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

Q1 2021
Earnings Conference Call Transcript

9 May 2021

Tabreed Participants:

Adel Salem Al Wahedi, Chief Financial Officer
Richard Rose, Senior Vice President – Finance
Souad Jamal AlSerkal, Vice President – Strategic Communications

Presentation

Operator

Ladies and gentlemen, welcome to Tabreed's First Quarter 2021 Earnings Call. I hand over the call to your host, Ms. Souad Jamal Al Serkal, Vice President, Strategic Communications. Madam, please go ahead.

Souad Jamal Al Serkal

Thank you, and good afternoon, everyone. Once again, my name is Souad Jamal Al Serkal, the Vice President of Strategic Communications here at Tabreed. On behalf of Tabreed management team, I would like to welcome you all and thank you for joining us for the Q1 2021 results conference call. I hope you are all keeping safe and healthy. Now, given that we are all working remotely, kindly excuse us for any technical issues on the 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. Adel Al Wahedi, Chief Financial Officer, and Mr. Richard Rose, Senior Vice President of Finance. I will first touch upon the recent unveiling of the new branding and corporate identity, then Mr. Adel will provide us with an overview of the First Quarter 2021, performance and key events. Following that, Richard will discuss the financial performance in more detail. Finally, Adel will then conclude the presentation and we will open the lines for your questions. Moving on to the next slide.

In April 2021, Tabreed unveiled its all-new branding and corporate identity, ushering in an exciting new chapter in the story of one of the country's most promising companies. On 11th April, the new company brand identity lit up the night sky in downtown Dubai, during a spectacular lights and graphics show projected against the iconic Burj Khalifa. As the show drew to a conclusion, Tabreed's previous branding dramatically morphed into the all-new identity. Now, if you missed it on the day, you can surely watch it on our social media account, @tabreedae on Instagram. Tabreed's new corporate identity, built around essential for progress as a core brand positioning, is more closely aligned with the company's current strategy where business transformation and growth are at the forefront.

The branding is more modern and dynamic, bolder in look and feel, and able to accurately articulate the Company's role in society, that of a catalyst for change with progress as its central tenet which reflects Tabreed's core values. Thank you and over to you, Adel.

Adel Salem Al Wahedi

Thank you, Souad, and thank you, everyone, for joining us today. I would like to begin by highlighting our Quarter One 2021 performance. Total revenue grew by 21.5%, driven by chilled water business growth of 22.3%. During the same period, EBITDA growth was 27.3% and, as a result, our EBITDA margins expanded from 61% in Q1 2020 to 63% in Q1 this year. Net profit during Q1 this year increased by 4% comparing to 3% growth over the same period of last year, with a margin of 24% over this quarter.

The quarter was eventful as we completed acquisition and consolidation of Saadiyat Island, a district cooling asset. We also published our first ever ESG report in March 2021 and unveiled all-new branding and corporate identity for Tabreed, as you have seen. Moving on to the next slide.

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 are the largest district cooling providers in the region and currently operate 86 plants across the region, delivering over 1.4 million tons of cooling.

Our operations saved over 2.26 billion kilowatt hours of energy consumption in 2020, enough to power over 128,000 homes for a year and equivalent to reducing over 1.35 million tons of CO_2 emissions. Moving on to the next slide, please.

This slide outlines our capacity growth strength across the region for 2020 and 2021, we guided a capacity of 75,000 RT, which we are confident of achieving by end of this year. The first quarter has been slow in terms of new capacity addition, and expect faster growth in the remaining part of the year.

At the beginning of 2021, we announced that we expected to add at least 120,000 RT of new connected capacity by the end of 2022. Of this, we expect around 80% to be contributed by consolidated entities and the balance, 20%, from equity accounted entities. Again, we are confident of delivering this target.

Tabreed continues to demonstrate its ability to deliver a steady increase in connected capacity in the region, driven by the growth in our key markets across GCC and by successfully leveraging our regional network to take advantage of commercial opportunities as and when they present themselves. Moving on to the next slide, please.

This slide recaps the evolution of our performance over the years. To summarise, Tabreed is a stable utility infrastructure business with long-term contracts with high-profile customers. This provides clear visibility of our earnings and cash flow. We currently have almost 90% of our capacity contracted for at least the next ten years. About 80% of our revenues are derived from fully government-owned and partially government-owned organisations, therefore limiting counterparty risks.

