Research Update:

Abu Dhabi Ports Co. PJSC Assigned 'A+' Rating; Outlook Stable

April 22, 2021

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Rating Action Overview

- Abu Dhabi Ports Co. PJSC (AD Ports) owns and manages all non-oil ports of Abu Dhabi and is 100% owned by the government via Abu Dhabi Development Holding Co. (ADQ), itself a 100% Abu Dhabi government-owned company.
- AD Ports' good competitive position is driven by very high revenue predictability, good operating efficiency, and modern infrastructure are offset by the company's limited market share in a very competitive region with high port density, high and rising expansionary capital expenditure (capex) fueling an increase in debt, and expected EBITDA volatility over the next two years.
- We have assigned our 'A+' long-term issuer credit rating and 'gcAAA' Gulf Cooperation Council (GCC) regional scale rating to AD Ports.
- The stable outlook reflects our expectation that the company's performance will remain strong, despite high and rising expansionary capex over the coming two years, resulting in negative free operating cash flow (FOCF) and rising debt levels, with S&P Global Ratings-adjusted funds from operations (FFO) to adjusted debt at 21%-26% and adjusted debt to EBITDA of 3.5-4.0x, in line with our 'A+' rating.

Rating Action Rationale

AD Ports enjoys a good competitive position in the GCC region, driven by very high revenue predictability due to contractual revenue from concessions and joint ventures (JVs) with world-leading shipping companies, good operating efficiency, and modern infrastructure. These are somewhat offset, however, by AD Ports' limited market share in a very competitive region with high port density, its high and rising capex that we expect will result in an increase in debt, and EBITDA volatility over the next two years.

We view AD Ports as a government-related entity (GRE), given its indirect state ownership via ADQ and its management of ports that we view as strategically important for Abu Dhabi's economy. In accordance with our criteria for GREs, our view of the very high likelihood of timely and sufficient extraordinary government support for AD Ports in the event of financial distress, if needed, is based on our assessment of AD Port's:

- Very important role for the government due to its systemic importance to non-oil trade (AD Ports handled 56% of all imports, 72% of all non-oil exports, and 40% of the food and beverage (F&B) trade of the Emirate of Abu Dhabi as per 2017 data). It is a key enabler of the government's diversification strategy, as set out in Abu Dhabi Economic Vision 2030, since it owns all the emirate's non-oil ports. Transportation, trade, and logistics have been identified as a key priority sector of Vision 2030. AD Ports has contributed 13.6% to Abu Dhabi's non-oil GDP, as well as 7.4% to the UAE's non-oil GDP in 2020 through approximately 212,000 jobs--either at AD Ports, or ancillary companies working with AD Ports--in the country.
- Very strong link with the government on the back of 100% government ownership via ADQ, long track record of extensive support and close control via a government-appointed board, despite financial independence. We do not currently expect any changes to AD Ports' shareholding structure.

Government support results in a four-notch uplift to the rating. ADQ has injected equity of AED700 million as of March 31, 2021 to support the company's capital structure. We expect further substantial equity injections in 2021 to the extent required to support AD Ports' growth and capital structure in line with the issuer credit rating. In addition, in 2020 the government transferred ownership of ZonesCorp (an Abu Dhabi government-owned industrial free zone based in the emirate) to AD Ports. Now, AD Ports' industrial and economic zones offering has a combined land area of 555 square kilometers (km) and more than 1,500 customers. As such, this cost-free transaction significantly enhances its scale. These government transactions support our view of a very high likelihood of timely and sufficient extraordinary government support for AD Ports in the event of financial distress.

On average, nearly 60% of AD Ports' future revenue is contractual in nature, such as long-term leases and service contracts with guaranteed base volumes, which is a supportive factor that led to revenue growth amid the pandemic. AD Ports manages all non-oil ports of the Emirate of Abu Dhabi and operates under a landlord model, which provides for relatively predictable revenue and cash flow generation compared with port operators. It focuses on origin and destination (O&D) services, which we view as less competitive and less prone to volume risks than the transshipment business. The company handles 56% of all imports, 72% of all non-oil exports, and 40% of F&B trade of the emirate as per 2017 data. The region's other means of transportation, notably rail, are not as developed as the ports. The company doesn't handle any crude oil-related exports, which comprise the bulk of Abu Dhabi's trade volumes.

The two key assets, Khalifa Port and Khalifa Industrial Zone Abu Dhabi (KIZAD), are highly symbiotic. Khalifa Port is the emirate's flagship deep water port, providing state-of-the-art facilities and maritime infrastructure. It is the first semi-automated port in the GCC and has very advanced technology. It is positioned as a gateway port to serve the growing local Abu Dhabi economy and its hinterland. KIZAD serves as a complementary industrial zone in close proximity to Khalifa Port. It offers free-zone and industrial-zone solutions for land leasing, pre-built warehouses, and free-zone offices. The relationship between Khalifa Port and KIZAD is synergetic through increased volumes for the port and transport efficiency for KIZAD tenants. The port allows KIZAD tenants to efficiently import production inputs and directly export final products and intermediates. The free zone has a wide portfolio of investment sectors including aluminum, automotive, engineered metals, port logistics, food processing, and other industries that rely on Khalifa Port.

