Aldar Properties Q2 2021 earnings call

Wednesday, 11 August 2021

Mohamad Haider Hello, everyone, and welcome to the Aldar Properties second quarter and first half of 2021 earnings call. This is Mohamad Haider from Arqaam Research, and as usual we are joined today by Mr Greg Fewer from Aldar Properties. He's the group chief financial and sustainability officer. Over to you, Greg.

Greg Fewer Thank you, Mohamad, and good afternoon, everybody, and welcome to our Q2 2021 results call. As Mohamad said, I'm Greg Fewer, the group chief financial and sustainability officer. Thank you, everyone, for joining. Thank you, everyone, for joining on the relatively brief exposure to our numbers.

I think with the national holiday tomorrow, we decided, having just walked out of our board meeting to approve these numbers, to have this call now, so I thank you all for tolerating just receiving the numbers and appreciate you haven't had a lot of time to go through them, but we thought it was better to have this call today, before the holiday, than after the long weekend, Sunday, Monday next week. We thought this was the best of a couple of bad options.

As ever, our investor relations team is available for any follow-up questions with you. Samar Khan, our head of investor relations, is very accessible, and once you've had a chance to look at the numbers, please do reach out to her with any other follow-up for this transcript or any other elaborations.

So overall, we're very pleased to report another very strong quarter. We're witnessing a meaningful uplift in activity this year, benefiting from improved consumer and business confidence in Abu Dhabi. This is once again testament to the UAE's effective response to the global pandemic, and rolling out a world-leading vaccination programme whilst also implementing strong federal policies to encourage investment and private sector development.

The supportive macro and policy backdrop is enabling a smooth and sustainable recovery which is positively impacting a range of our indicators, from increasing footfall and sales at retail properties, increased school enrolments, to robust demand for our residential developments.

Q2 group revenue increased 9% year on year, to 2.19 billion dirhams. During the quarter, we registered 2.35 billion dirhams in development sales, smashing our previous record for the quarter. The product management services segment is ramping up and recorded a significant increase in fee income.

Meanwhile, our investment properties continue to create steady income with improvements across our various segments. Q2 gross profit grew 15% year on year, to 824 million dirhams, and net profit increased 8%, to 521 million dirhams.

I would now like to dive a little deeper into [unclear] of Aldar Developments and Aldar Investment respectively. Revenue for the Aldar Developments business increased 7%, to 1.35 billion dirhams, and gross profit rose 10%, to 444 million dirhams, driven by robust development revenue. This was generated by new launches and a steady pace of sales of existing inventory, as well as a higher contribution from the fee-based projects management business.

We recorded our highest-ever quarterly sales of 2.35 billion dirhams in the second quarter of 2021, bringing the total for the first six months of 2021 to 3.4 billion dirhams. All our new development launches were rapidly sold out, and that momentum is extended into the third quarter, with recent sell-outs at Al Gurm Waterfront Plots and our Saadiyat reserve villa development.

We are seeing positive trends and pick-up in activity in the Abu Dhabi real estate market and are confident in our ability to successfully bring new projects to the market in the coming months.

Expatriate homeowners and foreign investors, very pleasantly, are representing more than 42% of the buyers across our development business. We also attracted strong demand from first-time homebuyers and return buyers who have shown appetite for high-quality, well-designed communities.

The strong sales in new developments in the period resulted in a 28% quarter-on-quarter increase in revenue backlog to 4.25 billion dirhams. Cash collections were up 36% year on year, to 1.06 billion dirhams, and was driven by successfully collected handovers at Mamsha, Yas Acres, West Yas, Water's Edge and Nareel.

Meanwhile, the project management services business unit is generating a consistent increase in the meaningful stream of revenue for our business, enhancing revenue visibility and providing healthy cash flow. Q2 revenue for this project management services business unit increased 58% year on year, to 367 million dirhams, and gross profit jumped 192%, to 108 million dirhams for the quarter.

Turning to Aldar Investments, our asset management platform, this has shown considerable resilience over the last year and continues to do so through the second quarter. In the second quarter, Aldar Investments revenue was 15% higher year on year, at 874 million dirhams, with net operating income for the businesses increasing 23%, to 375 million dirhams.

The investment properties portfolio produced a 5% year-on-year increase in NOI, to 308 million dirhams. Within that, the residential segment recorded just under 0.5% growth in NOI, driven by higher income from new leases. Occupancy increased to 89% at the end of the second quarter, from 88% a year earlier.

Meanwhile, retail saw an 18% increase in NOI, mainly due to higher footfall and sales, also reflecting the Q2 period when COVID hit last year, reflecting through improving consumer sentiment and purchasing power. Occupancy held firm at 86%, and is expected to be supported by good progress made on the Yas Mall redevelopment plan.

