Accounts Payable turnover (x)	1.3	0.5	0.7	1.0	1.1	1.1	1.1	1.1
Receivables turnover (x)	7.7	3.5	3.7	4.3	2.5	2.4	2.4	2.3
Inventory days	2.4	5.2	3.7	3.1	3.7	2.7	1.8	2.2
Payable Days	282.4	695.0	528.9	370.7	328.5	332.2	335.8	339.5
Receivables days	47.3	103.9	97.8	85.8	146.0	149.7	153.3	157.0
Cash Cycle	-232.6	-586.0	-427.4	-281.7	-178.9	-179.8	-180.7	-180.3
<b>Profitability Ratio</b>								
Net Margins (%)	21.2%	-10.4%	22.7%	23.3%	22.9%	20.4%	19.7%	19.5%
EBITDA Margins (%)	30.7%	18.7%	36.9%	30.7%	29.7%	28.8%	28.0%	27.7%
PBT Margins (%)	21.2%	-10.4%	22.7%	23.3%	22.9%	22.4%	21.6%	21.4%
EBIT Margins (%)	19.6%	-9.7%	20.3%	20.5%	21.0%	20.5%	20.0%	20.0%
Effective Tax Rate (%)	0.0%	0.0%	0.0%	0.0%	0.0%	9.0%	9.0%	9.0%
<b>Leverage</b>								
Total Debt (AED Mn)	4045	4284	3274	2888	2554	2449	2616	2984
Net Debt (AED Mn)	1238	1135	-604	-1848	-2447	-2772	-3376	-4209
Debt/Capital (x)	0.87	0.92	0.70	0.62	0.55	0.52	0.56	0.64
Debt/Total Assets (x)	0.32	0.34	0.25	0.20	0.17	0.15	0.14	0.14
Debt/Equity (x)	0.73	0.95	0.54	0.41	0.33	0.29	0.28	0.28

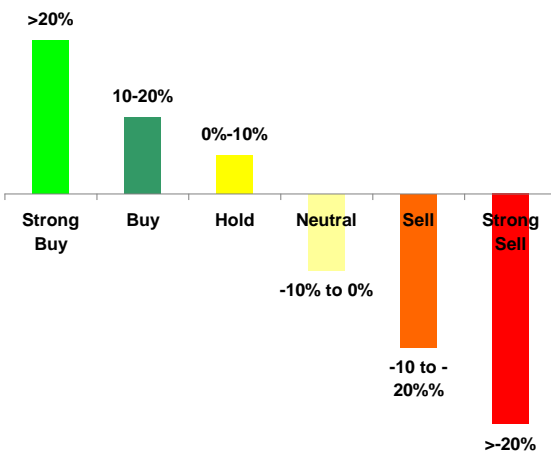
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## Rating Criteria and Definitions

### Rating



### Rating Definitions

<b>Strong Buy</b>	This recommendation is used for stocks whose current market price offers a deep discount to our 12-Month target price and has an upside potential in excess of 20%
<b>Buy</b>	This recommendation is used for stocks whose current market price offers a discount to our 12-Month target price and has an upside potential between 10% to 20%
<b>Hold</b>	This recommendation is used for stocks whose current market price offers a discount to our 12-Month target price and has an upside potential between 0% to 10%
<b>Neutral</b>	This recommendation is used for stocks whose current market price offers a premium to our 12-Month target price and has a downside side potential between 0% to -10%
<b>Sell</b>	This recommendation is used for stocks whose current market price offers a premium to our 12-Month target price and has a downside side potential between -10% to -20%
<b>Strong Sell</b>	This recommendation is used for stocks whose current market price offers a premium to our 12-Month target price and has a downside side potential in excess of 20%
<b>Not rated</b>	This recommendation used for stocks which does not form part of Coverage Universe

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