The company has established key partnerships with leading shipping companies based on long-term concessions, providing stability to revenue in scope for exponentially growing volumes at Khalifa Port. In 2018, the company signed a JV with Terminal Investment Ltd. (the container arm of Mediterranean Shipping Company, MSC), which more than doubled Abu Dhabi Terminal's (ADT, existing terminal at Khalifa Port) to 5.3 million twenty-foot equivalent units (TEU) from 2.5 million TEU in 2020. The JV has a 30-year concession agreement with volume commitments. The JV with COSCO Shipping Ports will operate under a 35-year concession. It is the second container terminal at Khalifa Port and the largest freight station in the Middle East (the JV is 90% owned by COSCO). The JV with Autoterminal Barcelona (51% ownership by AD Ports and consolidated) will create a roll-on/roll-off (RoRo) terminal in the region under a 15-year concession, leveraging on Autoterminal Barcelona's experience. The JV will manage the RoRo at Khalifa Port and progressively expand the existing car terminal.

Despite the pandemic, we expect partnerships with market leaders and high contractual revenue to support volume growth in 2020-2021. AD Ports experienced minimal impact from the COVID-19 pandemic because the ports stayed open for business during the lockdown months and trade was affected less than services were. Aside from cruise and car transshipment, all other cargo segments experienced volume growth. AD Ports has JVs with market leaders that are highly supportive of revenue growth: ADT; COSCO Shipping ports; Auto-terminal Khalifa port; and OFCO with Allianz Marine. Volume growth increased by nearly 16% and 33% in TEU containers and general cargo, respectively, from 2019 levels. In addition, O&D volumetric revenue from Abu Dhabi's GREs or cargo with Abu Dhabi custom waivers, which are less prone to competition, account for approximately 35% of group revenue. Abu Dhabi and its GREs are a captive market for AD Ports, as most imports for construction, the F&B industry, ADNOC (non-oil) supply chain elements, petrochemicals facilities, and aluminum go through AD Ports. About 60% of the company's revenue is contractual, i.e., long-term leases or guaranteed volumes.

AD Ports -- Key Operating Metrics

	2019	2020
Containers TEU (mil.)	2.8	3.2
General cargo - freight tons (mil.)	22.5	30.0
Cruise passengers (000)	493.0	254.0
RORO - units (000)	150.0	132.0
Land leased (square kilometers)	3.1	3.1
Utilities natural gas sales (mil. MMBTU)	16.5	14.7
Logistics Borouge volumes (mil. MTs)	3.4	4.0
Digital messages (000)	13.3	16.6

MMBTU--Million British thermal units. MT--Metric tons. N.A.--Not available. RoRo--Roll-on, roll-off terminal. TEU--Twenty-foot equivalent units.

Offsetting these strengths is the company's planned capex of AED8.7 billion over the next two years, of which AED3.2 billion will be spent on behalf of the government. AD Ports has been tasked to execute critical government capex to ensure the nation's food and medical security in the wake of COVID-19. Most of the company's growth capex will be directed to increasing capacity at KIZAD and Khalifa Port around the container terminal, South Quay, and Khalifa Logistics Port, for example, to accommodate the additional volumes expected under the various deals. Although there is execution risk in the capex plan, there is a successful track record of executing similar infrastructure investments.

Khalifa Port and other of the company's ports are located in a region with one of the highest density of ports in the world, which limits the company's market share and growth opportunities. A key competitor is the Jebel Ali Port in Dubai (22.4 million TEU capacity), which is attached to a more established free zone and located within close proximity of the Al Maktoum international airport. However, the two ports have different business models, with Jebel Ali focusing more on container traffic and transshipment. AD Ports today generates less than 10% of revenue from container operations. Additionally, KIZAD and ZonesCorp focus on industrial scale operators like Emirates Global Aluminium and Emirates Steel, with very large space requirements that cannot easily be accommodated by competing free zones.

Our view of AD Port's financial risk profile reflects a strong capital structure and cash flow generation, despite significant planned capex. We believe AD Ports will maintain S&P Global Ratings-adjusted FFO to debt of 21%-26% over the next two years. Adjusted debt to EBITDA is the main constraint to rating upside, expected to be 3.5x–4.0x in 2021-2022. In addition to heavy capex of AED8.7 billion over two years, this will lead to negative FOCF. The company's EBITDA margin is weaker than a typical landlord port's, such as QPH Finance Co. Pty. Ltd. in Australia (80% EBITDA margins), since AD Ports has various business lines other than concessions. Ultimately, terminal operations, marine services, and ancillary businesses carry much lower margins that dilute the strength of the concessions.