I'd like to remind you that in the fourth quarter we announced a 500 million dirhams redevelopment programme at Yas Mall, which will be delivered in phases over the next 12 months. The project will repurpose about 40% of the gross leasable area to create high-impact experiential retail and F&D spaces, as well as adding a total of 15,000 square metres of office space.

Turning to the commercial portfolio, NOI declined 0.5% year on year, mainly due to lease maturities within our operating village segment. However, the underlying office occupancy held firm, at 90%, supported by long-term committed lease contracts from government-related entities and corporate clients.

The hospitality and leisure business is recovering, with 79% improvement in NOI supported by an increase in third-party asset management fees and prudent cost control measures across the hotel units.

Meanwhile, Aldar Education reported a 208% increase, year-on-year increase, in net operating income, to 49 million dirhams. This growth was driven by a 16% increase in student numbers over the last academic year, and enhanced operational efficiencies.

Provis, which has increased scale materially through the acquisition of Asteco, produced a significant increase in NOI, to 17 million dirhams, driven by the completion of the Asteco transaction and some contribution in this quarterly earnings, along with growth across several of the service lines.

At the end of a strong quarter, Aldar's balance sheet remains very strong, with debt levels well within group policy ranges. Our liquidity position remains very healthy, with 4.5 billion dirhams of unrestricted cash, and a further 4.5 billion dirhams of long-term, undrawn, committed bank lines.

And benefiting from this strong liquidity position, we are actively seeking attractive opportunities presented to us at this time in the market. We will continue to launch new developments in premier locations during the remainder of the year, and at this juncture we'd like to revise our 2021 property sales guidance to over 5 billion dirhams.

We also expect to pursue further asset growth and diversification of our investment property portfolio, with an active deal pipeline heading into the second half of 2021, looking to deploy the surplus capital that we're building.

From a financing perspective, during the quarter we signed a new five-year, 300 million dirhams sustainability-linked loan with HSBC bank. This represents a real statement of intent from Aldar on integrating ESG into all the various functions within Aldar, and contributing to [unclear] Aldar as the highest ESG-rated real estate company, listed real estate company, in the UAE. And we very much welcome the opportunity to link our financing and our treasury operations to metrics and KPIs along our sustainability goals.

Amongst other initiatives in the second quarter, we also completed a business development climate risk assessment, following the TCF guidelines, and we joined the United Nations Global Compact, [unclear] sustainability initiative.

Sustainability at Aldar has also become very real for our employees, with sustainability integrated within the company's competency and performance management frameworks, along with numerous other policy improvements that we're making, contributing to our improving rankings along the ESG metrics.

So overall, in conclusion, very strong second quarter results, reflecting significant uplift in activity across Aldar's diverse interests over the last quarter. This has been a very busy period for us, and we expect to continue this accelerated pace of growth over the second half of the year. And with that, I'm very happy to turn things back to the operator and open the floor up to some questions.

Operator Thank you. If you'd like to ask a question, please press star followed by one on your telephone keypad now. If you change your mind, please press star followed by two. For those who have joined online, please press the flag icon. When preparing to ask your question, please ensure your phone is unmuted locally.

We currently have no questions, so as a reminder, if you'd like to ask a question, please press star followed by one on your telephone keypad now. If you have joined the call online, please press the flag icon. We have a couple of questions now. Our first question comes from Taher from J.P. Morgan. Taher, your line is now open, please proceed with your question.

Taher Safo Good afternoon. Thank you, Greg, and congratulations again on a solid set of numbers. A couple of questions, if I may. First, on the Development property sales. The momentum has been extremely strong, can you just maybe give us some more colour on the nature of the buyers between residents, non-residents, nationals, expats? That would be helpful.

And I think the second question is on the fee-based projects. We're starting to see these big government projects that you signed filtering through the P&L, so maybe if you can just give us some guidance on the run rate on those projects, as the other [unclear] wind down. This is, I think, the first part of the question.

And I think the second part, if we can just get maybe more clarity on what's happening within the investment portfolio, specifically within the retail portfolio, that would be helpful, in terms of trends. And how should we think about this active deal pipeline that you mentioned coming through into the second half? If you could just give us some clarity on sectors, segments, that would be helpful. Thank you.

Greg Fewer Sure, okay. First question, Taher, on the development sale, we included the statistic in our press release just to emphasise the point that we're seeing more interest now coming from a broader group of people. The local Emirati investor has always been the anchor of our development franchise, and they continue to be the important constituent, but we're seeing a broadening and a deepening of the expatriate and the foreign buyers into our projects.

