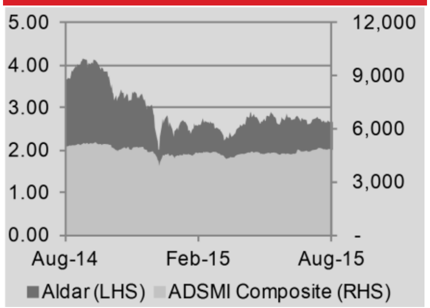
RECOMMENDATION: BUY

As on August 11, 2015	
Current Price	AED 2.67/sh
Target Price	AED 3.14/sh
Up/(down)side	+17.5%
M. Cap (AED million)	20,993
52 week range (L-H)	1.98-4.14
One year return	(26.8)%

Relative share price performance



Business Description

Aldar is a construction and real estate management company, headquartered in Abu Dhabi, UAE. It is one of the largest developers in the region and the Government of Abu Dhabi has a considerable stake in the company. Aldar's assets include 4,800 residential units, key flagship asset of Yas Mall, hotel portfolio, Formula 1 race track and Ferrari World amusement park.

Aldar Properties - Operational performance to offset bleak sector outlook

- **Initiate with 'Buy' rating; valuation upside of 18% at our TP of AED 3.14/s**
- **Yas Mall to further enhance recurring revenue stream**
- **More projects in the pipeline Project launches to accelerate to leverage the company's existing land bank**
- **Strong balance sheet to reduce the susceptibility to economic downturn**

Recurring revenues to get a boost from Yas Mall: Aldar's recurring revenue grew at a CAGR of 26% during 2010-14 to AED 2.2 billion, and contributed 34% to the company's top line. The group launched its key flagship asset, Yas Mall in November 2014, which is already 100% leased. Currently, 340 out of the total 370 trading units are operational. We expect the recurring revenue stream to increase by 30% YoY in 2015 to AED 2.9 billion due to contribution from Yas Mall.

Aggressive project launches to leverage the existing land bank: Aldar owns a huge land bank of over 77 million square meters, of which 90% of the land are in special investment zones and are open to investments by foreign nationals. The company has announced its plan to launch 7,300 residential units in the next five years and has already sold 1,103 units by end of 2Q 2015. In addition, Aldar has implemented IFRS from 1H 2015 and the revenue recognition from property sales will be smoothened over the construction period against the earlier lumpy top line contribution.

Robust balance sheet: Aldar's net debt declined from AED 26 billion in 2010 to AED 4.5 billion by end of 2014. Also, the company successfully refinanced the earlier debt facilities and cost of debt declined from 5.9% in 2013 to 2.7% in 2014. Aldar enjoyed a healthy cash reserve of AED 5.2 billion by end of 2Q 2015. This renders the company in a comfortable financial position to take up new projects and sustain any adverse economic scenario.

Attractive valuation; our TP offers an upside of 18%: We value the equity using SOTP method, with the recurring businesses contributing c. 65% of the total enterprise value. The existing project pipeline, along with the expected future launches to monetise the land bank, also contributes c. 23.6% of the company's EV. Our TP of AED 3.14/sh also includes the present value of receivables from Government of Abu Dhabi and other investments. Downside risks include further cut in the government's spending in the event of sustained low oil prices, poor response to the company's future project launches and further decline in hotel occupancy rates.

Summary Table - Key Forecasts and Ratios

AED Million	2012	2013	2014	2015F	2016F	2017F
Turnover	11,404	5,380	6,551	4,913	5,292	5,857
EBITDA	3,028	1,502	1,252	1,861	2,013	2,193
Net Profit	1,341	2,225	2,266	2,194	2,380	2,619
EPS (AED per share)	0.30	0.34	0.29	0.28	0.30	0.33
DPS (AED per share)	0.04	0.03	0.07	0.07	0.07	0.07
P/BV (x)	0.7x	1.1x	1.1x	1.0x	1.0x	0.9x
P/E (x)	4.2x	8.2x	9.2x	9.6x	8.8x	8.0x

Investment Rationale

Our valuation model predicts an upside of 18% from the current share price. We believe that the negatives related to oil price decline and spending cut by the government are already priced in the current share price

Expect upside of 18%; negatives already priced in

Our sum of the parts valuation model suggests an upside of 18% from the last traded price and leads to our 'Buy' recommendation. The company's recurring business contributes 65% of the enterprise value. The stock has already declined by 27% in the past one year as a result of low oil prices and spending cut by the government of Abu Dhabi. We believe that the negatives are already factored in the share price. In addition, the reinvigorating growth in the project pipeline, successful launch of Yas Mall and early implementation of IFRS are expected to drive the earnings upgrade going forward, and the stock price.