Tabreed has a track record of delivering profitable growth, EBITDA has increased at a CAGR of 15% per year since 2018. All the three recent acquisitions of Downtown DCP, Masdar and Saadiyat Island district cooling assets have helped us build a strong platform for future growth opportunities. These M&As have added significant concession capacity which we anticipate to connect in coming years. I will now hand over to Richard to talk about our financial results in more detail.

Richard Rose

Thank you, Adel. If you'd turn to slide 12 in the deck, let me start by highlighting the key points on our income statement for Q1 2021. So, as Adel mentioned, revenue grew by 21.5%, primarily driven by the Chilled Water business, which recorded growth of 22.3% during the period.

The key factors driving that movement were the acquisition of Downtown DCP last year, which added 20%, and the acquisitions of Masdar and Saadiyat during the course of the quarter, which added 4%. And this was offset to some extent by the impact of negative CPI.

Value chain businesses accounted for 5% of consolidated revenues and less than 1% of EBITDA. VCBs are non-core businesses but they continue to be profitable. EBITDA for Q1 2021 grew by 27.3% and EBITDA margins for the period were 63% compared to 61% in the same period last year. This margin enhancement was primarily driven by the consolidation of Downtown DCP, Masdar and Saadiyat Island assets as well as some savings in G&A and some impacts from the accounting adjustment relating to CPI.

Finance cost for the period was higher due to the two new loans that we raised last year to fund the growth and the acquisitions of the Downtown asset and the Saadiyat Island concessions. The share of results of associates and joint ventures was down due to higher one-off gains in the previous year. Net profit for the period increased by 4% compared to last year. We'll now look at the statement of financial position on the next slide.

Here, we see an increase in the balance sheet, including fixed assets, intangible assets and accounts receivable, all of those primarily driven by the consolidation of the new acquisitions of Downtown DCP, Masdar and Saadiyat Island district cooling assets.

Receivables are in line with the year end, given the growth in our business in the last few months, and DSOs have remained stable since the year end. The higher liabilities balance reflects the dividend payable at the quarter end and the balance outstanding to Aldar for the acquisition of the Saadiyat concessions. Turning to the next slide, we'll take a look at the cash flow statement.

Given the current difficult economic scenario, our cash flow generation during the period has been strong. Improvement in cash flow from operating activities compared to the same quarter last year was primarily driven by the consolidation of the acquisitions. In addition, DSOs have stabilised since the year end and post-quarter end receipts indicate further improvement.

Capex outflows relate to the partial settlement for the acquisition of the Saadiyat Island district cooling assets in the quarter. And overall, Tabreed retained strong liquidity with significant closing cash balances at the end of the period of 745 million as well as an unutilised revolving credit facility of 590 million. Let me now turn to the slide on the debt portfolio.

This slide provides the usual background on Tabreed's debt portfolio as at the end of March 2021. Tabreed has 5.9 billion dirhams of net debt and a gearing ratio of 53% at the quarter end. The increase in net debt reflects the corporate facility used to fund the Downtown DCP acquisition, and the Q4 $500 million bond issuance which was partly used to fund the acquisition of the Saadiyat Island assets.

Both the Moody's and Fitch rating agencies reaffirmed their investment grade ratings following those two acquisitions and the bond issuance. That completes the detailed review of our results for Q1 2021. And I'll now pass back to Adel for closing comments.

Adel Salem Al Wahedi

Thank you, Richard. So, in March 2021, Tabreed published its first ESG report. Tabreed is a highly sustainable business, delivering significant power efficiencies compared to other cooling alternatives. Despite a challenging year, Tabreed continued to make considerable progress on its business objectives whilst also ensuring the health and safety of its staff across all its operational sites.

In a year unlike any other, the Company maintained business continuity whilst ensuring the health and safety of all staff and partners across all Tabreed's entities. This resilience combined with our commitment to the communities in which we operate, to our staff and customers, and to the highest levels of governance across our operations reflect our very strong ESG credentials.

On the next slide, before we open the lines for Q&A, let me summarise, please. As a stable utility business model, Tabreed continues to deliver a strong financial and operating performance with the rise in profitability and margins. Tabreed has a strong investor base and experienced management team, solid corporate governance and market-leading transparency, demonstrated by board composition, with over 50% independent directors, including the Chairman.