And so we're seeing that in particular with the very expat-friendly jurisdictions like Yas and Saadiyat, and that's where our launches have really focused in the last couple of quarters. So Noya, Saadiyat, prime for expatriate homeownership, really taking advantage of this investment theme playing out here, which is Abu Dhabi's becoming more of a home for its long-term expatriates, expatriates actually converting from rental to homeownership, and expatriates investing here as they start to get five-year visas, ten-year visas, creating more permanent, sticky residency here.

And that's showing up in our numbers. We're seeing a lot of young people. The large age group is 31 to 45 in terms of overall buyer profile, and an increase in owner-occupier. So those numbers really are trending in the right direction, and underpinning the broadening and the confidence that we're having in our sale guidance, that, as I mentioned, we've increased now.

Your second question was on the project side. Yes, just over 100 million, 108 million, in profit from that division. It's still ramping up. What we're seeing is that the big, mega-projects that have come on from the ADQ transaction, in particular we had city [unclear] Yas, these are still in their relative infancy, the early age of the S curve of the development.

So with 108 profit for the quarter on the early side of developments of those big projects, we see further growth, quarter on quarter, coming from those big projects into the future. So we see that expanding.

On investments, you asked for a particular update on retail, our retail performance, going forward, is really going to be driven by Yas Mall. As I mentioned on the last call, it's a good time to have plans, for the last 12 months, for redevelopment of that mall, and to be executing it now, during COVID and before tourism opens up here. It's actually a very good time to be doing that.

And so, we still have leasing to complete at Yas Mall, it's still in the mid-80s in terms of occupancy. We have line of sight to get into the more traditional low-90s, where we expect to be within the next three to six months as we execute that investment plan. So you're going to start to see NOI growth pick up across Yas Mall as that plan plays out. That's probably the most important trend there.

We actually had a good quarter as well from a community retail perspective. Again, the theme that we saw, the very affluent, the local resident community here, staying in Abu Dhabi more for some of their immediate and discretionary spending. We're seeing that play out, and the stickiness of the sales at Yas Mall and the performance across our community retail malls.

And then finally, you asked about the pipeline of acquisitions. We've got a fair bit of cash piling up, and this has been a trend you've seen from Aldar over the last decade that I've been here, that we pile up cash over time, we position ourselves for acquisitions when they come up. Generally, they come up infrequently in our market, but when they do come up, you need to be liquid, you need to be ready to take advantage of them. And we're certainly doing that.

The most obvious example is we've got a bid out right now for an expansion into the Egyptian market, which we're extremely excited about. There's be more to play out on that, that's a very public transaction, we've got a mandatory bid we've had a couple of extensions on now, and you'll hear more from us in the coming days about that, as we work with the regulator and with that transaction.

But it's a statement of intent with us. We've got cash, we've got appetite to grow, certainly into Egypt, and domestically across the UAE, across our investment portfolio, across all the segments. We're seeing very interesting opportunities in education and with some of the other big property owners in the UAE around consolidation and putting our cash to work. I've talked too much, I hope that answered your four questions.

Taher Safo No, it's fine. Maybe just catching it from the end, which takes me to my final question, about education. It's quite significant the growth we have been seeing there, the number of student enrolments. I think currently you're sitting at 24,000. What is the endgame for Aldar Education? This is more maybe non-core from Aldar's perspective, but again you're seeing some very healthy revenue, gross profits and margins. How should we think about Aldar Education over the next 12, 18 months?

Greg Fewer That's been one of our success stories for sure. We have called that, and it remains, non-core, but highly valuable. And we're stepping back and we're calling the history of Aldar Education emanated and grew from our position as a developer where schools were blots on a master development and we had to build them as part of the communities, and we sort of build these one by one, started to manage them one-on-one, created excellent curriculum and focus, and the focus in the last five years has been about corporatizing it more and really flipping it from excellence in education into both excellence in education and profitability.

And we've absolutely achieved all that. The real growth has come from, going back to the themes in the market around the government of Abu Dhabi privatising a lot and Aldar being a trusted partner, is ramping up our fee business within Aldar Education. We took over the management of the ADNOC portfolio of schools, we've taken over a number of charter schools, and we see a healthy pipeline with a very active government in Abu Dhabi seeking private sector engagement in its schools further.

So I think you could see more there. And like with any valuable non-core business, you always seek monetisation opportunities, and schools is one of those areas where a lot of private capital…

And a lot of investors spend a lot of time in education, it's a very investable sector, so as we continue to corporatize it, as we continue to improve its profit margins, as we continue to scale it, lots of opportunities present themselves then to the owner of a non-core, highly valuable business, and the management team has every incentive to continue growing that and show good realisation opportunities for us.

