National Central Cooling Co. (PJSC)
(DFM: TABREED)

Q4 and Full Year 2019
Earnings Conference Call Transcript

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Tabreed Participants:

Bader Al Lamki, Chief Executive Officer

Jean-Francois Chartrain, Chief Operating Officer

Richard Rose, Chief Financial Officer (Acting)

Souad Jamal AlSerkal, Vice President - Strategic Communications

Presentation

Operator
Ladies and gentlemen, welcome to Tabreed's Fourth Quarter 2019 Earnings Call. I hand over the call to your host, Ms. Souad, Vice President of Strategic Communications. Madame, please go ahead.

Souad Jamal Al Serkal
Hi, this is Souad Jamal Al Serkal, Vice President of Strategic Communications at Tabreed. On behalf of Tabreed's management team, I would like to welcome you all, and thank you for joining us for the fourth quarter and full year 2019 results conference call.

Before we begin our presentation, I would like to remind you that some of the statements made in today's conference call may be forward-looking in nature and may involve risks and uncertainties. Kindly refer to slide two of the presentation for the detailed disclaimer. I would now request you to turn to slide number three for today's agenda.

On today's call, we have with us Mr. Bader Al Lamki - Chief Executive Officer, Jean-Francois (JF) Chartrain - Chief Operating Officer, and Richard Rose, acting CFO. Bader will first provide the highlights of 2019. Following that, JF will provide an overview of the recent events and operational performance. Richard will then discuss the financial performance in more detail. Bader will then conclude the presentation, and we will open the lines for your questions.

Thank you, and over to you, Bader.

Bader Al Lamki
Thank you, Souad. Thank you, everyone, for joining us today.

Tabreed delivered another strong year, with a robust financial and operational performance, which was driven by our strategic growth initiatives. Key highlights of our performance in 2019 can be summarized as follows. The full year 2019 revenues grew by 5.1% year-on-year, led by a 7% increase in the chilled water revenues. 2019 has seen a 10% increase in EBITDA, and as a result, our EBITDA margins grew as well from 48% last year to 50% in 2019.

We saw strong capacity addition during Q4 of 21,500 RTs, mostly across the UAE and Saudi Arabia. Tabreed also added five plants during the quarter, taking our total plants to 80 across the region. Total capacity additions throughout the year has been 51,300 RTs, of which 7,500 RTs were on the account of the recent acquisition of Masdar, two plants.

Our annual guidance for capacity growth relates only to organic growth. In this regard, we guided addition of 65,000 RTs over 2019 and 2020. We have delivered 44,000 RTs already of organic growth, achieving 67% of our target in the first year alone.

I would like to outline our revised capacity guidance for the next two years. Based on our current signed contracts in hand, we expect to connect at least 75,000 RTs of new capacity over 2020 and 2021. This guidance updates and replaces the guidance we gave a year ago.

Finally, as per our policy of growing dividends in line with the growth of the business, the board has proposed a dividend distribution of 10.5 fils, which is a one fils or 11% higher than the last year dividend distribution. This represents a consistent payout ratio of around 60%.

I will now hand over to JF.

Jean-Francois Chartrain
Thank you, Bader.

We are moving onto slide number six. This slide highlights the results of the initiatives undertaken by our business developments and operations team. Our growth during the year was a combination of greenfield projects, new connections to existing customers, as well as acquisition. It is important to note that our inorganic initiatives were all funded through the internally generated cash, which underpins the strength of our business model.

During the year, we added six new plants, taking our total number of plants across the region to 80. This includes a 20k RT plant at the King Khalid International Airport in Saudi Arabia, the 8.4k RT plant at the Mall of Muscat in Oman, two plants acquired from Masdar in UAE, and two new plants for existing customers also in UAE.

Tabreed acquired two plants from Masdar with current connected capacity of 7.5k RT and a potential to reach 11.2k RT in the near-term. This acquisition provides us with future growth opportunity of adding up to 69,000 RT under the concession agreement with Masdar.

Our acquisition of additional stake in Saudi Tabreed further strengthens our position as a leading international district cooling developer in one of the largest district cooling markets in the region.

Our partnership with Bee'ah is aimed at exploring opportunities to bring reliable, sustainable and cost-efficient district cooling solution to the Emirates of Sharjah.

Tabreed has initiated an ambitious multiyear efficiency and productivity program, and I'm pleased to report that it has already started yielding results. Water and energy efficiency performance in 2019 is encouraging, and we have now seen some meaningful cost savings.

Tabreed adheres to international standards of safety and operational excellence. We achieved in 2019, 10 million man hours without LTI. This was a result of continued HSE focus.

Strong operational performance and growth prospects, both in existing core markets of the UAE and GCC and in new geographies, will enable Tabreed to continue creating value for all our stakeholders.

Now, moving to slide number seven. We are providing the usual overview of the company. Tabreed is contributing to the region’s growth through efficient and environmentally-friendly cooling, enabling sustainable development. As our business grows, so does our positive environmental footprint. We currently operate 80 plants across the region and delivering 1.18 million refrigeration tons to our clients. Our operations, saved in 2019, over

2 billion kilowatt hours of energy consumption. It is enough to power 117,000 homes for a year and equivalent to reducing over 1.2 million tons of CO_2 emissions.

