

2Q19 results review

Real Estate | UAE | 14 August 2019

2Q19 net profit came in at AED51mn (-87% y-o-y). Earnings were 54% below our expectations. Topline continues to witness sharp decline but it was anticipated looking at last few quarters trend. The key reason for miss was sustained weakness in gross profit margin. While earnings uncertainty continues, pre-sales dipped to lowest quarterly levels seen since its IPO. Pre-sales recovery in previous two quarters seemed encouraging but another weak quarter now poses downside risk to our 2019E pre-sales. Amid weak pre-sales, management is focusing on delivering its backlog and handover of units. However, this is not well reflected in execution progress (as indicated by weak revenue recognition). Moreover, margins have failed to pick up casting uncertainty on sustainable profitability. We expect Damac's earnings to decline 83% in 2019E (after 58% drop in 2017). Cash flow generation has turned positive this year (free cash flows of AED220mn in 1H19 versus negative AED384mn in 2018), but remains well below uptick expected by us. Lastly, the key attraction of Damac Properties in the past was its high dividend yield. However, after no dividend payment in 2018 and lack of dividend policy, we expect another year of dividend disappointment in 2019. The stock is now trading at significant discount (2019E P/BV of 0.4x) and appears to be pricing in weak fundamentals. We maintain our Hold rating.

► **Revenue and margin weakness continues**

2Q19 revenues at AED971mn declined 46% y-o-y (after 18% y-o-y decline in 2018). Damac's revenue is largely derived from UAE projects and revenue recognition in UAE has slowed down considerably over last one year. Simultaneously, gross profit margin (GPM) performance has also deteriorated. 2Q19 GPM fell further to 27% versus our expectation of partial recovery (35%). Recall that management guided for sustainable margin of 40%, but last six quarters have delivered margins significantly below guidance.

► **Another weak quarter of pre-sales posing downside risk to our estimates**

2Q19 pre-sales came in at AED624mn, down 14% y-o-y and 47% q-o-q. After recovering in previous two quarters, it dropped to historical low quarterly level in 2Q. 1H19 pre-sales stands at AED1.8bn, implying required run-rate of AED1.3bn per quarter in 2H19 to meet our FY2019 estimate. This looks challenging looking at last five quarters. Thus, FY2019 pre-sales could fall short of 2018 level, which was already down 43% y-o-y.

► **Valuation discount to sustain on weak earnings, uncertainty of dividend**

The stock is now trading at significant discount of 0.4x 2019E P/BV, 60% below emerging markets peers and 65% below its historical average. We believe Damac's current valuation discount is likely to sustain given weak pre-sales and earnings outlook, high project concentration risk and insignificant recurring income contribution. Finally, its dividend outlook remains uncertain compared to its key peer (12% div. yield offered by Emaar Development).

Key Financials	2017	2018	2019E	2020E	2021E
Revenue (AEDm)	7,454	6,133	4,019	4,441	5,104
EBITDA (AEDm)	2,861	1,317	352	777	1,166
Net profit (AEDm)	2,760	1,152	193	643	1,050
EPS (AED)	0.5	0.2	0.0	0.1	0.2
EPS (% Change)	(25.3)	(58.3)	(83.2)	233.2	63.3
P/E (x)	2.1	5.0	29.6	8.9	5.4
Dividend Yield (%)	15.9	0.0	0.0	10.6	10.6
Total net debt (AEDm)	(2,705)	(1,226)	(1,424)	(1,747)	(1,952)
RoAE (%)	20.8	8.2	1.4	4.4	6.9

Source: ADCB Securities Equity Research

Fundamentals

Recommendation	Hold
Target Price	AED 1.1
Price	AED 0.95
Price 12m High/Low	AED 2.13/0.84
Market Cap.	AED5,717mn
Bloomberg/Reuters	DAMAC UH / DAMAC.DU

Price Performance Chart



Source: Bloomberg

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Financials

Income Statement (AEDmn)	2018	2019E	2020E	2021E
Revenue	6,133	4,019	4,441	5,104
EBITDA	1,317	352	777	1,166
Depreciation and amortisation	28	33	38	40
EBIT	1,289	319	740	1,126
Other income	26	49	51	52
Net Finance Cost	163	175	147	128
Profit before tax	1,152	193	643	1,050
Taxes	0	0	0	0
Minority interest	0	0	0	0
Net profit	1,152	193	643	1,050

Source: ADCB Securities Equity Research

Balance Sheet (AEDmn)	2018	2019E	2020E	2021E
Cash and cash equivalents	6,174	5,836	5,679	5,737
Other current assets	18,390	17,880	17,449	16,802
Total non-current asset	424	419	417	414
Total assets	25,176	24,455	23,894	23,291
Total current liabilities	6,119	5,858	5,134	4,232
Borrowings	4,948	4,412	3,932	3,785
Other non-current liabilities	0	0	0	0
Total liabilities	11,067	10,270	9,065	8,017
Minority interest	0	0	0	0
Shareholders' equity	14,110	14,303	14,946	15,391
Total net debt	(1,226)	(1,424)	(1,747)	(1,952)

Source: ADCB Securities Equity Research

Cash flow statement (AEDmn)	2018	2019E	2020E	2021E
Cash flow from operations	(373)	193	495	963
Net capex	11	20	25	25
Free cash flow	(384)	173	470	938
Net financing	182	(536)	(480)	(147)
Change in cash	(1,285)	(338)	(157)	58

