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

First Quarter 2018
Earnings Conference Call Transcript

26 April 2018

<u>Tabreed Participants:</u>

Stephen Ridlington, Chief Financial Officer

Richard Rose, VP – Finance

Rachel Emmett, Investor Relations

Presentation

Operator
Ladies and gentlemen, welcome to Tabreed's Q1 2018 Earnings Conference Call. I will now hand over to your host, Steve Ridlington, CFO, and Richard Rose, VP Finance. Sirs, please go ahead.

Rachel Emmett
On behalf of the Tabreed management team, I welcome you all and thank you for joining us for the Q1 2018 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 2 of the presentation for the detailed disclaimer.

On today's call Steve, our CFO, will first provide a quick overview of the Q1 2018 performance and key events.

Richard Rose, VP Finance, will then discuss the financial performance in more detail. We will then conclude the presentation and will open the lines for your questions.

With that, I'll now hand over to Steve to begin today's presentation. Thank you and over to you, Steve.

Steve Ridlington
Thank you, Rachel, and good afternoon everybody. Thank you for joining us today for our Q1 results call. Turning to slide five, first of all, the usual slide, I will begin by highlighting our first quarter performance and provide a snapshot of recent events.

Overall, Q1 revenues grew 2% over the same period last year, with chilled water revenues increasing around 1%. Despite slower revenue growth, the first quarter saw strong growth in EBITDA and net profit, reflecting little or no growth in costs. As a result, we recorded strong EBITDA margins of 54%. Connected capacity additions in the first quarter amounted to 1,500 refrigerated tons, all attributable to associates and joint ventures. Despite limited growth in revenues and capacity in the first quarter, we remain positive about the rest of 2018, we remain confident that we will deliver the 65,000 RTs of new capacity additions that we announced in January this year. We will deliver that over 2018 and 2019, as we said.

The other news this quarter is that you're aware we acquired the remaining 50% stake in S&T Cool, a joint venture with Aldar. We acquired Aldar's share in March this year. The plant currently has nearly 33,000 refrigerated tons of connected capacity and will deliver AED 50 million of additional revenue and AED 30 million of additional EBITDA in a full year.

Moving onto slide six, as you know, Tabreed is the only publicly traded district cooling company in the world. The UAE is our base of operations, where we have a presence in six

Emirates providing 773,000 tons of cooling to our customers through 63 plants. In addition to the UAE, we work with key strategic partners in four other GCC countries. We have a total of nine plants outside the UAE providing over 321,000 tons of cooling to our customers. Around 65% of our capacity is consolidated, while the rest is equity accounted as associates and joint ventures.

You will see a change of Tabreed's ownership of Bahrain District Cooling Company on this slide, where our ownership has increased from 90% to over 99% by buying out a minority shareholder. The acquisition cost AED 5 million and was done to provide complete control over the activities of Tabreed Bahrain.

Moving onto slide seven, the connected capacity slide, this shows the capacity growth trends across the region. At the beginning of 2018, we announced that we expected to add at least 65,000 tons of new connected capacity during 2018 and 2019. During Q1 2018, we added 1,500 tons of capacity of one of our joint ventures. We expect the majority of new capacity additions in 2018 to occur in the second half of the year, so the second quarter of 2018 may also show limited capacity additions. However, as I said, we remain confident of delivering the full 65,000 tons over the two-year period.

Q1 saw a shift of about 33,000 tons of capacity from the UAE equity accounted line to UAE consolidated capacity. This reflects the acquisition of the 50% of S&T that we did not already own. Tabreed continues to demonstrate its ability to deliver a steady increase in connections 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.

Moving onto the next slide, slide number eight on the first quarter headline performance. This slide recaps our performance over the recent year. To summarise, Tabreed is a stable utility infrastructure business, with long-term contracts with high profile customers. This provides us clear visibility of future earnings and cash flows. We currently have 95% of our capacity contracted for at least the next 10 years. Tabreed has a track record of delivering profitable growth. Our EBITDA and net income have both grown at 8% annually since 2015. We continue to generate strong cash flows and have a robust balance sheet for future growth.

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

Richard Rose

Good afternoon everybody. Turning to slide 10, I will start by highlighting a few key points on our income statement for Q1 2018.