Moving onto the next slide. Tabreed is the only publicly-traded and regional district cooling company in the world. The UAE is our base of operations, where we have a presence in six emirates, providing 795,000 tons of cooling to our customers through 67 plants. In addition to the UAE, we work with key strategic partners in four other GCC countries. We have a total of 13 plants outside of UAE, providing over 388,000 tons of cooling to customers. During the fourth quarter, we added five new plants across the region, taking our total number of plants to 80. Around two-thirds of our capacity is consolidated, while the rest is equity accounted for as associates and joint ventures.

Moving to next slide. It outlines our capacity growth trends across the region. At the beginning of 2019, we announced that we expected to add at least 65,000 RTs of new connected capacity by 2020. In fact, during 2019, we added 51,300 RTs of capacity across the region. Of this capacity, 31,400 were added at the consolidated level and 20,000 RTs through joint venture and associate entities.

As I have already mentioned, based on the current signed contracts in hand, we expect to connect 75,000 tons of capacity over 2020 and 2021. Of this, we expect the split between consolidated level and equity accounted with joint ventures to be 65/35%.

I will now move onto the next slide, number 10. This slide presents the guidance and the connection trend. Over the years, Tabreed has demonstrated a track record of delivering upon its guidance. We have delivered more than half of the guided capacity additions in the first year itself.

In 2019, Tabreed registered organic capacity additions of 67% or 44,000 RTs of the guided 2019/2020 capacity of 65,000 RTs provided last year. Our revised capacity guidance is now to add 75,000 RTs over 2020 and 2021. We continue to demonstrate our ability to deliver a steady increase in connected capacity in the region, driven by the growth in our key markets across the GCC and by successfully leveraging our regional network, to take advantage of commercial opportunities as and when they present themselves.

I will now hand over to Richard to talk about our financial results in more detail.

Richard Rose
Thank you, JF and welcome everybody to this year's annual presentation of the results.

This slide, 11, recaps our evolution of the performance of Tabreed over the years. And to summarize, Tabreed is a stable utility infrastructure business with long-term contracts and high-profile customers. This provides us with clear visibility of future earnings and cash flows, and we currently have 90% of our capacity contracted for at least the next 10 years. About 70% of our revenues are derived from Government-owned and partly Government-owned organizations, therefore, limiting our counterparty risks.

Tabreed has a track record of delivering profitable growth, and net income and EBITDA have increased by 9% per year since 2016. Our stable earnings enable Tabreed to maintain an attractive dividend payout. In line with our commitment to provide sustainable returns to our shareholders, the proposed dividend of 10.5 fils represents a 60% payout in line with last year.

I'll now turn to talk to you about the financial results in a bit more detail.

On slide 13 we have the income statement. Tabreed recorded an overall revenue growth of 5.1% with chilled water revenue increasing by 7%. The main factors driving chilled water revenue growth were consumption revenue growth of over 2%, new capacity in the UAE and Oman adding 1.3%, CPI adjustments on the capacity revenues from the beginning of the year added just over one percentage point and acquisition and consolidation of S&T in Q1 2018 made up the remaining.

In a relatively difficult economic scenario, consumption growth reflects the resilience of our core business model.

Value chain businesses accounted for 4% of consolidated revenues and 1% of EBITDA. VCBs are non-core to the business but continued to be profitable.

Gross margin improvement was a combination of IFRS 16 and efficiency gains as discussed by JF earlier.

IFRS 16 implementation resulted in reclassification of operating expenses in 2019, with depreciation of AED 20 million and finance costs of AED 17 million. Both depreciation and finance costs do not form part of EBITDA, which results in a slightly higher EBITDA margin in 2019.

Other gains this year include AED 27 million on account of initial recognition of new finance leases in both the UAE and Oman. And last year, we included the AED 32.6 million, gain arising on the sale of our partial sale of our stake in Saudi Tabreed. Net income adjusted for all other gains would have grown by 16%.

Turning now to slide 14, the statement of financial position. The significant movements in the balance sheet as of the end of the year compared to last year were primarily due to IFRS 16. This increased fixed assets due to the recognition of right-of-use assets, formerly known as operating lease assets. We've also seen strong receivables collection. Receivables compared to December 2018 were in line with revenue growth and actually down compared to our Q3 September 2019 results. Increase in corporate debt is primarily due to increase in lease liabilities on account of IFRS 16. We continue to deleverage and adjusted for IFRS 16 impact, the total debt reduced by AED 143 million year-on-year.

Turning now to the cash flow statement slide, 15. Tabreed continues to generate strong cash flows, which are being utilized to invest in growth and provide dividend returns to the shareholders. Operating cash flow increased by 18% over December 2018 and was strong at AED 782 million, which reflects the higher profitability of the business. Dividends received were higher last year than this year due to the special dividend that we received from Saudi Tabreed at the time of the dilution of our stake. Investing activity this year also included increase in our stake of Saudi Tabreed again and last year reflected the acquisition of S&T Cool.