SOTP Valuation Summary

	AED million	% Contribution in EV
Existing Development projects	1,056	4.0%
Operating Businesses	17,364	65.5%
Future projects leveraging land bank	5,212	19.7%
Associates and JVs	749	2.8%
Receivables from Government of Abu Dhabi	2,137	8.1%
EV	**26,518**	**100.0%**
- Net Debt at 2Q 2015	(7,098)	
+ cash @ 2Q15	5,250	
Target Equity Valuation	**24,670**	
Target Price	3.14	
Current Share price	**2.67**	
Upside potential	**17.5%**	

Source: Company Data, RocSearch

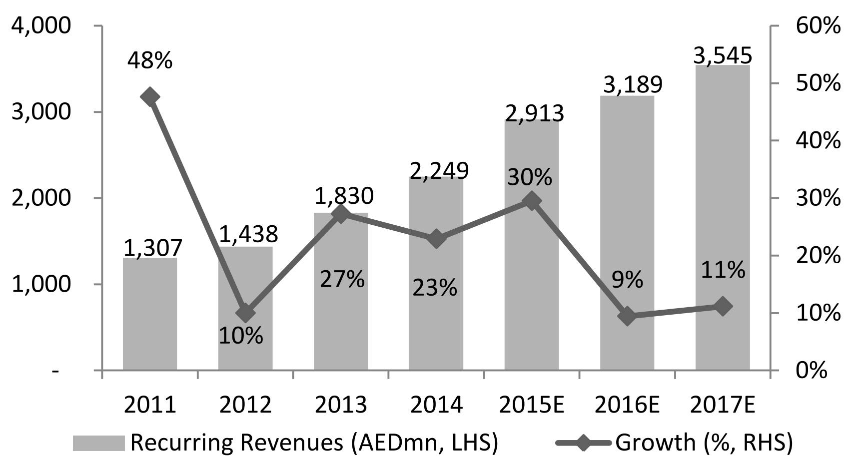
Recurring businesses provide a more stable and predictable source of income as compared to the property development and sales segment

Recurring revenue stream remains strong

Aldar generated AED 2.2 billion revenue from its recurring businesses, which include investment properties (IP) portfolio, operative villages, schools, leisure and hotels. The income from its recurring segments leads to stable and relatively more predictable top line performance compared to the its property development and sales segment, which is dependent on project completion and delivery. The recurring business registered a CAGR of 26% between 2010-14 period and constituted 34% of the total company revenue in 2014. We expect the strong growth in recurring business to continue on back of opening of Yas Mall in November 2014 and increase in leasing of commercial office space. Therefore, we project a CAGR of 16% for the 2014-17 periods and expect the revenue contribution to increase to 58% by 2017. Based on our valuation model, these recurring businesses contribute c. 65% of the total enterprise value.

The recurring business as an aggregate, recorded a higher gross profit margin of 45% in 2014, than that of the property development and sales segment at 12%. We believe that these businesses are less susceptible to economic downturns compared to the construction or property development and sales businesses. We expect steady future cash flows, since these businesses do not require significant investments going forward.

Financial Performance of Recurring Businesses



Source: Company Data, RocSearch

Yas Mall to drive leasing income

Yas Mall is one of the company's key retail assets, with net leasable area of 235k square meters. The asset is already fully leased and 340 out of total 370 trading units are operational. Its operations are expected to stabilise in another 12-18 months

Yas Mall, the second largest mall in Abu Dhabi, is located on Yas Island, a popular tourist destination in Abu Dhabi. The mall is situated near the Formula 1 race track and has a direct link to the Ferrari world amusement park. The mall has a net leasable area of 235k square metre and is second only to the Dubai Mall, which is spread over 1,124k square metres. It has been operational since November 2014 and is currently fully leased out. By the end of June 2015, approximately 340 stores were functional, out of total 370 units. The rest are expected to be fully operational by the end of 2015. The company expects the Yas Mall operations to fully stabilise by 2017. The lease rentals will also be adjusted upwards, once footfall in the mall increases. As per JLL, the average lease rentals on Abu Dhabi islands are about AED 3,000 per square metre annually. Once fully operational, Yas mall has the potential to contribute c. 9% to the Aldar's top line at the lease rental of 3,000 per square metre. As per our analysis, 5% increase in the lease rentals will lead to 1% increase in the group's overall revenue.