Taher Safo Okay, perfect, thank you very much.

Greg Fewer Thank you, Taher.

Operator Our next question comes from Rakesh from Franklin Templeton. Rakesh, your line is now open, please proceed with your question.

Rakesh Tripathi Thank you very much for the presentation and the call. I had just one question that was regarding the transfer of some of the residential assets that was supposed to happen to the Aldar Investment entity. I suppose there were some units that were to be transferred from the Bridges and then some units from Water's Edge, so where are we on that? Can you talk a little bit about what is the status and when do you expect those transfers to happen, those asset transfers?

Greg Fewer So the Bridges transfer actually took place in this quarter, so it's embedded in the ebbs and flows on the balance sheet, as the transfer from DWIP to Investment Properties. Just under 0.5 billion dirhams to reflect the Bridges. And Water's Edge is a project that's handing over literally as we speak, right now. And those transfers will take place in the third and fourth quarters of this year.

Rakesh Tripathi So these transfers happen via some exchange of cash? How is the parent compensated for these transfers?

Greg Fewer It's a capital contribution from the parent into Aldar Investment Properties.

Rakesh Tripathi So there's no cash outflow, really, at the Aldar Investment entity, really, for this?

Greg Fewer No, it's a capital contribution, and then there's the leverage applied to us, and then our leverage policy applies, and a 37% leverage would be attached to those projects.

Rakesh Tripathi 37% leverage, yes, okay, thank you. Thank you.

Operator As a reminder, if you would like to ask a question, please press star followed by one on your telephone keypad now. If you change your mind, please press star followed by two. For those who have joined online, please press the flag icon. Our next question comes from Harsh from International Securities. Harsh, your line is now open, please proceed with your question.

Harsh Oza Hi. Thanks for the presentation. Two questions from my side. There is an increase in the commodity prices, construction costs, over the last six to 12 months. I just wanted to understand how do you see the higher costs impacting your margin, not for the current project but maybe for the future projects? And if you can also share such a inflation component, how are you dealing with the contractors?

My second question is if you can briefly discuss your Egypt strategy, what role you intend to play. Obviously, it's a growing market, but again there is a sharp contrast with respect to interest rate, mortgage penetration demographics when we look compared to [unclear] Egypt. These are my questions.

Greg Fewer Okay, great, thanks, Harsh. So the first question on commodity prices, I guess the first comment is that our business model as a developer is to design a community, and then we tend to do lump-sum, fixed-price contracts with our contractors. So from a contractual perspective, commodity risk resides with the contractor.

And this commodity issue has been something that's definitely top of the contractors' minds for a long time, and in our procurement processes we're working closely with the contractors to make sure that they understand those risks that they're taking, which they do of course, and we have a view on how they're handling it.

And we are seeing an uptick in those prices and how they're pricing those in the contracts, so it's not something that is going to be increasing gross profit margins at all. In terms of an overall impact on it, we've got tenders out right now to conclude Noya, which are sales that we've already launched, and we're well into discussions with contractors on that.

And I wouldn't say we're overly concerned about profit margins right now, but you might see one or two points of compression on a couple of our projects on the margin, if prices continue to escalate. I know there's a big debate still about whether it's transitory or a bit more permanent. But on the existing stuff, it's all locked in already with the contractors.

So let's say a couple of billion, even less, of overall project value of which 60%, let's say, is contractors costs, and of that maybe half of that relates to hard quantities of steel or glass or cement that would be subject to this kind of risk. So when you do that step-down math, you might conclude that there's one or two per cent at risk, if things go against us, but I would give it too much concern right now.

And generally, I think we're pretty happy with how proactive the contractors have been about identifying this risk and working through the various mitigation strategies within the supply chain.

The second question was on Egypt. And we called out Egypt in our operating model change that we announced at the beginning of the year, and again, that's a strong belief in an investment thesis that the management team has, with our board, around that as a very attractive market, the segment we choose to play in.

So it's the upper, upper band in the Egyptian real estate market, and then the development industry there, the homebuilding industry there, it lends itself to our skillsets and our competencies quite well. Communities, well-planned communities, this high end of the Egyptian market is a growing one, it appreciates the kind of product that's in our DNA, and we have a lot to add to that market. So really, that's the thesis. So when we go out to execute that thesis, you can then see how SODIC is relevant in that context.

But we're also, with our network, with our shareholders and the origination work that our management team's built out there, there's a lot of interesting opportunities that are coming up that we think we're uniquely positioned to take advantage of in terms of access to interesting transactions, access to interesting partners. All those things, the macro and I think the alpha that we can bring with our original network, it makes it an interesting segment to play in for us.