We assess AD Ports' environmental, social, and governance risks as neutral to its credit quality. We do not envisage any carbon tax or environmental fines that could affect AD Ports' earnings quality because the company's ports are indirectly exposed to emissions from vessels using the ports. We consider social and environmental risks are unlikely to be primary drivers of AD Ports' credit quality. We believe AD Ports has a fair governance framework, reflecting the company's management experience and expertise in managing its ports and a strategy broadly in line with market trends.

Outlook

The stable outlook reflects our expectation that the company's performance will remain strong, despite high expansionary capex over the coming two years. This will result in negative FOCF and rising debt, with FFO to adjusted debt at 21%-26% and adjusted debt to EBITDA at 3.5x-4.0x, which is consistent with the rating. We anticipate the EBITDA margin will weaken to around 44%-46% over the next 24 months, due to higher operational costs associated with infrastructure ramp-up.

Downside scenario

We might lower the rating if AD Ports fails to maintain FFO to debt above 13% or debt to EBITDA below 4x. This could result from delays in future revenue and volume growth versus our expectation, increased operating costs, cost overruns under the capex plan, higher competition, or unfavorable economic conditions or geopolitical risks significantly reducing trade volumes to the region. This could also stem from delays in equity injections or government receivables from shareholders and related parties.

Upside scenario

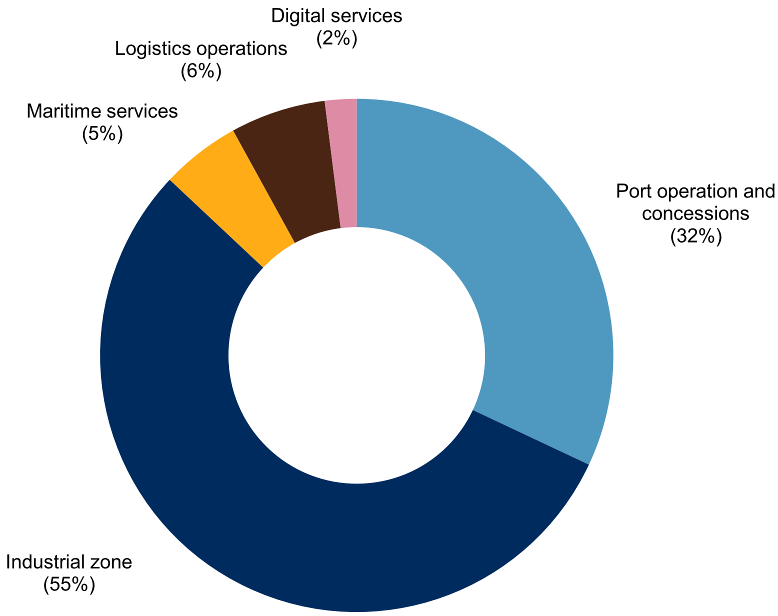
We view the potential for ratings upside over the next 24 months as limited because an upgrade would require one-notch improvements in both the stand-alone credit profile (SACP) and the sovereign credit rating, which is not our base case. Given that FFO to debt is strong, AD Port's SACP would strengthen on the back of adjusted debt to EBITDA of less than 3x on a sustainable basis, which is unlikely because of high investment requirements.

Company Description

AD Ports owns, manages, and operates 11 ports (commercial, logistics, community, and leisure) and terminals. AD Ports is 100% owned by the government of Abu Dhabi via ADQ. ADQ was established by law in 2018, with its existing status as a 100% government-owned entity and with the main objective of consolidating some of Abu Dhabi's leading GREs. The company has direct and indirect investments in more than 90 entities across a number of sectors, many of which provide essential services to Abu Dhabi and its citizens. ADQ has four economic clusters: Energy and utilities, food and agriculture, healthcare and pharmaceuticals, and mobility and logistics.

AD Ports operates a fully integrated business model. The company owns nine of the 11 ports in Abu Dhabi; it jointly (with global partners) operates the terminals at Khalifa Port; it owns adjacent industrial and free zones; and provides marine services, maritime training, cruise infrastructure, and digital solutions for ports (vessel management, payment solutions, etc. that help automate the processing of vessels and cargoes at the port). The company also operates Fujairah Terminals within the emirate of Fujairah on a 35-year concession agreement with Fujairah Port, and Kamsar Port in Guinea, West Africa, on behalf of Emirates Global Aluminium.

AD Ports EBITDA Breakdown
2020



Source: Company reports.