Aggressive project launches to leverage existing land bank

Aldar has a healthy line up of new projects, with majority of them coming up in the property development and sales segment. We expect the segment to get a boost from the aggressive project launches

The Aldar group has a substantial land bank of 77 million square metres in UAE, of which about 90% are in special investment zones and are open to non-UAE residents for investments. The existing land bank at a rate of AED 400 per square meters implies a value of AED 31 billion. Aldar has announced its plan to launch 7,300 units across its existing locations by 2020 and will be using its existing land bank. During 2014, the group launched two projects (Ansam and Hadeel) in prime areas of Abu Dhabi. It also announced three residential projects (Nareel, Meera and Merief) in 2015 YTD. The company also announced the construction of a new mall – Al Falah Mall – and the expansion of Al Jimi Mall. We believe that Aldar has a competitive edge in terms of land bank and the strong project pipeline will enhance the revenue from property sales and development segment. These projects will be sufficient for strong top line performance by the company till 2021.

Recent Projects Launched

Recent Projects Launched				
Project	Launch	Units Sold	Revenue	Expected
Property Development & sales				
Ansam	2014	472	4%	2017
Hadeel	2014	211	7%	2017
Nareel	2015	30	49%	2017
Land plot	2015	1	100%	2015
Merief	2015	274	0%	2017
Meera	2015	115	0%	2018
Land plot	NA	NA	0%	2016
Investment Properties				
Al Falah Mall	2015		NA	NA
Al Jimi Mall - Expansion	2015		NA	NA

Source: Company Data, RocSearch

IFRS implementation to smoothen revenue from property development and sales segment

Adoption of new guidelines to smoothen the revenue recognition from property development and sales

Aldar's existing project pipeline for property development and sales was drying up towards the end of 2014, and the revenue potential from the segment was also receding. Although the company has come up with a strong project pipeline these projects are expected to start the delivery of the residential units only by late 2016 or 2017.

Earlier, Aldar followed an accounting standard under which the company would have recognised revenue from property development and sales primarily post the completion of a project. Therefore, the revenue outlook for 2015 and 2016 was muted.

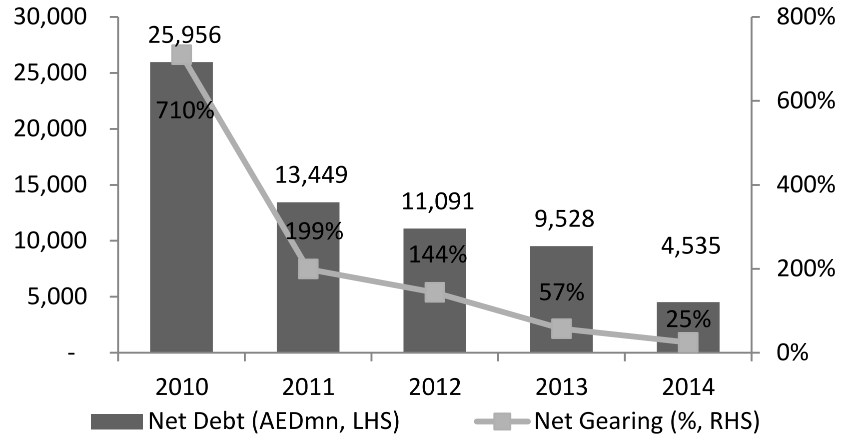
However, in July 2015, the company announced early adoption of IFRS 15, which will be applicable to its financial statements w.e.f. January 2015. Under IFRS 15, Aldar will recognise revenues when it receives payments for completion of a certain percentage of work as specified in the contract. This would result in smoothened revenue recognition. We estimate property development and sales segment revenue of AED 1.5 billion and AED 1.6 billion in 2015 and 2016 respectively.