Our cash-generating ability remains robust, driven by the long-term price certain contracts and enabling continued investment in growth of the business.

Slide 16 is the usual summary of our debt portfolio. This slide provides the background as at December 2019. Tabreed currently has AED 2.9 billion of net debt and a gearing ratio of 39%. However, it's important to note that IFRS 16 has increased reported debt by AED 295 million and net debt-to-EBITDA by 0.2 times. Excluding this impact of the accounting standards, both net debt and net debt-to-EBITDA are lower than last year.

Following the refinancing of our corporate facilities with a seven-year Sukuk and new corporate loans, we have relatively light scheduled repayments until 2025 when the Sukuk becomes due for repayment. Net debt and net debt-to-EBITDA have declined since 2016, as debt has been repaid and EBITDA has grown.

That concludes the detailed review of the results for 2019, and I'll now pass back to Bader for closing comments.

Bader Al Lamki
Thank you, Richard. Before we open the lines for Q&A, let me make a few closing remarks.

As a stable utility business model, Tabreed continues to deliver strong financial and operating performance, with rising profitability, stable margins and robust cash flows. In line with our commitment to enhance shareholders' return, our board has recommended a dividend of 10.5 fils per share for 2019, translating into a 60% payout.

In January 2019, we provided capacity addition guidance of 65,000 tons to be added over the coming two years and delivered 51.3 RTs during the year. We have now updated the guidance to add 75,000 tons over 2020 and 2021.

Tabreed has a flexible capital structure to fund future growth. As we have mentioned before, we will look at opportunities within and beyond the GCC, and provide you with an update as and when such opportunities materialize.

Today, Tabreed is stronger than ever before. We have a stronger shareholder base and management team with significant industry experience that spans over 22 years. We are working on various fronts, from business development to operation, to deliver growth and improved profitability.

Souad Jamal Al Serkal
Thank you for joining us for our fourth quarter and full year 2019 earnings call. We will now take any questions you may have.

Questions & Answers

Operator
[Operator instructions]
The first question comes from Divye Arora from Daman Investments. Please go ahead.

Divye Arora
So what we have seen is that there is a strong growth in the revenues in the Q4. The revenues are up around 10-11%. Can you please explain what is behind the strong growth, other than the CPI and the consumption growth? Is there any one-off there in the revenues?

The second question is, on a net income level, if you adjust for the one-off gains, so the income has grown by around 16% versus last year. Is there any impact of IFRS 16 on the net income? If you strip that out, then what is the growth on a like-for-like basis? And what is the impact on the net margins of the operating efficiencies that you have achieved? Thank you.

Richard Rose
With regard to the Q4 growth in revenue, there is a one-off in there, which is around AED 25 million. And that's arising from settlement of some issues that we have with one of our customers over some service commencement dates, which go back over a quite a long period of time. We managed to resolve those all at once quite unexpectedly, but very successfully, and that resulted in us recognizing an additional, just over AED 25 million of revenue in Q4. That won't be repeated again, we don't have any other issues like that.

Divye Arora
This is basically something which you've never recognize as a revenue before?

Richard Rose
Yes. That's right. That's correct. And then with regards to IFRS 16, that doesn't have any impact on net income. It reclassifies the costs associated with operating leases within the income statement onto different lines, so it can have some impact on the margin levels higher up in the income statement but doesn't have any impact on the bottom line net income.

Divye Arora
So this growth we have seen in the net income of 16%, if you strip out the other gains and losses, so this is coming obviously from the revenue growth. If we strip out even the one-off revenue, how much of the cost attached to that revenue, the one-off, which you've have taken AED 25 million? Is there a cost attached or is this just flowing into net income directly?

Richard Rose
No. It's just flowing down, Divye. There is no cost associated with that.

So to answer your last question. With regard to the efficiencies, I think we're at the beginning of, hopefully, what's a long journey in terms of operational improvement and using automation to try and develop the way that we run our business to make it as efficient as possible. I think what we can say now is that in the 2019 results, we're looking at a low double-digit impact on the net income level from the efficiency gains that we've made in 2019.

Divye Arora
Sorry. Low double-digit impact?

Richard Rose
And we would expect those to be recurring. Yes, that's correct.

Divye Arora
So if you strip out the one-off impact of this revenue, and take out the other gains and losses from both 2018 and 2019. So your income is growing by around 9%, which shows the impact of the growth in revenue, plus the margin increase together.

Richard Rose
Yes. That's correct.

Operator
[Operator instructions]
There are no further questions in the conference call. I will now give back the floor to the company. Thank you.

Conclusion

Souad Jamal Al Serkal
That concludes our full year 2019 earnings call. Tabreed looks forward to interacting with you at our earnings conference calls and investor conferences. Should you have any further questions, please do not hesitate to contact us.

Have a great day and thank you once again for joining this call.

Note: This transcript has been edited to improve readability

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