As Steve said earlier, we recorded a 2% growth in revenues, with chilled water revenue growth at 1%. The main factors driving chilled water revenue growth were new capacity additions, which added around 0.5% to revenues, the CPI indexation which added a further 1.5% as tariffs for several customers were escalated. CPI escalation will be applied to all customers by the end of the year. However, offsetting this was a decline in consumption volumes due to the cooler weather prevailing at the beginning of the year. Value chain businesses showed early signs of recovery and registered revenue growth of 5%.

Despite this, EBITDA rose 5% on the same period last year to 149 million, reflecting that we had little or no growth in costs. As a result, EBITDA margin increased from 52% in Q1 2017 to 54% in Q1 2018, partly due to the lower consumption volumes and also the cost management mentioned. Overall, the income statement continues to reflect the stable utility infrastructure model.

I will now turn to the statement of financial position on the next slide. There were some significant movements in the balance sheet in Q1 2018 compared to Q4 2017. The increase in fixed assets primarily reflects the addition of AED 400 million on consolidation of the S&T Cool following acquisition of the 50% stake from Aldar. The decrease in associate and joint ventures is also due to the consolidation of S&T and also an IFRS 15 adjustment of AED 194 million from one associate entity. The reduction in equity and reserves is due to the 2017 dividend of AED 217 million, the IFRS 15 adjustment previously mentioned, and the effect of implementing IFRS 9 of AED 81 million. The increase in other liabilities reflects payables due for the 2017 dividend and also to the S&T acquisition, and both of those payments were made in April 2018. Gearing at the end of Q1 2018 was 42%.

In summary, Tabreed's robust balance sheet continues to position us well for future growth opportunities.

Turning to the next slide, we will take a look at the cash flow statement, and I am pleased to report that Tabreed continues to generate strong ash flows which are being utilised to invest in growth opportunities and provide dividend returns to our shareholders. Operating cash flow was AED 171 million, which is up AED 95 million on the same period last year. This increase reflects continued strong profitability and a positive contribution from working capital movements in the quarter. CapEx in Q1 2018 was sharply lower than Q1 2017, which included the acquisition of the Nation Towers plant from ICT for AED 100 million. Lower financing outflows reflect savings in coupon payments as the mandatory convertible bonds were retired in 2017. Our cash generating ability remains robust, driven by long-term price certain contracts enabling investment in future growth.

Let me now turn to developments with the debt portfolio on slide 13. This slide provides background on Tabreed's debt portfolio, as I say, and the key points to note are, at the quarter end Tabreed has AED 3.1 billion of gross debt and a gearing ratio of 42%. Net debt and net debt to EBITDA have declined since 2016, as debt has been repaid and EBITDA has grown. The debt maturity profile shows significant debt repayments in 2021 and 2027 which are the final maturity dates of our main corporate facilities. The debt is largely AED-based and floating rate, although we hedge a significant part of the debt into fixed rates through plain vanilla interest rate swaps. Our policy is to hedge between 50% and 75% of our debt, and the current hedge ratio is 57%, which we expect to increase in the coming months. Overall, we have a strong leverage profile and headroom available for funding future growth opportunities.

That completes the detailed review of the Q1 2018 results and now I will hand back to Steve to conclude the presentation.

Stephen Ridlington
Thank you, Richard. Before we open the lines for Q&A, just a few closing comments on this slide; first we continue to deliver strong profitability and margins and robust cash flows. Second on capacity additions, while we have had a slow start to the year, we are confident of achieving our 65,000 tons of capacity guidance by end 2019. However, capacity additions this year may largely fall in the second half. During Q1 we completed the acquisition of a 50% stake in S&T from Aldar. Our clear priorities for the future are to deliver growth inside and outside the GCC, and efficiency in our operations. We believe we have the right shareholders and management team to deliver. We are very confident about our future. Thank you.

Question and Answer Session

Operator
Our first question comes from Metehan Mete, Waha Capital. Please go ahead.

Metehan Mete
You talked about successful completion of a three-year pilot project to develop digital smart controllers for the district cooling plants. Can you quantify at this stage how much of operating expenses implementing such a smart system would save on the district cooling side?