Harsh Oza Okay, so it's high-end, first and second-home in Egypt?

Greg Fewer Correct, yes.

Harsh Oza Understood, thanks, Greg.

Greg Fewer Thank you, Harsh.

Operator And for one final reminder, if you want to register a question, you can do so by pressing star followed by one on your telephone keypad now, or you may press the flag icon if you have joined us online. We have a question from Harsh from Goldman Sachs. Harsh, your line is now open, please proceed with your question.

Harsh Mehta Thank you. Hi, Greg, congratulations on the results. I just have one question. There's been another record quarter in terms of your development sales, and I was hoping to understand about the trends. Do you see this is more of pent-up demand that's getting reflected, or is it a structural shift based on the [unclear] that you're seeing, where there's something we can say is a sustainable demand, that this kind of trend will continue for the next few quarters?

And the second question is you also revised your guidance upwards in terms of development sales, and so just linking with the first question, is this something we should assume that's the kind of places that the management will be looking at, at least in the medium term, for the next few years? Thank you so much.

Greg Fewer Sure, yes. I guess the answer is it's a bit of both. There's clearly some pent-up demand, and I think that was a real catalyst for some of the immediate sales launches that we've had.

But I think what's given us a lot of confidence has been seeing the breadth and depth of the new customers that are coming through, especially on the expatriate side, and especially on the back of the practical impact that the government's reform programmes are having on the market. Long-term expats are feeling a lot more comfortable at deploying capital into property here, and we're seeing that live, in technicolour, in our sales.

With that broadening of the investor universe, we think that there is a structural shift to move up. Now, there's always a cyclicality to real estate sales, but if that's an up-and-down cycle, I think that whole up-and-down line has trended up. So we've historically guided sales in that 1,500 units a year, 3 billion to 3.5 billion of sales a year.

There's no doubt that these reforms are having a positive impact and that that's moving up. In terms of how much we're guiding around a perpetual increase, we don't normally do that but we've moved up our guidance this year, it's going to finish at well over 5 billion dirhams. How much of a permanent re-guide is that? That's tough to say at this point, other than I would agree with the statement that there's a structural shift up in demand foundations for Abu Dhabi real estate.

Harsh Mehta Interesting, thank you very much. And I just have two follow-up questions. One is are you able to pass through any price increases, given the robust demand that you've seen? And secondly, just in terms of the expat demand, could you help us understand what kind of product are they preferring? Is it apartments versus villa or mid-market versus high-end? Something around that, if you'd comment on it, thank you.

Greg Fewer On the price comment, because they've been sell-outs, the price increase has mostly been a function of the first couple of sales, the guys sell at, let's say, 100, and because they start selling like hotcakes, we very quickly move up to 102, 105, 107 during the sales events themselves. So that's the price increase we've seen.

I think in that context, what we're still doing at Aldar, in the Abu Dhabi market, is we're still bringing new products at new price points, so that's, I think, the predominant thing. Whether it's mid-market, with Water's Edge, or whether it's the Noya, or on the horizontal side, inventing new price points in the market, pushing up price increases need to be seen in the context of where we're introducing new price points.

But just as a function of the tremendous demand we've seen, in the hours and days around these launches, we have been very successful moving price increases, reflective of the very strong demand that we're seeing from customers.

Harsh Mehta Thank you.

Operator And I'll allow a few moments here for any last-minute questions to come in.

Greg Fewer And sorry, I didn't answer Harsh's second question around trends. Horizontal has definitely been the trend. And I think there's always been a bit of an expectation that COVID sentiment, getting out of glass and into horizontal villas, was a catalyst for that.

We definitely have seen that driving a lot of the sentiment. But in our market, because it's still a very supply-managed market, we've got very important, exciting destinations at Yas and Saadiyat that we're going to be focusing both villa and apartment developments on, as seen in the context of this constructive supply that we have in Abu Dhabi, and the emergence of these incredibly well invested destinations from a government perspective. We see trends that will be continuing the pace of launch, taking advantage of this new depth we're seeing within our customer base.

Operator There are no further questions on the line. I'd now like to hand back to the host for any closing remarks.

Mohamad Haider Greg, I think we have no other questions, do you have any closing remarks?

Greg Fewer No, other than thank you for dialling in, and enjoy, for those of you in the region, a good long weekend, and we look forward to speaking to you at Q3.

Mohamad Haider Thank you for your time today, and thank you everyone [overtalking].

Greg Fewer Thank you, Mohamad.

Mohamad Haider We hope to see you next quarter.