Source: ADCB Securities Equity Research

Valuation and leverage metrics	2018	2019E	2020E	2021E
P/E (x)	5.0	29.6	8.9	5.4
P/BV (x)	0.4	0.4	0.4	0.4
P/FFO (x)	4.8	25.3	8.4	5.2
FCF yield (%)	(6.7)	3.0	8.2	16.4
Dividend Yield (%)	0.0	0.0	10.6	10.6
EV/EBITDA (x)	3.4	12.2	5.1	3.2
Interest coverage (x)	4.0	1.0	2.6	4.4
Net debt/equity (x)	(0.09)	(0.10)	(0.12)	(0.13)
Net debt/EBITDA (x)	(0.9)	(4.0)	(2.2)	(1.7)

Source: ADCB Securities Equity Research

Key Ratios (%)	2018	2019E	2020E	2021E
ROAIC	7.8	2.7	4.9	6.9
RoAE	8.2	1.4	4.4	6.9
Revenue growth	(17.7)	(34.5)	10.5	14.9
EBITDA growth	(54.0)	(73.3)	120.8	50.0
EPS growth	(58.3)	(83.2)	233.2	63.3
EBITDA margin	21.5	8.8	17.5	22.8

Source: ADCB Securities Equity Research

Per-share data (AED)	2018	2019E	2020E	2021E
EPS	0.19	0.03	0.11	0.17
DPS	0.00	0.00	0.10	0.10
BVPS	2.33	2.36	2.47	2.54
Total no. of outstanding shares (mn)	6,050	6,050	6,050	6,050

Source: ADCB Securities Equity Research

Investment case

Damac is a Dubai centric developer with its sales mainly driven by foreign nationals. Pre-sales outlook has deteriorated since 2018 given soft market conditions driven by US\$ strengthening and increasing supply risk. In slow market, management is focussing on delivery of its backlog. However, lack of clarity on sharp margin decline over last one year blurs earnings outlook and cash flow visibility. We see its valuation discount to sustain amid weak pre-sales and earnings outlook, lower visibility and lack of revenue diversification towards recurring income.

Upside case AED1.5

Rebound in 2020-23E annual pre-sales to AED6.0bn (+40% from current run-rate) driven by property market recovery. In this case, Damac would trade at 2019E P/BV of 0.6x.

Downside case AED0.8

Decline in oil prices and sustained strength in US\$ would lower demand and pre-sales. Further risk arises from continued weakness in selling prices owing to high upcoming supply. As a result, cash collection would slowdown. We assume 20% lower 2019-23E pre-sales and annual cash collection than our current estimates for a downside case. In this case, Damac would trade at 2018E P/BV of 0.3x.

Results summary – 2Q2019

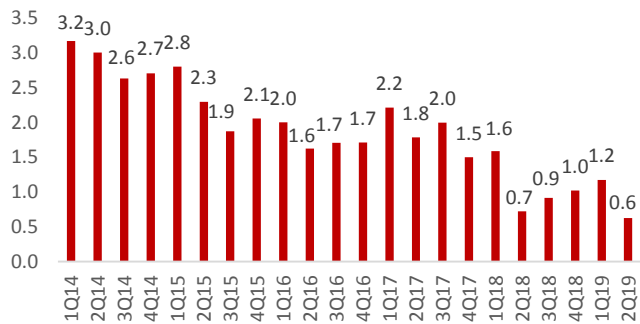
Fig. 1. 2Q19 results review

AEDmn	2Q19	2Q18	y-o-y	1Q19	q-o-q	2Q19E	Variance
Revenues	971	1,787	-46%	896	8%	1,000	-3%
Gross Profit	260	627	-59%	242	7%	350	-26%
Margin	27%	35%		27%		35%	
EBITDA	67	423	-84%	59	13%	140	-52%
Margin	7%	24%		7%		14%	
Net Profit	51	378	-87%	31	63%	110	-54%
Margin	5%	21%		3%		11%	

Source: Company, ADCB Securities Equity Research

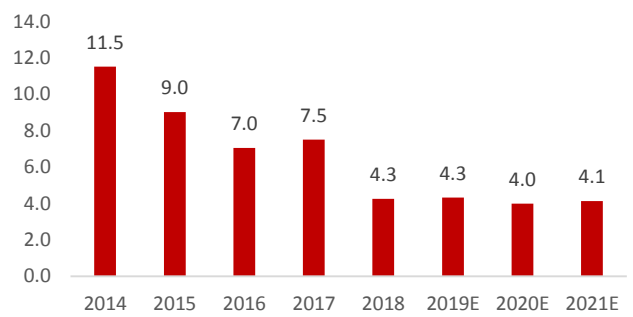
Damac's pre-sales trend

Fig. 2. Damac's quarterly pre-sales (AEDbn)



Source: Company, ADCB Securities Equity Research

Fig. 3. Damac's yearly pre-sales (AEDbn)



Source: Company, ADCB Securities Equity Research

Recommendation history

DAMAC PROPERTIES (DAMAC UH EQUITY)



Date	Recommendation	Target Price (AED)	Closing Price (AED)
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Rating Distribution

Rating	Coverage Universe %
Buy	75%
Hold	25%
Sell	0%

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Hold	(10%) – 15%
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