Tabreed has a flexible capital structure to fund the future growth. As we have mentioned before, we will look at opportunities within and beyond GCC and we'll provide you with updates as and when such opportunities materialise. We continue to work on various fronts, from business development to operations, to help drive growth and improve profitability. That concludes the presentation of our Q1 earnings. Thank you for your time today.

Questions & Answers

Operator
Our first question comes from Junaid Farooq of Frontier IM Partners. Junaid, your line is now open. Please go ahead.

Junaid Farooq
Thank you very much, gentlemen, for the presentation. This was very helpful. I have two question. The first one is on the debt capacity. If you can give some colour on, based on the current covenant, how much higher can you go from the current level of 5.8 times net debt to last 12 months EBITDA? That's one. And my second question is if you can give some colour on any divestment plans that you had earlier, notably, I think you were looking to exit Qatar, that would be very helpful. Thank you.

Richard Rose
Okay. Thank you, Junaid. So, two good questions. I think in terms of debt capacity, if you look at it in the context of a multiple of EBITDA, we're probably near that limit that we had. There isn't much more room for senior debt in the portfolio.

However, when we acquire these new businesses in this new market that we're facing at the moment where there is a lot of M&A opportunity, we are acquiring EBITDA at the same time, and it starts to flow from day one. So, I think there is still potential for us to grow quite significantly more and we are endeavouring to secure that growth as fast as we possibly can.

I think as far as your second question goes in relation to the divestment of QatarCool, all I can say on that is that yes, we have had some discussions with the other shareholders in Qatar. But at this point, we don't have anything further to announce in relation to any transaction that may be in the offing there.

Junaid Farooq
Okay, got it. Thank you very much.

Operator
Our next question comes from Yawar Saeed of International Securities Abu Dhabi. Your line is now open. Please go ahead, Yawar.

Yawar Saeed
Hi. Thank you for the presentation. My question is relating to operating cost.

Operator
Yawar, we are unable to hear your line very well. We have a chat question that is when this new investment platform entity in Singapore is going to be operational, what is the nature of this entity, and how would it be operated? That question comes from Pervez Ismael.

Richard Rose
Hi, it's Richard here. Thanks for the question in relation to the entity in Singapore. So I think as you know from the press release that we did, this is a partnership which is going to be 75% owned by Tabreed and 25% owned by IFC, who I'm sure you will know are part of the World Bank Group.

The intention is that any investments that we do, within India initially but also other areas of Asia, would go through this investment platform. And if IFC decide to decline a particular investment, then we can do it ourselves if we're very positive about that. But the intention is that all of the investments that we do in India and Asia will go through this investment platform.

And it'll be funded as necessary. So as we win new business in these markets, then we, us and IFC, will fund the entity. So it's not going to be funded upfront in advance. It will be funded as necessary. In terms of status, it's currently going through due diligence at IFC, so it's not yet up and running and operational. But we will make an announcement as soon as it is.

Operator
We take our next question from Jai Andrew Lawrence of Al Mal Capital. Jai, your line is now open. Please go ahead.

Jai Andrew Lawrence
Hi, Richard, Adel. Thank you for the call. I joined the call slightly late because of technical difficulties, but perhaps if we could have an update on Saudi. And previously when we spoke, I asked a question with regards to the mega projects that were coming up and what would be Tabreed's role within that. Is there anything perhaps that there would be updates with in that business or in that geography?

Richard Rose

Hi, Jai. Thanks for the question. I think Saudi remains a really important market for the Tabreed group, and we are as hopeful and excited about the potential in Saudi as I think many others are indeed.

So, my understanding is that we're actively bidding on all of the big projects that are out there that have, as yet, put out a request for tender in relation to cooling services. Often, these cooling services' tenders are also linked with other services at the same time, like the utility services. So in some cases, we're bidding in partnership with others. And in some cases, we're still waiting for the tenders to come out.

My understanding is we haven't lost any of these yet. But equally, we haven't won or been appointed to deliver district cooling services to any yet. So, I think watch this space and hopefully we will be successful and we'll be able to take advantage of those growing mega projects in the Saudi market.

Jai Andrew Lawrence

Well understood. And just one last question. In terms of the capacity guidance over the next two years, you're still sticking to the same guidance?

Richard Rose

We are, yes. I think it has been a slow quarter in terms of connecting new capacity. But nevertheless, we're still confident we can deliver that over the next two years, the 120,000 that we guided, and that we will also deliver the full 75,000 that we guided for last year and this year as well before the end of this year.