Stephen Ridlington
Yes, you're right. We have completed an initial three-year research project, but we can't yet get into the question of what that might end up saving us. I think there has to be a next step really, which is how does what that research has done translate into operational performance at the individual plants, so it's something that we're certainly going to be looking at and working on, but I am afraid it is not yet quantifiable.

Metehan Mete
My other question was whether there has there been any progress on the growth outside the GCC, like any synergies that you talked about previously regarding the ENGIE acquisition, like any growth in Egypt, India, or Turkish markets?

Stephen Ridlington
this is going to take time, there is no question. I can tell you, and we've said before, that we are accessing the ENGIE network to build the relationships, find opportunities in those markets, but this will take time. As soon as we have something to say, you will be the first

to hear about it. Moving into new markets is never a quick and easy thing, so just bear with us for a while.

Metehan Mete
Another follow-up question from my side was that you acquired S&T Cool that is on Reem Island and one of the margin accretion for your new acquisitions is where you have excess capacity to connect new customers. Do you have excess capacity in S&T Cool and when new buildings get completed can you connect them to the same cooling facility that you have?

Stephen Ridlington
In this particular case, not really, in the sense that the capacity that is installed in that plant is being largely utilised. However, the plant can be expanded and the network can certainly take additional loads, so we are anticipating that we're going to have to expand that plant at some point when new load comes on. Obviously, we won't do that until a new load is there but expansion is certainly possible.

Operator
Our next question comes from Vikram Vishvanathan, NBK Capital. Please go ahead.

Vikram Vishvanathan
My question is on the new district cooling markets. You obviously talked about Egypt, Turkey, and India in the past. Can you give us a sense of what is the market opportunity for district cooling in these new markets? Is it still at a very nascent stage or are there already district cooling plants in these countries, or maybe it's starting from scratch? Have you been able to do a market feasibility study in these markets and assess what kind of growth could you achieve in these markets over the next few years?

Stephen Ridlington
Yes, well, that's a really good question and it helps to answer the question that Metehan had earlier, because understanding the scale of those markets, particularly India as you'll imagine, it's a huge market and it does take some time to assimilate it. What I will say, based on our initial understandings, and it is initial at this stage, is that we have done more on Egypt and India than Turkey and both are at the relatively early stage of development. There are district cooling opportunities there, both in terms of new projects and some existing cooling that is already in place. Some of that is owned independently and some of it is owned by developers, so I think we're in no doubt that the potential scale in both of those markets is significant, but it is early days for them. It will take time, but there is no doubt in our minds that there is the ability here to make a material difference to the scale of the company and scale of business that we're currently doing.

Vikram Vishvanathan
All right and the opportunities in India and Egypt, are these mostly linked to new residential developments or is it commercial complexes…?

Stephen Ridlington
It's a bit of everything. There are some commercial, there are high rise towers, there's some existing plants. I think the opportunity set doesn't necessarily look very different to what we see here. It's just a question of when it develops and how quickly.

Operator
Our next question comes from Metehan Mete, Waha Capital. Please go ahead.

Metehan Mete
Just another final question from my side. If we ever get in a situation where the growth opportunities in the GCC and also outside the GCC will be limited, would you accumulate cash in your balance sheet or would you migrate into a better dividend pay-out policy for the shareholders?

Stephen Ridlington
Metehan, it's a good question and it is one that we would have to discuss further with our board, because the point at which you can make a judgement that growth is not happening and won't happen is a difficult one to call. What I will say is that I don't think that the management or our shareholders would expect us to want to sit on cash in the long-term. It's not the way we've operated in the past. You've seen our cash up to 400 million, 500 million perhaps, but then drop down again, so we'll obviously want to make sure we have the ability to continue to fund the company, but beyond that, I don't see us as a cash stockpiling type of company. We're a utility company and I would expect that over the long run we'll either invest it or return it to our shareholders.

Rachel Emmet
That concludes our Q1 2018 earnings call. Tabreed will be attending multiple investor events during the rest of the year and we look forward to meeting with you then. You can find further details on the last slide. Should you have any further questions, please don't hesitate to contact us. Goodbye and thank you once again for joining this call.

Note: This transcript has been edited to improve readability

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