Robust balance sheet

The group's debt levels have declined significantly over the past five years, aided by the company's re-financing efforts

The company's net gearing reduced significantly from 710% in 2010 to 25% in 2014 and its net debt reduced from AED 25.9 billion in 2010 to AED 4.5 billion in 2014. The group re-financed its existing bank loans worth AED 1.6 billion in the year 2014, which helped reduce the company's weighted interest cost to 2.7% in 2014 from 5.9% in 2013. As a result, the finance cost fell by a sharp 47% during the year. The reduction in debt also helped to improve the group's gearing to 25% in 2014 from 57% in 2013. Moreover, Aldar had a healthy cash balance of AED 4.7 billion in 2014. We believe that the company is less vulnerable to any economic downturn due to its strong cash position and low gearing.

Net Debt and Gearing



Source: Company Data, RocSearch

Abu Dhabi Government remains a key customer

Aldar benefits from its close association with the government of Abu Dhabi in the form of contracts, lower interest loans and subsidised land plots

The government of Abu Dhabi has an indirect shareholding of c. 38% in the Aldar group via Mubadala Development Co, Abu Dhabi investment co, National Bank of Abu Dhabi and others. The government is also one of the group's biggest clients and contributed overall revenues (including other income) of approximately AED 20.7 billion in the past five years, which implies an average contribution of 55% to the company's top line. Although the revenue from the Abu Dhabi Government was relatively modest in 2013 and 2014 at AED 2.7 billion and AED 2.3 billion respectively, it still contributed 45% and 31% of the total revenue. The company receives government grants in the form of government loans at below market rate of interest. The group has also been granted land by the government at prices lower than the market value. We believe that Aldar's strong relationship with the government augurs well for the company's long-term financial performance.

Government receivables of AED 2.3 billion to be paid by 2017

Receivables from the government for previously sold assets to provide steady cash inflow over the next two years

The group had AED 1.9 billion receivables from the government of Abu Dhabi by the end of Q2 2015, which represented 28% of total receivables. It included the amount to be received against the sale of Ferrari world theme park and central market for a sum of AED 6.5 billion in 2011 and Yas Island assets for AED 9.2 billion to the government in 2009. It also included the cost incurred on behalf of the government for the development of infrastructure in the country, which will be refunded by the government. As per the receivable payment schedule in the latest investor presentation, the receivables of AED 2.3 billion will be repaid by 2017, with scheduled payments of AED 1.6 billion in 2016. We expect timely payments from Abu Dhabi Government and these payments will remain a key source of steady cash flow for the group in the next 2-3 years.

Receivables Payment Schedule

Date of transaction	Deals with the government of Abu Dhabi	H2 2015	2016	2017
December, 2009	Sale of F1 Race Track	348	348	348
January, 2011	Sale of Al Raha Beach Land and Yas Island Assets	-	908	-
January, 2013	Shams Infrastructure Reimbursement & Sale of Gate units	-	300	-
Total		**348**	**1,556**	**348**

Source: Company Data, RocSearch

Aldar is already in compliance with the new regulatory framework and will be positively impacted in the long run as investor interest increases with more credible offerings

New real estate law governing off-plan sales

The Abu Dhabi Government has recently issued a new law regulating the real estate sector in the Emirates of Abu Dhabi. The law requires preparation of a real estate register to document all real estate transactions. Also, all off-plan units' transactions will be recorded to avoid issues, such as failure of contract execution or project completion. Moreover, for unfinished projects payments will be held in third party escrow accounts. We believe that the new law will be applicable to Aldar's businesses as it is involved in off-plan sales. The company management has iterated that they are already in compliance with the requirements. Also, the new law would create a secure buyer environment and be more conducive for the company as off-plan sales get more traction among the buyers.