Jai Andrew Lawrence

Thank You.

Operator

We take our next question from Zeeshan Bagwan. It reads, we read about the first district cooling licence to Saadiyat Cooling LLC, which serves Saadiyat Island, including Saadiyat Beach and Saadiyat Cultural District and Saadiyat District Cooling, which serves the New York University Abu Dhabi.

Under the new regulatory framework introduced by DoE, we wanted to understand about the impact from these new regulations on Tabreed's existing business. Will the new regulations lead to reduction in consumption fees for residential commercial units at Saadiyat Island and New York University Abu Dhabi? If so, what would be the potential fee reduction and its impacts on the revenues?

Will the new regulation lead to any pricing caps on the capacity charges that Tabreed offers to its various clients? Will there be additional costs involved for Tabreed to comply with these regulations? What additional services will Tabreed have to offer as part of this new regulation? And will this impact its profitability?

Richard Rose

Zeeshan, thank you very much for the multiple questions in there. I think what we can say so far is that we've been saying for many years that Tabreed welcomes regulation of the district cooling market. We see regulation as a way to ensure that district cooling is considered for all significant new developments and new cooling requirements within the market.

And that can only be good for us because we fundamentally believe in our business, as the regulator has said that they do as well, and the power efficiencies in particular that our business can offer as well as the continuity of service and the quality of service that we offer to our customers. So, we continue to welcome and support regulation.

I think it's early days with the regulator in Abu Dhabi at this point in time. Clearly, we're in very frequent dialogue with them. We're in the process of licencing those assets that we have in Abu Dhabi that are going to fall under the oversight of the regulator. And up to date, we just have the one asset licence, as you mentioned.

So that licencing of the Saadiyat entity resulted in the grandfathering of the contracts that were in place through the process of an acquisition that we did. So the original contracts are in place with Aldar. We've acquired them and they've been grandfathered under the new licencing regulations. There were a few very minor changes in that grandfathering process just to tidy up the agreements, as you'd expect in any acquisition really, but nothing that had any kind of material impact on our numbers.

I think going forward, it's very difficult to know exactly how the regulator is going to operate in terms of looking for savings. And they have said in their press release that they want to see savings for the ultimate end user customers of district cooling. So we're going to work with them to ensure that we can deliver those savings in a mutually beneficial manner, going forward.

But I think the key thing for us is that we've seen a contract which fundamentally reflects our business of a long-term district cooling provision with a two-tariff structure being grandfathered by the regulator. And that can only be good for us going forward.

Operator

We take our next question from Yawar Saeed, who says, the operating costs have increased in relation to revenue. Can we expect normalisation of it and gross margins, or is it related to new acquisition-led shifts in operating cost structure?

Richard Rose

Okay. I think, from quarter to quarter, always we see some kind of slight movements in margins. I think this quarter, we had a number of changes in the business, in particular, in relation to the three acquisitions that we completed, two of them last year, being Masdar and

Downtown DCP, one of them this year, being the Saadiyat concessions that we've discussed so far on the call.

But in addition to that, we see volume changes. Particularly in Q1, we see variations in volume from one year to another. Always, over the course of the year, they become immaterial and insignificant. So I don't think there's anything fundamentally going on that you need to be aware of in relation to margins. I think all you're seeing is that there's a lot of change in the business, and maybe some of that is coming through.

What I would say is from an operational perspective, our business becomes more and more efficient, particularly from the power utilisation perspective, every year. We have a number of programmes in place which are designed to reduce our power consumption and reduce our operating costs. So, going forward, I wouldn't anticipate that we're going to see operating costs increasing as a proportion of revenue, going forward.

Operator

Our next question comes from Rahmatullah Khan of Abu Dhabi Commercial Bank. Your line is now open. Please go ahead.

Rahmatullah Khan

Hi. This is Rahmatullah Khan from ADCB. I have a question on your interest costs. So a rough calculation gives me a sense that the cost of debt for you is around 4% plus. I just wanted to understand, given this low interest rate scenario and I still see that EIBOR is trending down over the last many months, what is your view on your interest cost going forward, how much you have issued a debt on the fixed coupon or how much out of the AED 6 billion is your flexible rate bank loan? Some kind of colour would be helpful.