Our Base-Case Scenario

- GDP growth for Abu Dhabi of 2.0% and 3.5% in 2021-2022.
- We believe AD Ports' performance has been resilient and should track economic trends. Except for cruise and car transshipment, we expect a full recovery in volumes for both containers and bulk cargo, aligned with that of global trade.
- We think tariff increases could be curbed amid pressure on businesses and therefore landlord ports with property portfolios in the precinct will be less affected by the pandemic, as seen in 2020.
- Revenue growth of 3%-5% in 2021-2022 linked to new infrastructure deliveries, transferred ownership of ZonesCorp, growth in the industrial zones, and expected volume growth from the JV deals.
- --Port, Logistics and Maritime services: future revenue increase led by the continued ramp up of the Khalifa Port terminals (including COSCO and ADT), commissioning of Safeen Feeders in June 2020, and OFCO vessel chartering JV and ESI transshipment contract from 2021.
- --Industrial zone: Occupancy ramp up in KIZAD and ZonesCorp, with both benefitting from their long-term leasing contracts. Both free zones also have ample space for future capacity expansion.

- --Additional multi-growth platforms: Utilities business, Digital.
- EBITDA margins of 44%-46% in 2021-2022 due to an increase in operational costs, as volumes are expected to grow.
- Heavy capex of AED8.7 billion ($2.4 billion) over two years, including AED3.2 billion ($870 million) of capex on behalf of the government, the cost of which will be reimbursed to AD Ports.
- Equity injection of AED700 million has been received as of March 31, 2021, with further substantial equity injections expected in 2021 to support AD Ports' capital structure and growth in line with the issuer credit rating.
- Settlement of AED700 million in 2021-2022 of short-term loan to shareholders and related parties.
- No dividend payments, in line with management's intention to reinvest cash flows in the business.

Key metrics

Based on these assumptions, we arrive at the following S&P Global Ratings-adjusted credit measures for AD Ports over the next two years:

- Adjusted FFO to debt of 21%-26%.
- Adjusted debt to EBITDA of 3.5x–4.0x.

Liquidity

We expect AD Ports to maintain adequate liquidity. We estimate the company's liquidity sources to exceed uses by at least 1.2x over the next 12 months, and net sources to remain positive even if EBITDA declines by 15%. We believe AD Ports has sound relationships with local banks and prudent risk management. However, the company does not yet have a track record in the public capital markets.

Principal liquidity sources

- Unrestricted cash balance of AED271 million as of Dec. 31, 2020;
- Undrawn committed revolving credit facility of $1 billion signed in April, with a maturity of three years;
- Our estimate of cash flow from operations of AED1.1 billion–AED1.3 billion;
- Equity injection of AED700 million had been received as of March 31, 2021; and
- Access to AED700 million loan to shareholders and related parties, receivable on demand by AD Ports.

Principal liquidity uses

- Short-term debt maturities of AED4.1 billion of which we expect $1.0 billion (AED3.68 billion) to be refinanced;

- Working capital outflow of about AED100 million;
- Capex of AED4.5 billion, of which only half is considered as committed capex (AED2.0 billion of capex is on behalf of the government, the cost of which will be reimbursed to AD Ports); and
- No dividend payments, in line with management's intention to reinvest cash flows in the business.

Covenants

AD Ports' debt is not subject to any covenants.

Ratings Score Snapshot

Issuer Credit Rating: A+/Stable/--

Business risk: Satisfactory

- Country risk: Intermediate
- Industry risk: Low
- Competitive position: Satisfactory

Financial risk: Intermediate

- Cash flow/Leverage: Intermediate

Anchor: bbb

Modifiers:

- Diversification/Portfolio effect: Neutral (no impact)
- Capital structure: Neutral (no impact)
- Liquidity: Adequate (no impact)
- Financial policy: Neutral (no impact)
- Management and governance: Satisfactory (no impact)
- Comparable rating analysis: Neutral (no impact)

Stand-alone credit profile: bbb

- Sovereign rating: AA/Stable/A-1+
- Likelihood of government support: Very high (+4 notches)

Related Criteria

- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Corporates | General: Corporate Methodology: Ratios And Adjustments, April 1, 2019
- General Criteria: Methodology For National And Regional Scale Credit Ratings, June 25, 2018

- Criteria | Corporates | General: Reflecting Subordination Risk In Corporate Issue Ratings, March 28, 2018
- Criteria | Corporates | Recovery: Methodology: Jurisdiction Ranking Assessments, Jan. 20, 2016
- General Criteria: Rating Government-Related Entities: Methodology And Assumptions, March 25, 2015
- Criteria | Corporates | General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- Criteria | Corporates | General: Corporate Methodology, Nov. 19, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities, Nov. 13, 2012
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- Emirate of Abu Dhabi, Nov. 27, 2020.

Ratings List

New Rating	
Abu Dhabi Ports Co. PJSC	
Issuer Credit Rating	A+/Stable/--
Gulf Cooperation Council Regional Scale	gcAAA/--/--