Investment Risks

Tepid real estate growth due to macroeconomic downturn

Decline in crude oil prices can impact the macroeconomic climate in UAE; thereby, hampering the demand and government spending in the real estate sector

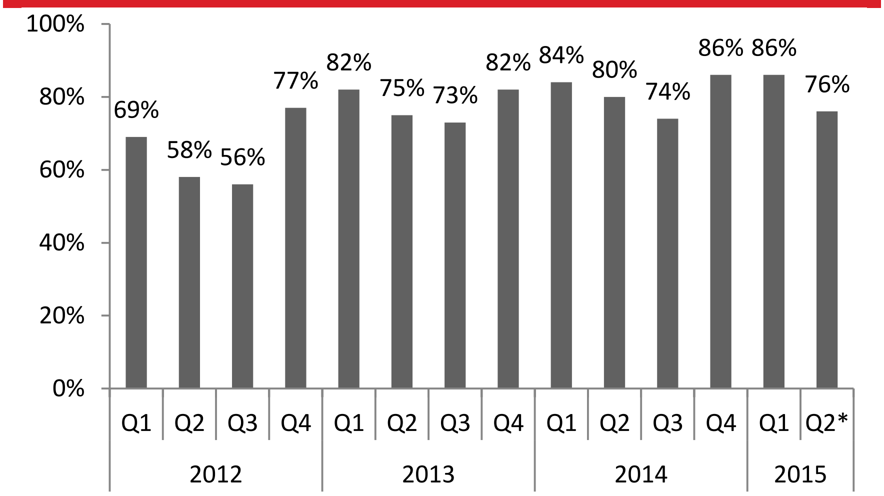
As per JLL's Q2 2015 report, the overall demand in Abu Dhabi real estate has slowed down. The reduced demand can be attributed to steep decline in crude oil prices, which has in turn led to cut down in the government's spending on infrastructure projects. The budget allocated for the infrastructure sector for the year 2015 declined by a steep 71.4% YoY to AED 1.8 billion from AED 6.3 billion in 2014. However, the slack in real estate supply in the short term is expected to keep the sector stable. The budgetary allocation by the government of Abu Dhabi towards the infrastructure sector would play a key role in determining the demand growth of the sector in the long term. If crude prices remain low or slide further, it can impede the demand in the real estate sector in UAE. The chances of reduced spending by government remains a downside risk to our earnings and valuation estimates. In addition, the government of Abu Dhabi is a major client of Aldar, and the impact of reduced government spending will be higher for the company than its peers.

Occupancy rates to moderate in hotel portfolio

Macroeconomic downturn can severely impact the occupancy rates as well as room rentals of the hotel segment

Aldar group has nine hotels with 2,536 rooms, with seven hotels on Yas Island. Despite being located on a popular tourist destination, the occupancy rate declined to 76% in Q2 2015 from 80% in Q2 2014. In addition, the segment is highly susceptible to macro-economic downturn and hotel occupancy and room rentals have moderated recently. We expect that the opening of Yas Mall and continued government initiatives, like expansion of international airport, hosting of world-class events and major campaigns to draw tourist to Abu Dhabi will offset the present weakness in the hotel segment. However, the recent decline in occupancy rates remains a risk to our earnings and valuation estimates.

Aldar's Cumulative Hotel Occupancy



* Calculated from Q1 2015 and H1 2015 data
Source: Company Data, RocSearch

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Aldar: SOTP Valuation

We have valued Aldar stock using SOTP as the company has different business models across segments. Our valuation model includes PV of EBITDA from recurring businesses, already launched property development projects and estimated value of land bank using future project announcements. We have also factored in the contribution from receivables from the government of Abu Dhabi, which will be received by 2017 and Aldar's investment in associates and joint ventures.

Valuation Snapshot

	AED million	Comment
Existing development projects	1,056	PV of cash flows from already launched projects
Operating businesses	17,364	PV of cash flows
Future projects leveraging land bank	5,212	PV of cash flows from 6,200 units
Associates and JVs	749	Valued at 80% of book value @2Q 2015
Receivables from Government of Abu Dhabi	2,137	PV of future cash flows
EV	**26,518**	
- Debt @ 2Q15	(7,098)	
+ cash @ 2Q15	5,250	
Target equity valuation	**24,670**	
Target price	3.14	
Current share price	**2.67**	
Upside potential	17.5%	

Source: RocSearch

We have used the WACC to discount the future cash flows, which is calculated using cost of equity (14.3%) and cost of debt (2.8%) with appropriate weights.

WACC Calculation

US treasury yield	3.3%
Global equity risk premium	4.6%
Country premium	1.5%
Beta	1.80
Cost of equity	14.3%
Cost of debt	2.8%
WACC	**11.4%**

Source: Bloomberg, RocSearch