Richard Rose

Thanks for that question, Rahmatullah. And I think what we can say on finance cost is that most of our finance costs are fixed. We have very little floating now. So, the $500 million bond that we took out in Q4 last year is at 2.5%. I think the all-in cost of the Downtown DCP facility after hedging and so on is broadly in the region of 2%.

But then we also have some legacy debt which, the Sukuk is, for example, at 4.5%. That was $500 million. That's still there in the debt portfolio. And then we have one or two smaller facilities and, of course, some of the overseas facilities which are consolidated costs which are a bit higher, in the same ballpark as the Sukuk.

I think we've done what we can to minimise our finance costs going forward. I think you also need to appreciate, I think, that the finance costs that are shown on the face of the P&L account include some finance lease-related costs as well. So our actual debt-related finance costs are managed down as low as we can get them.

Rahmatullah Khan

Just wanted to confirm that we should expect that the interest costs will be more or less at the same level that you reported in Q1?

Richard Rose

More or less, yes.

Rahmatullah Khan

Okay. My second question is since you mentioned during the presentation that probably your leverage ratio is very close to the limit where you retain your investment grade credit rating, does that mean that probably you are not going to bid any big offers in the UAE domestic market such as Nakheel?

Richard Rose

Certainly not. That’s not what I was alluding to. I think our debt to EBITDA ratio probably can’t move that much more. But of course, any of these new acquisitions, there are a number of significant targets out there in the market and you’re immediately buying EBITDA at the same time that you’re taking on those debt, if indeed we decide to fund any new acquisitions with debt.

So we do have a bit of capacity internally at the moment. We have a healthy cash balance and we have a revolving credit facility available to us which may allow us to do some of the less sizable transactions without having to revert to any new facilities. But no, we are active in trying to secure any of the major opportunities that are currently in the marketplace.

Rahmatullah Khan

I see. Fair enough. If I could, last, one small question. How much spare capacity you have now? So the frontline number is 1.4 million RT. And I think when you acquired Downtown and Saadiyat, you had some spare capacity which is not connected. Could you please remind me how much is still there?

Richard Rose

Yes. There’s quite a bit. The number of 1.4 million is our connected capacity. That’s the revenue-generating capacities that we have in place at the moment so we feel that that’s the most useful number to provide to the market. However, you’re quite right. A number of our contracts are for concession areas where the master plan has a maximum level of capacity which may not all be connected at this current time.

So, for example, the master plan in Masdar City has a maximum capacity size of 69,000 tons. And currently, I think we have around about 11,000 connected. So there’s significant future capacity potential in that Masdar concession, so any building that comes up in one of these concession areas will connect to Tabreed.

So other important concession areas for us include Raha Beach. I'm not fully aware, off the top of my head, what the potential capacity is there. And then the Downtown DCP, the Downtown district cooling concession that we have is also a very important concession and the maximum capacity size there is 235,000. And currently, we have about 170 kRT connected, something in that ballpark, maybe slightly less. So this, I wouldn't call it spare capacity. I'd call it future capacity.

In terms of spare capacity, when you consider our existing installed capacity versus connected, there is not a great deal of spare capacity. There's a little bit in some of our plants where we actively are looking for buildings in the area that we could try and connect with. These are non-concession areas. But generally, we will try and install capacity as it's required rather than install significant capacity and then wait for customers to come.

Rahmatullah Khan

Okay. Thank you so much. I really appreciate it. Very clear. Thank you.

Operator

We take our next question from Pervez Ismael, who says, if possible, could you please shed some light on this question again?.

Richard Rose

Hi. So I think this question related to IFC Singapore. I think the gist of the relationship there is that this is an investment vehicle for any growth that we manage to secure in India and the broader Asian market. It's 25% owned by IFC, 75% owned by Tabreed.

It'll be funded as and when we win contracts in those markets that I mentioned. Our initial focus is India. And currently, the entity is still going through due diligence with IFC. So it's not operating yet but we hope that that gets concluded in the very near future and that we can start to focus on growing and establishing our business in those markets..

Operator

We have no further questions, so I will hand back to Ms. Souad Jamal Al Serkal.

Souad Jamal Al Serkal

Thank you so much. So this concludes our First Quarter 2021 Earnings call. Tabreed always looks forward to interacting with you at our earning calls and 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. And please stay safe.

Note: This transcript has been edited to improve readability

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